ASSESSING CHEN SHUI-BIAN'S FIRST YEAR:
THE DOMESTIC AND INTERNATIONAL AGENDA

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May 31, 2001

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Assessing Chen Shui-bian’s First Year:
The Domestic and International Agenda

An International Conference
Sponsored by the Sigur Center for Asian Studies
George Washington University

Thursday, May 31, 2001

AGENDA

9:00 AM  Welcome – Bruce Dickson, George Washington University

9:15-10:30  DOMESTIC POLITICS
Presenters:
John Fuhs-sheng Hsieh, University of South Carolina
Shelley Rigger, Davidson College

Discussant:
Bruce Dickson, George Washington University

10:45-12:15  DOMESTIC ECONOMICS AND INTERNATIONAL TRADE
Presenters:
Karl Fields, University of Puget Sound
Alexander Tan, University of North Texas
Steve Waicho Tsui, National Chengchi University

12:30-1:45  LUNCH
Speaker: C.J. Chen, Representative, Taipei Economic and Cultural Representative Office

2:00-3:15  CROSS-STRAIT RELATIONS
Presenters:
Chien-min Chao, National Chengchi University
Suisheng Zhao, Washington College and Colby College

Discussant:
Ying-mao Kau, Taiwan National Security Council
Robert Sutter, National Intelligence Officer for East Asia

3:30-5:00  FOREIGN POLICY ISSUES
Discussants:
Shih-hsiung Chow, Institute of National Policy Research, and Institute of China Studies,
National Sun Yat-Sen University
Minxin Pei, Carnegie Endowment for International Peace
David Shambaugh, George Washington University
Alan Waehman, Fletcher School Law and Diplomacy, Tufts University

6:30  DINNER
Speaker: Harry Harding, George Washington University
The Department of International Affairs

AIA Information Conference

December 11, 12, 13

200 DMA

DOMESTIC POLICIES

Presenters:

[Names of presenters]

DOMESTIC ECONOMY AND INTERNATIONAL TRADE

Panelists:

[Names of panelists]

CROSS-STRAIT RELATIONS

Presenters:

[Names of presenters]

FOREIGN POLICY ISSUES

Discussants:

[Names of discussants]

DINNER

[Location or details of dinner]

Please note: This is an example of a conference agenda. The actual content might vary.
PARTICIPANTS BIOS

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Steve Waicho Tsui is full professor of the Department of Public Finance, National Chengchi University (since 1990), Taipei, Taiwan Republic of China, and also serves as the chair of the department. In addition, he is a course coordinator for the International Center for Land Policy, Studies and Training (a non-profit international institute cosponsored by the Taiwan government and the Lincoln Center on Land Policy, Cambridge, MA), Taoyuan, Taiwan, on the regular session of local public finance and taxation. From 1987 to 1989, he was the Director of the First Research Division, Tax Reform Commission, Ministry of Finance, Taiwan. His major research interests and publications are on the fields of public finance reform, economic development as well as economic relationships of the three economies across the Taiwan Strait.

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Assessing Chen Shui-Bian’s First Year: 
The Domestic And International Agenda

Introduction

Bruce J. Dickson

Many people who follow international affairs are familiar with the “Taiwan issue,” but they often have a rather one-dimensional notion of Taiwan’s situation. Taiwan is not just an issue in US-China relations, although it certainly is that. It faces various political and economic challenges that are often overlooked or poorly understood.

- It is often referred to as a “model of democracy,” but upon closer inspection it has major uncertainties and adjustments now underway. While these adjustments do not threaten the survival of its democracy, they do raise questions about whether the inner-party and intra-party rivalries benefit its democracy, whether partisan debates will sour public opinion toward politics, and whether Taiwan’s institutional arrangements are conducive to good governance.
- Taiwan is also noted for its rapid development and commitment to market principles, but many do not appreciate its importance to the US economy or how political factors often impinge on the market. US exports to Taiwan are approximately 40 percent higher than exports to China, and Taiwan is a major supplier of computer and other high tech components. Taiwan’s economy is heavily influenced by its politics, including the immense holdings of the KMT, the absence of a central bank and other regulatory devices free of political pressure, and political stalemates that slow the adoption of necessary reforms.
- While national identity remains an essential element of Taiwan’s politics and diplomacy, the simple dichotomy of “unification vs. independence” is a false one. Most people in Taiwan realize that these extremes on the spectrum of options available to Taiwan are highly unlikely, and they are searching for some type of accommodation that would be acceptable on both sides of the Taiwan straits.
- While Taiwan is often portrayed in the media as a “renegade province,” this term is not used by China itself. While it is not too wide of the mark, the description overlooks the important nuances and complex relations between China and Taiwan.

On May 31, 2001, the Sigur Center for Asian Studies hosted an international conference to assess Chen Shui-bian’s first year in office. It provided an opportunity to review his record so far, to consider the impact of the new Bush Administration on US relations with both Taiwan and China, and to anticipate future events, especially the December 2001 Legislative Yuan elections and how their outcome may influence Taiwan’s domestic and international agenda of issues. The papers presented and the discussion they generated helped shed light on some of the political, economic, and diplomatic issues noted above. By providing the papers and a summary of the conference discussions, I hope you will gain a better understanding of Taiwan’s current situation, which is far more interesting than the often sterile debate about the “Taiwan issue.”
Assessing Chen Shui-bian’s First Year
The Domestic and International Agenda

Conference Report

John Donaldson

Despite the dramatic events and changes during Taiwan’s President Chen Shui-bian’s first year in office, in many ways the past year can be characterized as “remarkably unremarkable.” The danger of armed conflict across the Taiwan Straits is real, and, as one expert noted, represents one of the world’s genuine potential flashpoints for superpower conflict. Surprisingly, however, Chen’s main challenge has been to manage not the military, but the economic and political crises on the island. Tension persists as the mainland continues a two-pronged strategy of maintaining military pressure while wooing Taiwan’s business leaders and opposition politicians, while the United States strategy of “strategic competition” with the mainland threatens to trap the island in the crossfire. Meanwhile, solutions to the economic and political crises present themselves as pressing issues for Chen, a shrewd politician but inexperienced president. Still the most interesting incident is the dog that did not bark: cross-strait tensions have been so far addressed short of armed-conflict.

These were among the issues discussed and debated during an international conference, “Assessing Chen Shui-bian’s First Year: the Domestic and International Agenda,” sponsored by the Sigur Center for Asian Studies at The George Washington University in Washington, D.C. on May 31, 2001. Because the seven papers presented at the conference over five sessions are appended to this report, no attempt will be made here to summarize them. Instead, this report highlights the questions, comments and debate among a diverse group of academics and policy makers from Taiwan, mainland China, the United States and elsewhere. These participants grappled with assessing not only the domestic and international impact but also the broader implications of President Chen Shui-bian’s first year in office.

Over the course of this conference, participants discussed a number of issues in four main areas: domestic politics, domestic economics and trade, cross-strait relations and foreign policy.

The Domestic Challenge

In terms of Taiwan’s domestic politics, three main issues were discussed: KMT adaptation to loss of the presidency, gridlock and coalition building, and the primary cleavages of the electorate.

KMT identity and politics

Participants noted that the unprecedented election of a non-Kuomintang (KMT) president presented challenges in two areas: to the parties and to government administration. The KMT, one participant suggested, is challenged by the need to redefine what the party represents. The party appears adrift. Although past accomplishments are valid, if the party hopes to
build up flagging support, hovering around 10 percent, reminding voters of them is insufficient. On the national identity issue, the KMT has veered recently from the “moderate” position represented by former president Lee Teng-hui, to Lien Chan’s more hard-line pro-unification stance, and has apparently shifted from the “Taiwanization” of the party. Justifying that move and clarifying the KMT position will be important to maintaining that party’s relevance.

Moreover, the issue of constructing a nuclear power plant, which the KMT turned into a political, then a constitutional, issue, backfired on the party, which was forced to back down. In addition, the KMT still has to address balancing economic growth, an issue the KMT promotes, with the environment, identified with the Democratic Progressive Party (DPP). Since the latter is popular with voters, this question is vital for the party.

One participant compared the relatively low-key Chen Shui-bian with the more flamboyant Lee Teng-hui. As examples, this participant pointed to the lack of inflammatory statements in Chen’s New York trip, and the lack of quarantine imposed during last year’s trip to Los Angeles. This suggests that U.S. President George W. Bush might be willing to help Taiwan break out of isolation. If these trips become more routine, they could help decrease tension, according to the participant.

Gridlock and coalition building
A number of participants suggested placing Taiwan’s divided government and gridlock in a comparative setting, noting that neither were unique to Taiwan. One participant, while questioning the accuracy of comparisons with France, argued that Scandinavian countries also faced issues in common with Taiwan such as the authority over selecting the premier and issues of legitimacy. Examining these countries could help suggest the future direction of Taiwan. This participant suggested that, while academics examining coalition building in other political entities focused on numbers of seats held by various parties, downplaying ideology, both numbers of parties and ideology will be important for understanding Taiwan’s politics after the December 2001 election for the Legislative Yuan.

Later, one western scholar noted that despite the wide-ranging discussion of gridlock and divided government, there was little discussion at the conference of constitutional reform, which might be necessary if gridlock and divided government continued.

Primary cleavage among voters: national identification
A number of participants questioned the suggestion of a stable voting pattern in legislative elections between “Pan-KMT” and “Pan-DPP” camps (described in John Hsieh’s paper), centering on the issue of national identity. While other issues can be important for choosing between parties within each camp, national identity has been the basis of choosing between the two camps, one participant argued. Some participants were surprised by this argument, which contradicted the idea that politics in Taiwan is strikingly fluid. Others noted that this contrasted with cleavages in other areas based on class or religion.

One participant inquired whether this cleavage held true even based on age and education. In reply, a participant from Taiwan presented data that suggest that other than poorly educated voters (who prefer independence), there is little difference in opinion on national identity based on age or education.

Another participant inquired about the political impact of the KMT’s massive financial resources. A panelist suggested that while resources and organization were important for the KMT, the most important issue was the cleavage based on national identity, and that even ethnicity was not as important an issue as the
difference of opinion on this issue.

Another participant asked about the impact of the military threat from mainland China on public opinion. The panelist noted that, according to polls, while many people reported they would favor independence if China renounced force, a large number also favored unification if the mainland became democratic. Paradoxically, about a quarter of respondents answered “yes” to both questions.

Finally, one participant questioned the impact of public opinion on elections, and whether election strategy was more important than public opinion in deciding elections. To illustrate this, the participant pointed to the fact that candidates can win a seat with only 8-10 percent of the vote. A participant replied that since the island’s electoral system is remarkably proportional, public opinion translates almost directly into electoral results. At the same time, this system encouraged corruption and vote buying since the system encourages members of the same party to compete primarily among themselves for seats in the Legislative Yuan.

**Domestic economics and trade**

A number of economic issues were discussed at the conference, including the effect of gridlock on the economy, Taiwan’s growing dependence on China, the impact of slow growth, Korea as a potential model for Taiwan’s economy, and the KMT’s assets.

**Gridlock and effect of politics on the economy**

One participant asked about the effects of political gridlock on the economy. One panelist responded that gridlock changed the perception of the people, noting that most of the severe drops in economic indicators occurred during the political battle over the building of the nuclear power plant. This panelist blamed in part the DPP for forgetting that “they were the minority party” in the Legislative Yuan. The participant, however, echoed the sentiment of many that Chen Shui-bian did not deserve all of the blame for economic malaise. Because of time lags, many of the economic problems can be traced back to the previous administration, or to a slowdown in the world economy that began before the Chen Shui-bian administration commenced.

One person noted that the lack of a central figure like Alan Greenspan was an important issue. Some of the malaise can be ascribed to the fact that the central bank is currently not an “independent political authority.” One participant suggested that once the party system “settles,” the government could make central bank authority “independent from everyday politics.”

Underscoring the effect of politics on economics, one participant pointed to the decision to dismiss the director of China Steel Corporation, the most profitable steel company in the world. Despite this success, and the former director’s popularity among workers, he was forced out for reasons of “local politics.” The participant pointed to this example to suggest that politics, not improving the economy, has unfortunately been placed as the first priority. The government therefore is “not working in the right direction.”

**Dependence on China**

One participant raised the ambivalent role of China as important to Taiwan’s economy. On the one hand, Taiwan residents’ lack of confidence in the government’s China policy is fueling the increasing capital flight to China, perhaps to an unhealthy degree; simultaneously, China presents hope for development. A panelist responded by comparing Taiwan to Hong Kong. For Hong Kong, manufacturing has received a “second life” by shifting to southern China. The same is true for Taiwan; in spite of a prohibition against large and high-tech enterprises directly investing in China, most big companies have operations there, including, most notably, research and development. If Taiwan is unable
to improve its investment climate and keep parts of these enterprises in Taiwan, then China increasingly will be a factor in Taiwan’s future. However, Hong Kong was successful in 2000, with 10 percent growth despite its manufacturing section having shifted to the mainland. Yet, since Hong Kong is politically a part of China, the result may not be the same for Taiwan.

In a later session on foreign policy, one participant underscored the dependency issue as the main variable in cross-strait relations. Yet another participant asked whether this dependence suggested Taiwan should close its economy to China, or open it further. By opening its economy to China, the participant pointed out Taiwan could create a mutual dependency. Moreover, this participant asked, would the World Trade Organization, which both mainland China and Taiwan hoped to join, constrain Taiwan’s options and compel it to open to the PRC.

**Slow growth and “catch up” economies**

One participant suggested that slowing economic growth of Taiwan could be a natural result of the economy’s “catch-up” and shift to a mature economy. Many participants seemed to reject this suggestion. One panelist responded by rejecting the view that Taiwan is in a middle-position, doing well relative to developing countries but on the lower end of developed countries. Suggesting that it is less misleading to compare Taiwan with other economies in the region, this participant noted that Singapore per capita GNP (US$ 30,000) and rate of growth (7-8 percent) were both greater than Taiwan’s. Another suggested that the slow-growth argument was “retiring,” and asked pointedly how Singapore’s economy could be explained.

Further, some participants highlighted the increased public pressure for Taiwan to develop its welfare state and transit system. For this effort, Taiwan requires a “medium” rate of growth between 5.5 to 6.5 percent. Without such growth, resources for this effort would be insufficient. Still another participant argued that the goal of a “Taiwan double” (doubling GNP per capita to US$ 30,000 within 5-6 years) was turning out to be “Taiwan trouble.” Therefore, these scholars suggest, a slower rate of growth comparable to developed countries would be deleterious to Taiwan’s social agenda.

Some participants linked declining growth to the difficulty of restructuring Taiwan’s industry. One scholar noted that Taiwan’s economy has been driven by small and medium-sized enterprises, which are not well funded and spend relatively little on research and development. In spite of a decade-long goal of modernizing its industrial structure, Taiwanese firms still manufacture components for companies like Compaq. Without rapid growth, making this shift will be difficult.

Another participant found irony in the fact that small- and medium-sized enterprises were once seen as signs of Taiwan’s economic strength, but are now seen as part of the problem. This participant pointedly asked whether the “Green Silicon Island” model suggested by the current government truly reflected a consensus. Moreover, this model presented a number of questions, including whether it is intended to supplement or replace the current system and what role China would take in this model.

Finally, one participant pointed out the link between mercantilism and growth. Since Taiwan is not a member of international institutions such the International Monetary Fund, it cannot rely on outside intervention in a crisis. Therefore, it must hold an inefficiently large of foreign capital reserves. Moreover, the shift to a democracy increases demands on the government for a “piece of the pie.” Given the continuing need to finance development and welfare, lower growth would cause political and social problems.
Korea as a model?

One participant pointed to the common difficulty both Korea and Taiwan have had in making the transition to democracy, with newly popularly elected administrations facing economic difficulties. Another participant suggested that the differences between the economies (Taiwan’s being based on small and medium-sized enterprises, while Korea’s was based on huge state-established Chaebols) signified that Taiwan should not model itself on Korea. The very size of these Chaebols made them “too big to fail,” even as the international community is compelling Korea to reform them. This fact, coupled with the dispersed coalition formation system in Taiwan, and the less access businesses enjoy to the state, suggest the lesson for a reforming Taiwan is to avoid following the Korean model.

KMT, Inc.

In response to Karl Field’s paper on the party-owned assets of the KMT, one participant asked about the distinctions the developmental role between party-owned and state-owned enterprises (SOEs). Fields argued that initially, there was little distinction between KMT, Inc. and SOEs. In contrast with governments in Korea and Japan, the KMT was able to leverage large amounts of capital for development and campaign funds, with little need to go outside the party hierarchy. Initially then, there was little distinction between the assets of the party and state. More recently, however, the KMT has faced intense pressure to separate these assets.

In response to a question, he noted the DPP was not likely to establish corporations of its own, since these corporations are unpopular and the KMT is moving away from them. While material resources clearly give an advantage, they do not guarantee electoral success, and the way they are obtained can be a liability.

Cross-strait relations

Participants debated the policies of mainland China and Taiwan towards cross-strait relations, as well as the relative importance of domestic politics in determining this policy. Many participants pointed to the unexpected stability that has emerged. At the same time, however, both sides in the conflict blame the other sides’ perceived inflexibility as a cause of the continuing stalemate.

A focus on China

Participants contrasted the common post-election expectation of a serious cross-strait confrontation with the surprisingly peaceful aftermath of Chen’s inauguration. One participant recounted a trip to mainland China, one week after Chen Shui-bian’s election. During this trip, a senior research fellow at China’s Center for Development and Peace warned the participant that as a result of the election of Chen Shui-bian, Taiwan would be attacked. Due in part to Chen’s May 20 speech, however, the status quo has been maintained and no conflict has occurred as yet. The speaker argued that China could “only wait and see,” and maintain the status quo.

A participant suggested that, compared to the Lee Teng-hui era, Beijing saw “things going its way.” Through its “two pronged” strategy, China has forged economic relationships and invited KMT officials to Beijing, while maintaining pressure on Taiwan. Moreover, Chen Shui-bian is not as provocative as Lee Teng-hui is, and that has enhanced stability. The participant argued that Chen would likely remain internally focused, moderate and vulnerable, all to Beijing’s liking. The PRC is therefore likely to continue reaching out. However, the speaker cautioned that the present situation, though stable, was delicate and tense, that both sides are hemmed in due to internal politics, and that military modernization would increase the tension. The overall situation, therefore, has not changed dramatically. In fact, another western participant objected to the term “stable,” and suggested the less optimistic term, “calm for the moment,” would be more appropriate.
Another participant argued that (what he called) China’s three-pronged foreign policy (united front, encouraging Taiwan’s economic dependence, and military deterrence) has been successful. First, he suggested China’s “united front” policy toward Taiwan was so far successful, and compared it to West Germany's Ostpolitik policy toward East Germany. Second, he described economic integration as a “key variable,” underscoring the impact Taiwan’s dependency on mainland China. Third, he focused on the remilitarization of the issue on both sides, and the qualitative and quantitative improvements the PRC has made relative to Taiwan.

This participant also highlighted two trends. First, the balance of power is not sustainable, the speaker argued, and that by 2010, the mainland will improve enough to be a significant threat to Taiwan. Second, Taiwan faces increasing pressure caused by the united front policy and increased economic dependence. To assess the future, this participant pointed to five variables: the success of the united front, the possible return of the KMT to power, domestic developments in the PRC (e.g., the upcoming 16th Party Congress of the Chinese Communist Party), ongoing tensions between the US and China over Taiwan, and the improvement of China’s military situation. He cautioned that the PLA, in modernizing their forces was not becoming a “military monster,” but rather would be a concern for Taiwan in the coming years, for instance, because it could enforce a quarantine. This buildup would drive American response, which would be exacerbated if U.S. concern continues to shift from Europe to Asia.

One participant from Taiwan argued that although Jiang Zemin’s hands were tied to some extent, “wait and see” was actually a proactive tactic. The participant questioned the coherence of China’s two-pronged strategy of maintaining military pressure while simultaneously reaching out to business leaders and KMT politicians. The military threat, this participant believed, could lead to a dangerous cycle if peace was not maintained. However, the status quo, though amorphous or vague, was good for all, in part because there were no better ideas for any of the three sides (the PRC, ROC and US), and that encouraged a realistic view for all sides.

**Taiwan election’s impact on cross-strait**
Participants debated the significance of the upcoming election for members of the Legislative Yuan. One participant argued that if the DPP does well, then the present stability might break down, and Beijing might perceive Chen as powerful and lose its present optimism. (As one participant stressed, although Chen and his advisors are looking for a positive response to the present situation, they could not accept the one-China principle, as it implies one nation. Another added that acceptance of the principle would preclude foreign participation in negotiation.) At the same time, this participant thought a DPP victory was unlikely, due in part to the poor state of the economy. This view contrasted somewhat to the argument, discussed above, that the main cleavage in Taiwan politics is based on national identity. If the DPP did poorly, this participant suggested Chen would remain weak and the status quo could continue relatively unchanged.

One participant wondered whether, now that China has made Chen Shui-bian “dance to Beijing’s music,” the Taiwan people might conclude that having the DPP in power is bad for Taiwan. One participant from Taiwan, however, argued that the policy differences between the KMT and DPP on the national question would continue to be minimal as long as there was a chance for Taiwan to remain independent. No party, he asserted, would advance surrendering sovereignty, because it was a “fundamental consensus.”

A participant, pointing to the previous speaker’s zero-sum terms, such as “maintaining
sovereignty” and “surrendering,” asked if there were possibilities for a non-zero sum stance. The other replied that there were such possibilities, but suggested Beijing’s inflexibility in negotiating alternative arrangements, such as confederacy or commonwealth, was responsible for lack of progress.

One participant stressed the inflexibility of Taiwan’s position. Although Chen Shui-bian himself is a flexible politician, his own inter-factional struggles reduced his freedom to establish his own policy. This is in contrast to former President Lee Teng-hui, who, one participant argued, was relatively autonomous and above institutions and even public opinion. The ambiguity of Chen Shui-bian’s policy is reflected in his contradictory view of the role of the reunification commission, as well as his view on the so-called “1992 Consensus.” The same participant noted that despite being hamstrung by factional politics, the party itself has changed a great deal (although not enough for the PRC’s taste), implying a degree of flexibility in the party’s direction. Others argued that Chen’s policy positions had less to do with factional political than they did with his sense of responsibility as the president to protect Taiwan’s security and independence.

The importance of domestic politics
One participant, responding to a question about the significance of the 16th Party Congress of the Chinese Communist Party, outlined two scenarios about its effect on cross-strait relations. If, as rumored, all top leaders retire and are replaced by the next generation of leaders, the speaker thought that they would leave the issue for successors to deal with, and that the current “wait and see” policy would continue. If on the other hand, President Jiang Zemin, Li Peng, and Li Lanqing maintain a position (as is also rumored), they might take a longer-term view, and might opt to change present policy. The participant underscored the use of national sentiment as a source of power by the leaders, which he thought might render “wait and see” less certain and stable.

One participant, responding to a presenter’s suggestion that the PRC perceived Chen’s words (for instance, his series of “No’s”) as being insubstantial and “mere words,” noted that mainland leaders might be changing the goal posts. During the campaign, the PRC’s leaders were directly threatening but now that President Chen backed off from independence, Beijing has increased its expectations from merely not declaring independence to proactively doing what they desired.

In response, another participant argued that Beijing’s pre-election concern about Chen’s provoking a war has changed to post-election relief. Although there are differing levels of expectations, the worst-case scenario from China’s perspective has not occurred. The speaker reaffirmed his belief that China perceived that President Chen’s “Five No’s” resulted not from his own convictions but from a combination of PRC military pressure and Taiwan’s domestic problems. As a sign of Chen’s insincerity, the speaker pointed to the contents of textbooks, Chen’s assertion that he was ethnically Chinese (i.e., not “Chinese”), Taiwan’s passport and currency which does not include “China,” and other signals. This speaker argued that China hoped Taiwan would re-adopt the one-China principle that was the policy of 1992, which did not include the 1999 demand that Taiwan and mainland China negotiate on a state-to-state basis.

Who’s responsible for this mess?
Participants were divided on which side, Taiwan or mainland China, was most important for directing the future direction of cross-strait relations. One participant argued that Taiwan was the driving force. Though all sides have a role to play, Taiwan has driven all changes in the situation. He underscored his point by quoting a
Chinese saying: “Fight or not fight: look to Taiwan. Real fight or fake fight: look to the PRC. Big fight or small fight: look to the United States.”

One participant argued that Beijing’s definition of independence was too broad, contending that Chen’s transit stop in New York City, like Lee Deng-hui’s alumni trip to Cornell University, did not have anything to do with the national question. The participant concluded that there was no way to satisfy Beijing. Therefore, though both sides must make an adjustment, neither side is willing to do so. Moreover, both the PRC and Taiwan are signaling their good will to the United States, and not to each other. This reinforced another participant’s view that both sides’ perception of each other’s insincerity is correct.

Subject to fate?
One participant expressed concern that since both sides are not flexible, neither side seems proactive. As a result, the situation seems uncomfortably “subject to fate” (accidents, for instance) because either side did not direct it.

Foreign Policy
Moving away from the issue of cross-strait relations to a broader focus on the foreign policies of Taiwan, the PRC and the United States, as they relate to politics on Taiwan, participants focused on a number of important issues. Because the panelists did not prepare written papers, a brief summary of their remarks are also included in this report.

Chinese foreign policy
One participant noted that Beijing has made foreign policy adjustments, but that these adjustments predated Chen Shui-bian’s era and were a reaction to Lee Teng-hui’s policy. The participant outlined three elements, described as a “holding action” based on low expectations of the United States playing a positive role from a PRC perspective. First, a gradual de-emphasis of the United States’ role in the Chinese-Taiwan “stalemate.” The U.S. did play a positive role, from the PRC’s perspective, culminating in September 1998 with President Clinton’s three “No’s.” This strategy, unsustainable due to lack of domestic support in the U.S., fell away due to U.S.-Chinese relations’ deteriorating for issues unrelated to Taiwan. The PRC previously hoped the US would play a role in bringing Taiwan back to the bargaining table, and preventing then-President Lee Teng-hui from moving further from the status quo. Neither was successful. For instance, Lee ignored the U.S. and almost produced a crisis in mid-1999.

Second, China has refocused on rebuilding bilateral ties with Asian countries, especially Japan (e.g., Premier Zhu Rongji’s 2000 visit), Korea (e.g., encouraging a rapprochement on the peninsula), and Southeast Asia. Third, China engages in “framework building,” for instance the “ASEAN Plus Two” framework, the idea of establishing a prototype Asian economic union, which notably excludes the United States and Taiwan.

This participant concluded this strategy has had mixed success, pointing to limited success in South Korea and Southeast Asia, as well as “bad luck” in Japan. Despite initial progress, the newly constituted nationalistic government suggested a decreased likelihood for improvement of ties between the two countries.

Taiwan’s foreign policy
A participant argued that while Taiwan’s domestic politics could be seen as a failure, its foreign policy has been “not bad,” and better than Lee Teng-hui’s because Taiwan is now viewed as a contributor to regional stability, not a troublemaker. The speaker suggested Chen will continue to improve in four areas. First, in the economic arena, which the speaker believed is “in trouble” but “fundamentally sound,” Chen is attempting to augment Taiwan’s role in contributing to the economies of China and Southeast Asia. Although other speakers emphasized Taiwan’s
contribution to China could be a two-edge sword, the speaker argued that this was a worthwhile risk. Part of this strategy includes the “three mini-links” policy, which the speaker noted was basically complete, with the exception of unresolved security issues. As a result, the speaker argued that the three mini-links should be a part of a larger package deal designed to build confidence and security assurance. Second, Chen is enhancing Taiwan’s image as an emerging democracy, including spearheading an NGO movement to tell the world about this. Third, Chen is continuing Taiwan’s role in ensuring the stability of Asia. Fourth, in terms of sovereignty, Chen has dropped the effort to secure recognition from small countries, and is shifting policy to improving substantial relations, while not provoking China.

One participant asked about Chen Shui-bian’s statement that Taiwan will not be a “pawn” to any great power. A participant suggested that these words might not have been well thought through, noting that Taiwanese democracy has increased the chances of such half-baked ideas being expressed. Another participant took issue with this, noting that Chen Shui-bian had many advisors, and, unlike former president Lee Teng-hui, he listens to them. He added that, unlike Lee Teng-hui, Chen Shui-bian surprises not by being provocative, but by being conciliatory. This participant suggested that the pawn “No” might be a conciliatory move to mainland China. Others believed the statement, made in Latin American soon after leaving New York City, reflected his desire to not let Taiwan be a victim of American political debates.

U.S. perspective

While cautioning that the lack of official statements concerning an Asian policy for the U.S. made conclusions difficult to draw, one participant focused on the change in tone and substance. In terms of tone, this participant focused on the U.S.’s shift to viewing China as a “strategic competitor,” and noted this was “more than just rhetoric.” In addition, he noted the absence of reaffirming the “Three No’s” policy.

Substantially, the participant argued the U.S. “Asia strategy” (as opposed to a “China strategy”) paralleled that of former president Ronald Reagan’s second term under then-Secretary of State George Shultz. This policy includes downgrading China, while building up relations, including security alliances, around China’s rim. He argued that the emphasis on refurbishing old alliances is disingenuous. The participant listed a number of changes in U.S. Taiwan policy, including granting visas to Lee Teng-hui and Chen Shui-bian, statements (slips of the tongue?) on “Good Morning America,” and an arms sales package. These would increase tension in the U.S.-China bilateral relationship. However, the speaker suggested that tension between the U.S. and China might ease after the APEC summit and Bush’s subsequent trip to the PRC.

One participant argued that conservative interest groups in the United States perceived China as “the real target,” and were using Taiwan as a “side-show” in this effort. Another participant from the west concurred, noting that Taiwan is seen as a tool for getting at China, due to concerns about deterring use of force in its “sphere of influence.” This participant suggested that leadership was needed to help the American public understand what is at stake, so that Taiwan would not be used as a way of “poking our fingers in Beijing’s eyes.”

A third participant later reinforced this sentiment, arguing that if Chen Shui-bian did not want Taiwan being used as a pawn, he should make it clear to the United States that, just as Taiwan doesn’t want too “cozy” a relationship between U.S. and China, the U.S. should also not go too far. This speaker noted that ‘Taiwan’s representative to the U.S., in his address to the conference, was forthright in his call for U.S. granting China PNTR. This needs to be said straight out as a part of the education of the
United States, needed because of a common perception that confrontation of China was good for Taiwan. However, a number of participants, while agreeing that a cooperative working relationship between the U.S. and mainland China was in Taiwan's interests, believed that this has been said clearly by the Taiwan side.

*Overdoing attention to detail?*

One speaker tried to add perspective to the proceedings by suggesting that focusing too frequently on "how we're doing" might focus analysis on minor changes in tone and distracting us from broader and more important issues. He pointed specifically to the fact that, while it appears that the U.S. is currently tilting "slightly" towards Taiwan, Bush fears moving too far from the middle of the road and the fundamental relationship has not changed fundamentally, a point that might be missed by too narrow a focus. Second, the speaker pointed to the PRC's use of domestic politics to make "excuses" for its behavior, which he suggested might be the start of a trend of a "good cop" (China's government) using a "bad cop" (domestic public opinion) in order to influence the foreign policy of others. The speaker concluded that the U.S. is still important to the relationship, and that Taiwan might do better to ask not what the U.S. can do, but suggest what the U.S. should not do. Another speaker stressed this point, arguing that Taiwan should think very carefully about whether it benefits from a poor U.S.- China relationship, or whether they would prefer the relationship to be "like Goldilock's porridge," not too hot and not too cold.

*Interim Agreements*

Harry Harding, in his speech (included in this set of papers), outlined a proposal for an interim agreement designed to increase regional stability. Many found the proposal provocative and made a number of comments. For instance, one participant asked if it was realistic to expect China to renounce force. Harding emphasized that his proposal needed to be taken as a package. In order for it to work, Taiwan, for instance, would have to keep some form of positive reassurance, such as political integration, on the table.

One participant, noting that both sides were very close, asked if direct negotiations were necessary in order to reach such an agreement. Harding suggested that, while not wanting to get too detailed without having direct involvement, the agreement did not need to be formal, but could be "informal" arrangements such as parallel statements.

Another participant suggested that Beijing would prefer institutionalizing the status quo. Harding replied that Beijing has not so much "accepted" the status quo as "tolerated" it. Mainland China is still dissatisfied with it because of the lack of dialogue, the constraint on ties and the military build-up. Moreover, the risk of accidents made the status quo undesirable. Harding suggested that the proposal discussed would create a "preferable status quo" with lower costs and risks. Further, this proposal would be preferable because the term "political integration" was vague about how far the process could go.

One participant mentioned a possible referendum on the island's status. However, Harding pointed to the complexity of such a referendum, suggesting that there would be political conflicts over both the wording and interpretation of the referendum.

*Parallels with the EU?*

Chen's invoking of the EU when discussing political integration troubled some participants because it implied a higher level of integration than Taiwan might be willing to go. Europe is centralized to a greater degree, for instance, than "one China, two systems" could possibly be. Another issue raised in terms of the EU was Taiwan's fear of being marginalized in the process, like Britain felt in its relationship with
the EU. This parallel evoked another alternative that was raised: a more symbolic "British Commonwealth" arrangement. One speaker suggested that a step-by-step process is therefore needed wherein no side would be expected or required to go further than they were willing to go.
Constitutional Arrangement and the Formation of Government

John Fuh-sheng Hsieh

The most conspicuous scene of Taiwan's domestic politics in the past year or so is the gridlock between the executive and legislative branches of government at the national level. As a result, not much has been accomplished, and the prospect for immediate resolution is at best cautiously optimistic. All these are, of course, closely tied to the constitutional arrangement. And I will first take a closer look at Taiwan’s constitutional arrangement, and then, on the basis of this, talk about the gridlock that has troubled this new democracy since the end of the presidential election last year.

The Constitutional Arrangement

According to the original formulation of the Constitution of the Republic of China (ROC), the constitutional form of government is essentially parliamentary. In accordance with the original Constitution adopted in 1946, the highest administrative organ in the country is the Executive Yuan (cabinet), not the presidency; although the premier, the head of the Executive Yuan, is nominated by the president, he or she has to be approved by the Legislative Yuan (parliament); the Executive Yuan is responsible to the Legislative Yuan, not to the president; and as promulgating laws and issuing mandates, the president has to get the countersignature of the premier or the countersignatures of the premier and the ministers concerned. All these stipulations indicate that the governing power resides in the hands of the Executive Yuan and the Legislative Yuan, not the president.

However, certain stipulations in the ROC Constitution deviate from the typical practices of parliamentary systems. For instance, members of the Legislative Yuan cannot serve simultaneously as government officials; the Executive Yuan cannot dissolve the Legislative Yuan; and the Legislative Yuan, only through the overriding of an executive veto, may force the premier to resign, but the premier may opt to accept the resolution of the Legislative Yuan. I have called such an arrangement “parliamentary system with a dose of separation of powers,” to distinguish it from the fusion-of-power system normally found in parliamentary democracies. The idea behind such a constitutional arrangement is to maintain a distinction between politics and administration, and to stabilize the executive branch.

However, for half a century up to the 2000 presidential election, ROC presidents, with the exception of Yen Chia-kan, had almost always enjoyed a great deal of power. This is, to a large extent, due to their position as the president or chairman of the ruling Kuomintang (Nationalist Party, KMT), the majority party in parliament. Given the highly centralized structure of the party, the president could, through party mechanism, easily intervene in the functioning of the government.
The recent constitutional reforms do not change much with regard to presidential power. It is true that the president is now popularly elected, rendering him more legitimacy in dealing with other branches of the government. But it does not necessarily mean that he or she gains more governing power. Indeed, in such parliamentary democracies as Austria, Iceland, Ireland, and Portugal, the president is also directly popularly elected, but cannot intervene in the policy-making process at will.

Also, a lot of people argue that, following the recent amendments, the president can appoint the premier without the need to secure the approval of the Legislative Yuan, so he or she becomes all-powerful. But this, again, is not quite right. In fact, in quite a few parliamentary democracies, no investiture vote is required. In the United Kingdom, for example, the monarch can, in theory, appoint anyone to the prime ministership. But he or she, under normal circumstances, will respect the will of parliament. Even if, occasionally, the monarch exercises his or her discretion, it does not mean that he or she will dictate policy matters as a result of it. In 1940, the king designated Winston Churchill, who was not yet the party leader at the time, to be prime minister. In 1957 and 1963, the queen twice bypassed the party leaders in the House of Commons by appointing Harold Macmillan and Lord Home, respectively, to be prime minister. However, the king or queen did not try to intervene in policy matters later on in these instances.

In fact, since the amendments now provide the Legislative Yuan with an explicit vote of no confidence directed at the premier, thus strengthening the latter’s accountability to the former, the president, under normal circumstances, may still have to appoint someone to be premier, who can be accepted by the majority party or the majority coalition of parties in the Legislative Yuan. Although, according to the amendments, the president may dissolve the Legislative Yuan after it passes a vote of no confidence—the premier may as well initiate the dissolution under similar circumstances—thus, to some extent, deterring the Legislative Yuan from engaging in rebellious acts. But this does not diminish the provision that the cabinet should be responsible to the parliament.

So even if we take into account the recent constitutional reforms, Taiwan’s constitutional form of government has not, theoretically, been changed too much—in fact, it may be argued that it moves even closer to the typical parliamentarism in the sense that, given the explicit vote of no confidence now possessed by the Legislative Yuan and the power to dissolve it by the executive branch, the executive and legislative powers are indeed more fused than ever before.

Many people argue that the current Taiwanese system resembles that of the French Fifth Republic. Yet, if we compare the two cases carefully, the formal powers of the ROC president remain limited as compared to those of his or her counterpart in France. For instance, the French president can preside over the Council of Ministers; can ask the parliament to reconsider a law; can bypass the National Assembly to submit a bill directly to the people in a referendum; can dissolve the National Assembly at any time except within a year following an election or during the exercise of emergency powers; and so forth. None of these is available to the ROC president. Therefore, the ROC president, even after recent constitutional reforms, still does not have comparable powers as enjoyed by the French president. To characterize the Taiwanese system as something similar to the French system is apparently an exaggeration.

Nonetheless, politicians may interpret the Constitution quite differently. For example, the president may ignore the majority party in the Legislative Yuan by appointing a premier he or she likes, and try to intervene in policy matters
later on. An instance such as this will certainly lead to confusion, or even confrontation with the Legislative Yuan. It is unfortunate if it happens. Nonetheless, it can be expected that, in the long run, the constitutional form of government in Taiwan will move toward some kind of parliamentarism if the current arrangement remains intact.

The Aftermath of the 2000 Presidential Election

Given the above interpretation, the presidential election, under normal circumstances, does not matter much. Hence, regardless of whether the Democratic Progressive Party’s (DPP's) Chen Shui-bian or KMT-turned-independent James Soong won the election of March 2000, no true turnover of power would ensue as long as the KMT maintained its majority status in the Legislative Yuan. However, as it turns out, the situation has been quite different.

Right after the election in which its candidate Lien Chan not only lost to Chen, but lagged far behind Soong, the KMT was in total disarray. President Lee Teng-hui was forced to step down from the chairmanship of the party amid protests asking him to be responsible for the loss of the election. Lien, the acting chairman and later the chairman of the party, was weak, and was unable to pump up the morale within the party. Also, the KMT was depicted as the representative of “black and gold politics” (namely, the involvement of organized crimes and big businesses in politics); thus, any thought to welcome the KMT back in government seemed morally unsound and politically incorrect.

For the KMT, sensing that a new parliamentary election would deprive it of the majority status in the Legislative Yuan, it was reluctant to use a vote of no confidence against the government that it disapproved of. At the time, the KMT faced not only competition from the DPP but also the newly-formed People First Party (PFP) led by Soong, which attracted a lot of people from the KMT and the New Party (NP). A new election might seriously reduce the KMT seats in the Legislative Yuan. Moreover, the fact that previous presidents had enjoyed a great deal of power, and the KMT had tried to justify such practices, also put the KMT in an awkward position vis-à-vis the new president and his party.

So, after the election, as the KMT hinted that, according to the logic of the French system, when the presidency and parliament were controlled by different political forces, the system should become parliamentary, the new president unequivocally rejected the idea, and the KMT retreated. In fact, Chen refused to talk to the KMT about the possibility of forming a coalition government, not to mention a majority government involving only the KMT.

A DPP government looked infeasible as well. With only about one-third of the seats in the Legislative Yuan, a DPP government would inevitably face strong challenges from the KMT and other political parties, and would be unable to accomplish almost anything.

As Chen was about to assume office, there was another important consideration, namely, the attitude of the military. Most of the military commanders are mainlanders and KMT supporters, and are fearful of the DPP’s position on the national identity issue. If Chen moved hastily toward Taiwan independence, it would certainly irritate these military men. Of course, such a move would also antagonize the People’s Republic of China (PRC), and possibly bring about military confrontations between Taiwan and China, a scenario that the United States would, from the very beginning, try to prevent from taking place.

As a result, the new president, in a carefully calculated move, picked up Tang Fei, a mainlander general, and a KMT member, to be premier responsible for forming a nonpartisan, “all-people” government. The appointment of
Tang was evidently aimed at pacifying “all the people,” including not only the KMT, but also the DPP, the military, the PRC and the U.S.

However, such a scheme soon proved to be unworkable. On the one hand, since the KMT as a party was excluded from the process of forming the government, it, as can be expected, had no intention of cooperating with the new government. On the other hand, even the DPP did not support it whole-heartedly because the party was not really consulted, and many people in the new cabinet remained from the old KMT government. Thus, the “all-people” government became truly nonpartisan, viz., supported by no party.

In early October, Tang resigned apparently because his ideas of governing were different from those possessed by President Chen and the DPP. Vice-Premier Chang Chun-hsiung, a former DPP legislator, replaced him. Consequently, a DPP cabinet was formed. However, since the DPP controlled only about one-third of the parliamentary seats, the government still would encounter a great deal of difficulties in the Legislative Yuan where the KMT still commanded a majority of seats (albeit a shaky majority). Even though the KMT might not opt for a no-confidence vote to topple the government, it could utilize a lot of other means to boycott it.

One instance suffices to make the point. In late October, the DPP government announced that it would, as long advocated by the party, halt the building of the fourth nuclear power plant. The announcement came right after President Chen Shui-bian's meeting with KMT Chairman Lien Chan, the first official meeting between the two after the election. The announcement was seen as purposefully humiliating to Lien. This irritated the KMT, the PFP, and the NP so much that the three parties were determined to work together to counteract the DPP government. They even called for recalling the president and the vice-president, and at one point, they came close to mustering the support of two-thirds of the Legislative Yuan members to pass it. Although the recall died down later, the conflicts between the executive and legislative branches went on. Given that the DPP control only one-third of the seats, the Executive Yuan was forced to retreat on almost all fronts.

As noted above, such conflicts are inevitable given Taiwan’s constitutional arrangement. On the one hand, President Chen attempts to run the government like a president under the presidential form of government while, in fact, the system is essentially parliamentary. On the other hand, the KMT is also to blame since it has been unwilling to use the vote of no confidence to change the course of the government, thus lengthening the stalemate existing between the two branches of government. Such a scenario may be changed only after the next parliamentary election scheduled for December 2001, barring an early dissolution. However, even with the new election, there is no guarantee that things will move in the “right” direction.

The Prospect
Since the late 1980s, the relative political fortunes between the pan-KMT camp, including the KMT, the PFP, the New Party, and the Democratic Alliance (DA), on the one hand, and the pan-DPP camp, including the DPP, the Taiwan Independence Party (TAIP), and the New Nation Association (NNA), on the other, have been very stabilize. In the Legislative Yuan elections, for instance, the KMT won 60.22% of the vote in 1989. Three years later, they received 60.5%, almost the same as they did earlier. In 1995, the NP entered the race. By adding the NP vote, the pan-KMT camp again obtained a similar amount of popular support (59.01%). In the 1998 election, the pan-KMT camp, including KMT, NP, and DA, received 57.23%, a bit less than
but not too much different from previously. For the DPP, it received 28.26%, 31.03%, 33.17%, and 29.56% of the vote in 1989, 1992, 1995, and 1998, respectively. Although its vote share fell in 1998, by adding the votes for TAIP and NNA, the pan-DPP camp still managed to get 32.58%, not dissimilar to the DPP vote three years earlier. A similar pattern may be found in the executive elections as well.

The stabilization of the political fortunes between the two major camps results mainly from the relative stability of the distribution of voters on the national identity issue, the major cleavage in the society underpinning the party configuration in Taiwan. It is unlikely that these will change drastically in the foreseeable future. Thus, under the circumstances, it will be very difficult for the DPP or the pan-DPP camp to win a majority of seats in the Legislative Yuan. Thus, after the new parliamentary election to be held later in 2001, President Chen can no longer keep a DPP government by claiming, as in the past, that the Legislative Yuan represents the "old mandate." Then, if no party is able to control a majority of parliamentary seats—a likely scenario—a coalition government has to be formed. (Of course, if no two or all of the three major parties will come together to form a majority coalition, a minority government as seen in many Nordic countries is still likely.)

The interesting question, then, is: who is going to coalesce with whom? There have been talks lately about a majority coalition consisting of the DPP, Lee Teng-hui's followers in the KMT, and the independents. If this comes true, the gridlock may be alleviated somewhat. But given the shakiness of such a coalition, the government may be held hostage by specific interests. Besides, such a coalition is not that feasible. For one thing, it is hard to imagine that a large number of KMT legislators may choose to defect. It is true that the KMT remains the richest party in the world, but more importantly, there are clear differences between the KMT and the DPP on many issues, particularly the one related to national identity. As mentioned above, the national identity issue is the major cleavage in society underpinning the party structure in Taiwan, and has been relatively stable over the years, resulting in the stabilization of political fortunes between the pan-KMT and pan-DPP camps. Thus, any KMT legislators who decide to leave the KMT to join the DPP-led coalition may risk alienating their original supporters while being unable to gain new votes from the traditional DPP support base.

If such a coalition is not feasible, the DPP may turn to the KMT or the PFP for help. Given the greater difference between the DPP and the PFP on issues such as national identity, it is more likely that the DPP will seek the cooperation of the KMT rather than the PFP. But from the KMT's perspective, the DPP is on the other side of the aisle, and the policy differences between the KMT and other parties in the pan-KMT camp are much smaller. Thus, the KMT may prefer a pan-KMT coalition to a KMT-DPP one. Then, if the pan-KMT camp insists on forming a pan-KMT coalition by excluding the DPP, President Chen may have no choice but to designate a pan-KMT cabinet. Otherwise, fierce confrontation between the President and the Legislative Yuan can be expected. The majority coalition, under the new circumstances, may not hesitate to use a no-confidence vote to counteract the President's moves.

Nonetheless, if Lee Teng-hui's followers, after the new parliamentary election, are able to maintain a sizeable presence within the KMT, and are thus able to force the KMT leadership to negotiate with the DPP in the name of, say, national salvation, a grand coalition government comprised of all major parties is also possible. For the pan-KMT leadership, a grand coalition may serve as a transitional phase toward the "true" majority rule, a minimum winning coalition of some sort. Ironically, if it ever comes to the point for the formation of a grand
coalition, it will be the PFP’s turn to consider whether to be in such a coalition or not. By staying outside the government, it may claim to be the only major opposition party in the game, hoping to reap any harvest from the government’s blunders.

Conclusion

The situation in Taiwan remains volatile. The kind of gridlock we have witnessed in the past year or so may not be easily resolved. Much, of course, depends upon how the political leaders interpret and are willing to abide by the Constitution. However, as long as the Constitution remains intact, the political leaders must eventually return to the spirit of the Constitution, so to speak. This is the remedy for the gridlock.

Notes

1 Some of these features in the ROC Constitution are not unique among parliamentary democracies. For example, parliamentarians are barred from serving in the government as well in the Netherlands, Norway, and Luxemburg. And in Norway, the cabinet cannot dissolve the parliament.


3 The latter point was stressed by Chang Chun-mai, the drafter of the ROC Constitution. See his Ten Lectures on the Democratic Constitution of the Republic of China (No publisher’s name, 1997). (These lectures were given in 1946.) Interestingly, he called the ROC government “modified parliamentary system.”

4 Of course, during much of this period, it was the authoritarian rule, so the president was able to control the situation by a variety of nonconstitutional means.


6 Right after the election, the KMT controlled 116 out of 224 seats in the Legislative Yuan.

7 According to the ROC Constitution, the recall of the president or the vice-president should be passed by two-thirds of all Legislative Yuan members and one-half of the valid ballots in a nationwide vote.

8 It should be noted here that, according to the official figure, the KMT got 53.02% of the vote in 1992.

However, this was not comparable to the 1989 figure because the ROC Central Election Commission (CEC) changed the rule of designating a candidate’s party affiliation due to the introduction of proportional representation to the election. Previously, any candidate who claimed to be, say, a KMT member would be regarded as such, but, now, only those who were officially nominated by the party would be able to be recorded as its candidates. In 1992, quite a few KMT heavyweights entered the race without nomination. Many of them later won the election, and rejoined the party fraction in the Legislative Yuan. So if we include them in the KMT figure, the party actually received 60.5% of the vote.

9 The difference between executive and legislative elections is that since the elections for executive offices are conducted under single-member district plurality system, the vote may converge to two major parties. As a consequence, the DPP has often been able to capture about 40% of the vote in such elections.


11 In executive election where single-member district plurality system is the rule, not very many offices are available, and short-term factors such as the candidates’ personal characteristics may loom large, the DPP may do very well, particularly when the pan-KMT camp is divided. But in the legislative election where the electoral system is more proportional, and given the large number of seats at stake nationwide, short-term factors may, as seen nationally, may cancel out. The distribution of parliamentary seats may better reflect the long-term fortunes of the various political forces.

12 In a zero-sum game, a coalition which is large enough to win but not too large is the obvious result. See William H. Riker, The Theory of Political Coalitions (New Haven, Conn.: Yale University Press, 1962). It is only under very unusual circumstances that a grand coalition may be formed.
Taiwan’s President Chen Shui-bian after One Year in Office

Shelley Rigger

In an interview with USA Today.com posted on May 2, Taiwan President Chen Shui-bian offered a modest defense of his first year in office. In winning the presidency a year ago, Chen, who represents the Democratic Progressive Party (DPP), was the first opposition politician to capture a branch of the national government from Taiwan’s long-time ruling party, the Kuomintang (KMT).

In defending his record over the past 11 months, Chen remarked, “We have successfully completed our very first and very peaceful transfer of power, and we are very pleased by this accomplishment despite chaos in our legislature and in our media ... Before the election, cross-Strait relations were considered the DPP’s and my personal weakness by the general public ... By now, even though we haven’t achieved any breakthroughs, relations have not worsened.”

It seems little enough to boast of—a transfer of power that was chaotic, although not violent; a relationship with China that has seen neither progress nor regress. The limited nature of Chen’s achievements underscores the difficulty of his first year in office, but also serves as a reminder of something we ought to know by now: transitions from authoritarianism to democracy are often protracted, and are nearly always fraught with uncertainty and peril.

Chen Shui-bian’s Annus Horribilus

There is no shortage of evidence that Chen Shui-bian’s first year in office was filled with hardship. On the economic front, Taiwan suffered a significant rise in unemployment (rising from a high of 2.9 percent in 1999 to nearly 4 percent in April 2001), while the Taiwan Stock Exchange has fallen from 8,600 to about 5,000 in the past 12 months. Politically, Chen has seen numerous challenges to his authority, including a recall effort in October and November in which members of the KMT and its successor parties, James Soong’s People First Party (PFP) and the New Party, attempted to remove the president from office. Most recently, law-makers from those parties—who hold almost two-thirds of the seats in Taiwan’s legislature—have called for the resignation of Premier Chang Chun-hsiung. Nor has Taiwan made the progress Chen had hoped for in its external relations. Although Beijing has toned down the angry rhetoric of a year ago, there is little sign that dialogue between Mainland and Taiwan authorities will resume soon.

Coverage of Chen’s first year in office by Taiwan’s domestic media and the international press, has focused on these negative developments. However, it is possible to discern a number of more positive trends and developments. To begin with, it is deceptive to blame political changes on Taiwan for the
Assessing Chen Shui-bian’s First Year

island’s economic woes; in fact, its economic troubles are shared by economies around the region, and the world. The declines in its stock market are matched or exceeded by other East Asian bourses, not to mention the NASDAQ. Given Taiwan’s tech-heavy market, it was inevitable that a weakening world market for technology shares and products would have a strong impact on Taiwan’s financial world.

At the same time, cross-strait relations—while experiencing little or no progress in the past year—have stabilized, following years of deterioration. Beijing has put aside the angry language that characterized Chinese leaders’ rhetoric toward President Lee Teng-hui and candidate Chen Shui-bian. Beijing is targeting its rage on specific (relatively marginal) figures such as Vice President Annette Lu, while deploying a united front strategy aimed at wooing Chen’s political adversaries. Meanwhile, scores of Taiwanese business leaders and politicians have visited the mainland since Chen’s inauguration, where they have been received a friendly reception. Many of these visitors have returned to Taiwan to urge Chen to expand trade and investment across the Strait. Some have also spoken favorably of Beijing’s proposals for political talks leading to unification. This honey-instead-of-vinegar approach has contributed to a softening of attitudes toward the mainland among the Taiwanese people. Still, there is an important exception to this trend. Mainland leaders have pointedly excluded Chen Shui-bian and his party from their charm offensive, preferring to concentrate their energies on his political opponents.

Political scientists have long identified the first turn-over of power from an authoritarian ruling party to the opposition as a key moment in the democratization process. Making that transition smoothly is always difficult, and since the KMT enjoys electoral legitimacy in the legislature, it saw little reason to yield power to its long-time opposition when the DPP captured the presidency. To make matters worse, the institution of the presidency established by the ROC constitution is a relatively weak office. As a result, Taipei is now the site of a protracted struggle between the executive and legislative branches over how authority is to be distributed under divided government.

The chaos and conflict that marked Chen’s first year in office partially masked an important feature of Taiwan’s transition to a DPP presidency. This transfer of power, however contested, almost certainly permanently altered the nature of politics in Taiwan. The return of non-democratic, single-party rule is highly unlikely. One possible outcome is realignment and restructuring in the party system; the KMT, which already has fissioned off two new parties, the New Party and the People First Party, may well split again, or lose members to a DPP-led coalition. And even if the KMT holds together and regains control of the executive branch while maintaining its edge in the legislature, the DPP is now an established player in national politics. Multi-party competition is institutionalized; dominant-party politics is unlikely to revive.

Chen Shui-bian’s life has been marked by extremes of fortune, but perhaps his most astounding stroke of luck was to benefit from a startling strategic error by his opponents, not once but twice. In 1994, Chen won the Taipei City mayor’s race with just under 44 percent of the vote. This minority vote share translated into victory because the conservative vote was split between candidates representing the KMT and the New Party. In 1998, these two parties joined forces to defeat Chen’s reelection bid. But the lesson was not well and fully learned; in the 2000 presidential race, the KMT failed to unify its supporters under a single candidate. Instead, James Soong, long a KMT stalwart, broke with his party and ran an independent campaign, while the KMT insisted on a much weaker candidate, incumbent vice president Lien Chan. (In the end, Soong captured 37 percent of the
vote, Lien, 23 percent.)

Chen’s victory in the presidential race rested on two factors. First, the KMT split made it possible to win without capturing a significant share of conservative votes. Second, Chen was able to overcome the reluctance of many voters who had shown a willingness to support the DPP in local races, but had doubts about the party’s ability to handle national office. Chen’s 39 percent vote share reflected his successful strategy of reassuring voters that he would not endanger the island’s security by taking an extreme position on the independence issue. Chen’s position on cross-strait relations was not significantly different from those of his opponents; if anything, Chen was more congenial to some of Beijing’s preferences, including opening direct trade and transportation links between Taiwan and the mainland.

Winning the presidency was difficult, but governing Taiwan turned out to be an even bigger challenge for a number of reasons. First, Taiwan’s constitution created a highly problematic institutional environment for the debut of divided government. The ROC constitution combines elements of presidential and parliamentary government, without providing adequate mechanisms for resolving contradictions between the two. For example, the president selects the premier, who heads the executive branch and proposes legislation. The president’s choice does not require legislative approval. If the legislature finds the premier unacceptable, its only option is to undertake a vote of no confidence, which, if it passes, opens the door for the president to dissolve the legislature. Thus, competing incentives make it likely that a legislature that opposes the premier will choose obstinacy and gridlock over decisive action. At the same time, the president’s freedom of action is stymied by the absence of a presidential veto or direct control over the cabinet.

A second problem facing President Chen was a lack of confidence from the start. Not surprisingly, given that he was elected with less than 40 percent of the vote, many Taiwanese doubted his ability. As the economic situation in Taiwan (and the rest of the world) deteriorated, these doubts intensified. But declining confidence further damaged the economy. These two trends reinforced one another, prompting a downward spiral in both the economic and political realms.

This spiral gained further momentum from some key mistakes President Chen made early on. Both the president and his party lacked experience in government—thanks in part to the KMT’s absolute refusal to relinquish meaningful policy-making positions to DPP members until it was forced to do so by the voters—and they made errors in policy and political judgment. One of President Chen’s greatest errors was overestimating the power of the presidency. The influence Taiwan’s Presidents Chiang Kai-shek, Chiang Ching-kuo and Lee Teng-hui derived from their status as chairmen of the all-powerful KMT masked the institutional weakness of the presidency, so it was only after several months in office that President Chen began to appreciate fully the constraints on his office.

However, Chen’s hubris should not be overstated. He recognized from the outset that he would need the support of legislators from the KMT and other parties to govern. His first premier, Tang Fei, was a KMT member who served as defense minister under Chen’s predecessor. Chen’s other cabinet appointments were drawn overwhelmingly from the ranks of the KMT and non-partisans; barely 15 percent of his initial cabinet picks were DPP members. What Chen did not anticipate was the depth of the KMT’s frustration and rage at its presidential defeat. The newly-minted “opposition” party chose a strategy of obstructionism over compromise, with KMT legislators routinely launching blistering attacks on Premier Tang and KMT members of his cabinet.
The KMT vehemently rejected Chen’s early gestures of reconciliation and compromise, hoping instead to drive him out of office, or at least force him to turn over the cabinet to KMT control. But the KMT dared not use the one weapon available to it that might have resolved the conflict unequivocally: a no confidence vote. The party dared not face the electorate so soon after the seeing its chairman, Lien Chan, humiliated in the presidential race. Instead of voting to replace the premier, the KMT launched a petition in the legislature to recall the president. But polls showed little popular support for such a move, and the KMT and its allies eventually shelved the idea, belatedly discovering the value of a “rational opposition.” Still, the damaged unleashed in those early, chaotic months has yet to be repaired. To make matters worse, Taiwan’s mass media have treated Chen with extreme skepticism at best, and many media outlets are actively antagonistic toward the president.

All of these factors combined to create two self-defeating patterns within Chen’s administration. First, because many of Chen’s antagonists were driven less by coherent programmatic differences than by raw political enmity, the administration became paralyzed by an unrelenting fear that it would be ambushed. Any position Chen took was attacked, even if it was consistent with long-standing KMT positions. For example, the “pro-business” KMT countered a DPP proposal to reduce the length of the workweek with a plan that was even more generous to workers. Second, the administration fell into a pattern of crisis management, responding to daily emergencies rather than articulating long-term plans and strategies.

Glimpses of Hope

Despite these difficulties, however, it is possible to discern a number of positive developments in the past twelve months. Above all, President Chen has led Taiwan away from the cliff on cross-strait relations. After mid-summer 1999, when President Lee Teng-hui described the relationship between Taipei and Beijing as a “special state-to-state relationship” relations between the two seemed headed for a crisis. Mainland rhetoric became even more heated in the run-up to the 2000 presidential, climaxing with the February release of Beijing’s White Paper on Taiwan policy and a speech in which Zhu Rongji pointedly warned the Taiwanese people not to elect a “pro-independence candidate” (by which he meant Chen Shui-bian).

In the event, however, Chen proved much less extreme on these issues than Beijing had anticipated. His victory speech and inaugural address both acknowledged the importance of peaceful cross-strait relations, and in those speeches he promised to take no steps toward Taiwan independence, so long as armed attack from the PRC was not imminent. In a speech given on New Year’s Eve, Chen went even further, offering his support for increased economic interaction between the two sides as a precursor to what he called “political integration.” Although Beijing has not acknowledged these overtures, they have won Chen some support in another important capital, Washington. In recent weeks Taiwan has won two important prizes from the U.S., including a robust arms sales package and a visa for President Chen to visit the U.S. Policy statements out of Washington suggest that under the Bush Administration, Taiwan’s relationship with the U.S. will be stronger and more secure than it has been for decades.

Regardless of the reaction in Taiwan or the U.S., Chen’s concessions to Beijing have fallen far short of the Chinese leadership’s requirements. Beijing has repeatedly stated that President Chen must agree to the “one China principle” in order for dialogue between the two sides to resume, a condition Chen is unwilling to accept. A key reason for his reluctance is public opinion within Taiwan. While few Taiwanese hold out much hope of achieving *de jure* independence, most are wary of accepting
Beijing's preconditions for talks.

Although some PRC leaders, including foreign policy guru Qian Qichen, have offered "lite" versions of the one China principle (according to Qian's formulation, "One China" means that there is one China, to which both Taiwan and the PRC belong), the Chinese government holds firm to its traditional view of one China (there is only one China, Taiwan is part of it, and it is the PRC) in the international arena. Thus, Taiwanese fear that if their government agrees to the "one China principle," the gesture will be interpreted as an acknowledging the PRC's superior status, and Taiwan will surrender its claim to a separate international existence. In short, despite weakening enthusiasm for independence among the Taiwanese people, political support for accepting Beijing's terms is still lacking. Without such a consensus, Chen's ability to make further overtures is limited.

Taiwan also made progress in certain policy arenas during President Chen's first year in office. On the issue of arms sales by the U.S., Chen's government sent clear signs well before the arms sales decision was announced that Taiwan would accept a package lacking the most provocative item on Taiwan's wish-list, Arleigh-Burke class destroyers equipped with the Aegis radar system. While the reasons for the Chen administration's retreat were complex, it did give the Bush Administration political cover for its decision to deny Taiwan the Aegis system. Chen's administration successfully promoted long-overdue banking reform legislation, and the cabinet's budget proposal passed with only minor tweaking in the legislature. The new government has made inroads against political corruption as well, and Taiwan's politicians are at least debating important issues that were off the table during the KMT's ascendancy, including sustainable development and balancing economic growth and environmental protection.

The State of the Transition

The next big event on Taiwan's political calendar is the legislative election scheduled for December 1, 2001. With a no confidence vote and early elections increasingly unlikely, the elections offer the first chance for breaking the political logjam that has plagued Taiwan for the past year. As the elections approach, political conditions in Taiwan are extraordinarily complex and volatile. With three significant parties competing, each of which contains factions and tendencies favoring an assortment of coalition options, the only certainty is uncertainty. Still, some features of the landscape are beginning to come into focus.

First, the DPP is a much more significant political actor in 2001 than it ever has been in the past. In fact, despite all the difficulties President Chen has faced in the past 12 months, the DPP still enjoys more popular support than its rivals. In electing Chen to the presidency, Taiwanese broke through an important psychological barrier. The DPP has held national office, and the world did not end. A DPP-led government is not only no longer unthinkable; it has become a reality. At the same time, the DPP is more unified and better organized than its opponents. In early April the party finalized its list of candidates for the year-end elections, ensuring maximum time in which to construct and carry out a coherent electoral strategy. Given Taiwan's complex electoral system, the party's preparations could prove decisive.

Second, the KMT is in disarray. With its support rate hovering around 10 percent, the old ruling party seems a shadow of its former self. Hanging onto its legislative majority will be extremely difficult; if it nominates enough candidates to hold the majority, it may fragment its limited vote share and end up even worse off than expected. As of May, the KMT is still working on its nominations list. In view of the large number of would-be KMT legislators—
which includes former National Assembly and Provincial Assembly members as well as legislative incumbents—maintaining unity through this competitive process is a monumental challenge. At the same time, KMT legislators whose policy preferences and political loyalties are close to those of former president Lee Teng-hui are being courted by the DPP, which sees them as potential coalition partners. For many of them, party chair Lien Chan is leading the KMT in an uncomfortably conservative and pro-unification direction. Of course, the KMT still has an enormous war chest, but it is not clear how the party can allocate and use those resources in this battle.

A third important factor in the run-up to the 2001 legislative election is Taiwan’s changing political environment. The rise of the DPP and the birth of the PFP will make for an unprecedented level of party competition this year. Lien Chan’s weak performance in the presidential election showed that the KMT no longer can count on party mobilization to win elections. The KMT also will find it difficult to employ its traditional mobilizational practices, including vote buying. The Ministry of Justice is targeting political corruption, and most of Taiwan’s municipalities are under DPP control; thus, both central and local governments will be far more vigilant in enforcing the laws against these practices than ever before. At the same time, candidates from each of the parties will have to develop new issues and positions on which to campaign. No longer can the KMT rest its case on the claim that a DPP victory would threaten cross-strait stability. Although there has been little progress on this front under Chen Shui-bian, the long-predicted cataclysm did not come to pass when he assumed office a year ago.

Finally, it is very difficult to predict what role the People First Party will play in this election. The party itself is extremely flexible and focused on strategic considerations. How it will behave in the future is contingent upon a huge range of factors, each of which is, in turn, difficult to anticipate. How many candidates the PFP recruits and nominates, how well those candidates perform, whether or not it chooses to cooperate with other parties before or after the election, which party it chooses as its ally—all of these still are open questions. Only when we know the answers will be able to discern the contours of Taiwan’s future political landscape.

In conclusion, Chen Shui-bian walked a tortuous path in his first year as president of Taiwan. Nonetheless, it is possible to discern glimmers of hope as the year comes to a close. If the legislative elections in December do not yield a workable coalition, it may be very difficult for Taiwan to move forward politically or in the realm of public policy. On the other hand, if the legislative elections bring about a realignment of political forces, either in the form of a new party system or a realignment of individual politicians within existing party structures, Taiwan will have taken an important step toward a more mature political system.
All Is Not Gold That Glitters: 
The Growing Liability of KMT, Inc.

Karl Fields

Introduction
Among others, Chaucer (Canterbury Tales) and Shakespeare (Merchant of Venice) remind us that not all that appears to be golden ends up being so. Addressing in this paper the fate and consequences of the financial and commercial assets of the world’s wealthiest but now deposed political machine, this seems a most appropriate metaphor.

The ostensible purpose of this paper is to provide an update and assessment of the fate of KMT, Inc.—the stable of enterprises and other assets owned and operated by Taiwan’s Nationalist Party (KMT)—since the long-ruling party lost the presidency to the Democratic Progressive Party’s Chen Shui-bian last March. This watershed transition is unquestionably a tribute to the island nation’s remarkable process of political democratization over the past half century. And while credit must be given to the courage and persistence of the opposition, this electoral victory had much more to do with processes occurring within the vanquished KMT itself. My own work seeks to demonstrate that chief among these processes is the problems that have emerged out of the party’s active involvement in the corporate sector and the unrivaled coffers of gold at the party’s disposal.

In providing this update however, this essay makes a more purposeful analytical argument. There is no question that KMT, Inc. can be justifiably criticized as the foundation and catalyst of Taiwan’s heijin or “black gold” politics of cronynism and corruption, with deleterious consequences for Taiwan’s electoral democracy and economic development. This, however, was not always the case. In an earlier time, this remarkably versatile conglomerate was in many ways zhenjin, or “true gold,” benefiting first and foremost the KMT, but also both Taiwan’s democratization and development. However, this past year has not been a kind one for KMT, Inc., as the very processes of democratization and liberalization initially aided but ultimately hampered by these party coffers have revealed its seamiest heijin elements. What once was true gold, this paper concludes, threatens now to be nothing more than yujin, or fool’s gold.

This paper first briefly traces the history of KMT, Inc., from its founding in the mainland era to the present, noting its remarkable expansion and evolving functions, as the needs and long-term goals of the ruling and more recently defeated KMT shifted over time. It then demonstrates both the initial virtues and ultimate vices of the party-owned corporate sector, examining specifically the impact of KMT, Inc. over time on the processes of economic development, political democratization, and the persistent though now waning hegemony of the KMT. The paper concludes with some
speculation on the future prospects of KMT, Inc.,
drawing on a second literary metaphor, that of
the albatross.

**Evolution of KMT, Inc.**

Elsewhere, I examine in more detail the
developmental history of the party-owned
enterprises and distill six separate roles or
functions (jineng) that KMT, Inc. has performed
on behalf of the Nationalist party-state. A
significant resource to the KMT regime
throughout its 55-year dominance of Taiwan’s
political economy, its wealth and prominence
grew substantially over time. For the purposes
of this paper, the primary focus of this section is
the events of this last year, as KMT, Inc.
commences its most dramatic reform process to
date in the face of government scrutiny, voter
revulsion, and even calls by KMT critics for
nationalization.

**A. Origins and Development**

For-profit activities within the KMT date back
to the 1920s in Shanghai, when the party began
trading stocks and cotton and established banking
operations in Shanghai in an effort to raise money
for party operations. In the 1940s, the party
moved to expand its business empire,
determining that party-owned enterprises (POE)
should be set up as legal entities, should not use
the party name, and should employ party
members, except for specialists who needed to
be recruited from outside (Liang and Tian; SCMP,
23 March 2000). By this time, the party
had established companies producing textiles,
machinery, food, flour, rubber, cigarettes and
glass bottles. It also operated banks, insurance
companies and property development firms.
Nearly all of these assets were lost in 1949 when
the regime fled to Taiwan.

These Mainland losses were more than
compensated for by the party-state’s inheritance
of all Japanese *sotokufu* (colonial government)
property and much *zaibatsu* industry as well.
These and a handful of firms brought over from
Mainland provided seeds of the KMT’s massive
wealth today. The KMT’s own published (and
highly selective) account of its empire divides
the historical development of the POE into five
decade-long phases. During the 1950s, or
“Initial Formation” (*chuchuang*) period, several
firms under Nationalist control on the Mainland
were salvaged, transferred and re-established in
Taiwan. During the 1960s, or “Laying
Foundation” (*zunji*) period, KMT, Inc. was still
rather small. Keeping pace with (and in many
cases anticipating) government industrial
policies, the KMT invested in cement,
pharmaceuticals, electronics manufacturing, and
land development.

In the 1970s, or “Development” (*kuozhan*)
period, KMT, Inc. began to take-off
in terms of scope, scale and organizational
complexity. The party established a large number
of new firms and began to make comprehensive
investments in a wide variety of industrial sectors.
The two largest of the seven KMT holding
companies, Central Investment and Kuang Hua
Investment, were established during this period
and began investing heavily in areas of particular
importance to government industrial policy,
particularly petrochemicals and the financial
markets. By the 1980s, or “Transition” (*zhuanxing*)
period, the party established and
promoted a number of insurance and other
financial service enterprises and invested heavily
in engineering, construction and energy resource
firms.

During these early decades, loyal party cadre
presided over and staffed this hodge-podge of
propaganda organs, munitions and basic
manufacturing firms, and financial, construction
and other service enterprises. Many of these firms
had monopolistic or oligopolistic privileges in
market sectors often reserved exclusively for the
party and state. These firms were interconnected
primarily by politicized vertical connections to
the KMT and secretive, complex, and
personalized cross-shareholdings among core members of the party elite.

B. 1990s Behemoth

But if KMT, Inc. was once secretive, monopolistic and grossly inefficient, growing market liberalization, the ending of martial law, and the tutelage of the entrepreneurial Liu Taiying (and his predecessor Xu Lide) brought about dramatic changes in the orientation and management of the enterprises under the party’s control (See Table 1). Chen Cheng’s primary preoccupation was to salvage and re-establish enterprises brought over from the Mainland and incorporate those inherited from the Japanese in order to enhance prospects for recovering the Mainland. Yu Guohua, who served simultaneously as head of the POE and chairman of Taiwan’s central bank utilized KMT, Inc. as a means for the party to dispense patronage and consolidate its hold over the republic. It was under Xu and Liu that the conglomerate came to resemble in many ways Taiwan’s private business groups, or guanxi qiye, with whom it came to compete and collaborate in both the domestic and international marketplaces.

Table 1: Leadership of KMT, Inc.

<table>
<thead>
<tr>
<th>“General Manager”</th>
<th>Tenure</th>
<th>Primary Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chen Cheng</td>
<td>1945-65</td>
<td>Recover Mainland</td>
</tr>
<tr>
<td>Yu Guohua</td>
<td>1965-83</td>
<td>Patronage, Party Power</td>
</tr>
<tr>
<td>Xu Lide</td>
<td>1984-93</td>
<td>Development, Patronage</td>
</tr>
<tr>
<td>Liu Taiying</td>
<td>1993-2000</td>
<td>Profit, Development</td>
</tr>
<tr>
<td>Zhang Changbang</td>
<td>2000-</td>
<td>Retrenchment, Transparency, Profit</td>
</tr>
</tbody>
</table>

During the 1990s, or “Expansion” (kuozhang) period, KMT, Inc. expanded most rapidly. It pioneered ventures in environmental protection and added to its stable of engineering, construction, design and development consulting firms, forming in essence a vertically integrated construction conglomerate within KMT, Inc. The party also established additional firms in banking, securities, and life insurance.

Under the guidance of economics professor and presidential confidant Liu Taiying, the POEs also experienced dramatic internal management and organizational changes. Liu promoted entrepreneurial management, appointed professional managers, strengthened the decision-making powers of the board of directors, established systems of corporate auditing, and expedited the public offering and listing of affiliated companies. The public offerings reduced the profile of the POE and increased the liquidity of party assets. He also forged strategic alliances both among the POE and between the POE and private domestic and foreign capital in an effort to acquire technology and expand economic scope and scale. KMT, Inc. also moved more investments abroad, in support of government diplomatic and development efforts, and as a means to shield investments from taxation and growing public scrutiny (Match, p. 30).

By the mid 1990s, KMT, Inc. consisted of over 150 party-invested enterprises, with the KMT retaining over 50 per cent ownership in roughly one-fourth of these firms. In 1994, the
party registered its corporate holdings under the KMT’s own name for the first time, listing some NTS36 billion (US$1.44 billion) in assets. This however included only the book value of the seven holding companies and excluded cash, real estate held by the party’s finance committee, and overseas properties often held in the name of local Chinese societies but controlled by the party (FCJ, 3Nov94).3

C. The Gold Rush: KMT, Inc. Under DPP Rule

In a study published in January of 2000, two respected journalists estimated total KMT assets at US$20 billion and placed 1998 net assets in party-owned enterprises at US$2.5 billion. The party held majority stakes in 32 firms and minority (but nonetheless often times de facto controlling) interests in more than 200 others (Liang and Tian). The party declared earnings from the POE of nearly US$260 million in 1999, down from earnings of nearly US$400 million the year prior (AFP, 23Mar00). Critics contend that even these sizable asset estimates are understated because they are often based on book not market value of properties and land holdings and exclude many properties offshore (SCMP, 23Mar00). One source contended that the party conglomerate consists of well over 300 firms and that the party controls assets of some US$200 billion (The Australian, 22Mar00).

This enormous wealth and its intimate connections to the KMT’s political dominance and increasingly egregious corruption, not surprisingly put these assets at the center of the 2000 presidential election and campaign. They have remained a prominent topic of the Chen administration’s first year in office.

In a dramatic effort to boost his candidacy by definitively distancing his campaign from the corrupt image of the KMT’s past, KMT candidate Lian pledged in a January 2000 campaign rally to cease the profit-making business operations of the party and turn party assets over to a private foundation. Lian also promised to eradicate the heijin politics, or gang and money connections, that have tainted local, and even national, political contests in Taiwan. In order to bring about these changes, Lian called for the swift revision of current laws to regulate political contributions, eliminate vote buying, and prevent those with criminal records from running for office (CNA, 2Jan00). He also called for the passage of two new laws: a Political Party Law that would preclude political parties from running profit-making businesses,4 and a Trust Enterprise Law outlining practical guidelines for transferring assets from the KMT to a private trust. Lian and the KMT also pledged to speed these laws through the legislative prior to the March election (AFP, 10Jan00).5

The following month, the Democratic Progressive Party issued a central policy resolution contending that that KMT had illegally confiscated assets left behind by the Japanese and had over time wrongfully expropriated state assets and rents that rightfully belonged to the government, not the KMT. The DPP argued that the KMT must prove in all cases that it had acquired its assets legally. Prior to its March election victory, the DPP introduced a law to parliament that would allow the government to deal with KMT assets in accordance with this resolution, force the KMT disclose the origin and nature of all assets, and ban all parties from running businesses (SCMP, 23Mar00).

In spite of these resolutions, Chen came to office in May with reassurances that the DPP government would not launch an attack on the POE. He pledged that while he would live up to his promise to separate state and party assets, his government would do so judiciously, proposing the establishment of an all-party parliamentary committee to investigate the sources of the assets (SCMP, 23Mar00; Metich, p. 31). In the event, the Control Yuan pursued the investigation, completing a report in March of this year, which contends that the KMT in
fact did unlawfully seize properties. At the time of this writing, the report has not yet been officially released, pending a second, possibly contradictory Control Yuan report still in progress (Matich, p. 26). In the Legislative Yuan, work continues on both the Party Law and Trust Law.

Thus after one year in office, the DPP-led Executive Yuan has little to show for its initial promises to tame if not break up or fully nationalize the assets of the KMT. Moreover few expect quick results. If and when the Party and Trust Laws are passed, because many of the assets are in legal companies and in many cases joint ventures, the KMT will have plenty of time to find ways to dispose of them, giving them to individuals or companies with no formal linkages to the party.

Moreover, the KMT has spent the past year (if not the last five years) scrambling to beat the DPP to the punch. The party is in the process of overhauling its business strategy once again, shedding its local stock portfolio and property investments, and jettisoning those overseas investments that have been losing money, including office buildings in Japan and Hong Kong and a resort hotel on Palau, one of Taiwan’s few diplomatic allies. While the KMT claims these moves are part of the party’s ongoing efforts to make the party more democratic, liberal, and transparent in all its operations, the DPP contends these measures are simply an attempt to legalize its theft of property and assets from the government (Matich, p. 32). Unquestionably, the KMT is looking anxiously and nervously at its declining popularity among rank and file voters as the year-end legislative elections draw nearer.

The KMT’s primary initiative has been to live up to Lian’s campaign promise to place the party’s assets in trust. Fourteen months after his initial pledge, Lian announced in early March of this year that the KMT would begin the first of three phases of consigning all KMT assets to trustees by placing NTS2 billion in cash assets in trust, allowing non-partisan financial advisors to invest the assets. In late March, the party placed NTS1 billion in cash with Chinatrust Commercial Bank and NTS$300 million with Central Trust of China. Another NTS$600 million in U.S. government bonds was consigned to Chinatrust Bank (CENS, 26 Mar01).

The KMT further announced that in a second phase, the party would consign all real estate holdings, including non-self use houses and land lots, which it valued currently at some NTS8.7 billion to trust. The carrying out of this second phase could not occur, the party argued, until a political party law and other relevant regulations are enacted. There have been contradictory statements from the KMT over the past six months regarding the volume, value, and original KMT acquisition of these holdings. On March 13, a KMT source placed the number of properties at 1633 plots of land with a combined market (not book) value of NTS16.4 billion (CENS, 13 Mar01). Two weeks later the party claimed that more than 90 percent of the properties were acquired over 40 years ago with a total acquisition cost of NTS$8.8 billion (CENS, 26 Mar01). In August of last year (in response to opposition charges of illegal acquisition), the party reported that these properties included 14 houses and 100 land parcels given to KMT with approval of township councils between 1967 and 1981, fully complying with existing laws. An initial investigation by the KMT found, it was reported, 688 buildings and 927 pieces of land around the island worth a total of NT$8.83 billion. (CNA, 22 Aug00).

Not until the third and final phase would the party proceed with those assets tied up in the party-owned enterprises, which the KMT valued at between NTS$60 and NTS$70 billion (down from a KMT estimate one year earlier of NTS$80 billion or US$4.21 billion) (CENS, 13 Mar01). Profits from these trust funds, it was announced, would be used to “support party activities, for
charitable purposes, and as pensions for retired party workers" (*Straits Times*, 17 June00). As part of its transparency measures, the KMT had also promised early in March of this year to release a complete and detailed list of its assets by the end of the month, but has not yet done so citing the ongoing investigation in the Control Yuan (March, 31).

If KMT, Inc. has been an elusive target, the Chen administration has been more effective in keeping its promises to crack down on *heijin* politics. Chen chose DPP legislator Chen “Mr. Clean” Dingnan to serve as his justice minister to fight political graft. Chen—who acquired the moniker for his anti-corruption efforts in Ilan—set up a special “Black Gold Investigation Center”, estimating that corruption, in addition to wasted funds, costs the government some NT$500 billion (US$16.2 billion) annually, or almost 30 percent of government spending. (*AFP*, 26 Aug00).

In August of last year, the investigation center launched a raid on the Zhenlan Temple, chaired by Taichung city council speaker Yen Jingbiao. Moreover, the former Pingtung County Council speaker—just one of many gangsters turned politicians in southern Taiwan—was executed the same month (*Taipei Times*, 4 Aug00). Also in August, KMT legislator and former chairman of Taitung Investment Bank You Huiyi was indicted for a 1995 stock manipulation case. As the first case to be filed against a standing legislator, this was widely seen as confirmation of government’s determination to crack down on political corruption (*AFP*, 16 Aug00). In January of this year, KMT legislator Wang Linglin—son of China Rebar conglomerate tycoon and long-time KMT ally Wang Youzheng—and another KMT legislator were charged with fraud in a 1990s land deal swindle (*CENS*, 4 Jan01).

Perhaps not surprisingly, *heijin* politics nonetheless continues. In May of this year, senior KMT officials were alleged to have offered bribes to buy votes in the April 2001 Provincial Farmers Association elections (*CP*, 3 May01). These associations are seen as crucial local power bases in the run up for the year end legislative elections. This path dependent course of partisan black and gold political machination remains both tempting, but perhaps ultimately fatal, for the KMT, as the following section reveals.

**KMT, Inc. as Asset and Liability**

Historically, the purposes of KMT, Inc. have been much broader than simply the corruption and collusion associated with *heijin* political activities. The POE in particular, as agents of the KMT, have performed a variety of functions and endowed the regime and party with a particular set of benefits and burdens. This section will demonstrate how KMT, Inc. has facilitated both Taiwan’s economic ascent and democratic transformation, but is now hindering economic and particularly financial liberalization and democratic consolidation. Perhaps most surprisingly, KMT, Inc. has also shifted over time from a key to both the corporate unity and local control of a hegemonic party to a tool wielded at the center by factional antagonists in mutual (and mutually destructive) recrimination. This section examines each of these processes (briefly) in turn.

**A. Economic Development**

**Agent of Development:** KMT, Inc. has been an important element of Taiwan’s developmental state. The party state secured political autonomy by bringing the ‘commanding heights’ of the economy in house, thereby resolving collective action problems through hierarchy and securing political autonomy by retaining or capturing its own profit-producing clients. This entailed circumscribing the emergence of large private capital and substituting state-owned and party-owned capital for private capital as developmental agents, patronage outlets, and sources of regime finance and campaign funds. History and ideology both shaped and facilitated
this strategic response. The KMT is Leninist in organization and remains informed by a quasi-socialist Sun Yat-Sen ideology that has uniquely qualified it for the task. This ideology and organization allowed the KMT regime to justify and carry out the proscription of private capital and assume ownership and management of its own set of industrial enterprises.

Early in Taiwan’s development, the Nationalist state was able to draw upon the deep pockets and scarce entrepreneurial and technological resources found within KMT, Inc. to build expensive public works and invest in projects requiring large capital expenditures (Matich, p. 28). KMT, Inc. was also a primary and relatively savvy investor in a wide variety of high-risk investments and strategic joint ventures in areas where the private sector was unwilling to support or (after the lifting of martial law) legislative opposition stymied the participation of state-owned enterprises.

KMT, Inc. also invested in trade and development centers in Tokyo and Hong Kong to promote products made in Taiwan, particularly the products of Taiwan’s host of small- and medium-sized industries. Those championing the projects insist the motivation was to promote Taiwan’s SMEs and to reduce Taiwan’s trade deficit; national goals pursued through party agents beyond the purview of legislative oversight. Similarly, POE were the vanguard of Lee Denghui’s “go south” initiative in encouraging investments in Southeast Asia, and away from an over reliance on foreign investment in the Chinese mainland. The party’s media enterprises—perennial loss leaders—also had an important role in selling Taiwan abroad (both commercially and diplomatically), employing the services of foreign consulting and public relations firms and distributing glossy print, video and Internet information on Taiwan.

**Tool of Exploitation:** These developmental virtues grew increasingly hollow over time, however, in the face of growing evidence of the economic and particularly financial misdeeds of the party conglomerate. What may have been initially risky and strategic investments gave way to monopoly and oligopoly positions in extremely lucrative industries from munitions and construction to bills finance and security margin lending. Privileged access to insider information and monopoly rents fueled not development, but gross inefficiency, nepotism, and political patronage, hampering essential economic and financial liberalization and handicapping democratization.

As KMT, Inc. grew, the cancer spread from a handful of protected party enterprises to include many state owned enterprises and private conglomerates as well. It is no surprise that in the past year investors have fled and shunned stocks belonging to companies associated with conglomerates known to have cozy relationships with the party. Many of these firms contributed generously to the party in return for favorable business deals and bank loans. Conglomerates such as Tuntex, Everfortune, and China Rebar not only have huge debts, but now also face a far less sympathetic financial system (AFP, 12Sep00).

This divorce of party and state assets is essential to Taiwan’s economic and financial well being, but is not without pain. Fifty years of organic fusion between the institutions and personnel of the party and Taiwan’s developmental state has not and will not end quickly nor easily. Moreover, the KMT-as-opposition not only has the capacity but also some incentive to not just publicize and complain about Taiwan’s recent economic and financial woes, but also to weaken the economy in an effort to tarnish the Chen administration.

**B. Political Democratization**

**Aided Democratic Transformation:** The KMT is both Leninist in organization and has remained until only very recently remarkably authoritarian
in its internal practices (Cheng; Moody). And with the exception of some genuine but heavily-influenced local level democracy (see next section), the Nationalist party-state governed Taiwan prior to events of the late 1980s with a high degree of authoritarianism if not autocracy. There can be no question that the coffers of KMT, Inc. bolstered this rigid internal and external system.

I also contend, however, that the remarkable transition from authoritarianism to democracy was possible only because the potential losers in this process—namely the KMT political elite and their families—could be assured of not only a continued livelihood, but also a privileged position in this new politically democratic arena precisely because of these same party resources. Both Jiang Jingguo and Lee Denghui governed the Nationalist Party with a very heavy hand, but neither of them, particularly Lee, could have promoted Taiwan’s process of democratization if he had not both controlled the purse strings and liberally employed the resources of KMT, Inc. This pot of gold not only funded campaigns, but also provided perquisites and even jobs for the many real and potential opponents to democratization.

**Stymied Democratic Consolidation:**
Although assurances of an uneven playing field may have facilitated elite initial acceptance of democracy, it has obviously exacerbated the problems of institutionalizing a fair and legitimate process of electoral contestation. Because of its literally unprecedented financial resources, the KMT remains the “500 pound gorilla” of Taiwan politics. And even as recent elections have shown that financial resources are not fully fungible in the political marketplace, the KMT’s capacity to “buy” elections through either increasingly illegitimate heijin practices or the more “legitimate” practices of political campaigning deemed acceptable in industrialized liberal democracies, the KMT will continue to hold unfair advantage in, and warp the outcome of, any electoral contest in which it participates.

For example, KMT, Inc. generated profits of some NT$8 billion (nearly US$260 million) in 1998. Speaking of the disposition of these monies, Liu Taiying claimed that half of the profits were used to pay party workers and the pensions of retired party members. The other half, some US$130 million, was available to fund “other party activities.” Arguably, the lion’s share (and in reality probably much more) has been available to fund political campaigns and otherwise enhance the KMT’s electoral prospects. Compare this sum—NT$8 billion—to the People’s First Party’s recently declared annual budget of NT$50 million (*CENS*, 31Mar01) or the DPP’s meager assets. In its recent member re-registration drive, the KMT brought it some NT$200 million in party dues alone, with membership of some 900,000 (compared to an estimated DPP membership of some 300,000) (*CENS*, 3Jan01).

Moreover, despite the KMT’s increasing transparency and the Chen administration’s relatively effective crackdown on some of the more egregious cases of black gold politics, this political corruption remains a cancer of both the party and Taiwan’s democratic consolidation. As Chu Yunhan has argued, organized crime, money and politics have long been intertwined in Taiwan and remain a real threat to Taiwan’s budding democracy (*Sinorama*, Mar00). Perhaps the only means of turning this heijin back into zhenjin would be to follow the (wishful) recommendation of the DPP to have the KMT hand over its assets to create a fund to promote Taiwan’s democracy as compensation for hindering its development in the past (*Taipei Times*, 8May00).

**C. KMT Hegemony**
Strategy of Central Corporatism and Local Factionalism: For many years the KMT managed to maintain cohesion at the center and an equally effective divide and conquer factionalism in local
political contests that kept the party strong and intact. The patronage and profits of KMT, Inc. have played essential but opposite roles at each of these two levels in the party. At the center, factionalism, and certainly defection, have been held in check by effective central control of the assets, profits, sinecures, contracts and other patronage opportunities associated with the KMT-owned enterprises. Straying too far from the center on policy issues or attempting to create a power center or fiefdom separate from the party hierarchy meant forgoing access to these fruits. At the local level, the KMT has long employed a divide and control strategy of encouraging factions and then balancing these factions by providing campaign funds and other resources to those local candidates favored by the central party.

Historically, neither the strategy of central corporatism nor that of local clientelism has been cheap, but both have been effective. The factionalized nature of the KMT and Taiwan’s SNTV/MMCD electoral system has meant that the KMT has had to broker among rival KMT candidates in determining who will ultimately receive the party’s endorsement. One way the KMT has been able to winnow the field of candidates has been to offer sinecures in party-owned enterprises in exchange for candidates’ willingness to bow out of the race and swing their support to the party’s favored choice. The KMT has also been very successful at capturing local political machines by awarding lucrative POE construction and other types of contracts and local monopolies, such as natural gas delivery, to local party bosses. These patronage awards explain much of the KMT’s continuing electoral strength at the local level even as it begins to falter at the national level.

The Centrifugal Pressures of Corruption and the Frankenstein of Local Factions: Liberalization of the political process has, however, altered the stakes by introducing new opportunities for electoral success without the blessings and beneficence of central party leaders at both local and national levels and both within and without the party. Predictably, this has made organized factionalism and even desertion more pronounced at the center, and has led to the disarray of the KMT’s carefully orchestrated local factionalism.

Factional divisions at the center and further defections from the party have not only persisted but grown. Most notable among these recent defectors is James Song Chuyu, who was compelled to take responsibility for a poor KMT electoral showing in 1992. But unlike previous “fall guys,” neither a patronage appointment as provincial governor nor a transfer of millions of dollars from KMT coffers to Song’s own political war chest—in accounts registered in the name of Song’s close relatives—were sufficient to prevent him from leaving the KMT and declaring his candidacy as an independent in the 2000 presidential race and ultimately creating his own party.19

Similarly, political liberalization has also both complicated and ultimately weakened local party patronage. Since the early 1990s, local factions have been less willing to abide by the party line on controversial issues and are more confident in their ability to win elections without party endorsement. This has led many local candidates not nominated by the party to either run as independents or to remain in the race as alternative KMT candidates. This intra-party competition has in turn benefited opposition parties, by diluting the organizational discipline of the KMT voting machine. This increased competition, both inside and outside the party, has also increased campaign expenditures and vote-buying, increasing the popular distaste for the pernicious influence of money politics.

**Future of KMT, Inc.**

Growing popular dissatisfaction with the odd marriage of politics and business in Taiwan in
An increasingly democratic environment has presented opposition politicians, disaffected KMT politicians, and now even the KMT with a mandate to shed unprecedented light on the origin, operation and workings of KMT, Inc. It has also led the party to engage in a thorough financial restructuring and to promote extensive internal political reforms. However, the looming presence of KMT, Inc., its complex intermingling with both the state and private sector, and the vested interests of those dependent upon its fruits—including thousands of party employees and conservative party cadres—suspicous of change—virtually guarantee that neither the nationalization of party assets nor even the substantial weakening of the party’s financial capital political influence is in the cards.

Even as a substantial portion of KMT, Inc. is placed in private trust beyond political influence, thereby limiting opportunities for the party or its invested-enterprises to seek rents or pursue political favors, and even perhaps legitimizing these party coffers to some extent in the eyes of voters, it will not level the playing field. Entrusting party assets will do nothing to limit the revenue stream from these investments to the party. In fact, some contend that the KMT could profit even more by entrusting its assets to professional managers because its only residual function would be profit, not patronage outlet or developmental vanguard or the other responsibilities it has historically shouldered.

But as noted at the outset, there is the real possibility that this shenjin turned heijin, may ultimately prove to be nothing more than yujin, or fool’s gold. Its glitter tempts, but ultimately may give little value to its holder. With apologies to Coleridge, I conclude with stanzas from the poem told by a wizened sailor who abused the very means of his earlier salvation, reaping grave consequences. His only salvation was to atone for his error and cut free the dead weight that cursed him. The KMT could perhaps learn from this ancient mariner in shedding its own heijin legacy.

The Rime of the Ancient Guomindang

Ah! well a-day! what evil looks
Had I from old and young!
Instead of the cross, the Albatross
About my neck was hung.......

The self-same moment I could pray;
And from my neck so free
The Albatross fell off, and sank
Like lead into the sea.

Notes
1 See Fields, forthcoming. This section on the evolution of KMT, Inc. draws substantially on a portion of that chapter. Over time, these functions have included (in descending order of significance) profit sources, patronage outlets, propaganda organs, developmental agents, market regulators, and diplomatic envoys.
2 The following paragraphs draw on this KMT study (Guomindang 1994).
3 Moreover, Liu Taiying has admitted that the actual market value of the KMT’s corporate holdings may be three times that of the book value (see Far Eastern Economic Review 11/8/94).
4 The draft of this law puts few strictures on how political parties run internal matters, but banned party-owned businesses and imposed stringent checks on party finances. The draft included a grace period of six months after its passage for the KMT to hand over its assets to a private trust (CP, 14Jan00).
5 Although the announcement was dramatic, calls for legislating an end to party-run businesses and the transferring – even nationalizing – of KMT assets were certainly not new. Since the lifting of the ban on opposition parties in 1986, opposition politicians and scholars had identified these moves as essential for leveling democratic contests in Taiwan. In fact, promulgating a political party law that addressed these issues was deemed a top priority by the influential 1996 nonpartisan National Development Conference (CP, 14Jan00). Economist and outspoken opponent of the KMT, Zhang Qingxi has long demanded

34
that the KMT “relinquish the vast majority of its assets to the central government in the form of trusts.” He argues that the revenues ought to go to the central government regardless which party is in power, and that the KMT needs to hand over not just its present portfolio and real estate, but also all monies plus interest the KMT has earned by selling off valuable pieces of property. “These assets do not belong to the KMT. They belong to the people of Taiwan and the KMT must return them” (As cited in Match, p. 30).

6 These latter moves also speak to the termination of the now deposed KMT’s role as both developmental and diplomatic vanguard.

7 The KMT rejected an offer by China Development Bank, both because of a perceived conflict of interest and also because of “Liu Taiying’s way of doing things.”

8 The following section draws in part on material discussed in Fields, forthcoming.

9 For example, in 1990 the government announced plans to issue private bank charters to a limited number (five or six) of new commercial banks. A former finance minister informed me that of the 19 applicant investor groups, the KMT’s proposal ranked 15th in terms of its fiduciary and operational soundness. Five licenses were ultimately granted, and the KMT’s Bank SinoPac (Shuxin) has been among the most rapidly growing, amidst charges of favoritism (Lu Rurkang interview January 1994; Fields 1995:149-50; Xu 1997:405).

10 Demonstrating either political savvy or expediency, Tuntex conglomerate’s Chen Youhao quickly switched loyalties from the KMT to the new government, a move that many suspect reflects the sympathies of his erstwhile mentor, former POE czar Liu Taiying.

11 The KMT is quick to point out that the stock market has shed half of its value since Chen took office. A KMT legislator noted last month that for first time, the monthly economic growth rate (in March) was lower than the unemployment rate. Last September, Taiwan also dropped in the World Economic Forum competitiveness rankings from fourth to tenth (Taipei Times, 27 Apr01; 11 Sep00).

12 There has been speculation that the KMT dumped stocks after last year’s election not just to liquidate assets, but also as a means of sulling the DPP’s economic and financial management, charges the KMT has denied (CP, 12 Jul00).

13 On 9 December 1999, KMT legislator Yang Jixiong publicly disclosed that in 1992 a single deposit of over NTS100 million (US$3.1 million) had been placed in an account, in a party-owned bank, registered in the name of the son of independent presidential candidate Song Chuyu. The legislator noted that an account in this same KMT-owned financial institution had also been opened in the name of Song’s sister-in-law. Yang charged that the money in these accounts was probably used in that year’s hotly contested legislative election, when Song played a pivotal role in the campaign as then secretary general of the KMT.

Over the next few weeks, a scandal unfolded that shook the campaign of frontrunner Song for the presidential election that was to be held on March 2000. More significantly, it also shed light on the linkages between the ruling party and business and the ways in which the KMT utilized both its vast financial resources and personal connections to influence politicians and win elections. The fallout from the scandal also revealed the growing, and increasingly unbridgeable, factional divisions within the ruling party. More importantly, while under authoritarian rule, KMT, Inc. had managed to bind the party together, as it served as an effective centralized source of funds and other types of patronage, there was now growing realization among party candidates that voter support could be influenced by exposing secrets of party patronage and vote-buying.

Far more significant than any potential—and clearly biased—criminal findings from the scandal, were the political consequences. Although the popular Song’s ratings in presidential electoral polls declined precipitously in the days following the outbreak of the scandal, it took little persuasive effort to convince voters in Taiwan of the general complicity of the KMT in this latest chapter of money politics, despite continued uncertainty about specifics. KMT candidate Lian Zhan, already trailing in popularity polls, suffered as much as Song from the revelations.

14 With apologies to Samuel Coleridge, author of “The Rime of the Ancient Mariner.”

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Taiwan’s Economy At T+1 And Counting:
Challenges, Dilemmas And Opportunities

Alexander C. Tan

Introduction
On May 2000, Taiwan inaugurated its first transfer of power when Chen Shui-bian was sworn in as the first non-KMT president of the republic. Public expectation of dramatic changes from KMT to DPP administration was tempered by the continued hold of the KMT on the Legislative Yuan. To ensure some level of cooperation from the legislature, President Chen appointed a premier with strong KMT ties and cabinet that is partly staffed by KMT members. The honeymoon period was short-lived, however, as the cabinet tackled the issue of the fourth nuclear power plant construction and Taiwan's energy policy. A political row and stalemate resulted and Tang Fei resigned as Premier and was replaced by DPP stalwart Chang Chun-hsiung.

The DPP administration, seeking to make good on its campaign promises and its internal party politics pressed its agenda on a KMT-dominated legislature. The resulting public squabbles and finger-pointing between the DPP-led executive branch and the KMT-dominated legislature created a perception of political indecisiveness on the part of the new DPP administration. The anxiety of investors and the business community was reflected in the significant decline in stock prices and the depreciation of the New Taiwan dollar.

The main agenda of the paper is to provide an observation and assessment of the prospects and challenges facing the Taiwan economy. A candid discussion and assessment of any country’s economy cannot be separated and delineated from the effects of the politics and political institutions. Having said that, in this paper I will use a more institutional and political economy approach in discussing the prospects, dilemmas, and opportunities for the Taiwan economy.

In the next section, I will briefly review Taiwan’s economic situation before and after May 2000. I will focus mainly on some of the basic economic indicators and how it has changed since May 2000. Following this discussion, I will highlight some critical economic issues that need to be tackled by the current administration and subsequent administrations. As a conclusion, I will then bring to light some of the critical political-economic questions that may compromise the ability of any administration in tackling critical reforms in the face of the pluralization of politics in Taiwan.

Economic Situation
In describing Taiwan’s economic performance, we have to be reminded that everything is relative. When compared to economic performance of many countries in the world and certainly against many of its neighbors, Taiwan’s economic fundamentals are good. Table 1 shows some basic economic indicators. As Table 1
shows, Taiwan GDP growth rate is healthy by world standards. Taiwan continues to enjoy strong economic growth rates, relatively low unemployment, low inflation, strong trade accounts, and high foreign exchange reserve holdings.

However, when the current indicators of economic performance are held up to performance of years past then there are reasons to believe that Taiwan may be headed into economic water that it has never before navigated. A cursory inspection of Table 1 can highlight several points—a relatively low GDP growth rate, decline in industrial production, a depreciating currency, and a lower stock market index. The poorer economic performance may not necessarily have been a result of actions or inactions of the Chen administration but can partly be explained by the general softening of the world economy in general and the US economy in particular. Unfortunately for any politician or government in power, voters are much more short-sighted and more concerned with what the government will do to resolve their problems. Seen from this perspective, whether justified or not the poor performance of the economy has affected the citizen’s approval rating of the Chen administration and thereby possibly threatened the DPP support among partisan independents and the middle class for the December 2001 legislative elections.

The public row over the construction of the fourth nuclear power plant created a mini-crisis of confidence within the business community and resulted in a perception of political instability in the international community. The Economist in an article published in November 2000 reported Taiwan may be headed on an island-wide financial crisis due to the increasing rate of non-performing loans and the saturation of the banking sector. Whether Taiwan is on the brink of a financial crisis is an empirical question but taking a look at several economic trends gives us reason to believe there is a softening in the economy as a whole. Let us now turn to look at some of these economic trends.

Gross Domestic Product (GDP) growth rate has been declining. Figure 1 shows that growth rate of the GDP from 1992 to 2000. Economic growth rate has been quite robust during the 90s decade, until the occurrence of the Asian financial crisis in mid-1997. In the first half of the 1990s, Taiwan’s economy grew by at least 8 percent a year, but after 1997 Taiwan’s economy saw a significant drop in its growth rate. One can point to several factors that may have

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<td>Gross Domestic Product Growth Rate</td>
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Source: Economist, May 7, 2001
contributed to a slow down in economic growth, including the consequences of the financial crisis on Taiwan’s trading partners and the devastating earthquake in central Taiwan in September 1999.

Exacerbating this situation is the slump being experienced by the information technology industries due to weak worldwide demand. Accounting for this decline in world demand for IT products, the Directorate-General of Budget, Accounting and Statistics (DGBAS) has readjusted its estimate of Taiwan’s GDP growth rate downward to 4.78 percent for the year 2001.

The unemployment rate is rising. Figure 2 shows that unemployment rate from June 1998 to March 2001 has been on an increasing trend. Despite this trend, it is not fair to characterize Taiwan’s unemployment as chronic unemployment like that experience by other neighboring countries. Economists generally label unemployment rates close to 4 percent as frictional unemployment. This said, the unemployment rates have increased to levels that were not seen in years past. More importantly, since Taiwan’s social welfare system is still undeveloped there may be undesirable social and political repercussions resulting from the increasing number of displaced workers.

Closer to most of the hearts (or should I say pockets) of Taiwan’s people is what is happening to the stock market. Since March 2000 the stock market has dropped by fifty percent. Figure 3 shows the performance of the stock market as measured by the weighted index from December 1999 to April 2001. The performance of the stock market has been abysmal to say the least. Around March 2000, the stock market weighted index was around 10,000 but since then has taken a significant decline—to about 5,200 in May 2001. Interestingly, it was about the time when the debate on the fourth nuclear reactor led to a stalemate that the weighted index dropped even further. Not until there was some resolution to the issue with the Grand Council of Justices ruling did the weighted index move up again. This drop in the stock index signals a general anxiety in the business community on Taiwan’s political stability.

Due to the participation of a substantial proportion of the citizenry in the stock market, the government felt compelled to take active measures in propping up the stock market by tapping into the “stock stabilization fund.” The
government also actively intervened in the stock market by using funds from postal savings funds and labor insurance funds among others. The active intervention in the stock market, for the record, did not begin with the Chen administration but instead this practice began in
earlier administrations. These intervention measures, while in the short run seem sensible, politically actually create a serious moral hazard problem for society as a whole. Moreover, active governmental interventions in the stock market through the use of public funds create unnecessary perversity in financial markets as the investors may not be socialized into a “risk culture” so to speak.

Another disturbing trend is the depreciation of the New Taiwan dollar. Figure 4 shows the Taiwan dollar and U.S. dollar exchange rate from December 1999 to April 2001. As the figure shows, since the inauguration of the Chen administration in May 2000, the New Taiwan dollar began to depreciate vis-à-vis the U.S. dollar. Interestingly, the biggest depreciation occurred during the period from the resignation of Premier Tang and the impasse that resulted from Premier Chang’s decision to unilaterally halt construction of the fourth nuclear power plant. It is important to remember that when currency A depreciates against another currency B, the demand for currency B increases as people exchange currency A in favor of B.

Reminiscent of the French Socialists victory in the presidential elections in the 1980s, the French Franc depreciated signaling uneasiness or anxiety in the business community. While in the French case the business community was reacting to a possible threat of nationalization, there is no threat of nationalization by the DPP administration. Instead, currency depreciation can be directly attributed to society’s (in general) and the business community’s uneasiness toward the prospect of political instability and political stalemate in Taiwan as a result of a divided government.

A the real estate market continues to be sluggish due to excess supply and businesses are experiencing weakening demands, local banks have been experiencing strains on their own
balance sheet. As reported in *China Times* (Feb. 17, 2001), overdue loans set a new record high of US$23.87 billion in December 2000. This non-performing loan ratio accounts for 5.34 percent of total loans, which is an increase from 4.88 percent in 1999. While this figure may seem low in comparison to the non-performing loan ratio of countries that experienced the financial crisis in 1997, the trend represented by the increase may only be a small symptom of a larger problem as “grassroots financial institutions” which have even worst overdue loan problems are not included in the figure reported by the Central Bank in December 2000 (*China Times Interactive*, Feb. 17, 2001).

Recognizing that something must be done to jump-start the economy, Premier Chang called an economic development conference on January 6-7, 2001 to explore avenues to stimulate the economy. On March 8, 2001, the government unveiled an economic development plan that is aimed at transforming Taiwan into a “green silicon island” by pouring some US$93.75 billion into the economy over the next four years (*Taipei Journal*, March 16, 2001). With these trends and new economic plan in mind, I will now turn to a discussion of several outstanding issues that will challenge the Chen administration in the years to come.

**Outstanding Issues**

It may not be totally fair to assign the blame for the downward trend in the economic indicators I have presented above on the one-year-old Chen administration. Oftentimes, there is a lag between the implementation of an economic policy and when the effect of the policy is felt. Unfortunately for the Chen administration, they were immediately thrust into dealing with the effects of the weakening of the world economy on Taiwan. Needless to say, the executive-legislative deadlock in Taiwan, which was partly brought about by the DPP forcing its own agenda in an opposition-dominated legislature, has not been helpful either.

As mentioned in the earlier section, the Chen administration has proposed a US$ 93.75 billion national economic development plan that calls for Taiwan to become a “green silicon island.” These plans are generally designed to stimulate Taiwan’s sluggish economy and create more jobs. However, the focus of this plan is generally on various projects that will improve the island’s transportation network, electricity supply, and at the same time ensure environmental protection and enhancement. Another key aspect to this plan is to encourage the further growth of the island as an information technology powerhouse by developing and enhancing existing and new science parks.

While the effort is laudable, several critical economic reform and restructuring issues remain outstanding and not directly tackled by the economic development plan. Unfortunately, many of these issues do not have simple solutions. Some of these issues include the reform of the financial and banking sectors; the reform of the stock market; industrial restructuring and upgrading; and, competition from neighbors in the information technology industries.

Since the liberalization of the commercial banking sector in 1990, there are 53 commercial banks and 360 credit cooperatives to cater to a population of only 23 million (*Taipei Journal*, March 23, 2001). Resulting from this saturation in the banking sector, overly competitive loan market, and weak credit supervision, many commercial banks have seen a rise in the incidence of non-performing loans. As reported by the Central Bank, in December 2000 non-performing loans account for 5.34 percent of total loans. Unfortunately, the rise in bad loans in the commercial bank sector is overshadowed by the bad loans in the non-banking financial institutions.

In response, the legislature has passed the financial institutions merger law and the Finance Ministry has drafted a financial holding company
law. The law will ease the merger of weaker banks with larger banks and at the same time allow the establishment of asset management corporations to buy claims on problematic loans. Bank mergers and asset management companies, however, are not panaceas to the problems faced by the financial industry. One likely problem that is occurring in the banking industry today is that the liberalization started in the 1990s that was supposed to have led to more competition is now resulting in a consolidation and domination of the banking sector by a few large private banks and many strong government banks. In other words, the intent of the earlier liberalization is now resulting in an oligopolization of the banking industry.

Besides the problems of too many weak banks and the oligopolization of the industry, further liberalization needs to be undertaken to increase the type of financial product available in the market. As Taiwan’s economy becomes more integrated into the global market and as Taiwan’s industries continue to upgrade and expand, the complex nature of business transactions and capita requirements to finance complex enterprise requires a more sophisticated finance and banking industry. Having said this, liberalization and regulation need to go hand in hand. In order to avoid the occurrence of a financial crisis as in Thailand and South Korea, strict monitoring by financial regulatory authorities is needed.

Banking and financial reforms cannot be discussed without mentioning the need for stock market reforms. The relatively small number of listed companies in Taiwan allows for a manipulation of the market by big investors. Furthermore, the liberal use of market intervention such as using the stock stabilization fund or other public funds have resulted in a perverse investment culture. Reforms in the stock market can begin with the liberalization of the stock market by allowing for a further increase in foreign participation in the market.

Industrial restructuring and upgrading are another critical issue that challenges Taiwan. In the face of the shortening of the product cycle and the challenges from low-cost producers, Taiwan’s small and medium-size industries are facing increasing difficulties in upgrading and remaining competitive in the world market. Indeed many of these industries have moved to Southeast Asia or to mainland China to take advantage of significant cost-savings to remain competitive. The one result of this outward movement of Taiwan’s producers is a possible hollowing-out of the economy.

Likewise, Taiwan faces significant challenges in the information technology industry. As Tun-jen Cheng (2001) recently pointed out, the PRC is increasingly becoming a major competitor for exports in information technology products. While it is true that many of these IT exports by the PRC are related to Taiwanese invested companies in the mainland, the shortening of the product cycle means that Taiwan’s current comparative advantage in IT products will erode sooner rather than later.

**Olson’s Sclerosis, Democratic Deficit, or What?**

Can these necessary reforms be undertaken in light of the pluralization of politics in Taiwan? Reforms under democratic systems are possible but, of course, difficult in light of the increased participation of diverse interest groups in the decision-making process. For most of Taiwan’s earlier development and certainly during the Asian financial crisis, the autonomy of the state technocracy has been a critical component in the decision-making process. That is, the ability of the regime to shelter the technocracy from the larger influences of society provides some breathing space for making critical and important economic decisions and policies.

I argued, in an earlier work, that Taiwan’s ability to avoid the effects of the Asian financial crisis is partly attributed to the political capacity of its relatively autonomous state technocracy.
and buttressed by an interest group structure that is weak and disperse (Tan 2000). Since the inauguration of the new administration on May 2000 and the further consolidation of Taiwan’s democracy, the economic policymaking process and political decision-making has become more transparent. Transparency allows for a larger participation of groups in society in the decision-making process. Furthermore, by making political and economic decision-making more transparent, it not only allow citizens to be more involved but makes public office holders more accountable for their actions.

While the virtues of more democracy in policy making are not disputed, Olson (1982) reminds us that in older democracies decision-making tends to be slow and is characterized by institutional sclerosis. Sclerosis and inefficiency in decision-making result because of rent-seeking behavior of interest groups involved in and/or affected by policies. The questions then is that in time of critical reforms, the rent-seeking process may not only affect the effectiveness of the reform measures but may undercut political will, stamina and persistence of elected officials concerned about being reelected.

NOTES
1 The DPP holds about one-third of the seats in the Legislative Yuan.

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Taiwan’s Economy During Chen’s First Year: 
Is there an Economic Crisis or Just a Recession?

Steve Waiho Tsui

Introduction
A recorded low, 1.06 percent annual rate of economic growth for the first quarter of 2001, since the first quarter of 1975, 26 years ago while the island economy was suffering from an international oil embargo shortly after its take-off in the late 1970’s; a recorded high rate of unemployment approaching 4.0 percent; reduction in both exports and imports in foreign trade; a 50 percent slide of the Taiwan security exchange price index since his inauguration; and the rapid accumulation of public debts which limits further borrowings and means to stimulate the ill economy by the government—these are the cruel economic realities facing Taiwan and also President Chen Shui-bian only one year after the transition of power. The shocking high speed of going downhill for the Taiwan economy partly reflects the unfavorable international market condition caused by a slowing global economic expansion. However, the lack of confidence in the new government’s competence in handling economic matters on the part of the general public, mostly, the business sector, and the inconsistency in economic policies increase the risk, uncertainty and of course, cost in investing in Taiwan. Capital outflow westward to the mainland looking for profitable investment opportunities comes from all lines of the industrial sector, from traditional textile to fast food, and even from Taiwan’s most advanced and internationally competitive manufacturing goods—IC’s and computer-related products.

The current economic conditions in Taiwan may yet signal the existence or approach of a crisis given the fact that Taiwan still manages to have positive economic growth and an increasing income level, on average. However, the severity of the present economic downturn should not be overlooked as a regular contraction of economic growth along a business cycle. Taiwan suffered more this past year than the 1997-1998 Asian financial meltdown. Remedy to the difficulties facing Taiwan is not simple economics. It is politics that matters.

In this paper, I will first give a brief review of the aggregate economic conditions in Taiwan during the first year of Chen’s reign, followed by discussion of more critical issues on a deteriorated environment to attract new investment, and also on the rising unemployment rate and a potential banking crisis as the economy weakens and the government intervenes more frequent in banking operations as a healing policy to business in trouble. As a consequence of this intervention, the banking system has placed itself in an even higher risk position, contrary to the policy goal of a series of financial reform efforts by the government. Concluding remarks then
follow at the end of the paper.

Some Observations on Taiwan’s Macroeconomic Performance during the First Chen Shui-bian Year

A heavy brake on robust economic growth

The latest estimate on Taiwan’s economic growth rate in the year 2000, released by the Directorate General of Budgeting, Accounting and Statistics (DGBAS) of the Executive Yuan, the cabinet, is 6 percent. This is at least a 0.5 percentage drop from forecast values given by research institutes including the Wharton Economic Forecasting Association, and also the forecast made by the DGBAS in September. The rapid slowing down of Taiwan’s economic activities under Chen’s presidency began at the end of last October when the decision to terminate the fourth nuclear power plant project was announced by the government. Following a continuous plunge of the Taipei security market, both the Taiwan Institute of Economic Research (TIER) and the Chungwha Institute of Economic Research (CIER), the two most important non-government economic research and forecast institutions on the island, adjusted their growth estimates downward, from July estimates of 6.37 percent to 6.27 percent by the TIER, and 6.6 percent in July to 6.41 percent by CIER. It is interesting to note that the DGBAS estimate was not revised and was maintained at a high 6.57 percent, which, of course, is the most optimistic and incorrect estimate, even though the DGBAS is also the agency in charge of gathering and compiling national statistics for the government.

In fact, last November, the Wharton, in its economic analysis on Taiwan’s economic prospects, pointed out that non-economic factors, rather than economic conditions, will be dominant in Taiwan’s further economic growth. Given the existing political deadlock between the new government and the oppositions, which is reinforced by an unfavorable exporting market of Taiwan products, mostly related to the slowing down of the U.S. economy, the forecast values made by different institutes for this year’s economic growth in Taiwan are further reduced. At the beginning of the new century, the DGBAS was still confident of a 5.3 percent annual growth rate, which was revised downward to 5.25 percent in mid-February. Both the TIER and CIER came up with more encouraging estimates, 5.69 percent and 5.74 percent, respectively. The Wharton’s latest estimate was 6.3 percent, a downward adjustment from the earlier 6.5 percent, where Merrill Lynch, basing numbers on the stagnating world economy, revised their forecast of Taiwan’s year 2001 economic growth rate to as low as 4.3 percent, from an earlier release of 5.7 percent.

The 1.06 percent annual growth rate in the first quarter of 2001 has proved that all institutions, government and non-government, domestic and international, underestimated the damaging effect of political instability on economic activities in Taiwan. The growth statistic just released not only recorded a 26-year low since the heavy set back on Taiwan’s economic development in 1974 by the first energy-crisis, it also reflected sluggish increases and even a falling trend in major expenditure components. Domestic private investment spending, which will both increase current aggregate demand for outputs and the capital stock thus results in higher productivity in the future, decreased by a rate of 7.54 percent. Public investment expenditures by the government and public enterprises were also reduced by 5.53 percent and 15.17 percent respectively. Consumer spending, the most important demand component against the gross domestic product, merely increased at a rate of 2.02 percent, the lowest growth rate since the quarterly statistics of this item was provided. Government consumption spending decreased by 7 percent despite a 3 percent raise in government employees’ salary since January this year. For the whole year, the DGBAS revised its forecast
to 4.02 percent, compared to its estimate of 5.25 percent made in February.

Earlier this year, the Council of Economic Planning and Development warned that international economic conditions deteriorated significantly beginning in the fourth quarter of 2000. Among the three major economic blocs, the United States suffered from a downturn that was heavier than expected. The Japanese seemed to fail to get over the long-term economic recession, and even the European countries began to experience a weakening of their economic growth. Thus, a lower pace of world economic growth was inevitable.

As a small, open economy with an extremely high dependence on international trade, facing a stagnating international economy, Taiwan will have difficulties in expanding its export market. Given the unfavorable external conditions and the unresolved political struggles and structural issues, the stimulation from an increase in government investment spending was offset by the speeding up of capital outflow across the strait to mainland China to avoid the rising uncertainty in Taiwan’s economic growth.

In fact, in the fourth quarter of 2000, increases in imports of machinery and equipment, an index reflecting the strength of domestic investment, dropped from a previous two-digit growth rate to zero. It was further decreased by 16.3 percent in the first two months in 2001, compared to the same period of 2000. The weakening of investment activities was envisaged. The bear stock market caused significant capital losses to the majority of stock market investors and the shrinking of personal wealth caused consumer spending cuts, and reduction in consumption spending is further effected by the continuously rising unemployment rate. Even though the government launched an NT$810 billion economic revitalizing program, interactions of internal and external factors unfortunately signal an as-tough, or even more difficult, year for Taiwan’s economic growth.

**Economic downturn in all dimensions**

Taiwan’s coincident index of business cycle indicators (http://210.65.15.74/English/i4.html) compiled by the CEPD, fell from 106.8 (1996=100) last September to 100.6 this January. With a slight rebound to 101.2 in February, it dropped further in March and April to 99.8. The leading index gave an even more sorrowful story of a recorded length of sliding over a fifteen-month period, from 108.5 in January 2000 to 93.3 in April 2001.

All components of the business indicators followed the same direction of movement. Financial components began their downturn from October 2000 given the fall in prices and volume of trading in the Taiwan stock market. Real components such as changes in volume of exports, level of manufacturing goods stock, and employment rates in the non-agricultural sector all decreased to a level signaling economic recession.

Another statistic showing the lack of confidence on domestic economic performance by the business sector was also compiled by the CEPD and obtained from surveys on economic growth predictions for the coming three months among domestic firms. In February 2000, the percentage of the sample in the survey having on optimistic outlook on Taiwan’s economy exceeded that with a pessimistic outlook by 39 percent. By the end of the year, the figure was 28 percent. For a longer forecasting period, the coming six months, results from the TIER surveys reported that a similar pattern, percentage difference dropped from 49 percent to 16 percent in the same period.

**Stock market and government policies**

A very high turn over rate and high degree of price and volume fluctuations, even under relative restrictive regulations compared to those in other regional economies, in Taiwan’s security market reflect the hyper-sensitivity of market
reactions to changes in investment conditions, including changes in government policies. Over the last year, Taiwan’s stock market adjusted promptly each time following major economic and political events.

The TSE index (http://www.tse.com.tw/docs1/index.html) surged after the March 18th presidential election to 10,186 on April 5th. It was 8,824 on April 28th when the designated Minister of Economic Affairs of the new government announced that the Ministry would establish a re-evaluation committee on the Fourth Nuclear Power Plant project. On the eve of May 20th, the TSE index climbed up to over 9,000 points. The stock market greeted President Chen in his inauguration with a 300-point drop in the TSE index.

On July 25th, the TSE index fell below the 8000 point “psychological threshold” as a reflection of the lack of confidence in the government’s risk management ability in the Pai-chang Si incident where four civilian lives were lost.

At the end of September, economic minister Lin submitted a proposal to the Cabinet to terminate the fourth nuclear power project. Later on October 3rd, Premier Tung Fe resigned from his post, and the TSE index plunged to 6000 points during the next transaction day. October 27th, Premier Chang announced the Cabinet’s final decision on the project. The TSE index immediately responded by a recorded low of 4,614. It took only six months to slash the weighted average price of all listed stocks into less than half the original level. The estimated asset losses in the stock market alone exceeded NT$4,678 billion, with total losses, accounting for the related business losses, more than NT$10,000 billion, equivalent to the sum of six and a half years of total central government budget, or eleven years of total central government tax revenue.

The government was also busy in tackling the bear market. Policies such as the Traditional Industry Revitalization Plan, the Knowledge-economy Plan, Five Guarantees, Eight Measures, Six Stock Market Stabilization Measures, direct interventions of the market since May 25th by the four publicly managed funds and the National Stabilization Fund, moral persuasions to domestic and foreign institute investors, and even threats to private investors by the Minister of Finance, unfortunately, were all ineffective in halting the continuous souring of the stock market.

The stock market did respond positively in mid-January of this year when a “non-constitutional” ruling by the Supreme Court over the Cabinet’s decision on the Fourth Nuclear Power Plant case was anticipated by the general public. The TSE index rose 248 points. When the ruling was officially disclosed on October 16th, the TSE index claimed 468 points for three consecutive transaction days.

The lack of confidence in the new government and rising uncertainty and risk due to inconsistent policies created further hurdles for the already deteriorated investment environment, to firms and investors from Taiwan and abroad, especially when the mainland’s investment opportunities are enlarging and becoming more profitable.

**Worsening Investment Environment and Soaring Unemployment**

*A rising rate of manufacturing closedowns and shutdowns*

Suspension on the already under construction fourth nuclear power plant, the reversal of the legislation approving the Mei-lung Dam project in southern Taiwan, and the passage of the “84 work hours” revision to the Basic Labor Law are all considered to be negative internal factors on domestic investment climate. In addition, the expectation for an improving relationship across the strait, arising from the friendliness and kindness behind major public speeches by the
President since he came to office, was never realized, prompted a rising share of businesses to decide to close down their investment in Taiwan, or at least, slow down or stop replacing their capital equipment and plant expansions.

Statistics on newly established factories released by the Ministry of Economic Affairs (http://moea.gov.tw/english/estatistics) show that since August 2000, the number of new factories registered within a month decreased steadily, and the number of new factories is 5,731, a 1.97 percent drop from the previous year figure. As for closedowns, more than 400 factories have ceased their operations each month since August, and the total number of closedowns amounted to 4,995, up 25.44 percent from 1999. It must be pointed out that the closedowns of factories not only occurred in traditional industries such as metallic and machinery industry, plastics, textile and garment industries, but also in electrical and electronics, the hi-tech industries in Taiwan.

Recessions across all sectors

The industrial production index, reported by the Ministry of Economic Affairs, gained a total of 7.73 percent in 2000 even though it decreased by 2.7 percent (on an annual basis) in December. The real-estate industry suffered the most by decreasing more than 18 percent, with the manufacturing sector dropping by 2.4 percent. Beginning this year, industrial production declined significantly. The manufacturing sector alone receded by 4.79 percent, a level comparable only to the time of the first oil-embargo in 1975. Production cuts occur in both the export-dominant industries, such as electronics and information products by 6.89 percent, metallic and machinery products by 6.35 percent, and domestic-demand-oriented industry, such as food and food processed products, by 5.53 percent. The most obvious warning signal to Taiwan’s future industrial development and progress comes from the higher than average output contraction in the electronics and information sector, the single most important sector supporting Taiwan’s economic growth for the past several years.

For the first quarter of 2001, forecasts on manufacturing production as a whole predict a 5.75 percent decrease, the largest drop since the first oil-embargo. Both the textile industry and transportation tools are predicted to suffer from a double-digit fall, 12.79 percent and 11.83 percent respectively, followed by the electrical and electronic industry, -6.92 percent, the metallic industry, -5.73 percent, and machinery industry, -4.92 percent.

Statistics also show that total business sales increased by 4.4 percent last December, the lowest rate of growth within a fifteen-month period. For January this year, total business sales actually dropped by a recorded 1.81 percent. Detailed figures show that international business sales decreased by 6.19 percent, and restaurant business sales decreased by 5.04 percent. The last item has particular meaning on consumer confidence about future economic strength.5

Decrease in the number of major investment projects

As a whole, the total capital investment amount in major investment projects from the private sector attained a historic peak of NT$719.2 billion, 50 percent higher than that of 1999.6 The number of major investment projects, on the contrary, continued to fall from 223 in 1999 to 194 in 2000. Meanwhile, over 70 percent of the investment was concentrated in the hi-tech industry. The sixth oil cracking plant of the Formosa Plastics alone was the most important investment item in traditional industries.

The decreasing number of major investment projects revealed that these big-spending plans are carried out by a smaller number of firms; even the average capital expenditure for each plan is expanding. Facing changes in domestic and international economic conditions, any single
Assessing Chen Shui-bian's First Year

firm, by revising its investment decision, may cause a significant drop in investment in Taiwan.\(^7\)

Both the number of new major investment projects and the total capital outlays from them decreased drastically entering this year. For the first two months, projected capital spending for all eleven major investment projects in the private sector amounted to NT$166.3 billion, a 41.4 percent dive from the 2000 level, for a total of 97 projects. Major investing enterprises, in addition, like the UMC and Formosa Plastics, are pending decisions on deferring their investment plans. Given all the unfavorable figures, it is hard to expect private firms will expand their domestic investment activities. The targeted amount of NT$725 billion in major investment projects in 2001 set by the Ministry of Economic Affairs seems rather unrealistic.

**A Rising unemployment rate**

The unemployment rate and the number of unemployed have increased steadily since last April. In July 2000, the unemployed labor force exceeded 300,000 with an unemployment rate of 3.06 percent and in April 2001, the rate of unemployment reached a new high of 3.96 percent with 385,000 unemployed workers. Most of the unemployment increases can be attributed to closedowns of firms and reduction in demand for outputs. Both blue- and white-collar workers share the burden of increasing unemployment; yet, it is the non-skilled labor that suffers the most. In February 2001, the unemployment rate for non-skilled labor exceeded 4.7 percent, a 1.2 percentage jump from the previous figure.

In fact, with a growing unemployment rate, increases in the average wage rate of the employed rose by a recorded low of only 2.5 percent in 2000. Logically, the number of labor disputes increased with the sluggish employment market. The number of labor disputes increased by 37 percent and the number of workers involved in these disputes jumped by 86 percent from the 1999 levels. The social impact of rising unemployment is reflected in rising criminal and suicide rates. Financial burdens on the already-troubled government budget also increased with a steady increase in spending on living allowances and re-training costs for the unemployed.

* A rising rate of bad and non-performing loans in the banking sector

The gloomy overall economic conditions, low rate of growth, rise in unemployment, and increases in business closedowns, have all had an impact on the banking sector. In addition to a decrease in demand, the ratio of non-performing loans in the banking sector (domestic banks and trusted corporations included) as a whole, according to statistics released by the Ministry of Finance (http://www.mof.gov.tw/English), at the end of 2000, an increase of 10.28 percent from the previous year. Among all the institutions, cooperatives of all forms maintained an extremely high ratio of non-performing loans, 15.68 percent, up 14.45 percent from the value of the previous year.\(^8\)

The Central Bank reported that at the end of 2000, non-performing loans in the banking sector as a whole, not including cooperatives, reached NT$773.5 billion, again a historic high. Of the total amount, 44.6 percent were loans to individual debtors. If cooperatives are also added, then the aggregate non-performing loans exceeded NT$900 billion. The seven largest domestic banks,\(^9\) at the end of February 2001, had non-performing loans worth over NT$400 billion, a clear warning signal for a deteriorating credit service quality.

Defaulted borrowers ranged from famous business groups to small and medium size enterprises, and to individuals, most of them mortgagees. The weak economy caused a fall in business profits or even operation losses. The sharply falling stock prices cut deeply in asset values of the investors, even leaving some with
negative personal wealth. The real estate market across the island, with the exception of perhaps Taipei city, was still in the midst of a ten-year downswing such that market value of houses mortgaged to the bank for investment purposes might be lower than the mortgage. Rising unemployment rates caused a fall in family incomes. All of these factors, combined and separately, hampered the debt paying ability of borrowers hence raising the risk level of bank operations.

*Slowing down of export and export orders received*

The value of exports and orders received in 2000 increased by 22 and 20 percent from 1999, given the strong international demand for Taiwan's production. However, the strength of export growth had already weakened in the fourth quarter. Export orders received in the first two months of 2001 slightly increased by 1.8 percent, basically reflecting the vigorous demand growth from Japanese buyers. In fact, orders from other major trading partners, namely the States and the European Union, were falling already. Given the hard landing of the U.S. economy, Taiwan's most important export market, it is hard to expect a stronger export demand to offset the sluggish domestic demand components.

*Conclusion*

Taiwan's economy literally cannot get any worse, according to the latest release of the readings from a composite economic indicator by the CEPD. The composite indicator in the past month fell to the lowest reading possible. Each of the nine indicators making the composite indicator gave a blue light, a reading that indicates a recession. At the same time, readings in the leading indicator, also compiled and released by the CEPD, suggest that the economy will not be getting better in the coming quarter or two. Ironically, if the economy gets worse, the current indicators will fail to show the reality since it is now in its lowest possible value already. This is a perfect example for the case of "indicator failure." Since it is at the bottom already, it is logical to conclude that the economy is approaching a crisis if it is not already in one.

Is the "new" government responsible for the worsening investment environment and the heavy dive of the overall economy in Taiwan only after one year of Chen's presidency? The results from a recent pool on CEO's of Taiwan's top 1000 companies suggested that business leaders had little confidence in the current political situation, with 84 percent saying that they were dissatisfied. For their advice to the government on how to best deal with the country's woes, they urged the government to push forward with concrete practicable economic policy, improve administration efficiency, and treat ameliorating cross-strait relations as the central feature of government action.

The current Taiwan economy consists of three specific characteristics commonly found in the development of Asian economies: a bubble economy dominated by the property and financial markets; a transformation in economic structure; and finally, spillover effects on domestic growth from international market fluctuations.

The last item is a short-run phenomenon such that one can either let the time heal or if an effective counter-cyclical policy can be implemented, it may shorten the suffering period. As for Taiwan, the decrease in demand for its exports is a result of domestic conditions in its trading partners economies, not a result of losing its competitiveness in the international market, at least not yet, especially for its major export items. Taiwan can wait for a market recovery, or, exactly as the government intended to do, it can try to stimulate domestic demand by a higher public, or, private spending level. The reality is that the government does not have the funds in hand to significantly increase public spending, and the private sector, business and consumers, on the other hand, are reluctant to spend more
given the uncertain economic future.

Looking at a long-term point of view, evidence from transactions and prices in the housing market and the stock market over the last ten years suggest that the bubble economy in Taiwan perhaps has finally come to an end. The diversion of excessive productive resources sunk into these two markets can now be released and put into real production opportunities. It is unfortunate that in the mean time the Taiwan economy is also struggling to complete its second structural transformation: from labor-intensive, small to medium business dominated industries to capital and knowledge-intensive hi-tech and information industries, and the modernization of traditional industries by taking the advantages of economies of scale and new technologies. It will take a long time to complete the transformation, and during the process, closdowns of firms, a rising rate of unemployment, and massive capital outflows are all part of the cost.

So, the symptoms are similar, and, whether Taiwan is facing an economic crisis of a very dismal future or “only” suffering from a recession such that once it is over there will be a brighter tomorrow, remains to be seen. The final outcome depends on the policy taken by the government. As for one, the government should refrain from further interventions directly or indirectly with the stock market in order to reduce the incentives for speculative transactions countering the government forces. Resources for making good government decisions are also in short supply. It would be a misallocation of resources to have Taiwan’s ministers safeguard the stock market and try to punish investors who have no confidence in government actions.

Revisions on regulations and, perhaps, basic attitudes toward economic ties across the Strait are urgently needed. The mainland, either as a production base, or as a potential market, is too important for Taiwanese enterprises’ (hi-tech or modernized traditional industries alike), for their growth and survival in the international competition arena.

NOTES
1 The DGBAS is a cabinet level agency of the central government in Taiwan where part of its duties is similar to that of the Office of Management and Budget in the States.
2 Measured by percentage increases in gross domestic product after inflation adjustments. Statistics reported in this paper are all compiled and released by government agencies. The web sites are provided. For statistical growth rates, check http://www.stat.gov.tw/mail.htm or http://www.dg. gov.tw/.
3 However, a former finance minister, Dr. Peter Chiu has pointed out that the scale of this program was exaggerated since the program mixed government expenditure already approved by the Legislative Yuan with new spending items. He also expressed doubts on the effectiveness of this program on rebooting sagging economic growth as only part of the expenditure, NT$110 billion, is in fact new, additional spending to those already appropriated by the Legislative Yuan in the 2001 central government budget.
4 Mr. Yen, the Minister of Finance, once remarked in front of the news media that the government would try very hard to let investors selling their stocks feel regret and sorry. Yet, despite this threat, sellers had proven to be the smart ones.
5 The DGBAS provided results from monthly surveys of consumer confidence for a long period of time. However, result are no longer released as of November 2000. The official explanation of the change of policy was that the results from the surveys would have misleading implications.
6 Major investment projects are investment plans with a capital outlays exceeding NT$200 million.
7 For example, the decision by the UMC to relocate one of its new IC production plants from Taiwan to Singapore caused a significant decline in private investment.
8 Based on these statistics and other information, The Economist predicted the explosion of a local financial crisis in Taiwan before the beginning of the Chinese New Year. The event did not come true, but the problem of extra-ordinary high ratio of non-performing loans and bad debts is yet to be resolved.
9 All these seven banks are or were public banks controlled by the central government, or the Taiwan provincial government before the 1998 downsizing.
DPP’s Fractional Politics and the Issue of Taiwan Independence

Chien-min Chao

The year 2000 was arguably the most critical and dangerous year in the Taiwan Strait area since a new era of understanding was ushered in in the late 1980's by Taiwan, allowing its citizens to establish contacts with relatives in the mainland. On the eve of the second presidential election held in March 2000, Premier Zhu Rongji warned Taiwan voters to think twice before casting their ballots for the “candidate of independence” lest they regret it afterwards. The fact that a pro-independence candidate Chen Shui-bian of the Democratic Progressive Party (DPP) was elected president caught Beijing authorities off guard. However, a year after the stunning results, with the country still reeling because of the political uncertainties brought by the change of helm, relations across the Taiwan Strait have seemingly been stabilized. Yet a relatively calm facade can hardly conceal the tensions beneath. The Beijing authority is much perturbed by the turnabouts the Chen administration has been trekking on the rocky road of cross-strait relations.

Two theories stand out to explain the seemingly lack of orientation in the DPP’s drive to soothe relations with China. Transition theorists stress the pain the new administration, as well as the society, must have suffered in the process of converting a country with a long history of autocracy to democracy. At the heart of the agony lies the issue of Taiwan independence. How could the party convince the people that it has mellowed enough to warrant a safe environment in the Taiwan Strait area? The problem is further complicated by the fact that Chen garnered only just over thirty-nine percent of the popular votes (less than 3 percentage points above another candidate) in the election and his administration has to face a parliament, the Legislative Yuan, in which his party maintains barely a third of the seats. It is clear from the outset that it is politics, not economics, that is at the core of the transition. It is this reorientation from a politics-centered party to suit an economic-centered society that the party feels most uneasy.1

That the government is still in transition was in evidence when the President vacillated in formulating the new administration’s position on the sensitive issue of “one China.” As an opposition parliamentarian, Chen was known to have rejected the principle by claiming that “one China” was the sole representation of the People’s Republic and had nothing to do with Taiwan. In the run-up to the presidential election held in March 2000, candidate Chen promised that, once in office, the issue would be put on the negotiation table. Since taking office, however, he has been running the gamut from a “future one China” to “one China, different definition” to the latest “there is no problem with the issue of China according to the ROC..."
constitution” and “political integration.” His assertion that there was only a “spirit of pursuing negotiation to resolve problems” rather than “consensus with regard to expression of the ‘one China’ issue” at a 1992 meeting between representatives from Strait Exchange Foundation (SEF) and Association of Relations across the Taiwan Strait (ARATS) confounds the issue even more.

The inconsistency ostensibly seen in the new administration’s China policy can also be explained by a second theory, the external influence. It is obvious that both Beijing and Washington have kept a wary eye on the Chen administration. The looming intimidation of a possible military attack from China and the constant reminder that the United States would not come to the rescue should Taiwan declare independence are reasons enough to keep Chen Shui-bian at bay.

As convincing as they are, the two theories have limited explanatory power. The transitionists fail to explicate why a politician as shrewd as Chen Shui-bian could not have made the transition smoother. While Chen and the party have been very sensitive to U.S. pressure, Washington and Beijing have more or less been steady in their respective policies towards Taiwan since Chen’s inauguration. It seems neither theory is capable of explaining the inconsistency that President Chen has exhibited in his policy towards China.

This paper opts for a third approach. I argue that it is the DPP’s factional maneuvering that has been the essential driving force behind Chen’s indecisiveness. Since factional configuration within the party has been fluid, the party’s policies towards mainland China have been affected and undergone drastic changes from time to time. The deep-rooted tradition of factionalism has also led to the conclusion that domestic political considerations constantly outweigh external pressures as determinants in the making of the DPP’s mainland China policies.

It is commonly known that the DPP has been stricken by factions. It is further recognized that the struggles could be nasty at times. Less is discussed as to how this internal division affects the party’s stand on the important issue of mainland China policy.

Finding their origins in an opposition movement called Dangwei, literally meaning out of the Party or KMT, the DPP was organized in a dyadic structure: a part of the party was composed of white-collar professionals with some employed in the public sector; a second part of its sympathizers and supporters came from grass-roots who formed the backbone of the social movements the party had organized. One issue that distinguished the two groupings has been their different views over the status of the island, pitting the moderates who were for de facto independence against the radicals who had been demanding de jure independence. The other issue of dispute has been the island’s relations with China: Is there a need to establish commercial ties with the mainland? What types of contacts should be established? The intensity of the debates has been mollified over the years and the two-faction system has evolved into a one-dominant faction since the mid-1990s. Consequently, the party’s mainland China policies in the past decade have been pretty much the history of adjustment and readjustment of its dominant and radical faction, the New Tide. It is the issue of Taiwan’s relations with China that has been at the center of the party’s transition.

The Higher You Get, the Colder You Become: The Transition Towards Radicalism

The DPP’s existence has been justified by its insistence on the creation of a new Taiwan identity. The party has been dogged from the very beginning by a binary vision on this particular issue. When two prominent figures Huang Sing-
chien and Chang Chun-hong were released after serving time for the 1979 Kaoshiung incident, the moderate Formosa faction (Meilidao xi) was fortified, setting the stage for a bipolar system in which two major factions dominated the internal policy debates for the next decade. By the time the party held its Third Party Congress in 1989, it was quite evident that the bipolar system was very much in existence with two major factions, the Formosa and the New Tide (xincaoliu xi), on the two ends of the Party’s political spectrum and two minors playing a conciliatory third party role. Two new minor factions were formed in 1992 when then legislator Chen Shui-bian split from the Formosa and formed his own Justice United Front and Frank Hsieh, current Party Chairman, who had been close to the radical New Tide, coalesced with a few heavyweights and formed the Alliance for Laissez-faire Nation, for the purpose of year-end election in the Legislative Yuan, a more enduring two-plus-two pattern was formed.

The issue central in the schism has been Taiwan’s status vis-à-vis that of China. Based on this criterion, the past history of that party manifests a full circle gyrating around the issue of zhumin zhijie, or plebiscite by inhabitants, trekking through the territories of calling for creation of a new and independent country known as the Republic of Taiwan to the belief that Taiwan is a de facto independent country and there is no need to further prove that. Under the two-dominant faction system, decisions were usually made out of compromise and the radicals often had the upper hand owing to their capability to maintain better discipline and coherence within their organization, forcing opponents to make concessions.

At its first Party Congress, held in November 1986, a clause was added to the DPP platform stating that “the future of Taiwan should be decided by its inhabitants,” pushing the issue of self-determination to the fore. But differences remained as to how and under what conditions a plebiscite should be carried out. To the moderate Formosa and its allies, self-determination is only one way to demonstrate that the people of Taiwan have the final say in choosing their destiny and independence is only one of the options; but for the more radical New Tide, “self-determination” is equivalent to independence. It was a term devoid of a unanimous understanding from the party’s top leadership down to the rank and file.

The first major test of the faction-stricken decision-making mechanism came in 1988 when disagreements emerged in a Party Congress while debating a possible amendment of the party platform to incorporate the sensitive subject of “freedom of independence.” Radicals led by party chairman Yao Jia-wen demanded that Taiwan “be handed back to its people” and that the DPP must “point out a direction for the people of Taiwan.” Other supporters cited favorable public opinions conducted by the Party machine to bolster the inclusion. But for the moderate Formosa, precaution was heeded and revision was advised against. Faced with this dilemma, two minor factions under the stewardships of Chen Shui-bian, who was a member of the Legislative Yuan and close to the Formosa in ideology, and Frank C. T. Hsieh, who was leaning to the New Tide, came to help with two separate compromise proposals. In the end, a conciliation was struck and the famous “four ifs” were invented: The DPP reserved the right to exercise independence (1) if the KMT and CCP entered negotiation without the DPP; (2) if the KMT betrayed the interests of the Taiwan people; (3) if the CCP attempted to conquer Taiwan by force; and (4) if the KMT refused to implement authentic democracy.

Taiwan’s democratic experiment with the arrival of the native president, Lee Teng-hui, in 1988 and a new wave of democratization among the former socialist states in East Europe and the Soviet Union hastened a drastic change for the
DPP at the turn of the 1990s. Consequently, the Party took a drastic turn towards radicalization, augmenting the power of the New Tide faction.

It was obvious that the influences of the New Tide and the third force were on the rise at the expense of the previously dominant faction the Formosa. (see Table 1) The return of the more radical independence advocates from abroad had helped tip the balance. The elections held in 1991 and 1992 in which the old “ten-thousand-year parliament” (wannien guohui) was structurally rejuvenated boosted the confidence of the young political party.8 Externally, the aversion of the international community displayed toward China after the suppression of the student movement in the Tiananmen Square incident in 1989, the collapse of the former Soviet Union, and the relative improvements of Taiwan’s standing in the international society, manifested by the F-16s sale by the Bush administration and the subsequent revision of its Taiwan policy by the Clinton administration in 1994, had all given rise to a sense of euphemism out of which the radical Taiwan nationalism was nurtured. For the next few years, the radical New Tide was poised to displace the Formosa and become the most dominant faction within the DPP. Consequently, the more open overtures dishonored by the party’s top echelon previously to reach out to China were irrevocably reversed.

The first sign of this sea of change surfaced in 1990 when the radicals asked to redefine the sovereignty of the country at the Second Central Committee Meeting of the Fourth Party Congress so that a more disparate identity could be carved out vis-à-vis China.

To counter the assertion of “one country, two regions,” coined by then Premier Hao Pei-tsun to counter China’s “one country, two systems” offense, and to show disapproval at the newly created National Unification Council, the radical New Tide faction wanted the government to declare that the sovereignty of this nation “does not extend to the Chinese mainland and Outer Mongolia” and to urge the PRC to publicly recognize Taiwan as a sovereign country. The move was echoed by the moderates who were in control of the party machinery in an attempt to reduce the repercussions these new initiatives might create from within the party.9 In the end, a resolution was passed granting the exclusion but with a less abrasive phrase of “de facto sovereignty,” rather than “original sovereignty.”10

The first major transition came in 1991. Influenced by the collapse of the Soviet Union and a new wave of democratization, the newly formed DPP adopted a draft constitution for the future new country entitled the Republic of

Table 1: Compositions of the central standing committees of the DPP Party Congresses

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<td>New Tide</td>
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<td>Other</td>
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Taiwan in August 1991. This was a major step towards severing sovereign relations with China and achieving the status of de jure independence. Two months later at the Fifth Party Congress, Lin Zuo-shui, a parliamentarian deemed as the foremost theorist for the cause of Taiwan independence, made a motion on behalf of the New Tide. It called for an amendment to the party platform to “establish a fully independent sovereign nation by the name of the Republic of Taiwan.”11 Hsu Sing-liang, a heavyweight from the Formosa faction campaign for the Party Chairmanship, reversed a long time position of favoring de facto independence and endorsed the radical proposition in order to garner support from the opposite camp.12 A voting bloc based on temporary political convenience was formed. The Congress then passed a resolution proposed by Chen Shui-bian to include the notorious “independence clause” in the platform and added a condition requiring a plebiscite before a new sovereign country was contemplated. It was further decided that the term CCP referred in the party platform should make way to a more “sovereign” one, the People’s Republic of China. These might have been the greatest change made in the party’s short history of less than two decades. From then on the party was to be stigmatized as the party for independence. The DPP would spend the next decade simply trying to shake off the obnoxious image derived as a result. The DPP had shifted from a more innocuous position where “plebiscite by the inhabitants of Taiwan” without presupposed conclusion of independence was displaced by a radical and fanatic Taiwan nationalism on which nation-building was preeminent.13 From then on, the issue of sovereignty and the creation of a new identity dominated the intra-party debate for years to come. As the party was about to find out, the goal of building a new country was not brought closer by the adoption of the clause as was widely believed, it was gaochu bushenhan (the higher you get, the colder you feel).

From Fanaticism to New Independence

Internal as well as external settings in the early 1990s had so greatly elevated an unrealistic expectation and euphemism within the DPP towards the founding of a new nation that in turn heightened the misgivings of some and the old cleavages along the line of ethnic divide in the society had been aggravated. The manifestation of radical and militant dispositions of the DPP had been confronted with resistance from both within and without the party, prompting a rethinking of the strategy.

The first challenge the DPP had to face was a reinvigorated and rejuvenated KMT. After a shaky start, President Lee Teng-hui gradually consolidated his power base against the old-guard within his party. Lee’s drive to democratize Taiwan and the localization process that was introduced had shortened the distance between the party he was leading and the biggest opposition party, the DPP. To the latter, the KMT was no longer an “outside regime” hijacked by a few elites fleeing from China and estranged from the masses. Expressions made by Lee such as “sad to be a Taiwanese,” “the new Taiwanese,” and “popular sovereignty” were greeted with trepidation by the DPP as they saw their legitimacy undermined irreparably.

On the other hand, the radicalization of the DPP as well as Lee’s localization drive had deepened the apprehension of the right wingers in the KMT over the direction that Taiwan was heading. The New KMT Alliance split from the old party and tried to expand its sphere of influence beyond the politically-oriented northern Taiwan and forayed into areas traditionally more sympathetic to the independently minded DPP. The founding of the Chinese New Party (later the New Party) and the subsequent election for the mayor of Taipei, pitting the popular NP candidate legislator Jaw Shao-kang against his colleague in the Legislative Yuan, the DPP super-star Chen Shui-
bian, and the tepid KMT incumbent mayor and candidate Huang Da-zhou, brought the ethnic confrontation to a new height. However, the intensity of the ethnic confrontations flared in the campaigning and the forthcoming of the first popularly-contested presidential elections in 1996 forced the DPP to make another round of adjustments. The defeat of the DPP candidate Peng Min-ming in the presidential election and the firing of missiles off shore of the island by Beijing on the eve of the election were causes for the change.

The moderates were worried about the emergence of fanaticism. In his much-vaunted book, Hsin hsing ming tsu (The Rising People), former Party Chairman Hsu Hsin-liang broached the idea of a new Taiwan nationalism in an attempt to differentiate it from the old type of nationalism. The old nationalism, according to Hsu, was defensive, timid and hateful in nature, while the new one was based on self-confidence, open-mindedness, and aggressiveness. Hsu questioned the wisdom of building a new nation in light of its relationship with its giant neighbor, China. The key to Taiwan’s future, Hsu argued, was to enlarge its economic and trade territory so that a new bond could be formed between the people and the government so that the old identity problem could be diverted.14 For the DPP veteran stalwart, the then opposition party was facing a crisis. While many countries had taken advantage of the new wave of democratization and successfully broken themselves out of the old rigid autocratic cocoon, Taiwan ran the risk of being excluded from the tide because its incapability to handle relations with China satisfactorily. Hsu’s arguments set the motion for a new round of debate within the DPP in which the old paradigm of Taiwan independence gradually gave way to a new line of arguments.

| Table 2 A contrast of positions between the moderates and the radicals |
|-------------------------------------------------|-------------------------------------------------|
| **pan-Formosa** | **the New Tide** |
| **Ideology** | economics determinism | politics first |
| | Taiwan and China have complementary interests | national security before economic interests |
| **Strategies** | Proactive | Defensive |
| | Taiwan’s living and existence have precedence | new national identity |
| | Dadaan xijin (Westward policy) keep China in check with commercial interests | Qiangban jianjin (self-strengthening and go slow with China) keep China in distance |
| **T/C Relations** | democracy more important than de facto independence | democracy and sovereignty at par sovereignty de jure independence |
| | plebiscite by the inhabitants | plebiscite is independence |
| **Attitudes towards KMT** | outside regime, but changing regime get involved | outside regime, hard to change refuse to participate (National Affairs Conference, National Unification Council) |
| **Means to power** | peaceful means through elections | peaceful revolution, mass movement |
in which pragmatism was added to the equation for the first time. From then on, the well-being of Taiwan and augmentation of strength of the island were elevated at par with sovereignty as the major DPP concerns in strategizing Taiwan’s relations with its neighbor across the Strait.

The moderates were not the only ones to respond to the calls for change. The transformation of the KMT into a new political force that is much more intertwined with the society, the rapid rise of China and the swift integration between the two economies had added new impetus to the old DPP decision-making mechanism. The most dramatic change came when Shi Ming-de, then party chairman and once a die-hard radical independence advocate, made a shocking announcement while visiting the United States in September 1995, triggering a second transition in the party’s stand on the issues of independence and national identity. Shi made it clear that once in power, “there is no need nor the party would declare independence.” This announcement has been deemed by some as a “paradigmatic revolution” in the evolution of Taiwan independence,15 forsaking the old conviction of seeking a new sovereign entity. Even Lin Zhuo-sui felt compelled to rephrase his previous position by saying that “sovereignty is already independent but the goal of nation-building is yet to be fulfilled.”16 Like any revolution, the change forebode an unprecedented vehement wake of debates in the party’s history. The new theory called for an end to the old position that the status of Taiwan had been undecided after Japan ended its colonial rule. To bring down the political establishment was no longer a priority; nor to build a new country. Instead, to craft a new image more appealing to the majority of the local voters and start preparing for a possible changeover of power had taken the precedence.

The humiliating defeat of DPP candidate Peng Min-ming in the 1996 presidential election, getting only twenty-one percent of the popular votes, was the immediate cause prompting this round of transition. Deputy Director of the DPP Cultural Department Chou I-zen issued the “Program of Taiwan Independence for the New Generation” in May 1996, challenging the “old Taiwan independence” publicly. Taiwan independence should not be based on hatred towards China, or towards the “regime from outside” (meaning the KMT), Chou contended, nor on the creation of a new name and flag.17 Maintenance of status quo had emerged as the new marker the younger generation of the DPP wanted to erect. The concern of losing legitimacy because of KMT transformation started the DPP transition so that the two parties would not become indistinguishable. But the transition has resulted in exactly that.

Tables 2 and 3 show that the metamorphosis of Taiwan independence in the mid-1990s was very much a reflection of the factional divergence characterized the party.

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<th>Table 3: A comparison of the old and the new independence movements</th>
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<td><strong>Taiwan’s status</strong></td>
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<td>Status quo (ROC on Taiwan)</td>
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It is apparent that electoral concerns have been the catalysts behind the transition. But external pressures could sometimes also facilitate the change. President Bill Clinton’s visit to China resulted in what appeared to Taiwan to be a disheartening “three no’s policy”—the U.S. would not support Taiwan independence, one China, one Taiwan, nor would the U.S. lend support to Taiwan’s quest for membership in international organizations which require statehood, prompted the DPP Central Standing Committee to issue a statement reaffirming Taiwan as a de facto sovereignty and any change in that capacity would require popular balloting. The notorious “plebiscite for independence” has thus been redefined as “referendum for unification.” In yet another critical resolution adopted by the Party in May 1995 concerning the future of Taiwan, the position that, by constitution, Taiwan is the ROC was acknowledged. This assertion not only brings semblance to the expression “ROC on Taiwan,” coined by former President Lee, it is only a step away from Chen’s latest overture that “there is no problem with the issue of China according to the ROC constitution.”

Chen Shui-bian in the Framework of Factions

President Chen Shui-bian has been lauded for his caution and moderation in handling cross-strait relations on the one hand, but reviled for his vacillation and unsteadiness on the other. In campaign stumpng, candidate Chen struck a conciliatory tone by saying that “Taiwan is a de facto sovereignty and its name is ROC according to the constitution.” This was considered a major break from the belligerent independence rhetoric the party had held previously. It is this confidence-building measure that ultimately won him the presidency. In his inaugural address, President Chen tried to calm the fears among those skeptical of his background by pledging “five no’s”: The new administration under his leadership would not declare independence, not abrogate the official name of the country, not incorporate the “state-to-state theory” into the constitution, not hold referendum on the issue of independence, and would not revoke the National Unification Guides and the National Unification Council.

But President Chen has also said a lot of things only to retract them later. As a member of the Justice Alliance, a minor faction sympathetic to the Formosa in ideology, Chen has been faithfully parroting what his faction, the moderate wing of the party, has been advocating over the years. But Chen’s unexpected victory and the DPP becoming a ruling party have fundamentally altered its factional map and henceforth, its modus operandi.

For the first time in the party’s history, there is a person who commands authority above factions. The history of “rule by factions” (paishi gongzhi) in which important decisions were discussed among chiefs of different factions trying to reach consensus, much like the way the LDP makes its decisions in Japan, is ended. In order to show support to the President and to better position to maximize political gains, four small factions, the Justice Alliance, Alliance for Laissez-faire Nation, the New Dynamics, and the New Alliance for Taiwan Independence formed the Mainstream Alliance. The dominant New Tide faction and the New Century, a weak remnant of the once mighty Formosa, coalesced to form a second power block.

However, the restructuring appears to be only in form rather than in substance and the factional pattern of consensus-seeking in the making of decisions ingrained in the Party’s history has proved hard to shake off.

As the head of a minority government, President Chen wanted to form an administration on a non-partisan basis, a “cabinet of all people” (guanmin neiye). The decision to pick general Tan Fei as the Premier was evidence of that
policy. Faced with strong opposition from the Legislative Yuan, he wanted to build a working alliance between the DPP and a proportion of the opposition KMT legislators with similar ideology. These policies had the support of the Mainstream Alliance, but unfortunately, the coalition between the New Tide and the New Century has been more reluctant to go along. Consequently, Chen was forced to concur with the resignation of Tan Fei to take the blame for the flip-flop over the construction of the fourth nuclear power plant. The New Tide has the lion’s share in the power game as it holds the keys to many important positions such as the secretary generals of both the Party and the cabinet.

Chen Shui-bian’s policies toward mainland China have to be understood in this factional picture. The first victim is the issue of “one China” policy. The Resolution on the Future of Taiwan, passed at the Second Plenary Meeting of the DPP Eighth Party Congress on May 1999, stated unambiguously that Taiwan should forsake the “one China” principle to avoid confusing the international community and facilitating a hostile takeover by the PRC. The party’s leadership on the left wing has constantly warned their followers of self-destruction should the principle be accepted. The president has on different occasions described himself as “ethnic Chinese,” dodging the term “Chinese.” Dr. Lee Yuan-tse, the highly respected head of the Academia Sinica who was believed to have helped tip the balance towards Chen at the last moment of the presidential election campaign by publicly throwing support behind him, was scorned by the DPP hardliners when the Cross-strait Cross-party Advisory Group (CCAG), a task force commissioned by the president to formulate consensus under Lee’s stewardship, came up with a recommendation that the “one China” issue is something the new administration could not run away from. DPP chairman Frank Hsieh, who, along with the President, has been deemed one of the most respected politicians in the ruling party, suffered the same fate when suggesting that unification can be an option. When trying to break the Taipei-Beijing stalemate by proposing sticking to the ROC constitution as a way to counter Beijing’s insistence on the “one China” issue, Hsieh was censured by members of his own faction, demanding that he stick with the party line while speaking on behalf of the party. Another prominent DPP politician, Legislative Yuan member Shen Fu-shiung, was dealt a similar blow when airing the possibility of joint sessions between the National Unification Council, a mechanism designed by former President Lee Teng-hui, and the CCAG as a compromise between the pro-independence advocates and the pro-unificationists.

The dissipation of the moderate wing in the DPP has put Chen in a very difficult position. Former Party Chairman and a major force representing the Formosa faction Hsu Sing-ling resigned from the Party to take part in the 1996 presidential election, only to lose to Peng Ming-ming in the primary. Some heavy-weights within the faction, including Chang Chun-hong, split from the faction to form the New Century faction in 1998 because of dissatisfaction with the Party’s strategy to ally with the KMT and its engagement policy with China designed by Hsu. The Formosa ceased to be a credible political force. (see Table 1) Faced with a single-dominant faction with a radical ideology Chen Shui-bian’s hands are tied. Before being elected president, Chen made it clear that he was in line with the party policy in ditching the “one China” principle since the political dogma belonged exclusively to the People’s Republic of China. But political reality has forced the President to make concessions. In a speech delivered after the surprising victory in March 2000, Chen proposed that “one China” be included as an issue to be discussed between the two sides. Two months later in his inaugural speech in May, Chen initiated that both sides work hard to solve the issue of “one China in the future.” In a speech
one month after that, he echoed the agreement reached during a meeting in 1992 between the two semi-official organizations, the SEF and the ARATS, in which “one China with different interpretations” was the gist. And finally, in his New Year address in 2001, Chen grudgingly complied with the conclusion handed out by the CIAG that “one China” is in line with the ROC constitution.

The twists and turns have vividly illustrated the factional differences engrained in the Party. The flip-flops would undoubtedly provide ammunition for Chen’s opponents, facilitating more disturbances and alienation within his own party.

Conclusion
The surge of radicalism in the early 1990s in the DPP has been a cause of concern for Beijing. It is the radical faction that has to bear the most brunt and henceforth, made the most adjustment. The moderates once allied for strategic reasons with the radicals leading to the adoption of the “clause of Taiwan independence” in the party platform. Interestingly, although the moderates have lost out in the power struggle due to their opponent, the radical New Tide’s extraordinary capabilities in maintaining good organization and discipline, their position on the sensitive issue of Taiwan independence has been adopted by the radicals. Over the years, the moderates have been urging revision of the “independence clause” to alleviate pressure from outside and reduce misgivings from potential voters. Shen Fu-shuang, a member of the Justice Alliance, made the request after then Taipei Mayor Chen Shui-bian lost in his reelection bid in 1998. After assuming presidency, it was rumored that the President was behind the scheme orchestrating a move to repeat the same call by Chen Ze-nan, a member of the New Century faction which is close to the Formosa in the ideological spectrum. For the moderates, the reason for not pushing for a total obliteration of independence is a strategic one so that it can be used as to lever to check against Beijing’s incessant demands.

As for the New Tide, the goal of independence is an untouchable shengzhupai (a holy plate). For a group known for good organization and discipline it must be extremely painful to be forced into concession on that cardinal principle. This explains a lot of the Chen administration’s wavering on the issue of Taipei-Beijing relations.

Looking from the cross-strait point of view, the situation is precarious at best. For Beijing, Chen Shui-bian is as distrust-worthy as one can ever be. Qian Qichen, China’s vice premier and the second in command in the CCP’s Office of Taiwan Affairs, unveiled in July 2000 that both Taiwan and the mainland are parts of China, instead of the more stereotypical “there is one China in the world and Taiwan is a part of it.” It was the first time that a major policy maker dished out such an inclusive definition of China, a reflection of the consternation on Beijing’s part.

Surprisingly, a new sense of urgency that the two sides were on a collision course has prompted them to double their efforts and navigate in waters of rapprochement. The most amazing outcome, as a sign of moving towards the center, has been the simultaneous reaffirming of the KMT’s policies carved out by former President Lee during his first term in office. The official name, the Republic of China, a term accepted by the DPP moderates from the beginning and acquiesced by the radicals by the mid-1990s, has been rediscovered as a buffer zone to settle the heretofore insolvable sovereignty issue. For Beijing, the sovereignty of China is indivisible and there is only one China in the world. Consequently, the mandate of the ROC was ended when the new communist regime was created in 1949. But in light of the fact that the new ruling party in Taiwan, under the heavy influence of the hardliners, might ditch “China” altogether, a more inclusive variant of
“China” has been suggested. Heartening for sure, but this new development is hardly catalyst for thawing relations across the Strait. The two sides are engaged in an intense cold war with a breakthrough nowhere in sight.

First, although the DPP has gradually redefined the terms of independence by stressing preservation of status quo over reconstruction of a new entity, it is highly unlikely that Beijing would find it acceptable. Chen’s New Year address has formally reaffirmed the “one China” creed albeit conditional on the ROC constitution, but it is not expected that Beijing would make any favorable response.

Second, even though the National Unification Guidelines, written in 1992 to correspond with the new developments in the Taiwan Strait area, have been repudiated as faking by Beijing authority from the outset, Chen’s intention towards the document was deemed as an indication of his stand on the independence issue. In his inaugural address, Chen pledged not to revoke the document. In his 2001 New Year speech, President Chen, in an attempt to implement suggestions put up by the CIAG, stressed that he would respond to the recommendation provided by the CIAG to “establish a new mechanism or readjust the old ones [meaning the National Unification Guidelines and the National Unification Council] as soon as possible.” This was construed as a devious way of accepting the old framework set by Chen’s predecessor, President Lee Teng-hui. But nothing has happened. Neither the document nor the Council is annulled, nor are they functioning either.

On top of the pronouncement of “one China” according to the ROC constitution and a possibility of resuming the NUC meetings, President Chen has painstakingly coined the term “political integration” in his latest address. This is a response to suggestions raised by people like DPP chairman Frank Hsieh that unification cannot be ruled out as an option for the people of Taiwan in the future. This is probably as far as the President can travel without mortally alienating his radical cohorts in the Party. Unsurprisingly, no response came from the other side of the Taiwan Strait, either.

The United States is another important factor prodding the two sides to find a common ground. The U.S. has just as much at stake with the two arch-rivals should cross-strait relations take a drastic spin to the worse. According to the Taiwan Relations Act, passed by the U.S. Congress in 1979, the country is obligated by law to keep the Taiwan Strait at peace. As Taipei-Beijing relations were heading into a tailspin since China test-fired missiles in 1996 at waters near Taiwan, the U.S. has been pressuring both sides to exercise restraint. Although it is not at all clear what kind of policy mix the Bush administration has in mind towards China and Taiwan, it is increasingly apparent that the policy of ambiguity is being modified so that any unrealistic expectations such as Taiwanese independence and military invasion from China against the island democracy would be deterred. In the fanfare following the military airplane collision in Hainan between the U.S. and China, and Washington’s decision to allow sale of a big package of arms to the island, the backbone of U.S. policies embodied in what is called the new “three no’s policies” and the “three pillars” developed by former President Clinton, are likely to be continued. In a visit to China in 1998, President Clinton unleashed the “three no’s policies.” To make up for the people of Taiwan, Clinton subsequently added “three pillars” to its cross-strait policy: one China principle, negotiations to settle disputes, and consent from the people of Taiwan for any change of status quo.

The collision of the U.S. espionage airplane with a Chinese jet fighter over the South China Sea illustrates the new relationship between the
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two countries. While economic and trade interdependence has been strengthened tremendously over the past decade, clashes over national interests are also looming large. Flanked by the world’s single superpower that wants to maintain the traditional regional balance of power and by a potential superpower that is increasingly impatient with the current “hegemonic” order, Taiwan must play its cards very carefully. That means less room for independence and henceforth, the radical faction of the DPP is to face continuous pressure to make further adjustments and that the Chen administration will inevitably continue to show inconsistency and incoherence over the issue of China.

NOTES
2 In preparation for the historic summit meeting between the two heads of the semi-official SEF and ARATS, representatives of the two organizations met in November 1992 to discuss the agenda. It was agreed that the “one China” principle expressed with their respective versions. After the agreement, the summit meeting was able to hold in April 1993.
3 The term “Formosa,” invented by the Portuguese in the 16th century when they first saw the island, was borrowed by Taiwan independence advocates and became synonymous with their cause. But for the Formosa faction, their position on the independence is relatively mild within the party. The term “xi” is used by the party to differentiate factions. “Xi” literally means “like system.”
5 Huang Defu, Minjindang yu taiwan diqu zhenzi minzhuhua (DPP and the Democratization in the Taiwan Area) (Taipei: Shiyin, 1993), pp. 118-121.
6 Minjin Pao (Taipei), no. 7, April 23-29, 1988, pp. 16-22.
7 Department of China Affairs of the DDP, Minzhu jinbudang lianian zheche zhongyiao wenjin huibian (Compilation of Important Documents of the DPP), no dates, p. 4.
8 After the end of the Sino-Japanese War, a constitution was promulgated in 1946 by the Nationalist government and elections were held to choose representatives for the Legislative Yuan, the Control Yuan and the National Assembly in the next couple of years. But since retreating to Taiwan in 1949 there had been only a few “supplementary elections” held to fill a few vacancies left by representatives who had passed away and no elections had been held to replace the whole chamber due to the consideration of legitimacy. The elections in 1991 and the following year were the first elections in which all members of the Legislative Yuan and the National Assembly were up for grabs.
10 *Zhonghua zhibao* (Taipei), October 8, 1990, p. 3.
12 *Zhiyi zhabao* (Independence Morning Post), August 26, 1991, p. 3.
15 Julian J. Kuo, *Minjintang zhanxing zhi tuong* (pp. 72
18 “Taiwan qianju jieyiwen,” (Resolution on the Future of “Taiwan”) in Department of China Affairs of the DDP. *Minzhu jinbudang lianian zheche zhongyiao wenjian huibian*, pp. 88-90.
20 The ideal was reflected in the Resolution on the Future of Taiwan.
21 The party held primaries in March to decide nominations for the upcoming Legislative Yuan elections at the end of 2000 and the New Tide faction was the sole winner. The faction has held overwhelming influence over the decisions made both by the party machinery and the administration.
Coping with the Chen Shui-bian Administration:
Beijing’s Wait-and-See Policy and Two-Pronged Strategy

Suisheng Zhao

Introduction: An Eventful but Relatively Quiet Year across the Strait

Although Beijing used military threat against the Taiwan independence force prior to the March 2000 presidential election in Taiwan, the relationship across the Taiwan Strait in the first year of Chen Shui-bian’s Democratic Progressive Party-led government has been relatively quiet. One year after Chen Shui-bian’s inauguration, the pre-election crisis has subsided considerably although tension across the strait remains. This first year has not produced any event that would have caused a violent reaction from Beijing, which, conceivably, could lead to a disastrous U.S.-China military confrontation. The relative quiet across the strait has made a mockery of predictions right before the election that Chen’s election would inevitably lead to war.

This relative quiet is particularly significant in the context of several potentially explosive events taking place around the first anniversary of the Chen administration. Among them, on April 24, the Chen administration was offered by the U.S. Bush administration the most impressive arms sale package in years. On April 25, offering a more explicit commitment to Taiwan than his recent predecessors, Bush said in a television interview broadcast that if the island came under attack from China, he would order “whatever it took” to help Taiwan defend itself. On May 21-23, Chen made a whirlwind transit visit to New York City. He was greeted by more than 20 U.S. lawmakers and the Mayor of New York City who had earlier refused to meet Chinese President Jiang Zemin. Chen’s visit was hailed as “a breakthrough for the diplomatically isolated island.” Surprisingly, China’s responses to all these events, including Chen’s New York visit, have been relatively restrained. With regard to Chen’s New York visit, Beijing only assigned an assistant foreign ministerial level official, Zhou Wenzhong, to deliver a symbolic protest to the U.S. acting Ambassador in Beijing after Chen’s departure for Latin America on May 23. This was in sharp contrast to Beijing’s response to President Lee Teng-hui’s Cornell trip in May 1995, when Beijing not only recalled its ambassador to Washington in protest immediately following Lee’s visit, but also launched military exercises shortly thereafter in the Taiwan Strait.

Some observers have attributed the relative quiet across the strait to Chen’s pragmatic and reconciliatory approach toward China after his election. Indeed, Chen has been skillful in steering “the ship of state between the rocks of reunification with China and the shoals of independence, to a safe but undefined harbor.” However, the other side of the story should also be counted for the relative quiet. That is, Beijing’s pragmatic wait-and-see policy, accompanied by a two-pronged strategy of
military pressure and peaceful united front inducement.

Indeed, Beijing’s leadership was deeply concerned with the prospect of Chen seeking immediate independence after the election as it would force Beijing to enter a war across the Taiwan Strait. Although many leaders in Beijing were aware that it would be almost impossible to bring Chen to heel short of war, most of the leaders at the top, particularly Jiang Zemin, were very reluctant to resort to military actions unless they had exhausted all other options. Jiang could not afford to see the loss of Taiwan during his watch, nor was he willing to confront Taiwan by fighting a war that would not only seriously damage China’s modernization program but also risk too many uncertainties, including the possibilities of U.S. intervention.

As a result, Beijing did not take dramatic military action after the election and, instead, made a wait-and-see policy and continued a liangzou chelue (two hands or two-pronged strategy) of military coercion and peaceful inducement. While preparing the military for the worst-case scenario, Beijing has intensified the united front tactics to invite Taiwan’s opposition politician to visit Beijing and lure Taiwan’s businessmen, particularly high-tech firms, to invest on the mainland. The essence of the wait-and-see policy was to postpone the tough decision until it could no longer be postponed any more. Ideally, Jiang would not have to make the tough decision until he has completed his term as the top leader of China. At that time, he would be able to declare the victory of deterring Taiwan independence in his term and leave the unresolved troubles to his successor.

To Jiang’s relief, the wait-and-see policy accompanied by the two-pronged strategy of military pressure and peaceful inducement seems to have paid some dividends. At the first anniversary of the Chen administration, the cross-strait relationship is still relatively manageable. Although Chen has not made any appreciable concessions to Beijing, he has not been in a position to provoke Beijing by creating any new crises that may force Beijing into an immediate show down. Many of the leaders in Beijing believed that this is because “Taiwan’s economic situation has been sliding and popular resentment is everywhere.” A PLA editorial on May 21, 2001 accorded three causes for the economic problems. One was that Chen has avoided the one China principle and therefore missed opportunities to improve Taiwan’s economic performance by linking with the dynamic mainland economy. The second was an internal power struggle that has dampened policy-making capacity of the Chen administration. And the third was that the Chen administration has spent huge amounts of money procuring arms from the U.S., going beyond Taiwan’s capacity and seriously hurting Taiwan’s domestic economy. In this case, far from moving Taiwan toward immediate independence, the Chen administration has been squeezed by internal economic hardship and political friction to find ways to resume dialogue with Beijing. Those leaders who have expected the political spill-over effect of economic integration across the strait may also point to the effectiveness of united front tactics as the social and economic integration between Taiwan and the mainland has been stronger than ever. More and more, Taiwan’s opposition politicians have visited the Chinese mainland and more and more profits-driven businessmen, including those with high-tech firms, have invested in the mainland in the past year. A Chinese official told this author that the economic integration across the Taiwan Strait may eventually reach the level where neither side could afford to separate from the other. In this case, Taiwan’s independence would be unthinkable.

In this case, while Beijing still deeply distrusts the Chen administration and will not reduce military pressure, it may have to continue the wait-and-see policy. It is reported that Chinese premier Zhu Rongji said “we are still
looking but have seen clearer and clearer” during his visit to Thailand in May 2001. In effect, Beijing has called for new ways of winning over the hearts and minds of Taiwan political oppositions and people with the hope that the opposition will replace the Chen administration in the next presidential election and start negotiations that would be more tuned toward Beijing’s terms. This expectation could just be Beijing’s wishful thinking. If that is the case, the wait-and-see policy will be interrupted. From this perspective, the Taiwan Strait remains one of the world’s most explosive potential flashpoints.

Beijing’s Two Pronged Policy
The two-pronged policy of military coercion and peaceful inducement is not new. Beijing has used this policy for national reunification since the founding of the PRC. Coercive strategy relies primarily upon the use or threat of the use of force in an exemplary and demonstrative manner. In contrast, peaceful inducement is an abstract front strategy that appeals to cross-strait political negotiations and economic and cultural exchanges to win the hearts and minds of the people in Taiwan for eventual reunification. Military coercion and peaceful inducement are two sides of the same coin and coercive logic is embedded in peaceful offense. This two-pronged strategy, however, has failed to reach its objective so far. As a result, Beijing’s policy has become a vicious cycle of peaceful offense and military coercion. This is a very dangerous game and may eventually lead to a war across the Taiwan Strait.

The coercive strategy was used primarily in the early years of the PRC, when Beijing planned to “liberate” Taiwan by military force. Peaceful offense was adopted systematically for the first time in 1979. It is a pragmatic and prudent approach and has been the preferred approach for Beijing’s leaders. It was briefly interrupted during the Taiwan Strait crisis of 1995-96 but was promptly resumed in 1997.

It is not deniable that the peaceful offense brought about some desirable changes in cross-strait relations. The most visible changes were the increasing economic exchanges and the beginning of functional negotiations between semi-official institutions across the Strait. However, Beijing’s peaceful offense never brought it closer to the objective of national reunification in the 1990s largely because of Taiwan’s political changes under Lee Teng-hui who opened up domestic political competition that gave a legitimate voice to Taiwan independence forces. Lee also launched an effort to expand its international space. While Beijing competed with the Taiwan government under the Chiang family before Lee came to power for the sole legitimate representative position of China, Lee quietly shifted the game to a new contest for Taiwan’s sovereign status.

Beijing was very frustrated with Lee. But the moderate and reform-minded leaders in Beijing still held high expectations for the effectiveness of peaceful offense. Jiang Zemin’s eight-point proposal for high-level negotiations to end the hostility across the strait on January 30, 1995 was the most important policy statement of the moderates. However, these moderates had to admit the limits of peaceful offense when they learned that President Lee Teng-hui was granted a visa for the historical visit to the United States in May 1995. Embarrassingly, Beijing’s leaders received relevant information only a few days before the U.S. Department of State officially announced Lee’s visit.

This embarrassing experience with peaceful offense resulted in Beijing’s return to the coercive strategy by launching a series of military exercises aimed at Taiwan in late 1995 and early 1996. The military exercises were accompanied by a strategic shift in the emphasis of Beijing’s policy in the following three aspects. One was to move from non-intervention in Taiwan’s internal politics to “ganyu taizheng” (intervening in Taiwan’s internal politics), including efforts
to influence Taiwan's presidential election outcomes. The second was to move from long-term waiting to "xiangsi tongyi" (setting a deadline for reunification), including setting a timetable for the final reunification. And the third was to move from an emphasis on peaceful reunification to an emphasis on "wuli baotai" (taking Taiwan by force).²

Adopting the strategy of military coercion did not necessarily mean that Beijing really wanted to fight a war with Taiwan. Beijing was reluctant to enter a war with Taiwan at the time for at least two reasons. First, war contravened China’s long-term and fundamental goals of economic modernization. Second, the PLA was not yet ready to decisively win the war. In this case, military exercises in 1995-96 were part of coercive military brinkmanship. Military force was used in an exemplary manner to demonstrate resolution and the willingness to escalate to high levels of military action if necessary. Military brinkmanship aimed at exploiting the fear of war in Taiwan in order to avoid war with Taiwan. China used military threats to reduce the likelihood of a declaration of independence by Taiwan and thereby make war less likely.

However, Beijing’s military strategy was not as successful as Beijing declared. The Taiwan independence movement was not halted by Beijing’s military threat. As a matter of fact, the DPP gained more popularity after the 1996 presidential election and won a landslide victory in the November 29, 1997 county magistrate and city mayor elections. This victory opened up the possibility of the DPP replacing the KMT as Taiwan’s ruling party.

Beijing would prefer to deal with the KMT, which still clung to "one China," rather than the DPP. However, Beijing’s leaders could not come up with any effective means, that was short of war, to deal with the situation after the failure of the military brinkmanship in 1995-96. Therefore, Beijing had to return to peaceful inducement and restarted the Wang-Koo meetings in 1998. But Beijing was caught by surprise by Lee Teng-hui’s “two-state theory” (liangguo lün) in July 1999. The feeling of betrayal ran very deep among Chinese leaders, hard-liners and moderates alike. As a result, Beijing once again interrupted the scheduled Wang-Koo meeting in fall 1999 in protest to Lee’s assertion of Taiwan sovereignty. The relationship across the Taiwan Strait was characterized by a political stalemate, which caused dense clouds to overshadow the 2000 election.

Beijing’s Pre-Election Threat and Post-Election Wait-and-See Policy

While Beijing was intimidated by Lee Teng-hui’s two-state theory, it was concerned even more about the prospect of electing a DPP president in March 2000. To cope with the uncertainty, Beijing decided to take unprecedented pro-active actions to influence Taiwan’s 2000 presidential election. The top priority was to prevent DPP candidate Chen Shui-bian from being elected as president.

Beijing’s main method of influencing Taiwan’s election was to make new threats of using force against Taiwan independence, particularly targeting Chen Shui-bian. These threats were expressed systematically in a new white paper released on February 21, just a month before the presidential election. The White Paper was entitled, “The One-China Principle and the Taiwan Issue” and issued by the Taiwan Affairs Office and the Information Office of the PRC State Council. It noticeably put forth “Three Ifs” to clarify the premise for the mainland using force against Taiwan. Before this White Paper, China had threatened military action only if Taiwan declared independence and/or in the event of foreign invasion of the island. The White Paper added the third “if,” a new circumstance in which China will take Taiwan by force. That is, if Taiwan indefinitely refused “the peaceful reunification through negotiations.”¹⁶ The blunt
warning showed Beijing’s increasing anxiety over Taiwan’s rejection over Beijing’s terms of national reunification.

In the final countdown week, Beijing became very concerned as it saw that the chance for Chen Shui-bian being elected president was boosted by the endorsement of several prominent academics and businessmen in Taiwan. In response, Beijing made another blunt threat. In his NPC news conference on March 15, three days prior to the election, Premier Zhu Rongji threatened the Taiwan voters, saying that “Taiwan independence forces’ victory will spark a cross-strait war and hamper cross-strait peace. We believe that these worries are a logical inevitability and concern all the Taiwan people’s personal destinies.” Zhu tried to create a sense of urgency to influence the election outcome by warning that, “at present, Taiwan people are facing an urgent historic moment. They have to decide what path to follow. They absolutely should not act impulsively. Otherwise, it will be too late for regrets.”

The coercive strategy once again failed and backfired as most Taiwan people and all three major candidates ignored Beijing’s threat. Beijing’s most unacceptable candidate, Chen Shui-bian, was elected as the president on March 18, 2000.

Leaders in Beijing were shocked by this outcome. However, weighing options, pragmatism prevailed as Beijing decided to refrain from using force or making further military threats. From the pragmatic perspective, the overriding task for the Chinese leadership is to turn China into a part of the world economic system. For pragmatic leaders such as Jiang Zemin, although it is important to prevent Taiwan from moving toward independence, China should not sacrifice its modernization efforts as long as Taiwan has not explicitly declared independence, as China needs time to modernize first and deal with many other urgent problems. China has made great efforts to carry out the economic reforms for joining the WTO. In fact the threat posed to political and social stability by the Falungong was the greatest challenge facing the Chinese government at the time. Jiang hoped to fulfill the modernization plan so as to leave his name in history. He did not want to see any disputes that could trigger cross-strait conflict, because this would hamper the execution of his primary task. In this case, the possibility of using military force against Taiwan should be the last choice, one that he would not want to resort to unless he had exhausted all other options.

In this case, Beijing adopted a more ambiguous wait-and-see policy. This policy was elaborated in the first official response by the Taiwan Affairs Office of the PRC State Council five hours after Chen’s election victory. It stated that Beijing would never allow independence for Taiwan but was willing to wait and see the words and deeds of the new president-elect Chen Shui-bian. While this statement firmly reiterated Beijing’s “one China principle,” it purposely left room for further maneuver.

In particular, it is very ambiguous about what action it would take to cope with the Chen administration. On the one hand, the statement said, “the election of a new leader in Taiwan cannot change the fact that Taiwan is part of Chinese territory. The One China principle is the prerequisite for peaceful reunification. Taiwan independence in whatever form will never be allowed. There is only one China, and Taiwan is an inseparable part of Chinese territory.” On the other hand, the statement said, “we should listen to what the new leader in Taiwan says and watch what he does. We will observe where he (Chen) will lead cross-strait relations. We are willing to exchange views on cross-strait relations and peaceful reunification with all parties, organizations, and personages in Taiwan who favor the One China principle.”

The statement made it clear that Beijing
would remain in contact with the Taiwan people rather than the president-elect. In this regard, the statement appealed to “Taiwan compatriots to combine their efforts with ours to safeguard the sovereignty and territorial integrity of the motherland, protect the fundamental interests of the Chinese nation, and realize the complete reunification of the motherland.” It is interesting to note that this statement never mentioned Chen Shui-bian by name once. It used a term, “the leader of Taiwan authorities,” to refer to Chen. The term has since been used in all official PRC publications to refer to Chen Shui-bian up to this day of the first anniversary of Chen’s presidency. Obviously, by not naming Chen Shui-bian by name, Beijing has still left room to work with him once he is backed into the proper corner.

The two-pronged vague wording of the statement showed that Beijing was not ready to carry out its harsh threat of war and wanted to open the door for possible reconciliation with Chen Shui-bian if Chen was willing to accept Beijing’s term of one China. It was reported that Jiang Zemin proposed a 16 characters’ guideline in response to the victory of Chen in the election: “rezhen guancha, laixing dengdai, buji buchao, baochi gaoya” (careful observation, patiently wait, no haste, and keep heavy pressure). This strategy of combining military pressure and peaceful offense together is to make the threat of military force a credible one in the physical sense while avoiding actually fighting war and keeping the danger and huge cost of a real military conflict within limits.

**Beijing’s Wait-and-see Policy supported by the Two-Pronged Strategy**

Although the wait-and-see policy kept the door open, Beijing never trusted Chen and has been deeply suspicious over the Chen administration not only because of his past vocal support for Taiwan independence but also because his party still maintains Taiwan independence as an issue on its party platform. While declaring the wait-and-see policy, Beijing continued the two-pronged strategy of military pressure and peaceful inducement to squeeze Chen to speak the words and take the deeds to the satisfaction of Beijing after he took the presidency.

The first words came from President Chen Shui-bian in his inauguration speech on May 20, 2000 when Chen made a pragmatic proposal on cross strait relations with the core of the so-called “one if and five no’s.” The one if is that, if the PRC gives up any plan to use military force against Taiwan, then Taiwan will retain the status quo by promising “five nos.” That is, no declaration of independence, no change in national title of the Republic of China, no change of constitution, no referendum on independence, no abolition of the Guidelines for National Unification. Chen also expressed his willingness to work with Beijing and jointly deal with the question of a “future one China.” Deviate from DPP party platform, Chen embraced the ROC constitution, which implies one China although a different one from the PRC. As one analysis indicated, Chen believed that “the president of the ROC must be guided not by the DPP platform, which calls for independence, but by his assessment of the realities of the situation.” For him, “war is not an acceptable alternative and therefore neither is de jure independence, which could provoke war.”

By the end of the year, Chen had made several fine tunes in his position on cross-strait relations and moved to a new middle course (xing zhongjian luxian), which was expressed as an idea of economic and policy integration (tonghe lun) in his 2001 New Year Day address. The theory tried to distinguish between “integration” as a process and “reunification” as an end. Before the end can be reached, the relationship must journey through a process of bringing the two sides closer together. This integration theory has caused a lot of debate in Taiwan. But, as one observer indicated, “no one can claim that Chen’s
integration concept is a harbinger of separation.” After a high-profile transit visit to New York City, Chen proposed a new mainland policy, called “five no’s,” during his visit to Guatemala on May 27, 2001. They five no’s are: no provocation against the mainland, no misjudgment of the situation, no acting as a U.S. pawn, no zero-sum game with the mainland, and no halt in the government’s efforts to improve cross-strait relations.

However, Beijing has not been satisfied with Chen’s words of “one if, five no’s,” the “integration theory” as well as the new “five no’s.” Beijing claims that it is still waiting for Chen’s deeds one year after the inauguration. Beijing accused Chen of “always playing shadow boxing and karate or empty-handedness (Kongshoudao) and possesses no sincerity at all in improving cross-strait relations.” Beijing has pointed to many deeds that it has been unhappy with. Among them are Chen’s continuing to seek the most advanced arms from the U.S. and transit visits to the U.S., Chen’s continuing insistence that he is only an ethnic Chinese and his refusal to convene the National Unification Council and assume the position of chairman. In addition, Beijing is concerned with the Chen administration’s continual modification of Taiwan’s textbooks to expand education of the island’s history, the declaration of the new Taiwan dollar to be the national currency instead of a local currency as it was considered in the past, and the consideration of the change of the Republic of China to Taiwan in passports issued by the government.

In a comment on Chen’s new five no’s, Guo Zhenyuan, a researcher in Beijing’s Institute of International Studies, believes that what Chen really wanted to say was “six no’s.” The sixth one is “no acceptance of the one China principle.” Another Chinese scholar, Zhang Yebai, also pointed out that Chen’s high-profile transit visit to New York City itself is a provocative action while one of Chen’s new five no’s is no provocation against the mainland.

To show its dissatisfaction, Beijing has refused to resume cross-strait talks or do any business with Chen and his government. As noticed by the Taiwan Government Information Office publication at the first anniversary of the Chen administration, Chen’s calls “for a resumption of talks have gone unheeded by the Beijing authorities, who seem more interested in entertaining business magnates and members of opposition parties than talking to Chen’s administration.” Indeed, sidestepping the SEF-ARATS process, Beijing has appealed to “people to people” links and waved the olive branch to Chen’s political rivals, particularly the opposition KMT politicians, who have dominated the legislature and blocked almost every major initiative by Chen and his party. Beijing is well aware that Chen has not been able to assemble a working coalition with the opposition parties in Taiwan and struggled with the fractiousness of his own party. In particular, Beijing has watched with satisfaction Taiwan’s economic difficulties caused by the worldwide economic slowdown and domestic political instability under the minority government. Beijing attributed Chen’s difficulties to his failure to improve cross-strait relations and his unwillingness to start the three links with the mainland but totally ignored the effects of the downturn of the global economy on Taiwan, particularly on its high-tech industry. As it is stated in a Remnin Ribao commentary, “After coming to power, because of his administrative errors, he is beset with troubles internally and externally. As the economic situation has been sliding and popular resentment is everywhere, his position is neither stable nor comfortable. Especially, as he obstinately adheres to the policy of ‘no haste, be patient,' he is strongly attacked by all circles within the island.”

In this case, Beijing has decided not to give any opportunities for Chen to break the political stalemate and reduce the domestic pressures from the Taiwan public and opposition parties. In
particular, Beijing has tried to prevent Chen from presenting a “false appearance of peace and prosperity” as Beijing believes that Chen has wanted to play a game of transfiguration to fool the Taiwan people. As a Renmin Ribao commentary stated, “In spite of the obvious cross-strait crisis of his own making, he simply dismisses it as cross-strait relations have not retrogressed, as though he has performed a meritorious service after coming to power. Befogging the minds of the people as such, he wants to benumb the general public, so as to do whatever he likes, practice fraud, and wait for opportunities to make a big fight.” In this case, Beijing would rather see the political stalemate across the strait to continue. Beijing clearly wishes to foreclose the independence issue before negotiations even begin and is waiting for international and domestic pressure to eventually compel Chen to compromise with Beijing’s terms of negotiation under the principle of one China.

To enforce its policy objectives of wait-and-see, Beijing has taken some specific measures to undermine the Chen administration since the inauguration in May 2000. The most important three policy measures follow. First is the continued military threat and pressure from all fronts to marginalize the Chen administration and force the DPP to compromise to Beijing’s one China principle. Second is to use the united front strategy to move along with the so-called Taiwan anti-independence forces, including engagement and dialogue with Taiwan’s opposition politicians of the KMT, the PFP, and the NP. Third is to do everything possible to win the battle over the hearts and minds of the Taiwan people, including making a more flexible interpretation of the “one China” principle. This is a strategy of simultaneous application of peaceful offense and military coercion. Beijing has sustained intensifying military pressure, combined with peaceful political, economic and diplomatic offense, to make more difficulties for the Chen administration. On the coercive front, Beijing has kept the military pressure and refused to assume cross-strait talks with the Chen administration and DPP unless they accept Beijing’s one China principle based on Beijing’s interpretation of the 1992 consensus. To prepare for military action, in late October 2000, Beijing adjusted the composition of the Central Leading Group for Taiwan Affairs (CLGTA) to give the military more voice over the Taiwan issue. Zhang Wannian, the vice-chairman of the Central Military Commission, was appointed CLGTA member. Xiong Guangkai, deputy chief of the PLA General Staff, took over the position of CLGTA secretary. After taking the new position, Zhang Wannian has been talking about the possibility of war with Taiwan in five years when he urged the PLA to step up combat readiness. Jiang Zemin has also made demands for the PLA to vigorously launch troop training through science and technology and take “winning the war” as the underlying objective for every military-related task. China’s weapons purchases and the 14 percent military spending increase in 2001 are directed almost exclusively at Taiwan. China has also accelerated new missile deployments facing the island.

While Beijing has kept military pressure, there have been no military tensions in the strait since President Chen Shui-bian was elected. This is because Beijing has launched a new round of the united front tactics of peaceful offense to widen its policy options. The two major targets of the new round of peaceful united front offense have been the opposition politicians and businessmen in Taiwan. It has intensified all kinds of contact with Taiwan’s political oppositions and business people to negate the gains of Chen during the election. It has seen the dividends of persuading the growing numbers of opposition politicians visiting Beijing to pay homage to the Chinese capital and wooing increasing number of Taiwan executives and high-tech talents doing business on the mainland.
since the election. Beijing believes that it has put increasing pressure on the Chen administration and may result in a realignment of Taiwan’s politics that is favorable to Beijing’s interests.

**Beijing’s United Front Tactics with the Opposition**

One of the two most important objectives in the new round of two-pronged policy offense is to boost united front tactics with the Taiwan opposition parties, which have not only tried to block Chen’s policy initiatives but also to wrest power from him. The logic is simple. The rivals or enemies of the pro-independence DPP and Chen administration could easily become Beijing’s friends or allies in the broad anti-independence united front. For this purpose, since Chen’s inauguration, Beijing has invited many opposition leaders, legislators and scholars to visit the mainland. It was reported that more than one-third of the 221 Legislative Yuan members visited the mainland by the end of 2000.

Before Chen took office, the only opposition party that Beijing was able to cultivate was the New Party, which has never played a role comparable to the KMT or DPP in Taiwan’s politics. Now the ruling party for over 40 years in Taiwan, the KMT, has shifted its opposition to the opposition. A new opposition party, the People First Party (PFP), led by the popular former Taiwan provincial governor James Soong Chu-yu, was founded after the presidential election. The opposition coalition has controlled the Legislative Yuan. The KMT itself maintains 113 seats while Chen’s DPP has only 66 seats.

In this case, Beijing has made an all-out effort to entice the opposition politicians to visit the Chinese capital. The results have been very impressive. One of the most publicized visitors in 2000 was KMT Vice-Chairman Wu Po-hsiung who visited Beijing and Shanghai and met with Beijing’s vice-premier Qian Qishen and China’s heavy-hand Taiwan policy advisor Wang Daohan in November. Another KMT Vice-Chairman, Vincent Siew (Xiao Wanchang), who was the prime minister, Taiwan’s No. 3 leader before he left office in May 2000, also visited Beijing and Shanghai with a delegation of business leaders, including Morris Chang, chairman of Taiwan’s largest computer chipmaker, Taiwan Semiconductor Manufacturing Co. (TSMC), in May 2001. A few days after Siew’s visit, John Chang (Chang Xiaoyan), the former KMT Secretary General and Chiang Ching-kuo’s son, also visited Beijing in late May 2000. In addition, Taipei City’s KMT Deputy Mayor Bai paid a visit to Beijing in February 2001. It has been speculated that the chairmen of the KMT and the PFP, Lien Chan and James Soong Chu-yu respectively, have been invited to visit the Chinese capital and they have accepted the invitation.

This is a strategy to court Taiwan’s oppositions with the attempt to establish a united front against the Chen administration. Beijing has used the united front tactics to cultivate the KMT leaders for many years with limited success. The new twist is that the KMT is now in opposition and is free to take advantage of its relationship with the mainland to compete with its political rival, the DPP and the Chen administration. This new twist, in Beijing’s view, has created the possibility for a new KMT-CCP United Front to isolate the Chen administration and see eventual reunification negotiation with the current oppositions that would replace Chen in the next election.

Beijing’s calculation is that if Chen does not make any appreciable concession, Beijing would not do any business with the Chen administration. Without the acceptance of Beijing, all of Chen’s efforts to find a modus vivendi would be an exercise in futility. In this case, cross-strait relations will not improve and hence political and economic instability would continue in Taiwan for the remaining years of Chen’s presidency. By working with the opposition leaders, Beijing hopes to reduce the chance that Chen gets the
cooperation of the opposition parties and forges a working coalition to stabilize the economy and political situation. This situation would enhance the chance of the oppositions winning the next legislative and presidential elections. A candidate from the KMT or perhaps one on a combined KMT-PFP ticket could defeat Chen or other Democratic Progressive Party (DPP) candidates at the presidential elections in 2004. The united front with the KMT and PFP will then certainly yield dividends. It was rumored that during talks with KMT visitors in recent visits, Beijing leaders offered unspecific political and even economic help to their guests to ensure the KMT could beat the DPP in Taiwan elections.22

As part of the united front tactics, Beijing has softened its insistence on a single definition for the one China principle and suggested a one China of the future ambiguous enough to allow a resumption of relations on the basis of the 1992 understanding between Beijing and the KMT administration. Vice-premier Qian Qichen officially rephrased the rigid one China principle with a more flexible expression for the first time in August 2000. He stated that “there is only one China in the world, Taiwan and the mainland are both parts of China, and China's territory and sovereignty brook no division.”23 This new official statement is different from the longstanding official position that “there is but a single China that is represented by the PRC and Taiwan is part of China.” At his meeting with Wu Poh-hsiung on November 23, 2000, Qian said that “saying the mainland and Taiwan are both a part of one China shows that Beijing is pragmatic and accommodating.”

This new and ambiguous phrase of one China principle was for the first time made unofficially by Wang Dachan as a trial balloon in his November 1997 meeting with Hsu Li-nung, head of Taiwan’s pre-unification New Alliance. Wang said, “the so-called one China concept does not refer to either the ROC or the PRC. The one-China idea indicated a unified China that will be created by the Chinese people of the two sides in the future.”24 Meeting with Lin Yang-kang, former vice-chairman of the KMT Central Committee, in May 1998, Wang repeatedly used this new phrase. He said that “one China should refer to a unified China that is jointly built by compatriots on both sides of the Taiwan Strait, and that the motherland does not mean the mainland but the country owned by Chinese on both sides of the Taiwan Strait.”25 However, reports held that Beijing’s Ministry of Foreign Affairs did not agree with this re-articulation and called Wang’s interpretation of one China “inaccurate.” The Beijing government had not officially confirmed this new interpretation of one China until Qian’s meeting with the KMT politicians in August 2000, three months after Chen came to power in Taiwan.

To ease Taiwan’s concern over Beijing’s insistence on the rights of using force against Taiwan, Beijing also sent a trial balloon with a new interpretation that emphasized the premises of not using force against Taiwan. At a press conference in the Chinese Embassy in Washington DC on February 28, 2001, Zhou Mingwei, the Vice-Minister of the Taiwan Affairs Office of the PRC State Council, made a new expression about the premise of using force. Zhou suggested changing the “three ifs” about the premise for the mainland to use force against Taiwan into “six as long as” to be the premise of not using force against Taiwan. He said that “as long as no foreign force invades and occupies Taiwan, as long as the U.S. abolishes ‘the Taiwan Relations Act’ and does not pass ‘Strengthening Taiwan Security Act,’ as long as the U.S. does not continue selling advanced weapons to Taiwan, as long as the Taiwan authorities promise not to join the Theater Missile Defense System (TMD), as long as the Taiwan authorities promise not to engage in the activities of Taiwan independence in any pattern, and as long as the Taiwan authorities promise to hold peace talks on issues of reunification with the mainland...
within a certain period of time acceptable to the mainland, the Chinese Government will not adopt non-peaceful means to resolve the Taiwan issue.” In a simplified way, he reduced the “six as long as” into “two as long as,” namely, “as long as the Taiwan authorities recognize the one-China principle and as long as U.S. and other countries do not invade Taiwan nor support the Taiwan authorities to use force to resist reunification.” Zhou believed that this new expression would be more acceptable to the Taiwan authorities and help win the battle over the hearts and minds of the Taiwan people.

Beijing Targeting Taiwan’s Businessmen Community

Other than to court the opposition politicians, Beijing’s new round of peaceful offense has also targeted Taiwan businessmen, particularly those in high-tech industries. Businessmen are driven by profit opportunities and by nature are opportunists, a fact that CCP united front tactics have exploited with success in the recent decades. Taiwanese businessmen have been searching for business opportunities on the mainland since the 1980s when the Taiwan government began to lift bans on trade and investment across the strait. They took advantage of the mainland’s cheap labor to set up factories to make sneakers, sporting goods or textiles in the 1980s-1990s. In fact, Taiwan’s entire sneaker industry ignored official restrictions on direct investment, laced itself up and moved to the mainland for the cheap labor and huge market. After China’s economy boomed throughout the 1990s, the flow of Taiwanese investment to the mainland accelerated, irregardless of the “no haste, be patient” policy set by Lee Tenghui.

To fully use the business opportunities on the mainland as a weapon of the united front, shortly after Chen Shui-bian’s election victory in March 2000, Beijing launched verbal warnings against Taiwanese business firms such as Acer and Evergreen Group for their support to Chen Shui-bian’s bid for Taiwan’s presidency. In the meantime, the new silicon wafer project of the Formosa Groups President Wang Yung-ching’s son, Winston Wong (Wang Wen-yang), received a warm welcome in Pudong, Shanghai, because Wang’s Yung-ching’s Formosa Group did not openly endorse Chen Shui-bian. Because developing good “guanxi” (personal relationship) is the key to survival, these big Taiwanese firms could not afford to offend Beijing if they want to continue their business in the mainland. Three months after Taiwan’s presidential election, Acer Group CEO, Stan Shih re-emphasized in a newspaper interview that he was always neutral regarding election campaigns. He even predicted that someday Taiwan and mainland China would be part of the same greater China.

The united front tactics targeting Taiwan’s businessmen has borne fruits for Beijing. A new tide of Taiwan investment to the mainland has come since the inauguration of Chen Shui-bian. According to the figure from Taiwan’s Mainland Affairs Council, Taiwan investment on the mainland almost doubled in 2000. The approved investment cases were 840, amounting to $2.607 billion, representing an annual increase of 72 percent and 108 percent respectively. In the first two months of January-February 2001, there were 137 cases of application for investment to the mainland, amounting to $1.56 billion, representing an increase of 38 percent and 21 percent respectively in comparison with the same months a year earlier. Cross-strait trade also reached $32.386 billion in 2000, an increase of 25.8 percent in comparison with 1999, making Taiwan China’s sixth-largest trading partner and China Taiwan’s second largest trading partner.

Taiwan still bans companies from investing in Chinese chip factories to protect the island’s own chip industry, but many high-tech firms skirt this law by investing through overseas units. These high-tech firms have found futures on the mainland not only due to lower wages but also due to a ready supply of bargain-priced engineering talent. As a New York Times report
indicated, Taiwan is no longer such an alluring place to do business. Land is scarce and expensive. The Hsinchu industrial park was the prototype for Asian technology parks when it opened in 1980. Today, it is overcrowded and prone to brown-outs because of inadequate electricity. In 1999, an earthquake briefly halted production at its chip plants and rattled the global industry. Taiwan’s labor force also comes up short. Its universities turn out 4,000 engineers a year, versus 145,000 in China. In Shanghai, a trained engineer costs one-quarter to one-third that of an engineer in Taipei. The disparity is even greater for ordinary workers.10

After setting up assembly lines in China, several high-tech companies are moving their research centers. Many Taiwanese in the service sector such as securities, insurance and law firms are also creating mainland offices, expecting China to open its service industry to foreign investors when it becomes part of the World Trade Organization. The investment flow has become a deluge. It is striking, as a reporter of Time (Asia) indicated, that Taiwan’s workforce, among the world’s most inventive and productive, is opting for China, not just as a place to invest in but a good place to live. Many Taiwanese who came to Shanghai and Beijing recently were startled by their transformations. The Time (Asia) article quoted a head of one Taipei’s top head-hunting firm, “It was amazingly abrupt—a year ago, suddenly everybody wanted to work in China.” According to an estimate by the Time (Asia) reporter, roughly 300,000 people, including many high-tech engineers and managers, have moved to China from Taiwan, and Shanghai is the hottest destination. This has given rise to a tide of “China fever,” or more precisely “Shanghai fever,” in Taiwan in the recent two years.31 A Beijing publication picked up from the headlines and the cover story of Taiwan’s newspaper and leading business magazines that the “Mainland investment fever” (Dalu touzi re), “Shanghai trips fever” (Shanghai kaoca re), and “high-tech industry westward moving fever” (gaokeji canye xijing re) have come one wave after another in the recent year. It attributed this development as a result of Taiwan’s recent economic slowdown and the prosperous life on the mainland.32

Indeed, economic and business ties across the strait have flourished in contrast to the political stalemate across the strait. One AP reporter found that many young Taiwanese see the mainland as a land of opportunity, not a hostile country. The new migrants are engineers for the high-technology industry and professionals in the service sector, including banking, securities and insurance.33 China’s biggest move to attract Taiwanese technology came in November 2000 when it set up a joint venture with Taiwanese businessman Winston Wong to build a chip factory in Shanghai. The Time (Asia) article reported that Winston Wong, the estranged son of Taiwan’s most colorful executive, has gone into business with Jiang Mianheng, the low-profile son of Chinese President Jiang Zemin. They have started a $1.6 billion venture to make integrated circuits in Shanghai’s new Zhangjiang Industrial Park. Their factory, Grace Semiconductor Manufacturing Corp. (Hongli Bandaoti Gongsii), is wholly foreign-owned, with Wong as CEO and Jiang serving on the board of directors. It broke ground in November 2000 and should start producing eight-inch (20 cm) silicon wafers, used to make computer chips, starting late 2002.34

The accelerated investment and migration of Taiwan’s high-tech firms and talents to the mainland started in late 1999, roughly during the 2000 presidential election. A New York Times report on the first anniversary of Chen’s presidency explained one of the economic causes for the sudden exodus after 1999. “Investment accelerated markedly after a devastating earthquake on Taiwan in 1999. The quake temporarily shut down much of the computer-related industry on the island, which is prone to
quakes, prompting many technology companies to shift production to China. Taiwan investors are also drawn to the vast mainland market. Half of Taiwan's high-tech products are now made on the mainland.35 Indeed, as another New York Times report indicated, Taiwan produced 25 percent of desktop PC's in Chinese plants in 2000. Compal Electronics, the second largest maker of laptop computers, said it would move 15 percent of its manufacturing to China in 2001, another 50 percent in 2002, and the rest within three years.36

The exodus of Taiwan's high-tech firms and talents to the mainland has significant economic and political implications. Economically, this wave of investment outflow is quite differently from the earlier ones. Essentially, the exodus has gone far beyond the realm of sneaker manufacturers looking for cheap workers and has triggered not only an exodus of Taiwan's sunset industries and financial capital, but also of Taiwan's best talents and cutting-edge industries, such as semi-conductor and notebook computers. The Time (Asia) report indicated that the island produces 10 percent of the world's integrated circuits, more than 60 percent of its motherboards and most of its notebook computers. Now Taiwan's two greatest assets—silicon chips and human brainpower—are fleeing to China. China's chip business is getting technology that took Taiwan more than 10 years to develop. Wong-Jiang factory is Taiwan's biggest high-tech project in China. Another one of Taiwan's best-known chipmakers, Richard Chang, is building a nearly identical plant in the same park, Semiconductor Manufacturing International, which includes a school for Taiwanese children. The two firms have lured more than 50 engineers from Taiwan's top chipmakers, offering high pay and prospect of stock options. Combined, the dozen production lines in the two factories should be able to produce about 1/5 of Taiwan's total output. The report quoted a Taiwan economic official that in five years, China may have dulled Taiwan's technological edge and stolen its best people. This may not happen that quickly because of China's inadequate legal protection to the high-tech industry. But the current trend is certainly not good news for President Chen Shui-bian.

If this economic implication is most worrying, the political implication of this exodus could be equally, if not more, worrisome to the Chen administration. It is striking that although the government has warned the possibility that Taiwan's manufacturing economy is being hollowed out, the business community continues to argue hard for the three direct links, on the grounds that having direct trade, travel, and communications will establish Taiwan's role as an operations center. The underling intention, however, is that the three direct links would not only reduce the cost and save time for businessmen doing business on the mainland but also facilitate them enjoying the best of both sides of the strait. Until recently, many companies have been reluctant to take their roots away from Taiwan despite the difficulties of doing business across the strait because the legal and business conditions in Taiwan are significantly better than on the mainland. But if Taiwan were to have direct links, it would then be possible for Taiwan businessmen to enjoy the rule of law and relative transparency in Taiwan while taking advantage of low labor costs, huge market potential, and minimal regulation on the mainland.

It is apparent that as many conglomerates are leaving amid signs of an economic slowdown in Taiwan and making money on the mainland, the support for the Chen government and independence will decline. When more and more China-bound conglomerates are generating more revenue in the mainland market than in Taiwan or elsewhere, they would move their entire businesses and even families to the mainland. As one reporter found, "in dormitory towns of the Yangtze and Pearl River deltas, where the cross-strait migrants are settling, Taiwanese
schools, noodle shops, karaoke parlours and beauty shops are ubiquitous.”

A new social breed is being created—native Taiwanese with long-term mainland Chinese residence, and a new generation of youngster who are born in Taiwan but raised in China. It would be one China for them as long as they can make money on both sides of the Taiwan Strait. It is from this perspective that the *Time (Asia)* report used the title “It’s one China when it comes to getting rich.” It quoted a professor of economics at Taiwan’s National Chengchi University who stated that China’s growing economic leverage could intensify the domestic urge to unify. In this case, those who have already voted once with their feet will be unlikely to cast a ballot for Chen Shui-bian. From this perspective, as Yun-han Chu indicated, the on-going trend has posed the island not only the risk of losing out Taiwan’s industrial core competence but also the risk of the hollowing-out of Taiwanese identity. This emerging cleavage, what Yun-han has called integrationist vs. anti-integrationist (Taiwan’s version of globalist vs. anti-globalist) would cut across the existing mainlander-Taiwanese separation as well as the north-south divide and possibly transfigure Taiwan’s partisan politics. It would not be a surprise if, after the billions of dollars from Taiwanese businessmen are invested on the mainland, Beijing developed highly effective pro-China interest groups to blackmail the island to accept its terms for reunification or at least use its deepening ties with the business community to exert pressure on the Taiwan government. This is what happened in Hong Kong to the colonial government in the closing years of British rule.

**Conclusion: The Uncertain Future**

The wait-and-see policy, together with the two-pronged strategy of military threat and peaceful inducement, has seemingly worked to Beijing’s favor so far. Despite the visions of war conjured by President Bush’s suggestion that the United States could help defend Taiwan with all cost from a Chinese invasion, the government of Chen Shui-bian on Taiwan has been notably quiet. As one observer indicated, “throughout the recent tensions in U.S.-PRC relations, ... Taipei did not rejoice over frictions following the airplane accident nor did it press hard for the Aegis-class cruiser sale as a fitting riposte to Beijing.” Although most Taiwanese politicians have welcomed Bush’s hard-line policy toward Beijing, they have also expressed wariness about becoming a pawn in the power struggle between Beijing and Washington. As Yu-ming Shaw, former deputy secretary general of the KMT, was quoted in the *Los Angeles Times*, “The United States and PRC have every reason to compete. But we cannot afford to be in the middle of that kind of competition. We are too small.”

It is hard to say if this is a result of the wait-and-see policy accompanied with the two-pronged strategy. The fact is that the social and economic integration between the mainland and the island has grown stronger than ever. For two decades, Beijing has lured Taiwanese investment to its shores hoping to make the island more economically beholden but this peaceful offense strategy never worked as well as it has in the past year. The recent fruits of working with the opposition politicians and business community in Taiwan seemed to give hope for the continuation of the peaceful united front strategy, which has been the most preferred strategy for Beijing’s leaders to deal with the Taiwan issue. For Jiang and other leaders at the top, the last thing they want is to face another crisis across the strait that would force Beijing to use force against Taiwan. In this case, while they have accused the Chen administration “to promote independence by postponing the reunification process” (*yitu chudu*), they would rather continue the wait-and-see policy and postpone military action as long as possible.

However, the continuation of the wait-and-see policy does not mean that the dangers of military conflict across the strait have been
reduced. Beijing's continuation of the wait-and-see policy is certainly not based on a sophisticated understanding of the political and economic dynamics in Taiwan. Beijing is right that Taiwan public opinion is both divided and volatile. In this case, it is indeed to Beijing's advantage to use the united front tactics to exploit the ties with the KMT and other opposition politicians in Taiwan while isolating the die-hard supporters of Taiwan independence. However, there is a difference between Beijing's exploitation of Taiwan's oppositions and the oppositions' exploitation of their ties with Beijing. Taiwan's oppositions are constrained by Taiwan's electoral politics and hence the concession they can make to Beijing has to be tested ultimately at the ballot box on the island.

Although the Chen administration has been troubled by its inability to improve both the domestic economic situation and cross-strait relations, the opposition has not become more popular in the polls the year after the DPP gained power. To work with Beijing may increase the number of their cards dealing with the DPP administration. However, the Taiwan oppositions are hardly in a position to meet Beijing's demands for national unification because to satisfy Beijing could alienate the majority of the Taiwan electorate and produce a smashing defeat in the next election. Although Beijing has attributed Taiwan's recent economic problems to Chen's failure to improve cross-strait relations, many Taiwan's workers have blamed Taiwan's businessmen investing on the mainland for Taiwan's increasing unemployment rate and other economic problems. It is far from clear that Taiwan's electoral politics will necessarily and neatly transfer economic interests of the business community into votes. For a variety of reasons, it is quite possible to imagine a sustained disjunction between the economic interests of Taiwan's businessmen and a large percentages of other members of Taiwan's population—workers, retired people, bureaucrats, to say nothing of DPP rank and file. Beijing may not understand or simply does not want to understand this dynamics. In particular, Beijing has constantly underestimated the sentiment against the communist regime in Beijing and the enduring support for the DPP in Taiwan.

In this case, it could be an illusion that if Taiwan's opposition leaders have come to the Chinese capital and economic independence has been sustained, war is unlikely. Taiwan and the mainland have not eased political tensions despite the increase in economic interdependence. If the recent history of Beijing's two pronged strategy of military coercion and peaceful offense can tell us anything, it is the recurrence of military crisis after the failure of peaceful offense. Beijing may become disappointed again after a period of wait-and-see. No Chinese leader could afford to see the loss of Taiwan during his watch. Jiang Zemin does not want to see a war across the strait, but if forced by the situation, he cannot shrink from sacrificing China's modernization plan. The rise of Chinese nationalism in recent years has further tied the hands of Chinese leaders. The patriotic education sponsored by the communist state in the 1990s placed emphasized on China's territorial integrity and national reunification. The high tide of protest that broke out over the U.S. accidental bombing of the Chinese Embassy in Yugoslavia was an expression of this patriotic sentiment. Taking action to reunify with Taiwan plays a special role in maintaining the nationalist credentials of the communist regime. Thus, the disappointment over the peaceful offense would guarantee a return to the emphasis on military coercion, which would start another very dangerous cycle of peaceful offense and military coercion. When Beijing has exhausted its strategic options in the cycle, it may be left without an option but to use military force for a real war across the Taiwan Strait. To prevent this worst-case scenario from taking place, a formal, negotiated, and enduring framework for cross-
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strait relations has to be established. The first step is to resume the dialogue across the strait between the semi-official agencies and eventually launch formal negotiations between the two governments on equal footing to end hostility.

NOTES

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Relations between the United States and the Republic of China on Taiwan: Retrospect and Prospects*

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Ladies and gentlemen: It's both an honor and a pleasure to be invited to deliver the keynote address today for the Sigur Center Conference "Assessing President Chen Shui-bian's First Year." You have arranged an impressive line-up of panel participants from both the United States and Taiwan, and this is bound to be a useful examination of developments during President Chen's first year in office. Taiwan’s rapid democratic transformation and wide-ranging social reforms have continued unabated over the past twelve months. It is an exciting and pivotal moment in our history, and we welcome your analytical perspective.

It is altogether appropriate that this conference is held under the auspices of the Sigur Center here at the George Washington University. The late Dr. Sigur was a longtime friend of Taiwan, and he was devoted to the cause of democracy and security throughout East Asia and the Pacific. He would have relished the opportunity to discuss the great strides made by the people on Taiwan and the future of their partnership with the United States. I knew Dr. Sigur well and respected his commitment not only to international relations but also to public service and scholarship. In fact, Dr. Sigur expressed his personal philosophy of life in the following way: I have approached life as a student, believing that learning as much as possible during the span allotted each individual in this world is at the heart of mankind's existence. It is through the continuing learning process that one is able to realize one's true potential and can best discover how better to serve one's fellow man.

I think this statement encapsulates so well Dr. Sigur's outlook on life and explains precisely why we engage here today in this academic exercise—both to learn and to discover the means of improving society and assisting in its advancement.

Today, I am going to offer a few observations, thoughts, and ideas regarding the relationship between the Republic of China on Taiwan and the United States in retrospect and its prospects for the future.

In Retrospect

First, in retrospect, the relationship between Taiwan and the United States has a long history. There have been numerous ups and downs, twists and turns. We still remember how in 1949 the United States almost gave up on the Republic of China. Then in 1950, the Korean War broke out and we moved to form a more lasting alliance. During the Cold War, Taiwan and the United States worked closely together to contain Communism in Asia. Then, in 1972, Nixon’s trip

* This talk was originally presented as the luncheon keynote speech at the conference.
to Beijing and the subsequent Shanghai Communiqué started a set of more complicated developments in the bilateral relationship. Diplomatic relations between Taiwan and the United States lasted until the first day of 1979, when the Carter administration switched recognition from Taipei to Beijing. That year, the U.S. Congress responded by passing the Taiwan Relations Act to reaffirm the close and friendly ties between our two countries. In 1982, the United States, under tremendous pressure from the PRC, signed the August 17 Communiqué with the PRC on U.S. military sales to Taiwan. At the same time, the U.S. provided us with the “six assurances,” which among other things promised Taiwan that the U.S. would never seek to serve as a mediator between the two sides.

Perhaps one of the most clear cut examples of the twists and turns in the Taiwan-U.S. relationship involves the sale of military items. In 1980, F-5Gs were considered an offensive weapon, but by 1992, the United States had decided to sell Taiwan F-16s for “defensive purposes.” I’d like to emphasize that U.S. influence and assistance was one of the major factors that allowed the people of the ROC on Taiwan to reach their current stage of economic and political development. And yet, the United States had to sever diplomatic ties with us. As a result, we have a unique and almost unprecedented bilateral relationship: two countries that are very friendly with each other and mutually supportive but which cannot conduct relations as they would prefer in the normal diplomatic way.

What conclusions can we draw from this brief review? Maybe nothing unusual. But tentative conclusions can serve as a helpful reference when we analyze the relationship between Taiwan and the United States. First, it is obvious that the U.S.-Taiwan relationship is not a simple bilateral relationship. Rather, it is influenced by regional, international, and global forces. It is also influenced by other sets of bilateral relationships, including the one between Taipei and Beijing as well as the one between Washington and Beijing. And, it is also subject to domestic developments in Taiwan, mainland China, and the United States.

Second, national interests are the primary consideration that determines policy. Now there are basically two kinds of interests: visible and invisible or, if you prefer, tangible and intangible. Tangible interests include such things as trade, investment, security, education, culture, science, and technology. Intangible interests include values and ideals, ideologies, and concepts such as freedom, democracy, and human rights.

Third, national interests can and do change or shift according to modifications in the objective environment and subjective conditions, depending on different perceptions, understandings, and interpretations. And national interests are often defined in relative and comparative terms.

Fourth, the relationship between Taiwan and the United States is so complex, so sensitive, and so important, yet there have always been efforts to stabilize, institutionalize, and otherwise improve it. This is most clearly reflected in the language of the Taiwan Relations Act, the Six Assurances, and the 1994 Taiwan Policy Review. It is also reflected in the three communiqués between the United States and the PRC.

To give you an idea of the breadth and depth of our relationship as it stands today, let me cite a few examples. Bilateral trade between the United States and Taiwan topped $64.8 billion last year. Taiwan was the United States’ seventh largest export market and seventh largest source of imports. You may not know that, over the last ten years, Taiwan has bought an average of 60 percent more from the United States than has mainland China. Last year, nearly 30,000 students from Taiwan were enrolled in a U.S. university or college. To date, we have signed at
least 134 formal agreements regarding cooperation in areas such as trade and investment, education, culture, science and technology, transportation, agriculture, environmental protection, and many other fields. Major airlines operate over 270 flights per week between Taiwan and the U.S., and the United States is the number one destination for travelers from Taiwan outside of Asia. Of course, there have also been close security ties between Taiwan and the United States.

But while our two countries have a great relationship, we still cannot do a number of things. The fact that we do not have diplomatic ties limits our access to each other and thus affects adversely the normal development of the relationship.

At Present
Having looked back and viewed Taiwan-U.S. ties in retrospect, let us now take a look at the relationship since President Chen’s election last year. Before that election, President Lee Teng-hui’s unanticipated “special state-to-state” formulation had already had quite an impact on bilateral relations. Then, the subsequent election of Chen Shui-bian, whose own party had advocated independence for Taiwan, further roiled the waters and led to tensions between Taiwan and the United States. Doubts were raised. People grew anxious and suspicious. But, President Chen quickly changed that by communicating effectively with the United States and publicly expressing his goodwill and sincerity towards the People’s Republic of China. His inaugural address and other remarks have alleviated these suspicions, maintained peace and stability in the Taiwan Strait, and established mutual trust between the United States and Taiwan. While the PRC still distrusts President Chen and his administration, the PRC has been very discreet so as not to disturb the status quo.

Basically, we believe U.S. policy toward the two sides of the Taiwan Straits has been formed in the last few decades by both major political parties with the participation of the U.S. Congress, the media, scholars, and, of course, administration officials. The policy has stability and continuity. So long as there are no major disruptions in the international community or in the U.S., mainland China, or Taiwan, we do not expect any major policy changes under the Bush administration.

Of course, different people and different parties may have different attitudes and approaches, perspectives and perceptions. You can see that from some of the statements made by President Bush and members of his administration. Last month, for instance, President Bush told ABC that he would do, quote, “whatever it took to help Taiwan defend herself.” You should not over interpret President Bush’s comment, but you can sense that his administration is very concerned about Taiwan’s security and peace in the Taiwan Strait. Secretary of State Colin Powell said, and I am paraphrasing, “If we weaken relationships with allies and friends, we weaken ourselves.” Other high officials in the Bush administration have also expressed their views by stating, “Taiwan is not trouble-maker. It is an opportunity.” This shows that the Bush administration has a positive and upbeat approach towards Taiwan’s security and Taiwan itself. Since President Bush’s inauguration, this approach has been evident in the U.S. decision on arms sales, the statement made by U.S. Secretary of Health Tommy Thompson supporting our participation in the World Health Organization, the U.S. decision to grant a visa to former president Lee Teng-hui, who is going to visit his alma mater soon, and the handling of President Chen’s transits in the United States.

We appreciate this positive approach and attitude. We believe it is an improvement, and we believe that such improvements are motivated by a desire to make the U.S. relationship with
To make Taiwan more reasonable, realistic, responsible, and reliable. This is good not only for Taipei-Washington relations but also for cross-strait relations and the Taipei-Washington-Beijing triangle because it provides more certainty and predictability. The improvements are definitely and absolutely not aimed at any third party. They merely reflect an acceptance and recognition of existing reality.

Prospects for the future
Now, let me turn to the future. Speaking for my government and for myself, I can say we are quite optimistic about the prospects for future partnership between Taiwan and the United States. Yes, there are so many uncertain elements existing in Taiwan, the mainland China, in the United States, and in this fast changing world. Like all international relations, ours should naturally evolve over time to stay abreast of changing circumstances domestically, and those in the surrounding context. In my estimation, future U.S.-Taiwan friendship and cooperation can or has to be defined by at least four fundamental features: Realism, Clarity, Maturity, and Mutuality.

1. Realism: For much of the past quarter-century, an element of artificiality has over-shadowed the bilateral relationship as both sides sought to cope with Cold War strategic considerations and external pressures. Implicitly and explicitly, Washington and Taipei agreed to circumvent sensitive areas through informal and contrived mechanisms and channels. I think both of us have gradually moved beyond that, accepting the fact that our common values and shared interests now justify certain fresh approaches to interaction that comport with reality. As those values and interests have become clearer over time, all of us have become “realists” to a greater degree. We recognize that “wishful thinking” will not promote democracy or guarantee regional stability.

2. Clarity: In close connection with the element of realism is the necessity of clarity; that is, we no longer feel obliged to wrap all our policies and principles in the cloak of ambiguity and nuance. I think experience has taught all of us that ambiguity is needed only when it does not cause confusion or invite misunderstandings that may in fact lead to instability and miscalculation. Honesty, trust, and commitment in any relationship necessarily require straightforward approaches. Clarity in U.S. policy also boosts our people’s psychological confidence, helping lay the groundwork for future talks across the Taiwan Strait.

3. Maturity: I think we can characterize the introduction of Realism and Clarity as symptoms of a welcome and necessary maturing of relations between the United States and Taiwan. After nearly 25 years of successful and productive cooperation under the Taiwan Relations Act, we have advanced to a point where we understand each other well enough to move to a new level of mutual confidence. This means, of course, that the relationship is on steady ground, and far less likely to be disrupted by occasional differences. Maturity is reflected in the fact that high level ROC officials can now transit U.S. territory without facing awkward and unreasonable obstacles.

4. Mutuality: This bilateral relationship has changed so much from the days when Taiwan had to rely almost wholly on the assistance of the United States. It is no longer a “one way street” by any means, but a normal conduit of mutual benefit and reciprocity. In the new age of the globalized economy, proliferation of information technology, and worldwide
democratization, our two peoples are going to find increasing opportunities to be mutually helpful and supportive of each other. Of course the United States will always be the larger and stronger partner, but I believe our relationship is acquiring a more natural balance of value and respect.

Based on these features and with a certain touch of idealism: I hope and believe there will continue to be improvements, or at least positive adjustments, in the conduct of relations between Taiwan and the United States.

I hope and believe the United States will continue to be interested in and concerned about the security of Taiwan and the peace and stability in the region.

I hope and believe the United States will continue to assist, or at least try to assist, Taiwan’s efforts to participate and play a more positive role in the international community, including certain international organizations.

I hope and believe that the United States can play a more active role as a stabilizer, and balancer to facilitate peace, including the resumption of dialogue across the Taiwan Strait.

I hope and believe that all parties concerned will be able to identify their common interests and will sooner or later work together to promote those common interests instead of dwelling on wasteful rhetorical exercises.

I certainly hope that one day the resources we now use to purchase weapons can be used for other peaceful purposes. This last weekend, I drove to Old Town Alexandria and saw how they had converted an old torpedo factory into an art gallery. What a wonderful example of beating swords into plowshares!

**Conclusion**

We consider our relationship with the United States to be paramount, not just because the United States is a global superpower, but because of the wide array of common interests and values shared by our two nations. There is no doubt at all that this will remain a complex relationship influenced by various extraneous circumstances, many of them beyond our control. But, it is also clear that extensive common interests shared by both countries will continue to grow over time. Given the comprehensive freedom and democracy, and the pro-active agendas shared by both our countries, together with the legacy of our long and friendly cooperation, I am very optimistic about prospects for the future.
Conference Summary

"Assessing Chen Shui-bian’s First Year: The Domestic and International Agenda"

Harry Harding

Throughout our discussions today, I was reminded of conferences on Hong Kong that were held in the first year after the transition to Chinese sovereignty. Before July 1, 1997, discussions of Hong Kong’s future had focused almost exclusively on what the new government’s relationship with Beijing would be.

And yet, that issue proved to be of far less immediate significance than originally anticipated. Instead, two other issues seemed of greater importance. The first was the severe impact of the Asian financial crisis on Hong Kong’s economy, and whether the crisis revealed deeper structural problems affecting Hong Kong’s economic future. The second concerned the flaws in the constitutional structure of Hong Kong: the uncertain relationships among an unelected chief executive without a political party, an elected legislature with representatives from organized political parties, and a professional civil service without accountability to the legislature.

There are obviously many differences between Hong Kong then and Taiwan now. But I am struck by the similarities. For much of the past year since Chen Shui-bian’s election, we have been asking whether there would be a crisis in cross-strait relations, given that Chen represented the political party that had historically stood for independence, and given that Beijing had threatened the use of force if Taiwan refused to negotiate unification. And yet, as Alan Wachman put it earlier today, this has been in many ways a “remarkably unremarkable year.” Tensions in the Taiwan Strait are in many ways lower than expected, and economic and cultural ties between Taiwan and the mainland continue to grow. Instead, our attention has been attracted by some unexpected domestic developments, similar in some ways to those that occurred in Hong Kong in 1997-98.

First, as in Hong Kong, there has been a significant downturn in the Taiwanese economy. This is the result less of financial problems in Asia, as it was for Hong Kong, than of a slowdown in the high-tech sector in the U.S. But in Taiwan as in Hong Kong, people seem uncertain about whether this is simply a cyclical phenomenon or whether it reflects deeper structural problems. Since 1997, Hong Kong has been debating whether or not it can continue to serve as an entrepot and financial center for the mainland, or whether it would have to find some newer comparative advantage. Similarly, we heard [at the conference] that Taiwan would have to make its “second structural transformation,” moving from any lingering commitment to labor-intensive manufacturing and toward becoming

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This summary was originally presented as the dinner speech at the conclusion of the conference.
a “green silicon island.” But we also heard about some of the obstacles to achieving this vision: the weaknesses in the banking and financial sectors, and the paradoxical problem that what was once seen as Taiwan’s great economic strength—its small- and medium-sized enterprises—may now be one of its shortcomings.

I wish we had had further discussion of this issue. How widely shared is the view that Taiwan should become a “green silicon island”? Does this vision replace—or supplement—the previous vision of Taiwan as an Asia-Pacific regional operations center? How serious are the obstacles to achieving this vision, and how readily can they be overcome? And, above all, how does China relate to this vision? As a partner, a competitor, or what?

Second, as in Hong Kong, the contradictions in Taiwan’s constitutional system have become apparent with the transition of power. The sharing of power between the executive and legislative yuan, the asynchronous elections to the two bodies, and the fact that different parties presently hold power in the two yuan, has led to what some of us earlier today described as “gridlock.”

And yet, there does not seem to be the same degree of demand for constitutional or at institutional reform on Taiwan as there is in Hong Kong. Our discussion led to the prediction that the Legislative Yuan elections this year will narrow the gap between the legislature and the executive, by ending the KMT’s majority in the Legislative Yuan and by making possible some kind of coalition government centered on the DPP.

But is this prediction overly optimistic? Will Taiwan’s present political deadlock indeed be resolved by the further workings of the electoral cycle? Or will Taiwan need some kind of structural political reform? And, if so, what kinds of reforms will be necessary? We’ll have to wait for the outcome of the elections to see.

Although cross-strait relations therefore did not dominate our discussions as much as might have been anticipated, there was still much to talk about—and still ample reason for concern.

To be sure, there are grounds for much relief, at least in the short run. The worst case scenarios that were presented on the eve of Chen Shui-bian’s inauguration—a provocative stance by Chen, a militant reaction by Beijing—have not occurred. Instead, all parties have acted with admirable restraint:

- Chen included what are now called the “original five nos” in his inaugural address, basically foreshewing a unilateral declaration of independence and keeping some elements of KMT’s previous “one-China policy” in place.

- Although Chen has not been willing to commit to reunification (and thus has found it difficult if not impossible to reaffirm the so-called 1992 consensus on the “one-China principle”), he has now introduced the intriguing idea of working toward the political integration of Taiwan and the mainland. (Ironically, if the European Union is in any way the model in Chen’s thinking, as some of his advisers suggest, it could ultimately provide for a far more powerful central Chinese government, with far more authority over Taiwan, than under Beijing’s “one-country, two systems” formula.)

- Chen also seems more willing to move more rapidly than his predecessor toward economic integration with the mainland, although his government remains concerned about issues of national security. The fascinating question here is whether Taiwan’s alleged dependence on the mainland is the result of having opened up too much, or too little. Would
Taiwan not become less dependent on the mainland if the PRC had more investment in Taiwan, and if mainland exports flowed in significant volumes to the island? Moreover, if both Taiwan and the mainland enter into the WTO, will restricting cross-strait commercial ties be a viable option for either party?

- For its part, although Beijing has not chosen to work with Chen, nor has it taken an overtly hostile approach toward Taiwan. Instead, it is pursuing “united front” tactics toward both the opposition parties and the business community, clearly hoping either that Chen will have only one term in office, or that he will be forced by powerful domestic constituents to modify his stance toward Beijing.

- Moreover, although still stated in vague terms and somewhat unofficial ways, China has largely moved away from its insistence on the “one-country, two-systems” formula to the more flexible concept of “one-country, whose form is yet to be determined.”

- Although the new Bush Administration in the U.S. seems more sympathetic to Taiwan than the Clinton Administration, the overall framework for American relations with Taiwan still remains the “one China” policy. The U.S. carefully avoided selling Taiwan the one weapon system (the Aegis-equipped Perry-class destroyers) that Beijing had clearly identified as being beyond its “red line,” and the White House denied that the President’s impromptu televised remarks about “doing whatever it takes” to defend Taiwan reflected any change in policy.

- Despite the signs of flexibility on both sides, neither has persuaded the other of its sincerity. Both seem to be hoping for more. Taiwan is hoping that China will agree to negotiations without political preconditions. Beijing is hoping that Chen Shui-bian, or his successor, will accept the one-China principle. And yet each side’s ability to be more flexible is constrained by domestic politics—both societal and factional.

- The framework for U.S.-China relations is slowly unraveling. In order to justify the largest arms sale to Taiwan since 1992, the Bush Administration revealed the so-called “Reagan Codicil” to the August 1982 communiqué on U.S. arms sales to Taiwan, which in Chinese eyes may make that document a dead letter.” Some in Congress want to declare Taiwan to be a “non-NATO ally,” and both Congress and the executive branch seem committed to increasing the level of military interaction and cooperation between the U.S. and Taiwan. Those developments could make the December 1978 communiqué on the normalization of diplomatic relations and the termination of the mutual defense treaty between the U.S. and Taiwan a dead letter as well. And, of course, given changes in political leadership and public opinion on Taiwan, a key premise of the Shanghai Communiqué of February 1972, also seems to be in doubt: the statement that “all Chinese on either side of the Taiwan Strait maintain there is but one China and that Taiwan is a part of China.”

- At the same time as these key documents are being challenged, the Clinton Administration’s conceptual framework for the U.S.-China relationship—building toward a “constructive strategic
beneficial economic and social ties, and lay the groundwork for an eventual resolution of differences, on terms yet to be determined.

Specifically:

- Each party must avoid both provocations of its own and overreaction to the provocations of others.

- Taiwan and China need to provide each other with negative reassurances. They should formalize a conditional renunciation of force by China in exchange for a conditional renunciation of independence by Taiwan. On that basis, they can also work to restrain the military build-up that is already underway.

- These negative reassurances must be matched by positive reassurances. Taiwan should explicitly keep open, as a preferred option, the possibility of political unification or integration with the mainland, if the appropriate preconditions can be met. The mainland should be more flexible about the formulas it has in mind and the procedures for getting there. These possibilities should be explored through Track II channels, if official Track I dialogue is not yet possible.

- China must understand that the key is to persuade Taiwan of the benefits of a political solution, not the costs of failing to achieve one. This requires Beijing to find not only more flexible terms for unification, but also ways of treating Taiwan as an equal partner in dialogue.

- Both sides should keep expanding their trade and cultural links. It is understandable that Taiwan would be concerned about issues of security, but it also should see the political and economic benefits of economic interdependence.
• The U.S. should stick to its existing policy framework regarding Taiwan: welcome a peaceful resolution acceptable to both sides, oppose unilateral acts by either part, support an expansion of dialogue, and promote an enhancement of Taiwan’s unofficial relations, both bilaterally and multilaterally, with the rest of the world. While the details of policy can and should evolve, maintaining a consistent framework, against the importunings of either side, is important.

• The U.S. should also continue to work toward a cooperative relationship with China. Cross-strait relations are not necessarily zero-sum, but it will be difficult to preserve a positive-sum relationship if the U.S. and China are committed to strategic competition. Taiwan will almost inevitably become a pawn in that competition.

The effort to promote these kinds of interim arrangements will be difficult, and may even fail. But given the risks, it is worth the effort. And the fact that, remarkably, this has been an unremarkable year gives some hope it will succeed.

NOTES

"These include: no declaration of independence (unless Taiwan were attacked by the mainland), no revision of the constitution to include Lee Teng-hui’s “two-states theory,” no referendum on independence, no revision of the National Unification Guidelines, and no change of the name of the Republic of China.

The text of the August 1982 communiqué provided that the U.S. would gradually reduce the quantity of arms sold to Taiwan, and would not exceed the level of quality sold at the time of normalization; the previously secret “Reagan Codicil,” in contrast, linked the level of U.S. arms sales to the “threat posed by the PRC ... [such that] Taiwan’s defense capability relative to the PRC will be maintained.” Robert G. Kaiser, “What We Said, What They Said, What’s Unsaid,” Washington Post, April 15, 2001.
The effort to promote these kinds of interests will not be difficult, and may even fail. How much more difficult it is to maintain and combat the interest of the U.S. in Taiwan, especially at the cost of maintaining the reputation of the U.S. in the eyes of the world. In Asia, our reputation is important.

NOTE

The U.S. should also continue to work towards a cooperative relationship with China. Cross-straits relations are important. If the U.S. and China can resolve the issues of cross-straits relations, a stable relationship is possible.

The U.S. should also continue to support the government's efforts in Taiwan. The government of Taiwan must be aware of its responsibilities and obligations.