

# I. Developments in the Real Economy

## 1. Overview



Taiwan's economy, bolstered by exports and private consumption, expanded at a moderate rate of 4.09 percent in 2005, after reaching a seven-year high of 6.07 percent in 2004. The pace of expansion slowed down in the first half of the year as exports lost steam amid softening global growth. Local manufacturing bounced back strongly in the second half of the year, largely benefiting from an upturn in consumer electronic products exports. Moreover, fostered by an improving job market, private consumption increased at a steady and moderate rate and helped support activity throughout the year. Breaking a six-year declining streak, the growth rate of government expenditures crept into positive territory. Private investment, however, dipped in the second half of the year and ended up subtracting slightly from growth.

The balance of payments registered an overall surplus of US\$20.06 billion in 2005, following the US\$26.6 billion surplus a year earlier. This surplus was primarily due to buoyancy in exports and a net capital inflow. The surplus on trade in goods rose by 11.59 percent to US\$18.0 billion. However, due to a rise in the outward remittance of investment income by non-residents, the current account surplus narrowed by US\$2.13 billion to stand at US\$16.37 billion, or 4.73 percent of GDP. The financial account recorded a net inflow of US\$1.78 billion, the result of a higher net inflow in other investment partly offsetting the net outflows in both direct investment and portfolio investment.

Consumer price index (CPI) inflation edged higher to 2.3 percent in 2005. Soaring food prices contributed 1.93 percentage points of the CPI advance as severe typhoons drove up vegetable and fruit prices, and oil and gas prices contributed 0.27 of a percentage point. The core CPI, however, remained rather subdued and rose just 0.65 percent as a result of intense competition in product markets and stable services prices.

Labor market conditions improved further, mainly attributable to the enforcement of the government's Project for the Creation of Job Opportunities, combined with the steady economic recovery during the second half of the year. The average unemployment rate edged down to 4.13 percent in 2005, its lowest level since 2001, while the average labor force participation rate rose to its highest level since 2000.

The central government was in a better fiscal position this year. Reflecting steady economic expansion, continued tax reform and curtailment of expenditures, the central government's fiscal revenue growth greatly outpaced its expenditure growth. As a result, the ratio of the central government's fiscal deficit to GDP declined from 1.83 percent in 2004 to 0.94 percent in 2005.

