

Economic Outlook in the Wake of the Presidential Elections

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Now that the presidential election is over; some are satisfied, whereas some are disappointed with the election outcome. But many citizens are quite discontent that various factors in this election, such as Chinese intervention, the timing of the election, and the merging of the presidential and legislative elections, favored a certain political camp. Still, it is up to voters to discuss all this in the next presidential election in four years' time. That's what makes Taiwan's democratic system so precious. That the election turned out as it did is, of course, closely related to the economic environment. Taiwan faces dramatic challenges given that the international political and economic situation in 2012 is expected to change drastically.

Now that the election is over we should return to discussing policies that have to do with economic and livelihood issues. This is particularly important now that the World Bank has markedly lowered its global economic growth forecast and warns that the world economy is unstable, the European debt crisis continues to widen, actual risk is as high as during the financial tsunami of 2008, and that a global recession as severe as a financial crisis could erupt. In this situation government and opposition should stand together and do their best to consider how to prepare for a possible economic slump and how to jointly solve the fundamental livelihood and economic problems.

Given the bleak economic outlook for 2012 and unanswered questions such as whether the European sovereign debt crisis and the slowing Chinese economy will be able to stage a soft landing and whether the U.S. economy will continue its slow recovery, the Taiwanese economy will have to struggle to achieve a reassuring 4 percent of growth. The composite

leading indicators compiled by the Organization of Economic Cooperation and Development (OECD) show a continued slowdown so that the world economy is forecast to perform worse in 2012 than last year. Iran, the world's fifth largest oil producer, insists on developing nuclear weapons and constantly seeks confrontation with Israel. Oil prices could soar as a result, which adds another big unknown to the global economic situation. Worldwide the major economic forecasting institutions expect the American economy to post a growth rate of just 1.0 percent. At the same time longstanding trends such as society's aging and structural unemployment are still severe, while domestic consumption is only a weak growth driver due to lacking consumer confidence. This is a big negative factor for all export-oriented economies including Taiwan.

European Union (EU) leaders have declared they will jointly take action to deal with the European debt crisis. But in the coming years the European countries need to aggressively cut their deficits and reduce government debt so that we won't see expansionary fiscal policy again, while social welfare spending is likely to be slashed. Private households will tighten their belts and companies will invest less so that domestic consumption in the Eurozone won't provide enough growth momentum. At the same time the predicted continued economic slump in combination with an unstable, volatile political, economic and social situation will make banks less inclined to grant loans. Given weak corporate investment and consumer confidence, economic growth in the Eurozone is not likely to be strong in the coming year.

With the United States and Europe, two major economies, not doing well, world economic

growth will be affected correspondingly. Should the European debt crisis grow worse, Taiwan's major trade partners including the United States and China will see an economic recession, which in return will affect Taiwanese exports. This is also the major reason why economic forecasters generally believe that Taiwan's economic growth rate will successively decline from quarter to quarter. We cannot optimistically expect growth momentum from domestic consumption given the unstable international economic situation and the bleak outlook for the stock and real estate markets. Consequently corporations have become conservative about next year's growth prospects, which will affect their readiness to invest as well as the progress of investment projects.

The latest national income statistics by the Directorate-General of Budget, Accounting and Statistics (DGBAS) show that Taiwan's investment registered negative growth of 3.35 percent in 2011. Although the contraction was not as severe as in 2008 and 2009, when negative growth reached 12.36 percent and 11.25 percent, respectively, but the downturn in investment is a major reason for sluggish domestic demand. With regard to the economic outlook for 2012, we need to seriously consider the lack of domestic investment momentum and the crowding out effect from excessive investment in China, and prudently propose concrete counter measures.

On top of the deteriorating economic situation, it is critically important for Taiwan's unscathed survival during the next economic recession that the reelected Ma government is able to draw a valuable lesson from its policy failures during the 2008 financial crisis. When the Ma government issued shopping coupons to respond to the financial crisis in the past, a widespread phenomenon was that consumers first spent their coupons instead of spending cash out of their own pockets. This proved in the end that the coupons

had only a currency substitution effect, yet failed to boost domestic demand and to alleviate the impact of the financial crisis. Since the NT\$82.9 billion worth of shopping coupon was financed through a fully debt-financed special budget, the government's fiscal stability was damaged further, causing a more severe fiscal imbalance and greater tax unfairness.

A big tough question that the Ma government will have to ask itself is how much room is there left for fiscal policy given the worsening fiscal deficit and the severe imbalance between government revenues and expenditures. After years of severe fiscal imbalance, the government had to borrow one out of every four dollars spent in 2011, which means that the financial deficit has reached a critical point.

Ministry of Finance data show that Taiwan's outstanding debt totaled NT\$4.9213 trillion at the end of 2011, which means that government debt as share of total expenditure already nears the 40 percent ceiling set in the Public Debt Act. The government will soon be left with no room for raising new debt. The government's improper spending and waste of money has increased the public's already high discontent with regard to fairness and justice. Examples of such wasteful spending are an estate and gift tax cut for high-income earners, a salary hike for military personnel, civil servants and teachers, annual expenditure of NT\$70-80 billion in interest subsidies for preferential savings accounts carrying 18 percent interest (for retired civil servants), the central government footing the huge bill for the 2010 Flora Expo in Taipei, NT\$80 billion worth of debt financed shopping coupons, infrastructure budget slack, and financial support for events to mark the 100th anniversary of the founding of the Republic of China, and production of the musical Dreamers.

How will the government, as pledged during

the election, address the social dis-location of the bust generation? How will it respond to public discontent over the perceived lack of fairness and justice? Now that five special municipalities have been created, the central and local governments rush to deal with the resulting problems. There is the specter of a possible slowdown of the Chinese economy, the question how the fourth nuclear plant can safely begin commercial operation, and whether the contract manufacturing model of the electronics industry is still feasible given razor-thin margins. Taiwanese banks have granted a total of NT\$600 billion in loans to the four big “bust” industries – display panels, LEDs, semiconductors, and solar energy. This amounts to more than 3 percent of the total loan volume. Once these four big ailing industries default on their loans, two to three years’ worth of bank profits will be gone.

When helping financially distressed industries, how can the government reduce the excessive risks that the banking industry is forced to bear, and how can it prevent that the entire nation has to foot the bill? No matter which camp you voted for in the presidential election; when it comes to all these problems we have no choice but to jointly bear the possible consequences of government policy success or failure. Against this backdrop, how could think tanks and scholars not continue to take an interest in and watch over the government’s performance? **BT**