

CHINESE TAIPEI

MIXED PERFORMANCE 2003

Chinese Taipei's economic performance in 2003 was mixed. The year began with the threat of US-led war in Iraq, which led to a slow-down in the global economy. As a result, first-quarter GDP growth in Chinese Taipei was a disappointing 3.5% down on following the strong recovery of fourth-quarter 2002. Although the US-led Iraq war had ended by second-quarter 2003, outbreaks of SARS across the Pacific region in the beginning of the second-quarter created havoc in all the regions economies, with Chinese Taipei among the worst hit. Chinese Taipei GDP contracted by 0.08% in the second quarter, and private consumption shrank by a disastrous 1.81%.

The government has implemented a number of stimulus measures to curb the various negative impacts of SARS including, the injection of NT\$50 billion special budget for the prevention of SARS and compensations of SARS victims, a NT\$20 billion employment bill for the affected labour force and a fiscal stimulus of NT\$57.7 billion in public projects in an attempt to revive the sluggish economy.

With an estimated multiplier effect of 1.02 for public projects and a timely end of the SARS epidemic, economic activities in Chinese Taipei quickly recovered. GDP growth in third-quarter 2003 was a robust 4.18%. By the fourth-quarter, consumer confidence had returned, driven by a

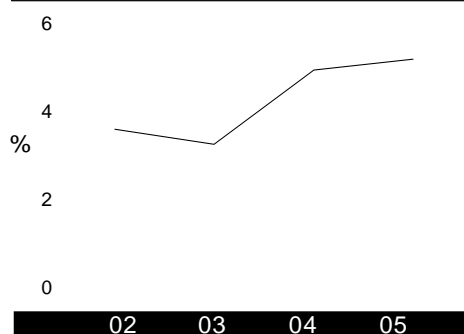
surge in foreign direct investment in the financial market and a bullish fixed asset market. Private consumption has returned to pre 2000 levels and the GDP growth in the fourth-quarter was 5.17%.

The economy grew by 3.24% in 2003. The unemployment rate remained around 5% for most of the year, and the consumer price index lingered around zero per cent with a yearly average of -0.28% . The strength of the international economic recovery—most notably, the better than expected economic growth in the United States—has led to the expansion of manufacturing production in Chinese Taipei and prompted increased private sector capital investments. As the Taiwan Stock Exchange (TAIEX) remains bullish, foreign institutional investors have been keen to invest in Chinese Taipei, and the TAIEX composite index has appreciated by over 34% in 2003.

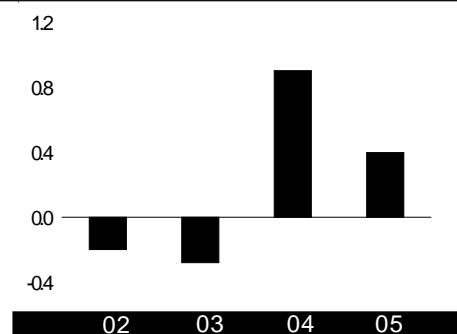
OUTLOOK 2004–2005

World trade will recover with the improved international economic climate. Chinese Taipei is a small open economy that depends heavily on international trade; Chinese Taipei's exports are buoyant when the US market is expanding. Total exports grew 10.5% in 2003, reaching a total of US\$144.2 billion. In terms of domestic consumption, the bullish financial market and the continuing boom in fixed asset markets are expected to fuel the growth

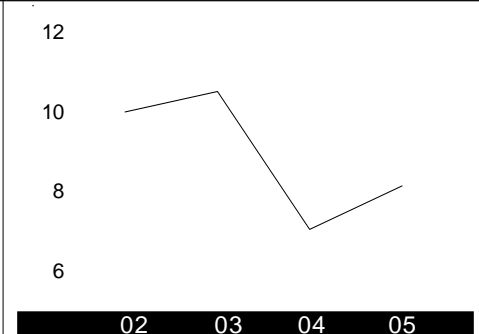
GDP growth



CPI inflation



Export growth



momentum. Private fixed investment is expected to grow by 14.5% in 2004. Furthermore, various public projects, including the high-speed railway and other public services, will help to fuel the growth for both private consumption and private investment. The Directorate-General of Budget, Accounting and Statistics forecasts GDP growth of 4.74 per cent, whereas the Taiwan Institute of Economic Research forecast is at a more optimistic 5.1%.

The OPEC's decision to reduce crude oil output means that oil prices are likely to remain high. An increase in the price of raw materials such as basic metal and petrochemical products has increased the cost of manufacturing export products. Appreciation of the new NT dollar has so far offset some of the increased price of raw materials. The consumer price index for 2004 is forecast by Taiwan Institute of Economic Research to be 0.9% and the wholesale price index 2.26%.

Although the US economic recovery appears robust, there is no inflationary pressure and the job market recovery has been slow. Thus the Federal Reserve is unlikely to raise interest rates during the year. The Central Bank of Chinese Taipei is likely to implement a loose monetary policy given the lack of inflationary threat and will follow to the US Federal Reserve's movements closely. Although the Bush Administration has reaffirmed its commitment to a strong dollar policy, the US dollar has fallen against all major currencies. Since the Central Bank of Chinese Taipei is committed

to the stabilisation of the NT dollar exchange rates, despite increasing pressure on other Asian currencies to appreciate, appreciation of the NT dollar will remain a gradual process.

At the beginning of 2004, the DPP (Democratic Progressive Party) government attempted to pass a five-year NT\$500 billion stimulus package in public construction. Had the public construction bill been voted through, it would have added an extra one per cent to GDP per annum. The bill was not voted through in the legislative branch of the government (Legislative Yuan) due to political infighting. However, the bill is expected to be passed during the second term of the legislative office in 2004. Given this, GDP growth for Chinese Taipei in 2004 is expected to exceed 5%.

RISKS

The biggest uncertainty lies in the US economy. The worsening US trade and budget deficit is likely to affect the stability of US dollar exchange rate. A sharp fall in the US dollar will reduce demand for imported goods in the United States causing world trade to contract.

China will also have a major influence on Chinese Taipei's economic performance. China, together with Hong Kong, is now Chinese Taipei's largest trading partner. Given China's growing importance in world trade, an unstable Renminbi is likely to affect the world economy, and Chinese Taipei will be among the worst affected. Therefore, the stability of the Renminbi will be one of the most important stability factors not just for

Chinese Taipei but the entire Asia Pacific region.

Relations between China and Chinese Taipei have not been cosy. Chinese Taipei's ever-increasing investment and trade with China make cross-strait relations more important now than ever and political tensions between the two even more costly.

Another major factor is the presidential election. The fiercely contested election was won by the incumbent Mr. Chen Shui-bian by a margin of only 29,000 votes, less than 1 per cent of all votes. The election saw an unusually high number of spoiled ballots, prompting the KMT and its allies to call the election unfair and refuse to concede defeat. Thousands of opposition supporters rallied in front of the presidential palace in Taipei on 20 March in protest against the outcome of the presidential polls.

The impact of the political unrest thus far appears to be marginal and the concerns for stability unfounded. The latest figures released by the Directorate-General of Budget, Accounting and Statistics suggest that trade figures have not been affected with both export orders and exports still strong.

The Taiwan Institute of Economic Research monthly survey of the manufacturing sector found very optimistic business sentiment. Some 97% of businesses in the 57 industries surveyed agreed that the current business climate was positive and would remain at least as buoyant if not better over the coming months. Only 3% of the businesses surveyed thought it would get worse.

TIER Business Climate Index

The composite indicator of the business climate, seasonally adjusted moving average, achieved a historic high of 117.97 in March 2004, the highest level since the Index first began in 1979.

Source: Taiwan Institute of Economic Research, April 2004.

