

BTI 2010 | Taiwan Country Report

Status Index	1-10	9.39	# 3 of 128	
Democracy	1-10	9.50	# 5 of 128	➔
Market Economy	1-10	9.29	# 2 of 128	➔
Management Index	1-10	7.12	# 6 of 128	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Transformation Index (BTI) 2010. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 128 transformation and developing countries are evaluated.

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Key Indicators

Population	mn.	22.9	HDI	-	GDP p.c.	\$	30,911
Pop. growth	% p.a.	0.3	HDI rank of 182	-	Gini Index		34.0
Life expectancy	years	79	UN Education Index	-	Poverty ²	%	-
Urban population	%	-	Gender equality ¹	-	Aid per capita	\$	-

Source: Directorate-General of Budget, Accounting and Statistics, Executive Yuan, R.O.C.

Footnotes: (1) Gender Empowerment Measure (GEM). (2) Percentage of population living on less than \$2 a day.

Executive Summary

Throughout the review period, Taiwan has remained a high performer in terms of institutionalizing democracy and its market economy. However, the global economic meltdown has affected the island republic negatively since the latter half of 2008, and will continue to do so over the coming months. A severe crisis of government emerged during the second Chen Shui-bian administration, which ended in May 2008. This paralyzed the legislative process and further aggravated the political divide between the “pan green” and “pan blue” party camps. The standoff resulted in a crushing defeat of the ruling Democratic Progressive Party (DPP) in the parliamentary and presidential elections in early 2008, giving the Kuomintang (KMT) under Ma Ying-jeou a strong mandate to pursue its pro-integration approach vis-à-vis the People’s Republic of China (PRC).

Notwithstanding the unresolved issue of Taiwan’s eventual political status, the island republic has sustained its accomplishments in political transformation, which have included the establishment of a high degree of stateness, meaningful elections and a sound judicial system, the absence of undemocratic veto actors, stable democratic institutions and a vibrant civil society. Although the persecution of former President Chen, who is accused of corruption and forgery, has led to much resentment among core “pan green” supporters in the aftermath of a disastrous election year for the DPP, neither the stability of the political system nor society’s overall support for it has suffered.

Taiwan’s economy performed well over most of the review period, despite the drop in the GDP growth rate from 5.7% in 2007 to an estimated 1.9% in 2008, due to the consequences of the global financial and economic crisis. However, all pre-crisis indicators suggest that the economy’s fundamentals are strong, and a quick rebound is likely once global markets start recovering. However, Taiwan’s budget will face growing deficits over the coming years, following the government’s passage of an expensive stimulus package. Financial sector reform

has made progress, and Taiwan's banking system is considered healthy by most international observers.

Taiwan's relations with the PRC eased substantially after the KMT came to power in May 2008. A range of important agreements signed in the months thereafter have established direct trade, transport and communication links and facilitated economic interaction between the two sides, to the benefit of Taiwan's export economy and its further integration in global production chains.

History and Characteristics of Transformation

For many years, political transformation took a backseat to economic transformation in the island republic of Taiwan. The foundations of a sound market economy were laid in the 1950s under the authoritarian leadership of Chiang Kai-shek. During that time, the state intervened with a strong hand in economic affairs, regulating and protecting domestic markets. In the four decades of authoritarian rule following the Chinese Civil War in 1949, Taiwan moved gradually toward a social market economy and established rudimentary social insurance systems. Democratic transition started in 1986 with the illegal foundation of the Democratic Progressive Party (DPP) on September 28th, which was tolerated at the time by the ruling Kuomintang (KMT) regime, and the lifting of martial law on October 15th of that year. More reforms followed, including most importantly the legalization of new political parties in January 1991. In 1991 and 1992, Taiwan saw free elections to its central parliamentary bodies for the first time, respectively to the National Assembly and the Legislative Yuan, thus marking the end of the transition process.

During the rest of the 1990s, democracy matured by means of successive constitutional reforms that, along with other changes to Taiwan's political system, paved the way for the first direct presidential election, held in early 1996. The incumbent president and KMT party chief Lee Teng-hui won this election and became Taiwan's "father of democracy." Successful democratic consolidation had already been achieved when Chen Shui-bian, an experienced DPP politician and former advocate of Taiwanese independence, unexpectedly won the March 2000 presidential election and rendered the KMT an opposition party for the first time since the exile government fled to the island in 1949.

The following four years gave rise to severe legislative inefficiency, due to partisan conflict between the ruling DPP and the KMT-led opposition, which commanded a majority in parliament and paralyzed the political process. Cross-strait relations soured as the new president pursued an agenda focused on assuring Taiwanese sovereignty against Beijing's "one China principle," and pushed for a referendum law and a new constitution during the March 2004 presidential campaign. After the incumbent president secured a narrow re-election victory, with a margin of only 30,000 votes, Taiwan's democracy was hijacked by a legal brawl over the ballot's outcome as well an investigation into an alleged assassination attempt on Chen and his

running mate Annette Lu on the eve of the presidential election. Nor did the December 2004 parliamentary elections overcome the impasse in the legislature, as Chen's ruling DPP and its "green camp" ally, the Taiwan Solidarity Union, failed to achieve an absolute majority. The following four years were shaped by ongoing parliamentary paralysis, rising partisanship as Chen's administration became entangled in corruption scandals, and a frustrated public that seemed to turn away from politics. However, political institutions proved strong enough to withstand the rough-and-tumble character of the second Chen administration.

After a steady, months-long downturn in its legitimacy and public appeal, the ruling DPP suffered a crushing defeat in the January 2008 parliamentary elections, followed by an even more disastrous outcome in the March presidential elections. The KMT gained a two-thirds majority in the Legislative Yuan, and its presidential candidate Ma Ying-jeou drove home an overwhelming victory against DPP counterpart Hsieh Chang-ting. Under the new KMT government, cross-strait relations eased substantially. Semiofficial Sino-Taiwanese negotiations were brought back on track, and new deals were struck between both sides that paved the way for direct transportation, commercial links and more political interaction in the future. At the beginning of 2009, the KMT administration could look back to a successful year, enjoying a sound public mandate and facing a depressed DPP in the midst of reinventing itself as an opposition party.

Transformation Status

I. Democracy

1 | Stateness

Although Taiwan's status under international law is contested, the Taiwanese state (officially named Republic of China) enjoys effective power and authority over its territory, including the islands of Taiwan, Penghu, Matsu and Kinmen. The state's monopoly on the use of force is thus not challenged.

Monopoly on the use of force

Though the domestic conflict over Taiwan's political future as an independent nation-state or as part of a new and unified China is yet to be resolved, the Republic of China's claim to unconditioned sovereignty is indisputable and fully legitimate among the islander population. The large majority of Taiwanese support the status quo in the Taiwan Strait, which they think best serves their security interests. Most studies show that Taiwanese national identity has been continually strengthening since the early 1990s, thus deepening the people's identification with their state and their desire for sovereignty. No groups are excluded from the political nation or political citizenship.

State identity

In Taiwan, state legitimacy is fully derived from a secular constitution. Religious dogmas play no role.

No interference of religious dogmas

Taiwan's civilian administration is generally sound and functional, though the second Democratic Progressive Party (DPP) administration was shaken by a number of serious cases of corruption. On various occasions while in opposition, the KMT accused Taiwan's courts of being too closely allied with the government. Since the KMT takeover in May 2008, it has been the DPP claiming that the legal system is manipulated by the new power-holders. However, these accusations remain unconvincing and are obviously linked to political maneuvering. The state administration does satisfactorily fulfill its functions, and persecution of political corruption is stern.

Basic administration

2 | Political Participation

There are no restraints on elections in Taiwan, which are usually fair and undisputed. Although the 2004 presidential ballot saw the opposition “blue camp” accuse the incumbent president and his party of fraud, these accusations could not be substantiated and were finally dismissed by the courts. The latest parliamentary and presidential elections in early 2008, which were once again hotly contested and accompanied by large-scale mass rallies, went smoothly. The significance of vote buying in local elections has declined over the years, though the practice continues.

Free and fair elections

All elected rulers have effective power to govern, and there are no veto powers or exclusive political domains that might negatively affect democratic participation. The Taiwanese military no longer plays an active role in domestic politics, as there are no active military officers in the civilian government and the military no longer administers internal security. The close connections between the armed forces and the Kuomintang (KMT) throughout the authoritarian era weakened steadily after democratic transition in 1986 – 1987, and were effectively cut when the DPP took over Taiwan’s government in 2000. The implementation of the National Defense Act in 2002 strengthened the institutions allowing for effective democratic control over the security sector, and there has been no case of active military involvement in Taiwan’s domestic politics for many years.

Effective power to govern

Freedom of association and freedom of assembly are unrestricted. Union activities remain constrained by law, but independent union organization has become more viable over the years. Since the founding of the Taiwan Confederation of Trade Unions in 1997, the island’s labor movement has gained much momentum and has successfully pushed for more rights and better financial compensation for workers.

Association / assembly rights

Freedom of opinion and freedom of the press are unrestricted, as confirmed by the 2008 Worldwide Press Freedom Index (released by the Paris-based Reporters Without Borders), in which Taiwan ranked 36th worldwide. According to Freedom House’s latest Freedom of the Press reports, Taiwan’s media environment has been ranked the freest in East Asia for two consecutive years. Press freedom benefits from robust constitutional and legal safeguards of the freedom of speech and the press, and a highly diverse and competitive media structure. At the end of 2007, Taiwan had 2,216 newspapers (with some 30 published regularly), 175 radio stations, five terrestrial TV companies, 66 cable TV companies (including four cable TV program transmission systems), and 155 satellite broadcasting channels. Government and party investment in privately operated radio and television companies was prohibited in 2003. A legally independent National Communications Commission (under the Executive Yuan), tasked with regulating and overseeing the broadcast media, was approved in 2005 and started working in 2006. There are no restrictions on the use of the Internet, which is currently

Freedom of expression

accessible to 71% of all Taiwanese households. Foreign media have free access to Taiwan and can work without restrictions, with the only exception being mainland Chinese journalists who, for security reasons, still face bureaucratic hurdles in winning permission to report from Taiwan.

3 | Rule of Law

The separation of powers into executive, legislative and judicial branches is well established, and there are no constraints on their basic functions. However, the current government system suffers from an inconsistent constitutional relationship between the president and the parliament; while the popularly elected president appoints the head of the Executive Yuan (the premier) without the consent of parliament (the Legislative Yuan), the latter has the authority to dismiss the cabinet by means of a vote of no confidence on the premier. Since the president can dissolve the legislature in such a case, parliamentary powers to effectively control the government are limited. There are almost no institutional guards against political stalemate when a minority government is in power. Combined with highly competitive behavior, the zero-sum approach of Taiwan's political camps contributed to great institutional deadlock during the DPP era. On the other hand, the separation of powers may be negatively affected by the dominance of one political party in the legislature and the presidential office, since the opposition is excluded from any political decision-making role concerning the appointment of the members of other constitutional bodies. Some traditional parliamentary powers are held by the Control Yuan, a constitutional body responsible for budgetary auditing and the investigation of government officials. Members of the Control Yuan are appointed by the president with the consent of the legislature. Due to political stalemate, the Control Yuan was inoperative between 2005 and 2008. After the KMT's straight victory in both the 2008 parliamentary and presidential elections, Taiwan's system of government has returned to quiet waters, though its structural defects have not thus far been tackled and constitutional reform is not an issue on any political party's current agenda.

Separation of powers

Judicial independence is well established in Taiwan. Political influence over the nomination of Supreme Court judges, judicial proceedings and court decisions was claimed by the KMT opposition during the Chen Shui-bian era and has been repeatedly alleged by the DPP since the May 2008 KMT takeover, but has not been convincingly substantiated.

Independent judiciary

Political corruption receives a great deal of attention in the mass media and is prosecuted rigorously under criminal law. However, members of parliament, cabinet members and members of county and city parliaments enjoy immunity, which often becomes an issue in domestic policy debates due to widespread corruption charges against public officials on all administrative levels.

Prosecution of office abuse

Civil rights are well-guaranteed and protected, and those who violate them are taken to court. The judicial system provides ample opportunities to seek redress for rights violations, and Taiwan enjoys a good human rights record according to all relevant international observer groups. Though improvement is still possible with respect to protecting the civil rights of Taiwan's growing community of foreign workers, recent amendments to the Immigration Act have strengthened this group's legal position considerably.

Civil rights

4 | Stability of Democratic Institutions

As a rule, all institutions work according to fixed procedures and are sufficiently controlled by a working system of mutual checks and balances. However, institutional efficiency was hampered by the confrontation between the DPP-led minority government and the KMT-led opposition majority in the Legislative Yuan during the 2000 – 2008 time period. Similarly, political gridlock stalled the operations of the Control Yuan after 2005, as the KMT opposition in parliament summarily rejected presidential nominations for Control Yuan members.

Performance of democratic institutions

All relevant political actors accept democratic institutions as legitimate. However, due to the island's history and the ideological polarization on the issues of Taiwanese independence and national identity, politics in Taiwan is still widely seen as a zero-sum game. Consequently, there is no embedded culture of compromise and cooperation that might help overcome institutional deadlocks when Taiwan is ruled by a minority government.

Commitment to democratic institutions

5 | Political and Social Integration

Taiwan has a stable, moderate and socially anchored party system, which enjoys broad popular consent. However, this system is polarized, as the two opposing party alliances (the "blue camp" comprised of the KMT, the People First Party (PFP) and the New Party (NP); and the "green camp" of the DPP and the Taiwan Solidarity Union (TSU)) take uncompromising stances on the issues of national identity, unification (with China) vs. (Taiwanese) independence, and cross-strait policy. On the other hand, the party system is responsive to the populace's diverging opinions on these matters and aggregates societal interests fairly well. In addition, the two party camps do not diverge very much when it comes to other policy fields such as anti-corruption, environmental protection, social welfare and industrial development. Finally, the party landscape's ideological cleavage may soon narrow substantially, as a new electoral law has been installed that does away with the old single non-transferable vote (SNTV) system in favor of a parallel system of mixed proportional and plurality representation. It is widely assumed that the new electoral rules will force the mainstream parties to soften their stances in order to attract more voters of the central moderate majority.

Party system

The nation's network of interest groups is close-knit, politically influential and operates independently of the state. Problems remain concerning the impact of one-issue groups and their horizontal integration, as well as the establishment of umbrella organizations to make Taiwan's numerous interest groups more effective. In addition, many interest groups, especially those leaning towards the DPP, have suffered from a loss of leaders who have gone into politics and who no longer take their group's objectives as their primary concern. Finally, Taiwan's civil society is still very much focused on ideological issues related to the unification-independence and national identity divides, and there remains too little private engagement in terms of charity and volunteerism.

Interest groups

Voter turnout, which usually lies between 60% and 80% for national and local elections, suggests rather strong citizen consent to democracy. Public frustration with government efficiency rose strongly during the second Chen administration (2004 – 2008), due to institutional deadlock caused by the DPP's polarizing Taiwanization policies and deteriorating Sino-Taiwanese relations. This frustration raised concerns among some domestic and international observers that consent to democratic norms might weaken in Taiwan. However, the situation has substantially eased since the May 2008 KMT takeover, and evidently did not detract from the people's still-strong commitment to democracy and the constitutional order.

Consent to democratic norms

Social self-organization has gained momentum since the democratic transition. Taiwan's middle-class social movements, though not decisive in the transition itself, played an important part in the process of democratic consolidation thereafter. Today, they do a good job in defending the public's many interests, supporting non-violence, tolerance and a democratic culture. Taiwan's civil society is not, in stark contrast to the party system, defined along ethnic or other cleavages, and it does its fair share to generate interpersonal trust, which is high among the populace according to most studies.

Associational activities

II. Market Economy

6 | Level of Socioeconomic Development

The country's level of socioeconomic development permits adequate freedom of choice for all citizens. Fundamental social exclusion due to poverty is qualitatively minor and is not structurally embedded. Income distribution, as measured by the Gini coefficient, is relatively equal and has slightly improved in recent years (2002:

Socioeconomic barriers

0.345; 2004: 0.338; 2007: 0.340). Among the countries in Asia and Oceania, Taiwan ranked first above both Singapore and South Korea, according to the 2007 – 2008 Human Development Index, calculated by the national statistical office (since Taiwan is not a U.N. member state).

Economic indicators		2004	2005	2006	2007
GDP	\$ mn.	331,007	355,958	366,357	384,768
Growth of GDP	%	6.2	4.2	4.8	5.7
Inflation (CPI)	%	1.6	2.3	0.6	1.8
Unemployment	%	4.4	4.1	3.9	3.9
Foreign direct investment	% of GDP	-	-	-	12.6
Export growth	%	21.2	8.8	12.9	10.1
Import growth	%	31.8	8.2	11.0	8.2
Current account balance	\$ mn.	19,728	17,578	26,300	32,975
Public debt	\$ mn.	-	-	-	-
External debt	\$ mn.	-	-	-	-
Total debt service	% of GNI	-	-	-	-
Cash surplus or deficit	% of GDP	-2.9	-0.6	-0.3	-0.4
Tax Revenue	% of GDP	17.9	19.6	19.7	19.7
Government consumption	% of GDP	-	-	-	-
Public expnd. on edu.	% of GDP	6.0	6.0	5.7	6.1
Public expnd. on health	% of GDP	6.0	6.0	6.0	-
R&D expenditure	% of GDP	2.4	2.5	2.6	2.6
Military expenditure	% of GDP	2.2	2.2	2.0	2.0

Sources: Ministry of Finance, R.O.C. | Directorate-General of Budget, Accounting & Statistics, R.O.C. | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security

7 | Organization of the Market and Competition

Taiwan's market economy is institutionally sound, with clearly defined and state-guaranteed rules for ensuring fair competition and largely equal opportunities for all market participants. It ranked 13th of 55 countries in the Switzerland-based International Institute for Management Development's 2008 World Competitive Yearbook, moving up five places from the year before. The report lauded Taiwan's economy for good government practices, business efficiency and high-quality infrastructure. In 2007, the Fair Trade Commission (a ministerial-level body) initialized a three-year plan to examine existing government regulations, aimed at enhancing competition. Market actors face neither entry nor exit barriers, though restrictions still exist on investments in and the transfer of technology to mainland China, hampering private entrepreneurialism to some extent. Also, there are restrictions on Chinese investors (both institutional and private) in Taiwan for political reasons.

Market-based competition

Compliance with the WTO regime, to which Taiwan gained access in January 2002, forced the island republic to abandon its last monopoly on tobacco and wine products, to reduce the majority of its tariffs on imported products to zero, and to substantially liberalize its trade with mainland China. The Fair Trade Law that took effect in 2002 ensures a coherent and effective approach to combating monopolies.

Anti-monopoly policy

With the exception of cross-strait economic relations, the state refrains from intervening in foreign trade. Intervention takes place mainly for security reasons and in order to control the level of Taiwan's trade and investment dependency on China. Some 40% of Taiwan's exports and 70% of its outbound investment now go to the Chinese mainland. Trade across the Taiwan Strait has intensified steadily over the last years. Since the KMT took over power from the DPP in May 2008, direct trade, transport and communication links between Taiwan and the mainland have been established for the first time, paving the way for more economic interaction and more competition in the Taiwanese market in the future.

Liberalization of foreign trade

The banking system has traditionally been a sore spot in Taiwan's otherwise high-performing economy. The situation improved during the review period, however. The ratio of non-performing loans has steadily declined (in December 2007 falling to just 1.8% of the total lending of domestic banks). The banking sector's external debt obligations are low, and several of Taiwan's leading commercial banks enjoy implicit state guarantees, as they are government-controlled. Consequently, the risk of potential losses related to bad loans has been reduced. Local banks have relatively low exposure to the U.S. subprime mortgage crisis as compared with banks in other Asian countries such as Japan. Consequently, their risk of having to raise funds in the market in order to recapitalize their balance sheets is limited. Meanwhile, the expanding role of foreign financial institutions in the local banking

Banking system

sector –Taiwan had 32 foreign-controlled banks in 2007 – has helped to improve confidence in the system, as opening the banking sector to foreign capital will intensify healthy competition between local lenders and international players. In 2007, Taiwan's Financial Supervisory Commission amended its regulations to allow financial holding companies' overseas banking subsidiaries to invest in mainland banks, and eased restrictions on mainland investments and operations of local banks. This will certainly push internationalization and thus benefit the island's banking and credit sector. Newly elected President Ma Ying-jeou has pledged to further open Taiwan's financial market for international investors, with the aim of making the island a first-class financial service hub comparable to Hong Kong or Singapore. In line with these policies, Taiwan abolished all restrictions on foreign ownership of Taiwanese securities in October 2008. Moreover, the financial restructuring that began in the late 1990s with the aim of curtailing an overcrowded and fragmented banking and credit sector has made some progress. Through mergers and acquisitions, the number of domestic banks decreased from 52 in 2002 to 39 in 2007. However, there were still more than 300 rural credit cooperatives (261 credit departments attached to farmers' associations and 25 to fishermen's associations) by the end of 2007, making the local financial sector still lack transparency and appear susceptible to political deals, especially to the benefit of the KMT.

All in all, Taiwan's banking system enjoys high capital levels, reasonable liquidity and an increasingly efficient regulatory environment, combined with a trend for more domestic mergers, competition and internationalization. It is deemed by most international analysts to present very low risk.

8 | Currency and Price Stability

Taiwan's foreign exchange policy has been consistently linked to the goal of financial and economic stability. This had generated solid foreign exchange reserves of \$297.7 billion by the end of 2007, the fifth-largest such sum in the world (by January 2009, this total had fallen somewhat to \$292.7 billion). Consistent with the price stability of recent years, Taiwan experienced low to moderate inflation levels during the review period, with consumer prices rising 1.8% and 3.6% respectively in 2007 and 2008, the latest increase stemming mainly from rising crude oil and other commodity prices, as well as agricultural losses caused by typhoons. The new Taiwan dollar came under slight upward pressure against the U.S. dollar during the review period, mainly because of a deteriorating climate in international commerce and trade. However, Taiwan's inflation and foreign exchange policies are soundly steered by an independent central bank and are carefully brought into concert with other economic policies.

Anti-inflation /
forex policy

Taiwan's total central government debt stood at 27.9% of GDP at the end of 2007 (estimated 2008 figure: 28.2%). The debt ratio is bound to rise over the next several years, as the government has implemented a stimulus package designed to combat the effects of the global economic crisis. At the same time, government policy is subject to the strict scrutiny of a central bank that enjoys a reputation for sound monetary supervision and control. As cross-strait economic integration is likely to intensify over the coming years, Taiwan's economy is expected to grow healthily, reducing public debt and budget deficit figures to manageable levels.

Macrostability

9 | Private Property

Taiwan's property rights regime is well established and properly overseen by government authorities.

Property rights

Taiwan's economy is mainly based on small and medium-sized private companies (a group that includes around 90% of the nation's companies), which are adequately protected by the state. The privatization process for Taiwan's numerous state-owned enterprises (SOEs) was initiated in 1989, when the Executive Yuan established a "Task Force for the Implementation of the Privatization of National Corporations." A large number of major SOEs have since been privatized, including China Steel, Taiwan Motor Transport Company, China Airlines, Chunghwa Telecom and three major banks. However, the process has slowed in recent years due to trade union resistance (as in the case of Taiwan Tobacco and Liquor), low profitability and a lack of willing investors (e.g., in the case of ship manufacturer CSBC). However, privatization does follow market principles, and most criticism has been directed at the government's inability to privatize its SOEs quickly enough, rather than at any ostensible attempt by the authorities to build up state oligopolies.

Private enterprise

10 | Welfare Regime

Taiwan's welfare regime provides for substantial protection against poverty and other social risks. Compulsory national health insurance (NHI) was introduced in 1995 and covers a wide range of medical treatments for all employed citizens. In 2007, more than 22.6 million people, or 99% of the population, were enrolled in the NHI program. Revenue is collected from monthly salaries. Private-enterprise employees have to pay 30% of the premium, employers 60% and the government 10%. National health expenditure stood at 6.1% of GDP at the end of 2006. Taiwan's NHI is rated as one of the best schemes in Asia, though it still faces financial problems due to inflationary drug pricing and rising costs for medical procurement. Comprehensive farmers' health insurance was introduced in late 2002. This scheme has closed a serious gap within the national health insurance

Social safety nets

system, which did not include farmers when it was introduced. Meanwhile, the scheme has been integrated into NHI.

Recent revisions to labor laws which took effect on 1 January 2009 enable workers to receive a regular monthly pension after retiring. Instead of receiving a lump-sum payment upon retirement as before, retirees will now receive a stream of annuity payments. The eligibility age is currently 60, and will remain so until 2017, after which it will gradually increase to 65 in 2026.

A compulsory national unemployment insurance scheme under the Labor Insurance Act, combined with a vocational training and employment service system, took effect in January 2003 and was revised in August 2008. It covers all employees with a record of 15 full years of employment and below 60 years of age. Insurance benefits are calculated on the basis of the number of months an employee has joined the scheme. Insured persons can also claim disability benefits spelled out in the Labor Insurance Act. Moreover, Taiwan has legislation governing monthly minimum wages.

Women's rights have been strengthened over recent years. Most notably, the Women's Policy guidelines (issued by the government-level Commission on Women's Rights Promotion in January 2004), the Gender Equality in Employment Act (March 2002) and the Sexual Harassment Prevention Act (February 2006) have promoted women's rights and gender equality, lifting the social status of women to one of the highest levels in Asia, as calculated by the U.N.-developed Gender Empowerment Measure.

Equal opportunity

Foreign spouses of Taiwanese from middle- and low-income families – mainly coming from mainland China and Southeast Asia – are supported financially by the government and offered free language training and a variety of educational programs. The government also approved changes to the enforcement rules of several immigration-related statutes in November 2008, making it easier for foreign spouses to apply for Taiwanese citizenship or permanent residency.

Concerning Taiwan's indigenous peoples, who account for about 2% of the total population, a number of specific social welfare programs and affirmative-action measures have been implemented over the last years. These include low-interest housing loans and home rental subsidies in urban areas for middle- and low-income indigenous families, privileged access to senior high schools, universities and Taiwan's civil service, and state protection of indigenous language and culture. The government has also, on the basis of the Indigenous Peoples Employment Rights Protection Act, taken measures to reduce this group's unemployment rate, granted a living allowance to indigenous senior citizens, boosted indigenous community health services, subsidized indigenous people's health insurance premiums, and secured their right to medical treatment. The social gap between these native groups

and the Taiwanese Han majority has thus narrowed over the last 10 – 15 years, but economic and social inequality is still striking.

The rights and interests of the disabled are protected. It is required by law that disabled persons make up at least 1% of the workforce at private enterprises with 67 or more employees and at least 3% of the workforce at government offices, public schools and public enterprises with 34 or more employees.

11 | Economic Performance

In spite of difficult political circumstances caused by the deadlock in the legislature and the considerable polarization in Taiwan's party system, the economy did well over most of the review period. GDP growth was 5.7% in 2007, but is projected to fall to 1.9% in 2008 due to the global economic meltdown. However, the economy is expected to grow moderately again by 2.1% in 2009. Export growth was healthy (11.8% in 2007) and remained in double digits until August 2008, when the crisis hit with full force. Exports plunged a record 42% in December 2008 as compared to the previous year, although the whole of 2008 still posted a 3.6% gain. The island republic's overall trade surplus stood at \$27.4 billion at the end of 2007, but fell to \$14.8 billion over the whole of 2008 and to just \$1.8 billion in December 2008. Barring the crisis, which was not homemade, Taiwan would once again have been a high-performing export economy by international comparison.

Output strength

This performance is underlined by continuous growth in foreign direct investment since 2002 (totaling \$11.1 billion in 2007, a 50% increase from 2006), placing Taiwan at 29th in the world, and number six in the region, behind Hong Kong, mainland China, South Korea, India and Singapore. Unemployment has been in constant decline over years (reaching 3.9% in 2007), rising slightly to an estimated 4.1% in 2008 (forecasts for 2009 are far more pessimistic, however). In recent years, tax revenues have been rising thanks to growing business profits, a strong stock market and the closure of tax loopholes. In 2007, revenues totaled 13.7 % of GDP, rising to 14.2% in 2008. Taiwan faced an overall budgetary deficit of 0.2% in 2007 and 1.9% in 2008, which does not appear too worrisome.

Subtracting out the impact of the global crisis originating in the United States, Taiwan's economy remains one of the strongest performers in Asia and worldwide. However, the current meltdown represents a big challenge for the island, especially if it strongly affects China, Taiwan's major export market and target for investment.

12 | Sustainability

Environmental awareness has been on the rise in Taiwan since the 1980s, mainly because of a strong social movement that pushed the government to make environmental protection a major concern in economic policy and planning. Today, environmental protection is institutionally integrated at the government level, both independently (through the Environmental Protection Administration or EPA, a central-government agency) and at the sub-divisional level within various government entities. This results in systematic environmental policy planning and a relatively low externalization of costs over the years.

Environmental
policy

Taiwan has a very well-developed education system with high-quality secondary and tertiary education and vocational training, reflecting the importance given to education in a society still heavily imbued with Confucian values. In 2007, gross enrollment in higher education stood at 85.3%. School curricula undergo continuous reform to keep the education system in line with international developments. Education has accounted for well over 19% of all government expenditure since 2005 (19.2% in 2007). This corresponds to an average of 3.8% of GDP per year between 2005 and 2007.

Education policy /
R&D

The Taiwanese government strongly supports research and development (R&D) in science and technology, as can be seen from the National Science and Technology Development Plan (2005 – 2008). The government wants to raise R&D spending to 3% of GDP, and seems well on its way to achieving this goal. In 2006 (the latest available figure), R&D expenditure grew 9.3% over its 2005 level, amounting to TWD 307 billion (\$9.5 billion), or the equivalent of 2.5% of GDP. Taiwan ranked 4th in the number of U.S. patents granted to its nationals in 2007, with 6,128 utility patents and 1,355 design patents.

Transformation Management

I. Level of Difficulty

Taiwan enjoys few structural constraints on governance thanks to the following factors: a high level of socioeconomic development; a sound market economy and good economic performance; a well-developed education system and research environment; a decent public health system; a well-qualified labor force; a capable bureaucratic apparatus; low social disparities in terms of income and status; a lack of serious ethno-religious conflicts; and an unchallenged state monopoly on the use of force. Social movements and social interest organizations of all sorts are firmly embedded within society and play an essential part in the daily exercise of democracy. The most serious impediment to governance stems from the country's diplomatic status and the contested nature of its sovereignty.

Structural
constraints

In light of Taiwan's long spell of authoritarian rule, there are only weak traditions of civic engagement, but social movements played a major role before and after the transition to democracy in the mid-1980s, and have contributed substantially to democratic consolidation. Today, Taiwan has one of the most vibrant – though small in absolute size – civil societies in Asia, characterized by numerous NGOs engaged in all sorts of public activity, and featuring high degrees of social and institutional trust. Though ideological polarization and division still play a role in Taiwan's civil society when national identity is at stake, recent developments suggest that this issue has lost some of its salience.

Civil society
traditions

The old conflict between “ethnic” mainlanders and Taiwanese over political power has evolved since the early 1990s into a cross-ethnic cleavage among the Taiwanese (and mainlanders) with respect to the island republic's national identity, and concerning the most sensible policy approach to China in order to secure long-term security and prosperity. During the Chen Shui-bian era this resulted in high-level political polarization, limiting the government's institutional efficiency. Undoubtedly, the Chinese claim to Taiwan and the related standoff between pro-independence and pro-integration forces – with the broad majority of the island's populace opting for the so-called status quo – remain the biggest obstacles facing Taiwan against the background of an otherwise positive assessment. However, the inauguration of a new KMT government under President Ma Ying-jeou suggests

Conflict intensity

that by now a solid majority has evolved that is both ready to engage in a more integrative approach towards the mainland and determined to uphold Taiwanese sovereignty. This has mitigated the polarization over cross-strait relations somewhat, though it remains to be seen if Ma's pro-integration course is sustainable.

II. Management Performance

14 | Steering Capability

Given the polarization of Taiwan's domestic political arena and the opposition majority in the legislature, the DPP administration in power until May 2008 found it difficult to carry through most of its legislative initiatives. Taiwan's government system does not provide effective institutional mechanisms to overcome political stalemate caused by a minority government facing a hostile parliamentary majority. Nor has Taiwan's political culture yet developed a sense of party cooperation or even cohabitation to ensure legislative efficiency in times of divided government. Moreover, a series of corruption scandals involving close advisers and relatives of President Chen Shui-bian (and ultimately the president himself) hampered his administration and undermined its legitimacy. Consequently, the steering capability of Chen's government was seriously curtailed. Particularly in Chen's last year in office, important policy measures in the realm of social welfare reform, capital market restructuring and cross-strait economic liberalization could not be implemented. Since the KMT won a two-thirds majority in the Legislative Yuan in January 2008 and secured a sound victory in the presidential elections two months later, the Ma administration now has a free hand to implement whatever policies it deems necessary. This gives the political leadership leeway to set and maintain strategic priorities. But even under conditions of extreme political polarization, with diverging majorities in the legislature and presidential office, there is a strong consensus among Taiwan's political elites that constitutional democracy and the institutions of a socially responsible market economy must not be jeopardized in times of crisis, or by the lingering conflict over Taiwanese independence and cross-strait relations. This consensus prevents government policy from becoming too short-term or election-oriented.

Prioritization

As Taiwan's market economy and democratic order are already well developed, any assessment concerning the implementation efficiency of the government's reform policies starts from an advanced vantage point. This said, the DPP government in

Implementation

charge during most of the review period was unable to realize its most important reform project after 2004 – a constitutional revision. A new constitution, which President Chen wanted to see implemented before the end of his term in 2008, was fiercely opposed by the KMT-led opposition in the legislature, although the need to streamline political structures and clarify the triangular relationship between the president, executive and legislature was widely conceded even in the ranks of the “pan blue” camp. Still, Chen’s obvious attack on the “one China” postulate inherent in the current ROC constitution was unacceptable to the KMT. Since its takeover in May 2008, the KMT government has been able to achieve a turnaround in cross-strait relations by pursuing a pro-integration approach and by implementing a series of policies related to economic liberalization and enhanced social interaction over the Taiwan Strait. As even critics of the KMT’s new approach toward mainland China admit, this has helped to strengthen Taiwan’s export economy, though it has arguably also enhanced the island’s economic dependence on its giant neighbor.

Generally speaking, there has been considerable political learning evident in economic and social policy-making. This is in large part thanks to strong public discourse and the leadership’s close relationships with well-established social organizations and interest groups which push for policy adjustments and new initiatives. The DPP government became increasingly sophisticated and professional in policy-making after taking power in mid-2000. However, it showed little learning or policy innovation in the realms of cross-strait relations or dealings with the “one China” principle, as these remained core issues of DPP ideology. Although economic rationales as well as a great deal of pressure from Taiwan’s business community and the public pointed toward opening up channels of direct trade, transport and communication with the Chinese mainland, the Chen administration clung to a conservative approach to liberalization of cross-strait relations. The new KMT government has substantially modified Taiwan’s approach to China, learning from the DPP’s failure to stabilize cross-strait relations. It has thus strengthened Taiwan’s economy by systematically expanding the island’s position in the mainland market. In the first months after its takeover, the new ruling party pursued a determined agenda of well-sequenced policy measures, which eased Sino-Taiwanese relations and paved the way for more positive interaction between the two sides while at the same time trying to expand Taiwan’s international space. However, it remains to be seen how the Chinese government will respond to this new approach if further initiatives to broaden Taiwan’s international representation encroach on the “one China” principle – and how the KMT government will react if these endeavors eventually fail.

Policy learning

15 | Resource Efficiency

In comparison with most other countries in the Asia-Pacific region, the government makes efficient use of available economic and human resources to pursue its transformation policies and implement further administrative reforms. While the top positions in Taiwan's administrative bodies are filled with political figures who may or may not be experts in their respective fields, the rank and file is recruited according to established rules and qualification levels. Taiwan's Examination Yuan, for example, is a constitutional organ responsible for the education, recruitment and evaluation of the country's public servants. Consequently, Taiwan's public service is professional and non-politicized, although there have been some recent cases of corruption, mostly by mid-level officials, particularly concerning the embezzlement of public funds. However, these cases have been made public by an attentive media and have been effectively dealt with by the responsible authorities and Taiwan's judicial system. For the time being, public debt figures stand at a manageable level, and Taiwan's budget planning is usually transparent and sound. The Council of Organizational Reform, a special organization tasked with driving administrative reform, was established at the government level in May 2002, and has a particular focus on deregulation, decentralization and outsourcing. Taiwan has also made progress in its efforts to set up comprehensive e-government services at all administrative levels.

Efficient use of assets

Since the president nominates the premier without requiring parliamentary consent, and thus can freely install the head of government, there is a relatively high degree of like-mindedness between the presidential and prime ministerial offices. Competing or even opposing interests between the two have rarely been observed in Taiwan's domestic politics. In the Chen Shui-bian era, the DPP caucus in the Legislative Yuan showed considerable loyalty to the president and his government, so that legislative initiatives passed down by the Executive Yuan were usually not contested by that caucus. However, due to a series of corruption scandals involving close associates and members of his family, Chen Shui-bian lost much esteem and intraparty authority in his administration's final years, making policy coordination much more difficult. Thanks to an overwhelming parliamentary majority and robust intraparty discipline, the new KMT government's policy-making has been very coherent so far, especially in the realm of cross-strait economic policy. Correspondingly, the important reorganization of the bodies responsible for cross-strait policy-making and implementation has exhibited a high degree of functional efficiency.

Policy coordination

Taiwan was ranked 39th (out of 178 countries) in Transparency International's 2008 Corruption Perceptions Index (CPI), making it a so-called middle integrity country. This is an acceptable result by international and regional comparison,

Anti-corruption policy

though it also suggests that little progress has been made over the last 10 years in the fight against corruption. A series of “sunshine bills” have been passed since the early 1990s to combat political corruption, the latest of which were the Political Contribution Act of 2004, which limits political donations and makes campaign financing more transparent, and the Lobbying Act of 2007, which requires lobbyists to register their activities and officials to report on communications with lobbyists within seven days. Most important for the containment of political corruption has been the 1993 Public Functionary Assets Disclosure Act, which requires the declaration of all income and assets by high-ranking officials and elected representatives. Party financing is regulated by law. Taiwan’s public and media are very sensitive to political corruption, having played a reasonably significant role in exposing officeholders who have come under charges of misbehavior. Taiwan’s anti-corruption policies are very strict, which is not really reflected in its current CPI ranking. This may point to a gap between factual and perceived corruption caused by a feeling of general disdain for party politics and the political elites, nurtured by a series of corruption scandals involving the family and close advisors of former president Chen Shui-bian during his second administration (2004 – 2008), and by the incapacitation of the Control Yuan in the final years of the Chen administration.

16 | Consensus-Building

There is still considerable disagreement between the two political camps on the issue of economic and social integration with the Chinese mainland, which is critical for the sustainability of Taiwan’s economic success. However, all major political actors agree that building and strengthening Taiwan’s market-based democracy are critical goals. No veto power survived the democratic transition and consolidation process of the late 1980s and 1990s.

Consensus on goals

There are no anti-democratic actors holding veto power in Taiwan.

Anti-democratic
veto actors

The most serious domestic cleavage, between advocates of Taiwan independence and a pro-integration approach towards China (which is not necessarily equivalent to advocating unification), is reflected in the ongoing division of the party system into two rival (“pan blue” and “pan green”) camps. As a matter of fact, the independence – unification/integration divide has evolved into conflict over the most promising policy approach toward the PRC. In that sense, the “identity cleavage” is less serious in Taiwan than it appears from the outside. There is no difference between the relevant political actors over the issue of de facto Taiwanese sovereignty, which all agree is to be uncompromisingly maintained. However, the DPP government under Chen Shui-bian polarized Taiwanese society with its pro-independence policies, and its call for outright rejection of the “one China” principle as a basis for cross-strait negotiations. The current KMT government has a

Cleavage /
conflict
management

strong public mandate to pursue its integration policies for the time being, but still faces a viable opposition that will likely have a strong comeback if the people feel disappointed by these policies' net results, or if they come to suspect a betrayal of Taiwan's sovereignty. President Ma Ying-jeou has tried hard to explain and justify his stance on cross-strait relations to the public and build a sustainable overarching consensus on his approach to integration, but it is too early to tell if he will be successful.

Civil society in Taiwan has meaningful access to the processes of political decision-making and is considered an important contributor to the formulation and evaluation of policies. Since the DPP evolved out of a movement of civic engagement during the authoritarian era, it strongly appreciated civil society input into the governing process. Hence, the DPP government sponsored regular meetings with civil society leaders and invited them to national conferences on particular problems such as economic and social development, environmental protection and educational reform. The legacy of the authoritarian era has left more distance between the KMT and Taiwan's civil society actors, most notably on the part of students (for example, the anti-KMT activities by the "Wild Strawberry" student movement in late 2008), environmental activists and intellectuals. However, the KMT is quite close to business organizations and takes their interests into serious consideration.

Civil society
participation

The most important cleavage in post-war Taiwanese society, the conflict between mainlanders and Taiwanese, has already been addressed by the former KMT government under Lee Teng-hui. In 1992, the Executive Yuan published the "February 28th Incident Research Report," which was the first official account of the tragedy based on solid academic research. In 1995, President Lee made a formal apology to the victims of the incident. Among other memorials erected, Taipei New Park was renamed 228 Memorial Park in 1996, and the 228 Incident Memorial Foundation was established to compensate the victims and their families. In 1997, February 28th was declared a national holiday. Newly elected President Ma Ying-jeou has taken further steps to clear up the history of the incident and of the equally painful period of Taiwan's "White Terror" in the 1950s. However, "228" has remained a sensitive issue in Taiwan's highly politicized society. It is still invoked by the "pan green" camp during election campaigns to remind the populace of the KMT's authoritarian past, and to mobilize it against China's claim to sovereignty over the island. As long as this strategy pays off, it seems that reconciliation has not been fully attained.

Reconciliation

17 | International Cooperation

Taiwan has been internationally oriented since its turn to export-led industrialization in the early 1960s. At the time, it made efficient use of U.S. economic aid, and it reacted positively to U.S. pressure for democratization and financial liberalization in the mid-1980s (which was a major step in pushing Taiwan to become a global center of computer technology). Taiwan's reputation for adapting to new circumstances and learning from its international environment is well known, and explains much of the "Taiwan miracle." Within the international community, it has earned a reputation of high credibility and reliability with respect to the continuous implementation of necessary market reforms – perhaps with the single exception of the banking and credit cooperative systems, which have long been supported by strong "traditional" forces resisting full-scale liberalization and transparency.

Effective use of support

Since China prevents Taiwan's entry into international and regional organizations and bodies in a state capacity, it is particularly important for Taiwan to demonstrate credibility, reliability and generosity in the international arena. The government has tried hard to convince the world's public that the degradation of its sovereignty is unfair, and that its diplomatic isolation deprives the international community of fully making use of Taiwan's expertise and financial might. This argument was made, for example, in the recent debate over Taiwan's member status in the World Health Organization. In fact, Taiwan enjoys a good reputation as a political partner and engaged donor of development aid and humanitarian assistance, as seen by the government's determined support to Myanmar after vast parts of that country were flooded, and to the Chinese government in the aftermath of the Sichuan earthquake. In the past, this reputation was compromised by what has been called "dollar diplomacy," referring to Taiwan's effort to trade development aid and economic assistance for diplomatic relations and international recognition. The new administration of President Ma Ying-jeou has declared at various occasions that it would abstain from such practices in order to strengthen its public image as being a responsible and a professional donor. Ma has also taken measures to bring U.S.-Taiwan relations back on track, after a chill related to former President Chen Shui-bian's Taiwanization policies and his resolute stance against Washington aimed at affirming Taiwanese sovereignty and national identity. Ma's changes include a new grip on Taiwan's defense policy, which was rather erratic during the Chen presidency as a result of the deadlock in the Legislative Yuan.

Credibility

Taiwan cooperates actively and successfully in regional and international organizations including the Asian Development Bank (ADB), the Asia-Pacific Economic Cooperation (APEC) and the WTO (though not under its official state name "Republic of China"). Generally speaking, the country has been a strong

Regional cooperation

advocate of regional integration and cooperation. During the Chen Shui-bian era, the only exception was cross-strait cooperation, which the DPP government intentionally constrained for political reasons. However, the new KMT government advocates systematic economic and social integration across the Taiwan Strait, underlining its commitment to develop good neighborly relations with the PRC.

Strategic Outlook

Starting in the 1950s, Taiwan successfully pursued transformation toward a market-based economy, and in the 1990s evolved peacefully into a consolidated democracy. The historic transfer of power in 2000, when the Democratic Progressive Party (DPP) won the presidency and took charge of the government for the first time, put the country's political institutions to a test. Confronted with a hostile majority in the legislature, strained relations with mainland China and serious economic slumps, the DPP government often sought to bolster its political legitimacy and gain public support through extraparliamentary means such as referendums, and by addressing the more radical segments of the electorate. This polarized the political discourse and heightened frustration with politics. However, Taiwan's democracy proved strong enough to cope with these problems.

Taiwanese politics took a U-turn following the March 2008 presidential elections, as the new administration of President Ma Ying-jeou embarked on a pro-integration approach toward China, seeking to strengthen Taiwan's export economy and attain new political leeway for Taiwan on the international stage. This strategy is sensible. For the time being, Ma enjoys sufficient support among the Taiwanese public to go ahead, though there is fierce resistance by core "pan green" supporters who claim he is selling out Taiwan. Cross-strait relations have substantially eased after the signing of a series of new agreements, negotiated by both sides, which have spurred the process of economic liberalization across the Taiwan Strait. It remains to be seen whether this new chapter of cross-strait relations can spill over into the political realm and produce innovative solutions for the sovereignty problem that overshadows the relationship between Beijing and Taipei. Much depends on the PRC government and its willingness to respond positively to Ma's mainland policies, and potentially give Taiwan more international room to maneuver. However, this willingness could be negatively affected by China's exposure to the global financial crisis and the consequences for economic and social stability, as any difficulties may translate into "rally round the flag" policies directed against Taiwan. If everything goes smoothly, Ma's mandate will become stronger and the DPP will face even greater problems in reinventing itself as a viable opposition party and political alternative. Currently, the party seems to be locked in struggle between those who continue to advocate a strict Taiwanization course and ultimate independence, and those who oppose this stance and demand more pragmatic policies. Given the economic and political disadvantages that Taiwan faces if its relations with the PRC are strained, it is important that both parties cooperate to ensure a strong overarching consensus that there be no inevitable trade-off between sovereignty and cross-strait integration.

Taiwan's market economy is basically sound, and it will further flourish thanks to ongoing cross-strait economic integration. The island's increasing interaction with the Chinese mainland should not only be assessed by taking stock of outbound investment and trade figures, but also by factoring in the growing numbers of Taiwanese students and professionals "emigrating to the motherland" for study, new job opportunities and profitable careers. Despite the intensity of

political confrontation in Taiwan over the best policy approach towards China, and the “deep green” orientation of much of Taiwan’s lower strata in the central and southern parts of the island, increasing segments of Taiwan’s middle class look across the Taiwan Strait and are open to closer ties with the PRC. This is an important development which should be encouraged by government policies. Further trade liberalization and cautious integration are all the more important as the global economic crisis puts additional pressure on the Taiwanese economy. This said, Taiwan must also pay attention to the dependence of its economy on the Chinese mainland, and to its fixation on information technology and electronics. Diversification of trade relations is as important as the expansion of “high-end manufacturing” and the tertiary sector, as was clearly spelled out in a recent Asian Development Bank (ADB) report. All in all, the latest agreements negotiated between Taipei and Beijing, establishing nearly unconditional direct trade, transport and communication channels across the Taiwan Strait, promise a peaceful and prosperous future for Taiwan – though all ultimately depends on the positive responses of the PRC political leadership, which must focus on pragmatic policies towards Taiwan and put the sovereignty issue on the backburner.