Taiwan's Strategic Position amid U.S. FART Act

March 2025

The Fair and Reciprocal Tariff (FART) Plan aims to address trade imbalances by ensuring tariffs on foreign goods match those imposed on U.S. exports. Taiwan is unlikely to face comprehensive tariffs due to no intentional currency manipulation, a smaller trade surplus compared to other countries, and growing U.S.-Taiwan military deals. Despite tariff disparities in select industries, Taiwan's dominance in semiconductor provide leverage in trade talks. A trade war remains unlikely, but Taiwan must navigate risks carefully.

By Cathay SITE

The Fair and Reciprocal Tariff (FART) Plan aims to address perceived trade imbalances by ensuring that tariffs imposed by the U.S. on foreign goods were equal to or "reciprocal" to the tariffs other countries placed on American exports. Key features and effects of the FART Plan are tariff matching, reducing trade deficits and bringing back manufacturing.

The administration will review the impact of foreign tariffs, taxes, nontariff barriers or measures, exchange rates, etc. on the U.S. economy. After tariff concessions from Canada and Mexico, the EU is ready to discuss cutting tariffs on autos and other goods to avoid a trade war with the U.S.

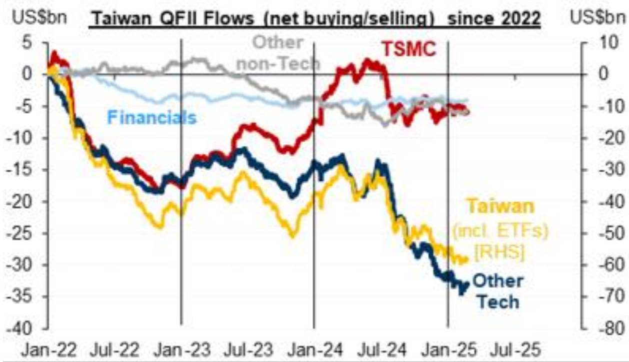
In our base case, the policy is highly likely to be implemented and is expected to replace Trump's original plan of imposing a 10% tariff on all global imports. Ultimately, it will take the form of reciprocal tariffs combined with industry-specific tariffs.

Full-scale tariffs on Taiwan are unlikely

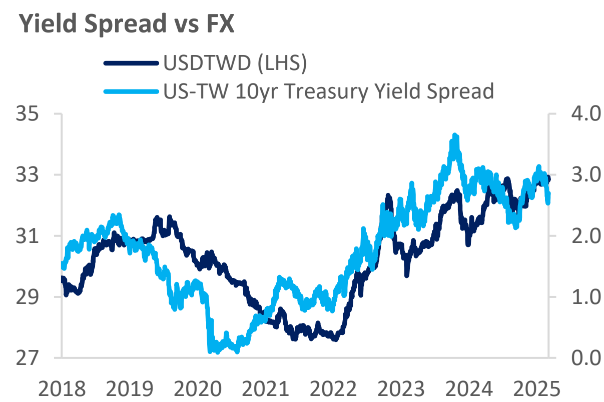
The likelihood of the U.S. imposing broad tariffs on Taiwan remains low due to the following reasons.

No intentional currency manipulation

The depreciation of the New Taiwan Dollar (TWD) is primarily driven by capital outflows and the widening U.S.-Taiwan interest rate differential, rather than direct intervention by Taiwan's central bank.



Source: Goldman Sachs

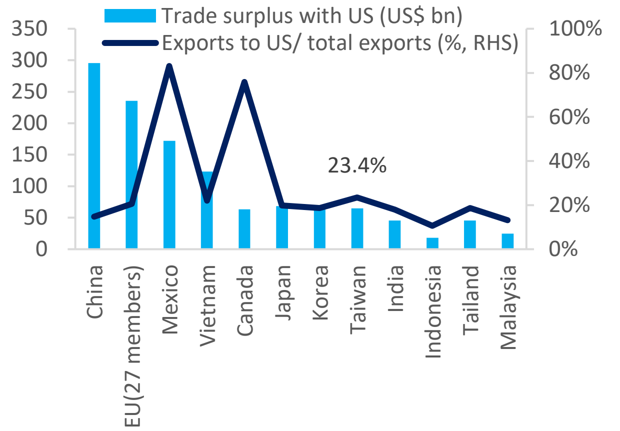


Source: Bloomberg, compiled by Cathay SITE

Taiwan is not a primary trade adversary

Based on trade balances and top-down average tariff differences, Taiwan is not a major target for tariff retaliation. Taiwan's trade surplus with the U.S. is significantly smaller than that of

China, the EU, Mexico, and Vietnam. According to Morgan Stanley estimates, Taiwan's bilateral tariff differential with the US is about 0.8%, much lower than other Asian countries such as Japan, South Korea, India, Thailand, and the Philippines (ranging from 2% to 6%). While Taiwan is not a primary target, its export dependence on the U.S. is 23.4%, making a tariff war a risk that cannot be ignored.



Source: Wind, compiled by Cathay SITE

Arms purchase to balance trade surpluses
Taiwan's recent increase in military procurement from the U.S. could help balance trade surpluses and reduce tariff-related risks. Taiwan authority plans to increase its defense budget to NT$ 760 billion in 2025 (approximately 3% of GDP). The potential US$10 billion arms purchase from the U.S. is equivalent to 60% of Taiwan's total military procurement during Trump's previous term.

Limited industry impact
Tariff disparities exist between Taiwan and the U.S., particularly in the food and automotive industries, while high-tech products such as ICT and semiconductors remain mutually tariff-exempt. Moreover, Taiwan holds strong market dominance in high-end electronics with substantial pricing power.

If Trump were to impose tariffs on Taiwanese semiconductors, the financial impact would be minimal given tariff implementation challenges. TSMC chips enter the U.S. in various forms, from Know Good Die (KGD), packaged chips, semi-finished modules to fully assembled consumer devices. Only KGDs are entirely manufactured by TSMC, making them the simplest to tax, but these account for less than 0.01% of TSMC's U.S. exports. Products like CoWoS involve components from other countries e.g., memory chips from the U.S. and Korea, making taxation more complex. Applying tariffs on modules or final products is even trickier.

TSMC's chips are core to U.S. tech firms and the enabler of U.S. AI leadership ambitions. The share of Taiwanese ICT orders to U.S. import - Automatic Data Processing Machines and Units Thereof stood at around 42%, implying strong U.S. dependence on Taiwanese servers and advanced semiconductors. This dependency together with TSMC's dominance in advanced processes provides Taiwan with strong leverage in trade negotiations. Also, several Taiwanese server ODMs are considering U.S. expansion which could further ease trade tensions.

Short-term challenges, long-term gains
On March 4, 2025, TSMC announced an additional $100 billion investment in the U.S. This move has a strong sense of déjà vu. TSMC's U.S. expansion mirrors Japan's auto industry in the 1970s when Toyota had to set up factories in the U.S. due to trade tensions. To this day, Japanese automakers still keep core R&D and technology in Japan while setting up U.S. production lines. One of TSMC's keys to success is its flexibility in responding to customer needs which requires timely and seamless communication with supply chains, most of which locate in Taiwan. Rest assured that this core advantage is difficult to fully migrate overseas for the foreseeable future.

This massive investment in U.S. chip plants could lower TSMC's overall gross margin but increase its revenue and gain stronger U.S. market positioning with strengthening ties with U.S. customers. According to an industry expert, even after all U.S. fabs come into operation, their total capacity will only account for 5–7% of TSMC's global production.

Additionally, the success of TSMC’s U.S. operations will still rely on Taiwan-based technical teams, highlighting Taiwan’s irreplaceable role in advanced semiconductor manufacturing.

In summary, a full-scale trade war is unlikely, but Taiwan should remain cautious about the risk considering its export dependence on the U.S. Its competitive edge in high-tech industries gives it pricing power and tariff resilience. Furthermore, TSMC’s recent announcement of U.S. expansion cements its role as a truly global semiconductor leader and may counterbalance potential geopolitical and tariff risks.