

# I. Developments in the Real Economy

## 1. Overview

During the first half of 2012, Taiwan's foreign trade and private investment contracted and private consumption growth slowed, as external demand remained weak amid sluggish global economic growth. However, external demand gradually stabilized in the second half of the year, boosting both exports and investment back to positive growth, and the economy picked up steadily. For the year as a whole, GDP grew at a pace of 1.26 percent.

The balance of payments registered a larger surplus of US\$15,484 million as a record-high current account surplus of US\$49,550 million more than offset a net financial account outflow of US\$31,503 million. In terms of price trends, the annual growth rate of the CPI rose to 1.93 percent over the previous year, mainly reflecting fuel and electricity price hikes and weather-related price fluctuations for fruits and vegetables. Central government revenue showed only a marginal decline, but the marked increase in expenditure on social welfare and economic development led to a larger government deficit of NT\$215.9 billion. Conditions in the labor market improved further. The unemployment rate fell to 4.18 percent in December 2012, bringing the annual average to 4.24 percent.

### **Economic Growth Decelerated Markedly**

For the first half of 2012, with lackluster global economic growth and feeble external demand, the domestic economy experienced tepid export growth, slowing private investment and more conservative consumer spending. As a result, the economy contracted by 0.12 percent year on year in the second quarter. Over the next six months of the year, the global economy gradually stabilized, Taiwan's external trade grew at a faster pace, and private investment and consumer confidence rose steadily. Against this backdrop, GDP growth firmed up to a 3.72 percent year-on-year increase in the fourth quarter. For the year as a whole, the economy expanded by 1.26 percent, lower than the 4.07 percent of the previous year.

In terms of GDP components by expenditure, both external and domestic demand declined in comparison with the previous year. Domestic demand contributed merely 0.11 percentage points to the annual economic growth rate, while net external demand recorded a higher contribution of 1.14 percentage points. On the output side of GDP, the industrial and services sectors grew by 0.94 percent and 0.83 percent, respectively, affected by weak demand both at home and abroad. Their respective contributions to the GDP growth rate were 0.33 and 0.52 percentage points. The

agricultural sector growth was dragged down by unfavorable weather conditions to negative 5.82 percent, contributing -0.08 percentage points to the growth in GDP.

### **BOP Surplus Widened**

In 2012, the record-high surplus in the current account helped to offset the net outflow in the financial account. The overall balance of payments showed a larger surplus of US\$15,484 million, compared to US\$6,239 million a year earlier.

In the current account, goods exports and imports both shrank, reflecting the impact of waning external demand. Exports fell by 2.4 percent, compared to the 3.6 percent drop in imports. As the decline in exports was smaller than that in imports, the trade in goods surplus increased to US\$30,735 million in 2012 from US\$27,848 million in 2011. The services account also recorded a wider surplus of US\$6,137 million, mainly owing to gains both in the receipts of merchanting trade and in travel receipts. As for the income account, as the revenue from residents' investments in foreign exchange assets and portfolio investments increased and the payments for non-residents' income from equity security investments decreased, the income account surplus rose to US\$15,277 million. Combined with a narrower current transfer deficit, the overall current account surplus grew by 20.2 percent to US\$49,550 million, rising to a share of 9.8 percent in GNP.

The financial account recorded a net outflow of US\$31,503 million. Among the components, portfolio investments exhibited a record-high net outflow of US\$42,447 million, mainly accounted for by a higher net outflow in residents' portfolio investments abroad. The net outflow of direct investment abroad observed another new high because investment in the mainland area continued to increase, as against a net inflow of inward direct investment. Overall, direct investment showed a smaller net outflow of US\$9,826 million. Furthermore, other investment had a net inflow of US\$20,442 million, mainly attributable to withdrawal of overseas deposits by the private sector and increased foreign borrowing by the banking sector.

### **Prices Rose Mildly**

In 2012, international raw material prices trended lower on account of weak demand, leading Taiwan's import prices in NT dollar terms to fall by 1.28 percent, while prices for domestic sales and exports fell 0.59 percent and 1.62 percent, respectively. Consequently, the WPI decreased by 1.16 percent.

In terms of consumer prices, retail prices of some goods and services went up to reflect the price hikes in fuel and electricity. Prices of fruits and vegetables also climbed higher in the second half of 2012, caused by typhoons and torrential rain. For the year as a whole, the CPI grew by 1.93 percent. However, the core CPI (excluding prices of fruits, vegetables, and energy) edged up by

1.00 percent, a milder increase compared to the previous year.

### **Government Deficit Mounted**

As tax revenue was squeezed by the economic slowdown and government-owned enterprises kept running up losses, total central government revenue declined in 2012. On the other hand, fiscal spending further increased during the year to support social welfare, transportation infrastructure, and environmental protection. As a result, the central government deficit did not continue to shrink as in the prior three years but widened instead to NT\$215.9 billion, the largest deficit in the past nine years.

In regard to revenue, income tax revenue was significantly boosted by an increase in dividend income, whereas the majority of those tax revenues susceptible to economic moderation did not fare well in 2012. Consequently, overall tax revenue edged up 1.6 percent from the previous year, accounting for 73.3 percent of total central government revenue.

In 2012, central government expenditure built up, mainly attributable to the considerably greater spending on social welfare and economic development. By category, social welfare made up the top share of total expenditure at 22.3 percent, followed by education, science and culture at 19.1 percent, and then by national defense at 16.1 percent. The proportion of spending on economic development grew from the 12.5 percent of 2011 to 14.0 percent.

The widened fiscal deficit also represented a stronger need for debt financing. At the end of 2012, the total outstanding debt of the central government rose by NT\$247.0 billion to a record NT \$5.01 trillion, and its ratio to GDP went up further from the 34.8 percent of the previous year end to 35.7 percent.

### **Labor Market Conditions Continued to Improve**

Entering 2012, an increase in employment caused the unemployment rate to trend down to 4.10 percent in April, the lowest since August 2008. Afterwards, slowing economic growth and a seasonal effect of fresh graduates surging into the job market combined to drive the unemployment rate up to 4.40 percent in August. However, a subsequent economic pickup led the pace of unemployment growth to moderate. For the year as a whole, the unemployment rate was 4.24 percent, 0.15 percentage points lower than the year before.

Considering a sustained business demand for labor, the number of employed persons averaged 10.86 million for the year of 2012, up by 1.41 percent from the previous year. By sector, services employment increased the most, at 1.68 percent, while employment in the industrial sector and agriculture rose by 1.12 percent and 0.39 percent, respectively.

The average monthly earnings of non-farm (industrial and services sectors) workers were NT \$45,888 per person in 2012, slightly higher by 0.30 percent over the previous year. The average regular earnings of non-farm workers increased by 1.28 percent to NT\$37,346. In real terms, a year-on-year decline of 1.60 percent was recorded. The real regular earnings of non-farm workers fell by 0.64 percent compared to a year earlier. Unit labor cost advanced by 2.37 percent, reflecting a 0.75 percent drop in the labor productivity index of the industrial sector and an increase in total employee earnings.

