

Asia-Pacific Center for Security Studies



April 2004

Cross-Strait Economic Relations: Opportunities Outweigh Risks

Denny Roy



***Occasional
Paper Series***

Report Documentation Page

Form Approved
OMB No. 0704-0188

Public reporting burden for the collection of information is estimated to average 1 hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to Washington Headquarters Services, Directorate for Information Operations and Reports, 1215 Jefferson Davis Highway, Suite 1204, Arlington VA 22202-4302. Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to a penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number.

1. REPORT DATE APR 2004	2. REPORT TYPE	3. DATES COVERED 00-00-2004 to 00-00-2004		
4. TITLE AND SUBTITLE Cross-Strait Economic Relations: Opportunities Outweigh Risks		5a. CONTRACT NUMBER		
		5b. GRANT NUMBER		
		5c. PROGRAM ELEMENT NUMBER		
6. AUTHOR(S)		5d. PROJECT NUMBER		
		5e. TASK NUMBER		
		5f. WORK UNIT NUMBER		
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) Asia-Pacific Center for Security Studies, 2058 Maluhia Road, Honolulu, HI, 96815		8. PERFORMING ORGANIZATION REPORT NUMBER		
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)		10. SPONSOR/MONITOR'S ACRONYM(S)		
		11. SPONSOR/MONITOR'S REPORT NUMBER(S)		
12. DISTRIBUTION/AVAILABILITY STATEMENT Approved for public release; distribution unlimited				
13. SUPPLEMENTARY NOTES The original document contains color images.				
14. ABSTRACT				
15. SUBJECT TERMS				
16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT	
a. REPORT unclassified	b. ABSTRACT unclassified	c. THIS PAGE unclassified	12	19a. NAME OF RESPONSIBLE PERSON

Cross-Strait Economic Relations: Opportunities Outweigh Risks

Paradoxically, the economic relationship between China and Taiwan is thriving even as long-simmering tensions between the governments have increased during the presidency of Chen Shui-bian. Cross-Strait trade and investment have inescapable and intense political overtones. It is a “low politics” issue wrapped in “high politics.” Taiwan finds the economic opportunities on the mainland irresistible. Yet Taiwan recognizes that trading with China supports the strategy of the country representing Taiwan’s chief security threat. Cross-Strait economic ties bear strongly on Taiwan’s continued economic health and political viability, and also stir up the most divisive political issues in Taiwan’s domestic politics.

This paper surveys the ways in which both China and Taiwan have politicized cross-Strait economic relations, mainly by tightly linking the economic relationship to their respective political agendas. While observers in Taiwan are prudent to thoroughly examine the implications of economic cooperation with the People’s Republic of China (PRC), a strong case can be made that Taiwan’s fears about economic integration with China are overdrawn. From the standpoints of both economics and security, the disadvantages to Taiwan of increased trade with and investment in China are arguably outweighed by the advantages.

PRC Politicization of Cross-Strait Trade

PRC officials have explicitly stated that economic interaction with Taiwan is intended to promote unification. This strategy was made clear as early as the May 1979 “Temporary Regulations Regarding Opening Trade with Taiwan,” which asserted that “Trade with Taiwan is a special form of trade in the transitional period before Taiwan returns to the motherland ... to create conditions for unification of the motherland.”¹ Subsequent PRC leaders have reiterated the political objective of cross-Strait trade.

From the PRC’s standpoint, Taiwan must reunify with China for both political and economic reasons. The political reason is that historically, unity is associated with national strength, and division with weakness. The Chinese nation will not be healthy or happy without unification because this aspiration is deeply ingrained in the hearts of all Chinese, according to PRC commentators. Without this psychological sense of fulfillment, China will not reach its full potential. The economic reason is that unification with Taiwan will contribute to China’s economic development because of the complementarities between the PRC and Taiwan economies. Like the legal arguments Beijing puts forward to support its claim to ownership of Taiwan, these arguments are not necessarily cogent or persuasive to a dispassionate observer, but they are widely accepted on the mainland.

China’s strategy of promoting substantial economic exchange as a means of bringing about Beijing’s ultimate objective, which is getting Taipei to accept political union on PRC terms, appears to be based on two primary assumptions. The first is functional spillover: economic cooperation requires a degree of low-level technical integration, which can expand into administrative coordination and, eventually, creeping political integration. Western Europe is the model for this process. In that case, governments initially resisted compromising their sovereignty but were willing to allow economic activities to cross political boundaries more freely. Technical cooperation allowed for a gradual and stealthy strengthening of supra-national political institutions. The results have been dramatic. A European Community, in which citizens of one member country are free to seek employment in another, is emerging where member states fought against each other for control of the continent twice in the last century.

The second assumption that apparently underlies China's strategy is socio-cultural spillover: human contact between Taiwanese and mainland Chinese that occurs as a part of cross-Strait economic exchanges will make it easier for Taiwan's people to desire—or at least agree to—political unification with China in the future. As Zhu Weidong, a researcher with the Institute of Taiwan Studies at the Chinese Academy of Social Sciences, puts it: “The exchange of visits is bringing the minds and feelings of the public on the two sides closer and has been playing a positive role in promoting mutual knowledge, understanding, and accommodation and in cultivating and enhancing their mutual trust. The closer and closer cross-Strait economic relations have laid a solid foundation for the improvement and development of cross-Strait political relations.”² This assumption draws on Samuel Huntington's argument in *The Clash of Civilizations* that common ancestry, language and culture are important forces rallying peoples together and establishing distinctions between “us” and “them” that will give rise to the major global political divisions in the post-Cold War world.³ Ironically, many Chinese analysts have severely criticized Huntington's work for its suggestion of inevitable long-term antagonism between China and the West.

China's strategy includes a good deal of politicking aimed at the Taiwan audience. Beijing argues that the attempts of “Taiwan authorities” to restrict the economic activities of Taiwan residents on the mainland have been interfering with the natural operation of market forces. This has been mainly to the detriment of Taiwan itself, which needs unfettered access to China's vast market and resources to sustain its economic development. Beijing has reiterated this argument more strongly since the economic downturn that has afflicted Taiwan since 2000. With the industries that powered Taiwan's rapid postwar growth peaking out, and with China becoming a major player in a wide variety of industrial sectors, Taiwan faces a bleak future in an increasingly competitive global economy unless it fully partners with China. In essence, Beijing asserts that Taiwan must unify with China to remain prosperous in the twenty-first century.

Representative of the PRC's view is the statement from Zhang Mingqing, an official of the State Council's Taiwan Affairs Office, calling on Taiwan's government to “move with the tide, respect popular opinion, abolish irrational restrictions as quickly as possible, and make tangible efforts to promote the development of cross-Strait economic and trade ties.” The cross-Strait economic issue emboldens PRC officials to turn the tables and charge Taipei with undemocratic policymaking.⁴

China believes strongly enough in the power of economic ties to achieve its political objectives that it is willing to accept a considerable economic loss as part of the bargain. The PRC offers Taiwan investors preferential tax treatment and has tolerated a long-running trade deficit with Taiwan that has reached more than \$20 billion annually.

Taipei Tries to Stem the Tide

Taiwan struggles with the question of whether to fear expanded economic contact with China as a threat to national security or to welcome it as a contributor to the island's prosperity and peace. The forces propelling cross-Strait economic relations are obvious: close geographic proximity, a common language and culture, and in some cases ancestral ties. Economic complementarities are even more compelling. Taiwan offers investment capital, managerial expertise and advanced technology, for which China yearns. China in turn offers Taiwan a relatively cheap and disciplined workforce, low overhead costs, and less demanding environmental regulations, plus additional tax incentives designed to attract Taiwan investors.

To a large degree, it appears the market has shaped, if not dictated, policy to the political leadership in Taipei. Taiwan's cross-Strait economic policy of the last two decades displays a pattern of grudging concessions to the domestic business community to liberalize restrictions on trade with and investment in China, in spite of the government's concerns about possible risks to national security. Taiwan businesspeople have often been ahead of the policymakers (i.e., violating the restrictions), with officials "in essence legalizing what is already taking place."⁵ Ironically, much of Taiwan's business community is ethnic Fujianese, who tend to be the strongest supporters of a distinct Taiwanese identity, de-Sinification, and Taiwan independence. Yet they lobby for freer cross-Strait trade, investment and travel, just as Beijing does, to the chagrin of many Fujianese political activists. This phenomenon invokes the adage that "the businessman has no country." It also suggests Taipei has only limited control over an area of vital national interest.

Taipei has frequently tried to encourage Taiwan investors to look for opportunities in other countries to reduce dependency on China. The government has long championed Southeast Asia, which offers some of the advantages found in China, as an investment destination. Most recently, the Ministry of Economic Affairs has promoted the virtues of investment in Eastern Europe and South Asia.⁶ This encouragement has had a marginal effect but has failed to displace China as the most attractive market for Taiwan investors.

Consequently, since the early 1990s, economic activity across the Strait has grown rapidly and steadily, with no end in sight to continued expansion. Trade between China and Taiwan is expected to exceed US\$50 billion in 2004, a 25 percent increase over that of last year. If investment through third parties is factored in, China may absorb as much as half of Taiwan's outbound foreign direct investment.⁷ Taiwan is China's second-largest source of imports, while China takes in a quarter of Taiwan's exports. Taiwan residents make more than three million trips to the mainland annually. An estimated one million Taiwan people live on the mainland, nearly half a million in the greater Shanghai area. New links continue to form yearly. In November 2003, for example, Beijing gave permission for four Chinese banks to establish representative offices in Taipei. Several Taiwan banks had already opened representative offices on the mainland in 2002.

The Chen Shui-bian government has fallen into the familiar pattern. Chen's core supporters are not ideologically inclined to favor accelerating cross-Strait economic ties. Yet the search for a way out of Taiwan's economic recession evidently motivated Chen to accept the main recommendations of the Economic Development Advisory Conference in August 2001. Chen's government replaced former President Lee Teng-hui's cautious policy of "no haste, be patient" with an "active opening, effective management" policy that included a repeal of the \$50 million limit on single Taiwan investment projects on the mainland.

The Three Links

Since 2003, the most prominent nexus of cross-Strait economics and politics has been the "three links" issue. Beijing has long advocated swift implementation of the three links (unfettered trade, transportation and postal service across the Strait).⁸ The question is no longer whether these links will eventually be established, but rather how quickly and under what circumstances. Chen's government has been under heavy pressure from the Taiwan business community to relent. They complain particularly about the additional time and expense of stopping over in Hong Kong during air travel between Taiwan and Shanghai. Some multinational corporations with headquarters or major operations in Taiwan, as well, have threatened to move to the mainland unless Taiwan agrees to direct shipping links with Chinese ports.

As a preliminary step, Chen's government opened the "three mini links" between the mainland and Taiwan's outlying islands in 2001. Although this was a favorable development from China's point of view, Beijing's initial reaction was cool, probably because the PRC wanted to limit the domestic political gains Chen would garner if the Taiwan public perceived he had made progress in cross-Strait relations. In October 2003, Taipei made it legal for a private organization to conduct negotiations with China on behalf of the Taiwan government on issues such as the establishment of direct transportation and trade links.

The "three links" issue drags because Taiwan's government has continued to raise objections on economic and security grounds to establishing them. Taipei has publicly embraced the notion that accelerating cross-Strait trade could economically harm Taiwan through a more rapid loss of jobs and technology to China and politically harm Taiwan by increasing its vulnerability to PRC economic coercion for political ends. Furthermore, some Taiwan military analysts argue that direct transportation links could be a threat to national security, as PRC warplanes could sneak in if Chinese jetliners were allowed to fly directly to airports in Taiwan. In the Taiwan government's proposal for future implementation of the three links published in August 2003, airliners flying in from China would take an indirect route through the airspace of a third country, a reflection of the Ministry of National Defense's ongoing concern.⁹

Chen's government essentially remains ambivalent toward the three links, and as the March 2004 presidential election grew closer his officials indicated they would not move quickly to establish the links. Several of Chen's appointees have recently argued that the potential benefits to Taiwan of direct transportation links are exaggerated by proponents. The overall effect, they say, could be negative, with a transfer of Taiwan's talent, resources and capital to China and marginalization of Taiwan's economy within the global trading system. In a July 2003 editorial in the *Taipei Times*, Huang Tien-lin, a national policy advisor to Chen, called direct links and a Beijing-sponsored proposal for a Taiwan-China free trade area "strategies aimed at making Taiwan quench its thirst with poisoned drinks." He decried "China's evil plan to bait Taiwan businesspeople" with "lures that make you lose reason and resistance ... to make you fall into its trap to be slaughtered." Former Taiwan President Lee Teng-hui and others argue that further cross-Strait economic integration would benefit a few Taiwan businesspeople but harm the majority of the island's population. In August 2003 Lee warned of Taiwan's people losing jobs to Chinese migrants and a drop in salaries and real estate prices in Taiwan to levels that prevail in China.

In October 2002, Chinese Vice Premier Qian Qichen made an attempt to de-politicize the three links issue by saying they could be considered "cross-Strait" instead of "domestic." This was a feeble gesture, however, when viewed against the abundant indications that China considers the promotion of cross-Strait trade an integral part of its strategy for achieving the political goal of unification.

Potential Threat to Taiwan's National Security

For Taipei, these deepening cross-Strait economic ties have serious political consequences. Analysts foresee several ways these ties could pose a danger to national security. The first potential threat is a weakening of Taiwan's economy. The relocation of Taiwan firms to mainland China to take advantage of lower overhead and labor costs understandably raises fears of a decline of manufacturing jobs in Taiwan and a hollowing out of Taiwan's industrial base.

Some observers also argue that heavy investment in China leaves Taiwan dangerously exposed to a possible downturn in a country that in some ways appears economically fragile. China is vulnerable to a crisis because it is undergoing a massive economic, social and political transformation. While China's economic reforms have accelerated economic development, they have also created turmoil and dislocation, and some Chinese have clearly benefited more than others. Many observers argue that China must maintain an annual economic growth rate of around 7 percent to stave off a serious socioeconomic crisis. China has been fortunate to enjoy consistent, rapid growth over the last two decades. But since economic growth tends to follow cycles of stronger and weaker periods, it will be very difficult for China to maintain such a high growth rate indefinitely. Other serious problems include unemployment caused by the privatization of uncompetitive state-owned industries, the influx of large numbers of migrant rural workers into Chinese cities, the potential collapse of China's fragile banking system, the growing disparity of wealth between rural and urban areas and between the eastern and western parts of the country, worsening pollution and the loss of arable land, and increasingly serious incidents of public disorder. At the same time, China will likely face further demands for political reform from the public, which could give rise to more mass protests such as those that took place in Beijing and other major cities in 1989. These actual and potential problems create conditions that could trigger a socio-economic upheaval. In such an event, foreign investors could suffer huge losses along with the rest of the Chinese economy.

A military conflict between Taiwan and China could be equally disastrous for Taiwan businesses on the mainland. Some might even be subject to collateral damage, as Taiwan Minister of National Defense Tang Yau-ming has said that Taiwan cannot rule out its own pre-emptive military attacks on the mainland, where hundreds of thousands of Taiwan citizens reside.¹⁰ One might argue, therefore, that Taiwan should curtail its investment on the mainland until the possibility of armed conflict diminishes.

A second fear is that through their economic ventures in China, Taiwan firms could help raise the technological proficiency of their potential adversary. The debate in 2001 and 2002 over whether or not to allow Taiwan investment in the production of 8-inch wafer fabrications typified the clash between economic and national security considerations. Computer semiconductor production has been Taiwan's flagship high technology industry, and many analysts have insisted Taiwan needs to maintain a qualitative edge over the Chinese economy to stay internationally competitive. Moving 8-inch wafer production to China would likely help China overcome Taiwan's advantage. Yet the pull of the marketplace was irresistible. Taipei decided to permit limited investment. According to one estimate, the movement of 8-inch wafer production to China will cost Taiwan seventeen thousand jobs by 2005.¹¹ Even if Taiwan benefited in overall economic terms, the question of relative gains arose: Taiwan could be helping to accelerate the PRC's economic domination over Taiwan, which could ultimately make Taiwan's political resistance to absorption by the PRC futile. Furthermore, helping the PRC upgrade its information technology capabilities could indirectly aid the modernization of the People's Liberation Army, Taiwan's military foe.

Third, Taiwan fears that heavy cross-Strait economic interaction creates a dependency on Taiwan's part that Beijing will be able to exploit for political purposes. If China becomes a crucial market or supplier, it could one day deny Taiwan continued access unless Taipei agrees to Beijing's proposal for unification. Some worry China could nationalize Taiwan-owned businesses or even hold Taiwan citizens residing in China as hostages to force its political will on Taiwan. The PRC has already used the cross-Strait economic relationship to attempt to gain political concessions—by arguing, for example, that Taipei's acceptance of the "one-China" principle will stabilize and improve the cross-Strait political environment, thus reducing the risk to Taiwan's

investments on the mainland. This tactic is quantitatively different but qualitatively similar to the extreme measure of taking Taiwan businesses and businesspeople on the mainland hostage to force Taipei to accept unification.

Finally, cross-Strait economic activity intensifies certain social issues that have ramifications for national security. Increased economic interchange involves more voluminous movement of people across the Strait. This human movement is generating several problems or potential problems that have mobilized criticism in Taiwan.

Taiwan citizens express worry that agents of the PRC government are infiltrating amidst the growing numbers of Chinese coming to Taiwan for work or as spouses of Taiwan residents. China is allegedly trying to steal technological secrets from Taiwan, especially targeting facilities such as the Chung Shan Institute of Science and Technology and the Hsinchu hi-tech industrial park. In August 2003 a group of Democratic Progressive Party (DPP) legislators warned of the danger of Chinese female spies working as bar hostesses seducing Taiwan's computer engineers and fighter pilots. The Taiwan press has raised the concern that PRC spies may be among the estimated one hundred thousand Chinese women that have entered Taiwan. In some cases the basis for their immigration turns out to be a sham marriage.

The fear of heightened espionage as a consequence of cross-Strait economic ties is not limited to Taiwan. China accuses Taipei's military intelligence service of using agents traveling in the mainland disguised as businessmen to gather national security secrets, and the Chinese government has tried and convicted what it says are several such people. Significantly, however, the Chinese follow such reports with the assurance that "the criminal acts committed by a few Taiwan businessmen neither will nor can affect the policy of [China] . . . continuing as always to protect the legitimate rights and interests of residents from Taiwan."¹² The Chinese position therefore is not that such incidents call into question cross-Strait exchange, but rather that cross-Strait exchange must take place in spite of such incidents. Nevertheless, Beijing is clearly unwilling to turn a blind eye to potential Taiwan espionage, even at the risk of marginally souring the atmosphere for cross-Strait trade—which souring occurs because lack of faith in the Chinese judicial system invariably leads Taiwan to question the legitimacy of these "spy" convictions.

Some commentators complain that Taiwan businesspeople who relocate to mainland China become unwitting mouthpieces for the PRC government, arguing in favor of Chinese positions such as affirming the one-China principle and speeding up integration. This phenomenon of a pro-PRC constituency in Taiwan could intensify with growing numbers of Taiwan children being raised and educated in China while their parents are working on the mainland, and with Taiwan businesspeople marrying PRC nationals and bringing them to Taiwan. Taiwan students attending universities in China is a particular concern because of young adults' high degree of political awareness and impressionability.

An indirect issue for national security is contagious disease. Taiwan considers its public health system superior to that on the mainland. Several serious communicable diseases that have been eradicated in Taiwan prevail in China. Cross-Strait travel creates the potential for Taiwan to suffer as a result of China's relative backwardness in hygiene and medicine, as underscored by the recent SARS epidemic.

Risks Overstated?

That cross-Strait economic interaction poses risks to Taiwan is undeniable. Some of these risks, however, may be overdrawn, and cross-Strait trade and investment also offer Taiwan considerable opportunities—both economic and political. A most obvious benefit is Taiwan’s considerable trade surplus with China.

With or without China, Taiwan’s economy faces challenges in the new century. Other countries have become more competitive in some of the industries that led Taiwan’s rapid postwar economic development. Membership in the World Trade Organization (WTO) requires trade liberalization that will severely threaten parts of Taiwan’s economy, such as small-scale farmers. Economic cooperation with China can potentially assist in the restructuring Taiwan needs to implement to remain prosperous. In the past, direct investment on the mainland has allowed Taiwan firms to upgrade their production. They established an “intra-firm division of labor,” moving their labor-intensive operations to China to take advantage of lower labor costs and keeping their higher value-added operations in Taiwan.¹³

The extent of the alleged industrial “hollowing out” of Taiwan, of which investment on the mainland is said to be a major cause, is debatable. The relative contribution of manufacturing to Taiwan’s gross domestic product has declined, but this is partly explained by the expanded contribution of the service industry. Higher productivity in manufacturing also contributes to de-industrialization.¹⁴ Neither of these two phenomena is directly related to cross-Strait trade.

There are two counter-arguments against the view that Taiwan’s government should restrict investment in China to prevent Taiwan from being dragged down by a mainland economic decline. First, it is not clear that China is a substantially riskier place to do business than many of the alternative venues. China, for example, weathered the 1997 financial crisis far better than did South Korea or some countries in Southeast Asia, which Taipei has touted as an alternative to investing in China. Second, while doing business with China undeniably involves risks, risk-analysis and investment strategy is a job for entrepreneurs, not governments. The Taiwan government should not, therefore, attempt to limit cross-Strait economic interaction in an attempt to protect Taiwan businesses from hurting themselves. Individual businesspeople are at least as concerned about their own bottom lines as the Taiwan government is and should be left to make their own calculations about risks. The role of government, on the other hand, is to provide them with the greatest number of opportunities.

Would China take Taiwan businesspeople on the mainland as political hostages? Tung Chen-yuan argues that this is politically impossible. Beijing publicly praises Taiwan citizens residing on the mainland as “compatriots loving their motherland.” They are fulfilling the PRC’s wishes and are to be rewarded rather than punished. This precludes the Chinese authorities, therefore, from depriving Taiwan people in China of property or liberty as a means of coercing “separatists” in the Taiwan government.¹⁵

It would be both economically and politically difficult for the PRC to attempt to use economic coercion against Taiwan. China has passed laws to protect Taiwan investment in China from nationalization or expropriation, such as the 1988 Regulations on the Encouragement of Taiwan Compatriots’ Investment and the 1994 Law on the Protection of Taiwan Investors. Observers in Taiwan may argue, of course, that PRC legal guarantees are not reliable. But there are other reasons, based on Chinese self-interest, why China would hesitate to squeeze the economic lifelines between Taiwan and the mainland. Much of China’s economically dynamic southeast coast is highly dependent on international trade. China’s economy, and particularly the

key southeastern coastal areas, would suffer heavily from a ban on imports from Taiwan. Investment from Taiwan supports the employment of hundreds of thousands of mainland Chinese.

Globalization has multiplied the international connections of Taiwan firms doing business on the mainland, and the entry of both China and Taiwan into the WTO places their economic relationship into a larger context and network. An obvious consequence of WTO membership for both China and Taiwan is that the WTO's arbitration procedure provides an avenue for Taiwan firms in China that believe they are mistreated to seek redress. Through the WTO, Taiwan could internationalize a dispute with China. The PRC may be reluctant to challenge Taiwan over perceived violations within the framework of the WTO since the organization would treat the two claimants as equals, which would be a humiliating exercise for Beijing.¹⁶ In fine, it would be difficult for Beijing to isolate and target "Taiwan" firms. Because so many of these firms have foreign partnerships, attempts by Beijing to punish or expropriate Taiwan businesses in China would invariably involve third-party nationals from countries China would prefer not to offend, including the United States, Japan, and Europe. Even if such an economic surgical strike against Taiwan were possible, the ripple effects of financial harm to the Asia-Pacific economies that depend on the good health of markets and suppliers in both Taiwan and China would be sufficient to raise international condemnation of China's economic coercion on strictly economic grounds, let alone political grounds.

Deepening cross-Strait trade and investment offers Taiwan the significant political benefit of creating a disincentive for war. China would suffer large financial losses in the disruption of commerce that a military conflict would cause. The threat of economic reversal is not guaranteed to deter Chinese action on a matter of national pride, but every decision is a matter of weighing costs against benefits.

The basic fear of many in Taiwan is that unchecked economic interchange will lead to China swallowing Taiwan politically, as the Chinese hope. This logic, however, is questionable. Strong economic and cultural ties do not necessarily lead to strong political ties. Political barriers in Western Europe have eroded, but elsewhere in the world can be found many bilateral relationships in which economic cooperation is very strong but there is little or no interest in a political merger. In the Taiwan Strait, more than a decade of growing economic exchange and social contact has not hastened political integration, which is virtually nil. Indeed, political negotiations have been frozen since 1999. Functional spillover may well be harder to achieve when political integration is the ostensible ultimate aim. When the focus is on economic interaction for its own sake, political integration may occur quietly without fully mobilizing its opponents. But if economic integration is acknowledged at the outset as a means toward attaining unification, politics will interfere with even the initial technical steps. Such appears to be the case in the Taiwan Strait.

The forces urging Taiwan toward political integration with the mainland, including cross-Strait trade and investment, are in competition with the forces that tend to solidify Taiwan's political separation from China. It is far from clear that the former will prevail over the latter. The generation of Taiwan residents with the greatest attachment to China and the greatest commitment to unification, the group of some two million mainland Chinese who moved to Taiwan in the late 1940s, is shrinking, giving way to an overwhelming majority who were born on Taiwan. The human contact between people from Taiwan and the mainland reinforces their cultural and in some cases family bonds, but also reaffirms that China and Taiwan have differing political cultures. Chinese tend to be collectivist, have little experience with democracy, and are accustomed to a low degree of public accountability for their leaders. By contrast, Taiwan's people are more individualistic and have decades of experience with democratic activism dating back to the struggle for self-rule while Taiwan

was under a Japanese colonial administration. Democratization in China could potentially narrow this gap in political culture across the Strait. Taiwan's political liberalization, however, is decades ahead of China's. Increasing wealth and the marketization of Chinese society are likely to bring about some form of political liberalization in the future. But the obstacles to democratization in China are daunting and preclude this outcome in the short term.

Chao Chien-min argues that "as commercial ties continue to ascend, political ties are stagnant and in some cases even retrenching." To support his assertion, Chao points to opinion polls that show a substantial decrease in key barometers of unification sentiment in Taiwan in recent years. The percentage of Taiwan people who favor eventual unification has dropped from nearly 70 percent to below 20 percent. Those who identify themselves as "Chinese" have dropped from a high of about 30 percent to less than 10 percent, while those who considered themselves "Taiwanese" have risen from less than 20 percent to nearly 50 percent.¹⁷

Conclusions

If there are not, on balance, strong reasons for Taiwan to resist deepening its economic ties with China, what drives the continued resistance? Taiwan's opposition to economic integration with China primarily arises from two political fronts. First, Taipei has hoped to win a substantial concession from Beijing in exchange for establishing direct links, such as renouncing the use of force, agreeing to treat Taipei as an equal, or dropping the insistence on Taiwan accepting the one-China principle as a pre-condition of cross-Strait talks. Up to now Taipei has not been successful and is therefore loathe to formally and fully accede to a Chinese demand without getting something in return.

The second basis of opposition is the intense public response to all matters involving China. The domestic political climate in Taiwan inhibits a cool-headed cost-benefit analysis of trade with and investment in China strictly on its merits. Since the single greatest political issue in Taiwan today is the island's ultimate political relationship with China, it is not surprising that this larger question, laden with onerous ethnic and political baggage, forms the context for thinking about cross-Strait economic relations. Taiwan's relationship with China is a bitterly divisive question that sparks accusations of treason between one-China proponents and Taiwan independence advocates. Linking the cross-Strait economics issue with these bitter domestic squabbles makes careful assessment by the public more difficult. Much of the opposition in Taiwan to deepening cross-Strait economic interaction appears to be based at least partly on emotional arguments rather than sound economic and political analysis. Thus, the most important political implication of cross-Strait economic relations may be that politics often acts to prevent thoughtful analysis of this important issue. Such analysis might reveal a great upside for Taiwan: that cross-Strait trade and investment do not put the island at risk of involuntarily losing its autonomy, and at the same time offer the important benefit of giving China hope of success through a strategy other than the threat or use of military force.

Cross-Strait economic exchange will continue, but uncertainties surround Taipei's attempts to manage this exchange: what limitations Taipei will impose, what national goals it will seek to achieve through the opportunities presented by economic cooperation with China, and how effective Taiwan's leadership will be in achieving those goals and in ensuring that the bilateral relationship is on balance beneficial to Taiwan.

Taiwan's ambivalence on the cross-Strait economic issue is another manifestation of the island's unsettled identity and the unresolved question of Taiwan's political destiny. In addition to its existential implications for

Taiwan, the question of Taiwan's political future generates the largest and most intractable problem in U.S.-China relations and is by far the clearest foreseeable cause of a possible military conflict between China and the United States.

If trade and investment across the Strait served to decrease the chances of war by strengthening China's stake in a peaceful political environment or by assuaging China's fears that Taiwan might be drifting toward independence, increased cross-Strait economic interaction would support America's interests in peace in Northeast Asia and a constructive working relationship with the PRC.

Discussion of other possible outcomes is largely speculative because of imponderable variables. On one hand, cross-Strait economic cooperation could help fulfill Beijing's wishes of unification by creating an economic dependency and perhaps even by weakening Taiwan's economy to such an extent that supporters of Taiwan independence lose their influence. On the other hand, and no less likely, embracing economic cooperation with China could be a means whereby Taiwan could retool and reinvigorate its economy and increase its security. If Taiwan businesspeople and their children are at risk of being Sinicized through their association with the mainland, there is also potential for the reverse: increased grassroots pressure for liberalization in China as a result of contact with people from richer and more democratic Taiwan, as well as a greater understanding among Chinese of the Taiwan mindset (including Taiwan's separate identity and the rationale for independence) and perhaps a diminution of the willingness to fight a war over Taiwan's international status.

The net impact of cross-Strait trade and investment on the unification question is therefore impossible to reliably assess in 2004. Increased economic cooperation, does, however, appear to offer hope of contributing to a political solution of the Taiwan issue agreeable to people on both sides of the Strait, which is in line with stated U.S. policy.

Dr. Denny Roy is a Senior Research Fellow in the Research Division at the Asia-Pacific Center for Security Studies. His work focuses on Asia-Pacific security issues involving China, particularly traditional military-strategic matters, foreign policy, international relations theory and human rights politics. Roy was previously a faculty member in the National Security Affairs Department at the Naval Postgraduate School in Monterey, California. He was also a research Fellow with the Strategic and Defence Studies Center at the Australian National University in Canberra. Roy has held faculty appointments at the National University of Singapore and Brigham Young University. He has five years of work and residency experience in Taiwan, Korea and Singapore.

*Roy is the author of *China's Foreign Relations* (Macmillan and Rowman & Littlefield, 1998) and *Taiwan: A Political History* (Cornell University Press, 2003). He is co-author of *The Politics of Human Rights in Asia* (Pluto Press, 2000) and editor of *The New Security Agenda in the Asia-Pacific Region* (Macmillan, 1997). He has also written many articles for scholarly journals such as *International Security*, *Survival*, *Orbis*, *Asian Survey*, *Security Dialogue*, *Contemporary Southeast Asia*, *Armed Forces & Society*, and *Issues & Studies*. Roy's recent contribution to the *Asia-Pacific Security Studies* series is "U.S.-Taiwan Arms Sales: The Perils of Doing Business with Friends" (April 2004).*

Notes

1. Cited in Chen-yuan Tung, “General Analysis of the Economic Relations between Taiwan and China—The Tradeoff between Economics and Security,” Association of Chinese Political Studies conference on “China Entering the New Millennium,” Washington, D.C., November 6–7, 1999, 41.
2. Zhu Weidong, “New Trend of Cross-Strait Relations in the New Century,” *Liaowang* (Beijing), no. 3, January 17, 2000, 7.
3. Samuel P. Huntington, *The Clash of Civilizations and the Remaking of World Order* (New York: Simon and Schuster, 1998).
4. Liao Yi and Xiang Jianguo, “State Council Taiwan Affairs Office Spokesman Answers Journalists’ Questions on Cross-Strait Relations,” *Xinhua*, September 26, 2001.
5. Karen M. Sutter, “Business Dynamism across the Taiwan Strait,” *Asian Survey* 42, no. 3 (May/June 2002): 523.
6. Luis Huang, “Taiwan Should Diversify Markets to Reduce Reliance on Mainland: MOEA,” Central News Agency, November 6, 2003.
7. Sutter, 528–29.
8. For a recent reaffirmation, see Taiwan Affairs Office of the State Council, “Actively and Realistically Promote ‘Three Direct Links’ across the Taiwan Strait by Reliance on the People and in the Interests of the People,” December 17, 2003, http://english.peopledaily.com.cn/200312/17/print20031217_130608.html.
9. Laurence Eyton, “Cross-Strait Links Possible. No, Really,” *Asia Times*, September 17, 2003, <http://taiwansecurity.org/News/2003/AT-091703.htm>, accessed November 5, 2003.
10. Sophia Wu, “Taiwan Military Doesn’t Rule Out Pre-emptive Attack on Mainland: Tang,” China News Agency, October 8, 2003.
11. *China Times* report, March 19, 2002; Chyan Yang and Shiu-Wan Hung, “Taiwan’s Dilemma across the Strait: Lifting the Ban on Semiconductor Investment in China,” *Asian Survey* 43, no. 4 (July/August 2003): 691.
12. Xinhua report, Hong Kong, September 2, 1998.
13. Tung, 21.
14. Robert Rowthorn and Ramana Ramaswamy, *Deindustrialization—Its Causes and Implications*, Economic Issues 10, International Monetary Fund, Washington, D.C., 1997.
15. Tung, 43n.
16. Sutter, 538.
17. Chien-min Chao, “Will Economic Integration between Mainland China and Taiwan Lead to a Congenial Political Future?” *Asian Survey* 43, no. 2 (March/April 2003): 289–90.



The Asia-Pacific Center for Security Studies (APCSS) is a regional study, conference, and research center established in Honolulu on September 4, 1995, complementing PACOM’s theater security cooperation strategy of maintaining positive security relationships with nations in the region. The APCSS mission is to enhance cooperation and build relationships through mutual understanding and study of comprehensive security issues among military and civilian representatives of the United States and other Asia-Pacific nations.

The Occasional Paper Series contributes to the APCSS mission to enhance the region’s security discourse. The general editor of the series is Lt. Gen. (Ret.) H.C. Stackpole, President of the APCSS. The views expressed in this publication are those of the author(s) and do not necessarily reflect the official policy or position of the APCSS, USCINCPAC, the U.S. Department of Defense, or the U.S. Government.

www.apcss.org