



Executive Summary

Semiconductor Quarterly Report Second Quarter, 2008

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INTRODUCTION

The US-Taiwan Business Council is committed to providing our members with tactical and strategic advice on how to succeed in the Taiwan market. As part of a suite of information products distributed to our members, the Council publishes several analysis reports each year. These reports are published each quarter, with an expanded report in the fourth quarter that covers the entire previous year.

The Semiconductor report focuses on the semiconductor industry as it relates to Taiwan, China, and the U.S., and provides up-to-date analysis of developments during each quarter. Each report also contains contact information valuable in initiating and maintaining a relationship with Taiwan private and government entities, as well as other useful information including trend charts and a glossary.

The US-Taiwan Business Council's Semiconductor Report has been published since the first quarter of 2002. Although these reports are distributed exclusively to members and to U.S. government employees, this executive summary provides some insight into the focus and contents of the report.

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QUARTERLY SEMICONDUCTOR ANALYSIS

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On Tuesday, May 20, 2008, East Asia changed in a profound way. Ma Ying-jeou was sworn in as president of Taiwan, ushering in a new era with the potential to unleash a technology juggernaut with trading partner China. While some nations suffer from military intervention or other dirty politics of the kind that ultimately slays fledgling democracies, Taiwan is now a stable and firmly established democracy. The island has undergone two major peaceful transfers of power between political parties – between President Ma’s Kuomintang (KMT or Nationalist Party) and former President Chen Shui-bian’s Democratic Progressive Party (DPP).

President Ma’s election victory probably means that the likelihood of a war between China and Taiwan – a war that would have been likely to involve the U.S. and would have shut down the global technology supply chain - has been greatly reduced. President Ma has spoken of seeking a peace accord with China, and in his inaugural address he committed to three no(s): No unification (with China), no independence (from China) and no use of force (against China).

Former President Chen and his political party advocates for independence from China. Despite Chen’s slightly toned down stance on formal independence during his time in office, he often aggravated the Chinese government, seemingly intending to bait China into outbursts that would ultimately cement Taiwan opinion against the mainland and secure votes for the DPP. The danger of this strategy was the possibility that China may be provoked into real military action. Indeed, U.S. officials had to step in at times over the past 8 years to try to help moderate passions on both sides of the Taiwan Strait. It didn’t help that Chen had a contentious relationship with the U.S. government as well.

During Chen’s term in office, the DPP also worked to slow the flow of trade between Taiwan and China for fear that Taiwan might be swallowed up by China through economic integration. Although China overtook the U.S. as Taiwan’s largest trading partner during Chen’s administration, his party had little to do with the change. Business people from the island were already investing heavily in China’s future. In fact, the DPP instead put up barriers to Taiwan investment in China, encouraged investment to alternative locations such as Vietnam, and prosecuted executives, particularly in the semiconductor industry, for alleged illegal work or investments in China. In contrast, President Ma has pledged to not only increase trade with China, but to also create a “Common Market” between them similar to the European Common Market. And he’s off to a quick start, a sign that preparatory work started long before his inauguration. For example, the first non-holiday direct flights between Taiwan and China in over 60-years took place on Friday, July 4, 2008. Indeed, the first 100-days of Ma’s presidency, though not yet finished, is likely to be remembered as a new blossoming of trade and goodwill between the two economies.

These increased ties and calls for more open trade and investment with China will put Taiwan’s technology prowess more closely in tune with China’s development, financing, and its vast market. China has made no secret of its aim to become a semiconductor industry powerhouse in the future, and it has spent billions of U.S. dollars to that end. Rich incentives for new chip factories, thousands of engineers pouring out of its universities each year, and other government work are all aimed at encouraging the development of a vibrant and vital chip industry on the mainland. Taiwan companies are well positioned to take advantage of China’s focus on semiconductors and technology.

This report will first take a look at the current downturn in the DRAM sector, and how Taiwan companies are coping by forming new partnerships. It will then detail the changes President Ma has made to liberalize ties with China, and examine the likely changes to Taiwan semiconductor industry investment in China. Finally, this report will explore Taiwan’s need to improve its chip investment rules while remaining mindful of its own security needs, before offering some conclusions and recommendations.

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