THE BROOKINGS INSTITUTION

WEBINAR

ASSESSING TAIWAN'S ECONOMIC RESILIENCE

Tuesday, December 3, 2024

PANEL DISCUSSION:

SYARU SHIRLEY LIN
Nonresident Senior Fellow, Center for Asia Policy Studies, The Brookings Institution
Chair, Center for Asia-Pacific Resilience and Innovation

ALICIA GARCÍA-HERRERO
Board Member, Center for Asia-Pacific Resilience and Innovation
Chief Economist for Asia Pacific, Natixis
Senior Fellow, Bruegel

RICHARD C. BUSH
Nonresident Senior Fellow, Center for Asia Policy Studies, The Brookings Institution

MODERATOR: RYAN HASS
Chen-Fu and Cecelia Yen Koo Chair in Taiwan Studies, Senior Fellow and Director, John L. Thornton China Center, The Brookings Institution

* * * * *

HASS: Good morning, everyone. My name is Ryan Hass, and I am the Koo Chair in Taiwan studies at the Brookings Institution. And today, I'm delighted to have an opportunity to moderate a panel on Taiwan's economic resilience. This event is the first in a partnership with the Center for Asia Pacific Resilience and Innovation, otherwise known as CAPRi, which is a leading independent think tank in Taiwan. We will use the coming hour to examine Taiwan's economic strengths, its potential risk points, as well as the road ahead, especially in light of China's relentless pressure on Taiwan and the presidential transition underway in the United States. We have an all-star panel to help us think through these questions.

I'm going to be inconsiderately brief and introducing each of our panelists so that we can maximize time for our discussion. But I encourage everyone to see their accolades and backgrounds on our event page on the internet. Our panelists are CAPRI founder and chair Syaru Shirley Lin. Shirley is also a nonresident senior fellow with the Brookings Institution. Her research and teaching focuses on cross-strait relations, international political economy and the challenges facing high income societies in Asia. Our second panelist joining us from an airport is Alicia García-Herrero. In addition to her work with CAPRI as a board member, Alicia is the chief economist for Asia Pacific at Natixis. If she has to leave slightly early, it is not in protest. It is in consideration of a flight that she will have to catch.

And our third panelist is the unofficial dean of Taiwan studies in the United States, Richard C. Bush. Richard was the first Koo Chair in Taiwan Studies at Brookings after a distinguished career in government. He has written too many books about Taiwan and U.S. Taiwan relations to cite here, but I will flag one, which is Difficult Choices, which is a book that examines the tradeoffs and policy choices that Taiwan leaders face. And it's particularly relevant to our conversation today. So, with that background and context out of the way, I'm going to jump straight into our discussion and I'm going to start with you, Shirley. Can you help us understand, just to set the stage, what is economic resilience and why is it important for Taiwan?

LIN: Thanks, Ryan. It's such a pleasure to be back at Brookings and also to join you for the first of Brookings CAPRi event. Economic resilience is one of the most important issues that CAPRi and Alicia and our focus on. The standard definition, of course, is to withstand for any society, especially

Taiwan, to withstand systematic shock that includes policy shock and otherwise. But at the same time, to create a consensus in the society, to grow the economy, to actually have economic resilience, which is part of societal resilience, as you know, for Taiwan, that's incredibly important in today's increasingly tense geopolitical environment. There are two challenges for Taiwan in that regard, and I'll be brief because I know that rhetoric and Alicia will add a lot to this. The first its overreliance on semiconductor and the technology ICT sector. Second is Taiwan's overreliance on China, both as a market and as a place for manufacturing.

HASS: So, with that as background is to what economic resilience is, I'm going to ask each of you to rank on a scale of 1 to 10 how economic reset resilient Taiwan is today, with one being not resilient and ten being fully resilient. Shirley, why don't we start with you and then we go to Alicia and Richard.

LIN: Well, I hate to be the first to answer the question because I don't have an answer. It's impossible to rate. I think the most important thing, actually, from my point of view, is to think about it comparatively. Over the past five years, as you know, the global economy had a huge health shock. The COVID-19 challenge. Even then, Taiwan grew at the highest rate in Asia and one of the highest in the world in 2021. But you can see that the economic resilience of Taiwan is dropping like the rest of the world. Over the next two years, the forecast and I think Alicia will be better able to rate than I can.

HASS: Over to you Alicia.

GARCÍA-HERRERO: Well, I can't read either, surely. But I can add that I think Taiwan has proven to be more resilient than we thought. This is not only COVID, but, you know, frankly, Taiwan's growth rate in the last few years is much higher than it was before. We used to be the whole out economy where, you know, everything would go to the mainland. That has changed dramatically.
And in that regard, I think that one is one of the very few places which has managed to go back from that hollow out to a new massive manufacturing platform, bringing back industries, which is quite impressive. However, maybe. Anyone could be dying of sepsis, if you think about it, meaning this very, very successful semiconductor industry is becoming that disease.

And although we can't really see that in inflation data into one which remains very low, although, you know, one wonders really why it is so low. If you look at the cost of living below, you know, housing prices. And it is just my worries that that because we've been so resilient, it may end up being a problem because it's creating income distribution issues, you know, and that might make Taiwan less resilient for reasons that in a way are not the ones that should have been in the very beginning. So, I would say Taiwan is becoming less resilient economically than it was only recently. And this is because of this kind of success idea.

HASS: Right, Richard. I think you're on mute at the moment.

BUSH: Yes. Sorry. Thanks for doing the program. I was not able to give Taiwan a composite ranking, so I broke it into two. And first of all, there is the private sector, which was a manufacturing sector. I give them high marks, sort of 8 to 9 out of 10. This is a very dynamic sector, very adaptive to demands and to changes in demand, reacts well to negative changes in the environment such as COVID. And to an apparent, impressive group of entrepreneurs. On the other hand, you have the political system. Couple of different aspects. One is the executive branch of the government, which I find to be overregulated in certain sectors, including finance, but a lot of other ones as well. But also, the competition and conflicts in the political parties. But, and, you know, if Taiwan is going to be resilient in a larger political sense, the political party is going to have to get together and work some work out some sort of consensus to underpin the society's future success.

HASS: We are going to come back to that question about politics and its implication, and kind of resilience soon. But before we do so, Alicia, I want to go back to something that you were talking about. Can you start out first by just sort of giving us an economist view into how Taiwan's economy is performing today, both relative to its past, but also relative to its peers?

GARCÍA-HERRERO: Yeah. So, frankly, Taiwan is performing pretty well. If you if you just happened to go to Seoul and you come back to Taipei, you'll see the difference. The South Korean economy is also very dependent on semiconductors, actually less than Taiwan. But they feel they're missing out on the opportunity. And when you actually land in Taipei, you can see, you know, this land of opportunities, AI chip related, you know, much more symbiotic with the U.S. So, in that regard, I think that one doing great. I mean, growth is well above potential. Wages are not growing as far as I have to say. There's still this issue of average wage wages being still very low. However, for the industry that quote unquote matters. They're doing exceptionally well wage wise.

Disposable income is growing. The stock market is doing well. I mean, you name it, however. This is again, bringing this kind of dichotomy between the sector that is doing well, which is growing and growing. Just one single company, 40% of the stock market. So, you know, it's like a little bit too much of a concentration and then the rest. The other thing on the positive side that I want to add is that the Taiwanese economy has diversified very rapidly. I mean, I can't think of any economy that has moved from exporting 40% to China in 2021 to barely 20%. I mean, as quickly as that. But this is because of the massive value of AI chips, which are basically going to the U.S. So, exports to the U.S. are blooming.

Maybe we shouldn't say this to the incoming president. I'm thinking the current account surplus is hovering between 15 and 12%. So don't check on this one because, you know, it can get pretty tough. And the diversification is also happening on the foreign investment. So, within the Biden administration, 80% of Taiwan's foreign investment was going to the mainland. Now it's barely 20%. So, you know, it's so rapid and it's so impressive. But again, the problems are on this dichotomy of sectors, which I think could harm the economy in the long run.

HASS: Well, let's stay there for a second, because you mentioned ‘Dutch Disease’ earlier, or ‘Dutch Tulip Syndrome.’ What is that? How does it apply to Taiwan and how concerned should we be about it?

GARCÍA-HERRERO: So basically, we want to buy an apartment in Taiwan. And it's not only in Taipei because actually housing prices are growing faster elsewhere. Why? Because for us, this is going to go on or, you know, it's just not only Taipei anymore. So, the whole island is becoming extremely expensive. And this is because there's a sector pushing prices up. The other sectors cannot catch up.

Those wages cannot catch up to the prices that are pushed by a single sector doing very well. So, you know, we economists use that concept of ‘Dutch Disease,’ which comes from the old tulip, tulips in the Netherlands, making whole the whole country very expensive and not affordable. So, the whole idea is affordability. I think that Taiwan has an affordability problem on the housing market and increasingly beyond the housing market. Yeah.

HASS: Surely. Richard, before we move on to Taiwan's political economy, would you like to weigh in at all on this issue of affordability and disease?

BUSH: Let me just reaffirm what Alicia said about the distribution problems that this IT dominated economy creates. And it has great political ramifications that we've seen over the last ten years. I do think that we shouldn't go too far in comparing IT chips to tulips. There's the impressive thing about Taiwan is that however, whatever sector you're in, it's constant innovation. How much can you innovative tulip, really? So, looking outwards, I think that you know there are risk with relying so much on chips. But as Felicia said, it's a desert diversifying economy. It's always adapting.

LIN: And I'll add to both my panelists are in full agreement on the issues that Alicia just raised about basically this driving inequality. So, the implications of a non-diversified economy are many. I think one of those things is the last 30 years. As you know, Ryan, Taiwan grew very fast during its golden age and under industrial policy about four decades ago. But the miracle, of course, is that it became more equal. And I think the last few years have really seen a change in that the top 20% ratio to the bottom 20% ratio, the bottom 20 in terms of asset is used to be 4.9 times. And now it's six basically we're talking about 6.1 times in 30 years. So, this rapid increase of inequality is leading to some other issues that I know we're going to talk about later in the program. But the second thing I want to pull back a bit on, and I agree with Richard to it's wonderful that Taiwan has an innovative society. And this year, we've on behalf of CAPRi, Alicia and I and many others, have actually been to several places Jakarta, Auckland. It's very hard to have an innovative society that continues to be innovative. So, I think it's great to have a foundation, but that leads to other problems like trade deficit with the U.S., of course, increasing trade deficit as the etcetera takes off. And then the issue, of course, is how to sustain that and to create jobs for young people, which the United States is also facing. But final word is resilience. We're talking about here is societal resilience. Economic resilience is the foundation of it. But to have public health resilience, to have security and to have all of the other things balance. And this is what, of course, Richard's book is all about.

HASS: Right? But I want to get to the more conceptual resilience shortly. But before we do so, Richard, let's turn to you to talk a little bit about Taiwan's political economy and to just help us take a step back and provide a historical lens to why Taiwan's economic policy has been so focused on supporting specific industries and to preserving such low tax rates.

BUSH: But let me talk about the tax rates first briefly. It Taiwan's government's revenue as a share of GDP is relatively low, around 15%. That is lower than a lot of other advanced economies in East Asia and elsewhere. That's understandable in a way, because it's one of the ways that Taiwan remains competitive, that at least that cost of doing business is less. Also, there is political resistance to higher taxes from households, corporations, stockholders. That's true in any democratic country. But for example, Taiwan has virtually no estate tax. So, wealth gets passed on and there's no redistribution. As you might expect.

Now, on this question of the government leadership of the economy, Taiwan is held up as an example of what political scientists call the developmental state, where at least in early stages, the government tries to pick product sectors that could be globally competitive and then allocate capital, technology, human resources and so on to bolster those sectors. And then probably spin them off into the private sector. And TSMC is a great example of this. Maurice Strong works for Texas Instruments. He goes back to Taiwan in the late 60s. There's a license with RCA and the Government Institute. E-Trade takes this over or takes this project over. Makes a lucky choice in semiconductors as the winner of the future and builds up the corporate capacity and then spins it off into TSMC.

So there is some merit in this, but there is a competing view and that is notwithstanding the companies that were fostered by the state, you have a lot of big companies today that started as little operations, the product of an agreement among a group of friends and family people to build a factory out in a rice paddy, producing something that fills a niche in the global marketplace. And it's many of these operations failed. A lot more succeeded and grew. And because they were very adaptive and innovative and if one product line was dying out, they would shift to a completely different one. That's quite, quite impressive. And it's the mix of state led in some sectors and private initiative and others that I think is the real Taiwan miracle.

HASS: Interesting. And you've coined the term difficult choices for Taiwan. What are the difficult choices that Taiwan policymakers must grapple with most right now while they try to preserve economic competitiveness?

BUSH: Well. I think there are two summarize. There are a couple of basic ones that need to be understood. And one of them we've talked about in a way, and that is the choice between fostering economic growth on the one hand and fostering human welfare on the other. And I've already mentioned, and we've mentioned the distribution problem that is created when you have your economy dominated by a technologically advanced sector and it creates gaps in income and wealth and housing and access to really good education. If you compare the. Top quintile of income. With the bottom quintile of income. The top one is 6.1, four times the bottom one. That means somebody in that top group has $6 to one of the guy at the bottom of the scale. And as I mentioned, the tax system does not redistribute wealth.

So, this is a, I think, a fundamental problem. And the bias has always been towards promoting growth. The demographics exacerbate this because Taiwan next year will enter a small group of economies that are called super aged. That means that over 20% of the population is 65 or older, which puts a great burden on the people who are still working and must support not only their own children, but also older generations and must pay help pay for higher pension payments and health care and so on. There's an interesting set of tradeoffs when it comes to energy, which is a component of growth. Taiwan relies on three main sources coal, oil, natural gas or fossil fuels. Then you have renewables which are starting to build, and then there's nuclear, which because of political reasons, is being phased out. The problem for me is that I want politicians have been arguing about this problem for 30 years at least, and they go back and forth on how much how nuclear should be dealt with. But it's my impression that if you are basing your economic growth on A.I., you're going to lead a hell of a lot more electricity than Taiwan produces for itself. And so how are you going to solve this problem? So, and then there's a bigger tradeoff, and that is between the good life. On the one hand, both economic well-being and human welfare and security on the other.

And this is, you know, the problem of how to cope with China. And there have been two main answers. One answer is engaging Beijing, cooperate wherever you can, and reassure Beijing about Taiwan's intentions. The other view is that. We can't trust China. Their intentions are malign, and the best thing we can do for ourselves is deterrence, including close cooperation with the United States. And this is another one fundamental issue where there is no agreement. It's this this tradeoff is reflected in the budget and. It's interesting that. Of the entire government budget, 67.9% goes to growth and welfare. 12.1% goes to defense. And. And it's another place where the political system has not been able to sort of reach a fundamental consensus.

HASS: Yeah. Well, I want to turn to Shirley now to help us understand how some of these things break along political lines. But, Richard, I think that your point about the percentage of government spending allocated to defense is probably a better measure of Taiwan's investment in events than percentage of GDP invested in defense because it speaks to the prioritization on a relative basis as being applied to defense. And that's probably where we should focus our attention. But surely help us understand how some of these issues that Richard just touched on. How do they break along partisan lines? Are they partisan issues? How do politics impact policy choices?

LIN: Yeah. So, I think Richard Alito pointed out the big sort of fault line in domestic debate. And I think this is where, of course, U.S. policy matters a lot. But coming to just a domestic debate, the three big policy issues that are dividing the people that have been divisive are energy policy, health reform, and, of course, defense.
So going back to the first point that Richard raised about nuclear policy, nuclear energy, energy, basically the way the government is now proposing to decarbonize. By the way, Taiwan is, relatively speaking, does not do too well on green transition. But, of course, as Richard pointed out, growth dominates as a priority. And I think things are really changing. So let me give you some data to substantiate that. First of all, within those so over 80% of KMT members were those who supported the claim to support nuclear energy. So that's one thing that's obviously a party divided party line

divided. But among the TPP members now supporters, actually 44% were 40 to 45% are for it and against it.

So, you could see now is becoming more even. Even those within the TPP understand that if there is no nuclear energy, how are we going to continue this growth rate when Japan and South Korea are achieving there will only achieve their goals if more than 20% of their energy mix eventually are going to be reliant on nuclear energy. More importantly, those under 30, 70% of Taiwanese young people support nuclear energy. And so, there is a generational divide where green transition is much more important to the younger generation than anything else. So, second on health, this I don't need to dwell on. But again, one of the things I'm doing a lot is to think about it comparatively. How is Taiwan doing compared to South Korea and Japan in terms of health?

We're a super aging society as Richer says. As of next year, we step into that super category, which is very scary as well as becoming a has been a high-income society. But if you look at Japan that spends 11% of its GDP on health. And I think maybe for defense it's not useful. But for our health, it's very important because there are global standards for this. And health is something that we're investing a lot of time and effort on. Korea spends 8% of its GDP on health. Taiwan spends merely 6%. Yet it's becoming so much older society, there are fewer younger people who need to support health. And we have wonderful health coverage. But during COVID longevity actually declined. So, what we're really doing with the health system is that we're taking care of urgent needs but really not doing things to help sustainability, health, sustainability, to keep people healthy, happy and have quality of life as they age.

The third issue that's very important and this we can talk about more with returning Alicia, who know a lot, is defense. And of course, there's no doubt that 2.4 or 5% this year is going to defense. And we know that Trump has already said 5%, 10%, whatever the number is, it's not really achievable. And it's not very helpful for Taiwan to overnight try to increase its budget, its government budget, as doctor says, which is a better, better measure when it also needs to spend more on health, more on energy. So, all of these priorities are the difficult choices that we're talking about. And I think defense is one issue where it's also very important that Taiwanese in the most recent surveys show about also just under 50% of the people believe in increasing taxes to increase spending on defense. But the similar percentage say no. And so, you can see it's a totally polarized society on all of these important issues. And that is what democratic governance is, is all about.

HASS: And so, surely, would you say that polarization is the main impediment to some of the reforms that are intuitively necessary to sustain Taiwan's economic growth and resilience? Or are there other political factors that are serving as impediments as well?

LIN: It's an interesting question conceptually, Ryan, because is it the cost or the effect? Is it a demonstration of the polarization that we have a divided government since January, where, of course, the KMT and the TPP actually dominate the legislature? And right now, of course, the Chairman of the TPP is in jail. And so, we have a very fractured domestic political scene. And the minister of labor has just resigned because of workplace culture. So, we see the. The parties are going through huge dramatic challenges and the committee as well with a lot of, of course, pro-China activities that people are very concerned about, as Richard says. So, there are those who are really concerned and those who say we need to accommodate China.

But the divided government that we have is probably a sign of the long-term polarization that will now, of course, be intensified as U.S. policy close in on forcing Taiwan to make even more difficult choices. So, the ability of Taiwan to be economically resilient rests very much on how it walks the tightrope between Beijing and Washington. And that has just become increasingly difficult with Beijing the way it is in Washington, moving towards actually squeezing Taiwan more in some people's view. And so, I think that the polarization in the government is emblematic of the societal division.
And the societal division is only worsened by external policy changes from both China and the U.S. and the entire geopolitical reconfiguration of supply chain that Alicia has done a lot of work on.

HASS: Great. Well, we've spent the first half hour looking from the inside out at Taiwan's economy. Let's spend a few minutes looking from the outside in. Surely identified China, China's slowing economy, as well as the return of President elect Donald Trump to the White House in the United States as twin factors that are going to put pressure upon Taiwan's economy. Can you help us think through how these twin issues are going to buffet Taiwan's economy? Alicia, maybe we'll start with you and then we'll go to Shirley and Richard.

GARCÍA-HERRERO: Well. It is quite clear that there are clouds out there for Taiwan. And Taiwan has not really been, you know, the target of any of Trump's kind of comments on ties. But I think it's coming because it's quite clear that if you focus on the trade surplus, as I mentioned before, why don't we NTD for, you know, for the strength of the economy, I mean. Very, very massive foreign reserves. I just think that Taiwan has a few, you know, got quite a big ticket to be spelled out in and get some of the flurry of tariffs that Trump is coming with. But I would I want to link your point to the previous issue about the tradeoffs. I want to highlight one trade off that I think one needs to tackle as soon as possible before the 20th of January. I mean, I know this is impossible, but just and that this opening up its economy, it needs to open its economy is very simple.

But, you know, Taiwan is still dominated by not only state owned. I mean, the banking sector is unacceptable. Many others, I mean, energy, you name it. But beyond that, in the private sector, it's actually very concentrated in a few names and families. We all know there's very little space for foreign competition in Taiwan. I mean, if you need to show your willingness, you need to change. You just need to change this and even at least show your willingness to change this, which I think Taiwan has not really done for years. This is the time to do it. So, I would say, you know, the challenges are there, but Taiwan work to show willingness to open up to become more open to foreign competition. Taiwan already has multinationals.

So those multinationals just don't keep reserves. You know, I see your rates, massive savings that go nowhere. It's the say is that all of this has to change because if you actually work and I finish here, if I were to cover the name Taiwan and I show you the picture of the economy, you will think it's the mainland. And this is a problem if you have a different discourse. You need to change this. That's the only way, I think, to, you know, to bring to call the attention of the West. Trump But even Europe, for that matter, because such a concentrated economy plus a big trade surplus, but a lot of savings and not opening up the rest of the world is the worst combination I can think of in the current geopolitical circumstances.

HASS: Interesting. Shirley?

LIN: I think it's quite important to remember Taiwan persevered and remain resilient despite not really having international status. And I think this is where really, if you look from the outside in, it's quite important for Taiwan to be engaged, continue to be engaged with China actually as $200 billion of our 400 billion foreign direct investment still remains in China. The last eight years has been remarkable, as Alicia says, in making trade and investment go down to a ten-year low. 28% of two-way trade is China. That's remarkable in the span of a few years. And yet FDI has also now dropped to only one third of its investment in the U.S. U.S. now is surpassed and is three times more than what I want to invest in China. But those are the low hanging fruit. To diversify even more now is going to be quite difficult.

And I think that if you look at what the economy economic structure is, Alicia is absolutely right. This is a chance to because of the difficulty in managing the tightrope between Washington and Beijing, this is a chance for Taiwan to actually open up. And this means from the education to reform its education system all the way to basically welcoming foreign talent to get the talent from all over the world. I just want to cite one data. There are only 30,000 white collar foreign workers in 2018, and that has increased to 49,000, which sounds like a great percentage increase, but it's nothing compared to Singapore, a much smaller place. But there are over 200,000 white collar workers who remain there for a very long time.

Very few people stay in Taiwan for a very long time. So, we have this issue of basically the talent not matching the opportunity. And that goes everywhere from private sector, the financial sector, the IT sector. We're moving from hardware to software, which will be the key to continue to innovate because we cannot be the cheapest manufacturing hub for many things forever and ever. And if we don't actually have the ability to attract both investment, so venture capital funds, entrepreneurship, NGOs like ours, all of this is very new to Taiwan in terms of creating an international environment. And I think that the under the Trump administration, if I could just jump ahead and say one thing, it'd be great that the Republican Party actually dominates both the executive and the legislative branch, and hopefully some kind of a deal would be possible for Taiwan in the U.S. as you've also written about this, the importance of this to help Taiwan domestically reform and really become part of a more competitive world.

HASS: Thank you. Richard, before I turn to you, let me just ask Alicia one final question before she runs to catch your plane. I know that you're you have, like, one minute. But what do you see? Just in a few sentences, as the growth drivers of Taiwan's economy going forward.

GARCÍA-HERRERO: Well, in the current circumstances, the growth driver is manufacturing and the carving out of growth comes from agents. That's what it is. But I think if one opens up to foreign competition, opens up to foreign labor, opens up to talent from the rest of the world more generally, I think the growth can come from many other sectors. The software, a culture, you know, tourism, I mean all of that is totally yet to be exploited and I think that would be the way forward.

HASS: Great. Well, safe travels. Fly safe. Thank you for joining us. Thank you so much. Well, to be continued.

GARCÍA-HERRERO: Richard. Thank you. Bye.

HASS: Bye. Richard, over to you. How do you see the twin factors of Trump and slowing growth in China impacting Taiwan?

BUSH: First of all, China. I think the economic challenge from China is that China will move up the technological ladder and displace Taiwan in a number of areas where Taiwan has dominated. I think that the U.S. export controls on technology to China, particularly semiconductors and the tools for making them, that's helping Taiwan a lot, even though that may not have been the intention. But it remains a challenge that Taiwan's going to have to face. And so, maintaining your innovative capacity to always stay 4 or 5 steps ahead is important. I think that there is probably a lot of competition between PRC products and Taiwan products. And third markets, which is one we don't talk about and which I confess I've never studied, so I don't know the facts of it, but I think that's worth exploring. I think that with Donald Trump, there is going to be further reshoring of Taiwan companies in the mainland.

This is something that started before Trump ever appeared on the scene anyway. And but we I think we have to keep in mind something about Donald Trump's psychology. You know, he doesn't care if jobs shift from China to Taiwan. He wants jobs in the United States. And that's what's politically important to him. And so that's why TSMC and Arizona or Texas are important. We? Need to understand that Trump does not understand the macroeconomic causes of trade deficits and trade surpluses. If he did, he would not rely on tariffs to deal with these imbalances. His officials in the first term tried to explain this, but they didn't get through the. He also doesn't understand that a product that is labeled made in China may not have all of its value or most of its value added in China.

A lot of its value in the IT space is probably added in Taiwan. So, if you're increasing tariffs on so-called Chinese goods, you're hurting, you're hurting Taiwan, you're hurting ourselves. And I hope that the second Trump administration will be skillful in how it applies and implements technology transfer controls, because it's quite possible for Taiwan to get hit in the crossfire. And so, this will require a lot of consultation with the Taiwan government, with Taiwan companies. I think there's the will on the Taiwan side to accommodate where possible and certainly to explain why a scalpel may be better than a sledgehammer.

HASS: Well, speaking of that analogy, President Trump has identified a defense budget figure that he would like to see Taiwan invest in its national security. It's 10% of GDP. Is that a reasonable standard to push Taiwan to reach? If not, why not? And what would be a better approach for encouraging Taiwan to strengthen its capacity to defend itself? Shirley, maybe we can start with you and then give Richard an opportunity to weigh in.

LIN: Wolf Blitzer will be the expert to ask on this. I would say that, as Richard said, it depends on your definition. It's current 2.45% of GDP is already taking out 12 to 19% of Taiwan's annual budget. And the budget, as the TPP government has proposed, has already been pushed back by the legislature six times. We're not able to reach an agreement on a budget and I think it's very difficult to imagine raising that to 5% and 10%, which will eliminate the budget for all other needs, and that will just create a more divided Taiwan and a Taiwan that's less able to help the United States achieve its goals in the region. So, whether short term or long term is completely unattainable. So, the real question is what can Taiwan do to further his defense?

And as I said, the society is very divided. Part of it, the division also is, if you ask actually a huge number of the respondents also were very pessimistic after Trump was elected that this would be good for Taiwan. So, I think it's quite important to realize, of course, Taiwan is very susceptible to external pressure from Washington and from Beijing, and it's not very helpful to put out a number that is unattainable for a society that is trying to balance all of its priorities and also be a good partner. I think the fact that Taiwan actually is trying to do its best right now present a lie is actually in the Marshall Islands.

And I've just come back from doing actually a research report launch in Auckland for Pacific Islands. If you look at what actually Taiwan can do in the region is quite incredible in terms of its economic outreach. The resilience in Taiwan can extend to resilience in Asia Pacific. That would make the American alliance actually stronger. And I think that the defense includes actually indigenous technology. Of course, indigenous, you know, building submarines as well as increasing. We have already lengthened our conscription and will do a lot more and a lot of people are supportive of that. But in a measured way that is achievable. I love to hear what Richard says.

BUSH: I think that any number as a percentage of GDP like 10%, it's not only unattainable, it's unreasonable that it's mixing apples and oranges. And as I've suggested before, the there are two better figures. One is a percentage of the government budget. And it happens that back in the mine show, in the early time periods, the percentage of the government budget was 10 to 11%. It's now over 12 as a result of the results of the administration. And given the other demands on the budget, that's a good achievement. Even more useful in understanding Taiwan's defense commitment. Is what's the absolute value of what is spent? And if you look at the increase in the size of the actual budget in terms of new Taiwan dollars during the tri administration.

That figure increased by 54.8%. That is quite an interest increase in a short period of time. But there's a question in the background that must be answered. And we can't just look at numbers, whatever, however valuable those matters are. And that is what is the money spent on. You could spend a lot of money buying F-35s if Donald Trump would allow them to be sold. But most analysts believe that China's military power is such that Taiwan's military airfields would be knocked out in the first couple of hours of a fight, and the planes could never get off the ground. So what good is all that money that you spend on F-35s? So there needs to be a defense strategy that is commensurate to the threat from China.

And actually, the U.S. and Taiwan have been discussing this for quite a while. And Shirley's mentioned, some of the ways you can increase it, but increasing the size of the force, increasing training, getting more pilots for the planes that they do have. I think that. If we're talking about the money that gets spent on defense, the main obstacle is the low tax rates, the resources, total resources available to the government. And if security is something that talent, I want people value really value. Then perhaps they need to make a sacrifice in terms of what they give to the government for defense. Assuming that there is a defense strategy that makes sense not only to the United States, but also to the people of Taiwan.

LIN: I can add to that, Ryan, if I could. So, I think just three days ago, you know, another $387 million in arms sales to Taiwan was just basically approved by the United States. But this immediately created on the ground, if I could say, on the opposition fiercely attacking this proposal and saying that exactly as Richard says, what's in the budget. And on top of it, sure, we can spend all of this money. And when tension really rises and something conflict were to happen, well, does U.S. really come to Taiwan's aid? And the so proposing a 10% merely is just going to increase the tension within the society. And that will not actually be helpful to Taiwan's resilience or the United States long term strategy, which you pointed out in your most recent article, which I thought was excellent, that the U.S. needs to think about its long-term strategy and short-term strategy in order to advance its national interest.

HASS: Well, thank you. I guess a really valuable addition. You know, one thing I've learned from Richard over the years is that the only actor that benefits from a divided Taiwan is the mainland. And we should be wary of actions or policies that fracture cohesion inside Taiwan. I have a few questions from our global virtual audience that I would like to run by you in the remaining time that we have. The first is from Matt Kane, who is a bureau chief of the Burns Bureau, who asks about how universal tariffs are being proposed by President Trump on the entire world, including Taiwan, will impact Taiwan and its economic trajectory. Do either of you have a perspective on this question?

LIN: I'll answer brutally first, because a massive amount of work has already been done in the last few days on this everyone's and trying to project and I would say somewhat consensus by several economists is that the hit will really be shown in 2026. So even if all the worst scenario in terms of the tariffs on China were to hit. Of course, Taiwan is integral is going to be hit very hard. But the slowdown will not happen until 2026. But everyone is trying to figure out a way out of that. So, the plus one strategy in terms of moving out of China has already been accelerating. And I think they're planning starting this year. Well, this will redirect a lot of the investment and the trade.

HASS: Richard?

BUSH: Well, as I said, and I'd like to say hello to Matt, you know, if you have a product that's labeled made in China, even though the value has been mostly added in Taiwan and Cupertino, California, it. It. It's affected by the 60%. It may be that the Taiwan and U.S. companies involved in that product would absorb some of the tariff increase, but it might be that they pass it totally on to Americans. So, Americans would be hurt. It would probably contribute to inflation in the United States, and it would reduce the standard of living of average Americans.

HASS: The next question is from Lynn Dougal, who is a Board Director of Micron. Len asks, what are the industry diversification options available to Taiwan?

LIN: Thank you, Lynn, for that question. I think that Taiwan actually has been trying very hard, as have other countries in and East Asia, in looking at biotech software. And those investments have been made for many years. But the difficulty, of course, of having a very successful semiconductor industry is such that it has really drawn all the talent. We're talking about young, inexperienced engineers to the sector, and that leaves actually less space to develop new industries in the long term. But I think green transition is something that Taiwanese to invest more on just because it's not green transitioning as quickly and to focus on growth. And I think those are other opportunities.

But of course, Taiwan is really the lynchpin of this in that unlike France, for example, or Germany, Taiwan does not have many industries that rely on Chinese parts and in that way makes green transition actually quite difficult. So, I think the question is a good one, and this is one where I think that actually the TPP government has had good plans the last eight years. And of course, astoundingly it won a third term but did not does not control the legislature. So unfortunately, I think planning is planning and the National Development Council, of course, has very good plans to face the challenge of aging society changing talent pool. However, I think with a divided government, very few of these long-term investments can be made in the next 2 to 4 years into years. Taiwan has a mid-term election like the United States, but unfortunately, I think it's great to know what should happen. But it's another thing to say how to do it with the current situation.

BUSH: Just a couple of comments. I think it was back in the 1990s when people in Taiwan started talking about biotech. And I confess, I don't know how well biotech is doing in Taiwan, but there's this impulse to try and pick winners. People in Taiwan, smart people, have known for a long, long time that they really need to develop software to go along with the hardware in the IT sector.
But it there's been some progress, but it doesn't happen in the way that you would expect an innovative country like Taiwan. I think part of the problem is has to do with the Chinese language. And if you're going to do software, it's going to have the most appeal. The apps are going to have the most appeal in other Chinese language societies, which means China, which is no slouch when it comes to doing software itself. But I think that also government regulations are holding Taiwan back. It's really hard to do a startup in Taiwan because of it's so difficult to establish your business. And there are limits on venture capital and private equity and so on. And so, it's just easier to go into the hardware sector.

HASS: I'm going to sneak one final question in for a lightning round here between the two of you, which comes from Mike Fonti, who is a policy adviser to the Democratic Progressive Party Mission in Washington, D.C. He asks, how might Taiwan's government best deal with income inequality to strengthen economic resilience? Now, you both have touched upon this at various points over the course of the conversation, Richard. You've talked about the estate tax and the need for greater redistribution. But I just want to give you a chance, if there's anything additional that you would like to add to what Taiwan can do to better address income inequality.

LIN: I guess I would say with the limited time we have that I think Taiwan, unlike other places, even though we have very lot state duty, is a place where dreams can come true. And I myself experience it because of the educational opportunity. I think if there are more education opportunities for young people across all economic classes and rural and city that Devi would be able to be reversed. And I think that includes international opportunity. The Taiwanese in the last 30 years have all been moving towards China because of the economic opportunity. And it's time to rebalance that interest. As Richer says, learn English and reengage with the international community. And that would help with inequality as well. And the innovation issue that Richard is talking about on the policy front.

BUSH: Just to add to that, it's my impression that there was an evolution in the Taiwan educational system away from engineering and other specialties that supported Taiwan's economic growth, on the one hand, towards sort of more liberal arts. And that so that created a bit of a talent drought for those companies that needed people with technical skills. So even as Taiwan's tertiary education system downsizes, there needs to be a move back to what made Taiwan successful in the first place.

HASS: Well, we've come to the end of our time. I want to thank you both for a tremendous conversation. We started out with the goal of trying to identify Taiwan's economic resilience, its economic strengths, its potential risk points and the trajectory going forward. I think that you have done a tremendous public service in illuminating answers to those questions and providing useful and very practical advice to policymakers in both Taipei and Washington as well. So let me, on behalf of your global audience, thank you for your time, your contributions today. To be continued. Bye bye.