



LISBON  
SCHOOL OF  
ECONOMICS &  
MANAGEMENT  
UNIVERSIDADE DE LISBOA

**MASTER**

INTERNATIONAL ECONOMICS AND EUROPEAN STUDIES

**MASTER'S FINAL WORK**

DISSERTATION

DO CHINESE SOES OPERATE ON A LEVEL PLAYING FIELD IN THE  
GLOBAL MARKET?

RUIYING WU

OCTOBER - 2019



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## **ABSTRACT**

Nowadays, state-owned enterprises are playing a considerable role in the global economic development. The spectacular growth of Chinese SOEs in the last two decades has specially shocked the whole world. However, there are also concerns for the global market due to their murky background. It is always suspected that they are not operating on a level playing field because they might receive some preferential treatment from the government. The purpose of this paper is to study whether Chinese SOEs are operating on a level playing field in the global market. Based on previous studies about Chinese SOEs and the case study about dispute cases involving Chinese SOE at the World Trade Organization since 2002 until now, we conclude that Chinese SOEs may not be operating on a level playing field all the time, even if the dispute cases analysed are not always conclusive. Only when there is more sunshine over Chinese SOEs could we see better if there is any real threats from Chinese SOE sector to the fair competition in the global market.

**Keywords:** State-owned enterprises, Chinese state-owned enterprises, World Trade Organization, transparency

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## **1. Introduction**

State ownership still remains significant in some middle- and low-income countries in spite of the high-speed development of privatization over the past two decades. State-owned enterprises (SOEs) are playing a considerable role in many countries, especially in some emerging countries. It cannot be denied that SOEs can contribute to correct the market failure in some essential industries in the domestic market, such as utilities and infrastructure, which can make an influence on citizen's daily life. However, due to their special public ownership, they might receive some preferential treatment from the government. Their exclusive privileges in some sectors could undermine the fair competition with other private enterprises and foreign enterprises in the domestic market.

With the continuing deepening of the links of international business, the performance of the SOEs could also be of great importance to the global market. Notably, Chinese SOEs have been contributing to the rapid growth and the huge influence of China's economy for the past two decades, which has raised concerns in other countries. It is concerning that Chinese SOEs could undermine the fair competition environment, as they might receive massive unfair advantages from the government. Such suspected competition distortive behaviours of Chinese SOEs are no longer only affecting the domestic markets, but have expanded to international trade. In recent years, disputes involving Chinese SOEs have increased friction between China and some of its important trading partners, such as U.S. and the EU.

This paper tries to discuss whether Chinese SOEs have been operating on a level playing field by using case study as its main methodology. The cases will be chosen from the disputes involving Chinese SOEs at the World Trade Organization (WTO). The WTO, as one of the most important pillars in maintaining the world economic order and also the only

global international organization dealing with the rules of trades among members, can be considered as an authority on global economic order. By studying the conclusions given by the WTO, it is visible that Chinese SOEs are probably undermining fair competition in the global market.

Due to the special characteristics of Chinese SOEs in the global market economy, there has been research done by Zhou (2000), Li (2014), ect, about the problems that they might bring. In China's domestic market, in spite of the contribution that SOEs have made to the economic development, the inefficiency problem also caused economic losses. Besides, with the preferential treatment provided by the government, Chinese SOEs enjoyed some exclusive privileges, which can skew the playing field against exported and imported goods and services, leading to unfair competition in the global market. Moreover, the state ownership can also be a concern in the international market as it may be driven by the state leadership and guidelines. This paper studies the topic of whether Chinese SOEs are competing fairly with other companies in the global market. Besides, we analyse whether the disputes about Chinese SOEs result from the lack of transparency in China's market and SOE sector. We conclude that Chinese SOEs have not operated on a level playing field in all dispute cases analysed and it is crucial to improve the transparency mechanism, as a way to know more about Chinese SOEs and potentially establish a healthy trading relationship based on trust among trading partners.

The study about whether Chinese SOEs operate on a level playing field is divided in three sections. Firstly, there is an introduction about the distinctive features of Chinese SOEs and if they can be considered as a problem both for themselves and for the global market. Secondly, we use the methodology of case study to analyze the dispute cases involving Chinese SOEs at the WTO, in order to understand the position of the WTO on whether Chinese SOEs operate on a level playing field. In the end, there are some suggestions for

improvement in transparency both in China and at the WTO, in order to improve the problems of Chinese SOEs in the global market.

## **2. Are Chinese SOEs A Problem?**

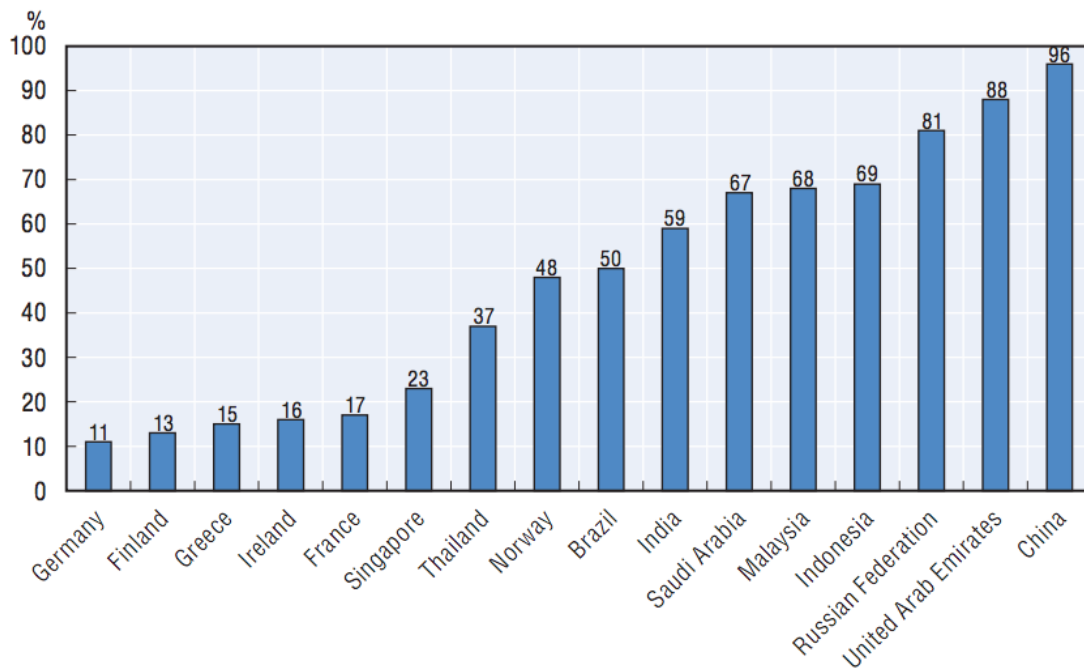
Chinese SOEs have been very controversial in the global market. This section will study the characteristics of Chinese SOEs and if they are a real problem, both for themselves and for the global market.

### **2.1 Chinese SOEs: distinctive features**

China has been experiencing the most remarkable social and economic growth and development in the world since its market reform in 1978. According to the World Bank, China is the world's second largest economy, and has also been the largest single contributor to world growth since the global financial crisis of 2008. Although much of this rapid growth is driven by the non-state-owned enterprises, the importance of SOEs in Chinese economy cannot be ignored. "The SOEs are increasing their domestic and global influence at unprecedented speed through accumulation of assets and profits" (Yu, 2014). In the current Chinese economic reform, "going globally" has been an important strategy for the development of Chinese economy. Since China joined the WTO, there are more and more Chinese SOEs reaching internationalization through international operations, foreign direct investment (FDI) and international mergers and acquisitions. The total overseas asset of Chinese SOEs is more than one billion dollars. Compared with other countries, the share of SOEs among the top ten Chinese firms is up to 96%, which exceeds that of any other country (The Organization for Economic Co-operation and Development (OECD), 2015, Figure 8.1).



**Figure 8.1. Importance of SOEs among countries' top ten firms**



Note: The shares refer to equally-weighted average of shares of SOEs in sales, assets and market value of country's top 10 firms (see Kowalski et al., 2013). Only countries with shares above 10% are shown. Source: Kowalski et al. (2013).

However, as the current reform is aimed at improving corporate governance and the competitiveness of SOE, there has been huge changes inside Chinese SOE sector. The share of gross domestic product of Chinese SOEs fell from more than 50 percent to 25 percent since 2003, and they only accounted for 5 percent of industrial enterprises in 2018, compared with 18 percent in 2003. Although the number of SOEs has decreased, the strength has not been weakened. In 2017, the assets of the centrally administered SOEs had reached around 10.4 trillion dollars, up more than tenfold from 15 years ago. In the report of Fortune Global 500 in 2018, there are 120 Chinese enterprises that made the list, among which there are 83 SOEs.

Chinese SOE sector has been existing since the foundation of the People's Republic of China in 1949. However, at that time, its role was more than to simply intervene, but to replace the market. With the economic reform in the 80s, the reform of Chinese SOEs was initiated at a low pace, aiming at increasing the productivity and vitality of SOEs. In the 90s, the wave of SOE's insolvency almost destroyed the whole sector and the national economy in

general. For this reason, the government started to improve the reform aiming at reinforcing the large SOEs while releasing the small ones. When China joined the WTO in the early 2000s, the reform was focused more on “improving corporate governance and establishing a modern enterprise system”(Li, 2002). Today, with the fierce international competition and economic crisis, however, the control to the large SOEs from the government has been increasing, which led to the situation where certain industries and services have been concentrated in a few central state-owned enterprises. In other words, in China, it has formed an oligopolistic economic pattern in certain important industries which are controlled by government through SOEs.

The most distinctive feature of Chinese SOEs is that their oligopolistic position in the domestic market does not rely on their unique advantages on technology, price, brand or service, but on the advantages granted by the government through administrative law, the resource allocation and other market-oriented measures. In this way, Chinese government can control and guarantee the sustainable development of national economy.

In short, SOEs in China are not “simply a policy instrument, but a real economic power of the government” (Chen, 2013). They play an important role in making sure the implementation and control of the national central industrial planning; they help to build a government dominance in certain strategic industries; they may have an easier access to enter the market with the massive advantages provided by the government; and they also have been growing with a faster pace due to various kinds of government support in the recent years.

## 2.2 Chinese SOEs: Are they a problem in China?

In spite of all the contribution that Chinese SOEs make to the economy, the problems inside SOE are serious. Among all, the inefficiency in the operation and the high level of government intervention are the most mentioned problems, as they are against the market-oriented principles in the global market.

In the domestic market, SOEs usually fulfill the obligation of correcting the market failure in consideration of public interest in some industries, such as utilities and networking industries, which can be natural monopolies or oligopolies. The direct participation of SOEs in such industries would contribute to “greater economies of scale, more efficient pricing, and higher levels of investment and innovation” (World Bank, 2006). In fact, nowadays, especially in the emerging economies, SOEs account for twenty to thirty percent of the economy activities.

However, in the case of Chinese SOEs, they are considered to be less efficient than those non-SOEs in terms of productivity, profit, etc. Li et al (2015) concluded that “Chinese manufacturing SOEs operate less efficiently than other companies in terms of profitability, labor productivity and firm growth.” The problem of inefficiency can result from the fact that Chinese SOEs are the beneficiaries of the government preferential treatment, such as subsidies, low interest rate, and soft-budget constraint. It is this preferential treatment that makes Chinese SOEs inefficient and highly indebted enterprises. According to the research of OECD (2019), “The SOE sector has been the major business group behind the corporate debt”, which accounts for around 88 percent of it. In 2009, the debt of SOE was already as much as 100 percent of GDP. As OECD (2019) concluded that the surge in SOE debt could be triggered by falling interest costs, pointing to the role of easy monetary conditions in the highly increasing debt of SOE.

The high level of government intervention of Chinese SOEs is another problem. For example, the leader of the fifty-three most important central SOEs are directly appointed by the Party’s Central Organization Department, which makes them not only entrepreneurs, but figures with high political status in the market. In this way, “a SOE is more like a government agency than a free market player” (Zhou and Wang, 2000). Moreover, local or central government are usually involved in most of the investment decisions of Chinese SOEs.

It is thought that it may serve political goals, which raises concerns in the global market.

Although the world realizes both the importance of Chinese SOEs and their problems, the knowledge we have about them is still very limited. In other words, it is a murky world that most people do not know much about, as Chinese SOEs lag their global peers in terms of transparency. For example, there is a divergence between their subsidiaries which were listed in China and listed overseas in terms of transparency. According to Susan Côté-Freeman, head of Transparency International's business integrity programme, the subsidiaries are often better listed overseas than the parent company in China. As a result of that, the transparency system overseas is better and requires more detailed information from the SOEs. However, it reveals that there is no appropriate legal system to regulate transparency in China, compared to the ones from western countries. Although Chinese SOEs are playing an important role in the global economy, the world knows little about it, which can increase the uncertainty of their impact on the worldwide economy. Therefore, Chinese SOEs can be seen as a potential problem.

### 2.3 Can Chinese SOEs be considered as a problem in the global market?

#### *2.3.1 Concerns about Chinese SOEs*

State ownership is not a new economic phenomenon. "Modern theories of ownership generally take a restrictive view of both regulatory failure and the role of the state as owner"(World Bank, 2006). Nowadays, SOEs are becoming a concern in the global market not only because of their fast growth, but also because of their special state ownership, especially in the emerging economies. The challenge is commercial, in view of their sheer size and the subsidies that they may receive from the government, which could affect the fair market competition. And the challenge is also political, given the worries that they may be driven by the state leadership and guidelines.

As already mentioned, as a reward for fulfilling the non-commercial tasks, SOEs can

receive some kind of explicit or even implicit compensations or advantages by their home government owners. The preferential treatment to SOE can be shown in the form of: preferential financing from the SOEs, state banks or other financial institutions, privileged access to information, subsidies, tax concessions and exemptions, grants and other direct payments, privileged position in the domestic market, etc (OECD, 2016).

It can be argued that many large private MNEs can also get this kind of “preferential financing”, when compared to some smaller-scale enterprises. Some banks prefer to provide loans with a lower interest rate to many large private MNEs due to their good market reputation. Therefore, state ownership is not the only condition for certain preferential treatment. In any case, these special compensations or advantages for SOEs are not necessarily shown in a transparent way, which can cause an unequal environment for other private enterprises.

The political concern is mainly because of the special state ownership, as the operations of SOEs can be related to the national development strategies and industrial policies. The concern is that the strategic policy objectives influenced by the government can be prior to the commercial objectives of maximising profits for SOEs, so they “have to factor in the political goals and non-business motivations of their state owners.” (Cuervo et al, 2014).

Nevertheless, there are also some analyses providing evidence that Chinese SOEs are not necessarily led by government dictate. Choudhury and Khanna (2014) proposed the theory in which SOEs may act globally in order to “to achieve resource independence from other state actors”. In other words, instead of accomplishing the strategic missions from the home government, some SOEs may prefer to carry out an oversea expansion to avoid being squeezed by the home government, and to make use of the favorable resources from the host countries. Besides, another core motivation for the SOEs to invest overseas, which is usually

ignored, is related to their own business plan and corporate development. For example, China's international energy investment accounts for a large proportion of China's outward direct investment (ODI). It is always considered that it represents the national strategy of energy security from China's central government. Nevertheless, Zhao (2015) thought that Chinese SOE in the energy sector, like other kinds of enterprises, are normally driven by profit and self-development, rather than by the energy strategy of central government. Internationalization of SOE could be a way of enhancing technological and management capabilities, allocating resources better and integrating the domestic product line of the enterprises.

Finally, the concerns about SOEs in the international market are also because of their "non-commercial" objectives or involvement in the critical infrastructure sector, which might endanger national security or other essential national interests of the host countries. However, as explained above, private MNEs can trigger similar concern. To some extent, foreignness is a more disquieting element than the state ownership.

### *2.3.2 China's trade-disruptive economic model*

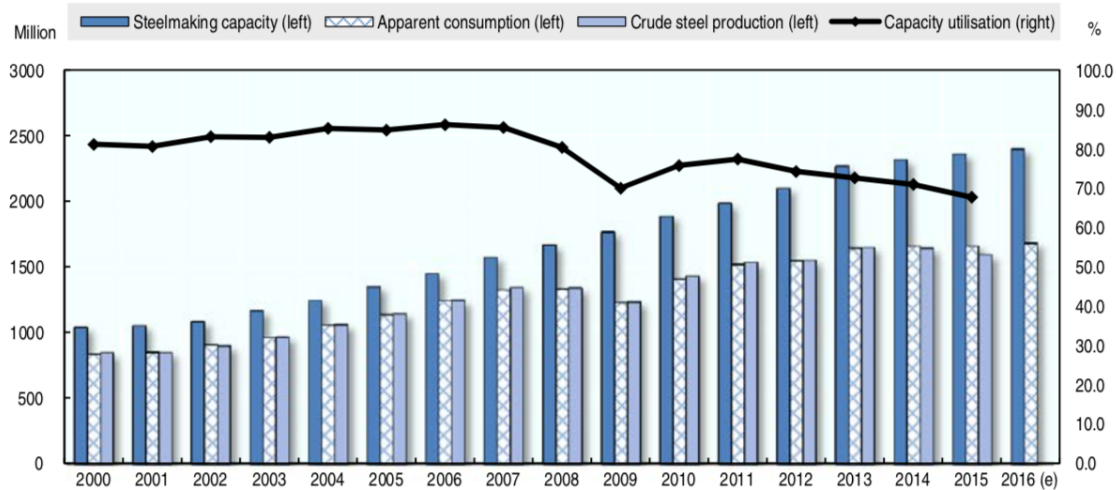
Nowadays, many countries have concerns not only about Chinese SOEs, but fundamentally about China's economic model. From the perspective of U.S. (WTO, 2019), "China still maintains a state-led, trade disruptive economic model not based on those fundamental principles" and it imposes high costs and brings up severe challenges to WTO members.

Government plays a very important role in China's economic development and this vital function of the government in the economy can be contrary to the principles of the market economy. Chinese government plays its role through a high level of indirect or direct control of the economy, such as government ownership and control of key economic actors. In the case of SOEs, the government keeps the control and the appointment of key executives

of SOEs, and provides them with the preferential access to the important inputs, such as capital and real estate. On one hand, the preferential treatment that Chinese SOEs have been receiving can lead to an unfair competition in the global market. On the other hand, it can raise the concern that SOEs are driven by political factors.

In addition, China's economic framework is based on the government planning, which requires Chinese SOEs to perform their functions according to government directives. Chinese government may provide massive market-distorting subsidies and other forms of support to SOEs in order to maintain the development of certain industries regardless of the market principles. Taking Chinese steel industries as an example, they have been receiving massive subsidies from the government. Despite of the continuing falling consumption of steel in the world market, Chinese state-owned steelmaking enterprises have been increasing their production. The gap between growing capacity and stagnant consumption continues to increase (OECD, 2016, Figure 1.11), leading to severe excess capacity in the global market. As U.S. (WTO, 2018) pointed out, that excess capacity in China can hurt global economy not only through direct exports from China but also through lower global prices and a glut of supply, which makes it difficult for even the most competitive producers to remain viable.

Figure 1.11. **World steelmaking capacity - Demand imbalances**



1. Data refers to crude steel. Capacity is defined as nominal crude steelmaking capacity. Capacity utilisation is calculated as crude steel production divided by nominal crude steelmaking capacity

Source: World Steel Association and OECD.

Even though a reform of SOE has been undergoing in China for years, it is not a reform that wishes to stop the intervention of the government in the economy, but one that makes the government play a better role in managing and controlling the economy. In other words, the aim of the current SOE reform in China is to make Chinese SOEs better, bigger, and with a stronger government leadership. It implies that the situation of Chinese SOEs in the global market would not change in the near future, and it would continue to be a concern.

### 3. Case Study

Since China joined the WTO, there have been many dispute cases in which China involved as the respondent. Among the forty-four cases in which China acted as the respondent, six of them involved Chinese SOEs. Such dispute settlement cases could be a source of information in themselves as well as revealing how other WTO members envisage Chinese SOEs. By interpreting the background and the conclusions given by the Panel and the Appellate Body, this section uses the methodology of case study in order to understand



the viewpoints of WTO on whether Chinese SOEs are operating on a level field in the global market. The cases that we studied in this section were the following:

<b>Dispute Settlement No.</b>	<b>Complainant</b>	<b>Respondent</b>	<b>Title</b>	<b>Main Complaint Reason</b>	<b>Main Conclusion/Status</b>
DS363	United States	China	Publications and Audiovisual Products	Only certain wholly or partially Chinese SOEs have the right to import certain publications and audiovisual products, while foreign companies are restricted to importing the products above.	China did not grant a non-discretionary manner for the right to trade and China's market access or national treatment commitments
DS372	European Communities	China	Foreign Financial Information Service and Suppliers	Any operation of the foreign financial information suppliers has to be approved by the Chinese state-owned news agency, Xinhua Agency, in China's domestic market.	China and European Communities reached an agreement as China promised to implement new measures to guarantee the trade rights of foreign financial information suppliers in China's domestic market.
DS373	United States	China	Foreign Financial Information Service and Suppliers	Any operation of the foreign financial information suppliers has to be approved by the Chinese state-owned news agency in the domestic market.	China and United States reached an agreement as China promised to implement new measures to guarantee the trade rights of foreign financial information suppliers in China's domestic market.

DS378	Canada	China	Foreign Financial Information Service and Suppliers	Any operation of the foreign financial information suppliers has to be approved by the Chinese state-owned news agency in the domestic market.	China and Canada reached an agreement as China promised to implement new measures to guarantee the trade rights of foreign financial information suppliers in China's domestic market
DS451	Mexico	China	Production and Exportation of Apparel and Textile Products	Chinese apparel and textile products have been receiving low-price of chemical fiber from state-owned producers, loan with low interest rate from state-owned banks, and some other preferential treatment from the government.	Pending
DS519	United States	China	Subsidies to Producers of Primary Aluminium	China has been providing subsidies to state-owned primary aluminium producer	Pending
DS379	China	United States	Anti-dumping and Counterveiling Duties	China and U.S. have different opinions over the definition of public bodies	China's state-owned banks can be considered as public bodies, so the low interest rate loans provided by them can be considered as subsidies. Other SOEs of steel and rubber cannot be considered as public bodies, therefore their investment of the input was not subsidies and it was not dumping.

*Case 1: China – United States: Measure affecting trading rights and distribution services for certain publications and audiovisual entertainment products (DS363)*

In this case, U.S. accused China of restricting trading rights and market access of foreign enterprises with respect to imported films, audiovisual home entertainment product, sound recordings, and publications, while only certain Chinese state-designed and wholly or partially state-owned enterprises have the right to import the products above mentioned. Viewed from the U.S., the measures appeared that foreign individuals and enterprises were accorded treatment less favorable than that accorded to enterprises in China, with respect to the right to trade. Instead, Chinese SOEs were enjoying exclusive privileges regarding the import of the products above.

The Panel eventually concluded that, Chinese measures in this case can be considered that they were inconsistent with China's obligation to grant in a non-discretionary manner for the right to trade and China's market access or national treatment commitments.

This case can reflect China's trade-disruptive economic policy of providing Chinese SOEs with exclusive privileges regarding imports, which skewed the playing field against imported goods and services. For example, by using the Internet censorship in China, China banned Facebook, Google, and other Internet companies from entering China's market arguing that the public morals have to be protected by the government. Moreover, the related publications and audiovisual entertainment products, to some degree, were also considered to influence public morals. However, China has not demonstrated that the relevant provision are "necessary" to protect public morals, and in fact, it can be considered as a means of restricting imports. Hence, we can conclude that Chinese SOEs received some support from the government that skewed the playing field against imported services and goods in various ways, such as market access limitations.

*Case 2 China – European Communities: Measures affecting financial informations services  
and foreign financial information suppliers (DS372)*

In this dispute case, the European Communities made an appeal to WTO that the presence of foreign financial information suppliers was prohibited or strictly limited; while the state-owned news agency in China, “Xinhua News Agency” acted as the regulatory authority for foreign news agencies and approval procedure in respect of foreign financial information provider. Any operation had to be approved by Xinhua or an agent designated by Xinhua. Hence, if potential users tend to subscribe the services of a foreign supplier, the service could not be provided unless there was an approval of Xinhua or the designated agency. Viewed from the European Communities, China’s measures were inconsistent with China’s obligations of the GATS, the TRIPS and China’s Protocol of Accession.

This case ended with the agreement reached between China and European Communities, as China promised to implement new measures in order to accord foreign financial information services and foreign suppliers no less favorable treatment than that accorded to Chinese financial information services and service suppliers.

There are two more cases (DS373 and DS378) that shared the same issue of China’s restriction on financial information and service provider, but appealed by the United States and Canada. Both of them were ended with agreement reached by the two parties.

We can conclude from these three cases that there was some unfair competition of Chinese SOEs by skewing the playing field against cross-border information and imported services in various ways, such as market access limitation and cross-border information restriction. However, unlike dealing with the unfair competition in China on the export side, other WTO members cannot react to China’s unfair competition regarding the imported goods or service by imposing anti-dumping measures, which makes it more difficult to

correct such unfair competition in a short term.

*Case 3 China – Mexico: Measures relating to the production and exportation of apparel and textile products” (DS451)*

In this case, Mexico pointed out that China appeared to provide some producers and exporters of apparel and textile products with various supportive measures, which included exemptions, reductions, offsets, refunds of income tax, municipal taxes, import duties and Value Added Tax for purchase of equipment for certain groups of enterprises, preferential prices for land use rights, discounted electricity rates and low-cost loans, extended loan repayment periods, and debt forgiveness provided by state-owned banks. Moreover, Mexico indicated that state-owned producers sell chemical fibers at below-market prices in Chinese market which was a cheap input for apparel and textile products. State-owned banks also played an important role by providing financial contribution. In other words, certain Chinese SOEs provided advantages for apparel and textile production and export. Hence, Mexico concluded that all the mentioned measures could be considered as subsidies because the support was from government, or an entity owned or controlled by the Chinese government, which is a “public body”. However, this case is still pending.

Although we do not have a conclusion for this case from the WTO yet, we can study the conclusion of a similar case, “Definitive Anti-Dumping and Countervailing Duties on Certain Products from China” (DS379), in order to speculate about the conclusion. In DS379, United States imposed measures of definitive anti-dumping and countervailing duties against China due to suspected financial contribution, benefit and specificity from Chinese government, while China considered that such measures were against the obligations of the U.S. under the framework of WTO, especially Agreement on Subsidies and Countervailing Measures (the SCM ) and the General Agreement on Tariffs and Trade 1994 (The AD

Agreement).

Additionally, in DS379, was mentioned a very important element, which is a “public body”. If SOEs constitute public bodies, any investment from a SOE, or the loans provided by the state-owned banks can be considered as subsidies. Viewed from the U.S., certain Chinese SOEs were public bodies, because Chinese government was the majority owner of these enterprises and therefore controlled them. However, China held the opinion that an entity can be called public body if it exercises powers to perform functions of a governmental character. Therefore, China did not consider SOEs as public bodies, and the investment of SOEs and the loans provided by state-owned banks should not be considered as subsidies. Nevertheless, the Appellate Body found that a public body is an entity that possesses, exercises, or is vested with, governmental authority. Therefore, in DS379, the Appellate Body determined that certain Chinese SOEs that supplied steel, rubber, and petrochemical inputs to companies should not constitute “public bodies”; while in view of Chinese government’s role in the banking sector, certain State-owned commercial banks that provided loans to the companies in the countervailing investigation could constitute “public bodies”.

DS451 is similar to DS379, as apparel and textile producers received cheap input from state-owned producers of chemical fiber and low interest rate loans from state-owned banks. According to the conclusion given by the Appellate Body in DS379, state-owned banks can be considered as public bodies, so Chinese apparel and textile production and export benefitted from subsidies provided by public bodies, which were certain Chinese SOEs.

#### *Case 4 China – U.S.: Subsidies to Producers of Primary Aluminium (DS519)*

In this case, United States accused China of having been providing subsidies to state-owned and private primary aluminum producers in China since 2007. The subsidies included

providing loans with a very low interest rate and other financing to certain state-owned primary aluminum producers through banks that are government agencies or entities, public bodies, or private bodies.

In both DS451 and DS519 state-owned banks were considered as public bodies, and the low interest rate loans and other financing for primary aluminum producers were considered as subsidies. Moreover, in this case, SOEs were not only the subsidies provider as state-owned banks provided low interest rate loans and other financing, but also the subsidies receiver, as state-owned primary aluminum producers received the advantages provided by the banks and the government. With such subsidies, Chinese SOEs have a better position in the international market in order to promote the export, which can not only undermine fair competition, but also can result in capacity excess in the global market.

Moreover, the disputes regarding public bodies between China and other WTO members resulted from that there was no clear definition and regulation about SOEs and public bodies at the WTO. Therefore, only by making every member recognize the clear definitions and rules can the WTO standardize the international operations of SOEs and reduce the disputes among members.

In short, by studying the dispute cases, WTO found that Chinese SOEs did have some unfair competition in the global market. On one hand, Chinese SOEs enjoyed some exclusive privileges regarding imports, which skewed the playing field against imported goods and services. On the other hand, the unfair competition can result from various supportive policies or preferential treatment that SOEs received from Chinese government or even some advantages that certain state-owned banks provided to other enterprises. However, we only studied a few cases in this section, which is insufficient to allow a definitive statement on the topic. Further studies should be based on more dispute cases of the WTO.

#### **4. Suggestions for Improvement in Transparency**

Transparency is “one of the basic rules governing the post-war trading system” (Ostry, 1998). The purpose of transparency is to “illuminate trade policy practices to the benefit of both government and traders” (Wolfe, 2017). Therefore, every WTO member should abide by transparency principles. At the same time, WTO is usually considered as the organization to negotiate and to settle disputes among members in the post-war trading system. Hence, transparency should be the “third way in which WTO rules and practices influence the trading system” (Halle and Wolfe, 2010), because transparency, “in the form of good data and a forum for surveillance, can reduce the propensity to resort to dispute settlement” (Wolfe, 2013).

##### **4.1 Transparency in China**

As Ostry (1998) mentioned, the core of the transparency for the current multilateral trade system is based on the administrative legal infrastructure of the member states, which could generate an “inside-out” enforcement in order to fulfill the ideal status of transparency. There are two important elements in nowadays transparency practices of WTO, which are democratic governance and efficient markets. By and large, the majority of the western countries do have their administrative legal infrastructure, sharing the same ideals of democratic governance and the similar market principles; while China seems incompatible with the Western Camp. Influenced largely by western legal system, modern Chinese legal system, however, still echoes its historical and cultural tradition. It revealed the problem that “there is no clear separation of powers in China - only a separation of functions” (Ostry, 1998). Besides, the status of market economy of China has been questioned by many WTO members ever since it joined the WTO. Zhou et al (2018) pointed out that the core debate was whether the existing framework of WTO is applicable for the intervention done by the Chinese government in the domestic market even international competition because of



“China’s state capitalism”.

On account of this gap between the standards of transparency mechanism of China and other members, the distrust to China could overburden the WTO dispute mechanism, which we can learn from the cases mentioned in the previous section. Under the circumstances, Chinese government needs to improve the administrative legal infrastructure, which can regulate the operations of SOEs. For example, it should require regular financial reports with the international standard from SOEs to make sure the information disclosure and to improve transparency. Meanwhile, Chinese SOEs should provide accurate financial reports to the public, which include their commercial and policy objectives and what kind of subsidies or support they are receiving from the government, etc.

All in all, information disclosure is the key point to improve the transparency mechanism in China. In order to improve the performance in information disclosure, Chinese SOEs should follow the principles of “trueness, completeness, timelines and openness” (Ma, 2005). “Trueness” is the most important principle, which requires Chinese government and SOEs to guarantee the information is true, simple and understandable. After all, transparency means nothing without true information. Besides, “completeness” requires SOEs to provide all kinds of information to the public, which includes both financial and non-financial information. We should not only know the financial situation of SOEs, but also the information that if they fulfill their social responsibilities, etc. Moreover, “timelines” demands a yearly governance and financial report in order to provide a more comprehensive summary of the operation situation to the public and the decision-makers. Last but not least, “openness” ensures that there will be easy access to the information for not only the shareholders, but also the stakeholders. Step by step, China will build a better transparency mechanism based on the guidance from WTO and the above principles of information disclosure.

## 4.2 Transparency at the WTO

The definition of transparency in WTO Glossary is “degree to which trade policies and practices, and the process by which they are established, are open and predictable.” Nowadays, it takes three forms of transparency in WTO: dispute settlement system, notification and surveillance. Among all, dispute settlement is the most well used, while it still exists a great deal of improvement for the other two. For instance, as Wolfe (2017) argues, the ambiguity about what requires notification results in the poor record of subsidies notification from members. In order to improve transparency, it needs to have a more detailed regulation about the information flow inside the WTO. It is necessary to clarify the purpose of the transparency practices for all members, as it can only work when all the involved parties share the same objective. To normalize the information management, there should be norms to define who should provide the information, who should collect the information, what information is needed and how the data should be presented to ensure the authenticity of the information. With the effective achievement of transparency mechanism inside the WTO, it could not only reduce the information asymmetry in order to rebuild the trust among member states, but also can increase the previsibility of the policies and the stability of the multilateral trade system.

In general, transparency seems like a “better discipline on the spillovers associated with SOEs than a search for binding rules” (Shaffer, Wolfe, and Le, 2015). “If trade policy is made in the light of day, it may not always be captured by interest groups”(Halle and Wolfe, 2007). It can also help us to understand better about Chinese SOEs and their influences that might cause to the relevant market and the global economy. Nevertheless, transparency is much more than an embedded principle of governance (Potter, 2014). It can only attain the expected status when all the members are willing to build a relationship with trust, share the information and make it as a habit.

## **5. Conclusions, Contributions, Limitations and Future Research**

SOEs have been playing an important role in many economies. However, the majority of SOEs are suspected of undermining fair competition environment in the global market. Chinese SOEs, as a typical representative of SOEs, are the focus of the problem. The debate on whether Chinese SOEs are operating on a level playing field in the global market never came to a conclusion.

This paper studies whether Chinese SOEs are operating on a level playing field under modern multilateral trading framework, by reviewing the concerns raised by them, and studying the disputes involving Chinese SOEs at the WTO. Although the cases we studied in this paper suggested that Chinese SOEs were not operating on a level playing field all the time, “it is very difficult for Members to assess China’s compliance with its WTO obligations”(WTO, 2018). In other words, we could only conclude that the result, by no means, is not conclusive, but only suggestive. Moreover, the disputes over Chinese SOEs could also stem from a lack of transparency within Chinese SOE sector. Therefore, the sunshine of transparency from WTO and China itself is needed to illuminate the murky world of Chinese SOEs so that the problem of Chinese SOEs could be exposed better and solved.

A limitation of this topic is that we do not have a fundamental solution for the problems that Chinese SOEs may put in the global market. Improving transparency mechanism in China and WTO can be very important for other members to know better about the murky world of Chinese SOEs and acting accordingly. However, to correct the suspected unfair competition problem existing in Chinese SOE sector, the reform within China is crucial. The needed reform cannot be the kind of reform that China is undertaking, which is aimed at reinforcing the power of the government in Chinese SOE sector. Instead, the reform should focus on the separation of government and enterprises, improving the vitality and

competitiveness of SOE, and adhering to the competition neutrality and market-oriented principles.

For further research, there are three aspects that can be studied. First of all, it can continue to follow further dispute cases at the WTO in order to get more evidence on whether China SOEs are operating on a level playing field. Moreover, this paper pointed that transparency could alleviate the concerns raised by Chinese SOEs theoretically. Therefore, it can be studied whether the disputes at the WTO can decrease by improving transparency mechanism with factual evidence. Last but not least, the reform of Chinese SOEs or even of the economic structure is the fundamental solution for the problem. Further studies can try to come up with more detailed market-oriented reform proposals.

In the end, despite the problems that Chinese SOEs bring to the global market, the purpose of the policy toward China should not be to block the business with Chinese SOEs or their investment. Instead, with the continuing development of economic globalization, “we need to learn how to live with Chinese SOEs as regular foreign investors as well as business rivals for a long time to come” (Chen, 2013).

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