

# Taiwan Business Forecast Report Q1 2015

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## Abstracts

### Core Views

Although exports rebounded sharply in Q314, weak global demand will pose increasing headwinds in 2015. Given Taiwan's over-dependence on exports, this will be a key risk for the economy going forward. On the political front, we expect Taiwan's political deadlock to persist beyond the November 29, 2014 local elections, as both the ruling Kuomintang party and opposition Democratic Progressive Party struggle to overcome internal divisions. Despite the KMT's weakness, the DPP is failing to offer itself as a credible alternative to the KMT.

In line with our expectations, the Central Bank of the Republic of China (Taiwan) (CBC) held its discount rate at 1.875% during its monetary policy meeting on September 25. We forecast interest rates to remain on hold until Q215 as the CBC focuses on maintaining growth as export orders have slowed and inflation should remain manageable.

Taiwan's proposed 2015 budget suggests that the government's failure to significantly curb expenditures will result in a persistent budget deficit despite new revenue streams from increased taxes. We forecast the government's budget deficit in 2015 to rise slightly to 1.8% of GDP before stabilising over the next few years. We expect the TWD to remain stable, ending 2014 at TWD30.00/USD and appreciating slightly to end 2015 at TWD29.50/USD. Taiwan's large current account surplus, high levels of foreign reserves, low inflation and relatively strong economic growth should provide support for the currency, even as its main trading partners experience currency weakness.

### Major Forecast Changes

Our expectations for slower growth in Taiwan's economy following Q314 figures have

prompted us to revise our forecast for 2015 downwards from 4.1% to 3.5, while maintaining our below consensus forecast for 3.1% real GDP growth in 2014. Weak global demand will pose increasing headwinds in 2015. Given Taiwan's over-dependence on exports, this will be a key risk for the economy going forward.

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Domestic Gridlock Will Persist Beyond Local Elections

Taiwan's political deadlock will persist beyond the November 29, 2014 local elections, as both the ruling Kuomintang (KMT) party and opposition Democratic Progressive Party (DPP) struggle to overcome internal divisions. Despite the KMT's weakness, the DPP is failing to offer itself as a credible alternative to the KMT.

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Taiwan's long-term political prospects are inseparable from its relations with China, and while cross-Strait relations have thawed in recent years, we believe the status quo will largely prevail. While further economic integration is likely between the two Chinas, we exclude meaningful political convergence. Meanwhile, Taiwan is extremely unlikely to regain internationally recognised independence. As a result, we believe Taiwan will remain in a political no-man's land - with this being the least worst path for political stability.

### **CHAPTER 2: ECONOMIC OUTLOOK**

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Our expectations for slower growth in Taiwan's economy following Q314 figures have prompted us to revise our forecast for 2015 downwards from 4.1% to 3.5%, while maintaining our below consensus forecast for 3.1% real GDP growth in 2014. Although exports rebounded sharply in Q314, weak global demand will pose increasing headwinds in 2015. Given Taiwan's over-dependence on exports, this will be a key risk

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In line with our expectations, the Central Bank of the Republic of China (Taiwan) (CBC) held its discount rate at 1.875% during its monetary policy meeting on September 25. We forecast interest rates to remain on hold until Q215 as the CBC focuses on maintaining growth as export orders have slowed and inflation should remain manageable.

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