Achieving Effective Governance under Divided Government and Private Interest Group Pressure: Taiwan’s 2001 Financial Holding Company Law

Sebastian Brück
Laixiang Sun

Department of Financial & Management Studies, SOAS, University of London,
London WC1H 0XG, United Kingdom

(THIS VERSION: (11 JANUARY 2006))

ABSTRACT
In recent years, the division of Taiwan’s government between a DPP-led executive and opposition-dominated legislature has led to rather inefficient policy-making. This problem has been exacerbated by the increasing involvement of interest groups in the island’s legislative process. Drawing on the case of the 2001 Financial Holding Company Law, this paper examines the conditions under which effective governance can still be achieved in Taiwan. The law, which allowed commercial banks, investment banks and insurance companies to be integrated within one legal entity, had been devised by the Chen administration to address Taiwan’s most severe banking crisis in decades. Analyzing its adoption process shows that concerted media pressure can succeed in forcing Taiwan’s major parties to jointly pursue beneficial legislation. Furthermore, the paper argues that interest group involvement in Taiwanese policy-making does not necessarily lead to crippling regulatory capture but, on the contrary, can entail welfare enhancing change.

Corresponding Author: Prof. Laixiang Sun, Department of Financial and Management Studies, SOAS, University of London, Thornhaugh Street, Russell Square, London WC1H 0XG, UK. Tel. +44-20-78984821, Fax. +44-20-76377075, Email: Laixiang.Sun@soas.ac.uk.
1. INTRODUCTION

Recent experience teaches that newly emerging democracies tend to face difficulties in establishing a productive balance between democratizing their polities and maintaining effective governance mechanisms. In Taiwan, this dilemma has also surfaced lately: Since the late 1980s, the political liberalization and democratization which have met with overwhelming approval by domestic and foreign commentators contrast with the mixed assessments of democratization’s effect on the quality of governance. While a few authors maintain that the Taiwanese government has maintained its previous autonomy and capacity for effective governance, the consensus view now holds that a number of difficulties stand in the way of coherent policy-making. Illustrating this sentiment, Rigger writes:

“It is the ability to provide political freedom while remaining accountable to the public that makes a democratic government democratic. But to be a government, it needs to govern – to respond with effective public policy to the popular preferences expressed through a free media and electoral process. It is on this front that Taiwan’s democracy has encountered its greatest challenges. In particular, Taiwan’s new democracy suffers from four serious failings: divided government leading to a legislative-executive stalemate, a failure of inter-party negotiation and compromise, inaction on critical issues and politicization and partisanship so extreme that the government is unable to move even in a crisis.”

To these ‘failings’ may be added another, related issue: A number of analysts have lately argued that increasingly powerful domestic economic interest groups exert significant pressure on Taiwanese policy-makers, thus further undermining the latter’s autonomy and, by implication, effective policy-making. The political stalemate described by Rigger may in fact have widened the scope for such ‘regulatory capture’.

According to this pessimistic view, the potential for effective governance in Taiwan has been much reduced in recent years, especially since Chen Shui-Bian’s election to the presidency in 2000 and the ensuing period of ‘divided government’ (while Chen won the presidency for the Democratic Progressive Party [DPP], elections to the Legislative Yuan yielded Kuomintang [KMT], People First Party and New Party)

---

1 In recent years Russia, for example, has illustrated this dilemma: The country witnessed increasing political freedoms over the course of the 1990s but only at the cost of severely undermined state capacity to provide effective governance. See for instance Stiglitz, Joseph, “Whither Reform: Ten Years of the Transition”, in: Pleskovic, Boris, Stiglitz, Joseph, Annual World Bank Conference on Development Economics 1999 (Washington D.C.: World Bank, 2000).


majorities in 1998, 2001 and 2004).\(^5\) Concrete policy issues where governance has been compromised range from cross-strait relations with mainland China to domestic economic policy-making.\(^6\)

In energy policy, for example, President Chen in October 2000 announced the executive’s decision to halt construction of the controversial 4\(^{th}\) nuclear power plant. Following an outcry by the business community, opposition lawmakers, holding a majority of seats in the Legislative Yuan, ferociously battled the executive’s decision, denying its legitimacy and demanding a recall of President Chen.\(^7\) In the end, the Council of Grand Justices stepped in and overturned the executive’s decision for “procedural reasons”.\(^8\) Construction of the nuclear power plant finally went ahead after a severe delay, but the combination of ‘divided government’ and the weighing in of business interests had hardly yielded efficient policy-making.

Financial sector policy-making in 2001 seemed to follow a similar pattern. At the time, Taiwan experienced its most severe banking crisis to date, which had begun in 1998. Resulting from long-standing structural deficiencies in the banking system as well as a cyclical downturn in economic activity, the crisis drove up non-performing loan (NPL) figures to previously unreached heights and undermined public confidence in Taiwan’s financial system.\(^9\) The government attempted to tackle the crisis with a variety of legislative measures, including the Financial Holding Company Law (FHCL).

The law offered financial companies such as banks, securities firms and insurance companies the opportunity to set-up financial holding companies (FHCs), which could operate subsidiaries across a wide range of financial services and thereby build business scale and scope. Following similar laws in Japan in 1996, the United States in 1999 and South-Korea in 2000, the 2001 Taiwanese FHCL was a deregulatory initiative that would tear down remaining barriers between different financial services, thereby ushering in a new era of so-called ‘integrated financial services provision’.\(^10\)

While the FHCL seemed a further step in the right direction of aiding the besieged Taiwanese banking sector, in June 2001 the DPP executive’s initiative was blocked by the Kuomintang, People First Party and New Party majority in the Legislative Yuan until the legislature’s session came to a close on June 6\(^{th}\), 2001. Faced with the prospect of yet another delayed reform, investors in Taiwan’s stock market reacted promptly: Following news that the Legislative Yuan failed to pass the FHCL, the Taiwan stock exchange index fell by 1.3% overall, with the banking and insurance sub-index losing 3.1% in a single day. One market analyst commented:


\(^6\) See Sheng, Lijun, China and Taiwan: Cross-Strait Relations Under Chen Shui-Bian (Singapore: Institute of Southeast Asian Studies, 2002), pp. 61-65 and Green, “Taiwan in the 1990s”.


There is too much partisan politics and the legislators’ failure to pass the Act demonstrates they are unable to work together to get through key legislation.”

At first, it therefore appeared as if divided government had once again choked effective governance: Apparently, opposition lawmakers blocked a potentially beneficial law so that the DPP could not benefit from an economic upturn in the year-end legislative elections. Furthermore, the circumstances surrounding introduction of integrated financial services provision in the United States in 1999 also suggested that rising private interest group pressure may have undermined Taiwanese financial policy-making: Typically, investment banks and insurance firms fear the increased competition by commercial banks they would face after the introduction of integrated financial services provision and thus tend to lobby lawmakers to prevent such deregulatory initiatives.

To the surprise of observers, however, the end of the regular Legislative Yuan session was not the end of the FHCL. After about 2 weeks of protracted negotiations, President Chen requested a ‘special legislative session’ (only the fourth in the history of Taiwan) from the members of the Legislative Yuan, which the latter agreed to. In late June, that ‘special session’ was then used to pass the FHCL and a number of other financial reform bills, setting-off Taiwan on the path towards integrated financial services provision and a looming recovery in the banking sector.

The question thus arises which factors account for the eventually successful adoption of the FHCL. In particular, why could the ‘failings’ of Taiwanese democracy that Rigger and others have drawn attention to all be overcome in the case of the FHCL? In addition, one may also wonder about the role played by private interest groups in the passage of the FHCL. As indicated above, the literature on the political economy of financial regulation typically posits that commercial banks will favor the introduction of integrated financial services provision as it offers additional business opportunities, while investment banks and insurance companies oppose such deregulation for fear of increased competition. Did financial interests, then, attempt to influence the FHCL-making process? Answering this question also sheds an important light on the opportunities for - and threats to – effective policy-making in modern Taiwan.

In section 2 this paper first provides an overview of the Taiwanese banking sector between 1949 and 2001. Sections 3 and 4 analyze and discuss how different financial sector stakeholders viewed and evaluated the 2001 Taiwanese FHCL, with section 3 focusing on the ‘public sector’ (the executive, legislature and regulators) and section 4 analyzing the ‘private sector’ (the financial sector and bank customers). For

15 In the literature on the political economy of regulation, two broad theories explaining regulatory change are commonly advanced, namely, the ‘public’ and the ‘private interest theory of regulation’. In this paper, public as well as private interest motivations for regulatory reform feature in section 3, while section 4 deals solely with private interest motivations. For background on these two approaches, see for example Kroszner, Randall S., Strahan, Philip E., “What Drives Deregulation? Economics and Politics of the Relaxation of Bank Branching Restrictions”, The Quarterly Journal of
empirical evidence, both sections draw on a review of news sources, the relevant academic literature and original interviews with Taiwanese regulators, bankers, management consultants and academics conducted for this study. Section 5 considers the law’s impact on the Taiwanese banking sector and concludes.

The paper demonstrates that actors in the ‘public sphere’ were united in their positive assessment of the FHCL’s effects, which was seen as offering the banking sector valuable opportunities for building scale and scope to overcome the banking crisis of 2001. While opposition lawmakers attempted to block the law for tactical, partisan reasons, strong media pressure eventually prevented them from doing so. In contrast to earlier deregulation moves in the United States, private financial interests in general also favored the law and lobbied to overcome the stalemate. While divided government and regulatory capture may impede Taiwanese policy-making in other areas, the introduction of integrated financial services provision provides an example of how divided government may be overcome by media pressure and a process one may term ‘benign’ capture. More generally, this paper identifies the forces aiding a newly democratized country in achieving the elusive yet productive balance between a democratized polity and effective governance alluded to above.

2. THE TAIWANESE BANKING SECTOR BETWEEN 1949 AND 2001

Table 1 shows major participants in the three important financial markets that together constitute the Taiwanese financial system. Note that not all of the listed institutions have been active in the financial system since 1949.

(Insert Table 1 here)

Since 1949, commercial banks have been the centerpiece of the formal Taiwanese financial system. The evolution of the Taiwanese banking sector between 1949 and 2001 can be divided into two distinct subperiods.

2.1. 1949-late 1980s: ‘Bureaucratic Banking’

Three distinct features characterized the Taiwanese commercial banking market between 1949 and the late 1980s: extensive government and KMT ownership of financial institutions, heavy-handed governmental regulation of the banking system in terms of entry, pricing, product offerings etc. as well as ‘financial dualism’. Regarding the first feature, the government and KMT owned up to 90% of all Taiwanese commercial banks in the indicated time period, thereby controlling similar shares of banking assets and deposits. Furthermore, the government strictly controlled bank entry, branching and interest rates. The business scope of commercial banks was effectively restricted to taking deposits and extending loans, resulting in

\[ \text{\ldots} \]

\[ \text{\ldots} \]
a clear separation from investment banks and insurance companies.\textsuperscript{20} Finally, as a result of extensive governmental and KMT interference in the formal financial and banking system, informal financial institutions thrived and provided significant amounts of funding in particular to small- and medium-sized enterprises (‘financial dualism’).\textsuperscript{21}

Between 1949 and the late 1980s, Taiwan thus exhibited a strongly regulated, bureaucratically dominated commercial banking system that succeeded on two counts: Economically, monetary control, price stability and a measure of systemic stability were achieved.\textsuperscript{22} Politically, the system in the 1949-1989 period helped the KMT to prevent the rise of indigenous, Taiwanese financial capitalists and thus bolstered the KMT’s grip on power.\textsuperscript{23} However, the Taiwanese banking system did not perform well in delivering transparency, competition, efficiency and innovation.\textsuperscript{24}

\textbf{2.2. The 1990s: Reform and Crisis}

Dissatisfaction with the indicated drawbacks of governmental and party interference in the financial system led to financial ‘deregulation, liberalization and internationalization’ in the late 1980s and early 1990s.\textsuperscript{25} Most importantly, a number of new, privately-owned banks were licensed, interest rates decontrolled and the activity scope of banks widened to include securities business such as trading, brokerage and underwriting.

At first, the reforms seemed to work. One influential analyst commented that in the 1990s:

“\textit{The [now] intense competition […] has meant reductions in lending rates, increases in deposit rates, improved customer service and development of new financial services.”}\textsuperscript{26}

The Taiwanese banking sector also performed comparatively well during the 1997 Asian financial crisis, a success that was in part traced back to seemingly superior banking regulation and supervision practices.\textsuperscript{27}

In the late 1990s, however, problems in the banking sector emerged: For a start, falling domestic stock and real estate markets, industrial relocation to China and falling export demand reduced economic growth and led to rising unemployment and NPL ratios.\textsuperscript{28} As described above, first President Lee Teng-Hui and then President Chen set out to address the NPL problem by various measures. For

\begin{flushleft}
\textsuperscript{22} Ibid.
\textsuperscript{24} Chang, “Reform of the Business Service Sector”, p. 240.
\textsuperscript{26} Shea, “Development and Structural Change”, p. 261.
\textsuperscript{27} “The flexible tiger”, \textit{The Economist}, January 1\textsuperscript{st}, 1998.
\end{flushleft}
example, in March 2001 President Chen announced that he supported the establishment of a resolution trust fund as well as asset management companies.\textsuperscript{29}

Nevertheless, addressing the NPL issue was not sufficient to resolve the banking crisis. Ever since a number of privately owned banks had entered the Taiwanese banking system in the early 1990s, too many banks were operating in the market, thus driving down margins and profits to unsustainable levels.\textsuperscript{30} To make matters worse for lenders, Taiwanese companies in the 1990s increasingly accessed capital markets directly to obtain funds, rather than taking out bank loans (a process known as ‘credit disintermediation’). While some Taiwanese commercial banks had a license for underwriting corporate securities, others did not. The latter banks consequently faced not only a decline in business margins but also in business volume.

Two new laws were supposed to ease these structural burdens affecting banks: The 2000 Financial Institutions Merger Law provided incentives for increased bank merger and acquisition activity. Most importantly in the context of this paper, the Chen administration furthermore introduced the FHCL into the Legislative Yuan in 2001.

2.3. The 2001 Financial Holding Company Law

The law made it mandatory for financial groups with assets exceeding 150 billion New Taiwan dollars\textsuperscript{31} to transform into financial holding companies. The law’s overall intention was revealed in Article 1:

“\textit{This Act is enacted in order to increase the synergy of financial institutions (as defined below), to consolidate the supervision of cross-financial industry, to promote the sound development of financial markets, and to protect the public interest.}”\textsuperscript{32}

Synergies were to be reaped from combining different financial activities within the same holding company structure. Article 36 stated that:

“A Financial Holding Company shall ensure the sound management of the business activities of its subsidiary(ies). The business of a Financial Holding Company shall be limited to investment in, and management of, its invested enterprise(s). A Financial Holding Company may invest in the following enterprises:

1. Banking enterprises
2. Bills finance enterprises
3. Credit card businesses
4. Trust enterprises
5. Insurance enterprises
6. Securities enterprises
7. Futures enterprises
8. Venture capital investment enterprises
9. Foreign financial institutions which have been approved for investment by the MOF; and

\textsuperscript{29} Chou, Stanley, “President makes credit cooperatives top priority”. \textit{Taipei Times}, March 1\textsuperscript{st}, 2001.
\textsuperscript{31} “Conglomerates may be transformed into holding companies”, \textit{Taipei Times}, July 5\textsuperscript{th}, 2001.
10. Other enterprises which the MOF [Ministry of Finance] considers to be financially related businesses”.

The list shows that after the liberalization move, Taiwanese FHCs were authorized to offer a substantial range of financial products typically available in modern market economies. While Articles 43 and 48 of the FHCL established some ‘firewalls’ between different FHC subsidiaries (for instance the provision in Article 43 that cross-selling activities were only permissible as long as they did not ‘violate the rights and interests of customers’), overall these restrictions were mild. Clearly, the lifting of diversification restrictions and thus the exploitation of scale and scope economies by FHCs was the express purpose of the Taiwanese FHCL, which also offered tax benefits to induce financial institutions to opt for FHC status.


3.1. Executive

The interviews conducted for this paper in Taiwan reveal that the Taiwanese executive at the time – President Chen’s first administration, elected in 2000 – viewed the FHCL positively for two main reasons. Given the fragmentation of the Taiwanese banking system and the negative impact this market structure had on bank profits, the administration hoped that the exploitation of scale and scope economies by newly formed FHCs would lead to the much needed consolidation of the banking (and wider financial) sector.

Compared to other Asian countries, the fragmented Taiwanese banking market in 2001 was associated with very low average performance indicators for the major banks (Table 2).

(Insert Table 2 and Figure 1 here)

By allowing banks to exploit scale economies more decisively via the FHCL, the Taiwanese leadership hoped that lenders would overcome market fragmentation and achieve return on asset and return on equity ratios comparable to banks in, for example, Hong Kong.

At the same time, the FHCL was also meant to address the problem of credit disintermediation faced by Taiwanese lenders. Fuelled by regulatory, financial and technological advances, non-financial companies nowadays tend to raise increasing amounts of finance directly in the money and capital markets. Consequently, profits from traditional lending activities have declined for many banks in advanced and emerging economies. The same development also affected Taiwanese commercial banks negatively in the 1990s, as shown by Figure 1 below. The graph reveals that compared to 1990, when 90% of all non-financial firms’ financing had been provided by intermediaries, this figure had declined to 75% by 2001. As it was typically the largest and most sophisticated Taiwanese companies that would seek direct

---

33 Ibid.
35 Interviews ‘1-12’ in Taipei and London.
financing, Taiwanese commercial banks increasingly lost their most lucrative customers.

Those commercial banks without a license to underwrite corporate securities were particularly hard hit by these developments. But as traditional lending activities declined in importance, even commercial banks acting as underwriters were anxious to upgrade their fee-based product base in order to retain old and acquire new corporate customers, thus stabilizing and diversifying earnings.\textsuperscript{37} To complicate matters, Taiwanese commercial banks in the 1990s could only hold 5 percent of a security company’s capital.\textsuperscript{38} Hence, banks without an underwriting licence could not simply acquire a license-holding investment banking subsidiary whereas banks that already owned an underwriting license had difficulties in upgrading their capabilities via acquisitions. The introduction of FHCs, which allowed banks to exploit scope economies by moving into or upgrading existing securities operations and by establishing insurance services, was seen as the adequate response by the executive to these problems.\textsuperscript{39}

An analysis of news sources confirms the insight that the executive promoted the FHCL due to the indicated considerations. The extensive press coverage regularly featured articles outlining the possible scale and scope economies that the government hoped to achieve with the law.\textsuperscript{40}

Other possible benefits strengthened the executive’s positive assessment of the FHCL’s effects. For example, the Chen administration also hoped for increased foreign direct investment as a result of passing the FHCL. Minister of finance Yen Ching-Chang explicitly predicted that an extra 5 billion United States dollars of foreign direct investment would flow into Taiwan once the FHCL was passed.\textsuperscript{41}

Apart from the law’s potential to help banks build scale and scope and attract additional foreign direct investment into Taiwan, thereby boosting economic performance and strengthening the DPP’s electoral fortunes in the upcoming Legislative Yuan elections in late 2001, President Chen and his Cabinet also pursued other goals with the legislation. In particular, a need to prove its economic policy credentials also seems to have contributed to the executive’s support for the FHCL.\textsuperscript{42}

After the DPP came to power in 2000, Chu argued that:

"From the perspective of democratic governance, the Democratic Progressive Party has come to power probably before its time. [...] In terms of its mentality, organizational ability, and administrative experience, the DPP is not fully prepared to take over."\textsuperscript{43}

When the economic crisis unfolded in the years 2000 and 2001, the DPP administration realized it had to shore up its economic policy credentials and mend relations with the business community. The FHCL, constituting an integral part of the overall financial reform program, acted as a ‘signal’ to the business community that the newly elected government after all was worthy of support – as well as future

\textsuperscript{37} Asmus, Brian, “Financial holding companies spur consolidation drive”, \textit{Taiwan Business Topics}, October 2003.

\textsuperscript{38} Gilley, Bruce, “Banking on buddies”, \textit{Far Eastern Economic Review}, November 13\textsuperscript{th}, 1997.

\textsuperscript{39} Interview ‘6’ in Taipei.


\textsuperscript{41} Lin, Kun-Hui, “Minister predicts US$5b investment if bills passed”, \textit{Taiwan News}, June 14\textsuperscript{th}, 2001.

\textsuperscript{42} Interviews ‘2’ and ‘4’ in Taipei and London.

\textsuperscript{43} Chu, “Democratic Consolidation in the Post-KMT Era”, p. 89.
campaign finance. Obviously, the FHCL could only win support from the local banking community if the latter actually favored bank business scope regulatory reform. As will be seen below, the financial sector in fact welcomed the law.

Foreign bank pressure to pass the FHCL also shaped the executive’s assessment. Foreign banks in 2001 occupied a small but lucrative niche in Taiwan: Whereas the market share of the 38 foreign banks at the time was under 3% in terms of deposits and loans, foreign banks averaged a relatively high 0.9% return on assets and a 23.1% return on equity. Foreign banks hence favored and lobbied for the potential opportunity to expand their business scope via the FHCL. Illustrating this sentiment, American Chamber of Commerce President Peter Banko (also Taiwan manager of Bank of America at the time) approvingly noted in 2001 that ‘financial reforms recently initiated by the government proved that Chen was committed to revitalizing the island’s ailing banking sector’.

The intention behind this praise for the President was obvious: Foreign bankers welcomed the increased flexibility associated with the FHCL, as it allowed them to fully leverage their parent institutions’ business model in the Taiwanese context. President Chen encountered further foreign pressure for passage of the FHCL on a trip to New York in May 2001: Bankers from Goldman Sachs, Merrill Lynch and Morgan Stanley ‘expressed their wish that Taiwan’s FHCL be passed as soon as possible to open the door to American FHCs’. European financial services senior executives also directly lobbied for passage of the FHCL.

Overall, then, Taiwan’s executive viewed the FHCL positively, as they expected it to help the local banking sector as well as satisfy private sector demands for liberalization.

3.2. Financial Bureaucrats

Regarding financial bureaucrats’ assessment of the FHCL, news sources and interviews with high-ranking employees of the Ministry of Finance’s (and later the Financial Supervisory Commission’s) Bureau of Monetary Affairs in 2001 reveal that the deregulation of banks’ business scope was favored by Taiwanese regulators.

A director of the Bureau of Monetary Affairs stated in an interview in June 2001 that:

“With the FHCL, it was our goal to aid local banks deal with the twin problems of market fragmentation and credit disintermediation by allowing them to broaden their business scope.”

Thus, to retain their reputation as competent regulators, officials in the Bureau of Monetary Affairs embraced the FHCL, beginning preparations for the law in early 2000. Regulators also pushed the new law forward because they hoped to achieve greater transparency of local business groups’ financial sector activities. Tsai Ching-
Nien, deputy director general of the Bureau of Monetary Affairs at the time, put it as follows:

“After the FHCL is passed and promulgated, [local] financial groups would have to convert themselves to FHCs. [That] would clarify the relationship between the headquarters and subsidiaries of these financial groups and regulatory supervision between agencies and these financial groups.”

As will be seen in the discussion of financial sector players’ stance on the FHCL below, Taiwanese business conglomerates already operated a range of financial subsidiaries even before the FHCL was passed, though these were not integrated in a single legal entity. Given the often opaque nature of these operations, regulators reasoned that their formal restructuring within a FHC would aid transparency. Improved transparency, in turn, was expected to facilitate successful regulation and supervision and thus boost Bureau of Monetary Affairs bureaucrats’ career prospects.

A major organizational change occurred within the financial sector regulatory apparatus after the FHCL was adopted. Before the FHCL and associated legislation was passed, regulators for different financial services had been organized in separate divisions under the Ministry of Finance. Following the FHCL, this structure was replaced in 2004 with an integrated regulator, the Financial Supervisory Commission. In the light of the Financial Supervisory Commission’s optimistic assessment of its own expanded role as an integrated regulator, it became obvious that the FHCL was favored by bureaucrats for two reasons: First, it promised better bank and economic performance in the short-run. Second, improved financial sector transparency was seen as leading to a long-term upgrade of regulatory capabilities and performance.

While regulators thus supported the law, they also succeeded in conveying their views to decision-makers. Expecting substantial reputational pay-offs, financial bureaucrats used their input function in the law drafting process to promote the FHCL. With the executive and financial bureaucrats decidedly in favor of the law from the beginning, what explains the shift in sentiment on behalf of legislators alluded to above?

3.3. Legislators

For understanding legislators’ assessment of the FHCL, one first of all has to outline the composition of parliament in June 2001. At the time, altogether five major parties were holding seats in the Legislative Yuan, apart from a number of minor parties and independent candidates. The opposition KMT, together with the People First Party and the New Party, accounted for over 60 per cent of seats, while the DPP held 30 percent.

Initially, it seemed in June 2001 that the ‘pan-blue’ camp would exploit its leverage and deny the DPP passage of the FHCL. On the 6th of June 2001, the Legislative Yuan session came to an end, with over 100 legislative initiatives, including the FHCL, not having been passed, meaning that their adoption was delayed until at least September 2001. Nevertheless, facing intense media pressure over the impasse,
opposition parties agreed to a request by President Chen Shui-Bian to hold a ‘special legislative session’ focusing on financial reform initiatives. During the two-day special session on June 26th and 27th, 2001, the FHCL, together with five pieces of related legislation, was finally adopted by a cross-party majority.

While the opposition parties’ behavior in the legislature – contributing to initial failure to adopt the FHCL but subsequently passing it jointly with the DPP - may appear confusing, their assessment of the FHCL was actually quite straightforward throughout. A majority of ‘pan-blue’ legislators favored the law from the beginning. On the 5th of June 2001, just before the parliamentary stalemate, the Taiwan News for example reported that:

“More than 100 bills [...] are stacked up awaiting passage as the current legislative session comes to an end. [...] Ruling and opposition parties [however] have an initial consensus on passing a financial holding company law because it helps to attract foreign investors.”

Financial sector professionals in Taipei, who were close to the legislative process at the time and were interviewed for this study, supported this analysis. From their point of view, all major parties were in favor of the FHCL, due to the promise it held for boosting the banking sector’s and overall economy’s performance. Indeed, one interview partner pointed out that deliberation on introducing integrated financial services provision had already begun under the last KMT presidency. In particular, a Financial Reform Task Force in 1998 had advocated the removal of barriers between commercial and investment banking. Given this analysis, what explains the opposition’s contradictory legislative behavior?

The answer to this question appears to be that the opposition attempted to block the FHCL for a time precisely because it exhibited such positive potential. Fearing that the quick adoption of the law would allow the DPP to benefit from improved economic conditions in the year-end Legislative Yuan elections, ‘pan-blue’ legislators tried to delay or even kill the initiative. However, in June 2001 media reports began to focus the public’s attention on the opposition’s maneuvering. For example, the Taipei Times complained in an editorial that unless the FHCL was passed, ‘the interests of the people of Taiwan’ would not be served. Similarly, The China Post ran an editorial in June 2001 calling for the adoption of the FHCL as it was ‘vitaly important to boosting the economy’. Another editorial published by The China Post in the same month stated that the FHCL would allow Taiwanese financial institutions ‘to become healthier and more efficient, and this in turn should aid economic growth in the year ahead and beyond’. The third major English language local newspaper, the Taiwan News, did not diverge from this assessment by proclaiming in a June 2001 editorial entitled “Urgent finance laws must not drag on”

---

56 Chen, “Chen signs request”.
61 Lee, The Development of Banking in Taiwan, p. 31.
63 Ibid.
64 “Priority must be given to key financial bills”, The China Post, June 15th, 2001.
that ‘effective financial reform [including the FHCL] greatly affects Taiwan’s economic development and cannot afford to fail’.

Suddenly, the opposition’s strategy threatened to backfire as voters might in the future turn away from the ‘pan-blue’ camp due to its disregard for Taiwan’s interest. With this scenario increasingly looming on the horizon, the KMT, People First Party and New Party leaders gave in and adopted the FHCL in the ‘special session’.

A few other factors contributed to the initial delay in adopting the FHCL, including parliamentary infighting over ‘pork barrel’ bills proposed by the KMT and DPP calculations that not passing the law would actually be beneficial too as it could be blamed on the ‘pan-blue’ opposition. Still, the main explanation for what happened at the time offered in the previous paragraphs is supported by the fact that the eventual adoption of the FHCL in late June 2001 was tied to a ‘sunrise clause’, after intensive pressure by opposition lawmakers for such an amendment. The latter meant that the law was to take effect only as late as November 1st, 2001, ostensibly to allow for proper arrangements regarding FHC regulation and supervision to be drawn up (FHCs were to be monitored by an integrated regulator as seen above). In practice, the amendment was designed to deny the DPP the chance of benefiting from an economic upswing as a result of the FHCL in the December 2001 parliamentary elections.

Foreign and domestic bank pressure on legislators presumably also contributed to their positive assessment of the FHCL. Given foreign banks’ interest in the law, it is safe to assume that legislators were the target of foreign bank lobbying efforts via lobbying bodies such as the American Chamber of Commerce. Moreover, particularly in the case of the KMT, (ownership) links to powerful business groups that supported the FHCL also shaped legislators’ positive view of the law, as the FHCL promised to lift the value of the KMT’s ownership stakes.

Therefore, legislators in Taiwan, whether they belonged to the DPP, KMT, People First Party or New Party, consistently viewed the FHCL positively, as it would aid troubled local banks. Fearing that a performance boost for banks in particular and the economy in general would favor the DPP in the year-end Legislative Yuan elections, the ‘pan-blue’ camp attempted to exploit its majority in the legislature to stop the law. Nevertheless, in the end, the societal consensus in 2001 that the FHCL would benefit Taiwan, which was forcefully advocated by the mass media, made it essential for the opposition to give in. In the case of the FHCL, therefore, mass media pressure proved capable of forcing a policy consensus onto a ‘divided government’.

---

67 For a selection of June 2001 newspaper editorials that stressed the importance of the FHCL for Taiwan, see the discussion above.
68 For ‘pork barrel’ bill controversies related to the initial delay in passing the FHCL see for example “What contributed to lawmaking inefficiency”, The China Post, June 8th, 2001. For allegations that the DPP itself tried to delay the FHCL to then blame the impasse on the opposition see “Speaker Wang denies stalling tactics in legislative meeting”, The China Post, June 6th, 2001.
69 “New financial bills expected to solve woes”.
70 “No cheers”.

14 SOAS, University of London

4.1. The Financial Sector

Other countries’ experience with liberalizing commercial banks’ business scope shows that such a policy move is likely to imply significant lobbying activity by commercial banks (who favor deregulation) as well as investment banks and insurance companies (who are opposed to it).\(^{71}\) In the case of Taiwan, commercial banks were indeed very supportive of the law.\(^{72}\) Interestingly, however, neither interviews nor news sources revealed significant contrary lobbying activities by investment banks and insurance firms prior to the passage of the FHCL in 2001. What explains this situation?

The attraction of the FHCL in the eyes of Taiwanese commercial banks is easily understood: While regulatory restrictions prevented banks from readjusting their business model, a number of factors combined in the 1990s to make the local banking market relatively unprofitable. Firstly, entry by private banks in the early 1990s had led to market fragmentation and overbanking, implying a structural impediment to healthy profits. Secondly, in the 1990s credit disintermediation began to affect Taiwan. Increasingly, the largest Taiwanese corporations were relying on direct methods of financing. Thirdly, since the late 1980s Taiwanese companies had become more international, due to two factors: While Taiwanese manufacturing firms in search of cheaper production locations relocated operations to South-East Asia and/or mainland China, a number of high-tech companies also expanded overseas in search of higher-margin, brand-based business.\(^{73}\)

Outflows of foreign direct investment are one way to illustrate this trend. Figure 2 shows how outbound Taiwanese foreign direct investment soared from negligible levels to an average of about 4.1 billion United States dollars a year between 1988 and 2001. As reported by numerous authors, actual outflows, especially to mainland China, were presumably even higher, with one report, for example, putting the overall figure for Taiwanese investment in mainland China (realized plus contracted foreign directed investment) as high as 100 billion United States dollars in 2000.\(^{74}\)

(Insert Figure 2 here)

Given that Taiwanese companies’ overseas expansion required the kind of integrated financial solutions that only commercial banks with a broad business scope can offer, the internationalization of Taiwanese companies in the 1990s exacerbated

---

71 See, for example, reference in footnote 12 above.

72 In the following discussion, the terms ‘commercial banks’, ‘investment banks’ and ‘insurance companies’ denote these institutions’ owners, managers as well as other employees. Supposedly, the interests of these different company stakeholders are all largely aligned, as the main challenge of any financial sector subgroup is to increase its share of, or defend its ‘spoils’ against, potential competitors. The approach presented here thus represents a ‘sectoral’ analysis of political competition (different economic sectors compete for influence) and not a ‘class-based’ analysis (classes such as ‘capitalists’ and ‘workers’ compete for influence). See Frieden, Jeffry A., “Invested Interests: The Politics of National Economic Policies in a World of Global Finance”, *International Organization*, Vol. 45, No. 4 (1991), p. 438.

73 Interviews ‘2’ and ‘3’ in Taipei.

the problems with the traditional business model of Taiwanese lenders. Integrated financial services providers from the United States, Japan and Western Europe emerged as a real threat to Taiwanese banks, capable of winning over the latter’s most profitable corporate clients. This issue was particularly acute when Taiwanese companies set-up operations in mainland China, since Taiwanese banks were not allowed to follow them there.

Consequently, caught between regulatory restrictions, market fragmentation, credit disintermediation and the internationalization of their corporate customers, commercial banks – whether publicly or privately owned – were very supportive of the FHCL as it allowed them to increase their operating scale and broaden their business scope.75

Commercial banks were also keen on two other advantages associated with the FHCL: Firstly, tax advantages followed from provisions of the FHCL that offered the possibility to offset profits in one FHC subsidiary by losses in another.76 Secondly, in contrast to previous regulations, the FHCL also allowed financial institutions complete ownership of banks.

Given the inefficiencies of the old regulatory structure, commercial banks pushed for the adoption of the FHCL. For example, the lobbying association of Taiwanese commercial banks, the Bankers Association of the Republic of China, strongly voiced its approval for the FHCL.77 Influence over regulatory decision-makers was also secured via other channels. In the case of publicly owned banks, connections to the government had traditionally been strong, as bankers were essentially civil servants.78 Regarding privately owned commercial banks, access to policy-making was facilitated by the rising importance of family-owned conglomerates in the Taiwanese economy. Recently, these ‘guanxiqiye’ or ‘related enterprise groups’ (Fields 1995, 63; Hamilton 1997, 259) have accounted for a significant and, especially in services, rising part of overall gross domestic product (Amsden 2003).79 The new commercial banks that entered the market in the early 1990s provide the most obvious example in this respect: All new entrants were owned by powerful local business conglomerates.80

Over the years, the families that controlled the conglomerates had managed to build up close connections with the executive and legislature, despite their often ‘Taiwanese’ background and initial distance from the former KMT dominated government.81 Given their increasing importance to the Taiwanese economy, such an outcome was hardly surprising: For instance, the top 100 Taiwanese conglomerates’ sales were equivalent to 8.3% of gross domestic product in 1998, as opposed to 4.6% in 1981.82 Clearly, their importance – and thus their potential access to and influence over policy-making - had been rising significantly since the early 1980s.

---

77 See the Association’s website: http://www.ba.org.tw/english043.asp.
82 Amsden, Beyond Late Development, p. 121.
Drawing on these connections to the government, Taiwanese conglomerates were thus ensured significant access to decision-makers in the financial regulatory process. For a start, benefits such as campaign finance had appeal to politicians of all parties. Moreover, KMT legislators in particular may have been responsive to demands by business conglomerates to pass the FHCL: Since the KMT owned equity stakes in financial conglomerates itself, it could hope for higher valuations of these shareholdings after the FHCL’s passage.

While commercial banks thus exerted pressure on the executive and legislature to pass the FHCL, opposition to banking scope deregulation from investment banks and insurance firms did not materialize. The cause of this surprising lack of opposition is related to the ownership structure of the Taiwanese investment banking and insurance sectors. Crucially, one of the sectors Taiwanese business conglomerates expanded into during the 1990s was the financial services industry. Taking advantage of financial liberalization initiatives, they established and/or acquired commercial banks, companies active in the capital and money markets as well as insurance firms.

As seen above, virtually all new banks licensed in the early 1990s had connections with family-owned conglomerates. While not as extreme, the ownership pattern in investment banking and life and non-life insurance firms was similar to the one found in commercial banking: Some ‘independent’ firms (without conglomerate connections) existed in the 1990s but often the most important firms were controlled by business conglomerates. Out of the eight Taiwanese investment and trust companies (investment banks) that were opened since 1971, four were wholly or partly owned by the KMT and the remaining four were owned by private related enterprise groups. In the case of securities and insurance companies, evidence similarly points to significant involvement by business groups.

Hence, it is clear that during the 1990s Taiwanese business conglomerates were operating subsidiaries in all kinds of financial business lines. In fact, many of the most important business conglomerates that operated financial subsidiaries in the 1990s did so across almost the entire range of financial services, implying the existence of ‘virtual financial holding companies’ even before 2001. The Taipei Times noted that out of the 27 conglomerates that were active in financial services before the FHCL was passed, 11 were active in commercial banking, investment banking and insurance, while 16 were operating in two out of the three business lines. For (financial) conglomerates such as Linyuan Group/Cathay or Fubon, the FHCL offered the valuable option of integrating their already existing financial holdings. In addition, conglomerates were keen to exploit the tax advantages and lifting of ownership restrictions that were associated with FHCs.

---

83 Interview ‘2’ in Taipei.
84 For the KMT’s involvement in Taiwanese corporations see, for example, “The long arm of the KMT”, The Economist, June 13th, 1998.
85 Amsden, Beyond Late Development, p. 124.
86 Fields, Enterprise and the State, p. 154.
87 While comprehensive ownership data is difficult to obtain due to the often secretive nature of Taiwanese conglomerates, a number of analysts confirm the involvement of family-owned groups in the investment banking and insurance businesses. See, for example, Amsden, Beyond Late Development, pp. 135, 155, 158. Also Chen, Kevin and Lin, Jackey, “Tsai led family to dominate nation’s finance business”, Taipei Times, September 29th, 2004. Flannery, Russell, “Why Sandy Weill chose Fubon’s Daniel and Richard Tsai to build a financial supermarket in Asia”, Forbes, May 28th, 2001.
89 Namgyal, “New law to help”.
Given these benefits, private business groups with financial interests were strongly in favor of banking scope deregulation.\textsuperscript{90} In the words of one Taiwanese FHC executive interviewed for this paper:

"Business conglomerates, especially, were in favor of the law. For example, our company already was a virtual financial holding company before the law was passed. Therefore, we benefited a lot from the law."\textsuperscript{91}

Of course such support implied that there was no resistance to the FHCL from investment banks and insurance companies that were affiliated with financial conglomerates. Furthermore, it appears that ‘independent’ companies in these business lines also did not voice any strong opposition – the large, ‘independent’ investment banks and insurers presumably viewed the FHCL as a welcome chance to expand their own business\textsuperscript{92}, while the smaller players did not have sufficient lobbying resources at their disposal to oppose the law. Thus, not only did commercial banks favor the law, but a majority of the investment banks and insurance firms in the financial system also did not oppose it.

4.2. Customers
Since FHCs can offer their corporate customers integrated ‘solutions banking’, thereby lowering search and transaction costs for clients\textsuperscript{93}, wholesale Taiwanese bank customers generally favored the law. Given the increasing internationalization and financial sophistication of Taiwanese manufacturers, the latter were supportive of a legislative initiative that allowed for the gradual replacement of traditional intermediaries by modern integrated FHCs.

Illustrating this sentiment, the chief financial officer of a Taiwanese high-tech company stated that:

"Local banks rarely understand my industry. [...] At any one time I have 15 banks offering me loans, but what I need are solutions. [...] No one is providing the integrated services and real industry insights that I need to grow my business."\textsuperscript{94}

Concerning retail customers, lower search and transaction costs for financial services similarly served as an inducement to embrace the FHCL.\textsuperscript{95} Moreover, the support of retail (and wholesale) customers for the FHCL was secured by putting in place relevant legal safeguards for consumer protection. For example, the FHCL ‘firewalls’ aimed at safeguarding confidential customer information helped to reassure retail and corporate bank clients about the law.\textsuperscript{96}

Given the advantages the FHCL potentially offered bank customers over the old regulatory framework, the latter generally approved of the law. Nevertheless, since bank customers represent a dispersed interest group with little direct access to

\textsuperscript{91} Interview ‘11’ in London.
\textsuperscript{92} Chou, Stanley, “Holding law passage imminent”, \textit{Taipei Times}, February 9\textsuperscript{th}, 2001.
\textsuperscript{94} Bowers, Tab, Gibb, Greg, Wong, Jeffrey, \textit{Banking in Asia}, p. 129.
\textsuperscript{95} Yang, Ya-Hwei, “Tackling the money pit with care”, \textit{Taipei Times}, November 7\textsuperscript{th}, 2001, p.8.
\textsuperscript{96} \textit{Ibid.}
decision-makers\textsuperscript{97}, their overall approval of the FHCL may have been more of a permissive condition for the law’s adoption, rather than a distinct, powerful driving force behind it.

5. AN ASSESSMENT OF THE FHCL’S IMPACT AND CONCLUDING REMARKS

Table 3 below provides a brief summary of the size, profitability and business activities of the FHCs that have come into existence in Taiwan since late 2001.

(Insert Table 3 here)

The 14 companies in the table together accounted for about 45\% of all Taiwanese financial market assets in 2004.\textsuperscript{98} The biggest 10 firms achieved an average return on equity of 13.6\%, which compared favorably to a financial industry-wide average return on equity of about 9.6\% in 2004.\textsuperscript{99} 11 of the 14 FHCs were active across the entire spectrum of financial services, including commercial banking, investment banking and insurance, while the remaining 3 were more focused.

Mergers and acquisitions activity in the market has meant movement towards the goals the Taiwanese government vowed to achieve with the FHCL: A number of relatively small banks such as Cathay and Fubon, for instance, built scale by utilizing their parent FHC’s strong balance sheets to acquire banking competitors that would previously have been out of reach. Alternatively, to build scope, banks that did not hold a securities underwriting license before acquired securities firms that could act as underwriters (for example China Development). Finally, other commercial banks that already held underwriting licences broadened their fee-based product offerings by acquiring securities firms and insurance companies (for instance Mega).\textsuperscript{100}

On the whole, recent financial sector mergers and acquisitions have resulted in a Taiwanese financial market in general and banking sector in particular that is still comparatively fragmented but now includes 14 FHCs that can serve as ‘anchor institutions’ for further consolidation activities. While successful Taiwanese banking sector reform thus has certainly not been completed, the FHCL brought definite, positive change to the Taiwanese banking landscape, where the 10 largest banks now achieve decidedly greater scale and returns than in 2001.\textsuperscript{101}

By adopting the 2001 FHCL, Taiwan followed a global, United States-led shift towards a more liberal regulation of bank activities by those countries that had previously separated commercial banking from investment banking and insurance activities (the People’s Republic of China, incidentally, remains one of the few countries that maintain such a separation).

The analysis provided here yields two important conclusions regarding Taiwan’s current political economy: Firstly, even under a situation of ‘divided

\textsuperscript{97} Large corporate customers may be an exception to this point.
\textsuperscript{98} Huang, Joyce, “Integration seen as worry for FHCs”, \textit{Taipei Times}, November 18\textsuperscript{th}, 2004.
\textsuperscript{99} Compare data at \url{http://www.boma.gov.tw/ct.asp?xItem=32339&ctNode=704}.
\textsuperscript{100} Information in this paragraph is from company annual reports, available from company websites.
\textsuperscript{101} For remaining problems in the Taiwanese banking system see “Folly by numbers”, \textit{The Economist}, November 26\textsuperscript{th}, 2005. For increasing scale and returns among the top-10 Taiwanese commercial banks in 2005 compare data at \url{http://www.banking.gov.tw/lp.asp?ctNode=1991&ctUnit=537&BaseDSD=7} as well as “Folly by numbers”, \textit{The Economist}, November 26\textsuperscript{th}, 2005 and Chung, Amber, “Mega Financial to acquire smaller bank”, \textit{Taipei Times}, December 17\textsuperscript{th}, 2005.
government’ which offers political opponents the opportunity and incentives to block legislative initiatives even if these appear beneficial to the population as a whole, important policy measures can be passed. In the case of the FHCL, the key factor that broke the deadlock between the DPP executive and ‘pan-blue’ dominated Legislative Yuan appears to have been the intense media pressure that policy-makers, in the end, could not afford to disregard if they did not want to tarnish their (parties’) reputation in the long-run. The pressure that Taiwan’s emerging civil society can potentially exert on policy-makers thus appears capable of making up for institutional ‘failings’ that undermine good governance.\footnote{Fell also makes this point for the ‘failing’ of corruption. See Fell, Dafydd, “Political and Media Liberalization and Political Corruption in Taiwan”, \textit{China Quarterly}, Vol. 184 (2005).}

Secondly, regarding the increasing scope for private sector lobbying afforded by Taiwan’s now democratized polity, the passage of the FHCL shows that such pressure does not have to contribute to political stalemate via attempts to further narrowly defined private interests. Indeed, the pressure that Taiwanese commercial banks and ‘virtual’ FHC brought to bear on policy-makers in the executive and legislature alike for passing the FHCL in 2001 seems to have helped along the adoption of a law that, if not perfect, will certainly enable Taiwan’s banking sector to move a step closer towards a more competitive configuration. Thus, Taiwan’s interest groups in the financial sector appear to have done their environment a favor by lobbying for the adoption of the FHCL, after deciding that the latter would bolster their own, private position. Hence, the increasing potential for interest group involvement in policy-making that modern day Taiwan’s political economy allows cannot, a priori, be labeled a ‘threat’ to effective governance: ‘Benign capture’, it seems, can support the remnants of the ‘autonomous’ Taiwanese policy-making apparatus in pursuing welfare enhancing change.

The case of Taiwan’s FHCL serves to show that democratization and effective governance do not need to be inversely related: Given certain conditions, a democratized polity may in fact contribute positively to coherent policy-making. This appears a valuable lesson and hopeful example for other, newly democratized countries.

\textbf{APPENDIX: Interview Details}

<table>
<thead>
<tr>
<th>Interview Number</th>
<th>Date (2005)</th>
<th>Location</th>
<th>Interviewee</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>April 8\textsuperscript{th}</td>
<td>Taipei</td>
<td>Chief country officer, a German bank</td>
</tr>
<tr>
<td>2</td>
<td>April 12\textsuperscript{nd}</td>
<td>Taipei</td>
<td>Professor, National Taiwan University</td>
</tr>
<tr>
<td>3</td>
<td>April 13\textsuperscript{th}</td>
<td>Taipei</td>
<td>Chief country officer, a French bank</td>
</tr>
<tr>
<td>4</td>
<td>May 23\textsuperscript{rd}</td>
<td>London (via phone)</td>
<td>Project leader, an American management consultancy</td>
</tr>
<tr>
<td>5</td>
<td>June 14\textsuperscript{th}</td>
<td>Taipei</td>
<td>Head of Research, an Asian investment bank</td>
</tr>
<tr>
<td>6</td>
<td>June 20\textsuperscript{th}</td>
<td>Taipei</td>
<td>Director, Bureau of Monetary Affairs</td>
</tr>
<tr>
<td>7</td>
<td>June 21\textsuperscript{st}</td>
<td>Taipei</td>
<td>Chief executive, a British bank</td>
</tr>
<tr>
<td>8</td>
<td>June 22\textsuperscript{nd}</td>
<td>Taipei</td>
<td>Chief representative, a Swiss bank</td>
</tr>
<tr>
<td>9</td>
<td>June 23\textsuperscript{rd}</td>
<td>Taipei</td>
<td>Director, Bureau of Monetary Affairs</td>
</tr>
<tr>
<td>10</td>
<td>June 25\textsuperscript{th}</td>
<td>Taipei</td>
<td>Chief representative, a German bank</td>
</tr>
<tr>
<td>11</td>
<td>June 27\textsuperscript{th}</td>
<td>London (via email)</td>
<td>Public relations executive, Taiwanese FHC</td>
</tr>
<tr>
<td>12</td>
<td>December 19\textsuperscript{th}</td>
<td>London (via email)</td>
<td>Project manager, Taiwanese FHC</td>
</tr>
</tbody>
</table>
NOTES

Table 1: Taiwan’s formal financial system: major markets and participants

<table>
<thead>
<tr>
<th>Major participants</th>
<th>Commercial banking market</th>
<th>Capital and money Markets</th>
<th>Insurance market</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Government-, private- and foreign-owned commercial banks</td>
<td>• Investment and trust companies (since 1971)</td>
<td>• Life and non-life insurance companies</td>
<td></td>
</tr>
<tr>
<td>• Cooperative banks</td>
<td>• Securities and brokerage companies</td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Postal Savings System</td>
<td>• Securities finance and bills finance companies</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


Table 2: Bank market concentration, average returns on assets and on equity in the banking industry of selected East- and South-East Asian economies in 2001

<table>
<thead>
<tr>
<th>Bank market concentration</th>
<th>Average return on assets**</th>
<th>Average return on equity**</th>
</tr>
</thead>
<tbody>
<tr>
<td>Singapore</td>
<td>2906</td>
<td>1.49</td>
</tr>
<tr>
<td>Thailand</td>
<td>1044</td>
<td>2.80</td>
</tr>
<tr>
<td>Indonesia</td>
<td>983</td>
<td>0.71</td>
</tr>
<tr>
<td>Hong Kong</td>
<td>968</td>
<td>1.47</td>
</tr>
<tr>
<td>Malaysia</td>
<td>899</td>
<td>1.24</td>
</tr>
<tr>
<td>Philippines</td>
<td>776</td>
<td>0.48</td>
</tr>
<tr>
<td>Taiwan</td>
<td>524</td>
<td>0.49</td>
</tr>
</tbody>
</table>

Note: * In terms of assets as measured by Herfindahl-Hirschman Index. Values > 1800 indicate a highly concentrated market structure. ** Unweighted average for 10 largest commercial banks.


Table 3: The 14 Taiwanese Financial Holding Companies in 2004

| Company       | Assets (New Taiwan billion) | Return on capital (%) | Business lines | | | |
|---------------|------------------------------|-----------------------|----------------|----------------|----------------|----------------|----------------|----------------|
|              |                              |                       | Commercial Banking | Investment banking | Insurance |
| Cathay       | 2,650                        | 17.0                  | X               | X               | X              |
| Mega         | 2,120                        | 13.6                  | X               | X               | X              |
| Hua Nan      | 1,600                        | 14.2                  | X               | X               | X              |
| Fubon        | 1,510                        | 9.9                   | X               | X               | X              |
| First        | 1,500                        | 14.1                  | X               | X               | X              |
| Chinatrust   | 1,430                        | 17.2                  | X               | X               | X**            |
| Shin Kong    | 931                          | 13.7                  | X               | X               | X              |
| Tai Shin     | 865                          | 16.2                  | X               | X               |                |
| Sinopac      | 595                          | 9.0                   | X               | X               | X              |
| E.Sun        | 498                          | 11.4                  | X               | X               | X**            |
| Fu Hwa*      | 312                          | 7.1                   | X               | X               | X              |
| China Development | 260          | -4.0                  | X               | X               |                |
| Jih Sun*     | 130                          | -1.6                  | X               | X               | X              |
| Waterland    | NA                           | NA                    | NA              | NA              | X              |

Note: * 2003. ** Insurance brokerage.

Source: Based on annual reports available from company websites. Figures are rounded.
Figure 1: Sources of funds in the non-financial sector in Taiwan, 1990-2001


Figure 2: Outflows of Taiwanese direct investment between 1984 and 2001

Source: 
Bibliography (Special Appendix For Referees Only)

Amsden, Alice H., Beyond Late Development: Taiwan’s Upgrading Policies (Cambridge: Massachusetts Institute of Technology Press, 2003)


Bowers, Tab, Gibb, Greg, Wong, Jeffrey, Banking in Asia: Acquiring a Profit Mindset (Singapore: John Wiley & Sons, 2003)

Canals, Jordi, Universal Banking: International Comparisons and Theoretical Perspectives (Oxford: Oxford University Press, 1997)


Fields, Karl J., Enterprise and the State in Korea and Taiwan (Ithaca: Cornell University Press, 1995)


