TAIWAN'S ECONOMY IN 2018: GROWTH DECELERATION IN THE WAKE OF CHINA-US TRADE WAR

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Executive Summary

1. Taiwan's economy in 2018 is expected to grow by 2.66% with GDP (gross domestic product) per capita progressing to US$25,048. Moderate export expansion contributed to economic growth in the first half of the year whereas domestic demand is likely to be the main economic pillar in the later half of 2018.

2. The economy has shown a clear deceleration to 2.27% in the third quarter of 2018, from over 3% in the previous two quarters. The negative contribution from net exports (-1.69%) for the first time since Q3 2016 is the main cause for the slowdown.

3. Private consumption has remained resilient thanks to the growth in salary (4.4% of year-on-year increase in the first three quarters of 2018), and relatively low inflation (1.7%) and unemployment rate (3.7%) in 2018 (Jan-Sep).

4. The escalating China-US trade war may weigh down Taiwan's economic growth potential. In 2016, eight out of the top 10 US-bound exporting companies in China were Taiwanese firms, many of which rely on importing key components from Taiwan for final assembly in China.

5. China-based Taiwanese firms responded to the trade war by either increasing production capacity on other manufacturing sites outside China or relocating factories to other countries. Some have planned to move production line back to Taiwan.

6. The impact from the China-US trade war on Taiwan's economy has so far been limited as consumer electronic products are not included in the current high tariff list against Chinese products. China and Hong Kong remain as Taiwan's largest export destinations, accounting for 41% of Taiwan's total exports in 2018 (Jan-Nov).

7. If America expands tariffs to an additional US$267 billion worth of goods, almost all Chinese goods would be affected. The weakening global demand due to the lingering effect of the trade war will overshadow Taiwan's export-oriented economy.

8. From a positive point of view, the China-US trade war provides an opportunity for Taiwan to diversify its external economic relations. Taiwan's slower economic progress over the last two decades indicates that its reliance on exports to China can no longer be a strong engine for economic growth.

9. While China remains as Taiwan's most important investment destination, accounting for 43% of Taiwan's total outward foreign direct investment (OFDI) in 2018 (Jan-Oct), Taiwan's export-oriented firms will need to move out to other countries, leaving behind domestic market-oriented firms to grasp local market opportunities.

10. With China's economic transformation and Trump's plan to bring the manufacturing sector back to the United States, the global supply chain network is about to change. Taiwan is in urgent need of more diversified free trade agreements to cope with the changing global economic structure.