

POLICY BRIEFING

# Taiwan

## The risk of marginalisation

### *Economic situation and trade relations with the EU*

#### **Abstract**

Taiwan, a member of the exclusive group of advanced Asian economies, increasingly faces the challenges typical of many post-industrial societies: growing inequality, an ageing population and competitive pressures from emerging economies.

The island's diplomatic status created additional challenges for Taiwan's export-oriented economy. The explosion of preferential trade agreements (PTAs) as a result of the deadlock of the Doha Round of negotiations at the World Trade Organisation has left Taiwan virtually excluded from the PTA process. To prevent its trade partners from turning elsewhere, Taipei pursues an active and 'flexible' commercial diplomacy. The means participating in plurilateral initiatives (such as the Trade in Services Agreement within the World Trade Organisation), normalising relations with the People's Republic of China and working on bilateral agreements.

Taipei has recently concluded economic cooperation agreements with two countries with which the island does not have diplomatic relations: New Zealand and Singapore. These accords have offered Taiwan hope that it may also eventually join more ambitious trade agreements, such as the Trans-Pacific Partnership. While this sort of adherence is possible under the WTO framework Taipei will also have to make concessions and earn the acceptance of the other parties.

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## Introduction: Taiwan's status as a commercial entity<sup>1</sup>

Although most countries do not have diplomatic relations with Taiwan, they trade with it as with a distinct entity and perceive it as a reliable and attractive partner.

All but 23 small countries of the world adhere to a 'one-China policy' and do not recognise Taiwan<sup>2</sup> as a sovereign state. Yet this has not prevented most countries from considering Taiwan an important and reliable commercial partner and treating the island as a distinctive jurisdiction in terms of economic cooperation, trade and investment. This autonomy was confirmed when Taiwan joined the World Trade Organisation (WTO) as the 'Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu' (or 'Chinese Taipei', in short) in 2002.

The accession of Chinese Taipei to the WTO was made possible because the WTO is not an association of States but is composed of independent custom entities. Article XXXIII of GATT 1947 stipulates that:

'A government not party to this Agreement, or a government acting on behalf of a separate customs territory possessing full autonomy in the conduct of its external commercial relations and of the other matters provided for in this Agreement, may accede to this Agreement, on its own behalf or on behalf of that territory, on terms to be agreed between such government and the CONTRACTING PARTIES<sup>3</sup>.'

Taiwan consequently enjoys the same rights as China, Hong Kong and Macao in the world of trading system. Taipei's accession to the WTO was, however, different from that of the two Chinese Special Administrative Regions, both of which had participated in the General Agreement on Trade and Tariffs (GATT) before the WTO was established<sup>4</sup>. Because of the sovereignty claims of the People's Republic of China (PRC) over Taiwan, China insisted that Taiwan join the WTO only after China was admitted. Indeed, most GATT contracting parties shared that view. In the end, the WTO Ministerial Conference approved Taiwan's accession less than one day after it had taken a decision on China's accession.

Article XXIV of GATT allows members of the WTO to conclude preferential trade agreements. This right has been increasingly used by Taiwan's competitors to compensate for the lack of progress in the WTO's Doha round of multilateral trade talks. Taiwan, on the other hand, has largely

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<sup>1</sup> For background, see [Policy Briefing Economic and Trade Relations with Taiwan](#), EP Policy Department DG External Policies, 2011.

<sup>2</sup> Taiwan is the informal name of the entity comprising Taiwan, the archipelagos of Penghu, Kinmen and Matsu, and some small close islands. Republic of China (ROC) is the name with which it refers to itself, inherited from the Republic founded in 1912, comprising today's 'mainland China' (People's Republic of China). Whilst ROC exercises *de facto* sovereignty over the above territory, China has maintained its sovereignty claim over Taiwan since 1949.

<sup>3</sup> [...] See interpretation of GATT article XXXIII with relation to Chinese Taipei, [http://www.wto.org/english/res\\_e/booksp\\_e/gatt\\_ai\\_e/art33\\_e.pdf](http://www.wto.org/english/res_e/booksp_e/gatt_ai_e/art33_e.pdf)

<sup>4</sup> See Chien Huei Wu, [WTO and the Greater China](#), Martinus Nijhoff Publishers, 2009.

refrained from concluding such agreements, primarily due to China's position that FTAs can only be concluded among sovereign states.

Yet Beijing has not opposed Taipei's trade accords with New Zealand and Singapore<sup>5</sup>. This is presumably because both countries also have free trade agreements (FTAs) with Beijing in place, although it is not clear whether and to what extent the three countries coordinated their agreements with Beijing. The resulting FTA-like accords demonstrate that Taiwan can conclude trade accords despite its lack of diplomatic relations – a fairly recent development.

For the most part, there are no trade agreements between Taiwan and countries that do not have an FTA with China. The exceptions are the five Latin American states which recognise Taiwan diplomatically. However, Taiwan is currently studying the feasibility of potential trade (economic cooperation) agreements with Israel, India, the Philippines and Indonesia, none of which has a bilateral FTA with China. (An FTA does exist, however, between China and the Association of South-East Asian Nations – or ASEAN – whose members include Indonesia and the Philippines.)

From Taiwan's point of view, the landmark Economic Cooperation Framework Agreement (ECFA) concluded with China on 29 June 2010, as well as other economic accords with Beijing, served as further proof of Taiwan's distinct administrative jurisdiction and a signal that Beijing is becoming more accommodating on Taipei's trade deals with other countries. From Beijing's perspective, the ECFA was a step forward in the *'irresistible historical process'* leading to *'complete reunification of China'*<sup>6</sup>.

The normalisation of relations across the Taiwan Strait has reassured the international community, but trade negotiations usually take place at a very slow pace. Besides bilateral trade agreements, Taiwan has also expressed interest in participating in regional trade agreements such as the Transpacific Partnership.

## 1. Recent economic performance

Like other advanced Asian economies, Taiwan faces growing inequality, an aging population, competition from neighbours with lower production costs, and scarcity of resources.

After a phase of rapid development from an agrarian to an industrial economy, Taiwan entered the post-industrial phase, requiring social and economic adjustments. Taiwan now belongs to the exclusive group of five advanced Asian economies, along with Japan, South Korea, Singapore and Hong Kong.

Between 1952 and 1980, Taiwan's economy grew at an average rate of 9%, then gradually slowed to a more sustainable pace. Despite the heavy recession of 2009, the islands' growth remained high for an advanced

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<sup>5</sup> China does not oppose economic dialogues of Taiwan 'as long as this does not contravene one China principle'. [South Atlantic News Agency](#), 29 August 2013

<sup>6</sup> [Hu Jintao's report at 18th Party Congress](#).

Taiwan is one of the most trade-dependent economies in the world. The island's exports are equivalent to around 66 % of its GDP (compared to 14 % in Japan or 50 % in South Korea).

economy: on average, 4.1 % between 2000 and 2010.

In 2011, Taiwan's GDP growth was 4.06 % and economists forecast 4 % and 5 % for 2012. Yet growth dropped to 1.26 %. This was largely due to global developments, which included the persistent crisis in the euro area, the uneven recovery of the US economy and China's slowing growth.

For 2013, economists have forecast a growth of 2.4 %-3.6 % in Taiwan, largely because of improved outlook for the US economy, China's growth, and expanding trade with Southeast Asia.

**Table 1:**  
GDP and GDP per capita of five advanced Asian economies

	GDP current prices (in USD billion)	GDP per capita (in USD)
Hong Kong	248.7	34 970
Japan	5 897.0	46 108
Singapore	265.6	50 000
South Korea	1 116.2	22 424
Taiwan	464.0	19 980

Source: IMF, 2011

These fluctuations are not surprising. Taiwan is one of the most trade-dependent economies in the world, and the value of its exports represents 66% of GDP (compared to 14% in Japan and 50% in South Korea). Taipei is also dependent on global raw material prices because its own resources are scarce. While Taiwan's occupies the 51st place in world in terms of population it is the 12th largest exporter, and 12th largest importer of goods<sup>7</sup>.

Overall, Taiwan's macroeconomic indicators are comparable to those of the other three East Asian 'tiger economies', i.e., Singapore, Hong Kong and South Korea. Its public debt is slightly above 40 % of the country's GDP and is on the rise, though still much lower than the one of most of industrialised countries and notably Japan (211%) which shares with Taipei a similar development path. As exports continue to be the driver of Taiwanese economy, and its companies continue to invest abroad, the island's current account maintains a high surplus (10.45% of GDP) – higher than in any other advanced Asian economy except Singapore.

### Structure of economy

The contribution of various sectors to GDP in Taiwan resembles the economic structure of most advanced economies. The services sector represents the major part of value added (68%), followed by industry

<sup>7</sup> If the EU is considered as a single entity. Otherwise, the 17th and the 18th respectively. [WTO profile](#), 2011.

(30%) and a small – though powerful and well-protected – farming sector (2%)<sup>8</sup>.

**Table 2:**

Taiwan's top-10 sectors ranked by value added

	2012 Level (Bil. US\$)	2013 Percent Change (Real terms)	Percent Share of GDP (Nominal terms)
1. Wholesale Trade	54.3	2.8	11.8
2. Real Estate	41.2	2.5	8.9
3. Retail Trade - Total	36.5	2.4	7.9
4. Public Admin. and Defense	35.0	1.6	7.6
5. Semiconductors, CBs, and LCDs	29.9	7.4	6.5
6. Education	22.4	1.4	4.9
7. Banking and Related Financial	20.2	2.9	4.4
8. Sanitation, Trade Organizations	19.2	4.3	4.2
9. Health and Social Services	15.2	1.7	3.3
10. Construction	14.6	3.0	3.2
Top-10 Total	288.3		62.4

Source: World Industry Service, IHS Global Insight, Inc

### Challenges to the industrial sector

Due to its rapid industrialisation and smooth transition from an economy based on lower added value industries to one dominated by high-tech niches, Taiwan's industrial policy is considered an example of success. The island has succeeded in dominating the world market in a number of areas such as semiconductors, optical disks, portable navigation devices and display panels. According to Market Intelligence and Consulting Institute of Taiwan, 89 % of the world's laptop computers, as well as 46 % of desktop PCs are produced by Taiwan's firms in manufacturing bases abroad, mostly in the PRC where production costs are lower.

Taiwan became a global leader in customised ICT component, semiconductor and notebook production both through its economic policies and the flexibility of its industrial model. Taiwan does have its own brands, such as notebook producers Acer and ASUSTeK, but the industry has extensively relied on contract manufacturing for other firms – e.g., semiconductors or original design manufacturing (ODM). The availability of a relatively cheap workforce in China allowed Taiwanese firms like Hon Tai (better known as Foxconn, maker of iPhones and iPads and generally the world's largest contract manufacturer) to adapt quickly to changing tastes in the IT market, without having to invest in expensive mechanisation.

Yet this model, which proved efficient for about two decades, is today being challenged. The profit margins of Taiwanese-customised ICT manufacturers are shrinking as living standards in China rise and production costs increase. Additionally, the prominent notebook niche faces constant and problematic changes in market preferences. Finally,

Taiwan has succeeded in dominating global markets in niche sectors but its industrial model is facing new challenges. To face them the government encourages research and development in companies, as well as foreign investment.

<sup>8</sup> Executive Yuan, ROC (Taiwan)-The Republic of China Yearbook 2012

Despite Taiwan's integration into global production chains, the island is concerned about its growing disadvantages relative to its competitors. Virtually all of them participate in (or are negotiating) regional or bilateral free trade agreements that trade barriers and align rules and standards.

Taiwan has encountered increasing competition, including from indigenous companies in China and South East Asia.

At the domestic level, the government has responded by encouraging research and development in companies and investment (or re-investment) in Taiwan by overseas Taiwanese businesses. Government initiatives have offered incentives for Taiwanese investors to return home, for example, and developed new free economic pilot zones.

The private sector has sought various solutions as well, adapting to market tastes, creating its own brands and moving from production to services, such as telecommunications, retail or after-sales services (Hon Tai), data storage (computer makers Quanta and Inventec) and recycling, including by recovering precious metals from computers and smartphones (ODM firm Wistron). As production costs on the mainland grow, some production is also likely to return to Taiwan.

Domestic challenges include the need to adapt the Taiwanese education system to increase the island's innovation capacity, improving energy security (see 2011 briefing<sup>9</sup>), decreasing the waste of water resources, and consolidating the relatively inefficient banking sector, which comprises 38 Taiwanese banks, some of which are owned by government<sup>10</sup>.

## 2. Trade relations and recent developments in trade policy

### 2.1. Trade relations overview

In 2003, China outpaced the US as Taiwan's main trade partner, and by 2012, China absorbed almost 40 % of Taiwan's exports. Japan remains Taiwan's main source of imports.

Taiwan's major partners fall into three main categories: countries in west Asia region involved in energy-related trade; Asian countries that serve as partners in global supply chains; and developed countries such as Japan, the United States and the European Union (EU). In 2012, China was the most important export destination and accounted for 27.2 % of Taiwan's total export value – or 39.4 % if Hong Kong were included – followed by ASEAN 6 (18.8 %), the United States (11 %) and the EU (8.7 %). In terms of imports, Japan is Taiwan's leading source, providing 17.6 % of the total value of Taiwan's imports (20.9 % in 2010), followed by China (16.1 % when Hong Kong is included), the US (8.7 %), ASEAN 6 (11.7 %), and the Middle East (16 %). Trade South East Asia has increased steadily since 2000, and imports from Middle East have grown considerably over the past two years.

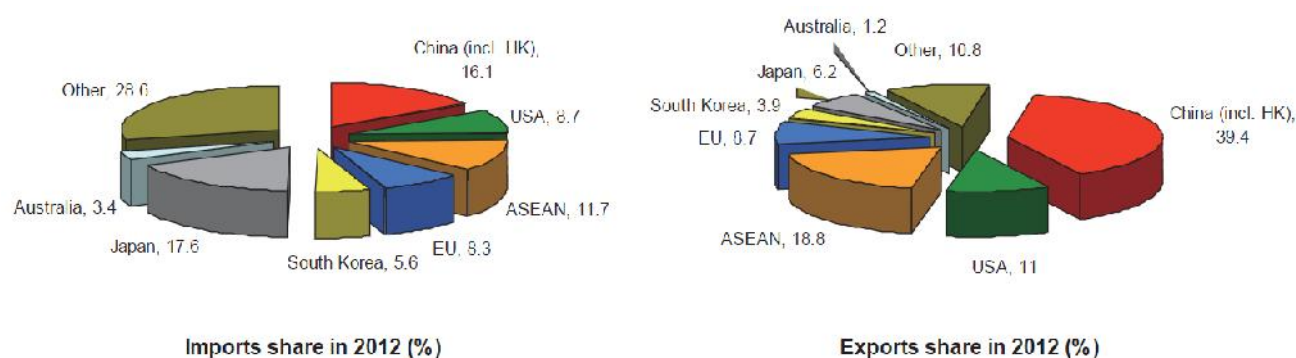
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<sup>9</sup> [Economic and Trade Relations with Taiwan](#), 2011, Policy Department. Accessible only from EP Intranet.

<sup>10</sup> Don Shapiro, *Taiwan Economy: Near term Upstick, Longer-term Challenges*, Brookings Institute, March 2013.



**Figure 1:**  
Share of Taiwan's imports  
and exports by partner



Source: European Economic and Trade Office, Taipei, 2012

Taiwan exports and imports mainly manufactured goods; these constitute 87.7 % of its total exports and 62.6 % of imports. Fuels and mineral products constitute almost a third of all imports (30.1 %) followed by farming products (5.5 %).

## 2.2. Taiwan's trade policy: recent developments

By mid-2013, Taiwan had concluded FTAs with the five Central American countries which recognise it diplomatically; these countries account for a total of 5 % of Taiwan's external trade<sup>11</sup>. Taipei has also concluded 19 agreements with China (including on non-trade issues) and finalised negotiations on two FTA-like economic cooperation agreements (ECAs) with New Zealand and Singapore. The island has also concluded and implemented a bilateral investment agreement with Japan, and is negotiating a similar accord with South Korea. Four other potential ECAs – with India, Indonesia, Israel and the Philippines – are under consideration. Yet this tally is very modest compared with others across Asia, where the number of FTAs concluded between January 2000 and April 2013 increased from 3 to 76, with more under development<sup>12</sup>.

The impasse of the World Trade Organisation's Doha Round negotiations and the subsequent proliferation of regional agreements have left Taiwan isolated from regional FTA networks. The government has therefore sought FTA with major trading partners.

For Taiwan's export-oriented economy and its limited political power, accession to the WTO provided the most favourable framework for dealing with trade issues. In the absence of progress in the organisation's Doha Round, Taipei has pursued its participation in plurilateral WTO processes, i.e. agreements among like-minded WTO members. It is member of the Government Procurement Agreement and participates in the 23-party talks on the Trade in Services Agreement (TISA). Given the high level of Taiwan's integration in global production networks, Taiwan generally benefits from regional integration processes, yet its current non-

<sup>11</sup> El Salvador, Honduras, Nicaragua, Panama, and Guatemala.

<sup>12</sup> Masahiro Kawai, Ganeshan Wignaraja. [Policy challenges posed by Asian FTAs](#), Asian Development Bank Institute.

participation in the boom of regional preferential agreements carries risks.

To avoid losing its current advantages, Taiwan is considering various options for joining regional networks. In 2010, it formulated its flexible approach to trade policy:

'To help Taiwan's economy expand in the future', the government announced, it would 'seek Free Trade Agreements (FTAs) with Taiwan's major trade partners' as 'one of the main aims of the flexible diplomacy policy'.

### **TPP and RCEP**

In 2012 the government of Taiwan indicated that the US, Singapore, New Zealand, Japan, EU, India and Indonesia were priority targets for ECAs, described as the 'lifeline' of Taiwan<sup>13</sup>. The President of Taiwan, Ma Ying-jeou, has also announced that Taiwan wishes to join Trans-Pacific Partnership (TPP) trade agreement within ten years<sup>14</sup>. Taiwan's agencies are studying the possibility of joining the Regional Comprehensive Economic Partnership (RCEP), which aims to create an FTA with ASEAN and the six partners with which ASEAN currently has FTAs – Australia, China, India, Japan, and New Zealand.

Taiwan's major trading partners are, in order of importance, China, Japan, the US, Southeast Asian countries, the EU and India (see table below). If Taiwan joined both the TPP and the RCEP, the island would enjoy preferential trade agreements (PTA) with all almost of these six except for the EU. If Taipei joined *either* the TPP *or* the RCEP, it would also benefit from PTAs with almost all of its major partners. The two agreements are very different in nature but not contradictory. The US-led TPP is probably the world's most ambitious trade agreement in its scope, which requires strong commitments and trade-offs from its members.

On the other hand, the RCEP will serve principally to minimise the complexities of the Asian FTA 'noodle bowl' – the tangled web of agreements that link the various countries – but there are concerns that the level of trade liberalisation in the RCEP will be very low. For Taiwan, both the TPP and the RCEP present advantages and challenges. Joining either would require the support of those already involved in these agreements, as well as strong commitments on Taiwan's side, including adapting domestic measures (e.g. standards, homologation issues).

Taiwan wishes to join the Trans-Pacific Partnership (TPP) trade agreement within ten years and has studied the potential benefits and disadvantages of adhering to the Regional Comprehensive Economic Partnership (RCEP)..

Taiwan's government agencies will be asked to prepare adjustment programs to gradually fulfil the conditions for joining the TPP.

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<sup>13</sup> [China Economic News Service](#), 5 July 2012.

<sup>14</sup> Negotiating parties are Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam. Japan engaged in full fledged talks at the 19<sup>th</sup> round, after having received support from all negotiating parties.

**Table 3:**

Taiwan's major trade partners and agreements in 2012

Country/region	% of total trade	Agreement	Remarks
China	21.9 %	18 various agreements, some in the ECFA framework	
Hong Kong	7 %		Hong Kong has proposed considering an agreement
Japan	11.2 %	Bilateral Investment Arrangement (BIA) September 2011	Includes investment protection, MFN, dispute settlement, positive lists
South Korea	5.2 %	Negotiations on bilateral investment protection agreement ongoing	
ASEAN 10	15.1 %		
○ Singapore	4.6 %	ECA negotiations upon finalisation	
○ Indonesia	2.2 %		Feasibility study on ECA
○ Philippines	2.1 %		Agreement to carry out a feasibility study
United States	9.5 %		TIFA (trade and investment framework agreement) – i.e. dialogue framework
India	5.2 %		Feasibility study on ECA
EU	8.3 %		Regular dialogues and consultations
New Zealand	2.3 %	ECA negotiations concluded July 2013	
El Salvador	5 % five countries together	FTA in force since 1 March 2008	Privilege diplomatic relations with Taipei rather than Beijing
Honduras		FTA in force since 15 July 2008	
Guatemala		FTA in force since 1 July 2006	
Panama		FTA in force since 1 January 2004	
Nicaragua		FTA in force since 1 January 2008	

Sources: MOEA, Council for Economic planning and development

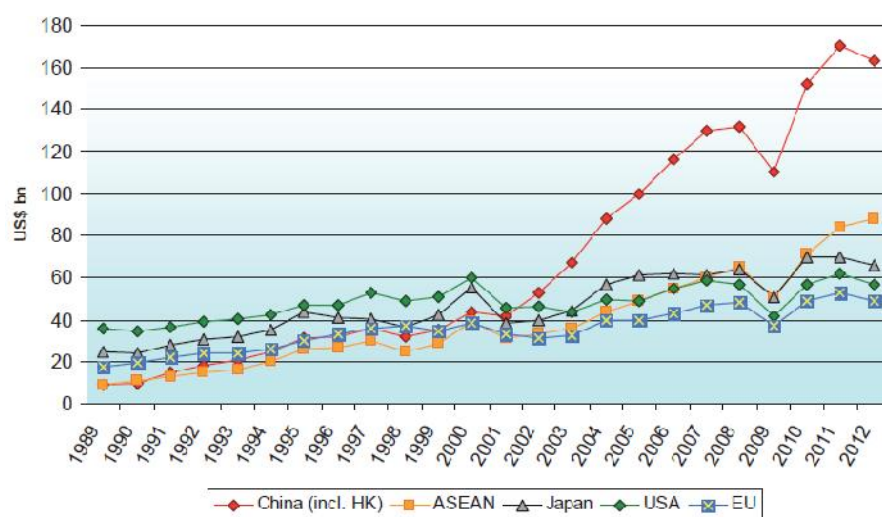
## 2.3. Relations with selected partners

### 2.3.1. Peoples' Republic of China

Taipei and Beijing are both fully fledged WTO members that hold WTO-incompatible restrictions against one another. Yet they refrain from challenging each other at the WTO, mainly because their challenges would raise sovereignty issues.

Between 1949 and the early 2000s, there was no direct trade or investment across the Taiwan Strait, as all commercial exchanges took place indirectly, mostly through Hong Kong. Even today, estimating the trade in goods between Taiwan and the PRC is complex, as official statistics do not reflect the substantial indirect trade<sup>15</sup>. Trade volumes started to grow in the late 1990s and accelerated after both the PRC and Taiwan joined the WTO. Currently, China is Taiwan's most important trade partner, and Taiwan is China's fourth-most important source of imports, after the EU, Japan and South Korea. Additionally, with more than 70 % of Taiwan's outward investment flowing to China, the island is the PRC's major source of foreign investments (apart from Hong Kong).

**Figure 2:**  
Taiwan's trade with China and other main partners



Source: EETO Factfile, 2012

The value of Taiwan's exports to China – USD 80.7 billion in 2012 – is approximately twice that of its imports from China –USD 40.9 billion that same year<sup>16</sup>.

Measures in both the PRC and the ROC are inconsistent with WTO rules. On China's side, they stem from Beijing's failure to recognise Taiwan's status as a full WTO member and from a number of unique non-tariff barriers. On Taiwan's side, barriers are more prominent and include restrictions in the merchandise trade that apply only to China. Nevertheless, neither side has filed a complaint at the WTO. China has refrained because such an action might imply a state-to-state relationship;

<sup>15</sup> See [The Implications of China-Taiwan Economic Liberalization](#), by Daniel H. Rosen and Zhi Wang, Peterson Institute for International Economics, 2011.

<sup>16</sup> [Taiwan's Bureau of Foreign Trade](#).

while Taiwan refrained for fear of losing the preferential treatment that Taiwanese enterprises enjoy in China<sup>17</sup>.

A short overview of bilateral investment relations can be found in the 2011 Policy Briefing<sup>18</sup>.

Taiwan's reasons for signing the ECFA included regularising its existing trade patterns, further liberalising trade/economic links and preventing the island from becoming marginalised by new FTAs in Asia.

Since Ma Ying-Jeou was first elected as President of Taiwan in May 2008, relations across the Strait have warmed, and Taipei and Beijing have concluded agreements to ease investment restrictions, as well as to establish direct air, postal and air links. On 29 June 2010, after negotiations that caused serious domestic controversies, the two signed the ECFA, which took effect on 12 September 2010. Taiwan's reasons for signing the ECFA included regularising the existing trade patterns, further liberalising trade/economic links and preventing the island from being marginalised by new Asian FTAs.

To circumvent any sovereignty issues, the ECFA was not signed between the governments but between specific agencies on the each side: the Association for Relations across the Taiwan Straits (ARATS) in the PRC, and the Straits Exchange Foundation (SEF) in Taiwan. Instead of establishing an outright FTA, the ECFA provided a legal basis for negotiating subsequent agreements and an 'early harvest list' specifying the goods that would benefit from tariff concessions. This proved the most suitable political solution to allow both sides to avoid the potential problems of an FTA or the sort of Comprehensive Economic Partnership Agreement (CEPA) that China has with Hong Kong. (For more information on the ECFA, see the 2011 Policy Briefing<sup>19</sup>.)

### **ECFA outcomes**

Cross-Strait economic relations were not immediately; or radically upended by the ECFA, in large part because a number of changes had already been implemented. Greater direct effects were expected later, in the medium term<sup>20</sup>. Yet the ECFA has considerably reassured Taiwan's other trade partners, leading – according to Taipei – multinationals to invest in Taiwan. On the other hand, those who oppose the agreement have argued that the cross-Strait accord has further isolated Taiwan and

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<sup>17</sup> See Pasha Hsieh, [The China-Taiwan ECFA, Geopolitical Dimensions and WTO Law](#), Singapore Management University, January 2011.

<sup>18</sup> [Economic and Trade Relations with Taiwan](#), EP DG EXPO Policy Department, 2011.

<sup>19</sup> [Economic and Trade Relations with Taiwan](#), EP DG EXPO Policy Department, 2011.

<sup>20</sup> E.g., Taiwan's CIER projected 1.66 % to 1.72 % GDP increase per year; PIIE estimated that Taiwan's economy will grow an added 4.5 % by 2020 but ASEAN economic integration processes would increase the effect to 5.3 %, <http://www.piie.com/publications/pb/pb10-16.pdf>

Economic cross-Strait relations have developed at an impressive pace, but the planned agreements have taken longer to sign than was expected.

made it too reliant on China's economy, thereby weakening Taipei's position vis-à-vis the mainland<sup>21</sup>.

Overall, since the rapprochement started in 2008, Taipei and Beijing have concluded 19 agreements – most of them economic – that have transformed bilateral business exchanges and altered political relations between Taipei and Beijing. However, the agreements within the ECFA framework have not progressed at the planned pace, and those that have been signed have yet to be properly implemented.

On 21 June 2013, SEF and ARATS signed the long-expected Agreement on Trade in Services. Like ECFA, the agreement was highly contested, and its implementation will be delayed – in this case because Taiwan's legislators have required a chapter-by-chapter approval. Their demand was largely prompted by the fact that there was little transparency in the negotiations, no consultations with stakeholders and no impact assessments. The Agreement on Trade in Services provides a 'positive list' which earmarks sectors to be liberalised, including business, communication, construction, the environmental, the health-related and tourism services.

### 2.3.2. New Zealand

On 10 July 2013 Taiwan and New Zealand signed the bilateral Agreement between New Zealand and the Separate Customs Territory of Taiwan, Penghu, Kinmen, and Matsu on Economic Cooperation (ANZTEC). Despite its relatively small economic significance, the agreement has a particular meaning for Taiwan. It is the first FTA-equivalent with a country that does not have diplomatic relations with Taipei. New Zealand is Taiwan's 40th largest trading partner, and Taiwan is New Zealand's 12<sup>th</sup>.

### 2.3.3. Singapore

Trade agreements with New Zealand and Singapore may be considered first steps towards integration into regional trade agreements and other bilateral trade accords.

On 17 May 2013, Taiwan and Singapore concluded technical discussions on their bilateral ECA. Taiwan's agreement with its sixth-largest trading partner covers – in addition to tariffs and trade in services – investment, e-commerce, public procurement and dispute settlement. When signed and ratified, the ECA will have a political value similar to that of the ECA with New Zealand.

Both agreements are regarded in Taiwan as a step towards a potential integration into the TPP and the RCEP, and as a sign that countries that have trade agreements with Beijing are increasingly ready to engage with Taipei. (In this vein, the fact that Switzerland signed an FTA with China in

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<sup>21</sup> According to polls, most Taiwanese support institutionalised negotiations with the Mainland China but there are more respondents who consider that negotiations are too fast than those who think they are too slow. At the same time, 84.5 % of population support maintaining status quo in Cross Strait relations which means 'no unification, no independence and no use of force'. Source: Mainland Affairs Council, 17 July, 2013.

2013 is seen in Taipei as an indication that Switzerland may also become another ECA partner<sup>22</sup>.)

#### 2.3.4. The United States

The United States has been Taiwan's principal strategic ally for over half a century. It was also Taiwan's main trading partner until 2003, when it was outpaced by mainland China. Taiwan is the US's tenth trading partner in goods. Significantly, it is the sixth most important export destination for US agricultural goods.

The trade dialogue between the two allies has experienced a certain fatigue in the recent years. In 1994, both sides initiated a framework for discussing bilateral trade relations – a Trade and Investment Framework Agreement (TIFA) – but this was suspended between 2008 and early 2013, largely due to a dispute about US beef products. TIFA has often been regarded as a starting point for a future FTA. However, given the US's current disinterest in bilateral trade agreements and what is perceived as Taiwanese protectionism, an FTA appears rather unlikely in the medium term.

In 2011, US-Taiwan exchanges of goods and services (excluding military and government services) were valued at USD 85 billion. The US had a deficit in its trade with Taiwan – USD 11.5 billion in 2011. This was composed of a deficit in the trade in trade goods which – USD 15 billion – which was partly offset by the US's surplus in the trade in services – USD 4.5 billion<sup>23</sup>.

### 3. EU-Taiwan Trade Relations

The EU-Taiwan merchandise trade represents roughly half of the EU-South Korea merchandise trade and one third of the EU-Japan merchandise trade.

During the past 20 years, EU-Taiwan trade volumes have increased four to twelvefold (depending on the method of calculation); however, Taiwan's relative share in the EU's total trade has fallen. In 2012, the bilateral trade in goods amounted to EUR 32.32 billion, making Taiwan the EU's 23rd-largest trading partner, down from the 14th position in 2010. Yet bilateral trade volumes remain significant. The EU-Taiwan merchandise trade represents roughly half of EU-South Korea merchandise trade and one third of EU-Japan merchandise trade.

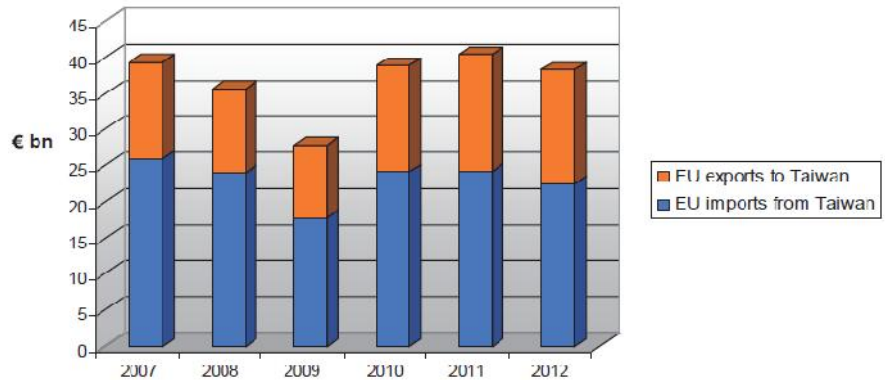
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<sup>22</sup> [CNA](#), 10 July 2013.

<sup>23</sup> US Trade Representative



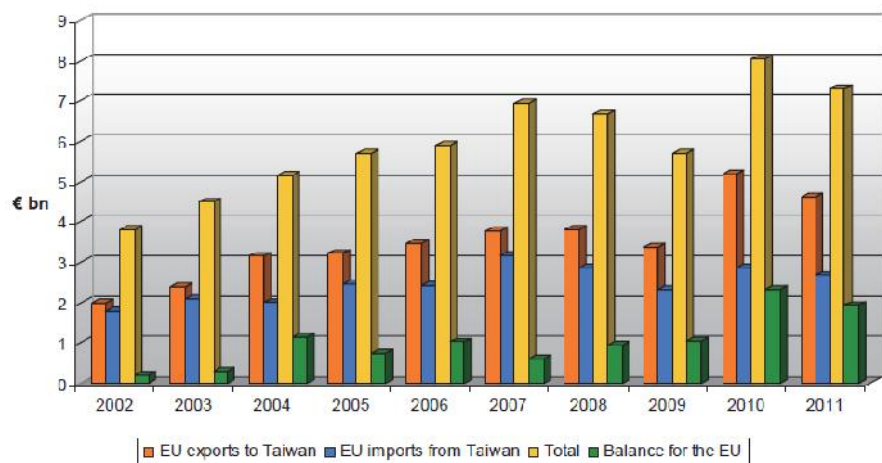
**Figure 3:**  
EU-Taiwan trade in goods



Source: EETO, 2012<sup>24</sup>

The value of the EU-Taiwan trade in services was EUR 7.3 billion in 2011 – a level considered below its full potential. Like South Korea and Japan, Taiwan is an important industrial partner for the EU when the trade structure is taken into account. Most of Taiwan's imports are telecommunications and office equipment, while most of its imports from the EU are machinery equipment, notably for information and communication technologies, car components and chemical products.

**Figure 4:**  
EU-Taiwan trade in services



Source: EETO, 2012

The EU is the biggest source of foreign investments in Taiwan, ahead of the US and Japan. European investment stocks account for more than one fourth of the total foreign direct investment

For Taiwan, the EU is the fourth-largest trade partner (after the PRC, Japan and the US) and the most important source of foreign direct investment (FDI) – 31 % of all of FDI flows into Taiwan in 2012. In 2012 European investments stock in Taiwan reached EUR 23.25 billion and accounted for more than one-fourth of the total foreign direct investment stock in Taiwan. As the biggest foreign investors in Taiwan, EU companies surpassed those from the US and Japan. EU's investment inflow in Taiwan —

<sup>24</sup> EEAS, [EU-Taiwan Factfile 2012](#).



stock in Taiwan.

EUR 10.3 billion in 2011 — is however low compared to Singapore (EUR122.8bn) and (China EUR 101.5bn)<sup>25</sup>.

Unlike exports and imports, in Taiwan's 2012 FDI into the EU (EUR 53.6 million) rose by 45 % compared to 2011. Nevertheless, Taiwan's investment in EU remained limited, representing less than 1 % of Taiwan's total FDI flows in 2012.

### 3.1. Considering an EU-Taiwan agreement

The arguments against the EU's pursuit of an agreement with Taiwan in the near future include the lack of an EU-China accord, the EU's busy agenda negotiating other trade agreements and the fact that the Taiwan already has an open economy.

While an agreement with the EU is one of Taiwan's priorities, it is not the main focus of its trade policy.

The arguments for a trade or investment accord include the size of Taiwan's market (including investments in China and elsewhere in Asia), its non-tariff measures that hamper trade and its

On numerous occasions, Taiwan's authorities and the European Chamber of Commerce in Taipei have called for a comprehensive economic cooperation agreement between EU and Taiwan.

In its 2006 communication, 'Global Europe - Competing in the World', the European Commission established key criteria for determining whether to develop free trade areas. These included market potential (economic size and growth), the level of protection against EU export interests (tariffs and non-tariff barriers) and FTAs with EU competitors<sup>26</sup>. The Commission's November 2010 communication, 'Trade, Growth and World Affairs', set further priorities, which included completing ongoing trade negotiations and focusing on the EU's strategic partners<sup>27</sup>.

An FTA with Taiwan was not earmarked as a priority. An ECA with Taiwan was also judged difficult to accomplish, given the Commission's engagement in several ongoing, challenging trade negotiations, and the fact that there are no trade agreements between the EU and Beijing.

Taiwan, on the other hand, has insisted that EU-Taiwan negotiations would help the EU to prepare for bilateral EU-China negotiations. It is also argued that the quality of its regulatory environment, growth potential and market size (especially given the scale of Taiwanese investment in China) mean that Taiwan would offer the EU a better opportunity in the face of current economic challenges than would many of the countries with which the EU is currently negotiating trade agreements<sup>28</sup>.

For Taiwan, an Economic Cooperation Agreement with the EU is one of priorities (as are the TPP and agreements with the US, Southeast Asia and India). Although the EU is not its main focus, Taiwan has actively worked to raise interest in the EU-Taiwan ECA, following the guidelines of the government's 'Position paper for lobbying the European Commission, European Parliament, European businesses and EU member states'<sup>29</sup>. At the same time, Taipei is well aware of the challenges of initiating an ECA. As a consequence, proposals have suggested other ways to enhance

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<sup>25</sup> EEAS, [EU-Taiwan relations - Trade and Investment](#).

<sup>26</sup> European Commission Communication 2006 "Global Europe - Competing in the World"

<sup>27</sup> European Commission Communication 2010 "Trade, Growth and World Affairs"

<sup>28</sup> Patrick A. Messerlin, The EU Preferential Trade Agreements: Defining Priorities for a Debt-Ridden, Growth-Starving EU, SciencesPo/GEM, January 2012

<sup>29</sup> See "[Overview of effort of Taiwan for FTA/ECA](#)", Ministry of Economic Affairs.

advanced regulatory environment.

economic exchanges, such as a **bilateral investment agreement**. Some EU business associations consider bilateral investment agreement a building block for a more comprehensive accord. Others argue that it also would help reduce the gap between the current level of bilateral trade in services and the level that could be attained.

The European Parliament has also called for the enhancement of the EU-Taiwan trade relations and for an economic cooperation agreement (see box below)<sup>30</sup>.

#### **European Parliament positions on EU-Taiwan trade relations**

12 September 2012

'urges the Commission and the Council, in accordance with Parliament's CFSP resolution of May 2011, to take concrete steps to further enhance EU-Taiwan economic relations, and to facilitate the negotiation of an EU-Taiwan economic cooperation agreement'

*On the Annual report on the Common Foreign and Security Policy (2012/2050(INI))*

11 May 2010

'given that the expansion of cross-strait economic relations is in the interest of both sides and of the EU, strongly supports the enhancement of EU-Taiwan economic ties and the signing of an EU-Taiwan economic cooperation agreement'

*On the Annual report on the main aspects and basic choices of the Common Foreign and Security Policy (CFSP) in 2009 (2010/2124(INI))*

### **3.2. Impact assessments of potential agreements/trade enhancing measures**

No sustainability impact assessment has been made on the potential EU-Taiwan FTA by the European Commission. However, equivalent studies have been prepared by various research institutions in both Europe and Taiwan. The report on the possible effects of trade enhancement measures (TEMs) by Copenhagen Economics in 2008, which was updated in 2012,<sup>31</sup> provides a useful estimate and allows comparison with South Korea and Japan<sup>32</sup>.

According to the report, TEMs with Taiwan could increase EU's GDP by EUR 2 billion per year. This is comparable to the relative contribution of

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<sup>30</sup> At the moment of writing, the European Parliament is considering a resolution on enhancement trade and investment relations between the EU and Taiwan, tabled for the plenary session of October 2013, [2013/2675\(RSP\)](#)

<sup>31</sup> The ex-ante assessments by Copenhagen Economics at the request of European Chamber of Commerce in Taipei "Gains from free trade with South Korea" (2007) and "Taiwan: Enhancing Opportunities For European Business" (2008). The assessment on EU-Taiwan TEM was updated in September 2012: "[EU-Taiwan Trade Enhancement Measures](#)".

<sup>32</sup> While the results of the subsequent assessments by the Commission on South Korea may have different and more up to date results, the assessment of Copenhagen Economics is facilitator in this context because of similar methodologies.

the EU-South Korea trade liberalisation (EUR 5 billion per year) as Taiwan's economy makes up 40 % of South Korea's economy. EU-Taiwan trade flows would be increased by 48 %; this can be compared to the projected increases of trade volumes to be derived from TEMs for Japan, South Korea and Canada – 23 %, 58 % and 37 % respectively. The greatest beneficiaries from EU-Taiwanese TEMs would be EU service sectors (engineering, transport, trade, financial). The liberalisation of goods trade would also benefit sectors in the EU, and notably the electronics and machinery, clothing and textiles sectors, food and beverages (20 % tariff on sparkling wines) and car producers (currently facing tariffs of 17.5 % and obstacles related to homologation).

Furthermore the authors conclude that, as the 5<sup>th</sup> largest economy in Asia, Taiwan meets the criterion of market size and growth potential. Another of the Commission's criteria – that the potential partner must have or be considering FTAs with the EU's competitors – is also the case, the report argues. Finally, the paper suggests that the urgency of instigating EU-Taiwan TEMs has increased since the entry into force of the EU-South Korea agreement.

Trade diversion away from Taiwan — the expected effect resulting from the EU-South Korea free trade agreement — has not happened yet.

It was expected that the EU-South Korea FTA will divert trade away from Taiwan, especially in the electronics were both compete. It has not happened yet – presumably because trade remains limited as a result of residual non-tariff barriers and suppressed demand in the EU market<sup>33</sup>. And while Taiwan's trade negotiations with EU competitors was also cited as an impetus for implementing TEMs, Taipei's progress on these negotiations has in fact been limited.

Other assessments of EU-Taiwan trade liberalisation that looks 'beyond geopolitics' have been made. One arguing in favour of comprehensive liberalisation was carried out by the Brussels-based European Centre for International Political Economy<sup>34</sup>. Another, made in 2008 by Taiwan's Chunghua Institute for Economic Research, proposed that an EU-Taiwan ECA would provide greater benefits for the EU than for Taiwan. An evaluation by Kenichi Kawasaki (RIETI, Japan) in 2011 ranked Taiwan eighth on the list of countries that would supply the EU with the greatest estimated GDP gains; Taiwan followed China, Japan, Russia, India, US, Thailand and South Korea in the list. The assessment, however, did not take into account certain factors, such as the partners' negotiating capacity and Russia's imminent accession to the WTO<sup>35</sup>.

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<sup>33</sup> Tseng Yea Jen, Challenges and Opportunities of a EU-Taiwan ECA. A Review of Political-Economic Perspectives, IFRI, November 2012, [ifri.org](http://ifri.org)

<sup>34</sup> [Beyond Geopolitics - The Case for a Free Trade Accord between Europe and Taiwan](#), 2010.

<sup>35</sup> Patrick A. Messerlin, The EU Preferential Trade Agreements: Defining Priorities for a Debt-Ridden, Growth-Starving EU, SciencesPo/GEM, January 2012. Original source Kawasaki, Kenichi, 2011. Impact of Trade Liberalization: Economic Model Simulations.

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In general, while the outcomes of such studies – which all presume to conduct their analysis independently of geopolitical considerations – differed, most suggest that potential benefits to the EU of an agreement with Taipei are comparable those offered by other FTAs being negotiated.

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Conference on the Future of the Japan-EU Free Trade Area, Keio University. October, 29, 2011.