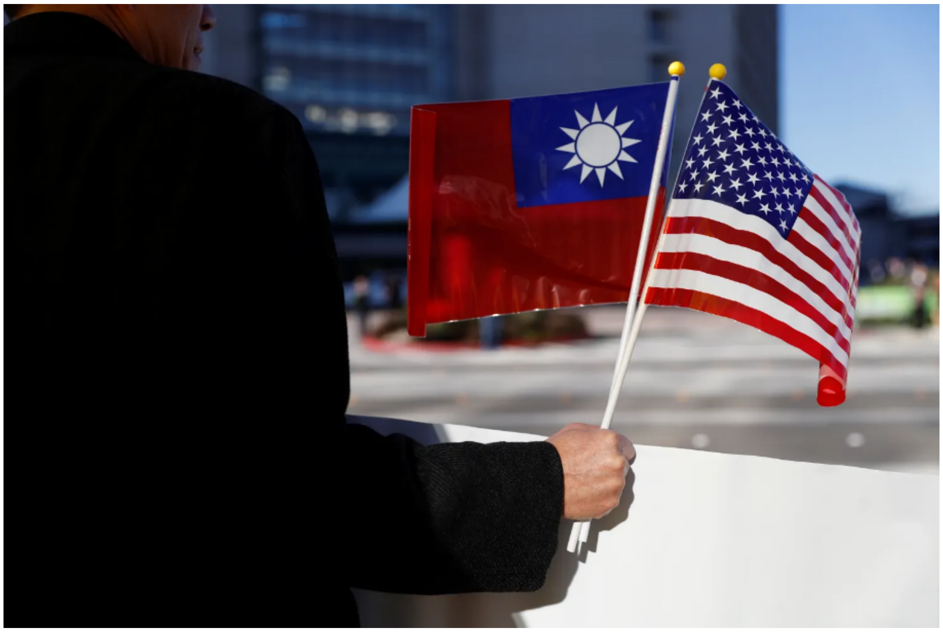
The United States-Taiwan 21st-Century Trade Initiative: A Model for "Benign Economic Statecraft"?

By Shantanu R. Kamat



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In this article, I provide a brief overview of the United States-Taiwan Initiative on 21st-Century Trade, negotiations conducted under its purview, and its deficiencies. Then, I introduce "benign economic statecraft," an approach that harnesses liberal tools to achieve national security objectives that states have frequently turned to more interventionist policy instruments to achieve. The "benign economic statecraft" approach will be considered as a means to pursue security interests, while preserving the liberal international order and promoting liberal institutions. I analyze the merits of expanding the U.S.-Taiwan Initiative into a broad free-trade agreement that contains market access provisions and reduces tariffs and other barriers to trade. Such an FTA could be a way to deploy economic statecraft to counter China's actions, without undertaking the herculean task of complete decoupling from the Chinese economy or advancing the deleterious goal of rejecting free trade and international economic liberalization. Finally, I analyze how a U.S.-Taiwan FTA could serve as a model for "benign economic statecraft" and how that would offer the United States the opportunity to reorient how it engages with the liberal international order.

United States-Taiwan Initiative on 21st-Century Trade

On 1 June 2022, the United States and Taiwan[h] launched the United States-Taiwan Initiative on 21st-Century Trade (hereinafter "the Initiative") to deepen cooperation, facilitate trade, and create a framework

[h] Acting through the American Institute in Taiwan (AIT) and the Taipei Economic and Cultural Representative Office (TECRO).

for negotiations down the road.[53] The Initiative was announced in the United States ten days after Taiwan was snubbed from the Indo-Pacific Economic Framework for Prosperity (IPEF), which forms a large part of President Joe Biden's East Asian strategy.[54] The non-inclusion of Taiwan in IPEF[i] created extra momentum within business, scholarly, and policymaking circles for separate international economic arrangements with the island economy.[55] The Initiative has elicited comparisons to IPEF and not only because of its development as an alternative way to foster U.S.-Taiwan cooperation. Nine of the eleven areas[j] identified by the Initiative for prospective negotiation overlap with IPEF provisions, with only the pillars concerning state-owned enterprises and non-market policies and practices lacking IPEF counterparts.[56] The Initiative and IPEF are also similar in what they leave out: market access commitments. Liberal economic policy scholars, as well as industry leaders, cite this exclusion as a reason that negotiations may be less fruitful than they otherwise could be.[57] Furthermore, the value of the Initiative could be attenuated by the fact that much of it is duplicative with other forums for U.S.-Taiwan dialogues on economic relations such as the Trade and Investment Framework Agreement (TIFA), the U.S.-Taiwan Economic Prosperity Partnership Dialogue (EPPD), and the Technology Trade and Investment Collaboration (TTIC).[58]

Despite these worries, one concrete agreement has been reached under the auspices of the Initiative. Agreed to in May 2023 and signed on 1 June 2023, the agreement directly addresses four of the eleven Initiative pillars that were laid out the previous year. It does so by committing the parties to a set of trade facilitation and customs administration measures, increases transparency regarding regulations, establishes anticorruption measures, and encourages SMEs in the United States and Taiwan to trade and invest in the other country.[59] The trade facilitation measures make up the bulk of the changes that the agreement sets into motion. Those measures simplify customs and border procedures and expedite trade through digitization of a whole array of processes.[60]

Nevertheless, the agreement falls short in several respects. Again, it contains no tariff reduction or market access provisions. Multiple commentators described the scope as limited to "low hanging fruit."[61] Trade policy scholar Inu Manak, for example, lauded the speed with which policymakers concluded the agreement (only one year after the Initiative's framework was put in place), but noted that contentious areas like agricultural trade barriers were avoided in negotiations.[62] Previously discussed paths forward like the elimination of double taxation on Taiwanese businesses operating in the United States to incentivize investments flows also failed to make their way into the final agreement.[63]

A second round of negotiations was launched in August and is ongoing.[64] According to a press release from the Office of the United States Trade Representative, the two parties have had productive discussions on agriculture, labor, and the environment.[65] However, it remains to be seen whether consensus can be reached on those issue areas.

"Benign Economic Statecraft"

Vinod K. Aggarwal and Andrew W. Reddie define "new economic statecraft" to encompass forms of "state intervention to influence trade, investment and industrial policy," instead of the old economic statecraft's focus on certain instruments like

[i] Many have speculated that the exclusion of Taiwan from the Indo-Pacific Economic Framework (IPEF) was done "in a nod to China's sensitivities about Taiwan being treated as a sovereign nation" and at the behest of certain Asian countries that were reluctant to fan the flames of mainland China's ire. See Palmer (2022) and Smith (2022).

[j] The Initiative's eleven specified issue areas are the following: trade facilitation, regulatory practices, agriculture, anti-corruption, supporting SMEs in trade, digital trade, "worker-centric" trade, environment and climate action, standards, state-owned enterprises, and non-market policies and practices. See Office of the United States Trade Representative (2022).

sanctions.[66] The goal is to use levers of state power to bend or influence international outcomes, especially in conditions of geostrategic competition.[67] Seeing insufficiencies in both neoliberal perspectives that focus on international economic growth to the exclusion of security, as well as neorealist views that highlight military power to the exclusion of international economic contestation, Aggarwal and Reddie offer "new economic statecraft" as a way to encapsulate the whole gamut of states' real-world actions today.[68] "New economic statecraft" can enrich our understanding of great power competition, especially in the twenty-first century context of a China whose rise has troubled much of the world and modern technologies which have worrying dual-use potential.[69]

The forms that "new economic statecraft" can take are as diverse as states' toolbox of economic policy levers, including industrial policy, strategic investments in what the state identifies as key industries (for instance, semiconductors and artificial intelligence), promotion of national champions, trade restrictions, export controls, investment restrictions and review procedures, and regulatory regimes.[70] What these interventions share is a departure from a rough postwar consensus on international economic liberalization, which took the form of tariff reduction; alleviation of onerous trade barriers; promotion of the flow of goods, services, data, and investment across borders; and international institutions like the World Trade Organization to facilitate this shift to an open and globalized world.[71] This departure is understandable in a world in which the United States faces China, a formidable peer competitor that is unafraid to use every economic tool at its disposal to gain a leg up on the United States. Nevertheless, the economic distortion that results from "new economic statecraft" is regrettable. As liberal economists have persuasively shown, moves away from free trade and toward protectionism have contributed to economically suboptimal outcomes, while also often failing to achieve the policies' purported national security objectives.[72]

The dilemma then is as follows: how can American policymakers simultaneously harness the benefits of a liberalization, globalization, and free trade, while also doing what is necessary to protect national security interests and best position themselves in a strategic game against China? I suggest one class of solutions here and discuss it in the context of U.S.-Taiwan trade relations. I introduce the concept of "benign economic statecraft," which is distinct from "new economic statecraft" but shares its major goals, including but not limited to national security, supply chain resilience, and strategic advantage vis-à-vis adversaries. "Benign economic statecraft" is defined here as the use of liberal institutions and/or instruments – such as free trade agreements, tariff and non-tariff barrier reduction, market access provisions, trade facilitation, etc. – to achieve the aforementioned objectives.

Unlike "new economic statecraft" which is inimical to principles and institutions of the liberal international order[k] (hereinafter "LIO"), "benign economic

[k] The precise definition of the liberal international order (LIO) is contested.
G. John Ikenberry identifies five necessary components that a liberal internationalist order must have: (i) openness (i.e. to international engagement and trade), (ii) international relations bounded and/or coordinated by rules and institutions, (iii) some form of security cooperation, (iv) acceptance of the possibility of reform and mutual benefit, and (v) global movement toward liberal democracy.
See Ikenberry (2018), 11: Ikenberry, G. John. 2018. "The end of liberal international order?" *International Affairs*, 94(1), 7–23. https://doi.org/10.1093/ia/iix241.
In addition to the international and rules-based aspects of the LIO, David A. Lake, Lisa L. Martin, and Thomas Risse emphasize the liberal components, combining political liberalism, economic liberalism (in either its classical liberal or "embedded liberal" form), and liberal internationalism (in John Ruggie's words, a multilateralism "which coordinates relations among three or more states on the basis of 'generalized' principles of conduct," which often involves foregoing short-term interests for long-term economic growth and stability). See Lake, Martin, and Risse (2021), 227-232: Lake, David A., Lisa L. Martin, and Thomas Risse. 2021. "Challenges to the Liberal Order: Reflections on *International Organization*." Challenges to the Liberal International Order: *International Organization* at 75 [Special issue]. *International Organization*, 75(2), 225–257. https://doi.org/10.1017/S0020818320000636.

statecraft" aims at the same goals, while preserving and in fact deploying liberal tools to achieve those ends. In that sense, "benign economic statecraft" could be a best of both worlds, in which liberal economic goals and security goals are pursued in parallel, with the pursuit of one not necessarily harming the pursuit of the other. Whether "benign economic statecraft" alone is sufficient to meet the global security challenges of the twenty-first century will not be conclusively resolved here. Rather, this piece introduces it as a theoretical contribution and perhaps something that policymakers can add to their toolkit as an alternative to more heavy-handed instruments of state power.

A U.S.-Taiwan Free Trade Agreement and U.S.-China Strategic Competition

During Xi Jinping's reign over the last decade, China has pursued economic statecraft more than ever, a development which has been reinforced by the era of strategic competition in which great powers find themselves.[73] Although China's economic statecraft efforts are far from universally efficacious, their scope, coercive nature, and dangers to the rules-based liberal international order (LIO) have concerned leaders and stakeholders around the world.[74] U.S. policymakers are faced with a seemingly intractable dilemma: they must actively compete with China's barrage of "new economic statecraft" policies, while also ensuring that their actions do not hasten the ongoing ossification of the global trading regime.

American policymakers have devised strategies that aim to thread the needle between respecting liberal economic goals and advancing security objectives. One suggestion goes under the name "selective decoupling," which Representative Mike Gallagher, Chair of the House Select Committee on Strategic Competition between the United States and the Chinese Communist Party, identified as one of three pillars[l] of a whole-of-government strategy to counter China.[75] Complete economic decoupling of the American and Chinese economies is impractical and would deprive Americans of the benefits of market access including lower prices and the ability to trade goods across borders.[76] However, Gallagher and Select Committee Ranking Member Raja Krishnamoorthi concur that in response to Chinese economic coercion, the United States should take proactive measures in certain sensitive sectors[m] including de-risking and diversification of those supply chains and industries that have a nexus to U.S. national security.[77]

However, de-risking and diversification cannot be achieved without an alternative to Chinese suppliers. Gallagher said, "You cannot selectively decouple, in my opinion, if you do not simultaneously deepen your economic engagement and technological collaboration with the free world at the same time to try and reduce our dependence on China."[78] The two – tackling the China challenge and increasing economic ties with other Asian countries – go hand in hand. And the latter should include traditional liberal institutions and tools like market access and free trade with peaceful economies. Gallagher's suggestion is consistent with adding "benign economic statecraft" to the American policymakers' toolbox. Not only can it in many cases be an alternative to damaging exercises of economic statecraft to counter China, but it can make attempts to counter China more fruitful, by enabling a gradual shift away from reliance on Chinese markets and suppliers. Moreover, it may also be an expedient way to generate buy-in from a business community that would otherwise be unwilling to countenance the economic disruption produced by an overly expansive departure from Chinese markets.[79] Gallagher added,

[l] The other two pillars that Mike Gallagher identified are hard power and ideological competition. See Gallagher (2023).

[m] In particular, Gallagher believes that U.S. economic policy should distinguish between trade in soybeans, textiles, and other goods without a clear nexus to national security, and those like critical minerals, pharmaceutical ingredients, and microelectronics, for which dependency on a strategic competitor could pose risks. See Gallagher (2023) and Ratnam (2023).

"And it should not be just the free world, as that's traditionally defined. We also have to get closer with some nontraditional partners."[80] Deeper economic cooperation in the Asia-Pacific should include expanding the United States-Taiwan Initiative on 21st-Century Trade into a true free trade agreement (FTA), which could be a potent tool of "benign economic statecraft."[81]

A U.S.-Taiwan FTA is not a new idea[n], but has received renewed attention in the last five years, given the salience of U.S.-China competition in American politics. During the Trump administration, however, Taiwan had fallen to the backburner in bilateral trade agreement talks.[82] A U.S.-Taiwan FTA would be a good deal for both parties. For the island economy, the commercial access it could obtain would assist its growth and survival.[83] For the United States, an FTA would achieve a dual objective: "secure better terms of trade while deepening strategic partnerships with China's rivals."[84] Despite Taiwan's small size and diplomatic isolation, it plays a large role in global trade, especially in key technology industries like semiconductors (which have dual-use capabilities and are critical for defense systems) and communications. Ashley J. Tellis noted that a "U.S.-Taiwan pact would accelerate the reorganization of Asian supply chains away from China and reduce China's ability to coerce America and its East Asian allies in times of crisis."[85]

Despite the U.S.-Taiwan Initiative's tremendous shortcomings, it does advance Taiwanese and American cooperation, which in turn bolster their positions vis-à-vis China. Former U.S. trade negotiator John Veroneau averred that the Initiative could hold powerful diplomatic significance, notwithstanding its relatively minimal economic impact.[86] I argue that using liberal economic tools to advance the sort of collaboration needed in the broader geopolitical arena – a centerpiece of the "benign economic statecraft" approach – is an especially worthwhile endeavor in the case of Taiwan. WTO data show that the United States was Taiwan's fourth largest recipient of merchandise exports in 2021, with the United States in turn being the second largest source of Taiwanese imports.[87] China is number 1 in both respects.[88] Expanding the Initiative into a free-trade agreement could be the beginning of a concerted effort to alter the balance.

For Taiwan, a U.S.-led trade agreement would allow a decades-long shift away from dependence on China. In the words of John Deng, Taiwan's minister without portfolio, "If our economy can not be strong enough, then there's only one place that we can go — China."[89] To preclude China from fomenting even more dependence on the part of Taiwan, the United States should present itself as a credible economic partner and bring Taiwan into the fold of an American-led rules-based trade order.[90] In addition to direct economic benefits, an FTA could pave the way for other advanced economies to seek greater economic relations with Taiwan or even join the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP), for which has already Taiwan has submitted a pending application.[91]

"In the past, the United States has 'friend-shored' by signing trade agreements with like-minded countries that eliminate tariff and non-tariff barriers to trade, thereby making it easier for goods, services, and capital to flow between them," writes Tori Smith.[92] Of late, by contrast, policymakers have put forth "anti-market policies associated with onshoring and nearshoring," whereby manufacturing, supply chains, and operations are returned to the United States or a proximate country. Given that "free trade agreements are a proven model for friend-shoring in a pro-market way," I argue that is amenable to be part of a "benign economic statecraft" approach.[93] Large-scale government interventions like the CHIPS and Science

[n] For example, a 2002 U.S. International Trade Commission report estimated the likely impact of such an agreement at the request of the Senate Finance Committee and the House Ways and Means Committee. See United States International Trade Commission. 2002. "U.S.-Taiwan FTA: Likely Economic Impact of a Free Trade Agreement Between the United States and Taiwan." Publication 3548, Investigation No. 332-438. https://www.usitc.gov/publications/docs/pubs/332/pub3548.pdf.

Act and other industrial policy measures frequently misallocate resources, underdeliver on promised benefits, and invite other countries to pursue distortionary interventions, like subsidies and export controls, of their own.[94] By contrast, an alternative that would encourage the private sector to better manage geopolitical risk and deal with supply chains disruptions amid strategic competition with China is to expand market access and lower barriers to the flow of goods and services.[95] A tried and tested way to do this is by offering FTAs to friendly economies, especially those that are strategically significant in key industries like semiconductors.[96] The United States has fallen behind in making FTAs, which means not only foregone economic benefits but a missed opportunity to assert itself in establishing the rules of the road and setting standards for the global economy.[97]

A U.S.-Taiwan FTA would incentivize friend-shoring in a place which adheres to important norms of the global trading system. In doing so, an FTA could help achieve the House Select Committee on the CCP's vision of de-risking, diversification, and selective decoupling from China. "The best way to incentivize companies to shift supply chains out of China is to create alternative markets for them that are economically viable and help them mitigate rising security concerns in China."[98] One study estimates that an expansive U.S.-Taiwan FTA that slashes tariffs and reduces non-tariff barriers across several industries would increase total trade by $6.2 billion for the United States and $3.8 billion for Taiwan.[99] Such an agreement would also reduce both the United States and Taiwan's economic ties to China, without adversely harming their economies. Taiwanese exports to China would decrease by $1.8 billion, and their imports from China would decrease by $323 million.[100] Furthermore, U.S. imports from China would decrease by $775 million.[101] China's total trade volume would fall by more than $1 billion annually, with a negative effect on Chinese GDP.[102]

Kurt Tong, former U.S. Ambassador for APEC, gave three key reasons in advocating for a U.S.-Taiwan FTA: (i) Taiwan's role in strategic trade, (ii) Indo-Pacific "economic geopolitics," and (iii) trade policy agenda setting.[103] All three indicate that the opportunity is ripe for the United States to pursue "benign economic statecraft." Taiwan's importance to the semiconductor industry[o] and the opportunity for the United States to demonstrate a commitment to the political economy of the Indo-Pacific region means the United States are strong reasons for American policymakers to leverage the Initiative and begin negotiations with Taiwanese authorities for a free-trade agreement.[104] Despite the fact that a lack of political will, especially in the United States, has been a critical impediment to securing an FTA, circumstances could be changing to make that prospect more propitious.[105] Although there has recently been bipartisan hostility to international trade, Taiwan seems to be an exception to the rule. A U.S.-Taiwan FTA could plausibly pass Congress, given legislators' hostility toward China, a bipartisan recognition of Taiwan's strategic importance, and members of both parties urging the executive branch to begin negotiating with Taiwan.[106] With the July 2023 passage of the United States-Taiwan Initiative on 21st-Century Trade First Agreement Implementation Act (H.R. 4004), Congress retroactively approved the agreement reached under the auspices of the Initiative, and appended reporting and consultation requirements for future negotiations.[107] In doing so, Congress ensured that it can effectively perform its role in international commerce and demonstrated a keenness to pursue further trade and investment relations with Taiwan.[p]

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[o] In particular, Taiwan is home to the Taiwan Semiconductor Manufacturing Company (TSMC) which produces high-end chips.

[p] H.R. 4004 will make U.S.-Taiwan trade negotiations more enforceable, transparent, predictable, and durable, and by so doing, will "strengthen[] economic ties with Taiwan for mutual benefit—emphasizing the past U.S. commitment to reciprocity in trade, whereby the United States would grant access to its market in exchange for similar concessions from its trading partners." See Manak (2023).

Implications for the Future of the Liberal International Order

I posit that a U.S.-Taiwan FTA can serve as a model of "benign economic statecraft," which can advance American security interests in an era of strategic competition with China, while also reaping the benefits of the liberal international order (LIO) which has promoted global economic growth since the 1950s. This approach is especially important in light of recent developments in U.S. economic policy. Consider the following.

The Trump administration's foreign economic policy toward East Asia was marked most prominently by his withdrawal from the Trans-Pacific Partnership (TPP) in 2017 and by his trade war with China – developments that were harmful to free trade and the LIO.[108] Hopes that President Biden would reverse the bulk of these policies have proven incorrect, with the endurance of economic statecraft and protectionist policy indicating that the LIO will continue to fragment.[109] The Indo-Pacific Economic Framework for Prosperity (IPEF), the Biden administration's signature policy framework for the Asia-Pacific, to which the U.S.-Taiwan Initiative looks similar, is weak and unlikely to advance either its putative economic or security goals.[110]

I contend that a new orientation of international economic policy is sorely needed, and this is where "benign economic statecraft" can play a role. As Mike Gallagher stated in an interview, "There's no trade agenda right now in Washington in either party, and that's a huge gap in our overall strategy."[111] The United States should be willing to pursue bilateral and minilateral regional FTAs in the Asia-Pacific so that countries reap the benefits of American market access and come to regard the United States as a valuable economic partner. Expanding the Initiative into a genuine U.S.-Taiwan free-trade agreement can serve as a model of how this approach can work. This is especially crucial in a world facing the bifurcation of investment, trade, and global value chains.[112] Bilateral FTAs, like one between the United States and Taiwan, would simultaneously acknowledge this reality, while managing to promote trade in a world in which the West will have to look beyond China for imports and investment.

The "benign economic statecraft" approach, which a U.S.-Taiwan FTA could help pave, can be applied to trade agreements with other countries and regions. The lessons can be applied to southeast Asia, for example, where countries have been upset with insufficient U.S. economic engagement and dithering on market access commitments.[113] The Biden administration has failed to capitalize because it does not appreciate that such commitments are the key lynchpin in securing countries' participation in a U.S.-led liberal order, rather than falling into the hands of China.[114] In Latin America too, countries such as Uruguay have moved to increase trade with China after and as a result of insufficient engagement from the U.S. to secure FTAs.[115] The United States should put in the work to assuage the fears of middle powers around the world to secure allegiance to the West and to forestall Chinese manipulation and influence.

In conclusion, policymakers in the United States should consider crafting a free-trade agreement with Taiwan, instead of merely pursuing weak policy vehicles under the extant U.S.-Taiwan Initiative on 21st-Century Trade. In doing so, they should add "benign economic statecraft" to their arsenal and be willing to deploy it in other instances with the primary goal of advancing American security interests in an era of strategic competition with China, while also reaping the benefits from trade partnerships that have been integral to global economic growth for more than seven decades.