

# I. Developments in the Real Economy

## 1. Overview

As external demand slumped amid the global downturn and domestic demand also contracted, Taiwan's economy weakened considerably in 2008. GDP growth decelerated to 0.12 percent accompanied by a marked rise in unemployment. Although current account surplus decreased, a lower net portfolio outflow in the financial account supported an overall balance of payments surplus of US\$26.3 billion. Inflation sped up in the first half of the year driven by surging international raw material prices, but then subsided with waning demand at home and abroad. The CPI increased by 3.53 percent in 2008, a relatively stable level among major countries. Central government finance remained in surplus for the third year, while registering a large decline from the previous year.

### **Economic Growth Slowed**

With strong demand from emerging economies, Taiwan's economy recorded a robust growth of 5.40 percent in the first half of 2008. However, the economic landscape was subsequently reshaped by a global downturn. GDP growth plunged to a negative 4.74 percent in the second half of the year with sharp contraction in exports, private consumption and investment. For 2008 as a whole, GDP recorded a growth of 0.12 percent, down from 5.70 percent in 2007. For the year, per capita GNP in nominal terms increased by US\$277, reaching US\$17,576.

Among all the expenditure components of GDP, net external demand continued to provide solid support to economic growth, contributing 2.17 percentage points to real GDP growth for the year. On the contrary, affected by reductions in consumption and investment, domestic demand growth fell sharply, posting a negative contribution of 2.05 percentage points for the year.

On the supply side, manufacturers cut production as global demand declined. The services sector, which accounted for 73.17 percent of GDP, contributed 0.5 of a percentage point to economic growth for the year, down from 2.90 percentage points in 2007.

### **Balance of Payments Exhibited Surplus**

In 2008, the current account surplus decreased to US\$25.0 billion due to a sharp decline

in goods exports, and accounted for 6.2 percent of nominal GNP, while the financial account showed a mild net outflow of US\$1.8 billion. As a result, the foreign reserve assets held by the Bank increased by US\$26.3 billion.

As the global economic downturn adversely impacted Taiwan's trade performance, exports grew by a mere 3.4 percent and imports growth slowed to 9.6 percent in 2008. As a result, the trade surplus on goods fell to US\$18.2 billion for the year, a decrease of 40.3 percent from the previous year. Due to an increase in service receipts and a decrease in service payments, the services deficit declined to US\$678 million in 2008. Surplus on the income account increased to US\$10.5 billion with surging income from residents' direct investment. Net current transfer payments decreased to US\$3.0 billion due to a decrease in outward remittances by residents to support their overseas relatives.

Capital account deficit rose to US\$334 million as acquisitions of intangible assets increased. The financial account exhibited a mild net outflow of US\$1.8 billion, as the net foreign portfolio outflow reached a historic high, while portfolio investment by residents exhibited the first net inflow on record.

### **Inflation Pressures Stepped Up**

Taiwan's inflation was elevated during the first three quarters of 2008 due to sharp increases in energy and food prices. Afterward, a downturn in sales and production, along with steep declines in the prices of energy and other commodities and a strengthening NT dollar against the US dollar, contributed to a substantial lessening of inflation pressures.

The headline inflation, as measured by the consumer price index (CPI), rose 3.53 percent in 2008, notably higher than the 1.80 percent increase in 2007. The core CPI, which excludes the direct effects of movements in fruits and vegetables, fish and shellfish, and energy prices, rose by 3.08 percent in 2008, also faster than the previous year's 1.35 percent.

### **Fiscal Position Remained in Surplus**

For 2008, central government finance remained in surplus for the third consecutive year at NT\$16.3 billion. However, the figure represented a large decline from the NT\$83.4 billion recorded in 2007 as the increase in government expenditure outpaced tax revenue. In 2008, central government revenue increased by a mere NT\$1.6 billion over the previous year to NT\$1,637.1 billion, mainly supported by an increase of NT\$34.3 billion in tax revenue. Income tax revenue was bolstered by robust economic growth in 2007, while revenue from securities transaction taxes and commodity tax trended down.

Central government expenditure increased by NT\$68.8 billion over the previous year to

NT\$1,620.8 billion, mainly driven by the increase in general subsidies and other expenditure to enhance the financial conditions of local governments. Meanwhile, to boost domestic demand and promote economic growth, the central government expanded infrastructure investment and set aside NT\$130.0 billion in a special budget for the Expansion of Investment in Infrastructure Construction. As a result, the ratio of central government expenditure to GDP rose to 13.1 percent, while the ratio of budget surplus to GDP dropped to 0.1 percent in 2008.

### **Unemployment Trended Upward**

Taiwan's labor market witnessed an unfavorable trend of rising unemployment rates amid an economic slowdown under the impact of the global financial crisis in 2008. In the first half of the year, employment grew at a healthy pace with steady economic expansion. However, the labor market softened from September, with slower employment growth and increasing unemployment rates.

To help boost employment, the government undertook a series of job creation plans in the last quarter of the year. Nevertheless, average employment grew by only 1.06 percent in 2008, slower than the previous year's 1.81 percent. The number of unemployed people reached a record high of 549 thousand in December, despite the government's job creation plans. The average unemployment rate for the whole year stood at 4.14 percent, the highest level since 2005.

In terms of earnings and labor cost, the average monthly earnings per worker in the non-farm sector inched up by a mere 0.02 percent over the previous year to NT\$44,424. As the decline in total production outpaced that in total working hours, the labor productivity index for the goods-producing sector decreased by 1.04 percent. The index of unit labor cost increased by 2.15 percent, resulting from a decrease in total production and an increase in total labor compensation.