



**Mobility Patterns and Strategies
Among Taiwan's Small and Medium-Scale
Business People**

by

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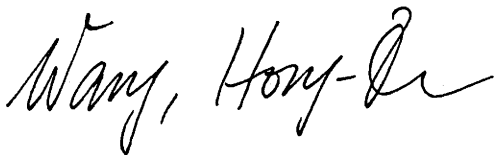
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Declaration

This dissertation was written while I was studying at the Contemporary China Centre at the Australian National University. The opinions expressed are my own, unless otherwise indicated.

A handwritten signature in black ink, reading "Wang, Hong-zen". The signature is written in a cursive style with a long, sweeping tail on the final character.

Wang, Hong-zen

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After undertaking PhD studies at the Australian National University, I am convinced that I made the right decision to come to Australia for post-graduate training. The research environment at Contemporary China Centre and ANU has been excellent, especially the intellectual milieu. Dr. Jonathan Unger's supervision pushed me to think hard about my research and writing. Through his discussion, I obtained a lot of insights into organising the whole thesis, and his comments supplied me with different views on how to improve my dissertation. Without his great help, I might not have persevered. It is a painful process to write a dissertation, and I am grateful to him for his supervision.

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I would like to dedicate the dissertation to my mother, who died on 19 August 1997. To see me finish the dissertation was one of her last wishes.

Hongzen Wang, Taipei, TAIWAN,
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ABSTRACT

This dissertation discusses the backgrounds, mobility strategies, and business practices of the small and medium-sized enterprise (SME) proprietors in Taiwan, set specifically in Taiwan's history of the past fifty years. A main focus is on how Taiwan's SMEs balance off profit-seeking behaviour and social norms in their business practices.

It is shown in Chapters One and Two that whereas a popular belief is that there exists a culturally-based drive among Taiwanese to become independent proprietors, the prevalence of SMEs in Taiwan is instead largely induced by structural factors. Differential educational opportunities have set limitations to upward mobility through credentials, especially among ethnic Taiwanese, and the first chapters show how and why, starting in the 1960s-70s, running one's own small business became the most significant mobility path of the less educated in Taiwan. The following four chapters (Three through Six) are devoted to discussions of the SMEs' internal management, including financial, marketing, human resources management, and the new overseas investment ventures. Throughout, attention is directed toward the special interpersonal dilemmas faced by family firms, the predominant form of SME in Taiwan.

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Introduction

Paradox reveals the truth
--Friedrich Duerrenmatt¹

This study is focused on the owners of small and medium-sized enterprises in Taiwan, upon their social origins after the second world war, and their strategies to be upwardly mobile through the establishment of independent businesses. The author seeks to de-mythologise some popular opinions about these people, and tries to expound the basic problems from the perspective of two contradictory forces-- social and market forces.

1. Literature Review

Most scholarly writing tends to put Taiwan in either a Chinese or East Asian context. Two different discourses are expressed in the disciplines of anthropology/sociology and economics/political economy. Most of the research on small and medium-sized enterprises (SMEs) in Taiwan is undertaken by the first pair of disciplines within the context of Chinese studies and by the second pair in line with an East Asian developmental model.

1.1. Anthropological and Sociological Works on Taiwanese Development

Those anthropologists and sociologists who perceive Taiwan as a frontier of Chinese culture² tend to emphasise the unique characteristics of Chinese entrepreneurs, so their works mainly focus upon the traditional factors which propelled the dynamic development of Chinese business. Their main concerns involve three topics: Firstly, why do Chinese like to be proprietors? Secondly, why does the Chinese firm tend to be small? Lastly, how does the Chinese culture of *guanxi* influence Chinese economic behaviour, which in turn includes two questions: a) why is the family firm so common in Chinese society, and b) how do

¹ Im Paradox erscheint die Wirklichkeit. See Friedrich Duerrenmatt, *Die Physiker (The Physicists)* (Zuerich: Verlage der Arche, 1962), p.79.

they utilise *guanxi* to run their businesses?

1.1.1 Why do the Chinese like to be their own bosses?

The bulk of research shows that Chinese seek to be proprietors,³ and the most common explanation has been a ‘Chinese mentality’. Chen Jiexuan (陳介玄) wrote that diligence as a world view (Weltanschauung) would highly value those who worked hard to strive to become a boss: ‘Without moral support from this ideology, those who tried to be upwardly mobile would not have access to social prestige, and their pursuit of profit would lack legitimacy’.⁴ Wong Siu-lun found that the desire to be autonomous is the drive to be one’s own boss.⁵

Though the cultural explanation sometimes talks about history, its history is static and unchanged. The authors seem to believe that social institutions never influence culture, or at most just play a minor role. For example, when he compared Hong Kong and Singapore business communities, Wong Siu-lun said that if all Singaporean institutions were the same as those of Hong Kong, the drive to be businesspeople would be the same in Singapore. This is an argument which will never be proved, like the claim from neo-classical economics that if there were no government intervention in the market, we would be better off than what we have at the moment. From another way to read his empirical findings, it exactly shows that different social institutions will influence the possibility of social mobility.⁶ One obvious defect of these explanations is that they fail to

²Murray and Hong sharply criticise the claim that the essence of Taiwanese culture is Chinese culture. See Stephen O. Murray and Keelung Hong, *Taiwanese Culture, Taiwanese Society: A Critical Review of Social Science Research Done on Taiwan* (Lanham: University Press of America, 1994).

³ See Victor Mok, ‘Small Factories in Kwun Tong: Problems and Strategies for Development’, in King Ambrose Y. C. and Rance P. L. Lee (eds.), *Social Life and Development in Hong Kong* (Hong Kong: The Chinese University Press, 1981), pp.81-104. Wong, Thomas W. P., ‘Inequality, Stratification and Mobility’, in Lau, Siu-kai, Lee, Ming-kwan, Wan, Po-san and Wong, Siu-lun (eds.), *Indicators of Social Development: Hong Kong 1988*, (Hong Kong: Hong Kong Institute of Asia-Pacific Studies, The Chinese University of Hong Kong, 1991). Other works, see notes below.

⁴See Chen, Jiexuan (陳介玄), *Xieli Wangluo yu Renji Wangluo—Taiwan Zhongxiao Qiye De Shehui Jingji Fenxi* (協力網絡與生活網絡--台灣中小企業的社會經濟分析, *Subcontracting and Personal Networks—social economic analysis of Taiwan’s small and medium-scale enterprises*) (Taipei: Lianjing Chubanshe, 1994), p.292.

⁵ See Wong, Siu-lun, ‘Business networks, cultural values and the state in Hong Kong and Singapore’, in Rajeswary Ampalavanar Brown (ed.), *Chinese Business Enterprise in Asia*, (London, New York: Routledge, 1995), pp.136-153.

⁶ See Wong, Siu-lun, 1995, *op. cit.*, pp. 145-146.

explain why certain groups are more likely to run their own businesses than others, e.g., Taiwanese (本省人) versus Mainlanders (外省人) in Taiwan. However, Susan Greenhalgh's research on Taiwanese urban society found that 'being Taiwanese' means drawing on family, community and religious ties to climb through small-scale business and then larger-scale entrepreneurship into the commercial and industrial elite. "Being Mainlander" means eschewing ties of kinship and community, and using contacts with people in the bureaucracy and a higher education to obtain a white-collar job in government, and hence a secure position in the bureaucratic elite'.⁷ Marshall Johnson argued that the Taiwanese held a comparative advantage in the small business world where networks, familiarity and trust are required.⁸ Their research shows that there is a different probability of Taiwanese and Mainlanders running a business, even though they hold the same 'Chinese cultural background'.

I will try to elaborate the reasons which underpin this difference. The factors that these authors suggest are not altogether convincing. If Taiwanese can use familial, communal ties to find a way in the business world, one cannot see any reason why the Mainlanders cannot do so, especially when they held relatively good opportunities to control the economy in the 1950s, and the public sector until the 1980s. For example, it would be easier for the Mainlanders to conduct business with the public enterprises than Taiwanese, if networks, familiarity and trust are required, as Marshall Johnson claimed. He and other authors hold to their claims because they did not analyse the initial conditions of the two groups in Taiwan in the 1950s, and the structural factors like family status or educational policies, which would largely determine one's subsequent mobility paths. I will explore these in Chapters One and Two.

Other authors look for structural factors to explain why Chinese strive to be proprietors. Donald DeGlopper found in a study in Lukang (鹿港) that almost all proprietors were working as craftsmen before they set up their own business. He

⁷See Susan Greenhalgh, 'Networks and Their Nodes: Urban Society on Taiwan', *China Quarterly*, no.99 (September 1984), pp. 529-552.

also found that those who desire to be 'independent' or 'mobile' were those who had been hired in small factories where employment was unstable.⁹ Another more comprehensive study done by Shieh Gwo-shyong (Xie Guoxiong, 謝國雄) found three factors affecting the likelihood of a blue-collar worker becoming a boss: the features of dependent capitalism, the specific labour regime in Taiwan, and a worker's age and marriage status.¹⁰ Though DeGlopper and Xie have noted the mobility paths of labourers, both of their studies are subject to criticism for not differentiating Taiwanese from Mainlander.

1.1.2. Why does the Chinese firm tend to be small?

There are three ways to explain the phenomenon: i.e., the traditional custom of family partition, state control, and the consequences of a particular path to economic development. Chinese family partition is most often cited as an explanatory factor. Equal partition of family property to each son makes it difficult for a family firm to grow large after the first generation.¹¹ Wong Siu-lun presents a more elaborated family firm life cycle.¹² He has argued that in different stages there are different possibilities to divide the family firm. The members of the third generation of the family are more likely to divide the family firm than the second generation. His model is similar to Shinichi Horie's (堀江俊一), who modeled the Chinese family partition into four stages: only communal property and familial ideology could bind the family (*jia*) together after the extended family

⁸ See Marshall Johnson, 'Classification, Power, and Markets: Waning of the Ethnic Division of Labour', in Denis Fred Simon and Michael Y. M. Kau (eds.), *Taiwan: Beyond the Economic Miracle* (Armonk, M. E. Sharpe, Inc, 1992), p.81.

⁹ See Donald DeGlopper, 'Artisan Work and Life in Taiwan', *Modern China*, vol. 5, no. 3 (July 1979), p. 304.

¹⁰ See Xie, Guoxiong (謝國雄), 'Heishou bian toujia--Taiwan zhizaoye zhong de jieji liudong (黑手變頭家--台灣製造業中的階級流動, Black-hands Becoming Their Own Bosses: Class Mobility in Taiwan's Manufacturing Sectors)', *Taiwan Shehui Yanjiu Jikan* (台灣社會研究季刊, *Taiwan: A Radical Quarterly in Social Studies*), vol. 2, no.2 (summer 1989), pp. 11-54.

¹¹ See Gary G. Hamilton and Nicole Woolsey Biggart, 'Market, Culture, and Authority: A Comparative Analysis of Management and Organisation in the Far East', *American Journal of Sociology*, vol. 94 (1988) (Supplement), pp. 52-94.

¹² See Wong, Siu-lun, 'The Chinese Family Firm: A Model', *The British Journal of Sociology*, vol. 36, no.1 (1985), pp. 58-72.

stage (II).¹³

Though they have noticed how traditional factors can affect organisational behaviour in the family firm, they ignore the other forces that intervene into traditional customs. For example, the control of important production materials by the state inhibited companies that would have liked to step into industries like petrochemical, communication or electric power that are large-scale and capital intensive.

Some other scholars would attribute the prevalent phenomenon of small and medium-scale enterprises to state control, like Hill Gates. She uses the term 'petty capitalism' to describe the general phenomenon of small business which has existed since the Song dynasty.¹⁴ The state policy to restrict family wealth confined such entrepreneurial activity to the construction of lineages which in turn created the social milieu for the prosperity of SMEs. In Taiwan, the Kuomintang state tried to create an 'unspoken alliance' with these petty bourgeoisie, the result being that the state left small business alone without interference.¹⁵ Susan Greenhalgh and Alice Amsden both have a different viewpoint, believing the state's control of credit, industrial raw materials and licenses hampered the growth of small enterprises.¹⁶ A Taiwanese scholar, Wang Zuorong (王作榮), believes that the government's fear of big business is the reason why there is little big business in Taiwan.¹⁷

These scholars have emphasised the importance of political force in shaping Taiwan's industrial structures, but this is still not an adequate account, for small firms exist everywhere, in the industrialised countries and in the less developed

¹³ See Horie Shunichi, 'Taiwan Kanzoku no Kazoku-jia ideorogi to jia shyutan' (Family of Taiwan Chinese: *jia*-ideology and *jia*-group), *Minzokugaku Kenkyu (Research on Ethnology)*, vol. 46, no.3 (1981), pp.311-313.

¹⁴ See Hill Gates, 'Small Fortunes: Class and Society in Taiwan', p. 178, in Denis Fred Simon and Michael Y. M. Kau (eds.), *Taiwan: Beyond the Economic Miracle* (Armonk, M. E. Sharpe, Inc, 1992), pp. 169-185.

¹⁵ *Ibid.*: p.178.

¹⁶ See Susan Greenhalgh, 'De-Orientalizing the Chinese Family Firm', *American Ethnologist*, vol. 21, no. 4 (1994), pp.766-767; Alice Amsden, 'Big Business and Urban Congestion in Taiwan: the Origins of Small Enterprise and Regionally Decentralized Industry', *World Development*, vol. 19, no.9, (September 1991), pp.1122, 1126.

¹⁷ See Wang, Zuorong, *Wang Zuorong Kan Taiwan Jingji (王作榮看台灣經濟, My Viewpoint on Taiwan is Economy)* (Taipei: Shibao Wenhua Chubanshe, 1988).

third world. For example, 96.9% of Australian enterprises were small businesses, which employed fewer than one hundred workers in the manufacturing sector and fewer than twenty in the service sector in 1993-94.¹⁸ In Japan, 99.4% were small and medium-sized enterprises in the non-agricultural sector, hiring fewer than three hundred employees in the manufacturing sector, fewer than one hundred in wholesale, and fewer than fifty in the service sector in 1981.¹⁹ In short, small and medium-scale enterprises exist everywhere, and are not unique to Chinese industrial organisation.

In contrast to these arguments, Donald DeGlopper has written that the prevalence of SMEs is the consequence of economic development rather than an historical remnant.²⁰ This explanation is consistent with the fact that in 1994 there were 55,700 newly set up companies,²¹ and these newly set-up firms had nothing to do with family partition. But on the other hand, we should not deny that this traditional custom influenced the closures of family firms. In Chapter Five, I will discuss the forces that inhibit a family firm from growing large.

1.1.3. How does *guanxi* influence Chinese economic behaviour?

As to this problematic, it would be very tempting to use ‘Chinese family’ as the basic unit to analyse ‘Chinese economic behaviour’, for in the Chinese studies of anthropology or sociology, the Chinese family system is a core discourse.²² Following this academic tradition, the modern economic unit, which is individual in Western economic analysis, is transformed into family (*jia*, 家), and family enterprise becomes equivalent to firm.

¹⁸ See Department of Foreign Affairs and Trade, *Winning Enterprises--How Australia's Small and Medium Enterprises Compete in Global Markets* (Canberra: Australian Government Publishing Service, 1995), p.8.

¹⁹ See Arita Tatsuwa (有田辰男), *Chusho Kigyo Montai no Kiso Riron* (中小企業問題の基礎理論, *The Basic Theory of the Problems of Small and Medium-Scale Enterprises*) (Tokyo: Nihon Hyoronsha, 1982), p.5, Table1.

²⁰ See DeGlopper, Donald R, *op. cit.*, p. 286.

²¹ See Small and Medium Enterprise Agency, the Ministry of Economic Affairs (經濟部中小企業處), *Zhonghuaminguo 84 Nian Zhongxiao Qiye Baipishu* (中華民國八十四年中小企業白皮書, *White Paper on Small and Medium Enterprises*) (Taipei: MOEA, 1996), p.64.

²² About the works on Chinese family and kinship, see Burton Pasternak's review on the topic. See Pasternak, Burton, "Economics and Ecology," in Emily Martin Ahern and Hill Gates (eds.), *The Anthropology of Taiwanese Society* (Stanford: Stanford University Press, 1981), pp.151-183.

For example, in the Australian government's research on Chinese business in Asia, it stresses that the economic unit is not the individual but the extended household.²³ This kind of definition will not be able to explain those companies which are owned by family members but run by 'outsiders'. To resolve this problem, Gary G. Hamilton and Kao Cheng-Shu claim that the features of the family firm in Taiwan are diversification, duplication of hierarchies, personal relations and personal networks and the importance of an inner circle. They understand the family firm in terms of trust-bearing personal relationships.²⁴ To define what a family enterprise entails, Chen Jiexuan uses the term 'quasi-familial solidarity', which means that a group of people, based on common interests, work together.²⁵ Their explanations simply turn the family enterprise into a business administration. Following their definition, one is not able to distinguish a family firm from a non-family firm, e.g., what is the difference between a partnership and a family enterprise. Wong Siu-lun's explanation of 'familism', which focuses on ownership but not on the linkage in transactions, is more useful in clarifying what a family firm is.²⁶

Scholars like to incorporate *guanxi* and *xinyong* (trustworthiness, 信用) in their analysis. Wong Siu-lun observes that family members have 'familial solidarity', which constitutes the core of a Chinese family enterprise. Because they are able to pull the outside world into the networks, the family firms work well.²⁷ In another paper, he argues that personal and particularistic business trust in late traditional China, including overseas Chinese communities, developed into a more systemic and universalistic trust which co-exists with traditional trust, providing a congenial environment for entrepreneurship to grow. In other words, he thinks personal trust/relationships are still very important in the modern Chinese world and he notes that systemic trust and personal trust are mutually

²³ See Department of Foreign Affairs and Trade, *Overseas Chinese Business Networks in Asia* (Canberra: Australian Government Publishing Service, 1995), p.126.

²⁴ See Gary G Hamilton and Kao Cheng-Shu, 'The Institutional Foundations of Chinese Business: The Family firm in Taiwan', *Comparative Social Research*, vol. 12 (1990), pp. 135-151.

²⁵ See Chen, Jiexuan, *op. cit.*, pp. 59-67.

²⁶ See Wong, Siu-lun, 1995, *op. cit.*, pp. 139-40.

²⁷ *Ibid.*: p. 139.

reinforcing.²⁸ Thomas Menkhoff's study argues that trust (*xinyong*) is the 'lubricant' of Chinese international trade and that kinship networks are also networks of trust.²⁹ Kao Cheng-Shu similarly writes that Taiwan's business organisational behaviour is shaped by the traditional factor of 'personal trust' which is not arbitrary but instrumental-rational.³⁰ Susan Greenhalgh observes that 'among the Chinese on Taiwan, *as among the Chinese generally*, there is a strong preference for economic relationships based on prior acquaintance and trust'.³¹ In another work, she has similar viewpoints to Hamilton and Kao: that duplication of posts in family enterprises, packages of individual incentives and group risk insurance, networks, and diversification strategies make family firms competitive in the market.³²

These authors all emphasise the importance and positive effects of traditional factors. *Guanxi* or *xinyong* in their explanation of business development serve as a repertoire that people who live within this cultural context can hold access to indefinitely. Though Susan Greenhalgh talks about the negative consequences of utilising familism as the basic trust network, i.e., it produces an atomistic, competitive society,³³ and a lack of market research, lack of scale of economy,³⁴ she did not write anything about this dark side of a 'network trust' until recently.³⁵

But as Ambrose Yeo-chi King writes, this is only a partial picture of the

²⁸See Wong Siu-lun, 'Chinese Entrepreneurs and Business Trust', in Gary G. Hamilton (ed.), *Business Networks and Economic Development in East and Southeast Asia* (Centre of Asian Studies, University of Hong Kong, 1991), p. 15.

²⁹See Thomas Menkhoff, *Trade Routes, Trust and Trading Networks: Chinese Family-Based Trading Firms in Singapore and Their External Economic Dealings*, unpublished Ph.D dissertation (1990), Faculty of Sociology, University of Bielefeld.

³⁰See Kao, Cheng-Shu, 'Personal Trust in Taiwan Business', in Gary G. Hamilton (ed.), *op. cit.*, pp. 66-76.

³¹See Susan Greenhalgh, 1984, *op. cit.*, p. 535. *Italics* author adds.

³² See Susan Greenhalgh, 'Families and Networks in Taiwan's Economic Development', in Edwin A. Winckler and Susan Greenhalgh (eds.), *Contending Approaches to the Political Economy of Taiwan* (Armonk: M.E. Sharpe, 1988), pp.231-236.

³³ See Susan Greenhalgh, 1984, *op. cit.*, p. 535.

³⁴ See Susan Greenhalgh, 1988, *op. cit.*, p. 236.

³⁵ See Susan Greenhalgh, 1994, *op. cit.*

Chinese cultural dynamic of network building.³⁶ The problem of these studies is that they treat the family firm as a coherent unit like an individual, so they cannot see any conflict and power relationships within the firms and between the family members. Some scholars have noted this kind of conflict, as in the works of Maurice Freedman³⁷ or Margery Wolf,³⁸ or recently Susan Greenhalgh.³⁹ The economic conflict either between brothers or between *fang* (households, 房) is not unusual. It becomes necessary to study the dynamic development of *xinyong* or *guanxi*, and the nature of conflict within and between family enterprises, as I shall do in the thesis.

Some other studies show a different image. Donald DeGlopper finds that cooperation and help in Lukang's businesses are not like the axiomatic obligations found among brothers. Such cooperation depends on pre-existing personal relations of *ganqing* (affection, 感情).⁴⁰ In her study of the tanning industry in a community of Hakka Chinese in Calcutta, India, Ellen Oxfeld does not idealise the Chinese traditional relationships (*ganqing* or *guanxi*), but instead finds that a cultural ethos that has been carried from the country of origin and perpetuated in the overseas environment expresses a whole range of human relationships that have long been encompassed by monetary transactions in the Chinese context: 'it should not be surprising to find *such transactions serving as a focal point in Mr. Zhou's description and assessment of family relationships*'.⁴¹ Another case is the Bangkok Metropolitan Bank controlled by the Tejaphaibul family, where 'the second generation became embroiled in family conflicts which led to one part of the family in control of the Bank severing the short-term credit lines to another

³⁶See Ambrose Yeo-chi King, 'Kuan-hsi and Network Building: A Sociological Interpretation', *DAEDALUS, Journal of the American Academy of Arts and Science*, vol. 120, no.2 (Spring 1991), pp. 63-84.

³⁷ See Maurice Freedman, *Lineage Organization in Southeastern China* (London: Athlone Press, 1958).

³⁸ See Margery Wolf, *Women and the Family in Rural Taiwan* (Stanford: Stanford University Press, 1972).

³⁹ See Susan Greenhalgh, 1994, *op. cit.*

⁴⁰See Donald R DeGlopper, 'Doing Business in Lukang', in W. E. Willmott (ed.), *Economic Organization in Chinese Society* (Stanford: Stanford University Press, 1972), pp. 297-326.

⁴¹See Ellen Oxfeld, 'Individualism, Holism, and the Market Mentality: Notes on the Recollections of a Chinese Entrepreneur', *Cultural Anthropology*, vol. 7, no.3 (1992), pp. 267-300. I have added the *Italics*. Mr. Zhou is the interviewee in the article.

part in control of the family's Kloster Beer interests'.⁴² Susan Greenhalgh has found that power dominance, especially gender dominance, exists within the family firm.⁴³

Besides the conflicts *within* the family firm, *guanxi between* the firms is also not as effective as some scholars have described. Hamilton and Kao wrote that such networks are very important when conducting business with other companies. When one has broader networks, one is more powerful. The relationships tend to be stable over the long term, and are based on reciprocal trust, loyalty and predictability.⁴⁴ Eugene Cooper observed that 'while the factors of price, quality and demonstrated reliability are important in the conduct of business in Hong Kong's free market, ascribed and affective bonds between businesspeople are perhaps more important than might be expected'.⁴⁵ Wong Siu-lun argued that business trust is the essence of personal ties, and that universalistic trust is also established step by step, creating a congenial environment for entrepreneurship to grow.⁴⁶ This kind of image is totally different from the competitive business world that neo-classical economics paints. So, too, Donald DeGlopper's research among Lukang businesspeople shows that business is business, and *guanxi* does not help. He found that one can do business with anyone, of any background, though not with a total stranger.⁴⁷ Victor Mok wrote that Hong Kong is a strong bastion of rugged individualism: an overwhelming proportion of the small enterprises in his study were interested neither in taking partners nor in being absorbed. Cut-throat

⁴² See Department of Foreign Affairs and Trade, 1995b, *op. cit.*, p. 138.

⁴³ See Susan Greenhalgh, 1994, *op. cit.*, p. 754.

⁴⁴ See Gary G Hamilton and Kao, Cheng-shu, *op. cit.*, pp. 145-146.

⁴⁵ See Eugene Cooper, *The Wood-Carvers of Hong Kong* (Cambridge: Cambridge University Press, 1980), pp.97-98.

⁴⁶ See Wong, Siu-lun, 1991, *op. cit.*, p. 15. Their observations derive from their interview data, but it could be that an informant tells an interviewer socially approved things, and conflicts between themselves and other people get skipped in their discourse. In my interviews, most informants mentioned the importance of *guanxi* and *xinyong*, but when I touched the sensitive topic like the conflicts between partnership, they did not like to talk a lot about that, especially those informants who are not very good friends of my friends who introduced me to interview them.

⁴⁷ See Donald DeGlopper, *Lukang—Commerce and Community in a Chinese City* (New York: State University of New York Press, 1995), p.205.

price competition is necessary to survive.⁴⁸

Based on my own research, I would argue that there is always a tension between private interests and social relationships. The pursuit of private interests is based on capitalist market calculation, which is imperative for every enterprise in the market, or they will be cast out in the competition. On the other hand, social relationships are non-contractual relations, which means that the relationships between kinship, neighbours, associations and religious belief are not based on the 'freedom of contract' and self-interested calculations, that liberal economists tout.⁴⁹ This kind of tension runs through different spheres of social life, as in personnel management in the family firms, in their business networks, in their financial control, *etc.* Since this tension exists everywhere, how to resolve this tension will become one of my main concerns.

Another commonly discussed topic involves the industrial relations of enterprises. Though all writers on the topic agree that most people use *guanxi* to find their job, the interpretations of industrial relations are very different: one writer claims that the personnel management is *paternalistic*, but another says that the relationship between the workers and boss is only superficial. Gordon Redding claimed that the Chinese management pattern generally is paternal.⁵⁰ Janet Salaff's comparison of family and non-family enterprises showed that this paternal management only exists in the family firm.⁵¹ Ambrose Yeo-chi King found that Chinese like to hire kinsmen on the grounds that they are reliable, competent and responsible.⁵² Xie Guoxiong found that firms hire people with

⁴⁸ See Victor Mok, 'Small Factories in Kwun Tong: Problems and Strategies for Development', in King, Ambrose Y. C. and Rance P. L. Lee (eds.), *Social Life and Development in Hong Kong*. (Hong Kong: The Chinese University Press, 1981), p.87, 89.

⁴⁹ The concept is derived from Karl Polanyi, *The Great Transformation--Origins of Our Time*. (Chinese, *Jubian: Dangdai Zhengzhi, Jingji de Qiyuan*, 鉅變：當代政治經濟的起源, tr. by Huang Shumin, Sh, Jiayin and Liao Wensheng, 黃樹民, 石佳音, 廖文生) (Taipei: Yuanliu Chubanshe, 1989).

⁵⁰ See Gordon S. Redding, *The Spirit of Chinese Capitalism* (Berlin: Walter de Gruyter, 1990), p.215.

⁵¹ See Janet W. Salaff, 'The Chinese Connection: Management Control Structures and the Search for Labour in Taiwan: Small Firms', in E. K. Y. Chen, Jack F. Williams and Joseph Wong (eds.), *Taiwan: Economy, Society and History*. (Hong Kong: Centre of Asian Studies, University of Hong Kong, 1991), p.199.

⁵² See Ambrose Y.C. King, and Peter J. L. Man, 'Small Factory in Economic Development: the Case of Hong Kong', in Tzong-biau Lin, Rance P. L. Lee and Udo-Ernst Simonis (eds.), *Hong Kong--Economic, Social and Political Studies in Development*. (New York: M.E. Sharpe, 1979), p.53.

whom they have *guanxi*, mainly family members or workers whom the boss was acquainted with in the factory in which he used to work.⁵³ Susan Greenhalgh also found that employment is mainly through personal networks.⁵⁴

On the other hand, Richard W. Stites found that 'workers are aware that surface friendliness with the owner is just that'.⁵⁵ Donald DeGlopper observed that the employer is not paternalistic, nor the employee dependent, and both sides like this kind of relationship.⁵⁶ If the worker is hired through personal networks, how come the relationships with the owner are on the surface only? But from the viewpoint of an employer, it is not hard to understand the contradictory findings, for the boss has to take care of social ties, and on the other hand has to calculate his own market interests, so how social ties and social distance can be maintained at the same time becomes important.

Another important research field involves the financial systems within Chinese society. Justin D. Niehoff's study of one village in Taizhong found all but one of the household factories there were financed by family savings, derived from the owners' and younger unmarried members of those households, especially the unmarried daughters.⁵⁷ Bernard Gallin and Rita S. Gallin argued that the modified joint families provided their members with the necessary economic base and security to begin new entrepreneurial activities.⁵⁸ This finding contradicts Wong Siu-lun's study in Hongkong, where he found the most general form in setting up a new enterprise was to cooperate with non-common descent, non-lineage members to raise the initial capital.⁵⁹ Xie Guoxiong's finding is congruent with Wong's. He found that most of the initial capital could be raised from one of the following two types of partnership: partnership with a trade company, or partnership with the workers or owner of the putting-out company.⁶⁰ All agree

⁵³See Xie, Guoxiong (謝國雄), *op. cit.*, 1989, pp. 38-39.

⁵⁴See Susan Greenhalgh, *op. cit.*, 1984, p. 535.

⁵⁵See Richard W. Stites, *op. cit.*, 1985, p. 236.

⁵⁶See Donald DeGlopper, 1979, *op. cit.*, p. 299.

⁵⁷See Justin D. Niehoff, 'The Villager as Industrialist: Ideologies of Household Manufacturing in Rural Taiwan', *Modern China*, vol. 13, no.3 (July 1987), pp. 278-309.

⁵⁸See Bernard Gallin and Rita S. Gallin, 'Socioeconomic Life in Rural Taiwan', *Modern China*, vol. 8, no.2 (April 1982), pp. 205-246.

⁵⁹See Wong, Siu-lun, 1985, *op. cit.*.

⁶⁰See Xie, Guoxiong, *op. cit.*, p. 38.

that it is very hard to borrow funds from the banking system, and quite often one has to resort to the informal financial sector to secure money.

But to raise initial capital and to get a loan for working capital are two different things. Few works discuss the latter topic. Some like to infer from the difficulty to raise initial capital to the situation of getting working capital. For example, Zhou Tiancheng (周添城) and Chen Jiexuan found that small and medium-scale enterprises in Taiwan are not able to get financial support from the regulated banking system.⁶¹ But in his research in Hong Kong, Victor Mok found that Hong Kong businesspeople did not lack working capital.⁶² If so, why do the small and medium-sized enterprises always complain about capital shortages? I will discuss this puzzle in Chapter Three.

Business practices involve self-interested calculation, and at the same time businesspeople have to be careful not to infringe any of the core social rules expected by society. But the contradictions between the roles assigned to them--to be a greedy capitalist, or to be a popular philanthropist--is not easy to handle. Some scholars have touched upon this problem. For example, Ambrose Yeo-chi King notes that there are cultural mechanisms to neutralise or to freeze the practice of *renqing* (human relationships, 人情) or *guanxi* in order to carve out room for instrumental rationality, which is necessary to maintain economic and bureaucratic life (in the Weberian sense).⁶³ But he does not tell us what sorts of mechanisms these are in the business world. Hwang Kwang-kuo (黃光國) argues that there are four ways to evade unwanted *renqing*, which include a) internalising the modern attitude of individualism, b) setting up and enforcing clear-cut rules of social interaction, c) leaving the interpersonal network of mixed ties, and d) psychological compartmentalisation,⁶⁴ but all he discusses are the individual

⁶¹ See Zhou, Tiancheng (周添城), 'Quanli Bianchui de Zhongxiao Qiye' (權力邊陲的中小企業, Small and Medium-Sized Enterprises and Power Periphery), in Taiwan Yanjiu Jijinhui (台灣研究基金會), *Longduan yu Boxue--Weiquan Zhuyi de Zhengzhi Jingji Fenxi* (壟斷與剝削--威權主義的政治經濟分析, *Monopoly and Exploitation--Political Economy Approach to Authoritarianism*) (Taipei: Taiwan Yanjiu Jijinhui, 1989), pp.111-112. Chen Jiexuan, 1994, *op. cit.*, p. 108.

⁶² See Victor Mok, 1981, *op. cit.*, p. 94.

⁶³ See Ambrose Yeo-chi King, *op. cit.*, p. 76.

⁶⁴ See Hwang, Kwang-Kuo, 'Face and Favour: The Chinese Power Game', *American Journal of Sociology*, vol. 92, no.4 (1987), pp. 963-967.

psychological mechanisms. If so, it seems that there is no social mechanism to solve the *renqing* dilemma, which is a social instead of psychological phenomenon. Besides, Hwang's explanation is *a*-historical, and he ignores that this kind of contradiction only exists in certain social formations, and that the way to resolve it also depends on the specific social context. I will argue that the self-regulating market in Taiwan's authoritarian political structure has a strong influence on business practices, which inserts tensions into one's social relationships. I will also investigate the social mechanisms, e.g., the rotating credit club, family division, a high turnover rate of workers, etc, that are utilised to reduce the tension.

1.2. Economic and Political Economy Writings on Taiwan's Development

After a period of long-term neglect toward research on East Asian development, Western scholars trained in economics and political economy in the 1980s suddenly awoke to dramatic economic achievements in the region which puzzled them. Like the sociologists and anthropologists, they tried to unveil common factors underlying the region's development.

There are three ways to talk about Taiwanese development in the East Asian context: in terms of Cultural Confucianism (CC), Strong States (SS) and a Magic Market (MM).

1.2.1 Cultural Confucianism

Following Weber's discussion of the Protestant ethic, some scholars have tried to discover a 'selective affinity' between the Confucian ethic and entrepreneurial spirit in East Asia which might contribute to its outstanding economic performance in the past few decades. Tu Wei-Ming (杜維明), for example, has argued that 'the particular kind of modern [East Asian] capitalism emphasises the self, a transformative force, as a centre of relationships, duty consciousness, personal cultivation, consensus formation and cooperation,...[a] high premium on education and ritual, the fiduciary community and government

leadership' which could be summarised as 'Confucian ethic'.⁶⁵ Such an ethic encourages, in a secularised world, a willingness to devote oneself to pursuing interests that are rendered morally legitimate.⁶⁶ The East Asian entrepreneurial spirit flourishes under such a drive.

Subject to many critiques that there is no concrete connection that can be shown to exist between the Confucian ethic and the East Asian entrepreneurial spirit, Tu has replied that 'indeed there is no causal relationship'.⁶⁷ If so, how do we know that the use of this explanation of 'Confucian ethic' is not instead simply the result of long-term economic development? In other words, cause and effect are ambiguous in his explanation.

Another critique of the cultural Confucian explanation focuses on its failure to explain the economic results in China, North Korea and Vietnam, whose claim to a Confucian cultural heritage is no less than the Japanese claim.⁶⁸ One way to respond to this critique is to explain East Asian development in terms of 'political culture'. Roy Hofheinz, Jr. and Kent E. Calder, in their book *The Eastasia Edge*, attribute the economic success of the capitalist states of East Asia to political flexibility and predictability, which are based on a high degree of respect for hierarchy and for order from top to bottom.⁶⁹ Such a close cooperation between the government and people gives government 'a central rudder...to undertake long-term policies', which in turn promotes economic development in an uncertain world. This kind of 'oriental' discourse also could be found in the reports of the Hong Kong colonial government when these describe the Hong Kong business community. In a report of the Hong Kong Government in 1966, 'the traditional Chinese view of the ideal relationship between government and people...is analogous to that which should exist between parents and children or

⁶⁵ See Tu, Wei-Ming, *Confucian Ethics Today—The Singapore Challenge*, (Singapore: Curriculum Department Institute of Singapore, Federal Publications, 1984), p. 84.

⁶⁶ *Ibid.*, pp. 75-76.

⁶⁷ *Ibid.*, p. 88. Here what Tu means is the so-called 'mechanic causality' which is distinguished from what Louis Althusser calls 'structural causality' or 'expressive causality'. See Louis Althusser, *Reading Capital*, 1970, Verso Edition.

⁶⁸ See Ruth McVey, 'The Materialisation of the Southeast Asian Entrepreneur', in Ruth McVey (ed.), *Southeast Asian Capitalists* (New York, Ithaca: Cornell University, 1992), p. 11.

⁶⁹ See Roy Jr. Hofheinz and Kent E. Calder, *The Eastasia Edge*, (New York: Basic Books, Inc., 1982), p.249.

between a shepherd and his flock'.⁷⁰ Similarly Zhang Jiaming (張家銘) used the term 'paternalistic leadership and management' to describe the relationship between the government and business community in Taiwan. This kind of relationship is based on a cultural conviction of 'trust and loyalty'.⁷¹

One problem with this kind of explanation is that the types of political regimes are so diverse that we cannot find the same relationships between the state and civil society across all the countries. For example, Hong Kong is basically a *laissez faire* state where no specific industrial policy is pursued by the government, while in Singapore the government forward-plans almost everything. How come these two totally different states have both succeeded economically?

Even when the government works closely with businesspeople, this does not tell us what the types of cooperation are. Does the authoritarian state command and the businesspeople follow, as in Singapore and Korea? Or do the businesspeople just mind their own business and never care what the policies are, as in Taiwan or Hong Kong?⁷² Or what of the strong power of the *Keidanren* (經團連, Association of Business Federations) to influence Japanese industrial policy? Flattening different political situations to a one-dimensional level cannot alert us to the important differences existing between the different locales. Throughout the thesis, I will focus on this problem of how the government and business community in Taiwan interact.

Another difficulty arising from this approach is that it fails to explain the different industrial structures in different countries. Why do Taiwan's small and medium-sized enterprises specialise in exports, while it is the enormous Zaibatsu and Chaebol which do so in Japan and Korea?

⁷⁰ Cited in Lau, Siu-kai, 'Utilitarianistic Familism: The Basis of Political Stability', in Ambrose Y. C. King and Rance P. L. Lee (eds.), *Social Life and Development in Hong Kong* (Hong Kong: The Chinese University Press, 1981), p.197, note 8.

⁷¹ See Zhang, Jiaming (張家銘), *Jingji Quanli yu Zhipei--Taiwan Daxing Qiye Zuzhi de Zhidu Fenxi*. (經濟權力與支配--台灣大型企業組織的制度分析, *Economic Power and Domination—Institutional Analysis of Taiwan's Large Enterprises*) (Unpublished Ph.D dissertation, Donghai University, 1989), p.328.

⁷² For the Hong Kong case, see Victor Mok, 1981, *op. cit.*, p. 85; K. Y. Yeung, 'The Role of the Hong Kong Government in Industrial Development', in Edward K. Y. Chen, Mee-Kau Nyaw and Teresa Y. C. Wong (eds.), *Industrial and Trade Development in Hong Kong* (Centre of Asian Studies, University of Hong Kong, 1992), p.56.

Since the Cultural Confucian approach cannot explain a lot of the variants in the individual countries in the region, a better way to resolve the problem is to differentiate between different levels of analysis. Ruediger Machetzki tries to identify six basic traditional socio-cultural characteristics in East Asia: i.e., a) a relatively low resistance from the traditional human and social viewpoints to the transfer of technology, b) a society highly pressed by a so-called ‘particularistic’ or ‘situational’ ethics, c) the nature of elite political and social teachings, d) an elite education that cultivates a high motivation to learn, e) group-oriented thinking, and f) a strong savings and investment consciousness, which contribute to a nation’s modernisation success.⁷³ Margot Schueller notes that the Taiwan government fulfills five political conditions: i.e., a) the elites are capable of implementing ‘collective’ economic interests as against individual interests, and by doing so, they legitimate their rule, b) the state extends its role, intervening into the market to initiate and coordinate industrial development, c) it adopts the experience of industrialised countries according to precise evaluations of one’s own country’s capability and world market situation, d) a willingness to learn and an emphasis on the value of knowledge, e) the use of private savings and state investment to raise capital formation, plus f) a Confucian cultural background, to explain industrialisation.⁷⁴ Such an explanation hints that one must have the ‘right’ culture and ‘good’ government to be successful in economic development. But what is a ‘right’ culture? Most Confucian cultural explanations suffer from the fact that they only cite the traditional merits to strengthen their arguments, while neglecting those darker traits in the culture which can be easily picked up from many other writings. When they try to account for the failure of development, they do the reverse, i.e., look for the negative cultural factors, as Weber did.

Another question is that they do not say clearly how a strong developmental

⁷³ See Ruediger Machetzki, ‘Kulturspezifische Basis der Wirtschaftspraxis’ (Specific cultural basis of economic practices), in Werner Draguhn (ed.), *Neue Industriekulturen im pazifischen Asien—Eigenstaendigkeiten und Vergleichbarkeit mit dem Westen* (New Industrial Cultures in Pacific Asia—Autonomy and Comparability with the West) (Hamburg: Mitteilungen des Institutes fuer Asienkunde Hamburg, 1993), pp. 24-32.

⁷⁴ See Margot Schueller, ‘Die Rolle des Staates im Industrialisierungsprozess’, (The State’s Role in the Industrialisation Process), in Werner Draguhn (ed.), *Ibid.*, p. 139.

state could appear in Taiwan. What kinds of cultures can deliver a 'good' political regime? What are the articulation mechanisms of these different levels? It is a riddle in such writings. The 'strong state' approach tells us more about these unanswered questions.

1.2.2 The Strong State

In the 1980s a mainstream explanation of East Asian development was the 'statist approach', which was best exemplified in Gordon White and Robert Wade's words, that 'the phenomenon of successful "late development"...should be understood primarily...as a process in which states have played a strategic role in taming domestic and international market forces and harnessing them to a national economic interest'.⁷⁵

Robert Wade says that what makes East Asia an economic success is 'a consistent and coordinated attentiveness to the problems and opportunities of particular industries, in the context of a long-term perspective or the economy's evolution, and a state which is hard enough not only to produce sizable effects on the economy but also to control the direction of the effects'.⁷⁶ He uses the term 'governed market' to describe the Taiwan government 'getting prices right' and 'selecting certain industries' to promote economic development. He does not deny that getting prices right matters, as neo-classical economics always emphasises, but he says it is an inadequate explanation. More important is that the Taiwan government implemented a discriminatory industrial policy to help to establish some key industries which later became competitive in the world market.⁷⁷ Thomas Gold similarly argues that 'any explanation of Taiwan's growth with stability must start with the Nationalist party-state, ...which, with a great deal of autonomy from particular social interests, effectively led sustained

⁷⁵ See Gordon White and Robert Wade, 'Developmental States and Markets in East Asia: An Introduction', in Gordon White (ed.), *Developmental States in East Asia* (New York: St. Martin's Press, 1988), pp. 1-29.

⁷⁶ See Robert Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialisation* (N. J.: Princeton University Press, 1990), p. 343.

⁷⁷ See Robert Wade, 'State Intervention in "Outward-looking" Development: Neo-classical Theory and Taiwanese Practice', in Gordon White (ed.), *Development States in East Asia* (New York: St. Martin's Press, 1988), pp.30-67.

economic development....'⁷⁸ M. Shahid Alam also attributes the economic success to the high level of the government's commitment to economic development, which manifested itself directly in a subordination of political to economic objectives.⁷⁹

Ruth McVey observes that 'the essential ingredient of the strong, developmental state has been seen as its possession of autonomy from sectoral and societal interests, and hence its ability not only to reconcile differences and maintain order but to map out a strategy for improving the country's place in the world capitalist system'.⁸⁰ In other words, a relatively autonomous state and foresightful bureaucrats are two fundamental factors accounting for a country's success. In this story, culture gets no role on the stage.

The problems lie in the links between political regimes, economic strategies and the outcomes. One argument is to associate an 'authoritarian regime' with effective industrial strategies. The bureaucracy knows what is good for long-term development, and it adopts certain policies to initiate economic growth. This argument can be easily refuted, for even if they had the will to adopt developmental strategies, it is still hard for them to evaluate which policies would be positive or negative for development. Keynesian and Neo-classical economics develop different policy suggestions, and how did these Asian economic planners know which one was suitable for them? Since there are major disputes among economists, how could these bureaucrats be so confident of their policies?⁸¹

Stephan Haggard notes that 'the causal connection between growth strategy and political regime may be made in either strong or weak form. The strong argument holds that there are political prerequisites for the pursuit of a particular

⁷⁸ See Thomas B. Gold, *State and Society in the Taiwan Miracle* (Armonk, New York/London: M.E. Sharpe, 1986), p.122.

⁷⁹ See M. Shahid Alam, *Governments and Markets in Economic Development Strategies—lessons from Korea, Taiwan and Japan* (New York: Praeger, 1989), pp. 86-87.

⁸⁰ See Ruth McVey, *op. cit.*, p. 13.

⁸¹ There was a debate among Taiwanese economists to define what policies the KMT government implemented. See Tsiang, Sho-chieh (蔣碩傑), 'Taiwan's Economic Miracle: Lessons in Economic Development', in Arnold C. Harberger (ed.), *World Economic Growth* (San Francisco: Institute for Contemporary Studies, 1984), pp.301-325. Tsiang is a monetarist. Another representative scholar is Wang, Zuorong, whose view is Keynesian. See Wang, Zuorong, *Women Ruhe Chuangzao le Jingji Qiji* (我們如何創造了經濟奇蹟, *How do we create the economic miracle?*) (Taipei: Shibao Chubanshe, 1978).

growth strategy. Political elites and their coalition partners are aware of these institutional requirements and restructure or maintain the political system to attain their economic policy goals. The weak form of the argument holds that authoritarian politics are “functional” for a particular strategy, even if economic objectives are not sufficient in themselves to explain changes of regime’. He adopts the weak argument and argues that an authoritarian regime mainly wants to restore order, but later on pursues economic objectives which can be successfully achieved under authoritarian rule.⁸² Edwin A. Winckler shares the same view. He writes that ‘East Asia’s strong states emerge from global competition...in response to pressures from the world system that are geopolitical before they are developmental’.⁸³

This argument is more moderate, but still insufficient. When one says an ‘authoritarian regime is functional to development’, one says nothing more than the statement ‘politics intervenes in social life’. It is a tautology. If East Asia had failed, they would say an ‘authoritarian regime is dysfunctional’. If we look back carefully at Taiwan’s development in the past century, we can find that its economy kept on growing throughout the Qing dynasty, colonial times and the postwar era.⁸⁴ Can we say that each of these different regimes in Taiwan was beneficial to growth?

Even if the political institutions are functional to economic performance after 1945, this approach still ignores social institutions, e.g., families, schools, factories, associations, and industrial organisations, which constitute one’s whole social milieu. When the regime tried to enforce its policies through political institutions, either by means of coercion or moral persuasion,⁸⁵ it had to face resistance from the bottom. As a Chinese saying expresses it, ‘the higher level has

⁸² See Stephan Haggard, *Pathways from the Periphery--the Politics of Growth in the Newly Industrialising Countries* (Ithaca and London: Cornell University Press: 1990), chapter 10, pp. 254-270.

⁸³ See Edwin A. Winckler, ‘Globalist, Statist, and Network Paradigms in East Asia’, in Edwin A. Winckler and Susan Greenhalgh (eds.), *Contending Approaches to the Political Economy of Taiwan* (Armonk, New York: M.E. Sharpe, 1988), p.278.

⁸⁴ See Liu Jinqing, (劉進慶), ‘Cong Lishi Guandian Tanta Taiwan Jingji Chengzhang Wenti’ (從歷史觀點探討台灣經濟成長問題, On the Problems of Taiwan Economic Growth--from Historical Perspective), *Taiwan Xueshu Yanjiu Huizhi* (台灣學術研究會誌, *Journal of Taiwan Studies Association*), 1987, no. 2, pp.84-89.

⁸⁵ See Stephan Haggard, *op. cit.*, p. 262.

a policy, the lower level has a counter-strategy'.⁸⁶ Power is not centred on one dictator, and every bureaucrat has some leverage to defend his own interests. In her findings on Wenzhou's economic development in the PRC, Liu Yia-ling exposes different strategies used by local leaders to fight against central policies for their own interests.⁸⁷ In Taiwan, corruption was widespread in different institutions before political democratisation. These bureaucrats were not powerful, but had enough power to impede any policy implementation from the top. The Chinese use the slang saying '*Yamen Bazikai, Meiqian Biejilai*' (衙門八字開，沒錢別進來)⁸⁸ to describe how to deal with bureaucracy. A statist approach does not explain that under such corrupt, inefficient circumstances, Taiwan's businesspeople still make money.

The strong state approach became obsolete after the 1997 Asian financial crisis, which hit one of the most praised 'strong state model' South Korea. Now everyone blames the state's policy of "distorted incentives, lax regulatory standards, poorly managed financial liberalisation and inadequate disclosure and supervision [that] encouraged excessive risk-taking".⁸⁹ Insufficient disclosure of information, inadequate transparency in decision-making, improper economic policies which allowed capital to pour into the real estate market, crony capitalism, etc, all contributed to the failure of the economic system. The once admired strong state becomes the destabilising factor in economic development.

Long before the outbreak of the financial crisis in East Asia, many Taiwanese political scientists had tried to understand the 'relatively autonomous state' from the perspective of a patron-client relationship between central and local power elites, and between the government and businesspeople, which is in contrast to the statist approach. This perspective sheds light on the local institutions which are most relevant to most businesspeople, especially to small and medium-sized enterprises, which operate within a local area and have nothing to do with the

⁸⁶ 上有政策，下有對策。

⁸⁷ See Liu, Yia-ling, 'Reform from Below: The Private Economy and Local Politics in the Rural Industrialisation of Wenzhou', *China Quarterly*, no. 130 (June 1992), pp. 293-316.

⁸⁸ It means that a government office welcomes everyone, but don't come here without bringing any money.

central government. For example, Chen Mingtong's (陳明通) study on local factions shows the strong ties between local politics and local monopoly economic activities.⁹⁰ Chen Dongsheng (陳東昇) unveiled the mechanisms of land speculation by local factions and private monopoly capital in Taipei County.⁹¹ Wang Hong-zen (Wang Hongren, 王宏仁), Wang Zhenhuan (王振寰) and Liu Jinqing (劉進慶) all wrote about the close relationship between the bourgeoisie and the state in shaping economic policies.⁹²

Their research is subject to one criticism: they do not incorporate the market forces in their analysis, and assumed that if one had good connections with the government, one would reap huge profits from the benefits. But from the viewpoint of a national economy, such firms could not reap profits endlessly, for their profits cannot exceed the capacity of the total economy. For example, some reaped money from speculating in the stock market and land market, but after the collapse of the bubble economy, most of these entrepreneurs were trapped in the economic recession, and had to find a way out.⁹³ Market forces will limit the reach of political power.

Based on my own research, I will try to explain the role of the 'relatively autonomous state' in the economy, and to understand how local power could counter the central state's policy and cause 'inefficiency' from the viewpoint of rationality in the economic system. In addition, I will discuss the limits of political

⁸⁹ See "World Bank Accepts a Share of Blame for Asia Crisis", *International Herald Tribune*, 25 March 1998, p. 20. Original report is the World Bank's *Global Development Finance 1998*.

⁹⁰ See Chen, Mingtong (陳明通), *Quyuxing Lianhe Duzhan Jingji, Difang Paixi yu Shengyiyuan Xuanju: Yixiang shengyiyuan houxuanren beijing ziliao de fenxi* (區域性聯合獨佔經濟、地方派系與省議員選舉：一項省議員候選人背景資料的分析, *Regional Oligopoly, Local Factions and Provincial Assembly Elections: an analysis of the background of candidates*) (Taipei: unpublished paper, 1989), p. 12.

⁹¹ See Chen, Dongsheng (陳東昇), *Jin Quan Chengshi--Difang Paixi, Caituan yu Taipei Duhui Fazhan de Shehuixue Fenxi* (金權城市—地方派系，財團與台北都會發展的社會學分析, *Money+Power City--Sociological Analysis of Local Factions, Zaibatsu and Taipei Metropolitan Development*) (Taipei: Juliu Chubanshe, 1995).

⁹² See Wang, Hongzen (王宏仁), *Zhanhou Taiwan Siren Duzhan Ziben zhi Fazhan* (戰後台灣私人獨佔資本之發展, *The Development of Private Monopoly Capital in Postwar Taiwan*) (Unpublished Masters thesis, National Taiwan University, 1988); Wang, Zhenhuan (王振寰), *Taiwan Xin Zhengshang Guanxi de Xingcheng yu Zhengzhi Zhuanxing* (台灣新政商關係的形成與政治轉型, *The State, Capital, and Taiwan Political Transition*) *Taiwan Shehui Yanjiu Jikan* (台灣社會研究季刊, *Taiwan: A Radical Quarterly in Social Studies*), no. 14 (1993) pp.123-163; Liu, Jinqing, 1975/1992, *op. cit.*

power constrained by market forces.

1.2.3 The Magic Market

Neo-classical economics is based on three assumptions: maximising behaviour, market equilibrium and stable preferences.⁹⁴ When doing an empirical study on economic development, unfortunately the neo-classical economists always direct their attention to market dis-equilibrium and leave the other two assumptions as self-evident. No wonder the free market is perceived as determining economic success or failure.

When they explore the economic development of East Asia, based on their ideology, they largely want to know how the government deregulates the market, gets prices right and induces people to invest in ‘comparative advantage’ industries. Samuel P. S. Ho claims that the lessons from Taiwan can be ‘viewed as a series of gradual adjustments to changes in its comparative advantages....The Taiwan experience *once again* confirms that administrative controls and other forms of interference with the market can seriously distort the economy’.⁹⁵ Because the Taiwan government has taken a ‘fairly sensible, practicable approach to development’, the high quality of the human resources in Taiwan exploit the opportunities provided by the market and Taiwan attains significant growth.⁹⁶ Jiang Shuojie (蔣碩傑) has argued that Taiwan adopted the ‘right’ interest rates and exchange rate policy in the 1950s, which made the Taiwan economy efficient and, therefore, produced good economic results.⁹⁷ Hou Jiming believes that the neo-classical economic policy adopted by the government, i.e., conforming to

⁹³ For example, the famous stock speculators Lei Bolong (雷伯龍), Yu Huaiyin(游淮銀), and the business group Hemei(和美) in Tainan area.

⁹⁴ See Gary S. Becker, *The Economic Approach to Human Behaviour* (Chicago: The University of Chicago Press, 1976), p. 5.

⁹⁵ See Samuel P. S. Ho, *Economic Development of Taiwan, 1860-1970* (New Haven and London: Yale University Press, 1978), pp. 248-251.

⁹⁶ See Samuel P. S. Ho, *op. cit.*, pp. 251-252.

⁹⁷ See Jiang, Shuojie (蔣碩傑), ‘Taiwan Jingji Fazhan de Qishi’ (台灣經濟發展的啟示, The Implications of Taiwan Economic Development), in Ma, Kai (馬凱) (ed.), *Taiwan Jingji Yanjiu Luncong—di yi ji, Jingji Fazhan yu Zhengce* (台灣經濟研究論叢—第一輯, 經濟發展與政策, *Essays on the Economy of Taiwan, vol.1, Economic Development and Policy*) (Taipei: Zhonghua Jingji Yanjiuyuan, 1991), p.22.

market mechanisms, is the secret of Taiwan's success.⁹⁸ This same scholar would also attribute the success to increased human capital,⁹⁹ while others praise the functioning of a 'free labour market'.¹⁰⁰ Such rhetoric is repeated over and over again in neo-classical economics writings.¹⁰¹ But the important contribution of this approach is that it points to a fact: where there is control over the market, there is underground economic activity. For example, the work of Chen Shimeng (陳師孟) *et al.*, exposed the inefficient aspects of government control over the financial and manufacturing sectors.¹⁰²

Many sociologists or anthropologists lose their sense of market forces when they try to dismiss the functioning of the market in modern society, as we have pointed out in the preceding literature review. Based on this perspective, I will discuss the problems arising from the government's control over certain industries, and shall observe how people under this political control could gain undue benefits from it.

But the assumptions of neo-classical economics are *a*-historical, and most Taiwanese economists tend to forget the history of Taiwan of the past fifty years. They talk about Taiwan's economic history so far as the history fits into their doctrines. Sometimes they forget that their assumptions are not found in reality.¹⁰³ Let me briefly note three of these assumptions. Firstly, maximising behaviour is a

⁹⁸ See Hou, Jiming (侯繼明), 'Jiegou Xuepai, Xingudian Xuepai yu Taiwan Gongye Shengji' (結構學派、新古典學派與台灣工業升級, Structuralist, Neo-classical Economics and Upgrade of Taiwan's Industry), in Ma Kai (ed.), *Ibid.*: p.32.

⁹⁹ See Hou Jiming, 'Jiaoyu, Renli yu Gongping de Jingji Fazhan: Taiwan de Shili' (教育、人力與公平的經濟發展：台灣的實例, Education, Human Resources and Economic Development with Equality: the Case of Taiwan), in Ma Kai(ed.), *Ibid.*: pp.41-61.

¹⁰⁰ See Wu, Huilin (吳惠林), 'Taiwan de Laodong Shichang yu Jingji Fazhan' (台灣的勞動市場與經濟發展, Taiwan's Labour Market and Economic Development), in Ma Kai (ed.), *Ibid.*: pp. 83-113.

¹⁰¹ See W. Galenson (ed.), *Economic Growth and Structural Change in Taiwan: The Postwar Experience of the Republic of China* (Ithaca: Cornell University Press, 1979); Lin C-Y, *Industrialisation in Taiwan, 1946-72: Trade and Import-Substitution Policies for Developing Countries* (New York: Praeger, 1979); Shirley W. Y. Kuo, Gustav Ranis and John C. H. Fei, *The Taiwan Success Story: Rapid Growth with Improved Distribution in the Republic of China, 1952-79* (Boulder: Westview, 1981); Bela Balassa, *The Newly Industrialised Countries in the World Economy* (Elmsford, N.Y.: Pergamon, 1981).

¹⁰² See Chen, Shimeng (陳師孟) *et al.*, *Jiegou Dangguo Ziben Zhuyi* (解構黨國資本主義, *Disintegrating KMT-State Capitalism*) (Taipei: Chengshe Baogao 1, 1991).

¹⁰³ See Wang, Hongzen, 'Jingji Qiji? or Jingjixue de Shenji?' (經濟奇蹟? 或是經濟學的神蹟, Economic Miracle? or Miracle of Economics?), *Zhongguo Luntan* (中國論壇, *China Tribune*), vol.25, no.3 (1987) pp.45-48.

product of historical capitalism and does not exist in other types of economies.¹⁰⁴ In search of East Asian development we have to know how traditional behavioural patterns fit into the capitalist market. Secondly, if there were ‘stable’ preferences, there would be no fashions, no new products to stimulate new markets.¹⁰⁵ Lastly, a self-regulating market is always accompanied by government controls; in fact, a capitalist market is an artificial product, which could not exist if there were no political intervention.¹⁰⁶ This argument can be seen from the ambivalent feeling toward government activity in neo-classical economics. The neo-classical economists are not anarchists, so they reluctantly support the concept of a ‘minimum state’, which no one can satisfactorily define.¹⁰⁷ The strong state approach provides an extreme critique of this assumption, but ironically both approaches generally ignore the role of tradition and social institutions, which is the setting of political and economic forces.

2. Theoretical Framework

Based on these observations and critiques of the work done by other scholars, I will use the two concepts of market relations and social relations, which are derived from the two concepts of a ‘self-regulating market’ and ‘protective social forces’ developed by Karl Polanyi, to analyse the forces acting on individuals in a family firm.

In the self-regulating market, in the depiction of neo-classical economics, human beings are self-interested, trying to maximise profits or utility, and to minimise costs, subject to the constraints set by the market. This depiction assumes *an atomised self-interested person conforming to market competition*:

¹⁰⁴ See Karl Marx, *Das Kapital*, Marx-Engels Werke vol. 23 (Berlin: Dietz Verlag, 1867/1977), pp. 85-98. Maurice Godelier, ‘The Rationality of Economic System’, in *Rationality and Irrationality in Economics* (New York and London: Monthly Review Press, 1966/1972), pp. 243-319. Marcel Mauss, *The Gift: forms and functions of exchange in archaic societies* (London: Cohen Press, 1954).

¹⁰⁵ See Herbert Marcuse/ tr. by Douglas Keller, *One Dimensional Man: studies in the ideology of advanced industrial society* (London: Routledge, 1991).

¹⁰⁶ See Karl Polanyi / tr. by Huang Shumin, Shi Jiayin and Liao Liwen, *The Great Transformation—Origins of Our Time* (Chinese, *Jubian: Dangdai Zhengzhi, Jingji de Qiyuan*, 鉅變：當代政治經濟的源起) (Taipei: Yuanliu Chubanshe, 1957/1989).

¹⁰⁷ See Milton Friedman, *Capitalism and Freedom* (Chicago: the University of Chicago Press), p.34.

atomised, because man is self-sufficient;¹⁰⁸ self-interested, because the pursuit of interests is in the nature of being human; conforming to market competition, because the market is self-regulating and conforming to market regulation is the only principle to survive. The relationships between a person and others are based on ‘self-interest’, on contracts, and on instrumental rationality. This kind of market relations is generally accepted in our capitalist world, which generates the market forces that bear upon individuals.

The concept of social relations is defined as the relationships between kin, friends, neighbours, associations, and religious belief. These are not based on the ‘freedom of contract’, or self-interested calculation, or a newly arisen political order, which violates the goal of a free market, i.e., the pursuit of maximised self-interest. People are *socially embedded and conform to social norms*: socially, because man is a social being, who cannot survive and develop one’s capacity without support from society as a whole;¹⁰⁹ embedded, because social action is ‘embedded in ongoing networks of personal relationships rather than being carried out by atomised actors’;¹¹⁰ conforming to social norms, because these act on individuals as if they objectively exist, as Emile Durkheim observed. The relationships between a person and others are based on norms, on power, and on values. This kind of social relations produces pressures on individuals.

Everyone in a capitalist society is embedded in market and social relations. I will use ‘market principle’ to denote the rules that economic man follows in market relations, while ‘social principle’ means the rules accepted by people in their social relations. The two principles influence individuals’ behaviour simultaneously. The rules set by the market principle may be consistent with social rules. However, often the social rules contradict the market principle. For example, it is not accepted behaviour for a shopkeeper to make money from sales made to his parents in Taiwan. Yet if the parents keep on taking away goods from the store to re-sell to their friends, what can the shopkeeper do? Can he charge his

¹⁰⁸ See Charles Taylor, ‘Atomism’, in his *Philosophy and the Human Sciences—Philosophical Papers 2* (Cambridge: Cambridge University Press, 1985), p.189.

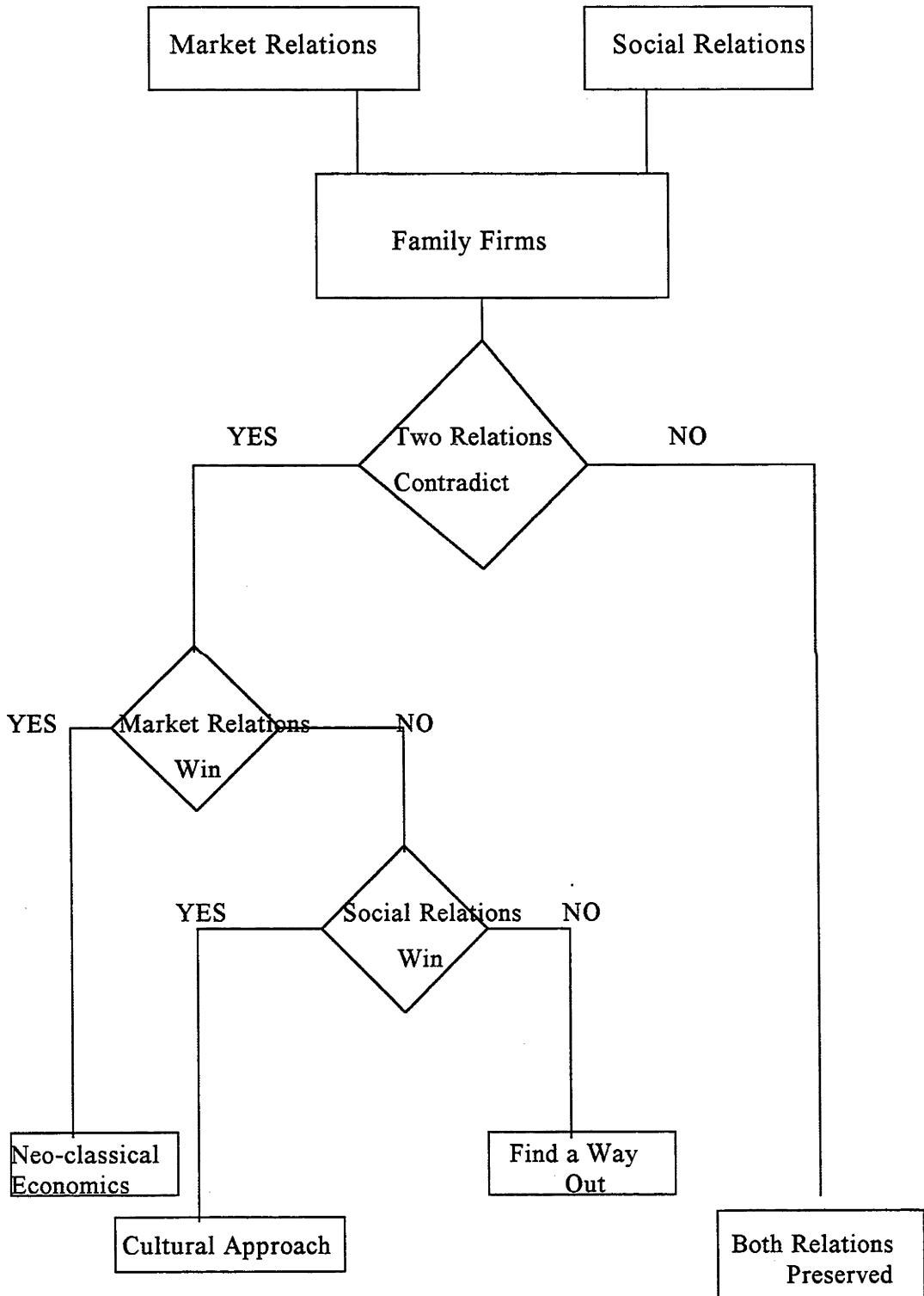
¹⁰⁹ *Ibid.*: pp. 204-206.

¹¹⁰ See Richard Swedberg and Mark Granovetter, ‘Introduction’, in Mark Granovetter and Richard Swedberg (eds.), *The Sociology of Economic Life* (Boulder: Westview Press, 1992), p. 9.

parents or must he behave filially until he goes broke? In the following pages, we will be able to see the contradictions arising from the working of the two principles. No one principle can be flattened to the other, and every business person has to face the two forces. 'Family enterprises' show the two forces acting on an organisation: the family belongs to social relations, while the enterprise is the basic unit in market relations. The strategies used by the head of the family firm entail both principles, and when there are contradictions, s/he has to find a way out.

I will observe the development and business practices of small- and medium-sized enterprises in Taiwan, which are mostly family firms, when they try both to make profits in the market and at the same time conform to the social norms imposed on them. My arguments are: if social relations and market relations do not conflict with each other, they can pursue profit with social approval. However, when the two elements are mutually exclusive, the proprietor has to choose either to follow social relations or market relations. Normally the market relations will prevail over social relations. When so, we would like to know what the social consequences will be. My logic can be seen in the following diagram.

Theoretical Framework



With this framework, I distinguish myself from the neo-classical economics and cultural approaches to family firms. Even though the tools and main assumptions are the same as in neo-classical economics, Oliver Williamson adds ‘transaction costs’ in his cost-benefit analysis of organisations. His claim is that any organisational form we observe in any situation is that which can reduce the transaction costs efficiently.¹¹¹ In mathematical expression, it is:

$$y = f(Xi)$$

subject to $g(Xi) \leq C$
 y : organisational form
 Xi : variable i (one of the variables is transaction cost variable)
 C : total cost

In this formula, a certain organisational form will appear if and only if a certain combination of all variables, which affect the emergence of an organisational form, is less than the total cost. Since the formula developed by Williamson is the same as in neo-classical economics, what I criticised in the former section also applies here. This approach ignores the values and loci of power within society. Too, it is tautological, for what we observe at the moment is deemed the most efficient with the minimum transaction costs. It also excludes any possibility of social change given that the *status quo* is deemed the most rational and efficient. In Chapters Three to Six, I will explore the tenets of neo-classical economics, and will argue that under certain conditions, social relations are more important.

My approach also distinguishes me from the ‘social embeddedness theory’ developed by Mark Granovetter and his colleagues.¹¹² Granovetter observes that ‘many economic problems that by tradition belong to the economists’ camp can be fruitfully analysed with the help of sociology’.¹¹³ He notes that ‘most behaviour is closely embedded in networks of interpersonal relations’¹¹⁴ and stresses ‘the role of concrete personal relations and structures (or “networks”) of such relations’ in

¹¹¹ Oliver Williamson, *Markets and Hierarchies* (New York: Free Press).

¹¹² Mark Granovetter, ‘Economic Action and Social Structure: The Problem of Embeddedness’, in Mark Granovetter and Richard Swedberg (eds.), *The Sociology of Economic Life* (Boulder: Westview Press, 1992), pp.53-81.

¹¹³ Richard Swedberg and Mark Granovetter, *op.cit.*, 2.

economic behaviour.¹¹⁵ He criticises the under- and oversocialised views of human action. Transaction cost theory is undersocialised, and functionalism or other sociological works are oversocialised. He claims that ‘the embeddedness approach to the problem of trust and order in economic life, then, threads its way between the oversocialised approach of generalised morality and the undersocialised one of impersonal, institutional arrangements by following and analysing concrete patterns of social relations’.¹¹⁶ In this way, economic life is embedded in social relations,¹¹⁷ and the self-regulating market disappears in his theory. For example, when he takes the example of the persistence of large numbers of small firms, he ‘suggests here that small firms in a market setting may persist instead because a dense network of social relations is overlaid on the business relations connecting such firms and reduces pressures for integration’.¹¹⁸ In other words, he does not believe that market forces will sweep away small firms because ‘there are social relations’ which make these small firms efficient enough to survive. If we put at one end of a pole the assumptions of neo-classical economics, which believes market relations will win in the long run, Granovetter’s New Economic Sociology should be placed at the other end of the pole, believing that social relations will win.

Yet the New Economic Sociology analysis is similar to neo-classical economics, in that it assumes rational action, subject to certain constraints. Granovetter says that ‘the assumption of rational action...is a good working hypothesis’, and ‘when situational constraints are fully appreciated’, all rational and non-rational behaviour can be analysed.¹¹⁹ Granovetter’s analytical method is similar in this respect to Gary Becker’s, who analysed discrimination, wage differential, etc, based on a rationality assumptions subject to social constraints.¹²⁰

Following this line of thinking allows us to escape the difficulties faced by

¹¹⁴ See Mark Granovetter, ‘Economic Action and Social Structure: The Problem of Embeddedness’, 1992, p.73.

¹¹⁵ *Ibid.*: p. 60.

¹¹⁶ *Ibid.*: p. 63.

¹¹⁷ *Ibid.*: p. 75.

¹¹⁸ *Ibid.*: p. 76.

¹¹⁹ *Ibid.*: p. 75.

neo-classical economics, which prophecies that the market will win in the future. Nor will I be trapped in the 'oriental discourse' whose description of economic actions in China is based on *xinyong* and *guanxi*. Rather, through the dialectical development of the two forces, I hope to explain the dynamic development and strategies of the family enterprises in Taiwan.

3. Structure of the Dissertation

The dissertation is organised in line with businesspeople's life histories. First I will discuss the origins of the small business class before 1960, showing the social and political setting of these businesspeople. Then I will discuss their educational backgrounds and their social mobility after they leave school. From Chapters Three to Five, I will analyse the business practices that prevail in Taiwan, including finances, marketing, and human resource management. The circumstances in which businesspeople make money, and how they run their business, will also be probed. Step by step, I will unravel the effects of different forces on businesspeople's behaviour. In Chapter Six, I will move the setting overseas, in order to observe how they manage and profit in a different socio-political context, which can be used as a contrast to practices at home in Taiwan.

Chapter One is a historical analysis, which tries to probe the different opportunities of people from different classes and ethnicities at the outset of the reorganisation of Taiwan society from 1945 to 1960. The socio-political setting influenced the mobility structures of each socio-economic constituency.

We will see in Chapter Two that educational achievement in Taiwan is not simply a result of 'perfect competition' based on merit. I will argue that the inequality of socio-economic status in the 1950s and 1960s reproduced inequality in education, which was worsened by the intervention of political power. I will examine the effect of education on occupational attainment, and the mobility strategies adopted by people with different educational levels. I will also explore the generally held belief that 'the Chinese mentality promotes efforts to become an independent proprietor'.

¹²⁰ See Gary S. Becker, *The Economic Approach to Human Behaviour* (Chicago: The University of

In Chapter Three, it will be seen how the political setting, which strongly distorts the functioning of the ‘free financial market’, carves out a space for those businesspeople who are able to benefit from the political regulations. But it shall also be seen how businesspeople without political power have to resort to pure economic means to promote their status and incomes. The situation after financial de-regulation will also be probed to understand how family firms accommodated to the new situation.

Marketing management and long-term relationships, which are often depicted in the ‘embeddedness theory’ or cultural approach, will be discussed in Chapter Four. It will be observed how price competition and the market influence long-term relationships among small and medium-sized business proprietors. Another important factor in the economy, power, will be introduced to analyse the manoeuvres of economic actors in the market. I will argue that only in certain of Taiwan’s social structures will utilisation of *guanxi* be prevalent and that this mechanism alters when the social structure changes.

In Chapter Five I will extend my analysis of the contradictions of social and market relations into the family, which has always been regarded as a coherent unit. I will observe the contradictions in the human resources management of family firms, and also will see how they resolve these dilemmas. I will incorporate the traditional practice of *fen-jia* (division of families) to observe new trends.

Chapter Six will focus on overseas investments by SMEs in recent years. Business management in finance, marketing and human resources will be explored in comparison with these SMEs’ practices in Taiwan. In a different foreign political context, how do they adapt themselves to the new environment in light of their goal of maximising profits?

4. Methodology

A common definition of small and medium-sized enterprises is that ‘a small business in the manufacturing sector has less than 100 employees and in the service sector less than 20 employees. A medium-sized enterprise has between

100 and 500 employees in manufacturing and 20 and 500 employees in services.¹²¹ This definition has been adopted widely in Europe and North America, even though some companies employ few workers but have substantial sales. The Taiwan government's definition is more strict, that 'a small- and medium-sized enterprise in the manufacturing sector employs fewer than 200 workers, and realised capital is less than NT\$60 million (about US\$2 million at the exchange rate of 1:30), and in the service sector fewer than 50 workers and ~~not~~ than NT\$80 million in business sales'.¹²² The circumstances of my informants' enterprises is shown in Appendix 1.

The data for my study are based, overall, on three sources: interview fieldwork conducted in Taiwan from March 1993 to January 1994 and from September 1997 to March 1998; the General Survey of Social Change in Taiwan, whose raw data I have analysed using a computer; and secondary sources containing the findings and analyses of other researchers.

The fieldwork entailed repeated in-depth interviewing with forty-two businesspeople and three officials, including two females and forty-three males. Because they regarded their own financial situation as secret, I had to develop my own personal networks (*guanxi*) to reach these businesspeople. All of these interviewees were either friends or relatives, or their friends and relatives, or their friends and relatives in turn. Due to these personal connections I could deal with their responses as basically trustworthy. Even so, I found that they tended to avoid answering questions on profits and political attitudes. To gather more in-depth and reliable information, it became important to reach 'key' interviewees who were willing to talk entirely openly, either based on religious belief or personal trust. I interviewed such people on repeated occasions. The backgrounds of the interviewees are listed in Appendix One.

Each interview lasted approximately two hours and was held either in the interviewee's factory or in a restaurant. I used a semi-structured questionnaire to

¹²¹ See Department of Foreign Affairs and Trade, 1995a, *op. cit.*, p. 8.

¹²² The definition of SME has changed seven times, and the latest revision was announced in 1995. This is the one I am citing here. See Small and Medium Enterprise Agency, *White Paper on Small and Medium Enterprises* (中華民國八十四年中小企業白皮書), 1996, p.354.

guide me, which included questions about their individual life history, production, marketing, finances, and external social and political relationships. The interview usually proceeded as follows: in the beginning I asked her/him to talk about her/his life since s/he was born. From her/his self-description, I gained background data on education, ethnicity, parents' occupations, and what sorts of jobs s/he did before s/he ran her/his own business. Whenever s/he mentioned a key question, e.g., her/his relationships with her/his siblings, I would dig into the relationships, which in the context of Taiwanese cultural values might often be considered shameful to talk about.

During October 1997, in the final stage of thesis-writing, I used a structured questionnaire pertinent to my dissertation's main themes, to obtain relevant information from another forty people. This enables me to make more generalised conclusions that build upon what I earlier had derived from the face-to-face interviews.

For the above reason that personal connections were necessary to attain access to respondents who are small and medium-sized businesspeople, the second sample was also not randomly selected, and it is not large enough to be representative. But I have sought to complement the interview and questionnaire data with a general survey. This survey was conducted by the Institute of Ethnology at the Academia Sinica (中央研究院民族學研究所). The respondents were randomly selected across the whole island.¹²³ I have obtained the raw computerised data for 1986 and for 1990 to 1993. Each survey contained information on more than two thousand respondents. In different years there were different survey topics, but each year's survey contained similar basic personal background data on occupational distributions, values, social stratification, and economic and political attitudes, which I have been able to utilise to study business activities in the 1980s and early 1990s. I have used a computer to do statistical analyses of the raw data.

In addition, to look back at the business history of the 1950s and 1960s, I

have had to depend in part on writings from that time, because most of my interviewees did not start their businesses until the 1970s. A wide literature review became essential to study this period. I have been to the Academia Historica in Taipei to find historical documentation, including official documents. The latter documents largely portray official viewpoints, which did not normally prove helpful to understand the businesspeople's viewpoint, but some of this material nonetheless proved valuable. Surveys conducted by the Joint Commission on Rural Reconstruction in the 1950s will be used to analyse the class structure at that time.

¹²³ About the sampling methods, implementation and preliminary results, see Qu, Haiyuan (瞿海源)(ed.), *Taiwan Diqu Shehui Bianqian Jiben Diaocha Jihua* (台灣地區社會變遷基本調查計劃, The Plan of the General Survey of Social Change in Taiwan) (Taipei: the Institute of Ethnology, Academia Sinica, 1991).

Chapter 1: Historical Origins of Taiwan's Small and Medium-Sized Enterprises (1945-1960)

In Taiwan numerous proprietors of small and medium-sized enterprises emerged in the 1960s. But what were their activities in the 1950s? What types of people, from what backgrounds, were engaged in industrial and commercial activities before 1960? How did they run their business? To understand the more recent decades, as I suggested in the Introduction, we need a historical perspective. The failure to probe into these earlier historical circumstances is, I would submit, a shortcoming of all those sociologists, anthropologists and political scientists who hold to an ahistorical approach, which I believe adversely affects their analyses. In this chapter, therefore, I will put on the hat of an historian.

I will briefly discuss the situation of small and medium-sized enterprises in the reorganisation of Taiwanese society after it was taken over by the Chinese Nationalist government. I will use historical data to delineate the class structures in this chaotic transition period from 1945 to 1949.

In the third part of the chapter I will discuss the class structure and mobility in the 1950s. This featured land reform implemented from above, ethnic differences, the state's strong economic control, and market fluctuations. However, let us start with the immediate post-war industrialisation and its influence.

1.1 The Chaotic Take-over (1945-1949)

Even though Japan surrendered in 1945, its influence on the later development of Taiwan cannot be neglected. Firstly, it created a reservoir of well-disciplined labourers for capitalist production. It also provided basic literacy, which enabled people to become small entrepreneurs in later decades when opportunities arose. Japanese Colonialism especially created a large number of businesspeople who could speak Japanese and who subsequently could develop close business connections with Japanese companies after the war.

Secondly, most of the industries during the colonial period were owned by Japanese, and these were subsequently 'nationalised' by the Nationalist government after 1945.

Most of the higher positions in these new public enterprises were occupied by the incoming Mainlanders (see Table 1.1 and 1.2), so the native Taiwanese had no chance to develop their careers in the public sector. Doing business in the private sector became one of the remaining paths to upward mobility.

Thirdly, the regulated economy established by the colonial government during the war was retained by the Nationalist government in the 1950s, and the private sector was dominated by the public sector throughout these years, until the boom of the 1960s when there arose an outlet for the private sector on the international market¹²⁴.

As noted, most large enterprises were Japanese-owned during the colonial period, and all of the Japanese companies were nationalised when the Nationalist government took Taiwan. The Nationalist army arrived in Taiwan on 25 October 1945. The colonial bureaucracy and Japanese enterprises initially continued to be operated by the Japanese according to new regulations set by the *Taiwan Xingzheng Zhongguo Gongshu* (Taiwan Administrative Governor's Office, 台灣行政長官公署) to avoid interruption to administration and production. Step by step, the personnel in these higher positions were replaced by newcomers and within a few years the old Japanese monopoly capital was replaced by Chinese party-state monopoly capital.¹²⁵ The production of the public sector in 1952 comprised 57.3% of total industrial production.¹²⁶ However, some of the 'enemy' property was sold to the private sector, and the sold enterprises bolstered the small business class.¹²⁷ In the following I will discuss how Taiwan society was reorganised in different groups. Some raked in exorbitant profits, but more lost out in the transition period.

¹²⁴ Relevant studies about the influence of Japanese colonisation on Taiwan include Tu Jaw-yan (涂照彦), *Nihon Teikoku Shugi ka no Taiwan* (日本帝國主義下no台灣, *Taiwan under Japanese Imperialism*) (Tokyo: The University of Tokyo Press, 1975); George W. Barclay, *Colonial Development and Population in Taiwan* (Princeton: Princeton University Press, 1954); Liu Jinqing (劉進慶), *Sengo Taiwan Keizai Bunshiki* (戰後台灣經濟分析, *Analysis of Postwar Taiwan Economy*) (Tokyo: The University of Tokyo Press, 1975); Zhou Xianwen (周憲文), 'Riju Shidai Taiwan Jingjishi' (日據時代台灣經濟史, *Taiwan Economic History during Japanese Colonial Times*) Taiwan Research Paper series no. 59. (Taipei: Economic Research Centre of Bank of Taiwan, 1958); Lin Jiwen (林繼文), *Riben Jutai Moqi (1930-1945) Zhanzheng Zongdongyuan Tixi zhi Yanju* (日本據台末期1930-1945戰爭總動員體系之研究, *Research on War Mobilisation System for in the Late Japanese Colonial Times*) unpublished Masters dissertation (1989), Graduate School of Political Science, National Taiwan University.

¹²⁵ Up to 1950, 860 Japanese enterprises were confiscated, but 19 of them were taken over by the KMT provincial party without any legal process. See Liu Jinqing, *op.cit.*, pp. 27-29.

¹²⁶ See Liu Jinqing, *op. cit.*, 117.

1.1.1. The Taiwanese Capitalists

Before the arrival of the Nationalist army, a lot of Japanese-owned land and factories were sold to Taiwanese at very cheap prices because the Japanese owners were afraid of Nationalist confiscation. According to a new law, such transactions with the Japanese before 15 August were recognised as legal. The problem was how to recognise the contracts made between Taiwanese and Japanese from the 16th of August to the 25th of October. Some speculative businesspeople forged contracts with wealthy Japanese to secure estates, and these contracts were forged with a date before 15 August. The head of Tatung Steel Company (大同鋼鐵廠), Lin Tizao (林提灶), collaborated with the Japanese and bought more than fifty houses, land, and machinery. In one night he became one of the most wealthy people in Taiwan. His son Lin Tingsheng (林挺生) later became a member of the Central Standing Committee of the KMT in 1969, which means that his economic power was recognised by the party. The transferred value of the estates was more than 30 billion, while the confiscated property put up for sale by Taiwan Province was valued at only 12 billion.¹²⁸ In short, some of the Taiwanese people reaped a lot of money in collusion with the Japanese during this chaotic transition period.

Another kind of speculative business was underground usury. The nominal interest rate set by the government was far below the inflation rate, so most of the money in the period flew into commercial or financial speculation. In the first half year of 1949, there were more than five hundred underground usurers, and the interest rate was as high as 80%, while the official interest rate was only 20%. The biggest moneylender had 250 billion dollars in deposits, while at that time the issue of Taiwan dollar banknote was only 470 billion.¹²⁹ In 1950, only 7% of farmers' loans derived from commercial banks (including the Land Bank), and 19% from the Farmers' Association, while 73% derived from private borrowing,¹³⁰ largely meaning rampant underground usury. A famous case involved Hou Yuli (侯雨利), who later became an important member of the Tainan Business Group in the 1950s. Though he had a textile factory and made a lot of profits

¹²⁷ *Ibid.*: pp. 26-27.

¹²⁸ See Huang Bing (黃炳), *et al*, *Petition to the National Resources Committee to Invalidate Those Transactions with the Japanese after the 15th of August*.

¹²⁹ See Liu Jinqing, *op.cit.*, p. 67.

¹³⁰ See Li Denghui (Lee Teng-hui, 李登輝), *Taiwan Nonggong Bumenjian zhi ZibenLiutong* (台灣農工部門間之資本流通), translated from his English work 'Intersectoral Capital Flows in the Economic

from selling cloth, his capital profits derived mainly from usury in the transition period. The amount of loans he provided was more than any co-operative credit union, and as much as a branch of the First Commercial Bank (one of the three commercial banks at that time).¹³¹

1.1.2 The Corrupt Mainlander Bureaucrats

After the uprising of February 1947, the National Resources Commission, which was in charge of all Chinese public enterprises, asked every Taiwan public enterprise to write a report on the ethnic distribution of the posts in each enterprise. The Nationalists knew very well that economic inequality was one cause of the uprising. From Table 1.1, 1.2 and 1.3 we can see that more Taiwanese worked as staff in the same given enterprises compared to Japanese times. But the problem was that the Mainlanders occupied almost every key position and they outnumbered the Taiwanese. The education of most of the Mainlander staff admittedly was high, and in terms of education they might have deserved their positions. But at that time 2,508 Taiwanese had been educated at Taiwan-based universities or colleges, more than 50,000 Taiwanese had graduated from Japan's tertiary educational institutions, and about a hundred Taiwanese had graduated from other overseas tertiary schools.¹³² Scarcely any had been assigned to important posts. So it was not education but ethnicity which determined economic opportunities at the time. Without a 'good background' a person could not be promoted in position, even if highly educated.

The public enterprises taken over by Mainlanders were trapped in corruption. During this period it was widely reported that public property was stolen, especially machinery. For example, the Taiwan Copper Mining Company (台灣銅礦公司) reported that before the arrival of the Nationalist army, 'thieves and bandits rose in swarms, and most of the equipment and small machinery sustained heavy losses. Even after the take-over,

Development of Taiwan, 1895-1960") Taiwan Research Paper series no. 106. (Taipei: Economic Research Centre of Bank of Taiwan, 1972), p. 119, Table 89.

¹³¹ See Xie Guoxing (謝國興), 'You Shang Er Gong: Guangfu Chuqi Tainan Bang De Tuibian' (由商而工: 光復初期台南幫的蛻變, From Commerce to Industry: the Transformation of Tainan Business Group in the Early Post-War Period), in Lai, Jeh-Han (賴澤涵)(ed.), *Taiwan Guangfu Chuqi Lishi* (台灣光復初期歷史, *Taiwan History During the Early Post-war Period*) (Taipei, Taiwan: Sun Yat-sen Institute for Social Sciences and Philosophy, Academia Sinica, 1993), pp. 335-364.

thieves and bandits were still audacious in robbing the property. Up to the end of March 1946 the loss reached 358,504.7 Taiwan dollars. From the first of April 1946 the company was restored to work, but it never stopped the burglars. By the end of May 1947 another 308,397.83 Taiwan dollars in equipment had been taken'.¹³³ No one knows whether it was stolen by cunning Taiwanese or by sly Mainlander managers. These machines presumably were subsequently bought and operated by the private sector.

Table 1. 1 Staff Distribution Between Japanese and Taiwanese in Japanese Enterprises (1944-45)

	Japanese	Taiwanese	Total	Year
Taiwan Copper Mining Co (台銅)	260	3	(?)	1944
Taiwan Engineering and Shipyard Co (台機與造船)	223	22	245	1944
Taiwan Aluminum Co (台鋁)	286	13	299	1945.3
Taiwan Fertiliser Co (台肥)	231	492	723	1945. ?
Yanshuigang Sugar Co (鹽水港製糖)	356	44	400	1945.12

Source: Documents from the reports of different companies submitted to the National Resources Commission.

Table 1. 2 Staff Distribution Between Mainlanders and Taiwanese in Public Enterprises (1946-50)

	Mainlander	Taiwanese	Total	Year
Taiwan Copper Mining Co (台銅)	117	72	169	1947.5
Taiwan Engineering and Shipyard Co (台機與造船)	22	146	168	1946.5
	130	187	317	1947.5
Taiwan Aluminum Co (台鋁)	82	39	121	1947.3
	153	47	200	1948.9
Taiwan Cement Co (台泥)	257	259	516	1950.6
Taiwan Steel Co (台灣鋼鐵)	58	8	66	1950.6

Source: the same as Table 1.1.

¹³² See Wu Wenxing (吳文星), *Riju Shiqi Taiwan Shehui Lingdao Jiecheng Zhi Yanjiu* (日據時代台灣社會領導階層之研究, *Research on Taiwan Leading Strata in Japanese Times*) (Taipei: 正中書局, Zhengzhong Publishing Co., 1992), pp. 114-124.

¹³³ At that time one Taiwan dollar could buy 12 kilograms of rice. See The Preliminary Work Team of Taiwan Copper and Mining Company of the National Resources Commission, *Ziyuan Weiyuanhui Taiwan Tongkuang Choubiechu Zai Tai Xiufu Shiye Ji Taibao Jiuye Qingxing Baogao* (資源委員會台灣銅礦籌

Table 1. 3 Distribution of Senior Positions Between Mainlanders and Taiwanese in the Taiwan Administrative Governor's Office, 1946

	Total	Chuzhang	Vice Chuzhang	Zhuan-yuan	Kezhang	Guzhang	Zhuren
		處長	副處長	專員	科長	股長	主任
MLD	251	8	2	76	37	90	38
	91.90%	100%	66.70%	87.40%	100%	93.80%	90.50%
TWN	22	0	1	11	0	6	4
	8.10%	0%	33.30%	12.60%	0%	6.20%	9.50%

Source: See Xu Bangnan (徐邦男), 'Dare ga Kimeru no ka--Kokumindo Seiken no Seisaku Kitei Kiko to Jinji Haichi' (Who makes decisions?--Policy decision making mechanism and personnel allotment in KMT regime), in Wakabayashi Masahiro (ed.), *Taiwan--Tenkanki no Seizi to Keizai (Taiwan--Politics and Economy in Transition)* (Tokyo:Tahada Shoten, 1987), p. 134.

Another problem in the public enterprises was factional struggle within the KMT party.¹³⁴ The Governor General, Chen Yi, assigned every Taiwan Provincial ministry post to members of his faction, which caused violent friction among different factions in the central KMT party. To counterbalance Chen's economic domination, the other factions occupied party and military positions. For example, the CC Clique controlled the KMT's provincial party, the Military statistical burea Clique (軍統派) controlled police organisations, and the Song Family (孔宋派) Clique assigned the members of its controlled National Resources Commission to take over the Japanese enterprises.¹³⁵ Such a factional struggle made it impossible for the public enterprises to function normally. Every faction member in the enterprises just wanted to appropriate higher profits for the faction and himself; no one cared about 'national' or common interests. Corruption became epidemic. One case is enough to illustrate the situation. Li Zhuozhi (李卓芝), a member of Chen Yi's faction, was general manager in the public enterprise Taiwan Paper and Printing Company. He sold some machines valued at more than ten million Taiwan dollars¹³⁶ at a very cheap price, and later bought these machines back for

¹³⁴ In the party there were five main factions: the CC, Military statistical burea, Song Family, Zhengxue and Tuan Cliques. The following paragraph is mainly from information in Chen Mingtong's article 'Paixi Zhengzhi yu Chen Yi Zhitailun' (派系政治與陳儀治台論, *Factional Politics and Chen Yi's Policy to Taiwan*), in Lai Jeh-Hang (ed), *Ibid.*: pp. 223-302.

¹³⁵ *Ibid.*: pp. 264-271.

¹³⁶ Unless noted, Taiwan dollar is used to designate old Taiwan dollar in this paragraph, which is different from the New Taiwan dollar used after June 1949.

his private company at 400,000 Taiwan dollars.¹³⁷ It is not hard to imagine, too, that because one public enterprise was the fortress for a faction, it was impossible for different companies to cooperate. In other words, there was little economic integration between different public firms. No wonder that in his General Report on Taiwan submitted to the National Resources Commission, S. Trone found ‘the general tenor in Taiwan is: each factory for itself, each manager by himself; if inflated big profits are made, then the industry is in order’.¹³⁸

1.1.3 The Speculative Mainlander Bureaucratic Capitalists

It was also a good time for Shanghai commercial capitalists and other Mainlanders to exploit the chaos to make money. The main export products from Taiwan were sugar and rice, while the main imported product was clothes from Shanghai. At that time the Chinese economy was under the Song Family Clique’s control. Its National Resources Commission was in charge of almost every public enterprise. From the manipulation of trade between Taiwan and Mainland China, it also reaped enormous profits. In 1946, the Commission, without paying a penny, shipped 150,000 tons of sugar from Taiwan to China, and purchased 400 million tons of coal at a very cheap price. In 1947 it ordered Taiwan to ship another 150,000 tons of sugar, 300 to 400 million tons of coals and 500,000 tons of rice to China without reimbursing any costs.¹³⁹

At the same time, it exported clothes from its controlled textile factories to Taiwan. The Song Family Clique’s textile capital derived from the taken-over of Japanese textile companies left in China. It reorganised all of these companies into the China Textile Construction Company (*Zhongguo Fangzhi Jianshe Gongsi*, 中國紡織建設公司), mainly based in Shanghai. In 1947 the company produced 37% of China’s silk and cotton materials, and 40% of Chinese cotton clothes.¹⁴⁰ Clothes were sold to Taiwan at a relatively high price. From January 1946 to September 1948, the clothes price index in Taiwan rose to 194.4 from 100, while the sugar price index was only 92.9 as compared

¹³⁷ *Ibid.*: p. 272.

¹³⁸ See S. Trone, *General Report on Taiwan*, unpublished manuscript submitted to the National Resources Commission, Nanking, China, January 21 1948, p.7.

¹³⁹ See Chen Mingtong, *op.cit.*, p. 264.

¹⁴⁰ See Watanabe Nagao, *Chugoku Shihonshugi to Sengo Keizai (Chinese Capitalism and Postwar Economy)* (Tokyo: Taiga Keizai Shunbunsha, 1950), p. 59. This is cited in Liu Jinqing, *op.cit.*, p. 231, note 9.

to the weighted total price index (=100).¹⁴¹ Why was the clothing price so high? One reason is that its import was monopolised by the Song Family Clique. Another reason was that the Taiwan dollar was undervalued as compared to the Chinese *Fabi* currency (legal currency, 法幣).¹⁴² If the Taiwan dollar was undervalued, it meant Taiwanese had to pay more to get the same quantity of products from China. Such an undervaluation was caused by hyperinflation in China and the fixed exchange rate system between the Taiwan dollar and *Fabi*, which did not change until January 1948. The Song Family Clique used its political and economic power to exploit the abnormal situation and grasped huge profits.

1.1.4 Taiwanese Landlords

Before 1960, Taiwan was still predominantly an agricultural country in the sense that farmers composed most of the population. In 1946, 57.8% of the total population was engaged in agriculture. About 40% of this agricultural population were tenants, and one-third semi-tenants, as can be seen from Table 1.4. The category of landowner included landlords and self-farming landowners. In 1944 the landlords owned about 32% of Taiwan's total arable land, while constituting only 3.5% of the total agricultural population.¹⁴³

Table 1. 4 Composition of the Agricultural Population (Households)

Year	Total	Agricultural Population (1946)			
		landowner	semi-tenant	tenant	farm labour
1946	527,016	172,314	148,580	206,122	--
	100.00%	32.70%	28.19%	39.11%	--
1948	645,941	216,736	154,460	231,224	43,521
	100.00%	33.50%	23.90%	35.80%	6.70%

Source: Wu Tianquan, *Taiwan de Tudi Wenti* (台灣的土地問題, *Land Problem in Taiwan*) (Taipei: unknown publisher, 1949), Table 10, appendix p. 5. Zhongguo Dizheng Yanjiusuo (中國地政研究所), *Taiwan Nongdi Jianzu Baogao* (台灣農地減租報告, *Report on Rent Reduction in Taiwan*) (Taipei: Zhongguo Dizheng Yanjiusuo, 1951), pp. 13-14.

Note: Semi-tenant means those farmers who owned some lands but not enough and had to rent more land to plough. Landowner includes farm-owners and landlords. Farm-labour means those who did not have any land and had to work for others.

¹⁴¹ *Ibid.*: p. 56, Table 13.

¹⁴² The Taiwan dollar's real purchasing power was about 30% undervalued in exchange for *Fabi*. See Liu Jinqing, *Ibid.*: p. 49.

¹⁴³ There were about 114,000 landlords, and the agricultural population was 3,318,235 in 1944. See Wu Tianquan (吳田泉), *Taiwan de Tudi Wenti* (台灣的土地問題, *Land Problem in Taiwan*) (Taipei: unknown publisher), p.30; Zhou Xianwen, *op.cit.*, p. 14.

Table 1. 5 Average Rent Payments in Different Counties (1927, 1948), %

Year	AREA					
	Taipei	Xinzhu	Taizhong	Tainan	Gaoxiong	Hualian
1927	54.0	51.2	49.5	45.7	45.3	--
1948	56.0	58.0	56.0	51.0	53.0	50.0

Source: See Hou K'un-hung (侯昆宏) (ed.), *Tudi Gaige Shiliao* (土地改革史料, *Land Reform Data of Modern China*) (Taipei: Academia Historica, 1988), p. 404. Wu Tianquan, *op. cit.*, appendix p.6, Table 12.

The land tenure system in the transition period was left untouched. The colonial system in which tenants paid rent in kind was simply inherited. The rent could be as high as over 70% of the whole year's crop, or as low as under 10%, depending on the relationship between landlords and tenants or the fertility of the land.¹⁴⁴ Table 1.5 shows how much the rent was in 1927 and 1948.

The rents were raised after the war. The reason is that the government raised taxes and landlords transferred the burden to their tenants. In that period, the Nationalist government was fighting against the Communist Party in the Mainland, so it needed to secure a grain supply. It adopted three different measures to collect more grain and at the same time to prevent inflation. In 1946 it asked all farmers to pay their land tax in kind. The second measure was to force landlords to sell their grain to the government according to the amount of land tax they paid. The third method was aimed at the grain of medium-to-big landlords. The more rice they had, the more they had to sell it to the government at a compulsory purchasing price.¹⁴⁵ This caused the landlords heavy losses, so one way to compensate was to raise rents. In Tainan, the share of the crops between landlords and tenants was raised from 5:5 in 1946 to 6:5 in 1947 and 6:4 in 1948.¹⁴⁶

¹⁴⁴ A survey done in 1952 on rural Taiwan shows the rent paid in 1948 as follows:

Rent	% of Tenants (N=351)
0-10%	5%
11-30%	8%
31-37.5%	3%
37.6-50%	21%
51-60%	16%
61-70%	8%
70-+%	8%
No answer	31%

See Joint Commission on Rural Reconstruction, *Rural Survey of Taiwan, October - December, 1952* (Taipei: Joint Commission on Rural Reconstruction, 1953), Tabular Materials Compiled From 1,176 Detailed Household Schedules, p. 9.

¹⁴⁵ For details of the process of forced grains-selling, see Liu Jinqing, *op. cit.*, pp. 60-65.

¹⁴⁶ See Hou K'un-hung (侯昆宏) (ed.), *op. cit.*, p. 366.

Of course, not every landlord relied on rent to survive. There were three different kinds of landlords. The big landlords usually had inherited their lands from the Qing Dynasty, and most of them had diversified their wealth into commercial and industrial activities in colonial times. The biggest landlord at that time, Gu Zhenfu (辜振甫), and the second, Lin Xiantang (林獻堂), already owned a lot of factories and banks in colonial times.¹⁴⁷ Their main activity was commercial and financial capital investment.

Another kind of landlord was less powerful nationwide, but locally influential. Most of them owned rice mills in the rural areas. The rice mills were often underground financial intermediaries where poor farmers and tenants borrowed at usurious rates. Because they owned a big granary and most peasants deposited grain in their granary, they could pool the unsold rice as a kind of deposit, and used this capital to invest in other commercial or financial activities.¹⁴⁸ But most of the ‘capital’ was used as usury. One sort was ‘*Maiqing*’ (買青), which means to lend farmers consumption funds or productive capital before planting, and after the harvest the loan had to be paid in kind: ‘the normal interest rate in Pingdong was 25% in 1952, while in an emergency, it could reach 40%, and in eastern Taiwan, the interest rate was even higher’.¹⁴⁹ Besides these local financial landlords, another sort of landlord were not wholly dependent on the rent income. They had jobs in co-operatives, farmers’ or fishermen’s associations in the local areas, and their incomes were mainly from the profits of these organisations.¹⁵⁰ They were managers or professionals, and were rural leaders. In the transition period, they were not greatly affected by the chaotic political and economic change.

Small landlords were more adversely affected. Natural disasters in 1946 and 1947, the hyperinflation, and the tax policy all increased their burden. Though they could transfer some of the burden to tenants, usually their lands were too small to cover all of the costs. But the fatal blow to these small landlords was yet to come.

¹⁴⁷ See Tu Zhaoyan, *op.cit.*, pp. 412-464. Also Zhao Wenshan (趙文山), *Taiwan ‘Sanqiwu’ Dizu Yundong de Toushi* (台灣三七五地租運動的透視·Thorough Understanding of Taiwan’s ‘Three-Seven-Five’ Rent Reduction Movement) (Taipei: Ziyou Chubanshe, 1949/12), pp. 131-132.

¹⁴⁸ *Ibid.*: p. 132.

¹⁴⁹ See Deng Xuebing (鄧雪冰), *Taiwan Nongcun Fangwen Ji* (台灣農村訪問記·Visit in Taiwan Peasant Village) (Taipei: unknown publisher, 1954), p. 96.

¹⁵⁰ See Zhao Wenshan, *op.cit.*, p. 132.

1.1.5 Taiwanese Peasants and Tenants

The average farm household, including landlords, owned only 1.4 hectares in 1948. Farm-owners had to pay higher taxes to the government, and had to deal with natural disasters and to cope with hyperinflation. Yet it was, of course, harder for tenants. They had to pay more rent to landlords as compared to colonial times, as we saw in Table 1.5. The survey done in October 1949 of 3,967 tenants, 1,032 farm-owners and 493 landlords gives a rough sketch of their living conditions.¹⁵¹

The expenditures of farm-owners were 63.2% of the landlords, while tenants' expenditures were only 37.7% of landlords in 1948. In the expenditures of tenants, 58.5% was spent on basic food and drink, a percentage that increased to 61% in 1949, reflecting a lower living standard. The survey shows that the smaller the land a tenant farmed, the higher percentage of his income he spent on food and drink.¹⁵²

Another figure shows that 18.7% of tenants were in debt, while the figure among farm-owners was only 9.3%. But the figures may be underestimates. No one wanted to expose her/his debt because usury was illegal under the law.¹⁵³ The interest rate in rural areas is shown in Table 1.6. The interest rate on private loans was almost 5 times more than the public interest rate, and the annual interest rate could reach as high as 432%.

Table 1. 6 Interest Rates Per Month in Rural Taiwan (1948-49)

<u>Year</u>	<u>Public Banks</u>	<u>Private Loans</u>
1948 (1-6)	3.6%	20%
1948 (7-12)	6.0%	30%
1949 (1-6)	10%	36%
1949 (7-12)	10%	36%+

Source: See Zhongguo Dizheng Yanjiusuo, *Ibid.*: p. 9.

¹⁵¹ See Zhongguo Dizheng Yanjiusuo (中國地政研究所), *Taiwan Nongdi Jianzu Baogao* (台灣農地減租報告, *Report on Rent Reduction in Taiwan*) (Taipei: Zhongguo Dizheng Yanjiusuo, 1951), p. 2.

¹⁵² See *Ibid.*: pp. 6-7.

¹⁵³ See Guomindang Zhongyang Gaizao Weiyuanhui Diliuzu (中國國民黨改造委員會第六組), *Taiwan Nongjia Jingji—Dang de Shehui Diaocha, Nongcun Dianxing Diaocha Baogao* (台灣農家經濟—黨的社會調查, 農村典型調查報告, *Peasant Economy in Taiwan—Social Survey of the Party, Report on Typical Village*) (Taipei: KMT, 1952), p. 17. It reports that ‘farmers were afraid that usury is illegal so that they did not like to report. Every interviewer had similar report. Their disguised reasons could be “only short-term turnover”, “not feel easy to report”, or obviously said “I am afraid it might affect my loan in the future”....’.

1.1.6 Taiwanese Workers

There were some 260,000 industrial labourers at the end of the war, when mass unemployment began to emerge.¹⁵⁴ This entailed three kinds of unemployment. The first involved Taiwanese soldiers dispatched back to Taiwan who could not find any job, a figure estimated at about 100,000.¹⁵⁵ Another was 'bureaucratic unemployment'. In 1945 there were 46,944 Taiwanese bureaucrats in the colonial bureaucracy, and the figure was reduced to 39,711 in December 1946. The figure for 1946 includes Taiwanese working in public enterprises, which had mostly been privately Japanese owned in colonial times. If we deduct this number, the figure comes to only 31,193. In other words, about one-third of the Taiwanese bureaucrats were laid off.¹⁵⁶ It was the same with the take-over of public enterprises, which laid off a lot of workers due to insufficient capital. The third kind of unemployment arose from the bankruptcy of small private enterprises. Because they were now cut off from Japanese supplies of material, many of these factories could not go on with their business. Another reason for bankruptcy were new regulations. For example, the government ordered that all reading materials for all schools should be ordered from the public enterprise Taiwan Printing Company, which drove many printing companies out of business. The situation was the same for private tobacco and wine manufacturers and import-export companies.¹⁵⁷

Life was hard for these unemployed. Most of them returned to rural villages and were responsible for the hidden unemployment seen in the successive increases of the agricultural population in these few years. From 1946 to 1948, the number of farmers increased by almost 23% (see Table 1.4). Even skilled professionals suffered. In 1946 the doctors of National Taiwan University Medical School went on strike because they did

¹⁵⁴ It was recognised by the secretary of Taiwan Zhangguan Gongshu Ge Jingen (葛敬恩) in his address to Provincial Assembly in June 1946. See Chen Xingtang (陳興堂) (ed.), *Taiwan "2.28" Shijian Dangan Shiliao--Nanjing Dier Lishi Dangan Guancang* (台灣二二八事件檔案史料—南京第二歷史檔案館藏, *Documents of Taiwan "Uprising February 28"—From Nanjing Second Academia Historica*) (Taipei: Renjian Chubanshe, 1992), pp. 78-88.

¹⁵⁵ See Xiao Shengtie (蕭聖鐵), 'Taiwan 228 Shijian de Jingji yu Wenhua Beijing--Shehui Qiwang Lilun zhi Yingyong' (台灣二二八事件的經濟與文化背景—社會期望理論之應用, *Economic and Cultural Background of the Uprising February 28 in Taiwan—Application of Social Expectation Theory*), in 228 Minjian Yanjiu Xiaozu (二二八民間研究小組, Folk research Team on the Uprising of February 28), *228 Xueshu Yantaohui Lunwenji* (二二八學術研討會論文集, *Essays on the Uprising of February 28*) (Taipei: 228 Minjian Yanjiu Xiaozu, Taimei Wenhua Jiaoliu Jijinhui, Xiandai Xueshu Yanjiu Jijinhui, 1992), p. 90.

¹⁵⁶ See *Ibid.*: p. 93 and Chen Xingtang (ed.), *op.cit.*, p. 664.

¹⁵⁷ See Zhang Qin (張琴), 'Taiwan Zhenxiang' (台灣真相, 'The Real Facts in Taiwan'), in Chen Xingtang, *op.cit.*, pp. 135-162.

not get enough in wages to cope with inflation.¹⁵⁸ The government did not have enough money to pay ordinary teachers, either. Their pay was delayed for three months in Taipei county from May to August 1946.¹⁵⁹ Such arrears were also reported in the ‘normal year’ of 1952.¹⁶⁰

1.1.7 Summary

From 1945 to 1949, Taiwan society experienced a chaotic take-over period. Real incomes in 1946 stood at only 10.64% of 1936, the year of highest incomes in colonial times.¹⁶¹ The average price index from January 1946 to September 1948 was 33,133 (1937=100), and the index worsened to 2,642,400 (1937=100) from October 1948 to June 1949, the month of the Taiwan Dollar Reform. In other words, the inflation rate was 7,975% in nine months. Wages and the income that farmers received for their rice lagged far behind the inflation rate. The wage index was only 33%, 29% of the total price index, while rice increased in price by only 90% and 74% in the two periods.¹⁶² Most native Taiwanese farmers, small landlords, tenants and workers were trapped in poverty.

Another segment of the native Taiwanese was little affected. They were the economic and political elites in colonial times, who still held influence in the new regime. They had been big landlords and capitalists under Japanese rule, and so long as their lands and enterprises were untouched by the new regime, they could use their power to appropriate profits and held onto their prestige through political participation. In this period big landlords transferred the burden of higher tax to their tenants. Besides, they had already diversified their wealth into commercial and financial activities, and were able to accumulate additional capital. Many of them later became leaders of business groups. After the uprising of February 28, 1947, some did not take part in politics any

¹⁵⁸ See Chen Xingtang, *op.cit.*, p. 68.

¹⁵⁹ See Xiao Shengtie, *op.cit.*, p. 93.

¹⁶⁰ In 1952, a report said that the mining companies owed labourers up to three months wages. They gave the workers the so-called ‘wage card’ which could be reimbursed in future. Most workers could not wait so long, so usually they discounted the ‘wage card’ up to 30% to get cash. See Guomindang Zhongyang Wei-yuanhui Sheji Kaohe Wei-yuanhui (國民黨中央委員會設計考核委員會, Scrutiny Committee in Central Committee, KMT), *Taiwansheng Changkuang Laogong Zhuangkuang Kaocha Baogao* (台灣省廠礦勞工狀況考察報告, *Reports on Labourers’ Conditions in Mining and Manufacturing Industries of Taiwan Province*) (Taipei: KMT, 1954).

¹⁶¹ See Xia Shengtie, *op. cit.*, p. 109, Table 1.

¹⁶² See Liu Jinqing, *op.cit.*, p. 56, Table 13.

longer,¹⁶³ but their economic power was still influential, insofar as they did not defy the new regime.

The new rulers from mainland China benefited the most from this power reshuffle. This privileged ‘carpetbagger’ group superseded the Japanese colonisers without changing the fundamental social and economic structures. As seen, too, different power blocks from China extended their battlefield to Taiwan, which contributed to economic and political underdevelopment in the period. Because they controlled most of the confiscated Japanese ‘enemy property’, which could not be properly operated under their management, economic performance in turn was interrupted.¹⁶⁴ The newcomers did not emphasise production, preferring sometimes to plunder the enterprises. They occupied every high post in the government bureaucracy, were granted privileges in doing business, and could rely on the armed forces to suppress dissent. The social cleavage between Taiwanese and Mainlander emerged in this period, especially with the violent suppression of the February 28 uprising.¹⁶⁵

Basically the colonial social class structures were left untouched, though they became more polarised in this period. The living standards of the small landlords, farm-owners, semi-tenants, tenants and workers worsened. As rulers, Japanese bureaucrats were simply replaced by Chinese bureaucrats, and the new antagonisms copied those of Japanese times. This would not change until the Nationalist government was defeated by the Communists in China and retreated to Taiwan. In trying to defend their last fighting base, they began to create new alliances. Land reform became a tool in this, which altered

¹⁶³ In their paper, Chen Mintong and Wu Naide find that there was ‘political disruption’ after the uprising of February 1947. In Gaoxiong county, the turnover rate in 1945, the year of the first county representative election after take-over, was only 20%, the same as in colonial time. But it increased to 80% in 1950, the first election after the uprising. They attribute the high turnout rate to ‘white-terror’. But this contradicts to Chen’s own finding in another article which says that most Taiwanese local factions owns local monopoly business, e.g., a local credit union. Almost every credit union was reorganised from Japanese cooperative union, which means that they were already influential in colonial times and kept their power in Nationalist times. See Chen Mintong (陳明通), Wu Naide (吳乃德), ‘Zhengquan Zhuanyi he Jingying Liudong’ (政權轉移和菁英流動, *Regime Transfer and Elites Mobility*), in Lai Jeh-hang, *op.cit.*, pp. 303-334.

¹⁶⁴ A popular joke at that time could express the Taiwanese feelings. The Taiwanese complained that the Americans treated the Japanese better than the Taiwanese because the American dropped only two atom bombs in Japan, but threw a whole Chinese army at Taiwan. This was reported by American journalist William Newton in March 1946. See Chen Xingtang, *op.cit.*, p. 65.

¹⁶⁵ See Yang Feng (楊峰), *Taiwan Guilai* (台灣歸來, *Return from Taiwan*) (Shanghai: Wenhui Newspaper, 4 March 1947), in Chen Xingtang (ed.), *op.cit.*, p. 113. It reports that the Taiwanese called those people from the mainland ‘people the from fatherland’ in 1945, but one year later, called them ‘Chinese’. They used a more discriminatory word ‘Waisheng Zhu’ (外省豬, Mainlander pig) after the military repression to express their resentment.

the social structure thoroughly.

1.2 Class Structures in the 1950s

No sooner had Chen Cheng (陳誠) been appointed as Taiwan's governor in 1949 than he announced an enforcement of the 375 Rent Reduction Act, a law from the mainland which was supposed to limit farm rent to a maximum of 37.5% of the total annual main crop yield. When the Nationalists took over Taiwan in 1945, a lot of naive tenants believed that they could ask landlords to reduce the rent according to the new Chinese law, which caused a lot of conflict between tenants and landlords at that time.¹⁶⁶ After the defeat in China, enforcement of the law became politically advantageous to the government, so as to create a new alliance with the rural population, composing more than 50% of the total labour force.

Rent reduction was the first step to reform the tenure system. The second step was the sale of public lands. The government owned more than 20% of total arable land in 1947. Most of these lands were confiscated property, especially the lands owned by the Taiwan Sugar Company, which had been a conglomerate of all colonial Japanese sugar companies. Though there had been a suggestion to sell public lands to tenants, it was not taken seriously into consideration until 1949. From 1948 to 1953, 35% of public lands were sold. Among the sold lands in the period, only 5% of the land was sold in 1948.¹⁶⁷ One can note that the Taiwan Sugar Company's better land was left almost untouched because its income was the main source for the government's foreign exchange reserves in the 1950s. It sold only about 14% of its secondary land to tenants.¹⁶⁸ On the one hand the Nationalists wanted to win tenants' support, but on the other it did not like to lose any revenue from its milk cow.

The third step was a Land to the Tiller Program whose main goal was to help to establish owner-farmers. It was implemented by the compulsory purchase of private tenanted farmland by the government and resale to the actual tiller. The political

¹⁶⁶ The rent reduction law was published in 1927, and was tried out in some provinces, but never much enforced. The conflict arising from tenants' requests and landlords' resistance was widely reported in the transition period. See Hou K'un-hung, *op.cit.*, pp. 352-353.

¹⁶⁷ See Tang Hui-sun (湯惠孫), *Land Reform in Free China* (Taipei: Chinese-American Joint Commission on Rural Reconstruction, 1954), pp. 80-81.

¹⁶⁸ *Ibid.*: pp. 69, 84. Taiwan's land is classified into different levels according to different fertility of the land. Government taxes the farmer according to the classification. 'Secondary' land means the 'second best' land.

motivation for this large-scale land reform was threefold: (i) the KMT wanted to create a new alliance, similar to the Rent Reduction Program, (ii) it wanted to eliminate the powerful influence of the landlord class in the rural areas, and (iii) it wanted to satisfy the expectations of the USA, which was pushing East Asian countries to reform their land tenure systems to prevent Communist infiltration.¹⁶⁹ The success of this land reform rested strongly on violent threats, and that the land reformers were reforming other people's land.¹⁷⁰

Through these reforms, the traditional social structures were deeply changed. Politically the landlord class was replaced by newly arising owner-farmers and local KMT branch cadres in the rural areas¹⁷¹; economically it diverted land-speculative capital into other spheres, and produced income redistribution effects to some extent.¹⁷² In the following pages I will limit my discussion to the impact of the reforms on class structures, the economic effects and the new possibilities that emerged to become businesspeople. But let us first examine the impact on Taiwanese local society of the influx after 1949 of Chinese immigrants, who started the land reform engine.

¹⁶⁹ See Theodore Reynolds Smith, *East Asian Agrarian Reform: Japan, Republic of Korea, Taiwan and the Philippines* (Connecticut: John C. Lincoln Institute, unknown publishing year, likely between 1967 and 1970), pp. 14-17. Taiwan's land reform was a ring of American planned agrarian reform in East Asia. Japan, Korea and Philippines had similar reform under American pressure.

¹⁷⁰ A lot of scholars have pointed out that the success of land reform in Taiwan was based on the military threat, especially after the massacre of February 28, 1947. The speaker of Pingdong's local parliament said that 'a driver in Taipei was sentenced to death because he caused a traffic accident. If a driver could be killed just because he violated a traffic law, we can imagine what the result would be if the landlords do not obey the law. Because landlords have the idea of the driver case in mind, the Rent Reduction Program was implemented easier.' See Zhao Wenshan (趙文山), *San Qi Wu Dizu Yundong de Toushi (三七五地租運動的透視)* (Taipei: Ziyou Chubanshe, 1949), p. 71.

¹⁷¹ The details of consolidating KMT's control in local politics, see Cheng Mingtong, *Paixizhengzhi yu Taiwan Zhengzhi Bianqian (派系政治與台灣政治變遷, Faction Politics and the Development of Taiwan Politics)* (Taipei: Yuedan Chubanshe, 1995), pp.152-166.

¹⁷² Only a few academic papers discuss the social effects of land reform. The best materials are from the research reports of the Joint Commission on Rural Reconstruction. See Arthur F. Raper, *Taiwan zhi Chengshi yu Gongye (台灣之城市與工業, Urban and Industrial Taiwan-Crowded and Resourceful)* (Taipei: U.S. Mutual Security Mission to China and National Taiwan University, 1954); E. Stuart Kirby, *Jinbuzhong de Taiwan Nongcun (進步中的台灣農村, Rural Progress in Taiwan)* (Taipei: Joint Commission on Rural Reconstruction, 1960); Arthur F. Raper, *Taiwan Muqian zhi Nongcun Wenti yu qi Jianglai zhi Zhanwang (台灣目前之農村問題與其將來之展望, Rural Taiwan-Problems and Promises)* (Taipei: Joint Commission on Rural Reconstruction, 1953); Martin M. C. Yang, *Socio-Economic Results of Land Reform in Taiwan* (Honolulu: East-West Centre Press, 1970); Chang Yen-tien, 'Land Reform and its Impact on Economic and Social Progress in Taiwan', *Industry of Free China*, vol. 23 No. 4 (April 1965); Cai Hongjin (蔡宏進), *Taiwan Nongdi Gaige dui Shehui Jingji Yingxiang de Yanjiu (台灣農地改革對社會經濟影響的研究, Research on the Influence of Land Reform on the Social Economy in Taiwan)* (Taipei: Jiixin Cement Cultural Foundation, 1967).

1.2.1 Bureaucratic Mainlanders

From 1946 to 1957 the population of civilian Mainlanders increased by more than one million, as Table 1.7 shows. Most arrived between 1949 and 1956. The large increase in Mainlanders from 1950-1957 included demobilised Mainlander soldiers. The figures in the table do not include soldiers, who comprised about 2% of Taiwan's total population. Such a big influx of new immigrants in such a short period had a strong impact on the indigenous society.

Besides soldiers, the non-soldier Mainlanders comprised 8% of the total population, and their occupations centred on tertiary industry. Almost 68% of the Mainlanders were in tertiary industry, as shown in Table 1.9. The Mainlanders' occupations in tertiary industry mainly centred on professional, clerical and sales work. A report observed that most of them were civil servants, staff in the communications sector and professionals (see Table 1.10).¹⁷³ Because they were loyal personnel of the Nationalist government, most of them having worked for the Nationalists on the mainland, the government felt a political obligation to take care of them. The result was that the public offices and enterprises became refugee shelters for these immigrants. Raper noted that 'the government's policy is to arrange for as many Mainlanders as possible to work in government',¹⁷⁴ and 'those who were from the mainland want to go back, but at the moment they have to get a job to survive, so it is almost impossible to lay off the redundant staff'¹⁷⁵.

More than one-fourth of Mainlanders were soldiers if we exclude those whose occupations are not categorised (see Table 1.8). Such a huge army was supposed to defend against Communist invasion with the help of the American seventh fleet. The government had to spend the lion's share of its fiscal budget to maintain this army. From 1952 to 1956 national defence expenditures in the central government budget averaged 80.9%. Even in the late 1980s, it still composed more than 50% of total central government expenditures. This caused budget deficits in the 1950s, which were financed by US aid, which comprised between 5.3% to 20.1% of the budget.¹⁷⁶ Without this aid,

¹⁷³ See Arthur F. Raper, translated by Quan Hansheng, Chen Shaoxin, *Taiwan zhi Chengshi yu Gongye*, *op.cit.*, p. 221.

¹⁷⁴ See *Ibid.*: p. 121.

¹⁷⁵ See *Ibid.*: p. 53.

¹⁷⁶ See Liu Jinqing, *op.cit.*, p. 189, Table 57; p.175, Table 49.

hyperinflation would have arisen similar to the postwar period.¹⁷⁷

Though there was universal compulsory military service after 1951, the standing army was mainly formed by Mainlanders. They were totally under the state's control. They were not allowed to marry until the 'successful recovery of the Mainland', a policy which was eased in the late 1950s; and they were not counted as a segment of the 'normal' population in official statistics unless they married and registered as a household.¹⁷⁸

Table 1. 7 Changes in the Taiwanese and Mainlander Population (1946-1957)

Year	Total (A)	TWN (B)	MLD (C)	C/A(%)
1946	6,090,860	6,059,139	31,721	0.52
1947	6,495,099	6,436,444	58,655	0.90
1948	6,806,136	6,678,969	127,167	1.87
1949	7,396,931	6,980,234	416,697	5.63
1950	7,554,399	7,029,459	524,940	6.95
1951	7,869,247	7,268,557	600,690	7.63
1952	8,123,374	7,473,544	649,830	8.00
1953	8,438,016	7,724,000	714,016	8.46
1954	8,749,151	7,983,087	766,064	8.76
1955	9,077,643	8,224,955	852,688	9.39
1956	9,390,381	8,435,965	954,416	10.16
1957	9,690,250	8,676,022	1,014,228	10.47

Source: Ryozauro Minami (南亮三郎)(ed.), *Taiwan no Jinko to Keizai* (Population and Economy in Taiwan) (Tokyo: Ajia Keizai Kenkyusho, 1971), p.30, Table 10.

Note: TWN means Taiwanese, and MLD means Mainlander.

The official unemployment rate was between 2.4% and 2.9% in the 1950s, but this must be an underestimate. A survey of rural areas in 1952 shows that the unemployment rate was 13% (see Table 1.11), while in urban areas in 1953 it was about 12.5%.¹⁷⁹ The figures did not include any underemployed. For example, about half of the working class

¹⁷⁷ As we know, the most convenient way for a government to finance its budget is to increase money supply from the central bank. The Nationalists did this in Taiwan through reform of the New Taiwan Dollar from 15 June 1949 to 1952. It caused inflation, which rose 57% in 1951 and 17% on 1952. The arrival of US aid in 1952 relieved the pressure to issue more banknotes. See Wu Congmin (吳聰敏), 'Meiyuan yu Taiwan de Jingji Fazhan' (美援與台灣的經濟發展, US Aid and Taiwan's Economic Development), in *Taiwan: A Radical Quarterly in Social Studies*, vol.1, no.1 (Taipei: Spring 1988), pp. 145-158. The developmental state theory should take into account such an 'irrational developmental budget' if such authors think the Taiwan government had a developmental mentality.

¹⁷⁸ They were not counted as a part of the population and labour force until 1969.

¹⁷⁹ See *Ibid.*: p. 218.

had only temporary jobs, which was counted as employment.¹⁸⁰

These workers in public offices or enterprises received wages in cash and in kind, including free housing or a housing allowance, rice, coal, oil, salt, etc. In June 1953, a civil servant's annual income was NT\$9,174, and half of the income was paid in kind. This wage was about 18.8% higher than the average income of NT\$7,722 (see Table 1.12). Because the pay was good and the job was stable, it attracted more educated people. The young men whose first formal job in the 1950s was in this sector averaged seven years of education compared to 5.8 years of education for young men in Taiwan as a whole.¹⁸¹ Mainlander bureaucrats had relatively stable jobs. They also thought they would be returning 'home' at any time, and thus had no incentive to leave the public service in order to establish a business.

Table 1. 8 Occupational Distribution Among Taiwanese and Mainlanders in the 1950s

OCCUPATIONS	ETHNICITY			
	TWN	%	MLD	%
Soldiers	2	0.08	28	17.95
Professional, technical and related workers	110	4.60	17	10.90
Representatives and officers	8	0.33	3	1.92
Managers in public and private enterprises	29	1.21	5	3.21
Clerical and related workers	122	5.11	15	9.62
Sales workers	209	8.75	14	8.97
Service workers	85	3.56	4	2.56
Agricultural, animal, forestry workers, fishermen and hunters	1084	45.37	20	12.82
Production and related workers, transport equip. operators and labourers	428	17.91	20	12.82
Occupations not categorised	312	13.06	30	19.23
Subtotal	2389	100	156	100

Source: I devised this table by putting raw survey data through a computer. The raw data derives from *The General Survey of Social Change in Taiwan, 1992*.

¹⁸⁰ See *Ibid.*: p. 215.

¹⁸¹ I have calculated this using a computer program from the raw data of 'A General Survey of Social Change in Taiwan, 1992'. Education differences among groups is statistically significant at the level of 1%. The mean of the educational years of different groups is shown as follows:

Self-employed	5.29	N=31
Employee	7.03	N=106
Work for Own Family	4.64	N=53
Housewife	4.50	N=2
Others	3.11	N=17
TOTAL	5.82	(N=209)

Table 1. 9 The Labour Force in Different Industries in the 1950s (By Ethnicity)

Industry Surveys		Unknown		Primary		Secondary		Tertiary	
		Father	Interviewee	Father	Interviewee	Father	Interviewee	Father	Interviewee
1989-90-1	TWN	59	46	183	121	28	56	46	93
	MLD	4	4	4	0	0	2	12	14
1989-90-2	TWN	52	49	199	126	27	71	62	94
	MLD	7	7	7	0	0	2	9	14
1991-92-1	TWN	42	33	253	95	36	96	86	193
	MLD	4	4	6	3	4	10	13	10
1991-92-2	TWN	34		157		17		36	
	MLD	0		1		1		14	
Subtotal	TWN	187	128	792	342	108	223	230	380
	MLD	15	15	18	3	5	14	48	38
TOTAL		202	143	810	345	113	237	278	418
2546	(2201)		(345)		1155		350		696
%(1)			13.6		45.4		13.7		27.3
%(2)					52.5		15.9		31.6
% (3)	TWN				(54.7)		(15.9)		(29.4)
	MLD				(16.7)		(15.1)		(68.2)
1953	TWN				(69.3)		(9.6)		(21.1)
Survey	MLD				(16.6)		(17.6)		(65.8)
1955	TWN				(29)		(20)		(51)
Survey	MLD				(4)		(22)		(74)
1952(%)	(4)				56.1		16.9		27.0
1955(%)					53.6		18.0		28.4
1958(%)					51.1		19.7		29.2

Source:

1. Derived by the author. Same as Table 1.8.
2. The 1953 survey was done by the Joint Commission of Rural Reconstruction. See Arthur F. Raper, (tr. by Quan Hansheng, Chen Shaoxin, *Taiwan zhi Chengshi yu Gongye* (台灣之城市與工業, *Urban and Industrial Taiwan-Crowded and Resourceful*) (Taipei: U.S. Mutual Security Mission to China and National Taiwan University, 1954), p. 221.
3. The 1955 survey is from Li Dongming (李棟明), *A Study on Social Increase of Population in Taiwan* (台灣地區人口社會增加之研究) (Taiwan: Taiwan Population Studies Centre, Taiwan Provincial Department of Health, 1968), p.71, Table 41. Original data is from Taiwan Provincial Government, Department of Civil Affairs, *Taiwan Provincial Household Statistics Summary, 1955* (Taipei: Taiwan Provincial Government, 1956).
4. The data is from A. Hermlin, P. K. C. Liu, and D. Freedman, "The Social and Economic Transformation of Taiwan", in Arland Thornton & Hui-sheng Lin (eds.), *Social Change & the Family in Taiwan* (Chicago and London: The University of Chicago Press, 1994), p. 72, Table 3.7. Original data is from Directorate-General of Budgets, Accounts and Statistics, Executive Yuan, 1984.

Notes:

1. Total number of different categories including unknown category is divided by 2,546.
2. Excluding the number of unknown category, divide the number of the three industry with 2201.
3. Ethnic occupation distribution in different industries, excluding the number of unknown category.
4. The figures here are labour force distribution in different industries. See source 4.

Table 1. 10 The Mainlanders' Occupational Distribution in Urban Areas (1953)

Occupations	interviewees	(%)
civil servants	71	20.06
communication workers	26	7.30
professionals	37	10.45
businesspeople	36	10.17
vendors	37	10.45
industrial workers	27	7.63
workers in other commercial activities	36	10.17
married soldiers	19	5.37
servants and others	24	6.78
unemployed	41	11.58
TOTAL	354	100.00

Source: See Arthur F. Raper, Quan Han-sheng, Chen Shao-xin, *Taiwan zhi Chengshi yu Gongye*, *op. cit.*, 218.

Table 1. 11 Employment in the Rural Taiwan (October-December, 1952)

(N=1,176)						
1952 Rural Survey	Farm-owners	Part-Tenants	Full-Tenants	Farm Workers	Non-farm People	All Others
Taiwanese	315	190	350	174	89	
Mainlanders		1	1	6	28	22
	(%)	(Full and Part Owners)				
On own farm		67%	66%	0	0	0
Maintenance		2%	3%	2%	1%	12%
Farm wages		4%	3%	19%	1%	1%
Non-farm wages		5%	6%	37%	54%	10%
Handicrafts, etc		8%	6%	13%	34%	15%
Unemployed		13%	12%	29%	11%	62%

Source: See Joint Commission on Rural Reconstruction, *Tabular Materials Compiled From 1,176 Detailed Household Schedules* (Taipei: unpublished manuscript, 1953), p.4, Table 1; p.6.

Note: The question asked by the Joint Commission on Rural Reconstruction is 'Use made of working time in last calendar year of husband'. The meaning of 'Maintenance' is not clear here.

Table 1. 12 Annual Household Income, 1953

Total Average	7,722
Employers	27,271
Self-employed	9,206
Workers	5,148
Professionals	11,708
Civil Servants	9,174
Others	7,128

Source: Arthur F. Raper, *Ibid.*: p. 124, Table 4.

1.2.2 Capitalist Mainlanders

A lot of rich political refugees brought gold bullion and US banknotes to Taiwan

after the Communist Party took over China. They used their money in three ways: industrial investment, underground speculation and hoarding.¹⁸²

Those who invested their capital in industry mostly had political connections with the Nationalist government, especially those in textiles. They shipped their dismantled machines from China, mainly from Shanghai, and went into operation under the government's protection. In 1953, seven out of the twelve big cotton textile factories were owned by Mainlanders, while four were public enterprises which were firmly controlled by Mainlander bureaucrats.¹⁸³ For example, the head of the Taiyuan (台元) Textile Company was Yan Qingling (嚴慶齡), who was the late president Yan Jiagan's (嚴家淦) brother. The company belonged to the Yu-long (裕隆, Yue-loong) business group, in which Madam Chiang Kai-shek held investment interests.¹⁸⁴ The other Mainlander capitalists who became big business groups all benefited from the government's protection policy in the 1950s.¹⁸⁵ One such important industry was the printing and publishing industry, which also benefited from the government's regulation of freedom of speech.

This kind of industrial investment, though it was a kind of bureaucratic capital, contributed to Taiwan's economy at that time, and to later development. Many future Taiwanese small businesspeople worked for a while in these companies, learned skills from their operation, and came out to run their own businesses when business opportunities emerged in the 1960s.

Another type of Mainlander capitalist were 'financial capitalists', who specialised in financial activities after they came to Taiwan. Some of the experienced Shanghai dealers dealt with the shares of privatised public enterprises released from the Land-to-the-Tiller reform. They set up businesses in Taipei, and connected up with small brokers in rural areas to purchase small landlords' shares, which were used to compensate their sale of

¹⁸² See Ziyou Zhongguoshe (自由中國社), 'Women de Jingji' ('我們的經濟', 'Our Economic Situation'), in *Jinri de Wenti* (今日的問題, *Problems Nowadays*) (Taipei: Ziyou Zhongguoshe, 1958), pp. 48-49.

¹⁸³ See Wang, Hong-zen, *Zhanhou Taiwan Siren Duzhan Ziben zhi Fazhan* (戰後台灣私人獨佔資本之發展, *The Development of Private Monopoly Capital in Postwar Taiwan*) (Taipei: unpublished Masters thesis, 1988), p. 27.

¹⁸⁴ See Liu Jinqing, *op.cit.*, p. 219.

¹⁸⁵ It included the Zhongxing Textile Business Group, Yuandong Business Group, Hualong Business Group, Jiaxing Business Group, Guofeng Business Group and Pacific Business Group. See Wang Hong-zen, *op.cit.*, p. 23. Hsiao Hsin-Huang Michael, 'The Entrepreneurial Process of Taiwan's Small-Medium and Big Business', *Zhongguo Shehui Xuekan* (*Chinese Sociology Journal*), no. 16 (1992), pp. 139-168.

land to the tenants.¹⁸⁶ The circulated shares of the four privatised companies became their speculative targets. The price rose five times in one year, and dropped to one-fifth in the successive year thanks to Shanghai speculative capitalists.¹⁸⁷

1.2.3. Taiwanese Landlords

Table 1.13 shows that in June 1952, landlords or part lessors composed 29.3% of total farm households. Strictly speaking, the 'real' landlords were 'full' lessors, which comprised 12.6% of total farm households.¹⁸⁸ Among these landlords, 87.3% were small landlords who owned paddy fields of less than two *Jia* (1 *Jia* is about 1 hectare), 9.3% owned between two and four *Jia*, while only 3.35% of these landlords owned more than four *Jia*.¹⁸⁹

Table 1. 13 Lands of Different Ownership Types, 1952-1953 (Unit: Jia)

OWNERSHIP TYPES	Individual	Joint	Corporate	Subtotal
Area of Owner-Cultivated Land	189,874	222,318	15,005	427,197
Area of Tenanted Land (1)	113,849	121,989	18,119	253,957
Subtotal	303,723	344,307	33,124	681,154
Number of Lessors	38,005	34,772	4,073	76,850
Number of Part Lessors, Part Owners	40,869	57,315	3,867	102,051
Subtotal(2)	78,874	92,087	7,940	178,901
Compulsorily Purchased Land (3)	32,063	99,796	11,709	143,568
% of Appropriated Tenanted Land = (3/1)*100%	28.16	81.81	64.46	56.53
Affected Landlord Households (4)	15,146	87,149	3,754	106,049
(%)=4/2	19.2	94.64	47.28	59.28
Purchased Land per Household (3/4)	2.12	1.15	3.12	1.35

Source: Tang Hui-sun, *op. cit.*, pp. 101, 105, 140.

¹⁸⁶ See Liu Jinqing, *op.cit.*, pp. 236-237.

¹⁸⁷ As the economic planner Yin Zhongrong (尹仲容) noted, to establish a legal stock market had an effect like the Shanghai stock market before 1949 where transactors were limited to small groups, and which had no positive effect on savings and industrial capital. See Yin Zhongrong, 'Dui Taiwan Sheli Zhengjuan Jiaoyisuo zhi Yijian' (我對台灣設立證券交易所之意見, Comments on the Establishment of Taiwan Stock Market'), in his *Wo dui Taiwan Jingji de Kanfa* (我對台灣經濟的看法, My Opinions to Taiwan Economy) (Taipei: Economic Planning Board, Executive Yuan, 1961), Second Part, p. 25.

¹⁸⁸ Another statistics shows that there were 142,175 landlord households, but it does not say what year it is. Let us assume that it was the statistics of 1951. In 1952 there were 679,750 farm households, so about 20% of farmer households were landlords. It is not greatly different from the figure Table 2.14 shows. See Guomindang Zhongyang Gaizao Weiyuanhui Diliuzu, *op.cit.*, p. 2, Table 1-3.

¹⁸⁹ See Tang Hui-sun, *op.cit.*, p. 103.

Another feature of land ownership in Taiwan was the high proportion of joint-owner households, which comprised 49.3% of total farm households and owned 50.5% of the total land. This was the product of traditional *fen-jia*, i.e., land is distributed equally to sons, and after a few generations, a small plot of land is owned by many people, but ploughed by one.

1.2.3.a The Influence of the Rent Reduction Program

For landlords, the first effect of rent reduction was a decrease in income. Rent payments decreased 29.3% in 1949. According to a survey, 73% of landlords' living standards were adversely affected. Among those landlords who held another job, only 56% were notably affected, while 98% of the other landlords were affected.¹⁹⁰ It was reported that the big and medium-size landlords were little affected because they usually had non-farm jobs in cities or towns. But for the small landlords who had only several hectares of land, this rent reduction program reduced their income to less than those of big tenants. They needed to terminate leases and to plough the land by themselves or by hired workers.¹⁹¹ From the beginning of 1950 to the end of June 1951, there had been 16,349 cases of lease termination and tenancy disputes, which increased to 35,313 one year later.¹⁹² Another way to cope with their reduced rental income was to find another job. But since they did not have any non-agricultural skills, and there were not a lot of industrial jobs available, they hardly could change their occupation.

The second effect of the rent reduction reform was a fall in farm prices and an increase in farms sold. When landlords heard that the Nationalist government would enforce the rent reduction program, they began to sell their land in 1948 (see Table 1.14). In 1949, the year the rent reduction program was implemented, the supply of land for sale increased abruptly to 10,791 hectares from 4,935 hectares in 1948. Under this situation, the land's price plummeted from 18,600 kilograms of unhulled rice per *Jia* in 1948 to 9,000 kilograms in 1950; the leased farm land could only be sold for half the price of owner-cultivated land.¹⁹³ Of the farms sold, 60.9% had been owned by landlords who owned more than 5 *Jia*. Where did the money go when they sold the land? For large

¹⁹⁰ See Zhongguo Dizheng Yanjiusuo, *op.cit.*, p. 7.

¹⁹¹ See Zhao Wenshan, *op.cit.*, pp. 72-73.

¹⁹² See Tang Hui-sun, *op.cit.*, pp. 50-56.

¹⁹³ See Tang Hui-sun, *Ibid.*: pp. 62-63.

landlords, 84.5% of the funds were invested in industry or commerce, while only 16.5% of the small landlords did likewise. 26.2% of the small landlords used the money to clear their debts.¹⁹⁴ It is obvious that the small landlords did not have a substantial chance to become businesspeople.

Table 1. 14 Number of Landlords Selling and Purchasing Land, 1946-49

Year	Number of landlords who sold land	Number of landlords who bought land	Land Sold (hectares)	Land Purchased (hectares)
1946	17,023	16,629	7,320	6,818
1947	14,017	16,234	4,205	4,545
1948	12,654	5,587	4,935	2,067
1949	22,960	16,412	10,791	6,893

Source: See Mao Yugang (毛育剛), 'Taiwan Tudi Gaige zhi Jingji Yanjiu' ('台灣土地改革之經濟研究', 'Economic Research on Taiwan Land Reform'), in Yu Yuxian (余玉賢)(ed.), *Taiwan Nongye Fazhan Lunwenji* (台灣農業發展論文集, *Essays on Taiwan Agricultural Development*) (Taipei: Lianjing Publishing Co., 1975), p. 163, Table 12.

Note: Calculation is based on land transactions in Xinzhu, Taizhong, Gaoxiang, Taidong, Hualian and Tainan.

1.2.3.b The Influence of the Land-to-the-Tiller Program

The Land to the Tiller Act of 1953 transferred 56.5% of the tenanted farms from the hands of landlords to tenants. Table 1.13 shows that 70% of the appropriated lands were jointly-owned. The number of appropriated joint landlords was 87,149. If we divide the size of the appropriated land with the affected landlords, the average size of the compulsorily purchased land of one landlord was 1.15 Jia for joint landlord owners, and 2.12 Jia for an individual owner. The reason why most of the appropriated lands were jointly-owned was because the jointly-owned landlords were smaller than individually-owned, and the government faced less resistance from these small landlords than from medium to large landlords. This table shows that only 19.2% of the individually owned lands were purchased, while almost all of the jointly-owned lands were appropriated.¹⁹⁵

There were many ways to evade appropriation. The first was to divide one's property and distribute it to sons. A second method, as noted, was to cancel the contracts with tenants and plough it themselves. Another method was to change the tenure contract to make the tenants wage-labourers, as 'wage-labourers' were not entitled to buy the lands that they were ploughing.

Landlords were compensated 30% through the shares of four public enterprises and

¹⁹⁴ Calculated from Zhongguo Dizheng Yanjiusuo, *op.cit.*, pp. 81-82, Table 15.

¹⁹⁵ See Liu Jinqing, *op.cit.*, p. 82.

70% through land commodity bonds in kind. At that time no one believed that the Nationalist government could pay the land commodity bonds for ten years, so some of them sold the bonds for a very low price in a very short period.¹⁹⁶ But research conducted in 1969 revealed that 85% of the interviewed landlords kept the land bonds to meet their living expenses. Commodity bonds were the major source of funds for consumption immediately after land reform, so the small landlords had to keep them.¹⁹⁷

How did these landlords dispose of their corporate stock? In a survey in 1966 of five hundred ordinary landlords and seventy-five big landlords, Martin M. C. Yang found that 98.4% of the ordinary landlords and 90.6% of the big landlords sold their stocks early, and that the prices they received, except for the Taiwan Cement Company, were 35% to 65% less than par value.¹⁹⁸ The small landlords were too small to control any company, and saw no benefits to keep stocks that did not provide immediate dividends, so they sold their shares to obtain cash. Their shares were mostly purchased by Shanghai capitalists who dealt on the stock exchange, and later on became concentrated in big landlords' hands, who had already been capitalists before the reform. The four privatised companies were under the control of these big landlords, who had already invested during colonial times. For example, the Taiwan Cement Company, the most profitable company among the four, was controlled by the Lin family of Banqiao (板橋), the Gu family of Lugang (鹿港), the Lin family of Wufeng (霧峰) and the Chen family of Gaoxiong (高雄) after the election of an executive board in October 1954.¹⁹⁹ An interviewee who worked as financial manager for the Jilong (基隆) Yan family confirmed that the four companies were controlled by the big landlords--including the Taiwan Mining Company and the Taiwan Agriculture and Forestry Company, which were agglomerations of Japanese small and medium-sized enterprises.

How did the landlords employ their capital when they sold their commodity bonds or stocks? Theodore Reynolds Smith found that all of the small landlords who sold commodity bonds used the money for their living expenses, and even among big

¹⁹⁶ It was reported that some landlords wanted the government can buy the commodity bonds so that the landlords can liquidate their capital. They would sell the commodity bonds as low as 25% of the value of the rice's market price. See Deng Xuebing, *op.cit.*, pp. 200, 223.

¹⁹⁷ See Theodore Reynolds Smith, *op.cit.*, pp. 93, 96.

¹⁹⁸ See Martin M. C. Yang, *op.cit.*, p. 238.

¹⁹⁹ See Liu Jinqing, *op.cit.*, p. 239.

landlords, only one-fourth invested in industry or commerce.²⁰⁰ In Martin M. C. Yang's survey, only 9.2% of small landlords and 17.6% of big landlords used it as capital for another investment, or to change occupation. In Smith's survey, their numbers came to 12.9% and 26.1% respectively. Obviously most of the capital was not invested in industry or commerce, contrary to the claims of the government and some scholars.²⁰¹

Yang's survey also shows that 20% of the ordinary landlords and 30% of the big landlords did change their occupation. He notes that 'big landlords had, in general, been able to enter comparatively large and modern businesses or industries, whereas the small and ordinary landlords had to pick up many kinds of non-farming jobs'.²⁰² In other words, to compensate for the loss of income, small and ordinary landlords had to work as wage labourers, while big landlords, as we mentioned, had already been businesspeople. Among those landlords who transferred their money into industrial and commercial activity, the investments were mostly operated by their children.²⁰³

Even when landlords invested in non-farming activities, it does not mean that the capital was put into productive industry. In 1957-58, there were many reports of land transfers.²⁰⁴ It was a kind of land speculation which should not be taken seriously as 'investment'. Such funds also became the source of the financial 'black' market in the countryside.

Thus a preliminary conclusion would be that after the reform, not a lot of landlords used the compensated money in industry or commerce. Some small and ordinary landlords entered business, but they did not compose the main part of the business class. The business class drew its recruits mainly from among the large landlords, and the small landlords' children.

²⁰⁰ See Theodore Reynolds Smith, *op.cit.*, p. 96.

²⁰¹ See Mao Yugang (毛育剛), *op.cit.*, pp. 146, 162; Wolf Ladejinsky, 'Agrarian Reform in Asia', *Foreign Affairs*, April, 1964.

²⁰² See Martin M. C. Yang, *op.cit.*, pp. 244-245.

²⁰³ See In Huang Dazhou's (黃大洲) survey, 53% of the investment was done by their children, 12% by brothers. See Huang Dazhou, 'Taiwan Nongdi Gaige du Nongcun Dizhu zhi Yingxiang' (台灣農地改革對農村地區之影響, The Influence of Land Reform on Landlords), in Lee Denghui (李登輝)(ed.), *Taiwan Nongdi Gaige dui Xiangcun shehui zhi gongxiang* (台灣農地改革對鄉村社會之貢獻, Contribution of Land Reform to Taiwan's Rural Areas), pp. 70-119.

²⁰⁴ A document of the Ministry of Economic Affairs reports that 'rich people feel depressed because they do not know how to use their capital. Depositing it in a bank will get little interest; loaning as usury is too risky; stocking speculative commodities is illegal; running a business has to pay high taxes....So the surplus

1.2.4 Farm Tenants

After the Rent Reduction Program, the standard of living of tenant farmers did not improve much. A survey conducted after the Program showed that the liability of the tenant farmers rose from 18.7% to 20.2%. Those tenants who did benefit from the policy spent most of their increased income on consumption (51.9%) due to poverty. Only 0.1% of the tenants invested in commerce.²⁰⁵ But the plummeting land price made it more affordable for them to buy their own land. Without the help of the Land-to-the-Tiller Program, 28,960 tenant families purchased 15,646 Jia of farm directly from landlords in 1953, which composed 6.2% of the tenanted land.²⁰⁶ The Land-to-the-Tiller Program helped 194,823 farming families to purchase 143,568 Jia of farm land offered by the government for resale in 1953.²⁰⁷ The percentage of tenant households was reduced from 36% in 1948 to 15% of the agricultural population in 1959. Tenanted land was reduced from 44% to 14% in the same period. It was a dramatic change in tenancy structures.

Though tenants were helped to become farm owners, their market situation in the first five years did not improve a lot. First of all, they had to pay a mortgage for the land for ten years. This meant that they were tied to the land for those ten years and did not have any surplus to invest in the land. They were like tenant-owners who paid the rent to the government instead of landlords. In fact, both Bernard Gallin's research in Hsin Hsing village and the Joint Commission on Rural Reconstruction survey in 1954 showed that the financial burden of the tenants who bought land increased because they had to pay a land tax and house tax, and the tax could not be reduced even if there were a natural disaster.²⁰⁸ Though the sources of income of tenant farmers and landlords were redistributed after land reform, it did not necessarily mean that tenant farmers obtained what the landlords lost. The government used a lot of methods to collect taxes, in order to secure the surplus from agriculture to finance its budget. According to Li Denghui's (李登輝, Lee Teng-hui) estimation, the landlords' share of agricultural income decreased from 25.19% in 1936-40 to 9.76% in 1950-55 to 6.26% in 1956-60, while the figures for non-landlords were

capital in rural areas begins to be used to buy land ...whose after-tax income is better than interest, and without any risk. The transfer of land becomes more frequent." See Hou K'un-hung, *op.cit.*, p. 744.

²⁰⁵ See Zhongguo Dizheng Yanjiusuo, *op.cit.*, p. 160.

²⁰⁶ See Tang Hui-sun, *op.cit.*, pp. 105, 137.

²⁰⁷ See Tang Hui-sun, *Ibid.*: p. 137.

67.08%, 77.18% and 81.43%, and for government and other public groups were 7.73%, 13.06% and 12.31% respectively.²⁰⁹ Apparently the government appropriated 41.0% of the income released from the landlords after land reform in 1950-55 and 24.2% in 1955-60.

After six years of the Land-to-the-Tiller Program, E. Stuart Kirby conducted a survey in 1959 on rural development which reported that 'according to local leaders' opinions, more and more farmers had to find non-farming jobs because of insufficient arable land and population pressure.²¹⁰ One trend was diminishing arable land per farm household.²¹¹ Official data showed that the households owning less than 0.5 hectare increased from 34% to 36%, while those owning more than 2 hectares decreased from 10.7% to 9.5% between 1956 and 1961.²¹² The size of the farm families was increasing in the 1950s and early 1960s because sets of rural sibling born at that time tended to be large: six or more were common.²¹³ The average persons in a farm household increased from 6.26 members in 1952 to 6.75 in 1962.²¹⁴

The result of insufficient land was either disguised unemployment in rural areas, or the creation of a large number of propertyless workers. Liu Jinqing estimated that in 1961 there were about a million potential surplus population in the agricultural sector, which was 44% of the total agricultural population.²¹⁵ But there were not a lot of industrial jobs at that time, so all the surplus population could do was to find part-time agricultural or industrial work, or to be a wage farmer. Yet part-time farming households decreased from 60% to 52% in the period, which implied there were few industrial work opportunities for the surplus population and that farmers had to put even more intensive labour into their own farm. At the same time, the number of wage farmers increased from

²⁰⁸ See Bernard Gallin, *Hsin Hsing, Taiwan: A Chinese Village in Change* (Berkeley: University of California Press, 1966).

²⁰⁹ See Lee Teng-hui, *op.cit.*, p. 83, Table 49.

²¹⁰ See Stuart E. Kirby, *op.cit.*, p. 75.

²¹¹ *Ibid.*: p. 70.

²¹² Original from *Taiwansheng Nongye Xuanyang Pucha Baogao* (Report on Farming Survey in Taiwan Province), 1956, Table 1, 3-2, 3-3; *Taiwansheng Nongye Pucha Zongbaogao* (Summary of General Agricultural Survey in Taiwan Province), 1961, Table 1, 2. Cited From Liu Jinqing, *op.cit.*, p. 350, Table 89.

²¹³ This data is from a personal communication from David Schak. The data was collected through his personal research.

²¹⁴ Ryozauro Minami (南亮三郎)(ed.), *Taiwan no Jinko to Keizai* (Population and Economy in Taiwan) (Tokyo: Ajia Keizai Kenkyusho, 1971), p.92, Table 6.

²¹⁵ See Liu Jinqing, *Ibid.*: p. 353.

0.7% to 4% of the total agricultural population from 1956 to 1961.²¹⁶

In summary, the newly arisen farm owners did not have much of a chance to be businesspeople in this period because, firstly, they had to pay a mortgage for ten years for the land they had just acquired; because, secondly, the increased income released from landlords was not totally transferred into their hands; and because, lastly, the increase of population exacerbated their burden, which required them to find supplementary jobs. With few opportunities, the most likely mobility path for them was to be a wage labourer in agricultural sector.

1.2.5 Employers and Self-Employed Workers

According to the 1956 Census, there were 86,650 employers, whose distribution in the primary, secondary and tertiary industry was 23,766 (27.42%), 29,353 (33.88%) and 33,531 (38.70%) respectively. The number of self-employed workers was 952,728, and the distribution among the three sectors was 720,673 (75.64%), 56,156 (5.89%) and 175,899 (18.46%) respectively. The employers composed 3.23% of the total labour force, while the self-employed were 35.5% in 1956.²¹⁷ Table 1.15 shows the number of employers and self-employed in the 1950s. The number increased gradually over the ten years.

Table 1. 15 Employers and Self-Employed in Industry, 1951-60 (per 1,000 Persons)

Industry Year	Primary	Secondary	Tertiary	Total
1951	581	64	161	806
1952	617	68	170	855
1953	648	71	179	898
1954	683	75	189	947
1955	717	79	199	995
1956	755	83	209	1047
1957	794	87	221	1102
1958	836	93	233	1162
1959	879	97	245	1221
1960	924	103	259	1286
1961	972	108	273	1353

Source: original data is from ILO, *Year Book of Labour Statistics*, 1967. Cited from Kato Hisanobu, *Taiwan no Rodoryoku Jinko* (Labour Force in Taiwan), in Minami Ryozauro (南亮三郎)(ed.), *op. cit.*, p.78.

²¹⁶ See Liu Jinqing, *op.cit.*, p. 350, Table 89.

²¹⁷ See The Taiwan Provincial Government, *A Summary Report on the 1956 Census*.

The employers' income in 1953 in the urban areas averaged NT\$27,271, about four times more than the average urban resident's income, and they belonged to the top 6% of total households (See Table 4.1).

Table 1.15 also shows that most of the non-farming self-employed were concentrated in tertiary industry. Usually a tertiary sector can absorb a huge number of disguised unemployed or marginally employed. It can accommodate landless farmers who had left their villages to find a job in an urban area. According to a survey conducted in urban Taiwan in 1952, 31.8% of the sampled families were self-employed. Though their annual income was 20% higher than the average income and close to a public servant's income, we have to take into account the diverse occupations in this category, which produced great income differences. For example, shopkeepers, drivers owning three-wheeled bikes or a wooden trailer, and a lot of marginal labourers were all counted as being in the same category. As Arthur F. Raper wrote, 'the self-employed is the result of surplus population. They cannot find any wage job, so they create these marginal jobs to survive. Most marginal labourers will be happy to accept any possible constant jobs'.²¹⁸ We can conclude that the self-employed category contained two income groups, one of which had some capital and ran a small shop or factory; the others were the marginal labourers who worked for themselves, but their incomes were unstable and meagre, and their status no more than that of a wage worker, and perhaps worse.

1.2.6 The Working Class

The number of employees increased steadily from 737,000 in 1951 to 1,222,000 in 1960. The percentage of wage labourers in the total labour force increased by only about 0.1% of the total labour force every year, from 35.8% to 36.8%. The work force's distribution among industries remained relatively stable, i.e., 20% in primary, 30% in secondary and 50% in tertiary industry.²¹⁹

The employees in primary industry were mainly tenants before land reform, farmers who did not own enough land to make a living after the reform, or cane-workers who had worked for the Taiwan Sugar Company. In 1952, half of the interviewed tenants had to

²¹⁸ See Arthur F. Raper, *op.cit.*, p. 145.

²¹⁹ Calculated from Kadoo Hisanobu, *op. cit.*, Table 7, 13.

work for others, while the percentage for landlords was only 25%.²²⁰ These hired farm labourers were not entitled to purchase landlords' land in the Land-to-the-Tiller Program, and their living conditions had deteriorated. The survey by Martin M. C. Yang noted that 72% out of 250 interviewed labourer households complained of this.²²¹ One reason why their living conditions deteriorated was that many landlords had had to sell their land and leave the farming business, and therefore no longer needed farm labourers. Their numbers increased from 0.4% of the agricultural labour force to 4% between 1956 and 1961, mainly due to insufficient land and increasing population.

The industrial workers' income was one third below the average income in urban areas (see Table 1.12). Mining, textiles and the metal machinery industry employed half of the workers, and so their conditions can be used to illustrate workers' situation in the period.

The monthly average wages in these three industries in 1953 were NT\$455, NT\$450 and NT\$439 respectively.²²² A KMT report observed that some mining companies could not pay wages on schedule, which meant many workers had to discount their 'wage card' up to 40% to borrow money for living expenses. The wages owed to workers amounted to four million five hundred thousand dollars.²²³ The accidental death rate in the coal mining industry in 1951 was 61 deaths per hundred million tons, while the figure in Japan was 24, and in the UK was only 2.3. Raper reported that only half of the workers had constant jobs, while the other half had to find any kind of temporary job.²²⁴

Almost 50% of the employees were in tertiary industry, and mostly in the service sector, which included street vendors, hairdressers, entertainers, housemaids, cleaners, etc. Most people in the sector were marginal labourers, and their jobs were only a means to survive in an urban area until they could find a job in manufacturing industry. This surplus population step by step was absorbed by the expanding manufacturing sector after Taiwan's economic take-off.

Since the income of the working class was so low, it was almost impossible for them

²²⁰ See Gaomindang Zhongyang Gaizao Weiyuanhui, *op.cit.*, p. 24, Table 4-8.

²²¹ See Martin M. C. Yang, *op.cit.*, p. 347.

²²² See Guomindang Zhongyang Weiyuanhui Sheji Kaohe Weiyuanhui, *op.cit.*, pp. 17, 73-74, 137-138. For the textile and metal machinery industries, I take the median as the average income because different factories had different average wages. Converted to annual average incomes, these figures were close to what Arthur F. Raper reported.

²²³ See *Ibid.*: pp. 17-18.

²²⁴ See Arthur F. Raper, *op.cit.*, p. 215.

to accumulate a lump sum of initial capital. But even though their market situation was very disadvantageous, this class provided a 'reserve army' of small businesspeople after the economic take-off. They utilised the skills they had learned in the factories to provide products through trade agencies to the world market.

1.3 Conclusion

We have observed some of the features of the postwar period which characterised the changed and unchanged parts of Taiwan society.

With the replacement of Japanese colonial government with mainlander Chinese, political power was strongly held in the hands of the newly arrived regime. The KMT enforced land reform policies after it fled to Taiwan, aiming to consolidate the party's legitimacy among peasants and to weaken the local elite's power. The landlord class vanished, and only large landlords were able successfully to transfer their capital into industry and to benefit from the reform.

The party state also benefited from the reform, politically and economically. The surplus it secured from the agricultural sector was directed toward financing its fiscal deficit, mainly in national defense. The small landlords, though they obtained a certain amount of compensation, did not enter business activity because of lack of a business skills, or because the compensation was too little to invest. Labourers and peasants obviously were too poor to go into any business requiring even a small amount of capital.

State power controlled the economic institutions, and thus good connections were a key to making any substantial profits in the 1950s, as we have seen from the development of the textile industry. International trade was mainly controlled through the foreign exchange rate system which favoured importers, who wanted to import as much as they could. Too much demand for foreign currency led to rationing, and this provided another method for the state to control businesspeople- and provided chances to participate in corruption at the same time.²²⁵

Under the regulated economy, there was not much chance for private capital to pursue maximum profits through market mechanisms alone. Either they made money under the protection of state power, or earned marginal profits by running a small shop. But after the reform of the foreign exchange rate system, plus many advantageous

²²⁵ See Liu Jinqing, *Ibid.*: p. 283, and my interview data.

international factors, Taiwan's businesspeople in both large and small firms rushed into trade. With the state's strong control of the international sector no longer possible, exports created a channel for those who had not had any chance for success in the 1950s.²²⁶ The flow of international capital in the 1960s from the United States and Japan created opportunities for assembly firms in Taiwan, which in turn produced backward linkage effects on local industries. But although there were good business opportunities to be grasped in the 1960s, the social structures formed in the 1950s would have certain effects on the life chances of the people occupying different economic positions. In the coming chapter we will see how different family backgrounds constrained educational opportunities, which in turn constrained one's occupational opportunities. We shall observe, too, who became the new small and medium-sized entrepreneurs.

²²⁶ See Zhou Tiancheng (周添城), *Quanli Bianchui de Zhongxiao Qiye* (SMEs in Peripheral, 權力邊陲的中小企業), in Taiwan Yanjiu Jijinhui (ed.), *Longduan yu Boxue—Weixuan Zuyi de Zhengzhi Jingji Fenxi* (*Monopoly and Exploitation—Political Economy of Authoritarian Rule, 壟斷與剝削—威權主義的政治經濟分析*) (Taipei: Taiwan Yanjiu Jijinhui, 1989) pp.97-118.

Chapter 2: Education and Social Mobility

2.1 Introduction

The relationship between a family's socio-economic status, the parents' education, and the child's education and occupational attainment is often probed in sociological studies. An obvious pattern is that the parents' social-economic status and education have a significant influence on their children's education which in turn affects their occupational attainment. Following this line of research, we can easily trace the mobility patterns of different classes.²²⁷

Oddly, the research on Taiwan businesspeople is normally divided into two fields: social stratification scholars tell us the general mobility patterns, but they do not explain why Taiwanese businesspeople adopt certain strategies instead of others to climb up the social ladder; and in particular, no-one previously has discussed the mobility patterns of small and medium-sized businesspeople in Taiwan.²²⁸ On the other hand, those who

²²⁷ Social Stratification is one of the biggest branches in sociology. The International Sociological Association has established a research committee for this theme. In this branch of sociology, one tradition is to probe the relationship between education, social origins and occupational attainment. See Donald J. Treiman, 'Industrialization and Social Stratification', in Edward O. Laumann (ed.), *Social Stratification: Research and Theory for the 1970s* (Indianapolis:Bobbs-Merrill, 1970), pp. 207-234; Hans-Peter Blossfeld and Yossi Shavit, 'Persisting Barriers: Changes in Educational Stratification in 13 Countries', in Yossi Shavit and Hans-Peter Blossfeld (eds.), *Persistent Inequality—Changing Educational Attainment in Thirteen Countries* (Oxford: Westview Press, 1993), pp.1-23; Peter M. Blau and Otis Dudley Duncan, *The American Occupational Structure*. (New York: Wiley, 1967); Pierre Bourdieu and Jean-Claude Passeron, *Reproduction in Education, Society and Culture* (Beverly Hills: Sage, 1977); Samuel Bowles and Herbert Gintis, *Schooling in Capitalist America* (New York: Basic Books, 1976).

²²⁸ See Kuanjeng Chen and Hsiu-Jen Jennifer Yeh, 'Social Structure at Work: The Effects of Educational Development on Educational Mobility in Taiwan'. Paper presented at *Conference on Social Stratification and Mobility: Newly Industrializing Economies Compared* (Taipei: International Sociological Association Research Committee 28, Institute of Sociology, Academia Sinica), pp. 123-150; Shu-ling Tsai and Heiyuan Chiu, 'Changes in Educational Stratification in Taiwan', in Yossi Shavit and Hans-Peter Blossfeld (eds.), *Persistent Inequality—Changing Educational Attainment in Thirteen Countries* (Oxford: Westview Press, 1993), pp. 193-227; Shu-ling Tsai, "Social Change and Status Attainment in Taiwan: Comparisons of Ethnic Groups", *International Perspectives on Education and Society*, vol. 2, pp. 225-256; Huang Yizhi (黃毅志), 'Taiwan Diqu Jiaoyu Jihui Bupingdengxing zhi Bianqian' (台灣地區教育機會不平等性之變遷, The Change of Inequality in Educational Opportunity), *Chinese Journal of Sociology* (中國社會學刊), vol. 18 (1995), pp. 243-73; Tsai Shuling and Haiyuan Chu (蔡淑玲, 瞿海源), "Bijiao Taiwan Ge Zuqun zhi Jiaoyu Qude" (比較台灣各族群之教育取得, Educational Attainment in Taiwan: Comparisons of Ethnic Groups), *Proceedings for Humanities and Social Sciences* (人文及社會科學), vol. 3, no.2 (1993): pp. 188-202; Yang Ying (楊瑩), *Taiwan Diqu Jiaoyu Kuozhan Guochenzhong Butong Jiating Beijing Zinyu Shoujiaoyu Jihui Chayi zhi Yanjiu* (台灣地區教育擴展過程中不同家庭背景子女受教機會差異之研究, *Effects of Educational Development on the Education Opportunities for Children of Different Sauce-*

conduct research on small and medium-sized businesspeople based on interviews or fieldwork almost never touch this topic of the relationship between parents' socio-economic background, education and occupation. They never analyse in detail who is more likely to become self-employed or an employer, though some of them have vague ideas about mobility paths.²²⁹ This chapter aims to make clear these mobility paths, and to offer some explanations as to why different types of people in Taiwan have opted for particular mobility paths.

In the first part of the chapter I will describe the general pattern of educational and occupational development in Taiwan, and will pay attention to the difference between Taiwanese and Mainlanders. In the second part, I will discuss educational development in postwar times, to discern some of the characteristics of the Taiwan education system in Taiwan, the role of the state and the ways in which a family's socio-economic background strongly influenced education. I will use path analysis to see these effects. Afterwards I will discuss why those who were who were less educated did not adopt collective strategies to improve their market situation. In the last section, I will review some hypotheses developed by other scholars on the phenomenon of 'opening one's own shop' in Taiwan.

2.2 Education, Occupations and Ethnicity

In the previous chapter we noted that most Mainlanders worked in tertiary industry, with Taiwanese in primary industry. Did the situation change after Taiwan's economic take-off in the 1960s? Let us see the distribution of these two groups in different industries.

economic Background) (Taipei: Taiwan Normal University, unpublished Ph.D. Dissertation, Department of Education, 1988).

²²⁹ See Xie Guoxiong (謝國雄, Shieh Gwo-shyong), "Heshou bian Toujia--Taiwan Zhizaoye zhong de Jieji Liudong" (Black-hands Becoming Their Own Bosses: Class Mobility in Taiwan's Manufacturing Sectors, 黑手變頭家—台灣製造業中的階級流動), *Taiwan Shehui Yanjiu Jikan* (台灣社會研究季刊, *Taiwan: A Radical Quarterly in Social Studies*), vol. 2, no.2 (summer 1989), pp. 11-54; Chen Jie-xuan (陳介玄), *Xieli Wangluo yu Renji Wangluo--Taiwan Zhongxiao Qiye De Shehui Jingji Fenxi* (協力網絡與人際網絡—台灣中小企業的社會經濟分析, *Subcontracting and Personal Networks--social economic analysis of Taiwan's small and medium-scale enterprises*) (Taipei: Lianjing Chubanshe, 1994); Donald DeGlopper, "Artisan Work and Life in Taiwan", *Modern China*, vol. 5, no. 3 (July 1979), pp. 283-316; Alice Amsden, "Big Business and Urban Congestion in Taiwan: the Origins of Small Enterprise and Regionally Decentralized Industry", *World Development*, 1991 (Sep.), vol. 19, no.9, pp.1122-35; Hill Gates, "Ethnicity and Social Class", in E. M. Ahern and Hill Gates (eds.), *The Anthropology of Taiwanese*

To exclude the effects of the older generation on occupational distribution, I will examine the occupations of those people who entered the formal labour market after 1960. Table 2.1, which I have devised through a computer analysis of raw survey data, shows people who had their first formal jobs in the 1960s, 1970s and 1980s. 50%, 51% and 54% of these people entered secondary industry, and 38%, 27% and 45% tertiary industry in the 1960s, 1970s and 1980s respectively. Such a trend reflects the fast industrialisation in the period from 1952 to 1992: the share of agricultural output in National Domestic Product was reduced from 32.2% to 3.5%, while industrial output increased from 19.7% to 41.4% and tertiary output increased from 48.1% to 55.1%.²³⁰ The fast growing industrial sector, especially the manufacturing sector, absorbed most of the new labourers.

Table 2. 1 Newly Recruited Labour Force in Industry, by Ethnicity, 1960-1990

	Primary	Secondary	Tertiary	Total
1960-69				
<i>Taiwanese</i>	40	154	115	309
(%)	12.9	49.8	37.2	100.0
<i>Mainlander</i>	1	12	14	27
(%)	3.7	44.4	51.9	100.0
Total(%)	12.2	49.4	38.4	100.0
1970-79				
<i>Taiwanese</i>	15	341	151	507
(%)	3.0	67.3	29.7	100.0
<i>Mainlander</i>	0	30	43	73
(%)	0.0	41.1	58.9	100.0
Total(%)	2.1	51.1	26.7	100.0
1980-89				
<i>Taiwanese</i>	9	245	176	430
(%)	2.1	57.0	40.9	100.0
<i>Mainlander</i>	0	42	62	104
(%)	0.0	40.4	59.6	100.0
Total(%)	1.7	53.7	44.6	100.0

Source: I have calculated this using a computer, upon the computerized Raw data of the *General Survey of Social Change in Taiwan, 1992*. The research was conducted by the Institute of Ethnology, Academia Sinica under the directorship of Professor Kuo-shu Yang and Hei-yuan Chiu. About the survey, see appendix 2.

From this table it can be seen that more Mainlanders went into tertiary than secondary industry as their first formal job, and the first formal job for Taiwanese centred in secondary industry. Table 2.2, which I have also devised from raw interview survey data, shows at what age they obtained their first formal jobs. The Taiwanese working age was 3.4 years younger than the Mainlanders'. Two possibilities might explain why Mainlanders entered the formal labour market later than Taiwanese: one is that many of them could not find a formal job after they graduated from school, so they either remained unemployed or at best found informal jobs which made them late to enter the formal labour market; a second possibility is that they stayed in school longer than Taiwanese. Table 2.3 shows how many years of schooling the two groups received.

Table 2. 2 Age of First Job, by Ethnicity (1960-1990)

1960-69	Male	Female	Average	Cases
Taiwanese	18.6(314)	16.9(158)	17.7	314
Mainlander	24.5 (13)	18.0 (14)	21.1	27
1970-79				
Taiwanese	20.2(210)	18.6(303)	19.2	513
Mainlander	22.0 (31)	19.9(42)	20.8	73
1980-89				
Taiwanese	21.4(197)	20.8(243)	21.1	440
Mainlander	22.4 (52)	21.1 (53)	21.7	105

Source: As Table 2.1.

Table 2. 3 Years of Schooling of Those Who Had a Formal Job, by Ethnicity (1960-90)

1960-69	Primary	Secondary	Tertiary	Average
Taiwanese	6.16(40)	7.16(154)	8.84(115)	7.77(309)
Mainlander	0.00 (1)	7.29 (12)	11.54 (13)	9.13 (26)
1970-79				
Taiwanese	7.80(15)	9.08(341)	11.52(151)	9.77(507)
Mainlander	0.00(0)	11.32 (30)	12.70 (43)	12.13(73)
1980-89				
Taiwanese	11.06(9)	11.03(245)	12.41(176)	11.60(430)
Mainlander	0(0)	11.62 (42)	13.31 (32)	12.63(104)

Source: As Table 2.1.

Table 2. 4 Year of Schooling by Date of Birth and by Ethnicity

Year of Birth	1926-1935	1936-1945	1946-1955	1956-1965	1966-1975	Average
Taiwanese	4.32(222)	5.73(379)	8.53(529)	10.80(645)	11.73(253)	9.05(2028)
Mainlander	8.08 (66)	7.27 (22)	12.70(361)	12.89(112)	12.52 (62)	11.42 (323)
Difference	3.76	1.54	4.20	2.09	0.79	2.37(2351)

Source: As Table 2.1.

Obviously the Mainlanders were consistently more highly educated than the Taiwanese throughout the postwar period, though the difference narrowed over time. Their higher education also explains why most of them had a job in tertiary industry. Though a supervisor in secondary industry requires more education than a stock clerk in tertiary industry, and hawkers and pedicab drivers in the tertiary industry are not much educated, tertiary industry usually requires a higher education. After controlling for ethnic background, I found that years of education largely account for the different rate at which they entered the different economic sectors.²³¹ When this educational difference is taken into account, the difference in the chance of the two ethnic groups entering tertiary industry narrows considerably (compare Table 2.1 and 2.3). Even for those Taiwanese entering secondary or tertiary industry, their education was lower than Mainlanders, as Table 2.3 shows.

Table 2.5 shows us the ethnic distribution in the category of self-employed (including employers) at different times. The Mainlanders' percentage is continuously lower than their sample distribution over the past forty years. In other words, they tended to work as an employee instead of running a shop or factory. If the more highly educated are more likely to be successful in business because of their knowledge, why did the more educated Mainlanders not have a higher probability to become self-employed or an employer? I will explain this later.

From the survey data, we can see three features. Firstly, the Mainlanders' education is consistently higher than the Taiwanese. Secondly, the proportion of Taiwanese in the self-employed or employer category is much higher than Mainlanders. Thirdly, the Mainlanders' occupations centred on white-collar jobs. Why did the socio-economic patterns not change over the past half century? In the following sections, I will discuss how the occupational distribution was affected by political, economic and social forces and the effects of education.

²³¹ The Pearson chi-square probability is less than 0.000 for both ethnic groups, which means that people with different education years have different possibility to enter different industries.

Table 2.5 Self-employed Ethnic Distribution in Secondary and Tertiary Industries (1950-90)

	Sample's Ethnic Ratio (Taiwanese: Mainlander)	Ethnic ratio in non-primary Industry	Self-employed
1950s	92.3:7.7 (980:82)	85.4:14.6 (205:35)	92.2:7.8 (71:6)
1960s	89.3:10.7 (1296:156)	83.5:16.5 (444:88)	91.6:8.4 (142:13)
1970s	90.3:9.7 (1772:190)	87.8:12.2 (870:121)	91.9:8.1 (227:20)
1980s	84.7:15.3 (2040:368)	83.1:16.6 (1230:245)	93.3:6.7 (278:19)

Source: see Table 2.1.

Notes:

1. The sample here is pooled from four sources: when respondents married, what were the occupation of her/himself, his/her father, spouse and spouse's father. Therefore I got two generations' occupational distribution. One problem of this pooling is that the sex ratio in the sample is 3:1, which means females are under-represented. But if we consider that the female labour-force participation rate was always lower than males, it is not a big problem to use the data.
2. Numbers in parentheses show the numbers of sampled informants: Taiwanese/Mainlanders.

2.3 Education After the War

According to human capital theory, education is a kind of capital that one can accumulate to facilitate finding a job in the labour market.²³² What one spends in education will be rewarded through a higher income or prestige in a future job. One question with this approach is the question of who pays the cost. But obviously it is not the educated individual who pays the cost, but instead, her/his family and the government. Educational inequality can be reproduced through the effects of socio-economic inequality, as many findings show.²³³

In other words, we have to distinguish between three different kinds of educational costs: one is the opportunity cost of getting an education, another is the tuition fee paid by the family, and the third is the cost covered by the government. Meritocracy is not the only principle in the education market. Social and political forces intervene in the market, which might reduce or reinforce the effects of personal merit. In this section I will discuss three features that characterised postwar education in Taiwan: firstly, the schools were hierarchically ranked; secondly, educational opportunity was unevenly distributed between Taiwanese and Mainlanders because of unequal socio-economic status; thirdly, education was tightly under the government's control.

²³² See Gary Becker, 1975, *Human Capital*. Chicago: University of Chicago Press.

2.3.1 The Hierarchically Ranked School System

Among the hierarchically ranked schools at the tertiary education level, National Taiwan University has always been regarded as the best university, then Qinghua or Zhengda, then other public and private universities. High schools' reputations are based on their 'examination passing rate' to university. Such a hierarchically ranked school system resembles the Japanese system, but is more monocentric because of the selection method and the state's education policy.²³⁴

In the entrance exam, those students from the few 'superstar' schools²³⁵ have a higher probability to enter the next educational level. For example, the overall pass rate to tertiary education in 1981 is about one-third of applicants, but the pass rate of the elite Jianguo senior high school is over 95%. In 1971, only two thirds of the graduating junior high school students could enter senior high school or junior college. The other third had to enter the labour market. It is more difficult to enter a tertiary institution. In 1981, thirty-four out of one hundred and eighty-seven academic senior high schools (18.2%) did not have any student successfully pass the university examination. Under 10% of the graduating students in seventy-six schools passed the exam. In other words, 58.8% of total academic high schools do not function as preparatory university training schools, despite the claimed goal for academic senior high schools set by the government.²³⁶

Because of the stratified school system, a vocational education becomes the 'least' prestigious in the educational system.²³⁷ For those who could enter high school, their first

²³³ See note 228.

²³⁴ See Ronald Dore, *The Diploma Disease* (London: George Allen & Unwin, 1976), pp. 46-50. In Japan, different universities individually test students on the same day, so sometimes the 'second-best' university could get 'higher marked' high school students. But in Taiwan, all universities jointly test high school students on the same days with the same questions. After the publication of the results, students can choose their university according to their results on the test.

²³⁵ It is so called 'Mingxing Xuexiao' (明星學校), which is defined as the passing rate to the next educational level.

²³⁶ See Zhang Chunxing (張春興), 'Minguo Sanshijiunian Yilai Xuexiao Jiaoyu de Fazhan yu Jiantao' (民國三十九年以來學校教育的發展與檢討, Evaluation of the Development of Schooling Education after 1950), in Zhongguo Luntan Bianji Weiyuanhui (中國論壇編輯委員會)(ed.), *Taiwan Diqu Shehui Bianqian yu Wenhua Fazhan* (台灣地區社會變遷與文化發展, *Social Change and Cultural Development in Taiwan Area*) (Taipei: Zhongguo Luntan Zazhi, 1985), pp. 407-408.

²³⁷ David Schak suggests that children from poor families generally prefer a vocational education as it provides them with occupational skills. This point exactly conforms to what I say here that poor socio-economic origins produce poor educational performance, and then the poor student correctly chooses to enter a less prestigious vocational school. Poor children might prefer a vocational education subjectively, but objectively they are not able to enter more the prestigious academic school.

choice was normally an academic school. Junior vocational school was the last resort of those who could afford further study. A survey conducted by the Ministry of Education in 1971, the first year of graduates from a nine-year compulsory education, showed that 85.21% of the graduating junior high school students in Taiwan wished to study further. Most of them would have liked to study in an academic senior high school, and few preferred a vocational junior college or high school.²³⁸ In 1984, the two 'best' vocational senior high schools in the Taipei area could recruit only 40% of their planned students. The situation in private vocational senior high schools was worse. There were over seven thousand vacancies in these private vocational schools.²³⁹

This hierarchy of schools reflects occupational prestige. A student graduating from a more prestigious school could get a more prestigious job. From this perspective, education becomes a pre-selection mechanism for the business community to determine who could enter which jobs and positions. Thus, young people spend all their energy in trying to enter a higher and 'better' school.²⁴⁰

To compete with others in the 'educational industry', students have to start their 'preparation' as soon as possible.²⁴¹ Family socio-economic background becomes important from the start. In colonial times, education was a privileged mobility path for upper-class Taiwanese. After the war, more and more children could go to primary and junior high school, as Table 2.6 shows. Elementary education was no longer a 'luxury', but it was still hard for students to enter junior high school before the nine years of compulsory education was promulgated in 1968, partly because of insufficient school capacity and partly because of the family's economic difficulties.

In 1955 and 1956, Xinzhu county and Gaoxiong city experimented in accepting every student who wanted to study in junior high school without taking any entrance exam. The survey reported that only 55% of the graduating students in Xinzhu and 62% in Gaoxiong continued their studies.²⁴² The report did not say why 40% of the pupils did

²³⁸ See Sun Bangzheng (孫邦正), *Liushinian Lai de Zhongguo Jiaoyu* (六十年來的中國教育, *Chinese Education in Last Sixty Years*) (Taipei: Zhengzhong Shuju, 1971), p. 300.

²³⁹ See Zhang Chunxing, *op. cit.*, p. 410.

²⁴⁰ The situation is the same in Japan. It is criticised by Japanese scholars as 'Schoolism' (gakkore, 學校歷) but not 'credentialism' (gakure, 學歷).

²⁴¹ A famous commercial advertisement is: '別讓你的孩子輸在起跑線上' (Don't let your children lose from the starting line).

²⁴² See Wang Yaquan (王亞權), 'Fazhan Chuji Zhongdeng Xuexiao Fangan zhi Shishi—Xinzhu

not want to study further, but from my interview data, every interviewee from that generation who today owns a SME emphasised that his family was too poor to afford for them to go to junior high school. Some of them had to work as an apprentice and at the same time went to a supplementary junior high school at night. Table 2.7, which I have devised from raw survey interview data, shows the average years of education by date of birth. Obviously the relationship between father's occupation and years of education is the same as in colonial times. It shows that in the 1950s and 1960s it was still not so easy for a poor family to provide their children with a higher education. The official data of the entrance rate into junior high school in 1955 was only 39%.²⁴³ As can be seen, a farmer's and manual worker's children lost out from the start. After prolonging compulsory education from six to nine years, the difference narrows, though they are still less educated.²⁴⁴

Table 2. 6 Development of Elementary Schools, 1944-1959

	Number of Schools	Number of Students	Enrollment Rate
1944	1,097	898,424	71.31
1945	1,053	850,097	80.01
1947	1,160	855,821	79.02
1949	1,199	892,758	79.07
1950	1,231	906,950	79.98
1953	1,300	1,060,324	87.75
1955	1,446	1,244,029	92.33
1957	1,597	1,480,557	94.61
1959	1,757	1,777,118	95.44

Source: From Yu Shu-lin, 'Jin Wushi Nian Lai Guomin Jiaoyu zhi Yanjin' ('The Evolution of National Education in Last Fifty Years'), pp. 343-344; 348-349. In Zhongguo Jiaoyu Xuehui (ed.), *Jin Wushi Nian Lai zhi Zhongguo Jiaoyu (Chinese Education in the Last Fifty Years)* (Taipei: Fuxing Shuju, 1977), pp. 322-359.

Gaoxiong Liang Xian Ziyuan Shengxue Shiyan Qingxing--' (發展初級中等學校方案之實施—新竹、高雄兩縣自願升學實驗情形, 'The Implementation Plan of Developing Junior High School--the Experimental Situation of Voluntary Further Study in Xinzhu and Gaoxiong Counties'), in Shi Jiansheng et al. (施建生等)(eds.), *Zhongguo Jiaoyu Xiankuang, (中國教育現況) (Chinese Education Updated, 2)* (Taipei: Zhonghua Wenhua Chuban Shiye Weiyuanhui, 1958), p. 350.

²⁴³ See Yu Shulin (余書麟), 'Jin Wushi Nian Lai Guomin Jiaoyu zhi Yanjin' ('The Evolution of National Education in Last Fifty Years'), in Zhongguo Jiaoyu Xuehui (ed.), *Jin Wushi Nian Lai zhi Zhongguo Jiaoyu (Chinese Education in Last Fifty Years)* (Taipei: Fuxing Shuju, 1977), p. 350.

²⁴⁴ In Japan, over 75% of Tokyo University students' fathers are from professional and managerial background, while among those who could not go to university, the main obstacle is the high tuition fee. A private university might charge as much as 1.5 million yen a semester.

Table 2. 7 Education by Father's Occupation and Date of Birth: 1946-75

Years of Birth	1946-55	1956-65	1966-75
Professional, technical and related workers; Administrative and managerial workers; Clerical and related workers	13.36(81)	13.08(124)	12.63(67)
Sales workers; Service workers	10.02(100)	11.68(142)	12.54(69)
Agricultural, animal husbandry and forestry workers, fishermen and hunters	7.29(262)	9.83(240)	10.94(69)
Production and related workers transport equipment operators and labourers	7.86(99)	10.80(181)	11.57(74)
Average	8.81(542)	11.06(687)	11.91(279)

Source: See Table 2.1.

Notes:

1. Based on informant's father's occupation when s/he was fifteen years old.
2. The informants include Taiwanese and Mainlanders.
3. Marginal workers, e.g., first-time job seekers are housewives, are excluded from the table.
4. Figures in parentheses show numbers of informants.

The combination effect of the hierarchical schooling system and socio-economic status was the emergence of 'after school lessons'.²⁴⁵ A rich or above average income family could send their children to private elementary and junior high schools famous for their 'examism'. They only teach the subjects that will be tested and ignore all other activities.²⁴⁶ Another way was to hire a private tutor after school. In Taiwan in 1995, the private tutoring wage per month, four hours a week, was about US\$230. In 1994 the official minimum wage was only US\$558 a month, and the per capita income per month was US\$936. An average family could not afford this extra education fee. Another cheaper way is sending children to cram schools²⁴⁷, which is more common for middle-income families, but the 'learning' effect will be less evident.

2.3.2 Educational Differences Between Taiwanese and Mainlanders

Was the difference in educational achievements between Taiwanese and Mainlanders over the past forty years institutionalised discrimination, or just the results of differences

²⁴⁵ It is called 'buxi' (補習, lessons after school) or 'ebu' (惡補, evil lessons after school).

²⁴⁶ See Sun Bangzheng, *op. cit.*, p. 203.

²⁴⁷ In Taipei, the most famous cram school area centres on Nanyang street near the Taipei railway station. One can see numerous students in uniforms coming here after school.

in socio-economic family background? I will review the evidence and then discuss the causes of the persistent differences.

Table 2.8 shows the changes of occupational prestige scores by ethnicity. A Taiwanese father's occupational prestige increased steadily from 29.96 in the 1950s to 39.76 in the 1980s. The Mainlanders' stayed close to a level close to 50. In short, Mainlanders' fathers enjoyed higher social prestige than Taiwanese, but the difference was progressively reduced over time. In the following section, I will confine myself to examining the effects of the educational standing of persons born in the 1940s to the 1960s, who comprised the major part of the labour force after the 1960s.

Table 2. 8 Socio-Economic Index of Occupational Status, by Ethnicity

Date of Birth	1936-45	1946-55	1956-65	1966-75
Taiwanese	29.96 (325)	32.62 (479)	35.51 (599)	39.76 (237)
Mainlander	46.05 (19)	57.19 (53)	50.24 (100)	50.46 (54)

Source: see Table 2.1.

Notes:

1. This index is coded according to the international socio-economic index of occupational status developed by Harry B. G. Ganzeboom, Paul M. De Graaf and Donald J. Treiman. See their work "Standard International Socio-Economic Index of Occupational Status", *Social Science Research* (Academic Press, Inc), vol. 21, 1992, pp. 1-56.
2. I use father's occupation when the informant was fifteen years old. Usually the occupation was steady over the life-span.
3. The index used here is 'minor group' scores instead of unit group scores because some occupations coded in the survey are not shown in Ganzeboom's index table. The score range is from lowest 17 (agricultural and animal husbandry workers) to 85 (jurists).
4. Figure in parentheses is number of informants.

From the winter of 1965 through the spring of 1966, Richard W. Wilson conducted research at some elementary schools in Taiwan. He evaluated the socio-economic status of the children at three schools: a city public school, an urban private school and a rural public school. Fathers of the children at the urban public school generally held medium-to-low occupational positions with corresponding incomes, while at the private school they enjoyed medium-to-high incomes and at the rural public school low-to-medium incomes.²⁴⁸ The status classification, though based on children's vague responses and the

²⁴⁸ See Richard W. Wilson, *Learning to be Chinese: The Political Socialization of Children in Taiwan* (Massachusetts: the M.I.T. Press, 1970), pp. 149-152.

author's own subjective estimates, did reflect the status difference of different schools. Normally the educational facilities in urban areas are better than in the countryside, and those in the private elementary schools better than in the public schools. The private elementary schools are usually the so-called 'superstar schools'.

The ethnic ratio (Mainlander to Taiwanese) in the three schools was 47:53, 92:8, and 40:60 respectively. The private schools mainly enrolled Mainlanders and their fathers' occupational status was 'medium-to-high'. Wilson's description is in agreement with the class structure we observed in the second chapter, where I argued that the Mainlanders (except for the soldiers or veterans) held better positions in the state bureaucracy and state enterprises or ran a business in the 1950s.

The most 'competent' students, as was earlier noted, could enter the academic high schools. A survey by Stephen M. Olson in 1968 showed that the numbers of Mainland students in one municipal academic senior high school was much higher than at a private academic and commercial-vocational school (see Table 2.9). The Jianguo (建國) school is the 'superstar school' in the Taipei urban area because only those who get the highest scores in the entrance exam could enroll. Those who failed to enter the municipal senior high schools would attend private academic schools, and the Yanping (延平) school is ranked in the middle of the hierarchy. The Yuda (育達) private commercial-vocational school is ranked as 'not a good school' compared to the other two schools if we use the criterion of examination marks. If we look at the student's father's education, it was highest in respect to the municipal academic, then the private academic and private commercial-vocational.²⁴⁹ A correlation between ethnicity and father's education in the table is easy to see. In the Jianguo academic senior high school, 60% of the students were Mainlanders, and in Yuda commercial-vocational senior high school 86% were Taiwanese. Fathers' education in Jianguo was 50% tertiary educated, while the figure for Yuda was only 5.4%. The private academic senior high school Yanping was in the middle. Obviously the effect of ethnic socio-economic differences could be seen in junior high school.

²⁴⁹ See Stephen M. Olson, 'The Inculcation of Economic Values in Taipei Business Families', in W. E. Willmott (ed.), *Economic Organisation in Chinese Society* (Stanford: Stanford University Press, 1972), pp.

Table 2.9 Characteristics of Middle-School Sample, Taipei, April 1968

Native Place and Educational Background	Name and Type of School			
	Yanping private academic	Jianguo municipal academic	Yuda private vocational	Total or Average
Total Number in Sample (grades 10 and 11 only)	192	227	224	643
Native Place				
Taiwan	77.10%	39.20%	86.20%	66.90%
Mainland	21.90%	60.80%	13.40%	32.70%
No information	1.00%	100%	100%	100%
Father's Education				
College or above	21.90%	49.30%	5.40%	25.80%
Higher Secondary	33.90%	27.80%	17.00%	25.80%
Lower Secondary	13.50%	7.50%	23.20%	14.80%
Primary or less	23.20%	11.50%	46.40%	27.20%
No Information	7.30%	3.90%	8.00%	6.40%

Source: See Stephen M. Olson, 'The Inculcation of Economic Values in Taipei Business Families', in W. E. Willmott (ed.), *Economic Organisation in Chinese Society* (Stanford: Stanford University Press, 1972), p.267, Table 1.

Entering a 'better' academic senior high school meant a better chance to enter university. A survey conducted by the Stanford Institute in 1961 showed 37% of the students graduating during 1957 and 1959 from universities were born in Mainland China (N=850), while the graduating students from senior vocational high school were only 6% Mainlander (N=1994).²⁵⁰

The statistical survey of education of Taiwan Province revealed the same situation. In 1967, 'when Mainlanders constituted about 14% of the total population and probably a somewhat lower proportion of school-aged youth, almost a quarter of the island's non-vocational high school students, 30% of its college students, and almost 40% of those enrolled in the top-ranking national universities were Mainlanders'.²⁵¹

Tables 2.10 and 2.11, which I again derived from raw national survey material, show the effects of ethnic, demographic and stratification factors on education and

261- 295. I have changed his Wade-Giles into Pinyin.

²⁵⁰ See Meiguo Jiazhou Shidanfo Yanjiusuo (Stanford Research Centre, California, USA), *Jiaoyu yu Fazhan--Zhonghuaminguo Jingji Fazhan Guocheng zhong Jiaoyu Jihua zhi Renwu (Education and Development--the Role of Educational Planning in Republic of China's Economic Development Process)* (Taipei: Council for Economic Planning and Development, 1962), p. 128.

²⁵¹ See Sheldon Appleton, 'The Social and Political Impact of Education in Taiwan', *Asian Survey*, vol. 16, no. 8 (1976) p. 706.

occupational attainment. Table 2.10 suggests that ethnicity, at least at first glance, seems to be an important factor affecting one's educational achievement, even after including in demographic variables, i.e., gender and date of birth. But after I put in the stratification variables, i.e., fathers' and mothers' education, its effect was reduced sharply from 2.24 years to 0.79. This means that the total effect of ethnicity on education is that the Mainlander on average was 2.61 years more educated than Taiwanese, but the indirect effect, i.e., from the demographic effect (0.37) and parents' educational background (1.45), contributes most to the total effect.²⁵² If we include the variable of father's occupation, which contributes 0.36 to educational attainment, then the ethnicity variable becomes insignificant. In other words, the 'obvious' ethnic cleavage phenomenon in educational attainment is in fact caused by stratification variables. From Table 2.4 we see that the educational difference between Taiwanese and Mainlander was narrowing, and Table 2.8 also shows the occupational prestige difference narrowing. We can expect that accompanying the improvement of the Taiwanese populace's socio-economic status, the ethnic educational difference would be gradually eliminated. This finding is contrary to Lin Zhongzheng (林忠正) and Lin Heling's (林鹤玲) finding in 1991, both of whom claimed that there is no sign to show the educational achievement difference had diminished.²⁵³

People without higher educational credentials have to enter lower prestige occupations. Table 2.11 shows the effect of different variables on occupational attainment. As in Table 2.10, ethnicity seems at first sight important to one's occupational prestige. The prestige score difference is 8.76, which is the total effect of ethnicity on occupational prestige. After putting in demographic variables, its effect is reduced only a little. But after I add the variables of parents' education and father's occupation, the ethnic variable and demographic variables both become insignificant. Yet all these variables together can explain only 24% of the total variations. If I include one's own education in the regression equation, R square increases from .24 to .42, i.e., almost

²⁵² About the decomposition of effects, see Duane F. Alwin and Robert M. Hauser, 'The Decomposition of Effects in Path Analysis', *American Sociological Review*, vol. 40 (Feb 1975), pp. 37-47.

²⁵³ See Lin Zhongzheng and Lin Holin, 'Taiwan Diqu Gezucun de Jingji Chayi' (Economic Difference Among Different Ethnic Groups in Taiwan Area), in Zhang Maogui (張茂桂) et al, *Zucun Guanxi yu Guojia Rentong* (*Ethnic Relationships and National Identification*) (Taipei: Yejiang Chubanshe, 1993), p. 132.

doubles, and parents' education becomes insignificant. This means that one's occupation status is very highly correlated with education. With each additional year of education, her/his occupational prestige score increases 2.11 points. The direct effect of parents' education diminishes to insignificance because its effect on an informant's occupational attainment is transmitted through one's own education. So we can say that the occupational difference between Taiwanese and Mainlanders would be eliminated if the gap in the educational difference between the two groups diminishes in future.

Table 2.10 Regression Analysis of Different Variables on Educational Attainment (1991-1992)

	Education Attainment			
Ethnicity	2.61	2.24	0.79	0.43(n.s)
Sex	--	-1.72	-1.76	-1.71
Dob1	--	1.27	0.89	0.88
Dob2	--	4.13	3.24	3.09
Dob3	--	6.1	4.81	4.64
Dob4	--	6.85	5.03	4.85
Father's education	--	--	0.30	0.21
Mother's education	--	--	0.22	0.18
Father's occupation	--	--	--	0.04
R square	0.04	0.33	0.50	0.5

Source: see Table 2.1, notes.

Notes: 1. n.s means not significant at 1% level.

2. Father's occupation is his occupation when informant was fifteen years old. The occupational status score is calculated from Ganzeboom *et. al.*
3. I have excluded the Aborigines in the samples. Ethnicity is coded into Taiwanese and Mainlander.
4. DOB means date of birth. DOB1 are those people born between 1936 and 1945. Dob 2 are those people born between 1946 and 1955. Dob 3 are those people born between 1956 and 1965. Dob 4 are those born after 1965.

Table 2. 11 Regression Analysis of Different Variables on Occupational Prestige Scores (1991-1992)

	Occupation Prestige Scores			
Ethnicity	8.76	8.6	2.33(n.s)	1.62(n.s)
Sex	--	-1.53(n.s)	-1.91(n.s)	1.11(n.s)
Dob1	--	2.19(n.s)	0.03(n.s)	-1.69(n.s)
Dob2	--	8.1	3.62(n.s)	-2.67(n.s)
Dob3	--	9.67	4.01	-5.15
Dob4	--	10.24	2.75(n.s)	-6.78
Father's education	--	--	0.32	-0.09(n.s)
Mother's education	--	--	0.61	0.23(n.s)
Father's occupation	--	--	0.26	0.15
Own Education	--	--	--	2.11
R square	0.04	0.08	0.24	0.42

Source: See Table 2.1, notes.

Notes: See footnotes in Table 2.10.

Then why does father's occupation have a significant influence on children's occupations? My analysis of the survey of 1992 shows that 61.8% of the respondents got their first jobs through personal networks, e.g., were introduced by family, friends or relatives, while only 38.2% found their jobs through an official employment office, newspaper advertisements or by passing a state examination.²⁵⁴ If so, father's social network could be an important source to find one's first job, and there is a tendency that the social network is based on similar social background. If one's child is incorporated into her/his network, s/he might find a similar job to her/his father. This question will be probed in detail in Chapter Five.

2.3.3 The State's Educational Policy

The ethnic, demographic and stratification factors explain 50% of the variation in one's education, as Table 2.10 shows. In other words, another 50% of the variation is not explained by these factors. These can be attributed to one's own efforts or talent, or the pre-existent state education policy, etc. In modern society, the state plays an important role in educational planning, which sets the constraints of the educational opportunities

of its people. Education is incorporated into the modern political system to achieve certain 'national goals' set by the state, e.g., language policy or economic policy, which will affect the development of education.

The KMT-controlled educational system after the second world war has had two notable features: (i) the government has used education as a means to control people's thinking; and (ii) educational expansion has been based on economic planning.

Education is the easiest and cheapest means to control ideology. The KMT regime tried to legitimise its rule as the sole 'representative' of China,²⁵⁵ and it felt it had to tightly control any 'heretical' discourse challenging its claims.²⁵⁶ Private education was seen as a potential 'challenger', so the establishment of new schools was put under strict control. This policy meant that although there was a high social demand for higher education throughout the postwar period, only a few private schools were allowed to be set up. The government argued that there was not sufficient finances to expand higher education, but at the same time did not allow the private sector to do so. It was not a problem of any lack of private capital. For example, after an 'open door' policy was proclaimed to set up private junior colleges in 1964, forty-one new private colleges were set up in five years, increasing the numbers in Taiwan from eight to forty-nine.²⁵⁷

This earlier policy of limiting higher education was aimed at political and ideological control, but its side-effect was to intensify the competition between students. Though the enrolment rate of graduating elementary school students in junior high school increased

²⁵⁴ The figure excludes those unknown, others, self-employed or home-workers which constitutes 18.4% of the sample. Calculated from Qu, Hai-yuan, *op. cit.*, 1992.

²⁵⁵ See Masahiro Wakabayashi (若林正文), 'Yoyu suru Naisen' (溶解suru内戦, Dissolving Civil War), in Masahiro Wakabayashi (ed.), *Taiwan--Tenkanki no Seiji to Keizai* (台灣—轉換期no政治to經濟, Taiwan: Politics and Economy in Transition) (Tokyo: Tahata Shoten, 1987), p.368.

²⁵⁶ The 1950s was called 'white terror decade', for all leftist intellectuals were either put in jail or purged. One famous anti-KMT magazine in the 1950s was shut down due to its proposal to have a new party. In the 1960s, two famous writers Li Ao (李敖) and Bo Yang (柏楊) were also put in jail in the name of 'intention of subvert the government'. See Dai Guohui (戴國輝), *Taiwan Zongti xiang* (台灣總體相, General Image of Taiwan) (Taipei: Yuanliu Chubanshe, 1991), pp.171-173.

²⁵⁷ See Jiaoyubu Jiaoyu Nianjian Bianzhuang Weiyuanhui (教育部教育年鑑編撰委員會, Education Annual Editorial Committee, Education Ministry), *Zhonghuaminguo Jiaoyu Nianjian* (中華民國教育年鑑, Education Annual--Republic of China) (Taipei: Zhengzhong Shuju, 1976), p. 677. Also see Chen Shufen (陳淑芬), 'Guangfuhou Taiwan Diqu Gaodeng Jiaoyu Shexiao Zhengce zhi Tantaoy' (光復後台灣地區高等教育設校政策之探討, Research on School Set-up Policy for Higher Education in Postwar Taiwan Area), in Lai Jeh-hang and Huang Chun-chien (賴澤涵, 黃俊傑) (eds.), *Guangfuhou Taiwan Diqu Fazhan Jingyan* (光復後台灣地區發展經驗, The Development Experience of Taiwan in the Post-war Era) (Taipei: Sun Yat-sen Institute for Social Sciences and Philosophy, Academia Sinica, 1991), p. 231,

from 33% in 1953 to 62% in 1967, the year before the introduction of nine years' compulsory education, the absolute number of 'failed' students in the junior high school exams increased steadily from 89,367 to 134,076.²⁵⁸ 'After-school lessons' became pervasive, which the education ministry in 1976 admitted was 'one of the most serious problems in recent educational development'.²⁵⁹ A rich family in this competition was more 'competitive' because it could better afford the after-school lessons. Mainlanders generally held better occupations, so they could better afford their children's 'extra education cost'. But the Mainlanders' children not only were helped by their higher socio-economic family status; they were also heavily subsidised by the government. All children of state employees received exemptions from tuition fees and were in line for scholarships at all educational levels,²⁶⁰ while other students had to pay tuition fees above the junior high school level. Civil servants, mainly Mainlanders, benefited the most from the subsidy. From 1950 to 1974, only 59% of the newly recruited civil servants who passed the state examination were Taiwanese, while 41% were Mainlanders.²⁶¹ The Mainlanders received a disproportionate educational subsidy from the government compared to its 15% of the total population warranted. At the same time, a special tax, which was based on agricultural income, was levied to finance educational expenditure.²⁶² In other words, through the government's financing policy, educational resources flowed from a disadvantaged class, the peasants, to a privileged class, public servants. No wonder Shu-ling Tsai and Hei-yuan Chiu found that a 'farming background exerts a negative impact on educational attainment at all [school-level] transitions'.²⁶³

Another important educational influence was related to economic-oriented planning.

appendix 2.

²⁵⁸ See Jiaoyubu Jiaoyu Nianjian Bianzhuang Weiyuanhui, *Ibid.*: pp. 227-228.

²⁵⁹ *Ibid.*: p. 227.

²⁶⁰ See Tsai Shu-ling and Chiu Hei-yuan, 'Changes in Educational Stratification in Taiwan', in Yossi Shavit and Hans-Peter Blossfeld (eds.), *Persistent Inequality—Changing Educational Attainment in Thirteen Countries* (Oxford: Westview Press, 1993), p. 218.

²⁶¹ These are the statistics for the 'advanced level exam' (高等考試, Gaodeng Kaoshi). The ratio for the 'general level exam' (普通考試, Putong Kaoshi) for civil servants is 79:21. The ratio of Mainlanders was considerably higher than its population ratio. See Kaoxuanbu (考選部, Examination Department), *Zhonghuaminguo Liushisannian Kaoxuan Tongji* (中華民國六十三年考選統計, *Examination Statistics, 1974*) (Taipei: Kaoxuanbu, 1974), pp. 32-33; 52-53.

²⁶² See Wang Zhiting (汪知亭), *Taiwan Jiaoyushi* (台灣教育史, *Taiwan Education History*) (Taipei: Taiwan Shudian, 1959), p. 176. As we have seen in Chapter One, the KMT government used 'extraction' policy to squeeze agricultural surplus for industrial development in the 1950s and 1960s.

²⁶³ See Tsai Shu-ling and Chiu Hei-yuan, *op. cit.*, p. 218.

In the 1950s and 1960s, vocational education was the mainstream education philosophy all over the world, which emphasised its function in promoting economic development. Taiwan was not exceptional.²⁶⁴ The decisive factor for the government to develop vocational education was the report of the Stanford Research Institute in 1962, which proposed that Taiwan increase its skilled labour supply to promote rapid economic development.²⁶⁵ Since then, entrance to academic schools was strictly controlled. On the one hand, the government encouraged the private sector to establish vocational schools to relieve the demand for higher education, and on the other the government set a target that adjusted the academic and vocational senior high student ratio from 80:20 to 30:70.²⁶⁶ This former ratio was successfully reversed to 32: 68 in 1988.²⁶⁷ It was a dramatic change. The effect of this economic-oriented policy is not hard to imagine: fewer and fewer students could study at academic senior high schools, which in turn intensified the competition among the students and among junior high schools to succeed in the students' race to climb into academic senior high schools. Table 2.9 shows that more of the Mainlander students studied in academic senior high schools, while Taiwanese students 'fell' into vocational senior high schools. Using a computer to analyse the raw statistics of 'A General Survey Data of Social Change in Taiwan, 1992-93', I have derived the ethnic ratio at different educational levels showing the highest degree earned (Taiwanese: Mainlanders): at academic senior high school, 76:24; junior college, 79:21; vocational senior high school, 87:13. The figure deflates the number of Mainlanders in academic senior high school because those who entered university or senior college are not counted in. The ethnic ratio in university is 74:26. The overall demographic ratio is 86.2: 13.8.

Education itself was sufficient to function as the main mechanism to reproduce socio-economic inequality in a competitive education market.²⁶⁸ The state's policy could

²⁶⁴ See Yang Yirong (羊憶蓉), *Jiaoyu yu Guojia Fazhan: "Taiwan Jingyan" de Fanxing* (教育與國家發展: 台灣經驗的反省, Education and National Development: Reflections on 'Taiwan Experience'), in Lai Jeh-hang and Huang Chun-chieh (eds.), *op. cit.*, p. 136.

²⁶⁵ See Jiaoyubu Jiaoyu Nianjian Bianzhuang Weiyuanhui (教育部教育年鑑編撰委員會), *op. cit.*, p. 628.

²⁶⁶ The ratio of academic and vocational school students in 1962 was 8:2. See Gai Zhesheng (蓋浙生), *Taiwan Renli Ziyuan yu Jiaoyu Fazhan zhi Guanxi Yanjiu (Research on the Relationships Between Human Resources and Educational Development in Taiwan)* (Taipei: Jiixin Cement Cultural Foundation, 1969), p. 135, Table 55.

²⁶⁷ See Yang Yirong, *op. cit.*, p. 149.

²⁶⁸ See Samuel Bowles and Herbert Gintis, *Schooling in Capitalist American: Educational Reform and the*

have reduced the negative effects of socio-economic differences, but in Taiwan, educational policy, on the contrary, reinforced the inequality.

2.4 The Patterns of Mobility Paths in Taiwan

Workers of low prestige occupations have to 'help themselves' to become upwardly mobile. In different countries labourers adopt different strategies to improve their market conditions. As seen, Taiwanese in the past forty years were less educated than Mainlanders. Under this condition, how did they use different strategies to improve their market situations? In the following pages, I will concentrate on the self-employed in non-primary industry. I will sketch a general employment history, and then discuss the occupational category of self-employed, which contains employers who hire workers, as well as petty bourgeoisie such as small shop-keepers or taxi-drivers, who do not hire workers. Section 2.5 will discuss the structural influences on mobility patterns.

Education often determines one's life-time occupation. Table 2.12 shows the change in occupational prestige scores in one's work life. We can see that the scores remained relatively stable, though most of the people were 'upwardly' mobile a little. This suggests that social stratification in Taiwan was largely determined in school, with students classified through the examination system. Their future occupations were largely determined when they attained different levels of schooling.

Table 2.12 Occupational Prestige Scores by Education in Different Life Histories

Occupation Prestigious Scores	First Job	Job when Married	Job when Interviewed
No Schooling	25.96	22.85	27.61
Self-learning/ dropout	31.25	29.84	32.64
Primary	33.73	33.08	35.39
Junior High School	37.69	38.43	39.86
Senior High School	44.79	46.76	48.04
Junior College	52.78	54.2	56.15
University	60.06	61.19	61.08
Postgraduate	69.68	67.63	69.66
Cases	1794	1448	1740

Source: see Table 2.1.

Note: Regarding the occupational prestige scores, see Table 2.8, note 1.

Table 2.13 provides a general sketch of employment history. The most distinguishing feature is that the percentage of self-employed increased over time. The typical employment history of the self-employed is: find a job in the labour market, and when you marry, become a housewife (for females) or set up a small shop (for males). This tendency occurs across generations.

Table 2.13 Changes of Employment in One's Working History

% of different kinds of employment	First Job	Job when Married	Job when Interviewed
Self-employed	5.8 (7.0)	12.4 (15.5)	21.5
Work for Others	64.6(78.3)	40.8(50.9)	45.2
Work for Family	8.6(10.5)	9.5(11.8)	6.7
Housewife	1.3 (1.5)	15.7(19.6)	19.8
No Job	--	1.4 (1.8)	3.3
Retired	--	--	2.7
Student	--	0.4(0.5)	--
Unknown or unmarried	19.7 (---)	19.7 (---)	0.7
Cases	2377	2377	2377

Source: see Table 2.1, notes.

Notes: The figure in parenthesis is the percentage excluding unknown or unmarried.

Table 2.14 shows the education and age background of the self-employed category. The number of self-employed in the non-agricultural sectors increases as time passes, but the self-employed in primary industry does not change much after marriage. Regarding the relationship between education and self-employed in the non-agricultural sectors, the higher the education the lower the percentage of that educational level who work as self-employed, as Table 2.15 shows. The effects of education on different kinds of employment do not differ for different dates of birth.²⁶⁹ Regarding the ethnic distribution, 23.2% of the Taiwanese (excluding those self-employed in primary industry) are self-employed, while only 11.1% of the Mainlanders are self-employed. In other words, those Taiwanese with less education are more likely to be self-employed over time.

²⁶⁹ I used the log-linear model to check the effects, and the effects of different educational levels on employment do not differ for different dates of birth.

Table 2.14 Education and Age of Self-Employment at Three Different Periods of Life

	Primary			Junior HS		
	First Job	Married	Interviewed	First Job	Married	Interviewed
--1945	59(31)	116(78)	144(77)	6(3)	11(6)	18(4)
1946-55	19(9)	54(19)	76(22)	7(5)	14(3)	24(3)
1956-65	1(1)	9(4)	17(5)	8(4)	16(7)	37(10)
1966-75	1(0)	1(0)	1(0)	1(1)	5(0)	7(0)
Total	80(41)	180(101)	238(104)	22(13)	46(16)	86(17)

	Senior HS			Junior College		
	First Job	Married	Interviewed	First Job	Married	Interviewed
--1945	1(0)	5(1)	16(4)	0	0	0
1946-55	6(1)	11(1)	32(3)	2(0)	7(1)	10(1)
1956-65	10(3)	23(3)	65(7)	3(1)	4(0)	17(0)
1966-75	7(1)	4(1)	19(1)	1(1)	0	3(1)
Total	24(5)	43(6)	132(15)	6(2)	11(1)	30(2)

	Tertiary			Subtotal		
	First Job	Married	Interviewed	First Job	Married	Interviewed
--1945	1(0)	4(1)	6(2)	67(34)	136(86)	184(87)
1946-55	3(0)	5(0)	9(0)	37(15)	91(24)	151(29)
1956-65	0	5(1)	7(0)	22(9)	57(15)	143(22)
1966-75	2(0)	1(0)	3(0)	12(3)	11(1)	33(2)
Total	6(0)	15(2)	25(2)	138(61)	295(126)	511(140)

Source: As in Table 2.1.

Notes: The figure in parenthesis is the number in primary industry.

Table 2.15 Percentage of Self-employed and Employed in the Non-Agricultural Sector, by Education

	Self-employed	Employed
Primary and less	32.3	52.9
Junior High School	28.6	61.4
Senior High School	23.0	69.3
Junior College	14.0	81.0
Tertiary and more	12.6	83.6
Cases	369	1031

Source: As in Table 2.1.

Notes: 1. % of the same level of education working as self-employed or employed.

2. The samples exclude primary industry.

What sorts of jobs are held by the self-employed in Taiwan? My computer analysis of the sample data of the survey of 1991-92 reveals 370 self-employed in non-primary industry. 142 out of these 370 (38.4%) hired workers to work for them, and so could be

called small employers.²⁷⁰ But most of the non-agricultural self-employed just ran a small shop of their own. 116 out of 370 (31%) are wholesale or retail trade owners, 35 (9.5%) are street vendors, 19 (5.1%) are taxi-drivers, 18 (4.9%) are restaurants owners. In other words, more than 50% of the non-agricultural self-employed are earning their living based on their *ex ante* labour²⁷¹ which depends on the market situation.

The employers do not have a different mobility path from the person who runs a small shop of his own. Most of their first jobs were as employees (71.8% of employers [N=142] and 64.3% of the small shopkeepers [N=221]), but by the time they married the percentage who remained employees was reduced to 37.3% and 35.7% respectively, while the percentage of self-employed increased from 11.3% to 40.8% and 12.2% to 32.6% respectively.

To hire workers or not has nothing to do with age, while a clear pattern is that the more educated rose through the private sector into circumstances where they are more likely to hire people. Of those who have less than six years of education, only 27.3% hire labourers, and the figure increases to 32.8% (junior high school), 47.8% (senior high school), 53.6% (junior college) and 63.6% (tertiary). This is consistent with the survey done in 1996 by the Directorate-General of Budget, Accounting and Statistics. This found that employers are more educated than self-employed workers. Among the employers, 38% were educated fewer than nine years, 36% are senior high school educated, and 26% received junior college and above education, while the figures for the three educational levels of self-employed workers are 44%, 34% and 22% respectively.²⁷² The number of workers that the employers hire is 12.3, and the figure of the self-employed workers is only 2.8.²⁷³

²⁷⁰ Here I use Erik Olin Wright's definition. See Erik Olin Wright, *Class, Crisis and the State* (London: New Left Books, 1978), Chapter 2.

²⁷¹ See Claus Offe, 'The Political Economy of the Labour Market', in *Disorganized Capitalism--Contemporary Transformations of Work and Politics* (Cambridge: Polity Press, 1985), p. 28.

²⁷² Computed from Directorate-General of Budget, Accounting and Statistics, Executive Yuan (行政院主計處), *Zhonghua Minguo Bashiwu nian Taiwan Diqu Renli Ziyuan Diaocha Tongji Nianbao* (中華民國八十五年台灣地區人力資源調查統計年報, *Yearbook of Manpower Survey Statistics, Taiwan Area, ROC, 1996*) (Taipei: Directorate-General of Budget, Accounting and Statistics, 1997), pp.164-165, Table 52.

²⁷³ Computed from Directorate-General of Budget, Accounting and Statistics, Executive Yuan, *Yearbook of Manpower Survey Statistics, Taiwan Area, ROC, 1996*, p.171, Table 57.

Even though the less educated Taiwanese are more likely to become self-employed, their occupations centre on low prestige jobs like street vendors, taxi-drivers or small shop owners. One possibility is that the less educated do not have sufficient human capital to learn new technologies to compete, so their work is mostly dependent on subcontracting. Those who were medium educated could not get good employment, or be promoted high in an organisation, but they were able to learn new technologies with the help of what they learned in high school. I found that those interviewees who emphasised competitive production technologies were usually those with vocational senior high school credentials or higher, while those who talked about their *guanxi* with others were usually less educated. Here it seems that education played a role in promoting economic success.

We can make the following points:

1. Occupational distribution has been largely determined by education, and the education system in Taiwan functions as a mechanism that reproduces social-status inequality.
2. People from different educational levels have different mobility paths. The general mobility pattern in Taiwan is: for the less educated to try to get a job in the labour market, and when possible, to be self-employed in a marginal, low prestige business; while for the higher educated, to get a prestige job as an employee and to stay within that organisation, relying upon the hope of promotion.
3. I distinguish employers from the others in the category of self-employed. The data show that generally employers are better educated than the petty-bourgeoisie.
4. Mainlanders are more educated than Taiwanese, and they are less likely to be self-employed. The ethnic cleavage in occupational distribution is basically the result of educational effects and *guanxi*, and the distinction between these factors was observed in 2.3.2.
5. Obviously the prevalence of the small and medium-sized enterprises in Taiwan is not induced by any 'cultural mentality'. Different educational levels set the general limitations to upward mobility, and for the less educated, one of the means to overcome this limitation is to withdraw one's labour power from the wage market and to open their own small business.

2.5 Structural Constraints on Collective Action

We are interested, among other things, in why the less educated, manual labourers adopted the so-called 'de-class-in-itself' strategy instead of trying improve their market situation collectively. I will discuss the structural factors which influence the strategies that manual labourers in Taiwan adopt.

2.5.1 Education as a kind of ideological control

Education is usually considered as a means to break socio-economic inequality. Yet the accepted values regarding upward mobility have direct and indirect social control effects. The direct effect is that the examination selection system is widely accepted as legitimate without any questioning. People are apt to believe that it is the most fair and efficient way to select elites to manage society, without any prejudice against poor families, because every student has to answer the same questions.

Such a widely accepted belief that educational opportunity is equally provided through such exams, plus the belief that a higher education is important for career success,²⁷⁴ produces an indirect effect: those who could not enter higher education are deemed failures in a competitive society. This is not only the social image of the less-educated, but also their self-image. The social and individual images are congruent because the less educated could only find low-prestige jobs, which reinforces the negative image of the less-educated. In the survey of 1992, 78% of the interviewees were not satisfied with their own educational performance.²⁷⁵ Such a self-image is produced within the ethos in which one receives a formal education. In Taiwan the teachers mark everything, including 'morality', on a hundred percent scale, and those getting higher marks are always regarded as more intelligent, hard-working and a model for every student. In junior high school, almost every school classifies students into two different sections: a front section which is established to 'whip' students to pass the senior high school examination, and a back section, which is said to accommodate those students

²⁷⁴ The survey shows that 89% of the informants think high education is 'very important' and 'important' for career success. There is no attitude difference between higher educated or less educated. See Qu Haiyuan, *op. cit.*, 1992, p. 232.

²⁷⁵ See Qu Haiyuan, *Taiwan Diqu Shehui Bianqian Jiben Diaocha Jihua (A General Survey of Social Change in Taiwan, 1991)* (Taipei: Ethnology, Academia Sinica, 1991), p.307.

who do not want to go on studying.²⁷⁶ According to my computer analysis of the 1992 national survey data, among those whose highest degree was an academic high school degree, 21% had been placed in the 'back section', and the figure for vocational senior high school was much higher, 32%, while for those who got a university degree, it was only 2.0%.²⁷⁷

In sum, education is recognised as a mechanism to distinguish the 'most capable' people from the 'incapable', on the one hand, and to legitimise the existing social hierarchy, on the other. One case shows this popular attitude towards the function of education. A friend explained to students at a junior college why the percentage of Mainlanders attending tertiary education is much higher than Taiwanese. She asked students to answer the question in a final examination. Even after they had been told the reason by her in class, a lot of students replied: because Mainlanders are more clever than Taiwanese.

People without higher educational credentials have to try to find alternatives if they seek to be upwardly mobile. Since the education system in Taiwan is not flexible, it is almost impossible for someone who is out of the school system to go back again to school, so almost no one can achieve upward mobility via this route. For example, one interviewee's daughter observed that her father, fifty-five years old, told her that his first aspiration had been to study at university, but under financial stress at that time, he had had to give up the expectation. He said that since it was impossible to attain a higher education, the alternative way open to him to raise his status was to strive to make money. But even if one has such a motivation to discard his or her inferior social and material status, why did s/he and others adopt individualistic measures instead of collective action? We have to examine the mechanisms which excluded the possibility of collective action.

2.5.2 The State-Controlled Labour Regime

Taiwan was ranked as an authoritarian regime before its democratisation in the mid-1980s.²⁷⁸ Under this condition, any collective action, including a labour movement, was

²⁷⁶ The back section of a school is called 'fangniu ban' (放牛班) which means let cows eat grass by themselves without any help. Usually no student in the section is interested in studying because they are socially defined as 'bad, backward and hopeless students'.

²⁷⁷ Calculated from *A General Survey of Social Change in Taiwan, 1992*.

²⁷⁸ See Edwin A. Winckler, 'Elite Political Struggle, 1945-1985', in Edwin A. Winckler and Susan

viewed as a threatening force to 'subvert' social stability and was kept under surveillance and suppressed.²⁷⁹

The methods to control the labour movement in Taiwan had been established in the period of fighting against the Chinese Communists, and after the KMT retreated to Taiwan the implementation of martial law consolidated the party-state controlled labour regime.²⁸⁰ A lot of laws were implemented to control labour, including a Trade Union Law, the Labour-Capital Disputes Law, the National Mobilisation Law, the martial law, Provisions for Controlling Agriculture, Industry and Commerce in the Emergency Period...etc. The most important means was to preempt workers' collective-dispute rights. According to clause six of the Trade Union Law, the industrial labourers over twenty years old in an area or factory could organise an industrial or occupational trade union, but up to 1988, 85% of Taiwan factories employed fewer than thirty workers, and the labourers in these firms were excluded from the right to organise a union.²⁸¹

Even when labourers were eligible to organise a union, the administrative bureaucracy could cooperate with employers to prevent the establishment of an 'unpopular' union. In one case, the labourers working in a shoe-manufacturing company wanted to organise a union, and after they had submitted the application form, the government office in charge of the matter notified the company immediately, and the company organised pro-company workers to organise a new union. The office forged the date of receipt to invalidate the first group because in one company only one union was allowed to be set up. Besides this arbitrary administrative power, the law forbade any coalition of local level unions. Local level unions needed to be subordinated to a higher level union, which was always controlled by the party-state.²⁸²

Greenhalgh (eds.), *Contending Approaches to the Political Economy of Taiwan* (Armonk: M.E. Sharpe, 1988), pp.151-171.

²⁷⁹ See Wang Jenn-hwan (王振寰), Fang Xiau-ding (方孝鼎), 'Guojia Jiqi, Laogong Zhengce yu Laogong Yundong' (國家機器, 勞工政策與勞工運動, State, Labour Policies and Labour Movement), *Taiwan Shehui Yanjiu Jikan (Taiwan: A Radical Quarterly in Social Studies)*, pp.9-14.

²⁸⁰ See Xu Zhengguang, *Cong Yihua dao Zizhu: Taiwan Laogong Yundong de Jiben Xingge he Qushi (從異化到自主: 台灣勞工運動的基本性格和趨勢, From Alienation to Independence: Basic Characters and Trend of Taiwan Labour Movement)*, paper presented at the conference 'Social Movements' held in Qing Hua University, 1988, p. 4.

²⁸¹ See Wang Hong-zen (王宏仁), *Zhanhou Taiwan Siren Duzhan Ziben zhi Fazhan (戰後台灣私人獨佔資本之發展, The Development of Private Monopoly Capital in Postwar Taiwan)*, unpublished Master thesis, Graduate School of Sociology, National Taiwan University, 1988.

²⁸² See Zheng Lulin (鄭陸霖), *Taiwan Laodong Tizhi de Jiexi: Jiegou Lianjie de Guandian (台灣勞動體*

Because Taiwan was a one-party state, the state administration was in fact controlled by the party, and orders from the party were ranked higher than administrative rules.²⁸³ For example, Gaoxiong fishermen submitted an application to organise a union, which was ratified by a government office, but the party disagreed, which caused disputes between fishing labourers and the government office for several years. So, too, there was a KMT party cadre in every large enterprise, located in the personnel office, to supervise labour/management relations.²⁸⁴

Through these kinds of control, trade unions in Taiwan lost any independent power to strive for labourers' welfare. Instead they sometimes became a periphery organisation of the party-state to control society. If working conditions became unbearable, or one's income remained low, one could do nothing but leave one's employment in order to find one's own way.

2.5.3 Social Network Controls

Besides the widely accepted ideology of futuristic orientation, which means the belief that one would be successful if s/he works hard,²⁸⁵ society needs more subtle control mechanisms to forestall any discontent among the disadvantaged classes. Party-state control is obviously a kind of precautionary means to bring social discontent under strict surveillance, but another more effective and less cost-consuming means is to mobilise social networks to drain off the discontent.

As we have seen, in Taiwan most people seek their jobs through personal networks. Under this situation, all labour-capital conflict is easily transformed into 'personal' relationships that can be mediated by friends, family or relatives. A case is the strike

制的解析：結構連結的觀點，*Analysis of Taiwan Labour Regime: Structural Articulation Viewpoint*), unpublished Masters thesis, Graduate School of Sociology, National Taiwan University, 1988. Michael Hsin-huang Hsiao, 'The Labor Movement in Taiwan: A Retrospective and Prospective Look', in Denis Fred Simon and Michael Y. M. Kau (eds.), *Taiwan: Beyond the Economic Miracle* (Armonk: M.E. Sharpe, 1992), p.155.

²⁸³ See Joseph Bosco, 'Taiwan Factions: Guanxi, Patronage, and the State in Local Politics', *Ethnology*, vol. 31, no.2 (1992), p.174.

²⁸⁴ See Xu Zhengguang, *op. cit.*, p. 5.

²⁸⁵ In a survey of 1985, only 9.1% of the informants disagreed with the statement that 'if one bears hardships, s/he will be successful'. 45.5% strongly agreed, 27.2% very strongly agreed and 18.1% agreed with the statement. See Zheng Weiyuan (鄭為元), *Gaodu Chengzhang Xia Taiwan Renmin de Jingji Taidu (The Economic Attitudes of Taiwan People Under High Growth)* (Taipei: Juliu Tushu Gongsi, 1990), p.39, Table 4.1.

against the Far Eastern Chemical Enterprise in May 1989. Many workers had got their jobs in the company through the help of relatives or friends, and during the strike period, some workers had to resist the pressure from their parents and relatives persuading them to retreat from joining the strike.²⁸⁶ Another case involved workers who joined an independent union and came under a lot of pressure from parents and the friends who had introduced them to work in the company: 'In the process of labour-capital conflict, the employer mobilised all social relations surrounding the union leaders to press them to stop fighting. Besides their parents, the main pressure came from those friends who had introduced them to work here'.²⁸⁷ Such a social network plays a key role in preventing the formation of collective class consciousness; in other words, the social networks individualise the workers, and if there is any successful collective action organised by labourers, it must go beyond the social network.

If the conflict escalated into collective action, the local politicians would intervene in the conflict. Usually the businesspeople had good relationships with local politicians. Local politicians and factions are formed on the basis of social networks, especially in rural areas,²⁸⁸ and they would be asked to mobilise their social networks to 'de-mobilise' the involved parties.

In his research on social protests in Taiwan in the 1980s, Wu Jiemin (吳介民) found that local factional politicians (mainly representatives from the city, county, and rural market towns) played key early roles *vis a vis* collective actions. They intervened in the collective actions through mediation or on-the-spot consultations. The social conflicts were set in the context of patron-clients networks which offered a negotiation 'pipeline' for the protesters and company, and for the protesters ? the local government. Such a

²⁸⁶ See Xia Linqing (夏林清), 'Zhan Shang Bagong Diyixian--You Xingdong Zhuti de Jiaodu Kan 1989nian Yuanhua 5yue Bagong Kangzheng de Fasheng ji Yingxiang' (站上罷工第一線—由行動主體的角度看1989年遠化5月罷工抗爭的發生及影響, On the Frontline of a Strike--The Emergence and Effects of the Strike in Far Eastern Chemical Enterprise in May 1989 from the Perspectives of Acting Agent), p. 257. In 'You Shiwu Quxiang dao Shehui Shijian--Youguan Taiwan Laogong Shenghuo de Diaocha Baogao' (由實務取向到社會實踐—有關台灣勞工生活的調查報告, *From Practical Orientation to Social Practices--Reports on Taiwan Labourers' Life*) (Taipei: Zhang Laoshi Chubanshe, 1993), pp. 241-288.

²⁸⁷ See Xia Linqing, 'Yige Zizhu Gonghui Kangzheng Licheng de Anli Diaocha Baogao--Jiegouxing Chongtu yu Geren Xuexi' (一個自主工會抗爭歷程的案例調查報告—結構性衝突與個人學習, A Case Study on the Resistance History of an Independent Union--Structural Conflicts and Individual Learning Process), in *Ibid.*: p. 217.

²⁸⁸ See Bruce J. Jacobs, *Local Politics in a Rural Chinese Cultural Setting: A Field Study of Mazu*

patron-client network could function because the protesters and the company were afraid of harassment from the intelligence agency, and they therefore preferred the local politicians, whom they were more familiar with, to 'serve the people'.²⁸⁹ As James C. Scott has observed, 'the effect of machine rule under universal suffrage is to submerge growing collective policy demands with immediate payoffs, thereby retarding the development of class-based political interests among the lower strata'.²⁹⁰

From the above analysis, we can understand why workers in Taiwan preferred to adopt the strategy of 'de-class-in-itself' rather than the strategy of 'class-for-itself' to improve their disadvantaged situation. Paid employees comprised 67.5% of the total labour force in 1996,²⁹¹ but almost every collective problem became transformed into an individual problem or became smothered through the three mentioned social mechanisms. Politically, the state administrative and policing apparatus preempted the emergence of any possible collective action. Socially, the social networks, mainly through kin networks and local factions, could 'demobilise' any collective action.

The ultimate effect was that whenever a labour-capital conflict erupted, one of the first resolutions that came to mind was to 'leave the place'. A survey done in 1992 shows that one out of five workers had changed their job in the past three years, and the average frequency was 1.34 times. The less one was educated, the more frequently one changed jobs.²⁹² Among the paid employees in the private sector, 4.4% wanted to change their job, while the figure for self-employed workers was only 2.06%, and only 1.76% of government employee wanted to change their jobs.²⁹³ Among the surveyed unemployed with work experience, 42% left their job because of dissatisfaction with the previous job,

Township, Taiwan (Canberra: Contemporary China Centre, 1980), pp.78-82.

²⁸⁹ See Wu Jiemin (吳介民), *Zhengti Zhuanxingqi de Shehui Kangyi—Taiwan 1980 Niandai* (政體轉型期的社會抗議—台灣1980年代), *Social Protests in the Transition of Regime—Taiwan in the 1980s*, unpublished Masters thesis, Graduate School of Political Science, National Taiwan University, 1990, pp. 80-82, 130-131, 134-135.

²⁹⁰ See James C. Scott, *Comparative Political Corruption* (N.J.: Englewood Cliffs, 1972), p. 151.

²⁹¹ Computed from Directorate-General of Budget, Accounting and Statistics, Executive Yuan, *Yearbook of Manpower Survey Statistics, Taiwan Area, ROC, 1996*, pp. 2, 51.

²⁹² Those received primary education changed jobs 1.42 times in the past three years, and the figures for junior high school, vocational senior high school, academic senior high school, college and university are 1.38, 1.37, 1.35, 1.24 and 1.20 respectively. See Directorate-General of Budget, Accounting and Statistics, Executive Yuan, *Zhonghua Minguo Bashiyinian Taiwan Diqu Gongzuo Jingyan Diaocha Baogao* (中華民國八十一年台灣地區工作經驗調查報告, *Report on the Work Experiences Survey in Taiwan Area, ROC, 1992*) (Taipei: Directorate-General of Budget, Accounting and Statistics, 1993), pp. 66-67, Table 25.

²⁹³ *Ibid.*: p. 126, Table 38.

and 70% of these dissatisfied workers were from the private sector.²⁹⁴ When wages or working conditions were really unsatisfactory, workers simply retreated from the labour market to become self-employed.

2.6 Thesis on 'the Boss Island'

Is the mobility path of small and medium-sized entrepreneurs in Taiwan unique as compared to other countries? We can check this in terms of two aspects: fathers' socio-economic background and educational attainment. Table 2.16 shows the socio-economic background of small business owners in three countries.

We notice, firstly, the bulk of small business owners are recruited from the lower-middle social strata in all three societies, but the percentage of those from the lower-middle class in Taiwan (59.7%) is the highest among the three. Secondly, the pattern of distribution between Taiwan and Hong Kong is closer than between Taiwan and Britain. Thirdly, the occupational distribution of businesspeople's fathers in Taiwan is almost the same as the occupational distribution of the total Taiwanese population (the figure in parenthesis). From this comparison, we can consider the question: is small business largely a 'safety net' for children from the upper classes, or is it largely an upward mobility channel for those from lower strata?

The high percentage of small business owners from lower-middle class families in Taiwan might reflect a specific economic development stage. The labour force in primary industry was reduced from 56.1% in 1952 to 17.0% in 1986. So it is not surprising that the occupations of most of the informants' fathers were in primary industry. The similar pattern in Taiwan and Hong Kong support this argument.

More than 50% of the businesspeople's fathers were farmers and self-employed, and only 9.9% (Taiwan) and 12.9% (Hong Kong) were from employer, managerial or professional background, but in Britain, the figure from the upper class was 31.7%. In Germany, 29.3% of small business owners' fathers were businesspeople, and 16.1% of their mothers were businesswomen.²⁹⁵ In short, the social background of European small

²⁹⁴ Computed from Directorate-General of Budget, Accounting and Statistics, Executive Yuan, *Yearbook of Manpower Survey Statistics, Taiwan Area, ROC, 1996*, p.212, Table 70; p.231, Table 81.

²⁹⁵ See Heinz Klandt, 'Trends in Small Business Start-up in West Germany', in Robert Goffee and Richard Scase (eds.), *Entrepreneurship in Europe -- the Social Process* (London, New York, Sydney: Croom Helm, 1987), p. 36, note 9.

business owners is quite different from Taiwan and Hong Kong. In Europe, a larger proportion of business founders are from business families than would be expected from chance, while in Taiwan, the opportunity for children from lower-middle strata is not less than for the upper strata, though the children of employers and the self-employed have a slightly higher chance to run a business of their own.

Table 2.16 Small Business Owners' Socio-Economic Background (%)

SEI of father	Taiwan (1991-92)	Britain (1984)	Hong Kong (1987)
Employer	6.4(3.7)		4.8
Manager	2.1(2.0)	29.4	1.6
Professional	1.4(1.3)	2.3	6.5
Self-employed	18.9(12.7)	6.1	36.7
Upper non-manual	2.8(4.9)		
Lower non-manual	7.1(7.1)	17.3	16.5
Manual	16.7(16.7)	28.5	8.1
Farmer	35.9(40.2)		19.0
Other	8.5(11.3)	16.4	6.8
N=	281(2377)	214	248

Sources:

1. Taiwan: The General Survey of Social Change in Taiwan, 1991-92, as disaggregated by myself.
2. Britain: David Goss, *Small Business and Society* (London and New York: Routledge, 1991), Table 3.1, p.52. Original data is from J. Curran and R. Burrows, *Enterprise in Britain: A National Profile of Small Business Owners and the Self-Employed* (London: Small Business Research Trust, 1988), p.25.
3. Hong Kong: Victor Fung-shuen Sit and Siu-lun Wong, *Small and Medium Industries in an Export-Oriented Economy: The Case of Hong Kong* (Hong Kong: University of Hong Kong, 1989), Table 7.11, p. 95.

Notes:

1. For classification of different occupations in Taiwan, see appendix 3.
2. Figures in parenthesis in Taiwan show the population distribution of fathers' occupations when informants were fifteen years old.
2. For civil servant in Hong Kong is classified in *Other*. Merchant (34.7%) and Hawker (2%) in the original table are classified into *Self-employed*.
3. Employer/Manager and Upper/lower non-manual workers in Britain are put in one category in original table.
4. This is classified into two categories in the French data: upper middle or upper-class, including top, middle management workers, independent workers, medium and large farmers; working class or lower middle-class occupation, including clerks, sales and shop assistants, skilled workers, foremen, semi-skilled and unskilled workers, agricultural labourers and small farmers. See Nonna Mayer, *ibid.*, Table 47, note 6 and appendix.

From Table 2.17, we see that the small and medium-sized enterprises served as an avenue of upward social mobility for the less-educated in Taiwan, Hong Kong and China, while in Colombia it seems to be a 'catch net' for upper-class children. In Taiwan,

excluding shopkeepers, street vendors and independent professionals, 38.9% of the small business owners held a senior high school degree but no higher, much higher than the proportion of the population. Ke Zhiming (柯志明) found that 'it is impossible to promote the less-educated in a bureaucracy, so 82% of the informants believed that to be one's own boss is the best way to be successful'.²⁹⁶ The situation is the same in China and Hong Kong. The percentage of post-secondary degrees among small business owners in the three Chinese societies is higher than the population distribution, but not so extreme as in Colombia, where 35.1% of the informants are university graduates. In Germany (1980), 53.3% of the small business owners had advanced secondary (*Abitur*) or comparable levels of educational attainment (versus 11.3% of the population). A similar relationship holds for the figures for post-secondary qualification (66.9% of an external control group and 90.6% of the entrepreneurs).²⁹⁷

This is a strong contrast. Though those with only a primary school education in one of the Chinese societies had a smaller chance to be one's own boss, those who acquired a secondary degree and cannot enter university are more likely to be upwardly mobile via this path. On the contrary, in Germany or Colombia the less one is educated, the progressively lower the opportunity to run one's own business. Obviously to be one's own boss in a Chinese society is like a 'social ladder' to climb up, while in Germany, Britain and Colombia, it is better viewed as a 'catch net' for the downwardly mobile.

Another commonly held thesis is that 'it is a traditional Chinese ethic to work hard to become one's own boss'. For example, a survey of 1988 in Hong Kong found that 83% of the interviewees believed that workers have a chance to become bosses, and 49% in Hong Kong think the best mobility path is to 'start one's own business'.²⁹⁸ Why is there such a widely held belief? Stevan Harrell suggested that the relevant 'economic ethic' of Chinese society is the ethic of entrepreneurship, which is defined as the investment of one's resources in a long-term quest to improve the material well-being and security of one's family.²⁹⁹ Such an ethic is future-oriented, as with the small-scale factory workers

²⁹⁶ See Ke Zhiming, *op. cit.*, p. 13.

²⁹⁷ See Heinz Klandt, *op. cit.*, p. 36, note 11.

²⁹⁸ See Wong, Siu-lun, 'Chinese Entrepreneurs and Business Trust', in Gary Hamilton (ed.), *Business Networks and Economic Development in East and Southeast Asia* (Hong Kong: Centre of Asian Studies, University of Hong Kong, 1991), p. 19.

²⁹⁹ See Stevan Harrell, 'Why Do the Chinese Work so Hard?', *Modern China*, vol. 11, no. 2 (April, 1985),

in Taiwan in Richard W. Stites's description, who worked hard in order not to have to be workers forever.³⁰⁰ Chen Jiexuan (陳介玄) noted that diligence as a world view would highly value those who worked hard to become a proprietor. He noted that without support from this ideology, those who tried to be upwardly mobile through this route would not have access to social prestige, and their profit-pursuit would lack legitimacy.³⁰¹

Yet such ahistorical explanations fail to explain Taiwan's specific historical context and ethnic cleavage. The simple fact that Mainlanders and Taiwanese developed their careers within Taiwan in different ways cannot be explained by these cultural explanations. If Mainlanders and Taiwanese inherit the same Chinese culture, why have the Taiwanese been more likely to hold a desire to be a proprietor? It also fails to explain why people with a secondary degree are more likely to become business owners and those with a primary degree are more likely to be small shopkeepers or street vendors. It also cannot explain why the occupational distribution of males and females is so different.

My explanation is that, given the job structures in Taiwan, the less educated do not have any career prospects in a small firm, and on the other hand they are not able to work in a big company or a bureaucracy compared with those with high credentials. In addition, there has been no effective collective way to improve their market situation in the labour market. So their best hope is to apply the skills they learned in the factories in setting up their own business. But to run a company, one needs some basic general knowledge, and thus those bosses with secondary degrees were considerably more likely to be successful than those who were only primary school educated.³⁰²

p. 216.

³⁰⁰ See Richard W. Stites, 'Industrial Work as an Entrepreneurial Strategy', *Modern China*, vol. 11, no. 2 (April, 1985), pp. 227-246.

³⁰¹ See Chen Jiexuan (陳介玄), *Xieli Wangluo yu Renji Wangluo—Taiwan Zhongxiao Qiye De Shehui Jingji Fenxi* (協力網絡與人際網絡—台灣中小企業的社會經濟分析, *Subcontracting and Personal Networks—social economic analysis of Taiwan's small and medium-scale enterprises*) (Taipei: Lianjing Chubanshe, 1994), p.292.

³⁰² We should not forget that the data only shows the existing, or successful in another sense, companies. It does not show the failed firms. Those lower-educated might have tried to open their shops, but failed, so they had to go back to their original occupation again. Here we do not have data about the failure rate of different firms of different social background.

Table 2.17 Formal Education of Small and Medium-Sized Entrepreneurs (%)

Education	Taiwan(A) 1991-92	Hong Kong 1987	China 1991-92	Colombia 1978-79	Taiwan (B) 1990
Less than Primary School	0(8.9)	4.3(16.1)	(22.3)	9.1	5.3
Primary School	18.1(29.9)	27.5(34.2)	19.3(34.6)	20.8	26.3
Junior High School	16.7(16.2)		(30.2)		34.2
Senior High School	38.9(26.8)	55.8(43.0)	76.2(11.0)	29.9	29.4
Technical School	13.9(9.7)	--	--	5.2	3.5
Post Secondary	12.5(8.5)	12.3(6.7)	4.5(1.9)	35.1	1.3
N=	72(2370)	278(--)	3161(--)	77	228

Sources:

1. Taiwan(A): The General Survey of Social Change in Taiwan, 1991-92. Taiwan (B): Ke Zhiming (柯志明), *Taiwan Dushi Xiaoxing Zhizhaoye de Chuangye, Jingying yu Shengchan Zuzhi--yi Wufenpu Chengyi Zhizaoye wei Anli de Fenxi* (台灣都市小型製造業的創業，經營與生產組織—以五分埔成衣製造業為案例的分析), *The Establishment, Management and Production Organisation of Small Enterprises—Case Studies of the Ready-made Clothes Industry in Wufenpu* (Taipei: Sinica Academia, 1993), p.33.
2. Hong Kong: Victor Fung-shuen Sit and Siu-lun Wong, *Small and Medium Industries in an Export-Oriented Economy: The Case of Hong Kong* (Hong Kong: University of Hong Kong, 1989), Table 8.1, p. 99.
3. China: Guojia Jingji Tizhi Gaige Weiyuanhui, Guojia Gongshang Xingzheng Guanliju (National Economic System Reform Committee, National Industry and Commerce Administration Bureau), *Zhongguo Geti, Siying Jingji Diaocha -- Jingying, Lirun, Shouru* (Economic Survey on Chinese Individual, Private Business -- Business Administration, Profits and Revenue) (Beijing: Junshi Yiwen Chubanshe, 1993), p. 118 & 344, Table 1-1-13 & 5-1-8.
4. Columbia: Mariluz Cortes, Albert Berry and Ashfaq Ishaq, *Success in Small and Medium-Scale Enterprises—the Evidence from Colombia* (Washington: Oxford University Press published for The World Bank, 1987), p. 148, Table 4-5.

Notes:

1. Figures in parenthesis show population distribution.
2. The data shown here includes only those small business owners, excluding self-employed or professionals who hire workers.
3. The figure on high schools in Colombia includes those who did not complete their high school degree. The survey was conducted in metalworking firms only.

To summarise the argument so far, for those from the lower socio-economic classes, small and self-employed businesses are more likely to serve as a means to climb up the social ladder, even though the opportunity might be more accessible to those from a higher socio-economic background. In terms of education, small business owners tend not to be highly qualified, and thus it becomes plausible that this represents an alternative career path for those without formal ‘credentials’.

2.7 Conclusion

In general, one’s educational opportunities highly correlate with family socio-

economic background. In Taiwan, as noted, this socio-economic background is also related to ethnicity. The Mainlanders tended to be more highly educated than the Taiwanese, though the gap has been narrowed. To explain the phenomenon, I traced back to the 1950s the fact that the postwar political structure determined occupations and the shape of the educational system. Mainlanders were mostly placed in public offices or public enterprises, which gave them better economic benefits. Most Taiwanese were farmers at that time. Such an occupational difference entailed economic inequality between the two groups which in turn affected educational opportunities for their children. Such an unequal opportunity structure was reinforced by the government's education policy. Educational institutions were tightly controlled according to economic planning, which meant students had to face strict examination selection. The upper classes' economic resources helped their children to pass the examinations, while the government heavily subsidised the education of the children of public servants. These government policies benefited Mainlanders more than Taiwanese.

Since children from better socio-economic backgrounds obtained better educations, they could get better jobs in the labour market. The way the less educated adapted was through an effort to scramble out of their class situation, where possible, by 'becoming one's own boss', as the best path to upward mobility open to them. Such a strategy was structured in Taiwan in a specific historical context and was not predominantly the effect of traditional culture. Two main reasons for a lack of alternative paths were: the state-controlled labour regime forestalled the emergence of a labour movement; and the specific social network relations dissipated any possible collective action. Under these mechanisms, when the employment situation was unstable, wages low, and working hours long, their only chance was to leave wage employment. As Hill Gates has noted, capitalism 'offered a social model of upward mobility based directly on wealth rather than on connections with the state through the highly limited channels of degree- and office-holding'.³⁰³

Thus, the general mobility pattern in Taiwan for the less educated has been to get a wage job first and then to become self-employed when possible. The booming world economy in the 1960s gave entrepreneurial blue-collar workers a chance to move out of

³⁰³ See Hill Gates, 'Money for the Gods', *Modern China*, vol.13, no.2 (1987), p.261.

the 'inferior' class. But when they decided to jump out of their original class to be self-employed, they have faced social structures constraining their economic activities. In the following four chapters I will discuss the specific structures imposed on them, and how they manage their business under these constraints. The first step they needed to take was to collect capital to establish any new business, so let me start with their initial financing.

Chapter 3: The SMEs' Finances

3.1 Initial Capital of SMEs

I have explained in Chapter Two that structural forces, i.e., poor working conditions, low education, and political control, push a lot of workers to establish their own business. When they decide to do so, there are four ways to raise enough initial capital, i.e., (i) to borrow from financial institutions, (ii) to use one's own savings, (iii) to use one's social relations to collect capital, and (iv) to borrow from special government funds.

Almost no-one raises their initial capital from a bank, as the banking system is like a pawn shop, in that it always requires collateral for the loan. The normal practice is that the borrower shows documents to prove the value of his or her collateral, and the bank will give a loan at 70% to 80% of the value.³⁰⁴ One interviewee's wife said that 'banks are like prostitutes, who only work for rich people: if one does not have money, banks will never serve a person'. Another said that 'unless one's company is already in good financial shape, and you also have personal *guanxi* with the banks, it's almost impossible to borrow from the banks. Besides, the bank staff always thinks that the more work means the more errors, and less work fewer errors (多做多錯, 少做少錯, 不做不錯); you are not able to borrow from them'. Among my 40 interviewees, not one raised their initial capital from the banking system.

One way is to borrow such money from public funds set up by the government. One fund is called 'Loans to Youths to Set Up a New Business' (青年創業貸款), which provides young people without any initial capital with low interest loans to establish their new business. Its interest rate is only 70% of the prime interest rate of the Bank of Taiwan.³⁰⁵ Though the cost of interest is very low, there are not a lot of people with accounts at the fund. Only one among my forty interviewees said that he had used this capital source to finance his initial capital when he set up a new firm.

³⁰⁴ Discussion with an official from a government bank. The normal practice is 60%, and the rest is a second mortgage, called *Ertai* (二胎).

³⁰⁵ See Yang Yahui and Xiao Xuanyiyi (楊雅惠, 蕭玄逸沂), *A Study on the Financing of Small & Medium Business* (中小企業融資之研究) (Taipei: Ministry of Economic Affairs, 1992), p. 111.

Instead, most of the businesspeople saved some money, combined with private borrowing, to establish their business. According to Taiwan's civil law, there are three types of ownership of a company: wholly-owned, partnership and corporation. Among my forty interviewees, twelve companies (30%) were wholly-owned when they were set up, and twenty-eight interviewees (70%) adopted a partnership to establish their first business.

If these businesspeople use their savings as the sole source of their initial capital, their businesses are usually small and easy to set up, as in the case of an informant who set up his company with a few thousand US dollars, hired an apprentice, and used a machine to produce moulds. Only five informants (12.5%) said that their initial capital derived from their own savings without any other source. These were all 'wholly-owned companies'.

In Taiwan the most common way to raise funds is to use one's existing social relations to pull together scattered savings. Seven out of forty (17.5%) informants borrowed money to set up their business. No brother or friend runs the company with them. Their initial capital source included: their own savings, parents or siblings as well as wife's dowry and rotating credit associations. Interestingly, none of them borrowed from friends or relatives outside one's core family. We will discuss this phenomenon after the problems of a partnership are analysed.

The main reason to adopt the form of a partnership to establish one's first business is a shortage of capital. The entry level for setting up a manufacturing company is getting higher and higher. Either one has enough social relations to borrow money from one's own networks, or one has to go in with partners. To raise one's own share may still depend upon capital from family members; from friends; and from less closely connected social networks, mainly informal rotating credit clubs.

The first source is based upon traditional family values: that one's family (*jiazu*, 家族) is communal so that everyone is supposed to contribute to it as a whole. Especially in the patriarchal Chinese society, the capital usually flows from females to males, and from parents to sons. As Justin D. Niehoff finds in Yingge town, female workers had to send their money back to their family, and to help their father or brothers to set up their

businesses.³⁰⁶ Norma Diamond's research in the 1970s in Tainan shows that the earnings of unmarried daughters were remitted to parents to supplement the budget of the household and to help with the schooling and maintenance of brothers during an extended education.³⁰⁷ In Hill Gates' research, one fifth of the enterprises were set up with the help of wives' dowries.³⁰⁸ Ka Chih-ming's (柯志明) research found that in Wufenpu, when initial capital derived from only one financial source, 83% of the one hundred and sixty-six sampled raised their initial capital from self-savings (41%), parents' contributions (20%), and loans from relatives (21%). If they could raise capital from more than one financial channel, the most important sources were 1) rotating credit associations (39%), 2) own savings (26%) and 3) parents' contributions (18%). As the sample was of small-scale enterprises, the percentage of one's own savings in the initial capital loomed large.³⁰⁹

In my own research, ten percent of the interviewees obtained their initial capital partly from their wives' dowries. The percentage is not as high as Hill Gates' finding. However, another six interviewees (15%) utilised their wives' networks to gain access to initial capital, including rotating credit association, wife's savings and her family's money. Besides the wife's contribution, nine out of the forty informants (22.5%) received some money from their parents or siblings.

Other sources of initial capital include borrowing from rotating credit associations or from relatives and friends, but it seems that a partnership is far more important than other sources, as can be seen in the fact that 70% adopted partnerships to set up their first business. It is also interesting to note that among the twenty-eight companies, only six of the interviewees (21.4%) borrowed money from their parents, and five out of these six were partnerships between brothers. We might say that there is a sharp line between core family and others. Parents tend not to lend out money to non-core family members, and newly set up companies that are partnerships between friends seem not to

³⁰⁶ See Justin D. Niehoff, *The Villager as Industrialist Ideologies of Household Manufacturing in Rural Taiwan*, *Modern China*, vol.13, no.3 (July 1987), pp.291-96.

³⁰⁷ See Norma Diamond, *Women and Industry: Taiwan*, *Modern China*, vol.5, no.3 (July 1979), p.325.

³⁰⁸ See Hill Gates, *Small Fortunes: Class and Society in Taiwan*, in Dennis Fred Simon and Michael Y. M. Kau (eds.), *Taiwan: Beyond the Economic Miracle* (Armonk: M.E. Sharpe Inc, 1992), p.177.

³⁰⁹ See Ka, Chih-ming (柯志明), *Market, Social Networks, and the Production Organizations of Small-Scale Industry in Taiwan—the Garment Industries in Wufenpu* (小型企業的創業、經營與生產組織—以五分埔成衣製造業為案例) (Taipei: Institute of Ethnology, Academia Sinica, 1993), p.

be able to borrow money from parents.

Though a partnership is the most common way to start a new business, the ending is usually unhappy. A general pattern for a partnership enterprise is: 1) cooperation in the form of capital and technical cooperation; 2) disputes, either over profits or distribution of losses, and 3) disintegration of the partnership, closing the shop, or one of the partners converting it into an individual property.³¹⁰ In the 1992 General Survey of Social Change in Taiwan, which I have disaggregated and analysed on computer, only 12.7% (sixty-five out of five hundred and ten self-employed) are in partnership businesses. In my own interview data, though 70% of the enterprises were initially partnerships, only eight out of these twenty-eight (28.6%) survived in the form of a partnership when I first carried out interviews in 1993, and in 1996, only six of them kept the cooperative form. One company had broken up, and another one was closed and the owner committed suicide. Half of the eight enterprises are brother-type partnerships, and one of them is getting ready to divide the company among the brothers, and another has established a new firm for his son. Clearly, the partnership enterprise is not the normal type in Taiwan's business community.

Following are three cases that illustrate typical patterns of a partnership.

Case 1

In 1974, some friends of an interviewee's brother co-invested in a company which was not very well administered. The interviewee resigned from his job to work for the new company, which was born of a merger of two tiny companies, and the partners from the other company lived in the firm's premises, which meant that they used the company's electricity and space. An argument ensued, and by the end of 1974, they divided the machinery into two parts and broke up the company.

Case 2

Seven people organised a new company. One shareholder later sold his shares (about

48, Table 2-15.

³¹⁰ Xie Guoxiong's finding is similar to mine. See Xie Guoxiong (謝國雄), 'Heishou bian toujia--Taiwan zhizaoye zhong de jieji liudong (黑手變頭家--台灣製造業中的階級流動, Black-hands Becoming Their Own Bosses: Class Mobility in Taiwan's Manufacturing Sectors)', *Taiwan Shehui Yanjiu Jikan* (台灣社會研究季刊, *Taiwan: A Radical Quarterly in Social Studies*), vol. 2, no.2 (summer 1989), p 38.

US\$20,000) to the interviewee's wife, because it was not profitable. Still later the company continued to make a loss, so the wife borrowed US\$40,000 from the informant's sister to solve the company's financial problems. After the US\$40,000 investment, she and another shareholder became the two major shareholders. Then the interviewee came to work for the company. He found that another shareholder always took a certain percentage as commission when he put out an order to a company which contracted for them. The interviewee thought that he should not take this kind of commission, for it increased the company's costs. They began to have 'unpleasant discussions', and as a result one night, another shareholder took away all the machines, and asked to withdraw all his shares from the company.

Case 3

The interviewee's father invested with his uncle in producing the core part of a clock (機心). In the first few years they did not succeed in breaking through technical bottlenecks. All the losses were financed through the support of his uncle, who ran a very successful restaurant in Taipei. Eventually, the product became much cheaper than that of Seiko, which was the monopoly supplier of this watch component, and they gained large profits. But now everyone began to worry about the distribution of profits. His uncle said that he had paid most of the costs in these few years, and should get 80% of the profits; while his aunt argued that she was the main figure to deal with all financial problems, so she should be awarded more. Besides this sort of profit-distribution problem, the interviewee's father was very critical of his uncle's decision to spend US\$80,000 to decorate the firm. On the other hand, his uncle was very angry at his father's embezzlement from the company. One day, his uncle and aunt asked his mother and father to leave the company, and gave them US\$500,000 as compensation. Afterwards, they set up a new company to compete with the uncle.

These kinds of partnership histories are very common in my interviews. Even the brother-type partnership is not immune from the pattern. As one informant said, 'After the blow, I deeply understand that even relatives want to make money, when he talked about how his relatives embezzled money from his father's company. Another

interviewee said 'I hate partnerships. There are always arguments between partners. Even when they have profits, they fight over the distribution of profits.'

So how can we explain the persistence of some partnership enterprises? David Schak finds that the persistence of partnerships depends on the size, capitalisation, technology and entry barriers. If it takes much effort, skills and capital to form a partnership, it is more likely to stay together. If the partners are relatively equal in capital, skills, guanxi or other assets, they can easily break apart and go their own ways. Another factor is whether there is a clear division of labour and management. If one person runs the business and the other(s) profit on their investments, it will probably endure.³¹¹

The most likely to survive is the partnership between brothers. Among the four surviving brother-type companies from 1993, three had a strong leader. Two were led by the eldest brother and another directed by their mother. In the remaining company, the brothers have a consensus that they do not hire family members on the company payroll. If one had hired a family member in the partnership company, it could be interpreted as expanding one's power in the company, and will cause suspicion among the others. The informant said that 'my wife does not come to help in the firm, for the company is owned by many brothers, and we all avoid bringing any family member to work here, especially the wife because they might have a different opinion which will definitely disturb the running of the company. So we don't allow any family member to intervene in the company's affairs'. This strategy is also adopted by another partnership company which was composed of friends' capital.

Another way to maintain a partnership is to co-invest in a company on equal terms. If there are profits from a co-invested company, all partners will benefit equally; and if the company fails, all will suffer. For example, the business of an informant is to put electric wires underground, so he needs cement to make the tubes. Another informant owns a construction company, which also needs cement. They co-invested to establish a cement-jerking company, which benefits both.

This kind of partnership pattern shows that a profit-oriented firm accommodates uneasily to the family ideology. Many brother-type partnerships end up dividing, and some have to resort to a dominant family member to put the company together. The distrust among family members can cause the break-up of a family firm. If this kind of

distrust exists in a family firm, we would expect that it is less likely to trust non-family members. We have found that none of the wholly-owned companies borrowed from friends or relatives when they began their business. The distrust between family members and non-family members explains this.

Besides borrowing money from one's core family or setting up a partnership company, another way to collect initial capital is to join a rotating credit group. The working of a rotating credit group is that one of the joining members, called Huitou (會頭, head of the rotating credit association) is responsible for collecting a certain amount of money from members. If it is a club with US\$100 and eleven members, everyone in the club can bid to take the money contributed from all members if one needs money. Everyone will get a paper to write down their bid, and the one with the lowest amount will win the bidding. For example, if one does not need money, s/he can write the amount of 100, which means s/he would like to collect 100 from every one. If one writes 90, s/he will collect 90 from the other ten people, i.e., US\$900 in total. In eleven months, everyone can obtain the bidding only once, and after her/his winning of the bidding, s/he has to pay the full amount of US\$100. For example, if one secures the rotating credit with the price of US\$90 in the second month, s/he will get US\$900 in total. The following nine months s/he has to pay US\$100 every month. If s/he paid 90 in the first month, the total amount s/he pays during the eleven months is 90 (first month) plus 900 (the following nine months), i.e., 990.

The interest rate is usually higher than the official bank rate. Take the example that we mentioned above: s/he pays interest of US\$90 (990-900), and the interest rate is $90/900=10\%$ for ten months, and the annual interest rate would be 12% .³¹² The earlier one bids for the credit, the higher is the interest rate, as Table 3.1 shows.

³¹¹ I am indebted to David Schak's comments on this issue.

³¹² The calculation of interest rates is more complicated than shown here. To know the method of calculation, see Tu, Jaw-yan (涂照彦), *NICS Kogyoka Ajia wo Yomu (NICS To Understand Asian Industrialisation)* (Tokyo: Kodansha, 1988), p.122, Table 4-4.

Table 3.1 Interest Rates in a Standard Rotating Credit Group

Period	Total amount one gets when one wins the bid	One pays when one gets the bid	Actual amount one gets when one gets the bid	Interests one pays(-) or gets (+)	unit: %
					Interest Rate
	(1)	(2)	(3)=(1)-(2)	(4)	(5)=(4)/(3)
1	10,000*24=240,000	10,000	230,000	0	0.0
2	10,000*1+8,500*23 =205,500	8,500	197,000	33,000(-)	16.7
3	10,000*2+8,400*22 =204,800	8,400	196,400	32,100(-)	16.4
4	10,000*3+8,200*21 =202,200	8,200	194,000	32,900(-)	16.9
5	10,000*4+8,000*20 =200,200	8,000	192,000	33,100(-)	17.2
6	10,000*5+8,000*19 =202,000	8,000	194,000	29,100(-)	15.0
7	10,000*6+7,700*17 =198,600	7,700	190,900	30,200(-)	15.8
8	10,000*7+7,400*17 =195,800	7,400	188,400	30,400(-)	16.1
	-----	-----	-----	-----	-----
24	10,000*24=240,000	10,000	230,000	90,000(+)	64.3

Source: Tu Jaw-yan (涂照彦), *NICS Kogyoka Ajia wo Yomu (NICS To Understand Asian Industrialisation)* (Tokyo: Kodansha, 1988), p.122, Table 4-4.

A rotating credit group is one of the major ways for businesspeople to collect initial and working capital to run a company. What one needs is only one's social networks and then one can kick off a new rotation if one needs capital. Eight out of my forty informants (20%) said that they collected initial capital by this method, and most of them agreed that this system was very helpful when they started their business. It is popular because the relationship between the lenders and borrowers is clear: creditor and debtor, no more and no less. The lender does not have to feel ashamed to ask for money back plus interest, whereas it is not common to ask for interest among friends if one lends out money. So this credit rotation system can be viewed as a kind of mechanism to solve the contradiction between the self-interest principle and the *renqing* principle.

3.2 Working Capital of SMEs

One should distinguish between the 'initial capital' for setting up a firm, and the 'working capital' after a firm has successfully been established. In the two phases, SMEs have different demands for capital. After running a successful company, one

would have no problem in getting bank loans to provide working capital. As mentioned, the banking system in Taiwan is like a pawn shop, lending money to those whose financial situation is good and with minimal risk of default. It is almost impossible for SMEs that lack capital to secure any loans from the banks. Many scholars proposed that the government should grant SMEs special funds or bear a certain risk for them. They said that the biggest problem that SMEs face is insufficient capital. But the SMEs do not obtain fewer loans than large companies. SMEs that are run well do not have any problem of capital circulation. They have enough capital to reinvest in new projects.

In my sample, only two informants (one operated a motorcycle assembly firm, the other a publishing company) complained about the difficulty of securing loans to expand production. The other companies do not have problems in getting working capital for their production, for either they can discount their letters-of-credit or notes receivable at the bank, or mortgage their machinery or land to borrow money.

Since the deregulation of the financial market, more financial tools have been introduced in the markets and made available for the SMEs to diversify their working capital. Four financial markets, i.e., the monetary market, the foreign exchange market, the capital market and the futures market, are available. For example, a company can use treasury bonds as a short-term savings tool when it has extra money, and sell them when it is in need of money. Or it can issue commercial paper to collect capital for production expansion. While more financial products are available to SMEs, they are not yet familiar with these products. In 1996, the use of commercial paper and bank's acceptances comprised only 1.5% of their total liabilities in contrast to 7.6% for big firms (see Table 3.2 and 3.3). The method of direct financing from financial markets will become more and more important as people become more familiar with them. More and more SMEs use the futures market to hedge the risk of exchange rate fluctuations. Some informants also said that they plan to issue stocks in the stock market to raise capital. The establishment of the OTC (over-the-counter) market gives SMEs more opportunities to do this because the OTC market sets lower thresholds for companies to participate.

It seems quite contradictory that some scholars believe that SMEs have difficulty in getting capital while most of my informants reported no problems. However, from the vantage point of banks, it is not difficult to explain: banks also want to make money,

and loans are based on risk calculation; if not on profit calculation, on political interest calculation. Those SMEs complaining about the banking system are usually not very well run companies, and have no support from local politicians. Their risk premium is thus too high for a bank to grant them loans. So these SMEs have to resort to the private financial market. For well-run companies, the risk is lower, and with mortgaged assets, the banks run almost no risk in granting loans.

As a result of financial liberalisation after the mid-1980s, more and more new financial tools are available in the financial market which enable private enterprises to get capital directly from the market instead of from intermediaries, e.g., issues of commercial papers, bonds or securities. Newly established banks are keen to compete to gain customers. However, the impact of financial liberalisation on big firms and SMEs is not the same, which can be observed from the liability structure viewed by enterprise size (See Table 3.2 and 3.3)

Liabilities of a company's balance sheet can be regarded as external capital sources, and the net worth is the company's internal capital funding. The two tables below show that more and more of the capital in big firms derives from internal funding, while more and more SMEs have sourced their capital from outside. Almost one out of two dollars (47.8% in 1996) in big firms is from the company's internal funding. It can be interpreted that big firms are able to sustain the company's development through their own capital. In contrast to these big firms' capital structure, the SMEs' internal funding was reduced from 40.7% to 34.0% between 1991 and 1996 due to the decline of the owner's equity, which means that they are more and more dependent on external capital sources. When they source their capital from outside, there is no difference between big firms and SMEs in terms of borrowing from financial institutions.

Another important external source of capital for private enterprises is 'trade credit', which accounts for 17% of the big firms' total liabilities, and 28% of the SMEs' in 1996. However, fewer and fewer big firms use this financial tool, while more and more SMEs have come to depend on it. This is because SMEs use less formal contractual relationships to do business with their counterparts. One exporter told me that 'we don't ask those well-known customers to issue letters-of-credit. Sometimes we just ask them to pay one third in advance and the rest can be paid one month after the goods set shipped. All these practices are based on mutual trust (*xinyong*)'. It is one of

the major financial tools by which Taiwan's SMEs manage their capital.

Table 3.2 Liability Structure of Big Enterprises, 1991-95

unit: %

	1991	1992	1993	1994	1995	1996
Liabilities	54.2	56.3	54.8	54.5	53.3	52.2
Loans from FIACD	25.0	25.4	22.8	23.3	22.0	16.4
Loans from Enterprises and Households	4.6	3.8	3.6	3.1	3.1	3.2
Commercial Papers and Bank's Acceptance	3.3	3.5	5.7	5.4	6.2	7.6
Trade Credit	18.0	20.2	18.9	17.6	16.3	17.0
Other Liabilities	—	—	—	—	—	8.0
Net Worth	45.8	43.7	45.2	45.5	46.7	47.8
Owner's equity	30.0	30.1	28.2	28.7	29.1	—
Retained Earnings	15.8	13.6	17.0	16.7	17.6	—
Total Liabilities	100.0	100.0	100.0	100.0	100.0	100.0

Source: *Zhonghua Minguo Taiwan Diqu Gongminying Qiye Zijin Zhuangkuang Diaocha Jieguo Baogao* (中華民國台灣地區公民營企業資金狀況調查結果報告, *Report on Public and Private Enterprises' Capital Conditions in Taiwan District, the Republic of China*) (Taipei: Economic Research Department, the Central Bank of China, 1993-1997). Data of 1996 is from news released on the 14th of April, 1998 by Central Bank.

Note: Other Liabilities include borrowing from government, overseas borrowing, domestic corporate bonds, overseas securities and other reserves.

Buyers ask favours from sellers to delay their payment as long as possible, while sellers would like to collect their money as soon as possible so that they can earn interest. Normally buyers issue a thirty to ninety days' post-dated cheque after the goods are delivered so that they can reduce their interest burden. Sellers can go to banks to discount the cheques and get cash. This kind of business practice was enforced by the government's Bills Law (票據法), for those who bounced their cheque would be put in jail. (The legal penalties were removed several years ago.) Besides, it was very difficult to open a chequing account in a bank.³¹³ Possessing a chequing

³¹³ Regarding the difficulty of opening a chequing account, see Shen Yingming (沈英明), *Dixia*

account represented one's *xinyong*, and the acceptance of the post-dated cheque became popular because the cheque had already been endorsed by the government and banks.

Table 3.3 Liability Structure of SMEs, 1991-95

unit: %

	1991	1992	1993	1994	1995	1996
Liabilities	59.3	59.7	60.9	64.3	65.8	66.0
Loans from FIACD	21.6	23.1	23.2	25.1	24.8	24.4
Loans from Enterprises and Households	13.1	13.8	14.9	14.4	15.0	11.0
Commercial Papers and Bank's Acceptance	0.1	0.1	0.4	0.4	0.6	1.5
Trade Credit	23.6	22.0	21.8	23.8	25.0	28.3
Other	—	—	—	—	—	0.8
Net Worth	40.7	40.3	39.1	35.7	34.2	34.0
Owner's equity	39.4	37.0	36.3	33.2	32.3	—
Retained Earnings	1.3	3.3	2.8	2.5	1.9	—
Total Liabilities	100.0	100.0	100.0	100.0	100.0	100.0

Source: *Zhonghua Minguo Taiwan Diqu Gongminying Qiye Zijin Zhuangkuan DiaoCha Jieguo Baogao* (中華民國台灣地區公民營企業資金狀況調查結果報告, Report on Public and Private Enterprises Capital Conditions in Taiwan District, the Republic of China) (Taipei: Economic Research Department, the Central Bank of China, 1993-1997). Data of 1996 is from news released on the 14th of April, 1998 by Central Bank.

Note: Other Liabilities include borrowing from government, overseas borrowing, domestic corporate bonds, overseas securities and other reserves.

The legal system underpinned the cultural practices of *xinyong* (trust). However, when a conflict of interest arises, e.g., when one is not able to pay back the money, the trust will give way to self-interest. A popular saying was 'cost ten, sell eight, default, pay back three, and profit five' (拿十、賣八、倒、還三、賺五). It shows the dilemma the seller has to face: s/he would like to extend credit (*xinyong*) to the buyer so that s/he can make more money, but s/he also has to worry about the risk of default. Intensive personal contacts become one major way for businesspeople to know buyers' *xinyong*, for the credit rating system is not yet sound in Taiwan. An interviewee who runs a Buddhist statue-molding company said that "after the default by my sister, I

started to know that I can't rely on the Bills Law at all. I always thought that having the skill would be enough to be a boss. With the protection of the Bills Law, it should not be a problem to accept a cheque. But now I know that management, the law and personal contacts are important as well." *Xinyong* is not an imperative cultural factor driving people to keep their word, but must be supported by legal and social factors to work.

The SMEs' ratio of borrowing from households and other enterprises is much higher than among big firms. From 1991 to 1995, the ratio increased from 13.1% to 15.0% in SMEs, but decreased to 11.0% in 1996, while in big companies it declined from 4.6% to 3.2% in the same period. This financial instrument is mostly based on private relationships, and thus we can conclude that SMEs are much more likely to use personal networks to secure capital than are big firms. This personal connection is mainly through shareholders' credits. According to a survey done by the Bank of Taiwan, 82% of the loans from households to SMEs come from the SMEs' own shareholders. When the SMEs make profits, they distribute the profit to shareholders instead of retaining it as a kind of reinvestment capital. The shareholders obtain their profit, and then lend out the capital to their own companies to gain higher interest (i.e., two times higher than the market rate).³¹⁴ The main reason to borrow from shareholders is that if the money did not go into the official financial market, the capital owner does not have to pay any tax on the interest s/he earns, and at the same time, can use this kind of accounting practice to hide income.

Big firms may borrow from the official financial market, or from the financial institutions accepting chequing deposits (FIACD), or issue bonds, securities or stock to collect capital, where interest rate is only half that of the formal financial market. According to an informant at the Bureau of Monetary Affairs, it has become a major financial tool for big firms in the past five years, accompanying the development of Taiwan's financial markets.

The private borrowings from households and enterprises are usually viewed as private financial markets. Because more SMEs borrow money from this private market,

³¹⁴ See Qiu Zhengxiong and Liu Yiru (邱正雄, 劉憶如), *Huobi yu Jinrong Shichang guonei Fazhan yu Guojihua Fazhan* (貨幣與金融市場: 國內發展與國際化發展, *Domestic and International Development of Monetary and Financial Market*) (Taipei: Bureau of Monetary Affairs,

it is often claimed that the SMEs lack capital and thus have to resort to a private financial market, which is regarded as a sign of the inefficiency of the financial market.³¹⁵ However, if we use the shares of loans as an indicator, the SMEs do not obtain less loans as a proportion of their sales volume than do the large firms. Up to the end of 1995, the SMEs obtained only about 37% of the total loans from the commercial banks, and most of this money went to big business. But from Table 3.4, we can see that the sales of SMEs in the economy are only around one-third of total sales, and the share of loans to them from the financial system is between 37% to 40% of total loans. Another indicator is the ratio of their loans from financial institutions, which shows no difference between the two groups (see Table 3.2 and 3.3). And the third reason to doubt this claim is that the SMEs' loans from households mostly derives from the shareholders' loans, and there is no sign that this is less efficient than borrowing from banks, for the kind of capital flow between borrower and lender is direct instead via financial intermediary, which will save certain part of transaction cost.³¹⁶

The Taiwan government has maintained a monthly report of the financial private market's interest rates since the 1950s. This means that it knows quite well that the prevailing interest rate is not the market-clearing interest rate; instead, it is distorted. This government's interest rate controls were strongly criticised by Taiwan economists for inefficiency, as they do not allocate scarce resources adequately, and do not help

1993), pp.83-84.

³¹⁵ See Yang, Yahui and Xiao Xuanyiyi (楊雅惠, 蕭玄逸沂), *A Study on the Financing of Small & Medium Business* (中小企業融資之研究) (Taipei: Ministry of Economic Affairs, 1992), pp.135-141; Zhou Tiancheng (周添城), *Taiwan Jinrong Guanzhi yu Jingji Fazhan: Shuangyuanxing Jinrong Tixi yu Erfenhua Shichang Jiegou* (台灣金融管制與經濟發展; 雙元性金融體系與二分化市場結構, Taiwan's Financial Regulations and Economic Development: Dual Financial System and Dichotomous Market Structures), *Taiwan Yinhang Jikan* (台灣銀行季刊, *Taiwan Bank Quarterly*), 1994, vol.45, no.1, pp.222-240; J. D. Shea, *Financial Development on Taiwan: A Macro Analysis*, *Conference on the Financial Development of Japan, Korea and Taiwan* (Taipei: Institute of Economics, Academia Sinica, 1990); Wu Huilin (吳惠林), *Zhengfu Ruhe Xiezu Zhongxiaoqueye* (政府如何協助中小企業, *How Can the Government Help Small and Medium-sized Enterprises to Transform?*) (Taipei: unpublished research paper, 1996), p.5, 17; Lin Zhongxiong and Peng Baixian (林鐘雄, 彭百顯), *Zhongxiao Qiye Jinrong yu Yiban Jinrong zhi Bijiao* (中小企業金融與一般金融之比較, Comparison of General Finance and Special Finance to SMEs), in Chen Mingzhang (陳明璋) (ed.), *Taiwan Zhongxiao Qiye Fazhan Lunwenji* (台灣中小企業發展論文輯, *Essays on Taiwan SMEs*) (Taipei: Lianjing Chubanshe, 1994), pp.195-267.

³¹⁶ See Qiu Zhengxiong and Liu Yiru (邱正雄, 劉憶如), *op. cit.*, 83-84.

those enterprises which really need the capital.³¹⁷ The system finally was liberalised in 1989. But why was the 'inefficient' financial system kept for over forty years? We would argue that this kind of distorted market mechanism was mainly used as a means of control, that financial institutions played a supportive role to control economic and political resources.

Table 3. 4 Small and Medium-Sized Enterprises' Shares of Loans and Sales

Year	unit: %	
	Shares of Loans	Shares of Sales
1988-91	41.49	34.76
1992	39.36	33.66
1993	38.77	33.87
1994	37.19	32.2

Source: Jingjibu (經濟部, Ministry of Economic Affairs), *Zhonghuaminguo Bashisi nian Zhongxiao Qiye Baipishu* (中華民國八十四年中小企業白皮書, *White Paper on Small and Medium-sized Enterprises in the Republic of China, 1995*) (Taipei: Ministry of Economic Affairs, 1996), p.58, Table 2-2-4; p.125, Table 4-2-1.

3.3 Loans and *Guanxi*

In short, in the financial system in Taiwan, the main financial intermediaries were controlled by the state, while local financial institutions were controlled by local KMT factions. The situation has not changed a lot nowadays, despite the liberalisation. If there is no interest rate control, or no political control, the financial institutions will allocate the capital according to the feasibility of a company's proposed investment and rate of returns. However, political power changes the 'economic rationality principle' and results in the practice of 'pulling *guanxi*'.

The policy of controlling interest rates and financial institutions until late 1980s inevitably resulted in a shortage of savings and the problem of 'favouritism'. The banks had to use credit rationing when allocating capital, which in turn increased the

³¹⁷ See Chen Shimeng (陳師孟) *et al.*, *Jiegou Dangguo Ziben Zhuyi* (解構黨國資本主義, *Disintegrating KMT-State Capitalism*) (Taipei: Chengshe Baogao 1, 1991); Jiang Shuojie (蔣碩傑), 'Taiwan zhi Lilyu Wenti' (台灣之利率問題, the Problem of Interest Rate in Taiwan), in Yu Zongxian (于宗先) (ed.), *Taiwan Huobi yu Jinrong Lunwenji* (台灣貨幣與金融論文集) (Taipei: Lianjing Chuban Shiye, 1975), pp.305-323; Liu Fuqi (柳復起), 'Taiwan you Tonghuo Pengzhang dao Jingji Wending de Jinrong Fazhan' (台灣由通貨膨脹到經濟穩定的金融發展, Financial Development in Taiwan: from Inflation to Stabilisation), in Yu Zongxian (于宗先) (ed.), *Ibid.*: pp.31-

opportunities to be corrupt. In a poll of executives by the *Far Eastern Economic Review* on the banking sector in Asia, 20.8% of the executives think that Taiwan's banking sector is to *a great extent* affected by corruption, and 54.2% think the degree is to *some extent*.³¹⁸

What companies asked for was a chequing account and loans. As noted, the use of the chequing account was to prove one's credibility, and the access to loans was for working capital and tax evasion, which will be discussed below. In order to obtain loans, even the top officers know that banks' customers had to give presents and to use *guanxi*.³¹⁹

Financial institutions consider three factors in evaluating applications: transaction records with the banks (*shiji*, 實績), trustworthiness (*xinyong*, 信用), and relationships (*jiaoqing*, 交情).³²⁰ A very profitable company would find it easy to obtain loans from the banks according to the market principle, for it will be able to pay back the money and has a lower risk of default. Big firms will not have any problem because their credit rating is much better than small firms. So the three factors are an invisible wall for SMEs to gain access to the formal financial market. Utilising *guanxi* becomes necessary for them.

A company has to keep a good transaction record with the banks so that banks can rely on its credibility and also profit from the transactions. Companies were asked to have a minimum savings balance in the bank in certain periods so that the bank can obtain a cheap source of capital. This kind of practice is called '*shiji*' (實績). Not only does the bank ask for the company to maintain a deposit account, but also needs the company to prove that it is a good customer and would never default. This criterion is more or less based on a credit evaluation, and it more or less regulates the banks' practices not to ensure these do not 'derail from the right economic track'. However, it seems that '*jiaoqing*' (交情) is most important among the three factors due to the specific political environment. As many interviewees mentioned, even if

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³¹⁸ See Far Eastern Economic Review, *Asian Executives Poll*, 07/Aug/1997, p.33.

³¹⁹ Yin Zhongrong (尹仲容), *op.cit.*, 21.

³²⁰ See Xiao Shengtie (蕭聖鐵), *Taiwan Minying Gongye Lixi Fudan zhi Fenxi (台灣民營工業利息負擔之分析, Analysis of Private Enterprises' Interest Burden in Taiwan)*, in Yu Zongxian (于宗先) (ed.), *op. cit.*, p.335.

one's company is very well run, it still needs to know someone in the bank and to keep a good relationship with her/him to arrange of loans easily.

A company can approach the financial institutions via local factions. Because most of the banks belonged to the state, workers in the banks were civil servants, and the only responsibility they bore was to their chief, who in turn had to be responsible to the provincial government, which is supervised by the provincial council. This means that provincial council representatives can exert pressure on banks to loan to certain people. When most provincial representatives belong to one local faction, it is not hard to imagine that the flow of loans from the banks mostly went to the local faction's businesses. It is widely assumed that every provincial council representative has the privilege of borrowing a certain amount of money. One businessman whom I interviewed said that "one of the advantages in putting a provincial representative's name on my company's board of directors is so that we can then borrow money from the banks easily".

For the civil servants in the bank, as long as the loan is legal and there is support from the top, even if the risk is high and the bank's profit is low, they still have to lend out the money, or they run the risk of offending their supervisors. In particular, the local financial institutions like the farmers associations or credit cooperatives, which are mostly controlled by local political factions, are also abused by local politics, and only those people with good relationships with local factions can secure loans from these institutions.

Businesses lacking the right 'political connections' have to follow the market rules, i.e., either their credit is good enough to borrow money from the banks, or they are able to find an 'underground way' to obtain access to the formal financial market; otherwise they have to resort to the financial 'black' market.

Demand creates its own supply, as Say said. There were a lot of companies that needed a chequing account, or money, but did not have good *guanxi* with the banks, so they needed to ask for a financial broker's help. It was required to have a person to 'introduce' the company to the bank in order to open a chequing account. It is also a common practice for a bank to ask for a guarantor if one wants to borrow money.³²¹ This gives an opportunity for those people familiar with banking practices or who have

good relationships with banks to become brokers and charge a fee for their service. Though this kind of service is illegal, it has existed for over fifty years.³²² For example, a few staff from one credit union in Taipei raised some money to run a company to help companies that needed deposit certificates in order to apply for a new company registration. They charged these companies 0.3% interest rate per day (108% per annum).³²³ Regarding the application for a chequing account, there was a market price: in 1982, a check account cost NT\$20,000 (US\$5 00). To delete a bad records for bouncing a check cost NT\$5,000.³²⁴

If a company cannot borrow from a financial institution, either by way of the normal process or 'underground', it has to resort to a private financial market and pays a higher interest rate. It can borrow from four sources in the private financial market: specialised private moneylenders, relatives or friends, rotating credit associations, and employees of the company.³²⁵ The latter three ways of borrowing money are based on personal *guanxi*. However, even the moneylenders like those in Dihua Street (迪化街) loan to those they are familiar with in order to minimise risk.³²⁶ Only a few moneylenders can be called 'usury shops'. If we add the cost of engaging with bureaucrats in the public banks, and the problems of finding guarantors, collateral, and the tedious application process, the cost of borrowing from the private financial market is not so high as it appears.³²⁷

From the above discussion, we see that companies need *guanxi* to borrow either in the official or private financial markets. This sort of *guanxi* is not necessarily inevitably a Chinese trait, but shaped in certain socio-political formations, and exploited as a means to achieve certain goals. Some people can utilise political *guanxi* and gain lower interest-rate loans from the organised financial market. People without political backgrounds would utilise personal connections to collect capital. However, we cannot say that having *guanxi* is in itself sufficient to ensure one can borrow money. If one does not have a good reputation in business (lacking *xinyong*), s/he will also find it hard to

³²¹ See Shen Yingming, *op.cit.*, p.15.

³²² *Ibid.*: p 16.

³²³ *Ibid.*: pp.16-17.

³²⁴ *Ibid.*: p.17.

³²⁵ See Xiao Shengtie (蕭聖鐵), *op.cit.*, p.333.

³²⁶ See Shen Yingming, *op.cit.*, p. 12; Yang Yahui and Xiao Xuanyiyi (楊雅惠, 蕭玄逸沂), *op.cit.*, p.221.

³²⁷ See Xiao Shengtie (蕭聖鐵), *op.cit.*, pp.333-336.

borrow. The Tainan Bang (Tainan business group, 台南幫), a loose coalition of enterprises, would not lend money to those businesses which lack good *xinyong*, even if it is an enterprise in its own group.³²⁸ If *guanxi* is based on calculated interests, it can be imagined that the so-called *Chinese guanxi* will evaporate when interests conflict.

3.4 SMEs and Tax Evasion

Although most of my informants have enough working capital for production and many of them do not need banks loans, many of them still borrow money from the banks. If well-run companies do not need capital from the banks to reinvest, why do they take out loans? The main reason is to evade tax.

Tax evasion is widespread among SMEs. One informant said that in 1987, the government scrutinised the tax files of ten publishing companies in the Tainan area, and 'of course every company was found to be guilty of tax evasion'. He himself was fined about US\$20,000. After the 'tax shock', he began to borrow money from banks to prove that he has difficulty in his finances and needs financial support from banks. He told me confidently that 'if they come to check for tax evasion again, they will never find any clue'. Another informant invested in a hotel. A provincial representative and a county representative also have shares in the investment. 'To invite them to join the investment will make it easy to get loans from the banks, and the purpose of borrowing money is not lack of capital, but to evade tax'.

How is this done? According to a report of the Taxation Office, the most common way is to claim less income than one actually earns in one's income tax statement; this accounted for 58% of the illegal cases found in 1982.³²⁹ The methods include: the owner do not issue sales invoices (22%), do not report general income (15%), do not report business income (15%), and do not report commission income (5%). There are at least two accounting practices used to evade issuing a sales invoice: first, when the company gets cash income, it is put in one's pocket, and the company reports a higher quantity of sales and a lower unit price when it issues invoices; second, to adjust the

³²⁸ See Shen Yingming, *op.cit.*, p.12.

³²⁹ See Xu Zhimin (許志民), *Zhongxiao Qiye Jianquan Kuaiji Zhidu yu Fangzhi Taoloushui zhi Yanjiu* (中小企業健全會計制度與防止逃漏稅之研究, *Studies on SMEs' Accounting System and the Prevention of Tax Evasion*) (Taipei: unpublished Master thesis, Graduate School of Accounting, Soochow University, 1986), p.35.

accounting for short-term borrowings, accounts receivable and deposits received from shareholders to hide the sales income.³³⁰ Table 3.3 shows that about 15% of SMEs' liabilities and stockholders' equity are from private borrowing. This percentage is much higher than the big firms' 3.1%. We also noted that most private borrowing in SMEs is through the deposits received from shareholders. This accounting practice explains why a lot of SMEs borrow money from the private financial market, i.e., tax evasion. For example, if a firm has sales of ten dollars, the company can credit ten dollars cash and debit ten dollars in the item of 'borrowing from shareholders' (股東往來) so that there is no transaction of the sales, and in future, the company can borrow ten dollars from a bank, and use the money to pay back the shareholders plus interest. When this step is reached, the money is successfully laundered.

Another common way to evade tax is to inflate the costs and expenditures so that one shows no profit. This comprised 17% of the reported tax evasion cases by the Taxation Office in 1982.³³¹ One common practice in the old days was to buy invoices from a 'paper company' (*rentou gongsi*, 人頭公司) as proof of expenditures, while in fact there is no transaction at all. It is very easy to set up a company, that some actually set up many such companies, then sell invoices to other companies so they can evade tax. After one or two years, the paper companies will close, and the person sets up another one to continue this activity. In these ways, the company can report a lot of costs which in fact it never incurs. For example, a company produces a product at a cost of 100, and sells it at the price of 120. In the normal case, it has to pay a profit tax. But instead buys phoney invoices to inflate the cost to 140. Thus it has to borrow 20 from a bank to cover the extra 20 in costs (140 minus 120). In the next year, if the cost and price of the product is unchanged, the company would make another 20 profit, which would be used to pay back the bank. So in these two years, the company accounts would show no profit at all on par value, but in fact have 40 in profits. Another way is that private expenditure is debited as company expenditure; and a third way is to give shareholders cheques and debit them as business expenditures. All these practices can inflate costs and transfer profits to shareholders.

How do they hide their money after they get the cash? The most common way is

³³⁰ *Ibid.*: pp.37-38.

to put the money in family members' bank accounts. Another way is to buy bearer bonds, then transfer the bonds to family members. One does not have to show any identification certificate to cash the bearer bonds, so this method has become popular among businesspeople.³³² In recent years, an increasingly popular way is to open an account in Switzerland and to launder money through underground financial intermediaries, like the jewellery shops on Hengyang street (衡陽路) in Taipei. One informant told me that his family is in Canada, and all his money is remitted from Taiwan via Swiss banks to Canada. Another way is to set up a company overseas, and make nominal purchases, then transfer the money to the overseas company, though there is no real transaction has occurred between the two companies at all.

3.5 The New Banks' Competition and Deregulation of Financial Markets

In 1992, the prohibition on setting up new banks was removed and eleven new banks were approved. Did this kind of deregulation improve the efficiency of the financial market and undermine the material base of KMT rule? On the one hand, we could say that with competition the financial institutions controlled by the government will improve their efficiency and abandon those politicised operations that violate market principles. However, Taiwan's polity has been transformed from authoritarian to 'populist authoritarian', which means 'the state centralises and uses power in an authoritarian way in the name of the common weal to legitimise its rule, but at the same time it intends to disregard the formal constitutional framework'.³³³ The state allows private big companies to conduct highly profitable business, and forms a new coalition with them in the name of the common weal. Before the lifting of martial law, this kind of coalition had no legitimacy, for the KMT-controlled government did not acquire any legitimacy from the votes. But after 1992, the government is elected, and its coalition with big business is legitimised by this democratic voting system.³³⁴ The new banks are all controlled by big companies (see Table 3.5), and their relationships with the government and local factions reinforce political power in the financial system.

³³¹ See Xu Zhimin (許志民), *op.cit.*, p.35.

³³² This story is heard from a friend who tried to evade huge taxation from the Taxation Office.

³³³ See The Editorial Board, 'A New State or A New Society: On the Present Situation and the Radical Alternatives' (由新國家到新社會—兼論基進的台灣社會研究), in *Taiwan: A Radical Quarterly in Social Studies*, no 20 (August, 1995), p. 6.

Table 3.5 The Background of Newly Established Banks (1991)

Name	Chairman	Main Investor	Background
Daan 大安	Lu Runkang 陸潤康	Yimei et al. 義美	All investors are Taiwan's top 100 Business Groups
Wantai 萬泰	Xu Shengfa 許勝發	Yulong 裕隆	4
Yuandong 遠東	Xu Youxiang 徐幼庠	Yuandong 遠東	5
Yatai 亞太	Qiu Jiexiong 邱家雄	Erming investing Co., et. al.	Big companies
Zhongxing 中興	Wang Yuyun 王玉雲	Huarong 華榮	12
Wantong 萬通	Wu Zunxian 吳尊賢	Tainan Business Group 台南幫	3
Yushan 玉山	Lin Zhongxiong 林鐘雄	Taihuo et. al. 台火等	Big companies
Lianbang 聯邦	Li Jingcun 李敬存	Lianbang Business Group 聯邦集團	the biggest land speculating group in Taiwan
Huaxin 華信	Lin Lixin 林立新	KMT et. al. 黨營事業	KMT
Baodao 寶島	Chen Chongguang 陳重光	Yimei et. al. 義美等公司	Big companies
Fubang 富邦	Cai Wancai 蔡萬財	Cathay 國泰	2
Zhonghua 中華	Wang Youzeng 王又曾	Liba 力霸	20
Huanya 環亞	Xie Rendong 謝仁東	Changyi 長億	Big Real Estate Co.
Taixin 台新	Wu Dongliang 吳東亮	Xinguang 新光	6

Source: Yan Junbao (嚴雋寶), *Taiwan Diqu Yinhang Fazhan 40nian* (台灣地區銀行發展四十年, *The Development of Banks in Taiwan Area*), (Taipei: Zhonghua Zhengxinsuo, 1991), pp.404-405.

Notes:

1. The number in the background column means the ranking of the investing business group in 1985 ranked by Zhonghua Zhengxinsuo.
2. The meaning of big companies is my own judgement based on their fame in Taiwan.

Nominally the Land Bank of Taiwan and the Chiao-tung Bank were privatised in 1996, as the government sold a portion of its shares on the market so that it holds less than fifty percent of the shares. Three commercial banks (Hua-nan, Chang-hwa and the First Commercial Banks) were approved to be privatised in September 1997. In the

near future the government will continue to privatise other public banks. Though the government's holdings are under 50%, it will still dominate these banks, and it will be able to exert pressure on them to follow its policies.³³⁵

These privatised and to-be-privatised banks will still be the most important actors in the financial market, but they will have another new role to play by, i.e., to be the final guarantor of the other private financial institutions. This means that they have a political errand to stabilise the financial system. Whenever an institution faces default, especially one of the local faction-controlled credit unions or farmer's associations, these banks will step in to lend it a hand.

This phenomenon was already evident in 1995, when a lot of local faction-controlled credit unions and farmers' associations ran into trouble, and the public banks had to 'clear all the bad debts'. Obviously the cost is paid by the taxpayers. Though most local financial institutions joined the central deposit insurance company after a series of financial crises, the risk premium that the insurance company charges is only 0.01% of total deposits, the lowest rate in the world. The company can offer such a low rate because its main shareholders are the Central Bank and the Ministry of Finance (over 99%), and most of its revenue derives from the interest on its equity of 10 billion Taiwan dollars. The government pays the insurance cost, and local factions gain the profits. This sort of design illustrates what James O'Connor notes: the basic contradiction of capitalism is the privatisation of profits and the socialisation of costs.³³⁶

Those SMEs which could not borrow money from the old banks³³⁷ are able to borrow money from the new banks to a certain degree, but there are limitations. Usually the new banks will supply capital first to their *guanxi qiye* (關係企業), the enterprises with which they have *guanxi*. If, after satisfying the needs of these customers, they still have capital to lend, businesspeople who would otherwise have to borrow money from the private market get access to loans. Since the end of the bubble economy in 1991, savings have been much higher than investment, and the new banks

³³⁵ Up to now, these privatised public banks are still regarded as state-owned, for the people in charge of these banks are civil servants and their names are still put in the 'address book of Executive Yuan and its Offices'.

³³⁶ See James O' Connor, *The Fiscal Crisis of the State* (New York: St. Martin's Press, 1973), pp.1-10.

³³⁷ 'New banks' refers to the banks set up after 1992, and the others are called 'old banks'.

have begun to loan out their excess savings to those SMEs which still heavily rely on the private market. This is the positive effect of competition. According to financial statistics, up to the end of 1997 the share of the new banks' loans to SMEs was 8.1% of total loans from all commercial banks, increased from 5.5% in 1994.³³⁸ One interviewed manager in a public bank said that the increase of loans to SMEs from the new banks comes mainly from the marginal customers of the old banks, which do not want to lend money to these SMEs because of the high unit cost.

However, by the end of 1997, the average percentage of loans to SMEs from commercial banks was 31.1%, and only two (Wantong and Baodao Commercial Banks) out of the seventeen newly established banks exceeded this percentage. Most of them lent out only 20% of their total loans to SMEs.³³⁹ In other words, most of the loans of these new banks go to big firms. The low share of loans to SMEs is partly due to the high unit cost of loaning to SMEs, and partly due to the new banks reluctance to join the 'Foundation of Guaranteeing SMEs' Credit' (中小企業信用保證基金), which is guaranteed by a government fund to lend out money to SMEs, according to an official at the Bureau of Monetary Affairs whom I interviewed.

Whenever the central bank reduces money supply and tightens the loans, it becomes hard for those marginal SMEs to borrow money from the new banks. In August 1995, an informant who usually obtains his capital from the private market, to which he has to pay 20% to 25% in annual interest rates, was informed by a newly established bank that he could borrow at the bank rate, which is never over 15%. But the financial crises of the credit unions and the following chain effect on farmers' associations made the new bank unable to give him any new loans, for the central bank tightened the money supply in response to the crisis.

Another influence of the new banks relates to the rise of interest rates in the private borrowing market. The ratio of the prime interest rate to the private borrowing rate was 2.5 in 1990, which increased to 2.8 in 1991, and 3.0 in 1992. After 1992, the ratio

³³⁸ Calculated from Jingjibu Zhongxiao Qiyechu (1995), *op. cit.*, p. 129, Table 4-2-2; Statistics Office, Bureau of Monetary Affairs, MOF (March 1998), *op. cit.*, pp. 18-22, Table 6.

³³⁹ See Finance Bureau, the Ministry of Finance, *Jinrong Yewu Tongji Jiyao* (金融業務統計輯要, A Summary Report on Financial Statistics) (Taipei: the Ministry of Finance, 1996). Cited from the Ministry of Economic Affairs, *84 Nian dui Zhongxiao Qiye Fudao Gaikuang Baogao* (民國八十四年度對中小企業輔導概況報告, Report on the Assistance Policy to SMEs in 1995) (Taipei: unpublished paper), p.86, Table 1.

remained at 3.3 without change³⁴⁰: in other words, the dual market is again restored to equilibrium. The establishment of new banks inevitably absorbs some capital in the private market, which reduces the supply of funds in the private market. So the ratio of prime interest rate and private market interest rate was raised, i.e., the interest rate in the private market is relatively high to attract more capital.

A new trend after the financial deregulation is that some land and stock speculators have begun to buy a milk cow, i.e., to buy a bank. They buy the shares of some financial institutions in the stock market so as control the operation of the bank. They then can influence the loan policy, and secure loans from their own bank to finance their speculations, especially in 1995, when most of their capital was trapped in sluggish land and stock markets. The most well-known such scandal is the case of the Overseas Chinese Commercial Bank, which was controlled by Liang Boxun (梁柏勳). Before he became the chairman of the board of the Overseas Chinese Commercial Bank, most of his loans were from certain public banks, where he used his power (mainly through his connections with the Provincial Governor James Soong, 宋楚瑜) to promote certain persons to key posts in the banks. After gaining control of the Overseas Chinese Commercial Bank, he loaned his *guanxi* companies NT\$3.5 billion (US\$140 million) from June to the end of November, 1995. Most of the loans up to the end of 1995 became bad debts.³⁴¹ Another case is the Taidong Small and Medium Business Bank, which was controlled by You Huaiyin (游淮銀). He lent out money to his several companies, which in turn put the money in his account in a commercial bank, which was his 'money laundry bank'.³⁴² More such potential cases could explode if this kind of 'privatisation of public interests' continues.

The contradiction of 'privatisation of profits and socialisation of costs' is rooted in Taiwan's specific political economy, i.e., the capitalist market and the populist authoritarian state. In a capitalist market, a badly-run company will be driven out of the market; however, if political force intervenes for political reasons, an uncompetitive

³⁴⁰ Calculated from *Taiwan Huobi yu Jinrong Lunwenji* (台灣貨幣與金融論文集) (Taipei: Lianjing Chuban Shiye, 1975), p.5, Table 4-2; *Zhonghua Minguo Taiwan Diqu Yinhang Jinrong Tongji Yuebao* (中華民國台灣地區金融統計月報, *Financial Statistics Monthly, Taiwan District, the Republic of China*) (Taipei: Economic Research Development, the Central Bank of China), from different years publications.

³⁴¹ See China Times, China Evening Times, 08, 09 January, 1996, p.3.

company can survive. Local faction-controlled financial institutions provide one example. The ruling party knows quite well that local factions are their bases to win votes in elections; however, the fall of any financial institution would cause more harm to its rule. At the moment, the ruling party tries to introduce market principles in the financial market, and hopes to reform these institutions step by step so that badly run credit unions or farmers associations could strengthen their competitiveness in the market. For example, it allows credit unions to change to commercial banks if the operations are well. By this way, the ruling party can still gain support of local factions, and at the same time prevent any criticism of bad management in the financial market.³⁴³

3.6 Conclusion

Contrary to most scholars' argument that SMEs need financial help from the government, an SME usually needs help only in its initial stage. Secondly, we found that the most common way to collect enough capital to establish a business is to use one's social relations: borrowing from family members and relatives, rotating credit associations and dowries, or cooperating with friends to form a partnership enterprise. However, this latter type of organisation usually does not last very long due to conflicts, including family firms organised by brothers or relatives. We found that a partnership company cannot survive long unless it is strongly led by one leader in a family, or mutual profit-sharing between partners. This type of business is initiated by *personal guanxi*, but usually ends in *conflicts of interest*. There is, again, always a tension between the profit-maximisation principle and the *guanxi* principle.

In this chapter, we have also examined the flow of working capital to small and medium-sized private enterprises. The source of capital consists of two parts, i.e., capital from the official financial market and private market. Compared to big companies, the capital source of SMEs from retained earnings and direct financing is much lower, while from trade credit and enterprises and households, which is regarded as the private market, it is much higher. A high percentage of SMEs using trade credit as financial

³⁴² This is heard from a friend working on the case.

³⁴³ See Bureau of Monetary Affairs, the Ministry of Finance, *The ROC Financial System and Policy* (我國金融制度與政策，八十三年修訂版) (Taipei: Bureau of Monetary Affairs, 1996), pp.62-63.

leverage due to the business practices shaped by the legal system (Bills Law). The reason why SMEs borrow a lot of money from enterprises and households is to evade tax. Since the share of loans to SMEs is equivalent to their shares of sales, and the percentage of total capital from financial institutions in total liabilities is almost the same as big firms, and least but not the last, since most private borrowings by SMEs is the item 'deposits received from shareholders', who want to earn higher interest and evade tax, we strongly doubt the claim made by many scholars that SMEs lack capital and so have to resort to the private market.

This kind of financial market is a mixed product of historical development, political control and market mechanism. It makes it hard for financial institutions to operate based on the profit-maximisation principle, and it reinforces the use of *guanxi* to get loans. Local political figures play a prominent role in mediating between money borrowers and money lenders.

Working capital is not a problem for those SMEs that are run well because they could use diverse financial tools to get credit: borrowing from shareholders, extension of trade credit, discounting their notes receivable or letters of credit. We found, instead, that SMEs want to borrow more money from the financial institutions so that they can evade tax. The government has implemented policies to supply more funds to SMEs, but obviously it created some space for them to exploit the system to maximise their self-interest.

Deregulation leaves more room for big firms to expand their territory into the financial markets. SMEs could benefit from deregulation to a certain degree, but those SMEs borrowing on the private market could not share the benefits. They even suffer from the crowding out effect in the financial market caused by the rising demand for capital.

Chapter 4: Marketing Management

4.0 Introduction

One popular image of the proprietors of Taiwan's SMEs is that they bring a suitcase, go overseas, attend an exhibition or visit customers, and try to persuade foreign buyers to put in an order. This image raises interesting questions: why do they go overseas to sell? How do they get in touch with the buyers? How do they market their products?

In this chapter, we will discuss where the markets are for SMEs' products, and why a certain kind of market distribution prevails. We will incorporate power relationships into our analysis to understand the use of *guanxi* and personal interactions in pursuit of profits in the business community. Different methods to sell products will be probed, and we will examine the interaction of social relations and market relations and discuss the function of price competition and its possible influence on personal interactions.

Two theories, social embeddedness theory and transaction theory, will be broached in my discussion, centring on the concept of *guanxi*. Social embeddedness theory tries to probe the bases of long-term relationships-- e.g., mutual trust and *guanxi*. However, as shall be seen, it cannot explain the disintegration of long-term relationships caused by market competition. Nor, as shall also be seen, can transaction theory explain adequately change and development in a relationship, for the theory is static and *a*-historical. First, however, in order to put our discussion into context, let us examine how Taiwan's SMEs have fared in the market at a macro -economic level.

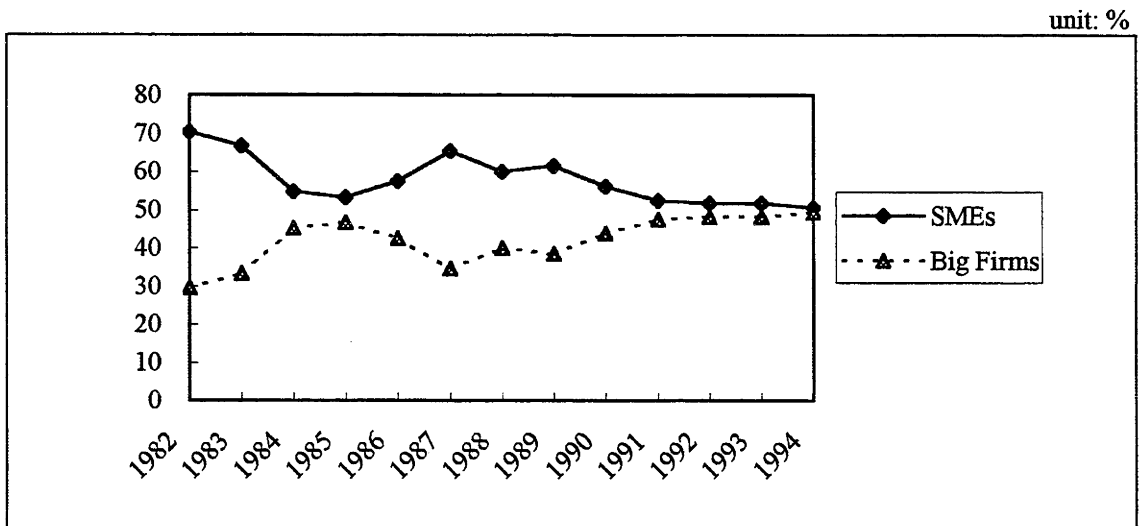
4.1 Outlets for SME Products

Figure 4.1 shows the contribution of SMEs to Taiwan's exports. The first thing to note is that the SMEs contribute more to sales in overseas markets than do big firms. However, after 1987, the year the New Taiwan Dollar started to appreciate, the SMEs' share began to decline, from 65.5% in 1987 to 50.6% in 1994. In 1996, the top 150 exporters mainly consisted of big electronics firms, comprising 32.7% of total exports.³⁴⁴

³⁴⁴ See Board of Foreign Trade (國際貿易局), *Woguo qian 150da Chukou Maoyishang yu Chukou Diqu, Chanpin Fenxi (Analysis of the Top 150 Exporters by Areas and Products, 我國前150大出口貿易商與出口地區、產品分析)* (Taipei: Board of Foreign Trade, 1997), unpublished paper. The data is from the

Yet the SMEs' share in Taiwan in the export market remains important as compared to Japan or Korea, where the top ten *Zaibatsu* or *Chaebol* handle more than a quarter of national trade.³⁴⁵

Figure 4.1 Share of SMEs and Big Firms in Export Markets, 1982-94



Source: Jingjibu (經濟部, Ministry of Economic Affairs), *Zhonghuaminguo Bashisi nian Zhongxiao Qiye Baipishu* (中華民國八十四年中小企業白皮書, *White Paper on Small and Medium-sized Enterprises in the Republic of China, 1995*) (Taipei: Ministry of Economic Affairs, 1996), p.48, Table 2-1-5.

The share of SMEs' sales is about one third of total sales, so we can use a simple way to calculate their share of exports in total sales (see Figure 4.2). In 1987, the overseas market absorbed about 77% of the SMEs' production, and the percentage declined gradually to 46% in 1994. The overseas market is not so significant for big firms, comprising a quarter to one-fifth of their total sales. Yet the SMEs' target market has changed notably, i.e., from overseas to domestic markets. Too, the SMEs' importance in the economy is declining, especially in the manufacturing sector, decreasing from 47% in 1986 to 37% in 1994.³⁴⁶

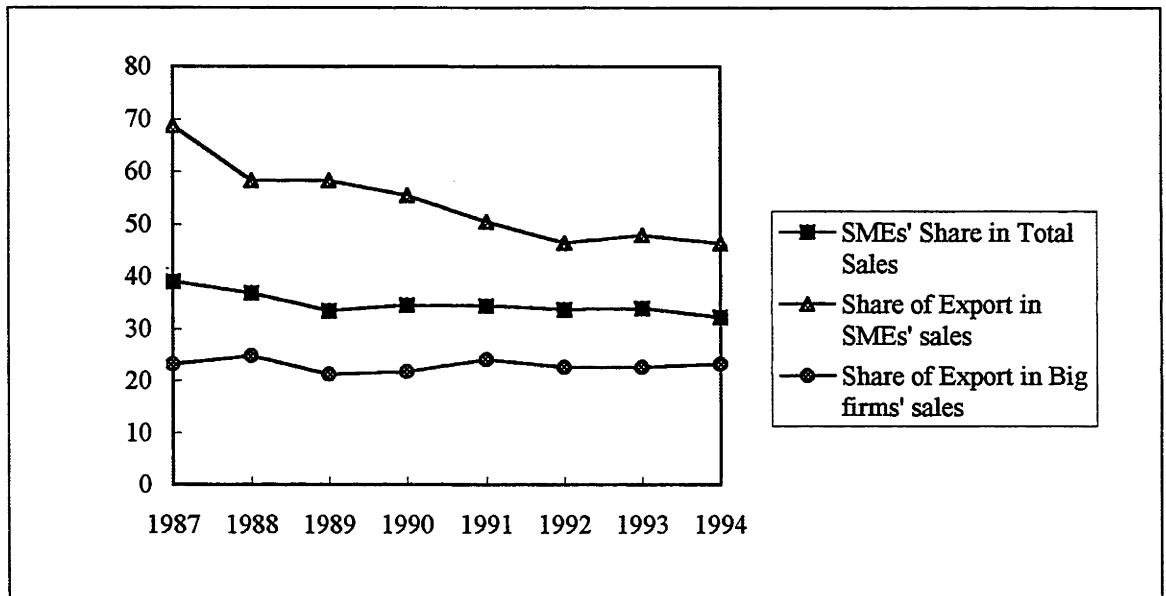
computerised import-export magnetic tape recording every company's capital, import and export products, value, unit price, destination. The top 150 exporters were selected as the analysis target, which is grouped as 'big firms', and the other companies are grouped as 'SMEs'. The definition is different from the definition of the Ministry of Economic Affairs, however, it tells something about Taiwan's export market at the enterprise level, which was never analysed before.

³⁴⁵ See ITC, *Survey of China's Foreign Trade—An analysis of China's export and import data at the enterprise level* (Geneva: International Trade Centre UNCTAD/WTO, 1995), p.15.

³⁴⁶ See Jingjibu (經濟部, Ministry of Economic Affairs), *Zhonghuaminguo Bashisi nian Zhongxiao Qiye Baipishu* (中華民國八十四年中小企業白皮書, *White Paper on Small and Medium-sized Enterprises in the Republic of China, 1995*) (Taipei: Ministry of Economic Affairs, 1995), p.372, Table 3-1.

To sum up, the domestic market is dominated by big firms, and the overseas market used to be the SMEs' arena, but gradually they have been overtaken by big firms. The big firms' power in the national economy is getting stronger.

Figure 4.2 The Share of Exports in SMEs' and Big Firms' Total Sales, 1987-94 unit: %



Source: Jingjibu (經濟部, Ministry of Economic Affairs), *Zhonghuaminguo Bashisi nian Zhongxiao Qiye Baipishu* (中華民國八十四年中小企業白皮書, *White Paper on Small and Medium-sized Enterprises in the Republic of China, 1995*) (Taipei: Ministry of Economic Affairs, 1996), p.48, Table 2-1-5; p.372, Table 3-1; Xingzhengyuan Zhujichu (行政院主計處, Directorate-General of Budget, Accounting and Statistics, Executive Yuan), *Zhonghua Minguo Taiwan Diqu Guomin Jingji Dongxiang Tongji Jibao* (中華民國台灣地區國民經濟動向統計季報, *Quarterly National Economic Trends, Taiwan Area, the Republic of China, 1997*), p.3, Table "Expenditures on GDP".

4.1.1 Historical Factors Affecting the Market Structures

Manufacturing and commerce are the two main industries in Taiwan. Their sales comprised, respectively, 45.3% and 35.8% of total sales in 1986. By 1994, however, the share of manufacturing was reduced to 32.9%, while commerce increased to 38.4%.³⁴⁷ In short, the relative importance of manufacturing industry is declining, and that of commerce is rising.

Though the SMEs have experienced similar economic structural changes in the manufacturing industry, their decline is faster. In 1986, the share of manufacturing sales in total SMEs' sales was 53.3%, which was reduced to 37.8% in 1994. For commerce, the share declined by only 1%, i.e., 35.4% in 1994 compared to 36.4% in 1986. The share

³⁴⁷ *Ibid*: p. 372, Table 3-1.

commanded by the construction industry gained during the period, from 2.9% to 17.1%, thanks to rising land prices after 1988.³⁴⁸

The SMEs' share of Taiwan's total commercial sales declined from 41% to 30% in this period, as the big firms expanded their operations in commerce. The above figures match the general picture outlined above: i.e., the big firms' influence has strengthened both in the domestic and overseas market in the past ten years.

Before the policy of economic 'internationalisation and liberalisation' in 1987,³⁴⁹ the domestic market was protected, and certain industries benefited a lot from this protectionist policy. The development of textile capital in the 1950s is a well-known case.³⁵⁰ Most of the present big business groups, including Yue Long (裕隆), Far Eastern (遠東), Jiixin Cement (嘉新水泥), Pacific (太平洋電線電纜), Tainan (台南幫), Xinguang (新光), and Tunex (東帝士), accumulated their initial capital in the 1950s with the help of an industrial policy to protect 'infant industry'.³⁵¹ It was the same in the petrochemical and cement industries: e.g., Formosa Plastics (台塑), Huaxia Haiwan (華夏海灣), Qimei (奇美), Changchun (長春), Taiwan Cement (台泥), and Dongnan Cement (東南水泥).³⁵²

The textile industry policy illustrates the protectionist policy which helped the big firms to dominate the domestic market. Shanghai textile capital had begun to flee with the Nationalist Party before the Communists took over the mainland in 1949. One informant relates that the Taiyuan Textile Company (台元), a major company in the Yue Long business group, had already utilised US aid funds to ship machinery to Taiwan when the

³⁴⁸ The sudden increase of construction industry in the share of total sales is partly caused by the new calculation method by the Ministry of Economic Affairs after 1990. See Ministry of Economic Affairs, *op. cit.*, p. 372, note.

³⁴⁹ See Board of Foreign Trade, *Foreign Trade Development of the Republic of China, 1995* (Taipei: Board of Foreign Trade, 1996), p.7.

³⁵⁰ See Thomas B. Gold, *State and Society in the Taiwan Miracle* (Armonk, New York/London: M. E. Sharpe, Inc., 1986), Chapter 5; Huang Dongzhi (黃東之), 'Taiwan zhi Fangzhi Gongye' (台灣之紡織工業, Taiwan's Textiles Industry), *Taiwan Yinhang Jikan* (台灣銀行季刊, *Taiwan Bank Quarterly*), vol. 7, no. 1, pp.10-11, 33; Lin Bangchong (林邦充), 'Taiwan Mianfangzhi Gongye Fazhan zhi Yanjiu' (台灣棉紡織工業發展之研究, Research on Taiwan Textiles Industry), *Taiwan Bank Quarterly*, vol. 20, no. 2, pp. 102-103; Liu Jinqing (劉進慶), *Sengo Taiwan Keizai Bunseki (Analysis of Post-war Taiwan Economy)* (Tokyo: The University of Tokyo Press, 1975), pp.213-233; Wang Hongzen (王宏仁), *Zhanhou Taiwan Siren Duzhan Ziben zhi Fazhan* (戰後台灣私人獨佔資本之發展, *The Development of Private Monopoly Capital in Post-war Taiwan*) (Taipei: unpublished Masters thesis, 1988), pp. 25-33.

³⁵¹ See Hongzen Wang, *Ibid.* pp. 25-29.

³⁵² *Ibid.* pp. 34-47.

United States still supported the Nationalist government in the civil war. The production capacity of the textile sector rapidly expanded after the Nationalist government retreated to Taiwan in 1949, and most new companies were from mainland China. Even after the amalgamation of native Taiwanese textile capital after 1954 into the Tainan Textile Company, the production capacity of thirteen Mainlander firms still comprised over two-thirds of the total textile production as of the end of 1962.³⁵³

After the outbreak of the Korean War the United States resumed her military and economic aid to the Nationalist government on Taiwan. Cotton was one of the most important materials for aiding the Taiwan economy. From 1951 to 1959 the total value of US aid cotton was \$139 million, about 16% of total economic aid.³⁵⁴ All the raw materials were rationed according to every firm's production capacity by the Economic Stabilisation Board.

How much benefit could one get for each bundle (470 pounds) of rationed cotton? The official price was NT\$4,150, but the black market price was triple that, i.e., NT\$13,000, and the finished product could be sold for up to NT\$26,000, meaning that if one could get one bundle of rationed cotton, one could earn over two million per month. The average income in 1953 was only NT\$7,722 per household per year (see Table 4.1). The price of farmland was about NT\$20,000 per *Jia* (甲).³⁵⁵

The big companies not only benefited from the supply of raw materials, they also got the lion's share of US financed loans. One informant complained that the hand-weaving firms could not borrow any money from the government at all, let alone get US AID loans: 'According to the local reports, most large private companies got help from US AID, but only a little reached the hands of smaller private firms'.³⁵⁶ As Thomas Gold has pointed out, 'Although officially anyone could apply for AID allotments, in practice mainlanders had an inside track, being familiar with procedures and having friends or relatives in the bureaucracy'.³⁵⁷ Another reason why most of the funds flowed to the large companies was

³⁵³ See Shi Minxiong (施敏雄) and Zhang Wenbo (張溫波), 'Taiwan de Fangzhi Gongye' (台灣的紡織工業, Taiwan's Textiles Industry), *Industry of Free China*, vol. 27, no. 6, pp. 2-11.

³⁵⁴ Calculated from Liu Jinqing, *Ibid.*, pp.220, 372.

³⁵⁵ One *jia* is about one hectare.

³⁵⁶ See Arthur F. Raper, *Taiwan zhi Chengshi yu Gongye* (台灣之城市與工業, *Urban and Industrial Taiwan—Crowded and Resourceful*) (Taipei: U.S. Mutual Security Mission to China and National Taiwan University, 1954), p.49.

³⁵⁷ See Thomas Gold, *op. cit.*, p. 70.

the Nationalist Party's policies. Some scholars have argued that the Nationalists preferred the development of small and medium-sized enterprises instead of large corporations because they wanted to prevent the emergence of 'corporate capitalism' on the one hand, and to create an 'unspoken alliance' on the other.³⁵⁸ But the leading industrial sectors in the first half of the 1950s were cement, textiles and plastics, and they were also the key planned industries in the Nationalists' First Four-Year Economic Plan.³⁵⁹ Only big companies had sufficient capital to operate in these industries. It is erroneous to say that the Nationalists preferred small and medium-sized enterprises from the very beginning. In 1954, a year of throat-cut competition and mergers between textile firms, Yin Zhongrong declared at a meeting that 'the government should encourage large firms to expand, to merge small firms. It is a natural tendency to perfect industrial development. From small to big, from many to few, the government can easily regulate the firms'.³⁶⁰ Another policy maker said that 'in the past few years, the government only paid attention to the development of some key industries and ignored the potential contributions of small and medium-sized enterprises for economic development'.³⁶¹

After 1953, the price of clothes and yarns dropped under the average weighted price and some firms were knocked out of the market.³⁶² To solve the problem of market saturation and encourage large firms to export, the government subsidised the big firms NT\$6 per US dollar of products that they exported.³⁶³ This delayed the pace of centralisation of textile capital, but in the economic recession of 1957-58, this occurred nonetheless.

³⁵⁸ See Hill Gates, 'Small Fortunes: Class and Society in Taiwan', in Dennis Fred Simon and Michael Y. M. Kau (eds.), *Taiwan: Beyond the Economic Miracle* (Armonk: M.E. Sharpe Inc), pp. 169-185.

³⁵⁹ See Zhang Guowei (張果為), *Taiwan Jingji Fazhan* (台灣經濟發展, *Economic Development in Taiwan*) (Taipei: Zhengzhong Publishing Co., 1967), p. 257, 786-795.

³⁶⁰ See Yin Zhongrong, *Wo Dui Taiwan Jingji de Kanfa* (我對台灣經濟的看法, *My Opinion of the Taiwan Economy*) (Taipei: Self-Publishing, 1954), p. 30.

³⁶¹ See Zhao Jichang (趙既昌), *Geguo Zhongxiao Qiye Fuzhi Cuoshi yu Women Nuli de Fangxiang* (各國中小企業扶植措施與我們努力的方向, SMEs support policies in other countries and what we should do), p.11, in Zhao Jichang (ed.), *Geguo Zhongxiao Qiye Fudao Cuoshi* (各國中小企業扶植措施, *SMEs Support Policies in Other Countries*) (Taipei: Guoji Jingji Ziliao Zhongxin, 1965), pp.1-14.

³⁶² See Huang Dongzhi, *op. cit.*, p. 30.

³⁶³ See Lin Bangchong, *op. cit.*

Table 4.1 Household Income Distribution, 1953

unit: NT\$, %

Household Income	Percentage of Household	Cumulative Percentage	Percentage of Total Income	Cumulative Income
1,600	23	23	3.5	3.5
5,010	37.9	60.9	17.3	20.8
9,000	14.6	75.5	12.2	33.0
13,000	8.1	83.6	10	43.0
18,000	5.5	89.1	9.3	52.3
24,000	3.6	92.7	8.3	60.6
31,000	2.6	95.3	7.7	68.3
42,000	1.9	97.2	7.6	75.9
59,000	1.2	98.4	6.9	82.8
85,000	0.8	99.2	6.5	89.3
120,000	0.5	99.7	5.9	95.2
145,000	0.3	100	4.8	100.0

Source: See Zhang Guowei (張果為), 'Minguo Sishier Nian Taiwan Geren Suode Fenpei zhi Guji' (民國四十二年台灣個人所得分配之估計, Estimation of Taiwan Income Distribution in 1953), in 'Zhang Guowei Jiaoshou Taiwan Jingji Lunwenji' (張果為教授台灣經濟論文集, Essays on Taiwan Economy from Professor Zhang Guo-wei) (Taipei: Chinese Cultural College, 1980), pp. 45-85.

From July 1957 to June 1958, about two hundred companies went into bankruptcy. It was widely believed that heavy taxes, usury, a reduced supply of credit and a limited domestic market were to blame.³⁶⁴ To find an outlet for surplus capital, large firms began to dump their products in the domestic market. One informant said that "the large firms' technology was at least ten years more advanced than ours and the quality of their products was much better than the small firms so that no small firm could survive if the large firms began to have a price war". The informant's wife added that during that period, as competitive pressures began to squeeze out small firms, she had to carry clothes from their own firm to sell in the streets, just like a street peddler. The market share of the large firms jumped from 50% to 90%.

The problem that textile capital faced was no longer technology, finance or taxes, but the market. Other industries had the same problem. For example, the cement industry had to export 18.5% of its total production after 1957 because of over-capacity.³⁶⁵ Since the domestic market was saturated, the only outlet for surplus capital was to export. But the

³⁶⁴ See Liu Jinqing, *op. cit.*, p. 250.

³⁶⁵ See Jiang Jingyi (蔣靜一), 'Taiwan zhi Shuini Gongye' (台灣之水泥工業, Taiwan's Cement Industry), in Bank of Taiwan (ed.), *Taiwan zhi Gongye Lunwen Jijuan 2* (台灣之工業論文集, Essays on Taiwan Industries, no. 2) (Taipei: Bank of Taiwan, 1958), p. 48.

foreign exchange rate system 'punished' exporting firms. For example, in June 1957, a firm that exported US\$1 of products could receive in exchange NT\$28.99, while the black market price for one US dollar was NT\$38.58, so whenever one US dollar of goods was exported, the firm was denied about 10 yuan of earnings, i.e., one-third of the export income.³⁶⁶

Between 1958 and 1963, the government initiated several reforms to correct the price distortions so as to create a congenial environment for exports. Starting in 1958 the Nationalist government reformed its dual foreign exchange rates system gradually, and reached a single exchange rate in September 1963.³⁶⁷ The reform created an environment for exports and opened a new era for Taiwan's economic development.³⁶⁸ It enabled a lot of SMEs to prosper in the years of an expanding international economy in the 1960s. In 1972, the share of the overseas market in SMEs' sales was 56%.³⁶⁹ The figure increased steadily to a peak of 69% in 1987, and then declined gradually. However, the government did not really want to deregulate the market and ease restrictions on imports. It relied increasingly on tariffs instead of quotas to protect the domestic market. Especially the level of protection for most intermediate and capital goods remained high throughout the 1960s to 1980s.³⁷⁰ Because the big firms had power over the domestic market, this kind of import-restriction policy left the domestic market untouched, and the dual market structure was more firmly established, i.e., the big firms dominated the domestic market, and the SMEs specialised in the export market.

Different factors facilitated Taiwan exports of all kinds of low-skill products to the US: the General Special Preference Customs System, which gives less developed countries special customs preferences; increasing domestic consumption stimulated by USA government fiscal policy; American multinationals in Asia exporting products back to the US for their mother companies (i.e., intra-firm trade increased); the diversified taste of American domestic consumption for different levels of goods; and the trade disputes

³⁶⁶ See Samuel P. S. Ho, *Economic development of Taiwan, 1860-1970* (New Haven and London: Yale University Press, 1978), p. 395, Table A66. The table charts the detailed changes in official exchange rates.

³⁶⁷ *Ibid.*: pp.195-196.

³⁶⁸ See Liu Jinqing, *op. cit.*, p. 247.

³⁶⁹ See MOEA, *Zhongxiao Qiye Shichang Xingxiao zhi Yanjiu* (中小企業市場行銷之研究, *Studies on SMEs' Marketing Management*) (Taipei: MOEA, 1992), p.16, Table 2-8.

³⁷⁰ See Samuel Ho, *op. cit.*, p.196.

between Japan and the US opened niches for products that Japan could not export.³⁷¹

4.1.2 Emerging International Factors Changing the Market Structures in the 1980s

This market structure remained unchanged until the impact of international economic forces emerging from the globalisation trend in the 1980s. Before 1986, the trade pattern was to import basic components from Japan, assemble products in Taiwan, and then export them to the US.³⁷² The expanding exports to the US market enabled Taiwan to accumulate huge foreign reserves in the first half of the 1980s (see Figure 4.3), but the value of the Taiwan dollar did not change at all, which means that it was undervalued.³⁷³

In 1985, the G5 countries agreed to let the US dollar depreciate against other main currencies.³⁷⁴ In 1986, the US began to put pressure on Taiwan to appreciate the Taiwan dollar in the name of fair trade. The exchange rate was changed from 1:40 to 1:28 in two years, which means that the cost calculations based on the old exchange rate increased 42.8% in terms of the Taiwan dollar. It drove many SMEs out of the market. Figures 4.1 and 4.2 show that the SMEs no more were a major player in the export market. On the other hand, the pressure from the US to open Taiwan's domestic market and to reduce custom tariffs, plus the increased purchasing power of the New Taiwan Dollar due to the depreciation of the US dollar, led to significantly increased imports, (see Figure 4.3). This also made it more difficult for SMEs to compete in the domestic market.

At the same time, the huge accumulated foreign reserves were converted into an increased money supply, and with the cost of manufactured products rising on export markets, there was no incentive to invest the money in manufacturing industry. Almost all of the money flowed into speculative business, i.e., land speculation, the stock market and the underground financial market, which produced a bubble economy. Land prices rose sky-high. This bubble economy reached a peak in 1990, and afterwards land and stock

³⁷¹ See Akira Suehiro, *Ajia Kougyouka no Dainamizumu (The Dynamics of Asian Industrialisation)*, in Akira Kudo (ed.), *Nijisseiki Shihonshyugi II (Twentieth-Century Capitalism II)* (Tokyo: University of Tokyo Press, 1995), pp. 172-176.

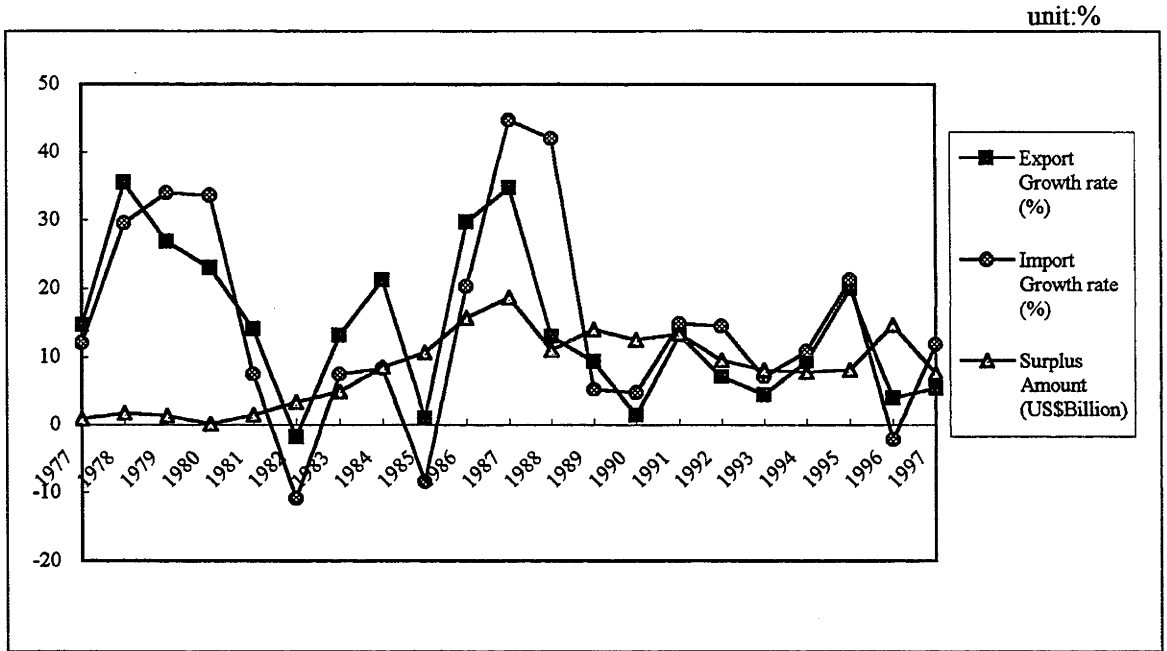
³⁷² The trend changes a little after 1986 after the sharp rise of Taiwan dollar, but even though, in 1995, export to US market totalled 26.4% of Taiwan's total export, dropped from 38.2% in 1986. Import from Japan keeps unchanged in the past decade, around 30% of total import. See Board of Foreign Trade, *op. cit.*, pp. 25, 27, Table 8, 9.

³⁷³ See Council for Economic Planning and Development, *Taiwan Statistical Data Book, 1996* (Taipei: Council for Economic Planning and Development, 1997), p.187, 150.

³⁷⁴ See Fuji Sougou Kenkyushyo, *Hiyakusuru TouAzia to Nihon--Raibaru ka Patona ka? (The Rising East Asia and Japan--Rival or Partner?)* (Tokyo: Fuji Sougou Kenkyushyo, 1994), p.4.

prices have been sluggish for years.

Figure 4. 3 Export and Import Growth Rates, 1986-96



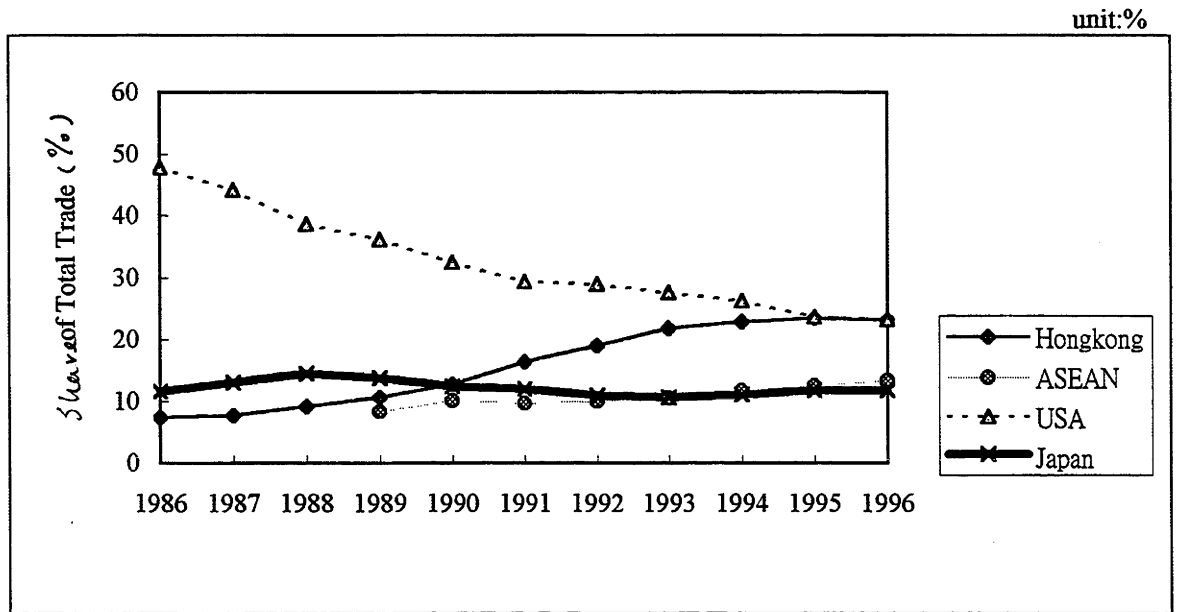
Source: Board of Foreign Trade, *Foreign Trade Development of the Republic of China 1996* (Taipei: Board of Foreign Trade, 1997), p.9.

To deal with the unprecedented economic situation, SMEs had to adopt new measures. One way was to try to find an overseas country with cheap labour and land to continue their production. Accompanying the eased tension with China, the shift of Taiwanese production bases to Southeast Asia and China has produced the so-called ‘investment-induced trade effect’. The increased investment into the two regions has greatly changed the trade patterns of Taiwan. Figure 4.4 shows that the US and the Japanese markets have gradually been taken over by Hong Kong and ASEAN firms. According to research by Taiwan’s Board of Foreign Trade, the relative importance of SMEs in ASEAN export market is higher than in the EU and Japan. The share of the top one hundred and fifty exporters in the ASEAN and Hong Kong market was 33% and 23% respectively in 1996, and the other smaller exporters had 67% and 77% shares, which is much higher as compared to their 56% share in the EU, and 61% in Japan.³⁷⁵ This ‘investment-induced trade’ pattern caused by the capital exports of SMEs also happens in

³⁷⁵ See Board of Foreign Trade, *Woguo qian 150 da Chukou Maoyishang yu Chukou Diqu, Chanpin Fenxi* (Analysis of the Top 150 Exporters by Areas and Products, 我國前150大出口貿易商與出口地區、產

Japan and Korea, and this 'convergence' is the result of globalisation, which helps the development of the larger regional economy.³⁷⁶

Figure 4. 4 Shares of Four Major Exporting Regions in Total Trade



Source: Board of Foreign Trade, *Foreign Trade Development of the Republic of China 1996* (Taipei: Board of Foreign Trade, 1997), pp.22-31.

Note: Currently ASEAN consists of 7 member countries including Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei, and Vietnam. The data before 1996 does not include trade data with Vietnam.

The transformation of Taiwan's political economy produced a brand new milieu for SMEs. In the coming sections, I will discuss how businesspeople utilise market principles based on price competition and *guanxi* based on personal contacts to gain orders. We also will be concerned with how social relationships are affected by the market principle. The two questions I will discuss first are the types of power relationships which are central to *guanxi*, and how such behaviour could be altered under political and economic change.

4.2 Types of Power Relationships

It is widely believed that the Chinese like to utilise *guanxi* to promote their business. If one possesses eight *guanxi* networks, and on average have four friends in each *guanxi*

品分析) (Taipei: Board of Foreign Trade, unpublished paper, 1997), p. 2.

³⁷⁶ See Klaus Schwab and Claude Smadja, "Power and Policy: the New Economic World Order", in *Harvard Business Review*, Nov-Dec., pp.40-50.

network, and if each one of these friends also has thirty-two friends, then one has $32 \times 32 \times 32 = 32,768$ direct and indirect contacts within three circles. So it is not a problem of finding a type of *guanxi* to use, but the problem of how to ‘pull and utilise’ (利用) it. When we talk about pulling and utilising (or more subtly, exploiting) *guanxi*, it is already implied that there is a power relationship in *guanxi*. Such a power relationship is constructed by multiple forces and not absolute, so each of the parties involved in the relationship has to adjust him or herself in a dynamic relationship.

Before discussing *guanxi*-utilisation, let me explain three different types of power relationships to clarify what sort of *guanxi* we are talking about. I will take one case of a publishing company to study the possible power relationships.

The books the publishing company produces can be sold through different marketing channels. One possible channel is to sell them directly to bookshops. In this situation, the relationship between the publishing company and a bookstore is a *pure market relationship*.³⁷⁷ The bookstore places its orders according to consumers’ demand. The second marketing channel is aimed at school libraries. In 1994 the Ministry of Education subsidised primary and high school libraries 100 million Taiwan dollars to buy ‘good’ books selected by the Government Information Office (新聞局). So the publishing companies strove to have their books on the list. Because the Government Information Office does not want to displease any publishing company, usually some books of every publishing company will be put on the list. So the main focus is in the second round: how to get orders from school libraries. Because the school principal holds the power to decide on the order, publishing companies have to spend a lot of time with the principals. Publishing companies normally have a list of principals’ names, addresses, telephone numbers and school budgets. An interviewee told me that he has to go out dining every day with a different principal. But such ‘dining-out’ social activity does not guarantee the order. More important is a ‘commission’, i.e., the publishing company gives back a certain percentage of its sales into the principal’s pocket. The market price of such a commission most often is 10%.

Another way to sell the books is to go to schools or government offices. Usually the

³⁷⁷ Here I do not mean that a market contractual relationship could exist without any kind of pre-existing social relationships. It is more appropriate to say that the two sides bargain irregardless of the existing social relations.

publishing company asks for a place to exhibit its books for a week, and the company's salesman tries to persuade white-collar staff to place their orders, or to give students a sheet filled with books titles, which is distributed by teachers in class, and to ask students to take these home to ask their parents' permission to tick off what books they want to buy. The next week the students hand the sheet to the teacher, and then the salesman goes to collect the sheets from teachers. Because schools are not supposed to be a 'profit-seeking' area, any kind of commercial activity requires the approval of the principal. In order to access this big market, which accounts for 15% of total sales, every publishing company has to 'deal with' the school principal. Obviously, the relationships between the publishing company and the school principal are not pure contractual market relationships, for the head is not a consumer nor does the company treat the head as a potential final consumer.

All the three types of *guanxi* relate to power relationships. In the first situation, the power relationship is on an equal basis. A bookshop will not order books from a publisher if there is no demand, so the two parties' relationship depends on a market demand-supply situation. I call this kind of relationship a *horizontal power relationship*. Another case is the supply side of the labour market, where a lot of labourers compete with each other for a job offered by an employer. In this case, there is conflict between workers, but there is no problem of domination. This situation conforms to neo-classical economics' pure competitive model which views every human relationship as a market relationship.

These kinds of horizontal power relationships are exhibited in the private capitalist economy, and its basic rules are exemplified in the three principles of civil law: freedom of contract, individual free will and property rights. Because the market is the only arbitrator, and the firm is only one of numerous competitors in the market, so any kind of personal ties would not help it to have any advantage against others. The only way for a firm to survive in the market is 'rationalisation'. Basically the bulk of small and medium-sized enterprises in Taiwan have to face this kind of power relationship: to compete with each other to win orders from the competitive world market. Some scholars like to emphasise how important Chinese *guanxi* is in doing business, but obviously it is not important in this kind of horizontal power relationship.

The second kind of *guanxi* we discussed above is not based on an equal, free relationship. This type of relationship could be counted as a kind of market, but not a perfect competitive market where every firm is free to enter and to exit. The school

principal holds the money, and he decides how to ration the money for different books. If the principal decided to buy A publishing company's products instead of B's, B could do very little to counterbalance the principal's decision. So no wonder the publishers have to spend so much time in establishing relationships with a school's principal. The *guanxi* is based on a patron-client relationship, and I would call this kind of relationship a *vertical power relationship*. Such relationships can be found in capital-labour, male-female, central politician- local politicians relationships.

Under the vertical power relationships, two parties interact on an unequal basis, and the weak is dominated by the powerful, so the weak, in order to profit for him/herself, must exploit every kind of means to keep good relationships with the powerful. Businesspeople are facing those who hold resources. They compete with other book publishers to offer better terms to the principal. To gain from the relationships one must show the other party that it is profitable for both if they keep up the relationship. How to transform the existing 'non-profitable' *guanxi* to mutual benefits becomes a very important business activity. Businesspeople in Taiwan have to face different structural constraints, so they have to 'pull *guanxi*' in every kind of business sphere.

Before the democratisation process in the mid-1980s, most corrupt activities were covered up to maintain an image of an upright government. At that time, knowing key persons had a lot of benefits: firstly, to gain loans from strictly controlled financial institutions; secondly, to get access to public purchases; thirdly, to evade tax; and finally to get preferential legal interpretations of codes. This kind of vertical power relationship is what most scholars would refer to as '*guanxi*'. But obviously this kind of specific power relationship is produced in specific political structures. After the democratisation period, such political-business relationships are not as tolerated any longer. By the force of public opinion and the opposition parties, a lot of illegal affairs were exposed, which gave bureaucrats a clear lesson: they have to do their work more according to the law. An interviewee commented on this kind of bureaucratic change: as compared to the 1960s, political corruption had lessened. In the 1960s, he had had to spend money on bribes to buy a manufacturing firm licence, and now he said he did not have to bribe any longer to obtain bureaucratic approvals.

In the third situation, a school principal or the head of an organisation holds the power to enter the market. S/he is not the resources' owner, but only a gatekeeper.

Institutions occupy the positions to control entry to the market. But on the other hand, we can see that there is a norm regulating which institutions are classified as able to compete in the market, and which are not. In other words, not every social institution is allowed to engage in free market exchange.

There are some specific areas where market principles are not allowed to function. Karl Polanyi says that certain mechanisms exist to protect the society from a pure market economy, such as public education which is not a 'natural result' of the market's functioning.³⁷⁸ Society assigns these kinds of institutions certain roles and functions which follow different rules from capitalist calculations. Other institutions like social help networks, compulsory military service, or religious institutions are all related to certain social value systems which might conflict with capitalist principles. In James O'Connor's terms, it is the contradiction of accumulation and legitimacy.³⁷⁹ The case of the publishing company that wants to sell its products in schools expresses this kind of contradiction: the company follows the rules of the market, i.e., to maximise its profits, under the constraints set by social norms. This situation can be seen from the street vendors who appropriate public space, like roads, sidewalks and parks, as their own private business space; or salesmen of rehabilitation equipment who intrude into hospital wards to sell their products without permission from patients or hospitals. There are more controversial issues like opening a casino in Penghu, issuing a lottery, setting condom-selling machines on campus, or allowing businesspeople to invest in China freely. We can see that certain goals and values contradict the profit-maximisation principle, and all these values either adjust to market rules or stick to separate rules. This could be named a *societal power relationship*.

A firm in capitalist society has to face these three kinds of power relationships. To maximise its profits is the basic tenet in capitalist society, and a firm has to adjust its role under different power relationships. I will discuss below how SMEs access the market under the three different power relationships.

4.3 Price Competition in a Competitive World Market

In neo-classical economics, price is the only indicator to match sellers and buyers.

³⁷⁸ See Karl Polanyi /tr. by 黃樹民, 石佳音, 廖文生譯, *The Great Transformation--Origins of Our Time*. (中文: 鉅變: 當代政治經濟的起源) (Taipei: Yuanliu Chubanshe, 1957/1989), p.289.

³⁷⁹ See James O'Connor, *The Fiscal Crisis of the State* (New York: St. Martin's Press, 1973), pp.1-10.

The dynamic process, according to this theory, is that all firms in the pure competitive market will not have 'excess profits' over the long term because if there is excess profit, the market will attract other firms to join to compete, and this will bring on a price war. If one firm, say T, lowers its price, another firm, J, will follow suit, or it will be knocked out of the market. If both of them reduce their price, their profit will be reduced. In the long run, the market will restore to an equilibrium where no firm has 'excess profits', and every firm will only get its 'normal profit'.

This kind of analysis to a certain degree matches Taiwan's trade development. If we assume that the world market is a pure competitive market, and Taiwan is one of the many suppliers in the market, and there are numerous SMEs in the market, we can use the terms of trade³⁸⁰ to represent the relative price of Taiwan's exported products. If the index is under one hundred, it means that the exported product is relatively cheaper, for the world price is one hundred at the moment, and the export price is less than one hundred. The lower the index, the cheaper the exported products. During the first half of the 1980s, the index was as low as seventy-five, which means that Taiwan's exported products were relatively cheap in the world market.³⁸¹ As we noted in the previous section, the New Taiwan Dollar was greatly undervalued during this time so the export price remained low, and exports increased, especially into the US market.

Another way to strengthen competitiveness is to raise productivity through the introduction of new technology. Rising productivity will enable the firm to reduce the product's price and to embark on a price war. Taiwan's technology is not so advanced as the Japanese, but Taiwanese firms sometimes have their own grass-roots R&D to keep up with the Japanese. The firm of one of my interviewees invented a machine to produce a special type of screw. Before the invention, the manufacturing firm had to import such machinery from Germany or Japan, which cost at least NT\$2 million, and the speed of manufacture was two hundred screws per minute. In 1989 the partner of the informant invented a machine which cost less than NT\$600,000, and it can produce a hundred and twenty screws per minute. This machine became very popular among firms that produced

³⁸⁰ Terms of Trade is the relative price index of imported and exported products. We divide the export price by the import price to get the index. If the value is more than one, it means that the price of exported products is relatively expensive compared to the price of imports.

³⁸¹ See Council for Economic Planning and Development, *Taiwan Statistical Data Book* (Taipei: Council for Economic Planning and Development, 1997), p.185, Table 11-2a. The 1991 constant price is 100.

this special type of screw, and after a price war, the Japanese overseas market was taken over by the Taiwanese in a short time. The informant said that 'my secretary received NT\$3 million (about US\$110,000) in 1990 as her bonus'.

However, the Taiwanese believe that 'if they can make it, I can', so after two years, another company in Taichung invented a similar machine to produce the same products. Competition drove down the price, and when more and more companies devised the machines, the production capacity multiplied overnight, and the price also plummeted. After the break of the partnership, the informant tried to find a new product to sell in order to avoid the fierce competition, but his partner kept on producing the same product, and two years later his partner's company went bankrupt due to price competition.

Another is the so-called 'non-price competition', e.g., the design of a product. Intellectual property rights is a new concept to Taiwanese, and before the US pressed the Taiwan government to protect American firms' interests in intellectual property rights, almost every company copied the most popular product design, and manufactured the same product at a lower price. The owner of a firm that produced pupil's reference books described the situation: in the old days, he copied the popular design of Japanese children's books, and tried to become a leader in the Taiwan children's book market. However, if one of his books was popular in the market, many other publishers would join in to compete with a similar books. At that time, there was a time lag before similar products appeared in the market, and he could keep one year ahead of other publishers, each time creating a new product for the coming year. However, the time lag becomes shorter and shorter, and when I interviewed him the time lag had been reduced to only one month.

A survey done in 1984 shows that about half of the SMEs that exported products (2,770 cases) complained that their competitors adopted a 'cut-throat pricing strategy'.³⁸² This situation has not changed, according to a macro-survey conducted by the MOEA in 1995, which also shows that about half of the interviewed firms (4,913 cases) think that the major marketing problem they face is 'cut-throat competition' from domestic firms. Among the firms that hired more than three hundred workers, 37% faced this problem, while 50% of the firms that employed fewer than ninety-nine workers believed that their

³⁸² See Board of Foreign Trade, *Zhongxiao Qiye Waixiao Daoxiang Chengzhang Diaocha Yanjiu Baogao* (中小企業外銷導向成長調查研究報告, Research on SMEs' Export Growth) (Taipei: Board of Foreign Trade, 1984), p.53, Table 4-3.

major marketing problem is 'throat-cut competition'.³⁸³ In other words, the smaller the firm is, the more competitive their product market is.

According to neo-classical economic theory, to deal with this harsh competition, companies can raise their productivity, either through mechanisation or rationalisation of production or overseas production. If they cannot adjust, they must exit the market. This reasoning is based on the assumption that efficiency and therefore the cost of production is the only determining factor in the market. However, we would argue that there are two non-economic ways to deal with competition, i.e., power manoeuvres and the establishment of long-term relationships, which are inextricably linked with the social structure. Our main concern here is now, under the specific Taiwan social structure, businesspeople sell their product through *guanxi*, or more precisely, through power relationships.

4.4 Economic and Political Power Manoeuvres

Neo-classical economists just notice the competition between suppliers, but they fail to see the power relationships in the market. This kind of manoeuvre can result from economic or political control.

As observed above, a price war could result from the pure competition between supplying firms. But it could also result from manoeuvres on the demand side. For example, it is a common business trick to tell one supplier that another supplier would produce it at a lower price so that the buyer will bring down the price. An informant said that in 1972 he successfully invented a new machine to produce iron tubes. An American importer tried to benefit by manipulating suppliers from Taiwan and Japan. He told the Japanese producer that Taiwan can produce this product at a lower cost. At the same time the American told the Taiwan company that the Japanese would take his order at a lower price. If he refused to accept the order, his firm would not be able to operate, so he had to engage in a price war. Through this kind of manipulation, the price war lasted over five years.

At that time he would have liked to cooperate with the Japanese firm to end the price war, but the Japanese firm believed that it could outlast him in the war, so it was not until

³⁸³ See MOEA, *Zhonghuaminguo Taiwan Diqu Zhizaoye Jingying Shikuang Yixiang Diaocha Baogao* (中華民國台灣地區製造業經營實況意向調查報告, *Survey Report on the Business Practices of Manufacturing Industry*) (Taipei: MOEA, 1995), pp.36-37, Table 7.

five years later that the Japanese firm offered to end the war. From then on they made an agreement that both would not accept the orders under a certain price, and agreed to a division of labour, i.e., he produced certain kinds of products, and the Japanese produced others. Before long the sales price began to rise.

This case shows us a kind of power relationship different from what neo-classical economics teaches us. Before J and T's cooperation, the relationships between A and J, T were vertical, and A could use his power to manipulate J and T, while the relationships between J and T remained competitive. But after cooperation was achieved, the triangular relationship turned into a dual relationship. Through their cooperation, J and T prevented any further price war and were able to change the 'market forces'.

As another example, a major effort by an interviewee's company has been to get the work to make a concrete tunnel for electric-power wire for Taipower (台灣電力公司, Taiwan Power Co.). There are about twenty companies who are eligible to bid for the work from Taipower, so they collaborate with each other throughout the island. Before the bidding, all of the firms had to reach an agreement on the price, and then every local company bid for the work in different regions. The firm can keep part of the money to cover its costs and a certain portion of the money as its profit, but then the rest of the money has to be distributed to other firms equally. These business practices are relationships that are perfectly fitted to a market.

Neo-classical economics might say that there would be a free-rider so that this kind of collusion would not last long, like the cartel of the OPEC. However, an organisation could use different methods to discipline its members. In the case mentioned above, the organisation could lobby the government to stop issuing licenses so that no potential competitor could enter the market. The second way is to use 'moral persuasion', a term used by the informant, to prevent the emergence of free-riders. If it does not work, violence could be the last resort.

Normally, the kind of vertical control relationship happens in the product distribution channel when one party controls access to a specific market. One informant produced ventilation fans, and most of the products reached customers through the wholesale chain store, Makro. But quite often Makro sold the product at the price lower than the production price to attract customers, which inevitably toppled the price structure constructed by different channels. He said that he had no choice but to cut the supply and

tried to find another channel. An American importer 'fed' an informant, i.e., the importer gave him a lot of orders, and step by step, the exporter had to rely on the importer's marketing channel. The informant said that after he found that his sales relied more and more on the importer, up to 40% of his total sales, he became vigilant, and tried to diversify his market. When the importer asked him to reduce the product's price and he refused, he still could survive the hard time while he sought new marketing networks for his products.

Another kind of power manoeuvre relies upon political influence, which is different from the economic domination mentioned above. In Taiwan, some public works are given to certain companies only. For example, 'important, national defence related' public construction is still put out to the construction department of the National Veterans Association (退輔會), which is a conglomerate operating all kinds of business activities.³⁸⁴ Such a conglomerate becomes an institution to protect the Mainlanders' economic interests, because most veterans are Mainlanders. They are granted the monopoly right to operate lots of commercial activities, and then in turn put out the jobs granted from the government to smaller firms, and earn the transfer profits without doing anything. For SMEs to get an order from the Association, they are subordinated to the gatekeeper who controls access to the market. Unless they change to another market, they have to rely on the Association, and to enter into a patron-client relationship.

The Association has a Taipei Service Centre. A retired general, who is a good friend of an informant's father, is in charge of the organisation. At that time, all construction work from Taipower was assigned to the Association, so the general occupied a good position to control Taipower's public construction work. Through good *guanxi* with the general, the informant was able to sell cement products to Taipower.

If the government's policy were not biased to favour retired Mainlander soldiers, the National Veterans Association would not have had the power to take this important public work; if the informant were not Mainlander, or his father had not known the general, the informant would not have had the opportunity to win a contract from Taipower; if the staff in Taipower had not been corrupt, they would have reported the collusive behaviour to the

³⁸⁴ This semi-official company was founded by special funds in the late 1950s, and owns 26 different kinds of companies. Because it is not public enterprise, it enjoys the independent financial status, and is a main financial source for KMT. See Chen Shimeng, Lin Zhongzheng, Chu Jingyi, Zhang Chingxi, Shi Junji and Liu Jintian, *Jiegou Dangguo Zibenzhuyi—lun Taiwan Guanying Shiye zhi Mingyinghua (Deconstruct Party-State Capitalism—On Privatisation of Taiwan Official Enterprises)* (Taipei: Chengshe Baogao 1,

Investigation Bureau. All these kinds of power manoeuvres are produced in a certain social context, and would not be sustained in another social structure. We could say that the degree of the transparency of the policy-making process determines the possibility of forming a closed shop. If certain kinds of information are not available for most people, it will be easy to form a closed relationship. In Taiwan, the prevailing closed social networks that can be used to access information and a corrupt government bureaucracy reinforce the difficulty to enter a relationship. Power manoeuvres become possible under this social structure, and *guanxi* becomes necessary.

4.5 Long-term Relationships--How to Balance Cost and Benefit

The second way to deal with market competition is to establish long-term relationships between buyers and sellers. Obviously any business practice to a certain degree should be based on mutual trust, a kind of collective conscience described by Emile Durkheim.³⁸⁵ The world division of labour, or commodity chains, as Geriffe described, must be based on some reliable networks.³⁸⁶ This is why many sociologists like to emphasise the social bases of economic functions.³⁸⁷

Social networks (*guanxi*) are the basis of such analyses. Research has that found *xinyong* (credit, reliability or trustworthiness) is very important in doing business. The impression also gets imparted that people living within the Chinese cultural context can

1991), p. 67.

³⁸⁵ See Emile Durkheim/ tr. by 王力行, *De la division du travail social* (社會分工論, Social Division of Labour) (Taipei: Shangwu Shudian, 1966).

³⁸⁶ See Gereffi, Gary, Miguel Korzenienicz, Commodity Chains and Footwear Exports. In William G. Martin (ed.), *Semiperipheral States in the World-Economy* (Westport, CT: Greenwood Press, 1990), pp.45-68.

³⁸⁷ See Wong Siu-lun, 'Chinese Entrepreneurs and Business Trust', in Gary G. Hamilton (ed.), *Business Networks and Economic Development in East and Southeast Asia*, (Centre of Asian Studies, University of Hong Kong 1991), p. 15; Thomas Menkhoff, *Trade Routes, Trust and Trading Networks: Chinese Family-Based Trading Firms in Singapore and Their External Economic Dealings*, unpublished PhD dissertation (1990), Faculty of Sociology, University of Bielefeld; Kao Cheng-Shu, 'Personal Trust in Taiwan Business', in Gary G. Hamilton (ed.), *op. cit.*, pp. 66-76; Susan Greenhalgh, 'Networks and Their Nodes: Urban Society on Taiwan', *China Quarterly*, no.99 (September 1984), pp. 529-552; Chen Jiexuan, *Xieli Wangluo yu Renji Wangluo--Taiwan Zhongxiao Qiye De Shehui Jingji Fenxi* (Subcontracting and Personal Networks--social economic analysis of Taiwan's small and medium-scale enterprises) (Taipei: Lianjing Chubanshe, 1994). Chen Jieying, 'Taiwan Zhongxiao Qiye Lingxihua Ziben Jiegou de Shehui Jichu' (The Social Base of the Fragmented Capital of Taiwan's SMEs), *Si yu Yan* (Thought and Words--Journal of the Humanities and Social Science Quarterly), vol. 30, no.3, pp.59-86; Chen Jieying, 'Taiwan Zhongxiao Qiye Jingyan Quxiang Jishu Leiji Moshi de Shehui Jichu' (The Social Base of the Accumulated Experience in Technology Procurement in Taiwan's SMEs), in Zai Benrui (翟本瑞)(ed.), *Taiwan Shehui yu Jingji Lunji* (Collection on Taiwan Society and Economy) (Taipei: Youshi Chubanshe, 1995),

access another part of the cultural repertoire—Chinese *guanxi*— to serve as a guarantee in business.³⁸⁸

This ‘cultural approach’ is partially correct. Many informants also emphasised this point when they talked about their business practices. In most transactions they do not need to sign any formal contract. But we should note that this business practice is not based on traditional merits. Both sides must benefit from this long-term relationship, or it will not work out.

Some Taiwan scholars try to construct different types of *guanxi* to analyse Taiwan businesspeople’s behaviour.³⁸⁹ In "flexible production networks", in "social engagement to gain orders or to secure a loan", all kinds of business activities are based on “Chinese *guanxi* networks, which are combined with business practicality and a human touch” (現實與人情). What they define as *guanxi* is quite ambiguous, for it includes every kind of interaction. If so, we can say that every business has to use its personal contacts to establish business relationships, which are combined with calculations of interest and specific social customs. This kind of behaviour is not confined to China or to business, but also applied to Japan and the USA, or to political clientelism, where social customs are only complementary to pursuits of power.³⁹⁰

4.5.1 Building and Utilizing Social Closure

Karl Polanyi argued that economic life is not organised by a self-regulating market; so, too, the labour market in capitalist society is also not regulated by market principles only. Social networks, or social closure, play an important role. Following I will discuss the formation of social closure and long-term relationships, and more important, I will talk about the factors which might cause the disintegration of the social networks or long-term relationships. The problem of how to establish and maintain a long-term relationship which involves both parties’ interests is more important than the typology of *guanxi*.

pp.293-322.

³⁸⁸ See literature review in Introduction Chapter.

³⁸⁹ This kind of approach is widely adopted by the researchers at Tunghai University. They set up a research centre to study the business behaviour in East Asia. See Kao Chengshu, Chen Jiexuan, Chen Jieying *et. al.*

³⁹⁰ See Hongzen Wang, ‘Dui Chen Jiexuan xian sheng “Guanxi yu Faling” de yidian Yijian’ (對於陳介玄先生“關係與法令”的一點看法, A Brief Comment on Chen Chieh-hsuan's "Personal Connections and Legal Rules: A Traditional Dimension in Taiwan Business", *Si yu Yan* (思與言, *Thought and Words—Journal of the Humanities and Social Science Quarterly*), 1993, vol. 31, no. 2, pp. 247-250.

Research done by Egan and Mody shows that American buyers prefer long-term, stable, and direct relationships with both developed and developing country suppliers.³⁹¹ They also report that ‘developing countries’ firms may find it more difficult to enter relationships and thereby break into industry networks....they may find they are increasingly unable to get their first orders’.³⁹²

The situation they describe applies not only to the newly developing countries, but also to a new company which wants access to the market. One’s family could be helpful in this. One informant produces components in Tainan, and exports most of his products. He has two boys, and he has already begun to plan their careers. Whenever he goes overseas to visit his foreign distributors, he takes his two boys with him, and introduces them to the distributors’ children. ‘It will become the two kids’ capital, and will be helpful to their future business’, he explained.

However, not everyone is lucky enough to have a ‘good family’ or ‘useful’ social relations to utilise. Those excluded from a network have to find a way to access the network, which is called ‘*guanxi*-pulling’ (拉關係). Nevertheless, one who wants to “pull” *guanxi* has to be able to offer benefits to the other party, or it is hard for one to cut into a *guanxi*.

In Chapter Two, we have shown that the mobility path for Taiwanese is that one works for a while before marries, and after marriage, one tries to open a business of one’s own and become a proprietor. The first phase could be called a ‘network building period’, which is viewed by Taiwanese as a necessary process. One utilises one’s early working experience to know more ‘friends’ for future business. An informant hired a secretary to receive foreign guests: ‘After two years, she quit the job, set up her own trading company, and took away one of our biggest customers’.

In a broader sense, all networks can be one’s capital. Besides the family ties one can utilise, one can also utilise broader social relations. An obvious commercial activity to mobilise social relations so as to make money is direct selling. In his research on Taiwan’s direct selling, Pei-Chia Lan found that, besides turning to their immediate social relations to sell products, more important ways among direct salespersons to make money are to

³⁹¹ See Mary Lou Egan and Ashoka Mody, ‘Buyer-Seller Links in Export Development’, *World Development*, vol.20, No. 3 (1992), p.325.

³⁹² *Ibid.*: p.329.

‘activate their *remote* networks, create new networks with strangers, and further, transform these social networks’.³⁹³ One’s immediate social circle is too small to find big potential buyers. A salesperson has to expand his social relations hips. Lan found that strangers or remote friends are “better” customers than close friends.³⁹⁴

Another kind of social relations that can be utilised is clientelism, which is the kind of social closure that limits certain people’s access. Hans Schenk finds that in clientelist relationships in India, for instance, only if the lower caste offers the upper caste certain benefits can they be included in clientelist relationships.³⁹⁵ The dual political clientelism in Taiwan gives certain people power to gain an economic rent, and only those people who give support to the patrons could access the network. For example, to find a job in a farmers’ association requires help from local politicians, who control the local institutions. It will be difficult for anyone who is not in the circle to get a post. Even in central government offices, the kinds of posts that do not require qualifications are usually occupied by high-ranked officials’ relatives or friends.³⁹⁶ An informant sells kitchen wares, whose two main marketing channels are construction sites and retail stores. The formal channel has a much higher share of his sales. A legislator, who owns a big construction company in Taoyuan, ran in a political campaign in 1992, and the informant had to support and help him to win the election in order to gain orders from the legislator’s company. This kind of social closure is more or less based on the concept of reciprocity. One party gives support, either economic or political, and the other party provides economic benefits. It is an “interests community” (*Interesse Gemeidschaft*), where self-interests bind them together, much as neo-classical economics assumes.

Big firms usually do not have problems in using *guanxi* to market their products. They have a public relations department to promote relationships with all relevant parties, and the hig-ranking managers often have good relationships with the most important people in the society such as the club of *Jinshi* (金石) and *Qingsong* (青松), which count many important people among their members.

³⁹³ See Pei-Chia Lan, ‘*Disciplinary Capitalism: Networking Power and Emotional Labor in Direct Selling*’, unpublished paper presented at North American Taiwan Study Conference Austin (June 1998), p. 13.

³⁹⁴ *Ibid*: p. 14.

³⁹⁵ See Schenk, Hans, ‘Corruption--What Corruption? Notes on Bribery and Dependency in Urban India’, in Peter M. Ward (ed.) *Corruption, Development, and Inequality* (London: Routledge, 1989) pp. 110-122.

³⁹⁶ No data is available on this point. But one popular joke is that one can offend one’s boss, but never offend those low-ranked employees who had attained their positions without passing the state examination,

Smaller companies have to establish new relationships step by step, and need to use competitive offers such as low prices. An informant who processes iron products observes that doing business depends on *jiaoqing* (交情, friendship, or personal relationships), but if one wants to enter a business, s/he has to use price competition to gain orders. Normally the buyer will tell the supplier how much the cost is, and asks the supplier to offer a price less than the prevailing price, at the same quality, or the supplier will not place an order. In this way, one can establish a business relationship with the other party step by step. The research done by Egan and Mody concurs. They note that 'relationships tend to grow incrementally, with their duration and depth more evident *ex post* than *ex ante*.'³⁹⁷

Even though social closure is based on mutual trust and reciprocity, the market situation still influence the relationships. One informant's first overseas customer was Australian, and their relationship persisted for over ten years. Even after the sharp rise of production costs in Taiwan after 1987, his buyer still placed orders with him. For both of them, these orders were not at all profitable, but they tried to maintain this relationship so far as possible. After 1990, his Australian buyer had to switch his orders to China, and he said that both of them felt relieved. Their relationship in the beginning was based on profit-calculation, but later it developed into a relationship of mutual trust and reciprocity but under the pressure of prices, even though both of them tried to keep the relationship going, it became hard to maintain it without mutual benefits.

We know that an economic system is linked by different sectors, and if a link of the chain breaks, the economy will be dysfunctioning: car manufacturing needs thousands of different spare parts, and any problem with the production of components will cause an interruption in car-making. The centre-satellite production system organised by a lot of firms is a kind of long-term relationship which tries to minimise the instability of procurements of spare parts from the centre firms and of the quality of components supplied by satellite firms.

A case studied by the Taiwan government shows that a close tie between the centre and satellite firms has helped this industrial network grow and profit over the past fifteen years. Taiwan Liwei (台灣麗偉) contracts with about one hundred and fifty satellite firms to produce machinery. Liwei supplies raw materials, machine modules and technology to

and who are too well connected to offend.

satellite firms, and the satellite firms assemble the final products. Whenever Liwei devises a new model, it will train the satellite firms, and teach them how to use the new technology to assemble parts for it. The two sides meet once weekly to discuss the problems in production, quality control and information on new technology. Through this kind of intensive interaction, they are able to produce internationally competitive machinery.³⁹⁸

Though this subcontracting system is maintained on the basis of mutual trust and benefits, if some do not follow the rules, e.g., to keep up the good quality of their products, it will create problems for the centre company. So a subcontracting system will work better if there are pecuniary rewards in the system. 'When a firm subcontracts its products, it will find subcontractors with good reputations (信用好) to do the work', an informant noted. 'It is not a problem to control the quality of put-out products, for the upstream subcontractor will check the product produced by the downstream firm. If the quality of the downstream firm is not good, the upstream firm would not accept it. If it had been accepted, and could not pass my quality control, the firm would not be able to get the money from me, and at the same time would have to pay money to the downstream firm.' In other words, the company uses a 'mutual monitoring' mechanism to guarantee quality, which also ensures the functioning of the reciprocal rewards system.

A second way to avoid the dilemma of keeping a good relationship with partner businesses is to avoid doing business with close friends or relatives. To use an earlier example, the direct salespersons in Taiwan sell more to strangers and remote friends because when a salesperson tries to make money from a friend, s/he has to run the risk of losing the friends.³⁹⁹ Only strangers or remote friends will not give this kind of social pressure on the businessperson.

4.5.2 Disintegration of Social Closure and Relations

The kind of long-term economic relationship mentioned above is more or less based on mutual trust and reciprocity, with the help of economic calculations. This reciprocity is not like a clientelist relationship, where power relationships are unequal, yet long-term

³⁹⁷ *Ibid.*: p.326.

³⁹⁸ See Jingjibu (經濟部, Ministry of Economic Affairs), *Zhonghuaminguo Bashisi nian Zhongxiao Qiye Baipishu* (中華民國八十四年中小企業白皮書, *White Paper on Small and Medium-sized Enterprises in the Republic of China, 1996*) (Taipei: Ministry of Economic Affairs, 1996), pp.216-219.

³⁹⁹ See Pei-chia Lan, *op. cit.*, p. 14.

economic relationships have the same troubles that clientelist relationships face, i.e., how to balance assets and liabilities. The cases of partnerships that we discussed in Chapter Three suggest that even a long-term established network is fragile. Market relations can interfere with one's social relations, and one has to find a way to accommodate both.

In a capitalist economy, 'meeting that product's *quality* specifications at a competitive *price* and adhering to reliable *delivery* standards are minimum requirements for selling in the market.'⁴⁰⁰ A firm that cannot meet the minimum requirements will not be able to sustain any long-term relationship. No buyer can stand, over the long term, high-cost products, as in the case of the Australian buyer. Another informant had run a shoe manufacturing company, but the oil crisis in 1973 drove up the cost of PVC raw materials by 80%, and he could not bear the high cost. He had to close his firm, even though many 'overseas lines' had cooperated with him for a long time.

Even family-based networks can be unreliable, even though one has full information about one's family members. In 1983, four million Taiwan dollars (about US\$150,000) that an informant had lent to his sister and uncle were in default, and the rest of his savings of one million Taiwan dollars was also in default to a friend. "That is because I over-trust others", he commented. Another informant organised a club with ten other companies, and they have a financial credit network with each other. But one company ran into difficulty in 1995 and this company could not pay back six million dollars to her (about US\$230,000) because of an economic recession. They still have business deals, but their relationship has been changed into a 'more pure market relationship', and since then they have not maintained any social functions with each other. The two cases illustrate that one has to fulfill one's social role in a market, and one's asset, i.e., one's social network, is also one's liability. Both of the two informants played their social roles (brother and friend), and were asked to lend money not following any market principle, i.e., economic calculation, but when another party is not able to fulfill their obligation (to pay back the money), their social relations could not be sustained.

What if the social closure or long-term relationships break down after the intervention of market forces? In Taiwan, this used to be resolved by social pressure or violence, and not through a legal system. But in an increasingly internationalised economy, it is harder to use these old means.

What is critical is how to maintain social networks which are in trouble. Often such relationships terminate with no further connections. If so, the question is how to claim back one's money. The 'victims' would like to retrieve their money, but the other side may not have sufficient money to pay back the debt, or even if they have, prefer not to pay it back. So before making any business commitment, e.g., to loan, to sell or to buy, one has to bear the risk and must be prepared for a default. One has to calculate, if the other business fails, what sorts of means are available to claim back the money. One way is to go to court and ask for legal restitution. But the political system interferes with the judiciary, so even if one could have legal restitution, it might take years, which is too high a cost for businesspeople. This knowledge contributes to the phenomenon that in Taiwan's business community, it is rare to sign a contract, as mentioned. It shows that there is no trust in the legal system.

Social pressure is used as the second way to claim back a debt. In a modern legal system, every legal subject is independent of each other. But obviously the social institutions do not function in that way. In Taiwan, the view persists that members in a family belong to one family instead of being many different independent legal subjects. Every member is supposed to share duties in common for their family. So one's family is usually regarded as one's business guarantor.

Before the amendment of the Bills Law in 1988 it was a criminal offense if one bounced a check, for the state wanted to enforce transactions. Quite often a company's legal owner was the wife, and the manager was the husband. The company used the wife's personal cheques to do business with other companies. If this company went broke and cheques bounced, the wife would be put in jail instead of the 'real' owner, the husband. One female informant recalled that her husband told her that she knew much more about finance so that she should be board chairman, and used her name to issue cheques. After they separated she suddenly realised why her husband wanted her to be board chairperson.

Why do people accept this kind of cheque which is not the real owner's? Because people believe that a family is a community where everyone is supposed to share responsibility. One case is the "European Community Market Building", which was built and sold by Huang Jinzhou (黃錦洲). He failed in his financial investments and fled with the money to Canada. He owed investors about NT\$20 billion (about US\$750 million). Later he committed suicide in Canada. Creditors asked his family, mainly his sister, to clear

⁴⁰⁰ See Egan and Mody, *op. cit.*, p. 321. *Italics added by author.*

the debts. His sister promised that she would do her best to clear off the debts, though she has no legal responsibility at all.⁴⁰¹

This kind of social pressure to secure transactions work in a community-based or 'relationship' society, but urbanisation, the prevalent nuclear family system, and the internationalisation of capital flows reduces the influence of traditional community pressure. Besides, people are better educated and know how to use the law to escape from the negative side of traditional values.

Another means is to use force to take back money. The final resort to the law is of course also based on force, i.e., to use state power to implement the law.⁴⁰² But if the state power fails to protect transactions, and social pressure is ineffective, the last method is private violence, i.e., to ask a gangster to resolve a dispute.

The influence of criminal elements in Taiwan is widely known. In 1995, the speaker of Pindong county council shot dead a businessperson over their business disputes. The speaker of Gaoxiong county council was shot to death by a township representative in the same county because of business conflicts. According to a report, over 80% of local council representatives have criminal records.⁴⁰³ In an unpublished internal official document, the Minister of Justice admitted that five wanted gangsters and the wives of another two gangsters were elected as county representatives in January 1998.

In previous decades, these gangsters were under strict supervision by the state. But after the lifting of martial law and democratisation, that power no longer prevails. They are entitled to campaign for political posts. At the same time, the KMT party tries to cooperate with them to keep its power, so the gangsters' influence has expanded.

A successful gangster often has his own business, mainly in land speculation and government project bids.⁴⁰⁴ He also tries to make money by 'solving disputes' between people. This becomes an important way for people to secure their debts. One informant said that when he faced a situation where he could not claim back debts owned to him, he went to court to claim NT\$500,000. The jury recommended he settle out of court, for if he

⁴⁰¹ See *Ziyou Shibao* (自由時報, Liberty Times), Huang Jinzhou Dajie: Mama Di Jia Jixiaoshi jiu Yuhai... (黃錦洲大姐：媽媽抵加幾小時就遇害, Huang Jinzhou's eldest sister: Mother was victimised few hours after she arrived Canada.) 08 January 1996, p.3.

⁴⁰² See Max Weber, *Politik als Beruf (The Profession and Vocation of Politics)*. In Peter Lassman and Ronald Speirs (eds.), *Weber's Political Writings*, p.310. He said that every State is founded on force.

⁴⁰³ See Chen Dongsheng, *Jinquan Chengshi (Money & Power City)* (Taipei: Juliu Chubanshe, 1995), p. 68.

⁴⁰⁴ See *Gongshang Shibao* (Commercial Times), *Weibiao Huati Zaocheng Huati Weibiao* (圖標話題造成

sued, in the end he might get only NT\$5,000 back. A friend introduced him to a criminal investigation police officer to settle the case. The policeman asked a gangster to demand the money. The debtor had no money, but had a house valued at NT\$1.7 million. So the informant paid 0.9 million to the debtor, and the policeman and gangster also charged 0.3 million from the debtor, and the informant obtained the house. Another informant took back 50% of his NT\$60,000 debt with the help of a gangster. But 'the aftermath never ends', as he described it, 'for the gangster came back over and over again to ask for money, and asked me to find *jobs*'.

However, social order cannot be built upon violence. In the near future, the resort to traditional social pressures will need to be replaced by the establishment of trust in the legal system, because it is increasingly unfeasible to resort to the old communal forms any more and the 'rule of gangsters' is not a realistic alternative for the business community. After the first direct election of Taiwan's president in 1996, Lee Teng-hui had tried hard to solve the 'gangster-money' complex (黑金政治) by enforcing implementation of the law. Though the KMT's power derives partially from the support of corrupt local factions, it may not survive politically if it keeps a close relationship with them. The KMT has to respond to popular demands, and in the coming few years, the dilemma--to solicit support from local factions or from the people--may dominate the tactical agenda.

4.6 State Regulations and Societal Power

It is possible today to lobby to alter planned regulations. Usually the government has to choose between different interests. In the process of enacting National Health Insurance (全民健保), for instance, the government had to resist the pressure from the business community and implemented the project earlier than planned.⁴⁰⁵ The policy to prohibit business investment in China has also evoked enormous resistance; many important business community leaders criticised the policy as 'reducing Taiwan's competitiveness in the world'.

According to the Statute Governing Relations between the People of Taiwan and the Mainland Areas (兩岸人民關係條例), a company investing in China has to report to the

話題圍標, *Exclusion topic makes topic exclusive*, 05 May 1996, p.22.

⁴⁰⁵ See Tang Wenhui (唐文慧), 'The Political Processes of National Health Insurance Initiation in Taiwan', *American Asian Studies* (forthcoming, 1998).

Investment Commission or it will be fined; however, the investments reported to the Taiwan government in 1995 are only one third of the amount shown in Chinese statistics.⁴⁰⁶ One informant who invested in a shoe manufacturing company in Fuzhou said that he had been to China before the government allowed people to travel there. In 1989, at the time of the Tiananmen Massacre, he had been planning to build a factory for the past three years. He analysed the situation, and believed that the Chinese government would not change its 'opening' policy, and that it might now give greater benefits to foreign capital in order to attract investment and reduce the negative image from which it suffered. He kept to his plan, and built a factory that employs more than five thousand workers. He told me proudly that 'about one third of Nike's shoes are made by our company'.

This kind of business activity had an impact on the government's policy, and in September 1990, the Taiwan government relaxed the law to allow Taiwan business to invest in China 'indirectly' if the amount is under US\$1 million. Businesspeople can touch the 'untouchable' and push the government into changing policy.

Though businesspeople are able to lobby the government to change its policy, the regulations of overseas governments are beyond the control of Taiwan's businesspeople. Other nations control access to their domestic market, either through tariffs or non-tariff barriers, in order to protect domestic industry. So the export-oriented SMEs have to pay attention to the international economic milieu, since their business could easily be affected by any policy change by foreign governments.

A common industry policy adopted by an overseas government is to restrict the import of semi-finished goods so that domestic industry could develop the ability to produce industrial components, which have a higher price in the world market. The manager of a Taiwanese firm producing umbrellas, which invests in China, said that it exports basic components from Taiwan, processes the umbrellas in China, and leaves the last processing step, i.e., attaching the handle of the umbrella, to be finished in Taiwan, so that they could export the product from China as a semi-finished product and enjoy the tax incentive program offered by the Chinese government.

Another informant complained that his marketing channel is controlled by another

⁴⁰⁶ Taiwan's statistics show US\$1.09 billion, while China's is US\$3.16. See MOEA, *Liang'an Jingmao Guanxi Fazhan zhi Tanta* (兩岸經貿關係發展之探討, Exploration on Economic and Trade Development Across the Taiwan Strait) (Taipei: MOEA unpublished paper, 1997), p.14.

Taiwan company, for business orders from Southeast Asia flow to that company. The informant could not export his product to Southeast Asia countries separately because the tariff was as high as 30% for semi-finished products, and was taxed at only 10% for finished goods. Another company used his products to assemble a finished machine to export, so the informant had to depend on that company.

A new issue at the WTO is to discuss the anti-dumping policy adopted by the United States.⁴⁰⁷ It is often regarded as a kind of protectionist policy for American domestic industry. One informant benefited a lot from American policy to levy anti-dumping tariffs on iron tubing in the period from 1979 to 1981, and from 1987 to 1991, for Japanese and Brazilian products. Products from the two countries were levied a 50% anti-dumping tax, while Taiwan's tariff was only 6.58%. He said that the market vacuum opened by the tariff against Japan was 'too big to swallow'.

However, the market protection measures of tariff barriers are no longer acceptable to the international economic community. A more subtle way to protect 'national industry' is to use the terms of 'fair trade', 'human rights' or 'labour issues' to bar certain goods from certain countries. In the near future, these issues will become major disputes between developed and developing countries, and SMEs will have to face a 'social charge' from their target market, especially from Western countries.⁴⁰⁸

4.7 'Guanxi' and Long-Term Relationships

Some scholars emphasise the importance of *guanxi* networks in the Chinese business community, and quite often this social network is regarded a kind of 'social capital', as if the broader the network, the more capital one owns.⁴⁰⁹ Gary Hamilton and Kao Cheng-shu write that in Taiwan 'The relationships defined by the roles tend to be stable over the long run. They are based on reciprocal trust, loyalty and predictability'.⁴¹⁰ But their hypothesis

⁴⁰⁷ See Board of Foreign Trade, *WTO Xinjiapo Buzhangji Huiyi Zhanwang (WTO 新加坡部長級會議展望, Outlook of WTO's Ministerial Conference in Singapore)* (Taipei: Board of Foreign Trade, unpublished paper, 1996).

⁴⁰⁸ See Hongzen Wang (1997), *op. cit.*, pp. 160-161.

⁴⁰⁹ See Jane Kaufman Winn, 'Not by Rule of Law: Mediating State-Society Relations in Taiwan through the Underground Economy', in Murray A. Rubinstein (ed.), *The Other Taiwan—1945 to the Present*. (Armonk, New York: M.E. Sharpe, 1994), pp.204-209; Gary G. Hamilton and Kao Cheng-shu, "The Institutional Foundations of Chinese Business: The Family Firm in Taiwan," *Comparative Social Research*, vol. 12, 1990, p. 145.

⁴¹⁰ Gary G. Hamilton and Kao Cheng-shu, *op. cit.*, p. 145.

ignores the fact that this specific social closure is formed under a specific Taiwan social formation, which can be transformed or destroyed by newly arisen social forces. The price competition, the power manoeuvres or the rise of a new party can change the shape of social closure. A firm that used a social relationship to gain orders from a public organ has to face competition from outsiders, in a democracy or free economy, as in the case of the cement company that sold products to Taipower. Competitors wrote letters to the Ministry of Justice Investigation Bureau to ask for an investigation into its collusive monopoly. Accompanying the process of democratisation, the earlier corruption can no longer be tolerated, and the *interest community* comes under great pressure to disintegrate. In 1996, strong public opinion regarding corruption in a new airport construction project forced the government to take actions to investigate it, and also forced a KMT party-owned enterprise to pull out of the bidding.⁴¹¹

Secondly, the broader one's social network is, the more obligations one has to bear. It is like the balance sheet, where assets are always equal to liability plus equity. The network will collapse if one could not fulfill her/his duty. A Taiwanese saying is that 'it is more difficult to pay back a *renqing* debt' (人情債難還). People instead prefer to use pecuniary rewards to pay back what they owe.

Regarding the existence of long-term relationships, transaction theory tries to explain the contradictions between short-term profit-maximisation (struggles between buyers and sellers and between themselves) and long-term personal trust in terms of economic cost. This theory argues that every transaction will incur a cost: for example, to acquire credit, to know the quality of one's products, to quote prices, etc. All these kinds of costs will be marked up into a product's price. But if buyers and sellers have established long-term relationships, many costs would be saved and hence reduce the cost and price. Based on this incentive, a long-term social network would help to reduce the whole transaction cost. This can also be applied to industrial organisation. For example, clothes can be finished in a firm, or be put out and finished by many firms. Which organisation of production is used depends on the total cost one form or another will incur.

The problem with this theory is that it is tautological and static: tautological, because

⁴¹¹ This situation is like the history Karl Polanyi interpreted, but in the opposite way, that the anti-self-regulating market movements were spontaneous in order to protect different groups' own interests. People who are deprived the right to access certain profits would gather together to fight for their interests.

what exists becomes reasonable to be labelled as a cost reduction; and what does not exist is therefore deemed to be comparatively high cost; static, because there is no analysis of dynamic processes in this theory.⁴¹² When it says that the existing social networks reduce transaction costs, it just says the existing social system is the best up to now, but says nothing about how it evolved and where it will be going. We would like to know the dynamic development of the social institutions, but their reply will be only: when the transaction cost is changed, they will be changed. For example, many informants said that the subcontracting of shoe and textile production in Taiwan did not appear until the mid-1970s, and before that time, any newly increased orders were met by expanding the production scale.⁴¹³ How do we explain this change? They might say because of the rising costs to produce within a firm, the institutions had to change to a subcontracting system. But then why do both forms exist at the same time after the 1970s? Since the concept of cost is too broad to include everything, we have no idea what are the most important factors in evaluating transaction costs.⁴¹⁴

Not all relationships are long-term, and not all long-term relationships are close. Step by step, a short-term relationship could be changed into a long-term relationship; and too, step by step, a long-term relationship can be transformed and destroyed. A relationship is dynamic and developmental, and people in the relationship have to balance the assets and liabilities. It is not governed by economic calculations only, nor by social relations only, but a dynamic result of the two forces.

So transaction cost theory tells us one side of the story, i.e., that economic links, both short-term and long-term, are organised along the principle of minimum cost, but this does not tell us what sorts of social institutions are employed to assign everyone a role to play and to provide mechanisms to guarantee the transactions' security. It is always assumed

⁴¹² This is the basic problem of neo-classical economic analysis, which uses comparative equilibrium to explain change, and once the world reaches equilibrium, it will never change. So 'in the long run', we would all reach an equilibrium, where market efficiency would govern our life.

⁴¹³ Also see the survey done by a Japanese scholar in the first half 1970s on bike-manufacturing, who found that the subcontracting system was not well developed because of less developed industrial linkages. See Take Mizuno (水野武), 'Chusho Kigyo no Shihon Yushitsu--Taiwan ni Okeru Kemikarushyuzu Seizogyo no Shirei wo Chuxin to shite' (中小企業 no 資本輸出--台湾 ni Okeru Kemikarushyuzu 製造業 no 事例 wo 中心 to shite, SMEs' capital export--the case of the chemical shoes industry in Taiwan) (Tokyo: Yuhikaku, 1973), p.200.

⁴¹⁴ Douglass C. North tries to analyse the evolution of social institutions by the concept of transaction costs. He told us to find out those factors which changed the transaction costs of institutional arrangements. If so, we cannot see any important factor in the theory at all. See Douglass C. North, *Institutions, Institutional*

that the modern legal system is able to do this, but we have argued that other institutions, such as social pressure arising from social relations, or gangsters, are much more important to provide security to transactions. Besides, transaction theory cannot explain the structural changes caused by the profit-pursuing activities, like the lifting of controls on Taiwanese investment in China, or the demand to privatise public enterprises.

In contrast with transaction theory, the cultural approach, as in the Taiwanese scholars' explanation of Taiwan's development, tells another side of the story, but this story is also static and *a*-historical. The 'Chinese way' of marketing is like an 'orientalist concept', which excludes the common experience of capitalist society, i.e., the market forces that can destroy a long-term established social network.⁴¹⁵ Both of the theories are partially correct, but not wholly.

4.8 Conclusion

Meeting a product's quality specifications, at a competitive price, and adhering to reliable delivery standards are the three minimum requirements for selling in the market. Without these, there can be no co-operation or long-term relationship. That is business.

However, one might not be able to sell one's product in a market even if a company can meet the three requirements. Political and economic power manoeuvres, and certain forms of closures can result in a barrier to market entry. These kinds of closures are produced in certain social contexts which cannot be reproduced elsewhere. I have explored the close cooperation between big firms and the government in the 1950s, which resulted in a segregated market: big firms specialised in the domestic market, while SMEs sold their products overseas. In the late 1980s, the international political and economic forces opened the domestic market, and pushed the big firms to sell more overseas. The relative importance of the American and Japanese markets for Taiwanese SMEs was gradually replaced by China and ASEAN.

The concept of 'embeddedness' used by some scholars expounds this point.⁴¹⁶ Many

Change and Economic Performance (Cambridge: Cambridge University Press, 1990).

⁴¹⁵ For Karl Polanyi, the tragedy the industrial revolution brought is not the lowering of living standards, but the destruction of the traditional community, a kind of cultural disaster for the working class. See Karl Polanyi, *op. cit.*, pp. 271-289.

⁴¹⁶ See Mark Granovetter and Richard Swedberg, 'Introduction to the Sociology of Economic Life', in Mark Granovetter and Richard Swedberg (eds.), *The Sociology of Economic Life* (Boulder, San Francisco, Oxford: Westview Press, 1992), pp.1-26.

Taiwan scholars like to use the concept '*guanxi*' to depict this business closure in Taiwan. I have argued that the prevalent utilisation of *guanxi* resulted from a specific social milieu, and not so much the innate cultural traits of Chinese businesspeople. Pulling *guanxi* is important because it enables businesspeople to make profits. Because the *guanxi* is based on mutual interests, it is dynamic and developmental. Following Polanyi's analysis of capitalist society, I have argued that 'the economy is directed by market prices and nothing but market prices, where human beings behave in such a way as to achieve maximum money gains'.⁴¹⁷ The prevailing market forces intervene in social relations, and even though there are social closures and long-term relationships, they can disintegrate due to differences of interest. The pursuit of profits not only influences personal interactions and relationships, it also pushes the state to conform to the market trends. When Karl Marx wrote that capitalist forces are in some ways progressive, he meant that individuals transformed feudal social values when they were driven to pursue individual profits. From this viewpoint, we can understand the role of businesspeople in Taiwan's democratisation process: when there was an interest for them to maintain the system, they collaborated with the ruling party; when there are conflicts of interest, they would break the rules without hesitation. A businessperson has to exploit his *guanxi* to make profits, but at the same time s/he is sometimes unconsciously testing and chipping away at the existing social order, as with the government's 'Go Slowly Toward China' policy, which often has been challenged by the business community.

All transactions must be based on mutual trust to a certain degree, and this kind of trust is underpinned by law, or social pressure, or private violence. Traditionally, social pressure provided a strong measure of transaction security, but no longer operates so effectively in a modern context. Gangsters can alternatively be resorted to, but this ultimately becomes dysfunctional to the smooth operations of any business community. We can expect that Taiwanese SMEs will increasingly rely on law courts to adjudicate and to guarantee trust, with less resort to social pressure or the threat of violence.

⁴¹⁷ *Ibid*: p.10.

Chapter 5: Human Resources Management

In a pure capitalist labour market, the relations between capitalists and labourers are theoretically similar to two commodities exchanged in the market. Taiwan's economists mainly adopt this viewpoint to interpret Taiwan's labour market.

At the same time, Chinese enterprises are usually described as 'family enterprises', for they are usually controlled and managed by a family. This is often praised by scholars who see Chinese culture as one of the secrets of Taiwan's economic success. Pure market forces do not function in such a 'traditional values-laden labour market'. This approach does not, however, tell us why there are a lot of failing family enterprises, and why the turnover rate of the labour force is so high.

In this chapter I will discuss labour-capital relations, and, contrary to economists, will observe how the traditional cultural values, set in specific political and economic structures, affect organisational behaviour, which might not follow market principles, i.e., other considerations might be placed prior to profit calculations. I will explore the social norms, which influence the ways to find a job, and the industrial relations in an enterprise. I will also discuss the reasons why Taiwan's family firms want to employ family members as their inner circle.

However, the cultural factors are not left intact, and we will see how market forces condition the working of traditional values and, moreover, when these factors do not fit into a capitalist society, how the enterprise will be changed. I will discuss the consequences of hiring an inefficient family member in an enterprise, and the family division caused by family discord. I will compare the new types of family division in industrial Taiwanese society, which are different from Wong's model based on agricultural Chinese society. In the last part of the chapter I will explore the new labour market situation after the mid-1980s, and try to identify the new ways that the family enterprises adapt to cope with the new circumstances.

5.1 The Economic Structure and Family Firms

According to the definition set by the Ministry of Economic Affairs, about 98% of

Taiwan's firms in 1995 were SMEs.⁴¹⁸ They absorbed about 80% of the total labour force.⁴¹⁹ However, the data does not show the role of the family firm in the economy. In Chapter Three, I mentioned that most of my informants' companies are wholly-owned (獨資). The government data confirm that 60% of the SMEs in 1995 were wholly-owned, and only 1.3% of the SMEs adopted any form of partnership (合夥). 28% were limited companies (有限公司), and 10% were stock-holding companies (股份有限公司).⁴²⁰

From the viewpoint of ownership, we can safely say that at least 60% of the SMEs were not so much individually owned but rather were family firms, and that these SMEs employed more than 50% of the total labour force. Too, many of the stock-holding companies are also family firms. In their research of Taiwan's business groups, Hamilton and Kao found that sixty-three (66%) out of the ninety-six groups are family firms, and thirty-one (32%) also counted as 'quasi-family firms', though in a Western legal sense these would be considered partnerships.⁴²¹

This kind of organisational form has an influence on Taiwan's economic activities. We need to know why Taiwan's businesses adopt this sort of organisational form. Is it a product of Chinese culture? Or a kind of organisational form adapted to a specific political economy? Let me start with the cultural factors, and then observe how they fit into the capitalist economy.

5.2 Working for the Patriarchal Family

In Chapter Two we have shown that running a successful business is an upwardly mobile path for those not successful in climbing the educational ladder. Another important inspiration derives from family values. Many interviewees said that they had to work day and night when they started their business. They felt it their duty to do so, as they had taken money belonging to the family, which reduced the security of the whole family. If they failed, all of the family would be seriously affected. Martin King Whyte also found that 'the

⁴¹⁸ The definition has been changed seven times. See Jingjibu (經濟部, Ministry of Economic Affairs), *Zhonghua minguo Bashisi nian Zhongxiao Qiye Baipishu* (中華民國八十四年中小企業白皮書, White Paper on Small and Medium-sized Enterprises in the Republic of China, 1996) (Taipei: Ministry of Economic Affairs, 1996), pp.351-354, appendix 1.

⁴¹⁹ *Ibid.*: pp. 56-57.

⁴²⁰ *Ibid.*: p. 71.

⁴²¹ See Gary G. Hamilton and Kao Cheng-shu, 'The Institutional Foundation of Chinese Business: the family firm in Taiwan', *Comparative Social Research*, vol. 12 (1990), p. 143.

continuing strong family obligations make it possible to mobilise individuals very successfully for family-based entrepreneurial activities'.⁴²²

The data that I computed from 'A General Survey of Social Change in Taiwan, 1992', running all of the data through my computer, shows that 21.5% of the interviewees were self-employed, and 6.7% worked for their families (see Table 5.1). If we exclude retired people, housewives, and unknown cases, more than one out of three worked for their family. Even when we exclude farmers (one hundred and eighty-three cases), about 27% of the informants worked for their family.

Table 5.1 Working Place Distribution, 1992

unit: %

Category	Self-employed	Work in Company	Work in Family	Un-employed	Retired	House-wife	Unknown	TOTAL
Frequencies	512	1075	160	79	63	471	17	2377
Percent (1)	21.5	45.2	6.7	3.3	2.7	19.8	0.7	100.0
Percent (2)	28.0	58.9	8.7	4.3	--	--	--	100.0

Source: Calculated from "A General Survey of Social Change in Taiwan, 1992". The research was conducted by the Institute of Ethnology, Academia Sinica under the directorship of Professor Kuo-shu Yang and Hei-yuan Chiu.

Notes: Percent (1) includes those people not counted in the labour force statistics, and percent (2) excludes these people.

Who works for the family? I have computed from the 'General Survey' that sixty-seven percent of them were females and thirty-three percent were males. Among the females, 76% of them did not receive any wage, while the figure for males is only 50%. In other words, far more females worked as unpaid family workers. The official data shows that the percentage of unpaid family workers in the total labour force is declining, down from 12.4% in 1978 to 8.4% in 1996, and that the share of unpaid female family workers increased from 62.6% to 74.6% within this group.⁴²³

Another statistic computed from the same database is that among the one hundred and forty-five self-employed who hired more than one worker in their business, excluding

⁴²² See Martin K. Whyte, 'The Chinese Family and Economic Development: Obstacle or Engine?', *Economic Development and Cultural Change*, vol 45, no. 1, (Jan 1996), p. 17.

⁴²³ See Directorate-General of Budget, Accounting and Statistics, Executive Yuan (行政院主計處), *Zhonghua Minguo Bashiwu nian Taiwan Diqu Renli Ziyuan Diaocha Tongji Nianbao* (中華民國八十五年台灣地區人力資源調查統計年報, *Yearbook of Manpower Survey Statistics, Taiwan Area, ROC, 1996*) (Taipei: Directorate-General of Budget, Accounting and Statistics, 1997), pp.52-53, Table 14.

farmers, 72% of the employers were males. Adding together the owners and those who work for their family, those who answered 'I take part in important decision making', 69% are males. According to the government's survey in 1996, 87% of all employers are males.⁴²⁴ This confirms the patriarchal image of Taiwan's family firms, which usually use unpaid family females, while the owners and decision makers are mostly males.

Not only are the decision-making posts in the family firms largely occupied by males, but capital flows from females to males, and from parents to sons. The wife's dowry and 'private savings' (私房錢) are used to help the husband's business, and the wife's separate occupation serves as the family's safety net when the husband fails in business. One of my respondents had a wood-processing firm. After a default on a cheque, he was arrested and put in jail. His wife had to sell dumplings in the local market in Gaoxiong, and all her income was used to pay the debt, the three children's education and the rent. Another informant said that his wife encouraged him to set up a company, and if he had failed, she still had a stable teaching job at a school, which would have enabled her to support the family with three children. Her support made him decide to open a factory of his own.

Though female family workers contribute to the family firm, and they are legally entitled to inherit the family property, they are not entitled to inherit according to Taiwanese custom. In her research of gender differences in household resource allocation strategies, Holin Lin finds that Taiwanese and Mainlanders' sons 'actually got much more in the division of parental property' other than cash (see Table 5.2).⁴²⁵

Cash is normally given to the daughter as her dowry. A daughter working in the company might get a dowry as her reward, but the dowry would soon be channeled into her husband's initial capital if her husband wants to open a business. A company is usually taken over by a son, though daughter(s) also work in the family firm. Many male informants told me that it is important to have a son. One informant has three daughters, one of whom works in a big company, and the other two work in his own company. He said that he did not have any incentive to expand the firm, even though there is an expanding market, for he does not have a son to inherit the business he has established. Another

⁴²⁴ *Ibid.*: pp. 52-53, Table 14.

⁴²⁵ See Holin Lin (林鶴玲, Lin Heling), 'Gender Culture as Economic Determinant: Household Resource Allocation Strategies Among Ethnic Groups in Taiwan', paper presented at *Conference on Social Stratification and Mobility: Newly Industrializing Economies Compared* (Taipei: International Sociological Association Research Committee 28, Institute of Sociology, Academia Sinica, 1998), p. 103.

respondent placed his two sons into the company, and even though they are not competent, according to the respondent's brother, he still wants to leave the factory to the two sons after he retires. At the moment, most of the managerial work is done by the two daughters-in-law.

Table 5.2 Who Actually Got What in the Division of Parental Property

Column pct (Count)	(percentage in its ethnic group population)			
	Taiwanese		Mainlander	
	<u>Daughter(s)</u>	<u>Son(s)</u>	<u>Daughter(s)</u>	<u>Son(s)</u>
Land	4.6 (43)	62.9 (582)	6.0 (5)	41.0 (34)
House	2.6 (24)	12.6 (117)	6.0 (5)	16.9 (14)
Cash	6.2 (57)	2.2 (20)	9.6 (8)	3.6 (3)
Others	1.5 (14)	0.3 (3)	6.0 (5)	0 (0)

Source: See Holin Lin (林鹤玲, Lin Heling), 'Gender Culture as Economic Determinant: Household Resource Allocation Strategies Among Ethnic Groups in Taiwan', paper presented at *Conference on Social Stratification and Mobility: Newly Industrializing Economies Compared* (Taipei: International Sociological Association Research Committee 28, Institute of Sociology, Academia Sinica, 1998), p. 103, Table 3B.

But working hard for a patriarchal family does not mean that one needs to work for one's own family enterprise. One can also work in a big company and remit money back to the family. The question is why a lot of family members do work in a family enterprise. I would argue that there are two main reasons: to keep non-family workers from sharing in the profits; and to evade tax. To use family members to work in one's company is like killing two birds with one stone, i.e., reducing any labour-capital conflict and engaging in Taiwan's most common form of corruption.

5.3 Labour-Capital Relationship in SMEs

On the one hand, an owner of an enterprise prefers to hire more family members or relatives, for it is easy to use social relations to de-mobilise the other labourers, as we have seen in Chapter Two. But on the other hand, the owner has to run the risk of hiring an inefficient relative. It is almost impossible to fire a relative, for one has to follow the

traditional norm and be kind to all one's friends and relatives.⁴²⁶ A family firm has to balance the cost and benefit of employing family members and relatives. In this section, I will discuss how the SMEs recruit labourers, how they manage them, and what the possible outcomes are when conflicts arise.

5.3.1 The Role of Social Relations in Job-Searching

In the 1960s, a lot of the workers were from rural areas, and they had to find their first job through personal connections in the urban areas. An informant told me that in the 1950s, labourers from Beimen mainly went to Gaoxiong and Tainan. He emigrated to Gaoxiong, not because there was a job for him, but because he believed that there might be a job, and more important, because he had a classmate whom he could rely on to provide a free sleeping space. If there were no such social contact in Gaoxiong, he would have gone to Tainan, because Tainan is much nearer to Beimen. A personal network based on a common hometown provided the most important social network on which migration was premised. Migrants tended to select their residences or occupations on the basis of relatives and friends from the same community, as Alexander Chien-chung Yin observed of Penghu immigrants in Gaoxiong,⁴²⁷ Ke Zhimin (Ka Chi-ming, 柯志明) of Wufenpu (五分埔) emigrants in Taipei,⁴²⁸ and Michael Backman of overseas Chinese in Southeast Asia.⁴²⁹ The formation of the immigrant community was based on an 'immigration net', which means one person 'pulls' another into the newly established community and forms a distinct social network. It serves two economic functions: one is to supply a labour force for owners who are from the same community; the other is to provide basic social help for newly arrived sojourners.⁴³⁰ For workers and bosses, it

⁴²⁶ It is hard to define what is close relatives. Those workers introduced by relatives or friends are not close relatives, for they do not belong to the first circle of the boss. Close relatives could be those relatives who have direct contact with the boss, and interact more frequently than others.

⁴²⁷ See Alexander Chien-chung Yin, 'Voluntary Associations and Rural-Urban Migration', in Emily Martin Ahern and Hill Gates (eds.), *The Anthropology of Taiwanese Society* (Stanford: Stanford University Press, 1981), p. 327.

⁴²⁸ See Ke Zhimin, *Xiaoxing Qiye de Chuangye, Jingying yu Shengchan Zuzhi—yi Wufenpu Chengyi Zhizaoye wei Anli de Fenxi* (*The Establishments, Managements and Production Organisation of Small Enterprises—Cases Study of Ready-made Clothes Industry in Wufenpu*) (Taipei: Sinica Academia, 1993).

⁴²⁹ See Department of Foreign Affairs and Trade, *Overseas Chinese Business Networks in Asia*, (Canberra: Department of Foreign Affairs, Commonwealth of Australia, 1995), pp.13-18.

⁴³⁰ It also serves political function. In Gaoxiong, a newly planned industrial city in the 1920s, there are three factions which were based on immigration background. One is called 'Zaidi' faction (在地), another

became an indispensable ‘instrument’ in finding a job or in doing business.

This situation has not changed a lot after 30 years. This can be observed in the survey data that I computed on the ways in which people obtained their jobs. Fei Xiaotong’s classification of Chinese *guanxi* is adopted here to distinguish the closeness of the relationship with the interviewee, i.e., with the ego (自我) in Fei’s term.⁴³¹ Excluding those working in primary industry, and according to closeness, I find that only one-third of the people obtained their job through an impersonal channel, e.g., the state exam, an employment bureau, a public advertisement, or a company’s formal recruitment. One-fourth of the sample were introduced by non-relatives, e.g., friends, teachers, classmates or colleagues, 12% were introduced by family members or relatives to work in a non-relative’s company, while 30% worked for their family, a relative’s business or were self-employed.⁴³² A survey done by the government similarly shows that 41% of the SMEs’ employees were introduced to work in a company via personal contacts, and 52% were recruited by impersonal methods.⁴³³ The statistics imply that social networks in searching for a job are important.

According to the yearly survey done by the Directorate-General of the Budget, Accounting and Statistics, 40% of the employed in 1979 obtained their jobs through the introduction of relatives/ friends or teachers. The percentage declined to 34.5% in 1996. The way of finding a job by referring to ads or posters doubled from 11% to 22% in the same period.⁴³⁴ This long-term data reveals that, even though social networks are important in searching for a job, their relative importance is declining, accompanying the capitalist development of Taiwan’s economy.

Cross-tabulating how people find jobs with company size in terms of workers, we find that the smaller the business size, the more likely that it hires people introduced by family members and relatives. According to my own computations of the 1992 survey,

is ‘Penghu’ (澎湖) and the other one is ‘Tainan’ (台南) faction, whose members are mainly from Beimen area. Both Penghu and Tainan factions are organised by those immigrants from these two counties.

⁴³¹ See Fei Xiaotong (費孝通), *Xiangtu Zhongguo Xiangtu Chongjian* (鄉土中國，鄉土重建) (Taipei: unknown publisher), p. 27.

⁴³² Calculated from “*A General Survey of Social Change in Taiwan, 1992*”, question 56: How do you find your present job and your first job? Valid cases are 1,513.

⁴³³ See Small and Medium Enterprise Agency, the Ministry of Economic Affairs, *Zhonghuaminguo 84 Nian Zhongxiao Qiye Baipishu* (中小企業白皮書, *White Paper on Small and Medium Enterprises*) (Taipei: MOEA, 1996), p. 97, Table 3-2-8.

those firms employing less than twenty persons recruited 49% of their labour force from among family members or relatives, 28% were introduced by friends or colleagues, and 23% through impersonal recruitment. The figures for companies employing fewer than one hundred workers were 22%, 36% and 42% respectively; while for those employing more than five hundred workers, they were 12%, 37% and 51% respectively. The survey done by the government in 1997 showed that among firms employing more than three hundred workers, 81% of the labourers are recruited by public selection, and only 10% are introduced by the workers in the firm. The figures for those firms hiring less than thirty workers are 63% and 27% respectively.⁴³⁵

In short, social networks play an important role in recruiting the labour force, but their importance is declining gradually. The role of social networks is also different between SMEs and big firms. The bigger the firm, the less important the social network in helping to find a job.⁴³⁶ When a company grows to a certain size, its social network reaches a limit, and it has to resort to less personal ways to recruit its labour force.

5.3.2 Social Roles and Self-Interests in Working Place

Different ways of recruiting manpower will influence the capital-labour relationships in the company. We have discussed the labour-capital relationships in Chapter Two. For SMEs, it is easy to use small group pressures to control labour. In this kind of organisation, traditional social relations play a key role to harmonise labour-capital relationships.

To cite an example, three brothers jointly ran an electronic components company, and they hired a niece to work as personnel manager. She continuously emphasised the importance of 'keeping good relationships within a family' (家內要和) when I asked her the key to the success of the company. Regarding the turnover rate of the labour force, she said that she was exceptional, for she had worked there over ten years, and 'eight out of ten technicians will leave', she said with contempt. Her words show that she does not identify

⁴³⁴ See Directorate-General of Budget, Accounting and Statistics, Executive Yuan, *op. cit.*, pp. 264-265, Table 99.

⁴³⁵ See Directorate-General of Budget, Accounting and Statistics, Executive Yuan (行政院主計處), *Zhonghua Minguo Taiwan Diqu Shiye Renli Guyong Zhuangkuang Diaocha Baogao* (中華民國台灣地區事業人力雇用狀況調查報告, *Report on the Employment of Manpower, Taiwan Area, ROC, 1997*) (Taipei: Directorate-General of Budget, Accounting and Statistics, 1997), p.66, Table 17.

⁴³⁶ Calculated from "A General Survey of Social Change in Taiwan, 1992", question 56: How did you find your present job and your first job? And question 21: how many workers are there in your company? Valid cases are 1026.

herself as an 'employee' at all. She has tried her best to fulfil the 'family member's role' in the company. That is why she disliked the high turnover rate of the labour force, which reduced the possibility of accumulating the skills to operate the company.

The rules set within the organisation might be grounded in pre-existing social norms, not rules set by either capitalists or the legal system. One's identity is multifaceted, and one's identity as an employee is not necessarily dominant. If the labour-capital relationship does not dominate the work place and instead other social relationships prevail, the rules within the organisation might not follow the capitalist logic. Under this circumstance, labourers have to try to maximise their income under the constraint of their social roles.⁴³⁷ At another company, the labourers were mostly introduced by friends in the neighborhood of the factory, and my informant said that 'the production efficiency of these old female workers is as good as that of young female workers, for they're more willing to adjust their time to comply with the company's production schedule, and they are also willing to work overtime.' These old female workers were willing to do so because they were poor and needed more money, and they had to keep good *ganqing* with the boss.

Not everyone follows the social norms set for them, however. Most labourers assume the social role of a worker for the short term, but then leave after s/he has learned the necessary skill to open his/her own shop. Another interviewee said that 50% of the newly recruited workers will leave in the first year, and another 20% in the coming year. As seen in Chapter Two, the less educated try to get a job in the labour market, but seek the opportunity to become self-employed. Yet this kind of short-term proletarianism makes it possible to endure unreasonable pressure from the work place. The research in Wufenpu done by Ke Zhiming shows that relatives are more willing to do overtime work, and are more flexible in meeting the boss's requirements, though they also complained about it and felt exploited. Richard W. Stites found that 'workers are aware that surface friendliness with the owner is just that';⁴³⁸ the deeply rooted labour-capital conflict still exists.

From the boss's perspective, s/he also plays two roles in a profit-seeking organisation, those of the capitalist minded business(wo)man, and the kind philanthropist. She or he can seek to exploit the social relations to enhance his or her dominance over the workers for profit. But the owner does not necessarily behave in a paternalistic way and take care of the

⁴³⁷ This point is consistent with neoclassical economics theory on utility maximisation.

⁴³⁸ See Richard W. Stites, *op. cit.*, 1985, p. 236.

workers as in the relationship between father and sons.⁴³⁹ Gordon Redding has argued that the management pattern is paternal. But my comparison of family and non-family enterprises showed that this paternalistic management only exists in the family firm, and even there the management pattern is not always paternal. Ambrose Yeo-chi King found that Chinese like to hire kinsmen on the grounds that they are reliable, competent and responsible.⁴⁴⁰ But when self-interests conflict, the 'generous' side of patriarchy gives way to self-interest.

I asked owners their opinion of the Basic Labour Rights Law. They all complained about its 'bias towards the workers'. One extreme case is an interviewee who spent most of the time talking about his experience in joining the Ciji (慈濟) Buddhist sect when I interviewed him. He said he used to be an alcoholic, but after conversion to the Ciji Buddhist sect, he changed his personality totally and his family life became 'warm and happy'. "Religion also changed my attitudes toward workers. I used to think that I spent money to hire them, but now I think that they spend their time to work only for a low remuneration. Now I treat them as if they are my family members". But when I asked him about the Basic Labour Rights Law, he said that 'this law is copied from Japan. But the government did not consider that the Japanese and Chinese national characters are different. Japanese will work hard seven days to get seven days' reward, but Taiwanese would 'steal time' (be lazy) as much as possible, even if they are paid for seven days.... This law is like "raising rats to bite rice bags" (養老鼠咬布袋), encouraging labourers to fight against their boss.' Self-interest almost always plays a key role in the owner's decision-making, and religious belief or ethics has little role to play in this domain.

This finding is consistent with Donald DeGlopper's observation that the employers are not paternalistic, nor are the employees dependent, and that both sides like this kind of relationship.⁴⁴¹ Though the boss and workers are linked through social relations in the beginning, their later interactions follow the logic of capitalism, i.e., an impersonal way of interactions would be more effective in realising profits.

⁴³⁹ See Gary Hamilton, and Nicole Woolsey Biggart, 'Market, Culture, and Authority: A Comparative Analysis of Management and Organisation in the Far East', *American Journal of Sociology*, vol. 94 (1988) (Supplement), pp. 52-94.

⁴⁴⁰ See Ambrose Y. C. King and Rance P. L. Lee (eds.), *Social Life and Development in Hong Kong* (Hong Kong: The Chinese University Press, 1981).

⁴⁴¹ See Donald DeGlopper, 'Artisan Work and Life in Taiwan', *Modern China*, vol. 5, no. 3 (July 1979), p. 299

Family firms which hire family members and relatives or friends also have labour-capital conflicts. The most common contradiction involves the promotion of workers. Important positions are reserved for family members, and not so close relatives find it difficult to get promoted. As in the family firm mentioned above that is controlled by three brothers and their relatives, non-family members do not have much opportunity to be promoted in the firm, so these workers leave to find their own way.⁴⁴² When I computed the survey data of ‘*A General Survey of Social Change in Taiwan, 1992*’ for the question ‘What is the outlook for your career?’, the mean score--that is, the optimism regarding promotion--of those finding a job by impersonal means is statistically significantly higher than those who had used a personal way (excluding the self-employed in the sample).⁴⁴³ We have found that the bigger the firm, the more likely it is to recruit labourers in an impersonal way, so we can say that the career outlook in the big firms is better than for those working in relatives’ firms.

Income distribution shows the same pattern. For males, those working for one’s family or co-investing with relatives, or self-employed, have higher incomes than those whose jobs were introduced by relatives or friends, and the average incomes of those finding their jobs through an impersonal way lay between the above two groups.⁴⁴⁴ This indicates that in family firms, family members are paid better than non-family members.

If the career outlook in a small family firm is not good, and if the pay is not as good as expected, workers leave and look for another job or they set up their own company. This reaction can resolve the contradiction between social relations and market relations: on the one hand, both boss and workers can keep the social relations harmonious on the surface; on the other hand, labour can shift to keep the market efficient.

5.4 Family Enterprises and Tax Evasion

As noted earlier, one reason to use family members to be managers is to evade tax. Almost everyone complains about the government’s inefficiency and corruption. Most of

⁴⁴² Xie Guoxiong also found the same result in his fieldwork. See Xie Guoxiong, *op. cit.*, p. 34.

⁴⁴³ It is a seven scale question from -3 to 3. The higher the score, the better the outlook for one’s career, and the expected mean score is zero after recoding. The mean score of those finding their job in an impersonal way is 0.72, while those introduced by family members to work in a non-relative company report an average outlook of 0.65, and those introduced by friends score 0.56. $p < 0.00$.

⁴⁴⁴ Male’s average monthly income of those finding their job in impersonal way is NT\$34,567, while those introduced by family members to work in non-relative company report NT\$30,244, and that by friends is NT\$29,973. Self-employed reported NT\$41,406, and working for one’s family was NT\$31,548.

my informants said that they would pay more tax if the taxes were really used for social welfare or public works. But they claim that too much of the taxes go into bureaucrats' pockets: 'the more we pay, the more they get'. Tax evasion has become epidemic. In Chapter Three we have discussed how taxes are evaded in practice. Here we will discuss corruption, and the utility of hiring family members to cope with corruption.

5.4.1 Government Regulations and Bribery Practices

The Chinese saying '*Yamen bazi kai, meiqian bie jinlai*' (衙門八字開，沒錢別進來)⁴⁴⁵ expresses the phenomenon of pervasive corruption. The situation has changed slightly since Taiwan's democratisation, but according to a *Far Eastern Economic Review* survey in May 1995, Taiwan is still ranked as the most corrupt country among the four little tigers.⁴⁴⁶ In 1993, 45.7% of interviewees agreed that without bribery it is difficult to deal with civil servants, while only 26.4% disagreed. When asked about local government bureaucrats, 55.5% felt their integrity was suspect, while only 12.9% believed there was no problem.⁴⁴⁷ Unpublished research by the Ministry of Justice in 1997 shows a low degree of popular faith in officials in various government departments. Table 5.3 shows the results of the survey. As it demonstrates, in only one department did most public servants gain even the 'passing' score of six.

An interviewee, M, said that he was required to reduce the amount of ash his factory produced according to a new environmental law. Bureaucrat A 'recommended' to him some 'highly rated' companies to do the work. He quoted X company, one of the good rated company, which asked for US\$32,000, while another 'non-rated' Y company charged only US\$20,000. Naturally, he gave the work to company Y. After construction, the new equipment failed to pass inspection. M asked Y why he failed to pass the subsequent inspection, and Y in turn rang A to know what the problems were. It turned out that A wanted a 'commission' of US\$6,000 for this work. M was very angry, and asked A to come to his factory to take the 'commission'. Though M recorded what they talked about when A came to take the money, he did not go to court because he 'did not have time to deal with these things'. He said that he later listed this expenditure as a 'cost in socialising'. Afterwards he found that X company was run by a local politician's relative,

⁴⁴⁵ It means that a government office welcomes everyone, but don't come here without bringing any money.

⁴⁴⁶ See *Far Eastern Economic Review*, 27 May 1995.

and many factories asked these 'good-rated' companies to do the environmental protection work to prevent harassment from the bureaucracy. If the people in charge of the environmental protection inspection are thus corrupt, given that they were the only ones to get a passing score of 6 (Table 5.3), we can imagine the corruption of the public servants in other departments.

Table 5.3 Subjective Impression of the Integrity of Public Servants

	Mean Score
Local Representative (地方民代)	4.1
Representatives at Central Government Level(中央民代)	4.3
Civil Servants in Charge of Urban Planning (建管人員)	4.7
Civil Servants in Charge of Customs Inspection (海關人員)	4.8
Minister (首長級官員)	5.1
Police (警察)	5.1
Judge, Prosecutor (法官、檢察官)	5.4
Civil Servants (一般公務人員)	5.5
Civil Servants in Charge of Taxation (稅務人員)	5.5
Civil Servants in Charge of Environmental Inspection (環保人員)	6.0

Source: Ministry of Justice, *Taiwan Diqu Minzhong dui Zhengfu Lianzheng Zhuguan Zhibiao—Minyi Diaocha Baogaoshu* (「台灣地區民眾對政府清廉政治主觀指標」民意調查報告書, *Report of the Subjective Index on Government's Integrity in Taiwan*) (Taipei: the Ministry of Justice, 1997), pp.63-69.

Note: Interviewee was asked to mark a score ranging from 0 to 10 to evaluate the officials' integrity. 0 means not upright at all, and 10 means 100% upright. In Taiwan, 6 is the passing score, a score of less than six indicates failure.

Even where bureaucrats are not corrupt, it still takes a long time to process an application. For most industries, especially the construction industry, time is money, and approval of an application one day earlier means saving one day's interest on invested capital. For example, because land is extremely expensive in Taiwan, after purchasing a site a construction company will want to start as soon as possible. But the application procedure may vary from one month to three months, depending on bureaucrats' 'free-will'⁴⁴⁷. If the construction licence is approved one month earlier than normal, the company can save a huge amount, enough to pay the 'socialising cost' incurred from dealing with bureaucrats. The head of one very big construction company in Taiwan complained at a conference that because of bureaucratic harassment '*min bu liao sheng*'

⁴⁴⁷ See Qu Haiyuan (瞿海源), *op. cit.*, pp. 232-233.

⁴⁴⁸ In Chinese, this term also connotes the meaning of 'arbitrary'.

(民不聊生，people cannot survive any more). To deal with 'bureaucratic work', her company organised a team and spent a lot of time in establishing connections with bureaucrats. What the company wants is to speed up the bureaucratic approval process. When 'a case' is processed the head of the company would arrange to meet bureaucrats to express his gratitude for the help. Big companies can organise a work-team to specialise in this work, but small and medium-sized enterprises have to resort to their *guanxi* with a local faction.

The two cases mentioned above lie within the legal framework, and bureaucrats cannot be charged as corrupt if they simply 'recommend' that businesspeople do something, or give a hand to companies to speed up applications. Yet every sphere that involves government intervention gives bureaucrats a chance for corruption. When one starts a business, one has to face different regulations for environmental pollution prevention, labour health and safety protection etc. To run a profitable business in Taiwan, one has to run the risk of corruption, as most informants who are businesspeople told me. The following cases are all illegal ways in which businesspeople deal with bureaucrats.

To set up a company one has to comply with a lot of government regulations. Generally speaking, it is difficult for small enterprises to meet these regulations, so these businesspeople have to take 'detours' to get the required licences. To send a 'red envelope' (bribe) is the easiest way. The above mentioned Ministry of Justice survey shows that 22% of the interviewees or their relatives had given a red envelope to civil servants with power to decide on a matter of importance to them.⁴⁴⁹ One of my informants had planned to operate a factory in the 1960s to produce motorcycle components, but he did not have enough capital to buy land to construct the factory, so he set it up in his own house. But according to the law, one cannot set up a factory in a residential area, so he could not get the licence. Through the help of a Gaoxiong City Councilor, he bribed a bureaucrat 'several tens of thousands' of Taiwan dollars to get the licence, by signing a debt-credit contract to pretend that he owed the bureaucrat money. Several months after he had bribed the bureaucrat, the bureaucrat was reported for bribery, but 'luckily' the investigation skipped his own bribery.

⁴⁴⁹ See Ministry of Justice, *Taiwan Diqu Minzhong dui Zhengfu Lianzheng Zhuguan Zhibiao--Minyi Diaocha Baogaoshu* (「台灣地區民眾對政府清廉政治主觀指標」民意調查報告書, *Report of the Subjective Index on Government's Integrity in Taiwan*) (Taipei: the Ministry of Justice, 1997), p.37.

The police are responsible for household registration, so they are aware of every household's situation. If one uses one's house as a factory, s/he is supposed to 'express her/his gratitude' for the 'hard-working' policemen three times a year, at Chinese New Year, Dragon Boat Festival and Mid Autumn Festival (September). When these festivals approach, police will patrol their area to remind small shop-owners or street vendors that it is time to express their gratitude. There is a market price for this expression of gratitude, depending on the area and businesses. For example, the Zhongshan District (中山區) of Taipei charges more than the Muzha District (木柵區). And if a policeman is assigned to Taoyuan county, which is famous for its illegal sex industry, this assignment could be regarded as a kind of promotion, though s/he is at the same rank and gets the same wage. If a businessman dares forget to express his gratitude, police will visit his shop or company daily to check whether the standard of equipment is in accord with the regulations. Street vendors are illegal, as are shops which occupy sidewalk space. It is also illegal to put an appended attic on one's roof without permission from the City or County Construction Department. If a policeman wants to harass a company, it is very easy to find an irregularity. This also applies to taxation officers. One informant complained that 'the taxation officers came to check our accounting in February, and after three months, they came again. I can't stand it any more. Whenever a head of the taxation office is changed, they come to check the accounting. Their intention is obvious, they just want a red envelope'.

Most businesspeople dare not offend the police or stir up trouble for them. The most common means for small shop-keepers and street vendors to protect their interests is to ask a city or county councillor or a provincial representative to support them to maintain their business without crack-downs, as well as to pay money to the police to be rid of their daily harassment.⁴⁵⁰

Factories have to satisfy even more government regulations, especially regarding industrial safety and environmental protection. However, there are only a few inspectors to check the thousands of factories every year. Such an inspection easily becomes a formality. The normal procedure is: inspectors inform the factory what day they will come,

⁴⁵⁰ The famous Zhou Rensen (周人蔘) case shows the widespread corruption of Taiwan's police. The Bureau of Investigation found several accounting books listing many famous political figures, including

so that the company can better 'prepare' for the inspection. To do so, the company is cleaned up, raw materials or finished products are removed from the fire exits, and illegal foreign guest workers are hidden away. When the inspectors come, usually they just chat with the boss. After one or two hours, they go out to have a sumptuous meal, and the boss gives each 'small gifts' to express his gratitude for their hard work.

Businesspeople also have to deal with taxation. One expressed to me the opinion that if you want to know the Taiwan economic miracle, go to study taxation law. Another claimed to me that Taiwan's GNP is two thirds under-estimated because Taiwanese report only one third of their income. From their statements, it is not hard to imagine how widespread tax evasion is in Taiwan.

The two main ways to avoid being audited are to give the taxation officers red envelopes or to allow them to hold a share of equity in one's company. To give a red envelope is usually mediated by accountants, whose main task is to save money for the business. To allow officers to 'join one's investment' depends on how much profits a company can make and how strong-willed the officers are who want to put money in the company.

5.4.2 The Inner Circle and Tax Evasion

In Chapter Three I discussed how taxes are evaded. It is an open secret that companies keep three sets of account books. One set, recording the 'real' business operations and revenues, is for internal use. Only top managers of the inner circle are allowed access to this set. Another set is to show to the taxation officials, and it usually shows a deficit or little profits. The third is used to secure loans from banks, and it shows high profits. One informant noted that 'Taiwanese have a talent for tax evasion'. If the cost of bribery is lower than the gains from tax evasion, why not bribe. However, since tax evasion is not legal, it is always confidential, and only certain people can gain access to the real accounting book. To use family members can prevent the exposure of illegal matters.

If a family enterprise is small and labour-intensive, e.g., a subcontracting firm or one of the tiny clothing manufacturing firms in Wufenpu, the profits are mainly from the family members' own labour, and what they get is a 'normal profit in the competitive market'. The

policemen. See Bi Diaoyu (畢刁瑜), 'Zhou Rensen Renmai Dapuguang' (周人蔘人脈大曝光, Exposure of Zhou Rensen's Social Relations), *Caixun* (財訊), no.171 (1996), pp.212-220.

Taxation Office usually does not pay much attention to this kind of business, though it might have a higher income than that of wage labourers. For example, an informant opened a Chinese medicine shop, and on average his family can earn A\$10,000 a month. But two persons have to work from 5:00 a.m. till 12:00 p.m., which means their hourly wage is 25% higher than a wage worker.⁴⁵¹ Every year they are taxed only a few thousand Taiwan dollars.⁴⁵²

But companies bigger than micro-enterprises have to be careful, for the Taxation Office often keeps an eye on them, and usually it is easier to check their capital flow. They hire more workers, and usually the work place is separated from their home, unlike micro-enterprises. However, one informant said that if one pays tax as the laws regulate, no company in Taiwan will be profitable.

Civil servants in the Taxation Office are counted as one of the four evils.⁴⁵³ One of my respondents privately related that the Taxation Office fined him a few million US dollars for tax evasion in January 1995, and up to now the case was not yet been 'solved', for the officials hinted to him that 'everyone more or less evades tax and we know how to deal with it'. He has talked many times with the persons who are in charge of the case, and has asked his provincial representative to help to 'bargain' how much legal and illegal money he should pay. This corrupt situation is well known, and even the head of Formosa Plastic, the largest manufacturing enterprise in Taiwan, criticised that 'if there is one company evading tax, we can say confidently that all companies in the industry evade taxes, for the accounting principles make it impossible for one company to evade tax without the cooperation of upstream or downstream companies.... Everyone knows that tax evasion is pervasive and has lasted for a long time. So obviously many of the staff in the Taxation Office collude with companies to make money'.⁴⁵⁴

In September 1997, the Investigation Bureau prosecuted a group, consisting of civil servants at the Taipei Taxation Office, for cooperating with accountants to help more than

⁴⁵¹ Their hourly wage is $A\$5,000/(17*30)=A\10 , and a wage worker's is $A\$1,500/(8*25)=A\7.5 . The average wage in manufacturing industry is NT\$30,720 in 1994, and NT\$33,765 in 1996.

⁴⁵² About a few hundred Australian dollars. Exchange rate of one Australian dollar is about twenty Taiwan dollar. The average wage in manufacturing industry is NT\$30,720 in 1994, and NT\$33,765 in 1996.

⁴⁵³ The four evils are judges, police, secret agents and Taxation Office servants. See Twu Jaw-yann (涂照彦), *NICS--Kougyouka Ajia wo Yomu (NICS--Reading Industrialised Asia)* (Tokyo: Kodansha, 1988), p. 127.

⁴⁵⁴ See Wang Yongqing (王永慶), *Wang Yongqing Bamai Taiwan (Wang Yongqing Checks Taiwan's Disease, 王永慶把脈台灣)* (Taipei: Taiwan Daily News, 台灣日報, 1997), p. 75.

1,600 firms to evade tax over the past decade.⁴⁵⁵ The reporter commented that ‘businesspeople might not want to hide their income, but the probability of meeting a clean officer at the Taxation Office is too low, so they have to protect themselves by way of bribery’.⁴⁵⁶

The companies have to keep secret of their tax evasion and bribery, and family members are trusted to keep the secrets. In big firms, there is an inner circle to manage the company’s finance, and to ward off the government’s investigation, and to work closely with the civil servants from the Taxation Office.⁴⁵⁷ In SMEs, the family members comprise the inner circle. I have found that the females, either wife or daughter or aunt or daughter-in-law, usually take care of financial matters in the SMEs. In Taiwan, it is a stereotype that women are more capable in managing money than men, and normally a company’s accounting is controlled by a female. She has to hide income and to collaborate with accountants to fake financial statements.

5.5 Contradictions Between Strong Social Ties and Inefficient Management

As noted, to evade taxes and to keep the profits in the family *vis a vis* employees’ demands for higher wages, companies tend to use family members as managers in an inner circle. Expanding the concept of familial ties, Hamilton and Kao write that the Chinese family enterprise should be understood ‘in terms of trust-bearing personal relationships that can be used to generate economic and control networks within and beyond the group’.⁴⁵⁸ One hypothesis developed by them from their re-definition is that ‘*guanxi* relationships, in turn, constitute one’s personal networks that allow one to mobilize resources and manpower within and among firms. In a general sense, the larger and more cohesive a person’s network, the more powerful that person is considered to be’.⁴⁵⁹ However, this kind of conclusion neglects the basic principle underlying the function of a network, i.e., the reciprocity principle; and secondly, ‘such an embeddedness of economic activity in social relationships should not be seen as capable of producing its own sources

⁴⁵⁵ See China Evening Times, *Liwenxin An Douchu Shuiwuquan Heimu* (李文鑫案抖出稅務圈黑幕, *The Case of Liwenxin Reveals the Black Box of Taxation Office*) (30/09/1997), p. 4.

⁴⁵⁶ *Ibid.*: p.4.

⁴⁵⁷ See Gary G. Hamilton and Kao Cheng-shu (1993), *op. cit.*, p. 146.

⁴⁵⁸ *Ibid.*: p. 148.

⁴⁵⁹ *Ibid.*: p. 146.

of allocative efficiency'.⁴⁶⁰

5.5.1 Reciprocity and Social Networks

Karl Polanyi argues that there are three different principles that organise our economic life, reciprocity, redistribution and householding (*oeconomia*). The Chinese *guanxi* network is based on the principle of reciprocity. The basic tenet is that when one takes, one gives back in return. The Taiwanese saying 'Chiren Yijin, Huanren Baliang' (吃人一斤，還人八兩—eat one *jin*⁴⁶¹ from others, give back eight *liang* in return) shows the burden of receiving favours. In the old days, when it was not easy to find a job in the manufacturing industry, if one was introduced to work in a factory by an acquaintance or relatives, it means that the introduced obtained a favour from the boss, and s/he was supposed to pay back the favour. The best way to pay this back was to perform well in the firm. However, as earlier noted, this sort of 'giving a favour to workers' is declining, with more and more people finding their jobs through impersonal ways. Since the workers may not have any special obligation to the boss, the relationship between them and the boss becomes based more on pure market principles.

If one wants to broaden one's network, one has to spend more, which might be beyond one's means if the network is too large. Even if the network is small, one faces the *renqing* dilemma. In Taiwan, it is popular to ask some powerful persons such as legislators or high ranking government officials to write or speak to the decision-maker in a bureaucracy. The decision-maker has to decide whether s/he should give a hand or not. If the introduced person's qualification is sub-standard, or the *guanxi* between the recommender and the decision-maker is not close, the introduced case will be filed. If the powerful person owns a company, it might be easy to put these people in the company because s/he can decide it. If so, the company has to face the dilemma, i.e., to conform to social ties or to market efficiency. If the powerful person has to ask other people's favour, s/he has to consider how to pay back the *renqing* in future, in other words, s/he will become a *renqing* debtor. So when one has a broad social network, one will have higher *renqing* pressure, which is liability against one's assets. If the cost of *renqing* becomes too high, one will not be able to maintain such a broad network. So a personal network is

⁴⁶⁰ *Ibid.*: p. 148.

⁴⁶¹ *Jin* and *liang* are the weight measurement in Taiwan. One *jin* equals 600grams, or equals 16 *liang*.

basically sustained by one's ability to give.

When one is no longer able to give, e.g., when one leaves the key position which provides one with power, the network will soon shrink. One company owner was a legislator, and was involved in a business with several others. But after he lost office, many of the partners pulled out, and the Taxation Office started to check his accounting. He asked one of his partners, who held a high-ranking government post, to help, but the 'friend' did not respond. The Chinese saying '*renqing* is as thin as a paper' (人情薄如紙, *Renqing bo ru zhi*) describes this experience. One's social network is artificial, and a broad network can be very fragile if the network is built upon the position one occupies.

5.5.2 Familial Ties vs. Company Profits

A second problem with Hamilton and Kao's hypothesis is that a family firm is still an enterprise, which has to conform to market forces to make a profit. If it has an inner circle, these people must be competent to make profits for the firm. Yet employing family members to work at managerial positions might not be based on their competence or productivity but on familial ties. A problem will arise if members of the inner circle are incompetent or are not devoted to the company.

It is quite common, as noted, for the boss's wife or daughter to do the company's accounts even if she knows nothing about keeping books at the beginning. Learning by doing is a common pattern, and she may go to an after-school institute to learn the basic skills. The boss's brothers or sons are in charge of sales or production, and their acquisition of the necessary skills is on-line training -- training through working.

However, not every family member is good at business or willing to look after the family firm. An extreme case of this dilemma is a boss who is the eldest son, and had a strong traditional conviction that he would bear all the family responsibilities. When he was young he sacrificed for his family regardless of the cost and helped all of his brothers to 'stand up in society proudly' (在社會上站得起). He established a firm which, step by step, employed his brothers. In his company, all family members have equal rights but unequal obligations. Before dividing living costs among *fangs* (*Hokkien*, 各房分隨人吃) in 1992 all family members could take as much money as they wanted from the pooled funds earned from the family enterprise, 'like a small communist society', he said. For example, his two children both went to national universities, where the tuition fees are only one-fourth of

those private universities. His brothers have more children and all went to private universities. Though he had to do most of the work, he got much less money from the pool. He has great authority in the family, but it means that his brothers could be lazy and leave the work to him. He complained that they did not even know how to write an invoice after working for twenty years in the company. He had invested in another company and assigned a brother to manage it, but because of the brother's incompetence this investment failed, and his brother returned to his old job. My interviewee concluded that 'the defect of a traditional family enterprise is that everyone is the boss, but no one is the specialist. Everyone has opinions, but no one does their fair share. Our traditional culture emphasises ethics and morality, but if we follow its doctrines, we will not survive'.

This is an extreme case. Family enterprises operating 'like a communist society' are not a common phenomenon in Taiwan, but it shows the dilemma a family enterprise can face, the contradictions between market principles (efficiency) and family values (xiaoti, 孝悌, fraternal solidarity). On one hand, traditional values require a family to take care of all family members, and on the other, the market principles require that an enterprise treats everyone in terms of their competence. If a family enterprise uses family members to evade taxes and to keep outsiders from sharing in the profits, it also runs the risk of family discord and production inefficiency. As the family expands and more family members are incorporated into the family enterprise, it is more and more difficult to handle these problems.

One interviewee's company operated very well in the 1970s and at the beginning of the 1980s; however, the marketing channel was controlled by a wholesaler in Taipei, so the owner had thought to set up a distribution company with his brother, who taught at a teachers' college. His brother took NT\$3 million from him in the early 1980s, but used it for other purposes. The news spread quickly in the business community, and produced a domino effect. The NT\$40 million he had borrowed in the private financial market was withdrawn by creditors, and 'the company almost collapsed'.

5.5.3 *Fen-jia* as a Mechanism to Resolve Contradictions

If a firm is run by the family, it will eventually experience the family cycle, and a decision to split the family. There are two different views on the causes of family division. In his research on agrarian Chinese society, Maurice Freedman concluded that the ability of

the father to exercise authority is the key element that ties the whole family together.⁴⁶² However, for Myron Cohen and Arthur Wolf, 'the fate of a family is decided by all of the adult men individually and rationally in search of economic advantage'.⁴⁶³ Margery Wolf uses the concept of 'uterine family' to explain the break of the solidarity expected of brothers in Chinese society due to the different economic calculations in the family composed of different uterine families.⁴⁶⁴ Sung Lung-sheng has argued that the distinction between inherited property and acquired property is relevant to family division, and 'the principle governing the division of acquired property leaves more room for disagreement'.⁴⁶⁵ Chen Xiangshui (陳祥水) also noted that conflicts in the interests of brothers resulted in the family division.⁴⁶⁶ Shunichi Horie (堀江俊一)⁴⁶⁷ and Siu-lun Wong (黃紹倫)⁴⁶⁸ developed models for the Chinese family cycle, and *fen-jia* (splitting family property) happens in the 'extended type I' in Horie's model, or the 'segmented phase' in Wong's model. Both of them agree that differences of interest among *fangs* are the main reason for *fen-jia*.

The contrary findings of Maurice Freedman as against other scholars express the two social forces we use here, i.e., the social and market relations which course through the family unit. On the one hand, filial and solidarity relationships are moral norms for a family. Thus, the hiring of family members to work in the family enterprise is supposed to be the decent and proper thing to do. On the other hand, the pursuit of individual interests can become the seed of family discord. Division in the traditional family is a mechanism to solve the contradictions arising from the family enterprise.

In the studies mentioned above, all but Wong focuses on agricultural society. In

⁴⁶² See Maurice Freedman, *Chinese Lineage and Society* (London: Athlone Press, 1971).

⁴⁶³ Cited from Arthur P. Wolf, 'Domestic Organization', in Emily Martin Ahern and Hill Gates (eds.), *The Anthropology of Taiwanese Society* (Stanford: Stanford University Press, 1981), p.343.

⁴⁶⁴ See Margery Wolf, *Women and the Family in Rural Taiwan* (Stanford: Stanford University Press, 1972).

⁴⁶⁵ See Lung-sheng Sung, 'Property and Family Division', in Emily Martin Ahern and Hill Gates (eds.), *The Anthropology of Taiwanese Society* (Stanford: Stanford University Press, 1981), p.377.

⁴⁶⁶ See Chen Xiangshui (陳祥水), 'Fenji, Jicheng yu Shuangqin de Fengyang: Yige Nantaiwan Nongcun de Gean Yanjiu' (分家, 繼承與雙親的奉養: 一個南台灣農村的個案研究, Family Division, Inheritance and Parents' Supporting System: A Case Study in Southern Taiwan Rural Village), p. 95. *Qinghua Xuebao* (清華學報, *Tsing Hua Journal of Chinese Studies*), new series XXIV(1994), no.1, pp. 85-125.

⁴⁶⁷ See Horie Shunichi (堀江俊一), 'Taiwan Kanzoku no "Kazoku"--jia ideorogi to jia shyutan' (台灣漢族no「家族」-家ideorogi to家集團, Family of Taiwan Chinese: jia-ideology and jia-group), *Minzokugaku Kenkyu* (民族學研究, Research on Ethnology), vol. 46 (1981), no.3, pp.299-314.

⁴⁶⁸ See Wong Siu-lun, 'The Chinese Family Firm: a Model', *British Journal of Sociology*, vol. 36 (1985), no.1, pp. 58-72.

capitalism, land is one of the three major production factors and is a kind of capital, so Wong applied the concept of *fen-jia* to capitalist enterprises, which have capital such as machinery, land and manufacturing equipment. I will extend some of these scholars' arguments to industrialised Taiwan, where the capitalist family enterprise cannot avoid cultural influence. However, some of their arguments are not applicable to *fen-jia* in the 1990s due to the changed social milieu and occupational and structural changes.

If a family firm follows the rules of capitalism, i.e., the goal of maximising profits for the enterprise, it will not face the *renqing* dilemma, and an incompetent family member would be fired. However, the different brothers in the family all are shareholders, and all the shareholders are at the same time the managers. In non-family firms, managers are replaceable if they do not perform well. In the family firm, ownership and management are mixed, and no one can ask the family managers to leave, for they are also shareholders. Unless the family firm is managed by non-family members, the ownership among brothers will need to be divided. The first method makes a company no longer a true family enterprise, and it becomes a profit-oriented company without any family ingredient, even if the family members still own large shares of the firm. The second involves *fen-jia*. As Burton Pasternak noted, the shape of Chinese family patterns is mainly determined by external forces.⁴⁶⁹ The end of a family firm depends on the two forces acting on the family enterprise if there are family disagreements or conflicts.

Many scholars believe that *fen-jia* is the main reason why there are so few big businesses in Chinese society, for any lump-sum wealth will be divided. This ignores the fact that capitalist business enterprises are newly arisen and that most small and medium-sized enterprises started up in business just a few decades ago and have not yet experienced the problem of *fen-jia*. Moreover, this ignores the existence of big business groups in Taiwan. Wong Siu-lun's model suggests that in the end the Chinese family firm will either disintegrate or will revert to the centralised phase in which the family firm is controlled by one family member. It is almost impossible for a big firm to emerge in his model that is run as a family business group.

⁴⁶⁹ See Burton Pasternak, 'Economics and Ecology', in Emily Martin Ahern and Hill Gates (eds.), *The Anthropology of Taiwanese Society* (Stanford: Stanford University Press, 1981), pp.151-183.

5.5.4 Types of *Fen-jia*

We have to distinguish between three types of *fen-jia*: the first is the traditional type, i.e., to divide family property, mainly land, to sons equally, and its equivalent in modern society, to divide a house or a family enterprise. The case of 'the small communist society' discussed above is typical of this type of *fen-jia*. A company was originally set up by an informant and his father, and then gradually his brothers joined the company. Before his father died, the family was organised on the basis of paternal authority, as Freedman portrays. However, after his father's death my informant inherited his father's authority and was able to prevent the family firm from splintering. His authority did not depend on culture but on his devotion to the family. He had finished only junior high school and spent the remainder of his youth working with his father. His brothers were all able to finish senior high school or college thanks to his financial support. However, because the family firm was a sort of 'acquired property', his brothers had the right to ask for family division. If so, the family enterprise would be fragmented; if not, a lot of quarrels could arise if the brothers had different ideas or if there were conflicts over profit-sharing. For my informant, the problem was that the land and the house they occupied were registered in the names of his brothers, so if he decided to *fen-jia* he would be penniless. So he has to delay family division, at least until he could buy a house of his own for his nuclear family. Then, he said, he will divide the property as soon as possible. The Xinguang (新光) and Guoji (國際) business groups are two famous cases in Taiwan. In August 1995, the third son of the Guoji business group sued his brothers for embezzling equity from one of their companies. But the unspoken reason was a quarrel over the distribution of the property left by their father.⁴⁷⁰

Wong claimed that the eldest son normally inherits the position of chief executive position of a family firm, but the other brothers might not acquiesce to his authority, which would cause domestic tensions. The younger brothers could either acquire skills different from the elder brother and occupy different managerial positions, or ask for new ventures that they can run using their individual management.⁴⁷¹ The family firm of this type is more or less like a partnership company. However, it is also possible that a family enterprise is

⁴⁷⁰ See Zhongyang Ribao (Central News Daily, overseas edition), 06, 07, September, 1995, p.3. This kind of family division will result in the division of property, but different brothers use the same 'brand name' like Xinguang. It resembles Japanese Keiretsu after the World War II.

inherited by one son, while other sons get an equal value in money. In this case, the enterprise would continue operating without the dilemmas described above. If no son would like to take over the business of the father, there will also be no problem of fraternal squabbling. A number of informants complained that their sons do not wish to inherit the company they have set up, and all they can do is 'wait and see'. One informant had worked for a landlord in Gaoxiong, who had vast holdings in commercial fish ponds. 'After the father died', he said, 'no son wanted to run his business. They have their own occupations such as doctor, legislator, scholar, so they don't want to be a businessman.'

In Taiwan's expanding economy, with different occupations available to the younger generation, an arrangement can be made for one son to inherit the company, while other sons go out to work. In this case, the so-called *fen-jia* is only the division of money, and it does not affect the running of the company at all. For example, an informant asked his eldest son to inherit his steel company, while the second son, a doctor, got the money to run a hospital, and the third, a university lecturer, got money to buy a flat. Property, in terms of money, is equally divided among brothers, but in such cases does not result in the disintegration of a family firm. Social relations are preserved, and market relations are left untouched, avoiding family discord.⁴⁷² This type of *fen-jia* is new, and as Taiwanese society continues to industrialise, and more and more job opportunities in secondary and tertiary industries become available to family members, this type of family-firm division will be more prominent.

There is another way to prevent the family division disputes. It is common for the father to invest in different industries for different sons so that they have equal property inheritance, which prevents any argument over family division. One interviewee, whose firm produces cans to store chemical materials, opened another company to import and process iron. The first firm will be passed to his eldest son, and the second to the second son. In 1992 he was establishing a third firm, which involves a co-investment from the first two sons, but this third firm will belong to the third son. In other words, the property of the father is equally divided among sons through inter-investment by the three sons.

This type of family division occurred in the second phase, i.e., the centralised phase

⁴⁷¹ See Wong Siu-lun, *op. cit.*, p. 66.

⁴⁷² This type of *fen-jia* is more or less like the Japanese division of a family, i.e., only the eldest son inherits the family business, and all other sons find other jobs by themselves.

of paternal control, in Wong Siu-lun's model, and not in the third, segmented phase. This sort of *fen-jia* has developed in a capitalist business environment, and does not occur in the Chinese agricultural society. It is a combination of capitalist profit calculation and the family life cycle. Both principles, i.e., profit maximisation and harmonious familial relations, are preserved in this manner of family division.

In capitalism, capital always seeks the most profitable outlets, and when a family enterprise is well run and has earned money, the owner does not leave the money idle. S/he can either expand production or invest in another business. A survey done by the government in 1995 shows that about 70% of the surveyed 5,954 companies in manufacturing industry have no intention to diversify their investment into a different business. The four main reasons for not taking a diversification strategy are labour shortages (12.7%), insufficient profitability (12.6%), difficulty in securing loans (11.1%) and cut-throat market competition (10.8%).⁴⁷³ Among those who have diversified, half (49.3%) replied that the saturation of their main product market is the main reason to diversify their investment.⁴⁷⁴ In my own interviews, most of the new investments of my informants are based on their social networks from which they get the information about new market opportunities. These are not necessarily in the same industry in which they are working. If there is a good prospect of profits, they will put the money into it. Hamilton and Kao call this 'opportunistic diversification investment', for 'the investment pattern leads to an unusually wide spread of product lines within groups, and results in business groups being largely composed of a series of medium-sized firms'.⁴⁷⁵ We have emphasised that a family firm is still an enterprise in a capitalist society, and when a firm has profits, its main product may be in the mature phase in the product life cycle and it has to make hay while the sun shines. Investment diversification is one strategy to expand its market. In Taiwan, the significance of this sort of investment diversification has a specific cultural meaning, for it not only follows the market principle, but also preserves the tradition of family division. One informant owns a construction company. In 1989 he bought a grit-mining company. One son is in charge of the construction company, and the other is in

⁴⁷³ See Ministry of Economic Affairs (經濟部), *Zhizaoye Duojiachua ji Guojihua Diaocha Baogao (製造業多角化暨國際化調查報告, Reports on the Diversification and Internationalisation of Manufacturing Industry)* (Taipei: MOEA, 1995), pp.156-159, Table A-11-2.

⁴⁷⁴ *Ibid.*: p. 92, Table A-7-1.

charge of the new one. Though he is the real boss of the two companies, the two sons operate their respective companies, and needless to say will inherit their own company when *fen-jia* takes place. Through this form of investment, the informant avoided the worst of the construction recession in the construction industry in the 1990s, profiting from the new company.⁴⁷⁶

This kind of family division accommodates market principles and social relations nicely. It can avoid family disputes caused either by different management styles of the brothers in a company, or by uneven shares of company profits. It also conforms to market principles that every individual firm is responsible for its own profits. If a brother or a family member is not competent, it will affect only the relevant company and will not adversely affect the other.

In this case, it is quite easy to become a business group which consists of different firms run by the same family members. Business groups in Taiwan are usually of this type. It does not conform to the Wong model in which a family firm will be either fragmented or centralised. It is fragmented if we observe it from the transfer of ownership of several firms to different sons. However, from the perspective of the father entrepreneur, it is centralised. If all brothers work together, it forms a business group, and will not necessarily lead to any one phase in Wong's model.

As seen, we ought not reach the conclusion that a family firm cannot expand in scale to become a business group. There are three other factors inhibiting the growth of a family enterprise: firstly, market forces will exclude those enterprises which are not competitive. A lot of new firms open every year and a lot of others fold. In 1991, the average five-year survival rate of all enterprises was 68.8%, and the survival rate in the industrial sector was 73.6%.⁴⁷⁷ In 1994, 55,700 companies were newly set up, amid 18,501 closures.⁴⁷⁸ Though not all of the failures were newly established firms, the new firms have had to face a market

⁴⁷⁵ See Gary G. Hamilton and Kao Cheng-shu, 'The Institutional Foundation of Chinese Business: the family firm in Taiwan' (1990), p. 144.

⁴⁷⁶ He said that there are three subsidiaries of the new company to issue invoices and 'evade tax'.

⁴⁷⁷ See Small and Medium Enterprise Agency, the Ministry of Economic Affairs, *Zhonghuaminguo 84 Nian Zhongxiao Qiye Baipishu* (中小企業白皮書, *White Paper on Small and Medium Enterprises*) (Taipei: MOEA, 1996), p. 64.

⁴⁷⁸ *Ibid.*: p. 61. According to Cheng Zhengcang, in the 1980s, on average 381 new manufacturing firms entered the market, and 244 firms exited the market. See Chen Zhengcang, *Taiwan Zhizao Changshang Jiuru yu Tuichu zhi Yanjiu* (台灣製造廠商加入與退出之研究, *Firm Entry and Exit in Taiwan Manufacturing Industries*), *Shehui Kexue Luncong* (社會科學論叢, *Forum on Social Sciences*), p.229.

shared with old firms and are less likely to succeed. The survey done in 1995 shows that 44% of the existing SMEs have operated their business less than five years, while the figure for big enterprises is 32%. One out of five SMEs operated their business less than two years.⁴⁷⁹ This means that only about half of the existing enterprises survive more than five years, and if a firm wants to grow big, it has to face harsh market competition. Chen Zhengcang (陳正倉) found that the more competitive the market is, the higher the entry and closure probability.⁴⁸⁰

Secondly, as seen, family firms try to evade tax and turn to using family members to keep its financial secrets. Using family members can also prevent the labour-capital conflicts that afflict capitalist production. We have explained the dilemma the family enterprises face here, for if the family members (inner circle) are not competent, they would be expelled from the market.

Thirdly, even if a firm is very successful, it has to face the traditional problem of *fen-jia*. Businesspeople without a son, or in which no son is willing to take over their business, will not expand their business. For businesspeople with sons but only one enterprise, it is quite possible that the quarrels between brothers would fragment a business. Only those people with many enterprises to distribute equally to sons, or with one son inheriting the enterprise(s), could expand their scale of production and organise a business group.

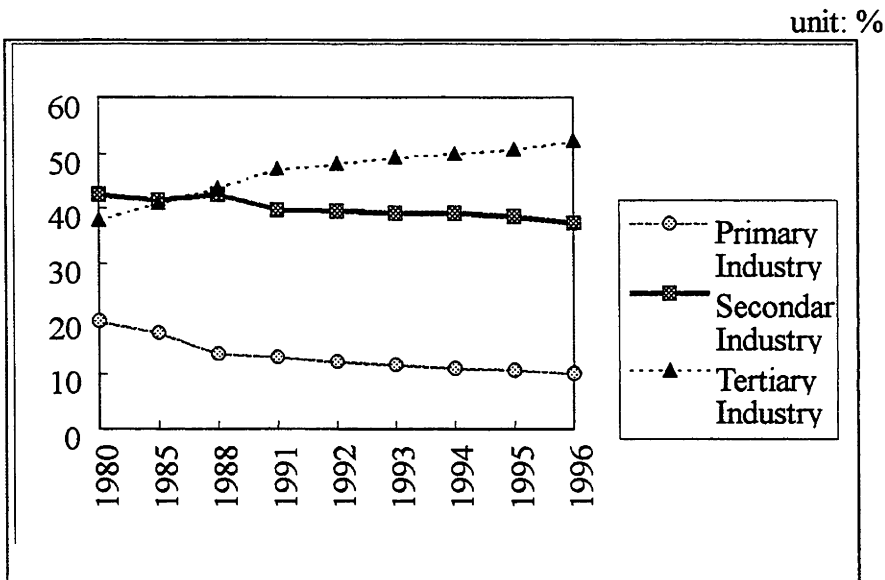
5.6 The New Market and Employment Situations

After the mid-1980s, labour shortages became a common topic among enterprise owners. The younger generation is not willing to work in manufacturing and insist on high pay and good working conditions. Figure 5.1 shows the employment structural change after 1980. The secondary sector reached its highest employment share in 1987, and then declined gradually, overtaken by the tertiary sector in 1988.

⁴⁷⁹ See Small and Medium Enterprise Agency, the Ministry of Economic Affairs, *op. cit.*, p. 72, Table 2-2-8.

⁴⁸⁰ See Cheng Zhengcang, *op. cit.*, p. 230.

Figure 5.1 Structure of Employees by Industry



Source: Council for Economic Planning and Development, *Taiwan Statistical Data Book* (Taipei: Council for Economic Planning and Development, 1997), p. 20.

After the lifting of martial law in 1987, workers could organise unions and could strike, but because most firms are family firms, it was difficult to take collective action. In smaller firms, it is easy for the boss to use social relations to prevent collective action and consciousness. When I computed the survey data of ‘*A General Survey of Social Change in Taiwan, 1992*’, which asked ‘do you agree to take collective action to strike’, I found that the bigger the firm, the more likely that the respondent would agree. The difference between groups is statistically significant at the level of 5%.⁴⁸¹

Labour shortages became a problem in the late 1980s, and many firms today complain that they cannot find enough workers. In a survey conducted in 1997, 23% of the manufacturing firms said that they faced the problem of labour shortages, varying directly with firm size. Among those hiring more than three hundred workers, 54% face this problem, compared to only 18% of those employing less than thirty workers.⁴⁸² Manual labourers (45%) and semi-skilled labourers (26%) are the most in demand. The workers needed by the firms hiring more than three hundred workers comprise 46% of the total

⁴⁸¹ It is a four scale question, i.e., strongly agree, agree, disagree and strongly disagree. Firm size is grouped into ‘no employees’ ‘less than twenty employees’ ‘fewer than one hundred employees’, ‘fewer than 500 employees’ and ‘more than 500 employees’. The mean score of the five groups is 3.06, 2.99, 2.95, 2.86, and 2.89 respectively.

⁴⁸² See Directorate-General of Budget, Accounting and Statistics, Executive Yuan, *Report on the Employment of Manpower, Taiwan Area, ROC, 1997*, p. 2, Table 1.

labourers required, while only 3% for those employing less than thirty workers.⁴⁸³

Some firms have sensed the change in the business environment and have begun to adopt methods conforming to market forces and to rationalise their human resources management. A survey done by the government revealed that the four main ways for SMEs to cope with labour-force shortages are: raising wages (26%), rationalisation of production (24%), reducing the scale of production or utilising a putting-out system (16%), and employing foreign workers (13%).⁴⁸⁴

Some of my interviewed companies said that they would move production lines overseas. With increasing land costs and the rising value of the New Taiwan Dollar, investment in Southeast Asia and China is one way to reduce production costs. I will discuss this topic in the next chapter.

Using the putting-out system can reduce costs. An interviewee who runs a textile firm said that he was happy to put out all the processes of his work because it resolves labour problems. He enjoys it when petty sub-contractors owning one machine bring presents in visiting him and ask him to give them work to do. He also says that he is no longer harassed by workers. Many informants said that the putting-out system did not emerge until the mid-1970s when there was no longer a cheap labour force. As Ke Zhiming has pointed out, the putting-out system became popular after the mid-1980s when it became harder to find any relatives or friends to work in the small-scale enterprises.⁴⁸⁵

However, the putting-out system is based on a specific industry structure, i.e., one with an easily divisible production process, in which it is easy to set up a small firm and in which big firms are willing to put out certain parts of the production process.⁴⁸⁶ The production process of traditional industries like textiles, electrical machinery and mechanical appliances are divisible. An informant who produces machinery to manufacture plastic milk bottles said that after he got an order, he designed the module, and then put out different parts of the machine to different single-task factories. Each single-task factory hands its finished products to him, and he then assembles the different parts in his factory and ships the assembled to the customer.

Besides the factor of divisibility, the putting-out system is also confined to the

⁴⁸³ *Ibid.*: pp. 32-39, Table 6.

⁴⁸⁴ See Small and Medium Enterprise Agency, *op. cit.*, p. 99, Table 3-2-10.

⁴⁸⁵ See Ke Zhiming, *op. cit.*, p. 45.

⁴⁸⁶ See Xie Guoxiong, *op. cit.*, p. 31.

difficulty of setting up a firm to produce a part of a product. If the cost of establishing a sub-contracting factory is high, it is unlikely that such a system will be set up. In Taiwan, no one cared about environmental costs before the mid-1980s, taxes were low, and workers were relatively cheap, so the determining factor was capital. One informant had a wool-spinning factory. He said that only a part of the whole production process could be put out, and the last stage of weaving wool products like combing wool is hard to put out due to the expensive machinery, that is not affordable by a small firm.

Using the putting-out system, a company can save different kinds of costs if the product quality is acceptable. It can save labour costs, which includes wages and social security expenses. It also saves the cost of the stock of raw materials and inventory. An informant got orders from customers, and then ordered raw steel from upstream companies, mainly China Steel, and transported the steel to a factory owned by others. After the factory finished cutting the steel according to orders, the products were carried to customers directly. He said proudly that 'I do not need any capital to set up a capital-intensive factory. Though the profit is less, e.g., you earn only two dollars per ton compared to three if it is cut by your own factory, it is still profitable, and I save a lot of troubles by not running a factory.'

Toyota's *JIT* (just in time) production prevails in Taiwanese industry, as in the manufacture of computers.⁴⁸⁷ A new type of production is *BTO* (buy to order), which means that a big firm will not put in an order until a customer places one. Thus, the cost of inventory can be transferred to the subcontractors. *JIT* and *BTO* methods of management, and the putting-out system, transfers the cost to subcontractors and reduces the burdens of larger firms.

The putting-out system is usually based on the availability of a marginal labour force, or in Marx's term, a reserve army. This system mobilises housewives and children, students, retired people, and even prisoners in jail.⁴⁸⁸ Because this marginal labour force does not work under the same roof, there are no obvious labour-capital confrontations, and

⁴⁸⁷ See Pan Meiling (潘美玲) and Zhang Weian (張維安), *Tanxing Shengchan yu Xieli Wangluo* (彈性生產與協力網絡, Flexible Production and Cooperative Networks) (Taichung: Tunghai University, 1997), unpublished manuscript, pp. 7-10.

⁴⁸⁸ See Xie Guoxiong (G. S. Shieh, 謝國雄), 'Yinxing Gongchang: Taiwan de Waibaodian yu Jiating Daigong' (隱形工廠：台灣的外包點與家庭代工, Invisible Factory: Subcontracting Points and Homeworkers in Taiwan), *Taiwan Shehui Yanjiu Jikan* (台灣社會研究季刊, *Taiwan: A Radical Quarterly in Social Studies*), no.13 (1992), pp. 142-147.

complaints about the Basic Labour Rights Law will not emerge. However, the marginal labour force is not only used in putting-out, but also in some big firms in order to reduce labour costs.

One owner uses older workers to deal with his labour shortages. All of the workers in his firm are Obasan (a Japanese term used in Taiwan, meaning women aged over forty), whom he described as 'not operating machines as swiftly as the young workers, but docile and willing to work overtime when it is urgent to turn out a batch of products'.

A popular recent method is to hire 'guest workers'.⁴⁸⁹ Taiwan had only 3,000 foreign workers in 1991, but this increased to 292,000 in 1996.⁴⁹⁰ 63% of the guest workers work in manufacturing industry. The textile and electronics industries absorbed another 26% of them.⁴⁹¹ According to regulations, the employer cannot pay a guest worker less than the minimum wage set by the government. In 1993, the minimum monthly wage was NT\$14,000 per month (about US\$550). Guest workers are usually paid the minimum wage, which is about 50% of the average wage received by native workers in manufacturing.⁴⁹² However, about six months of the wage of the guest workers goes to their government and brokers, and so they do not receive any money in the first few months. Thus, when they arrive in Taiwan, they always ask the employer to give them more work to do. This enables the employer to operate the machines more efficiently as no machine will be idle if the machines work twenty-four hours a day. An interviewee praised the Thai guest workers as 'easy to use' (好用). 'Because they have to pay back the money they borrowed in their home country, they have to work hard to earn more money. They hope to work overtime every day, and if possible, sixteen hours a day so as to earn NT\$30,000 a month'.

Not every company is eligible to import foreign workers. One informant was not able to employ guest workers. He found a rule set by the government that a 'newly set-up company is allowed to import workers', so he closed his old firm, applied to establish a

⁴⁸⁹ See M. G. Quibria, 'Labour Migration and Labour Market Integration in Asia', *The World Economy*, vol. 20, no.1 (1997), pp. 21-42.

⁴⁹⁰ See Jingjibu (經濟部, Ministry of Economic Affairs), *Zhonghua minguo Bashiliu nian Zhongxiao Qiye Baipishu* (中華民國八十六年中小企業白皮書, White Paper on Small and Medium-sized Enterprises in the Republic of China, 1997) (Taipei: Ministry of Economic Affairs, 1996), pp.3-11, 3-12.

⁴⁹¹ *Ibid.*: pp. 3-12.

⁴⁹² See Council for Economic Planning and Development, *Taiwan Statistical Data Book* (Taipei: Council for Economic Planning and Development, 1997), p. 22.

new one, and at the same time applied to import foreign workers. “Most workers in my factory are guest workers”, he said. “They work very hard, and can work day and night. Even though our languages are different, I show them how to operate the machines, and then they know how to do it. My machines can be operated twenty-four hours a day to meet the demand from customers. This reduces my capital expenditure.”

However, the economic recession beginning in 1995 drove up the unemployment rate, and many native workers demanded that guest workers be prohibited, for the labour tasks like construction and lower skilled work, which used to be taken by aboriginal people or retired veterans, are gradually being taken by foreign workers. The shutdown of many big factories makes the issue hotter. But from the perspective of the boss, since guest workers are ‘easy to use’, the government should not prohibit their use. These labour-capital conflicts in the domestic economy are being transformed into conflicts between different groups of workers. Accompanying the globalisation of the economy, labour migration problems have emerged.

The third way is to rationalise production, i.e., to use more capital and machinery to replace labour, or to ‘democratise’ the work place. An interviewee rationalised his production lines after 1990 and spent a lot of time discussing with his staff how to raise efficiency and minimise the wastage of production materials, or to arrange the production flow more efficiently. In 1992, he found that labour costs increased from 11% to 40%, and he began to further rationalise labour costs. He did not purchase more capital goods to automate production, but tried to find out where his labour force was redundant and sought to cut high labour costs. Another informant changed his personnel management from 1988. He asked his workers their opinions about how to pay wages, and the wage was changed from an hourly wage to piece wages. Whenever he gets an order, he will let everyone know how much money he will get from the job, and then discusses how to distribute the profits between the owner and workers. The criterion for the distribution is based on the ‘piece wage’, i.e., how much time the workers need to manufacture the product, and he then would convert that time to a wage. He said that the monthly wage of the workers increased from NT\$30,000 to 80,000 (about US\$3,000) and at the same time he saved a lot in supervisory management costs.

5.7 Conclusion

In this chapter, I have explained how traditional values operate in family enterprises. Obviously cultural theory could explain the development of Chinese business, but cultural theory does not pay any attention to markets and political forces and thus fails to explain the failure of a lot of family enterprises. We cannot deny the importance of traditional values, but we have to put them within the context of specific social structures, which might hinder or facilitate the functioning of these values. In Taiwan, corrupt political and economic structures encourage the use of family members as an inner circle in the family enterprise. But the imperative of market forces will drive these family enterprises out of the market if they are not efficient enough to compete with others.

Family values are important in the operation of family firms. Traditional values filial help to tie together the different interests among family members, but the market principle disintegrates the cohesion. So-called *renqing* is not only an asset of a family enterprise, but also a liability, and the more the *renqing*, the more one becomes liable to become indebted others. Personal networks are not always assets to one's balance sheet.

Fen-jia is one way to the circumvent incompetence of family members and to resolve disputes among them. *Fen-jia*, however, might result in the fragmentation of a family firm. But as I have noted, what is more common today in Taiwanese society is that the father sets up more than one small firm and distributes them equally to different sons. Too, the development of the Taiwanese economy offers more opportunities for the younger generation to seek new occupations and they do not need to rely on the family firm. This will reduce the tendency of a family firm to splinter if only one son inherits the property while others accept monetary compensation. When a father entrepreneur 'opportunistically' diversifies his investment and sets up firms for more than one son, there will be the possibility of forming a business group, which is outside the predictions of Wong's model. In other works, the cultural constraint of *fen-jia* generates a unique type of economic organisation – the existence of numerous SMEs and business groups at the same time.

Because of Taiwan's labour shortages since the late 1980s, companies have had to change their ways of managing human resources. One way is to rationalise production lines, and employ less workers. A second method is to utilise a putting-out system and transfer the costs to smaller firms. A third way is the hire foreign workers. Lastly, many SME

owners have sought to production lines overseas, which will be discussed in the next chapter.

Chapter 6: SMEs' Overseas Investment

I have written at length about the social structures affecting business practices in Taiwan. In this chapter, I will discuss the business practices of Taiwan's SMEs abroad. The social structures they face abroad are different from what they encounter in Taiwan, and some of their business practices shift in line with this. Comparing these differences in their business practices can illuminate how much 'Chinese business practices' are affected by culture, and how much they are situated within a specific social setting. I will discuss financial management, marketing management and human resources management in the alienated social milieu. Among other things, it will be seen that their human resources management is much more authoritarian overseas than in Taiwan, which refutes the myth of Chinese 'paternalistic' management.

6.1 The Trend to Invest Overseas

The sharp appreciation of the Taiwan dollar in the mid-1980s was one of the major reasons to shift production lines overseas. According to a 1991 survey conducted by the Ministry of Economic Affairs, what also pushed companies to make such investments was not only the exchange rate, but also rising labour costs and land costs (55%, 40% and 39%); and the three main attractions overseas were cheap labour costs, a developing overseas market and a desire to sell products from within the local market (67%, 54%, 30% out of five hundred and seventy-four firms sampled).⁴⁹³ After 1991, the reasons to invest overseas changed slightly. Utilising cheap labour remains important, but not as significant as before. For those firms investing between 1987 and 1991, 67% singled out cheap labour as the main reason to invest overseas, a percentage that declined to 55% for firms investing after 1995. The potential local market and an effort to produce locally for Taiwan's buyers gained weight after 1995. (See Table 6.1)

⁴⁹³ See Jingjibu Tongjichu (經濟部統計處, Statistics Section, MOEA), *Zhonghuaminguo Taiwan diqu Zhizaoye Touzi Yixiang Diaocha Baogao* (中華民國台灣地區製造業投資意向調查報告, *Report on Manufacturing Industry's Investment Purposes in Taiwan, ROC*) (Taipei: Economic Ministry, 1992/April), pp. 9-10.

Table 6.1 Reasons to Invest Overseas

Unit: %

Firm Size by Employee	Local Market Potential	Request from Overseas Buyers	Follow Taiwan's Buyers	Globalisation	Cheap Labour	Domestic Investment Milieu Deteriorated
> 300	59.8	25.4	14.8	44.9	55.5	26.3
> 100	50.0	23.4	14.1	34.8	56.5	30.4
< 99	46.9	24.4	22.3	19.6	67.4	36.0
Year of Overseas Investment						
Before 1986	65.6	16.4	14.8	27.8	62.3	24.6
1987-91	44.7	26.0	15.7	26.7	67.3	34.8
1992-94	48.9	24.8	20.6	24.5	64.5	37.0
After 1995	56.8	22.7	27.3	29.6	55.0	23.6
Investment by Area						
China	48.8	22.1	24.5	19.4	72.1	38.2
Hong Kong	58.8	41.2	27.5	52.9	31.4	15.7
USA	70.4	38.9	8.3	43.5	22.2	10.2
Malaysia	43.3	34.3	7.5	43.3	53.7	26.9
Singapore	66.7	33.3	11.1	50.0	27.8	11.1
Thailand	40.6	14.5	14.5	33.3	69.6	36.2
Indonesia	47.4	15.8	7.9	13.2	79.0	34.2
Philippines	22.7	22.7	0.0	40.9	81.8	50.0
Vietnam	24.4	15.6	11.1	26.7	64.4	40.0
Average						
	49.6	24.5	19.8	26.3	63.7	33.5

Source: Jingjibu Tongjichu (經濟部統計處, Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duiwai Touzi Shikuang Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業對外投資實況調查報告—八十五年, *Survey on Overseas Investment of the Manufacturing Industry in Taiwan, ROC, 1996*) (Taipei: MOEA, 1997), pp. 70-73, Table 4.

Note: The question is multiple choice, so the sum of the percents is over 100.

Table 6.2 shows the amounts Taiwanese companies invested overseas in a range of Asian countries. This overseas investment increased sharply after 1986. Before 1990, most overseas investment poured into Southeast Asia, but after the easing of political tensions between Taiwan and China and the development of China's economy, huge amounts of Taiwanese capital flowed into China starting in 1991. Up to the end of 1997 China absorbed about half of the Taiwanese capital invested overseas. In 1997, however, only about 21% of this capital flowed into China. This was a result of the Taiwan government's

'Go Slow Toward China' (戒急用忍)⁴⁹⁴ policy, which was intended to counterbalance China's military exercises from July 1995 to March 1996.

Table 6.2 Areas and Annual Amount of Overseas Investment (1986-1997)

unit: million US\$

Year	1959-1987	1988	1989	1990	1991	1992
Thailand	885.0	859.9	892.2	782.7	538.5	289.9
Malaysia	151.2	306.1	799.7	2,347.8	1,326.2	574.7
Philippines	16.9	109.9	148.7	140.7	12.0	9.1
Indonesia	2,400.6	913.0	513.2	618.3	1,057.3	563.3
Singapore	465.3	6.4	5.2	47.6	12.5	8.8
Vietnam	--	--	1.0	228.2	498.1	538.8
China	--	--	--	--	2,710.0	5,543.0
Subtotal	3,919.0	2,195.3	2,360.0	4,165.3	6,199.2	7,527.8

Year	1993	1994	1995	1996	1997	Subtotal
Thailand	215.0	477.5	1,803.9	2,785.8	*405.9	9,441.2
Malaysia	331.2	1,122.8	567.8	310.3	480.4	8,318.2
Philippines	5.4	267.8	13.6	7.4	13.1	744.5
Indonesia	127.5	2,487.6	567.4	534.6	3,414.9	13,284.2
Singapore	69.5	100.7	31.6	165.0	230.3	1,142.9
Vietnam	398.5	495.8	1,216.9	530.0	241.0	4,301.9
China	9,965.0	5,395.0	5,777.0	5,141.0	*1320.7	35,851.7
Subtotal	11,116.0	10,347.8	9,992.6	9,637.8	6,150.7	73,307.7

Source: Originally from Thailand BOI, Malaysia MIDA, the Philippines BOI, Indonesia BKPM, Vietnam SCCI, Investment Commission, MOEA. Cited from Touzi Yewuchu (投資業務處, Investment Department), *Woguo zai Dongxie Geguo Touzi Tongji Jianxi* (我國在東協各國投資統計簡析, *Brief Analysis on Taiwan's Investment in ASEAN*) (Taipei: Investment Department, unpublished paper, 1998).

Note: '*' means the figure was collected in November, 1997, rather than at year end.

6.1.1 Who Invests Overseas?

In a survey conducted by the Ministry of Economic Affairs in 1996, 47% out of the surveyed large enterprises (over three hundred employees) had already invested overseas,

⁴⁹⁴ This policy was addressed by President Lee Teng-hui in a public speech on 14 September 1996 to limit Taiwan's economic exchanges with China because of China's political intention to 'utilise' *Taishang* to force Taiwan government to make concessions to China. See Mainland Affairs Commission (陸委會), *Kuayue Lishi de Honggou--Liang'an Jiaoliu Shinian de Huigu yu Qianzhan* (跨越歷史的鴻溝—兩岸交

while only 29% of the firms employing less than three hundred but more than one hundred workers had done so. The figure fell to 25% for firms employing less than a hundred workers.⁴⁹⁵ The percentage of SMEs investing overseas is obviously quite high. Electronics (25%), plastics products (11%), metallic products (9%) and textiles (5%) are the four main industries to invest overseas.⁴⁹⁶

A Ministry of Economic Affairs survey in 1991 found that most labour-intensive industries, especially those firms which had invested in China, reduced or stopped their domestic production, while heavy industries either maintained or expanded their production scale. This means that SMEs that were not internationally competitive found they had to move their production lines abroad, while for big firms the overseas investment is a business strategy to adjust and expand their global production. This kind of SME overseas investment is much like Japanese overseas direct investments before the mid-1980s, which aimed at securing a local market or for re-export to the US market.⁴⁹⁷ This is different from a multinational company, which sets its marketing strategy and components production according to different regions' economic situation. For example, a Japanese multinational company has invested in Malaysia to produce VCRs, but its components derive from one hundred and seventeen firms producing in Japan, Malaysia, Singapore, Thailand and Australia.⁴⁹⁸ The survey of 1996 shows that the three main reasons for big firms that employ over three hundred workers to invest overseas are to enter the local market (60%), cheap labour (56%) and globalising their business (45%). For SMEs employing less than a hundred workers, finding cheap labour (67%) is more important. However, entering the local market is another important reason (47%), as is a new trend to follow Taiwan's buyers by going overseas to invest (22%).

流十年的回顧與前瞻，*Crossing Historical Cleavage—Past and Future of Exchanges Across Taiwan Strait* (Taipei: Mainland Affairs Commission, 1997), p. 419.

⁴⁹⁵ See Jingjibu Tongjichu (經濟部統計處，Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duojiachua ji Guojihua Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業多角化暨國際化調查報告, *Reports on the Diversification and Internationalisation of Manufacturing Industry*) (Taipei: MOEA, 1995), p. 40, Table 5-1.

⁴⁹⁶ See Jingjibu Tongjichu (經濟部統計處，Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duiwai Touzi Shikuang Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業對外投資實況調查報告—八十五年，*Survey on Overseas Investment of the Manufacturing Industry in Taiwan, ROC, 1996*) (Taipei: MOEA, 1997), p. 46-49, Table 2-4.

⁴⁹⁷ See Akira Suehiro, *Ajia Kougyouka no Dainamizumu* (*The Dynamics of Asian Industrialisation*), in Akira Kudo (ed.), *Nijisseiki Shihonshyugi II* (*Twentieth-Century Capitalism II*) (Tokyo: University of Tokyo Press, 1995), p.180.

⁴⁹⁸ *Ibid.*: p. 181.

6.1.2 Where to Import Material to Produce?

The data shows that in 1994 about three-quarters of the Taiwanese firms imported the bulk of their product's materials from Taiwan,⁴⁹⁹ while the percentage in Japan for investments in less developed countries in 1990 was 79.1%.⁵⁰⁰ From this investment pattern, we can see that overseas investments do not necessarily have much backward linkages to the local economy. This might result in an enclave economy, as dependency theory would predict. But as time passes, will these overseas firms buy more materials and intermediary goods from the local economy, if the local economy can produce the same quality products? The survey of MOEA shows that the longer a company is established in a local economy, the more likely that it purchases components from that local economy.⁵⁰¹ Table 6.3 similarly shows that the earlier a firm invested overseas, the more likely that it uses components or semi-finished goods from local enterprises, and the less dependent it became on Taiwan's sources. For Japanese companies, only 53.5% will import the basic materials from Japan after five years, while 35.7% will buy theirs from local non-Japanese companies.⁵⁰² In the history of Taiwan's economic development, there is a similar so-called 'technology spill-over effect', as in the cases of TV production⁵⁰³ and sewing machines,⁵⁰⁴ also called a 'trade substitution effect'. This means that the expansion of the host country's industry will eventually remove the necessity to import intermediary goods from the parent country. If overseas affiliates can produce the same quality products as in Taiwan with lower cost, Taiwan will increase imports from the overseas affiliates, which will induce a 'reverse import effect', and reduce the surplus gap between the investing country and the host country.⁵⁰⁵ The shrinking trade surplus with ASEAN in these years can be viewed as the result of this 'trade substitution effect' and 'reverse import effect', especially with

⁴⁹⁹ See Zhang Yingzhe and Zhang Longhong, *op. cit.*, p. 69.

⁵⁰⁰ See Economic Planning Bureau, *op. cit.*, 134, Table 1-12.

⁵⁰¹ See MOEA, *op. cit.*, 1995, p.19.

⁵⁰² See Economic Planning Bureau, *op. cit.*, 134.

⁵⁰³ See Suehiro Akira, *op. cit.*, pp.173-175.

⁵⁰⁴ See Schive Chi (薛琦), "Technology Transfer Through Direct Foreign Investment: A Case Study of Taiwan Singer". *Proceedings of the Academy of International Business: Asian -Pacific Dimensions of International Business*, 1979 (Dec.).

⁵⁰⁵ See Lin Caimei (林彩梅), 'Duoguoji Qiye Jishu Yizhuan yu Woguo Chanye Guoji Shuiping Fengong' (多國籍企業技術移轉與我國產業國際水平分工, Technology Transfer of MNE and the International Horizontal Division of Labour of ROC's Industry) (Taipei: Chinese Culture University, 1995), pp. 7-8.

Malaysia.⁵⁰⁶

Table 6.3 Source of Components and Semi-Products for Overseas Affiliates

Firm Size by Employees	From Taiwan	From Local <i>Taishang</i>	From Local Enterprise	From Other Country	unit: %
> 300	50.5	12.8	22.0	15.2	
> 100	52.9	14.6	19.2	13.3	
< 99	51.0	21.0	21.3	6.7	
Year of Overseas Investment					
Before 1986	40.3	12.8	28.9	18.0	
1987-91	51.1	18.2	21.6	9.1	
1992-94	49.5	20.1	21.7	8.7	
After 1995	59.4	17.0	15.7	7.9	
Average	51.1	19.7	21.1	9.1	

Source: Jingjibu Tongjichu (經濟部統計處, Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duiwai Touzi Shikuang Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業對外投資實況調查報告—八十五年, *Survey on Overseas Investment of the Manufacturing Industry in Taiwan, ROC, 1996*) (Taipei: MOEA, 1997), pp. 97-98.

6.1.3 The Economic Effect of Overseas Investment

The trend to invest overseas helped to create a booming trade between Taiwan and other East Asian countries. It is the so-called 'investment-induced trade effect'. Companies moving their production out of Taiwan could either dispose of their machinery in Taiwan or ship it overseas to produce the same products. Since to use the machinery to produce in Taiwan is no longer profitable, it is usually not sold in Taiwan but shipped overseas. This is one reason why Taiwanese companies' sales to ASEAN countries and Hong Kong (including China) increased steadily. Its major export products centred on electrical machinery and mechanical appliances, which comprised 51.5% and 34.6% of total trade in the two regions in 1996.⁵⁰⁷ Table 4.3 shows that Taiwan's exports to ASEAN countries increased from 10% of total exports to 13.3% between 1992 and 1997, while imports

⁵⁰⁶ Board of Foreign Trade, MOEA (經濟部國際貿易局), *Guoji Maoyi Qingshi Fenxi* (國際貿易情勢分析, *Analysis of International Economy*) (Taipei: Board of Foreign Trade, MOEA, Jan 1998).

⁵⁰⁷ See Board of Foreign Trade, *Foreign Trade Development of the Republic of China, 1996* (Taipei: Board of Foreign Trade, 1997), p.26, 30.

increased from 8.4% to 11.6%. Exports to Hong Kong and China increased more significantly, from 18.9% to 23.5% in the same period, but imports remained insignificant because of Taiwan's restrictions on imports from China.

For those Taiwanese firms investing in ASEAN countries, the percentage of imported machinery is 89.7%. 72.1% of this imported machinery comes from Taiwan.⁵⁰⁸ 84% of the SMEs and 85% of the big businesses shipped their machines from Taiwan.⁵⁰⁹ This situation is the same for Japanese companies that invested in less developed countries. According to a survey done by the Japan Economic Planning Bureau in 1990, 62.9% imported their own company's machines when they started their overseas firm, and 27.6% bought the machines from other Japanese companies located in Japan. In total, over 90% used Japan-made machines to produce in less developed countries.⁵¹⁰

However, this increasing interdependent trade relationship makes Taiwan vulnerable to the Asian financial crisis that commenced in 1997. I will leave this issue to the end of this chapter.

6.2 Starting a New Business Overseas

6.2.1 The Overseas Chinese Community and Taiwanese Overseas Investment

One advantage for *Taishang* (Taiwanese businesspeople investing overseas, 台商) to invest in East and Southeast Asia is that there are a lot of overseas Chinese (*Huaqiao*, 華僑), who can play the role of middleman to channel capital. Their situation is similar to those Japanese SMEs which tried to invest overseas in the late 1960s, and found Taiwan was the most convenient place for them because many of the older Taiwanese are fluent in Japanese.

Malaysia is a good case. One informant's father came to Taiwan after 1949, and his family keeps in touch with their relatives scattered in Asia. One of his cousins is Malaysian

⁵⁰⁸ The survey is done in 1994 by MOEA. See MOEA, *Woguo Duiwai Touzi dui Dongnanya Guojia Jingji ji Shehui Yingxiang zhi Shizheng Yanjiu (Zhaiyao Baogao)* (我國對外投資對東南亞國家經濟及社會影響之實證研究—摘要, *A Summary Report of Taiwan's Overseas Investment and its Socio-Economic Impact on Local Society in ASEAN*) (Taipei: MOEA, 1995), p.17.

⁵⁰⁹ See Zhang Yingzhe and Zhang Longhong, *op. cit.*, p.69, Table 2.

⁵¹⁰ See Keizai Kikakuchou Chouseikyoku, *Nihon to Sekai wo Kaeru Kaigai Chokusetsu Tousei (Economic Planning Bureau, Overseas Investment that changes Japan and the World)* (Tokyo: Ookurashou Printing Bureau, 1990), p.132, Table 1-8.

Chinese, and with his help he set up his firm in Penang, and his cousin became the manager of the factory. In 1997 he set up another new firm with the help of another cousin in China. Many informants said that language is one of the major problems they face, and overseas Chinese become good candidates to bridge the gap between two languages.

Because these small and medium-sized investors have no command of other languages, China has become the most popular place to invest. The benefit is that they can handle everything by themselves without middlemen. From the building of the factory to labour management, they are able to communicate with the local people. An informant investing in Malaysia and China compared the labour management in the two countries. 'In Malaysia, language and culture are two major problems. Malaysian workers complain to the Ministry of Labour Affairs whenever there is a dispute. In China, I can communicate with them in Mandarin, and explain everything when they have questions. So in two months, the production line can be equipped with a labour force and ready for production.' The language problem also affects the decision of where to locate the factory. In Guangdong, *Taishang* firms cluster in Dongguan (22%) and Shenzhen (25%),⁵¹¹ while in Malaysia, they cluster in Penang (40%) and Klang Valley near Kuala Lumpur (32%).⁵¹² They choose these locations to facilitate doing business with the many other *Taishang* in these areas, and they can expect local personnel to have learned Chinese.

For those places where Chinese is not the official language, overseas Chinese who speak Mandarin or Hokkien become the intermediators.⁵¹³ The most popular intermediators are overseas Chinese who studied in Taiwan and went back to their host country to work. Up to 1996, there were more than eight-two thousand overseas Chinese students from Southeast Asia who had graduated from Taiwan's universities, and up till 1997, more than one hundred thirty-five thousand overseas Chinese students who had

⁵¹¹ The data is calculated from 1991 up to November 1996 according to Taiwan government's released data, which is different from China's statistics. See Jinjibu Touzi Shenyi Weiyuanhui (經濟部投資審議委員會, Investment Commission, MOEA), *Zhonghuaminguo Huaqiao ji Waiguoren Touzi, Dui Dalu Jianjie Touzi Tongji Yuebao* (中華民國華僑及外國人投資, 對大陸間接投資統計月報) (Taipei: Investment Commission, MOEA, Nov. 1996), p.55.

⁵¹² See Gong Yijun (龔宜君), *Guoguo Touzi yu Taiwan Guanlian: Taishang zai Malaixiya de Yixie Guancha* (跨國投資與台灣關聯: 台商在馬來西亞的一些觀察; Cross-Border Investment and Linkage with Taiwan: Some Observations on *Taishang* in Malaysia) (Taipei: Sinica Academia, unpublished conference paper, 1997), p. 12.

⁵¹³ In Taiwan's university campus, there are more and more ads on the wall to find overseas students to teach local language. Usually these students are offered jobs before they graduate.

studied in Taiwan.⁵¹⁴ They become the reserve army for the *Taishangs'* investment in the area. One company's executive manager said that these overseas Chinese students were very helpful to his investment in Penang when he came in 1987. They introduced government officials and relevant managers of the industry to him, which enabled him to evaluate the investment environment quickly. In another firm, the executive manager, general manager and purchasing managers are all Malaysian Chinese with diplomas from Taiwan. In Malaysia, the Association of Taiwan-Graduated Students has become the most important consulting organisation for *Taishang*.⁵¹⁵

6.2.2 The Host Countries' Policies and Types of Ownership

In Chapter Three, we found that in Taiwan the most common means to start a new business is through a partnership, which gradually evolves into a wholly-owned company. A survey done by the *Ministry of Economic Affairs* in 1996 shows that the most common type of ownership among those investing overseas is wholly-owned (61%)⁵¹⁶ (See Table 6.4). However, once abroad, the proportion of partnerships is much higher than in Taiwan. In Taiwan, only 12.7% enterprises adopt the partnership format, while among those companies investing overseas, the percentage reaches 67% in some regions. In the same survey done in 1995 with the same question, but using 'single choice' instead of multiple choice, the percentage of joint ventures among 1,680 firms is 45%, which is still higher than 12.7%.⁵¹⁷

The different ownership forms adopted by *Taishang* are based upon profit calculations that are affected by the host government's policies. In his research on the Canadian-Chinese business community, Peter S. Li found that partnership was the most common form before the Second World War due to a lack of labour and capital in the

⁵¹⁴ See Jiaoyubu Tongjichu (教育部統計處, Statistics Section, the Ministry of Education Affairs), *Huiguo Shengxue Qiaosheng Renshu Tongji* (回國升學僑生人數統計, *Statistics on Overseas Chinese Students Studying in Taiwan*) (Taipei: the Ministry of Education Affairs, 1998), p.73.

⁵¹⁵ See Gong Yijun, *Cross-Border Investment and Linkage with Taiwan: Some Observations on Taishang in Malaysia*, p. 12.

⁵¹⁶ The data does not tell us whether it is the present ownership type, or it is the type when one invested overseas. The question it asks in the questionnaire is "Regarding to overseas investment, what is the type your company adopts?" (貴公司對外投資所採取之型態). The question is ambiguous, for it can not refer to the past and the present type in Chinese. However, according to the explanation of the business organisation in page nine, I will assume that it asks the present ownership type.

⁵¹⁷ See Statistics Section, MOEA, *Reports on the Diversification and Internationalisation of Manufacturing Industry*, p. 240, Table B-13.

community. When Chinese family members were allowed to immigrate to Canada after the Second World War, labour force shortages no longer posed a problem, and the 'ethnic partnership system' gradually disappeared.⁵¹⁸

Table 6.4 Types of Ownership in Host Countries

Firm Size by Employee	unit: %								Total Number
	Wholly-Owned	Joint Venture with Taiwan co.	Joint Venture with overseas Taiwan co.	Joint Venture with local co.	Joint Venture with host government	Joint Venture with foreign co.	Other		
> 300	64.4	12.7	4.7	29.7	10.2	17.8	4.7	236	
> 100	58.7	11.4	8.2	27.7	10.3	14.1	6.5	184	
< 99	60.8	16.7	7.6	21.5	9.8	8.2	1.7	892	
Year of Overseas Investment									
Before 1986	60.7	11.5	13.1	32.8	8.2	14.8	4.9	61	
1987-91	65.0	14.5	5.7	26.3	9.7	11.5	3.2	434	
1992-94	59.0	15.2	7.0	23.0	10.9	9.2	2.7	597	
After 1995	59.6	17.7	8.6	19.1	8.2	12.3	2.3	220	
Investment by Area									
China	63.7	15.4	5.2	20.0	12.6	10.0	2.2	849	
Hong Kong	60.8	9.8	13.7	29.4	5.9	7.8	3.9	51	
USA	71.3	17.6	11.1	22.2	1.9	14.8	5.6	108	
Malaysia	47.8	25.4	10.5	31.3	4.5	11.9	3.0	67	
Singapore	44.4	5.6	5.6	50.0	0	38.9	0	18	
Thailand	52.2	10.1	14.5	42.0	5.8	10.1	0	69	
Indonesia	34.2	13.2	13.2	44.7	5.3	2.6	10.5	38	
Philippines	54.6	0	0	31.8	0	9.1	13.6	22	
ASEAN 5	36.1	10.7	8.2	29.6	3.2	8.9	3.2	280	
Vietnam	48.9	24.4	4.4	17.8	13.3	15.6	2.2	45	
Average	61.1	15.2	7.2	23.9	9.9	10.8	2.9	1312	

Source: Jingjibu Tongjichu (經濟部統計處, Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duiwai Touzi Shikuang Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業對外投資實況調查報告—八十五年, *Survey on Overseas Investment of the Manufacturing Industry in Taiwan, ROC, 1996*) (Taipei: MOEA, 1997), pp. 76-77, Table 4.

Note: The question is multiple choice, so the sum of the percent is over 100.

⁵¹⁸ See Peter S. Li, 'Chinese Investment and Business in Canada: Ethnic Entrepreneurship Reconsidered',

The host country usually designs very good packages to attract foreign capital. However, it also wants to gain from the policy, e.g., for the foreign-owned company to export its products to earn foreign exchange, or to encourage co-operation between local and foreign firms so as to access new technology from foreign companies. If there are restrictions on the establishment of wholly-foreigner-owned firms, foreign investments are more inclined to take a joint venture format. Foreign investors will calculate the costs and benefits so as to take advantage of the offers of the host country.

The Chinese government encourages joint ventures. The local authorities always ask foreign investors to agree to provide a large sum of investment capital, though the realised capital is often less than what has been promised. Up to the end of 1996, the negotiated capital of Taiwan's investments was US\$34.5 billion, but the investment capital actually was recorded as only reaching US\$14.9 billion, 43% of the negotiated capital.⁵¹⁹ Besides, the products of a wholly-foreigner-owned company can be sold only to a certain degree in China's domestic market, so this also encourages foreign capital to enter into a joint venture with local enterprises. Malaysia has similar restrictions. As one informant said, 'so far as I know, most Taiwanese firms investing in China are joint venture companies. That is because the businesspeople are not familiar with the local social milieu, so they are afraid of putting all their money there. Besides, the products of wholly-foreigner-owned company have to be exported. So they prefer to take the joint venture form to reduce the risk on the one hand, and to be able to sell the products in the domestic market on the other hand.' In Malaysia, the government regulates that there must be at least two local shareholders in a foreign invested company. A common way to evade the regulations is to ask local Chinese to find two *Alibabas*⁵²⁰ who contribute one Malaysia dollar to be a shareholder, but the real business is controlled by the Taiwan investor. In the Philippines, the local people should have at least 60% of the shares, but an informant found an *Alibaba* via his friend. Different government policies produce different outcomes.

The distribution of ownership types differ from country to country. Among the 1,312 surveyed firms, 849 (65%) had invested in China and 45 (3.4%) in Vietnam. There two

Pacific Affairs, vol. 66, no. 2, p. 225.

⁵¹⁹ See Mainland Affairs Commission, *Crossing Historical Cleavage--Past and Future of Exchanges Across Taiwan Strait* (1997), p. 372, Table 7-1.

⁵²⁰ This means Malays whose names are put on the board by overseas investors but who do not have any real power.

countries have 'socialist economies', and most business activities to a are still under government control.⁵²¹ Joint ventures with local governments provide one way to escape bureaucratic harassment -- and enables a foreign company to benefit from the newly established relationship. One businessman runs a wholesale centre in Guangdong, which distributes goods to other provinces in China by railway. However, railways in different provinces are managed by different provincial bureaux. Other provincial railway bureaux might not take care of the goods, and might leave them at the provincial railway station for a long time. So this businessman co-operates in a venture with the army, and whenever he ships the commodity by railway, he puts a label 'Military Use' on it, which enables the shipped goods to be transported quickly.⁵²² 12.6% of the Taiwanese businesspeople who have invested in China and 13.3% of those who invest in Vietnam establish joint ventures in with the host government, which is much higher than the percentage of joint ventures in any of the other five ASEAN countries (3.2%) or the USA (1.85%) (see Table 6.4).

6.2.3 Wholly-Owned Companies and Tax Evasion

If a company is not targeting the other country's domestic market, or the host government restricts the sale of products in the domestic market, or controls the foreign exchange, it usually takes the form of a wholly-owned firm abroad. In a country controlling foreign exchange, it will be easier for the parent company to manage all the finances. One company has an affiliate in Malaysia. The affiliate's orders and financial transactions clearances are made in Taiwan. The parent company remits money to the affiliate every month to pay wages and to meet the other costs of business operations, but the money to pay for the imported goods and the money received from exported goods is cleared in Taipei instead of in Kuala Lumpur. In this way, the company can prevent the problem of foreign exchange controls. More important, I believe, is to evade tax, which often takes the form of 'price transfers'.

Taiwan data show that only 39% of the firms' overseas operations made any profits,

⁵²¹ See Mainland Affairs Commission (陸委會), 'Zhonggong Guoqi Gaige zhi Youli ji Buli Tiaojian' (中國企改革之有利及不利條件, Situations of the Reform of Chinese Public Enterprises), *Dalu Gongzuo Jianbao* (大陸工作簡報, *Briefing on the Work on Mainland China*), Executive Yuan Meeting, no. 2561, p. 3-16.

⁵²² See Mainland Affairs Commission (陸委會), *Taishang fu Dalu Touzi Shibai Anli zhi Yanjiu* (台商赴大陸投資失敗案例之研究, *Research on the Failed Taiwan Businesspeople in Mainland China*) (Taipei: Mainland Affairs Commission, 1992), p. 182.

and 30% reported a loss, while the rest reportedly broke even, according to the survey of 1996. The earlier a company set up overseas, the more profits it made. 50% of those firms going overseas after 1995 reported a loss, and only 21% showed a profit. Big firms employing more than three hundred workers profited more (51% out of 217 firms) than SMEs employing less than three hundred (about 37% out of 1,033 firms).⁵²³ We can doubt that the firms were telling the government the truth. Though it is possible that high initial costs would not provide immediate returns, another possibility is tax evasion.

In the case above, after the parent company receives an order in Taiwan, it puts this order to the Malaysian affiliate to produce it. Say that the money it gets for the order is \$200, and the raw materials cost \$100, the wage cost is \$20, and business operations cost \$10, it will profit by \$70. However, the affiliate company can inflate the cost of raw materials to \$165, and the rest of the cost (\$30), i.e., wage costs plus business operations costs remain the same, so in total the cost to produce the product becomes \$195, and the profit in Malaysia is reduced to \$5. Another way to keep the profit in Taiwan is to put out the order at the price of \$135, which will leave the Malaysian affiliate with a \$5 profit. Because the booking is made 'within a company between different firms', it is easy to control the shift of profits between different places, depending on the tax rate charged by different governments.

In a similar sense, a Taiwan company selling to Taiwan companies in the host country would adopt wholly-owned ownership to control its financial management. An informant says that the transactions incurring credits and debits between *Taishang* in Dongguan (東莞), China, are cleared in Hong Kong instead of in Dongguan. For example, A company sells products to B company, and B gives A a cheque, which will be cleared in Hong Kong.

The rule of '*lailiao jiagong*' (來料加工, import materials to process) imposes a certain tax rate for the company, and then the company is free to sell its products in the domestic market. The tax rate depends on the arbitrary judgement of the officer. After receiving the tax, the government will not charge any business tax. So it is important to tell the government that there is no profit in producing the products so that the government will not tax too much. The company can inflate the cost of imported raw materials, or deflate the selling price to another company. To work out such a system depends on co-

⁵²³ See Statistics Section, MOEA, *Survey on Overseas Investment of the Manufacturing Industry in Taiwan*,

operation between *Taishang*. So the system is like a conglomerate owning different firms, which transfer the products within the company, though in fact they have independent accounting. The transactions between these firms can be cleared overseas so that the profits cannot be checked by the government, and it can be remitted to Taiwan freely without government controls.

A company executive discussed with me a tax difference between Taiwan and Malaysia: that in Taiwan, one has to pay a 0.6% business income tax every year, no matter whether one has profits or not, while in Malaysia, if one does not have any profit, one does not have to pay any tax. So in Taiwan, after paying the 0.6% tax, one can 'enjoy' the rest of one's profits. But in Malaysia, if one never has a profit, one cannot buy goods, or the government would trace where your money derives from. I asked him: if you never show a profit in Malaysia, what can you do with your money? He replied that he will not buy anything there, so it should not be a problem. In other words, he will report no profit in Malaysia, and bring all the profits back to Taiwan via an 'underground way'.

6.3 Capital Sources for Overseas Investment

In Taiwan, as shown in Chapter Three, when one starts a new business, the most common way to raise initial capital is to use one's existing social relations to pull together scattered savings. This kind of capital-raising method is not common for SMEs investing overseas. If these SMEs have not already accumulated enough capital in Taiwan, they are not able to borrow money for this purpose from local financial institutions. In China there are some financial institutions like rotating credit clubs similar to Taiwan's, but most Taiwan businesspeople lack social contacts there, and it is almost impossible for them to collect initial capital like in Taiwan for their new investment.⁵²⁴

Taiwan companies remit cash to the host country to build up a firm; or sell their Taiwan machinery to the newly established firm as a part of the new investment; or grant their company's copyright to the affiliate or transfer technology, and use this as a part of their share. The different ways of capital-raising are shown in Table 6.5.

ROC, 1996, pp.169-170, Table 17-2.

⁵²⁴ See Fan Jinming (范锦明), 'Dalu Minjian Zijin Rongtong Qudao yu Taishang Yinying Celyue' (大陸民間資金融通渠道與台商因應策略, Private Financial Channels in China and the Strategies Taishang can adopt), *Taiwan Liangan Qianzhan Tansuo* (台研兩岸前瞻探索, Explore the Future across Taiwan Strait) (Taipei: Taiwan Research Institute, 台灣綜合研究院), no. 7 (1998), pp. 33-46.

Table 6.5 Capital Sources for Overseas Investment

unit: %

Firm Size by Employees	Cash	Machinery	Supply of Raw Materials, Semi- or Finished Products	Granting Patents or Technical Transfers	Other	Total Number
> 300	93.2	47.9	24.6	10.2	1.7	236
> 100	89.7	57.6	32.6	9.8	0.0	184
< 99	73.9	67.3	45.3	9.2	0.9	892
Year of Overseas Investment						
Before 1986	88.5	63.9	45.9	16.4	0.0	61
1987-91	80.0	62.9	40.3	9.9	1.4	434
1992-94	75.4	64.0	40.5	8.5	0.5	597
After 1995	87.7	56.8	35.0	9.1	1.4	220
Investment by Area						
China	73.9	73.0	45.0	9.2	0.5	849
Hong Kong	92.2	41.2	19.6	3.9	2.0	51
USA	91.7	26.9	27.8	7.4	0.0	108
Malaysia	91.0	47.8	28.4	11.9	0.0	67
Singapore	83.3	22.2	27.8	22.2	0.0	18
Thailand	89.9	40.6	33.3	11.6	4.4	69
Indonesia	92.1	71.1	31.6	7.9	0.0	38
Philippines	81.8	59.1	54.6	9.1	9.1	22
Vietnam	88.9	68.9	33.3	6.7	0.0	45
Average	79.6	62.4	39.8	9.5	0.9	1312

Source: Jingjibu Tongjichu (經濟部統計處, Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duiwai Touzi Shikuang Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業對外投資實況調查報告—八十五年, *Survey on Overseas Investment of the Manufacturing Industry in Taiwan, ROC, 1996*) (Taipei: MOEA, 1997), pp. 79-80, Table 5.

Note: The question is multiple choice, so the sum of the percent is over 100.

Remittance of cash from Taiwan is the most common way to collect capital to establish an overseas company. Table 6.5 (above) shows that the smaller a firm, the less likely is it to remit cash, and the more likely to sell machinery in the host country as part of the new firm's build-up of capital overseas. For those investing in China, 73% of the surveyed firms used machinery as a part of the initial capital for the new venture, which is higher than with any other country. The percent remitting cash to build a new factory in China is only 73.9%, the lowest percent among the countries invested in.

This phenomenon has to do with the political policies and institutions of the host country. If the political structure of the host country is not stable, or corrupt, the investor would like to have returns from his investment as soon as possible, especially for small- and

medium-sized enterprises. An informant said that 'I never think of the problem of who will inherit my property in China. What concerns me is how quick I can make a profit and take back my investment money. The amount of the initial investment should be got back in three years, and the sooner the better'.

One easy way to lower their exposed investment is to sell the used machinery to the host country, or to use it as a part of a joint venture's investment capital. The machinery shipped overseas is usually overvalued so that the Taiwanese sellers could 'earn two hands': the first hand is the real value of the machine, which is counted as a part of their investment capital; and the second hand is the overvalued portion which takes the place of capital in the joint venture, and which ensures a Taiwan SME would not lose a lot of money even if the overseas firm fails to make profits.⁵²⁵ For example, an informant co-invested with a Chinese counterpart in a firm to produce poly-plastic utensils. He owned 40% of the NT\$1.3 million shares, i.e., 0.52 million. But he sold his machines at a value of one million, so he took back 0.48 million from his Chinese partner. In this way, he ensures that he gets back the full value of his machines, and at the same time secures returns in the future from the Chinese market. According to a survey on foreign investment conducted in 1994 by the Chinese government, the price of 'investment in kind' is 20% overvalued.⁵²⁶

To be successful in this kind of deal depends on imperfect local information about the market price for the used machinery and corrupt political structures. In China and Vietnam, the local governments and their public enterprises were the only potential partners with foreign investors to establish joint-venture firms. The generous investment package designed for foreign capital provides the bureaucrats with incentives to work with overseas capital. However, the sale to such joint-ventures of machinery at inflated prices will become transparent in future if the market information flow is freer, and it will be more difficult for *Taishang* to use the same tricks to take back their money.

⁵²⁵ *Ibid.*: p. 30.

⁵²⁶ See Jingjianhui Jingyanchu (經建會經研處, Research Department, Council of Economic Planning), *Dalu Waizi Zhengce zhi Yanbian ji qi dui Taishang de Yingxing* (大陸外資政策之演變及其對台商的影響, *The Evolution of Chinese Foreign Investment Policy and its Influence on Taishang*) (Taipei: Council of Economic Planning, 1997), pp.2-12.

Table 6.6 Markets for Overseas Taiwan Companies

unit : %

Firm Size by Employees	Taiwan	Local Market	Other Area	Total Number
> 300	12.1	43.0	44.9	213
> 100	9.9	46.7	43.4	171
< 99	10.2	43.2	46.7	842
Year of Overseas Investment				
Before 1986	13.3	47.0	39.7	60
1987-91	8.7	40.0	51.3	425
1992-94	9.6	46.1	44.3	576
After 1995	16.9	43.1	40.0	165
Investment by Area				
China	9.9	40.2	49.9	794
Hong Kong	7.6	40.1	52.4	49
USA	9.7	66.9	23.5	103
Malaysia	6.6	45.5	47.9	65
Singapore	5.8	44.9	49.3	17
Thailand	10.2	50.1	39.8	62
Indonesia	18.8	48.7	32.6	32
Philippines	22.3	29.4	48.4	19
Vietnam	27.2	28.5	44.3	42
Average	10.5	43.6	45.9	1226

Source: Jingjibu Tongjichu (經濟部統計處, Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duiwai Touzi Shikuang Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業對外投資實況調查報告—八十五年, *Survey on Overseas Investment of the Manufacturing Industry in Taiwan, ROC, 1996*) (Taipei: MOEA, 1997), pp. 145-146, Table 12-2.

Regarding working capital, a survey done in 1993 shows that 56% of *Taishang* in China obtained their working capital from their Taiwan parent company, 16% of them borrowed money from China's banks, and 11% acquired it from their Chinese counterpart partners.⁵²⁷ In Chapter Three I have argued that borrowing from the banks is a strategy to evade tax. This kind of practice seems not to work in China. The main reason is that these companies are foreigner-owned, and the profits they make in China will be remitted to the parent companies. Since the practice of 'price transfer' mentioned above provides another

⁵²⁷ See Investment Commission, MOEA (經濟部投資審議委員會), *Taishang yu Waishang zai Dalu Touzi Jingyan zhi Diaocha Yanjiu -- yi Zhizaoye Weili* (台商與外商在大陸投資經驗之調查研究—以製造業為例, *A Comparative Study of Foreign Investment in Mainland China, Take the Example of Manufacturing Industry*) (Taipei: Investment Commission, MOEA, 1994), p.175, Table 7-41.

means to transfer profits to the mother country, and at the same time to escape the control of foreign exchange, there is no need to borrow from banks in China. In addition, the corrupt procedures to remit money overseas in China make foreign companies more likely to use the 'price transfer' strategy to be rid of hassles,⁵²⁸ which will reduce the *Taishang's* demand for working capital from banks in China.

Table 6.6 (above) shows the market for the products of overseas Taiwan business. There is no significant difference between different firm sizes for the product outlets. 11% of the firms re-export their products to Taiwan, while 44% of them sell their products in the local market, and 46% sell their products in areas other than Taiwan and the host country. This market distribution seems not to change as time passes. A survey done by the Ministry of Economic Affairs in 1995 asked the firms two questions: where *was* the market for their products when they began to operate their overseas production; where *is* the market for their present products. The difference between the two periods is not significant at all.⁵²⁹

6.4 Markets for Overseas Products

6.4.1 Exports of Overseas Produced Products : the Role of Parent Firms

Table 6.7 shows the marketing channels for overseas production. The Taiwanese parent company plays an important role in selling the products produced overseas, and the smaller the firm, the more important the role it plays. The importance of the parent firm in Taiwan depends on the marketing strategy adopted by the Taiwanese company, and the marketing ability of the host country to the world market.

If the overseas affiliate is only a production base, which is co-ordinated by the parent firm to produce components for other affiliates, or aims at exporting to a third country like the USA, its marketing channel is more likely to be controlled by the parent firm. One interviewed company produces children's books for its American buyer, and it produces semi-finished products in Taiwan, exports these to China, processes them there, and then

⁵²⁸ *Ibid.*: pp. 178-179.

⁵²⁹ In the first year of operation, 12.6% re-exported products to Taiwan, 10.2% sold in the hosting country, and 47% exported to third countries. The figures in 1995 are 11.3%, 40.5% and 48.2% respectively. See Statistics Section, MOEA, *Reports on the Diversification and Internationalisation of Manufacturing Industry*, *Ibid.*: pp. 194, 195, Table B-8, B-9.

re-exports them to the USA. The order is firmly controlled by the parent company in Taiwan, and the overseas affiliate is only a production base. Most of the Taichung umbrella-producing firms moved to China after 1987. They export the parts, assemble the umbrellas in China, and re-export the semi-finished products to Taiwan. Only the last piece of the umbrella is finished in Taiwan. Big firms like ACER, which produces computer motherboards in Subic Bay, the Philippines, and exports these to Taiwan to assemble, relocate production bases in different overseas affiliates to take advantage of different countries' comparative advantage.

Table 6.7 Marketing Channels for Overseas Production

unit: %

Firm Size by Employees	Parent Company in Taiwan	Overseas Affiliate	Other Company in Taiwan	Company in Host Country	Company in a Third Country
> 300	47.9	64.4	3.0	18.6	8.5
> 100	50.5	64.7	5.4	21.7	5.4
< 99	54.8	55.4	13.3	19.3	10.8
Year of Overseas Investment					
Before 1986	50.8	73.8	1.6	19.7	0.0
1987-91	55.3	59.2	9.0	16.1	1.4
1992-94	51.8	54.9	14.1	22.5	0.5
After 1995	52.3	61.4	5.5	18.2	1.4
Investment by Area					
China	59.1	52.4	13.1	17.8	10.0
Hong Kong	43.1	70.6	5.9	19.6	17.7
USA	28.7	80.6	4.6	25.9	6.5
Malaysia	49.3	73.1	4.5	17.9	7.5
Singapore	16.7	72.2	0.0	50.0	22.2
Thailand	43.5	73.9	2.9	23.2	2.9
Indonesia	42.1	63.2	13.2	21.1	7.9
Philippines	63.6	59.1	9.1	9.1	13.6
Vietnam	68.7	40.0	8.9	15.6	4.4
Average	53.0	58.3	10.4	19.5	9.6

Source: Jingjibu Tongjichu (經濟部統計處, Statistics Section, MOEA), *Zhonghuaminguo Taiwan Diqu Zhizaoye Duiwai Touzi Shikuang Diaocha Baogao, Bashiwu Nian* (中華民國台灣地區製造業對外投資實況調查報告—八十五年, *Survey on Overseas Investment of the Manufacturing Industry in Taiwan, ROC, 1996*) (Taipei: MOEA, 1997), pp. 148-149, Table 13.

In less developed countries like China, Vietnam or the Philippines, the parent company in Taiwan plays a key role to channel the products to other overseas markets because of the limited marketing experience of the host country. Research by Egan and Mody shows that a new trend for NIE firms is to source inexpensive footwear in LDCs for US buyers as production costs rise in the home countries, but the buyer-seller links are not changed. Another type of intermediation occurs when the US buyer seeks an equity partnership.⁵³⁰ The NIE firm provides on-site training and other management, while the US side supplies assured orders. This trend is enforced by non-tariff barrier policies implemented by Western countries, e.g., quota restrictions, regulation of origin of production, and countervailing duty taxes.⁵³¹

The established buyer-seller links are not easy to enter for the LDC companies. One interviewed American-Taiwanese importer said that his Christmas gifts are imported from China, which is mainly sourced through Taiwanese companies with which he has co-operated for a long time. A Taiwan partner was producing ceramic products, but moved to China to produce because of rising labour costs and the improved quality of the Chinese ceramic industry. However, the Taiwan partner keeps the core part of the product design and technology innovation in Taiwan, while production is left to the overseas affiliate. In this buyer-seller link, the Taiwan company plays a pivotal role to channel the products from China to the USA, and other LDC companies cannot easily access the link. We noted in Chapter Five that 'price, quality and delivery' are three key elements in doing business. Long-term co-operation with the Taiwan company gives the foreign buyer the minimum guarantee that the co-operating party is reliable in these three respects. One complaint often heard from *Taishang* is that 'a Chinese firm has no idea of quality'. One *Taishang*, who had imported raw material from Taiwan to produce plastic-related products, tried to source the raw material in China to reduce transportation costs. He ordered the raw material from one Chinese enterprise, which was able to provide quality materials and to

⁵³⁰ See Mary Lou Egan and Ashoka Mody, 'Buyer-Seller Links in Export Development', *World Development*, vol.20, No. 3 (1992), p.324.

⁵³¹ See Board of Foreign Trade, MOEA (經濟部國際貿易局), *Woguo Jiaru Shjie Maoyi Zuzhi Cankao Ziliao—Gongyepian 5* (我國加入世界貿易組織參考資料—工業篇(五), *Reference to the Application to Accession to WTO—Industry Sector 5*) (Taipei: Board of Foreign Trade, MOEA, 1996), pp. 11-13. This situation is similar to Japanese SMEs which expanded their overseas investment after the 1980s due to wage rises at home and protectionist measures abroad. See United Nations Conference on Trade and Development, *Small and Medium-sized Transnational Corporations*, (New York: United Nations, 1993), p.56.

deliver on time. However, when the Chinese enterprise could not supply enough raw material for all of its customers, it cut its supply to this *Taishang*. The *Taishang* had to compensate his American buyer.⁵³²

The buyer-seller's link is not static, and a survey finds that more and more exporting channels are taken over by overseas affiliates. 46% of the surveyed firms in 1993 said that their export marketing is controlled by the Taiwan parent firm. This had dropped from 54% in 1992. 42% of the firms in 1993 replied that the export marketing was controlled by the co-invested firm in China, which had increased from 29% in 1992.⁵³³ Table 6.7 also shows the same tendency: the longer the overseas affiliate is established, the more likely is the affiliate to control the marketing channel. When these Asian countries are able to establish business networks abroad, the orders received by Taiwan will be replaced. This is one reason why the Taiwan government insists on the policy of 'Go Slowly Toward China' proposed by President Lee Teng-hui.⁵³⁴

6.4.2 Overseas Produced Products Sold in the Host Country

If the finished products are sold on the domestic market, it is more likely to utilise its overseas affiliates to sell the products locally. 58% of the surveyed firms replied that their products are sold by their overseas affiliates' marketing networks (see Table 6.7).

In Dongguan, most *Taishang* only trade with *Taishang*. One informant said that he only does business with other *Taishang* because he does not trust Chinese companies. 'The cost of doing business with *Taishang* is high, but it is higher to do business with Chinese companies', he said. He sells electronic components to another big *Taishang*, and gets a four-month post-dated cheque. If he sells to a Chinese company, he asks for cash--for he does not trust them.

In Taiwan, a subcontracting system is prevalent, and whenever a company needs to

⁵³² See Mainland Affairs Commission, *Research on the Failed Taiwan Businesspeople in Mainland China*, *op. cit.*, 56-57.

⁵³³ See Investment Commission, MOEA (經濟部投資審議委員會), *Taishang yu Waishang zai Dalu Touzi Jingyan zhi Diaocha Yanjiu -- yi Zhizaoye Weili, di Ernian* (台商與外商在大陸投資經驗之調查研究—以製造業為例(第二年), *A Comparative Study of Foreign Investment in Mainland China—Take the Example of Manufacturing Industry, the Second Year*) (Taipei: Investment Commission, MOEA, 1995), p.159, Table 6-27.

⁵³⁴ See Lin Yujun (林昱君) and Chen Tianzhi (陳添枝), *Taishang dui Dalu touzi zhi Xinqushi yu Jiuweiji* (台商對大陸投資之新趨勢與舊危機, *New Trend and Old Crisis of Taiwan's Investment in Mainland China*) (Taipei: unpublished conference paper, 1997).

buy raw materials or components to assemble, normally it has no difficulty in finding a source. In China, however, the integration of upstream and downstream industries is not yet established, so it is frequently a problem for a *Taishang* to find adequate sources of supply. The situation these *Taishang* face is similar to Japanese investment in Taiwan in the late 1960s and early 1970s. The Japanese investors complained that there was no integrated industrial structure to supply all the necessary parts for assembly in the late 1960s and early 1970s.⁵³⁵ SMEs from Taiwan in China have the same complaint. Because there is no established subcontracting system in China, and no reliable delivery and quality, it reinforces the co-operation between *Taishang* in the same region, such as Shenzhen or Dongguan, to form a tight co-operative industrial structure. Another way to resolve this problem of sourcing input materials or processing semi-finished goods is to expand the firm size and to include all of the different parts of the work in the same factory, whereas in Taiwan it would be finished by many single-task factories. For example, one informant noted that connecting electrical cable for manufacturing is normally done by a different firm in Taiwan, but in China, the *Taishang* employs skilled labourers in the factory to do the work. The main reason is that labour costs are very cheap in China compared to the putting-out charge of other companies. 'A firm employing fifty workers in Taiwan can employ five hundred workers in China because of low wages, so more of what the firm needs is produced in the factory rather than purchased from other companies.'

The impact of the close co-operation between *Taishang* overseas is that many upstream firms of a certain industry close their factories in Taiwan and move overseas to produce. A core firm established in one overseas place will inevitably pull many satellite firms to go overseas with it. If a satellite firm goes overseas to invest with its core firm, its products produced overseas are sold to its core firm there. As Table 6.2 shows, one out of four firms went overseas with their Taiwan buyer, i.e., the core firm, after 1995. One informant producing electronic components said that his company will go to China if his core firm decides to set up a new firm there. Another one producing screws explained the rationality of Lee Teng-hui's 'Go Slowly' policy. He said that Chunyu (春雨) Steel company is the core firm in the production system. It produces machines to sell to satellite firms to produce screws to meet its order from overseas. The government policy at the

⁵³⁵ See Chapter Four.

moment is to forbid investments worth over NT\$50 million (about US\$1.7 million) to invest in China. If Chunyu decides to invest in China, which is highly possible, all of the satellite firms will go to establish firms with Chunyu. This will inevitably reduce Taiwan's domestic production, and employment there. He believes that the trend is irreversible, and he notes that in the near future China will be able to establish its own integrated production system just like Taiwan's.

6.4.3 *Guanxi* and Channels

Table 6.6 shows that 44% of the firms sell their overseas products in the host countries. Many companies, as noted earlier, establish joint ventures with local companies to sell those products. This has two advantages: firstly, it matches the regulations set by the host country to encourage national industrial development; secondly, it can utilise the local social system to promote its sales in the host country. For example, an informant has a joint venture with a Chinese partner to produce polythene utensils in Guizhou. He has a 40% stake in the company, and 60% of the products can be sold in the domestic market. The marketing problem is left to his Chinese counterpart, for he has no idea of the domestic market. According to a survey done in 1993, three out of four firms left their marketing activities to be managed by the joint venture company instead of by the Taiwan parent firm.⁵³⁶

For example, there are two channels in the Chinese food market to reach consumers: a multi-layer wholesale channel, including an exclusive wholesale agency (總經銷) and other smaller wholesalers (二批、三批), and a retailing system, including department stores, supermarkets and individual shops.⁵³⁷ *Taishang* have to co-operate with Chinese businesspeople to establish their own channels to compete with the existing channels, mainly controlled by Chinese public enterprises. The *Taishang* did not know about the marketing channel very well when they entered the market, and had to resort to local people's help, mainly high ranking persons in the public enterprises who are familiar with

⁵³⁶ See Investment Commission, MOEA, *A Comparative Study of Foreign Investment in Mainland China—Take the Example of Manufacturing Industry, the Second Year (1995)*, p.156, Table 6-25.

⁵³⁷ See Zhang Huiwen (張慧文), 'Dalu Taishang Xingxiao Moshi zhi Yanjiu' (大陸台商行銷模式之研究, Research on *Taishang*'s Marketing Patterns in Mainland China), *Taiyan Liangan Qianzhan Tansuo* (台研兩岸前瞻探索, *Explore the Future across the Taiwan Strait*) (Taipei: Taiwan Research Institute, 台灣綜合研究院), no. 7 (1998), p. 58.

the traditional channels, wholesalers and retailers.⁵³⁸ Another way to have a share in the China market is to grant certain rights to a local company which is familiar with the local market. One publishing company grants its copyright to different companies in different provinces, and they collect cash from the royalty the Chinese firms pay. Many of these companies are in the so-called 'track two' marketing channel (第二渠道), which is different from the traditional channel controlled by public publishing companies like Xinhua (新華) or Sanlian (三聯).

We often hear that *guanxi* is so important in Chinese society that one is not able to sell products without *guanxi*. From my interviews, this claim is quite true. One informant said that China is like the Taiwan government in the 1960s, and the way he deals with Chinese officials is the same as how he dealt with the Nationalist government: to bribe the key local bureaucracy in charge of the Taiwan compatriot's investment. However, I would argue that it is the institutional structures which enable some persons to exploit the system so that *guanxi* becomes dominant in social life, and not that cultural factors dominate people's behaviour.

Information circulation is strictly controlled in China. Since the Communist Party controls this in local areas, party officials are often the persons with whom *Taishang* want to co-operate. 'There are piles of regulations on foreign investment, but no one really knows what the policy is', one informant complained. Because the right to interpret legal codes is held by the Party officials and the bureaucrats, to keep a good relationship with them becomes necessary. He said that his partner is a local official, and through his interpretation of the legal codes, the required export quota, 40% of his products, has been removed, and all of his products can be sold in the domestic market.

Research done by Zhang Huiwen (張慧文) shows that the five most successful Taiwanese food companies in China all established their good connections with local politicians⁵³⁹. Interviewees who invested in China argued in favour of the same strategies. One informant invested in China with the help of his cousin to set up a firm in his cousin's local county in Guangdong. The cousin is the head (廠長) of a public enterprise, who has good *guanxi* with the local party secretary (書記). There was a large mound at the site

⁵³⁸ *Ibid.*: p. 60.

where he planned to build the factory, and it would have cost him a lot of money to level it. He bribed the secretary, and the secretary then ordered the villagers to remove the mound without paying any money.

Another case is that of a Chinese partner whose brother is vice party secretary of a city. The Chinese partner has a one-third stake in the company. The land belongs to the local government, but is used by the cadres to make profits for themselves. The informant is happy to work with them, for he does not have to worry about finding land to build his factory, and nor have to worry about harassment from the local bureaucracy, mainly from the Taxation Office, Public Security or the Party. Any hassles are left to his Chinese partner to deal with. Both parties benefit from the co-operation.

Guanxi is so important in China that everyone has to 'buy' it in terms of pecuniary calculations. For example, an informant paid the local secretary to find some construction companies to build a factory. The newly built factory will be able to pass the regulations even it is not fully equipped. The *Taishang* saves a lot of money; and 'The party secretary is very rich. If China's anti-corruption policy is implemented strictly there, he will be sentenced to death'. It is the institutional structure which enables him to exploit this *guanxi* to make money. No power counterbalances the local politicians in China, and they are utilising the economic reform opportunities to pursue their own interests.

Because there are no predictable rules for doing business in China, *guanxi* becomes epidemic. Because *guanxi* is dynamic, no-one can guarantee that the long-term relationship will last. If one side is not honest in this mutual *guanxi*, it is easy to go broke. One informant's friend had a joint venture in China. In the beginning, the company ran very well, and made money. Then the Chinese partners asked to expand the scale of production to meet market demand. The Taiwan partner was reluctant to do so, for he wanted to take back his initial investment as soon as possible. He nonetheless felt under pressure to put money into the new expansion. But the Chinese partners kept on demanding that he increase the capital, and in the end the Taiwanese side was unable to meet the requests, found himself shunted aside in terms of any returns from his investment, and finally abandoned all his shares in the company.

Another *Taishang* had a joint venture in China to produce sports shoes. There were

⁵³⁹ See Zhang Huiwen · Research on *Taishang*'s Marketing Patterns in Mainland China (1998), pp. 60-61.

a lot of problems from the beginning, e.g., loose quality control, and no professionals to manage the newly established factory. After he surmounted the problems the company began to generate profits, and two production lines were fully utilised to meet the increasing orders. When the supply was not enough to meet the demand, he planned to set up another new wholly-owned factory to avoid the problems he had faced before. However, when the Chinese partners knew of this plan, they thought their interests were infringed, and started to boycott him. The export license was normally handled by the Chinese partners, and they started to slow down the export application processing. The orders for raw materials were made by the Chinese partners, and they began to restrict the supply of raw materials so that the company was not able to deliver the products in time.⁵⁴⁰ From the perspective of the Chinese side, this *Taishang*'s behaviour had been 'dishonest', for he did not put the company's interest over his own. From the *Taishang*'s perspective, the bad experience of the past has made him hesitate to enter into a joint venture again.

The utilisation of *guanxi* in China will be transformed in the near future, especially when China gains admission to the World Trade Organisation. Some scholars would argue that embeddedness is important for business practices, but in the face of a more open market power, particularistic rules will be less important. The studies of Zhang Huiwen show that increasing numbers of *Taishang* are adopting a strategy to reach customers that less and less relies on traditional *guanxi* practices to sell products.⁵⁴¹ Price and quality competition is a common way to win a market share, but in the Chinese domestic market, throat-cut price competition is not a good strategy for *Taishang* to compete with long-established Chinese products. They often instead need to set a higher price to put their products in the 'high quality' level. The market in China is so big that every company can target a segmented market, and the high-price domain is a good path to cut into the market in a way that distinguishes *Taishang* products from Chinese. The successful Dingxin (頂新) business group and the President (統一) business group have adopted this strategy, and skilfully avoid overlapping the same price range as local Chinese food manufacturing companies. With modern marketing skills, the new entrants can win market share in the competition without totally resorting to traditional *guanxi*.

⁵⁴⁰ See Mainland Affairs Commission, *Research on the Failed Taiwan Businesspeople in Mainland China* (1992), pp. 19-21.

⁵⁴¹ See Zhang Huiwen, *Research on Taishang's Marketing Patterns in Mainland China* (1998).

6.5 Human Resources Management

As noted, rising labour costs in Taiwan provide a major reason why SMEs move production lines overseas. In 1993 when I interviewed businesspeople, they all complained about the labour shortages and the difficulties in managing workers. One informant said that 'nowadays it is the workers' day. However, when economic recession comes, it will again be our days.' They do not have to wait until a recession year in China and Southeast Asia. They already have the upper hand in dictating to workers there.

6.5.1 Labour Sources

China and the Southeast Asian countries, except for Malaysia, are relatively labour abundant, so it is no problem for them to recruit low-skilled workers locally. As one interviewee investing in China said: whenever I put a red paper on the billboard, hundreds of people come to ask for the job.

According to a survey by the Investment Commission, more than half of the *Taishang* recruit a labour force publicly, while more than 35% of the labour force are introduced by Chinese partners, and about 14% are introduced by the company's employees.⁵⁴²

Most managers are from Taiwan. They have difficulty in recruiting skilled labourers from the local area. One informant said that it is easy to find a worker with an elementary school education, but very difficult to get a worker with a senior high school background. He said that most university graduates go to Shenzhen, and in Dongguan it is not at all easy to employ skilled labourers even if you offer a higher wage. One reason is that the units (*danwei*, 單位) with skilled workers do not release the workers.⁵⁴³ In Southeast Asia, as noted, the graduates who attended school in Taiwan have become the most popular group for *Taishang* to turn to in order to resolve management and language problems. In China, a *Taishang* tries to train skilled labour using local senior workers, or dispatches Taiwanese managers to serve as instructors. However, more than 40% of the surveyed *Taishang* complained that they spent a lot of money to give training, and then the trainees leave to

⁵⁴² See Investment Commission, MOEA (1995) 'A Comparative Study of Foreign Investment in Mainland China: The Example of Manufacturing Industry (Second Year), *op. cit.*, p. 161.

⁵⁴³ *Ibid.*: p. 165.

find another better job.⁵⁴⁴

Besides the capable workers and managers, *Taishang* have to take in some 'unproductive' workers or managers because of *renqing* pressures in the local society. I will leave this issue to section 6.5.3.

6.5.2 Authoritarian Management Style

In this region of a labour surplus, management becomes more authoritarian, if not dictatorial. It is often heard that foreigner-owned factories abuse workers, especially in the factories owned by firms from Korea, Hong Kong and Taiwan. In 1995, a fire killed more than hundred workers in Thailand because the Hong Kong company had locked the exit doors to prevent the workers from slipping out of the factory during work.

Militarised management is not rare. Anita Chan found that some Taiwanese and Korean owners have a kind of authoritarian management pattern 'reminiscent of the 19th-century Industrial Revolution.'⁵⁴⁵ In a *Taishang* factory, a huge sign that hangs over an elevated walkway reads: loitering underneath, Y100 penalty.⁵⁴⁶

One informant, who had owned a shoe-making company in Taichung, moved his production line to Shenzhen. He told me with pride that they organised the company like a military unit. All of the workers are organised into a 'squad' (班), several squads compose a platoon (排), and three platoons are organised into a company (連). All workers are required to be accommodated in a dormitory established by the company, which is similar to a military camp. In the morning, all the workers get up at six o'clock. Breakfast ins from 6:30 to 7:00. After breakfast, they have to listen to a speech from managers. They work from eight to five, with an hour break for lunch. After work, most of the workers do overtime work, normally from six to ten o'clock. The workers are mostly from other provinces. They want to make more money, and have nowhere to go, so they are willing to work overtime. If not, they still have to stay in the dorm. When they want to leave the factory camp, they have to get permission from the senior manager. Another interviewee said that they require workers to work nine hours a day, six days a week, though the legal working days are five days a week. One owner with a shoe factory in China jested that 'we

⁵⁴⁴ *Ibid.*: p. 170.

⁵⁴⁵ See Anita Chan, 'The Emerging Patterns of Industrial Relations in China and the Rise of Two New Labor Movements', *China Information*, vol. 9, no. 4 (Spring 1995), p.48.

have already recovered Mainland China (反攻大陸), for every Chinese worker has to sing Taiwan's military song every day'.⁵⁴⁷

This kind of management style cannot be said to be 'paternalistic' in any way. The manner of management used by *Taishang* overseas illustrates again what is argued in Chapter Five, that when self-interest is at stake, the 'generous' side of paternalism gives way to self-interest. The workers in the *Taishangs'* factories are not family members, nor relatives, nor compatriots, so there is no incentive to be generous or paternalistic. A profit-oriented capitalist logic prevails.

6.5.3 Effective Management and Unproductive *Guanxi*

In the overseas affiliates, the Taiwanese businesspeople do not have the problem of employing relatives, for they have to hire a local labour force. So they are able to avoid the conflict between hiring inefficient relatives and pursuing higher profits. However, they sometimes face instead the problem of hiring redundant workers who are not economically productive but who have politically important relatives. In China, as one informant complained, even though his company is wholly-owned the local government also assigns an 'official representative in the firm' (駐廠代表), which is a waste of money for the company. Wherever he goes, the representative follows him, which makes him feel like he is under surveillance.

So far the representative has not intervened, but if there are many managers from the Chinese counterpart in a joint venture, or if political activities are assigned by the Communist Party, it will cause efficiency problems. The Party regulates that a firm employing more than three hundred workers has to organise a party branch, and the workers have to take part in all assigned political activities. This kind of political regulation causes a lot of trouble for labour management through interruptions of normal production.⁵⁴⁸

More often than not, the Chinese cadres assigned to high-ranking positions in the

⁵⁴⁶ *Ibid.*: p. 49.

⁵⁴⁷ This song is 'Jiutiao Haohan zai Yiban' (九條好漢在一班, A *squad* of nine good guys), which has no anti-communism text.

⁵⁴⁸ See Wei Lizhi (魏立志), 'Cong Zhonggong Qiye Guanli Tizhi tan Fudalu Touzi Taishang Gongchang zhi Guanli' (從中共企業管理體制談赴大陸投資台商工廠之管理, *Taishang's Management in*

firm do nothing. One *Taishang* with a joint venture in China complained, for example, that Chinese cadres were paid a lot of money but have no function in the factory at all. What is worse, according to interviewees, in factories where they did have functions they did not take responsibility for the tasks to which they were assigned, which caused interruption of the production lines. They did not supervise the Chinese workers, and when a machine broke or there were quality defects, they did not pay any attention. The *Taishang* have had to negotiate with their Chinese counterpart to hire more Taiwanese managers to replace such Chinese cadres.⁵⁴⁹

If *Taishang* have to employ Chinese cadres to tackle unexpected problems, they prefer sometimes to pay them periodically in the name of 'consultants' (Guwen, 顧問). As consultants, they do not have to come to the company every day. Or they pay these cadres every time that a case is resolved with their help. This kind of *guanxi*-utilisation is flexible, based on pecuniary calculations.⁵⁵⁰ When a *Taishang* refuses to accept those workers recommended by Chinese cadres, one common trick used by the *Taishang* is to 'open the position', and ask for high qualifications, e.g., to ask if the employee is able to speak English. *Taishangs* use such tactics to prevent local Chinese officials from putting their own relatives into the factory.⁵⁵¹

Another way to evade this dilemma is to endure the situation in the short term, and to try to earn back their investment as soon as possible. *Taishangs* running small and medium-sized enterprises have no intention to stay overseas for good, and their investment plan is always short-term. One informant said that he never thinks of what will happen after five years. One reason for this kind of thinking is market competition from local firms. An interviewee explained why he wants to take back all his investment capital in two to three years: 'The Mainlanders are very clever. They're able to make any kind of machine, if they get the opportunity to have a look at the machines. They are able to copy our machines and produce similar products to compete with us. So in the long run, we will not be able to win

China—Perspective from the Communist China's Enterprise Institutions), *Xiangjiao Gongye* (橡膠工業 · Rubber Industry) (Taipei), vol.17 (October, 1993), no.10, p.5

⁵⁴⁹ See Mainland Affairs Commission, *Research on the Failed Taiwan Businesspeople in Mainland China* (1992), p. 20.

⁵⁵⁰ See Wei Lizhi, *Taishang's Management in China—Perspective from the Communist China's Enterprise Institutions* (1993), p.5.

out in the same product market. I have to grasp my market niche, and make my money as soon as possible before the Mainlanders come into competition with us.'

This kind of short-term investment strategy, plus the newly emerged labour shortage problem in Malaysia, enticed many *Taishang* to move again to another locale with cheaper labour. In Malaysia, as an alternative many *Taishang* have hired guest labour from Indonesia and Bangladesh, whom they pay less than Malays. However, more often they move the production lines to other countries to find cheaper labour. The head of the Malaysia *Taishang* Club, which consists of three hundred and thirty members, said that about twenty to thirty percent of the *Taishang* have left Malaysia. The Malaysian Minister of Human Resources complained that thirty-one Taiwan firms closed their factories and owed workers back pay.⁵⁵² In contrast, China and Vietnam have been able to offer cheap labour to the *Taishang* on good terms, and there is no sign showing that the investment in China is decelerating.

6.6 The Asian Financial Crisis and *Taishang*

The Asian financial crisis that started in May 1997 in Thailand and swiftly spread to Malaysia, Indonesia and Korea, has had an impact on *Taishang* whose products are sold in the host countries and export. According to their product outlets and raw material sources, we can distinguish four groups: those that utilise local raw materials and produce for export; those that import raw materials and export their products; those that utilise local raw materials and sell in the domestic market; and those that import raw materials and sell in the domestic market.

The first group benefits the most from this crisis. The kind of 'price transfer' business practice that was earlier mentioned provides a way to ward off the impact of the financial crisis coursing through Southeast Asia. One *Taishang* said that his company profited 100% during the crisis period. It exports computer components all over the world, and the

⁵⁵¹ See Ding Zhida (丁志達), '*Taishang zai Dalu Qiye Laodong Renshi Guanli de Fangfa*' (台商在大陸企業勞動人事管理的方法, *Taishang's Human Resources Management in China*), *Zhonghua Zhanlyue Xuekan* (中華戰略學刊, *Journal of Chinese Tactics*) (Taipei, Sep. 1996), p.207.

⁵⁵² See Gong Yijun, *Cross-Border Investment and Linkages with Taiwan: Some Observations on Taishang in Malaysia*, p. 12.

export price is quoted in US dollars.⁵⁵³ The second category of firms also make money, though less than the first group.

The financial turmoil has had an adverse impact on those *Taishang* who produce for the local market. If they buy raw materials in the host country, and sell in the domestic market, normally they have to pay for the raw materials in cash, but get a post-dated cheque after the sale. During the crisis, the bouncing of cheques is so frequent that they report great difficulties in doing business. If the *Taishang* imports raw materials, and sells in the domestic market, it will face currency exchange losses and defaults.⁵⁵⁴ Table 6.6 shows that about half of the *Taishang* sell their products in local markets in Malaysia, Indonesia and Thailand, the three countries most adversely affected by the financial crisis. Their situation could be said to be precarious.

The dramatic devaluation of the local currencies caused many East Asian countries to reform their financial institutions. For example, the Thai government has closed fifty-eight financial companies, and fifty-six companies were sold by the government's Asset Management Corporation in February 1998. If the *Taishang* borrowed money from these banks, they will have problems in finding other capital sources. Even if they borrow money from the 'good' banks, the high interest rate makes the loan overly expensive. In a trip to Southeast Asia organised by the Council for Economic Planning and Development in January 1998 to understand the difficulties faced by local *Taishang*, most of the complaints heard involved the problems of acquiring working capital from local banks.⁵⁵⁵ Taiwan's Central Bank has deposited US\$20 million in every overseas Taiwan bank to support more loans to *Taishang*, and the Ministry of Finance also has tripled to US\$100 million (NT\$3 billion) the capital of the 'Overseas Chinese Credit Foundation', which was set up to help overseas Chinese to borrow money from local banks overseas.⁵⁵⁶ The effect of these policies is not yet known, but if economic growth is negative in the region, e.g., if the

⁵⁵³ See Liberty Times (自由時報), *Dongnanya Taishang Lizhengshangyou Zhanxian Renxing* (東南亞台商力爭上游展現韌性, *Taishang in Southeast Asia Strives to Work Better, Showing Their Strength*), 2 Feb. 1998, p. 15.

⁵⁵⁴ See Board of Foreign Trade, *Taiguo Jingmao Qingshi ji Jinrong Weiji zhi Fenxi* (泰國經貿情勢及金融危機之分析, *Analysis of Economic, Trade and Financial Crisis in Thailand*) (Taipei: unpublished paper, 1998), p. 12.

⁵⁵⁵ Council for Economic Planning and Development, *Dongnanya Touzi Maoyi Kaochatuan Kaocha Baogao* (東南亞投資貿易考察團考察報告, *Report on the Visit to Southeast Asia*) (Taipei: Council for Economic Planning and Development, unpublished paper, 26 Jan. 1998), p. 9.

⁵⁵⁶ *Ibid.*: p. 10.

economic growth rate in Thailand is -3.5%, Indonesia 0%, Malaysia 2.5%,⁵⁵⁷ these *Taishang* will have difficulty selling their products in the host countries, a problem of markets rather than working capital.

6.7 Conclusion

In the era of globalisation, Taiwan's SMEs follow the capitalist logic and relocate their production, mainly within East Asia. Domestic factors such as labour shortages, the abrupt appreciation of the Taiwan dollar, and more restrictive environmental regulations, plus inducements such as overseas governments' preferential investment policies and low labour costs, explain the new ventures overseas.

As in Taiwan in the 1960s, to find 'influential partners' abroad is indispensable if one needs to secure approvals from overseas officials. These 'influential' partners include retired bureaucrats, leaders of the local Chinese community, local businesspeople, or, in China and Vietnam, local governments. But not every partner is co-operative and reliable. Conflicts often arise and relationships break down.

It is more to find joint ventures overseas so as to exploit the host country's investment laws. As in Taiwan, tax evasion is also common among the *Taishang*. However, the way taxes are evaded is different than in Taiwan. More methods are available, with 'price transfers' the main strategy.

The original buyer-seller's link between the *Taishang* and overseas buyers remains unchanged except that the products are no longer produced in Taiwan. The Western buyers are still used to putting in orders to *Taishang* to source their goods. Unless the host countries can develop their own competitive industry, the marketing channels in these countries are still controlled by foreigners. Accompanying the localisation of the *Taishang* in the host countries, the overseas affiliates play a more and more important role in marketing. The build-up of an integrated industrial structure overseas makes overseas *Taishang* transactions with local *Taishang* more frequent, which will reinforce the connections between them, but at the same time also raises the productive skills of the host countries.

Overseas management of labour is different than in Taiwan because the *Taishang* are

⁵⁵⁷ *Ibid.*: p. 17, Table 2.

not socially embedded in the foreign milieu. Their management of labour is more authoritarian. The local managers employed by the overseas affiliates are not necessarily efficient in management, and the firm faces the *renqing* dilemma of Chinese officials trying to implant relatives in the company. As observed, some *Taishang* have found ways to prevent this difficulty by demanding high qualifications for the positions or by paying them as consultants on a 'piece wage' instead of a monthly wage. Overall, the Taiwan SMEs in China endure short-term frustrations in order to make a quick return rather than invest for the long term.

Chapter 7: Conclusions

7.1 Summary of Findings

This thesis discusses the life histories, mobility strategies, and business practices of small and medium-sized businesspeople, set specifically within Taiwan's history of the past fifty years.

Chapter One discussed the genesis of the modern-day small businesspeople, starting with the immediate aftermath of World War II and the retreat of the Kuomintang from the Mainland in the late 1940s.

The class structure in the 1950s was a result of market and political forces, which created an 'ethnicised class structure'. The Mainlanders were placed in the public sector. In an age of high unemployment, to obtain a job in the public sector meant that one's livelihood was guaranteed. At that time life chances were not only determined by one's market situation, but also by the intervening political forces.

Set in this class structure, who was more likely to become a proprietor, i.e., what was the picture of economic mobility after the 1950s? I have explored different factors which might affect the possibility of mobility. Education as a kind of human capital was the most important factor in occupational achievement. But it was an individual factor embedded in a social formation. In Taiwan, the occupational distribution was largely determined by education, and we find that the education system in Taiwan functions mainly as a mechanism to reproduce social-status inequality. The government strictly controlled the expansion of education based on economic planning. The ratio of students in academic and vocational high schools reversed from 7:3 to 3:7 in twenty years. Children from a better socio-economic background had a better chance to go to the academic schools and later on to university. The Mainlanders were better educated than Taiwanese in the past half century, because of their parents' higher education, good occupations and the state's subsidies.

Chapter Two has sought to explain why people from different educational levels have had different mobility paths. The general mobility pattern in Taiwan is for the less educated to endeavour to get a job in the labour market, and when possible later on, to be

self-employed; while for the higher educated, the strategy was to get a prestige salaried job. Because Mainlanders were more highly educated on average than Taiwanese, they were less likely to be self-employed. The ethnic cleavage in occupational distribution is basically the result of educational effects, as I have demonstrated through my statistical analysis of the raw data of the 1992 Taiwan's Social Chang Survey. As the educational gap narrows, the ethnic cleavage in occupations disappears.

The prevalence of small and medium-sized enterprises in Taiwan is induced by the history of occupational constraints. Different educational levels set the general limitation to upward mobility, and for the less educated one of the means they can use to overcome this limitation is to withdraw his/her labour power from the wage market.

We are interested in why these less educated, often manual labourers adopt a so-called 'de-class-in-itself' strategy instead of trying improve their market situation collectively? Three structural factors have constrained the possibility of collective actions of a 'class for itself' nature: education within Taiwan as a kind of ideological control; the party-state controlled labour regime, and social network controls. Education legitimised the ideology that the higher one is educated, the more one deserved a good job in government and in other large organisations. People without high educational credentials have had to find alternative mechanisms to be upwardly mobile. They could not organise to protect their collective interests because the Nationalists controlled every kind of social activities to prevent anyone who might destabilise their rule. A more subtle control mechanism, at a lower level, involved social network controls, which employ traditional ways to keep people in line. To get a job in Taiwan, one is usually introduced by an acquaintance, which makes it harder to unite in any collective way. The proprietor can mobilise one's social network to demobilise one's collective action.

Set in the context of Taiwan's political regime and the international economy, I examined business practices in Taiwan. Contrary to the arguments of many scholars who believe the Chinese way of running a business is unique, I tried to explain the historical-social structures behind these practices, and to 'de-mythologise' 'orientalist' discourses regarding Taiwan's business community. The following four chapters were devoted to discussions of a small- and medium-sized enterprise's internal management, including financial, marketing, human resources management, and the new overseas investment

ventures.

In Chapter Three, I have described Taiwan's financial system. I found that the working capital sources of SMEs derived from internal retained earnings, and external trade credit, household sector and other enterprises. The legal system affects business practices which induces SMEs prefer to use trade credit as financial leverage. One reason why SMEs borrow a lot of money from other enterprise and households is to evade tax. Since the share of loans to SMEs is equivalent to their shares of sales, and the percentage of total capital sources from financial institutions in total liabilities is almost the same as big firms, and since a lot of private borrowing by SMEs comprises 'deposits received from shareholders' who want to earn higher interest and evade tax, the usually claimed hypothesis that such SMEs lack working capital and therefore have to resort to the private market should be put in doubt.

Taiwan's financial market is a mixed product of historical development, political control and market mechanisms. The KMT confiscated Japanese banks after the Second World War and made them a means to maintain political and economic control. The government also co-operated with local factions and granted them the privilege to run local financial institutions. This kind of financial control reinforces the use of *guanxi* to get loans from the financial institutions, which gives local political figures a prominent role in mediating between borrowers and lenders.

Under these structural constraints, I have argued that, firstly, to distinguish the two stages of the SMEs' development clarifies whether the SMEs need capital urgently. An SME normally needs help only in its initial stage, contrary to most scholars' argument that established SMEs need financial help from the government. I also found that the most common way to collect enough capital to initiate a business is to use one's social relations. Co-operating with friends or relatives to form a partnership enterprise is a common means to start up a new business. Funding is secured from family members, relatives, rotating credit associations and dowries. However, partnerships usually do not last very long, unless strongly led by the dominant member of a family. This type of business is often initiated by *personal guanxi*, but ends in *conflict* between differing interests.

Often, SMEs that have already been established want to borrow more money from financial institutions so that they can evade tax, which has nothing to do with lack of working capital. The government has implemented policies to supply more funds to SMEs, but the SMEs exploit the system to maximise their self-interest.

In Chapter Four, I discuss the marketing strategies adopted by Taiwan's SMEs. The minimum requirements to sell a product is to meet quality specifications at a competitive price and to adhere to reliable delivery standards. There will be no co-operation or long-term relationship if these requirements are not satisfied. However, these are only minimum requirements. There are barriers to market entry that make it hard for those outsiders to enter a market. I have noted the close co-operation between big firms and the government in the 1950s, which resulted in a segregated market: big firms specialised in the domestic market, while SMEs sold their products overseas. In the late 1980s, the pressures from the United States forced the government to open the domestic market, and indirectly pushed the big firms to sell more overseas. Accompanying the rise of East Asian economic power, Taiwan's original export markets for SMEs, the USA and Japan, have been gradually replaced by China and ASEAN.

I have also argued that the prevalent utilisation of *guanxi* results from specific social milieux, and is not an innate cultural trait of Chinese businesspeople. The goal of pulling *guanxi* is to make profits for the businesspeople. *Guanxi* is dynamic, based on mutual interests. I agree with Polanyi's analysis and argue that Taiwan's economy 'is directed by market prices and nothing but market prices, where human beings behave in such a way as to achieve maximum money gains'. The social closures and long-term relationships can disintegrate due to differences of interest.

I also probed the role of businesspeople in Taiwan's democratisation process: when there was an interest for them to maintain the system, they collaborated with the ruling party; when there are conflicts of interests, they would break the rules without hesitation, as with the government's 'Go Slow Toward China' policy, which is often challenged by the business community. A businessperson exploits his *guanxi* to make profits, and he or she is sometimes unconsciously tests and chips away at the existing social order.

All transactions must be based on mutual trust to a certain degree, and this kind of

trust is underpinned by law, or social pressure, or private violence. In Taiwan, traditional social pressure provided security in transactions, but it does not necessarily work in modern times.

In Chapter Five, I explained how traditional values operate in Taiwan's family enterprises. One of the values is the patriarchal organisation of a family firm, where females are less well paid and placed in less important posts. Another example is how *guanxi* (connections) is utilised by people to find their jobs. A small enterprise is more likely to hire workers through *guanxi* than a big firm, which more frequently recruits workers in impersonal ways. However, the long-term data reveals that the relative importance of getting a job through *guanxi* is declining in line with social structural change.

Because more workers are hired through *guanxi* in SMEs, the labour-capital relationships there are more often based on personal relationships than in big firms, and it is easier to demobilise workers by using group pressure in SMEs. However, the tension between employers and workers still exists, and one way to avoid direct confrontation is to leave the working place. This explains why the turnover rate in Taiwan's labour market is so high, which is often praised by Taiwan's economists as 'flexible'.

In SMEs, family members often compose an inner circle, and control the managerial positions. One of their functions is to evade tax and to prevent any revelations of tax evasion practices. Though traditional filial values help to tie together the different interests among family members, the market principle and differences in self-interest normally eventually disintegrate the cohesion. A typical problem in a family enterprise is that incompetent family members hold responsible positions. This runs the risk of the enterprise being managed. But when the firm dismisses the incompetent family member, it runs into the problem of family discord.

Fen-jia is one resolution to the dilemma facing families. Three types of *fen-jia* have been distinguished. One of these will inevitably result in the fragmentation of a family firm, which is often cited as the reason why Chinese enterprises are small. However, a more common type of *fen-jia* today in Taiwanese society is that the father sets up more than one small firm, and distributes them equally to different sons. Alternatively, since more occupations are available to the younger generation accompanying Taiwan's economic

development, not all of one's sons need rely on the family firm. In some cases, only one son inherits the property while others accept monetary compensation. When a father entrepreneur diversifies his investment and sets up firms for more than one son, there will be the possibility forming a business group. In other words, the cultural constraint of *fen-jia* generates a unique type of economic organisation--the existence of numerous SMEs and business groups at the same time.

In Chapter Six I discussed the overseas activities of Taiwanese businesspeople after the mid-1980s, when domestic factors such as labour shortages, the abrupt appreciation of the Taiwan dollar, and more restrictive environmental regulations pushed them to look outward, accompanying the international trend toward globalisation. My main concern in this chapter is to compare the business practices of businesspeople at home and abroad.

Taishang easily transplanted overseas their past experience in Taiwan. To find 'influential partners' in Taiwan in the 1960s, including retired bureaucrats, leaders of the local Chinese community, or local businesspeople, was sometimes indispensable if one needed to secure approvals from local politicians. However, we should not view this kind of *guanxi* as permanent, for not every partner is co-operative and reliable. When there is internal conflict, the relationship will break down.

Compared to the common form of wholly-owned SMEs in Taiwan, once successfully established, it is more common to find joint ventures overseas, for joint ventures can benefit from the host country's investment laws. As in Taiwan, tax evasion is also common among the *Taishang*. There are more methods available, with 'price transfer' the main strategy.

The original buyer-seller's link between *Taishang* and overseas buyers remains unchanged except that the products are no longer produced in Taiwan. Unless the host countries can develop their own competitive industry, the marketing channels in these countries are still controlled by foreigners. The Western buyers are still used to putting orders to *Taishang* to source their goods. The overseas affiliates play a more and more important role in marketing accompanying the localisation of the *Taishang* in the host countries. Too, the build-up of an integrated industrial structure overseas makes overseas *Taishang* transactions with local *Taishang* more frequent, which will strengthen the connections between them, and also raise the productive skills of the host countries.

Because the *Taishang* are not socially embedded in the foreign milieu, overseas management of labour is different from Taiwan's. Their management of workers is more authoritarian.

7.2 Theoretical Reconsiderations

In this section, I will elaborate the Polanyian approach that I have used in my thesis, then discuss the three main theories on Taiwan's economic development: i.e., neo-classical economics, the 'governed' market, and the Chinese cultural approach.⁵⁵⁸

Karl Polanyi wrote that the establishment of a self-regulating market economy needs violent intervention by the government: i.e., *laissez faire* is the result of artificial government interventions, and the limitations on *laissez faire* emerged naturally.⁵⁵⁹ Polanyi's reasoning is that order and law are indispensable for the establishment of a market economy. Without the enforcement of law securing the safety of transactions, the 'freedom of contract' as the basic tenet of civil codes would not be able to operate. Even the most conservative economists such as Milton Friedman could not deny this point.⁵⁶⁰ It is more striking to say that the emergence of state regulations is a natural result of a market economy. Polanyi refuted the Marxist explanation of state regulations as functional to capitalist development, and he also denied neo-classical economics' 'false saying' that regulations help to inhibit development of a market economy. He argued that a feature of our modern times is to protect society from any harmful effects resulting from a self-regulating market economy.⁵⁶¹ This meant that ultimately the socialist movements or peasant movements of the 19th century were not conspiracies arising from political ideologies, but were only a natural reaction against the imperatives of market forces that drove an increasing proportion of the populace to take part in an increasingly capitalist market, selling labour or products.

⁵⁵⁸ No one up to now has used a Marxist approach to explain Taiwan's development of a business community, so I will skip this paradigm, which is often criticised by the Polanyian tradition.

⁵⁵⁹ See Karl Polanyi, *The Great Transformation—Origins of Our Time*. (Chinese, *Jubian: Dangdai Zhengzhi, Jingji de Qiyuan*, 鉅變：當代政治經濟的起源, tr. by Huang, Shumin, Shi, Jiayin and Liao, Wensheng, 黃樹民, 石佳音, 廖文生) (Taipei: Yuanliu Chubanshe, 1989), p.240.

⁵⁶⁰ See Milton Friedman, *Capitalism and Freedom* (Chicago: the University of Chicago Press, 1962).

⁵⁶¹ See Karl Polanyi, *op. cit.*, p. 155.

This viewpoint is also shared by Karl Marx. It is well known that Marx, following Hegel's tradition, used the 'dialectical method' to write his '*Das Kapital*'. Though his method is deductive, from the basic unit of capitalist society, i.e., commodity, to the demise of capitalism, his main concern is the social tensions arising from the *commodification* of social relations produced by capitalist development. In the last section of the first chapter of *Das Kapital*, Marx discussed at length 'the nature of commodification fetishism and its secrets'. Only in capitalist society does a human being's social life adopt the form of exchange, which seals the real social relations of private labour.⁵⁶² Marx said that the social relations of producers to labour appear as the social relations of objects which stand outside themselves.⁵⁶³ The market economy is the dominant form of our economic life, but it is full of conflicts and antagonisms springing from the law of the market.⁵⁶⁴

Bearing in mind such analyses of capitalist society, I endeavoured to expound the basic social tensions existing in Taiwan society by examining the case of the development of small and medium-sized enterprises. On the one hand, the market forces even non-economic organisations to conform to its rules, i.e., minimum cost, maximum profit. On the other hand, if a society is organised solely by market principles, it will not be able to function. Social norms are also important in our daily life, including business life. As Karl Polanyi observed, we have to acknowledge that power and values are a part of the reality,⁵⁶⁵ which it is necessary to incorporate into the analysis of a society and an economy. If this is so, it becomes evident that any approach adopting a one-sided theory will be inadequate; we need to see both sides: i.e., the contradictions between market relations and social relations.

⁵⁶² See Karl Marx, *Marx-Engels Werke*, Band 23 (Berlin: Dietz Verlag, 1971), p. 87.

⁵⁶³ *Ibid.*: p.86.

⁵⁶⁴ An und fuer sich handelt es sich nicht um den hoeheren oder niedrigen Entwicklungsgrad der gesellschaftlichen Antagonismen, welche aus den Naturgesetzen der kapitalistischen Produktion entspringen. See Karl Marx, *op. cit.*, p. 12.

⁵⁶⁵ See Karl Polanyi, *op. cit.*, p. 390.

7.2.1. The Fictitious Self-Regulating Market

Karl Polanyi noted that state regulations are natural results of a market economy, and Taiwan government's control of the economy provides illustrations of this story. The uneven distribution of occupations in the public and private sector of the two major ethnic groups in the 1950s illustrated the influence of political power in affecting a society's occupational structures. Moreover, the labour force was not totally proletarianised, i.e., did not become a commodity, after Taiwan's economic take-off. The workers could flow back to the rural area, where the farm family still could support family members when they became unemployed in the urban area. This situation is different from English workers' situation at the beginning of the 19th century, when they were expelled from their lands and displaced by sheep. The third production factor, capital, was always controlled by the government. As we have seen, there were two financial systems in one country, i.e., the regulated financial market and an unregulated financial market. There was no 'free capital market' at all.

The organisation of production was also shaped by social values and culture, which is not what the transaction cost theory depicts: that they are organised by economic principles. Though family enterprises are very common in the world, different societies have different ways to operate the enterprises according to different socio-political contexts. Family enterprises have to take on a traditional responsibility to take care of family members on the one hand, and have to conform to market forces to make money on the other. These two different principles produce a lot of organisational tensions, as we have observed in Chapter Five.

To the extent that production factors and organisations are regulated in terms of political power and social values, there will be no free market economy in the sense claimed by neo-classical economics. Neo-classical economics tries to explain the development of Taiwan's economy in terms of 'getting prices right' and in the assumption that the magic of the market would steer every economic agent's behaviour toward the optimum, i.e., economic success. For example, Samuel P. S. Ho claims that the Taiwan experience *once again* confirms that administrative controls and other forms of

interference with the market can seriously distort the economy,⁵⁶⁶ and Jiang Shuojie (蔣碩傑) has argued that correct interest rates and a correct exchange rate policy in the 1950s made the Taiwan economy efficient, producing good economic results.⁵⁶⁷ I would submit that they were just using the ideology of neo-classical economics to interpret Taiwan's development. They believe that any factor hampering the market's functioning should be removed to build up 'an efficient market'. But as we have seen, political power and social values played an important role in the economy; it is a false hypothesis that Taiwan was a free market economy and that this led to its economic success.

One possible criticism of this approach is that if there were no intervention from the government and tradition, the economy would be better off than it is. This approach is widely accepted in the 'new economic history approach' which uses econometrics to calculate what the economy would be if there were no factor A.⁵⁶⁸ This school can be traced back to the 'old economics tradition' of Friedrich Hayek, William G. Sumner, Herbert Spencer and Ludwig von Mises, who believed that without interventions, the market would solve all problems. As Karl Polanyi observed, 'this is their last excuse'.⁵⁶⁹ Because these 'economic liberals' could not find any evidence to explain why there have always been interventions since the establishment of the market economy, they attribute this to the hypothesis of an 'anti-market conspiracy'. Trade unions, monopolisers, politicians, farmers and environmentalists are all villains who unite together to oppose the functioning of market forces.

When we review Taiwan's postwar history, we discover immediately that this hypothesis has no empirical support. One piece of evidence is the education policy which we discussed in Chapter Two. If the government had followed a *laissez faire* policy, it would not have regulated the development of private schools. Most economists agreed at

⁵⁶⁶ See Samuel P. S. Ho, *Economic Development of Taiwan, 1860-1970* (New Haven and London: Yale University Press, 1978), pp. 248-251.

⁵⁶⁷ See Jiang Shuojie (蔣碩傑), 'Taiwan Jingji Fazhan de Qishi' (台灣經濟發展的啟示, 'The Implications of Taiwan Economic Development'), in Ma Kai (馬凱) (ed.), *Taiwan Jingji Yanjiu Luncong—di yi ji, Jingji Fazhan yu Zhengce* (台灣經濟研究論叢—第一季, 經濟發展與政策, *Essays on the Economy of Taiwan, vol. 1, Economic Development and Policy*) (Taipei: Zhonghua Jingji Yanjiuyuan, 1991) p.22.

⁵⁶⁸ See Douglass C. North, *Institutions, Institutional Change and Economic Performance* (tr. by 劉瑞華, 制度、制度變遷與經濟成就) (Taipei: Shibao Chubanshe, 1994).

the time that it was beneficial to regulate the education market according to the needs of national development. They forecast that Taiwan needed more skilled labour after its economic take-off, and they recommended to restrict the development of academic schools, and to expand vocational education. Therefore the ratio of academic school students to vocational students could be reversed from 7:3 to 3:7 in twenty years. This kind of regulation has not been criticised by Taiwan's economists at all; instead, they all praise the high quality of Taiwan's human resources and the success of Taiwan's education.⁵⁷⁰ They also asked to set up a Fair Trade Committee to *regulate* monopoly business. In other words, the problem lay not in regulation or intervention, but in economic theory. They could behave like *interventionists* to advocate regulations, all the while that the economists preached the virtues of a fictitious self-regulating market, but not *laissez faire*.⁵⁷¹

7.2.2 The Orientalistic Discourse

Sociologists and anthropologists sometimes seek to dismiss the function of the market in modern society. They emphasise the primacy of cultural values and traditional social institutions, but forget that the development of a market system will inevitably bring about changes in society, and social institutions can be subordinated to the market economy.⁵⁷²

One of the traditions emphasises the importance of cultural values in business organisational behaviour. This genre of research and analysis endorses some widely accepted hypotheses:

- it is the Chinese mentality which drives the Chinese to want to be proprietors.⁵⁷³

⁵⁶⁹ See Karl Polanyi, *op. cit.*, 244.

⁵⁷⁰ See Hou Jiming (侯繼明), 'Jiegou Xuepai, Xingudian Xuepai yu Taiwan Gongye Shengji' (結構學派, 新古典學派與台灣工業升級, 'Structuralism, Neoclassical Economics and Upgrade of Taiwan's Industry'), in Ma Kai (ed.), *Ibid.*: p. 32; Wu Hui-lin, 'Taiwan de Laodong Shichang yu Jingji Fazhan' ('Taiwan's Labour Market and Economic Development'), in Ma Kai (馬凱) (ed.), *Ibid.*: pp. 83-113.

⁵⁷¹ See Karl Polanyi, *op. cit.*, p. 250.

⁵⁷² *Ibid.*: p. 154.

⁵⁷³ See Richard W Stites, 'Industrial Work as an Entrepreneurial Strategy', *Modern China*, vol. 11, no.2 (April 1985), p. 238; Chen Jiexuan, *Xieli Wangluo yu Renji Wangluo—Taiwan Zhongxiao Qiye De Shehui Jingji Fenxi (Subcontracting and Personal Networks—social economic analysis of Taiwan's small and medium-scale enterprises)* (Taipei: Lianjing Chubanshe, 1994), p.292; Wong, Siu-lun, 'Business

- the equal partition of family property to each son makes it difficult for a family firm to grow large after the first generation.⁵⁷⁴

- the economic unit in Chinese business is not the individual but the extended household.⁵⁷⁵

- ‘familial solidarity’ constitutes the core of the Chinese family enterprise. Because they are able to pull the outside world into their networks, the family firms work well.⁵⁷⁶

- kinship networks are also networks of trust.⁵⁷⁷

- Guanxi* tends to be stable over the long term based on reciprocal trust, loyalty and predictability.⁵⁷⁸

- the Chinese management pattern is paternalistic.⁵⁷⁹

- the Confucian ethic encourages a willingness to devote oneself to vigorously pursuing the family’s material interests over both the short and long term.⁵⁸⁰

This cultural approach is just a variant of the ‘Orientalistic discourse’ which *objectifies* Chinese society and gazes at it from the eyes of Western culture. Its adherents try to discover the factors underlying ‘Chinese’ society which have not altered in the past thousand years. Marx has made the criticism of political economists that in their analysis there is history before the emergence of capitalism, but no more after the emergence of capitalism. This criticism can also be applied to this cultural approach: there is history in different countries, but no history in a particular individual country. In their analysis, political and market forces seem never to have an effect on organisational behaviour. But as we have argued, political and economic power have influenced the ethnic distribution

networks, cultural values and the state in Hong Kong and Singapore’, in Rajeswary Ampalavanar Brown (ed.), *Chinese Business Enterprise in Asia* (London, New York: Routledge, 1995), pp.136-153.

⁵⁷⁴ See Gary G. Hamilton and Nicole Woolsey Biggart, ‘Market, Culture, and Authority: A Comparative Analysis of Management and Organisation in the Far East’, *American Journal of Sociology*, vol. 94 (1988) (Supplement), pp. 52-94.

⁵⁷⁵ See Department of Foreign Affairs and Trade, *Overseas Chinese Business Networks in Asia* (Canberra: Australian Government Publishing Service, 1995b), p.126.

⁵⁷⁶ See Wong, Siu-lun, 1995, *op. cit.*, p. 139.

⁵⁷⁷ See Thomas Menkhoff, *Trade Routes, Trust and Trading Networks: Chinese Family-Based Trading Firms in Singapore and Their External Economic Dealings*, unpublished Ph.D dissertation (1990), Faculty of Sociology, University of Bielefeld.

⁵⁷⁸ See Gary G Hamilton and Kao Cheng-shu, *op. cit.*, pp. 145-146.

⁵⁷⁹ See Gordon S. Redding, *The Spirit of Chinese Capitalism*, (Berlin: Walter de Gruyter, 1990), p.215.

⁵⁸⁰ See Tu Wei-Ming, *Confucian Ethics Today--The Singapore Challenge*, (Singapore: Curriculum Department Institute of Singapore, Federal Publications, 1984), pp.75-76.

in occupations, which made different ethnic groups experience different mobility patterns, and rendered the Taiwanese group more likely to become proprietors (Chapters One and Two); economic development influences the method of family division, and there is no reason to believe that a family firm cannot grow large (Chapter Five); the economic unit in Chinese business is not necessarily the extended household and it is not necessarily efficiency, instead, a lot of internal conflicts bedevil the family enterprise (Chapter Five); *guanxi* is not always stable, and when there are conflicting interests, it is highly possible that *guanxi* relationships will disintegrate, as we have seen with the buyer-seller's link in Chapter Four; Taiwanese (Chinese) management is not paternalistic at all in their overseas factories (Chapter Six); and the conflicting interests among family members make a family firm hard to maintain. All the cases that I have discussed above show that social relations are not easily maintained if they contradict market principles.

7.2.3 A 'Governed' Market without a Market

Another approach in the sociological tradition puts emphasis on political forces in shaping occupational structures and industrial organisations. It is mainly propounded by scholars of political economy. Their hypotheses include:

- Taiwanese, versus Mainlanders, held a comparative advantage in the small business world, where networks, familiarity and trust are required.⁵⁸¹

- the KMT state tried to create an 'unspoken alliance' with the petty bourgeoisie, the result being that the state left small business alone without interference.⁵⁸²

- any explanation of Taiwan's growth amidst stability must start with the Nationalist party-state, which effectively led sustained economic development.⁵⁸³

⁵⁸¹ See Marshall Johnson, 'Classification, Power, and Markets: Waning of the Ethnic Division of Labour', in Denis Fred Simon and Michael Y. M. Kau (eds.) *Taiwan: Beyond the Economic Miracle* (Armonk, M. E. Sharpe, Inc, 1992), p. 81.

⁵⁸² See Hill Gates, 'Small Fortunes: Class and Society in Taiwan', in Denis Fred Simon and Michael Y. M. Kau (eds.) *Taiwan: Beyond the Economic Miracle* (Armonk, M. E. Sharpe, Inc, 1992), p. 178; See Susan Greenhalgh, 'de-Orientalizing the Chinese Family Firm', *American Ethnologist*, vol. 21, no. 4 (1994), pp.766-767; Alice Amsden, 'Big Business and Urban Congestion in Taiwan: the Orgins of Small Enterprise and Regionally Decentralized Industry', *World Development*, vol. 19, no.9 (Sept. 1991), p.1122, 1126.

⁵⁸³ See Thomas B. Gold, *State and Society in the Taiwan Miracle* (Armonk, New York/London: M.E. Sharpe, 1986), p.122.

●local factions could reap great benefits if they maintained good connections with the government.⁵⁸⁴

Their analysis is close to reality, but they ignore two important aspects: the social institutions and market forces, which might resist any intervention of political power and therefore will weaken any policy intentions from above. In Chapter Two we have argued that the open economy in the 1960s offered the less educated, mainly Taiwanese whose family background was not as good as the Mainlanders another path to be upwardly mobile. This ethnic economic division had nothing to do with primordial ethnicity, but was constructed upon political power. Yet at the same time, the numerous small and medium enterprises are the result of economic development instead of a policy result, as Donald DeGlopper has argued.⁵⁸⁵ Nor had the Nationalist state the intention to create an 'unspoken alliance' with small and medium-sized enterprises, as we have shown in Chapter One that most financial assistance in the 1950s went to big business because of its close alliance with the KMT regime.

All the same, the government's means of control created a space for people to exploit the regulations. The underground economy was the symbiotic product of government regulations. In the study of the 'entrustment program' in Chapter Four, we also saw that businesspeople exploited it to make huge profits from the government's cotton rationing. So, too, SMEs benefited from the regulated financial system to evade tax (Chapter Three). But this does not mean that one could exploit and profit from the regulations indefinitely. Market forces will constrain such exploitation, just as the saturation of the domestic textile market after 1954 drove many SMEs to dump their products at a loss. While intervention occurred in the market, the market could not be totally controlled.

This 'governed market' school of scholarship often ignores the widespread corruption, tax evasion, embezzlements and bribery in Taiwan's business and government

⁵⁸⁴ See Chen Mingtong, *Quyuxing Lianhe Duzhan Jingji, Difang Paixi yu Shengyiyuan Xuanju: Yixiang shengyiyuan houxuanren beijing ziliao de fenxi (Regional Oligopoly, Local Factions and Provincial Assembly Elections: an analysis of the background of candidates)*, unpublished paper, 1989:12; Chen Dong-sheng, *Jin Quan Chengshi—Difang Paixi, Caituan yu Taipei Duhui Fazhan de Shehuixue Fenxi (Money+Power City—A Sociological Analysis of Local Factions, Zaibatsu and Taipei Metropolitan Development)* (Taipei: Juliu Chubanshe, 1995).

⁵⁸⁵ See Donald R. DeGlopper, 'Artisan Work and Life in Taiwan', *Modern China*, vol. 5, no. 3 (July 1979), p. 286.

relationships. In Chapter Three and Four, we showed that to deal with the government bureaucracy it is necessary for a company to engage in such practices. The market is 'governed', but it has not thereby necessarily become more efficient. These activities are part of an 'unseen' market which could destroy any policy intentions claimed by the government.

7.2.4 The Paradox between the Market and Society

We ought not idealise the market's magic power, nor the strong state's capacity, nor traditional cultural values. These factors' influence is not linear, nor possess any '*mechanical causality*'. We rather see the relationships between these factors as *dialectical*, showing the paradox of how different social forces as these work on individuals and organisations.

Many scholars have explored the basic contradiction underlying capitalist society, i.e., *accumulation* and *legitimacy*. Karl Polanyi used this concept to explain the rise of fascism, and the meaning of freedom in modern society.⁵⁸⁶ James O'Connor argued that the fiscal crisis of the welfare state could not be resolved because the state has to spend money to support economic development on the one hand, and to provide welfare to save labourers from pauperisation on the other. The state could not raise taxes to pay for its expenditures, for this will discourage capital investment. In other words, the capitalist society's method is 'to socialise cost, but to privatise profits'.⁵⁸⁷ Jurgen Habermas used the same concepts to analyse the dilemma of the modern capitalist state.⁵⁸⁸

But up to now it seems no one in Taiwan has tried to analyse the dilemma of certain social institutions or organisations in the interstices between market forces and social values, or more precisely, the institutional changes in the process of economic development. If the dissertation has any theoretical contribution, it would be here. Throughout the thesis, I tried to discover what contradictory effects a given policy or set of social institutions would produce in Taiwan. The ethnicised class structure in the 1950s helped the next generation of Mainlanders pursue white collar jobs, but they also

⁵⁸⁶ See Karl Polanyi, *op. cit.*, pp. 383-392.

⁵⁸⁷ See James O'Connor, *op. cit.*, pp. 5-10.

⁵⁸⁸ See Jurgen Habermas/ tr. by Thomas McCarthy, *Legitimation Crisis (Legitimationsprobleme im Spaetkapitalismus)* (Boston: Beacon Press, 1975).

lost the chance to pursue economic opportunities in the 1960s, when the world economy offered a congenial business environment. The economic development promotion policies reduced companies' production costs, but at the same time supplied those firms with tools to 'make money from the state', as with the financial aid to SMEs or the export tax rebate.⁵⁸⁹ Workers in Taiwan acquired their jobs through social networks, which in turn also became a tool for the capitalists to deal with the labour movement, and produced a high turnover rate of workers. And we have seen how the family firm tries to take care of its family members, but how this could result in employing inefficient members, which in turn reduces its competitiveness in the market, and produces conflicts within the family. Broad social networks help one's business, but at the same time require one to fulfil responsibilities to the network, which become a business cost.

In the Introduction, I cited Duerrenmatt's words: paradox reveals the truth. There are no linear relationships in human affairs; only from contradictions can we see the basic problems of a society. Taiwan's experience in the past illustrates how people adjust themselves to the impact of different powerful forces. No single force could generate this great transformation. Accompanying the conflicts and economic development, people have learned how to deal with different situations wrought by an admixture of political, social and economic forces. By solving the contradictions arising from the structures they created, they are writing their own history, and generating further paradoxes. As Karl Polanyi noted, though it deprives us of our freedom, we have to face social reality, and accept it without complaining, and if so, it will give us the courage and strength to fight against injustice and limitations. These limitations give us the insight: we lose old freedoms, which are just illusions (by this, Polanyi means the freedom of contract proposed by liberalism), and the new freedom we obtain is real.⁵⁹⁰

⁵⁸⁹ The import tax would be given back if a company used the imported goods to produce goods and export it. Quite often they imported materials and sold it in domestic market. At the same time, they exported rubbish, but claimed that they had used the materials and exported it, so that they could claim back the import tax. In business community, it is called 'profit two hands'—profit from domestic sale, and from export tax rebate. Many Taiwanese companies use the same strategies when they invest in China nowadays.

⁵⁹⁰ Karl Polanyi, *op. cit.*, p. 392.

APPENDIX

Appendix 1 Background of Interviewees

Date of Birth	Education	Father's Occupation	Siblings	Children	Company	Workers
1938	College	Tailor	2	2M, 1F	Construction	Put-out
1936	Primary	Fisherman	7	1M, 5F	Construction	Put-out
1949	College	Boss of a Factory	4		Fertiliser	20-30
1952	Primary	Farmer	8		Auto Parts	7
1949	Primary	Peddler	7	3M	Printing	2
1946	Senior Vocational High School	Died at eight years old/ brought up by his brother	?	1M, 4F	Machinery	12
1942	Junior High School	Driver	7	2M, 1F	Plastic Tube	15
1949	College	Boss of a Small Shop	8	2F, 5F	Printing	30-40
1941	Primary	Tailor	8	1M, 4F	Kitchen Wares	16
1928	Primary	Short-term Worker	5	3M, 1F	Construction	Put-out
1940	College	Commerce	3	2M	Metal Parts	200
1938	Senior High School	Doctor of Chinese Medicine	6	2M, 1F	Publication	15-20
1930	Senior Vocational High School	Worker in a Newspaper Co.	?	2M, 1F	Toys, Phones	250
1933	Primary	?	?	2M, 1F	Shoes	200-220
1949	Senior High School	Short-term Worker	8	3F	Publication	30
193?	University	?	?	3F	Auto Parts	80
1963	Junior High School	?	10	2M	Machinery	20
1939	College	Landlord	?	1M, 2F	Plastics	50-60
1951	Primary	Landlord	9	?	Kitchen Wares	30-40
1954	Senior Vocational High School	Secretary to a Manager of a Public Textile Enterprise	4	2F	Electronics	70
1947	Junior High School	Died/ Brought up by Grandmother	0	1M, 2F	Machinery	30
1941	Junior Vocational High School	Farmer	7	2M, 2F	Textile	50-60
1952	Senior Vocational High School	Manager of a Trading Co.	3	3M, 1F	Electronics	25
1939	Primary	Boss of a Factory	4	1M, 1F	Fertiliser	5
1952	University	Civil Servant		2F	Motorcycle	150
1950	Junior Vocational High School	Boss of a Rice Factory	5	1M, 2F	Machinery	50
1933	Senior Vocational High School	Businessman	7	2M, 1F	Carton	35
1952	University	Civil Servant	?	2M	Construction	50
1951	College	Farmer	4	1M	Cement	200
1945	Primary	Tenant Farmer	3	2M, 1F	Metal Moulding	15
1944	Primary	Fisherman	8	1M, 2F	Machinery	160
1930	Primary	Farmer		3M, 2F	Steel Processing	260

1943	Senior Vocational High School	Fisherman	4	1M, 3F	Textile	17
1921	Primary	Farmer	6	1M, 4F	Furniture	0
1935	Primary	Boss of a Factory	5	3M	Iron Products	5
1949	Primary	Landlord	7	2M, 1F	Food	120
1955	Senior High School	Farmer	?	2M	Electronics	65
1939	Senior High School	?	?	1M, 3F	Trading co.	5
1956	Senior Vocational High School	Farmer	10	1M, 1F	Cans	35
1953	University	Civil Servant	5	2M	Trading co.	6
1951	University	Farmer	?	2M	Electronics	60
1948	University	Teacher	?	2M, 1F	Electronics	15

Appendix 2 Data Analysis

Table 1.8 and 1.9 are made from 'A General Survey of Social Change in Taiwan'⁵⁹¹ of 1989-90 and 1991-92. Each time they had two different questionnaires. In the two questionnaires of 1989-90 and the first questionnaire of 1991-92 it asks informants two questions: what was your father's occupation when you were eighteen years old (fifteen years old in 1991-92)? What was your first occupation? In the second questionnaire it asks only father's occupation when the informant was fifteen years old. To get the occupation structures in the 1950s, I select those informants born between 1931 and 1942 for the survey of 1989-90 and that between 1935 and 1946 to be my samples. When they were 18 or 15 years old, they were in the 1950s and we can pool their fathers' and their occupations as analysing data. In total I got 2,545 samples from these pooling. Because the old generation engaged more in primary industry, and young generation shifted to secondary or tertiary industry, so the pooling can show the occupation structures of these two generations. One problem is that the second questionnaire of 1991-92 do not include the question 'what was your first occupation', so the samples of old generation will be higher. I compare the percentage of the samples distributed in the different industries with official statistics in 1952 and 1955, and find the tertiary labour force in my samples is higher than official data. If we consider the official data did not include soldiers in the labour force statistics until 1968, we can say that the percentage of tertiary industry should be higher in the official data. In 1956 the number of soldiers were about 270,000, and the total labour force excluding soldiers were 3,231,000 (1955).⁵⁹² If we include soldiers in the data, the percentage of tertiary industry in total labour force was about 36% which is higher than that of my samples. Another way to check the sample is to deduct the soldiers from the samples and calculate the percentage of tertiary industry which is 30%, very close to the official data which is 28.4% in 1955. So basically the data is not so biased.

Another problem is that not all informants' first jobs was found in the 1950s. Some

⁵⁹¹ The data analysed in the paper were collected by the research project, 'A General Survey of Social Change in Taiwan' funded through grant from National Science Council, Republic of China (NSA-73-0301-H001-18). The research project was conducted by Institute of Ethnology, Academia Sinica under the directorship of Professor Kuo-shu Yang and Hei-yuan Chiu. the view expressed herein are the author's own.

⁵⁹² See Li Dong-ming, *A Study on Social Increase of Population in Taiwan* (Taiwan: Taiwan Population Studies Centre, Taiwan Provincial Department of Health, 1968), pp.61. Gupu Xiaoxiong (ed.), *Taiwan de Gongyehua: Guoji Jiagong Jidi de Xingcheng* (Taiwan Industrialisation: the Formation of International Processing Base) (translated from Japanese by Lei Hui-ying) (Taipei: Renjian Chubanshe, 1992), pp.246, appendix table 5.

had the job before 1950 and some after 1960. So here I have to make an assumption that it is randomly distributed so that the expectation of the first working year is in the 1950s.

One more problem is that Mainlanders in the samples were under-represented. Mainlander was about 12% of total Taiwan population, but in my sample, it is only 6.1%. Though it is under-represented, but it will not affect the inference for analysing their occupation distribution as one-specific group.

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