June 22, 2007

Timothy Stratford
Assistant USTR, China Affairs
Office of the United States Trade Representative
600 17th Street, NW
Washington, D.C. 20508

Dear Tim,

Over the past 2-3 years we have seen a significant rise in mergers and acquisitions activity in the Taiwan market. America's leading private equity companies - led by The Carlyle Group, KKR, Oaktree and Blackstone - have all been actively pursuing deals in Taiwan.

Private Equity (PE) generally acts as a positive force on any capital market, creating value for existing shareholders of companies, for related industries, as well as for the market as a whole. Companies that are acquired generally benefit from the knowledge and expertise brought to the table by the PE companies and by their franchise relationships, as PE firms generally seek to make their gains via an increase in the overall value of an acquired company. This means that they must make the company even better than before – through indigenous growth, increased profitability, better service to its customers, etc. – in order to increase the value of the acquired company beyond the price point at which they originally invested.

In Taiwan, we have seen the most active mergers and acquisitions activity in the banking sector, as Taiwan has pursued a policy of consolidation of state owned banks - as you know the sector is heavily over banked. However, the Taiwan government seems only interested in the purchase of distressed assets and its attitude changes markedly when a takeover of healthy assets takes place or is even suggested.

The Carlyle Group & Advanced Semiconductor Engineering (ASE)
In the fall of last year, The Carlyle Group tendered an offer for Advanced Semiconductor Engineering (ASE), a semiconductor packaging and testing company, a bid made after a period of negotiation with ASE's senior management. Carlyle's attempt at entry into Taiwan's semiconductor market reflects the high caliber of Taiwan businesses and a desire to link the U.S. and Taiwan - arguably the two most important semiconductor markets in the world.

It is critical for the Taiwan government to realize that acquisitions by private equity companies are as effective a means of sector rationalization as buyouts by companies within the same sector. Carlyle already manages a global portfolio of semiconductor companies, and by joining that group ASE would have been positioned to take advantage of opportunities to purchase synergistic business units from other portfolio companies.

Coupled with follow-through on Taiwan's January 2006 decision to liberalize its cross-Strait investment policy in the chip assembly sub-sector, a consummated deal might have allowed ASE to accelerate its growth - by purchasing operations from Freescale, for example, or perhaps even from non-portfolio companies (such as NXP) looking to capitalize on the trend towards shedding global chip assembly operations. Not only would the Taiwan sub-sector as a whole have benefited, but other Taiwan companies like TSMC and UMC would have seen benefits as well.

The news of Carlyle's interest in ASE sparked a market-wide rise in Taiwan, with the TAIEX gaining 7.2% between late November 2006 and mid April 2007. When the initial offer was made, ASE stock was valued at NT$35.50 per share, meaning that the initial offer of NT$39 per share reflected fair market value with a small premium. At the close of the market on April 17, however, ASE's share price had risen over 15% to just over NT$41 per share. ASE set up an investment committee to examine the proposal and to ensure that all ASE shareholders, not just founder and largest shareholder Jason Chang and his family, would benefit from the transaction – a key step in today's market where minority shareholder interests can not be ignored. In the end, and due to the excessive delays in consummating the deal, the market value of ASE had risen past both the original and a revised offer by Carlyle. Ultimately, it was failure to agree on a price for ASE that scuppered the deal.

While the TAIEX's 7.2% overall rise was modest, it still represents gains from the attention paid to a single deal, and a potential increase in M&A activity will surely have an even greater positive impact on the valuation of Taiwan's companies. It's a huge opportunity to increase the overall value of Taiwan's economy, and to increase the capital it has at its disposal. It is also an opportunity to increase the attention paid to Taiwan by the global business community, since it is also a fact that Taiwan's companies still are not paid nearly enough attention as gateways to mainland China.

However, Taiwan does not have a great deal of experience with mergers and acquisitions (M&A) of this size, particularly outside the banking and financial services sectors, so the bureaucracy is thrown into turmoil when such deals are proposed. The lack of a permanent and transparent process for M&A activity to be reviewed in a timely manner can result in confusion and delays. For example, Taiwan presently requires in excess of 17 different government agencies to review acquisitions such as the proposed Carlyle/ASE deal. Not only does this add costs to any such transaction – costs that may inhibit capital from even exploring Taiwan's market - but it also leads to delays that may even cause deals to ultimately collapse, like it did in this case.

Concerns for Private Equity

The Carlyle Group's failed bid for ASE raises some serious concerns for the membership of the US-Taiwan Business Council. Taiwan's Financial Supervisory Commission (FSC) is open to takeovers of "bad" banks in Taiwan, but it's unclear whether they would allow Private Equity firms to take over healthier or very good banks, or if they would be allowed to participate at all in the privatization of large government owned banks.

Also, it's not just leading technology firms such as ASE that are deemed sensitive, but companies with large market capitalizations in general, as de-listing such firms is seen as bad for Taiwan from an equity market perspective. This will also be true as Taiwan looks to divest itself of Taipower, Chinese Petroleum and other state owned assets. The Council is deeply concerned that future transaction activity in Taiwan will exclude the private equity community and that a bias within the system will work against not only PE firms, but even against the very notion of taking large public companies private.

In addition, the FSC has said that they may have some opinions on how deals are actually financed (potentially deeming the amount of leverage put on the businesses as being too much), instead of leaving that to the private sector. Of course, if they want to go down that path and prevent domestic banks from participating in such loans, they will then make their own banks less competitive not only within Taiwan but on a regional basis.

I think that, for now, the initial FSC interest in legislative changes to the Business Mergers and Acquisitions Act has subsided with the failure of the bid for ASE. It seems that the recent Fu Sheng deal (Oaktree Capital Management), the just announced Yageo deal (KKR), and some soon to be announced acquisitions of troubled banks are meeting with FSC approval and general support.

Nevertheless, the Council is concerned that the recent threats from the FSC over regulatory and legal changes that would prejudice the interests of the private equity community in Taiwan may reappear. I am therefore respectfully writing to request that the Office of the United States Trade Representative raise the issue of private equity participation in the Taiwan market at the upcoming Trade & Investment Framework Agreement (TIFA) meeting this summer in Washington, D.C.

The Council seeks clarification on several issues:
- Taiwan's overall position vis-à-vis private equity.
- The lack of a formal, transparent and expedited process for reviewing transactions like the Carlyle/ASE deal, and plans for developing such a process.
- The lack of a consistent policy that spans the entire Taiwan economy. All business sectors should be open to investment, free of the Taiwan government arbitrarily choosing winners and losers.

The US-Taiwan Business Council urges the Taiwan government to make all haste in finishing its internal discussions and crafting of new regulations for the semiconductor industry. These new regulations should include a thorough, transparent, and straightforward process for mergers and acquisitions (M&A) in Taiwan's technology sector. The lack of a permanent and timely process for reviewing M&A activity in the technology sector adds costs that may inhibit foreign investment from even exploring Taiwan's market. In addition, it leads to delays that may cause deals to ultimately collapse – a contributing factor in the Carlyle Group/Advanced Semiconductor Engineering (ASE) buyout plan.

Increased M&A activity in Taiwan would have a positive impact, as it would increase the overall value of Taiwan's economy, as well as increase the capital at the market's disposal. It is also an opportunity to increase the attention paid to Taiwan by the global business community, releasing synergies with portfolio companies and accelerating positive market trends. Adding further to this most critical of bilateral trade relationships is inherently in the interests of the U.S. business community.

Sincerely,

Rupert Hammond-Chambers

Rupert Hammond-Chambers
President

cc: Eric Altbach, Deputy Assistant USTR, Office of China Affairs, Office of the United States Trade Representative
Rick Ruzicka, Director, Trade and Commercial Programs, American Institute in Taiwan
Jim Hildebrandt, Managing Director, Bain Capital Asia, LLC
Anthony Leung, Senior Managing Director, Blackstone Group Asia, Ltd.
William Ferguson, Group Marketing Executive, Asia Pacific, Citigroup, Inc.
Maarten Ruijs, Managing Partner & Chief Investment Officer, CVC Asia Pacific, Ltd.
Timothy Marsh, Senior Vice President, Global Client Development, GE Consumer Finance
Joe Bae, Managing Director, Kohlberg, Kravis, Roberts, Inc.
Mark Chiba, Chairman, Longreach Management Group
Richard McCormack, Vice Chairman, Merrill Lynch
Dan Carroll, Managing Director, Newbridge Capital, Ltd.
William Kerins, Managing Director, Oaktree Capital (Hong Kong), Ltd.