

Taiwan Insight

20 March 2000

The presidential election

Not so much about independence as about corruption

The Taiwan election was not about relations with China. No candidate supported greater independence from China. Had the Kuomintang (KMT) not split, James Soong, the candidate softest on China, would have won an overwhelming victory.

The KMT's weakness resulted from President Lee Teng-hui's imposition of an unpopular candidate, which split the party. The Democratic Progressive Party's (DPP) strength resulted from its abandoning the independence platform and focusing on denunciations of KMT corruption and abuse of power. We believe this doubled the party's share of votes.

DPP charges against Lee's government, Lee's charges against James Soong, a divided government, attacks on the KMT business-government complex, and the disintegration of the KMT imply severe domestic political turbulence.

Accelerated economic integration with China and liberalisation of the Taiwan economy should imply economic benefits from Chen's rule.

Crisis with China will be avoided if, and only if, Chen Shui-bian agrees to discussions based on the one-China principle. Early signs are hopeful, but we expect Taiwan markets to be extremely volatile.

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The election results

The Taiwan election of 18 March, 2000, was above all an exuberant exercise in democracy. Some 83% of the electorate participated, close to three times the participation rates in some Western elections. Although it is impossible to quantify the number who flew home from other countries to vote, we know the number was large, including some who flew home from places like New Zealand. This gives overwhelming democratic legitimacy to the result.

The DPP's Chen Shui-bian won 39.3% of the vote, independent (former KMT) James Soong won 36.8%, and KMT candidate Vice-President Lien Chan won 23.1%. The candidate of the New Party, which advocates early moves toward reunification, and a breakaway DPP candidate won only single-digit percentages.

Chen won despite KMT resources

Chen Shui-bian's victory was particularly noteworthy in view of the overwhelming resources of the KMT candidate he opposed. The KMT has at its disposal the economic power of a business empire variously valued at US\$7-20bn. We lean toward the lower end of the spectrum; estimates that are lower than US\$7bn value KMT real estate holdings at book value, which is absurd since many properties were acquired decades ago when Taiwan was one of the world's poorest economies. Cash generated by this business empire is freely used to support KMT candidates, particularly the top candidate. The KMT controls all land-based television in Taiwan, two stations through its own ownership and one through the Ministry of Defence. Through regulatory mechanisms and substantial direct ownership, the KMT controls the banking system, and uses that control to sustain both its own enterprises and its political position. The KMT has considerable ability to determine the outcome of court cases, a crucial advantage in an election where charges of corruption were prominent; the absence of an independent judiciary was a significant election issue, and the promise to create an independent judiciary was a major DPP promise. KMT patronage capabilities, particularly at the village level, have in the past assured political hegemony.

Thus Chen Shui-bian's victory was the broad equivalent of an opposition party winning in China within a few years of a hypothetical future decision by the Communist Party to hold free elections. This was an impressive result indeed.

Had the KMT not split, Soong would have won

Equally impressive was the showing of James Soong, the candidate most associated with a softer line toward China. His tally was just 2.5% short of Chen's even though he lacked both the KMT's patronage machine and the DPP's organisation. Moreover, he was the target of the full weight of President Lee Teng-hui's personal fury, including use of the politicised prosecutorial system against him. The fact that Soong came close to Chen, and trounced Lien Chan, is crucial to understanding what this election was about. Soong, who has leaned toward closer ties with China, and Chen, who has leaned toward more distant ties, roughly split the non-KMT vote, in a sense cancelling out the cross-Strait policy issue. Soong was consistently the most popular KMT politician until well after President Lee chose Lien Chan as his running mate. Had the KMT chosen its candidate democratically, Soong would have been the KMT candidate and would have won the election overwhelmingly.

Most significant of all was the trouncing of Lien Chan by both Chen and Soong. Given all the resources at his disposal, plus the effective support of China, the election was a total repudiation of his candidacy. Since Lien Chan was seen merely as a shadow of President Lee Teng-hui, the election was also an overwhelming repudiation of President Lee.

What the election was not about

The election was not about independence

The world's press has given readers a clear view of what the Taiwan election was about: it was about whether independence-supporter Chen Shui-bian and his independence-seeking party would win. That view is entirely wrong. Throughout the campaign Chen repeatedly stated that he would never declare independence, or even hold a referendum on independence, unless Taiwan was attacked. The view of the DPP as the party of independence was, at a minimum, four years out of date, and the DPP would have been repudiated by the electorate if it had remained the party of independence.

Taiwan voters support the status quo

Taiwan politics has changed, and the Western media have not caught up with the changes. One thing that has not changed, however, is that polls of the people of Taiwan show little support for independence. There are two constants in Taiwan politics. First, voters do not want Beijing to have any additional say over their lives, present or future — not political life, not social life, not economic life, not foreign policy. Second, the voters do not seek independence and do not wish to provoke China. Taiwan does not want to be like Macau. Nor does it want to be Kosovo.

After interviewing representatives of all political parties in Taiwan in March 1999, we summarised the change in Taiwan politics in an April 1999 report as follows:¹

"In the Western press, and particularly in the US press and in US Congressional commentary, there is a familiar view of Taiwan's relations with the mainland. In this view, the people of Taiwan crave independence. The opposition DPP strongly advocates independence, and its coming to power would precipitate a crisis with China. For its part China is increasingly aggressive and militaristic toward Taiwan as shown by its missile-throwing in 1996. Following the recovery of Hong Kong in 1997 and the forthcoming recovery of Macau in December 1999, Chinese President Jiang Zemin is anxious to recover Taiwan during his tenure; he has set a timetable for doing so and for this purpose is frantically building up military forces, including a sudden huge increase in missiles opposite Taiwan. Over in Taiwan, President Lee Teng-hui is caught between these forces and is bravely standing up for his beleaguered Republic of China.

The remarkable thing about this widely held view is that little of it is true. Public opinion polls show that, while the people on Taiwan have a horror of being swallowed by communism,² and while those on Taiwan who have a direct attachment to the mainland have gradually died off, a clear majority has always opposed declaring independence and still does. Voters in the December 1998 parliamentary election delivered major defeats both to the New Party, which advocates greater efforts to achieve unification with the mainland, and to the leading candidate of the DPP, Taipei mayor Chen Shui-bian, who once was outspoken in advocating moves in the direction of independence. The opposition DPP, as it has come closer to sharing real power, has gradually moved toward the centre of gravity of public opinion; while it has not altered its original pro-independence written charter, current leaders support the status quo. The lead toward accepting the status quo was provided by the DPP's previous chairman, Mr Hsu, and has now been substantially followed by Chen Shui-bian. They bridge the gap between the original charter and their current stance, on those rare occasions when it is necessary to do so, by saying that Taiwan already has real independence and therefore the important thing is to defend what they already have. A declaration of independence, most of them acknowledge, would be a sure way to jeopardise what they currently have. Moreover, DPP officials have been vigorous in advocating closer economic ties with the mainland — a crucial issue for their Taiwanese business political base.

¹ William H. Overholt, *Taiwan: escaping the flames*, Nomura, 16 April, 1999, page 17.

² 78% of those polled in a southern city of Taiwan in 1998 opposed rule by Beijing. Cf "China Blasts Taiwan for Playing Democracy Card", Reuters News Service, 16 December, 1999.

Similarly, the governing KMT has gradually moved over many years from a position that it is the sole legitimate government of China to the position that it is one of two governments of China; as with the DPP, the core of the party leadership effectively endorses the status quo. This move has led to the formation of the splinter New Party, which feels more strongly about eventual unification. In short, while there are still differences of emotion and rhetoric, for all practical purposes the leaderships of the two major parties have converged on a consensus supporting the status quo.

In short, a vital shift has occurred in Taiwan politics. On the China issues, the KMT has moved out from under its leader to a position of even greater moderation than in the past. The DPP has shifted from being primarily a party of independence to primarily a party demanding clean government and serving as an advocacy channel on local issues. The New Party has largely abandoned its advocacy of early efforts toward reunification and in any case its weak electoral base is getting weaker. The leadership consensus of the parties reflects opinion and reality for the Taiwan public. Life in Taiwan is very comfortable, and one must search very hard to find anyone who yearns to die for independence; Taiwan is not Kosovo and it is not East Timor. The centre of gravity of Taiwan public opinion prefers the DPP stance on relations between politics and business (less corruption, less interest group influence) and the faction of the KMT (led by James Soong) that is most reassuring about supporting the status quo in relations with China."

Taiwan has an effective consensus on China policy...

In short, Taiwan opinion had moved toward a consensus on China policy. Virtually the entire electorate supported the status quo. The KMT put one spin on its support for the status quo, namely that it supported unification but only when mainland China has become a perfect democracy. The DPP put another spin on it, namely that Taiwan already had all the important attributes of independence and should not do anything to put them at risk. The bottom line was a national consensus on the status quo. In the election campaign, all candidates sought to distance themselves from Lee Teng-hui's provocative approach to the mainland, and all offered specific overtures to reassure voters improve relations with Beijing. James Soong has always been relatively conciliatory toward Beijing. Lien Chan offered a "peace plan", and Chen Shui-bian suggested repeatedly that he could be the Richard Nixon of Taiwan, implying that he had such credibility on the subject of Taiwan's stature that he was the one with the best political base to be able to cut a deal with Beijing.

...but wants more status

There were two footnotes to this status quo consensus. First, virtually the whole core of the Taiwan electorate supported an enhanced international stature for Taiwan, particularly as expressed in active participation in international organisations. Closely tied to this, virtually the whole electorate resonated to Lee Teng-hui's concept of the "New Taiwanese", an expression that encompassed the sense that mainland immigrants and native Taiwanese were now one people, combined with a search for Taiwanese stature. Second, though both KMT leaders, James Soong and Lien Chan, were part of the consensus about not provoking China, and so were both DPP leaders, Chen Shui-bian and Hsu Hsin-liang, President Lee Teng-hui was outside it. President Lee was part of the hardline Cold War generation. And, just as important, he is the only major leader of Taiwan who has no cultural ties to China; he is a colonial figure whose first language and cultural inclinations are Japanese.

President Lee is outside the consensus

The consensus was seemingly belied by the charters of the two major parties. The DPP charter continues to call for a referendum on independence, and KMT documents have guidelines for a presumptively early reunification. But these are just obsolete documents that each party could rectify only by paying a political price at the margin; like Al Gore talking to the labour unions about China, the DPP and KMT would prefer not to pay any price, even at the margin.

...but the DPP adopted a popular policy

However, at this point the DPP also changed. It changed from a party of independence to a party of clean government, from a party denouncing China to a party denouncing corruption. And once it did, it evoked a tremendous popular response.

Here it is necessary to sketch in some recent history that has gone almost unreported in the West. Under Chiang Kai-shek on the mainland the KMT had been guilty of corruption virtually unmatched, but in Taiwan he and his son Chiang Ching-kuo cleaned up the party until Taiwan politics was cleaner than in Japan and cleaner than in most major US cities — not quite on a par with Hong Kong or Singapore, but definitely moving in that direction. In the Lee Teng-hui era, the pendulum started to move sharply in the other direction.

Corruption and...

The spread of mafia-type organisations, the multiplication of kidnappings, the tolerance of gangsters in the legislature, the increasing use of the banking system to support hapless KMT firms and other favoured enterprises, manipulation of the stock market, the deterioration of infrastructure planning and construction for corrupt reasons, the replacement of a minister who was too effective at fighting corruption, the refusal to support banking reforms that would inhibit abuses, and the spread of personal corruption among those associated with the president are among the most striking phenomena of recent Taiwan. President Lee was criticised in the 1996 election campaign inter alia for allegedly buying into a golf course for a tiny fraction of market value. All of this gave turbo power to a DPP newly committed to a focus on clean government.

...unfair KMT political practices fuelled DPP support

Paired with public disgust over outright corruption was disillusionment with abuse of power by the KMT. If Taiwan was to become a real democracy, it had to move beyond neo-Leninist democracy to elections with a level playing field. So long as Taiwan politics had been obsessed with the China threat and with domestic divisions between mainland immigrants and native Taiwanese, levelling the playing field was not at the top of the public agenda. But once Taiwan had reached basic consensus on those issues, moving to real democracy became a major issue. The manipulation of the courts by Lee's administration became a major issue. Lien Chan was forced to propose that the KMT business empire be placed in trust and thereby be sterilised from political uses. (The KMT stalled on the ground that it was necessary to put in new laws to regulate trusts.) Ridding Taiwan of what was called "black gold politics" became a central theme of the campaign.

Public concern over corruption and abuse of political power gave transcendence to one of the critical moments of the 2000 campaign: days before the election, President Lee's national security adviser defected to the opposition, announcing that he did not want to be part of a government run by criminal gangs. This, together with Nobel Prize winner Lee Yuan-tseh's nearly simultaneous and even more dramatic endorsement of Chen, appear to have put Chen over the top.

Lee's desperate gambit

President Lee's situation was desperate

In the summer of 1999, Lee Teng-hui faced a desperate situation. He had begun with a sure thing, namely continued KMT dominance of Taiwan. The KMT was the only party with experience. It had most of the election funds and patronage levers. It was the party that voters trusted to manage the economy and protect them from Beijing. He was the hero of Taiwanese equality with mainlanders and of Taiwan's democratisation. But he had put all this in jeopardy. By making it clear that he would impose Lien Chan he had split the KMT, and by using the old Leninist powers and allowing corruption to spread he had given the DPP an unthinkable shot at victory.

An attack on James Soong...

President Lee's subsequent actions brilliantly finessed these problems. An investigation of James Soong's finances disclosed that he had transferred large amounts of campaign funds to his personal accounts. Although there is no law in Taiwan against doing this, and though Soong claimed that President Lee instructed him to make the transfers, the amounts were so large (US\$11.7m) that Soong's popularity declined drastically — to about the same levels (23-26%) as those of Lien Chan and Chen Shui-bian. Taiwan journalists believe that almost any senior politician would be vulnerable to similar investigations, and they report there was considerable resentment of the focusing of the prosecutor's apparatus on one candidate, but the tactic, commonly used in Asian politics, did reduce James Soong's popularity to the same level as Lien and Chen. In the aftermath of this tactic, each of the three held almost exactly a quarter of the votes.

...plus "state-to-state relations" offered a path to KMT recovery

Together with the earlier declaration of "special state-to-state relations", this decisively changed the agenda of the presidential campaign. Instead of being focused on DPP accusations of corruption against the sitting government, the campaign was focused on DPP embarrassment over being outflanked by the KMT on relations with the mainland and on accusations of corruption against James Soong. Rarely in political history have two political gambits transformed such a losing hand as Lee Teng-hui held in early 1999 into a fully competitive one.

Soong was in deep trouble owing to Lee's ability to manipulate the prosecutor and the courts. Chinese threats over Lee's July declaration helped Lien Chan, and Lien Chan pressed his advantage to the fullest, arguing that Chen was a dangerous provocateur who might start a war with China. The Western press echoed the Lee Teng-hui line, almost overwhelmingly characterising Chen falsely as the candidate of Taiwan independence and until the last days of the campaign failing to pick up the importance of the anti-corruption theme. But in the end Taiwan's voters rejected the line that Chen was a provocateur, resented Lee's unfair targeting of Soong, and resonated to the DPP anti-corruption drive.

The DPP is clear that political reform promises led to victory

When Chen's top people were asked why he won the election, they cited the drive for reform. This was true even of the foreign affairs director, Hsiao Bi-khim, who cited the electorate's "desperate desire for change, for clean government", and said the victorious DPP "will start with [creating the] independence of the judiciary". She went on to cite the "social welfare platform" and insistence that "political parties should not own enterprises".⁵ The shift in platform explains most of the difference between the 21% of votes the party garnered in 1996 and the 39.3% victory in 2000. That would still not have been nearly enough if the KMT had possessed internal democracy and had chosen the most popular candidate.

⁵ Interview on Bloomberg electronic news, March 18, 2000, at 22:25.

The China factor

China's policy: one country, two systems

China's policy toward Taiwan has remained consistent since Beijing's September 1981 offer to Taiwan of "one country, two systems". Under that offer, Taiwan would be allowed to maintain its own social freedom, political democracy, market economy, all its current or locally chosen or elected officials, and its own armed forces. This is similar to the formula offered the following year to Hong Kong but substantially better; the Hong Kong chief executive is subject to a Beijing veto, Hong Kong is governed by a constitution-like Basic Law written by China, and Hong Kong can have no independent foreign policy or military arms. Taiwan would be subject to none of these constraints.

Beijing has assumed time was on its side

The governing Chinese assumption about relations with Taiwan has been that this offer will become increasingly attractive over time, since China is developing and reforming so fast that, in the opinion of Chinese officials, over the decades China will become much more like Taiwan and therefore will eventually be an attractive partner.

Based on the assumption that its offer is exceptionally generous and will become more attractive over time, and that the international community backs the one-China policy, Beijing has made no serious effort to build up military forces that would be capable of taking Taiwan by force. While Beijing's military machine improves over time, for instance gradually increasing the number of missiles it possesses, Beijing has given low priority to military modernisation, it has not in recent years accelerated its production of missiles, and it has not changed its deployments to concentrate a higher proportion of its forces on Taiwan. Frequent suggestions in the media that there has been a major buildup designed to intimidate Taiwan are dismissed by the most authoritative US military sources as simply false.

On the other hand, Beijing has always been just as unwilling to sign an assurance that it would never under any conditions use force as Abraham Lincoln, who earnestly sought a peaceful resolution with the secessionist southern states, would have been unwilling to sign such an assurance. Taiwan was part of China longer than the US has been in existence, and any Chinese leader who proposed to turn it loose would be overthrown immediately.

But Beijing has always been anxious about Lee Teng-hui's efforts to change Taiwan's status. In the early and mid-1980s, Lee's government provided strong incentives for a number of small countries to accept "personal" visits by him and afterward proclaimed these as diplomatic triumphs which enhanced Taiwan's international status. He then applied the same formula to the US, providing endowment money to Cornell University in return for an invitation to speak as an alumnus and spending millions of dollars on Congressional lobbying to ensure that he would be allowed to accept the invitation. China, promised by the administration that this tactic would not be allowed to succeed, reacted angrily when President Clinton, faced with strong Congressional support for Lee, bowed to the tactic. China's subsequent missile-throwing overreaction convinced much of the world that Beijing was dangerous and militaristic.

Beijing had to react to "special state-to-state relations"...

To Beijing, Lee's July 1999 declaration of "special state-to-state relations" came very close to a declaration of independence. The declaration created a horrible dilemma for Chinese leaders. If they did not react firmly, then the world would assume they had acquiesced. This would be particularly true if they went ahead with the planned visit of their top Taiwan negotiator to Taipei, Wang Daohan. If they did not proceed with negotiations, they would be blamed for intransigence; if they did go ahead, they would be seen as acquiescing. So they had to react. On the other hand, if they responded with missiles and military exercises, they would alienate world opinion as they had done in 1996. So they deliberated until February 2000, and announced a policy that they believed was firm but not an overreaction: they strongly reaffirmed that Taiwan was part of China and said that they reserved the right to use force if

...and believed its response was moderate

Taipei refused indefinitely to negotiate. But they deliberately set no deadline for negotiations, and for the first time they accepted Taipei's conditions that the negotiations be conducted on the basis of equality and that practical matters like cross-strait trade could be negotiated first. Subsequently, Jiang Zemin further softened China's approach by stating that he did not see cross-strait relations as particularly tense.

The US saw it as election intimidation

The military threat was the only aspect reported in most of the Western press, and in fact the Chinese statement was reported almost exclusively as an attempt to intimidate the voters against voting for Chen Shui-bian, who was almost always identified as the candidate supporting independence. Certainly, Chen's rising star heightened Beijing's anxiety, but the Chinese statement primarily responded to Lee Teng-hui's "special state-to-state relations" declaration and warned whatever candidate became president not to proceed further down that street. The imminent meeting of the National People's Congress and the passage by the US House of Representatives of the Taiwan Security Enhancement Act (TSE) had as much to do with the timing of the announcement as the Taiwan election did.

Several aspects of the Chinese response to Lee are noteworthy.

Taiwan is more important than WTO

The timing came just as the US Congress is about to vote on permanent Normal Trade Relations (PNTR), to implement China's entry into the World Trade Organization (WTO). It seemed foolhardy to many Westerners to make an inflammatory declaration about Taiwan just as Congress was about to consider PNTR and the Senate to consider TSEA. To the Chinese, however, it seemed foolhardy even to consider that a matter of national territorial integrity could be held hostage to an economic agreement.

China seems strongly united over Taiwan

Second, the reaction of the Chinese population is crucial. Chinese students studying in the US report that Jiang Zemin ordered a consultation with groups of them and that almost unanimously these relatively liberal, highly educated students, many of whom are more sold on US-style management of economics and politics than on the way their government manages these, counselled much stronger reactions than the one Jiang eventually settled on. The same sources indicate that polls on the mainland find around 95% of the population willing to support war over Taiwan if necessary to preserve one China.

As it became clearer, in the days before the election, that Chen was the frontrunner, Premier Zhu Rongji gave an impassioned speech about Taiwan. He spoke about the unity of China, about how much China had sacrificed over the decades to regain its unity. He said China was willing to make concessions to the people of Taiwan, because after all they are fellow Chinese. But he warned against thinking that a military balance adverse to China would prevent China from acting if Taiwan headed toward independence. The reaction in the West: here is one more example of Chinese overbearing bluster. The reaction in China was more like Americans' reaction to President Kennedy's Cuban Missile Crisis speech. China is politically prepared for war if necessary.

Lee's initiative has altered Beijing's sense that time is on its side...

Third, Lee's "special state-to-state relations" initiative appears to have changed Chinese leaders' previous conviction that time was on their side. The initiative was subsequently accompanied by films and statements emphasising how much Taiwan has become a separate culture. Under Lee, for instance, Taiwan has stopped teaching Chinese history in most schools and substituted Taiwan history. There are suggestions that the future might bring a shift from conducting school and government in Mandarin to conducting them in Taiwanese. To the extent that Chinese leaders are convinced by this line of argument coming out of Taipei, they will inevitably feel less confident about waiting for decades for reunification and more pressured to impose deadlines and threaten force.

...implying more forceful measures

Identity politics can be affected by policy

Reality is much more nuanced. Taiwan has indeed grown away from the mainland, because a generation grew up that had no experience of the mainland. There is a "New Taiwanese" identity, elegantly captured by Lee Teng-hui's phrase. At the same time, Taiwanese are now visiting the mainland more than ever, and much of Taiwan's business is effectively integrated with the mainland. Statistical analysis shows that all of Asia's markets rise and fall with the yen — except for the China-Hong Kong-Taiwan complex, which follows its own separate rhythms. Perhaps more to the point, businesses seeking to form management teams for China discover time after time that one should form the management team in Taiwan, not in Hong Kong, because China's basic business practices and cultural assumptions share so much with Taiwan's and so little with Hong Kong's. Under these circumstances, whether Taiwan continues to grow farther from China or closer is heavily a matter of government policy in Taipei.

The military equation

The military situation has been overemphasised, so we will address it in the briefest terms.

No capability to seize Taiwan

As noted earlier, China has not built a military capable of attacking Taiwan. It has not thought it to be necessary. Beijing has been obsessed with economic reform to the exclusion of all other priorities, and it simply thought it wouldn't need the military wherewithal to attack Taiwan. Thus Beijing has only a handful of modern military aircraft, hardly any modern tanks, and a pitiful blue-water navy. Moreover, the People's Liberation Army is engaged in a top-to-bottom reorganisation that would make conflict particularly difficult for the next few years. But China has an economy that could support a much larger effort and could over five to eight years build a formidable force.

Taiwan is formidable

Taiwan, on the other hand, has so much modern military equipment that it will take at least five years to be able to utilise what it already has — not counting what some elements of the US Congress would like to add. Backed by the US, its position is so strong that there is simply no way that Beijing could occupy the island by force within the next few years. On a straight military calculation, therefore, the mainland's position is simply hopeless.

But politics count, too

But Clausewitz called war a continuation of politics by other means. Taiwan, backed by the US, would win the first round and the second round, and probably the third, fourth and fifth rounds. But the outcome of round 150 will be a function of political will. The Chinese leadership has public support on this subject in a depth that resembles North Vietnam in 1965. In Taiwan, there is no faction that wants to fight China over the flag, when China has consented under the "one country, two systems" proposal that Taiwan can maintain whatever economy, socio-political freedom, and government it wants. When Taiwan was facing the possible military imposition of communism in 1958, there was ample willingness to fight. Today the willingness to take strong positions on relatively marginal diplomatic status issues is weak and completely dependent on confidence that the US Congress will provide whatever backing Taiwan needs.

A long, slow war

If the relationship were to move toward a war that neither side currently wants, China would sink a few ships bound for Taiwan and all ships would stop heading for Taiwan unless and until they were convoyed by US and Japanese warships. Since trade is over 100% of GNP, that means a lot of expensive convoys and heavy losses of both men and material. Although Taiwan is not Vietnam, and the blue water gives advantages to the defender, a quick, sterile victory from 40,000 feet simply would not be possible given the vastness of China. It would be a long war. The US would take the war home to China, and China would find ways to take the war home to the US. There would be heavy casualties, possibly hideous casualties and smoking cities, in both countries. This would not be Kosovo, and application of the Kosovo principle to Taiwan might well have the same consequences as applying the Korean War analogy to Vietnam did.

...possibly building up to very high casualties...

In the end, the US public can be mobilised to fight long and hard over the democracy, freedom, and prosperity of Taiwan in the face of any risk of imposition of communism, but it is not likely to be willing to absorb tens of thousands of casualties over the issue of whether a free, democratic, prosperous Taiwan flies one flag or another. This is the fundamental wisdom behind the position of the last six US presidents, who have frequently reiterated their willingness to fight for Taiwan's freedoms but, equally, their unwillingness to fight for a Taiwan that provokes war by moving toward independence.

...would be to Beijing's advantage...

The one thing predictable is that the war would not be short and that by round 150 all sides, China, the US, and especially Taiwan, would be losers. Lee Teng-hui brought Taiwan to the point where one has to write such scenarios, but fortunately all three potential successors, and the leaders in Beijing, have so far shown an inclination toward a more moderate course.

Chen's policies toward China

*Initial stance: soft spin,
hard policy*

Along with the other candidates, Chen has adopted a conciliatory tone toward China. In his acceptance speech he proposed a peace treaty and invited Chinese leaders to visit Taiwan. But he also said that it was his mission to defend the "independent sovereignty" of Taiwan and that "Taiwan people will never accept the 'one country, two systems' policy that China has placed on Hong Kong and Macau". Moreover, the proposal of a peace treaty is something both sides know is unacceptable to Beijing, which has always said that it will never sign an international treaty over what it regards as a domestic issue. This was, for instance, a major sticking point in discussions with the Carter administration in Washington during the 1970s.

*China listening, Chen
possibly softening*

What China will demand is not early unification on harsh terms but rather some early commitment to political discussions about the status of Taiwan and some bow toward acceptance of a one-China policy. Unless this is forthcoming, there will eventually be serious conflict. The time remains early, and China has indicated that it cares about policy, not person, but in the wake of Lee Teng-hui's "state-to-state relations" gambit, China will not wait long for some sign that Chen is willing to accept the one-China principle and negotiate. Chen's promise to separate himself from the DPP is a positive sign, and even more positive was a statement on 20 March that he might be willing to discuss the one-China principle.

*Washington voices
against "one China"
enhance tension*

Simultaneously, in Washington, there is an increasingly widespread view that the vitality of Taiwan's democracy demands a rethinking of the old one-China policy. The executive branch, always concerned with keeping the peace in Asia, has adhered strictly to its old promises and policy. But journalists and members of Congress, who focus more on ideological concerns, increasingly call for re-evaluation; the fact that China has for nearly two decades made its willingness to let Taiwan have its own politics within a big tent is usually ignored by people who hold this opinion. Among those calling for a re-evaluation, there is widespread disbelief that China would actually go to war over Taiwan. If Taipei and Beijing do not find their way forward to dialogue, there is some risk that future historians will write of that disbelief as one of the great miscalculations of the early 21st century. In the meantime, the calls for reassessment make Beijing even more anxious and create still more pressures for early movement toward "one China".

Chen's economic programme

No detailed economic programme

Assuming that the political issues with China are finessed, the DPP economic inclinations are highly auspicious for Taiwan's economy. We say, "inclinations", because the DPP does not have a detailed economic programme. Throughout the lifetime of the party, it has been exclusively focused on political issues, particularly China policy and clean government. At least until recently, DPP leaders were quite open in acknowledging that they had no particular economic programme and no particular economic competence. But they have some strong inclinations, and they inherit a KMT-created policy-implementation machine that is one of the world's most competent. The DPP has governed quite effectively at the local level, including the mayoralty of Taipei, where Chen was an effective if highly abrasive mayor.

Campaign emphasis on social welfare

The party's campaign emphasis has been on its "social welfare platform", which includes promises of better pensions and better health care. At least as yet, there is no indication that such programmes would involve drastic changes in Taiwan's economy or its fiscal burden.

Faster economic integration with China

More significant, the core of the DPP is entrepreneurs and educated professionals who support faster opening of economic relations with China. If, as seems likely, Chen accelerates moves toward direct trade and removes many of Lee Teng-hui's barriers to investment in the mainland, the Taiwan economy and particularly its hi-tech sector should benefit greatly. Transportation companies would benefit greatly from direct trade with the mainland.

Attenuating the business-government nexus

The core of the DPP campaign has been targeted against the KMT business-politics nexus. The DPP has declared that "political parties should not own enterprises". It has said that it will investigate the KMT business empire and separate out businesses that have been acquired illegally. It has denounced government favours to companies owned by the KMT, and it has denounced the use of those companies' profits to support the KMT political machine. It forced Lien Chan to promise to put the business empire in trust. All this foreshadows a fundamental restructuring of significant parts of the Taiwan economy. This will potentially be painful for some KMT-connected companies but could bring far more efficient use of resources. The negatively affected companies would be part of the old economy, such as infrastructure and construction, whereas the beneficiary would be the new economy, the entrepreneurial electronics and other hi-tech companies.

It could actually be more difficult for a DPP president to restructure the KMT business empire in the face of a KMT-dominated legislature than to embarrass an all-powerful KMT president into thorough reform. But if Chen is able to tell the banks that they do not have to support illiquid KMT business groups, if he is able to clean up the system of awarding contracts, if he is able and willing to release the banking system from day-to-day political control, then the benefits to the Taiwan economy would be quite substantial. If the KMT continues to divide and disintegrate, as it was doing in the two days after the election, then this could happen very quickly.

In the meantime, the government will continue to support the currency and the stock market, and has adequate funds to do so. If, however, the KMT engages the banks' funds in this effort, as it did during Asian crisis, then the banks could be hurt.

Auspicious prospects

On balance, if one makes the large assumption that the international and domestic political situations can be managed, then the Taiwan economy should benefit substantially from liberalisation under Chen.

Domestic politics

Even if it avoids a crisis in cross-Strait relations, Taiwan is headed for a tumultuous year in domestic politics.

A fight over the KMT empire

First, the dismantling, rearranging, or political sterilisation of the KMT business empire will threaten the careers, financial positions and business arrangements of many of Taiwan's most powerful families.

A fight over corruption

Second, the politics of corruption has gained huge momentum. The DPP has charged the Lee Teng-hui government with serious corruption. Lee Teng-hui has brought charges against James Soong for corruption. By bringing charges against Soong for allegedly taking KMT money for personal use, Lee has validated the use of the prosecutor and the courts in bringing such charges, even though Taiwan's law technically allows the practice; in doing so, he has set a precedent for such charges, and by all accounts much of the Taiwan political establishment is vulnerable. So long as Lee was confident that his personal choice of candidate would be in control of the prosecutor and the courts, there was little risk in setting this precedent. Now, he has potentially put the whole KMT leadership at risk. But the establishment will fight back furiously, and the establishment chose the prosecutors and the judges. Moreover, outside KMT headquarters on 19 March, demonstrators were demanding reassurance that Mrs Lee had not fled the country, on the assumption that if she has not she may be vulnerable to prosecution. Finally, the legislature includes well-known gangsters whom Mr Chen may seek to evict.

DPP president, KMT legislature

The new president will have to deal with a legislature that is still dominated by the KMT. And it is a scrappy legislature, where fist fights frequently erupt. Trying to pass new laws, for instance ones that ban transfer of campaign funds to personal use and ban political party ownership of business, may cause more frequent fist fights.

The tenure of Lee as KMT president

Lee Teng-hui had hoped to stay on indefinitely as KMT president, possibly playing the kind of powerful elder statesman role that Lee Kwan Yew plays in Singapore. Already, in response to violent demonstrations and denunciations for splitting the KMT, he has promised to step down when his current term ends in September. In the meantime, he is president of the country until May and as such controls the armed forces during a time of great tension with China. He now has a long history of using crises with China for political advantage, so there will be concern about this. And outspoken factions of the party will not sit quietly with the idea of Lee remaining party president until September.

Disintegration of the KMT?

James Soong has indicated that he will form a competing political party, thereby institutionalising the fracture of the KMT. The most powerful KMT politician other than Lee and Soong, namely the popular mayor of Taipei, has announced his resignation from the Standing Committee of the KMT. In short, the KMT is disintegrating. Theoretically, it could regroup and, for instance, dismiss the old leadership and invite James Soong to revitalise the party. But Lee's tenure until September stands in the way of that.

Fortunately for Taiwan, the economy is resilient and the most dynamic parts of the economy are not at risk from potential political fratricide. In this, Taiwan is different from Malaysia or Suharto's Indonesia. But the likely political turmoil will make the equity and currency markets quite volatile.

In this regard, the decision of Chen Shui-bian to step down from leadership of the DPP is an unwise gesture. It will not mollify Beijing, which cares only about the concrete details of cross-Strait policy, and it will weaken Chen just when he needs the strongest possible base of institutional support for complex negotiations across the Strait and for bloody political battles in Taipei.

Conclusions

Unprecedented stress

Taiwan is headed for a period of domestic and foreign political stress that is unprecedented since Chiang Kai-shek's troops moved to Taiwan in the late 1940s. The result, at a minimum, is going to be market volatility and general uncertainty until it is clear whether Chen can deal with the forces of chaos both across the Strait and in Taipei itself.

But also unprecedented resilience

Counterbalancing this, there is extraordinary political flexibility and goodwill, together with extraordinary economic resilience. Taiwan at the beginning of 1999 was headed toward unprecedented consensus at home and peace abroad. It had resolved the old tensions between mainlanders and locals, and agreed on being New Taiwanese. It had resolved the division over China policy and reached consensus on the status quo. China was looking inward and just wanted to build its economy. Without Lee Teng-hui's decision to impose an unpopular candidate, the KMT in the person of James Soong would just have triumphed yet again, the domestic consensus would be intact, and there would have been no need for the gambit that created the crisis over state- to-state relations.

The fundamentals support a better situation

In fact, the basis for consensus at home and peace abroad remains intact. There are no fundamental divisions over economic policy, except over the KMT empire, which is a small proportion of the economy. There is a consensus on the status quo with China, if it can be restored and the right name can be given to it. China has shown willingness to tolerate Taiwan's democracy so long as Taiwan's democracy calls itself part of China. The economy of Taiwan is the best-managed and most resilient in Asia, thanks to good KMT stewardship for half a century, and it can withstand all manner of personal and factional political fireworks in Taipei.

Given these strong fundamentals, there is a good chance that Taiwan can use this crisis to move to a new threshold of real democracy, an even more vigorous economy freed of political shenanigans, and a more stable relationship with the mainland.

But high risk remains

Nevertheless, investors would be wise to wait a while to see whether the assorted politicians can take proper advantage of the opportunity.

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