

Taiwan: Central bank's surprising pause leads to a USD/TWD revision

Even in the face of weaker economic data, the central bank decided to stay put in June. As such, we are revising our USD/TWD forecasts for the rest of the year



Source: Shutterstock

Rate cut on hold even though the economy has weakened

Taiwan's central bank decided to put a rate cut on hold, and the policy rate remains at 1.125%. The consensus was for it to fall to 1%.

The decision came despite a continued rise in the unemployment rate to 4.1% and the economy being in deflation since February. CPI is currently at -1.19% year-on-year. Though industrial production in April was positive, at 3.5% YoY, it fell 7.4% month-on-month. Export orders also showed a 4.3% contraction on a monthly basis in April. This reflects the impact of Covid-19 on global demand.

Consumption data, meanwhile, showed that domestic demand has been affected by uncertainty in the job market. Retail sales fell 10.2% YoY in April and contracted 4.2% MoM. This suggests that people are not expecting jobs to come back quickly.

Exports and imports fell 2.0% YoY and 3.5% YoY, respectively, in May.

These numbers make it all the more surprising that the central bank decided to stay on hold.

One more rate cut is still in the cards

It is likely that the central bank is trying to buy some time in the hope that the economy, especially the export sector, will recover very soon. This is not impossible given that Taiwan's semiconductor industry has successfully filled the gap left by US technology companies.

But still, given that unemployment has been hit by Covid-19, and that cases worldwide do not seem to be subsiding quickly, Taiwan's central bank could still cut interest rates to 1% at the next policy meeting on 17 September.

Revising USD/TWD forecasts

We expect the Taiwan dollar to gradually strengthen against the US dollar given the central bank's latest decision. The USD/TWD spot rate is around 29.62. We expect it to be volatile when the next export data is released, as this could be worse than expected.

Our forecasts for USD/TWD are revised to 29.63, 29.65 and 29.60 for the end of 2Q20, 3Q20 and 4Q20, respectively.