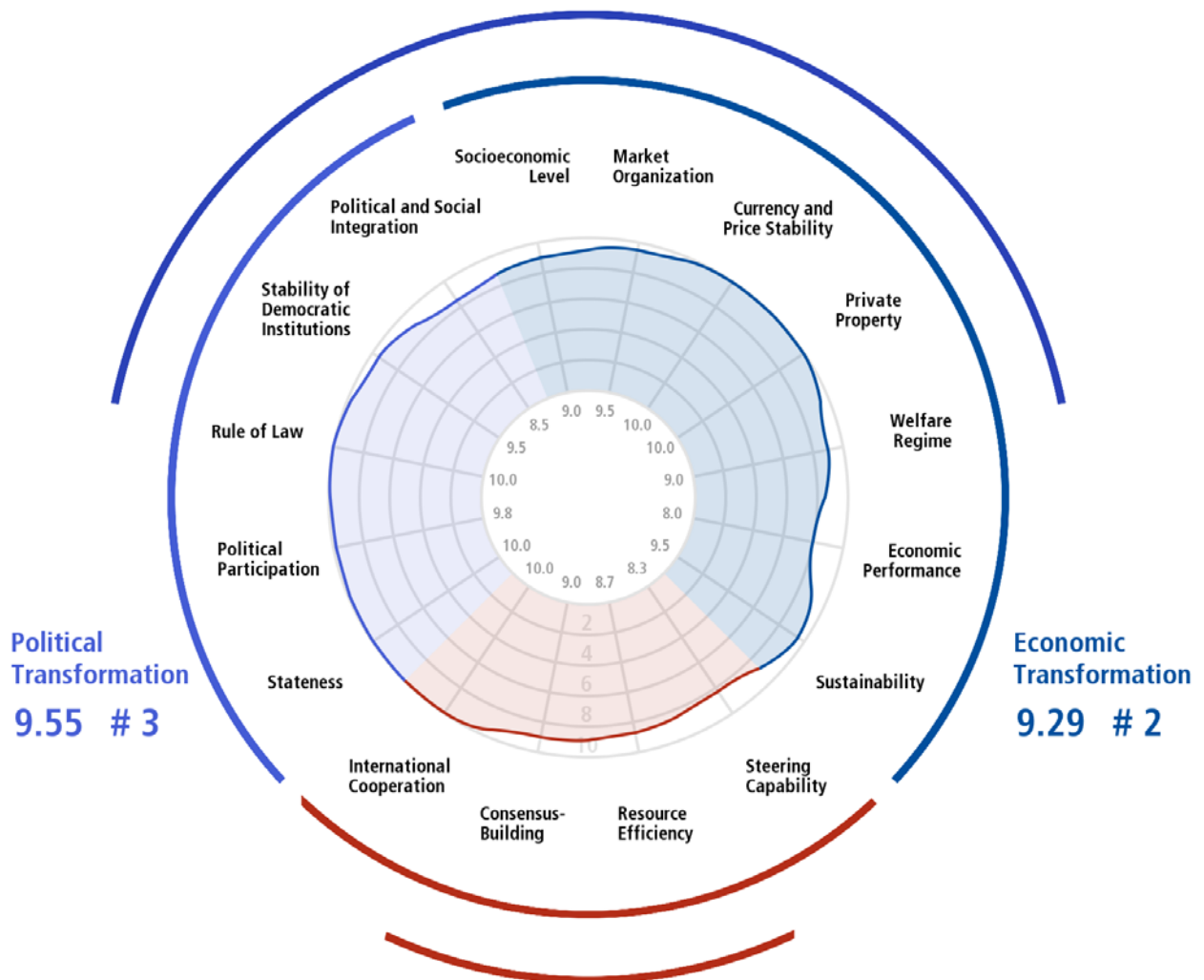


# Taiwan

## Status Index

**9.42 # 3**

on 1-10 scale out of 129



This report is part of the Bertelsmann Stiftung's Transformation Index (BTI) 2018. It covers the period from February 1, 2015 to January 31, 2017. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at <http://www.bti-project.org>.

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## Key Indicators

Population	M	23.5	HDI	-	GDP p.c., PPP \$	48095
Pop. growth <sup>1</sup>	% p.a.	0.2	HDI rank of 188	-	Gini Index	-
Life expectancy	years	80.0	UN Education Index	-	Poverty <sup>3</sup>	% -
Urban population	%	61.0	Gender inequality <sup>2</sup>	-	Aid per capita	\$ -

Sources (as of October 2017): The World Bank, World Development Indicators 2017 | UNDP, Human Development Report 2016. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

## Executive Summary

Throughout the period under review, Taiwan has remained a high performer in terms of democratic politics and liberal market policies. It continues to enjoy a high degree of stateness, meaningful elections, the absence of undemocratic veto actors, stable democratic institutions and a vibrant civil society, and does extremely well in guaranteeing its citizens political rights and civil liberties. Politically, the review period was dominated by the run-up to the January 16, 2016, general elections and the transitory period before the inauguration of the newly elected president on May 20. Throughout 2015, President Ma Ying-jeou and the ruling Kuomintang (KMT, Chinese Nationalist Party) were under heavy pressure by the opposition DPP (Democratic Progressive Party) and a re-politicized civil society, which severely attacked the government for selling out the country to China through their accommodating policies of cross-Strait economic integration and liberalization. In the face of the KMT's crushing defeat in the 2014 local elections, the failure to revive a sluggish economy, and a lame duck president suffering from extremely low approval ratings, the KMT dissolved into internal infighting. This led to the sacking of its presidential candidate three months prior to the elections and the DPP's landslide electoral victory, with its candidate, Tsai Ing-wen, winning the presidency and the party achieving a 60% parliamentary majority. The result not only marked the third peaceful transfer of power through direct elections in Taiwan, but also the election of the first woman to the country's top political position. Most observers agree that this was not so much a vote for a significant change in Taiwan's external relations, in which the DPP has traditionally endorsed de jure independence from China, but rather a sign of a maturing demos voting an incompetent government out of office. However, despite broad general approval of the principles and procedures of liberal democracy, there are worrisome signs of disillusionment with the established political institutions. Only two-thirds of the voting population participated in the elections, and trust in government institutions has further declined from already low levels during the review period.

These political developments were closely related to Taiwan's sluggish economy, which highlighted the dangers of the country's close economic integration with the mainland and

dependence on exports in times of declining Chinese growth rates and cooling global demand. Exports took a hit with negative growth of -10.9% in 2015 and another -1.8% projected for 2016. The economy remained almost stagnant through the review period with 0.72% growth of GDP in 2015, and 1.5% in 2016. GDP per capita actually fell from US\$22,668 in 2014 to US\$22,384 in 2015 and US\$22,530 in 2016. After a slight deflationary trend in 2015 that saw inflation at -0.31%, consumer prices again increased slightly in 2016 at 1.40%. Nonetheless, unemployment rates remained stable during the review period slightly below the 4% threshold, and public finances were healthy, with solid tax revenues, manageable and decreasing public debts and foreign reserves reaching a new record high of US\$434.2 billion in 2016. Overall, Taiwan remained one of the world's top twenty economies in terms of macrostability, international competitiveness, and market-friendly policies, despite the risks seen by many market actors posed by the country's economic dependence on China and concerns over political stability after the 2016 elections.

## History and Characteristics of Transformation

In Taiwan, political transformation has long taken a backseat to economic transformation. The foundations of a sound market economy were laid in the 1950s under the authoritarian leadership of Chiang Kai-shek and the KMT. 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 that followed the Chinese Civil War in 1949, Taiwan moved gradually toward a social market economy and established rudimentary social insurance systems. Democratic transition began with the illegal founding of the DPP on September 28, 1986 – a move tolerated at the time by the KMT regime – and the lifting of martial law on July 14, 1987. More reforms followed, most importantly the legalization of new political parties in January 1991. In 1991 and 1992 respectively, Taiwan saw the first free elections to its central parliamentary bodies, the National Assembly and the Legislative Yuan, marking the end of the transition process. During the 1990s, democracy matured by successive constitutional reforms that, along with other changes to Taiwan's political system, paved the way for the first direct presidential election in early 1996. The incumbent president and KMT party leader, Lee Teng-hui, won this election and gained himself the epithet of Taiwan's "father of democracy."

Successful democratic consolidation had already been achieved when Chen Shui-bian, an experienced DPP politician and stout advocate of Taiwanese independence, unexpectedly won the March 2000 presidential election and made the KMT an opposition party for the first time since 1949. The following eight years were dogged by severe legislative inefficiency as the partisan conflict between the ruling DPP and the KMT-led opposition, which commanded a majority in parliament, paralyzed the political process. Cross-strait relations further soured as the new president pursued an agenda of assuring Taiwanese sovereignty against Beijing's "one China principle" and pushed for a referendum law and a new constitution. Politically paralyzed and delegitimized by corruption charges against himself, a number of family members and close advisers, Chen Shui-bian became a "lame duck" toward the end of his second administration and

caused the DPP dramatic losses in the 2008 parliamentary and presidential elections. The KMT returned to power with President Ma Ying-jeou and a two-thirds majority in the Legislative Yuan. The new administration immediately embarked on a pro-active China policy by restarting cross-Strait negotiations, which have so far produced 23 accords signed between Taipei and Beijing, including the establishment of direct trade, transport and communication links across the Taiwan Strait, an investment protection agreement and a quasi-free trade pact (Economic Cooperation Framework Agreement, EFCA). Relations between Taiwan and China have become more stable after 2008, a major factor to ensure the incumbent KMT government re-election in the January 2012 presidential ballot.

However, eight years of trade liberalization, greater integration, and an overall accommodating cross-Strait policy has not led to a solution of the sovereignty dispute between Taipei and Beijing, and China's military threat continues unabated. Moreover, Taiwan's serious economic downturn in the wake of China's slowed growth in 2014 to 2015 has shown the dangers of too much economic dependence on the mainland's economy. An increasing share of the populace has grown disillusioned with the economic benefits of further cross-Strait integration. Consequently, the Cross-Strait Service Trade Agreement (CSSTA), signed in June 2013, has not been ratified due to strong political and civil society opposition, which culminated in the March and April 2014 protests of younger Taiwanese. The so-called Sunflower protests have led to a return of civil society to the center stage of politics, broadened the debate over Taiwan's economic and cross-Strait policy and revitalized the political party system with the establishment of a number of new political parties styling themselves as unaligned "third forces" outside of the political mainstream, most prominently the New Power Party (NPP). The 2016 general elections resulted in a crashing defeat for the KMT, which not only lost the presidential race to the DPP candidate Tsai Ing-wen, but also its majority in the Legislative Yuan, where the DPP secured 68 out of 113 seats, with the KMT's 35 and five seats for the NPP. Overall, however, the Taiwanese continue to overwhelmingly support maintaining the status quo in the Taiwan Strait and uncompromisingly stick to Taiwan's de facto sovereignty, if not de jure independence.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

## Transformation Status

### I. Political Transformation

#### 1 | Stateness

Although Taiwan's status under international law is contested, the Taiwanese state (which is officially named the Republic of China (ROC)) enjoys effective power and authority over its territory, including the islands of Taiwan, Penghu, Matsu and Kinmen.

While the long-lasting struggle over Taiwan's national identity has been replaced by a more policy-oriented public discourse over the speed, scope and limits of economic and socio-cultural integration with the mainland, the conflict over Taiwan's political future as an independent nation-state or as part of a unified Greater China remains to be resolved. The large majority of Taiwanese support the status quo in the Taiwan Strait, which constitutes the best compromise between their existential security interests in the face of China's militant rejection of Taiwan's formal independence and a distinct Taiwanese national identity, namely a growing identification with their state and a desire for sovereignty building since the 1990s. This trend continued even under the presidency of Ma Ying-jeou (KMT, 2008-2016), who initiated more Beijing-friendly policies, resulting in more stable cross-strait relations, more intensive economic interaction and more people-to-people exchange. Similarly, President Tsai Ying-wen, a former ardent critic of the so-called 1992 consensus, has pledged to maintain the status quo in the Taiwan Strait, to preserve the deepened integration achieved under her predecessor while ensuring the Taiwanese people's self-determination and the nation's democratic system.

Question  
Score

Monopoly on the  
use of force

10



1

State identity

10



1

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

No interference of religious dogmas

10



Taiwan's civilian administration is differentiated, professional and provides sound and reliable public services throughout the country. The judicial system, law enforcement and the taxation bureaucracy are well established and functional. Access to water, education and health services is secure and the existing, highly developed communication and transport infrastructure is continually subject to modernization.

Basic administration

10



## 2 | Political Participation

All relevant political offices are subject to competition in regular, universal and secret multi-party elections, which are usually undisputed and widely covered by the media. There are no restraints on the electoral process, which is fair and transparent, and professionally run by the non-partisan Central Election Commission. Vote buying (attracting voters with small gifts, free lunchboxes and small amounts of money as “tokens of appreciation” has come to be expected by most voters in suburban and rural districts) in local elections is still rampant and has so far weathered all legal action. In the 2016 general elections, over 500 individual cases of vote buying were reported. Overall, however, vote buying in Taiwan's electoral process has to be considered more a cultural habit than an effective political stratagem, as it does not seriously jeopardize the fairness or outcomes of elections, not least due to sharp media attention, strict regulations and resolute prosecution by the authorities.

Free and fair elections

10



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

Effective power to govern

10



Freedoms of association and assembly are constitutionally guaranteed, generally unrestricted and extensively exercised. The right to strike is established by law. Existing restrictions on the freedom of assembly are specified by law, especially the Assembly and Parade Act, and originated in Taiwan's early post-martial law period. They have been condemned repeatedly as too strict and in parts unconstitutional both by domestic and international civil rights groups, as well as in a 2014 decision by Taiwan's Constitutional Court. According to that act, protesters require advance permission by the local police authorities, police can restrict protests near government buildings, and rallies may be subject to forceful dispersal by the police. In early 2015, 199 participants of the 2014 Sunflower protest movement were charged for occupying the parliament and the Executive Yuan, which led to renewed domestic and international pressure by rights activists to amend the act and loosen the restrictions. In May 2016, a draft amendment of the act was proposed to the Legislative Yuan that would abolish the government's authority to withhold approval for demonstrations. Until the end of the review period, however, the amendment has not passed the parliament.

Association /  
assembly rights

10



1

Freedom of opinion and freedom of the press are well established and are exercised unrestrictedly, with vigorous and diverse reporting on government policies and alleged official wrongdoing. Taiwan's 2005 Freedom of Government Information Law guarantees public access to government documents. There is no media censorship. Individual incidents of police obstruction and violence against journalists covering demonstrations are reported, and journalists face defamation charges for critically reporting on politicians, but no systematic media harassment or violence against reporters have been reported during the review period. However, worries about an increasing media concentration in the hands of tycoons with large-scale business interests in China, to the detriment of objective reporting and press freedom, have continued during the review period. Also, there are many stories about self-censorship of critical news reporting on China in those media outlets controlled by Taiwanese entrepreneurs operating on the mainland. Taiwan's internet is free and up to date. There has been no official attempt to block websites that are critical of government policy.

Freedom of  
expression

9



1

### 3 | Rule of Law

The separation of powers into executive, legislative and judicial branches is well established and there is no extralegal execution of governmental power. The government system is structurally handicapped by the constitutional relationship between the president and parliament in times of divided government: 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 a vote of no confidence against the premier. Since the president can dissolve the legislature in such a case, the powers of the parliament are

Separation of  
powers

10



limited and there are almost no institutional guards against political stalemate in cases of divided government (i.e., when the president and the legislative majority belong to different parties). Debate on constitutional reforms to address these structural problems and introduce a parliamentary system, which had gained some momentum in recent years, has been put on the back burner during the review period and has not been included in the DPP's administration agenda.

Judicial independence is well established in Taiwan and court trials are generally fair. The court system is well differentiated. Taiwan's judges are well-trained (often abroad) and professional. Judicial corruption is not endemic. Nonetheless, throughout her presidential campaign as well as in her 2016 inauguration address, President Tsai has highlighted judicial reform as one of the core policy goals of her administration in order to address popular mistrust in the country's court system, which has proved long-standing and deep-seated despite the country's comparatively good performance in terms of judicial effectiveness and fairness. Similarly, past allegations by the DPP-led opposition and affiliated civil society groups of Taiwan's courts being too closely allied with the KMT government and "political persecution" of former president Chen Shui-bian (on medical parole since early January 2015) could not be substantiated by legally relevant evidence.

A range of sunshine laws regulate political donations, declarations of income for public servants and the rules for political lobbying. Political corruption receives a great deal of attention in the mass media, even though most observers agree that the country does reasonably well in preventing and prosecuting large-scale corruption. It is an important issue on the platforms of all relevant political parties and is prosecuted rigorously under criminal law. An official Agency Against Corruption (AAC) was established in June 2011, mimicking similar institutions in Hong Kong and Singapore, and since 2013 an online database of government documents has further increased transparency. Fierce competition between the political camps, aggressive reporting and an educated and highly sensitive population ensure that high-profile corruption charges receive much publicity, such as the November 2015 bribery charge of former New Taipei City deputy mayor, Hsu Chih-chien. Vote buying in local elections remains a problem in Taiwan as it is established practice since the early days of democratization and regarded as inevitable by most politicians. However, the judiciary is prosecuting vote buying activities and punishing those found guilty.

The constitution prohibits discrimination based on race, sex, religion, political opinion, national origin or citizenship, social origin, disability, sexual orientation and gender identity, and the authorities effectively enforce these prohibitions. Consequently, Taiwan enjoys a very good human rights record according to all relevant international observer groups and there are no reports of unlawful or arbitrary use of state power against the population or any specific minority. Civil rights are constitutionally guaranteed and well protected, and those who violate them



1

Independent judiciary

10



1

Prosecution of office abuse

10



1

Civil rights

10



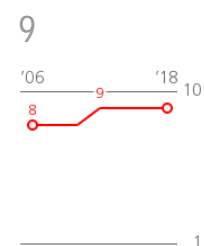
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are taken to court. The judicial system provides ample opportunities to seek redress for rights violations. Court trials follow due process, and there are no reports of physical abuse of prisoners. The police largely respect the ban on arbitrary detention, and attorneys are usually allowed to monitor interrogation to prevent abuses. Throughout the period under review, same-sex marriage remained illegal. However, in December 2016 an amendment of the civil code to legalize such unions passed the first parliamentary reading, and is expected to be voted into law in early 2017. The review period also saw continued improvements in Taiwan's immigration policy concerning the legal position of foreign spouses, a group particularly vulnerable to discrimination and exploitation, most notably concerning easier access to legal aid and naturalization. In October 2016, residency restrictions were eased for Taiwan's 625,000 migrant workers (mostly from Indonesia, the Philippines and Vietnam), though they remain limited to employment as industrial laborers, marine workers and household caregivers. Moreover, while the provisions of the Labor Standards Law cover these blue-collar migrant workers, existing standards are not easily monitored and enforced on household workers and workers in the fishing industry, which facilitates exploitation and sexual harassment. Taiwan continues to adhere to the death penalty against all domestic and international protest with the government regularly citing opinion surveys to prove that a majority of the populace supports capital punishment for serious crimes.

#### 4 | Stability of Democratic Institutions

All government institutions are democratically legitimized, work according to legal procedures and are sufficiently controlled by a working system of mutual checks and balances. All political decisions are prepared, made, implemented and reviewed through legitimate procedures by the appropriate authorities. The existing semi-presidential system is prone to deadlock in times of divided government, but no meaningful attempts of constitutional reform toward a more coherent system of government have been made during the period under review. In addition, Taiwanese political competition is characterized by a fierce, zero-sum nature both across and within parties. This undermines lawmaking efficiency even in times where president and parliamentary majority are from the same party, as has been the case during the review period.

Performance of democratic institutions



All relevant political actors accept the democratic institutions as legitimate and there are no attempts to realize political goals outside of legally defined democratic channels.

Commitment to democratic institutions

10

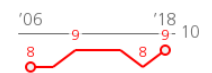


## 5 | Political and Social Integration

The party system is relatively stable, socially anchored and enjoys broad popular support. Diverging opinions across popular and societal interests are reflected and aggregated reasonably well, while clientelism does not play a major role in party politics. Party system fragmentation is low. Even though 18 parties participated in the 2016 general elections, the party system is dominated by the two large parties, the DPP and the KMT, and their respective party alliances, the DPP-led “pan-green alliance” that includes the Taiwan Solidarity Union (TSU), and the KMT-led “pan blue alliance” that includes the People’s First Party (PFP) and the Non-Partisan Solidarity Union (NPSU). In the Eighth Legislative Yuan (2012-2016), the two large parties accounted for 104 out of the 113 members of parliament (92% of all seats; KMT: 64 seats; DPP: 40 seats). Similarly, the DPP and KMT account for 113 of seats in the Ninth Legislative Yuan (since 2016; DPP: 68, KMT: 35). Party system volatility is also relatively low, but Taiwan’s political system is sufficiently permeable to allow new political parties to enter. The 2016 legislative elections saw not only the TSU dropping out of parliament, but also the emergence of the newly founded New Power Party (NPP), which developed out of the 2014 Sunflower Student Movement and won five parliamentary seats based on an unaligned “third force” platform, despite ideological similarity to the DPP’s agenda. Political polarization concerning the diverging stances on Taiwan’s China policy, the major policy difference between the two camps, has declined somewhat during the review period with both the DPP and the KMT targeting the large majority of voters who consider themselves close to the center of the unification-independence spectrum. Moreover, the 2015 to 2016 campaign was dominated by the two parties’ diverging platforms for strengthening the country’s ailing economy, with the KMT promoting greater international integration, and the DPP focusing on strengthening Taiwan’s domestic economy and social safety.

Party system

9



Taiwan is home to a wide variety of civil society groups, including unions, professional and business organizations, social and environmental movements, and other associations, which represent a broad range of societal interests. This network of interest groups is close-knit, politically influential and operates independently of

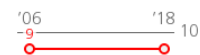
Interest groups

9

the state. There are no attempts by non-state interest groups to abandon democracy or organize political violence and no group can dominate others. Parts of Taiwan’s civil society remain focused on ideological issues related to cross-strait policy and the unification/independence split, sometimes resulting in factional strife and public clashes, which became particularly visible during the 2014 Sunflower Student Movement. At the same time, the momentum generated by the student movement has given important external impulses to the somewhat calloused (sclerotic, petrified) political landscape and has helped put a range of social justice and civil rights issues on the political agenda, including judicial reform, LGBT rights, land rights for Taiwan’s aboriginal peoples and the abolition of the death penalty.

Voter turnout took a hit in the 2016 general elections, with only 66.3% of the voting population participating in the elections, the lowest since the transition to democracy. In line with strengthened alternative forms of political participation and communication through social media and civic activism, this suggests a degree of disillusionment with the established political institutions. This is also reflected in the levels of trust in government institutions, which has further declined from an already relatively low level. According to the latest data for Taiwan from the Asian Barometer Survey (2016), only 25% of respondents expressed trust in the presidency and the national government, respectively, with 70% distrusting these institutions. Trust in the representative organs is even lower, with only 12% and 17% trusting political parties and the legislature, respectively. However, the majority of Taiwanese express strong consent for the principle of democracy: while only 47% would agree that democracy is preferable under all circumstances, 88% hold that democracy is the best kind of government despite its problems, 75% reject authoritarian alternatives and 64% are satisfied overall with the way democracy works in Taiwan.

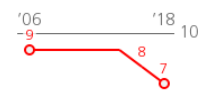
Generally speaking, social self-organization is well developed in Taiwan. A variety of organizations, including an outspoken environmental movement, social groups and lively religious communities, are the backbone of Taiwan’s democracy. They create a climate of tolerance and a culture of non-violence and democratic deliberation. Based on the latest 2016 Asian Barometer Survey data for Taiwan, interpersonal trust is fairly high, despite social tensions over Taiwan’s national identity and political status (the independence/unification divide). While 54% express the opinion that one has to be “very careful in dealing with people”, 64% agree that most people are trustworthy and only 20% think most people would try to take advantage of others given the chance.



1

Approval of democracy

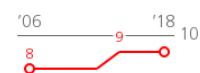
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1

Social capital

9



1

## II. Economic Transformation

### 6 | Level of Socioeconomic Development

Taiwan is a highly developed market economy. The country’s level of socioeconomic development permits adequate freedom of choice for all citizens. Fundamental social exclusion due to poverty, gender, religion or ethnicity is qualitatively minor to nonexistent and is not structurally embedded. Taiwan’s poverty rate is low in international comparison and stands at 1.5 % according to the latest available data. Income distribution – as measured by the Gini coefficient – is relatively equal and has been stable around 0.34 since 2010 and throughout the review period. This stands in contrast to an energetic domestic debate on rising social inequality in Taiwan caused by low economic growth, stagnant wages and highlighted by their shrinking share of Taiwan’s GDP. According to the most recent data available (2014), Taiwan is considered a country with very high human development. At 0.882, it would rank 25th globally in UNDP’s Human Development Index. Moreover, Taiwan has a relatively low level of gender inequality, ranking 5th worldwide with a Gender Inequality Index of 0.052. The most socially excluded group is Taiwan’s 625,000 strong foreign blue-collar worker community employed as household caregivers, factory workers and in the fishing industry who suffer from low salaries and social discrimination, but also enjoy increasing support from civic groups and social organizations. The new DPP government has announced intentions to improve their legal and socioeconomic position. However, a major problem is the dependence of migrant workers on private brokerage agencies in Taiwan, which depress their salaries by taking huge commissions. This results in many of them leaving their commissioned jobs very quickly to find better paying illegal work, which further increases their vulnerability to exploitation.

Question  
Score

Socioeconomic  
barriers

9



1

Economic indicators		2013	2014	2015	2016
GDP	\$ M	511599.0	530515.0	525236.0	<b>529575.0</b>
GDP growth	%	2.2	4.0	0.7	<b>1.5</b>
Inflation (CPI)	%	0.8	1.2	-0.3	<b>1.4</b>
Unemployment	%	4.2	4.0	3.8	<b>3.9</b>

Economic indicators		2013	2014	2015	2016
Foreign direct investment	% of GDP	-	-	-	-
Export growth	%	3.8	5.6	-0.3	1.7
Import growth	%	4.5	5.0	2.0	2.6
Current account balance	\$ M	53054.0	63812.0	76165.0	74280.0
Public debt	% of GDP	39.0	37.9	36.6	36.2
External debt	\$ M	53054.0	63812.0	76165.0	74280.0
Total debt service	\$ M	5908.0	4682.0	4518.0	5551.0
Net lending/borrowing	% of GDP	-3.2	-2.7	-1.8	-2.2
Tax revenue	% of GDP	8.0	8.4	8.7	-
Government consumption	% of GDP	14.7	14.5	14.0	14.3
Public education spending	% of GDP	1.5	1.5	1.5	-
Public health spending	% of GDP	0.1	0.1	-	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	1.9	1.8	1.9	1.9

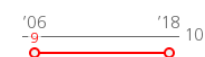
Sources (as of October 2017): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

## 7 | Organization of the Market and Competition

Taiwan's market economy is institutionally sound with transparent, clearly defined and state-guaranteed rules for ensuring fair competition and largely equal opportunities for all market participants. A Fair Trade Commission supervises business practices to ensure fair competition. Business freedom is high and market actors face neither entry nor exit barriers. Taiwan ranks consistently high in global economic indices in terms of ease of doing business, economic freedom and competitiveness. According to the Economic Freedom of the World Annual Report 2016, Taiwan is ranked 23rd with a score of 7.65 out of 10 (based on 2014 figures), and 3rd in Asia behind Hong Kong and Singapore. It did particularly well in the categories of government size, sound money and credit market regulations. According to the Global Competitiveness Report 2016-2017, Taiwan is ranked 14 out of 138 countries, and in the 2017 Index of Economic Freedom, Taiwan was ranked 11th with very high scores for well-specified property rights, and freedom of business, monetary transactions and trade. The main limitation on Taiwan's economic openness remains the restricted access for Chinese firms to Taiwanese markets despite considerable liberalization since 2008. Investment in a number of

Market-based competition

9



strategic sectors like LED, solar cells and display panels remain capped for mainland investors at less than 50%. In non-strategic sectors of Taiwan's manufacturing industries, however, mainland Chinese capital can increase its ownership to more than 50%. Plans to reduce further the barriers of Chinese investment into Taiwan's sensitive telecommunications sector and the lifting of Chinese capital inflow have stalled with the non-ratification of the Cross-Strait Trade in Service Trades Agreement (CSSTSA) in the aftermath of the 2014 Sunflower protests. The DPP government has pledged that it will not advance further cross-strait liberalization until the Legislative Yuan passes a cross-strait supervisory bill to monitor all agreements between China and Taiwan.

Even though the state maintains its monopoly over certain basic utilities and services (e.g., water supply and postal services), market competition is well established and legal frameworks exist to combat cartels. The Fair Trade Law that took effect in 2002 ensures a coherent and effective approach to combating monopolistic structures or predatory price fixing. In January 2017, the Legislative Yuan passed an amendment to its electricity act that effectively ended the monopoly of state-run Taiwan Power Co. (Taipower) in the electricity market by allowing "green" energy producers to sell directly to customers.

Taiwan enjoys a high degree of trade freedom, as its economy is heavily reliant on its export economy. The country is one of the world's principal exporters of electronics and IT-technology. Tariff rates on industrial products are comparable to those found in industrialized nations such as Japan and the United States, and Taiwan generally plays to WTO rules. With the exception of cross-strait economic relations, the state refrains from intervening in investment planning and foreign trade. Intervention in the former mainly takes place in order to control the level of Taiwan's high trade dependency on China, but also to restrict mainland investment in sensitive sectors, most notably, real estate, finance and telecommunications.

Some 40% of Taiwan's exports and more than 60% of its outbound investment have gone to the Chinese mainland (including Hong Kong) over the last two decades, resulting in a high trade dependency on China, which has worried critical observers for quite some time. The ratification of follow-up agreements to the cross-strait Economic Cooperation Framework Agreement (ECFA) to liberalize further trade in services and goods across the Taiwan Strait has been halted after the March 2014 Sunflower protests. The DPP government has pledged that it will not advance further cross-strait liberalization until the Legislative Yuan passes a cross-strait supervisory bill to monitor all agreements between China and Taiwan.

According to official data, at the end of 2015 Taiwan had 39 commercial banks, which accounted for 79.24% of total deposit accepted and 89.08% of total loans extended in Taiwan. 30 local branches of foreign (including mainland Chinese) banks were responsible for 1.37% of total deposits and 3.33% of loans. 23 credit cooperatives, which mainly service regional customers, accounted for 1.44% of total

Anti-monopoly  
policy



1

Liberalization of  
foreign trade



1

Banking system

9



deposits and a market share of loans of 1.49%. Taiwan has a tightly regulated and transparent banking system, which is effectively supervised by the Financial Supervisory Commission (FSC) and an independent central bank. The capital and stock market is reasonably developed and in principle open to foreign participation. Banks benefit from a high proportion of stable customer deposits and flexibility to access domestic capital markets. Also, the system's low use of cross-border funding makes it less vulnerable to contagion risks during periods of turbulences in global capital markets like the 2008/9 global financial crisis. The official non-performing loans (NPL) ratio of Taiwanese domestic banks was 0.23% and 0.27% at the end of 2015 and 2016, respectively. The slight increase during the review period was driven mainly by the economic slowdown in China. The capital adequacy ratio of Taiwan's banking stood at 12.98 % in mid-2016, well above the statutory Basel III minimum of 10.5% that is required by 2019. A 2016 stress test under the auspices of the FSC diagnosed Taiwan's banking industry as having sufficient financial resilience, and international analysts agree that Taiwan's banking system is overall stable and poses low risk.



On the negative side, real estate-related loans account for an unhealthy 40% in the books of Taiwan's domestic banks and the banking sector remains dominated by fully and partially state-owned banks and is highly fragmented. Taiwan's banking system has the lowest banking concentration ratio of the large financial systems in the region. While this reduces the threats of excessive concentration in a few "too big to fail" institutions, it has led to fierce competition that drives down profitability close to unsustainable levels. Moreover, to improve profitability, Taiwanese banks have expanded into potentially unstable regional markets, including China and Myanmar, which exposes them to greater risks, as exemplified by the increase in non-performing loans in 2016.

## 8 | Currency and Price Stability

Taiwan's government and central bank pursue a prudent foreign exchange policy that has been consistently linked to the goal of financial and economic stability and steered the county rather well through the 2008/2009 global financial crisis and its aftermath. Taiwan's central bank is fully independent and enjoys one of the best reputations in Asia for its cautious and reliable interest rate policies. As a result, inflation levels and volatility have been low during the review period with its consumer price index (CPI) at 1.40% in 2016, after a slight deflationary trend in 2015 that saw inflation at -0.31% (compared to 0.79% in 2013 and 1.20% in 2014). The New Taiwan dollar (TWD) has slightly devalued against the U.S. dollar, with a projected average exchange rate of TWD 32.33 per U.S. dollar in 2016, up from TWD 31.91 in 2015 (compared to 29.77 in 2014 and TWD 30.37 in 2014).

Anti-inflation /  
forex policy

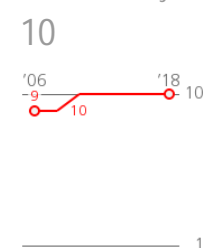
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Taiwan's outstanding total public debt (measuring non-self-redeeming debts across all levels of government) has slightly decreased over the review period from 37.9% of GDP in 2014 to 36.6% in 2015 and is projected at 35.5% in December 2016. These figures are comparatively low by global and regional standards and must be viewed against a long track record of prudent fiscal policy-making and resolute debt control as part of Taiwan's overall economic policy, suggesting effective crisis management and macroeconomic stability. Taiwan's foreign exchange reserves have reached a new record high of US\$ 434.2 billion in 2016.

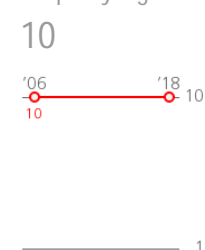
#### Macrostability



## 9 | Private Property

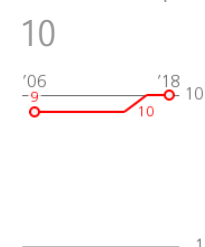
Taiwan's property rights regime is well established and enforced by an independent judiciary. The country consistently ranks high in terms of property rights in global economic freedom and business environment indices. This is despite individual disputes over land expropriation that have received much media attention in recent years and have highlighted vague language in Taiwan's Land Expropriation Act and deficient implementation of compensation regulations. While Taiwan is not member of the World Intellectual Property Organization (WIPO), it adheres to the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), established an Intellectual Property Court in 2008 and, since 2009, is no longer listed on the U.S. Special 301 Watch List of countries with inadequate intellectual property laws.

#### Property rights



Taiwan's economy is mainly based on small- and medium-sized private companies (some 1.4 million, around 98% of all companies according to 2015 figures), which are adequately protected by the state. The state continues to be directly involved in a number of "strategic" economic areas (shipbuilding, petroleum, steel, sugar, tobacco and liquor, banking, insurance and railway transport), in some cases holding the majority of shares. Basic utilities (conventional power production, water supply and postal services) remain monopolized by state-owned enterprises (SOEs), even though the January 2017 amendment to the electricity act allows "green" energy producers to sell directly to customers. SOEs such as the China Petroleum Corporation (CPC) and Taiwan Tobacco and Liquor Co. continue to control large market shares even in liberalized markets. Except for the state monopolies, SOEs compete directly with private companies. The eventual privatization of all residual SOEs has been expected for some time, but not much progress has been made in this regard during the review period.

#### Private enterprise



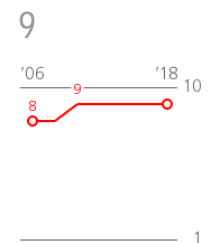
## 10 | Welfare Regime

With social welfare net expenditures accounting for 22.8% of the government budget in 2015 and 22.3% in 2016, Taiwan has one of the most comprehensive and well-developed welfare regimes in Asia. The social safety net is close-knit and provides for substantial protection against poverty and other social risks. The state provides a compulsory National Health Insurance (NHI) program for all citizens, including foreigners who have lived in Taiwan for more than six months, unemployment insurance, voluntary labor pension with portable retirement accounts, and mandatory coverage by a national pension scheme, which includes the unemployed, non-working spouses and freelancers. Financial support is also given to the disabled and disadvantaged households, including living cost allowances, health care and special subsidies. Moreover, amendments to the Public Assistance Act, which came into force on July 1, 2011, stipulate the conditions of long and short-term assistance to lower and middle-income households by providing living subsidies covering different areas of threatened well-being. In May 2015, the legislature approved the Long-Term Care Services Act, which outlines the legal framework for a comprehensive strategy to deal with the long-term care requirements of Taiwan's rapidly aging population.

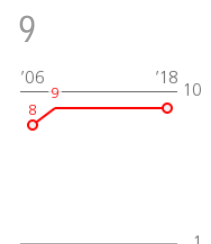
Following the January 2013 reform of the NHI aimed at increasing revenues and balancing the structural deficits that had plagued the system since its inception, the government funds at least 36% of the NHI budget, while the rest is financed by premiums paid by the insured and employers. The NHI budget is supplemented by a charge of 2% on non-payroll income from stock dividends, interest earnings, rents and bonuses exceeding four months' salary, as well as additional income from the Health and Welfare Surcharge on Tobacco Products (TWD \$20 or US\$ 0.60 per standard pack of cigarettes) and proceeds from the national lottery. Military conscripts, prison inmates and low-income households do not need to pay; their premiums are fully paid by the government. Since 2010, revenues have been consistently larger than expenditures, such that by the end of 2015 a solid reserve of TWD \$229 billion had accumulated. The new DPP-led government has made the expansion of the welfare regime one of its main priorities.

According to the constitution, all citizens are equal before the law "irrespective of sex, religion, race, class, or party affiliation." Women's rights have been continuously strengthened in recent years, with a focus on preventing and legally condemning domestic violence and sexual assault, but also on protecting women's' labor rights. A cabinet-level Department of Gender Equality was installed in 2012. The Gender Equality in Employment Act, last amended in 2013, stipulates that the principle of equal pay for equal work must be respected, while adequate mechanisms to prevent sexual harassment are implemented in every workplace. Employees – both female and male – may apply for unpaid parental leave for up to two years in order to care

Social safety nets



Equal opportunity



for their children under the age of three. The act also ensures women the right to eight weeks of paid maternity leave.

According to the 2014 U.N. Gender Inequality Index, Taiwan ranked first in Asia and fifth in the world (its calculated index value is 0.052, with a score of 1 meaning extreme gender inequality), trailing only Slovenia, Switzerland, Germany and Denmark. Taiwan's Gender Gap index was 0.72 in 2015 (measuring gender gaps in economic participation, educational attainment, political representation, and health), which would rank Taiwan 43rd globally and second in Asia (behind the Philippines).

Further progress has been made during the review period. While female literacy rates (97.5%) still slightly trailed men's (99.7%) in 2015, in 2014, female university students outnumbered their male counterparts for the first time, and accounted for 50.41% of all university students in 2015, mirroring trends in other highly developed countries. Similarly, women's labor participation rate has risen, and the pay gap has been closing gradually. In 2015, the share of women of the workforce was 50.74%, and 50.8% in 2016, up from 50.46% in 2013. Also in 2016, women earned on average 16.4% less than men in the non-agricultural sector, down from 18% in 2013. 2016 marked an important year for women's greater role in Taiwanese politics with the first election of a female candidate to the presidency. Women also make up more than half of the members of the Control Yuan, about four-tenths of the Examination Yuan, and 38% of the Ninth Legislative Yuan.

The biggest problem concerning gender equality is related to deeply entrenched cultural traditions, which also has had an impact on the legal system. Under Taiwan's notorious adultery law, sexual infidelity remains a criminal offense and "unfaithful" women tend to receive harsher treatment than men. There is also much pressure on women to waive their inheritance rights in favor of male relatives, as according to traditional practice, only men can pass down property and the family name. As in other parts of East Asia, abortion of female fetuses is reported in Taiwan, even though the long uneven sex ratios at birth have declined somewhat to 108.27 boys to 100 girls in 2015.

Taiwan's indigenous peoples, accounting for about 2% of total population, have access to a number of social welfare programs based on specific laws to protect their rights. These include low-interest housing loans and rent subsidies, privileged access to senior high schools and universities, a 1% quota within the workforce at government agencies, public schools and state enterprises with 100 or more employees, and the protection of their language and culture. The social gap between these native groups and the Taiwanese Han-majority has narrowed over the years, but inequality still exists.

## 11 | Economic Performance

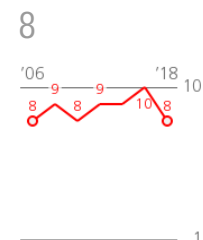
During the review period, Taiwan's economy has been hit hard by cooling of global demand and, especially, the downturn of the mainland Chinese economy, which underlines the dangers of too strong cross-strait economic integration and Taiwan's dependency on export markets. Exports took a hit with negative growth of -10.9% in 2015 and another -1.8% projected for 2016, compared to growth of 2.8% in 2014. Due to sluggish domestic demand and severe drops in imports of -15.8% in 2015 and -2.8 in 2016, the overall trade surplus continued to rise over the review period from US\$ 38.2 billion in 2014 to US\$ 48.1 billion in 2015 and US\$ 49.8 billion projected for 2016. This was reflected in the overall growth of the economy. After solid growth of 4.02% in 2014, GDP hardly grew throughout the review period with only 0.72% in 2015, and a projected 1.50% for 2016. GDP per capita actually fell from US\$ 22,668 in 2014 to US\$ 22,384 in 2015 and is projected to reach US\$ 22,530 in 2016. Inflation as measured by the consumer price index (CPI) rose to 1.40% in 2016, after a slight deflationary trend in 2015 that saw inflation at -0.31% (compared to 0.79% in 2013 and 1.20% in 2014).

Unemployment remained relatively low with slightly increasing labor participation rates of 58.65% in 2015 (up from 58.54% in 2014), and 58.75% projected for 2016. Unemployment rates also decreased slightly from 3.96% in 2014 to 3.78% in 2015, but were projected to rise again in 2016 to 3.92%, which is relatively low in comparison to other advanced industrial economies, but considered high in Taiwan. Tax revenues totaled 12.3% of GDP in 2015 and 13% in 2016, which is low compared to OECD countries, but similar to figures found in other East Asian developmental states as South Korea. In 2016, Taiwan's current account showed a solid surplus of US\$ 70.94 billion, down from US\$ 76.17 billion in 2015. Gross capital formation declined at -0.37% in 2015 compared to the previous year, and is projected to have increased at 2.12% in 2016.

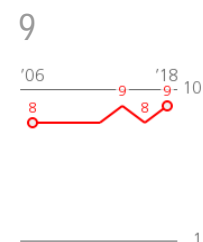
## 12 | Sustainability

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 planning. Today, environmental protection is institutionally integrated through the independent cabinet-level Environmental Protection Administration (EPA) and at the sub divisional level within different government entities, resulting in systematic environmental policy planning and a decreasing externalization of costs over the years. Taiwan has quite a sophisticated regulatory framework for environmental policy in place, and there is a broad consensus that economic development must be ecologically sustainable. In 2016, the Ministry of Economic Affairs launched the

Output strength



Environmental policy



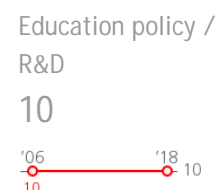
five-year Green Trade Action Plan to reduce the carbon footprint of trade in products and services and to support Taiwanese companies in coping with international environmental standards.

Taiwan is heavily dependent on fossil fuels for energy sources, with oil, coal and natural gas accounting for 90.8% of all energy supplies in 2015, and nuclear power and renewable energy 7.28% and 1.92%, respectively. Consequently, greenhouse gas emissions pose the most serious long-term problem for Taiwan's environmental performance. The development of green technologies and mechanisms for raising energy efficiency is an important part of the government's "Master Plan of Energy Conservation and Carbon Mitigation," which was approved in 2010 and renamed the "National Green Energy and Low Carbon Master Plan" in May 2014. The plan stipulates ten individual measures, including an adequate regulatory framework, the lowering of the share of energy derived from fossil fuels, and environmental education and public instruction. In June 2015, the Greenhouse Gas Reduction and Management Act was passed by the Legislative Yuan, setting a target of reducing Taiwan's greenhouse gas emissions to less than half its 2005 level by 2050. It also stipulates the establishment of a national action plan for climate change and implementation measures for slashing greenhouse gases. Overall, CO<sub>2</sub> emissions were cut by 34.62 million tons between 2010 and 2015.

Taiwan has three nuclear power plants, whose safety and long-term waste disposal have become even bigger public concerns since the 2011 Fukushima incident in Japan. The construction of a fourth nuclear power plant was halted in 2014 due to massive social protests against nuclear energy production in Taiwan. The Tsai government stated in May 2016 that nuclear power would be phased out completely by 2025.

Taiwan ranked 60 out of 180 countries in the 2016 Environmental Performance Index (down from 46 in 2014). Despite the loss of 14 rank positions, the index value for Taiwan actually increased from 62.18 in 2014 to 74.88 and the country performed considerably better than most countries in the region. The Index indicates positive achievements in air quality, "greening" agriculture (reduction of subsidies and pesticide control), protecting biodiversity/habitat, the protection of fish stocks and exposure to environmental health risks.

Taiwan has a very well-developed education system with high-quality secondary and post-secondary education as well as vocational training, reflecting the importance given to education in a society still heavily imbued with Confucian values. The literacy rate stood at 98.6% at the end of 2015. In the same year, the gross enrollment rate of all levels of education stood at 95.10% and for post-secondary education at 83.73%, which is high compared to international figures. Since 2014, tuition-free education has been extended from nine years of schooling to 12, with the first nine years being compulsory (six years of elementary school and three years of junior high school). As of 2015, almost all junior high school graduates continued on to further



studies, including academic senior high school or vocational training in technical high schools. In the same year, 37% of Taiwan's population had higher education degrees.

School curricula undergo continuous reform to keep the education system in line with international developments, though it is very hard for Taiwan to do away with the tradition of rote learning at the primary and secondary level. On the other hand, Taiwanese pupils are regularly among the world's best performers in international comparative tests, particularly in mathematics and science.

Total expenditures for education stood at 4.93% of GNI (with 3.68% public expenditures and 1.25% private) in 2015, which is not particularly high in international comparison, given the fact that Taiwan is an industrialized nation in which a good education is of preeminent significance. However, with 20.31% of all government expenditures in 2015, Taiwan spends a comparatively large share of government money on education.

R&D is a major concern for Taiwan's natural resource-poor economy and has long been a policy priority. In 2014, the former National Science Council has been upgraded to the Ministry of Science and Technology (MOST). The Taiwanese government manages 13 science parks spread out all over the island, which offer infrastructural hardware and services to high-tech firms. It focuses its resources on the development of cutting-edge technologies like nanoscience and nanotechnology, intelligent electronics, cloud computing, genomic medicine and biotechnology.

R&D spending is very high in comparison to international standards, with overall expenditures at 3% of GDP in 2014, totaling TWD 483.49 billion (US\$ 14.5 billion), out of which 21.7% of R&D expenditures were funded by the government and 78.3% came from private investment. In the 2016-2017 World Economic Forum's Global Competitiveness Report Taiwan is ranked 12 out of 138 countries in company spending on R&D, 17th in university-industry collaboration in R&D and 24th in capacity for innovation.

## Governance

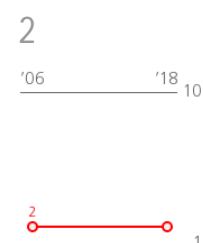
### I. Level of Difficulty

Taiwan enjoys few structural constraints on governance thanks to its high level of socioeconomic development; its sound market economy and good economic performance; a well-developed education system and research environment; a well-qualified labor force; a capable bureaucratic apparatus; relatively 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.

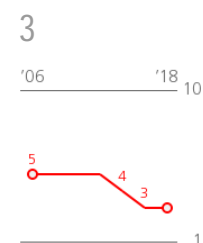
However, Taiwan is a small island country, roughly two-third of its landmass is mountainous, and the country is handicapped by high exposure to natural calamities, as typhoons and earthquakes hit the island every year and tax the government's administrative capabilities and financial resources. Moreover, Taiwan is almost completely dependent on energy imports, which leaves the country vulnerable to external shocks. Taiwan's main structural constraint is its diplomatic isolation and China's de facto veto power concerning its participation in the international community as a sovereign state, which significantly impedes the latter's self-determined management of international relations.

Taiwan's civic engagement has strengthened continuously since the end of the authoritarian era in the mid-1980s, when social movements played a major role in the transition to democracy and then contributed substantially to democratic consolidation. Today, Taiwan has one of the most vibrant civil societies in Asia, characterized by numerous NGOs engaged in all sorts of public activity. Ideological polarization and division concerning issues of national identity and Taiwan's relationship to China still play a role, and at times, impact negatively on the state-society relationship. However, the Sunflower movement of 2014 not only gave Taiwan's civil society a new push and political relevance, it proved the political system's ability and flexibility to react to the voiced grievances and transfer them into orderly channels of political competition through the existing party landscape. It also triggered the emergence of the New Power Party as a self-declared alternative "third force" next to the two main party camps.

Structural constraints



Civil society traditions

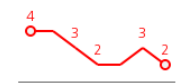


There is no politically motivated violence in Taiwan. The isolated, but much publicized, instances of violence against protesters during the 2014 Sunflower student protests have not been repeated during the review period. The old conflict between mainlanders and native Taiwanese has evolved into a cleavage within society concerning Taiwan's future political relationship with China and the most sensible approach to secure the nation's sovereignty, long-term security and prosperity. However, the ideological confrontation between those leaning toward Taiwanese de jure independence and those favoring reconciliation with China (while maintaining Taiwan's sovereignty and de facto independence) continues to dominate the political arena, and has contributed to highly contentious inter- and intraparty competition, zero-sum politics and partisan gridlock during most of the review period.

Conflict intensity

2

'06 '18 10



## II. Governance Performance

### 14 | Steering Capability

In general, Taiwan's government sets strategic priorities and only rarely postpones them in favor of short-term political benefits. In prioritizing policy goals, Taiwan's decision-makers can draw on a wide net of professional expertise, including a well-differentiated administrative apparatus, a lively civil society and independent think tanks. In general, they use these inputs effectively. Moreover, no political actor in Taiwan departs from the basic priorities of maintaining and further developing the already high normative standards of Taiwan's market-based democracy achieved in the preceding decades. In practice, however, the government's ability to implement carefully set strategic priorities has been limited due to China's de facto veto power on Taiwan's foreign policy ambitions, and the considerable polarization in Taiwan's public sphere concerning the best approach to deal with Beijing's direct and indirect political and economic influence. The latter also continues to dominate the substantive differences between the two major party camps, leading to fierce zero-sum political competition. Given Taiwan's system of government, this can lead to deadlock in times of divided government. When the president has a robust parliamentary majority, political prioritization and wide-ranging reforms are much easier. However, for much of the review period, the KMT's control over the presidency and an almost two-third (61% of seats) majority of the KMT-led "pan-blue" camp in the legislature has not prevented intraparty infighting and political stalemate in the face of a contracting economy, the party's dismal performance in the 2014 local elections, Ma Ying-jeou's weakness due to extremely low popularity ratings, and resolute civil society opposition to the president's cross-Strait policy. Under the Tsai Ing-wen government, which has been in office since May 2016,

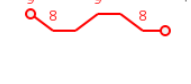
Question

Score

Prioritization

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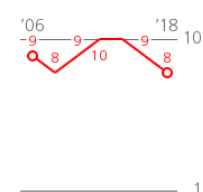
conditions for coherent policies and strategic prioritization have again been extraordinarily good, with the DPP controlling a super-majority of 60% of all parliamentary seats and at least initially very high approval ratings for the president. Moreover, already in its early months the DPP government has put on track core initiatives such as the strengthening of alternative energy sources, judicial reform and the expansion of Taiwan's welfare state. However, political maneuvers such as the September 2016 freezing of the KMT's party assets signal that the DPP government might not be above giving priority to partisan goals.

As Taiwan's market economy and democratic order are already well developed, any assessment concerning the implementation efficiency of the government's priority policies starts from an advanced vantage point. Moreover, the day-to-day implementation of political decisions by Taiwan's differentiated and professional administration works well, and there have been no cases of serious administrative obstruction or bureaucratic foot-dragging. The rapid realization of the KMT's reformist cross-Strait policy since 2008 underscores the ability of Taiwan's political and administrative system to enact systematic and speedy political change if sufficient political capital is spent. For much of the review period, however, the implementation of far-reaching reforms, such as the ratification of the highly unpopular Cross-Strait Service Trade Agreement, has been hampered by the KMT's weakness in the face of a sluggish economy, bad results in 2014 local elections, low approval ratings, and the resulting intraparty power struggles in the 2015 electoral campaign. Conditions for effective implementation have improved in the second half of 2016, with the DPP controlling the presidency and parliament, and the new government's political measures suggest an increase in the ability to implement new policies. However, the Tsai government has been criticized for failing to implement coherent policies in important issue areas such as the five-day work week, pension reforms and cross-Strait relations.

Generally speaking, political learning in Taiwan takes place in economic and social policy-making, thanks to the leadership's generally close-knit relations with well-established social organizations and interest groups who keep it informed of the need for policy adjustments and new initiatives. Taiwan also has a widely stretched system of special committees equipped with scholars and bureaucrats who are affiliated with or attached to government ministries and commissions in order to evaluate policies and give advice on identified shortcomings and necessary corrections. Policy learning has come the hard way for the KMT government, which abandoned its failed attempt to push the Cross-Strait Service Trade Agreement through parliament after the 2014 Sunflower protests and did not restart the ratification process before the inauguration of the new DPP government. Given the KMT's drastic weakness between the 2014 local elections and Tsai Ing-wen's May 2016 inauguration, there was little room for political improvement through political learning, flexibility and political innovation. The DPP and its leader, Tsai Ing-wen, in turn, have proven willing and able to reformulate their stance on cross-Strait policy in the 2015-2016 electoral campaigns,

#### Implementation

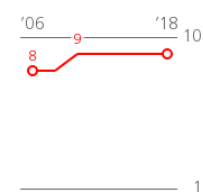
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#### Policy learning

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and successfully accommodated both their core pro-independence constituency and broader shares of the electorate, which expects a more pragmatic and less ideological approach to the party's policy toward the mainland.

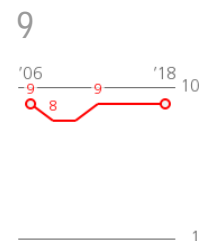
## 15 | Resource Efficiency

Taiwan has a postwar history of efficient bureaucratic policy-making, which earned it the label of a successful development state. Against this background, and compared to most countries in Asia, Taiwan's government makes efficient use of available economic and human resources to pursue its policies. While the top positions in Taiwan's government and administrative bodies are filled with political appointees who may or may not be experts in their area of responsibility, the rank-and-file is recruited according to established rules and qualification levels. As special constitutional organ, the Examination Yuan is responsible for the education, recruitment and evaluation of the country's public officials. Local government in Taiwan is divided into 13 counties, three so-called provincial cities that have the same status as counties and six special municipalities that are directly under the jurisdiction of the central government. These divisions have autonomous democratically elected legislatures and governments (magistrates in counties, mayors in cities and special municipalities) and have the power to collect taxes such as land, house and vehicle taxes. Petty corruption is not common and high-profile cases of corruption in Taiwan's bureaucratic apparatus are rare and mostly involve politically nominated public officials, not professional civil servants.

Taiwan's public sector makes efficient use of taxpayer's money. With 19.6% in 2016, government spending takes a relatively small share of GDP compared to other highly developed countries, and state budgets tend to be balanced, with a slight budget surplus of 0.13% of GDP in 2016 and manageable total state debt of 35.5% of GDP. Effective auditing is ensured through the Ministry of Audit under the Control Yuan, an independent policy body that is headed by an auditor-general nominated by the president and appointed by the Legislative Yuan. Budget planning and implementation is transparent, and both the individual ministries as well as the cabinet-level Directorate General of Budget, Accounting and Statistics (DGBAS) publishes a wide range of data on expenditures and programs.

Taiwan's resource efficiency is reflected in its good showing in a number of international indexes. For instance, it ranked 14 out of 61 listed countries in the 2016 World Competitiveness Yearbook and 14 out of 138 in the Global Competitiveness Index, both of which measure government efficiency, among other things. Worries concerning the government's budgetary reserves to refinance the various national pension fund schemes have existed for some years now and have relativized the positive picture of Taiwan's resource efficiency to some extent. Moreover, the

Efficient use of assets



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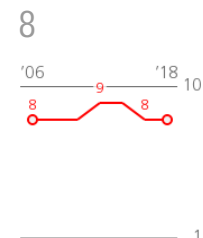
expansion of social welfare spending announced by the Tsai government is likely to put greater pressure on public budgets and taxpayers in the future.

Traditionally, Taiwan's political system has been shaped by both personal ties and bureaucratic networks stretching across all government tiers, which ensures effective policy coordination and coherent policies. It is strongly influenced by the president, who not only determines the foreign and China policy agenda but is also expected to decide on conflicting policies and competing interests within the government apparatus. Since the president nominates the prime minister without parliamentary consent, there is usually a high degree of like-mindedness between the presidential and prime ministerial offices. Structurally, Taiwan's semi-presidential system of government is best prepared for policy coordination when president and the parliamentary majority are controlled by the same party, but weakens the chances for coordination in times of divided government. However, during much of the review period, the KMT government's ability to deliver well-coordinated policies was undermined by the contracting economy, serious intraparty strife (as evidenced, most clearly, by the sacking of the KMT's presidential candidate Hung Hsiu-chu during the campaign), the party's dismal performance in the 2014 local elections and Ma Ying-jeou's extremely low popularity ratings in the last two years of his presidency. With the DPP controlling both the presidency and a super-majority in the Legislative Yuan, the chances for a coherent policy have again increased significantly after the May 2016 inauguration of Tsai Ing-wen.

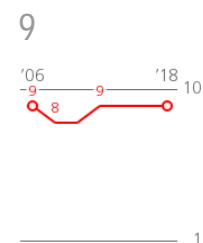
Taiwan possesses a well-developed framework of strict and stringently enforced anti-corruption regulations that target both bribery of civil servants and public officials, and commercial corruption between private enterprises. The legal framework for combating corruption is based on the criminal code and a number of "sunshine bills" that have been passed since the early 1990s, including the Anti-Corruption Act, which was last amended in June 2016. Political corruption is targeted by the Public Functionary Assets Disclosure Act of 1993, which requires the declaration of all income and assets by high-ranking officials and elected representatives. The 2004 Political Contribution Act limits political donations and makes campaign financing more transparent. A lobbying act took effect in August 2008 that requires lobbyists to register their activities and local government officials and elected representatives to inform their responsible agencies of their communication with lobbyists. The 2011 Anti-Corruption Informant Rewards and Protection Regulation has put in place a framework to protect whistle-blowers reporting corruption and defines rewards for informing the authorities of corruption cases.

A Special Investigation Division, under the Supreme Court Prosecutors Office, investigates corruption issues involving the president and other high-ranking government officials, including high-ranking military officials as well as corruption related to elections. Building off the example of Hong Kong and Singapore, Taiwan established an Agency Against Corruption (AAC) in July 2011 under the Ministry of

#### Policy coordination



#### Anti-corruption policy



Justice to make the prevention, investigation and prosecution of corruption more effective. The Control Yuan, a specific constitutional body that supervises government and public officials, partakes in the effort to curb political corruption. Its Ministry of Audit is responsible for ensuring that public resources are spent efficiently. Furthermore, Taiwan's media and public are very sensitive to political corruption and regularly play a role in exposing officeholders who have been charged with misconduct.

In 2015, 368 cases of public corruption involving 1,082 individuals were prosecuted. Local vote buying remains a serious problem in Taiwan but is considered by both politicians and voters as an inherent part of local political culture rather than political corruption. In the 2016 general elections, over 500 individual cases of vote buying were reported. Nevertheless, offenders of regulations related to vote buying and political donations are prosecuted and there is a constant tension between the legal struggle against this practice on the one hand and its perceived inevitability as a social institution on the other.

Compared to political corruption, commercial corruption is less stringently regulated and progress in this area has not been made during the review period. Politics and big business remain closely intertwined and especially in public procurement bribery of government officials and diversion of public money to the private sector has been reported. In August 2016, seven officials of Taiwan's Railway Administration were jailed in a corruption case for accepting bribes and sex services in exchange for helping private firms secure contracts for eight rail projects. Despite repeated calls for the Legislative Yuan to pass the Commercial Anti-Bribery Act to address bribery in the private sector, the draft bill remained on hold since 2014.

## 16 | Consensus-Building

All major political actors firmly agree on maintaining and strengthening Taiwan's democracy. Existing strong, and partly ideological, differences between the two main political camps concerning the proper approach toward the People's Republic of China and the independence-unification question does not undermine the overall firm consensus among elites and the public on Taiwan's identity as a democratic state.

All major political actors firmly agree on Taiwan's character as a market economy based on the rule of law, free trade and a relatively close-knit social welfare net. The existing differences between the two main political camps concerning the correct economic policy, including the degree of further integration with China's economy, does not undermine the overall firm consensus among elites and the public on Taiwan's identity as a democratic state with a market economy.

Consensus on goals

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There are no anti-democratic veto actors in Taiwan.

Anti-democratic  
actors

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The most serious domestic cleavage between advocates of Taiwanese independence and a political arrangement with China (including unification) is reflected in the ongoing division of the party system into two rival (“pan-blue” and “pan-green”) camps. In recent years, this ideological confrontation has increasingly turned into a conflict on the scope, context and strategic timing of pragmatic cross-strait policies and economic integration. During the review period, no serious progress was made to depoliticize this central cleavage, which is the only issue on which the two political party camps differ substantially, due to the heated political competition in the aftermath of the May 2014 Sunflower protests, the KMT’s crashing defeat in the November 2014 local elections and the partisan stalemate in the run-up to the January 2016 general elections. Little changed in the severity of political competition after the DPP’s landslide electoral victory, and parts of the new government’s policy agenda such as the freezing of the KMT’s financial assets and the politicized commemoration of the February 28, 1947, (“2-28”) suppression of Taiwanese protests against the KMT government are likely to perpetuate existing cleavages.

Cleavage /  
conflict  
management

8

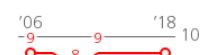


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Generally speaking, civil society in Taiwan has meaningful access to political decision-making and is considered an important contributor to the formulation, implementation and evaluation of policies. Both the DPP and KMT have close ties to and in general welcome the contribution of civil society groups in the political process. Moreover, the political system is sufficiently open to allow the direct political participation of civil society through the creation of new parties such as those that have formed out of the activist groups of the 2014 Sunflower protest movement, most notably the New Power Party (NPP), which won five out of 113 parliamentary seats in the 2016 parliamentary elections. The government sponsors regular meetings with civil society leaders and invites them to national conferences on particular problems regarding economic and social development, environmental protection or educational reform. The Ministry of Justice has a long tradition of cooperating closely with civil society organizations, and civil society plays an important role in the process of judicial reforms initiated by the new DPP government in 2016. At the same time, ideological polarization continues to divide many movements and groups, thus making it difficult for them to speak to politicians from rival camps.

Civil society  
participation

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While the conflict between Mainlanders and Taiwanese (culminating in the “2-28-incident” of 28 February 1947 when troops brutally suppressed a popular anti-government uprising) and the crimes of the KMT regime during the “White Terror” era in the 1950s and 1960s were addressed during the 1990s and 2000s, reconciliation and transitional justice have received renewed interest during the review period. In advance of the 70th anniversary of the “2-28 incident” in 2017 and playing to still deep-seated anti-KMT sentiments among parts of the DPP’s supporters, Tsai Ing-wen has repeatedly called for renewed investigation into the massacre during the 2015-2016 presidential campaign, and in her inauguration address, pledged to publish a full report on “2-28” within three years. This echoes the efforts by academics and civil society activists, who have been promoting transitional justice and the setup of a truth commission for some time to clarify the question of political responsibility and help those who were victimized during the “White Terror” tell their stories and gain compensation from the government. The KMT has refused to discuss the dark side of its authoritarian past, especially with respect to its huge party assets accumulated during the martial law period, which have made the KMT one of the richest political parties in the world, and which the DPP has wanted to recuperate for the national treasury for a long time. Shortly after the new government was in office, the DPP-dominated legislature passed the “Act Governing the Handling of Ill-Gotten Properties by Political Parties and Their Affiliate Organizations” and created a new cabinet-level investigative committee to probe into the KMT’s financial assets. Immediately after its establishment, the Ill-Gotten Party Assets Settlement Committee has declared all KMT-assets except for membership fees, donations, and government subsidies illegal, and in September 2016 has ordered the freeze of substantive financial amounts. These policies are controversial even among pro-transitional justice observers, however, who fear that they are mainly political maneuvers to weaken the KMT, which will lead to greater divisiveness instead of furthering reconciliation.

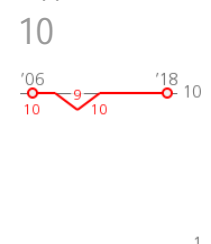
#### Reconciliation



## 17 | International Cooperation

Taiwan’s integration into the international community is constrained by China’s strict stance on banning the country’s access to all international organizations that are based on the principle of national sovereignty, which sets limits on the country’s ability to benefit from and make use of support from international partners. In December 2016, Taiwan terminated diplomatic ties with São Tomé and Príncipe, officially in response to the African nation demanding an “exorbitant” amount of financial aid. As of December 2016, only 20 countries (mainly smaller countries in Central America and Africa) and the Holy See maintain official diplomatic relations with Taiwan. Consequently, Taiwan’s reform agenda has been driven mainly by domestic considerations and public pressures, even though Taiwan’s successful transformation and continuing adherence to the principles of democracy and free market economy have been an important factor to ensure support from its international partners such

#### Effective use of support





as the U.S. Moreover, under various euphemisms for its national title, Taiwan participates in a large number of international organizations. Taiwan's reputation for adapting to new circumstances and learning from the international environment has been well known since the days of the "Taiwan miracle."

Since China prevents Taiwan's entry into most international and regional organizations and bodies which require state capacity, it is particularly important for Taiwan to demonstrate credibility, reliability and generosity in the international arena. Within the international community, the country has earned a reputation of high credibility and reliability in implementing necessary market reforms. Since its access in 2002, Taiwan has smoothly integrated into the WTO framework to facilitate global trade. It implements WTO rules well. Problems result from Taiwan's obstinacy concerning issues related to nomenclature in international organizations when it feels marginalized or discriminated against by China. Efforts by the KMT government to enlarge Taiwan's "international space" through its conciliatory cross-strait policies have mostly failed to entice Beijing to change its stance. By convincing the world's public that it rightfully claims sovereignty and that its diplomatic isolation deprives the international community of Taiwan's full expertise and financial might, Taiwan enjoys a good reputation as a political partner and engaged donor of development aid and humanitarian assistance. In recent years, it has largely abandoned "dollar diplomacy" as a means to trade financial support for international recognition, both for reasons of low effectiveness, severe public criticism and, most notably, with the goal of improving cross-strait relations. However, hopes for more "international space" and a softening of China's rigid stance restricting Taiwan's participation in the international arena have not materialized under the outgoing KMT government. Tensions across the Taiwan Strait have actually risen after the DPP landslide victory in the 2016 elections, despite President Tsai's comparatively conservative approach to cross-Strait policy that avoided any formal departure from the "1992 consensus" and called for cross-Strait dialog. However, China incrementally increased pressure on Taiwan by freezing bilateral contacts, banning official participation in international conferences such as the November 2016 UN Climate Conference in Marrakech and pressuring Taiwan's international partners into further isolating the island country.

Within the limits posed by Beijing's refusal of Taiwan's participation in international political organizations, Taiwan is a strong advocate of and reliable participant in initiatives advancing regional integration and cooperation. The country cooperates actively and successfully in regional and international organizations like the Asian Development Bank (ADB), the Asia-Pacific Economic Cooperation (APEC) and the WTO (though not under its official state name of "Republic of China"), and has observer status at the World Health Assembly. Taiwan is involved in complex territorial disputes with China and neighboring Southeast Asian countries about control over the uninhabited but resource-rich (fish, petroleum, natural gas) Spratly and Paracel archipelagos in the South China Sea. In 2015, the Ma government

#### Credibility

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#### Regional cooperation

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launched a South China Sea Peace Initiative to address the conflict by shifting the focus from questions of territorial sovereignty to jointly developing and sharing resources. A similar approach has contributed to calming the dispute with Japan over the Japanese-administered Senkaku Islands (called Diaoyu in Taiwan) in the East China Sea since the 2014 Taiwan-Japan agreement that regulates fishing in the waters around the islands.

The main issue in Taiwan's regional cooperation continues to be the relationship with mainland China, which continues to block Taiwan's inclusion in regional free trade regimes, most notably the ASEAN Free Trade Zone and the projected Regional Comprehensive Economic Partnership regime. Taiwan's further economic and societal cooperation with the People's Republic has stalled during the review period after the 2014 Sunflower protests against the KMT government's proposal of a Cross-Strait Service Trade Agreement (CSSTA). Little substantial progress has been made despite a number of high-profile direct political contacts across the Taiwan Straits, such as the November 7, 2015, meeting of President Ma Ying-jeou and China's President Xi Jinping in Singapore, the December 2015 establishment of a direct hotline between Taiwan's Mainland Affairs Council and the PRC's Taiwan Affairs Office, and the five-day visit of Taiwan's former Minister of Justice to China in March 2016. Semi-official bilateral relations across the Strait have been effectively closed down by Beijing immediately after Tsai Ing-wen's inauguration, who had declined to express her support of the so-called 1992 consensus that acknowledges the existence of a single China with different interpretations across the Taiwan Strait. Since May 2016, the Chinese government has all but terminated contacts between the mainland's Association for Relations Across the Taiwan Straits (ARATS) and Taiwan's Straits Exchange Foundation (SEF), two semi-official agencies to handle technical issues in cross-Strait relations, and the official, cabinet-level Taiwan Affairs Office (China) and Mainland Affairs Council (Taiwan).



## Strategic Outlook

Cross-Strait relations will continue to dominate Taiwan's political, social and economic development over the next years. The weakness of the KMT government in the aftermath of the May 2014 Sunflower Protests and an empowered and civil society-supported opposition have stalled further rapprochement and cross-Strait integration, both of which have become even more unlikely with the DPP's victory in the 2016 general elections – due to both the party's own ideological position and China's hostile stance toward the DPP. The ultimate objectives of China and Taiwan are certainly different: whereas the former seeks eventual unification, the latter wants to maintain sovereignty (or de facto independence). This is a basic contradiction that makes the Taiwan Strait a perennial hotspot in the regional security architecture. Against this background, it is hard to predict where relations between Taiwan and China will lead and much will depend on factors Taiwan's decision-makers cannot control, especially economic and political developments in the People's Republic, but also the policies of the new administration in the United States.

For China, the Taiwan question will continue to be a matter of national relevance, and will become more prevalent if the government in Beijing should feel pressured into more aggressive nationalist policies by intra-elite struggles or a serious economic cool down. But even below the threshold of Beijing demanding political talks on unification, much will depend on whether Beijing will continue its current aggressive strategy of undermining Taiwan's international relations, putting stress on Taiwan's economy by reducing the number of Chinese tourists able to visit Taiwan and dividing Taiwan's domestic political forces by refusing to work with the DPP and courting the KMT. Particularly worrisome is Beijing's new approach to isolate Taiwan by putting pressure on third countries to deal with Taiwan through China in international relations, which was exemplified in the (successful) demand to extradite 223 Taiwanese criminal suspects to China, not Taiwan.

The potential instability of Taiwan's long-lasting and friendly, if not always uncomplicated, relationship with the United States has been highlighted by the much-debated phone call between Tsai Ing-wen and president-elect Trump in December 2016, and Trump's protectionist rhetoric and criticism of perceived currency devaluation by the U.S.'s trading partners, which has already led to some degree of currency appreciation in Taiwan in early 2017. The greatest danger for Taiwan would be if the United States, under Trump, decides to use Taiwan as a bargaining chip in negotiations with Beijing.

In light of these external contingencies and its relatively narrow latitude for unilateral action, Taiwan's government should: (1) aim to continue its policy of strategic ambiguity toward national identity and sovereignty; (2) abstain from rash moves toward formal independence; and (3) attempt to garner international awareness and support from democratic states for its beleaguered position and help bolster it against China's aggressive moves to further limit Taiwan's international space. The new government should also attempt to establish trust with its main political rival, the KMT, in order to minimize Beijing's ability to divide political forces on the

island. The main imperative would be that the DPP not abuse its tremendous political power to damage the KMT, including its future chances of winning elections. In this regard, the government's hasty attack on the KMT's party assets is highly troublesome. At the same time, the KMT needs to pacify its destructive internal conflict to become a functional oppositional party again, and should resist China's efforts to draw the party in and split Taiwan's political landscape, not least to avoid being perceived by voters as a disloyal opposition, which would only further undermine public trust in parties and political representatives. Consequently, it should consider the medium-term implications of much publicized, high-profile visits such as the November 2016 trip of KMT chairwoman Hung Hsiu-chu to China. Finally, the Tsai administration should address the growing public disillusionment with established political institutions and very low approval of political representatives through measured political reforms and effective policies. The new government's comprehensive and inclusive approach to reforming the judiciary, which by many Taiwanese is considered ineffective and unfair, is a very good start, provided it is not abused for partisan short-term political gains. Others include the further development of the welfare state and, most importantly, stabilizing Taiwan's economy.