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The Security Assistance for Taiwan Debate: FMF Loans versus Grants

By: Russell Hsiao

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As tensions mount in the Taiwan Strait and concerns about a military conflict grow, the US Congress has been actively discussing and planning for new ways to facilitate the flow of military capabilities to Taiwan amid slowdowns caused by other processes and considerations. Even before Russia’s invasion of Ukraine, Senator Josh Hawley (R-MO) and Representative Mike Gallagher (R-WI) in 2021 introduced the [Arm Taiwan Act of 2021](#), followed later that year by the [Taiwan Deterrence Act](#), introduced by Senator James Risch (R-ID). These bills would each authorize the United States to offer Taiwan military assistance or foreign military financing (FMF) in order to expedite the means by which the island-democracy could acquire defense articles and services necessary to help it defend itself. These calls have occurred against a backdrop of rising concern among senior US military planners, who in recent years have begun sounding the alarm about the possibility that the People’s Liberation Army (PLA) could invade Taiwan as early as [2025](#) or [2027](#).

Eligibility for the FMF program is determined by the Department of State and executed by the Department of Defense. FMF determination enables recipient nations “to purchase US defense articles, services, and training through either foreign military sales (FMS) or, for a limited number of countries, through the foreign military financing of direct commercial contracts (FMF/DCC) program.” FMF may be provided to a partner nation on the basis of either a [grant or direct loan](#). This unique program is currently offered to only a select few US security partners, including countries such as Israel, Jordan, and Egypt.

The Debate Over Grants vs. Loans for Taiwan in the 2023 NDAA

At least initially, there was notable pushback against these proposals: primarily focused on Taiwan’s status as a relatively wealthy country not in need of financial assistance, as well as concerns that mandating the purchase of certain equipment would be too heavy-handed, and would infringe on Taipei’s sovereign decision-making to purchase the types of equipment that best meet its own objectives. However, the pro-

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posal was generally met with warm receptions from Taipei and its supporters for potentially opening new modes of defense and security cooperation between the United States and Taiwan. In analyzing the content of the two initial bills, GTI Senior Non-Resident Fellow [Michael Mazza](#) observed, “A key insight inherent in both bills is that the current American approach to assisting Taiwan in defending itself has proven insufficient. Arms sales remain a crucial and necessary component, but they have failed to provide Taiwan with the full spectrum of needed capabilities at a suitably rapid pace.”

The general language of the 2021 legislative proposals was eventually included in the 2023 *National Defense Authorization Act (NDAA)* that was passed by Congress and signed into law by President Joseph Biden in late 2022. Specifically, the [2023 NDAA](#) stated that “there is authorized to be appropriated to the Department of State for Taiwan Foreign Military Finance *grant* assistance up to \$2,000,000,000 for each of the fiscal years 2023 through 2027.” If included, the authorization would have made up a significant portion of the total USD \$6.1 billion for FMF enacted in the [2023 budget](#).

Despite the authorization of FMF grants by the committees of jurisdiction, in the [Consolidated Appropriations Act](#)—which was passed into law after the authorization bill came into effect—[appropriators in Congress](#) only included the approval of loans, with no mention of the grants. The language of the [relevant appropriations](#) states “that the gross principal balance of such direct loans shall not exceed \$2,000,000,000, and the gross principal balance of guaranteed loans shall not exceed \$2,000,000,000.” The inconsistency of the authorization bill with the appropriation bill underscores a frequently misunderstood aspect of the US policy process: that the [US Constitution](#) mandates that “the power of the purse be exercised through the lawmaking process, allowing Congress to craft the terms of appropriations or deny appropriations outright through legislation.” In effect, this means that the critical decision of ultimate appropriation is determined by a relatively small committee of members.

This obvious but critical difference between a loan (which would have to be paid back) and a grant (which would not) is now the focus of heated policy debates. As noted earlier, while the NDAA 2023 included provisions for the authorization of up to USD \$2 billion in FMF for Taiwan, it did not clarify whether this funding would be provided as a grant or loan. Consequently, the Consolidated Appropriations Act that was legislated at the end of 2022 only appropriated up to USD \$2 billion in loans for Taiwan in 2023. Moreover, the interest on the authorized loans would make it more cost-effective for Taiwan to take out its own loans

to purchase the equipment, if they wanted to purchase them at all.

The Debate Continues in 2023

This apparent disconnect in authorizations and appropriations prompted several senior Republican members of Congress to issue a [letter to the Biden Administration](#) in February 2023, calling on the executive branch to increase its budget request for FMF grants in the 2024 budget request. In the letter, the members noted: “The loans included in the most recent appropriations bill are potentially helpful, but without FMF grants, loans are not enough to address the scale of this challenge.” In calling on the executive branch to include funding for military assistance grants for Taiwan, the lawmakers concluded that: “This would signal to Congress and Taiwan that the administration in fact prioritizes resources for the policies it has publicly supported and signed into law.”

When asked about the implications of the appropriation of FMF loans rather than grants, [Randy Schriver](#), chairman of the Project 2049 Institute and the former assistant secretary of defense for Indo-Pacific security affairs under the Trump Administration, noted:

[T]he fact of the matter is the FMF tool in the form of loans is not likely to be leveraged because our friends in Taiwan...are wealthy enough to invest through the FMS channel or direct commercial sale channel. [...] [N]o matter what the particular vehicle for security assistance, I think the more fundamental question is coming to the meeting of the minds with Taiwan on what those priorities should be [...] Our friends in Taiwan are dealing with coercion every day and are very much interested in being able to meet that coercion challenge with intercepts and presence [...] if the Congress is able to say this [is] important enough—not only for Taiwan but more importantly to US security interests for Taiwan to have additional capabilities [that] we think it’s so important that we will be part of the funding ourselves then [...] I’m for it.

Conclusions

After two years of intense debate following the initial introduction of the military assistance and FMF legislations, the policy arguments are no longer centered on whether Taiwan should be considered a FMF security partner. Instead, they are more specifically focused on how this growing and evolving defense partnership could be more optimally prioritized and structured. However, Congressional appropriators remain narrowly focused

and skeptical of Taiwan's *need* for grants from the United States.

The clear upside to FMF grants for Taiwan is that it would give Washington more skin in the game in determining, in consultation with Taipei, the exact capabilities that are necessary for the island's self-defense. It would also help to relieve domestic political pressure within Taiwan against raising its defense spending by pushing back against the [misleading narratives and myths](#) that are commonly associated with US arms sales. Finally, and perhaps most critically, it would immediately make available a sizeable increase in defense spending that could rapidly augment the type of defense capabilities that Taiwan needs to deter China. This is especially crucial now, as the [intelligence community](#) has assessed that Xi Jinping (習近平) has ordered the rapidly-modernizing PLA to have the *capabilities* to invade Taiwan by 2027. It is worth remembering that it took nine years for Ukraine to field the capabilities that it has now in defending against Russia's invasion.

As Taiwan is unlikely to take the FMF loans due to the aforementioned reasons, this could potentially renew the lingering impression of some in the United States that Taiwan is not serious about its defense. However, this would be a flawed understanding of the budgetary processes of both sides. Additionally, it is worth noting that Taiwan already spends around 30 percent of its central government's [annual budget](#) on defense-related expenses, and the [budget for 2023](#) is also significantly higher than that of the previous year.

As Taiwan readies for its national elections to be held in January 2024, Washington should also be mindful of how US arms sales to Taiwan could play out politically within [Taiwan's raucous political debate](#). Indeed, when the original bills proposing military assistance and FMF were introduced, [Mazza](#) observed that "opposition politicians in Taiwan have already raised [concerns](#) the bill will impinge on its sovereignty. Because both bills so openly treat Taiwan as a junior partner, they threaten to undercut the *diplomacy* that is desperately needed to ensure an effective combined defense."

In an increasingly tight budgetary environment for the United States—particularly after the Russian invasion of Ukraine—the debate over a distinction between urgency and imminency takes on a different meaning. To be clear, the fact that something may not be *imminent* does not make it any less *urgent*. Accordingly, policymakers interested in arming Taiwan will need to strike a fine balance as they negotiate budgetary issues. One workable solution under consideration may be to provide smaller FMF grants to Taiwan in stopgap measures, which could pri-

oritize the capabilities that Taiwan needs right away. Whatever appropriators ultimately do, working through this process now would ensure that if the time comes when Congress would need to rapidly flow capabilities to Taiwan, it has the legislative procedures in place to do so. Neither party can afford to be penny wise and pound foolish, because the costs would undoubtedly be much higher later.

The main point: While recent US Congressional bills have provided avenues to provide Taiwan with crucial FMF, disconnects between authorizations and appropriations—as well as a lack of understanding regarding budgetary processes on the Taiwan side—have weakened the policy. In order to ensure that Taiwan is not caught unprepared for a Chinese invasion, US policymakers should work to streamline and clarify the process for providing FMF grants to Taiwan.

(The author would like to thank GTI Intern Melynn Oliver for her research assistance.)

KMT Factional Divisions and their Implications for the 2024 Election

By: Zaki Atia

Zaki Atia is a Spring 2023 intern at the Global Taiwan Institute.

The opposition Kuomintang (KMT, 國民黨) delivered a strong performance during the November 2022 ["9-in-1" elections](#), in which the KMT candidates won 13 of the top political posts in local government across 22 appointments. However, it remains too early to conclude that a monumental shift in Taiwanese politics, or "blue wave," is underway. Looking at other recent election cycles, while the KMT fared exceptionally well in the 2018 midterms, it nevertheless experienced a catastrophic defeat to the Democratic Progressive Party (DPP, 民進黨) during the 2020 presidential election—thereby indicating that a strong midterm result does not directly translate into a national election victory. As it approaches the upcoming 2024 presidential election, the KMT has several challenges ahead. First, while local elections tend to emphasize domestic issues such as fiscal policy and infrastructure, cross-Strait relations and issues of Taiwanese identity play a larger role in national elections. As the party that still advocates for the electorally handicapping ["1992 Consensus"](#) (九二共識), the KMT is disadvantaged on this front. Second, when looking at two key variables that are strongly correlated with voting behavior—party identification and national identity—the DPP maintains a [growing lead over the KMT](#) in

both of these categories.

Due to the structural disadvantages the KMT faces on cross-strait policy, as well as shifting Taiwanese demographics, the party still has a tough road ahead leading up to the 2024 presidential election. Opinion polls have clearly demonstrated that the majority of Taiwanese are opposed to unification with China, though most also believe there is no need to formally declare independence, a middle-ground that the [DPP has successfully occupied](#). The challenge for the KMT is to reclaim its position as the “mainstream” party, a goal that will likely only become viable if the KMT were to revise its divisive China platform. Despite its losses against the DPP in the past two presidential elections, [Nathan Batto](#) notes that the KMT has consistently “proven unwilling or unable to move to a new position through internal party mechanisms.”

The primary reasons for the KMT’s reluctance to reform the so-called “1992 Consensus” and other elements of cross-strait policy are the continuing factional divisions within the party. From an outside perspective, it may appear obvious what the KMT needs to do to maximize its chances of winning. However, the older, more conservative, and more pro-unification wings of the party still wield a significant degree of influence over party platforms and personnel. In the lead-up to the 2024 elections, will these factional divisions continue to hinder the KMT’s ability to produce a tenable candidate and policy platform?

An Overview of KMT Factional Composition

The KMT’s factional composition consists of three broad main groups. First is the so-called “Mainlander” faction (外省派), in which former President Ma Ying-jeou (馬英九) still exercises significant influence behind the scenes. As the party’s mainstream faction, it remains highly committed to signature policies representative of Ma’s legacy, such as the “1992 Consensus.” The second faction is [Huang Fu-hsing](#) (黃復興), a veterans’ organization that is highly effective at mobilizing votes among retired military personnel. The organization typically holds “deep blue” positions, such as a [hardline pro-unification stance](#). The third is the local “Taiwanese” faction (本土派). While this group has the requisite ideological flexibility to push for internal party reform, it has historically struggled to accumulate political clout ever since the departure of its [two most prominent leaders](#), Lee Teng-hui (李登輝) and James Soong (宋楚瑜). On balance, the ineffectiveness of the local faction largely leaves the Mainlanders and Huang Fu-hsing as the most prominent players within the KMT, even as their policies have grown increasingly unpopular among the general electorate. This mismatch between

the views of influential voices in the party, and the attitudes of median Taiwanese voters, represents the core element of the KMT’s electoral difficulties.

The Lessons of Johnny Chiang

The local Taiwanese faction has previously tried to present a more electorally viable party-wide position, but [generational differences](#) within the party have hampered progress. One recent example emblematic of this tendency was the brief tenure of Johnny Chiang (江啟臣) as chairman of the KMT in 2020. Chiang initially rose to prominence as a legislator who branded himself as a different breed of KMT politician, willing to put forward a reformist vision. As chairman of the party, he introduced a proposal for a [KMT “redesign,”](#) which notably distanced the party from the controversial “1992 Consensus” and emphasized the importance of safeguarding the Republic of China’s (ROC) sovereignty, democracy, and human rights.

However, former President [Ma strongly opposed this proposal](#). Within three days of Chiang’s initial attempt to reorient the party, he met with Ma and substantially revised his plans: he included the “1992 Consensus” as the basis of for cross-strait dialogue, while stressing the importance of opposing Taiwanese independence. The final “redesign” was almost entirely consistent with Ma’s vision, suggesting that Chiang’s efforts had been stymied.

This episode demonstrates how Chiang’s local faction lacked the political capital to enact change. While Chiang was nominally the chairman, the party—at least in terms of its official positions—was still under the *de facto* leadership of Ma Ying-jeou. The KMT experienced an [increase in party identification](#) under Chiang’s leadership, implicitly indicating broader public support for the new direction the party was heading in. Despite this, Chiang still [lost his party chair re-election bid](#) to Eric Chu (朱立倫), a traditional KMT politician affiliated with the Mainlander branch of the party.

In short, whenever new voices are daring enough to reflect on the KMT’s lack of electoral viability and aim to revise the party’s platform—particularly as it pertains to China—they quickly face opposition from the KMT mainstream.

Candidate Selection and Factional Politics

According to recent [survey data](#), New Taipei City Mayor Hou You-yi (侯友宜) is the most popular candidate amongst potential KMT presidential nominees, even faring better in some polls than the presumptive DPP contender Lai Ching-te (賴清德). However, it is unclear whether Hou himself wants to run,



Image: Senior KMT leaders, including current Chairman Eric Chu (center), Vice-Chairman Andrew Hsia (second from left), and former President Ma Ying-jeou (right) at a campaign rally prior to the November 2022 elections. (Image source: [New Bloom Magazine](#))

as he was recently [re-elected for his second term](#) as mayor. Han Kuo-yu's (韓國瑜) experience in the aftermath of his failed 2020 presidential bid exemplifies the political consequences of prematurely abandoning your mayoral post to run for president.

Hou's popularity largely stems from the fact that he [belongs to belongs to no KMT faction](#). He is neither known as a "deep blue" politician nor a reformer. Instead, he is well-liked for his [competent governance](#) as mayor of New Taipei City. Indeed, his lack of factional ties is simultaneously his biggest source of strength and weakness. Thus far, he has been able to avoid controversial partisan statements that could alienate large swathes of the Taiwanese electorate. During Hou's 2022 mayoral debate, for instance, he presented himself as a "[light blue](#)" candidate—who avoids direct criticism of the Tsai Ing-wen (蔡英文) Administration, and comments very little on cross-Strait relations.

However, it remains unclear how sustainable this position is. To secure enough votes within the party to secure the nomination as the KMT's presidential candidate, proving partisan loyalty is vital. Indeed, traditional KMT elites have historically been suspicious of Hou on the grounds that he was originally promoted to his role as director-general of the National Police Agency (NPA, 內政部警政署) during the administration of the DPP's [Chen Shui-bian](#) (陳水扁). Furthermore, while the issue of cross-Strait relations can be avoided in local elections, the Taiwanese public tends to be more sensitive to this issue during [presidential elections](#). DPP politicians such as Lin Chia-lung (林佳龍) have already criticized Hou for what they label as a deliberately vague cross-Strait policy that fails to address difficult questions regarding the "1992 Consensus" or the "one-China principle" (一中原則).

This leaves Hou You-yi in a bind, as he is unlikely to be able to maintain his vague, non-committal cross-Strait policy. While he can distance himself from traditional KMT policy platforms to maintain his popularity as a more moderate, "light blue" candidate, this would likely come at the expense of party support during the nomination process. Alternatively, he could increasingly make statements implying his tacit approval of traditional KMT policies to curry favor with the old guard, but in turn lose the support of the average voter. It is very possible that Hou will be forced to embrace divisive positions under the pressure of KMT leadership. While he may seem popular now, in the eyes of the electorate, Hou may become a wholly different candidate by the time election season comes around.

The current party Chairman Eric Chu is another potential presidential nominee who has stronger ties to the Pan-Blue base. However, his antiquated views on cross-Strait relations, as well as his poor [overall popularity ratings](#), cast serious doubts on his viability as a presidential candidate. Meanwhile, the business mogul [Terry Gou](#) (郭台銘) remains a potential disruptor for the KMT nomination process, and boasts a considerable amount of popularity. However, he faces several obstacles to running—most notably, his withdrawal from party membership in 2019.

2024 National Election Platform: Dogma over Popularity?

Regardless of who the KMT selects as their 2024 standard-bearer, it is unlikely the party will significantly revise its approach to cross-Strait relations. From the case of Chiang's failed party redesign, to Vice Chairman Andrew Hsia's (夏立言) recent [visit to China](#) reaffirming the KMT's adherence to the "1992 Consensus," it is clear the old guard is not ready to embrace reform.

To make its position more attractive, the KMT establishment will likely look for inventive ways to frame the DPP as the party disrupting the status quo. During the lead-up to the 2022 local elections, [Ma](#) brashly asserted that "a vote for the DPP is a vote to send our youth to war." These comments could be seen as an indirect criticism of Tsai's [military restructuring legislation](#), which aims to extend conscription from four months to one full year for men born after 2005. Moves such as these, the KMT will likely contend, are dangerous and unnecessarily ideological efforts to seek Taiwanese independence and provoke China. As the conscription policy will chiefly impact Taiwanese youth, a voting base the [KMT](#) has historically had a hard time appealing to, this campaign tactic may reflect an attempt to secure their support. However, it is notable that a recent [poll](#) shows that the conscription extension is popular with the majority of Taiwanese, including younger respondents aged 30-39, as well as par-

ents who have children under 18.

Even if these arguments help the KMT gain some ground, the “redesign” Chiang had in mind is still probably the most viable direction for the party. The fact remains that Taiwanese identity continues to [skew “green”](#)—that is, in the direction of a stronger sense of native Taiwan identity. As such, committing to the same outdated cross-Strait policy that underperformed during the past two elections is unlikely to address the structural issues associated with the KMT’s dwindling voter base. Additionally, as national elections are often framed as a referendum on cross-Strait relations, Taiwanese voters are likely to closely monitor China’s behavior this year. The Chinese government has repeatedly made its preference for the KMT clear. However, its efforts to influence the election may [backfire](#). Just as the DPP’s 2020 election victory was heavily [influenced by the Hong Kong protests](#), the 2024 election could be defined by the Chinese Communist Party’s (CCP) ability, or lack thereof, to exercise prudence.

Against the backdrop of Chiang’s inability to “redesign” the KMT and Andrew Hsia’s two visits to China over the past year (in which the KMT and CCP re-endorsed the “1992 Consensus”), the KMT appears to be heading into the 2024 presidential elections without any real meaningful changes to its cross-Strait policy. It is increasingly clear that those in the party that have a reformist vision do not currently possess the political capital to see it implemented, while the more influential elites have proven that they lack the ideological flexibility to pursue a less polarizing platform. As [Shelley Rigger](#) observed after the 2016 election, “instead of reshaping its priorities to fit the expectations of a changing society, the KMT seems to be doubling down on its self-marginalizing approach.” To this day, it remains to be seen whether the KMT can escape this pattern of self-defeating behavior.

The main point: The KMT will have its best chance in the 2024 election if it is willing to revise its unpopular China policy. In practice, however, longstanding factional divisions may preclude the possibility of the KMT embracing the most electorally viable strategy.

The Other Opposition: The TPP in 2023 and Beyond

By: Joe Bauer

Joe Bauer is an analyst based in Washington, DC. He is a graduate of the Johns Hopkins School of Advanced International Studies (SAIS), and a Pacific Forum Young Leader.

As the dust settles on [Taiwan’s 2022 local elections](#), the speculation and focus towards the 2024 presidential election begins. Following the poor performance of the Democratic Progressive Party (DPP, 民進黨) in the November elections, President Tsai Ing-wen (蔡英文) has [resigned](#) from her post as party chair, while those in the Kuomintang (KMT, 中國國民黨) bask in their victory. On both sides of the political spectrum, party leaders have begun to jockey for position as their party’s respective presidential nominee. Beyond these headlines, however, one other party sits at a crossroads of uncertainty following the results of November’s elections: Taiwan’s other major opposition party, the Taiwan People’s Party (TPP, 台灣民眾黨).

Founded in 2019, the nascent political party quickly rose to prominence on the back of its founding leader and chairman, former Taipei Mayor Ko Wen-je (柯文哲). As the mayor of the capital city, Ko was in a unique position to forge a new political identity separate from those of the mainstream parties. Stating that his alignment was neither with the “Pan-Blue” camp of the KMT, nor the “Pan-Green” of the DPP, Ko opted instead to represent his new party with turquoise, a color blending both. Ko seemingly hopes that through the TPP he can upend the traditional two-party system, attracting a new base of moderate voters and catapulting himself into higher office. The uphill battle he faces and the barriers he must overcome to achieve this will make this a difficult task.

Green Beginnings and the Test of Taipei

Through much of his adult life, Ko had been a strong advocate for DPP politicians, supporting former President Chen Shui-bian (陳水扁) during the latter’s time first as mayor of Taipei, and later as president of Taiwan. Even after Chen’s time in office ended and his reputation became tarnished with corruption allegations, Ko continued to remain loyal, [lobbying](#) for Chen to receive greater medical treatment and alleging that the former president’s prosecution was politically motivated. Ko’s support for the DPP continued beyond Chen, as he advocated on behalf of Tsai Ing-wen (蔡英文) during her initial 2012 presidential run. While he has shared his disagreements with President Tsai and

her party over their stance on cross-strait relations with China, Ko has generally presented his strategic goals as aligned with the DPP.

Ko's own political ambitions became evident in January 2014, when he officially announced his intention to run for the soon-to-be vacant seat of Taipei City mayor following the end of KMT's Hau Lung-pin's (郝龍斌) second and final term in office. Given his previous ties with—and support of—the DPP, Ko initially considered running as a DPP candidate before ultimately deciding to continue as an independent, albeit in collaboration with DPP coordinators. After initially refusing to join in DPP preliminary debates, Ko eventually did agree to take part, proving widely popular among the Pan-Green base. As a result, the DPP declared that it would not challenge Ko, and would instead opt for a coalition of [support](#) in which Ko himself would remain independent. Without a DPP challenger, Ko's only real competition came from the KMT-backed Sean Lien (連勝文), a businessman-turned-politician who ultimately proved no threat on election day: Ko [won handily](#), securing the second-highest vote total ever for the post, behind only former President Ma Ying-jeou (馬英九) in 2002.

While Ko enjoyed a productive first term in office, his run for reelection in 2018 proved more challenging. Following increasingly harsh disagreements with Ko, the DPP made the decision to [pose a challenger](#) candidate in the mayoral election, ultimately landing on Pasuya Yao (姚文智). Yao had previously campaigned to be the DPP's 2014 candidate for the position, but the decision to align with Ko left those ambitions unfulfilled. While most observers did not expect Yao to achieve victory outright, many questioned whether the DDP could act as a spoiler, sapping votes from Ko and possibly allowing KMT candidate Ting Shou-chung (丁守中) to win the election. This nearly became the case, as the final results on election day showed Ko [narrowly escaping defeat](#) by securing 580,820 votes (41.05 percent) compared to Ting's 577,566 (40.82 percent).

Ko's split from the DPP became increasingly pronounced his second term in office, as he adopted a more moderate, if not China-friendly approach. Striking a sharp contrast with DPP leadership, he often [repeated slogans](#) such as the "two sides of the [Taiwan] Strait are one family." While it can be argued that Ko's seemingly tacit agreement to a hybrid of Beijing's "One-China" framework may be intended to benefit constituents through economic ties (illustrated by his regular participation in the Shanghai Taipei Forum [上海-臺北城市論壇]), some have [noted](#) that Ko's catering to the Pan-Blue base has been steadily growing over time.

Ko's attempts to expand his influence continued in 2020, as the TPP competed in its first-ever Legislative Yuan election cycle, winning five seats and becoming the third-largest party in the body. This achievement would grant the TPP a new platform beyond Ko's post in Taipei and start the process of expanding the party's influence beyond the capital.



Image: Taipei City Mayor and Taiwan People's Party Chairman Ko Wen-je speaking at a conference on education policy in Taipei (November 10, 2022). (Image source: [Central News Agency](#))

The Road Forward

As the end of Ko's second term in office approached ahead of the 2022 local elections, many questioned whether his young party could continue without its maverick leader holding a prominent political office. While Ko's popularity in Taipei [remained steady](#), with approval ratings rising and falling throughout the pandemic, few other members of the party seem poised to pick up the mantle and become leading national figures. Though Ko has [openly alluded](#) to his desire to make a run for Taiwan's presidency in 2024, a strong base of political support would still be crucial to carry on momentum.

Come election day, results were mixed. The [highlight victory](#) was that of Ann Kao (高虹安) who won the mayoralship of Hsinchu City by nearly ten points over a DPP competitor. Kao, just 38, is the youngest female county magistrate or mayor in Taiwan's history, and will oversee a seat that is home to Hsinchu Science Park, one of the premier global centers of semiconductor manufacturing and development. While Kao presents a promising young face for the party, controversy has risen following allegations that she plagiarized aspects of her doctoral thesis, an accusation similar to one that recently led to the October 2022 [resignation](#) of fellow TPP legislator and close Ko ally Tsai Pi-ru (蔡壁如).

In addition to Kao's victory, 14 other TPP candidates scored wins

in local councilor seats across nine different localities and municipalities. While the result is notable in that it is the first local election in which TPP candidates challenged for such positions, only in Taipei City did the party manage to attain the three or more seats necessary to form a local party caucus, a previously announced goal. The final result of note was the defeat of Vivian Huang (黃珊珊) in the campaign to succeed Ko as mayor of Taipei City. Huang competed in the race as an independent candidate, though she had the close backing and [support](#) of Ko, under whom she had previously served as Taipei deputy mayor. Huang finished third in the race, [receiving](#) approximately 25 percent of the vote, with the KMT's Chiang Wan-an (蔣萬安) ultimately securing the win in the capital.

Following these results, the question stands as to where the party goes from here. While Ko may now opt to focus fully on a presidential run in 2024, without holding elected office he will be forced to [create his own platform](#) from which to generate headlines and policy discussion. This will put him at an immediate disadvantage relative to other leading contenders—such as Vice President Lai Ching-te (賴清德) of the DPP or New Taipei City Mayor Hou You-yi (侯友宜) of the KMT, who face no such constraints. As previously stated, Ko has increasingly leaned toward the Pan-Blue camp. And while the KMT's impressive showing in last year's local elections is noteworthy, these results [will not necessarily translate](#) come 2024, when the electoral focus shifts away from kitchen table issues and toward cross-Strait affairs.

While it is certainly possible that Ko can fine-tune his approach to attract moderates from both the Blue and Green camps in the years to come, it remains just as likely that he could instead play the role of a third-party spoiler, siphoning away a small but significant portion of the vote from either of the leading party's candidates. With the 2024 campaign season now on the horizon, leading figures of the DPP and KMT will begin to make their case as to why they should be the face of their party in the forthcoming presidential election. From his seat atop the TPP, Ko will face no such intra-party rival, though whether he is able to take advantage of that opportunity remains to be seen.

The main point: While the strong showing of the KMT and poor performance of the DPP have generated most of the headlines in the wake of Taiwan's recent local elections, the showing of the TPP should not be overlooked. As the 2024 presidential election approaches, Ko Wen-je's young party could play a significant role, though major uncertainties remain.

One Year after the Ukraine War: Economic Implications of a Potential War in the Taiwan Strait

By: Chiang Min-hua

Chiang Min-hua is a research fellow and economist in the Asian Studies Center at The Heritage Foundation.

Vladimir Putin's invasion of Ukraine has roiled energy markets and food supply chains, sending economic shockwaves around the world. This prompts an important question: What would happen to the world economy if China invaded Taiwan? Clearly, the economic impact would be much more devastating and profound than that of the Ukraine war, given the fact that Taiwan and China are both far more integrated into the global economy. Even without direct military intervention from the United States, a Taiwan-China war would devastate the global economy like a weapon of mass destruction.

The Geopolitical Roots of Taiwan-China Economic Ties

Taiwan's booming economy and deep economic ties with the United States and China have been a consequence of evolving geopolitical factors. Its economic development—driven by US aid, investments, and exports to the American market—was inextricably linked to its role as a key anti-Communist fortress in the region early in the Cold War. Given the threat of an invasion from China, the United States considered it imperative that Taiwan prosper economically in order to support the island's major military requirements.

By the end of the 1970s, US foreign policy shifted. Abandoning its previous antagonistic approach to China, Washington increasingly moved to open diplomatic and economic ties with Beijing, as both came to see the Soviet Union as a common enemy. The United States granted China [Most Favored Nation \(MFN\)](#) status in the 1980s and 1990s, allowing China to enjoy far more favorable trade terms. In 2000, Washington granted [Permanent Normal Trade Relations \(PNTR\)](#) status to China shortly before its admission to the World Trade Organization (WTO) in 2001.

Apart from using China to counterbalance the Soviet Union, the United States was hoping that trade and economic engagement would help to change China. As [President Bill Clinton declared in 1998](#): "Trade is a force for change in China, exposing China to our ideas and our ideals, and integrating China into the global economy."

America's opening to China also served as an impetus for greater cross-strait integration between the Chinese and Taiwanese economies. Taiwanese firms that aimed to export final consumption goods to overseas markets moved their labor-intensive manufacturing to China to lower production costs.

Today, as China grows more belligerent, it has become clear that the United States' efforts to change China by integrating it into the global economy proved a failure. Not only is China far from embracing American ideas of democracy, but it has become a threat to the United States in terms of [military power](#) and [high-technology development](#). The war in Ukraine has strained bilateral tensions even further. In addition to its regular military harassment activities near Taiwan, China is distancing itself from the West through its ["unlimited" partnership](#) with—and [economic support](#) to—Russia.

De-coupling the Cross-Strait Production Network and Changing Geopolitical Contexts

For more than three decades, Taiwan has relied on exporting key components and semi-industrial goods to China for final assembly. This model is now changing. Taiwanese firms started to shift some production away from China to other developing countries more than a decade ago due to increased labor costs on the mainland. The growing United States-China rivalry has accelerated investment relocation. China's share of Taiwan's outbound foreign direct investment (FDI) has declined from 84 percent in 2010 to 34 percent in 2022, according to [Taiwan's Investment Commission](#).

One key component of China-Taiwan trade has been the semiconductor industry. However, the shift of semiconductor production away from China has become more pronounced since the outbreak of the COVID-19 pandemic. China's share of Taiwan's outbound investments in electronic parts, computer, and optical product manufacturing decreased [from 67 percent in 2020 to 42 percent in 2022](#).

In 2022, China and Hong Kong remained Taiwan's largest export destinations. However, the growth rates of its exports to China and Hong Kong have turned negative, whereas exports to other major markets (such as Southeast Asia, the United States, Japan, and Europe) have increased significantly, according to [Taiwan's Ministry of Finance](#) (MOF, 財政部).

Demand from China-based Taiwanese businesses for capital equipment and semi-industrial goods was once the main driver of Taiwan's exports to China. With the number of Taiwanese businesses in China decreasing, [demand from Chinese compa-](#)

[nies](#) and [foreign companies located in China](#) has become the main driver of Taiwanese exports to China. Taiwan's supply of key components to China remains essential to Beijing's ambitions to play a role in global supply chains.

However, Taiwanese exports of key components to China are likely to slow even further following new US [restrictions on exports](#) to China of semiconductor chips that use US technology. In addition, Apple shifting a quarter of its production of [iPhones from China to India](#) could further reduce Taiwan's exports of key components to China. While Taiwan can continue to export its chips to India for making iPhones, China might lose one of its key economic pillars: exporting final consumption goods such as the iPhone to the world market.

An Economic Evaluation of China's Military Invasion of Taiwan

Unlike Russia's security concerns after the collapse of the Soviet Union, China's foreign policy has been rooted in a quest for economic modernization. [1] China's more extensive involvement with the world economy provides multiple channels for Western countries to sanction China. However, economic interdependence is a double-edged sword: [China's greater integration with the global economy](#) might restrain potential [economic sanctions](#) from Western countries, as it will also hurt the countries that impose sanctions.

If tensions over Taiwan continue to rise, the question is: Which side can better bear losing the benefits derived from economic interdependence? It should be easier for Western countries and companies to line up substitutes to fill China's manufacturing role (such as India, Vietnam, and other developing countries) than it would be for China to find alternative sources of technology, and replacement markets for its exports of final consumption goods. Indeed, the Chinese Communist Party (CCP) would risk losing its political control over the whole country if it lost Western export markets and sources of advanced technology.

However, rationality may not be enough to deter further, and more aggressive, Chinese military activities in the Taiwan Strait. China has not ceased or slowed its provocative military actions near the island of Taiwan, even as its economy has declined over the past few years. Several prominent military analysts now predict that China is likely to invade Taiwan between [2024](#) and [2027](#).

Conclusion

Taiwan's economy and its relations with China have been shaped by a complex mixture of geopolitical and global economic dynamics between major powers. Both countries' exten-

sive trade with the rest of the world would make any war in the Taiwan Strait a catastrophe for the global economy.

The triangular relations between China, Russia, and the United States have dramatically changed since the 1990s. Before the Ukraine war, [Russia's GDP](#) was comparable to South Korea, a middle power in the world. Russia's economy is likely to shrink even more after the war. By contrast, China's economic modernization has enhanced its military muscle and emboldened its ambitions to challenge the United States' leadership role in the world. Integrating China into the global economy failed to make it a reliable partner for the United States.

In drafting any plans for military action against Taiwan, Beijing will consider how the United States and its European allies have reacted to Russia's invasion. The eruption of the war in Ukraine is also a wake-up call for Taiwan. The ruling Democratic Progressive Party (DPP, 民進黨) government has been making efforts to strengthen Taiwan's overall defense capabilities through the "[strengthening all-people's defense military force restructuring plan](#)," announced in December 2022. The Ministry of National Defense (MND, 中華民國國防部) has also proposed a [14 percent hike in defense spending in 2023](#) to beef up Taiwan's defense capabilities.

Sustaining these new military expenditures will require robust economic growth. So far, declining exports to China and the relocation of investments out of China have not had a severe impact on Taiwan's economy. However, Taiwan will require greater political and economic engagement with a wider variety of countries in order to continue diversifying its economic ties.

The main point: A war over Taiwan would have severe negative repercussions for the world economy. However, the potential economic and political turmoil from launching a war against Taiwan will likely not restrain China's provocative military actions. A new China policy is imperative to prevent a conflict in the Taiwan Strait from devastating the global economy.

[1] Jeanne L. Wilson, *Strategic Partners: Russian-Chinese Relations in the Post-Soviet Era* (New York: M.E. Sharpe, 2004), 199.

The "Southern Semiconductor S Corridor" and the Role of Taiwan Industry in US-China Competition

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Following a classified briefing on February 9 with military and intelligence officials, Republican senators reportedly expressed concern that US manufacturing may have inadvertently contributed to the [Chinese spy balloon](#) that recently violated US air space (as well as similar balloons that have [overflowed other countries in the Asia-Pacific region](#)). According to a source familiar with the briefing, components in the Chinese balloon had [Western-made parts](#) and English writing.

Others have previously expressed similar concerns about Western and allied technology ending up in Chinese weapons. Back in 2019, US officials warned Taiwanese diplomats that Huawei (華為) was using Taiwan Semiconductor Manufacturing Company (TSMC, 台積電)—built semiconductors in Chinese missile guidance systems [aimed at Taiwan](#). In 2021, a *Washington Post* story also reported that the Chinese company Phytium Technology Co. (飛騰) was using [TSMC chips](#) in advanced Chinese military systems, to which Taiwan Minister of Economic Affairs Wang Mei-hua (王美花) responded that "to the best of our knowledge" the Chinese military was not the intended end-user for any of TSMC's chip exports.

Nonetheless, [Ou Si-fu](#) (歐錫富), a research fellow at the Institute for National Defense and Security Research (INDSR, 國防安全研究院) in Taipei, has pointed out challenges associated with imposing export controls on semiconductors: "The problem is that the chips are dual-use technology," and as such, "they can be bought off the shelf for one application and then used in military equipment that is aimed right back at Taiwan."

This issue is at the heart of the dilemma currently facing policymakers in the United States, Europe, and Asia: how can governments maintain national security in the face of increasingly globalized, interlinked defense and industrial sectors? Driven by the desire to maintain—or acquire—production capabilities in key military-related industries, governments often inject national security considerations into discussions of economic management. Since threats to such supplies contribute directly to military capability, these sorts of economic threats have essentially become military threats.

The semiconductor industry, by virtue of the dual-use applications of its products and critical role in national defense industrial bases, has both major economic and military significance that give it an outsized role in the emerging geopolitical competition between the United States and China. Continued advancements in Taiwan's semiconductor sector—to include the construction of major new research and development (R&D) and manufacturing facilities in southern Taiwan—are likely to further reinforce Taiwan's leading role in this critical industry.

“Strategic Industry”: Rationales for State Intervention in the Semiconductor Sector

Besides the dual-use characteristics of many semiconductor products, the broader semiconductor industry is also viewed as a “strategic” or “critical industry” due to its vital role in a modern economy. The chip industry is considered particularly “strategic” due to its linkages to the rest of the economy, and the possibility of monopoly profits in this sector. Furthermore, the relatively fixed sunk cost of R&D and capital equipment investments, and the decreasing unit costs with improved yields, create “first mover advantage,” in which a privileged position in one market can create scale economies over rivals and capture more technological externalities (positive externalities) in future generations of semiconductor products. [1]

The linkage argument is best illustrated by the electronics “food chain” theory, in which upstream and downstream industries’ competitive fortunes are interlinked in a complex ecological system that makes each dependent on the health of the others. [2] As witnessed during the COVID-19 pandemic and resultant chip



Image: Local Tainan City officials at the inaugural ceremony for opening the “ITRI Compound Semiconductor Southern Development Base”—one of the links in the “Southern Semiconductor S Corridor” that will expand semiconductor production in southwestern Taiwan. (Image source: [Tainan City Government](#))

shortages, damage to the chip sector caused the German automotive industry to suffer losses, culminating with then-German Minister of Economic Affairs and Energy Peter Altmaier [writing to his Taiwanese counterpart](#) Wang Mei-hua to encourage TSMC to ramp up production. When there was a shortage in the component level of advanced (e.g., smaller than 10 nanometer) chips from TSMC, this also posed a serious risk to other high-tech sectors, as these products are crucial [inputs](#) in smartphones, computers, and military and space equipment.

Many industries employing semiconductors are considered integral to national security, and are typically deeply connected to national defense. Given these considerations, such industries are often subject to considerable government oversight and intervention. Furthermore, since it can cost more than [USD \\$20 billion](#) to build a new chipmaking plant, the list of leading-edge firms capable of manufacturing at scale has essentially been reduced to three: TSMC, Intel, and Samsung. This short list makes each company that much more important.

“Chip Wars” and the Enduring Importance of Taiwan

Given the importance of the sector, it is not surprising that the semiconductor industry has been characterized by repeated US Government interventions: first during the chip war with Japan in the 1980s, and now with China in the 2020s. The 1980s was characterized by greater integration of the commercial and defense sectors, and the globalization of an increasingly commercial defense industrial base. At the same time, the Japanese semiconductor industry emerged as a major force in the world market. By 1985, Japan's share of the global market for Dynamic Random Access Memory (DRAM) chips had surpassed the United States, with Washington accusing Tokyo of [dumping](#) chips in an effort to [cripple](#) the US industry. The trade friction was exacerbated by comments from an ultranationalist member of the Japanese Diet, [Shintaro Ishihara](#), who threatened to cut off semiconductor supplies to the United States and sell them to the Soviet Union instead. Eventually, amid rising concerns about defense dependence on foreign—especially Japanese—sources of supply, US policymakers established [SEMATECH](#) in 1987—a joint government-industry consortium intended to revitalize the US domestic semiconductor manufacturing industry.

Now history is being repeated in the ongoing [US-China “chip war.”](#) The United States has spearheaded the establishment of the “Chip 4” alliance—with partners Taiwan, South Korea, and Japan—in order to ensure a resilient semiconductor supply chain. The American Institute in Taiwan (AIT) hosted the first virtual [meeting](#) of the group on September 28, 2022. Notably,

Taiwan's TSMC plays a key role in this alliance, given its near-monopolistic 92 percent of market share for advanced semiconductors. Given the US Department of Defense's growing need for a secure and reliable chip supply, [reshoring](#) semiconductor manufacturing capability is at the top of the US agenda. The new [TSMC chipmaking facility in Arizona](#) is one example of these efforts.

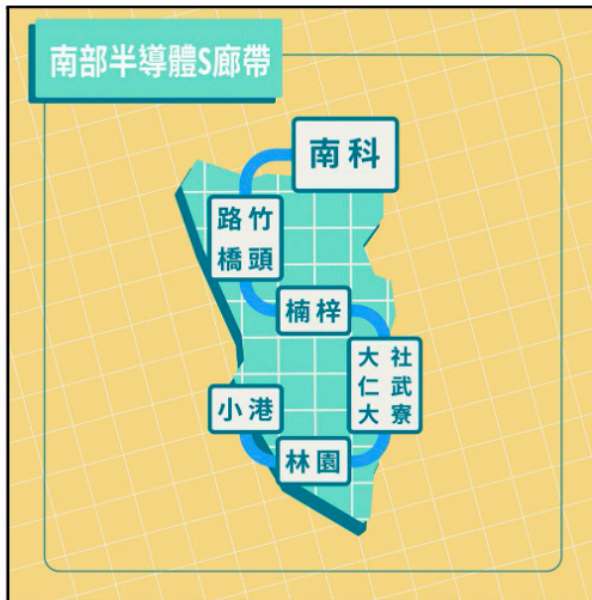


Image: A diagram depicting the existing or planned facilities that will form the “Southern Semiconductor S Corridor” between Tainan and Kaohsiung—a group of facilities intended to further advance semiconductor production in southern Taiwan. (Image source: [Kaohsiung City Government](#))

The “S Corridor” and Taiwan’s Role in Supply Chain Security

Besides reshoring, TSMC in [Kaohsiung](#) is also playing an important role in Indo-Pacific supply chain regionalization. To that end, Nanzih Technology Industrial Park will become the core zone of Taiwan’s “[Southern Semiconductor S Corridor](#)” (南部半導體S廊帶)—a policy priority envisioned by Kaohsiung Mayor Chen Chi-mai’s (陳其邁) administration, which is intended to establish a new technology industrial cluster in southern Taiwan (centered around the greater Kaohsiung area). The project will “connect Tainan Science Park, Renwu Industrial Park, Ciaotou Science and Technology Park, and Nanzih Technology Industrial Park” in an S-shaped corridor. Besides TSMC, the project has already attracted other major technology companies such as Win Semiconductors Corp, the Netherlands-based NXP, and the Germany-based Merck Group. Furthermore, Nanzih Technology Industrial Park is already home to Taiwan’s second largest semiconductor company, Advanced Semiconductor Engineering (ASE, 日月光半導體製造股份有限公司). In August 2022,

TSMC held a groundbreaking ceremony for their [new plants](#) in Nanzih, which are slated to first produce 28 nanometer chips used mainly in the automotive industry, as well as [seven nanometer chips](#) in the near future.

Nonetheless, it is important to point out that US-China trade friction in semiconductors does not necessarily mean a *decoupling* from China’s economy, but rather a selective *diversification* and remapping of the high-tech supply chain. China remains a top trading partner for Taiwan and other allies such as Japan and South Korea, and as Taiwan’s Deputy Economic Affairs Minister [Chen Chern-chyi](#) (陳正祺) has observed, “I don’t see [how] we can completely decouple from China. That’s not realistic.” Moreover, as Major Jessica Taylor and Jonathan Corrado argued in a recent article in [The National Interest](#), due to the globalized nature of the chip supply chain, decoupling would be expensive and could potentially alienate US partners, as well as inhibit the innovative capacity of US companies. Thus, at this juncture, the “Chip 4” alliance seems to be a prudent way forward to build resilience in the supply chain, as policymakers in Taiwan, the United States, and allied countries continue to balance the trade-off between maintaining national defense and innovation in an increasingly globalized industrial sector.

The main point: Given TSMC’s near monopolistic position in production of advanced semiconductors, Taiwan is a linchpin in supply chain security for the United States and its allies—and the construction of new facilities for semiconductor production in southern Taiwan will further reinforce Taiwan’s importance in this industry.

[1] In general, a strategic industry is one characterized by high entry barriers, first-mover advantages, high sunk costs, and externalities. As noted in the early 1990s by analyst Laura D’Andrea Tyson, high research and development (R&D) expenditures and steep learning curves create entry barriers for firms lacking sufficient capital, and encourage them to develop “technology drivers”—“a high-volume product with a relatively simple design.” In doing so, such firms may “hone [their] manufacturing skills and transfer [their] learning to more complicated, lower volume, high value-added devices.” See: National Advisory Committee on Semiconductors (NACS), *A Strategic Industry at Risk: A Report to the President and the Congress* (Washington, DC: 1989); and Laura D’Andrea Tyson, *Who’s Bashing Whom? Trade Conflict in High-Technology Industries* (Washington, DC: Institute of International Economics, 1992), 89.

[2] NACS, *Strategic Industry at Risk*, 9.