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## **ASIAN ECONOMIC INTEGRATION AND CROSS-STRAIT RELATIONS**

For the purpose of the bilateral exchange, this paper will consist four parts: (I) the Evolution of “ASEAN Plus Three” (APT); (II) Challenges Ahead for APT; (III) the Impacts of APT on Taiwan; and (IV) Some Observations and Recommendations for the Evolution of Cross-Strait Relations.

### **(I) The Evolution ASEAN Plus Three (APT)**

Before the Second World War, in 1940 Japan initiated the “Greater East Asian Co-Prosperity Zone” with the aim to establish a new regional order, with Japan and Manchuria as the centre. However, the initiative was aborted with Japan’s defeat in 1945. The post-war Yoshida Doctrine renounced militarism and avoided a heavy military expenditure. Instead, Japan single-mindedly devoted her talents, resources, and energy to a rapid economic reconstruction and export-led growth. Japan adhered to the role of a merchant state. When the Prime Minister Kakuei Tanaka visited Southeast Asia in 1974, anti-Japanese riots erupted in Thailand and Indonesia. Tokyo’s foreign policy establishment realized that the image of Japan as a self-serving economic organism had become a liability in the region. Although the Fukuda Doctrine of 1977 did not succeed, it reflected an aspiration of the then Japan to play a more active political role by “bridging” the non-communist ASEAN nations and the communist Indochina states. In the meantime, the four post-War decades found a stable Asian market mechanism with its manifestation articulated in the “flying geese theory”. In 1990, Malaysia proposed an “East Asian Economic

Caucus" without the "Caucasians", which was aborted with the U.S. objection and Japan's following suit. In 1996, the Clinton-Hashimoto Joint Declaration sealed the U.S.-Japan strategic partnership in the regional security.

The outbreak of the Asian financial crisis in September 1997 gave birth to the inaugural ASEAN Plus Three (APT) Summit. At the second summit in 1998, a 26-member East Asian Vision Group (EAVG) was established to study and advise on a long-term regional cooperation. At the third summit in December 1999, the leaders agreed to make the meeting permanent, and eight areas for cooperation were identified in the Joint Statement, which included economy, currency and finance, human resource development, and the development cooperation. In 2000, the Chiang Mai Initiative was postulated, which had two components. An "ASEAN Swap Arrangement" originally put forward in 1977 was to be expanded to cover all ten current members, and it increased in size from US\$200 million to US\$1 billion. The other, a more important, one is a network of bilateral swap agreements which was to be set up between individual ASEAN members and the "plus three" countries. Furthermore in 2000, priorities for economic cooperation were set up on the question of information and communication technology, SMEs and trade/investment; moreover, an envisaged APT FTA is to be studied, which might include six FTAs, namely the ASEAN Plus China, ASEAN Plus Japan, ASEAN Plus Korea, Japan-China FTA, Japan-Korea FTA, and China-Korea FTA.

In 2001, after the accession to the WTO, China made an active move to formally establish the 26-member Boao Forum for Asia (BFA), and had the permanent Secretariat set up in Boao, China. This presumably symbolized China's capability to lead the regional forum. What followed was the ASEAN Plus China Agreement in 2002, aiming at establishing an FTA between China and the ASEAN6 by 2010, and furthermore the ASEAN10 by 2015.

At the 6<sup>th</sup> APT Summit in 2002, an Asian Economic Community, proposed by Japan, was meant to be gradually formalized with the existing APT dialogue, with concrete measures the scope of which went beyond economic and financial cooperation and covered politics, security, environment, energy, culture, education, and social cohesion.

Furthermore, in lieu of the progress on the front of the ASEAN Plus China, Japan and ASEAN signed the Tokyo Declaration in December 2003, aiming at establishing the ASEAN Plus Japan FTA by 2012. Beginning with Japan's 2003 Whitepaper on Trade, by way of the continuation of Japan's strategies for regional cooperation FTAs with ASEAN and Korea first, and then the APT were to be signed, and then a link was to be made with Taiwan.

As to ASEAN Plus Korea, it is expected that a Framework Agreement on Comprehensive Economic Partnership between ASEAN and Korea should be signed in October 2005, which would include a zero-tariff scheme for 80% of the bilateral trade in goods, and negotiations on services trade and investment to be discussed in 2006.

It has been noted that in 2003, China's trade deficits with Taiwan, Japan, and Korea registered US\$14.7 billion, US\$40.4 billion, and US\$20.3 billion, respectively; whereas China's trade surpluses with the U.S. and the European Union reached US\$58.6 billion and US\$19.1 billion, respectively. In other words, China's earning from trade with the West went to Asian neighbours' pockets. Furthermore, with the steady progress made in APT, there have been external interests and internal discussions which entertained various possibilities of an expanded membership, including the ASEAN Plus Five (with Australia and New Zealand; or rather Hong Kong and Taiwan perhaps), or ASEAN Plus Three Plus Three, otherwise ASEAN Plus Six, i.e. a vision of the inclusion of Australia, New Zealand, and India, or what have you.

Given the occurrence of the Asian financial crisis, the rise of Asian conscience, China's accession to the WTO and the growing confidence in taking up an active regional role, Japan's keeping abreast with the regional engagement, Korea's growing sense of catching up, and ASEAN's continuous interest in serving as the "hub" rather than "spokes" in the process of the regional economic cooperation, it seems that the APT is marching towards institutionalisation. In addition to the Summit initiated in 1997, the APT today boasts of annual meetings of Economic, Foreign, Labour and Agricultural Ministers, as well as the senior officials' level meetings – by the name of East Asia Study Group – to coordinate the APT cooperation agenda. The future development of APT, at its current agreed pace, could form the biggest FTA in the world by 2015, with a total population of 1.98 billion. This will certainly provide a new global economic landscape with a tri-polar balance of power.

## **(II) Challenges Ahead for APT**

Despite the positive aspects described in the last section, some potential constraints and future challenges merit our attention.

### **U.S. Concerns Remain with a Strategic Positioning in Sight**

The U.S. strong opposition to the East Asian Economic Caucus (EAEC), proposed by Malaysia in 1990, was effective in that Japan and Korea expressed a lukewarm attitude thereto then, and thereby the fate of the EAEC was ill aborted. However, the Asian conscience, stirred up by the Asian financial crisis, outweighed the earlier concern, and in effect witnessed the reincarnation of the EAEC in the name of the APT. Nevertheless, the U.S. reserved concern and their invisible hand remained evident not only in the passive objection to the envisaged Asian Monetary Fund but also in the active pursuits of the Enterprise for the ASEAN Initiative (EAI). The EAI aims to encompass bilateral dialogues with ASEAN members so as to sustain American commercial interests on the one hand and assist ASEAN in upgrading

production, distribution and coordination. The US-Singapore FTA symbolized the U.S. continuous strategic interests in the region. Furthermore, the U.S. maintained their bilateral military engagements of various sorts, with Japan, South Korea, Taiwan, the Philippines, Australia, Singapore and Thailand in the region. Recently, the China-pressuring has been somewhat reminiscent of the Japan-bashing in the 1980s. There have been strong calls for China's currency valuation and policy reform in the exchange rate policy. After the lifting of the textile quota mandated under the WTO Uruguay agreement in January 2005, China's surging export to the U.S. has generated threats of retaliation unless China either imposes voluntary restraints or levies export tax on their textile products. The U.S. also pressured the EU to follow suit. It seems that the trade war will not go away any time soon.

### **China's "Peaceful Rise" Remains Uncertain:**

With the accession to the WTO in 2001, China further turned into the locomotive of the regional economic growth. With the nominal GDP ranked the 5<sup>th</sup> in the world, China's stake in the world economy is paramount. China's aspiration to peaceful development, articulated time and again in the policy statements, will be showcased in the run-up of the 2008 Olympic Game in China. Therefore, China takes a special stance on favouring multilateral cooperation manifested in the "New Security." The concept of the "New Security" has frequently been articulated in China's policy statements which concern new mandates in the areas of anti-terrorism, anti-narcotics, securing energy resources, stabilizing currency and finance, etc. The new perception has transcended beyond the traditional military concern. China continues to play an active role in the North Korea issue, the Shanghai Cooperation, and in mustering confidence-building campaigns with the neighbours surrounding her vast territories. China has also raised an eyebrow on the recent US-Japan pronouncement of Taiwan as their "common security concern." The recent issuing of the "Anti-Secession Law," which was meant to crystallize China's stance against Taiwan's separatist movement, has also aroused indignant sentiments across the Strait, an unfavourable pronouncement from the U.S. and the postponement of lifting the arms embargo by the EU. However, the endorsement of the "One China" principle by the leading "Green Camp businessman", Mr. Hsu Wen-Lung, who is both an investor in China and a supporter of the separatist movement, and the current and upcoming "peaceful visits" by the opposition parties' leaders have certainly tipped off the negative impact of the Law. China has dangled the carrot of much-wanted bilateral economic cooperation to Taiwan KMT Party Chief Lien Zhang, and will continue to whet Taiwan's enormous appetites for more. Nevertheless, the road of the coming negotiations on "One China" and ensuring China's peaceful development would be a bumpy one, to say the least.

### **Leadership Competition between China and Japan in the region**

The rise of China has created some tension between the two regional powers. China objected to Japan's proposition of establishing an Asian currency immediately after the Asian Financial Crisis, and insisted that keeping the Reminbi intact would be the best thing for China to do for the region at the time. The competition between China and Japan in vying for regional leadership seems only too obvious, and sooner or later China and Japan will face the challenge of competitive balance of regional influence and cooperative goodwill for the regional leadership. Japan has been a loyal U.S. ally since the post-Second-World-War period. Japan has lately been inspired to become a "normal nation" by amending the post-War Constitution, especially Article 9, which prohibits Japan's remilitarisation of non-defence nature. The U.S. have recently backed up Japan's wish to become a permanent member of the U.N. Security Council, but China has not been ready to agree to an expanded membership of the Council. Despite her expression of "deep remorse" on the war-time atrocity created during the World War recently articulated by Prime Minister Koizumi, the actions of textbook treatment on the war time history and the continuous visits paid to the war memorial at the Yasukuni shrine have, according to Asian nations, and China in particular, not matched up the words so expressed.

However, given the fact that China has replaced the U.S. as Japan's largest trade partner with the bilateral trade reaching 22 trillion Yuan, and that Japan's UN Security Council dream remained unfulfilled, it is not likely that the worsening of the relationship would be forthcoming. Furthermore, the ASEAN members do not take the Sino-Japan mild tension seriously, as it serves the purpose of keeping Japan on its toes and thereby stay engaged in the region.

### **The intra-ASEAN trade remains stagnant, and the competition with China in trade and investment remains real**

The ASEAN Free Trade Area (AFTA) was established in 1992, but the intra-trade dependence among the ASEAN members registered an increase from 18% in 1992 to 23% in 2002, not highlighting the expanded membership in the span of ten years. ASEAN attempts to accelerate its pace of liberalization by three years in advance of its original schedules, and to achieve the zero tariff by 2007 for the ASEAN 6 and by 2013 for the remaining 4. ASEAN has further selected seven industries as priority industries for an earlier development, namely the automobile industry, textiles, electronics, IT, medical equipments, plastic and tourism. However, the "Plus three" countries play an indispensable role in most of these industries. In addition, ASEAN's shares of export markets to China, the U.S. and Japan constitute 7.27%, 17.8% and 15.3% of its total export; whereas China's shares of export markets to ASEAN, the U.S. and Japan constitute 6.78%, 22.7% and 16.6%, respectively. Therefore, there is overlapping in export products as well as a com-

petition in export markets between ASEAN and China. Furthermore, a parallel phenomenon could be found in the area of FDI as well. Since 2000, the annual inbound FDI flow to China totalled 40 billion, whereas to ASEAN only 8 billion. China remains vivid to ASEAN both a threat and an opportunity.

### **The development levels among APT remain diverse**

Let us take the GDP of 2004 as an indicator: there was a 17-times larger disparity between the well-to-do Japan (with US\$29,400) and Myanmar (with US\$1,700). Although under the assumption of a high trade dependency and a high degree of complementariness, an expanded trade among the APT could be possible, but the needs for a structural reform and the sequencing of the reform could be unstable and taxing. The challenges ahead for the economic integration under the circumstances of cultural and linguistic diversity could be tantamount as well. From the hindsight, ASEAN's earlier insistence has its merit in that ASEAN should be the hub, whereas the "Plus Three" the spokes in the drive of the hub-and-spokes theory toward integration. This is to ensure that there will be more beneficial arrangements for the "ASEAN Plus Three" rather for the "Three Plus ASEAN", so to speak.

### **The "Plus Three" integration will come in due course, but it is not to be expected too early**

There is some similarity in the economic conditions of China, Japan and Korea, such as big-scale enterprises, strong steel industry, substantial mineral import, etc. They could easily become natural allies in certain negotiations. Currently, the three have achieved preliminary consensus on the negotiation items which will include only public finance, macro-economics, and quarantines. Compared with the other two, Japan is less forthcoming regarding the negotiations among the three, particularly dreading a detrimental consequence in negotiating the agriculture issue. Although Japan and Korea are undertaking bilateral negotiations, the progress is somewhat stalled. As to China, Japan has insisted that the time is not ripe, and that China first needs to implement her WTO commitments.

### **The proliferation of FTAs/RTAs may well mitigate the impact of the APT**

Under Article XXIV of the WTO, there is a 10-year allowance for favourite treatments under FTAs. Unless favourable conditions are well negotiated, operationalised and implemented, the expected benefits may not be accrued. There are currently 40 plus bilateral and plural FTAs, and 30 plus more under negotiation within the Asia-Pacific region. Furthermore, there are cross-continental FTAs, such as the US-Singapore, US-Australia, and Korea-Chile ones, etc. with complicated and

diverse favourite treatments, such as Rules of Origin with a “spaghetti-bowl” effect. The proposition concerning the establishment of the FTAAP (Free Trade Area of Asia Pacific), which would cover the 21 members of the APEC, was aborted last year, and may well resurface this year with some die-heart determination. All these may well cancel the originally intended outcome of the APT. However, we should note that many of the proliferating FTAs are more strategic in outlook than solid in substance. Some are meant to function as a counter-force, still others as bargaining chip against the desirable others.

The potential constraints listed above are not to be perceived as pouring cold water over the sizzling PTA, but could rather be seen as a check-list alert for making further efforts in achieving a meaningful outcome.

### **(III) The Impact of APT on Taiwan**

Taiwan has signed an FTA with Panama, a formal diplomatic ally. The actual economic benefit is minimal given the low starting base in the bilateral trade. However, the bilateral FTA symbolizes a breakthrough and a declaration in that despite China’s warning against signing the FTA with Taiwan (given Taiwan’s lack of de-jure national sovereignty), Taiwan as a WTO member should be eligible to enjoy any benefits as other members do while fulfilling her obligations.

So far, Taiwan has been unable to sign any FTAs with the APT members. Nor does it seem feasible for Taiwan to be included in the APT unless there is a major breakthrough in the cross-strait relationship. China has proposed a China-Hong Kong-Macao-Taiwan economic zone, but the “One China” principle has been getting in the way. With the consensus built between the CCP and the KMT during the KMT Party Leader Lien Zhan’s recent visit, it seems that a bilateral economic cooperation arrangement could be entertained if both could be innovative about what “One China” means.

According to the Industrial Bureau’s data, other things being equal, if Taiwan were excluded from the APT, the GDP would be reduced by 0.98%, trade conditions worsened by 1.14%, and social welfare benefits diminished by US\$4.3 billion. The total industrial productivity would plunge by US\$6.97 billion, with textile industry suffering the downturn by US\$1.95 billion, the plastic industry by US\$940 million, and the electronic industry by US\$710 million. The estimated total export would be reduced by US\$2.36 billion. Furthermore, the current Taiwan’s investment in China constitutes 74.35% of the total outward investment, and Taiwan’s trade dependency on China market has a 24% stake, the biggest share among Taiwan’s trade partners. Taiwan’s total trade with ASEAN constitutes 12.8% of the total trade, with a surplus of US\$1.9 billion. No doubt, if Taiwan is excluded from the APT, and there is no special bilateral arrangement with China or any ASEAN members, Taiwan’s economics would suffer substantively.

#### **(IV) Some Observations and Recommendations for the Evolving Cross-Strait Relations**

With the dynamic changes in policy formulation and substantive cross-strait exchanges, we should take note not only of the positive evolution but also some negative bottlenecks and potential bubbles in the continuous construct for harmonious cross-strait relations.

##### **Cross Strait Relations to adjust to a new reality**

Taiwan's cross-strait policy in general has been evolving from the "No Haste, Be Patient" to "Active Liberalization and Effective Management" after the non-partisan "Economic Development Advisory Conference (EDAC)" reached consensus in August 2001. China's cross-strait policy in general has evolved into "Tougher for the Tough, softer for the Soft", which in literal terms means being even tougher for those with an uncompromising agenda, but being even softer for those with a compromising agenda.

##### **Taiwan's Relations with "Hong Kong, China" and Macao to continue turning for the better**

With the completion of the Closer Economic Partnership Arrangement (CEPA) between Hong Kong, China and the PRC early this year, the triangular economic interactions among the PRC, "Hong Kong, China" and ROC have become most intriguing. The ROC government has initiated extensive contacts and communication with various sectors in Hong Kong and Macao to expedite exchanges and cooperation between Taiwan and these two areas. Taiwan's representative office in Hong Kong (i.e., the Hong Kong Affairs Bureau) has recently set up an office in the Chek Lap Kok Airport in Hong Kong. The measures have been revised to facilitate the entry and stay procedures for Hong Kong and Macao residents. In 2001, a Taiwan-Macao aviation pact was signed and a reciprocal aviation tax exemption agreement was extended. Taiwan is also currently conducting aviation consultations with Hong Kong.

##### **To search for the highest common denominators for mutual benefits**

The seemingly irreconcilable deadlocks of the PRC's "One China" policy or Taiwan's "Democracy First, Unification Later" requires mutual understanding and compromise. If political will exists on both sides across the strait to effect a major breakthrough in the deadlock and forge a common denominator, a "Pareto optimal"



approach would have to be in place by either postponing the issue indefinitely with own explications, respectively or targeting a timeframe for a revisit when both sides are comfortable in the course of time. "One China" or "democracy" should not be a prerequisite for any rational dialogue, all the least so when mutual understanding and domestic consensus building remain a far-fetching journey to make. Democracy, no less than the "One China" issue, requires a non-imposing, self-generating nurture and transformation from within, and could only serve as one of the experience-sharing agenda items in a matured relationship. Any pre-condition would render negotiations ill-faith and unproductive. Specific issues, such as a tariff concession on agricultural produce, tourist exchange, direct transportation links or an ICT cooperation for instance, should be charted out as a priority negotiation agenda item.

### **To forge direct bilateral dialogue without unnecessarily ambiguous messages among various parties**

Confidence-building between the relevant parties across the strait is an indispensable ingredient for a recipe to success. If the necessary ingredient is not sufficient for a dialogue, then any third party's involvement should be invited to forge a multilateral dialogue. The United States have been a long-time partner of Taiwan in economic, political and security deliberations. With the three communiqués between the U.S. and the PRC, and the "Taiwan Relations Act" between the U.S. and Taiwan, a balance is supposed to be maintained so as to ensure regional stability across the Strait. Nevertheless, in my humble view, an open dialogue between the two parties is of tantamount importance on an informal, if not on agreed-upon formal, basis. Taiwan's amendment to the Cross-Strait Act allows the granting of negotiation authorities by the government to civilian groups so as to conduct the bilateral negotiations. However, if a bilateral dialogue renders impossible in a given time, a mutually agreeable third-party or multi-parties engagements in the process should be re-considered to drive the dialogue process in a more cool-headed fashion and more constructive direction. Any indirect interpretation of a phenomenon, with or without a third party's involvement, seems worst of its kind and could create unnecessary cross-strait tensions.

### **To generate a good-will cross-strait relationship by including, not excluding, Taiwan in the regional and international organizations**

The security issue has evolved from the traditional, or more narrowly defined, national security issue to a more broadly defined human security issue. Human security covers areas of basic needs (i.e., food, shelter and health), and human dignity, and it ensures that people are free from the fear of lacking jobs, food, medical facilities, and of encountering brutal abuses. In the case of the SARS (Severe Acute

Respiratory Syndrome) in the second quarter of 2005, Taiwan revived the long-held aspiration of becoming a member of the World Health Organization (WHO). However, Taiwan encountered the PRC's strong opposition and an arrogant triumphant attitude, which in turn triggered an intensified resentful sentiment at home, and a consequential, though after all not sustainable, call for a nation-wide referendum on Taiwan's accession to the WHO. Furthermore, at the APEC Leaders' Summit in Thailand, the PRC's implicit and subtle gestures as usual further illustrated its continuous attempt in diminishing Taiwan's role with any connotation of national sovereignty, such as the dialogue among the foreign ministers in the discussion of the counter-terrorists measures, etc. Taiwan, with her significant geopolitical profile in the region, could certainly contribute to the regional security environment as a constructive partner. China's unyielding stance ought to be modified in due course so as to not further alienate Taiwanese people, whose hearts would eventually determine the future of the cross-strait relations. By inclusion, China and Taiwan would stand to win in the non-zero-sum game; by exclusion, China and Taiwan would both lose in the zero-sum game in the long run, although some short-sighted viewers may maintain that China wins with continuous suppression of Taiwan's international profile.