

Will Taipei Be the Next Hong Kong? *Democratic Institutions and Taipei's Future as a Global City*

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Smart money is surging out of China. Slowing economic growth and a government crackdown on corruption have led to an outpouring of funds as China's wealthy seek out safe havens for its accumulated wealth. No one knows just how much money is leaking out of the Chinese economy, but a 2013 IMF report predicts that full capital account liberalization will result in outflows of 15 to 25 percent of GDP.¹ That amounts to between \$1.2 trillion and \$2.1 trillion looking for a new home.

And it is not just money that is on the move. According to a 2012 paper by Cheng Li, Director of the John L. Thornton China Center at the Brookings Institution, an internal Chinese Communist Party report found that at least three-quarters of the senior executives from China's major state-owned enterprises had acquired foreign residency or passports for members of their immediate families.² Countries all around the world seeking to capitalize on this trend have investor visa programs designed to attract rich Chinese immigrants.

Where will all these people and their money go? The surprising answer may be Taipei. There are good reasons to think that Taipei, the capital city of Taiwan, could become one of Asia's most important financial centers and Greater China's first truly global city, joining the top rank alongside London and New York. Chief among these reasons is that Taiwan's robust civil society ensures continuing rule of law in a way that China's autocracy and Singapore's managed family democracy cannot. Taipei already has most of the institutional machinery necessary to become a major East Asian business services hub. Given the extraordinarily rapid pace of social and economic change in Asia, any future consolidation of Asian business in Taipei could happen very quickly.

¹ Tamim Bayoumi and Franziska Ohnsorge, "Do Inflows or Outflows Dominate? Global Implications of Capital Account Liberalization in China" (working paper, International Monetary Fund, 2013: 14).

² Cheng Li, "The End of the CCP's Resilient Authoritarianism? A Tripartite Assessment of Shifting Power in China," *The China Quarterly* 211 (2012): 617.

An international visitor to Taipei today might be forgiven for failing to see any potential for transformational change. By Western standards, Taipei can seem like a crowded and dirty city. It is not a major international financial center. English skills among the population appear to be relatively poor. The Globalization and World Cities Research Network places it as a fourth tier city alongside regional centers like Jakarta and Warsaw.³ International brands are available, but Taipei is no Hong Kong. And, of course, looming over it all is the threat from across the Taiwan Strait.

But Taipei also has cultural, political, and societal advantages that are unique within Asia, and these institutional advantages will only strengthen over the next fifteen years. Modern Taiwan shares a language and a history with the mainland. Although Taiwan is permanently tethered to China, Taipei is effectively independent of the Chinese authorities. Taiwan's freedom and democracy make it a safe haven from the vicissitudes of arbitrary government, which is practiced on the mainland and increasingly in Hong Kong. Furthermore, Taiwan's robust civil society ensures that Taiwan will ultimately solve the health and safety problems that plague much of the region.

Competitive liberal democratic countries like Taiwan are inherently better placed to deal with the complex problems that arise in modern society and economics than are countries ruled by a single party or that lack a full spectrum of political debate. Problems like corruption and the selective rule of law arise everywhere, but in countries with liberal institutions these kinds of problems can be exposed and dealt with openly. Businesses operating under liberal institutions may be wary of government regulation, but they do not have to operate in fear of uncompensated expropriation or arbitrary imprisonment.

Taiwan is already a liberal democratic country and Taipei is by global standards a very rich city. Taiwanese companies are global high-technology leaders and Taiwan is host to a sophisticated business community with extensive international experience, but Taipei is not yet a global city. In the 2010s and 2020s, macro trends such as capital and human flight from China and Hong Kong, increased tension between China and Japan, and the repatriation of hundreds of thousands of experienced businesspeople from China to Taiwan will likely converge to position Taipei to become a global city. As Hong Kong, Seoul, Shanghai, Singapore, and even Tokyo become marginalized within East Asia as regional or niche economic centers, Taipei could emerge as Greater China's and East Asia's one truly global city.

A Global City for All of China

Sociologist Saskia Sassen influentially characterized global cities as the “command centers” of the world economy, coordinating activities that are widely dispersed in

³ Globalization and World Cities Research Network, *The World According to GaWC 2012*, (Loughborough University: 2012).

geographical terms.⁴ Global cities are conduits for foreign direct and portfolio investment and serve as major centers of business services like banking, business consulting, insurance, investment advice, legal services, and trade finance. These cities are highly networked nodes of global economic activity.

Beijing is the center of the Chinese universe. However, as a capital city that governs one-fifth of humanity, it hardly has the human resources to manage China's economy—let alone China's economic relationships with the other four-fifths of humanity. The city of Beijing is indubitably and indelibly Chinese, not worldly or global. Though Beijing is the governing city of the world's most populous country, it ranks a measly thirty-fifth as a focus city for global producer services firms.⁵ Lacking an international commercial presence, it is not and never will be China's global city.

When people think of where China goes to meet the world, they think of Hong Kong and Shanghai. The internationalization of Hong Kong and Shanghai dates back to the 1842 Treaty of Nanjing, which ended the First Opium War and lasted nearly a century. Shanghai towered over Hong Kong before Japan's invasion in 1937 and later Communist victory in the Chinese Civil War. In the second half of the twentieth century, especially after the 1997 handover, Hong Kong became China's window to the world.⁶

The competition between Hong Kong and Shanghai in the twenty-first century is reminiscent of the competition between Amsterdam and London in the eighteenth century or between Boston and New York in the nineteenth century. In each case, a larger city with greater political power overtook a smaller, richer rival. The losing city continued to grow in absolute terms in each case, but was eclipsed by the much faster growth of the winner.

Will twenty-first century China tell a similar story? The key difference between the Shanghai-Hong Kong rivalry and previous financial rivalries is that China is a one-party state that lacks basic freedoms and robust civil society institutions. Property rights are anything but secure and never will be so long as the Chinese Communist Party (CCP) administers a unified party state. Investment calculations in China must always factor in the possibility of political interference or outright confiscation, imprisonment, and even execution. Today, opaque CCP offices, rather than official state institutions, administer China's anti-corruption campaign.

These considerations seem to favor Hong Kong over Shanghai. The problem for Hong Kong is that it is slowly but inexorably coming under tighter Chinese government (and CCP) control, as China's response to the 2014 Hong Kong pro-democracy protests

⁴ Saskia Sassen, *The Global City: New York, London, Tokyo* (Princeton: Princeton University Press, 1991).

⁵ P.J. Taylor and D.R.F. Walker, *World Cities and Global Firms, Globalization and World Cities Research Network*, Loughborough University.

⁶ Stephen Chiu and Tai-Lok Lui, *Hong Kong: Becoming a Chinese Global City* (Oxford: Routledge, 2009).

has made clear.⁷ Local business leaders often have no choice but to support this transition: their huge property investments in both Hong Kong and China proper require that they stay on good terms with Beijing.

The simple fact is that Hong Kong assets are now domestic Chinese assets and are increasingly treated as such by the Chinese government. The result is that Hong Kong is morphing from a rich offshore financial center used as a conduit for foreign investment into China into a rich onshore business center managing financial assets that are no longer Hong Kongese but Chinese. If Shanghai is China's New York, then Hong Kong will become China's Boston.

Singaporean pundits can see the opportunity created by hot money eager to find a home beyond China's reach, and the Singapore government is actively courting Chinese investors with light-touch regulation and red-carpet treatment.⁸ Of course, countries as far afield as Australia, Canada, and even the United States are also active in courting Chinese money. But none of these jurisdictions are practical operational hubs for China-focused businesses.

Singapore is often thought of as "Asia's global city," but Singapore is too far away (a six hour flight from Beijing), too foreign (culturally Southeast Asian and diaspora Chinese rather than unambiguously modern Chinese), and ultimately too risky (due to one-party, one-family rule) to become a permanent business base for China and the rest of East Asia.

Of course, Singapore is already a major global financial center. But China accounts for half of Asia's total economic output. For a city to become the Asian equivalent of London or New York, it must be the default location that companies use as a base for their businesses in China. It is hard to imagine major international corporations running their pan-China operations from Singapore.

Singapore may continue to flourish as an offshore financial center and focal point for hot money escaping China, but it will not become China's global gateway city. Nor will Seoul or Tokyo, as both are major cities that are outside of the Chinese cultural zone, ruled by governments that feel threatened by China, and that do not speak Chinese. Even North American and European companies do not run their China operations from Seoul or Tokyo. Seoul and Tokyo will forever remain national centers, rather than global ones.

It is possible that China will remain a multi-centered economy with financial and economic power widely dispersed throughout the country. But the historical tendency

⁷ Clare Baldwin, "China's No. 3 Leader Warns Hong Kong Activists against 'Crossing a Line,'" *Reuters*, March 6, 2015.

⁸ Lye Liang Fook, "Singapore's Economic Involvement in China's Reform," in *China's Reform in Global Perspective*, ed. John Wong and Zhiyue Bo (Singapore: World Scientific, 2010).

in other countries has been for economic power to consolidate even as economic operations disperse. For example, many major American banks now have administrative centers and even headquarters buildings spread throughout the country. Nonetheless, real financial decision-making is ever more concentrated in New York. Economic power will consolidate in China too, but as long as China's politics remain authoritarian and opaque, such a consolidation can only occur offshore.

As Hong Kong transitions from an offshore to an onshore center, Taipei is well positioned to pick up both business and skilled professionals from Hong Kong. Taiwanese business networks are already highly developed both in the southeastern Pearl River Delta (PRD) region of China near Hong Kong and in the central Yangtze River Delta (YRD) region, which includes Shanghai City and the Jiangsu and Zhejiang Provinces. It is only a matter of time before these existing industry-based networks graduate to become advisory and services networks.

Deepening Ties between Mainland China and Taiwan

In thinking about the future of cross-strait relations between Mainland China and Taiwan in the long term, it is instructive to go back just a few years to the turn of the millennium. In 2000, there were no direct flights between Taiwan and the mainland. Trade was practically non-existent, while direct trade and cross-strait investment were both prohibited. The 2000 presidential victory of Chen Shui-bian of the independence-minded Democratic Progressive Party (DPP) led to fears of direct military confrontation across the Taiwan Strait.

Fast-forward to 2015. There are currently 840 weekly flights between Taiwan and Mainland China, plus charters and unlimited additional flights over the Chinese New Year holiday.⁹ Taiwan airports collectively serve more mainland destinations (fifty-four) than Hong Kong (forty-four).¹⁰ An agreement to allow Mainland Chinese passengers to transit in Taiwan on their way to other overseas destinations was under negotiation at the end of 2014 and is expected to conclude soon.¹¹ And Taipei's Taoyuan Airport is the tenth busiest air cargo hub in the world.¹²

Of course, trade has also flourished. Mainland China is now Taiwan's largest trading partner and Taiwan is the mainland's fifth largest. Direct Taiwan-mainland trade of \$197 billion (2013) is nearly 40 percent as large as U.S.-China trade of \$521 billion, despite the fact that Taiwan has a population of just twenty-three million and much of Taiwan-mainland trade is still routed indirectly through Hong Kong. Mainland

⁹ Hsin-Yin Lee, "Unlimited extra Taiwan-China flights set for Lunar New Year," *Focus Taiwan*, December 26, 2014.

¹⁰ Don Lee, "'Stealing Our Jobs': Taiwan Angry as Ties with China Deteriorate," *Los Angeles Times*, April 4, 2014.; Hong Kong International Airport Fact Sheet, accessed January 28, 2015.

¹¹ Shelley Shan, "Taoyuan Airport Plans Expansion," *Taipei Times*, November 17, 2014.

¹² "ACI Annual World Airport Traffic Report," Airports Council International, December 22, 2014.

China's second, third, and fourth largest trading partners—Japan, Hong Kong, and South Korea—are all closely linked to Taiwan as well.¹³ Northeast Asia is a highly networked trading hub that, if not centered on Taiwan, has Taiwan at its center.

Trade between Taiwan and the mainland is governed by the 2010 Economic Cooperation Framework Agreement (ECFA). The ECFA and its associated Investment Protection and Promotion Agreement (known as the IPA) is only a framework agreement for closer integration (not a full, detailed trade treaty), but it does include extensive “Early Harvest” lists liberalizing trade in major categories of goods and mostly non-financial services. The passage of the ECFA was highly controversial in Taiwan. In addition, the 2013 signing of the follow-up Cross-Strait Service Trade Agreement (CSSTA) was the spark for Taiwan's Sunflower movement protests. The CSSTA remains unratified as of this writing.

Even without the CSSTA, Taiwanese professional services firms are now mostly free to operate in Mainland China. They have already begun offering services to the 88,000 Taiwanese firms operating on the mainland.¹⁴ Once they develop sufficient expertise, these services firms will almost certainly extend their offerings to other overseas businesses operating in China. Taiwan's longstanding commercial and historical ties with South Korea and (especially) Japan make it likely that businesses from those countries may prefer Taiwanese professional services firms over domestic Chinese ones. Although Japanese businesses often face extreme popular hostility on the mainland, they are usually warmly welcomed in Taiwan.¹⁵

Hong Kong firms may in the future become uncompetitive in the onshore market for services. The ECFA gives Taiwanese businesses much greater rights in Mainland China than the 2003 Closer Economic Partnership Arrangement (CEPA) between China and Hong Kong accords to Hong Kong businesses.¹⁶ Crucially, the ECFA and IPA also give businesses on both sides access to dispute resolution mechanisms, including formal mediation in cases in which government expropriation of investments is alleged. These rights also apply to investments via third party intermediaries.

Thus, for example, a Mainland Chinese investor that “round trips” investment through Taiwan gains access to international mediation in cases of government expropriation. Round-tripping can be done by first sending funds offshore to Taiwan and then reinvesting in China through a Taiwanese company. The implications for Chinese investors seeking additional protections vis-à-vis their own government are obvious. Given that business in Taiwan is generally conducted in Chinese (not English), this kind of

¹³ “Top 10 Trading Partners of the Chinese Mainland,” *China Daily*, February 19, 2014.

¹⁴ “A Bridge over Troubled Waters: Taiwan, Japan and South Korea Employ Huge Numbers of Mainland Chinese,” *The Economist*, November 8, 2014.

¹⁵ Michal Thim and Misato Matsuoka, “The Odd Couple: Japan & Taiwan's Unlikely Friendship,” *The Diplomat*, May 15, 2014.

¹⁶ Yun-wing Sun, “Comparing CEPA and ECFA: Economic Integration in the Asia-Pacific Region,” (paper, Hong Kong Institute of Asia-Pacific Studies, 2014).

investment round-tripping has suddenly become very easy for non-internationalized local elites in Mainland China.

This is not to suggest that Taipei's financial destiny is to be an offshore haven for questionable Chinese investments. For better or worse, all large-scale investors now make regular use of offshore tax havens, opaque shell corporations, and all sorts of legal legerdemain involving cross-border financial flows. The point is that Taiwan—unlike Hong Kong—now has investment relations with Mainland China that are on par with those of most of China's major trading partners.

Taiwanese companies operate with a depth in China that is rivalled only by those of Hong Kong, Japan, and South Korea. Currently, protection for investments flowing through Taiwan is on par with those afforded to investments from Japan and South Korea (and much better than those from Hong Kong). Additionally, Taiwan conducts business in Mandarin Chinese, unlike Japan, South Korea, and even Hong Kong. If any city in East Asia is going to become a major offshore center for business services in China, the process of elimination indicates that Taipei may be the only option.

Robust Civil Society in a Real Democracy

When China's Hurun Report rich list asked Chinese millionaires why they planned to emigrate, they gave three main reasons in roughly equal measure: child education, air pollution, and food safety.¹⁷ Like Mainland China, Taiwan in the 2010s has experienced controversies in all three of these areas. Unlike Mainland China, Taiwan is a robust democracy in which civil society movements can effectively influence government to promote positive political change. Taiwan's highly engaged citizenry actively holds its government accountable for solutions.

Taiwan President Ma Ying-jeou and the governing Kuomintang's (KMT) attempt to push through ratification of the CSSTA in early 2014 over the objections of much of civil society (and even a faction of the KMT itself) led to the blossoming of the Sun-flower resistance movement and a three-week occupation of Taiwan's parliament (the Legislative Yuan). As a result, President Ma's popularity plummeted and the KMT suffered a historic defeat in the November 2014 local elections.

While this can be read as a setback for cross-strait relations and the future of Taiwan's economy, an alternative reading is also plausible. The robust civil society that checks government power and enforces the alternation of parties in office in Taiwan is the same robust civil society that will ensure that Taiwan's education system is relatively cleansed of political biases, that Taiwan's air pollution is brought under control, and that Taiwan's food supply is secured from contamination. In the long run, democracy is much more important for the success of Taiwanese businesses and the Taiwanese economy as a whole than the ratification of any particular trade treaty.

¹⁷ Scott Cendrowski, "Why China's Rich Are Leaving," *Fortune*, June 5, 2014.

Whatever happens to the CSSTA and whoever wins Taiwan's 2016 elections, East Asia's economic integration will continue—and Taiwan will be in the middle of it. Taiwan shares a language and a culture with the mainland, but has political and social structures that more resemble those of Japan and South Korea. The importance of these advantages can be seen by contrasting the fate of Hong Kong's Umbrella movement with that of Taiwan's Sunflower movement. As civil society in Hong Kong fights a losing battle for relevance (and even survival), civil society in Taiwan continues to have a decisive influence over major economic policy decisions.

It is not preordained that Greater China must have a global city that integrates East Asia as London does with Europe and the Middle East and as New York does with the Americas and much of the rest of the world. Another completely credible scenario is a permanently fractured East Asian economy in which multiple regional centers dominate Mainland China, Seoul and Tokyo remain primarily national centers, and Japanese, South Korean, and Taiwanese companies operate in China via decentralized provincial-level operations. The general global tendency seems to be toward the consolidation of corporate control functions, but this is hardly an ironclad law of economics.

Coming together may, however, be a tendency of human beings. Human factors are very difficult to measure and are thus often overlooked in business-focused media and academic research. Smart, creative professionals do not want to live in Beijing or Shanghai because they do not want to poison themselves every time they breathe. Successful entrepreneurs do not want to risk their businesses on the arbitrary judgments of a compromised and capricious court system. The success of global cities like London and New York is predicated on their embeddedness in the kinds of free and democratic societies in which people want to live and participate.

Ironically, the ultimate effect of the repression of the pro-democracy Umbrella movement in Hong Kong may be to drive professionals (and their businesses) out of the city. Many of the movement's activists are, after all, students at Hong Kong's top universities. It is not inconceivable that there will soon be an exodus of educated people from Hong Kong seeking freer lives elsewhere, as was originally feared in 1997. Some of them may find their way to Taipei, and Taipei may become the richer for it—in more ways than one.

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