



Executive Summary

Semiconductor Quarterly Report Third 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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What do spoiled milk in China and Taiwan semiconductors have to do with each other? Turns out quite a bit actually.

Taiwan failed to publish new rules for Taiwan chip investment in China in September – despite an earlier government promise to do so – and the culprit is tainted Chinese milk. Rather, the delay has a lot to do with the political fallout from the melamine-tainted milk scandal in China.

The Taiwan people elected the first China-friendly president in nearly a decade at the polls earlier this year, despite Chinese missiles aimed at the island and a standing threat to invade if Taiwan declares independence. But the Taiwanese were willing to overlook these threats in hopes that greater trade with China would both encourage peace and boost the island's economic growth.

Given his wide victory at the polls, President Ma Ying-jeou has implemented a series of new policies to throw open the doors to trade and diplomacy with China. The results of his work are nothing less than revolutionary: people may now fly directly between China and Taiwan for the first time in six decades; thousands more Chinese tourists may visit Taiwan each year; Taiwan banks and insurance companies may expand in China; and Taiwan companies are free to invest billions of more dollars in China.

Unfortunately, the positive forward momentum of these changes has run smack into the global economic slowdown and the widening Chinese milk scandal. Taiwan citizens have become sick on the tainted milk, and hundreds of products have been pulled from Taiwan supermarket shelves over melamine fears. Some Taiwanese have pointed to the deadly milk as another example of why Taiwan should not trust China, and the milk scandal could ultimately lead to stunning setback for the new president of Taiwan and his pro-China policies.

The scandal has breathed new life into Taiwan's largest opposition party, the Democratic Progressive Party (DPP), which is using it to try to roll back some of President Ma's China trade initiatives. Semiconductors are a key point of contention. Politically in Taiwan, this is no time to introduce a new plan to allow chipmakers to invest hundreds of millions of dollars in China. Such moves would stoke fears of capital flight and lost jobs. The melamine scandal in China, it turns out, has cost the nation semiconductor investment from Taiwan – at least for now.

This quarterly report will review possible China investment rule changes, still anticipated at some point in the near future, and how they might affect Taiwan chipmakers. It will discuss the current global economic downturn and what it means to Taiwan companies, particularly in regards to capital spending by DRAM makers, in addition to possible strategic moves. Many people in Taiwan and elsewhere thought Taiwan Semiconductor Manufacturing Co. (TSMC) might strike a deal with US-based Advanced Micro Devices (AMD) to buy its factories and become its global partner. The report will also discuss how no such deal was struck - instead, AMD struck a deal with an investment fund from the United Arab Emirates - but how that may ultimately be to TSMC's benefit.

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