Taiwan's capabilities in international trade

Ming Lee
*The University of Montana*

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TAIWAN'S CAPABILITIES IN INTERNATIONAL TRADE

By

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B.B.A., National Taiwan College of Marine Science and Technology, 1980

Presented in partial fulfillment of the requirements for the degree of Master of Business Administration University of Montana 1986

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Dean, Graduate School

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Date Dec. 16, 1986

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Chapter 1

INTRODUCTION

Although Taiwan's flourishing economy, with continuous high rates of economic growth in recent years, has been acclaimed throughout the world as a modern miracle—one of Asia's Four Dragons—most western people may not know why Taiwan enthusiastically plays an active role within the fabric of complicated and competitive international trade despite the country's scarce natural resources and high population density. First, this paper introduces The Taiwan Model in economic development. It explores and analyzes the impact of the Chinese background on the modern Taiwan businessman's behavior. The environmental internal and external influences on Taiwan's foreign trade, which include land reform, population change, and the relationship of substantial diplomacy with foreign countries, are discussed as well. The paper also briefly describes the key points of Taiwan's economic achievements on international trade.

Taiwan presently is worried about a number of barriers which undermine the country's trading capabilities. These trading bottlenecks—the trade-surplus with the United States, dependence on imports from Japan, commercial counterfeiting problems, and pressure as a result of massive

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foreign exchange reserves—are examined in detail. Finally, Taiwan's future international trade prospects are considered in relation to strong competition from South Korea and effects of the open door policy of mainland China.

Whether or not other developing countries can duplicate Taiwan's experience is debatable. Admittedly, the impact of the Republic of China on Taiwan the past 30 plus years has been considerable. This paper provides clues for those concerned about the prospects of Taiwan's future foreign trade.

Taiwan, a small island with an area of 13,885 square miles, is slightly smaller than Switzerland, the Netherlands, or the combined area of Massachusetts and Connecticut. With a population of 19 million, limited arable land, and few natural resources, the disparity of incomes between the top wage earners and those at the bottom was reduced in 1985 to 4.36 to 1 from 15 to 1 in the 1950s. Thus the majority of the people are middle class.2

Taiwan's economic development could be traced first, from 1895 to 1945, the period of Japanese colonization, and second, from 1951 to 1965, the period of United States economic aid. During the former, the Japanese did not intend to develop Taiwan's industry to a high degree. Their concentration was on developing agricultural raw materials which could be exported to Japan to support Japanese industrialization.3 Nonetheless, the 50 years of Japanese
rule on Taiwan were typified by colonized economic
development along with rigid political control.

During the second period, United States aid assisted
Taiwan socially, militarily, and economically. The aid
primarily helped recover Taiwan's postwar economy and it
controlled inflation in the early 1950s. The aid also
inaugurated a favorable climate for private investments
or enterprises which were free to concentrate on
labor-intensive processing industries. This gave Taiwan a
great advantage in international trade.\(^4\) Japan and the
United States still are Taiwan's major trading partners in
the global economy.

In 1949 the Nationalists withdrew from mainland China.
Their failure to carry out land reform envisioned by
Dr. Sun Yat-sen, father of the Republic of China,
led to a great urgency to formulate and implement a
series of agricultural development programs which
consolidated the future foundation of industrialization and
provided the incentives necessary for the island's economic
growth. Subsequently, under prudent economic development
strategies during the 1960s and early 1970s, several Export
Processing Zones (where imported raw materials and
intermediate goods were processed into finished goods for
export) were established to attract foreign capital and
accelerate the rate of export expansion.\(^5\)
Chapter 2

THE TAIWAN MODEL IN ECONOMIC DEVELOPMENT

Impact of Traditional Chinese Characteristics on Modernized Businessmen's Behaviors

The Chinese traditional philosophy of life emphasizes a close family system, a great respect for education, and the brotherhood of man. As an ethical system, Confucianism has served the Chinese well for 2500 years and has become a paramount force in Chinese traditional culture. Today most Chinese in Taiwan, regardless of their specific religious affiliations, or lack of them, are affected behaviorally and attitudinally by Confucianism.6

Due to rapid industrialization and westernization, Taiwan's society has changed which, in turn, has influenced the people's standards of value judgments. Businessmen particularly face challenges imposed by changing social and material environments. In terms of moral and social responsibilities, the thinking of the people has remained virtually unchanged as they have attempted to adapt to an evolving society combining old traditions with new ideas.

Since the Chinese in Taiwan are deeply affected by traditional culture, Confucian teachings stressing loyalty, forgiveness, and moderation—the guiding principles of
life—are deeply rooted in the minds of the people. The family unit continues to be the nucleus of society. Filial piety is considered a cardinal virtue. The Chinese approach to human relationships is learned in the family: children are taught to respect their parents at home, teachers in school, and elder people in society. These attitudes radiate from the family to the whole of society.

The traditional Chinese concept, based on Confucianism, emphasizes the obligation of children to parents, and young people to elder people. Accordingly, the young in an organization or company must comply with traditional rules that require expressing a deferential demeanor to their superiors and heeding their opinions in decision making. Under these circumstances, what Taiwan's businessmen display in the face of strong competition in international trade is a kind of teamwork more than individual performance.

Friendliness and personal warmth are important also. There is an old Confucian saying: "It is a joy for a friend to come from afar." This has been rephrased by businessmen in Taiwan: "A buyer from far away received to dinner at a restaurant is a worthwhile affair." For businessmen in Taiwan, eating is more than a biological necessity; they prefer to settle bargains around a dinner table than around an office conference table. This involves much mutual inviting and yielding, and the seating must be just right. Via formal and informal dinners, Chinese businessmen
strive to increase their understanding of one another and make good trades.

Adoring nature is another traditional characteristic of most Chinese. They extol the harmony of humanity and nature, attempt to apply it to their personalities, and imitate it in their calligraphy. This adaptation to the physical environment has greatly influenced Chinese culture and behavior. 

For instance, written language in China began with simple pictographs which represented objects. Many present-day Chinese characters have evolved from these pictographs. Moon, written as 月, developed from the ancient 月. Other examples are the sun, formerly 日, now 太; mountain, formerly 日, now 島; water, formerly 水, now 水. Many basic pictographs have been extended or combined to form ideographs. Sun, 日, and moon, 月, together, 明, mean bright, illustrious, and clear. A tree, 木, doubled, 林, forms the character for forest. If tripled, 林, the character means a dense forest. The process of character evolution from pictograph to ideograph illustrates that the Chinese are good at imitating and that they abound in imagination.

In addition, duplicating Chinese characters challenges the artistic imagination. The making of a good calligrapher is a slow and arduous process. It requires many years of copying old masters before one can create a style of one's
own and be labeled a true calligrapher. Alas, the ancients would be dismayed that this imitation process has resulted in distorted thinking among modernized businessmen in Taiwan. Many copy hot-selling consumer products for profit even when their actions are illegal or they are violating business ethics.

The Chinese background, steeped in traditions, has generated positive and negative effects on modern businessmen in Taiwan. The Chinese in general, not only businessmen, continuously maintain their traditional culture while assimilating outside cultures. How to combine the best of the traditional and the new cultures, and promote the businessmen's social responsibilities and ethics, is the basis of this study.

Environmental Influences

Success in international trade has earned Taiwan an honored title: Newly Industrialized Country of Asia. Why has Taiwan been so successful in comparison to others? It has been suggested that Taiwan's unfavorable economic geographic factors and lack of natural resources have more than been compensated by an abundance of human resources. It also has been suggested that the country's close proximity to mainland China, shadowed by Communist dictatorship, has forced Taiwan to increase its strength via the pursuit of foreign trade as a means of survival.
Internal Factors

The island of Taiwan is 244 miles long from tip to tip and 89 miles wide at the broadest point. Its northern extremity is 655 miles southwest of Japan and its southern tip is 225 miles north of the Philippines. Although the soil is fertile and the climate is favorable, only one fourth of the island is suitable for cultivation. The remaining terrain is mountainous, covered by forests of indifferent commercial value. Taiwan's important natural resources are coal, limestone, and natural gas, present in insufficient quantities for local needs. On the whole, Formosa has not been bountiful.10

Under Japanese rule from 1895-1945, Taiwan was an agricultural colony. The Japanese pursued a vigorous exploitation policy with a view to creating an agrarian economy to compensate for Japanese industrialization. Taiwan exported primary products, especially rice and sugarcane, and imported manufactured goods, that is, about 90 percent of the exports went to Japan and almost as large a proportion of the imports came from there.11

The other most important trading partner was mainland China, although it accounted for but a modest proportion of trade. The per capita value of Taiwan's external trade was 39 times that of mainland China and one and one-half times that of Japan.12 When the Republic of China took over the
island, Taiwan's economic well-being was significantly dependent on the export of agricultural products.

After World War II Taiwan was restored to the Republic of China. As a result of the war, her trade had declined considerably. When mainland China fell to the Chinese Communists in 1949, Taiwan's economic relations with the mainland were severed along with a trading relationship. The small island faced an urgent necessity to shift its export market to other parts of the world. Maurice Scott stated Taiwan's economic situation in his article, "Foreign Trade:"

Deprived of protected markets in Japan and China for its exports, the economy of Taiwan was left to reestablish itself as an independent economy for the first time in its history.13

The Taiwan government expanded agricultural products for export, reduced imports, and coordinated industrial development. It concentrated on establishing and expanding industries to supply the domestic market, especially the production of fertilizer to increase agricultural output. By the end of the 1950s, when Taiwan began its export orientation, world trade and the world economy were embarking on a long period of constant expansion. The world climate and Taiwan's timing were right!14

Under colonial rule the Japanese gave the Taiwanese little opportunity to enter secondary and higher education.
Neither were the Taiwanese permitted to occupy any senior governmental or managerial positions. In 1949 a large number of industrialists, businessmen, engineers, scientists, and administrators migrated to Taiwan when the Nationalists withdrew from mainland China. Most of them were highly educated and trained.

These mainlanders became the elite of society and made significant contributions to economic development in Taiwan the past 37 years. They filled the technical personnel and skilled supervisory vacancies caused by the departure of the Japanese in 1945, and were responsible for government aid as well as economic and trading policies that followed. As a result, Taiwan's foreign trade conditions gradually stabilized.15

When, in 1949, approximately one million Chinese migrated from the mainland to Taiwan, the population was estimated to be over six million.16 In the years that followed, the population increased rapidly under Nationalist rule. By 1983 the population reached 18.7 million, a 1.49 percent growth rate, with a density of 520 per square kilometer.17 This population density was one of the highest in the world with 64.5% between the ages of 15 to 64. This represented a tremendous and vigorous work force.18
In addition, because the government concentrated on educational reform throughout the years, especially in technical and vocational colleges, Taiwan has a high-quality as well as abundant human resource to cope with the demands of technology and international trade. The natural resources are limited, but the Chinese in Taiwan view their human resource as inexhaustible.

External Factors

Corruption within the monetary system and failure to carry out land reform were major factors in the civil war which resulted in the Nationalists leaving the mainland. Although they pulled out in 1949, the civil war between them and the Chinese Communists never officially has ended. Even now the leaders of mainland China continually advocate the liberation of Taiwan and unification of China.

After retreating to Taiwan, the Nationalists were eager to establish a sound economic system and implement a series of agricultural developments which consolidated the future capabilities of foreign trade development. No persuasion was needed to enlist everyone in a campaign to rebuild and develop Taiwan's economy. In the early 1950s the government and the people perceived intuitively that Taiwan was their last opportunity, their last place to survive. They had to do their best to maintain the small island—or be buried by the Chinese Communists. In the 1960s the
ability of leadership to sustain the morale of the people in Taiwan and expand international trade rapidly lay, in part, upon the diplomatic support of its principal trading partners, the United States and Japan, and upon the country's worldwide diplomatic relations.

As the Chinese Communists, through control of China mainland, won international recognition and became regarded as the sole legitimate government of China, Taiwan faced increasing difficulties in the diplomatic world. Taiwan maintained diplomatic relations with many countries and membership in important international organizations until the beginning of the 1970s, but acceptance of the Chinese Communists as a member of the United Nations in 1971 precipitated a major change. Taiwan withdrew from the United Nations and lost diplomatic recognition; at the same time, the Communist government in Beijing gained recognition.

In the wake of Taiwan's expulsion from the United Nations, Japan, Taiwan's most important partner in Asia, switched its recognition to Beijing in 1972, as did 25 other countries between 1971 and 1972. By 1977, 111 countries had established relations with Beijing. Only 23 countries maintained relations with Taipai.20

A further difficulty arose when the United States established diplomatic relations with mainland China, announced by President Carter in December 1978. Taiwan
responded by breaking off official relations with Washington and terminating the 1954 Mutual Defense Treaty. The period of shock which followed caused a drop in the stock market. Unease about the future was experienced by the public. Taiwan felt that its security was seriously threatened.

The U.S. Congress passed and President Carter signed the Taiwan Relations Act in 1979. This Act established a new relationship with the United States, defined as unofficial, and provided for many-faceted and ongoing economic, cultural, and technological relations with Taiwan. The Taiwanese government subsequently expanded its overseas lobbying efforts, encouraging other countries not recognizing Taiwan to adopt the American formula.

Taiwan made further efforts to expand and strengthen international trade by setting up semiofficial "substantial diplomacies." The economic growth and foreign trade expansion enhanced Taiwan's stability and position in the international business community, and helped compensate for the series of diplomatic setbacks experienced in recent years. The government proved that it was capable of adjusting to pressure and effectively leading its businessmen into exploiting new markets via different channels.

No matter what develops between Taiwan and mainland China in the future, the latter might take advantage of
Taiwan's gradually deteriorating diplomatic position to initiate different kinds of pressure on Taiwan's foreign trade. The effectiveness of pressure heavily depends on the reaction of Taiwan's trading partners, such as the United States and Japan, to mainland China's attempt to interfere in trade with Taiwan. Taiwan's economic achievement and trading development must be elevated continuously through its "substantial diplomacy" to make the trading partners realize that Taiwan's free enterprise system, relatively open society, and deep involvement in foreign trade play an active role and make a significant contribution in international affairs.

**Economic Achievements of International Trade**

Any island economy, by the very nature of its geographic arrangement, must rely on trade to survive. Taiwan is no exception to this rule. Wou Wei pointed out in his article, "New Trends in the Republic of China's External Economy Policy," that the course of Taiwan's economic development, like the island economies of Japan and England which used foreign trade as transitional measures to foster their domestic economic strengths, and gradually became less dependent upon foreign trade, has been heavily dependent upon foreign trade to support its agricultural and industrial developments. Taiwan is unlike the small island city-states (island-urban types) of Singapore and Hong Kong,
with economic development concentrated in industry in accordance with their urban developments.24

Today, because Taiwan's geographical sea-surrounded environment is limited, the island has become more dependent on foreign trade to establish substantial economic ties with other countries, hoping thereby to stimulate the economy. Under the circumstances, Taiwan took on a high-growth rate and export-oriented strategy of economic development in order to generate rapid growth in foreign trade.

From 1952 to 1985, exports grew in value from $0.1 billion to $30.7 billion, and imports from $0.2 billion to $20.1 billion.25 The trade balance has shown a greater surplus every year since 1976 (with the exception of 1975, the oil crisis year). In 1985 the amount of trade surplus amounted to $10.6 billion. (See Table 1.)

During the last few years, 1975-1984, Taiwan has been ranked second, after Singapore, in economic growth in the world.26 By 1985 Taiwan was ranked, via data released by the International Monetary Fund, as the tenth largest exporting nation in the world, well ahead of other developing countries. For imports, Taiwan ranked nineteenth. Combining imports and exports, Taiwan was the fifteenth largest trading nation in the world. On the whole, Taiwan's foreign trade constituted 84.6% of its GNP in 1985.27 This reflects Taiwan's high degree of economic dependence on foreign trade.

15
Table 1

Foreign Trade Volume*

<table>
<thead>
<tr>
<th>Year</th>
<th>Total trade</th>
<th>Index† (1975 = 100)</th>
<th>Surplus (+) or deficit (-)</th>
<th>Proportion of total trade to GNP</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>GNP</td>
</tr>
<tr>
<td>1975</td>
<td>11,260.5</td>
<td>100</td>
<td>(-) 642.9</td>
<td>15,293</td>
</tr>
<tr>
<td>1976</td>
<td>15,765.2</td>
<td>140</td>
<td>(+) 567.4</td>
<td>18,318</td>
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<tr>
<td>1977</td>
<td>17,871.6</td>
<td>159</td>
<td>(+) 849.8</td>
<td>21,364</td>
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<tr>
<td>1978</td>
<td>23,714.0</td>
<td>211</td>
<td>(+) 1,660.2</td>
<td>26,196</td>
</tr>
<tr>
<td>1979</td>
<td>30,877.1</td>
<td>274</td>
<td>(+) 1,329.7</td>
<td>32,346</td>
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<tr>
<td>1980</td>
<td>39,543.7</td>
<td>351</td>
<td>(+) 77.5</td>
<td>40,022</td>
</tr>
<tr>
<td>1981</td>
<td>43,810.7</td>
<td>389</td>
<td>(+) 1,411.6</td>
<td>45,920</td>
</tr>
<tr>
<td>1982</td>
<td>41,092.5</td>
<td>365</td>
<td>(+) 3,315.9</td>
<td>46,500</td>
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<tr>
<td>1983</td>
<td>45,409.7</td>
<td>403</td>
<td>(+) 4,835.7</td>
<td>49,754</td>
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<td>1984</td>
<td>52,415.5</td>
<td>465</td>
<td>(+) 8,497.3</td>
<td>56,638</td>
</tr>
<tr>
<td>1985</td>
<td>50,823.4</td>
<td>451</td>
<td>(+) 10,610.2</td>
<td>60,078</td>
</tr>
</tbody>
</table>

*Unit: U.S. $ million.
†Percent growth since 1975.

Source:

The rapid expansion of Taiwan's foreign trade is guided by a series of economic plans which establish goals and provide incentives and stimuli for the private sector through several approaches. The primary features of these approaches may be recapitulated as follows: (1) land reform, (2) U.S. economic aid, and (3) export processing zones.

Land Reform

The early land reform was carried out in three stages. In 1949 farm rents were reduced from a prevailing level of 50 percent or more to 37.5 percent of the annual yield of the principal crop. In 1951 lands owned by the government were sold to tenant farmers. The third stage, begun in 1953 with passage of the Land-to-the-Tiller Act, was completed in less than two years. This program limited the holdings of landlords to seven acres of rice land and transferred the excess land to those farming it. The tenants paid for the land in 10 annual installments while the landlords received full compensation in the form of crop bonds and stocks in four government corporations.28

Briefly, land reform may be viewed as a recognition of the agricultural system which, directly, provided former tenants an incentive to put more efforts and resources into increasing agricultural output. Indirectly it improved cultivation methods, especially with multiple cropping.
and irrigation. Although agricultural products still have to be imported in considerable quantities—the labor force has tended to move agriculture into the industrial sector—land reform provided a sound basis for export success in agricultural products such as sugar, bananas, and mushrooms in the early period, and consolidated the future foundation for industrialization.29

U.S. Economic Aid

In the early 1950s Taiwan was in a critical financial and economic position. The basic necessities of living were in short supply. The widespread budget deficit and price inflation could have undermined the political stability and economical viability of Taiwan. U.S. aid primarily nurtured public confidence in the success of the Taiwanese government's programs.30

U.S. aid contributed to the economic transformation of Taiwan three ways: (1) influencing the formation of governmental economic policies, (2) investing directly in development, and (3) providing goods that released Taiwan's funds for investment. By these approaches, aid-financed imports accounted for 30 percent of domestic investment in Taiwan throughout the U.S. economic aid program. In the meantime, exports expanded.31

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The most important consequence of U.S. aid was the boosting of private enterprise by creating a climate for private investment and promoting greater reliance on market forces. U.S. economic aid had been terminated in 1965, but Taiwan was stimulated to take further steps to improve the climate for private investment and promote exports for economic takeoff. Exports to obtain investments and credits from foreign sources also were increased.32

Export Processing Zones

After the termination of U.S. economic aid, the government in Taiwan adopted a series of approaches for directly reinforcing the establishment and expansion of export industries and enacted a program for the encouragement of foreign investment. Three Export Processing Zones (EPZs) were established in Kaohsiung, Tarthung, and Nantze.

An EPZ, a combination industrial district and free trade zone, is designed so investors can import basic materials, process them, and export finished products. Foreign investors setting up factories within an EPZ receive considerable advantages and enjoy special incentives. These include low-cost skilled labor, exemption from customs duties on the importation of raw materials, machinery, parts, and exported products, tax holidays, and developed support facilities. All make zonal operations attractive.34
EPZs have contributed to Taiwan three ways:

1. Via attracting foreign capital, about 75 percent of the total earnings of the three EPZs were used to pay for local costs, thereby leaving a substantial amount of foreign exchange in Taiwan.

2. Via technology transfer, EPZs accelerated the development of Taiwan's industry. That is, a number of satellite industries gradually developed to supply the needs of EPZs and directly influenced the island's economy.

3. Via the rapid expansion of labor-intensive exports, EPZs have become an important source of industrial employment and have reduced the initial labor surplus.

Briefly, the contribution of EPZs to Taiwan is accelerating in export expansions and it has multifold significance. Throughout the past 37 years, land reform and U.S. economic aid has increased agricultural output and farmers' living standards, and induced local entrepreneurs to become investors in Taiwan's industrial and economic development. Stimulated by a cutoff of U.S. aid, the establishment of EPZs helped Taiwan develop an export-oriented economy and served as a conveyor of up-to-date technology. These approaches have successfully shifted Taiwan from an undeveloped to a developing country. Based on the smooth implementation of these approaches, Taiwan's foreign trade has grown dramatically and been praised as a successful model for other developing countries.
Chapter 3

CURRENT BOTTLENECKS OF INTERNATIONAL TRADE

Taiwan's foreign trade with its export-oriented policy has, in past years, generated much profit and placed the country in a favorable situation. On the other hand, a limited domestic market has created greater dependence on foreign trade and concentration in export markets in the United States and Japan. Taiwan thus faces a number of problems. These involve trade surplus with the United States, imports that are heavily dependent upon Japan, commercial counterfeiting problems, and massive foreign exchange reserves.

At the same time, the global economy has become more interdependent. That is, any country's policies, economic or political, may seriously affect other countries' economic development. Developed countries do their utmost to sustain superiority in their industrial output while most developing countries attempt to promote their industrialization. Accordingly, both developed and developing countries try to stimulate exports but, contrarily, block imports. Taiwan, faced with this sophisticated situation, is in a dilemma. How to solve these problems and break through trading bottlenecks have become important issues.
Trade Surplus with the United States

Taiwan maintains economic and cultural ties with the United States although she has received no economic aid from the United States since the mid-1960s. The break in formal diplomatic relations between Taiwan and the United States occurred at the end of 1978; nonetheless, Taiwan's bilateral trade with the United States has continued to exist and has grown rapidly.36

Taiwan is heavily dependent on overseas supplies of raw materials and export markets because of her limited natural resources and export-oriented strategy. The United States has dominated this trade, particularly in regard to Taiwan's export markets. This has led to a trade surplus in Taiwan's favor since 1967.37 During the last 10 years, 1975-1986, Taiwan's exports to the United States increased from U.S. $1.8 billion to U.S. $14.9 billion, and imports from the United States increased from U.S. $1.7 billion to U.S. $5 billion. The average growth rate per year in regard to exports to the United States was 20.9%, but imports from the United States were only 12.7% (see Table 2).

By 1985 Taiwan's two-way trade with the United States soared to U.S. $19.6 billion, accounting for 38.4% of Taiwan's total foreign trade, which made Taiwan the sixth largest trading partner of the United States. Meanwhile, Taiwan's exports to the United States of U.S. $14.8 billion
Table 2
Taiwan's Trade with the U.S.A.*

<table>
<thead>
<tr>
<th>Year</th>
<th>Exports Amount</th>
<th>% of total export</th>
<th>Imports Amount</th>
<th>% of total import</th>
<th>Total trade Amount</th>
<th>% of total trade</th>
<th>Surplus (+)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>1,822.7</td>
<td>34.3</td>
<td>1,652.1</td>
<td>27.8</td>
<td>3,474.8</td>
<td>30.9</td>
<td>(+) 170.6</td>
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<tr>
<td>1976</td>
<td>3,038.7</td>
<td>37.2</td>
<td>1,797.6</td>
<td>23.7</td>
<td>4,836.3</td>
<td>30.7</td>
<td>(+) 1,241.1</td>
</tr>
<tr>
<td>1977</td>
<td>3,636.3</td>
<td>38.9</td>
<td>1,963.8</td>
<td>23.1</td>
<td>5,600.1</td>
<td>31.3</td>
<td>(+) 1,672.5</td>
</tr>
<tr>
<td>1978</td>
<td>5,010.4</td>
<td>39.5</td>
<td>2,376.1</td>
<td>21.5</td>
<td>7,386.5</td>
<td>31.1</td>
<td>(+) 2,634.3</td>
</tr>
<tr>
<td>1979</td>
<td>5,652.3</td>
<td>35.1</td>
<td>3,380.8</td>
<td>22.9</td>
<td>9,033.1</td>
<td>29.3</td>
<td>(+) 2,271.5</td>
</tr>
<tr>
<td>1980</td>
<td>6,760.3</td>
<td>34.1</td>
<td>4,673.5</td>
<td>23.7</td>
<td>11,433.8</td>
<td>28.9</td>
<td>(+) 2,086.8</td>
</tr>
<tr>
<td>1981</td>
<td>8,163.1</td>
<td>36.1</td>
<td>4,765.7</td>
<td>22.5</td>
<td>12,928.8</td>
<td>29.5</td>
<td>(+) 3,397.4</td>
</tr>
<tr>
<td>1982</td>
<td>8,758.9</td>
<td>39.4</td>
<td>4,563.2</td>
<td>24.2</td>
<td>13,322.1</td>
<td>32.4</td>
<td>(+) 4,195.7</td>
</tr>
<tr>
<td>1983</td>
<td>11,333.7</td>
<td>45.1</td>
<td>4,646.4</td>
<td>22.9</td>
<td>15,980.1</td>
<td>35.2</td>
<td>(+) 6,687.3</td>
</tr>
<tr>
<td>1984</td>
<td>14,867.7</td>
<td>48.8</td>
<td>5,041.6</td>
<td>23.0</td>
<td>19,909.3</td>
<td>38.0</td>
<td>(+) 9,826.1</td>
</tr>
<tr>
<td>1985</td>
<td>14,770.3</td>
<td>48.1</td>
<td>4,746.5</td>
<td>23.6</td>
<td>19,516.8</td>
<td>38.4</td>
<td>(+) 10,023.8</td>
</tr>
</tbody>
</table>

*Unit: U.S. $ Million.

Source:
R.O.C., Foreign Trade Development of the Republic of China, 1985 (Taipei: Ministry of Economic Affairs, Board of Foreign Trade, 1986), Table 13, p. 25.
and imports from the United States of U.S. $4.8 billion left a deficit for the United States of U.S. $10 billion. The trade volume made Taiwan the third largest exporter to the United States, following Japan and Canada, in 1985.38

Although the United States is Taiwan's largest trading partner, Taiwan's continual escalating trade surplus with the United States has become a serious bilateral trade problem to the United States. Additionally, the perennial U.S. trade deficit, which has worsened in recent years, has increased public opinion against foreign trade in American business communities. The subject also is heatedly discussed in the U.S. Congress.

To right this imbalance, some urge restricting imports while others suggest expanding American exports. More than 300 protectionist bills have been proposed, one after another, in the U.S. Congress. The Jenkins and Thurmond Amendment Bills are the most important and typical.39 Thus far these two bills have been vetoed repeatedly by President Reagan in light of abiding by free trade, but it is expected that protectionist pressure will resurge in the U.S. Congress from time to time. In face of the pressure of mounting protectionism in the United States, Taiwan's chronic trade surplus with the United States has become unendurable to the United States. Taiwan's future bilateral trade with the United States will, without a doubt, experience many more challenges and tests.

24
The trade imbalance between Taiwan and the United States exists for several reasons. The major one is that Taiwan produces low-cost and increasingly high-quality consumer goods that are very competitive in the American market. The United States consequently imports large volumes of textiles, footwear, and electronic products from Taiwan every year. This is more economical than manufacturing them at home, the imported goods are reasonably priced, and their quality is attractive. In return, Taiwan's imports from the United States are primarily agricultural products (e.g., wheat, soybeans, and cotton), chemicals, and machinery. On the whole, American manufacturers' attempts to dominate Taiwan's market with industrial products is difficult because of consumer preferences, Japanese competition, and tariff barriers.

Taiwan's cheap, skilled labor permits the country's attractive-quality merchandise to enter the United States market at a low cost. Indeed, the labor force is one of Taiwan's most valuable assets. The youthfulness of the labor force and Taiwan's high standard of education increase labor's adaptability and speed of learning, and keep manufacturing costs low. For instance, the expansion of exports is concentrated on particular industries (textiles, clothing, canned foodstuffs, and electronic products) in which techniques, in part transferred from developed countries, become familiar to technicians and workers.
Accordingly, manufacturing cost, especially in the costs of learning, could be decreased.41

Furthermore, average wages in Taiwan are lower than in the United States. In 1985 the average monthly earnings of manufacturing employees in Taiwan was around U.S. $340.42 Even though wage rates are moving up with inflation, unit costs still are below the United States level. Aside from low wages, Taiwan's laborers work long hours in comparison with United States laborers. In 1985, for example, the average monthly working hours of manufacturing employees in Taiwan was 206 hours.43

Taiwan's high quality labor force, low wage rates, and longer working hours give the country a competitive advantage in labor-intensive products and encourage it to specialize in the production and exportation of these goods. United States investors would like to shift their production processes from the United States to Taiwan in terms of Taiwan's higher productivity, then repatriate the cheaper products in order to earn substantial profits in the U.S. market.

In 1976 the United States initiated a 10-year Generalized System of Preferences (GSP) under which duty exception privileges are offered to developing countries. Taiwan is one of the beneficiaries. Because Taiwan's light industrial products and processed agricultural products are entitled to these privileges, they have become very
competitive in the American market. This has led to sustained rapid growth in Taiwan's exports to the United States and a trade surplus in Taiwan's favor.\textsuperscript{44}

Taiwan has held 27\% of the share of GSP imports to the United States (more than any other country in the world), but the United States has not acquired the same treatment from Taiwan. In view of the imbalanced trade between Taiwan and the United States, the U.S. Congress is attempting to curtail the share allocated to Taiwan. If this comes about, it will be a terrible blow to Taiwan's critical trade relationship with the United States.\textsuperscript{45}

Because Taiwan takes on limited import liberalization, in order to protect developing domestic industries, American exports face considerable tariff and nontariff barriers in the Taiwan market. The trade surplus is, therefore, due partly to the high tariff structure and nontariff barriers.\textsuperscript{46}

Taiwan's customs duties, viewed as financial revenues for the government in past years, remain at a high level in general. For example, a number of imports, such as consumer goods and luxury items, have tariffs as high as 100\%; machinery, word processors, and home and kitchen articles also have excessive tariffs.\textsuperscript{47} Meanwhile, tariffs have been levied on a CIF (cost, insurance, and freight) rather than an FOB (free on board) pricing basis, giving American exporters an adverse position. That is to say, the
Japanese—America's strongest competitor in the Taiwan domestic market—have enjoyed much lower freight charges because of their proximity to Taiwan. Therefore, an item which costs exactly the same at the factory gate in the United States and Japan will carry a higher duty if it comes from the United States.\textsuperscript{48}

Taiwan's economic development is somewhat affected by the Japanese. The Japanese have successfully maintained a protected market against foreign producers by using nontariff barriers. Taiwan has tried to duplicate some of the approaches to protect its domestic industries.\textsuperscript{49} As a result, nontariff barriers have built up, one after another, against imports of a number of goods and services. These various import bans are implemented by administrative order or by denying import permits. In this sense, American exports often are subject to bans or severe limitations. Under nontariff barriers foreign businessmen are allowed a limited scope in insurance, accounting, shipping, and other services. Thus American firms face difficulties selling services to Taiwan.\textsuperscript{50}

Heavy competition from Japan is another major obstacle to expanding U.S. imports to Taiwan. Via its proximity to Taiwan, Japan has more trading advantages in the Taiwan market than does the United States. In addition to lower shipping charges, Japanese vendors have advantages such as
shorter delivery time and quicker backup on parts and services.

The time difference between Taipei and Tokyo is an hour; it takes but two hours by plane from Tokyo to Taipei. The cost of transporting a salesman to Taipei from Japan is cheaper, perhaps by half, than from the United States. When considering time and cost, Japan can provide more proximate and convenient after-sales service to Taiwan than can the United States.\textsuperscript{51}

Reversing the long-term imbalances on trade, which have been a matter of serious concern between Taiwan and the United States, cannot be done overnight. But progress—bilateral trade negotiations—should be made. With the continuing efforts of both countries, the rate of improvement should accelerate.

Taiwan should try to decrease dependence on the United States, which would make Taiwan's foreign trade less vulnerable to fluctuations in the American economy. It is expected that some of Taiwan's exports will be restricted in the near future by protectionism in the United States because legislators supported by economic interest groups have increased pressure on the Reagan administration. Taiwan does not, therefore, need to concentrate trade exclusively on the U.S. market. It ought, rather, to diversify its exports to Europe or other regions of the world, thereby dispersing its risk on international trade.\textsuperscript{29}
Under the U.S. Generalized System of Preferences (GSP), Taiwan with U.S. $3 billion of its exports gaining duty-free entry to the United States in 1984, is ranked the top beneficiary among 140 developing countries and territories. Any country and its products which benefit from the GSP will "graduate" one after another from the GSP's list sooner or later. Taiwan is no exception.

Taiwan's exports cannot heavily depend on the GSP and hope to enjoy long-running duty-free advantages, and Taiwan must, therefore, quicken her pace to graduate from the GSP's list as soon as possible. In other words, if Taiwan expends efforts to revamp her industrial structure and promote her industry from labor-intensive to technology-intensive products with low cost and high quality, it will have more comparative advantages in the American market even without GSP's protection.

Taiwan's current tariffs average a high 7.8%--which often are criticized by American exporters. What is more incredible is that Taiwan levies a 60% protective tariff on imports of textiles and footwear when she has dominated most market shares in the United States for many years. Also, there is a 50% tariff on imported umbrellas--and Taiwan is the world's largest producer. In truth, these industries (textiles, footwear, and umbrellas) ought to be able to stand by themselves without continual protection.
Today Taiwan, with tremendous foreign exchange reserves, can afford to open her markets further. If Taiwan intends to stimulate domestic markets, she must lower unreasonable import duties. This would also reduce the trade imbalance with the United States, lower consumer prices, increase domestic consumption, and help stimulate production and the economy as a whole.

Nontariff barriers might be needed to protect domestic infant industries. On the other hand, some industries in Taiwan, automobiles, for example, have been protected for many years by various kinds of import bans and still cannot stand on their own. This kind of nontariff barrier should be discontinued because industries under long-term protection become weak and dependent upon it. Import liberalization, in place of nontariff barriers, would help develop and stimulate weak industries via American technology and capital goods purchased. It also could narrow the growing trade gap with the United States.

Taiwan's markets are small, but their potential buying power is good. Taiwan has not, however, been able to develop in some fields of high technology and she needs to acquire this know-how from developed countries. The United States must take advantage of this opportunity to catch the market share of Taiwan's imports. In view of the heavy competition from Japan, though, American vendors should emphasize after-sales service—as do the Japanese in Taiwan.
To meet this problem, American vendors must employ local agents or distributors in Taiwan, and stock parts and service equipment. Building and maintaining good reputations means that U.S. companies must send technicians to Taiwan regularly to ensure that the parts are stocked, technical skills are kept up, and customers' needs are satisfied. Through these approaches the United States would improve its market position in Taiwan.

Of course, Taiwan cannot declare a preference for free trade and import liberalization one day, then wipe away all tariff or nontariff barriers the next; but, unfair trade deserves correction. On the other hand, Taiwan's natural resources are limited; it is necessary to import raw materials for her industry and manufacturing. If other countries slam their doors and close their markets for protectionism, Taiwan cannot survive. Free trade and import liberalization are Taiwan's only options for balancing the trade surplus with the United States, the country's future development in international trade, and the island's economy as a whole.

Imports Depend Heavily Upon Japan

After World War II Japan benefited greatly from the tolerant and kind treatment of the Chinese and their government, and gained much via trade with and investments in Taiwan the past three decades. Similarly, the Republic of China benefited from
contacts with Japan. These included the experience of Japanese economic development, the introduction of technology from Japan, and the diffusion of management skills.\(^5\)

Thus, in terms of geographic propinquity, historical background, business practices, and approximation of levels of technological development, Taiwan and Japan have maintained a close relationship with one another.

Despite the break in diplomatic relations in 1972, two-way trade between Taiwan and Japan scarcely was affected. Ironically, Taiwan's bilateral trade with Japan is the inverse of that with the United States (see Table 3). That is, as Taiwan's largest supplier, Japan has enjoyed a consistent surplus in bilateral trade since 1946.\(^5\) Although the bilateral trade conditions with Japan have been unfavorable, Taiwan's trade deficit has increased—as well as her economic development and export boost.

In the past 10 years, 1975-1984, Taiwan's imports from Japan increased from U.S. $1,812 million to U.S. $6,442 million, and exports to Japan increased from U.S. $694 million to U.S. $3,187 million. In other words, Taiwan's trade deficit with Japan soared from U.S. $1.118 million to $3,255 million. In 1985 Taiwan's two-way trade with Japan totaled U.S. $9,014 million: exports to Japan were U.S. $3,460 million and imports from Japan were U.S. $5,554
Table 3
Taiwan's Trade with Japan*

<table>
<thead>
<tr>
<th>Year</th>
<th>Exports</th>
<th>Imports</th>
<th>Total trade</th>
<th>Deficit (-)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Amount</td>
<td>% of total export</td>
<td>Amount</td>
<td>% of total import</td>
</tr>
<tr>
<td>1975</td>
<td>694.2</td>
<td>13.1</td>
<td>1,812.2</td>
<td>30.4</td>
</tr>
<tr>
<td>1976</td>
<td>1,094.7</td>
<td>13.4</td>
<td>2,451.5</td>
<td>32.3</td>
</tr>
<tr>
<td>1977</td>
<td>1,120.1</td>
<td>12.0</td>
<td>2,643.0</td>
<td>31.1</td>
</tr>
<tr>
<td>1978</td>
<td>1,570.3</td>
<td>12.4</td>
<td>3,678.1</td>
<td>33.4</td>
</tr>
<tr>
<td>1979</td>
<td>2,248.6</td>
<td>14.0</td>
<td>4,561.4</td>
<td>30.9</td>
</tr>
<tr>
<td>1980</td>
<td>2,173.4</td>
<td>11.0</td>
<td>5,353.2</td>
<td>27.1</td>
</tr>
<tr>
<td>1981</td>
<td>2,478.7</td>
<td>11.0</td>
<td>5,928.6</td>
<td>28.0</td>
</tr>
<tr>
<td>1982</td>
<td>2,377.8</td>
<td>10.7</td>
<td>4,780.2</td>
<td>25.3</td>
</tr>
<tr>
<td>1983</td>
<td>2,477.1</td>
<td>9.9</td>
<td>5,586.7</td>
<td>27.5</td>
</tr>
<tr>
<td>1984</td>
<td>3,186.5</td>
<td>10.5</td>
<td>6,441.8</td>
<td>29.3</td>
</tr>
<tr>
<td>1985</td>
<td>3,459.9</td>
<td>11.3</td>
<td>5,554.4</td>
<td>27.6</td>
</tr>
</tbody>
</table>

*Unit: U.S. $ Million.

Source:

Taiwan's trade deficit with Japan was reduced 35.9% in 1985 because a series of promotional activities produced adverse effects. On the whole, in 1985 Taiwan's two-way trade with Japan accounted for 17.7% of Taiwan's total foreign trade, next to the United States. Japan accounted for 11.3% of Taiwan's exports, and 27.6% of the imports (see Table 3), which made Japan the largest exporter to Taiwan.59

Taiwan's trade deficit with Japan has existed many years. Taiwan has attempted to adjust her trade relations with Japan, but it has been difficult to substantially narrow the gap. The perennial trade deficit with Japan can be attributed to five factors.

First, Taiwan was ruled by the Japanese for about 50 years. Some entrepreneurs, especially those in the senior generation educated under Japanese colonial administration, share a cultural bond with the Japanese. This colonial heritage tends to make Taiwan businessmen prefer to cooperate with the Japanese rather than with Americans. In addition a subjective, obstinate ideology has grown among industrialists and consumers that Japanese products are superior in quality to American ones. Consequently Japanese goods, such as machinery, capital equipment, or consumer
goods, are exported to Taiwan in whopping quantities every year to meet the needs of industrialists and consumers. This is another basic reason why Japan dominates the largest share of Taiwan's import market.

Second, because Japan has a restrictive policy toward the importation of manufactured products, most of Taiwan's exports to Japan are low-valued agricultural commodities and processed products such as bananas, canned food, textiles, and manufactured metals. Taiwan's demand for Japanese imports are costly capital goods and raw materials such as machinery and tools, transportation equipment, and iron and steel, which Taiwan needs for her industrial development. Obviously, the difference in the import/export structure between Taiwan and Japan generates an imbalance in Japan's favor. This unfavorable situation, which has existed for decades, contributes to the enormous trade gap between the two countries.

Third, Taiwan's economy is heavily dependent on foreign technology to support her economic development. Taiwan wants to upgrade her technology and attain greater self-reliance through imported technical skills. Japan has been the preferred technological source because of the geographical proximity between Taiwan and Japan, and the relative ease with which Chinese and Japanese work together. From 1952 through 1984 Japan has accounted for
65% of the technical cooperative ventures in Taiwan compared to the 22% of the United States.  

Japanese firms accept cooperative agreements in order to sell their parts and raw materials to local manufacturers in Taiwan. The Taiwanese firms then assemble the parts into finished goods. The cooperative agreements provide the Japanese companies with extensive control of the production processes in their host country firms. The Japanese don't, however, provide the Taiwanese with the sought-for technology. The cooperatives have not produced the greater technological independence that Taiwan desires. But they have promoted trade; Taiwan has become a profitable parts and raw materials market for Japan.

Fourth, Japan handles the major portion of Taiwan's import market because she is in an ideal position to attract Taiwan businessmen and consumers to purchase Japanese goods. That is, as previously noted, Japanese vendors promote their products via excellent distribution networks and after-sales service organizations in Taiwan. Also, Japanese vendors are attempting to enter the domestic financial market with low interest rates. For example, Japanese computer manufacturers are offering unusually long-term leases on their machines; lessees enjoy nominal or no lease payments for the first year or two of their leases. The Japanese are using these strategies to channel control of the market share in Taiwan.
Fifth, as do many developing countries, Japan has adopted high tariff rates and nontariff barriers to protect her domestic market. Taiwan's exports to Japan often are subject to restrictions and strict examinations. Vegetables and fish particularly are restricted by high tariff rates; machines and automobile parts are prohibited for quality and security reasons. Because Taiwan businessmen seldom hold product promotion activities in Japan, they cannot precisely understand consumers' tastes and, thus, cannot enter the Japanese market.

In face of the perennial trade deficit with Japan, Jack F. Williams pointed out the basic approach to solve the problem:

This trade imbalance with Japan is unlikely to be solved until Taiwan's economy is developed to a level high enough that it no longer needs the technology and high-quality consumer goods of Japan but can produce them on the island itself.

Taiwan must, therefore, seek advancement in technology, improve her industrial structure, and upgrade the quality of her products so that she may export more to and rely less on Japan for imports. Furthermore, Taiwan has to strengthen her base for foreign trade and intensify technical coordination with North American and European countries so as to improve her overall marketing functions.

Adjusting Taiwan's trade relations with Japan requires expanding Taiwan's exports to Japan. Before doing this, the government and business community should send a survey team.
to Japan to acquire a better understanding of the fundamental characteristics of the Japanese market and consumers' preferences. Too, the government should strengthen the organization of business communities by helping Taiwan traders exhibit their products in Japan and explore the possibility of future sales outlets.

Although the trade imbalance with Japan cannot be solved within a short time, Taiwan must continue her efforts and take advantage of the recent policy of the Japanese government to gradually open the market to augment Japanese market shares. The value of Japanese yen has risen steadily. This should make it advantageous for Taiwan to increase exports to Japan.68

Commercial Counterfeiting Problem

An internationally famous cosmetic manufacturer had to go to Taiwan personally to halt a "Mom and Pop" operation that was not only counterfeiting his product locally but selling it on the international market. He found the product excellently copied, so good in fact, that he ended up starting to buy the glass containers which had been copied after his original and manufactured in Taiwan.69

The protection of property rights, including patent copyrights and trademarks, has created problems in Taiwan. Local manufacturers can produce cheap and nice counterfeits of Rolex watches, Gucci handbags, Vaseline hair tonic, and other hot-selling consumer products. For example, an imitation $1,450 Cartier Santos watch sells for $23 in
Taiwan. Before last year, copies of the IBM personal computer appeared under the names Pineapple and Orange. These models have been denied importation by U.S. Customs and Taiwan has been accused of violating copyrights and patents.\(^{70}\)

The counterfeiting problem has become a worldwide phenomenon. It exists in many developing countries, including Singapore, Hong Kong, Korea, Thailand, mainland China, Mexico, Colombia, and others trying to take a shortcut to economic success.\(^{71}\) Over the past several years many developed countries, especially the United States, have experienced a rising tide of counterfeit products from developing countries. They have counterattacked by adopting legal actions and media campaigns, and exerting economic and political pressures upon the developing countries.

The government in Taiwan recognizes the seriousness of counterfeiting problems and has tried to crack down on them. Still, in 1982 Taiwan was identified as the world's major source of counterfeit goods by the International Anticounterfeiting Coalition.\(^{72}\) In 1985 Taiwan passed amendments to her trademark and copyright laws. Under the new laws the penalties for counterfeiting trademarks registered in Taiwan, or reproducing the intellectual work of another without authorization, are raised to a maximum of 5- and 3-year imprisonments, respectively.\(^{73}\) Nonetheless,
counterfeiters generally receive light sentences which do not serve as strong deterrents to violators. For example, from January to July 1985, 353 persons were adjudicated guilty in counterfeiting cases, but only four were sentenced to one to two years imprisonment—a mere 1.1% of the total cases (see Table 4).

Table 4

Statistics of Judicial Judgment in Counterfeiting Cases from January to July 1985

<table>
<thead>
<tr>
<th>Type of case</th>
<th>No. of persons punished</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total</td>
</tr>
<tr>
<td>Trademark infringement</td>
<td>297</td>
</tr>
<tr>
<td>Patent infringement</td>
<td>29</td>
</tr>
<tr>
<td>Copyright infringement</td>
<td>27</td>
</tr>
<tr>
<td>Totals</td>
<td>353</td>
</tr>
</tbody>
</table>

Source:

The infringements result in monetary damages to the infringed parties, and to the leading astray of entire industries and smearing of the nation's image as well. Furthermore, counterfeiting has generated negative effects on the business and investment climate. Foreign investors
cite poor patent protection as a primary reason for their reluctance to take high technology to Taiwan.\textsuperscript{74}

The causes of counterfeiting are complicated. A major cause of counterfeiting is generated by international firms that specifically and persistently engage in the importation of counterfeit goods to other countries. They shuttle between developing countries with a variety of samples of best-selling commodities, take advantage of low labor costs in those countries, and produce large quantities of counterfeit goods. Then the goods are shipped around the world. Sometimes the manufacturers in the developing countries are not aware their mass production of the samples constitutes counterfeiting. When a country implements strong measures against counterfeiting, the international firms transfer their activities to another country.\textsuperscript{75}

The shortsightedness of Taiwan's industrialists is another cause of counterfeiting. During the past two decades Taiwan has experienced rapid economic development and is trying to develop more technology-intensive industries. Many local industries have acquired the technological capability to manufacture a wide variety of products, but they have invested little in research, development, or marketing. Because they are lagging behind, the industrialists are tempted to use the trademarks, research, and developmental efforts of others as a shortcut to financial success.
Some industrialists in Taiwan are not well-educated. They fear high technology—and failure. They hesitate to design new products, create new brands, establish marketing channels, and exploit new foreign markets. Rather than cooperate with governmental directives to invest money in research and development, they pursue self-interests via counterfeiting. As long as their products are lucrative, their fear is less when they risk imitating hot-selling, popular products and inundating the international markets at discount prices.76

In practice, these speculators realize that cranking out low cost copies cannot continue. At the same time, an old Chinese proverb is deeply rooted in their minds: "It is better to be the head of a chicken than the tail of an ox." Each wants to acquire maximum profits for as long as possible regardless of the consequences.77

Counterfeiting has disclosed that a serious gap exists between manufacturing capacity and marketing, research, and development in Taiwan. To overcome this weakness, the government should require industrialists to spend a fixed percentage of annual sales on research and development. This would encourage them to design new products and generate a greater incentive to develop marketing expertise.78
In addition to emphasizing research and development, the government should consider the following as other ways of combating the counterfeiting problem:

1. Increasing penalties for counterfeiting and refusing to commute imprisonments into fines.

2. Forming a professional tribunal on trademarks, patents, and copyright matters to facilitate the adjudication of counterfeiting cases.

3. Upgrading the status of the Anticounterfeiting Committee to strengthen the Committee's role in the planning, supervision, and coordination of a nationwide campaign against counterfeiting.

4. Stepping up the cultivation of talents in the field of commercial design and encouraging creative work in an effort to eliminate counterfeiting.

5. Accelerating social education to instill correct ideas into the minds of the people re the protection of property rights that should not be infringed upon or used arbitrarily.  

If these methods were strictly implemented, the counterfeiter gradually would vanish. In the meantime, the counterfeiting issue has greatly hindered Taiwan from launching into a new era of trading development. If Taiwan wishes to sustain a good standing in the international economic community, and attract foreign investment, technology know-how, and international trade, she must make
every effort to shed her copycat image. Although Taiwan has a long way to go before her copyright and trademark protection meets standards expected in the developed world, she must persuade her industrialists to look beyond their immediate quick profits and lift their visions toward larger, more lasting gains.

A Burden as a Result of the Massive Foreign Exchange Reserves

In its increasing access during the past 30 years to the bounty of an affluent society, the Republic of China on Taiwan has accumulated massive and still-growing foreign exchange reserves. It is now awash in an overflow of idle capital. Meanwhile, various sectors of the economy, the overall society, and especially of industry cannot find the financial investment needed to improve their structures and technology for future challenges. After their long voyage from an island backwater to a status as one of the world's better-off national communities, both our people and government must face a truly big problem: "How to use money?"80

Many developing countries worry about their onerous foreign debts, but Taiwan wonders how to digest massive foreign exchange reserves. As of January 1986 Taiwan had a foreign debt of only U.S. $5 billion, but she has accumulated U.S. $26.1 billion in foreign exchange reserves. The Central Bank of China holds U.S. $22.5 billion and nine commercial "foreign exchange" banks hold approximately U.S. $3.6 billion. It is expected that reserves could reach U.S. $35 billion at the end of 1986. The size of Taiwan's foreign exchange holding is ranked fifth in the world behind
West Germany, the United States, Japan, and France. The total account is equal to the combined foreign exchange reserves of Canada, South Korea, and the five ASEAN members (the Philippines, Indonesia, Malaysia, Thailand, and Singapore).

According to a general standard, a country should have foreign currency sufficient to purchase three to six months worth of imports. In 1985 Taiwan imported U.S. $20 billion worth of goods which required a monthly expenditure of about $1.6 billion. With the Central Bank holding U.S. $22.5 billion, Taiwan's foreign exchange reserves can purchase 13 months worth of imports. It is obvious that the reserves are in excess of the normal standard and that they represent idle money.

While the massive accumulation of foreign exchange reflects that the consecutive trade surpluses were achieved by Taiwan because of her success in export expansion, it also creates a serious problem. That is, the huge amount of idle foreign exchange reserves was deposited in local banks or abroad to earn interest; it was not appropriately invested in upgrading the overall economy, the industrial structure, and elevating living standards.

In general, 90% of Taiwan's imports are raw materials and machines which are used to support the island's industrial development. In recent years Taiwan's economy has faced a labor-intensive/technology-intensive transition,
but some industries have failed to adequately maintain and replenish equipment and machines. Additionally, the government's economic orientation and alternative paths are unclear. Thus a willingness to invest, via public or private sector, remains low.  

Taiwan's capital investment in raw materials and equipment has declined since 1980. In 1980 the capital for public and private industries totaled New Taiwan Dollar (NT $) 456 billion, which accounted for 31% of the GNP. By 1985 the capital for public and private industries was almost unchanged at NT $455 billion, but it accounted for only 19% of the GNP.  

In the wake of the decrease in capital investment, the annual imports of raw materials and machines also declined. As long as public or private willingness to invest remained low, the imports of capital investment would not increase. Furthermore, the overabundant foreign exchange reserves of trade surplus--exports over imports--would continue to increase as well.  

On the other hand, the high foreign exchange reserves and low capital investment signify that Taiwan has not developed an appropriate capital market to transform its savings into investment. That is to say, Taiwan's huge amount of export earnings flow into short-term foreign securities rather than into long-term domestic investments. Most of this huge foreign exchange surplus has been used
to purchase foreign national bonds, mostly U.S., with a yearly payoff of about 10%. Should the rates of foreign exchange fluctuate drastically, the foreign currencies deposited in foreign banks would incur a great loss if risk were not dispersed.

Under the present successive trade surplus, the NT Dollar has been forced to appreciate in order to curb increases in the foreign exchange reserves. This situation puts the government and industries in a dilemma and is forming a latent crisis to Taiwan's future economic development four ways:

1. It will discount the value of foreign exchange reserves whether deposited in local or foreign banks.
2. Due to the appreciation of NT Dollars, Taiwan's exports will become less competitive—especially during a growing economic recession.
3. If economic recession persists, it will result in high unemployment and directly impact public living standards.
4. If worse comes to worse, Taiwan will lose her ability to improve the country's overall economic and social structure as well as competitiveness in markets around the world.

The most direct and effective way to resolve the massive foreign exchange reserves is to open up Taiwan's markets through import expansion. This method would not
only enable local people to enjoy a higher quality of life but allow other countries to participate in foreign exchange with Taiwan and stimulate their economic growths also. Meanwhile, increasing imports can force domestic industries to upgrade their product quality, make their operations more efficient, and reach new milestones through competition.88

In case of an overall economic transition, every sector of Taiwan—industrial, technological, research and development, the basic infrastructure, the environment, and education—needs money for further development. Because public and private willingness to invest remains low and most industrialists don't know how to make appropriate investments, the government should draft an investment program that would include equipment replenishment, productivity promotion, marketing strategies, and efficient management to guide hesitant industrialists.89 As the investment climate warmed and assumed shape, the mass of frozen idle capital would thaw and find an outlet.

Besides increasing domestic investment, the Taiwan government must encourage industrialists to engage in overseas investments because the massive foreign exchange reserves serve as potential assets. Before, Taiwan's foreign exchange was deficient. Capital that flowed out of the country was viewed as a kind of capital loss. Thus the government restricted the overseas activity of Chinese firms
in regard to the amount that could be invested and set stipulations on the debt/profit ratio.

It's another story today. If Taiwan approaches overseas investment, especially in the United States, it could acquire four advantages:

1. Digesting the overabundance of idle capital.
2. Offsetting the pressure of foreign protectionism.
3. Having access to foreign markets, management, and high technology.
4. Elevating Taiwan's economic and trading status in the world.90

Via overseas investment Taiwan can strengthen its competence to meet the competitive trading challenge of developing countries. The foreign exchange reserves resemble a reservoir that can release excessive water and let needed water flow in. How to control the floodgate of foreign exchange reserves while avoiding inundation or insufficiency is the government's obligation.

If Confucius were alive today, he would not say, "Worry not about scarcity but uneven distribution; worry not about poverty but instability." He would be more likely to say, "Worry not about sufficient funds but low investment; worry not about wealth but how to use it."
Chapter 4

FUTURE PROSPECTS

Strong Competition from South Korea

Like Taiwan in past decades, South Korea has been acclaimed one of Asia's Four Dragons due to its soaring economic achievement. Although South Korea is facing a number of political challenges from North Korea's military threat, students' demonstrations, and the political pressures of opposing parties, it has not discarded its ideal to march toward a country with great economic power. Furthermore, South Korea announced that when it hosts the Olympic Games in Seoul in 1988, it will do so in the guise of a fully advanced country.\(^1\)

Taiwan and South Korea have basically identical cultural backgrounds that stem from the Confucian discipline. Confucian devotion to education molds people who are literate and ambitious. As Confucian believers, Taiwan and South Korea are progressing rapidly in economic development and international trade and are displaying remarkable achievements. South Korea acts more intrepid than Taiwan and is more ahead in some respects. Today, South Korea is a strong competitive rival to Taiwan in international trade.
Taiwan and South Korea took a similar approach, by export expansion means, to stimulate their economic growths, but South Korea preferred a devaluation policy, without regard to inflation, to promote its exports. Unlike South Korea, Taiwan stressed price stability with a view to avoiding economic unsteadiness and inflation. As a result, South Korea's export prices in U.S. dollars have gradually become more competitive than Taiwan's prices in recent years.  

In addition, South Korea upgraded industrial exports with greater intensity than Taiwan. In other words, the South Korean government directly interfered in the country's industries in order to acquire dramatic gains in industrial growth and export performance. Consequently, under the government's power a number of small companies were forced to merge. Several conglomerates were formed such as Hyundai, Daewoo, and Samsung.

The government supports these conglomerates by foreign debts. These conglomerates also responded to government directives to invest in research and development, purchase advanced technology from overseas, and establish commercial information networks in developed countries. Presently, through trial and error, South Korea has built up steel, automobile, and shipbuilding industries which can compete directly against Japan. Last year South Korean automobiles replaced Japanese cars as Canada's No. 1 import. This year
Hyundai's new car, the Excel, went on sale in the United States, and orders were strong.  

The government in Taiwan used less pressure and fewer inducements to persuade private enterprises to merge and form conglomerates than did South Korea which had mammoth industrial groups driving the entire economy. Contrarily, numerous small companies exist in almost every industry in Taiwan because everyone wants to be a company president. According to 1983 data, 85% of all factories employed fewer than 50 workers and 89% had fixed assets worth less than US $250,000.  

In the past years these small companies, which primarily were family-oriented, contributed much to developing Taiwan's international trade. They also revealed weaknesses in changes in the world trade picture and South Korea's strong competition. The major weakness is that the companies are too small to do their own marketing overseas. They have too little capital and experience to invest in high technology and elbow aside multinational competitors in foreign markets.  

Taiwan, with her massive foreign exchange reserves--unlike South Korea which had only U.S. $2.6 billion in foreign exchange reserves and a foreign debt that reached to $45 billion in 1985--has the capital and capability to compete with South Korea. In order to meet South Korea's strong competition and catch up with her industrial
exports, Taiwan should merge the out-of-date and family-run companies. The government must offer subsidies and tax concessions to companies investing in high technology industries. Ultimately, for the purpose of overtaking South Korea's marketing strategy, Taiwan must set up marketing networks and distribution channels in the world to collect commercial information and gain a bigger market share in foreign countries.

**Effects of the Open-door Policy of Mainland China**

When Deng Hsiao-ping took over the Communist regime in 1978, mainland China opened her door and engaged in economic reform which involved the marketization of transactions and privatization of property rights. Furthermore, this reform opened foreign capitalist trade, loans, and investments. This helped the backward economy that resulted from mainland China's self-imposed 20-year isolation. Whether or not Deng's economic reform succeeds or fails, it has at least provided an opportunity for Chinese people to become acquainted with the Western world and touch the capitalistic society.

Along with her open-door policy, mainland China has actively involved herself in foreign trade. More and more "Made in China" products are being rushed into international markets, especially the American market. Most
of the mainland China exports to the United States are cheap textiles and garments, which are Taiwan's major exports also, second to electrical machinery and apparatus. In face of the pressure in the American market from the low-wage competitor of mainland China, Taiwan would gradually lose her advantage in the cloth and clothing trade. What's more, if mainland China persists in her current economic reform, it is expected that mainland China will catch up with Taiwan's exports in footwear, toys, canned foods, sporting goods, and paper products in the future.98

Mainland China launched a series of peaceful overtures for establishing "three links" (mail, trade, and air/shipping services) with Taiwan as a first step toward the ultimate goal of reunification. Taiwan has tenaciously insisted on a "three no" policy (no contacts, no negotiation, and no compromise) with her old enemy.99 It's interesting that, indirectly, a trading relationship between Taiwan and mainland China has been forming since the late 1970s. This has grown significantly up to the present time.100

Official Taiwan figures show that total indirect trade was U.S. $51,000 in 1977. That figure jumped to U.S. $21 million in 1979, U.S. $242 million in 1980, and U.S. $390 million in 1981.101 In 1984, total indirect trade came to U.S. $560 million and to U.S. $1.5 billion in 1985 of which Taiwan's exports accounted for 77%.102 Most of the indirect

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trade passes through Hong Kong, Singapore, or Japan, which then is sold to mainland China. The major Taiwan exports to mainland China are older-model motorcycles, black-and-white TV sets, and machinery; mainland China exports only cotton and Chinese medicines to Taiwan.103

Direct trade with mainland China is illegal in Taiwan now. The Taiwan government does not, however, interfere with indirect trade because the "Made in Taiwan" products are sold to buyers (middlemen) in Hong Kong or Japan. As before stated, Taiwan is deficient in natural resources and raw materials which mainland China can supply sufficiently, yet Taiwan's highly productive industrial economy can manufacture many products such as calculators, electronics, appliances, machinery, and so on which currently are much in demand in mainland China.

In theory, through indirect trade it appears that there will be an economic complementarity between Taiwan and mainland China.104 Too, it will give Taiwan a chance to enter this big market and demonstrate the superiority of her economic system. In reality, with respect to political issues, indirect trade is very complicated; it is far from being clear and simple.

Taiwan has two concerns: how long mainland China's open door policy will be in effect and how dependable the mainland market is. If, in the indirect foreign trade relationship, Taiwan becomes overly dependent upon mainland

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China, Taiwan would have difficulty surviving should the relationship suddenly terminate. Indeed, her overall economy would be bankrupt. It is hoped that the growing trade is the result of natural forces deriving from the increased liberalization of economic planning and trade on mainland China.105

In general, trade is more or less risky—whether with mainland China or other foreign countries. The Taiwan government cannot, therefore, adopt a "head in the sand" policy to evade the indirect trade issue with mainland China. The government ought, instead, to provide her manufacturers and traders with information about marketing in mainland China, and teach the businessmen how to disperse trade risks if they want to penetrate the mainland China market through middlemen. By means of indirect trade, opening the mainland China door wider should be pleasing to the Chinese in both countries.

**Governmental and Entrepreneurial Efforts**

Now, spurred by intense competition from lesser developed areas with cheaper labor, Taiwan's economy is undergoing a second transition. The traditional industries in Taiwan, such as textiles and the assembly of consumer electronic products, served the island well when her economy was in the early stages of industrialization and there was a huge amount of inexpensive manpower to be employed.
Today, because of an increasing standard of living, labor in Taiwan is not as cheap as before. The labor-intensive industries, which gradually have become sunset industries, are unable to effectively compete in the international market against the cheap labor of Malaysia, Indonesia, Sri Lanka, and mainland China.106

Under these circumstances the Taiwan government and her industrialists need to understand that there is only one way to go. The country's future development in foreign trade is dependent upon upgrading industries in the direction of more sophisticated capital and technology-intensive operations such as computers and precision machinery. Success will require large amounts of human capital in the form of skilled laborers, technicians, engineers, and managers.

The government should expand and improve vocational and technical education to cope with the future technical and mechanical needs. Also, the industrialists could hire executives and managers from developed countries as technical advisors and managers in the factories.107 The government or the industrialists could try to lure overseas Chinese employed in high technology companies in advanced countries to return home, and use them to set up and promote high technology methods in Taiwan.

International trade today has become increasingly oriented toward marketing rather than production. Collecting and transmitting market information promptly to
traders presently is weak in Taiwan. The government should try to establish a nationwide commercial information center for exporters. Through this center, manufacturers and exporters could obtain appropriate information that would enhance understanding about which kinds of products are competitive and which potential foreign markets are worth exploiting. It could educate exporters learning to evaluate their competitors' strong and weak points and assist them in analyzing new market trends.108

In view of the changing international market and rising wages, the future prospects of Taiwan's foreign trade will rely on how rapidly Taiwan can transform its labor-intensive industries into technology-intensive industries. Timing is a critical factor. The Taiwan government and the industrialists must accelerate their pace to improve the island's industries in order to upgrade Taiwan's competition in international markets.
Chapter 5

CONCLUSION

International trade is vital to Taiwan. Throughout the years, under a strong and stable economic system, Taiwan has built a solid foundation for its foreign trade. In the 1970s two oil shocks and two political shocks—the 1971 expulsion from the United Nations and the 1979 withdrawal of U.S. diplomatic recognition—rendered Taiwan a terrible blow, but success with the export expansion policy has enhanced Taiwan's self-reliance and her trade capabilities. Furthermore, it has proven that the island's economic and trading achievement can withstand any test of radical shifts in the international community.

In the past years the world economic situation has undergone some unfavorable changes. Sentiments of protectionism have risen to an unprecedented height in most developed countries and have adversely affected Taiwan's foreign trade. In addition, Taiwan's foreign trade has reached a peak and some products, when compared with those of cheap-labor developing countries, have lost their competitive advantage.

Under economic transition, today Taiwan's foreign trade faces a number of problems. The essential question is how...
to identify, develop, and exploit new areas of comparative advantage in the future international environment.

Facing such a double challenge from developed countries and developing countries requires that Taiwan revamp her industrial structure, increase her productivity, and secure raw material sources in order to support sustained export growth. Taiwan has to internalize her economy and liberalize all import restrictions and, thereby, stimulate domestic industries toward advanced development. Moreover, commodity and market diversification are urgent.

The Taiwan government and business community have accumulated substantial experience in adapting themselves to new situations at each initial juncture. The government and businessmen have, therefore, sufficient competence to take appropriate approaches when coping with today's trading obstacles. With a concerted effort of the government and the people, Taiwan ought to be able to achieve a new milestone in the course of her trading development. If successful, Taiwan's struggle in international trade will be a beacon of hope and a source of motivation to others facing the same kind of trading problems.
ENDNOTES


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22 Ibid.


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