The State and Taiwan's Mainland Economic Policy

TSE-KANG LENG

This article adopts the state-centered approach to analyze Taiwan's cross-straits economic policy in the 1990s. I use the "strong-state paradigm" to explain Taiwan's development in the past forty years. While the neo-liberal school of political economy stresses the advantage of laissez-faire policies, and dependency theorists emphasize international constraints upon development, the statist approach focuses on the state's capacity and autonomy in manipulating the state-society relationship and in governing the market.

The East Asian developmental states in general and Taiwan in particular work with and often promote the market, which is employed as an instrument that exposes particular industries to international competitive pressures. A selective industrial policy for economic development involves (1) state initiatives that decide which products or technologies should be encouraged; (2) public resources or influences over private resources to carry through these initiatives, and (3) a big before-the-fact strategy.[1] The state's regulative policies compete with the market mechanism in the international arena. The state must meet the major challenges presented by profit-seeking businessmen and economic interdependence among trading states. It needs to accommodate domestic social forces on the issue of trade and investment and to protect national interests through deliberate designs to enhance its competitive edge and increase international cooperation. The strong state initiates policies according to autonomous actions of the state elite, leads the market force, and adjusts the economic structure to accommodate the changing international environment.

This article will highlight one crucial perspective of the state-centered approach: the regulative capacity of the state, with an emphasis on formal rules, policy instruments, and informal routines. With these formal and informal procedures set in a socioeconomic context, I will discuss the capacity and institutional goals of state actions. First, I will compare the legal framework and the actual business performance of Taiwan's trade and investment with mainland China; I also discuss the impact of economic dependence on Taiwan's autonomous state actions. Finally, I will analyze the state's efforts to lead and impede the market motivations of private firms, and, in explaining Taiwan's cross-straits economic policy, I will provide an alternative explanation of the state's autonomy and capacity in relation to the "strong-state paradigm."

Economic Interaction Across the Taiwan Strait

Taiwan's economic policy toward mainland China follows the mercantilist model of trade regulation. While the liberal school of international trade emphasizes comparative advantage and the market mechanism as the major sources of economic change, the mercantilist/economic nationalism school focuses on the state as the predominant actor in using foreign economic relations to achieve political interests and national security. Mercantilist, economic nationalism recognizes that markets must function in a world of competitive groups and states.[2] Hence, regulating trade and investment for the sake of national interests could be legitimized as autonomous state actions.

According to Taiwan's current policy, direct economic linkages with mainland China are prohibited. Most economic activities between Taiwan and mainland China must be conducted through a third party, normally Hong Kong.

The Taiwan government tries to intervene directly into the booming economic interactions with mainland China through strict economic regulations. The state utilizes coercive political instruments to resist market incentives and business interests in mainland China. Its regulative policies, however, fail to confine profit-seeking Taiwanese businessmen from rushing into the mainland market. According to the official statistics of the Hong Kong government, the total indirect trade volume between Taiwan and mainland China reached U.S. $8.6 billion in 1993. These official statistics, however, are much below the actual amount of capital flow. As Economic Minister Chiang Ping-kun indicated, more than 60 percent of cross-straits trade was conducted directly.[3] The Board of Foreign Trade of the Ministry of Economic Affairs (MOEA) estimated that the total trade in 1993 would reach U.S. $13.83 billion if transit cargo and air trans-shipment figures excluded by Hong Kong were added.[4]

According to Ma Tien-tse, secretary general of the Chinese Marine Research Association (Taiwan), the indirect trade through Hong Kong is conducted in three different ways. First, commodities are shipped from Taiwan to Hong Kong, entering the Hong Kong port and customs, and then are transferred to other ships heading for mainland China. Second, commodities are exported from Taiwan to Hong Kong, and then transferred to surface transportation to mainland China. The Hong Kong Customs Service has import records, but no export ones for this method. Third, cargo vessels transfer export goods from Taiwan directly onto other cargo vessels heading for mainland China in the Hong Kong sea area, without unloading cargoes in the harbor and going through Hong Kong Customs. Among these three ways of re-export trade, only the first one is included in official statistics of re-export trade value by the Hong Kong Customs Service.[5]

Hence, official statistics from Hong Kong reflect only part of the bilateral trade value. In order to estimate the real trade value, I first calculate the differences between Taiwan's export to Hong Kong shown in Taiwan's customs data and Hong Kong's import from Taiwan shown in Hong Kong's customs data. Taiwan's export value to Hong Kong is larger than Hong Kong's import value from Taiwan. The statistical differences represent the value of commodities that are transferred to mainland China en route without going through Hong Kong customs. The 1994 data show the import-export differences as 7.5 billion U.S. dollars, shown as item 4 in table 1.

Second, considering the market size of Hong Kong, there is no way that it can absorb all the imports from Taiwan. In 1994, Hong Kong imported about U.S. $13 billion of commodity goods from Taiwan. The figure for re-export goods from Taiwan to mainland China through Hong Kong was U.S. $8.5 billion. Of the remaining 4.5 billion dollars of goods, a large portion was also re-transferred to mainland China but through different channels. According to the estimate of Sung Yun-wing, a professor of Chinese University of Hong Kong, the ratio of the re-transfer is about 82 percent and the amount U.S. $4.2 billion.[6] The Mainland Affairs Council of Taiwan estimates the ratio as 70 percent, which results in the value of U.S. $3.15 billion.[7] Because trade via Hong Kong does not reflect all the trade value between Taiwan and mainland China (some of it is through other places, such as Japan and South Korea), I will use the higher estimate of 82 percent to get closer to the real trade value. The value of U.S. $4.29 billion is shown as item 5 in table 1.

Hence, from table 1, if we add item 4 and item 5 on the official statistic data of Taiwan's indirect export to mainland China through the Hong Kong Customs Service, the real trade value in 1994 would reach 20.32 billion U.S. dollars.

For the investment data, there also exists a big gap between data from Taiwan and from mainland China. Table 2 shows a sharp contrast of Taiwanese investments approved by the Taiwan and mainland government. Data from mainland China are based on the negotiated instead of the contracted value of investment; the real amount should be lower than the negotiated value. However, in order to show the motivation of Taiwanese businessmen on mainland China to break up investment barriers from Taiwan, the negotiated value, which reflects the original business transaction, provides a better measure. The main reason for this large gap in investment data is that many Taiwanese businessmen conduct direct investment without the approval of the government; another reason is that many businessmen report lower-than-actual amounts to the Taiwanese government.[8]

The huge statistical gap between the official data and actual value proves that indirect trade and investment polices are weak. Taiwanese businessmen adopt flexible strategies to adjust to the changing economic environment in mainland China and to resist political intervention from Taiwan.

Table 1. Adjusted Exports to Mainland China (in U.S.$ millions)

Year	Taiwan's exports to Mainland China via HK (1)	Taiwan's exports to HK (2)	HK's imports from Taiwan (3)	The difference between HK's imports from Taiwan and Taiwan's exports to HK (4)=(2)–(3)	HK's imports from Taiwan re-transferred to Mainland China (5)=(3)–(1)x82%	Estimated real Taiwan's export to Mainland China (6)=(1)+(4)+(5)
1981	384.20	1,897.00	1,896.40	0.60	1,240.00	1,624.80
1982	194.50	1,565.30	1,570.10	–4.80	1,127.99	1,317.69
1983	157.80	1,643.60	1,600.00	43.60	1,182.60	1,384.00
1984	425.50	2,087.10	2,217.50	–130.40	1,469.44	1,764.54
1985	986.80	2,539.70	2,682.40	–142.70	1,390.39	2,234.49
1986	811.30	2,921.30	3,072.80	–151.50	1,854.43	2,514.23
1987	1,226.50	4,123.30	4,275.10	–151.80	2,499.85	3,574.55
1988	2,242.20	5,587.10	5,682.40	–95.30	2,820.96	4,967.86
1989	2,896.50	7,042.30	6,606.90	435.40	3,042.53	6,374.43
1990	3,278.30	8,556.20	7,439.90	1,116.30	3,412.51	7,807.11
1991	4,667.20	12,431.30	9,605.00	2,826.30	4,049.00	11,542.50
1992	6,287.90	15,416.00	11,156.30	4,259.70	3,992.09	14,539.69
1993	7,585.40	18,454.90	12,047.20	6,407.70	3,658.68	17,651.78
1994	8,517.20	21,263.00	13,575.70	7,505.30	4,297.21	20,319.71

Source: Liang An Ching Chi Fan Hsi Pao Kao (Monthly Report of Cross-Straits Economic Relations), Taipei: Mainland Affairs Council, June 1994, 33, March, 1995, 24; Min Chung Jih Pao (Popular News), 25 June 1994; and my own calculations.

Table 2. Investment Projects Approved by Taiwan and Mainland China

Year	Approved by Taiwan		Approved by Mainland China	
	No. of Projects	Amount (in U.S.$ millions)	No. of Projects	Amount (in U.S.$ millions)
1991	237	174.158	1,735	1,392.340
1992	264	246.992	6,430	5,547.900
1993	9,329	3,168.411	8,292	8,523.840
1994	934	962.21	6,247	5,397.000
Total	10,764	4,551.771	27,425	24,364.900

Source: Liang An Ching Chi Fan Hsi Pao Kao (Monthly Report of Cross-Straits Economic Relations), Taipei: Mainland Affairs Council, June 1994, 45, 6.

Policy Instruments to Regulate Taiwanese Businessmen

In addition to legal restrictions on trade and investments, the Taiwanese state seeks to use the following ways to regulate Taiwanese businessmen on mainland China.

Business Registration

In general, Taiwan's mainland economic policies cannot keep up with the actual cross-straits economic interaction. According to the "Statute Governing Relations of Taiwan and mainland China People," all the investment activities on mainland China must be approved in advance; all the investment activities conducted before the promulgation of the law must be registered within six months; and violators will be fined up to NT $3 million (U.S. $120,000).[9] From the legal perspective, the investment regulations are very strict and the punishment is severe.

As my preceding analysis shows, however, registered investment projects are much fewer than real projects. Moreover, until the end of 1993, MOEA had never punished businessman for illegal investments in mainland China.[10] In early 1994, the government released "Regulations Governing Business Activities in mainland China." As expected, few businessmen have registered to the MOEA, even though the procedure was revised and simplified.[11]

Financial and Monetary Instruments

Taiwan's financial policies have been useful in manipulating economic growth and development. To promote economic growth, the government adopts financial and monetary policies to accommodate the financial needs of specific industries. These include policies for exports and strategic industries, as well as setting up specialized banks and selective credit-control policies. These special sectors of the economy are provided with special medium- and long-term low interest loans. The interest rate difference between the strategic loans and the prime rate is around 1.75-2.75 percent.[12]

The financial instruments can also be used to control Taiwanese investments abroad. In allocating loans to stimulate domestic investment, the Central Bank of Taiwan gives priority to firms with investment projects in Taiwan's domestic market,[13] while constraining credit to firms investing in mainland China. Even though firms get the approval from the MOEA to invest in big projects in mainland China, the maximum amount of foreign exchange allowed by the Central Bank is only U.S. $3 million. Some firms must revise or cancel their projects in mainland China; others will continue their projects by using illegal channels to get foreign exchange.[14]

Taiwanese businessmen in mainland China obtain most of the capital from Taiwan. Because mainland banks are cash poor, they have limited funds to lend to Taiwanese enterprises. It is also difficult for Taiwanese business people to get loans from the local branches of Hong Kong or other foreign banks because they usually require land ownership or other collateral. Hence, 56 percent of their capital is from Taiwan, 25 percent from mainland China, and 11 percent comes from a third country.[15] Furthermore, until mid-1994, Taiwanese banks were still not allowed to establish branch offices in mainland China. Taiwanese businessmen must get their loans from domestic banks in Taiwan, which are subject to macro-economic control.

Taiwan, however, is unable to control enterprises effectively through financial tools because Taiwanese enterprises can obtain their capital through multiple channels. A substantial portion of capital is from the black market, which the government is unable to control through financial means. Firms get 50 to 55 percent of their capital from financial institutes, while more than 20 percent of the capital is from black markets.[16]

Moreover, Taiwanese businessmen can bring their capital out of the territory either by purchasing travel checks or transferring foreign exchange earned from exports. Exporters sometimes will keep their foreign exchange to invest in mainland China. As CitiBank in Taipei estimates, the total foreign exchange of Taiwan's exporters that was not changed to New Taiwan dollars rapidly expanded from U.S. $2.89 billion in 1987 to U.S. $24 billion in 1991.[17] A large portion of the foreign exchange flows directly into mainland China, and the Central Bank of Taiwan is unable to control this capital outflow.

Business Protection

Although big enterprises gradually get the momentum to invest in mainland China, small- and medium-size firms still constitute the majority of Taiwanese enterprises. These dynamic firms adopt flexible policies to survive and grow in an unfavorable environment.

Taiwan utilizes two major ways of assisting and guiding Taiwanese enterprises in mainland China. The first is to urge mainland China to sign the "Agreement to Protect Taiwanese Businessmen in mainland China." From Taiwan's perspective, current PRC regulations provide uncertain protection for the property and privilege of Taiwanese businessmen. A formal legal agreement between Taiwan and mainland China is crucial to protect the interests of Taiwanese businessmen.

Mainland China, however, refused Taiwan's proposal for the following reasons: (1) Taiwanese businessmen should be protected by PRC's domestic law, instead of a state-to-state agreement; Taiwan is a province of PRC, not a sovereign state;[18] (2) Because Taiwan does not allow direct investment in mainland China, there are no such "Taiwanese businessmen." Technically, most "Taiwanese businessmen" are Hong Kong or American businessmen; (3) the cross-straits investment is not reciprocal; mainland firms are not allowed to invest in Taiwan. Thus, there is no need to sign an agreement to protect one side without guaranteeing mutual benefits.[19]

Taiwan's attempt to sign the investment protection agreement was unsuccessful because it was a political rather than an economic issue. The PRC insisted that the Taiwanese investment was "a special kind of domestic investment" and should be regulated by domestic laws. From Beijing's perspective, the Taiwanese government tried to utilize the economic issue to enhance its status as an equal party in signing the agreement.

Another measure adopted by the Taiwanese government to protect businessmen was the establishment of a cross-ministry working force serving as a conciliation body. The main goal of this working force is to provide necessary business information and to establish Taiwanese business associations in mainland China. Until mid-1994, there were sixteen Taiwanese business associations in major mainland cities.[20] The Taiwan Affairs Office of PRC's State Council, however, intervenes directly in the personnel and general operations of these business associations. For example, the Taiwan Affairs Office always "recommends" vice directors to these associations. Furthermore, Taiwan's Straits Exchange Foundation (SEF) can participate very little in the daily operation of Taiwanese business associations. The SEF is supposed to serve as a bridge between the government and businessmen to solve problems, but its mainland counterpart is reluctant to cooperate. Among the 140 inquiries sent by the SEF, only 14 received replies from its mainland counterpart.[21]

Taiwanese businessmen need to establish their own "kuan-hsi" network and use the "back door." As a Taiwanese businessman says, policies, negotiations, or agreements signed by Taipei and Beijing help very little; what really controls the daily life is the local city or county government, or even a low-ranking official in a small department.[22] According to a survey conducted by a private institute, 78 percent of the Taiwanese businessmen will find "their own way" to solve problems in mainland China; 13 percent contact mainland officials, and only 6 percent solve problems through Taiwanese business associations.[23]

Taiwan's Economic Dependence on Mainland China

One inevitable effect of the booming cross-straits economy is Taiwan's economic dependence on mainland China, which has been increasing in the past few years. Table 3 shows the adjusted degree of economic interdependence between Taiwan and mainland China. The degree of dependence of Taiwanese exports to the mainland market has far surpassed the "warning line" of 10 percent set up by the MOEA. Furthermore, table 4 illustrates the proportion of Taiwan's trade surplus with mainland China to Taiwan's total international trade surplus. Without the trade surplus with mainland China, Taiwan's international trade would have a deficit instead of a surplus, thus illustrating the importance of the mainland market in Taiwan's international trade.

Taiwan's economic dependence on mainland China greatly constrains Taipei's

Table 3. Economic Interdependence between Taiwan and Mainland China

Year	Shares of Exports to Mainland China in Taiwan's Total Exports (%)	Shares of Trade with Mainland China in Taiwan's Total Trade (%)	Shares of Exports to Taiwan in Mainland's Total Exports (%)	Shares on Trade with Taiwan in Mainland's Total Trade (%)
1981	7.19	3.54	0.34	0.77
1982	5.93	3.00	0.38	0.73
1983	5.51	2.85	0.40	0.69
1984	5.79	3.12	0.49	0.69
1985	7.27	4.17	0.42	0.56
1986	6.31	3.70	0.46	0.62
1987	6.66	3.71	0.73	0.89
1988	8.19	4.07	1.01	0.99
1989	9.61	4.88	1.12	1.18
1990	11.62	5.78	1.23	1.61
1991	15.15	7.49	1.57	1.99
1992	17.85	8.75	1.32	9.46
1993	20.78	10.21	1.20	9.58
1994	21.83	12.42	1.53	9.36

Source: Liang An Ching Chi Fan Hsi Pao Kao (Monthly Report of Cross-Straits Economic Relations), Taipei: Mainland Affairs Council, June 1994, 33, 37, March 1995, 29; *Taiwan Statistical Data Book 1993,* Taipei: Council for Economic Planning and Development, 1993, 190; and my own calculations.

Table 4. Taiwan's Trade Surplus with Mainland China in Total Trade Surplus

Year	Taiwan's Trade Surplus with Mainland China (in U.S.$ millions)	Taiwan's International Trade Surplus (in U.S.$ millions)	Percentage
1987	3,285.61	18,695.37	17.57
1988	4,489.17	10,994.56	40.83
1989	5,787.53	14,038.63	41.23
1990	7,041.75	12,498.44	56.34
1991	10,416.55	13,317.76	78.22
1992	13,420.72	9,493.70	141.36
1993	16,548.24	7,800.00	212.16
1994	19,700.00	7,700.00	255.84

Source: Liang An Ching Chi Fan Hsi Pao Kao (Monthly Report of Cross-Straits Economic Relations), Taipei: Mainland Affairs Council, June 1994, 28, 33. *Taiwan Statistical Data Book 1993,* Taipei: Council for Economic Planning and Development, 1993, 196. Associated Data, Cited from Internet Source, 8 February 1994, and 8 January 1995, and my own calculations.

capacity to cool down the mainland fever. In mid-1993, in order to stimulate exports to the United States, the Central Bank of Taiwan intervened directly into the foreign exchange market, which led to the depreciation of New Taiwan dollars in relation to U.S. dollars.[24] The commodity export to the United States in 1993, however, still declined 6.8 percent from the year before, while the indirect export to mainland China rose 20 percent.[25] The reason why the state's intervention policy fails to stimulate exports is that the mainland market has gradually replaced the U.S. market in attracting the largest portion of Taiwan's exports. Policies targeted at the U.S. market did not enhance the macro-economic situation in Taiwan as a whole.

Thus, Taiwan's economic dependence on mainland China has put Taiwan in the dilemma of having to choose between slowing the economic growth by cooling down trade relations with mainland China or adopting more liberal cross-straits economic policies—at the risk of national security—to stimulate the economy.

Taiwan's economic dependence on the mainland market gives China the political leverage to manipulate Taiwan's domestic economy. As Kenneth Waltz argues, the word "interdependence" obscures the inequalities of national capability and plays the trick of "all states are playing the same game." All states are definitely not playing the same game. A state that is heavily involved in the international economy but cannot shift to relative autarky is vulnerable.[26] Trade and commerce become a direct source of power and coercion, and thus an alternative to war.

China sees the advantages of attracting Taiwanese trade and investment. To encourage investments from Taiwan, in 1988 the State Council promulgated a set of twenty-two measures, which contained all the special inducements offered to foreign investors, but went several steps further. For example, Taiwan investors are allowed to sell stock in projects, rent government-owned factories, and take over and operate state enterprises by guaranteeing a certain amount of earnings to the state and keeping the rest. Taiwanese investors can appoint relatives on mainland China as agents to manage their projects, and there is no time limit on their projects. Taiwanese investors can also buy and sell real estate and leave such acquired property to heirs.[28]

Mainland authorities try to use preferential treatments to achieve their political goals. At the PRC's 1990 National Working Conference on Taiwan Affairs, policy statements such as "to promote political integration through economic exchange," "to raise popular pressure on the government of Taiwan," and "to lead to the unification with the motherland" were openly made regarding cross-straits economic relations.[29] Premier Li Peng further indicated in the "Government Report" that the main goal of the PRC was to use economic interaction as an instrument to promote "three links"[30] with Taiwan; the achievement of these will be a breakthrough in China's unification under the "one country, two systems" formula.[31]

To sum up, autonomous actions of the Taiwanese state have been constrained by economic dependence on mainland China. Taiwan's export performance is closely linked with the domestic economic conditions in mainland China. According to a regression analysis on the correlation between Taiwan's export change and mainland's economic policy, indirect exports from Taiwan to mainland China decrease by about 30 percent to 40 percent whenever mainland China adopts a deflationary or retrenchment policy.[32] In other words, it is the mainland's macro-economic policy that manipulates Taiwan's export sales. Taiwan's vulnerability is further reinforced by the fact that mainland China tries to use Taiwan's increasing economic dependence to achieve political goals.

Reflections on the State Autonomy and State Capacity

The strong-state paradigm emphasizes that state leaders are capable of resisting pressures from private interests and translating their will into public policy. The state not only provides public goods to the society, but also intervenes directly into the market system to achieve goals set up by autonomous state actions. During the 1960s and 1970s, the intervention of the Taiwanese state was an action of "market augmenting" in the sense that it reduced uncertainties and risks related to business, generated and disseminated information about opportunities, and inspired an impression of expansion among the people.

The Taiwanese state's intervention into the booming cross-straits trade and investments in the 1990s, however, is a "market restriction" policy. Moreover, the state lacks a vision to guide the market. The goals of cross-straits economic policy—market benefits or security concerns—are very ambiguous.

One of the key factors contributing to market forces prevailing over the state is the dynamic attitude of small- to medium-size Taiwanese businesses. The strong-state paradigm argues that it is state intervention and state incentives that create the international competitiveness of the Taiwanese firms. In the 1960s and 1970s, however, under the monopoly of state enterprises and the pressure from big enterprises supported by high tariffs, small enterprises were squeezed out of the domestic market. They had no choice but to shift their endeavors to the international market. These small- and medium-size firms constituted more than 80 percent of Taiwan's total exports, but were not qualified for major governmental assistance. According to the "Regulation of Encouraging Investment," which was regarded as the most powerful tool for state intervention, only limited-liability companies, not solely owned companies, could enjoy tax breaks and low interest rate loans from the state.[33] Small and medium enterprises, which are mostly family enterprises and over 70 percent solely owned, absorbed surplus labor in the countryside and adopted very flexible strategies to adjust to the changing international market.

The so-called "Taiwan economic miracle" was created by the autonomous state and dynamic small enterprises. Since the late 1980s, the small enterprises have led the march into the mainland market as they conducted business around the edges of, and sometimes against, Taiwan's legal restrictions. Economic benefits represent the only force driving them to invest or transfer their labor-intensive factories to the booming coastal areas in mainland China. Moreover, small enterprises were always one step ahead of state laws because state agencies were slow to reach consensus about regulating cross-straits economic relations; the state was "chasing" the market mechanism instead of governing it, thus partially legitimizing the existing situation.

The state also failed to decrease its economic dependence on mainland China. After twenty years of export-led growth, the state's efforts to adjust its economic structure and upgrade the industry level in the mid-1980s were not very successful. Therefore, labor-intensive industries lacked the motivation to upgrade their technology and to create a vertical division of labor with mainland China. The result was the total exodus of these labor-intensive firms to mainland China, regardless of state restrictions.

Up until 1992, Taiwan's exports consisted of products with a lower to a middle level of technology. Quantitatively, from 1983 to 1992, machinery and electrical equipment had grown about threefold. Most of the electrical equipment firms, however, conducted their business as original equipment manufacturers (OEM)s, selling products as components to other companies. For example, most computer makers in Taiwan are still not interested in creating their own brand names on the international market; their prominent goal is to make quality parts at very low prices. Taiwanese firms adopt new technologies at a fascinating speed, but few of them are developed at home. After mainland China commercializes its heavy and basic industry capacities, this OEM type of manufacturing, with its low cost of labor, may be substituted by mainland China.[34]

Furthermore, after accumulating huge amounts of foreign exchange reserves since the mid-eighties, the state failed to stimulate domestic investments. The result was an abundance of idle capital in the domestic market, which led to an unusual boom of the stock and real estate markets. During the 1987–91 period, the manufacturing sector experienced a decline and industrial upgrading was stagnant.

As a newly industrialized nation in which small- and medium-size enterprises prevail, Taiwan needs active state intervention to upgrade its industrial level. As Laura Tyson argues, competitive advantage in high-technology industries is "created," not endowed by nature. Imperfect competition, strategic behavior, dynamic economies of scale, and technological high-technology industries provide a fertile ground for interventionist policies.[35] In 1980, the Hsinchu Science Industry Park (HSIP) was established to lure back Taiwanese researchers from overseas. The HSIP focuses on a few sectors, including semiconductor and integrated-circuit industries, and houses about 4,000 scientists.[36] After a few years of development, HSIP's growth has slowed down in the past two years. In late 1993, the state revised the "Regulations of Promoting Industry Upgrading" and provided a five-year tax break for newly established high-technology companies.[37]

All in all, to reduce its economic dependence on mainland China, Taiwan has to create a vertical division of labor, to transfer low-end and labor-intensive industries to mainland China, and to develop high-technology products in the domestic research and development sectors. That is what Japan has done to enhance its international competitiveness after the rise of Asian NICs. Taiwan's efforts to upgrade the industrial level, however, are less successful. The "hollowing out" effects of Taiwan's labor-intensive industries are obvious, further weakening Taiwan's economic autonomy and exposing Taiwan to mainland China's potential political interference through economic tools.

Conclusion

This article challenges the utility of the strong-state paradigm in analyzing Taiwan's mainland economic policy. In Taiwan's authoritarian past, the strong state controls foreign trade to raise revenue and expand technological and supply capacities. Although the regime contains a substantial amount of industry and trade bias, the active intervention of the state to promote export-led growth proved to be successful in Taiwan.

In managing cross-straits economic relations in the 1990s, the state fails to enforce restrictive laws and policy instruments to regulate the business community. Private firms follow the market mechanism to cultivate the mainland market, and the state simply legitimizes the existing situation. Small- and medium-size enterprises play a crucial role in Taiwan's economic interactions with mainland China as they resist pressures from Taiwan and survive in the changing investment environment of mainland China. The state has not had firm control on them for the past thirty years, and they continue to be an obstacle to state policies on cross-straits economic interactions. Economic profit is their ultimate goal, and the state is failing in its attempt to divert their business interests to the southeast Asian countries. Their emigration to mainland China, with the Taiwanese state's failure to upgrade its industrial level, increases Taiwan's economic dependence on mainland China.

The state can no longer fully guide or govern the market as it did in the past; it needs to cooperate and compete with market forces. To grasp the complete picture of Taiwan's cross-straits economic policy, the Taiwanese state should no longer be regarded as a monolithic body. Since the late 1980s, democratization has released social forces and indirectly led to the split of political elites. While the bureaucracies suffer from interagency conflicts, the business community begins to penetrate the state structure and regains bargaining power on the issue of cross-straits trade and investment. Hence, to discover the reasons for the state's failure to govern the market, several factors must be taken into consideration: the impact of democratization, the political nature of cross-straits economic policy, bureaucratic coordination, and the bargaining process between the state and the business community. While Taiwan gradually develops a cooperative and coexistent relationship with its society, cross-straits economic policy must have a greater importance in post-authoritarian Taiwan.

NOTES

1. Robert Wade, "Industrial Policy in East Asia: Does It Lead or Follow the Market?" in *Manufacturing Miracles* eds. Gary Gereffi and Donald Wyman (Princeton: Princeton University Press), 234.
2. Robert Gilpin, *The Political Economy of International Relations* (Princeton: Princeton University Press, 1987), chapter 2.
3. *Kung Shang Shih Pao, (Business Times)*, 26 January 1994.
4. *Dow Jones International News*, 7 March 1993. Cited from Internet resource of *China News Digest*.
5. *Tzu Yu Shih Pao (Freedom News)*, 12 December 1993.
6. *Min Chung Jih Pao (Popular News)*, 25 June 1994.
7. Kao Koong-lian, *Trade and Investment Across the Taiwan Straits* (Taipei: Mainland Affairs Council, 1993), 5.
8. *Liang An Ching Chi Nien Pao (Annual Report of Cross-Straits Economy)* (Taipei: Chung Hua Institute of Economic Research, 1994), 236.
9. *Collected Regulations of Investing on Mainland China*, (Taipei: Ministry of Economic Affairs, 1993).
10. *Lien Ho Pao*, 12 October 1993.
11. *World Journal News*, 28 March 1994.
12. Shea Jia-dong and Yang Ya-hwei, "Taiwan's Financial System and the Allocation of Investment

Funds," in *The Role of the State in Taiwan's Development*, eds. Joel Aberbach, David Dollar, and Kenneth Sokoloff (New York: M.E. Sharpe, 1994), 193-230.

13. *Kung Shang Shih Pao (Business News)*, 11 June 1993.

14. *Chung Shih Chou Kan (China Times Weekly)*, 18 September 1993, 19.

15. Ho Yung-ching and others, *To Tzu Ta Lu Shih Chang (Investing in Mainland China)* (Taipei, Management Science Association, 1993), 42.

16. Yang Ya-hui, "Taiwan's Monetary Policies and Economic Development," *Industrial Development and Economic Policy* (Taipei: Chung Hua Institute of Economic Research, 1993), 198.

17. Milton Yeh, "Ask a Tiger for Its Hide," unpublished manuscript, 1994, 4.

18. *Kung Shang Shih Pao (Business News)*, 15 May 1993.

19. Chen An and Peng Li, "Tai Shang Ta Lu To Tzu Chuan I Pao Chang Hsieh I Po His (An Analysis of the Agreement of Taiwanese Businessmen Protection)," Xiamen: *Tai Wan Yen Jiu (Taiwan Study)*, No. 4, 1993: 60.

20. Working Document of Straits Exchange Foundation.

21. Interview with Chen Jung-yuan and Chang Kuo-pao, staff members of Straits Exchange Foundation.

22. Interview with Liu An-kuo, a Taiwanese lamp-maker. 1 August 1994.

23. Unpublished manuscript by Tai-Yu management consultant firm, Taipei, Taiwan.

24. *Lien Ho Pao*, 22 May 1993.

25. *Liang An Ching Chi Fan His Pao Kao*, ibid., 74.

26. Kenneth Waltz, "The Myth of National Interdependence," in *The International Cooperation* ed. Charles Kindleberger (Cambridge: MIT Press, 1970).

27. Albert Hirschman, *National Power and the Structure of Foreign Trade* (Berkeley: University of California Press, 1969), 15.

28. *Foreign Broadcast Information Service-China*, 29 March 1989, 72; Clough, ibid., 42.

29. Yen Tzung-ta, "Retrospection and Refection on the Impact of Cross-Straits Economic Relations," in *Cross Straits Relations and the Future of China* (Taipei: Democracy Foundation, 1991), 59.

30. "Three Links" refers to direct trade, direct postal service, and direct transportation.

31. Chen Teh-sheng, *Liang An Cheng Ching Hu Tung (Political-Economic Interaction between Taiwan and Mainland China)* (Taipei: Yung Yeh Chu Pan She, 1994), 58.

32. Kao, ibid., 1993, 345.

33. Yu Tsong-hsin, "Small-medium Enterprises in Taiwan," in *Economic Development in Taiwan*, ed. Kao Hsi-chun and Li Cheng (Taipei: Commonwealth, 1991), 211.

34. Interview with Wu Chao-min, a System Engineer of Acer Computer Corporation in Taiwan. Acer is one of the a few exceptions to have its own brand name in the international market. However, key components, such as Hard Disk, CD ROM Drive, and LCD (Liquid Crystal Display) in the Laptop computers are controlled by Japanese companies such as NEC, Sharp and Toshiba.

35. Laura Tyson, *Who is Bashing Whom? Trade Conflict in High-Technology Industries* (Washington D.C.: Institute of International Economics, 1992), 4-9.

36. *The Economist*, 21 May 1994, 93.

37. Hsiao Wan-chang, "A Report of Economic Restoration," A Report delivered at Central Standing Committee Meeting of KMT, 30 June 1993. In *Chung Yang Jih Pao* (1 July 1993).