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**Remarks on Cross-Strait Economic  
Integration  
After WTO and SARS**

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By

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# Remarks on Cross-Strait Economic Integration

## After WTO and SARS

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The current trends in the cross-Strait business environment make increasing economic integration inevitable. The question for political leaders on Taiwan is, should greater integration be embraced or fought? In order to investigate the nature of this issue on Taiwan, it is important to examine the varying perspectives of the Pan-Green (Democratic Progressive Party (DPP), Taiwan Solidarity Union), the Pan-Blue (Kuomintang (KMT), People First Party (PFP)), and the approach taken by the business community.

### **Pan-Green**

The Pan-Green coalition is fighting a rear guard action against further economic integration, fearing the gradual erosion of Taiwan's identity and their ability to shape Taiwan's future political trajectory.

The three Mini-links were suspended in April 2003 as a consequence of SARS, a decision that was completely political in motivation and spurred on by the Chen Shui-bian pro-Taiwan faction.<sup>1</sup> There is no political pressure to keep links with the mainland closed, but Taiwan is probably not going to move quickly to restore them in the near-term. It is unclear whether the ability to make progress on establishing direct links to the mainland is a critical political issue right now, but it will possibly become one as SARS subsides and if there is a long lapse before the three Mini-links resume.

It is likely that the DPP will use economic integration as an issue in the coming presidential election. It will cite the "hollowing-out" of Taiwan's industrial base (mostly in the south of Taiwan, a strong DPP base) as a reason for caution and will advocate a slow process for removing barriers to direct links. It will accuse the KMT of undermining that process through reckless engagement with China. The tit for tat exchange between Lien Chan and Chen Shui-bian in March (over Lien Chan's "journey of peace" to China, where Chen's response was re-branding it the "voyage of surrender") is a vivid illustration of the tone that can be expected this coming election season.

An increasingly marginalized Vincent Siew (within the DPP) has finally succumbed to President Chen's wooing and accepted a role in Chen's administration with the economic advisory panel.

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<sup>1</sup> The Mini-links opened two of Taiwan's islands closest to the mainland, Kimmen and Matsu, to direct cross-Strait traffic in shipping, communication, and travel. These links were reopened in July 2003.

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Siew's influence comes at a good time for Chen, and it will buy the President time and credibility, of which he has increasingly little. Siew is a strong proponent of a legal and regulated cross-Strait business environment, as evidenced by his "Cross-Strait Common Market" idea and foundation. It will be important to give Siew some time to demonstrate that he has influence in Chen's administration. However, it is likely that he will have an uphill battle against those who are ideologically opposed to further integration. There are also lingering questions regarding the Panel's relationship with the Mainland Affairs Council (MAC).

### **Pan-Blue**

The close relationship of the Pan-Blue camp with many of the businesses that are heavily vested in China make it the natural ally in a fight to remove barriers to cross-Strait trade.

Lien Chan would clearly like a more conciliatory posture towards business with China, and he has the opportunity to articulate it in the election campaign. However, as a lackluster orator and campaigner, it will be challenging for him, and therefore will perhaps be left to his associate James Soong, who is good at both. Soong would also be able to absorb some of the blows the DPP will undoubtedly inflict in that debate.

On the Three Links, in a speech delivered in March 2003, after receiving the KMT endorsement for the 2004 ticket, Lien said, "I will push for immediate opening of a direct air link with China and sign several agreements with China so that Taiwan and mainland people can live in peace."

### **The Business Community**

The mood in Taiwan's business community is glum. They are very pessimistic about the macro-political picture through March 2004. It has been noticeable that few business leaders have been offering public comments on the present state of Taiwan's economy, or on Taiwan's policies towards China.

Interestingly, Hon Hai Precision Industry Co. remitted \$67.7 million in earned income for 2002 back to Taiwan from their China operations. Acer followed suit in a similar transaction and remitted \$10 million in earned income back to Taiwan for 2002. These are highly unusual transactions, as the profits generated by Taiwan companies in China invariably go undeclared or are remitted to offshore banking facilities.

It is likely that both the Pan-Green and Pan-Blue camps will endeavor to draw in the business community this fall and winter to strengthen their positions and add liquidity to their election campaigns. It's unlikely, however, that the business leaders will do much, if any, heavy lifting on the cross-Straits issue. It is simply too political.

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## SARS and Taiwan

### Political

The DPP has worked hard over the past months to propagate the belief that SARS is forcing Taiwan businesses to reconsider their investments in China. While there is no doubt that SARS has reduced the growth in cross-strait commerce, it is still growing as a percentage of year-on-year trade.

The DPP camp will almost certainly point to Beijing's poor handling of SARS to undermine China's credibility and those who would reach out to China (read KMT/PFP). China's handling of SARS was broadly viewed in Taiwan as having hurt Taiwan's ability to manage the crisis, and that, coupled with the problems with access to the World Health Organization and continued denial of observer status to that forum, will certainly be an election campaign issue. With the link between China's behavior on SARS and the death of Taiwan citizens, it is not a stretch to suggest that China's political apparatus unduly placed Taiwan citizens in harm's way. Chen will certainly hammer the Pan-Blue camp hard on its China position and cite SARS as a reason for continuing to go very slowly with China and as a showcase for the inherent pitfalls in further integration.

The KMT will draw on the poor handling of SARS by the Chen administration, particularly in Taipei. Taiwan's lack of central control hampered the ability of both local and national authorities to coordinate their activities, and Chen's willingness to score political points against Taipei Mayor Ma Ying-jeou undermined the effort at a critical juncture in the early stage of the outbreak. Since the infamous incident when four emergency workers were caught in a flash flood and could have been saved but for infighting amongst emergency services, the Chen administration and Taiwan as a whole have demonstrated a poor grasp of crisis management, which the KMT may seek to highlight in the upcoming presidential campaign.

### Economics

There is a slight change in the global footprint of Taiwan's businesses with the emergence of "China plus one". A private poll of Taiwan businesses conducted by the U.S.-Taiwan Business Council concluded that some orders had gone to Taiwan subsidiaries and non-China facilities in South East Asia (Malaysia, Vietnam & Thailand) and Europe (mostly the Czech Republic) instead of China, but this was in response to the short-term disruptions in the supply chain by SARS and not indicative of a long-term trend. The business model employed by Taiwan's companies still has investments focused on a low-cost manufacturing base and geographical proximity to the core market. That places Taiwan, China, Mexico and the Czech Republic as favorite investment areas for Taiwan businesses. There is unlikely to be any broad impact on cross-strait investment flows as a consequence of SARS.

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## WTO, Taiwan, and China

### Political

Sadly, it would appear that China and Taiwan have found a new venue for the two sides to draw members of the international community into their petty squabbling. The example below is one that demonstrates the distractions their differences bring to those who have vastly more important matters, specifically the Doha round, to worry about.

Taiwan made a tactical error in placing a senior member of the Ministry of Foreign Affairs in the WTO mission office instead of filling the ranks solely from the Ministry of Economic Affairs, the Ministry of Finance, the Ministry of Transportation & Communication, and the Council for Economic Planning & Development. In doing so the Chen administration sent the wrong message about the mission, and provided China an opportunity to encroach on pre-accession arrangements.

Director General Supachai Panitchpakdi apparently approached Yen Ching-chang (Taiwan's representative to the WTO) in February 2003 to discuss four separate issues that the secretariat wished Taiwan to address. There is no hard evidence that the Chinese were behind the request, but there is no reason for the Director General of the WTO to make such requests unless a third party was motivated to apply pressure.

The requests apparently included:

1. *Name Change.* The Director General requested the Taiwan mission change its name from the Separate Customs Territory of Taiwan, Penghu, Kimmen and Matsu (Chinese Taipei) to the Office of the Permanent Mission for Taiwan, Penghu, Kimmen and Matsu.
2. *Titles.* He requested that the heads of the mission not be referred to as Ambassador and Deputy Ambassador but Representative and Deputy Representative.
3. *Switzerland.* He requested that a letter would be exchanged with the Swiss government acknowledging that the presence of the Taiwan mission did not confer any recognition of Taiwan sovereignty by Switzerland.
4. *Taiwan Legislation.* He also requested that any use of Taiwan legislation in WTO work (and the language use of ROC, etc.) would be accompanied with a cover letter clarifying that there was no suggestion of legitimacy or Taiwan sovereignty.

It has been rumored that the PRC's list was longer, but this is what Supachai agreed to take to Taiwan. Since that time ROC and PRC officials have gone back and forward on these issues but have made no progress to date. The United States has expressed its support for maintaining Taiwan's role in the WTO as per their accession agreement, without the changes in name and the loss of status that such a name change would imply.

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## Issues for the United States

The Taiwan account continues to drift, although the early stages of a recovery in two main areas of bilateral relations can be seen.

### Defense

The inability of Taiwan to move on the April 2001 defense package is causing significant tension in the overall relationship vis-à-vis security. While the quiet exchanges that were started by Kurt Campbell in the late 1990s have reaped significant rewards, the purchase of the Kidd class destroyers remains the only significant purchase in two years, and Taiwan continues to drag its feet on the serious matter of its own defense.

Since February 2003, there has been a marked change in Taiwan's posture and a genuine up-tick in rhetoric supporting a greater effort on Taiwan's part to procure systems in three areas: missile defense, ASW and C4ISR. A steady stream of delegations is traveling to the United States to discuss procurement and the United States is stressing the need for more urgency on Taiwan's side.

### Business

The passing of the recent law governing intellectual property rights (IPR) in the last legislative session of the Legislative Yuan further strengthens the ability of Taiwan's courts and law enforcement agencies to arrest and prosecute IPR violators. This is encouraging. What is not yet clear is the level of enforcement that can be expected, as this has been the primary issue for the United States over the past 18 months.

## U.S.-Taiwan Free Trade Agreement

### Background

On November 6, 2001, Senator Max Baucus proposed the U.S.-Taiwan Free Trade Agreement Act of 2001 (S1636), authorizing the negotiation of a free trade agreement (FTA) with Taiwan and providing for expedited congressional consideration of such an agreement. The proposal was read twice in Congress and was referred to the Senate Finance Committee on November 6, 2001. On January 17, 2002, following Taiwan's admission to the WTO, the Senate Finance Committee, through its chairman Senator Baucus, submitted to the U.S. International Trade Commission a request for an examination of the likely impacts of a U.S.-Taiwan Free Trade Agreement. The Commission's findings were published in a report on October 21, 2002, and concluded that trade between Taiwan and the United States would increase and that both economies would likely experience relatively small but positive economy-wide effects from an FTA.

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The office of the U.S. Trade Representative has to date not expressed an intent to launch into FTA negotiations with Taiwan, but there are currently two pending concurrent resolutions (98 and 117) in Congress that urge progress on a U.S.-Taiwan FTA.

Observers do not foresee negotiations on a U.S.-Taiwan FTA starting in the short-term (the next 18-24 months), until some of the current issues in the bilateral trade relationship have been resolved, and Taiwan has met its commitments to the WTO. Several outstanding issues in IPR protection (particularly in optical media), telecommunications sector liberalization, the rice import system, and pharmaceuticals have to be addressed before an announcement on FTA negotiations can be considered.

There is also a recognized need for further liberalization of the cross-strait business environment for the U.S.-Taiwan-China economic relationship to benefit fully from a U.S.-Taiwan FTA. However, as the medium to long-term strategic value of a U.S.-Taiwan FTA – including stabilizing the cross-strait environment, thereby reducing risk for U.S. companies operating in Taiwan and China – is recognized, support for dialogue on an FTA with Taiwan to encourage substantial discussions on the benefits of a free trade agreement will increase.

### *Timeline of Congressional FTA Activities*

DATE	ITEM	STATUS
November 6, 2001	Senator Max Baucus proposes the U.S. Taiwan Free Trade Agreement Act of 2001 (S1636), authorizing the negotiation of a Free Trade Agreement with Taiwan and providing for expedited congressional consideration of such an agreement.	The proposal was read twice and was referred to the Senate Finance Committee on November 6, 2001
January 17, 2002	Senators Max Baucus and Chuck Grassley of the Senate Finance Committee submit a request for an examination of the likely impacts of a U.S.-Taiwan Free Trade Agreement to the Chairman of the U.S. International Trade Commission.	Fact finding study began February 6, 2002  Report released October 21, 2002
October 21, 2002	The U.S. ITC publishes "U.S.-Taiwan FTA: Likely Economic Impact of a Free Trade Agreement Between the United States and Taiwan"	N/A
March 18, 2003	Representative Jim Ramstad submits concurrent resolution 98, calling for Congress to express support for launching negotiations to enter into a free trade agreement with Taiwan.	Referred to the House Committee on Ways and Means on March 18, 2003  Referred to the Subcommittee on Trade on March 20, 2003
March 25, 2003	Representative Robert Wexler submits concurrent resolution 117, calling for Congress to reaffirm its commitment to Taiwan and the Taiwan Relations Act by, among others, publicly supporting a U.S.-Taiwan Free Trade Agreement.	Referred to the House Committee on International Relations on March 25, 2003
June 11, 2003	Senator Max Baucus writes a letter to United States Trade Representative Robert Zoellick expressing support for efforts to liberalize trade through FTAs, mentioning Taiwan as a potential FTA partner, and referencing the request for a General Accounting Office report on the selection process for FTAs.	GAO report on the selection process for negotiating FTAs due to Senate Finance Committee on November 1, 2003