PROJECT FOR THE
NEW AMERICAN CENTURY

PROJECT PAPER
A U.S.-TAIWAN FREE TRADE AGREEMENT

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The free trade agreement or FTA and its close relative the Customs Union seem to be the preferred instrument of international trade diplomacy.[1] There are now dozens of such special arrangements to eliminate trade barriers between neighbors or selected trading partners all over the world. These agreements have co-existed with the multilateral global trading system since the beginning of that system, owing to the recognition from all parties that these special relationships were inevitable and, in the view of most, beneficial.

Many of these agreements have natural and obvious geographic or cultural roots, but some trading powers, notably the European Union and the United States have cast the net fairly widely. The European Union -- which is itself a preferential trade agreement -- has been striking arrangements with trading partners from Africa to South America.[2] Though some have criticized the European agreements for excluding agriculture and thus potentially conflicting with the World Trade Organization requirements, the EU has seemed to systematically employ FTAs to promote its international trading interests by securing traditional markets and expanding into new ones.[3]

For its part, the United States established FTAs in the 1980s with Canada and Israel and expanded that list in the 1990s to include Mexico.[4] The Clinton Administration late in its tenure struck a new FTA with Jordan and initiated negotiations with Singapore and Chile[5]. Upon taking office, the Bush Administration expanded the effort. It joined with Congress to approve the U.S.-Jordan FTA,[6] completed negotiations on the U.S.-Chile and U.S.-Singapore FTAs,[7] and initiated new talks with Morocco[8], the countries of Central America,[9] Australia,[10] South Africa,[11] and Thailand.[12] Further negotiations are said to be under consideration with Bahrain, the Dominican Republic, and all of the countries of the Middle East.[13]

Some have criticized the selections for not obviously advancing U.S. trade interests. International trade considerations, however, have never been and can never be the only basis on which countries establish special trade relationships. In almost every case, economic interests are weighed in addition to diplomatic, security, and even social interests. For example, the first U.S. Free Trade Agreement was with Israel, a small, far-away trading partner. Clearly and appropriately other interests were considered in deciding to conclude the pact. Legitimate concerns can be raised about particular FTA partner selections of the Bush Administration, although in each case a good affirmative case can be advanced, particularly in light of world events.

It is harder to understand, however, why some countries have not been selected as potential FTA partners. Perhaps the most difficult case is Taiwan. Taiwan is a strong ally that has blossomed into a vibrant democracy with good records by almost every objective measure. Taiwan is also a strong trading power that is a promising potential market for many U.S. exports.

This paper analyzes the potential for a U.S.-Taiwan FTA. In addition to reviewing the literature on the subject, it considers the potential pros and cons of such an arrangement and addresses the concerns that have kept a U.S.-Taiwan FTA from becoming a reality.

A PROFILE OF U.S.-TAIWAN TRADE

The United States and Taiwan have a substantial bilateral trade relationship. Taiwan -- one of Asia's original economic tigers -- has had strong economic growth particularly since 1961. During that period and with help from strong exports to the United States, Taiwan managed to transform itself from a largely agrarian economy to a fully industrialized economy. The annual economic growth of over 8 percent for that period also allowed Taiwan's per capita income to rise from developing country levels to an annual level of nearly $13,000 - comfortably set among the list of developed economies.[14] As it stands today, Taiwan has gone from focusing on fairly low value, labor-intensive products to high tech manufacturing that plays a particularly important role in laptop computers, semiconductors, and related technology[15].

As noted, Taiwan's trade relationship with the United States has been strong for decades. Taiwan consistently ranks among the United States' ten largest trading partners. Taiwan is presently the 10th largest market for U.S. exports and the 8th largest source of U.S. imports.[16] **(Table A)**

Although Taiwanese commerce has diversified in recent years, the United States remains Taiwan's largest trading partner, its top export market, and the second largest source of imports into Taiwan (Japan is first). Aside from the United States, Taiwan's major trading partners are Japan, Hong Kong, China, the European Union, Korea, and Singapore.[17] **(Table B)**

Total trade between the United States and Taiwan hit a high of nearly $63 billion in 2000. Since that time it has slumped due to sluggish economic growth in both countries. Taiwan has maintained a substantial trade surplus with the United States in recent years -- on the order of $15 billion, but both countries have seen their exports to the other decline since 2000.[18] **(Chart C)**

Leading U.S. exports to Taiwan are electrical machinery, equipment, scientific instruments, and agricultural products. **(Chart D)**

Taiwan is a strong market for U.S. agricultural exports; currently, it is the fifth largest export market for U.S. agricultural products. U.S. agricultural exports to Taiwan in 2001 stood at $2.3 billion. This figure represents a decline from five years earlier. The major explanation for the decline is the impact of the Asian financial crisis and slow economic growth in both countries. Wheat, grains, soybeans, and cotton made up the bulk of U.S. agricultural sales to Taiwan A number of other products, such as meats, breakfast cereals, and animal feeds round out U.S. agricultural exports to the Taiwanese market.[19]

Leading Taiwanese exports to the United States are concentrated in manufactured products. The leading items are consistently office machines, computers, electrical machinery, and telecommunications products.[20] **(Chart E)**

The substantial U.S.-Taiwan trade relationship is also supported by substantial bilateral investment. Taiwan is a major site for U.S. overseas investment. Most of the investment, as is typical of the pattern with other countries, is concentrated in the sectors in which trade is concentrated. U.S. investment in Taiwan totaled $7.7 billion in 2000[21] and is focused in manufacturing, the financial sector, and wholesale trade, and services.[22] Taiwanese investment in the United States is concentrated in the manufacturing sector. Although there is some dispute about exact figures, Taiwanese foreign investment is now concentrated in mainland China with investment in the mainland far outstripping investment in the United States and other trading partners. **(Chart F)**

COMPARISON WITH OTHER U.S. FTAs AND POTENTIAL FTAs

Until recently, the United States maintained relatively few FTAs. The United States struck its first FTA with Israel in 1986.[23] Subsequently, an FTA was concluded with Canada in 1988,[24] which was broadened to include Mexico in the North American Free Trade Agreement in 1994.[25] The Clinton Administration negotiated an FTA with Jordan in 2000, which the Congress approved in 2001.[26]

The Bush Administration has taken an ambitious tack on negotiating new FTAs. Two FTAs launched by the Clinton Administration were wrapped up shortly after Congress granted new negotiating authority in 2002. The Congress approved these FTAs by large margins in the summer of 2003.[27] The Bush Administration has also launched new negotiations aimed at reaching an FTA with a number of countries, including Australia, Morocco, Thailand and the countries of Central America.[28] The President also announced his ambition to conclude a Free Trade Agreement encompassing the entire Middle East in the next decade. Other countries have been suggested as possible FTA partners for the future.

Compared to other U.S. FTA partners and potential FTA partners, Taiwan ranks very high. In fact, of that group, only Canada and Mexico traded more with the United States than Taiwan -- and that was in 2002, a year when total trade contracted somewhat because of difficult economic conditions. Even under those conditions, the United States and Taiwan traded more than 50 times as much as the U.S. and Jordan or the U.S. and Morocco. Trade between the United States and Taiwan was more than eight times greater than trade between the United States and Chile. Trade between the United States and

Belize, the smallest on the current list, was less then one quarter of one percent of trade between Taiwan and the United States.[29] **(Chart G)**

Of course, the simple volume of trade is only one of the issues to be considered in selecting potential FTA partners. The volume of trade, however, coupled with the issues addressed later in this paper makes a strong prima facie case for Taiwan as an FTA partner.

ECONOMIC ANALYSIS OF A U.S.-TAIWAN FTA

To date, the only comprehensive study of a U.S.-Taiwan FTA released in the United States was conducted by the U.S. International Trade Commission (ITC) at the request of the U.S. Senate Finance Committee.[30] It was issued in October 2002. The International Trade Commission is an independent agency of the federal government that is tasked with a number of responsibilities in implementing and reviewing U.S. trade policy. This study was done as part of the ITC's function as the federal government's "think-tank" on trade issues. The Commission regularly performs policy analyses of a wide variety of topics and reviews of trade agreements before they are approved by the U.S. Congress.

The ITC's report includes a comprehensive review of the issues associated with a U.S.-Taiwan FTA, including an analysis of the U.S. and Taiwanese economies, a review of trade and investment flows between the United States and Taiwan, trade agreements relevant to the topic, and trade barriers in both countries relevant to the topic.

The core of the ITC analysis is a general equilibrium economic simulation of the impact of a U.S.-Taiwan FTA on both economies. Compared to the baseline of projected trade flows under current conditions, the ITC analysis found that the overall impact on both the U.S. and Taiwan would be small in terms of total GDP growth, an expected outcome. From the U.S. perspective, both exports to and imports from Taiwan would rise. After four years of operation, with 2001 used as a starting date, U.S. exports to Taiwan were projected to increase by 16 percent while imports from Taiwan would rise approximately 18 percent.[31]

Of course, any economic modeling exercise, including this one, has limitations. The assumptions on growth and the behavior of private sector actors are all debatable. In addition, a real FTA may have a slow phase-in in certain sectors. In addition, the impact of new rules in services, intellectual property, or trade in services are difficult to capture in modeling exercise, given the complexity of agreement provisions and limited experience. Still, the overall results of the ITC study are generally compatible with work done from many sources on a number of trade agreements.

On a sectoral basis, the ITC study predicted substantial gains in exports and in the affiliated portion of the U.S economy in agriculture, motor vehicles and parts, electronic equipment, and machinery and equipment. The sharpest declines -- less than half of one percent -- came in the U.S. textiles and apparel sector.[32]

For Taiwan, gains were projected in textiles and apparel (as much as 8 percent increase in total output), transportation equipment, chemicals, and some agricultural sectors. Declines were projected in some agricultural sectors, wood and paper products, electronic equipment, and meat and dairy products. In general both the aggregate and the sectoral gains and losses were larger in Taiwan than in the United States largely owing to the larger size of the U.S. economy.[33]

Both economies were projected to enjoy small positive net welfare gains.[34] Again, this result is consistent with economic analysis of similar agreements.

In general the ITC study confirms the conventional wisdom that an FTA is likely to generate gains for both economies, with limitations due to the overall size and relative openness of both economies. The listing of sectoral gains and losses may be the most interesting in that it identifies those industries likely to feel the strongest impact of a U.S.-Taiwan FTA. But caution should be used in analyzing the sectoral impacts because the precise provisions of an FTA could have substantial impact on the timing and size of those impacts.

CONCERNS ABOUT A U.S.-TAIWAN FREE TRADE AGREEMENT

Several concerns have been raised by opponents of a U.S.-Taiwan FTA. In addition to the concerns that apply to all free trade agreements, such as displacing U.S. workers, or undermining the World Trade Organization, there are three specific concerns raised regarding an FTA with Taiwan that warrant specific attention.

Intellectual Property

Protection of intellectual property, which includes various patented, trademarked, and copyrighted material, such as films, recordings, and drugs, has been an ongoing problem between the United States and Taiwan for many years. In recent years, attention has focused on illegal copying of copyrighted material including films and musical recordings at factories in Taiwan. Reported links between illegal copying operations in Taiwan and those in mainland China, have received considerable public attention.[35]

The United States has a procedure under its trade law known as Special 301 which is dedicated to focusing attention on intellectual property issues. Each year, under this provision the USTR identifies several categories of warnings climaxing in identification of a country as a “priority” country. A country’s placement on one of the several “watch list” may result in negotiations to resolve problem, often under threat of retaliation or WTO action.[36]

In 2003, Taiwan was named to the Priority Watch list -- the highest warning level -- for the third consecutive year. Many other countries are also named to watch lists, including Germany the country where intellectual property problems have the largest impact according to U.S. industry. But Taiwan was also identified as "one of the largest sources of pirated optical media products in the world." The repeated naming to the Priority Watch List and the associated rhetoric indicate increasing U.S. pressure to resolve this issue.[37]

Taiwanese officials from the President on down have pledged efforts to improve enforcement and heightened monitoring and compliance efforts have been launched. Last year, the government of Taiwan also signed agreements for proper use of the software Microsoft Office Suite and Norton Antivirus with software vendors.[38] Still, while acknowledging some progress, U.S. trade officials continue to argue that more must be done.[39]

Intellectual property has become a routine component of recent free trade agreements. The issue was first brought into the global trading system in 1994, during the Uruguay Round of GATT negotiations, and it has provoked continuing complaints from the developing world over access to patented drugs. Subsequent U.S. FTAs, notably those with Jordan, Singapore, and Chile, have included extensive intellectual property protection provisions.[40] Still, there have been continuing -- sometimes serious -- intellectual property protection issues with current and future FTA partners; notably Mexico, Thailand, and several Middle Eastern countries.[41]

In the case of Taiwan, the Administration and some in the private sector have reportedly raised Taiwan's record on intellectual property protection as a reason to not pursue an FTA. Recent press reports suggest that intellectual property protection is being identified by the Administration as a major source of bilateral tension effecting overall trade relations.[42] Some have speculated that this may in part be a negotiating tactic on the part of both parties to try to improve Taiwan's record before initiating FTA negotiations.

The emphasis on protection of intellectual property as a priority for U.S. trade policy is understandable and appropriate. It is unclear, however, why this issue would -- by itself -- be a barrier to proceeding with FTA negotiations. As noted, intellectual property concerns have never been used as a disqualifying issue with other current and potential FTA partners.

In fact, an FTA negotiation may be the best avenue for addressing intellectual property issues. In such a negotiation, the United States has considerable leverage given the interest of Taiwan's leadership in negotiating an FTA with the United States. An FTA negotiation would provide a unique opportunity to ensure attention to this issue at the highest level of the Taiwanese government. With such interest in concluding an agreement on the Taiwanese side, the U.S. could expect to win provisions like those in other FTAs, vastly improving respect for and enforcement of U.S. companies' intellectual property rights.

Given Taiwan's interest in an FTA with the United States it might even be possible to break new ground on intellectual property rights. Previous FTAs have provided the opportunity for ground breaking agreements on difficult issues. Consider the U.S.-Canada FTA on services,[43] the NAFTA on investment,[44] and the U.S.-Jordan FTA on trade and environmental issues.[45] One can imagine many possible inventive concepts being applied to intellectual property in an FTA between the United States and Taiwan. A mechanism for direct private sector access to dispute settlement analogous to that provided in the investor-state provision of the NAFTA is just one example.

Trade Diversion

One concern raised generically regarding all FTAs, Customs Unions, and preference programs is that special trading relationships can result in trade losses by parties outside of the special arrangement. In other words, the preferential tariff and trade concessions granted to beneficiary countries provide them a competitive advantage versus other countries.[46] This phenomenon is known as trade diversion.

The impact of trade diversion is often thought to be limited in cases where the trade relationship is already large, such as the United States and Canada. But in cases where the trading relationship is more limited and other countries would be competitive absent a special trade relationship the effect might be considerable, especially in case where, like Jordan, or Israel, the FTA partner is far from the United States. In preference programs, such as the U.S. Caribbean Basin Initiative or the African Growth and Opportunities Act, the stated purpose is essentially trade diversion and giving these countries unique access to the U.S. market to serve various geopolitical objectives.[47] In some cases, trade diversion from countries like China to countries like Mexico or various CBI beneficiary countries are even identified as a reason to pursue these special programs because these countries are morel likely to purchase U.S. exports or serve other objectives than the countries being diverted from, usually East Asian countries[48].

Concern about trade diversion is the primary reason that some have advanced for favoring global trade negotiations over all special relationships, most particularly FTAs. The founders of the world trading system -- while recognizing the tension between multilateral trade as embodied in the Most Favored Nation concept of the GATT/WTO and FTAs -- recognized from the outset that such special trade relationships were a political and perhaps economic inevitability. For example, the European Community, later the European Union, evolved shortly after the global trading system began to take shape. Still, the EC did not sideline the global trading system. In fact, working with the United States the member countries of the European community and eventually the EC itself formed the political core of like-minded countries that created and later expanded the global trading system. Thus, there was never truly an issue of whether these special relationships would be allowed, but rather on what terms. Article 24 of the WTO effectively defines the terms by requiring that FTAs encompass substantially all trade and be phased in within a finite period of time, which a working group later suggested would normally be ten years.[49] But even on those terms, there is no doubt that some trade diversion is the inevitable result of almost every FTA. This is why the arrangements are often sold domestically as a way to gain an advantage over competitors form third markets.

The case of a U.S.- Taiwan FTA is no different; some trade diversion is virtually inevitable. Critics have focused their criticism in this regard on the textile and apparel sector. As noted earlier, credible estimates of the likely impact of a U.S.-Taiwan FTA suggest that Taiwan's textile and apparel exports to the United States are likely to rise. Given that the U.S. industry -- particularly in the apparel sector -- is in a long-term decline, Taiwan's new exports are likely to come at the expense of another textile and apparel exporter, the primary suspect being mainland China.[50]

Some critics have suggested rather paternalistically that this may be a poor investment of Taiwan's resources. This is a debatable point and not one that has had any impact on policymakers in the United States and Europe where those same arguments could be made with greater force. In the end, it is probably safe to assume that Taiwan and Taiwanese investors can make their own investment decisions.

The more serious concern is that Taiwan's mainland neighbor will lose textile and apparel exports to the United States. Given China's low labor costs and dominant competitive position in the textile and apparel industry, it is almost a certainty that every FTA that impacts this sector is likely to have some at least potential trade diversion effect from China. This competitive position means that the Chinese industry is likely to grow strongly in absolute terms in the foreseeable future as the global liberalization in this sector moves forward. Thus, the impact is likely to be only lower when compared to a hypothetical global free trade case.[51]

Further, since these special arrangements are proliferating quite rapidly it seems strange to level this concern only at an FTA between the United States and Taiwan when it might be leveled with equal or greater force against FTAs between the United States and Thailand or Colombia, for example.

Beyond that, there are legitimate concerns about a world in which the United States is entirely reliant upon a country with which its long term relationship is uncertain and at times confrontational for any important commodity. The concern is probably less intense with regard to textiles than food or semiconductors, but it is a concern nonetheless.

More importantly, the United States has repeatedly chosen to strike special arrangements with other countries and groups of countries -- CBI, AGOA, Andean Trade Preference Act, and even NAFTA -- with part of the stated rationale from policymakers that imports from these countries were preferable to importing from East Asia, particularly China. Certainly, any rationale advanced to defend trade with these countries applies with equal force to Taiwan. Taiwan is a solid market for U.S. products. Taiwan has undergone a difficult but highly successful transition from authoritarian state to true democracy under U.S. tutelage. Given this development and the unique history of U.S.-Taiwan relations, a strong case can be made that an FTA with Taiwan should be a priority of U.S. foreign policy -- certainly above the countries of the Andes or the Caribbean.

In short, any diversion of trade from China or elsewhere to Taiwan under a U.S.-Taiwan FTA, is entirely in keeping with WTO rules and likely to serve U.S. interests on a number of fronts.

China's Objections

There is little doubt that the core objection to a U.S.-Taiwan FTA is concern over offending mainland China. This is not to say that the intellectual property protection, trade diversion and other concerns are not validly taken. It is difficult to accept, however, that these justify not pursuing an FTA with Taiwan, given that they apply with equal or greater force to other FTAs which the United States is enthusiastically pursuing. In large part, these concerns seem to be false fronts to conceal the real concern, offending Beijing.

As anyone familiar with the complex balancing act that characterizes China-Taiwan-United States relations can attest, China takes umbrage at virtually any move by the United States to upgrade its treatment of Taiwan. China claims Taiwan as a renegade province and objects to any measure which would acknowledge the reality that Taiwan is a de facto separate country. From the mainland's perspective, a visit by Taiwan's President to his U.S. alma mater is cause for an international tirade.[52] Ongoing sales of weapons and low level visits by U.S. officials are cause for routine protest.[53] In the recent SARS health crisis, China even sought to limit the ability of the World Health Organization to come to the aid of Taiwan.[54] Beijing would certainly protest an effort by the United States to strike an FTA with Taiwan.

The simple truth is that China would prefer Taiwan did not exist -- at least, not as an independent democracy. Taiwan, however, is a strong and vibrant democracy with a population comparable in size to California, Australia, or Canada. In point of fact, Taiwan --- while much smaller than mainland China -- is actually larger in terms of population than the majority of the world's countries.[55] The United States should no more be willing to have its relations with a young Asian democracy constrained by Beijing, than it would its other strong allies, like Australia or Canada.

Despite the complex and sometimes befuddling history of U.S. relations with Taiwan, the Taiwan Relations Act specifically authorizes an ongoing relationship, including trade agreements, between the United States and Taiwan.[56] Bilateral trade negotiations and agreements between the United States and Taiwan on topics, such as intellectual property protection, have been going on for decades. Taiwan is a member of the WTO, albeit as a customs territory.[57] A bilateral free trade agreement would be nothing more than another step in a trade relationship going back decades between two separate WTO members. Provided the agreement met the conditions set in Article 24 of the WTO, China would have no grounds to complain.

Nor is there reason for worry that concluding an FTA with Taiwan would cause China to become uncooperative in international affairs. As a member of the United Nations Security Council, China wields considerable diplomatic influence. The United States believes China is essential in dealing with North Korea's and its nuclear program[58] and other issues. China, however, does not pursue North Korea's stability, or combat terrorism, as a favor to Washington. These goals serve China's own interests. There is no reason to think that China will stop acting in its own interests because the United States pursues its legally mandated relationship under the Taiwan Relations Act with Taiwan.

And even if Beijing were to protest appropriate U.S. initiatives toward Taiwan, is there any real doubt as to the appropriate U.S. response? If Beijing were to make similar demands with regard to another democratic ally -- Australia, Canada, or New Zealand -- would the United States even contemplate capitulation? The clear answer is no. Would the answer be any different if the islands of New Zealand or Australia lay just off China's coast? Again, no. The answer should be different for Taiwan. In fact, forcing the U.S. to abandon an FTA between Washington and Taipei would only fuel further mainland demands regarding not only Taiwan, but also Beijing's other objectives, such as the South China Sea, Tibet, or foreign policy disagreements with the United States. Indeed, this scenario seems much more plausible than a dramatic shift on Beijing's policy with regard to North Korea in the event of a U.S.-Taiwan FTA.

Beijing's displeasure, in and of itself, is a monumentally poor reason for the United States not to do something. In this case, Beijing's objections to a U.S.-Taiwan FTA have no substantive validity and thus deserve no weight in making policy.

AFFIRMATIVE CASE FOR A U.S.-TAIWAN FTA

Notwithstanding objections to the concept or impact of free trade agreements, it is undeniable that we are in the era of the FTA. Europe has been pursuing FTAs with various countries for some time.[59] The United States has enthusiastically launched a wave of FTA negotiations. There has been for some time a consensus in the economic community that trade liberalization is a strong engine of growth. In fact, some argue, one of the strongest in the post-war era. Over time, this support has led to the development of a political consensus with a wide range of policy makers in both major political parties supporting free trade. Recent strong congressional approval for free trade agreements with Chile and Singapore demonstrates that this consensus -- although undergoing some strain in the last decade -- continues influence trade policy.[60]

That being the case, the question might more appropriately be framed in terms of "which" rather than "whether." Viewed from that perspective, the absence of Taiwan from the list of countries eligible for FTA negotiations is notable and difficult to explain. From a purely economic perspective, Taiwan is the largest potential FTA partner for the United States to be excluded from consideration. The European Union is barred for political reasons and because of agriculture disputes. China has an unreliable trade policy-making machinery and would face U.S. domestic opposition over its human rights record, among other things. As noted in the introduction, the existing U.S.-Taiwan trade relationship is larger than any with an existing or pending FTA partner, except Canada and Mexico, and far eclipses that with many of the countries now in FTA talks with the United States.

The ITC study concluded that an FTA would help both Taiwan and the United States expand trade and improve economic growth. While all economic models concede that the impact of a U.S.-Taiwan FTA would be limited on the U.S. economy given its large size, which incidentally would be the case with all FTAs, all available analysis points to a positive economic impact.

Beyond the direct impact on the U.S. economy, a U.S.-Taiwan FTA would provide an important doorway for America's entry into the region. It is possible, for example, to imagine a marriage of American capitol and technology with Taiwanese language skills and cultural knowledge helping to establish a stronger economic foothold for U.S. companies in China.

Foreign Policy Rationale

None of the FTAs the United States has negotiated was pursued strictly for economic reasons. In each case, there are unique political, diplomatic or strategic concerns that make the potential FTA partner attractive. Certainly, those concerns were dominant in many cases, including Israel, Jordan, Morocco, and others. In the case of Taiwan, however, a strong case could be made for pursuing an FTA on these factors alone. The U.S. is committed to Taiwan's defense. Indeed the Taiwan Relations Act recognizes the U.S. commitment to Taiwan and speaks to the close historical, cultural and personal ties United States has with Taiwan.[61]

Moreover, Taiwan is a textbook case of an authoritarian government that has completed the transition to democracy culminating in a peaceful hand over of power and thriving multi-party democracy. Taiwan is a strong demonstration case that the U.S. prescription of democracy and free markets can succeed. The very existence of a thriving Taiwan is a powerful example for other countries and a possible model for reform in mainland China. Surely, for foreign policy reasons the United States should do all that it reasonably can to bolster Taiwan and stabilize its economy. The establishment of an FTA would seem to promote these objectives in a way that nothing else could.

At the very least, it is in the United States interest to provide Taiwan alternatives to excessive reliance on mainland China for commerce and trade, which might, and China hopes will, undermine a self-sufficient, independent Taiwan. This seems to be the primary reason why the concept of an FTA with the U.S. is popular in some circles within Taiwan.

There is considerable basis for the view that an FTA would allow for expanded economic ties with the United States. Dismantling barriers would certainly -- as the ITC study predicts -- lead to a substantial increase in bilateral trade. Both Taiwan and the United States would become more important trading partners for each other. The new opportunities would likely induce businesses in both countries to invest in building new capacity to trade with the other country. This is particularly true in Taiwan's case given its smaller size relative to the United States. The expanded trade would also bring expanded bilateral investment -- again as the ITC predicts -- to support the expanded trade.

Given its proximity and cultural affinities, Taiwanese business would certainly continue to find China attractive, but doing business in China has considerable risk for Taiwanese business, particularly given the tense ties between Beijing and Taipei. At minimum, an FTA would likely increase trade and commercial ties between Taiwan and the United States and provide a real alternative to Taiwanese business to ever expanding trade and commerce with China. It is important to keep in mind that the United States remains far and away the largest market for most of the products produced in Taiwan.

Trade Policy Benefits

Finally, international trade policy could reap benefits from an FTA with Taiwan. As noted, FTAs can demonstrate the potential for foreign trade agreements in new areas, which can then be used as a template for future agreements. The U.S.-Canada FTA served this role with regard to trade in services, and the NAFTA with regard to investment. The close relationship between the U.S. and Taiwan coupled with Taiwan's interest in an agreement might make it possible to break new ground in intellectual property, as suggested earlier, or establish a sweeping agreement in services -- an area highlighted by the ITC report.[62]

One of the often stated reasons for pursuing FTAs aggressively is that it puts pressure on non-parties to be more supportive and forthcoming in WTO talks in order to ensure that they are not cut out of markets by FTAs. This was a prominent rationale for launching the U.S.-Canada FTA and it seems to have paid off in the creation of the WTO. But it is difficult to see how a U.S. FTA with Jordan or Morocco, with their small economies, puts pressure on the EU or Japan to devote themselves to WTO talks and make difficult concessions. An FTA between two of the world's ten largest trading powers -- the United States and Taiwan -- would, however, send a powerful signal That signal might also make China move forward more aggressively in implementing the WTO commitments it has made and negotiating new ones, rather than dragging its feet in trade talks as it now does.

CONCLUSION

The case for a U.S.-Taiwan FTA is compelling on economic, diplomatic and strategic grounds. In fact, the combined case made by these interests far outweighs that for any other FTA partner. The fact that such negotiations are not a priority for the

United States is due to an unfortunate subordination of these interests to a misplaced concern over offending China. That concern, however is simply not sufficient justification for failure to embrace the tremendous multi-faceted opportunity offered by a U.S.-Taiwan FTA.

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[1] A free trade agreement or FTA is a broad liberalizing agreement between two or more countries. To comply with the WTO it must involve the dismantling of trade barriers - tariff and non-tariff – on "substantially all" trade between the parties.
[2] Office of the United States Trade Representative, *available* at http://www.ustr.gov.
[3] *Id.*
[4] *Id.*
[5] *Id.*
[6] *Id*.
[7] *See* http://www.ustr.gov/new/fta/chile.htm and http://www.ustr.gov/new/fta/Singapore.htm (last visited Aug. 21, 2001.)
[8] *See* http://www.ustr.gov/new/fta/morocco.htm (last visited Aug. 21, 2001.)
[9] *See* http://www.ustr.gov/new/ftacafta.htm (last visited Aug. 21, 2001.)
[10] *See* http://www.ustr.gov/new/fta/Australia.htm (last visited Aug. 21, 2001.)
[11] *See* http://www.ustr.gov/new/fta/sacu (last visited Aug. 21, 2001.)
[12] Office of the United States Trade Representative, available at http://www.ustr.gov.
[13] Id.
[14] Shirley W. Y. Kuo and Christina Y. Liu, *The Development of the Economy of Taiwan, Asian Pacific Economic Literature*, pp. 36-49, 1999.
[15] Kuo-Ting Li, *The Evolution of Policy Behind Taiwan's Development Success,* 54 (World Scientific Publishing, 1995.
[16] Adapted from World Trade Organization 2001 statistics.
[17] *Id.*
[18] U.S.-Taiwan FTA: Likely Economic Impact of a Free Trade Agreement Between the United States and Taiwan, USITC Pub. 3548, Inv. No. 332-438, at 3-6 to 3-10 (Oct 2002) ("USTR Pub. 3548").
[19] Compiled from official statistics of the U.S. Department of Commerce.
[20] USITC Pub. 3548, at 3-9, (compiled from official statistics of the US Department of Commerce).
[21] U.S. Department of Commerce, Bureau of Economic Analysis, available at http://www.bea.doc.gov.
[22] *Id*.
[23] Office of the United States Trade Representative, available at http://www.ustr.gov.
[24] *Id.*
[25] *Id.*
[26] *Id.*
[27] *Id.*
[28] *Id.*
[29] US Bureau of the Census: Foreign Trade Division © **USA Trade Online.**
[30] U.S.-Taiwan FTA: Likely Economic Impact of a Free Trade Agreement Between the United States and Taiwan, USITC Pub. 3548.
[31] *Id.*
[32] *Id.* at 7-5 (GTAP database and USITF calculations).
[33] *Id.* at 7-14 - 7-15 *Id.* at 7-5 (GTAP database and USITF calculations).
[34] *Id*.
[35] Tim Culpan, *Taiwan Remains On Watch List,* BPI Communications, June 7, 2003.
[36] *Id*.

[37] *Id*.
[38] *Id*.
[39] *Id*.
[40] *See* http://www.ustr.gov/regions/eu-med/middleast/US-JordanFTA. Shtml (last visited Aug. 21, 2003).
[41] *See* http://www.ustr.gov.
[42] *U.S. May Delay High-Level Contact Over Trade Disputes*, Financial Times Information, Global News Wire, October 17, 2002, LexisNexis.
[43] *See* http://www.ustr.gov.
[44] *Id*.
[45] *Id*.
[46] *See* http://www.ustr.gov.
[47] For the most part, products with substantial domestic comparison are excluded from or have limited benefits under such a program.
[48] See http://www.wto.org.
[49] *Id*.
[50] USITC Pub. 3548 at 5-1 to 5-3.
[51] International Trade Forum *available* at http://www.tradeforum.org.
[52] Anthony Spaeth, *Into The World; Lee Teng-Hui's Visit Is a Public Relations Triumph For Taiwan and a Problem For U.S.-China Ties*, Time Magazine, June 19, 1995, at 38.
[53] *Foreign Ministry Spokeswoman Repeats China's Opposition To Arms Sales to Taiwan*, BBC Worldwide Monitoring, June 20, 2001.
[54] *Chinese Official Says Taiwan Damaged Cross-Strait Ties By Refusing SARS Help*, BBC Worldwide Monitoring, June 2, 2003.
[55] UN statistics on population *available at* http://www.census.gov/cgi-bin/ipc/idbrank.pl (last visited Aug. 21, 2003).
[56] Taiwan Relations Act, Pub. L. 96-8, § 2, 93 Stat. 14, 14-15 (1979).
[57] *See* http://www.ustr.gov/reports/nte/2003/Taiwan.pdf, (last visited Aug. 21, 2003).
[58] Edward Alden and Andrew Ward, *Pyongyang Raises Hope Of Reaching Negotiated Peace On Nuclear Arms North Korea*, Fin. Times (London), Aug. 2, 2003, at 8.
[59] European Union FTA's, *available* at http://www.wto.org.
[60] Helen Dewar, *Senate Approves Chile, Singapore Trade Pacts; U.S. Hopes To Create Global Network*, The Wash. Post, Aug. 2, 2003, at E2.
[61] Pub. L. No. 96-8, § 2, 93 Stat. 14, 14-15 (1969).
[62] USITC Pub. 3548 at 5-24 to 5-32

A

Top U.S. Trading Partners

2002				January to March 2003			
Rank	**Country**	**Trade in billions of $US**	**Market Share**	**Rank**	**Country**	**Trade in billions of $US**	**Market Share**
1	Canada	371.39	20.00%	1	Canada	96.84	20.56%
2	Mexico	232.26	12.51%	2	Mexico	56.24	11.94%
3	Japan	172.93	9.31%	3	Japan	41.46	8.80%
4	China	147.22	7.93%	4	China	37.6	7.98%
5	Germany	89.11	4.80%	5	Germany	23.33	4.95%
6	United Kingdom	74.12	3.99%	6	United Kingdom	18.89	4.01%
7	Korea, Republic of	58.17	3.13%	7	Korea, Republic of	14.45	3.07%
8	**Taiwan**	50.59	2.72%	8	France	11.33	2.41%
9	France	47.43	2.55%	9	**Taiwan**	11.25	2.39%
10	Italy	34.38	1.85%	10	Italy	8.64	1.83%
	Other FTA Partners and Prospects						
	Singapore	31.01	1.67%		Singapore	7.83	1.66%
	Australia	19.56	1.05%		Israel	5.25	1.11%
	Israel	19.48	1.05%		Australia	4.28	0.91%
	Chile	6.39	0.34%		Chile	1.73	0.37%
	Egypt	4.22	0.23%		Egypt	0.92	0.20%
	Morocco	0.96	0.05%		Bahrain	0.45	0.10%
	Bahrain	0.81	0.04%		Jordan	0.28	0.06%
	Jordan	0.82	0.04%		Morocco	0.22	0.05%
	World	**1,856.86**			**World**	**471.06**	

Adapted from World Trade Organization 2001 Statistics

B

World Trade Powers, Ranked by Aggregate Imports and Exports

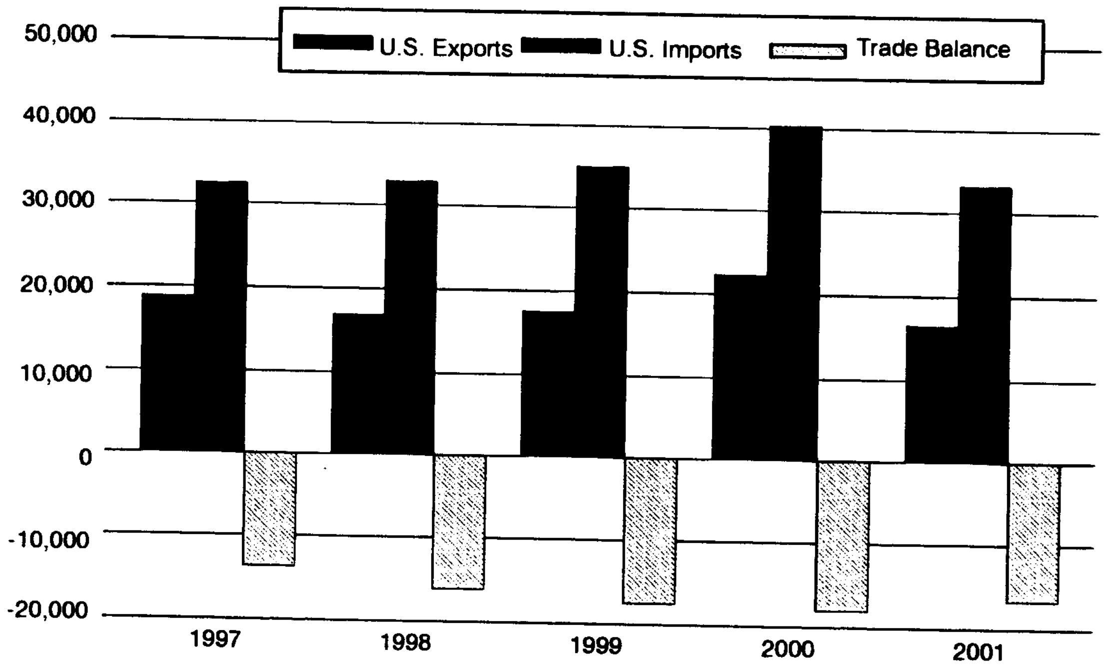
1	European Union (excluding Greece and Luxembourg)
2	United States
3	China (including Hong Kong)
4	Japan
5	Canada
6	Mexico
7	Korea
8	Spain
9	Singapore
10	Taiwan

Adapted from World Trade Organization 2001 Statistics

C

Figure 3-1
U.S trade with Taiwan, 1997-2001

(Millions of dollars)



Source: Compiled from official statistics of the U.S. Department of Commerce.

D

Table 3-2

U.S. exports to Taiwan, classified by two-digit SITC, 1997-2001 (million dollars)

SITC	1997	1998	1999	2000	2001
77 Electrical machinery, apparatus	3,063.0	2,923.9	3,384.3	4,814.0	3,687.7
79 Transport equipment, n.e.s.	2,128.3	2,667.9	2,108.1	1,438.5	1,255.7
72 Machinery specialized for particular industries	1,136.2	968.8	1,536.3	2,837.1	1,210.7
87 Professional, scientific and controlling instruments and apparatus, n.e.s.	840.4	877.5	1,085.7	1,976.8	1,065.7
75 Office machines and automatic data processing machines	862.5	797.4	737.7	961.8	838.9
74 General industrial machinery and equipment, n.e.s.	711.1	703.0	689.9	828.8	743.5
51 Organic chemicals	1,044.6	781.8	911.5	1,093.8	665.6
89 Miscellaneous manufactured articles, n.e.s.	653.4	626.0	457.3	677.2	646.9
04 Cereals and cereal preparations	872.3	538.4	608.4	613.9	643.2
76 Telecommunications and sound recording	555.0	572.2	429.1	567.1	484.2
57 Plastics in primary forms	421.7	346.8	402.3	452.3	418.4
22 Oil seeds and oleaginous fruits	650.7	277.2	395.2	389.7	388.6
71 Power generating machinery and equipment	328.0	303.9	293.3	434.9	354.0
73 Metalworking machinery	576.5	414.1	581.4	802.5	331.0
59 Chemical materials and products, n.e.s.	271.1	261.8	322.6	362.6	282.1
05 Vegetables and fruit	301.8	270.0	280.6	295.6	261.0
52 Inorganic chemicals	273.1	173.3	174.2	206.2	259.9
99 Non -identified products	246.9	243.3	259.6	326.8	232.6
21 Hides, skins and furskins, raw	214.7	165.3	165.0	184.1	201.3
28 Metalliferous ores and metal scrap	185.4	124.5	106.8	140.6	160.2
54 Medicinal and pharmaceutical products	108.1	101.4	113.8	139.9	144.2
88 Photographic apparatus, equipment and supplies and optical goods, n.e.s.; watches and clocks	115.8	125.6	146.3	194.2	146.4
93 Special transactions and commodities not classified according to kind	89.8	79.4	99.6	107.4	141.8
78 Road vehicles (including air-cushion vehicles)	438.6	258.8	204.0	229.5	140.4
64 Paper, paperboard, and articles of paper pulp	248.8	173.4	157.4	159.2	139.3
26 Textile fibers and their wastes	131.6	139.9	74.3	121.9	131.0
69 Manufactures of metals, n.e.s.	152.9	145.2	128.9	145.0	129.3
55 Essential oils and resinoids and perfume materials	133.4	112.9	109.1	130.7	123.0
66 Nonmetallic mineral manufactures, n.e.s.	114.9	83.8	84.7	90.6	112.4
09 Miscellaneous edible products and preparations	124.5	114.3	118.5	88.3	112.1
68 Nonferrous metals	240.8	200.2	161.7	203.1	100.7
58 Plastics in nonprimary forms	97.6	82.3	96.6	131.0	94.2
25 Pulp and waste paper	160.3	113.5	113.9	113.6	83.7
53 Dyeing, tanning and coloring materials	69.2	57.5	70.7	110.3	80.7
01 Meat and meat preparations	61.1	62.9	116.4	123.6	78.4
08 Feeding stuff for animals	93.9	86.0	74.5	78.8	76.5
61 Leather, leather manufactures, n.e.s.	35.6	59.1	43.4	61.8	62.5
27 Crude fertilizers (imports only)	75.3	82.4	78.0	69.1	61.5
33 Petroleum, petroleum products and related materials	153.8	128.4	119.9	130.1	60.0
12 Tobacco and tobacco manufactures	95.7	76.9	52.2	61.0	60.0
Other	804.6	602.2	546.2	510.6	416.7
Total	18,882.9	16,923.3	17,639.7	22,403.7	16,626.1

Source: Compiled from official statistics of the U.S. Department of Commerce.

E

Table 3-4
U.S. imports from Taiwan, classified by two-digit SITC, 1997-2001 (million dollars)

SITC	1997	1998	1999	2000	2001
75 Office machines and automatic data processing machines	9,875.5	9,560.5	9,640.8	10,592.2	8,751.3
77 Electrical machinery, apparatus	5,750.2	5,438.0	6,369.6	8,492.3	5,878.5
89 Miscellaneous manufactured articles, n.e.s.	2,145.8	2,105.7	2,256.2	2,654.6	2,470.8
76 Telecommunications and sound recording	1,589.7	1,926.4	2,237.6	2,986.2	2,361.9
69 Manufactures of metals, n.e.s.	2,313.1	2,427.2	2,487.6	2,639.1	2,321.3
84 Articles of apparel and clothing accessories	2,164.4	2,222.5	2,075.7	2,159.8	1,907.3
74 General industrial machinery and equipment, n.e.s.	1,182.4	1,282.3	1,410.5	1,472.4	1,376.6
78 Road vehicles (including air-cushion vehicles)	986.7	1,082.9	1,168.2	1,334.6	1,124.9
82 Furniture and parts thereof	924.2	966.7	1,009.1	1,031.2	765.6
93 Special transactions and commodities not classified according to kind	322.0	415.8	584.0	586.9	713.9
65 Textile yarn, fabrics, made-up articles, n.e.s	743.8	731.1	761.1	739.7	704.1
72 Machinery specialized for particular industries	541.7	568.6	616.4	704.8	626.0
98 Estimate of import items valued under $251	232.7	323.2	424.9	502.8	417.4
87 Professional, scientific and controlling instruments and apparatus, n.e.s.	283.0	341.0	343.7	433.8	372.7
67 Iron and steel	248.7	329.1	449.1	648.6	346.8
62 Rubber manufactures, n.e.s.	266.1	280.7	304.5	317.5	316.4
88 Photographic apparatus, equipment and supplies, optical goods, watches and clocks	360.4	375.5	361.1	342.2	282.6
73 Metalworking machinery	319.8	396.2	304.9	358.4	250.9
58 Plastics in nonprimary forms	198.0	207.6	210.5	257.6	229.8
79 Transport equipment, n.e.s.	64.0	99.7	118.2	155.0	184.6
03 Fish, crustaceans, molluscs, preparations thereof	183.6	206.1	220.0	180.0	184.2
71 Power generating machinery and equipment	137.4	142.4	161.7	184.1	182.7
66 Nonmetallic mineral manufactures, n.e.s.	232.6	187.8	182.0	182.2	167.6
81 Sanitary, plumbing, heating and lighting fixtures	274.1	262.4	260.9	235.2	156.8
83 Travel goods, handbags	183.5	176.4	149.1	138.4	129.8
51 Organic chemicals	73.6	83.1	68.8	84.6	111.7
57 Plastics in primary forms	74.0	89.3	109.2	128.2	104.5
63 Cork and wood manufactures	146.4	126.1	114.1	108.9	85.8
33 Petroleum, petroleum products and related materials	0.1	0.0	13.4	2.0	81.5
59 Chemical materials and products, n.e.s.	16.0	22.4	31.8	94.8	81.3
85 Footwear	183.1	144.1	110.9	91.7	75.4
26 Textile fibers and their wastes	49.2	57.7	63.5	75.8	74.4
68 Nonferrous metals	69.5	81.9	98.4	106.8	73.6
09 Miscellaneous edible products and preparations	36.1	31.9	40.9	39.2	51.4
64 Paper, paperboard, and articles of paper pulp	44.5	41.4	43.4	44.9	41.0
29 Crude animal and vegetable materials, n.e.s	53.2	44.8	43.9	53.2	38.8
05 Vegetables and fruit	25.1	27.8	33.4	41.1	35.6
55 Essential oils and resinoids and perfume materials	22.3	23.3	25.4	31.9	35.4
52 Inorganic chemicals	16.0	16.2	18.7	19.8	28.6
61 Leather, leather manufactures, n.e.s.	30.8	24.5	26.3	26.8	23.6
Other	111.2	114.8	107.6	104.7	95.0
Total	32,474.3	32,984.8	35,057.0	40,383.7	33,261.7

Source: Compiled from official statistics of the U.S. Department of Commerce.

F

Table 3-6
U.S. direct investment in Taiwan, 2000 (million dollars)

Sector	Net capital outflows to Taiwan	U.S. investment position in Taiwan
Manufacturing, total	567	3,692
Electronic and other electric equipment	303	1,454
Chemicals and allied products	74	1,483
Primary and fabricated metals	15	60
Food and kindred products	11	59
Industrial machinery and equipment	-5	188
Transportation equipment	(2)	65
Other manufacturing	(2)	381
Wholesale trade	242	871
Finance, insurance, real estate	207	1,972
Other industries	107	285
Services	49	154
Depository institutions	-26	703
Petroleum	(1)	60
All industries	1,147	7,737

[1] Less than $500,000 (+/-).
[2] Suppressed to avoid disclosure of individual company data.
Source: U.S. Department of Commerce, Bureau of Economic Analysis, found at Internet address *http://www.bea.doc.gov*, retrieved Apr. 22, 2002.

Table 3-7
Taiwan direct investment in the United States, 2000 (million dollars)

Sector	Net capital outflows to the United States	Taiwan investment position in the United States
Manufacturing, total	11	1,179
Chemicals and allied products	-20	782
Primary and fabricated metals	(1)	(1)
Food and kindred products	-1	-1
Machinery	30	342
Other manufacturing	2	56
Wholesale trade	85	722
Retail trade	(1)	21
Depository institutions	9	878
Finance, except depository institutions	6	65
Insurance	(2)	(2)
Real Estate	2	56
Other industries	(2)	(2)
Services	90	240
Petroleum	(1)	-4
All industries	186	3,224

[1] Less than $500,000 (+/-).
[2] Suppressed to avoid disclosure of individual company data.
Source: U.S. Department of Commerce, Bureau of Economic Analysis, found at Internet address *http://www.bea.doc.gov*, retrieved Apr. 22, 2002.

Taken from USITC Pub. 3548, Oct. 2002

G

FTA PARTNERS AND POTENTIAL PARTNERS TRADE WITH THE UNITED STATES FOR 2002

PARTNER COUNTRY	TOTAL	IMPORTS FROM US 2002 (DOLLARS)	EXPORTS TO US 2002 (DOLLARS)
Canada	*370,010,204,391*	*209,087,563,492*	*160,922,640,899*
Mexico	*232,086,088,316*	*134,615,816,831*	*97,470,271,485*
Taiwan	**50,529,709,040**	**32,147,880,509**	**18,381,828,531**
Singapore	31,020,101,503	14,802,181,035	16,217,920,468
Central America Total	20,793,222,532	11,259,482,954	9,533,739,578
Costa Rica	6,258,268,150	3,141,789,973	3,116,478,177
Honduras	5,832,419,992	3,261,342,816	2,571,077,176
Guatemala	4,840,797,615	2,796,365,594	2,044,432,021
El Salvador	3,646,402,223	1,982,316,579	1,664,085,644
Belize	215,334,552	77,667,992	137,666,560
Thailand	19,653,081,876	14,792,895,726	4,860,186,150
Australia	19,563,765,876	6,478,771,903	13,084,993,973
Israel	*19,442,319,012*	*12,415,663,377*	*7,026,655,635*
South Africa	6,559,647,599	4,034,106,407	2,525,541,192
Chile	6,393,483,876	3,784,495,696	2,608,988,180
Morocco	957,842,277	392,412,616	565,429,661
Jordan	*816,771,852*	*412,334,063*	*404,437,789*
Current FTAs			
Source: US Bureau of the Census: Foreign Trade Division © **USA Trade Online**.			

8/13/2003