

# **Taiwan and China: Exploring the Limits of Economic Integration**

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# Taiwan: Cross-Straits Disappointment

## Relative Performance of Taiwan's Stock Market in the Past Two Years



Source: finance.yahoo.com

# Just a Matter of Time ...

*“Taiwan, HK, and China are all economically and culturally integrated to the extent that separation really doesn't make sense anymore. Of course, HK is still a ‘Special Administrative District,’ and it has its own currency and a distinct dialect, but HK folks have a 70% stake in nearby businesses in Guangdong & nearby provinces. And I suspect that the only thing that the Taiwanese and the mainlanders will argue about is who speaks Mandarin with a better accent. I'll probably give Taiwan another 15 years or so before all of ‘Greater China’ officially becomes one again (HK already is a part of China with a special status). If you talk to any of the locals in Taiwan or HK, you'll probably hear that's what they think too.”*

*Posted by: Sam at April 28, 2007 12:12 PM*

# Southern Manhandling

PLAY THIS AGAIN!



Chinese envoy attacked in Taiwan

Pro-independence protesters in Taiwan have jostled a Chinese envoy to the ground and attacked his car.

Source: <http://www.youtube.com/watch?v=wuozDzoflhw>, accessed 10/29/08

# Taiwan Growth More Synchronous with China

## Output Correlations between China and Selected Economies

Economy	Time Period	Output Measured in:			
		Local Currency	LC, per capita	PPP	PPP, per capita
<i>Taiwan</i>	1979-2002	0.32	<b>0.27</b>	0.47	0.36
	1991-2002	0.56	<b>0.53</b>	0.59	0.55
<i>Korea</i>	1979-2002	0.16	0.13	0.27	0.20
	1991-2002	0.13	0.05	0.26	0.19
<i>Japan</i>	1979-2002	-0.13	-0.24	0.38	0.28
	1991-2002	0.04	-0.02	0.30	0.24
<i>Hong Kong</i>	1979-2002	0.18	<b>0.14</b>	0.44	0.30
	1991-2002	0.42	<b>0.36</b>	0.53	0.48
<i>Singapore</i>	1979-2002	0.06	<b>-0.04</b>	0.39	0.36
	1991-2002	0.60	<b>0.58</b>	0.64	0.61
<i>U.S.</i>	1979-2002	0.36	<b>0.37</b>	0.51	0.47
	1991-2002	0.07	<b>0.20</b>	0.20	0.23

Source: Cheung-Chinn-Fujii (2007), Table 3.2

# China-Taiwan Trade Shrinking in Relevance

## Share in China's Imports

	Taiwan +						
	Hong Kong	Taiwan	All HK Trade	Korea	Singapore	Japan	US
<b>1991</b>	27.5%	5.7%	20.8%	1.7%	1.7%	25.8%	12.6%
<b>2002</b>	3.7%	13.1%	18.2%	9.8%	2.4%	18.3%	9.3%
<b>2007</b>	1.3%	8.8%	11.6%	10.9%	1.8%	14.0%	7.3%

## Share in China's Exports

	Taiwan +						
	Hong Kong	Taiwan	All HK Trade	Korea	Singapore	Japan	US
<b>1991</b>	44.7%	0.8%	6.3%	3.0%	2.8%	14.3%	8.6%
<b>2002</b>	18.0%	2.0%	3.4%	4.8%	2.1%	14.9%	21.5%
<b>2007</b>	15.1%	1.7%	2.3%	4.6%	2.4%	8.4%	19.1%

## Share in China's Total Trade

	Taiwan +						
	Hong Kong	Taiwan	All HK Trade	Korea	Singapore	Japan	US
<b>1991</b>	36.6%	3.1%	13.1%	2.4%	2.3%	14.9%	10.5%
<b>2002</b>	11.2%	7.2%	10.4%	7.2%	2.3%	16.5%	15.8%
<b>2007</b>	9.1%	4.8%	6.4%	7.4%	2.2%	10.9%	13.9%

Source: Cheung-Chinn-Fujii (2007), Tables 2.6, 4.1; IMF *Direction of Trade Statistics*; CEIC

# FDI to China Likely Correlated with Trade

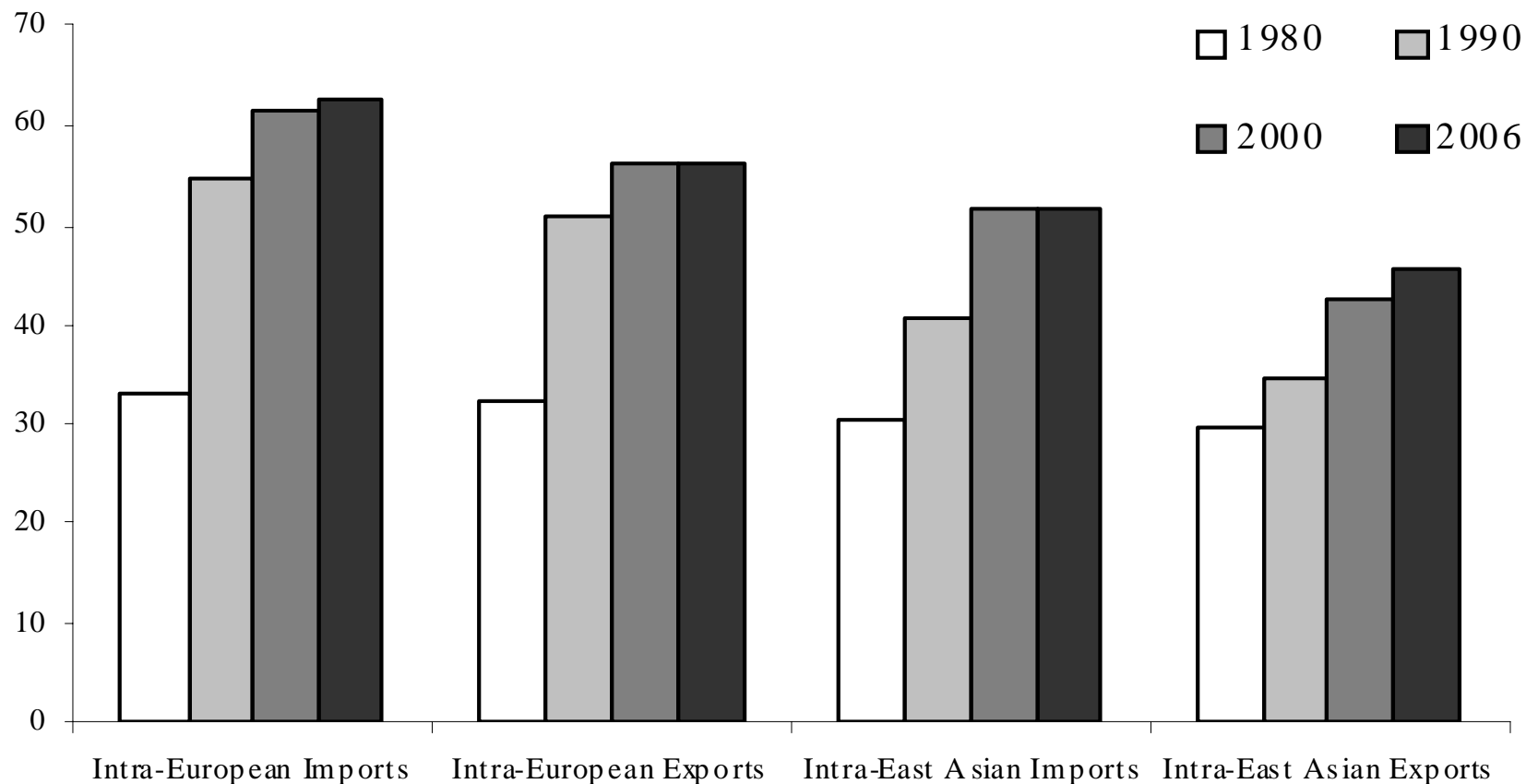
## China's FDI by Source

	Hong Kong	Taiwan
	Flows (US\$m)	
1991	2,405	466
2002	17,861	3,971
	Share of Total Chinese FDI	
1991	55%	11%
2002	34%	8%

Source: Cheung-Chinn-Fujii (2007), Table 4.2

# Intra-Asian Trade Compared to Europe

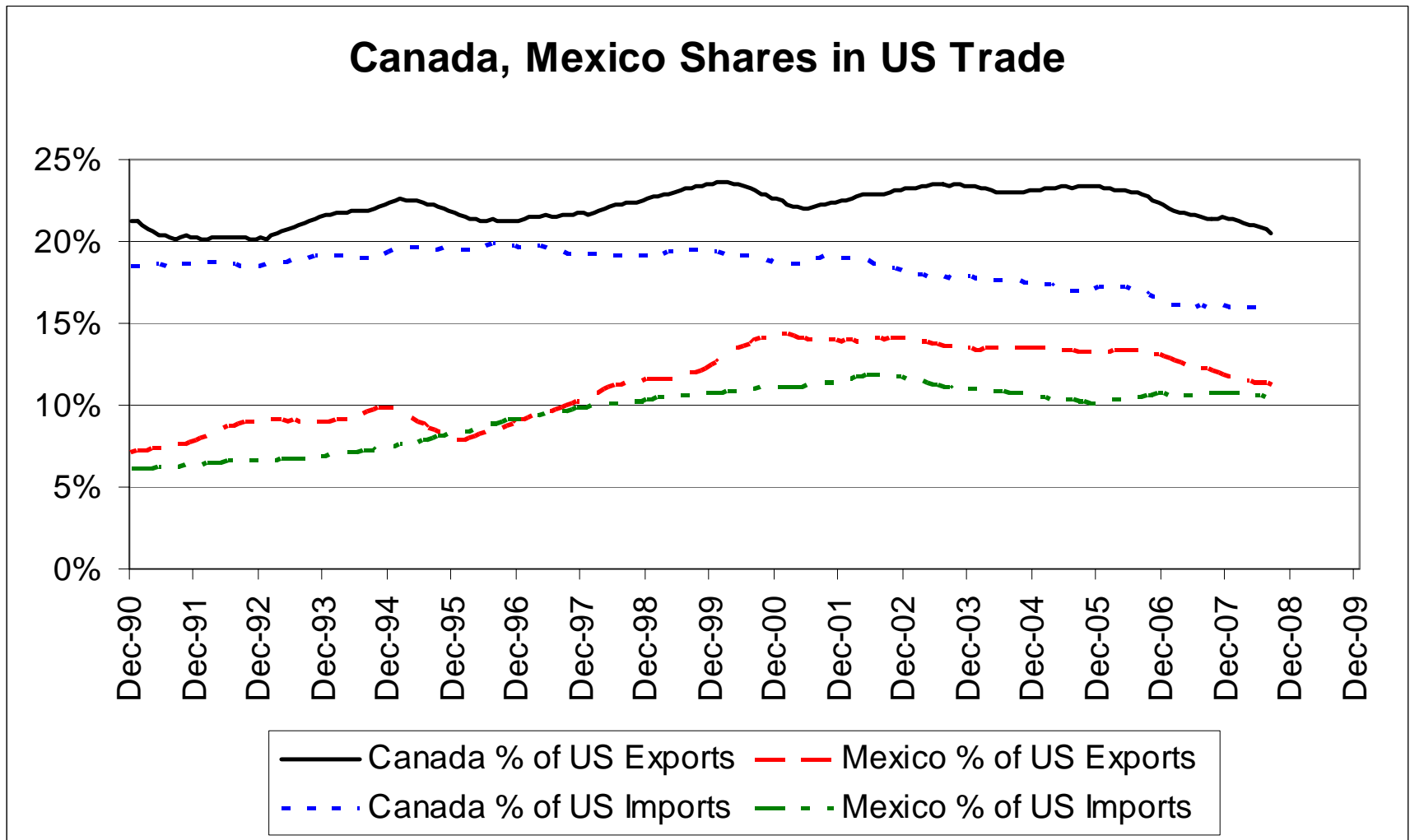
## Intraregional Trade, Europe vs. East Asia, 1980-2006



Note: East Asia = China, Hong Kong, Indonesia, Japan, Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand. Europe = the EMU.

Source: IMF *DOTS 2008* and *Statistical Yearbook of China 2007*

# The Limits of Trade Penetration Across Borders



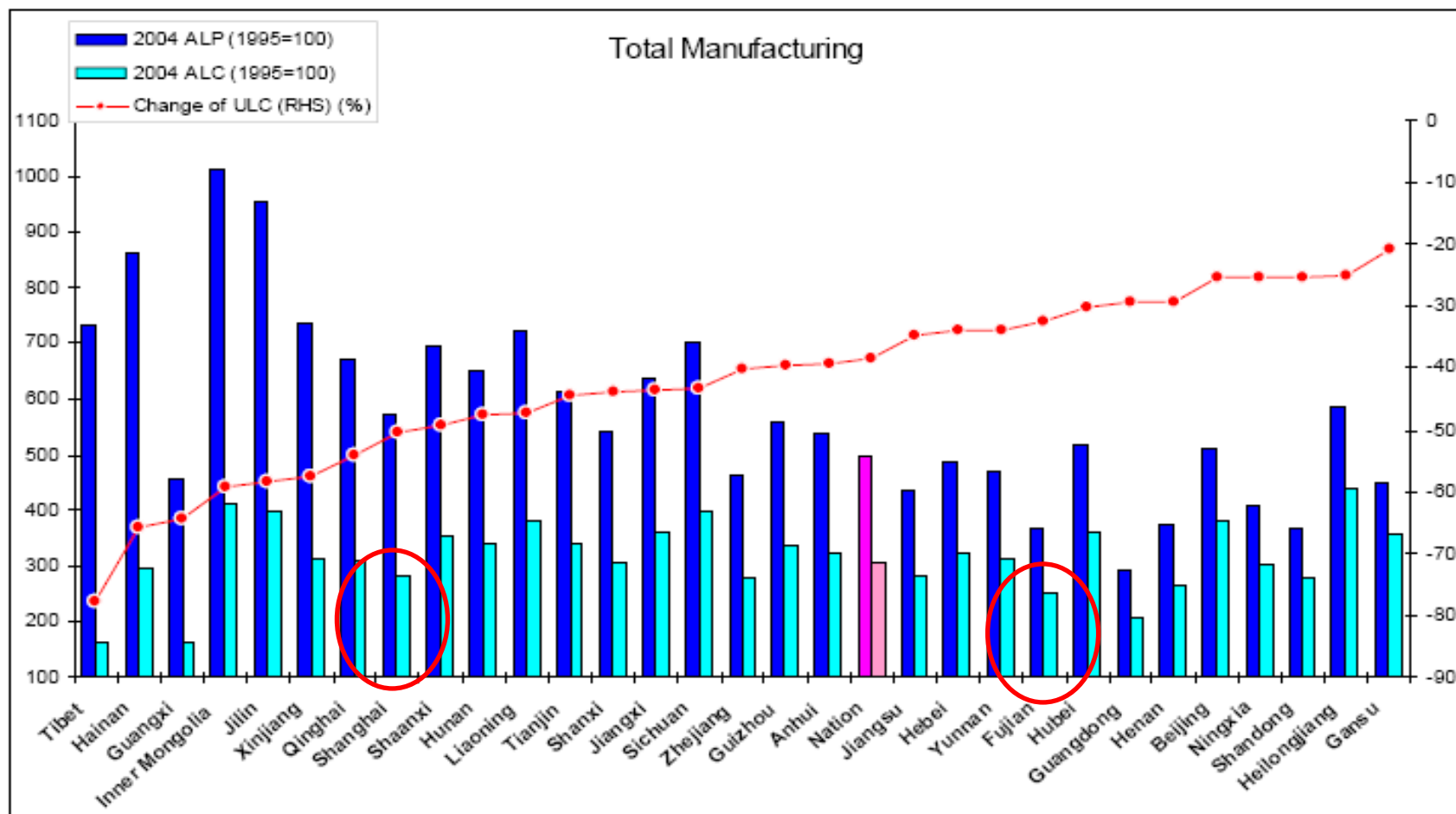
Source: CEIC

# Why Trade Integration May Hit Limits

- Convergence of factor prices
  - Important but incomplete evidence
- How much further global supply chain may stretch
  - Generally appears to be more opportunities to extend global supply chain
  - But global, secular forces (technology, competition) pushing supply chain not a Taiwan-specific argument for more integration (other Asian economies also affected)
- Not if improvement in varieties can reach much further around Asia (Krugman)

# China: Remarkable Productivity Gains to 2004

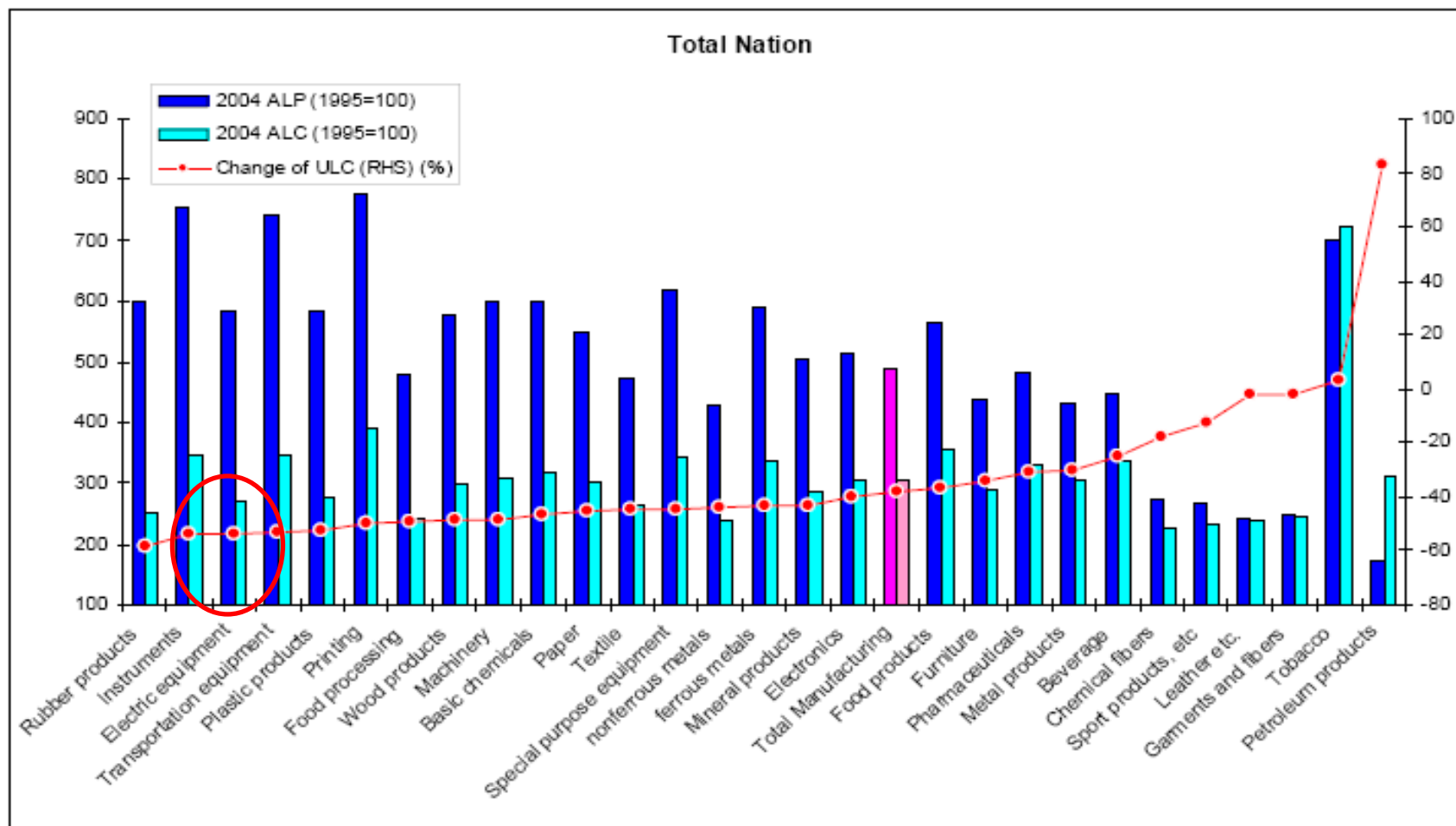
Change in Average Labor Compensation (ALC), Labor Productivity (ALP) and Unit Labor Cost (ULC) by Province for Manufacturing



Source: Chen, et al. (2008)

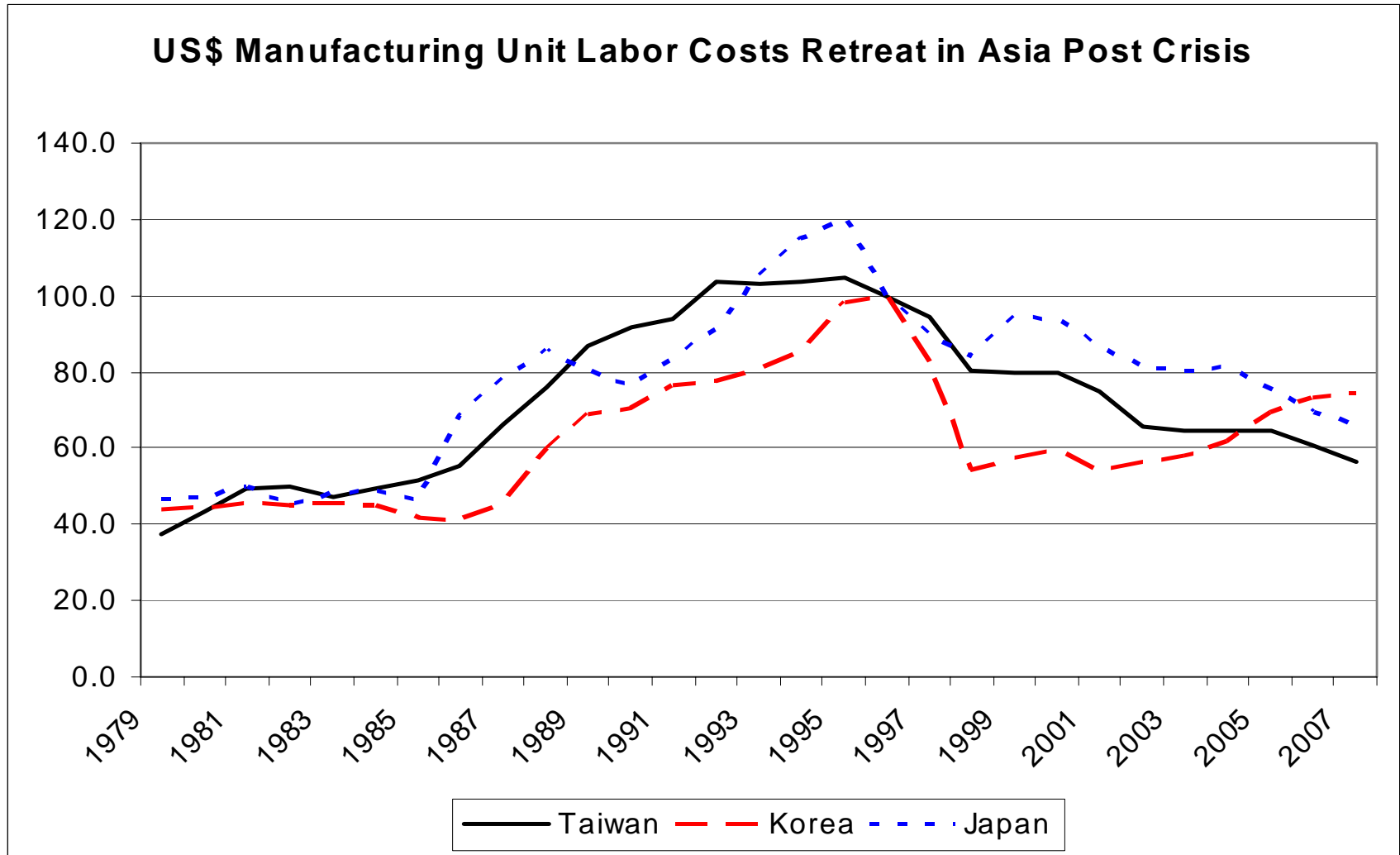
# China: Competition Restrains ULCs to 2004

Change in Average Labor Compensation (ALC), Labor Productivity (ALP) and Unit Labor Cost (ULC) by Industry



Source: Chen, et al. (2008)

# Other Northeast Asia Also Gain Competitiveness

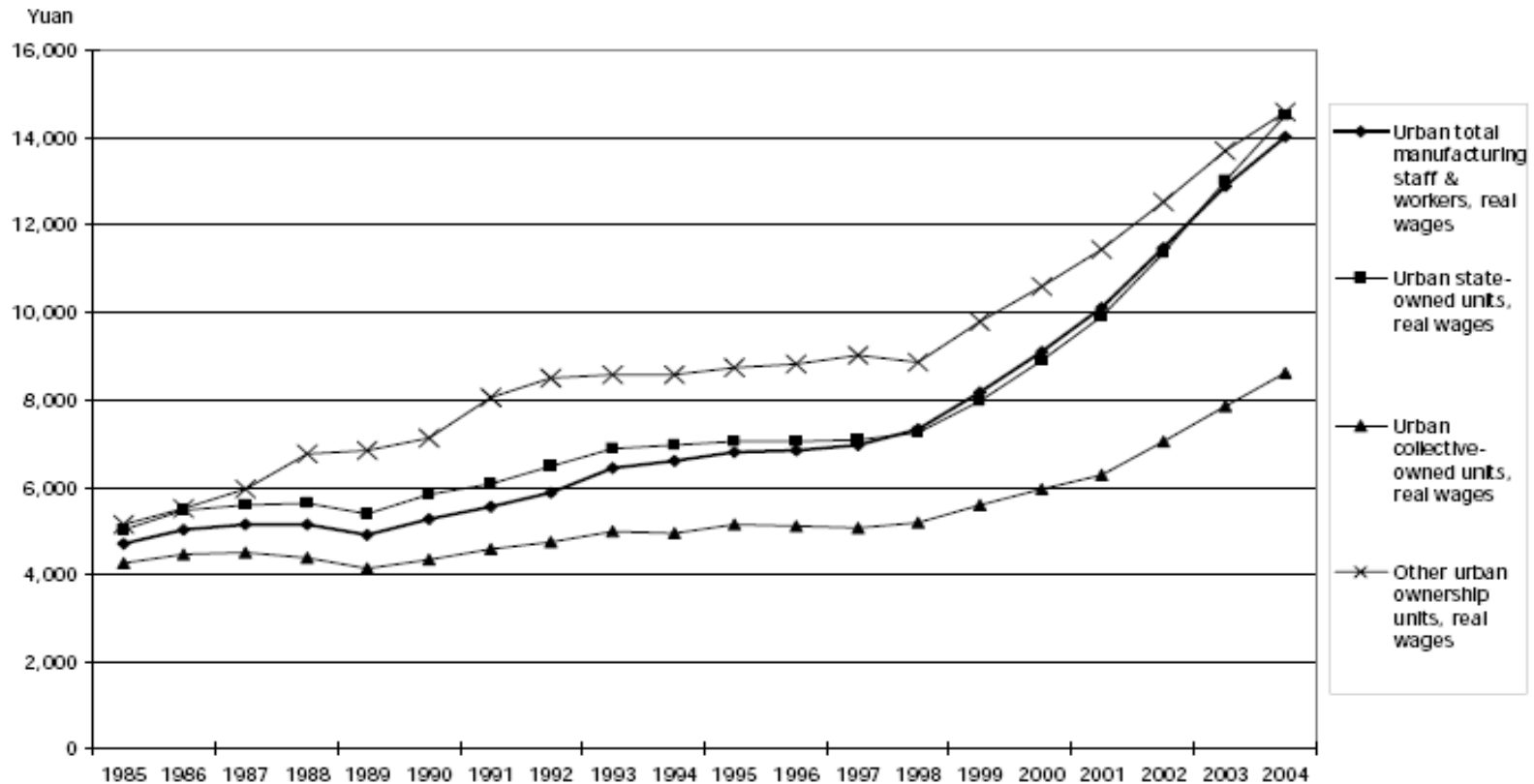


Source: U.S. Bureau of Labor Statistics

# China: Growth in Real Wages

Figure 1. Average annual real wage of urban manufacturing staff and workers in China, 1985-2004

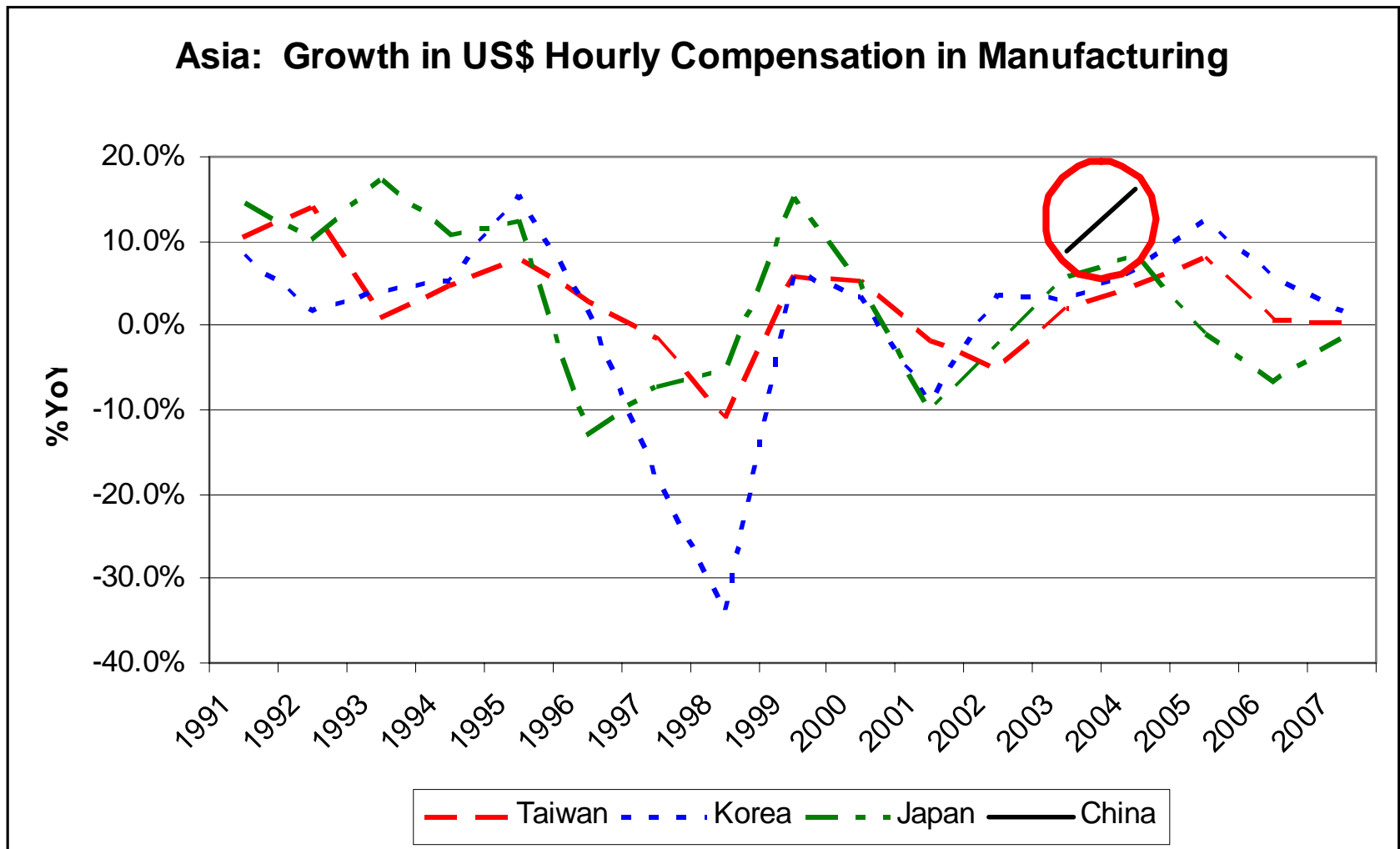
(In constant 2004 yuan)



Note: Benefits excluded.

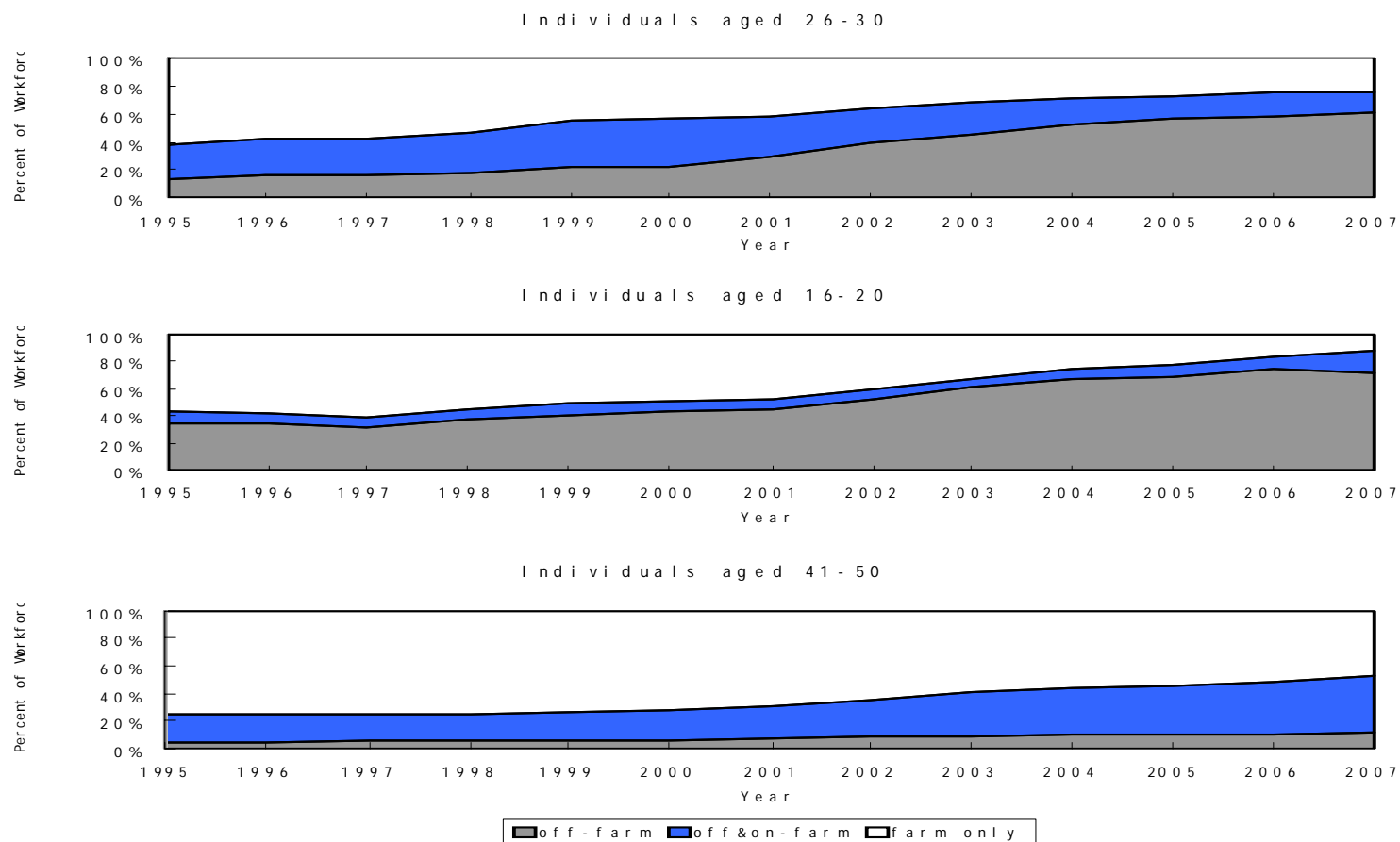
Source: Banister (2007)

# China's Wide Wage Gap Should Be Narrowing



Source: U.S. Bureau of Labor Statistics; Banister (2007)

# China: The Kids Are All Rice (Not)



Source: Authors' survey.

Note: See Figure 1 for description of figures.

**Figure 3.** Percentage of Rural Labor Force Engaged in Off-farm and On-Farm Employment, by range of ages.

Source: Rozelle, et al. (2008)

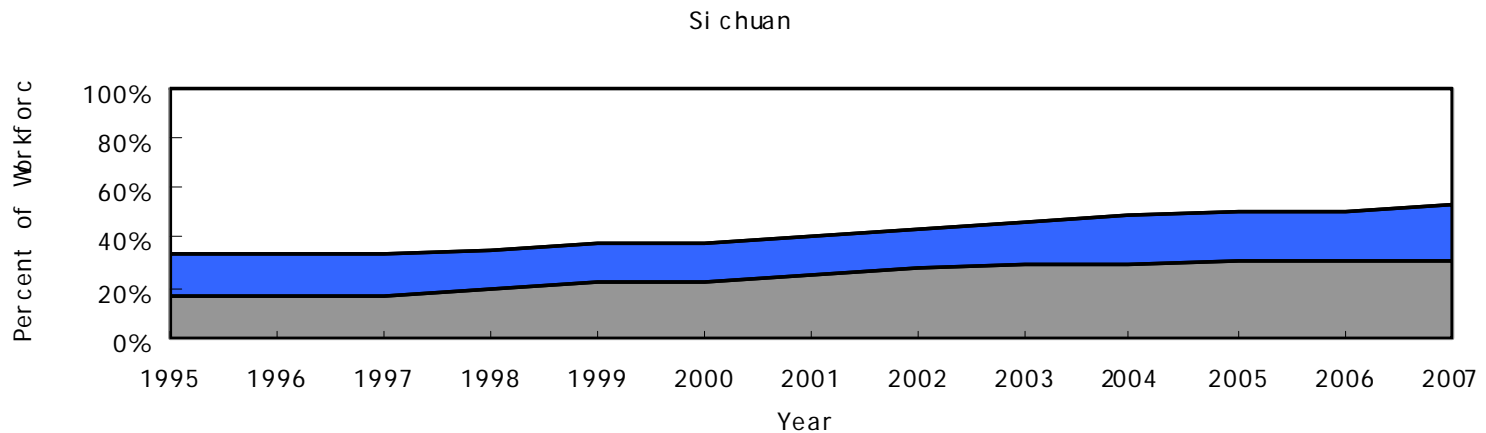
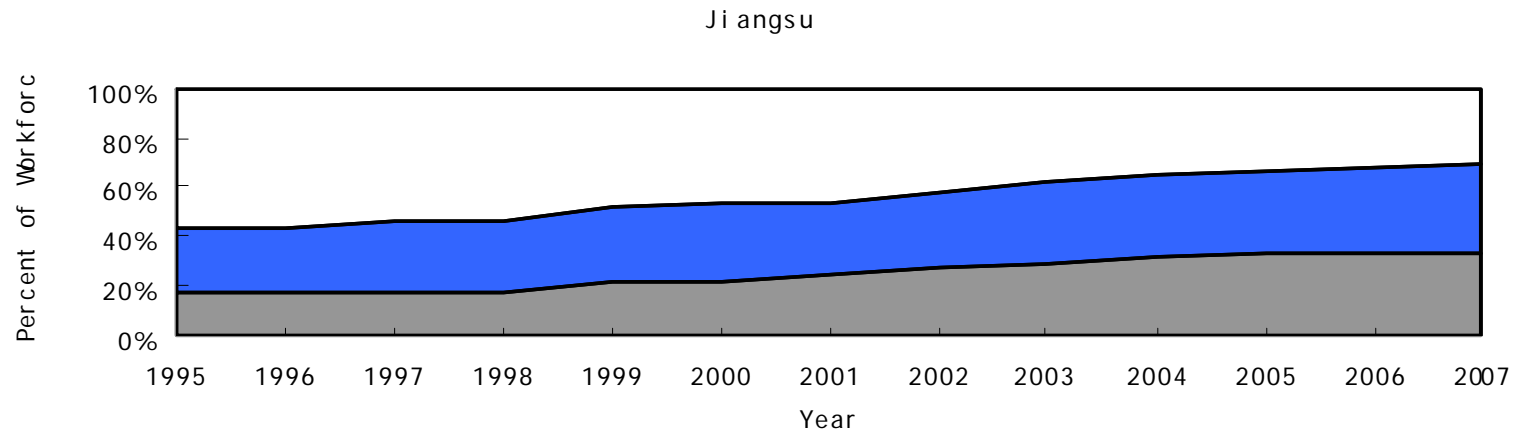
# China: Floating Population by Age

Table 4. Comparison of Labor Participation Rates in Percentage of Individuals that Participate in the Off-farm Labor Force by Age Categories and Gender, 2004 and 2007.

age cohorts	percentage with off-farm work in			
	2004		2007	
	male	female	male	female
16-20	84.8	66.7	98.0	89.4
21-25	90.2	73.8	94.5	81.3
26-30	82.9	54.2	87.9	59.6
31-35	85.6	43.5	81.2	53.5
36-40	73.9	32.1	92.2	45.0
41-50	61.9	28.1	75.5	36.6

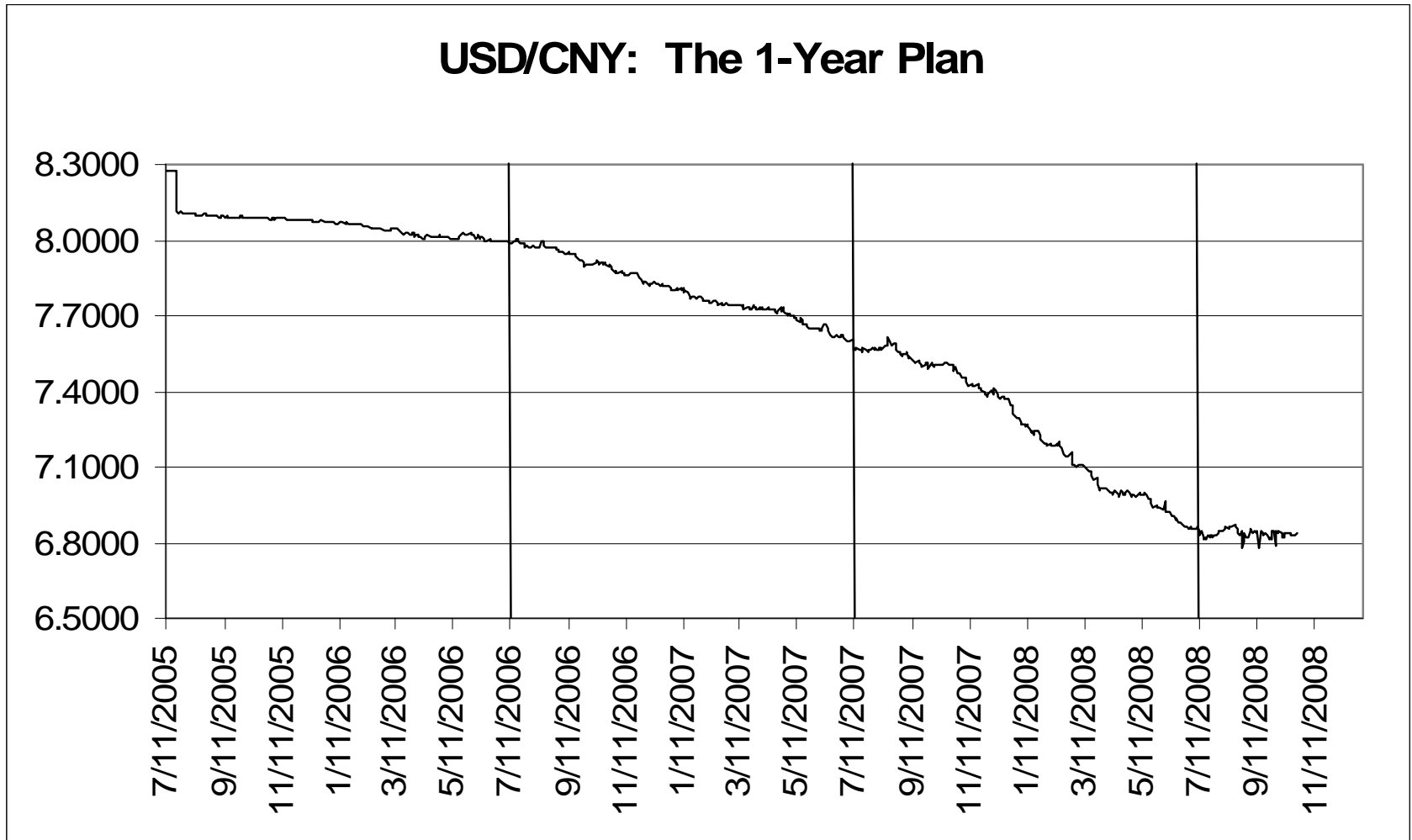
Source: Rozelle, et al. (2008)

# China: No City for Old Men (nor Women)



Source: Rozelle, et al. (2008)

# China: Appreciation Will Push Up US\$ ULCs



Source: Federal Reserve Board

# Sweden and Norway – From Ja to Nei

- “The very nature of economics is rooted in nationalism.” – Joan Robinson
- Key idea is that state-building/nationalism and economic development/modernization are two separate processes
- Generally state-building and modernization are mutually reinforcing, but this was an exception
- Norway a nation of small freeholders, “flexible specialization,” more democratic
- Sweden more aristocratic, large business legitimacy, much more extensive development of financial capital, faster growth

# A Few Concluding Thoughts (1)

- Given measures showing declining importance, unlikely that economic factors by themselves can be counted upon to act in the future as a sufficient bulwark against military conflict
- The best part of the upside from economic integration may be behind us
- Does not mean reversion to confrontation is inevitable
- Does suggest future political integration will require more exclusively political work

## A Few Concluding Thoughts (2)

- Recognize current interest of China, US to fudge the Taiwan issue
  - Not sure if this is a stable equilibrium
- Democracy as a separate process (Sweden/Norway), one that may well affect the equilibrium
- A need for creative diplomacy – the peaceful future of cross-straits relations requires new diplomatic doctrines and compacts
- Points to a focus on the quality of political leadership development on both sides of the Straits

**Thank You**