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A Political Analysis of Taiwan's Economic Dependence on Mainland China

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This article argues that an analysis of the political impact of Taiwan's economic dependence on mainland China should be put into a broader spectrum of the international division of labor. The traditional wisdom of economic statecraft holds that economic dependence may increase the chance of economic sanctions from hostile nations and thus endanger national security. However, in the era of economic globalization, unilateral economic sanctions are rarely effective. This article examines whether the cross-Strait economic interaction is "asymmetric" or "interdependent." Due to the introduction of such international factors as strategic business alliances and multinational cooperation, it is difficult to identify businesses of the target country while imposing sanctions. To guarantee national security, the Taiwanese state has to adjust its role to promote internationalization and create a comprehensive division of labor with the other side of the Taiwan Strait.

Keywords: cross-Strait relations; economic sanction; foreign direct investment; multinational corporations; national security

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This paper examines the impact of economic dependence on Taiwan's economic policy toward mainland China. Since the lifting of trade and investment restrictions in 1987, Taiwan has adopted a more prudent policy

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of indirect economic transaction with mainland China. This prudence is based on the fact that political rivalry between Taipei and Beijing still exists and Taiwan's economy has gradually become dependent on mainland China. Hence, despite the attacks from Beijing and Taiwan's business community, Taipei still insists on gradualism in further opening up cross-Strait economic relations.

However, whether Taiwan's "economic dependence" will open the door for future economic sanctions from mainland China requires more thorough discussion. In this paper, the author intends to examine whether cross-Strait economic transactions are asymmetric or mutually beneficial and will also discuss the impact of economic globalization on the state's capacity to utilize political means, such as economic sanctions, to influence trade and investment. This paper will first review current Taiwan policies regarding cross-Strait trade and investment, and then follow with an analysis of the economic interdependence between Taiwan and mainland China. The author will also put cross-Strait economic relations in the broader spectrum of the international division of labor and cross-national cooperation. After reviewing all these factors, the impact of economic dependence on Taiwan's relations with mainland China can be clarified.

Taiwan's Policy Toward Mainland China in the Shadow of Economic Dependence

From an economic perspective, cross-Strait economic relations are asymmetric. Since the opening of legal indirect trade and investment in 1987, Taiwan has enjoyed a large trade surplus with mainland China. At the same time, shares of exports to mainland China in Taiwan's total exports have also been on the rise—from 2.28 percent in 1987 to 18.39 percent in 1997. Table 1 shows the evolution of Taiwan's economic dependence on mainland China. These rates would be even higher if trade through Hong Kong was included.[1] Mainland China's export dependence

[1]For a detailed explanation of counting cross-Strait trade value, see Tse-Kang Leng, *The*

Table 1
Economic Interdependence Between Taiwan and Mainland China

Year	Value of Taiwan's Exports to Mainland China (US$ millions)	Share of Exports to Mainland China in Taiwan's Total Exports (%)	Value of Mainland China's Exports to Taiwan (US$ millions)	Share of Exports to Taiwan in Mainland China's Total Exports (%)
1987	1,226.50	2.28	–	–
1988	2,242.20	3.70	–	–
1989	3,331.90	5.03	–	–
1990	4,394.60	6.54	319.70	0.51
1991	7,493.50	9.84	594.80	0.83
1992	10,547.60	12.95	693.50	0.82
1993	13,993.10	16.47	1,461.80	1.59
1994	16,022.50	17.22	2,242.20	1.85
1995	19,433.80	17.40	3,098.10	2.08
1996	20,727.30	17.87	2,802.70	1.86
1997	22,460.30	18.39	3,915.40	2.14

Sources: *Liang'an jingji tongji yuebao* (Monthly Report of Cross-Strait Economic Statistics) (Taipei, Mainland Affairs Council), February 1997, 24, 26; *Jinchukou tongji yuebao* (Monthly Statistics of Exports and Imports, Taiwan Area, ROC) (Taipei, Ministry of Finance), February 28, 1998, 10; *Renmin ribao* (People's Daily), January 22, 1998; data from the ROC Ministry of Economic Affairs.

on Taiwan, however, is relatively small.

Given this situation, national security has become a main concern for Taiwan's mainland economic policy makers. Their basic perception is that mainland China is trying to "use economic interaction to force political concessions" and "push the business community to influence the Taiwan government."[2] High economic dependence may lead to capital outflow to mainland China, decrease domestic investment, and expose Taiwan to the mainland's political interventions. The combination of this high economic dependence and the escalation of political confrontation since 1995 has led ROC President Lee Teng-hui to request the business community to be *jieji*

Taiwan-China Connection: Democracy and Development Across the Taiwan Straits (Boulder, Colo.: Westview Press, 1996), 110.

[2]Lien Chan, "Government Work Report to the Legislative Yuan" (September 6, 1996).

yongren (cautious and self-restrained).[3]

The ultimate goal of *jieji yongren* is to regulate Taiwanese investments of big enterprises and high-tech industries in mainland China. Under this guidance, the Taiwan government has attempted to minimize the negative impacts on domestic development and gradually release restrictions on investment. In May 1997, the Ministry of Economic Affairs (MOEA) released a set of new criteria for rating "special cases" categories of investment projects. For example, if the industry is labor-intensive and less competitive in the international market, the chance of being approved to invest in mainland China is higher. By the same token, approval is more likely if firms have more investments in Taiwan's domestic market and international market than mainland China, or have accumulated investment capital from the international market rather than Taiwan's domestic market.[4] According to these criteria, economic bureaucracies quantify the suitability of each investment project. Moreover, new criteria have set the ceiling for any single investment project at US$50 million. This new set of regulations is based on the hope that Taiwanese investment in mainland China will be used as an instrument to transfer outdated technologies and labor-intensive industries. Under these new criteria, larger investment projects having "reverse" impacts on Taiwan's international competitiveness and domestic investment are greatly constrained.

Hence, Taiwan's economic policies toward mainland China cannot be fully understood through cost-benefit analysis. Due to political risk concerns, the state has tried to take part in the booming economic relationship and "apply the brakes" to protect national security. Three official principles have been declared in regard to governing cross-Strait economic interactions. The first principle is balance between national security and economic benefit: the Taiwan government will open up economic interactions step by step, depending on the political situation across the Taiwan Strait. The second principle is national interest: the main concern in promoting cross-Strait economic relations is Taiwan's economic autonomy and its

[3]Lee Teng-hui, "Opening Remarks at the Third Conference on Business Management" (Taipei, September 14, 1996).

[4]*Zhongyang ribao* (Central Daily News) (Taipei), May 29, 1997.

competitiveness in the international market. Economic relations with mainland China should thus enhance, rather than reduce, Taiwan's economic superiority. The third principle is stability: the long-term goal of Taiwan's economic policy toward mainland China is to promote long-term political stability across the Taiwan Strait.[5] Under these basic guidelines, issues such as the opening of direct trade, postal, and transportation links are under consideration, but as of yet have not been realized. Such ad hoc measures as "offshore transshipment centers" are being established, and a "National Development Conference" convened in late 1996 also urged the government to "prudently assess investment by large-scale Taiwanese firms and make reasonable standards for regulation."[6]

In contrast, mainland China's strategy is to utilize its economic attractiveness to thwart Taiwan's political intervention in Taiwanese business investment in the mainland. From mainland China's perspective, Taiwan's policy of economic gradualism is against the trends of regionalization and globalization. Taiwanese businessmen may also lose their advantage in competing with multinational corporations in the mainland market. Mainland leaders have, moreover, reiterated that the hope of unification is "invested in the general public on Taiwan"; political controversies should not influence economic cooperation across the Taiwan Strait.[7] The mainland government has also maintained a low profile, focusing on substantial efforts to attract Taiwanese investment without resorting to vocal propaganda.[8]

In brief, mainland China understands the economic importance of the mainland market to the Taiwanese business community, and is forming a bottom-up alliance to challenge Taiwan's current economic statecraft. As one major mainland propaganda machine indicates, strengthened economic exchanges and cooperation "will inevitably promote economic develop-

[5]Mainland Affairs Council (MAC), *Cross-Strait Relations and Economic Policies Toward Mainland China* (Taipei: MAC, 1997).

[6]*National Development Conference Resolutions* (Taipei: National Development Conference Secretariat, January 1997), 19-20.

[7]Jiang Zemin, "Promoting Peaceful Reunification," *Liang'an guanxi* (Cross-Strait Relations Monthly), October 1997, 2; *Renmin ribao* (People's Daily), January 27, 1998, 1.

[8]*Lianhe bao* (United Daily News) (Taipei), July 31, 1997, 9.

ment and prosperity, and the shared economic interests of both sides will in turn contribute to political unification. Cross-Strait cooperation will not only lay a firm economic foundation for China's reunification, but also boost economic development in the Asia-Pacific region and the whole world."[9] Thus, in contrast to Taiwan's pure realist perspective, mainland China is wrapping its realist policies in functionalist terms.

To summarize, political vulnerability has forced Taiwan to look at economic dependence and interdependence from an angle different from that of pure economic considerations. From Taiwan's perspective, mainland China's preferential treatment to Taiwanese businessmen results only from political concerns. The ultimate goals are to change the business community's attitude toward mainland China, form bottom-up pressure to open up comprehensive economic interaction, and finally achieve "mainlandization" through economic interdependence. Given the fact that Taiwan's economy is becoming gradually dependent on mainland China, Taiwan's bargaining chips will thus also decrease. In a worst-case scenario, as Taiwanese leaders indicate, mainland China could hold Taiwanese businessmen as "hostages," or punish Taiwan with economic sanctions. To decrease Taiwan's vulnerability, the most important task is to decrease economic dependence, especially in the high-tech sector and large-sized enterprises, on mainland China. These above considerations have created the need for the *jieji yongren* strategy.

Economic Dependence and the Threat of Economic Sanctions

Facing a political and military rivalry across the Taiwan Strait, Taiwan's prudence toward economic interaction is well grounded, as Taiwan's economic dependence may open the door for possible economic sanctions from mainland China. In reality, economic sanctions refer to the withdrawal of trade or financial transactions for the purpose of political coer-

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[9]"Taiwan Criticized for Imposing Obstacles on Cross-Strait Trade," *Beijing Review*, October 28-November 3, 1996, 8.

cion, and have long been regarded as a useful tool to press the target country for compliance. In other words, economic sanctions are used as coercive economic statecraft, which may influence economic costs and benefits of both the initiator and the target country. Scholars also indicate that economic sanctions may also serve as a middle road or surrogate to military actions.

In a groundbreaking study, Hufbauer, Schott, and Elliott classified economic sanctions according to foreign policy objectives into five categories: making modest changes to the target country's policies; destabilizing the target government; disrupting a minor military adventure; impairing the military potential of the target country; and making major changes to the target country's policies.[10] Thus, sanctions are used by the sending country to punish, to deter, and to rehabilitate. In addition, economic sanctions could also be used to demonstrate the resolve of the sending country. These moral and psychological instruments are imposed because the cost of inaction is seen as greater than the cost of sanctions. Economic sanctions are sometimes used as a surrogate for other measures. Sanctions provide a popular middle road, adding teeth to international diplomacy even when the bark is worse than the bite.[11]

However, Hufbauer, Schott, and Elliott's data indicates that the effectiveness of economic sanctions is limited (see table 2). Only 35 percent of the 115 cases they examined could be regarded as "successful." Moreover, the effectiveness of unilateral sanctions was even lower. From 1945 to 1990, the success rate of unilateral U.S. sanctions was only 29 percent. The success rate of U.S. unilateral sanctions in the post-1970 era declined sharply as compared to the pre-1970 era—from a 69 percent success rate to a 13 percent success rate.[12]

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[10]Gary Hufbauer, Jeffrey Schott, and Kimberly Elliott, *Economic Sanctions Reconsidered: History and Current Policy*, 2nd edition (Washington, D.C.: Institute of International Economics, 1990), 38.

[11]Kimberly Elliott and Gary Hufbauer, "New Approaches to Economic Sanctions," in *U.S. Intervention Policy for the Post-Cold War World*, ed. Arnold Kanter and Linton Brooks (New York: W.W. Norton, 1994), 134.

[12]Kimberly Ann Elliott, "Evidence on the Cost and Benefits of Economic Sanctions" (Testimony Before the Subcommittee on Trade of the House Committee on Ways and Means, October 23, 1997), 4.

Table 2
Effectiveness of Economic Sanctions as a Foreign Policy Tool

	Number of Successes	Number of Failures	Success Rate (%)
All cases	40	75	35
Cases involving U.S. as a sanctioner:			
1945-90	26	52	33
1945-70	16	14	53
1970-90	10	38	21
Unilateral U.S. sanctions:			
1945-90	16	39	29
1945-70	11	5	69
1970-90	5	34	13

Source: Kimberly Ann Elliott, "Evidence on the Cost and Benefits of Economic Sanctions" (Testimony Before the Subcommittee on Trade of the House Committee on Ways and Means, October 23, 1997), 4.

Moreover, scholars are still skeptical about the forty cases which Hufbauer, Schott, and Elliott claim to be "successful." A critical study on their data indicates that among these forty cases, only five could thus be claimed as "successful." Of the remaining cases: eighteen were determined by force, not economic sanctions; eight were failures in the sense that the target state never conceded to the coercer's demands; six were trade disputes rather than instances of economic sanctions; and the results of three were indeterminate.[13]

Since the collapse of the Cold War system in the late 1980s, forming an alliance of multilateral economic sanctions has become more difficult. In addition to the demise of ideological confrontation, another factor contributing to the ineffectiveness of economic sanctions has been the increasing trend of economic interdependence and globalization. This trend introduces two challenges to economic sanctions: first, the cost to sanctioning

[13]Robert A. Pape, "Why Economic Sanctions Do Not Work," *International Security* 22, no. 2 (Fall 1997): 99.

countries becomes more difficult to estimate. Except for extreme cases where the dependence is unidirectional (target country dependent on initiator), a nation wishing to impose sanctions on another also sanctions itself. Second, due to the international division of labor in economic affairs, the target country is becoming harder to define. Attacking the target may influence all the countries doing business with this target, and thus increase the international pressure to cease such coercive policies.

Finally, even though Taiwan is still wary of mainland China's intentions to use economic sanctions, this special kind of economic statecraft has important limitations. Successful sanctions must meet the following criteria:

1. The target country is much smaller than the country imposing sanctions, and economically dependent on the sending country.
2. The benefits of economic sanctions are greater than the cost.
3. The initiator country is successful in forming an international alliance for sanctions.
4. The initiator is able to regulate the business community to undertake bilateral trade and financial transactions.

All these four criteria are closely related to economic dependence and economic internationalization. If Taiwan's external trade relations continue to be heavily dependent on mainland China and cross-Strait economic transactions remain "bilateral" in nature, this asymmetric relationship is indeed potentially dangerous to Taiwan.

Coping with Economic Dependence

The first strategy to escape from economic dependence is to find alternatives to replace the mainland market. A possible alternative location for Taiwanese investment is Southeast Asia. Since the announcement of Taiwan's "southward" policy in 1994, this government-led movement has been regarded as leverage to balance the "westward" trend of investing in mainland China.

As compared to society-led investment activities, southward policy has strong official support. Taiwan's large-sized enterprises have also taken the lead in marching into this region. In 1994, the MOEA released a three-year plan which included many investment projects led by both state- and KMT-owned enterprises such as Taiwan Sugar, Taiwan Salt, Chinese Petroleum, and Central Investment corporations.[14] To show support for the new policy, many large-sized enterprises, such as the President and Tuntex groups, also initiated new projects in this region. More importantly, waves of investment fever have also coincided with the "ice-breaking" or "peace" trips of Taiwan leaders to Southeast Asian countries.

Given the recent economic turmoil in Southeast Asian countries, the Taiwan government has taken the opportunity to revive investment fever and expand diplomatic influence in the region. For example, a new "Action Plan to Promote Economic Cooperation with Southeast Asian Countries" was released in March 1998. This plan intends to set up a controlling company to manage investment, improve the financing of Taiwanese businessmen in the region, and enhance bilateral cooperation in economic affairs.[15] China Development, a KMT-supported company, recently announced the purchase of a 50 percent stake in Bangkok First Investment & Trust, an affiliate of Bangkok Bank, for US$14.8 million.[16]

However, private enterprises' reactions toward the southward policy during the recent economic turmoil have been mixed. For instance, manufacturing investors have been less than enthusiastic because they lack the management skills to take over shaky firms. More importantly, many companies with experience in the region have stated that they would prefer to be in mainland China, as the productivity of Chinese workers is higher and trainable managers are easier to recruit.[17] In a recent case, Kao Ching-yuan, CEO of Taiwan's President Group, announced the suspension of projects worth US$20 billion in the Philippines before leaving Taiwan to

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[14]*Jingji ribao* (Economic Daily) (Taipei), January 14, 1998, 3.
[15]*Gongshang shibao* (Commercial Times) (Taipei), March 6, 1998, 3.
[16]Julian Baum, "On the Prowl," *Far Eastern Economic Review*, April 2, 1998, 49.
[17]Ibid.

Table 3
Taiwanese Investment in Southeast Asia, 1987-97

Unit: US$ millions

	Singapore	Thailand	Malaysia	Indonesia	Philippines	Vietnam
1987	1.30	5.37	5.83	0.95	2.64	–
1988	6.43	11.89	2.71	1.92	36.21	–
1989	5.21	51.60	158.65	0.31	66.31	–
1990	47.62	194.40	184.89	61.87	123.61	–
1991	12.54	86.43	442.01	160.34	1.32	17.14
1992	8.79	83.29	155.73	39.93	1.22	20.17
1993	69.47	109.17	64.54	25.53	6.54	158.40
1994	100.73	57.32	101.13	20.57	9.60	108.38
1995	31.65	51.21	67.30	32.07	35.72	108.15
1996	164.98	71.41	93.53	82.61	74.25	100.48
1997	230.31	57.55	85.09	55.86	127.02	85.41

Source: ROC Ministry of Economic Affairs.

join CEPD Chairman P.K. Chiang's delegation to that region.[18] The President Group has extensive investment projects in Southeast Asia, and is also the number one investor in mainland China.

Table 3 shows the trends in Taiwanese investment in Southeast Asia over the past few years. Investment has generally increased since 1992, but there has been fluctuation in some countries, such as Thailand and Malaysia. The sharp decrease of investment value in 1997 is obviously due to the financial crisis in Southeast Asia, and demonstrates that regional unpredictability and instability could be major factors impeding further Taiwanese investment. In contrast, Taiwanese investment in mainland China has maintained constant growth, even under such pressures as the international sanctions imposed in the wake of the Tiananmen Square event of June 1989.

From an economic perspective, mainland China is a natural choice for Taiwanese businessmen. If we only look at the statistics, Taiwan's exports are indeed heavily dependent on mainland China. However, cross-Strait

[18]*Zhongguo shibao* (China Times) (Taipei), January 12, 1998, 4.

economic interactions are composed of both investment and trade. Compared to pure trade, home country investment has greater social and economic impacts on the host country. Furthermore, cross-Strait trade is in large part investment-driven, which means that most Taiwanese exports to mainland China are utilized by Taiwanese firms. This implies that the true dynamism of cross-Strait economic interaction is investment, not just trade.

The other side of the coin of Taiwan's economic dependence is that mainland China also needs Taiwan. In some way, "dependence" may also imply interdependence. When mainland China opened its doors to the outside world in the early 1980s, Taiwanese investment provided necessary capital and technology for the mainland's export-oriented industries, especially labor-intensive industries. These "sunset" industries in Taiwan are mainland China's "sunrise" industries. In other words, Taiwan's investment in mainland China since the 1980s has been business-led and based on mutually beneficial economic interactions. Moreover, Taiwan's exports to mainland China are in reality investment-driven; that is, they support Taiwanese investment in mainland China. Rather than commodity goods, the majority of Taiwanese exports to mainland China are semifinished materials and equipment. These goods are utilized by Taiwanese firms in China's coastal areas and then reprocessed for export to the world market. From this perspective, Taiwan's large trade surplus with mainland China should not be regarded as a kind of pure trade dependence. It is a part of China's dynamic export-oriented industries, which have supported China's sustained growth since the early 1980s.

Table 4 shows the Taiwanese investment in mainland China from 1985 to 1996. Due to the fact that the Taiwan government did not allow legal indirect investment until 1991, pre-1991 investment from Taiwan was relatively low. In addition, a large portion of "Hong Kong investment" is from the Taiwan business community. In order to avoid legal restrictions from the government, a large amount of Taiwanese capital enters the mainland market under the umbrella of "Hong Kong investment." Hence, it is not easy to distinguish investments from Taiwan and Hong Kong. It is believed that the real share of Taiwanese investment in mainland China's total foreign direct investment (FDI) should be higher than the reported 8.4 percent.

Table 4
Foreign Direct Investment Flows to China, by Origin, 1985-96

	Total (US$ millions)	Share (%)
Hong Kong & Macau	102,000	58.0
Taiwan	14,703	8.4
Japan	14,082	8.0
United States	13,885	7.9
South Korea	4,334	2.5
United Kingdom	3,419	1.9
France	1,265	0.7
Italy	963	0.5
Total including others	175,733	100.0

Source: *EIU Country Profile, 1997-98* (London: EIU, 1997), 52.

Taiwanese investment has also made certain contributions to mainland China's economic development. Calculated from the 1995 data, these contributions can be found in the following perspectives. First, Taiwanese investment has created 3.9 million job opportunities, or about 2.2 percent of mainland China's nonagricultural employment. Second, the manufacturing output of Taiwanese firms has reached US$33.57 billion, or about 3.1 percent of mainland China's gross industrial output value. Third, Taiwanese enterprises have created an export value of US$21.44 billion, or about 14.4 percent of mainland China's total export value.[19] In addition to these quantitative contributions, Taiwanese investment has brought in invisible influences such as marketing and management skills to Chinese industries. Moreover, the influence of Taiwanese enterprises has not been just limited to the coastal areas. A large portion of factory workers in Taiwanese firms is from inland provinces such as Sichuan and Hunan. These expansion effects will bring economic benefits as Taiwanese firms become more integrated into mainland China's economic development. It may be premature to say that Taiwan and mainland China have formed a relation-

[19]Charng Kao, "Taiwanese Investment in Mainland China and Its Impacts on Mainland's Economy," *Jingji qingshi yu pinglun jikan* (Review of Economic Situation), internet edition, May 1997, 2-4.

ship of economic interdependence, but claims of "statistical dependence" should certainly be examined more thoroughly.

Economic Globalization and Economic Dependence

The globalization of firms has rendered it more difficult for both sides of the Taiwan Strait to effectively control capital and trade flows. Traditional mercantilist thought presumes that states can control private firms, and thus use economic relations as a leverage to protect national interests. Nowadays, globalized firms cannot be easily "used" by any single country. Internationalization may twist or alleviate the political effects of economic dependence because firms have gradually become more independent.

Taiwanese investment in mainland China is also a part of the global trend of economic internationalization. As stated earlier, the Taiwan government prohibits the investment of high-tech and infrastructure industries in mainland China. However, Taiwanese firms have adopted strategies of international operation to escape from government regulations. For instance, Taiwanese capital can be found in the Nanjing-Wenzhou railway project in mainland China. The Acer group has also utilized its subsidiaries in Malaysia to invest in CD-ROM factories in Suzhou through technology transfers.[20] Since technology transfers through a third country is not clearly prohibited by current Taiwanese policies, this kind of internationalization strategy has thus taken advantage of the gray areas in legal restrictions.

Another strategy used by Taiwanese enterprises has been to obtain capital in the international capital market to support their mainland projects. The favorite places for this type of fund-raising activity by Taiwanese business communities are Singapore and Hong Kong. Wong-Wong Cookies Company, the biggest Taiwanese company of this kind in mainland China, has accumulated more than US$63 million from the Singaporean stock market. Even though Hong Kong has been an integral part of China since July 1, 1997, many Taiwanese companies are optimistic about

[20] *Jingji ribao*, March 23, 1998.

its highly liberalized capital market and are utilizing Hong Kong as a base of financial management.[21] Other multinational corporations such as Formosa Plastics have used their branch companies or subsidiaries in a third country to undertake projects in mainland China. Moreover, Taiwanese investors can bring their capital out of Taiwan by transferring the foreign exchange earned from exports. Exporters sometimes retain their foreign exchange to invest in mainland China, and a large portion of this flows directly into China, with Taiwan being unable to control the capital outflow.[22] In reality, if the investors own dual nationality and do not have Taiwan residence status, their investment activities are outside legal restrictions.[23]

Another example of internationalized firm behavior is Formosa's power plant project in Zhangzhou, Fujian province. When Formosa's Y.C. Wang announced the project in mid-1996, it caused a major shock to Taiwan's mainland economic policies. However, in this US$3 billion investment, the mother company would only contribute US$400 million, or approximately 14 percent of the total. Formosa's overseas subsidiaries will play the major investor role, while international banks, including Japan's Mitsubishi and Sumitomo and several German banks, had expressed interest in loaning more than US$2 billion.[24] In other words, major financial support would have been from international rather than domestic sources. According to the reviewing rules of the MOEA Investment Commission, Taiwanese companies' foreign subsidiaries can freely invest in mainland China without reporting to the government if the mother companies' stock share does not exceed 20 percent. In the Formosa case, the mother company holds only 10.6 percent of the stock.[25]

Although Wang finally submitted the investment project to the government for review, he himself later withdrew the proposal under pressure

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[21]Ibid., March 3, 1997.

[22]Leng, *The Taiwan-China Connection*, 114.

[23]According to the current Nationality Law in Taiwan, maintaining dual nationality is permitted by law.

[24]*Zhongguo shibao*, July 9, 1996.

[25]*Zili zaobao* (Independence Morning Post) (Taipei), May 29, 1996.

from the MOEA. However, as in the Haicang case, this project has not come to a stop; Wang has made it clear that the Zhangzhou project will not be used to "support the Chinese Communist bandits," claiming that he intends to give most support to Taiwanese companies in mainland China, import most equipment from Taiwan, and enhance Taiwan's international competitiveness through an economic division of labor with mainland China. In March 1998, Wang announced that Formosa planned to sell the ownership of the Zhangzhou factory to foreign companies. Once the restrictions of the Taiwan government are lifted, Formosa will buy back the factory. According to the MOEA, such moves "do not go against the current policy."[26]

Unilateral Dependence and International Strategic Alliances

Economic dependence may endanger national security if countries take advantage of this unique relationship and initiate economic sanctions. However, unless a multinational alliance of imposing sanctions is created, unilateral sanctions rarely work. On the other hand, if the target country's investment has close ties with multinational firms, the "target" of attacking such investment becomes ambiguous. Under such a situation, the coercer has to be cautious in using economic sanctions even though the target country's investment is dependent economically on the sending country.

The forming of strategic alliances has been a recent trend of cooperation among firms. In the new world of economic globalization, individual firm boundaries have become fuzzier as their sphere of influence over the management of resources has been extended to embrace a variety of cooperative arrangements and network agreements. The new constellation of strategic alliance is a loosely coupled system characterized by coordinate specialization in the production of goods and services, as informal contracts govern the behavior of individual members, without any one domi-

[26] *Lianhe bao*, March 31, 1998.

nant member, and negotiation and consensus-building take place before collective action.[27]

One major stimulus of the strategic alliances between Taiwanese and international firms has been the opening up of mainland China's domestic market. In the early stages of Taiwanese investment, small and medium-sized firms relocated their business wholly or partially to mainland China, and utilized the mainland's cheap labor and land costs to process their commodity goods for the international market. These small and medium-sized firms were Taiwan's pioneers of export-led growth in the 1960s and 1970s, and then became Taiwan's first explorers of the mainland market in the late 1980s. In contrast, large-sized enterprises have focused on Taiwan's domestic market in the past few decades, and their plans for mainland China were not realized until mainland China gradually opened its domestic market in the mid-1990s.

Rather than competing with multinational corporations (MNCs), some Taiwanese firms have worked instead to be a bridge between foreign firms and mainland China's domestic companies. Due to cultural and linguistic differences, MNCs sometimes have encountered difficulties in utilizing mainland China's resources. Allying with Taiwanese firms can help resolve these difficulties and enhance their bargaining power through collective actions. Furthermore, mainland China's "investment protection agreement" with foreign countries can also serve as an indirect umbrella for strategic alliances.

In fact, as a part of the Asia-Pacific Regional Operations Center, the Taiwan government has taken initiatives to promote the forming of international strategic alliances. However, these efforts have been limited to attracting MNCs in order to invest and transfer know-how technologies to Taiwan's domestic soil. Due to the constraints of current policies, the government does not intervene in strategic alliances among private firms formed to attack the mainland market. Hence, strategic alliances between

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[27]For a more detailed discussion of theories of strategic alliance, see Paul Vaaler, "Twilight of the Multinational Firms," *The Fletcher Forum of World Affairs* 22, no. 1 (Winter/Spring 1998): 117-23; John Dunning, *Alliance Capitalism and Global Business* (New York: Routledge, 1997).

Taiwanese firms and MNCs are in large part a result of private efforts. According to various surveys, most Taiwanese strategic alliances concentrate in the fields of transportation tools and food industries. As stated earlier, these industries are domestic rather than export-oriented. The natural choice for an investment site for the domestic market is Shanghai, which offers a huge consumer population in the Yangtze River delta.[28] A typical alliance would involve Taiwanese firms providing marketing and production capacities and MNCs offering technologies and capital. Furthermore, since strategic alliances focus on mainland China's domestic market, foreign brand names are crucial for success. The use of Taiwanese marketing and production methods can have helped to successfully market these brands in China.

Multinational companies can also play a role in integrating enterprises on both sides of the Taiwan Strait. Many MNCs have investment projects on both sides, and thus have indirectly created a vertical and horizontal division of labor between Taiwan and mainland China. For example, Xian Yangson, a joint venture with Johnson & Johnson, has conducted technology cooperation with Taiwan's counterparts via its mother company.[29] Under the coordination of the American company, a joint project incorporating Japanese, American, Chinese, and Taiwanese companies was realized in 1997. The Taiwanese partner is Han-hsiang, a government-supported aviation company. In an S-92 Hellibus helicopter project, Taiwan will invest 6 percent, while the mainland company will contribute 2 percent of the share. According to the plan, the Taiwanese division is responsible for the nose, the mainland division for the tail, the U.S. division for the engine, and the Japanese division for the main body.[30] Such international division of labor makes political interventions more unlikely, as the "target" of political coercion becomes more difficult to define.

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[28]Fengshuo Yang, "An Analysis of Taiwanese Investment in Mainland China by Strategic Alliances," *Jingji qingshi yu pinglun jikan*, internet edition, November 1996, 3-5.

[29]*Gongshang shibao*, December 27, 1997, 7.

[30]*Lianhe bao*, October 15, 1997, 9.

Alternatives to Economic Sanctions: The Business Community as the Source of Pressure

The escalation of the business community's autonomous role may alleviate the political effects of economic coercion, but this autonomy is a double-edged sword. In many cases, the Taiwan business community has pressed the government to further open up economic interactions with the lucrative mainland China market. In effect, the host country receiving FDI does not need to "lobby" the home country for lifting the restrictions, as the home country's business community itself is the best spokesman.

The issue of China's most-favored-nation (MFN) status in the United States is a representative example. A coalition of trade associations, lawyers, and corporate officials was formed for the perennial battle to assure that China continues to receive MFN benefits. The leading organization of the "New China Lobby" is the ad hoc Business Coalition for U.S.-China Trade coordinated by the Emergency Committee for American Trade, a bloc of fifty-five major U.S. companies committed to free trade, including General Motors, Mobil, Exxon, Caterpillar, United Technologies, Boeing, Cargill, Philip Morris, Procter and Gamble, TRW, Westinghouse, IBM, and a few dozens more. As one leading public relations firm in Washington, D.C. indicates, this business coalition, which has credibility and influence over public opinion, can be a critical component of China's communication program. This coalition can also be organized into a force for change.[31]

The Seattle-based Boeing Company plays a crucial role in this alliance. Today more than 60 percent of China's airliners are Boeing-built, and China is expected to order an additional 1,900 commercial jets worth US$124 billion over the next twenty years. Overall, the China deal accounts for about 14 percent of Boeing's commercial aircraft orders.[32] Fifteen of Boeing's two-dozen staff lobbyists work the China beat, more than on any other issue, contacting lawmakers and executive agencies. Moreover, Boeing has launched a massive grass-roots effort to drum up support

[31]Robert Dreyfuss, "The New China Lobby," *The American Prospect*, January/February 1997, 30-37.

[32]*Asian Wall Street Journal*, May 27, 1994.

among thousands of small business whose fortunes are as tied to China as their own. Boeing alone has 40,000 suppliers located in virtually every state in the United States.[33]

These spontaneous lobbying activities are market-driven. Thus, the mainland government does not need to "pursue" these corporation officials to speak on its behalf, as the mainland market is in fact the biggest spokesman for the Chinese government. Earlier discussion indicates that the real target of Taiwan's *jieji yongren* policy is Taiwan's large-sized enterprises. However, as mainland China gradually opens its domestic market, the anxiety of these enterprises is also on the rise. In addition to Formosa's challenge to the current policy, leaders of individual industries have also launched attacks on the Taiwan government's policy of restraint. The business community argues that without the "three direct links," Taiwanese firms will not be able to compete with foreign companies on the mainland market. They have also indicated that even under the current "three links" prohibition, Taiwan's economic dependence on mainland China is also increasing annually. Thus, it is obvious that cross-Strait economic interaction is becoming an "economic" issue, not a political one.[34]

The pressure to further ease restrictions on mainland trade also comes from business leaders who have important political connections with the government. Kao Ching-yuan argues that the Taiwan government should open all industries (except military-related ones) to invest in mainland China. Kao is the head of the Chinese National Federation of Industry (Taiwan) and a member of the KMT Central Standing Committee. Another tycoon who has pushed hard to open direct commercial and transportation links is Chang Rong-fa, the owner of the Evergreen Group, which operates the biggest cargo fleet in the world. He indicates that under the current policy, business opportunities will slip away and foreign firms will occupy the biggest slices of the mainland market. He has even offered to serve as a special envoy between Taiwan and mainland China.[35] Given the fact

[33]*The News Tribune*, May 12, 1997.
[34]*Lianhe bao*, March 27, 1998.
[35]*Zhongguo shibao*, October 15, 1997.

that Chang has an especially good relationship with the Taiwan government and President Lee Teng-hui, challenges from the Evergreen Group have been a major shock to the government's economic policies toward mainland China.

Conclusion

Economic dependence on mainland China has brought Taiwan's decision-makers face to face with a dilemma. From an economic perspective, the mainland market is a natural location for Taiwanese investment. In reality, if one subtracts the trade surplus with mainland China enjoyed since the late 1980s, Taiwan's foreign trade would run at an overall deficit rather than a surplus. However, political and military tensions across the Taiwan Strait have forced the Taiwan government to adopt a more conservative trade and investment policy than economic considerations would mandate. The main concern is that Beijing may use Taiwan's economic dependence as leverage to force political concessions from Taiwan. In a worst-case situation, Beijing may even use economic sanctions as a substitute for military action. Given the fact that Taiwan's economic dependence has increased and efforts to find alternative investment sites have not been too successful, the mainland market may be a "fatal attraction" for Taiwan. Thus, Taiwan regards cross-Strait economic interaction as a political rather than economic issue.

However, Taiwan's political "balance" is not necessarily at a deficit. Taiwanese exports to mainland China have been investment-driven, and have had social, cultural, and even political impacts on the mainland's local development. Hence, quantitative "dependence" cannot cover the fact that Taiwanese investment has created a certain "interdependence" in economic relations. If Taiwanese investment plays an increasing role in the mainland's local economic development, the latter's central government might hesitate to use coercive means to cease this relationship. Since trade and FDI-related industries are the most dynamic sectors in mainland China's economy, Beijing would need to calculate the costs and benefits before imposing economic sanctions.

Furthermore, economic globalization has challenged the traditional wisdom that the state can control bilateral trade and investment activities for political purposes. Through various strategic alliances and internationalization policies, defining "real" Taiwanese investment has become more difficult. Therefore, Taiwan's economic dependence must be put in a broader category of international division of labor. The possible "target" of mainland Chinese economic sanctions thus becomes much more ambiguous.

The real pressure for Taiwan's economic dependence has been bottom-up voices to ease economic restrictions, namely pressure from Taiwan's business community. As mainland China further opens its domestic market, the incentives for Taiwan's large-sized enterprises to explore the mainland market will also rise. Mainland China's leaders understand their own country's economic attractiveness, and thus have focused united front endeavors on Taiwan's business community. In other words, the current policy of *jieji yongren* clashes not only with the Beijing authorities, but also with the market mechanism. It is obvious that the latter presents a much greater challenge to Taiwan's decision-makers.

To summarize, protecting national security while at the same time promoting economic benefits is not an easy job for Taiwan. In an era of economic globalization, international-oriented firms have gradually become independent actors between host and home countries. The home country finds it more difficult to regulate firm behavior as part of a strategy to decrease the "economic dependence" on certain markets. Also, the host country is not able to impose sanctions without hurting other international partners, including itself. In Taiwan's case, the best way to decrease the political effects of economic dependence is not to perfect legal restrictions, but rather to improve the local infrastructure and introduce more international factors into Taiwan's future development. Real security can be guaranteed only after including mainland projects as a sector of Taiwan's grand strategy of developing an international division of labor. Under such circumstances, rather than being a "guide" to the business community, the role of the state would be to warn of political risks on the mainland and to fertilize Taiwan's domestic high-tech industries. The state should neither "teach" the business community what not to do, nor make decisions for them. Taiwan's continuous development is based on a prosperous economy, and a healthy economy depends on successful adjustment to accommodate international competition. Without these internationalization strategies, Taiwan's economic dependence on mainland China truly poses a threat to its national security.