II. International and domestic economic and financial conditions

2.1 International economic and financial conditions

The global economy recovered better than expected in 2009. However, this occurred at varying speeds across different countries and regions. The recovery was proceeding somewhat sluggishly in major advanced economies and relatively more rapidly in most emerging and developing economies. China, a country that in recent years established increasingly closer economic and trade links with Taiwan, experienced a rapidly accelerating economy alongside its strong credit expansion, but the government signaled a tightening monetary policy stance.

Risks to global financial stability subsided, but banking systems were still weighed down under the lingering pressures of refinancing and capital recapitalization. Credit supply to households and the corporate sector has yet to recover. Growing sovereign risks in some advanced economies could spread to financial systems and across borders, compromising global financial stability. For emerging economies, large capital inflows led to fears of rising risks of inflation and asset bubbles.

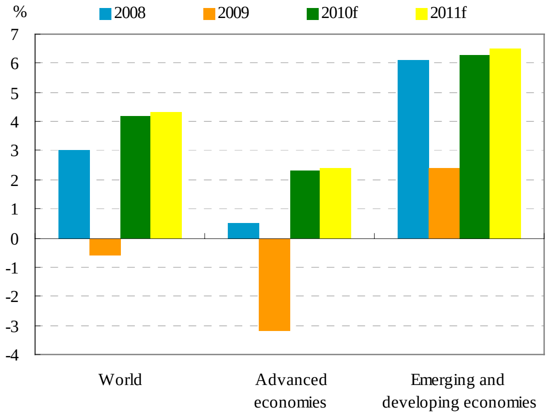
Global recovery evolved at a stronger pace than expected and inflationary pressures receded, but unemployment rates remained high

In the first half of 2009, global output suffered from a sustained downturn, resulting from sluggish economic activity in major countries and weak international financial conditions. In the second half of 2009, the output in major economies declined only moderately or even rebounded to positive growth, fostering a stronger-than-expected global recovery. A key factor bring the global economy out of recession was the effectiveness of expansionary fiscal policies and easy monetary policies. The International Monetary Fund (IMF) statistics stated that the global economic growth rate contracted substantially to -0.6% in 2009 from 3.0% a year earlier. The global economy is projected to experience an ongoing recovery with a growth rate of 4.2% in 2010 and to expand further by 4.3% in 2011[7] (Chart 2.1).

[7] IMF, "World Economic Outlook," April 2010.

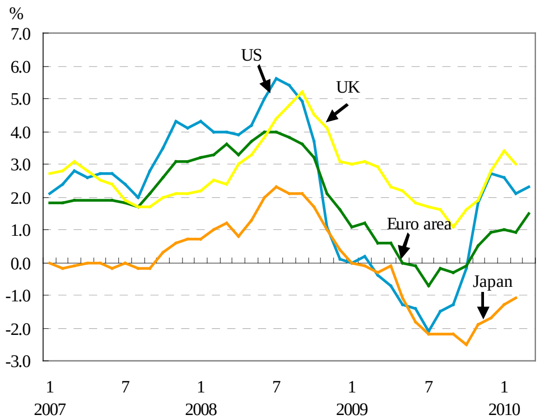
By the end of 2009, the global economy showed signs that it was rebounding from a deep trough, but at varying speeds across different countries and regions. Supported by an upswing in the inventory cycle and a gradual rebound in private consumption, output in advanced economies turned to a favorable improvement, but might continue to recover tepidly. The IMF forecasts that output in advanced economies will rebound by 2.3% and 2.4% in 2010 and 2011, respectively, following negative growth of -3.2% in 2009. The recovery in emerging Asia was the most outstanding. Sharp increases in domestic demand and the fast expansion in global trade helped many emerging and developing economies to grow at a robust pace. The IMF projects emerging and developing economies will register economic growth rates of 6.3% and 6.5% in 2010 and 2011, respectively, following growth of 2.4% in 2009.

Chart 2.1 Global economic growth rates



Note: Figures for 2010 and 2011 are IMF estimates.
Source: IMF, “World Economic Outlook,” April 2010.

Chart 2.2 Consumer price inflation rates in major economies

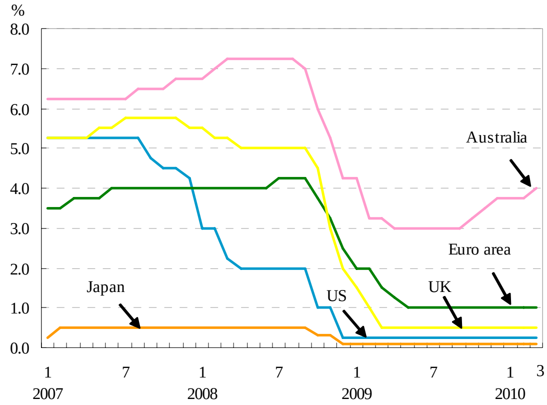


Note: Figures for the euro area are based on Harmonised Index of Consumer Prices (HICP) inflation rate. The others are based on consumer price index (CPI) inflation rate.
Sources: BLS and DataStream.

As for consumer prices, in the face of the world economic slowdown, together with a higher base a year earlier, the consumer price index (CPI) inflation rate in most economies pursued a downward trend from early 2009 onwards. However, consumer prices rose and turned to an upward trend in 2009 Q4, driven by a faster pace in the global recovery (Chart 2.2). The IMF forecasts global inflationary pressures to remain subdued and the global CPI inflation rate is expected to rebound to 3.67% in 2010, following an inflation rate of 2.45% in 2009. Consumer prices are predicted to rise at varying speeds across regions. In 2010, the CPI inflation rate in advanced economies is expected to stand at 1.49%, whereas in emerging and developing economies it is anticipated to post a sharp increase of 6.19%.

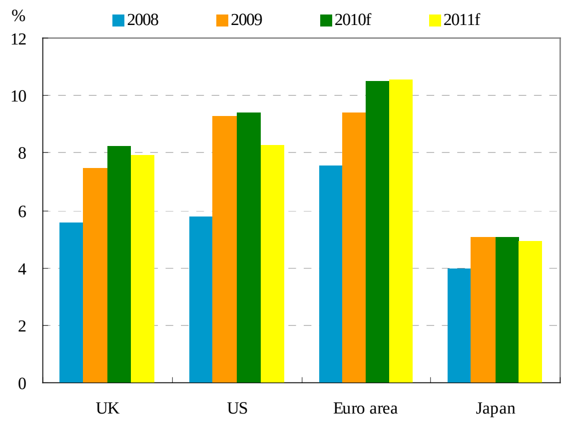
Regarding monetary policy, many central banks stopped cutting policy rates from the second half of 2009 onwards. The reason behind this was that the credit crunch in global financial markets was relieved, a sustained global economic recovery was underway and historically low interest rates existed in many countries. In view of subdued downside risk, the Reserve Bank of Australia initiated interest rate increases and successively raised the cash rate target four times, each by 25 basis points, to 4%[8] from October 2009 to March 2010 (Chart 2.3). Central banks in some countries (such as Norway, Israel, Malaysia and India) also raised their policy rates subsequently. In addition, the board of governors of the Federal Reserve System (FED) announced an increase in the discount rate from 0.5% to 0.75% on 18 February 2010, while the target range for the federal funds rate remained at 0 to 0.25% (Chart 2.3).

Chart 2.3 Policy rates in major economies



Note: Figure for Australia is based on cash rate target; for the US, federal funds rate; for the UK, official bank rate; for the euro area, the main refinancing operations fixed rate; and for Japan, uncollateralized overnight call rate.
Source: Central banks' websites.

Chart 2.4 Unemployment rates in major economies



Note: Figures for 2010and 2011 are IMF estimates.
Source: IMF, "World Economic Outlook," April 2010.

Major advanced countries were likely to face a jobless recovery owing to surging unemployment rates during the recession. The IMF forecasts that in 2010 the unemployment rate for the UK and the US will move up to 8.25% and 9.41%, respectively. At the same time, Japan's unemployment rate is projected to increase to 5.08%, whereas in the euro area it is expected to sharply rise to 10.52% (Chart 2.4). Some countries with fragile fiscal positions, such as Spain and Ireland, are estimated to reach peaks of 19.40% and 13.50% through 2010, respectively. Looking ahead, the IMF foresees that these economies will be unlikely to experience drops in unemployment rates until 2011.

The global economic recovery was highly supported by the macroeconomic policies adopted by national governments, and emerging fiscal vulnerabilities in advanced economies may expose the global economy to uncertainty. In this context, the IMF offered the following recommendations to ensure a stable and balanced global recovery:

8 As of May 2010, the cash rate target has moved up to 4.50%.

- Major advanced economies should promptly put credible medium-term fiscal consolidation plans in place and launch financial reform;
- Emerging economies warrant vigilance in monitoring sizable capital inflows;
- The timing and strategy of the exit from policy support needs to be prudentially decided;
- Advanced economies facing high unemployment rates should adopt necessary policy actions to help the jobless and to foster employment;
- Emerging economies with excessive current account surplus should promote domestic consumption, whereas advanced economies with large current account deficits need to abate their consumption of imports with the aim of rebalancing global demand.

China's economic growth accelerated and credit expanded at a strong pace, but monetary policy signaled a tightening stance

The momentum of China's economic growth was solidifying, whereas consumer prices were gradually rebounding

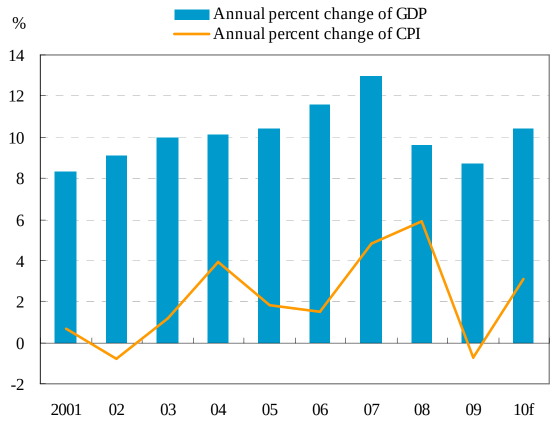
China's economic recovery proceeded at an accelerated pace from the second half of 2009 onwards, underpinned by a series of economic stimulus measures worth up to RMB 4 trillion aimed at increasing domestic demand. Economic growth increased to 9.1% and 10.7% in Q3 and Q4, respectively, and registered 8.7% through the whole of 2009. The momentum of domestic economic growth mainly stemmed from run-ups in fixed asset investment as well as rising domestic demand spurred by government subsidy policies. However, trade surpluses shrank notably from a year earlier as the contraction in exports was more than the decline in imports. Global Insight projects China's economic growth through 2010 to widen to 10.4%[9] on the back of a wide range of policy actions implemented by the Chinese government for the sake of promoting domestic consumption.

Regarding consumer prices, the CPI inflation rate was negative in nine consecutive months. The decline was because of low levels of capacity utilization, lackluster private consumption, and moderate increases in the prices of international raw materials and commodities, which combined to put downward pressure on domestic prices in the first three quarters of 2009, coupled with a higher base of the CPI inflation rate over the same period a year earlier. In November 2009, the CPI inflation rate turned positive due to rebounding consumption demand and mounting food prices. Nevertheless, for 2009 as a whole, the inflation rate

[9] Global Insight Estimate in April 2010.

posted a figure of -0.7%. It is expected to bounce back to 3.1% in 2010 according to the IMF's projection (Chart 2.5).

Chart 2.5 Economic growth rate and CPI inflation rate in China

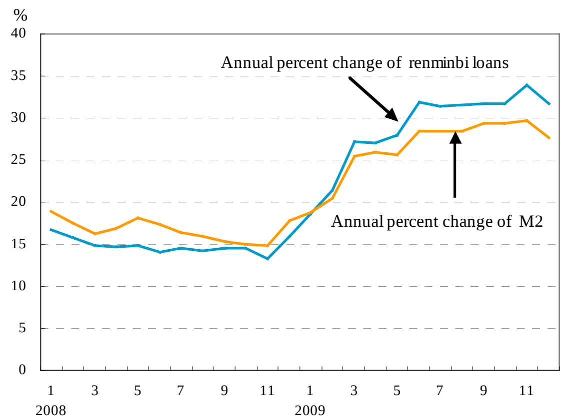


Note: Using Global Insight projection for economic growth and IMF projection for CPI inflation rate in April 2010.
Sources: National Bureau of Statistics of China, Global Insight and IMF.

Bank credit and asset prices boomed, while monetary policy signaled a tightening stance

Following the People's Bank of China (PBC) launching extremely easy monetary policies from September 2008 onwards, domestic investment in China increased dramatically. This not only became a pivotal driver for economic growth but also spurred expanding growth in bank credit. The annual growth rate of M2 rebounded to 27.7% in December 2009 from a trough of 14.8% in November 2008, while the annual growth rate of renminbi loans originated by local banks also picked up to 31.7% from a low of 13.2% over the same period (Chart 2.6). Furthermore, newly granted renminbi loans reached RMB 9.59 trillion in 2009, exceeding the annual target of RMB 5 trillion, and increased by RMB 4.69 trillion from 2008. This reflects an over-accelerating expansion in credit. In addition, despite the surge in public investment, private investment activities remained slack due to declining exports and rising labor costs. As a result, excessive capital inflows to equities markets and the real estate market fueled rises in equities and property prices, raising the attendant risk of asset price bubbles.

Chart 2.6 Annual growth rate of M2 and renminbi loans in China



Source: PBC.

In 2009, the PBC kept the benchmark one-year deposit and lending rates unchanged at 2.25% and 5.31%, respectively. However, in response to the rapid expansion in credit, the PBC and the China Banking Regulatory Commission (CBRC) successively implemented measures to strengthen the monitoring of bank loans and to improve the soundness of risky assets from the second half of 2009 (Table 2.1). Moreover, the PBC substantially contracted market liquidity from January to May 2010 through targeted policy actions, including: (1) raising the reserve requirement ratio (RRR) for financial institutions three times by a total of 1.5 percentage points; (2) conducting open market operations by raising the interest rate of issuance for three-month and one-year central bank notes by 8 basis points and 16.59 basis points, reaching 1.41% and 1.93%, respectively. These policy actions signal that monetary policies are shifting toward a tightening stance.

Table 2.1 Measures to enhance the control of bank loans

Announced by	Measures
The People's Bank of China (PBC)	Fostering the issuance of specific-counterparty bills by the central bank to major banks.
PBC The China Banking Regulatory Commission (CBRC)	1. Launching tightened mortgage policies via the following regulations: · The down payment to loan ratio for first-time homebuyers should not be less than 30%. · The down payment to loan ratio for second-time homebuyers should not be less than 50% and the lending rate is not allowed to be less than 1.1 times the PBC benchmark lending rate. · Lending to third-time homebuyers was suspended. 2. Banks could suspend mortgage lending to non-resident citizens who fail to offer certificates which evidence payment of taxes or social insurance for one year or more.
CBRC	Requiring that the capital adequacy ratio of major banks should be up to 11%, while that for small-medium banks should be up to 10%.
CBRC	Increasing the non-performing loan coverage ratio of financial institutions to 150% from 144.5% by the end of 2009.

Note: Specific-counterparty bills refer to the bills issued by the People's Bank of China to specific counterparties.
Source: CBC staff summary; End-April 2010 data.

The financial system experienced a period of restoration, but surging sovereign risks could spread to the banking system

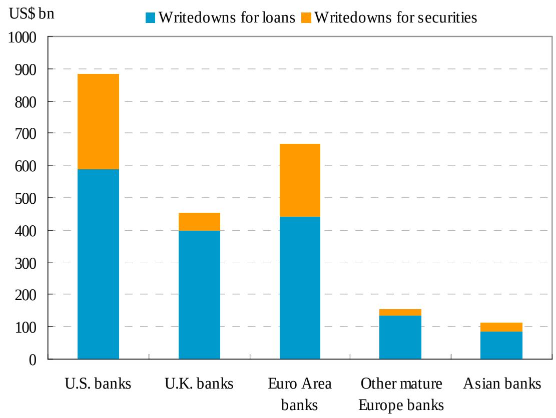
In 2009, with economic fundamentals improving and substantial public support remaining in place, the health of the global financial system was generally restored as global financial markets rebounded sharply from deep troughs and overall systemic risks mitigated. The global banking system has improved but could be vulnerable to refinancing and capital raising pressures. Credit supply to households and the corporate sector has yet to recover. In some advanced economies, soaring sovereign risks, mainly arising from worsening fiscal balances and rapid accumulation of government debt, could spill over to banking systems and across borders. This needs to be promptly addressed by national governments. In addition, massive capital inflows to emerging economies are raising concerns about elevating risks of inflation and asset bubbles. A deliberate response to this situation is warranted.

The global banking system has improved, but refinancing, capital raising and constrained credit supply pressures may lie ahead

With an ongoing economic recovery and improved financial market outlooks, the health of banks was restored and their capital conditions also improved markedly in most economies. In April 2010, the IMF revised downward its forecast for global asset writedowns to US$2.3 trillion[10] (Chart 2.7). Of this amount, around US$1.5 trillion had been realized by the end of 2009.[11]

The health of the global banking system has improved, but pressures from refinancing and recapitalization, coupled with still-constrained credit supply, may lie ahead. Many large banks relied on central bank emergency support to alleviate their short-term funding pressures amid the global financial crisis. However, the IMF estimates that there is nearly US$5 trillion of bank debt due to mature in the coming three years. This will coincide with heavy government bond issuances and succeed the removal of central bank emergency measures over the same period, putting refinancing pressures on those large banks. Despite the fact that the level of overall capital in the banking system has increased, capital requirements are expected to increase dramatically under the revision of the new capital accord (namely Basel II) framework.[12] This, along with the fact that banks have not fully realized asset writedowns, is likely to intensify recapitalization pressures on banks in the future. In addition, credit extension to households and the corporate sector remains constrained owing to still-tightened lending standards and weak credit demand. Small and medium enterprises (SMEs), especially, have suffered more pronounced impacts. In this respect, national governments need to take supportive measures in hopes of promoting economic recovery.

Chart 2.7 Estimates of global asset writedowns



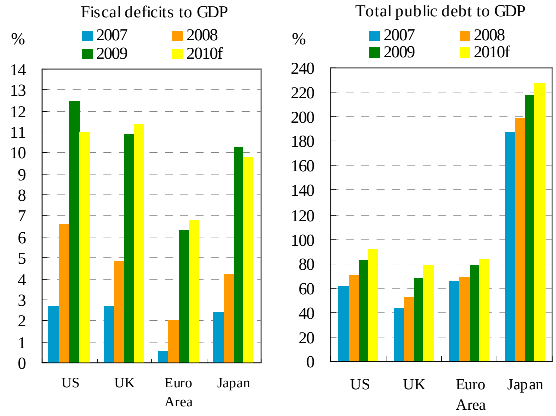
Note: "Other mature Europe banks" includes banks in Denmark, Norway, Iceland, Sweden and Switzerland. "Asian banks" includes banks in Australia, Hong Kong, Japan, New Zealand and Singapore.
Source: IMF, "Global Financial Stability Report," April 2010.

[10] The IMF's previous estimate of global asset writedowns in October 2009 was about US$2.8 trillion.
[11] IMF, "Global Financial Stability Report," April 2010.
[12] The Basel Committee on Banking Supervision (BCBS) released a consultative document: "Strengthening the Resilience of the Banking Sector" in December 2009. The key elements of this proposal include: 1) developing the amendment of the new capital accord (Basel II); 2) requiring banks to enhance the quality of capital and to build up capital buffers; and 3) introducing leverage ratios to complement minimum capital requirement standards.

Mounting sovereign risks in advanced economies could be transmitted to banking systems and across borders

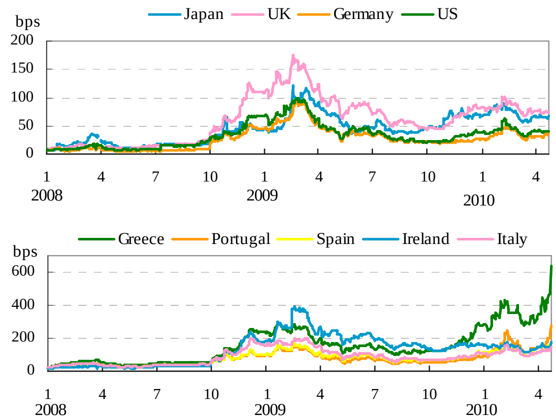
During the recent financial crisis, advanced economies sharply expanded the scale of government expenditures and debt with a view to rescuing financial systems and revitalizing the economy, resulting in soaring public debt and deteriorating fiscal imbalances. Among major advanced economies, fiscal deficits to GDP ratios for the US, the UK and Japan all exceeded 10% in 2009, while the government debt to GDP ratio in Japan registered 217.6% over the same period and is expected to continue to spiral upward in 2010 (Chart 2.8). The surge in public debt and the deterioration of fiscal balances have triggered mounting sovereign risks. As a result, credit default swap (CDS) spreads of government bonds for those economies continued to increase. From the second half of 2009 onwards, concerns over elevated public debt and political uncertainties in the UK and Japan have led to the surge in their CDS spreads. In some southern European countries (most notably Greece, Spain and Portugal), CDS spreads for government bonds successively hit new record highs from February 2010 as fears of sovereign debt crises have triggered a loss of investor confidence in financial markets (Chart 2.9).[13]

Chart 2.8 Fiscal deficit and public debt in major economies



Note: Figures for 2010 are IMF estimates.
Source: IMF, "World Economic Outlook," April 2010.

Chart 2.9 Credit default swap spreads in major economies



Note: Figures are based on 5-year credit default swap securities.
Source: Bloomberg.

The sovereign debt crisis unfolding in some advanced European economies could possibly be transmitted to their local banking systems through close ties between governments and banks. For example, local banks holding massive amounts of government bonds may suffer the losses on falling bond prices and the soaring issuance rates of government bond also may

[13] As of the end of April 2010, the CDS spread for Spain hit a historical peak of 173.38 basis points on 8 February 2010. In Greece and Portugal, CDS spreads stood at record highs of 638.87 basis points and 276.195 basis points on 23 April 2010, respectively.

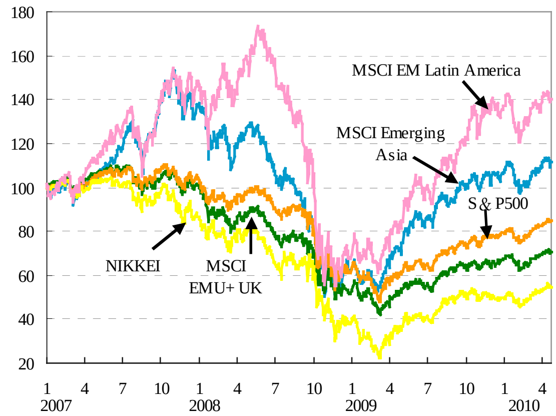
raise the funding costs of local banks. Moreover, the sovereign debt crisis might spread to other countries via interlinkages of the global financial system. To reduce sovereign risks, the IMF suggests those economies to urgently develop creditable medium-term fiscal consolidation plans and emergency measures that command public support. It is worth noting that such plans and measures should be put in place to intensify market confidence, so as to prevent the sovereign debt crisis from deteriorating and causing negative spillovers.

Abrupt increase in capital inflows into emerging economies have raised concerns about elevated risks of inflation and asset bubbles

Since 2009 Q2, the renewal of global investors' risk appetite and low interest rates in advanced economies, together with better economic growth prospects for emerging markets, have attracted massive capital flows into emerging economies, particularly to Asia (excluding Japan) and Latin America, for investing in securities. As a result, asset prices rebounded substantially. The performance of equity markets outpaced other financial markets, with key international stock indices rebounding dramatically during March-October 2009. However, global equities prices slumped again in November 2009 due to emerging concerns about the sustainability of government finance in Dubai and Greece (Chart 2.10). In real estate markets (excluding China), the rise in property prices was less than equities prices and was within historical norms.

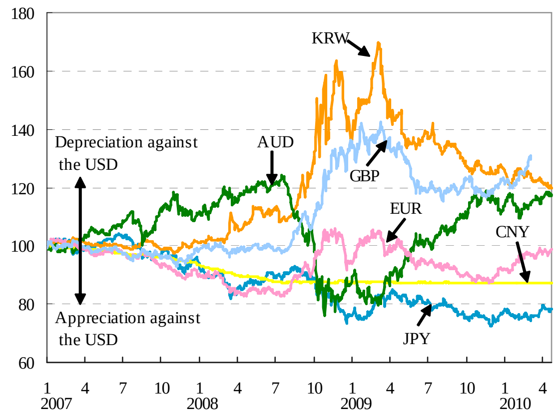
Ongoing massive capital inflows to emerging economies not only raised concerns about the risks of inflation and asset bubbles, but also increased appreciation pressures on some currencies (such as the renminbi and the Brazilian real). In some economies, exchange rate volatility increased dramatically (for

Chart 2.10 Performance of key international stock indices



Note: January 1 2007 = 100.
Source: Bloomberg.

Chart 2.11 Movements of various currencies against the US dollar



Note: January 1 2007 = 100.
Source: Bloomberg.

example, the Korean won) and could potentially compromise the stability of their financial markets and commodity prices (Chart 2.11). Moreover, in those countries with less flexible exchange rate regimes, large capital inflows could complicate the implementation of monetary and exchange rate policies, increasing difficulties to safeguard financial stability. The IMF encourages policymakers in these emerging economies to use macroeconomic policies and macroprudential policies in response to the capital inflow surges. Alternatively, introduction of capital controls could be considered given that these policy measures appear to be insufficient and the capital inflows are likely to be temporary.

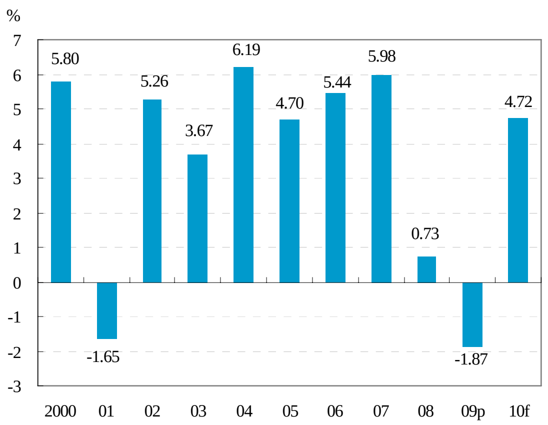
2.2 Domestic economic and financial conditions

In line with the ongoing revival of the global economy, Taiwan's economy recovered steadily and turned to positive growth in 2009 Q4. Domestic prices remained stable. Fueled by the current account surplus and ample foreign exchange reserves, short-term external debt servicing ability remained strong. Overall external debt servicing ability was robust due to a contraction in the scale of external debt. Nevertheless, the government's fiscal deficits widened along with rising government debt.

Domestic economy resumed growth

Driven by shrinking exports, slack private consumption and a sharp contraction in private investment, the economy dropped to negative growth of -9.06% and -6.85% in 2009 Q1 and Q2, respectively. In the latter half of 2009, benefiting from the global economic recovery, the momentum in exports strengthened. As the global economic outlook improved dramatically, along with rising private consumption and investment, and an expansion in public expenditure, the domestic economy showed signs of recovery. As a result of the fledgling economic recovery and the influence of a low base, the downward movement in domestic output improved significantly and posted negative growth of merely -0.98% in Q3. Moreover, the growth rate turned to positive 9.22% in Q4, the highest growth rate recorded since 2004 Q3. Based on DGBAS statistics (Chart 2.12), annual economic growth registered -1.87% for 2009, 2.60

Chart 2.12 Economic growth in Taiwan



Note: Figure for 2009 is preliminary, while figure for 2010 is forecast by DGBAS.
Source: DGBAS.

percentage points lower than the previous year.

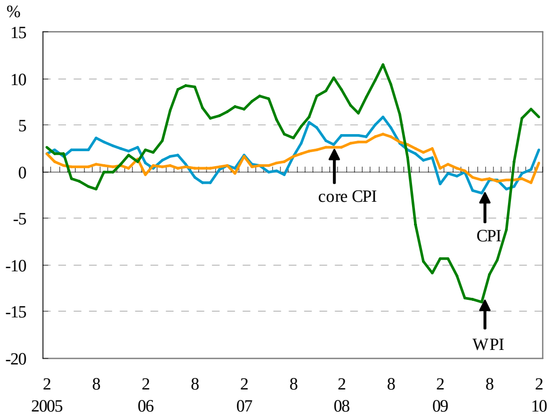
Looking ahead, the brighter global economic situation may continue to boost Taiwan's exports and private investment, and the mild growth in private consumption is likely to sustain. The DGBAS predicts annual economic growth will increase to 4.72%[14] in 2010 (Chart 2.12).

Domestic prices remained stable

The international prices of crude oil and agricultural and industrial raw materials rebounded from the beginning of 2009 as a result of the global economic recovery but exhibited a large decrease compared to the same period of the previous year. The wholesale price index (WPI) inflation rate continued to drop but gradually rebounded after reaching a trough of -13.99% in July 2009. The annual WPI inflation rate dropped to -8.74% in 2009, far below the 5.15% a year earlier. Affected by declines in oil prices, coupled with slackness in effective demand owing to higher unemployment rates and shrinking wages, the CPI inflation rate in 2009 was negative for eleven consecutive months, except for the Chinese Lunar New Year effect in January. Similarly, the core CPI[15] inflation rate was negative for seven consecutive months from June 2009 (Chart 2.13). The annual CPI and core CPI inflation rates in 2009 were -0.87% and -0.14%, respectively, lower than the 3.53% and 3.08% a year earlier.

The average WPI inflation rate from January to February 2010 accelerated to 6.31%, while the average CPI and core CPI inflation rates registered 1.30% and -0.06%,[16] respectively, over the same period (Chart 2.13). As the prices of crude oil and agricultural and industrial raw materials keep ascending in line with the upturn in global demand and abundant liquidity in the banking system, the DGBAS projects the annual WPI and CPI inflation rates in 2010 to rise to 4.78% and 1.27%,[17] respectively.

Chart 2.13 Consumer and wholesale price inflation rates



Note: Figures are measured on a year-on-year change basis.
Source: DGBAS.

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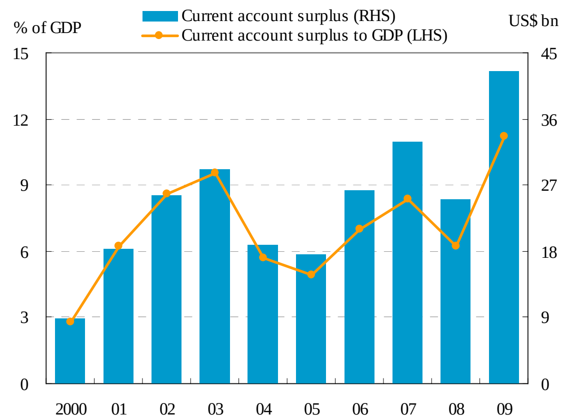
14 The figures are based on a DGBAS press release on 22 February 2010.
15 The term "core CPI" in this report refers to a consumer price index excluding perishable fresh fruits and vegetables, fish and shellfish, and energy.
16 The figures are based on a DGBAS press release on 5 March 2010.
17 The figures are based on a DGBAS press release on 22 February 2010.

Persisting current account surpluses and abundant foreign exchange reserves

Taiwan's imports and exports both experienced declines in the first three quarters of 2009. Nevertheless, the decrease in imports was larger than that of exports, and hence the current account surplus persisted. Meanwhile, there was an ongoing accumulation of the trade surplus caused by import and export surges in Q4. As a result, the annual current account surplus was US$42.57 billion in 2009, increasing notably by 69.46% compared to that in 2008. The ratio of the current account surplus in relation to annual GDP registered 11.22%[18] through the whole of 2009 (Chart 2.14).

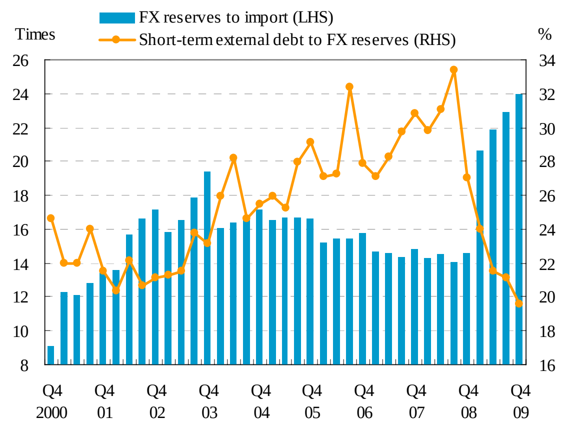
The balance of payments recorded a surplus of US$54.13 billion in 2009 owing to the continued current account surplus and sustained net inflows in the financial account from non-resident securities investments and other investments. This, coupled with the fact that major currencies (such as the euro and pound) held as part of the foreign exchange reserves appreciated against the US dollar over the same period, caused Taiwan's foreign exchange reserves to continue accumulating and reach a high of US$348.2 billion at the end of 2009, and further up to US$355 billion at the end of March 2010. Therefore, it reflects that foreign exchange reserves are sufficient. Moreover, foreign exchange reserves at the end of 2009[19] were enough to cover 23.96 months of imports, while the ratio of short-term external debt to foreign exchange reserves dropped sharply to 19.60% over the same period.[20] This was affected by the increase in foreign exchange reserves, as well as the decline in imports and short-term

Chart 2.14 Current account surplus



Note: Current account surplus and GDP are annual figures.
Sources: CBC and DGBAS.

Chart 2.15 Short-term external debt servicing capacity



Notes: 1. FX reserves and external debt are end-of-period figures.
2. Imports are average monthly figures.
Sources: CBC, DGBAS and MOF.

[18] For the ratio of current account deficit to GDP, the cutoff point for risk is 3%. A country in which the reading is greater than 3% and has risen by at least 5 percentage points from the previous year is considered to be at relatively high risk.
[19] A country with an import cover of foreign exchange reserves more than three months is considered to be at relatively low risk.
[20] The general international consensus is that a reading of less than 50% indicates relatively low risk.

external debt. These data imply that Taiwan's foreign exchange reserves have a strong capacity to meet payment obligations for imports and to service short-term external debt (Chart 2.15).

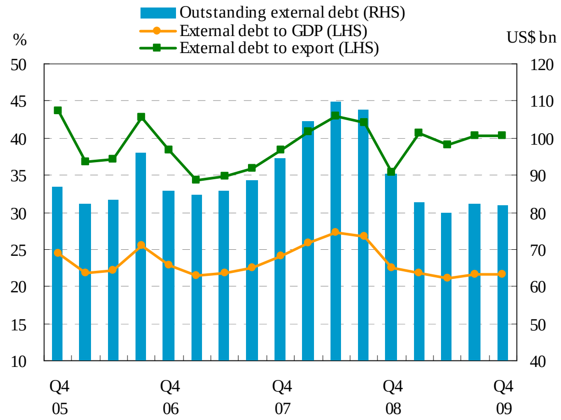
External debt contracted and debt servicing capacity remained strong

There was a substantial reduction in Taiwan's external debt[21] in the first half of 2009 caused by a fall in private external debt. However, external debt increased in 2009 Q3, triggered by increasing foreign capital inflows to local bond investments. Outstanding external debt rose to US$82 billion, or 21.62% of annual GDP, at the end of 2009.[22] Moreover, the ratio of external debt to annual exports stood at 40.27% as of the end of 2009, higher than a year earlier. Nevertheless, export revenues were still sufficient to cover external debt (Chart 2.16), and there were no signs of servicing pressure on external debt.[23]

Rising fiscal deficits increased government debt

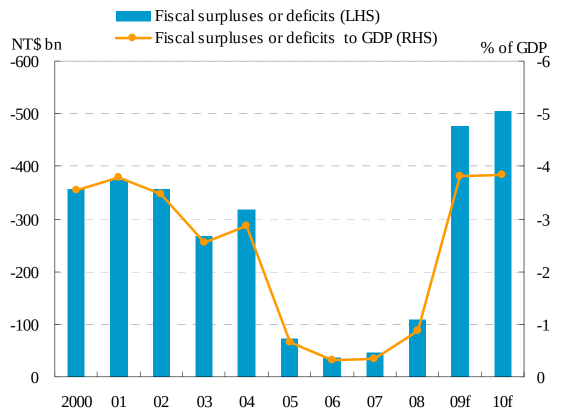
Driven by the implementation of measures aimed at revitalizing the economy and promoting consumption from September 2008 onwards, fiscal deficits trended upwards. The fiscal budget deficit in 2009 expanded to NT$476.4 billion, or 3.80% of annual GDP,

Chart 2.16 External debt servicing capacity



Notes: 1. External debt are end-of-period figures.
2. GDP and exports are annual figures.
Sources: CBC and DGBAS.

Chart 2.17 Fiscal position



Notes: 1. Fiscal position data includes those of central and local governments.
2. Data of fiscal surpluses (deficits) are end-of-period figures. Figures for 2009 and 2010 are budgeted ones.
Sources: MOF and DGBAS.

[21] External debt is defined by the CBC as the combined amount owed to foreign parties by Taiwan's public and private sectors, including long-term debt with a maturity of greater than one year and short-term debt with a maturity of one year or less. The term "public external debt" refers to debt that the public sector is either obligated to repay directly or has guaranteed (starting from December 2004, figures for public external debt include outstanding foreign debt arising from repo transactions between the CBC and international financial institutions). The term "private external debt" refers to private-sector foreign debt that are not guaranteed by the public sector.

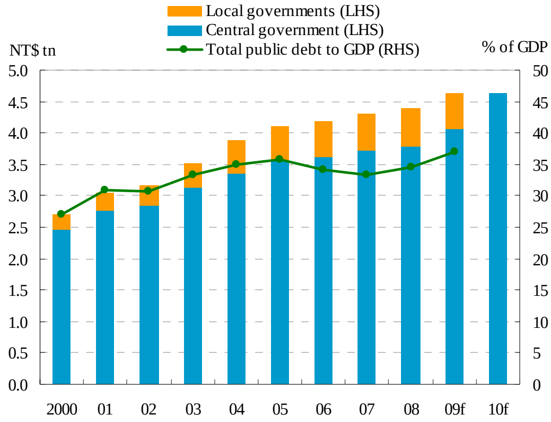
[22] The general international consensus is that a country with the ratio of external debt to GDP lower than 50% is deemed to be at relatively low risk.

[23] The general international consensus is that a ratio of external debt to exports of less than 100% indicates relatively low risk.

and the ratio may further increase to 3.85%[24] in 2010 (Chart 2.17).

In 2009, outstanding public debt at all levels of government[25] expanded to NT$4.64 trillion, or 37.03%[26] of annual GDP, well above the NT$4.38 trillion[27] in 2008, as fiscal deficits increased and central and local governments relied on debt issuance to finance debt servicing expenditures. It is expected that public debt is likely to grow further in 2010 on the back of increasing public debt for supporting the expansion of infrastructure construction expenditures (Chart 2.18).

Chart 2.18 Public debt



Notes: 1. Outstanding public debt refers to non-self-liquidating debt with a maturity of one year or longer, excluding external debt.
2. Outstanding public debt for 2009 and 2010 are budgeted figures; data of 2010 for local governments is not available.

Sources: MOF and DGBAS.

[24] Under the 1992 European Union Maastricht Treaty and the subsequent Stability and Growth Pact, fiscal deficits in EU member nations are not allowed to exceed 3% of GDP.

[25] The term "outstanding debt at all levels of government" as used in this report refers to outstanding non-self-liquidating debt with a maturity of one year or longer. Final audited figures for outstanding one-year-or-longer non-self-liquidating public debt (NT$4.4 trillion) issued by all levels of government during the 2008 fiscal year is equivalent to 35.01% of the average GNP for the preceding three fiscal years (NT$12.5 trillion). This figure is below the ceiling of 48% (i.e. 40% for central government and 8% for local governments) set out in the Public Debt Act.

[26] Under the Maastricht Treaty and the subsequent Stability and Growth Pact, outstanding debt in EU member nations is not allowed to exceed 60% of GDP.

[27] If adding in debt with a maturity of less than one year and self-liquidating debt, outstanding public debt at the end of 2008 stood at NT$5.33 trillion.