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Snap

# Taiwan’s central bank cuts rates too

Taiwan has cut rates to 1.125% but we think more is to come. The fiscal stimulus should look to help the economy more directly rather than its current scattergun approach as the impact of the coronavirus has turned into a global demand issue that is likely to hurt the economy even post-Covid-19. As a result, we've lowered our TWD and GDP forecasts

## Taiwan cuts rates for the first time since 2016

Taiwan's central bank cut policy rates more aggressively than the market expected. The rate cut from 1.375% to 1.125% is deep, but in line what other central banks are doing around the world. This is the first move since 2016, and lower than the 1.25% we saw during the global financial crisis.

For the first time, the central bank has introduced a TWD 200 billion lending pool for small-medium enterprises for six months, which aims to help SMEs surf through the tide of Covid-19’s damage on operations, which should, in turn, stabilise the job market. In our view, this should be more effective than the fiscal stimulus planned by the government so far.

But we think the assumption that Taiwan needs low interest rate funding for a period of six months is quite optimistic.

Global demand has been hit and the recovery may be gradual if the job market is dismal even after Covid-19 subsides, which will subsequently lower demand for electronic products, e.g. smartphones, which are more of a luxury item than a necessity. Taiwan’s manufacturing and export demand will also be hit but this relief lending pool should help.

To prevent tight liquidity conditions, a liquidity injection of up to 180 days funding now includes banks, bills, postal, security firms, insurance companies.

## Fiscal stimulus could help SMEs

Taiwan has scaled up its fiscal stimulus from TWD60 billion, discussed on 27 February, to TWD100 billion on 18 March 2020. This is now equivalent to 0.5% of nominal GDP estimated by the government for 2020, up from 0.3% in late February. But the scale of this package is still smaller compared to other economies' stimulus, which is generally 2% or above GDP.

The smaller scale of fiscal stimulus could be explained by the unaffected manufacturing and export sector. But if we look ahead, many manufacturing economies are still battling with Covid-19, as their factory operations remain suspended.

### Revising USD/TWD forecast

Even though Taiwan is not slashing rates like the Federal Reserve, the TWD is going to be weaker against the USD because of the flight to safety to US Treasuries, and capital outflows from Taiwan's stock market.

We believe this flight to safety behaviour will last until Covid-19 subsides in the US and Europe and, in the meantime, we hope this does not lead to a global financial crisis that turns liquidity risks into credit risks.

Based on the above assumptions we revise our USD/TWD forecasts for the end of 1Q20 to 4Q20. These are 30.5, 31.00, 30.50 and 30.00, respectively.

### Another downgrade to Taiwan's GDP

We are a lot less optimistic than the government or the central bank on Taiwan's GDP growth for 2020. The rapid spread of Covid-19 will hit global demand for electronic products, which is Taiwan's main export item.

Moreover, the fiscal stimulus is too small to help SMEs and the job market if the global demand for electronic goods like smartphones continues to be persistently weak.

Therefore, we downgrade our forecast for Taiwan's GDP growth to -0.4% from 0.8% for 2020.

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