

I. Developments in the Real Economy

1. Overview

The fallout from the global financial crisis continued to overshadow Taiwan's economy during the first half of 2009. With the gradual recovery of the global economy, Taiwan's economy has regained momentum since the fourth quarter of 2009. The balance of payments remained in good shape and registered a record high surplus as the current account and net inflow on the financial account both reached historic highs. Meanwhile, falling prices of oil, vegetables and fruits led consumer prices to decline. The unemployment rate climbed to a record peak in August and then gradually trended downwards. As reduced revenues and increased expenditures due to tax cuts and the economic downturn, central government finances turned to a deficit, after registering surpluses for three years.

Gradual Recovery in the Second Half of 2009

In the first half of 2009, Taiwan's external trade declined, which in turn affected economic activity and the labor market. As a result, GDP growth was mired in negative territory. In the second half of the year, the nascent recovery of the global economy alleviated the decline in Taiwan's exports and GDP growth turned positive in the fourth quarter. In terms of domestic demand, the government adopted an expansionary fiscal policy, including consumption vouchers and infrastructure construction. However, economic doldrums continued in the first half of 2009, as unemployment rose, private consumption weakened, and firms delayed investment due to low capacity utilization. In the second half of the year, as emerging economies regained strength and the government's stimulus efforts bore fruit, private consumption and investment gradually picked up. For the year as a whole, Taiwan's GDP still shrank by 1.87 percent, compared to 0.73 percent growth in the previous year.

With regard to the expenditure components of GDP, both external and domestic demand were below favorable levels. Nevertheless, net external demand contributed 1.48 percentage points to GDP growth due to a larger decline in imports than exports. Domestic demand, on the other hand, subtracted 3.34 percentage points from GDP growth. On the production side, the industrial sector was more severely affected than the services sector with respective contributions of negative 1.47 and negative 0.15 percentage points to GDP growth.

Balance of Payments Surplus Hit a Historic High

On the current account, a greater decrease in imports over exports resulted in a goods trade surplus of US\$30.8 billion, a large increase of 66.6 percent from the previous year. Services recorded the first surplus ever, at US\$1.3 billion, due to a decrease in transportation and travel payments and an increase in travel receipts. Income surplus expanded to US\$12.7 billion mainly owing to a decrease in payments to equity investment by nonresidents. As a result, the current account surplus was US\$42.6 billion, a significant increase of 69.5 percent over the previous year.

The net inflow in the financial account was largely attributable to other investment, which exhibited a record high net inflow of US\$25.8 billion, as the government reduced estate and gift tax rates, the US actively tracked taxes on the affluent, and overseas businessmen repatriated funds. Portfolio investment by nonresidents also showed a large inflow of US\$21.4 billion, mainly for investing in Taiwan's stock markets and overseas depository receipts issued by Taiwan's businesses. Portfolio investment abroad by residents shifted to a net outflow of US\$31.7 billion, mainly as residents invested in foreign securities through banks' earmarked trust funds and life insurance companies invested in foreign bonds.

For the year 2009, the overall balance of payments recorded a surplus of US\$54.1 billion, posting a historic high.

Prices Remained Relatively Stable

Compared with the previous year, prices of oil and other international commodities declined significantly in 2009. Import prices decreased by 13.89 percent as denominated in the US dollar and by 9.61 percent in the NT dollar. The milder decline reflected a depreciation of the NT dollar against the US dollar. Therefore, the WPI decreased by 8.74 percent, the largest decline ever recorded.

Regarding consumer prices, import prices and retail prices were dampened by the decline in international commodity prices, while the rising unemployment rate and lackluster effective demand further depressed prices. As a result, the CPI decreased by 0.87 percent in 2009 and core CPI (excluding fruits and vegetables, fish and shell fish, and energy) decreased by 0.14 percent. Overall, price levels remained relatively stable in 2009.

Government Finance Turned into Large Deficit

For 2009, the central government revenue amounted to NT\$1,553.5 billion, 5.3 percent less than the previous year, mainly due to a significant decline in tax revenue dragged down by the economic downturn and tax cuts. Total government expenditure increased by 6.1 percent to reach NT\$715.5 billion after the government further stepped up public spending and social

welfare-related expenditure. Furthermore, a special budget of NT\$280 billion was allocated for economic stimulus measures such as the shopping voucher scheme, expanded infrastructure spending and Typhoon Morakot disaster relief and reconstruction efforts. In sum, the central government ran a deficit of NT\$162.0 billion, as opposed to a surplus of NT\$23.2 billion in the previous year.

To finance the fiscal deficit and debt principal repayment, the central government raised NT\$164.5 billion through issuing government bonds and borrowing from banks. The NT\$280.0 billion special budget also incurred a demand for debt financing. As a result, total outstanding debt of the central government amounted to NT\$4,141.9 billion at the end of 2009. The ratio of outstanding central government debt to the three-year average of nominal GDP rose from last year's 31.2 percent to 32.8 percent.

Rising Unemployment Rates

Economic recession took a toll on Taiwan's labor market in 2009, with a decrease in job opportunities and an increase in the number of workers involuntarily unemployed. The annual average unemployment rate increased by 1.71 percentage points over the previous year to 5.85 percent, the largest ever year-on-year increase. In response, the government launched short-, medium- and long-term measures to promote employment and raise the quality of human resources.