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Opening up or closing the door for foreign trade – Russia and China compared
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Abstract

The phenomenal economic growth in China and relative decline in Russia have made these two emerging economies more similar during the last quarter of the century. Both are large, middle-income countries dependent on foreign trade and burdened with many structural problems that partly stem from their communist past. The domestic structural issues may indeed explain most of the apparent growth slow-down in both of these economies. This short note argues that a significant difference between the two is visible in trade policies. As China is sticking to the “Opening up and reform” policies, Russia is becoming increasingly protectionist. These differences have become increasing visible since the global financial crisis.

Keywords: China, Russia, foreign trade, WTO, trade barriers
Introduction

Some twenty years ago Russia was clearly more advanced of the two countries by almost any measure of economic development; it had liberalized foreign trade and significant parts of capital account, removed most of the price controls and privatized almost all former SOEs. The post-Soviet economic collapse notwithstanding, incomes per capita were more than three times higher than those in China. Russia had already achieved much of what China was only striving for. Thanks to extremely rapid growth in China, these economies today are much more similar. Both are large, middle-income countries dependent on foreign trade and burdened with many structural problems that partly stem from their communist past.

Both China and Russia face a growth slowdown, albeit from very different levels. Russia is in a process of adjusting to levels of potential growth at 1–2% annually from levels at around 7% a decade ago. China is clearly at the beginning of a long-term growth slow-down towards levels typically experienced in other middle-income countries. The low-hanging fruits of imitating and adapting foreign innovations already have been picked and both countries face the broad challenges of increasing productivity in the (former) SOEs, adjusting pension system to a decline in workforce and of increasing the scope and quality of domestic R&D.

The striking feature is that now, when economic structures, standard of living and long-term growth challenges are more similar, the differences in key trade policy areas increasingly pronounced. The marked difference between the trade policy choices of China and Russia stems from fundamentally differing views on two broad matters. Firstly, benefits of globalization, and consequently benefits of trade integration, global trade arrangements and lowering trade barriers are seen very differently. Both Russia and China hugely benefitted from globalization, increasing global trade and the rapid economic growth that followed, especially during the 1990’s and early 2000’s. China clearly managed to benefit more from global integration and WTO membership than Russia ever did. Secondly, the perceptions on private markets and therefore desirability of foreign competition as a driving force of economic growth are somewhat different.

The role of natural resources and the composition of exports may explain a good share of these policy differences, but conscious policy choices on opening up or closing the doors may matter a great deal. The next section of this short note will describe some differences in attitudes towards the WTO and the section three will highlight some developments in trade barriers in these economies. The section four concludes.

Joining the WTO

Given that both countries currently are relatively open economies, with foreign trade and FDI having an important role in economic growth of the last two decades, it is surprising how different their attitudes to trade liberalization has been. China’s strategy of “Opening up” was introduced by Deng Xiaoping already in 1978, and foreign trade and FDI have played a central role in China’s economic reform process ever since. Russia’s economic reforms started later, with rapid trade liberalization in non-energy sectors in 1992–1993. Even though some import tariffs were raised after the initial liberalization, the Russian trade regime largely remained one with low tariffs and very little quotas. Manufacturing exports, however, did not increase in a manner comparable to most CEE countries or the Asian transition economies. Since the initial liberalizations, China has continued to open up, whereas Russia’s attitude to further liberalization and increasing exposure to foreign competition has been ambivalent at best. The process of joining the WTO is illustrative of this difference.
For China joining the WTO has been an integral part of the policy of opening-up and liberalizing the economy. China, an initial member of GATT officially became a member in December 2001. As a result, China made significant commitments to liberalise and further open up its economy. Within a transitional period of only three years, China committed to e.g. allowing foreign trade operations to all companies, eliminate dual pricing practices for export goods, adhere to agreements on intellectual property rights, allow foreign participation in key service sectors, and substantially decrease average import tariff levels. In addition to WTO commitments, China has formed many bilateral free trade agreements with for example South Korea, Australia, ASEAN and Switzerland to open up trade even further.

Even prior to the membership, in 2000 China already was no longer a minor player in global trade.\(^1\) Since the membership China’s role has only increased. In 2014, China was number one exporter and number two importer of merchandise trade with exports 12.3 % of global total, imports 10.3 %. For commercial services, China was number 5 exporter and number 2 importer (exports 4.7 % and imports 8 % of global total).

Russia joined the WTO after tedious negotiations ten years after China, in August 2012. Russia had started negotiations already in 1993, but the political will to conclude the negotiations varied over the years. Prospects for joining looked better at around 2002–2003 when several serious institutional reforms stabilizing and liberalizing the economy were underway. A second moment of increased hopes for the membership appeared at around 2007 as Russia had successfully concluded the bilateral negotiations. The remaining multilateral negotiations were deemed difficult but not unfeasible. The global financial crisis and the resulting economic crisis once again shifted Russia’s priorities.

When the crisis hit in late 2008, the Russian government quickly increased a number of import tariffs and paused the WTO negotiations. Then, in a surprise move, president Putin announced in June 2009 that Russia would seek WTO membership only as a member in the (future) Eurasian Customs/Economic Union. The economic crisis of 2008–2010 clearly changed Russia’s priorities in trade policies away from multilateral framework towards protecting domestic industries from the foreign competition. Russia quickly became the G-20 member that imposed most trade restrictions. By the end of 2010, the Global Trade Alert database contained 132 measures introduced by Russia since October 2008, which was 10 % of measures introduced worldwide (Gerasimenko, 2012).

Russia returned to membership negotiations in late 2010 and the last remaining issues were agreed by end-2011. Russia committed to decreasing average tariff levels, not from the lower levels in 2007, but from the levels elevated by the various anti-crisis measures and incorporated into the Customs Union tariffs in 2010. Russia was granted transitional periods of 5–7 years to decrease tariffs in chemical industry, aircraft and some agricultural products. For car industry, a very long transition period until 2018 was allowed for phasing out the local content restrictions. (O’Neal, 2014).

Russian commitment to decreasing trade barriers and allowing more foreign competition did not last long. It took only 11 months after accession for the first trade dispute against Russia to be opened (“recycling fee” on imported cars). To compare, China was first indicated as respondent in trade dispute in March 2004, over three years after joining the trade organization (VAT on integrated circuits). During the whole membership period (August 2012–August 2016) Russia has been involved in 38 dispute cases (4 as complaint, 7 as respondent, 28 as third party)\(^2\). Since year 2002 China has been involved in 181 dispute cases (13 as complaint, 37 as respondent, 132 as third party)\(^3\).

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1 China was the 7th leading exporter and 8th largest importer of merchandise trade and the 12th leading exporter and the 10th largest importer of commercial services globally in year 2000. WTO fact sheets [https://www.wto.org/english/news_e/pres01_e/pr243_e.htm](https://www.wto.org/english/news_e/pres01_e/pr243_e.htm)

2 [https://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm#rus](https://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm#rus)

3 [https://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm](https://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm)
For Russia, joining the WTO was not a project linked to fostering structural change or economic growth. In fact, many analysts have questioned if Russia ever intended to follow the WTO rules and being a meaningful partner in global trade (Åslund, 2006; Weafer, 2014). Only two months after joining the WTO, Russian Security Council (the inner circle of Russian decision-making) convened to address WTO issues. The focus, however, was not on how to benefit from the membership. The council was to discuss “the formation of an effective mechanism to protect and promote the interests of Russian producers on the domestic and foreign markets, as well as reducing the risks to the population, in the first place - in single-industry towns and regions of the preferential localization of individual industries”4. It was made very clear that Russia did not intend to reform the single-industry towns nor to allow increased foreign competition to harm preferential industries.

Moreover, effective participation would require substantial administrative capacities, something that Russia still lacks (Zubacheva, 2015). Even a Russian permanent mission to WTO was established only in December 2013, more than a year after joining the organization5. A widely held view is that Russia has largely been unable to benefit from the membership (Connolly 2015). China on the contrary, has been remarkably more determined in using WTO membership to its own benefit. Partly the differing attitudes may be explained by the trade structures of the two countries. Russia’s exports are dominated by raw materials that face little if any import barriers globally and therefore membership in WTO could not easily offer immediate benefits. Further, due to the dominance of raw materials in her exports, Russia is less integrated into global value chains and therefore somewhat less dependent on smooth imports and exports. There was, however, a wide consensus among researchers that membership would be hugely beneficial for the Russian economy. Increasing competition in domestic markets should have offered an opportunity to push for productivity gains within both services and manufacturing. (Jensen et al., 2007.) It’s hard to assume these membership benefits would have occurred before fall of 2014, when import-substitution policies and restrictions on imports took the central stage in Russia’s trade policies. Since 2014 Russia has become increasingly protectionist, mostly due to domestic political choices favoring import-substitution in almost all areas of economic activity.

Import-substitution vs. climbing up the quality ladders

WTO/GATT members do not always have any more liberal trade regimes than non-members (Rose, 2007). Even though WTO has a strong positive effect on trade volumes, the impact of a country’s membership depends on what that country does with the membership. The countries that have clearly benefited are those enjoying lower import tariffs in destination countries (Subramanian and Wei, 2007). Some new evidence also highlights that opening up for foreign banking activities does not increase aggregate productivity growth on average, but it benefits the sectors most dependent on external finance (Lai et al 2016). One could reasonably assume these findings to indicate that benefits from increased FDI depend on existing business structures in host country. Opening up to trade and FDI per se do not necessarily foster economic growth. The host country must be determined to secure adequate business climate and market-supporting institutions to make most out of trade liberalization.

While China is often seen as an example of successful liberalization, Russia, quite the contrary, has championed on increasing trade barriers after its membership in the global trade body. According to data collected by Global Trade Alert, Russia and India have implemented almost 450 trade restrictions in since late 2008, more than any other BRICS economy. During the same period, China

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4 Russian Security Council meeting on WTO, November 2012, reported by RIA Novosti http://ria.ru/economy/20121121/911529141.html
“only” implemented 200 measures discriminating against foreign competition (See Figure 1 below). In 2015, Russia introduced more discriminatory trade measures than any other country. China did not make it into the global top-10 list (Evenett and Fritz, 2015).

Figure 1. Measures introduced by China and Russia that influence foreign commercial interests, cumulative sum since Oct 2008.


Notes for red=almost certainly discriminates, amber=likely discriminates, green=does not discriminate against foreign commercial interests. For more information, see the definitions at www.globaltradealert.org.

China appears slightly more liberal also on some other internationally comparable metrics on trade policies. The latest OECD Trade Facilitation Indicator 2015 ranks China slightly above Russia. The indicator is a combination of eleven sub-indices and China ranks higher in eight of them. Russia’s ranking is above China only in measures describing “external border agency coordination”, “appeal procedures” and “availability of advance rulings”. Since entering the WTO in 2012, Russia’s performance has been stable of getting worse. (OECD, 2015).

The evidence suggest that Russia’s WTO membership did not bring along a boost for policy coordination or further trade liberalization. In fact, Russia has experienced a marked shift towards protectionism and outright import-substitution. Many of the recent import restrictions and requirements on domestic content were drafted as a response to economic sanctions imposed on Russia in August 2014, but the shift towards favoring more state intervention, more protectionist trade measures and stricter regulation has been visible already much earlier, especially since the global financial crisis. (O’Neal, 2014).

One may reasonably ask what may have been the outcome of these policy differences. Given the short time period, a thorough study on the matter will have to wait, but the initial conclusion based on recent economic growth is not flattering for Russia. China has greatly benefited from decreased tariffs, increased market access and increased domestic competition that has enabled not only growth in exports but also climbing up the quality ladders (Pula and Santabarbara, 2012). In 1990, only 10 %
of China’s exports was in high-technology goods. By 2000, the share had doubled to around 20% and in 2014 the share was already closer to 30%. The current share is very high, even when compared to some Asian neighbors like Japan and South Korea.

The role of high-tech goods in Russia’s exports has remained below 10%, and most of it consists of goods of (military) aerospace industries. In comparison early 2000’s, Russia has been climbing down the quality ladder in international trade (See Figure 2 below). These figures based on gross trade naturally hide significant differences in domestic content of exports, but the overall levels clearly show how closely linked to global value chains China is.

Figure 2. High-technology exports, % of total manufacturing exports.

![Figure 2. High-technology exports, % of total manufacturing exports.](source:http://www.bof.fi/bofit_en)

Source: World Bank, World Development Indicators.

A similar picture emerges also if one looks at the level of complexity of exports in these two countries provided by the Atlas of Economic Complexity. The complexity index is measured as the variety of products the country produces refined by the number of countries able to make those products. A country with a high index value is understood to export sophisticated goods that only a small number of other nations export. The point estimates are hardly informative, but as seen in Table 1, China’s exports have grown more diversified over the period whereas Russia’s have not.

Table 1. Economic Complexity Index values, 1995–2014.

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<tbody>
<tr>
<td>China</td>
<td>0,58</td>
<td>0,41</td>
<td>0,58</td>
<td>0,80</td>
<td>1,10</td>
</tr>
<tr>
<td>Russia</td>
<td>0,62</td>
<td>0,53</td>
<td>0,62</td>
<td>0,32</td>
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ECI ranks how diversified and complex a country’s export basket is with higher values indicating higher complexity.

There is fresh evidence that trade liberalization has brought new opportunities for domestic producers and lead to increasing varieties of domestically produced goods, and therefore helped to *increase* domestic content of exports in China (Kee and Tang 2016). This positive cycle is absent in Russia.

These differences are also reflected in how China and Russia have approached their common neighborhood in Central Asia during the last decade. The current Chinese initiative, the One Belt One Road, aims to promote economic well-being mainly via offering cheap funding for individual infrastructure projects in Central Asian economies. Russia’s approach, building a common economic space of Eurasian Economic Union (EEU), rests mostly on building a high-level political infrastructure and promoting intra-EEU trade. No wonder China has become the major trading partner of the area providing money, know-how and options for energy exports while Russian success in fostering economic integration has remained poor. (Simola, 2016).

**Conclusions**

On a number of broad economic measures Russia and China have grown more similar over the last decade and a half. Since 2012, both Russia and China have seen a move towards a political model centered around a single strong leader not seen in many decades. Both have become more assertive in their foreign policies, rising issues on e.g. former Soviet space and on South China Sea, respectively. Especially Russian leadership has made clear its foreign policy actions have supremacy over economic matters.

This note argues that even as both countries have grown more similar and turned more authoritarian and more self-confident in international arenas, the difference in the underlying attitude towards potential benefits of international trade has become even more pronounced. Where China has consistently regarded opening-up policies and WTO membership as a crucial element in its development path, Russian leadership has very clearly demonstrated that it wishes to rely on economic self-sufficiency, import restrictions and domestic technologies. Lately, Russia has become the nation imposing a highest number of harmful trade restrictions worldwide.

It is somewhat hard to believe that in today’s interconnected world Russia’s mercantilist and state-lead policy would enhance national welfare in medium to long term. In twenty years we may know the result— but the current outlook is not particularly encouraging.
References


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