

THE UNIVERSITY OF HULL

**EXTERNAL INCENTIVES, INDUSTRIAL DEVELOPMENT AND
REGIONAL ECONOMIC INTEGRATION**

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REGIONAL ECONOMIC INTEGRATION**

The revival of regional integration in the European Community (EC) in the early 1980s has brought about profound implications for the development of regional integration and its related theory. Firstly, European industry searching to promote its competitiveness highlighted the need for a "European-level" solution to European economic decline and contributions to the relaunching of European integration. Secondly, as a result of the renewed momentum for regional integration, external factors which were neglected by previous efforts in theory-exploration, have become more noticeable in the process of regional integration.

The purpose of this thesis about external factors is to analyse to what extent the progress of regional integration is driven by the private sector. The relaunching of European integration which brought about the successful passage of the Single European Act has demonstrated the crucial contribution of the business community to accelerating the progress of integration.

This thesis further offers an analysis of the proposition that the impact of external factors on industrial development is the key to understanding the process of creating the Chinese Economic Area (CEA). It explores the argument that instead of being motivated by political factors, the process of regional integration is primarily stimulated by industrial development in the private sector. It concludes by suggesting a new focus for the study of regional integration - the "external incentives-industrial development" approach, and comparative insights into the EC and the CEA.

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LIST OF ABBREVIATIONS

ADB	Asian Development Bank
ADCS	Advanced Developed Countries
AFTA	Asian Free Trade Area
ANICS	Asian Newly Industrialised Countries
APEC	Asia Pacific Economic Cooperation
ARATS	Association for Relations Across the Taiwan Straits
ASEAN	Association of South East Asian Nations
CAP	Common Agricultural Policy
CBI	Confederation of British Industry
CEA	Chinese Economic Area
CEO	Chief Executive Officer
CNFI	Chinese National Federation of Industries
CPCIT	China Promotion Council for International Trade
CSCE	Conference on Security and Cooperation in Europe
DPP	Democratic Progressive Party
EAEC	East Asia Economic Caucus
EC	European Community
ECSC	European Coal and Steel Community
ECU	European Currency Unit
EDC	European Defence Community
EEA	European Economic Area
EEC	European Economic Community
EEIG	European Economic Interest Groups
EFTA	European Free Trade Association
EMS	European Monetary System
EMU	European Monetary Union
EP	European Parliament
EPU	European Payments Union
ERT	European Roundtable
ESPRIT	European Strategic Programme for Research and Development in Information Technology
EU	European Union
EURATOM	European Atomic Energy Community
GATT	General Agreement on Tariffs and Trade
GCCHK	General Chamber of Commerce of Hong Kong
GDP	Gross Domestic Product
GERD	Gross Domestic Expenditure on R & D
GNP	Gross National Product
GSP	General System of Preferences
IGOS	Inter-governmental Organisations
IMF	International Monetary Fund

KMT	Kuomintang
LDCs	Less Developed Countries
MFN	Most Favoured Nation
MITI	Ministry of International Trade and Industry
NAFTA	North American Free Trade Area
NATO	North Atlantic Treaty Organisation
NGOs	Non-governmental Organisations
NICs	Newly Industrialised Countries
OECD	Organisation for Economic Cooperation and Development
OEEC	Organisation for European Economic Cooperation
OPEC	Organisation of Petroleum Exporting Countries
PAFTAD	Pacific Association for Trade and Development
PBEC	Pacific Basin Economic Cooperation
PECC	Pacific Economic Cooperation Council
PRC	People's Republic of China (Beijing)
PWC	Preliminary Working Committee
R & D	Research and Development
ROC	Republic of China (Taipei)
SEA	Single European Act
SEF	Strait Exchange Foundation
TNCS	Transnational Corporations
UN	United Nations
UNICE	Union of Industrial and Employers' Confederation of Europe
VCR	Video-Cassette Recorder
VER	Voluntary Export Restraint

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CHAPTER ONE

INTRODUCTION

1.1. DEFINITION AND CRITIQUES: THEORIES OF REGIONAL INTEGRATION

1.1.1. Integration Theory: The Emphasis on The Internal Processes of Integration

Integration, according to Karl Deutsch, is "the attainment, within a territory, of a 'sense of community' and of institutions and practices strong enough and widespread enough to assure, for a 'long' time, dependable expectations of 'peaceful change' among its population."¹ This definition implies that peaceful change or reorientation of attitudes will be spontaneously reflected when psychological sense and physical transactions are heading toward a satisfactory point. Ernst Haas has defined integration as "the tendency toward the voluntary creation of larger political units, each of which self-consciously eschews the use of force in the relations between the participating units and groups."² Furthermore, he believes that integration is a process of political actors' shifting their loyalties, expectations and political activities toward a new centre.³ Again, he refers the further cooperation among states to the voluntary motives which would be based upon peoples' self-consciousness, both elites and masses, rather than upon external compulsion.

1. Michael Hodges, "Integration Theory", in Trevor Taylor, (ed.), *Approaches and Theory in International Relations*, (London: Longman, 1987), p. 237.

2. Ibid.

3. James Dougherty, and Robert L. Pfaltzgraff, Jr., *Contending Theories of International Relations - A Comparative Survey*, 2nd edition, (New York: Harper & Row, Publishers, 1981), p. 421.

Charles Pentland shares Haas's perspective on integration. However, he focuses more on the abolition, circumvention, and reduction of the sovereign power of modern nation-states as the main process of integration.⁴ Moreover, according to Donald Puchala's creative argument of integration, integration is also seen as a set of processes that produces and sustains a "Concordance System". Within this system, interests are thought to be harmonised, differences are supposed to be compromised among actors, and mutual rewards are reaped from their interactions.⁵ The process of integration is leading states concerned towards a new centre of transnational institutions. Therefore, Johan K. De Vree points out that integration is conceptualisation of a political process between two or more states. Integration is then confirmed by James Caporaso and Alan Pelowski as the development of new structures and functions at a new system level which is seen as more comprehensive than previously.⁶ Among those distinguished definitions of integration, Leon Lindberg's is a particularly comprehensive and orderly one. He defines integration as follows:

"1) the process of nations forgoing the desire and abilities to conduct policies and seeking to make joint decisions or to delegate the decision-making process to new central organs;

2) the process of political actors being persuaded to shift their expectations and political activities to a new centre; and

⁴. C. Pentland, *International Theory and European Integration*, (London: Faber & Faber Limited, 1973), p. 29.

⁵. Donald Puchala, "Of Blind Men, Elephants and International Integration", *Journal of Common Market Studies*, 10: 3, (1973), p. 277.

⁶. Dougherty, and Pfaltzgraff, Jr., *Contending Theories of International Relations - A Comparative Survey*, p. 422.

3) the process of the evolution of a collective decision-making system among nations."⁷

Like other international theories, integration theory based on the assumptions above is also controversial, and even confused by various interpretations. Although many research works, such as Karl Deutsch's and Ernst Haas's, have made substantial contributions towards a theory, there is as yet little agreement on an individual independent variable of integration. This is the reason why while some tend to highlight the process of integration, others emphasise the condition of integration. In spite of this enduring argument, the idea of regional integration has been more practically seen as "a means of promoting peaceful cooperation and reducing conflict between states in various parts of the world."⁸ Furthermore, regional integration to some extent can be seen as a way of facilitating mutual interest among member states by collectively strengthening and promoting industrial competitiveness and international bargaining power in their external relations, e.g. the European Community (EC) on behalf of its member states in negotiating bilateral trade arrangements and the global trade talks under the General Agreement on Tariff and Trade (GATT). In addition, regional integration provides collective mechanisms for regional economies to sort out their differences and so to benefit from their strength, i.e. customs, monetary and, to a less extent, political unions, as well as regional development funds.

According to the traditional federalist approach to regional integration, the goal of the integration process is to form a supranational state which is based upon a

⁷. Leon Lindberg, *The Political Dynamics of European Economic Integration*, (Stanford: Stanford University Press, 1963), p. 6.

⁸. Hodges, "Integration theory", p. 238.

constitution, or a national contract, agreed by member states of a regional union. The most important point here is that federalists "are concerned to direct the integrative process toward a definite, well-articulated ideal - a supranational state with specific characteristics."⁹ Since for the federalists the end-product of the process of integration is a "political community", they stress political solutions which therefore should be directed by decision-making powers. Jean Monnet, one of the founders of the idea of the united Europe,¹⁰ shared the federalists' objective of a united Western Europe.¹¹ He believed that instead of handing authority over specific functional areas to separate international agencies, individual states would have to support a single regional executive, which would gradually come to take on the character of a federal European government.¹²

Unlike the federalists, David Mitrany, the pioneer of functionalism, did not regard regional unification as a means to prevent war. On the contrary, he advocated the creation of a whole series of separate international functional agencies,¹³ which he thought would lead to the formation of less tightly knit communities (or at least something like a pluralistic community of states),¹⁴ each of them having authority over one

⁹. Ibid., p. 148. The traditional federalist argument is out of date. John Pinder refurbishes as a neo-federalism. See Pinder, "European Community and nation-state: a case for a neo-federalism", *International Affairs*, 62: 1, (Winter 1985/6), 41-54.

¹⁰. Unless otherwise suggested, "Europe" and "European" are used synonymously with Western Europe and the people in this area, particularly the European Community and the European Free Trade Association's member states throughout the thesis. On no account "Europe" does refer to Eastern Europe.

¹¹. The federal institutional arrangement for the United States of Europe See Jean Monnet, *Mémoires*, (Paris: Librairie Arthème Fayard, 1976), pp. 334 and 468.

¹². Ibid., Chapter 16.

¹³. Mitrany in 1948 emphasised that: "the true choice is not between the present competitive nationalisms and a lame international federation, but between a full-fledged and comprehensive world government and equally full-fledged but specific and separate functional agencies." See Mitrany, "The functional approach to world organisation", *International Affairs*, 24: 3, (July 1948), p. 360.

¹⁴. Charles Pentland, "Functionalism and theories of international political integration", in A. J. R. Groom, and Paul Taylor, (eds.), *Functionalism: Theory and Practice in International Relations*, (London: University of London Press Ltd., 1975), p. 15.

specific area of human life and exempt from control by a single government. Since the growing complexity of international systems had increased the essentially technical, nonpolitical transactions among states, such activities not only created a demand for technical specialists at the national level, but also raised technical problems at the international level. To solve those problems, Mitrany suggested one should rely on collaboration among technicians rather than politicians.¹⁵ His proposition was to encourage governments to hand over the affairs of "low" politics, including economics and welfare, to those transnational functional agencies for the benefit of the world community.¹⁶ The functionalist design was to avoid entanglement with sensitive "high" politics in order to reduce potential obstacles to cooperation. In fact, the core of Mitrany's theory is a doctrine of "ramification" according to which the progression of collaboration in one technical field will lead to collaboration in other fields.¹⁷ As a result, functional activities could re-orient the nature of international transactions by diffusing national loyalties and redirecting the framework of international cooperation. Accordingly, the main features of functionalism contain functional interdependence, sector approaches, non-governmental transactional actors.¹⁸ Although the functionalists did not directly refer to their ultimate goal as transnational political institutions, the implication of the spillover effect (which successful cooperation in one dimension

¹⁵. David Mitrany, *A Working Peace System*, (Chicago: Quadrangle, 1966), pp. 72-73.

¹⁶. See David Mitrany, "A War-time Submission (1941)", *The Functional Theory of Politics*, (London: Martin Robertson, 1975), p. 116.

¹⁷. As Mitrany said: it "might in time provide a solid foundation for political union." See *Ibid.*, p. 121.

¹⁸. Puchala, "Of Blind Men, Elephants and International Integration", p. 278.

encroaches into other sectors) has led them to the internal process of integration.

Instead of emphasising the possible outcomes of deduction, the students of neofunctionalism, such as Ernst Haas, Philippe Schmitter, Leon Lindberg, Joseph Nye and Robert Keohane, focused upon practical developments within the EC to explore integration theory. In response to the progress of the EC, Haas assumes that integration proceeds as a result of the behaviour and expectations of relevant elites in the governmental and private sectors. Therefore, integration has been involved in decision-making processes and power, which refers to politicised neofunctionalism. Schmitter raises three hypotheses as neofunctionalist characters: spillover; externalization which assumes member states "will find themselves compelled to adopt common policies vis-a-vis nonmember third parties";¹⁹ and politicisation. In the general neofunctionalist's view, integration has a cumulative tendency which will "involve more national actors in an expanding variety of policy areas and in an increasing degree of joint decision making."²⁰

Using both communications and system theory, Deutsch is concerned with the relationship between communication and the integration of political communities. He believes that "the building of political units depends upon the flow of communications within the unit as well as between the unit and the outside world."²¹ According to this perception, communication flows gradually develop certain inward- and outward-looking transaction frameworks. As the transaction goes through those communication channels, interdependence

¹⁹. Philips Schmitter, "Three Neo-functional Hypotheses about international integration", *International Organisation*, 23: 1, (1969), p. 165.

²⁰. *Ibid.*, p. 166.

²¹. Dougherty, and Pfaltzgraff, Jr., *Contending Theories of International Relations*, p. 424.

among them is therefore accelerated. Deutsch and his associates set forth two sub-types of security-community: *amalgamated*, in which those independent political units have become a single unit with a decision making centre, i.e. federal type; and *pluralistic*, in which separate governments retain their legal independence, i.e. confederations and conventional international organisations at the regional level.²² Because Deutsch tends to consider the political unit as a whole in the process of integration, vertical and horizontal communications of societal elites become an important factor. Furthermore, in structure, as the integration process carries on, there seems to be a hierarchy among political units, central and peripheral areas. Deutsch concludes that "successful integration is attained when the subjective criterion of certain elite expectations is met: if the expectations of key elites in the region converge toward demands for peaceful change and other benefits thought to be obtainable only through the union, integration is underway."²³ Basically, pluralism starts from increasing communication flows and builds up the networks of interdependence which would intertwine those political units together. While the interaction networks have already been established, their interests would be deeply connected to each other. A regional consensus would emerge, which is Deutsch's "integration threshold". In sum, what these theoretical approaches are commonly suggesting is that the task of achieving regional integration rests upon transitional processes within a certain community, while growing common interests may serve as a driving force.

²². Ibid., p. 524; also Ernst Haas, "Challenge of Regionalism", in Stanley Hoffmann, (ed.), *Contemporary Theories of International Relations*, (Englewood Cliffs: Prentice-Hall, 1960), p. 224.

²³. Haas, *ibid.*

1.1.2. The Neglect of the External Dimension by Theories of Regional Integration

According to theories of integration, the process of regional integration involves all sorts of complicated economic and political interactions between the likely member states, which has drawn their attention to the internal process of integration. In the theory-building process, much attention was paid to internal factors of a regional system because theorists were inclined to examine the basic assumptions made by two pioneer study groups. First, the communication theories of Karl Deutsch and others argue that the connection of peripheries to the core of a region lead to transaction flows among regional actors. Regional integration then appears to be a constant transaction under certain networks. Secondly, Haas's work focuses on intersocietal political processes among pressure groups, political parties, elites,²⁴ which results in a number of research projects concentrating on European Community institutions and their concerns.

In practice, it is apparent that unless an integrating union is completely closed to or isolated from international society, the process of integration and the interactions between states involved is bound to be considered not as "without" but "within" the international political and economic system. Although the development of the EC has been driven by different external incentives since it was created, integration theory has paid little attention to them. In the

²⁴. For the detail see Karl Kaiser, "The Interaction of Regional Subsystems - Some preliminary Notes on Recurrent Patterns and the Role of Superpower", *World Politics*, 21: 1, (Oct. 1968), p. 87.

past few decades the theorists of integration have almost exclusively concentrated on the basis of *processes* and *internal factors* to explain and generalise, as well as predict regional integration, e.g. the federalists' formation of super-statism, the functionalists' process of the functional spill-over, and the neofunctionalists' approaching politicisation. They cared much more about the development inside of a regional integration system (the EC) than about the interaction between the system and outside systems. Their focus on processes and internal factors has conceivably gained some prominent successes both in theory-building and the analysis of regional cooperation.

However, this "internal" orientation has been criticised by some scholars as intentionally separating regional integration from political reality.²⁵ The bias towards "internal" studies and the absence of external factors may, to some extent, have to shoulder a responsibility for the failure to form a more complete theory. Integration theory was unable to explain the disruptions to the integration process between high politics and low politics, unable to deal with the setbacks in national economies to European integration in the 1970s,²⁶ and incapable of displaying the reasons for the relaunching of European integration in the 1980s, as well as too distant from understanding the emergence of subregional groupings in the Asia-Pacific region.²⁷ Studying Caribbean

²⁵. Such as Kaiser, "The Interaction of Regional Subsystems"; Joseph Nye, "Patterns and Catalysts in Regional Integration" *International Organisation*, 19, (Autumn 1965); also James Caporaso, "The European Community in the world system : Prolegomena to a political economy of the European Community" *Journal of European Integration*, 2: 3, (May 1979).

²⁶. About the Gaullist disruption to the integration process and the critique about the applicability of the theory see Pinder, "European Community and nation-state: a case for a neo-federalism", pp. 50-54.

²⁷. Economic cooperation in the Asia Pacific region refers mainly to cooperations between subregions of East Asia and Southeast Asia, which more narrowly include economic groupings amongst China, Japan, South Korea, Taiwan, Hong Kong, ASEAN countries and countries Indo-China.

integration, one scholar succinctly pointed out "what the political theory of integration has failed to do is to account for the factors outside the region that have influenced the process of regional co-operation."²⁸ Especially, as a part of international study, regional integration should also be considered in the context of the international environments concerned. This implies that the interaction between a regional integration system and the outside world is as important as the internal process. Examples are the impact of international trade talks (global system) under the General Agreement on Tariffs and Trade (GATT) on the Asia-Pacific regional economic groupings, and the United States and the former Soviet Union (external powers), imposing positive and negative influences respectively on European integration; and the British influence (colonial links) in the Caribbean Community and Common Market (CARICOM) and East African Community (EAC).²⁹

There has been, then, a neglect of theories of regional integration in terms of external factors. For example, Puchala criticises functionalism more straightforwardly. First, few developments in contemporary international integration have progressed in the way that the functionalists proposed. Since national governments remain the key players and pivotal in integration systems, it seems that in the near future people see no sign of their releasing control on most of the functional task areas. Secondly, "there are simply no non-political issues in relations among states."³⁰ Thirdly, "the functionalist model misses the essence of the growth and

²⁸. W. Andrew Axline, "Regional Co-operation and National Security: External Forces in Caribbean Integration", *Journal of Common Market Studies*, 27: 1, (September 1988), p. 1.

²⁹. For the British influence see Thomas S. Cox, "Northern Actors in a South-South Setting: External Aid and East African integration", *Journal of Common Market Studies*, 21: 3, (March 1983), pp. 283-312.

³⁰. Puchala, "Of Blind Men, Elephants and International Integration", p. 274.

expansion of international regimes during international integration."³¹ Moreover, the functionalists have not explained very clearly how people may achieve international cooperation by circumventing politics among states. Finally, they have failed to demonstrate how international cooperation is in fact to be achieved during the process of international integration. Puchala complains that the functionalist does not deal with the reality. Haas criticises Mitrany for having taken insufficient account of the power element, and postulates that power is not separate from welfare. Power, then, is defined as a means to assure the realisation of welfare aims. In practice, the evolution of European integration meant that the EC's institutions generated certain political authority and jurisdiction over its member states and citizens to ensure that the policies were in accordance with the Community's interests and were being effectively implemented.

Stuart Holland in 1980 criticised the economic focus of neofunctionalism. First of all, there is a misidentification of the nature of the economic interests involved. Holland's critique is based upon a four-fold classification of capitalist businesses, i.e. large-scale multinational corporations, large-scale national enterprises, small-scale multinational corporations, and small-scale national enterprises.³² His main argument is that the EC's member states † have been entangled with complicated individual economic interests. Therefore, different governments will face different combinations of pressures. Secondly, he criticises the neofunctionalist's economic theory which is based on the assumption that economic growth would continue unabated in the

³¹. Ibid.

³². Stuart Holland, *Uncommon Market*, (London: Macmillan, 1980), pp. 109-110.

capitalist economies; and finally that all the EC member states would benefit from that growth in the long run.³³ However, this assumption is not totally correct. The two oil crises in 1974 and 1979 abruptly ended the duration of economic boom which the capitalist economies had enjoyed since the 1950s, and the EC has suffered from low growth rates and high rates of unemployment. Holland prefers to restore the idea of capitalist economics as a cyclical process. Therefore, he admits that the focus of regional integration would have to rest upon the wider international dimension.

After Haas publicly announced in 1976 that the proposition of regional integration was obsolescent, it seemed to mark an end to the efforts to explore integration theory. In practice, by that time neofunctionalists had been suffering from their miscalculation of the internal political diversity of the EC in the 1960s which had led to the Gaullist opposition halting the European integration movement. In addition, neofunctionalists could hardly come to terms with the aftermath of the economic turbulence of the stormy 1970s during which economic cyclical recession and the first oil crisis together drove the EC's member states to seek national solutions to their economic problems. It is therefore important to stress that traditional explorations of integration theory which have emphasised internal processes of integration are out of touch with the reality of the interdependence inherent in the international economy. It also implies that the motives for European integration have been built upon a combination of ~~from~~ internal and external + incentives in various periods. Accordingly, it is necessary to

³³. The criticism was based on economic theory see Ibid., p. 49-85.

identify and to highlight the impact of external incentives on the process of regional integration.

1.2. EXTERNAL INCENTIVES AND REGIONAL INTEGRATION

During the 1950s and 1960s, the progress of West European integration dramatically marched forward, because of general political pledges of national cooperation in the arrangement of the post-War European political structure and because of steady European economic growth. Although political motives and the thought of European security contributed to the then optimism of encouraging further European integration, European economies in the context of sustained economic growth were more inclined to act on the arrangement for political and economic integration. As a result, the integration patterns of a customs union and common market were brought about in the wider framework of the Treaty of Rome in 1957 in the hope that member states would benefit from the development of scale economies within the Community. Throughout the history of European integration, economic development and national commitment have become twin variables for the progress of European integration. As a result of prolonged recession and the two oil crises, economic development and industrial interests have then emerged topping the national and the European agenda. These brought about the impetus for political and economic integration in Western Europe.

Ernst Haas wrote in 1976 that the increasing interdependence between European countries and the rest of the world had caused European integration to ebb. He conceded that integration theory had failed because of its neglect of

external factors which influenced the process of integration.³⁴ Many scholars, such as Robert Keohane, Stanley Hoffmann, A. Moravcsik, and W. Sandholtz and J. Zysman, also confirmed that in the 1970s and 1980s an international political and economic structural shift, as an external factor, was a necessary condition for European integration to begin moving again.³⁵ The impact of economic turbulence in the 1970s on the development of regional integration has therefore changed the theorisation of integration. Those who had previously emphasised internal political processes in integration have been challenged by the rise of international economic interdependence, which has brought external influences to bear on the internal processes of regional integration in Western Europe and emphasised the importance of exogenous economic development in the process of economic integration.

If the short-term effect of the oil crises in the 1970s on regional integration in Europe was disintegration, its long-term impact on regional integration in the 1980s and after was actually to encourage economic integration. To a large extent, industrial factors became both a necessary and a sufficient condition for the renewal of European integration in the early 1980s. Industrial prosperity and growth were basic conditions for economic and social integration within the Community. In the 1950s and 1960s, apart from political motives, the progress of European integration was encouraged by buoyant economic growth that resulted from good industrial performance. When European industry became less capable of

³⁴. See Haas, *The Obsolescence of Regional Integration Theory*, (Berkeley: Institute of International Studies, The University of California, 1976).

³⁵. See Keohane and Hoffmann, "Institutional change in Europe in the 1980s", in their co-eds., *The New European Community: Decision Making and Institutional Change*, (Boulder: Westview, 1991), 1-40; Moravcsik, "Negotiating the Single European Act: National Interests and Conventional Statecraft in the European Community", *International Organisations*, 45: 1, (1991), 651-688; Sandholtz and Zysman, "1992: Recasting the European bargain", *World Politics*, 42, (October 1989).

competing in global markets in the mid-1970s as a result of its ageing industrial structure crippled by recession, economic slowdown brought European integration to a halt. Therefore, industrial restructuring processes would ideally revive not only the European economy as a whole but also regional economic integration. In that particular circumstance, along with politicians, European industrialists took the lead in campaigning for industrial integration grounded on the advantages of all-out integration that in effect have triggered the progress of economic as well as political integration in the EC. If transnational business groups were to be the most sensitive and vulnerable actors in facing international structural change, then they would be the most dynamic propulsive forces in pushing integration forwards. Therefore, the influence of external factors on regional integration and the role of economic development in the process of economic integration have become the features of present regional integration in the EC and elsewhere. These emphases could help to reshape the theory of regional integration and our understanding of the role played by external factors in recent developments in integration in both the European Community and the Chinese Economic Area.

1.2.1. External Incentives on the Periphery of the Theory of Regional Integration

Since the late 1960s, the contribution of external factors to regional integration has gradually come to be noticed by students of regional integration as part of a theoretical reappraisal driven by the setbacks incurred by previous attempts at theorising regional integration. The

emphasis of these discussions on external factors has helped to demonstrate the reality of regional integration in Europe and elsewhere. However, external incentives have been noticed by only a few students and therefore have remained marginal to main stream integration theory. For instance, Karl Kaiser's initial attempt in 1968 to examine the external factors in the evolution of regional systems was largely derived from the apparent disregard of these factors, e.g. alliance relations and superpower politics, by the theory.³⁶ Kaiser further describes this inadequate theoretical dimension as follows:

"We now know to some extent how in the process of integration, societies, pressure groups, parties, and governments interact across national frontiers *within* the region, but not how they interact with the *outside* world."³⁷

In spite of theorists' general lack of interest in understanding the contribution of external incentives to integration, external factors motivating the evolution of regional integration have never been entirely dismissed from the literature, particularly with reference to the impact of the United States and the Soviet threat on the birth of European integration. Criticising integration theory, Ernst Haas in 1971, Donald Puchala in 1973, and Stanley Hoffmann in 1966, though taking different perspectives, similarly noticed the importance of the influence of the international political and economic environment on the processes of regional integration. According to Kaiser in 1968, Amitai Etzioni's *Political Unification* may be the only example in integration theory which attempts to handle systematically and to

³⁶. Kaiser, "The Interaction of Regional Subsystems", pp. 85-86.

³⁷. Ibid, p. 88.

generalise properly about external factors by developing a framework for the preconditions, accompanying conditions, stages and termination of the unification process.³⁸ Unlike others, Kaiser considers the environment in the "pre-unification state" in the form of "a common enemy".³⁹ This external element concerned with security threats is regarded as an original motive, or more likely a catalyst, to unification. In this way, Etzioni emphasises the interactions between the union-forming system and the external security threat.

In a similar context, Etzioni refers to the role of "external elites" in the evolution of integration, such as the United States' role in European integration. According to Etzioni, there is an internalisation of external elites during the process of integration. Internalisation implies the process "in which control of a system is taken over by member-elites from external elite-units".⁴⁰ In practice, in the context of the establishment of the EC, the Community's elites had been gradually internalising certain functions with respect to economic, military, and foreign policy through taking control of these areas previously performed by the United States. For example, to manage the aid of the Marshall Plan and to replace the many bilateral payments to the United States into a multilateral system of payment, the European Payments Union (EPU) which was established in 1950 under the Organisation for European Economic Cooperation (OEEC) set up a

³⁸. Ibid.

³⁹. Although in Kaiser's analysis of Etzioni's paradigm the relationship between external military threat and integration has been questioned, whether the threat helps integration or not, it undoubtedly facilitated the processes of unification at the beginning of regional integration. For this detail see Karl Deutsch and others, *Political Community in the North Atlantic Area*, (Princeton University Press, 1957); Kaiser, "The US and the EEC in the Atlantic System - The Problem of Theory", *Journal of Common Market Studies*, 5, (June 1967), pp. 396-397.

⁴⁰. Ibid, p. 398.

clearing mechanism for payments funded by the United States among the Union's members and thus generated an expansion of trade.⁴¹ In terms of economic policy, the establishment of the EPU represented Europeans' efforts to establish their own monetary competence. These efforts boosted a hope for economic integration, as a result.⁴²

But, together with this perception of internalisation of external elites, on the other hand, a regional integration system, such as the EC, is seen as permeated in many other ways by external factors. The overlapping development of the Western alliances has always accompanied the evolution of the European Community. To take the example of the EPU once more, the arrangements for the EPU, to some extent, did imply some discrimination in trade and payments against the United States, but the United States not only tolerated this discrimination but also devoted its intellectual and political support to the EPU.⁴³ In the military field, although West European countries most of the time shared the United States' strategy against the former Soviet Union, the British and French decision, as a result of processing internalisation, to build up their own national nuclear deterrents was not in accordance with the US' multilateral schemes for nuclear defence.⁴⁴ However, Etzioni's perception of internalisation is but a part of the external relations of the integration process. In fact, as Kaiser has argued, the perception cannot help us explain the restraints on interdependence. It is

⁴¹. For the development of the EPU and its importance see Daniel Gros and Neils Thygesen, *European Monetary Integration: From the European Monetary System to European Monetary Union*, (London: Longman, 1992), pp. 4-9.

⁴². Indeed, many officials within the US government were keen to advocate economic integration and customs unions in Europe as a means to economic efficiency and growth. See Alan S. Milward, *The Reconstruction of Western Europe 1945-51*, (London: Methuen, 1984), p. 56.

⁴³. Gros and Thygesen, *European Monetary Integration: From the European Monetary System to European Monetary Union*, p. 6.

⁴⁴. Kaiser, "The US and the EEC in the Atlantic System", p. 398.

because the countries engaging in the process of integration have been firmly intertwined into complex communication networks and have changed the way that nation-states act in the realist world.⁴⁵

Stanley Hoffmann criticises the theory of integration for its absence of "an explicit treatment of the role of superpowers, defence policy, matters of prestige, and tensions extending beyond the area of integrating states."⁴⁶ Since his framework covers the relations between Europe and the United States in the context of international systems, he argues that "one must examine more than the relation of each unit (in a community) to the international system"⁴⁷ and we should therefore distinguish two types of inter-state behaviour: states which are engaged in the process of integration towards political community, and states that do not participate in this collective action. The former type was brought into the interactions within integrating groups evolving the formation of supranational institutions, negotiations for common interests, the transformation of national loyalty. On the other hand, the latter would be treated "in the realm of traditional strategic-diplomatic inter-state behaviour" by the former states.⁴⁸

There were some scholars working on non-European bases of integration, whose realisation of the role of outside forces had urged the need for adopting external elements in integration theory. Joseph Nye reviewing the Haas-Schmitter's pattern of nine variables to regional integration in less

⁴⁵. Ibid., p. 400.

⁴⁶. See Kaiser, "The Interaction of Regional Subsystems", p. 89; also Hoffmann, "Obstinate or Obsolete? The fate of the Nation-State and the Case of Western Europe", *Daedalus*, (Summer 1966), pp. 862-915.

⁴⁷. See Hoffmann, "Obstinate or Obsolete", p. 905.

⁴⁸. Kaiser, "The US and the EEC in the Atlantic System", p. 401.

developed areas, Africa and Latin America,⁴⁹ proposes that there is a need for the concept of a "catalyst" to supplement the insufficiencies of theories which single out internal variables to explain integration. According to Nye, "the concept of a 'catalyst' is consciously a *deus ex machina*. It is an attempt to focus attention on the role of relatively accidental and more historically unique factors in regional integration."⁵⁰ He further suggests that the study of integration should refer to the external environment of world politics in which an integration process takes place.⁵¹

In contrast to Nye, Roger Hansen argues that the Haas-Schmitter's model suffers from a serious theoretical inadequacy in its dealing with less developed areas' integration because of its neglect of those exogenous factors in the international environment that affect the integration process.⁵² Those arguments benefit Nye's explanation of "catalysts" which include the use of military force and economic aid to accelerate the cooperation among East African countries. The success of operating transnational institutions, especially in the field of economic aid, seems to depend upon the willingness of one dominant external power. Nye discovers, moreover, that the third countries, other international organisations, and nongovernmental actors, such as international corporations, can be involved in an

⁴⁹. The Haas-Schmitter's pattern was to quantify the levels of the politicisation of economic unions through nine variable which were assumed as background conditions: 1. the relative size of the states, 2. the rate of transactions, 3. the degree of pluralism, 4. the extent of elite complementarity, 5. the degree of congruence in the minds of the participating governments, 6. the powers of union; and process conditions: 7. the decision-making style of economic unions, 8. the rate of transaction, 9. adaptability of governments. See Haas, and P. Schmitter, "Economics and Differential Patterns of Political Integration: Projections About Unity in Latin America", *International Organisation*, 18: 4, (Autumn 1964), pp. 705-737.

⁵⁰. For Nye's definition of catalyst see his "Patterns and Catalysts in Regional Integration", p. 882.

⁵¹. *Ibid.*, p. 883.

⁵². Roger Hansen, "Regional Integration - Reflections on a decade of theoretical efforts", *World Politics*, 21: 2, (January 1969), pp. 249-250.

integration process, and should be considered as important determinants.⁵³ His view on catalysts to regional integration tends to be in favour of the positive role that a catalyst can play in advancing integration. Therefore, in revising the early Neo-functionalist model, he asserts that "involved external actors" which are as important as other original "process mechanisms" should be taken into account into the integration process.⁵⁴ Nye therefore suggests that a catalyst is more likely to be a supplement to the conditions established in the Haas-Schmitter's pattern.⁵⁵ In this respect, Nye establishes the study of external factors as a necessary part of regional integration.

Attempting to analyse the interaction between regional subsystems, Kaiser argues that in history American contributions to the success of European integration appear an absolutely indispensable factor which the theory does not reflect well.⁵⁶ The American elites had taken part in the process of European unification in the field of administration and the European establishments (Etzioni's argument). In addition, the United States had also provided military shelter, and economic aid and cooperation to Europe (Nye's argument about catalysts). All the efforts and supports of the United States for Western Europe had indeed created a favourable context for European integration. Kaiser hence tried to use a socio-political system of interacting units to analyse the interdependence between the EC and the rest of the world. He defined his conceptual framework as two relevant developing systems : the Atlantic system, and the EC as a

⁵³. Nye, "Comparing Common Markets - A Revised Neo-functionalist Model", in Leon Lindberg and Stuart Scheingold, (eds.), *Regional Integration - Theory and Research*. (Cambridge, Mass.,: Harvard University Press, 1971), p. 207.

⁵⁴. Ibid., pp. 207-223.

⁵⁵. Nye, "Patterns and Catalysts in Regional Integration", p. 883.

⁵⁶. Kaiser, "The Interaction of Regional Subsystems", p. 90.

subsystem within the larger framework of the Atlantic alliance.⁵⁷

Under this overlapping system, Kaiser expects that integration can progress if it is considered as a special case of system transformation. Whatever perspective is taken to define integration, like unification, community building, sector integration, and functional integration, it is really concerned with system transformation. Kaiser stresses that:

"Within Europe, integration aimed at a transformation of traditional relations among states and at the creation of new supranational units and decision-making centres, a goal which was actively supported by the United States. Within the Atlantic system as a whole, European unification was to change the existing distribution of influence and formal structure by shifting influence to, or creating, new centres of communication and decision-making in Europe."⁵⁸

He therefore refers those process of transformation in integration to structure, tasks performed in common, and transnational forces.⁵⁹ While those transformations will presumably lead to new styles of community, the existing relevant systems will also be undergoing structural transformation. For instance, no sooner was integration in the EC extended to establish new centres and networks of decision-making than the Atlantic system was forcing the EC to pursue common policies towards the US, e.g. in the fields of agriculture and general commerce.⁶⁰ This acceleration not only came from internal process of integration but also from external influences. As a condition of the Marshall Aid Plan, for example, the US insisted that European countries had to

⁵⁷. Kaiser, "The US and the EEC in the Atlantic System", p. 406.

⁵⁸. Ibid., p. 413.

⁵⁹. Ibid., pp. 410-412.

⁶⁰. Ibid., p. 419.

cooperate with each other and tried to organise themselves in order to make best use of their resources, which served as an external push to start the process of integration.⁶¹

Among Haas's contributions on integration during 1958, we can hardly find any discussion about external factors to integration. Although Haas himself did not focus on external factors whilst exploring the theory, he did acknowledge that they were quite important for theory-building. He once confessed that something was missing in his exploration of the integration process in Western Europe.⁶² But he did not see, as Hansen has pointed out, its theoretical inadequacy "as a product of its disregard for the interaction between exogenous and endogenous variables."⁶³ Doing quantitative research for regional integration in 1969, Haas and his colleague formally regarded external factors as an independent variable. In fact, three 'new' variables, dependence on the external world, the perception of dependence, and objective external pressure, were accrued to the previous Haas-Schmitter's model (nine variables).⁶⁴ The research emphasised, however, not the actual exercise of external pressure but rather the perception of dependence by the actors including threats from the external world and reliance on moral and physical aid.⁶⁵ Haas' research indicates that 'the perception of dependence' accounts for

⁶¹. Many Americans discussed the Marshall Plan as "thought it were some thing being done to Europe rather than with Europe." The then Germany's chief officer for the Marshall Aid, Karl Albrecht said: "(The Aid) encouraged us to intensify our efforts toward European cooperation." See Harry B. Price, *The Marshall Plan and Its Meaning*, (Ithaca, New York: Cornell University Press, 1955), pp. 292-295.

⁶². Hansen especially pointed out that Haas himself realised insufficiency of the theory. See Hansen, "Regional Integration - Reflections on a decade of theoretical efforts", p. 250. Based on Haas, "the 'Uniting of Europe' and the Uniting of Latin America", *Journal of Common Market Studies*, 5, (June 1967), p. 327.

⁶³. Ibid.

⁶⁴. The three variables were *dependence* on the background conditions, *external pressure* on conditions at time of union and on process conditions. See Mario Barrera and Ernst Haas, "The Operationalisation of Some Variables Related to Regional Integration: A Research Note", *International Organisation*, 23: 2, (1969), pp. 151-152.

⁶⁵. Ibid.

twenty per cent, 'external pressure' on conditions at time of union for twenty five per cent, and 'external pressure' on process conditions for ten per cent.⁶⁶ As far as the result is concerned, external factors seem to be more important on conditions at the time of union than during other integration periods. Moreover, the research suggests that the more a regional union relies on its big neighbour, such as the Central American Common Market (CACM) on the US, and the European Free Trade Association (EFTA) on the EC, the more the union suffers from external pressure. Haas explains that "high perception of dependence is thought to reinforce the desire for unity in order 'to get out from under'" and "to achieve a united common front against external force."⁶⁷

Haas has realised that the relations between regional system and external world "can be of immense importance in explaining integration."⁶⁸ He goes further to categorise various exogenous variables as three groups, namely, 'the global system', 'a single state', and 'a regional countersystem'. To begin with, while the subsystem perceives itself struggling or unequal within the existing global system, the perception appears to be a driving force for the members of the subsystem, above all the developing countries, to integration in order to be 'getting out from under'. Next, Haas defines 'a single state' as "the extraregional force which aids or hinders integration."⁶⁹ His concerns here reflect the previous discussion on Etzioni and others' external elites helping regional integration. Finally, because cooperation and conflict (or competition) exist between different integration

⁶⁶. For detail result of the indication see *Ibid.*, p. 153.

⁶⁷. *Ibid.*, p. 152.

⁶⁸. Haas, "The Study of Regional Integration : Reflections on the Joy and Anguish of Pretheorising", in Leon Lindberg, and Stuart Scheingold, (eds.), *Regional Integration - Theory and Research*, (Cambridge, Mass.: Harvard University Press, 1971), p. 16.

⁶⁹. *Ibid.*

unions, the impact of extra-regional counterunions is defined as "a definite aid to integration."⁷⁰

However, in the military field, regional union may exist only as long as the threat from its counter-union (integration elsewhere) remains, such as the North Atlantic Treaty Organisation (NATO) in relation to the Warsaw Pact Organisation and the Association of South-East Asian Nations (ASEAN: Indonesia, Thailand, Malaysia, Philippines, Singapore and Brunei) in relation to the Indo-China Federation (Vietnam, Cambodia and Laos).⁷¹ In the economic field, Haas realised that among industrialised countries economic union may survive because the countries seek a united front in coping with another union, like the EFTA in relation to the EC and the ongoing North American Free Trade Area (NAFTA) and the emerging regionalism in Asia-Pacific in relation to the 1992 programme of the EC. Haas's observation and exploration of regional integration has depended upon both international and European environments of that time. Since then, in response to oil crises, economic recession and industrial competition, Western Europe has been gearing up its integration momentum as a result of realising that external political and economic challenges would have to be taken on collectively. In effect, this realisation of the necessity of regional economic integration has become widely known, as the world is entering a new era of regionalism.⁷² Hansen has criticised Haas's

⁷⁰. Ibid., pp. 16-17.

⁷¹. According to a research in 1990, the reason why the NATO has not disappeared after the collapse of the Warsaw Pact is mainly because three reasons: the military might of the former Soviet Union, the necessity of the nuclear deterrence in a post-Cold War Europe, and maintaining American presence in Europe. See Barry Buzan, et al. *The European Security Order Recast: Scenarios for the Post-Cold War Era*, (London: Pinter Publishers, 1990), p. 226. Although ASEAN was not originally established for military purpose, since the late seventies it has been more or less integrated in collective defense understanding against regional potential threats, as the Vietnamese threat became obvious.

⁷². Lawrence Krause, "Trade Policy in the 1990s I: Goodbye Bipolarity, Hello Regions", *The World Today*, (May 1990).

recognition of integration and disintegration as two rival social processes as still "too isolated from external variables that may well help to account for the variety of outcomes observed."⁷³ Furthermore, he suggests that there are "certain 'compelling' international environmental pressures which may trigger and sustain integration efforts."⁷⁴ He favours the interaction between subsystems since he believes that "the minimum degree of interaction between system and regional subsystem may enhance the prospects for success."⁷⁵

Among these arguments on external factors to integration, there appears to be a gradual realisation of the importance of external factors to regional integration that was neglected in the earlier exploration of the theory. Most theoretical explorations appeared before the 1970s in the context of the traditional character of international relations, in which the idealist approach contested against the realist one in shaping international integration theory. In the 1960s and 1970s, most of the regions concerned with integration were just starting their integration process or, if not, just trying to negotiate with each other for the basic consensus of a union. Therefore, what the theorists have done, or could do, was to trace the background conditions, and to investigate the integration process simply by adopting a related case - European experience. In other words, these research contributions were actually the repercussions of their specific era, and were not sufficient to explain all the external variables that integrating unions would meet. For example, while in the Cold War era high politics had been the predominant concern of the national actors, the factors of sovereignty, prestige,

⁷³. Hansen, "Regional Integration - Reflections on a decade of theoretical efforts", p. 252.

⁷⁴. Ibid.

⁷⁵. Ibid.

security, and national interest were undoubtedly a lot more important than low politics.

Nevertheless, while low politics today has more international salience, international communications have already gone beyond national boundaries. As the world since the 1970s has plunged into global economic, social and environmental challenges, those important external incentives to integration are noticeably no longer able to be regulated by the old structure. How to improve the understanding of regional integration that has involved interactions between different integration unions is far beyond the knowledge of those original studies. In particular, there has been a relatively increasing importance of global, regional, environmental, economic, and social issues in the agenda of international politics, which clearly delivers the message that regional integration ought to have different implications for the world of the 1980s and after. In short, the old assumptions have been challenged, some are discredited and some are rendered invalid. Hence, in many respects the early theories are now outdated.

1.2.2. Redefining Regional Integration to Take Account of External Incentives

As the process of regional integration becomes living in an interdependent world politically and economically, so the later studies in regional integration have begun to acknowledge the significance of external factors. This is due to the efforts to study integration in developing countries where external influences are much more observable. In 1983, Thomas S. Cox, an ex-staff member of the United Nations

Development Programme, concisely sketched the relations between regional integration and external environment. He stated that:

"the overall external environment can affect integration through the formation of trade, investment and aid links between a given system and a third party or parties in the developed world. Integration schemes must also contend with the establishment of parallel links between individual members of the scheme and an outside actors or actors."⁷⁶

Cox's argument has not only emphasized the importance of external factors to regional integration, but also pinpointed that some non-political external factors, e.g. international trade, overseas investment, and foreign aid, have also played an important part in the process of integration. As far as the theoretical assumption is concerned, the argument referred to external factors has actually gone beyond the original frameworks of regional integration derived from Deutsch's "communities", which were concerned with transaction flows across national borders within an integration union.⁷⁷

W. Andrew Axline in criticising neofunctionalism points out that it was based on a particular conception of the relationship between economic growth and organisational change, which "never really went beyond the study of regional organisation as a unit of analysis."⁷⁸ He explains that it offered a rather limited generalisation of the economic integration of Western industrialised countries. It is true

⁷⁶. Cox, "Northern Actors in a South-South Setting: External Aid and East African integration", *Journal of Common Market Studies*, 21: 3, (March 1983), pp. 283-284.

⁷⁷. Deutsch's attention to transactions of countries was between people's communications, as countries were considered clusters of population. See discussion in James E. Dougherty, and Robert L. Pfaltzgraff, Jr. *Contending Theories of International Relations: A Comprehensive Survey*, p. 425.

⁷⁸. Axline, "South Pacific Region Cooperation in Comparative perspective: An Analytical Framework", *Political Science*, 36: 2, (December 1984), p. 40.

that in the new international setting, the neofunctionalist experience in Europe has been unable to predict the further development of the Single European Market itself and cannot explain the regional cooperation among the developing countries. It is because its success in Europe was still largely limited to economic cooperation which has not yet led to a political union of common foreign and security policies in the current system of the nation-state centre. Moreover, it lacks applicability to regional integration among developing countries in the conditions of economic underdevelopment, of fragile pluralistic democratic political systems, and, above all, of vulnerability to external influence.

In his study, Axline especially emphasises that the existing theory of economic integration "still does not take into account some of the most important external forces that influence regional cooperation, powerful states in the region and at the global level, which are not formally partners in regional cooperation, but which exert influence on it."⁷⁹ For most of the relatively weak or small countries, like those in the Caribbean and South Pacific, in terms of political influence, military capability, and economic underdevelopment, regional integration is very likely to be influenced by the outside world. For example, external factors involved in the process of regional cooperation, either pushing it ahead or holding it back, in the South Pacific region are from various sources, such as global powers, hemispheric powers, regional powers, and non-state actors.⁸⁰ The ANZUS countries (Australia, New Zealand, and the United States) in the 1970s and 1980s strongly supported South Pacific regional cooperation as an effective means of maintaining a favourable strategic posture

⁷⁹. Ibid, p. 43.

⁸⁰. See Axline, "South Pacific Region Cooperation in Comparative perspective", pp. 47-49.

over the increasing presence of the Soviet Union and China in the region.⁸¹

As a matter of fact, the integration process of the EC has also been influenced by various external factors. Although one might argue that the attempt to solve internal quarrels between member states and transitional problems of moving further integration has been the main part of the EC integration performance, which was the main concern in integration theory, this does not rule out external incentives as important driving forces for European integration. After all, regional integration takes place in the context of the international political and economic system. From here, the theoretical framework has shown itself incapable of keeping up with the development of European integration. To refurbish the theory, Axline proposes that widening the range of variables and allowing external factors to be included is the way to broaden theoretical perspectives and to meet the practical situations in developing countries.⁸² External factors, he suggests,

"are likely to be an important influence on the pattern of regional cooperation by directly affecting the costs and benefits of cooperation for the region as a whole, and the distribution of the perceived opportunity costs for each of the participants."⁸³

According to this definition, a number of external factors to Caribbean integration were brought out in his research: the run-up negotiations for the first Lome

⁸¹. Regional cooperation in South Pacific resulted partly from regional states' attempts to reshape and control the influence of metropolitan countries, and partly from the ANZUS countries' efforts to control other external involvements in the region. See Gregory E. Fry, "Regionalism and international politics of the South Pacific", *Pacific Affairs*, 54: 3, (Fall 1981), pp. 476-482.

⁸². Axline, "Regional Co-operation and National Security", p. 1.

⁸³. Axline, "South Pacific Region Cooperation in Comparative perspective", p. 45.

Convention (positive factor), United States opposition to policies that interfered with free market forces in Central American (negative factor), Canada's support of the Caribbean Development Bank and a regional trade agreement (positive), changes in the international economic structure (negative), and the dramatically soaring world oil prices following economic recession in the 1970s (negative).⁸⁴ Expanding the detail, Axline further establishes a structure of external influence by examining those external factors which influence "the costs and benefits of specific regional options, and the costs and benefits of alternative policies for individual member states."⁸⁵

Regional integration practices in many areas, given in Table 1.1, have shown the importance of external factors in the development of regional integration. At the global level the superpowers had an impact on regional cooperation because of their pursuit of ideological and geo-political interests. At the regional and hemispheric level, groups of powerful actors provide a second level context which directly affects the process of regional cooperation with regard to economic, political, and strategic interests. Regional integration in most cases is likely to be seen as a means to increase members' economic interest and security. However, owing to the link between external actors and the process of regional integration, any policies toward regional cooperation determined by members' perceptions of costs and benefits "are subject to external forces."⁸⁶ In other words, external actors always work for their own interests, either for or against regional policies to integration. When a powerful external

⁸⁴. Axline, "Regional Co-operation and National Security", p. 2.

⁸⁵. Ibid, p. 8.

⁸⁶. Axline, "South Pacific Region Cooperation in Comparative perspective", p. 46.

TABLE 1.1. NUMERICAL INDICATIONS OF INFLUENCE LEVELS OF EXTERNAL INCENTIVES ON REGIONAL INTEGRATION IN VARIOUS REGIONS

	EC	CARICOM	LAFTA	EAC	SPC	APC
Global System	3/2	2/n	3/n	1/1	2/n	2/n
Super-Powers :	3/2	3/3	3/n	2/2	2/n	2/n
Regional Powers	3/0	2/2	1/n	1/n	2/n	3/n
Counter-unions	0	2/2	2/n	1/n	2/n	2/n
Non-state Actors (IGO/NGO)	1/1	3/2	3/n	2/1	1/n	2/n

- Note : i. CARICOM = Caribbean Community and Common Market.
 LAFTA = Latin American Free Trade Association.
 EAC = East African Community.
 SPC = South Pacific Community.
 APC = Asia-Pacific Community.
- ii. The two sets of numbers used here are simply measured by the categories of the relationship between external factors and regional groups on conditions before (for the first set of numbers), and at the time of (the second set) integration process, if applicable.
- iii. The categories are indicated as follows :
- | | | | |
|---|----------------------|---|---------------|
| 1 | anxious & concerning | 0 | irrelevant |
| 2 | influential | n | not available |
| 3 | subordinate | | |

Source: Based mainly on Axline, "South Pacific region cooperation in comparative perspective", 1984; Axline, "Regional co-operation and national security", 1988; Cox, "Northern Actors in a South-South Setting", 1984; L. Krause, *The Common Market: Progress and Controversy*, 1964; and Sung-Joo Han, "The Pacific Cooperation Concept: Scope and Limitation", *Korea & World Affairs*, 7: 2, (Summer 1983), and the present development in Asia-Pacific.

actor is trying to monopolise its vested interest in a region, it will try to press ahead its integration initiatives to

regional countries or to diversify their individual interest in order to retard the emergence of regional unions against its interest, as in the case of American Caribbean Basin Initiative. Conversely, the British role in East African integration was positive through its former colonial links with Kenya, Tanzania, and Uganda to help them build up a cooperation structure. Although the UK might have its own thoughts about encouraging East African integration to maintain its traditional influence, regional integration here seemed to meet the mutual interests of all parties at the outset of negotiation.

It seems that whichever factors there may be, external actors to regional integration should be considered with respect to the integration process, which help work out a new framework. In addition, Cox focused on external aid to regional integration. In the case of East African integration, the donor/recipient relationship between external actors and the integration members was recognised as an important stake for integration. External aid here "was used to buttress local integration and cooperation sentiment."⁸⁷ Further, he indicated that "resources provided by the industrialised countries of the north can help accelerate the pace and depth of integration by assisting the system to move towards higher forms of integration, including the integration of production."⁸⁸ Like the contribution of the Marshall Plan to European integration, external aid in East Africa from various actors, such as from the USA, the UK, Canada, Scandinavian countries, China, the United Nations and the World Bank, made some important contributions to the integration process during the community's period of consolidation. This provided

⁸⁷. Cox, "Northern Actors in a South-South Setting", p. 285.

⁸⁸. Ibid.

political support to enhance the psychological identity of members, and economic help to build up the community's bureaucracy and member states' development. All in all, Cox concluded that "what does seem to come through loud and clear is that external aid can play a very useful role both symbolically and substantively during the initial years of an LDC integration system."⁸⁹

Through Axline's efforts to characterise external incentives, a more realistic thinking about regional integration anchored in the world of interdependence has been brought about. Therefore, considerable progress has arisen from paying greater attention to external factors. Changes in the international economic structure as a whole, e.g. intense external competition over markets, a larger scale of international negotiations, and increasing trade development with other regions, enable regional integration to be accelerated by the development of regional industrial restructuring. According to this review of the recent research on external factors in integration theory, a common concern has been with those less tangible factors to regional integration, in particular external impacts on economic development and industrial competition, which were neglected by the earlier exploration to the theory. The arguments above have clearly focused more on the actual development of European integration rather than on theoretical frameworks of integration. In order to increase our understanding of regional integration, a framework should therefore consider both actor- (external actors involvement) and system-factors (the influence of systems and functional mechanisms) together. Systems' influence means that the change of international

⁸⁹. Ibid., p. 307.

trends, e.g. economic recession, protectionism and technology advancement, will directly or indirectly result in changes in the costs and benefits of regional integration. The influence of functional mechanisms implies that global or counter-union's functional rearrangements, such as industrial restructuring, will result in regional groups reconsidering or being forced to change their policies, as in Table 1.2.

TABLE 1.2. GENERAL OUTLINES OF EXTERNAL INCENTIVES TO REGIONAL INTEGRATION

System-Factors:	
International Systems:	recession, restructuring economic order, economic linkages
Counter-Unions Competition:	market, trade, protectionism, investment
Functional Mechanisms:	trade, energy, industrial development, technology,
Actor-Factors:	
Superpowers:	military cooperation, economic aid
Regional Powers:	political & economic initiatives,
Governmental Organisations:	transnational institutions,
Non-governmental Organisations:	transnational interest groups,
Transnational Corporations:	regional business strategy

This thesis will explore regional integration by focusing upon external incentives, their impacts on industrial development and how they have affected the progress of regional integration both in the European Community and in the developing Asia-Pacific economic grouping, in particular in the Chinese Economic Area (CEA) mainly based on Southern China Economic Zone including Taiwan, Hong Kong, and China's Guangdong and Fujien provinces. The development of this

conceptual framework, however, does not deny the contribution and importance of internal political developments to the ultimate success of integration.

1.3. THE EUROPEAN COMMUNITY AND THE CHINESE ECONOMIC AREA

When Western Europe was suffering from recession, in the early 1980s, which was attributed to obsolescence in the European industrial structure and intense external competition from the US, Japan and the Newly Industrialised Countries (NICs),⁹⁰ the attempt to reinforce European industrial competitiveness through the completion of the European Internal Market (or Single European Market)⁹¹ triggered the relaunching of European integration. Unlike the previous political momentum for integration, the relaunching of European integration was derived, to a large extent, from European industry's response to its lack of international competitiveness. Completing the Internal Market Programme embodied in the White Paper and endorsed in the Single European Act (SEA) was urged by European industrialists, politicians, and academics. On the relaunch of European integration, what appeared to be crucial was that the appeal for the relaunch reflected Europeans', in particular industrialists', pervasive discontent with the ways the EC and

⁹⁰. According to OECD in 1979, the NICs included Brazil, Greece, Hong Kong, South Korea, Mexico, Portugal, Singapore, Spain, Taiwan and Yugoslavia. However, throughout this thesis, the NICs refer merely to Asian NICs (Hong Kong, South Korea, Singapore and Taiwan) and Latin American NICs (Brazil and Mexico), unless otherwise suggested. See OECD, *The Impact of the Newly Industrialising Countries on Production and Trade in Manufactures*, reported by the Secretary-General, (Paris: OECD, 1979).

⁹¹. According to Lord Cockfield, the "Completion of the Internal Market" is officially accepted in the EC. In France, it is called "*le Marché Grand*", while in Britain the "Single Market" is commonly used. See Lord Cockfield, "The real significance of 1992", in Colin Crouch and David Marquand, (eds.), *The Politics of 1992: Beyond the Single European Market*, (Oxford: Basil Blackwell, 1990), p. 1.

national governments impotently managed their economies in coping with external challenges. Ever since the late 1970s, much of the European decision-making agenda in the EC and national levels has been beset by trade deficit, unemployment, industrial failing, and declining competitiveness. At that time, the progress of European integration had been largely driven by a desire for counterbalancing external economic challenges.

Thereby, the EC carried out industrial restructuring as part of its economic development aiming at increasing the strength of the European economy as a whole, for example with several European industrial collaboration programmes intended collectively to enhance technology research and development for improving European industrial competitiveness. There have been various factors widely noted as the related benefits of the relaunch of European integration, such as a general recognition of the need for the reform of the inefficient EC's decision-making, the settlement of the British budgetary rebate, an elite alliance across Europe, and the coalition of ruling parties in West European countries. The general demand for the improvement of European competitiveness has contributed much more to the achievement of European consensus and endorsement of national governments than has been recognised by integration theorists. What one cannot deny about integration dynamics is that political agreement has been based on the assumption that stronger West European economies would result in political integration. There may have been other influences on the passage of the SEA within the EC's governing structures, e.g. the demand for institutional reform, and for more efficient and democratic decision-making, but it was the industrial impetus of seeking

to respond to external competitive challenges from the US and East Asia which was a critical factor in the renewed enthusiasm for integration in Western Europe in the 1980s.

Recently, the emergence of the Asia-Pacific Economic Cooperation (APEC), the advancing Asia-Pacific subregional economic grouping, and the agreement of a tripartite North American Free Trade Area (NAFTA) linking the US, Canada and Mexico, have been realised as a response to the 1992 programme of completing the European Single Market.⁹² In the context of regional cooperation around the Asian Pacific area, as the EC 1992 programme is being pushed forward, this vigorous movement of economic cooperation has been accelerating, especially around Japan, the Asian NICs (ANICs: Hong Kong, Singapore, Taiwan and South Korea) and ASEAN Countries as well as China and Vietnam. Above all, the agreement of the European Economic Area (EEA) on the 22 October 1991 which combined the EC and EFTA economies, has established the largest economic system in the world, which has become an enormous external incentive to Asia-Pacific economic cooperation. Economists argue that this is a symbol of the growing regionalisation of the world trade system.⁹³

The changes in the international political and economic system that have been influencing the context of Asian regionalism include "the evolution of US-Soviet relations from conflict to cooperation, the collapse of communism in the Soviet Union and Eastern Europe, the reversal of the 'locomotive' role of the United States, the ascendancy of

⁹². See various arguments about which the EC as an external factor has contributed to the emergence of regional integration in Asia-Pacific and North America: Susumu Awanohara and Nayan Chanda, "Uncommon bonds", *Far Eastern Economic Review*, (18 November, 1993), p. 16; "Year of the blocs?", *Asiaweek*, (12 January, 1993), p. 42; Tetsuo Naito, "North American Free Trade Agreement (NAFTA) and its influence on Asia", *Pacific Business and Industries*, 2, (1993), p. 7.

⁹³. *Financial Times*, (23 October 1991), p. 3.

Japan as the world's banker, and the economic integration of North America."⁹⁴ These issues have, to some extent, become an external driving force for Asia-Pacific economic cooperation. Facing increasing restraints on their foreign trade with developed economies, Asia-Pacific regional export-led economies have sought to adjust their industrial structures and, thus, maintain their competitive advantage and persistent economic growth. Moreover, the rapid economic growth in East Asian economies has been accompanied by the growth of subregional economic groupings. Industrial development is, therefore, important for an understanding of the development of economic integration in the Asia-Pacific region, particularly the emergence of subregional groupings, e.g. the CEA.

Since the 1980s, the developing trend of new regionalism with special reference to industrial competition has been shaping the new world order, and could lead to the redistribution of world power. In particular, the movement of European unification has been a very strong external economic incentive to Asian Pacific cooperation. As far as those efforts to advocate regional cooperation are concerned, the positive progress towards European integration appears to be the force behind a great European "economic fortress". For those countries which depend very much upon trade such as the ANICs the emergence of the EC's protectionism against those traders has served as a "catalyst" to direct them to a common interest of pursuing regional economic groupings.⁹⁵ In short,

⁹⁴. Richard Drobnick, "Economic integration in the Pacific region", Technical Papers, No. 65, OECD Development Centre, Under the direction of Charles Oman. Produced as part of the research programme on Globalisation and Regionalisation, (May 1992), p. 15.

⁹⁵. As protectionism is increasing in the EC against outside suppliers in general, and the ANICs in particular, new regionalism has emerged in the North America and Asia-Pacific. The Asian NICs in facing the increase of protectionism have been advocating regional economic grouping as a way of sheltering their interest and strengthening their competitiveness. For the EC's external policy vis-à-vis the Asian NICs see Sun-Taik Han,

all these developments suggest that economic incentives either endogenous or exogenous, (which were hardly considered by the theorists, because they did not exist then), have come to dominate the recent development of regional economic integration.

It was the external pressure of international structural change on national industrial development that triggered the relaunching of European integration in the 1980s. To meet Japanese and American competition, European business groups actively and closely worked with the Commission, and in return won credit for initiating the proposals to complete the Internal Market and lobbying for relevant policies. So, shouldering the recovery of the European economy and well being, national and transnational business groups, which were a necessary condition, contributed to the success of negotiating the SEA with the priority of unifying the market. The completion of the Internal Market, the crucial part of the SEA, was strongly advocated by European industrial groups and their blueprints of changing economic scale in Europe.

The importance of industrialists in pushing forward integration in Western Europe has provided a useful model to the understanding of the process of economic integration in the CEA. Especially, while the relationships between China, Hong Kong and Taiwan have still been confined for political reasons, their close economic and industrial ties driven largely by Taiwanese and Hong Kong's businessmen have brought about a subregional economic grouping in East Asia. Despite the fact that no political arrangement has yet been made for cooperation, numerous business contracts within the CEA have stimulated the progress of economic integration. Although the

European Integration: The Impact on Asian Newly Industrialising Economies, (Paris: OECD, 1992), pp. 28-35.

CEA may as yet be an intangible concept for many people, it has already attracted much of the business flows in East Asia and is to a large extent involved in most of Chinese overseas economic activities in the Asia-Pacific region. In addition, regional decision-makers have increasingly paid their attention to this kind of economic development.⁹⁶ While economic complementarity may be the essential condition for the formation of a subregional grouping, the actual engine for this is nothing more than businessmen seeking to gain a favourable position in international competition.

Following the Japanese example, the ANICs have emerged as some of the most energetic regional economic players in the Asia-Pacific region. In the 1980s, as most of the low cost economies in Southeast Asia and China have gained a comparative advantage in the production of labour-intensive industries over the ANICs, the ANICs have engaged in industrial restructuring by relocating their sun-set industries, e.g. textiles, footwear, and toys, in low cost economies, and by upgrading their technologies at home in order to move industrial structures upwards into knowledge-, capital- and technology-intensive industries, e.g. Singapore and Hong Kong's financial and shipping services, Taiwan's computer and South Korea's machinery and transport equipment. This developing trend has triggered the prospects for regional economic integration through intensifying intra-regional trade, foreign investment, and an international division of labour.

The emergence of Asia-Pacific subregional groupings has been based upon a recognition of the importance of economic

⁹⁶. The Asian Development Bank Workshop on Growth Triangles held at the Manila headquarters in May 1993 expressed the high regional interest in this development of subregional grouping. See "Growth Triangles will spur development", *ADB Quarterly Review*, (May 1993), p. 24.

development in stimulating economic integration. In the context of wishing to strengthen competitiveness and accelerate economic development and the growth of trade, the CEA has emerged as one of the major subregional groupings in East Asia. Economic complementarity amongst regional economies has been an important incentive for the formation of Asia-Pacific subregional economic groupings. During the last decade, Hong Kong, Taiwan and overseas Chinese have poured enormous amounts of capital into China initially seeking manufacturing bases, but eventually hoping to exploit the domestic market. Intensifying economic transactions within the region have created an industrial division of labour, which is a necessary condition for economic integration. The course of industrial restructuring in the ANICs has been interlinked with China's reform process for economic development, which has led to the formation of economic groupings along China's coastal areas. Unlike the driving forces behind regional economic integration in the EC, the emergence of the CEA has been driven primarily by the private sector. In short, in response to external challenges, industrial development has promoted regional integration in both the EC and CEA.

1.4. OVERVIEW

The purpose of this thesis is therefore twofold. It is, firstly, to explore the proposition that the process of industrial restructuring is strengthening regional cohesion and thereby bringing about progressive economic integration against the context of world economic interdependence and industrial competition. Throughout the 1970s, due to economic

recession followed by the wake of two oil crises and protectionism, the diversification of national interest by the enlargement of the EC and the procedural weakness within the EC's decision-making machinery, the pace of European integration as well as economic growth were slowing down, a condition which came to be termed "Eurosclerosis" or "Europessimism".⁹⁷ In the early 1980s, at the peak of Eurosclerosis, European industry was undertaking industrial restructuring through collaborations under the auspices of the European Commission. The pressure for further industrial restructuring asserted by European industry with the endorsement of the EC led to the relaunch of European integration. It was this pressure that contributed largely to the passage of the SEA and the creation of the Single Market. It can therefore be seen that industrial restructuring may act as a stimulus to regional economic and political integration thereby offering an important contribution to our understanding of both the theory and practice of regional integration.

Secondly, this thesis aims to demonstrate that industrial restructuring and its impact on regional integration offers the key to an understanding of the regional economic development of the CEA. In particular, the interaction of individuals and corporations in the private sector, which has led the process of CEA integration, has been sufficiently powerful to be able to overcome political difficulties. Although this pattern of industrial restructuring leading to regional economic integration may be more limited in scope

⁹⁷. For the factors which caused Eurosclerosis See Dennis Swann, *The Single European Market and Beyond: A Study of the Wider Implications of the Single European Act*, (London: Routledge, 1992), pp. 12-14. In economic terms, Eurosclerosis was the symptom of the decline of labour productivity, little investment, the decline in profitability and weakening industrial competitiveness. See M. V. Posner, and J. R. Sargent, "A case of Euro-sclerosis?", *Midland Bank Review*, (Winter 1987), pp. 9-17.

than that in Europe, there may be some important parallels between the patterns of industrial restructuring and economic and political integration in the two regions. These attempts to make a comparison of the industrial driving processes of political and economic integration in Western Europe and East Asia provides some useful insights for our understanding of regional integration. To begin with, the thesis provides a survey of the literature on integration theory and the contribution of external factors to regional integration and attempts to create an analytical structure for economic and political integration. In Chapter Two a historical analysis of European integration divides the postwar period into three categories: 1945-1973, 1973-1980 and 1980-1992. Chapter Three focuses on the impact of the European integration movement on European industry, the economic crisis facing European industry and its special interests in the process of advocating the programme to complete the Internal Market. It also emphasises the key role industrialists have played in obtaining the internal market.

Chapter Four analyses the Asia-Pacific region where industrial development has had so much effect on the formation of regional economic groupings. Chapter Five focuses on the concept of the CEA, and analyses the impact of industrial development on the formation of the CEA. In this particular economic grouping, industrial development across the borders of interdependent economies has raised expectations of further economic integration, and, to some extent, raised the possibility of Chinese reunification.

Despite other political constraints within the CEA itself, Taiwan-China's political stalemate in particular may have limited its further development. Chapter Six therefore

provides an important vision of Chinese economic integration being driven by the private sector. This chapter therefore focuses on the internal political constraints which the CEA is currently suffering from, which highlight the particular development of the CEA under the existing political impasse. The development of the CEA, therefore, gives evidence for a reappraisal of regional economic integration. Chapter Seven focuses on external constraints on the formation of the CEA, concentrating on Japan's political and economic complementary interests to China, the wary perspective of the ASEAN countries, the effect of the European Single Market, and the impact of the NAFTA on the CEA. Finally, the assessment of industrial development in the experience of the EC and the CEA suggests that exogenous industrial development has not only been a significant contributory factor to European economic integration, but is also applicable to the formation of Chinese economic integration.

CHAPTER TWO

EXTERNAL INCENTIVES FOR EUROPEAN ECONOMIC INTEGRATION: A HISTORICAL ANALYSIS

This chapter analyses the context in which European political and economic integration has taken place through exploring international incentives that stimulated the progress of political and economic integration. Since the end of the World War II, the process of European integration has been largely driven in the first place by political motives (a hope for peace) and more recently by socio-economic factors (general demands for maintaining economic prosperity, creating jobs and enhancing industrial performance). In general, regional economic integration is an adjustment process of economic relations amongst member states of a regional grouping, which results from the emergence of common interests through economic interaction. Federalist, functionalist and neofunctionalist approaches of regional integration have focused upon exercising the "internal processes" of a community. As far as the formation of the European Community was concerned, the momentum for political integration at the earliest stage seemed to be a reaction to the destruction of war. Immediately after the Second World War, pacifists and federalists in Europe, e.g. Jean Monnet and Altiero Spinelli, sought to organise some kind of European union to combine German with French interests in order to eliminate any possibility of conflict in the future. Thus, the Schuman Plan, which stemmed from the need to manage steel and coal, because of their potential for being used to manufacture weapons, was brought about.

So, at the outset of European integration, the basic motivating force was the desire for West European security and welfare. However, as soon as the Soviet sphere of influence was established in East Europe in the late 1940s, Western Europe was then driven to seek much deeper political and military cooperation with its Atlantic allies. Meanwhile, the United States in order to help rebuild Europe on the one hand, and to impose its superpower politics on Western Europe to contain the Soviet aggression on the other, supplied Europe with large scale economic aid in the form of the Marshall Plan in 1947. In order to distribute aid, European countries were conditioned by the Plan to organise themselves together. From this the Organisation for European Economic Cooperation (OEEC) resulted. With American encouragement the OEEC had introduced a mechanism for international cooperation between West European countries. Thereafter, until the collapse of communism in Eastern Europe in 1989-90, European integration had always coexisted with superpower politics, illustrating the influence of external factors on European integration.

Although Karl Deutsch has argued that every forward step towards European integration was achieved by members' efforts,¹ these sometimes could not fully explain either the reasons why members of the EC should go along with integration or the incentives that lay behind the political momentum for further integration. Integration theorists have been unable to explain or to clarify when and how the pace of integration reached the threshold that pushed it on towards the next step to integration.² Others have argued that European integration was

¹. Deutsch has argued that the volume of transactions, political, economic, or cultural within an integrating union throw a burden upon institutions and member states for change. See Deutsch, *Political Community at the International Level: Problems of Definition and Measurement*, (Garden City, N.Y.: Doubleday & Company Inc., 1954), p. 39

². If there is a detailed schedule of integration, it would be Balassa's categories of integration: a free trade area, a custom union, a common market, an economic union, and

not only implemented by internal efforts but accelerated by external incentives which were likely to be the main factors in driving integration beyond the next threshold.³ If some detailed rules for integration could be recognised and drawn up into a formula for integration, then it would be much easier for member states to control the progress of regional integration. It is evident that member states in the process of political, economic and social integration have always had to take account of the costs and benefits of integration. However, once external pressures become so strong that they will cost members more than the costs of integration, the external costs emerge as a decisive force pushing member states to reassess whether they should proceed with integration or not.

What sorts of external pressures have arisen? How did these pressures affect European integration? In the post-war period, because of the power vacuum and economic depression in Europe, external actors, most notably superpowers, were continuously able to influence the progress of European integration through the projection of military forces and economic aid. During the 1970s and 1980s, global recession brought Europe a further structural crisis in its industry and foreign trade, which resulted in mass-unemployment, sharply increasing raw material costs, less commitment to inward investment, and fierce competition in domestic and international markets from Japan, the USA, and the NICs.

complete economic integration. The categories can be seen as five different steps to integration. The threshold between each different step of integration is decisive. However, the moment at which the progress of integration becomes mature enough to enable it to be upgraded remains theoretically unclear. See Bela Balassa, *The Theory of Economic Integration*, (London: George Allen & Unwin Ltd., 1962).

³. Such as Amitai Etzioni, Stanley Hoffmann, Joseph Nye, Karl Kaiser, Ernst Haas, and Roger Hansen. For their detailed arguments refer to the previous chapter.

TABLE 2.1. PENETRATION RATE*: INDUSTRIAL PRODUCTS ON THE INTERNAL MARKET (percentage change between 1973-1982)

	EC	USA	Japan
High-demand Sectors:	+7.9	+5.9	+1.6
Electrical & Electronics hardware	+10.9	+6.7	+1.7
Information technology, office automation & precision equipment	+14.7	+4.5	+1.3
Chemicals & pharmaceuticals	+3.6	+2.9	+1.5
Medium-demand Sectors	+1.8	+2.3	+0.2
Low-demand Sectors	+3.8	+4.2	+1.4

Note: * penetration rate = imports / domestic demand.
Source: EUROSTAT and Commission departments.

In terms of the penetration rate of industrial products on the internal market,⁴ in high-demand sectors notably the electrical and electronics industries, information technology and chemicals, European markets over the period of 1973-1982 had the highest increasing penetration rate compared with the American and Japanese markets (Table 2.1). Moreover, European export market share in high-demand sectors declined largely by -2.5 per cent from 1973 to 1983, while the US and Japan, on the contrary, increased their market share by 2.7 per cent and 5.6 per cent respectively over the same period (Table 2.2).

TABLE 2.2. EXPORT MARKET SHARE (percentage change between 1973-1983)

	EC	USA	Japan
High-demand Sectors:	-2.5	+2.7	+5.6
Electrical & Electronics hardware	-1.8	+2.4	+11.4
Information technology, office automation & precision equipment	-5.0	+5.0	+8.0
Chemicals & pharmaceuticals	-1.0	+1.9	+0.5
Medium-demand Sectors	-1.2	-0.3	+6.1
Low-demand Sectors	+4.1	+1.0	+1.4

Source: EUROSTAT and Commission departments.

⁴. Penetration rate, one of the useful indicators to assess the impact of imports on domestic industrial performances, is total imports over domestic demands.

Apart from unemployment, Europe's ratio of non-wage labour costs to total labour costs was 40.1 per cent. This was also much higher than the US' (27.8 per cent) and Japan's (21.0 per cent) in 1981.⁵ These unfavourably high costs resulted in the decline of profitability in the European manufacturing industry. The net rate of return on the fixed capital in the EC4 (France, West Germany, Italy and Britain) was 18.7 per cent in 1960-1973 and 13.4 per cent in 1974-1979, while Japan was 35.6 per cent and 21.0 per cent, and the US was 29.1 per cent and 20.6 per cent.⁶ As a result, relative to its main industrial rivals, the USA and Japan, the EC suffered from a lack of industrial competitiveness, which in turn stimulated a desire in both the public and private sectors for a revival of European integration.⁷ European industrialists, notably of the European Roundtable (ERT) along with the Union of Industrial and Employers' Confederations of Europe (UNICE),⁸ began a campaign of lobbying national governments and the EC bureaucrats for the completion of a single European market, as a means of improving the performance of European industry and commerce.⁹

⁵. Non-wage labour costs are principally social security contributions of the employer. Europe's higher ratio of non-wage costs to total labour costs was attributed to high social security costs, albeit hourly labour costs in manufacturing were lower in European countries than in the US. Information base on Institut der Deutschen Wirtschaft, *Informationsdienst*, No. 18, Köln, 1982. See Michael Emerson, (ed.), *European Stagflation*, (Oxford: Clarendon Press, 1984), pp. 204-205.

⁶. Information based on OECD and the EC Commission. *Ibid.*, pp. 201, 203.

⁷. Through industrial development, politicians and industrialists met a broad consensus to take account of European dimension in national policy and business strategy. See "Improving competitiveness and industrial structures in the Community", Document, Commission of the European Communities, 1987, pp. 34-36.

⁸. The Roundtable founded in 1983 was originally named the Roundtable of European Industrialists. It had grouped 30 chief executives from Europe's biggest companies in 1988, including AB Volvo, Fiat, Philips, Saint-Gobain, Daimler-Benz, Plessey, Ferruzzi, Nestlé, Telefonica, Norsk Hydro and Nokia. The UNICE created in 1958 has been recognised as official spokesperson for European business and industry vis-a-vis the European institutions and in 1989 was made up of a 32 industrial member federation (The Confederation of British Industry and its equivalents) from 22 European countries with a permanent Secretariat based in Brussels.

⁹. See Jacques Pelkmans, "Completing the internal market for industrial products", Document, Commission of the European Communities, 1986, p. 34.

Many researches concluded that the EC would have to unify further in order to respond effectively to external competitive pressures and to undertake a stronger political and diplomatic role on the world stage.¹⁰ Thus, European integration has been constantly inspired by external factors, whether positive or negative, or whether continual or contingent events. On this basis, the process of European integration can be divided into three phases according to the character of a particular historical period. Firstly, from the post War era up to 1973, political motives and external actors played an important part in the process of European integration (Appendix F-2.1). Secondly, between 1973 and 1980, the outbreak of two oil crises in 1973-74 and 1979 worsened worldwide economic recession, which resulted in the transformation of the international economic structure and caused a deterioration of European industrial structure. European integration prior to 1973 was based on economic expansion from which industrial growth benefited considerably. European integration came to a halt as a result of the European economy being hard hit by recession (Appendix F-2.2). Finally, from 1980, Vicomte Etienne Davignon, European Commissioner for industry from 1977 to 1985 and for Research and Technology from 1981 to 1985, led the Plan for the European Strategic Program for Research and Development in Information Technology (ESPRIT) which successfully converged 12 big European firms endeavouring to focus on the Community's rather than national markets.¹¹ Since then, the European

¹⁰. Such researches were under the sponsorship of the Commission of the EC. For example, a series of relaunching Europe reports were published on *European File*, 16/81, 3/82.

¹¹. The ESPRIT programme agreed by the Executive Community of 12 big firms which included Siemens, AEG and Nixdorf (Germany); GEC, ICL and Plessey (UK); Olivetti and Stet (Italy); Philips (the Netherlands); and Thomson, GCE and Bull (France). For the successful performance that ESPRIT credited to European industrial development see Lynn K. Mytelka, and Michel Delapierre, "The alliance strategies of European firms in the information

dimension of industrial collaboration has become not only a European guideline of industrial strategy but also an effective approach for the understanding of economic integration (Appendix F-2.3).

2.1. 1945-1973: THE POST WAR ERA - SUPERPOWER POLITICS AND THE RECONSTRUCTION OF THE EUROPEAN COMMUNITY

2.1.1. The Effort for Political and Economic Integration as a Means and Ends of Conflict Resolution

The disastrous War in Europe between 1939-1945 was a turning point for Western Europe in many respects. Firstly, West Europe was no longer the leader of international politics and had taken second place in world affairs. The emerging new global balance of power between the Soviet Union and the United States made Western Europe a superpower political arena. Secondly, the war and its aftermath transferred the balance of power in Europe, which resulted in an equality of power within the region.¹² Moreover, either scattered (such as Belgium, the Netherlands, Spain, Portugal and Italy) or substantially weakened (France and Britain), the warworn European colonial empires were incapable of continuing to administer colonies. As their colonies became independent nations, the loss of controlling colonies changed European countries' past apathy to European common affairs and pushed them to rethink the whole structure of their political and economic relations with the world and each other. As a result, these changes of European political structure contributed to

technology industry and the role of ESPRIT", in John H. Dunning, and Peter Robson, (eds.), *Multinationals and the European Community*, (Oxford: Basil Blackwell, 1988), pp. 147-149.

¹². After the War, there was not any hegemon dominating Western Europe. See arguments by Gordan Smith, *Politics in Western Europe: A Comparative Analysis*, 2nd edition, (London: Heinemann Educational Books, 1976), p. 240.

the emerging context of political and economic integration in Europe. Indeed, "the survival of the (European) Community must largely be attributed to the fact that it has filled a political vacuum in Europe."¹³

American thinking of rebuilding Europe was based on its global strategy of containing the Soviet aggression and in the belief that revitalising the European economy would assure its success in those political and military aims. Therefore, the decisive US moves to help reconstructing European countries and their economies brought about the North Atlantic Treaty Organisation (NATO) in April 1949 for European security and the OEEC for economic recovery. Together these two organisations dominated the whole pattern of the early development of European political integration. The Marshall Plan which was to encourage European industrial reconstruction attached a condition that every participating country should accept a common programme of recovery and cooperate to establish a permanent organisation, the OEEC, to serve that aim. The establishment of the OEEC to distribute the Marshall aid marked a decisive step towards peacetime cooperation for a common stance in Europe and offered a valuable institutional framework to further regional cooperation.¹⁴

As early as the 1950s, nearly all of Europe was drawn into rival superpower blocs by a series of international events: the Truman Doctrine, Marshall Aid, a currency reform in West Germany, the Berlin Crisis, the founding of COMECON (Council for Mutual Economic Assistance), the founding of NATO, the failure of the EDC (European Defence Community), the recruitment of West Germany into NATO and the establishment of

¹³. See Mark Blacksell, *Post-War Europe: A Political Geography*, (Folkestone: Wm Dawson & Sons Ltd., 1977), p. 83.

¹⁴. For the details of the OEEC operation see *Ibid.*, pp. 35-47.

the Warsaw Pact.¹⁵ Diebold has recorded how superpower politics was imposed on Western Europe by economic aid, and how this influenced European attitudes towards integration:

"To justify massive American aid, Europe would have to make the greatest possible use of its own resources. That would require close cooperation and, in particular, a breaking of the barriers to the exchange of goods inside Europe."¹⁶

Concerning European security and prosperity, Jean Monnet suggested pooling coal and steel between France and Germany under international control in the belief that integration of crucial industrial sectors would allow Germany to be reintegrated into the community of European nations and thus assure peace in Europe, which brought about the Schuman Plan on 9 May 1950.¹⁷ The outbreak of the Korean War and the increase of steel consumption for war industries hastened the need to bring Germany's industries to live under international control, which resulted in the establishment of the first European supranational institution, the European Coal and Steel Community (ECSC). Moreover, during the Korean war there were growing fears of a Soviet attack on Western Europe and general demands for West Germany to contribute to NATO, which encouraged the six members of the ECSC (Belgium, France, West Germany, Italy, Luxembourg and the Netherlands) to sign the

¹⁵. Barry Buzan, Morten Kelstrup, Pierre Lemaitre, Elzbieta Tromer, and Ole Waever, *The European Security Order Recast: Scenarios for the Post-Cold War Era*, (London: Pinter Publishers, 1990), p. 37.

¹⁶. William Diebold, Jr., "The Process of European Integration", in Lawrence Krause (ed.) *The Common Market - Progress and Controversy*, (Englewood Cliffs, N.J.: Prentice-Hall, 1964), pp. 29-30.

¹⁷. Jean Monnet, one of the pioneering figures of post-war Western European integration, was the first President of the ECSC. He put forward this creative idea to the then French Foreign Minister Robert Schuman. See "1988 European Jean Monnet Commemorative year", *European File*, 9/88.

EDC.¹⁸ Despite the fundamental purpose of the ECSC to encourage economic expansion, industrial growth, increase of employment and a rising living standard for member states through the establishment of a common market in coal and steel, the decisive reason for a community was nothing more than a political concept to reposition Germany in the community of Europe in a multinational framework.¹⁹

At the beginning of European Integration, one might wonder why the momentum for signing the Treaties of Rome establishing the European Economic Community (EEC, generally referred to as the Common Market) and the European Atomic Energy Community (EURATOM) was not overshadowed by the failure of the EDC.²⁰ Apart from these constant external factors of the Soviet threat and American aid to Europe, some other external contingent events were to play an important part in acting as a stimulus for the progress of political integration. For instance, after the ECSC was established in 1951, its original six member states were hoping to move towards further political integration. However, the prospects for further political integration was not so promising, as the Six were wondering if the experiment of the ECSC would work. The French government took the first initiative of further integration - known as the "Pleven Plan" - for the EDC.²¹ Ironically the

¹⁸. Britain refused the EDC at the beginning. The EDC was not ratified by France and Italy, as its initial reason - the Korean War had ended - did not exist. See Blacksell, *Post-War Europe: A Political Geography*, pp. 90-91.

¹⁹. Buzan, Kelstrup, Lemaitre, Tromer, and Waever, *The European Security Order Recast: Scenarios for the Post-Cold War Era*, p. 145.

²⁰. As far as the internal factors were concerned, the federalists regained the momentum for further integration by focusing economic field in order not to entangle with the issue of national sovereignty. That brought about the agreement for the Six in March 1957. See John Pinder, *European Community: The Building of a Union*, (Oxford: Oxford University Press, 1992), pp. 7-8.

²¹. As steel and coal were put under international management, the French Prime Minister René Pleven, advocated that defence was to follow suit. Although the EDC was rejected, a general demand for an independent European defence initiative brought about the Western European Union with the full participation of the UK, Italy and West Germany. *Ibid.*, pp. 91-92.

French National Assembly led by General Charles de Gaulle rejected the treaty, which served as a serious blow to the wider European Political Community and the cause of European integration.

Although the successful emergence of the EEC was attributed to the growing spirit of compromise amongst the Six, mainly between France and West Germany over agricultural and industrial products, several contingent international events catalysed that progress. The Soviet troops crushed the Budapest uprising in 1956. It "sharply underlined the need for greater Western European cooperation."²² It was because Soviet action on this scale brought about fears of its ability to project its military power in other parts of Europe if need be. In addition, for the French government, with its reluctant negotiating position, the 1956 Suez debacle and the setback to its colonial power in Algeria made it more conciliatory towards its neighbours. It was these external events that propelled the Six down the road to integration.

Officially, American support for the Common Market was based on the belief that a strong ally is a good ally and economic integration would strengthen the members' capacity to provide their own security.²³ Because the external security question was very important in this period, the development of European integration was intertwined with that of the military alliance, NATO. In fact, American efforts were intended not only to reinforce the defence of Western Europe itself, but also to bolster Western Europe's capacity to take more responsibility for the maintenance of global order. At the same time, the growing strength of West European integration

²². Allan Williams, *The European Community - The Contradictions of Integration*, (Oxford: Blackwell, 1991), p. 25.

²³. L. Krause, "The Common Market : Progress and Controversy", in Krause (ed.) *The Common Market - Progress and Controversy*, p. 6.

reinforced the American frontline against the threat of Soviet aggression to Europe.

In the private sector, the US penetration of West European markets rested on capital investments by multinational corporations. According to the US Department of Commerce's report about American investment in 1965-1966, "(investment) rose by seventeen per cent in the US, twenty one per cent in the rest of the world, and forty per cent in the Common Market."²⁴ In 1967, one European commentator expressed the fear that "this European Market is basically American in organisation, American industry in Europe."²⁵ He quoted the view of Harold Wilson, the former British Prime Minister, that "the primary objective of Europe must be to prevent the domination of our economy by the Americans."²⁶ Many amongst the political and business elites of Western Europe believed that greater integration was the only way to stand up to international competition. As a result, European "third force" sentiment was emerging in the continent, particularly in France, in accordance with the progress of integration.²⁷ This was a core belief of the Gaullists. The calls of the third force for European nonalignment helped members to cohere in a common internal position, and to pursue external policies which were independent from the superpowers. This may be considered as a psychological impetus to integration, which actually led both the public and private sectors to a common voice in response to external challenges.

²⁴. J-J Servan-Schreiber, *The American Challenge*, (London: Hamish Hamilton, 1968), p. 6.

²⁵. *Ibid.*, p. 3.

²⁶. *Ibid.*, p. 15.

²⁷. See Krause, "The Common Market : Progress and Controversy", p. 4; also Stanley Hoffmann described it as the "resisters", in particular the French, "Obstinate or obsolete? the fate of the nation-state and the case of Western Europe", *Daedalus*, 95: 3, (Summer 1966), pp. 862-915.

2.1.2. Internalisation of External Incentives and European Integration

The successful establishment of the three European Communities (ECSC, EEC and Euratom) suggested that there had been increasing recognition of the need for political and economic integration amongst the Six member states, in particular to meet external demands. Throughout most of the 1960s, disputes over the role of the European institutions and political integration between France and other EC members held up the momentum of political integration, because French President Charles de Gaulle's intention to overhaul the structure of the European Communities kept reversing the agenda of political integration to the original argument of how to build the Community.²⁸ Moreover, the row between France and the US over international trade and security was also shaping the progress of European integration. The establishment of the Common Agricultural Policy (CAP), the united EEC against the US in the round of multinational negotiations from 1963-67, popularly known as the Kennedy Round, under the auspices of the General Agreement on Tariffs and Trade (GATT), and the efforts to establish an economic and monetary union had shown a great deal of external constraint variously propelling the EC's integration progress.

Developing the Common Market, the Six were seeking for the alignment of the common external tariff on imports from non-member countries, while reducing tariffs amongst their own members. According to the conditions set out in the GATT regulation to ensure that the formation of a customs union

²⁸. Throughout the history of the EC, there have been two tendencies in French European policies influencing the progress of European integration: the federal route enunciated by Monnet-Schuman, and the route towards cooperation of states (confederate Europe) promoted by de Gaulle. See Jonathan Story, and Guy de Carmoy, "France and Europe", in J. Story, (ed.) *The New Europe: Politics, Government and Economy since 1945*, pp. 187, 204.

amongst regional economies does not harm the interests of the third parties, the EEC was bound to complete the customs union within a certain period and substantially to cover all members without discrimination.²⁹ As a result, the Six accelerated the progress of the establishment of the European customs union and subsequently reached the final stage in which duties were abolished within the EEC, eighteen months ahead of schedule in July 1968.

As the Common Market and the EFTA were in turn established in 1958 and 1960, the US government anticipated a considerable impact from regional trading blocs in Europe on world trade. The Kennedy administration was very anxious that the preferential trading blocs in Europe would divert trade from the US markets to Western Europe and the planning of the European common agricultural policy would adversely affect American agricultural exports to Europe. Especially, the European customs union provided a wider European market as the common external tariff stimulated overseas investment in Europe and away from the US. This would further aggravate the US balance of payments.³⁰ In 1961, when Britain announced that it would apply for EEC membership, the message suggested to the US that the EFTA countries may follow suit. The US President John Kennedy in 1962 was urged to call for an Atlantic partnership between the US and a uniting Europe to negotiate for the liberalisation of international trade under the auspices of the GATT. His trade proposals were made to prevent the Western world dividing into regional trading blocs. At that critical moment, President de Gaulle made use of American demands to push through French policy to establish

²⁹. R. C. Hine, *The Political Economy of European Trade: An Introduction to the Trade Policies of the EEC*, (London: Harvester Wheatsheaf, 1985), p. 43.

³⁰. Gerald Meier, *Problems of Trade Policy*, (Oxford: Oxford University Press, 1973), p. 26.

the Common Agricultural Policy,³¹ because the French government threatened to withdraw from the Community, if its agricultural interests would not be recognised by its partners.³² To secure the Six's interests in the coming negotiation with the US and to assure the management of the Common Market in a common direction, other members of the EEC therefore agreed to adopt the CAP.

During the 1960s, the issue of monetary cooperation was global. The International Monetary Fund (IMF) acted under the auspices of the US dollar as a major actor in this in promoting credit assistance and examining changes in par values. However, the US was subjected to continual current account deficit and capital outflows, which resulted in the weakness of the dollar and the instability of the Bretton Woods System.³³ In addition, when the customs union and the CAP were established in the EEC, the exchange-rate adjustments appeared to disrupt the Common Market's functioning because of the application of fixed common prices in some agricultural products. The major currency crisis burst out in 1968 involving the French franc and the German D-mark. As a result of the settlement of the crisis, a franc depreciation following by a D-mark appreciation exposed the EEC's lack of a mechanism to manage economic and monetary cooperation between its member states. This needed to be addressed. The great attempt to create an economic and monetary union was made by

³¹. The basic regulations for the CAP were adopted in 1962. The acceptance of the CAP came at the time of the establishment of the customs union in 1968, after a lengthy negotiation within the EC. Jonathan Story, "Europe in the global state and market system", in J. Story, (ed.), *The New Europe: Politics, Government and Economy since 1945*, (Oxford: Blackwell, 1993), p. 28.

³². Gerald Meier, *Problems of Trade Policy*, p. 212.

³³. Western statesmen institutionalised an international monetary order through the creation of the IMF at Bretton Woods, New Hampshire in 1944, through which international liberal trade and monetary systems came into being under American leadership. See David Blake, and Robert Walters, *The Politics of Global Economic Relations*, 4th edition, (Englewood Cliffs, New Jersey: Prentice-Hall, Inc., 1992), pp. 68-70.

the Hague summit and was crystallized into the Werner Plan which was submitted to the Council in October 1970.³⁴ Although the impetus for an economic and monetary union was to some extent derived from the EEC's dissatisfaction with the fluctuation of their exchange-rate because this would easily threaten the fledgeling CAP in terms of prices, the ambition to secure greater monetary independence from the US was a major driving force.

Throughout the 1960s, the six original countries of the EC had achieved the customs union with the Common External Tariff and the first common policy in agriculture by compound efforts for internal political processes and policy response to external restraints. In terms of political integration, however, when General de Gaulle, the nationalist French President, returned to power in 1958, European integration came to be overshadowed by his controversial concept of the confederate or intergovernmental form of Europe integration that rejected Monnet's idea of federalism. De Gaulle's ambitious plan was to construct a pan-European grouping on the Continent based on a Franco-German axis.³⁵

In 1961, the French government promoted the "Fouchet Plan" for a union of states drafted by President de Gaulle, which was to provide for confederate structures and to allow national governments to preserve sovereignty in all important areas.³⁶ The Plan which had a clear French perspective on the European political future set up four permanent

³⁴. Pierre Werner, the Prime Minister of Luxembourg, led a group of national and EEC officials to prepare a report that scheduled the attainment of an economic and monetary union by 1980.

³⁵. For more Gaullism and the Gaullist vision of Europe see Mally's analysis, *The European Community in Perspective*, pp. 84-93.

³⁶. The most obvious establishment was supposed to be the Council at the level of heads of state or government whose decision was made by unanimous voting. For detail of the Plan see Gerhard Mally, *The European Community in Perspective: The New Europe, the United States and the World*, (London: Lexington Books, 1973), pp. 195-196.

intergovernmental committees to promote policy integration in foreign, defence, commercial and cultural affairs, which incurred strong opposition from its five partners. In particular for West Germany and Italy, the planning of cooperation in defence and foreign policies would depart from the Treaty of Rome and weaken the EEC and NATO to which they were very much committed.³⁷ The Benelux countries which feared French domination within an intergovernmental European structure of cooperation argued that the fundamental change of the structure raised in the Plan should be delayed until the problems of British accession were resolved.³⁸ The discussion of the Fouchet Plan was then abandoned and never resumed.

During the 1960s, European political integration was inactive due to a series of policy conflicts between France and its allies. France disagreed with the US dollar privilege over its exemption from the rules of international exchange and never fully shared the American containment approach to East-West relations. Under President de Gaulle, France challenged the whole structure of the Cold War and the Western alliance. As a result, France took action in 1963 to propose a new international reserve currency to replace the dollar.³⁹ In protesting against the Atlantic alliance's domination in West European defence, and against the lack of credibility of NATO's nuclear strategy, in 1966 France withdrew from military integration within NATO. Moreover, although Paris agreed the

³⁷. Derek Urwin, *The Community of Europe: A History of European Integration Since 1945*, (London: Longman, 1992), p. 106.

³⁸. Ibid.

³⁹. De Gaulle was convinced by his economic adviser Jacques Rueff that the inflow of dollars was to be blamed for causing French inflation. Facing balance-of-deficit, other countries had to pay in foreign currencies or gold, while the US could simply print its currency to cover external debts. The dollar privilege granted it "the capacity to finance any foreign policy activities it might choose." For detailed argument see Henry R. Nau, *The Myth of America's Decline: Leading the World Economy into the 1990s*, (New York: Oxford University Press, 1990), pp. 140-142; also Blake, and Walters, *The Politics of Global Economic Relations*, pp. 74-78.

EEC interests to be represented by the Commission in the Kennedy Round, de Gaulle's suspicion of the extensive American influence in the talks had never eased away. The widening gap between France and the US resulted in France twice vetoing the British application to join the EEC in 1963 and 1967. As far as the US was concerned, the British membership of the EEC would reinforce the Atlantic alliance and support the US negotiation target of tariff-free trade with the EEC in the Kennedy Round.⁴⁰ Indeed, de Gaulle feared that the British presence in the EEC would be threatening the leading position of France and, most importantly, the British membership would give the Americans "a vote in the EEC".⁴¹ During a meeting in 1966, de Gaulle told the British Prime Minister Wilson, that France still did not know whether it would be possible for Britain to follow any policy distinct from that of the United States.⁴²

In 1965, France boycotted the meetings of the Council of Ministers due to clashing with its counterparts over the questions of a common agricultural policy and of establishing the EC's own resources and budgetary control. What France really protested about was not the unsatisfactory bargain in a common agricultural policy but the federal intention that the other five put through in the negotiation.⁴³ However, seven months later, to end the French "empty chair crisis", the Six

⁴⁰. For the EEC and the GATT see R. C. Hine, *The Political Economy of European Trade: An Introduction to the Trade Policies of the EEC*, pp. 78-81; for American perspective see Gary C. Hufbauer, *Europe 1992: An American Perspective*, (Washington, D. C.: The Brookings Institution, 1990), p. 5; also Gerald Meier, *Problems of Trade Policy*, p. 26.

⁴¹. See Buzan, et al., *The European Security Order Recast: Scenarios for the Post-Cold War Era*, p. 146; also Urwin, *The Community of Europe: A History of European Integration Since 1945*, pp. 120-125.

⁴². See Ben Pimlott, *Harold Wilson, (Biography)*, (London: Harper Collins Publishers, 1992), p. 441.

⁴³. For more details of de Gaulle's opposition to the five see Urwin, *The Community of Europe: A History of European Integration Since 1945*, pp. 107-113; the issue of the Parliamentary control of budget was the main quarrel between France and the five, see Pinder, *European Community: The Building of a Union*, pp. 12-13.

managed to regenerate integration momentum by reaching the Luxembourg Compromise (in which the French side asserted a right of veto in the Council whenever their important national interests are at stake, while the other five maintained their stand for the majority vote. This virtually amended the principle of majority voting introduced by the Treaty of Rome). This Compromise implied a step in the direction of increased national control over the EC, which was partly to be blamed for blocking further economic and political integration through approaches from transnational institution in the 1970s and 1980s. Despite the progress of European integration being deterred by political crises, in 1965 the Six still pushed through the Merger Treaty to converge three Communities as the European Community (implemented in 1967).

Soon after President Georges Pompidou took office after de Gaulle in 1969, European integration development entered the post-Gaullist era of optimism with more encouraging achievements. For example, as the new government of West Germany headed by Willy Brandt decided to go for the "Ostpolitik" (Eastern policy), in order to maintain West Germany's firm commitment to the Community Pompidou was urged to regenerate the momentum for further integration. In addition, the turbulence in the international monetary system, as it became apparent that the dollar and sterling were in deep trouble, jeopardised Europe's interests and stimulated the Six to further cooperation. Pompidou called for a meeting of the heads of government which brought about the Hague summit in 1969. The summit was an important turning point for European integration in that it cleared the way to the enlargement of the EC, met consensus on the development of common policies, reaffirmed ultimate goals for political

integration, and approved a systematic development of the EC's own resources.

Thereafter, up to 1973 the momentum of European integration was fuelled by the Davignon Report of the Commission for foreign policy cooperation,⁴⁴ and the Werner Report for economic and monetary union in 1970,⁴⁵ which encouraged the successful Treaty of Accession in 1972 between the EC and Britain, Ireland, Denmark and Norway (After the hard negotiation with the EC over the sensitive issue of fisheries, the Norwegians in a referendum rejected membership of the EC by 54 per cent votes against and 46 per cent for accession). Moreover, in 1972 the first summit meeting of the Nine in Paris with the participation of Britain, Ireland, and Denmark appealed for European union "to recognize clearly the unity of its interests, ...(and) to make its voice heard in world affairs",⁴⁶ as the EC became pursuing more independent foreign policy from of the United States.⁴⁷ Despite the Paris summit's further confirmation of the Commission as a partner of national governments rather than a supranational entity, the optimism of member states' consensus for European integration was raised to its peak.

⁴⁴. As stipulated in the Report "Being concerned to achieve progress towards political unification, the Governments should decide to cooperate in the field of foreign policy." Report by the Foreign Ministers of the Member States on the Problems of Political Unification (Davignon Report), adopted in Luxembourg on October 27, 1970, *Bulletin of the European Communities*, 11/1970, p. 11.

⁴⁵. Report to the Council and the Commission on the Realisation by stages of Economic and Monetary Union in the Community, (Werner Report), Supplement to *Bulletin of the European Communities*, 11/1970.

⁴⁶. The Opening Address by President Pompidou in Communique of the Summit Conference of the Heads of State of the New Europe in Paris, October 19-20, 1972.

⁴⁷. In the early 1970s there was an upsurge of popular movements in Europe opposed to US international policy. In particular they were hostile to the US involvement in the Vietnam War. See John Palmer, *Europe Without America: The Crisis in Atlantic Relations*, (Oxford: Oxford University press, 1987), p. 48.

2.2. 1973-1980: GLOBAL ECONOMIC RECESSION AND THE PARALYSIS OF EUROPEAN INTEGRATION

By 1973 the member states of the EC seemed to have reached a certain consensus on the necessity of pushing for further political and economic integration. Furthermore, the new French President Giscard d'Estaing and West Germany's Chancellor Helmut Schmidt shared in common the idea and objectives of summit meetings in the development of the EC and thus reinforced the axis of Franco-German cooperation which anchored the momentum of European integration. However, since the first oil crisis struck the world to the brink of recession in the winter of 1973-1974, the upheavals in international economic and political systems made the EC's member states hesitate to commit themselves further and so aggravated their policy differences from each other. As a result, international economic challenges to the EC became much more critical for European integration than the internal political processes. After the first enlargement of the EC, any further move forward political integration had actually been blocked by the dispute over keeping the costly CAP and the problem of budget contributions.

While the oil crisis brought about an attempt by Third World countries to create a new international economic order, the Organisation of Petroleum Exporting Countries (OPEC) began to challenge the West's economic dominance in the aftermath of the oil crisis.⁴⁸ The collapse of the Bretton Woods System of which fixed currency values had acted as a stable international monetary system, led to the onset of global economic recession. This collapse symbolised the relative

⁴⁸. Stephen D. Krasner, *Structural Conflict: The Third World Against Global Liberalism*, (Berkeley: University of California Press, 1985), p. 96.

decline of American hegemony in international economics. Western Europe now faced an economic challenge not only from Japan but also from the fast growing Asian NICs. At the end of the decade, when Western Europe fell into a period of industrial failure and economic depression, industrialists in association with politicians sought to complete a single market in order to revive industrial dynamics and economic strength - the engine of economic integration. They appealed for a return from regression against European integration and a renewed momentum for an improved economy.

2.2.1. The Change of the International Economic System and Euroclerosis

The late 1970s and early 1980s have been widely regarded as the apogee of Europessimism. It was not only because of the oil crises and the global economic recession, but also because of the declining competitiveness of European industry and of business confidence, and a new challenge of competition for market share from the Far East, Japan and the Asian NICs (ANICs).⁴⁹ West European economic performances were lagging far behind their principal rivals, the US and Japan, as well as the NICs to some extent.⁵⁰ The economic downturn facing the Europeans derived partly from their fragmented national markets with the various regulations set by different national governments, compared to the unified single domestic markets

⁴⁹. In terms of European industrial competitiveness, this new wave of competition began in the late 1970s, which was described as the third wave. In this, European economies were characterised by faltering economic growth different from the previous two waves of competition, e.g. differences in industrial productivity in the 1950s and technology gaps in the mid-1960s, in the context of growing economies. See Commission of the European Communities, "Completing the internal market for industrial products", Document, by Jacques Pelkmans, 1986, p. 34.

⁵⁰. See John Pinder, "Our Industrial Competitors And The management Gap: Europe, Japan, The NICs And The New Technologies", *Policy Studies*, V. 5, (July 1984).

of the United States and Japan.⁵¹ The Europeans were losing ground in high technology sectors to the US and Japanese producers on the one hand, and in some consumer goods' sectors to the relative low cost producers on the other.

Since the 1970s, the global political and economic system has been going through a dramatic change. Oil price rises came on top of the collapse of the Bretton Woods System in August 1971, when the United States unilaterally repudiated its commitment to exchange gold for dollars.⁵² Although American power was not in decline in absolute terms, the relative decline of its influence in economic and political arenas was incontestable.⁵³ The international system of bipolarity had begun running towards one of multipolarity. After the US loosened its control on the international monetary system, the shift to flexible exchange rates and the turbulence on the world energy market left the EC member states suddenly facing fluctuating exchange rates and an increase in their cost of production. As a result, the EC in 1979 launched the European Monetary System (EMS) to stabilize its member states' currency values. It was emphasised that a hegemony, either a power or a mechanism, was necessary to the stability of international regimes.⁵⁴ While the United States was unable to dominate the world economic system, the world economic order was therefore characterised by more of a multilateral than a bilateral

⁵¹. Such as "Europe's Technology Gap", *The Economist*, (24 November, 1984), p. 103.

⁵². Some studies have gone through the history of the Bretton Woods system in detail. See Joan Spero, *The Politics of International Economic Relations*, pp. 48-55; and Robert Gilpin, *The Political Economy of International Relations*, (New Jersey: Princeton University Press, 1987), pp. 134-142; as well as Blake, and Walters, *The Politics of Global Economic Relations*, pp. 74-79.

⁵³. Though some other studies disagreed with the argument of the decline of American power, such as Susan Strange's article "The Persistent Myth of Lost Hegemony" *International Organisation*, 41: 4, (Autumn 1987), Gilpin suggested that it will be more accurate to realise the decline in relative terms. See Gilpin, *The Political Economy of International Relations*, pp. 344-345.

⁵⁴. Robert Keohane, *After Hegemony: Cooperation and Discord in the World Political Economy*, (New Jersey: Princeton University press, 1984), chapter 2.

pattern, and preoccupation with more regional than global issues. These international factors together contributed to "Eurosclerosis" and so to the delay of European integration. While the EC was incapable of tackling external challenges collectively and effectively, individual member states resorted to their own national prescriptions.

The Energy Crisis and International Economic Challenges to Europe

During the 1970s, in terms of its political and economic power, America⁵⁵ was facing a relative decline. West Germany and Japan had successfully begun to challenge the US' domination in international markets. However, this challenge has not brought about a new political framework for the international economic system. The US might have withdrawn from shouldering economic management alone, but on the other hand, the EC and Japan were either unable to take charge or not inclined to do so.⁵⁵ For three decades since the end of the War, apart from its security dependence on the US, European prosperity had been deeply dependent upon the world political economy of "American-centred regimes", which rested on three set of benefits: a stable international monetary system, provision of open markets for goods, and access to oil at a stable price.⁵⁶ Under the American-centred regimes, Western industrialised countries were therefore able to enjoy cheap resources, fuel and raw materials.

⁵⁵. Gilpin argues that in the early 1980s Western Europe's poor economic performance made the likelihood of its being the leader of the international economic system improbable, and Japanese export-led trade structure, which is deeply dependent upon overseas markets and unlikely to open its domestic market to other trade partners, has resulted in its lack of qualification to become the leader. See Gilpin, *The Political Economy of International Relations*, p. 376.

⁵⁶. Keohane, *After Hegemony: Cooperation and Discord in the World Political Economy*, p. 139.

TABLE 2.3. CRUDE PETROLEUM: THE CHANGING STRUCTURE OF PRODUCTION (in percentage)

Country and Group	1955	1960	1970	1971	1973	1975
Developed economies	48.0	37.9	24.0	23.7	21.0	22.2
Developing countries	41.3	46.5	57.8	58.8	61.0	56.1
Planned economies	10.7	15.6	17.3	17.5	18.0	21.8
U S A	44.5	33.9	21.0	19.4	16.4	17.3
OPEC	36.2	41.0	51.4	52.6	55.5	49.7

Source: *World Economic Survey*, UN, 1975, p. 68.

During the first oil crisis in 1973-74, OPEC exerted a decisive control over the price and supply of oil and broke through the domination of the "seven sisters", international oil multinationals.⁵⁷ Developed countries shared 48 per cent of the crude petroleum market in 1955, but saw their share decline to 20 per cent in 1974, as a result of the rise of OPEC. (For changes in the share of the United States and OPEC refer also to Table 2.3). In the aftermath of the energy

TABLE 2.4. PRIMARY COMMODITIES IN SELECTION: CHANGES IN RELATIVE PRICES, 1970-1975

	index of commodity price relative to the unit value of manufactures (1960-1969 = 100)					
	1970	1971	1972	1973	1974	1975
petroleum	87.9	97.4	103.5	118.4	328.8	296.6
sugar	94.9	98.4	116.5	132.1	291.1	211.4
zinc	101.7	102.1	113.4	181.4	227.8	147.6
cocoa	107.5	79.9	86.5	138.3	172.5	120.5
tin	106.6	95.6	95.2	101.6	146.5	113.8
maize	99.9	92.7	87.8	122.4	135.5	103.3

Source: Information here was based on the United Nations, *Monthly Bulletin of Statistics*, and selected from *World Economic Survey 1975*, UN, p. 49.

crisis, in other major commodity markets producers at once attempted to raise prices by organising cartels, e.g. in the

⁵⁷. The "seven sisters" international oil companies were five American (Standard Oil of New Jersey, known as Exxon today, Standard Oil of California, Mobil, Gulf, and Texaco), one British (British Petroleum), and one Anglo-Dutch (Royal Dutch-Shell). Spero, *The Politics of International Economic Relations*, pp. 293-295.

markets for bauxite, bananas, and copper.⁵⁸ Consequently, as part of the Third World's "trade strategy", not only did oil prices go up dramatically,⁵⁹ but also the prices of non-oil energy products (refer to Appendix F-2.4)⁶⁰ and of other major commodities soared (Table 2.4). The upsurge in commodity prices between late 1972 and early 1974 was soon reflected in manufacturing costs, and further resulted in the high prices manufactures passed on in the following years (Compare petroleum per barrel prices in 1973 and in 1974, and wheat per ton in 1973 and in 1974, with the index number of export unit value of manufactures in the same period in Table 2.5).

TABLE 2.5. CHANGING PRICE RELATIONSHIPS: ENERGY, FOOD, AND MANUFACTURES, 1965-1975

YEAR	petroleum*	wheat**	manufactures***
1965	1.80	59.47	103
1970	1.80	51.61	117
1971	2.19	61.53	124
1972	2.47	69.78	134
1973	3.27	138.02	156
1974	11.58	164.97	186
1975	11.53	143.07	213

Note: * dollars per barrel

** dollars per ton

*** index of export unit value (1963=100)

Source: *World Economic Survey 1975*, UN, p. 48.

In Table 2.6, indices of non-fuel primary commodity prices display an upward trend from 1973 to 1985, which resulted in increasing prices of commodity exports of both

⁵⁸. Ibid., pp. 331-338.

⁵⁹. "For the industrial country group as a whole, the average price of petroleum products to end-users rose by 162 per cent from 1973 to the first quarter of 1979". See *World Economic Outlook*, IMF, (May 1980), pp. 74-75. In real terms, oil product prices increased by 58 per cent from 1972 to 1978; and from 1978 to 1980 petroleum products rose by 67 per cent. *World Economic Outlook*, 1981, p. 99.

⁶⁰. For industrial countries as a group, average energy product prices rose in nominal terms by 147 per cent from January 1973 to the first quarter of 1979. *World Economic Outlook*, (May 1980), p. 75. In real terms, energy as a whole in the period of 1972 to 1978 increased 48 per cent; the following two years energy prices raised 35 per cent. *World Economic Outlook*, 1981, p. 99.

industrial and developing countries. In terms of manufacturing prices, developing countries had a much better competitive position than industrial countries in most of the period recorded except for 1979. In other words, as far as trade is concerned, the price increases, which in industrial countries was much higher, in fact, did not result from the shortage of supply markets. (Rather, it was partly because of the resurrection of Third World consciousness that they could prevent their resources from being exploited by the developed countries, and partly because those developing countries supplying oil raised their political profile towards the West and made claims to play a major role in the management of their resources.)⁶¹

TABLE 2.6. INDICES OF NON-FUEL PRIMARY COMMODITY PRICES, 1970-1985

(1980 = 100)	in US dollars		deflated by prices of manufactures	
	DCs	ICs	DCs	ICs
1970	36.8	37.4	107.9	109.8
1972	36.1	41.1	92.7	105.7
1973	55.4	69.8	121.0	152.4
1974	71.4	80.4	131.3	148.0
1975	59.2	67.8	95.1	108.9
1976-79	82.8	77.3	109.9	103.2
1980	100.0	100.0	100.0	100.0
1982	77.4	82.1	83.4	88.5
1984	86.0	87.1	99.4	100.8
1985	75.4	76.2	86.8	87.8

Note: DCs: commodity exports of developing countries.

ICs: commodity exports of industrial countries.

Source: *World Economic Outlook*, IMF, (April 1986).

In the end, the high profile that the developing countries took, led in 1974 to demands for movement towards a

⁶¹. Caroline Thomas, *In Search of Security: the Third World in International Relations*, (Brighton: Wheatsheaf Books, 1987), p. 76.

new international economic order in order to push forward a new international commodity regime in accordance with developing countries' interests.⁶² Meanwhile, in the EC, the rising price of raw materials on which industrial growth was based resulted in the increase of production costs and further caused rises of prices to consumer's.⁶³ (The EC's annual increase rates in consumer prices accounted for 8.4 per cent

TABLE 2.7. THE GROWTH RATE OF REAL GDP IN THE EC, USA AND JAPAN (percentage)

	1960/70	1972	1973	1974	1975	1976	1977	1979
EC	4.6	4.0	6.0	1.6	-1.6	5.0	2.3	3.1
USA	3.8	5.8	5.4	-1.3	-1.0	3.5	4.9	1.5
Japan	10.7	8.9	9.8	-1.0	2.4	6.0	5.4	5.7

Source: Eurostat.

TABLE 2.8. THE EC GROSS FIXED CAPITAL FORMATION IN VOLUME TERMS (average annual growth rate in 1970 prices)

	1960-70	1970-73	1973-76	1976-78
	5.7	3.9	-1.8	1.9

Source: Commission of European Communities, "Changes in industrial structure in the European economies since the oil crisis", *European Economy*, special issue, 1979.

TABLE 2.9. THE EC PRIVATE CONSUMPTION IN VOLUME (average annual growth rate in 1970 prices)

	1960-70	1970-73	1973-76	1976-78
	4.6	4.6	2.2	2.8

Source: as Table 2.8.

in 1973, 13.4 per cent in 1974 and 12.8 per cent in 1975). The increase in inflation brought the EC a slowdown in economic

⁶². The NIEO was also carrying a hope of developing countries to adjust the North-South economic relationship. *Ibid.*, p. 78.

⁶³. In 1974 and 1975, wages in the EC countries were increased to keep up with the direct inflationary effects of the oil price increase. See Commission of European Communities, "Annual Economic Report 1979-1980", 4, (November 1979), p. 32.

growth (see Table 2.8, also Appendix T-2.1, T-2.2, T-2.3, and T-2.4), rising unemployment rate,⁶⁴ increased tension in industrial relations, declining investment (Table 2.8), weak demand (Table 2.9) and a continual decline of business confidence following the substantial loss of comparative advantages inside and outside domestic markets.

The crisis facing European industry can be mainly attributed to exogenous factors which diminished its comparative advantage in industrial products over its rivals. The ageing European industrial structure could not keep pace with the new wave of challenges, such as the increasing price of energy and raw materials, higher costs of industrial production, the need to increase R & D investment in innovative products for staying competitive, and the need to increase spending on a higher standard of pollution control. For example, the Chairman of Rank Xerox (UK), Derek Hornby, recorded that by the time of the outbreak of the first oil crisis Rank Xerox was highly profitable and successful. It was the 1973 oil crisis and the change of regimes in business competition from new Far Eastern rivals with their low manufacturing costs which upset its leading market share for the rest of the 1970s.⁶⁵

In fact, up to the early 1980s, some European countries, such as West Germany and Britain, had performed remarkably in industrial restructuring to revive their economies in the face of external challenges.⁶⁶ In private sectors, many firms had

⁶⁴. The EC9 accounted for 2.7 per cent unemployed people of total civilian labour force in 1973, 4.0 per cent in 1975, 5.0 per cent in 1979 and 9.1 per cent in 1983, for details refer to Appendix T-2.5. The information for the nine EC countries based on Eurostat do not include Greece, Spain and Portugal.

⁶⁵. Rank Xerox's market share at this time was reduced from 90 per cent to about 45 per cent. See Hornby, "Can we teach ourselves to change?", *The Royal Bank of Scotland Review*, 151, (September 1986), p. 15.

⁶⁶. West Germany successfully adjusted its industrial structure to face up to competition in the early 1970s. See "Changes in industrial structure in the European economies since the oil crisis 1973-78", *European Economy*, Special issue, (1979), p. 79. The Conservative

survived from the general economic slowdown of the 1970s by carrying out radical restructuring processes. For example, Philips, the Dutch multinational enterprise, which restructured the character of its industry by trimming off its scattered overseas factories, had successfully improved their competitiveness in countering strong industrial rivalry.⁶⁷ After re-organising its management team, shedding excessive work force and raising capital, Italian Olivetti survived from recession and became Europe's biggest office automation and data processing group in the early 1980s.⁶⁸

Changes in The International Monetary System

When President Nixon of the United States unilaterally announced the end of the convertibility of US dollars to gold in August 1971, the Bretton Woods System on which the stable monetary system and most industrial countries were dependent came to an abrupt end. Following many efforts and tedious negotiations among the Group of Ten, mainly on whether the other industrial countries' currencies should be revalued relative to the dollar or whether the dollar should be devalued straight away,⁶⁹ a compromise brought about a system

government in Britain in the 1980s set a new industrial policy to transfer control of nationalised industry sectors to private ownership, and at the same time to liberalise the market through competition, as well as to reduce the powers of public sector unions. Christine M. E. Whitehead, "Experience With Privatisation in Britain", in Keith Cowling and Horst Tomann, (eds.), *Industrial Policy After 1992-an Anglo-German perspective*, (Anglo-German Foundation for the Study of Industrial Society: London, 1990). For the details of privatisation in other OECD countries, see Barrie Stevens, "Prospects for privatisation in OECD countries", *National Westminster Bank Quarterly Review*, August 1992.

⁶⁷. In Europe alone Philips closed 40 factories by 1986. Huge and unprecedented lay-off plans were considered necessary to the industry for competitiveness. See Graham Turner, "Inside Europe's Giant Companies: Cultural Revolution at Philips", *Long Range Planning*, 19: 4, (1986).

⁶⁸. Since Carlo de Benedetti was recruited as the CEO of Olivetti in 1978, Olivetti had the entire first-line management removed and 14,000 workforce cut. He has turned the company into the biggest player in Europe. See Graham Turner, "Inside Europe's Giant Companies: Olivetti Goes bear-hunting", *Long Range Planning*, 19: 2, (1986), pp. 13-15.

⁶⁹. The Group of Ten: Belgium, France, Germany, Italy, the Netherlands, Sweden, Canada, Japan, the United Kingdom, and the United States. Joan Spero, *The Politics of International Economic Relations*, p. 46.

of exchange rates by bargaining between different currencies. The United States faced a balance of payment deficit in the 1970s. As many economists believed that it could be amended by a devaluation of the dollar or realignment with other currencies, the American government was trying to push the idea as a part of its policy, known as the Nixon Doctrine, to reduce international burdens. Nevertheless, most other industrial countries with either a large amount of dollar holdings or with balance of payment surplus were reluctant to press ahead with a realignment or a domestic adjustment between their currencies and the dollar, even though the dollar was actually at risk.

In the 1960s, as far as the EC was concerned, exchange rate adjustments were the major factor influencing the Customs Union and the CAP.⁷⁰ Following continuing US current account deficits in the first half of the 1970s, divergence in economic performances appeared dramatically inside Europe where inflation increased sharply. In five of the EC countries, inflation rates were well above 20 per cent.⁷¹ Owing to the increasing intra-EC trade flows, the members of the EC with experience of the CAP, based on common prices and relying on stable exchange rates, found themselves in an awkward position to cope with the monetary turbulence. In particular, those industries dependent on exports either to EC neighbours or to other trade partners suffered from a great uncertainty in prices. There was an early transitional exchange rate mechanism, the "snake", derived from the Werner Report of 1970.⁷² The idea of establishing an optimum currency area to

⁷⁰. For details of the development of European monetary matters and the exchange rate effect to the CAP see Daniel Gros, and Niels Thygesen, *European Monetary Integration: From the European Monetary System to European Monetary Union*, (London: Longman, 1992), pp. 9-15.

⁷¹. Ibid., p. 25.

⁷². The "snake" from 1972-1978 was initially known as the "snake in the (dollar) tunnel". The margin of bilateral fluctuations against the US dollar were agreed at 4.5 per cent, \pm 2.25. For the detailed development of the "snake" see Gros, and Thygesen, *European Monetary Integration*, pp. 15-24.

stabilise exchange markets re-emerged as the main topic on the EC agenda in terms of integration.

Most European industries' experience was of dramatically waning price competitiveness due to volatile currencies. For example, the international price competitiveness of the UK mechanical engineering industry deteriorated simply because the rapid appreciation of sterling resulted in the average price of machinery exported from the UK being increased by about 10 per cent.⁷³ From 1975 to 1979 British mechanical engineering industry's productivity (output per employee) rose by only 4 per cent. Over the same period, productivity (value added per employee) of the West German mechanical engineering industry increased by 15 per cent, about 50 per cent higher than the UK's. That of Japan surged ahead by 52 per cent.⁷⁴ In general, British industry in most of the 1970s was afflicted by lower productivity and higher costs. While productivity of British industry's annual growth rate fell from 6.5 per cent in 1973 to 0.3 per cent in 1974, -0.4 per cent in 1975, 0.4 per cent in 1979 and -4.2 per cent in 1980, its labour cost per unit of output increased dramatically from 7.0 per cent in 1973 to 22.2 per cent in 1974, 33.6 per cent in 1975 and 23.3 per cent in 1980.⁷⁵ The appreciation of sterling further worsened its competitive position in world markets. As a result, it suffered a loss of market share. The relationship between exchange rates and industry was critical to industrial survival. For instance, relative unit export values in national currencies and in dollars produced a different competitive position in different countries. In national currency terms the USA, Germany, Switzerland and Japan

⁷³. M. W. Henry, "The competitiveness of the UK mechanical engineering industry: The effects of fluctuating exchange rates", *Barclays Review*, 56: 2, (May 1981), p. 36.

⁷⁴. *Ibid.*, p. 38.

⁷⁵. Changes from 1974 to 1981: UK industry's productivity rose only 1.2 per cent, while the average EC's increased 2.9 per cent; UK industry's labour cost increased 16.9 per cent, while the average EC's grew 10.5 per cent. Information is based on Eurostat from Commission of European Communities, *European Economy*, 10, (March 1982).

improved their competitive position in 1982-1985 (see Appendix F-2.5). However,

"the disruptive effects of unstable exchange markets and especially the problem of the weak dollar led to political support for a new European initiative to fix rates within the EEC."⁷⁶

For the Europeans, the establishment of a common monetary system with fixed exchange rates would mean that the Europeans could avoid the costs of converting one currency to another within EC markets. Thus, in July 1978 the heads of the EC countries in the European Council agreed to "a scheme for the creation of closer monetary cooperation leading to a zone of monetary stability in Europe."⁷⁷ The EMS was a system with: firstly, fixed exchange rates among the members and a floating rate with the outside world; secondly, the creation of a European Currency Unit (ECU) which is a basket of EEC currencies serving as a basis for fixing exchange rates; and, thirdly, a network of credit arrangements and plans for a future European Monetary Fund for financing payment imbalances and supporting the fixed rates.⁷⁸

2.2.2. A Return from The Regression of European Economic Integration

As the previously stable international political and economic framework that European countries had taken for granted began to dissolve, European countries realised that

⁷⁶. Spero, *The Politics of International Economic Relations*, p. 68.

⁷⁷. "Resolution of the European Council of 5 December 1978 on the establishment of the European Monetary System (EMS) and related matters", *Bulletin of the European Communities*, 12-1978, p. 10.

⁷⁸. Spero, *The Politics of International Economic Relations*, p. 68.

their original consensus for integration had failed to provide a political and economic framework in Western Europe capable of addressing the crisis. Further, the global recession almost resulted in the collapse of the consensus. Williams has noted how "global economic conditions were making government more protective, and the road to integration had become far more difficult."⁷⁹ European Industrialists therefore appealed for a higher level of economic integration to be achieved in order to face up to the external challenges arising from recession. Although the late 1960s' optimism about integration was unable to protect member states' common interests from global recession, it was not the case that the faith was completely lost in the capacity of West European integration to survive such problems in the future. The EC seemed to lack flexibility and accountability to respond to the changing global economic conditions on behalf of its member states, because the essential limitation of intergovernmentalism on regional integration itself easily choked off any common policy towards external issues, especially those which contended with national trade policy. Conversely, the limited extent of West European integration showed that a large scale of regional solidarity was necessary to meet external challenges. Etienne has noted that "the maintenance of a common position with regard to external development became a favourite method of strengthening internal cohesion."⁸⁰

As national governments began to move towards protectionism, individual member states appeared determined to follow their own national policies to address the effect of the oil crisis at the expense of others' interests. Moreover,

⁷⁹. Williams, *The European Community - The Contradictions of Integration*, p. 51.

⁸⁰. Henri Etienne, "Community Integration: The External Environment", *Journal of Common Market Studies*, 18: 4, (June 1980), p. 298.

to control the EC development, the Giscard-Schmidt approach of European integration favoured intergovernmental cooperation rather than transnational institutions. This regularised the practice of summitry into the European Council in 1974. (France and West Germany were wary of the Commission getting too powerful and pushing integration too far). The function of the powerful Council was to set "new targets and lay down the guidelines for future progress, modify or abandon existing programmes, and resolve disputes between the members at the highest level."⁸¹ Thereafter, as the Council was influential at the heart of the EC but remained outside the EC framework, the EC had actually become an intergovernmental organisation with decision-making taken by way of continual bargaining in the Council, which was not based on a sense of European interest but of individual national interests. (The European Council received its legal recognition within the EC framework only when the Single European Act was adopted.)

During this period, EC members may claim some credibility for harmonising their political and economic stand in international affairs, such as organising the Conference on Security and Cooperation in Europe in 1975 and in international trade negotiations. It did not mean that individual member states would willingly commit more to the Community. Rather, economic integration was hampered by the rise of national protectionism. Despite working hand in hand for the Common Market, in the face of external challenges individual member states retained their trade barriers against the exchange of goods, personnel, and services against each other. In terms of building-up a transnational community, there was little to be credited in progressive integration.

⁸¹. Urwin, *The Community of Europe: A History of European Integration Since 1945*, p. 175.

Summitry intergovernmental cooperation could well stir up political reasons for national protectionism. From 1975 to the mid-1980s, the agenda of summit meetings was fully occupied with the quarrels of reforming the CAP and the prolonged British complaint of its excessive contribution to the EC budget. In particular, after Margaret Thatcher became the British Prime Minister in 1979, she tried to argue the issue of the CAP and its budgetary complaint together, while her European partners preferred to see them as separate. As a result of internal political entanglements within the EC, no promising progress towards integration was made during this period except for the establishment of the European Monetary System.

Facing the new international economic setting, European political elites and industrialists realised that they were not likely to keep their superiority, or even to survive from the competition, unless they could work together. Despite industrial restructuring they were still not able to compete with their main trade partners, the United States, Japan and the NICs to some extent, because their counterparts had factor advantages of either market scale or lower costs of production and strong productivity with which the fragmented European markets could not compete. It seemed that merely restructuring individual industries was not an absolute guarantee of staying competitive since the international business setting was undergoing a great revolution in respect of its structure and market formation.⁸² What more the EC could do was to seek for industrial cooperation at European level and the completion of

⁸². For example Japanese enterprises' lean techniques were not only reducing the large proportion of labour by automation but also effectively eliminating the cost of production by specialising the network of factories and standardising their products. Japanese swift variable cost of production (wage) to fixed cost (equipment and machinery), specialise the function of each factory within their management network and create "Flexible manufacturing systems". See "Can Europe compete?", *Fortune*, (December 2, 1991), pp. 50-51. As a result, the industry lowers the cost of production, increases profits, and promotes industrial efficiency. See "Jobs and technology", *The Economist*, (March 24, 1984), pp. 67-68.

the internal market. While internal political stalemate thwarted any forward step of European integration, there was increasing dissatisfaction with the European "uncommon market" from the grass-roots voice of the business community calling for European industrial collaboration and market integration. Many European industrialists and politicians looked increasingly favourably towards the establishment of a single European market in order to strengthen European industrial competitiveness by taking advantage of scale economies.

For example, Wisse Dekker of Philips, Carlo de Benedetti of Olivetti, the Italian office-machinery maker, Helmut Maucher of Nestlé, the Swiss food giant, and Dieter Spethmann of Thyssen, the West German steel maker, believe that "becoming big in a big internal market is the only way to stay internationally competitive."⁸³ In the case of Philips, it experienced a slipping share of world markets, so "Philips's trading profits dwindled from 9 per cent of annual sales in 1974 to 4 per cent in 1980".⁸⁴ Dekker complained that for Philips the most galling obstacle to becoming more competitive was Europe's uncommon market which "denies Philips the big, open domestic market that gives American and Japanese competitors such a strong launching pad into world markets."⁸⁵ Similarly, Fabrizio Galimberti, Chief economist of Fiat, points out baldly that "Potential economies of scale were not being realised because political realities and the segmentation of European markets prevented rationalisation of supply."⁸⁶ Robin Biggam, the Chief Executive Officer (CEO) of BICC Plc, the UK largest road builder, states that:

"the creation of an effective Common Market in Europe could of itself reverse the trends of this century when firstly the US and latterly Japan achieved a much higher

⁸³. "European Co-operation: Bosses want the common market Brussels never built", *The Economist*, (May 26, 1984), p. 75.

⁸⁴. *The Economist*, (January 5, 1985), p. 66.

⁸⁵. *Ibid.*, p. 67.

⁸⁶. Galimberti, "Getting Fiat back on the road", *Long Range Planning*, 19: 1, (1986), 25.

rate of growth than Europe, and this represents the opportunity of Europe to us as industrialists."⁸⁷

Urging a common industrial strategy, the Chairman of the French electronics giant Thomson International, Jean Caillot, stresses that:

"Europe must be much more than a Common Market. Europe must be a genuine economic Community capable protecting the social advantages This status can only be achieved with a powerful European industry based on a common industrial strategy that will guarantee Europe's competitiveness on the whole market."⁸⁸

Apart from the big corporations demanding integration, other businessmen were also very eager to see a "genuine" common market. For instance, according to the Institute of Directors, a London based professional association for company directors: "British Business was growing enthusiastic for using the EC as a vehicle for economic recovery" and agreed that the targets of the common market should be speeded up by the end of 1988.⁸⁹ Moreover, when Jacques Delors presided over the meeting of the European Commission in early 1985, he pointed out that "it was easier to tackle problems collectively than individually. There were multiplying effects over and above what one country could do on its own."⁹⁰ Earlier, Britain and Italy had agreed "on the need to push the EC forward into a new phase of industrial integration that will enable Europe to compete effectively with America and Japan in new technology".⁹¹ To create a genuine internal

⁸⁷. International Business Intelligence, *1992-Planning for the Engineering Industries*, (London: Butterworth & Co Ltd. and Eurofi Plc., 1989), p. 433.

⁸⁸. Based on a presentation at the Financial Times Conference: World Electronics - Europe's Role in an International Industry, London 26-27 April, 1989, See *Ibid.*, p. 418.

⁸⁹. "UK institute calls for 'genuine' common market", *Financial Times*, (1 April, 1985), p. 2.

⁹⁰. *The Times*, (8 January, 1985), p. 6.

⁹¹. "EEC 'needs industrial unity' to match competitors", *The Guardian*, (20 October, 1984), p. 4; also *British Business*, (26 October, 1984), p. 313.

market, Helmut Kohl, the Chancellor of West Germany, argues that "We must also encourage the convergence of our national economies. We should also make greater use of the opportunities for industrial cooperation than in the past."⁹² One European People's Party's study on the recovery of the European economy stated that:

"Europe's inability to apply technological advance to the dissemination of innovations in both new and traditional products and production processes is becoming fully apparent. This is the most serious aspect because it will have repercussions for the future. It cannot be allowed to get worse and can most easily be counteracted only on a Community scale."⁹³

It seemed that in the face of increasingly intense external challenges, the campaign for a single market became widely realised as a way of bringing about economic strength. This generated the momentum for a renewal of European integration as a result.

2.3. 1980-1992: INDUSTRIAL COMPETITION AND THE IMPETUS FOR THE RELAUNCH OF EUROPEAN INTEGRATION

The prolonged economic stagnation and relative industrial decline in the EC during the 1970s and 1980s had gradually resulted in the loss of European industrial competitiveness in international markets to the US, Japan, and more strikingly the NICs. Information in Table 2.10 suggests that while nine major world economies (including four major EC economies) decreased their world market share, in terms of GDP, from 72.1 per cent in 1963 to 68.7 per cent in 1983, the NICs steadily

⁹². *The Times*, (18 January, 1985), p. 7.

⁹³. Emilio Colombo, "The Economics Recovery of Europe", *European Digest*, 50, (May 1985), p. 11.

expanded their share from 3.5 per cent to 6.2 per cent in the same period. With respect to exports of manufactures, the NICs' market share grew much more impressive from 1.9 per cent in 1963 to 8.7 per cent in 1983.

In terms of competition in technology development, the EC industries felt very vulnerable in competing with Japanese and American industries both in the EC markets themselves and in world markets. Furthermore, while all industries had faced strong cost-cutting competition in the early 1980s, the EC was unable to meet the challenge of the

TABLE 2.10. SOME INDUSTRIAL COUNTRIES AND THE NICs' SHARE IN WORLD MARKET ECONOMIES (per cent)

1. Gross Domestic Product (at constant 1975 prices)						
	1964	1973	1978	1980	1981	1983
G9 ^a	72.1	70.6	69.1	68.2	68.5	68.7
NICs6 ^b	3.5	4.7	5.6	6.1	6.3	6.2
2. Exports of Manufactures (at current prices)						
G9	74.6	71.8	71.6	70.5	70.8	69.0
NICs6	1.9	4.3	5.6	6.6	7.7	8.7

Note: ^a. G9: Australia, Canada, France, W. Germany, Italy, Japan, Sweden, UK and US.

^b. NICs6: Brazil, Mexico, Hong Kong, S. Korea, Singapore and Taiwan.

Source: Based on the UN information from OECD, *The Newly Industrialising Countries: Challenge and Opportunity for OECD Industries*, Paris, 1988.

NICs in many major industrial sectors, such as electronics, textiles and clothing, and steel. For the period from 1970 to 1985, the import penetration ratios of four major EC economies by the NICs increased significantly in all manufacturing products, and in textiles and electricals, in particular (Table 2.11). A European trade deficit and industrial failure were brought about as a result. In addition, trade development between the EC and the NICs from 1980 to 1987 was not

balanced. The trade deficit of the EC against the NICs had deteriorated from ECU 2.9 billion in 1980 to ECU 6.7 billion in 1987 in manufactured products, which implied that the NICs' exports had dramatically increased market penetration in most major European industrial sectors.

TABLE 2.11. IMPORT PENETRATION RATIOS: total NICs, 1970 and 1985

eco./era	Total Manu.		Textiles ^a		Electricals ^b		Radio & TV ^c	
	1970	1980	1970	1980	1970	1980	1970	1980
France	0.15	0.79	0.11	2.08	0.01	0.73	0.06	2.39
W Germany	0.38	1.40	1.33	7.96	0.04	1.32	0.38	5.36
Italy	0.27	0.91	0.34	1.18	0.07	0.52	0.40	3.91
UK	0.41	1.42	2.10	7.74	0.14	1.15	0.37	4.11

Note: ^a. Textiles, Clothing, leather and footwear

^b. Electrical machines & appliances

^c. Radio, TV and communication equipment

Source: As Table 2.10.

In terms of trade structure, the EC was more dependent on imports of strong-demand industrial sectors - such as electrical equipment and electronics, information technology, automated office equipment and chemicals and pharmaceuticals - than were the US and Japan. In 1983, among total industrial imports the EC's imports of strong-demand sectors accounted for 29.8 per cent, while the US' and Japan's accounted for 27.0 per cent and 26.2 per cent respectively.⁹⁴ In terms of trade in high-technology products which will determine the future of industry and the economy, the EC's share of exports of high-technology products suffered an insufficient increase from 23 per cent in 1963 to 24 per cent in 1981, while the US increased from 29 per cent to 33 per cent and Japan jumped

⁹⁴. Commission of European Communities, "Competitiveness of European industry: situation to date", by Pierre Buiges, and Philippe Goybet, *European Economy*, 25, (September 1985), p. 22.

from 16 per cent to 38 per cent in the recorded years (Table 2.12).

TABLE 2.12. SHARE OF EXPORTS OF HIGH-TECHNOLOGY PRODUCTS IN TOTAL MANUFACTURED EXPORTS

	1963	1970	1981
EC10	23	22	24
USA	29	28	33
Japan	16	25	38

Note: EC10 does not include Spain and Portugal.

Source: Commission of the European Communities, *European Economy*, 16, (July 1983), p. 126.

TABLE 2.13. SPECIALISATION INDICES IN TRADE IN HIGH-TECHNOLOGY PRODUCTS

	1963	1970	1978	1981
EC10	1.01	0.94	0.88	0.87
USA	1.27	1.18	1.27	1.19
Japan	0.72	1.07	1.27	1.37

Source: As Table 2.12.

In addition, counting on specialisation indices in trade in high-technology products the EC declined from 1.01 in 1963 to 0.87 in 1981. Conversely, the US managed to retain roughly the same levels (from 1.27 to 1.19) and Japan increased from 0.72 to 1.37 (Table 2.13). Above all else, in the field of electronics and information technology, Europe was incapable of competing with the US and Japan in high-technology development. Although "a weakness in electronics technology has often been seen as the reflection of a more general weakness in the development and exploitation of new and unfamiliar technology", some acknowledge that "Eurosclerosis" probably has little to do with any general lack of

technological and entrepreneurial dynamism.⁹⁵ It then seems to point towards general policy problems within the EC.

In the political arena, from 1974 to 1985, while the European integration movement was on the intergovernmentalist track, the European Council emphasised intergovernmental cooperation through negotiation rather than transnational institutions. European integration was therefore characterised by the performances of summit meetings. It was clear to see that the conflict of national interests became inevitable in this intergovernmental cooperation. The British complaint about its excessive budget contribution to the EC and the costly CAP damaged the effort of the Ten (with Greece gaining access to the EC in 1981) in seeking further integration. Following the leaving of Roy Jenkins, an able President of the Commission in 1981, Giscard and Schmidt also left the political scene soon after. While the new French President, François Mitterrand, and the West German Chancellor, Helmut Kohl, did not yet reach the cosy Franco-German partnership that had characterised the Giscard-Schmidt era, Mrs Thatcher became the dominant political personality of the EC.⁹⁶ The Genscher-Colombo Plan of 1981 appealing for more EC common policies and of the Stuttgart summit of 1983 was undermined partly because of Britain's recalcitrant attitude towards negotiation of the proposed EC budgetary system. (The Genscher-Colombo Plan was not welcomed by the European Council, because the initiative suggested that the role of EC institutions should be made more explicit including formalising the Council, and the EC budget would have to increase.) Many academics and politicians shared a sense of

⁹⁵. See Pari Patel, and Keith Pavitt, "Is Western Europe losing the technological race?", *Research Policy*, 16, (1987).

⁹⁶. Urwin, *The Community of Europe: A History of European Integration Since 1945*, p. 225.

alarm and urgency about the EC in the early 1980s, as the EC ran into stagnation and crisis in both politics and economics.

The EC's institutions and its member states gradually realised an urgent need to steer the EC away from Eurosclerosis through various down-to-earth programmes of industrial collaboration. Against this context of political stalemate and economic weakness, since 1980, there have been two unprecedented trends developing which have greatly influenced the progress of European integration. Firstly, successful experiments of Europe-wide industrial collaboration have shown a critical step in defusing external challenges and thus increasing industrial competence. While the European Council struggled with national interests, the Commission proposed plans for industrial collaboration in the hope of promoting European industrial strength in technology development and market cooperation. It was presumed that European industrial collaboration would lead to the establishment of a European technological community and further generate momentum for the completion of the internal market. In 1980, the industry Commissioner, Vicomte Davignon, appealed to European industrialists for inter-Europe industrial cooperation under the ESPRIT programme in order to promote their development of technology and thus strengthen their common international market competitiveness. The ESPRIT programme appears to serve dual needs: "to reduce the costs, risks and uncertainties of knowledge production and to secure a wider market through standardisation into co-operation among EC firms."⁹⁷ The success of the ESPRIT further inspired the second EC programme "Research for Advanced Communications in Europe" (RACE) and led to immediate demand for the ESPRIT II.

⁹⁷. See Mytelka, and Delapierre, "The alliance strategies of European firms in the information technology industry and the role of ESPRIT", p. 147.

The development of these high-technology programmes has significantly resulted in the development of "corporate networks" in Western Europe.⁹⁸ The consensus on building up mutual industrial strength which would depend upon the advantage of a wider single market became more widespread.

Secondly, to echo this European scale of industrial collaboration, European industrialists teamed up with the Roundtable to address their demand to the EC and their governments for a single European market on which future industrial development is highly dependent. Unlike the existing European interest groups, e.g. the UNICE, the European Trade Union Confederation and the Committee of Professional Agricultural Organisations which lobby the EC for their specific sectors of interest,⁹⁹ the industrial alliance amongst the largest enterprises throughout Western Europe has focused more on overall economic improvement and on the implications of European integration for industry. The emergence of the industrial alliance has boosted the industrialists' campaign for a single European market. The impetus for the renewed interest in European integration partly derived from the efforts to solve the problems and concerns of European industry. The relaunch of European economic integration was triggered, to a large extent, by industrial interests in accordance with overall European economic interests. Increased integration would construct European industrial strength in order to face up to intense industrial competition worldwide.

⁹⁸. Albert Bressand and Kalypso Nicolaidis, "Regional integration in a networked world economy", in William Wallace, (ed.), *The Dynamics of European Integration*, (London: Pinter Publishers for the Royal Institute of International Affairs, 1990), p. 43.

⁹⁹. The main function of those interest groups was to exchange information between member states and to collect and pass on information between affiliates and EC institutions. See Emil Kirchner, and Konrad Schwaiger, *The Role of Interest Groups in the European Community*, (Aldershot, Hants.: Gower, 1981), p. 16.

Since 1984, the impetus for the relaunch of the EC has become energetic because:

"the European Community entered a particularly dynamic phase in its development; common concerns were translated into common goals, and institutional and constitutional reforms were put in place. The pressures for reform in the Community showed that intergovernmentalism had its limits. Institutional reform would have to go beyond the limits of intergovernmentalism."¹⁰⁰

In 1984, President Mitterrand tried to reassert France's credibility of leading the EC by pushing through the resolution of Britain's budget complaint, the CAP's reform and the enlargement in the Fontainebleau summit. In addition, as persistent external economic challenges and industrial competition remained an agenda at issue, efforts for the renewal of European integration have further stepped up the new prospects for European political integration. Within the EC, internal political manoeuvres settled the prolonged disputes owing to the fact that the completion of the single market would serve ~~for~~ Europe's best interests in coping with external challenges. Thereafter, European integration has returned to driving for transnationalism, as the institutional reforms approved in the SEA have encouraged the campaign for the single market.

The collapse of communism in Eastern Europe in 1989 and the political disintegration of the former Soviet Union in 1992 have stimulated new momentums for the EC "widening" integration eastward. To make sure that the post-communist East European countries do not reverse the past mistakes and are driving towards the West's market-oriented form, the EC has committed itself in principle to allow the East Europeans /^o

¹⁰⁰. Brigid Laffan, *Integration and Co-operation in Europe*, (London: Routledge, 1992), p. 55.

gain access to the EC.¹⁰¹ For sound economic reasons, the East Europeans' low-cost industrial production would shield the EC from low-cost East Asian rivals, which has encouraged more firms to establish an industrial division of labour across Europe.

2.4. CONCLUSION: EXTERNAL INCENTIVES AND EUROPEAN INTEGRATION

Throughout the course of European integration, external incentives, like internal political and economic factors, have played a critical part. During the 1950s, the bipolar international political system left the war-torn Western Europe little option but to tie into the Atlantic Alliance from which European integration was generated. For political reasons, European integration was encouraged by the United States as a means of strengthening its global strategy to contain the Soviet Union. In the 1960s, international monetary turmoil caused by the troubled US dollar, American industry's penetration in Western Europe, and increased trade disputes between the EC and the US about agricultural exports, brought about the impetus for further economic and monetary integration in the EC. As the US in 1962 called for an Atlantic partnership to sort out trade problems, this incentive led the EC to move to further economic integration, e.g. the establishment of the CAP.

Global recession and two oil crises in the 1970s greatly struck European economies and the progress of European

¹⁰¹.According to the German proposal, the six East European countries, Czech Republic, Hungary, Poland, Slovakia, Romania, and Bulgaria have been given the year 2000 as a target to be in the EC. See *The Economist*, (10 September, 1994), p. 23. The EU has invited these six countries to attend regularly its meetings of ministerial councils and summits. See *The Daily Telegraph*, (6 October, 1994), p. 18.

integration. European industrial failure and poor economic performances led to the period of Eurosclerosis. The progress of pursuing the Common Market was halted, as many member states of the EC turned to protect their own "national champion" industries. Fierce industrial competition coming from the US, Japan, and the NICs, challenged the EC in terms of industrial productivity, technology development, and market sharing. The completion of the Internal Market Programme for which industrialists have campaigned, became not only the means of the EC's economic salvation but also the motor for European economic and political integration.

To summarise the role of external incentives, in the 1950s international superpower politics stimulated Western European countries to explore the possibilities for political integration. In the 1960s, European integration was influenced not only by changes in the international political system, but also by attempts to liberalise the world trade regime and by the weakness of the international monetary regime. After the first oil crisis, instead of political motives taking the lead, economic recession and industrial competition became decisive influences in the progress of European political and economic integration. Accordingly, the EC was counting on the process of industrial development to cope with external challenges. While the EC was beset by political disputes over the British budgetary contribution from the late 1970s to 1984, intense competition globally in industry and technology development where the EC lagged behind its rivals, generated renewed momentum for the establishment of the single European market. That has since helped to set forward the progress of European integration.

CHAPTER THREE

INDUSTRIAL RESTRUCTURING AND BUSINESS SUPPORT FOR THE RELAUNCH OF EUROPEAN INTEGRATION

This chapter seeks to demonstrate the importance of industrial development for an understanding of economic and political integration by focusing upon the role played by industrialists in Western Europe in the drawing up of the Single European Act (SEA). By supporting this process, industrialists played an instrumental role in the relaunch of European integration. The first section analyzes the relationships between European industry and the progress of political and economic integration, and the impacts of external incentives on the process towards industrial unity since the beginning of European integration in the early 1950s. The second section examines why European industries facing the economic crisis of the 1970s combined multinational interest groups to lobby Brussels and how the failure of European industry in international competition became an issue in the process of economic integration. The general realisation that European industries were losing competitiveness in terms of production, markets and the development of technology has generated the impetus towards industrial unity and further economic and political integration. Therefore, the last section focuses on European industrialists' involvement in the process of negotiations which contributed to the drawing up and passage of the SEA.

In terms of the relaunch of European integration, the SEA and the completion of the Internal Market programme were the EC's two major events of the mid-1980s.¹ It is important to

¹. For discussion of the Rome Treaty about the Common Market, and the SEA about the Single Market that sets a new target of European integration by 1992, see Jacques Pelkmans,

note that the SEA has resurrected the hope for and brought forward the momentum for European integration. Students of regional integration have optimistically claimed that "neofunctionalism ought not to be considered dead! It seems to have retained explanatory power."² When studying the dynamics of the 1980s' relaunch of European integration and the 1992 initiatives, many have tended to focus on political factors, amongst and inside the national governments of the EC, economic factors, and institutional factors:³

Paul Taylor has noted that the new dynamics of the EC integration in the 1980s came from the settlement of the British complaint about their excessive budgetary contributions, a campaign for strengthening the EC's institutional decision-making ability that led to the 1984 Draft Treaty on European Union, the agreement on the SEA, a new programme for achievement of a Europe without frontiers by 1992, and the reform of the Common Agriculture Policy.⁴ Roy Pryce has focused on the outcome of the 1984 Fontainebleau meeting of the European Council. He has also emphasised the importance of the agreements reached on these critical issues. He particularly suggests that a widespread and growing reaction against the ineffectiveness of the EC contributed the most to the momentum for a relaunch.⁵

"Europe 1992: internal and external", in Finn Laursen, (ed.), *EFTA and the EC: Implications of 1992*, (Maastricht, The Netherlands: European Institute of Public Administration, 1990), pp. 5-32.

2. Finn Laursen, "Explaining the EC's new momentum", in *ibid*, p. 47.

3. David R. Cameron, "The 1992 initiative: causes and consequences", in Alberta M. Sbragia, (ed.), *Euro-Politics: Institutions and Policymaking in the "New" European Community*, (Washington D. C.: The Brookings Institution, 1992), pp. 35-64; Moravcsik focused on institutionalism see "Negotiating the Single European Act", pp. 42-48.

4. Paul Taylor, "The new dynamics of EC integration in the 1980s", in Juliet Lodge, (ed.), *The European Community and the Challenge of the Future*, (London: Pinter Publishers, 1989), p. 3.

5. See Roy Pryce, "Relaunching the European Community", *Government and Opposition*, 19, (1984), pp. 486-500.

Juliet Lodge has pointed to the fact that along with the European Parliament's initiatives, several "negative factors", i.e. the continued recession, rising unemployment, the need for the EC to try to safeguard and improve its position vis-à-vis the US and Japan, the EC's further enlargement and institutional deadlock, also contributed to the momentum for further integration by "encouraging widespread reflection on the EC's future."⁶ She reminds us that although there was a pervasive belief about the urgent need for reform in the EC, without the Intergovernmental Conference in 1985 on European Union and a draft treaty of the European Union initiated by the European Parliament (EP), "it is doubtful whether any steps would have been taken by the governments to try to improve the EC's prospects and its functioning."⁷ She implies that the EP's commitment to expanding EC competences and promoting common (union or supranational) action contributed much to the successful signing of the SEA. This institution-initiated focus lays stress very much on the decision-making of the EC institutions, and their relations with national governments.

Andrew Moravcsik divides the explanations for the success of the SEA into two, "the first stressing the independent activism of international or transnational actors and the second emphasizing bargaining between leaders of the most powerful states of Europe."⁸ In response to the question why the change appeared then, he, therefore, focuses on an elite alliance between EC officials and pan-European business interest groups, ruling party coalitions between France, West

⁶. Juliet Lodge, "The Single European Act: Towards a new Euro-Dynamism?", *Journal of Common Market Studies*, 24: 3, (March 1986), p. 203.

⁷. Ibid., p. 204.

⁸. Andrew Moravcsik, "Negotiating the Single European Act", in Keohane, and Hoffmann, (eds.), *The New European Community: Decisionmaking and Institutional Change*, (Boulder: Westview Press, 1991), p. 43.

Germany and Britain, and Franco-German negotiations for a "two track" Europe.⁹ The successful negotiation for the SEA was mainly derived from the strong demand for completing the internal market, and institutional reforms that attempted to make the EC's decision-making more effective and democratic. From the industrial point of view, however, the momentum for the successful passage of the SEA rested upon the strong support of European industry and the prospects for better European economy and industrial strength. In order to achieve a single European market, it was necessary for the EC and its member states to carry out institutional and decision-making reforms. John Pinder rightly suggests that, in terms of industrial competitiveness, the reason why Europe was left behind by the US and Japan was mainly due to the fragmentation of national markets in Western Europe, which eventually contributed to a consensus for urging the completion of the internal market and institutional reforms.¹⁰

As far as the SEA was concerned, the largest single section of the SEA was devoted to completing the internal market. The completion of the internal market implied "much more in terms of the scope of European integration than is apparent from the SEA."¹¹ Since the early 1980s, a new wave of industrial competition, driven by a "third industrial revolution",¹² and the search for cost-cutting in production,¹³ has governed the pace of the global economy, weakened the function of the world trading multilateral system, and boosted

⁹. Ibid., p. 42.

¹⁰. John Pinder, "The Single Market: a step towards European Union", in Juliet Lodge, (ed.), *The European Community and the Challenge of the Future*, pp. 94-95.

¹¹. Juliet Lodge, "The Single European Act and the new legislative cooperation procedure: a critical analysis", *Journal of European Integration*, 11: 1, (1987), p. 6.

¹². Used the term by John Pinder, "The Single Market: a step towards European Union", p. 95.

¹³. Global industrial competition has demanded a cut in production costs with simultaneous advances in technology. See Richard Barnett, and John Cavanagh, *Global Dreams: Imperial Corporations and the New World Order*, (New York: Simon & Schuster, 1994), pp. 283-309.

the trend towards regionalism. The need for governments and industrialists to address Europe's flagging competitiveness was to be one of the major triggers of the 1980s' relaunching of European integration. As a result, an unprecedentedly influential industrialists alliance emerged actively to push forward the progress of European integration. The agenda for completing the internal market was enshrined in the SEA (Article 13, 14 and 19), which recognised the fact that the removal of all internal frontiers (physical, technological and fiscal barriers) for strengthening industrial operations and economy as a whole would encourage an industrial unity and contribute to the political consensus upon which future integration would be based.

3.1. INDUSTRIAL DEVELOPMENT AND THE EVOLUTION OF EUROPEAN INDUSTRIAL UNITY

3.1.1. National Interests and Making European Industrial Policies

The history of European integration has always been influenced by external factors, both political and economic, which indeed triggered the whole process. In the 1950s and 1960s West European integration was in fact strengthened not only by West European countries' demand for peace and prosperity (shown for example in the Benelux countries' cooperation and improved Franco-German relations), but also by the influence of superpower politics. Europeans' demands for integration were encouraged, if not directly pushed, by the United States. The development of European stability and prosperity was considered by American elites as the best policy to oppose the communist threat from the East. In short,

the early development of regional integration in Western Europe seemed to be a natural product of the Cold War whose security and bloc politics, the East-West confrontation, had predominantly overshadowed national decision-making with regard to international economic and political cooperation.¹⁴

For the original Six of the ECSC, "West European integration did not involve sacrificing national economic interests on the altar of Europeanism; rather, considerations of national economic gain provided the motor force which carried them down the road of West European integration."¹⁵ In the 1950s, the industrial structures of the Six showed great similarities, in which industrial sectors accounted for about one-third of the work force (agricultural sectors about a little less than one-third and the rest in service sectors). Each individual state was concentrating upon its own national economy rather than upon the joint economic problems of Europe. The main reason for retaining the application of restrictions at the national border was simply to avoid "a cycle of mutually destructive retaliation."¹⁶ In spite of different national interests existing amongst West European economies, during the 1950s, their economic targets were similar in seeking to achieve a satisfactory national growth rate (which was obtained at around 5 or 6 per cent), to maintain stability in prices, employment and foreign exchange

¹⁴. On the question of the struggle for power and national interest, as the realists of international politics, Hans Morgenthau, Raymond Aron, etc., emphasised, nations pursue their best interests by employing naked force against each other. In the Cold War's bipolarity system, confrontation and conflict were expressed in national policy with the emphasis on security and militarism. Indeed, European integration in the early period was in accordance with American global strategy. For the argument of security factors as an "high politics" agenda see Joan E Spero, *The Politics of International Economic Relations*, 3rd edition, (New York: St. Martin's Press, 1985).

¹⁵. David Arter, *The Politics of European Integration in the Twentieth Century*, (Aldershot: Dartmouth, 1993), p. 119.

¹⁶. Raymond Vernon, "Enterprise and Government in Western Europe", in Vernon, (ed.), *Big Business and the State: Changing Relations in Western Europe*, (London: The Macmillan Press, 1974), p. 4.

earning, and to deal with the social and political problems within each national economy.¹⁷ These efforts marked the European economy as a whole for the period with fast expansion, full employment, heavy investment, low energy and raw material prices (refer to Appendix T-2.1 and T-2.2). The tendency of industrial sectoral development within the Six was moving towards nationally industrial integration instead of broad industrial integration between countries, because "no country freely gave up its industrial sectors to the benefit of other member states, where such sectors might be more efficient."¹⁸

For example, in order to make the steel industry competitive, the ECSC treaty sought to eliminate the barriers to interstate trade, subject industrial cartels and concentrations to administrative supervision and establish common commercial rules for pricing and sales. The transnational ECSC's vision of harmonisation of the European steel industry incurred the steel makers' deep suspicion of competition. This resulted in their defensive action with increased combination between them.¹⁹ Subsequently, the Six retreated from the transnational vision of industrial competition towards national planning, which pressed each country "to save its steel industry at the expense of the others."²⁰ The French government went further to veto a High Authority (of the ECSC) proposal in July 1966 to replace national subsidies with Community financing to the industry.

17. Ibid.

18. Henk W. De Jong, "Sectoral development and sectoral policies in the EC", in Alexis Jacquemin, (ed.), *European Industry: Public Policy and Corporate Strategy*, (Oxford: Clarendon Press, 1984), p. 149.

19. J. E. S. Hayward, "Industry - Steel", in Vernon, (ed.), *Big Business and the State: Changing Relations in Western Europe*, p. 279.

20. Ibid.

During the 1960s, West European countries enjoyed strong economic growth (The EC's GDP per capital growth rates from 1960 to 1970 were around 5 per cent: Belgium 4.8 per cent, West Germany 4.4 per cent, France 5.7 per cent, Italy 5.3 per cent and the Netherlands 5.5 per cent).²¹ In that unprecedented era of economic growth, Europe was experiencing a boom in productivity, private investment and employment. As far as economic integration was concerned, although European industrialists were very concerned with the possible effects of the progress of integration on the business environment, they did not pay close attention to integration itself.²² It was because of the early uncertainty surrounding integration and the nature of the integration arrangements, as well as interdependent networks with the rest of the world, that elites within national governments tended to dominate the issues of integration. The participation of industrialists at this stage was not a necessary condition for the forward momentum of integration.

In terms of the private sectors, the establishment of the Common Market by the Treaty of Rome had not produced industrial concentration on a European scale as had been expected but very much on a national basis, although the Commission of the EEC proposed a policy of European industrial concentration in a statement to the European Parliament and a memorandum presented to the Council of Ministers in December 1965. It had become evident that by 1965 industry in the Six had generally made few adjustments necessary for future survival. In 1968, the then EC Commissioner for industry, Guido Colonna Di Paliano, recorded that:

²¹. *World development Report 1985*.

²². Ernst Haas, *The Uniting Europe: Political, Economic, and Social Forces 1950-1957*, (London: Stevens & Sons, 1958). He noticed the lack of active elite business support for the early European initiatives.

"(the Six) had done little to assure adequate profits for future development, in a climate of growing competition at home as well as abroad. To the extent that firms had remained too small to function in a large, free, and open market, the solution depended largely on the public authorities' willingness to remove the barriers that prevented changes in the structure of industry."²³

Indeed, at one time the Common Market provided little incentive for industrial cooperation in a wide range of sectors, since these nationally based firms "have been frequently able to improve their competitive capacity first through concentrating on a domestic basis and then by expanding into the markets of other member states through direct sales and the establishment of wholly owned subsidiaries."²⁴ While national interests were far ahead of European interests, European states' approaches to the practice of business and industry by making use of the public ownership in enterprises served for nothing more than national targets. In the context of the Cold War and European economic recovery, West European national governments' commitment to international economic cooperation was rather passively pushed by the progress of political integration.

In the mid-1960s, as European economies gradually overcame the problems of post war reconstruction, it became important for the European countries to show that their economies and industries were independent of the United States. This would imply that they were once again of some importance in world affairs. Therefore, American economic

²³. Guido Colonna Di Paliano, "Why Europe needs continental-scale firms", *The Atlantic Community Quarterly*, 6: 4, (Winter 1968-69), p. 567.

²⁴. Steven J. Warnecke, "Industrial policy and the European Community", in Warnecke and Ezra N. Suleiman, (eds.), *Industrial Policies in Western Europe*, (New York: Praeger Publishers, 1975), p. 166.

predominance in Europe through direct investment and transnational corporations engaged in key sectors was made an issue of European industrial strength, which encouraged the EC to take a more interventionist strategy.²⁵ In order to compete with their American counterparts, "Europeans would have to emulate the American industrial structure - particularly in regard to the size of corporations and in the new-high-technology fields."²⁶ Industrial groups, such as the UNICE and the Patronat Français, pointed to an urgent need to change the disparity in size of European enterprises and European political and economic network compared with those of the US.²⁷ As a result, a programme of industrial concentration through cross-frontier mergers and industrial links was brought forward. In terms of industrial competitiveness, the challenges from American industrial superiority became a motive to the development of industrial unity.

In 1970, a Commission report by Guido Colonna Di Paliano for establishing a Community industrial policy highlighted the importance of industrial unity in spearheading European integration:

"If the general well-being is to be improved, industry must be able to make the most of the Common Market, as an entity, and as an entity permitting large-scale operations."²⁸ "A common industrial development policy encouraging the creation of a European industrial 'fabric' is indispensable if three vital objectives are to be achieved: the establishment of firm foundations for the economic - and soon the political - unity of Europe, the maintenance of economic growth, and a reasonable

²⁵. Dennis Swann, *Competition and Industrial Policy in the European Community*, (London: Methuen & Co., 1983), p. 136.

²⁶. Warnecke, "Industrial policy and the European Community", p. 177.

²⁷. *Ibid.*, p. 178; also Swann, *Competition and Industrial Policy in the European Community*, p. 136.

²⁸. Commission of European Communities, "Principles and general datelines of an industrial policy for the Community", Supplement to Bulletin of the European Communities, 4/1970, p. 5.

degree of technological independence of major world powers."²⁹

Nevertheless, this approach to industrial concentration relying upon the private sector was neither advancing to full scale industrial cooperation nor to a European level industrial policy. At the centre of the intergovernmental and transnational tug of war in the decision-making of the EC, the private sector in response to the Commission in seeking a European industrial network for political goals was reluctant to make a case.³⁰ During the 1970s' international economic turbulence, the prospect for European industrial unity was given a big push by exogenous economic problems: slower growth, increasing unemployment, declining investment, rising prices and fluctuating exchange rates.

3.1.2. Industrial Unity as A Catalyst for European Economic Integration

The conventional understanding of regional integration, in theories such as federalism and neofunctionalism influenced by a state-centric approach, has focused more on political approaches and motivations for regional integration, taking into account national interests rather than the wider regional interest.³¹ In addition, the conventional approach, emphasising internal processes of regional integration, has highlighted political, economic, and cultural transactions between states within a region from which "consensual values for the

²⁹. Ibid., p. 4.

³⁰. Warnecke, "Industrial policy and the European Community", pp. 160, 184.

³¹. The conventional understanding here is mainly concerned with the exploration of integration theory. Integration, in the view of the realist, is not the dominant characteristic of either world society or of inter-state relations. See A. J. R. Groom, and Alexis Heraclides, "Integration and disintegration", in Margot Light and A. J. R. Groom, (eds.), *International Relations: A Handbook of Current Theory*, (London: Pinter Publishers, 1985), p. 175.

achievement of common goals" have resulted.³² Both theory and practice have confirmed that the progress of regional integration is influenced by political aspirations. The motivations of regional economic integration were in general coming much more "from above" (high politics) than "from under" (low politics). Laffan has asserted that the Western European regional system "was moulded by the priority of the superpowers, the need to reach an accommodation on the German question, and the imperative of political, social and economic reconstruction."³³ Therefore, in the establishment of Benelux Custom Union and the ECSC, for instance, political and security considerations were amongst the most important factors behind integration.

Furthermore, Robson has argued that "the initiative for Economic and Monetary Union (EMU) in Europe that subsequently developed in the late 1960s was predominantly motivated not so much by any obviously pressing economic necessity for the conduct of the Common Market itself but rather by a political desire to provide a focus and a driving force for European integration in the next decade."³⁴ Functional cooperation was a means rather than an end of integration. As the spillover effect is to be brought about automatically by frequent interaction, argued by functionalists and neofunctionalists,³⁵ within the existing cooperation networks amongst European

³². Ibid., p. 174.

³³. Brigid Laffan, *Integration and Cooperation in Europe*, (London: Routledge, 1992).

³⁴. Peter Robson, *The Economics of Internal Integration*, 3rd. edition, (London: Unwin Hyman, 1987), p. 158.

³⁵. In Mitrany's functionalist theory, a doctrine of "ramification" to integration process explains the natural and progressive development of collaboration which generates a need for more functional collaboration in other fields. David Mitrany, *A Working Peace System*, (Chicago: Quadrangle Books, 1966), p. 97. Although neofunctionalists take a "spillover" effect to integration for granted, Ernst Haas, the major exponent of neofunctionalism, has reasserted that the idea of "spillover" is not automatic but probable. See Haas, "The Study of Regional Integration: Reflections on the joy and anguish of pretheorizing", in Lindberg, L. and Scheingold, S. (eds.), *Regional Integration*, (Cambridge, Mass., Harvard University Press, 1971).

nations, business activities gradually emerge as one of the main forces for integration by pushing the policy-making of national governments and the European Community.³⁶

After the recession of the mid-1970s when the developed economies experienced falling rates of economic growth, high inflation, and mass unemployment, the lesson for national elites was that economic affairs were of primary importance. Thereafter, there have been widespread worries about survival amongst European private industries. State interference, used by the Left governments in Western Europe as an industrial strategy, involving large scale nationalisation, price controls, bureaucratic meddling, and confiscatory tax systems, was depressing industries. Furthermore, the rise of powerful trade unions throughout Western Europe gave rise to demands for work-sharing arrangements and guaranteed job security, and newly militant environmentalists in France and West Germany hindered the private sectors from expanding operations that the industries required.³⁷ In addition, high inflation rates dampened the prospects of increasing economic growth whilst action to reduce inflation caused an increase in unemployment.

Higher inflation led to efforts to cut production costs by shedding labour leading to higher unemployment in European companies, such as the Dutch electronics giant Philips,³⁸ Ford (Britain),³⁹ and SGS-Ates, the Italian semi-conductor

³⁶. To some extent the economic factors have gradually replaced politics, or more precisely security, as the most outstanding factors in national decision-making processes, especially in the post Cold War era. In the theoretical debate, pluralists and structuralists are particularly associated with this arrangement. See Michael Banks, "The Inter-Paradigm Debate" in Light, and Groom, (eds.), *International Relations - A Handbook of Current Theory*, pp. 7-20.

³⁷. Robert Ball, "The surprising new optimism of Europe's C.E.O.s", *Fortune*, (August 14, 1978), pp. 112, 114.

³⁸. Philips cut 68,000 jobs in 1970-1985. For Philips' restructuring process in the 1980s see Graham Turner, "Inside Europe's Giant Companies: Cultural Revolution at Philips", *Long Range Planning*, 19: 4, (1986), pp. 13-15.

³⁹. Ford Britian shed 40,000 jobs in 1979-1984. See "More job cuts, Ford chief says", *The Times*, (30 October, 1985), p. 4.

producer.⁴⁰ Bob Lutz, the head of Ford Europe, in 1985 stated that "we have no choice but to continue reducing the head count to become competitive."⁴¹ Labour costs, social charges (From 1974 to 1981 industrial compensation per employee in nine EC countries increased 13.8 per cent, while in the US it grew 9.9 per cent and in Japan 10.7 per cent.)⁴² and the costs of meeting new environmental standards rose as a result. The fading of industrial profitability (The EC net rate of return on fixed capital excluding the construction industry accounted for 10.6 per cent in 1960-73, 5.9 per cent in 1974-80 and 4.0 in 1981.)⁴³ resulted in the depression of investment and of business confidence in the EC.

As a result, European political elites, at both the national and supranational levels, started to work closely with leading industrialists in an attempt to improve industrial competitiveness.⁴⁴ Industry and politicians turned to the creation of the Single European market as the core of their strategy to improve industrial competitiveness as well as the economy as a whole.⁴⁵ It is clear that the neofunctionalist argument with its emphasis on the contribution to integration made not so much by social-economic factors as by the interaction of political and

⁴⁰. It cut 1,500 out of its 5,300 workers in Italy by 1984. See *The Economist*, (December 8, 1984), pp. 73-74.

⁴¹. "More job cuts, Ford chief says", *The Times*, (30 October, 1985), p. 4.

⁴². Based on Eurostat, see Commission of European Communities, "Unit labour costs in manufacturing industry", *European Economy*, 10, (March 1982).

⁴³. The EC here includes six countries, Belgium, Denmark, France, Italy, the Netherlands and the UK. Information estimated by the Deutsches Institut für Wirtschaftsforschung from The Economic and Social Situation of the Community, Economic and Social Consultative Assembly, 1985.

⁴⁴. This view has been reflected in many studies as a pervasive need for the alliance between governments and industry, e.g. Jacques Pelkmans and Alan Winters, *Europe's Domestic Market*, (London: RIIA, Routledge, 1988), p. 6; Margaret Sharp, "The Single Market and European policies for advanced technologies", in Colin Crouch and David Marquand, (eds.), *The Politics of 1992: Beyond the Single European Market*, (Oxford: Basil Blackwell, 1990), p. 105.

⁴⁵. Commission of the European Communities, "Completing the internal market for industrial products", by Jacques Pelkmans, Document, 1986, p. 34.

economic factors,⁴⁶ has not been able to keep up with the progress of European integration in the mid-1980s. Socio-economic factors have been in the vanguard of demands for a single European market.

The practical measures taken towards strengthening the Commission's partnership with industry were revealed in the White Paper of 1985 by the European Commission to the European Council. In chapter six of the Paper, the Commission stated that "Community budgetary and financial facilities make their full contribution to the development of greater cooperation between firms in different Member States" and "the Community is now, for the first time, setting the stage for a new type of association to be known as the European Economic Interest Grouping (EEIG) that will be governed by uniform Community legislation."⁴⁷ According to the Council's Regulations governing the EEIG, to ensure that the grouping would work for the Community's interest, there would be a Contact Committee composed of the representatives of the Member States and the Community.⁴⁸ This legal confirmation of the close ties between the European Commission and European industrialists has symbolised their joint efforts to push forward the completion of the internal market and the wider process of integration.

The impetus for the relaunch of European integration played an important role in reaching the Draft Treaty on European Union (EUT) in the EP.⁴⁹ Whilst the EP called for political reforms in the EC's institutions which suggested that the EP should share more power in pursuit of a People's

⁴⁶. See Juliet Lodge, "integration theory", in her (ed.) *The European Community - Bibliographical Excursions*, (London: Francis Pinter Publishers, 1983), pp. 6-16.

⁴⁷. Commission of the European Communities, "Completing the Internal Market", White Paper from the Commission to the European Council, (Milan, 28-29 June, 1985), COM(85) 310 final, (14 June 1985), pp. 34, 35.

⁴⁸. Council Regulation (EEC) No. 2137/85, of 25 July 1985, on the European Economic Interest Grouping. This regulation came to effect on 1 July, 1989. *Official Journal of the European Communities*, L199, (31 July 1985), pp. 1-9.

⁴⁹. For the detail about the EP and the development of the EUT see Juliet Lodge, "The Single European Act: Towards a new Euro-Dynamism?", *Journal of Common Market Studies*, 24: 3, (March 1986), p. 203-223.

Europe, the Commission backed by industrialists placed its hopes on the completion of the internal market as the primary engine of integration. To create the internal market, the Commission realised that a certain degree of political agreement for the reform of EC decision-making would have to be reached in order to avoid any proposal about improving industrial performance becoming bogged down at the implementation stage. To address economic and monetary policy, scientific and technical research and energy policy at the supranational level, on which the restoration of European industry's international competitiveness would depend, and the creation of the internal market would be based, the Community would have to be backed by political commitment from the member states. In a discussion paper to the Council, the Commission stated that it:

"would call for a return to the decision-making methods which, in the early years of the Community's existence, produced the policies on which it is based."⁵⁰

In 1984 at the Fontainebleau summit of the European Council, an ad hoc Committee on institutional reforms (called the Dooge Committee) was established.⁵¹ In 1985 at the Brussels summit, there was a call for the completion of the internal market. In June 1985, a key Commission report, the White Paper, by Lord Cockfield, the then Commissioner for Internal Market, emphasised the completion of the internal market and was endorsed by the 1985 European Council's Milan summit. Commenting on the Paper for completing the internal market by the removal of technical, physical and fiscal barriers, the

⁵⁰. Commission of the European Communities, "discussion paper for the special Council meeting of 20 to 21 September 1983 on the question of improving the international competitive position of European firms", COM(83) 547 final, (14 September, 1983), p. 12.

⁵¹. Another Committee for the creation of a People's Europe (the Adonnino Committee) was also established at the same time.

Economic and Social Committee of the EC, an influential consulting body on some key policy issues,⁵² believed that:

"For this reason the appropriate decisions will have to be taken with the unswerving political will to succeed, to overcome reservations and obstacles." Therefore, The Committee "urges the Council to reform its decision-making capacity. It calls on the Council to accept qualified-majority decision-taking. In order to cope with the large volume of legislation needed to complete the internal market, this is necessary."⁵³

These efforts prepared the law for the Single European Act of 1986. In the SEA, the task to complete the internal market represented "not only a firm step towards unity in the EC, but was an essential prerequisite to future economic growth, employment and trading prospects in the world."⁵⁴

In the peak of the "Europessimism" or "Eurosclerosis", politicians, academics, and industrialists alike lost their confidence in the future of European integration because of the indecisive and discordant European Community, and its bad performance in dealing with the recession. Despite the fact that the European Council had realised the need for the internal market at the 1981 Luxembourg meeting, and later that year in London, nothing had been brought about in reality but a mere confirmation of the internal market between the Council and the Commission. Even in December 1982 at the Copenhagen summit, Gaston Thorn, the then President of the Commission, "recommended" the European Council for the first time to remove national non-tariff barriers, simplify frontier

⁵². The ESC under the treaties of the EC is to be consulted compulsorily on nine subject-matter specialties. It is made up of representatives of trade unions and professional bodies. It gives its advisory opinions on the proposals made by the Commission.

⁵³. Economic and Social Committee of the EC, Opinion on the "Completing the internal market - White Paper from the Commission to the European Council", CES(85) 1019, (27 November 1985), pp. 2-3.

⁵⁴. Ibid., p. 1; a similar viewpoint has been expressed on many occasions, such as that of the French Government's initiative about revitalisation of the Community. See "French Government memorandum on revitalisation of the Community", *Bulletin of European Communities*, 11, (1981), p. 92.

formalities, increase competition in public procurement, equalize legal rights and tax codes for companies, and open up trade in financial services.

The widespread feeling of impotence in the management of the European economy was described as the complications of national economic diseases.⁵⁵ Individual member states of the EC facing the recession endeavoured to protect their own markets and industries through the use of public funds to aid and maintain "non-viable companies" at the expense of fellow member states. According to a study published by the Commission in 1979, the crisis facing Europe's industry at that time was: firstly, a fourfold increase in oil prices; secondly, increases in raw material costs; thirdly, the repercussions of the international monetary crisis; and fourthly, additional competition from recently industrialised countries.⁵⁶ Since the cost of industrial production was soaring due to the increase in expenditure on energy and materials as well as wages, European industry was losing ground in world markets not only to Americans and Japanese but also to those of the NICs. Some European industries, such as those in foodstuffs, textiles, shipbuilding, and steel, which had led the competition for years, could no longer compete with the market new comers whose low production costs had already earned them a rising share of the world market.

Another study identified signs of a European "malaise": firstly, unemployment in the community stood at a level of around 10 million; secondly, considerable vulnerability in the energy sector; thirdly, a badly-directed and poorly-exploited research and development (R & D) effort; and fourthly, a relative decline in European competitiveness.⁵⁷ High

⁵⁵. Such as West Germany's Swedish disease (over-indulgent welfare state), the Dutch disease (compounding the Swedish with gastro-enteritis of the exchange rate), the Belgian disease (swollen budget deficit and galloping indexation), the Italian disease (booming inflation), and the British disease (multiple sclerosis). See Michael Emerson, *Europe's Stagflation*, (Oxford: Clarendon Press, 1984), p. 195.

⁵⁶. *European File*, No, 3/79: "The Community's Industrial Policy", (February 1979).

⁵⁷. *European File*, No, 3/82: "Relaunching Europe: A New Community for Industry and Employment", (February 1982).

unemployment in Western Europe was evidence that industries were suffering from a decrease in output and unsuccessful national macroeconomic policy, an inefficient R & D effort, in terms of commercial applications in comparison with principal competitors in the United States and Japan, leaving a wide gap between R & D spending and Commercial applications, and diminishing competitiveness resulting from increasing unit labour costs and low productivity. These problems revealed the inability of existing national economic frameworks to cope effectively with global competition, on the one hand, and a growing demand for a European rather than national solution, on the other.

Lord Cockfield pointed out and the Cecchini report suggested that the beneficiaries of a single market in 1988,⁵⁸ would be European industries and businessmen. Behind the political scenes the industrialists were one of the most active groups pressing for further moves towards integration. Their efforts were not only originally intended as a response to the economic crisis, but for establishing a cross-border industrial unity. For example, the formation of EEIG which evolved from European Cooperation Grouping in 1974 aims at encouraging cooperation across frontiers in the Community.⁵⁹ A series of important events contributed to relaunching the pace of European integration. These were the settlement of the excessive British budgetary contribution in 1984, the emergence of the 1984 Draft Treaty on European Union, the agreement on the SEA and a new programme for a Europe without frontiers by 1992, and finally the agreement about a package

⁵⁸. "Making a real Common Market: Lord Cockfield points the way to the future", *Europe 85*, (November/December 1985), pp. 17-18; Paolo Cecchini, *The European Challenge: 1992 The Benefits of A Single Market*, The Cecchini Report - Official Facts and Figures, (Aldershot: Wildwood House, 1988).

⁵⁹. Even the British were ready to consider the benefits of this proposal for industrial unity, as the proposal of the formation could be helpful to British companies. See 25th Report, European Communities Committee, the House of Lords, 1883-1984 session, (24th July, 1984).

of budgetary measures in 1988.⁶⁰ Through the delicate negotiation process amongst European political elites, mainly the German, French, and British, a consensus developed about the importance of promoting further integration. Others have focused on European political circumstance and acknowledged that the pervasive shift in government coalitions, from communist Left to market socialist Left in Spain, Italy and France in the first half of the 1980s, planted the successful seeds of negotiation.⁶¹

More recently, some who have tried to pin-point the explanation for the 1992 programme argued that there were generally three reasons why the 1992 programme turned out to be a driving force for integration:

"One approach would look to the internal dynamics of the integration process itself, as in integration theory. A second would concentrate on the domestic politics behind the regional agreements. The third approach focuses on elite bargains in response to the challenges and opportunities posed by international and domestic changes."⁶²

These approaches together have advanced beyond the range of the traditional theories of integration, i.e. federalism, functionalism, neofunctionalism and pluralism, although internal processes of integration remain their key interest. They include the pro-European movement, the development of transnational institutions, member states' interaction, and their domestic settings. Some external factors, e.g. the worldwide economic trend, the change of international

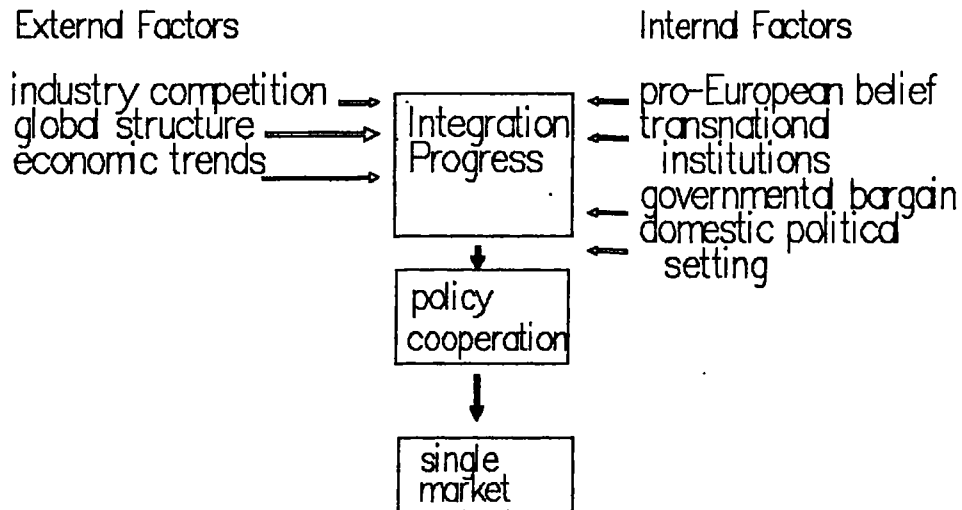
⁶⁰. For the process of the SEA see Andrew Moravcsik, "Negotiating the Single European Act" in Keohane & Hoffmann, (eds.), *The New European Community: Decision making and Institutional Change*, p. 41; for the diplomacy about the British budgetary rebate in 1984, and the cause and character of the SEA see Paul Taylor, "The New Dynamics of EC Integration in the 80s", in Juliet Lodge, (ed.), *The European Community and the Challenge of the Future*, (London: Pinter Publishers, 1989), pp. 3-25.

⁶¹. For example Stephen George, *Politics and Policy in the European Community*, (Oxford University Press, 1985), pp. 180-197.

⁶². Wayne Sandholtz, and John Zysman, "1992: Recasting The European Bargain", *World Politics*, 42, (October 1989), p. 97.

structures, and some sporadic international crises, have also largely contributed to the relaunch of European integration.

FIGURE 3.1. INFLUENCES ON EUROPEAN INTEGRATION



The progress of European integration has been therefore an outcome of an interaction between internal and external factors, as illustrated in Figure 3.1. However, a fourth approach may be brought forward, which focuses on the role played by European industrial groups undergoing strong external competitive challenges in the process of industrial restructuring and the relaunch of European integration. Prior to the SEA, except for the Community's pre-emptive research programme, the ESPRIT, there was, indeed, little EC-wide industrial and technological cooperation. In the mid-1980s, after European industrialists' lobbying campaigns for a favourable business environment in Europe, transnational and national élites were mobilised towards further integration.

According to Wisse Dekker, the President of the Dutch electrical giant Philips, European integration in the 1950s

was mainly initiated by politicians, while in its current "industrial" phase it has been initiated by business leaders.⁶³ To a large extent, Jacques Delors, President of the European Commission, and the industrialists' "alliance" concentrated pro-European support and hence strengthened the bargaining position with national governments. European industrial unity was first launched in order to reinforced industrial competitiveness. As a result, economic integration would then be formally brought in, and later social and political integration follow suit.⁶⁴ The re-emergence of European integration in the 1980s, has had implications for the process of integrating differences amongst certain groups.

FIGURE 3.2 INDUSTRIAL DEVELOPMENT AND INTEGRATION
A European Case

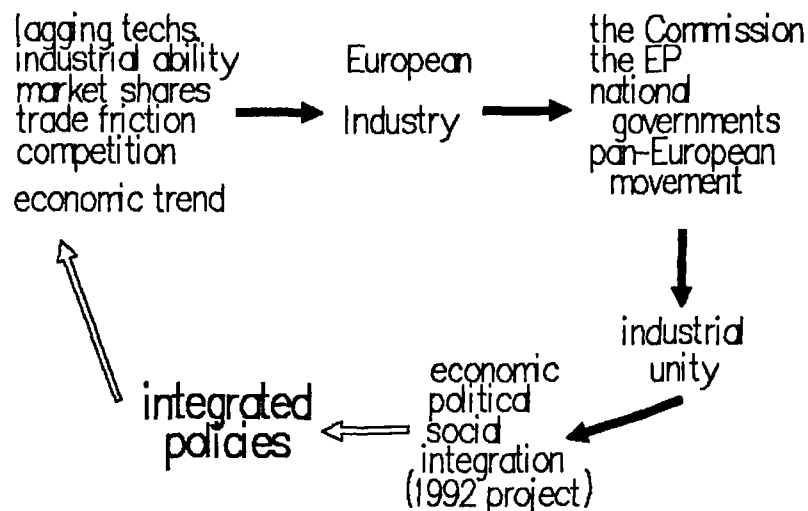


Figure 3.2 shows how the context of European integration changed in the 1980s and how industrial unity pressed the

⁶³. Wisse Dekker, "Europe's economic power: potential, and perspectives", speech delivered to the Swiss Institute for International Studies, Geneva, (25 October, 1988).

⁶⁴. As far as the relaunching of integration was concerned, the study here refers to the real reasons behind the successful multinational negotiation and the active Commission to complete signing the SEA.

integration progress ahead. A number of external factors served as the drive for European integration in terms of industrial development of the EC, albeit most of them turned out to have a negative effect on European industry. The completion of the internal market in the White Paper and the SEA has been initiated to integrate the interests of industrialists within the EC, as industrialists seek for a more favourable economic framework to cope with external ~~external~~ challenges. As a result, economic integration brought forward the possibility of further social and political integration. Yet, there were also some other factors, such as favourable domestic settings, a pro-Europe belief shared by most outstanding political elites, and an active Commission led by Jacques Delors, which were as important as the change of international structure to integration.⁶⁵ Given the very great complexity of the integration process therefore it should not be thought that the successful relaunching of integration could be mobilised by one factor only.

3.2. THE IMPACT OF INDUSTRIAL COMPETITION ON EUROPEAN INDUSTRY AND THE PROGRESS OF EUROPEAN INTEGRATION

3.2.1. The Relative Decline of European Industry

It is critical to emphasise how distressed European industry was in the 1970s facing the recession and increasing

⁶⁵. A number of studies have discussed all those factors which were regarded as supplying possible incentives to integration. Keohane, and Hoffmann's three hypotheses of making the SEA were: spillover, political economy, and domestic politics. See "Institutional change in Europe in the 1980s", in their (eds.) *The New European Community: Decision Making and Institutional Change*, pp. 18-25; the similar view shared by Sandholtz and Zysman's three approaches, including integration theory, domestic politics, and elite bargaining, in "1992: recasting the European bargain", pp. 97-103; Moravcsik's two approaches, transnational and Intergovernmental institutionalism, bringing the success of the SEA, in his "Negotiating the Single European Act", pp. 46-48.

external industrial competition in order to provide an explanation of the industrial dimension of the change of European integration. Since the mid-1970s, Europe's production of goods and services was more dependent on traditional industries than was the case in Japan and the USA. According to one European report, "In volume terms, the Community industrial production in December 1983 was 116.0 (1975 base=100) as against 132.8 for the USA and 152.3 for Japan."⁶⁶ In the exporting of goods and services in world markets amongst major industrial countries from 1965 to 1986, while Japan's share rose to 12.03 per cent in 1986 from 4.53 per cent in 1965, the United Kingdom declined continuously from 13.25 per cent in 1965 to 8.75 per cent in 1986. On the whole,

TABLE 3.1. THE OECD COUNTRIES' WORLD MARKET SHARES OF GOODS AND SERVICES (1965-1986)

	1965	1970	1975	1980	1981	1983	1985*	1986*
USA	17.69	16.01	16.92	17.30	16.44	13.97	12.69	12.43
Jap.	4.53	6.22	7.79	9.47	10.43	10.88	11.92	12.03
FRG**	15.03	15.19	14.90	14.44	15.02	15.18	14.98	15.12
F	7.37	8.11	9.21	9.52	9.61	9.60	9.18	9.13
UK	13.25	11.72	10.86	9.69	9.13	9.15	8.83	8.75
I	5.33	6.11	6.27	6.47	6.48	6.73	6.38	6.29
Others	36.32	36.64	34.05	33.11	32.89	34.49	36.02	36.25
OECD	100	100	100	100	100	100	100	100

Note: * based on forecast. ** FRG: West Germany

Source: Based on OECD, Statistics of External Trade, quoted from Hatzichronoglou, "Mutations Technologiques et Compétitivité de L'Industrie Française: Dix Constatations".

West Germany's, France's and Italy's shares decreased in 1983-86, although they had enjoyed the increase in the 1960s and

⁶⁶. *The Economic And Social Situation Of The Community*, Economic and Social consultative Assembly, (1985), p. 2.

1970s⁶⁷ (Table 3.1). The export of manufactures from these industrial countries reflected a similar trend over the same period (Table 3.2). The slowdown of European industrial growth was attributed to its aging industrial structure which adjusted more slowly than the US and Japanese industries to technological innovation.

TABLE 3.2. THE OECD ECONOMIES' MARKET SHARES OF EXPORTS OF MANUFACTURES

	1965	1970	1975	1980	1981	1982	1983
USA	19.5	17.8	16.4	15.3	16.9	16.4	15.7
Jap.	7.5	9.7	11.0	11.8	14.3	13.7	14.7
FRG	15.4	16.6	17.2	16.7	15.6	16.5	15.9
F	8.2	8.1	9.4	9.4	8.8	8.4	8.3
UK	11.2	9.1	8.1	8.9	7.4	7.5	7.0
I	6.1	6.4	6.7	7.0	7.0	7.2	7.1
Can.	5.1	6.4	4.2	4.1	4.6	4.7	5.3

Source: as Table 3.1.

TABLE 3.3. A PRODUCTIVITY COMPARISON OF THE EC10, JAPAN AND THE US (1973 = 100)

	<u>Economy as a whole</u>			<u>Manufacturing Industry</u>		
	EC10	Japan	USA	EC10	Japan	USA
1974	101.5	99.4	97.5	101.3	99.1	96.2
1976	106.8	103.5	99.5	108.7	114.4	100.8
1978	112.0	114.6	101.1	114.9	133.7	105.3
1979	114.5	119.0	100.7	119.9	146.3	105.3
1980	115.3	122.9	99.9	121.1	160.0	103.5
1981	116.3	126.6	101.4	124.1	168.4	106.4

Source: Based on OECD information, from "The Economic and social situation of the Community", Economic and Social Consultative Assembly, 1985.

According to the OECD standardised statistics, productivity in the economy as a whole and in manufacturing industry in particular has risen faster in the EC than in the

⁶⁷. Thomas Hatzichronoglou, "Mutations Technologiques et Compétitivité de L'Industrie Française: Dix Constatations", *Revue D'Économie Politique*, 95 année, 5, (1985), pp. 580-582.

United States, but slower than in Japan. Table 3.3 for productivity shows that the EC was at 116.3 in 1981 (based on 1973=100), compared with the United States' 101.4 in the same year, and for manufacturing industry the EC' was at 124.1 against the United States' 106.4 in 1981.

TABLE 3.4. TOTAL LABOUR COSTS, PRODUCTIVITY AND UNIT LABOUR COSTS IN MANUFACTURING: UK, USA AND GERMANY, 1971-1983 (UK = 100 at all time)

	USA				GERMANY			
	1971	1976	1981	1983	1971	1976	1981	1983
Total LC	236	209	146	186	151	208	145	160
LP	294	284	302	298	133	147	157	153
Unit LC	80	74	48	62	114	141	92	105

Note: LC: labour costs, LP: labour productivity.

Source: *National Institute Economic Review*, 110, (November 1984).

However, it has been noticed that this situation has often been accompanied by massive labour-shedding in declining European industries rather than by an expansion in the high productivity sectors.⁶⁸ In any event, labour productivity is higher in the USA than in Europe. Some studies suggested that the USA had much higher productivity than its European counterparts throughout the 1970s and most of the 1980s⁶⁹ (See Table 3.4). According to a UN industry and development global report about manufacturing, Japanese industrial production grew by 40 per cent from 1975 to 1983, the fastest growth rate

⁶⁸. "The Economic and Social Situation of The Community", p. 2; also see Edward Balls, "Too lean for a long life", *Financial Time*, (27 July, 1992), p. 12. "In the US the extension of service sector employment to increasing numbers of women may have partly caused aggregate productivity performance to drop." see Michael Emerson, *Europe's Stagflation*, (Oxford: Clarendon Press, 1984), p. 199.

⁶⁹. "Industrial Labour Costs, 1971-1983", *National Institute Economic Review*, 110, (November 1984), p. 64. Only two major European industrial countries were discussed comparing total labour costs, productivity and unit labour costs with the United States'. See also Vanessa Rossi, John Walker, Douglas Todd, and Kenneth Lennan, "Exchange Rates, Productivity and International Competitiveness", *Oxford Review of Economic Policy*, 2: 3, (1986), p. 58.

amongst the major industrial countries. None of the major European countries reached this rate. By contrast, Britain declined by 8 per cent in the same period (refer to Appendix T-3.1).

While European economic downturn was prolonged in the late 1970s, falling business confidence resulted in a fall in investment.⁷⁰ For example, European industry's investment in the Community's manufactured products decreased steadily from 16.7 per cent in 1970 to 11.9 per cent in 1978 (Table 3.5). The EC's rate of investment in the first half of the 1980s, the peak of Europessimism, was lower than the USA's and

TABLE 3.5. EUROPEAN INDUSTRY'S INVESTMENT IN THE EC

	1970	1972	1974	1976	1978	1980	1982
investment ratio	22.9	22.8	22.4	21.1	20.7	21.2	19.7
growth rate	6.2	3.6	-3.7	3.5	2.8	2.0	-1.3
manuf. products	16.7	14.6	14.2	12.5	11.9	...	...

Note: investment rate (gross fixed capital formation as % of GDP), growth rate (volume in %).

Source: Eurostat.

TABLE 3.6. THE INVESTMENT RATE OF TOTAL INDUSTRY IN THE EC, THE USA, AND JAPAN (current price in %)

	1975	1980	1981	1982	1983	1984	1985
EC7	12.9	13.2	12.3	11.4	11.5	11.8	12.4
USA	10.5	12.2	11.8	11.7	12.3	13.3	13.9
Japan	20.8	19.9	20.2	20.1	18.6	17.4	17.3

Source: *European Economy*, 25, (September 1985), p. 131.

Japan' (Table 3.6).⁷¹ In March 1982 the European Council expressed its concern at the level of productive investment in Western Europe, and then agreed with the need for the Community and each member state to take all necessary steps to

⁷⁰. *The Economic And Social Situation Of The Community*, p. 3.

⁷¹. Rate of investment in current prices in total industry, including strong demand, moderate demand, and weak demand industry.

reverse this trend.⁷² Among those obstacles to investment raised in a same report to the European Commission, the lack of profitability of European industry was most apparent (refers to Appendix T-3.1 which shows that the US and Japan had the best performance in value added manufacturing well above other major European economies in the years concerned).

TABLE 3.7. NET OPERATING SURPLUS AS A PERCENTAGE OF FIXED CAPITAL

	1960-73	1974-79
EC4	18.7	13.4
USA	29.1	20.6
Japan(gross surplus)	34.2	32.0

Note: EC4: France, Italy, the UK and West Germany.

Source: *European Economy*, 14, (November 1982), p. 153.

Also, Table 3.7 shows that the net yield on business capital in manufacturing industry was markedly lower in the EC4 than in the USA and Japan. It was due to low profitability of industry and increasing uncertainty over the economic situation. As investment decreased in the EC, eventually European industry as a whole was exposing itself as having an aging and inflexible industrial structure with which it could not keep up with the more innovative Japanese and American economies. European industries were concentrating too much on their short-term interests in existing markets rather than on the longer term, because they could not afford to invest cash into expanding production in competitive markets. Moreover, Japan and the USA have constantly invested in new labour-saving technology that will make manufacturing much cheaper, of better quality, and more efficient, whilst Europe has

⁷². "Commission Communication to the Council on the problem of investment", *European Economy*, 14, (November 1982), p. 151.

lagged behind.⁷³ (See Appendix F-3.1 & F-3.2 about the investment in plant and machinery, and robot population, which are considered very important factors for industry in the future.) In terms of the application of patents and the registration of industrial design, two indicators for industrial ability, Europeans were lagging far behind the gains of Japan and the USA in all items of patents considered. Even some NICs, Brazil and South Korea, were close to the European's performance in some industrial sectors (refer to Appendix T-3.2).

From 1975 to 1984, Japanese performance in industrial design was far stronger than any others' and South Korea had outstandingly achieved industrial design levels in line with those of European competitors (see Appendix T-3.3). Strong design ability gives industries a solid production basis from which to develop new products. The Japanese try to develop as short a life cycle of commercial products as possible in order to diversify against industrial competition simply by fortifying the design ability, innovation and development, as well as by marketing. On the contrary, European industries tend to remain operating in traditional markets with relatively low productivity and less innovative capability.

TABLE 3.8. EC EXPORTS TO DEVELOPING COUNTRIES (in %)

average annual change		share of extra-EC trade	
1970/60	4.9	1960	40.6
1980/70	18.2	1970	31.0
1989/79	5.8	1980	41.2

Source: *Eurostat: external trade - Statistical Yearbook 1990*, recapitulation 1958-89.

⁷³. For example, in American car industry one robot can do the work of up to six workers. While each employee costs US\$22-24 an hour, the robot can do all their work for \$6 an hour. *The Economist*, (March 24, 1984), p. 67.

During the 1970s, European industries were gradually losing overseas market shares, partly because of intensifying trade and capital transactions within the European market itself, rather than from expanding trade with developing countries (Table 3.8).⁷⁴ For example, during 1970 and 1982 the EC lost trade shares in advanced industrial goods to Japan (e.g. the share in ASEAN imports, SITC VII - machinery and transport equipment - in particular, see Table 3.9) in all major markets, even in its own common market. At the 1985

TABLE 3.9. THE SHARE OF THE EC IN ASEAN IMPORTS, 1970-1983 (in %)

	SITC 0+I	II	III	IV	V	VI	VII	VIII	Total
1970	12.8	3.3	2.3	9.3	35.5	12.2	31.5	22.3	18.9
1976	8.0	2.4	0.3	5.4	26.8	11.1	26.4	16.5	14.5
1981	9.6	3.5	0.4	3.7	26.0	11.7	18.9	17.6	12.2
1983									12.2

Source⁷⁵: Derived from UN, *Commodity Trade Statistics*, Series D, Various issues, *IMF 1984 Yearbook*.

TABLE 3.10. THE PERCENTAGE CHANGE IN MARKET SHARES OF THE EC, THE USA, AND JAPAN, 1973-1980

	EC	USA	JAPAN
Manufactured products:	-0.2	0.7	2.0
/steel	-1.7	-0.1	2.3
Equipment goods:	-0.7	-0.1	2.3
/office & telecom equipment	-1.0	2.2	1.8
/road vehicles	-3.7	-3.2	10.3

Source: *European Economy*, 14, (November 1982), p. 151.

ASEAN Ministers conference, it was suggested that the EC was "losing out to Japan and the USA in the prosperous markets of

⁷⁴. Rolf Langhammer raised five general factors which were in turn driving the trend of the EC trade within the EC itself. For details see *ibid.*, p. 143.

⁷⁵. Information based on Rolf Langhammer, "EEC-ASEAN relations: institutional deepening but modest economic impact", in Christopher Stevens and Joan Verloren van Themaat, eds., *Europe and the International Division of Labour*, EEC and the Third World: A survey 6, (London: Hodder and Stoughton, 1987), p. 141.

South-east Asia".⁷⁶ As regional trade blocs have developed, the trade diversion effect between the EC and the ASEAN has been going on for some time. While the former has concentrated on its intra-regional trade, the latter has become deeply involved in intra-Pacific trade networks. In extra-community trade in manufactured products, the EC's market share fell throughout the 1970s (Table 3.10), although its share was still larger than those of either the USA or Japan.

The Fear of A Widening Technology Gap

At the height of Europessimism, Western Europe recognised an inability of European industries to compete with their American and Japanese rivals, particularly in high technology industries. Nor could they see off the NICs' strong challenge in lower technology industries. The most obvious examples were those European "crisis sectors", i.e. steel, textile and clothing and shipbuilding industries, at the mercy of economic slowdown, diminishing demand and international competition.⁷⁷ Gradually, even electronics and electrical, motor, and information industries have relatively declined. Changes of European industrial export specialisation indicators from 1972 to 1983 saw electrical equipment and electronics decline by -0.08, transport equipment by -0.08 and information technology by -0.19, and changes of import specialisation over the same period saw their increase by 0.24, 0.20 and 0.23 respectively.⁷⁸

⁷⁶. *The Guardian*, (18 October, 1985), p. 8.

⁷⁷. See T. Hitiris, *European Community Economics*, 2nd edition, (London: Harvest Wheatsheaf, 1991), pp. 304-309.

⁷⁸. Import and export specialisation indicators are based on the calculation of imports or exports in a sector in one country over total imports or exports of that country by Volimex, DG II. Indicators here express the figures for the EC10 (excluding Portugal and Spain). See Commission of European Communities, "Competitiveness of European industry: situation to date", *European Economy*, 25, (September 1985), pp. 23. 27.

High-technology industry is supposed to be the guarantee of future prosperity. By the mid-1980s, Western Europe's share of high-technology products (aerospace, automatic data-processing equipment, electronic and electrical machinery, and telecommunications equipment) in the world market has fallen away sharply from its earlier stronger position. For example, Japanese export market share in the automatic data-processing equipment [Ⓢ] machine, electronic equipment, and telecommunication equipment, rose remarkably and hence left its major rivals, EUR 12 and the US, at the mercy of its powerful output. While in the scientific instruments, electrical machinery, and non-electrical machinery Japan's share also increased steadily from a quarter to one third of the market. The EUR 12 on the contrary lost quite a lot of market shares. The only exception was that the EUR 12 in aerospace had about a half of the market share and in chemicals dominated some three-fifth^s of the market in most of the recorded period (Refer to Appendix T-3.4). The perilous trend to Europe showed that the markets of automatic equipment and electronics telecommunications industries were dominated by Japan and of the aerospace industry by the United States. Moreover, European markets were severely penetrated by the Class 2 partners (developing countries) from index number 100 in 1980 to 244.9 in 1986, Asian NICs in particular.⁷⁹ That is in fact bringing gloom to its hope for a bright industrial future, as Japanese shares in many high-technology industrial products have surpassed the EC's in the first half of the 1980s.

In terms of lagging European technology, it refers European industry's weakness to research capability,

⁷⁹. See Appendix T-3.5 for details about the NICs penetrating the EC market in *Eurostat, Statistical Analysis of Extra-EUR12 Trade in Hi-Tech Products, 1989.*

availability of venture capital, skills in design and production management, quality control, reliability and service facilities, marketing arrangements, and consumer, corporate and governmental demand.⁸⁰ Simply, the industrial performance and market shares are the indicators to evaluate technology levels. Whereas, whatever the arguments concerned with the real content of the European technology gap may be,⁸¹ the technology gap could be simply reduced into two related fields: inadequate investment in R & D, and a weak ability for commercial application could be the reasons why Europeans have been unable to meet its rivals' challenge. According to the EC's figure, the Gross Domestic Expenditure on R & D (GERD) of EUR 10 as a whole was well over ~~the~~ Japan's in any year listed, although it was still far behind the American R & D

TABLE 3.11. GROSS DOMESTIC EXPENDITURE ON R & D AS A PERCENTAGE OF THE GDP: THE EC10, USA, JAPAN

R & D/GDP%	1975	1979	1980	1981	1982	1983
W. GERMANY	2.24	2.40	2.42	2.49	2.58	2.59
FRANCE	1.80	1.81	1.84	2.01	2.10	2.14
UK	2.10	2.28	2.31	2.42	2.34	2.27
EC10	1.81	1.87	1.89	1.99	2.03	2.05
USA	2.38	2.37	2.46	2.51	2.66	2.70
JAPAN	2.01	2.10	2.22	2.37	2.47	2.62

Source: "Europe and the New Technologies - Research, Industry, Social EC", Economic and Social Committee, 1986, p. 10.

spending. However, Japan's share of GERD in the GDP was not only growing faster but was larger than Europe's share (2.01

⁸⁰. Roger Williams, "The EC's technology policy as an engine for integration", *Government and Opposition*, 24: 2, (1989), p. 159.

⁸¹. John Marcum argues that European problem was not simply R & D, but inadequate investment in this field and widespread rigidities in many European institutions whose policy was aimed at preserving status quo rather than promoting change. Stanley Woods makes it clear that the problems were not really technological but derived from European political, social and economic rigidities which obstacle innovation. He points out that the crucial step to Europe for technological success is to exploit every single technologies commercially. Williams then concludes that "the technological area in which Europe most lags are consumer electronics, computers and telecommunications." *Ibid.*, pp. 160-161.

in 1975 to 2.62 in 1983 compared to Europe's 1.81 in 1975 to 2.05 in 1983) (see Table 3.11). In fact, the shares of the EC's three biggest countries, West Germany, France, and Britain of GERD in the GDP all exceeded 2 per cent at the period.

One EC study straightforwardly points out that this is due to the inadequacy of national science policy within the Community.⁸² The trouble not only results from some sort of governmental policy discrimination in public procurement but also from the overlapping investment in the same area. In other words, over-emphasizing big firms does not improve technological levels in general firms, which causes market strong players to stay stronger and weak players to remain weaker. Also, the rationale of individual countries' investment in R & D was that it was expected to be a means of improving its own competitiveness. Nevertheless, the assumption to some extent did not bring the EC as a whole an expecting ^{ed} upgrade of technology, but diminished the general + competitiveness of the EC because countries were virtually competing with one another within the EC rather than cooperating. Therefore, as far as the investment in R & D is concerned, much of the effort was offset by merely competing inside the EC markets, rather than international competition.

As an effect of Europe's fragmented markets, there was in the duplication of investment in the same R & D fields which caused "an appalling waste of resources" in Europe.⁸³ Each European country carried on R & D itself and developed its own design and evaluations to match different national standards. Therefore, their developed-products were rarely sold and

⁸². *Europe and the New Technologies, Research Industry Social*, Brussels 1986, R & D Industry Social Aspects, p. 10.

⁸³. "Europe's Technology Gap", *The Economist*, (24 November, 1984), p. 109.

applied to the other countries. In the end, Europe was not only wasting "human resources" in doing the same things, but also mutually diminishing market ability itself. Moreover, while Japan spent US\$1.5-2 billion on R & D for the latest generation digital switches and North America spent some \$3 billion, Western Europe used up more than \$10 billion on 10 different switching systems.⁸⁴ Mr. Malcolm Ross, with the management of consultant firm Arthur D. Little in Wiesbaden, estimates that "Western Europe used three times as many hardware and software engineers as either North America or Japan in developing its switches."⁸⁵

Apart from the R & D investment, commercialising ability is also a critical factor for the industrial future. In other words, "to achieve the effect science and technology requires to be translated into innovation".⁸⁶ Whatever R & D is, the most important thing is to commercialise research programmes and hence to back industrial production. In fact, this is what the industrial competition of developing technology is all about among industrial countries. Nonetheless, European countries do not seem to meet this requirement for developing high-technology products. The amounts of patents' application among main industrial countries show clearly the industrial ability for innovation in each country (refer also to Appendix T-3.2). Japan has emerged as the fastest growing innovative economy in the world. With its difficulties in many existing industrial circumstances, Europe's inability to lead competition became ever more obvious.

Weakening Industrial Competitiveness

Industrial competitiveness is a critical factor in industrial survival. In other words, it is a key item in

⁸⁴. Ibid.

⁸⁵. Ibid.

⁸⁶. Roger Williams, "The EC's technology policy as an engine for integration", p. 161.

profit-gaining and market sharing. Industry should obtain a more competitive position, at least, by enjoying either comparative advantages of low costs in production processes and outputs, or the quality of technology. That is to say that the demand of consumers for goods is dependent upon "prices, quality and the novelty of the goods on offer."⁸⁷ By all means, to improve competitiveness, corporations focus on reducing the cost of production including advancing technology, for an effective production on the one hand, and improving the technology to upgrade the quality and to accelerate innovation of their products on the other.

The EC's loss of its industrial competitiveness to its rivals became apparent in the early 1980s. Most accusations about the decline focused on the EC's uncontrollable high costs of production which derived from the rapid increases of wages and low productivity, although Western Europe was hit by high inflation.⁸⁸ The Confederation of British Industry (CBI) warned in March 1985 that "British wages are rising too fast, productivity is increasing too slowly". The worrying evidence of the nation's declining labour cost competitiveness raised by the CBI in 1985 was that "the increase in earnings in manufacturing industry last year averaged 8.5 per cent compared with 6.5 per cent in France, 4 per cent for Japan and the USA, and 3.5 per cent for West Germany."⁸⁹ However, the British case was merely a molehill compared to the mountain of European problems with industrial structures, particularly

⁸⁷. Pierre Buigues, and Philippe Goybet, "Competitiveness of European Industry: Situation to Date", *European Economy*, 25, (September 1985), p. 17.

⁸⁸. As a matter of fact, one authority argued that the over-valued exchange rate of European countries also contributed a lot to the high price economic structure which resulted in their industry less competitive. Ann Morgan, "Protectionism and European Trade in Manufactures", *National Institute Economic Review*, 109, (August 1984), p. 48.

⁸⁹. "CBI issues pay and productivity warning on Budget eve", *The Times*, (18 March, 1985), p. 2.

wage settlements and productivity.⁹⁰ Moreover, Mr. Kaspar Cassani, the head of International Business Machines (IBM), launched an attack on the uncompetitiveness of European labour arguing that high wage rates were paralysing industry with regard to employing labour and expanding business.

TABLE 3.12. EARNINGS PER HEAD, LABOUR PRODUCTIVITY, AND REAL UNIT LABOUR COSTS (1972 = 100)

	<u>Earning</u>			<u>Productivity</u>			<u>unit labour costs</u>		
	EUR7	USA	JAP	EUR7	USA	JAP	EUR7	USA	JAP
72	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
75	113.7	102.7	119.4	107.3	102.3	109.2	106.0	100.4	109.4
80	129.6	111.4	142.9	129.7	111.5	171.3	99.9	99.9	83.4
81	131.6	111.6	148.7	133.1	115.0	179.5	98.9	97.0	82.8
83	134.3	114.9	161.3	142.0	118.7	196.6	94.6	96.8	82.0
85	138.7	117.5	175.8	155.8	125.1	223.6	89.0	93.9	78.6

Note: EUR7: Belgium, Denmark, France, W. Germany, Italy, the Netherlands, and the UK.

Source: *European Economy*, 25, (September 1985), pp. 126, 128, 129.

The unit labour cost which is dependent upon the relationship of earnings per worker and labour productivity is a key indicator of competitiveness.⁹¹ Although Japan has got the fastest growing rate of earnings per worker in companion with EUR7 and the USA in all relevant categories, in the period recorded in Table 3.12, it has also had the highest productivity rate in relation to the others. In addition, the USA during most of the time recorded had the higher growing rate of productivity relative to the earnings per worker, which made the Americans competitive. Therefore, EUR7 as a

⁹⁰. For the detailed discussion of wage settlements and comparative Japanese and British systems see Neil Dunn, "The Japanese 'Shunto': Are There lessons for the UK", *The Royal Bank of Scotland Review*, 151, (September 1986).

⁹¹. Exports prices are determined by the unit labour cost, all other non-labour costs and the marketing policy of exporters including the profit which exporters wish to make on their sales abroad. Among them the unit labour cost is purely decided by the production factors. "Industrial Labour Costs, 1971-1983", *National Institute Economic Review*, 110, (November 1984), p. 64. For those principal factors affecting industrial competitiveness see C.-René Dominique, and Muhittin Oral, "Exporting to Northern markets: the making of an industrial competitiveness index", *Industry and Development*, (Vienna), 18, (1986).

whole was repeating the British story in terms of waning competitiveness, as a result of increasing unit labour costs to industry which resulted from relative high earning rates and low productivity. In fact, high European prices were derived not only from the cost of production and inflation, but also from the overvalued exchange rate.⁹² In addition, some focuses on market share in terms of industrial competitiveness point out that:

"A country's industrial competitiveness rests on its ability to retain and expand its shares of world markets and to maintain a balance on its domestic market between imports and national output that is compatible with its exports performance."⁹³

Concretely, Buigues and Goybet's traditional assumption (domestic demand = output - exports + imports) highlights domestic market demand as an indicator to assess the competitiveness of the EC countries and their main partners in market share of categorised sectors. According to the formula, the fluctuation of exports and imports implies a changing trend of demand market from which competing market shares could be shown. Therefore, the growth of Japanese penetration into the EC market in all industrial sectors could be directly read from the market demand's data. By contrast, the market share structure of the EC as a whole has no longer focused on high and moderate demand industries but on weak demand industries.⁹⁴ Another supplementary development with regard to

⁹². For discussion of the overvalued European exchange rate see Morgan, "Protectionism and European Trade in Manufactures", p. 48. Within the EC market, as a result of establishing the common market, the prices of goods have been fixed in the common market high prices system to protect European producers at the expense of general consumers' interests in enjoying lower world market prices. See T. Hitiris, *European Community Economics*, 2nd edition, (Hemel Hamstead: Harvester Wheatsheaf, 1991).

⁹³. Buigues, and Goybet, "Competitiveness of European Industry: Situation to Date", p. 11.

⁹⁴. Ibid.

competitiveness could be reflected in the sliding market share of Europeans in international business. According to *Fortune International*, ranking the 500 largest corporations outside the USA by their nationality, Japan and some NICs, particularly, in the period of 1975-1985 gained their increasing trends steadily, and the EC9 as a whole obtained almost an half of the 500 largest corporations in 1975, but decreased to just over two-fifths of them in 1985. (Table 3.13)

TABLE 3.13. 500 LARGEST INDUSTRIAL CORPORATIONS OUTSIDE THE USA (1975-1985)

	1975	1976	1978	1980	1982	1984	1985
Japan	122	117	125	121	134	150	147
EC 9*	242	232	233	229	221	295	204
NICs 4**	9	14	20	25	21	23	23

Note: *: Belgium, Denmark, France, W. Germany, Ireland, Italy, Luxembourg, the Netherlands, UK.

** : Brazil, Mexico, South Korea, Taiwan.

Source: *Fortune*, (August 1976-August 1986).

To gain more market shares, apart from reducing the cost of production, corporations and national governments have been undergoing high-technology development efforts, as a part of targeting strategy to upgrade the existing technology for more effective production processes and better quality of products. Joint ventures, strategic partnerships, and other forms of co-operation are equally important for industrial prospects to market share and the cost of developing technology, as well as to obtain advanced technology. European economies were inclined to an inward-looking trend which, as many protectionists believe, could allow them to be shielded from international competition. From international business and free economics points of view, international competition could

bring about a necessary growth of industry's scale and also an industrial rationalisation. Thus, the more a company presents in a competitive market, the better industrial structure it will be. Consequently, the Community's ability in many areas to compete in future was under threat. In general, the Community's loss of competitiveness implied a loss of comparative advantage in many areas and an inadequate scale of production.⁹⁵

The EC's inability to meet industrial competition, in effect, drives its firms to industrial unity and to a large extent to economic integration. For many, particularly big firms such as Philips, Siemens, Nixdorf, Bull, ICI, Ericsson and Olivetti, community-level research is the right, perhaps the only, direction in which to resurrect the lagging industries. The message directly coming from those big firms was that "no single European country alone was independently able to develop a technology policy to win the support of multinational industries."⁹⁶ Wisse Dekker, went further that "the only form in which a European industrial policy is possible is on a Pan-European level."⁹⁷ The supporting arguments can therefore be summarised as follows: 1. The nature of communication and market scale. Some R & D fields are heading to a transnational action and a potential larger market. 2. Sharing financial burdens. It has become necessary to spread the costs and risks because many research projects are beyond the financial and human means of an individual country. 3. Long-term character. Instead of national governments' short and medium-term projects, the Community offers an opportunity for dealing with structural problems. 4. Reasonable use of limited resources. The Community can ensure

⁹⁵. The most serious areas are consumer goods, of which clothing and textiles are the most important, and certain engineering products, such as cars, consumer electronics and those advanced technological components concerned. For full discussion see Morgan, "Protectionism and European Trade in Manufactures", p. 57.

⁹⁶. *Financial Times*, (25 April, 1985), p. 1.

⁹⁷. *Ibid.*

optimal use of rare resources within the EC, and prevent the duplication of efforts. 5. The development of new common policies. The Community R & D can be used to underpin the EC's sectoral policy and to tie national vital interests to Europe's future. 6. A catalytic effect to integration. The Community level R & D is not only integrating national policies by aggregating scientists and research teams and by improving the dissemination of information and research results inside the Community, but also facilitating R & D results to be converted into commercial goods and be applied in the common market.⁹⁸

3.2.2. European Industry Countering External Challenges

The changing international industrial structure has had a destabilizing effect on European industry,⁹⁹ because:

"many firms have not perceived the implications of these structural transformations early enough and some countries have persisted in massively investing in heavy industries with limited world demand prospects at the very moment these industries are taking-off in some LDCs. Simultaneously, investment in new high-technology industries, like electronics, have not been sufficient to compensate for other sectors' difficulties."¹⁰⁰

The fragmented markets within the EC with different national regulations on tax, and the movement of labour, goods and capital even worsened industry's competence against industrial competition. Facing the "Uncommon Market", West European industry's long-term prospects were not rosy. Therefore, in

⁹⁸. For more detailed discussion about all arguments above see *European File*, N. 11/79, "Science, Research and the European Community", (June 1979).

⁹⁹. Jacques Lesourne, "The changing context of industrial policy: external and internal developments", in Alexis Jacquemin, (ed.), *European Industry: Public Policy and Corporate Strategy*, (Oxford: Clarendon Press, 1984). The author has very detailed description of the new economic context facing European industry.

¹⁰⁰. *Ibid.*, p. 21.

response to international competition, West European industry began to focus more closely on its home market and to depend on protectionism. As a result, the recession got much worse. With the rise of the competitive challenge from East Asia, it was evident that national strategies were not going to draw Europe out of recession. It became apparent that European business would have to become more competitive in international markets, if it was going to survive.¹⁰¹ It seemed that only by expanding industrial scale economies through the creation of a single European market - to unify the fragmented national markets, could the European Community build up a solid economic basis for international competition. The idea encouraged the EC member states to start to pool their resources to advance technology, to share capital markets, services, and labour.

In 1981, the Commissioner for internal market, Vicomte Davignon, brought together a group of large European information technology firms to form the Thorn-Davignon Commission, which was not only to develop proposals for technology matters but also to consider liberalising the European market. The projects in this pioneer mission of forming the ESPRIT were generally co-funded by the EC and industry on a fifty/fifty basis. More importantly research results were shared between all participants of the projects.¹⁰² Significantly the ESPRIT brought about the effect of creating "an important constituency amongst business pressing for the completion of the internal market" and was

¹⁰¹.Such as Wayne Sandholtz, and John Zysman, "1992: Recasting the European bargain", *World Politics*, 42, (October 1989).

¹⁰².Margaret Sharp, "The Single Market and European Policies for Advanced Technologies", p. 108.

proved to be "a catalyst to a far wider reorganisation of European industry."¹⁰³

In the private sector, the European Roundtable united business interests to lobby the Commission in Brussels.¹⁰⁴ The Roundtable's "Memorandum", which stressed the most important issues facing European industry, served as a basis for supporting the Commission during the debates in the Stuttgart Summit of the European Council in June 1983.¹⁰⁵ In its grand design for upgrading Europe's transborder transport infrastructure, the Roundtable paid close attention to Europe's cross-border weakness from which Europe's economic and social development had suffered. The Roundtable emphasised that:

"To be competitive, Europe's industry must extract more productivity from its invested capital. Europe's international businesses must not be prevented from achieving economies of scale and optimum marketing and manufacturing strategies by shortcomings in transport and unnecessary frontier bureaucracy. Equally, Europe can only become a thriving, unified market if there is the freest possible movement of goods, people, capital and ideas."¹⁰⁶

Wisse Dekker quoted a Japanese view of a future scenario in which America will be providing the world with food as the granary, Japan with its Far East partners will become the world's supplier of industrial products and Europe will be the cultural museum of the world. European industry was lagging

¹⁰³.Ibid., p. 116.

¹⁰⁴.The European Roundtable, previously the Roundtable of European Industrialists, was established in 1983 and chaired by Perh Gyllenhammar, the CEO of AB Volvo. After Wisse Dekker, Philips' Chairman, took the chairmanship in 1988, the headquarters has since been moved to Brussels from Paris, which the change has led the Roundtable to become "pan-European" in its approaches to European integration. See Axel Krause, "Many groups lobby on implementation of market plan", *Europe*, (July/August 1988), p. 25.

¹⁰⁵."Achievements of the European Roundtable", mimeograph, by European Roundtable, (May 1988).

¹⁰⁶."Missing Links: Upgrading Europe's Transborder Ground Transport Infrastructure", A report for the Roundtable of European Industrialists, (December 1984).

behind in the technological race especially in information technology. Furthermore, in 1985, he identified some hard facts facing the EC, e.g. unemployment, the deterioration of competitiveness, zero return for the private sectors; and working times too short.¹⁰⁷

While many businesses in Europe were losing profits and market share, and some were even dying out, Japan and the Asian NICs were filling the "market vacuum" with their rapidly advancing technology and low cost production at the expense of EC industry. To cope with this challenge, Dekker believed that an internal market of continental scale based on free movements of goods and services would have a beneficial effect on Europe's competitive position. He explained how important it was to assist industry:

1. In the first place, economies of scale are needed to cover the gigantic rise in research and development costs which are characteristic of modern technology and which exceed the scope of national markets.

2. In the second place, increases in scale are necessary in order to arrive at competitive cost prices in Europe, because economies of scale and speed of growth are also the strategic elements used by our competitors world-wide to exploit the learning curve effect.

3. In addition, a homogeneous infrastructure based on uniform European standards will be an important stimulus to the rapid application of innovative products and systems and of new technologies in Europe.

¹⁰⁷. "The EC has 12.5 million unemployed, many of them young people. Its relative competitive position on the world market has deteriorated, because of its productivity lagging behind wages increases by 10% in the last 10 years. The percentage of social charges in wage and salary costs is about twice those of its competitors in Japan and the USA. A booming bureaucratic governmental culture, which absorbs more than half of the GNP to settle two third of total number of civil servants for producing translations, needs to be reconsidered. The combined results of the largest 100 companies in Europe (excluding oil) in 1980 show a profit level of 0 per cent. Working times in the EC are to be shortened to 1400 hours per year, whereas Japanese competitors work 2100 hours, and the Koreans work 2800 hours per year. The epicentre of world trade is shifting from the Atlantic to the Pacific Ocean." "Europe 1990", speech given by Dr. W. Dekker, at the Centre for European Policy Studies in Brussels, 13 November 1984, on the occasion of the presentation for the programme "Europe 1990 - an agenda for action".

4. Advantages of scale and rapid application in the market are equally important for the small and medium sized companies, since it (the single market) fosters the development of a good subcontracting and suppliers' climate in which high-level specialisation can thrive.

5. Economies of scale and European uniformity would remove many of the uncertainty and doubts which exist among financiers, constructors and those who exploit high-technology development strategies.

6. The combination of free goods traffic and homogeneous standards on a European scale would result in a great reduction in stocks, bring down cost prices and improve the competitive position.

7. Consensus between economic partners is increasingly developing into an additional production factor. A really homogeneous Common Market would constitute the basis for such a European consensus."¹⁰⁸

Having examined a wide range of measures and proposals from the Roundtable for improving industrial performances, the Commission clarified four key areas for action to improve the international competitiveness of European firms.¹⁰⁹ All these suggested actions were later incorporated in the White Paper - "Completing the internal market". Institutional change, transnational business interest groups, national politics, and elites' alliances seemed to be the determinants of the successful negotiation for the SEA.¹¹⁰ But, the question also arose as to why the Commission was so enthusiastic about the creation of the single market at that moment, while national governments were reluctant to discuss further integration in any direction. The dynamic Commission was, to a large extent, bolstered by the support of European industry for facilitating

¹⁰⁸.Ibid, p. 4.

¹⁰⁹.European Commission, "Community measures to improve the international competitiveness of European Firms", COM(83)578 final, 29 September, 1983. Four key areas were: improving the economic and monetary context, dynamic use of the internal market, scientific research and the development of advanced technologies, and energy policy.

¹¹⁰.See Sandholtz and Zysman, "1992: Recasting the European bargain"; and Paul Taylor, "The new dynamics of EC integration in the 1980s", in Juliet Lodge, (ed.) *The European Community and the Challenge of the Future*, (London: Pinter Publishers, 1989).

integration, more precisely by industrial leading groups, the Roundtable and the UNICE, and it was this friendly alliance which proved to be vital for the passage of the SEA. Indeed, before the European Council actually reached a consensus on the framework for progress to the future integration, European industrialists had put their proposals through the Commission and individual national governments.

3.3. EUROPEAN INDUSTRY, THE COMPLETION OF THE INTERNAL MARKET, AND EUROPEAN INTEGRATION

3.3.1. The Need for the Completion of the Internal Market and the Formation of an Industrial Coalition

It was that change of international economic structure in the 1970s and early 1980s, which served as an external factor striking the European economy and brought about the rallying of industry, which has contributed to progress to the completion of the internal market and the SEA, as well as integration in general. Although it is still in question how far the importance of industry, or "transnational business interest", is to the above progress, many have confirmed industrial implications for the revitalisation of European integration.¹¹¹ It may be that the argument of industrialists' influencing the decision-making of the EC, at both the Community and national levels, has not been noted clearly enough, because informal communication between industrialists

¹¹¹ Moravcsik, "Negotiating the Single European Act", pp. 67-68, pointed out that transnational business interest was "ineffective" to the negotiation. However, there are many more confirmations taking the opposite view. Such as Sandholtz, and Zysman, "1992: Recasting the European Bargain"; and Lord Cockfield in an address to the London Europe Society, *Europe 85*, (November/December 1985), pp. 17-18.

and the EC decision-makers has been essentially "the most influential mode".¹¹²

As a result of European response to economic downturn during the late 1970s and early 1980s, protectionism, undertaken, to a large extent, at the national and the Community level, emerged as a means of shielding those uncompetitive industries and their related interest groups from external competition. New protectionism noted as using non-tariff barriers was caused by economic recession, intensified by two oil shocks; by the emergence of new economic powers (Japan and the NICs); by technological change; and by the advent of floating exchange rates.¹¹³ To cope with this turbulence, European countries were inclined to dismiss their commitment to the Community of transnational management. Instead, they continued the "national champions" strategy¹¹⁴ with direct governmental intervention, which "had increased the perceived diversity of national situations and competition among European states."¹¹⁵ The new protectionism in Europe was quietly imposed on most external suppliers ranging from quota restrictions through "voluntary export restraint" (VER) and orderly marketing arrangements to allow certain industries and firms to be subsidised. As a result, even European industries themselves were also hindered by the rising trade barriers of their neighbouring countries.¹¹⁶

¹¹² Keith Richardson, Secretary General of the European Roundtable, confirmed this communication behind the political scene. See his "Europe's industrialists help shape the Single Market", *Europe*, (December 1989), p. 19.

¹¹³ Jean Pearce, "Europrotectionism: the challenge and the cost", *The World Today*, (December 1985), p. 225.

¹¹⁴ "National champions" strategy, which was motivated by the need to resist the American challenges in France in the 1960s, was to develop firms to be large enough to compete under the auspices of national governments. For example, big firms such as Fiat in Italy, Renault and Saint-Gobain in France have the right to claim government subsidies. See Ezra Suleiman, "Industrial policy formulation in France", in Warnecke, and Suleiman, (eds.), *Industrial Policies in Western Europe*, p. 31.

¹¹⁵ Keohane and Hoffmann, (eds.), *The New European Community: Decisionmaking and Institutional Change*, p. 22.

¹¹⁶ Morgan, "Protectionism and European Trade in Manufactures", p. 45.

There has been always an argument within the EC about whether or not to raise protectionism against imports from other countries. Indeed, the fear of trade retaliation from the rest of the world, and the relatively smaller share of imports in the Community than in national expenditure, have made protectionism less likely at the Community level.¹¹⁷ The "Poitiers effect", for example, was just one of the cases of European national protectionism against all imports including those from other "fellow member states of the EC" into a domestic market. While aiming at the "Japanese invasion" in consumer electronics, the French government in October 1982 ordered that all imports of video cassette recorders (VCRs) would have to pass through the customs of its inland city, Poitiers, all the VCRs imports were seriously delayed by the custom's insufficient ability. Not only were the Japanese products suffering from a non-tariff barrier, but also other European VCRs producers in Denmark, West Germany, and the Netherlands were hurt.¹¹⁸

Apart from its lagging technology development and weakening productivity, European industry was unable to compete with the American's and Japan's because of insufficient market scale and their relatively heterogeneous markets. The common market of the EC was actually composed of several fragmented markets which had inevitably cost Europe a slowing pace of economic development.¹¹⁹ As national interests were put in first place, the continued use of barriers at a

¹¹⁷.Ibid., pp. 56-57; also the White Paper of the Commission pinpoints that the remaining national protectionism which has worsened the European economy in the recession, will have to be cleared away. See Commission of the European Communities, "Completing the Internal Market", White Paper from the Commission to the European Council, p. 5.

¹¹⁸.This well known case was then cited as the "Poitiers effect". For detail see *World Development Report 1987*, The World Bank, p. 141.

¹¹⁹.For the details of the unnecessary cost paid due to market fragmentation in the EC see the analysis with related policy in Pelkmans, "Completing the internal market for industrial products", pp. 21-27; also the EC official assessment of the cost see Cecchini, *The European Challenge: 1992 The Benefits of A Single Market*, part 1.

number of national borders caused additional costs in many areas that can be summarised as follows:

"high administrative costs caused by national bureaucratic requirements; high transport costs due to delays at borders; high costs due to different national standards for goods; the duplication of work on separate Research and Development programmes; intervention by national governments, preventing open competition; national markets keeping costs artificially high and reducing choice for consumers; and economic expansion limited by the inability to spread across borders."¹²⁰

Two economists, Jacques Pelkmans and Alan Winters, in 1988 suggested that "static losses in the markets for goods for around ECU 10 billion per annum due to border measures and ECU 15 billion due to public purchasing biases... ."¹²¹ Moreover, the fragmented markets in the EC had substantially hindered any possibility of developing higher technology in cooperative form, because research and development for higher technology by any single country would again expose the vulnerability of all separated individual national markets to their principal rivals, Japan, and the USA. What appeared to be necessary for the European economy and industrial competitiveness was to complete a single market, which would encourage pooling enough capital for R & D and sharing the risk of technology development as any individual country would be unable to compete with such technological development based on a region of the market size of Japan and the USA. In March 1985, a Commission's report on strengthening industrial bases clearly pointed out this weakness of European industry.¹²²

¹²⁰.International Business Intelligence, *1992-Planning for the Engineering Industries*, (Butterworth & Co. Ltd and Eurofi Plc., 1989), p. 4.

¹²¹.Pelkmans, and Winters, *Europe's Domestic Market*, p. 53; for the details of the national barriers which existed then and their likely costs, see Chapter two, pp. 16-53.

¹²².Commission of the European Communities, "Strengthening the technological base and competitiveness of Community industry", COM(85) 84 final, (19 March, 1985), pp. 1-2.

Moreover, national policies on implementing individual standards, technical regulations, industrial subsidiaries, and protected markets for public procurement were encouraging "the national character of industrial structures and the fragmentation of the common market."¹²³ To prevent these national approaches from further jeopardising European hopes for facilitating technology, the Commission in 1985 firmly decided to launch a new programme - "Towards a European Technology Community", through two main approaches: to complete the internal market, and therefore to make better use of the unified market by states in order to enable industry to be competitive.¹²⁴ The needs for a single market to improve industrial competitiveness were wide spread right across Europe.

During the first half of the 1980s, the European Council had repeatedly pledged to complete the internal market as an essential to advancing European integration. In 1982 at the Copenhagen summit, the European Council decided that "before the end of March 1983, on the priority measures proposed by the Commission to reinforce the internal market." That decision resulted in the Internal Market Council. Its first meeting was in January 1983. Lord Cockfield recalled that its work was "fragmentary and insufficiently focused", because it lacked a complete programme to satisfy all and a timetable to press ahead.¹²⁵ In agreeing to the Solemn Declaration on European Union in 1983 in Stuttgart, the heads of state or government confirmed their commitment to "the completion of the internal market ... in particular the removal of the

¹²³.Ibid.

¹²⁴.Ibid., p. 2; also Commission of the European Communities, "Towards a European Technology Community", COM(85) 530 final, (30 September, 1985).

¹²⁵.Lord Cockfield, "The real significance of 1992", in Colin Crouch and David Marquand, (eds.), *The Politics of 1992: Beyond the Single European Market*, (Oxford: Basil Blackwell, 1990), pp. 3-4.

remaining obstacles to the free movement of goods, capital and services" and called for developing common policies at the Community level in transport, commerce, development and industry.¹²⁶ In June 1984 at Fontainebleau, the European Council asked the Council and the Member States to study the measures which could lead to "the abolition of all police and customs formalities for people crossing intra-Community frontiers..." In December 1984 in Dublin, the European Council agreed that the Council should take steps to complete the Internal Market."

Further, in March 1985 in Brussels, the European Council emphasised "action to achieve a single market by 1992 thereby creating a more favourable environment for stimulating enterprise, competition and trade."¹²⁷ Most initiatives in front of the European Council significantly highlighted improving the economic situation and industrial competitiveness, although they very much tended to more political approaches, e.g. the Genscher-Colombo initiative and 1983 Solemn Declaration of European Union in Stuttgart.¹²⁸ The heads of state and government endorsed the White Paper in June 1985 at the Milan summit, in which the Paper carried forward the internal market programme into the SEA. The completion of the internal market provided the trigger for the SEA to endorse a whole range of policies which had been agreed in the Solemn Declaration of Stuttgart.¹²⁹ It is conceivable that the most critical issues in front of most national governments,

¹²⁶ "Solemn Declaration on European Union", *Bulletin of European Communities*, 6, (1983), p. 27.

¹²⁷ Refer to various declarations by the European Council to the Commission of the European Communities, "Completing the Internal Market", White Paper from the Commission to the European Council.

¹²⁸ See "Revitalizing European Union", *Bulletin of European Communities*, 11, (1981), p. 10; and "construction of Europe must be more clearly oriented towards its general political objectives..." see "Solemn Declaration on European Union", p. 25.

¹²⁹ Lord Cockfield, "The real significance of 1992", p. 5.

prior to negotiations of the SEA, were to get the "internal market" programme and the supports for the necessary EC decision-making reforms through legal confirmations. The multinational negotiations for a single act were therefore intend to achieve that target and to bargain for each national interest in a European agenda.

Wisse Dekker in a speech pointed out that "the economic recession and the pressure of both Japanese and American competition have created a better climate for making people aware of the need for a Community approach in Europe."¹³⁰ Indeed, the mounting general concern with the weakness of European economy and its industrial performance, devoted much attention to the economic policy cooperation at both European and national levels, which had raised the major interest in European integration. Belief in actual advantages of the single market and further integration could provide the only solution for European countries to sort out their economic and social difficulties. What the political commitment of the member states to the SEA implied was that the real impetus towards the completion of the internal market was not directly derived from the political consensus obtained by the 33rd European Council in the Luxembourg summit in 1985, but very much relied on the recognition of economic realities. Giovanni Agnelli, the Chairman of Fiat, stated that:

"[T]he current unity of Western Europe is not so much the result of a utopian dream as it is the political recognition of economic reality: the reality of global markets, the reality of economic interdependence and the

¹³⁰ "Europe 1990" speech by Dr. W. Dekker, President of N. V. Philips' Gloeilampenfabrieken, at the Centre for European Policy Studies in Brussels, 13 November 1984, on the occasion of the presentation of the programme "Europe 1990 - an agenda for action", pp. 9-10.

reality of competitive pressures - all of which make cooperation essential."¹³¹

Until Europeans realised their loss of industrial competitiveness in world and home markets, they would not commit themselves to the unity of industrial, and economic development at Community levels. Indeed, prior to the context of European politicians' alliance with industrialists in the 1980s, the European business community was often objecting to the concept of the common market brought about by politicians. It was the change in international competition and the advance of high technology that reversed the situation in which European industrialists "are keeping the pressure on politicians to transcend considerations of local and national interest."¹³² Carlo de Benedetti, the CEO of Olivetti and one of the active figures in the Roundtable, states directly that:

"the need for change was recognised much later by politicians than by the Italian business community, which had already begun to access other European markets to achieve a European dimension. Today, industry, banks and consumers are putting pressure on the politicians to implement the project of the single European market by the established deadline."¹³³

The reasons why the Single Market plan, or, to some extent, European integration has been making such remarkable progress since the mid-1980s were that "the business community has shown much more vigorous support for the building of Europe in the 1980s than ever before."¹³⁴ Although the signing of the SEA and the integration progress thereafter have shown

¹³¹ Agnelli, "The Europe of 1992", in Jeffrey A. Frieden, and David A. Lake, (eds.), *International Political Economy: Perspectives on Global Power and Wealth*, (New York: St. Martin's Press, 1991), p. 424.

¹³² Ibid.

¹³³ Benedetti, "Europe 1992 is a necessity for Italy and Europe", *Europe*, (April 1989), p. 39.

¹³⁴ Richardson, "Europe's industrialists help shape the single market", p. 18.

a great step forward towards the European Union, the fulfilment of the 1992 programme remains appropriate for sound economic reasons and thus confirms the importance of industry engaging in the process of initiating the Single Market. However, the completion of the internal market has implications for making a favourable business environment in the EC which the national governments of the twelve have been encouraging and for which their industry has long lobbied. In early 1985, the Davos Symposium suggested that "all governments are becoming aware of the importance and the necessity of the entrepreneurial spirit" and "their new role will be to create the conditions which will guarantee maximum business dynamism."¹³⁵ In addition, Delors' inaugural address to the EP also highlighted that the Commission proposed to take actions in three directions: "a large market and industrial cooperation, the strengthening of the European Monetary System, and the convergence of our economies to lead to higher growth and more jobs."¹³⁶

3.3.2. The Involvement of Industry in the Process of European Integration

Industrialists' eagerness to pursue the single market was based on the prospects for business interests. Their efforts for the completion of a single European market have, to a large extent, contributed to relaunching European integration. In the period of evolving the single "Act", industrial development became one of the crucial factors for European

¹³⁵.The Davos Symposium, organised by the Economy World Forum, presented jointly by European leaders and heads of business. For details see "How to overcome 'Euro-sclerosis': a report on the Davos Symposium", *Europe 85*, (May 1985), pp. i-ii.

¹³⁶. "We shall be saying no to scepticism, no to defeatism, and no to all excuses", *Europe 85*, (January/February 1985), p. 6.

integration, as programmes studied by the Commission about industrial competitiveness and technology had suggested that strengthening industrial bases in a single market environment could raise hopes for the advancing European development on which European integration is dependent. Lord Cockfield emphasized that:

"[T]he people whose interests are the most directly affected are not governments at all. but trade and industry. They have to generate the wealth (but) governments merely dissipate it. Their views should be the decisive factor, not the views of government."¹³⁷

In 1983, the year of European economy at its ebb, the European Roundtable emerged as a spearhead for industry. Its objective, described by Keith Richardson, its Secretary General, is "to strengthen Europe's economy and to improve its global competitiveness, which it pursues by identifying the most important issues, analyzing the critical factors, and making its views known to the political decision makers."¹³⁸ The Roundtable's weight with the EC officials derives not only from the economic power its members have held right across Europe,¹³⁹ but also from "the organisation's seminal role in launching the 1992 programme."¹⁴⁰ The ERT has been carrying out various studies in critical issues, e.g. its "Memorandum", "Missing Link" for financing infrastructure development, "Making Europe Work" for unemployment, and "Clearing the

¹³⁷. "Making a real Common Market: Lord Cockfield points the way to the future", p. 18.

¹³⁸. Richardson, "Europe's industrialists help shape the single market", p. 19.

¹³⁹. Although the European Roundtable had only 40 members (for details see Appendix T-3.6) in 1987, these businesses combined sales worth \$400 billion a year, and more than three million workers on their payrolls. Their influence on economic and industrial policy is considerable. See Keith Richardson, "Europe's industrialists help shape the Single Market", pp. 18-20. Refer Appendix T-3.6 to Appendix T-3.4 the change of the EC market share, the industries which suffered the most became the most active lobbying groups.

¹⁴⁰. James N. Gardner, *Effective Lobbying in the European Community*, (Deventer, The Netherlands: Kluwer Law and Taxation Publishers, 1991), p. 47.

Lines" for business communication, which have been the common vision of European industry and have been incorporated into the wider Community's development.¹⁴¹ For example, the "memorandum" written on request of the then Commissioners, Davignon and Ortoli, advocates industrialists' support for the Commission during the debates in the Stuttgart summit in 1983.¹⁴² The "Missing Link" report provoked a joint EEC-ERT task force which was set up by the Commission in order to generate more private capital in infrastructure development, which has resulted in the creation of "Financial Engineering" in Directorate II of the Commission.¹⁴³

The more influential ways to speak out on behalf of industry have been direct communication between the Roundtable and the EC and national decision-makers. The Roundtable may send a representative group "to meet the Commission to discuss a whole range of major policies, or talk to an individual Commissioner about a single thorny issue."¹⁴⁴ Moreover, every six months, it discusses priorities with senior ministers or the Prime Minister of the government's Presidency of the EC. On 14 June 1985, for example, when the White Paper was presented to the heads of government and state before the Milan summit, Jacques Delors and other Commissioners, at the same time, held talks with a delegation from the Roundtable led by the then Chairman and CEO of AB Volvo, Perh Gyllenhammar.¹⁴⁵ Both sides shared the same feeling of an urgent need to develop technological cooperation in Europe.

¹⁴¹.These four reports were completed by 1987 and their main concerns have been the focal points of national governments and the EC, such as the Anglo-French Channel Tunnel and a European high-speed train network. See the European Roundtable, "Achievements of the European Roundtable", mimeograph.

¹⁴².See *Ibid.*, p. 2. François-Xavier Ortoli at that time the Commissioner for Economic and Monetary Affairs.

¹⁴³.*Ibid.*, pp. 3-4.

¹⁴⁴.Richardson, "Europe's industrialists help shape the single market", p. 19.

¹⁴⁵.*Bulletin of European Communities*, 6/1985, p. 38.

Furthermore, the most important part of the Roundtable's lobbying has been to express its views through "the individual members in their personal contacts with national governments and parliaments, business colleagues and industrial federations, and in private speaking engagements."¹⁴⁶ The progress in reaching the SEA and thereafter in implementing the 1992 programme has shown the business' pragmatism.

The Roundtable has "contributed significantly to the creation of a better dialogue and understanding between industry and politicians and notably the European Institutions."¹⁴⁷ The EC Commission in 1986, after the SEA was approved, asked Wisse Dekker, the then vice-chairman of the Roundtable, to form a supporting internal market committee of its members to press for "completing the internal market". Moreover, Dekker's committee went to Brussels to deliver the Roundtable's recommendations, before the July Eurosummit in 1986.¹⁴⁸ Another active group, the UNICE, composed of members of over 30 employers' and industrial associations throughout Western Europe, sought to create an outcome favourable to business. Its Secretary-General, Zygmunt Tyszkiewicz, has stated that "nine-tenths of our work comprises the regular, invisible interchange of ideas between our experts and the EC Commission's civil servants," and "UNICE also is used by the Community institutions to speak out to industry and to lobby our members."¹⁴⁹

Wisse Dekker, praised as one of the outstanding co-founders of the Roundtable, deserves "a footnote to history as

¹⁴⁶ Richardson, "Europe's industrialists help shape the single market", p. 19.

¹⁴⁷ See the European Roundtable, "Achievements of the European Roundtable", mimeograph.

¹⁴⁸ For the "investigation" committee for "completing the internal market" see the brief discussion in Roy Eales, "Europe's business knights regroup", *Multinational Business*, 3, (Autumn, 1987), p. 36; for the regular meetings between the Roundtable and the Commission see Richardson, "Europe's industrialists help shape the single market", pp. 18-19.

¹⁴⁹ Axel Krause, "Many groups lobby on implementation of market plan", p. 24.

the visionary behind the 1992 programme."¹⁵⁰ In his well-known presentation in Brussels at the beginning of 1985, Dekker evaluated Article II of the Treaty of Rome upon which the EEC's aims were set as: the establishment of a common market and a more convergent economic policy of the member states. As he described the problems Europe faced, which were largely attributed to Europeans' failures of finishing the "homework" given in Rome in 1957, Dekker launched a five-year plan (1985-1990) in the relevant Philips staff departments, which was intended "as a pragmatic aid to bringing that common European market in 1990 closer to realisation."¹⁵¹ His "Europe 1990" plan emphasized two pragmatic approaches, concrete steps and a detailed timetable, to help completing the "homework" on trade facilitation, fiscal matters, Value-Added Tax (VAT), standardisation, and government procurement.¹⁵²

Many have credited Dekker's initiative of "Europe 1990" with the successful agreement of the 1992 programme in the SEA.¹⁵³ It was this paper that drew the President of the Commission Jacques Delors' attention to undertake the study for completing the internal market for European economic integration, and virtually filled in the conceptual blueprint of Lord Cockfield's "White Paper". Ten months after his first paper was delivered, Dekker gave another speech in Bonn trying to assess the progress by then since the "Europe 1990" was launched in January, and to draw up the agenda in detail. After consulting with seven related "target groups" (governments, the European Parliament, the media, the European

¹⁵⁰ Michael Johnson, "Dutch cool profile: Wisse Dekker", *International Management*, (September 1989), p. 50.

¹⁵¹ "Europe 1990" by W. Dekker, p. 3.

¹⁵² Ibid., p. 4.

¹⁵³ Johnson, "Dutch cool profile: Wisse Dekker", p. 50; Richardson, "Europe's industrialists help shape the single market", p. 19; and Gardner, *Effective Lobbying in the European Community*, p. 47.

movement, the experts, the EEC Commission, and the Council of Ministers), he confirmed that the plan "Europe 1990" had been widely welcomed.¹⁵⁴ The plan was largely supported by national governments of member states, and by the European Parliament, particularly the "Kangaroo group" which had developed initiatives for supporting the "Europe 1990" plan and making it widely known.¹⁵⁵ In his own words, Dekker realizes that the White Paper had an important feature in common with "Europe 1990": "it contains a schedule and fixes dates for all the steps towards a real common market."¹⁵⁶

Despite the fact that Dekker's papers may stem from the practical plan of Philips itself, his vision has been undoubtedly projecting far beyond current European scale economies to the future of European integration. One may argue that the progress of the completion of the internal market had long been developed incrementally during the first half of the 1980s. However, with respect to the White Paper and the SEA, throughout the ERT's efforts to initiate the plan it is clear that industry's role was far more prominent as a trigger rather than an implementer. As many leading industrialists found, "there was a positive attitude towards industry playing an active role in the creation of a united Europe."¹⁵⁷ One concise analysis suggests that "the ERT is both the spiritual progenitor of the 1992 process and the single most powerful business group in Europe. It's not surprising, then, that when ERT talks, Eurocrats listen."¹⁵⁸ If there is one combined factor on which all general economic, political and

¹⁵⁴ "Europe 1990 - An Agenda For Action: progress and follow-up", Speech delivered by Dr. W. Dekker, to the "Deutsche Gesellschaft für Auswärtige Politik E. V." on October 9th, 1985, in Bonn, pp. 1-3.

¹⁵⁵ *Ibid.*, p. 2.

¹⁵⁶ *Ibid.*, pp. 2-3.

¹⁵⁷ *Ibid.*

¹⁵⁸ Gardner, *Effective Lobbying in the European Community*, p. 48.

institutional factors of the 1992 programme and thus of European economic integration have depended, it has been industrial development and the pressure exerted by multinational resources.

3.4. CONCLUSION

During the 1970s' recession, the EC witnessed the relative decline of its industry and overall economic performance, because its industrial structure had become outdated. Eurosclerosis was derived from the disadvantages of the "uncommon market". To strengthen industrial competitiveness and thus to cope with external industrial challenges, member states of the EC in the 1980s focused on the process of industrial restructuring. That process propelled the impetus of European industrial collaboration and relaunched European integration. Since 1980, increasingly fierce international competition has renewed the momentum for pressing ahead with the completion of the internal market from which the relaunch of European integration has resulted. Industrialists have taken an unprecedentedly high profile in lobbying for the single European market. At that moment, the EC's competence to cope with external economic pressures hinged upon the completion of the internal market and progressive European economic and political integration.

The process of campaigning for the relaunch of European integration in the mid-1980s showed how external economic challenges have periodically forced forward the progress of integration beyond that contemplated by the immediate political agenda. From the relaunch of European integration, a

new analytical framework of regional economic integration has emerged - the "external incentives-industrial development" approach. Despite its functionalist roots, this approach bases the process of regional integration upon the interdependent world of industrial competitiveness, and emphasises exogenous industrial development as a positive factor to the process of regional integration. This analytical framework of regional economic integration includes some variables: external economic challenges; exogenous industrial development by regional and multinational industries, in particular by the private sector; the need for the development of scale economies; and industrial cooperation of technology developing. Since 1980, these variables have been amongst the most prominent generators of European integration. Political factors have been diluted by these factors, although this does not deny their critical importance to the development of regional integration. The remainder of this thesis makes use of this framework to analyse the incentives and the implications of the emergence of the Chinese Economic Area in the context of growing Asia-Pacific subregional economic groupings.

CHAPTER FOUR

ECONOMIC DEVELOPMENT AND THE PATTERN OF REGIONAL ECONOMIC INTEGRATION IN THE ASIA-PACIFIC REGION

Where regional economic integration is concerned, related economies putting forward cooperation programmes have always taken into account any economic advantages which might accrue to them. Although political incentives have been crucial in advancing the progress towards regional integration, profits have remained the most fundamental motive for economic integration for the private sector. This is what the theoretical approach to economic integration has suggested about the mutual benefits of the "trade creation" effect. In particular, an integrated market allows economic factors, i.e. capital, goods, services, and personnel, to be able to move freely across national boundaries thereby making the best use of resources. Without the presence of mutual economic advantage, therefore, there is little hope for individual national economies to boost their prospects for regional integration and to maintain their commitment to existing regional groupings.

The purpose of this chapter is to explore economic development in the context of incremental Asia-Pacific economic cooperation, in general, and the impact of industrial restructuring in the Asian Newly Industrialised Countries (hereafter ANICs) on the development of subregional economic groupings right along the West Pacific Rim, in particular. It does not seek to review the ANICs' own developmental process, nor is it an economic assessment of the ANICs performances individually. It is, instead, an analysis of their attempts to

resolve structural problems by developing economic interdependence with their neighbouring economies, which in turn has inched forward regional economic integration. Furthermore, through an examination of the division of labour in the regional economies, the prospects for economic integration can be evaluated. The analysis focuses on the extent to which their efforts have brought about the regionalisation of industrial development which in turn has accelerated the progress of economic integration in Asia-Pacific, while regional economies are pursuing a strategy of globalisation.

Since the late 1980s, a number of international trends have been shaping the context of Pacific regionalism.¹ Firstly, the collapse of communism in the Soviet Union and Eastern Europe has, more or less, defused the Cold War in the Pacific area, and reminded China, one of the lone communist "fortresses" in East Asia which has been implementing a more pragmatic policy towards the market economy, to keep up with the prosperous Asia-Pacific economy. Secondly, the relative decline of the United States has been reflected in its suffering a huge trade deficit with the East Asian export-led economies. An increasingly protectionist orientation has emerged in North America, as a result. Therefore, East Asian export-led economies will have to increase the volume of intra-Asian trade to replace their traditional export market to the United States, so that their economic growth will not be slowed. Thirdly, the effect of North America and the European Community becoming more protectionist has boosted the importance of Japan for the East Asian export-led economies.

¹. Richard Drobnick, "Economic integration in the Pacific region", Technical Papers, No. 65, OECD Development Centre, Under the direction of Charles Oman. Produced as part of the research programme on Globalisation and Regionalisation, (May 1992), p. 15.

Japan has become an investor, banker, trader, and technology supplier for all East Asian export-led economies, but has also provided a large market for their exports. This Asia-Pacific economic cooperation may be leading to a new phase of economic integration. Furthermore, China has re-affirmed its reform and open door policy to the world, which implies that it like Japan will continue to promote Asia-Pacific economic cooperation.

In addition, there are two sources of uncertainty which could decisively affect Pacific regionalism. Firstly, the global trading regime is very likely to be fragile, "as regional integration proceeds, as intra-firm trade continues to grow, and as trade among strategic alliance partners increases."² To avoid an immediate breakdown which would have caused a global trade war, the Uruguay Round global trade talks of the GATT finally reached an accord by the deadline of 15 December, 1993, imposed on the Clinton administration by the US Congress. Although the prolonged Uruguay Round negotiations have ended with a compromise, it does not mean that it has brought about immediate assurance for economies and regional blocs around the world over trade problems. Many believe that "the end of the Uruguay Round will not be the end of trade talks - or trade battles".³ The future for freer trade could be more troubled.⁴

Secondly, the trade friction between Japan and the United States could jeopardise the world trade regime under the GATT, and also block trans-Pacific regional cooperation. On the one hand, Japan has continued to benefit from a huge trade surplus with the United States, but, on the other hand, Japan has kept

². Ibid.

³. The Americans and Europeans both conceive that more negotiations will continue. Jay Branegan, "And that's a wrap", *Time*, (27 December, 1993), p. 30.

⁴. *The Economist*, (18 December, 1993), pp. 13-14.

its domestic markets relatively closed to foreigners. Since the US Omnibus Trade Act of 1988 was introduced, US administrations have made use of "super 301" legislation as a foreign policy instrument pressing Japan and others for bilateral trade negotiations.⁵ Trade surpluses, protected domestic markets, and the US threat of imposing "super 301", characterise the current picture of the US-Japan's trade row. Most recently, on 11 February, 1994, in the White House meeting between the US President Clinton and the then Japanese Prime Minister Morihiro Hosokawa, a showdown over US access to Japanese markets brought about renewed tension. Subsequently, the US has threatened to cite Japan in a "Super 301" action.⁶ The US believes that because Japan is different from other industrialised countries, increased bilateral pressure is the only way to bring about change.

Japan's ongoing political reforms may yet provide scope for the government of a new generation to act more decisively in dealings with the US. For the present, in its state of political disarray, the Japanese coalition government is inclined "to take a rigid line against US pressure for numerically measured decreases in Japan's record trade surplus and increases in the market share of imported goods."⁷ Predictably, Japan, as suggested by many politicians and bureaucrats in Tokyo, is likely to adopt a tougher stand

⁵. For details see United States Senate, "Super 301: Effectiveness in Opening Foreign Markets", hearing before the subcommittee on international trade of the Committee of Finance, 101th Congress, second session, April 27, 1990.

⁶. "Super 301", the centre of the Omnibus Trade Act of 1988, provides "a mechanism through which U. S. trade negotiators can threaten the eventual imposition of special surcharges on a country's imports if that country does not agree to modify its 'unfair' trade practices (as unilaterally defined by the US), but gives the President great flexibility in determining whether or how far to apply the sanctions." See Robert Z. Lawrence, and Charles L. Schultze, "Evaluating the options", in their co-edited, *An American Trade Strategy Options for the 1990s*, (Washington D. C.: The Brookings Institution, 1990), p. 5.

⁷. See Jurek Martin, and William Dawkins, "Sparring partners in a new game", *Financial Times*, (11 February, 1994), p. 17.

against foreign pressure.⁸ Many observers have feared that it might trigger a trade war.⁹ This uncertainty will undoubtedly undermine not only any plans for Asia-Pacific regional economic integration but also the critical American relationships for the Asian-Pacific exporting economies on which their economic development is highly dependent. The desire for bridging Asian export-led economies and North American economies through a larger political framework that would provide them a framework for regular talks to reduce trade friction, has, in part, contributed to the emergence of the Asia-Pacific Economic Cooperation (APEC).

Economic development in the Asia-Pacific region has been very successful in promoting regional economic prosperity, firstly in Japan in the 1970s, later in the ANICs in the 1980s, and then in another group of fast 'catching up' industrialising economies (the 2nd tier of the ANICs), i.e. Malaysia, Thailand, Indonesia, the Philippines, and China, in the late 1980s and 1990s. Regional economies apart from Japan, have been sharing very similar patterns of economic development, i.e. considerable levels of dependence upon American and Japanese technologies and industrial techniques, and American markets. Since the mid-1980s, the ANICs have been commonly suffering from the "NICs disease" - namely rapidly appreciating currencies, soaring property prices, and shortages of labour, thereby losing their comparative advantages in labour-intensive industries. As a consequence,

⁸. For example, Shintaro Ishihara, a maverick Liberal Democratic Party member, said that "Now it is time for us to say no sometimes and then make counter-proposals." Ibid.

⁹. For the most recent trade row between the US and Japan see reports "Tough Talk", *Business Week*, (28 February, 1994), pp. 14-16; for Japanese response to the showdown see "The Japanese are hardly heading for the bunkers", pp. 17-19; and the reasons Japanese took a tough stand towards the US see "Saying no", *The Economist*, (19 February, 1994), pp. 74, 77.

industrialists have been seeking to relocate their industries in Southeast Asia and China.¹⁰

Regional economic development has increased the momentum of economic integration in the region. The economic framework of an international division of labour in production, resulting from the ANICs-based foreign investment flows, their upgrading of technology, and industrial cooperation in the region has raised the possibility of further and future economic integration. However, economic integration will be meaningful only if regional economies have been actively participating in an international division of labour.¹¹ It is quite clear that the ANICs' industrial restructuring has contributed to exports of capital, technology, and industrial experience to other East Asian developing economies. The result of these exports has been to allow other regional economies to share the benefits of successful industrial performance. Furthermore, cross border investment and inter-industry cooperation have not only created comprehensive economic ties between regional economies, but have also generated certain common business interests, e.g. their commitment to keep the world trade system free and open. The growing trend of economic tie-ups occurring amongst a group of neighbouring economies involved in smaller areas right along the West Pacific Rim, is parallel to the general development of Asia-Pacific economic cooperation. The clearest example can be seen in the case of the emergence of "subregional economic groupings" in the Asia-Pacific area,¹² such as the Growth Triangle, between Singapore, Malaysia, and Indonesia; and the Southern China Economic Area between Taiwan, Hong Kong, and

¹⁰. This relocation of such industries has been part of their strategy of restructuring industries to regain competitiveness. See W. B. Kim, "Industrial restructuring and regional adjustment in Asian NIEs", *Environment and Planning A*, 25, (1993).

¹¹. M. Panic, *National Management of the international Economy*, (London: Macmillan, 1988), p. 5.

¹². There have been various terms used, such as "economic circle", "economic zone", and "triangle", but "subregional grouping" is used here as a general term to be distinguished from Asia-Pacific "regional economic cooperation".

the Fujien and Guangdong provinces in China. Nevertheless, East Asian subregional groupings today have made their own way towards economic integration by relying upon industrial cooperation in which governments' full endorsement has followed rather than led, especially in the case of the emergence of the Chinese Economic Area, the Bohai Sea Economic Circle, and the Yellow Sea Economic Circle.¹³ On account of the ANICs economic development, the impact of the ANICs' policy for industrial restructuring has been to change both the pace of structural adjustment, and the political circumstances in the rest of the Asia-Pacific area as a whole, resulting in the rise of economic subregional groupings.

4.1. THE EMERGENCE OF SUBREGIONAL GROUPINGS IN THE CONTEXT OF ASIA-PACIFIC ECONOMIC COOPERATION

Since the early 1960s, in response to the progress of European integration programmes Asia-Pacific economic cooperation has been advanced by several attempts to form regional economic integration.¹⁴ None of these programmes has yet developed a consensus amongst all economies in the region in terms of European patterns' regional integration. Some have argued that in general the Asia-Pacific area lacks the favourable conditions for regional integration present in Europe.¹⁵ "East Asia and the Pacific are a relatively unpromising environment for regionalism", because the wide

¹³. In his contribution to China's economic cooperation network in Asian-Pacific region, Jin identified three basic economic circles based on China's coastal area. Instead of the CEA, he described the area covering Taiwan, Hong Kong, Fujien, and Guangdong provinces, as the Taiwan Straits Economic Circle. Huongfan Jin, "China's open door policy and Asian-Pacific economic cooperation", *The Korean Journal of International Studies*, 22, (1990), pp. 125-147.

¹⁴. The programmes in the Asia-Pacific region were brought about partly by a desire to rival the EEC. See Per Magnus Wijkman, and Eva Sundkvist Lindström, "Pacific Basin integration: A step towards freer trade", in John Nieuwenhuysen, *Towards Freer Trade Between Nations*, (Melbourne: Oxford University Press Australia, 1989), p. 145.

¹⁵. *Ibid.*, pp. 148-152.

differences in levels of industrial development, in particular, have also made a desire to form "a common and equitable mandate" less likely.¹⁶ Furthermore, Asia-Pacific economic cooperation in terms of political implication has been a relatively recent trend, compared with Europe's longer period of efforts at political cooperation since the second World War. While in Europe strong political pressure promoted the emergence of economic integration, the Asia-Pacific area appears to have little similar political pressure. There are many competing interests derived from different cultural, political and economic preferences amongst the region's countries.

For decades, general efforts for pan-Pacific economic cooperation have been carried out in various forms by academics, businessmen, and government officials, e.g. the Pacific Trade and Development Conference, the Pacific Basin Economic Council and the Pacific Economic Cooperation Conference. Since the mid-1980s, economic development in the Asia-Pacific area has been going through a transitional phase following the ANICs' industrial restructuring process. Although there have been different situations in each of the ANICs depending on their own political and economic environment, some general factors have contributed to this change: the appreciation of the Japanese Yen and the currencies of the ANICs against the US dollar; the democratisation, rising wage rates, and stricter environmental protection regulations in force; the 1989 elimination of the Generalised System of Preference (GSP) status of the ANICs by the United States; and China's open market.¹⁷ Due to demands

¹⁶. Staffan B. Linder, *The Pacific Century: Economic and Political Consequences of Asian-Pacific Dynamism*, (Stanford, California: Stanford University Press, 1986), p. 114.

¹⁷. Drobnick, "Economic Integration in the Pacific Region", 1992, p. 22.

for self-adjustment of industrial structures in order to regain competitiveness, the ANICs have allowed some of their low-level skilled industries to relocate in Southeast Asian countries and China. At the same time, they have pressed ahead with the upgrading of their domestic technology. This restructuring process in the ANICs has not only reinforced the existing regional trade structure, but also built up much more comprehensive economic ties, based on this industrial division of labour, with Japan and developing countries in the region. A new economic East Asian map has appeared based around subregional groupings. According to geographic characters, subregional groupings generally can be divided into three groups: the Japan Sea Zone, including the Yellow Sea Zone, and the Tumen Delta; the Southern China Zone; and the ASEAN Free Trade Area plan, including the Growth Triangle, the Northern Triangle, and the Baht Economic Zone.¹⁸

There are four "mini strategic triangles: the "manufacturing triangle" of Japan, Thailand, and Indonesia; the "Chinese triangle" of China, Taiwan, and Hong Kong; the "growth triangle" of Singapore, Malaysia and Indonesia; and the "trade triangle" of South Korea, North Korea, and China's Shantong Peninsula.¹⁹ An American official has pointed to a "growth cluster" phenomenon in East Asia with intra-regional economic ties forming without regard to national borders. The phenomenon has occurred in a number of subregions: in Hong Kong, Taiwan, and Southern China, in Sino-Russian border trade, in the Korean private sector's ties with China's Jilin, Liaoning, and Shandong provinces, in the interest in a Tumen

¹⁸. Although recently there have been different arguments about subregional groupings in East Asia, the category here is based on a Japanese work. T Aoki, and H. Ohashi, "Asia: integration of the world's most dynamic economies", *Tokyo Business Today*, (June 1992), pp. 26-29.

¹⁹. Kanmao Wang, "The Pacific and the Global economy", *The Pacific Review*, 5: 2, (1992), p. 138.

River development project, and in a "Growth Triangle" involving Singapore, Malaysia, and Indonesia.²⁰ The rush to triangulate in the Asia-Pacific area has been largely driven by "the world economic recession and the perceived threat of protectionism from emerging trade blocs in Europe and North America."²¹

Although the ANICs have not been the only contributors to the impetus bringing forward regional economic cooperation in general, they do offer the possibility of subregional economic groupings which contribute to a larger framework of pan-Pacific cooperation. Without fully involving the tedious formality of governmental scrutiny, the ascendance of subregional groupings, driven by the private sector, to some extent, results from the anxiety of regional economies concerning the prospects for a world trade regime and at the same time for successful regional economic integration. It may be more accurate to state that the emergence of subregional groupings is partly a pragmatic response of regional economies to regional autarky, and partly a natural result of East Asian traditional business links through personal contact rather than bureaucratic practices.²²

4.1.1. Economic Development and Asia-Pacific Economic Cooperation

Asia-Pacific Economic Cooperation: the General Context of Economic Integration

Stuart Harris once said that "the interest in regional economic cooperation in Asia-Pacific region has not always

²⁰. "The Asia-Pacific area needs a stronger sense of community" address by William Clark, Jr. to the Mid-America Committee, Chicago, 4 December, 1992, *ASEAN Economic Bulletin*, 10: 3, (March 1993), p. 382.

²¹. Sandra Burton, "Growing by leaps-and triangles", *Time*, (17 January, 1994), p. 24.

²². *Ibid.*

been motivated by a logical understanding of the need. It was often a response to what appeared to be happening elsewhere."²³ Indeed, for decades, the dynamics of the economic cooperation movement in this region have partly resulted from some sort of "defensive stand" against the emergence of regional integration in Europe and North America.²⁴ Because of the different rates of economic development in East Asia, most initiatives for economic cooperation have lacked a common interest shared by all regional economies.

The first ever institution-establishing initiative for economic cooperation, the Pacific Free Trade Area, brought about by the Japanese Professor Kiyoshi Kojima in the early 1960s, was regarded as a response of the five Pacific developed economies - Japan, Australia, New Zealand, the United States, and Canada, to the immediate effect of the European achievement of regional integration.²⁵ Kojima, in the early 1970s, observed that: "The enlarged Eurobloc will continue and strengthen its inward-looking policies, intensifying intra-regional development and raising the degree of its self-sufficiency which are the purposes of the integration" and "These Pacific basin countries should join efforts in obtaining a bargaining power equal to the Community so that they could deal with it from a better position."²⁶ While in the second half of 1980s the relaunching of European

²³. Stuart Harris, "Varieties of Pacific economic cooperation", *The Pacific Review*, 4: 4, (1991), p. 308.

²⁴. Many have shared this reactive attitude. Toichi Funabashi, "The Asianization of Asia", *Foreign Affairs*, 72: 5, (November/December 1993), p. 79; Frank B. Gibney, "Creating a Pacific Community: A time to bolster economic institutions", *Foreign Affairs*, 72: 5, (November/December 1993), p. 20; and Linda Low, "East Asian Economic Grouping", *The Pacific Review*, 4: 4, (1991), p. 375.

²⁵. Drysdale quotes others who have said that the proposal for a Pacific free trade area is primarily a reaction to the establishment of the EEC. Peter Drysdale, *International Economic Pluralism: Economic Policy in East Asia and the Pacific*, (New York: Columbia University Press, 1988), p. 207.

²⁶. Kiyoshi Kojima, "A Pacific Free Trade Area proposed", *Pacific Community*, 3: 4, (July 1972), pp. 586, 587.

integration put forward a target for the completion of the European Single Market in 1992, and the US-Mexico-Canada North American Free Trade negotiation started off, the effect of the promotion of such regional economic integration has stepped up the APEC concept.²⁷ It was these external factors that spurred on regional economic cooperation to a "G7 summit like an influential intergovernmental mechanism".²⁸

Since 1960, a series of initiatives have brought forward economic cooperation in the Asia-Pacific area and have continued shaping up the progress of economic integration²⁹ (see Table 4.1). For decades, the Japanese and Australians, the greatest enthusiasts in pan-Pacific cooperation programmes, have advocated the development of Asia-Pacific economic cooperation through the promotion of regional trade and economic development, which, in turn, contributed to various proposals either of ideas or of establishing institutions. However, there has as yet to emerge a grand blueprint similar to EC-like economic integration in the region, not only because the existing differences between regional social, political and economic systems have prevented them from producing a regional identity, but also because the East Asian export-led economies *per se* have not relied so much on regional markets. In the past few decades, although many proposals, such as the PAFTA and OPTAD, were sponsored by some

²⁷. The background to the emergence of the APEC was trade tension between East Asian economies and Western countries. For the details see Andrew Elek, "Asia-Pacific Economic Cooperation (APEC)", *South East Asia Affairs*, (1991), pp. 33-48.

²⁸. Helen Hughes, "Does APEC make sense?", *ASEAN Economic Bulletin*, 8: 2, (November 1991), p. 125.

²⁹. For details of the development of Asia-Pacific economic cooperation in the past few decades see Peter Drysdale, *International Economic Pluralism: Economic Policy in East Asia and the Pacific*, pp. 207-222; Norman D. Palmer, *The New Regionalism in Asia and the Pacific*, (Lexington, Massachusetts: Lexington Books, 1991), Chapter 8., pp. 133-155; Lawrence T. Woods, "Non-governmental organisations and Pacific cooperation: back to the future?", *The Pacific Review*, 4: 4, (1991), pp. 312-321; and for a review of Pacific economic cooperation see Hadi Soesatro, "Institutional aspects of Pacific Economic Cooperation".

governments, e.g. the Japanese and Australian, and were planned for converging the related governments' policy, no firm commitment from any government has yet appeared for the matter of regional cooperation.³⁰ With limited governmental commitment, the efforts for economic integration in the Asia-Pacific region have focused principally on the construction of transnational networks on a non-governmental basis.

TABLE 4.1. INITIATIVES FOR PACIFIC ECONOMIC COOPERATION: A HISTORIC BRIEF OUTLINE

1960	a Pan-Pacific organization ^a (M. Kajima)
1963	in a report for the JERC ^b calling for annual meetings of five developed Pacific nations (S. Okita)
1965	Pacific Free Trade Area (K. Kojima)
1967	Pacific Basin Economic Council (Japanese and Australian Business groups)
1967	Association of Southeast Asian Nations (A. Malik & T. Khoman)
1968	Asian Pacific Bloc Establishment Plan (T. Miki)
1968	Pacific Trade and Development Conference (K. Kojima & T. Miki)
1969	A System of Collective Security in Asia & the Pacific Community (L. Brezhnev)
1977	Fukuda Doctrine (Fukuda)
1977	Organization of Pacific Trade and Development (P. Drysdale & H. Patrick)
1978	Pacific Basin Cooperation Study Group (M. Ohira)
1980	Pacific Economists Community (K. Kojima) Pacific Basin Cooperation Concept (PBC Study Group) Pacific Economic Cooperation Conference
1981	ASEAN-Pacific Forum (K. Kojima)
1989	Asia-Pacific Economic Cooperation (R. Hawke)
1990	East Asian Economic Caucus (D. Mahathir)
1992	ASEAN Free Trade Area

Note: ^a. It became "Union of Asian Countries" in 1973.

^b. Japan Economic Research Centre

Sources: Based mainly on Hadi Soesastro, "Institutional aspects of Pacific Economic Cooperation", in Hadi Soesastro, and Sung-Joo Han, (eds.), *Pacific Economic Cooperation: the New Phase*, (Jakarta: Centre for Strategic and International Studies, 1983), pp. 1-52.

³⁰. Hiroshi Kitamura, "Asian-Pacific economic cooperation: the role of governments", in Hadi Soesastro, and Sung-joo Han, (eds.), *Pacific Economic Cooperation: the Next Phase*, pp. 159-160.

Although those institutions, characterised by nongovernmental colour, have yet to claim complete success for their efforts to lead regional economic integration, they have generated a prevalent interest in the goal of Pacific cooperation. From the onset of the Asia-Pacific economic cooperation movement in the early 1960s, this has largely stemmed from a tripartite network of academics, businessmen, and governmental officials, which has meant that economic cooperation has been based more on bargaining between different individual interests than on the definition of common interest. Nevertheless, these efforts for Asia-Pacific economic cooperation have never been so important as to water down those official regional organisations which have been continuously devoted to regional economic integration for decades. The Economic and Social Commission for Asia and the Pacific (ESCAP) under a regional commission of the United Nations and the Asian Development Bank (ADB) are both comprehensive and influential regional official organisations.³¹ In spite of being an all-regional comprehensive organisation bridging regional and international interests and institutions, the ESCAP has not been counted for the main stream of Asia-Pacific regional economic integration.³² Although the ADB has a substantial capacity to develop more extensive projects of regional trade and economic issues, it has actually only on occasion served beyond its original function of development financing.³³ Therefore, both

³¹. The ESCAP was renamed in 1974. Its original organisation was the Economic Commission for Asia and the Far East (ECAFE) established in 1947 by the Economic and Social Council of the United Nations. The ADB was established in 1965 under the auspices of ECAFE.

³². The ESCAP, derived from its predecessor, the Economic Commission for Asia and Far East, was a contact point in the establishment of the ADB. It was not designed for serving as the sort of regional association promoting economic and political integration. Drysdale points out that its weakness lies in its comprehensiveness and remoteness from policy influence in its diverse membership. See his *International Economic Pluralism*, p. 210.

³³. See Drysdale, *International Economic Pluralism*, pp. 210-211.

the ESCAP and ADB have not been included in discussions about evolving regional economic cooperation.

In 1965, the Pacific Trade and Development Conference (PAFTAD), derived from Kojima's proposal for a Pacific Free Trade Area, came into effect.³⁴ The PAFTAD, an academic and policy oriented institution, has long been recognised as the intellectual driving force of economic cooperation. Its major contributions to Asia-Pacific economic cooperation and diplomacy have taken three forms. Firstly, the PAFTAD provides a forum to embrace economists from all parts of the region, including those from Southeast Asia, China, the former Soviet Union, and Pacific Latin American economies, in policy research and debate. Secondly, its research programmes have been widened from the earliest trading arrangements to technology, and industrial policy. Thirdly, its extensive network is widely spread over the region through academics tying up with governmental officials and businessmen.³⁵

The business-oriented Pacific Basin Economic Council (PBEC) was launched in 1967-68 by business leaders from Japan, Australia, New Zealand, Canada, and the United States. According to R. Sean Randolph, the international Director General of the PBEC, "the underlying philosophy of PBEC embraces active support for multinational economic cooperation in the Pacific region and the building of bridges between different economic communities."³⁶ The PBEC now operates as a network of about 1000 firms and senior corporate executives who seek a favourable public policy climate for business.

³⁴. Kojima believed in 1977 that Pacific economic cooperation should be taking practical steps based more on functional rather than institutional integration. The idea of favourable benefits of a free trade area was brought about. See Kojima, *Japan and A New World Economic Order*, (Tokyo: Charles E. Tuttle Company, 1977), p. 173.

³⁵. The PAFTAD's contributions in this part refer to Lawrence T. Woods, "Non-governmental organisations and Pacific cooperation: back to the future?", pp. 313-314.

³⁶. On Randolph's letter sent to Professor Palmer, see Norman D. Palmer, *The New Regionalism in Asia and the Pacific*, p. 137.

Due to its early organisational preoccupation and limited representative qualities, the PBEC's ability to enhance the political function of representation beyond its original intention of encouraging communication within the regional business community, has been limited.³⁷ Nevertheless, through the PBEC annual meeting, delegates, in most cases leading national industrialists, expect each other to carry forward their own government policies in discussions. Because of this informal communication between regional industrialists, and between them and their governmental officials, the PBEC, to some extent, serves as "a vehicle for the exchange of information and a conduit for communication between states."³⁸ It is clear that the business communities everywhere are concerned with the development of more open markets. There have been some doubts inside the PBEC about regional economic cooperation as a whole. As economic development is taking place against the background of diversification in the Asia-Pacific area, the PBEC has contributed to an increasing common business interest in the maintenance of an open and free global or at least regional economic system. Although the PBEC's capacity in leading regional economic cooperation is insufficient, its importance lies in its seeking the optimal business environment that will keep up with growing economic development and business-based subregional groupings in the region.

Amongst all the nongovernmental organisations for Asia-Pacific economic cooperation, the Pacific Economic Cooperation

³⁷. In the early period of the PBEC, it was suggested by Japanese and Australian businessmen that initial membership should be restricted to firms and individuals from the five developed countries, Japan, Australia, New Zealand, the USA, and Canada. Its inability to integrate the Chinese and Russian delegates has prevented it from representing the interests of the region as a whole. See Woods, "Non-governmental organisations and Pacific cooperation: back to the future?", p. 315.

³⁸. Ibid.

Conference (PECC), formally launched by participants attending a Pacific Community seminar held in Canberra in 1980, could well be the most significant. As the logical extension of the PAFTAD and PBEC, the PECC's national delegations have been organised on the basis of tripartite interests: academics, business leaders, and state officials. In addition, the PAFTA, and PBEC are institutional members of the PECC along with the ADB. Unlike the PAFTAD and PBEC, the PECC's network for cooperation has been, to a considerable extent, advancing towards taking political implications into account. This is facilitating negotiations between national states and between different societal sectors. This function has won the PECC credit to enhance official relationships between its members in the discussion of common problems and policies through "unofficial" forums.³⁹ The PECC's successful managing of a Pacific perspective in the Uruguay Round of multinational trade negotiations has shown its capacity to a transnational forum of expressing a common regional interest.⁴⁰ More regional governmental commitment is the prerequisite for any further regional cooperation. Increasing governmental commitment to regional cooperation programmes may well have created the context for the emergence of the APEC as an influential institution.

The APEC concept initiated by the Prime Minister of Australia, Mr. R. J. Hawke, in 1989, was originally conceived as "an informal forum of officials from Asia-Pacific countries in response to the rise in economic regionalism - notably the

³⁹. In January 1980, the then Australian Prime Minister, Malcolm Fraser, and Japanese Prime Minister, M. Ohira, agreed to hold a non-governmental seminar to explore Pacific economic cooperation further, which brought about the "unofficial" PECC in the Canberra seminar later that year. See Kitamura, "Asian-Pacific economic cooperation: the role of governments", p. 160; and Hadi Soesastro, "Institutional aspects of Pacific Economic Cooperation", p. 24.

⁴⁰. Woods, "Non-governmental organisations and Pacific cooperation: back to the future?", p. 317.

EC and NAFTA."⁴¹ The APEC was at first intended to be an informal consultative forum. In 1991, the member states of the APEC in the 3rd annual ministerial meeting in Seoul sought to commit themselves to an "open regionalism" of free trade and economic collaboration. A "Seoul APEC Declaration" which recognised the need to establish a secretariat has attempted to transform a consultative to an institutional operation of the APEC.⁴² Moreover, since the United States took over the chairmanship from Thailand in September 1992, the Clinton administration has sought to transform the forum from "a 'talking shop' to an achievement-based group" especially at the Seattle APEC summit meeting in November 1993.⁴³ Unlike many other regional economic cooperation initiatives, the APEC "is not an organisation, and does not aim to have an organisational form."⁴⁴ Whether the APEC will gradually evolve into a mechanism for regional economic integration remains to be seen. Its main objective has, nevertheless, been to coordinate and congregate regional interests for improving the global multilateral trading framework. Furthermore, as described by an American official, the APEC provides an excellent vehicle for achieving regional trade liberalisation that will encourage more ambitious Asia-Pacific integration.⁴⁵

Unlike the economies in the European Community, Asia-Pacific regional economies have been characterised by a more outward-looking orientation which has been reflected in their exporting of manufactured products largely to developed markets. Although the intra-regional trade has steadily

⁴¹. Susumu Awanohara and Nayan Chanda, "Uncommon bonds", *Far Eastern Economic Review*, (18 November 1993), p. 16.

⁴². For details of the Declaration see "APEC announces Seoul Declaration", *Korea Newsreview*, (23 November, 1991), p. 4.

⁴³. Awanohara, and Chanda, "Uncommon bonds", p. 17.

⁴⁴. Hughes, "Does APEC make sense?", p. 125.

⁴⁵. See "The Asia-Pacific area needs a stronger sense of community" addressed by William Clark, Jr. to the Mid-America Committee, p. 383.

increased recently, the economies remain heavily dependent not upon the regional market itself, but upon the rest of the world markets.⁴⁶ Generally, their industries see themselves as global rather than "regional traders".⁴⁷ Since their outward-looking strategy has made them very vulnerable to exogenous factors, particularly developed countries' trade policies, protectionism, and exchange rate fluctuations, the economies in the Asia-Pacific region have sought to defend themselves against such external challenges by forming their own regional groupings. Regional economies' hopes for establishing a regional bloc to reduce exposure to international competition and protectionism have given APEC a leading role. The APEC's main role in the region should be to bring the regional economies together continuously, and, in the global economy, to act on their behalf as "a regional lobby for open global trade."⁴⁸ Their outward-looking perspective has been a major reason why Japan and the ANICs have yet to show "much sense of community, or much interest in regional cooperation" in spite of their increasing economic interdependence.⁴⁹ This may also explain why Asia-Pacific economic cooperation has been more successful thus far in non-governmental rather than in inter-governmental forms.

In general, Asia-Pacific economic cooperation was initially based on nongovernmental, or informal activities which led to the creation of three functioning institutions, the PAFTAD, PBEC, and PECC in the region. Only the APEC has emerged in 1989 as a pan-Pacific official consultative forum. Later, in 1990, the idea of the East Asian Economic Caucus

⁴⁶. In 1980, the exports of the West Pacific accounted for 37.3 per cent of its intra-regional trade. In 1989, it rose to 46.6 per cent. See C. H. Kwan, "The emerging pattern of trade and interdependence in the Pacific region", *Tokyo Club Papers*, 4: 2, (1991), pp. 139-141.

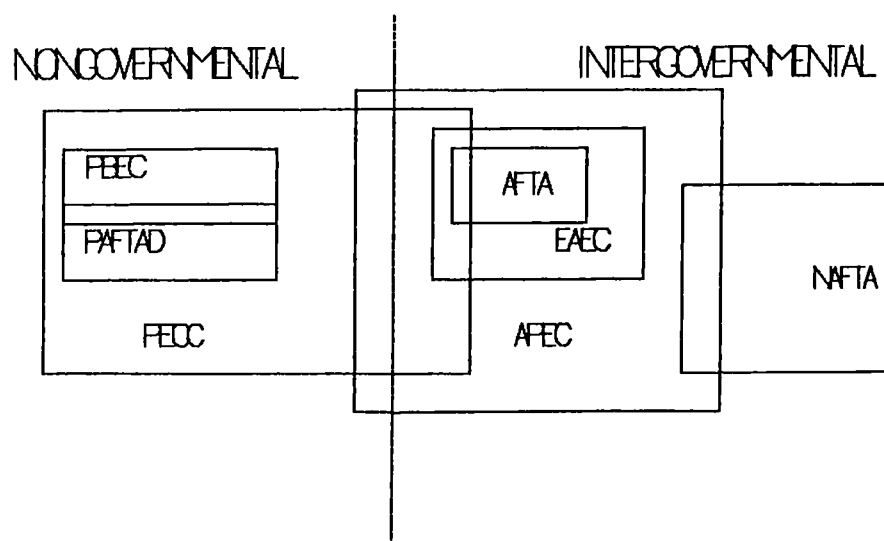
⁴⁷. Bryce Harland, "Whither East Asia?", *The Pacific Review*, 6: 1, (1993), p. 16.

⁴⁸. Hughes, "Does APEC make sense?", p. 125.

⁴⁹. Harland, "Whither East Asia?", p. 16.

(EAEC),⁵⁰ an exclusive Asian grouping, was developed on an inter-governmental basis, albeit it has yet to obtain the commitment of the Japanese, which is crucial for the EAEC's fate. It has been continuously renounced by the United States. In 1992, the ASEAN countries put forward their ambitious plan to form the ASEAN Free Trade Area (AFTA). It has become clear that through the APEC's mechanism, bridging the East Asian economies to the NAFTA would provide a milestone not only for Asia-Pacific economic cooperation but also for the world economy as a whole (See Figure 4.1). This new trend of regional economic cooperation

FIGURE 4.1. ASIA-PACIFIC ECONOMIC COOPERATION



based more on official level contact may promote the "movement" of Asia-Pacific economic cooperation towards regional economic integration. As long as the shape of the new

⁵⁰. The EAEC which was originally proposed by Malaysia as the East Asian Economic Group (EAEG) is expected to include Japan, China, South Korea, Taiwan, Hong Kong, and ASEAN. "Trade Blocs: Who's who", *Asiaweek*, (13 January, 1993), p. 43.

world trade order is at stake, and the EC and the NAFTA continue to become more inward orientated, it is very likely that the current trend towards a Pacific trade bloc will continue. Despite sharp criticism from the United States, the ASEAN has already adopted the concept of the EAEC as "an independent, subordinate institution to the APEC."⁵¹ To some extent, the EAEC and the APEC could be the double edges of an Asia-Pacific economies' sword thrusting into the rest of the world. On the one hand, by leading Asia-Pacific economic cooperation, the APEC could well be the regional multilateral mechanism for integrating individual interests in negotiations with other economies, so that the tensions between different regional trade blocs will be reduced. On the other hand, the EAEC appears to have resulted from a defensive reaction to protectionism elsewhere.

Economic Development: A Tool for Economic Integration

Against the background of general efforts for Asia-Pacific economic cooperation, growing economic development has brought about an economic interdependence which "has begun to forge a sense of cohesion across the Pacific."⁵² If the original momentum for pan-Pacific economic cooperation arose from a passive reaction to the threat (exogenous factor) of regional economic integration elsewhere, the dynamics of economic integration in the region appear now to be driven by rapid regional economic development and growing international competition. To some extent, exogenous factors have served as a trigger to push forward initiatives for economic cooperation in the Asia-Pacific region.

⁵¹. See M. G. G. Pillai, "Emerging Trade Alliances in Asia", *Economic and Political Weekly*, 27: 5, (1 February, 1992), p. 199.

⁵². "The Asia-Pacific area needs a stronger sense of community" addressed by William Clark, Jr. to the Mid-America Committee, p. 386.

In the 1960s and 1970s, East Asian economies except for Japan were not yet prominent internationally. Asia-Pacific economic cooperation, or regional "economic integration", was a topic only between developed economies in the region, namely Japan, Australia, New Zealand, the United States, and Canada. In the early 1970s the ANICs started the catching-up process of economic development, following Japan's example. Later, during the 1980s, ASEAN economies followed the ANICs' example. Such East Asian dependent and interdependent development between economies can be described in three tiers:

"Japan, the NIEs, and ASEAN constitute three tiers of countries at different levels of skill, wage rate, and development. The flow of investments from the upper to lower tier of countries acts as a transmission belt in transmitting growth momentum from one tier to the next."⁵³

As far as the progress of economic development is concerned, the relationships between East Asian economies have enormously increased especially in the last decade, albeit such increases were not necessarily based on political congruence, owing to e.g. ASEAN's suspicion of Japan's increasing influence over the region through its economic power, and political distrust between China and Taiwan. More and more practical indices suggest that the increasing economic interdependence amongst Asia-Pacific countries has been brought into being by intra-regional trade, investment, inter-industry cooperation, and division of labour. According to APEC's definition, intra-Asian-Pacific trade in terms of total trade shares has risen from 57 per cent in 1970 to 66 per cent in 1988.⁵⁴ The most impressive development amongst

⁵³. Low, "East Asia Economic Grouping", p. 378.

⁵⁴. This intra-regional trade figure including cross-Pacific trade is more conspicuous than the figure for the intra-West Pacific trade. Compare the discussion in Low, "East Asia

East Asian economies in the last decade has been rising intra-investment not only from already developed countries, such as Japan, the United States, and European countries, but also from the ANICs, which "is a phenomenon reflecting growing economic cooperation and integration in this region."⁵⁵ While the ANICs have been one of the major recipients of foreign direct investment in the region, they have also devoted very substantial resources to intra-regional investment. Such new patterns of investment reveal that the transformation of East Asian economic development is under way through "an extensive industrial restructuring and a sophisticated subregional division of labour."⁵⁶ The emergence of the division of labour across all East Asian economies has, to some extent, deflected them from any possible political rows caused by trade disputes over competition for export markets.

Asia-Pacific economic integration, if it occurs, will be based on the virtual economic interdependence derived from the regional economies' adoption of the same economic development model, rather than on a preoccupation with benefiting from scale economy. It will be the progress of economic development that activates the initiatives for regional economic integration. Although politically Asia-Pacific economic integration remains the target, at least in the current situation, it is economically more likely to be brought to effect on a subregional scale reflecting day-to-day economic transactions, rather than on a pan Asia-Pacific basis.

Economic Grouping", p. 379; and C. H. Kwan, "The emerging pattern of trade and interdependence in the Pacific region", pp. 139-141.

⁵⁵. The extensive foreign direct investment conducted by Japan and the ANICs respectively has been studied in Edward K. Y. Chen, "Foreign direct investment in East Asia", *Asian Development Review*, 11: 1, (1991), p. 32.

⁵⁶. *Ibid.*, p. 33.

4.1.2. The Rise of Subregional Groupings

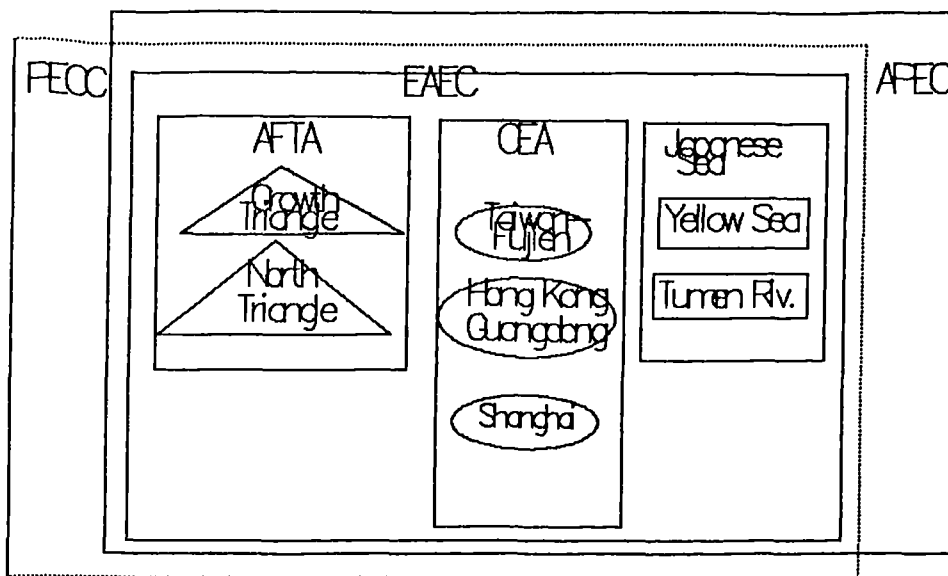
Since the mid-1980s, the world trade structure has been going through a dramatic change moving from a multilateral arena to the formation of regional trade blocs, as a result of the slow progress in the trade negotiations of the Uruguay Round. During the Uruguay Round, uncertainty over the future of world trade was aggravated by the staggering economic performance of Western industrialised countries and an increasing tendency of protectionism. In this context of uncertainty and growing competition pressures, a number of regional trade groupings have emerged throughout the world.⁵⁷ Developed economies, notably the EC and NAFTA, have been especially credited with gaining much of the success in forming regional trade groupings. By way of contrast, to seek a strengthened position to cope with possible future trade battles between regional groupings, individual developing countries are keen to avoid being left out of any potential trade grouping. The Asian-Pacific economies have already made a few efforts by private and public sectors to form trading blocs in order to safeguard their market competitiveness and strengthen negotiating leverage in case of the collapse of the GATT negotiations.

The concept of the Chinese Economic Area and the Growth Triangle searching for "natural allies" reflects in particular Hong Kong, Taiwan, and Singapore's aspirations to maintain their market competitiveness. The emergence of the EAEC and

⁵⁷. The EC, the EFTA, and the Visegrade Pact (Poland, Hungary, Czech Republic, and Slovakia) in Europe. See "Trade Blocs: Who's who", *Asiaweek*, (13 January, 1993), p. 43; the NAFTA, Andes Free Trade Zone, the Southern Cone Common Market (SCCM), and the Caribbean Community in America. See report in *Financial Times*, 7/8 December 1991; the EAEC, AFTA, the South Asian Preferential Trade Agreement (SAPTA), the Economic Co-operation Organisation (ECO) in Asia, see "Trade Blocs: Who's who", *Asiaweek*, (13 January, 1993), p. 43 and *The Times*, 24 February 1992, p. 10.

AFTA, on the other hand, implies more searching for a consensus in the region in terms of trade. The keen efforts to date have been the outcome of regional economies' industrial restructuring process and the development of regionalism in the EC and NAFTA.⁵⁸ Malaysia's Prime Minister, Mahathir Mohamad, the most known enthusiast in the region for forming an exclusively Asian regional grouping - the EAEC, has warned that economic blocs in Europe and North America are forcing East Asian countries to follow suit.⁵⁹ Graham Hayward, the executive director of the Singapore International Chamber of Commerce, has stressed that the formation of AFTA or a similar body, has become "a useful insurance policy" for regional economies.⁶⁰ (See Figure 4.2)

FIGURE 4.2 ASIA-PACIFIC SUBREGIONAL GROUPINGS



In general, regional trade blocs are intentionally pursuing common stands to cope with other trade counterparts

⁵⁸. "Year of the Blocs?", *Asiaweek*, (13 January, 1993), p. 42.

⁵⁹. "The stubborn holdout", *Time*, (22 November, 1993), p. 57.

⁶⁰. "Year of the Blocs?", *Asiaweek*, (13 January, 1993), p. 42.

by establishing the common regulations for their internal markets and a consensus in international negotiations. The interest of individual countries will supposedly be protected by projecting a common stand against external challenges. Such a decisive move is entirely dependent on governmental commitment and policy cooperation. However, the development of a subregional economic grouping in Asia-Pacific area does not comply with Western conventional knowledge of inward-looking trade blocs, partly because there has yet to exist a comprehensive economic grouping to generate a common interest, and partly because increasing economic ties between regional economies have not been based on political motivations, but rather on economic development. For example, the Growth Triangle is made up of Singapore's capital, financial facilities, and well developed industrial base, and Indonesia and Malaysia' abundance of land and labour force.⁶¹

During the period of the ANICs' industrial restructuring, a political motivation behind economic cooperation has been to consolidate security arrangements in the post Cold War era. Singapore through the development of the Growth Triangle which ties in Malaysia and Indonesia has gained advantages for its city state's security. Hong Kong has been especially keen to develop economic interdependence with China, which could be the only way for Hong Kong to remain economically active after 1997. In accelerating economic transactions across the Taiwan Strait, possibly resulting in the creation of the Chinese Economic Area, the political tension between Taiwan and China has largely abated. Although China remains a potential political threat to Taiwan, their all round relationship has improved at an unprecedented speed. This has clearly suggested

⁶¹. See Lee, Tsao Yuan *Growth Triangle: the Johor-Singapore-Riau Experience*, (Singapore: Institute of Southeast Asian Studies, 1991).

that the more their economic interests are combined together, the less likely China will be to use force.

Whilst in recent years South Korean producers of light industrial goods have also rushed to take advantage of China's cheap labour costs for their production, big firms in the heavy and chemical industries have also been targeting China's huge domestic market by setting up sales bases.⁶² Part of South Korean industrial restructuring strategies has been to move manufacturing sectors away from labour-intensive products, which has resulted in South Korean enterprises' persistent investment in North East China.⁶³ A common business interest has been brought about as a result. In terms of security in Northeast Asia, while North Korea remains a potential threat, China's pursuing peace and stability as its most important goal in the region is rather convincing to South Korea.⁶⁴ The increasing economic ties between South Korea and China may have blended economic interests with South Korean willingness to sooth the continual tension in the Korea Peninsula. Believing in Beijing's influence over the Pyongyang regime, in his trip to Beijing in March 1994, South Korean President Kim Young Sam was hoping to persuade his Chinese counterpart to step in the quarrel of North Korea's development of nuclear weapons.⁶⁵

62. See "A west-bound gold rush?", *Business Korea*, 10: 11, (May 1993), p. 18.

63. Shim Jae Hoon, "China market roars", *Far Eastern Economic Review*, (27 May, 1993), p. 44.

64. As China is currently undertaking great reform for its economic development, a peaceful and stable Korean Peninsula remains in China's best interest. For Chinese and North Korean relations see Brian Bridges, *Korea and the West*, (London: Routledge & Kegan Paul for Royal Institute of International Affairs, 1986), pp. 68-72.

65. "Interview: South Korea's Kim Young Sam - Making a plea for patience", *Time*, (28 March 1994), p. 28. While Li Peng, China's Premier, agreed to work with President Kim, he was granted a £2 billion investment promise from Samsung Electronics. *The Times*, (3 November, 1994), p. 11.

4.2. INDUSTRIAL RESTRUCTURING AND THE DEVELOPMENT OF SUBREGIONAL ECONOMIC GROUPINGS

In the last few decades fast economic growth and their export-led strategies have led the ANICs to focus on trade with other economies to propel their economic development. As neoclassical theory contends, the occurrence of exchanges is determined by the producers' expectation of advantages and disadvantages. The comparative advantage based on low cost production had led the ANICs to compete successfully with their trade counterparts in developed economies in certain sectors, such as textiles, automobiles, steel, shipbuilding, electronics and electrical equipment. For decades, commentators have consistently focused on the general similarities in ANIC development, such as cheap labour, the state's intervention in economic development and hard working workers, because it was these factors that won the ANICs' producers the comparative advantage over the products of their developed counterparts in the world markets.⁶⁶

However, the ANICs have, since the 1980s, suffered from a loss of comparative advantage because of the mounting pressure to their exports from low cost products from other developing countries, such as Indonesia, Malaysia, Thailand, the Philippines, and above all China.⁶⁷ These countries are equipped with abundant low cost production factors, notably

⁶⁶. For discussion in detail of the ANICs' successful story see: Frederic C. Deyo, (ed.), *The Political Economy of the New Asian Industrialism*, (Ithaca, New York: Cornell University Press, 1987); arguing that the better performance in ANICs is rather due to the effectiveness of state intervention, Jenkins suggests this lesson to some Latin American NICs - Rhys Jenkins, "The political economy of industrialisation: A comparison of Latin American and East Asian Newly Industrialising Countries", *Development and Change*, 22, (1991), pp. 197-231; and confirming the quality of the ANICs' labour force James Riedel, "Economic development in East Asia: doing what comes naturally", in Helen Hughes, (ed.), *Achieving Industrialisation in East Asia*, (New York: Cambridge University Press, 1988), pp. 25-27.

⁶⁷. OECD, *The Newly Industrialising Countries: Challenge and Opportunity For OECD Countries*, (Paris, OECD, 1988), p. 8; also discussion in Tun-jen Cheng & Stephan Haggard, *Newly Industrializing Asia in Transition: Policy Reform and American Response*, (Berkeley: Institute of International Studies, University of California, 1987), pp. 3-9.

cheap land, labour, and natural resources, and are eroding the ANICs' share of the world markets, mainly in the labour-intensive industrial products, e.g. textiles, footwear, toys, and consumer electrical products. As soon as these low cost developing countries in the region started the process of catching-up the ANICs by adopting export-led strategies for economic development in the early 1980s, the ANICs' trading position as a group of low cost manufacturing exporters was at stake.

In addition, the ANICs' position as an attractive low cost production base has also been weakened, above all in labour-intensive industries. For example, as Thomson Consumer Electronics, the French electronics giant, is chasing lowest-cost labour to keep its products competitive, the company has been operating in East Asia since 1975 because of cheap labour costs. In response to the increase of labour cost in the ANICs (See Table 4.2), Thomson has cut production in Taiwan and Hong Kong and opened plants in South China and Indonesia, as many ANICs' indigenous industries are also relocated in their neighbouring countries.⁶⁸

TABLE 4.2. THOMSON'S SURVEY OF LABOUR COSTS

country	labour (French Francs cost/hour)
Germany	120
France	100
UK	60
Taiwan	25
Hong Kong	22
Singapore	20
Thailand	6
Malaysia	5
China	2.5

Source: *The Times*, (7 October, 1992), p. 28.

⁶⁸. For more details see Ross Tieman, "Broadening horizons of Asia Pacific extend opportunities for the West", *The Times*, (7 October, 1992), p. 28.

Moreover, at the other end of the economic development spectrum, developed countries, facing intensifying competition from their trading counterparts, have quietly imposed protectionist measures, notably by setting up import restrictions, including tariff and above all non-tariff barriers, against exports from other economies (e.g. the EC's import quotas, export restraints, and unfair trade measures), though the free trade spirit has always been claimed. Particularly, during the worldwide economic recession, the ANICs have steadily expanded their shares in world markets with the increase of trade surplus against most of their trade partners, which have incurred new protectionism in the EC and the US. According to an OECD study, discriminatory trade restrictions by OECD countries have risen in recent years and mainly focused on Japan and the ANICs.⁶⁹ Focusing on the EC's trade policy to the ANICs in the 1980s, one study suggests that the EC import barriers not only increasingly target developing countries in general and the ANICs in particular, but also their new export items, e.g. colour TVs, and computers that arouse fierce competition to EC products.⁷⁰ The other study points out that the ANICs, for example, have often become the targets of the EC anti-dumping charges, due to their substantial trade surplus against the EC and the lack of bargaining power.⁷¹ (see Table 4.3)

To fortify their international competitiveness, the ANICs have, since the mid-1980s, launched a process of industrial restructuring, seeking to upgrade their industrial structure by, on the one hand, increasing investment in improving the quality of their products and upgrading technology, and on the

⁶⁹. Ibid., p. 73.

⁷⁰. Sun-Taik Han, *European Integration: The Impact on Asian Newly Industrialising Economies*, produced as part of the research programme on Globalisation and Regionalisation, (Paris: OECD, 1992), p. 27.

⁷¹. Chien-nan Wang, and Jui-ling Hsu, "The impacts of the European integration on Taiwan and Taiwan's responses", 1992 Sino-European Conference on Economic Development: Impacts of the European Integration and Responses of Non-EC Countries, Chung-Hua Institution for Economic Research, Taipei, Taiwan, 6-7 May 1992.

other hand, allowing more inefficient sun-set industries to die or relocate, instead of merely sticking to their previous strategy of cutting production costs. These processes of restructuring have derived, to a large extent, from external competition for markets and advantage. As a result, the ANICs' efforts at exogenous industrial restructuring have reinforced the existing regional industrial division of labour that has been exploited by the Japanese for years.

TABLE 4.3. EC ANTI-DUMPING CASES AGAINST ITS TRADE PARTNERS

Exporting countries	1981-1984	1985-1988
Developed countries	60	31
Developing countries	45	79
ANICs	3	27
Taiwan	3	6
South Korea	1	14
Non-Market countries	98	31

Source: Chien-nan Wang, and Jui-ling Hsu, "The impacts of the European integration on Taiwan and Taiwan's responses", in 1992 Sino-European Conference on Economic Development: Impacts of the European Integration and Responses of Non-EC Countries, Chung-Hua Institution for Economic Research, Taipei, Taiwan, 6-7 May 1992.

A large part of the ANICs outflow of investment in and industrial relocation to Southeast Asian countries and China happened in the last few years and has dramatically changed the economic structure of East Asia. This new trend of investment from the ANICs has been more substantial than investment from the Transnational Corporations, because the ANICs' investment in those neighbouring countries has involved a lot more companies, which is crucial if economic integration is to take place. For example, according to the Taiwan official figure in 1993, there were about 2,600 companies

investing about US\$900 million in Mainland China.⁷² South Korea has also increased its investment in China sharply from US\$42.4 million in 69 projects in 1991 to US\$205 million in 270 projects in 1992.⁷³ Subregional economic groupings have emerged as a result of the ANICs' pursuing industrial adjustments together with their efforts to globalise their enterprises and markets.

Apart from their rapid growth performance, it is difficult, as one analysis has suggested,⁷⁴ to find a common denominator of characteristics amongst the ANICs. Each ANIC has its particular background of economic development which has shaped its own industrial structure, such as the development of South Korea and Taiwan with their relatively sound monetary and fiscal policies when compared with Singapore and Hong Kong's free markets. During the ANICs' earlier development, their common shortage of resources, and narrow domestic markets characterised their development. In terms of industrial structure, Korea and Taiwan are quite similar since both have concentrated on manufactures. In comparison, Hong Kong and Singapore, experiencing an entrepot development, are much more focused on international services (business, transport, financial, communication, etc.), although they are also remarkably successful in the export of manufactures which accounted for over 20 per cent of their GDP annually in the first half of the eighties.⁷⁵ Nevertheless, whatever the basis of ANIC prosperity, their economic success

⁷². The official figure was calculated by the registration in the Ministry of Economic Affairs. Although the actual figure remains unclear, the figure suggested by the Ministry put it around 4,000 companies and US\$3 billion. See K. L. Kao, *Kuo Ton Kan Ling Yu Lian An Kuen Si* (National Guidelines for Unification and the Relationships between two Sides of the Taiwan Strait), Mainland Affairs Council, Executive Yuan, Taipei, 1992.

⁷³. Shim Jae Hoon, "China market roars", p. 45.

⁷⁴. OECD, *The Newly Industrialising Countries-Challenge and Opportunity For OECD Countries*, p. 8.

⁷⁵. Ibid.

has been based on the export of certain labour-intensive products.

Since the mid-1980s, the United States has investigated the ANICs' advantages in trade with the US and has tried to deal with the East Asian economies individually rather than in "a monolithic whole".⁷⁶ In the late 1980s, while the US has continuously conferred the GSP to most Southeast Asian countries and China allowing their products easy access to the US market, the ANICs' GSP status has been eliminated.⁷⁷ These factors are further weakening the competitive advantage of the ANICs. For instance, Korean economic success was partly dependent on the creation in 1970 of export zones based on 90 per cent Japanese investment. However, spiralling wages, trade union militancy, high land prices and fixed government policy for export have already damaged the confidence and the competitiveness of Japanese companies in the zones. As the original advantageous incentives for investment no longer exist, the Japanese are increasingly likely to move out of the Korean zones soon.⁷⁸ Moreover, the increasing pressure on the appreciation of the ANICs' currencies has sharpened the threat to the competitive advantage of their exports.

The ANICs' capital- and technology-intensive industries linked with the developed markets were hit by the worldwide recession and savage competition in the late 1980s, especially shipbuilding, auto, and machinery industries, as well as

⁷⁶. The differentiated US policy towards East Asian economies was identified in a report "U. S. trade relations with Asia" of a staff study mission to Korea, Taiwan, Hong Kong, China, Thailand, Singapore, and Indonesia, to the Committee on Foreign Affairs, US House of Representatives, (November 30 to December 27, 1986).

⁷⁷. The GSP is based on duty-free treatment on most manufacturing products from developing countries with the exception of textiles and some leather products. The continuing GSP treatment has been linked to the actual trade performance of each developing country, by products. When exports to the US exceed an absolute threshold related to US GNP (around \$57 million in 1989) or account for more than 50 per cent of all exports from developing countries of that product, the US will call off the GSP treatment in the following year. See Richard Cooper, "Trade policy as foreign policy", in Robert M. Stern, (ed.), *US Trade Policies in a Changing World Economy*, (Cambridge, Massachusetts: The MIT Press, 1989), p. 303.

⁷⁸. "Goodbye to all that", *Far Eastern Economic Review*, (13 December, 1990), p. 64.

computer industry. For example, for fear of excessive capacity at a time when shipbuilding suffered from world recession, some companies, Daewoo Shipbuilding and Heavy Machinery Co., Hanjin Heavy Industries Co., and Hyundai Heavy Industries Co. have agreed with the South Korean government imposition of a limitation on shipbuilders' capacity.⁷⁹ The fast growing South Korean and Taiwanese computer makers were among the victims of world recession and the computer price war in 1991 launched by the big three, IBM, Apple, and Compaq Computer Co.⁸⁰ Taiwan's Acer Inc., the leading computer maker, suffered a substantial loss of revenue.⁸¹

In South Korea, while Samsung Electronics was expected to post a loss of US\$40 million on exporting personal computers, Koryo Systems, the country's 1990 Silver Tower Trophy holder of export performance award and the fifth largest computer maker, even went out of business in October 1991.⁸² In addition, many ANICs' industries have been based on investments by the developed economies, notably Japan and the United States, either through joint venture agreements or by licensing, from which their indigenous industries will gain access to higher technology. However, these channels have seldom offered a total transfer of the technology from the investors, especially the Japanese. Rather, through these agreements or investments, the developed economies have continued to dominate. For instance, although Samsung, the

⁷⁹. The South Korean government curbed shipbuilding companies from expanding in August 1989 and has now lifted the ban in spite of Daewoo, Hanjin, and Hyundai's opposition. See *Korea Newsreview*, (1 January, 1994), p. 26.

⁸⁰. "Computer crash", *Far Eastern Economic Review*, (17 October, 1991), p. 105.

⁸¹. Although Acer's rapid expansion in the late 1980s was responsible for draining out its profit margin, worldwide recession faltered its pace. See Carl Goldstein, "Acer in the hole", *Far Eastern Economic Review*, (13 December, 1990), p. 62. Returned from stagnation since early 1993, Acer's ambition to be one of the world's top five PC makers remains alive. See special interview to Acer's Chairman Shih, I. L. Yany, "Hong Gi Ru Her Fan Bai Wei Shern" (How did Acer come back), *Commonwealth*, (1 August, 1993), pp. 104-109.

⁸². "Computer crash", p. 105.

TABLE 4.4. THE ASIAN NICS INVESTMENT IN REGIONAL DEVELOPING COUNTRIES (US\$ mil.)

HK/ ^a	China	Indonesia	Thailand	Malaysia	Philippines
1987	1,947	135	125	11	28
1988	3,466	240	451	50	27
1989	3,160	407	561	42	133

Taiwan/ ^b	China	Indonesia	Thailand	Malaysia	Philippines
1989	552	158	892.2	815	148
1990	1,011	618.3	782.59	2,383	140
1991	1,737	1,056.5	583.46	1,314.21	11.61
1992	6,430	563.3	290	602	9.27

Sing./ ^c	China	Indonesia	Thailand	Malaysia	Philippines
1986-88	111	116	157	112	1
1989	124	166	411	338	24

S Korea/ ^c	China ^d	Indonesia	Thailand	Malaysia	Philippines
1986-88	na	78	171	7	1
1989	na	466	41	70	17
1990	22.1	na	na	na	na
1991	42.4		1,141 (ASEAN 4) ^e		
1992	205		1,424 (ASEAN 4)		

Note: ASEAN 4 = Indonesia+Thailand+Malaysia+Philippines.

Sources: ^a. E. K. Y. Chen, "Foreign Direct investment in East Asia", *Asian Development Review*, 11: 1, (1993).

^b. Majestic Trading Co. Ltd., London - 1993 Annual Report.

^c. W. B. Kim, "Industrial restructuring and regional adjustment in Asian NIEs", *Environment and Planning A*, 25, (1993).

^d. Shim Jae Hoon, "China market roars", p. 45.

^e. Actual investment figure. Ed Paisley, "Time for a new start", *Far Eastern Economic Review*, (13 August, 1992), p. 38.

then biggest conglomerate in Korea and also maybe the biggest single electrical producer outside Japan in Asia,⁸³ has made a tremendous effort to increase its world market share of electrical products in the last few years by upgrading its technology through its R & D spending, it is still suffering

⁸³. "Samsung: Korea's hope for high tech", *Business Week*, (27 January, 1992), pp. 22-24.

from the shortcomings of its core technologies i.e. sophisticated computer IC and semi-conductors. For these it is still heavily dependent on Japanese technology.

The structural problems of the ANICs are clearly shaped by two-way pressures: the low production costs of other regional developing countries facing their downstream industries, and the technology constraints on the upgrading of their higher value-added industries. In fact, for the ANICs these are not only problems of industrial restructuring itself, but also a political challenge ahead to re-organise regional economic cooperation (refer to Appendix F-4.1). In the process of industrial restructuring the ANICs have released domestic capital to invest in Southeast Asian countries and China (see Table 4.4). These investment flows have also carried a transfer of technology and management practices, and an increase in local employment, which has made up a regional framework for division of labour.⁸⁴ As a result, the momentum for further regional economic integration has been generated.

4.3. THE INTERNATIONAL DIVISION OF LABOUR AND REGIONAL ECONOMIC INTEGRATION

Although there have not yet been formal discussions amongst the ANICs about integration and there has been keen competition for overseas markets, they are actually increasing their consultation and business cooperation among themselves, for example over Singapore's client role for Taiwanese products exporting to South Asia and the former Soviet Union, and Hong Kong's role of matchmaker for the business marriage

⁸⁴. Drobnick, "Economic Integration in the Pacific Region", 1992, p. 25.

of Taiwanese and Chinese products. A "vertical development" linking the ANICs and their neighbouring economies in the context of industrial division of labour has been going on substantially and spontaneously largely through business links and other economic pursuits in East Asia.⁸⁵ To some extent, this growing trend of integrating the progress of regional economic development in East Asia has demonstrated a strong impetus to endorse the likely subregional economic groupings, albeit political cooperation within the region has been less likely to take a lead in the efforts for regional economic integration. In this favourable economic context with the ANICs projecting their innovative economic capacity into the region, subregional economic groupings have been arising. Regional economies have already benefited from their economic complementarity to each other through certain industrial divisions of labour.

4.3.1. The Hong Kong-Guangdong-Shenzhen Triangle

The most outstanding example of a subregional economic grouping is Hong Kong's efforts to participate in and benefit from China's economic development. The growing triangular economic zone of Hong Kong, Guangdong, and Shenzhen special economic zone is to be the next growing star in prosperous East Asia. The Province of Guangdong itself has become the fastest growing area in the world, and will within two decades become the "fifth tiger" following the current four tigers,

⁸⁵. Each of the ANICs is building its own "market sphere of influence" with geographic proximity linking their neighbouring economies together. In terms of economic development timing, the term "vertical development" hence implies the economic relationship between each ANIC and its neighbours.

namely Hong Kong, Singapore, Taiwan and South Korea.⁸⁶ Whilst Southern China has got huge potential for cheap labour coupled with the government's special preference for export-orientation, Hong Kong is pouring huge amounts of capital, technology, knowledge of marketing, business and financial services and skills and management into economic cooperation. Japanese and American investment has been playing the same role in Taiwanese and Korean economic development as Hong Kong investment in China. On the one hand, Hong Kong enjoys low cost of production, but is prepared to share the advancing market and manufacturing experience, on the other. The industrial structure of this combined economy has been focused on manufacturing due to its cheap labour and easier access to raw materials and markets.

In the long run, China's heavy industrial experience may well be a critical driving force for the absorption of Hong Kong's commodity economy. As most of Hong Kong textile and electrical industries are limited in their access to most of the OECD's markets by various non-tariff barriers, especially anti-dumping regulations and Voluntary Export Restraint, cooperation with China offers the easiest access to these markets for manufacturers. This is a way of circumventing trade restrictions protecting developed markets. In turn, Hong Kong's informed business and development experience has benefited Chinese development. In addition, notwithstanding the fact that Hong Kong is about to be handed over to China in 1997, the British colonial linkage gives it a pivotal position to cement the relations between this triangle and the EC. With

⁸⁶. Li Hau, Chinese Communist Party secretary for the city of Shenzhen, proposed in November 1991 that developing the city at current economic growth rate, will mean that in twenty years Shenzhen will be able to keep pace with Hong Kong and Singapore. See *Sing Tao Daily News*, (23 November, 1992); also "The fifth tiger is on China's coast", *Business Week*, (6 April, 1992), pp. 22-24.

respect to the exchange of information, marketing experience, and market resources, this triangular development is critical to China and to those who are concerned with China's market. If Hong Kong keeps its free trade orientation after 1997, it will need to expand its access to markets to further strengthen its competitiveness. The spontaneous linkage of the triangle tells that the ANICs with their narrow domestic market and poor resources are expecting to amplify their own economic scope by linking up with other economies.

4.3.2. The Singapore-Johor-Riau Growth Triangle

Another triangle economy, which is to be an innovative example of joint marketing at the international level, is comprised of Singapore, the Malaysian state of Johor and the Indonesian Riau Islands (Batam and Bintan). Following a series of Singapore-Indonesia and Singapore-Malaysia ministerial meetings from 1988 to 1991, the Growth Triangle has officially come into being. The initiatives for this subregional economic grouping were derived partly from Singapore's desire to strengthen its international competitiveness, and partly from Singapore's new thinking on ASEAN's fruitless economic cooperation.⁸⁷ This again is another complementary economic complex. Speaking at an investors' forum in Jakarta in 1990, Lee Hsien Loong, Singapore's then Trade and Industry Minister, said:

"Singapore is short of land and labour, but has more developed infrastructure and a higher concentration of manufacturing and service industries. Indonesia (as well

⁸⁷. Michael Vatikiotis, "Triangular vision", *Far Eastern Economic Review*, (26 July, 1990), p. 15.

as Malaysia) has abundant labour and natural resources, and potential for tremendous growth once these are organised and developed."⁸⁸

As the Singapore industrial structure is dependent heavily upon foreign investors, which consist of many TNCs, the triangle is intended to develop higher technology by offering an enormous investment opportunity and environment to those investors who come from the developed countries with their high technology. In order to globalise its economy to cope with future competitive challenges, Singapore which has learned from the experience of the TNCs, has been trying to extend its hinterland to its neighbouring economies as a way of expanding its economy. Allowing neighbouring economies to share its successful economic performance, Singapore has been trying to portray itself as an economic powerhouse in the triangle to be the broker for further updating advanced high technology from the TNCs and a manager for economic development. Tun Daim Zainuddin, a former Malaysian Finance Minister, realises that "Prosperity is our goal, and that prosperity should be shared".⁸⁹ It is this which has brought the triangle economic complex into effect.

The concept of the triangle has stemmed from the global competitive strategy of the TNCs which have diversified their production processes in different countries. The purpose of the diversification of production has been the search for competitive advantage. The Japanese electrical giant Sony, for example, has been producing some electronics components in Taiwan, assembling in Malaysia, but helping its marketing and management operations in Japan. Indeed, with Batam and Johor's ready labour and land at competitive rates, and Singapore's efficient infrastructure and technical expertise, the triangle

⁸⁸. Ibid.

⁸⁹. Sandra Burton, "Growing by leaps-and triangles", p. 24.

is making itself more attractive to foreign investment and more competitive in world markets. This is what Singapore's former Prime Minister, Lee Kuan Yew has envisioned: "From Singapore, they can serve not only their home market, but also the regional and world markets. Furthermore, they can tap the region's bigger and cheaper labour pool. Labour-intensive parts of a product can be done in neighbouring countries and exported to Singapore for more capital- or skill-intensive operations."⁹⁰

If a single subregional grouping is thought of as an element of Asia-Pacific regional economic integration in a limited area, the drive will certainly be derived from a common interest in economic development. The Growth Triangle was initiated by the governments of Singapore, Malaysia, and Indonesia, but their movement has lagged far behind the businessmen's pace of development.⁹¹ Although some sceptics in Malaysia and Indonesia see this project as having specific Singaporean objectives, already in 1991 there were 28 multinational corporations, including the regional biggest business group Liem Sioe Liong's Salim Group and companies controlled by Suharto's family, planning to invest in Batam Island in response to Singapore's proposal for the development of the Triangle.⁹²

4.3.3. Taiwan's Economic Sphere Of Influence

Taiwan's economic activities for competitive advantage stretch both to the developed economies for higher technology

⁹⁰. Ellen Salem, "Twinned hinterlands", *Far Eastern Economic Review*, (18 August, 1988), p. 77.

⁹¹. The private sector has been playing a much more active role in the process of inching ahead the grouping than the governments. see T Aoki, and H. Ohashi, "Asia: integration of the world's most dynamic economies", p. 27.

⁹². Michael Vatikiotis, "Search for a hinterland", *Far Eastern Economic Review*, (3 January, 1991), p. 35; It is said that Indonesian tycoon Liem Sioe Liong's close relationship with the Singapore government has helped advocate the concept of the Triangle. See special report *Central Daily News*, (13 March, 1994).

and the developing economies for low cost production factors. Many have already noticed that Taiwan as Asia's newest banker is challenging the Japanese role "as the paymaster of regional industrial integration."⁹³ It is outstandingly cash-rich, according to a recent report. Its foreign exchange reserves have reached the highest in the world at over US\$90 billion (in 1992), and it has become an attractive investor in the region. Taiwan has been going through a process of industrial restructuring and structural adjustment during the last decade. Many small and middle enterprises, especially those inefficient and labour-intensive industries on which the Taiwan miracle was based, have barely survived international competition because of rising labour costs and land prices, currency appreciation, and tighter pollution controls at home. The adjustment itself through outflow investment and manufacturing relocation has facilitated a hope for regional economic integration.

TABLE 4.5. THE TOP FOUR FOREIGN EXCHANGE RESERVES HOLDERS
(US\$ bn)

	Taiwan	Japan	Germany	USA
1992	90.1	71.6	91.0	60.3
1993	84.2	98.5	77.9	62.4

Source: *The Economist*, (12 March, 1994), pp. 153-154.

To break through its diplomatic isolation and to maintain its competitive advantage, the Taiwanese government is actively promoting overseas investment.⁹⁴ Companies seeking

⁹³. See *Time*, (13 January, 1992), p. 15; and Jonathan Moore, "The upstart Taipans", *Far Eastern Economic Review*, (19 April, 1990), pp. 82-87.

⁹⁴. Overseas investment as an instrument of foreign policy tightly links investors and the host countries. These international economic linkages are expected to tie countries' interests closer. These diplomatic concerns are especially meaningful for Taiwan since direct investment can be an effective approach to both markets and friendship. Perhaps, its capital is the only trump card that Taiwan has got in hand. See "Taipei's Offshore

low-cost bases for manufacturing products destined for the US and the EC markets started the latest investment wave in 1987. Most are labour-intensive industries making shoes, garments, toys, handbags and consumer electronics in South East Asia.⁹⁵ Apart from the low-cost manufacturers of South East Asian countries, the overseas Chinese communities which have been easily tied to Taiwanese business and offered powerful local marketing allies for Taiwanese entrepreneurs, have been another attractive incentive for investment in Taiwan. The similarity of social and cultural background is also an important factor for investors. Since the investment wave started, Taiwanese investment has rapidly increased in South East Asian countries. Investment to the region which accounted for over US\$ 500 million in 1987 (by early 1993, this figure went up to US\$ 12 billion)⁹⁶ and for US\$ 2.5 billion in 1989 including China, has been recognised as "the key to a second spring for Taiwan industry."⁹⁷ Indeed, this is especially important for those labour-intensive and low-technological industries, such as Hua Loong Textile Co., and the national China Steel Co. in Malaysia, and the Yuen Foong Yu Paper Manufacturing Co. in Indonesia. Moreover, Taiwanese investment in this region has become ubiquitous not only among ASEAN members but also in Vietnam. A new figure shows that Taiwan and Hong Kong are the biggest foreign investors in Vietnam. Up to early 1994, together they have proposed more than US\$ 2.7 billion (total \$6.8 billion) in 269 projects (total 787), and far outpaced the regional number one investor - Japan.⁹⁸

Trade between Taiwan and China is booming much more significantly, as both sides have gradually allowed the expansion of communication between their complementary

Empire", *Far Eastern Economic Review*, (18 March 1993), pp. 44-50; also "China, Taiwan and hurt feelings", *The Economist*, (19 February, 1994), pp. 73-74.

⁹⁵. Jonathan Moore, "The upstart Taipans", p. 84.

⁹⁶. That accounts for almost half Taiwan's outflow investment US\$25 billion. See "Taipei's Offshore Empire", p. 44.

⁹⁷. Jonathan Moore, "The upstart Taipans", p. 86.

⁹⁸. See "Asian investors lead the way in Vietnam", *Financial Times*, (24 February, 1994), p. 7.

economies. Although for political reasons trade is still indirect, most of it via Hong Kong, and the rest via Japan and Singapore, the competitive advantage for investors is attractive. Recently, Taiwan entrepreneurs have been focusing their investment to China on the south east coastal province of Fujien - Xiamen, due to kinship, the same dialect and geographic proximity.⁹⁹ Some criticise Taiwan businessmen in this area as merely seeking for short-term advantage rather than long-term development of the area. In fact, Taiwanese investment is dependent upon market conditions which means that investment is following Chinese economic indicators. Because the Beijing regime may change its policy after the communist old guards leave the scene, the uncertain political situation has cast some doubt on long-term investment. In addition, bureaucratic red tape, management problems and a shortage of raw materials has frustrated not only hundreds of manufacturers already operating there but also a great number of investors.¹⁰⁰ In spite of some scepticism about the future, economic and even political contacts between Taiwan and China are still increasing steadily. Apart from increasing trade and investment figures, and the regular basis of the quasi-official talks between the Strait Exchange Foundation and the Association for Relations Across the Taiwan Straits, recently, the Taiwanese government has proposed a joint venture with Singapore to explore oil, natural gas, and tourism on China's Hainan Island.¹⁰¹

In terms of economic development, Taiwan like other ANICs, is half way to becoming a developed economy. What it is really short of is the high technology to upgrade its industrial high value-added products. With respect to

⁹⁹. Taiwanese businessmen recognise that kinship and sharing the same dialect with Fujien people are sometimes even more important than a contract particularly for running businesses in the Chinese society, in terms of establishing "guan si" (personal relationships) and introducing management knowledge.

¹⁰⁰. Julian Baum, "Second thoughts", *Far Eastern Economic Review*, (1 November, 1990), p. 68.

¹⁰¹. Margaret Dawson, "The Taiwan Strait never seemed so narrow", *Business Week*, (24 January, 1994), p. 24.

technology, Taiwanese investment to the region has almost nothing to do with the procurement of technology. Rather, regional economic integration is much more concerned with production and market cooperation. In the sense of regional integration, Taiwanese economic development has been tied firmly to the regional countries through the export of direct investment, low- and middle-level technologies and manufacturing experience, and the import of raw materials and labour forces. One might expect the "spillover" effect to come in the scope of industrial cooperation and of policies concerned. In other words, their mutual interest will be converged in international trade negotiations for the products concerned. For example, in early 1992, while the US Congress was seeking to link the annual renewal of China's Most Favoured Nation (MFN) trading status to fulfilment of American demands on human rights, missile proliferation, and trade practices as a way of disciplining China, Hong Kong and Taiwan foresaw that they would suffer a great loss. Therefore, both Taiwan and Hong Kong took an action to urge "the United States to maintain China's MFN status."¹⁰²

4.3.4. The Northeast China-Korea--Japan Triangle

As an ANIC, South Korea also can not escape from structural problems. South Korean development has been much more determined by state intervention than that of other ANICs. To implement structural adjustment for short-term as well as for long-term purposes, South Korean government intervention has been the main driving force in response to

¹⁰².For details see Harry Harding, "The US and Greater China", *The China Business Review*, (May-June 1992), p. 22.

fierce international competition. Recently, for instance, to make better use of investment in technology and productivity to increase competitiveness, the South Korean government has called for an industrial specialisation policy of reorganising industry which asks *chaebol*, the highly diversified industrial conglomerates, to concentrate on three core businesses.¹⁰³ Since its development is focused on large and heavy industry, this direction has resulted in its industry being characterised by rapidly changing comparative advantage, highly concentrated export markets prone to protectionist pressures, a high degree of industrial concentration, and a strong technological dependence on Japan.¹⁰⁴

South Korean industries have been through structural adjustment for a decade or so, and comparative advantage has shifted from traditional and labour-intensive industries (such as textile yarn and thread, cotton fabrics, wood manufactures, printed matter, sound recorders, and office supplies) to capital-intensive industries (such as ships, electrical equipment, metal products and iron and steel). Although this adjustment did enable some industries to survive international competition, South Korea like other ANICs is encountering a technological threshold which may not be easy to break through by national R & D spending. This is the reason why the ANICs are eager to seek the possibility of joint ventures or any kind of technical cooperation programme in order to get the higher technology for upgrading their industries.

Since South Korea's recent main industrial strategy has been concentrated on its moving up the technology ladder,¹⁰⁵

¹⁰³. See John Ridding, "S Korea's industry giants pick their core businesses", *Financial Times*, (23 April, 1991), p. 4.

¹⁰⁴. D. M. Leipziger, "Industrial Restructuring In Korea", *World Development*, 16: 1, (1988), p. 126.

¹⁰⁵. OECD, *The Newly Industrialising Countries*, 1988, p. 37.

many resources have been devoted to this end. In spite of its having the highest spending in R & D among the ANICs and trying to reduce technology imports from Japan, South Korea is still heavily dependent upon Japanese technology (see Table 4.6). In addition, as the South Korean industrial restructuring has changed the focus of its industrial activities to capital-intensive sectors, traditional overseas markets have been replaced by the developed markets of the EC and North America. To compete with these developed economies and other Asia-Pacific subregional economic groupings, South Korea's need to develop its technology ladder has increased its close relationship with Japan.¹⁰⁶

TABLE 4.6. SOUTH KOREA TECHNOLOGY IMPORTS FROM JAPAN (US\$ million)

	amount	No.	amount	No. (in %) ^a
1962-80	168.3	1017	36.8	58.8
1985	35.4	108	25.2	50.2
1990	341.4	333	31.4	45.1
1991	372.5	277	31.5	46.8
1992	266.3	232	31.3	43.5

Note: ^a. Japan's share of percentage in total.

Source: Based on Korea Institute for International Economic Policy, *Korea Newsreview*, (19 February, 1994), p. 16.

To extend industrial capacity and to survive from international competition, South Korea has already spread out its labour-intensive industries to north east China as well as to the South East Asian countries. Korea, like Japan, has also entered into China's domestic market, albeit its pace has been far behind Hong Kong and Taiwan. Since the normalisation of the Beijing-Seoul relationship in August 1992, the two way trade has been increasing.¹⁰⁷ In the sense of economic

¹⁰⁶. "Technology imports from Japan dwindling", *Korea Newsreview*, (19 February, 1994), pp. 16-17.

¹⁰⁷. The statistics show that while its imports from China have steadily grown from US\$3.4 billion to \$3.9 billion, South Korea's exports to China have doubled in the same period

development, South Korea is playing the middle man role to Japan and China. The industrial focuses of Japan (advanced technology), Korea (skilled and marketing experience) and China (low-cost production and manufacturing base) represent respectively three different development levels of a complementary economy which is conducive to their further economic cooperation.

It is clear that Seoul's rush towards China is not purely business.¹⁰⁸ Politically, South Korea's desire to strengthen its position against North Korea has served as a drive to develop relations with China. Seoul's political intention is in accordance with Beijing's policy which centres on maintaining peace and stability in the peninsula in order to assure a peaceful environment for China's development. A "dual track" approach, which ties simultaneously to Pyongyang and Seoul, has become China's Korean policy after the 1980s.¹⁰⁹ Moreover, China's huge domestic market is attractive to Korean entrepreneurs. The rapidly growing Chinese economy has motivated the South Korean economy undertaking the restructuring of its industry. China is now the most preferred country for investment of South Korean enterprises.¹¹⁰ With geographic proximity, ethnic connection, and historic links to Korea and Japan, Shandong and Liaodong Peninsulas as well as the area along the Yellow Sea have become the main economic zone of Korean and Japanese investment. The zone has long been characterised as a heavy industrial development centre with easy access to raw materials, such as oil, iron ore, and coal, and with China's skilled but cheap workers.

from \$2.37 billion to \$5 billion. See Yu Kun-Ha, "Korea-China economic ties rise to new peak", *Korea Newsreview*, (26 February, 1994), p. 26.

¹⁰⁸ "South Korea plays the China card", *Business Week*, (11 April, 1994), p. 19.

¹⁰⁹ Hao Jia, and Qubing Zhuang, "China's policy toward the Korean Peninsula", *Asian Survey*, 32: 12, p. 1142.

¹¹⁰ *Korea Newsreview*, (26 February, 1994), p. 26.

Therefore, South Korea has been increasing investment in and cooperation ties with China, as this cooperation will not only allow Korean industries access to the market and improvement of their international competitiveness but will also win Chinese assurance in regional security to tame North Korean aggression. The Chinese market, an increasing exports' destination for South Korean industrial goods, rose from 71.4 per cent in 1991 to 164.7 per cent in 1992. Targeting the China market potential, Hyundai Group has boosted its car sale from shipment of 714 units in 1992, worth US\$9.5 million, up to 14,700 units worth US\$148 million in the first quarter of 1993.¹¹¹ Already, as many South Korean heavy industrial companies have profited from their investment in this area, such as Daewood's cement factory in Shandong, Samsung Electronics' VCRs assembly in Tianjin, and Goldstar's industrial water pipe plant, more small- and medium-sized firms are following suit.¹¹² Although Japan's investment in China is behind that of Hong Kong, Taiwan and the US, due to its concerns about the high risk of investing in China, recently, some Japanese big firms, Toshiba, Sanyo, Canon, Sanyo-Nissho Iwai, Matsushita, have started to pour in capital and technology to Dalian, a port for Liaodong Peninsula.¹¹³

Through existing economic links, a new subregional grouping in Northeast Asia has emerged. The concept of Northeast Asian Economic Cooperation has included two economic development areas: the Yellow Sea Economic Zone combining South Korea, Japan, and the Chinese provinces of Liaoning and Shandong, and the Tumen River programme with China, two

111. Shim Jae Hoon, "China market roars", p. 46.

112. Ed Paisley, "The harvest to come", *Far Eastern Economic Review*, (3 September, 1992), p. 12.

113. "A golden gate on the Yellow Sea", *Business Week*, (14 March, 1994), p. 22.

Koreas, Japan, Russia, and Mongolia.¹¹⁴ The Yellow Sea Economic Zone, as yet an academic sketch, has been characterised by complementary economic links between China-South Korea-Japan. The Tumen River programme now envisioned under the United Nations Development Program (UNDP) has become attractive because it is also a complementary economic complex which will combine China, Russia, and North Korea's abundant natural resources and manpowers with South Korea and Japan's capital. Moreover, its enormous potential as a regional market "could encompass nearly 300 million population, have a collective GNP of almost US\$3 trillion, and account for nearly one-third of world trade."¹¹⁵ Again, like other subregional economic groupings in Asia-Pacific, these two concepts to make up of Northeast Asian trade bloc as a whole, are driven mainly by academics and businessmen, and less by any governmental commitment.¹¹⁶ However, most recently, South Korean President Kim has brought his vision of Yellow Sea Economic Zone to China's leaders. As a result, both China and South Korea have agreed to cooperate in four key industries, autos, aerospace, telecommunications, and electronics.¹¹⁷

4.4. THE PROSPECTS FOR REGIONAL ECONOMIC INTEGRATION IN THE ASIA-PACIFIC REGION

In terms of economic development, the ANICs' growing economies as a whole are threatened by low-cost producers in

¹¹⁴.For details of Northeast Asian economic cooperation see: Joseph P. Manguno, "A new regional trade bloc in Northeast Asia?", *The China Business Review*, (March-April 1993), pp. 6-11; Guo Zhen Yuan, "The related factors and prospects for the development of Northeast Asian Economic Cooperation", *The Korean Journal of International Studies*, 24: 2, (Summer 1993), pp. 171-183.

¹¹⁵.Manguno, "A new regional trade bloc in Northeast Asia?", p. 7.

¹¹⁶.Guo Zhen Yuan, "The related factors and prospects for the development of Northeast Asian Economic Cooperation", p. 172.

¹¹⁷."South Korea plays the China card", p. 18.

other developing countries and developed countries' protectionism and pressure to open the ANICs domestic markets.¹¹⁸ The ANICs export-led economies are very vulnerable and sensitive to external challenges. In the context of the development of regional groupings for reinforcing competitiveness, the ANICs' efforts towards industrial restructuring (which could be generalised as "exogenous industrial structural processes"), have generated a momentum to promote the formation of Asia-Pacific subregional groupings. Instead of being driven by political motivations, the emergence of Asian-Pacific subregional groupings has been driven by external economic pressures and the response of private sector interests. By contrast, the development of the Pan-Pacific or Asia-Pacific economic cooperation movement, has been characterised by more talking and theorising than action. Regional groupings with high political profile have not as yet been fully accepted by countries in the region. Whilst President Clinton wished to move APEC towards becoming some sort of "free trade vehicle" at the Seattle summit in November 1993, some Asian leaders remained suspicious.¹¹⁹

The ANICs' exogenous structural problems, including the wearing away of the comparative advantage of their products, and their shortcoming in advanced technology, have served as a drive to boost the possibility of forming subregional economic groupings. Projecting their economic strength in the region, the ANICs have taken practical action by means of increasing foreign direct investment in and industrial links with the region itself. While the ANICs since the mid-1980s have undertaken an industrial restructuring process, not only have

¹¹⁸.For detailed analysis about the ANICs' restructuring see W. M. Kim, "Industrial restructuring and regional adjustment in Asian NIEs", *Environment and Planning A*, 25, (1993), pp. 27-46.

¹¹⁹.James Walsh, "Toward the Pacific Age", *Time*, (22 November, 1993), p. 53.

regional economic structures changed but also more sophisticated subregional divisions of labour have developed as a result. This trend is very likely to continue, as long as regional economies continue to intensify their links with each other and regionalism elsewhere remains a head-on trade issue.

What the Asia-Pacific subregional grouping does imply for the ANICs is a need to improve their competitiveness and the prospect of mutual benefits. The biggest part of the ANICs structural problems has been the shortage of labour and falling profit margins resulting from the rising production costs at home. Subregional groupings have provided an extensive economic space to allow the ANICs to regain their competitive advantage by exchanging their economic development expertise. To a large extent, Asia-Pacific economic integration at the subregional level offers an effective means of overcoming labour shortages and of balancing differences in regional economic development. These are what the prosperous cases of Taiwan and Hong Kong tied with Southern China, and Singapore tied with the Johor state of Malaysia and Riau Island of Indonesia, have shown.

CHAPTER FIVE

THE IMPACT OF THE EMERGENCE OF THE CHINESE ECONOMIC AREA ON REGIONAL ECONOMIC INTEGRATION

The purpose of this chapter is to analyse the newly emerging geopolitical concept of the "Chinese Economic Area" (CEA) on the assumption that there are industrial advantages to economic integration,¹ and demonstrating that the process of economic integration has been driven by the profit motives of private enterprises rather than the political motives of governments. Defining the process of industrial integration, therefore, becomes the main focus here. Although the precise factors contributing to this part of regional economic integration are yet to be confirmed, industrial activities have undoubtedly been one of the major influences. The CEA's increasing intra-regional trade, and investment flows are, due to its diverse levels of development, notably based on mutual industrial complementarities between China, Taiwan, and Hong Kong. The industrial complementarity was made up of: China's comprehensive, yet elementary, industrial ability, and affluence of land and work forces; Taiwan's technology, financial power, and manufacturing ability; and Hong Kong's international marketing skills. Whilst businessmen, investors, and economists are looking closely at all intra-regional transaction flows and their implications for economies as a

¹. The notion of the "Chinese Economic Area" has been widely identified by academics and in international institutions, such as the OECD, and the World Bank, although there are some other terms in use, e.g. "Greater China", "South China Economic Sphere", "Chinese Economic Community". Basically, whatever the term, they are all referring to China, Taiwan, Hong Kong and Macao. In reality, the CEA is based on "South China Economic Sphere" which includes Hong Kong, Taiwan, Fujien, and Guangdong. Through their close industrial links, a full schedule for integration may be appearing.

whole, there is an increasing focus on the industrial level of integration.²

For many people who live in the region, any programme for integration beyond the economic level is part of a more distant dream of Chinese national reunification. In the process of forming the CEA, any moves beyond mere business considerations may reflect political intentions, since Beijing is particularly eager, though not openly, to project its own perspective on unification onto economic activities, to which Taipei is especially sensitive. On many occasions, scholars, particularly from Taiwan and Hong Kong, have been very much concerned that this hidden political intention could hurt fledgling economic cooperation. One author boldly points out that Beijing tends to politicise all economic activities as if trade is an instrument of unification.³ The increasing flow of Taiwan's investment to China is likely to be seen as "a prelude to economic and political unification."⁴ The actual development of the CEA has been inspired for decades largely by business or market forces rather than by political intentions, because of political conflict between Mainland China and Taiwan.

Since the economies of Hong Kong, Taiwan and China complement each other well, intra-economy links and close

². Randall S. Jones, Robert E. King, and Michael Klein, "Economic integration between Hong Kong, Taiwan, and the coastal provinces of China", *OECD Economic Studies*, 20, (Spring 1993). In the past few years, Charles H. C. Kao has written many articles to provoke the idea of "Economic China" mainly in his co-founded *Global Outlook*, (Monthly in Chinese); Charng Kao, "A Greater China Economic Sphere: Reality and Prospects" *Issues and Studies*, 28: 11, (Nov. 1992); see also Bruce S. Stewart, "Integrating economic resources across the Taiwan Strait", *Euroview*, (European Council of Commerce and Trade in Taipei), (June-July 1993).

³. Kai Ma, "Favourable Factors and Obstacles in Economic Development Between economies of the Taiwan Strait", paper presented in "Mainland, Taiwan and Hong Kong Economic Cooperation Trend" Conference in Beijing, (9-10 September 1993). Many others at the conference shared his view.

⁴. Natasha Alperowicz, "In Taiwan the private sector comes to the fore", *Chemical Week*, 152: 2, (January 20, 1993), p. 28.

economic relationships are already flourishing.⁵ The network for economic cooperation, therefore, has already arisen and is quickly intensifying as a result of an "unstoppable tide" of trade crossing the Taiwan Strait.⁶ Although in most of this research "economic integration" and "economic cooperation" are sometimes interchangeable in terms of the formation of a trade bloc, the former is likely to be determined by "the intensity of relations between participating states and the manner in which those relations are organized and managed."⁷ According to a recent study on the development of the CEA, Hong Kong, Taiwan and China have already collectively formed an interdependent economy by trade, foreign direct investment, and financial flows.⁸ By and large, there has been regional industrial division of labour which was traditionally regarded as tantamount to the first stage of economic integration.⁹ Since this formation is so far led by private sector profit seeking, in the years ahead, a trans-party organisation is likely to appear through business association links rather than political negotiation. The formation of the CEA could lead to its economic integration. Nevertheless, this should merely be treated as building the essence for starting the economic integration process.

According to Karl Deutsch's definition, a "community" would require a certain transaction volume to reach a "threshold" level before a group of countries can be

⁵. David K. P. Li, "Evolution of the Greater China productivity triangle", *World of Banking*, 11: 5, (September/October, 1992), p. 11.

⁶. See Julian Baum, "The unstoppable tide: rapid rise in Taiwan-China trade pressures Taipei", *Far Eastern Economic Review*, (20 May, 1993).

⁷. Brigid Laffan, *Integration And Co-operation In Europe*, (London: Routledge, 1992), p. 3.

⁸. Randall S. Jones, Robert E. King, and Michael Klein, "Economic integration between Hong Kong, Taiwan and the coastal provinces of China", *OECD Economic Studies*, No. 20, (Spring 1993).

⁹. P. Marer, and J. Montias, "The Council for mutual economic assistance", in A. El-Agraa, (ed.), *International Economic Integration*, (London: Macmillan, 1988), p. 156.

considered to be at the inception of integration.¹⁰ Although his concerns were mainly about heading towards political community, for which transaction volume will be meaningful only in accordance with the establishment of transnational institutions, it does not imply that the application of economic integration would be removed from the requirement of a threshold. What he did not clarify was the relationship between transaction volume and the threshold.

However, the development of the CEA gives evidence of a different profile. To begin with, a certain threshold level for confirming integration is clearly everywhere necessary. It is yet to be proven that political involvement is a necessary condition for transaction volume to lead to transnational institutions. There have been a large amount of transactions carrying on within the CEA, but it seems to be less likely that transnational institutions with governments' involvement would be determined by these transaction flows at present. Whereas, it is not suggested that, without clear schedules for creating transnational institutions, economic integration in the CEA would be blocked forever.

With its different characteristics from the EC, in terms of the shape and process of integration, the CEA is advancing towards its own particular form of integration. Economic development is driving similar economies to create an integrated regional economy. Nevertheless, there are some questions left to be answered. Why is pursuing economic integration in the CEA possible and necessary for three of the economies? How are economic transactions, low-politics' activities, building up confidence in the CEA in an atmosphere of continued political hostility and tension? What will

¹⁰. Karl W. Deutsch, *Political Community at the International Level: Problems of Definition and Measurement*, (Garden City, NY: Doubleday & Company, Inc., 1954), p. 39.

industrial integration imply? Is the CEA heading towards a process of economic integration in accordance with Bela Balassa's "conventional progress" framework?¹¹

5.1. THE ORIGINS OF THE "CHINESE ECONOMIC AREA"

Fomented by ever greater international competition in trade accompanied by the appearance of regional trading blocs, economic integration in this region is forcing Asian Newly Industrialised countries (hereafter the ANICs include Hong Kong, Singapore, Taiwan, and South Korea) to realise that future business development is not going to be as easy as it once was, because the ANICs' export-led economies are heavily dependent upon international markets and free trade. Through industrial cooperation with their neighbours, on the basis of developmental complementarity, they are seeking to face up to the competitive challenge posed by international rivals. The evolving concept of the Chinese Economic Area, which was brought about in this context of economic development, was initiated by academics from Hong Kong, Taiwan and China. What they have been trying to do is to develop a framework, in accordance with conventional integration theory to regulate the rapid increase of business transactions between the economies.

The listed concepts in Table 5.1 which were, to a large extent, derived from Hong Kong and Taiwan's wishful thinking about Chinese industrialisation, were coincidentally presented in the context of fierce international competition and

¹¹. According to Balassa's analysis of the levels of economic integration, there are five stages: free trade area, customs union, common market, economic and monetary union, and total economic integration. In his *The Theory of Economic Integration*, (London: Allen and Unwin, 1962).

industrial complementarity. As business transactions making up industrial complementarity have intensified in recent years, these ambiguous concepts seem to have become more useful and accessible. The incentives for regional integration have tended to be external, with international competition, industrial restructuring, and changes in international politics jointly providing a catalyst for regional economic integration.

TABLE 5.1. THE EVOLUTION OF THE CHINESE ECONOMIC AREA

1980	C. L. Huang	The Chinese International Community (HK) The Chinese Economic Community
1987	K. Y. Chen	Chinese Sphere (Asian Research Centre, HK U.)
1988	C. Y. Cheng	Greater China Common Market (Asian Studies Committee, Ball U., Indiana, USA)
1988	I. T. Chen	China Economic Sphere (Taiwan Research Institute, China Academy of Social Science, Beijing)
1988	H. C. Kao	Asian Chinese Common Market (Global Views Magazine, Taiwan)
1989	H. S. Zhin	Economic Sphere for the Both Sides of the Taiwan Strait (Asia-Pacific Economic Research Institute, Fujien Academy of Social Science, China)
1989	F. G. Chou	Southeast China Free Tree Area (Southeast Information Centre, HK)
1990	C. S. Wong S. P. Hsu	Southern China Economic Sphere or South China Economic Collaboration Area (Taiwan Research Institute, Xiamen U., Fujien)

Source: 1. *Economic Daily News*, (21 June, 1992).
 2. *Kuo Gi Ging Gih Ching Shih Chou Boa*,
 (International Economic Trend Weekly), 977, pp.
 9-10.

5.1.1. International Competition And The Context For Integration In East Asia

Economically, unlike the EC, the development of the West Pacific countries is quite heterogeneous. While Japan has been a member of the OECD for decades, others, the ANICs, ASEAN

countries (Indonesia, Malaysia, Philippines, and Thailand)¹², China and the Indo-China countries (Vietnam, Laos, and Cambodia), are still among the list of developing countries. (refer to GDP per head in Table 5.2) However, their economies enjoy, to some extent, a mutual complementarity in terms of their industrial development structures, which make different sorts of division of labour possible. In fact, Japan, the most highly developed economy, possesses the most advanced technologies which its neighbouring countries are especially thirsty for. What Japan needs, and is desperately short of is raw materials, overseas markets and basic labour forces of which these other regional countries possess an abundance.

TABLE 5.2. EAST ASIAN COUNTRIES GDP IN FOUR GROUPS IN 1990 (in US\$)

Japan	17,620	Singapore	15,880
		Hong Kong	15,600
China	1,990	Taiwan	12,670
North Korea	2,000	South Korea	6,730
Cambodia	1,100		
Vietnam	1,100	Malaysia	6,140
Laos	1,100	Thailand	3,990
Myanma	660	Philippines	2,300
		Indonesia	2,180

Source: Based on UNDP information, see "Survey: Asia", *The Economist*, (30 October, 1993), p. 6.

One has to understand that the practical advantages of cooperation are the main incentive for regional integration. At the middle level of economic development, there are the ANICs, whose industrial structures have already been enriched by capital- and technology-intensive industries and even some

¹². Singapore has been ranked in the ANICs' group, while another small but rich member of the ASEAN, Brunei, is also considered to be different from the rest of ASEAN countries.

high-technology industries, during the 1980s.¹³ At the bottom, ASEAN countries and China are catching up industrially through the same process of moving from resource-based exports to labour-intensive and low-technology manufacturing industries, as the ANICs did in the 1960s and 1970s.¹⁴

An international division of labour has, therefore, been established throughout East Asia in the past few decades. A new model of a horizontal division of labour is emerging among Japan, the ANICs, and ASEAN, as well as China. For example, Japanese automakers, Toyota and Mitsubishi, and consumer electronics manufacturers, Matsushita, have set up systems in which parts are being produced through an international division of labour right across the ANICs and ASEAN countries.¹⁵ The traditional vertical division of labour between Japan's manufacturing products and other regional economies' raw materials is becoming less prominent.¹⁶ This model is characterised not only by different levels of economic development, but also by the variety of industrial structures amongst the regional economies. Furthermore, there are different levels of technological development which may

¹³. In terms of composition of manufactured exports, the obvious increase of exports in office machines, telecommunications and sound equipment, and transport equipment has shown the changing pattern of these exports. In Singapore and South Korea, the share of these sophisticated industries accounted for less than 2 per cent in 1966 and more than 30 per cent in 1987. Taiwan's exports' structure also shows a similar change. Its share of these industries rose from 16.4 per cent in 1970 to 28.3 per cent in 1983. For the detailed list of the ANICs' manufactured exports see Anis Chowdhury, and Iyanatul Islam, *The Newly Industrialising Economies of East Asia*, (London: Routledge, 1993), pp. 75-79; for the background of South Korea and Taiwan's industrial restructuring by the government's policy see *The East Asian Miracle: Economic Growth and Public Policy*, A World Bank Policy Research Report, (Washington D. C.: Oxford University Press, 1993), pp. 127-134.

¹⁴. In the case of Thailand, while its heavy industries, high-skill, labour-intensive industries rose from 41.6 per cent in 1970 to 50.5 per cent in 1986, food and related industries declined from 39.3 per cent to 26 per cent in the same period. See *The East Asian Miracle: Economic Growth and Public Policy*, pp. 134-146.

¹⁵. Although Japanese consumer electronics sector has been redirected to local demands, its basis of international division of labour has not been diminished. Iwao Kubo, "Symbiotic growth: Japanese firms in Asia", *Tokyo Business Today*, (June 1992),

¹⁶. Unlike the horizontal division of labour, the vertical division of labour refers industrial cooperation to production process which combines upstream (obtaining raw materials) with downstream (manufacturing) industrial operation.

offer a good reason for further industrial cooperation. There have been three types of horizontal division of labour in East Asia so far. Firstly, a division of trade between manufactured products. Unlike the previous vertical division of labour, even Japan has increased its imports of manufactured goods, largely electrical machinery, by intra-firm trade between Japanese Transnational Corporations (TNCs), parent firms and their affiliates in other regional economies.¹⁷ Secondly, a division of trade between different products within the same industry, an inter-industry horizontal division of labour, e.g. trade between yarn and fabric in the textile industry, electronic parts in the electronics industry, and spare parts in the auto industry. Thirdly, the horizontal division of labour between the same kind of manufactured products with different factor combinations, e.g. the ANICs and Japan in producing video equipment, the former with simple designs and the latter with more advanced ones.¹⁸ Overall economic development and industrial structures in East Asia have been widely seen as a pattern of "flying geese" (where industrial laggards follow in the footsteps of the industrial leaders).¹⁹ While Japan leads the international division of labour in East Asia, the ANICs and the rest of the regional economies are

¹⁷. For the detailed figures of substantial Japanese increases in imports from nine Asian countries see Richard Drobnick, "Economic integration in the Pacific Rim", *Technical Papers*, No. 65, OECD Development Centre, (May 1992), p. 22; about the increase of this kind of intra-firm trade, for detail see Shujiro Urata, "The increase of direct investment abroad and change in Japan", in Eric D. Ramstetter, *Direct Foreign Investment in Asia's Developing Economies and Structural Change in the Asia-Pacific Region*, (Boulder: Westview Press, 1991), pp. 189-196.

¹⁸. Shi Chun Li, "Japan's role in the international division of labour", in Susumu Awanohara, (ed.), *Japan's Economic Role In The Asian Pacific Region: Policy Implementation and Responses*, (Hong Kong: Centre for Asian Pacific Studies, Lingnan College, 1990), p. 22.

¹⁹. In various articles, the pattern of "flying geese", which was first postulated by Japanese Professor, Kaname Akamatsu, in the 1930s, has been widely used to describe the fast growing East and Southeast Asian economies led by Japan. Refer to Saburo Okita, "Japan's role in Asia-Pacific cooperation", *Annals*, APPSS, 513, (January 1991), pp. 25-37; Joseph Romm, "Japan's flying geese", *Forbes*, 150: 12, (23 November, 1992); Steve Chan, *East Asian Dynamism: Growth, Order, and Security in the Pacific Region*, (Boulder: Westview Press, 1990), p. 41.

more or less tied into the regional industrial structure. Consequently, it seems that the emergence of regional economic integration is the preferable outcome of the rapid developing industrial division of labour in East Asia.

The Johnsonian approach, one of the traditional approaches to regional economic integration, believes that the motive for integration between smaller economies and developing countries is derived from integrating members' collective objectives.²⁰ The most obvious of these is "a collective desire for industrialisation."²¹ Basically, regional economic integration is a vehicle by which members may collectively tackle obstacles to economic development among the economies of the region and thereby increase their collective well-being. But, why should they work together? The answer lies with the similarity of developmental experience and with the international division of labour which ties up the industrial bases of member states into a more effective and stronger economy.

In terms of the TNCs, Japanese companies have maintained the headquarters of their businesses in Japan itself, manufactured components in Taiwan, and assembled products in Malaysia or Thailand. As part of their global strategy, Japanese Hitachi, and Sanyo have established the international network for their division of labour by improving the technology level of their operation in Taiwan and moving assembly operation from Taiwan to Malaysia.²² In other cases,

²⁰. Based upon a criticism to the Vinerian approach of weighing the cost and benefits of regional integration, The Johnsonian approach was developed systematically by Harry G. Johnson, "An economic theory of protectionism, tariff bargaining, and the formation of customs unions", *Journal of Political Economy*, 73,(1965); and C. A. Cooper, and B. F. Massel, "A new look at customs union theory", *Economic Journal*, 75, (1965).

²¹. Joseph C. Brada, and José A. Méndez, "Political and Economic Factors in Regional Economic Integration", *Kyklos*, 46, (1993), p. 187.

²². Chikara Higashi, and Peter Lanter, *The Internationalisation of the Japanese Economy*, 2nd edition, (Boston: Kluwer Academic Publishers, 1990), p. 344.

Japanese companies have gone to Taiwan for components which are produced by Taiwanese manufacturers in China or Southeast Asia. For example, the procurement of Cyclepress, the Japanese bicycle industry giant, from Taiwan for bicycles and components to the value of ¥20 billion (Japanese Yen) in 1993 happens to be in the context of Taiwan's industrial division of labour, i.e. "Taiwan taking orders, China producing, and exporting to Japan".²³ Originally equipped with Japanese capital goods, the Taiwanese, in addition, possess a rich and experienced OEM-oriented infrastructure (Original Equipment Manufacturer)²⁴ that "is remarkably adaptable to changes in worldwide demands."²⁵

For the same reasons, the Japanese through Hong Kong, either via subsidiaries or agents, have invested in China improving industrialisation in the region and also establishing an international division of labour. For example, an investment bank, co-funded by Japanese, C.Itoh & Co. Ltd., and by Morgan Stanley Groups, an American securities firm, in May 1993 decided to invest ¥1 billion in Chinese Strategic Investment Co., an Indonesian overseas Chinese enterprise in Hong Kong for access to Chinese market. According to C.Itoh & Co. Ltd., strategy to China through overseas Chinese is to supply some 180 Chinese national companies with machines and raw materials in order to tie them into their industrial

²³. Especially, the mounting appreciation pressure on the Japanese yen has put Japanese companies to the verge of losing competitive advantage, which directly results in Japan increasing procurement for components from neighbouring economies, instead of from costly domestic producers. The bicycle industry, among others, is most prominent one. *Central Daily News*, (26 August, 1993).

²⁴. OEM is a way of industrial cooperation between big name companies and producers, which allows manufacturers to produce goods for their buyers licensed with buyers brand names, such as in foot wear industry (OEMs: Reebok, Hi-Tech, and Puma); in toy industry, (OEMs: Hasbro, Mattel, Bandai, and Tomy). See *Importing from Taiwan*, (Hong Kong: Trade Media Ltd, publishers of Asian Sources Group of trade magazines, 1989), pp. 52-53, 55-57. Even in the computer industry, many of the world's leading computer makers turn to Taiwan's OEMs, such as IBM, Hewlett-Packard, Compaq, and Epson. See *Taiwan Industrial Panorama*, 11: 21, (November 1993), p. 3.

²⁵. See *Importing from Taiwan*, p. 43.

division of labour.²⁶ The Japanese have in these ways been able to cut their costs of production and increase their competitiveness against Western competitors. Through this Japan-Taiwan-China pattern, "Other parts of Asia are increasingly being drawn into a hierarchical network of production and exchange."²⁷

Upgrading technology, expanding market shares and managing access to raw materials are always the basis of restructuring industrial structure within a country or an industry itself. But, a new wave of severe competition in some technology-intensive industries, for instance electronic, electrical, and computer industries, has been pushing economies towards industrial integration.²⁸ Recently, international big names of Computer and Information companies, Philips of the Dutch, Microsoft, Hewlett-Packard, and International Business Machines (IBM) of the United States, have been trying to integrate related industries in Hong Kong, Taiwan, and China into their "Greater China" operation.²⁹ On the supply side, the competition has aroused the need for industry either to cut production costs or to upgrade their existing production technology. On the demand side, the need for scale economies in marketing networks has forced industry to undertake various strategic alliances.

Against this background, East Asia is entering a new era of integrating economies by tying up capital, resources, and manpower, and to an increasing extent setting up a macroeconomic policy for looking outwards. In addition to

²⁶. *Mou Yi Kuai Shuen*, (Traders' Express), 1090, (9 August, 1993).

²⁷. Mitchell Bernard, "The Post-Plaza Political Economy of Taiwanese-Japanese Relations", *The Pacific Review*, 4: 4, (1991), p. 365.

²⁸. According to the EC experience, firms are pooling their resources together for R & D and market share in order to get better positions against their American and Japanese competitors, before and after economic integration.

²⁹. For the ongoing development in the CEA see *Central Daily News*, International Edition, (13 November, 1992).

Japanese involvement in the region, Singapore, Taiwan, Hong Kong, and South Korea have contributed since the mid-1980s decisively to the booming regional economy with their massive inflows of inward investment, mature technology, and experienced management. Taiwan, for example, used to be the manufacturing base for Japanese companies through OEM exporting to the United States. Now, with most of its manufacturers of OEM moving to Southeast Asia and China, Taiwan has become not only one of the biggest investors in the region but also a capital- and technology- intensive economy, just as Japan was in the 1970s.

All the ANICs, Hong Kong, Taiwan, Korea, Singapore, are commonly handicapped by high wages and a shortage of labour which have resulted in their current economic problems, notably in labour-intensive industries, while China and the countries of Indo-China possess a superabundance of labour derived mostly from liberalising their agricultural sectors. With the existing complementing labour markets, China has served as the main labour supplier to support its neighbouring ANICs' manufacturers in gaining competitiveness in related labour-intensive industries. This has resulted in the relocation of the ANICs' manufacturers to China. Even so, over the past few years, China has exported some of its excess labour abroad, some even through Korean enterprises.³⁰ According to information collected in April 1992, there were 4,000 migrant workers from Mainland China working in Japan, another 25,000 working in Hong Kong.³¹ In late June 1993, the number of Chinese working abroad hit 148,000.³² It is said that a great number of illegal emigrants from China have been

³⁰. *Beijing Review*, 36: 37, (September 13-19, 1993), p. 28.

³¹. *Far Eastern Economic Review*, (2 April, 1992), p. 21.

³². *Beijing Review*, 36: 33, (August 16-22, 1993), p. 29.

working in neighbouring countries, i.e. South Korea,³³ and Taiwan. As economic transactions are intensified in the CEA, the trend of exchanging personnel, workers, technicians, scientists, scholars, between China, Taiwan and Hong Kong, is set to rise rapidly. Over the last few decades, Taiwan has accumulated huge capital reserves from export earnings and from fast expanding trade with all major economies. Taiwan's manufacturing base for the Japanese, which led to a Japanese dominated "Japan-Taiwan-USA" trade relationship during the 1960s and 1970s, has been diluted. Foreign investment and exports of industrial production to other regional developing economies have shaped Taiwan's leading role in a new "Taiwan-China-USA" trade pattern.

TABLE 5.3. THE JAPAN-TAIWAN-USA PATTERN OF TRADE

Japan >	capital, technology, management, marketing
Taiwan >	OEM, labour-intensive manufacturing, GSP
USA >	export market

TABLE 5.4. THE TAIWAN-CHINA-USA PATTERN OF TRADE

Taiwan >	capital, technology, management
China >	OEM, labour-intensive manufacturing, GSP
USA >	export market

The story of Taiwan's industry moving to China for a manufacturing base is like Hong Kong's. On the one hand, it is seeking to cut production costs for increasing competitiveness against other competitors. On the other hand, it is seeking to share China's trade preferences - Most Favoured Nation (MFN), General System Preferences (GSP), and quotas - in the developed markets, in order to circumvent possible

³³. "Vanishing assets", *The Economist*, (20 November, 1993), pp. 86, 89.

protectionist obstacles. However, evidence has emerged of an American investigation of its trade deficit with China. Over the period of 1987 to 1991, the US trade deficit with China had increased sharply, while its trade deficit with Taiwan and Hong Kong had decreased (Table 5.5). This clearly implies a large scale transfer of manufacturing from Hong Kong and Taiwan to South China.³⁴ In other words, according to the Hong Kong government's own estimation, were the United States to revoke China's MFN status, "the territory would lose up to \$15.7 billion in overall trade, up to \$2 billion in income, and as many as 60,000 jobs."³⁵

TABLE 5.5. THE US TRADE DEFICIT WITH CHINA, TAIWAN, AND HONG KONG (\$ billion)

	1987	1988	1989	1990	1991
US with China	3.4	3.5	6.2	10.4	12.7
US with Taiwan	18.9	12.6	13.0	11.1	9.9
US with H K	6.5	4.6	3.5	2.7	1.1

Source: Department of Commerce, USA, 1992.

Above all, China's huge market potential is encouraging Taiwan's producers to take up Chinese brand names in international markets. The size of China's market is large enough to support Taiwan's industrial production in its attempts to establish its own reputation. For instance, the owner of Shin-Shing Shoes Co., Y. K. Chen, points out that with China's market prejudice in favour of shoes made in

³⁴. Harry Harding, "The US and Greater China", *The Chinese Business Review*, (May-June 1992), p. 22.

³⁵. Pamela Balinger, "The birth of Greater China", *The Chinese Business Review*, (May-June 1992), p. 14.

Taiwan he is sufficiently confident to establish his own brand name away from an OEM position.³⁶ The Chairman of the Fu-Ta Umbrella Co., T. F. Chen, also shares this view that "You can not allow your turnover to be decreased at the time of bringing a new brand name to the market. So, the only way forward here is to expand production and market share through manufacturing in China."³⁷ These developments suggest that with as yet untapped economic potential, further moves toward integration within the CEA seems likely.

5.1.2. Restructuring Industries And Strengthening Competitiveness Through Market Opportunities

In spite of the political hostility between Beijing and Taipei, the booming trade flow between China and Taiwan is prompting more economic cooperation (see Figure 5.1). While Taiwan and China are carrying out "indirect trade" mostly via Hong Kong, the British colony, which is to be returned to China in July 1997, has been tied into the network of Chinese "economic unification", whether intentionally or not. Hong Kong, with its geographic proximity to China, has long been an outlet for capital, know-how and technology for China's closed economy,³⁸ even in the turbulent Cultural Revolution era. Moreover, Hong Kong, an entrepot with outstanding financial expertise, a well-developed communications infrastructure and, in particular, proximity to China, serves foreign investors as a launch pad to China and Southeast Asia. Accordingly, the

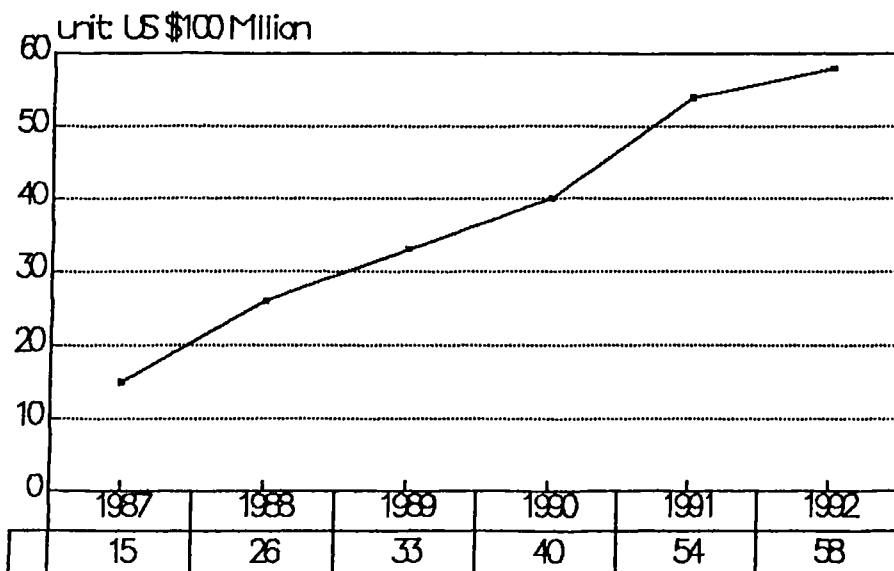
³⁶. *Central Daily News*, International Edition, (10 September, 1993), p. 8.

³⁷. "Taiwan R & D, Mainland Manufacturing", *Commonwealth*, (1 March, 1992), p. 40. Fu-Ta Umbrella Co. is now manufacturing in Taipei for more sophisticated upstream development and Xiamen for downstream lower price umbrellas.

³⁸. Hong Kong has been generally recognised as a financier, trading partner, middleman, facilitator, and investment centre for China. See John Burns, "Hong Kong in 1992: struggle for authority", *Asian Survey*, 33: 1, (January 1993), p. 29.

Hong Kong Government Trade Department summarises seven facts of importance to Hong Kong in relation to China: "Hong Kong and China are each other's No. 1 trading partner. China as a market for Hong Kong goods. China as a base for outward processing activities. Hong Kong is an important market for Chinese goods, an important entrepot for China, an important location for Chinese interests and the largest investor in China."³⁹

FIGURE 5.1 TAIWAN'S GROWING INDIRECT TRADE WITH CHINA



Source: International Trade Bureau, MOEA ROC, 1993, & Hong Kong Custom Statistics

The Japanese have been eyeing Hong Kong's economic links with China. More than a quarter of Japan's exports to China have been channelled through Hong Kong.⁴⁰ Hong Kong's ties to China's economic power house, Guangdong Province, is even more impressive, with the investment of US\$17 billion in the province, the control of 30,000 enterprises, and employment of

³⁹. For all details of figures collected by Hong Kong Government Trade Department see "China & Hong Kong: Some Important Facts", (May 1993).

⁴⁰. "Shogun wedding", *Far Eastern Economic Review*, (28 June, 1990), p. 70.

three million workers.⁴¹ Many foreign investors are using Hong Kong's stock market as a way into China, because "it has more listed companies than any other stock market in the world involved in China, the region's fastest growing economy."⁴² Above all, many Hong Kong companies with exposure to Chinese economy have been targets for investors, such as China Light & Power, Hong Kong Telecom, Hong Kong Electric, and HSBC Holdings. Even its business characteristics express its willingness and availability to be a bridge between China and the rest of the world. For instance, the Chairman of Wharf (Holdings) Ltd., Peter K. C. Woo, said that:

"[W]ith the continued integration of the economies of China and Hong Kong, Wharf intends to act as a bridge to develop business between its mainland Chinese partners and business associates from other parts of the world."⁴³

Since Beijing's 'open door' policy was announced in 1979, the first wave of Hong Kong investment, mainly led by small and medium enterprises, has poured into nearby Guangdong, and Fujien Provinces. Not only have Hong Kong businessmen swarmed to find manufacturing bases in China, but other investors, Japanese and American as well as Taiwanese at a later date, have been flocking there in search of low cost production. They have brought with them their management expertise and marketing experiences in lower level technology and labour-intensive industries which could hardly survive at home (where they were once called sunset industries). Examples are toys, textiles, umbrellas, consumer electronic components, dyeing, and foot wear.

⁴¹. See James Walsh, "The ties that bind", *Time*, (21 March, 1994), p. 35.

⁴². Simon Holberton and Patrick Harverson, "Foothold on cliff of opportunity", *Financial Times*, (9 November, 1993), p. 19.

⁴³. See Chairman's statement at 1992 Report, The Wharf (Holdings) Ltd.

Hong Kong's Advantages For China

As far as Hong Kong businessmen are concerned, booming Chinese investment means high profits, the survival of their sunset industries, and circumvention of American trade protection. According to analysts on the Hong Kong stock market, many companies have got more than one manufacturing base in China and normally could expect payback from investment in only two to three years.⁴⁴ One successful businessman, Patrick Wang, the managing director of Johnson Electric, one of the world's leading manufacturers in micro-motors, said that his investment in China had been paid back "many times over" and revealed that Johnson's post-tax return on investment had been 20 per cent over the last few years.⁴⁵ Many investors believe that these high profits have been gained largely from the effects of scale economies derived from China's huge market. In China, foreign investors are normally able to expand their businesses to a larger scale with a smaller amount of capital than in Hong Kong. Low cost production factors and the larger market tend to encourage producers to go for a larger volume of production in order to ensure a stable market share. For Hong Kong, China's prospect as a highly industrialised environment supports Hong Kong's continuing prosperity and more importantly future stability. For China, Hong Kong's business efforts are accelerating its progress towards industrialization in accordance with the emergence of a massive and booming economic grouping.

While China's "Open Door" policy accelerated its economic development, most of Hong Kong's industries were suffering the "NICs disease", namely soaring wage and rent costs, and, more

⁴⁴. *Hong Kong Economic Daily*, (in Chinese), (28 September, 1991).

⁴⁵. Simon Holberton, "China on a wing and a prayer", *Financial Times*, (7 July, 1993), p. 3.

seriously, a severe shortage of labour.⁴⁶ In terms of economic development, China's less developed economy has got plenty of land, almost limitless and cheap labour, but lacks capital, management and applied technology expertise for which Hong Kong is renowned. Both economies, therefore, have begun an unprecedented process of economic cooperation through an industrial division of labour and complementary economies to which:

"(Hong Kong entrepreneurs) brought their capital, their know-how, and their Western customers. Their motives were straightforward: the tiny British territory simply ran out of enough workers to make all the toys, cameras, clothing, and other labour-intensive products the West wanted to buy. When a low-cost labour pool became available across the border, they tapped it, slowly at first, then with growing enthusiasm."⁴⁷

Gradually, Hong Kong industrialists have moved production to China. Some listed companies in Hong Kong, producing stereos, televisions and accessories, computer hard disks, and toys, have completely relocated their operations in China.⁴⁸ As a result, the large amounts of capital that China has been longing for have flowed in. According to the Chinese Ministry of Foreign Trade and Economic Cooperation, foreign investment in China totaled US\$37 billion (utilised value) in the period of 1979-1992, and about \$21.2 billion was contributed by the biggest investment sources from Hong Kong and Macao.⁴⁹ In 1992 alone, Hong Kong's investment in China accounted for 68.3 per cent of China's total US\$11.3 billion utilised foreign direct

⁴⁶. In their arguments, two writers described the symptoms as the "NICs disease". See T. Aoki, and H. Ohashi, "Asia: integration of the world's most dynamic economies", *Tokyo Business Today*, (June 1992), p. 27.

⁴⁷. Ford S. Worthy, "Where capitalism thrives in China", *Fortune*, (9 March, 1992), p. 34.

⁴⁸. *Hong Kong Economic Daily*, (28 September, 1991).

⁴⁹. Simon Holberton, "China on a wing and a prayer", p. 3.

investment.⁵⁰ Up to early 1994, Hong Kong has accounted for 64 per cent of the US\$135 billion committed to China ventures since 1979.⁵¹ Hong Kong investment in industrial manufacturing in China alone accounted for about a quarter of HK\$100 billion by 1993.⁵² It was this investment as an accelerator of industrialization that made Southern China and Hong Kong become a borderless economic area. One economic survey stated that:

"The most striking element of the Dengist reforms is their extraordinary dependence on foreign trade and foreign investment as engines of development."⁵³

The part China plays in this economic interdependence is as a manufacturing base with its plentiful cheap labour and land, whilst Hong Kong is supplying management, marketing, technology, and, above all else, capital and finance. In addition, although China's preferential trading status is subject to political quarrels with the US over human rights performance,⁵⁴ its enjoyment of the GSP and the MFN persuades manufacturers from Hong Kong and Taiwan to shelter in China, e.g. using China's export quotas in the case of textiles and garments.⁵⁵ Previous sunset industries of Taiwan and Hong Kong,

⁵⁰. The same year, Taiwan accounted for 9.3 per cent, Japan for 6.6 per cent, the US for 4.6 per cent, and European Union for 2.2 per cent. See also *Financial Times*, (7 July, 1993), p. 3; *Financial Times*, (5 August, 1993), p. 15; *The Economist*, (16 April, 1994), p. 103.

⁵¹. James Walsh, "The ties that bind", p. 35; Hong Kong and Macao account for US\$147.27 billion out of \$216.91 billion all contracted investment in China. See *Financial Times*, (20 May, 1994), p. 7.

⁵². The information based on Credit Lyonnais Securities. See Simon Davies, "Hong Kong investors warm to mainland cooling", *Financial Times*, (2 September, 1993), p. 4.

⁵³. "A driving force", *The Economist Year Book 1993 edition*, p. 155.

⁵⁴. For recent rounds of Sino-American row and the division within the Clinton administration over the issue linking annual renewal of the MFN and human rights, see Susumu Awanohara, "Washington's ire", *Far Eastern Economic Review*, (20 January, 1994), pp.56-57; Carl Goldstein, "Moving forward", *Far Eastern Economic Review*, (3 February, 1994), pp. 51-52; Susumu Awanohara, "Collision course", *Far Eastern Economic Review*, (3 February, 1994), pp. 18-20; and "China: can he save face?", *Business Week*, (18 April, 1994), p. 14-15.

⁵⁵. Economic and Social Commission for Asia and Pacific, United Nations, *Economic and Social Survey of Asia and the Pacific 1992*, (1993), p. 64.

most notably dyeing, umbrellas, foot wear, electronics, have been revived in this way and are becoming stronger and more competitive. Subsequently, bigger firms have followed suit, which have brought about a further wave of investment. More recently, with a more promising policy announced for preferential access to markets and profits, the Chinese authorities have been favouring foreign direct investment in infrastructure. This sort of investment symbolises business confidence betting on China's economic future, e.g. Hopewell's superhighway project, and Wharf's power station and road,⁵⁶ as well as Hutchison Whampoa's US\$1.1 billion container terminal project for Shanghai.⁵⁷

Hong Kong accounts for over 80 per cent of the foreign investment and foreign trade in Pearl River Delta, the most prosperous part of Guangdong,⁵⁸ and is the biggest investor in China as a whole, though some uncalculated investment flows have been originally redirected from China itself via Hong Kong agents back to China.⁵⁹ In return, Chinese firms, which are at the moment the leading investors in Hong Kong, mostly from Guangdong, have invested in various sectors, mainly in tertiary industries, real estate and financial services. Mainland Chinese investment in Hong Kong was up from US\$12 billion in 1991, and \$15 billion in 1992, to \$18 billion in 1993 (figures show only the first six months of 1993). Moreover, Chinese "hot money" flows deposited in Hong Kong

⁵⁶. Ian Hargreaves, and Simon Holberton, "Hong Kong's one for the road", *Financial Times*, (28 September, 1993), p. 19; for a list of investment of infrastructure see *Shin Pao* (Hong Kong Economic Journal), (16 December, 1992.) .

⁵⁷. Carl Goldstein "Stranglehold lessens", *Far Eastern Economic Review*, (15 October, 1992), p. 60.

⁵⁸. See Ford Worthy, "Where capitalism thrives in China", *Fortune*, (9 March, 1992), p. 35.

⁵⁹. According to the declarations of China's State Council, "Provisions for the Encouragement of Foreign Investment" 1986, and "Provisions for the Encouragement of Investment By Taiwan Compatriots" 1988, special privileges have been given to Hong Kong and Taiwan investors. Some Chinese companies redirect their returns through agents outside China to be seen as foreign investment in order to take tax free advantage. See Michael S. Serrill, "Money mad", *Time*, (12 July, 1993), p. 38.

banks were also up from US\$4 billion in 1990 to near \$10 billion in the first quarter of 1993.⁶⁰ In the first half of 1992, Chinese firms bought property worth about US\$ 6.6 billion. Brokers estimated that they will be able to own 20 per cent of all property in Hong Kong by 1997.⁶¹ For many people in Hong Kong and Taiwan, it is nothing but a show of Chinese determination to take over Hong Kong and an early intention to dominate the capitalist society after it has been taken over. Indeed, China's pouring more than US\$ 10 billion into Hong Kong in the last few years is regarded as not only a procedure to take over the British colony smoothly, but also a political profile to convince the Hong Kong business community of its persistence in capitalism.⁶²

One of the "spillover" effects with which theoretical integration is concerned is the rise of industrial integration. Not only has industrial integration here created frequent interaction networks, but also it has brought about exchanges of employment in the labour markets. In other words, simple economic cooperation has been encroaching into society. About a decade ago, manufacturers in Hong Kong employed about 900,000 workers in the colony and none in Guangdong. Now, "their Hong Kong payroll is down to about 700,000. But they have employed three million workers at some 30,000 factories in Guangdong."⁶³ What one can see through this close relationship, without casting any doubt on progressive integration, is its economic potential and the deepening and widening trend in the division of labour. As China and Hong Kong today have become each other's largest investment

⁶⁰. Both investment and deposit figures were based on *Time* graphic. Ibid.

⁶¹. *Far Eastern Economic Review*, (23 July, 1992), p. 49.

⁶². Louis Kraar, "A new China without borders", *Fortune*, (5 October, 1992), p. 41.

⁶³. James Walsh, "The ties that bind", p. 35.

destination, economically each one is already "inextricably linked" to the other.⁶⁴

Taiwanese Industrial Investment In China Via Hong Kong

In 1987, the Nationalist government in Taiwan liberalised the policy limiting contact with China, which since then has resulted in a full range of economic transactions. Because of the ongoing political stalemate between Taiwan and China, businessmen on both sides of the Taiwan Strait have had to trade with each other via a third party. As the "two way" trade and investment flows have amplified, Hong Kong has become the third party for this indirect trade. Since most of Taiwan's trade with and investment in China are directed through Hong Kong, recently there have been more Taiwanese investments flowing into Hong Kong itself.⁶⁵ There are two reasons. Firstly, under the existing political impasse Taipei only allows its business flows through Hong Kong to ensure flexibility in policy, to provide bargaining chips with China, and to prevent its economy from being too dependent on China.⁶⁶ Secondly, as the actual need grows in the Taiwanese business community for trade with China, Taiwanese small and medium enterprises, in turn, have set up branches or connections with local agents in Hong Kong to conduct business in China. Most recently, even big firms have followed suit. Walsin Lihwa Co., one of the leading cable & wire manufacturers in Taiwan, for example, has acquired a 64.2 per cent interest in the publicly listed Success Holdings in Hong Kong. The purpose of such

⁶⁴. Louis Kraar, "A new China without borders", p. 41.

⁶⁵. According to the information of Majestic Trading Company Ltd., Taiwan's Ministry of Economic Affairs representative in London, Taiwanese recent investments in HK are especially in trade, property, hotel, shipping, financial services and Hong Kong stock and futures markets. Refer to 1993 Annual Report of Majestic Trading Company Ltd., (April 1993).

⁶⁶. "Mainland fever is there to stay", *Business week*, (3 May, 1993), p. 20.

acquisition was, due to the booming China market, to use Hong Kong as a base for further overseas investment in China and the rest of the Asian region.⁶⁷

Local businessmen believe that without any Taiwanese banking presence in Hong Kong to support the investment in China, there has to be an individual financial management office in Hong Kong in order to manage the capital flow into and out of China.⁶⁸ It is also necessary to set up in Hong Kong to comply with Taipei's policy of no direct links with China. Growing trade between China and Taiwan has lured Taiwanese businessmen to set up about three thousand intermediary companies in Hong Kong in the past five years.⁶⁹ Amongst them, there are over two thousand companies focusing on trade.⁷⁰

TABLE 5.6. TAIWANESE INVESTMENT IN CHINA

Year	Agreed Projects	Agreed Capital(US\$ Mil.)
1983-87	80	190
1988	435	520
1989	552	437
1990	1,011	892
1991	1,737	1,391
1992	6,430	5,540
Total	10,245	8,970

Source: Annual Report of Majestic Trading Co. Ltd., 1993. based on Hong Kong newspaper *Ta Kun Pao* and an estimation.

Since Taiwan officially bans direct Taiwanese investment in China, there has been a great deal of "illegal" investment conducted through various channels without official

⁶⁷. Information quoted directly from Walsin Lihwa Corporation 1992 Annual Report.

⁶⁸. Information taken from interviewing Taiwanese businessman over the period of July and August, 1993, in Taipei. Y. L. Wang, deputy-manager of Chuanshyh Garment Co., Ltd., pointed out that an office in Hong Kong under whatever trade name is crucial for investors to get money inflow from Taiwan and outflow to China. However, its most important job is to link to Hong Kong's financial service channels to make sure that their payback on investment can be safely steered out of China. (10 August, 1993).

⁶⁹. *Commercial Times* (Kun Shang Shi Bao), (21 May, 1993).

⁷⁰. See *The Independent Weekly Post* (Chi Li Chou Bao), (25 March, 1994).

permission. In spite of the restrictions of official policy , there has been little sign that investment flows have been slowing down (Table 5.6). Due to recognition of the important role of Taiwanese investment in China, three of Taiwan's state-owned commercial banks, Chang-Hua, the First, and Hua-Nan, set up representatives in Hong Kong in 1992. Since September 1993, Hua-Nan Commercial Bank has been operating its first Hong Kong branch which is starting to assist Taiwan's investors with financial management services.⁷¹ Up to May 1994, altogether seven Taiwanese banks have established their operations in Hong Kong, mainly providing financial services for Taiwanese businessmen and investors.⁷² Further financial integration programmes should be brought into being soon. As many of the bank's customers have already invested in China, particularly in labour-intensive industries, Taipei-based private China Trust Commercial Bank, one of Taiwan's top ten banks, opened its representative office in Hong Kong in November 1993 to be able to serve its customers well and establish links with its counterparts on the mainland. Its new chief representative, Vance Chin, states that "Closer relations with banks from both sides (China and Taiwan) is ultimately unavoidable."⁷³

Since 1987, Taiwan has been rapidly increasing its trade with China through Hong Kong. This booming trade relationship is reflected in economic indicators. Among Taiwan's exports to Hong Kong are almost around 40 per cent of the exports destined to China in the years recorded (See Table 5.7, also

⁷¹. *Central Daily News*, International Edition, (24 September, 1993).

⁷². Hua-Nan and the First Commercial Banks and Bank of Taiwan have branches in Hong Kong. Chang Hwa Commercial Bank is to follow suit soon. The Medium Business Bank of Taiwan, China-Trust Commercial Bank and Taipei Business Bank have also set up Hong Kong offices. See *Central Daily News*, International Edition, (24 May, 1994).

⁷³. Henry Sender, "China Beachhead", *Far Eastern Economic Review*, (2 December, 1993), pp. 81-82.

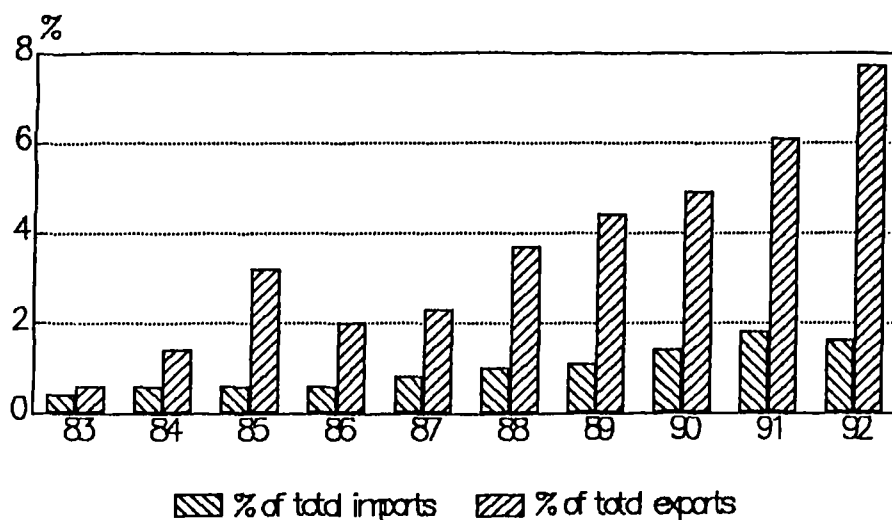
refer to Figures 5.2, 5.3). Whilst in the past few years, Taiwan's trade surplus with the US has been reduced following pressure to diversify export markets, Taiwan has increased its

TABLE 5.7. TRADE BETWEEN TAIWAN AND HONG KONG, AND TAIWAN'S SHARE OF HONG KONG RE-EXPORTS TO AND FROM CHINA (unit: \$ million)

YEAR	EXPORT TO HK			IMPORT FROM HK		
	amount	% re-export to China		amount	% import from China	
		amount	% export to HK		amount	% import from HK
1987	4,118	1,226.5	29.8	754	288.94	38.3
1988	5,580	2,242.2	40.2	1,922	478.69	24.9
1989	7,303	2,869.5	41.2	2,205	586.9	26.6
1990	8,556	3,278.3	38.3	1,446	765.36	52.9
1991	12,430	4,667.2	37.5	1,944	1126.0	57.9
1992	15,416	6,287.9	40.8	1,781	1119.0	62.8

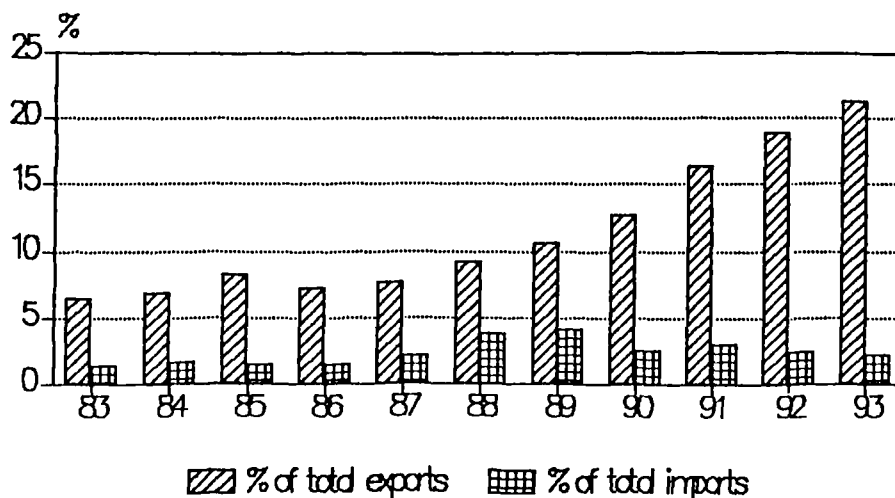
Source: International Trade Bureau, Ministry of Economic Affairs, R. O. C., based on HK Custom Statistics, 1993.

FIGURE 5.2 Taiwan's Trade with China as a Percentage of Its Total Exports and Imports



Source: ROC Custom Statistics, 1993

FIGURE 5.3 Taiwan's Trade with H K as a Percentage of Taiwan's Total Exports and Imports



Note: 1993 covers only Jan. to June.
Source: ROC Custom Statistics, 1993

trade surplus with Hong Kong and China. In 1990, Taiwan's trade surplus with China accounted for 20.11 per cent of its global trade surplus, and with Hong Kong 56.90 per cent. In 1992, the trade surplus with China reached 54.53 per cent, and with Hong Kong 143.8 per cent of its global surplus.⁷⁴

TABLE 5.8. HONG KONG RE-EXPORTS TO ITS MAJOR ASIAN TRADING PARTNERS (share of the total in %)

Destination	1989	1990	1991	1992
China	29.9	26.8	28.7	30.7
Japan	6.4	5.9	5.5	5.4
Taiwan	4.8	5.1	4.6	3.8

Source: *Hong Kong 1992 and Hong Kong 1993*, HK Government.

Moreover, Hong Kong's re-exports to China and Taiwan account for over one-third of its total re-exports. Hong

⁷⁴. Information is based on International Trade Bureau, Ministry of Economic Affairs, R. O. C. See *Liang Ann Ging Gih Tong Gih Yueh Bao*, (Economic Statistics Monthly for Two Sides of the Strait), Mainland Affairs Council, The Executive Yuan, (June 1993).

Kong's 'middleman' position for the "two Chinas" is crucial.⁷⁵ From the perspective of trade development, China, Taiwan and Hong Kong have already become very important partners, a trend likely to be increased in the future. Although trade relationships do form transaction networks between partners, this alone is not a sufficient condition for economic integration. Above all, Taiwan, Hong Kong, and China, to a lesser extent, have established outward-looking economies which have directly resulted in their successful economic development. Their continuation of trading with the rest of the world remains as crucial as their intra-regional trade.

When the world was twice hit by the raised high prices of oil and economic recession in the early 1980s, the rise of protectionism in developed economies threatened international trade. It was these changes of the economic situation worldwide that intensified international competition and, thus, drove trade partners to seek industrial strength together through closer cooperation. The formation of the CEA has been accelerated by increasing intra-regional trade flows, foreign investment, and, above all, the industrial division of labour from which mutual complementary economies have stemmed.⁷⁶ The ratio of the intra-industry trade between China and Taiwan to Taiwan's total commodity trade in manufacturing sectors rose from 5.53 per cent in 1985 to 28.78 per cent in 1991, and non-manufacturing sectors rose from 28.18 per cent to 56.54 per cent in the same period. In 1991, the horizontal division of labour accounted for 75.42 per cent of total Taiwanese investment in China and Hong Kong, and for about 18.49 per cent in the vertical division of labour.

⁷⁵. Refer to footnote 32. John Burns, "Hong Kong in 1992: struggle for authority", *Asian Survey*, 33: 1, (January 1993), p. 29.

⁷⁶. Penelope Hartland-Thunberg, *China, Hong Kong, Taiwan and the World Trading System*, (London: Macmillan, 1990), pp. 97-98.

According to some empirical surveys, Taiwanese businessmen investing in China procured 80 per cent of the materials, components and equipment they needed for operation from Taiwan; and only about 15 per cent from Chinese local industries.⁷⁷ Among others, footwear, umbrellas, toy manufacturers, accounted for 90 per cent of their procurement from Taiwan; those industries for plastic, electronics, and vehicles were amongst the highest procuring from China for their local operations (about 20 per cent).⁷⁸ Like Hong Kong, Taiwan, since the early 1980s, has also suffered the "NICs' diseases", which in manufacturing sectors have turned out to be serious. Because the history of Taiwan's economic development has been based more on the growth of labour-intensive manufacturing industries, growing wages, soaring land prices, and a shortage of labour have hit related industries very hard, resulting in the exodus of its indigenous industry to South East Asia and China.

For general manufacturers in Taiwan, their export-orientation is largely shaped by the changing trends of international markets. Therefore, for the sake of keeping competitiveness, production factors are always cost sensitive. Cutting production costs has been the ANICs competitive strategy for some time. Unfortunately, since the mid-1980s, due to Taiwan's huge trade surplus against the US, the New Taiwan Dollar has been under American pressure, dramatically appreciating against the US Dollar from NT\$ 40.32 in 1983 to NT\$ 25.40 in 1992. This brought about a crisis for Taiwanese exporters, although the appreciation occurred over a relative

⁷⁷. Economists normally investigate industrial complementarity between China and Taiwan by studying intra-industry trade, division of labour, components procurement, and semi-finished products. All figures above have shown rapid increase throughout the period examined (1985-1991). *Economic Yearbook for The Two Sides of the Taiwan Strait, 1992*, (Taipei: Chung-Hua Institution for Economic Research, May 1993), pp. 84-89.

⁷⁸. *Ibid.*, p. 87.

long period. In terms of price, Taiwanese competitiveness was fading away. Furthermore, Taipei's government in the mid-1980s introduced a "Labour Standards Law" to legitimise labour's fundamental rights which frustrated most employers.⁷⁹ In a public letter to the government, Wang Yeung-Ching, Taiwan's leading industrialist, Chairman of Formosa Plastics Co., warned that the law had not only increased business costs, but also changed the diligent habit of labour on which Taiwan's economic development had relied.⁸⁰ Wage rates rose and the trades union movement became active as a result.

The cost of labour in Taiwan's manufacturing sectors rose more than 60 percent in US dollars between 1986 and 1988.⁸¹ Employers were desperate, because they were facing diminished profit margins or even bankruptcy. Moreover, as the environmental protection movement became active during the 1980s, more restrictive environment protection standards were introduced.⁸² For example, due to serious industrial pollution, Wus Printed Circuit Co. Ltd., ranked as the 48th biggest electronic company in the country,⁸³ was coerced into stopping production for one month by the Taiwanese Environmental Protection Administration in 1992, which the company's chairman L. K. Wu confirmed was the biggest push for the company to relocate in Kuenshang, near Shanghai.⁸⁴

⁷⁹. In an interview to Mr. Thomas Huang, Chairman of Taiwan Sweater Industry Association, he complains that it was this particular law which drove off many businesses in the past few years. The interview has undertaken in Taipei, on 23 July, 1993.

⁸⁰. Wang Yeung-Ching's "Ten thousand words" letter was widely regarded as a strong voice from industrialists to warn the government policy. See *Central Daily News*, International Edition, (22 February, 1993), p. 3.

⁸¹. Chi Schive, "The emerging role of Taiwan in the rising Asian-Pacific Regionalism", *Industry of Free China*, (May 1993), p. 33.

⁸². Tzong-Shian Yu, "A Quick Adjustment of Taiwan to an Enhanced Economic position in the World", Occasional Paper, No. 9205, Chung-Hua Institution For Economic Research, Taipei, (August 1992), p. 6.

⁸³. See special survey for the biggest 1000 manufacturers in Taiwan on *Commonwealth*, (5 June, 1993).

⁸⁴. C. Y. Tian, "Nan Dian Zai Kuenshang Zao Hwei Tsung Tien", (Wus Printed Circuit Co. Ltd. finds its Spring in Kuenshang), *Business Weekly*, (28 June, 1993), p. 36.

TABLE 5.9. A COMPARISON OF THE AVERAGE FOREIGN EXCHANGE RATES OF CHINA, TAIWAN, AND HONG KONG (National Currency Per U S Dollar)

YEAR	RMB	NTD	HKD
1983	1.98	40.32	7.27
1984	2.80	39.52	7.82
1986	3.72	35.55	7.79
1988	3.72	28.17	7.78
1989	3.76	26.17	7.82
1990	4.72	27.10	7.79
1991	5.32	25.74	7.76
1992	5.74	25.40	7.73

Source: 1. The Central Bank of China, R.O.C., April, 1993.
2. *Ta Kun Pao*, (Hong Kong),

As the Taiwanese currency appreciated in value (refer to Table 5.9), "hot money" flows released from sunset industries circulating around the country were immediately directed to an illegal gambling lottery, and later into the stock market and real estate.⁸⁵ Consequently, owing to property speculators, there were less available land for industrial expansion and soaring property prices which halted private investors' programmes. Taiwan's industrial tycoon, Wang Yeung-Ching, for example, was even bidding for a US\$7 billion comprehensive industrial zone first in Fujien Province's Xiamen special economic zone for his 6th naphtha cracker, later in Yangtze River in 1992, which was then banned by the Taipei government for fear of taking away about one third of Taiwan's industrial base to China.⁸⁶ Part of the reason for Wang's China bid derived from his failing to find a suitable site to expand his business in Taiwan.

⁸⁵. In detail, see Tzong-Shian Yu, "A Quick Adjustment of Taiwan to an Enhanced Economic position in the World", Section II, Financial "High Fever".

⁸⁶. Wang's China projects started in 1989. The very first project in Xiamen was postponed, due to Taipei authority's objections. Wang and Beijing ended up with no agreement. See *Global Views*, (15 December, 1992), pp.46-47; Julian Baum, "Taking the plunge: Formosa Plastics confirms huge petrochemicals plan", *Far Eastern Economic Review*, (22 April, 1992), p. 75; another ambitious investment plan in China by the Cathay Insurance and Construction Group, the largest in these businesses in Taiwan, was blocked. see Carl Goldstein, "The bottom line: Taiwan capital, factories pour into China", *Far Eastern Economic Review*, (17 September, 1992), p. 23..

All in all, these changing economic factors have boosted production costs higher than ever. Mr. G. C. Liao, Chairman of Chen-Chou Enterprise Ltd., argued that following the fast speed of urbanization, nowadays fewer and fewer employees wish to work in a traditional factory.⁸⁷ Similarly, Mr. L. L. Liao, Chairman of Merry Electronic Co. Ltd., told the same story that the reason why he located in China was not because of the lower social costs, but because of the serious shortage of labour.⁸⁸ (Refer to Appendix F-5.1, Employment by industry in Taiwan.) Even the world's leading bicycle maker, Giant Machinery Co., has suffered a labour shortage in its most significant manufacturing site in Taiwan.⁸⁹ In Taiwan, too frequent hiring and firing of workers in manufacturing industries has resulted in instability in production procedures and quality. Even foreign buyers have urged their Taiwanese sub-contractors to move to China in order to maintain the quantity and quality of their production.⁹⁰ For most profitable labour-intensive industries in Taiwan, their Achilles heel is the shortage of labour. These disadvantageous factors for Taiwanese industry over time appear to be incentives, if not positive advantages, for the formation of the CEA. To begin with, Taiwan's currency appreciation raised its buying power overseas, and therefore brought about a foreign investment stimulus. The climate for domestic investment has deteriorated, which has led to complaints by industrialists and demands for remedial action.

⁸⁷. *Commonwealth*, (1 March, 1992), p. 32.

⁸⁸. Mei-Lui specialises in producing inter-phones and microphones. *Commonwealth*, (1 March, 1992), pp. 22, 40.

⁸⁹. Its Manufacturing site in Taiwan was at the time the largest in the world. *Global Views*, (15 December, 1992), p. 42.

⁹⁰. The most obvious case here is the footwear industry. For instance, the American firm, Nike, guarantees some regular orders for Taiwanese partners to manufacture in China. In return, Taiwanese suppliers to Nike brought their management teams to China. See *Far Eastern Economic Review*, (17 September, 1992), p. 24.

In 1992, a survey of the one thousand biggest Taiwanese companies showed industrialists' concerns about future industrial development.⁹¹ Most industrialists are frustrated by their operating costs in Taiwan and if they are ever to choose a foreign destination for their industrial expansion, most of them will place China at the top of the list. (Refer to Appendix F-5.2.) In 1993, another survey, on the trends of foreign direct investment of companies listed on the stock market conducted by *Business Weekly* in Taipei, confirmed that 58.8 per cent of all Taiwanese companies thought that China was likely to be the most favourable destination for investment.⁹² (Refer also to Appendix F-5.3.) While labour-intensive manufacturers have been driven out of the country, some of them have immediately found a more favourable climate for manufacturing in China. Some have even closed all their businesses in Taiwan, but most of the others maintained their headquarters in Taiwan from where they manage capital flows, overseas orders, marketing, R & D, assembly and transportation.

Only manufacturing operations are conducted from their Chinese base. Entrepreneurs have suggested that, by early 1992, at least 80 per cent of companies in footwear, briefcase, toy, and umbrella industries, had been seeking relocation in mainland China.⁹³ Taipei's Ministry of Finance's calculations show that Taiwan's footwear manufacturers have nearly all relocated in China, and about 80 per cent of the

⁹¹. The survey which focused on business confidence in the CEO of the one thousand biggest manufacturers was conducted by Commonwealth Magazine Co. The result was published in *Commonwealth*, (1 March, 1992).

⁹². "Ch'u Taiwan Hou Chi Yieh Wan Na Li Chü?", (Where are enterprises to go, after leaving Taiwan?), *Business Weekly*, (24 May, 1993). The survey sampling 242 companies on the stock market on their FDI trend was trying to analyze the possible influence on Taiwan industrial structure as a whole.

⁹³. *Commonwealth*, (1 March, 1992), p. 16.

textile industry has also re-set up in China.⁹⁴ Although the Taipei government fears that these capital investments in China could hollow out Taiwan's industrial basis and result in economic dependence on China,⁹⁵ Chao Yao Tung, former minister of Economic Affairs, pointed out that almost all Taiwanese companies relocating in China have been importing materials and machinery from Taiwan and depending upon Taiwan's headquarters for commercial R & D.⁹⁶ In other words, these developments, from a positive point of view, are creating industrial division of labour within the CEA. Perhaps, the relocation of Taiwan's clock & watch industry serves as a typical example of the division of labour across the CEA: production in China, design and marketing in Taiwan, and finance and exportation in Hong Kong.⁹⁷

The result of an earlier survey suggested that by 1992 most Taiwanese investment in China would derive from labour-intensive industries delivering lower level technology and used equipment, and by taking advantage of low cost production factors in China. Nevertheless, more recent investment flows tend to be targeting China's domestic market instead of export markets. This recent survey clearly demonstrates a changing trend of investment for upgrading the industrial division of labour in terms of target markets and technology involved, e.g. recent investment by President Foods and Giant Manufacturing.⁹⁸ President Foods, already number one in Taiwan's food industry, whose investment is mainly concerned

⁹⁴ L. C. Wang, "A decade's retrospection on Taiwanese businessmen's China investment", *Management Magazine*, 218, (August 1992), p. 101.

⁹⁵ See Luisetta Mudie, "Fleeing investors shake Taiwan", *Financial Times*, 28 August, 1992), p. 3. About the government's worry see K. L. Kao, "Trade and investment across the Taiwan Straits maintaining competitive advantage, pursuing complementarity", Mainland Affairs Council, The Executive Yuan, R. O. C., 1993, pp. 11-13.

⁹⁶ L. C. Wang, "A decade's retrospection on Taiwanese businessmen's China investment", p. 101.

⁹⁷ See *The Independent Weekly Post* (Chi Li Chou Bao), (25 March, 1994).

⁹⁸ Carl Goldstein, "The bottom line: Taiwan capital, factories pour into China", p. 24.

with scale economies in China, has been building up a business network equipped with its advanced food processing technology to access the market. According to its Chairman, C. Y. Kao, the huge Chinese domestic market is propping up its long term strategy of internationalisation. Through its market share expansion in China, in 25 years President Foods could become the world number one.⁹⁹

Giant Manufacturing, which has already become the world's leading manufacturer of bicycles, is also seeking to maintain its superiority through market segments between Taiwan's higher value added products and China's middle and lower value added products.¹⁰⁰ In the short term, China provides a base for industrial revival for labour intensive industries and an important market from which Taiwan earns its trade surplus. An anonymous electrical company owner pointed out that: "We were lucky enough to have China's market absorbing Taiwanese manufactures and products, otherwise it is very likely that many Taiwanese companies could be out of business by now."¹⁰¹ Officials confessed that even if there was not an open Chinese market, the Taiwan economy, in the face of the worldwide recession in the early 1990s, would inevitably depart from its previous high growth track.¹⁰²

5.1.3. Overseas Chinese "Nostalgic Investment" In China

For decades, overseas Chinese have played an important part in Chinese modernisation by inputting capital, management

⁹⁹. *Global Views*, (15 December, 1992), p. 40.

¹⁰⁰. *Global Views*, (15 December, 1992), p. 42.

¹⁰¹. *Commonwealth*, (1 March, 1992), p. 32.

¹⁰². Koong-Lian Kao, *Trade and Investment Across the Taiwan Straits Maintaining Competitive advantage, Pursuing Complementarity*, Mainland Affairs Council, The Executive Yuan, R. O. C., 1993.

skills, and technology. Many overseas Chinese have been concerned to invest in places where their ancestors came from.¹⁰³ The reasons for that were based not only on the business consideration of profits, but also on the ties of kinship on which most overseas Chinese entrepreneurs rely for developing their business across national borders. Overseas Chinese investment from Southeast Asia was mostly in accordance with their previous emigrant routes back to Southern China. These investments therefore carry a message both of a simple economic incentive and of a nostalgia for home. One empirical survey suggests that "while nostalgia for the motherland has played its part, their main motive for home is profit."¹⁰⁴

With overseas Chinese heading for home, the worldwide web of their business has become a catalyst for the formation of the CEA. Nowadays, not only have many Taiwanese and Hong Kong businessmen made China the focus of their business growth for the next decade, but also many overseas Chinese businessmen, particularly, from Southeast Asia have followed suit. In spite of the early investment from Taiwan and Hong Kong seeking for low cost production factors and thus, for quick profits, more recently businessmen from both economies have engaged themselves in longer term projects for China's economic development, because of China's commitment to reforms, and increasing higher profile of the idea of the CEA.

It was the unprecedentedly large number of overseas Chinese investing in China from Southeast Asia, joining forces with Taiwanese and Hong Kong businessmen, that has brought

¹⁰³.Chinese belief of "Lo yeh guei ken" (As a leaf is for the root, so a person is for his homeland.) keeps driving overseas Chinese home.

¹⁰⁴."SE Asian Chinese head for home", *Asian Business*, 29: 4, (April 1993), p. 25.

about the preliminary condition of forming the CEA.¹⁰⁵ Analysing their investment strategies, which are characterised by five main factors, one can dig up the recent trend of developing the CEA as follows:

"1. They are motivated less by China's cheap labour costs and plentiful land and more by the country's latent consumer demand. 2. They are helping to modernise China's primary industries and build up its infrastructure. 3. They are bringing to China the management skills they have successfully used in ASEAN to apply sophisticated Western technology in an underdeveloped environment. 4. They are advancing into places often ignored by other foreign investors. 5. Cash-rich and debt-free, they are committing long-term investment to China."¹⁰⁶

Doing business in China today, businessmen realise that the first priority has not been seeking a good contract, but a good "guan si" (personal relationship) in the society. Because the modern legal systems of Western countries have not yet taken root in mainland Chinese society, most foreign businessmen there complain about corruption, bureaucratic inefficiency, and lack of regulations to follow. This unhealthy business environment, to some extent, allows informal, private, and even underground business activities to play a major part.¹⁰⁷ It does not mean, though, that shortcomings of the Chinese economic system, in terms of the western developed market economies, is to be a necessary condition of overseas Chinese investment. Since an element of Dengist reforms has been heavily dependent upon foreign trade and foreign investment, China's persistent market opening and

¹⁰⁵. Many scholars agreed with overseas Chinese entrepreneurs helping to establish the CEA in Beijing's Conference of "Mainland, Taiwan, and Hong Kong Economic Cooperation Trend" in 9-10 September, 1993. See special report in *Central Daily News*, International Edition, (11 September, 1993).

¹⁰⁶. "SE Asian Chinese head for home", *Asian Business*, 29: 4, (April 1993), pp. 24-25.

¹⁰⁷. Many Taiwanese businessmen interviewed in August 1993 commonly recognised that successful "guan si" means a successful start for business.

economic potential have served as economic incentives to lure foreign investment. Maybe coincidentally, for many generations "Chinese entrepreneurs have been operating in a network of family and clan".¹⁰⁸ Their businesses in China and elsewhere have been set up by means of family links, either by joint ventures, or partnerships. For example, overseas Chinese tycoons have favoured this linkage: Liem Sioe Liong, the leading Indonesian entrepreneur, who came originally from Fujien Province, has recently developed his businesses in Fuzhou (Fujian), and Mei Zhou Island (Fujian) in cooperation with Fuzhou Municipality, and Taiwan investors respectively.¹⁰⁹ In the case of investing in China, dialect, kinship, a common origin in a clan, a village or a county, have provided a certain assurance for overseas Chinese business.¹¹⁰ For example, S. Y. Tan, President of Kao-Lo Foods Co. in Taiwan, who left mainland China in the late 1940s, recalled that his business in China began by cooperation with Yuo-Li Trading Co., one of China's special trading bodies established for linking Taiwanese, through the introduction of a friend from high school in the mainland.¹¹¹

Unlike Japanese *Keiretsu* (industrial groups anchored by major banks), the network of Chinese entrepreneurs is characterised by its diversity and yet potential open system: "it represents access to local resources like information, business connection, raw materials, low labour costs, and different business practices in a variety of environments."¹¹² It can be seen that in access to China's market, in general,

¹⁰⁸ John Kao, "The worldwide web of Chinese business", *Harvard Business Review*, (March-April 1993), p. 24.

¹⁰⁹ See *Asian Business*, 29: 4, (April 1993), pp. 26-27.

¹¹⁰ *The Economist Yearbook*, 1993 Edition, p. 154.

¹¹¹ *Business Weekly*, 182, (19 May, 1991), pp. 33-35.

¹¹² John Kao, "The world wide web of Chinese business", *Harvard Business Review*, (March-April 1993), p. 24.

the Japanese have not been as successful as overseas Chinese enterprises. For example, in 1991, amongst 13,086 of China's total proven foreign investment venture projects, Hong Kong and Macao signed 8,879 projects, and Taiwan signed 1,735 projects. Japan had 607 projects.¹¹³ While overseas Chinese have taken advantage of China's economic development by expanding their businesses widely from coastal areas and riversides into the hinterland, all Western and Japanese firms can do is watch enviously, and struggle "to keep up with the overseas Chinese".¹¹⁴

The overseas Chinese today, including people in Taiwan and Hong Kong, account for 55 million around the world, and have continuously projected their economic dynamics across continents. One analyst even describes Chinese business networks as the "Chinese commonwealth".¹¹⁵ Whatever names have been used, the global network of the Chinese business community happens to be a "loose common market system" based not on geography but on a common culture. China's quickly growing economy has shown that, on the one hand, China has greatly profited from the resources contributed from these networks; on the other hand, pooling resources to China, overseas Chinese entrepreneurs have extended industrial cooperation with other overseas Chinese and mainland Chinese entrepreneurs. Therefore, China's persistent reforms have brought about a large scale of cooperation between overseas Chinese entrepreneurs, from which the CEA has stemmed. The effect of the Chinese entrepreneurs' jamboree in China has boosted the reality of bringing the CEA into being.

¹¹³. *Economic Yearbook for The Two Sides of the Taiwan Strait, 1992*, p. 533 (Appendix table 37).

¹¹⁴. "China's diaspora turns homeward", *The Economist*, (27 November, 1993), p. 79.

¹¹⁵. John Kao defines that this commonwealth is not based on one country or continent, but a network of entrepreneurial relationships. See his article "The worldwide web of Chinese business", *Harvard Business Review*, (March-April 1993).

5.2. THE EFFECT OF ECONOMIC INTERACTION BETWEEN CHINA, TAIWAN, AND HONG KONG: ADVOCATES OF INTEGRATION

Within the existing favourable political and economic circumstances pursued purposefully by related governmental policy, economic interactions, trade and investment flows, across existing borders occur spontaneously through the activities of businessmen pursuing profits. While massive trade and investment flows rush into China seeking profits from the booming Chinese economy, regional governments right across East Asia have far outstripped business communities' steps to act on this. The trend is for a remarkable pace towards interdependence of related economies, although at first the transaction among them was not focused by an ambitious integration plan. As the transaction flows inside the CEA, based more on economic complementarity, turn faster and more frequently, so emerging networks have brought about a rethinking of economic integration.

On the contrary, instead of governmental initiatives, the great volume of transaction has raised strong demands for certain organisations to resolve the problems which have occurred in the process of transaction. The importance of the establishment of such organisations was later realised and endorsed by the governments. Indeed, there have been some individual semi-official organisations dealing with common functional problems across the Taiwan Strait. For example, the Taiwan-based Strait Exchange Foundation, and the China-based Association for Relations Across the Taiwan Strait (ARATS), on behalf of their own respective government's interests, managed to hold the first summit meeting for mail and documentary registration between China and Taiwan in April 1993 in

Singapore.¹¹⁶ Since then, the talks between the two bodies have continued on a regular basis in accordance with the consensus agreed in the first meeting for dealing with their functional affairs. Because these talks were frequently interrupted by Beijing's intention to politicize them (to Taipei's anxiety), they have always ended without agreement. The fourth meeting in Beijing continued the talk up to March 1994.¹¹⁷

However, their emergence from already complex transactions provides some evidence that there is a strong demand from the business community for regulation of their transactions across the Strait. This is, to some extent, directing governments' policy.¹¹⁸ Unlike transnational institutions for integration elsewhere, what these groups in the CEA are attempting to be, for now, is "a mediator", on the part of the business communities, rather than "a manager", by governments, of the likely integration. It is very distinctive that the transaction volume within the CEA today presents an unbalanced relationship, or maybe more precisely a distorted partnership. Because of the policy restraints, Taipei does not want its market to be fully opened to China without further endorsements of friendliness from Beijing, as enshrined in Taipei's recent "Guidelines for National Unification". Although Taipei has continuously defied Beijing's proposal for direct communication and has reluctantly allowed its businessmen to trade with China via Hong Kong and elsewhere, trade and investment between China and Taiwan is still expanding very fast. There is a likelihood that direct trade

¹¹⁶. See *Summary of World Broadcast*, FE/1675, (29 April -3 May, 1993).

¹¹⁷. *Central Daily News*, International Edition, (28 March, 1994).

¹¹⁸. Charles H. C. Kao points out that Taiwan's mainland policy is not made by the government or Kuomintang, but by Taiwanese businessmen who have invested in China. The Vice Chairman of Strait Exchange Foundation, C. V. Chen, confirms that Taiwanese businessmen are the promoters of developments in mainland policy and the relations between the two sides of the Strait. *Central Daily News*, International Edition, (11 March, 1993).

between Taiwan and China sooner or later will be set up, as pressure from industrialists has increased. In addition, Hong Kong's position to be the "third country" of Taiwan's trading gateway to China will change in 1997. This has made Taipei feel the pressure of either changing policy to allow limited "direct trade" between Taiwan and certain Chinese ports, or to seek for alternative means for continuing "indirect trade". Indeed, in terms of planning a regional operational centre and mainland policy, it becomes clear that there are struggles within the Taipei government.¹¹⁹

For Taiwanese industrialists, in the first wave of China investment, China used to be merely a base for labour-intensive manufacturing for export. More recently, China has been treated as a manufacturing base for intermediaries, components and semi-finished products, which have been redirected back to Taiwanese assembly lines for export.¹²⁰ An empirical study has pointed to the immediate advantage of importing Chinese semi-finished products for Taiwanese industries' exports, because the market price for products labelled "made in Taiwan" is about 10-15 per cent higher than that for the same products but labelled "made in China".¹²¹ Namely, with Taiwan's labels on, exporting products will be more profitable. To proceed towards further integration in the CEA, governmental commitment from Beijing, Taipei, Hong Kong, will be decisive, in theory and in practice. Before political hostility between Taipei and Beijing can be watered down, the

¹¹⁹.See *Central Daily News*, International Edition, (21 March, 1994).

¹²⁰.For example, members of the Bicycle Manufacturing Committee of the Taiwan Association of Vehicle Industries, confirmed that the decision to import bicycle components from China has been agreed to increase competition in related sectors. *Central Daily News*, International Edition, (30 August, 1993). Taiwan's clothing industry is hoping for the government's consent for the import of more semi-finished products from China in order to build up the international division of labour. *Central Daily News*, International Edition, (8 July, 1993).

¹²¹.Charles H. C. Kao, Joseph S. Lee, and Chu-Chia Steve Lin, *An Empirical Study of Taiwan Investment on Mainland China*, (Taipei, Commonwealth Publishing Co., Ltd., 1992). p. 135.

Chinese and Taiwanese governments will have to act on behalf of their businessmen's interests in dealing with increasing members of practical problems caused by their increasing interactions. In the meantime, indigenous industries within the CEA and the TNCs endorse the ongoing CEA with more investment projects and by preparing operation centre plans targeting the CEA as a whole rather than a single economy. This could positively improve both economic growth and prospects for integration.

5.2.1. Governments' Commitment to the Formation of the Chinese Economic Area

As the transaction flows have tied the industries in China, Taiwan, and Hong Kong, into various frameworks for the division of labour, the level of their industrial interdependence, which is composed of the current trade regime for commodities, investment, and industrial cooperation on exchanging semi-finished products, personnel and technologies, becomes more and more apparent. Facing the increase of business, economic, and social transactions inside the CEA, businessmen can never again let go of this opportunity for profits and market share in the CEA. Nor would governments risk missing any opportunity of forming a regional bloc. Singapore's former Prime Minister, Lee Kwan-Yew, stated that:

"Chinese reunification is not so easily accomplished. But, as soon as transactions between the two sides of the Strait begin, reunification is to be a dynamic and everlasting process. ... So, the ongoing (benign) situation between them will not be reversed anyway."¹²²

¹²².Translated from Chinese. Information was based on an interview in *Central Daily News*, International Edition, (6 September, 1993).

The more the Chinese economy integrates into the world economy, the more it will be directed by global market forces rather than by the Chinese state. Part of the effect of market forces has been to intensify the business, political, and economic transactions across the Strait which make up the beginning of economic integration, and to a lesser extent, of Chinese reunification. In spite of political obstacles, the transactions have continuously thrived and problems which occurred are being collectively sorted out. Therefore, official moves to link with each other have concentrated on bringing about common ground for removing the differences.

Chinese Endorsement of Reform

China's commitment to its reformist open door policy has become a crucial factor not only for its own economic development but also for the possibility of the formation of the CEA. No Chinese official has ever commented openly on the economic integration of the CEA. Most recently, for the first time, Chinese Vice-Premier and Foreign Minister Qian Qichen directly made a reference to the concept of "Greater China Economic Sphere" as being still far from a reality.¹²³ Beijing's willingness to keep a low profile over the CEA is obvious in case there may be a backlash from other countries, notably Japan and the ASEAN countries.

In spite of the lack of formal confirmation of the CEA from Beijing, its guarantee of the reformist policy has been a positive incentive. In comparison with China's economic

¹²³ Qian Qichen, in his visit to Los Angeles on 22 November right after the annual meeting of Asian Pacific Economic Cooperation conference in Seattle, openly expressed the Beijing government's attitude to the concept of "Greater China Economic Sphere". It was the first time that a Chinese official commented on this concept. See *Central Daily News*, International Edition, (25 November, 1993).

reform, its political change has not been prominent. In terms of progress towards democracy, the focus has been not so much on the political system, but on arranging the transfer of power. It is very clear that Deng Xiao-Ping's "theory" encourages more reforms to promote market-driven economic growth, but, at the same time, Deng is inclined to keep quiet about political change. In other words, its legitimacy stems from "its ability to deliver economic prosperity without forfeiting political security".¹²⁴ Deng said in 1984 that "the domestic policies emphasize two points - politically, to develop democracy, and economically, to adopt reform" under the rules of socialist development.¹²⁵ Deng's perception of linking democracy and reform characterised by Chinese socialism is very different from Western definitions of a pluralist society. His concept of democracy may have focused on democratic centralism in the party's system,¹²⁶ which allows party elites, rather than the public, to be involved in the decision-making process in order to legitimize the collective leadership. Such theoretical understanding has set up a complex political and economic paradox: a "socialist market economy", with a socialism characteristic of China.

No matter what will happen in the unpredictable power struggle of Beijing, persistent reform on the economic front has unquestionably been a necessary part of the Chinese development. So long as the reform is to continue in China, economic build-up is likely to push the formation of the CEA further forward. For Beijing, insistent reform will

¹²⁴.Elizabeth J. Perry, "China in 1992: An experiment in neo-authoritarianism", *Asian Survey*, 33: 1, (January 1993), p. 14.

¹²⁵."Brief introduction to some of Deng's speeches", *Beijing Review*, 36: 47, (22-28 November, 1993), p. 33.

¹²⁶.This understanding has been announced by Deng's party followers in the third Plenary Session of the 14th Central Committee of the Chinese Communist Party. See *Beijing Review*, 36: 47, (22-28 November, 1993), p. 30.

undoubtedly speed up its economic development which has been tied in with Hong Kong and Taiwan as well as the other economies in the region. Since early 1992, the Beijing government's reformist policy has been confirmed on many important occasions, i.e. in January 1992, Deng Xiao-Ping's Southern tour; in October 1992, the 14th Communist Party Congress' affirming a capitalist economic development; and in April 1993, the first session of the eighth National People's Congress endorsing a Chinese style of capitalism. With Congress approval, "a socialist market economy" has been set as a goal of China's reform.¹²⁷ According to China's own explanation, a "socialist market economy" is "a comprehensive concept, which seeks to combine the superiority of public ownership with a rational disposal of resources ensured by a market economy."¹²⁸ One surmises the implication of this term as "free markets without free politics; a vibrant private sector alongside a dominant public sector; a further opening to the west, but a vigorous fight against pollution by some western ideas."¹²⁹

The Premier Li Peng, the hardliners' protégé, in a press conference even said that "economic development is the most important task for this government" and that "the government will ... open wider to the outside world over the next five years."¹³⁰ Jian Zemin, Chinese President, urged the deepening of reforms as "crucial in solving new contradictions and problems in China's economic activities" and called for "stepped-up efforts to carry out reforms in all fields, especially in the areas of the financial, investment and

¹²⁷ *Beijing Review*, 36: 15, (12-18 April, 1993), p. 9.

¹²⁸ "Jian on foreign and domestic issues", *Beijing Review*, 36: 34, (23-29 August, 1993), p. 10.

¹²⁹ "Capitalism, Chinese style", *Financial Times*, (14 October, 1992), p. 20.

¹³⁰ "Jian on foreign and domestic issues", p. 10.

taxation systems, to speed up the establishment of a socialist market economy."¹³¹ Furthermore, Zhu Rongji, Chinese Vice-Premier, said that "China's booming economy has given investors and businessmen more and more confidence because of its tremendous potential and wide ranging opportunities" and asserted that "China will not slow down its reform."¹³²

Although there is always a danger ahead of the return of the hardliners, both sides of the political groups in Beijing have agreed that reforms will have to be carried on in dealing with the actual economic development. As long as China's reform programme remains in place, its desperate demand for foreign capital will lead to increased dependence on Hong Kong and Taiwan. More and more people, especially in the Hong Kong and Taiwanese business communities, trust that the deepening and widening effects of economic interactions between China, Taiwan and Hong Kong will only encourage the formation of the CEA. As far as economic integration is concerned, the development of the CEA has reflected, up to now, China's bases defining the current reform as having pure economic and unofficial features. It is very likely that Beijing will be positive to the formation of the CEA, as long as it retains self-restraint by confining itself to an economic event.

Hong Kong: Tying up with China

Hong Kong has been very keen to develop commercial links with China, because not only has its highly commercialised, industrialised economy of export orientated strategies taken advantage of China's low cost production factors, but also its "middleman" role with regard to China has increased its

¹³¹ "Jiang calls for deepening reforms", *Beijing Review*, 36: 37, (13-19 September, 1993), p. 5.

¹³² "Reform guarantees further development", *Beijing Review*, 36: 38, (20-26 September, 1993), p. 5.

importance in managing foreign investment flows to China. Apart from the economic incentives of advantages, Hong Kong's investment boosted economic growth in China generally, and the nearby province Guangdong particularly, and has carried with it an undetected belief in steering China's economy to greater integration with the capitalist economic world. This may have contributed much to the emergence of China's recent market approach. It seems likely that if the economic development gap between Hong Kong and China can be narrowed down further in the next few years, market forces will then take charge of Hong Kong's fate, even after 1997 under China's government. Recent examples of Hong Kong entrepreneurs' heavy investing in China's infrastructure have reflected this hopeful line of thinking.

Because of the free market economy, Hong Kong's enterprises have been profit-orientated. In addition, Hong Kong's industrial development policy has been based on a *laissez-faire* approach. What the government has intended has been to "provide the private sector with an economic environment and the infrastructure conducive to rapid growth, including the provision of adequate industrial support facilities and services".¹³³ While China's open door to the outside world encouraged great opportunities for potential businesses, the Hong Kong government has been actively offering specific help for enterprises. For example, the Hong Kong Trade Development Bureau set up links with Beijing in 1986. Since then, the Bureau has purposively played an important role in linking Hong Kong enterprises with China.¹³⁴ It may be that such efforts have arisen from a British hope of

¹³³.OECD, *The Newly Industrialising Countries: Challenge and Opportunity for OECD Industries*, (Paris: OECD, 1988), p. 47.

¹³⁴.*Global Views*, (15 December, 1993), p. 146.

securing vested interests with as strong a presence in the CEA as they used to enjoy in the colony.

It is, therefore, in the Hong Kong government's interest to involve itself actively in the formation of any economic grouping with China. In the short term, China's industrial scale economies could reinforce Hong Kong's economic power through further industrial cooperation to which they have both contributed. As Singapore has been for the Malaysian economy, so Hong Kong may become for the Chinese economy, and to some extent for the CEA. In the long term, with a leading role in the CEA, Hong Kong will be much more confident about keeping its prosperity within the Chinese "socialist market economy". Facing an uncertain future over the political structure currently in place, Hong Kong's future may all depend upon tightening its links with China, or at least with Southern China economically. Although the current tension between Hong Kong Governor Chris Patten and Beijing about Hong Kong's political reform has caused a division of Hong Kong society, Hong Kong's will to tie its economy to China's economic development remains solid.

Taiwan: Asian Pacific Regional Operational Centre?

The Taipei government has brought forward a very ambitious programme of building itself up as a regional operation centre, for R & D, manufacturing, finance, and transportation. This programme has inspired widespread discussion amongst officials, economists and industrialists in Taiwan, because of its implications for the development of the CEA. One governmental analysis suggests that:

"[F]rom the viewpoint of resource complementarity and division of labour, current restrictions on indirect

investment and trade across the Straits will be relaxed to an appropriate degree; technological exchange will be strengthened; and more effective guidance and support will be given to Taiwan manufacturers that invest in mainland China."¹³⁵

Dozens of economic reasons seem to support the programme that has been put forward, including diversified export markets, upgraded industries, balanced bilateral trade, an improved environment for investment, and internationalisation of management to cope with fierce global competition. Since 1992, the transactions between Taiwan, Hong Kong and China have reached a "threshold" which has brought their relationship into a new era of interdependence. According to a conservative estimation, there are at least 10,000 Taiwanese companies now located in China, and total investment has reached the record level of US\$ 10 billion.¹³⁶ Unofficial guesses in Taiwan put the amount of investment at US\$ 15 billion-25 billion.¹³⁷

What this programme is concerned with is the preliminary conditions that Taiwan must develop to become an operational centre, and its prospects in the CEA. To become a regional centre Taiwan will have to remove all political and legal obstacles in order to accommodate multinational corporations' business strategies. The Director of the Commerce Department of the United States in Taipei, Mrs Ying Price, pointed out that Taipei's non-communication policy with China will definitely bar many multinationals from Taiwan, simply due to lack of access to the CEA market.¹³⁸ As far as the regional

¹³⁵. *Economic Revitalization Program: An Action Plan for the Promotion of Private Investment*, Council for Economic Planning and Development, Republic of China, (July 1993), p. 8.

¹³⁶. I. S. Kao, Director of the Industrial Development and Investment Centre, under the Ministry of Economic Affairs, quoted this information to confirm the government's intention to act on this change in "The Feasibility of Taiwan to be Asia-Pacific Regional Operation Centre". See *Business Weekly*, (24 May, 31 May, and 28 June, 1993).

¹³⁷. *The Economist*, (22 May, 1993), p. 73.

¹³⁸. *Business Weekly*, (28 June, 1993), pp. 61-63.

operation centre is concerned, the programme has to be considered in the context of economic integration in the CEA. If Taiwan is to be an Asia-Pacific regional operation centre, in addition to other necessary conditions, it will have to define its position in the CEA first, which means that Taiwan's direct trade links with China will be essential. More recently, Taipei has proposed an alternative policy for negotiating "selective" direct trade links with Beijing.¹³⁹ While current transactions are considered as in the short term phase, the preliminary conditions for a regional operation centre have been regulated in the medium term, according to the Guidelines for National Unification.

From an economic perspective, the regional operation centre will be conducive to Taiwan's economic success through alliances with the TNCs for upgrading technology and establishing a leading role in the division of labour across the CEA. Although the Taipei government has never blatantly advocated the concept of the CEA, it has tacitly recognised its importance with regard to its programme for the regional operation centre.¹⁴⁰ In accordance with its Guidelines and market forces, modifications in policies have been quietly brought forward:

"[R]elaxation of indirect trade across the Straits and expansion of imports of semi-finished products from the mainland. Promotion of cross-Straits exchange of industrial technology and recruitment of talent from the mainland. Strengthening of guidance and support for Taiwan businessmen investing in the Mainland."¹⁴¹

¹³⁹. *Central Daily News*, International Edition, (14 September, 1994).

¹⁴⁰. In an interview on 13 August, 1993, Dr. H. H. Tsai, Vice Chairman of Council for Economic Planning and Development, R. O. C., admitted that the government has endorsed the formation of the CEA in its programme for the regional operation centre.

¹⁴¹. *Economic Revitalisation Program: An Action Plan for the Promotion of Private Investment*, (July 1993), p. 13.

Many argue that the emergence of the CEA has served as a pure economic cooperation mechanism in the greater Chinese community.¹⁴² In spite of less open confirmation of economic integration from governments, Taipei's commitment to the CEA has been repeatedly apparent in its partnerships with the TNCs. (see Appendix T-5.1) In response to the reality occurring in the CEA, the Industrial Development Bureau under the Ministry of Economic Affairs in Taipei has drafted a comprehensive framework for integrating "industrial division of labour across the Taiwan Strait".¹⁴³ In addition, the Council for Economic Planning and Development, a ministerial level institution, under the Executive Yuan, emphasises that to keep up with the increasing trend of economic exchange between China and Taiwan, Taiwan will not be hesitant in developing its future economic blueprint based upon China as a hinterland. A practical move has been setting up an Asia-Pacific regional operational centre on Taiwan's west coast as an expediency as no direct link exists with China.¹⁴⁴

In commenting on Taiwan's regional operation centre programme, a French businessman, Olivier C. Moore, Chairman of the Taipei-based European Council of Commerce and Trade, has stated that for many European enterprises Taiwan is seen as a business springboard from which many of the TNCs have launched their business development from Taiwan to China, and to the Chinese community in Southeast Asia.¹⁴⁵ The American Offshore

¹⁴² Professor C. Y. Cheng of Ball University, USA, and Professor W. S. Chen of Fu-Dan University, China, argued that pooling resources in the CEA through rational distribution could generate a certain economic unity in the Conference for "Trade Relationship Between the Two Sides of the Strait" held in Taipei, 27-28 September, 1993. *Central Daily News*, International Edition, (28 September, 1993).

¹⁴³ *Central Daily News*, International Edition, (13 December, 1993).

¹⁴⁴ *Central Daily News*, International Edition, (12 December, 1993).

¹⁴⁵ According to his comments, Taiwan has got a solid manufacturing base, plenty of skilled labour, a superior geographic location in the Asia-Pacific market, and the same cultural

Institute has offered an insight into the industrial cooperation occurring in Taiwan. It states that:

"[A]s major industrial corporations from around the world and especially the high technology sectors open regional offices in Taiwan, joint ventures between the newcomers and Taiwanese businesses and agencies aim at strategic placement for basic needs in key areas such as semi-conductors, chemicals and telecommunications. China is the main target of this planning."¹⁴⁶

5.2.2. Global Strategy Vs. Regional Economic Integration: The Position of Transnational Corporations in the Chinese Economic Area

Clearly, multinationals base their strategy for investment on profit through the making of opportunities. In terms of protectionism and national trade barriers, regional integration has less clear effect in the TNCs' global market operation. Whilst people usually notice the TNCs' profit gaining strategies, they tend to ignore how important the TNCs are in the process of regional integration. Corporate integration is the term used by some to define the causes and effects of integration activities.¹⁴⁷ Regional government officials describe how important the TNC was to regional economic development:

"the very rapid growth of East Asian economies over the past three decades has been due, in large measure, to the

background as China, foreign companies can therefore use Taiwan as a multi-functional base in the CEA. See *Central Daily News*, International Edition, (13 August, 1993).

¹⁴⁶ "Taiwan stimulates Pacific Rim", *The Diamond File, Offshore Investment*, 37, (June 1993), p. 8.

¹⁴⁷ John Dunning and Peter Robson, "Multinational Corporate integration and regional economic integration", *Journal of Common Market Studies*, 26: 2, (December 1987). More discussions can be found in the same volume.

technology, capital, and managerial and marketing know-how contributed by multinational corporations."¹⁴⁸

From the perspective of regional economic integration, through industrial division of labour, in some cases division of trade, which was established as a result of foreign capital investment, various national economic interests in the region could be linking together. The hope is that a common interest will emerge as a result. For example, whilst many other industries are seeking to pursue industrial cooperation within the greater Chinese market individually or collectively, the information and computer industries have already established their own links targeting the CEA. Microsoft, Philips, IBM and Hewlett-Packard have since 1992 set up headquarters in Taiwan to manage rationalisation of their resources covering Taiwan itself, China, and Hong Kong.¹⁴⁹ In the petrochemical industry, ICI (London) has invested in China and Taiwan gaining a market share in the CEA as a way of looking ahead to the wider Asia-Pacific market.¹⁵⁰ Through the TNCs' "greater China" marketing vision, one can expect that an increased exchange of resources, personnel, and components will intensify existing interdependence, which will be meaningful and beneficial to economic integration.

Apart from the technology and marketing experience that the TNCs normally introduce, their targeting of the CEA is concerned today with an exchange of managerial and technical personnel. Philips' President, J. D. Timmer, for instance, in

¹⁴⁸. Vincent C. Siew, Chairman of Council for Economic Planning and Development, (former Minister of Economic Affairs), in a speech for the American Chamber of Commerce, "The Prospects of the ROC as a Regional Operation Centre", *Industry of Free China*, (March 1993), p. 15.

¹⁴⁹. *Central Daily News*, International Edition, (13 November, 1993).

¹⁵⁰. Natasha Alperowicz, "ICI's Asia/Pacific operations set for significant growth", *Chemicalweek*, (November 25, 1992), p. 35.

a speech to mark the 25th anniversary of Philips Taiwan, pointed out that:

"... with our active participation in this market (the Pacific basin) with its prospects for growth and its enormous potential, Philips definitely intends to expand its presence in this region.", and "Philips Taiwan has always been the essential 'Chinese component' in the Philips family."¹⁵¹

Taiwan Philips' management teams, thus, have been chosen to run its Asia-Pacific strategy of access to the CEA.¹⁵² Within its global strategy, the development of Hewlett-Packard's greater China plan emphasises establishing networks and exchanging managerial experience between China, Taiwan and Hong Kong. Since Hewlett-Packard is already highly focused on China's domestic market, there has been a group of Taiwanese managers sent to China in the belief that well-educated and experienced Taiwanese managers probably are the best to conduct business in China in order to become "networking technicians" for their Western and Chinese clients.¹⁵³ For reasons of culture, language, and technology, some Japanese firms have employed Taiwanese technicians in their mainland China development. N. Tatara, a standing member of the board of Mitsushita Taiwan Ltd., reveals that the company has sent out seven engineers it has trained in Taiwan to help other Mitsushitas operating in China.¹⁵⁴ Recently, some cases of strategic alliance between the TNCs and Taiwan's companies targeting the CEA have brought about the division of labour

151. Philips Taiwan in Perspective, 25th Anniversary (1966-1991), 1991.

152. *Central Daily News*, International Edition, (30 May, 1993).

153. Information obtained from an interview with Mr. Jia-Bin Duh, Deputy General Manager, Hua Pu Information Technology Co. Ltd., (Subsidiary of Hewlett-Packard in China), on 6 August, 1993 in Taipei.

154. *Taiwan Industrial Panorama*, 20: 11, (November 1992), p. 3.

within the CEA. Examples are: Carpenter Technology Co. of the US and Walsin Lihwa Electric Wire & Cable Co. of Taiwan; Taiwan's Teco Electric & Machinery Co. and Nippon Electric Co. (NEC).¹⁵⁵ Moreover, while American Telephone & Telegraph Co. (AT&T) developed a strategic alliance in 1993 with the Taiwan telecommunication industry "to manage technology transfers, win contracts and operate manufacturing projects", AT&T was discussing the formation of joint ventures with China to make telephone switching equipment.¹⁵⁶ Many indigenous industries have also followed in the TNCs' footsteps to expand their operation within the CEA. For example, Nan Ya Plastics Co., Taiwan's leading manufacturer, announces its plan to set up a US\$30 million plastic factory in Guangzhou to supply upstream materials to Taiwan's downstream plastic producers.¹⁵⁷

Industrial cooperation in targeting the greater vision of the CEA amongst the TNCs and indigenous industries is virtually paving out a preliminary approach toward further economic integration. Those industrial cooperations are all but knitting transaction networks between regional economies regardless of political constraints. These networks are considered a preliminary and necessary development to forming a community. Logically, an industrial strategy bound up with cooperation would not necessarily advance to a larger scale of integration. But it is to be borne in mind that integration would not be thought of without those efforts for industrial unity which are naturally or purposively underway. However, while the depth and width of industrial links go beyond the

¹⁵⁵ *Taiwan Industrial Panorama*, 21: 4, (April 1993), p. 3.

¹⁵⁶ *Taiwan Industrial Panorama*, 21: 3, (March 1993), p. 3.

¹⁵⁷ *Central Daily News*, International Edition, (1 April, 1994).

definition of business strategies, a larger scale economic spillover is yet to appear.¹⁵⁸

5.2.3. Pre-Transnational Institutions for Economic Integration: Regional Business Associations on the Move

A great move toward economic integration has been going on for a decade or so between China, Hong Kong, Taiwan, and the Asian Chinese Community, though it doesn't seem to be quite following the European track. The Japanese scholar, Saburo Okita, the head of the Domestic and International Policy Studies Institute in Tokyo, made the comparison that:

"one of the big differences between East Asian integration and European integration is that in Europe it's based on treaties. In East Asia it's based on market force."¹⁵⁹

European integration was motivated by political factors from the beginning, though it has been manifested mainly in economic forms. The development of the CEA, one of the East Asian groupings driven by market forces, has been pushed spontaneously by the efforts of many businessmen in the private sector. It is only activists, mainly businessmen and academics, who have recognised these developments in terms of integration. Although businessmen scarcely consider economic activities beyond their own self-interest, some have understood a growing need for setting up industrial organisations to act in their common interest.

¹⁵⁸.Industrial cooperation could be leading not just to the formation of joint ventures, but also integrated management, labour markets, marketing networks, to name but a few developments. Hence, the TNCs' lead may draw many more small and medium size enterprises towards industrial cooperation.

¹⁵⁹. "Will Japan rule a new trade bloc?", *Fortune*, (5 October, 1992), p. 47.

There have been an absence of official links between Beijing and Taipei. Businessmen have relied on their own "guan si" (personal relationship) with China. Many different functional organisations have emerged as a result, e.g. the semi-official Strait Exchange Foundation (SEF), and the Association For Relations Across the Taiwan Strait (ARATS), the unofficial Association for Commerce across the Taiwan Strait and many other industrial associations. To begin with, some organisations developed as trouble-shooters or, to some extent, to promote dialogue. The Taiwan Computer Association which, amongst many others, has been successful in setting up a "street for electronics in Shanghai", has managed to sort out all legal procedures and marketing in China for over thirty computer companies from Taiwan.¹⁶⁰ The SEF's earlier business was mainly dealing with smuggling and expatriating smugglers on behalf of the government. Whilst these activities gradually became a routine, demands for larger scale cooperation became increasingly powerful. The first talk between the SEF and the ARATS in Singapore in April 1993 marked a new milestone for further cooperation and dialogue between China and Taiwan. More importantly, a network of regular consultation has been agreed.

Another influential organisation has been the Commercial Development Foundation across the Taiwan Strait led by P. S. Chan, the Chairman of the Taiwanese Association of Commerce. Sponsored by 48 entrepreneurs who are currently actively investing in China, the Foundation exists to collect business information, provide consultant services, arrange commercial exhibitions, bring together Taiwanese businessmen, and for

¹⁶⁰ "A street for electronics", which is invested by Taiwanese electronics and computer industries, is predicted to be an electronics and computer centre in Eastern China. It has formally started operating since October 1994. See *Central Daily News*, International Edition, (17 October, 1994).

marketing research.¹⁶¹ As usual, China has immediately created a parallel organisation, Economic and Trade Association across the Strait, to liaise with it. China's intention to take the lead in private sector transactions is clear. Some leading industrialists in Taiwan and Hong Kong have appealed for greater cooperation between the three economies. The "Hong Kong-Taiwan Committee For Economic and Trade Cooperation" was established in this context in 1992 to strengthen economic and trade cooperation between Hong Kong and Taiwan. Thereafter the Committee promised to meet on a regular basis in rotation of two sides once a year. At the second meeting, held in Taipei in May 1993, over twenty entrepreneurs from Hong Kong, led by M. S. Chan, the Chairman of the General Chamber of Commerce of Hong Kong (GCCHK), and about a hundred local industrialists led by S. F. Hsiu, the former Chairman of the Chinese National Federation of Industries (CNFI), called for improved administrative regulations to speed up the trade between them. Taipei's decision-makers in economic and mainland affairs were also present because of its importance.

Most recently, Chairman Hsiu of the CNFI has launched omnidirectional moves to integrate economic resources inside the CEA in company with the GCCHK and the China Promotion Council for International Trade (CPCIT). He believes that in terms of capital, resources, and technologies, current transaction networks do not measure up to the objective of economic effectiveness.¹⁶² He has firmly devoted himself to the concept of forming a Southern China Economic Sphere upon which the CEA economic integration is based. In the present stage of economic transactions, trade, foreign investment, and making-

¹⁶¹.H. R. Huang, "Su Shih Ba Wei Chi Yei Chia Kun Chuang Liang An Shih Yei", (Forty-eight entrepreneurs collectively create business across the Strait), *Business Weekly*, (5 April, 1993).

¹⁶².*Central Daily News*, International Edition, (11 September, 1993).

up industrial division of labour, have taken place to a considerable extent in the area of Hong Kong, Taiwan and Southern China, i.e. Guangdong and Fujien provinces. According to Taiwan's official statistics on locations of Taiwanese investment in China, permitted investment which has mainly gone to Shenzhen, Guangdong, Xiamen, Guangzhou, and Fuzhou, accounted for 55.95 per cent of Taiwan's total permitted investment in China in 1991; and 44.37 per cent in 1992.¹⁶³ In addition, information about Taiwanese manufacturers' geographic locations also shows that the coastal areas have been the most favoured.¹⁶⁴

In Chairman Hsiu's report on an investigative trip to Hong Kong and China in late October 1993, in terms of industrial cooperation, he suggested that Taiwanese mainland investment will have to be brought to a macroeconomic-level in the CEA as a whole, and develop more details for the industrial division of labour with China through individual industrial associations.¹⁶⁵ Furthermore, K. C. Lin, President of Sino-Japan Feed Industry Co., proposes that to be more effective in managing trade, commerce, and investment between China, Taiwan, and Hong Kong, it is better to establish a collective sharing company combined with capital and entrepreneurs from the above economies through tasks undertaken jointly for the CNFI (Taiwan), the GCCHK and the CPCIT (China).¹⁶⁶ The essence of this proposal is combining:

¹⁶³.Information was based on Investment Commission, Ministry of Economic Affairs, R. O. C.

¹⁶⁴.In April 1991, among 1503 companies registered with the Taipei government, there were 1854 companies relocated in Southern coastal China: companies in Xiamen (275/11%), Fujien Province (323/12.9%), Dongguan (187/7.5%), Guangdong Province (561/22%), Shenzhen (379/15.1), Zhuhai, and Shantou (129/5.2). Ibid.

¹⁶⁵.*Central Daily News*, International Edition, (31 October, 1993).

¹⁶⁶.This proposal was announced on 1 November, in Hong Kong at the conference for "Lian An Shan Bien Gin Mao " (Economic and trade relationship amongst three parties between two sides of the Taiwan Strait), which was the first meeting ever joined by leading industrial associations between China, Taiwan, and Hong Kong. See various reports in *Central Daily News*, International Edition, (1-4 November, 1993).

Taiwan's capacity in design, commercial R & D, marketing, and management; Hong Kong's financial and trading prominence; and China's promising production and manufacturing advantage. Although this plan is so far merely for industrial cooperation, keen willingness to form "a company", which would, to some extent, be a managing body for further cooperation, has been shared by many businessmen in the CEA. To avoid any uncertainty, Lin's proposal has been regarded as a practical move to integrate capital, technology, marketing, and manufacturing in the CEA in order to guarantee the current optimal economic transactions between the three economies.¹⁶⁷ If this can be worked out, industrial cooperation between China, Taiwan, and Hong Kong will be able to bring about the hope for economic integration.

5.3. CONCLUSION

Although the CEA has so often been the marketing concept of the business community in the region, its increasing economic importance has become the focus for industrial development, economic growth and regional economic integration. Since the mid-1980s Hong Kong and Taiwan have been undertaking industrial restructuring in order to survive external competition in trade and industrial development. China, on the other hand, has been on the reformist track since 1979, during which period its industrial structure and economy as a whole have been rapidly modernising. It is this fundamental economic complementarity between China (market and labour), Taiwan (capital, manufacturing experience and

¹⁶⁷. *Central Daily News*, International Edition, (3 November, 1993).

technology) and Hong Kong (financial service and transport centre), which has provided the favourable incentives for their economic cooperation.

The post-Cold War international political and economic context which favours economic interaction, because of increasingly intense industrial competition, and overseas Chinese intensifying their investment in the Asia-Pacific region, has accelerated the process of the formation of the CEA. More importantly, intense global industrial competition and the emergence of regional trading groupings with protectionist measures have marginalised Taiwan and Hong Kong's trading position in world markets as the suppliers of cheap manufacturing products. As part of a strategy of industrial restructuring, Taiwan and Hong Kong have relocated their manufacturing sites in and have increased their direct investment in low-cost neighbouring economies, i.e. China and Southeast Asian countries. As China is experiencing rapid economic development, the potential market in China provides Taiwan and Hong Kong their best opportunity for restructuring industry. Moreover, industrialists recently from China, Hong Kong, and Taiwan have started to campaign for closer economic cooperation in the hope of building-up industrial partnership within the CEA. While economic benefits, instead of political motives, have been the constant driving force behind the formation of the CEA, the private sector has from the beginning been leading the process of the CEA's economic integration. The peculiar political atmosphere between China and Taiwan and between China and Hong Kong, has reinforced this trend.

CHAPTER SIX

POLITICAL CONSTRAINTS IN THE CHINESE ECONOMIC AREA AND THEIR IMPLICATIONS FOR ECONOMIC INTEGRATION

The emergence of the Chinese Economic Area has profited from the general favourable trend of the "three Chinas" rallying towards economic integration in response to the need of Hong Kong and Taiwan for industrial restructuring and of China for further economic development. Although there are as yet no official links between Taiwan and China, and Taiwan and Hong Kong to endorse their economic ties, the governments of the three have been inclined to support quietly the concept of economic grouping. Nevertheless, their thriving economic ties are subject to political constraints, particularly, the prolonged antagonism between China and Taiwan, and the new row between China and Britain over the future of Hong Kong. These political constraints nevertheless have not blocked economic links, because the Chinese Economic Area has been based very much on its complicated business links and less on political commitment. It is to be seen in the future of the CEA whether or not advancing economic integration clearly relies on the settlement of political constraints. In terms of economic interaction, however, the spillover effect becomes noticeable driving both economic and political development into a benevolent circle. So far, economic integration generated by the forces of economic development has gone beyond political stalemate. Even in contending with each other politically, China and Taiwan have not been able to sacrifice their immediate complementary economic interests.

This chapter analyses political constraints within the CEA and political developments of "the three" which have contributed to the emergence of the CEA. It examines to what extent political constraints will shape the future of the CEA. The shortage of official collaboration between the economies of the CEA has thrown doubt upon their further moves towards economic integration. The purpose of this chapter is primarily to show that despite political difficulties, economic development and industrial cooperation, the key factors in the progressive development of the CEA, could well be an example in explaining the process of regional economic integration.

6.1. THE POLITICAL IMPETUS TOWARDS THE CREATION OF THE CHINESE ECONOMIC AREA

The emergence of regional economic integration relies on a favourable international political and economic setting, as well as on domestic political and economic situations in the relevant countries. While the formation of the CEA, so far, has owed little to political factors, the governments in China, Taiwan and Hong Kong remain the critical factor on whether the CEA is coming into being or not. Although these governments were officially apathetic to the development of the CEA, there have been some policies pursued by each government favourable to the CEA. In the context of political compliance with economic transactions which has intensified in response to external competition, the CEA has thus been able to come about to a considerable extent, in fact. How has political development cultivated favourable circumstances for the formation of the CEA? In particular, due to political hostility, China and Taiwan have not yet developed a

consistent official communications network. It is, therefore, very important to have a detailed understanding of recent political developments in the relevant economies.

6.1.1. Beijing's Reformists in the Ascendency

Beijing's reforms have not only led to China's increasing openness as a market and thus allowed further economic links with Hong Kong and Taiwan, but have also encouraged the developments towards economic integration. Although it remains to be seen how substantial China's reforms are in stimulating the formation of the CEA, the authority of Beijing's policy on economic reforms has undoubtedly encouraged the business community's hope for the CEA. At the end of 1978, Deng Xiaoping emerged as the leader in the Third Plenum of the 11th Central Committee of the Chinese Communist Party (CCP). Since then, with his management group in charge, Deng's economic reforms have created a remarkably fast economic growth performance. Many believe that Deng's "strong faith in technocrats, technology and people's preoccupation with material betterment" has been the crucial trigger for successful reforms.¹ In addition, although he has not been officially in charge of all policy-making, Deng has intervened in economic policy-making on some important occasions, which, in effect, underlined Deng's confirmation of persistent reforms and rebutted possible criticisms from the communist conservatives. For example, Deng's Southern tour to Shenzhen Economic Special Zone in early 1992 contributed not only towards clearing away the uncertainty about economic reforms

¹. Lucian W. Pye, "An introductory profile: Deng Xiaoping and China's political culture", *China Quarterly*, 135, (September 1993), p. 441.

in the wake of the post-Tiananmen hard-lines, but also towards backing the reform policy politically. Again, while Beijing started to brake its economic growth in Summer 1993, Deng's call to speed up economic development occupied the agenda of a plenary session of the Chinese Communist Party's Central Committee held in the following November.²

The reform era resulted from Deng's distancing himself from the previous faulty economic policy initiated in late 1978 by Chen Yun and Li Xiannian with whom he closely allied at the time.³ That economic belief was still characterised as "ensuring the leading role of the planned economy and making the market economy an adjunct."⁴ In 1984, Deng's decision on urban reform and speeding up progress towards reform was endorsed in the Third Plenum of the 12th CCP Central Committee. The planned economy became a "planned commodity economy" which broke away from the conventional ideology that the commodity economy conflicted with socialism.⁵ During 1987-88, Deng repeatedly pressed ahead economic reforms and openly praised the reformist policy in order to keep pumping energy into the reform process.

After the 1989 Tiananmen incident, to tame the conservatives, Deng allowed the Premier, Zhao Ziyang, to be displaced and expediently slowed down economic reform in the attempt to diminish the damage from the aftermath of the pro-democracy "counter-revolution turmoil". At the beginning of 1992, Deng's intention to gear up the reform was shown in his Southern tour to Guangdong. Deng suggested that "a planned economy is not socialism. And a market economy is not

². See "Politics in Command", *Far Eastern Economic Review*, (25 November, 1993), pp. 14-15.

³. Barry Noughton, "Deng Xiaoping: The economist", *China Quarterly*, 135, (September 1993), p. 500.

⁴. "Dialogue on socialist market economy", *Beijing Review*, (26 October-1 November, 1993), p. 34.

⁵. Ibid.

capitalism - there are markets under socialism as well."⁶ While economic development and fast paced reform were becoming pervasive, Beijing's decision-makers realised that market forces were clearly advancing into the heart of the reform. So they explained that "the more developed and highly socialised commodity economy is actually a market economy."⁷ During Deng's domination of the 14th Congress of the CCP in October 1992, the term of the "socialist market economy" was formally introduced.⁸

From the long process of Deng's working up to the "socialist market economy", one can figure out that the reformists have been seeking for legitimacy for their reforms and open policy. It is therefore clear that the reforms have been characterised by Deng's personality. As many China observers have noticed, China's economic development has been guided through Deng's wielding influence over key circles of power in China.⁹ Maybe this one man show is the major reason why many businessmen, in particular the Japanese, still keep a cautious eye on China in respect of their long-term investment. However, in the past 15 years or so, Deng himself has realised that if the reform is to carry on in China, the political power will have to be assumed by a group of elites rather than a single person, through institutional transformation processes rather than a power struggle.¹⁰ Deng has been continually projecting his "theory" of economic reform to assure the continuation of the reform on his

⁶. Ibid. p.35

⁷. Ibid.

⁸. Ibid. p. 35, also "Dengism enshrined", *Far Eastern Economic Review*, (22 October, 1992), pp. 10-11. For the detailed definition of the term "socialist market economy" see section below.

⁹. This view was pointed in Barry Noughton, "Deng Xiaoping: The economist".

¹⁰. In various speeches made in the late 1980s, Deng, the "second generation" leader, has emphasised that the reformist "third generation" team led by President Jiang has been made ready for the transfer of power. See *Deng Xiaoping Wenxuan*, vol. 3, (Beijing: People's Publishers, 1993), pp. 296-301 & 309-314.

approved track. Deng's "theory" calls for political relaxation in order to allow more social resources to be used in economic development, and "let more people get rich first".¹¹ Part of Deng's achievement was his shift of political attention from the Chinese Communist Party itself and governmental organisations to economic construction. Deng's advocacy of a rapid growth economy and openness to the outside world was based largely on increasing private sectors and restructuring state sectors, which all happened in an environment of political relaxation. Under Deng's theory the central government will have to delegate authority to the lower level (local) governments for economic decision-making, as part of his idea of decentralisation of authority.¹² According to this idea, there appear to be: five special economic zones (SEZ); the fifteen coastal open cities; and the three estuary areas supporting the above SEZ and some coastal cities.¹³ In this context of economic incentives largely released from political constraints, the coastal area quickly follows the pace of the market economy to tie firmly in with world markets. The coastal provinces, have, to some extent, become autonomous in terms of economic decision-making regardless of central government's economic retrenchment since 1988. They have soon taken outward-looking economic approaches in place of the previous national policy of import substitution. Deng's credit

¹¹. The main points of speeches made in Wuchan, Shenzhen, Zhuhai, Shanghai, in the visits from 18 January to 21 February 1992, *Deng Xiaoping Wenxuan*, vol. 3, p. 374.

¹². Refer to Barry Noughton, "Deng Xiaoping: The economist", p. 504.

¹³. The five SEZs: Hainan, Shenzhen, Zhuhai, Shantou, and Xiamen; the fifteen coastal cities: Dalian, Qinghungdao, Tianjing, Yantai, Jinan, Qingdao, Lianyungang, Nantong, Shanghai, Ningbo, Wengzhou, Fuzhou, Guangzhou, Zhangjiang, and Beihai city; the three estuary areas: Zhangjiang Delta, Zhejiang Delta, and Minnan Triangle District. For details see Huongfan Jin, "China's open door policy and Asian-Pacific economic cooperation", *The Korean Journal of International Studies*, 22, (1990), pp. 128-129.

for economic reform was once again seen in allowing provincial economic plans and the private economy to go forward.¹⁴

The Tiananmen incident, which was seen by China's old guard, e.g. Chen Yun (member of Politburo Standing Committee, the CCP Central Committee 1978-1985), Peng Zhen, (Chairman of Standing Committee, National People's Congress in 1983) and Bo Yibo (Deputy-chairman of Central Commission for Guiding Party Rectification, the CCP 1983-1987), as a threat to their power, had resulted in the hardliners on the rise retrenching against further reform. In addition, as they witnessed the collapse of communism later the year in Eastern Europe and Mongolia, the hardliners were trying to move the clock back by taking up conservative policies. As one commentator succinctly noted: "the latter half of 1989 and first half of 1990 represented a return to the ruling techniques of old."¹⁵ The Premier Zhao Ziyang, the major practitioner of Deng's theory, who was made a scapegoat of the democratic upheaval for Deng, stepped down as a result of being blamed for causing the chaos.

Nevertheless, the conservatives themselves found shortly that their policies did not accord with the developing reality of China's growing economy and the rising expectations of civil society in which political relaxation was becoming more general. Widespread passive resistance appeared, as a result, in the shape of:

"enterprises and localities that failed to remit taxes to central authorities; provinces that balked at reasserted central control; work stoppages and increased worker absenteeism; intellectuals and urban residents who feigned compliance with post-Tiananmen investigations;

¹⁴. Deng's speeches in 12 June 1987 and 25 May 1988 encouraged provincial governments to speed up the reform. See *Deng Xiaoping Wenxuan*, vol. 3, pp.236-243 & 264-265.

¹⁵. David Shambaugh, "China in 1990: the year of damage control", *Asian Survey*, 31: 1, (January 1991), p. 48.

cadres who failed to implement ideological campaigns; and ordinary consumers who voted with their pocketbooks by hoarding savings."¹⁶

Apart from the general passive resistance in China, the demands of the international market and international political sanctions against the Chinese government for the Tiananmen incident reminded the hardliners that China can not be isolated from world society. 1990 was described as a year "in which China demonstrated the decisive power of a decade of reformist change" and "facing considerable domestic and international pressure, the leadership had no choice but to bow to the reality that China had qualitatively changed during the 1980s."¹⁷ Those factors maybe helped to force China's policies to swing back to reformist approaches. Deng himself delights to see and advocate speeding up the reform process. Consequently, as part of re-generating his reforms, Deng in April 1991 promoted some provincial elites with strongly reformist outlooks into the power centre of Beijing, e.g. the Vice-Premier Zhu Rongji (former Shanghai Mayor), and the Vice-Chairman of Chinese People's Political Consultative Conference, Ye Xuanping (former Guangdong Governor). This is evidence that, in the post-Tiananmen political situation, the conservative approach in leadership has been reversed in favour of the reformist.¹⁸ Furthermore, the so-called "cross century leading team" was decided in the 14th Congress of the CCP in October 1992 and later ratified by the 8th National People's Congress in favour of the reformists: Jiang Zemin, the President; Li peng, the Premier; Qiao Shi, the Chairman of National People's Congress, and Li Ruihuan, the Chairman of

¹⁶. Ibid., pp. 48-49.

¹⁷. Ibid., p. 49.

¹⁸. Tai Ming Cheung, "The wind changes: reformists favoured in appointments to state council", *Far Eastern Economic Review*, (18 April, 1991), p. 12.

Political Coordination. The signs for persistent reform have been greatly reinforced by the retreat of the old guards and their associates from this team.

In the past 15 years of China's reform, there have been clear indications that within the Chinese leadership there has existed a main division, or factionalism.¹⁹ The division is between Deng's reformists, "who believe that economic reform is essential to maintain the communist party in power and keep China socialist," and "those who believe that market orientated reforms endanger both these aims."²⁰ Some have tried to categorise the division of Chinese leaders, according to their political stands.²¹ Although most scholars tend to agree that economic liberalisation has a close linkage with political democratization, many still doubt that China's economic reforms approaching towards the market economy will create pressures for political freedom.²² This contradiction of the theory and the reality in China may well reflect the diverse beliefs of Beijing's leaders, and perhaps tell the reason why economic reforms have implied exploitation and experiment rather than a planned goal.

While the Tiananmen incident, from the hardliners' point of view, was evidence of economic liberalisation leading to political demands, the reformists assume that persistent economic reform is the only way forward for the party and socialism in China. Deng's reformist approach is more close to

¹⁹. Richard Baum, "Political stability in Post-Deng China: problems and prospects", *Asian Survey*, 32: 6, (June 1992), pp. 491-505.

²⁰. Ian Jeffries, *Socialist Economies and the Transition to the Market*, (London: Routledge, 1993), p. 172.

²¹. Such as: Baum's three main policy clusters: a neo-Maoist anti-reform group, a bureaucratic-conservative group, and a more progressive market-reform group. R. Baum, "Political stability", (June 1992), p. 494; Shambaugh's political alignment in the CCP: Ultra-conservatives, "soft" conservatives, moderates, and reformists. See Shambaugh, "China in 1991: living cautiously", *Asian Survey*, 32: 1, (January 1992), pp. 19-31.

²². Argument about social change with this linkage has been widely recognised. See Elizabeth J. Perry, "China in 1992", *Asian Survey*, 33: 1, (January 1993).

the reality of China's economic development today. The immediate political effect for Deng has been the safeguarding of the communist party's position in China. It is, nevertheless, true that the current economic reforms in China have not been given official credit for carrying out political reforms. In reality, through economic reform and open door policy, Chinese society has been turning to a "shadow pluralism" which could gradually transform the social and even the political system.²³

One of the main concerns inside Beijing has been the relationship between the central and provincial governments. Since the early 1980s, fiscal and administrative decentralisation has brought about autonomous provincial and local governments in China with increasingly independent ability in economic policy-making, which has resulted in their disregarding many of Beijing's regulations, mainly about economic growth speed and profit-sharing schemes. Although the central government has proposed some austerity programmes proposed since 1988 to tighten up its grip on economic policy in coping with inflation, unequal income distribution, and inappropriate budget sharing caused by the overheated economy, it is yet to be seen how far the provincial initiatives of "bold development" will be restrained. Especially in the Southern Chinese provinces, the pioneering and successful examples of China's economic reforms, led by Guangdong and followed by Fujien, have continued to go their own ways, in spite of Beijing's attempts to reassert central control.²⁴ While the Southern Chinese provinces' "bold development" in economics has stemmed largely from Deng's "theory" stimulating

²³. Gordon White, *Riding The Tiger: The Politics of Economic Reform In Post-Mao China*, (London: Macmillan, 1993), p. 236.

²⁴. For a series of special reports on Chinese provincial autonomy challenging the centre, see *Far Eastern Economic Review*, (4 April, 1991), pp. 21-30.

rapid economic growth, Beijing's wish to control the pace of economic reform has never been far in doubt. As provincial and local governments in China have obtained the initiative on economic policy in favour of deepening and widening reforms, this policy orientation has provided a favourable political background for Southern China's economy to be able to link firmly with Hong Kong and Taiwan, in terms of trade, industries, and technologies.

The political change in China, though not an official initiative, has been the interaction of two forces: briefly, market and state.²⁵ While China's leaders have realised that market forces constitute the drive for economic development, the legacy of the planned economy provided by the Communist Party remains the core of reforms. Accordingly, in October 1992, in the 14th Congress of the CCP and, in November 1993, in the 3rd Plenum of the 14th CCP's Central Committee, state-owned enterprises, with which the hardliners are concerned, were still emphasised as the core of the economic reform, with a complement of private enterprises. But, the central government has not been able to keep pace with provincial governments on economic development, although the former has time and again issued directives to slow down the overheated economy. There is an uncertainty about how far Deng's toleration of the provinces' going it alone will prove to be a temporary expediency, and when the central government would want to regain economic authority over provinces. Should that be the case, the present reform and open approach would be in danger. In the 3rd Plenum of the 14th Central Committee of the CCP, the attempt to strengthen the leadership and reinstate the supremacy of the party have been endorsed as a necessity

²⁵. Gordon White, *Riding The Tiger: The Politics of Economic Reform In Post-Mao China*, p. 238.

on China's way to further economic development towards a market economy.²⁶

The earlier reformist strategy was that the reform was a means to introduce an "open policy" in order to generate enough foreign resources for China's economic development, and at the same time allowed foreign investors to take advantage of China's growing economy. As far as the reform is concerned, China's economy increasingly intertwines with the market forces of the world economy. In the early 1990s, the results of the open policy have been pushing forward the reform process. Politically, the reformist approach which relies on market economies has, on the one hand, implications for the fate of the reformists in the context of Beijing's power struggle against the hardliners; and it has, on the other hand, provided a kickstarter for China's fast growing economy and, thus, favourable circumstances for the birth of the CEA. Especially, as economic and social transactions have been intensified across China, Taiwan and Hong Kong, there appear to be common interests over commercial links. While the Bush administration of the United States, for example, approved unconditional renewal of the most-favoured-nations' (MFN) trade status for China's exports to the US in 1991 and 1992, increasing pressure from Congress to reduce the trade deficit with China has made it clear that the White House should reconsider trade policy with China. The present US President Clinton is said to link the renewal of the MFN for China with China's human rights performance.²⁷ This worries all Chinese enterprises targeting the American market, including many from Hong Kong and Taiwan. Without the MFN, goods from China will

²⁶. See "Decision of the CPC Central Committee on some issues concerning the establishment of a socialist market economic structure", *Beijing Review*, 36: 47, (22-28 November, 1993).

²⁷. Nayan Chanda, "Misguided complacency", *Far Eastern Economic Review*, (18 November, 1993), p. 22.

face new tariffs increased from 9-50 per cent.²⁸ The negative impact of withdrawing China's entitlement for the MFN on Hong Kong would cost 43,000 jobs and US\$1.2 billion income in the first year of its enforcement.²⁹

Unquestionably, so far, Deng's efforts for economic reforms have created a favourable political impetus to the formation of the CEA. When Deng Xiao-Ping dies, it is uncertain which way China will go. The major "weakness" which communism has suffered is that there are no rules for the power succession within the Party itself apart from power struggles which may have planted a landmine in the future of China's reforms. There is an unpredictable political scenario ahead. Nevertheless, it is sure that Deng will leave the scene with a strong collective leadership of the reformist mind in place guarded by his reformist "theory" for China's development, and perhaps for the CEA.

6.1.2. Hong Kong: A Hope for Living away from Crisis

Hong Kong's development of its China linkages is not based on political incentives, but rather on historical and practical demands, economic incentives. Unlike Taiwan with regard to China, Hong Kong under British colonial rule, though it has never had democracy, has not been politically restrained, and perhaps actually it is not necessary to concern itself with political issues in developing its relationships with China. Even in Chairman Mao Zedong's self-

²⁸. John P. Burns, "Hong Kong in 1992: Struggle for authority", *Asian Survey*, 33: 1, (January 1993), p. 31.

²⁹. For full discussion of the negative effects to China, and Hong Kong, as well as the US itself see House of Representatives, "Renewal of MFN trading status for the People's Republic of China", Hearing and Markup before the Committee on Foreign Affairs, 102nd Congress, 1st Session, Washington, 26 June, 1991, pp.15-17.

reliant period, Hong Kong was an important trading partner for China. Economically, Hong Kong's position as a middleman for Taiwanese, overseas Chinese, and many other foreign entrepreneurs to link with China, gives it prominence in the formation of the CEA. On the whole, in the formation of the CEA, Hong Kong has been politically in a passive position to be swirled into the focal point of the "Greater China" in contrast to its economic dynamics. Whatever its political reservations, Hong Kong will soon be a Special Administrative Region of China as stipulated in the 1984 Sino-British Joint Declaration, the basis of China's drafting a Basic Law for Hong Kong. According to the Basic Law, China is entitled to appoint the future Hong Kong chief executive and other senior officials. Since the Basic Law ratified by China's National People's Congress in April 1990, people in Hong Kong have been very suspicious of China's bona fides, because Beijing's willingness to pilot Hong Kong's future by its own track has been obvious at the expense of Hong Kong's democratic demands.

During most of China's reforms of the 1980s, Hong Kong increasingly deepened and speeded up its all round ties with China. After passing through a short period of shattered confidence about its future soon after the Sino-British Joint Declaration, Hong Kong regained initiative in its economic dynamics a couple of years later. Since the Joint Declaration left the details of the transition to be negotiated between China and Britain, negotiations beginning in 1988 have so far brought serious disagreement over Hong Kong's system of government after 1997. The present Hong Kong governor, Chris Patten, proposed a constitutional reform in Hong Kong in October 1992, which has provoked a new round of reprimands from Beijing. In his reform proposals, he has tried to alter

the composition of the Executive and Legislative Councils and their relationships to each other.³⁰ As far as China is concerned, the most threatening feature of these reform proposals, which are attempting to put forward a more democratic power base through people's direct election to the Legislative Councils, is not so much in the proposal itself, but in the way of introducing it. Chinese officials respond strongly to the proposals "not because they advance democracy in Hong Kong but because they provide a concrete basis for a struggle over the exercise of authority over Hong Kong during the transition."³¹ The British government alleges that the proposals have been made to comply with the demands by the growing middle class for a more democratic system. For example, the change of the current Hong Kong political system has been regarded by the United Democrats, the first real political party, as a necessary warranty for Hong Kong's autonomy and prosperity under the Chinese reign.

However, China remains very suspicious of the British attempt to speed up Hong Kong's change to democracy just before its return to China, while this had been intentionally ignored by Britain in the past. The distrust has been based on general Chinese Communist Party's perceptions of Britain. Chinese leaders' belief that the main British interest in Hong Kong is to extract large sums of money has beset every round of their negotiations.³² By the end of 1993, the 17 rounds of negotiations have not yet brought the two to compromise over their differences.³³ China continuously criticises Britain for

³⁰. For details see John Burns, "Hong Kong in 1992", pp. 26-29.

³¹. Ibid., p. 27.

³². About Chinese perceptions of Britain, Michael Yahuda's survey has sketched out a general picture of what the British believe. See Yahuda, "Hong Kong's future: Sino-British negotiations, perceptions, organisation and political culture", *International Affairs*, 69: 2, (1993), pp. 252-256.

³³. For the historic review of the Sino-British negotiations see Yahuda's analysis, Ibid., pp. 245-252.

doing little to reach agreement and threatens economic chaos for Hong Kong if need be.³⁴ Governor Patten insisted on pressing ahead with electoral reform regardless of Chinese opposition, and on 23 February 1994, the vote in Hong Kong's Legislative Council showed the margin of support for his reform. As a result, enraged Beijing has stepped up its repudiation of the British action and has pledged to abolish any political arrangements made without its consent. In doing so, China has showed its design for its favoured future political structure for Hong Kong by emphasising the importance of the Preliminary Working Committee (PWC), a group of 57 Chinese officials and Hong Kong plutocrats.³⁵ This confrontation between the two parties has cast a long shadow over Hong Kong's future. In spite of the political disputes obscuring the bright future, Hong Kong's economic links with China have steadily intensified, as many Hong Kong businessmen agree that "economic alliance (with China) will be the best guarantee of future liberties."³⁶

Since Hong Kong has been one of the most private-orientated economies in the world with literally no governmental intervention in a *laissez-faire* system, the Hong Kong government's, in fact the British government's, policy does not direct the colonial business community in any way. In this respect, Hong Kong has remained largely a community of capitalism and open markets. "People generally were satisfied with the administration. Although they lacked self-government Britain provided a rule of law that respected human rights, offered plentiful economic freedoms and maintained social and

³⁴. The economic connection between China and Hong Kong has made this threatening suggestion unlikely to come about. See *The Economist*, (18 December, 1993), pp. 16 and 68-70.

³⁵. *Financial Times*, (25 February, 1994), p. 6.

³⁶. This view has been shared by the Liberal Party, supported by Conservative big business forces, and the Business and Professional Federation. James Walsh, "The ties that bind", *Time*, (21 March, 1994), p. 35.

political stability."³⁷ This means that political developments in Hong Kong itself, particularly the pre-1997 democratic movement, do not happen to be a necessary condition for the Hong Kong business community to develop close relationships with China and Taiwan.

In fact, due to Hong Kong's profit-orientated society, the uncertainty about the pending negotiation between China and Britain has, to some extent, brought about a sense of crisis in doing business with Hong Kong. Therefore, a backfire effect emerges within the business community which is demanding a predictable and stable economic future. Whatever political commitment to Hong Kong's future will come about, it is clear for Hong Kong itself that its last trump to play with China has been establishing an economic grouping. Namely, deepening economic cooperation with China, Guangdong in particular, and Taiwan through trade, investment, and industrial unity, Hong Kong could, thus, bring itself the only hope of maintaining the present prosperity for as long a period as possible. While intensive economic cooperation may be heading towards economic integration between China, Taiwan and Hong Kong, the "three Chinas" could thus find themselves well positioned in a complementary economic structure, i.e.: Hong Kong: finance and service centre; Taiwan: R & D and management centre; and China: manufacturing centre and market.

Pragmatically, Hong Kong can therefore maintain its leading role as a gateway, as it is now, for China's economic development, if Hong Kong is able to pursue successfully the formation of the CEA. It seems very likely that any political compromise brought about by Britain and China could assure Hong Kong's future less than could the firm establishment of

³⁷. Penelope Hartland-Thunberg, *China, Hong Kong, Taiwan and the World Trading System*, (London: Macmillan, 1991), p. 104.

an economic grouping. Two arguments which concern Hong Kong's role in the CEA have been brought to focus on Hong Kong for some time. Firstly, whether full democracy and universal suffrage in Hong Kong after 1997 are really able to guarantee its autonomy away from Beijing, the United Democrats believe that this political issue is a crucial factor if Hong Kong is to retain prosperity and autonomy. Further, they "have attempted to strengthen the accountability of the Hong Kong government through its Legislative Council."³⁸ On the other hand, a pragmatic approach has emerged from the business community which is increasingly shared by people in general in Hong Kong, which has thrown doubt upon any attempt to challenge Beijing's weight over Hong Kong. Instead, the Hong Kong business community, which is more concerned with practical economic performances and their relationships with China, argues that the only common interest between Britain, China, and Hong Kong on shaping Hong Kong's future has been, so far, to encourage Hong Kong's current economic performance to persist.

For example, Linus Cheung, deputy managing director of Cathay Pacific Airways, one of the Hong Kong businessmen optimistic about Chinese rule, has said "[M]y understanding of China's policy toward Hong Kong is that they will be receptive to anything that will further its stability and prosperity. There is no reason to destroy a success story."³⁹ Moreover, the business community suggests that "there is no need to upset China and give Hong Kong democracy, when the colony has thrived without democracy for the past 95 years."⁴⁰ Businessmen in Hong Kong, therefore, would rather acquire a solid ground

³⁸. John Burns, "Hong Kong in 1992", *Asian Survey*, 33: 1, (January 1993), p. 24.

³⁹. Mark Clifford, "Mainland Bounty", *Far Eastern Economic Review*, (27 January, 1994), p. 40.

⁴⁰. Lulu Yu, "Business and democracy compete to shape future of Hong Kong", *The Times*, (31 December, 1992), p. 25.

in economic affairs from China than keep pressing ahead with demands to China for more political concessions. Even the chairman of the British-run Swire Pacific, Peter Sutch, has expressed the same message to that of the Hong Kong business community. He said: "We as businessmen in Hong Kong see our role as continuing to invest here and in China. That is as good a guarantee of future prosperity and stability as anything else."⁴¹ Simply, there is a possibility that whenever China takes Hong Kong under its rule, any political commitment prior to this change could be dismantled. This has been warned time and again by Beijing.⁴² In protesting against the unilateral British proposals for Hong Kong's future political structure, China has not only seriously threatened to abolish any political arrangements made without their consent,⁴³ but has also quickened the pace of preparing for the handover by pushing the PWC to draft an outline of Hong Kong's post-colonial political structure.⁴⁴

As many Chinese government units, enterprises, individual officials, and personal families have profited by means of the links with Hong Kong during the 1980s, they have in growing numbers shared the Hong Kong business community's pragmatic thinking about persistent prosperity. It has been pointed out that "these personal family interests provide some assurance that the Chinese government will not purposely kill the goose that lays the golden eggs that so many influential families have in their personal nests."⁴⁵ To maintain this through existing economic networks of interdependence, Hong Kong, as

⁴¹. Mark Clifford, "Back to China", *Far Eastern Economic Review*, (27 January, 1994), p. 40.

⁴². Lulu Yu, "Business and democracy compete to shape future of Hong Kong", p. 25.

⁴³. *The Economist*, (18 December, 1993), p. 16. and *Central Daily News*, International Edition, (18 December, 1993).

⁴⁴. See Simon Holberton, "Riding to the future on a Hong Kong Harley", *Financial Times*, (14 February, 1994), p. 5.

⁴⁵. Kenneth Lieberthal, "The future of Hong Kong", *Asian Survey*, 32: 7, (July 1992), pp. 670-671.

China's matchmaker, is able to marry China to Taiwan and the rest of the world. Hong Kong's capitalist society will, hence, be preserved, whilst China's interests become increasingly intertwined with transactions with Hong Kong. Likewise, China's "socialist market economy" will be evolving peacefully into a more capitalist market economy.

How important is the democratic system for Hong Kong's free economy? In the past, Hong Kong's economic performances were not based on a democratic system, but rather on an efficient administration. Therefore, there are plenty of grounds for questioning why people in Hong Kong ought now to seek for a democratic system which may unwisely risk a retaliation from Beijing. Will Hong Kong still be as prosperous as it is now after China's "one country, two systems" rule is in place? Nobody seems to be sure about whether a democratic reform in Hong Kong will do anything to help in securing Hong Kong's prosperity. At least, a democratic system based on representing people in Hong Kong could serve as a bargaining chip in balancing Beijing's power, especially, as Beijing has bowed to provincial and local governments in economic policy, as a result of economic reforms in China.

Hong Kong has long been within the British "one country, two systems" context of colonial rule. Politically, Hong Kong has had no parliament and its people could not vote. Economically, "while the British economy was subject to much government ownership, control, and interference, Hong Kong operated a free enterprise, free-trade system that was arguably the most private-sector oriented economy in the world."⁴⁶ Many entrepreneurs, mainly the Business and

⁴⁶. Penelope Hartland-Thunberg, *China, Hong Kong, Taiwan and the World Trading System*, 1990, p. 99.

Professional Federation, and the public have begun to worry that the row between Britain and China may bring a backlash against their future, and they have turned against the governor's new reform proposals.⁴⁷ One entrepreneur states directly that "Hong Kong has never been democratic during 150 years of British rule, and this is not the time to start."⁴⁸

6.1.3. Democratisation and Taipei's Mainland China Policy

Political Reform and the Progressive Mainland Policy

In July 1987, in response to social and economic changes in Taiwan, its late president Chiang Ching-Kuo decided to lift the 38-year-old Emergency Decree, which placed the society in a status of war against communist China. In November 1987, the Taipei government released the policy restraint on Taiwan residents from visiting their relatives in mainland China for considerations of humanity. This has marked a new page in the relationships between China and Taiwan since 1949, the year when "China" became legally divided into "two Chinas". At the same time, the process of democratisation in Taiwan was further strengthened by lifting the ban on newspapers, and the establishment of opposition parties.⁴⁹ Six years on, with Taiwan's political development underpinning the relationships across the Taiwan Strait, the intensifying transactions, which have occurred in economic, social, cultural sectors, and, to a lesser extent, in the political domain (by quasi-official approval) between China and Taiwan, have not only greatly improved their mutual understanding and benefits, but also

⁴⁷. John Burns, "Hong Kong in 1992", 1993, p. 28.

⁴⁸. "Going it alone", *Time*, (13 December, 1993), p. 33.

⁴⁹. *Republic of China Yearbook, 1990-1991*, p. 198.

strongly enhanced their willingness to cooperate with each other in an unprecedented progress.

Although the new relationship with mainland China has boosted a prolonged hope for peaceful unification in both Taiwan and China, it has also stirred up political controversy in Taiwan over acceptance of "one China" or "one China, one Taiwan" between the ruling party, the Kuomintang (KMT) and the opposition party, the Democratic Progressive Party (DPP).⁵⁰ The China ties have long appeared to have a love-hate ambivalence in Taipei's political agenda. While the KMT remains insistent in its claim of sovereignty over China and the hope for national unification, the DPP, once in power, prepares to cut away this Chinese umbilical cord from Taiwan. This would, the DPP assumes, allow Taiwan to get rid of the effect of "one China" thinking on the fundamental problems of Taiwan's constitutional structure and foreign relations.

Since early 1988, the president Lee Teng-Hui, also the KMT's chairman, has included the reform of political life among his approaches to constitutional reform in general and to his reappraisal of the mainland policy in particular. In terms of the mainland policy, the reform's immediate effect has been in accelerating Taipei's policy towards a more practical one. The increasing transactions between China and Taiwan have derived from this. When President Lee took power in early 1988, the major task of the constitutional reform was to allow the re-election of the members of the so-called "eternal congresses" whose original members had not been re-elected in order to maintain the Taipei government's

⁵⁰. "One China", as it is interpreted by the KMT, means the Republic of China which contains Mainland China, Taiwan, and even Mongolia. That is where Taipei's goal for national unification stems from and coincides with China's "one China". The DPP prefers "one China, one Taiwan", which implies that Taiwan will be independent from the "myth" of "one China" to establish a complete new country with the name of the Republic of Taiwan or the like.

legitimacy in China since the first election in 1947 which had been held in the mainland.⁵¹ The conservatives inside the KMT used to claim that those members of the "eternal congresses" represented their constituencies in mainland China which had been occupied "illegitimately" by an "insurgent group", the Chinese Communist Party. The claim, presumably, assisted the KMT not only to stress Taipei's legitimacy over the whole of China but also endorsed the ROC as the only "one China" in international society. From this point of view, any attempt to reform this "distorted" constitutional structure would be blameworthy for breaking China up.

Before the presidential election in May 1990, people demanded the dissolution of the National Assembly, the abolition of the "Temporary Provisions Act", a timetable on Taiwan's political restructuring, and convening a National Affairs Conference to schedule constitutional reform. As the reform continued to be pressed ahead, at the end of 1991, an election based on constituencies in Taiwan was held for new members of the National Assembly. The decision to hold the election has marked an end of an essential element of the outdated political myth on which the Taipei government's constant claims for its *de jure* sovereignty over China has been based. Further, the following year, another general election for the members of the Legislative Yuan was held.

⁵¹. According to the constitution of the Republic of China issued on 25 December, 1945, in the then Capital Nanking, the government structure is composed of five Yuans, Executive, Legislative, Judicial, Examination, and Control Yuans, under the lead of the president indirectly elected by the National Assembly. The "eternal congresses" which included the members of the Legislative Yuan, the Control Yuan, and the National Assembly were seen as a symbol of political legitimacy. In 1969 the first partial election for the new members of the National Assembly was held. The Control Yuan elected two new members in the same year. In addition, in 1975 the first by-election of the Legislative Yuan allowed 52 new members to be elected directly from constituencies in Taiwan. For a brief discussion of the processes of re-electing the "eternal congresses" see *Republic of China Yearbook, 1990-1991*, pp. 110-114, 118-120, 128-130.

While President Lee's reform has brought credit to the government over the issue of constitutional legitimacy, increasing criticism has poured over Lee's intention to pursue a programme of "two Chinas". President Lee, described by the conservatives as pursuing the policy for "Du Tai" which implies withdrawing the claim of sovereignty over the whole of China and at the same time recognising the Beijing regime, has resulted in a split of ideology within the KMT: the Taiwan wing and the "one China" wing, or the main stream and the non-main stream.⁵² However, that does not imply that the "one China" policy has been officially changed in Taipei. Lee's reformist approaches have brought about a pragmatic attitude that has bolstered an effort to establish "one China, two governments" or "one China, two areas", which places the Beijing and Taipei government on equal footings, without risk of changing the existing "one China" policy.⁵³ An official document clearly states that "the ROC government's 'one China' policy is a policy that acknowledges division, promotes exchanges, and seeks unification."⁵⁴

Indeed, Lee's pragmatism in the exercise of these foreign and mainland policies appears to have two profound implications for Taipei's politics. Firstly, his recognition of de facto "two Chinas", based on a nominal "one China", could keep his constitutional reform proposals safe from sharp

⁵². The "Du Tai" criticism claims that the Taipei government will recognise its current effective sovereignty over Taiwan and Kinmen, Matsu Islands only, and be keeping the national name as the Republic of China. In contrast, the DDP's "Tai Du" has tended to establish a new Taiwan Republic. In the "one China" understanding, the Taiwan wing tends to see "one China" means the ROC and recognises the "two Chinas" reality of China's division since 1949. The "one China" wing worries that the passive policy towards unification may lead to a permanent division. For full discussion about "one China" and "two Chinas" policy see Julian Baum, "Parting of the ways", *Far Eastern Economic Review*, (12 November, 1992), pp. 16-18; also "Split in the ranks", *Far Eastern Economic Review*, (24-31 December 1992), p. 25.

⁵³. See discussion in Jürgen Domes, "Taiwan in 1991: searching for political consensus", *Asian Survey*, 32: 1, (January 1992), pp. 45-46.

⁵⁴. See "The Republic of China's 'one China' policy", *Reference: ROC on Taiwan*, RR-92-07, (10 November, 1992).

criticism in his reorganisation of a central governmental structure based on Taiwan itself rather than on its proclaimed constituencies in mainland China. President Lee has been skillful in manoeuvring the reform process while confirming the "one China" policy at the same time. In February 1991, the Guidelines for National Unification were made the guiding principles of the government's mainland policy, which was composed of four parts, i.e.: one unified China; two equivalent political entities on the two sides of the Taiwan Strait; three phases: the short term - exchange and reciprocity, the medium term - mutual trust and cooperation, the long term - consultation and unification; and four principles of reason, peace, parity, and reciprocity.⁵⁵ After the overall re-election of both the National Assembly and the Legislative Yuan in 1991 and 1992 respectively, the president's reform programme with confirming "one China" has not only been able to reduce political intensity in Taipei and between Taiwan and China, but has also indirectly shown up the awkward situation Taipei has had in its policy stand. In this way, the president may have already sown a seed for reform towards further restructuring.

Secondly, the Taipei government has adopted a practical approach which is helping to making up its own say on its international status. In contrast to conventional diplomacy, this has considerably facilitated the country's pursuit of "substantive diplomacy" through economic gears. Since Taipei's diplomacy has long been overshadowed by China's power in international politics, Taipei is not yet able to make its own

⁵⁵. "The Key Points and Content of the Guidelines for National Unification", Mainland Affairs Council, The Executive Yuan, R. O. C., 1991.

way without being intimidated by Beijing.⁵⁶ Although China and Taiwan have brought their stands together on "one China", China places the two of them in a centre-periphery hierarchy, while Taiwan insists on an equal status. In real terms, Taipei's foreign policy is based upon its moving forward of mainland policy. This makes Taipei's decision-making on foreign policy very vulnerable to Beijing's threats. In the case of application for membership of the United Nations, for instance, whatever Taipei's efforts there recently, it seems to be hopeless so far for Taipei to enter through the formal procedure of application, because Beijing's boycott will certainly kill any attempt of Taipei to get access to the UN. (China is one of the five permanent members in the Security Council.) The lesson taught in the case of the United Nations reminds Taipei that it would be very wise, instead, to negotiate directly with Beijing in order to bring the quarrels between the "two Chinas" to a peaceful solution, before any further progress can be achieved. It seems to Taipei that there will be no breakthrough by means of conventional diplomacy before the "two Chinas" issue is first settled. Indeed, for years, Beijing has been trying to redirect Taipei's diplomatic efforts towards direct negotiation between the two ruling parties, the KMT and CCP. Increasing economic transactions between the two in the past few years have made official contacts more likely to come about.

Knowing the difficulty, Taipei's pragmatic approach in adopting the "one China, two governments" formula or a similar one has suggested ways in which to diversify its foreign policy from mainland policy. Although there is still

⁵⁶. For Beijing's blunt and acrimonious charges in this issue see the document, "The Taiwan Question and Reunification of China", by Taiwan Affairs Office & Information Office, State Council, in August 1993, *Beijing Review*, 36: 36, (6-12 September, 1993), documents part.

indifference about "dual recognition" in international politics today due to Beijing's strong objections, Taipei has been the more practical in relinquishing its "one China" insistence in practical diplomacy to accommodate the reality of "two Chinas". This has given Taipei credit in developing new ties with other countries.⁵⁷ For example, on his way to visit Singapore in March 1989 President Lee commented on the Singaporean media calling him "the President from Taiwan", instead of "the President of the Republic of China". He said that although he disagreed with what he had been called, he could still accept it.⁵⁸ Instigated by the president's "summit diplomacy", Taipei has launched a "Southward policy" targeting economic and trade relationships with the Association of South East Asian Nations countries.⁵⁹

Unification? Taiwanese Independence? the Chinese Economic Area?

Apart from economic transactions, there are many indicators such as the rapid increases of numbers of letters exchanged, phone calls made, and tourist visits between China and Taiwan, that have together suggested a general trend of transactions which is very likely to intensify in the present situation. According to the statistics, letters sent from Taiwan to China amounted to 1.98 million in 1988, and hit 6.04 million in 1991. In contrast, letters sent from China to Taiwan amounted to 2.03 million in 1988, and 8.8 million in 1991. While phone calls made from Mainland to Taiwan amounted

⁵⁷. Taiwan's recent major diplomatic breakthrough see "Ancient fears", *Far Eastern Economic Review*, (3 December, 1992), p. 8; "China, Taiwan and hurt feelings", *The Economist*, (19 February, 1994), pp. 73-74.

⁵⁸. See the special report for Lee Teng-Hui's performances in three years presidentship in *Central Daily*, International Edition, (20 May, 1993), and more comments on the president's policy in the press conference see *Central Daily*, International Edition, (22 May, 1993).

⁵⁹. "China, Taiwan and hurt feelings", p.73-74; various reports about President Lee's "holiday diplomacy" in *Central Daily News*, International Edition, (8 February - 18 February, 1994).

to 0.77 million time in 1989, and increased to 8.02 million in 1991, Taiwanese calls made to Mainland amounted to 0.73 million in 1989 and jumped up to 14 million in 1992 (not including December). Taiwanese tourists to China via Hong Kong amounted to 0.43 million in 1988, and 2.8 million in 1991.⁶⁰ In response to mounting pressures from the public in general, and the business community in particular, for regulating the increasing transaction flows between China, Hong Kong, and Taiwan, Taipei has worked hard to ease tension across the Taiwan Strait. This has been recognised as a positive impetus towards improving the relationship between Beijing and Taipei.⁶¹ Particularly, instead of being passive towards China as in the past, Taipei's political stance to Beijing, backed by a series of political reforms at home, has been rather active in initiating programmes. For example, in policy, Taipei's fresh "no winner, no loser" stand in meeting Beijing's "zero-sum" strategy; in practice, institutionalising the contacts between China and Taiwan by setting up the quasi-official Strait Exchange Foundation (SEF).

The substantial increase of contacts has brought about a serious contest between arguments for unification and for independence in Taiwan. Against the political reform context in Taiwan, there is a big question mark over what Taiwan's interest will be in pursuing unification, particularly for those who favour developing links with China. As the KMT carries on the "nativisation" of the leadership with more native Taiwanese emerging on the scene, scepticism about the

⁶⁰. This information is based on the Directorate General of Posts, and the Directorate General of Telecommunication, the Ministry of Communications, R. O. C. for mails and phone calls. About the tourists, the information was estimated by Hong Kong China Travel Agent. See "Lian An Gin Gi Fen Shi Bao Gou" (Economic Analysis Report on Two Sides of the Taiwan Strait), Mainland Affairs Council, Executive Yuan, R. O. C. January 1993.

⁶¹. Peter Wickenden, "Taiwan's bridge to the mainland", *Financial Times*, (30 April, 1991), p. 21. and also "Taiwan clears path for improved links with China", *Financial Times*, (21 May, 1991), p. 6.

Chinese unification is rising not only in the opposition party, but also in the KMT itself. The pragmatic approach in Taipei has taken this potential uncertainty into account by leaving unification to evolve over generations, although the government is still making unification in principle an eventual national goal.

In terms of political belief in Taiwan's destiny, the KMT has been placed in the unification-independence tug of war between Beijing and the DPP. In this respect, Beijing appears to be sharing the KMT's intentions about unification against those of the DPP. Ever since its emergence, the DPP has been continuously advocating self-determination, and pressing the government for a referendum to decide Taiwan's future over independence. Since 1988, there have been some resolutions passed by the DPP advocating independence and acknowledging the separation from China. By the end of 1991 for the critical election of the National Assembly, the DPP's assertion of independence was brought to a new pitch by raising the slogan of "Republic of Taiwan", producing the "Draft Constitution of Taiwan" and staging a public demonstration demanding that government should apply for the United Nations' membership immediately. More controversially in October 1991, the DPP formally adopted the resolution to include the Taiwan independence clause into its party manifesto for the election campaign. That political move was blamed for a sharp plunge of the stock market and of foreign investment in Taiwan.

The gradually bipolarising arguments about unification and independence in Taiwan has worried Beijing a great deal especially as regards unification.⁶² Beijing has on many occasions threatened that it would not hesitate to use an

⁶². Qingguo Jia, "Changing relations across the Taiwan Strait: Beijing's perceptions", *Asian Survey*, 32: 3, (March 1992), p. 283.

"adequate means" other than a peaceful one to "unify" Taiwan if Taiwan would ever dare to declare its independence. In reality, the claim for Taiwan's independence risks immediate retaliation from China and is prejudicing Taiwan's national interest prematurely. This could further jeopardise Taiwan which is already in danger in respect of its international status. At present, economic, political and social circumstances between Taiwan and China are at a far too premature stage to solder together unification. The pursuit of either immediate unification or independence will clearly bring nothing but disaster to Taiwan's well-being. For Taipei's decision-makers, the status quo policy which allows the incremental approach to take place gradually remains the most favourable.

In 1991, the KMT won 71.17 per cent of the vote and 254 out of 325 seats in the National Assembly election. The message sent by the public was clear and warns that the extreme activists for Taiwan independence can find little place in Taiwan. The radical argument over unification and independence calmed down as a result. In terms of insistence on unification, the DPP has been criticising the government for playing the "Beijing card" at the expense of the people's interest in Taiwan. Indeed, there has been a very tricky scene between Beijing, the KMT and the DPP over the issue of unification and independence. While the KMT accuses the DPP of risking the country's fate, Beijing always joins in with condemnation of the DPP for committing a "national crime" in attempting to separate Taiwan from China. As far as the KMT is concerned, whatever the arguments between Beijing and the DPP, each of them serves just as a policy "balancer" to the other in Taipei's politics.

For the Taipei government, national unification is far from practical because of the current political stalemate between Taipei and Beijing. Taipei's reformists in favour of the status quo policy are seeking to expand economic links with China. A practical approach to this is leading strategically to a context of more secure cooperation between the "two Chinas" which circumvents possible political clashes, before acceptable working arrangements for harmony of some sort could be reached. President Lee proposed in 1990 the complete opening up of academic, cultural, economic, trade, scientific, and technological exchanges as a foundation for mutual respect, peace and prosperity.⁶³ These proposals have improved the circumstances for the concept of the CEA which the KMT has continued to develop according to opportunity.

6.2. THE CHINA-TAIWAN POLITICAL STALEMATE

The concept of the CEA appears to be the most important grand design for proceeding to economic integration and then to Chinese unification. Thus, the CEA could be regarded as an early step towards economic integration which has been brought about by the transactions between the "three Chinas", Hong Kong, Taiwan and Mainland China. Although in general the CEA itself has been widely considered to be a process of economic integration, without doubt its formation has always been accompanied by political considerations about the possibility of unification from which brakes to economic integration have derived. Because of the different definitions of the meaning of Chinese unification, both Taiwan and China in progressing

⁶³. Peter Wickenden, "Taiwan clears path for improved links with China", *Financial Times*, (21 May, 1990), p. 6.

towards the CEA have inevitably been distracted by persistent arguments about "Chinese sovereignty" that have shaped their relationships for decades. The political dead-end between the two has derived from their both claiming the "one China" policy. In both Taipei and Beijing's view, Taiwan is an inalienable part of China according to history. However, China (People's Republic) asserts that its "inarguable" sovereignty should include Taiwan, as Beijing has become the representative of "China" in international society, since it took over power from the KMT's Nationalist government in 1949. In spite of the irrationality of its claim of sovereignty over Taiwan which in fact has never been in many way ruled by Beijing's regime, Beijing's assertion that "the PRC is the true and only one China" has resulted in Taiwan's international status being at issue for some considerable time.⁶⁴ According to Beijing, the relationship between Beijing and Taipei has therefore been defined as a "domestic affair".⁶⁵

Against this, Taipei's realistic approach of "one China, two political entities" which is placing Beijing and Taipei on the relationship of a "quasi inter-governmental" one, has not yet caught international attention. While China perceives that Chinese unification is based on the process of "peaceful unification" and the framework of "one country, two systems" according to which Taiwan would be "incorporated" into China as a special administrative region, Taiwan asserts that in the process of national unification Taiwan ought to be respected as an independent political entity so that the two could start

⁶⁴. The question of China's representative was in favour of Taipei (Republic of China), until China got into the UN in 1971. For China's stand on unification see the most recent Beijing declaration on "The Taiwan Question and Reunification of China", by Taiwan Affairs Office & Information Office, State Council, in August 1993.

⁶⁵. Ibid.

the process of unification at an equal level.⁶⁶ As usual, although China's policy towards national unification is a peaceful one, it has never been too gentle to remind others that:

"[H]owever, any sovereign state is entitled to use any means it deems necessary, including military ones, to uphold its sovereignty and territorial integrity."⁶⁷

Notwithstanding political barriers, transactions between the three towards economic integration have been continually intensifying. It is important to note that while the economic integration that has happened in the rest of the world has been led by political motives, business-led economic cooperation in the CEA is gradually forming itself and then passing on practical problems to political authorities for resolution. It is also clear that the respective governments in the CEA have been surprisingly inactive in the progress of grouping, in comparison with governmental commitment to integration elsewhere. Clearly, the historic enmity overshadowing relations between Beijing (communism) and Taipei (capitalism) could be the main factor imposing an unbalanced relationship in which China impels all the countries of the world to comply with its "one China" policy of downgrading the political status of Taipei. However, the CEA's contributions to regional economic integration have been enormous especially against the context of political confrontation. It may further

⁶⁶. For Taipei's response to Beijing's declaration see the Mainland Affairs Council's declaration of "There is only 'China question' and no 'Taiwan Question'" on 16 September, 1993. Also an article by Lien Chan, the Prime Minister of the Republic of China on Taiwan, "The Republic of China on Taiwan Belongs in the United Nations", *Orbis*, 37: 4, (Fall 1993), pp. 633-641.

⁶⁷. See the Beijing's declaration on "The Taiwan Question and Reunification of China".

suggest that industrial development has been one of the major factors behind the advance towards economic integration.

6.2.1. Political Stalemate Contributes to Distorted Transactions

In practice, efforts for economic integration through the CEA are not based upon political intentions, but upon the result of economic transactions. Whether national unification will come about as a result of economic integration, is as yet uncertain. It is more realist to assume that the creation of the CEA is being driven plainly by economic integration in current political circumstances. There is reason to be very cautious about the contradiction between the actual development of the CEA and the existing obstacles to cooperation, because those obstacles, linked to political hostility between Taiwan and China in most cases, will bar all prospects of deeper engagement to integration. In fact, this remains the main reason why the present and future development of the CEA has been in doubt especially in comparison to projects for regional economic integration elsewhere. The conditions for approaching the process of economic integration have been inequitable and distorted by being intertwined with the political intractability of the "one China" myth in relation to which Beijing's and Taipei's policies have evolved. Until now, direct business links between Taiwan and China have not yet been officially and legally permitted by Taipei. The "indirect trade", which was announced in July 1985 with the "three no's" principle⁶⁸ and only allowed trade with

⁶⁸. The "three no's" of indirect trade were set for "no direct trade with China, no contact with Mainland Chinese officials, no governmental intervention on businessmen contacting

China directed through any third party, (Singapore, Japan, and, to a larger extent, Hong Kong), is characterised by the political expediency of the Taipei government. Because of the fear of Chinese aggression, in taking account of its national security, Taipei has little choice but to limit the free exchange of production factors, including capital, goods, services and personnel.⁶⁹

Although there is a strong demand for free exchange of the production factors with which the economic integration of the CEA is concerned, the importance given to economic factors in Taipei's China policy has lagged far behind political considerations. The distorted transaction patterns of trade and investment between the economies has lasted for some time, as Taipei's renunciation of the "three nos" policy has been subject to Beijing's good will. Under the existing policy framework, Taiwan's trade with China has unnecessarily increased the cost of business because of the need to pass through the "third place" with more customs and shipping delays. Nevertheless, with mounting pressure from the business community to maintain competitive advantage, the Taipei government has been keeping one eye open to the possibility of more liberalised trade with and investment in China.⁷⁰

Since 1991, a number of developments have stimulated a second wave of investment in China. Firstly, in March 1991, government policy allowed business investment projects in China to be legalised through registration and legal

for indirect trade". See *Economic Yearbook for the Two Sides of the Taiwan Strait 1992*, (Taipei: Chung Hua Institution for Economic Research, 1993), p. 343.

⁶⁹. K. L. Kao, "Lian An Gin Mou Shien Kuan Yu Zhan Wuang", (Recent economic and trading situation and prospects between the two sides of the Strait), Mainland Affairs Council, Executive Yuan, R. O. C., (March 1993).

⁷⁰. S. C. Su, and S. M. Chen, "Yiu Gi Chan Chieh Su, Chien Kuei Chan Kai Shih", (As the guerrilla battle is over, the war begins - The second wave of China fever for Taiwan's businessmen), *Business Weekly*, 182, (19 May, 1991), p. 19.

application procedures from the Ministry of Economic Affairs.⁷¹ Secondly, the Beijing visit of the then Secretary-general of the newly founded SEF, Charng-Ven Chen, facilitated a consultation framework to settle problems caused by increasing contact between China and Taiwan, and broke through their cold relationship to establish a working context with its Chinese counterpart, Association for Relations Across the Taiwan Straits (ARATS). Finally, the National Assembly in Taipei revised the national constitution to end the state of war with China.⁷²

Although more industrial sectors have been allowed to set up in China with the government's help in registering in Hong Kong or Singapore to fulfil the legal requirement of "indirectness", the policy has not yet been changed for the purpose of promoting more complete economic integration. In terms of economic integration, trade development between all parties has been based on reciprocity in order to allow the formation of certain exchange mechanisms to undertake cooperation over investments and industries. Once again, political obstacles are to the fore. For Taipei, the relations with China always have to take account of the island's security. In comparison, Beijing's ever closer movement towards Taiwan is intended to pave the way for eventual unification. According to the Taiwanese government, more Chinese economic incentives to welcome Taiwan's enterprises will bring about two effects. Firstly, through relocating various industries in China, Taiwan's economic basis will be hollowed out completely and so become dependent upon the Chinese market. Secondly, once Taiwanese entrepreneurs have

⁷¹. See *Economic Yearbook for the Two Sides of the Taiwan Strait 1992*, p. 346.

⁷². Peter Wickenden, "Taiwan moves to end 'state of war'", *Financial Times*, (2 April, 1991), p. 4; also his "Taiwan's bridge to the mainland", *Financial Times*, (30 April, 1991), p. 21.

relocated in China, they are very likely to become the pawns of Beijing to press Taipei's decision-makers for more favourable policies through their interest groups in Taipei.⁷³ In addition, many in Taiwan cannot easily forget their impressions of communist aggression and worry that "the more money they invest in China, the more vulnerable they will be to manipulation by the Chinese government."⁷⁴ But, however loud the arguments for and against its China policy, Taiwan is steadily advancing towards China, economically, socially, and perhaps soon politically, at least for the purposes of economic cooperation, if not for unification.

However, this represents merely a one-sided story. Many of Taiwan's entrepreneurs have, to some extent, been acting as middlemen between Beijing and Taipei. Entrepreneurs have also been influencing economic and industrial policy in Taiwan and more recently in China. For example, C. Y. Kao, the chairman of President Food, to facilitate investment in China, has convinced the Beijing authorities to allow foreign investors to acquire raw materials in China itself, this has meant that his company has been permitted to set up a ketchup factory in Xingjiang Province with access to local tomato farms. His large scale investment in China came only after Taiwan's policy altered in his favour, for which he had lobbied the government for some time.⁷⁵ Kao is more eager to make sure that policies on both sides of the Taiwan Strait are always

⁷³. These perceptions were mainly gathered from a series of interviews with Taipei's officials whose works have been linked with Taiwan's China policy, taken in Taiwan in July and August 1993. However, they are not in agreement with those of businessmen and related officials in the Ministry of Economic Affairs who have been much more in favour of developing economic links with China. Although these views could apparently be regarded as conservative, in various surveys the public support the argument for further removal of restrictions in relations with China, as suggested by the United Daily's survey in October 1988 stating that direct trade with China was favoured by 38% and opposed by 27% in a sample of 911. See K. L. Kao, "Lian An Gin Mou Shien Kuan Yu Zhan Wuang", (Recent economic and trading situation and prospects between the two sides of the Strait), p. 64.

⁷⁴. "Twixt handshake and armlock", *The Economist*, (22 May, 1993), p. 73.

⁷⁵. See *Business Weekly*, (19 May, 1991), 182, pp. 30-31.

favourable to his business, in order that he may achieve his ambitions to create the number one food enterprise in the world, and has made a good start in offering products to over a billion consumers in China. Furthermore, there is an increasing optimism that once the direct links between all three economies, namely China, Taiwan, and Hong Kong, are further developed, the rate of economic and industrial growth will increase which will strengthen the prospects for economic integration. Therefore, for the sake of economic integration, political barriers will have to be torn down as soon as possible.

A number of scholars have pointed to the obstacles which will hinder the progress of economic integration in the CEA. For example, Huang-hsun Chin stresses that the different economic systems between China's planned economy, and Hong Kong and Taiwan's export-led economies have made the CEA as a comprehensive economic integration an unrealistic hope. P'ei Lu argues that the industrial division of labour between Taiwan, Hong Kong, and China has only been a vertical one rather than a mixture of different types of industries. Ts'un-I Yin states that in terms of trade and technology among the three, they rely more on foreign markets than on each other's market for imports and exports. Moreover, Charng Kao believes that the differences in economic structure between China, Hong Kong and Taiwan serve as an impediment to the formation of any regional economic community.⁷⁶ In reflecting the reality of economic links that occur in the CEA all the differences have been significantly narrowed down in the past few years.

⁷⁶. All above scholars' arguments about the obstacles to the CEA were derived from a survey of the literature by Charng Kao, "A 'Greater China Economic Sphere': reality and prospects", pp. 57-58.

Nevertheless, political factors remain the biggest obstacle to the future of the CEA.

To avoid political stalemate, many scholars in Taiwan tend to be pragmatic about the CEA and to suggest that attention be concentrated on the development of business links which, over time, will eliminate the obstacles to economic integration.⁷⁷ One scholar points out that because of the European experience of integration, national economic development, and social and political relations will have to be cooperative in order to make progress towards regional economic integration.⁷⁸ The efforts to create the CEA do not have to focus on establishing organisations at the current stage. More practical work should be attempted to accelerate economic development, and thereby dilute political hostility.

6.2.2. The Origin of the Unequal Relationship: the Common Insistence on "One China"

Political confirmation of regional integration by governmental agreements and the establishment of transnational institutions has been assumed to be a prerequisite of integration elsewhere. Nevertheless, the CEA seems to be pursuing a different track of integration which does not involve the signing of agreements, the establishment of transnational institutions, and, above all, the obtaining of governmental endorsement. Whilst China and Taiwan are still officially antagonistic towards each other, integration between them has been increasing in step with their fast

⁷⁷. Ibid.

⁷⁸. Tai-Yin Liu, the then Chairman of Taiwan Economic Research Institute, Taipei, has appealed for more constructive relations between the three economies. See L. C. Wang, "Tai Shang Da Lu Tao Chi Shih Nien Hue Koo", (A retrospection for a decade of Taiwanese Mainland China investment", *Management Magazine*, 218, (August 1992), p. 100.

growing economies. Notwithstanding this optimistic development, the CEA's future clearly depends on political cordiality between both sides.

In 1949, the de facto "two Chinas", the People's Republic of China (PRC-Beijing) and the Republic of China (ROC-Taipei), were established on both sides of the Taiwan Strait as a result of the civil war between the Communist and Nationalist Governments. A duel between both governments has been pursued ever since. In the 1950s, China's "blood-bathing Taiwan" policy, had led it to a few failed assaults on Kinmen and the Matsu Isles, reflecting the intense confrontations which accompanied the Cold War international system. Endless confrontation between China and Taiwan has been repeatedly manifested not only in the pursuit of diplomatic recognition from foreign countries but also over membership of international organisations.⁷⁹ The problems of the "China representative" were conspicuous both in the history of the United Nations and international politics.⁸⁰ In these, an inferior international position has always been awarded to the loser in the context to gain recognition - earlier to the PRC but later to the ROC. Joined with the Cold War crusade against communism, in the 1950s and 1960s, the ROC was able to mobilize its allies to support its "one China" policy and to claim its overall sovereignty over China to block the PRC.⁸¹ Indeed, this achievement was subject to the American "containment" policy towards communism. The objective at that

⁷⁹. For details refer to Fu-Kuo Liu, "The Problems of Participating in International Organisations Facing the Republic of China, Since 1971", a MA Dissertation of Graduate School of Diplomacy and International Law, National Chengchi University, Taipei, January 1987.

⁸⁰. About the UN's voting on the "China representation" question and its implications for international politics see Kuo-Chang Wang, *United Nations Voting on Chinese Representation*, (Taipei: Institute of American Culture, Academia Sinica, 1984).

⁸¹. Joseph Frankel described this situation in China as a sort of confusion between legal status and actual independence. See Frankel, *International Relations In a Changing World*, 4th edition, (Oxford: Oxford University Press, 1988), pp. 20-21.

time pursued by the United States as champion of the ROC was to exclude the PRC from participating in the UN, and to enable the ROC to claim its legitimate right to represent all Chinese people. As part of its campaign to contain communism globally, the United States had mobilized all its policy instruments with the nonrecognition policy in order to block the PRC's access to world organisations.⁸² However, as the United States in the early 1970s was pursuing a new policy of US-China rapprochement with a view to ending the Vietnam War and reducing US-Soviet confrontation, the effort led to restructuring the global balance of power system, from a bipolar to multipolar system.⁸³ In 1971, Henry Kissinger's secret trip to Beijing not only accelerated the change of US foreign policy towards China, but also brought about a new era of the triangular global power structure between USA, the Soviet Union, and China.

As a result of the United States' change of policy, the ROC, in 1971, lost support in the voting at the meeting of the UN General Assembly that year. The PRC, claiming to be the only and legitimate government of China, took over all privileges that the ROC had had in the UN, notably a permanent seat on the Security Council, and a seat in the General Assembly, as a result. This change was a threshold of the PRC-ROC confrontation in the PRC's favour. As a result, Taipei's diplomacy since then has fallen into a "blind-spot" of international society with diplomatic recognition from usually

⁸². For an exhaustive study of the US global containment policy against communism and its campaign to bar the PRC from international recognition see Lung-Chu Chen, and Harold D. Lasswell, *Formosa, China, and the United Nations: Formosa in the World Community*, (New York: St Martin's Press, 1967), pp. 20-33.

⁸³. Kissinger's secret trip sparked the momentum of the new American China policy towards Beijing. See Akira Iriye, *China and Japan in the Global Setting*, (Cambridge, Massachusetts: Harvard University Press, 1992), pp. 122-123.

less than thirty foreign countries.⁸⁴ Because both Beijing and Taipei insist that there is only one China, a diplomatic relation with either China involves a choice as to which is the legitimate government of China. Because of international realpolitik, most countries have selected the PRC as the true "China". In 1979, the United States shifted its "China recognition" to Beijing, Beijing claimed this as its biggest win over Taipei in the diplomatic bids to represent the true China. China's policy of "forced liberalisation" has since then been toned down a little to "peaceful liberalisation".⁸⁵

In fact, since 1949, as Beijing and Taipei, have been pursuing the "zero-sum" policy towards each other, the two Chinas have been the victims of their insistence on the policy of "one China" in terms of their diplomatic gains or losses, according to which diplomatic recognition to one of them has always been accompanied by repudiating the other. Most recently, Saudi Arabia in 1991, South Korea in 1992, and Liberia and Lesotho in 1993 shifted their "China recognition" from Taipei to Beijing; Niger in 1992 and Burkina Faso in 1994 shifted to Taipei, as a result of "one China" policy. In this respect, the implication of "one China" policy has been attempts to downgrade the other's state status.⁸⁶

⁸⁴. At the end of 1993, the number of diplomatic recognitions from third countries adds up to 28. In February 1994, the ROC signed a new friend, Burkina Faso, which has brought the number to 29. *Central Daily News*, International Edition, (4 February, 1994).

⁸⁵. The "force liberalisation", which proposes to use force for the national reunification with Taiwan, has long been the core of China's policy towards Taiwan, although recently Beijing's tone has moderated. The "peaceful liberalisation", announced by Yeh Chien-Yin, the then President of National People's Congress, was composed of the "nine points of peaceful suggestions" with the principles of "Shan Ton, Shi Liou" (three communications and four transactions).

⁸⁶. Before 1991, Taipei regarded the Beijing regime as "banditry". Part of Taipei's foreign policy was preventing the PRC from obtaining diplomatic recognition in international society. Nowadays, after the modification of its national constitution, Taipei has recognised the PRC as a political entity. However, Beijing has never yet softened its high profile policy to downgrade Taipei's international status to be recognised as its province.

The real problem between Beijing and Taipei is the quarrel about "governing" and "reigning" from which Beijing's current policy towards unification, the so-called "one country, two systems", has stemmed. According to Taipei, since the May 1991 ending of its war state with the PRC, the ROC has recognised the PRC as another political entity in China. Therefore, there are two governments sharing the sovereignty of "one China". However, only one sovereign government in China is allowed under the current international legal system. In response to the two Chinas reality, Taipei has appealed to have equal recognition of the two in international society and to continue to govern its existing territories before national unification occurs.⁸⁷ But, being influential in world politics, Beijing is inclined stubbornly to deny the reality of "two Chinas", so Taipei's suggestion has been denounced as the partition of China.

The problem of "one country, two systems" was addressed by Deng Xiao-Ping in 1984, when he suggested resolving the Hong Kong and Taiwan problems within a framework of unification, following the communique between China and Britain about Hong Kong's future. The concept, which became the top policy guideline of China's unification strategy, was linked to the earlier 1979 "peaceful liberalisation".⁸⁸ The concept is to be a tentative framework for unification, and is part of China's commitment to allow Hong Kong to remain a capitalist economy within a wider communist framework - in Beijing's term: a socialist economy with a Chinese character. China's ultimate target is unification with Taiwan. In sum,

⁸⁷. A report, "ROC's Foreign Relations and Diplomatic Administration", published by Ministry of Foreign Affairs in December 1992, has recorded ROC's foreign policy in detail. The report was summarised in *Central Daily News*, International Edition, (28 January, 1993).

⁸⁸. See "Deng Xiao-Ping Taen Lian An Kuen Si", (Deng Xiao-Ping talked about the relationship between the two sides of the Strait), *Central Daily News*, International Edition, (5 November, 1993).

according to Deng, "one country, two systems" within the PRC will allow mainland China to continue its communist system and Hong Kong and Taiwan to preserve their capitalist systems.⁸⁹

Taipei so far officially continues to claim its sovereignty over the whole of China (even including Mongolia),⁹⁰ although many pragmatists in Taiwan criticise the government's insistence on maintaining its existing policy on China as ridiculous.⁹¹ In practice, in foreign relations, Taipei has been more willing to represent where it currently rules rather than where it might have ruled, which could be in effect leading to "two Chinas" as a result. Whether to realise "two Chinas" as a fact, with the abandonment of the goal of national unification or Taiwanese independence without bothering over the China connection, has become a question over national identity, above all between the KMT and the DPP, in domestic politics.⁹² By way of contrast, Beijing asserts that there is only one China, the PRC, and Taiwan is a province of China. If Taiwan decided to challenge this strong stand by moving away from China towards an independent Taiwan, Beijing warned on many occasions that it would not hesitate to use force to check this. Therefore, Beijing has sought to

⁸⁹. Ibid.

⁹⁰. The Nationalist government announced the invalidity of the 1946 Sino-Soviet Friendly and Mutual Assistance Treaty through which China formally recognised Mongolia as an independent country, as a result of the Soviet Union's violation of the friendly spirit of the earlier treaty. A few conservatives inside the KMT still believe that in order to reserve a right to reclaim it in the possible future either through the International Court of Justice or whatever means, it should be considered to be a pre-emptive allegation of which the independence of Mongolia has not yet been completely agreed in terms of legality.

⁹¹. There are plenty of people in Taiwan who disagree with the government's "one China" policy. The younger generations and the supporters of the opposition, Democratic Progressive Party, based on a "Taiwan independent" policy, with no inherited nostalgia for the mainland, have asked for the abandonment of the one China illusion and to admit the reality of "two Chinas". For the opposition party, abandoning "one China" implies that Taiwan is to be an independent country without bothering about the China problem any more. See "The survey - Taiwan: on the move", *The Economist*, (10 October, 1992), p. 2. The argument of "one China" has even split the KMT. See Julian Baum, "Parting of the ways", *Far Eastern Economic Review*, (12 November, 1992), pp. 16-18; Baum, "Split in the ranks", *Far Eastern Economic Review*, (24-31 December, 1992), p. 25.

⁹². Ibid., p. 7.

convince others that it reigns over Taiwan, although it has never governed it. One can, thus, identify two different perspectives. China is always trying to downgrade Taipei's international status as a fully independent country. The downgrading of Taipei is a part of its strategy of "one country, two systems". One scholar of Taipei points out that the term "one country, two systems" might be agreeable if there was not a conflict over who should be the central and who should be the local government.⁹³

Throughout most of the 1980s, diplomatic battles spilled over to international organisations, both inter-governmental and non-governmental. Because Taiwan's economic miracle has reinforced the government's confidence in diplomacy, "substantive diplomacy" has emerged as a pattern for developing its diplomatic relationships through informal, unofficial and economic means with those who retain diplomatic relationship with Beijing, in order to break through China's "besiegement".⁹⁴ It is possibly on account of Taiwan's strong economic performance that many countries cannot ignore Taiwan, finding ways to exchange "quasi-official" offices with Taiwan.⁹⁵ As a result of other countries succumbing to China's strategy of downgrading Taiwan, Taipei's representatives at

⁹³. Fuldien Li, "The legal structure of the "one country, two system" policy and its impact on reunification of China", paper presented in "The Relationship Between Two Sides of The Taiwan Strait For the Twenty First Century", Yale Association For The Relationship Between China and Taiwan, Yale University, (2-3 April, 1993).

⁹⁴. As Taipei decided to adjust its policy stand over diplomatic recognition, "substantive diplomacy", or "flexible diplomacy", a "self-conceded" policy, has operated, where unofficial relationships become more prominent than conventional official relations through mainly economic means, including foreign aid, and investment, accompanied with other economic development cooperation. In traditional international law, one country has only one government to which diplomatic recognition and international obligation are accorded. Taipei's authority has been undermined for its lack of international recognition.

⁹⁵. Taiwan's exchange of representatives with foreign countries has been kept low profile in order not to provoke China. The quasi-official offices appear in various expedient nomenclatures, e.g. Taipei Representative in UK (London) vs. Anglo-Taiwan Trade Committee (Taipei) for ROC-UK; Coordination Council for North American Affairs Office vs. American Institute in Taiwan. See *Republic of China Yearbook 1991-92*, (Taipei: Kwang Hwa Publishing Company, 1992), pp. 233-236; also "The survey - Taiwan: on the move", p. 7.

international organisations have been forced to be known not as those of the ROC, but under other nomenclatures, such as "Taipei, China", in the Asian Development Bank (as a model to be used in inter-governmental organisations) and "Chinese Taipei" in the International Olympic Committee (as in non-governmental organisations).⁹⁶

China's assault on Taiwan's international presence has not eased off at all regardless of their intensifying economic relations in recent years. For example, Beijing has obtained recognition from Riyadh (Saudi Arabia) and Seoul (South Korea).⁹⁷ This recognition angered Taipei greatly. Although Beijing has been suggesting on many occasions that it is more amiable towards Taiwan in order to promote economic exchanges and its economic development,⁹⁸ yet nothing has been solved in respect of its insistence on its high political profile. Due to China's reluctance to alleviate its political pressures on Taiwan, the transaction between them has been officially an unequal one, which has slowed down economic integration in general, and the talks about unification in particular. Whilst China regards talks between Beijing and Taipei as "domestic affairs" to be based on negotiation between both ruling parties, the Chinese Communist Party and the KMT, Taiwan views them as a series of international negotiations between the governments of Beijing and Taipei or at least between two equals. In the former scenario, China is dealing with Taiwan

⁹⁶. In 1985, when China participated in the ADB for the first time, the ADB authority accepted the representative from Beijing as "China", the ROC, previously China's representative in the organisation was forced to be renamed as a result of the preliminary negotiations between Beijing and the ADB, albeit Taipei protested strongly. For the details of China membership in the ADB see Fu-Kuo Liu, "The Problems of Participating in International Organisations Facing the Republic of China, Since 1971".

⁹⁷. For details see the special report by the Ministry of Foreign Affairs, ROC. According to the report, China is still trying to exclude the ROC from being present at international organisations, at the moment of its improving economic relationship with Taiwan. A summary can be found in *Central Daily News*, International Edition, (22 March, 1993).

⁹⁸. Dennis Van Vranken Hickey, "China's threat to Taiwan", *The Pacific Affairs*, 5: 3, (1992), p. 255.

province, as a talk between central government and local government, which Taiwan rejects. In the latter scenario, the attempt of Taiwan to treat China (the PRC) as another equal "government" has been sharply criticised by Beijing as Taiwan "intriguing" with the "two Chinas" concept in international society to transform the China question into an international affair. China's nightmare has been that a concession to the "two Chinas" concept could lead from the de facto division of China, the PRC and ROC, to the division de jure, which will certainly shatter Beijing's hopes for national unification. This persistent obstruction from Beijing almost kills off any effort of Taipei to be a full member of the international community, as exemplified by membership of the UN.

In short, politically there seems to be a lack of contact between China and Taiwan, at least at the moment. Most recently, the SEF and the ARATS, on behalf of their own governments, have been developing their contacts in dealing with "functional and technical" matters across the Taiwan Strait. More regular meetings have been called over various problems, such as smuggling, the arrangement for repatriating smugglers, and hijacking. The first Koo-Wang meeting in Singapore in April 1993 focused on three major topics: setting up systematic channels of communication, increasing economic cooperation, and promoting exchanges in culture, education, science, and technology.⁹⁹ In the meeting, the Chinese representative also announced its basic stand on economic cooperation across the Taiwan Strait as follows:

⁹⁹. Tang Shubei, vice chairman of the ARATS, told the press conference before the meeting about the major focuses. "Wang-Koo meeting to be held in Singapore", *Beijing Review*, (26 April-2 May, 1993), p. 7.

"[T]he mainland and Taiwan should work together towards the same goals and for mutual benefit, achieve common prosperity and rejuvenate the Chinese nation. In the current stage, relations between both sides of the Taiwan Strait should focus on economic exchanges and cooperation. Political differences should not impede economic cooperation."¹⁰⁰

This is how Beijing and Taipei are supposed to be treating their different basic political and economic stands. Indeed, the diversity of policy seems to be coming up only in the contacts of these two "civilian organisations", as the increasing economic, social, cultural transactions have drawn both sides' attention to more practical matters.¹⁰¹ At governmental level, before Beijing tones down political pressure and military threat to Taiwan, there will not be a full scale free exchange between China and Taiwan. With respect to the economic advance and its national security, Taiwan, after all, has got few cards to play, apart from its economic strength.

Although China is concerned with improving the economic strength of the Chinese nation, it did not state any cordial possible political plan, but tried instead merely to press its intention of developing direct exchange of mail, trade, and air and shipping services to Taiwan.¹⁰² That suggestion of establishing direct links at the Singapore meeting was immediately criticised by Huang Kun-Huei, Chairman of the Mainland Affairs Council, a ministerial level institution of

¹⁰⁰. *Summary of World Broadcast*, FE/1675, (29 April, 1993), p. A1/1.

¹⁰¹. The SEF and the ARATS basically are two organisations authorised by their own governments, so that both governments can pass their messages to each counterpart through these two agents. This special arrangement is also in compliance with current policy in their political stalemate. The term "civilian organisations" is in use in Taipei official circles.

¹⁰². In the first discussion of the meeting to be limited to the field of functional issues, Wang Daohan, chairman of the ARATS, raised the intention of direct links across the Taiwan Strait which was considered by Taipei as a sensitive political matter, and was rebutted by his counterpart, Koo Chen-Fu. *Central Daily News*, International Edition, (28 April, 1993).

mainland policy-makers in Taiwan. He rebutted China's suggestions as intentionally bringing up political issues to fish in troubled water.¹⁰³ To encourage direct links across the Strait, Taipei has become more anxious about a positive response from Beijing with regard to its renunciation of the use of force for unification, treating Taiwan as an equal, and allowing Taiwan to enter international organisations.¹⁰⁴ Economic integration of the CEA will depend upon Beijing's softening its high profile political stance.

Against the backdrop of this political constraint businessmen from Taiwan have been bravely penetrating into China's economic activities, though they have been largely seeking nothing but business advantages. These entrepreneurs have been not only spreading economic initiatives for growth, but also establishing frameworks for economic integration. Economic reform in China has brought about economic development and, to some extent, changed its backwardness as an agricultural economy, especially in the coastal provinces. As the basis of industrial development between China, Taiwan and Hong Kong has been expanding much deeper and wider in terms of various industrial sectors, so the forward progress of the CEA is advancing at an appropriate pace regardless of the warning signals of politicians.

6.3. CONCLUSION: THE IMPACT OF POLITICAL DIVISION ON THE CHINESE ECONOMIC AREA

In the theory of integration, political involvement is critical for a group of states basing themselves on a common

¹⁰³ *Summary of World Broadcast*, FE/1675, (29 April, 1993), p. A1/6.

¹⁰⁴ "The survey - Taiwan: on the move", p. 17.

hope for prosperity through government agreements, co-operating together to apply agreed regulations and to reserve advantages for themselves.¹⁰⁵ According to economic integration theory, when there appear to be increasing economic links between a group of economies resulting from the trade creation effect, grouping is more likely to come about. From the theoretical arguments, the only question lies on how far these economic groupings can go without political motives. The effect of trade creation contributes to the original impetus towards economic grouping. It is industrial development based on division of labour that brings regional economic grouping alive, even without political endorsement.

In the CEA, concern about weakening competitiveness has led businessmen and industrialists from both Taiwan and Hong Kong to rush into China to invest regardless of the risk of political instability and hostility. A trade creation effect, which enhances Chinese economic development and revitalises many labour-intensive industries in Hong Kong and Taiwan, has been clearly based on economic complementarity between China, Taiwan and Hong Kong. Without being initiated by the related governments, business flows, trade, investment and finance, as well as some active industries have increased and contributed towards the formation of the CEA. An economic grouping in the CEA through the efforts of the private sectors has shown that the demand for economic development and its processes can be an important incentive to economic integration in the region. Indeed, many studies have discovered that economic integration in less developed countries (LDCs) is seen as a likely way or instrument to bring about the economic development of whole regions. For example, Jaber summarises arguments of limited

¹⁰⁵.A. El-Agraa, (ed.), *International Economic Integration*, (London: Macmillan, 1988), p. xiii.

traditional theory relating to regional integration in LDCs as follows:

"Economic integration in case of LDCs should be treated as an approach to economic development rather than as a tariff issue. Accordingly, it combines various aspects which could improve the international trade position as well as raise the level of economic development of LDCs."¹⁰⁶

Penaherrera argues that one of the "principal motivations" for economic integration in developing countries was industrial development and technological progress.¹⁰⁷ To date, various definitions of what international economic integration is and how economic integration comes about have revealed differences at different levels of development. Jovanovic argues that:

"[I]n the developed market economies, integration means a way to introduce the most profitable technologies and allocate them in the most efficient way; in the centrally planned economies it means the planning of the development of certain activities; and in the developing countries it has the meaning of a tool for economic development."¹⁰⁸

Nevertheless, these arguments were all based on the development of integration promoted by governments and the experiences of integration among homogeneous economies. Except for the case of the CEA, never has any economic integration been launched without meeting these "general rules" of integration between related economies. Since China's

¹⁰⁶.Tayseer A. Jaber, "The relevance of traditional integration theory to less developed countries", *Journal of Common Market Studies*, 9: 3, (1971), p. 256.

¹⁰⁷.Germanico Salgado Penaherrera, "Viable integration and the economic co-operation problems of the developing world: part two ", *Journal of Common Market Studies*, 19: 2, (December 1980), p. 175.

¹⁰⁸.Miroslav N. Jovanovic, *International Economic Integration*, (London: Routledge, 1992), p. 7.

"socialist market economy" has never yet been linked with a real capitalist economy, sceptics in or outside the region have always challenged any possibility of a mixed economy of the type that is emerging with the CEA.¹⁰⁹

Nevertheless, in spite of so many doubts and political barriers, the emergence of the CEA has been a promising development by facilitating economic transactions for economic advantage. Apart from economic incentives for forming the CEA, non-economic factors, such as Chinese expectations of unification, and the starting negotiations for unification, have also been projected as helping to shape the CEA, a still vague concept of the economic "Greater China". No wonder why the first Koo-Wang meeting, which was supposed to be merely making a positive contribution to the formation of the CEA, has been widely regarded as a political probe concerning further governmental involvement. Although officially all sides in the CEA up to now have only worked for the purpose of individual economic prosperity, the development of the CEA has come about in relation to efforts for Chinese national unification, which will certainly accelerate further moves towards the CEA. There have been more critical economic reasons than political ones to support their combining together. Maybe, at this stage, from an enthusiast's point of view, a successful CEA will become a milestone for prospects for a new vision of a "Chinese Community".

¹⁰⁹.In a survey of Chinese enterprises conducted by Lancaster University Management School, the result suggests that China's state enterprises have still dominated its economy. They accounted for half of industrial output and 70 per cent of urban workforces. See Alexander Nicoll, "Long march to market", *Financial Times*, (27 September, 1993), p. 14.

CHAPTER SEVEN

EXTERNAL CONSTRAINTS ON THE FORMATION OF THE CHINESE ECONOMIC AREA

The development of economic cooperation in the Asia-Pacific region has been characterised by Japanese leadership in economic development, mushrooming subregional economic groupings, and overseas Chinese trading and financial networking.¹ Although there has yet to be a clear political commitment from governments in the region, the formation of regional groupings has been an increasing trend, to combine neighbouring economies in order to increase their economic strength. For Asian NICs, it is a great benefit to have their interests represented in any possible economic grouping rather than to be excluded.

External constraints which challenge the CEA as well as the rest of the Asian-Pacific economies, have resulted from the change of international trade practices, particularly the protectionist regional trade policy, and intensifying competitive pressures from the establishment of the single market in the EC and of the North American Free Trade Area (NAFTA).² For other regions, the EC's 1992 programme for the single market as an external constraint has worried East Asian traders about the loss of market share in the European markets as a result of the trade diversion effect. The EC could serve, on the other hand, as an impetus to reinforce the de facto industrial alliance in the Asian-Pacific economies. In spite of official inertia, the formation of the Chinese Economic

¹. Philippe Régnier, Yuanming Niu, and Ruijun Zhang, "Toward a regional 'block' in East Asia: Implications for Europe", *Issues and Studies*, 29: 3, (March 1993), p. 22.

². For an explanation of the NAFTA and its protectionist inclination see *Financial Times*, (17 November, 1993), p. 6.

Area, like other recent self-forming subregional groupings in the Asia-Pacific region, may well be a part of ANICs' economic strategy, above all for Hong Kong and Taiwan. Economic integration within the CEA is not yet mature in terms of the European experience of integration, although the de facto economic integration is cumulatively occurring through regional "integration" of commerce, division of labour and technology diffusion, and finance.³ Should economic integration happen to advance, industrial development will be the essence of the CEA. Whether it is limited to economic integration or it will experience a spillover effect to political integration, the development of the CEA for now is pragmatically concentrated on intensifying business links between the three economies. Japanese influences over regional integration will clearly be shown in future business-driven development of the CEA.

While many advantageous economic factors, i.e. complementarity and competitive advantage, within the CEA have appeared to encourage further moves towards economic integration, the formation of the CEA has also been propelled by the emergence of regionalism elsewhere, which has virtually shifted the weight of multilateral trade structures to regional concentrations. In addition, the United States has begun to pursue unilateralism which has inevitably caused trade friction between the US and the Asian-Pacific economies, Japan in particular.⁴ Because Hong Kong, Taiwan and China have been highly dependent upon foreign trade, the development of the CEA has, therefore, been subject to external constraints largely from major trading partners, the United States and

³. Ibid.

⁴. Soogil Young, "East Asia as a regional force for globalism", in Kym Anderson, and Richard Blackhurst, (eds.), *Regional Integration and the Global Trading System*, (London: Harvester, Wheatsheaf, 1993), p. 135.

West European countries. As a result, the pressures of competition sharpening export profit margins have boosted the ANICs' desire for the formation of a subregional grouping. The CEA, as a subregional economic grouping parallel to the Growth Triangle and the Japanese Sea Economic Zone in Asia-Pacific, will have to be considered in the general context of Asia-Pacific economic cooperation. In addition, Japan and ASEAN countries' general response to the CEA has special implications for its future.

The purpose of this chapter is to examine the impact of external constraints on the formation of the CEA and to what extent Chinese economic integration has been stimulated by the efforts to strengthen competitiveness in reaction to trading constraints generated by the EC and NAFTA. The analysis also focuses on the Japanese political and economic influences on the formation of the CEA. In addition, the formation of the CEA has been partly motivated by the ethnic Chinese overseas. Luring more overseas Chinese investments in the region, the CEA as a "suction pump" has worried its ASEAN neighbours. This may provide a partial explanation of why the CEA has been kept to low profile by the related governments.

7.1. CHANGES IN THE ASIA-PACIFIC POLITICAL ECONOMY AND THEIR IMPACT ON CHINESE ECONOMIC INTEGRATION

International politics today is undergoing a dramatic change in the post Cold War era. The conventional wisdom of strategic and ideological confrontation seems to have been left behind in most parts of the world, as the former Soviet Union disintegrates. So far as international politics is concerned, regional trading blocs appear to be the emerging

focus for rivalry between nations. Recently, the world's three main trading regions in Western Europe, North America and Asia-Pacific, have clearly assumed the shape of a "love-triangle".⁵ The three regions' increasing focus more on intra-regional trade, above all on the part of the EC, than on their trade with the rest of the world, has suggested that the development of a regional inward-looking focus will shape the new international economic regime.⁶ In 1990, while intra-regional exports in Western Europe, North America and Asia, accounted for US\$1,164 billion, \$178 billion, and \$358 billion respectively, exports of the three regions to the rest of the world totaled \$421 billion, \$340 billion, and \$421 billion.⁷

Recently, the Asia-Pacific community has been undergoing a transformation of industrialization economically, democraticization politically, and trading "blocization" regionally. Although these changes may have been stimulated by various factors, the progress of the transformation has generally been driven by the demands of industrialization. As far as economic development is concerned, since the Asian-Pacific economies have long depended heavily upon US' export markets, they have now attempted to change the structure of their foreign trade by increasingly emphasising intra-regional trade.⁸ This is partly because of the US putting pressure on its Asian trading partners for a solution of its trade imbalance and partly because of the growing demands within Asian markets themselves. In consequence, sub-regional groupings based on economic complementarity have emerged right along the West Pacific Rim in the hope that regional economies

5. See *Far Eastern Economic Review*, (8 October, 1992), p. 70.

6. Lawrence Krause, "Trade policy in the 1990s I: good-bye bipolarity, hello regions", *The World Today*, 46: 25, (May 1990), p. 83.

7. The trade figure for Western Europe includes the EC and the EFTA. *Ibid.*

8. C. H. Kwan, "The emerging pattern of trade and interdependence in the Pacific region", *Tokyo Club Papers*, no. 4, part 2, (1991).

would strengthen their international competitiveness through market expansion and industrial cooperation. It is still too early to judge whether increasing economic interdependence will bring about regional economic integration, although many alternatives have been set forth by academics and individual governments.⁹

An increasing number of economic development programmes in the region has been driven and, in some cases, led by the private sector rather than by governments.¹⁰ Driven by economic incentives, the business communities in the region are by far the most devoted to programmes developing subregional groupings, most notably in the case of the Chinese Economic Area. Perhaps because of regional countries' diverse political interests, little has yet been achieved politically between their governments towards the promotion of economic cooperation, except for the formation of ASEAN. To a large extent, political motivations have been serving as yet as a complementary rather than a dominant factor to economic cooperation in the Asia-Pacific region.

The end of the Cold War may have speeded up transactions among the "three Chinese communities", namely China, Taiwan, and Hong Kong. Trade, investment and economic cooperation clearly have run ahead of any other national priority for transactions between the rival "two Chinas" - the Republic of China (Taipei) and the People's Republic of China (Beijing). It has been suggested that China's main threat today may not come from a particular country's military invasion, but from

⁹. Such as the Malaysian government's proposal for an East Asia Economic Caucus and Singapore's Growth Triangle. Various scholars have proposed a "Greater China".

¹⁰. In terms of overseas direct investment, regional industrial development is driven or led by the private sector. An example is the Kwan-Da Groups, composed of six leading Taiwanese food companies, in the case of the Philippines' Subic Bay development. In a meeting with the Group's representatives, President Ramos of the Philippines has promised a more favourable policy and infrastructure. See *Central Daily News*, International Edition, (14 May, 1993).

multi-level economic and scientific challenges from the Western industrial countries, the ANICs, some ASEAN countries, and some Eastern European countries.¹¹ Above all, the impact of China's economic reforms on its domestic democratic demands may have posed more immediate challenges to the Beijing regime than anything else. Post-Cold War China has taken an active role in regional political and economic affairs. Included in this are pressures towards the transformation of the international political system from a bipolar to a multipolar system, approaches to reform and to an open door policy. China's thriving recent economic dynamics have great importance in bringing about continuing East Asian economic prosperity, while the rest of the world stagnates in economic recession.

In the context of the changing international system, Taiwan has been relatively released from the distortions and strangulation of China's "one China" policy in international politics. While economic topics have shaped post-Cold War international transactions, many Western countries have allowed more official links with economically flourishing Taiwan regardless of Beijing's diplomatic pressures, particularly in the case of arms sales.¹² In addition, lasting worldwide economic recession provides an opportunity for Taiwan to exercise its economic influence and improve its relations with the rest of world because of this. Notably, while Taiwan has launched its massive "six-year national

11. Qimao Chen, "New approaches in China's foreign policy: the post-Cold War era", *Asian Survey*, 33: 3, (March 1993), pp. 240-241.

12. The US President George Bush, in August 1992, agreed to sell 150 F16 air fighters to Taiwan. Three months later, the French government allowed Taiwan to buy 60 Mirage 2000-5E fighter jets. see "Ancient fears", *Far Eastern Economic Review*, (3 December, 1992), p. 10. In consideration of larger business interest in China, in December 1993, the French Prime Minister Edouard Balladur has bowed to Beijing's pressure agreeing to limit its relationship with Taipei. See Lincoln Kaye, "Learning to bow", *Far Eastern Economic Review*, (27 January, 1994), pp. 12-13.

development plan" with total expenditure up to US\$ 303 billion since early 1991, many big international firms have taken advantage of Taiwan's offers, and, in return, have been lobbying their own governments to develop official links with Taiwan. France, the most active and successful one, for example, has upgraded its non-diplomatic relationship with Taiwan by allowing a ministerial meeting in 1990 to advance its interest in Taiwanese public construction projects. Within two years, many European countries rushed ministerial visits to Taipei in the footsteps of the French.¹³

China's open door policy to the world, accompanied by Taiwan's change of policy to China, has made their economic interactions far more profitable than ever before. However, change of policy alone is not able to stimulate all kinds of transaction flows, unless it is accompanied by some practical incentives, such as economic advantages and a favourable international system. In the last few decades the triangular strategic relationships of the US, the Soviet Union and China, have dominated international relations in the Pacific region. For the strategic reason of confronting the Soviet Union, the US allied with China and was very concerned with "China factors" in its East Asian foreign policy, in particular the policy to Taiwan stipulated in the 1981 Taiwan Relations Act of the US Congress which is subject to the 1971 Sino-American Shanghai Communique acknowledging that the PRC is the only China. This new American policy inclining towards Beijing and its "one China" emphasis has resulted in China's being able to intervene in any third country's decision to develop official links with Taiwan. That far-reaching American acknowledgement of "one China" has even been exploited by Beijing to present

¹³. See Julian Baum, "Ménage à trois", *Far Eastern Economic Review*, (27 January, 1994), p. 14.

its criticism of foreign countries' arms sales to Taiwan as interference with China's domestic affairs. An example is the transaction over the two submarines deal between Taiwan and the Dutch government in 1982.

Ever since the Soviet Union disintegrated, "China could no longer exploit the favourable strategic status between the two superpowers".¹⁴ Therefore, the "China factors" have been less significant for American foreign policy than they used to be. As a result, trade policy is becoming the most important part of China-US relations. The US military presence in Asia has been diminished, partly because of the Soviet Union's disappearance and partly because Japan has been vigorous enough to take a higher profile. More than this, the US is increasingly concerned with its own home affairs, as the White House has to face difficulties in convincing the American public about maintaining its costly military presence in Asia, as a former US consul general in Hong Kong said in a panel.¹⁵ The post Cold War period has left Asia with some unsolved "simmering disputes" - in the Korea Peninsula, Taiwan Straits, Spratly and Paracel Islands, Kenkaku Islands, and China's political succession, to name but a few.¹⁶ Many have agreed that "security for Asia (in the post Cold War era) has to be redefined largely in economic terms."¹⁷ Therefore, on the

¹⁴. Quimao Chen, "New approaches in China's foreign policy", *Asian Survey*, 33: 3, (March 1993), p. 238.

¹⁵. In the Singapore panel scrutinising Asian security organised by *Time international*, Burton Levin reminded Asian countries that they will have to get need to a prosperous Asia without US military cover in the new era. See "Home alone: a new era - special report", *Time*, (27 January, 1992), pp. 8-23.

¹⁶. For details of the traditional trouble spots of the region, see "Home alone: a new era - special report", *Time*, (27 January, 1992), pp. 8-23. James Walsh, "A leaner, meaner fighting machine", *Time*, (10 May, 1993), pp. 44-47.

¹⁷. Many participants shared the trend in the study panel by *Time* magazine in Singapore in outlook on Asian security. See "Home alone: a new era - special report", *Time*, (27 January, 1992), p. 8.

whole, "securing access to markets and technology" has become Asia's most critical concern.¹⁸

This is not to suggest, however, that this optimistic tone has ruled out any possible danger from political turmoil and war in the region. In dealing more with economic recession than with military confrontation, most Western countries, since 1990, have sharply cut their defense budgets (with France cutting 4.3 per cent, Britain 5.6 per cent, Germany 16 per cent, the US 16.6 per cent, and Spain 19.3 per cent).¹⁹ The US Clinton administration has even offered a five year plan from 1994 to 1998 to slash a total US\$124 billion from defense spending.²⁰ On the other hand, as US troops pull out from the Philippines they are leaving "a vacuum in the middle of Asia's new political, military, and economic universe".²¹ Fearing political uncertainty, Asian countries, as they are able to afford it, have begun to enter a new "arms race" by pouring money into more up-to-date weaponry systems.²²

In terms of the CEA, although there may be potential political ambition for unification on the agenda of both Beijing and Taipei, the CEA development so far has not been directly led by politics. However, the post Cold War scenario has provided a political acquiescence between the "three Chinas" to the CEA development, which could be regarded as a necessary supplement to the thriving economic transactions. In terms of economic integration, the consensus of the three has focused more on integration of economic development and on pursuing industrial competitive strategy globally. Through its

¹⁸. Ibid.

¹⁹. Many in Europe confess that "a force-cutting campaign has gone too far". A reprisal has been considered by the NATO alliances. See "Attacking the cut", *Time*, (12 April, 1993), p. 36, 38.

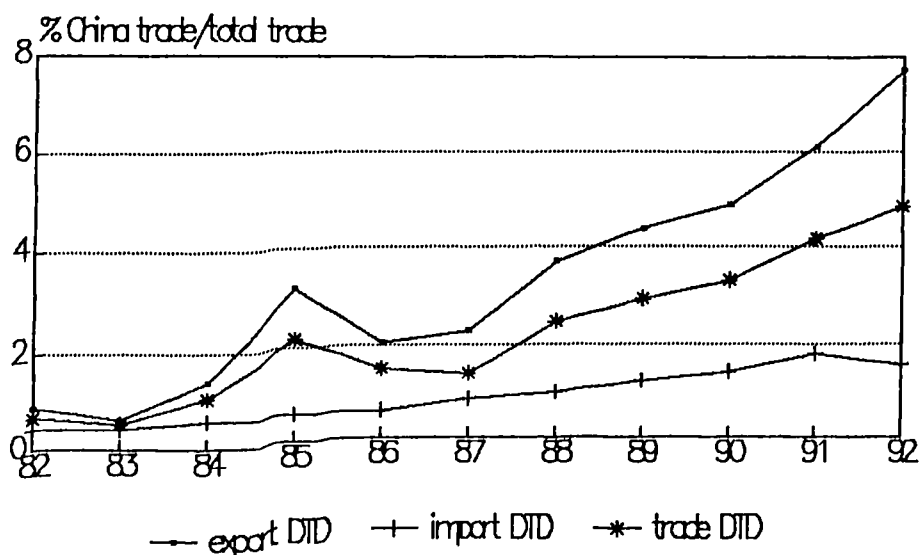
²⁰. See Bruce Van Voorst, "Man in a minefield", *Time*, (5 April, 1993), pp. 42-43.

²¹. "The new universe", *Time*, (17 May, 1993), p. 49.

²². See Ibid., and "Asia unleashed", *The Economist*, (3 April, 1993), pp. 15-16.

investment incentives to Taiwanese businessmen, Beijing is certain to attract Taiwanese industries to the Mainland in order to deepen the degree of Taiwan's dependence on the Chinese economy. (Refer to Figure 7.1.) Beijing's political intention could be infiltrated into Taipei via Mainland Taiwanese business interest groups, e.g. in the case of business groups lobbying the Taipei government for "direct trade" with China. In consequence, the Taipei government could lose its political initiative against China and find itself increasingly at the mercy of Beijing.²³

FIGURE 7.1. THE DEGREE OF TAIWANESE TRADE DEPENDENCE ON CHINA (DTD)



Source: International Trade Bureau, MOEA, R.O.C., 1993, & H.K. Custom Statistics

In the case of Hong Kong and China, since Hong Kong is to become China's responsibility after 1997, the increasing commercial transactions between them offer the hope of political harmonisation between different political and

²³. Taiwanese officials are deeply concerned about further direct links with China which could result in the loss of economic superiority over China. This worry is expressed in the government's various documents and publications. see Koong-Lian Kao, *Lian Ann Ging Mou Shian Kuan Yu Chan Wang*, (Current Economic and Trade Situation and Outlook Between Two Sides of the Strait), Mainland Affairs Council, The Executive Yuan, R. O. C., 1993.

economic systems. For Beijing, politically, Hong Kong's return is certain, but it is still doubtful whether Hong Kong will be able to fit into its "one country, two systems" framework of unification. As China is pledged to maintain Hong Kong's current prosperity for 50 years in the 1984 Sino-British Agreement, Beijing has, therefore, geared up its economic activities to attract Hong Kong investors, and, most importantly, to demonstrate its commitment. In addition, China has not only poured a great deal of capital into Hong Kong, but also won over the confidence of the local business community and even the support of politicians, except for those who are pro-democracy. Hong Kong's grass-root anti-Patten Business and Professional Federation, led by Gordon Wu and property tycoon Vincent Lo, has as an aim to keep a good relationship with Beijing.²⁴ In contrast to the United Democratic Party, the Liberal Party and the Democratic Alliance for the Betterment of Hong Kong are both taking a pro-Beijing line. Trying to defuse political mistrust, politically, Beijing is moving quickly and loudly to express its willingness to tie in with Hong Kong's capitalism. In reality, Beijing shows no hesitation about taking over control of Hong Kong's economic dynamics. In the light of the handover in 1997, Hong Kong has little option but to integrate with China economically. Soon after Hong Kong's future was decided in the 1984 agreement, there appeared to be less confidence about that future. This resulted in a large outflow of business and emigration.

The change of Asia-Pacific trade structure with its gradually increasing emphasis on intra-regional trade has, to some extent, also promoted the competition between regional

²⁴. See for detail James Walsh, "The ties that bind", *Time*, (21 March, 1994), pp. 34-35.

economies themselves, because of limited regional markets and restrained world markets. In addition, China's commitment to economic development in the context of the post-Cold War environment has virtually recognised the importance of Hong Kong remaining prosperous. Hong Kong businessmen have gradually realised that it would be wise to concentrate on making commercial links with a reforming China not only to gain profits and strengthen competitiveness but also to assure their long term security. In return, Hong Kong's pumping capital into China will safeguard China's current reforms. As Hong Kong has resumed its investment flows in China after the Tiananmen incident, Hong Kong's big firms have launched, since 1992, a series of large scale infrastructure investment projects in China, which has boosted a "second wave" of investment.²⁵ The move towards longer term investment in infrastructure, instead of quick profits, characterises the change of investment flows and their endorsement of the Basic Law. For example, Gordon Wu's Hopewell Holdings, a construction conglomerate, has launched a US\$ 1.2 billion six-lane expressway between Hong Kong and Guangzhou.²⁶ In reflecting the Chinese business community's view on the recent row between Hong Kong governor, Chris Patten, and Beijing, Wu comments that "Our biggest and only opportunity is to work with them gently and concentrate on the economy".²⁷ Cheng Yu-Tung's New World Development has become further involved in Chinese real-estate business.²⁸ The New China Hong Kong Group Ltd., set up in May 1993 with collaboration between Hong Kong

²⁵. *Shin Pao* (Hong Kong Economic Journal), (16 December, 1992.)

²⁶. *Fortune*, (9 March, 1992), p. 39.

²⁷. *Financial Times*, (28 September, 1993), p. 19.

²⁸. Henny Sender, "China Savvy", *Far Eastern Economic Review*, (22 April, 1993).

and China, has devoted its business to Chinese infrastructure, real estate, and telecommunications.²⁹

7.2. THE APPREHENSION OF NEIGHBOURING ECONOMIES ABOUT THE CHINESE ECONOMIC AREA

The intention of the CEA, especially as perceived by its neighbouring countries in Southeast Asia, is the resurrection of Chinese nationalism. As the sense of an integrating Chinese community in East Asia has grown following massive trade and investment flows launched by overseas Chinese in the region, other regional economic powers, notably Japan and ASEAN, have been anxiously following developments. For Japan, the establishment of the CEA may further disrupt the alternative regional grouping proposed by the Japanese and others. More worryingly, for ASEAN, given its economic domination already by ethnic Chinese, economic integration based on the CEA within a larger regional framework exclusively covering the Chinese community could raise the suspicion that Chinese economic power will dominate all the region. It could be for this reason that so far the "three Chinas", China, Taiwan and Hong Kong, have been reluctant to support the CEA openly.

In addition, many proposals for regional integration have been based on individual interests and therefore there has been less support from regional countries for any particular plan. For example, the East Asia Economic Caucus (EAEC) proposed by Malaysia, has not as yet been welcomed in the region. Regional leaders even including those of ASEAN countries themselves, President Suharto of Indonesia in

²⁹. Jonathan Karp, "The new insiders", *Far Eastern Economic Review*, (27 May, 1993).

particular, have cast some doubts on its prospects.³⁰ As a result, many economies, instead, have hustled to expand in their own hinterlands through which their economic strength to compete in the world market will be improved.

7.2.1. Incompatibility or Compatibility: Japanese Interest and the Formation of the CEA

Since Japan has been involved in almost all the processes forming sub-regional blocs directly or indirectly in East Asia in terms of industrial development, any emerging regional bloc that does not work in favour of Japanese interests will not be feasible. As the dominant economic actor, Japan has been a major determinant of the remarkable economic growth of the Asia-Pacific region, especially in most of the East and Southeast Asian economies. Notably, the fast growing economies in East and Southeast Asia have been based upon the "flying geese" pattern of economic development led by Japan.³¹ Indeed, Japanese industrial experience and technological expertise have spread to every part of the regional economic development.

It can be argued that there appear to be five possible scenarios for the Asia-Pacific region: the Yen bloc, the Beijing bloc, the Western Pacific community, the pan-Pacific community, and Cooperating Asia-Pacific subgroups.³² Apart from

³⁰. Since Malaysian Premier Mahathir's EAEC openly excludes the US, Canada, Australia, and New Zealand, the cautious response of the US and most the APEC countries has halted the plan. Fearing US opposition, Japan, a proposed leading member in the EAEC, has been reluctant to support the idea.

³¹. Reinhard Drifte called the "flying geese" pattern a "three stage" economic hierarchy. See his *Japan's Foreign Policy*, (London: RIIA, Routledge, 1990), p. 92.

³². Duk-Choong Kim, "Open regionalism in the Pacific: A world of trading blocs?", *American Economic Review*, 82: 2, (May 1992). His other article sketches the future in more detail. "Scenarios for an Asian Bloc?", *The Korean Journal of International Studies*, 24: 2, (Summer 1993), pp. 190-195.

the political considerations of other powers, notably the US, and Russia, Japanese industrial strength has virtually tied its neighbours' economic development in to its own networks of foreign aid programmes, trade links, foreign investment, and even more crucially technological transfers. The creation of an industrial division of labour between China, Taiwan and Hong Kong, and between China and South Korea, for instance, has taken place against the context of Japanese industrial domination, from the control of technology for upstream products right through to the markets.

As the rising economic power capable of rivalling American economic supremacy, Japan has its own plan to lead a single regional economic unit. Perhaps because of previous partly successful attempts with regard to proposed regional blocs in the Pacific community (see Chapter Four in detail), Japan's new strategy, called the New Asian Industrial Development (New AID) Plan, was announced in January 1987 by its Ministry of International Trade and Industry (MITI). The plan was mainly based on practical industrial cooperation which has already existed widespread across East Asian economies throughout their catching-up process on the way to economic development. Since the mid-1980s, Japan and the ANICs have steadily expanded their foreign investments in the region itself, not only because of dramatic appreciation of their currencies but also because of the decade-long slowing down of economic performances in most Western industrialised countries, the momentum of Asia-Pacific economic cooperation, and regional governments' policies.³³ As a result, a regional

³³. For details of reasons for the rapid growth in intraregional investment and individual countries' investments, (Japan, Hong Kong, China, Taiwan, and South Korea), see Edward K. Y. Chen, "Foreign direct investment in East Asia", *Asian Development Review*, 11: 1, (1993), pp. 24-59. For Japan's expanding investment in the ANICs in the 1980s and its implication of market effects see Drifte, *Japan's Foreign Policy*, pp. 94-95.

division of labour led by Japan has raised the possibility of forming "a de facto economic sphere".³⁴ Indeed, Japan's plan is to coordinate its overseas development assistance, trade, and foreign direct investment throughout Japan, the ANICs, ASEAN countries and China, in order to enable Japan effectively to manage regional industrial production.³⁵ A single economic unit led by Japan, which is the centre of the plan, has exposed Japan's attempt to integrate East Asian economies to rely more on economic means than political ones.

The Japanese plan is, to a large extent, reliant on the stable relationship between China and Japan. Described by the former Japanese Prime Minister, Kiichi Miyazawa, Japanese-US and Japanese-China relations are the two wheels of its foreign policy. The former is running on a "world order track", while the latter is running on an "Asian order track".³⁶ In East Asia, Japan's role as a "regional stabiliser" projecting its economic and, to a less extent, political strength to balance confrontation in the region between powers, in particular the USA, the Russian Republic, and China (in the case of the Korea Peninsula), has been notable.³⁷

In retrospect, Japan's relations with China in the pre-normalization period were largely shadowed by the United States' policy of containing communism. In the early 1970s, the change of US policy to open relationships with China, to force the revaluation of the Japanese Yen and to impose quotas on Japanese textile exports to the United States, guided by

³⁴. Toru Nakakita, "The takeoff of the East Asian Economic Sphere", *Japan Review of International Affairs*, (Spring/Summer 1991), pp. 70-73.

³⁵. Joseph Romm, "Japan's flying geese", *Forbes*, 150: 12, (23 November, 1992).

³⁶. Jihua Zhou, "Japan's Foreign policy choices for the twenty-first Century: A Chinese perspective", in Tsuneo Akaha, and Frank Langdon, (eds.), *Japan in the Posthegemonic World*, (Boulder, Colorado: Lynne Rienner Publisher, 1993), p. 196.

³⁷. Muthiah Alagappa, *Japan's Political and Security Role in the Asia-Pacific*, (Malaysia: Institute of Strategic and International Studies, 1988), p. 25.

the "Nixon Doctrine" of 1969, shocked Japan.³⁸ This has partly brought Japan onto the course initiated by the Americans to confirm that the importance of China has to be taken into account in pursuing regional peace and national security. Since 1971, the year of Sino-Japanese normalisation, the relationship between them has steadily developed with a common security target of eliminating the Soviet threat.³⁹ By linking China with Japanese security, Japan has shown its eagerness to support China's economic development and most recently China's reform and open door policy from the beginning by means of increasing foreign development aid, investment, and trade.⁴⁰ The solid intention to link with China has lain in a belief that a stable and prosperous China is vital to Asia's peace and to Japan's interests. Whatever role Japan is to play in the world and the region itself, acceptability to China is all the more important, because "without a good political relationship with China, Japan cannot hope to win widespread acceptance as a leader elsewhere in Asia."⁴¹ For decades, Sino-Japanese relations have been conditioned by complementary concerns in economic matters and in Chinese political prejudice against Japanese expansionism.⁴² These facts have

³⁸. For this change of US policy which caused shocks for the Japanese see the discussion in Donald C. Hellmann, "Japanese Politics and Foreign Policy: Elitist Democracy Within an American Greenhouse", in Takashi Inoguchi and Daniel I. Okimoto, (eds.), *The Political Economy of Japan, Volume 2. The Changing International Context*, (Stanford, California: Stanford University Press, 1988), p. 364.

³⁹. Scholars have found recently that the regional dimension of Japan's security strategy has still been dominated by the threat of the former Soviet Union. They have urged Japan to adjust its security strategy to the changes in the Soviet Union. See Fred C. Iklé, and Terumasa Nakanishi, "Japan's grand strategy", *Foreign Affairs*, (Spring 1991), pp. 82-84.

⁴⁰. See Whiting, "China and Japan: Politics versus Economics", pp. 41-44; also Qingxin Ken Wang, "Recent Japanese economic diplomacy in China: political alignment in a changing world order", *Asian Survey*, 33: 6, (June 1993), pp. 625-641.

⁴¹. For a similar observation of the importance of China in Japanese foreign policy to the region, note the statement of the former Japanese ambassador to China, Yosuke Nakae, that "It is certain that without friendly and cooperative relations between Japan and China there can be no support for peace, stability and prosperity in Asia." David Arase, "Japan in East Asia", in Akaha, and Langdon, (eds.), *Japan in the Posthegemonic World*, p. 123.

⁴². Based on his previous contribution to Sino-Japan relations, *China Eyes Japan*, (Berkeley: University of California Press, 1989), Allen Whiting continues to emphasize the heritage

contributed to their highly asymmetrical economic interdependence.⁴³ Under economic complementarity, China gets access to Japanese machinery, chemical products, technology, and steel and other metallic products on which China's development relies, while Japan, in return, imports food stuffs and raw materials, in particular coal and oil, and makes use of the Chinese potential market.

Japanese industrial development within the CEA has appeared to be a part of a Japanese global strategy. All national economies of the CEA have been receiving Japanese capital, amounting to a large proportion of Japan's private overseas investment. This is partly because the Chinese economic reform opening its market to the world has brought enormous commercial potential, and partly because for Japanese businessmen China could offer the best opportunity to gain competitive advantage, not merely comparatively, over their potential rivals.⁴⁴ In terms of the structural relationship between Japan and the CEA's economies as a whole, industrial cooperation, across the Taiwan Strait between three economies, namely Taiwan, Hong Kong, and China, was largely based on labour-intensive industries, which relied on Japanese passed-on technologies and machineries, during the first wave of overseas Chinese rushing into China seeking locations substitutive for production. As the CEA has developed and

of Chinese enmity against Japanese aggression in observing their relations. See his "China and Japan: Politics versus Economics", *The Annals*, AAPSS, 519, (January 1992), pp. 39-51.

⁴³. Sino-Japanese trade is basically asymmetrical in both quantitative and qualitative terms. While the China trade is about 4-5 per cent of total Japanese foreign trade, Japan's trade links with China account for about one fifth of total China foreign trade. In addition, Japanese aid and private investment in China have also contributed to this asymmetry. See Whiting, "China and Japan: Politics versus Economics", pp. 41-42; Japan is quite confident about maintaining this asymmetrical interdependence in favour of Japan for some time, Arase, "Japan in East Asia", p. 123.

⁴⁴. For labour intensive industries, comparative advantage is based on cutting production costs, e.g. wage and rents. However, for those capital- and technological-intensive industries, competitive advantage stems from market share rather than simply lower cost of production factors.

become more noticeable, the global strategy of Japanese companies has been to gain access to the great market and manufacturing sites in the CEA through the creation of an industrial division of labour.

Nissan Motor Co., the number two automaker in Japan, for example, has expanded its cooperation with Yueloong Motor Co., Nissan's Taiwanese partner, in order to engineer the larger global framework which was documented in its recent Asian strategy for the 21st century. The centre part of its plan is focused on Japan itself, Taiwan, Thailand, and Mainland China.⁴⁵ The first practical step has been to introduce a newly designed small commercial vehicle in summer 1994, which is to be built in Taiwan and Thailand.⁴⁶ Earlier, a joint venture between Nissan Motor and Taiwan-based Honda Sophisticated Instrument Co. had been announced which would invest in China through partnership with China Motor Trading Hua-Tong Co. for a manufacturing factory with a production capacity of up to 400,000 cars per year.⁴⁷ Nissan is not alone in taking the Taiwanese short cut to the Chinese market. Toyota, the number one Japanese automaker, intends to incorporate a Taiwanese partner, Kuo-Ruei Motor Co., into its network of international manufacturing ventures. It already possesses a new factory in Taiwan, set up in May 1993, which Toyota has regarded as its launching pad to China.⁴⁸

In the Cold War era, Japan's economic relationship with China had blended with political and security considerations concerned with counterbalancing the Soviet Union. The purpose

⁴⁵. *Central Daily News*, International Edition, (30 September, 1993).

⁴⁶. "The great Asian auto race", *Business Week*, (25 January, 1993), p. 24.

⁴⁷. *Central Daily News*, International Edition, (20 July, 1993).

⁴⁸. In his visit to Taiwan, President Tatsuro Toyota stated that the "new big car factory", located in Kuan-In Industrial Park, Toayuan, Taiwan, is planned, in five years, to have a production capacity of 200,000 cars annually. *Central Daily News*, International Edition, (8 May, 1993).

of Japan's official development aid and foreign direct investment was to further its strategic interest in helping China to accelerate its modernisation, and so strength China's geopolitical importance for Asian stability, to some extent, even at the expense of short-term Japanese business interests.⁴⁹ In addition, continued economic modernisation in China has demonstrated its potential market ability which the Japanese business community could not afford to ignore. With the onset of the post-Cold War era in the late 1980s, whilst Japan emerged as an economic superpower and China's importance in military and political terms became much clearer, its China policy became an important part of Tokyo's "global diplomacy".⁵⁰ Japan's adherence to this policy was plainly expressed in the Houston G7 summit in the summer of 1990, where Prime Minister Kaifu announced Japan's third package of yen loan to China with severe criticism pouring from other leaders, because of the Japanese pursuing their interests at the expense of moral principles at the time of global sanctions against China in the wake of the Tiananmen incident.⁵¹ It is very clear that China is more important for Japan in economic terms in the short term than in political terms. Therefore, the formation of the CEA as an enlarged Chinese market has unquestionably tempted the Japanese business community.

It was not surprising that the Japanese took the lead in breaking the diplomatic silence surrounding China just a few months after the June 1989 incident. Although many Japanese

⁴⁹. Japan's Ministry of International Trade and Industry (MITI) and Ministry of Foreign Affairs (MFA) are two major players in shaping China policy. When Hua-Deng took over Beijing by ousting the Gang of Four, the MFA believed that its loan should be used to stabilise the new ruling regime at a time of fragility. Wang, "Recent Japanese economic diplomacy in China: political alignment in a changing world order", pp. 633-634.

⁵⁰. Ibid., p. 634.

⁵¹. Ibid., pp. 634-635.

big firms remain very cautious about the potential political instability of Beijing, and the likely political struggle that will occur when Deng Xiao-Ping dies, a large number of small and middle sized companies, like Hong Kong and Taiwanese enterprises, have flocked into China to take advantage of low cost production factors. In the late 1980s, Japanese direct investment in and trade with the "three Chinas" was greater than that with the ASEAN countries (See Table 7.1).

TABLE 7.1 JAPAN'S AID, TRADE, AND INVESTMENT IN EAST ASIA

	AID(US\$mil.)	TRADE(\$bn.)	INVESTMENT(\$bn.)
China	2,177	53.19	2.00
Taiwan	n	78.51	1.23
Hong Kong	n	46.22	4.18
CEA Total	2,177	178.02	7.41
Indonesia	1,433	48.26	1.72
Malaysia	777	29.49	0.99
Philippines	1,364	13.30	0.33
Singapore	n	36.93	2.35
Thailand	1,307	26.50	1.81
ASEAN Total	4,881	154.48	7.20

Note: total trade (1986-89), total direct investment (April 1986-September 1989).

Source: Based on MITI & Ministry of Finance, see Charles Smith, and Louise do Rosario, "Empire of the sun", *Far Eastern Economic Review*, (3 May, 1990), p. 48.

As the "three Chinas" combination has become Japan's leading trading partner in Asia, Japan's exports to the CEA rose by 23 per cent in comparison with the 1992 figure to US\$56.1 billion, and its imports from the CEA grew by 9 per cent to \$28.8 billion.⁵² Whilst the worldwide economic

⁵². "Hong Kong, Taiwan, China lead Asian trade partners: 'three Chinas' voraciously gobbling up Japanese goods", *Japan Times Weekly International Edition*, 33: 21, (24-30 May, 1993), p. 13.

recession has slowed down the European and North American economies dramatically, the increasing transactions inside the CEA have brought about the fastest growing economic performance in the world, from which Japan's troubled sectors, the electronics and car industries, have benefited through increased exports.⁵³

MITI's general trade policy guidelines for China, announced in 1991, suggest three major policy objectives: to intensify bilateral trade relations and cooperation, to ensure that China remains an important source of Japan's energy supplies and an important export market for Japan, and to avoid isolating China and thereby preserve peace and stability in East Asia.⁵⁴ To promote its relationships with China is clearly in Japan's interest. As the CEA develops, its market potential is becoming widely known. In 1992, Toyota Motors, accompanied by a group of Japanese trading houses and a transportation company, Sankyu, established new businesses in China. This surge of direct investment by big Japanese firms has been most important. It has led to China becoming Japan's second biggest trading partner.⁵⁵ Apart from reinforcing economic ties with China, Japan's desire to take advantage of the formation of the CEA has been apparent through its encouragement of trade with and direct investment in Hong Kong,⁵⁶ and its setting up the regional operation centre for firms in Taiwan in accordance with the government's aspirations in the CEA.⁵⁷

53. Robert Thomson, "Beijing encourages Tokyo trade links", *Financial Times*, (23 September, 1992), p. 8.

54. Information was based on MITI, *Trade and Industry*, (March 1991), p. 24. Quoted from Qingxin Ken Wang, "Recent Japanese economic diplomacy in China", p. 632.

55. Robert Thomson, "Beijing encourages Tokyo trade links".

56. For Japanese investment in Hong Kong for the period of 1985-90, see Carl Goldstein, and Anthony Rowley, "Shogun wedding", *Far Eastern Economic Review*, (28 June, 1990), pp. 70-71.

57. In response to Taipei's program of becoming the regional operational centre, Japanese transnational corporations seem to have lagged behind American and European TNCs' moves

TABLE 7.2. TOP FOUR FOREIGN INVESTORS IN CHINA (US\$ bn.)

	H. K.	USA	TAIWAN	JAPAN
1979-84	64.9	10.2	-	11.5
1985	41.3	11.5	-	4.7
1986	14.4	5.3	-	2.1
1987	19.5	3.4	1.0	3.0
1988	34.7	3.7	4.2	2.8
1989	31.6	6.4	5.2	4.4
1990	36.8	3.6	9.9	4.6
1991	68.3	5.5	14.0	8.1
1992*	80.0	30.0	34.9	25.0
Total:				
1979-92	391.5	79.6	68.3	66.2
(1988-92)	(251.4)	(49.2)	(67.3)	(44.9)

Note: * 1992 was an estimation.

Source: Industry Bureau, Ministry of Economic Affairs, *Kung Yeh Gien Hsun*, (Industry Brief Information), 23: 9, (September 1993), p. 34. Information based on *Chung Kuo Dui Wuai Gin Gih Mou Yi Nien Gien*, (China Yearbook for Foreign Trade, Beijing); C. D. Yien, L. C. Lin, and C. Chung, "Tai Shun Da Lu Tou Tze Gi Mou Yi Tze Yien Giou", (A research for Taiwan's businessmen China investment and trade), Chung Hua Institution for Economic Research, (June 1992).

There may be various reasons for Japanese business being drawn into China. Firms may go to China for "defensive" reasons in order to preempt their competitors and preserve their market share.⁵⁸ Being jealous of, perhaps even afraid of, overseas Chinese businessmen benefiting too much from China's recent reforms,⁵⁹ Japanese firms have clearly showed their concern by the increase in their recent Chinese investment, albeit it is not yet clear how far Japanese investment has got

there. Sony, the best known Japanese electronics giant, has chosen Taiwan to be the base of its regional operation centre for manufacturing. Refer to Chapter five for details.

⁵⁸. Denis F. Simon, "China in the World economic system", *Proceedings of the Academy of Political Science*, 38: 2, (1991), p. 24; Reinhard Drifte argues that Japan is being forced into increasing investment in China for "competitive" reasons, as its neighbouring ANICs have invested in China to take advantage of China's low production factors. See his *Japan's Foreign Policy*, p. 99.

⁵⁹. "Hua Ren Yu Hua Chiao Chi Yeh Shien Chi Da Lu Toa Tze Rer", (Chinese and overseas Chinese enterprises launch China fever of investment), *Central Daily News*, International Edition, (4 May, 1993).

something to do with these "defensive" reasons (compared with other major investors in Table 7.2). However, it is not so difficult to imagine that for larger sized firms, in particular, expanding market share always implies victory over competitors. While industries in Hong Kong, Taiwan, South Korea, and ASEAN countries, as well as the United States and Europe, have been setting up business in China regardless of the risk, increasing competition and the need to cut costs have pushed Japanese industries to follow suit to avoid being left behind. Due to the persistent economic slowdown in the European and American markets in the late 1980s and the early 1990s, and, by contrast, the strong economic growth performance in the CEA, business attention has largely shifted to East Asia. This directly resulted in mounting pressure on the part of the Japanese for access to the CEA.

Although the Japanese have contributed to almost all parts of East Asian economic development, in terms of transferring industrial experience and technology the Japanese have still kept out their partners from the most critical advances and high technology industries, with which the developing countries of the region have as yet to be satisfied.⁶⁰ In many cases, firms, which are linked with Japanese companies by cooperation arrangements or any other business protocols, have been complaining about their parsimonious technology transfers for years. Even the relatively advanced ANICs have made such complaints against the Japanese, let alone the rest of less developed East Asian countries. For example, the Samsung group, one of the largest South Korean conglomerates, the most formidable non-Japanese Asian company, is still highly dependent upon US and Japanese

⁶⁰. Edward J. Lincoln, "Japan's Role in Asia-Pacific Cooperation: Dimensions, Prospects, and Problems", *Journal of Northeast Asian Studies*, (Winter 1989), p. 10.

partners for vital equipment. The Japanese above all have shied away from sharing industrial secrets.⁶¹ The original purpose behind the Japanese transferring their technology was not to stimulate greater technological independence in their local partners, but to promote Japanese trade and to framework the vertical division of labour in favour of Japanese companies.⁶² Although it is not surprising that the Japanese put their business interests first, nevertheless, it is paradoxically, to a large extent, outstanding Japanese investment flows which have accelerated regional development and technological levels. As far as developing technology in the CEA is concerned, Taiwan's excellence in the manufacture of commercial appliances and China's strength in fundamental research could augur well for future industrial cooperation. It also implies that through an industrial division of labour based on technological cooperation, the CEA as a whole, instead of being dependent upon Japan or anywhere else, could develop its own technology base to support its further economic development.

For example, Inventa Electronics Co. Ltd., one of Taiwan's leading electronics companies, has taken the lead in taking advantage of China's well-trained R & D personnel as an advocate for its business strategy. By the end of 1992, the company had recruited 250 staff for its laboratory from universities around its Shanghai subsidiary. Thereby, it has spread its framework for its industrial division of labour across East Asia: lower technology and larger quantity production in Malaysia; R & D in China; and headquarters in

⁶¹. "Samsung: Korea' hope for high tech", *Business Week*, (27 January, 1992).

⁶². Edwin A. Winckler, and Susan Greenhalgh, (eds.), *Contending Approaches to the Political Economy of Taiwan*, (New York: M. E. Sharpe, Inc., 1988), pp. 213-215.

Taiwan.⁶³ Another example shows that Tsang Kuen Enterprise Co., a successful electrical company, has organised its division of labour, according to industrial ability, through its subsidiaries. In terms of production, China is to be the main supplier of components, and Mexico and the Czech Republic are to be the location of its assembly plants. In respect of R & D, Taiwan is to be the location of applied research and China the location of its fundamental research.⁶⁴ In the short run, these joint efforts of Chinese and Taiwanese business will not easily rival the Japanese in terms of technology. In the longer term, economic integration in the CEA will not only strengthen industrial output, but also accelerate technological development. In this respect, the CEA appears to be gaining potential as a rival to Japan's economic domination in the region. However, that will only be achieved after the CEA is working fully and successfully.

7.2.2. Long Lasting Anxiety Comes True: A Chinese Economic Threat To ASEAN

From the Southeast Asian countries' point of view, Chinese economic integration combining the economies of China, Taiwan and Hong Kong, is likely to reopen a historic ethnic wound of anti-Chinese sentiment in the region, which was on the way to being healed. It may also stir up new competition in terms of economic development. In response to the trend of worldwide regionalism, East Asian countries are forming their own groups to promote their individual interests, whether stimulated by governments or by business itself. In Asia-

⁶³. Y. W. Ho, "Gin Gi Chung Kuo De Gien Bin - Tai Shan", (The pioneer of Economic China - Taiwanese businessmen), *Global Views*, (15 December, 1992), p. 44.

⁶⁴. *Ibid.*, p. 43.

Pacific, the Japanese "flying geese" industrial development pattern has brought about the world's fastest growing economies amongst Asian NICs since the 1970s, and another tier of ANICs (mainly Malaysia, Thailand, Indonesia, and Philippines) since the mid-1980s, as well as China. In all these fast growing economies, except for South Korea, regional economic activity seems to be dominated by Chinese businessmen. Due to overseas Chinese families' particular business networks that extend into every major market in Southeast Asia, Japanese linking up with Chinese-owned companies in the region is considered to be one of the major factors in Japanese success there.⁶⁵

In Southeast Asia as a whole, the combined wealth of the 40 million overseas Chinese in the region, sources suggest, may reach US\$200 billion.⁶⁶ These tremendous business groups have established a powerful regional network, over time, through capital flows, joint ventures, marriages, political expediency, and a common culture and business ethics.⁶⁷ Moreover, overseas Chinese are essentially stateless. Their businesses are founded on shared dialect, personal relationships, kinship, and a common origin in a clan, a village or a county. As one study states very straightforwardly, "the remarkable economic performance of the Overseas Chinese in the ASEAN countries is fact and cannot be explained away by any statistical or structural hypothesis."⁶⁸

In Indonesia, in the mid-1980s about 70-75 per cent of the country's assets belonged to the ethnic Chinese. The Indonesian Chinese, about 4 per cent of the population,

⁶⁵. Ford S. Worthy, "Keys to Japanese success in Asia", *Fortune*, 124: 8, (7 October, 1991).

⁶⁶. Henny Sender, "Inside the Overseas Chinese networks", *Institutional Investors*, 25: 10, (September 1991), p. 38.

⁶⁷. Ibid., p. 41.

⁶⁸. Victor Simpao Limlingan, *The Overseas Chinese in ASEAN: Business Strategies and Management Practices*, (Manila: Vita Development Co, 1986), p. 158.

controlled 17 of the 25 biggest business groups in the country. The Thai Chinese, according to a survey in the mid-1970s, 8-10 per cent of the population, owned 90 per cent of the commercial and manufacturing assets, and half the capital of the banks. Only about 1 per cent of the population of the Philippines is Chinese, but their companies account for two-thirds of the sales of the 67 biggest commercial companies. Sales of the smaller companies are even more dominated by the Chinese.⁶⁹ The Chinese, the second biggest ethnic group, account for a third of the population in Malaysia, but have a much larger share of Malaysian economic power and virtually dominate its business.⁷⁰

TABLE 7.3 THE ETHNIC CHINESE IN SOUTHEAST ASIA (in million)

	population*	Chinese**	in %***
Indonesia	181.4	7.2	3.9
Thailand	57.5	5.8	10.0
Malaysia	18.3	5.2	28.4
Singapore	2.8	2.0	71.4
Burma	42.1	1.5	3.5
Vietnam	67.6	0.8	1.1
Philippines	62.3	0.8	1.2

Source: * *Asia 1992 Yearbook*, Far Eastern Economic Review, (December 1991).

** *The Economist Yearbook 1993 Edition*, p. 153.
Information based on *Overseas Chinese Economy Yearbook*, R. O. C.

*** own calculation.

Although formal racial discrimination has disappeared in much of Southeast Asia, except in Malaysia, the recent development of "China fever" seems to have provoked anti-Chinese sentiment. Singapore, for example, has responded to "China fever" in a positive way by "making China its top

⁶⁹. Information above quoted from *The Economist Year Book 1993 Edition*.

⁷⁰. "That sucking sound is China slurping up money", *Business Week*, (30 August, 1993), p. 19.

overseas investment priority".⁷¹ Furthermore, the Singapore government has actively participated in the process of forming the CEA, and, to a larger extent, to Chinese unification. In terms of security and long term economic development, it is in its vital interest that Singapore, a city-state, continuously pursues its internationalisation. This includes taking positive account of blood of relationships with China and Taiwan in particular. Indeed, Singapore, always regarded by the regional Chinese community as a "Chinese place", is in an unquestioned position to be a middleman in whom both Taipei and Beijing unsuspectingly trust.⁷² During the first ever direct talks between quasi-official representatives of Beijing and Taipei, the Strait Exchange Foundation (SEF) and the Association for Relations Across the Taiwan Straits (ARATS), held in Singapore in April 1993, it was said that Singapore, as "an objective third party" for both of the players, had advocated the talks between China and Taiwan from the first emergence of their possibility.⁷³

As a result, as Singapore's policy steers its attention away from already existing cooperation with Malaysia and Indonesia in its "Growth Triangle" with China, its ASEAN partners have already cast some doubt on the intention of

⁷¹. Michael Selwyn, "SE Asian Chinese head for home", *Asian Business*, 29: 4, (April 1993), p. 25; In 1993 about half Singapore's overseas investment projects in China received help from Singapore's Economic Development Board. See "Giant leaps", *The Economist*, (2 April, 1994), pp. 64-65.

⁷². K. S. Liao, "Singapore De Da Lu Tzen Tse Gih Ch'i Tsai Lian An Kwan Shi De Tsu Yun", (Singapore's Mainland policy and its role playing on the relations between two sides of the Strait), *Central Daily News*, International Edition, (23 April, 1993).

⁷³. Singapore's role, played in the first quasi-official meeting of China and Taiwan, was significant. According to information revealed, Singapore's former Prime Minister, Lee Kuan Yew, played a key role in helping Taipei and Beijing to arrange the meeting in Singapore. In February 1992, Lee visited his Taipei counterpart, the premier Hau Pei-Tsung, forwarding a message from China's President Yang Sun-Kuen for a dialogue between Beijing and Taipei. See *Central Daily News*, International Edition, (19 April, 1993); also Cora L. S. Wang, *With a Clear Conscience*, (Taipei: Commonwealth Publishing Co., 1994), pp. 262-264.

Chinese investment.⁷⁴ The leader of Malaysia's opposition party "Semangat '46", Tengku Razaleigh Hamzah, has bluntly criticised Malay Chinese for investing too heavily in China. He also contended that with the economic integration of China, Taiwan and Hong Kong, the appearance of the CEA is threatening the regional countries' security.⁷⁵ The anxiety inside these governments over China's absorption of foreign investment has increased, although there is little sign yet that there is going to be a new wave of anti-Chinese sentiment. Nevertheless, following some major deals in China involving overseas Chinese from Southeast Asia in 1992 and 1993 (Table 7.4), signs of a backlash around the regional governments has emerged. Indonesia's State Minister for Investment Promotion, Sanyoto Sastrowardoyo, has accused ethnic Chinese businessmen of investing too much in China.⁷⁶ Some regional media sources even warned that anti-Chinese sentiment would return, if ethnic Chinese conglomerates do not reinvest in Malaysia and Indonesia eventually, using their earnings from investment in China.⁷⁷ In April 1994, a workers' demonstration over a wage dispute ended up as an anti-Chinese outbreak in Medan in Indonesia. It is said that the event can be partly attributed to criticism about recent ethnic Chinese investment in China.⁷⁸

Moreover, in terms of economic development, China and most ASEAN countries, except for Singapore and Brunei, are nearly at the same level of economic development. With regard

⁷⁴. See C. H. Wu, "Singapore Da Lu Rur Yin Chia Ling Kuo Yie Lui", (Singapore's "China fever" causes doubt from neighbouring countries), *Central Daily News*, International Edition, (24 May, 1993).

⁷⁵. T. M. . Hsui, "Mien Duei Chu Kuo Ren Ging Gih Tong Her, Ker Kuo Ging Yu Giou Gia", (Facing Chinese Economic Integration, Countries are astonished and worried about it), *Central Daily News*, International Edition, (1 June, 1993).

⁷⁶. "That sucking sound is China slurping up money", p. 19.

⁷⁷. Based on Hong Kong Economic Journal's report on 17 August, 1993, see "That sucking sound is China slurping up money", p. 19. Earlier in a special report on China, the same warning had been expressed. See "The spark plug of Asia's future", *Business Week*, (17 May, 1993), p. 30.

⁷⁸. See *Central Daily News*, International Edition, (19 April, 1994).

TABLE 7.4. RECENT INVESTMENT BY OVERSEAS CHINESE FROM
SOUTHEAST ASIA IN CHINA

country	company(tycoon)	investment(US\$ mil.)
Thailand	Charoen Pokphan	3,000
	Bankok Land	1,400
	Soon Hua Seng	1,000
Singapore	Jia Tong Group	500
	Vikay Group (Owned by Indonesian Herman Tanlhaha)	260
	Hong LWY Holdings (Peter Lim, Tony Wong, Steven Lam, and Chris Yong)	210
Indonesia	China Strategic Investment (Oel Hong Leong)	260
	Lippo Ltd(Mochtar Riady)	130
	Lippo Ltd	40
Malaysia	Kuok Group(Robert Kuok)	300
	Kuok Group	130
	Berjaya Corp(Vincent Tan)	100
Total		US\$7,300

Source: "SE Asian Chinese head for home", *Asian Business*,
(April 1993), p. 26.

to their recent economic development, they have all taken advantage of their lower costs in wages, land, and resources to encourage the relocation of many labour-intensive industries from Japan and the ANICs. In seeking to woo foreign investors to further their economic development, Southeast Asian countries have experienced strong competition from China at the same end of the development spectrum. Since the mid-1980s, the ANICs have joined forces with the Japanese investing in Southeast Asia to gain access to lower cost production factors which no longer exist in their home countries.⁷⁹ While China's economic development has been

⁷⁹. Although there have been huge investments from Japan and the ANICs in North America for access to these markets, more recent investment trends seem to target Southeast Asia for their lower cost production. For investment flows see Rober L. George, "The surge in Pacific capital flows", *Asian Finance*, (15 December, 1988). For the purposes of the ANICs'

speeding up to fully comply with reformist policy, more and more foreign investors have been pulling their businesses, in labour-intensive industries in particular, out of Southeast Asia because production factors there, over time, have no longer been as competitive as they were when businesses were set up a few years ago.

As one of Malaysia's single largest investors in manufacturing sectors, Taiwanese investors, for example, have complained that the Malaysian government is unlikely to widen its industrial incentives, is unable to control fast increasing labour costs, and is not reliable about the difficulties of securing visas which are of particular importance for Taiwanese enterprises and their expatriate executives and imported technicians.⁸⁰ In early 1993, the then Vice-Economic Minister of Taiwan, P. K. Chiang, stated that Malaysia's investment climate was getting worse due to rising labour costs and social problems. Moreover, George C. H. Wang, the director of Taipei's Economic and Cultural Centre in Malaysia, a leading organ of Taiwanese business, pointed out that changes in the economic situation, China's accelerating economic reforms as well as those in many other countries, such as Vietnam and Indonesia, have offered better investment incentives and a declining interest in Malaysia.⁸¹ Indeed, an analysis by the Taiwanese Ministry of Economic Affairs suggests that the recent decline of Taiwan's investment in Southeast Asia has resulted mainly from the changed investment

investment in Southeast Asia see Kong Yam Tan, "Industrial restructuring in the East Asian Newly Industrialising Economies and the implications for ASEAN and ASEAN-China Economic Relations", in Siow-Yue Chia, and Bifan Cheng, (eds.) *ASEAN-China Economic Relations: In The Context of Pacific Economic Development and Co-operation*, (Singapore: Institute of World Economics and Politics, 1992).

⁸⁰. Doug Tsuruoka, "No more Mr Nice Guy", *Far Eastern Economic Review*, (18 March, 1993), p. 46.

⁸¹. Ibid.

situation there, caused by soaring labour costs, and the cancellation of tax preferences.⁸²

The same story has been repeated with Taiwanese investment in Thailand. The Mint Shine Electrical Co., a Christmas tree light maker, for example, came to Thailand for its cheap labour to gain a competitive edge in 1988. Complaining that the minimum wage has jumped nearly 50 percent between 1989 and 1992, the company has decided to shift production to China.⁸³ Thai Sanho, a manufacturer of sports shoes, had to close its factory in Thailand in January 1993, because their competitive advantage from cheap production had been lost to their competitors in China and Indonesia. Moreover, Lynns Group, a maker of audio equipment, has gradually drained off much of its operation in Thailand. The group's factory in Shenzhen, China, is taking over more production.⁸⁴

The immediate effect of the redirection of investment to China is that foreign investment in Southeast Asian countries has decreased sharply. The Japanese, the biggest foreign investors in the region, have been lured by the Chinese "ultimate market" with its 1.2 billion-strong consumer market, the world's most attractive investment opportunity in the early 1990s.⁸⁵ Since 1990, Japanese investment in China has nearly tripled to a current annual rate of \$882 million.⁸⁶ The trend in Japanese direct investment in Asia seems to be away from Thailand and Indonesia, in favour of investment in China

⁸². *Central Daily News*, International Edition, (14 June, 1993).

⁸³. Gordan Fairclough, "Chopping the chopsticks: some labour-intensive firms flee Thailand", *Far Eastern Economic Review*, (18 March, 1993), p. 48.

⁸⁴. Although labour-intensive industries have escaped from Thailand, foreign investment has increasingly tended towards higher-technology industries. See Fairclough, "Chopping the chopsticks", p. 48.

⁸⁵. Brian Caplen, "An opportunity too good to miss", *Asian Business*, 28: 10, (October 1992).

⁸⁶. Yoko Shibata, "Japan's investment targets in Asia", *Global Finance*, 7: 2, (February 1993), p. 64.

and Vietnam.⁸⁷ It is yet to be proven to what extent these industries' withdrawal of capital from Southeast Asia has been encouraged from China. Nevertheless, clear evidence exists that the Taiwanese, another of the region's biggest investors, have also cut their investment in Malaysia, the Philippines and Thailand sharply in the last two years, as their eagerness to invest in China took off.⁸⁸ (Refer to the series of Figure in Appendix F-7.1 for details.) There is a tendency to blame China when questions are asked about the causes of this shift. Djisman Simandjuntak, executive director of Prasetiya Mulya, a business school in Jakarta, says "China must be the main factor (for its plunging foreign investment)."⁸⁹

Apart from competing for foreign investment, these countries have gradually been facing increasingly strong competition from Chinese exports in labour-intensive industries such as footwear, textiles, and electronics.⁹⁰ According to a shift-share analysis of competition amongst ASEAN, China and the ANICs in the Japanese market, for instance, the results suggest that ASEAN exports have suffered the most from the recent entrance of China into the Japanese market.⁹¹ In seven of the ten Standard International Trade Classification (SITC) categories, China has a competitive advantage, compared to ASEAN, especially in crude materials and machinery plus transport equipment. It is notable that the competition has mainly stemmed from their similarity in terms of economic development and their exports of labour-intensive industrial products.

⁸⁷. Joy M. Tadaki, "China and Vietnam tempting for direct investment", *Japan Times Weekly International Edition*, 33: 4, (25 January-31 January, 1993), p. 15.

⁸⁸. Julian Baum, "Taipei's offshore empire", *Far Eastern Economic Review*, (18 March, 1993), p. 45.

⁸⁹. "That sucking sound is China slurping up money", p. 19.

⁹⁰. "The spark plug of Asia's future", p. 30.

⁹¹. Fred Herschede, "Competition among ASEAN, China and the East Asian NICs: A shift-share analysis", *ASEAN Economic Bulletin*, 7: 3, (March 1993).

Another two studies have also discovered that China and ASEAN do compete directly for market shares in labour intensive industries, such as clothing, textiles, footwear, furniture, textile yarn, thread and toys, in the United States, Japan, other Asia-Pacific countries and Europe.⁹² The two economies have tended to pursue economic development by following the ANICs model of industrialisation through the export of labour intensive products to developed countries. Since the export markets for these products are restrained by worldwide economic recession and protectionist pressures from developed countries, it has been inevitable that tense competition has arisen between the two and has cast a shadow on their future relationship.⁹³ Although there is yet to emerge an obvious regional integration framework in the Asia-Pacific region, every subregional grouping has inevitably hinged on each others' development, because their common characteristic of outward-looking economic development, has, to some extent, tied them to the larger framework of an international industrial division of labour. Each developing grouping is likely to be acknowledged by others because of their mutual interests. The CEA has not been excluded from this linkage.

For the ASEAN countries, the possible economic impact of the CEA, whether positive or negative, deserves to be analysed further. As the CEA is a natural and "loose formation",⁹⁴ the governments' unwillingness, as of yet, to become involved in its formation implies that the current economic transactions, either inter-regional or intra-regional, will not be changed.

⁹². R. Tyers, P. Philips, and C. Findlay, "ASEAN and China exports of labour-intensive manufacturers: performance and prospects", *ASEAN Economic Bulletin*, 1: 3, (March 1987); John Wong, "Integration of China into the Asia-Pacific region", *The World Economy*, (September 1988).

⁹³. Kong Yam Tan, "Industrial restructuring in the East Asian Newly Industrialising Economies", pp. 190-191.

⁹⁴. Charng Kao, "A 'great China Economic Sphere': reality and prospects", *Issues and Studies*, 28: 11, (November 1992), p. 63.

So long as the CEA remains the concern of the private sectors, the increasing intra-regional economic ties are likely to accelerate Asia-Pacific regional economic cooperation to help along regional economic development. In the long-term, a strong Chinese economic group right next to the ASEAN would probably outweigh any other regional grouping and become the leader in the region. For now, the development of subregional groupings is likely to boost the de facto "Japanese Yen Bloc" in Asia-Pacific.

7.3. THE EMERGENCE OF REGIONALISM AND CHINESE ECONOMIC INTEGRATION

7.3.1. The Impact of the Single European Market on the Formation of the Chinese Economic Area

Owing to historic, geo-political linkage, and in particular market dependence, the US' market's importance to the CEA as well as to the other East Asian economies is relatively more notable than the ECs'. However, since the mid-1980s, owing to increasing protectionism in the US, a strategic demand of the ANICs for trade diversification away from the US markets has steadily increased their trade relationship with the EC.⁹⁵ Above all, the "graduation" of the ANICs from the US Generalized System of Preference (GSP) in 1989 has further reduced their dependence on the US.⁹⁶ While

⁹⁵. For example, Taiwan's exports to the US market accounted for 48.8 per cent of its total exports, its highest level, in 1984. Since then, as its efforts to diversify market dependence, Taiwan has steadily reduced its exports to the US to 32.4 per cent in 1990, and 28.9 per cent in 1992. On the other hand, Taiwan's trade with Europe has increased from 10.4 per cent in 1984, the lowest point, to 17.9 per cent in 1990, and 17.2 per cent in 1992. See *Taiwan Statistical Data Book, 1993*, Council for Economic Planning and Development, R. O. C.; *Economic Progress & European Trade of the Republic of China, 1993*, Euro-Asia Trade Organisation.

⁹⁶. C. H. Kwan, "The emerging pattern on trade and interdependence in the Pacific region", *Tokyo Club Papers*, 4, part 2, (1991), p. 145.

the ANICs export dependence upon the US accounted for 37.2 per cent of total exports in 1986, and 30 per cent in 1989, their export dependence upon the EC accounted for 10.6 per cent in 1985, and 13.9 per cent in 1989.⁹⁷ Taiwan's trade alone with North America, including the US and Canada, accounted for 37.6 per cent of total trade in 1983, and 27.5 per cent in 1992. In the same recorded period, Taiwan increased trade with the EC from 11.1 percent to 17.2 per cent.⁹⁸ While Hong Kong's exports to the EC, too, increased from 18.2 per cent of total exports in 1985, to 22 per cent in 1987, the US share of its exports declined from 44.4 per cent to 37.3 per cent.⁹⁹

In terms of export goods, the ANICs major export items to the EC are electronics, textiles, and shoes; more recently joined by office machines, stereos, and electrical equipment, whose prices the Europeans have found hard to compete with.¹⁰⁰ In addition, Taiwan, for example, has continuously enjoyed a trade surplus in trade with the EC, from US\$491 million in 1983 to \$1.48 billion in 1992.¹⁰¹ In the case of China-EC trade, China's rapidly increasing trade surplus against the EC was US\$10 billion in 1991 and about \$12.1 billion in 1993.¹⁰² Due to their continuous trade surplus against the EC and EC industry's failing to compete, the ANICs and China have been subjected to the EC protectionist backlash, anti-dumping actions in particular. Altogether, anti-dumping investigations initiated by the EC against Asian export economies comprised

⁹⁷. The import figure has also suggested the same developing trend. Information based on IMF, Direction of Trade Statistics and Taiwan's Monthly Statistics of Exports and Imports, see *Ibid.*, p. 140.

⁹⁸. Figures for Taiwan refer to Euro-Asia Trade Organisation, *Economic Progress and European Trade of the Republic of China 1993*, p. 27.

⁹⁹. Elaine Kurtenbach, "Dragons against the fortress", *International Management*, (October 1988), p. 62.

¹⁰⁰. *Ibid.*

¹⁰¹. See *Economic Progress and European Trade of the Republic of China 1993*, Euro-Asia Trade Organisation, p. 4.

¹⁰². See the IMF figures *Financial Times*, (25 February, 1994), p. 8.

half the 169 cases between 1987 and 1991.¹⁰³ In 1991, China was hit with four such investigations and Taiwan with two, while Hong Kong and South Korea were under another Brussels' anti-dumping investigation in their export of floppy disks.¹⁰⁴ Not satisfied with quota restrictions on Asian imports, recently, European textile makers, one of most dynamic lobbying groups, have tried to press the European Commission to step up anti-dumping investigations. An expert said that anti-dumping inquiries have always a "trade chilling effect", because even though they do not end in a fine, European importers would become reluctant to do business with firms subjected to the Commission's investigation and probable fine.¹⁰⁵

Although China's booming exports to the EC and the US may have partly resulted from the development of the CEA, as Taiwan and Hong Kong's producers have relocated in China, there is not yet a clear empirical survey on how much its two CEA partners have contributed to China's performance in foreign trade. In economic terms, while the EC has moved towards completing the single market and, at the same time, stepped up its protectionist actions against East Asian economies, the progress of Asia-Pacific regionalism in general and of the CEA in particular has been accelerated, as a result.¹⁰⁶ Of course, the development of the CEA has been characterised by both its defensive (increasing collective economic weight) and offensive (strengthening its competitiveness) tendencies towards regionalism elsewhere. The effects of the EC in 1992 on its trade partners in the developing world have been shown in trade creation and

¹⁰³. "If you can't beat 'em", *Far Eastern Economic Review*, (8 October, 1992), p. 71.

¹⁰⁴. Ibid.

¹⁰⁵. Shada Islam, "Textile trouble", *Far Eastern Economic Review*, (3 February, 1994), p. 50.

¹⁰⁶. This general trend has been notable in Asia-Pacific economic cooperation. See arguments in Lawrence Krause, "Trade policy in the 1990s I: goodbye bipolarity, hello regions", *The World Today*, 46: 5, (May 1990), pp. 83-84.

diversion effects. As European countries with the Single Market in place to strengthen competitiveness take on their competitors, there is likely to be a further redirection of trade away from European traditional suppliers and towards intra-EC trade.¹⁰⁷ In fact, the trade diversion effect of the EC's 1992 programme will be greatest for "low-value, undifferentiated, highly price-elastic goods, such as textiles, clothing, footwear, leather goods, electronic components, metals, chemicals."¹⁰⁸ Amongst all developing countries' groups, Asian NICs and ASEAN countries including China will be the worst losers facing the trade diversion effect of the EC's 1992 programme.¹⁰⁹

The general implication of the completion of the European single market for the CEA has been the EC's protectionist challenge and the challenge of competition.¹¹⁰ The EC's protectionism will be more discriminating in a new trade structure in granting preferences to neighbouring economies, such as the current members of the European Free Trade Association (EFTA), the Mediterranean countries of Turkey, Malta, and Cyprus, East European countries, and the Commonwealth of Independent States in various manners. Against this, there will be a most discriminated hierarchy of preferences against East Asian economies. As they compete with these preferred EC economies in a wide range of products the EC markets will turn bitter. Furthermore, the completion of the single market will inevitably result in a more rational competitive environment within the market itself. As a result, less competitive European industry will generate demands for

¹⁰⁷.See Michael Davenport and Sheila Page, *Europe: 1992 and the Developing World*, (London: Overseas Development Institute, 1991), p. 18.

¹⁰⁸.See Sheila Page, "Europe 1992: views of developing countries", *The Economic Journal*, 101, (November 1991), p. 1559.

¹⁰⁹.Ibid., p. 1560.

¹¹⁰.Soogil Young, "East Asia as a regional force for regionalism", p. 136.

increasing trade barriers, such as in addition to anti-dumping duties, local content, origin provisions, and financial assistance to selected industries, in order to regain competitive advantage against external competitors.

TABLE 7.5. ESTIMATIONS OF EC 1992 EFFECTS ON DEVELOPING COUNTRIES (million ECUs)

group of countries	trade diversion	total effect ^a
ACP countries	-477	361
Maghreb countries	-534	80
South Asia and China	-1125	-119
Asian NICs	-4077	-1491
ASEAN countries	-464	-18
Western Hemisphere	-751	246
OPEC	-847	1224

Asian NICs	creation	diversion	total effect (US\$ mil.)
Hong Kong	725	-735	193
Taiwan	1087	-1468	-262
South Korea	797	-1003	-75
Singapore	487	-759	-195

Note: ^a. The total effect is calculated together with regard to trade creation and diversion effects.

Source: Information is based on Page, "Europe 1992: views of developing countries", p. 1560; Michael Davenport, "Primary benefits", *Far Eastern Economic Review*, (13 June, 1991), p. 69.

Apart from European industry's demand for protection from outsiders' competition, the EC's willingness to encourage more exports from East European economies under special arrangements will do more harm to East Asian economies.¹¹¹ In addition, those export items of the ANICs that retain high similarity to the European counterparts' are much more likely to be subjected to protectionist practice. One economic research on the impact of the EC 1992 on Taiwan's exports, suggests that Taiwanese exports of textiles and clothing, for example, have met competition from the EC countries with regard to export similarity index: Italy with 73.96, Portugal

¹¹¹ Lawrence Krause and Soogil Young have expressed the same worry.

65.13, France 63.80, Greece 58.23, and Spain 58.22.¹¹² In terms of industrial sectors, the ANICs' and China's consumer electronics have been subjected to the strongest protectionist backlash in the EC (Table 7.5), not only because of strong industrial lobbying for protection, but because of their products' high similarity to those of the EC makers.¹¹³

In the face of this gloomy picture for Asian exporters with regard to the European Single Market, many have suggested the ANICs taking up some alternative policies: allying with European firms, making approaches to EC's neighbouring countries that have treaty gaining access to the EC, diversifying trade to other areas, reinforcing competitiveness by further restructuring, or expanding intra-Asia-Pacific trade.¹¹⁴ However, it seems that the likelihood of establishing a regional economic cooperation grouping is the "ultimate solution" for Asian economies.¹¹⁵ As far as the CEA is concerned, it seems that Taiwan and Hong Kong's interest is better served everywhere by integration into the CEA than separate from it. Apart from other marketing strategies, which Taiwan and Hong Kong's exporters may have sought for in order to gain access to the European market, the fundamental economic complementarity amongst the CEA economies provides their industries with a better opportunity to compete, in particular in labour-intensive industries. Persistent regional

¹¹².The ESI = 100 represents perfect similarity between analyzed economies' export structure, which would evoke competition. See Chien-nan Wang, and Jui-ling Hsu, "The Impact of the European Integration on Taiwan and Taiwan's Response", in 1992 Sino-European Conference on Economic Development: Impact of the European Integration and Response of Non-EC Countries, Chung-Hua Institute for Economic Research, Taipei, 6-7 May, 1992.

¹¹³.See Davenport and Page, *Europe: 1992 and the Developing World*, p. 42.

¹¹⁴.Peter J. Buckley, Hafiz Mirza, and Kate Prescott, "Europe 1992 and its impact on Pacific futures", *The Pacific Review*, 4: 4, (1991), p. 373.

¹¹⁵.Ibid; Soogil Young agrees with this suggestion. See his "East Asia as a regional force for globalism"; also Kym Anderson suggests East Asia economies need to club together with North American economies as a way of maintaining an open global trading system. See "Europe 1992 and the Western Pacific Economies", *The Economic Journal*, 101, (November 1991), p. 1549.

industrial restructuring processes and integrating complementary economies, therefore, will give economies in the region a brighter prospect for international trade.

7.3.2. Cooperation or Competition: the Effect of the North American Free Trade Area on the Chinese Economic Area

In terms of economic structure, European integration has taken the form of "horizontal integration", which integrates regional countries with nearly the same degree of economic development.¹¹⁶ NAFTA, by contrast, will progress on a complementary basis through a general vertical division of labour: on the one hand, the United States and Canada, providing advanced technology, capital, markets; Mexico, on the other hand, serving as a manufacturing base with low-cost labour. It is clear that after NAFTA was legally launched in January 1994, there is going to be a change of trade structure in the three economies, with the US and Canadian industries taking advantages of Mexico's cheaper labour rate, which would help them build up competitive advantage over their competitors elsewhere. Although the general American public, in particular trade unions relating to jobs being relocated in Mexico, retain doubts about the economic effect that NAFTA will bring about, the fact that industrial division of labour has taken place will benefit industries inside NAFTA.¹¹⁷ US Trade Representative Carla Hills stressed that NAFTA would, on

¹¹⁶.Tetsuo Naito, "North American Free Trade Agreement (NAFTA) and its influence on Asia", *RIM Pacific Business and Industries*, 2, (1993), 8.

¹¹⁷.The arguments around for and against the NAFTA became a public fuss in the US. All sides' arguments have been discussed in Gary Hufbauer, and Jeffrey Schott, *NAFTA: An Assessment*, (Washington, D.C.: Institute for International Economics, 1993). A clarified discussion the NAFTA myth and misconception is provided by William A. Orme, Jr. "Myths versus Facts: The whole truth about the half-truths", *Foreign Affairs*, 72: 5, (November/December, 1993), pp. 2-12.

the one hand, help the US companies compete with their Japanese and European rivals more effectively by using Mexico's cheaper labour through industrial collaboration, and would, on the other hand, guard against East Asians penetrating the US market through Mexico.¹¹⁸

The main contents of the NAFTA agreement have two noticeable features: tariffs to be abolished within 15 years and rigid country-of-origin regulations to be introduced (see Table 7.6). Before NAFTA comes into being, there are at present about 70 per cent of Mexican products entering the US market tax-free under the GSP, and the average tariff on the US imports from Mexico is already low at 3.4 per cent, (Canada 2.4 per cent for the Mexican products).¹¹⁹ Therefore, while tariffs will be abolished within NAFTA and be kept at the current rates for outsiders, it will not pose an immediate threat to East Asian exporters. However, NAFTA's regulations of country-of-origin highlight the group's protectionist propensity, which is likely to hit Mexico's East Asian investors hardest, particularly in the sectors of textiles, motor vehicles, and electronics and electric products. For example, clothing made in Mexico would have to use yarn or fibre made in North America rather than imported from East Asia.

Similarly, a range of consumer and industrial-electronic products ought to be equipped with printed circuit assemblies made in NAFTA.¹²⁰ For most Asian firms, the tight regulations of NAFTA will accelerate their efforts for internationalising production and will increase their foreign investment in

¹¹⁸ "New kid on the bloc", *Far Eastern Economic Review*, (27 August, 1992), pp. 50-51.

¹¹⁹ Figure was based on International Trade Commission, see Han Soo Kim, and Ann Weston, "A North American Free Trade Agreement and East Asian developing Countries", *ASEAN Economic Bulletin*, 9: 3, (March 1993), p. 289.

¹²⁰ Susumu Awanohara, "Not-so-fine print: NAFTA's details may exclude Asian traders", *Far Eastern Economic Review*, (24 September, 1992), p. 106.

TABLE 7.6. THE MAIN CONTENTS OF NAFTA AGREEMENT

Framework	Tariffs to be abolished within 15 years. Strict country-of-origin regulations to be introduced
Tariff	Every 5 years on item-by-item basis. In first 5 years, 90% of Mexico's exports to the US and 60% of US exports to Mexico to be covered.
Motor Vehicles	Tariffs on auto parts to be abolished in 5 years. Local content ratio to be set at 50% in first 4 years and at 62.5% beginning in the 9th year.
Electronic & Its Products	Use of certain parts produced in North America to be required for selected products such as computers (mother boards) and TVs (picture tubes).
Textiles	Import duties to be abolished within 10 years. Country-of-origin regulations to be tightened (use of yarn made in North America to be required).
Maquiladora	Tariff exemption system to be abolished by 2001.
Energy	Mexico's oil industry to be partially opened to foreign investment (oil field ownership prohibited).
Finance	Mexico's financial markets to be completely liberalised beginning in 2000. Companies in NAFTA area to be allowed to establish wholly owned local subsidiaries within the area.
Others	Agricultural produce, land transportation, telecommunications, investment, regulations, environmental protection, etc.

Source: Excerpted from Tetsuo Naito, "North American Free Trade Agreement (NAFTA) and its Influence on Asia", p. 9.

Mexico in order to benefit from access to the integrated market. Strict rules about country-of-origin will accelerate further integration of related industries within NAFTA at the expense of outsiders. A complementarity within the textile industry, for instance, between the American upstream makers

and the Mexican downstream makers will step up their collaboration and strengthening competitiveness against East Asian products. As a result, they will together discourage imports from outsiders, which would bring about the trade diversion effect for their trade partners. The American Textile Manufacturers' Institute went even further, appealing for 100 per cent North American content in imported textiles.¹²¹

The general picture of NAFTA drawn by the Agreement has worried exporters from the ANICs and ASEAN countries, because their similarity to Mexico in the stage of industrial development would lead to fierce competition.¹²² One study concludes that East Asian countries, the ANICs in particular, would be larger losers from the trade diversion effect than Latin American countries both in absolute and relative term, as a result of their export, high similarity to those of Mexico.¹²³ Indeed, World Bank economist Alexander Yeats says that Asian manufacturers of labour-intensive products such as textiles, toys, and footwear will suffer a trade diversion of up to US\$400 million a year.¹²⁴ Direct foreign investment heading towards a region aims partly to take advantage of regional integration, namely free trade and market scale, and partly to circumvent the possible trade barriers discriminating against outsiders. Therefore, there are reasons to believe that the formation of NAFTA will lure those inflows of foreign investment to Mexico, in particular those East and

¹²¹ "America's back door", *Far Eastern Economic Review*, (11 July, 1991), p. 44.

¹²² According to OECD reports, Mexico, along with the Asian four NICs, Brazil, Greece, Portugal, Spain, and Yugoslavia, was also classified as a NIC. See *The Impact of the Newly Industrialising Countries: on Production and Trade in Manufactures*, Report by the Secretary-General, (Paris: OECD, 1979); also *The Newly Industrialising Countries: Challenge and Opportunity for OECD Industries*, (Paris: OECD, 1988).

¹²³ See Kim, and Weston, "A North American Free Trade Agreement and East Asian developing Countries", p. 295.

¹²⁴ "New Kid on the bloc", p. 51.

Southeast Asian export-oriented investments targeting the US market, including those of companies originally US-investing in regional operations.

As far as the CEA is concerned, Taiwan's export dependence on the North American market has long been substantial. In 1990, Taiwan exported US\$25 billion to North America, which accounted for 38.7 per cent of its total exports. At the same time, while Hong Kong exported \$21 billion to North America which accounted for 26.3 per cent of its total, China's dependence on North America was the least with \$8 billion, about 11.6 per cent of its total exports.¹²⁵ It has become likely that Taiwanese and many foreign investors in the CEA targeting the US export market would be distracted in their industrial operation from the CEA by Mexico's privileges in NAFTA. According to the China Export-import Bank of the ROC, which offers loans and guarantees services for exporters, compared with the previous year the volume of Taiwanese enterprises' export insurance for investment in ASEAN countries and Vietnam doubled in the first four months of 1994. It increased six times for investment in Mexico in the same period.¹²⁶ Consequently, the investors from the CEA who would be forced to comply with NAFTA's strict local content regulations will have to produce many more of their components in North America. Whatever economic advantage or disadvantage this development will generate to the CEA economies eventually, the effect of NAFTA has stimulated industrial adjustment to reinforce competitiveness within the CEA, by bringing about increasing industrial integration.

Apart from the economic effect to be brought about by NAFTA, the potential expansion of NAFTA has more striking

¹²⁵ Information based on IMF, *Direction of Trade Statistics*, 1991.

¹²⁶ *Central Daily News*, International Edition, (31 May, 1994).

effects on the emergence of economic groupings in the Asia-Pacific region. "Enterprise Initiative for the Americas", a notion originally proposed by the former US President Bush in 1990 has developed into the lively concept of the "Western Hemispheric Free Trade Zone" which has won support from most Latin American governments.¹²⁷ The potentially protectionist NAFTA expanding to a western hemisphere trading bloc linking all parts of Latin America would pose even greater psychological threat to the system of open regionalism and free trade which the Asian-Pacific economies have long asserted. Already Latin America has been evolving into a cluster of free trade zones, customs unions, and various bilateral and trilateral free trade arrangements, such as Mexico-Chile-Venezuela Free Trade Agreement of April 1991, Mexico and five Central American countries free trade agreement of August 1992, the custom union of the Andes Common Market signed in September 1992, the South American Common Market signed in March 1991, and the Central American Economic Union in 1993.¹²⁸ Applauding the US Congress for ratifying the NAFTA agreement, Alejandro Foxly, the Chilean Finance Minister, said that Chile would be the next on the US free trade agenda. US officials also pointed out that Argentina and Venezuela are most likely to follow suit.¹²⁹

Accordingly, there appear to be two implications of the NAFTA expansion for economic development and regional

¹²⁷.The new US trade policy towards its neighbours in Latin America has been regarded as less confrontational. Stephen Fidler, "Where trade winds blow", *Financial Times*, (19 Novemebr, 1993), p. 25.

¹²⁸.For the development of American regionalism see Andrew Hurrell, "Latin America in the New World Order: a regional bloc of the Americas?", *International Affairs*, 68: 1, (January 1992), pp. 121-139. For all trade arrangements in Latin America see Susumu Awanohara, "Liberal infection: Asia concerned by pacts in the Americas", *Far Eastern Economic Review*, (10 September, 1992), pp. 73-74; Naito, "North American Free Trade Agreement (NAFTA) and its influence on Asia", pp. 11-12; *Financial Times*, (19 Novemebr, 1993), p. 25; also more recently Barbara Rudolph, "Free Trade fever", *Times*, (3 October, 1994), pp. 50-51.

¹²⁹.Stephen Fidler, "Where trade winds blow", p. 25.

integration in the Asia-Pacific region. Firstly, in response, the Asia-Pacific Economic Cooperation (APEC) has stepped up efforts to become the hub linking Asian economies and NAFTA. The Asia-Pacific export-led economies are more eager than ever before to seek for regional integration to assure their interests in open regionalism. By means of APEC tying up with NAFTA, the aspirations for pan-Pacific integration could serve regional economies' persistent goals for economic growth by securing free trade. Secondly, the emergence of subregional groupings represents the other level of regional integration by way of industrial restructuring. The increasing constraints imposed by NAFTA on the export-led economies in Asia-Pacific provide them with an impetus to carry out industrial restructuring and to collaborate industrially both at national and international levels, which would intensify prospects for regional integration. The emergence of the CEA has rightly reflected this development, as industrialists in the region have been pursuing the strength of their competitive advantage by international division of labour.

CHAPTER EIGHT

CONCLUSION: REGIONAL ECONOMIC INTEGRATION IN A WORLD OF INCREASING COMPETITION

Traditional theories of regional integration, derived from academic efforts to understand the establishment of the EC, do not cope well with actual developments, because of their neglect of external factors. This has handicapped their extension to practical application. While nowadays many of the problems of the world remain concerned with national development, social welfare and human well-being, individual economies have shown their enormous weakness in tackling those problems on their own. The emergence of a globally interdependent economic system has changed international regimes and has increasingly blurred national borders and the boundary of market and state.¹ In particular, in terms of economic and trade policy, national economies have become more vulnerable than ever before to external challenges. They therefore need wider frameworks other than national ones to cooperate with each other so that their interests may be assured and their problems may be solved collectively with more strength. The need for cooperation has provided a favourable impetus for the emergence of regional integration, or of "new regionalism" in a world of increasing competition.² Therefore, in the context of clustering regional groupings, we are bound to consider not only the internal processes which

¹. Changes in international regimes is referred to in the discussion in Robert O. Keohane and Joseph S. Nye, *Power and Interdependence*, 2nd edition, (Glenview, Illinois: Scott, Foresman and Company, 1989); Charles W. Kegley, Jr. and Eugene R. Wittkopf, *World Politics: Trend and Transformation*, 3rd edition, (London: Macmillan, 1989), p. 180.

². Norman Palmer argues that this emergence of regional blocs in an era of interdependence marks a new regionalism different from the old regionalism that appeared in the 1950s in Europe. See Palmer, *The New Regionalism in Asia and the Pacific*, (Lexington, Massachusetts: D. H. Heath and Company, 1991).

influence integrating economies but also the external effects of economic interdependence, such as international competition and trade disputes. These are what Keohane and Nye have argued to be the focal point of interdependence.³ Extending the notion of interdependence from states to regions, they argue that external factors should be taken into account in the process of regional integration.

8.1. EXTERNAL INCENTIVES, INDUSTRIAL DEVELOPMENT AND REGIONAL ECONOMIC INTEGRATION

Throughout this thesis, the "external incentives-industrial development" approach has stressed that regardless of the political scenario, the pursuit of regional economic integration will proceed as long as there is a strong demand for industrial restructuring by a group of economies in a region. In the 1970s, while the process of European integration was grounded by a combination of global recession, two oil crises, and an intergovernmentalist approach to European cooperation, the EC's economy as a whole suffered from poor economic performance and the disadvantages of an "uncommon market". Increasing international competition in productivity, development of technology, and market share, further weakened individual European industries in both European and world markets. Industrialists and politicians came to realise that their future economic strength would be at risk, unless they could pool their resources to complete the Internal Market. As a result, exogenous industrial restructuring regenerated the momentum for European integration. One politician states:

³. See Keohane and Nye, *Power and Interdependence*, pp. 6-11.

"[B]y the 80s, under the stimulus of competition from abroad, especially from Japan, and of the progressive return of European Governments to the principles of free markets, the process of integration shifted into high gear."⁴

When European industry sought competitive industrial strength by way of an expansion of industrial collaboration and proposed a single European market programme, its effect was to transform the previously sluggish pace of integration. Not only has European industry projected its European vision over economic development and integration, but also foreign investors, e.g. Japan, the USA and the ANICs, who have been looking on Europe as a single market for a long time, have assimilated a European business vision based on regional identities. Furthermore, industrial collaboration in the EC not only regenerated the momentum for European integration but also inspired a new type of regionalizing industrial competitiveness on which regional groupings elsewhere have hinged. Parallel to industrial development, the resumption of European political and economic integration has also provided a new framework for the study of regional integration through an analysis of industrial development in response to competition from abroad. Although successful negotiations between national governments contributed to legalising initiatives for European integration, European industrial demand for the completion of the Internal Market was more important for bringing forward political consensus on the need for further integration. Lord Young, the British former

⁴. Brian Mulroney, *Trade Outlook: Globalization or Regionalization*, Singapore Lecture, (Singapore: Institute of Southeast Asian Studies, 1990), p. 7.

Secretary of State for Trade and Industry, recalled in 1988 just that:

"[I]n the early 1980s no meeting of Heads of Government was completed, it seemed, without a call to action. But for a long time we did not get much beyond the rhetoric. Lord Cockfield's White Paper, completing the Internal Market, submitted to the Milan European Council in June 1985 was a major landmark, and the political impetus has accelerated since then."⁵

Against this background of a lack of political impetus between European governments for action, the Completion of the Internal Market Programme generated incentives for further economic and political integration. The relaunch of integration was demanded rather more for strengthening industrial development than for reforming the EC institutions.

This "external incentives-industrial development" perspective of regional integration has provided, if not invented, a more accurate tool for understanding the emergence of subregional groupings in the Asia-Pacific region. The development of regional groupings in Asia-Pacific has shown that though different from European forms and definitions of integration, especially without any existing supranational political frameworks, the process of regional economic cooperation is being facilitated by the demands for industrial development and economic growth in the face of industrial competition. It is far too early to establish a common political framework to regulate cooperation because there is a certain historical insufficiency of experience of cooperation in the region, and a lack of both a common goal for economic

⁵. Lord Young, "Creating a Single European Market I: a British view", *The World Today*, (March 1988), p. 38.

interactions, and political commitment to regional integration which as yet hardly exist amongst Asia-Pacific economies. It seems to be more accurate at this stage to use the term "economic cooperation" rather than "economic integration" in the Asia-Pacific region, as many economic interactions in the region are undertaken by means of cooperation at state-level or industrial sector-level rather than by integration of transnational institutions. Economic cooperation of subregional groupings in the Asia-Pacific region characterised by the private sectors' dynamics could, therefore, offer a new pattern of regional integration.

Michael Haas in his definition of "the Asian way" has pointed out that informal incrementalism stresses the "utility of noninstitutional frameworks for discussion, while operational activities are entrusted to organisations without elaborate constitutional specifications."⁶ Furthermore, stressing a principle of "primacy of economics over politics", Haas suggests that "Asian countries have gradually come to the realisation that they must work together economically on a truly multilateral basis ... " and "[A]lthough economic competition keeps prices of primary products down in the First World, cooperation serves the best economic interests of the developing countries of Asia."⁷ Accordingly, there is not and will not be, at least in the foreseeable future, extensive regional integration in Asia-Pacific leading to political integration. This proposition has hinged on the successful renovation of the world trade regime, but, certain notions of economic integration will prevail further as regional industry undertakes further cooperation ventures.

⁶. Michael Haas, *The Asian Way to Peace: A Story of Regional Cooperation*, (New York: Praeger, 1989), p. 8.

⁷. *Ibid.*, p. 19.

The emergence of the Chinese Economic Area, in particular, has been stimulated by intense global industrial competition, dynamic industrial momentum and economic complementarity, in spite of political difficulties. As far as the process of economic integration is concerned, the private sector, driving by the vision of establishing regional business complexes able to compete in world markets, has played the most important part in the formation of the CEA. This perspective takes major account of industry's role in the process of economic integration. In actual development, as economic complementarity has brought about the opportunity for industrial cooperation, industrialists in the CEA have been pressing ahead the agenda for economic integration. By contrast, traditional academic wisdom about regional integration has found itself incapable of explaining why the pace and momentum of integration are now motivated by external factors, generated by industrial development and led by the private sector.

In terms of industrial development and industrialists' attitudes, European integration was relaunched by the efforts of industrialists to campaign for the single market that would strengthen their industrial competitiveness, create more jobs, and develop high-technology. By contrast, while the decline of the ANICs' industrial competitiveness, in labour-intensive industries in particular, was largely due to the shortage of labour and rapidly rising production costs, the momentum of Asia-Pacific subregional groupings has been based on efforts to strengthen their competitiveness and so to maintain their economic growth. Moreover, in the CEA, the transnational corporations projecting their regional marketing strategy into the "greater China" area have produced a business vision of

regional identities, which has encouraged more interactions collaborating in technology development, management, personnel training and production through the TNCs' regional frameworks. As the TNCs have helped to organise the regional division of labour, they have served as an external impetus to regional integration.⁸

In terms of the issue of employment, while one of the major effects of the Single European Market is assumed to be the creation of more jobs, the CEA will allow Hong Kong's and Taiwanese manufacturers to gain convenient access to China's affluent labour markets. In the face of increasing competition in world markets, individual economies in the EC and CEA have become more willing to commit themselves to various programmes for industrial cooperation and market integration.

8.2. THE ESSENCES AND INCENTIVES OF EUROPEAN INTEGRATION AND CHINESE ECONOMIC INTEGRATION

According to traditional theories of integration, unless a certain degree of political cooperation, or a political framework, exists between relevant countries, integration will not be meaningful. Industrial development has contributed much to the revitalising of European integration, in particular to bringing forth national support for integration initiatives. Although the Single Market has not yet brought about the full benefits expected (in the single market's first year the EC's GDP decreased by 0.3 per cent and its unemployment rose to 10.5 per cent of the workforce),⁹ it is unlikely that European

⁸. "Lobby for free trade and removal of barriers to trade" is one of the positive contributions that the TNCs have had. See an assessment by Kegley, Jr. and Wittkopf, *World Politics: Trend and Transformation*, pp. 160-161.

⁹. "Survey: the European Union", *The Economist*, (22 October, 1994), p. 11.

economies would have performed better without the Single Market. One commentator has suggested that the EC has built "a Europe for business" by the commitment to the Single Market and now politicians should create "a Europe for people".¹⁰ While in the last decade the EC's task was to strengthen its competitiveness, on top of the effort for industrial strength the EC must now focus on social issues like unemployment and balancing regional development. Over all, industrial influence remains at the forefront in pushing ahead economic integration and social integration.

The assumption that industrial development and the activities of the private sector have stimulated economic integration has provided a new and systematic approach to account for the emergence of Chinese economic integration. The progress of the CEA has apparently and essentially been stimulated by flourishing business flows and the need for industrial development to face up to fierce industrial competition. The CEA has so far been limited to purely functional cooperation between China, Taiwan and Hong Kong in the face of existing political and external constraints. However, with regard to the progress of industrial development, China, Taiwan, and Hong Kong have already established de facto cooperation frameworks through business links. This de facto economic integration has appeared to be based on an industrial division of labour rather than political motives. This fact demonstrates that the economic cooperation of the CEA which has been taking place has not been based on political incentives, but on business incentives, i.e. comparative advantage and economic complementarity .

¹⁰. Jay Branegan, "Reinventing Europe", *Time*, (19 September, 1994), pp. 32-41.

The formation of the CEA aims at stimulating economic growth and the economic development of related economies. Industrial strategies of both the private and public sectors in the CEA for the 1990s and after are driving the CEA towards a closely tied economic framework. Given the fact that the private sector is leading the pace of economic integration, the CEA has been a result of appealing for more comprehensive cooperation in industrial development between Hong Kong, Taiwan and China. This business-driven process of economic integration in the CEA has come to challenge the traditional understanding of regional integration in Western Europe, according to which economic integration heads towards political integration and the process of economic integration is regulated and led by political actors.

This development of economic integration in the CEA is contrary to, particularly, European integration that has been based on a clear political agenda accompanied by economic frameworks in which the relationship and obligations of the EC and its member states are stipulated. The area of least similarity in the process of regional integration of the two regions has been the impetus of economic and industrial development. Although cultural homogeneity and the emergence of regional identity may have contributed to the essentials of regional integration in both cases, it has been the momentum of industrial development and industrialist intentions that have given the EC and the fledgling CEA a start.

While industrial development has boosted the momentum of European integration on the basis of a transnational political framework, the emergence of the CEA is entirely based on industrial development against the context of persisting political antagonism. As industrial development has brought

about a regional business identity and the impetus for economic integration, businessmen in China, Taiwan, and Hong Kong now want a further inter-national or trans-national business framework in order to expand their business ambitions and to assure their long-term interests inside and outside the CEA. A transnational economic complex other than national unification is more likely as the foreseeable future for the CEA.

APPENDICES

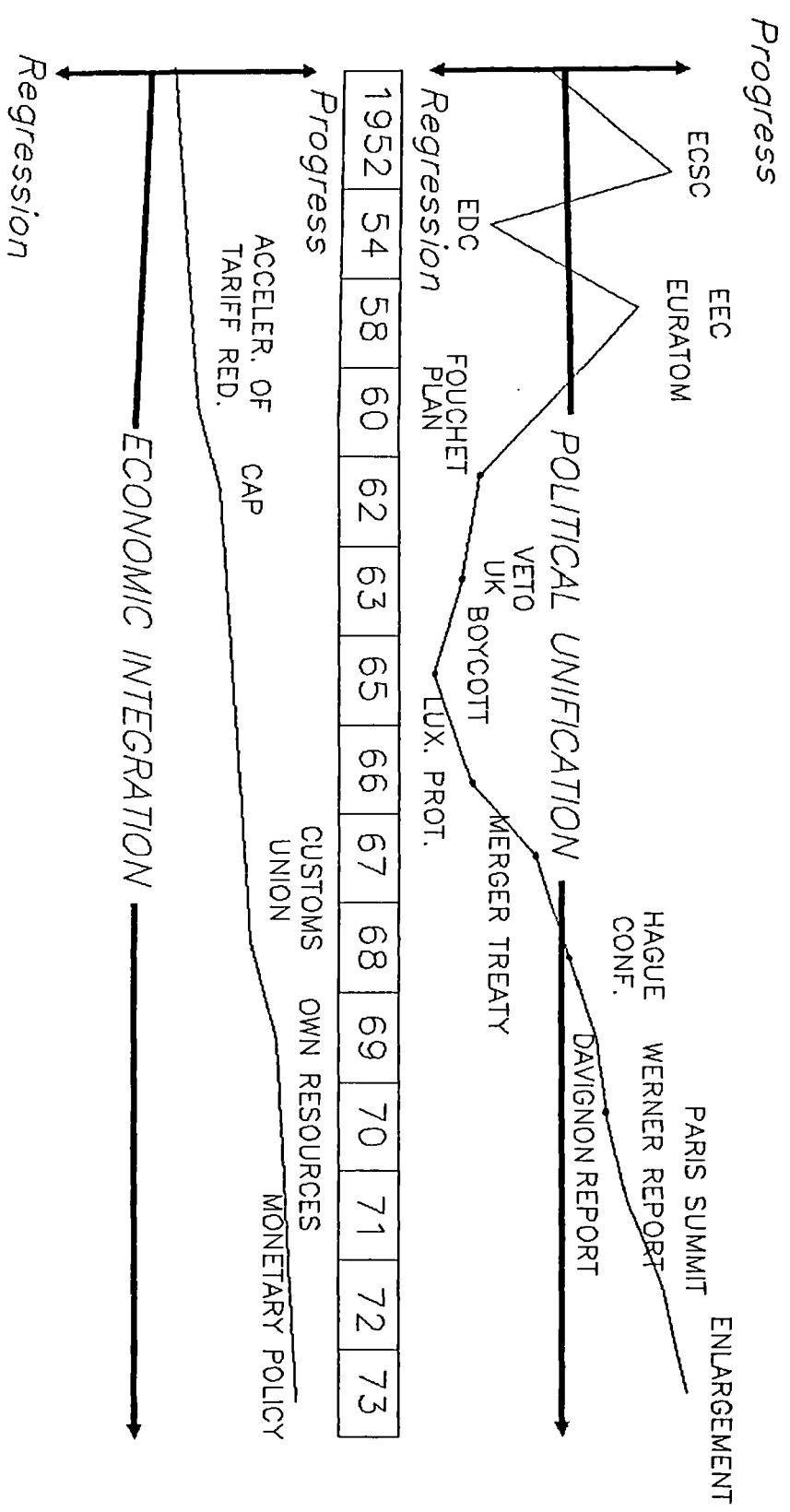
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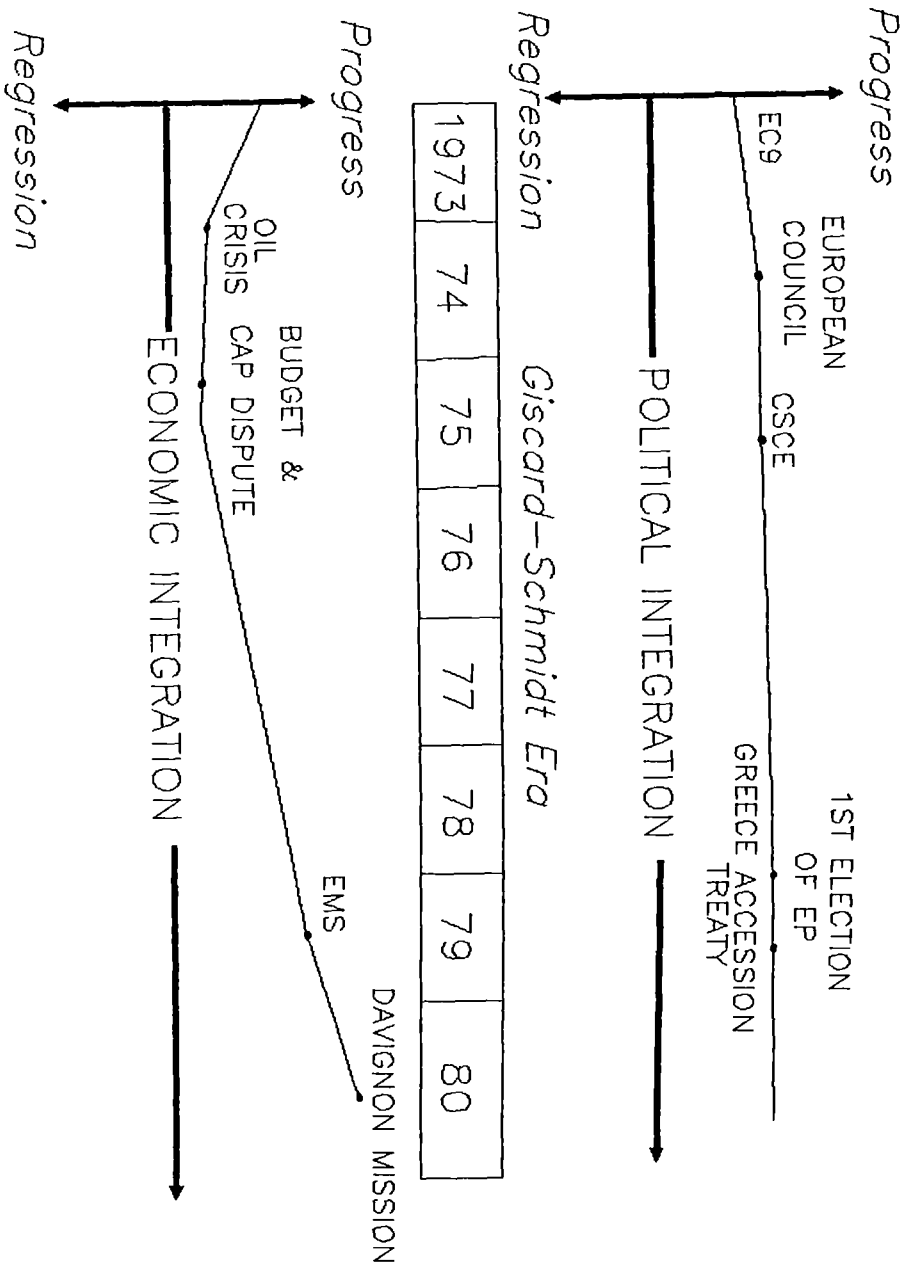
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APPENDIX. F-2.1. THE POLITICAL AND ECONOMIC DEVELOPMENT OF THE EUROPEAN COMMUNITY 1952-1973

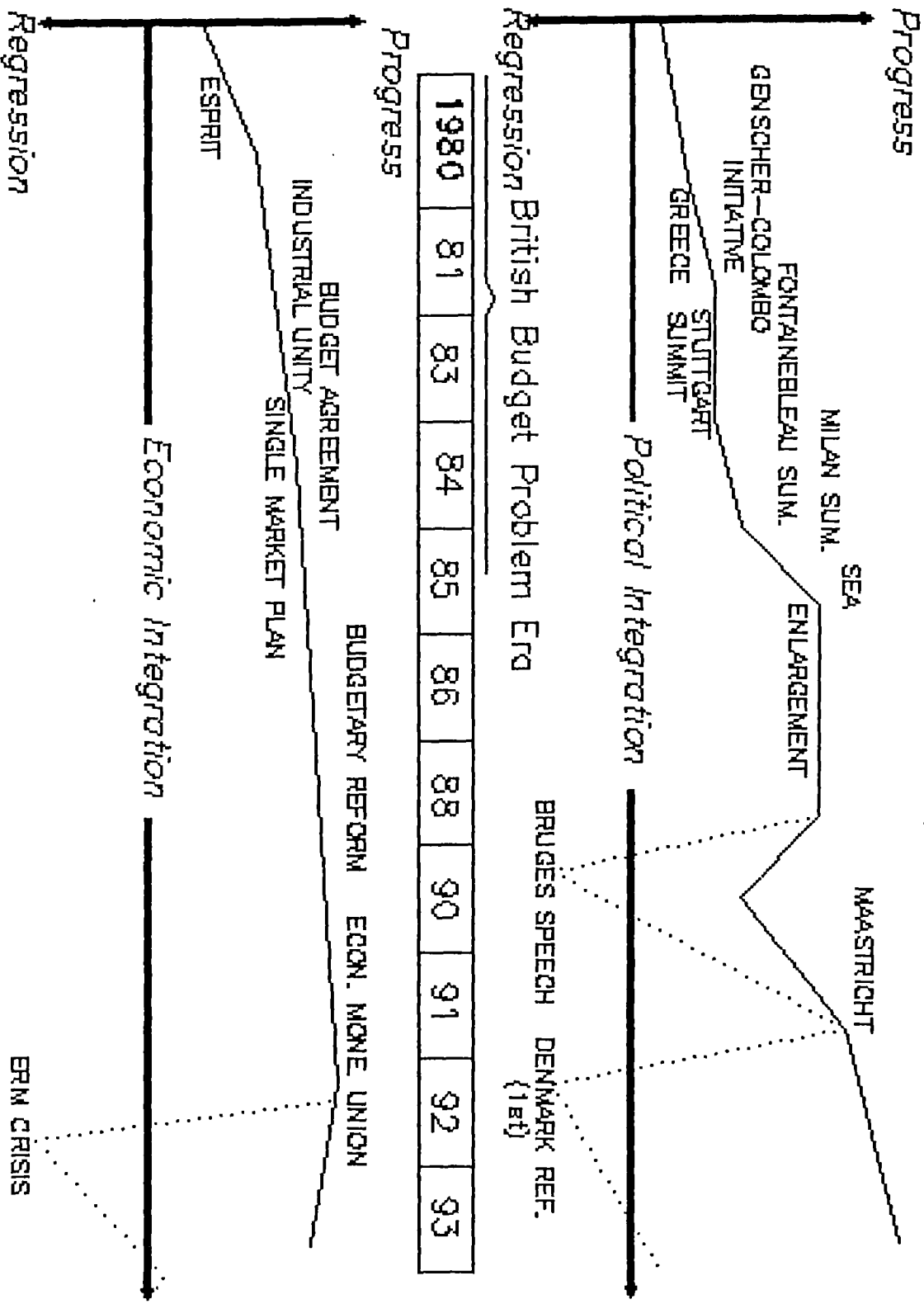


Source: G. Mally, *The European Community in Perspective*, p. 96.

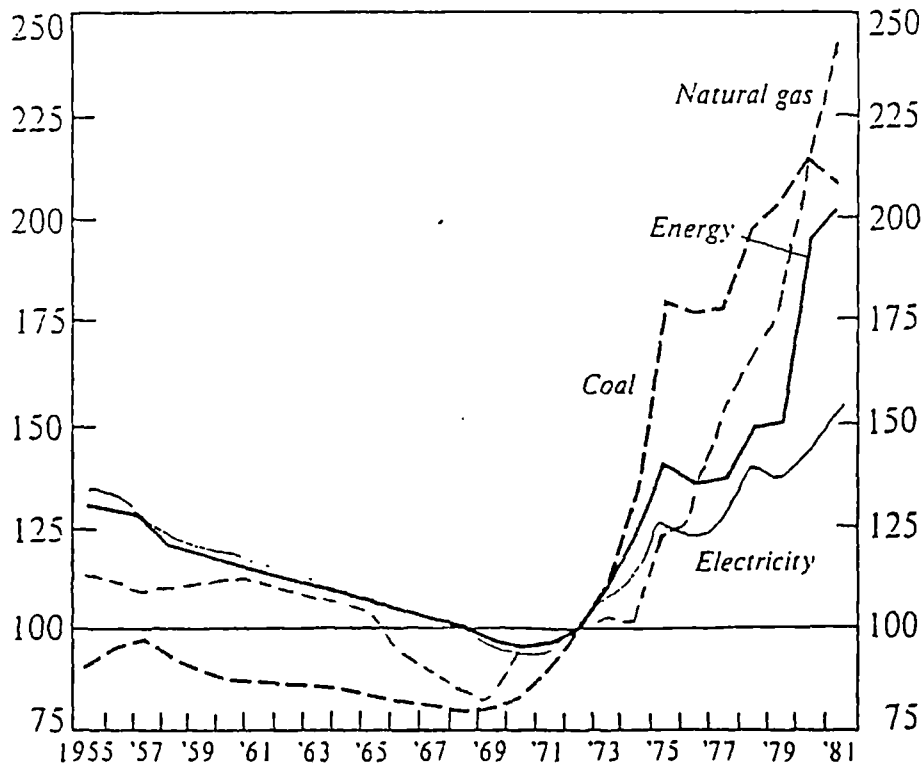
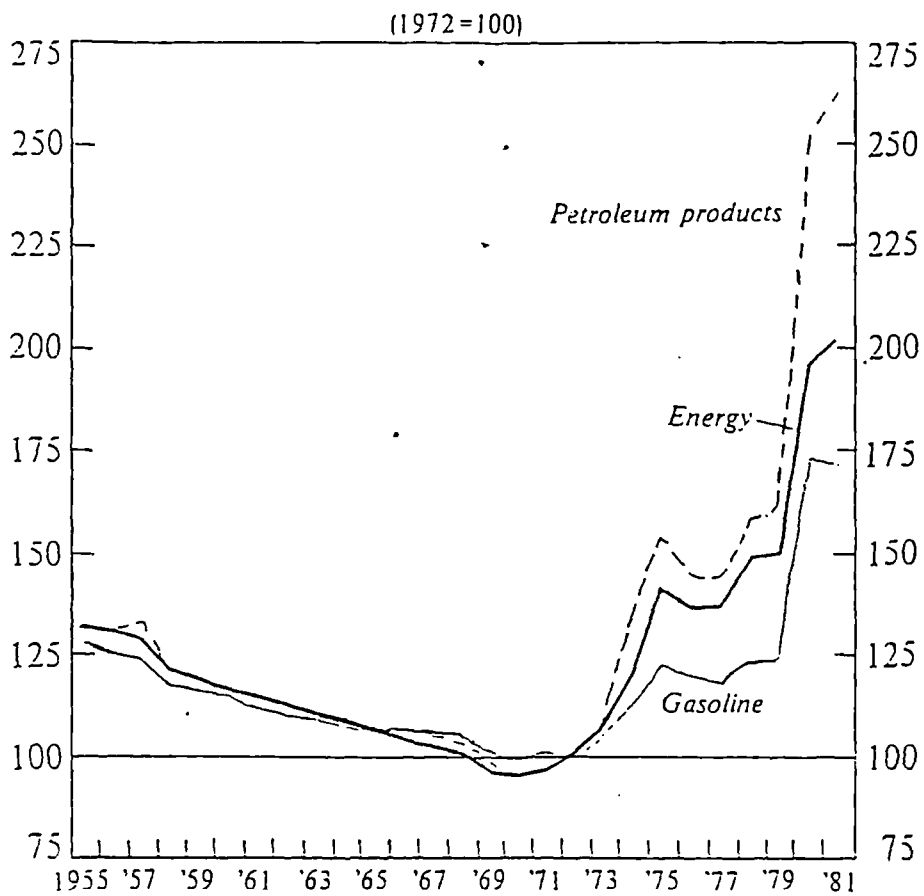
APPENDIX F-2.2. THE POLITICAL AND ECONOMIC DEVELOPMENT OF THE EUROPEAN COMMUNITY 1973-1980



APPENDIX F-2.3. THE DEVELOPMENT OF THE EUROPEAN COMMUNITY 1980-1993

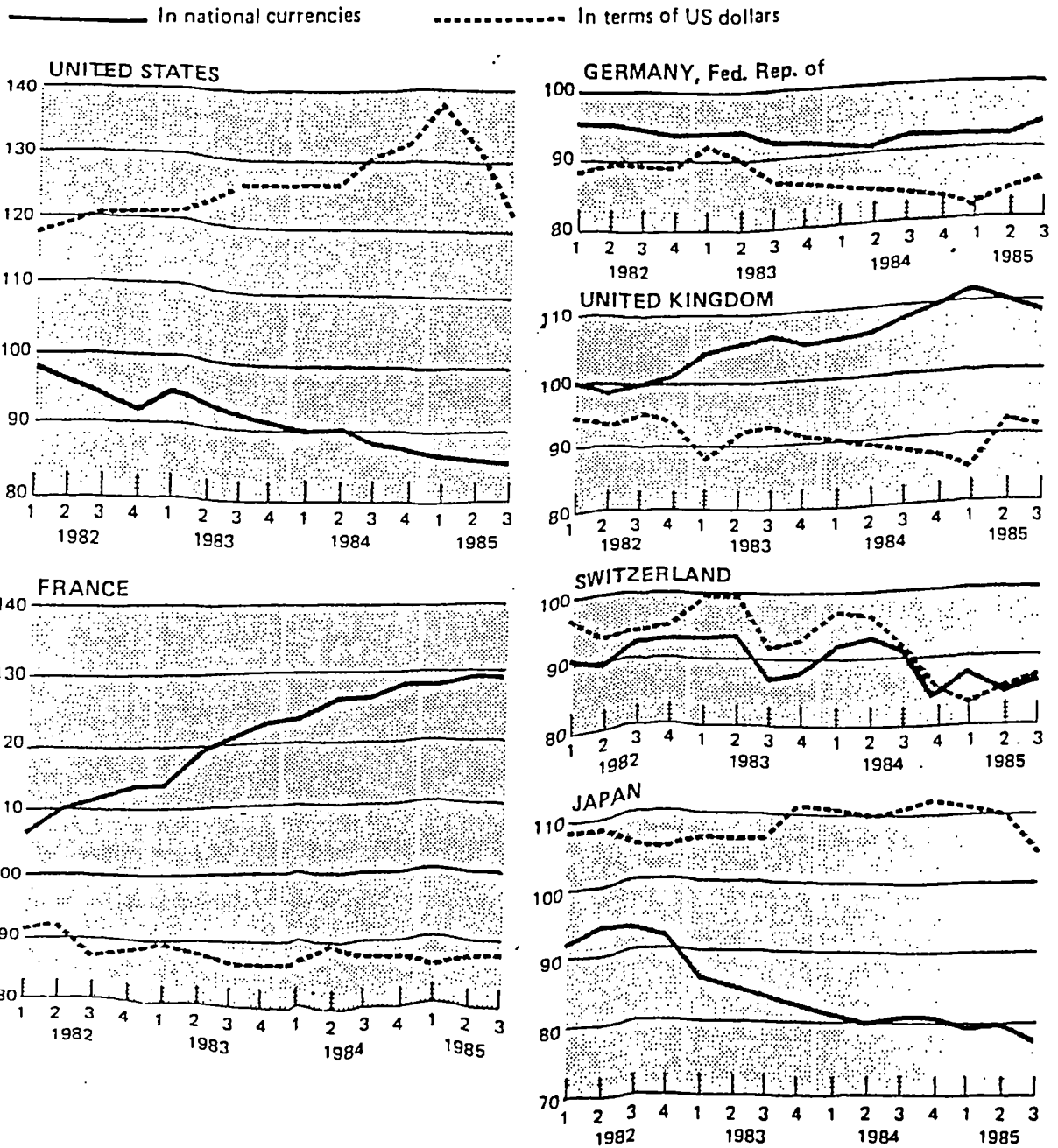


APPENDIX F-2.4. INDUSTRIAL COUNTRIES: REAL USER PRICES OF ENERGY AND ENERGY PRODUCTS, 1955-81



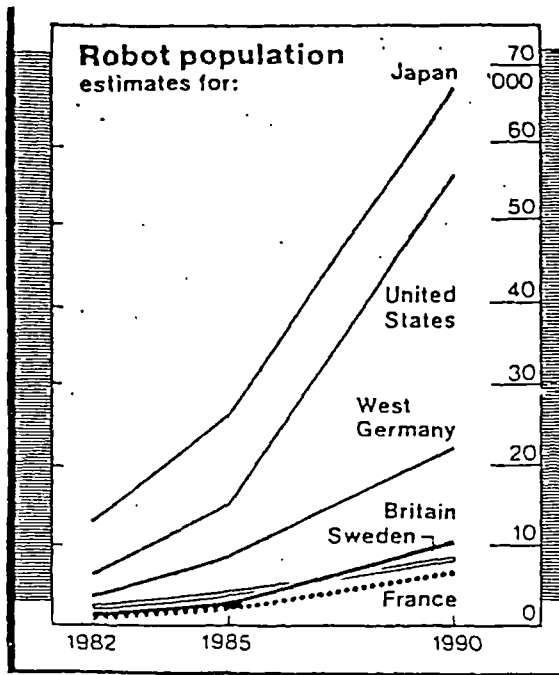
Source: IMF, *World Economic Outlook 1981*.

APPENDIX F-2.5. RELATIVE UNIT EXPORT VALUES (1980=100)



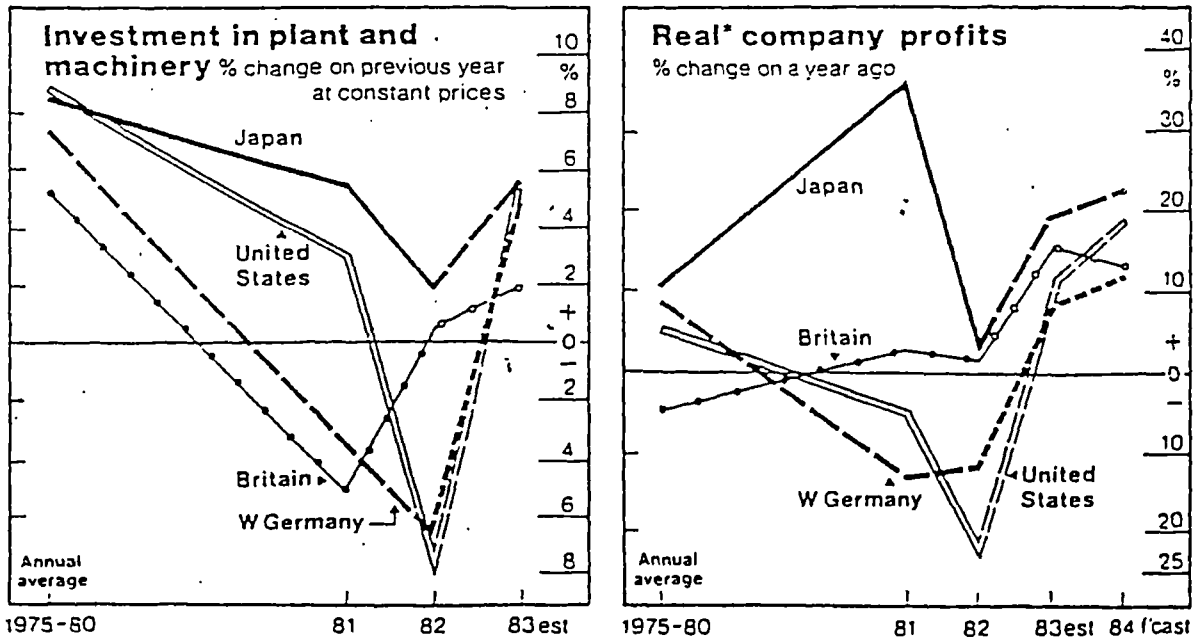
Source: Based on IMF, *International Financial Statistics*, (January 1986), *Economic Survey of Europe in 1985-1986*, UN.

APPENDIX F-3.1. A WORLD OF ROBOTS



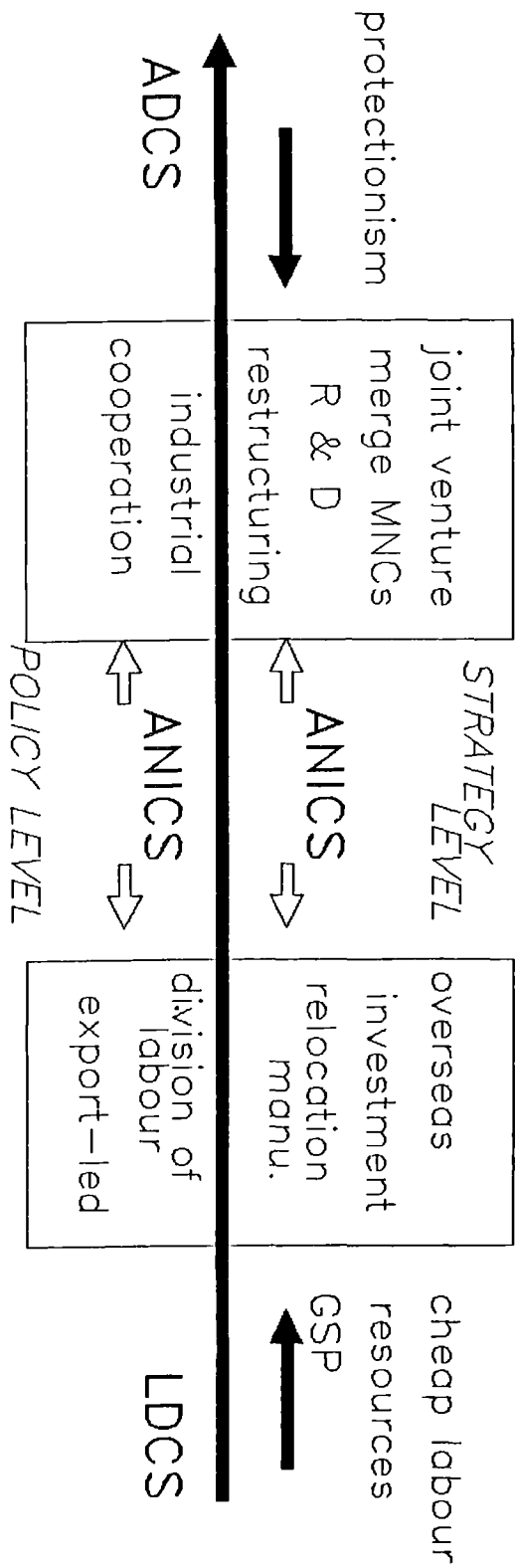
Source: *The Economist*, (24 March, 1984), p. 68, based on Merrill Lynch, OECD.

APPENDIX F-3.2. PAYING FOR TOMORROW'S WORLD

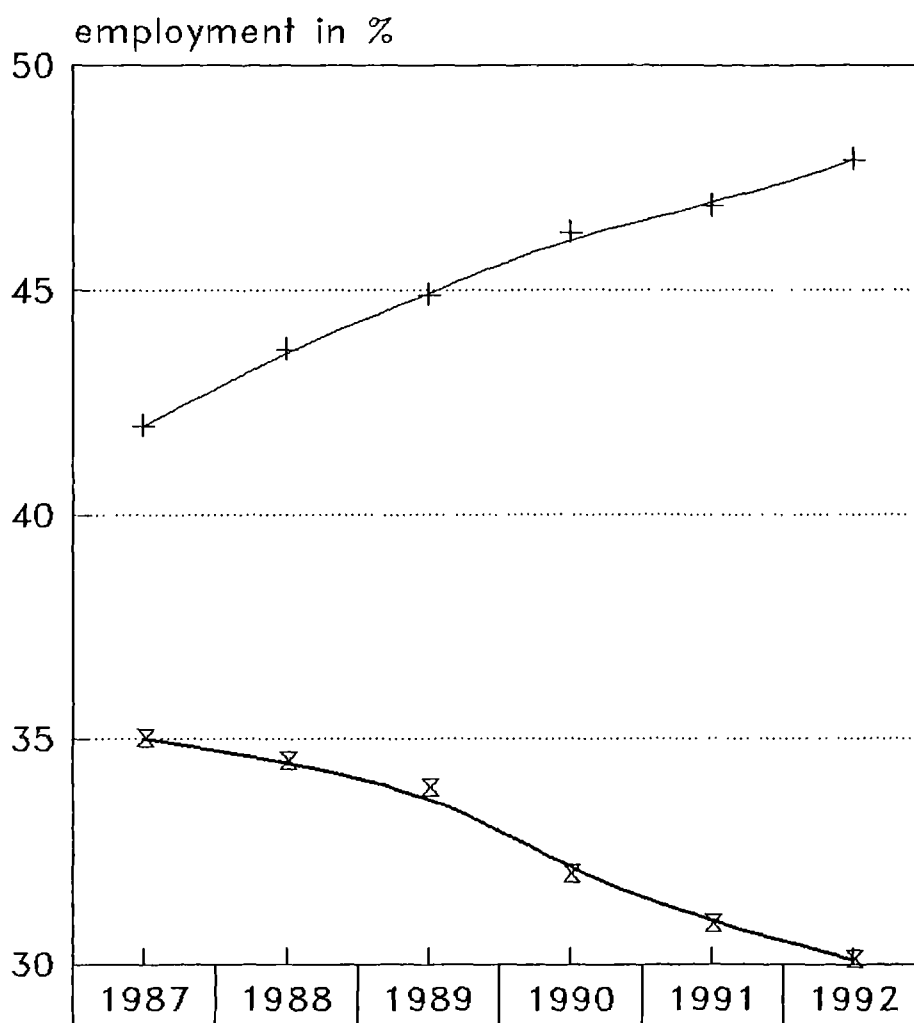


Source: *The Economist*, (24 March, 1984), p. 68, based on Philips and Drew, OECD, US Dept of Commerce.

APPENDIX F-4.1. THE TRADE STRUCTURE OF
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APPENDIX F-5.1. EMPLOYMENT BY INDUSTRY IN TAIWAN : MANUFACTURING AND SERVICES

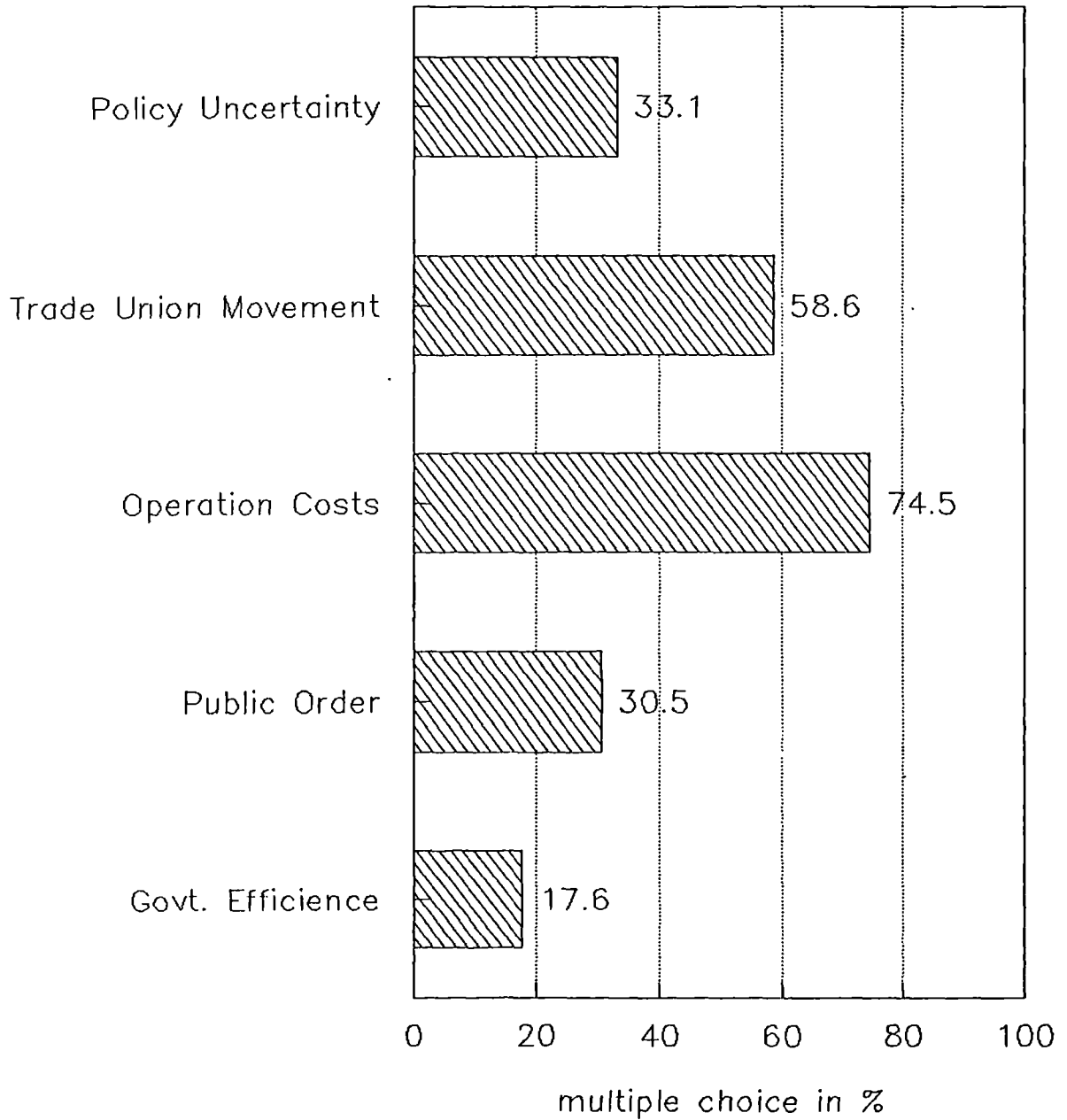


Services	42	43.7	44.9	46.3	46.9	47.9
Manufacturing	35	34.5	33.9	32	30.9	30.1

—x— Manufacturing —+— Services

Source: Directorate General Budget, Accounting and Statistics, R. O. C., 1993.

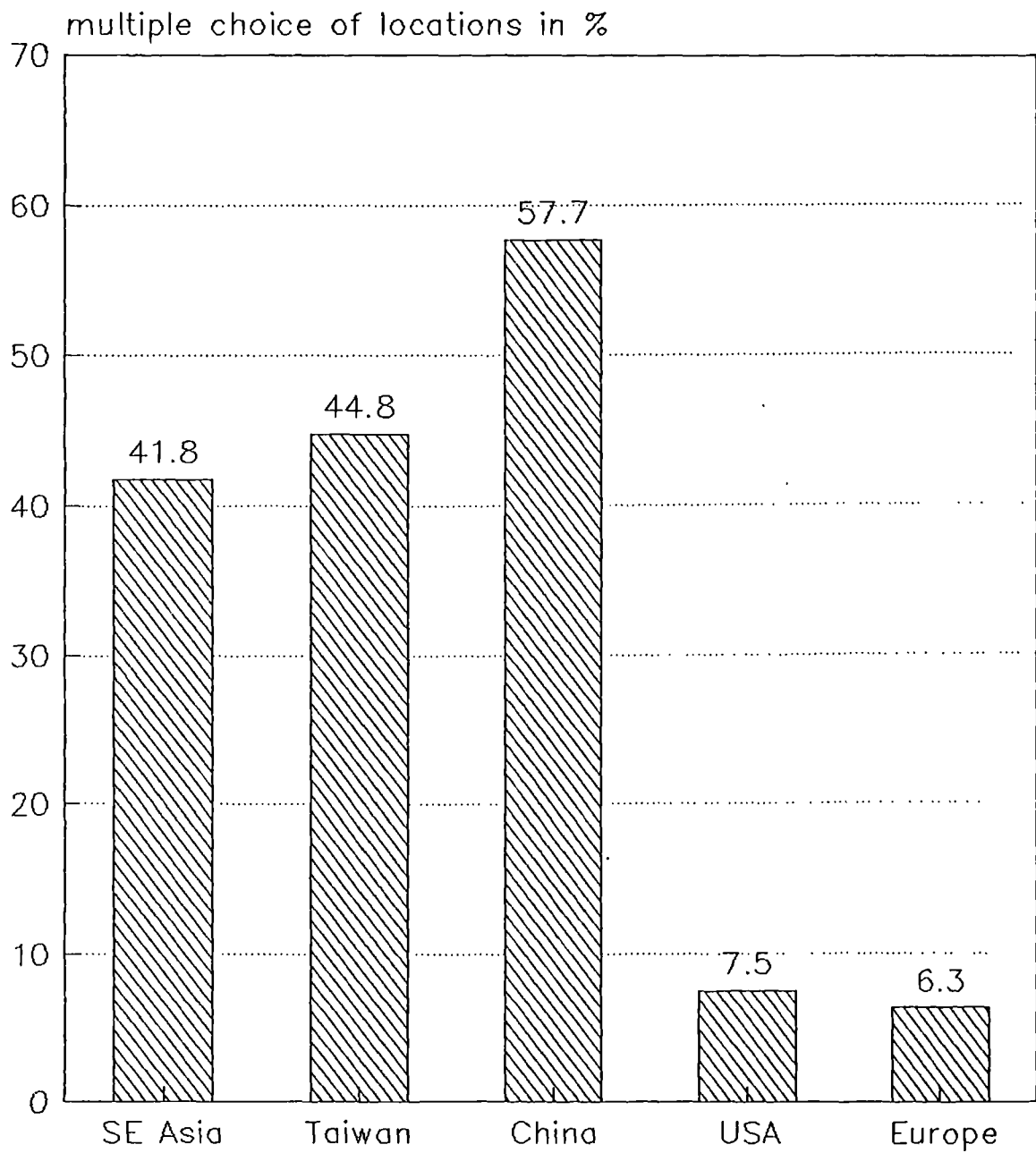
APPENDIX F-5.2. DISADVANTAGEOUS FACTORS OF INVESTING IN TAIWAN



Note: A survey of questionnaire answered by 1000 enterprises in Taiwan

Source: *Commonwealth*, (1 March, 1992).

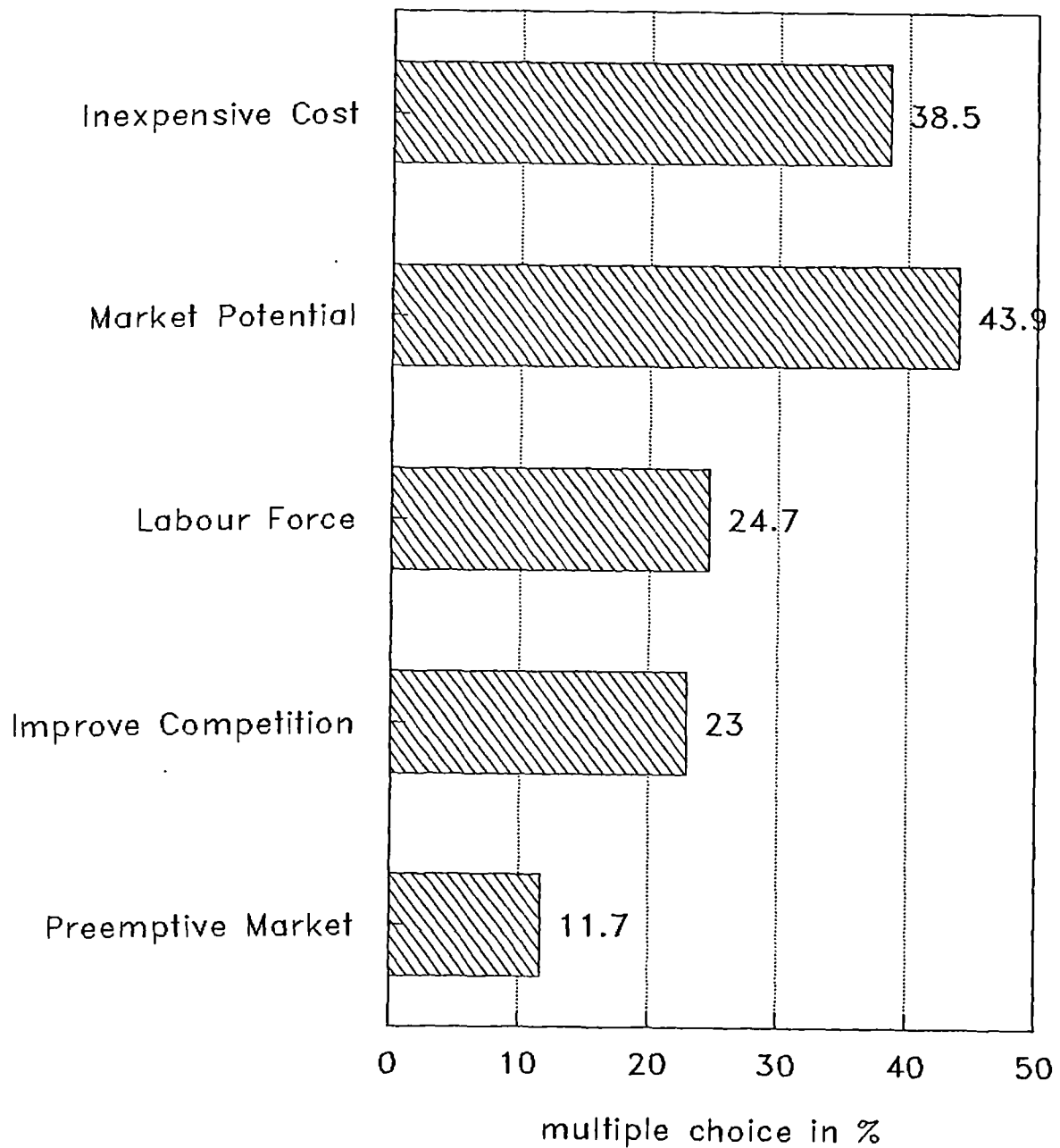
APPENDIX F-5.3. IDEAL LOCATIONS FOR TAIWAN ENTERPRISES: INVESTMENT TRENDS



Note: Information basis as in F-5.2.

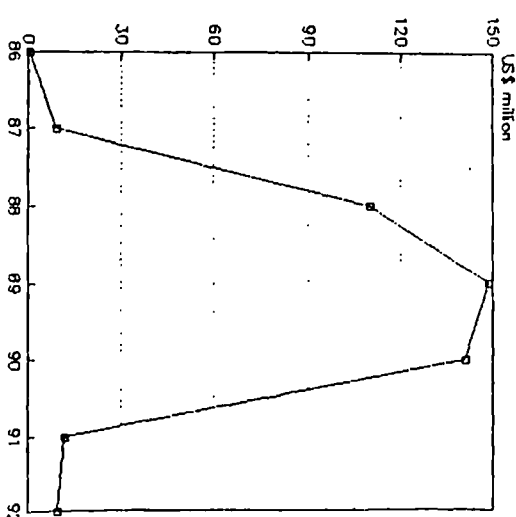
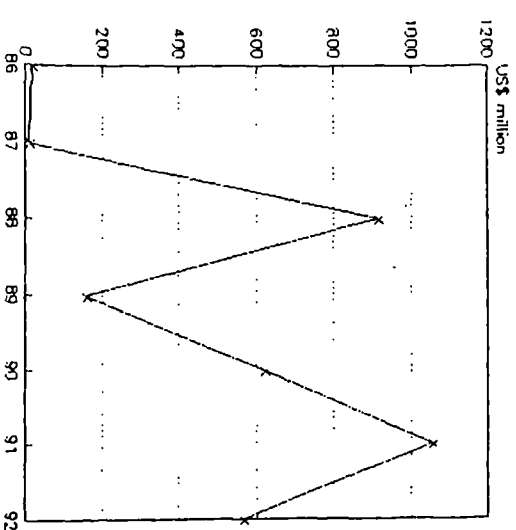
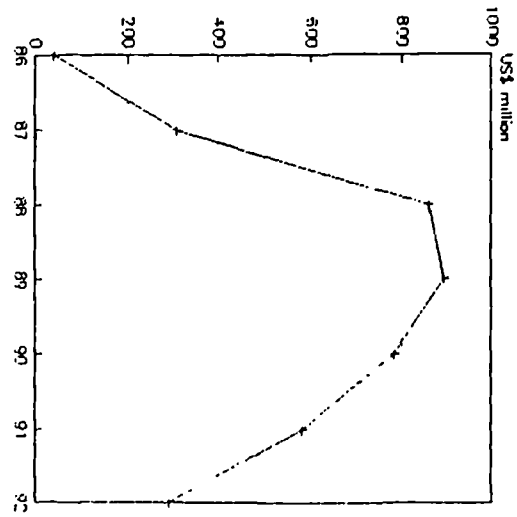
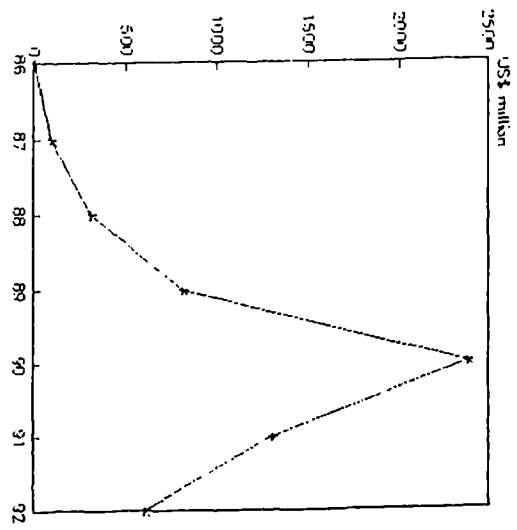
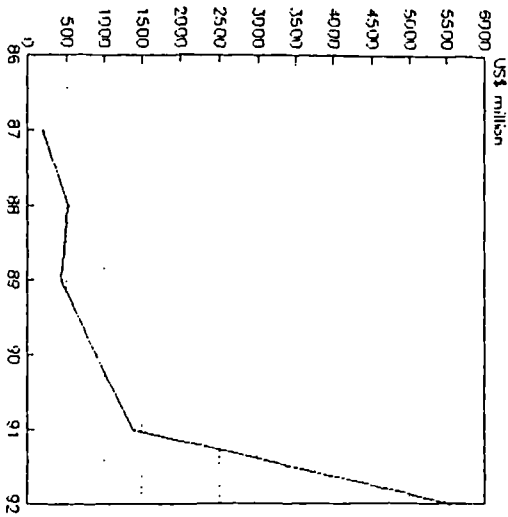
Source: *Commonwealth*, 1 March, 1992.

APPENDIX F-5.4. THE MOST IMPORTANT
FACTORS OF TAIWANESE INVESTING IN
CHINA MARKET



Note: Information basis as in F-5.2.
Source: *Commonwealth*, (1 March, 1992).

APPENDIX F-7.1. TAIWAN'S APPROVED DIRECT INVESTMENT IN
CHINA AND SOME ASEAN COUNTRIES



Source: Ministry of Economic Affairs, R. O. C.

APPENDIX T-2.1. CONSUMER PRICE INDEX NUMERS IN THE EC,
JAPAN AND THE US (all items 1980=100)

country \Year	1977	1978	1979	1981	1982	1983	1984	1985	1986
B	86	90	94	108	117	126	134	141	142
DM	74	81	89	112	123	132	140	146	152
F	73	80	88	113	127	139	149	158	162
FRG	89	91	95	106	112	116	118	121	121
GR	60	67	80	125	151	181	214	256	315
IR	69	75	85	120	141	156	169	178	185
I	64	72	83	118	137	157	174	190	202
L	87	90	94	108	118	128	136	140	140
NL	71	73	77	87	92	95	98	100	100
P	57	69	86	120	147	184	238	284	317
SP	62	75	87	115	131	147	164	178	194
UK	69	75	85	112	121	127	133	142	146
EC9	76	81	88						
EC10				111	124	136	147		
EC12								170	181
US	74	79	88	110	117	121	126	131	133
JAP	86	90	93	105	108	110	112	115	115

Source: The United Nations, *Statistical Yearbook 1985/86*.

APPENDIX T-2.2. THE EUROPEAN COMMUNITY: THE GROWTH RATES
OF OUTPUT, EMPLOYMENT AND INVESTMENT, 1950-70

	output GDP	employment	investment
Belgium	3.5	0.4	22.4
Denmark	4.0	1.1	21.0
France	5.0	0.4	23.7
Germany	6.2	1.2	27.0
Greece	6.0	0.9	23.1
Ireland	2.5	-0.7	21.9
Italy	5.4	0.4	22.1
Netherlands	5.0	1.1	26.0
Portugal	5.1	0.2	18.8
Spain	6.1	0.8	22.6
UK	2.7	0.5	17.5

Source: Derek Aldcroft, *The European Economy 1914-1990*,
3rd edition, (London: Routledge, 1993), p. 140.

APPENDIX T-2.3. GROWTH RATES OF GROSS DOMESTIC PRODUCT AND EMPLOYMENT 1950-1987

	1950-1973			1973-1987		
	GDP	Employment	GDP/EM	GDP	Employment	GDP/EM
EC12	4.7	0.6	4.1	1.9	0.1	1.8
USA	3.7	1.5	2.2	2.5	1.9	0.6
Japan	9.6	1.7	4.1	3.8	0.8	3.0

Source: As T-2.2.

APPENDIX T-2.4. THE EC12 ECONOMIC PERFORMANCES 1960-1990

	1973/60	1980/73	1985/80	1990/85
Real GDP	4.8	2.2	1.5	3.1
Employment	0.3	0.1	-0.4	1.2
Investment	5.6	0.3	-0.6	5.7
prices	4.6	12.4	8.8	4.1

Source: Commission of the European Communities, *European Economy*, 42, (1989), p. 111.

APPENDIX T-2.5. UNEMPLOYMENT RATE: THE EUROPEAN COMMUNITY, USA AND JAPAN (percentage of civilian labour force)

	EC12	USA	JAPAN
1964	1.9	5.2	1.2
1966	2.0	3.8	1.3
1968	2.7	3.6	1.2
1970	2.4	4.9	1.2
1964-70	2.3	4.2	1.2
1972	2.8	5.6	1.4
1974	2.8	5.6	1.4
1976	4.7	7.7	2.0
1978	5.3	6.1	2.3
1980	6.0	7.1	2.0
1971-80	4.1	6.4	1.8
1982	9.0	9.7	2.4
1984	10.7	7.5	2.7
1986	10.7	7.0	2.8
1988	9.7	5.5	2.5
1990	8.5	5.4	2.2
1981-90	9.6	7.1	2.5

Source: Commission of European Communities, *European Economy*, 46, (December 1990).

APPENDIX T-3.1. MANUFACTURING OF MAJOR INDUSTRIAL COUNTRIES

	1975	1980	1983
USA value added/na (in million dollars)	369056 /c	442691 /c	458479 /c
value added (in million dollars)	440770	789900	...
industrial production index	100	124	123
gross output (in million dollars)	1038100	1857100	...
employment (in thousands)	17108	19210	20385
UK value added/na (in million dollars)	68638 /c	53818 /c	50874 /c
value added (in million dollars)	82067	163791	...
industrial production index	100	96	92
gross output (in million dollars)	204578	420814	...
employment (in thousands)	7394	6462	5303
J value added/na (in million dollars)	150316 /c	215061 /c	228356 /c
value added (in million dollars)	157028	340748	363496
industrial production index	100	135	140
gross output (in million dollars)	435780	974895	1002810
employment (in thousands)	10565	10253	10426
I value added/na (in million dollars)	55667 /c	74879 /c	87463 /c
value added (in million dollars)	51010	97231	...
industrial production index	100	130	120
gross output (in million dollars)	122836	251426	...
employment (in thousands)	3582	3333	3124
FRG value added/na (in million dollars)	158655 /c	187568 /c	177119 /c
value added (in million dollars)	144279	268948	207599
industrial production index	100	121	116
gross output (in million dollars)	291402	633333	494516
employment (in thousands)	7284	7229	8576
F value addea/na (in million dollars)	102051 /c	114733 /c	111708 /c
value added (in million dollars)	92827	170308	130193
industrial production index	100	113	110
gross output (in million dollars)	223551	430142	317767
employment (in thousands)	5325	5058	4712

Source: Industry and Development Global Report 1991/ 92, UNIDO.

APPENDIX T-3.2. PATENTS: APPLICATIONS, GRANTS, PATENTS IN FORCE

country & area	application for patents				grants of patents				patents in force			
	1975	1982	1983	1984	1975	1982	1983	1984	1975	1982	1983	1984
B	13224	3858	3066	2835	13144	3826	3031	2764	125158	81304	72332	64499
DM	5959	5801	6087	6278	2423	1530	1155	1089	16944	...	10625	...
F	40437	22242	21176	20200	14320	23144	25043	23666	351912	285848	264556	353683
FRG	60095	47826	47103	45209	18290	16306	20913	21758	125863	136723	137220	137638
GR	2981	3260	3211	3490	1831	2236	2183	9153	...	...	...	...
IR	2844	3110	3094	3372	979	1083	1020	1152	5864	8065	7856	7791
I	...	...	12080	11519	...	...	1049	1900	...	...	...	...
L	2548	710	...	554	1885	574	...	554	15230	12392	...	16955
NL	15267	5085	4500	3979	3845	6653	8361	10257	22311	28043	32403	38236
POR	1467	1826	1851	1852	3035	1213	1200	637	...	1863	3036	3955
SP	10522	10201	9850	10700	9258	9710	8806	8213	54500	...	...	...
UK	53400	37093	34691	32828	40689	29590	28254	18867	249671	228067	229549	222558
JAP	159821	235324	252685	282314	46728	5060	54701	61800	...	404293	419143	439489
US	101014	109625	103703	111284	71994	57889	56862	67201	1060230	1199526	1193527	1192322
BRA	8794	7678	7202	6719	911	10074	6061	4887	...	...	...	...
H K	629	711	892	830	605	558	740	1010	...	...	...	...
S K	2914	5924	6394	8633	442	2607	2433	2365	...	8346	9960	11979
MEX	...	4806	4095	4003	...	2583	2247	1737	...	36659	38706	40331
SIN	...	648	857	931	...	519	391	...	...	8707	9098	...

Source: World Intellectual Property Organisation (Geneva).
Quote : Statistical Yearbook 1985/86, UN.

APPENDIX T-3.3. INDUSTRIAL DESIGN: APPLICATIONS, REGISTRATIONS GRANTED, REGISTRATION IN FORCE

	Applications for regist.				Registrations granted				Registrations in force			
	1975	1982	1983	1984	1975	1982	1983	1984	1975	1982	1983	1984
DM	1001	1234	1259	1189	876	1015	1043	1040	6715	7366	7338	7403
F	4175	4660	5013	5971	12177	13089	13813	15937	140000	174000	182000	191000
FRG	2979	4247	...	...	56840	65958	66118	67680	4389	...	...	...
IR	230	395	365	403	210	298	372	400	1109	1958	2073	2254
I	...	...	9637	10300	...	...	19	316	...	...	...	...
POR	374	571	540	658	482	233	153	421	...	...	...	...
SP	3967	2632	2477	2641	3458	2070	3033	1896	17860	...	...	...
UK	4730	6233	6792	7237	3019	4450	6878	6697	34141	35640	38310	39827
JAP	52250	59390	57618	54683	34829	33499	32237	34191	118619	271401	276399	282593
US	6269	8174	8082	8739	4282	4944	4564	4938	43258	52850	54306	56169
BRA	...	994	1340	1323	...	787	645	415	...	...	...	...
S K	6707	11902	13947	15870	1589	4751	6367	7108	12253	18370	21647	23813
MEX	...	521	444	630	...	327	320	254	...	1835	1846	1544

Source: Statistical Yearbook 1985/86, UN.

**APPENDIX T-3.4. EXPORT MARKET SHARES OF SELECTED
COUNTRIES IN HI-TECH PRODUCTS (current ECU in %)**

	EUR 12	USA	JAPAN	EFTA	TOTAL
I. Aerospace					
1978	44.9	49.5	0.8	4.8	100
1980	61.3	35.7	0.6	2.4	100
1982	56.5	39.5	1.1	2.8	100
1984	53.7	42.5	0.9	2.9	100
1986	49.9	45.2	1.1	3.8	100
II. Automatic data-processing equipment & machines					
1978	30.8	57.7	9.9	1.6	100
1980	30.7	58.0	9.6	1.7	100
1982	25.7	54.2	18.7	1.5	100
1984	20.3	43.0	35.5	1.2	100
1986	26.7	22.0	49.2	2.1	100
III. Electronic equipment					
1978	31.8	42.1	22.7	3.4	100
1980	26.5	44.8	25.4	3.3	100
1982	23.4	46.4	27.6	2.6	100
1984	19.8	40.3	37.9	2.0	100
1986	28.6	24.0	43.9	3.4	100
IV. Telecommunications equipment					
1978	30.4	11.7	49.2	8.8	100
1980	28.0	11.5	52.1	8.3	100
1982	22.4	12.6	57.1	7.8	100
1984	17.2	9.8	66.7	6.3	100
1986	19.0	7.6	66.0	7.3	100
V. Scientific instruments					
1978	29.0	22.6	31.2	17.1	100
1980	30.0	26.4	29.1	14.5	100
1982	28.0	30.1	30.3	11.5	100
1984	26.8	32.3	31.9	9.0	100
1986	29.7	26.6	33.9	9.8	100
VI. Electrical machinery					
1978	49.6	12.5	22.5	15.4	100
1980	48.8	13.8	22.4	15.0	100
1982	46.3	15.8	23.5	14.4	100
1984	38.7	17.2	30.9	13.2	100
1986	39.5	14.5	30.6	15.4	100

VII. Non-electrical machinery

1978	43.8	29.0	19.9	7.3	100
1980	43.5	31.6	16.6	8.3	100
1982	39.8	32.0	19.6	8.6	100
1984	35.2	31.0	24.6	9.3	100
1986	32.1	31.0	25.3	11.6	100

VIII. Chemicals

1978	59.7	17.3	11.8	11.2	100
1980	61.8	16.3	11.2	10.7	100
1982	55.8	21.3	12.3	10.6	100
1984	54.0	22.5	13.2	10.3	100
1986	60.1	15.1	13.1	11.7	100

Source: Eurostat, *Statistical Analysis of Extra-EUR 12 Trade in Hi-tech Products, 1989.*

**APPENDIX T-3.5. EUR12 INDIVIDUAL HI-TECH PRODUCTS BY
INDUSTRY AND MAIN PARTNER: IMPORTS**

PRODUCT/PRODUIT	1978		1982		1984		1985		Annual Growth (%)		
	M.ECU	%	M.ECU	%	M.ECU	%	M.ECU	%	1978-82	1982-86	1978-85
<u>INDUSTRY: AEROSPACE/INDUSTRIE: AERIEN</u>											
AIRCRAFT PISTON ENGINES (71311) MOT.EXPLOSION A PISTON/AVIONS											
USA	13.3	82.7	16.1	76.6	13.5	74.3	19.7	86.0	4.9	5.1	5.0
SWEDEN / SUEDE	0.1	0.4	0	0.1	0.2	1.1	1.0	4.5	-37.5	210.4	39.3
CANADA	0.2	1.2	0.1	0.4	1.6	8.7	0.9	4.1	-19.2	84.7	22.2
AUSTRIA / AUTRICHE	0	0.1	0.3	1.4	0.2	1.0	0.6	2.6	109.3	19.4	53.1
SINGAPORE / SINGAPOUR	0	0	0	0.1	0	0	0.1	0.5	21.8	76.2	45.5
PARTS NES OF 7144,71481 (71491) PROP.A REACT.TURBO PIEC.DETACH											
USA	344.8	87.7	1043.7	82.7	1210.8	79.7	1548.0	83.1	31.9	10.4	20.6
CANADA	9.2	2.3	54.9	4.4	51.7	3.4	52.6	2.8	56.4	-1.1	24.4
JAPAN / JAPON	0.4	0.1	24.5	1.9	10.1	0.7	44.8	2.4	181.4	16.3	80.9
SINGAPORE / SINGAPOUR	1.0	0.3	1.8	0.1	22.5	1.5	26.1	1.4	15.2	94.6	49.7
PHILIPPINES	0.3	0.1	0.2	0	8.5	0.6	23.0	1.2	-8.8	219.3	70.7
HELICOPTERS (79210) HELICOPTERES											
USA	18.3	75.4	51.3	28.4	12.4	2.3	21.8	5.5	23.3	-19.3	2.2
BRAZIL / BRESIL	0	0	0	0	0	0	6.2	1.6	0	0	0
SWITZERLAND / SUISSE	1.8	7.2	0.7	0.4	1.7	0.3	2.8	0.7	-21.3	42.5	5.9
IRAQ / IRAK	0	0	0	0	2.5	0.5	1.4	0.4	0	0	0
CANADA	0	0	0	0	0	0	0.1	0	0	0	0
AIRCRAFT NES 2000KG OR LS (79220) AERODYN.A MOT.2000KG ET MOINS											
USA	21.5	97.7	24.9	52.6	20.6	55.8	57.7	56.0	3.8	23.3	13.1
BRAZIL / BRESIL	0	0	0.6	1.2	0.6	1.6	5.1	5.0	0	71.6	0
CHILE / CHILI	0	0	0	0	0	0	1.7	1.7	0	0	0
CANADA	0	0	0.1	0.2	0	0	1.1	1.0	0	77.3	0
AUSTRIA / AUTRICHE	0.1	0.5	0.3	0.7	1.1	3.1	0.2	0.2	30.0	-12.8	6.5
AIRCRAFT NES OVER 15000KG (79240) AERODYN.A MOT 15000KG ET PLUS											
USA	590.9	96.1	749.8	68.2	741.0	43.4	1576.6	77.0	6.1	20.4	13.1
SINGAPORE / SINGAPOUR	0	0	0	0	0	0	40.7	2.0	0	0	0
ROMANIA / ROUMANIE	0	0	0	0	0	0	15.5	0.8	0	0	0
KUWAIT / KOWAÏT	0	0	0.4	0	10.5	0.6	7.6	0.4	0	111.9	0
NIGER	0	0	0	0	0	0	6.8	0.3	0	0	0

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PRODUCT/PRODUIT	1978		1982		1984		1985		Annual Growth (%)		
	M.ECU	%	M.ECU	%	M.ECU	%	M.ECU	%	1978-82	1982-85	1978-85
AIRCRAFT PARTS NES (79290) PIECE DETACH.POUR 792											
USA	581.3	83.1	931.4	35.5	1108.4	37.9	1509.3	79.9	11.6	13.8	12.7
CANADA	11.4	1.6	19.4	0.8	15.9	0.5	33.1	2.1	14.1	19.2	16.6
SAUDI ARABIA / ARABIE SAOU	7.2	1.0	17.8	0.7	13.7	0.5	24.5	1.3	25.3	8.3	16.5
SWEDEN / SUEDE	4.2	0.6	10.0	0.4	12.7	0.4	23.0	1.2	24.2	23.1	23.6
TAIWAN	2.9	0.4	5.8	0.3	9.4	0.3	22.1	1.2	23.6	34.3	28.8
INDUSTRY: AUTOMATIC DATA PROCESSING MACHINES/ INDUSTRIE: MACHINES AUTOMATIQUES A TRAITEMENT DE DONNEES											
ELECTRIC TYPEWRITERS (75111) MACHINES A ECRIRE ELECTRIQUES											
JAPAN / JAPON	10.7	14.7	68.8	40.6	161.0	54.8	65.1	47.6	59.1	-1.4	25.3
SWITZERLAND / SUISSE	19.7	27.0	21.0	12.4	29.3	9.9	25.0	18.3	1.7	4.4	3.0
SINGAPORE / SINGAPOUR	2.5	3.4	12.2	7.2	10.6	3.6	13.2	9.6	49.3	2.0	23.4
SWEDEN / SUEDE	8.5	11.6	11.4	6.7	20.3	6.9	9.5	6.9	7.7	-4.5	1.4
BRAZIL / BRESIL	0	0	2.5	1.5	4.2	1.4	8.5	6.3	197.2	36.3	101.3
ANALOG, HYBRID COMPUTERS (75210) ORDINATEUR ANALOG, HYBRIDES											
USA	42.6	82.5	91.0	77.8	55.3	66.9	40.5	52.2	20.9	-18.3	-6
JAPAN / JAPON	3.8	7.4	1.5	1.3	7.4	8.9	6.2	9.6	-20.4	42.1	6.4
SWITZERLAND / SUISSE	0.6	1.2	0.8	0.7	2.2	2.6	2.3	4.4	6.6	33.1	21.3
SWEDEN / SUEDE	2.1	4.1	1.9	1.7	2.3	2.7	2.4	3.7	-2.2	5.4	1.6
TAIWAN	0	0	0	0	0.2	0.3	2.3	3.5	0	205.7	0
DIGITAL COMPUTERS (75220) ORDINATEUR DIGITAL											
USA	158.5	92.6	472.2	89.0	884.0	79.6	811.6	58.0	31.4	14.5	22.7
JAPAN / JAPON	0.6	0.3	27.1	5.1	131.7	11.9	211.9	15.1	160.5	67.1	108.7
KOREA REP.	0	0	0	0	1.4	0.1	123.4	8.8	111.5	786.2	332.9
TAIWAN	0	0	0.3	0.1	4.4	0.4	76.3	5.5	0	311.6	0
HONG KONG	0	0	1.4	0.3	8.9	0.8	67.7	4.8	0	161.8	0
DIGITAL CENTRAL PROCESSORS (75230) UNITE CENTR. TRAITEM. DIGITAL											
USA	215.5	85.5	566.5	79.8	1185.3	77.5	1184.6	53.2	27.3	20.3	23.7
JAPAN / JAPON	15.5	6.1	74.3	10.5	127.7	8.3	287.8	14.1	48.0	40.3	44.1
KOREA REP.	0	0	0.1	0	33.6	2.2	122.4	6.0	0	535.6	0
HONG KONG	0	0	2.7	0.4	51.6	3.4	117.9	5.8	211.5	156.3	182.6
TAIWAN	0	0	0.5	0.1	11.0	0.7	57.3	2.8	0	230.2	0

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PRODUCT/PRODUIT	1978		1982		1984		1986		Annual Growth (%)		
	M.ECU	%	M.ECU	%	M.ECU	%	M.ECU	%	1978-82	1982-85	1978-85
DIGITAL CENTRAL STOR UNITS (75240) UNITE MEMOIRE CENTR.DIGITAL											
USA	24.3	88.4	57.9	82.1	56.2	56.7	100.1	92.0	24.2	14.7	19.4
JAPAN / JAPON	1.2	4.2	5.5	7.8	7.1	6.4	9.4	7.7	47.6	14.1	29.5
SINGAPORE / SINGAPOUR	0	0	0.1	0.1	0	0	2.5	2.1	0	162.6	0
TAIWAN	0	0	0	0	0.8	0.7	2.2	1.8	-15.9	532.4	139.5
SWEDEN / SUEDE	0.9	3.3	0.8	1.1	1.3	1.2	1.6	1.3	-3.6	20.1	7.5
ADP PERIPHERAL UNITS (75250) UNITE PERIPHERIQUE ADAPTATION											
USA	812.2	79.6	2149.3	75.3	3005.0	60.2	2706.2	48.2	27.5	5.9	16.2
JAPAN / JAPON	29.5	2.9	255.2	8.9	954.8	19.1	1651.4	29.4	71.5	59.5	65.4
SWEDEN / SUEDE	107.2	10.5	205.3	7.2	327.9	6.5	370.4	6.6	17.7	15.8	16.3
TAIWAN	0	0	7.7	0.3	170.4	3.4	274.5	4.9	273.1	144.0	201.7
SINGAPORE / SINGAPOUR	0.1	0	2.3	0.1	113.7	2.3	154.4	2.9	126.1	190.8	156.4
OFF-LINE DATA PROC EQUIP (75280) MCH.AUXIL.TRAITEMENT INFORMAT.											
USA	202.4	82.4	222.7	85.6	233.0	73.1	183.9	50.0	2.4	-4.7	-1.2
JAPAN / JAPON	14.7	6.0	13.5	5.2	42.5	13.3	86.8	23.6	-1.9	59.0	24.9
SINGAPORE / SINGAPOUR	0.2	0.1	0.1	0	2.5	0.8	21.9	5.9	-31.3	357.3	77.2
SWEDEN / SUEDE	11.8	4.8	3.8	1.5	4.1	1.3	17.5	4.8	-24.4	46.1	5.1
SWITZERLAND / SUISSE	4.9	2.0	6.7	2.6	9.7	3.0	14.0	3.8	8.1	20.3	14.0
<u>INDUSTRY: ELECTRONIC EQUIPMENT/INDUSTRIE: EQUIPEMENT ELECTRONIQUE</u>											
ELECTRO-MEDICAL EQUIPMENT (77410) APP.ELECTRICITE MEDICAL											
USA	69.7	62.5	157.0	64.8	176.6	59.9	172.1	47.0	22.5	2.3	12.0
JAPAN / JAPON	11.3	10.1	51.3	21.2	71.9	24.4	134.0	36.6	46.0	27.1	36.2
SWEDEN / SUEDE	13.1	11.7	12.7	5.2	12.1	4.1	13.5	3.7	-8	1.7	0.4
SWITZERLAND / SUISSE	9.0	8.1	10.7	4.4	12.1	4.1	12.5	3.4	4.4	3.8	4.1
AUSTRIA / AUTRICHE	2.6	2.4	3.7	1.5	6.9	2.3	11.6	3.2	8.6	33.5	20.4
X-RAY APPARATUS, ETC (77420) APP.RAYONS X											
USA	55.5	51.1	111.4	62.5	118.7	51.5	84.6	35.4	19.0	-6.6	5.4
JAPAN / JAPON	8.5	7.8	17.2	9.7	26.7	11.6	43.6	18.2	19.3	26.1	22.6
SWEDEN / SUEDE	9.4	8.7	10.3	5.8	21.9	9.5	40.0	16.7	2.1	40.5	19.8
SWITZERLAND / SUISSE	12.9	11.8	16.9	9.5	21.6	9.4	25.0	10.4	7.1	10.2	8.7
AUSTRIA / AUTRICHE	4.2	3.9	5.4	3.1	7.5	3.2	11.5	4.8	6.8	20.5	13.4
TV PICTURE TUBES (77610) TUBES CATHODIQUES POUR TV											
JAPAN / JAPON	132.7	42.3	201.1	58.5	166.8	48.3	172.4	49.8	10.9	-3.8	3.3
AUSTRIA / AUTRICHE	17.7	5.6	16.2	4.7	69.9	20.2	76.1	22.0	-2.2	47.3	20.0
KOREA REP.	1.6	0.5	1.4	0.4	4.4	1.3	27.3	7.9	-3.6	109.5	42.1
TAIWAN	6.7	2.1	3.8	1.1	8.7	2.5	5.6	1.6	-13.3	10.4	-2.1
SINGAPORE / SINGAPOUR	0.1	0	8.1	2.4	3.9	1.1	2.9	0.8	179.4	-22.9	46.8

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	M.ECU	%	M.ECU	%	M.ECU	%	M.ECU	%	1978-82	1982-86	1978-88
OTH ELECTRONIC TUBES,ETC (77620) AUT.LAMPE TUBE VALVE ELECTRONQ											
JAPAN / JAPON	11.0	10.3	31.5	18.2	77.7	28.1	111.6	35.4	30.2	37.2	33.6
USA	44.5	41.6	83.2	48.2	108.2	39.2	85.0	27.9	16.9	1.4	8.9
KOREA REP.	0.4	0.4	0	0	3.5	1.2	17.7	5.6	-49.8	420.8	61.7
TAIWAN	0.1	0.1	0.4	0.2	5.9	2.1	13.1	4.2	34.2	146.1	81.8
SWITZERLAND / SUISSE	4.0	3.7	5.2	3.0	6.1	2.2	7.7	2.4	6.8	10.2	8.5
DIODES,TRANSISTORS,ETC (77630) DIODES TRANSISTORS ET SIMILAIR											
USA	143.4	39.2	215.8	35.8	306.6	30.4	271.7	25.3	10.8	5.9	8.3
JAPAN / JAPON	19.2	5.2	56.6	9.4	170.0	16.9	230.1	21.5	31.1	42.0	36.4
MALAYSIA	27.1	7.4	77.9	12.9	86.2	8.5	60.8	5.7	30.2	-6.0	10.6
HONG KONG	17.2	4.7	24.6	4.1	45.3	4.5	54.9	5.1	9.4	22.2	15.6
AUSTRIA / AUTRICHE	30.9	8.5	27.1	4.5	37.9	3.8	54.1	5.0	-3.2	18.8	7.2
ELECTRONIC MICROCIRCUITS (77640) MICROSTRUCTURES ELECTRONIQUES											
USA	319.6	51.5	655.4	42.4	1302.9	35.4	941.4	29.7	19.7	9.5	14.5
JAPAN / JAPON	18.8	3.0	169.6	11.0	643.1	17.5	559.8	17.7	73.3	34.8	52.9
MALAYSIA	17.1	2.8	78.5	5.1	288.4	7.8	293.8	9.3	46.3	39.1	42.6
SINGAPORE / SINGAPOUR	53.0	8.5	162.4	10.5	237.0	6.4	195.5	6.2	32.3	4.9	17.5
TAIWAN	28.0	4.5	77.7	5.0	175.5	4.8	185.9	5.9	29.0	24.4	26.7
PIEZO-ELC CRYSTALS,MRTD (77681) CRISTAUX PIEZO-ELECTR.MONTES											
JAPAN / JAPON	9.4	42.7	16.1	38.0	31.5	40.4	31.4	47.6	14.5	18.2	16.3
USA	6.7	30.4	8.7	20.4	15.4	19.7	8.6	13.0	6.7	-2	3.2
MALAYSIA	0.1	0.3	4.7	11.1	9.7	12.4	6.2	9.4	189.2	7.3	76.2
KOREA REP.	1.4	6.5	3.0	7.0	6.7	8.6	3.6	5.4	20.4	4.7	12.3
TAIWAN	0	0	1.1	2.5	3.4	4.4	3.4	5.2	264.0	34.5	121.3
ELECTRONIC COMPON PTS NES (77689) PIECE DETACHE NDA DE 776											
JAPAN / JAPON	17.7	19.6	34.4	24.8	74.6	36.5	85.6	41.2	18.1	25.6	21.8
USA	34.6	38.3	58.9	42.6	63.9	31.3	55.2	27.0	14.2	-1.2	6.2
SWITZERLAND / SUISSE	3.9	4.3	5.9	4.2	9.4	4.6	9.6	4.6	10.9	13.0	12.0
AUSTRIA / AUTRICHE	6.0	6.6	6.3	4.6	7.2	3.5	3.8	1.8	1.3	-11.8	-5.5
BRAZIL / BRESIL	1.0	1.2	0.1	0	0.2	0.1	3.1	1.5	-51.5	169.3	14.3
ELECTRO-MAGNETS,ETC (77881) AIMANT ELECTRO PERMANANT ETC											
JAPAN / JAPON	11.9	27.8	26.6	36.8	40.7	34.4	55.9	42.4	22.3	20.4	21.3
USA	15.8	37.0	23.8	32.9	44.3	37.5	29.7	22.6	10.7	5.7	8.2
SWITZERLAND / SUISSE	7.4	17.3	10.6	14.7	14.2	12.0	24.0	18.2	9.5	22.6	15.9
AUSTRIA / AUTRICHE	2.2	5.1	3.1	4.3	4.5	3.8	4.0	3.1	9.4	6.7	8.0
BRAZIL / BRESIL	0.2	0.4	0	0	2.2	1.9	2.3	1.7	-34.7	190.8	37.8

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	M.ECU	%	M.ECU	%	M.ECU	%	M.ECU	%	1978-82	1982-86	1978-86
<u>INDUSTRY: TELECOMMUNICATIONS EQUIPMENT/ INDUSTRIE: EQUIPEMENT TELECOMMUNICATIONS</u>											
COLOUR TV RECEIVERS (7610) RECEPT.TV COULEUR											
JAPAN / JAPON	126.0	37.6	194.8	30.2	206.0	30.2	233.8	27.1	11.5	4.7	8.0
AUSTRIA / AUTRICHE	93.1	27.8	153.3	23.8	93.4	13.7	139.2	16.2	13.3	-2.4	5.1
FINLAND / FINLANDE	20.5	9.1	60.6	9.4	84.1	12.3	121.1	14.1	18.7	18.9	18.8
SINGAPORE / SINGAPOUR	20.0	6.0	100.5	15.6	120.0	17.6	109.7	12.7	49.7	2.2	23.7
SWEDEN / SUEDE	54.7	16.3	57.7	8.9	98.6	14.4	79.2	9.2	1.3	8.2	4.7
MONOCHROME TV RECEIVERS (76120) RECEPT.TV NOIR ET BLANC											
KOREA REP.	13.3	9.5	14.8	13.8	14.9	15.7	15.5	19.8	2.7	1.2	2.0
ROMANIA / ROUMANIE	0.4	0.3	0.2	0.2	6.3	6.6	9.3	11.9	-11.4	149.9	49.8
JAPAN / JAPON	51.1	36.5	16.0	15.0	11.8	12.4	8.6	11.0	-25.2	-14.3	-19.9
TAIWAN	41.1	29.3	39.8	37.3	27.4	28.8	8.2	10.5	-9	-32.6	-18.3
HONG KONG	0.6	0.4	7.0	6.5	4.0	4.3	7.2	9.2	87.3	0.8	37.4
MTR VEHIC RADIO RECEIVERS (76210) RECEPT.RADIO POUR AUTOMOBIL											
JAPAN / JAPON	69.6	61.7	122.3	52.9	154.7	49.9	200.5	42.6	15.1	13.2	14.1
KOREA REP.	1.6	1.5	22.9	9.9	42.4	13.7	91.7	19.5	93.3	41.4	65.3
BRAZIL / BRESIL	4.6	4.1	3.0	1.3	28.4	9.2	67.6	14.4	-9.8	117.3	40.0
MALAYSIA	0.1	0.1	3.7	1.6	13.7	4.4	35.3	7.5	132.0	75.3	101.7
SINGAPORE / SINGAPOUR	1.3	1.2	23.1	10.0	33.9	10.9	28.4	6.0	104.7	5.4	46.9
PORTABLE RADIO RECEIVERS (76220) RECEPT.RADIO PORTATIFS											
JAPAN / JAPON	125.2	39.7	158.7	29.4	160.9	27.1	218.2	26.2	6.1	8.3	7.2
HONG KONG	69.5	22.0	106.3	19.7	97.6	16.4	130.3	15.6	11.2	5.2	8.2
SINGAPORE / SINGAPOUR	37.4	11.9	88.8	16.5	85.1	14.3	99.9	12.0	24.1	3.0	13.1
KOREA REP.	24.1	7.6	32.3	6.0	60.4	10.2	98.6	11.8	7.6	32.2	19.3
MALAYSIA	9.6	3.1	30.3	5.6	54.6	9.2	97.6	11.7	33.1	34.0	33.6
OTHER RADIO RECEIVERS (76280) RECEPT.RADIO AUTRES											
JAPAN / JAPON	282.7	64.2	204.7	40.3	196.8	35.6	255.0	44.1	-7.8	5.6	-1.3
TAIWAN	19.5	4.4	70.1	13.8	113.7	20.6	98.0	16.9	37.7	8.7	22.3
HONG KONG	41.7	9.5	72.5	14.3	77.8	14.1	80.6	13.9	14.8	2.7	8.6
KOREA REP.	26.0	5.9	56.7	11.2	61.0	11.0	31.9	5.5	21.6	-13.4	2.6
SINGAPORE / SINGAPOUR	26.3	6.0	54.8	10.8	39.8	7.2	28.2	4.9	20.1	-15.3	0.9
ELECTRIC GRAMOPHONES, ETC (7631) ELECTROPHONE ETC.											
JAPAN / JAPON	111.7	83.0	143.3	91.8	156.3	90.2	363.7	91.2	6.4	26.2	15.9
TAIWAN	0.3	0.2	0.8	0.5	3.5	2.0	12.7	3.2	24.5	100.7	58.0
KOREA REP.	0.2	0.2	1.3	0.8	2.7	1.5	8.3	2.1	54.2	59.0	56.6
USA	7.6	5.7	5.5	3.5	1.7	1.0	3.4	0.3	-7.8	-11.5	-9.7
GERMAN DEM REP / REPUBLIQUE	0.8	0.6	1.7	1.1	1.8	1.0	2.3	0.8	20.4	8.5	14.3

EUR12 : Individual Hi-tech Products by Industry and Main Partner : IMPORTS
 EUR12 : Produits Hi-tech Individuels par Industrie et par Partenaire Important Principaux : IMPORTATIONS

PRODUCT/PRODUIT	1978		1982		1984		1985		Annual Growth (%)		
	M. ECU	%	M. ECU	%	M. ECU	%	M. ECU	%	1978-82	1982-85	1978-85
TV IMAGE, SND RECORDERS, ETC (76331) APP. ENREGISTR. REPROD. IMAGE, SON											
JAPAN / JAPON	106.4	61.6	1110.3	49.4	1623.1	90.7	1489.0	78.4	79.7	7.6	29.1
AUSTRIA / AUTRICHE	46.7	27.1	75.5	3.4	63.1	3.8	118.2	6.2	12.7	11.9	12.3
KOREA REP.	0	0	0	0	1.1	0.1	92.2	4.9	12.6	606.5	182.1
HONG KONG	0.1	0	0.8	0	1.6	0.1	71.6	3.8	101.0	204.5	147.4
USA	16.3	9.4	18.9	0.8	28.2	1.6	29.8	1.6	3.8	12.0	7.9
DICTATING MACHINES, ETC (76338) MCH. A DICTER ET AUTRES											
JAPAN / JAPON	284.2	65.8	387.6	63.0	601.1	74.0	498.5	70.2	9.1	6.5	7.3
AUSTRIA / AUTRICHE	59.5	13.8	34.0	6.0	39.2	4.8	45.7	6.4	-13.1	7.7	-3.2
HONG KONG	10.3	2.4	35.6	6.3	41.1	5.1	39.9	5.6	36.4	2.9	18.4
TAIWAN	13.2	3.1	15.0	2.6	27.4	3.4	30.9	4.4	3.2	19.9	11.2
KOREA REP.	23.1	5.3	36.5	6.4	36.1	4.4	28.5	4.0	12.2	-6.0	2.7
LINE TELEPHONE, ETC EQUIP (76410) APP. ELC. TELEPH. ETC. PAR FIL											
JAPAN / JAPON	22.0	15.8	52.8	23.1	113.6	26.6	268.9	41.2	24.5	50.2	36.8
USA	34.1	24.6	66.7	29.2	119.9	28.1	137.8	21.1	18.2	19.9	19.1
SWEDEN / SUEDE	38.9	28.0	24.6	10.8	55.0	12.9	77.8	11.9	-10.9	33.4	9.1
TAIWAN	1.2	0.9	5.8	2.6	11.4	2.7	43.6	6.7	49.1	65.2	57.0
HONG KONG	0.2	0.2	9.2	4.0	34.6	8.1	36.1	5.5	157.8	40.6	90.4
MICROPH, LOUDSPKR, AMPLIFR (76420) MICROPH. HT-PARLEUR AMPLIFICAT											
JAPAN / JAPON	215.4	64.0	317.5	60.6	295.3	57.7	322.1	59.1	10.2	0.4	5.2
TAIWAN	9.7	2.9	49.9	9.5	63.1	12.3	69.0	12.7	50.7	8.4	27.8
USA	67.0	19.9	76.8	14.6	68.4	13.4	59.9	11.0	3.5	-6.0	-1.4
KOREA REP.	8.3	2.5	22.8	4.3	29.1	5.7	29.5	5.4	28.7	6.6	17.1
AUSTRIA / AUTRICHE	4.2	1.3	9.4	1.8	13.4	2.6	13.0	2.4	22.1	8.4	15.0
TV, RADIO TRANSMITTRS, ETC (76430) APP. EMETTEUR RECEPT. RADIO TV											
JAPAN / JAPON	54.2	39.1	87.9	31.4	74.6	28.3	114.8	33.5	12.9	6.9	9.8
USA	47.3	34.1	90.0	32.1	91.4	34.6	104.9	30.6	17.4	3.9	10.5
FINLAND / FINLANDE	0.5	0.3	2.2	0.8	7.0	2.7	20.8	6.1	47.9	75.3	61.0
SWEDEN / SUEDE	6.8	4.9	9.6	3.4	11.1	4.2	16.7	4.9	9.2	14.8	12.0
TAIWAN	3.9	2.8	13.0	4.6	12.5	4.8	15.8	4.6	35.2	5.1	19.2
RADIOTELEPHONE, ETC RCYRS (76481) RECEPT. RADIO-TELE-PHON. -TELEGR											
USA	8.3	40.3	20.8	44.9	24.2	35.1	17.6	29.4	25.9	-4.1	9.9
JAPAN / JAPON	4.9	23.8	10.2	22.1	11.9	17.3	16.9	28.2	20.3	13.3	16.8
SWITZERLAND / SUISSE	3.1	15.1	3.4	7.3	6.9	10.0	11.2	18.7	2.2	34.8	17.4
SWEDEN / SUEDE	1.4	6.6	3.2	6.9	6.5	9.4	6.5	10.8	23.9	19.1	21.5
SOUTH AFRICAN CUSTOMS UNIO	0	0.1	0	0.1	0.1	0.1	1.3	2.2	12.2	130.7	60.9

EUR12 : Individual Hi-tech Products by Industry and Main Partner : IMPORTS
 EUR12 : Produits Hi-tech Individuels par Industrie et par Partenaire Important Principaux : IMPORTATIONS

PRODUCT/PRODUIT	1978		1982		1984		1986		Annual Growth (%)		
	M.ECU	%	M.ECU	%	M.ECU	%	M.ECU	%	1978-82	1982-86	1978-86
TELEVISION CAMERAS (76482) APP.PRISE-YUE TV											
JAPAN / JAPON	11.6	59.0	153.5	87.8	164.5	87.0	393.4	93.6	90.7	25.7	54.9
USA	5.9	30.0	16.3	9.3	14.1	7.5	10.0	2.4	28.8	-11.5	5.7
TAIWAN	0	0	0.1	0.1	1.2	0.6	1.8	0.4	93.0	95.3	94.2
SINGAPORE / SINGAPOUR	0	0.2	0.1	0	0.2	0.1	1.5	0.4	5.8	123.4	53.9
NORWAY / NORVEGE	0.1	0.5	0.3	0.2	0.6	0.3	1.4	0.3	35.7	44.3	39.9
RADAR APPARATUS, ETC (76463) APP.RADAR RADIO-DETECT.SONDAGE											
USA	56.5	44.9	177.4	71.7	177.5	62.7	155.9	61.9	33.1	-3.2	13.5
JAPAN / JAPON	7.4	5.8	22.5	9.1	20.9	7.4	31.2	12.4	32.3	8.5	19.8
SWITZERLAND / SUISSE	23.7	18.9	11.7	4.7	22.0	7.8	17.8	7.1	-16.1	11.0	-3.5
SWEDEN / SUEDE	6.7	5.3	3.3	1.3	3.6	1.3	6.9	2.7	-16.2	20.1	3.3
CANADA	1.6	1.3	2.4	1.0	3.6	1.3	5.8	2.3	11.0	24.4	17.5
PTS NES OF APPAR OF 76410 (76491) PIECE DETACH.POUR APP.DU 76410											
SWEDEN / SUEDE	57.5	46.4	94.0	36.7	125.6	31.5	154.9	30.2	13.1	13.3	13.2
USA	17.9	14.4	46.6	18.2	76.1	19.1	151.6	29.5	27.0	34.3	30.6
CANADA	4.3	3.4	39.4	15.0	75.8	19.0	67.5	13.1	73.1	15.1	41.2
JAPAN / JAPON	1.9	1.6	17.2	6.7	23.2	5.8	33.7	6.6	72.4	18.3	42.3
SWITZERLAND / SUISSE	12.6	10.1	12.2	4.7	13.4	3.4	20.3	4.0	-8	13.7	6.2
PTS NES OF EQUIP OF 76420 (76492) PIECE DETACH.POUR APP.DU 76420											
JAPAN / JAPON	6.1	29.8	11.7	34.9	13.4	31.5	12.1	32.2	17.8	0.7	3.9
USA	8.5	41.8	11.3	33.5	12.4	28.9	8.9	23.8	7.3	-5.8	3.5
TAIWAN	0.5	2.2	3.1	9.1	7.7	17.9	7.5	20.2	61.6	25.2	42.2
AUSTRIA / AUTRICHE	2.9	14.3	5.1	15.1	5.8	13.6	4.8	12.9	15.0	-1.3	3.5
SWITZERLAND / SUISSE	0.4	1.9	0.3	1.0	0.6	1.4	1.1	2.8	-3.4	32.3	13.1
TELECOMM EQUIPMT PTS NES (76493) PIECE DET.P 761,762,7643,7648											
USA	85.5	36.8	229.6	39.8	267.4	39.6	273.6	36.3	28.0	4.5	15.9
JAPAN / JAPON	44.6	19.2	130.5	22.6	138.1	20.5	190.8	25.3	30.8	10.0	13.9
SWEDEN / SUEDE	12.0	5.2	31.1	5.4	39.9	5.9	56.2	7.5	26.8	16.0	21.3
SWITZERLAND / SUISSE	17.2	7.4	24.1	4.2	33.4	5.0	42.5	5.6	8.8	15.2	11.9
AUSTRIA / AUTRICHE	18.7	8.0	30.7	5.3	34.2	5.1	36.0	4.8	13.3	4.0	3.5
PARTS ETC OF SOUNDS EQUIP (76499) PIECE DETACH.ACCESS.POUR 763											
JAPAN / JAPON	32.3	29.0	87.7	38.4	259.6	68.1	597.8	75.3	28.4	61.0	44.0
AUSTRIA / AUTRICHE	10.5	9.4	55.1	24.1	37.2	9.8	87.9	11.1	51.5	12.4	30.5
USA	41.9	37.6	37.7	16.5	31.6	8.3	23.7	3.0	-2.6	-11.0	-6.9
SWITZERLAND / SUISSE	18.4	16.5	11.4	5.0	13.2	3.5	15.9	2.1	-11.3	10.3	-1.1
TAIWAN	0.2	0.1	1.0	0.4	3.3	0.9	11.5	1.5	57.5	85.9	71.1

Source: Eurostat, Statistical Analysis of Extra-EUR 12
 Trade in Hi-tech Products, 1989.

APPENDIX T-3.6. THE MEMBERS OF THE ROUNDTABLE OF EUROPEAN INDUSTRIALISTS IN 1987

Torvild Aakvaag General director Norsk Hydro, Norway	Luis Magana President Furnas Electricas de Cataluna, Spain
Umberto Agnelli Deputy chairman Fiat, Italy	Helmut Maucher Managing director Nestlé, Switzerland
Carlo de Benedetti Chairman and CEO Olivetti, Italy	Hans Merkle Chairman supervisory council Robert Bosch, West Germany
Jean-Louis Beffa Président directeur général (PDG) Saint-Gobain, France	Jerome Monod PDG Lyonnaise des Eaux, France
Werner Breitschwerdt Chairman Daimler-Benz, West Germany	Curt Nicolin Chairman ASEA, Sweden
Sir John Clark Chairman and CEO Plessey, UK	Antony Pilkington Chairman Pilkington Bros, UK
Viscount Etienne Davignon Chairman Sibeka, Belgium	Stephan Schmidheiny Chairman Anova, Switzerland
Wisse Dekker Chairman supervisory board Philips, Netherlands	Patrick Sheehy Chairman BAT Industries, UK
Raul Gardini President Ferruzzi, Italy	Luis Solana Presidente Compania Telefonica Nacional de Espana, Spain
Alain Gomez PDG Thomson, France	Dieter Spethmann Chairman management board Thyssen, West Germany
Pehr Gyllenhammar Chairman and CEO Volvo, Sweden	Poul Svanholm Director De Forenede Bryggerier, Denmark
Patrick Hayes Chairman Waterford Glass, Ireland	Josef Taus Managing partner Constantia Industrieverwaltung, Austria
Kari Kairamo Managing director Nokia, Finland	Pierre de Tillesse Managing director Petrofina, Belgium
Karlheinz Kaske President and CEO Siemens, West Germany	Jacopo Vittorelli Managing director Pirelli, Italy
Olivier Lecerf PDG Lafarge Coppee, France	

Source: Roy Eales, "Europe's Business Knights Regroup", *Multinational Business*, 3, (Autumn 1987).

APPENDIX T-5.1. TRANSNATIONAL CORPORATIONS AND TAIWAN'S
PROGRAMME FOR A REGIONAL OPERATION CENTRE (1992-1993)

1. Formal Confirmation

TNCs	CONTENT	STYLE	PARTNER	MARKET
AT&T	Hi-tech/ market	SA	MOEA	Asia- Pacific
GE	Finance & Tech. 60% share	SA	MOEA HT Co.	Asia- Pacific
Carpenter Tech. Co.	Patents & tech.		MOEA & WLEWCC	Asia Pacific
Motorola		SA	PEWA	CEA
GM	OPEL Plan parts	SA	MOEA & Kuochan M	Asia- Pacific
IBM		SA	MOEA	CEA
ABB Group		SA	MOEA	
Siemens	DRAM		Sub Co.	Asia- Pacific

2. Intention and In Negotiation: Strategic Alliance,
Joint Ventures, Technology Cooperation, and Subsidiary
Investment

Nippon Elect. Co	Satellite network	JV	Teco EMC	Pan Pacific
Whirlpool	40% share	Invest	Teco EMC	AP
Westinghouse EC	Defence Tech.	SA	Mitac	CEA, AP
Bull Computer Gemplus	IC cards Manu./Lab	JV JV	TSEC/Gemp TSEC/Bull	Asia Asia
Pratt & Whitney	Engine Repair	Tech. Coop.	CAL	AP, China
Daewoo Group	Vehicles	JV	Tuntex G	CEA, ASEAN
Microsoft	Marketing			CEA
BAe	RJX Airplane	JV	TAC & RR	AP

Rolls Royce Group (RR)	New Jet Engine	JV	TAC & BMW	Asia
Hewlett Packard	Hi-tech Marketing		Sub Co & Wang	CEA
Federal Express	Transport			CEA
Philips	Semi-conductor		Sub Co	AP
Daimler-Benz Groups			TAC	CEA
Northern Telecom.	Electr. & Home Appl	JV		CEA
Du Pont	Tech Exchange		ITRI	CEA

3. Others In Consideration

Japan's Copyer Rank Xerox		Procure Procure		CEA
Rank Xerox	Photocopy Machines	Manuf.		CEA
Fujitsu		Procure	Acer	
Bayer				
3M				
Rohoman-Haas				

- Note: 1. SA (Strategic Alliance), JV (Joint Venture), MOEA (Ministry of Economic Affairs), AP (Asia Pacific), TAC (Taiwan Aerospace Co.), ITRI (Industrial Technology Research Institute), Sub (Subsidiary), CAL (China Airlines), TSEC (Taiwan Solomon Enterprise Co.), CMC (Chinese Motor Co.).
2. Information showed here does not include those cases signed prior to the announcement of the regional operating centre programme.

- Source: 1. *Taiwan Industrial Panorama*, Industrial Development & Investment Centre, Ministry of Economic Affairs, ROC, V. 20-21, various numbers, October 1992-September 1993; and
2. *Central Daily News*, International Edition, various reports, (January-September 1993).

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