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Cross-Asset- and Strategy-Research

Why Taiwan matters



Moritz Kraemer -- Chief Economist

LBBWResearch@LBBW.de

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The world depends on Taiwanese semiconductors

The controversial visit by the Speaker of the US House of Representatives, Nancy Pelosi, to Taiwan has dominated the headlines and bond markets worldwide in recent days. The island with its just 24 million inhabitants is territorially claimed by the 60 times more populous People's Republic of China (henceforth referred to as China).

Beijing's saber-rattling has noticeably increased. China is currently holding military maneuvers around Taiwan. Many observers assume that the territorial waters of Taiwan could also be affected.

The risk of an escalation has increased

One suspects that the timing of Pelosi's visit, the first by such a senior US representative in a quarter-century, was determined by electoral tactics. It currently looks likely that her Democratic Party will lose its majority in the November mid-term elections. Such an outcome would also remove Pelosi from Washington's political center stage.

Growing skepticism about Xi Jinping's China is one of the few policy areas on which the two otherwise hopelessly divided parties agree. Republican accusations that the Democrats are "soft on China" will now no longer stick in the run-up to the elections.

Nevertheless, the visit came at the worst possible time. Elections are not only coming up in the US. Xi Jinping also wants to be re-elected for an unprecedented third term in the fall. Although this will be more of a ceremonial appointment than a genuinely contested election, Xi Jinping nonetheless cannot afford to appear weak either. Even less so as Pelosi's visit coincided with the celebrations to commemorate the 95th anniversary of the creation

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of China's People's Liberation Army. Belligerent rhetoric is easily inflamed in such a nationalistic backdrop. The danger of an escalation has increased.

Taiwan's key role in the global economy

An open military conflict (still) appears unlikely in the short term. But we must anticipate the consequences of military action. China sees reunification with Taiwan as a historic mission, just as the Kremlin sees the incorporation of Ukrainian territories. It will not desist its ambition to eventually absorb Taiwan.

An invasion, or even just a maritime encirclement of Taiwan, would have catastrophic consequences for the world economy. Even if there is no direct confrontation with American associations and even abstracting the economic effect of possible sanctions and countersanctions between China and the US.

Taiwan is the world leader in the production of semiconductors, which in today's electronic world have become indispensable components for countless products from automobiles to smartphones. The Taiwanese company [TSMC](#) alone has a market share of over 50%. In the case of the most complex semiconductors, the market share is even estimated at over 90% (see figure). A disappearance of these products would trigger the "mother of all supply chain problems" and plunge the world into a deep recession.

The US has begun to prepare for this emergency. In July, legislation was passed that will support the US chip industry with over \$50 billion. In times of rising geopolitical tensions, proactive industrial policies are back in fashion.

Europe's dependence on Chinese and Taiwanese semiconductors is even greater than on Russian gas. Today Taiwan is a friendly and cooperative state. For how much longer?

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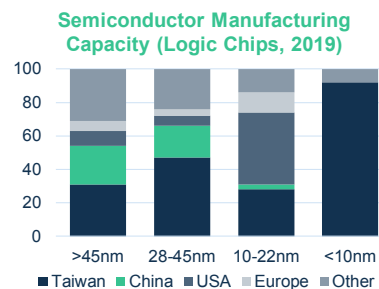
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Source: US Semiconductor Industry Association

The disappearance of Taiwanese semiconductors would plunge the world into a deep recession
