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TAIWAN LOOKS ALL SET TO THRIVE IN A POST-COVID WORLD

For our global fund, Taiwan has been an absolutely stellar performer in the past 10 months or so. And the reasons for our optimism about Taiwan are multifaceted, not in the least its exemplary handling of the coronavirus situation.

At a time when US Secretary of State Antony Blinken has hinted that Washington could send naval fleets to South China Sea in case of military escalation from China, a move unprecedented since the Taiwan Strait Crisis in 1954, heads of states globally are realizing just how dependent they have become on the island democracy as China continues to push the world to avoid official dealings with Taiwan, which it regards as a province.

Global demand for semiconductors, which are used in almost all electronics from phones to laptops and cars, increased dramatically with more people choosing to stay indoors. Along with South Korea, Taiwan controls roughly 80% of the semiconductor industry globally; in fact, Taiwan Semiconductor Manufacturing Company (TSMC) controls 50% of the global chip market.

Taiwan has created a massive industrial and technological silicon shield on the back of a multi-pronged approach involving technology transfers from the US in the 1980s and '90s, the aggressive wooing of overseas-trained talent and top-down government planning. This dominance in the chip industry allowed

Taiwan to leverage its increased strategic importance for economic and political importance, being reliant on China for economic growth and the US for national security.

Markets as a whole in Taiwan went up around 35% in 2020, a majority of it contributed by TSMC, which witnessed a 70% uptick in its market cap. Contextually, TSMC comprises over a fourth of the total market cap of Taiwan, which was the fastest growing emerging economy in 2020 (GDP growth rate of 3.1%).

TSMC contributes to roughly 20% of estimated private sector investments, according to estimates from the Taiwan Institute of Economic Research. So much so that some executives and government officials are calling Taiwan the island that TSMC built. TSMC makes chips for the latest Apple products, major automakers across the US, Europe and Asia and US F-35 fighter jets.

Unlike in many industries and geographies across the world, valuations of electronics and semiconductor industries in Taiwan haven't approached insane levels despite the unprecedented opportunity that was there. To provide a flavour, despite a weighted average growth in market cap of almost 70% in CY20, there was just a tepid rise in the weighted average price to earnings ratio of the firms from 23.8 in 2019 to 25.3 in 2020.

Taiwan was able to keep its debt profile and inflation in check, leading to better growth

Cold wars often harm strategic third parties in ways they cannot control and global travesties often provide opportunities for the very few. On the back of a turbulent 2019, with trade tensions between China and the US escalating,

Taiwan had a lean year in terms of exports, with two of its major partners involved in a trade conflict. Smart tactical management of the pandemic at the beginning of 2020 allowed it to function without a high number of covid cases even as its neighbours were struggling.

For 2021, Taiwan's GDP is expected to grow at 4.6%, according to the directorate general of budget, accounting & statistics, driven mostly by higher export value (exports are expected to go up almost 10% in 2021 to \$380 billion, compared to 4.6% in 2020) of semiconductors and electronics, stemming from an increase in both prices and volumes while their prices haven't gone up significantly.

Partially aided by efficient handling of the pandemic, Taiwan has been able to keep its debt profile and inflation in check, leading to better growth last year in comparison to its developed and emerging market peers such as the US, UK and China.

A shift in working patterns across the world due to the pandemic has led to higher demand for electronics. Coupled with a shortage of chips, this has resulted in production cuts at major automakers. As a result, almost all semiconductor and electronic equipment companies in Taiwan have made unparalleled investments in expanding capacities. This point towards a continued rise in demand for semiconductors and electronics.

Optimism from Taiwan's accounting and statistics office signalling the best year in terms of GDP growth in 2021 at 4.6% also point towards the same for the markets, which in the first quarter have witnessed a 10% rise in dollar terms. In view of our positive outlook of the Taiwanese markets, we have increased our exposure to Taiwan from 1.5% in May to 7% currently.

Shankar Sharma and Devina Mehra are co-founders and part of the fund management team at First Global Capital Management.



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