

Trade and Investment and the Taiwan Straits -building bridges

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October 26-27, 2002
Berlin, Germany

* A Paper presented at an international conference on 'Exploring Federalism and Integration: The EU, Taiwan, and Korea,' hosted by the European Institute for Asian Studies (Brussels), Institut d'Etudes Politiques de Paris (Asia-Europe Centre), Institut für Asienkunde (Hamburg), International Institute for Asian Studies (Leiden), Nordic Institute for Asian Studies (Copenhagen) in collaboration with Freie Universität Berlin, Centre for Chinese and East Asian Politics.

1. Trojan horse or harbinger of peace?

Are economic and trade relations between Taiwan and mainland China really conducive to peace in the Taiwan Straits and stability in the Asia-Pacific region? Or does Taiwan's growing dependence on mainland China enable Beijing to gain greater economic, social and even political leverage over Taiwan, affecting Taiwan's national security and upsetting the regional balance? In other words, are those economic and trade relations a harbinger of peace or a Trojan horse? That is the issue I would like to discuss with you here today.

For the past fifty years, the situation in the Taiwan Straits has been an issue of major importance for the Asia-Pacific region, and has had a significant bearing on international power relations across the board. During the Cold War, an uncomplicated state of plainly military and political standoff prevailed in the Taiwan Straits; but since the end of the Cold War, the situation in the Taiwan Straits has become obscure and complex. On the political side, antagonism has persisted. Talks and communication have continued on an on-again, off-again basis. Basically, the two sides have not been able to reach a consensus on the issue of sovereign equality, which could even become an igniting-point for fresh conflict. On the military side, while the two sides have not on the surface reverted to a state of warfare, they have stepped up their armaments spending at an unprecedented rate over the last ten years. According to figures from the Stockholm International Peace Research Institute (SIPRI), Taiwan was the world's largest importer of weapons from 1994 to 2000, spending an annual average of US\$2.5 billion on arms purchases. It was only last year that Taiwan slipped down from that top position to ninth in the world, with mainland China replacing it as the biggest weapons importer. Indeed, mainland China's military spending has been growing by double digits from year to year, with this year's official budget set at 166 billion renminbi. That is equivalent to the annual income of 200 million mainland farmers, whose earnings average around only 800 renminbi a year. And it is an open secret that mainland China's official budget far understates the actual figure for its military expenditure.

2. Building a new bridge

But at the same time, a new bridge has appeared across the Taiwan Straits – the bridge of economic links. This bridge began to form around the early 1980s. At first it made for a route of indirect trade, and soon after indirect investment, via Hong Kong. Later on, it came to span the development of direct investment and trade. Over the course of twenty years, this bridge has been transformed from a single plank to a grand viaduct.

According to WTO statistics, mainland China ranks 6th among the world's largest trading nation, while Taiwan ranks 16th. Economic and trade relations between these two major trading powers continue to grow. Since November last year, mainland China has replaced the United States as Taiwan's biggest export market (see Table 1). And Taiwan is currently mainland China's second largest source of imports (see Table 2). Cross-straits bilateral trade volume is rising steadily, as is the level of trade dependence between the two sides. Statistics compiled by Taiwan's Board of Foreign Trade put the aggregate volume of cross-straits trade at US\$30 billion in 2001 (see Table 3).

On the investment side, mainland China is by far the biggest recipient of foreign direct investment from Taiwan. Our own records show that, up to and including the first half of 2002, Taiwan's investment in the mainland amounted to US\$21.43 billion. Mainland China's figure is much higher, at US\$31.06 billion as of June this year (see Table 5). We can be sure that the actual amount far exceeds the official statistics. Among foreign investors in the mainland, Taiwan ranks in third place, with only Hong Kong and the U.S. having invested more there.

3. The contribution made by the economic bridge: looking back over the last twenty years

We now face the reality that a bridge has already been erected across the Taiwan Straits. But does that bridge open the way for emissaries of peace to pass, or does it allow access for a deadly Trojan horse into Taiwan? Let us examine this question from two points of view:

First we need to ask: How has this bridge served the two sides of the Taiwan Straits over the last two decades? Then we need to ask: What functions will the bridge perform in the future, and how traffic on the bridge will be regulated?

For mainland China, the bridge has certainly made a huge contribution to its reform and opening over the last two decades, resulting in the inflow of a huge amount of foreign capital and technology and generation of substantial foreign exchange earnings. Most of the electronics and information products that mainland China now ships to the U.S. and Europe are manufactured by Taiwan-invested firms. Moreover, investment in the mainland by Taiwan firms has created between five and ten million jobs for people on the mainland.

What, then, has the bridge done for Taiwan? **At the end** of the 20th century, when Taiwan's economy entered a major transitional phase, mainland China offered it a potentially vast new market. At this critical time, it gave Taiwan's traditional and less competitive industries fresh opportunities for development. Furthermore, cross-straits trade has yielded a massive trade surplus for Taiwan. According to our official statistics, in the first half of this year alone, our exports to the mainland reached an estimated US\$14.84 billion, while shipments in the other direction amounted to US\$3.55 billion. That created a trade surplus in Taiwan's favor of US\$11.29 billion, up by 30.7% from the same period last year.

On the economic side, the development of cross-straits trade and economic relations over the last two decades has altered an important pattern of division of labor that prevailed in the Asia-Pacific regional economy during the Cold War era, namely the three-way division of labor among the U.S., Japan and Taiwan. Embracing globalization, European countries have been able to augment their presence in the Asia-Pacific, so that a new a model has emerged for a three-sided division of labor, with the G8 (even OECD) countries led by the U.S. and Japan on one side and with Taiwan and mainland China on the other two sides.

Apart from its economic significance, how has the bridge affected general cross-straits relations and regional peace? Though the mainland Chinese authorities do not like any mention of "peaceful evolution," it cannot be denied that contacts between Taiwan's business people and their mainland

counterparts have introduced some of the prevalent values of the outside world to the mainland. At present, there are nearly one million of people from Taiwan living in the mainland. Direct people-to-people contacts make for mutual understanding and help to dispel the distorted images of Taiwan and Western countries engraved in the Chinese people's minds by official propaganda.

Even more importantly, the mainland's growing trade and economic ties with the West and Taiwan must have brought home clearly to its leaders that their country has to modernize to sustain its economic growth and that they cannot lightly cut off this vital flow of economic blood. When tension flared in the Taiwan Straits in 1994-95 and again in 1999, it was alleviated not only by international intervention but also to a large extent by the mainland's own economic considerations.

4. What will come across this bridge in the future?

If this bridge has contributed to maintaining Asia-Pacific regional stability over the past two decades, will it go on playing a positive role over the next twenty years? My answer is: Yes and no.

Let us start with the negative factors. First of all, the more cross-straits trade and economic relations heat up, the more Taiwan's trade and economic dependence on the mainland increases. During the first half of this year, that level of dependence reached 16% (see Table 4), already a definite cause for concern.

Secondly, although Taiwan is still ahead of the mainland in technical and managerial capabilities, it goes without saying that it is much easier to rise from low to medium levels than to go on rising from there to the highest levels. Moreover, the higher the level of technology invested in, the higher the level of risk it entails. Mainland China is making constant progress on the technological front, while Taiwan's industrial upgrading is proceeding relatively slowly. This has become a matter of concern. For if Taiwan's technology and capital continue to flow across the Taiwan Straits, it will eventually cost us our superiority over the mainland. That is why the discussion over our IC industry entering the mainland has generated such heated contention in the past year.

Thirdly, another concern is that the more closely our businesses and people entwine their interests with those on the other side of the Straits, the greater will be the force of support for mainland China within Taiwan, and that Beijing could try taking advantage of this to influence our government policy-making.

Certainly, for the sake of our national and regional security, we cannot afford to ignore any of these concerns. We cannot afford to truly allow a Trojan horse to enter Taiwan. However, cross-straits trade and economic ties cannot simply be cut off. Even a slowdown in the development of such ties will surely bring harm to ourselves. Furthermore, if they were to be cut off, it would leave only political and military confrontation to stoke up the level of conflict. Therefore, the real question to be asked now is: What should we do?

5. Actively pursuing free trade agreements and a cross-straits common market

But the situation really is not as bleak as all that. If we look at it from a positive perspective, the question to be asked is: How to establish a mechanism to ensure the stability and mutual benefit of cross-straits trade and economic ties and safeguard the interests of both sides? Such a mechanism would, in addition, boost the whole region's economic well-being as well as underpin its political stability and peace.

Now that the two sides of the Taiwan Straits have become members of the WTO, both must accept its rules and framework. Under this framework, Taiwan and the mainland will have more opportunities for interaction and a common basis for conducting talks. What Taiwan must consider is how best to use the rules and safeguards of the WTO to advance the establishment of institutionalized trade and economic relations across the Taiwan Straits and at the same time draw on the power of multilateral relations to secure the stable development of cross-straits trade and economic ties.

I believe this can be accomplished through the following approach: In the long term, we should pursue the establishment of a "cross-straits common market," and in the short term, Taiwan should negotiate for free trade agreements with mainland China as well as with the U.S., Japan, the E.U., and other major economies. By becoming party to a number of bilateral and multilateral economic and trade agreements, we can create an economic safety net that will not only safeguard Taiwan's economic security but also safeguard other countries' economic interests in the Asia-Pacific region and on the two sides of the Taiwan Straits.

The idea of a cross-straits common market comes to me from the example set by the countries of Europe. The European experience tells us that, only if we can first put aside political issues and seek economic cooperation will we be able to establish mutual trust and then move on toward political differences.

The cross-straits common market would have two special characteristics. First, it would be based on open economic integration, established within the framework of Asia-Pacific economic integration and compatible with the WTO. Second, it would emphasize complementarity, allowing the economies of Taiwan and mainland China to complement each other in such ways as to help secure the prosperous development of markets on both sides of the Straits as well as in the whole Asia-Pacific region. For example, Taiwan's mature logistics management capabilities can be combined with the mainland's vast market potential to develop regional and global operations or logistics centers.

Establishing a cross-straits common market is a long-term undertaking. A very important step along the way is the signing of a free trade agreement between Taiwan and mainland China. This would enable the two sides to further reduce non-tariff barriers, move toward adopting common standards, better harmonize their relevant regulations, and bring their economies into closer alignment. At the same time, they can extend economic cooperation into such areas as jointly conducting R&D and developing special economic zones.

6. The role of Europe and other advanced industrial nations

As I have said earlier, in the future an important model for division of labor in the Asia Pacific will be that among the G8 (even OECD) countries, Taiwan and mainland China. This will be an amalgamation of multilateral or multi-bilateral relationships. To secure the stability of this model, not only do we need to cement close ties between Taiwan and mainland China and between the advanced industrial countries and mainland China, but we also need to forge close links between Taiwan and the advanced industrial countries. We need to sign free trade agreements with those countries, thereby augmenting our role in international economic and trade cooperation. Such cooperation will be beneficial to the advanced industrial nations, in terms of securing their economic interests in the Asia Pacific.

We need Europe, the U.S. and Japan to give their support to Taiwan, through persuasion and exertion of pressure on the authorities in Beijing. Hopefully, a change of mind will make them willing to put aside political differences and to join with Taiwan and the advanced industrial countries in creating a stable mechanism for economic and trade cooperation in the Asia Pacific.

Recently, the European Parliament has passed a resolution calling on North and South Korea as well as on mainland China and Taiwan to open political dialogue. It urged the two sides of the Taiwan Straits to halt their arms race, and asked China to remove the missiles deployed in its coastal provinces along the Taiwan Straits. This resolution has heartened us greatly. It demonstrates the growing importance of the Taiwan Straits issue to European interests, and also the willingness of the countries of the European Union to join in building a peaceful and stable order in the Asia Pacific.

Lastly, I would like to reiterate one point: The countries of Europe need not fear that their interactions with Taiwan will pose an obstacle to their relations with mainland China. They should view them positively as constructive steps to secure their interests in China and the Asia Pacific. Taiwan is not a troublemaker upsetting regional security; it is, rather, a force for stability. We are willing to engage peacefully with mainland China and to strengthen our economic and trade relations. Indeed, these are things we know we must do. But these interactions must take place under international safeguards. As long as Europe works in cooperation with both sides of the Taiwan Straits, the countries of Europe will be able to find a balanced and steady pathway through this region. Let all of us join together to create, share and uphold the stability and security of a flourishing regional economy in the Asia-Pacific.

Ladies and gentlemen, thank you for your attention.

Annexes

Table 1: Comparison of Taiwan's Exports to the U.S. and Mainland China

Unit: US\$100 million

Year	Taiwan's Exports to U.S.	Taiwan's Exports to Mainland China
1991	223.21	69.28
1992	235.72	96.97
1993	235.87	127.28
1994	243.37	146.53
1995	264.07	178.98
1996	268.66	191.48
1997	295.52	205.18
1998	293.76	183.80
1999	309.02	212.21
2000	348.15	261.44
2001	276.54	240.61
2002 Jan.~June	128.80	148.41

Source: Board of Foreign Trade, Ministry of Economic Affairs, ROC.

Table 2: Mainland China's Imports from Its Principal Trading Partners

Unit: US\$ million

Year	Japan	E.U.	U.S.	Taiwan	S. Korea	H.K.	Singapore
1993	23,303	14,427	10,633	12,934	5,360	10,501	2,647
1994	26,319	16,938	13,977	14,084	7,318	9,488	2,491
1995	29,005	21,254	16,118	14,784	10,293	8,591	3,398
1996	29,184	19,883	16,155	16,182	12,483	7,828	3,613
1997	28,993	19,201	16,298	16,442	14,886	6,990	4,387
1998	28,207	20,729	16,961	16,630	15,020	6,658	4,225
1999	33,768	16,492	19,480	19,528	10,726	6,892	2,631
2000	41,512	30,848	22,363	25,494	23,208	9,429	5,060
2001	42,797	35,723	26,202	27,339	23,389	9,423	5,143
2002 Jan.~June	23,150	17,497	12,098	16,837	12,227	4,904	2,851

Source: Compiled from *China Customs Statistics*.

Table 3: Cross-Straits Trade since 1991

Unit: US\$100 million

Year	Taiwan's Exports to Mainland China	Taiwan's Imports from Mainland China	Total Volume of Cross-Straits Trade	Taiwan's Trade Surplus with Mainland China		Cross-Straits Entrepot Trade as % of Taiwan's Total Foreign Trade
				Value	As % of Taiwan's Total Trade Surplus	
1991	69.28	11.26	80.54	58.02	43.57	7.62
1992	96.97	11.19	108.16	85.78	90.65	10.53
1993	127.28	10.16	137.44	117.12	145.85	13.76
1994	146.53	18.59	165.12	127.94	166.16	13.75
1995	178.98	30.91	209.89	148.07	182.61	13.26
1996	191.48	30.60	222.08	160.88	118.54	13.88
1997	205.18	39.15	244.33	166.03	216.86	13.60
1998	183.80	41.11	224.91	142.69	241.15	12.90
1999	212.21	45.26	257.47	166.95	153.15	13.73
2000	261.44	62.23	323.67	199.21	239.73	13.43
2001	240.61	59.02	299.63	181.59	116.19	14.78
2002 Jan~ June	148.41	35.51	183.92	112.90	119.19	18.12

Source: BOFT, MOEA, *Statistics on Cross-Straits Economic Situation*, various issues.

Table 4: Cross-Straits Trade Dependency since 1991

Unit: •

Year	Taiwan to Mainland China			Mainland China to Taiwan		
	Export Dependency	Import Dependency	Trade Dependency	Export Dependency	Import Dependency	Trade Dependency
1991	9.09	1.79	5.79	1.57	10.86	5.94
1992	11.90	1.55	7.05	1.32	12.03	6.53
1993	14.96	1.32	8.48	1.11	12.24	7.02
1994	15.75	2.18	9.26	1.54	12.67	6.97
1995	16.03	2.99	9.75	2.08	13.55	7.47
1996	16.52	2.99	10.17	2.03	13.79	7.66
1997	16.81	3.42	10.33	2.14	14.41	7.52
1998	16.62	3.93	10.45	2.24	13.11	6.94
1999	17.45	4.09	11.08	2.32	12.81	7.14
2000	17.63	4.44	11.23	2.50	11.61	6.82
2001	19.58	5.50	13.02	2.22	9.88	5.88
2002 1st half	23.82	6.72	15.98	2.50	11.54	6.80

Sources: Extrapolated from BOFT, MOEA, *Statistics on Cross-Straits Economic Situation*, various issues, and *China Customs Statistics*, various issues.

Table 5: Taiwan Investment in Mainland China since 1991

Unit: US\$100 million

Year	Taiwan Statistics		Mainland China Statistics			Ratio•••		
	Cases	Amount	Cases	Contracted Amount	Realized Amount	(1)	(2)	(3)
1991	237	1.74	3,884	35.37	8.69	9.52	6.76	3.72
1992	264	2.47	6,430	55.43	10.50	21.78	9.54	9.54
1993	9,329	31.68	10,948	99.65	31.39	65.60	8.94	11.41
1994	934	9.62	6,247	53.95	33.91	37.30	6.53	10.04
1995	490	10.93	4,852	57.77	31.62	44.61	6.33	8.43
1996	383	12.29	3,184	51.41	34.75	36.21	7.02	8.33
1997	8,725	43.34	3,014	28.14	32.89	59.96	5.44	7.26
1998	1,284	20.35	2,970	29.82	29.15	38.17	5.72	6.41
1999	488	12.53	2,499	33.74	25.99	27.71	8.18	6.45
2000	840	26.07	3,108	40.42	22.96	33.93	6.48	5.64
2001	1,186	27.84	4,214	69.14	29.80	39.14	9.99	6.36
2002 Jan~ June	611	15.36	2,179	43.63	19.24	50.08	9.92	7.83

Note 1: Ratio (1) indicates Taiwan investment in mainland China as percentage of Taiwan's total foreign investment, according to Taiwan's statistics.

Ratio (2) indicates contracted investment in mainland China from Taiwan as percentage of mainland China's total contracted inward foreign investment, according to mainland China's statistics.

Ratio (3) indicates realized investment in mainland China from Taiwan as percentage of mainland China's total realized inward foreign investment, according to mainland China's statistics.

Note 2: Figure for 1991 in mainland China's statistics indicates cumulative investment.

Note 3: Figure for 1993 in Taiwan's statistics includes investment from previous years that was registered in 1993.

Sources: Mainland Affairs Council, *Cross-Straits Economic Statistics Monthly*, various issues; Chunghua Institute for Economic Research, *Mainland China Industrial Development Quarterly*, various issues; DRI Asia Database.