

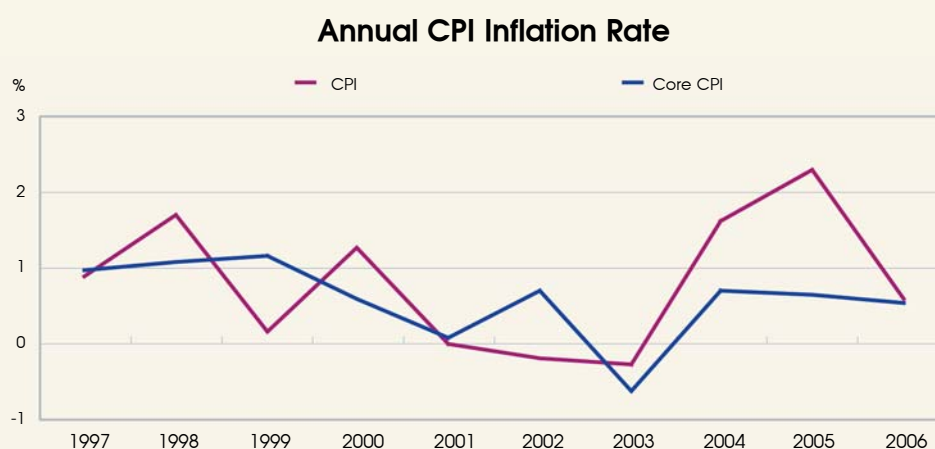
4. Prices

Taiwan's wholesale price index (WPI) rose by 5.64 percent in 2006, largely reflecting the continuing surge in international primary commodity prices and the weak New Taiwan dollar. However, the headline consumer price index (CPI) inflation rate remained low and stable. The CPI rose only by 0.60 percent as a decrease in vegetable prices, a decline in output unit labor cost, intense competition in the domestic retail market and slackened domestic demand alleviated most of the upward pressure from higher tobacco health taxes and soaring energy prices. The core CPI (consumer prices excluding fresh fruits and vegetables, fish and shellfish, and energy) rose by 0.54 percent.

Steep Increase in Wholesale Prices

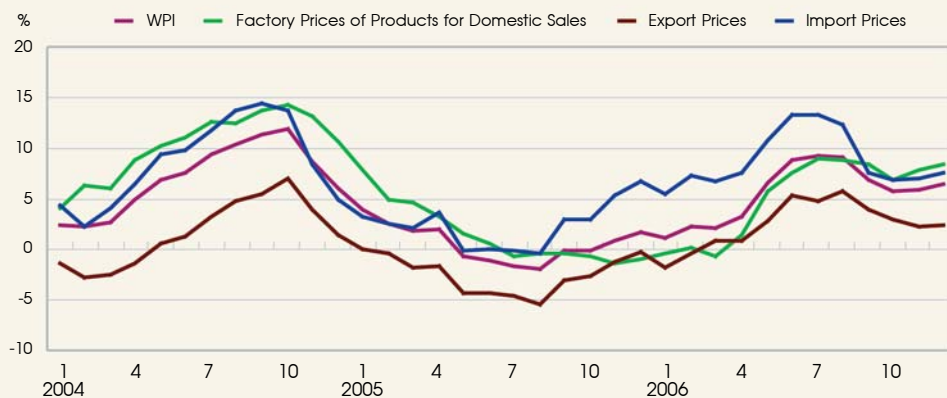
The WPI annual rate increased to 5.64 percent in 2006. Broken down by the major components of the WPI, factory prices of products for domestic sales and import prices rose markedly, while export prices remained moderate.

In US dollar terms, import prices increased by 7.61 percent as robust demand for crude oil, iron, steel, copper, rubber, chemicals and plastics pushed up prices of primary commodities. In local currency terms, import prices increased 8.82 percent as the 1.1 percent depreciation of the NT dollar against the US dollar aggravated the increases in prices. Factory prices of products for domestic sales rose by 5.27 percent, reflecting the increase in global primary commodity prices, despite the decline in domestic vegetable, fruit, livestock and poultry, and



Source: Price Statistics Monthly, Republic of China, DGBAS, Executive Yuan.

Annual Change Rate of WPI

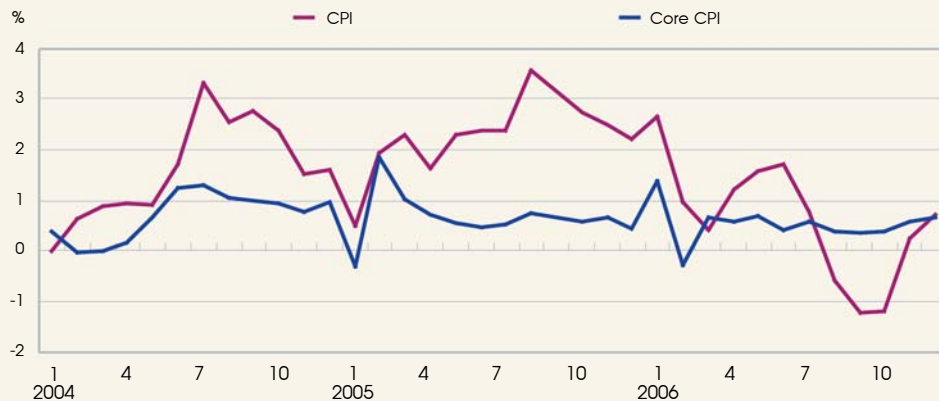


Source: Price Statistics Monthly, Republic of China, DGBAS, Executive Yuan.

electronic product prices. Export prices in terms of the US dollar and the NT dollar increased moderately by 1.32 percent and 2.50 percent, respectively, as prices of Taiwan's exports, especially IT products including computers, communication and audio-video equipment, went down due to highly competitive international markets.

Commodity prices typically increase as economic activity accelerates and capacity utilization rises, especially in cases where the supply is relatively fixed in the short run. The wholesale prices of products for domestic sales rose by 6.89 percent for the year 2006. Among the components, the prices of raw materials and intermediate materials rose by 14.54 percent and 7.96 percent, respectively. However, they accounted for a small share of total production costs, and thus the increases had little effect on overall CPI inflation. More importantly, market competition promoted by globalization made it difficult for firms to pass on higher input costs to consumers, thereby, the prices of finished goods only edged up by 0.25 percent.

Annual Change Rate of CPI



Source: Price Statistics Monthly, Republic of China, DGBAS, Executive Yuan.

Stable Consumer Prices

The core CPI inflation rate fluctuated remarkably in the first two months of 2006 due to seasonal factors influenced by the Chinese New Year holidays. However, from March onwards, the core CPI inflation rate remained in a steady range between 0.35 and 0.70 percent and edged up by 0.54 percent for the year as a whole. The mild core CPI rate reflected weak consumption demand, intense domestic market competition and relatively stable services prices.

The CPI rose by 0.60 percent in 2006, with most of the increase coming from the first half of the year. The CPI inflation rate fell to negative territory for three consecutive months starting from August mainly due to the high-base effect of vegetables and fruits prices.

The main upward factors contributing to CPI inflation in 2006 were as follows:

- (1) Tobacco and betel nut prices rose by 11.30 percent due to an upward adjustment in tobacco health taxes.
- (2) The hike in international petroleum prices caused significant increases in domestic oil and gas prices by 11.31 percent and 9.79 percent, respectively, pushing electricity and transportation fees up in Taiwan.

During the same period, however, the main factors offsetting CPI inflationary pressures

Percentage Changes in the Major Components of the CPI in 2006

Item	Annual change rate (%)	Contribution to CPI inflation rate (percentage point)
CPI	0.60	0.60
Food	-0.67	-0.18
Vegetables	-8.95	-0.33
Fruits	1.04	0.03
Fish & Shellfish	0.70	0.01
Energy	7.97	0.43
Oil	11.31	0.30
Gas	9.79	0.10
Electricity	1.36	0.03
Core CPI	0.54	0.46
Garments	-4.35	-0.14
Durable Consumer Goods	-1.65	-0.12
Communication Fees	-3.14	-0.09
Tobacco & Betel Nut	11.30	0.27
Medical Care Services	4.37	0.12
Tutorial Fees	2.29	0.06
Residential Rent	0.21	0.04

Source: Price Statistics Monthly, Republic of China, DGBAS, Executive Yuan.

were as follows:

- (1) The high-base effect brought the year-on-year vegetable prices down by 8.95 percent.
- (2) Services prices remained relatively stable. For example, communication fees continued on a downward stream since 1995 and helped to lessen inflationary pressures.
- (3) Driven by increased productivity and subdued upward pressure on wages, unit labor costs were down for the fifth consecutive year.
- (4) Domestic demand slackened as a result of the weak private consumption caused by credit card and cash card defaults, and this, in turn, led to decreases in prices of semi-durable consumer goods (such as garments) and durable consumer goods (such as computers, communication and audio-video equipment).

