



**China-Taiwan Relations:
Missed Opportunities**

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The agreement to conduct an expanded round of direct cross-Strait charter flights during the 2006 Lunar New Year could have marked the resumption of progress on practical cross-Strait ties. However, reacting to his party's defeat in the recent county elections, President Chen announced Jan. 1 his intention to more "actively manage" – meaning to tighten restrictions on – cross-Strait economic ties. Nevertheless, President Hu Jintao and other Chinese officials continued to signal their interest in expanding cross-Strait transportation, economic, tourism, and cultural ties. In late January, President Chen announced his intention to abolish the National Unification Council (NUC). His motives were primarily domestic, but the implications of this proposal sparked a sharp response from Washington and Beijing. In the end, Chen stopped short of abolishing the Council. Cross-Strait rhetoric has been heated, but tensions have not escalated. In late March, Chen began announcing steps to implement further restrictions on investment in China. The most serious result of these developments has been that opportunities for expanding mutually beneficial economic ties and for making progress on practical cross-Strait issues have once again fallen victim to President Chen's domestic political maneuvering.

Charter flights

The second round of direct New Year's charter flights was conducted successfully by airlines on both sides between Jan. 20 and Feb. 15, but without the fanfare that accompanied the first flights a year earlier. The number of flights was increased to 72, the number of cities served was expanded, and the restriction that only Taiwan businessmen could use the flights was removed. Despite the continuing requirement that the flight paths go through Hong Kong airspace, the program was again seen as a success that proponents hoped would provide a basis for progress on other cross-Strait transportation issues. But that was not to be.

Chen tightens controls

On Jan. 1, President Chen Shui-bian announced plans to exert greater control over Taiwan's economic ties with the mainland. In 2001, when Taiwan was in the midst of its first recession, Chen adopted a less restrictive cross-Strait economic policy under the slogan "active opening, effective management" that was designed to help Taiwan's economic recovery. This policy had always papered over a contradiction between the

Democratic Progressive Party's (DPP) business supporters who favor expanding cross-Strait economic ties and DPP fundamentalists who want to restrict them. In the wake of the party's stunning defeat in the December 2005 county elections, Chen began signaling his desire to consolidate the DPP base among its core fundamentalist supporters. In rephrasing his early slogan this January as a new policy of "active management, effective opening" Chen was appealing to fundamentalists by placing priority on managing (that is restricting) rather than opening cross-Strait economic ties.

Chen also made it clear that in the planned Cabinet reorganization, all officials would be expected to support this new policy. In this respect, the most significant personnel shift was replacing Vice Premier Wu Rong-yi, a respected nonpartisan economist, with Tsai Ying-wen, a lawyer, a colleague of former President Lee Teng-hui and a person well known for favoring a cautious, restrictive approach on cross-Strait relations. The moderate outgoing premier, Hsieh Chang-ting, said in his departure press conference that he regretted not having been more successful in promoting a spirit of reconciliation in both domestic and cross-Strait contexts. More pointedly, Hsieh commented that he continued to favor progress on the "three links." Despite considerable misgivings within the DPP, party and government officials have toed the line on Chen's new policy.

Chen's January announcement explains why a series of measures to liberalize cross-Strait economic ties that the business community had expected to be approved in late 2005 were not implemented. These measures included easing limits on the capital companies can invest in China and approvals for additional 8-inch wafer plant exports and for chip design and packaging firms to invest in the mainland. Economic Minister Ho told the press that Powerchip, one of the firms applying to export an 8-inch plant, should focus on investing in Taiwan. There is now no expectation that these measures will be implemented.

The first step to implement the new policy came in early January. Taipei indicted United Microelectronics Corp. (UMC) Chairman Robert Tsao and Vice Chairman John Hsuan, alleging they helped establish a rival Chinese chip firm, Hejian Technology Corp. A few days later, UMC was fined NT\$5 million for investing in Hejian without government approval. These moves were intended to signal the government's intention to clamp down on unauthorized investments in China.

The administration began announcing its new controls in late March. The Mainland Affairs Council (MAC) stated that "large investments" and those involving "sensitive technologies" would be subjected to a new political level "policy inspection" in addition to the normal Investment Commission review. Corporate executives making personal investments in China would have to obtain their corporate board's approval. The Financial Supervisory Commission will consider ways to strengthen controls on loans for investments in China. The deposit required of travel agencies hosting PRC tourists will be doubled to NT\$ 2 million and the fines imposed when a Chinese tourist overstays will be increased.

Despite Chen's new policy, the business community has continued to press for easing restrictions. Shortly after the successful New Year's charters, Taiwan airlines called on the government to authorize regular weekend cross-Strait charter flights. In March, TSMC chairman Morris Chang urged the government to authorize the transfer of 0.18 micron chip technology for use by Taiwan chip manufacturers in China.

Beijing remains positive

Many have concluded that Beijing has no intention of doing business with Chen during his remaining two years in office. It has long been clear that Beijing sees no hope or reason for political talks, as there is no prospect that President Chen will agree to Beijing's one China condition. Nevertheless, there is considerable evidence that even now Beijing is open to having nongovernmental front groups negotiate not just the recent New Year's charters but also other charter flights and tourism issues.

Not long after Chen's new policy was announced and one might say despite that announcement, President Hu Jintao made an inspection trip to Fujian. While there he made a well-publicized visit to the Haicang Investment Zone, where he met with Taiwanese investors. Hu reiterated PRC policy to encourage Taiwanese investment, promote cross-Strait economic ties, and adopt measures beneficial to Taiwanese business. Hu urged nongovernmental organizations to start talks soon on the "three links." On Jan. 18 just before the Lunar New Year, Jia Qinglin, chairman of the Chinese People's Political Consultative Congress (CPPCC) and number-four man on the Politburo Standing Committee, met with Taiwanese business association representatives and again called for nongovernmental organizations to negotiate on charter and tourism issues. On Jan. 25, Civil Aviation Association of China (CAAC) officer Pu Zhaozhou, who had negotiated the New Year's charters for Beijing, called for negotiating additional holiday and weekend charters.

Two weeks later, after Chen announced his plans to abolish the National Unification Council (NUC), Pu Zhaozhou appeared at a Taiwan Affairs Office (TAO)-sponsored press conference and expressed an even more forthcoming view in calling for talks on both passenger and cargo charter issues. Cargo flights had been a Chen administration priority before Chen's Jan. 1 announcement. At the end of the New Year's charter flights, China National Tourism Association (CNTA) President Shao Qiwei urged progress on tourism issues. On Feb. 27, just when Chen's announcement on the NUC was expected, the TAO called for nongovernmental tourism organizations to hold consultations on Chinese tourism to Taiwan. Just what contacts have been held between nongovernmental association representatives on charter and tourism issues is not clear, but each side has attempted to place the onus for delay on the other.

At the annual National People's Congress (NPC) meeting in early March (shortly after Chen's decision on the NUC), it was natural that senior Beijing leaders put emphasis on their determination to check Chen's dangerous separatist moves. Nevertheless, the very brief references to Taiwan in Premier Wen Jiabao's NPC work report were expressions of well-known PRC views, including a reference to promoting the three links on a

comprehensive, direct two-way basis. When asked about Chen's actions at the end-of-NPC press conference, Premier Wen began by criticizing Chen for trying to block the three direct links and restrict the development of cross-Strait economic ties, policies that Wen said would make Chen unpopular.

On March 22 during the visit of a KMT delegation, the KMT and TAO Chairman Chen Yunlin announced plans for a KMT-CCP co-sponsored conference on cross-Strait economic and trade issues in Beijing on April 14-15. Taiwan airlines and the KMT have proposed that charter flights patterned on the New Year's flights be arranged on a weekly basis. It is planned that the conference will provide a forum for announcing some understandings on the technical aspects of how weekly passenger charter flights could work. The involvement of the KMT in this process will make it even more difficult for the Chen administration to accept the arrangements.

National Unification Council

At a press conference in his hometown during the Lunar New Year, President Chen surprised attendees by proposing that the moribund NUC and the policy under which it had been established, the 1991 National Unification Guidelines (NUG), be abolished. This was significant in part because in his first inaugural address Chen had made a commitment that the NUC would not be abolished. What was behind this proposal? Chen's motives were domestic – to appeal to DPP fundamentalists and to undermine support for KMT Chairman Ma Ying-jeou by tarring him as a proponent of the Council and of unification, which Ma had ill-advisedly stated earlier to be the KMT's eventual goal.

Washington reacted quickly and publicly by stating both that it opposed any unilateral changes to the status quo (implicitly including abolishing the NUC/NUG) and that it supported expansion of transportation and communications links and cross-Strait economic and cultural ties, a comment aimed at Chen's restrictive approach to cross-Strait issues. Beijing's reaction was again to accuse Chen of being a troublemaker who was sabotaging cross-Strait relations. The U.S. exerted heavy pressure on Chen not to abolish the NUC, by sending a senior NSC/State team to Taipei on a confidential mission to underline U.S. concerns directly to President Chen. On Feb. 27 Chen announced that the NUC would "cease to function" and the guidelines would "cease to apply." A few days later after Taipei had made clear on the public record that these phrases did not mean abolish, Washington considered the issue acceptably settled. Beijing however was seriously concerned and also saw a propaganda opportunity. President Hu and Premier Wen called Chen's decision deceptive and dangerous, and Beijing has continued to use the issue to mobilize international opposition to President Chen.

Ma enunciates his cross-Strait policy

In trips to Europe in February and the U.S. in March, KMT Chairman Ma Ying-jeou laid out his views on cross-Strait issues, which after a few missteps have settled into a consistent set of talking points. The KMT's goal is to preserve the status quo; neither

unification nor independence is a current issue. Independence is an option for Taiwan's people, but it is not an option sought by the KMT. The KMT accepts the one China principle, but asserts that each side has its interpretation of it. In office, the KMT would seek to resume talks on the basis of the 1992 consensus and negotiate practical agreements on travel, tourism, and other issues to stabilize cross-Strait relations. The KMT would also seek an accord with Beijing to assure peace for 30-50 years and seek a *modus vivendi* on Taiwan's international participation. Taiwan would strengthen ties with the U.S., Europe, Japan, and others. In Washington, Ma packaged these ideas under the slogan "five do's" to contrast his positive approach to cross-Strait relations to Chen's "five no's."

Such policy statements are quite in line with longstanding U.S. policy. This helps explain why Ma was very well received by the Bush administration when he visited Washington March 22-23. The official press in China reported favorably on Ma's visits but omitted mention of his ideas concerning "one China, respective interpretation" and a long-term *modus vivendi* – an indication that these are problematic issues for Beijing. The TAO did restate that in talks conducted on the basis of the 1992 consensus Taiwan's international participation could be discussed.

Trade and investment

Statistics for 2005 indicate a mixed picture for cross-Strait economic ties. According to Taipei's Board of Foreign Trade, Taiwan's exports to China reached \$51.8 billion, up 15.2 percent, while Taiwan's imports from China totaled \$19.9 billion, up 19.5 percent. While this growth was strong, the growth rate of total trade was the slowest since Taiwan recovered from its 2001 recession. While total cross-Strait trade thus reached \$71.7 billion according to Taiwan statistics, Beijing's figures put the total as usual at a higher figure, \$91.2 billion. China remained Taiwan's largest export market accounting for 27 percent of Taiwan's global exports. Nevertheless, Taiwan's share (11.3 percent) of PRC imports again declined slightly because China's imports from other countries grew more rapidly than those from Taiwan. Taiwan is becoming less competitive in the China market.

According to Taipei's Investment Commission, Taipei approved investments in China totaling \$6 billion in 2005, down 13.5 percent from the previous year. Taiwan's investment statistics are at best indicative only of trends. A poll of manufacturers conducted by the Ministry of Economic Affairs indicated that, despite the Chen administration's efforts to discourage investment in China, for the first time over 80 percent of Taiwan's global foreign direct investment went to the mainland in 2005.

Panda politics

At the end of the quarter, Taipei formally rejected Beijing's gift of pandas offered to KMT Chairman Lien Chan last summer. Beijing had been propagandizing their offer both to symbolize the more positive and friendly aspects of Hu Jintao's policy toward Taiwan and to score diplomatic points by offering the cuddly creatures free of charge, a feature

that the PRC, a party to the Convention on the International Traffic in Endangered Species (CITES), could only offer for gifts made to its domestic (as opposed to international) institutions. The Chen administration of course does not want the pandas precisely because they symbolize the non-hostile aspects of Beijing's policy and justifies its rejection of the gift as inconsistent with the fact that Taiwan is not part of the PRC and hence can't accept them free of charge. The losers in this tit-for-tat game are again the people of Taiwan, the majority of whom would love to receive the pandas.

Looking ahead

Given the political impasse, the private sector plays a large role in cross-Strait dealings, and ties are growing in many sectors. However, Chen Shui-bian's discouragement of investment over the past year and his new policy of tighter controls are impeding the natural development of cross-Strait economic and cultural ties. The principal loser is Taiwan and Taiwanese companies whose economic competitiveness in the China market will continue to erode because of government imposed restrictions. The Chen administration's decisions not to grant liberalizations long sought by Taiwan's internationally minded firms contributes to Taiwan's sub-par economic performance, discourages foreign direct investment in Taiwan, makes Taiwan a less attractive location for foreign business, and undermines Taiwan's international influence. Beyond these significant costs, Chen's new policy means that opportunities to negotiate arrangements to open cross-Strait travel and tourism for the benefit of Taiwan are being missed.

Uncertainty about Chen Shui-bian's intentions will continue to cast a pall over U.S.-Taiwan and cross-Strait relations in the months ahead. While tensions remain low, Beijing is deeply concerned that Chen will take other steps to pursue what they describe as his separatist agenda. Nevertheless, Beijing does want to expand cross-Strait economic and cultural ties and will look for ways to accomplish this, working with the private sector and opposition parties and giving as little credit to the Chen administration as possible. As this is an unattractive proposition for the Chen administration, little progress on these functional issues can be expected.

Chronology of China-Taiwan Relations January-March 2006

Jan. 1, 2006: President Chen Shui-bian's New Year's address calls for new policy of "active management, effective opening."

Jan.3, 2006: Chen asks British parliamentarians to review "one China" policy.

Jan. 6, 2006: TAO criticizes Chen; calls for progress on three links.

Jan. 6, 2006: MAC says Beijing using pandas for unification propaganda.

Jan. 9, 2006: United Microelectronics (UMC) officials indicted.

Jan. 13, 2006: Taiwanese and Chinese firms establish JV air cargo airline.

Jan. 14, 2006: Hu Jintao visits Haicang area in Xiamen; calls for progress on three links.

Jan. 14, 2006: *Janes* reports that U.S. turned down Taiwan request for info on JDAM and HARM missiles.

Jan. 17, 2006: President Chen criticizes KMT for “singing duet” with PRC.

Jan. 18, 2006: CPPCC Chairman Jia Qinglin meets local TAO heads; urges progress on “three links.”

Jan. 20, 2006: New Year’s charter flights begin.

Jan. 20, 2006: Premier Hsieh says he supports direct flights.

Jan. 20, 2006: KMT leaders pledge to push for weekly charter flights.

Jan. 25, 2006: CAAC’s Pu Zhaozhou says Beijing wants weekend and holiday charters.

Jan. 27, 2006: WHO secretariat rejects proposal giving Taiwan observer status.

Jan. 28, 2006: Beijing announces names for gift pandas.

Jan. 29, 2006: President Chen proposes scrapping National Unification Council (NUC).

Jan. 30, 2006: State Department reaffirms status quo in cross-Strait relations, but supports expanded political, economic, social, and cultural exchanges.

Feb. 2, 2006: KMT chairman Ma Ying-jeou warns Chen not to break five “noes” commitments.

Feb. 5, 2006: PRC MOFA spokesman says Chen’s NUC comments strain peace/stability.

Feb. 7, 2006: KMT Chairman Ma’s interview in *Asian Wall Street Journal*.

Feb. 8, 2006: Chen says his NUC policy is response to Ma’s unification goal.

Feb. 8, 2006: TAO calls Chen a troublemaker sabotaging cross-Strait ties. CAAC’s Pu Zhaozhou urges Taiwan to negotiate on charters.

Feb. 12, 2006: National Security Council Acting Senior Director for Asian Affairs Dennis Wilder and Clifford Hart, director of the State Department’s Taiwan Desk, reportedly travel secretly to Taiwan to try to dissuade Chen Shui-bian from abolishing the National Unification Council.

Feb. 13, 2006: KMT Chairman Ma speaks at London School of Economics.

Feb. 15, 2006: New Year's charter flights end. CNTA's Shao Qiwei calls for tourism cooperation.

Feb. 15, 2006: Ma in Dublin says independence an option for Taiwan, but not KMT.

Feb. 15, 2006: UMC fined for investment in Hejian.

Feb. 17, 2006: EVA and other Taiwan airlines propose weekend charters.

Feb. 21, 2006: KMT's Su Chi claims authorship of "1992 consensus."

Feb. 22, 2006: Taipei press reports NSC & State officials visited Taiwan on weekend.

Feb. 22, 2006: TAO Chairman Chen Yunlin says abolishing NUC would jeopardize ties.

Feb. 22, 2006: KMT delegation discusses tourism & charters with TAO.

Feb. 24, 2006: Amb. Burghardt appointed AIT chairman; Stephen Young as AIT director.

Feb. 27, 2006: TAO official reaffirms PRC interest in facilitating tourism to Taiwan.

Feb. 27, 2006: President Chen announces NUC will cease to function.

Feb. 27, 2006: State Dept. reiterates policy, says Chen has stopped short of abolishing NUC.

Feb. 28, 2006: President Hu describes Chen's actions as a "dangerous step."

Feb. 28, 2006: Beijing reiterates that pandas will be free.

March 1, 2006: EU statement says ceasing NUC operations will not help stability in Strait.

March 2, 2006: Premier Wen urges international community vigilance against Chen.

March 2, 2006: State Dept. spokesman comments on NUC, seeks clarification regarding cease vs. abolition.

March 3, 2006: Taipei MOFA spokesman says "cease to function" is not abolition.

March 5, 2006: Premier Wen's NPC Work Report addresses Taiwan in standard terms.

March 5, 2006: Jia Qinglin urges CPPCC members to reach out to DPP hardliners.

March 7, 2006: At hearing, U.S. Sen. John Warner warns Taiwan against provoking China.

March 10, 2006: Former Deputy Secretary Armitage visits Taipei.

March 14, 2006: At NPC press conference, Premier Wen calls Chen dangerous and deceitful.

March 17, 2006: Secretary Rice in Sydney says Taiwan has engaged in problematic behavior.

March 18, 2006: DPP holds demonstration against PRC threats to Taiwan.

March 20, 2006: Taiwan MND report says China gaining a military edge.

March 21, 2006: TSMC Chairman Morris Chang calls for export of 0.18 micron technology.

March 21, 2006: KMT chairman Ma at Harvard calls for cross-Strait *modus vivendi*.

March 22, 2006: KMT chairman Ma visits Washington; meets State Deputy Secretary Zoellick and others.

March 22, 2006: MAC announces some new measures to reduce reliance on China, tighten controls on investments to the mainland, and crackdown on smuggling.

March 22, 2006: TAO and KMT announce plans for April 14-15 economic and trade conference in Beijing.

March 24, 2006: DPP cancels planned “grand debate” on China policy.

March 26, 2006: In Jakarta, Jia Qinglin calls on friends to help defeat separatism.

March 31, 2006: Taipei’s rejects applications for zoos to import gift pandas.

