WTO Accession, 'Greater China' Free Trade Area and Economic Relations across the Taiwan Straits

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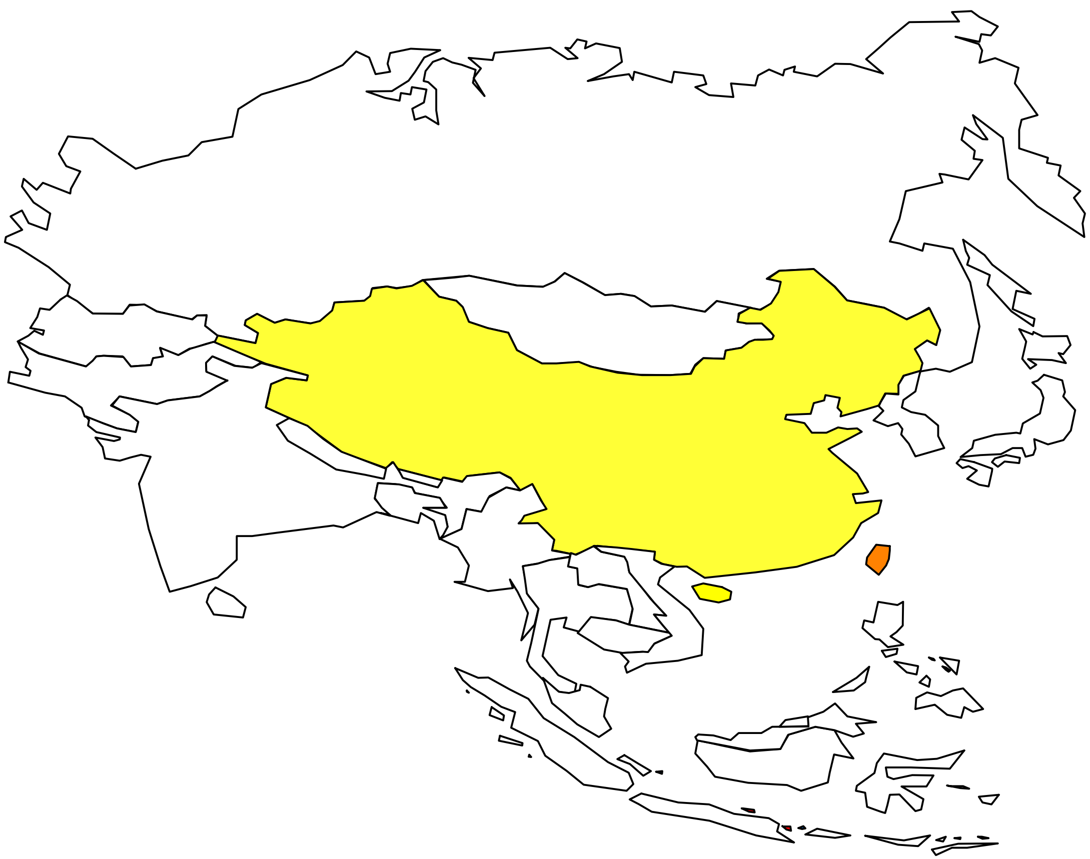
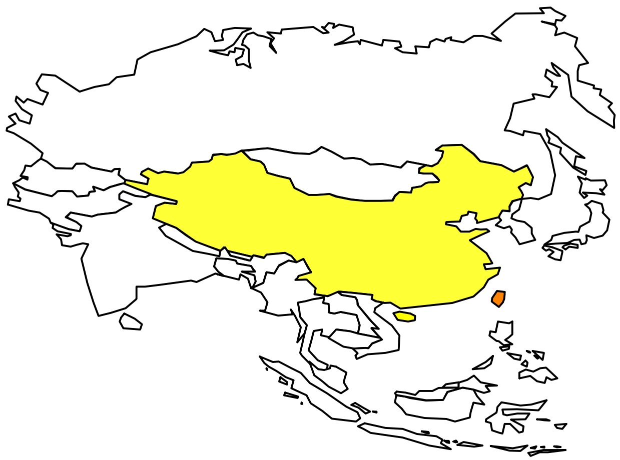


Briefing Outline



- Growing Economic Interdependence between Taiwan and China
- The numerical model and simulation design
- Simulation Results
- ***Impact on Patterns of World Trade***
- ***Impact on Trade Flows between China, Taiwan and Their Major Trade partners***
- ***Impact on economic growth and social welfare***
- Conclusions and Implications for Cross Strait Economic Relations

Growing Economic Interdependence between China and Taiwan

- Indirect trade between China and Taiwan increased from less than $1 billion in 1987 to more than $31 Billion in 2001
- The dependence of Taiwan's exports on China and Hong Kong's market from less than 8 percent in 1987 to 28 percent in 2000
- The actually used direct investment from Taiwan has reached $27.5 billion by the end of June 2001 and account for nearly 40 percent of Taiwan's total overseas investment
- Besides political deadlock, trade between China and Taiwan, even indirectly from Hong Kong, is still highly regulated today. As the Mach of 2002, there still 23 percent (2335 item) of the 10,238 10-digit HS commodities not permit to be imported from China to Taiwan.

Method of Analysis

17-region, 25-sector global CGE model

• Includes China and Taiwan's major trading partners and covers major production and trade activities in the world economy

• Recursive dynamic, solves from 1997 to 2011 annually

• Linked with a macro econometric model to obtain rate of economic growth, balance of trade, gross investment and government spending in each region, then generates the corresponding pattern of sectoral output and trade across the world economy

• Import embodied technology transfer, sector specific TFP

• Version 5 GTAP database is the primary data source

Simulation Design

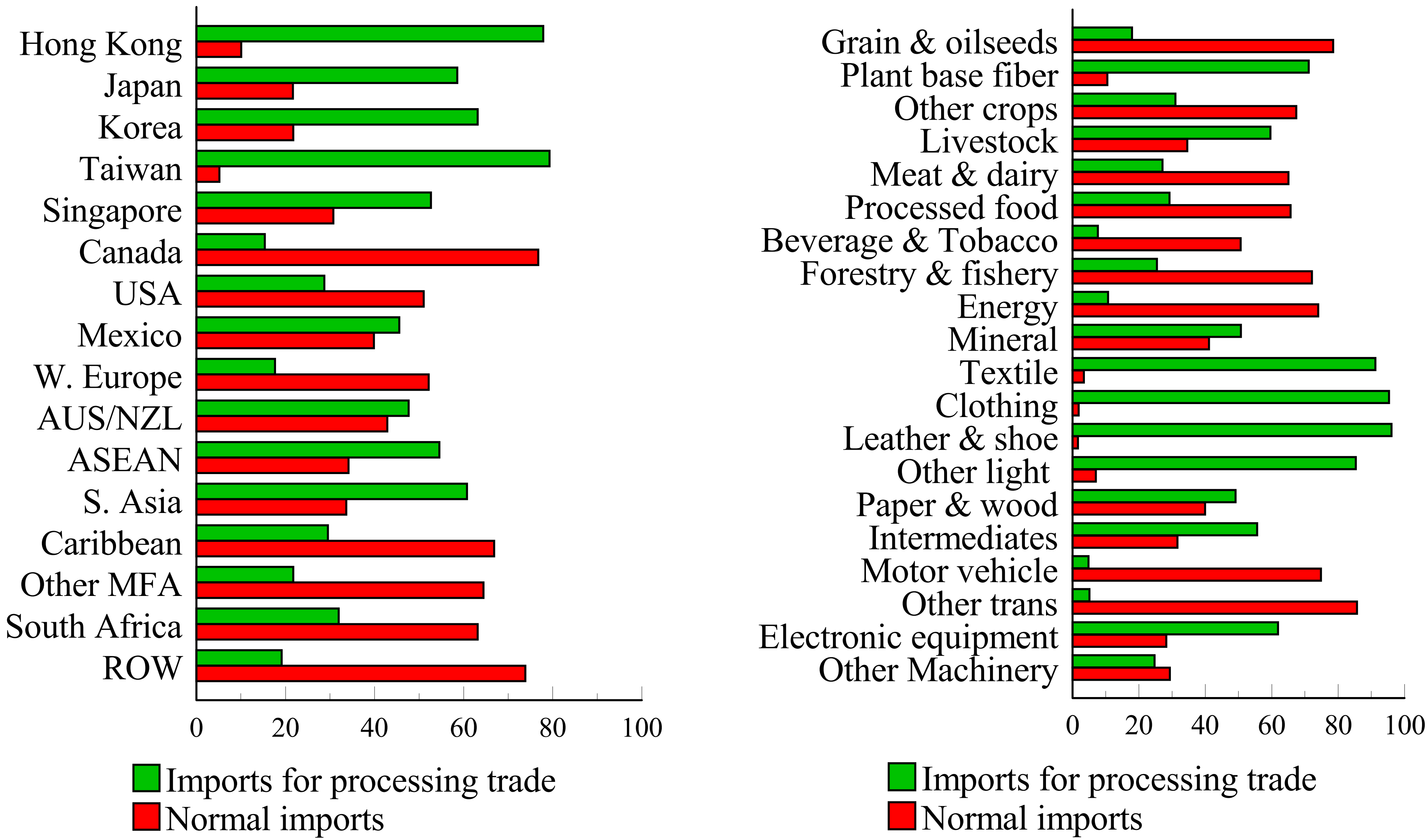
- A baseline from 1998-2011 is established first as Scenario I (the Uruguay Round Case). It generates a reference growth path of the world economy with the implementation of the Uruguay Round trade liberalization, but without China and Taiwan's participation. It is a calibrated "benchmark" and serve as a basis of comparison for counterfactual simulation
- The second scenario includes China and Taiwan in the liberalization process (the Accession Case), all other assumptions are keep the same with Scenario I
- The third scenario assume a free trade area is created among China, Taiwan and Hong Kong after China and Taiwan's WTO Entry (Greater China FTA case).
- The differences between the Accession and FTA Case with the baseline equal our estimates of the impact of China and Taiwan joining the WTO and the impact of a greater China FTA respectively

Simulation Design: China and Taiwan's WTO Offer

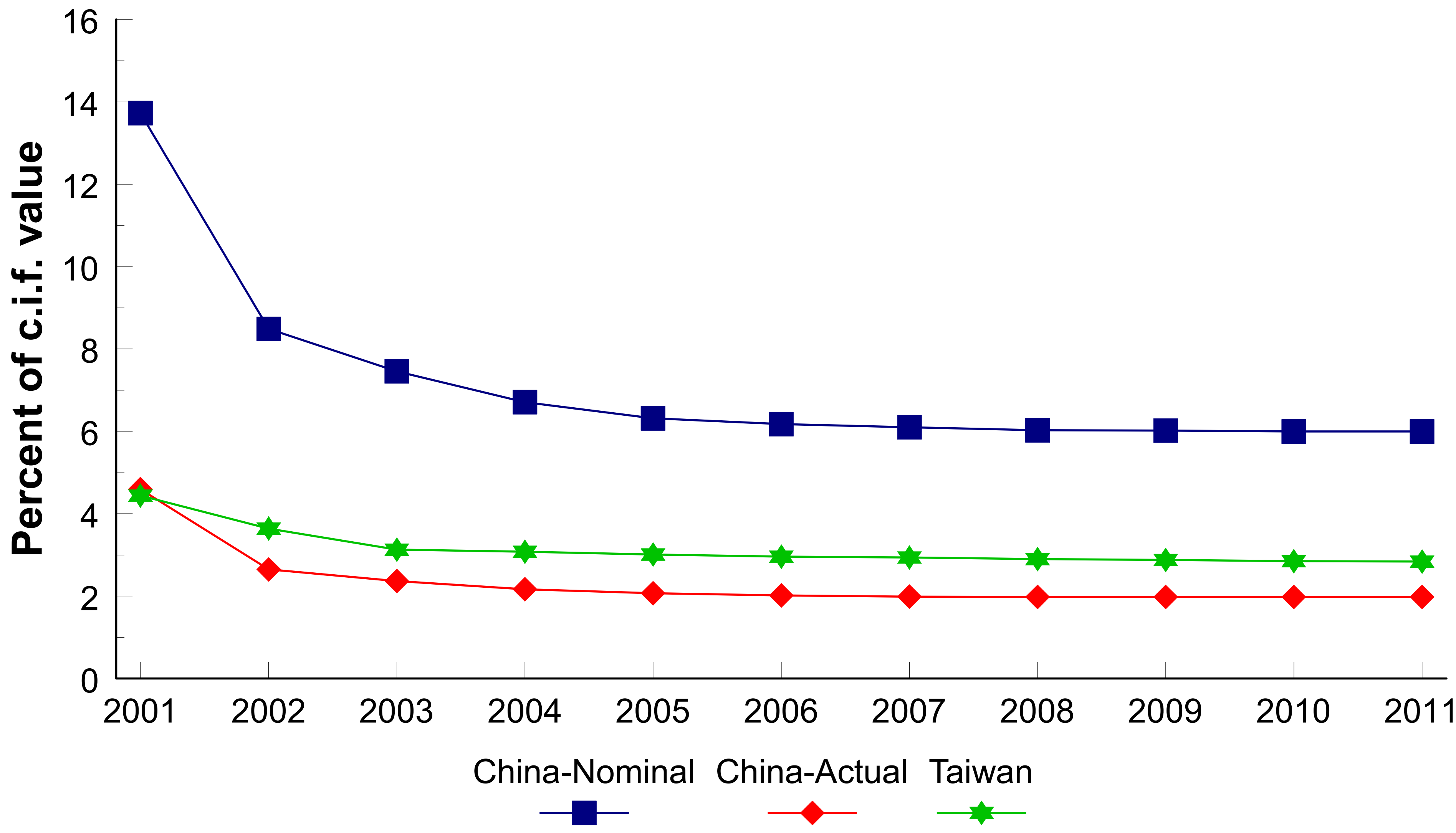
- Tariff reduction in both agricultural and manufacturing products (China and Taiwan);
- Elimination of non-tariff barriers in five years (China and Taiwan);
- Agricultural trade liberalization (China and Taiwan). 2 percent growth of the quota each year in the baseline and 5 percent growth each year from 2001-2004 in the accession case and elimination of such import quotas at 2005;
- Opening up of major service sectors (China);
- Phase out of MFA quota on textile and clothing.

The Share of China's Normal and Processing Trade by Sector, 1998

percent

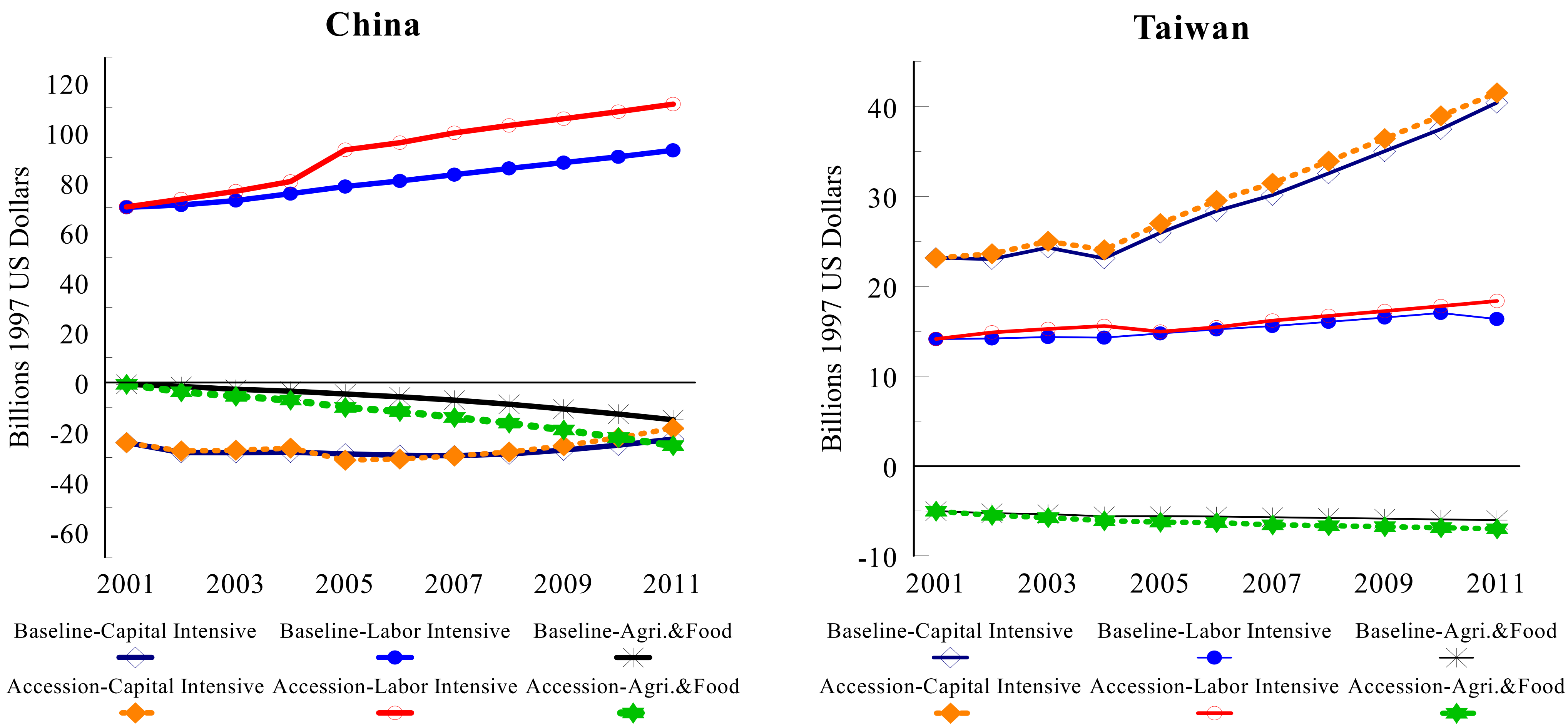


Assumed Tariff Reduction in China and Taiwan



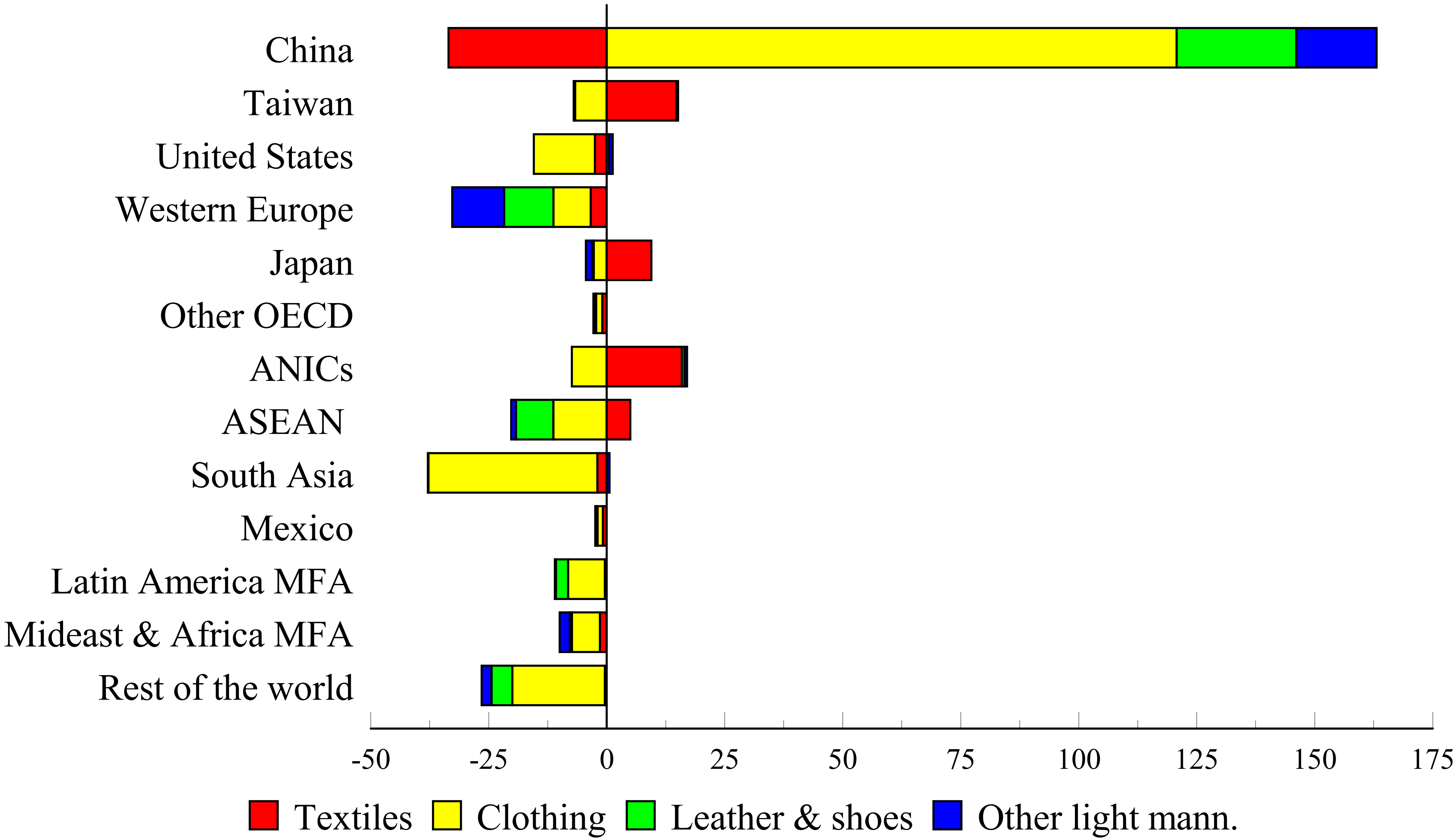
Impact of WTO Entry on China's and Taiwan's Net Trade

2001 - 2011



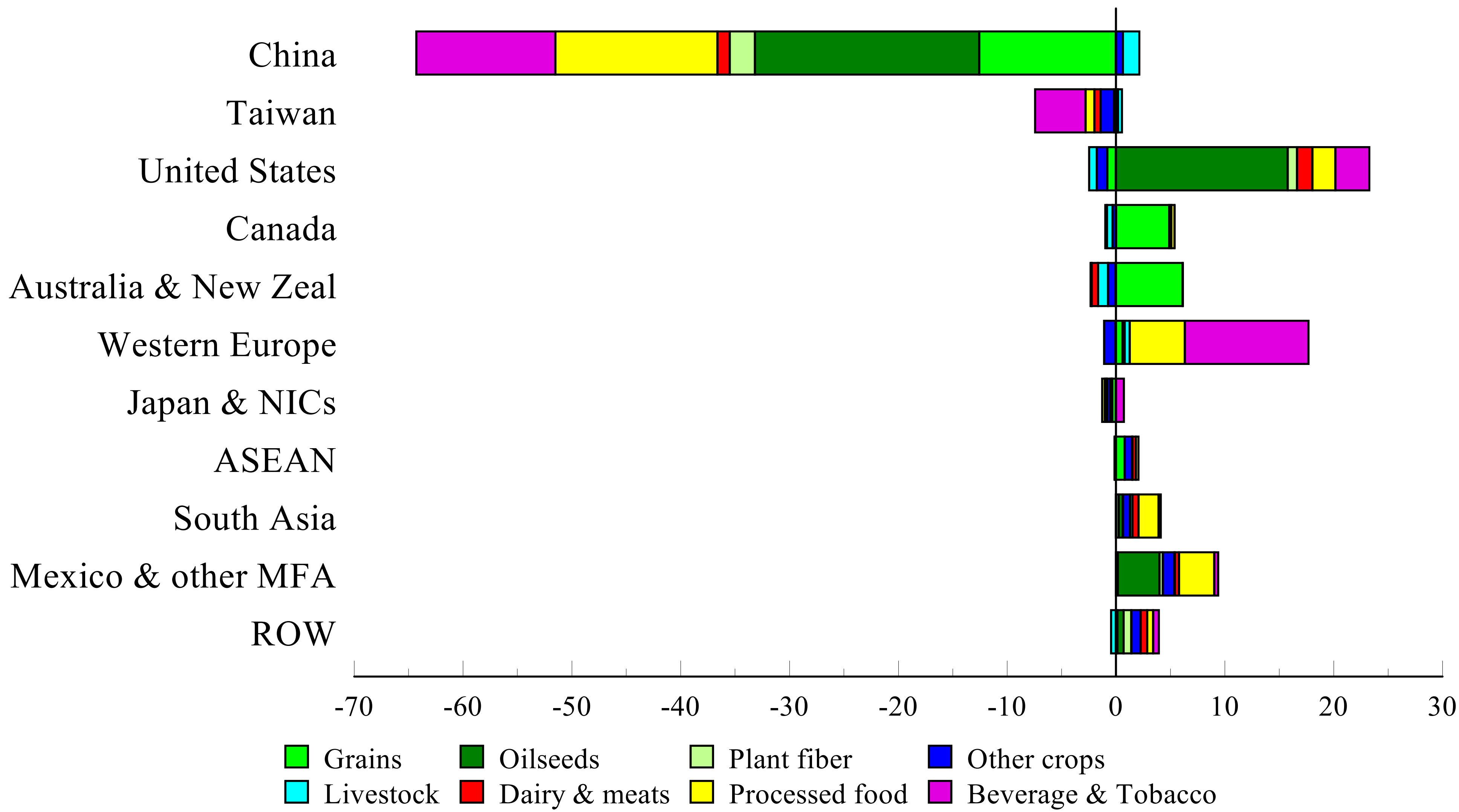
Changes in Net Labor Intensive Exports between a WTO with and without China and Taiwan

Billion of 1997 U.S. dollars, 2002-2011



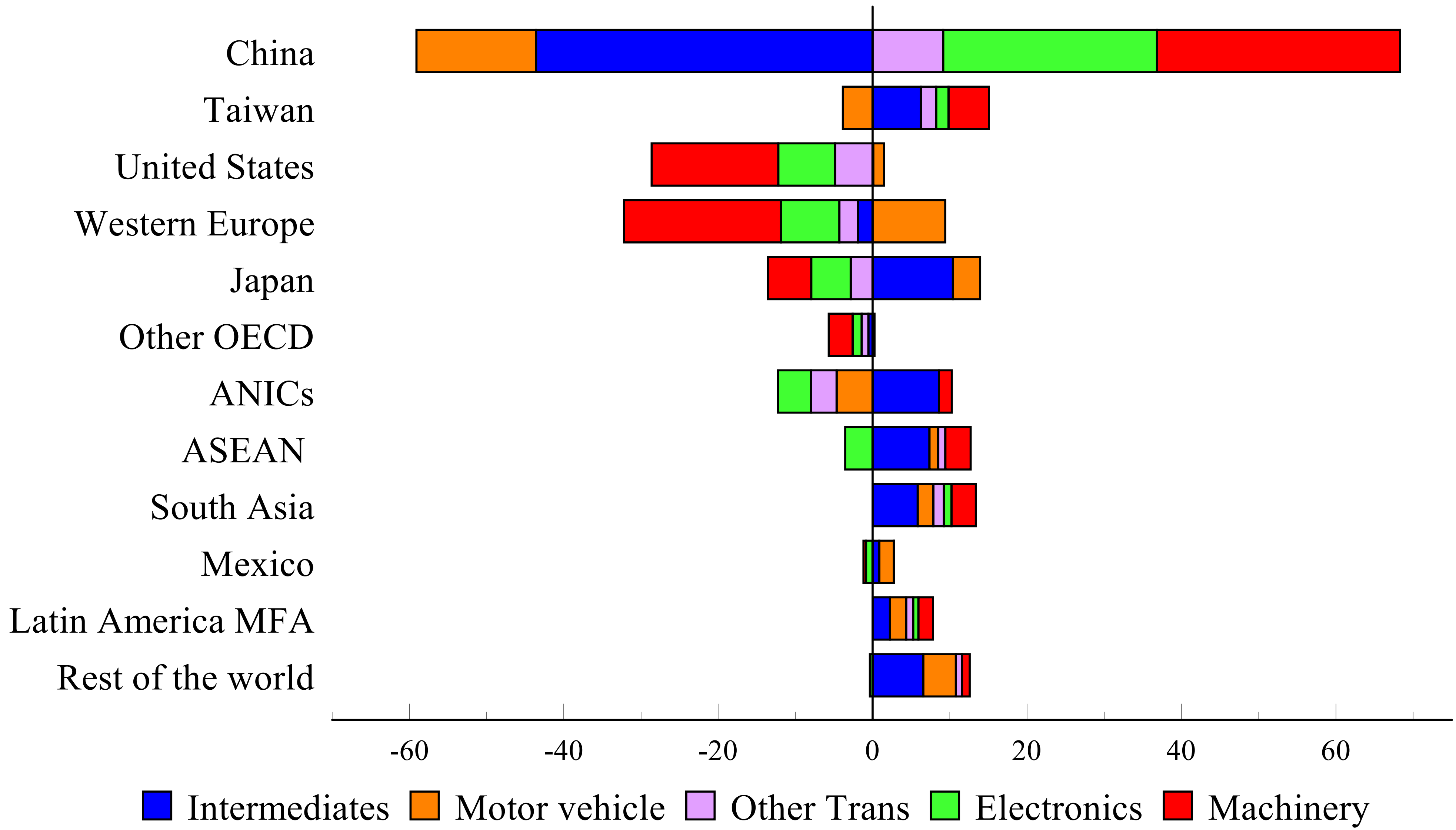
Changes in Net Agricultural Exports Between a WTO with and without China and Taiwan

Billion of 1997 U.S. dollars, 2002-2011

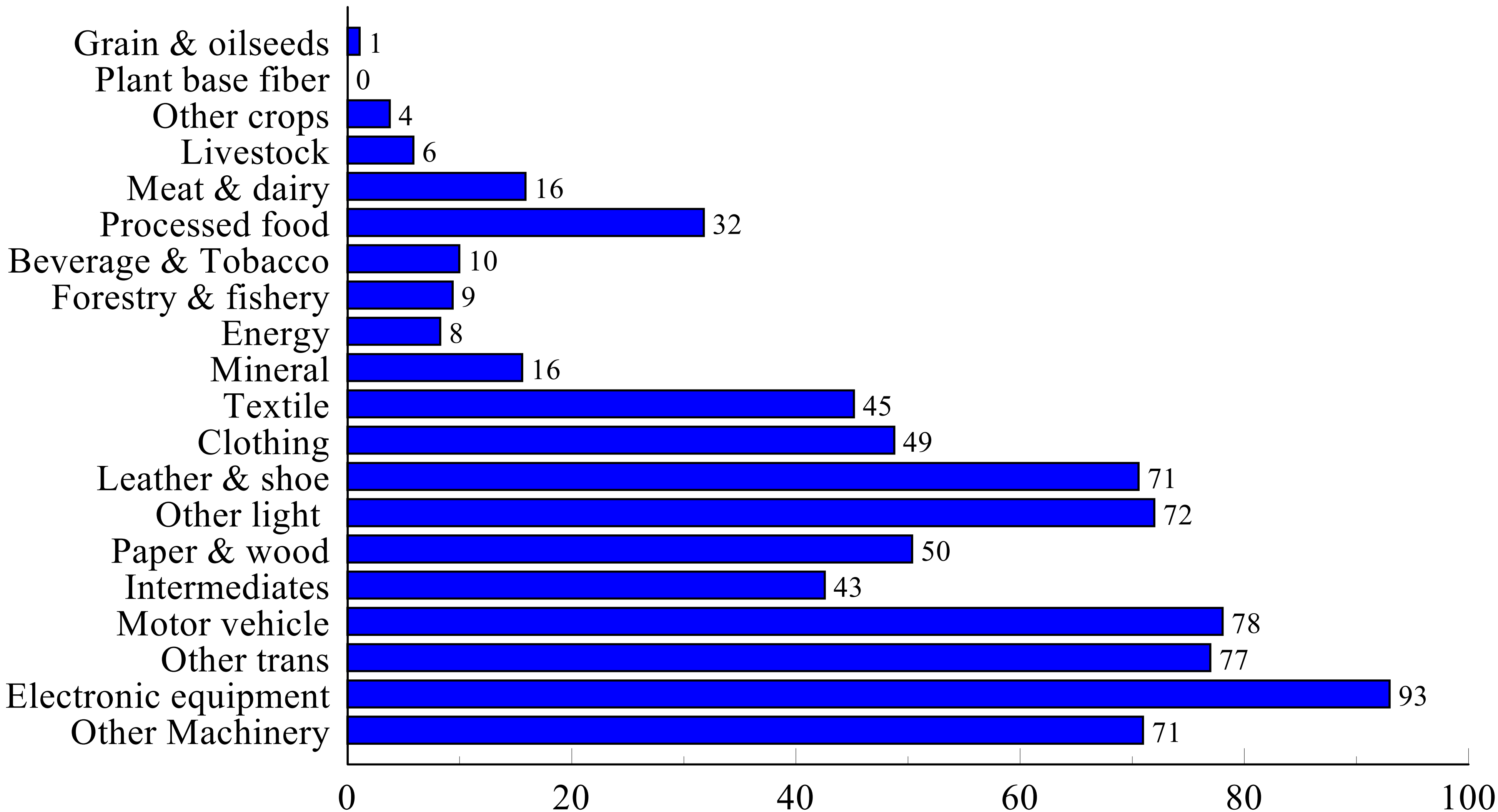


Changes in Net Capital Intensive Exports between a WTO with and without China and Taiwan

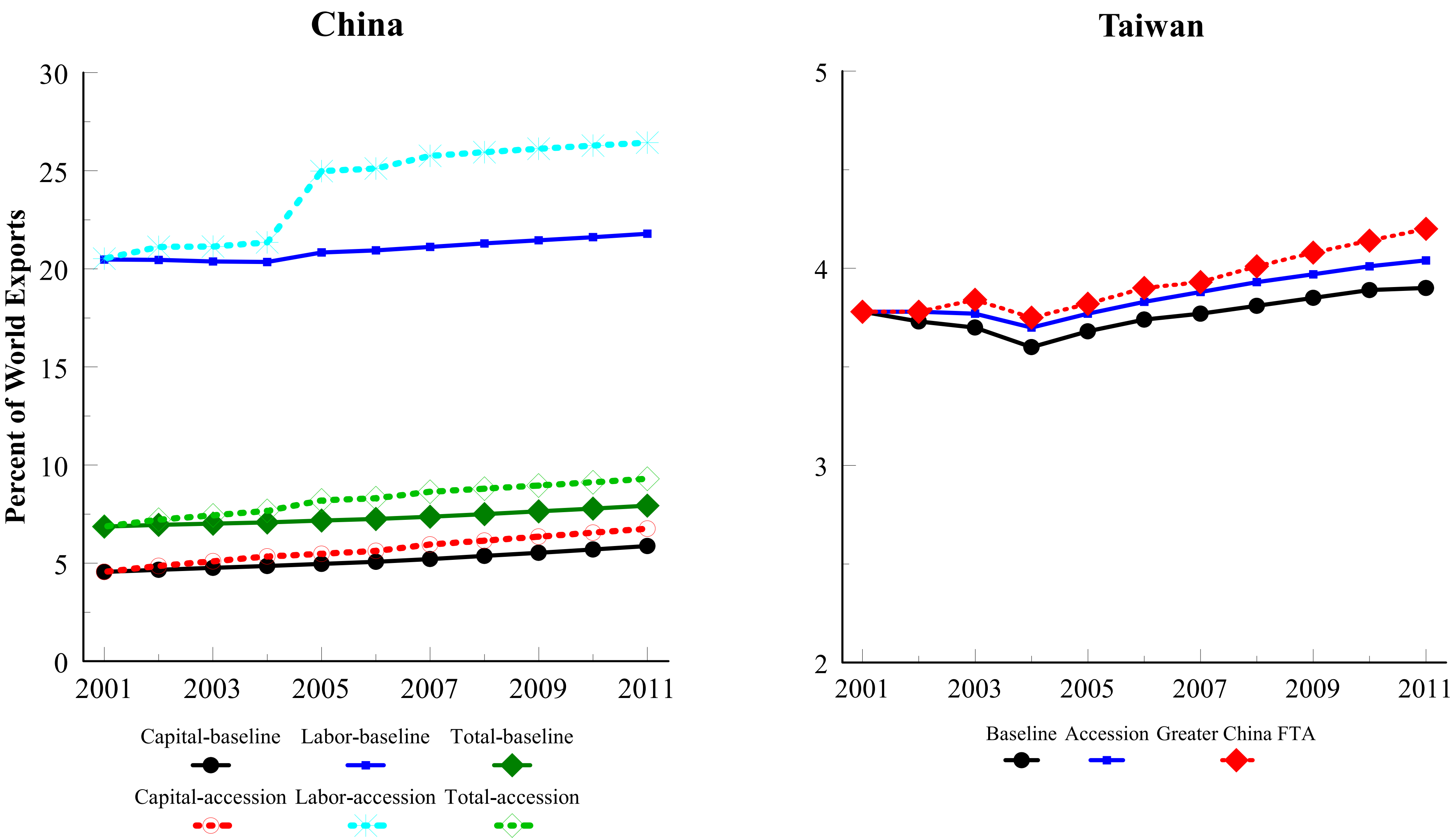
Billion of 1997 U.S. dollars, 2002-2011



China's Processing Exports as Percent of Total Exports by Sector
1998



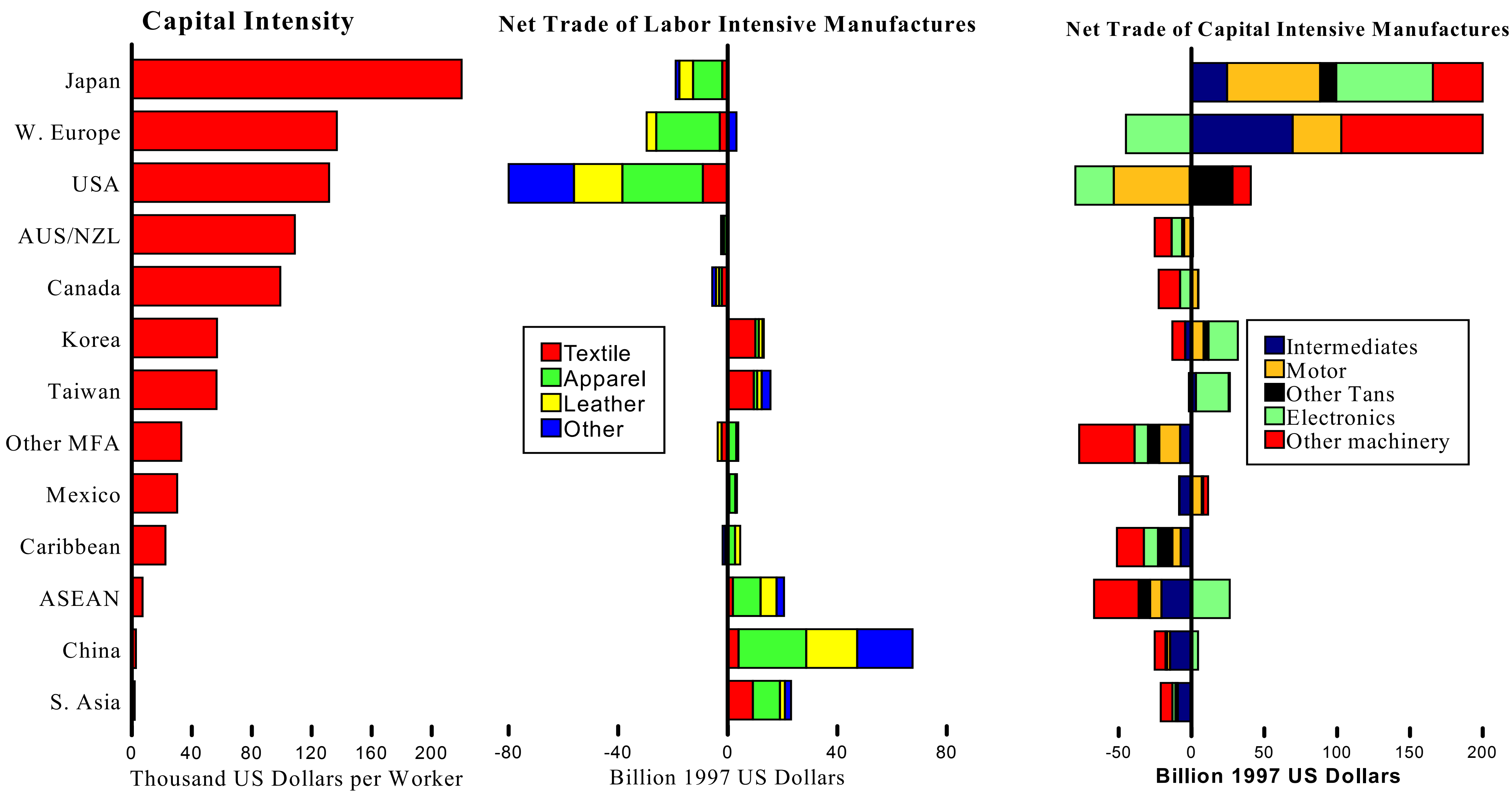
WTO Entry Increase Both China and Taiwan's Manufactured Export Share in the World Market 2001-2011



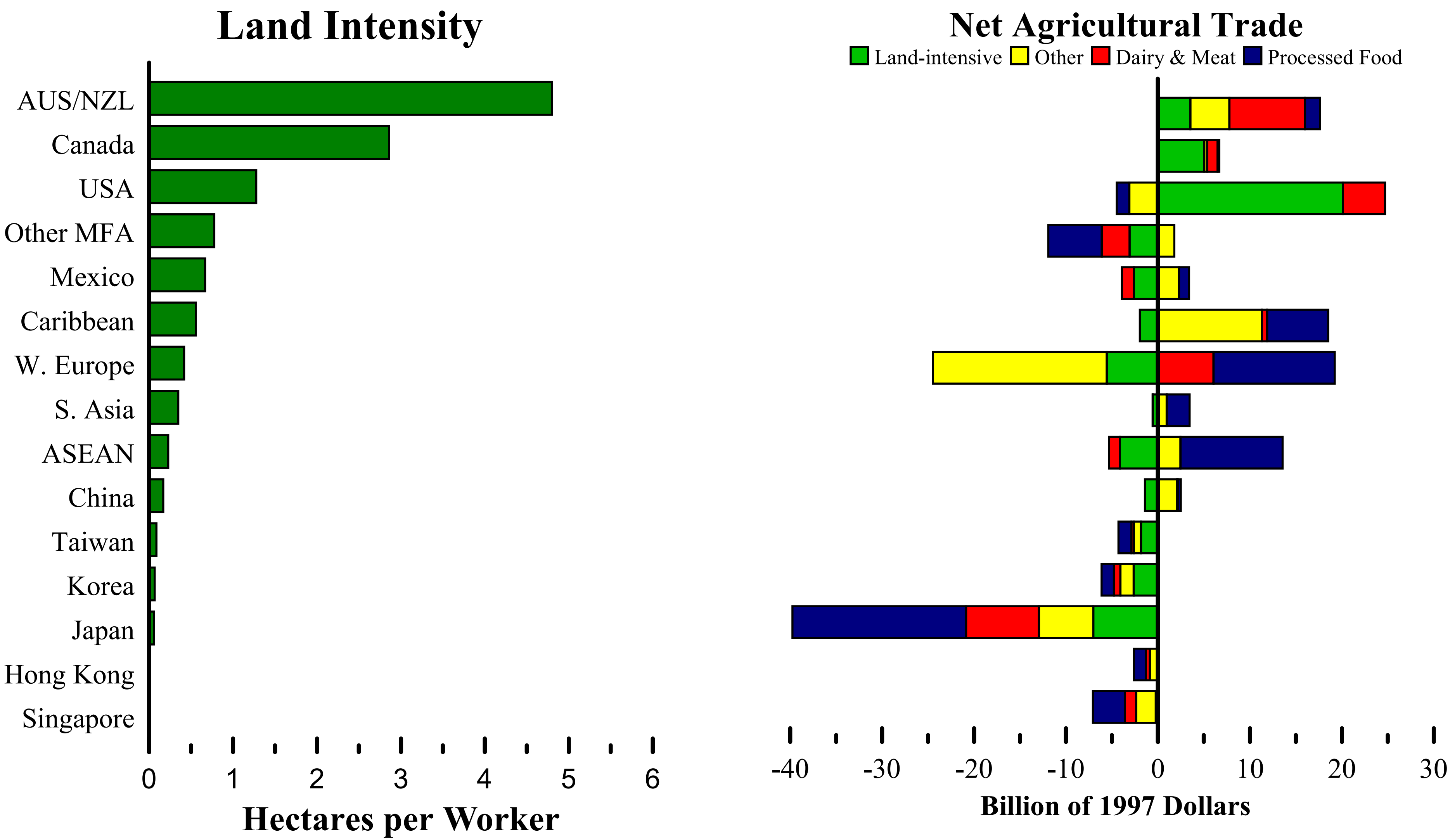
The Driving Force for China Emerging as a World Manufacturing Center

- Factor endowment
- International segmentation of commodity production processes, which is an important aspect of economic globalization.
- The competition in the global market
- Production relocation in Asia
- More than $300 billion of FDI flows to China in recent years

Countries with Abundant Labor Tend to Export Labor Intensive but Import Capital Intensive Manufactures, 1997



Countries with Abundant Land Tend to Export Agricultural Products, 1997

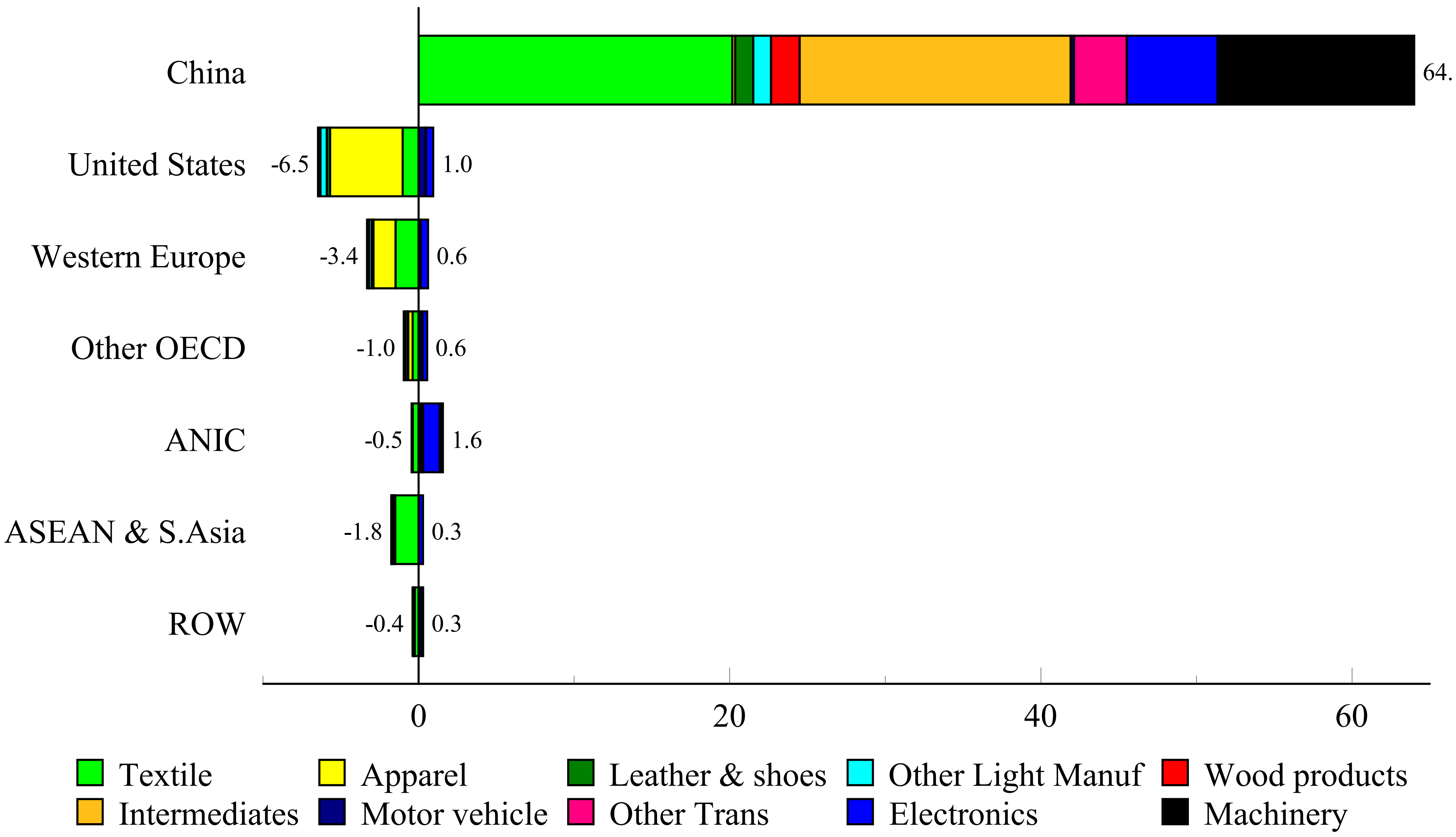


Three Aspects of China's Comparative Advantage in Engaging Labor-intensive Productions

- China has a much lower labor cost in terms of percent of wage cost in per unit output, not only relative to major developed countries, but also relative to most developing countries
- The size of the labor force in China is very large
- This huge labor force is distributed over vast geographical regions that differ greatly in stages of economic development

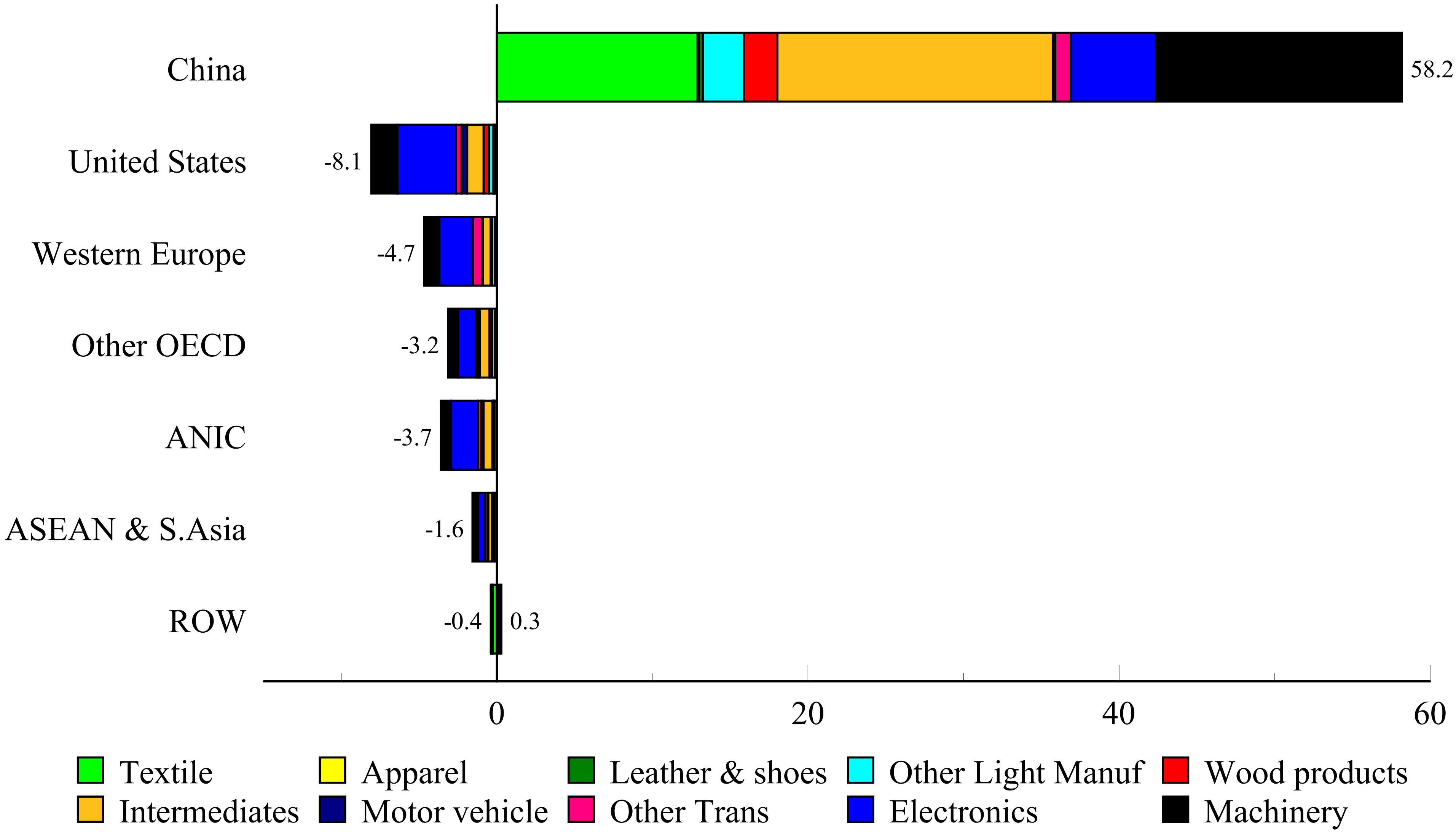
Impact of WTO Entry: Increase Taiwan's Exports of Intermediates and Capital Goods to China, Decrease of Labor Intensive Finished Products to The U.S.

2002-2011 accumulated



Trade Diversion Effect of a Greater China FTA:Taiwan Further Divert its Exports from Other Countries to China

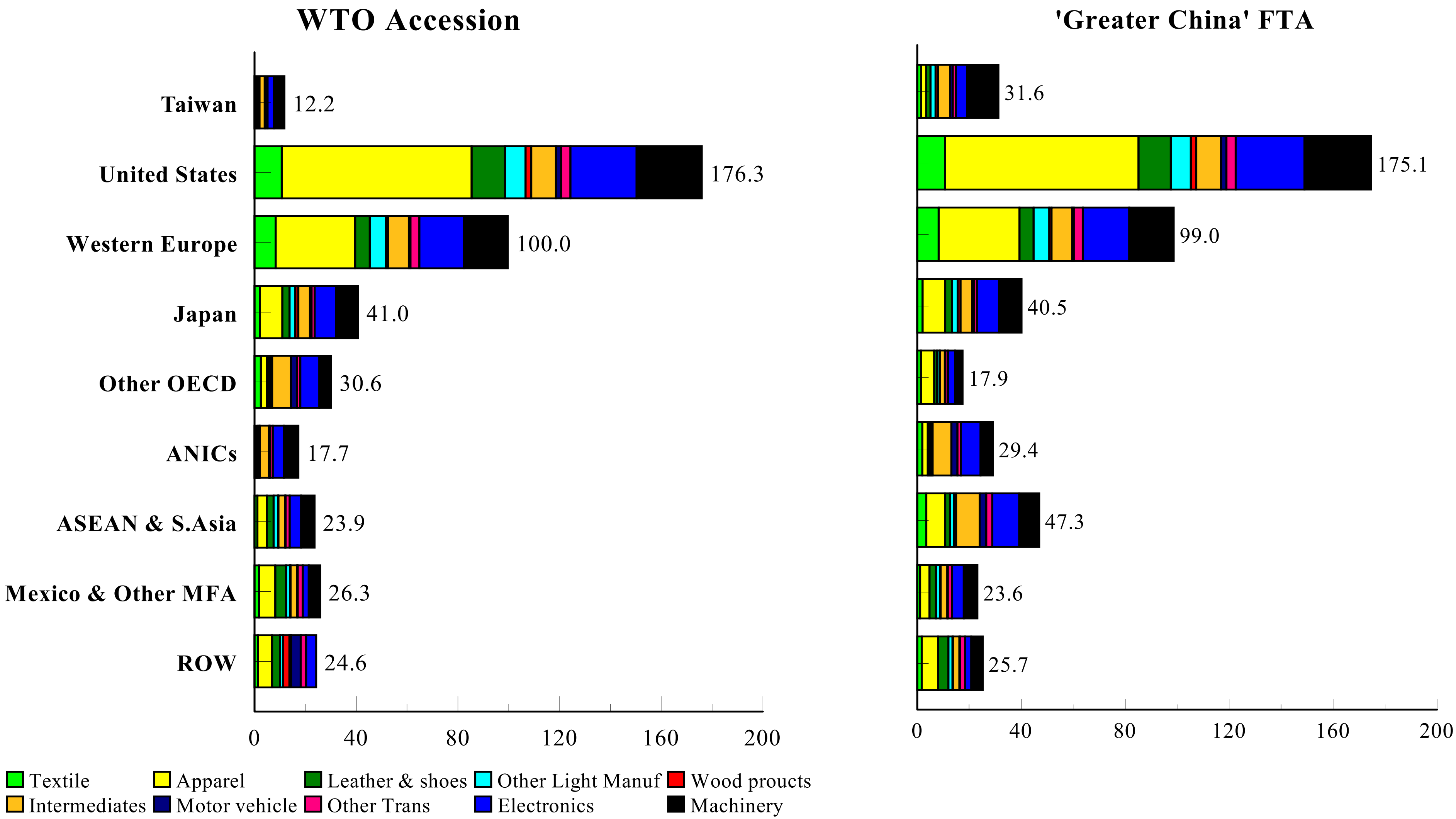
2002-2011 accumulated



Impact of Trade liberalization in China's Exports:

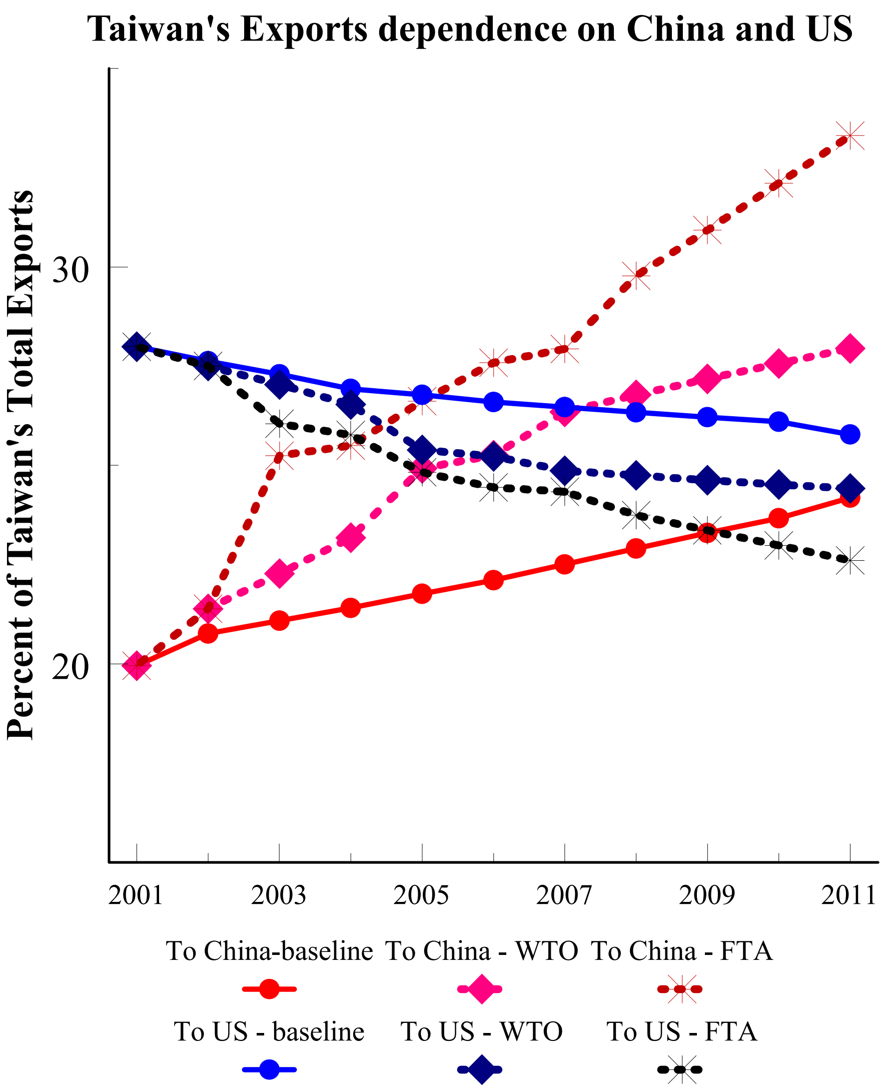
Increase China's Labor-intensive Finished products to Developed Countries, Intermediate and Capital Goods to Developing Countries

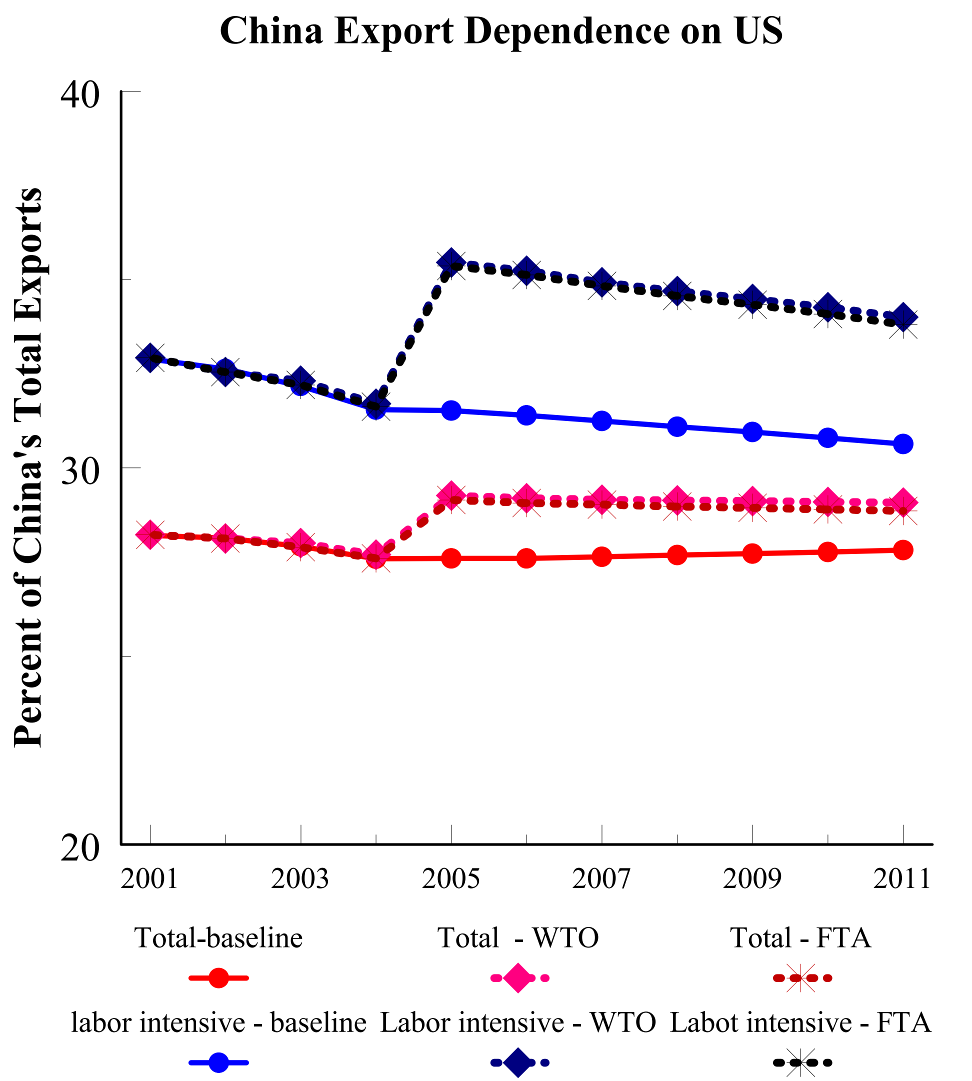
2002-2011 accumulated



The Redirection of Trade Flows between China, Taiwan and the United States

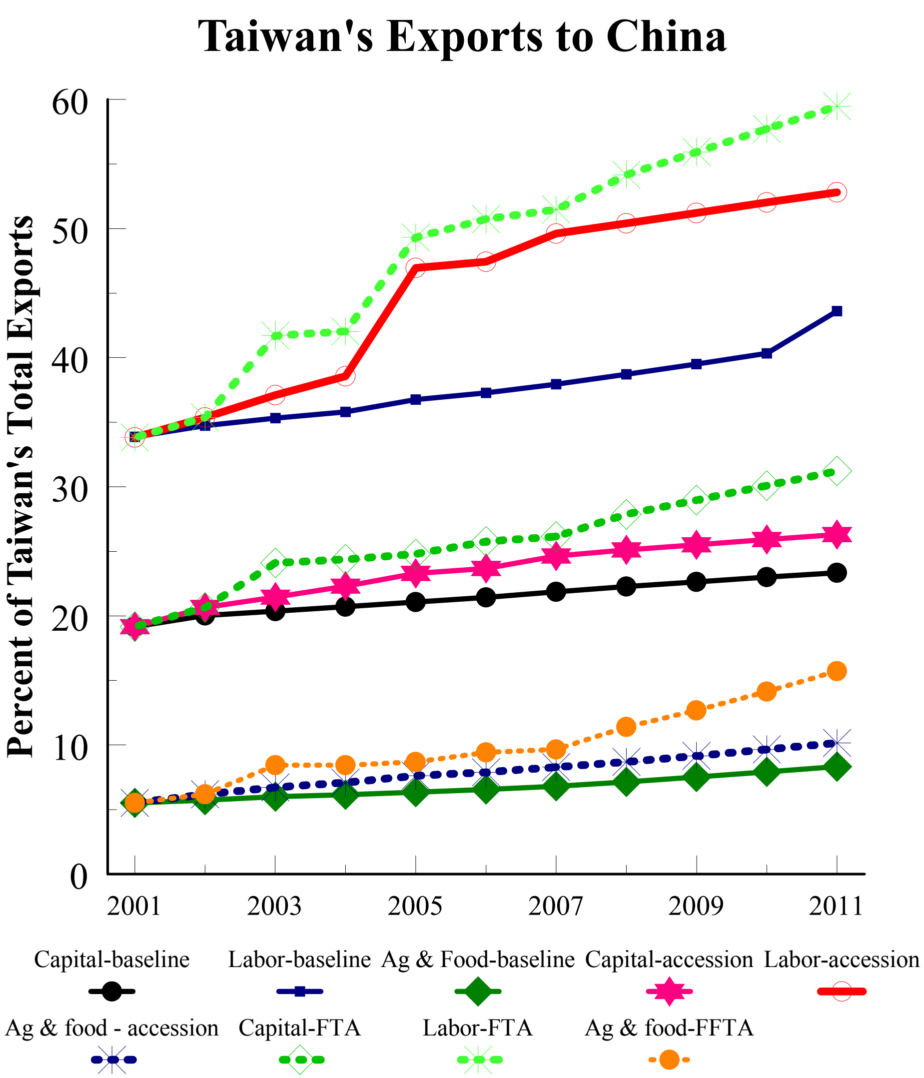
2001-2011

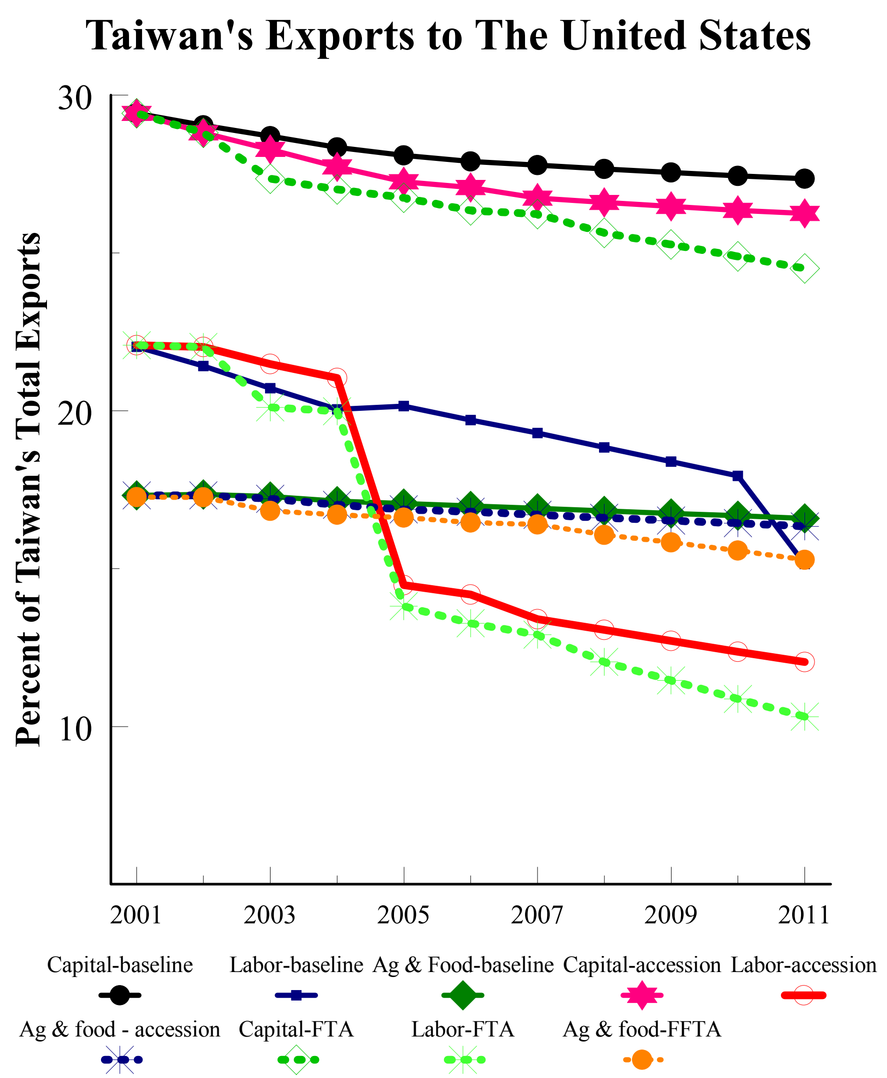




WTO Entry Increase Taiwan's Export Dependence on China, But Decrease its Dependence on US. Market, Especially in Manufactured Products

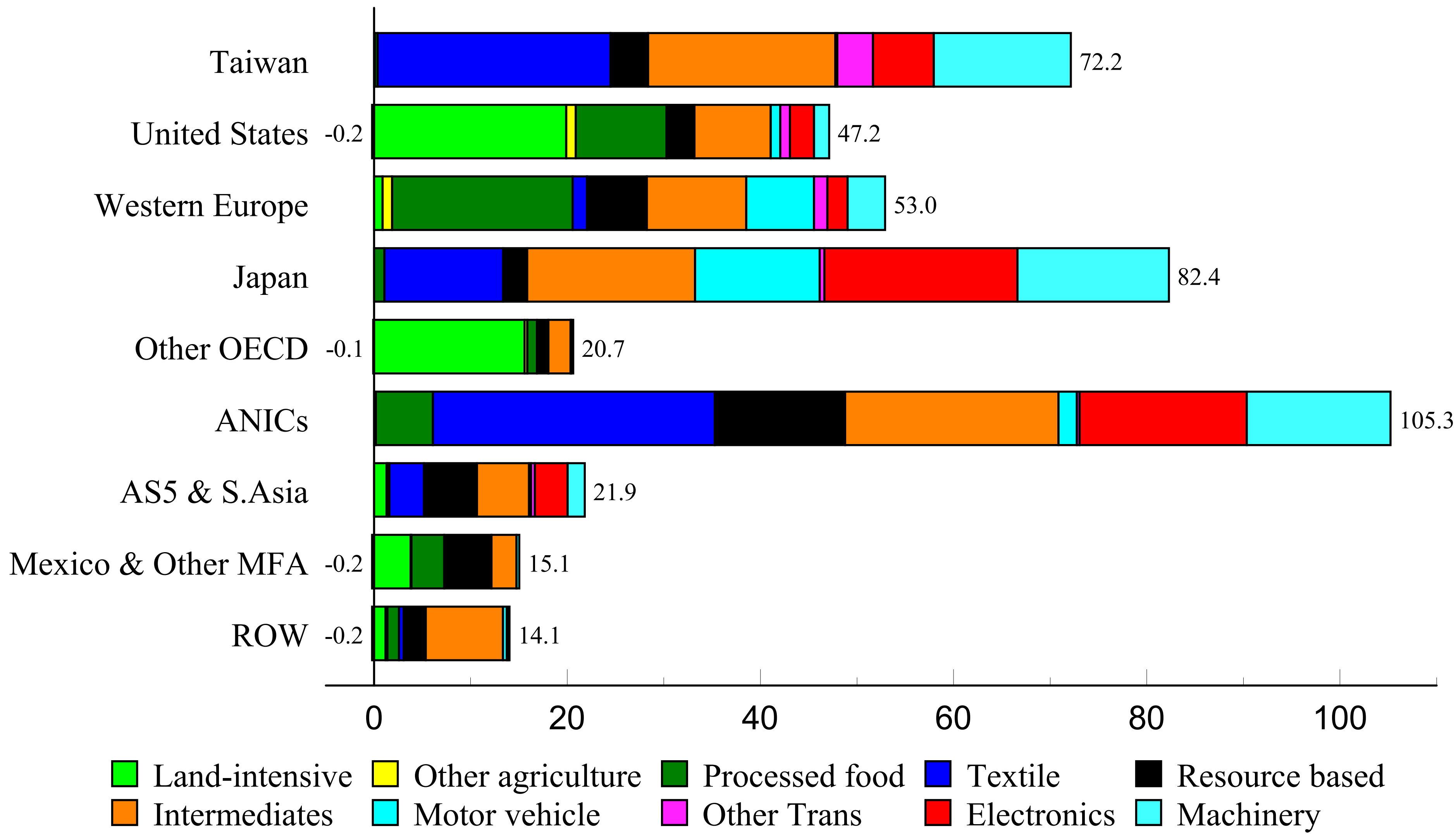
2001-2011





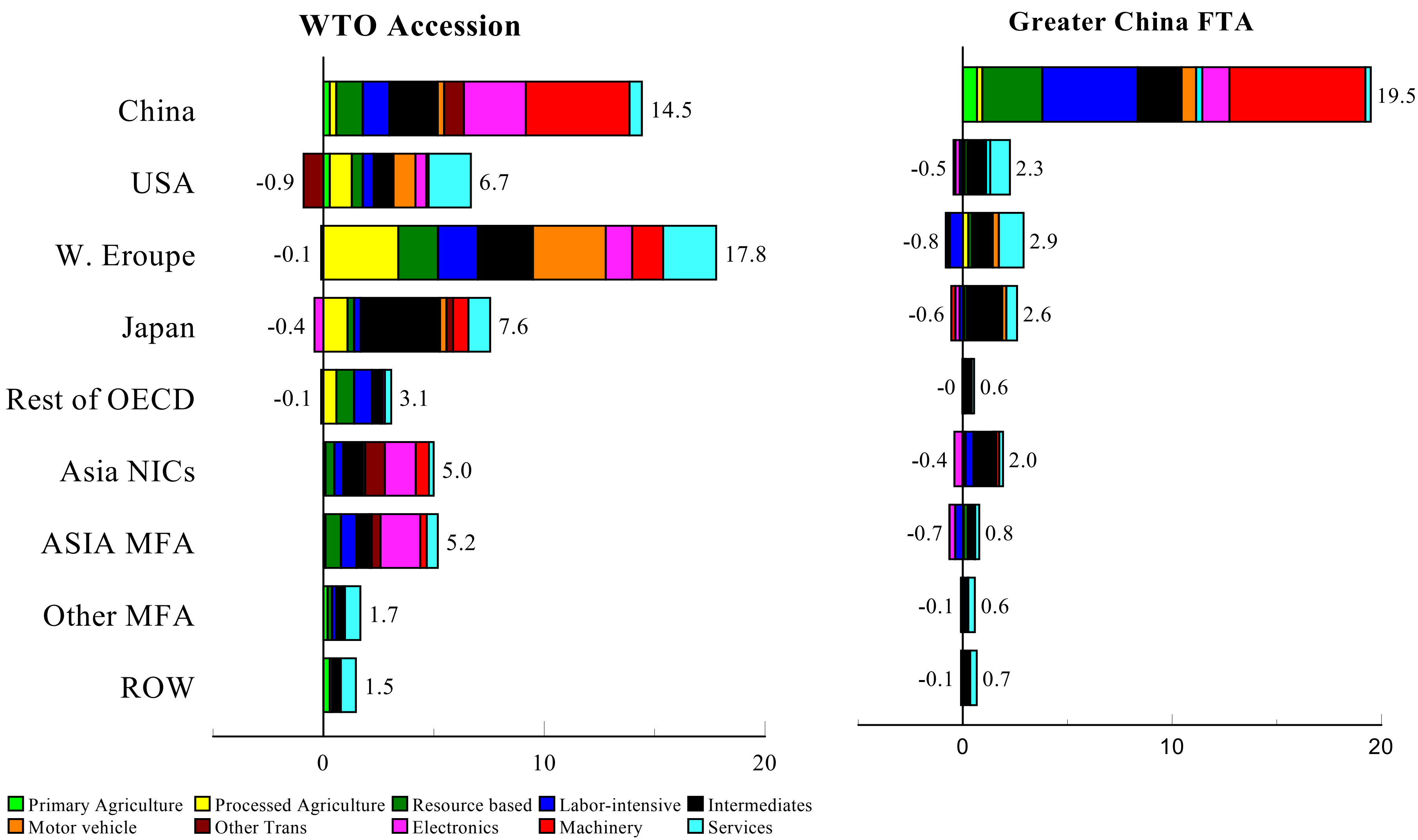
Impact of WTO Entry: Increase of China's Imports of Intermediates and Capital Goods from Asian and Industrial Countries, and Agricultural Products from Land Abundant Countries

2002-2011 accumulated



Impact of WTO Accession: Taiwan imports more agricultural, intermediate and capital intensive goods from developed countries

2002-2011 accumulated

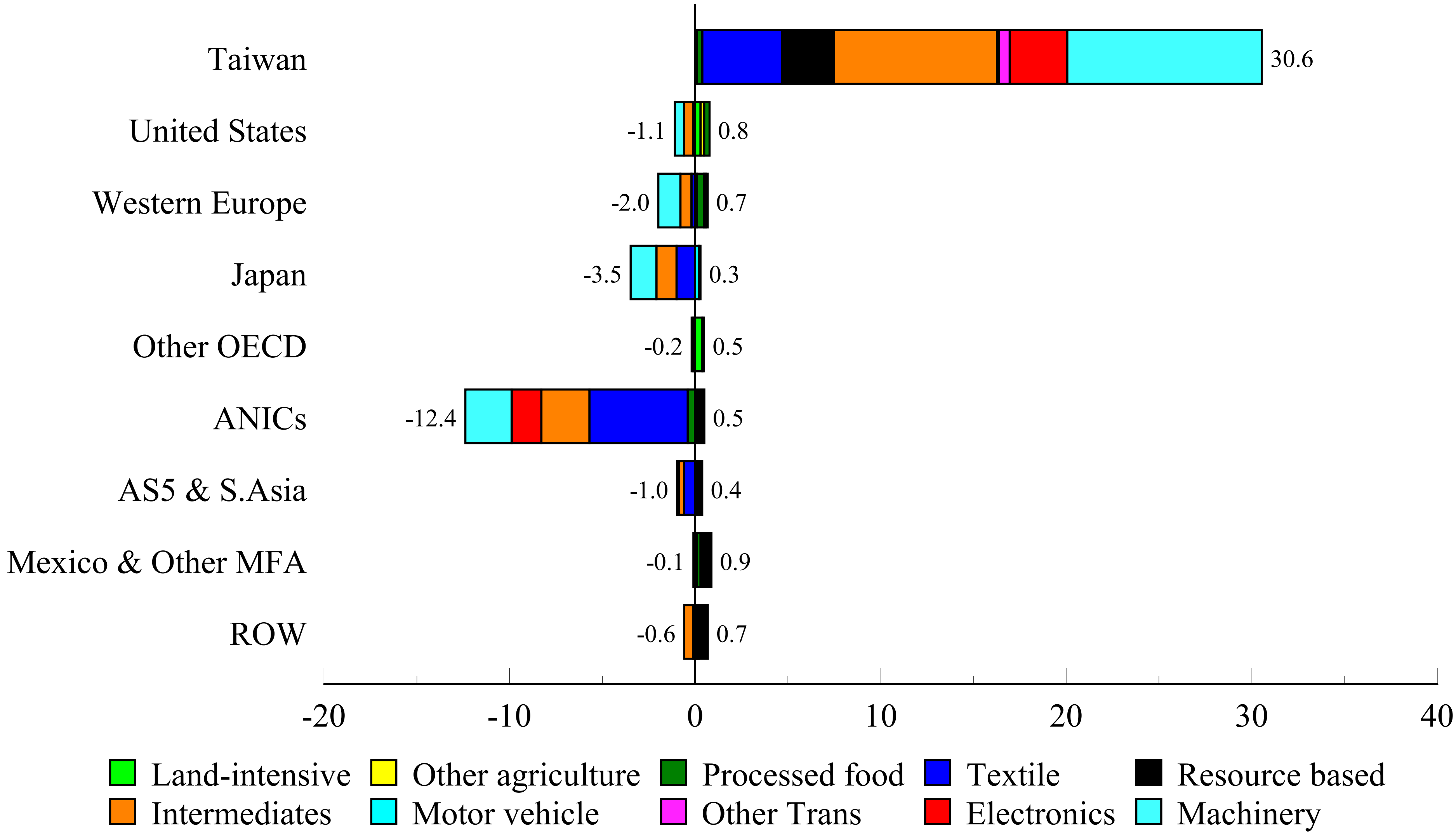


Redirection of Trade Flows

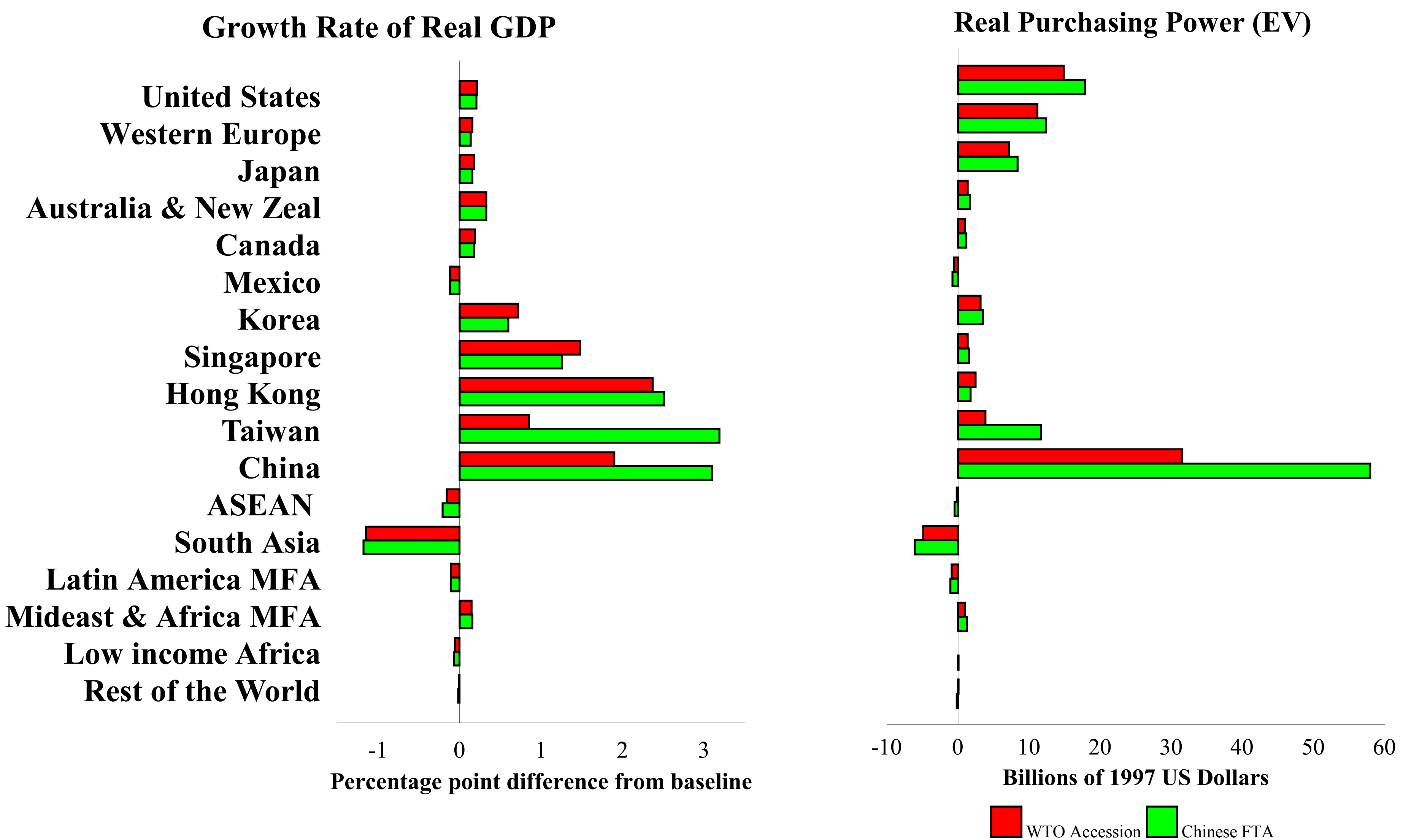
- The further increase in NICs' exports of intermediate and capital goods to China
- The further increase in China's exports of manufactured finished goods to developed countries and low-end durable manufactured products to developing countries
- The further decline of NICs' exports of labor-intensive finished goods to developed countries
- The further increase of NICs' high technology products imports from advanced industrial countries are all the results of such an adjustment process.
- China and Taiwan's WTO entry will further accelerate this process.

Impact of a 'Greater China' FTA:China Divert its Imports from Other Countries to Taiwan

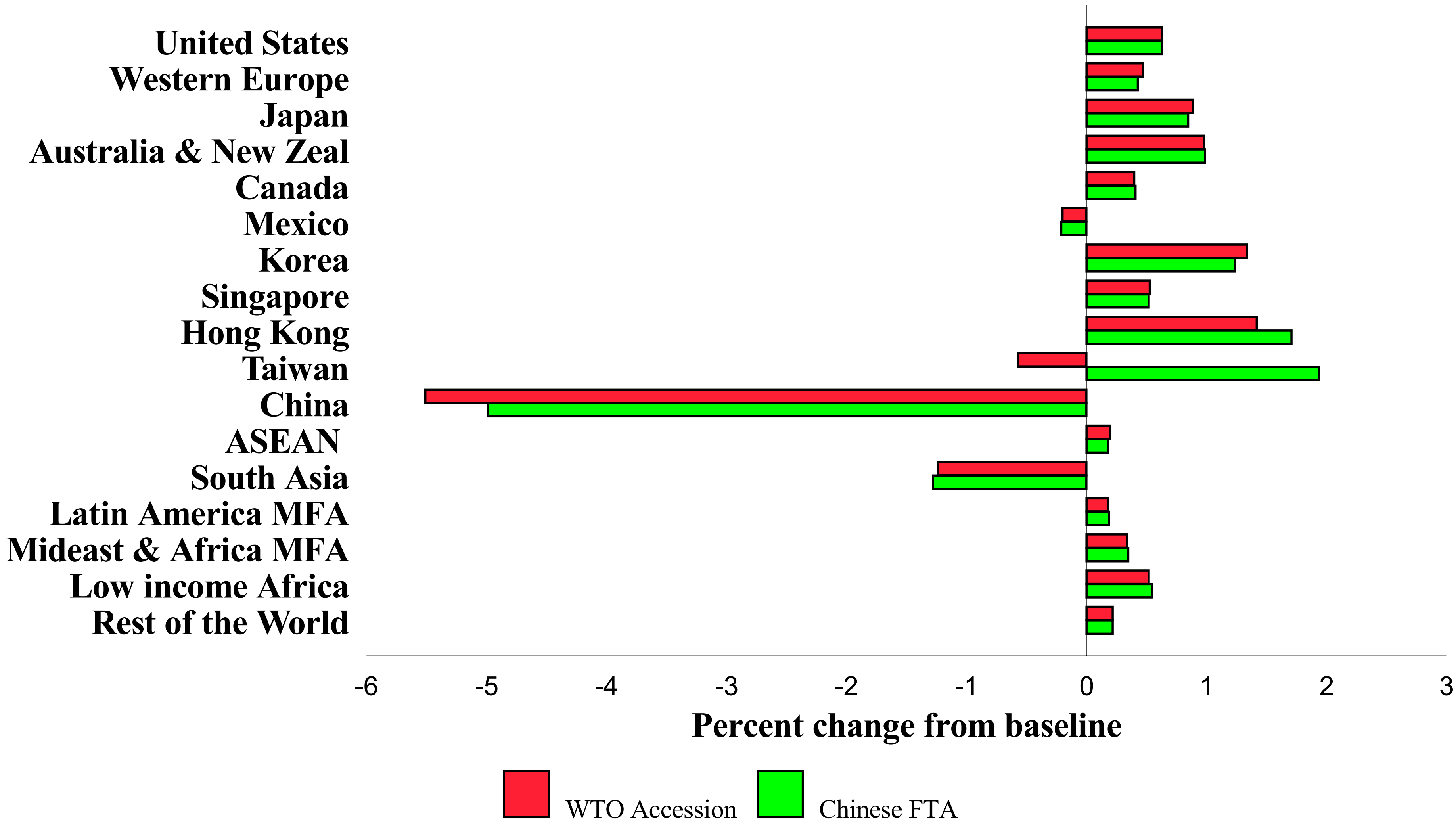
2002-2011 accumulated



China is the Biggest Gainer in its WTO Accession Taiwan Gains More from Further Integration with China United States and Rest of the World Also Gain from Liberalization in Chinese Economies



Impact of China and Taiwan's WTO Entry: Changes in International Terms of Trade



Conclusion

- **The simulation results shown that China will gains the most from its WTO entry. It will emerge as the world largest manufacturing center during its integration into the world economy. Taiwan will become an upstream suppliers for China's massive manufacturing productions.**
- **The economic dependence of Taiwan on China will further increase and enable China to replace the US as the number one of its export market. A greater China FTA will further reduce the cost of vertical integration among manufacturing industries across the Strait and enhance the efficiency of production factor allocation within the three Chinese economies, thus enable them become a stronger competitor of manufactured goods, especially for labor-intensive products, electronics and low-end capital-intensive products in the world market.**

Conclusion -- continued

- Taiwan will gain more economically by further integrate its economy with China via greater China FTA or other means after its WTO entry.
- Rest of the world, especially developed countries and Asian newly industrialized economies, as well as resource abundant developing countries would also benefit from further liberalization of Chinese economies. Only developing countries with an endowment and export structure similar to China's, such as South Asia and ASEAN countries may experience keener competition in labor-intensive exports and lower prices for their products.

Policy Implications

- **Economic interdependence between China and Taiwan will further deepen and economic integration of the two economies will accelerate after both of them enter the WTO. This is a continued trend that started in the mid-80s driven by market force and is a part of the production relocation process based on changing comparative advantages in East Asia region. It is also an organic component of economic globalization.**
- **Therefore, economic integration across the Taiwan Strait is not a policy preference but a fact of life determined by the 'invisible hand' and rooted from the position of China and Taiwan in the dynamic chain of international comparative advantage. No matter what efforts are made by governments on both sides of the Strait, this economic integration process may only be slowed down or accelerated. The future direction of the course is impossible to change by any political will.**
- **Economic integration is the best strategy to pursue a peaceful and stable Cross Strait relations and provides a win-win prospect for China, Taiwan and the United States.**