

# Taiwan Economic and Trade Development

## A. Economic growth

The Taiwanese economy, as an export oriented economy, was badly affected by the financial crisis. The first half of 2008 was characterized by high growth rates (6.2 % for the first quarter, 4.5 % for the second quarter) and inflation due to sharp increases in energy and food prices. The global financial turmoil began filtering through the real economy from September 2008, when demand of major overseas markets dropped. As a result exports declined sharply, inflation came to an abrupt end and industrial production contracted significantly. The labour market responded quickly to the economic situation, resulting in a sharp increase of unemployment in the last quarter of 2008. Growth rates for the third and fourth quarter of 2008 stood at -1.0% and -8.6 % respectively, resulting in an overall growth rate of 0.06 % in 2008.

In 2009, government statistics recorded negative growth rates for the first half of the year, but the DGBAS (Directorate-General of Budget, Accounting and Statistics) forecasts a positive GDP growth for the last quarter of 2009. GDP per capita in 2008 was estimated at US\$ 17 083.

## B. Money and Finance

Motivated by media reports of further improvements in cross-strait economic trade relations between Taiwan and China, Taiwan's stock markets were buoyant in the first two quarters of 2008. However, the expansion of the global financial crisis made Taiwan's stock indices fell sharply in the second half of the year: in October 2008, the stock exchange index plummeted 47.5 % with respect to October 2007.

On the other hand, the impact of the global financial turmoil on Taiwan's banking and insurance sector has been relatively limited due to regulatory restrictions on the exposure to risky assets that Taiwanese banks and insurance companies have to observe. Moreover, in its 2008 reports, the Central Bank considered the asset quality of the overall banking sector in Taiwan healthy, due to continuing efforts to write off and sell non-performing loans. The ratio of non-performing loans in domestic banks decreased from 1.8 % in January 2008 to 1.5 % at the end of 2008. The government also follows closely the ongoing financial consolidation in what she considers an overcrowded banking sector. In 2008, a total of six M & A deals were completed, of which three involved foreign banks (HSBC, DBS and Standard Chartered Bank), which is, according to the Financial Supervisory Commission, a strong indication of foreign participants' commitment to Taiwan's financial market.

The NT dollar shifted from appreciation in the first quarter of 2008 to depreciation in the third quarter of 2008, due to outward remittances by foreign investors. Over the whole of 2008, the NT dollar traded on average 31.5 against the USD. Volatility in the NT dollar exchange rate increased to 6 % by mid 2008, then returned to a more steady state.

In December 2008 Taiwan's foreign exchange reserves amounted to US\$ 291.7 billion, an increase of US\$ 21.4 billion in comparison with Dec. 2007, making Taiwan the holder of the world's fourth largest exchange reserves, behind China, Japan and Russia. The main factors contributing to the increase in foreign exchange reserves were: firstly the appreciation of the Euro, Yen and other major currencies against the US dollar, which made foreign exchange reserves denominated in these currencies worth more in terms of the base currency, the US dollar, and secondly returns from foreign exchange reserves management.

For 2008, central government finance remained in surplus for the third consecutive year at NT\$ 16.3 billion, with budget surplus standing at 0.1 % of GDP in 2008. This figure represents a considerate decline from the NT\$ 83.4 billion surplus in 2007. The decline can be attributed to the increasing government expenditures in 2008 resulting from the increase in general subsidies to enhance the financial conditions of local governments and the extra investments in infrastructure in 2008.

Against the background of the economic crisis, the Central Bank has cut discount rates from June 2008 on. Standing at 3.6 percent in June 2008, discount rates have been cut by 162 basic points to 2.0 percent in December 2008. In 2009, discount rates were reduced further to 1.2 percent in February 2009.

### **C. Foreign Trade**

Despite the economic downturn, Taiwan's total trade continued to expand in 2008. Total trade amounted to US\$ 496.0 billion, a rise of 6.4 % in comparison with 2007. Exports posted an increase of 3.6 % in 2008, surpassing the record year 2007 with a total amount of US\$ 255.6 billion. Imports recorded a 9.6 % increase in 2008.

The trade figures for 2008 as a whole conceal dramatic shifts in export and import figures during the year. The first half of 2008 exhibited health growth figures for both import and exports: imports and exports increased by 21.4 % and 14.4 % respectively between January and September 2008. From October to the end of the year, imports and exports dropped significantly with respect to the previous year, by 22.9 % and 24.7 % respectively. In 2009, trade figures continued this downward trend: in June 2009, imports stood at 66.5 % of the level of June 2008, exports at 69.6 % of the level of June 2008. On a more positive note, signs of recovery became apparent during the first six months of 2009 as both imports and exports increased at a month-to-month basis and recorded much higher levels in June 2009

than in January 2009 (imports stood at US\$ 15.1 billion in June against US\$ 8.9 billion in January 2009, exports stood at US\$ 16.9 billion in June against US\$ 12.3 billion in January 2009).

China remained Taiwan's most important export market in 2008 with a share of 26.1 % of Taiwan's total exports and an annual increase in export of 7.1 %. Although exports to the US and to Hong Kong fell by 4.1 % and 13.9 % respectively, (the largest decrease since 2001 in the case of the US), both are still important export partners of Taiwan: Hong Kong was its 2<sup>nd</sup> most important export partner commanding a share of 12.8 % of Taiwan's total exports in 2008, whereas the US took the third place in the ranking with a share of 12.0 %. Also the ASEAN countries have become important trade partners of Taiwan. Export to these countries rose by 7.2 % in 2008, accounting for 15.2 % of total exports. Export to the EU27 stood at 10.9 % of total trade. Interestingly, within the EU, trade with the new member states seem to have been hit the most hard: export to and import from these countries decreased sharply, whereas the rest of the EU exhibited a moderate increase in export and no change in the level of import. Main export items in 2008 were: electronics (34.0%), machinery (10.6%), optical, photographic, precision and medical instruments (8.4 %), mineral fuels (7.2%) and plastics (6.7%).

Total imports grew more significantly than total exports in 2008: an increase of 9.6% was recorded over the whole of the year. Japan, China and the US are the largest importing countries with respectively 19.3%, 13.0% and 10.9% shares of total trade. The EU27 commands a share of 8.1 % of total imports. Main import items in 2008 were: mineral fuels (25.7%), electronics (19.6%), machinery (9.7%), iron and steel (6.2%), optical, photographic, precision and medical instruments (4.3%).

Because of the gap between the growth percentages of exports (3.6%) and imports (9.6%), the traditional large trade surplus decreased to US\$ 15.1 billion. The trade surplus with the US, Korea and Hong Kong decreased sharply (respectively -19.8%, -39.4% and -13.7%), while the trade surplus with important trading partners such as the EU, Singapore, Malaysia and Indonesia showed an upwards trend (respectively 19.1%, 19.9%, 55.6% and 29.9%).

#### **D. Industry and Commerce**

Industrial production registered an average decrease of 1.8 % in 2008, the first negative growth rate since 2001. Mostly industrial production within the consumer goods sector got hit hard by the economic downturn, resulting in a decrease of 5.3%. From January to June 2009, industrial production fell by 24.3 % but showed signs of recovery in the second quarter of 2009 as consumption picked up.

## **E. Labour**

In the first half of 2008, employment grew at a healthy pace with steady economic expansion. However, employment growth started to slow down from September, resulting in a record high of the number of unemployment in December 2008 – 549 000 persons. The government undertook a series of job creation plans in the last quarter of the year to boost employment, but the average employment growth was still limited to 1.0 % in 2008. The average unemployment rate for the whole year stood at 4.1 %, the highest level since 2005. In the first two quarters of 2009 the downward trend on the labour market continued. The average unemployment rate stood at 6.0 % in July 2009.

As for the employment by industry, 5.1 % of Taiwan's labour force was working in the primary industry, 36.8 % in the secondary industry (mining, manufacturing, construction and utilities) and 58.0 % in the tertiary industry (commerce, transportation and other services) in 2008. While 58.0 % of the labour force was working in the services industry, the service sector accounted for 73.3 % of GDP in 2007, which indicates opportunities for employment growth in this industry. In 2008 the average monthly earnings in the industry and services sector amounted to NT\$ 44 424, staying at about the same level as in 2007.

## **F. Consumption and Investment**

Private consumption growth has been seriously hurt by the falling stock and housing prices. The government launched a new scheme of monthly relief subsidies for low-income households and a short-term employment program which should mitigate this effect. For 2008 as a whole, private consumption decreased by 0.3%. Also private investment fell sharply by 13.2%, reflecting the worldwide tendency for companies to put capital expenditures on hold. Government investment increased slightly by 0.3 % in 2008, but is forecasted to grow by 22.3 % in 2009, due to infrastructure development plans and notably the i-Taiwan projects, 12 major construction projects put forward by the new administration from May 2008.

With a share of 70.5 % of all outward investment in 2007, China remains the main destination for Taiwan's outward investment. According to the statistics of the Mainland Affairs Council, the accumulated investments of Taiwan accounted for 5.4 % of all investments into China in March 2009, which makes Taiwan the fifth most important investment source. The share of yearly Taiwanese investment into China has in general been on the decline: whereas Taiwan's investment represented 8.3 % of the total foreign direct investment in China in 1996, this had decreased to 2.0 % in 2008. However, in recent years it has been noticed that offshore financial centres such as the Virgin Islands have attracted a lot of investments from Taiwan and are figuring prominently among the top 10 of the largest investors in China. There is a possibility that Taiwanese companies are investing in China through these so-called tax

havens, which would make the actual investment amount of Taiwan into China much higher.

The regions most popular among Taiwanese businesses in China have been the Pearl River Delta (Guangdong province) and the Yangtze River delta or the Shanghai-Nanjing-Hangzhou triangle (Jiangsu, Zhejiang and Fujian provinces and Shanghai). These provinces absorbed more than 63.8 % of all Taiwanese investments in China in 2008. The sectors attracting the greatest amount of Taiwanese investment have been electronic parts and components, electrical and optical products and electrical equipment. Till 2008 Taiwanese companies were allowed to invest a maximum of 40 % of their net asset value into China. From August 2008 on, the Taiwanese government eased this investment limit to 60 % of the net asset value. Subsidiaries of multinational companies in Taiwan will be exempt from any investment limit on their investments in China, which will boost Taiwan's position as a regional headquarter and a stepstone to China and other Asian countries. On June 30, the Taiwanese government opened 192 business sectors to Chinese investors, including 64 sectors in the manufacturing industry, 117 in the service industry, and 11 in public construction.

Taiwan's outward investment apart from China stood at US\$ 4.4 billion at the end of 2008. The Caribbean islands, Singapore and Vietnam were the most popular investment targets. The US, traditionally a popular investment target for Taiwanese companies, saw inward investments from Taiwan falling by 70.3 % in comparison with the record year 2007. By contrast, Asian countries raised their share of total outward investments (except for China) to 45 % in 2008.

***Taiwan outward investment apart from mainland China in 2008 –US\$1000***

	Cases 2008	Amount 2008	% of total amount 2008	Amount 2007	% of total amount 2007	% change
<b>Total</b>	387	4,466,491	100	6,469,978	100	-31.0
<b>Caribbean Sea</b>	58	1,686,462	37.8	1,578,468	24.4	6.8
<b>Singapore</b>	14	697,626	15.6	1,194,110	18.5	-41.6
<b>Vietnam</b>	31	639,325	14.3	109,282	1.7	485.0
<b>US</b>	67	399,576	8.9	1,346,020	20.8	-70.3

*Source: Investment Commission, Ministry of Economic Affairs*

The greatest share of Taiwan's investment overseas (40.2%) went to the financial and insurance sector (mostly to investment holding companies), while electronics manufacturing got the second largest proportion with 20.2%.

Inward investment in Taiwan in 2008 amounted to US\$ 8.2 billion in 2008. The financial and insurance sectors absorbed 53.1 % of the combined value of investment, followed by the electronic parts and components manufacturing (8.3 %). The distribution of this investment is

reflective of the major transformation foreign investment is going through. While previously most foreign investment was concentrated in the industrial sectors, the last few years foreign investors have moved into financial services and communications. In 2008 the US, the European countries (notably the Netherlands), and the Caribbean islands were among the main sources of foreign investment in Taiwan, occupying a share of 34.7% and 14.8% of the total FDI respectively.

**Taiwan inward investment in 2008 – US\$1000**

	Amount 2007	% of amount 2007	Amount 2008	% of amount 2008	% change
<b>Total</b>	15,361,173	100	8,232,059	100	-86.60
<b>US</b>	3,147,520	20.5	2,856,815	34.7	-10.18
<b>Europe</b>	7,096,393	46.2	2,139,396	74.9	-231.70
<b>Netherlands</b>	6,313,591	41.1	1,620,085	56.7	-289.71
<b>Caribbean Sea</b>	2,396,465	15.6	1,219,924	42.7	-96.44

Source: Investment Commission, Ministry of Economic Affairs

In the World Competitiveness Report 2009-2010 of the World Economic Forum, Taiwan is ranked 12<sup>th</sup> out of 133 countries globally and 4<sup>th</sup> in Asia in terms of global competitiveness. According to the report, Taiwan has now entered the third and most advanced stage of development as defined by the Global Competitiveness Index framework, which means that innovation gets more weight in the overall score (15 %). As a result, Taiwan now gets fully rewarded for its outstanding capacity to innovate, ranking 6<sup>th</sup> out of the surveyed countries for its innovation capacity. The Economist Intelligence Unit's 2008 IT competitiveness survey ranked Taiwan 2<sup>nd</sup> in the world and 1<sup>st</sup> in Asia, ahead of Japan and Korea due to its strong performance in the R & D environment.

## G. Price

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 contributed to a substantial lessening of inflation pressures. According to the Directorate General of Budget, Accounting and Statistics, Taiwan's inflation rate, as measured by the consumer price index (CPI), raised by 3.5 % for 2008. The CPI started at relatively low levels at the beginning of the year and peaked at 5.8 % in June, to decrease during the second half of the year to 1.27 % in December 2008. The Wholesale Price Index (WPI) exhibits a similar pattern, peaking at 11.4% in July and then decreasing sharply during November and December 2008 because of decreasing crude petroleum and natural gas prices. The WPI rate for 2008 was 5.1%. The

decline of commodity prices in the second half of 2008 lowered inflation risk and improved real income growth among customers.

During the first half of 2009, both the CPI and the WPI exhibited negative growth, raising worries of deflation. In the first 7 months CPI was 0.7 % and WPI 11.7 % lower than in the same period of last year.