

Taiwan: A Locomotive In Transition

By Keiji Furuya

Among the NICs (newly industrializing countries), Taiwan is regarded as economically outstanding. Its average annual growth rate of 10% over the past decade, and its gain of 11.6% in the first half of this year, stand out sharply in a world finally recovering from recession.

Taiwan's per capita GNP in 1983 amounted to US\$2,673 and shows signs of rising to US\$3,000 this year, which is far above that of its neighbors in Asia, apart from Japan and Singapore. Despite a lack of major natural resources, including oil, and a population of only 19 million in an area about the size of Japan's southernmost major island of Kyushu, Taiwan is about to join the ranks of the economically advanced nations of the world.

The biggest problem now is how to break away from its reliance on labor-intensive industries and develop technology-intensive ones. Most advanced nations have succeeded in this after much difficulty, but barriers unique to Taiwan stand in its way. Surmounting them will not be easy. But it will have to succeed, if economic development and expansion are to be achieved.

First among Taiwan's special economic characteristics is its extreme dependence

on exports against the background of its international isolation resulting from its stand toward China.

At present, Taiwan maintains formal relations with just over 20 countries, including Republic of Korea in Asia and Saudi Arabia in the Middle East. It does not have diplomatic relations with either Japan or the United States, which are its biggest trading partners. Exchange with them is thus limited to the private level.

What accelerated the international isolation of Taiwan was the severance of diplomatic relations with Japan in 1972. Ironically, however, its economy began to grow rapidly from around that time.

Taiwan, which rose from the ruins of World War II like one building a house from scratch, as authority spokesman James C. Y. Soong said in a speech in July this year, stressed agriculture as the basis of its economic reconstruction.

Tropical blessings

Blessed by a tropical climate, the agricultural reforms implemented by the Taiwan authorities were a tremendous success. As soon as a self-sufficient structure, of which there are only a few in

Asia, was established, the authorities shifted priority to the development of light industry and the expansion of import-substitute industries. Their action contrasts sharply with that of Republic of Korea, which started out from a similar position. Republic of Korea is often compared with Taiwan as an NIC, but it adopted the policy of giving priority to heavy industry.

In the early part of the 1950s, agricultural products, which had accounted for over 90% of Taiwan's overall exports, fell to less than 50% in the second half of the 1960s. They were replaced by light industrial products.

In 1983, industrial goods accounted for 93.1% of all exports. From the fourth quarter of that year, textiles, which had occupied the top position until then, were overtaken by electronic and electrical goods. In short, Taiwan's export structure achieved a dramatic transformation within only two decades—from agriculture to light industry, then to heavy industry and now to electronics.

During this period, Taiwan adroitly overcame two oil crises. Its GNP has expanded from US\$10,266 million in 1973, immediately after the severance of Japan-Taiwan relations, to US\$49,754 million today, a 4.7 growth-fold. Per capita GNP has risen 3.9 times, from US\$690 to US\$2,673, at current prices.

However, its economic structure whereby nearly 50% of its GNP depends on exports is unusual when compared with Japan's level of around 10% and Republic of Korea's 30%. Moreover, exports to the United States account for an extremely high proportion of the total. Whereas in 1980, they amounted to 34.1%, or approximately one-third of the total, they increased to 45.1% in 1983 and to approximately 49% in the first half of 1984.

Japan plays an extremely large role in Taiwan's import of basic materials and machinery for processing goods for export.

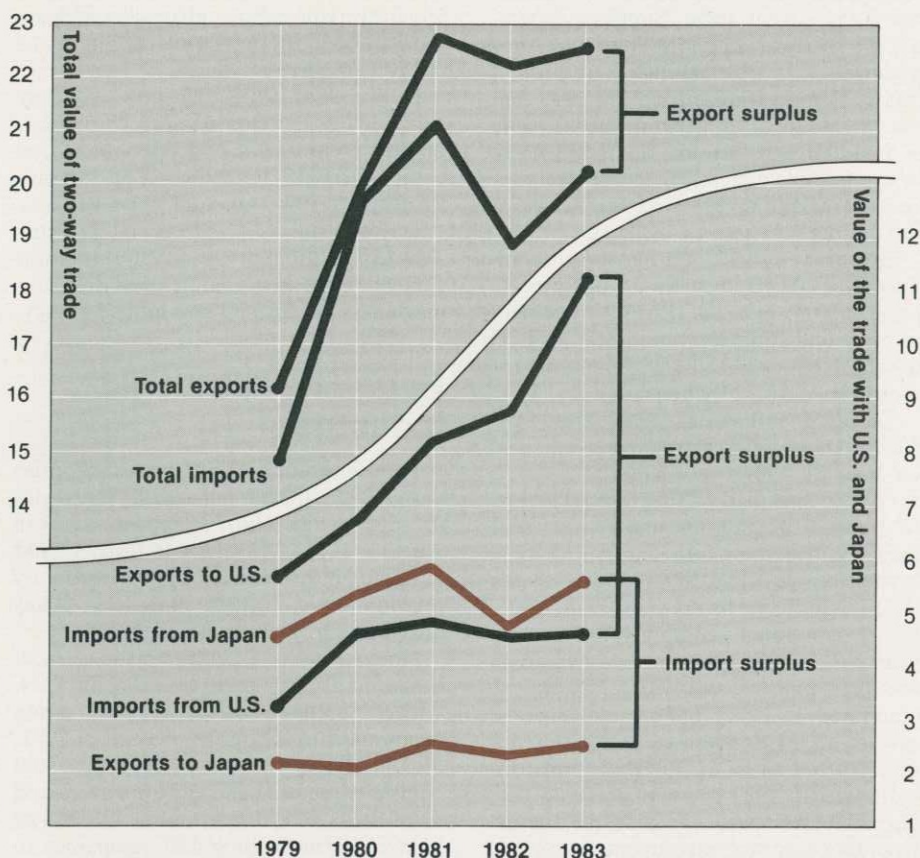
According to 1983 statistics, the United States ranked first as the export destination for Taiwanese products, with US\$11,333.7 million. It surpassed the



Capital city Taipei. Taiwan is poised to join the ranks of the world's economically advanced nations.

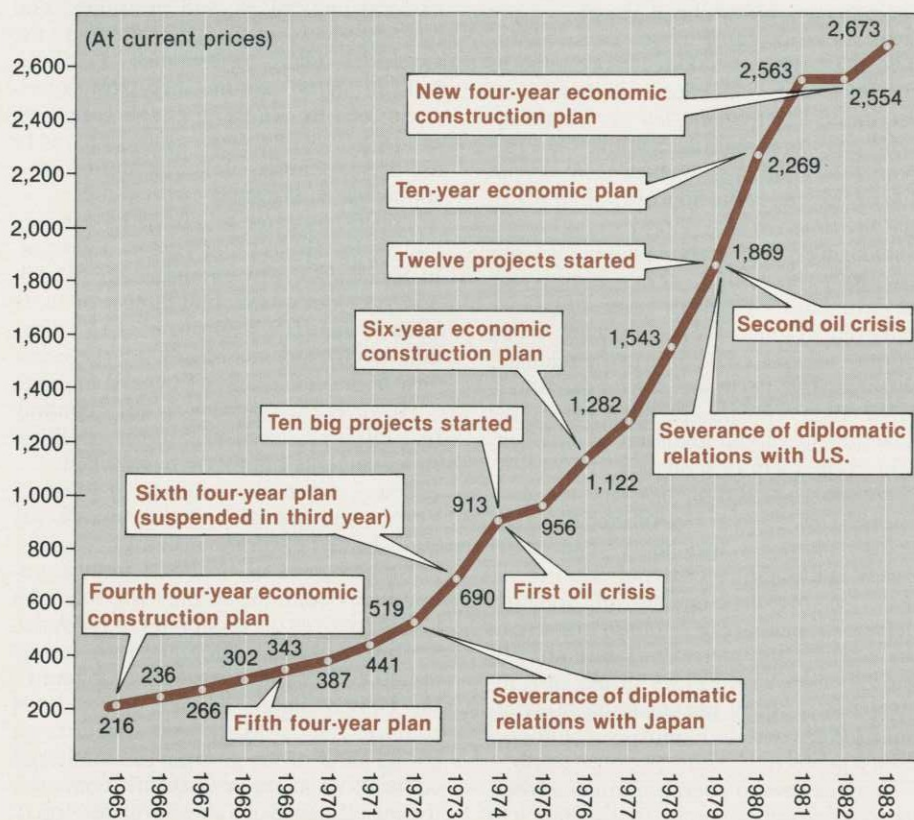
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Trade Imbalance (US\$ billion)



Source: Bureau of Statistics, Directorate-General of Budget, Accounting & Statistics, Executive Yuan (DGBAS)

Per capita GNP (US\$)



Source: Bureau of Statistics, Directorate-General of Budget, Accounting & Statistics, Executive Yuan (DGBAS)

US\$10,000 million level for the first time in history. The U.S. ranked second in Taiwan's imports, with US\$4,646.4 million. Taiwan's balance of trade with the United States is US\$6,687.3 million in its favor. Japan comes second among importers of Taiwanese goods with US\$2,494.4 million. However, Taiwan's imports of Japanese products are valued at US\$5,586.7 million, surpassing those of the U.S. by nearly US\$10,000 million. Imports from Japan exceed exports by US\$3,092.3 million.

In other words, the flow of goods—import of materials, their processing and export—has become a one-way traffic, starting from Japan, going to Taiwan and then to the United States. It sustains a large segment of Taiwan's economy.

Vulnerability to friction

This also represents vulnerability in Taiwan's economy. Although a member of the Free World, its lack of diplomatic relations with either Japan or the United States makes it difficult to settle such problems as economic friction through negotiation by official organizations. And since Taiwan relies heavily on exports, it is greatly affected by changes in the international environment.

Its trade composition of a surplus with the United States and a deficit with Japan has grown even more marked with the recovery of the American economy. In particular, the favorable balance of trade with the United States in the first half of this year amounted to US\$4,845 million on a customs clearance basis, indicating that it will far exceed the results of the preceding year. As a result, Taiwan's foreign currency holdings are expected to total a huge US\$22 billion, an increase of approximately US\$8 billion by the year-end over the US\$13,780 million recorded at the end of last year.

Already, the United States is undisputedly adopting protective trade measures against Taiwan. Taiwan has embarked on ways to improve the trade balance with the United States by announcing tariff reductions on 59 daily items, including cosmetics, beginning in January 1985. Since this structural problem cannot be solved easily, it poses the danger of becoming a big shackle on the Taiwan's economy, which relies heavily on exports to America.

Enemies in both directions

Taiwan's second problem is the fact that its economy is of a dual structure, consisting of both advanced and developing elements. While, on the one hand, it possesses high-level technology that matches advanced nations in such fields as

color TV and microcomputers, on the other, it is incapable of manufacturing motor vehicles on a purely domestic basis. And although the ratio is declining, small and medium-size businesses with 300 workers or fewer are responsible for 65% of all exports. Most of them are limited to labor-intensive industries.

As a result, it takes a beating from the advanced nations with respect to the export of industrial goods that require extensive advanced technology to produce, and is prodded from behind by the developing countries that are catching up in the export of labor-intensive goods. It is in the unfortunate position of having "enemies in both directions."

At one time, Taiwan enjoyed the benefits of still being at the development stage, as can be seen from the success of its export processing zones where it combined the technology and materials of the advanced nations with cheap labor.

As a result, however, of an improvement in the national income, a gradual rise in prices, and a squeeze in the supply and demand of labor, wages have begun to exceed worker productivity. From 1976 to 1982, whereas the gain in labor productivity averaged only 5.5% annually, wages continued to climb at an average rate of 18.8%. In 1983, the rise in wages (5.5%) finally slowed down, falling below the growth of labor productivity (13.4%), but the advantages of being at the development stage had already been lost.

Crowded out

As a consequence, in the export of advanced nation-types of products, Taiwan began to compete with the United States, its biggest trading partner, to which it sells more than it buys, and Japan, with which it has an extremely unfavorable trade balance. On the other hand, in the export of developing country-types of products, it competes against other Asian nations which have the advantage of low wages. In short, it has been crowded out, perhaps transitionally, from the so-called framework of the integrated division of business among advanced and developing countries.

Still more important, it must not be forgotten that Taiwan recognizes that China, whose output is rapidly expanding, is its greatest rival in developing country-types of products. In that sense, the maintenance of Taiwan's competitive strength in this domain is related to international politics. It now faces many tasks, such as upgrading the technology of small and medium-size manufacturers, as well as their rationalization.

The third special problem facing Taiwan is its unique public-and-private dual industrial structure. Practically all of its basic industries, such as steel, oil and chemicals, shipbuilding, electric power

and aluminum, are authority-operated. They functioned very effectively during the development stage. Supplied systematically with materials at low cost, they managed to evolve rapidly in the initial phase of industrialization. The fact that the private sector in general was also able to maintain international competitiveness in exports was due largely to the effectiveness of authority-operated businesses at the "upper reaches" of industry.

However, private businesses not involved in basic industries do not possess large capital. For this reason, investment in plant and equipment and technological development, said to be indispensable for industrial vigor, is inadequate.

Taiwan's influential newspaper, the *United Daily News*, warned in its editorial on June 23, 1984:

"According to the Directorate-General of Budget, Accounting and Statistics of the Executive Yuan, our country's national savings last year totaled 627.2 billion yuan (US\$1 equals approx. 39 yuan), but investments amounted to only 454.1 billion yuan, 173.1 billion yuan below savings. In the first half of this year, investments amounted to 222.3 billion yuan against savings of 351.8 billion yuan, a difference of 129.5 billion yuan. In GNP terms, investments in 1980 accounted for 34.2%, but thereafter declined for three successive years. Last year, investments accounted for 22.8% and in the first half of this year were down to 20.5%. While investments are not promoted, a sustained growth of the economy cannot be achieved."

In May this year, Premier Yu Kuo-hwa, who was appointed Director-General of the Executive Yuan, declared that future economic development lay in "liberalization" and "internationalization." On this point, the economic journal, *Commercial Times*, expressed its approval in an editorial on June 13:

"During the early phase of our country's economic development, the government's program and guidance achieved results. However, there is an aspect of 'intervention' in 'guidance.' With capable personnel having been nurtured today in the private sector, the government should abandon its intervention in the form of guidance.

"As for internationalization, the government has up to now protected domestic vested interests through a high tariff policy and complex controls. Such measures bar the development of domestic industries, encourage inflation and inflict damage on consumers. The internationalization which Yu Kuo-hwa speaks of is interpreted to mean liberalization in external relations and the elimination of unnecessary protective measures domestically."

With respect to liberalization and internationalization, some in Taiwan feel it is premature. Whatever the case, the dual

public-private structure at the base of Taiwan's economy creates inflexibility. Urgently required are efforts to activate the economy by stimulating the vitality of the private sector.

During the 1970s, Taiwan's economy achieved a structural transformation, moving from a light to a heavy industrial base, through its "Ten Construction Projects" (1974-) and its "Twelve Construction Projects" (1979-). At present, Taiwan is continuing to cope with structural changes in the advanced fields of precision machinery, electronics and biotechnology.

Fostering "strategic industries"

In August 1982, the Taiwan authorities designated these advanced industries (producing 151 items, increased to 169 in August 1984) as "strategic industries" and adopted measures to foster them by providing low-interest, long-term loans and technological development aid.

Noteworthy as a project is the science-based industrial zone in Hsinchu City, where foreign enterprises are being encouraged to locate. By the end of 1983, 56 businesses in the electronics and computer sectors had been approved, and 37 of them were already in operation. The plan calls for inviting 150 companies to locate in the zone by 1989. A total of 14,000 engineers, principally graduates of the science and engineering departments of local universities, will be trained and new products developed. Behind the ambitious plans to establish a Taiwan "silicon valley" are the successful experiences of the Kaohsiung and Taichung export processing zones. Taiwan plans to use these successes as the foundation for a sophisticated industry.

Taiwan allocates 41.1% of its national budget to defense and foreign relations. In fiscal 1985, this amounted to 133 billion yuan out of the total budget of 323.1 billion yuan. It will not be easy to undertake a far-reaching reform of the economy with such a heavy financial burden.

However, in considering the economy of Taiwan, its international political entanglements cannot be overlooked.

Today, when the collapse of Western Europe and the dawn of the Asia-Pacific era is being talked about, Taiwan remains outstanding among the NICs and will undoubtedly continue to play the role of a locomotive for the economies of the Asian nations. Although it does not have formal diplomatic relations with either Japan or the United States, or with the ASEAN countries, it is likely that, against the background of the growing economic and cultural ties in the Asia-Pacific community, the influence of Taiwan will develop to the point where it cannot be ignored. ●