

SECTION 2: CHINA AND TAIWAN

Introduction

On May 20, 2016, Taiwan's President Ma Ying-jeou, whose policies led to an eight-year period of improved relations between Taiwan and China, left office and Tsai Ing-wen of the Democratic Progressive Party (DPP) became president of Taiwan. President Tsai has pursued a pragmatic cross-Strait policy of "maintaining the status quo" of neither formal independence for Taiwan nor unification of Taiwan and China. However, she has not acquiesced to Beijing's demand that she endorse the "one China" framework for cross-Strait relations that Taipei and Beijing both endorsed during the Ma Administration. Although Beijing's approach to the Tsai Administration is still developing, cross-Strait relations have entered a new period, and Beijing is using various levers to pressure President Tsai, including the suspension of official communication with Taipei.

President Tsai faces tremendous challenges in formulating a cross-Strait policy, boosting Taiwan's economic growth, and addressing the threat from China's military modernization. She is pursuing the objectives of diversifying Taiwan's export markets and enhancing Taiwan's deterrent capability, efforts in which Taiwan's relationship with the United States plays a key role. U.S.-Taiwan economic and security ties are robust, but they also have areas in need of strengthening.

The United States continues to support Taiwan's efforts to participate in the international community. Taiwan's international engagement expanded during the Ma Administration, but it remains limited in many ways due to Beijing. Since President Tsai's election, Beijing has increased its pressure on Taiwan in the international arena, a problem that could grow more severe in the coming years if cross-Strait relations sour significantly.

This section explores cross-Strait relations since President Tsai's election, cross-Strait trade and investment, Taiwan's international engagement, Taiwan's military and security situation, and U.S.-Taiwan relations. It is based on consultations with experts on Taiwan and cross-Strait relations, the Commission's fact-finding trip to Taiwan and China in 2016, and open source research and analysis.

Cross-Strait Relations

Cross-Strait Political Relations after President Tsai's Election

Despite President Tsai's efforts to reassure Beijing of her policy direction, the Chinese government has suspended official communication with Taipei. Also, during the Commission's June 2016 trip to Taiwan, a Taiwan official told the Commission that China had

reduced visits to Taiwan by Chinese tourists.¹ So far, however, Beijing has refrained from taking some of the more drastic costs-imposing measures it could direct against Taipei, such as enticing countries with diplomatic relations with Taipei to cut ties and establish relations with Beijing instead, or stopping the implementation of cross-Strait agreements that were signed under the Ma Administration.²

Taiwan's 2016 Elections

Taiwan's electorate achieved several milestones in 2016: the election of Taiwan's first female president, the third peaceful transition of presidential power between political parties, and the DPP's first absolute majority in Taiwan's legislature—the Legislative Yuan. Tsai Ing-wen won the election with 56.1 percent of the vote, while Eric Chu, the presidential candidate of the Chinese Nationalist Party (Kuomintang or KMT), finished with just 31.1 percent.³ DPP candidates also won 68 seats in the Legislative Yuan compared to 35 seats for the KMT and 10 for other parties.⁴

The election outcomes were the result of voter dissatisfaction with the outgoing Ma Administration and the KMT as well as with Taiwan's struggling economy, President Tsai's focus on domestic economic issues (rather than cross-Strait relations) during the campaign, and the rising concern among Taiwan citizens about the potential negative impact of growing ties with China on Taiwan's economy and political autonomy.⁵ According to Lin Chien-fu, a professor in the department of economics at National Taiwan University, who met with the Commission in Taiwan, the problem of unaffordable housing in Taiwan also was an important issue for voters.⁶ The housing price to income ratio increased by almost one-half.⁷ Real wages fell following the 2008–2009 global financial crisis and failed to recover to pre-crisis levels in subsequent years.⁸

During President Ma's tenure, which was characterized by a thaw in some aspects of cross-Strait relations and a reduction in overall tensions, Taiwan and China signed 23 cooperation agreements and expanded economic, educational, travel, and government-to-government contacts and communication. These initiatives culminated in a meeting between President Ma and Chinese President and General Secretary of the Chinese Communist Party Xi Jinping in Singapore in November 2015, the first meeting between the leaders of Taiwan and China since 1949. During President Ma's two terms in office, however, Taiwan's economic growth slowed significantly amid stagnant wages, unemployment in Taiwan's largely high-skilled workforce, weak entrepreneurial innovation, low inbound investment, and an electorate increasingly worried about China's ability to influence Taiwan and the impact of agreements with China on Taiwan's economy.⁹

Taiwan's Economic Challenges

Taiwan faces many economic challenges. First among them is the Taiwan economy's dependence on exports, particularly to China. (See section on "Cross-Strait Trade and Investment" for more information.) The Tsai Administration seeks to shift Taiwan's "efficiency-driven model" to an "innovation-driven model."¹⁰ The efficiency-driven model refers to Taiwan's economic strategy of linking itself to regional supply chains, primarily through China, and expanding exports to increase growth. A Taiwan official told the Commission that the Taiwan government wants to collaborate with the United States, Japan, Europe, and Israel to develop a model for innovation in Taiwan and collaborate in the areas of research and development (R&D), human resources, and financial capital. Taipei is also interested in expanding economic exchanges with India by, for example, encouraging Indian engineers to move to Taiwan and by encouraging collaboration among Indian and Taiwan technology industries.¹¹ Furthermore, the Tsai Administration is promoting the development of five "strategic industries": green energy, defense, the Internet of Things, biotechnology, and smart precision machinery.¹²

Access to energy is a looming concern: observers in Taiwan told the Commission that Taiwan may face electricity brownouts by 2017 due to low energy reserves.¹³ Taiwan is highly dependent on imported energy sources to fuel its export-oriented industries. Currently, about 98 percent of the energy that Taiwan consumes is imported. Of that amount, the vast majority comprises fossil fuels from the Middle East.¹⁴ Taiwan has three active nuclear power stations, all of which are scheduled to be decommissioned between 2018 and 2025.¹⁵ The state-owned electricity provider, Taipower, financed the construction of a fourth nuclear power station, which was set to become operational by 2015. In 2014, however, Taiwan's government voted to halt construction of the plant amid protests and safety concerns following the 2011 Fukushima nuclear disaster in Japan.¹⁶

Observers in Taiwan also told the Commission that Taiwan is experiencing a "brain drain."¹⁷ A scholar explained that this problem is the result of low wages, income disparity, and high housing prices.¹⁸

Although there is no indication that developments in Hong Kong played a role in the election outcomes in Taiwan, activists in Taiwan are concerned about the fate of freedom and democracy in Hong Kong and have demonstrated support for activists there.¹⁹ More broadly, the idea of adopting Hong Kong's "one country, two systems"* framework—Beijing's stated framework for cross-Strait unification—as a model for Taiwan has long been unpopular among the Taiwan public. However, J. Michael Cole, senior non-resident

*The "one country, two systems" framework is a policy measure adopted by the People's Republic of China following the establishment of Hong Kong and Macau as Special Administrative Regions. The system grants Hong Kong and Macau the right to self-govern their economy and political system to a certain extent, excluding foreign affairs and defense.

fellow at the University of Nottingham's China Policy Institute, told the Commission that developments in Hong Kong have intensified the Taiwan public's opposition to Chinese rule and the one country, two systems framework.²⁰ (See Chapter 3, Section 3, "China and Hong Kong," for more information on developments in Hong Kong.)

President Tsai's Cross-Strait Policy

President Tsai campaigned on solving domestic economic and social problems and a pragmatic cross-Strait policy of "maintaining the status quo" in Taiwan's relations with China. She expressed her commitment to peace in the Taiwan Strait and a "consistent, predictable, and sustainable" cross-Strait relationship.²¹ During a speech in Washington, DC, in June 2015, she explained that "the conduct of cross-Strait policy must transcend the position of a political party and incorporate different views."²² She went on to say, "If elected President, I will push for the peaceful and stable development of cross-Strait relations in accordance with the will of the Taiwanese people and the existing [Taiwan] constitutional order. [The accumulated outcomes of more than 20 years of negotiations and exchanges] will serve as the firm basis of my efforts."²³ These statements appeared intended to reassure the Chinese government that she would not pursue formal independence for Taiwan.

Since her election, President Tsai has built on this policy platform and taken several additional steps to signal goodwill and flexibility and reassure Beijing about her intentions. During the campaign and in the months after the Taiwan elections, Beijing consistently and repeatedly insisted cross-Strait relations must be conducted through the framework of the "1992 Consensus"—a tacit understanding reached at a meeting between representatives of Taiwan and China in 1992 that there is only "one China" but that each side may maintain its own interpretation of the meaning of "one China."²⁴ Unlike President Ma, President Tsai has not explicitly endorsed the 1992 Consensus, but she has moved closer to China's framework in her articulation of her cross-Strait policy. Explaining the policy in an interview with Taiwan's *Liberty Times* several days after the election, President Tsai reiterated that representatives of Taiwan and China had in fact met in 1992 and that they sought to "find common ground and put aside differences."²⁵ She also said that during the meeting, the two sides "achieved several common understandings and acknowledgments" and that she "understands and respects that historical fact."²⁶ Then, during her inauguration address in May 2016, she stated that her administration would conduct cross-Strait relations in accordance with Taiwan's Act Governing Relations between the People of the Taiwan Area and the Mainland Area.²⁷ Richard C. Bush, director of the Brookings Institution's Center for East Asia Policy Studies, wrote that "the references to the two 'areas' could be taken to imply that

*The KMT and the Chinese government assert that this consensus was reached, but the DPP rejects the existence of this consensus.

†This law, which was passed in 1982 and has been amended many times, pertains to travel, employment, marriage, and other legal matters. It refers to Taiwan and mainland China as areas and thus implies they are part of the same country. Taiwan's Mainland Affairs Council, *Act Governing Relations between the People of the Taiwan Area and the Mainland Area*.

they are part of the same country and so satisfy Beijing.”²⁸ These statements do not seem to have satisfied Beijing, however.

Beijing’s Approach to President Tsai

Beijing’s approach to President Tsai has been a combination of statements of insistence on the 1992 Consensus and opposition to independence for Taiwan, warnings and other measures meant to put pressure on her administration, and some demonstrations of nuance and potential flexibility. During a press conference at the end of January 2016, in response to a question about cross-Strait relations, a spokesperson for China’s Taiwan Affairs Office (TAO)* said, “For over 20 years, the history of the development of cross-Strait relations has already thoroughly proven that by insisting on the common political framework of the ‘1992 Consensus’ and opposition to ‘Taiwan independence,’ the prospects for cross-Strait relations are bright. If this does not happen, the boat of peaceful development of cross-Strait relations will encounter terrifying waves and could even capsize completely.”²⁹ The spokesperson made a similar statement in his response to another question later in the press conference, and in several other responses to questions he gave implicit warnings about what might happen if the Tsai Administration did not accept Beijing’s cross-Strait framework.³⁰

Despite these hardline statements, Beijing later demonstrated some nuance and potential flexibility in the remarks of Minister of Foreign Affairs Wang Yi. In February, after delivering a speech in Washington, DC, Minister Wang responded to a question about the impact of the election on ties between China and Taiwan first by striking a calm tone about President Tsai’s election, saying it was “just a change of government in Taiwan. . . . It’s something natural. It should not come as too big a surprise.”³¹ Then, in the most noteworthy part of his response, he said that he hopes and expects President Tsai would “indicate that she wants to pursue the peaceful development of cross-straits relations, and that she will accept the provision in Taiwan’s own constitution that the mainland and Taiwan belong to one, the same China.”³² Minister Wang then added a veiled warning,[†] but his statement about Taiwan’s constitution—although not identical to President Tsai’s statement—echoed her pledge to conduct cross-Strait relations according to the “existing [Taiwan] constitutional order.” Mr. Cole wrote, “Although we should not read too much into the foreign minister’s comments . . . it nevertheless hints at the possibility of a more flexible, and perhaps more pragmatic, approach to Taiwan.”³³

During March meetings in China with a delegation of U.S. analysts organized by the Center for Strategic and International Studies, Chinese interlocutors articulated several areas where Beijing claimed to demonstrate goodwill and flexibility. Bonnie S. Glaser, senior advisor for Asia and director of the China Power Project at

*The Taiwan Affairs Office is an agency within China’s State Council that is responsible for overseeing China’s cross-Strait policies.

†Minister Wang said that people in Taiwan will not accept a violation of Taiwan’s constitution, because “they want to see the continued peaceful development of cross-straits relations. They want to see more mainland visitors. They want to pursue more business ties with the mainland. And they want to live in a climate of peace and tranquility. The next government in Taiwan must think about these issues in a serious way.” Wang Yi, “Statesman’s Forum: Wang Yi, Minister of Foreign Affairs, PRC” (Washington, DC, February 25, 2016).

the Center for Strategic and International Studies, writes that the interlocutors made the following points:

The Chinese believe that they have shown some flexibility and goodwill to Tsai Ing-wen and the DPP. For example, Beijing has indicated that if the DPP cannot embrace the 1992 Consensus, it “can come up with a new version” using alternative wording to express its core meaning. Another example of the Mainland’s goodwill cited by the Chinese side is the policy of not demanding more from the DPP than it has asked of the KMT. From Beijing’s perspective, it is not raising the bar and is not unilaterally changing the cross-Strait status quo. Rather, it is Tsai and the DPP that is changing the status quo. A third example that the Mainland says is a sign of its goodwill toward the DPP is Xi Jinping’s statement at the [National People’s Congress] that Beijing’s policies and principles toward Taiwan will not change because of changes in Taiwan’s political situation, including willingness to pursue peaceful development of cross-Strait relations.³⁴

In March, China re-established diplomatic relations with The Gambia, which Beijing had theretofore opted against following The Gambia’s severing of its diplomatic ties with Taiwan in 2013.³⁵ In 2008, at the beginning of the Ma Administration, Taiwan and China reached a tacit understanding—what President Ma unilaterally declared to be a “diplomatic truce”—to stop poaching each other’s diplomatic partners in order to maintain positive momentum in the cross-Strait relationship.³⁶ Although Beijing’s move to establish relations with The Gambia technically did not break the diplomatic truce—because The Gambia had already cut ties with Taiwan in what appears to have been a decision that was not influenced by Beijing*—it was almost certainly intended to convey to the Tsai Administration that Beijing is willing to draw away countries with which Taiwan has diplomatic relations.³⁷

In the context of a discussion of the Chinese government’s response to the Tsai Administration, one Taiwan official told the Commission that China had significantly reduced Chinese tourism to Taiwan.³⁸ According to Taiwan’s Mainland Affairs Council (MAC),† between May 20 and August 16, Chinese tourists traveling to Taiwan with tour groups fell by 37 percent.³⁹ In September, an estimated 10,000 Taiwan tourism industry workers and representatives marched in Taipei to call for assistance from the government in response to the drop in Chinese tour groups.⁴⁰ During the Ma Administration, Taiwan reduced barriers to Chinese tourists visiting Taiwan and the number of Chinese tourists increased from around 330,000 in 2008 to about 4.2 million in 2015.⁴¹ According to one calculation based on data from Taiwan’s Bureau of Tour-

*There is no public evidence that suggests Beijing enticed or pressured The Gambia to cut diplomatic relations with Taiwan. According to Taiwan’s Minister of Foreign Affairs, The Gambia’s decision was the result of Taiwan’s rejection of a request by The Gambia’s president for more aid. Angela Tsai and Scully Hsiao, “Gambian Aid Request Linked to Broken Ties with Taiwan: Minister,” Central News Agency (Taiwan), November 25, 2013.

†The Mainland Affairs Council is a cabinet-level agency in Taiwan’s executive branch that is responsible for overseeing Taiwan’s cross-Strait policies.

ism, the revenue from Chinese tourists in Taiwan reached \$6.8 billion in 2015.⁴²

Beijing's insistence on the "one China" principle precludes any country or international organization from simultaneously diplomatically recognizing China and Taiwan, thereby restricting Taiwan's full participation in the international community. Due to Beijing's insistence on this principle, Taiwan generally can only participate in international fora using other names, such as "Chinese Taipei." In May, Beijing apparently agreed to Taiwan's continued participation as an observer in the annual conference of the UN World Health Organization's World Health Assembly. The World Health Organization has extended an invitation to Taiwan to participate as an observer every year since 2009. This year's conference was held several days after President Tsai's inauguration, and a Taiwan official announced that Taiwan had received the invitation on May 6.⁴³

Beijing has tried to put the onus on the Tsai Administration to maintain positive cross-Strait relations and positioned itself to deflect all responsibility should relations sour. During a press conference on May 11, a TAO spokesperson said:

*Who is working hard to protect the common political foundation and protect the peaceful development of cross-Strait relations and who is destroying the common political foundation of cross-Strait relations and changing the status quo of cross-Strait relations, who is protecting roads and who is tearing down bridges, I believe everyone can see very clearly. . . . If there is gridlock in cross-Strait relations or a crisis occurs, the responsibility is on those who change the status quo.*⁴⁴

Beijing continued to pressure the Tsai Administration in its response to President Tsai's inauguration speech on May 20. TAO director Zhang Zhijun delivered a statement in which he said, "The contact and communication mechanism between the Mainland's Taiwan Affairs Office and Taiwan's Mainland Affairs Council and the consultation and negotiation mechanism between the Association for Relations Across the Taiwan Straits and Taiwan's Straits Exchange Foundation* are built on the political foundation of the 1992 Consensus. Only by affirming the political foundation that embodies the One China principle can the institutionalized cross-Strait exchanges continue."⁴⁵

Since President Tsai's inauguration, Beijing has followed through on its warning, at least in part, and suspended "the cross-Strait contact and communication mechanisms."⁴⁶ In June 2016, a TAO spokesperson announced that "the cross-Strait contact and communication mechanisms have been suspended because Taiwan did not recognize the 1992 Consensus, the political basis for the One China principle."⁴⁷ The spokesperson noted the mechanism had been suspended since President Tsai's inauguration.⁴⁸ Earlier that month, the deputy minister of MAC said that communication between the

*The Straits Exchange Foundation and the Association for Relations Across the Taiwan Strait facilitate cross-Strait negotiations in the absence of formal ties between the governments of Taiwan and China. Although the two bodies are semiofficial organizations, they receive direction from their respective governments.

two governments was ongoing at the division director level.⁴⁹ Also in June, a Taiwan official told the Commission that Beijing suspended formal exchanges between MAC and TAO, but informal communications through “desk phones and fax machines” still occur.⁵⁰ Beijing also has suspended communication and meetings between the Straits Exchange Foundation and the Association for Relations Across the Taiwan Straits.⁵¹ According to an article published on May 31, an anonymous individual affiliated with China’s Association for Relations Across the Taiwan Straits told Taiwan’s *United Daily News* that the association had not responded to any faxes or telephone calls from the Taiwan side since the inauguration.⁵² In July, during an interview with the *Washington Post*, President Tsai was asked, “Since your inauguration in late May, the Chinese have cut off the official channel that was used to communicate between Taiwan and the mainland. How do you plan to handle day-to-day relations with Beijing?” President Tsai responded, “We have always had diverse channels of communication across the strait. These include not just official communications but also people-to-people contacts.” Then, when asked, “Are you, the president, in touch with your counterparts in the Chinese government?” she said, “Different levels of the government have different ways of communicating with their counterparts in China. At this stage, I cannot go into too much detail.”⁵³

Cross-Strait Agreements

In August, the TAO director told Taiwan business representatives in China that Beijing would continue to honor the 23 existing cross-strait agreements signed under the Ma Administration.⁵⁴ However, since China has made official and quasi-official cross-strait exchanges contingent on Taiwan’s acknowledgement of the 1992 Consensus and thus far has expressed dissatisfaction with President Tsai’s attempts to reach a compromise on this issue, the potential for additional cross-strait agreements is uncertain. Regarding potential new agreements, the TAO director said, “It is impossible for the doors to be open without the ‘1992 consensus’ as a foundation.”⁵⁵ The Ma Administration had engaged in negotiations with Chinese counterparts on a trade in goods agreement and an agreement on reciprocal representative offices in each other’s territory, but the two sides had not yet concluded the talks on either of these potential agreements.

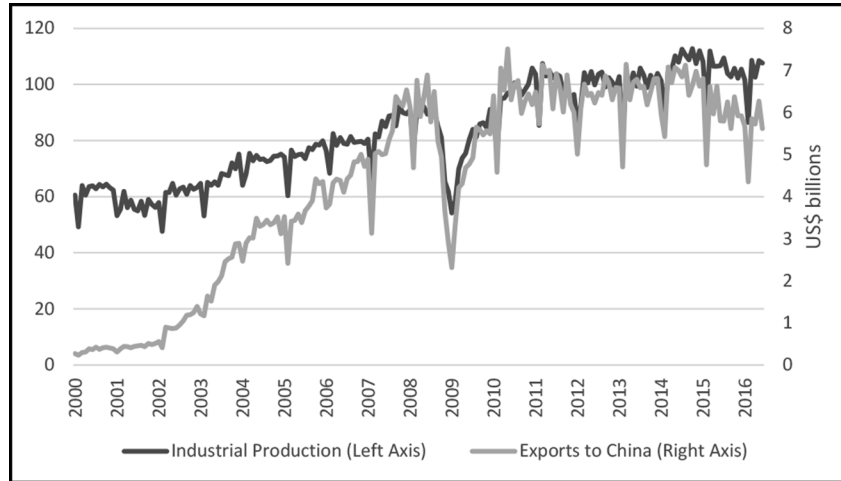
The fate of the Cross-Strait Trade in Services Agreement (CSSTA), which Taiwan and China signed in 2013 but the Taiwan legislature has not ratified, is also uncertain. The Tsai Administration plans to wait until the legislature passes a cross-strait agreements oversight bill before it addresses the future of the CSSTA and continues negotiations on the trade in goods agreement.⁵⁶ The CSSTA has been stalled in the legislature since March 2014, when protestors occupied the legislative chamber in opposition to the agreement—a protest movement that was given the name the Sunflower Movement. Protestors were concerned that the Ma Administration conducted the negotiations in a nontransparent manner and the Legislative Yuan had not reviewed the agreement. To end the occupation, one of the terms to which the then legislative speaker agreed was the creation of an oversight mechanism for cross-strait

agreements.⁵⁷ Since then, many draft bills for such a mechanism have been proposed, but they were not debated.⁵⁸ Much of the political logjam was the result of disagreement over the roles of the Legislative Yuan and the Executive Yuan (Taiwan's executive branch) in the oversight process.⁵⁹ Ker Chien-Ming, head of the Legislative Yuan's DPP caucus, said in August 2016 that the Legislative Yuan would review the bill during the fall legislative session.⁶⁰ How the bill will fare is uncertain. Although the DPP has a majority in the Legislative Yuan, the version of the bill proposed by the DPP caucus has been criticized by civil society groups.⁶¹ In addition, Mr. Ker in January 2016 said that the DPP's stance on the CSSTA was that the agreement should be renegotiated.⁶² Although it is unknown whether the Tsai Administration will call for the agreement to be renegotiated, if it chooses to do so, the question remains whether Beijing will agree.

Cross-Strait Trade and Investment

In 2015, Taiwan's economic growth slowed to less than 1 percent as exports dropped significantly amid China's economic slowdown and low global demand.⁶³ Taiwan's exports also were hurt by increased competition from Chinese high-tech suppliers, which undercut them on cost.⁶⁴ With China ranking as its largest trading partner, Taiwan's export-oriented economy is dependent on China and vulnerable to fluctuations in China's economy.⁶⁵ Taiwan's industrial production* has grown increasingly tied to its China-bound exports. In the years after Taiwan joined the World Trade Organization, Taiwan's exports to China grew rapidly as Taiwan-based firms expanded manufacturing operations in China and established regional supply chains, especially in information technology products. By the time the Ma Administration took office in 2008, fluctuations in Taiwan's industrial production closely tracked exports to China (see Figure 1).⁶⁶

*Industrial production is quantified using the industrial production index, which measures outputs of the industrial sector of the economy, including manufacturing, mining, and utilities.

Figure 1: Taiwan's Industrial Production, 2000–2016

Note: 2016 data are through June. The export data in this figure include re-exports.

Source: Taiwan Ministry of Economic Affairs and Ministry of Finance via CEIC database.

Scholars at the Chung-Hua Institute for Economic Research told the Commission that although Taiwan's economy showed negative gross domestic product (GDP) growth in the first two quarters of 2016, Taiwan's manufacturing will pick up in the final two quarters to make up for these losses. Taiwan's GDP growth tends to fluctuate based on the release schedules of certain products that Taiwan companies help to produce. For example, Taiwan had exceptionally good GDP growth in 2014, mainly attributable to high sales of the iPhone 6 rather than any sustained improvement in Taiwan's economic situation.⁶⁷

To address Taiwan's economic dependence on China, the Ma Administration strived to diversify Taiwan's export markets, efforts that President Tsai has continued. President Tsai and the DPP have emphasized their objective of moving Taiwan toward participation in the U.S.-led Trans-Pacific Partnership (TPP) trade agreement, and President Tsai is moving forward with plans to enhance Taiwan's trade and investment with the countries of Southeast Asia, South Asia, and Oceania, part of her "New Southbound Policy," which is discussed later in this section.⁶⁸

Goods Trade

As of August 2016, China remains Taiwan's largest trading partner, biggest export market, and top source of imports.*⁶⁹ In 2015, annual cross-Strait trade totaled \$111.4 billion,† comprising 22.6 percent of Taiwan's total trade.⁷⁰ However, total cross-Strait trade also decreased by about 11 percent in 2015 compared to 2014.⁷¹

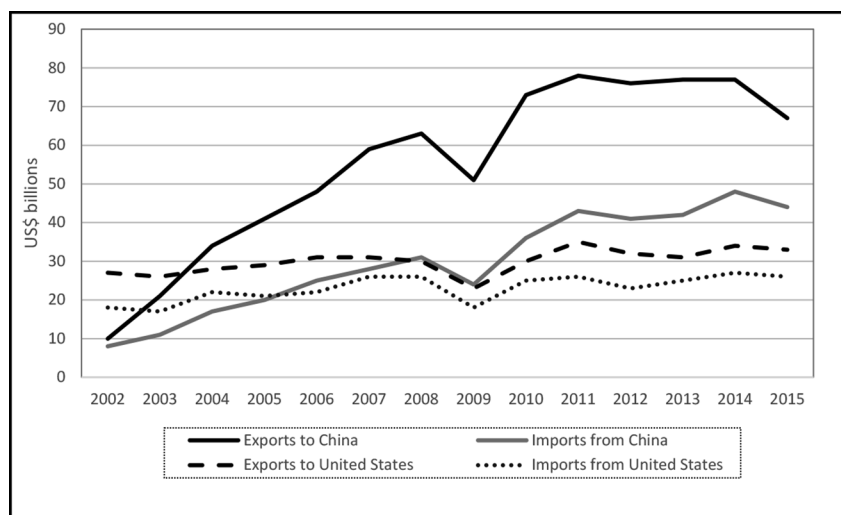
Taiwan's exports to China have been hit hard by the slowdown of China's economy.⁷² Taiwan's exports to China in 2015 were

*Trade statistics in this section do not include Taiwan's trade with Hong Kong.

†All trade statistics from Taiwan's Bureau of Foreign Trade in this section exclude re-exports and re-imports.

\$67.2 billion, comprising 25.4 percent of Taiwan's exports to the world.⁷³ Year-on-year, Taiwan's exports to China shrank by 13.2 percent and its trade surplus with China decreased by 21.5 percent in 2015 (see Figure 2).⁷⁴ Taiwan's exports to China were dominated by semiconductor-related and liquid crystal display-related products in 2015.⁷⁵ These products composed all of Taiwan's top five exports to China and more than a quarter of the value of Taiwan's total exports to China (see Figure 3).⁷⁶ Taiwan's exports of these top five products to China decreased by 17.8 percent in 2015.⁷⁷

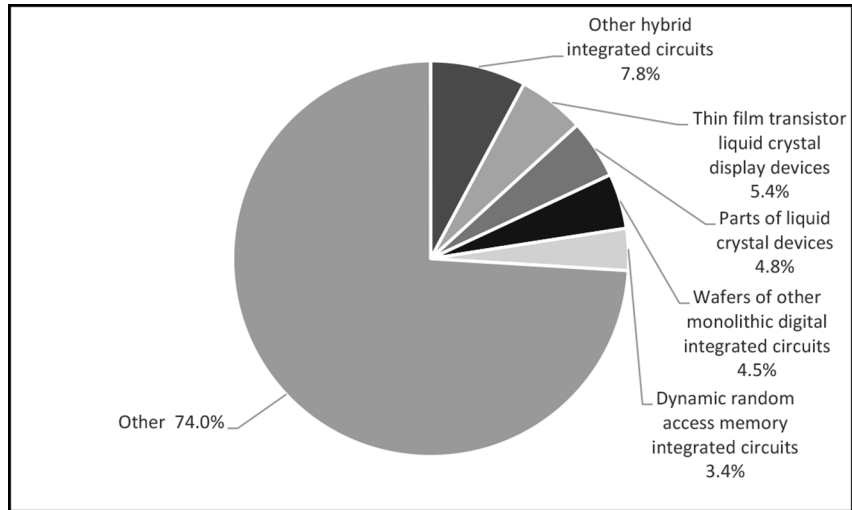
Figure 2: Taiwan's Trade with China and the United States, 2002–2015



Source: Taiwan's Bureau of Foreign Trade, "Trade Statistics." <http://cus93.trade.gov.tw/ENGLISH/FSCE/>.

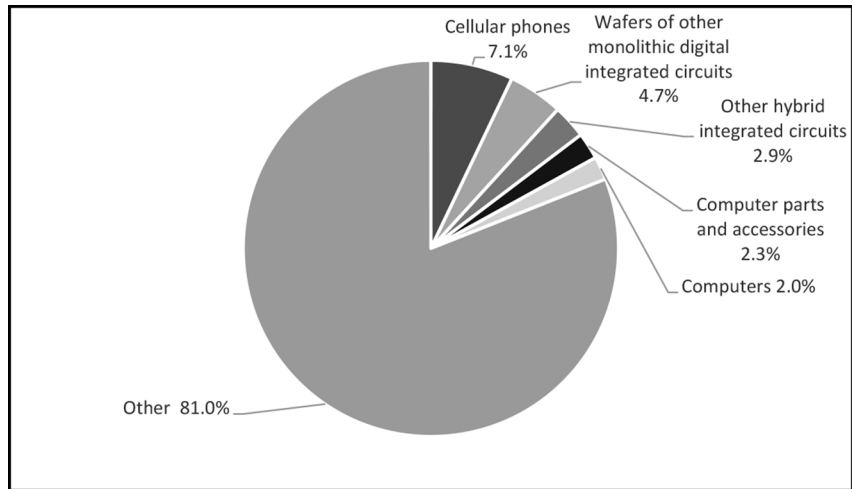
Taiwan's imports from China in 2015 were \$44.2 billion, comprising 19.4 percent of its total imports.⁷⁸ Despite imports from China decreasing by 8 percent, China remained Taiwan's largest source of imports.⁷⁹ Just as semiconductor-related products were among Taiwan's top exports to China, they also were among Taiwan's main imports from China.⁸⁰ (Taiwan firms generally design and manufacture unfinished microchips and other semiconductor-related products in Taiwan for assembly and testing in China; China then typically exports the finished products back to Taiwan.)⁸¹ Taiwan's other major imports from China included cellular phones and computers and computer parts and accessories.⁸² Despite the overall decrease in imports, imports of cellular phones increased by 37.6 percent and imports of wafers for microchips increased by 10.2 percent.⁸³ Both cellular phones and wafers for microchips were among Taiwan's top five imports from China (see Figure 4).⁸⁴ Imports of the other top five products all decreased, with microchips decreasing by 14.3 percent, computer parts and accessories decreasing by 7.1 percent, and computers decreasing by 15.8 percent.⁸⁵

Figure 3: Taiwan's Top Five Exports to China, 2015



Source: Taiwan's Bureau of Foreign Trade, "Trade Statistics." <http://cus93.trade.gov.tw/ENGLISH/FSCE/>.

Figure 4: Taiwan's Top Five Imports from China, 2015



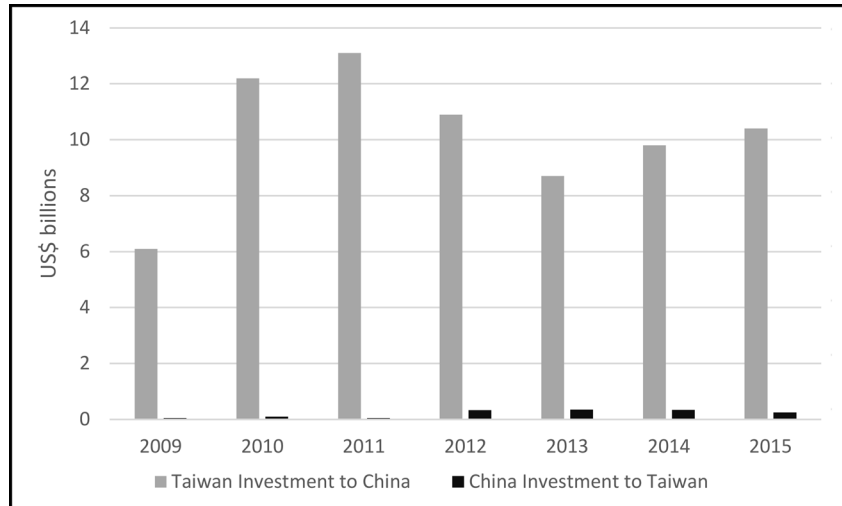
Source: Taiwan's Bureau of Foreign Trade, "Trade Statistics." <http://cus93.trade.gov.tw/ENGLISH/FSCE/>.

Foreign Direct Investment

China is Taiwan's top destination for foreign direct investment (FDI).⁸⁶ According to official Taiwan data, Taiwan FDI to China in 2015 totaled \$10.4 billion.⁸⁷ Between 2014 and 2015, this number increased by 5.8 percent.⁸⁸ In 2015, for the second year in a row, Taiwan FDI to China recorded growth after decreasing in 2012 and 2013 (see Figure 5).⁸⁹ The growth in FDI over the past two years was primarily the result of new Taiwan FDI in the electronic parts manufacturing and computer manufacturing sectors in 2014, followed by an increase in Taiwan FDI in the financial and insurance sectors and the non-metal mineral products manufacturing industry in 2015.⁹⁰ In 2015, investment in the financial and insurance sectors comprised the largest percentage of Taiwan's total FDI in China, with 25.4 percent.⁹¹ The next largest recipients of Taiwan FDI in China in 2015 were electronic parts and components manufacturing (11.2 percent) and computers, electronic, and optical products manufacturing (10.1 percent).⁹²

Year-on-year, the value of Chinese investment in Taiwan dropped by about 27 percent to approximately \$244 million in 2015, but the number of Chinese investment cases approved by the Taiwan government increased by 25 percent to 170.⁹³ According to Taiwan's National Development Council, a policy planning organization under the Executive Yuan, the number of cases increased while the value decreased, primarily because the majority of Chinese investment in Taiwan is in services, and investments in services are generally smaller than those in manufacturing. The council reported that the percentage of Chinese investments in services increased by 9.7 percent to a total of 79.4 percent of all Chinese investment in Taiwan in 2015.⁹⁴ FDI from China had been steady between 2012 and 2014 after it more than tripled between 2010 and 2012,⁹⁵ a spike largely due to the Ma Administration's loosening of investment caps and regulations on Chinese investment into Taiwan.* Chinese investments are still limited. All investments require Taiwan government approval, and the Taiwan government prohibits Chinese investors from appointing managers or having controlling stakes.⁹⁶ In 2015, 62.4 percent of the value of Chinese FDI to Taiwan was in wholesale and retail, 10.4 percent was in electronic parts and electronic components manufacturing, and 7.3 percent was in information and software services.⁹⁷

* For example, in March 2012, Taiwan loosened Chinese investment caps of 10 percent stakes in local firms and 50 percent in joint ventures in Taiwan's semiconductor and metal tool manufacturing sectors, among others. PricewaterhouseCoopers, "Chapter 4: The Bigger Picture—China's Impact on the Semiconductor Industry 2012 Update," September 2012.

Figure 5: Cross-Strait Investment, 2009–2015

Source: Taiwan's Ministry of Economic Affairs, Investment Commission, *Monthly Report*, December 2015.

Taiwan's International Engagement

Taiwan continues to pursue greater participation in the international community through its official diplomatic relations with 22 countries,* efforts to expand its participation in international organizations, and initiatives to strengthen economic and unofficial diplomatic partnerships with countries other than China. As discussed previously, one of Taiwan's successes in 2016 was its continued participation in the World Health Assembly as an observer. This year also saw new and ongoing challenges to Taiwan's ability to participate in the international community, however. It is unclear whether all of these developments were part of a concerted effort by Beijing to pressure the Tsai Administration, but should Beijing seek to increase pressure on Taipei, it may move to further limit Taiwan's participation in international organizations and invite some countries with which Taiwan has diplomatic relations to cut ties and establish diplomatic relations with China.

Efforts to Expand International Participation

Taiwan's "New Southbound Policy": One of the Tsai Administration's main initiatives to expand Taiwan's international participation is its "New Southbound Policy" of enhanced engagement with the countries of Southeast Asia, South Asia, and Oceania.⁹⁸ Although a major objective of the initiative is to expand Taiwan's trade and investment with these countries in order to diversify its export markets, President Tsai and James Huang, the official who

* Taiwan has diplomatic relations with Belize, Burkina Faso, the Dominican Republic, El Salvador, Guatemala, Haiti, the Holy See, Honduras, Kiribati, the Marshall Islands, Nauru, Nicaragua, Palau, Panama, Paraguay, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Sao Tome and Principe, Solomon Islands, Swaziland, and Tuvalu. Taiwan's Ministry of Foreign Affairs, "Diplomatic Allies."

is leading the initiative, have said that it will be focused on much more than trade and investment.⁹⁹ According to its guidelines, the initiative will include cooperation in the areas of agriculture, education, culture, and tourism.¹⁰⁰

Seeking participation in INTERPOL: According to Taiwan's Criminal Investigation Bureau, Taiwan's exclusion from the International Criminal Police Organization (INTERPOL) means that it does not receive updates from the organization on transnational crimes, and Taiwan police cannot participate in training provided by INTERPOL.¹⁰¹ In March, U.S. President Barack Obama signed a bill (S. 2426) that mandates the secretary of State to report to Congress within 90 days on the U.S. government's strategy for supporting Taiwan's participation in INTERPOL as an observer. This bill is another step in the U.S. government's longstanding efforts to advocate on behalf of Taiwan's participation in international organizations. President Obama signed a similar bill (H.R. 1151) in 2013 regarding a U.S. strategy to support Taiwan's participation as an observer in the UN's International Civil Aviation Organization (ICAO).*

Challenges

Not invited to participate in the 2016 ICAO Council Assembly: In September, Taiwan's Minister of Foreign Affairs confirmed that ICAO did not invite Taiwan to participate in the ICAO Council Assembly, which was held in late September and early October, in a reversal from the previous assembly. A spokesperson for China's TAO said Taiwan could not participate because the Tsai Administration had not endorsed the 1992 Consensus.¹⁰² The president of the ICAO Council invited Taiwan to participate as his guest in the 2013 ICAO Council Assembly, a forum which is held every three years. The 2013 assembly was the first official ICAO meeting to which Taiwan had been invited in 42 years.¹⁰³

Blocked from other UN meetings and OECD meeting: In April, under pressure from China, the Belgian government barred a Taiwan government delegation from attending a meeting on the steel sector organized by the Belgian government and the Organisation for Economic Co-Operation and Development (OECD) in Brussels. The delegation had already attended a meeting that was part of the same symposium earlier in the day. Although Taiwan is not a member of the OECD, it has been allowed to attend some OECD meetings since 2002.¹⁰⁴ In June, a professor of labor relations from Taiwan's Chung Cheng University and a study group she was leading were blocked twice from attending an annual conference of the UN's International Labor Organization. The professor had led study groups to attend the conference in 2014 and 2015 without a problem.¹⁰⁵ In July, Taiwan officials were not allowed to participate in a meeting of the Food and Agriculture Organization of the UN's Committee on Fisheries, an organization in which they have been permitted to participate since 2003.¹⁰⁶

*The U.S. Department of State submitted both reports to Congress. Executive Communication EC5932, 114th Cong., 2nd Sess., June 28, 2016.

Difficulty joining the Asian Infrastructure Investment Bank: In early April, the president of the Asian Infrastructure Investment Bank announced that if Taiwan wanted to join the bank China's Ministry of Finance would have to apply on its behalf. This is the same standard the bank applied to Hong Kong, thereby treating Taiwan as if it were part of China. The Taiwan government rejected this condition, stating, "It hurts our dignity."¹⁰⁷

Failed repatriation of fraud suspects: Between April and September, about 200 Taiwan citizens living in Armenia, Cambodia, Kenya, and Malaysia who were accused of committing telecommunications fraud against people in China were deported from those countries to China, rather than to Taiwan.¹⁰⁸ At the beginning of the Ma Administration, Taipei and Beijing signed the Cross-Strait Joint Crime-Fighting and Judicial Mutual Assistance Agreement, which includes the return of individuals suspected of and convicted of crimes from one side to the other.¹⁰⁹ In 2011, after the Philippines deported 14 Taiwan citizens suspected of telecommunications fraud to China, cross-Strait negotiations led Beijing to return the suspects to Taiwan.¹¹⁰ Subsequently, Taipei and Beijing developed a pattern of law enforcement cooperation in countries with which Taiwan does not have official diplomatic relations, though this cooperation was not part of the 2009 agreement.¹¹¹ This cooperation enabled Taiwan to bring many Taiwan citizens who were suspected of committing crimes in those countries back to Taiwan.¹¹² Beijing has been unwilling to continue this cooperation since President Tsai was elected. However, Beijing's initial motivation for not allowing the suspects to be sent to Taiwan may solely have been its desire to crack down on telecommunication fraud against Chinese citizens. The first group of Taiwan citizens who were deported from Kenya in April 2016 had been arrested in December 2014 and Beijing requested that they be sent to China in January 2015, one year before President Tsai was elected.¹¹³ Nonetheless, Beijing is now likely also using these cases as another means to pressure Taipei.*¹¹⁴

Threat of severed diplomatic relations: No countries have severed diplomatic ties with Taiwan since President Tsai's election, and there is no evidence to suggest China has invited them to do so. Zhang Zhixin, a research fellow at the Shanghai Institute for International Studies, estimated in 2013 that Beijing had rejected overtures from at least five countries with diplomatic relations with Taiwan since then President Ma was elected in 2008.¹¹⁵ However, Beijing could establish ties with some of these countries if cross-Strait relations significantly worsen.¹¹⁶ In 2016, Beijing and the

*During a press conference in August a reporter requested a TAO spokesperson confirm whether MAC had protested to Beijing through cross-Strait communication channels regarding Kenya's deportation of Taiwan citizens to China. In his response, the spokesperson reiterated that the mechanisms for cross-Strait communication and talks had been suspended because Taipei had not endorsed the 1992 Consensus. He added that "the Taiwan side should face up to this fact and make practical efforts to resume the working of these mechanisms." Xinhua, "Taiwan Affairs Office: The People on Both Sides of the Strait Support Cracking Down on Telecommunications Fraud According to Law. The Taiwan Side Should Make Practical Efforts to Resume the Working of the Cross-Strait Contact and Communication Mechanisms," *China's Taiwan Affairs Office*, August 8, 2016.

Vatican—which has diplomatic relations with Taiwan*—were reportedly in talks to address longstanding areas of disagreement. The two sides have disagreed about whether the Vatican should be allowed to appoint bishops in China as it does elsewhere. The Vatican also does not approve of eight bishops that were appointed by the Chinese government.¹¹⁷ A resolution of these issues and warming of relations between China and the Holy See could put Taiwan's relations with the Vatican at risk.

Difficulty signing free trade agreements: Taiwan is at a disadvantage when competing economically with other countries such as South Korea, because it is more difficult for Taiwan to sign free trade agreements¹¹⁸—in large part because Beijing pressures other countries not to sign free trade agreements with Taiwan.¹¹⁹

The Tsai Administration's Approach to the East and South China Sea Disputes

Taiwan, which is one of six claimants of land features in the South China Sea,† rejected the ruling of the arbitral tribunal at the Permanent Court of Arbitration in The Hague in the case *The Republic of Philippines v. The People's Republic of China* in July,‡ though Taipei's response has not been nearly as vociferous as Beijing's. Taiwan stated several reasons for rejecting the ruling: (1) it deemed the tribunal's designation for Taiwan ("Taiwan Authority of China") incorrect and "demeaning to the status of [Taiwan] as a sovereign state;" (2) the tribunal did not formally invite Taiwan to participate in the case or ask for Taiwan's views;¹²⁰ and (3) although Taiwan-controlled Itu Aba (a land feature in the Spratly Islands called Taiping Island by Taiwan and China) was not originally included in the Philippines' submission, the tribunal ruled that it is a rock rather than an island (see Figure 6).§ Itu Aba is the largest natural land feature in the Spratly Islands and the only one that Taiwan controls; some observers thought it had a strong chance of being designated an island, instead of a rock, by the tribunal.¹²¹ Taiwan's Ministry of Foreign Affairs also stated, "That [Taiwan] is entitled to all rights over the South China Sea Islands and their relevant waters in accordance with international law and the law of the sea is beyond dispute."¹²² The day after the tribu-

*The Vatican established ties with the Republic of China government in 1942 and maintained those ties after the government moved to Taiwan and Beijing expelled the Vatican's ambassador from China in 1951. Kevin Hsu, "China and the Vatican: Toward a New Era?" *Diplomat* (Japan), September 22, 2016.

†The other claimants are Brunei, China, Malaysia, the Philippines, and Vietnam. See Chapter 2, Section 1, "Year in Review: Security and Foreign Affairs" for more information on the East and South China seas disputes.

‡For more information on the tribunal's ruling, see Caitlin Campbell and Nargiza Salidjanova, "South China Sea Arbitration Ruling: What Happened and What's Next?" *U.S.-China Economic and Security Review Commission*, June 12, 2016.

§The distinction, as defined by the UN Convention on the Law of the Sea, between an island and a rock is important because each type of feature generates a different maritime entitlement. Islands, which must be above water at high tide and be capable of sustaining human habitation or economic activity of their own, can generate exclusive economic zones out to 200 nautical miles. (An exclusive economic zone is a 200-nautical-mile zone extending from a country's coastline within which that country can exercise exclusive sovereign rights to explore for and exploit natural resources, but not full sovereignty.) Rocks, which are defined as being above water at high tide but unable to sustain human habitation or economic activity, only generate a 12-nautical mile territorial sea. UN Convention on the Law of the Sea, "Article 121: Regime of Islands;" UN Convention on the Law of the Sea, "Part 2: Territorial Sea and Contiguous Zone;" and UN Convention on the Law of the Sea, "Part 5: Exclusive Economic Zone."

nal's ruling, President Tsai addressed officers and enlisted personnel on a Taiwan Navy frigate. In President Tsai's remarks she said the ruling "has seriously harmed the rights and interests of our country with respect to the South China Sea islands."¹²³ The ship was originally scheduled to leave the next day for a routine patrol of the South China Sea, but, as part of Taiwan's response to the tribunal's ruling, it set sail the same day.¹²⁴ Taiwan is not a signatory to the UN Convention on the Law of the Sea (UNCLOS), because it lost its seat at the UN before the convention was established. Thus, Taiwan is not bound by the tribunal's decision.

Figure 6: Map of South China Sea



Source: Figure adapted from *Economist*, "Hai-handed," January 13, 2014.

Prior to the ruling, Taiwan had taken some positive steps to clarify its claims in the South China Sea in accordance with UNCLOS and initiated efforts to reduce tensions and establish coordination and cooperation mechanisms with other claimants.¹²⁵ Taiwan has an opportunity to further clarify its position now that the tribunal has clarified the legal status of the features in disputed waters.

Taiwan and the 11-Dash Line

The nine-dash line on Chinese maps of the South China Sea is based on a map with a line containing 11 dashes that was published in 1947 by the government of the Republic of China, which later moved to Taiwan at the end of the Chinese civil war.¹²⁶ There are various explanations of the original meaning of the line. Although the line clearly encompasses the land features that the Taiwan government claims, it is unclear whether it also indicates a claim of sovereignty or jurisdiction over the waters within the line.¹²⁷

One interpretation is offered by Dustin Kuan-Hsiung Wang, a professor in the Graduate Institute of Political Science at National Taiwan Normal University. Dr. Wang discussed the original purpose of the 11-dash or U-shaped line in e-mail correspondence with Commission staff. Dr. Wang wrote: “The meanings of the U-shaped line were probably twofold: one was to demarcate an area of the South China Sea within which the Republic of China claimed all islands. Under this, the claim was not intended to encompass all the water within the lines, but rather, all the land sovereignty within the lines. The other was to express the perception of undecided maritime boundaries between the Republic of China and her neighbors. However, further negotiations were needed between them, therefore the U-shaped line was expressed in (eleven) dashes.”¹²⁸

In 1993, the Taiwan government adopted the Policy Guidelines for the South China Sea, which declared that “the South China Sea area within the historic waters limit is the maritime area under the jurisdiction of the Republic of China, where the Republic of China possesses all rights and interests.”¹²⁹ The Taiwan government continues to claim the land features in the South China Sea, but its position regarding the waters appears to have changed over time. During the last 20 years, Taipei has gradually stopped using the term “historic waters.”¹³⁰ In September 2014, then President Ma said, “The principle that ‘sovereignty over land determines ownership of the surrounding waters,’ which is set out in [UNCLOS], applies to disputes concerning sovereignty over both land and sea.”¹³¹ President Ma’s clarification of Taiwan’s position that maritime entitlements should be derived from sovereignty over land in accordance with UNCLOS contrasts with China’s vague and expansive sovereignty claims to nearly all of the land and sea within its nine-dash line, which encompasses around 90 percent of the South China Sea (the South China Sea encompasses more than 1.4 million square miles of water). The Tsai Administration appears to be continuing this trend away from Taiwan’s earlier, more expansive claims, choosing not to mention the dashed line in its response to the arbitral tribunal’s ruling.¹³²

The Tsai Administration's policy toward the disputes in the East and South China seas* has been similar so far to that of the Ma Administration, which proposed diplomatic frameworks and signed agreements with other claimants to encourage the setting aside of territorial disputes and promotion of joint resource development. The most recent agreement was reached between Taiwan and the Philippines in November 2015, with the two sides achieving consensus on "avoiding the use of violence or unnecessary force, establishment of an emergency notification system, and establishment of a prompt release mechanism" for fishermen from one country who are detained by the other.¹³³ In March 2016, Taiwan and the Philippines agreed to establish a hotline to notify each other of fishing accidents, to conduct joint inspections of fishing boats, and to exchange inspection reports.¹³⁴ Keeping with the spirit of these previous endeavors, in her inaugural address President Tsai said, "Regarding problems arising in the East China Sea and South China Sea, we propose setting aside disputes so as to enable joint development."¹³⁵ Later, in June, the Tsai Administration announced that it was establishing a maritime affairs cooperation dialogue with the Japanese government to address the dispute between Taiwan fishermen and the Japanese government over rights to fish at Okinotori Atoll, a land feature in the East China Sea that Japan asserts is entitled to a 200 nautical mile exclusive economic zone and that Taiwan and China believe does not have this right, among other issues.¹³⁶

Taiwan Military and Security Issues

Cross-Strait Military Balance

As the Tsai Administration took office, it faced the challenges of a Chinese military modernization program that had dramatically increased despite eight years of enhanced cross-Strait economic, people-to-people, and government ties. Broadly, the cross-Strait military balance has shifted toward China.¹³⁷ The People's Liberation Army (PLA) possesses both a quantitative and a qualitative military advantage over the Taiwan military and is capable of conducting a range of military campaigns against Taiwan.

- The PLA Rocket Force (previously the Second Artillery Force) has approximately 1,200 short-range ballistic missiles and 200–500 ground-launched land-attack cruise missiles.†¹³⁸ According to congressional testimony by U.S. Defense Intelligence Agency Director Lieutenant General Vincent R. Stewart in February 2015, all of China's short-range ballistic missiles are deployed across from Taiwan.¹³⁹ The primary purpose of the majority of these missiles is to deter a move toward formal independence by Taiwan or to destroy Taiwan's ports and air-

*Taiwan is one of three claimants to the Senkaku Islands (known as the Diaoyutai in Taiwan and Diaoyu in China) in the East China Sea. The other claimants are China and Japan.

†Official U.S. and Taiwan estimates of China's number of short-range ballistic missiles and land-attack cruise missiles vary. According to the Taiwan Ministry of National Defense's August 2015 report on China's military power for the Legislative Yuan, China has 1,700 ballistic and cruise missiles, and 1,500 of these missiles are deployed against Taiwan. Senate Armed Services Committee, *Hearing on Worldwide Threats*, written testimony of Vincent R. Stewart, February 26, 2015; Zhu Ming, "Ministry of National Defense: China Keeps 1,500 Missiles Deployed against Taiwan," *Storm Media* (Taiwan), August 31, 2015. Staff translation.

fields should Beijing choose to do so. Although it has not greatly expanded in size since the late 2000s, China's short-range ballistic missile arsenal has become more lethal with the introduction of new missile variants with longer ranges and improved accuracies and warheads.¹⁴⁰

- The PLA Air Force and Navy have about 2,100 combat aircraft, of which approximately 600 are modern.*¹⁴¹ Fewer than 330 of Taiwan's combat aircraft are modern. As part of its efforts to further enhance the capabilities of its fleet of combat aircraft, China signed a contract with Russia to purchase 24 Su-35 fighter aircraft in November 2015.¹⁴² China is also developing the J-20 fifth-generation fighter aircraft and has already tested its fifth and sixth prototypes of the aircraft.¹⁴³
- The PLA Navy has more than 300 surface combatants, submarines, and missile-armed patrol craft, in addition to China's highly capable coast guard and maritime militia.¹⁴⁴ Taiwan, on the other hand, has 90 naval combatants, comprising four submarines† and 86 surface ships.‡¹⁴⁵ As China's naval modernization continues, an increasing percentage of these ships will be modern§ and feature advanced weaponry. For example, the PLA Navy recently has acquired a land-attack capability, as the new LUYANG III-class guided missile destroyer is capable of launching land-attack cruise missiles.¹⁴⁶ In addition, China continues to enhance its amphibious capabilities.¹⁴⁷ Most recently, in January 2016, the PLA Navy launched a new tank landing ship and in March 2016 it commissioned three others.¹⁴⁸ (See Chapter 2, Section 1, "Year in Review: Security and Foreign Affairs," for more information on developments in Chinese military modernization.)

In its preparation for a Taiwan contingency, the PLA conducts a variety of exercises, including antisurface warfare and amphibious exercises, and it has increased the complexity and realism of these exercises.¹⁴⁹ For example, the PLA conducted an amphibious landing exercise in an undisclosed location off of southeastern China in May 2016. The forces involved in the exercise belonged to the 31st Group Army from the Eastern Theater Command, the theater command that is responsible for contingencies involving Taiwan and

* "Modern" combat aircraft are defined as possessing advanced avionics and weapons systems. These aircraft include the J-10, J-11, JH-7, Su-27, and Su-30. For more information on the Commission's definition of "modern" combat aircraft, see U.S.-China Economic and Security Review Commission, *2014 Annual Report to Congress*, November 2014, 309.

† Two of these submarines are only used for training.

‡ Taiwan's coast guard is in the midst of a ten-year shipbuilding program that will bring its forces to 173 ships. Taiwan does not have a maritime militia. Mrityunjay Mazumdar, "Taiwanese Coast Guard Launches OPV amid Ongoing Force Development Programme," *Jane's Defence Weekly*, May 28, 2015.

§ In reference to China's submarine force, the term "modern" is used in this Report to describe a submarine capable of employing antiship cruise missiles or submarine-launched intercontinental ballistic missiles. These include the JIN nuclear ballistic missile submarine, SHANG nuclear attack submarine (SSN), SONG diesel attack submarine (SS), KILO 636 SS, and YUAN diesel air-independent power attack submarine. In reference to China's surface force, the term "modern" is used to describe a surface ship that possesses a multi-mission warfare capability, is armed with more than a short-range air defense capability, and has the ability to embark a helicopter. These include the following: LUHU destroyer (DD), LUHAI DD, LUZHOU guided missile destroyer (DDG), LUYANG I/II/III DDG, SOVREMENNYY I/II DDG, JIANGWEI I/II frigate (FF), JIANGKAI I FF, and JIANGKAI II guided missile frigate. For more information on the Commission's definition of "modern" submarines and surface ships, see U.S.-China Economic and Security Review Commission, *2014 Annual Report to Congress*, November 2014, 300.

Japan. The exercise included amphibious armored assault vehicles, helicopters, and special operations forces attacking a hypothetical enemy beach.¹⁵⁰

China's large defense expenditures are a major challenge for Taiwan. China's defense budget grew by double digits almost every year between 2005 and 2015,* increasing the official defense spending gap to more than \$130 billion. In contrast, Taiwan's defense budget has grown modestly.¹⁵¹ The defense budget submitted by Taiwan's Executive Yuan for 2016 of 321.7 billion New Taiwan Dollars or \$9.8 billion (about 2 percent of GDP) represented an increase of 2.8 percent over the 2015 budget.¹⁵² In 2016, China's announced military budget grew by single digits for the first time since 2010 with an increase of 7.6 percent to 954.35 billion renminbi or \$146.7 billion (1.3 percent of projected GDP).[†]¹⁵³ The slow growth of Taiwan's defense budget was due to a number of factors, including: the improvement in cross-Strait relations that reduced the concern of some in Taiwan regarding China's military threat to Taiwan; growing competition for government resources, particularly from social welfare programs; increasing government debt; partisan political wrangling; and uncertainty about the future of U.S. arms sales to Taiwan, particularly requested sales that Taiwan factors into its budget but are not completed due to delays resulting from unresolved issues on both sides.¹⁵⁴ In the years prior to President Tsai's election, the DPP promised to raise Taiwan's defense budget to 3 percent of GDP.¹⁵⁵ However, in June 2016, Taiwan Premier Lin Chuan said the 2017 defense budget would not reach that level due to financial constraints.¹⁵⁶

Faced with a growing threat from PLA modernization, Taiwan has sought to enhance its military capabilities in part by indigenously developing platforms and weapons systems. Advanced anti-ship cruise missiles, air defense missiles, and fast attack and stealthy catamaran-style patrol ships are among the newest platforms and weapons systems that Taiwan has produced. Some of the developments in Taiwan's procurement of domestic military equipment over the past year include the following:

- *Missile corvette*: Taiwan's TUO JIANG-class catamaran-style missile corvette is projected to enter serial production in 2018.¹⁵⁷ Taiwan commissioned the first ship in this class in March 2015, and after identifying several areas in which the ship needed improvement, has since created a new design for serial production.¹⁵⁸ Taiwan may build up to 11 more ships in the TUO JIANG-class. The new corvette has stealth features and better range, endurance, and sea-keeping ability than Taiwan's other patrol ships, and it is equipped with 16 anti-ship cruise missiles.¹⁵⁹ It also has two torpedo tubes and a towed sonar array.¹⁶⁰ These features will enhance the survivability and lethality of Taiwan's antisurface and antisubmarine forces in a potential cross-Strait conflict.¹⁶¹

* This measurement is according to China's announced defense budgets, not actual aggregate spending. China's announced budget omits major defense-related expenditures, such as purchases of advanced weapons, R&D programs, and local government support to the PLA.

† See Chapter 2, Section 1, "Year in Review: Security and Foreign Affairs," for more information on China's defense budget.

- *Naval combat system:* Taiwan is developing the Hsun Lien combat system with which it will equip ships across the Taiwan Navy.¹⁶² With Hsun Lien, Taiwan seeks to develop a combat system that can track and engage numerous targets in various domains in order to enhance Taiwan's fleet air defense against China's antiship cruise missiles as well as the Taiwan Navy's ability to attack the PLA Navy's surface combatants and submarines.¹⁶³
- *Submarines:* Taiwan is moving ahead with its plan to indigenously build submarines with foreign assistance. The Tsai Administration has expressed hope that the U.S. government will assist with this process.¹⁶⁴ Taiwan has begun to design the indigenous submarine, a stage it hopes to complete by 2019, and announced the opening of its development center.¹⁶⁵ Taiwan currently has four submarines; two are operational Zwaardvis-class submarines and two are decommissioned U.S. Navy GUPPY-class submarines (which have undergone upgrades since the 1940s) used only for training.¹⁶⁶ The Taiwan Navy's already limited ability to conduct antisurface warfare against China's expanding fleet of modern surface ships will continue to erode as Taiwan's submarine force ages.

Taiwan also seeks to enhance its military capabilities through procurement of military platforms and weapons systems from overseas. Select military equipment Taiwan is acquiring from the United States* includes the following (see also the discussion on arms sales, military-to-military contacts, and U.S.-Taiwan defense relations in "U.S.-Taiwan Relations," later in this section):

- *F-16 fighter upgrade:* Taiwan and the United States continue to move forward with the upgrade of Taiwan's 144 F-16 A/B fighter aircraft. Following the initial flight in October 2015 of the first two upgraded fighters, which were built by Lockheed Martin, the chairman of the board of Taiwan's Aerospace Industrial Development Corporation announced in May 2016 that the company's facility in Taiwan—where the upgrade for the rest of the fleet will occur—is projected to be completed by the end of 2016, and the upgrade will begin in 2017.¹⁶⁷ The most important part of the upgrade is the installation of active electronically scanned array scalable agile beam radar made by Northrup Grumman.¹⁶⁸ This radar will enable Taiwan's F-16s to better detect China's advanced combat aircraft.¹⁶⁹
- *P-3C Orion maritime patrol aircraft:* By July 2016, Taiwan was projected to receive the remaining two of 12 P-3C antisubmarine aircraft it purchased from the United States in 2007 (they had not been delivered at the time this Report went to print).¹⁷⁰ The P-3Cs, which began arriving in 2013, will replace the Taiwan Air Force's fleet of 11 S-2T antisubmarine aircraft that have been in service for over 40 years.¹⁷¹ The P-3C will increase the capabilities and endurance of the Taiwan

*Although the United States is Taiwan's most important source of advanced military equipment, companies based in Germany and Singapore, among other countries, supplied technology for Taiwan's TUO JIANG-class missile corvette. Wendell Minnick, "Taiwan Navy Accepts New Catamaran," *Defense News*, December 31, 2014.

military's fixed-wing maritime patrol aircraft force, improving Taiwan's ability to perform antisubmarine warfare and intelligence, surveillance, and reconnaissance missions.¹⁷²

Defense Policy and Strategy under the Tsai Administration

During its first year in office, the Tsai Administration further articulated its defense policies and defense strategy, which will build on and refine the policy platform expressed by the DPP and President Tsai in recent years and during her campaign.* In a May 2015 policy paper, the DPP announced that a DPP administration would initiate an open defense policy discussion and issue its own quadrennial defense review within ten months of taking office.¹⁷³ Between June 2013 and May 2015, the New Frontier Foundation, the DPP's think tank, issued 12 defense-related policy papers that call for: building and acquiring asymmetric platforms; creating a new military service for cybersecurity and electronic warfare; bolstering missile defense capacity; building improved combat survivability against missile strikes; restructuring the ground force into specialized rapid response units; and maintaining capabilities in air and sea control.¹⁷⁴ In May 2016, following President Tsai's inauguration, Minister of Defense Feng Shih-kuan told the Foreign Affairs and National Defense Committee of the Legislative Yuan that the Administration would move forward with establishing the new cyber service of the military.¹⁷⁵

Support for Taiwan's defense industry and indigenous R&D are major components of President Tsai's defense policy. Three of the New Frontier Foundation's 12 defense policy papers focus on these issues and President Tsai held a press conference in October 2015 to discuss her defense industrial policy. During the press conference she outlined the three areas of domestic defense technology on which her administration would focus its efforts: aviation and aerospace, shipbuilding, and cybersecurity. She specifically called for the development of a new trainer aircraft and next-generation fighter aircraft and pledged that Taiwan would begin the development of a prototype of an indigenous submarine in 2016, with a plan for the first boat to be launched in ten years.¹⁷⁶ Regarding funding for such programs, in addition to the DPP's pledge to restore defense spending to 3 percent of GDP annually, one of the DPP's policy papers advocated for 70 percent of all new defense spending to go toward "military investments," including procurement of weapons and equipment, defense construction, and R&D.¹⁷⁷ Another policy paper also set the goal that by 2020 no less than 60 percent of these military investments will be spent on indigenous R&D.¹⁷⁸

President Tsai will continue Taiwan's building of an all-volunteer force, which began under former President Ma. During her campaign she advocated for several changes to military personnel policy and voiced support for slowing the transition away from con-

*President Tsai faced an early challenge in her tenure as commander-in-chief of the Taiwan military when a Taiwan Navy patrol ship accidentally launched an antiship cruise missile during an exercise and the missile struck a Taiwan fishing boat, killing the captain and injuring three crew members. The subsequent investigation found that procedural errors by crew members led to the accidental launch of the missile. Chen Wei-han, "MND Explains Cause of Missile Incident," *Taipei Times*, August 30, 2016.

scription.¹⁷⁹ Taiwan's transition to an all-volunteer force has been far more costly than expected, increasing budgetary pressure on R&D as well as operations and maintenance funding.¹⁸⁰ To find additional savings, Taiwan in 2013 decided to reduce its active duty force from 275,000 to 215,000 by 2015,¹⁸¹ and had planned to reduce the force to 170,000 by the end of 2019.¹⁸² The Legislative Yuan passed a resolution to suspend the latter reduction.¹⁸³ Taiwan has struggled with recruitment and retention, and despite recent improvements, the Ministry of National Defense's projection for personnel at the end of 2016 was still below the force level it assessed to be necessary to meet Taiwan's defense needs.¹⁸⁴ Therefore, the ministry decided to conscript approximately 23,100 men in 2016 for one year of compulsory active duty service.¹⁸⁵

Taiwan Military Training and Activities

The Taiwan military routinely conducts a range of exercises to maintain combat readiness; integrate new weapons systems and tactics; test and improve its capabilities; and demonstrate to the Taiwan people, China, and others that it has a credible deterrence capability. In 2016, select major exercises and activities included the following:

- *Antisubmarine exercise:* In January 2016 the Taiwan Navy conducted antisubmarine reconnaissance and escort exercises involving an antisubmarine helicopter, a frigate, a destroyer, a replenishment vessel, and a missile patrol ship.¹⁸⁶
- *Han Kuang exercises:* Taiwan's annual Han Kuang exercises began in April with a five-day, computer-assisted command post exercise, a combat simulation exercise in which commanders, staff, and communications personnel participate.¹⁸⁷ Live-fire exercises were held in August and were scheduled to be held again between October and November.¹⁸⁸ The live-fire exercises in August included information and electronic warfare, joint air defense, counter airborne and amphibious landing, joint antisubmarine warfare, and reserve mobilization, among other missions.¹⁸⁹ The exercises were held at many locations across Taiwan, including offshore islands. For the first time, civilian information technology specialists were recruited to participate in the cyber defense and attack portions of the exercises.¹⁹⁰

China's Espionage against Taiwan

China's aggressive intelligence activities against Taiwan pose a threat to Taiwan's security and to the security of U.S. military information and equipment to which Taiwan has access. (See Chapter 2, Section 3, "Chinese Intelligence Services and Espionage Threats to the United States," for more information on Chinese intelligence operations.)

These activities showed no sign of abating during the eight years of cross-Strait rapprochement.¹⁹¹ Many cases of Chinese espionage against Taiwan have come to light in recent years.¹⁹² According to a report by Taiwan's National Security Bureau, in 2014 there were 15 cases of alleged spying.¹⁹³ In his written testimony for the Com-

mission's hearing on Chinese intelligence services and espionage threats to the United States, David Major, the founder and president of CI Centre, presented a list with the names of 56 individuals who were arrested or indicted in Taiwan due to their alleged involvement in Chinese espionage plots over the past 14 years. According to Mr. Major, these were plots to "accrue the most significant technology and intelligence from [Taiwan's] military and all three intelligence services. Much of this technology was developed by the U.S. defense community in the United States and sold to Taiwan. Justifiable concerns about the security of U.S. defense systems sold to Taiwan is a byproduct of this espionage activity."¹⁹⁴

The increased travel between Taiwan and China that resulted from the warming of cross-Strait ties under the Ma Administration increased Taiwan's vulnerability to espionage by expanding China's opportunities for intelligence operations against Taiwan targets in both Taiwan and China. With its loosening of regulations on Chinese tourists, Taiwan has allowed individuals to travel independently without a tour group. Among other espionage risks, this development has made ensuring the security of Taiwan defense installations more difficult. Taiwan's *Liberty Times* reported that in October 2015 many Chinese independent travelers were riding electric scooters and bicycles taking pictures of the Jioupeng Military Base, where Taiwan tests missiles.¹⁹⁵

In the face of the Chinese espionage threat, the Taiwan military has implemented measures to impede Chinese intelligence activities. Peter Mattis, China fellow at the Jamestown Foundation, writes that "Taiwan has made several substantial efforts to improve security—including trip reporting and routine polygraphs for personnel with sensitive access as well as boosting its counterintelligence staff—and serious offenders can, but not always, receive heavy prison sentences."¹⁹⁶

William Stanton, former director of the American Institute in Taiwan and current director of Taiwan's National Tsinghua University's Center for Asia Policy, said in 2013 that cases of Chinese espionage against Taiwan "have been harmful not only because of the potential loss of unknown quantities of classified information, but also because their success and frequency serves to undermine U.S. confidence in security cooperation with Taiwan."¹⁹⁷ However, Mr. Major testified to the Commission that "if the USA begins to slowdown or stop the transfer of needed technology and information with Taiwan for fear of espionage loss then the PRC wins and Taiwan is doomed."¹⁹⁸ He noted that "during the period 2001 to 2016 154 individuals arrested in the USA were involved in providing sensitive information and/or technology to entities in China. Thus PRC 'espionage' is a problem and reality for both [Taiwan], the USA and the world as a whole."¹⁹⁹

Beyond Chinese espionage, Taiwan faces the challenge of Chinese political warfare. A scholar told the Commission that China conducts influence operations against Taiwan through academic institutions, cultural groups, and artistic organizations.²⁰⁰ Chinese political warfare not only seeks to affect views within Taiwan but also views of Taiwan held by people in other countries. For example, Mr. Cole wrote that some of the ways that China conducts political warfare against Taiwan are through PLA "officers at inter-

national conferences (if they speak good English, they are likely political warfare officers) and through comments to the media (including specialized publications such as *Defense News*) portraying the Taiwanese military apparatus as incompetent, careless, and/or entirely penetrated by Chinese intelligence.”²⁰¹ These activities are part of a longstanding and extensive effort by Beijing that is ultimately aimed at subjugating Taiwan under Beijing’s rule by influencing views of China within Taiwan, undermining Taiwan’s status in the international community, and sowing distrust between Washington and Taipei.²⁰²

U.S.-Taiwan Relations

Political Relations in the Tsai Ing-wen Era

U.S.-Taiwan relations are on track to expand on the growth in cooperation and mutual trust that developed during the Ma Administration. During her speech in Washington, DC in 2015, now President Tsai emphasized that Taiwan will be a reliable partner of the United States, and in an op-ed published by the *Wall Street Journal* during her trip she described the United States as “Taiwan’s most important strategic partner” and advocated for “broadening multi-faceted cooperation with the [United States].”²⁰³ Later, in September 2015, she explained that Taiwan’s relationship with the United States and other like-minded democracies will be based on “mutual trust, respect, and communication.”²⁰⁴ Immediately following President Tsai’s election, the U.S. government praised Taiwan’s democracy and expressed its anticipation for partnering with the Tsai Administration and its appreciation to then President Ma for his contribution to strengthening U.S.-Taiwan relations.²⁰⁵ In the following months, other U.S. officials expressed praise for Taiwan’s democracy.²⁰⁶ In Congressional testimony in February on U.S.-Taiwan relations, Deputy Assistant Secretary of State in the Bureau of East Asian and Pacific Affairs Susan Thornton said, “The people on Taiwan have built a prosperous, free, and orderly society with strong institutions, worthy of emulation and envy. . . . Last month’s free and fair elections were yet another victory for Taiwan’s vibrant democracy.”²⁰⁷ Prior to President Tsai’s inauguration, Deputy Assistant Secretary Thornton also expressed support for President Tsai’s approach to cross-Strait relations. In an interview with Taiwan’s Central News Agency she said, “I think there has been a very good political basis laid for the continuation of cross-strait exchanges, as President-elect Tsai also has mentioned.”²⁰⁸

Trade and Investment

President Tsai’s emphasis on the importance of Taiwan’s relations with the United States, on strengthening economic partnerships beyond China, and on Taiwan joining TPP almost certainly will help to deepen U.S.-Taiwan economic ties during her administration.

In 2015, Taiwan became the United States’ ninth largest trading partner, surpassing India, Italy, and Brazil.²⁰⁹ Bilateral trade to-

taled \$66.6 billion, a 1.2 percent decline since 2014.*²¹⁰ The United States exported \$25.9 billion in goods to Taiwan and imported \$40.7 billion in goods from Taiwan.²¹¹ Taiwan is also the seventh-largest importer of U.S. agricultural products.²¹² The United States remained ahead of Japan as Taiwan's second largest trading partner.[†]²¹³ The United States is Taiwan's third largest export market and source of imports.²¹⁴ The top U.S. exports to Taiwan include industrial machinery, semiconductors, civilian aircraft, and military equipment.²¹⁵ The top U.S. imports from Taiwan include semiconductors, telecommunications equipment, vehicle parts, cellular phones, and computer accessories.²¹⁶ In addition, the United States is Taiwan's largest source of FDI.²¹⁷ Taiwan is the 29th largest investor in the United States in terms of total stock of FDI, and Taiwan companies employed more than 12,000 U.S. workers as of 2013. Taiwan is also a major participant in the U.S. Department of Commerce's SelectUSA Investment Summit.[‡]²¹⁸

Although U.S.-Taiwan economic ties remain strong, substantive progress in some areas of ongoing trade and investment negotiations slowed in recent years.²¹⁹ Both sides discuss bilateral economic issues primarily through a Trade and Investment Framework Agreement (TIFA), established in 1994. The last TIFA meeting was held in October 2016, during which the United States and Taiwan discussed a range of bilateral economic issues, including agriculture, pharmaceuticals and medical devices, intellectual property rights protection, trade barriers, and investment.²²⁰ However, the two sides have yet to resolve a dispute over U.S. pork imports, one of the most contentious issues in the economic relationship.²²¹ Although Taiwan loosened some restrictions on residual levels of ractopamine § in U.S. beef imports in 2012, it maintains these restrictions on pork imports. Several key roadblocks to overturning restrictions include pressure from Taiwan's pork industry and Taiwan citizens' aversion to the use of ractopamine in pork production.²²² The Tsai Administration has not announced whether or not it will remove the restrictions.

One area with great potential for expanding the scope of U.S.-Taiwan economic relations is cooperation in the information and communications technology (ICT) industry. According to Lotta Danielsson, vice president of the U.S.-Taiwan Business Council, who spoke at an event at the Center for Strategic and International Studies in August 2016, Taiwan has evolved from a purely

*Trade statistics from the U.S. Census Bureau in this section include re-exports and re-imports.

†Trade statistics from Taiwan's Bureau of Foreign Trade in this section exclude re-exports and re-imports.

‡The U.S. Department of Commerce's SelectUSA program helps foreign companies invest in the United States and assists U.S. economic development organizations in attracting FDI. The annual SelectUSA Investment Summit is the program's most high-profile conference for promoting FDI in the United States. U.S. Department of Commerce, "SelectUSA."

§ Taiwan banned imports of U.S. beef because Taiwan citizens were concerned safeguards to prevent mad cow disease were insufficient and because U.S. farmers' use of ractopamine, a controversial feed additive that promotes leanness in meat. Ractopamine is widely used in U.S. pork and beef production, but Taiwan, the EU, and China have banned the use of ractopamine based on health and safety concerns. The issue was partially resolved when the Taiwan government established a maximum residue limit for ractopamine in beef in September 2012, allowing U.S. beef exports greater access to Taiwan. In 2013, the U.S. became Taiwan's largest beef supplier by value. J.R., "Gored," *Banyan Asia (Economist blog)*, March 8, 2012; Shirley Kan and Wayne Morrison, "U.S.-Taiwan Relationship: Overview of Policy Issues" *Congressional Research Service*, April 22, 2014, 34-36; and Cleo Fu and Emily Scott, "U.S. Beef Exports to Taiwan Realize 2013 as Record Year," *USDA Foreign Agricultural Service*, March 31, 2014.

trade-based partner to an innovation partner of the United States.²²³ Cooperation in R&D between the United States and Taiwan is strong. U.S. companies HP, DuPont, and Dell have R&D centers in Taiwan; and Google and IBM have cloud computing centers in Taiwan.²²⁴ The U.S. and Taiwan governments hosted the inaugural U.S.-Taiwan Digital Economy Forum in December 2015. In an upcoming meeting later this year, both sides will continue to focus on bilateral collaboration on cross-border ICT applications, legal and regulatory frameworks, the expansion of global ICT connectivity, data privacy, and intellectual property protection.²²⁵

Military and Security Cooperation

U.S.-Taiwan security cooperation includes arms sales, training, advising, exchanges, and equipment maintenance.²²⁶ This partnership helps Taiwan enhance its ability to deter and, if necessary, defend against an attack from the Chinese military.

On December 16, 2015, the U.S. Department of State notified Congress* that it had approved the potential sale of \$1.83 billion in arms to Taiwan,²²⁷ including the following items: (1) two refurbished and upgraded OLIVER HAZARD PERRY-class guided-missile frigates; (2) AAV-7 amphibious assault vehicles; (3) Javelin antitank missiles; (4) BGM-71F tube-launched, optically-tracked, wireless-guided (TOW) antitank missiles; (5) man-portable Stinger missiles; (6) MK-15 Phalanx close-in weapons systems (CIWS); (7) Multifunctional Information Distribution System Low Volume Terminals (MIDS/LVT-1) and Joint Tactical Information Distribution System (JTIDS) data communications support; and (8) Taiwan Advanced Tactical Data Link System (TATDLS) and Link-11 communication systems integration (see Table 1).²²⁸

This most recent notification brings the value of the Obama Administration's total notifications of Taiwan arms sales to Congress to over \$14 billion.²²⁹ Despite the large value of arms sales notifications, the Administration's prior notification occurred more than four years before in 2011. The package also did not include advanced fighter aircraft and assistance to Taiwan's indigenous submarine program, in which Taiwan has expressed interest. Although the time period between notifications to Congress was almost certainly affected by concern within the executive branch about the impact of arms sales to Taiwan on U.S.-China relations,²³⁰ budgetary constraints in Taiwan also likely were a factor. Ongoing payments for U.S. weapons that were notified previously likely put pressure on Taiwan's budget.²³¹

*The executive branch is required to notify Congress of arms sales through the foreign military sales process that meet or exceed the following values: \$14 million in major defense equipment, \$50 million in defense articles or services, and \$200 million in design and construction services. Paul K. Kerr, "Arms Sales: Congressional Review Process," *Congressional Research Service*, April 19, 2016.

Table 1: 2015 U.S. Arms Package and Its Utility in a Cross-Strait Conflict

Platforms, Weapons, and Systems	Utility in a Cross-Strait Conflict
Two PERRY-class guided missile frigates (refurbished)	These general-purpose escort ships, which will be equipped for antisubmarine, surface-to-surface, and surface-to-air operations ²³² would help Taiwan protect other ships against PLA submarines, surface combatants, and aircraft.
36 AAV-7 Amphibious Assault Vehicles	The AAV-7s will strengthen the expeditionary capability and mobility ²³³ of the Taiwan Marine Corps and would help Taiwan deploy troops along Taiwan's coastline in the event of an invasion.
208 Javelin antitank missiles	These portable missiles ²³⁴ would help Taiwan defend against PLA tanks, mechanized infantry, and helicopters.
769 BGM-71F TOW 2B-Aero antitank missiles	With a range of 4.5 kilometers (3 miles), ²³⁵ these missiles would help Taiwan engage PLA tanks and mechanized infantry at a distance.
250 Stinger surface-to-air missiles	These missiles, with a range of five miles, ²³⁶ would help Taiwan engage PLA aircraft approaching or over Taiwan.
13 MK-15 Phalanx CIWS guns	The Phalanx CIWS is a close-range point-defense system ²³⁷ and would help to defend Taiwan's surface combatants against PLA missiles and aircraft.
Support for MIDS/LVT-1 and JTIDS	MIDS—a command, control, communications, computers, and intelligence system—and JTIDS—a radio communications system ²³⁸ —would enhance communication and coordination across the Taiwan military during a cross-Strait conflict.
TATDLS and Link-11 Integration	TATDLS is a beyond line-of-sight datalink system that would enhance communication, data sharing, and integration between Taiwan's surface ships. ²³⁹

Source: Information about the number and type of each weapons system is compiled from U.S. Defense Security Cooperation Agency, "Major Arms Sales," December 16, 2015.

The items in the December 2015 announcement will provide modest improvements to Taiwan's military capabilities.²⁴⁰ Mr. Cole wrote about the package, "Political symbolism aside, this week's arms package does have some defensive value."²⁴¹ Moreover, the announcement sent a message to Beijing and Taipei that the United States remains committed to Taiwan's defense.

Military-to-military contacts between the United States and Taiwan have dramatically increased in recent years. According to Deputy Assistant Secretary Thornton, the number of annual "security cooperation events" with Taiwan has nearly doubled in recent years.²⁴² Furthermore, the number of U.S. Department of Defense personnel visiting Taiwan increased from around 1,500 in 2012 to more than 3,200 in 2015.²⁴³ Among other areas of training, the United States provides training to Taiwan fighter pilots, special operations personnel, and rapid runway repair personnel, and Taiwan military personnel study at U.S. military institutions.²⁴⁴

Nevertheless, the U.S. government practice of limiting the highest rank of U.S. military personnel who can visit Taiwan to colonels and captains (O6 level) prevents the most senior U.S. officers from gaining firsthand knowledge of the Taiwan military and the operational environment in a potential cross-Strait conflict.*²⁴⁵ In addition, Taiwan is not invited to a number of major U.S.-led military exercises, such as the biennial Rim of the Pacific (RIMPAC) exercise—which included China in 2014 and 2016—and the Red Flag air-to-air combat training exercise, and other security exercises, such as the biennial cybersecurity exercise Cyber Storm. Participating in such exercises, even as an observer, could help Taiwan enhance its ability to defend itself and provide the Taiwan military with more opportunities to interact with other militaries.

Other Areas of Cooperation

Beyond commercial and security ties, U.S.-Taiwan relations span many other areas, including environmental protection and humanitarian assistance and disaster relief.²⁴⁶ One of the most dynamic U.S.-Taiwan initiatives is the Global Cooperation and Training Framework, which the two countries established in June 2015. Through this initiative, the United States and Taiwan jointly train experts from the Asia Pacific in areas including the empowerment of women, public health, energy, and information and communication technology.²⁴⁷ Taiwan has already hosted several programs under the initiative, such as a training course for laboratory professionals on diagnosing, preventing, and responding to Middle East Respiratory Syndrome, and a training course for government officials and health care professionals on the prevention and control of dengue fever.²⁴⁸

Another area where the United States and Taiwan are collaborating is cybersecurity. In May, a delegation led by Assistant Secretary of Commerce for Industry and Analysis Marcus Jadotte visited Taiwan to attend the first-ever U.S.-Taiwan Cyber Security Forum and advance cybersecurity cooperation.²⁴⁹ Assistant Secretary Jadotte and the Taiwan Computer Association signed a statement of intent, which the assistant secretary said “calls for both sides to explore ways to work together to counter cybersecurity risks and make the Internet a safer place for individuals and businesses.”²⁵⁰ The delegation included representatives of companies such as Cisco Systems and Lockheed Martin.²⁵¹

Taiwan’s Role in the U.S. Rebalance to Asia

In May 2015, the Obama Administration provided its most detailed explanation of Taiwan’s role in the U.S. Rebalance to Asia

*The versions of the National Defense Authorization Act for Fiscal Year 2017 passed by the Senate (S. 2943) and the House (H.R. 4909) include a sense of Congress that “the Secretary of Defense should conduct a program of senior military exchanges between the United States and Taiwan that have the objective of improving military-to-military relations and defense cooperation between the United States and Taiwan.” The exchanges would occur at least once a year in the United States and in Taiwan and would involve active-duty general or flag officers and civilian Department of Defense officials at the level of assistant secretary of defense or above. The bill was still in conference negotiations at the time of the publication of this Report. Joe Gould, “Congress Girds for Defense Spending, Policy Fights,” *Defense News*, September 2, 2016; National Defense Authorization Act for Fiscal Year 2017, S. 2943, 114th Cong., 2nd Sess., July 7, 2016; and National Defense Authorization Act for Fiscal Year 2017, H.R. 4909, 114th Cong., 2nd Sess., May 26, 2016.

strategy. (See Chapter 4, “China and the U.S. Rebalance to Asia,” for more information on the Rebalance to Asia strategy.) U.S. Secretary of State John Kerry, in a written response to a question from the House Foreign Affairs Committee, described deepening U.S.-Taiwan engagement on trade and investment, cooperating on regional economic integration through the Asia Pacific Economic Cooperation forum, and making available U.S. defense articles and services to Taiwan. He said, “Collectively, these activities demonstrate our continued commitment to Taiwan’s peace, security, and prosperity as part of the U.S. rebalance.”²⁵² Prior to Secretary of State Kerry’s letter, other U.S. officials have mentioned Taiwan’s role in the Rebalance but have not elaborated about how Taiwan fits into the strategy.²⁵³ This lack of clarity could be due to concerns about the impact on U.S.-China relations of openly emphasizing Taiwan in the strategy.

The Tsai Administration is striving for Taiwan to be included in the second round of negotiations of TPP, which has been described by Obama Administration officials as the central economic component of the Rebalance strategy. In her meeting with the delegation led by Assistant Secretary Jadotte in May, President Tsai said, “The 12 TPP member states account for 37 percent of Taiwan’s total trade. It’s crucial for us to join TPP.”²⁵⁴ Some analysts have advocated for the United States to support Taiwan’s bid to join TPP.²⁵⁵ A place in TPP would enable Taiwan to participate more fully in regional economic integration and expand market access for its exports,²⁵⁶ supporting its efforts to diversify its export markets. One business representative in Taiwan told the Commission that joining TPP is a crucial step toward ensuring Taiwan maintains its economic competitiveness.²⁵⁷ For the United States, Taiwan’s participation in TPP would allow U.S. companies greater access to Taiwan’s economy,²⁵⁸ which ranks 22nd in the world in terms of GDP by purchasing power parity and is larger than the economies of half of the current TPP member countries.²⁵⁹ In addition, Dr. Bush and Joshua Meltzer, senior fellow in global economy and development at the Brookings Institution, explained that by including Taiwan, TPP would include an “important driver of trade and investment in the Asia Pacific region.”²⁶⁰ Scholars at the Chung-Hua Institute for Economic Research in Taiwan told the Commission that even if Taiwan is unable to join TPP, carrying out the economic reforms necessary to meet TPP’s standards, including a better regulatory environment and increased government transparency, will benefit Taiwan.²⁶¹ Another scholar added that these reforms also would improve Taiwan’s prospects for a free trade agreement with the United States.²⁶²

Other ideas raised in recent years for enhancing U.S. engagement with Taiwan include increasing science and technology and defense-industrial cooperation, expanding U.S.-Taiwan joint training programs in various fields for experts from third countries, collaborating with the Taiwan military to enhance maritime domain awareness in the Pacific Ocean, and inviting Taiwan to participate in U.S.-led multilateral military exercises.²⁶³ In February 2016, Randall Schriver, president and chief executive officer of the Project 2049 Institute, in testimony to Congress stated, “The Taiwanese economy has long relied upon maintaining a technological

comparative advantage, and sustaining this advantage is an important driving force shaping the future of the region. . . . The U.S. and Taiwan could deepen and broaden their economic relationship by expanding [science and technology] cooperation. Additionally, [science and technology] cooperation could help Taiwan maintain its technological advantage and produce mutually beneficial innovations.”²⁶⁴ In March, at an event at the George Washington University, Mr. Shriver suggested that the United States consider expanding the U.S.-Taiwan Global Cooperation and Training Framework to include other like-minded countries, such as Australia, Japan, and India, among the trainers and to include training in areas such as antipiracy and counterterrorism.²⁶⁵

Scholars in Taiwan told the Commission that humanitarian assistance and disaster relief and search and rescue are areas with great potential for expanded U.S.-Taiwan cooperation. They said that Taiwan has very capable humanitarian assistance and disaster relief and search and rescue forces and pointed out that the second-largest humanitarian assistance and disaster relief training center in East Asia is in Taiwan.²⁶⁶ One example of U.S.-Taiwan cooperation in humanitarian assistance and disaster relief occurred in 2010 when a Taiwan Air Force transport aircraft landed in the United States to refuel during its flight to deliver relief supplies to Haiti following a major earthquake.²⁶⁷ The previous year, after Typhoon Morakot hit Taiwan, the U.S. military assisted with the recovery effort by transporting construction vehicles and equipment and relief supplies to the affected areas.²⁶⁸

Implications for the United States

Taiwan’s presidential and legislative elections in January 2016 once again demonstrated the vibrancy of its democracy and the common values that are one of the pillars of U.S.-Taiwan relations. The elections also demonstrated that Taiwan is a model for other countries in the region and around the world. As Kurt Tong, principal deputy assistant secretary in the Department of State’s Bureau of Economic and Business Affairs, explained in a speech about Taiwan in March 2016, “Taiwan’s evolution into a robust democracy, and a strong free market economy, with a vibrant civil society, make it a model for others.”²⁶⁹

Taiwan’s robust democracy, civil society, and technology sector, and its vast expertise and experience in various areas, such as humanitarian assistance and disaster relief, make it a strong partner for the United States in facing global challenges. As the United States seeks to engage in capacity building in the Asia Pacific, Taiwan is assisting with these efforts through the Global Cooperation and Training Framework.

Taiwan also is a contributor to regional peace and stability through its efforts to promote the setting aside of territorial disputes and joint resource development in the East and South China seas. Two examples of this policy are the fisheries agreements that Taiwan signed in recent years with Japan and the Philippines, respectively. Other actions by Taiwan that support U.S. objectives of rule of law and peaceful resolution of disputes include taking steps

to clarify its claims in the South China Sea and expressing support for multilateral negotiations on the South China Sea.²⁷⁰

Going forward, in this new period of cross-Strait relations following the election of President Tsai, whether tension between Taiwan and China will increase is unclear. Should tension grow significantly, the United States may have to devote more attention to cross-Strait relations. Furthermore, Ms. Glaser writes that “a spike in cross-Strait tension increases the risk of a wider conflict through political and even military escalation, which could draw in the United States.”²⁷¹ Beijing further limited Taiwan’s participation in international organizations, which is not in U.S. interests. Taiwan has much to contribute to the international community in areas including aviation safety, public health and combating the spread of infectious diseases, and law enforcement and fighting transnational crime.²⁷²

The U.S.-Taiwan security partnership contributes to regional peace and stability by enhancing Taiwan’s ability to deter an attack by the Chinese military. However, China’s military modernization presents a significant challenge both to Taiwan’s ability to defend itself and to the United States’ ability to intervene effectively in a cross-Strait conflict should it choose to do so. It also improves China’s ability to use the threat of military force to coerce Taiwan into making political concessions.

Conclusions

- In 2016, Taiwan held historic elections, in which Tsai Ing-wen of the Democratic Progressive Party (DPP), was elected Taiwan’s first female president and the DPP gained an absolute legislative majority for the first time. Despite President Tsai’s pragmatic cross-Strait policy focused on maintaining the status quo, Beijing appears to remain skeptical of President Tsai and has applied pressure on her administration with various statements and actions.
- China remains Taiwan’s largest trading partner, biggest export market, and top source of imports. However, cross-Strait trade has slowed, in large part due to the negative impact of China’s economic slowdown and the emergence of Chinese competitors on Taiwan’s information technology exports to China, which underscores the vulnerability of Taiwan’s export-dependent economy to developments in China.
- Taiwan’s ability to participate in the international community is not only crucial to the wellbeing of its people but is also key to Taiwan’s ability to contribute to international safety, security, and prosperity. Beijing restricts Taiwan’s participation in international organizations and has placed additional limitations on Taiwan’s international activities since President Tsai was elected. Should Beijing seek to further increase pressure on Taipei, it may take additional steps to restrict Taiwan’s international space, including by enticing some countries with which Taiwan has diplomatic relations to cut ties and establish diplomatic relations with China.

- China's military modernization remains focused on preparing for a range of Taiwan contingencies, and the advancement in the capabilities of the People's Liberation Army (PLA) presents a significant challenge to Taiwan's ability to defend itself and the U.S. military's ability to effectively intervene in a cross-Strait conflict. Taiwan is engaged in a robust program to enhance its defensive capabilities through its domestic defense industrial production, the procurement of U.S. weapons systems, and its transition to an all-volunteer force, efforts which the Tsai Administration seeks to refine and build upon. However, the cross-Strait military balance has shifted toward China, and the PLA possesses both a quantitative and a qualitative military advantage over the Taiwan military.
- U.S.-Taiwan relations have transitioned smoothly from the Ma Administration to the Tsai Administration and continue to strengthen and expand in scope. Security cooperation remains a robust area of the U.S.-Taiwan relationship.

RECOMMENDATIONS

China and Taiwan

The Commission recommends:

- Members of Congress and Congressional staff seek opportunities to advance U.S.-Taiwan economic, political, and security relations, support Taiwan's participation in international organizations, and draw attention to Taiwan's democratic achievements and contributions to the international community.
- Congress urge the executive branch to make available to Taiwan, consistent with the Taiwan Relations Act, defense articles and services required to address the continuing shift in the cross-Strait military balance toward China.
- Congress direct the U.S. Department of State to reexamine its policy guidelines on reciprocal visits by senior U.S. and Taiwan military officers and civilian officials with the aim of increasing high-level exchanges.
- Congress request briefings by the Office of the U.S. Trade Representative (USTR) on the status of the Trade and Investment Framework Agreement negotiations with Taiwan and direct the USTR to identify enhanced negotiating procedures to resolve outstanding issues and ensure an accelerated path to conclude such talks.

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