1. Introduction

Since the 1997/1998 financial crisis, important developments have occurred in East Asia’s regional economic relations. Two trends are especially noteworthy. The first of these is the establishment of the ASEAN Plus Three (APT) framework, involving the ten member states of the Association of Southeast Asian Nations (ASEAN)¹ plus Japan, China and South Korea. The APT represents the first formalised, summit-based and exclusively East Asian economic grouping yet operationalised. It has mainly focused on developing new mechanisms of regional financial governance, thus working to avert another regional financial crisis and generally attempt to better manage East Asia’s growing regional economic interdependence. The second regional trend concerns the proliferation of (mainly bilateral) free trade agreements (FTAs) in East Asia and the Asia Pacific. The ASEAN-China FTA has especially generated much interest, as have the various FTA projects of Japan, South Korea, Singapore, Thailand and other East Asian states. Together, the expanding web of FTAs in the region and the fast evolving APT framework are having profound effects on the calculus of East Asia’s regional economic relations. Taiwan’s position in these developments has been relatively marginal. China’s contestation of Taiwan’s politico-diplomatic legitimacy has significantly narrowed its FTA options and the chance of ever becoming a full APT member. This paper makes a study of

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¹ Namely Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam.
these new developments in East Asia’s regional political economy, Taiwan’s prospects of engaging them, and the implications for Taiwan of remaining relatively marginalised in new APT and FTA processes.

2. Taiwan and East Asia’s Pre-Crisis Regional Political Economy

Taiwan’s foreign economic policy (FEP) has always been defined by ‘contested statehood’ factors (Dent 2002). Its ambiguous position in the international community derives from the Peoples Republic of China’s (PRC) insistence that Taiwan is a Chinese province and not a sovereign nation-state, a view formally accepted by the large majority of national governments. Despite the extensive internationalisation of Taiwan’s economy, its FEP must work within significant external constraints that primarily derive from this predicament. It has thus had comparatively limited ‘diplomatic space’ in which to manage its foreign economic relations, although changes in the nature of the international political economy – particularly the growing salience of non-state units and actors – have created new diplomatic possibilities for Taiwan. Moreover, Taiwan has been forced more down the FEP ‘low politics’ route due to many conventional ‘high politics’ foreign policy routes being closed off.

To some extent, Taiwan’s limited ‘high politics’ options was not so much of a constraint in its foreign economic relations with East Asian neighbours before the 1997/98 financial crisis. Up to then, East Asia’s regional economic integration had been primarily developed through the process of regionalisation rather than regionalism. Regionalisation arises generally from the regional concentrations of internationally linked private-sector activities (e.g. trade, investment and other economic transactions), whereas regionalism occurs as a result of public policy initiatives, such as an FTA or other state-led projects of economic co-operation and integration that originate from inter-governmental dialogues and treaties. Both are mutually reinforcing processes: for instance, an FTA breaks down barriers hindering commercial transactions between parties to the agreement, while well established regionalised business networks help exploit the potential of FTAs and other integrational agreements. However, East Asia hosted very few such agreements by the mid-1990s, as is later detailed, and Taiwanese firms were furthermore well integrated into the region’s international business networks. In 1991, Taiwan
had also become, as had China and Hong Kong, a member of the Asia-Pacific Economic Co-operation (APEC) forum, which in 1994 launched a plan to create a ‘free trade and investment zone’ by between 2010 and 2020. Thus, Taiwan’s commercial interests in the region were not by this time that disadvantaged by the politico-diplomatic constraints of ‘contested statehood’.

This situation, though, began to change quite dramatically after the 1997/98 financial crisis, whereby the crisis itself helped catalyse significant changes to the East Asian regional political economy. At a generalised level, the most important change has been the marked increase in international economic agreements between East Asian nation-states as together they have sought to better manage their regional economic interdependence in the aftermath of the crisis. We examine the nature and scope of these agreements below, and how, as a ‘contested state’, Taiwan’s ability to participate in East Asia’s new regional political economy is somewhat limited, as is examined below. The extent to which this disadvantages Taiwan in both economic and political terms is also discussed.

3. The ASEAN Plus Three (APT) Framework

3.1 Early Beginnings

The APT framework consists of the ten member states of ASEAN and the three Northeast Asian states of Japan, China and South Korea. It is historically significant as APT represents the first real coalescing of an East Asian economic grouping. The framework was established in December 1997 at its inaugural summit convened in Kuala Lumpur, during the height of the region’s financial crisis (Stubbs 2002, Tay 2001, Webber 2001). The APT was thus initially shaped in the crucible of crisis-related events, and it is therefore not surprising that its principal focus has remained fixed on issues of regional financial governance in East Asia.

2 The term ‘regional political economy’ is a derivative heuristic device stemming from international political economy (IPE) analysis. By regional political economy, we are thus referring to the social, political, and economic arrangements affecting a region’s systems of production, exchange, and distribution and the mix of values reflected therein, thus drawing upon Strange’s (1994) definition of IPE but with ‘region’ substituted for ‘global’.
Japan did much of the preparatory work in this field. In early response to the first outbreak of the financial crisis, Tokyo proposed the creation of an Asian Monetary Fund (AMF) in September 1997. The AMF was conceived as a standby fund of US$100bn to provide emergency financial assistance to East Asian countries whose currencies were subject to disruptive speculative pressures. Taiwan also backed this Japanese initiative, whereby the two offered to pool their considerable foreign exchange reserves in order to operationalise the AMF. However, the US opposed to the idea because of concern over how the AMF would undermine the multilateral competence of the IMF, and hence indirectly lead to a loss of American structural power and influence over the international financial system (Rapkin 2001). This was despite Japan’s argument that the AMF would be a new facility to provide additional resources to supplement those of the IMF, if required. China was against the AMF proposal too, mainly because of Taiwan’s involvement but also owing to this perceived hegemonic manoeuvring of Japan’s within the East Asian regional political economy. Consequently, other East Asian states proved reluctant in backing the AMF initiative.

While this first attempt at developing regional financial governance mechanisms in East Asia failed, other more acceptable proposals from Japan followed, and this whole process was to later converge with the APT process. In October 1998, Japan unilaterally launched its New Miyazawa Initiative (NMI, named after Japan’s then finance minister), which was primarily based on US$30 billion of extended liquidity provision for East Asian economies if they again found themselves in financial crisis. Other APT member states generally welcomed the NMI and other related initiatives from Japan, such as the US$5 billion Special Yen Loan Facility, especially after how the crisis had by this time revealed the IMF’s failures and inadequacies in dealing with the region’s financial problems (Hughes 2000). Moreover, the NMI both provided a foundation stone for later developments in East Asian financial co-operation, as well as helped catalyse discussions on regional finance at the second APT summit, convened at Hanoi in December 1998. Here, East Asia’s leaders agreed under the ‘Hanoi Plan of Action’ to develop new methods for improving regional financial stability. In addition, China’s proposal for regularised APT Finance Ministers Meetings at the vice-ministerial level was accepted and operationalised in March 1999. This was upgraded to full ministerial level the following year at Chiang Mai, Thailand, where APT finance ministers met at the sidelines of an Asian

3 Japan’s then Finance Minister, Eisuke Sakakibara, also admitted later that part of China’s opposition to the AMF proposal was due to his failure to consult Beijing before the AMF’s launch (The Japan Times, 24.02.2004).
Development Bank (ADB) meeting in May 2000 and proposed the Chiang Mai Initiative (CMI).

3.2 The Chiang Mai Initiative (CMI)

A few months later at the Fourth APT summit held in November 2000 at Singapore, East Asian leaders formally endorsed the CMI plan, which essentially constituted a more regional approach to averting another financial crisis. At its centre are a series of bilateral currency swap agreements between APT member states. A currency swap is an agreement to exchange one currency for another and to reverse the transaction at some later date. The idea here is for harder currencies (e.g. dollars, yen, euros) to be initially swapped for softer local currencies facing severe speculative pressure in the markets, thus providing a counter-pressure mechanism to help stabilise the exchange rate of that local currency. The CMI is accompanied by a number of other supportive or related arrangements, namely: (i) an agreement to exchange information on short-term capital movements in East Asia, including the establishment of an early warning system to monitor signs of emergent financial crises; (ii) the exchange of views among APT members on reforming the international financial architecture; (iii) regularised meetings between deputy or vice-ministers of finance to review all CMI-related developments. As Ravenhill (2002) is keen to point out, the CMI is not an ‘AMF mark II’ because it rests upon a combination of bilateral agreements rather than the creation of a regional institution. Moreover, the liquidity provision involved is nowhere near as large as that proposed under the ill-fated AMF. Within the CMI, the core ASEAN economies agreed to raise their contributions to their own pre-existing ASEAN Swap Agreement (ASA) facility from a total of US$200 million to US$1 billion. Additional currency swap deals were initiated across APT’s wider membership, with a total of 13 bilateral arrangements signed by April 2004 (Figure 1). Taken together with the ASA, these currency deals amounted to US$33 billion. This represents a mere fraction of the combined foreign exchange reserves at the disposal of East Asian states that together would total at around US$1.5 trillion, which represents 60 percent of the world total. It was generally

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4 This ASEAN scheme had been established back in 1977.
5 By October 2002, Japan’s forex reserves stood at US$461 billion, China’s at US$266 billion, South Korea’s at US$117 billion, and ASEAN had a combined total of US$204 billion (Korea Economic Update, December 2002). These were comparatively very large sums. For example at the same time the US’s forex reserves stood at around US$60 billion.
accepted that such low swap arrangement sums were likely to prove insufficient to fend off a major speculative ‘attack’ on an unstable currency (Chalongphob 2002). For example, there was an estimated $150 billion capital outflow in the three months following the Thai baht devaluation in July 1997.6

There are a number of possible reasons why the CMI did not at this early stage involve more ambitious levels of currency swap funding. Firstly, there are competing demands upon East Asian forex reserves, and substantial shares of them may be tied up elsewhere.7 Secondly, it was more politically expedient for the CMI to start with relatively small sums at the outset. What was more important at this point was the initial trust-building exercise that the CMI represented. Following on from this is the third main reason, which relates to lessons learnt from the AMF episode. The APT member states were wary of the CMI being perceived as a challenge to the IMF’s multilateral competence, and therein posing a threat to US foreign economic policy interests. Not only may the relatively small sums involved in the bilateral currency swap agreements be partly intended to allay any AMF-related anxieties, but also more importantly operationalising the agreements themselves are subject to IMF conditionality. Under current CMI arrangements, only 10 percent of the initial swap arrangements can be released unconditionally: thereafter beneficiaries must reach agreement with the IMF on a programme of economic reforms before further assistance is conferred.

Notwithstanding the limited regional ambition demonstrated by the CMI in its first phase, it nevertheless marked a significant step forward in East Asian financial co-operation, not least because of the almost complete lack to region-wide co-operation in this field before the 1997/98 crisis (ADB 2004, Henning 2002). Furthermore, there were indications towards the end of 2003 that APT member states were looking to significantly fortify the CMI system, in particular by multilateralising it. China was the first to officially propose converting the CMI’s separate bilateral arrangements into a unified multilateral currency swap arrangement at the October 2003 APT summit in Bali, whereby member countries would contribute from their

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7 For example, Ravenhill (2002) notes that a sizable share of Japan’s forex reserves is tied up in US Treasury securities.
foreign exchange reserves into a central fund, thus creating an AMF-style institution. Some APT countries strongly supported this proposal, although the APT group as a whole made no firm commitment at this stage at endorsing it.

Further discussions on the multilateral upgrading of the CMI system continued, however, into early 2004, driven largely by speculation about formal proposals to be tabled by the APT Research Group on financial and monetary co-operation at the APT Finance Ministers Meeting in May that year. Indeed, it was generally thought that these proposals would go beyond simply multilateralising the CMI to recommend the establishment of an East Asian exchange rate system, similar to that practiced by the European Union in preparation for introducing the euro single currency. Adopted such a system would require a relatively significant degree of economic and political co-operation amongst East Asian states. However, post-crisis trends in East Asian exchange rate management suggest that many countries in the region are heading back to pegging currency arrangements, either to the US dollar or a basket of currencies, while avoiding either a hard peg or free float system. Any APT proposal for a regional exchange rate system based on relatively loose commitments and constraints (e.g. wide upper and lower band limits) could be accepted by a core group of member states. To be effective, this would need to be underpinned by much larger amounts of foreign exchange reserves currently committed to the CMI currency swap arrangements.

3.3 The Asian Bond Market Initiative (ABMI)

A further key development within the APT group at strengthening regional financial governance has been the Asian Bond Markets Initiative (ABMI). The ABMI is designed to pool together the region’s huge domestic savings and reserves, better utilising them through fostering viable domestic and regional bond markets. A bond is usually a fixed-interest, long-term security that can be issued by governments, firms, banks and other institutions. Developing an Asian regional bond market would enable wider currency diversification to take

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8 It would also resemble the European Monetary Cooperation Fund of the 1970s and 1980s, on which the EU’s Exchange Rate Mechanism was based.
10 *Business Times (Singapore)*, 02.03.2004.
place through the issuance of local currency-denominated bonds by Asian issuers to investors in the region, thus allowing governments, corporations and financial institutions access to long-term funding in their respective domestic currencies. The ABMI plan was first discussed at the APT Deputy Ministers Meeting held in Chiang Mai in December 2002, and then formally endorsed by the APT Finance Ministers in September 2003. In between then, at the June 2003 Asia Co-operation Dialogue (ACD) meeting, eleven Asia-Pacific central banks agreed to establish an Asian Bond Fund with initial capital of US$1 billion. Later on that year in October 2003, the Asian Development Bank gave grants to Indonesia, Malaysia, Philippines, and Thailand to help them develop domestic bond markets as part of the APT’s new Guarantee Mechanism for the ABMI. The following month, a second Asian Bond Fund was launched by an enlarged group of Asia-Pacific central banks worth at least around US$1.5 billion, but unlike the first Fund the new bonds were denominated in Asian currencies rather than in US dollars. As with the first Fund, though, this was to be managed on behalf of the central banks by the Bank for International Settlements based in Hong Kong. A Thai proposal for a third Asian Bond Fund soon followed in February 2004, again involving APT and ACD member countries and again denominated in local currencies.

There is a strong case for developing an Asian regional bond market. One of the root causes of the 1997/98 financial crisis was the over reliance on short-term borrowing in foreign currencies by East Asian firms, banks and other institutions. Investing in long-term, local currency bonds would therefore help avoid this predicament. East Asia’s huge accumulation of savings have been deposited in local banks, much of which are then funneled to international financial centres and a significant amount of this is invested back into the region in turn. This causes what is known in market-speak as a problem of maturity and currency ‘double mismatch’, which increases the vulnerability of host emerging economies to sudden massive reversals of this capital and to the consequent large depreciation of currencies and a domestic banking crisis.

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11 The ACD was established by Thailand in 2002, and provides a forum for debate and co-operation on political and economic matters. Relevant ministers from most Southeast Asian states (except Burma), Japan, China, South Korea, Bangladesh, India and Pakistan, as well as Bahrain and Qatar, have attended ACD meetings.
13 This included the 11 East Asian countries and Australia and New Zealand that participated in the first Asian Bond Fund, plus India and Kazakhstan this time.
14 Business Times (Singapore), 17.11.2003.
owing to the rapid deterioration of the balance sheets of borrowers and financial institutions.\textsuperscript{16} This was one of the transmission mechanisms that triggered East Asia’s financial crisis in July and August 1997.

Like the CMI, the ABMI provides East Asia with the opportunity to utilise the region’s huge financial resources for promoting its own regional financial stability and economic development, rather than investing in, or diverting these resources to other regions. Furthermore, as one financial analyst remarked, “People in Asia want to reduce their exposure to the dollar but there is nowhere to go. China is looking at the euro, as an alternative to the dollar, and there is a sense of urgency there to develop the Asian bond market.”\textsuperscript{17} A 2003 survey indicated that there is a potential demand for at least US$100 billion a year of Asian bonds if these could be freely traded across borders.\textsuperscript{18} In the same year there were around 1,400 public bond issues amongst East Asia countries that raised some US$66 billion in total, but this represents a mere fraction of the US$16.8 trillion US dollar bond market, of which about 30 percent are government issues.\textsuperscript{19}

At this point in time it remains unclear what an APT-driven Asian regional bond market will look like. The ABMI is still in its infancy, and much depends on whether the recommendations of the APT Research Group are endorsed at the forthcoming 2004 APT summit.\textsuperscript{20} However, what is clear is that a number of East Asian countries are looking to internationalise their national bond markets. Most significantly, Japan is exploring different means to open up foreign access to its US$5 trillion government bond market, and China is also seeking to develop its 1 trillion renminbi government bond market.\textsuperscript{21} More generally, US pressure on East Asian states to revalue their exchange rates, hence making their exports less price competitive, could provide a further spur to East Asian financial regionalism, a view expressed by Randall

\textsuperscript{17} Michael Preiss, Chief of Investment Strategies at CFC Securities, Hong Kong. \textit{Business Times (Singapore)}, 17.11.2003.
\textsuperscript{18} \textit{Business Times (Singapore)}, 17.11.2003.
\textsuperscript{19} \textit{Business Times (Singapore)}, 17.11.2003.
\textsuperscript{20} In the meantime, two APT Working Groups have been established on ABMI matters, one on Creating New Securitised Debt Instruments and the other on Credit Guarantee Mechanisms. A joint meeting between both was convened in April 2003 in Seoul. Additional APT Working Groups relating to Asian bond market issues are to be set up, most likely after the APT Research Group makes its report recommendations.
\textsuperscript{21} \textit{Business Times (Singapore)}, 17.11.2003.
Henning at the Institute of International Economics based in Washington DC. Individual states may find it difficult to resist such American pressure, but an East Asian regional group with its combined financial resources would not. The fact that the APT group hold more 60 percent of the world’s foreign exchange reserves and yet hold less than 13 percent of the quotas in the IMF – to which voting shares are closely tied – creates further incentive for strengthening East Asia’s own regional powers of financial self-determination. In the meantime, the ASEAN Plus Three group will remain ‘Asia Minus Taiwan’ whilst China maintains its opposition to Taiwan membership as a separate political entity.

4. New FTA Projects in East Asia and the Asia-Pacific

4.1 The New FTA Trend Takes Off

The proliferation of bilateral free trade agreement (FTA) projects in the Asia-Pacific has become an important new defining feature of the region’s international political economy (Dent 2003, Dobson 2001, Lloyd 2002, Ravenhill 2003, Webber 2001). At the time of the 1997/98 East Asian financial crisis, the Asia-Pacific was host to only a small handful of FTA projects (Figure 2). At five concluded FTAs in total, this represented a very small number by global region comparison (Table 1). Yet within a few years the Asia-Pacific had become host to the world’s fastest growing concentration of new FTA projects. By the end of 2003, the region was host to a total of 54 FTA projects in various stages of development (Figure 3). In this rapid expansion of FTA project activity in the Asia-Pacific, 16 new FTAs have been concluded in the region since the 1997/98 crisis. Ten of these have involved East Asian states and five have been completely within the East Asian region. This is set against the continued expansion of FTA activity globally. From 1997 to 2003, the number of concluded FTAs in the world more than doubled from 72 to 159 (Table 1). In this context, the new Asia-Pacific FTA trend is constituent to the intensifying FTA trend worldwide, although as mentioned earlier the region’s FTA expansion has been particularly noteworthy with its total number more than

\[ 22 \text{ Channel News Asia, 17.03.2004.} \]
\[ 23 \text{ 'Concluded' here refers to FTAs that have been signed by involved parties after the satisfactory conclusion of official FTA negotiations between them.} \]
\[ 24 \text{ This last group comprises AFTA, Japan – Singapore, China – ASEAN, China – Hong Kong SAR and China – Macao SAR.} \]
quadrupling over the same period from 5 to 21. There are main general explanations behind the new Asia-Pacific bilateral FTA trend.

The first of these concerns the *trade institution falterings of ASEAN, APEC and the WTO* on advancing their respective trade liberalisation agendas from the late 1990s onwards. For ASEAN, this relates to difficulties arising from realising both the objectives and potential ASEAN Free Trade Area (AFTA) project since the 1997/98 financial crisis (Mahani 2002). For APEC, its problems over realising its centrepiece 2010/2020 free trade and investment zone project came to a head at its 1998 summit, when a disagreement between Japan and APEC’s Anglo-Pacific members (primarily the US) over agricultural trade liberalisation caused serious damage to the organisation itself (Rapkin 2001). However, APEC’s failure to get significant traction on its 2010 / 2020 regional trade liberalisation project is more an issue for its Anglo-Pacific member states (the US, Canada, Australia, New Zealand) than its East Asian members, who are far more interested in APEC’s economic co-operation and developmental projects. Most importantly of all, regarding the WTO, its faltering at its 1999 Seattle Ministerial Meeting made a particularly profound impact upon traditionally staunch multilateralist East Asian states like South Korea, Japan and Singapore. Other Asia-Pacific states have also been frustrated with the slow progress in the WTO on trade liberalisation agricultural. Subsequent problems with advancing the Doha Development Round of global trade talks, most recently at the September 2003 Cancun Ministerial, has only confirmed the view to many Asia-Pacific policy-makers that a fortified bilateral FTA policy helps make for a more risk-averse approach in light of a possible collapse in the multilateral trade order.

The second general explanation lies in East Asia and Asia-Pacific states’ *response to the global FTA trend*. For example, the only FTA project initiated in East Asia before the 1997/98 crisis was AFTA. Bilateral FTA projects presented a means for East Asian states to catch up with their industrial rivals (e.g. from Latin America and Eastern Europe) in the wider global FTA trend, and secure comparable market access to key export markets. Thirdly, the new Asia-Pacific bilateral FTA trend may be explained by *evolving strategic diplomacy motives*. For East Asian states in particular, bilateral FTA projects offered a viable means to cement international economic relations at a time when financial crisis-induced tensions threatened to destabilise regional trade diplomacy. In this sense, they could also be seen as a new mechanism for better managing economic interdependence in the region. However, strategic diplomacy motivations
changed with the FTA trend itself: as the number of FTA players and projects grew so it became increasingly costly to stay out of the game.

4.2 Taiwan’s FTA Policy and Strategy

As with China, Taiwan could not effectively develop FTA projects with trade partners until it acceded to the WTO: other member countries wanted Taiwan and China within the ambit of WTO trade rules and norms first before initiating any FTA negotiations with them. Compared to many other core East Asian states – such as Japan, South Korea, Singapore and Thailand – both arrived relatively late to the region’s FTA game. In October 2001, Taiwan indicated it would pursue bilateral FTAs soon after formally joining the WTO, which was scheduled for January 2002.\(^{25}\) The Taiwanese Government established an FTA Task Force in November 2001, formed between the Ministry of Foreign Affairs and Ministry of Economic Affairs, and it also announced that Singapore, New Zealand, Japan and the US were the most probable candidates for Taiwan’s initial FTA partners.\(^{26}\) In the same month, China and ASEAN indicated they would sign an FTA the following year.

At first Taiwan’s FTA policy made a promising start, and various projects were initiated in November 2001. An informal ministerial level agreement between Taiwanese and Japanese officials was to initiate a private-level feasibility study on a bilateral FTA project.\(^{27}\) In the same month, US Senator Max Baucus tabled a bill to Congress that would authorise the US to negotiate and sign a bilateral FTA with Taiwan.\(^{28}\) This coincided with a visit made by Chen Po-chih, Chairman of the Council for Economic Planning and Development to Washington DC, where he reportedly found considerable support amongst US thank tanks, such as the Heritage Foundation, for a US – Taiwan FTA project.\(^{29}\) Meanwhile, at the November 2001 APEC summit in Shanghai, attending officials from Taiwan and Singapore informally


\(^{27}\) This was to be managed by the respective communities of the East Asia Businessmen’s Conference, a private channel of communications between Taiwan and Japan established in 1972.

\(^{28}\) *Taiwan Central News Agency*, 09.11.01.

\(^{29}\) *Taiwan Economic News*, 14.11.2001.
discussed the idea of a bilateral FTA project. Informal discussions between Taiwan and New Zealand on a bilateral FTA had also occurred during late 2001.30

By May 2002, the US’s International Trade Commission (ITC) had commenced its scoping study of a prospective US – Taiwan FTA. In the meantime, Taiwan had formally proposed a bilateral FTA project with Singapore31, but had announced that it wished to exclude around 800 product lines from any future FTA with Singapore, mostly relating to textile and clothing products.32 Further informal discussions between Taiwan and New Zealand on a future bilateral FTA had also taken place in April 2002.33 Around this time, Taiwan and Panama – one of the Central American states with which Taipei conducts full diplomatic relations – announced their plans to commence bilateral FTA negotiations later that year.

No doubt after observing this progress, Beijing sought to constrain Taiwan’s FTA options. In June 2002, Chinese Minister of Foreign Trade and Economic Co-operation, Shi Guangsheng, stated his government’s opposition to any of its diplomatic partners signing FTAs with Taiwan, warning that they would encounter serious political troubles, with their trade and economic relations with the mainland being adversely affected. He repeated this thinly veiled threat in November 2002 at a news conference in Beijing.34 This seems to have had an immediate effect on Singapore, which reportedly sought thereafter to slow the pace of development of its FTA project with Taiwan. By June 2003, the Taiwan – Singapore project was suspended after Singapore reportedly introduced a new precondition that the negotiations and the FTA be carried out under the ‘one China’ principle, a position not acceptable to Taiwan.35 The prospects of Taiwan’s other FTA projects with Japan and New Zealand also diminished after the warning statements made by Beijing during 2002.36 The US was the only diplomatic partner of China that did not appear to take much notice of these, although discussions between Washington and Taipei on any future FTA had become mired by disputes over intellectual property rights (IPR) and other issues pertaining to Taiwan’s compliance to its WTO accession

31 Straits Times, 19.03.2002.
34 Taiwan News, 15.11.2002.
35 Taiwan Economic News, 30.06.2003.
36 Some private sector feasibility studies on a Japan – Taiwan FTA have since been conducted but their activities have not generated much public interest.
commitments, e.g. on agriculture and pharmaceuticals. These have persisted into 2004 with the result that US – Taiwan FTA negotiations may not commence for some time yet.

Taipei did manage, though, to launch FTA negotiations with Panama in October 2002, leading to a successful conclusion of talks in August 2003. This first FTA signed by Taiwan’s entered into force in January 2004. Panama is an insignificant trading partner for Taiwan, and the economic benefits of the Agreement were far outweighed by the political benefits. Taipei had gained experience at learning how to negotiate and construct an FTA (although the provisions of the Taiwan – Panama FTA drew much upon the template of the US’s FTA model, for example on rules of origin), and moreover had set a diplomatic precedent by signing such a trade agreement. Taiwan has reportedly initiated bilateral FTA projects with other Central American diplomatic partners, namely Costa Rica from October 2002 and Guatemala from March 2003.37 However, taken together, the twenty-seven relatively small states that Taiwan’s enjoys full diplomatic relations with account for only four percent of its total trade. In commercial and ultimately political terms, Taiwan’s FTA options here are currently rather limited.

Moreover, progress on FTA projects with more important trade partners, such as Japan and Singapore, has been slow or even non-existent since 2002. Attempts have been made by Taipei to initiate new FTA projects with the Philippines and the Association of Southeast Asian Nations (ASEAN) as a whole, but little traction has been achieved here too.38 The announcement from the Taiwanese Government in October 2003 that it is flexible on the title conferred to Taiwan (e.g. ‘Chinese Taipei’, as used in APEC) in any prospective FTA failed to achieve the desired effect amongst its trade partners.39 Or at least this is what appears to be the case from the relative lack of media reports on Taiwan’s FTA project activity. One could conclude that since Beijing’s threatening statements to prospective FTA partners of Taiwan in 2002, Taipei has adopted a more clandestine approach to developing its FTA projects.40 Unlike many other Asia-Pacific government websites, there is no homepage icon link to Taiwan’s

37 See Taiwan News, 12.10.2002 and Taiwan News, 12.03.2003 respectively.
40 For example, Economics Minister, Lin Yi-fu, stated in November 2002 that Taiwan had made substantial progress concerning FTA discussions with quite a few countries, but he declined to reveal the names of these nations (Taiwan News, 06.11.2002).
FTA policy: indeed, on the BOFT website the information offered on the historic Taiwan – Panama FTA is three or four link-steps back. There have also been very few government press releases to the media over 2003 and 2004 concerning Taiwan’s FTA policy.

Nevertheless, Taiwan is unlikely to have made much ‘secret progress’ with its FTA projects, and is still confronted with the prospect of being marginalised in the new East Asia and Asia-Pacific FTA trend. Of extra concern is China’s increasing engagement in this trend, and the ASEAN – China FTA (ACFTA) project deserves particular mention here. While Taipei may not be feeling too anxious about ACFTA given that will not be fully implemented until between 2010 and 2015, it does have considerable potential to disadvantage Taiwan-based producers exporting to either China or Southeast Asia, especially in key sectors such as electronics and IT products where close competitive rivalry between all parties exist. This issue is further discussed in the following section. In addition to ACFTA, China has signed FTAs with Hong Kong and Macao, and currently has plans to also sign FTAs with Australia, New Zealand, India and Chile. Beijing has even raised the idea of creating a Northeast Asian FTA between China, Japan and South Korea, although Tokyo and Seoul have been somewhat cool to the idea.

Beijing has even proposed an FTA between Taiwan and China. The idea was first raised in November 2003 in context of China just having signed its Closer Economic Partnership Arrangements with Hong Kong and Macao earlier that year, in which FTAs were embedded. However, the same “two regions, one country” principle was being offered, which was unacceptable to Taipei. While there exists some support amongst Taiwan’s business community for a conventional FTA with China, as part of liberalising the restrictions on Cross-Strait commerce, the Taiwanese Government would be reluctant to sign an FTA with Beijing for reasons of economic and national security (Dent 2001).

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41 This was more or less admitted by Liu Jung-chuo, Director-General of the Ministry of Foreign Affairs’ Economic and Trade Department, who commented in September 2003 that, “Taiwan has encountered difficulties about signing bilateral trade agreements with other countries due to pressure from China.” Taipei Times, 26.09.2003.

42 Japan Times, 05.11.2002.

5. Taiwan’s Prospects in East Asia’s New Regional Political Economy

What, then, are Taiwan’s prospects in the new regional political economy of East Asia? Taipei has been aware of how both FTA and APT processes have the potential to marginalise Taiwan if it is not able to effectively engage in their respective integrational developments. While it has been able to participate in the new bilateral FTA trend (but not the APT framework), little progress has been achieved thus far on this front, and convincing key trade partners to sign FTAs with Taiwan will prove difficult for reasons previously discussed. In light of these challenges, various new ‘task forces’ have been recently established within Taiwan’s foreign economic policy framework. In addition to the FTA Task Force, there is also a ‘Go South’ Task Force charged with developing economic relations with Southeast Asia (hence diversifying commercial linkages away from mainland China), and a Strategic Task Force on Participation in International Economic and Trade Affairs that primarily seeks to advance Taiwan’s engagement with international economic organisations.

It was stated earlier that Taiwan’s relative marginalisation in the new East Asia regional political economy is ultimately of concern if its firms are put at commercial disadvantage in relation to their competitors. The regionalisation of Taiwanese business activity is already extensive, but this has become increasingly skewed towards mainland China, its natural commercial partner ‘sub-region’ within East Asia. As previously hinted, Taiwan’s growing commercial dependence on mainland China poses a number of economic and national security dilemmas for Taipei. Regarding FTAs, although new agreements such as ACFTA and others that China signs could actually help those Taiwanese firms producing mainland ‘local content’ products that are exporting to important Asia-Pacific markets, Taiwan’s own lack of FTA progress could further deepen its commercial dependence on the PRC. As Taipei Mayor Ma Ying-jeou commented in October 2003 at the 12th East Asia Economic Summit regarding the effects of ACFTA, “Although it will take place seven years from now, still you can see that goods ... in the ASEAN countries can enter the Chinese mainland without tariffs… Taiwan will still have to pay tariffs, which will put Taiwanese businesses at a competitive disadvantage.”44 He further stated that more Taiwanese businesses would relocate to China if Taiwan cannot

secure similar free trade pacts, and more generally that, “We do not want to be left in the cold when regional integration is taking place.”

If Taiwan does not manage to keep pace on the FTA front with East Asian neighbours such as South Korea, Singapore, China, Thailand, Malaysia and other countries producing similar products, then Taiwanese firms will be disadvantaged to the extent to which the new East Asian FTA trend develops. Moreover, the WTO’s recent falterings – from its 1999 Seattle Ministerial to 2003 Cancun Ministerial – have made FTAs more critically important in terms of market access when the multilateral trade system is itself not making progress and also under pressure.

What, then, can Taiwan do to develop an effective FTA policy and strategy in the future? The selection of official diplomatic partner countries like Panama, Guatemala and Costa Rica may appear somewhat illogical given these offer very little in commercial terms. On the other hand, they are good ‘practice swing’ FTA partners that provide Taipei with valuable experience at negotiating such agreements, and furthermore help establish Taiwan as a viable and trustworthy FTA partner itself. Amongst Taiwan’s significant trade partners, the US offers to the best prospect in both economic and politico-diplomatic terms. As mentioned previously, Washington is not likely to take much heed of Beijing’s thinly veiled threats, and an FTA with the US would offer Taiwanese firms freer market access to their second biggest export market (after China). However, there are a number of challenges facing Taipei just getting an US – Taiwan FTA project to the initial negotiating stage. It would require considerable movement on domestic economic reforms, especially relating to the aforementioned current bilateral disputes over IPR and other issues. In addition, there are a number of other Asia-Pacific states queuing up for FTA deals with the US, including Thailand, Malaysia, South Korea, the Philippines, Panama, and New Zealand, as well as various countries from other regions. Recent FTAs signed by Washington are also instructive: once negotiations did commence, Taiwan should be prepared to make significant concessions on agriculture and other sensitive industry sectors but not necessarily expect reciprocity from the US, especially on agriculture. Taipei should also anticipate Washington to push hard in their demands for service sector market access and wider commercial regime reform, e.g. privatisation.

45 Ibid.
Whereas the US has a penchant for asymmetric neo-liberal FTAs, Japan’s own FTA projects—or Economic Partnership Agreements as it prefers to call them—combine trade liberalisation with ‘developmental’ aspects, whereby provisions on enhancing mutual economic co-operation and development are conferred equal status with promoting freer trade. Given that Taiwan shares a similar developmental tradition with Japan, this FTA project may prove easier to negotiate than that with the US, although again agriculture is likely to prove the an extremely difficult area of negotiation. Furthermore, like the US, there is a long list of countries that wish to negotiate an FTA with Japan, and Taipei would have to undertake some very skilful diplomacy indeed to secure prioritisation here for Taiwan. Smaller FTA partners (e.g. Singapore, New Zealand) with formal diplomatic relations with China are less likely to prioritise Taiwan as a FTA partner owing to Beijing’s warning statements if they do. Finally, the Taiwanese Government must remained engaged in its efforts to help advance the WTO’s Doha Round of global trade talks as multilateral trade agreements on widening market access still offer Taiwanese firms better commercial opportunities than FTAs on the whole.

Regarding the APT framework, Taiwan cannot expect to accede to membership in the foreseeable future given its ‘contested statehood’ predicament, so what are the problematics of marginalisation here? On one level, not being party to APT’s regional financial governance initiatives may not pose a dilemma given that Taiwan still retains the world’s third largest store of foreign exchange reserves (between $150 - $200 billion) after Japan and China. The Taiwanese Government does not have a general problem raising cash for its procurement and other spending commitments, and the NT dollar is a relatively stable currency and may want to maintain a flexible exchange rate regime. More generally, Taiwan has one of the world’s smartest central banks in the Central Bank of China, as demonstrated over the 1997/98 financial crisis, and the economy’s external financial position remains strong through consistent trade surpluses. As things currently stand, Taiwan has more to offer the APT framework rather than vice versa.

The main problem for Taiwan is what the APT could become over the next decade and beyond. It has already it has made more progress than most commentators were predicting even a few years ago, and there is a strong chance that the APT could lay the foundation for an EU-style regional integration bloc in East Asia. Aside from efforts at fortifying regional financial
governance, there are other notable initiatives to emerge within the framework. This includes projects on promoting small and medium-sized enterprises, the provision of training courses on using environmental technologies, the APT Natural Gas forum, annual APT Ministerial Meetings (e.g. Economic, Labour), discussions on food security issues, and various other programmes such as APT Young Leaders and the e-APT Working Group. In terms of overall practical achievement, the APT framework has thus made advances in regional co-operation rather than integration. Ideas on how to proceed to the latter have, though, been proposed at recent APT summits. For example, there has been talk of creating an East Asian Free Trade Area or Zone, common market and even full monetary union.

These are bold objectives for a young regional framework like APT to aspire. Yet East Asia’s leaders understand that these are extremely long-term goals. As Chinese Premier Zhu Rongji commented at the November 2000 in Singapore, APT is a channel through which to “gradually establish a framework for regional financial, trade and investment co-operation, and furthermore to realise still greater regional economic integration in a step by step manner.” It is also worth noting that in the EU’s antecedent founding Treaty of Rome of 1957 lay the long-term vision of one day establishing a European common market. The point here is that while over-ambitious objectives can prove counter-productive – especially if scheduled deadlines for realising them are missed – longer-term goals provide critical direction and purpose to a regional framework.

There is also the issue of how certain APT processes and the new FTA trend may become increasingly conflated. Already we have seen how the APT framework has helped facilitate the development of bilateral FTA projects between East Asian states, as well as become the natural forum to discuss regional trade integration. On the first of these matters, China and the ASEAN group used APT in every stage of the development of their ACFTA project: agreement on launching a joint feasibility study was announced at APT’s 2000 summit at Singapore; a year later at the 2001 summit in Brunei, both sides came to a general agreement about the terms of the FTA; finally, at the 2002 summit in Phnom Penh, the ASEAN-China FTA was formally signed. A feasibility study into establishing an EAFTA has been conducted, although the report stated this was, “a long-term goal”, and should “take into account the variety of differences in

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*International Herald Tribune, 27.11.2000.*
developmental stages and the varied interests of the countries in the region.\textsuperscript{47} Taiwan’s omission from such a project, if it ever were to be initiated, could have serious political and economic consequences for the island’s long-term future.

6. Conclusion

Important new developments in East Asian regional economic relations have transpired since the 1997/98 financial crisis. These have centred on the new bilateral free trade agreement (FTA) trend and the recently emerged ASEAN Plus Three (APT) framework that incorporates all the major economies of East Asia except Taiwan into a coalescing regional grouping. Both processes are forging new co-operative and integrational links on a level and on a scale never seen before in East Asia. In this shift from \textit{regionalisation} to \textit{regionalism} there have been ensuing changes in East Asia’s regional political economy. While the both the FTA trend and APT framework are relatively young and not that yet well developed, they have brought out a proliferation of new international economic agreements between the region’s states. As a ‘contested state’, it has been difficult for Taiwan to engage in these twin processes. Taiwan’s only signed FTA to date has been with Panama, an insignificant trade partner and one of the few states worldwide that diplomatically recognise Taiwan over China. Furthermore, Taiwan’s prospects of ever joining the APT group are virtually non-existent whilst Beijing continues to oppose its membership of such organisations.

This paper has charted the development of the new FTA trend in East Asia and the Asia-Pacific and the APT framework, that to date has mainly focused on strengthening regional financial governance in East Asia. It has also examined Taiwan’s prospects of engaging these processes and the implications for Taiwan of remaining relatively marginalised in relation to them. Taipei does have some options on the FTA front but must combine domestic economic reform and skilful diplomacy if progress is to be achieved. At present, neither the WTO or APEC look likely to deliver market access benefits for Taiwanese firms to offset the market access costs of Taiwan being peripheral to the region’s FTA trend. Taipei can perhaps rightly depend on the

\textsuperscript{47} \textit{Japan Times}, 14.10.2002.
resourcefulness of Taiwanese businesses to themselves offset these costs to some extent. Regarding the APT framework, Taiwan’s non-participation could be problematic if it eventually develops into a more substantial regional integration arrangement. Being outside such an emerging regional bloc would be disadvantageous in both political and economic terms. It would not bode well for East Asia’s fourth economy to be sidelined in any new systems of regional economic governance that develop over forthcoming years. Taiwan must hope that its politico-economic interests will not be outpaced by these new developments in East Asian regional economic relations, and that new opportunities for engaging in them will arise over time.
References


### Table 1: Free Trade Agreements by Global Region, 1990 – 2003

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<th>FTAs by Region</th>
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<th>% of total</th>
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**Notes:** includes customs unions
Figure 1  Bilateral Currency Swap Agreements under the Chiang Mai Initiative (by April 2004)

Notes: 1. Extension of previous swap arrangement negotiated under the New Miyazawa Initiative (NMI); 2. The Japan-China swap is denominated in yen-renminbi, the only agreement not US dollar-based; 3. Provisional figures.

Sources: Henning (2002), various news media.
Figure 2  Asia-Pacific Free Trade Agreement Projects (before 1998)
Notes: * Initiated Pacific-3 tri-lateral FTA project from October 2002. ** PICTA (Pacific Island Countries Trade Agreement) involves the 14 Pacific Island Countries. Chile FTAs with other Pacific Latin American countries include Colombia and Ecuador, both in force from 1995. These two countries have been omitted because they have no FTA project links with other sub-regions in the Asia-Pacific. China also had an FTA link with the Central American Common Market (CACM) group by this date, in which Costa Rica was the first to start implementing (noted), with a bilateral FTA with El Salvador also in place by this time. Costa Rica and Guatemala were the only CACM members with FTA project links with other sub-regions in the Asia-Pacific by 2003. Mexico had negotiated FTA links with other CACM members by 2000, a CACM-Canada FTA was signed in 2002 (building on previous bilateral FTA link); a CACM-Canada FTA talks started in November 2001, and CACM-US FTA talks since 2003. CACM as an entity has been omitted in order to avoid graphic complications.