

Prospects of the Taiwan Strait West Coast Economic Zone

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I. Introduction

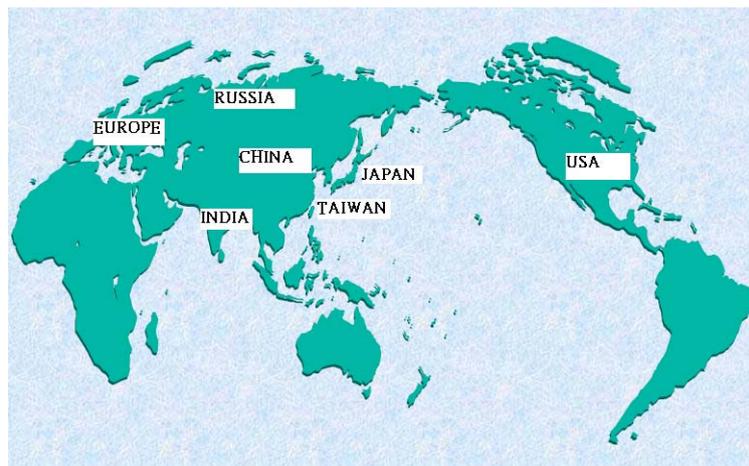
Since February 2001, China's Fujian provincial government has been actively advocating the Taiwan Strait West Coast Economic Zone (thereafter the Economic Zone). The Fujian government would like to develop its economy by strengthening its infrastructure and integrating the Fujian economy with foreign economies. Without the Chinese central government's policy endorsement and financial support, Fujian's plan had no substantial progress in this regards between 2001 and 2005.

In March 2006, the Economic Zone proposal was formally endorsed in the 11th five-year (2006-2010) economic and social development guidelines passed by the Chinese National People's Congress. With the blessing of the Chinese central government, will the Economic Zone proposal succeed in the future? In particular, will the Economic Zone proposal significantly facilitate economic integration and cooperation between Taiwan and Fujian? These are the questions this paper would like to address. Firstly, this paper introduces briefly both the Taiwan economy and China's Fujian economy. Secondly, this paper elaborates the content and purposes of the Economic Zone. Thirdly, this paper analyzes the proposal of the Economic Zone with regards to economic exchange and cooperation between Taiwan and Fujian. Finally, this paper concludes with assessment and prospects of the Economic Zone.

II. Taiwan and Fujian

Taiwan is formally known as the Republic of China, including the Taiwan island group, the Pescadores (Penghu) in the Taiwan Strait, Kinmen and Matsu off the coast of China's Fujian province. The main island of Taiwan is situated in the western Pacific between temperate Japan to the north, subtropical southern China to the west, and the tropical Philippines to the south. It is bounded to the east by the Pacific Ocean, to the south by the South China Sea and the Luzon Strait, to the west by the Taiwan Strait and to the north by the East China Sea. That is, Taiwan lies on major air and sea transportation routes in the region. The island of Taiwan is about 394 km long and 144 km at the widest point; it has a land area of 36,179 square km and a total of 1,566 kilometers of coastline (including the Penghu Islands). (See Map 1)

Map 1. Taiwan in the World



In 2003, Taiwan's gross national product (GNP) reached US\$295.6 billion, and its per capita GNP was US\$13,139. Gross domestic product (GDP) in 2003 grew to US\$286 billion, of which the industrial sector contributed 30.6 percent and agriculture only 1.8 percent. The service sector, which has been particularly robust and responsible for generating more than 50 percent of Taiwan's GDP since 1988, accounted for 67.6 percent of the GDP in 2003. In terms of foreign trade, the share of heavy and technology-intensive industrial products in total exports rose considerably to register 75.3 percent in 2003 and 77.2 percent in 2004.

Meanwhile, the share of imported capital goods increased from 20.5 percent in 2003 to 21.4 percent in 2004.

Fujian is one of the provinces on the southeast coast of China. The Fujian province borders the Zhejiang province to the north, the Jiangxi province to the west, and the Guangdong province to the south. Taiwan lies to the east, across the Taiwan Strait. The Fujian province is right at the juncture of China’s economically most developed areas: the Yangtze River Delta to its north and the Pearl River Delta to its south. (See Map 2.)

Map 2. The Fujian Province of China



Fujian is one of the wealthier provinces of China. Xiamen was one of the first cities in China to be opened up to foreign trade and investment as a Special Economic Zone (SEZ) in 1979. Because of the closeness both geographically and culturally with Taiwan, the Xiamen SEZ targeted Taiwan to attract Taiwan businesspeople’s investment and facilitate bilateral trade. As of December 2005, Fujian received US\$ 3.9 billion of foreign direct investment from Taiwan. Over the past twenty-five years, the Fujian province has maintained close business and trade connections with Taiwan.

From 1994-2004, the average growth rate of Fujian’s GDP was 12.5 percent and that of per capita GDP was 11.3 percent. In 2004, the provincial GDP reached RMB 605.3 billion, up

12.1 percent over the previous year; the per capita GDP amounted to RMB 17,218, with 11.4 percent rise over the previous year. In 2005, Fujian's nominal GDP was 648.7 billion yuan (US\$ 81 billion), a rise of 11 percent from the previous year. In terms of foreign trade, in 2004, Fujian's imports and exports registered US\$ 47.6 billion, an increase of 34.6 percent over the previous year. Of that, the exports reached US\$ 29.4 billion, a rise of 39.1 percent; and the imports US\$ 18.2 billion, a rise of 27.9 percent.

III. The Content and Purposes of the Economic Zone

Generally speaking, the Economic Zone proposal has two policy instruments: reinforcing infrastructural construction and fostering regional economic integration between Fujian and neighboring Chinese provinces and between Fujian and foreign economies. The Fujian province will build an urban transportation system, which will cut the time to travel between major cities to less than four hours and the travel time between major cities. The province also gave priority to construction of deep water harbors at Xiamen, Fuzhou and Meizhou harbors to increase their transportation capacity and competitiveness in urban development. In addition, provincial railways and major highways will also be accelerated to put the economic zone in practice.¹

As a matter of fact, the most important feature of the Economic Zone proposal is to foster economic integration between Fujian and Taiwan. The Chinese government attaching a great deal of importance on this proposal has both reasons of politics and economics. From the political perspective, the Chinese government would like to utilize Fujian's geographic and cultural proximity with Taiwan to reinforce people and economic exchange between Taiwan and Fujian. During the National People's Congress (NPC) held in Beijing in March 2006, many NPC deputies advocated that Fujian should be defined as a special zone for

¹ BBC Monitoring International Reports: "China's Fujian Province Accelerate Key Cities Construction," Sep 6, 2004.

Taiwan by implementing the Economic Zone proposal and other political experimental proposals for unification across the Taiwan Strait.² Nevertheless, if China's political motive is to attract more Taiwan's investment and thus increase the possibility of reunification, China should propose expanding economic exchange and cooperation between Taiwan and the Yangtze River Delta or the Pearl River Delta, where most of Taiwan businesspeople gathering in China, instead of Fujian.

From the economic perspective, the Chinese government would like to promote Fujian's economic development through implementing the Economic Zone proposal. Based on current trend of FDI inflow from Taiwan, the Chinese government should attach more emphasis on developing Fujian's overall economic development by strengthening economic linkage between Taiwan and Fujian given Fujian's special historical, cultural, geographic, and economic relations with Taiwan. According to Taiwan's official statistics, Taiwan's investment in Fujian peaked at US\$ 750 million in 2002, then declining to US\$ 450 million in 2004 and US\$ 398 million in 2005.

Taiwan's annual FDI in Fujian declined over time not only in terms of the absolute amount but also the relative term compared to other Chinese provinces. By the end of 1998, the shares of Taiwan's cumulative FDI in Guangdong, Jiangsu (including Shanghai), Fujian, and Zhejiang to that in China were 34.1 percent, 31.4 percent, 11.4 percent and 4.4 percent, respectively. By the end of 2005, these shares changed to 27.8 percent, 44.9 percent, 8.2 percent and 6.8 percent, respectively. Fujian's share of Taiwan's FDI in China declined from 7.4 percent in 2004 to 6.6 percent in 2005. This is evident that Fujian did not successfully attract Taiwan's investment through its geographic, cultural, and language advantage compared to other Chinese provinces. Many Taiwan businesspeople have been migrating to northern China. This should be a major concern for the Fujian provincial government.

As a matter of fact, compared to other Chinese coastal provinces, Fujian suffers from

² "Fujian Was Defined as a Special Zone for Taiwan," *Zhongguo Shibao* [China Times], March 6, 2006, p. A13.

many relative disadvantages in attracting Taiwan's investment in terms of market size, transportation convenience and industrial structure. For instance, in terms of comprehensive competitiveness of Chinese cities, best performing Xiamen in the Economic Zone ranked number nine in 2004, far behind Shanghai in the Yangtze River Delta and Shenzhen and Guangzhou in the Pearl River Delta, which ranked as number one to three.³ Based on the surveys of the Taiwan Electrical and Electronic Manufacturers' Association, Fujian's ranking in 30 Chinese provinces and municipalities declined from number nine in 2001 to number fourteen in 2005.⁴

As a result, the Fujian province particularly emphasized urban and transportation development and industrial cluster in its "Development Guidelines of the Taiwan Strait West Coast Economic Zone" promulgated in November 2004, which aimed at expanding its market size and improving its infrastructure to attract more FDI. Particularly, as Dean Zhen Yan of the Fujian Academy of Social Sciences pointed out, the main idea of the Fujian government to develop the Economic Zone is to take advantage of the similarities of history, culture, language, and economic development between Fujian and Taiwan to promote bilateral economic exchange, cooperation and prosperity.⁵ Therefore, the following section will elaborate the relationship between the Economic Zone and cross-Strait economic relations.

IV. The Economic Zone and Cross-Strait Economic Exchange

From the perspective of history, culture, and language, around 70 percent of Taiwan population came from Fujian, granting Fujian a special advantage in economic integration between Taiwan and China. This is the reason why Fujian was chosen by the Chinese government as the first province to engage economic exchange with Taiwan in the late 1970s.

³ *Zhongguo Chenshi Jingzhengli Baogao* [The Paper on the Competitiveness of Chinese Cities], Vol. 3, edited by Pengfei Ni (ed.), (Beijing: Social Science Literature Publisher, 2005), pp. 3-17.

⁴ Taiwan Electrical and Electronic Manufacturers' Association, *Neixiao Neimao Lian Shengji* [Opportunities Led by Internal Distribution and Domestic Trade] (Taipei: Business Weekly, 2005), pp. 66-69, 76.

⁵ Zhen Yan, conference note, October 21, 2005.

In addition, the current status of Fujian's economic development is equivalent to Taiwan's economic development of 1960s-1970s. Fujian's current three pillar industries – electronics, petrochemical and mechanics industries -- are also Taiwan's leading industries, making two economies complementary with each other. Based on these two foundations, Fujian would like to promote further economic exchange and cooperation with Taiwan to facilitate Fujian's economic development.⁶

Although the Chinese central government and the Fujian provincial government do not clearly elaborate the details of the Economic Zone to facilitate economic exchange and cooperation between Taiwan and Fujian, some important Chinese scholars have been providing general propositions from Fujian's perspective, such as Dean Zhen Yan and Director Fei Li of the Graduate Institute of Cross-Strait Relations in the Xiamen University.

Li proposed that the strategy of the Economic Zone on Taiwan can be divided into three levels: goal, content and policy. In terms of short-term goals, Li suggested that Taiwan and Fujian should form bilateral trade preferential treatment and investment facilitation measures like the closer economic partnership arrangement between Hong Kong and China. This goal should be achieved by resuming direct air and sea links between Taiwan and Fujian. In terms of medium-term goals, Taiwan and Fujian should achieve comprehensive, direct and reciprocal economic exchange and cooperation by establishing a bilateral economic dialogue mechanism. In terms of long-term goals, Taiwan and Fujian should achieve full economic integration by establish a bilateral economic cooperation mechanism and a common market.⁷

In terms of content, Li emphasized, Taiwan and Fujian should begin with preferential trade arrangement, then free trade area, and finally full economic integration. There would be two aspects of this content. First is to implement a preferential policy of bilateral commodity and service trade compared to the World Trade Organization regulations. Second, Taiwan and

⁶ Zhen Yan, conference note, October 21, 2005.

⁷ Fei Li, "On the Economic Relations with Taiwan in the Taiwan Strait West Coast Economic Zone," *Dongnan Xubao* (Fujian), 2004, pp. 27-28.

Fujian provide each other with more convenience measures of bilateral trade and investment, including trade and investment promotion, custom facilitation, commodity inspection, e-commerce, transparency of law and policy, cooperation of small-medium enterprises, and cooperation in the Chinese medicine industry.

Finally, in terms of policy, Li proposed that Fujian should unilaterally fulfill Chinese commitments to the WTO in advance to Taiwan businesspeople, promote bilateral financial cooperation (first unilaterally allow Taiwan's financial institutions to operate in Fujian), promote bilateral industrial cooperation (including capital intensive industry, technology-intensive industry and agriculture), facilitate transportation between two sides in order to expand bilateral division of labor, advocate exchange between bilateral people and cities, establish economic negotiation mechanism (including investment protection, economic dispute settlement, and protection of intellectual property rights), etc.

Although the guidelines for the Economic Zone do not limit to economic exchange and cooperation between Taiwan and Fujian, at least including self-strengthening of Fujian's economic fundamentals and economic exchange and cooperation between Fujian and foreign economies, successful promotion of economic exchange and cooperation between Taiwan and Fujian would be critical to the success of the Economic Zone. Yen and Li are both important scholars to draft the Economic Zone proposal and their suggestions are basically reflected in the plan. The following section would provide preliminary assessment and prospects of the Economic Zone.

V. Assessment and Prospects of the Economic Zone

There are two major instruments for the Fujian government to promote economic exchange and cooperation with Taiwan in the Economic Zone: unilateral preferential treatment for Taiwan businesspeople and bilateral agreements on reciprocal exchange and cooperation. As for the former, Fujian's maneuvering room is very limited. The main

instrument Fujian can unilaterally implement is to facilitate bilateral trade and investment. Other trade and investment preferential treatments are restricted under World Trade Organization rules.

In the foreseeable future, Fujian can hardly compete with the Yangtze River Delta and the Pearl River Delta in the manufacturing industry due to its limitations on market size and transportation convenience. Particularly, Taiwan's investment of electronics and electrical appliances in China makes up over 40% of Taiwan's total investment in China and these industries display strong cluster tendencies. It is unlikely Fujian's unilateral preferential treatment will reverse the long-term trend of Taiwan businesspeople expanding investment in the Yangtze River Delta and around the Bohai Area. At most Fujian's preferential measures could slow the speed at which Taiwanese companies move north.

Secondly, in the Economic Zone proposal, many suggested policy measures involve with the establishment of a bilateral economic exchange and cooperation mechanism between Taiwan and Fujian, particularly in the service industry. Taiwanese investment in Fujian's service sector will be an important aspect of future bilateral economic exchange and cooperation because most of Taiwan's manufacturing enterprises have been allowed to invest in China. In the service industry, both sides across the Taiwan Strait still have many restrictions on investment and probably need to sign an agreement of exchange and cooperation frameworks prior to the opening of the service sector.

However, to establish these frameworks require bilateral negotiation between Taiwan and China or Fujian. It is too early to judge whether Taiwan and China are willing to negotiate with each other through their authorized organizations. In order to promote economic exchange and cooperation between Taiwan and Fujian, both Yen and Li were very cautious by emphasizing that the Fujian government should adopt an approach of "separating politics and economics" or "economics first" to avoid cross-Strait political dilemma. Particularly, they emphasized that Fujian should strive for the support of the central government in this

regards.⁸ Nevertheless, there are too many sensitive political variables in cross-Strait relations. It is very difficult to establish a bilateral negotiation mechanism for the Economic Zone with full support from both governments of Taiwan and China.

If Fujian could unilaterally open up its service sector for Taiwanese businesspeople to invest and operate, of course it would increase the willingness of Taiwanese businesspeople to invest in Fujian. However, these preferential treatments would violate the principle of the WTO's most favored nation treatment and thus might provoke other countries' objection. Furthermore, these preferential treatments could be only temporary incentives, insufficient to persuade large numbers of Taiwanese businesses in other parts of China to transfer their manufacturing bases to Fujian due to Fujian's small market size. As long as other areas of China provide similar preferential treatments, Fujian's advantage will disappear very soon.

Thirdly, implementation of preferential trade arrangements and a free trade area between Taiwan and Fujian would be very difficult because in reality Fujian is not an independent custom area, completely isolating from other provinces in China in terms of trade flow. It will be very difficult to identify the origin of goods and service. Chinese commodities might be exported to Taiwan through Fujian and Taiwan commodities might be exported to whole China through Fujian. This will create enormous difficulties in managing trade across the Taiwan Strait. The preferential treatment agreements between Taiwan and Fujian might end up in effect the bilateral agreements between Taiwan and China.

Fourthly, the goal of full economic integration (like economic union) suggested by Li is more difficult to achieve for Taiwan and Fujian. From the perspective of economic integration theory, in addition to opening up each other's commodity, service, and production factor markets, full economic integration requires both sides coordinate in their monetary policies, fiscal policies, social welfare policies, industrial policies and product standards, etc. By

⁸ Fei Li, "On the Economic Relations with Taiwan," *Dongnan Xubao*, p. 27. Zhen Yan, conference note, October 21, 2005.

definition, the Fujian province is not an independent sovereign state per se and does not have capacity to implement the full economic integration agreement with Taiwan.

In conclusion, the Economic Zone is by no means a bad idea for creating a win-win situation for both Taiwan and Fujian by establishing closer economic exchange and cooperation mechanisms, but might run into a great deal of problems at both the negotiation and realization stages given current cross-Strait political stalemate. Be that as it may, Fujian's unilateral preferential treatments and opening measures to Taiwanese businesspeople would expand marginally economic exchanges between Fujian and Taiwan. As for accelerating comprehensive economic exchanges and integration between Taiwan and Fujian, it will be possible only after Taiwan and China reach an agreement on comprehensive economic exchange and cooperation. With its particular cultural and geographic advantages, Fujian will continue to play an important and unique role in future cross-strait economic exchanges and cooperation.