INTERNATIONAL JOURNAL OF BUSINESS, 7(3), 2002 ISSN:1083-4346

The Three-way Economic Relationships among U.S., Taiwan, and China

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ABSTRACT

The study investigates the economic relationships in terms of trade and foreign direct investment among U.S., Taiwan, and China. Our results indicate that their relationships are increasingly linked.

JEL: *F14, F18, F21*

Keywords: *Trade; Foreign direct investment; Economic relationships*

I. INTRODUCTION

The relationships among the United States, Taiwan and People's Republic of China have attracted attention both politically and economically [Chai (1999) and Janow (1998)]. The changing relationships among the three parties have become more conspicuous as the ruling party platform of the new Taiwan government leans toward pro-independence and the current Bush administration in the U.S. takes a tougher stance on the U.S.-China diplomacy. Seeking a new equilibrium is on the front burner in the millennium.

It is undeniable that the three economies are increasingly linked. My research aims to shed light on the economic relationship and illustrate its increasing importance in recent years. Economic ties studied in the paper are basically focused on international trade and foreign direct investments (FDI). Some misconceptions of their economic ties are clarified.

We discuss separately China's trade, bilateral trade between China and Taiwan, and the economic relationship between Taiwan and the U.S. The economic links between China and the U.S are discussed briefly, and some policy implications are drawn.

II. CHINA’S TRADE

International trade is an important component of China's economic growth. The economic growth rate had sustained at about 9 percent per year for almost two decades before the 1997 Asian financial crisis. Table 1, Panel A, documents China's export and total trade (exports and imports) for the period 1990-2000. In 1999, exports amounted to US$ 194.9 billion, almost about 20 percent of China's gross domestic product (GDP). Total trade was US$ 360.6 billion, just over about 36 percent of its GDP. Exports increased to US$ 249.2 billion (23 percent of GDP) and the total trading increased to US$ 474.3 billion (44 percent of GDP) in 2000. We can draw two conclusions from these data. China's economic growth depends critically on its external trade sector. China is also economically vulnerable with this amount of dependence on international trade.

Table 1, Panel B, identifies China's top ten trading partners in the year 2000. The ranking of these trade partners has been quite stable for the past several years. Japan is the largest trading partner, making up about 18 percent of China's total trade, followed by the U.S., which accounts for about 16 percent. Taiwan ranks as the fifth trading partner, accounting for over 6 percent of China's total trade. Thus, Taiwan and the U.S. are indeed strategically important trading partners with China.

Table 1
China trade statistics

Panel A: Gross domestic product (GDP) and trade (US $billion)

Year	GDP		China Export		China Total Trade	
	RMB (¥)	US$	Export	%GDP	Total trade	%GDP
1990	1855	387.77	62.09	16.01	115.4	29.76
1991	2019	379.32	71.84	18.94	135.7	35.77
1992	2402	435.55	84.94	19.50	165.5	38.00
1993	3452	599.11	91.74	15.31	195.7	32.67
1994	4662	540.92	121.0	22.37	236.6	43.74
1995	5826	697.67	148.8	21.33	280.9	40.26
1996	6779	815.35	151.1	18.53	289.9	35.56
1997	7380	890.25	182.8	20.53	325.1	36.52
1998	7900	954.21	183.8	19.26	324.0	33.95
1999	8265	996.98	194.9	19.55	360.6	36.17
2000	8900	1073.58	249.2	23.21	474.3	44.18

Source: China GDP (1978-1995) from Huang (1998)
China GDP (1996-2000) from U.S. Department of Commerce.
China total trade from Ministry of Foreign Trade and Economic Cooperation (MOFTEC), http://www.moftec.gov.cn
China export from China Council for the Promotion of International Trade (CCPIT) statistics (2000).

Panel B**:** China 's top ten trade partners in 2000 (total trade by customs, US$ billion)

Rank	Country	Total Trade	% of Total PRC Trade	% of China's GDP
1	Japan	83.17	17.54	7.75
2	U.S.	74.47	15.70	6.94
3	Hong Kong	53.95	11.37	5.03
4	South Korea	34.50	7.27	3.21
5	Taiwan	30.53	6.44	2.84
6	Germany	19.69	4.15	1.83
7	Singapore	10.82	2.28	1.01
8	United Kingdom	9.90	2.09	0.92
9	Australia	8.45	1.78	0.79
10	Russia	8.03	1.69	0.75

Source: PRC General Administration of Customs, China Customs Statistics (2001).

III. TRADE POLICY AND ECONOMIC RELATIONS BETWEEN CHINA AND TAIWAN

Following China's open-door policy implemented in 1978, a trade relationship between Taiwan and China started to develop. Trading between China and Taiwan began first as an exchange among fishermen of merchandise, which was followed by indirect trade relations. From China's perspective, trade with Taiwan promotes contact between the two governments and economic integration between the two economies. At the same time, China can provide Taiwan business people with resources such as labor and land for expansion.

In April 1980, China allowed imports from Taiwan to be duty free as "inter-provincial material exchange." On May 1, 1981, Taiwan imports were declared to be domestic products and thus exempt from custom tariffs.

In July 1985, Taiwan allowed entrepot trade but prohibited direct trade. After Taiwan's lifting of travel restrictions to China in 1987, an increasing number of Taiwan business people have gone to the mainland for trade and business opportunities.

Table 2 documents the different stages of trade relationships and policy changes between the two parties. It is fair to say that since 1979, the relationship between China and Taiwan has not been straightforward but rather has evolved with ups and downs. Basically, however, both sides seem to be making efforts to improve their economic ties. Most recent links of finance and trade across the straits in 1999 and 2000 are illustrative.

Taiwan has been an important trading partner with China for the past decade. At the same time, Taiwan is also an export-oriented economy. Table 3, Panel A, displays exports and imports of Taiwan for the 1990-2000 period. Total trade for Taiwan is 76 percent of its GDP in 1990, rising to 89 percent of its GDP in 2000. This is remarkable growth in the importance of the trade sector in Taiwanese economy for the past decade.

Table 4 displays the export/import trade and foreign direct investments between China and Taiwan over 1979 -2000. The general trend is increasing trade between the two economies, suggesting that their economic ties are tightening, despite their unstable political relationship as shown in Table 2. The results in Table 4 further confirm the global trading pattern, which are seen to have grown in recent decades.

Table 2
Trade policy between China and Taiwan, 1979-2000

Year	China's policy toward Taiwan	Date	Taiwan's policy toward China
01/1979	China's National People's Congress (NPC) Standing Committee issued a "Message to Compatriots on Taiwan" calling for an end to military confrontation and limits on direct mail, trade, and travel.	04/1979	Taiwan president Chiang Ching-Kuo issued the "Three No's" policy regarding China: no direct contact, no direct trade, no direct negotiation.
04/1980	China allowed Taiwan imports to be duty-free		
05/1981	Taiwan imports are considered domestic products and pay no custom tariffs.	07/1985	Taiwan allowed entrepot trade but prohibited direct trade
09/1981	China's NPC, issued Nine Points Proposal, "Elaborations on Policy Concerning the Return of Taiwan to the Motherland and Peaceful Unification" including exchanges of mail, trade, air and other travel, shipping, tourists, and academics, and permission for family reunions, freedom of entry and exit for Taiwan's people, and Taiwanese investment in China.		
07/1988	China's State Council (CSC) issued regulations for encouraging investment by the people of Taiwan.	09/1987	Chiang Ching-kuo proposed to Kuomintang (KMT) that Taiwan residents be permitted to visit relatives on the mainland.
11/1989	Indirect telephone calls and telegrams between China and Taiwan were permitted for the first time. Taiwanese businesses allowed to invest in China with generous incentives.	07/1988	The KMT 13th Party Congress adopted a policy to ease trade and travel restrictions for Taiwanese.

Table 2 (continued)

Year	China's policy toward Taiwan	Date	Taiwan's policy toward China
03/1990	The Taiwan-Invested Enterprises Association, the first trade association of Taiwanese business-people on the mainland, was established.		
06/1990	China's new leader, Jiang Zemin, requested that the Taiwanese and mainland Chinese sit down to discuss any and all issues.		
03/1994	NPC adopted the "Law to Protect Investments by Taiwan Compatriots"	06/1990	Lee Teng-hui convened a meeting to establish the National Unification Council and formulate the Guidelines for National Unification.
12/1999	CSC issued " Detailed regulations for protecting Taiwan Investment," provides that Taiwan investment entities can exploit natural resources, purchase stocks in state-owned enterprises, etc.	09/1999	The Ministry of Finance allowed mainland China citizens in Taiwan to open foreign currency bank accounts and time deposit accounts, and to remit money, which may not exceed US$5,000 in each transaction.
		12/2000	Taiwan government proclaimed "exchanges in shipping, mail and trade" between Jinmen island, Masu island, and Fuzhou and Xiamen ports of Chinese Mainland.

Source: Author's own data.

Table 3
Taiwan's total trade, 1990-2000 (US$ billion)

Panel A: Taiwan's export and import

Year	Taiwan GDP ($)	Taiwan Export	Taiwan Import	Total Trade	Trade/GDP
1990	160.2	67.21	54.72	121.93	76%
1991	179.4	76.18	62.86	139.04	78%
1992	212.2	81.47	72.00	153.47	72%
1993	224.3	85.09	77.06	162.15	72%
1994	244.3	93.04	85.35	178.38	73%
1995	264.9	111.66	103.55	215.20	81%
1996	279.6	115.94	102.37	218.31	78%
1997	290.2	122.08	114.42	236.50	81%
1998	267.3	110.58	104.66	215.24	81%
1999	288.0	121.60	110.68	232.28	81%
2000	323.5	148.32	140.00	288.32	89%

Panel B: Taiwan's top five export products, 2000 (US$ billion)

Products	Amount	% of Total Export
Machinery, Electronic and Electric Appliances	82.6	55.6
Textile	15.2	10.3
Basic Metal	13.5	9.1
Plastic/Rubber	9.1	6.1
Transportation	5.8	3.9

Sources: Quarterly National Economic Trends August 2000 (Taiwan) p. 34.
www.trade.gov.tw/english
http://www.info.gov.hk/censtatd/chinese/hkstat/hkinf/nat_account/nat_account_index.html

Table 4
China-Taiwan trade and foreign direct investments (FDI) 1979-2000 (US$ billion)

Year	China-Taiwan Trade				FDI From Taiwan to China	
	China Export		China Import			
		(% PRC's GDP)		(% PRC's GDP)	FDI	%PRC's GDP
1979	0.06	0.02	0.02	0.01		
1980	0.08	0.03	0.23	0.09		
1981	0.08	0.03	0.38	0.14		
1982	0.08	0.03	0.19	0.07		
1983	0.09	0.03	0.16	0.05		
1984	0.13	0.04	0.43	0.14		
1985	0.12	0.04	0.99	0.32		
1986	0.14	0.05	0.81	0.29		
1987	0.29	0.10	1.23	0.40		
1988	0.48	0.13	2.24	0.59		
1989	0.59	0.14	2.90	0.68	0.15	0.04
1990	0.32	0.08	2.26	0.58	0.22	0.06
1991	0.59	0.16	3.64	0.96	0.47	0.12
1992	0.69	0.16	5.87	1.35	1.05	0.24
1993	1.46	0.24	12.90	2.16	3.13	0.52
1994	2.24	0.41	14.10	2.60	3.39	0.63
1995	3.10	0.44	14.80	2.12	3.16	0.45
1996	2.80	0.34	16.20	1.98	3.47	0.43
1997	3.40	0.38	16.40	1.85	3.29	0.37
1998	3.87	0.41	16.60	1.74	2.91	0.31
1999	3.95	0.32	19.50	1.58	2.60	0.26
2000	5.03	0.47	25.50	2.37	2.30	0.21

Source: MOFTEC statistics (2001) and from Huang (1998)

China's total trade (imports and exports) with Taiwan of US$ 30.53 billion in the year 2000, which amounts to 2.84 percent of China's GDP and 9.4 percent of Taiwan's GDP. This amount of bilateral trade between China and Taiwan is clearly important to both China and Taiwan. It should be pointed out that Taiwan's exports to China (US$ 25.5 billion) are higher than its imports from China (US$ 5.03 billion), implying a trade deficit of US$ 20.47 billion for China. This result implies that Taiwan relies more on China in terms of trade flows than the other way around. In fact, some of the imported goods are reprocessed in China and then for export purpose.

Foreign direct investments between China and Taiwan are similarly one-sided. That is, investment flows are primarily from Taiwan to China as shown in Table 4. The increase in FDI from Taiwan to China since 1989 can be explained by the trade policy changed detailed in Table 2, as China has provided more incentives for attracting Taiwan investors. Taiwan's leading investments in China consist of chemicals, basic metals and metal products, plastic products, food and beverage processing, textiles, non-metallic minerals, machinery equipment, paper products and printing, banking and insurance and services.

Table 5 documents the top five provinces where Taiwan investments are located. Jiangsu and Guangdong are the two provinces most heavily invested by Taiwanese investors. Together, investments in these provinces make up over 87 percent of all Taiwan's investments in China.

Table 5
Taiwan investments in top five provinces of China in 2000 (US$ million)

	Province	Amount	% of Total Taiwan Indirect Investment in China
1	Jiangsu	1,251.6	48.0
2	Guangdong	1,019.7	39.1
3	Fujian	99.5	3.8
4	Hebei	92.6	3.6
5	Zhejiang	68.7	2.6

Source: Investment Commission Ministry of Economic Affairs Annual Report (Taiwan), March 2001.

Coastal areas in China appear to be favorable locations for Taiwan's investments. Friedmen, et. al. (1996) analyze the important factors for locational choices for foreign investors selecting a particular location site. Coastal Chinese cities provide a good transportation network and proximity to Taiwan. The purchasing power in these coastal areas is also high. Coastal areas in fact have been set up as special economic zones, attracting foreign investors who can enjoy certain tax and other advantages, such as reduced red tape and regulations when investing in these areas. Nor is there a language barrier, as people in Taiwan and China speak the same language.

Investments from Taiwan to China appear to be large. The cumulative investment amount is more than US$ 26 billion between 1989 and 2000 as shown in Table 4. This amount is a conservative estimate. The investment amount is a cumulative value over time and not represented by current flows of money. Though the Taiwan government imposes ceilings on amounts to be invested in China, Taiwanese firms can allocate investment capital to China via offshore companies. This means investments will likely exceed the official reported figure of total investment to China from Taiwan. In fact, some suggest that the investment amount may be around US$ 30-40 billion.

Given the large amount of investment, we need to put the data into some sort of perspective with regard to value and risk. First, some reported values of investments are not necessarily stated at market prices or replacement cost, because some of the machines and equipment shipped to China may have been used in Taiwan before, and thus have been depreciated a great deal. Their economic value in Taiwan may be minimal. Second, some of the investments have produced sales abroad after investing in China, resulting in returns to the original Taiwan investors. Finally, some investments may have already earned back the original payback-period payoff. Thus, the total amount of investment from Taiwan may have been reduced. Alternatively, some investment risks have been properly accounted for. Exchange rate risk, political risk, and market risk are always present in any foreign investment, which are not easy to quantify.

IV. ECONOMIC RELATIONS BETWEEN TAIWAN AND THE U.S.

Taiwan is an export-oriented economy whose its growth rate depends on external demands for its goods. The largest market for Taiwanese goods is the U.S. because of its high purchasing power and market size.

Table 6 displays the trade relationship between Taiwan and the U.S. Since 1990, the total trade (exports and imports) of Taiwan with the U.S. has been increasing. In 2000, Taiwan's total trade with U.S. was more than 40 percent of Taiwan's GDP, implying its heavy dependence on the U.S. market. When the trade figure with China is added, the trading volume with the two countries represents about 50 percent of Taiwan's GDP.

In addition to trade, U.S. companies have invested heavily in Taiwan's economy for the past several years. U.S. foreign direct investments (FDI) in Taiwan have risen from US$ 3.78 billion in 1994 to US$ 6.86 billion in 1999. At the same time, Taiwan companies also have substantial direct investments in the U.S. In 1999, the total Taiwan FDI in the U.S. was about US$ 2.98 billion. Several Taiwan companies have in fact raised equity on the New York Stock Exchange and in the over-the-counter market.

V. ECONOMIC RELATIONS BETWEEN CHINA AND THE U.S.

Trade between China and the U.S. was basically non-existent from 1949 to 1978 because of the isolation policy pursued by China. Since Deng Xiaoping's open-door policy in 1978, trade relationships between the two countries have started to develop. Trade has been increasing on both sides for the past two decades. Yet, there are many trade disputes between the two parties, typically centered around intellectual property rights, market access, and terms for entry into the World Trade Organization (WTO) [see Janow (1998)].

It seems clear that China has gradually opened up its market to foreign investors and is constantly reducing barriers to entry. Further improved conditions will be seen with China's entry into the WTO and as more foreign financial institutions and information technology industries can compete on an equal footing with the Chinese companies.

Table 6
Taiwan trade

Panel A: Taiwan-U.S. trade and FDI, 1990-2000 (Unit: US$ Billion)

Year	Taiwan Export		Taiwan Import		Balance	FDI US->Taiwan		FDI Taiwan-->US	
		(%TW GDP)		(%TW GDP)			%TW GDP		% TW GDP
1990	22.67	14.15	11.49	7.17	11.18				
1991	23.02	12.83	13.18	7.35	9.84				
1992	24.60	11.59	15.25	7.19	9.35				
1993	25.10	11.19	16.17	7.21	8.93				
1994	26.71	10.93	17.11	7.00	9.60	3.78	1.55		
1995	28.97	10.94	19.29	7.28	9.68	4.29	1.62	2.14	0.81
1996	29.91	10.70	18.46	6.60	11.45	4.48	1.60	2.13	0.76
1997	32.63	11.24	20.37	7.02	12.26	5.01	1.73	2.84	0.98
1998	33.12	12.39	18.16	6.79	14.96	6.26	2.34	3.14	1.17
1999	35.20	12.22	19.13	6.64	16.07	6.86	2.38	2.98	1.03
2000	40.51	25.29	24.38	15.22	16.13				

Source: U.S. Department of Commerce (2001).

Panel B: Taiwan's top ten trading partners in 2000

Country	Rank	% of Total Trade
United States	1	20.79
Japan	2	19.13
Hong Kong	3	11.62
South Korea	4	4.47
Singapore	5	3.63
China	6	3.62
Germany	7	3.62
Malaysia	8	3.1
Netherlands	9	2.44
Philippines	10	2.30

Source: Board of Foreign Trade (Taiwan), http://cus.moeaboft.gov.tw/

Table 7, Panel A, displays U.S trade statistics for the years 1990-2000. Exports represent about 10.72 percent of GDP, while total trade (exports and imports) is about 25.16 percent of GDP in 2000. These ratios are relatively lower compared to those of China and Taiwan, suggesting that the strength of the U.S. economy lies largely in domestic consumption and investment.

The trade component as a percentage of U.S. GDP has increased substantially for the past years, however (i.e., trade/GDP is 15.32 percent in 1990 vs. 25.16 percent in 2000), implying the increasing importance of the U.S. trade sector. In 2000, the U.S. trade deficit for all countries combined is US$ 369.69 billion, which appears to be large in nominal terms. Given the size of the U.S. economy, though, this is only 3.7 percent of its GDP, a relative small component of its entire economy.

Table 7
U.S. trade statistics

Panel A: U.S. trade, 1990-2000 (US$ billion)

Year	GDP	Total Trade		Export		Trade Deficit	
			% of GDP		% of GDP		% of GDP
1990	5,803.20	888.90	15.32	393.59	6.78	101.72	1.75
1991	5,986.20	908.86	15.18	421.73	7.05	65.40	1.09
1992	6,318.90	1,273.35	20.15	616.92	9.76	38.69	0.61
1993	6,642.30	1,358.70	20.46	641.68	9.66	72.30	1.09
1994	7,054.30	1,508.58	21.39	698.30	9.90	100.91	1.43
1995	7,400.50	1,691.19	22.85	795.65	10.75	99.89	1.35
1996	7,813.20	1,803.93	23.09	850.78	10.89	104.32	1.34
1997	8,318.40	1,981.81	23.82	937.59	11.27	104.73	1.26
1998	8,790.20	2,032.86	23.13	932.98	10.61	166.90	1.90
1999	9,299.20	2,177.45	23.42	956.24	10.28	264.97	2.85
2000	9,963.10	2,506.49	25.16	1,068.40	10.72	369.69	3.71

Source: US Department of Commerce (2001), http://www.doc.gov

Panel B: U.S. top ten trading partners in 2000

Country Name	US$ Billion	% of U.S. GDP
Canada	405.64	4.07
Mexico	247.63	2.49
Japan	211.83	2.13
China	116.32	1.17
Germany	87.98	0.88
United Kingdom	85.04	0.85
South Korea	68.20	0.68
Taiwan	64.89	0.65
France	50.04	0.51
Singapore	37.00	0.37

Source: U.S. Department of Commerce (2001).

Table 7, Panel B, reports the ranking of countries that trade with the U.S. Neighboring countries, Canada and Mexico are still the leading trading partners. China and Taiwan are the fourth and the eighth largest trading partners of the U.S., respectively, suggesting their importance in U.S. trade transactions.

The trading figure in Table 7 for China is somewhat different from that in Table 1, Panel B for several reasons. The trade figure in Table 1 was recorded according to China's Customs by country of origin while the data in Table 7 represent goods and services recorded by the U.S. government. In addition, the U.S. government also treats some U.S.-Hong Kong trade flows as a part of China-U.S. trade.

International trade with China and Taiwan represents only 1.17 percent and 0.65 percent of U.S. GDP, a small fraction of the U.S. economy. These results further imply that any change in U.S. trade policy will have a substantial impact on both China and Taiwan. Maintaining good relations in the U.S.-Taiwan-China triangle is assuredly more critical to China and Taiwan because the U.S. is a large trading partner to them, while the U.S.-Taiwan-China trade figure represents a tiny percentage of trading to the U.S.

Table 8 provides trade and foreign direct investments data between China and the U.S. The amount of exports and imports has been on the rise since 1985. In 2000, the amount totals to US$ 116.31 billion, which is about 10.83 percent of China's GDP. Thus, the U.S. represents an important trading partner to China.

The leading types of U.S. exports to China include power generation equipment, air and spacecraft, electrical machinery and equipment, fertilizer, medical equipment, plastics and articles, oilseeds, paper and paperboard, and organic chemicals. China's leading exports to the U.S. are electrical machinery and equipment, toys and games, footwear and parts, apparel, furniture, leather and travel goods, plastics products, medical instruments, and iron and steel.

Although Chinese company investment in the U.S. started in 1996, the amount of investment in recent years is still relatively small. On the other hand, U.S. foreign direct investments in China are on the rise. U.S. companies invest in China primarily in three different forms: joint ventures, licensing, and wholly owned subsidiaries. Given the flexibility of the wholly owned subsidiary structure, it is likely that many joint ventures have been converted into subsidiaries in recent years.

The large trade deficit between China and the U.S. in recent years has received severe criticism from labor groups in the U.S., who suggest job displacement of U.S. workers with the import of foreign products. The trade deficit between China and the U.S. is about US$ 83.81 billion in 2000. At the same time, one should note that U.S. economy in recent years has enjoyed relatively low inflation, due in part to inexpensive but valued imports from China and other countries.

The increasing China-U.S. trade deficit raises the concern that trade issues for the U.S. and China will be similar to those experienced between Japan and the U.S., and result in intense competition between the two countries. This issue is worth some consideration. In economic trade theory, if two countries are producing similar products, oligopolistical power and a strong industrial structure in one country will help that country's market share of the products while hurting the other one. For example, Japanese firms are exporting cars and electronic products, which are also produced in the U.S. It can be argued that U.S. firms will be hurt, given Japanese market power in exporting these goods.

Table 8
China-U.S. trade and FDI 1985-2000 (US$ billion**)**

Year	China Export	(%PRC's GDP)	China Import	(%PRC's GDP)	Balance	FDI US->China	%PRC's GDP	FDI China-->US	%PRC's GDP
1985	3.86	1.27	3.86	1.26	0.06	0.357	0.117		
1986	4.77	1.70	3.11	1.11	1.66	0.315	0.112		
1987	6.29	2.07	3.50	1.15	2.79	0.263	0.087		
1988	8.51	2.25	5.02	1.33	3.49	0.236	0.062		
1989	11.98	2.82	5.76	1.36	6.23	0.284	0.067		
1990	15.24	3.93	4.81	1.24	10.40	0.456	0.118		
1991	18.97	5.00	6.28	1.66	12.70	0.323	0.085		
1992	25.73	5.91	7.42	1.70	18.30	0.511	0.117		
1993	31.54	5.26	8.76	1.46	22.80	2.063	0.344		
1994	38.79	7.17	9.28	1.72	29.50	2.491	0.461		
1995	45.54	6.53	11.75	1.68	33.80	3.083	0.442	0.329	0.047
1996	51.51	6.32	11.99	1.47	39.50	3.444	0.422	0.197	0.024
1997	62.56	7.03	12.86	1.44	49.70	3.239	0.364	0.175	0.020
1998	71.17	7.46	14.24	1.49	56.90	3.898	0.409	0.253	0.027
1999	81.79	8.20	13.11	1.31	68.70	4.216	0.423	0.339	0.034
2000	100.06	9.32	16.25	1.51	83.81	4.384	0.406		

Source: China GDP (1985-1995) from Huang (1998)
China GDP (1996-2000) U.S. Department of Commerce.
China-U.S. trade data U.S. Department of Commerce.
http://www.census.gov/foreign-trade/balance/c5700.html.
China FDI (1985-1997) U.S. Department of Commerce.
China FDI (1998-1999) MOFTEC.

In the case of trade between the U.S.-China, the implication is quite different. According to trade theory, if two countries are specialized in producing goods to their comparative advantage, both parities will benefit. China's exports to the U.S. are primarily shoe wear, textile products, and toys, which require materials and labor-intensive processes. These products are not directly competing with those produced by U.S. industries. From a theoretical point of view, U.S. wages and thus the living standards of workers will not be adversely affected by Chinese imported products of this sort. As a result, the impact of the Chinese trade deficit is quite different from the impact of the Japanese-U.S. trade deficit.

It seems clear that both U.S. and Chinese governments should in fact encourage these trade flows rather than opposing them, as they are beneficial to both countries.

One final comment about the U.S.-China trade is in order. As Table 8 indicates, the U.S. trade deficit has increased in recent years. In 2000, the trade deficit with China amounts to US$ 83.81 billion. In fact, this figure is misleading because over 45 percent of the China's exports to the U.S. are produced by foreign affiliated companies of the U.S., Taiwan, Japan, and Korea, among others. The value-added component by Chinese companies is small relative to the total export amounts in items labeled as China exports (products). Given the huge amount of foreign direct investments in China dedicated to producing China exports, the U.S.-China trade deficit is somewhat overstated.

Table 8 also indicates a growing amount of foreign investments from the U.S. in China. In 1999, the amount of FDI was reported as US$ 4.22 billion. While some companies may not have obtained profits as expected, it is long-run market share and market potential expected that explains U.S. FDI.

The reported U.S. investments in China are likely to be underestimated, because many U.S. companies invest in China via Hong Kong. The amount is then not reported as FDI in China.

After China's entry into the WTO, Chinese markets will be opened up to U.S. companies in the areas of information technology, financial institutions (banks and insurance), and automobile industries, in which U.S. companies have a competitive advantage. This is why the U.S. companies support China's entry into the WTO.

VI. CONCLUSION

The U.S.-Taiwan-China triangular foreign direct investment and trade patterns have several implications for their economic relationships. First, the growth of both China and Taiwan economies depends critically on the external trade sector because trade is an important component in their GDP. The implication is that policy-makers should rethink policies that aim at diversifying domestic industries so that an economy will not be critically dependent on the trade sector.

Second, the facts that the U.S. has experienced trade deficits and is less dependent on trade for growth do not imply that the U.S. economy is not dependent on its trade flows. The low inflation rate in the U.S. is related to the inexpensive but desirable imports from China and Taiwan. U.S. firms would benefit from capitalizing on their comparative advantages in producing high-value and high-tech goods.

Finally, the economic relationships in the U.S.-Taiwan-China triangle have become more important in recent years. All three economies will be increasingly dependent on stable relations in terms of their overall domestic growth, employment, and inflation. The U.S.-China relation is unlike the U.S-Soviet relation, which basically concerns political matters. The U.S.-China relation primarily concerns economics, and the economic relationship is beneficial to both economies. With the strong backing of

U.S. companies, recognition that there are economic benefits for all sides will help maintain stability of the U.S.-Taiwan-China triangle in the coming years.

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