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Beyond Geopolitics – Is there a Case for a Free Trade Accord between the EU and Taiwan?

Taiwan’s decades of strained, often hostile, relations with mainland China have isolated the island diplomatically and economically. But since 2008, a major rapprochement across the Straits is underway. Late June, both sides signed a trade agreement, the Economic Cooperation and Framework Agreement (ECFA). Will that be a bridgehead to Taiwanese free trade agreements (FTAs) with key trading partners, as the current administration hopes?

The EU has launched major FTA initiatives in Asia but has not considered Taiwan. There is a widespread belief that China will oppose any move towards an EU-Taiwan FTA, and that the latter would upset EU-China diplomatic and commercial relations. This has prevented a serious discussion about the pros and cons of an EU-Taiwan FTA from even starting. ECIPE’s new paper examines whether there is an economic case for an EU Taiwan FTA and discusses the geopolitical issues around a potential future agreement.

Taiwan offers real opportunities for European firms to increase market access and raise their profile in Asia. In particular, it could boost the competitiveness of the European ICT sector. Taiwan has a distinctive niche in the global ICT production chain, especially in the import and export of intermediary inputs, i.e. parts and components. Taiwan, with only 23 million inhabitants, has 19 firms in the OECD’s list of top 250 global ICT firms, compared with 9 from South Korea and 39 from the EU. Taiwanese ICT production is increasingly research-and-development (R&D) intensive. Taiwanese firms account for roughly 80 per cent of the global production of laptops. These are mainly exported via mainland China.

Overall, EU-Taiwan trade and foreign direct investment (FDI) perform well below potential: there is much room for improvement. Taiwan-EU goods and services trade and FDI are low compared South Korea’s and Hong Kong’s commercial relationships with the EU. The biggest gains from the liberalisation of EU-Taiwan commerce would come from “deep integration”, i.e. rules that address trade-and-investment barriers “behind the border”. There are peak tariffs on both sides that would need to be eliminated – on TV, video and other electronics products in the EU, and automobiles and beverages in Taiwan. But most gains in goods trade would accrue from the elimination of Taiwan’s double- testing requirements and Taiwan-specific standards that diverge from international standards. This particularly affects European exports in electronics, electrical equipment, automobiles, medical equipment and pharmaceuticals. Even more gains would come from further opening Taiwan’s services sectors. European services that are likely to benefit most are telecommunications, financial and business services, transport and environmental services. An accord between the EU and Taiwan could significantly boost FDI in Taiwan, in particular through services liberalisation.

For the EU, an FTA with Taiwan, seen in isolation, would not deliver large aggregate gains given the limited size of the Taiwanese market. But it would potentially deliver much larger gains in the context of greater Taiwan-China economic integration. That would free up “triangular” (EU-Taiwan-China) trade and associated FDI, with European firms – particularly in ICT – using Taiwan as a high-value hub in Greater China and wider east-Asian supply chains. China has quickly become by far the most important trading partner for Taiwan, and the current government realises that Taiwan’s globalisation has to proceed via China. Hence a barrage of initiatives to liberalise cross-Straits commerce. These initiatives must go further. ECFA starts with modest trade liberalisation. Taiwan still bans imports from mainland China on 2249 products. Despite recent liberalisation, mainland Chinese investments into Taiwan remain tightly controlled. And there are restrictions on Taiwanese investment into the mainland, although these have been eased.

Though Taiwan is not recognised as a sovereign state by most members of the United Nations (and all its major trading partners), strictly legal obstacles to signing FTAs with them are minimal. Taiwan is an independent customs territory, and a full member of the WTO, and of APEC. As such, nothing should prevent it from signing FTAs. Furthermore, Taiwan already has bilateral investment treaties (BITs) with several Asian countries, double-taxation and intellectual-property agreements with various EU member states, and an Open Skies agreement with the USA. Ultimately, obstacles to Taiwanese FTAs are political rather than legal. Taiwan’s initial challenge is to bring itself onto the EU’s radar screen. And both sides would need to reassure China that any agreement among themselves is not a move towards formal Taiwanese statehood and independence.

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