

Taiwan central bank hikes by 12.5bp

Taiwan's central bank has raised the discount rate by 12.5bp to 1.5% in an attempt to curb inflation pressure. We expect the rate hikes to continue in Taiwan in the second half of this year. Due to the higher inflation threat, we are downgrading our GDP forecast for 2022



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Taiwan's rate hikes continue but this one is mild compared to the Fed's

Taiwan has increased its policy rate for the second time this year. This hike of 12.5bp is smaller than the previous 25bp hike in March. The central bank continued to point to inflation as the big threat to growth and the main reason behind the rate hike.

Looking at Taiwan's CPI inflation rate in relation to other major economies, Taiwan's rate is moderate at 3.39% year-on-year in May, while the US, UK, and eurozone CPI inflation rates range between 8% and 9%. This also explains the smaller hike by Taiwan's central bank.

The central bank also increased the reserves ratio by 0.25 percentage points, which should have little impact on short-term borrowing costs, and therefore overall interest rates in Taiwan in the short term. SO we may not see a significant impact on TAIBOR in June from the increase in reserve ratio. The increase in reserve ratio should have a more long-term impact on interest rates, which should be reflected in 3Q22.

Taiwan economy may not withstand fast rate hikes

Taiwan's economy has a big growth engine of semiconductor manufacturing. This engine relies on consumer demand for smart devices, automobiles and other products that require semiconductor chips.

Mainland China is a big consumer market nowadays, and it has only just started to recover from Covid-19 lockdowns, and the risks of further isolated, shorter lockdowns continue to exist.

As such, Taiwan is facing higher inflation as well as a more uncertain market for its semiconductor sector. The economy may not be able to withstand a steep rate hike path.

We believe a slower rate hike path is more appropriate for Taiwan, and we expect two more 12.5bp hikes in 2H22 which should balance the risk of higher inflation and the uncertainty faced by the semiconductor sector.

We keep our forecasts for the policy discount rate at 1.75% by the end of 2022. At the same time, we revise our CPI inflation forecast higher which means lower real GDP growth at 3.84% for 2022.

Author

Iris Pang

Chief Economist, Greater China

iris.pang@asia.ing.com