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# STATE AND BUSINESS IN THE ERA OF GLOBALIZATION: THE CASE OF CROSS-STRAIT LINKAGES IN THE COMPUTER INDUSTRY\*

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**Tse-Kang Leng**

The economic and political entanglement between Taiwan and China provides rich materials for examining the interaction between the state and business in the era of globalization. It will be seen that the earlier East Asian “developmental state” model of analysis<sup>1</sup> no longer holds, due to the rise of autonomous business communities that have integrated their operations into a global division of labor. This has eroded the regulatory capacity of the state. It will be seen that the governments both in Taiwan and in the PRC have had to adjust to the new realities by wrestling with new policy models.

This paper will examine, first, the general framework of state–business relations in cross-Strait economic interactions; second, the collective efforts of Taiwanese and global firms to develop the Chinese market; third, the process of “localization” of globalized Taiwanese firms in China; fourth, efforts on both sides of the Strait by the two central states, the municipal governments and quasi-state agencies to accommodate the forces of globalization; and finally, given the highly political nature of cross-Strait interactions, how direct or indirect political interventions by the two central governments have complicated this relationship.

## **The Framework for Analysis**

Sean O’Rian uses Ireland to illustrate a new type of successful role for the state. He argues that the way in which the Irish state has learned to mediate between local and global networks differs noticeably from the East Asian Newly Industrialized Countries (NICs), which he labels “bureaucratic developmental states”. These are characterized by state autonomy, which is reinforced by the

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<sup>1</sup> On this model, see, for example, Robert Wade’s influential book *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization* (Princeton: Princeton University Press, 1990).

coherence of the state bureaucracy and its selection of “national champions” in the export-oriented model of growth. He points out that in Asia, local firms’ alliances with the bureaucratic developmental state are being undermined as the firms become more and more closely aligned with the interests of their international business partners and locate some of their own production abroad.

O’Rian’s “flexible developmental state”, as in Ireland, instead adopts two new strategies. To cope with the challenges of globalization, the “flexible developmental state” connects to flows of capital by attracting foreign direct investment and then builds local networks of production and innovation around this; at the same time, the state fosters indigenous networks of innovation and then encourages them to internationalize. The effect of both strategies is to connect the local economy to the global economy in a way that encourages local industrial transformation, accumulation and development.<sup>2</sup>

Linda Weiss argues that in the current climate of globalization the state needs to promote various forms of public-private “innovation alliances” that can serve as platforms for acquiring, upgrading and spreading technology.<sup>3</sup> Ulrich Beck posits that the whole process of globalization involves a kind of “organized irresponsibility on the part of corporations”. Those with the advantages of mobility and a global network are able to weaken individual states by playing one off against the other.<sup>4</sup> Ronen Palan argues that the state, faced with this challenge, should not retreat but instead restructure capacities to cope, especially to meet rising demands from the business community. In principle, countries respond similarly to the forces of globalization, and they are therefore forced to compete by offering attractive legislative packages to corporations.<sup>5</sup>

At the same time, globalization remains “embedded” in specific places. As Saskia Sassen points out, global processes are structured by local constraints, such as the composition of the local workforce, its work culture and its prevailing political culture. Processes of economic globalization are constituted as concrete production complexes situated in specific places.<sup>6</sup>

As elaborated in the preceding analysis, globalization and government efforts to cope with autonomous corporate dynamics have become major driving forces that challenge the earlier form of the developmental state model. This can be seen clearly in the context of cross-Strait economic relations.

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<sup>2</sup> Sean O’Rian, “The Flexible Developmental State: Globalization, Information Technology, and the Celtic Tiger”, *Politics and Society*, Vol. 28, No. 2 (June 2000), pp. 163-165.

<sup>3</sup> Linda Weiss, *The Myth of the Powerless State* (Ithaca: Cornell University Press, 1998), pp. 70-80; see also “Is the State being Transformed by Globalization?”, in Linda Weiss (ed.), *States in the Global Economy* (Cambridge: Cambridge University Press, 2003), pp. 293-317.

<sup>4</sup> Ulrich Beck, “Redefining Power in the Global Age: Eight Theses”, *Dissent* (Fall 2001), p. 86.

<sup>5</sup> Ronen Palan, “Recasting Political Authority: Globalization and the State”, in Randall Germain (ed.), *Globalization and its Critics* (New York: St. Martins Press, 2000), p. 158.

<sup>6</sup> Saskia Sassen, “Cities and Communities in the Global Economy”, *American Behavioral Scientist*, Vol. 39, No. 5 (March/April 1996), pp. 631, 636.

### **The Global Division of Labor and Taiwanese Investment in China: A Case Study of Computer Design and Manufacture**

Taiwanese capital and technology in China have become integrated parts of a global economic division of labor, fully utilizing comparative advantages on both sides of the Taiwan Strait to enhance economic efficiency and to maximize benefits. This is true of both the labor-intensive industries such as shoemaking and more high-tech industries such as notebook PC production. Due to the impact of economic globalization since the late 1990s, pure “Taiwanese firms” are becoming more difficult to identify. Many are registered as foreign companies or investment firms. They are now involved in truly international operations and logistics, and the state’s limited instruments of control over the domestic economy have become inadequate to regulate the strategic alliances of business.

Quanta Computers Inc. provides an example of the global operations of Taiwanese firms and their alliances with multinational corporations in developing the Chinese market. Quanta has served as a contract manufacturer to Dell, Compaq/HP, Gateway, Apple, IBM, Sony, Sharp and other brand-name multinationals since the mid-1990s. Although the brand name Quanta is almost unknown to PC consumers, Quanta surpassed Toshiba as the world’s No. 1 notebook computer manufacturer in 2001.<sup>7</sup> Of the global shipment of 37.6 million notebook computers in 2003, Quanta produced 9.3 million units, almost 25 per cent of world output.<sup>8</sup>

Dell, which accounts for half of Quanta’s sales, is the global master of just-in-time manufacturing and has provided Quanta with the impetus to maintain its high standard. However, not until it started working with Quanta’s design and manufacturing team did Dell’s laptop PC business really take off. According to the 2002 data, the Texas-based PC maker relies on the Taiwanese company to produce 55 per cent of its notebook computers.<sup>9</sup>

In order to compete with Japanese and Korean PC giants, Taiwan’s entrepreneurs have to be adaptable to rapid change and short product cycles in the notebook computer industry. Normally, the US brand-holder provides the Taiwanese manufacturer with a roadmap, such as product specifications and performance, while the Taiwanese side usually generates the technical ideas, then

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<sup>7</sup> “Quanta Confirmed as World’s Largest Notebook Producer, According to IDC”, PR Newswire Association, Inc., 13 May 2003, [www.prnewswire.com](http://www.prnewswire.com).

<sup>8</sup> The total forecast for production of notebook computers in 2004 is 47 million units and it is estimated that Quanta’s share will increase to 28.7 per cent. “Quanta and Compaq to Boost Global Output”, *Global Sources*, 15 January 2004, [www.globalsources.com](http://www.globalsources.com); “Taiwan’s notebook PC OEMs see brighter prospects for 2004”, *Global Sources*, 17 November 2003, [www.globalsources.com](http://www.globalsources.com); “Asustek squeezes into world top-five notebook contract makers”, 6 February 2004, *Global Sources*, [www.globalsources.com](http://www.globalsources.com).

<sup>9</sup> Bruce Einhorn, “Quanta’s Quantum Leap”, *Business Week*, 5 November 2001, p. 79; Faith Hung, “Quanta Holds Course In Turbulent Times—EMS Provider Manages To Make Headway Where Others Have Foundered”, *EBN Manhasset*: 17 December 2001, Issue 1293; p. 48; “Computer maker Quanta coming to Nashville”, 29 May 2003, [www.tennessean.com](http://www.tennessean.com).

creates and delivers the final product. By means of a highly interactive joint development process with its Taiwan partner, a brand-holder can come up with a new model notebook in just six to nine months.

The growth of Taiwan's notebook computer design capacity makes such international alliances interdependent. Dell adopts the strategy of getting the firms that produce for it to compete with each other.<sup>10</sup> Given this precarious relationship, Taiwanese notebook producers have been trying to reduce the risk of over-dependence. Quanta, for example, serves 9 of the 10 major notebook manufacturers in the world. Since late 2003, Quanta has also served China's PC company Legend and has become one of its major partners.<sup>11</sup> Given the fact that the profits have become slim due to keen competition, Quanta has decided to diversify its production lines to develop new markets such as liquid-crystal-display (LCD) TV. According to the management of Quanta, the non-PC products will occupy at least a quarter of Quanta's total production in 2004.<sup>12</sup>

Given the tense political situation across the Taiwan Strait, multinational IT firms try to maintain flexibility *vis-à-vis* their Taiwanese partners. Since Taiwan does not allow direct transportation links with China, Dell's international procurement officers in Taiwan could not effectively oversee manufacturing in China, while Chinese IT professionals face discrimination in wages and employment protection in Taiwan. Dell's strategists in the Greater China area, however, do not intend to lean toward any side. In 2001, Dell opened its first overseas R&D center in Shanghai. One year later, Dell reorganized its China R&D capacities and strengthened its Taiwan development center. Dell's China development center is in charge of lower-level PCs and software, whereas the one in Taiwan concentrates on the development of notebook computers and personal digital assistants (PDAs).<sup>13</sup>

For their part, the Taiwanese PC firms have little choice but to move their manufacturing capacities to China, in order to cut costs, enhance international competitiveness and maintain their global production networks. The decisions on relocating and branching out in China are often made jointly by the international brand-holders and their Taiwanese contractors. In reality, most of the major Taiwanese IT manufacturers had already established networks of upstream suppliers of key parts inside China. Most Taiwanese PC parts suppliers in the supply chain are in a similar situation.

In the past, the "Made in China, by Taiwan" type of operation was found in the labor-intensive industries, such as the alliance between the world's largest manufacturer of footwear (the Pou Chen Corp. of Taiwan) and Nike in sports shoes production. Nowadays, the alliances between Taiwanese PC makers and

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<sup>10</sup> Fang Guojian, *Haikuo Tiankong: Wo zai Daier de suiyue* (Wide Sea and Sky: My Years in Dell) (Taipei: Tianxia Publishing Co., 2002).

<sup>11</sup> *Gongshang shibao* (Business Times), 9 February 2004.

<sup>12</sup> *Gongshang shibao*, 10 February 2004.

<sup>13</sup> Guan Zhenxuan, "Waishang xin yibo de Taiwan re" (A New Wave of Taiwan Fever of Foreign Business), *Tianxia zazhi* (Commonwealth Magazine), 1 October 2002, pp. 112-116.

multinational corporations in China have created similar arrangements across the Taiwan Strait in the IT sector, concentrated in China's major metropolitan areas such as Shanghai. Over the past few years, these Taiwanese firms have made substantial contributions to China's global share of the IT market. For instance, Quanta shipped 70 per cent (5.6 million units) of its notebooks from its Shanghai factory in 2003, while this number was just 25 per cent in 2002.<sup>14</sup> In 2003, 20 million notebook computers were manufactured by Taiwanese manufacturers in China, while the total of the global output of Taiwanese notebook PC makers was 25 million units.<sup>15</sup>

The case of Quanta provides an example of the attempts by the Taiwanese firms to create a division of labor across the Taiwan Strait. Quanta spent NT\$115 billion (US\$3.3 billion) on R&D for flat-panel components, and has recruited 5,000 engineers and workers for its research facility and manufacturing plant in Taiwan.<sup>16</sup> To gain an advantage in cutting-edge technology, Taiwanese IT firms form various alliances with multinational corporations to enhance their R&D capacities.<sup>17</sup> To retain its competitive advantage in global networking, the Taiwan state, as will be seen, has had no choice but to encourage these alliances, financially and otherwise, in order to assist the Taiwanese business community to improve global logistics capacities and to enhance R&D caliber within Taiwan.

### **From "Global Firms" to "Chinese Firms": Localization of Taiwanese IT Companies in China**

Taiwanese IT firms in China are no longer entirely "Taiwanese" in nature but rather have often become "hybrid". The Chinese government even tends to regard these hybrid Taiwanese firms as model companies. Semiconductor Manufacturing International Corporation (SMIC, or Zhongxin), which will be discussed in the following pages, provides a good example. The process of localization in technology, human resources and state-business relations adds an important dimension in the current efforts of globalized Taiwanese firms to escape from the regulatory regimes of the Taiwanese state.

Founded in April 2000, SMIC is a US\$1.46 billion Taiwanese semiconductor company located in Shanghai's Zhangjiang High-Tech Park. It is registered as an American company to avoid possible intervention from Taipei. It has good reason to do so. Although the Taiwanese government, under pressure from the business

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<sup>14</sup> Abe De Ramos, "Quanta's Leap", CFO Asia, 29 October 2003, [www.cfo.com](http://www.cfo.com).

<sup>15</sup> "China Overtakes Taiwan in Notebook PC Production", October 2003 Issue, Nikkei Electronics Asia, [neasia.nikkeibp.com.html](http://neasia.nikkeibp.com.html); Institute for Information Industry, MIC, January 2004; "Taiwan Information Industry Marks Solid Progress", [www.taipeitradeshows.com.tw](http://www.taipeitradeshows.com.tw).

<sup>16</sup> "Quanta builds Fifth-Generation Flat-Panel Plant", Nikkei Electronics Asia, August 2003 Issue, [neasia.nikkeibp.com.html](http://neasia.nikkeibp.com.html).

<sup>17</sup> As one example, Taiwanese IT firms such as Advantech, Asustek, Quanta and Wistron have joined Microsoft's "Asian Incubation Project for Embedded Server Applications" in order to ally with the software giant in product development.

community, finally relaxed some of its restrictions on semiconductor investment to China in 2002 under the principle of “positive opening, effective management”, Taiwanese firms are allowed to establish only three silicon-wafer foundries in China, and the level of technology is limited to 8-inch wafers or below. Moreover, whoever invests in 8-inch wafers in the PRC must launch a new investment project to produce 12-inch wafers in Taiwan. Taiwanese semiconductor companies are not allowed to invest in cutting-edge semiconductor technology in China, but can export less advanced 0.25 micro-circuit technology. With the status of an “American company”, SMIC has already employed 0.13 micro-production technology in the PRC, outstripping what most Taiwanese competitors could offer.

SMIC has transformed itself into a multinational firm through strategic alliances with other international IT giants. For example, Motorola and SMIC signed a long-term strategic relationship agreement in October 2003 in exchange for SMIC shares, and Motorola will gain a seat on SMIC’s board of directors.<sup>18</sup>

The hybrid SMIC plans to localize its recruitment policies and to attract and train local Chinese expertise. Already, mainland Chinese engineers have replaced a large number of Taiwanese senior engineers at the management level. In a few years, the core management team may possibly be controlled by Chinese instead of Taiwanese IT elites.<sup>19</sup> In order to expand and consolidate its domestic roots, SMIC also provides internships for local Chinese university students and graduates, especially in the field of IC design. Normally, these local “seeds”, under the supervision of SMIC’s international team, are given the opportunity to complete their master’s thesis or PhD dissertation.<sup>20</sup> Chinese universities produce 50,000 to 60,000 graduates with master’s or doctoral degrees in engineering each year, and this pool of brainpower is potentially the most important source of SMIC’s human capital.

In addition to SMIC’s base in Shanghai and new facilities in Tianjin, SMIC has established a Beijing manufacturing facility. This Beijing project is designed to strengthen SMIC’s political and business networks and facilitate its recruitment of highly-qualified graduates from top universities in Beijing. This agenda intends to exploit the two major IT bases in Shanghai and Beijing, while also ensuring that the company’s operations are politically correct.

State capacities in China are devolving from the central government to local governments in the coastal areas. Sub-national actors such as Guangdong Province and the Shanghai municipal government now play a key role in accommodating the economic needs of foreign investors. In line with this trend, a

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<sup>18</sup> “Motorola and SMIC Announce Strategic Foundry Relationship to Fully Utilize Semiconductor Factory”, SMIC Press Releases, Austin, Texas, Shanghai and Tianjin, 24 October 2003, [www.smics.com](http://www.smics.com).

<sup>19</sup> Interview with a senior Taiwanese manager of SMIC, Shanghai, 9 July 2004.

<sup>20</sup> Tse-Kang Leng, *A Political Analysis of Information Technology Development: Shanghai in Comparative Perspective* (Zixun Chanye Quanqiuhua de Zhengzhi Fenxi) (Taipei: INK, 2002), p. 247.

number of city governments in China have enhanced their R&D capacities and formed alliances with SMIC to promote local competitiveness in the IT sector. For instance, the Shenzhen National Integrated Circuit Design Industrialization Base, one of the seven bases that were approved by governmental authorities in December 2001, started operations in April 2003. The base is positioned as a public technical resource to provide technical services for the integrated-circuit design enterprises of Shenzhen and its surrounding areas. The Shenzhen municipal government made an investment of 50 million yuan and built an electronic design automated instrument platform, a testing and experimental platform, a training platform, and a platform for intellectual property rights consultancies.<sup>21</sup> The new momentum of SMIC in the Chinese market has been closely linked with and embedded in such local contexts.

### **State Incentives, Local States and Quasi-State Agencies**

Given the fact that the Taiwanese firms have developed independent strategies of globalization and localization to explore the Chinese market, the government in Taiwan has had to strive to adjust its role in governing the cross-Straits economy beyond the traditional command and control methods. As discussed in the previous sections, developmental state revisionists stress the state's promotion of international alliances in order to achieve global competitiveness. Such state action focuses on public-private alliances and supports the globalization of private firms by providing the necessary infrastructure and R&D facilities.

An example is the plan of Taiwan's Ministry of Economic Affairs (MOEA) to enhance Taiwan's R&D capacities and create a comprehensive division of design and manufacturing processes across the Taiwan Strait. MOEA plans to spend NT\$100 billion (US\$2.9 billion) to set up six research and development clusters in Taiwan over the next 5 years. The project aims to foster the formation of high-tech industrial centers based on these R&D clusters. The ministry expects at least 30 multinational enterprises to open regional research centers in Taiwan by 2006 and to team up with local enterprises on R&D work. MOEA, local enterprises and multinationals have co-organized 15 R&D alliances and there are plans to form another 60 such alliances by 2006.<sup>22</sup> MOEA plans to use incentives such as tax breaks, R&D subsidies and low-interest loans to encourage foreign and domestic firms to set up R&D centers.<sup>23</sup>

In order to enhance its design capacities in Taiwan, Quanta has filed requests with the Taiwanese government for support of its R&D activities. Quanta needs a site of more than 100 acres for a new plant. The National Science Council (NSC)

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<sup>21</sup> *SinoCast China Business Daily News*, Dallas, 23 April 2003, p. 1.

<sup>22</sup> Multinationals that have opened R&D centers in Taiwan to date include HP, Dell, Aixtron AG and Sony.

<sup>23</sup> "Taiwan plans to Set Up Six R&D Clusters in Five Years", China Economic News Services, 27 May 2003.



of Taiwan is in charge of site procurement, and has located a tract in Taoyuan.<sup>24</sup>

Another case of a public-private alliance for upgrading R&D capacities is Hon Hai's project in Taipei County. The Hon Hai case is important in that it demonstrates the state's attempt to retain major logistics capacities in Taiwan. Hon Hai was among the first major Taiwanese electronics manufacturers to venture into China. It is estimated that 90 per cent of Hon Hai's net profit now comes from its business in China. The after-tax revenue of Hon Hai for the first half of 2003 reached NT\$10 billion (US\$290 million), and 67 per cent of this is generated by its plants in China.<sup>25</sup> Keeping Hon Hai's headquarters and R&D in Taiwan is a strategy the Taiwanese state needs to pursue.

In 2003, when Hon Hai decided to set up new global operations headquarters together with an R&D center in Taipei County, it was frustrated in its negotiations with local authorities. Hon Hai considered reducing or even withdrawing its plan. Due to the strong endorsement of the Ministry of Economic Affairs, plans for a science park in Taipei County finally got underway, including a downsized Hon Hai facility. This compromise spared MOEA as well as Taipei County from the considerable embarrassment that would have resulted from a Hon Hai pullout.<sup>26</sup>

It turned out that Hon Hai had a competitive offer from the Shanghai City government. As well as a huge tract of land with roads and other infrastructure including optical cable as well as water, power and gas utilities offered to Hon Hai cost-free, Shanghai also offered a golf-course improvement beside the proposed Hon Hai facility. In stark contrast, Taipei County could only offer tax advantages.<sup>27</sup> Shanghai can provide a more attractive package for Taiwanese companies like Hon Hai, and this is a serious challenge to Taiwan's official policy to encourage such firms to keep their "roots in Taiwan".

### The Role of Local States in Economic Globalization

The cases of Quanta and Hon Hai demonstrate the importance of local incentives in cross-strait economic interactions. As Saskia Sassen has noted, missing from most "retreat of the state" arguments about globalization are the actual processes, activities and infrastructures crucial to the implementation of globalization.<sup>28</sup> Overlooking the locations of economic globalization has served to distort the role played by central governments and by the governments of major cities.

Including local governments in the analysis adds three important dimensions to the study of economic globalization. First, such an approach breaks down the state into a variety of components that are significant for understanding international economic activities. Second, it shifts our attention from the power

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<sup>24</sup> *Gongshang shibao*, 28 October 2003.

<sup>25</sup> *Da gong bao* (Impartial Daily), 15 September 2003.

<sup>26</sup> *Zhonghua ribao* (China Daily News), 16 April 2003, [www.cdnnews.com.tw](http://www.cdnnews.com.tw).

<sup>27</sup> ET today.com, 15 April 2003, [www.ettoday.com](http://www.ettoday.com).

<sup>28</sup> Saskia Sassen, *Cities in the World Economy* (Thousand Oaks: Pine Forge Press, 2000), p. 2.

of large corporations over governments and economies to the range of activities and organizational arrangements necessary for the implementation and maintenance of a global network of factories, service operations and markets. Third, it contributes to a new focus on place and on the urban social and political order associated with these activities of the global network. Focusing on localities and cities allows us to specify a geography of “strategic places” on a global scale, as well as the micro-geographies and politics unfolding within these places.<sup>29</sup>

The importance of local authorities and cities in the process of globalization is seen in Monica Varsanyi’s argument that we have to understand how various social forces within cities create trans-state flows in the era of globalization. Studying this local momentum allows us to get at the place-based processes: that is, the ways in which social, political, cultural and economic processes at the local level connect with global dynamics. In essence, this approach attempts to understand the dynamics of globalization from a “bottom-up” perspective, in which we are concerned with how various political and economic interests within a city are attracted to the opportunities posed by globalization.<sup>30</sup>

In short, in addition to the main framework of national-level analysis of cross-Strait relations, sub-national factors have become crucial links with economic globalization. Taiwanese investment has concentrated in China’s southeast coastal area and greater Shanghai; and in the interactions of the local governments there and business interests, the local authorities end up playing roles in accommodating or resisting the political interventions of central governments.

Shanghai has become one of the hottest spots for Taiwanese capital and personnel flows into China.<sup>31</sup> In the booming IT sector, the Shanghai municipal government itself has become a major investor and financial supporter. The participation of the Shanghai government in specific projects has become a stabilizing factor increasing the confidence of Taiwanese investors.<sup>32</sup> The municipal government, for instance, has invested alongside Taiwanese venture capital to foster incubators and start-up IT companies. Strong incentives and the professionalism of Shanghai officials impress overseas Chinese IT entrepreneurs. This new local momentum attracts capital and talent to the greater Shanghai area.<sup>33</sup>

As compared to other southern Chinese regions such as Guangdong Province, the transparency of laws and regulations in Shanghai help the business

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<sup>29</sup> Ibid., p. 4.

<sup>30</sup> Monica Varsanyi, “Global Cities from the Ground Up: A Response to Peter Taylor”, *Political Geography*, Vol. 19 (2000), pp. 35-36.

<sup>31</sup> For instance, see Tse-Kang Leng, “Economic Globalization and IT Talent Flows: The Taipei/Shanghai/Silicon Valley Triangle”, *Asian Survey* (March/April 2002), pp. 230-50.

<sup>32</sup> Interview in Taipei, 1 December 2003, with the CEO of a financial consulting firm for Taiwanese businesspeople in China.

<sup>33</sup> Interview with Hua Yang, Vice Secretary General of Hua Yuan Science Association, San Jose, USA, 9 December 2003. Hua Yuan is a Silicon Valley – based, non-profit organization promoting high-tech exchange between the US and China. Most members in Hua Yuan are engineers from mainland China.

community develop accurate estimations of costs and profits. Business owners in the high-tech sectors agree that Shanghai is not the most innovative place for advanced technology developments, but regulatory transparency, the booming producer service industries and the rich supply of local skills in the service sector make Shanghai the most attractive place in China for hi-tech foreign firms to set up branches or headquarters.<sup>34</sup>

However, this has encouraged keen competition among multinational firms, along with increased rents and other costs, and some Taiwanese companies are gradually being squeezed out of the Shanghai metropolitan area. A considerable number have moved to adjacent Jiangsu Province. For example, Kunshan and Suzhou have attracted hundreds of Taiwanese companies, which form clusters of Taiwanese electronics specialty firms. Enjoying the lower operating costs, infrastructure and human resources of the flourishing Yangtze River Delta, major Taiwanese firms enjoy the status of a “big monster” in Suzhou, whereas they had seemed a “small potato” in Shanghai.<sup>35</sup>

In this keen competition to attract investment, local governments in China provide unauthorized tax exemptions and land-use privileges to Taiwanese investors. This unauthorized preferential treatment may lead to controversies with the central government and financial disputes afterwards. In order to avoid such troubles, Taiwanese investors negotiate with both the local and central governments to obtain the status of “new high-technology” for their investment projects. Once the status of “new high-technology” is obtained, more preferential treatment and guarantees are secured.<sup>36</sup>

However, Taiwanese firms need to expend a good amount of energy in their dealings with Chinese local governments even when their business is identified by the PRC central government as “new high-tech” industry. The Chinese local administrations have obvious advantages in helping Taiwanese firms to set up new businesses at an early stage as compared to the Taiwanese local governments, but problems with the local Chinese authorities sometimes occur after these firms begin to operate and to gain profits. In the long run, the “cooperative” local Chinese government may play both a negative and positive role in accommodating Taiwanese business interests.

Even so, Taipei City perceives rising challenges from the major mainland Chinese cities and must compete fiercely to stay a step ahead. To attract high-tech investments to Taipei, the city government provides low-interest loans and tax incentives to targeted industries such as IT and biotech. During a visit to major high-tech companies in Silicon Valley in the summer of 2003, Taipei Mayor Ma Ying-jeou sought to attract investment by offering increased financial incentives and vocational training services. He particularly invited chip design firms to set

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<sup>34</sup> Interview with the owner of a start-up software company, Shanghai, 15 July 2004.

<sup>35</sup> Wording from an interview with a manager of a high-tech Taiwanese firm in Suzhou, 14 August 2003.

<sup>36</sup> Interview with an official of the Taiwanese Business Association in Shanghai, Shanghai, 5 August 2003.

up technological support centers, product-testing facilities and laboratories in Taipei, and he extended his welcome to other IT and biotechnology companies as well.<sup>37</sup> Taipei is campaigning to establish itself as the research, design and marketing core in the Greater China area and the location of Taiwanese business headquarters.<sup>38</sup>

Given Taipei City's eagerness to become a logistics and operations center for the Greater China region, the city needs to promote direct capital, commodity and personnel flows with China. The city's drive to create a division of research design and manufacturing processes with mainland Chinese cities has been undercut, however, by the hostility of the Chen Shui-bian government and its policy of restricting direct cross-Strait interactions. Taipei Mayor Ma Ying-jeou has filed protests with the central government and engaged in several rounds of direct confrontations. The central-local conflict is further complicated by the fact that the pro-independence ruling party at the central level tries to blame KMT mayor Ma for neglecting national security by promoting direct links with China. Taipei's drives to embrace globalization and engage China thus have become the focus of a political power struggle in Taiwan.

Sections of the central government are also trying hard to keep the cutting-edge high-tech R&D in Taiwan. Taiwanese and foreign companies normally sign contracts with the Industrial Development Bureau of the Ministry of Economic Affairs to facilitate the establishment of their R&D capacities in Hsinchu Science Based Industrial Park, or Neihu and Nangang Software Parks in Taipei.

### **The Role of Quasi-State Agencies**

In addition to the state apparatus at the central and local levels, new quasi-state agencies have emerged to handle the complex economic interdependence between Taiwan and China. Given the sensitive political nature of cross-Strait economic relations, the state agencies in Taiwan face a dilemma over whether to prioritize national security concerns or economic incentives. Thus the semi-official Straits Exchange Foundation (SEF) was, until recent years, a useful vehicle for the Taiwanese state in handling cross-Strait matters such as business services and trade negotiations. But after Taiwan's 1998 announcement that cross-Strait relations were "special state-to-state relations", the Chinese authorities rejected SEF as the formal channel for cross-Strait interaction and negotiation.

As Taiwanese firms develop their own strategies for conducting business with and in China, the economic bureaucracies in Taiwan try to transform their roles into service providers to cope with the economic challenges and political

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<sup>37</sup> "Taipei Mayor Visits Silicon Valley to Court Investors", *Asia Pulse*, 28 August 2003; "Taipei Mayor Ma Ying-Jeou visits firms in Silicon Valley to court investors", NTIS, US Dept of Commerce, 27 August 2003.

<sup>38</sup> Keynote speech of Mayor Ma Ying-jeou, delivered at a conference on the Challenges to Taipei of Globalization, Taipei, 11 February 2004.

sensitivities. For the purposes of economic relations, the China External Trade Development Council (CETRA) has filled the void. CETRA was created by the Ministry of Economic Affairs as a non-profit organization some thirty years ago, and throughout its history CETRA has been a major promoter of Taiwan's foreign trade while keeping a very low profile. It plays an increasingly important role in cross-Straits economic interactions. The CETRA strategy is to build Taiwan into an "international sourcing center". Given the global trend toward outsourcing, this is supposed to help transform Taiwan's role in the cross-Straits economic dynamic from "producer" to "distributor" and "service provider". CETRA began establishing representative offices in China in 2002, to link the global sourcing activities of multinational corporations with Taiwan's economic interests in China.<sup>39</sup>

CETRA has targeted six major product categories: wireless and broadband communications, auto parts, electronic medical and health-care equipment, mobile set components, optical office machines, and optical telecommunications, as its focuses.<sup>40</sup> CETRA also utilizes its role as an exhibition and trade show organizer to foster deals between Taiwanese corporations and international buyers, including Chinese buyers. At Computex 2003 in Taipei, representatives from China were among the most active buyers. Twelve major IT companies from China attended, including Legend, Haier, TCL, BOE Technology Group Co., Tsinghua Tongfang Computers and Peking University's Founder Corporation. It is estimated that the orders placed by the Chinese companies were worth US\$3 billion.<sup>41</sup> CETRA's chief executive agreed with his Chinese counterpart to assign a special exhibition hall exclusively for Chinese electronics at Computex 2004.

CETRA's semi-governmental status enhances its international networking with counterparts in other Asian countries. The cooperation between CETRA and the Japan External Trade Organization (JETRO) is a good example. The major concern of Japanese firms in China is to establish secure supply chains suitable for Japanese manufacturers, and CETRA, together with JETRO, organizes Taiwanese suppliers to form strategic alliances with Japanese firms to guarantee a smooth supply of parts and semi-finished products. CETRA also helps JETRO to identify Taiwanese firms in China suitable for Japanese manufacturers, and CETRA also works with local Taiwan business associations in China to attract the Japanese buyers.<sup>42</sup>

CETRA has also helped Chinese firms to outsource IT products to Taiwanese partners. Legend alone bought about US\$1.4 billion worth of cell phones, handheld devices and notebook PCs from Taiwanese firms in 2003. Given the

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<sup>39</sup> Interview with David Liu, Deputy Secretary General of CETRA, 4 August 2003.

<sup>40</sup> "Exploring Global Markets by our International Sourcing Center", Market Development Division, China External Trade Association, 6 August 2003.

<sup>41</sup> Computex 2003 Special report—Companies in mainland China have purchased over 100 billion in Taiwan, IT Home, 26 September 2003.

<sup>42</sup> Interview with officials at the JETRO Shanghai Branch, 11 August 2003; also an interview with officials at JETRO headquarters in Tokyo, 3 February 2004.

current political situation in Taiwan, the semi-official CETRA has no choice but to keep a low profile in promoting this new type of economic activities.

However, due to its semi-governmental status, quasi-state actors like CETRA cannot totally isolate themselves from the macro-political environment in Taiwan. In January 2004, the official name of CETRA was changed to TAITRA (Taiwan External Trade Development Council). This shift reflects the current policy of the ruling Democratic Progressive Party to distinguish Taiwan's identity in the titles of organizations. In early 2004, TAITRA's new director ordered that TAITRA's Beijing branch be closed in order to slow down further cooperation with mainland Chinese partners.<sup>43</sup>

### **The Political Jockeying over Taiwan's Economic Relations with China**

During Taiwan's authoritarian past under Chiang Kai-shek, business interests were channeled by the patron-client framework of the one-party political system. By developing an accommodation with local KMT political factions and state-owned enterprises, the Taiwanese business community learned to co-exist with the authoritarian state. After Taiwan's democratization, the larger enterprises formed strategic alliances with both the ruling and opposition parties to enhance their political influence, mostly through campaign donations and by helping to finance policy think tanks for the politicians. For small and medium-sized firms, the most common way to enhance their access to power was to establish various business associations and to engage in informal group consultations and lobbying.<sup>44</sup>

Despite this, historically they have had limited leverage in influencing state policies in Taiwan. Facing constraints from the Taiwanese government in the 1990s, when they invested in manufacturing in China they had no choice but to register their factories as Hong Kong firms or to transform these "illegal businesses" into domestic Chinese firms to avoid possible punishment from Taiwan.

Taiwan's official economic policies today have changed considerably. They reflect an on-going tug-of-war in Taiwan between national security issues, the various political parties' stances on policy, and market forces. As noted in Yu-Shan Wu's paper in this journal issue, whereas the Lee Teng-hui administration in the 1990s remained highly suspicious about cross-Straits economic relations and adopted the pro-security policy of "patience over haste", this policy was replaced by one of "positive opening, effective management" during the first term of Chen Shui-bian's presidency. Direct investment to China with a value of less than US\$50 million is allowed, but the Taiwanese state still attempts to impose hurdles in the high-tech sectors, out of security concerns.

As elaborated in Yu-Shan Wu's paper, the major political parties today, except for the staunchly pro-independence Taiwan Solidarity Union, espouse

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<sup>43</sup> Interview with the head of the Asia Pacific Affairs Division of the Market Promotion Department of TAITRA, 24 June 2004, Taipei.

<sup>44</sup> Chen Dongsheng, *Jinuan chengshi* (Money, Power and City) (Taipei: Juliu, 1999), pp. 34-36.

various degrees of pro-engagement policy. The major difference between the ruling DPP and the pan-KMT alliance is in their attitudes toward the “one-China principle”. Without a negotiated compromise on the one-China principle, formal negotiations between China and Taiwan to resolve major economic issues such as the “three direct links” (economic, postal and transportation) become very difficult. The business community in Taiwan continues to push the government to open up the three direct links, but as yet to no avail.

As the Taiwanese government gradually opened the gate to direct investments in China in the late 1990s, the business community still also faced various forms of supervision and inspection by the government. However, since Taipei cannot oversee many of the restrictive regulations for plants located inside China, it is their daily operations and dealings with local officials in the PRC which really concerns the business people.

For their part, the PRC authorities seek to exert political pressures on investors so as to further the mainland’s anti-DPP cross-Straits policies. Although there is no direct order from the Chinese central government to suppress the mainland business activities of pro-DPP Taiwanese businesspeople, local Chinese officials tend to “speculate” on policy objectives from above and try to identify “Green-party [that is, actively pro-DPP and pro-Chen Shui-bian] Taiwanese businesspeople”. Local officials compare the lists of Chen Shui-bian’s state advisors in his first and second terms, and figure out their affiliated businesses in China. The easiest ways to punish the green party businesspeople is to inspect their tax records or to implement local regulations such as environmental impact assessment standards more strictly.<sup>45</sup>

A recent case concerns a very large company, the Chi-Mei group, founded by Hsu Wen-lung in the 1960s. Hsu and his Chi-Mei group have maintained a good relationship with the Taiwanese government. Hsu’s strong support of Taiwanese independence helped him to create a solid alliance with former President Lee Teng-hui. More recently, Hsu has served as a state advisor to the DPP government, has provided campaign donations to Chen Shui-bian’s 2004 presidential campaign, and has sponsored the Taiwan Think Tank, Chen’s major policy analysis institution.

The Chi-Mei group is the world’s largest manufacturer of a plastic material called ABS, and the mainland is its major market. Since 1996, the company has established a petrochemical complex in Zhenjiang, Jiangsu Province, and after a new expansion the total investment will reach US\$600 million and production capacity will exceed the group’s Taiwan facilities.<sup>46</sup> Chi-Mei Optoelectronics Corp., the world’s fourth-largest supplier of flat-panel displays for computers and television, has also launched plans to

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<sup>45</sup> Interview with a representative of a Taiwanese Business Association in Shanghai, 9 July 2004.

<sup>46</sup> “Tancha Lupi Taishang Xu Wenlong de Neidi Jidi” (Exploring the Green Taiwanese Businessman Hsu Wen-lung’s Mainland Projects), *Zhongguo jingying bao* (China Business), 7 June 2004, p. 4.

build a factory to assemble flat-screen monitors in Ningbo, Zhejiang Province.

The Chi-Mei Group's political tendencies finally led to direct intervention by China's central government. After the re-election of President Chen Shui-bian, the spokesman of the Taiwan Affairs Office of China's State Council stated that China does not welcome the "green Taiwanese businessman". In editorial comments in the *People's Daily* in May 2004, China called Hsu a "Big-shot for Taiwan independence" and argued that, even though Hsu benefits a lot from China's vast market and low costs, he still believes that "The mainland is like Taiwan's economic colony".<sup>47</sup>

However, the deterioration of China's relations with the Chi-Mei Group provided a chance for it to enhance its connections with the Taiwanese state. Not long after the release of the "Green Taiwanese businessman" editorial, Chi-Mei Optoelectronics signed an agreement with 35 banks in Taiwan for a syndicated loan of US\$2 billion. These 35 banks include major public-owned banks such as the Bank of Taiwan, Chang Hwa Commercial Bank, Chiao Tung Bank, Hua Nan Bank and others.<sup>48</sup> The US\$2 billion loan will fund the construction of Chi-Mei's 7.5 G TFT-LCD plant in the South Taiwan Science Park. Considering the special status and situation of Chi-Mei, the large bank loan is seen as compensation for Chi-Mei's troubles in China. Chi-Mei's choice of locating its plant in Taiwan is also a symbol of support for the Chen Shui-bian administration's policy to "keep the roots in Taiwan".

On a par with the Chi-Mei Group, the Evergreen Group has similarly enjoyed a good relationship with Lee Teng-hui and subsequently the Chen Shui-bian administration. The President of the Evergreen Group, Chang Rong-fa, was in the State Advisory Group in the first Chen administration from 2000 to 2004. As the head of one of the largest sea cargo groups in the world, however, Chang became more anxious as direct sea and air links between Taiwan and China were delayed. In the past four years, Chang has opted to improve his relationship with China and gradually de-linked his connections with the DPP government. The Evergreen Group has become one of the very few Taiwanese enterprises informed well in advance by Chinese authorities about major announcements on Taiwan policy.<sup>49</sup> On the eve of Taiwan's 2004 presidential election, Chang launched severe attacks on the policy adopted by the Chen Administration to obstruct direct cross-Strait links. Almost immediately after China's attack on the Chi-Mei Group, Chang paid a visit to China and was well received.

Other Taiwanese businesspeople with investments in China are following a course similar to the Evergreen Group. Increasing numbers have gone further and have decided to "choose sides" and move their business roots completely out of Taiwan. In the tug-of-war to attract Taiwanese businesspeople, the Taiwanese

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<sup>47</sup> *Renmin ribao* (People's Daily), 31 May 2004, p. 1.

<sup>48</sup> "Chi Mei Opto Gets Loan to Fund 7.5 G Plant", *Electronic Engineering Times*, 15 July 2004.

<sup>49</sup> Interview with officials of the Taiwan Affairs Office in Shanghai, 8 July 2004.



state is losing leverage.

Many other Taiwanese businesspeople with investments in China are making a point of distancing themselves from the Chen Shui-bian government.<sup>50</sup> They have also directly lobbied the President. Months earlier, on the eve of Taiwan's 2004 Presidential election, the Taiwan Business Association branches in the major Chinese cities made "Ten major demands" to the Taiwanese government to facilitate cross-Straits economic relations. These demands included such major policy shifts such as air links.

## Conclusion

In the cross-Straits context, Taiwan's state power is constrained by globalization and the localization strategies of individual Taiwanese firms. These firms have developed various networks with Chinese local governments, regardless of the policies of Taiwan's central government to discourage this. Taiwan's decision to lift the ban on "China initiatives" had been pushed through by corporations under pressure to reduce costs, even though the Taiwanese state had been hesitating to promote the creation of a division of labor across the Taiwan Strait due to political concerns.

Being able to offer low operating costs, Chinese local authorities, as has been seen, have taken initiatives to attract Taiwanese manufacturing as well as R&D facilities. Regardless of what policy stance the Taiwanese government takes, in the long term more and more Taiwanese firms will become "Chinese firms" in essence. The Taiwanese state thus faces multiple challenges from global operations, including this transformation of Taiwanese corporations.

In the early 1990s, Taiwanese firms often used the threat of relocation to China as leverage to extract concessions from the central and local governments in Taiwan. At that time, such plans to relocate were the stuff of industrialists' dreams. Since the late 1990s, however, their China projects are no longer just bargaining chips. Now, based on their experience and more rational calculations of costs, firms have discovered that their investments in China pay off better than investments in Taiwan. The balance of economic profits leans toward the Chinese side, but the local states on the two sides of the Taiwan Strait are still competing with each other to attract lucrative Taiwanese investments.

In order to bolster Taiwan's competitiveness, the Taiwanese state has tried to transform its role from a direct intervener and regulator into a deal-maker and R&D facilitator. These new roles differ from those of the earlier East Asian "bureaucratic developmental state". The Taiwanese state today endeavors to attract multinational corporations to establish research facilities in Taiwan and to encourage Taiwanese firms to retain their headquarters at home. These efforts are

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<sup>50</sup> After the 2004 presidential election, in response to the Chinese government's threat to "find the Green Label", only 10 per cent of the local heads of the Taiwanese Business Association attended the annual gathering of the Dragon Boat Festival organized by the Taiwanese government. In the past, at least 70 per cent of the local TBA heads within Taiwan attended this annual event. *Jingji ribao* (Economics Daily) (Taiwan), 21 June 2004, p. 2.

close to O'Rian's description of the "flexible developmental state" which focuses on fostering better connections between the state and the global economy, and they also exemplify Weiss's thesis that such a state focuses on public-private alliances for innovation. The local governments in China act similarly.

The forces of globalization have altered state power and state-business relations in cross-Strait economic interactions. First of all, different levels and parts of the state apparatus must be differentiated in the analysis. This does not mean the "demise" of the state at the central level, but it does mean that lower-level governments have gained a greater role. The older developmental state paradigm treats the state as a coherent body of policy-making. A revised developmental state approach must take account of changing economic demands and business interests. Because globalization must be "embedded" in local settings, local governments become crucial actors, with roles similar to a central "developmental state". Moreover, due to the sensitive nature of cross-Strait economic relations, many "quasi-state actors" have emerged to develop better connections with the business community and with global economic forces. These new quasi-state actors, even though still "central level" in nature, are deal-makers and service providers, not regulators and king-makers.

Second, compared to the early stages of cross-Strait economic interactions, Taiwanese firms have developed more independent roles in forming global alliances to explore the Chinese market. The processes of globalization and localization of Taiwanese firms in China demonstrate a widening gap between state goals and business interests. Taiwanese firms are embedded in the local Chinese environment, but also link local Chinese interests with global capitalism through the firms' global operations and logistics.

Last but not least, political factors still play a key role in determining the interactions between business and state. As has been observed, the policies of the Chinese central government at times have had a negative impact on local government incentives to accommodate Taiwanese business interests. And across the Strait, instead of managing the challenges of globalization entirely proactively, the Taiwanese state since the mid-1990s has considered its cross-Strait economic dependency as a threat to national security. Economic issues have been mingled with non-economic concerns such as "national identity" and security. Thus Taiwan's economic bureaucracies, even when favoring a "flexible developmental state" agenda, sometimes adopt passive policies in order to avoid political attack. Even though cross-Strait economic interaction has developed into a global rather than bilateral relationship, it is hindered by Taiwan's domestic politics and Beijing's efforts to threaten firms that are close to the DPP.