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Taiwan and the People's Republic of China Foes or Partners?

by Axel J. Halbach, Munich *

Taiwan is developing ever more perceptibly into what both Peking and Taipei consider it to be: a province of China, albeit a province sui generis — part of China and yet an independent state, enjoying world-wide recognition though denied diplomatic relations, a leading commercial power but without proper commercial treaties. The prosperity which has been generated in the island is an ever present temptation for the People's Republic. Is it tempting enough to provoke an appeal to arms? Or is Red China's perfectly legitimate interest directed primarily at the exchange of goods and technologies?

Many columns have been filled in the newspapers during recent weeks in an attempt to find an answer to these questions and scholarly analyses will no doubt follow soon. The consensus of opinion among commentators, however disparate their starting points, is that a step-by-step rapprochement between the two Chinas is for a variety of reasons more likely than an armed conflict. That the present interest of the PR China in Taiwan is predominantly economic and to a lesser degree military is not in doubt. Even in the turbulent sixties when Peking could on several occasions — for instance in 1962, when the famine in southern China caused a heavy influx of Chinese into the territory of Hongkong, and again in 1967, during the excesses of the Cultural Revolution — have gained control of the administration of Hongkong without running a great international risk, Peking let its opportunities slip. Back in 1967 Lisbon had offered to enter into negotiations with the Chinese Government on ways of divesting itself, without loss of face, of its responsibility for Macao — but China declined. The persistence in the status quo of the prosperous colonial enclaves right on its doorstep evidences that these territories were even in those days more important to China as gateways to the world than their possible incorporation into the own dominion. Could not similar considerations apply to Taiwan as a prosperous free trade zone with its security guaranteed by Peking and under the latter's foreign-political control, possibly conjointly with the USA?

* Ifo-Institut für Wirtschaftsforschung. A longer version of this article, in German, can be found in: Ifo Schnelldienst, 8/79, p. 13 ff.

¹ Further information about mainland China's development concept will be found in Hans-Gert Braun, Die wirtschaftliche Öffnung Chinas — ihr entwicklungstheoretischer Hintergrund (The economic opening of China — the development theoretical background), in: Ifo Schnelldienst, 1/79, p. 5 ff.

From the viewpoint of the present leadership in Peking this question is certainly to be answered in the affirmative. Taiwan's economic potential as it presents itself today and its potential importance for the economic advancement of the People's Republic will be discussed in the following sections.

Development Concept and Economic Growth

The National Chinese Government in Taiwan has always aimed at an essentially market-economic order and liberal economic policy and allowed as much scope as at all possible to private initiative. Private ownership of the means of production and free competition are safeguarded in Taiwan. Foreign investments are encouraged by the authorities to the best of their ability and may be made without native private or public capital participation. Only in the infrastructural sphere and in certain strategically important sectors of the economy which cannot be developed adequately by other means (especially iron and steel, non-ferrous metals, petrochemicals, energy) does the state operate as an investor. This policy has brought about a marked change in the role of the state in the industrial growth process which was from an early stage the salient feature of the island's economic development and prosperity. Despite the active role of the state in industrial planning the public sector's share in industrial production — 57 % in 1952 — has been dwindling continually; by 1977 it was down to just below 20 %.

The development model of Red China¹ was, in contrast, from the outset based on central planning and direction of the economy to which the two

rivalling guidelines — evolution of a socialist mentality (according to the Maoist concept) and productivity orientation (Liuist concept) — were both subordinated. The central planning was twinned with strong pressure to conform and considerable restrictions on choice of jobs and movement inside the country. The modern part of the economy of the People's Republic was transferred step by step to state ownership, a process which was completed without exception by 1956. The effective influence of the state on the economy, however, extends far beyond the modern sector. Leaving aside the question whether the 900 million mainland Chinese could ever have been economically mobilized in a relatively short span of time by similar methods as applied with convincing success by the 17 million inhabitants of the island, these opposite development strategies alone were bound to lead to disparate economic results. Starting with a highly constructive land reform which did not eradicate but gradually enlarged the agricultural, industrial and commercial middle class until the whole of the populace had in the end been "bourgeoisized", the production potential of the island experienced an exemplary upsurge. In the early years US capital certainly helped to achieve this result; by 1965, when the US economic aid came to an end, a total of \$ 1.4 bn had been provided as capital aid in addition to \$ 2.5 bn of purely military aid. The successes from that time onwards at the latest are however to be attributed overwhelmingly to the proficiency of the Chinese population which was reflected not least in the fact that a favourable investment climate and the existence of financial incentives made the island ever more attractive for foreign private capital. By 1965 the foreign direct investments in Taiwan still totalled no more than \$

100 mn; in the years since they have made up amply for the discontinuation of US economic aid. By the end of 1978 the authorized foreign investments had climbed to \$ 1.9 bn. The new foreign investments now average about \$ 200 mn a year. More than three quarters of all foreign investments to date have gone into industry, 5 % into building and close on 20 % into the services sector. Expatriate Chinese are prominent in the building and services sectors while most of the industrial investments were made by US, Japanese and — lately — also European firms.

The positive effect of these foreign investments does not however downgrade the work performance and entrepreneurial talents of the Chinese themselves in any way. They are not only respected but feared in neighbouring countries because of these qualities. Their intuition and their gift of improvisation are unsurpassed. So is the high discipline of the workers, their quick grasp, diligence and willingness to learn, and these are assets which foreign investors appreciate. They explain the magnitude of Taiwan's achievements.

Taiwan has set itself the target of accomplishing the transition from a developing country with poor raw material resources to a modern industrial state in the early eighties. All the present evidence suggests that its objective will be achieved. In the years from 1965 to 1978 its real gross domestic product (GDP) rose on average by 9 % (the nominal rate was 16.6 %). This unusually high rate over as long a period as 13 years is all the more remarkable as the island had in 1965 already attained a degree of industrialization which was outstanding among developing countries and had no natural resources to aid such rapid growth.

Table 1

The Gross Domestic Product of Taiwan and the People's Republic of China: Composition and Growth

Sector of economy	Taiwan				People's Republic of China ²			
	NT\$ bn 1965	%	NT\$ bn 1978 ¹	%	Y bn 1965	%	Y bn 1974	%
Agriculture and forestry	26.6	23.7	89.0	10.6	49.1	32.6	67.1	25.2
Mining	2.1	1.8	8.6	1.0	64.6	42.9	138.8	52.1
Manufacturing industry	29.1	25.6	330.0	39.4				
Electricity, Gas, Water	2.4	2.1	23.0	2.7				
Building	4.5	3.9	40.2	4.8	8.0	5.3	14.0	5.2
Wholesale and retail trade	16.8	14.8	86.8	10.4	28.9	19.2	46.4	17.4
Transport and traffic	6.0	5.3	50.4	6.0				
Miscellaneous	26.2	23.1	210.0	25.1				
Total	113.7	100.0	838.0	100.0	150.6	100.0	266.2	100.0
Per-capita income in US\$	205		1,304		95		410 ³	

¹ at 1977 prices; ² at 1957 prices; ³ in 1976, according to World Bank calculations — Taiwan puts the mainland per-capita income in 1978 at \$ 198 only.

Note: US\$ 1 corresponds to NT\$ 40 (in 1965) and NT\$ 38 (in 1977); Y 1 about DM 1.20.

Sources for Taiwan: Statistical Yearbook of China, 1977; Monthly Bulletin of Statistics, 1978; Industry of Free China, 1978.

Source for P.R. China: Ulrich Menzel, Theorie und Praxis des chinesischen Entwicklungsmodells (Theory and practice of the Chinese development model), Opladen 1978, p. 620.

While the originally dominant agricultural sector which in 1952 still provided 32 % of GDP had by 1978 fallen back to less than 11 % (cf. Table 1)², the manufacturing industry has become the most important sector by far of the economy. In the ten years from 1967 to 1977 the industrial output increased at a real annual rate of nearly 15 %. Its contribution to GDP rose from no more than 15 % (in 1952) to 39 % in 1978 and will exceed 40 % in the coming years. The GDP contribution of the secondary sector as a whole has in consequence advanced from less than 32 % in 1965 to 47 % (in 1978) while the primary sector underwent over the same period a relative decline from 25 % to less than 12 %.

The growth potential of the island economy is even greater than appears from the average figures achieved up to 1978, for the pace of advance has varied greatly as a result of the oil crisis and the world recession following it. From 1965 to 1973 the annual growth rate was over 10 %. In 1974 it plummeted to 0.6 %, and in 1975 it amounted to 3.1 %. It was only in subsequent years that the earlier trend rate was resumed; 1978 proved an exceptionally good year for Taiwan: the real expansion by 12.8 % was the highest in 30 years, and the expectations for growth in the future are not significantly lower. Official forecasts assume a real expansion rate of about 9 % a year up to 1985, based largely on progress in the secondary and tertiary sectors.

With a per-capita income of US\$ 1,300 (in 1978) Taiwan no longer belongs to the group of developing countries proper although its economic strength cannot of course as yet be gauged by European standards; its gross domestic product of \$ 23 bn (about DM 42 bn) in 1978 was similar to the social product of Berlin (West). But compared with the People's Republic there is a very wide relative difference. Although Taiwan set out from a rather less favourable position, the People's Republic had, according to World Bank calculations, in 1976 a per-capita income of \$ 410 (cf. Table 1) whereas Taiwan's was already \$ 1,020. Another source estimates the per-capita income of the PR China (also in 1976) at no more than \$ 340 with a GDP at current prices of \$ 324 bn³.

² It is to be noted in regard to this table and other statistical comparisons in this article that the national accounting system of the PR China not only differs on many essential points from Western methods of calculation but is based on sporadic and sometimes contradictory data published by Peking. The figures given in this article are based on careful analyses and estimates by Western economists. That their calculations give — in part widely — differing results is shown by a publication of the Bundesinstitut für ostwissenschaftliche und internationale Studien (Federal Institute for Eastern and International Studies) (cf. Werner Klatt, *China's National Accounts — as seen by Western Analysts*, Cologne, December 1978).

³ Cf. Werner Klatt, *ibid.*, p. 41 f. Such differences between the various estimates are mainly due to different assumptions about population numbers. Even official planning documents of Red Chinese authorities indicate differences of up to 100 millions.

Taiwan puts the per-capita income in mainland China for 1978 as low as \$ 198⁴.

At a first glance the two states do not seem to differ profoundly in economic structure. In mainland China the GDP contribution of agriculture has also been receding since 1965 while the secondary sector is of increasing importance. But in Red China agriculture still accounts for more than twice as large a share of GDP as in Taiwan, and its relative decline is proceeding at a significantly slower pace. In Taiwan one in three of all inhabitants is still living in the countryside and earning his livelihood in agriculture; in mainland China four out of five do so. The high share of industrial value added — 52 % in the People's Republic compared with 42 % in Taiwan — is deceptive as a not unsubstantial part of the 52 % is made up of raw materials (mineral oil, coal, iron ore, non-ferrous metals) which are not shown separately whereas the 42 % of Taiwan with its poor raw material resources represent only the output of manufacturing industry including energy generation. At what prices the raw materials produced in Red China are valued in the statistics is not known so that it is unfortunately impossible to give a reliable estimate of their share of the 52 % of industrial production recorded by the PR China. Included in it were 470 mn tonnes of coal (in 1975), 90 mn tonnes of mineral oil (in 1976), 32 mn tonnes of iron ore (in 1975) and 34 mn tonnes of phosphates (also in 1975). These figures suggest that the share of raw materials was fairly substantial. The building sector made an almost equal relative contribution to GDP in the two Chinese states but in the tertiary (services) sector there were considerable differences although methodological problems make a comparison virtually impossible. The communist states have always objected to the western system of national product computation. Only goods and services which are regarded as productive are as a rule counted as part of the GDP. Any activity which does not contribute directly to the material output — for instance, various services of a personal, professional or public nature (incl. defence) — are termed unproductive. Many figures have to be estimated or readapted to allow a meaningful comparison with western data.

The general economic development on the mainland also proceeded in investment cycles, as well as production cycles, which however were due to other causes than the cyclical growth of Taiwan which was dominated by its dependence upon the world economy. The PR China regained the pre-war level of production about 1955 (Taiwan in 1952). Thereafter followed four five-year plans in

⁴ According to a report by the Central News Agency, Taipei, dated February 1979.

succession but these were held back time and again by crop failures, the suspension of Soviet aid and the Cultural Revolution and became less and less relevant as planning instruments. In the end there was very little point in speaking of plan fulfilment — in sharp contrast to the indicative planning in Taiwan where the actual plan fulfillment rate often exceeded 100 %. The last complete cycle ended in 1974 together with the fourth five-year plan period. A ten-year plan for the modernization of China was adopted in 1976; it envisages the completion of 120 major projects (including ten iron and steel works, nine non-ferrous metal plants, nine new coal mines, the opening of ten new oilfields and the construction of 30 power stations; besides, the long-distance rail network is to be greatly extended, and five new big ports are to be built). This plan forms part of what is known as the Four Modernizations (agriculture, industry, defence, and science and technology) which are to transform the PR China by the year 2000 into a modern industrial state. The People's Republic is not badly placed for such an effort. Mainland China has already a relatively comprehensive industrial system; although its production is oriented exclusively to the domestic market, it could no doubt be rapidly extended. The population is intelligent; illiteracy is almost unknown. The backwardness of agriculture is at present still most noticeable but the plan provides for the mechanization of 85 % of the principal working processes in agriculture by 1985.

The average rate of economic growth in the PR China in the ten years from 1965 to 1975 is put at 6–6.5 %. Agriculture expanded at an annual rate of about 3 %, industry (incl. mining and building) at 8.5 % and the services at 6.5 %. In 1976 the economic growth was at a standstill, and for 1977 no details have as yet become known, but remarks by the party chief Hua Kuo-feng signified a definite leap forward in 1978: the industrial production rose in that year by 12 % over the preceding year; the plan target of 30 mn tonnes for crude steel was attained in early December already⁵; the crude oil output rose by 11 % to 105 mn tonnes, coal to 600 mn tonnes and energy by about 14 %. Like the unusually fast economic growth in Taiwan, this short-term increase last year was essentially due to better utilization of existing capacities rather than to capacity extensions which however will from now on be needed to ensure future growth.

For this reason it is impossible to deduce the long-term prospects for mainland China from the exceptionally positive results of 1978. The GDP is planned to grow by about 8 % annually between 1975 and 1985. The steel output is to be raised to 60 mn tonnes, the production of grains from 280

to 400 mn tonnes. The planned growth rate seems unduly high however — not only in relation to past achievements. Various calculations indicate a long-term growth potential of no more than 6–6.5 % per annum — exactly the same rate as hitherto. One important reason for this assumption of slower growth than planned is that experts regard the planned investment ratio of 25–30 % of GDP as virtually unattainable. In Taiwan such a ratio has been achieved regularly year after year since 1972. Industry is expected to expand fastest in the People's Republic — at about 8 % a year — while the estimate for agriculture is 2–2.5 % and for the services sector 4 %. The targets of 10 and 4 % set in the ten-year plan for industry and agriculture are markedly higher than these estimates.

A direct economic comparison of the two Chinas shows up the fact that although the production of the PR China is of course much larger in actual volume (\$ 324 bn as against \$ 17 bn — both in 1976), its economy is far less dynamic than that of Taiwan. Its overall economic growth was about one-third lower, and in the industrial sector which is of special relevance for the modernization process the growth rate on the mainland was only a little more than half of that in the island. The per-capita income in the People's Republic was — as shown by various computations — one-fifth to at most one-third of that in Taiwan. There is a great deal of evidence to suggest that there will not be much change in this respect in the future.

The structural changes are thus proceeding much more slowly in mainland China than in Taiwan. It is unlikely that the island could improve the food supply on the mainland in the event of affiliation but its industry would possibly make a substantial contribution by complementing the industrial structure of Red China. This aspect will therefore now be discussed in a little more detail.

Industrial Structure and Industrialization Strategy

It was only after the second world war that Taiwan set about the independent establishment of a manufacturing industry⁶. Four phases of industrial development can be marked out in the postwar period. In the first phase — from 1945 till 1952 — the focus was on the rebuilding of the strategically important industries (energy, fertilizers, textiles) 75 % of which had been destroyed in the war. The feature of the next phase — from 1953 till 1960 — was the swift expansion of consumer goods production on a basis of import substitution

⁵ Large quantities of steel (about 12 mn tonnes) had nevertheless to be imported.

⁶ Cf. Werner H. Strigel, *Industrialisierungserfolge in Taiwan* (Industrialization successes in Taiwan), in: Ifo Schnelldienst, No. 22/1978.

and light industry with special attention to food processing and textiles. The foundations were laid at the same time for a number of industrial enterprises which were to determine the dynamism of Taiwan's industry in the following third phase — from 1963 till 1975 — which was export-oriented and laid stress on industrial modernization and erection of basic and technology-intensive plants. The electrical and electronic industry developed during this period into the dominant industry; the chemical, petrochemical, mechanical engineering, ceramic and plastics industries and wood and paper processing also surged ahead while the textile industry continued to expand. The fourth and so far last phase opened in 1976. It is to transform Taiwan in a few years into a modern industrial state with a high degree of inter-industrial integration. Priority is being given to the establishment of capital- and technology-intensive heavy industries to replace imported supplies to domestic manufacturers and also to engage in exports. The (precision) engineering and vehicle industries, metal processing, the production of chemicals and petrochemicals, the basic industries (iron and steel, non-ferrous metals) and the electrical engineering sector are to receive special promotion.

Table 2
Gross Industrial Production of Taiwan,
by Industries

Industry	1967		1977	
	NT\$ bn	%	NT\$ bn	%
1. Food, drinks and tobacco	18.3	22.5	66.4	10.5
2. Textiles, clothing, leather	15.1	18.5	142.9	22.7
3. Wood processing and manufacture	3.6	4.4	16.9	2.7
4. Paper and printing	4.0	4.9	21.6	3.4
5. Chemical industry, mineral oil, coal, rubber and plastics processing	17.2	21.1	190.3	30.2
6. Fine ceramics, glass, stones, earthenware	5.7	7.0	24.0	3.8
7. Metallurgy	4.0	4.9	28.1	4.5
8. Metal goods, machinery, vehicles	13.1	16.1	135.3	21.5
9. Miscellaneous manufactures	0.5	0.6	4.0	0.7
Total	81.5	100.0	629.5	100.0

Source: Industry of Free China, Vol. 49, No. 5, May 1978; calculation by the Ifo-Institut.

The structure and growth of industrial production in Taiwan over the ten years from 1967 to 1977 are shown in Table 2 (comparable data for the PR China are unfortunately not available): The share of light industry (groups 1–4, 6, 9) has declined from 58 to 44 % of total industrial production while the importance of the so-called heavy industries increased correspondingly. The output of chemicals, petrochemicals, mechanical engineering products and electronics rose above the average. The real rate of industrial growth was almost 15 % a year; in 1978 it came close to 20 %.

An average real growth rate of approximately 13 % is forecast for Taiwan's industry in the years from 1977 to 1985, and this will result in further shifts in the weight of particular industries. Although the output volume of the light industries is to rise by about 160 %, their share of the industrial production is to fall further — to 30 % — which will strengthen the preponderance of the heavy industries — scheduled to contribute 70 %. In the light of experience these plan figures look quite realistic.

As mentioned earlier, the state has been playing a less and less important entrepreneurial role in the industrial sector during recent years. By 1977 the share of the public sector was down to barely 20 % of industrial production while foreign firms accounted for about 17 % (in 1976). The state-owned enterprises are confining themselves in the main to the strategically important sectors of energy generation and oil processing (refineries, petrochemicals) and a few sections of basic industry (iron and steel, aluminium, fertilizers, phosphates). Shipbuilding and a small section of the mechanical engineering industry have been added to these of late. All other industries are dominated by private enterprise.

The significance of the industrial development in Taiwan cannot be properly appreciated without consideration of the actual output figures involved as exemplified in Table 3. Although in no way representative, they may give some idea of the level of production achieved to date. A direct comparison with the PR China was unfortunately only in a very few instances possible but, as far as the comparison goes, it shows clearly that Taiwan was practically all along the line far ahead in relation to the size of its population. The difference is particularly striking in the generation of energy which may be regarded as a good indicator of overall economic activity. It amounted in 1976 to 27 bn kWh in Taiwan and to 131 bn kWh in the PR China; mainland China with 50 times as many inhabitants as Taiwan had not quite five times as much electricity. For 1978 National China calculated the island's per-capita energy supply at 2,022 kWh, against no more than 150 kWh on the mainland.

Before these figures are considered, it seems advisable to review the phases of the industrialization in Red China in order to pinpoint similarities and differences between the two Chinas. The first phase of industrialization on the mainland began with the inauguration of the first five-year plan (in 1953). It was marked by the forced development of the coal and steel industries and certain sections of the mechanical engineering industry. The second wave of industrialization got

Table 3
Production of Selected Industrial Products in
Taiwan and in the PR China

Product	Unit	Taiwan 1977	PR China 1974
Sugar	mn tonnes	1.0	4.0 ²
Cotton fabrics	mn metres	1,361	7,600
Cotton and synthetic yarns	1,000 tonnes	400	.
Shirts and trousers	mn	618	.
Synthetic fibres	1,000 tonnes	544	.
Umbrellas	mn	34	.
Leather shoes	mn pairs	5.1	.
Tires and inner tubes	mn	75	.
Paper and cardboard	mn tonnes	1.0	6.0
Cement	mn tonnes	11.5 ¹	37.3 ²
Fertilizers	mn tonnes	1.8	39.9 ³
Iron and steel	mn tonnes	2.6 ¹	29.0 ²
Motor engines	1,000	703	.
Sewing-machines	mn	1.5	.
Cameras	mn	1.6	.
Tape recorders	mn	3.6	.
Television sets	mn	7.0 ¹	.
Digital watches	mn	10.0 ¹	.
Electronic calculators	mn	7.0 ¹	.
Automobiles	1,000	80 ¹	.
Motor cycles	1,000	600 ¹	.
Bicycles	mn	2.0	.
Tractors	1,000	.	133 ³
Electric energy	bn kWh	34.4	131.0 ³

¹ 1978; ² 1975; ³ 1976.

Sources: Industry of Free China, Vol. 49, No. 5, May 1978; CNA Newsletter, February 1979; OECD, Science and Technology in the People's Republic of China, Paris 1977, p. 187; DIW-Wochenbericht 15/1977, p. 126 ff; UN Statistical Yearbook for Asia and the Pacific, 1977.

under way about 1965 and lasted until 1975 — for the whole of the third and fourth five-year plan periods. Special attention was paid to the growth of the mineral oil, chemical and petrochemical industries (especially fertilizers and artificial fibres) as well as agricultural machinery and mechanical equipment (tractors, irrigation, machines for making fertilizers). The special feature of this second industrialization phase was that it was accomplished largely with China's own resources. The deliveries by the USSR and other socialist countries were tapered off, and the imports from western countries carried relatively little weight. The start of the fifth five-year plan (1976–1980) marked the opening of a third phase of industrialization about which provisional data only can so far be given. To go by the rapidly increasing imports of complete industrial plants from the OECD area, petrochemicals and plastics in particular are now to the fore. Electronics and second-generation steelworks seem to be other key areas; the investments in these fields do not only serve an extension of capacity but suggest a shift to special high-quality steels and steel processing. The fifth plan thus gives once more the priority to heavy industry and the production of investment goods, linking thus up with the plan-

ning objectives of the fifties when the Soviet example of forced industrialization in the thirties still held sway.

These steps towards industrialization have brought about a decisive transformation of the industrial structure on the mainland. In 1933 73 % of China's industrial production was still supplied by the consumer goods industry, and textiles and food, drinks and tobacco still accounted for two-thirds of it. The metallurgical, metal processing and machinery industries generated no more than 5 % of the industrial value added. In 1952 the light industry was still supplying close on 65 % of the entire industrial output. By 1973 the investment goods or heavy industry had however finally overtaken the consumer goods industry by providing 60 % of the total.

The contrast between a predominantly private-enterprise consumer-oriented industrialization policy (in Taiwan) and one that is state-directed and investment-oriented (as in the PR China) is reflected by the marked differences in the weighting of industrial investments in the early years. At the present time both strategies are, however, pointing in almost the same direction. Both Chinas are giving priority to petrochemicals, metal processing, mechanical engineering and electronics, and the differences in the rating of light and heavy industries have faded. Considerable differences in the supplies available to the population are however shown to exist by the figures relating to the actual level of production (Tables 1 and 3) rather than the proportional figures. While the heavy industry in Taiwan merely complements an existing relatively comprehensive consumer goods industry which meets a fairly substantial part of the world demand for certain products in addition to comparatively exacting requirements of the domestic population, the consumer goods industry in Red China has no other aim than that of covering, at best, the mostly undiversified minimum needs of the 900 million inhabitants.

This fact is regarded by some writers as posing a serious threat to the liberalization tendencies perceivable at present. The backlog of unsatisfied requirements is so huge and the expectations of the 900 million Chinese have risen so much compared with previous years that it will be impossible to harmonize the resultant demand with the effects of forced heavy industrialization. Effective inhibition of present consumption is a prerequisite of concentration on the investment goods sector. The output figures which have become known for 1978 do indicate that the light industries have increased their production of consumer goods, in part substantially. These successes however stem almost entirely from higher capacity loading and

better work organization and cannot be repeated or maintained in coming years without creation of new capacities. The Red Chinese planning focuses however on investments in the capital goods sector.

This example shows – as do many others – that an industrialization left mainly to the working of private initiative will at first build upon consumer demand, which can be mobilized easily, and such a strategy is also pursued most easily with the know-how which the workforce already possesses or can be given by brief training; diversification into investment goods areas will follow later when the manpower potential and growth of demand allow it. In state-planned industrialization on the other hand priority is given to the investment goods sector to the neglect of individual needs. Hence there exists a danger – according to a current thesis – that as soon as the wider horizon of expectations and pressure of demand resulting from internal liberalization comes in conflict with the economic planning objectives, the liberalization will be stopped or countermanded ⁷.

Table 4
The Foreign Trade of Taiwan and the People's Republic of China in Comparison
(in \$ mn)

Year	Taiwan			People's Republic of China		
	Exports	Imports	Surplus/ Deficit	Exports	Imports	Surplus/ Deficit
1970	1,481	1,524	– 43	2,090	2,240	– 150
1972	2,988	2,514	+ 474	3,090	2,790	+ 300
1974	5,639	6,966	– 1,327	6,250	7,300	– 1,050
1976	8,166	7,599	+ 567	7,080	6,480	+ 600
1977	9,361	8,511	+ 850	7,840	6,450	+ 1,390
1978	12,705	11,022	+ 1,683	a	a	

^a The total trade in both directions is estimated at \$ 17 bn and, by another source, \$ 20 bn (cf. *Süddeutsche Zeitung* of Jan. 8, 1979 and *Mitteilungen der Dresdner Bank*, No. 4, 1979).

Sources: Taiwan Statistical Data Book 1978; CNA Newsletter No. 4, January 1979; *DIN Wochenbericht* No. 25/1977.

This conclusion is not unjustified and shows that the West has good political reasons to assist the PR China, irrespective of the far-reaching commercial expectations. It would be most unfortunate if the pragmatists were to lose control because of lack of economic success. The present leaders in mainland China seem to see things in a similar light. They want know-how and training most of all – the Cultural Revolution has deprived the People's Republic of an entire generation of technicians and competent managers – but they seem increasingly to be giving up their fundamental objections to foreign production plants. Two models are currently under discussion as possible

forms of industrial cooperation. One is the usual joint-venture enterprise with foreign capital participation of up to 25 %; in dispute is here still whether and in what form profit transfers abroad are to be permitted. Another model which is already being practically applied by Chinese from Hongkong is that a foreign entrepreneur invests and imports capital, machinery and equipment while the People's Republic provides the site for the plant as well as the manual and non-manual labour. The remuneration of the workers is settled by a contract with the Chinese Government which apportions the wages to them. During the contract period – of three to five years from the start of production – all profits go to the investor whose capital is repaid by the Government in yearly instalments over the same period. When the contract has run its course, the plant becomes the property of the PR China.

There is no doubt that the consumer expectations of the mainland Chinese could be met most efficiently (while simultaneously pursuing planning objectives of a different nature) by at least partial use of Taiwan's production potential for the PR China. The output figures given in Table 3 by way of illustration indicate to what extent Taiwan is already producing for the world market; 90 % of the production of textiles, 80 % of wood processing, 76 % of the electronics and 64 % of the mechanical engineering output are already being exported, and these are only a few examples. There is in effect no single industry in Taiwan which does not engage in exports, and most of them are sending nearly 50 % or more of their output abroad. The paper, printing and metallurgical industries are the only ones with a relatively low export ratio. In some products – especially textiles and electronics – Taiwan is now, owing to increasing protectionist tendencies in the world market, coming up against certain sales limits; if the Chinese mainland market were opened, these would become immaterial.

The attraction of such cooperation for Red China would be that not only could Chinese requirements be satisfied but it could be done without additional foreign currency outlays. It has been made clear by Red Chinese circles that possible commercial dealings with Taiwan would not be viewed as normal foreign trade transactions but as intra-Chinese trade exchanges. Taiwan in turn could obtain the raw materials it needs in large part (crude oil, iron ore, non-ferrous metals, etc.) without spending foreign currencies. The People's Republic will have in effect no fundamental interest in impairing Taiwan's export potential by tying its capacities too tightly to the mainland. More important than the production potential of the island is for mainland China the foreign currency

⁷ Cf. Hans-Bernd Schäfer, *Einige Probleme der neuen chinesischen Industrialisierungsstrategie* (Some problems of the new Chinese industrialization strategy), in: *Vierteljahresberichte*, No. 74, 1978, p. 275 ff.

surplus which could be brought in by Taiwan in the event of affiliation. This aspect will be discussed in greater detail in the next section.

Foreign Trade and External Dependence

The most easily perceptible effect of the opposite development strategies on the mainland on the one hand and in the island on the other is the different degree of economic integration with the world market⁸. Although Taiwan is geographically a midget compared with the People's Republic, its foreign trade volume was in 1977 25% higher than that of mainland China; in 1978 the margin was, according to provisional data, almost 40%⁹. Such substantial differences are bound to cause surprise unless the autocentric development of the PR China is seen as an attempt to go its own way as far as at all possible, without depending upon the rest of the world.

Taiwan followed an exactly opposite way. Political motives always played a great role in its external economic relations; the foreign trade was part of foreign policy. The exchange of goods with other

countries is proving an increasingly useful instrument for demonstrating through merchandise exports the success of Taiwan's own policy and economic set-up on the one hand and for involving foreign interests through large imports and thus spiking the diplomatic blockade. However, it is not only for political, but for purely economic reasons that Taiwan depends more than any other country upon a flourishing foreign trade. The scantiness of its indigenous raw materials, the relatively small population, a high and rising level of industrialization in conjunction with above-average standards of education and advancing consumer demands from the workforce make steadily growing exchanges of goods with other countries imperative. The increasing political isolation since the admission of the PR China to the UN has not impeded the consistent extension of Taiwan's international trade relations. Taipei has, it is true, had to resort to a multitude of ad hoc solutions and provisional arrangements to make up for the lack of diplomatic relations and this has given rise to a highly complex and fragmented foreign trade organization, but this did not really interfere with trade as such. Taiwan is currently maintaining trade relations with 140 states; countries with which it has no diplomatic relations in 1977 accounted for 44.6% (in 1975 59.3%) of its exports and (in 1978) 68.4% (in 1975 66.7%) of its imports.

⁸ Cf. also Anton G ä l l i , Außenhandel der VR China und Taiwans — ein Systemvergleich (The foreign trade of the PR China and Taiwan — a comparison of two systems), in: Ifo Schnelldienst, No. 31, 1976.

⁹ The total foreign trade volume of the People's Republic in 1978 is estimated at \$ 17 bn.

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V E R L A G W E L T A R C H I V G M B H - H A M B U R G

The PR China regarded the foreign trade — emergency purchases (especially of grains) apart — chiefly as a means of technology transfers and a contribution to the industrial development of the country¹⁰. After the ending of the massive Soviet investment aid in the fifties China needed above all Western investment goods for the establishment of an autarkic economy. Both these aspects — technology transfer and industrial development — are at present again coming very clearly to the fore. Table 4 shows the development of the foreign trade of the two Chinas since 1970.

The foreign trade of the PR China quadrupled in dollar terms in this period; Taiwan's trade expanded twice as fast. Unlike the People's Republic which adheres strictly to the principle of covering imports by an equivalent amount of exports — a trade deficit was quickly expunged by drastic import cuts in subsequent years — Taiwan has been operating with growing export surpluses since 1971; only in 1974, after the oil price rises, was the surplus for once replaced by a deficit. By 1978 Taiwan's foreign trade had risen to nearly \$ 24 bn; by 1981 it is planned to reach \$ 38 bn (at constant prices). The structural trade surplus may be expected to rise further in absolute figures, though less quickly than hitherto because greater efforts are being made to bring in more imports. The growth rate will exceed 20 % on the export side and may be about 18 % a year on the import side. The export ratio¹¹ came close to 48 % in 1977 and rose to about 54 % in 1978, an especially successful year for Taiwan's exporters. How little in comparison the mainland economy depends on the outside world is indicated by the export ratio of 2.2 % recorded by the PR China (for 1976). Taiwan's exports and imports together exceeded the island's GDP (in 1978); in the PR China they amounted to no more than 4.2 % of GDP (in 1976).

The ratio is however likely to increase notably in consequence of the reorientation of Red China's economic policy. In 1978 alone the volume of foreign trade is thought to have risen by 15–20 %. Although the foreign trade is in principle to be expanded primarily by increasing exports, there is today evidently a greater readiness to incur medium-term debts and accept long-term credits in order to get closer to the objective of the Four Modernizations. The potential for trade expansion must not be overrated however because of the spectacular business deals and statements of intent reported recently. The absorptive capacity for imports is limited, not least because there are not enough technical experts and skilled workers to

assimilate the foreign technology at the desired pace. Those who know mainland China regard an expansion rate of more than about 15 % per annum from 1978 to 1985 as unrealistic.

The salient feature brought out by a comparison of the categories of goods traded by the two Chinese states is the preponderance of industrial products in the export trade of Taiwan. In 1978 they amounted to 89 % of all exports; including processed agricultural products they reached 95 %. Other agricultural exports provided the remaining 5 %.

The exports from the People's Republic are also marked by a slow relative increase of semi-finished and finished goods. Raw materials (incl. mineral fuels) and foodstuffs, etc., were another important source of export earnings however. These two groups together supplied in 1975 nearly half of all exports; chemical products, machines and vehicles accounted for 9 % and semi-finished and finished goods for 43 % (almost half of which were textiles, yarns and fabrics). The most important export articles of mainland China — textiles, agricultural produce, coal and paraffinic oils — are only of limited interest to Europe. The People's Republic possesses however rich mineral deposits; given increased exploration and exploitation, non-ferrous metals could occupy an important position in its balance of trade, and a marked increase of raw material exports may in any case be expected in the coming years. About 10 mn tonnes of mineral oils are currently exported each year; by 1985 this figure is to be raised to 25 mn tonnes.

Of the imports into Red China about 10 % are at present foodstuffs (chiefly grains though their share fluctuates widely according to the country's own crop results). Most of the imports — about 80 % — consist of chemical products, machines, vehicles, semi-finished and finished goods. The next few years will undoubtedly bring further increases; light industry products in particular will also be imported on a larger scale. The general raising of wage rates and the introduction of bonus payments have given the mainland Chinese more purchasing power while the supply of goods is certainly not abundant. Besides, import duties of 20 to 200 % make the importation of luxury goods such as radio receivers, cameras, television sets and cosmetics a very profitable source of revenue for the state. Cooperation with Taiwan would therefore offer special advantages in this field. Taiwan's declared intention of stepping up the exports of investment goods in the future also fits in with Red China's requirements.

The composition of Taiwan's imports is determined chiefly by the growing raw material require-

¹⁰ No fewer than 156 complete plants were imported from OECD countries between 1972 and 1976.

¹¹ Exports in relation to GDP.

ments of the industry in the island and secondly by the nutritional needs of its growing population; only about 85 % is at present covered by local production. Agricultural and industrial raw materials are therefore the major imports, accounting for over two-thirds of the total. The People's Republic could in theory supply a considerable part of these. Taiwan's imports of investment goods have fallen off slightly in recent years — from 30 % to at present 25 % — while the imports of raw materials have risen correspondingly; consumer goods account for no more than 7 %; they have been virtually unchanged for a number of years.

Taiwan's major trading partner is the USA; with 39 % of all exports and 22 % of imports it ranked first and second respectively in 1978. The bilateral balance of trade with the USA has been in surplus since the late sixties. The pattern of trade with Japan is the opposite; it is Taiwan's most important supplier (33 % in 1978) but ranks second as a customer (12.5 %). Japan is traditionally also the most important foreign trade partner of the People's Republic. It accounted for over 30 % of mainland China's trade in 1977; more than half of that was made up of Japanese steel and Chinese oil. Second in importance as a trade partner of mainland China was Hongkong; 16 % of the Red Chinese trade in 1977 passed through the Crown Colony — mainly from the People's Republic to other countries while the exports and re-exports from Hongkong to the mainland amounted only to a little under \$ 60 mn. The Federal Republic of Germany ranked third in 1977 (as in previous years) with about 7 %. With communist countries the Chinese conducted only 15 % of their foreign trade.

The mainland trade with Taiwan is not shown in the official statistics at all but trade exchanges are certainly already taking place. Taiwan received mainland goods via Hongkong equivalent to almost DM 60 mn in 1977 and DM 50 mn in the first half of 1978; spices, Chinese medicaments, certain earths for making porcelain and other basic materials were the main items. There is still very little trading in the opposite direction, at least via Hongkong. Goods made in Taiwan probably play a larger role in the mainland imports from Japan, for Japanese firms are well represented in Taiwan's three "export processing zones". Red China is currently showing itself greatly interested in normal trade exchanges with Taiwan. A spokesman for the Trade Ministry of the People's Republic recently voiced again the hope that close contacts would soon be established with industrial and commercial circles in Taiwan.

Beside the possibility of buying consumer goods at advantageous prices, mainland China's interest

in close affiliation of Taiwan is to a significant degree due to the latter's structurally positive trade balance which could hasten the modernization process in Red China by increasing the all-Chinese import potential. The People's Republic wants to pay for future import increases chiefly with oil, coal and possibly also non-ferrous metals. In 1978 China produced about 105 mn tonnes of crude oil. The output is likely to increase substantially when the new oilfields have been opened up; the domestic requirements will however go up quite as much.

Mainland China has so far always managed to keep its trade in medium-term balance but this required strict control of imports. A measure of liberalization will be desirable and even necessary in the future. The foreign exchange reserves of mainland China are at present estimated at \$ 5 bn (incl. \$ 3 bn in gold) compared with about \$ 7 bn in the small island of Taiwan. Red China's import potential would be increased quite substantially by the addition of the island's reserves. It is also hoped in mainland China that additional foreign currency resources could be mobilized through the good connections of many overseas Chinese with the international world of finance, through activities of the Bank of China and its sister institutes in Hongkong and through systematic promotion of tourism even though infrastructural deficiencies still impose relatively narrow limits to efforts in this field. Mainland China was visited by 100,000 tourists, 30,000 other visitors and about 400,000 Chinese from Hongkong and Macao in 1978 — twice as many as in the preceding year but as many as can be accommodated at present. It is estimated that Red China earned last year \$ 200–300 mn from foreign visitors. Taiwan was visited in 1978 by 1,200,000 foreigners, and over 1,500,000 a year are expected by 1980; the island earned at least \$ 550 mn in foreign currencies from tourism.

From what has been said it is clear that in the short term Red China has more to gain from affiliation of the island to the mainland than Taiwan. It is therefore perfectly understandable that National China is at present disinclined to enter into talks with the mainland. But the starting positions, however unequal at the moment, may change. The protectionist tendencies to be noticed in the world market in regard to certain products point to the limits set to the expansion of exports and thus of the economic growth of Taiwan; these limits could be extended for a long time to come by the opening of the mainland market. Besides, both parts of China are inhabited by Chinese — and Chinese have always been adept at arriving at the most favourable alternative for themselves. Otherwise there would be no Hongkong today — and otherwise there would also be no largely autonomous Taiwan in the more distant future.