

I. Developments in the Real Economy

1. Overview

Taiwan's economic growth accelerated to 5.70 percent in 2007 from the 4.03 percent in the previous year. The major driving forces were strong exports and a pickup in private investment and consumption. Although the current account surplus hit a record high, it was less than the net outflow on the financial account. The balance of payments thus exhibited a relatively small deficit. As surging international commodity prices and a typhoon-induced vegetable price hike weighed on inflationary pressure, the CPI rose by 1.80 percent, a moderate level compared with other countries. The unemployment rate was 3.91 percent, the same as in the previous year and the lowest since 2001. Moreover, central government finance continued to improve and recorded the largest budget surplus since 1999.

Solid Economic Growth

In 2007, Taiwan's GDP expanded by 5.70 percent, outperforming the 4.89 percent in the previous year. Exports remained vigorous as strong demand from emerging economies more than offset the effect of the subprime mortgage crisis-ridden U.S. and Europe. Domestic demand picked up gradually against a dwindling impact of credit card defaults. Private investment continued to grow mildly, led by semiconductor companies' capacity expansion.

Economic growth was mainly driven by external demand, which contributed 3.74 percentage points to economic growth. The manufacturing industry accounted for 2.65 percentage points of economic growth, the largest contribution among all sectoral components. The services sector grew moderately and accounted for 71.06 percent of domestic production. Per capital GNP reached US\$17,294 in 2007, an increase of US\$800 from the previous year.

Small Deficit in Balance of Payments

In 2007, the balance of payments registered record highs in both current account surplus and financial account net outflow. The current account surplus reached US\$31.7 billion or 8 percent of nominal GNP. The financial account exhibited a net outflow of US\$38.9 billion. As a result, the foreign reserve assets held by the Bank slightly decreased by US\$4 billion, which was relatively small compared with the foreign exchange reserves of Taiwan.

Increase in exports exceeded that in imports. Therefore, the trade surplus on goods grew

to a record high of US\$29.4 billion, up 25.8 percent year over year. Taiwan's exports to Vietnam and India grew notably, and Vietnam has become Taiwan's second largest export market. Due to an increase in technical service expenditures, the services account deficit went up to US\$5.4 billion. Surplus on the income account increased to US\$11.5 billion owing to growth in residents' direct investment income and investment income on foreign exchange reserves. Net current transfer payments decreased to US\$3.8 billion because of the increase in inward remittances. Capital account deficit shrank to US\$0.1 billion as acquisitions of intangible assets decreased. The financial account net outflow reached a historic high, mainly due to a surge of residents' overseas investment.

Rising Inflationary Pressure

Taiwan's wholesale price index (WPI) increased by 6.46 percent in 2007 due to a surge of international commodity prices and a depreciation of NT dollars against US dollars. The skyrocketing international raw material prices and a typhoon-induced vegetable price hike both added to inflationary pressure. The CPI inflation rate was 1.80 percent for 2007, higher than 0.6 percent of the previous year but still below the 2 percent target set by the Council for Economic Planning and Development. Core CPI (CPI excluding fresh fruits and vegetables, fish and shellfish, and energy) went up by 1.35 percent, over the 0.52 percent of 2006. Both CPI and core CPI inflation were moderate compared with other countries.

Continuously Improved Employment

Thanks to sustained economic expansion and the government's job-creating programs, labor market conditions continued to improve. The unemployment rate was 3.91 percent, the lowest since 2001. The average labor force participation rate was 58.25 percent, an increase of 0.33 of a percentage point from the previous year. The labor force participation rate for females hit another new high while that for males remained on a declining trend.

The annual average employment reached a new high of 10 million and 294 thousand persons and a growth of 1.81 percent year over year. Among the components, employment in the services sector increased by 1.8 percent and employment in the manufacturing industry rose by 2.37 percent.

The average monthly earnings of workers in the non-farm sectors increased by 2.28 percent from the previous year to NT\$45,112. After deflated by CPI, real monthly earnings rose by 0.47 percent from 2006. As the increase in total production outpaced that in total working hours, the labor production index for the manufacturing industry went up by 7.47 percent. Higher growth in labor productivity than in earnings led to a decrease of 5.37 percent in unit labor cost in the manufacturing industry, among which the drop in the electronic parts and components

industry was the most striking.

Strengthening Fiscal Position

The central government finance continued to improve. With steady economic expansion, continuous tax reform and curtailment of government expenditures, the central government's fiscal revenue outpaced its expenditure. In 2007, central government revenue increased by NT\$86.1 billion over the previous year to NT\$1,632.5 billion, mainly supported by a NT\$114.4 billion surge in tax revenue. Central government expenditure, however, increased moderately by NT\$23.1 billion over the previous year to NT\$1,552.9 billion. As a result, the central government finance exhibited the largest budget surplus of NT\$79.6 billion since 1999.

Although the general budget of the central government for 2007 did not require any debt financing, the special budget still relied on bond issuance and borrowing as financing sources. Total outstanding debt of the central government continued to increase by NT\$98.5 billion over the previous year-end to NT\$3,723.6 billion at the end of 2007. Nevertheless, the ratio of outstanding central government debt to GDP dropped to 29.6 percent, indicating better fiscal conditions with lighter debt burdens.

