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India–Taiwan Economic Partnership
Building a New Growth Model

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A dynamic democracy and home to the world's leading ICT technology and knowledge-based services, Taiwan is now looking beyond its traditional trading partners and investment destinations in China and Southeast Asian countries, towards India as one of its most strategically important economic partners in its expanded "Go South" policy, for the next decades. Business interests in Taiwan, starting with the ICT industry and expanding to other sectors, have driven considerable Taiwanese business delegations to visit India to explore emerging trade and investment opportunities.

India adopted a Look East policy since 1991. Despite this, the compound economic GDP growth rate between 1990 and 2010 reached only 6.6 per cent. Thus, the total trade linkages and economic integration between India and the Southeast and East Asia have yet to meet the business community's expectations. Being an active player in the region, Taiwan has all the potentials to be India's strategic economic partner in the "Era of Asian Economic Integration". It is, therefore, of timely significance to review India–Taiwan trade and economic relations, and provide new directions for Indian policy makers and business leaders for enhancing bilateral economic relations.

The Taiwan Economy

Taiwan has enjoyed a significant economic growth rate between the 1970s and the 1990s, and is recognized as one of the four "Asian Tigers", along with Singapore, South Korea and Hong Kong. During this period, real GDP growth rate has averaged about 8 per cent. However, Taiwan had also faced increasing land and labour costs. Exports also suffered due to the appreciation of the New Taiwan Dollar against the US dollar.

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Since the 1980s, Taiwan has been forced to undertake industrial re-structuring by off-shoring its labour intensive manufacturing industries to Southeast Asia and China, while promoting technology industries and more value added services at home.

Being a small island country, with a population of 23 million, Taiwan has been an outward economy, highly dependent on global demand for its own economic growth. With the continuous expansion of Taiwanese investment in Southeast Asia and China, the rapid development of the electronics and machinery industries, and strong exports has not only fuelled Taiwan's economic development in the 1990s and 2000s but has also led to the establishment of regional production networks and value chains centered around Taiwan.

The first "wave" of substantial overseas investment by Taiwanese firms began in the late 1980s, beginning in Southeast Asian countries, and then expanding to China. According to the Investment Commission, the Ministry of Economic Affairs (MOEA) of Taiwan, government-approved outbound investment projects amounted to a total of US$ 77.4 billion from 1952 to 2012. The foremost destination was Asia, receiving more than one third of the total investment.

However, this official data does not include Taiwan's investment in China. Due to political rivalry across the Taiwan Straits since 1949, the Taiwan government did not opened investment in China until 1992, when the then President Lee Tung Hui decided to officially relax bans on cross straits economic exchanges, and allowed trade with and investment in China.[1] During 1990–2012, the government had approved more than 40,000 investment cases in China, with a total investment of US$ 124.5 billion. It is informally estimated that, if unreported or indirect investment is included, investment in China by Taiwanese firms may well reach US$ 250 billion, accounting for more than 70 per cent of Taiwan's total overseas investment. This high concentration, together with the fact that exports to China comprise around 40 per cent of Taiwan's total exports, makes the issue of Taiwan's economic dependence on China more acute.

India-Taiwan Economic Relations

India and Taiwan did not have strong economic and commercial relations until the late 1990s, after the governments of both countries decided to mutually designate representative offices, the India-Taipei Association (ITA) in Taipei, and the Taipei Economic and Cultural Center (TECC) in New Delhi – in March 1995 to promote trade, investment, and other aspects of bilateral cooperation. It is seldom mentioned that economic ties between India and Taiwan were developed much earlier, and can be dated back to the 1980s, when Indian firms opened up subsidiaries or trading companies in Taiwan. Their functions mainly included sourcing consumer products from Taiwan, and exporting gold, silk and other natural resources to Taiwan. However, in the 2000s, most of these trading companies closed, and moved to China following the movement of Taiwanese firms that began to set foot in China after the prohibition of investment was officially lifted in 1992. The retreat of the Indian trading companies in Taiwan was a signal of the substantial "movement" of Taiwanese firms to China.

In 2003, the Ministry of Economic Affairs, Taiwan, decided for the first time to add India in the priority export markets of a series of government trade promotion programs. Most Taiwanese firms began to take interest in the emerging market and, since then, bilateral trade began to grow. The past decade has witnessed bilateral trade increase at an average 2 digit rate, and reach a historic high at US$ 7.57 billion in 2011.

Mutual investment flows between India and Taiwan had been very low until early 2000s when India was included in an expansion program of Taiwan's "Go South" policy. The "Go South" policy was first adopted in 1994, when the Taiwan government tried to distract Taiwanese firms from investing in China by providing region-specific investment incentives and "administrative guidance" to lead investment flows, particularly into Thailand, Indonesia, and the Philippines in the Southeast Asia region. India was added at a later stage when the policy was further expanded. However, to most Taiwanese firms, India in these years was considered as an extension of the Southeast Asian region, and not a separate potential market.

It is important to note that there is a close correlation between Taiwan's interests in India and Taiwan's interests in China. Starting from mid-2000s, when the investment environment in China began to appear less favorable, some Taiwanese firms began to look outside China in search of both overseas investment destinations and new markets to diversify dependence on China. Wage increases, the shortage of labour in the south eastern coastal provinces of China, and the enforcement of new labour and environmental laws all drove an increasing number of Taiwanese firms away from the once "world factory". India and some Southeast Asian countries, such as Vietnam and Indonesia, naturally became new attractions with their abundant workforce and relatively low wages.

According to a report released by FICCI, most large Taiwanese ICT and electronics firms have a presence in India, including Delta, Lite-on, Synnex Tech., Asus Tek, BenQ, Acer, Media Tek, and the world's largest electronics contract manufacturer Foxconn, among others. However, the total volume of FDI inflows from Taiwan to India has remained very low. According to DIPP statistics, total investment has been only around US$ 66 million, representing 0.03 per cent of total investment flows received by India during the period of January 2000 to December 2012. It is noteworthy that the FDI inflows from Taiwan in the past four years (2009–2012) have demonstrated a significant increase. FDI volumes in these four years reached US$ 46 million, comprising around 70 per cent of the total accumulated FDI since April 2000. The sharp growth contrasted with the consecutive decline of FDI flows from Taiwan to China since 2009. This implied that Taiwanese firms are "returning" to Southeast Asia, some moving to India, after leaving investment in China since the late 1990s. India is, in this context, receiving growing attention from Taiwan.

It is important to note, however, that there is a huge gap between DIPP official data and informal estimation by TECC of Taiwan in New Delhi. According to the TECC informal survey, if one takes a broader definition of "Taiwanese firms operating in India" and include both direct and indirect investment by Taiwanese firms, realized and planned investment may total around US$ 1.4–1.5 billion. This difference indicates that Taiwanese firms tend to prefer to "detour" their way when investing in India due to tax or other operational reasons. It also means that India, data may not be capturing the actual investment by Taiwan in the country, and hence underestimates the growing potential of Taiwanese investment coming to India.

Why Taiwan Matters to India

Taiwan is a small economy, with a population of 23 million. The scarcity of natural resources, and increasing land and labour costs have driven Taiwanese firms to relocate their manufacturing factories in Southeast Asia and China, while those operating in the island managed to upgrade in order to differentiate from their competitors in the host countries. Following the labour intensive industries, more technology- and capital-intensive industries also began to set foot in China, targeting the huge Chinese domestic market. According to 2012 UNCTAD World Investment Report, in 1990 outward FDI Stock of Taiwan was reported at US$ 30.36. In 2011, the volume reached US$ 213.06–around 4 times the volume of inward FDI stock.

The production networks established by Taiwan-invested manufacturing operations in China and Southeast Asia have not only created millions of jobs across the countries but have also helped develop manufacturing industries, as also made possible economic restructuring in some host countries. For example, in the 1990s, more than 2,000 Taiwanese electronics firms invested in Penang, Malaysia, and helped establish one of the most important electronics clusters in Southeast Asia at that time. In China, Taiwanese firms have also been important players contributing significantly to the development of the private sector and various manufacturing industries, ranging from textile and garment, footwear, toys to electronics and electrical machinery. Benefitting from capital, technology and management knowhow brought by Taiwanese firms, economic modernization in the eastern coastal provinces of China began to take place, followed by provinces in the Yangtze River Delta.

In 1989, Taiwanese firms again became the "Pioneers" in Vietnam when the Socialist country first opened its door to foreign investors. In the following years, till the late 2000s, Taiwan had remained top investor in the country, accumulating FDI volume reaching US$ 23.52 billion in 2011.

These days, Taiwanese firms are hustling off to another resource-rich emerging market in the region – Myanmar. Starting with small and medium sized firms followed by larger ones, these firms have explored every possible opportunity to build business ties with the country. Though the government of Myanmar has avoided developing official relations with Taiwan due to its "One China" policy, the private sector in this country embraces Taiwan with open arms. The Taiwanese investor is different from Chinese firms (which focus on mining, infrastructure and power plants), or from Korean and Hong Kong investors (who focus mainly on real estates and natural resources), in always concentrating on manufacturing industries. Technological distribution and industrial upgrading are hence made possible.

How do the production networks and supply chains work? For example, Taiwan is known to be a hub of ICT production. Taiwan firms produce more than 80 per cent of notebook computers and their peripherals. Most of the production is not in Taiwan. Some parts are made by factories in Guandong province, China, while others are made in Malaysia and the Philippines. The R&D function is maintained in the headquarters or in the mother companies in Taiwan. With operations in different countries, Taiwan is *de facto* integrated into the regional economy, though officially, Taiwan is not a member of the ASEAN nor has it signed any ASEAN+1 FTA with the ASEAN.

In 2011, the Indian government passed the New Manufacturing Policy envisaging the establishment of mega-manufacturing hubs to attract foreign investment. The utmost goal is to increase the share of the manufacturing sector in GDP from 16 per cent to 25 per cent by 2020. However, it is reported that the investment inflows after the announcement of the policy have not been phenomenal. In this regard, the experiences, technology and knowhow of Taiwan in developing production networks and value chains are of strategic importance to India. Taiwan can play a vital role in helping India to realize its New Manufacturing Policy and build a stronger manufacturing sector.

India has not been a favourable investment destination for manufacturing industries. This can be reflected in the FDI statistics released by DIPP, Ministry of Commerce and Industry. According to DIPP, in terms of sector wise FDI equity inflows during the period of April 2000 to April 2013, six out of the top ten sectors that have received the most FDI in India were services sectors, which include services, constructions, telecommunications, computer software, hotels and tourism. The only four manufacturing sectors among the ten sectors are drugs and pharmaceuticals, chemicals, automobile industry and metallurgical industries. During this period, FDI inflows in services sectors (including financial, banking, insurance, business, outsourcing, R&D, courier, tech. Testing and analysis, etc.) reached US$ 37.47 billion, together with FDI inflows in construction development (including townships, housing, built-up infrastructure and construction-development projects) totalling US$ 22.22 billion, comprising of more than one third of the total FDI inflows into India.

The lack of strong industrial foundations, and very complicated central and state-level tax and legal systems make manufacturing in most states in India difficult and costly when compared with China and most Southeast Asian countries. Due to difficulties in domestic sourcing, manufacturers have to import raw materials or semi-finished products, key components and parts for production from other countries. If India can promote the integration of Taiwanese firms in upstream and downstream industries, and with other necessary components and parts suppliers, such vertical investment can help build Indian domestic manufacturing.

For example, India is well known for its comparative advantage in software and services, while Taiwan is a dominant producer and exporter of ICT goods. There is huge potential of benefits if the two countries can collaborate in the ICT industry. Recently, Taiwan has begun to show a fair amount of interest in the ICT sector in India. Several leading Taiwanese firms, such as Foxconn, Wintek Technology, D-Link, Synnex Tec, AsusTek Computer Inc, Acer and Benq, have already established their presence in India. Most of them are services, or sales, and distribution offices.

Moreover, the fact that India has not been able to develop diverse and strong manufacturing industries has, to a large degree, become an obstacle to the country's economic restructuring, and the pursuit of further economic growth. It is also the main reason for the constant deficit in the balance of payments, trade deficit, and high unemployment rate. Moreover, as the East and Southeast region is accelerating economic integration, India needs to build a strong manufacturing sector, or otherwise it will lose to the competition with China and other ASEAN member states, and turns to serve only as a market for Chinese, Japanese and Korean brands.

The Possibility of an India–Taiwan Economic Cooperation Agreement (ECA)

In January 2011, the Indian Council of Research on International Economic Relations (ICRIER), and a non-profit research institute in Taiwan, Chung Hua Institution for Economic Research (CIER), signed an MOU to conduct a two-year joint study on enhancing trade, investment and economic cooperation between the two countries. In September 2013, the joint study report will be published, and made available to the public who take interests in seeing more business opportunities arising from an enhanced India-Taiwan trade and economic relationship. One of the findings of the joint study is that India and Taiwan have high complementarities in trade and industrial structure. The think tanks, therefore, strongly propose to both governments to review current economic relations and stock-take all existing barriers and obstacles, and establish a TECC–ITA working group[2] to examine the possibility of a bilateral Economic Cooperation Agreement (ECA).

According to the study, India and Taiwan both suffer from tariff and non-tariff measures and trade potentials are hence not fully realized. The reduction of tariff will not only bring considerable economic benefits to India, but also help develop a stronger manufacturing sector in India by encouraging more Taiwanese firms to invest in India.

In June 2010, Taiwan and China signed an Economic Cooperation Framework agreement (ECFA), which mandates both governments to complete negotiation of four agreements that make a complete package of the Cross Straits Free Trade Agreement. These four agreements include a trade agreement on goods, a trade agreement on services, an investment agreement, and a dispute settlement mechanic. In May 2013, the trade agreement on services was negotiated, but not yet reviewed and ratified by the parliament. In June, Taiwan further signed a Free Trade agreement with New Zealand.

It is of timely importance to examine bilateral economic relations between India and Taiwan, and consider more pro-active actions to enhance existing economic cooperation, including considering possibility of an India–Taiwan ECA.

Enhancing Economic and Industrial Cooperation in RCEP

In 2011 the ASEAN invited six of its FTA partner countries, namely China, Japan, South Korea, Australia, New Zealand and India, to discuss how ASEAN and these countries can work together towards a more integrated economy in the region. The Leaders decided to negotiate a Regional Comprehensive Economic Partnership (RCEP) and launched negotiations among the 16 countries in May 2013. The goal is to conclude and sign the RECP by end of 2015, together with the realization of the ASEAN Economic Community (AEC) as mandated in the 2015 Vision by ASEAN Leaders.

The AEC is to integrate ASEAN Member States into a single market and single production base, supported by and in collaboration with neighbouring FTA partner countries. The RCEP negotiation will establish the world's largest FTA in the world, comprising of 3.3 billion of population. The ample supply of young labour force and an emerging middle class in the RCEP promise huge potential benefits from an integrated regional economy. In addition, thanks to the decade long implementation of tariff reduction and the gradual removal of restrictions of Foreign Direct Investment (FDI) committed in the ASEAN+1 FTAs, complicated regional production networks and supply chains have been built through foreign investors in joint efforts with their local business partners, particularly in China and some ASEAN Member States, such as Singapore, Thailand, Malaysia and Vietnam. These regional production networks have benefited participating ASEAN Member States in the past two decades by building up manufacturing bases directly or indirectly supporting exports to international markets. The decision to negotiate the RCEP will further enhance opportunities of RCEP member countries participating in the regional production networks. However, these will also a pose challenges for those countries that are not a part of the production networks.

India has adopted the Look East policy since 1991 to strengthen economic exchanges with Asia, particularly ASEAN Member States. However, though India is gradually taking part in the regional production networks, India's role has not been highly visible, and has focused mostly on the low level of "value-addition" in the region.[3] This is reflected in the low and stagnant share of manufacturing to GDP in India. Therefore, one of the policy goals of the recently announced National Manufacturing Policy (NMP) is to address the need to enhance India's involvement in the regional economy, and strengthen India's manufacturing competitiveness. The need to realize this policy goal is now more acute when ASEAN Member States and their FTA partner countries are moving towards the formation of the RCEP.

India and Taiwan can work together in participation in the regional production networks. The past five decades of industrial development and overseas investment in the region have enabled Taiwan to stand at a preferential position in the regional product networks and supply chains. These days, an increasing number of Taiwanese firms are relocating their manufacturing bases away from China, and consider India as a potential new "Asia Factory". Moreover, India and Taiwan can also work together to improve the productivity and quality in India's manufacturing sector. There are ample opportunities for India and Taiwan to develop a comprehensive partnership that covers cooperation in high value added manufacturing industries and knowledge based services, R&D collaboration, and joint human resource development, among others.

Notes

[1] The government of Taiwan had adopted a No-Engagement policy with China since 1949, until Present Lee relaxed the ban and allowed Taiwanese citizens to visit China, and open indirect trade and investment in 1992.

[2] The Taipei Economic and Culture Office (TECC) and India–Taipei Association (ITA) are representative offices set up by Indian and Taiwan governments in each other's capitals; they provide services including the issuing of visas, and the promotion of trade and investment.

[3] Rajat Kathuria, Global Value Chains in the Indian Context, Presentation at the OECD Global Value Chains Meeting, Paris, 19 March 2013 http://www.oecd.org/dev/partnerships-networks/Session2_R.%20Kathuria.pdf

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