



Asian Leadership in Policy and Governance

Cross-Strait Economic Cooperation and Asian Regional Integration: Why Joint Participation of China and Taiwan Is Good for Them and the Region?
Yih-chyi Chuang

Article information:

To cite this document: Yih-chyi Chuang . "Cross-Strait Economic Cooperation and Asian Regional Integration: Why Joint Participation of China and Taiwan Is Good for Them and the Region?" *In* Asian Leadership in Policy and Governance. Published online: 28 Aug 2015; 107-127.

Permanent link to this document:

<http://dx.doi.org/10.1108/S2053-769720150000024005>

Downloaded on: 15 February 2016, At: 21:59 (PT)

References: this document contains references to 0 other documents.

To copy this document: permissions@emeraldinsight.com

The fulltext of this document has been downloaded 30 times since NaN*

Users who downloaded this article also downloaded:

Kristy Hsu, (2015), "ASEAN Centrality: A Quest for Leadership Role in East Asian Economic Integration", *Public Policy and Governance*, Vol. 24 pp. 69-105 <http://dx.doi.org/10.1108/S2053-769720150000024004>

Lowell Dittmer, (2015), "China's New Leadership and Global Role", *Public Policy and Governance*, Vol. 24 pp. 21-43 <http://dx.doi.org/10.1108/S2053-769720150000024002>

Jonathan Spangler, (2015), "The Evolution of Leadership Styles in the South China Sea: Contextual Factors and Shifting Approaches in China and the United States", *Public Policy and Governance*, Vol. 24 pp. 159-185 <http://dx.doi.org/10.1108/S2053-769720150000024007>

Access to this document was granted through an Emerald subscription provided by emerald-srm:264686 []

For Authors

If you would like to write for this, or any other Emerald publication, then please use our Emerald for Authors service information about how to choose which publication to write for and submission guidelines are available for all. Please visit www.emeraldinsight.com/authors for more information.

About Emerald www.emeraldinsight.com

Emerald is a global publisher linking research and practice to the benefit of society. The company manages a portfolio of more than 290 journals and over 2,350 books and book series volumes, as well as providing an extensive range of online products and additional customer resources and services.

Emerald is both COUNTER 4 and TRANSFER compliant. The organization is a partner of the Committee on Publication Ethics (COPE) and also works with Portico and the LOCKSS initiative for digital archive preservation.

*Related content and download information correct at time of download.

CHAPTER 5

CROSS-STRAIT ECONOMIC COOPERATION AND ASIAN REGIONAL INTEGRATION: WHY JOINT PARTICIPATION OF CHINA AND TAIWAN IS GOOD FOR THEM AND THE REGION?

Yih-chyi Chuang

ABSTRACT

This chapter investigates the evolution of cross-strait economic relations and Asian regional integration and its implications for future development in the region. Trade and investment in Asia is fundamentally market-driven, and cross-border FDI is the major driving force. This investment-induced trade explained the cross-strait economic relations and intensive trade in intra-industry and intra-regional trade in Asia. The rise of China in 1990s with the assistance of Taiwanese firms further accelerated the trend of integration by forming regional production networks. However, after 2000 institutional arrangement like bilateral or plural-lateral FTA emerged to normalize and institutionalize the de facto

Asian Leadership in Policy and Governance
Public Policy and Governance, Volume 24, 107–127
Copyright © 2015 by Emerald Group Publishing Limited
All rights of reproduction in any form reserved
ISSN: 2053-7697/doi:[10.1108/S2053-769720150000024005](https://doi.org/10.1108/S2053-769720150000024005)

economic integration. RCEP and TPP have evolved as the two major platforms for Asian regional cooperation with two key players, China and the United States, on each side. We argue that in the long run the win-win solution that the two platforms will further merge into FTAAP, which benefits all participants including China and the United States. However, in the short run, based on its 50 years of developmental experience, Taiwan can play an important role to promote and consolidate Asian regional integration as a technology provider and resource coordinator for the region and a risk buffer for entering Chinese market. We thus propose a roadmap for Taiwan and China to jointly participate in regional integration process. In the intermediate run, Asian economies need to change the structure toward more regional-centered trade in final goods through domestic consumption market in order to reduce the dependence on Western markets and mitigate any loss may arise from external shocks.

Keywords: Cross-strait economic relations; regional economic integration; production network and sharing; RCEP; TPP

THE EVOLUTION AND IMPLICATIONS OF CROSS-STRAIT ECONOMIC COOPERATION

Since 1949 after the retreat of the Nationalist led by Kuomintang (KMT) from Mainland China to Taiwan, there has been no contact both politically and economically across the Taiwan Strait between Taiwan and Mainland China. It was not until 1990 that cross-strait investment and trade started to emerge and accelerate afterward. The major driving forces are two-fold. Politically, the lift of Martial Law in 1987 by the Taiwanese government unilaterally ended the civil war between KMT and CCP and later the policy allowing for Taiwanese Mainlanders to visit their relatives in the Mainland due to the reason of human right had opened the door for connection across the Taiwan Strait. Economically, in the mid-1980s due to increase in wage and implementation of Labor Standard Law to protect workers, the urge for environmental protection, difficulty in getting factory land, and the appreciation of \$NTD because of accumulation of huge trade surplus in particular with the United States, traditional industries especially labor-intensive ones started to move outward looking for off-shore

production with cheap labor costs, and the destination of Taiwanese outward foreign direct investment first began for countries in South-East Asia such as Thailand, Malaysia, and the Philippines in the late 1980s, but then started to shift toward Mainland China mainly due to both sides sharing same culture and language, which significantly reduce the transaction costs across the borders. From 1990 to 2012, the accumulated FDI from Taiwan to China reached over \$1,200 billion USD and created more than 10 times of trade over investment. The close economic relations of investment-induced trade were mainly due to division of labor across the Taiwan Strait. In short, it is a vertical integration of industries that Taiwan produced important parts and components and then shipped to China for final assembly. This is a purely market-driven integration regardless of government policy interventions¹ (Figs. 1 and 2).

In May 2008, Taiwan experienced second power turnover and KMT regained its political power. Mr. Ma Ying-jeou won the presidential election and started Three Direct Links with Mainland China and later on June 29, 2010 signed Taiwan-China Economic Comprehensive Framework Agreement (ECFA) to formalize and institutionalize the de facto trade and economic relationship across the Taiwan Strait for the past 20 more years. Under the 1992 Consensus between KMT and CCP, as of December 2014

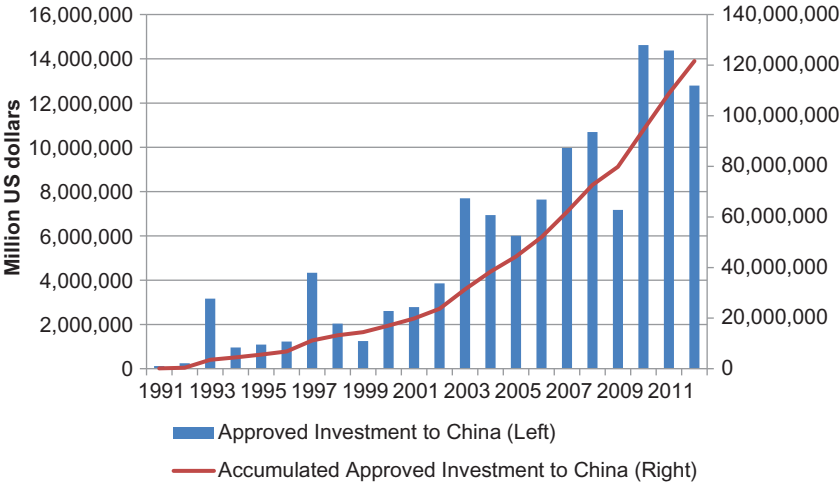


Fig. 1. Taiwan's FDI to China. Source: Cross-Strait Economic Statistics Monthly, various issues, Mainland Affairs Council, Republic of China (Taiwan).

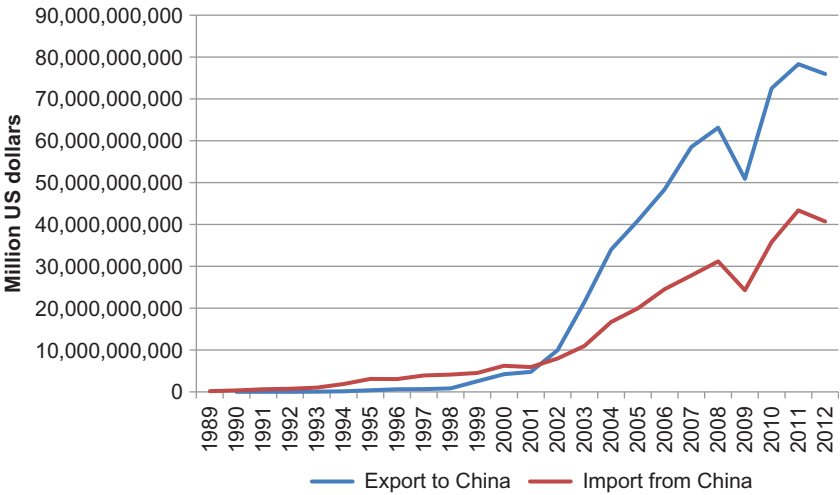


Fig. 2. Taiwan’s Trade with China. *Source:* Cross-Strait Economic Statistics Monthly, various issues, Mainland Affairs Council, Republic of China (Taiwan).

both sides had held 10 rounds of meetings and talks and reached 21 agreements.² The 1992 Consensus was considered as a smart strategy for both sides across the Strait because it avoided the unsolvable political dispute with a vague definition of “one China” and thus allowed both sides to focus on the issues of economic cooperation. Therefore, under the situation of no mutual trust between Taiwan and Mainland China, undoubtedly, the 1992 Consensus is the foundation for the existing dialogues and resulting agreements.

The recently inked Cross-Strait Services Trade Pact in June 2013 is an important benchmark to signal the entering of profoundal zone of the cross-strait economic cooperation. In addition to continuing decline of tariff and opening up for commodity trade, the real contents of economic cooperation include market access to services and convergence of rules and structures; industry cooperation and clustering among big, medium, and small enterprises; innovations in business models by integrating manufacturing and service industries; establishment of money clearing mechanism and Taiwan as a off-shore clearing center for RMB; financial cooperation and loans and financial support for small- and medium-size enterprises; and China’s outward FDI to Taiwan. The ECFA is like a FTA, but its real meaning is beyond traditional one merely on facilitating trade and investment and moreover it focuses on industry cooperation to streamline and

complete industrial supply chain, including product standard, joint R&D, and creation of own-brand names by utilizing China's huge domestic consumption market in the near future as China is transforming from outward-oriented to inward-oriented economy. The ultimate goal of cause is from China market to Asia market, and eventually to world market. Thus, the implication of ECFA is important and mutually benefited for both sides across the Strait to cooperate and prosper together in global business.

Though ECFA formalizes and institutionalizes cross-strait economic relations, the political power and economic scale between the two sides differ greatly. Thus, up to the moment the economic relations between Taiwan and China remains asymmetric in nature, that is, China opens more items and less restrictions than Taiwan does. In the long run, it will slow down Taiwan's path for further economic liberalization and hinder the steps for Taiwan to negotiate trade with neighbor countries and thus jeopardize Taiwan's participation in the regional economic integration. Taiwan is a small and resource-scarce economy, opening up is the only strategy for survival and development. It has been showed that small and open economy benefits most under globalization, and past five decades of Taiwan's economic developmental experience was typical evidence. Therefore, how to enlarge Taiwan's international space in trade and investment is very critical for Taiwan's future development. Under the wave of globalization and the surge of regional integration, any country which excludes from regional integration will be marginalized and the disadvantage and damage will be larger the greater the domain of integration. In the past, countries in Asia form production networking through market-driven force, but today institutional arrangement, either bilateral or plural lateral, seems an inevitable and formidable way for consolidated economic integration. As a result, Taiwan cannot bear the loss of exclusion from Asian regional integration. Taiwan's government should have the obligation to let its people understand the benefits and costs of participation in regional integration, promulgate to reach consensus and get ready to participate as a responsible and reliable member of the integrated region.

The incumbent Taiwanese government adopted diplomatic truce policy with China, and this result reduces money game between two sides to attract diplomatic allies significantly and maintains a stable and formal diplomatic relations with the existing partners. In fact, Taiwan should have more positive attitude and affirmative move to gain more international space, of course, China remains the decisive factor. President Ma has made a big move to improve the cross-strait economic relations resulting in

signing the ECFA with China. ECFA is an important stepping stone for Taiwan's internationalization. Thus, Taiwan cannot have no ECFA, but more importantly Taiwan cannot only have ECFA. In this regard, how to make reasonable and fair arrangements for Taiwan and China joint participation in Asian economic integration is challenging the leaders on both sides.

ASIAN REGIONAL DEVELOPMENT: PAST AND PRESENT

International Division of Labor and Regional Production Sharing in Asia

In the past, trade in Asia is very much market-driven and intra-regional trade oriented. This has to do with the export-led trade policy adopted by Asian economies since 1960s beginning with NIEs and then followed by ASEAN and China. The flying geese development paradigm in 1970s and 1980s reflected the concurrent growth in hierarchical order of Asian economies lead by Japan through foreign direct investment. Petri (2012) shows that intra-Asian foreign direct investment is dominated by flows from high technology economies to medium technology economies. The diversity of Asian economies in their development stage and endowments encompasses different comparative advantages along the supply chain which provide the opportunity to form the regional production networks within East Asia and then export to meet the final demand of the Western markets. It is this type of open regionalism that facilitates trade in intermediate goods by forming regional production sharing. More importantly, utilizing its size to realize the economies of scale and unlimited cheap labor supply in assembly and production, China has become a regional production center and world factory. The rise of China in the 1990s reinforced intra-regional trade in East Asia and vertical division of labor is the driving force. Asian trade more and more centered on China. Parts and components have become the major trade in East Asia, and their imports are growing more rapidly than their exports, see Fig. 3. Moreover, with the standardization and modularization of electronics and IT-related products, among those traded goods, machinery and transport equipment is the leading sector in both China's exports and imports with a corresponding share of 47.44% and 43.16%, respectively. Moreover, 73.89% is imported from Asia and 44.47% is

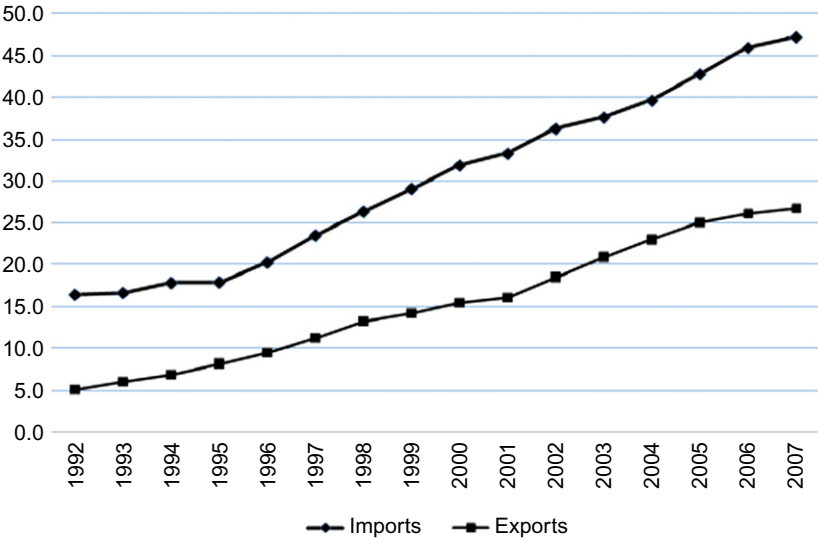


Fig. 3. Share of Parts and Components in China's Manufacturing Trade with East Asian Countries, 1992–2007 (%). Source: Athukorala (2010, Fig. 2).

exported to Asia. This rigorous intra-industry trade in machinery and transport equipment implies an international division of labor among Asian economies and an important role played by China as the world factory for assembly. Thus, the rise of China promotes international division of labor and regional production sharing and facilitates the process of regional economic integration in East Asia.

However, the triangular pattern of trade under open regionalism in East Asia makes the region more vulnerable to the external shocks. For example, the 2008 global financial crisis has hit the Asian economies severely especially those highly open economies, such as China, Japan, and Taiwan. Recent data also show no sign of decoupling of Asian economic growth to the Western markets.³

*The Institutional Arrangement for Economic Cooperation
in Asia since 2000*

The first institutional arrangement for economic cooperation in Asia is the forming of the Association of South-East Asian Nations (ASEAN)

organized by 10 nations, in 1967. However, these 10 nations have a great divergence in many aspects such as history, politics, culture, and religion in particularly each with different socioeconomic development stage. Later, they further proposed to form an ASEAN FTA (AFTA) in 1992. As these countries are very diverse in many aspects and ASEAN as a group is less organized, institutionalized, and loose-fitting. Thus, it requires an unambiguous and well-defined development strategy if it want to become an ASEAN Economic Community by 2015. The 1997 Asian financial crisis is another triggering factor for consolidation of economic integration as many key members of ASEAN, such as Thailand, Indonesia, and the Philippines, all suffered from the crisis. The exposure of the fragility of Asian economies under the crisis was a wake-up call for integrated economic cooperation in the region. The Chiang Mai Initiative in 2000 was a first response to the issues.⁴

The rise of China in the 1990s accelerated and reinforced the regional product networks in Asia through investment and trade. From ASEAN's perspective, enlarge the existing integration by cooperation with countries outside the ASEAN turned out to be an effective way to promote further domestic reform under external pressure and strengthen integration of inside members. In addition, the slowdown and setback in multilateral trade negotiation under WTO in the late 1990s and early 2000s had activated bilateral or plural-lateral trade agreements at regional or cross-regional level. Moreover, after China's accession to WTO in 2001 China had realized that regional integration may be the best way for China to cope with globalization by adopting the strategy to have economic cooperation and integration with neighboring countries. Of cause, the very long run strategy for China confronting globalization is that big power is the key, neighboring partner is the primary, and developing country is the foundation. In terms of the path of economic cooperation, China is slow and lagging behind, China only has 12 FTAs and none of their partners are big powers due to geopolitical and diplomatic relations, no to say that the rise of China may also imply the treat of China to the region and the world as the expansion of military build-up keep increasing along with its accelerated economic growth. Under these circumstances, neighboring and developing countries such as ASEAN becomes first priority on its top list for economic cooperation.

For ASEAN, China is the major importer of their intermediate goods and materials, and economic cooperation with China can attract more FDI from abroad and prevent ASEAN being marginalized due to the rise of China as the world factory. As a result, ASEAN and China signed

Comprehensive Economic Partnership Agreement (CEPA) in 2002 and later concluded in 2010. This process is called ASEAN plus 1, namely China. The process of ASEAN Plus has the purpose to avoid the competition between China and Japan for being leader or hegemonic power of the region and it also reflects China's intention for general perception of the peaceful rise of China. This includes an important cooperation in infrastructure building between China and countries such as Myanmar, Vietnam, Laos, and Cambodia along with China's policy moving toward the development of inner and western parts of China. Of course, for China to form a greater Chinese economic circle or CFTA is even the core for its regional integration, in June and October, 2003 China assigned CEPA with Hong Kong and Macau, respectively, and later on June 29, 2010 signed Economic Cooperation Framework Agreement (ECFA) with Taiwan to normalized and institutionalized *de facto* economic integration across the Strait.

ASEAN plus China is an economic integration between two developing economies with 1.7 billion of population, 2 trillion in GDP, and 1.23 trillion of trade. This is the largest economic integration among developing countries. However, there is a major difficulty that they are all export-oriented economies heavily relying on export of final goods to Western advanced economies such as the United States and EU. The integration between China and ASEAN is purely on production sharing of upstream parts and components and downstream assemble. Thus, any causes lead to economic slowdown in the Western countries will generate profound effect on China and ASEAN, that is, the integration is vulnerable to external shocks.

The formation of ASEAN plus China has helped intensify the strength of billows and waves for the process of institution-led integration in the region. It promotes another two ASEAN plus one, namely ASEAN plus Japan and ASEAN plus Korea. Later it becomes ASEAN plus three. To secure its position in the region, China further negotiated with Japan and Korea to form CJK FTA, the most advanced and largest in economic scale in the North-East Asia. This is by far the most influential and highest economic benefit sub-regional integration agreement in Asia. This move has challenged the position of ASEAN as the hub of Asian economic integration. Fearing being marginalized, ASEAN further advocate the enlargement of the regional integration process by including three additional partners, Australia, New Zealand, and India, to form ASEAN plus six or the so called Regional Comprehensive Economic Partnership Agreement (RCEP) to consolidate ASEAN's center position in the ASEAN plus process. Thus, RCEP is the largest FTA based on economic interests in Asia.

Toward a Regionally Centered Economic Growth

The future development of East Asia heavily relies on its internal market as the driving force for the region like NAFTA and EU did. A self-sustained Asian community requires a huge domestic market with sufficient purchasing power and China with its large population and mass potential consumption capabilities is likely the momentum of Asian domestic market. In order to do that, China has to swift its development strategy from an outward-oriented to an inward-oriented and consumption-based and gradually reduces its dependence on exports to the Western markets allowing a balance growth path of consumption, investment, and exports to sustain its long term growth.

The center of world economic activity will increasingly shift to Asia. Shocks to the U.S. and European economies, or stagnation of these economies, will have less and less impacts on Asia. In 2009, 22.0% of China's exports of goods went to European Union and 18.38% to the United States. For Asia to be self sustainable, the export-oriented strategy adopted by most Asian economies need to switch focus more on serving the intra-regional markets, especially the consumption market. As China developed by increasing the purchasing power of the economy and with the accession to WTO, China has the potential capacity to transform the economy from world factory to regional consumption market. This change will benefit the region by re-strengthening regional production networking on the one hand and increasing intra-regional trade on the other hand, both would definitely not only stabilize Asian regional development but also reduce possible damages generated by external shocks.

The recent global Financial Crisis started at the third quarter of 2008 caused by the 2007 sub-prime mortgage loans crisis in the United States has gradually transmitted to the global real sector. As a result of sluggish world demand of merchandise trade due to credit crunch and the shrink of individual's wealth, export-oriented Asian economies suffered from a serious hit. In January 2009, China's exports dropped by 17.5%, the largest decline since 1994. In order to stimulate exports, some Asian economies have devalued their currencies. For example, as of early February 2009 the Korean Won had fallen 31% against the U.S. dollar in the past year. Devaluation game is not the appropriate policy at the moment as the decline in exports was mainly caused by the income effect of sluggish external demand not the price per se. The proper policy should collectively increase the domestic consumption of Asian economies as a whole to stimulate domestic demand instead of exports.

It is the time to change the twisted structure of the West being engaged in excess consumption, while Asian economies continuously produced and supplied cheap products to the West and saved their earning from exports as foreign reserves to finance the borrowing from the West. Incidentally, the global financial crisis actually provides a precious opportunity to change China from world factory to consumption market which is beneficial to the Asian economy and the formation of Asian regional integration.

Toward a Better Regional Architecture for Economic Integration

The Rebalancing Strategy of the United States in Asia

The United States is against the forming of any institutional configuration of East Asian economic cooperation worrying that it may strengthen regional independence and thus leads to destructive trade wars and jeopardize world free trade system. Moreover, the rise of China implies that China may become the de facto leader in the ASEAN Plus process in the future and a threat to the regional stability. This view is actually shared by most of the Asian economies. As a result, the intension of the United States to reengage in the region is obvious and also welcome by the region except China. Indeed, the Trans-Pacific Partnership (TPP) is the most likely platform for the United States to return to Asian economic community and a means to address long-standing U.S. interests in Asia. The recent speech of Japanese Prime Minister Shinzo Abe pointing out that Japan should join TPP is a typical example from this perspective. Former Singapore Prime Minister Lee Kwan Yew, has also urgently warned that unless the United States becomes more engaged in Asia, through reassuming leadership for APEC and other trans-Pacific institutions, China will inexorably emerge as the regional hegemon to the detriment of United States – and the rest of Asia's – national interests. In this regard, the most likely result would be the advocate of a more open and comprehensive Asia Pacific-wide FTA (FTAAP), accounting for more than three billion people and over half of global GDP.

TPP is an important platform for the U.S. rebalancing strategy in Asia. Some may even consider TTP as important economic strategy to block and mitigate China's influence in Asia as its high quality required standards and institutional design is to exclude China's participation. There are two extreme views on whether RCEP and TTP are substitutes or complements? As the two major players, China and the United States, are against each other, one believe that basically there should be a competition

between the two super powers and thus end up with substitutes. However, I am inclined to the other side that consider they are complements as many members are joining the two sides and the number will increase over time, thus mutual interests for cooperation are the most likely outcome in the future. For example, Japan had agreed to participate in TPP and Korea is considering joining too. [Petri, Plummer, and Zhai \(2012\)](#) also find that both RCEP and TPP would generate significant benefits for members as well as reward enlargement for both current and future members.

In fact, Japan benefited most from this new wave of regional integration by attending both RCEP and TPP as Japan are considered to be passive and lagging behind China in regional integration. It is intuitive that enlarge one's participation in regional integration the larger the number of members the better the economic benefit. In contrast, any one exclude from the integration process will be marginalized and the greater the domain of integration the worse economic loss.

However, there is a big difference between RCEP and TPP. TPP is a high-quality and high-standard FTA, its major focuses are usually beyond traditional trade and investment by containing issues related to IPR, labor protection, government procurement, state-own enterprises, environmental protest and control, etc. RCEP, in contrast, is more pragmatic focusing on traditional trade and investment and more loose and flexible allowing different designs, such as exclusions or special treatment for certain sensitive items or industries, to fit different countries' needs and in accordance to their development stage. In this regard, RCEP is more appropriate and benefited economically than TPP for Asian economies. However, the United States remains the largest trading partner for the export-oriented Asian countries, and moreover the United States is also their political ally for their national and regional security in particular against the threat of China.⁵ Thus, attending TPP has its political and economic reasons for Asian countries. Therefore, participation simultaneously in both RCEP and TPP is the most likely solution for Asian economies. In fact, if RCEP and TPP are further merged into Asia-Pacific FTA, this regional-wide institutional arrangement will benefit all participants including China and the United States. I am optimistic to this win-win solution as the number of members joining both sides will definitely increase over time. In the short run, any contest or competition for leadership and dominance between the two super powers may be inevitable. Then, of course, RCEP and TPP, which consist 28.4% and 29.3% of world GDP, respectively, remain the two most important and competing platforms for regional cooperation and integration in Asia.

THE IMPLICATIONS FOR THE FUTURE ASIAN ECONOMIC INTEGRATION: A CROSS-STRAIT PERSPECTIVE

As Taiwan is excluded from both TPP and RCEP at the moment, Taiwan will be marginalized in the long term if Taiwan remains status quo. Taiwan's marginalization is not in the common interests of the region and the United States, and it may even jeopardize the stability of regional security due to Taiwan's important geopolitical location in the region. In terms of economic benefits, the gains is higher from RCEP than TPP for Taiwan as RCEP represents the regional production networking and sharing in the region and Taiwan is an active player in the region. Of cause, Taiwan would like to join both if possible. We all know that why Taiwan cannot participate in RCEP is mainly due to China factor for political reason of one China policy. Since second power turnover by KMT that Mr. Ma Ying-jeou won the presidential election in 2008, under the 1992 Consensus between KMT and CCP, both sides have reached 21 agreements. The signing of Taiwan-China ECFA in 2010 is an important step to improve and institutionalize cross-strait economic relations. However, even both sides have direct dialogue but still lack of mutual trust, which may postpone or even interrupt further cooperation due to any incidental event. The leader of the two sides should have the wisdom to set aside the twisted and complicated political dispute and concentrate on mutual benefits of economic cooperation to smoothly transform the economic structure of China and Taiwan by aiming at Chinese domestic consumption market first, then at Asia market and final at world market. There are lots of opportunities for cross-strait industry cooperation to form a complete supply chain, to do joint R&D, to create product standard, and even to development brand-name jointly. Currently, China only signed and concluded twelve FTAs with mostly small economies. If Taiwan and China can work and cooperate together, it is not only good for the domestic development but can also facilitate the internationalization of both sides across the Strait. The peaceful solution for internationalization by both sides can also generate the good image of the peaceful rise instead of the threat of China for the neighboring countries in the region.

What Can Taiwan Do for the Region?

For the development of an integrated Asian consumption market, Chinese consumption market is in particularly relevant as China has the largest

population of potential middle class about three to four hundred million people. However, at the moment Chinese domestic markets are relative segmented and regional disparities in income, education, and health-care are widening as the economy developed after thirty years of economic reform emphasizing on the local special economic zones and coastal-area development approach, which leads to over-investment and excess capacities. The China's Twelve Five-year Plan (2011–2015) intends to shift development strategy from outward-oriented to more inward-oriented and change industry structure from labor-intensive to more capital- and technology-intensive with special emphasis on the seven strategic industries. In fact, the development of Chinese domestic consumption market requires closer coordination and cooperation of manufacturing and service industries. However, service sector is relatively less developed and downplayed in the past of China's rapid industrialization process. To smooth the structure transition of Chinese economy, the cooperation of Taiwanese firms in China is relevant as Taiwan shares common language and culture with China and Taiwanese firms have heavily engaged in doing trade and investment with China since 1990. This de facto closer economic tie between Taiwan and China is basically through vertical integration of industries by the full play of division of labor across the Taiwan Strait.

To better serve domestic consumption market a complete upstream-downstream supply chain management, including innovation and branding, product design, assembly and production, marketing and logistics services, is critical and needs the combination of both hard power and soft power. In this regard, the industry cooperation by taking comparative advantage of both sides, China in basic research and production and Taiwan in design, applications, and services, should be a win-win solution and mutually benefited. The stability across the Strait should be conducive to the regional stability as well.

Moreover, Taiwan can also contribute to the Asian regional integration in many aspects. Since the end of WWII, Taiwan had gone through the rapid industrialization process in the 1960s and 1970s and became a solid manufacturing base. Since the mid-1980s Taiwan's industry structure has started to change into service-oriented, and service sector now occupies 70% of GDP as the most of the advanced countries do. Thus, based on Taiwan's 50 years of developmental experience, Taiwan can be a technology provider of appropriate technology for the emerging Asian countries and a resource coordinator for the region. Most importantly, Taiwanese economy is centered and characterized by the small- and medium-sized enterprises which are also the backbone of most emerging economies

desperately needed for technology transfer and spillovers. Moreover, Taiwan knows China better than any countries in the region. China is a socialist centrally planned market economy, and there are lots of uncertainties and market risks involved in doing business especially in the Chinese fragmented domestic markets. Thus, Taiwan can be a gateway and risk buffer for any foreign firms trying to enter Chinese market by reducing the explicit and implicit transaction costs which may arise.

THE ROADMAP FOR TAIWAN AND CHINA JOINTLY PARTICIPATES IN ASIAN ECONOMIC INTEGRATION

How Taiwan and China can work out to collectively participate in Asian economic integration is very critical at the moment. Both sides should have the wisdom to find a win-win solution, which is a reasonable and fair arrangement as described several times in public by the Chinese leaders.⁶ Here, I propose a roadmap with several possible paths for Taiwan and China jointly participate in regional integration.

First, Cross-strait customs union: as Taiwan and China are members of WTO, hence both can form a custom union under separate customs territory status, which escapes the trouble of independent state or country sovereignty dispute.⁷ However, being members of a customs union they should adopt a common policy with each other. This could be difficult for Taiwan as the current trade agreement under ECFA is rather asymmetric across the Strait. Taiwan opens less and restricts more for Chinese products, while China opens more and restricts less for Taiwanese products. Due to political reason and asymmetry in economic size, Taiwan is not quite possible to accept equal treatment of trade and investment policy across the Strait. However, China needs to abandon the concept of state, which may also difficult to follow.

Second, The Greater Chinese economic circle or Chinese FTA: Great China includes Mainland China, Hong Kong, Macau, and Taiwan; it is consistent with China's internationalization strategy that start from the center and gradually to the peripheral. The greater China is the core center and thus the forming of greater Chinese FTA is the top priority of China. This is why China persistently urges Hong Kong to sign FTA with Taiwan. However, in this way Taiwan is afraid of being like another Hong Kong to China. Taiwan has to build up its self-confidence not to be unified by China in this way. Of course, using separate customs territory status under

WTO is a possible solution for greater Chinese FTA. For China, this second path is better than the first one as it fits China in international FTA strategy.

Third, CJK plus Taiwan: CJK is a very important FTA for North-East Asia, Korea gains most in CJK and Taiwan suffers most as Taiwan and Korea share similar export structure. China and Korea had reached a FTA agreement in November 2014 and China-Japan FTA and Japan-Korea FTA may take longer time to sign. The participation of Taiwan with CJK can facilitate and smooth the process as Taiwan knows China well and is quite friendly with Japan and Korea. The inclusion of Taiwan will reduce Japan and Korea's fear for the aggressive attitude of China and Taiwan can be a trustworthy middleman for the negotiation. In fact, the formation CJK FTA will accelerate the process of marginalization of Taiwan, and this result definitely is not what China would like to see in this way. Among the exports to China by Taiwan and Korea, 63% of items are overlapping, particularly in petrochemical products, machinery, and LCD panels. For Taiwan, Japan, and Korea, it is Taiwan that China would like it to benefit most among them. Therefore, having Taiwan's inclusion in CJK negotiation should be welcome by China provided the issue of country sovereignty is solved first.

Lastly, ASEAN + China + Taiwan: this could be the best solution path. The forming of ASEAN + China + Taiwan has a very important strategic meaning as Taiwan can play a pivotal role to facilitate Asian regional integration especially for those late comers in the region. It can build a complete supply chain that China as the final consumption market, ASEAN as the production base, and Taiwan as a coordination and distribution center. This combination reinforces the complementary relationship among each of the three partners according to their comparative advantage. For the late comers, based on Taiwan's successful industrialization experience in the 1960s and 1970s Taiwan can provide them with appropriate technology for industrialization. As for China, based on Taiwan's past experience of post-industrialization process since the mid-1980s, Taiwan can help the structure transformation of China from outward-oriented and manufacturing-centered economy to inward-oriented and consumption- and service-based economy. Moreover, Taiwan can be the resources coordinator and logistic and management center for the cluster based on its internationalization and globalization knowledge. Hence, giving Taiwan more international space is conducive to China's internationalization. China should realize that the disappearance of Taiwan in international arena is totally a loss to China and the region.

Taiwan is a small and open economy, and globalization benefits Taiwan's development in a great extent. Thus, Taiwan's exclusion from regional economic integration will be a tragedy as Taiwan will be marginalized gradually, which will slow down the path for regional economic development and jeopardize regional security as well. In fact, Taiwan should participate in both RCEP and TPP, especially the most profitable RCEP as the first priority. This internationalization strategy is so critical for Taiwan's future development that any political party who becomes the ruling party still have to put it in top priority. Of course, we would like to see the union of RCEP and TPP to become FTAAP, a real APEC-wide FTA for the region and a win-win solution for the two platforms.

*What Can Leaders from China and Taiwan Do for Them
and for the Region?*

The major problem of both sides across the strait is the lack of mutual trust. The recent dispute in service trade pacts under ECFA is a good example. Any economic agreement between only Taiwan and China will be considered by Taiwan eventually leading to political unification. For China, however, giving more space in the international organizations or participations to Taiwan may imply that Taiwan will seek for independence. Thus, from China's perspective institutional arrangement between both sides should be suffice and a greater Chinese economic zone will do. In fact, Taiwan is a small and open economy and internationalization is the only way for Taiwan to thrive. Therefore, Taiwan's leader should persuade China that Taiwan needs more room for internationalization not because of seeking independence; moreover Taiwan's participation in the region not only is good for China's further internationalization but also benefits the region as mentioned above.

Recently, in order to enlarge and facilitate its internationalization in accordance with the world standard, both China and Taiwan adopted a strategic move by launching China (Shanghai) Pilot Free Trade Zone and Taiwan's Free Economic Demonstration Zone in 2013, respectively, hoping that its development experience, particularly in the liberalization of service sector, can be replicable to the rest of the nation. Therefore, a zone-to-zone cooperation should be conducive for both sides' domestic structure transformation of service sector and its internationalization in the future. As a result, the zone-to zone experiment can be an important vehicle for both sides to create mutual trust through mutual assistance in accessing global

market and collectively participate in the regional and global economic integration. Under current architecture of regional cooperation, as proposed here ASEAN+China+Taiwan and CJK+Taiwan should be seriously taken into account by both sides, and it should be a win-win-win solution for all (Taiwan, China, and the region). It should be clear also that it will solve the current deadlock in service and commodity trade agreements between Taiwan and China. Of course, a meeting between two sides' leaders, Ma Ying-jeou and Xi Jinping, could be considered a smart move toward that direction. It definitely requires the wisdom of the leaders from both sides.

Finally, it should be clear that China is very important for Asian regional economic development as China is not only a world factory but a world market in the future as well. From either demand side or supply side of markets, Asia heavily depends on China. However, fortunately or unfortunately, for regional peace and security Asia urgently needs the United States to balance the regional powers. That is another reason why we have both RCEP and TTP in Asia. In the long run, the United States cannot sustain as the single hegemony power in the world as the economic power of the United States is declining over time, even the adoption of quantitative easing monetary policy cannot change the underlining structure problem in the United States. For national security reason, every year Asian countries have to spend a large amount of money on national defense and weapon procurement, which is a distraction of resources from economic development. If Asian countries can develop a close and common-interest economic relationship with China which may result in a peaceful and harmonious environment for the region, then the risk of military confrontation or war can be minimized. This is a major question not only for Taiwan but also for all Asian countries facing the rise of China. No country in Asia or the whole world knows China better than Taiwan, which has a fruitful development experience and has gone through a complete process of industrialization in the 1960s and 1970s, re-industrialization in the 1980s, and de-industrialization since 1990s. Based on these experiences, Taiwan can contribute a lot to the region as well as the world economy, especially for accelerating the process of economic integration in the region. Taiwan is a Formosa and it can be the lighthouse of the region and a spotlight of the world provided that Taiwan participates actively in the regional and world economic arena. From both economic and political perspectives, thus the collective participation of Taiwan and China into Asian regional integration network will be conducive to the peaceful development of the region and the world.

CONCLUDING REMARKS

This chapter investigates the evolution of cross-strait economic relations and Asian regional integration and its implications for future development in the region. Politically, the lift of Martial Law in 1987 and economically the process of de-industrialization in late 1980s caused Taiwan to start FDI and trade with China. Then the cross-strait economic relationship was characterized by vertical division of labor that Taiwan produced parts and components and China conducted final stage assembly. Despite Taiwanese government's intervention by adopting restricted trade policy toward China after 1996 based on national security reason, trade, and investment between Taiwan and China continued to surge over time. China had become Taiwan's largest trading partner after 2001 surpassing the United States. However, this *de facto* cross-strait economic integration was eventually normalized and institutionalized by signing ECFA on June 29, 2010.

Likewise, trade and investment in Asia is fundamentally market-driven and cross-border FDI is the major driving force with Japan and the NIEs being the key players. This investment-induced trade link has caused intensive trade in intra-industry and intra-region in Asia. The rise of China in 1990s with the assistance of Taiwanese firms further accelerated the trend of integration by forming regional production networks. However, 1997 Asian Financial crisis revealed the vulnerability of Asian economies to external shocks, and hence the need to have economic cooperation among Asian economies to stabilize the regional development. Given a series of setback of multilateral trade negotiations under WTO since late 1990s, after 2000 institutional arrangement like bilateral- or plural-lateral FTA emerged as the effective way to facilitate trade and investment for regional development. The signing of ASEAN and China CEPA in 2001 triggered the process of "ASEAN plus" for regional economic integration. Over the years, RCEP under the process of ASEAN Plus Six and TPP led by the United States as its strategy of rebalancing Asia have evolved as the two major platforms for Asian regional cooperation with two key players, China and the United States, on each side, respectively.

We argue that in the long run the win-win solution that the two platforms will further merge into FTAAP which benefits all participants including China and the United States. However, in the short run, the process of regional integration needs to be consolidated with more cooperation and less competition. Based on its 50 years of developmental experience Taiwan can play an important role to promote and consolidate Asian regional integration as a technology provider and resource coordinator for the region

and a risk buffer for entering Chinese market. Taiwan's participation will help China's structure change and its internationalization, and bring appropriate technology and know-how to the late comers in the region. We thus propose a roadmap for Taiwan and China to jointly participate regional integration process and how it can be a win-win-win solution for them and the region. This definitely requires the wisdom of the top leaders, Ma and Xi, from Taiwan and China. In the intermediate run, Asian economies need to change the structure toward more regional-centered trade in final goods through domestic consumption market in order to reduce the dependence on Western markets and mitigate any loss may arise from external shocks.

NOTES

1. Taiwanese KMT government under former President Lee Teng-Hui adopted restricted "No Haste and Be Patient" trade policy toward China in 1996 for national security reason. The successor DPP government led by President Chen Shui-Bian from 2000 to 2008 also followed suit by adopting similar restricted trade policy to China.

2. The 1992 Consensus was reached under an unofficial talk in Singapore in 1992 between KMT and CCP, and it means that "one China with different interpretations," that is, only "one China" though each side is free to interpret the meaning of "one China" in its own way.

3. See, for example, [Athukorala \(2010\)](#).

4. In response to 1997 Asian financial crisis, in an annual meeting held in Chiang Mai, Thailand on June 6, 2000 ASEAN, China, Japan, and Korea proposed a multi-lateral currency swap agreement among them to form a regional financial safety net against regional short-term financial liquidity risks and external financial shocks.

5. Recent disputes in East China Sea and South China Sea are examples of the Asian regional security.

6. Reasonable means in accordance with one China principle, and fair implies that Taiwan fairly need more international space for development but not for independence.

7. The official title of Taiwan's membership in WTO is the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu.

REFERENCES

- Athukorala, P.-C. (2010). *Production networks and trade patterns in East Asia: Regionalization or globalization?* ADB Working Paper Series on Regional Economic Integration No. 56, Asian Development Bank.

- Petri, P. A. (2012). The determinants of bilateral FDI: Is Asia different? *Journal of Asian Economics*, 23(3), 201–209.
- Petri, P. A., Plummer, M., & Zhai, F. (2012). *The trans-pacific partnership and Asia-Pacific integration: A quantitative assessment*. Policy Analysis in International Economics No. 98. Washington, DC: Peterson Institute for International Economics and East-West Center.