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Taiwan's Economic Development and

Its Economic Relationship with Mainland China

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Taiwan's Economic Development and Its Economic Relationship with Mainland China*

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I. Introduction

In the period from 1949 to 1993, the relationship between Taiwan and mainland China has changed drastically. Before 1980, the two sides of the Taiwan Straits were in a state of serious hostility. What people in the world focused on when thinking about China was the strong contrast between the two sides: Taiwan had created a miracle of economic development while mainland China was still a poor and backward area. However, from 1980 on, peoples' image of China has gradually changed. Mainland

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China's economy has greatly improved through the implementation of economic reform and the open-door policy. The relationship between the two sides has dramatically shifted from military confrontation to peaceful coexistence and from economic blockade to trade exchange and unilateral investment. Upon entering the 1990s, mainland China has achieved remarkably rapid economic growth while the world economy has been in recession. One wonders whether there is some relationship between Taiwan's economic development miracle and mainland China's rapid economic growth. The purpose of this paper is to attempt to answer this question in the context of (1) the underlying reasons for the mainland engaging in economic reform and adopting an open-door policy, (2) the impact of Taiwan's economic achievement on the mainland's policymakers, (3) the breakthrough of the blockade between the two sides, (4) the recent development of economic relations between the two sides, and (5) prospects for economic relations between the two sides. Finally, some concluding remarks will be drawn from the previous analysis.

II. The Main Reasons Why Mainland China Engaged in Economic Reform

Through the 1980s, all communist countries except mainland China assumed that the communist system was the best political and economic system in the world. In the late 1970s, in contrast, a few mainland Chinese leaders had begun to sense that the

communist system produced only poverty and struggle. They also realized the seriousness of two pressures: the external impact and internal crisis.

1. External Impact

In 1972, when former president of the United States Richard Nixon knocked on the door of mainland China[1], many mainland officials began to have the opportunity to contact foreigners from the western world and learn of the contrasts in economic development between South Korea and North Korea, West Germany and East Germany, and Taiwan and the mainland. Before the 1950s, there were no economic differences between them, but by the 1970s, the differences in their economic achievements were stark. To the mainland, the most important of these great economic achievements was the so-called Asian "Four Dragons."[2] The Four Dragons are characterized by traditional Chinese culture, and, except for in South Korea, the majority of the people involved are Chinese. The entire world recognizes that only the Four Dragons have managed to sustain rapid economic growth. Why, then, did the mainland continue to suffer poverty and backwardness? A definitive answer to this question would have had a great impact on the mainland.

2. Internal Crisis

People in the mainland experienced cruel class struggle and many political movements, particularly from 1958 through 1978. These included the Anti-Rightist Movement, the establishment of people's communes, the Great Leap Forward, the Great Cultural Revolution, etc., which caused worker ethics and labor productivity to

deteriorate and reduced people in the mainland to a desperate condition. The Beijing government realized that if economic conditions could not be improved, both the ruling party and the government would be in danger. In view of economic development trends in the world and the strong desire of Chinese people, the Beijing government had to alter its inappropriate method of development and adopt economic reform measures.

III. The Impact of Taiwan's Economic Achievements on the Policymakers of Mainland China

Since the time Taiwan, as a separate political entity, became an opponent of the mainland, the economic performance of Taiwan has attracted the attention of the mainland. Taiwan's remarkable economic achievements from 1950 through 1980 had a great influence not only on the people of the mainland but also on the policymakers of the Beijing government. Taiwan's economic achievement can be characterized as having high economic growth with equitable income distribution, mild inflation, low unemployment, and sound public finance (see Table 1).

From 1952 to 1980, the average GNP growth rate was 9.22 percent, the highest in the world. During the same period of time, income distribution gradually improved indicating that rapid economic growth did not create unequal income distribution. By 1980, per capita GNP was US$2,344. The unemployment rate dropped from 4.36 percent in 1952 to 1.23 percent in 1980, indicating no unemployment problem. The

Table 1. Economic Indicators of Taiwan

Year	Growth Rate of GNP	Per Capita GNP (Current Value)		Unemployment Rate	Inflation (Rate of Change in Consumer Price Index)	Income Distribution*	Trade Surplus US$ Million
		N.T. Dollar	U.S. Dollar				
1952	12.00	2019	196	4.36			-71
1953	9.34	2602	167	4.13	18.80		-64
1954	9.54	2759	177	4.02	1.70		-118
1955	8.11	3162	203	3.73	9.90		-78
1956	5.50	3502	141	3.65	10.50		-76
1957	7.27	3959	160	3.66	7.50		-64
1958	6.56	4282	173	3.80	1.30		-70
1959	7.75	4782	131	3.82	10.60		-74
1960	6.44	5601	154	4.01	18.50		-133
1961	6.84	6078	152	4.21	7.80		-127
1962	7.89	6498	162	4.11	2.40		-86
1963	9.36	7137	178	4.33	2.20		-30
1964	12.29	8113	203	4.22	-0.20	5.33	5
1965	11.01	8697	217	3.30	-0.10		-106
1966	8.97	9480	237	3.00	2.00	5.25	-86
1967	10.61	10685	267	2.29	3.40		-165
1968	9.13	12151	304	1.72	7.93	5.28	-114
1969	9.05	13783	345	1.88	5.05		-164
1970	11.32	15544	389	1.70	3.55	4.58	-43
1971	13.01	17730	443	1.66	2.83		216
1972	13.38	20885	522	1.49	3.01	4.49	475
1973	12.78	26596	695	1.26	8.19		691
1974	1.16	34974	920	1.53	47.47	4.37	-1327
1975	4.44	36642	964	2.40	5.22		-643
1976	13.70	43033	1132	1.78	2.50	4.18	567
1977	10.25	49449	1301	1.76	7.04	4.21	850
1978	13.99	58282	1577	1.67	5.76	4.18	1660
1979	8.45	69115	1920	1.28	9.76	4.34	1329
1980	7.12	84398	2344	1.23	19.00	4.17	78
1952-80 average	9.22			2.83	7.99		
1981	5.76	98179	2669	1.36	16.33	4.21	1412
1982	4.05	103803	2653	2.14	2.72	4.29	3316
1983	8.65	113103	2823	2.71	1.59	4.36	4836
1984	11.59	125496	3167	2.44	-0.22	4.40	8497
1985	5.55	131430	3297	2.91	-0.40	4.50	10624
1986	12.57	151148	3993	2.66	0.70	4.60	15680
1987	11.87	168114	5275	1.97	0.52	4.69	18695
1988	7.84	181185	6333	1.69	1.29	4.85	10995
1989	7.33	198389	7512	1.57	4.40	4.94	14039
1990	5.02	213888	7954	1.67	4.13	5.18	12498
1991	7.24	235699	8788	1.51	3.62	4.97	13317
1992	6.02	256682	10202	1.51	4.46	5.24	9494
1981-92 average	7.79			2.01	3.26		
1952-92 average	8.50			2.42	5.62		

Source: 1. Taiwan Statistical Data Book 1993, Council for Economic Planning and Development, Republic of China.

2. Statistical Abstract of National Income, Taiwan Area, Republic of China, 1951-1992, Directorate-General of Budget, Accounting and Statistics, Executive Yuan.

*The ratio of the richest division to the poorest division in five equal divisions of family numbers by family income.

inflation rate was also low (except for 1974 and 1980 when hyperinflation was experienced due to the oil crises) and the balance of trade went into surplus starting in 1976. By 1980, it can be said that Taiwan had successfully transformed from a poor society to a rich one.

Taiwan's remarkable economic achievement can be attributed to the following factors:

(1) Social and political stability: This is a key factor in economic development. It is impossible for any country to carry out economic reform without political stability. Since the 1950s, Taiwan has maintained a harmonious and stable social and political condition, and no social or political conflicts have gotten in the way of the process of economic development. This condition has also provided the prerequisite for maintaining a favorable investment climate.

(2) Priority given to agricultural development: Before the 1950s, Taiwan was an agriculturally oriented economy. In consideration of the importance of agricultural development, the government in Taiwan decided to undertake land reform through the three steps of a 37.5 percent rent reduction for main crops, the sale of public land to its cultivators, and the land-to-the-tiller program. The land reform program was successfully completed in the early 1950s and its result was that it greatly raised farmers' productivity and substantially improved their standard of living. Agricultural products and agricultural processing products were the major exports in the early stage of Taiwan's economic development. They earned foreign exchange used for importing raw materials and machinery

equipment to support industrial production.[3]

(3) The encouragement of investment: The shortage of capital was a bottleneck to economic growth. To encourage local investment and attract foreign investment, the government promulgated the ''Statute for the Encouragement of Investment'' in 1960 which exempted businesses from the obligation to pay corporate income taxes for a certain period of time after a new investment project began production. Export processing zones were set up in the 1960s, based on a free trade zone concept in order to reduce the cost of production, thus increasing competitiveness.[4]

(4) The development of small businesses: In Taiwan, although there are many government-run enterprises, there are many more small- and medium-sized enterprises, accounting for 98 percent of the total number of firms. They can cope with the rapid change in external economic conditions in a very flexible way and they are resilient when they encounter difficult problems. They have made a great contribution not only to the expansion of exports but also to the improvement of income distribution. Since the 1970s, the government has begun to pay more attention to the development of small businesses, establishing administrative offices and special banks to provide services to small firms.

The above measures can serve as lessons to the mainland. In fact, the Beijing government has introduced them in the mainland and they have begun to bloom there.

(1) The Beijing government has abandoned the people's communes, letting the land to farmers under the agricultural contract responsibility system and gradually

relaxed price controls over agricultural products. From 1979 through 1984, the growth rate of the agricultural sector was very high, averaging 7.4 percent, and from 1985 through 1992, it was about 4 percent. The standard of living for farmers has substantially improved.

(2) The Beijing government has established a number of special economic zones to attract foreign investment. Local governments have also made use of whatever means they have at their disposal to attract foreign investment. Because of their endeavors, many foreigners have made a large amount of investment not only in the special economic zones but also in the countryside, making a great contribution to the prosperity of the coastal area.

(3) Small businesses have been allowed to develop. Before the 1980s, only the government ran enterprises and no private enterprises were allowed. Since the Beijing government adopted economic reforms, many household-owned firms and township-run firms have been established and have so rapidly developed that they are able to export and compete with government-owned enterprises. Many household-owned firms and township-run firms make a profit while many government-owned enterprises cannot.

(4) Over the last 14 years, the mainland has achieved very high economic growth, improving the people's living standard. This can be attributed to many factors, but political stability should be considered the most important.

From the above analysis, we can see that the experience of Taiwan's economic development has been duplicated in the mainland.[5]

IV. Breakthrough of the Blockade between the Two Sides

As mentioned before, it was strictly forbidden that the two sides of the Taiwan Straits from 1949 to 1980 have any communication whatsoever. However, the blockade between the two sides was broken first by the Beijing government in 1979 and then by the Taipei government in 1987.

On January 1, 1979, the Chinese communist party issued ''A Letter to the People in Taiwan'' concerning peaceful unification of the fatherland, calling for direct postal, trade and transport links between the two sides.[6] In September 1981, Marshall Yeh Chien-Ying, in his capacity as chairman of the Chinese Communist Standing Committee of the People's Congress forwarded a nine-point proposal which, among other things, suggested that the Chinese Communist Party and the Nationalist Party should hold party-to-party talks. Two years later, the Chinese communist leader, Deng Xiaoping proposed his ''one country, two systems'' scheme for uniting China, while at the same time refusing to renounce the use of force against the Taiwan area.[7]

To these proposals, the Taipei government had no official response until 1987. In November 1987, the Taipei government lifted martial law and announced that residents in the Taiwan area would be permitted to visit relatives on the mainland. In July 1988, the ruling party in Taiwan passed a proposal for ''Mainland Policy in the Current Stage'' and in September 1990, the Taipei government established the ''National

Unification Council.'' In January 1991, the ''Mainland Affairs Council'' was set up and the formation of a private nonprofit organization, ''The Straits Exchange Foundation,'' which is responsible for dealing with general affairs for the people, was approved.

Obviously, the policy measures taken by the authorities of the two sides have broken through the blockade between the two sides and opened the door to indirect trade and unilateral investment. No doubt, this drastic change is historically significant.

V. Recent Developments in Economic Relations between Taiwan and Mainland China

Before 1979, due to military confrontation, there was no trade between Taiwan and the mainland and any transaction was illegal and subject to strict punishment. However, since 1979, when the Beijing government initiated economic reform and the open-door policy, indirect trade between the two sides began to take place through Hong Kong and smuggling activities also increased. Total trade amounted to US$0.78 million in 1979. With the lifting of martial law in 1987, bilateral trade through Hong Kong has substantially increased. By 1992, it amounted to US$7,406.9 million and Taiwan's trade surplus with the mainland was US$5,169 million, accounting for 54.4 percent of the total trade surplus of Taiwan. In a matter of just a few years, Taiwan's trade has come increasingly to depend on the mainland market. In 1992, the degree of export dependence on the mainland was 7.72 percent while the degree of import dependence on

the mainland was 1.55 percent. It should be noted that from 1977 to 1990, the trade surplus with the United States was larger than the trade deficit with Japan. Since 1991, the trade surplus with the United States is no longer larger than the trade deficit with Japan. The trade surplus with the mainland is used to make up the difference (see Table 2).

So far, the investment relationship between the two sides is still unilateral, meaning that only Taiwanese businessmen have made investment in the mainland and not vice versa. Before 1985, no records exist indicating the extent of investment in the mainland. However, since that time, unilateral and nondirect investment has begun to take place.[8] Most of this investment has been made in Guangdong and Fujian provinces through agencies in Hong Kong, Singapore, Bangkok, and Japan so as to protect operations and profits earned in the mainland and avoid judicial disputes with local governments and Chinese partners. Recently, Taiwan's investment has extended to Jiangsu, Shandong, Hainan, Shanghai, Wuhan, and Sichuan. As for an estimate of Taiwan's investment in the mainland, no reliable data exists. According to the Ministry of External Trade of the Beijing government, the accumulated amount of agreed investment by Taiwan's businessmen is US$9 billion (see Table 3).[9]

Nondirect investment made in the mainland is essential not only to the mainland but also to Taiwan. The Tiananmen Incident resulted in a sharp decline in investment from many western countries. Investment from Taiwan has filled the gap and produced a stimulating effect. At the same time, many small Taiwanese businesses have moved

Table 2. Commodity Trade between Taiwan and the Mainland Through Hong Kong

unit: US $ million

Year	From Taiwan to Mainland		From Mainland to Taiwan		Trade Balance	
	Amount (1)	As % rate of Increase	Amount (2)	As % rate of Increase	Amount(3) (1)-(2)	As % of Total Trade
1979	21	--	55	--	-34	--
1980	242	1037.80	78	40.65	164	51.25
1981	390	61.07	76	-2.82	314	67.38
1982	208	-46.65	89	17.90	119	40.06
1983	168	-18.98	96	6.77	72	27.27
1984	425	152.38	127	33.04	298	53.99
1985	987	132.13	116	-9.16	871	78.97
1986	811	-17.92	144	24.25	667	68.84
1987	1226	51.27	289	100.47	937	61.85
1988	2242	82.81	478	65.68	1764	64.85
1989	2896	29.18	596	22.60	2310	66.34
1990	3278	13.18	765	30.41	2513	62.16
1991	4667	42.37	1126	47.19	3541	61.13
1992	6288	34.73	1119	-0.62	5169	69.79

Source: The Hong Kong Government, Statistics Department.

Table 3: Taiwan's Investment in Mainland China

Unit: US$ Million

Year	Items of Agreed Investment (1)	Amount of Agreed Investment (2)	Average Scale (3)=(2)/(1)
1983-1987	80	190	2.38
1988	435	520	1.20
1989	552	437	0.79
1990	1011	892	0.88
1991	1737	1391	0.80
1992	6430	5540	0.86
1993 1-3 month	1755	1030	0.59
Total	12000	10000	0.83

Source: The Ministry of External Trade, PRC.

to the mainland in order to survive and develop since they have lost their competitiveness in the world market due to the rapid appreciation of the N.T. dollar against the U.S. dollar by more than 50 percent and the sharp rise in production costs. In fact, the trade relationship between the two sides has been strengthened by the development of their investment relationship, and a vertical division of production between the two sides has accordingly formed.

In addition, many residents on Taiwan have visited their relatives in the mainland and sent money to them. Every year, many people from Taiwan go to the mainland for sightseeing. In 1992 alone, 1.5 million people from Taiwan went to the mainland. This is also helpful to the mainland's economic development.

VI. Prospects for Economic Relations between the Two Sides

The development of relations between Taiwan and mainland China originates from two sources: one is the political consideration and the other is economic demand. The goal of the unification of China is no doubt the most important political consideration. This common goal is helpful in lifting many barriers and promoting mutual exchange. The private sector emphasizes economic interests. Bilateral trade and nondirect investment are beneficial to both sides. The mainland can make use of Taiwan's capital, management, marketing, and production techniques while Taiwan can make use of the mainland's cheap labor, raw materials and potential market. This combination creates greater comparative advantages and raises competitiveness. Particularly to Taiwan's businessmen who face protectionism from NAFTA and the European Community single market, the best choice is to take advantage of the productive resources of the mainland on the one hand, and to make use of the mainland's market on the other.

Based on the above considerations, it can be said that the economic relationship between the two sides is promising. If the mainland can maintain an average growth rate of 7-8 percent, and Taiwan can sustain an average growth rate of 6-7 percent in the next decade, it can be expected that the two sides together will form a great economy. In the past five years, many economists have suggested the formation of a "Greater Chinese Economic Sphere." Unfortunately, the governments on both sides are not interested in

this proposition because of political considerations. It is true that a formal Chinese Economic Sphere cannot be established while ideological and political conflicts still exist on the two sides. However, it is possible to have an informal Chinese Economic Sphere if economic relations between the two sides continue to be further improved on the basis of mutual benefit.

VII. Concluding Remarks

Based on recent economic developments, Taiwan and mainland China will still maintain high growth compared to other countries, while the development of their economic relationship will be further strengthened. Before 1990, the mainland economy was deeply influenced by the remarkable achievement of Taiwan's economy, while since 1990, the development of Taiwan's economy seems to increasingly depend on the mainland, which is reflected not only in the volume of trade but also in the volume of investment.

Some people on Taiwan have begun to worry about whether the future of Taiwan's economic development will be subject to changes in the mainland economy. According to the principle that one should not put all one's eggs in one basket, we should diversify our trade as well as our investment. Actually, where to make investment depends on the investment climate and with whom to conduct trade depends on competitiveness. Thus, it is difficult for the government to force changes. From an

alternative point of view, by 2000, the mainland economy will be a market economy and economic liberalization will have materialized. As for who will be the master of all of China, it is not a political party but the people who are capable of choosing an ideal government for themselves.

However, Taiwan itself must maintain high economic growth with equity. In order to achieve this goal, Taiwan must accelerate its technological progress and improve its investment climate and living conditions. Only in this way will Taiwan have the capacity to play a positive role in the process of uniting China.

Notes

1. In 1972, former President Richard Nixon was the first president of the United States to visit Beijing, paving the way for the establishment of diplomatic relations with communist China in 1979.

2. Including Taiwan, South Korea, Hong Kong and Singapore.

3. The strategy of Taiwan's economic development was "developing industry by virtue of agriculture and supporting agriculture by virtue of industry."

4. Export Processing Zones made a great contribution in the creation of employment and the introduction of management skills. As for the introduction of "know-how," however, the scheme failed.

5. This can be seen from the laws and regulations used for economic development. Although not all the laws and regulations of Taiwan have been applied in the mainland, many of them, in revised form, have been utilized as blueprints.

6. The achievement of these three direct links has been rejected by the Taipei government. Right now, they are accomplished through Hong Kong and other foreign ports. If the Beijing government recognizes that Taiwan is a political entity, these direct links can be implemented.

7. The scheme of "one country, two systems" has been rejected by the Taipei government since it implies that the Beijing government is the central government while the Taipei government is a local government.

8. Nondirect investment means that Taiwan's businessmen make direct investment in the mainland in the name of an agency in Hong Kong, Japan, Singapore, or Bangkok. Direct investment means making investment in industrial production. If investment is made in the stock or bond market, it is indirect.

9. It should be noted that agreed investment is not realized investment. The former is based on agreements signed by investors, while the latter is the amount actually arriving in the mainland. According to estimates made by the Taipei government, this amount is much lower.

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