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Li & Fung Research Centre  
11/F, LiFung Tower,  
868 Cheung Sha Wan Road,  
Kowloon, Hong Kong  
Tel: (852) 2300 2470  
Fax: (852) 2635 1598  
E-mail: [lfrc@lf1937.com](mailto:lfrc@lf1937.com)  
<http://www.lifunggroup.com>

## Analysis of the Economic Cooperation Framework Agreement (ECFA) between the Chinese Mainland and Taiwan

### Background

- Taiwan signed the Economic Cooperation Framework Agreement (ECFA) with the Chinese Mainland on 29 June 2010, which is a milestone in cross-strait ties.
- The ECFA aims to set out the framework and targets; and is not a one-off agreement. More deregulations are in the pipelines.
- To satisfy the demand for urgent actions in certain sectors, the ECFA includes the early harvest list, which will hopefully take effect in January 2010 after the Legislative Yuan's approval.

### Content of the early harvest list

- The Chinese Mainland will eliminate the tariffs imposed on 539 import items from Taiwan in several stages.
- Taiwan will follow a similar time frame to eliminate the tariffs it presently imposes on 267 goods from the Chinese mainland.
- On service sector liberalization, The Chinese Mainland agreed to open up 11 service industries to Taiwan and Taiwan will open up 9 service sectors in return.

### Impacts on Taiwan

- The ECFA is set to further advance cross-strait relations and give a major boost to two-way trade.
- The ECFA opens the door for similar treaties between Taiwan and other countries.
- The ECFA, coupled with the progress in Three Linkages and government policies to lure foreign investment, will enhance the incentive for multinationals to invest in Taiwan.
- Some multinationals may see Taiwan as a priority cooperation partner and gateway to enter the Chinese Mainland market.

### Impacts on Hong Kong

- The ECFA may weaken the role of Hong Kong as a gateway to the Chinese Mainland and the middleman between the Chinese Mainland and Taiwan. A new positioning of Hong Kong is called for amid the improved cross-strait economic cooperation.
- The Chinese government has reportedly reassured Hong Kong that all CEPA+ offers in the ECFA will be incorporated into the CEPA.

## **Analysis of the Economic Cooperation Framework Agreement (ECFA)** **between the Chinese Mainland and Taiwan**

### **I. ECFA in brief**

#### **1. Background**

Taiwan signed the Economic Cooperation Framework Agreement (ECFA) with the Chinese Mainland on 29 June 2010, which is a milestone in cross-Strait ties. The ECFA aims to set out the framework and targets; and is not a one-off agreement. The content will be expanded step-by-step in future negotiations. More deregulations are in the pipelines.

To satisfy the demand for urgent actions in certain sectors, the ECFA includes the early harvest list, which will hopefully take effect in January 2010 after the Legislative Yuan's approval. Goods and services not included in the early harvest list will be dealt with in future ongoing negotiations.

Apart from the trade pact, the two sides have also signed an agreement on intellectual property rights protection.

#### **2. Content of the early harvest list**

The early harvest list includes tariff reduction/ removal and liberalization of trade in services.

##### **(1) Tariff concessions**

The early harvest list for Taiwan turned out to be slightly better than expected, in terms of the number of covered export items (539) and dollar value (US\$13.8bn; 16.1% of Taiwan's exports to the Chinese Mainland) of goods. Import duties on 72 of the 539 items will fall to zero at the start of 2011. Tariffs on these 72 items currently stand at 5% and below. Import duties on another 437 items, which currently range between 5.5% and 15%, will be eliminated at the start of 2012. Tariffs on the remaining 30 items, which currently stand above 15%, will fall to zero in three stages by January 2013. Taiwan will follow a similar time frame to eliminate the tariffs it presently imposes on 267 goods from the Chinese mainland.

Exhibit 1 and 2 provide a summary of the early harvest list at goods:

## Exhibit 1: Taiwan's exports to the Chinese Mainland

Sector	Items	US\$bn	As % exports to the Chinese Mainland
Petrochemical	88	5.94	6.93%
Textile	136	1.59	1.85%
Machinery	107	1.14	1.33%
Transportation	50	0.15	0.18%
Agriculture	18	0.02	0.02%
Others	140	5.00	5.84%
Total	539	13.84	16.14%

## Exhibit 2: Taiwan's imports from the Chinese Mainland

Sector	Items	US\$bn	As % imports from the Chinese Mainland
Petrochemical	42	0.33	1.21%
Textile	22	0.12	0.43%
Machinery	69	0.47	1.75%
Transportation	17	0.41	0.02%
Others	117	1.53	5.64%
Total	267	2.86	10.53%

Included in the agreement is a set of provisional rules governing certificate of product origins. The provisional rules prescribe more stringent regulations in defining product origins. According to the head of Taiwan's Department of Customs Administration, the required percentage of content provided at product origins should be between 40% and 50%.

## (2) Open market access in service sectors

**The Chinese Mainland agreed to open up 11 service industries to Taiwan**, which include accounting and audit; computer services (software & data processing); research & development (natural science & engineering); convention; professional design; film import; hospital; civil aircraft maintenance; banking; securities; insurance.

One highlight is that Taiwanese banks are granted to do Renminbi (RMB) business to Taiwan companies after establishing branch and being profitable for one year vs two years under the Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA) and three years under the World Trade Organization (WTO). After establishing branch for two years and being profitable for one year, Taiwanese banks can do RMB business to all kinds of clients. Life insurers will also receive slightly better treatment, i.e., lower capital requirement in setting up a JV in the Chinese Mainland.

**Taiwan will liberalize 9 service sectors to the Chinese Mainland**, which include research and development; convention; exhibition; product design; film import; agency services; sports and entertainment; air ticketing; banking and financial services (excluding securities, futures and insurance).

Requirements on “service suppliers” in the ECFA are similar to those in the CEPA. “Service supplier” as used in the ECFA refers to any person (natural/ judicial person) that supplies a service:

- Natural person – a natural person with identity document
- Judicial person – any legal entity duly organized under the applicable laws of the Chinese Mainland or Taiwan, including any corporation, trust, partnership, joint venture, sole proprietorship or association (business association). A service supplier should have engaged in substantive business operations for 3 years or more (5 years for certain financial institutions).

## 3. Issues subject to further negotiations

The Chinese Mainland and Taiwan will jointly set up a committee (兩岸經濟合作委員會) for cross-Strait economic cooperation to ensure ECFA agreements can be reached and to supervise the implementation of the ECFA. The committee will hold routine meetings every six months and may have interim meetings upon agreement by the two sides.

The two sides will continue discussing agreements for commodity trade, service trade and investment six months after the ECFA takes effect. Further discussion will include tariff reduction and removal; rules of origin; customs procedures; trade remedies. Discussions on service trade agreement will focus on cutting and removing restrictive measures gradually, enlarging the service sectors covered, and enhancing cross-Strait cooperation.

The two sides also agree to enhance cooperation in medical and health, intellectual property protection, investment protection, finance, trade facilitation, customs, and E-business at the new round of talks.

## II. ECFA vs CEPA

### 1. Trade in Goods

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| ECFA | <ul style="list-style-type: none"><li>□ 1,592 Hong Kong origin products can enter the Chinese Mainland tariff-free.</li><li>□ Broad categories of the covered items: Pharmaceutical products, plastics and plastic articles, textiles and Clothing, food and beverages, base metal products</li><li>□ 55,541 Certificate of Hong Kong Origin under CEPA have been approved as in May 2010.</li></ul> |
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| CEPA | <ul style="list-style-type: none"><li>□ 539 items for Taiwan's export to the Chinese Mainland</li><li>□ 267 items for Taiwan's import from the Chinese Mainland)</li><li>□ Broad categories of covered items: Petrochemical, textile, agriculture, machinery, transportation (the list will be expanded in future ongoing negotiations)</li></ul> |
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### 2. Trade in Services

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| ECFA | <ul style="list-style-type: none"><li>□ The Chinese Mainland liberalize 11 service sectors: Accounting and audit; computer and related services, (software &amp; data processing); research &amp; development (natural science &amp; engineering); convention; professional design; film import; hospital; civil aircraft maintenance; banking; securities; insurance</li><li>□ Taiwan opens up 9 service sectors: Research and development; convention; exhibition; specialty design; film import; agency services; sports and entertainment; air ticketing; banking and financial services (excluding securities, futures and insurance)</li></ul> |
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| CEPA | <ul style="list-style-type: none"><li>□ The Chinese Mainland has liberalized 44 service sectors to HK</li><li>□ Broad categories that are the same with the ECFA: accounting, computer and related services, research &amp; development, convention, audiovisual, medical and dental, banking; securities and futures; insurance</li><li>□ On top of the ECFA: distribution, legal, storage and warehousing, advertising, freight forwarding agency, logistics, air transport, individually owned stores, management consulting, patent agency, trade mark agency, exhibition, job referral agency, telecommunications, tourism, professional qualification examinations, transport (comprising road freight/passenger transportation and maritime transport), market research, job intermediary, real estate and construction, building-cleaning services, photographic, public utility, information technology, cultural, translation and interpretation, environmental, services related to management consulting, printing , social services, services incidental to mining , scientific and technical related consulting, rail transport, technical testing &amp; Analysis and product testing, sporting</li><li>□ A total of 2,233 certificates have been issued as in May 2010</li></ul> |
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### 3. "Early and pilot implementation"

Since 2008, the Chinese Mainland and Hong Kong announced 41 measures (including related measures in Supplement VII to CEPA) for "early and pilot implementation" in Guangdong Province. These pilot measures serve to demonstrate the effect of liberalization in the respective service sectors and contribute positively to the exploration of cooperation and integration of the service industries of Hong Kong and Guangdong.

### III. Impacts on Taiwan

The ECFA is set to **further advance cross-strait relations and give a major boost to two-way trade**. The Taiwan's Ministry of Economic Affairs predicted that GDP growth would up from 1.65% to 1.72%; export will grow by 5%. Though some worry that only big conglomerates in Taiwan would benefit from the deal while the majority of smaller businesses would be seriously affected. In addition to gradual tariff reductions in goods and open-ups in services after signing the ECFA, one of the possible supplements is to deepen development in Strait-West Coast Economic Zone particularly for the financial sector.

Signing the ECFA will also help Taiwan avoid being marginalized in the face of increasing trade blocs in the region and **opening the door for similar treaties between Taiwan and other countries**. There are 266 FTAs (Free Trade Agreements) /RTAs (Regional Trade Agreements) currently in effect globally, of which 41 are signed by Asian countries. However, for political reasons, Taiwan has not yet had any positive response from "target trading partners" to its endeavor in promoting bilateral FTAs. Taiwan has only signed 5 bilateral FTAs, which accounted for 0.2% of the island's global exports in 2009. As the Association of Southeast Asian Nations (ASEAN) Plus One free trade zone has come into effect, many products traded between the 10 ASEAN member states and the Chinese Mainland will be tariff-free. This places Taiwan's exports to these countries at a great disadvantage.

The inking of the ECFA will hopefully reduce the obstruction to Taiwan's effort to sign FTAs with other trading partners with improved cross-strait ties. According to the Japanese Chamber of Commerce & Industry, Taipei 2009 Taiwan White Paper Issue (October 2009), if the ECFA comes into being, it should form a great opportunity for Taiwan and Japan to discuss signing an FTA. The European Chamber of Commerce Taipei 2009-2010 Position Paper Overview (October 2009) also stated that "the sooner Taiwan signs the ECFA with The Chinese Mainland, the quicker political impediments to other countries (including the EU) signing economic agreements with Taiwan will be removed."

The ECFA, coupled with the progress in Three Linkages and other measures offered by the Taiwan government to attract foreign investment and to encourage the return of Taiwan businesses to the domestic markets (such as the reduction of corporate income tax and offering incentives for building R&D centers) will **enhance the incentive for multinationals/ Taiwan companies to invest in Taiwan**. Some multinationals may see Taiwan as a priority cooperation partner and gateway to enter the Chinese Mainland market. The Taiwan government also wishes to lure multinationals to establish their global innovation centers and multipurpose operation hubs for transshipment, logistics, distribution and end-processing in Taiwan.

Sector-wise, financials and selective manufacturing sectors (ie, petrochemicals, autos/bikes, textiles, and machinery), should first benefit from the early harvest list. As the ECFA expands, we expect broader service sectors (ie, airline/shipping, retailing, and financials) will benefit.

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### Exhibit 3: Sectors to benefit

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	Benefits from early harvest list
Technology	Neutral
Financials	Positive for banks
Petrochemical	Slightly positive
Steel	Slightly positive
Construction/ real estate	Neutral
Airline/ shipping	Neutral
Food/ retailing/ hotels	Neutral
Auto	Slightly positive
Textile	Slightly positive
Overall	Slightly positive

Source: BofA Merrill Lynch Global Research

## IV. Impacts on Hong Kong

Some people worry that the inking of the ECFA may weaken the role of Hong Kong as a gateway to the Chinese Mainland and the middleman between the Chinese Mainland and Taiwan. A new positioning of Hong Kong is called for amid the improved cross-strait economic cooperation. Industries with lower thresholds such as re-export trade are more likely to be affected by the ECFA. Hong Kong-Eastern China re-export business will be affected in particular as the route between Taiwan and Eastern China is much shorter. However, the impacts on high-end service industries like banking, accounting, legal services, IPO, should be minimal.

The Chinese government has reportedly reassured Hong Kong that all CEPA+ offers in the ECFA will be incorporated into the CEPA.

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