

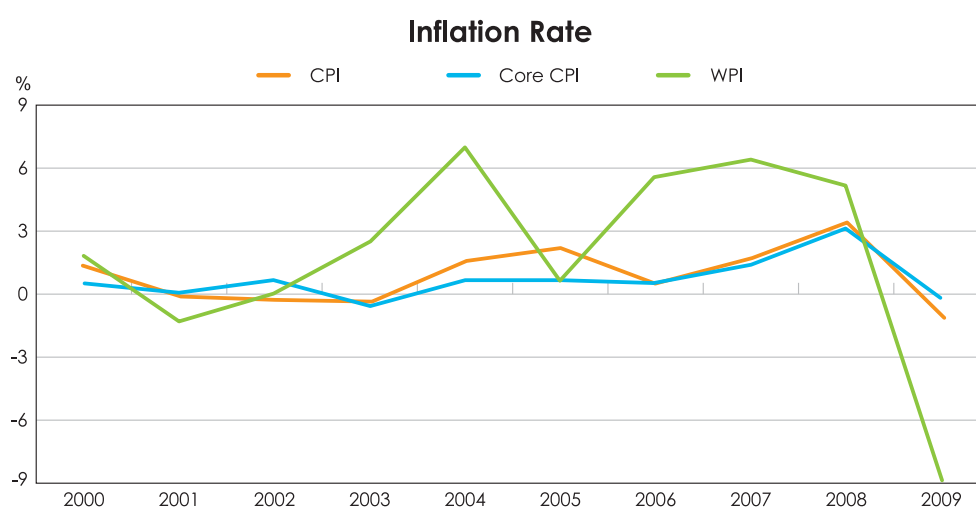
4. Prices

Taiwan's inflation fell into negative territory in 2009, largely driven by the steep drop in international commodity prices from the historically high levels reached in the previous year. In addition, slack domestic demand caused by rising unemployment and subdued compensation also dragged inflation down. Headline inflation, as measured by the consumer price index (CPI), declined to -0.87 percent in 2009, the lowest level on record. The core CPI, which excludes fruits and vegetables, fish and shellfish, and energy prices, fell by 0.14 percent in 2009, significantly lower than the 3.08 percent increase in the previous year.

Large Decrease in Wholesale Prices

The wholesale price index (WPI) decreased by 8.74 percent in 2009, the largest decline in history, mainly reflecting the sharp retreat from 2008's spike in international commodity prices in the face of a dampened global economy. In the first seven months of the year, the annual growth rate of the WPI displayed a downward movement and fell to an all-year low rate of -13.99 percent in July. Afterwards, it recovered and turned positive to reach 1.06 percent in November. To end the year, the WPI rose by 5.75 percent in December, owing to the low base effect caused by a dramatic fall in commodity prices in the same period of the previous year.

Broken down by the major components of the WPI, the annual rates of change of import prices, domestic sales excluding import prices, and export prices declined substantially in 2009, mainly on account of marked drops in international raw material prices.

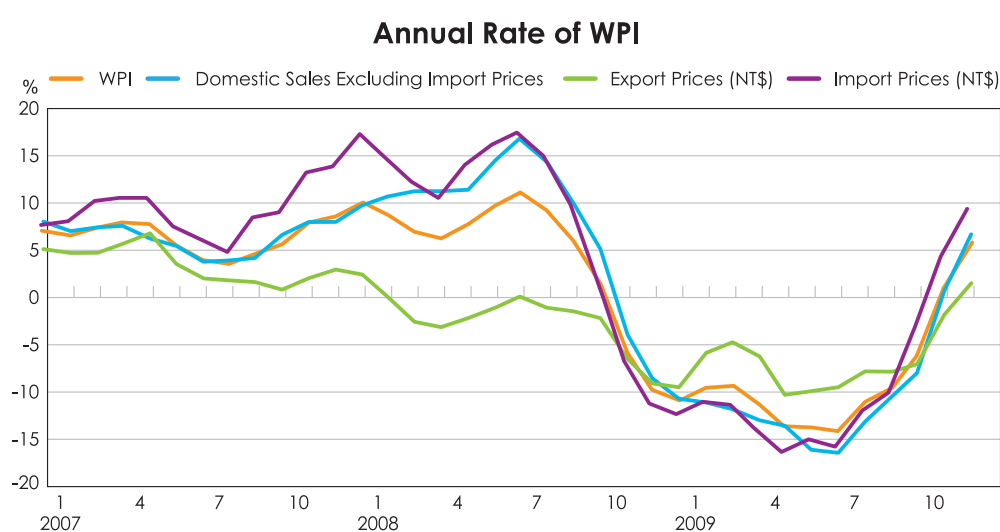


Source: Price Statistics Monthly, DGBAS, Executive Yuan.

Import prices fell by 13.89 percent in US dollar terms, the steepest drop in history, due to declining international raw material prices since the second half of 2008. In local currency terms, import prices only decreased by 9.61 percent, with the difference largely reflecting the depreciation of the NT dollar against the US dollar. Among the components of import prices, a 13.84 percent decrease in prices of raw materials, which account for 77.19 percent of imports, was the major contributor to the decline in import prices. In contrast, the prices of capital goods and consumer goods, which make up 15.97 percent and 6.83 percent of imports, increased by 8.19 percent and 4.28 percent, respectively.

The annual change in export prices in US dollar terms was -10.95 percent, compared with a 2.12 percent increase in 2008. Due to the depreciation of the NT dollar against the US dollar in 2009, export prices in terms of the NT dollar declined by 6.60 percent, compared with a 2.14 percent decrease in 2008.

Prices of domestic sales excluding import prices fell by 10.0 percent in 2009, notably lower than the 8.54 percent increase in the previous year. This was attributable to the drop in imported costs of primary commodities, and the consecutive decreases in the prices of domestic electronic components, computers, and electronic and optical products due to subdued domestic demand. Among the components of domestic sales excluding import prices, the prices of quarrying and mineral products and manufacturing products decreased by 16.76 percent and 12.31 percent, respectively. In contrast, the prices of water supply, electricity, and gas rose by 8.89 percent in the year because of the rising cost of electricity.



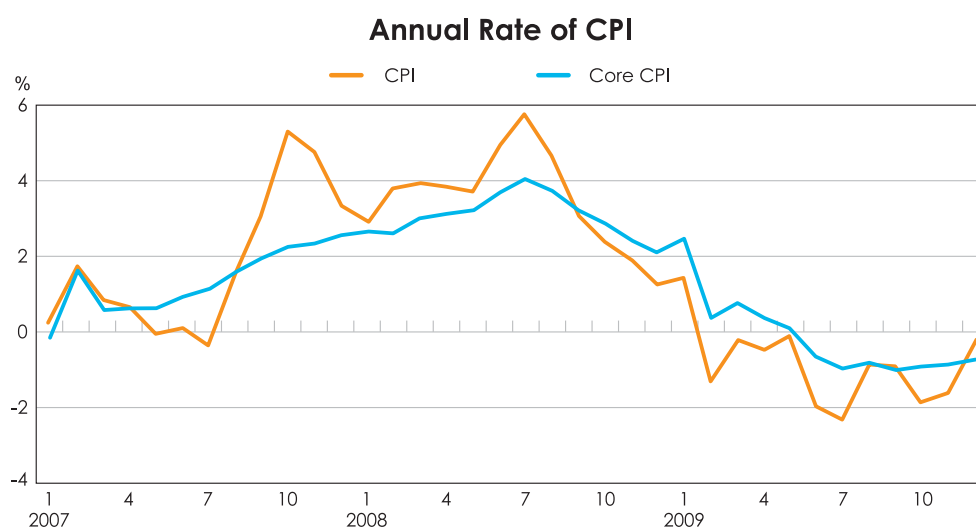
Source: Price Statistics Monthly, DGBAS, Executive Yuan.

Consumer Prices Moved Down Slightly

The CPI decreased at an annual rate of 0.87 percent in 2009, and monthly inflation rates stayed in negative territory throughout the year except for January. The decline in CPI inflation was driven by the pass-through effect from decreases in imported prices of raw materials into the general price level amid a weak global economy. In addition, sluggish domestic demand stemming from rising unemployment and subdued compensation added to the downward pressure on inflation. In particular, declining international oil prices, and prices for vegetables and fruits contributed minus 0.81 of a percentage point to the decline in the CPI. The core CPI inflation was -0.14 percent during 2009 as prices of other retail goods and services remained relatively steady.

The main downward factors contributing to the CPI decrease in 2009 were as follows:

- (1) Compared with the dramatic fall in the second half of 2008, international petroleum prices rebounded in 2009 due to the onset of global economic recovery, and a rise in market speculation. However, average international petroleum prices in 2009 still fell by 37.67 percent compared with 2008. As a result, the decline in the imported costs of petroleum and natural gas lowered domestic oil and gas prices, which fell by 10.40 percent and 8.92 percent and accounted for 0.37 and 0.10 of a percentage point in the CPI decrease, respectively.
- (2) Due to high base effects stemming from severe damage caused by typhoons and cold weather in 2008, prices of vegetables and fruits declined by 10.76 percent and 5.75 percent in 2009, and subtracted 0.28 and 0.16 of a percentage point from the CPI inflation rate, respectively.



Source: Price Statistics Monthly, DGBAS, Executive Yuan.

- (3) Prices of durable consumer goods fell by 4.73 percent and accounted for -0.33 of a percentage point to the CPI inflation rate, as slack domestic demand and fierce market competition made it difficult for firms to pass on higher costs to consumers, and prices of cars and motorcycles declined due to tax deductions enacted as part of domestic policy stimulus measures in 2009.
- (4) Education and entertainment prices decreased at an annual rate of 2.34 percent, subtracting 0.11 of a percentage point from the CPI inflation rate, mainly caused by the economic downturn, an H1N1 virus outbreak, and slashed prices of airlines tickets.
- (5) As fees of passenger transport, internet and cell phones adjusted downward, prices of transportation and communication services declined by 1.09 percent, deducting 0.08 of a percentage point from the CPI inflation rate.

The main upward factors contributing to CPI inflation in 2009 were as follows:

- (1) In line with the adjustment of the tobacco health and welfare surcharge from NT\$10 to NT\$20 in June 1, 2009, prices of tobacco and betelnut rose by 10.46 percent, contributing 0.15 of a percentage point to CPI inflation.
- (2) Prices of fish and shellfish increased at an annual rate of 4.36 percent in 2009 as their prices reveal an upward trend due to decreasing catch in the long term.

Percentage Changes in the Major Components of the CPI in 2009

Item	Weight (%)	Annual rate of change (%)	Contribution to CPI inflation rate (percentage point)
CPI	100	-0.87	-0.87
Tobacco & Betelnut	1.5	10.46	0.15
Fish & Shellfish	1.7	4.36	0.08
Food away from Home	8.9	0.70	0.07
Electricity	2.2	3.46	0.07
Total	14.3		0.37
Fuels and Lubricants	3.3	-10.40	-0.37
Durable Consumer Goods	7.5	-4.73	-0.33
Vegetables	2.5	-10.76	-0.28
Fruits	2.8	-5.75	-0.16
Education and Entertainment	4.3	-2.34	-0.11
Gas	1.0	-8.92	-0.10
Transportation & Communication Services	7.7	-1.09	-0.08
Total	29.1		-1.43
Others	56.6		0.19

Source: Price Statistics Monthly, DGBAS, Executive Yuan.

- (3) The cost of eating out, which went up in 2008 because of higher food prices and cooking costs, continued to rise modestly by 0.70 percent in 2009, as it is difficult for retailers to lower such prices.
- (4) Driven by higher imported prices for fuel, natural gas and heating oil inputs for electricity generation, electricity prices moved up by 3.46 percent.