

Taiwan

Status Index (Democracy: 9.35 / Market economy: 9)	9.18	Management Index	7.37
HDI	0.902 ¹	Population	22.7 mio. ⁴
GDP p. c. (\$, PPP)	23,400 ²	Population growth	0.64 ⁵
Unemployment rate	4.09 ³	Women in Parliament	20.9 ⁶
UN-Education Index	n/a	Poverty²	0.83 ⁷
		Gini-Index	32.6 ⁸
<p>¹Figure for 2002 released by DGBAS. ²Estimated figure for 2003. ³Figure for Dec. 2004. ⁴Figure for July 2004. ⁵Estimated figure for 2004. ⁶Figure for latest parliamentary election in Dec. 2004. ⁷Official figure for “low-income population” in 2003. ⁸Latest figure for 2000.</p> <p>Source: Directorate-General of Budget, Accounting and Statistics, R.O.C. (http://www.dgbas.gov.tw/); Council for Economic Planning and Development, R.O.C. (http://www.cepl.gov.tw/); Election Study Center, National Chengchi-University, R.O.C. (http://www.nccu.edu.tw/); CIA World Factbook 2004 (http://cia.gov/cia/publication/factbook/).</p>			

A. Executive summary

This report will show that throughout the review period Taiwan has made progress in economic transformation and enjoys a consolidated democracy that has withstood the latest test of sharp domestic polarization and critical cross-strait relations after two elections of a pro-independence president in 2000 and 2004. The positive accomplishments of Taiwan’s political transformation after the 1986 to 1987 period - such as a high degree of state coherence, meaningful elections, the absence of undemocratic veto powers, stable democratic institutions and a vibrant civil society - have been preserved, the unresolved issue of national identity notwithstanding.

In the 2000 to 2001 period, Taiwan faced the strongest recession since the 1970s due to the aftermath of the Asian financial crisis and legislative paralysis during the first administration of Chen Shuibian. Taiwan’s well-institutionalized market economy has rebounded strongly since then. This was accompanied by new efforts at financial sector reform, which strengthened the banking system and will result in more resilience for Taiwan’s economy in the future.

Taiwan’s level of socioeconomic development is high, with income distribution remaining close to equal and social disparities still rather small. Currency and prices are stable. Economic development is based on a well-developed education system and a sound research and development (R&D) sector. Property rights are well defined, and reforms of the welfare regime have made further progress. Political extremism is non-existent.

On the negative side, welfare policies are still insufficient to fully protect the people from the negative side effects of a capitalist system. Government budgets have suffered from substantial deficits throughout the review period due to Keynesian policies in the aftermath of the Asian financial crisis, rising burdens concerning social welfare and military procurement in particular. A zero-sum mentality among Taiwan's political actors still leads to friction and highlights the lack of experience with institutionalized consensus-building beyond established party boundaries, clearly to the detriment of Taiwan's economic development and political coherence.

However, the biggest danger to the country's democratic transformation clearly stems from the Chinese sovereignty claim over the island and Beijing's threat of using force to bring about unification. Certainly, this danger has intensified by the pro-independence policies of the first Democratic Progressive Party (DPP) administration while it hardly affected the functionality and domestic legitimacy of Taiwan's democracy. At the time of this writing in the beginning of 2005, Taiwan is at the point of turning into a "normal democracy" that may or may not survive the tide of the times.

B. History and characteristics of transformation

In Taiwan, political transformation took a backseat to economic transformation. The foundations of a sound market economy were laid in the 1950s under the authoritarian leadership of Chiang Kai-shek. During that time, the state intervened strongly in economic affairs, regulating and protecting domestic markets. During four decades of authoritarian rule until the end of the Chinese civil war in 1949, Taiwan moved gradually toward a social market economy, and rudimentary social insurance systems were established. Democratic transition started in 1986 with the illegal founding of the DPP on September 28 - which was then tolerated by the ruling Guomintang (GMD) regime—and the lifting of martial law on October 15 of that year. More reforms followed, most importantly the legalization of new political parties in January 1991. In 1991 and 1992 respectively, Taiwan saw the first ever free elections of its central parliamentary bodies, the National Assembly and the Legislative Yuan, marking the end the transition process.

During the rest of the 1990s, democracy matured by successive constitutional reforms that, among other changes to Taiwan's political system, paved the way for the first direct presidential elections held in early 1996. These were won by incumbent president and GMD party chief Li Denghui, who became Taiwan's "father of democracy". Successful democratic consolidation was already achieved when Chen

Shuibian, an experienced DPP politician and former advocate of Taiwan independence, unexpectedly won the March 2000 presidential elections and made the GMD an opposition party for the first time since the end of the authoritarian era.

The following four years saw severe legislative inefficiency as the ruling DPP and the GMD led opposition, which commanded a numerical majority in parliament, thus paralyzing each other. Cross-strait relations further soured as the new president pursued an agenda of assuring Taiwanese sovereignty against Beijing's "one China principle" and pushed for a referendum law and a new constitution during the March 2004 presidential campaign. After his narrow victory of just some 30,000 votes, Taiwan's democracy was hijacked by a legal brawl on the ballot's outcome and the investigation of an alleged assassination attempt on Chen and his running mate Lu Xiulian on the eve of the presidential election.

However, the political institutions proved to be strong enough and the public mind sufficiently rational to overcome the turmoil of the election aftermath. Parliamentary elections in December 2004 did not change the impasse in the legislature, with Chen's ruling DPP and its "green camp" ally, the Taiwan Solidarity Union, failing to achieve an absolute majority. In early 2005, it is unclear whether the political bickering of the previous four years will continue or if a more constructive deal can be struck between the opposing camps. Given the negative impact of domestic power politics on the economy during the first Chen administration, another four years of legislative standstill and suspended economic and social reform might seriously undermine the public's trust in the political elites, while Taiwanese democratic institutions will remain solid.

Taiwan's transformation into a burgeoning market economy and industrialized country took place in several stages. During the 1950s, import substitution following successful agrarian reforms from 1949 to 1953 created a strong light-industrial sector that absorbed all surplus labor. This policy was supported by U.S. economic aid amounting to about \$100 million per year between 1951 and 1965. In the early 1960s, Taiwan shifted to export-led industrialization by systematically liberalizing markets and, by the means of fiscal stimuli, supporting new industries to become internationally competitive. From the start of the 1970s, Taiwan's labor-intensive economy quickly turned capital- and technology-intensive, making it one of the leading trading nations in East Asia.

The Asian financial crisis had only limited effect on Taiwan with its currency regime restricting speculative trade with derivatives, its export economy predominantly based on small and medium-sized enterprises with low demand for credit, and its financial system comparatively sound. However, poor performing loans have become a major problem in the aftermath of the crisis when the banking system and Taiwan's

notorious local credit cooperatives came under more scrutiny by the government and the media. During the review period, Taiwan's economy regained strength after a serious recession and unemployment rates at historic peaks in 2001. Banking and financial sector reform has proceeded, as have (more protracted) efforts to strengthen the social welfare system.

C. Assessment

1. Democracy

Since the takeover of a DPP government in the middle of 2000, Taiwan's democracy has proved to be stable; serious transformation shortcomings no longer exist. However, the deadlock in the legislature and strong polarization between the different party camps has led to much vexation and even anxiety among the island population. Administrative systems are functional, while public safety and order have been generally assured.

1.1. Stateness

Taiwan's status under international law remains unclear. However, the Taiwanese state (officially named Republic of China) enjoys effective power and authority over its territory, including the islands of Taiwan, Penghu, Mazu and Jinmen. The conflict over Taiwan's political future as an independent nation-state or a part of a new and unified China is yet to be resolved. The overall majority of Taiwanese support the current status quo in the Taiwan Strait, which serves their security interests best. However, most studies show that Taiwanese national identity has been constantly strengthening since the early 1990s, deepening the people's identification with their state.

1.2. Political participation

In Taiwan, there are no restraints on elections, which are usually fair and undisputed. However, the latest 2004 presidential ballot saw a serious battle of the opposition "blue camp" against alleged fraud instigated by the incumbent president and his party. Besides some 300,000 invalid votes, the GMD and the People First Party (PFP) leaders accused president Chen Shuibian of having faked an assassination attempt that may have secured his razor-thin victory by mobilizing last-minute sympathy votes. However, the judiciary later rejected these allegations. The influence of organized crime on local party organizations, particularly on the part of the GMD,

still presents a problem, though Chen Shuibian's government has made further progress to contain this phenomenon during the review period.

All elected rulers have effective power to govern, and there are no veto powers or exclusive political domains that might negatively affect democratic participation.

Freedom of association and freedom of assembly are unrestricted. Union activities are still constrained by law, but independent union organization has become more viable over the years, and important labor reform bills are awaiting passage in the Legislative Yuan. Freedom of opinion and freedom of the press are unrestricted. The former control of the media by the mainlander elite to the disadvantage of other groups—Hoklos, Hakkas and aborigines—has practically vanished.

1.3. Rule of law

The separation of powers among the executive, legislative and judicial branches is largely established. The constitution still lacks a sufficient definition of the relationship between parliament (Legislative Yuan) and president in the event that the president is supported only by a minority in the parliament - as has been the case since 2000.

Politics in Taiwan is still very much based on a zero-sum mentality of the political actors that does not yet allow for sustainable informal consensus-building or even formal coalition agreements between different party camps. This has resulted in continuous bickering in the Legislative Yuan during the first Chen administration (2000–2004) and a virtual paralysis in legislation. After a new Chen administration was sworn in May 2004, it remains to be seen at this point if a more constructive mode of interaction between the GMD and DPP can be established in coming years.

Progress has been made concerning judicial independence. Political influence on court decisions was not observed, and the judiciary's reputation has substantially improved. The Taipei High Court was in the public spotlight for much of 2004, as it had to deal with the opposition's legal fight against the outcome of the March presidential elections. It rejected two lawsuits filed by the GMD and PFP because of lack of evidence for fraud, decisions that attracted criticism by those parties but broad acceptance as impartial verdicts by the population. Political corruption receives a great deal of attention in the mass media and it is prosecuted under criminal law. Members of parliament, cabinet members, and members of county and city parliaments enjoy immunity. Civil rights are not restricted, and those who violate them are taken to court.

1.4. Stability of democratic institutions

All relevant political actors accept the democratic institutions as legitimate. As a rule, all institutions work according to fixed procedures and are sufficiently controlled by a working system of mutual checks and balances. However, institutional efficiency is hampered by the confrontation between a DPP-led minority government and a GMD-led opposition majority in the Legislative Yuan. Since the population has shown considerable dissatisfaction with this situation and responded with a rather low voter turnout in the December 2004 Legislative Yuan elections, the political parties feel some pressure to adjust their parliamentary tactics in the coming years.

1.5. Political and social integration

A stable, moderate, socially anchored party system enjoying broad popular consent has developed in recent years. However, this system suffers from polarization in the run-up to important elections, as the two opposing party alliances (the “blue camp” of GMD, PFP and New Party or NP and the “green camp” of DPP and the Taiwan Solidarity Union or TSU) focus on nationalist and ethnic issues reviving the old conflict between Taiwanese and mainlanders.

A major decision was made in August 2004 when the Yuan abolished the old single non-transferable vote (SNTV) electoral system and introduced a single district, dual vote system. Pending a constitutional revision scheduled for May 2005, this will very probably result in the disappearance of Taiwan’s smaller parties and the establishment of a more stable two-party system. The network of interest groups is relatively close-knit and politically influential. Only Taiwan’s trade unions are not particularly powerful, mainly because of the prevalence of small and medium enterprises and the legacy of the authoritarian era. Voter turnout, which generally is between 70 % and 80 % for national and local elections, highlights the population’s strong consent to democracy. Only the latest legislative elections in December 2004 saw a sharp decline to 59 % after a long and extremely conflict-filled election year that fatigued many voters. Trust is high among the population, although still hampered to some extent by the so-called Taiwanese-mainlander conflict and the contentious issue of national identity.

2. Market economy

2.1. Level of socioeconomic development

The key indicators show a high level of development. Among the group of transformation countries in Asia and Oceania, Taiwan ranked second on the HDI

scale after Singapore in 2004 (the 2002 figure has been computed by Taiwanese authorities along HDI methodology because Taiwan does not appear as a separate entity in HDR statistics). The country's level of socioeconomic development permits adequate freedom of choice for all citizens. Fundamental social exclusion because of poverty is qualitatively minor and not structurally ingrained. Income distribution—as measured by the Gini coefficient—is still relatively equal, even if slightly less balanced than in the past. According to the latest available figures, Taiwan's Gini coefficient stood at 0.345 in 2002 after 0.326 in 2000. Representation of women in the country's parliament stands at 20.9 % after the December 2004 parliamentary elections, which is a high value in regional perspective.

2.2. Organization of the market and competition

Taiwan's market economy is institutionally sound with clearly defined and state-guaranteed rules for ensuring fair competition and with largely equal opportunities for all market participants. Compliance to the WTO regime, to which Taiwan gained access in January 2002, has so far not been criticized by other members.

The state refrains from intervening in investment planning and foreign trade with the exception of cross-strait economic relations, mainly for security reasons and in order to control the level of Taiwan's trade dependency on China. However, recently existing rules have been changed for more investment capital to be transferred to the mainland and more imports of Chinese goods allowed into Taiwan. At the same time, the state is urged to further liberalize trade between the two sides by an influential community of Taiwanese businesspeople heavily engaged in China's economic development. The Fair Trade Law promulgated in 2002 ensures a coherent and effective anti-monopoly approach, although state monopolies or quasi-monopolies still exist in certain sectors, for example energy, telecommunications and transport.

Because union organization and activism has become stronger in recent years, the DPP government has backtracked on the administration's earlier declared commitment to the 1991 statute governing the privatization of state-run enterprises (SOEs). In accordance with this regulation, another 18 SOEs must still be privatized. Meanwhile, financial restructuring (a response to worrisome ratios of non-performing loans piling up to 8.8 % in March 2002 according to government figures - November 2004: 4.35 %) has made good progress, such as the establishment of asset management companies and financial asset services companies authorized to purchase bad loans. Moreover, a four-grade, reward penalty measure was introduced by the Ministry of Finance in April 2003 in order to supervise a bank's non-performing loan ratio.

Generally speaking, a systematic overhaul of the financial and banking system, which started in 1997, continued during the review period, downsizing the overcrowded banking sector, enhancing transparency of banking operations and further liberalizing capital markets. Consequently, both systems have gained solidity and maintained a decent degree of resilience to cope with speculative investment. Stricter regulation and control of Taiwan's notorious local credit cooperatives still lags behind, but is under debate. Taiwan ranked 12th in the International Institute for Management Development (IMD) World Competitive Yearbook (2004) for "nurturing competitiveness," making a jump from the previous year's 17th place and highlighting the government's efforts to enhance the overall efficiency of Taiwan's market economy.

2.3. Currency and price stability

Inflation has been constantly negative during most of the review period and climbed up again only recently (2004: 1.6 %), reflecting a high degree of price stability and consistent foreign exchange policies. This has led to a slight depreciation of the New Taiwan (NT) dollar against the U.S. dollar, the Japanese yen and the euro. The Central Bank of China has been independent since the middle 1980s and it enjoys a reputation of sound monetary supervision and control. Taiwan's total public debt and budget deficit are problematic and stood at 26.9 % and -3.1 % of the GDP at the end of 2004 respectively, with debt rising continuously over the review period. In addition, external debt ratios have been constantly going up, forcing the government to carry through difficult adjustment measures in coming years.

2.4. Private property

Taiwan's property rights regime is well established and its market economy overwhelmingly based on private ownership. Long-term privatization of SOEs and government banks has continued, albeit slowly, and remains consistent with official anti-monopoly policies and market principles. However, privatization meets growing resistance of Taiwan's trade unions, which have staged several protests against the government's SOE policy and are determined to go on fighting the legally binding 1991 statute governing the privatization of state-run enterprises. In addition, SOE privatization has only been moderately successful so far, with eight out of 13 former state-owned enterprises having gone bankrupt in the process.

2.5. Welfare regime

Taiwan's welfare regime has made progress during the period of review and is certainly one of the most developed ones in the Asian Pacific region. However, funding the different schemes is a problem, especially in times of severe budget and expenditure constraints.

National health insurance was introduced in 1995 and it covers a wide range of medical treatment for all employees. Revenue is usually collected from monthly salaries (4.5 %), split among employees, employers and the government. However, the government was forced to launch an emergency package to save the scheme from bankruptcy in early 2005. Extensive outpatient treatment seems to be one of the main reasons for the current problems; insufficient financing is another. Comprehensive farmers' health insurance was introduced in late 2002 for all farmers over 15 years of age engaged in agricultural work for more than 90 days a year. This new scheme has closed a serious gap within the national health insurance system, which does not include farmers.

A compulsory national unemployment insurance scheme combined with a vocational training and employment service system took effect in January 2003 covering all employees. A draft law for a new labor insurance pension plan is currently under revision in the Yuan to provide for a system that, among other issues, introduces individual pension accounts portable between companies. This would be an important modification of the old labor insurance law operating with non-transferable accounts only, given the high degree of job fluctuation in Taiwan's economy dominated by small and medium enterprises. These enterprises do usually not survive the current 15 to 25 years during which an employee has to stay at the same firm before becoming eligible for pension benefits. It would also reduce the huge pension gap that exists between Taiwan's workers and the traditionally privileged public sector employees and civil servants.

Besides the government's efforts to establish the necessary institutional framework, a growing number of non-governmental organizations (NGOs) has ensured that emerging social differences are publicly debated and could so far be sufficiently compensated. Women's rights and welfare have been considerably strengthened over the last 10 to 15 years, although the picture gets much darker for those women laborers of mostly Southeast Asian countries are taken into account that have been coming to Taiwan in rising numbers recently. Like in other transforming countries, taking care of foreign laborers remains an underdeveloped field of social welfare policy in Taiwan.

2.6. Economic performance

Taiwan's economy has regained strength during the review period. While facing negative growth in 2001 (-2.18 %), it has continuously increased since then to 5.93 % in 2004. This corresponds with rising import figures since 2002 and decreasing unemployment (at a historical peak in 2002) as well as rising private consumption since 2004. Taiwan's export figures have also done well after 2001, resulting in a solid positive current account. The island's overall trade surplus (2003: \$16.9 billion) is significantly topped by its trade surplus with China (2003: \$24.4 billion), pointing at rising ratios of trade dependency on the mainland that are approaching the critical 10 % threshold (2004: 9.4 %) and that have been worrying many in Taiwan for a long time (Taiwan Mainland Affairs Council).

2.7. Sustainability

Environmental awareness has been on the rise in Taiwan since the 1980s. Environmental protection has been institutionally integrated at the government level both independently (by the Environmental Protection Administration or EPA) and at the sub-divisional level within different government entities, resulting in systematic environmental policy planning and a relatively low externalization of costs over the years.

Taiwan has a very well developed education system with high quality secondary and tertiary education as well as vocational training, reflecting the special value that education enjoys in this post-Confucian society. School curricula now undergo continuous reform to keep the education system in line with international developments. Education amounted to 18 % to 20 % of all government expenditure and to 4.3 % to 4.5 % of the GDP between 2001 and 2003.

Launched in 2002, the Challenge 2008 a six-year national development plan aims at making Taiwan the leading R&D location in Asia and bringing about "digital Taiwan." Consequently, public sector research and official support for Taiwan's various science parks stands high on the agenda of government finance. Between 2.2 % and 2.5 % of the GDP has been spent on R&D during the review period.

3. Management

3.1. Level of difficulty

Taiwan enjoys few structural constraints on governance thanks to the following factors: its high level of socioeconomic development; its sound market economy and

good economic performance; well-developed education system and research environment; well-qualified labor force; capable bureaucratic apparatus; low social disparities in terms of income and status; the lack of serious ethno-religious conflicts; and an unchallenged state monopoly. Although Taiwan's traditions of civil society, rule of law and democracy are weak given its colonial past and long authoritarian era after 1945, social movements and social interest organizations of all sorts are now firmly entrenched in society and play an essential part in the daily exercise of democracy.

The conflict between mainlanders and Taiwanese has evolved into a cleavage between Taiwanese disagreeing on the most sensible approach vis-à-vis China in order to secure long-term stability and prosperity for the island. This has resulted in high-gear political polarization putting some constraints on the efficiency of Taiwan's government institutions, especially concerning the relationship between the president and the Legislative Yuan. Undoubtedly, the Chinese claim over Taiwan is the biggest caveat to the generally positive assessment of Taiwan's level of difficulty.

Profile of the Political System

Regime type:	Democracy	Constraints to executive authority:	2
System of government:	Presidential-parliamentary	Electoral system disproportionality:	11.6
		Latest parliamentary election:	11.12.2004
		Effective number of parties:	3.3
Head of State:	<i>Chen Shui-bian</i>		
Head of Government:	<i>Frank Chang-ting Hsieh</i>	Cabinet duration:	01.02.2005- present
		Parties in government:	2
		Number of ministries:	7
		Number of ministers:	39

Source: BTI team, based upon information by country analysts, situation in July 2005. Constraints to executive authority (1-6 max.) measures the institutional constraints posed by a federal or decentralized state, a second parliamentary chamber, referenda, constitutional and judicial review and the rigidity of the constitution. Electoral disproportionality (Gallagher index) reflects the extent to which electoral rules are majoritarian (high values) or proportional: $\frac{1}{2} (v_i - p_i)^2$; v_i is the share of votes gained by party i ; p_i is the share of parliamentary mandates controlled by party i . For presidential/ semi-presidential systems, the geometric mean of presidential election and parliamentary election disproportionality is calculated. Effective number of parties denotes the number of parties represented in the legislature, taking into consideration their relative weight (Laakso/Taagepera index) = $1 / (\sum p_i^2)$; p_i is the share of parliamentary mandates controlled by party i . Number of ministries/ ministers denotes the situation on 1 January 2005.

3.2. Steering capability

The government's strategy of economic and social reforms was largely determined, but also hampered, by sometimes-uncompromising political leadership and the choice of confrontational tactics against the background of a minority government having to come to terms with a highly politicized and hostile opposition. This resulted in a

deadlock in parliament and lost time negatively affecting the reform drive that Taiwan needs to further adjust its economic, financial and social systems. With the March 2004 presidential elections approaching, the DPP administration was becoming ever more focused on its political agenda to promote Taiwanese consciousness and nation building, forcing the GMD and PFP opposition to counter on the very same battleground of national identity, thus neglecting other policy fields. In fact, Taiwanese politics has become completely high jacked by the cross-strait conflict and the issue of national identity, making concerted reform policies difficult. Given the results of the December 2004 parliamentary elections that have prolonged the situation of a DPP government facing a “blue camp” majority in the Legislative Yuan for at least another three years, the Taiwanese leadership’s steering capability might further deteriorate. However, public pressure might also entail new efforts to cooperate and overcome the traditional zero-sum mentality of Taiwan’s political actors, ushering in a new era of inter-party cooperation.

3.3. Resource efficiency

The government generally makes efficient use of available economic and human resources to pursue its transformation policies. Financial sector reform has been planned adequately and implemented efficiently. Public service is cost effective and reliable, although comes under regular attack during the typhoon season when heavy rainfalls and landslides plague the island and put pressure on local administrations. Corruption has been curbed quite successfully in recent years and is exposed to extensive media coverage and public debate whenever a case is reported.

The Council of Organizational Reform at the government level was established in May 2002 for driving forward government reform, particularly focusing on deregulation, decentralization and outsourcing. Taiwan has also tapped into a huge electronic government project to provide special Internet services to the public and enhance administrative efficiency.

The institutional framework of governance generally provides for a high degree of coordination among conflicting political objectives and their translation into coherent policies. However, given the current standoff between the DPP and the GMD-led opposition, policy coherence is often hampered by unavoidable compromising in the legislature or counterproductive insistence on second-best solutions just for carrying away a small political victory. Intra-governmental lacunae can be a side effect of this.

3.4. Consensus-building

All major political actors agree on building and strengthening Taiwan's market-based democracy. No veto power has survived the democratic transition and consolidation process of the late 1980s and 1990s.

The most serious domestic cleavage between advocates of Taiwan independence and those of Chinese unification is reflected in the party system and has, albeit much less than in the past, an ethno-political dimension. The DPP government under Chen Shuibian has aggravated these tensions by pushing Taiwanese nationalism and rejecting the "one China" principle as a precondition for Sino-Taiwanese talks. Consequently, the political confrontation between the opposing party camps has become more uncompromising than ever before. At the same time, however, this does not lead to irreconcilable tensions in the broader society, which has proved to be pragmatic and ready to stop all political gambling with the cross-strait issue or national identity at the ballot box. Therefore, while the current leadership limits its own capabilities of promoting social capital among Taiwan's citizens by its political agenda, it does not necessarily destroy interpersonal trust and solidarity at their present levels. Its efforts to nurture a feeling of national belonging and identity must also be seen as a project to build up such trust and solidarity against the past legacy of ethnic and political antagonism.

3.5. International cooperation

Since it is not admitted into international and regional organizations and bodies in a state capacity because of China's resistance, it is important to Taiwan to demonstrate proven credibility, reliability and generosity in the international arena. By trying to convince the world public that the degradation of its sovereignty is unfair and that its diplomatic isolation deprives the international community of fully making use of Taiwan's expertise and financial might, Taiwan enjoys a good reputation as political partner and willful donor of development aid and humanitarian assistance - although this is often linked to political expectations to raise Taiwan's international recognition or even gain diplomatic status (known as "dollar diplomacy").

Under designations such as "Chinese Taipei", Taiwan has diplomatic relations with 25 states (as of January 31, 2004), which are diplomatically of minor importance and constantly pressured by China to switch camps. It has extended its membership to 22 intergovernmental organizations, most prominently among them the World Trade Organization. Moreover, it maintains 92 representative offices or branch offices in the capitals and major cities of 59 countries. Although these carry various names like "Taipei Representative Office" or "Taipei Economic and Cultural Office", they perform most of the functions of embassies and consulates general. At the same time,

48 countries without formal diplomatic relations with Taiwan have established 58 representative offices or visa-issuing centers on the island (Government Information Office, Taiwan Yearbook 2004, p. 117).

Concerning cross-strait relations, the DPP-led administration under president Chen Shuibian has made repeated overtures to the Chinese government for restarting a dialogue. His continuous rejection of the “one China” principle as a pre-condition for such talks, as well as strong pro-independence policies, has done nothing to strengthen Beijing’s trust in Chen. Still, lacking credibility in Beijing under conditions of a serious military threat does not discredit Taiwan’s overall reliability elsewhere.

4. Trend of development

4.1. Democratic development

Taiwan has already enjoyed an uncontested state monopoly on the use of force, an efficient public administration, a working judicial system, good quality public services, stable public safety and resilient democratic institutions before the review period.

Democratic consolidation was confirmed under the first Chen administration (2000–2004) during a standoff between the president and the opposition-dominated legislature. It was further confirmed by the post-election turmoil in 2004, when Chen’s razor-thin victory in the March presidential elections was tarnished by a mysterious assassination attempt on the eve of the elections and charges of fraud by a frustrated opposition. Although political participation declined somewhat in the ensuing legislative elections of December 2004 due to the people’s estrangement from politics after a year of uncompromising party quarreling, this does not indicate any long-term political troubles. The judiciary has proven its impartiality when dealing with two legal suits filed by the GMD-PFP alliance to annul the result of the presidential elections.

Taken as a whole, the stability of Taiwan’s democracy has been preserved, while it faced a decline in institutional efficiency. Taiwan’s party system awaits major changes after another constitutional revision expected in 2005 when the current SNTV system will be changed into a proportional voting system resembling the German model. There is much to be said for the evolution of a two-party system that fits Taiwan’s political landscape better than the current one and will deepen its democracy further.

4.2. Market economy development

Recent available indicators of social and economic development for most criteria of human development, gender equality, education levels and per capita income show progress over the review period.

Table 2: Development of socio-economic indicators of modernization

	HDI	GDI	GDP Index	Gini Index	UN Education Index	Political representation of women	GDP per capita (\$, PPP)
2000	0.891	0.888	n.d.	32.6	n.d.	22.2	22,760
2002	0.902	n.d.	n.d.	n.d.	n.d.	26.4 ¹	23,400 ²

¹Figure for latest parliamentary election in Dec. 2004; ²Estimated figure for 2003.

Source: Directorate-General of Budget, Accounting and Statistics, R.O.C. (<http://www.dgbas.gov.tw/>); Council for Economic Planning and Development, R.O.C. (<http://www.cepd.gov.tw/>); Election Study Center, National Chengchi-University, R.O.C. (<http://www.nccu.edu.tw/>); CIA World Factbook 2004 (<http://cia.gov/cia/publication/factbook/>).

The institutional framework of Taiwan's market economy has improved during the review period, mainly due to ongoing reforms in the financial and banking systems. WTO-led tariff reductions have proceeded and import controls been further eliminated. Measured in macroeconomic data, the economy has been back on the track of substantial growth after the 2000-2001 recession and therefore made a significant jump compared with the preceding review period. It is therefore fair to say that Taiwan's economy has improved both quantitatively and qualitatively over the last four years.

Table 3: Development of macroeconomic fundamentals (2001–2005)

	2001	2002	2003	2004	2005**
Growth of GDP in %	-2.2	3.6	3.3	5.9	4.3
Export growth in %	-17.2	6.3	10.4	6.2	n.d.
Import growth in %	-23.4	4.9	13.1	21.3	n.d.
Inflation in % (CPI)	-0.01	-0.20	-0.4	1.6	0.48 (Jan.)
Investment in % of GDP	18.7	17.7	17.4	18.4	18.6
Total tax revenue in % of GDP	13.3	12.6	12.7	12.9	n.d.
Unemployment in %	4.58	5.16	5.00	4.09	n.d.
Total public debt in % of GDP	29.7	29.7	32.2	33.7	34.0
External debt in % of GDP	12.2	16.0	22.0	26.9	27.4
Budget deficit in % of GDP	-6.7	-4.4	-2.9	-3.1	-3.2
Current account balance in \$billions	17.9	25.6	29.0	20.3	22.4

* Estimated figures; ** Projected figures.

Source: Ministry of Finance, R.O.C. (<http://www.mof.gov.tw/>); Directorate-General of Budget, Accounting & Statistics, R.O.C. (<http://www.dgbas.gov.tw/>); Deutsche Bank Research (<http://www.dbresearch.com>).

D. Strategic perspective

Taiwan has seen a very successful transformation into a market-based economy since the 1950s and into a consolidated democracy during the 1990s. The historic transfer of power in 2000 when the DPP won the presidency and took charge of the government for the first time has put quite a lot of pressure on political institutions. In spite of party infighting and legislative paralysis during the first administration of Chen Shuibian, Taiwan's democracy proved to be strong enough to cope with these problems. At the time of this writing at the beginning of 2005, the blue and green camps have to decide about their future relationship: ongoing confrontation or a turn toward more cooperation for the benefit of the people's well being.

The upcoming National Assembly elections in May, which must seek the support of the people via referendum, will further deepen Taiwan's democracy. The elections are supposed to pave the way for the passage of another constitutional reform package that will do away with the National Assembly itself, introduce a voting system of proportional representation, downsize the Legislative Yuan by more than half of its current seats, and bestow the right of constitutional revision upon the legislature.

However, this process will not go on without new challenges to the Sino-Taiwanese relationship. Abolishing the pan-Chinese National Assembly and establishing the right of referendum for constitutional change will be taken as striking evidence of Taiwan's quest for independent statehood by the Chinese government. With bilateral relations at an all-time low since Li Denghui's famous statement in 1999 that Taiwan and China maintain a "special state-to-state relationship", a military confrontation in the Taiwan strait can not be ruled out.

However, China's sovereignty claim over Taiwan does not affect the latter's democracy too much, since all political actors and party camps subscribe to the idea that present-day Taiwan enjoys undisputable sovereignty and independence. They only differ on the question of how this fact should translate into a reasonable Chinese policy that ensures Taiwan's security and prosperity in the future. The European Union may be more assertive in demanding a peaceful solution to the cross-strait conflict and, for the sake of its own interests affected by Asian-Pacific security, may be more outspoken on the possibility of temporary dual state coherence under the roof of "one China".

There is more conceptual creativity and political courage needed to resolve the conflict peacefully. Taiwan's market economy is sound, although more still has to be

done to strengthen the financial sector and to control non-performing loan ratios. The current budget deficit is explained by an official stimulus policy to revive the economy after its sharp downturn in the 2000 to 2001 period, but must be reduced to back up confidence in the government's economic competence and in long-term state capacity.

It seems at this point that Taiwan's political parties realize the need to overcome their zero-sum mentality in order to bring about more inter-party trust and cooperation. The change of leadership soon expected in the GMD and PFP, but also in the DPP before long, will probably contribute to more pragmatism in Taiwan's party politics and cross-strait relations. For the time being, Taiwan faces as many challenges as opportunities for the continuation of its success story.