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The Geopolitics of Taiwan: Part I

Tensions over Taiwan have been steadily escalating in recent years. When President Trump was elected in 2016, [one of the first official contacts](#) he made was with President Tsai Ing-wen, the leader of Taiwan. Accepting this call infuriated Beijing, which views Taiwan as a province of the People's Republic of China (PRC). Recently, there have been alerts [from American military officials warning that China has hostile designs on Taiwan](#). [Chinese warplanes regularly enter Taiwan's airspace](#), normalizing this hostility.

There are numerous subcurrents in Asia; the predominant one is that China no longer accepts U.S. hegemony in the region and seeks to become the dominant power of that continent.¹ However, having the goal of hegemony and becoming a hegemon are two different issues. The size of China's economy clearly makes it a world power. [The country has been rapidly building its military](#) to compete with the U.S. At the same time, it has serious vulnerabilities that prevent it from ousting America from the Pacific region.

Taiwan encapsulates many of the issues surrounding China's goal of hegemony. In this report, we will examine them in depth. In a subsequent report, my colleague,

¹ Allison, Graham. (2017). *Destined for War: Can America and China Escape Thucydides's Trap?* New York, NY: Houghton, Mifflin, Harcourt. Our review of the book and concept can be found [here](#) and [here](#).

Patrick Fearon-Hernandez, will build off this research to examine the global semiconductor industry which has much of its critical infrastructure in Taiwan. To some extent, the geopolitics of Taiwan, in general, and the semiconductor industry, specifically, detail the current situation surrounding globalization. As globalization comes under strain, the stresses are being exhibited clearly in Taiwan and in semiconductors.²

In Part I of this report, we will begin with a history of Taiwan. Next, we will address current relations between the PRC and the Republic of China (ROC) and the end of strategic ambiguity. In Part II, we will analyze the geopolitical importance of Taiwan and China's military options. In Part III, we will examine how Xi Jinping may react, in light of his ascendancy to power. Finally, we will conclude with market ramifications.

The History of Taiwan

There is evidence that suggests the Han Chinese began settling in Taiwan in the 11th century, although it appears that hostile indigenous tribes hampered development. It wasn't until 1624 that the Dutch established

² Because these reports touch on not just macroeconomic and geopolitical issues, but will also discuss industries and companies, we want to acknowledge the support and counsel provided by our colleagues at Confluence Investment Management on the Value Equities and International Equities Investment Committees. Dan Winter, Matt Sinkovitz, Mark Keller, Joe Hanzlik, and Greg Tropf provided insight and information in our research. While acknowledging their contributions, any errors and omissions in this report are mine alone and the research reflects my sole conclusions.

a commercial base in Taiwan. The Chinese ousted the Dutch in 1662, and the area was ruled by Chinese warlords who were remnants of the collapsing Ming dynasty that was being expelled by the incoming Qing dynasty. One of the Ming loyalists was Captain Zheng Chenggong, who was responsible for removing the Dutch from Taiwan. Zheng³ successfully began a series of raids on the mainland and built the Kingdom of Tungning, which, at its peak, included parts of the central coast of the mainland, partial control of Shanghai, and several miles inland along the Yangtze River. Although the Qing eventually regained control of Taiwan and ended the Kingdom of Tungning, Zheng's exploits serve as a reminder to modern PRC leaders that Taiwan can be a "launch pad" for invaders and thus they see an independent Taiwan as a significant threat.

China maintained control of Taiwan until 1895, when China was defeated in the First Sino-Japanese War. As part of the peace treaty, China ceded Taiwan to Japan. The Japanese began industrialization of the island, building transportation networks, public infrastructure, and public schools. Japan also embarked on a program of suppression and assimilation of the aboriginal people, conducting aggressive military actions against tribes that resisted Japanese rule but also allowing groups that cooperated to earn second-class citizenship. At the onset of the Pacific War and World War II, thousands of Taiwanese joined the Japanese military. The Imperial Navy operated a base out of Taiwan. In general, many native Taiwanese have a favorable view of Japan, which is unusual in the region.

Japan's defeat in World War II ended its control of Taiwan. The Nationalist Chinese

under General Chiang Kai-shek were given control over the island. The military government run by the Nationalists was corrupt, inefficient, and very unpopular with the native Taiwanese. In 1949, after the Nationalists were defeated in the Chinese Civil War, Chiang Kai-shek and his followers fled to Taiwan and established the Republic of China (ROC). As they departed, the Nationalists carried many national treasures and all of China's gold and foreign currency reserves. Mainland China, controlled by the Communists, established the PRC.

Both nations considered themselves the legitimate government of China. The ROC maintained seats in its legislature for the districts on the mainland even though it was impossible to hold elections in those areas. Chiang Kai-shek ruled Taiwan under martial law. The KMT, the political party of the Nationalist Chinese, was the only legal party in Taiwan.

The United States, the primary protector of Taiwan, considered the ROC to be the legitimate government of China. American forces were stationed on the island. However, with President Nixon's trip to China in 1972, the U.S. and the PRC began the process of normalization. U.S. combat troops left Taiwan on March 26, 1975, and [military advisors gradually left](#). By January 1, 1979, when official recognition shifted to the PRC, all U.S. troops had vacated Taiwan. The ROC lost its status in the United Nations at this time. That same year, the United States passed legislation indicating it would protect Taiwan from mainland Chinese military threats. In 1992, the PRC and the ROC agreed on the "1992 Accord," which indicated that there was only one legitimate government of China;

³ Also known as Koxinga.

however, using “strategic ambiguity,”⁴ both considered themselves to hold that honor.

By the mid-1980s, Chiang Kai-shek’s successor, his son Chiang Ching-kuo, began to liberalize the government. Martial law was eased in 1984 and abolished in 1987. Political parties were allowed; the DPP was established to represent the interests of the native Taiwanese, which account for 80% of the island’s population. In 1991, the KMT finally forced legislators who held seats for mainland districts to retire, paving the way for legislative elections. In 1996, the ROC held its first presidential election. Lee Teng-hui of the KMT won.

In the 2000 election, Chen Shui-bain of the DPP won the presidency on a platform of defending native Taiwanese rights. He persistently pushed for independence from China. The PRC viewed these threats as the equivalent of civil war, since it treats Taiwan as a province of China. The U.S. was also unhappy with Chen’s policies as they increased tensions in the region. The Chen administration persisted in not allowing direct transportation, mail, and trade links. This did not stop Taiwan investment into the PRC, but it made such activity more difficult. Although the DPP controlled the executive branch, the KMT maintained control of the legislature. The legislature prevented proposals designed to trigger confrontations with the PRC. Chen won two terms in office but the DPP failed to hold power in 2008, and the KMT, led by Ma Ying-jeou, prevailed in the presidential election.

Ma Ying-jeou, unlike Chen Shui-bain, worked hard to improve relations with the PRC. Ma signed 23 different cross-strait

economic agreements; virtually all the pacts were negotiated in secret. In 2016, Tsai Ing-wen returned the DPP to power and, unlike Chen Shui-bain, she also carried the legislature. Since her election, relations with China have deteriorated. Beijing actively tried to reduce her chances of re-election, but those failed, and she won a second term in 2020.

Current Relations Between the PRC and ROC

Relations between the ROC and PRC remain frosty. Beijing argues that President Tsai is not committed to the One China policy and [ended official contact with the ROC government in June 2016](#). Since taking this action, the PRC has systematically worked to weaken Taiwan’s global standing. It has used economic and political leverage to encourage countries to not recognize the ROC. Since 2016, six countries have switched recognition from the ROC to the PRC. The only European state that still recognizes the ROC is the Vatican, and given negotiations over Roman Catholics in China, that could reverse at any time. At present, only 15 nations give the ROC full diplomatic recognition.

China has also forced [businesses to refer to Taiwan as part of China](#). It has prevented Taiwan from participating in international bodies such as the World Health Organization. As noted above, over the past two years, it is has [repeatedly violated Taiwan’s airspace](#).

The PRC wants Taiwan to accept its vision of the 1992 Accord of “one country, two systems.” [In general President Tsai has refused to accommodate Beijing on this issue](#). What does Beijing want?

1. The ROC no longer exists as a political entity;

⁴ Strategic ambiguity is a diplomatic tactic in which two parties say exactly the same thing but derive completely different meanings from the words.

2. The flag of Taiwan would be replaced by the PRC flag;
3. Taiwan would become a special administrative region, e.g., Hong Kong;
4. Taiwan would no longer have foreign or defense policies;
5. Taiwan's economy and society would be maintained;
6. Taiwan would also have its own army;
7. Beijing would choose Taiwan's leaders.⁵

Clearly, if Taiwan accepted these conditions, the government of the island would no longer be independent. It is hard to see how the current government in Taipei would agree to these demands. And so, the PRC continues its policy to isolate and intimidate Taiwan, while Taiwan continues to resist.

At the same time, despite these tensions, [China remains Taiwan's largest export target](#), taking 29.7% of the island's exports. [Its combined trade surplus with China and Hong Kong is \\$87.2 billion](#). Although the political environment may be tense, China and Taiwan have close economic ties.

The End of Strategic Ambiguity

Strategic ambiguity is a useful concept in diplomacy and international relations. In a nutshell, it means that two or more parties say exactly the same thing in an agreement but mean something entirely different. The PRC, ROC, and the U.S. have all engaged in strategic ambiguity since the U.S. decided to normalize relations with the PRC.

The U.S. position was that the Nixon administration realized that Chinese and Soviet relations had deteriorated to the point of near conflict. By normalizing relations with Beijing, Washington could reduce Moscow's influence on China. But

⁵ <https://www.cfr.org/report/united-states-china-and-taiwan-strategy-prevent-war>; see p. 27.

normalization came at the cost of no longer recognizing the ROC. Politically, that was difficult. America was in a Cold War with the Communist bloc, of which the PRC was a member. Thus, Washington needed to continue to protect Taipei without offering overt support. The U.S. made regular arm sales to Taiwan and made it clear to Beijing that it would oppose unification through military means. The Taiwan Relations Act of 1979 codified that the U.S. would oppose unification by any means other than a peaceful transition. President Reagan made "Six Assurances"⁶ to Taiwan (which were classified). They were:

1. The U.S. has not set a date for ending arms sales to Taiwan;
2. It has not agreed to consult with the PRC on arms sales to Taiwan;
3. The U.S. will not play a mediation role between Taiwan and China;
4. The U.S. has not agreed to revise the Taiwan Relations Act;
5. The U.S. has not altered its position regarding the sovereignty of Taiwan;
6. The U.S. will not exert pressure for Taiwan to enter negotiations with the PRC.

The Clinton administration opposed a visit to Cornell by then-Taiwan President Lee Teng-hui in 1995 but relented under congressional pressure. The PRC responded to this visit by firing missiles into Taiwanese waters.⁷ The Bush administration was concerned that Chen Shui-bian of the DPP would raise tensions so this administration made it clear the U.S. would not support independence.⁸ The Obama administration sold advanced weapons systems to Taiwan but also Obama's term coincided with KMT President Ma Ying-jeou's administration

⁶ Op. cit., p. 16-17

⁷ Ibid., p. 17

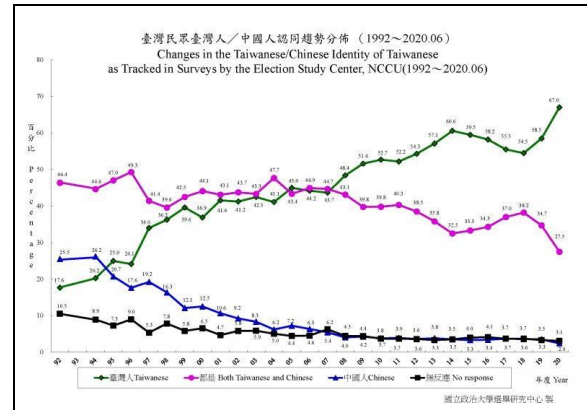
⁸ Ibid., p. 18

where relations between Taipei and Beijing were mostly friendly.⁹ The Trump administration had a confrontational relationship with the PRC and used increasingly high-level exchanges with Taiwan to pressure Beijing.¹⁰

The U.S. policy toward China and Taiwan is to officially accept the “One China” policy but to maintain a high level of unofficial ties to Taiwan. The U.S. is comfortable with the status quo. As we will discuss below, Taiwan occupies critical space in the region and thus the U.S. would prefer to maintain influence with Taiwan. Washington would also like to keep China from taking direct control as long as possible. The uncertainty reflects how badly the U.S. wants to defer Beijing’s control; in other words, [would the U.S. go to war to prevent a takeover?](#) If the citizens of Taiwan wanted to peacefully join the mainland, the U.S. would likely acquiesce. But the U.S. does not want to see a hostile annexation of the island. The U.S. has purposely kept its desire to maintain the status quo unclear. This uncertainty has been sustained in order to avoid giving Beijing a reason to invade and also to give Taiwan the impression that it might not support independence. Interestingly enough, it is generally assumed in both Beijing and Taipei that the U.S. would oppose a hostile takeover of the island; [perhaps only the U.S. has any uncertainty.](#)

Although ambiguity serves the U.S. well, it is becoming less attractive to Taipei and Beijing. After Chang Kai-shek took the Nationalist remnants to Taiwan, there were no doubts about where either side stood; both Taipei and Beijing considered themselves to be Chinese and the legitimate government of the country. But, with the democratization of Taiwan and fading

memories of the nationalist/communist civil war, a majority of Taiwanese see themselves as predominantly citizens of Taiwan.



(Source: [Noah Smith](#))

This change in attitude presents a serious problem for the PRC. If those living on the island increasingly view themselves as citizens of their island and not of the mainland, the likelihood of a mutual transition is lessened. Complicating matters further are [polls showing that 61% of adults have an unfavorable view of the PRC](#) and that the majority of Taiwan’s adults support closer ties with the U.S.

The issue of Hong Kong complicates matters further. The terms that Deng Xiaoping accepted for the turnover of Hong Kong to China were dubbed “one country, two systems.” Deng promised to give Hong Kong a high degree of autonomy for five decades, allowing the former British colony to have its own courts and hold elections. For the most part, until Xi, Chinese leaders honored that promise. However, over the past two years, Xi has jettisoned that contract. Beijing has taken control of Hong Kong and is increasingly interfering with the legal system and reducing personal and press freedoms. Xi’s actions in Hong Kong have not been lost on Taipei. It is clear that the “one country, two systems” policy is no longer operable in Hong Kong, meaning there is no guarantee that any such system

⁹ Ibid., p. 18

¹⁰ Ibid., p. 19

will be honored if Taiwan accepts annexation.

If the majority of Taiwanese view themselves as a distinct and separate people from China and if joining the mainland means losing their elections and legal system, it's difficult to see the social or political allure of accepting peaceful annexation. It appears that General Secretary Xi has concluded the same. And so, time isn't on the side of Beijing. Although China's military will continue to improve, attitudes in Taiwan will likely continue to deteriorate toward the PRC, and the U.S. and Taiwan can work to build defenses against a Chinese military action.

Therefore, we expect the U.S. to maintain strategic ambiguity but that China and Taiwan will be less supportive of that idea. From Beijing's perspective, there is little benefit to maintaining the status quo. Taiwan knows that an open declaration of independence would lead to war so it will likely try to behave in a way that is *de facto* independent—in other words independent in everything without a declaration.

Part II

Next week, we will analyze the geopolitical importance of Taiwan and China's military options.

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