

2. Monetary Management

Lowering Policy Rates to Bolster Economic Growth

For the year 2020, the spread of the COVID-19 pandemic plunged the global economy into a severe contraction. To mitigate pandemic-induced impacts on the domestic economy and on employment, and to preempt the adverse implications of massive cross-border capital flows for financial stability, the Bank announced a policy rate cut in March. The discount rate, the rate on refinancing of secured loans, and the rate on temporary accommodations were reduced by 0.25 percentage points to 1.125%, 1.5%, and 3.375%, respectively, effective March 20, 2020.

Conducting Open Market Operations to Ensure Stable Growth of Monetary Aggregates

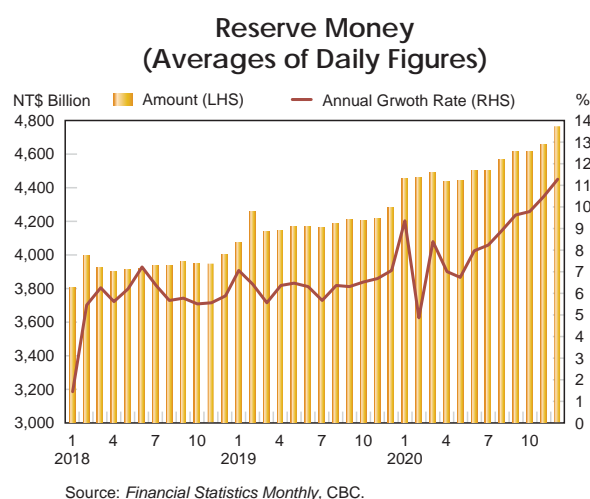
In 2020, the Bank managed market liquidity through open market operations by issuing CDs in response to domestic economic and financial conditions, which helped maintain reserve money, monetary aggregates, and the overnight call loan rate at appropriate levels.

(1) Managing Market Liquidity

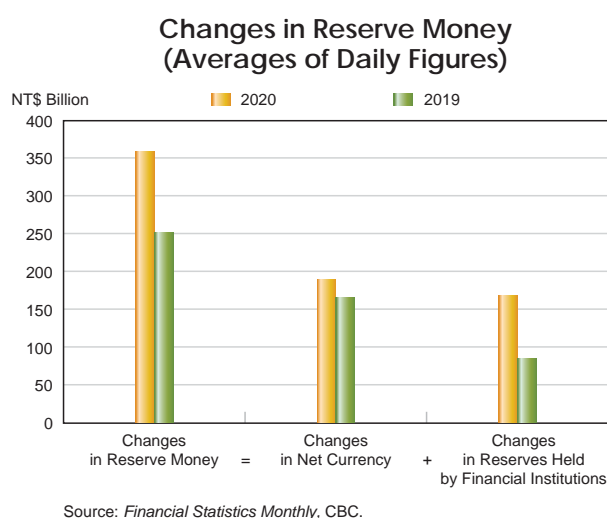
The Bank continued to conduct open market operations by issuing CDs. At the end of the year, the total outstanding amount of CDs issued by the Bank was NT\$9,168 billion.

(2) Higher Growth in Reserve Money

Reserve money grew at a faster pace of 8.59% for the year 2020, 2.17 percentage points higher than the previous year's figure. In terms of the monthly movements of reserve money, the annual growth rates of reserve money for January and February are often more volatile as the exact timing of the Lunar New Year holidays shifts on the Gregorian calendar each year. In 2020, reserve money posted an annual growth rate of 7.08% during this period. Afterwards, the annual growth rate hit a yearly low of 6.75% in May, mainly because of net foreign capital outflows. Demand for funds increased with a domestic economic recovery from June onwards, and banks' demand for reserves rose with net foreign capital inflows from October. The annual growth rates of reserve money continued to rise in subsequent months and reached a yearly high of 11.34% in December.



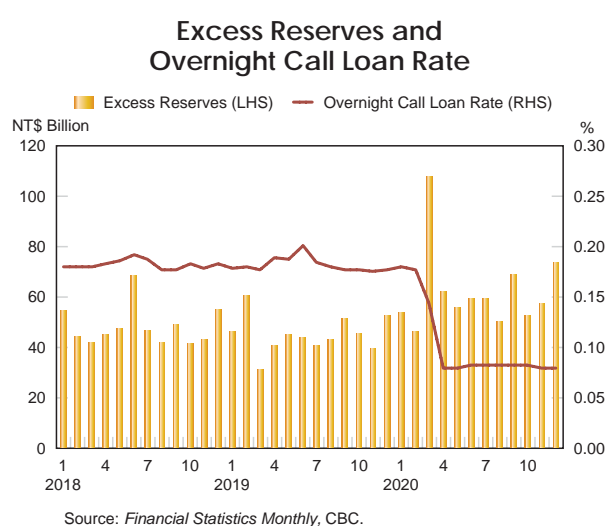
On the demand side, reserve money, measured on a daily average basis, increased by NT\$360 billion over the previous year. Of the components, net currency increased by NT\$190 billion and the annual growth rate rose to 9.17% from 8.77% the previous year; reserves held by financial institutions expanded by NT\$170 billion, with the annual growth rate trending up to 8.02% from 4.02% the previous year. Currency held by the non-bank public grew moderately because the Bank's policy rate cut in March led the interest rates paid on bank deposits lower, enhancing the willingness to hold currency in hand. Meanwhile, the overall growth rate of banks' reserves increased compared to the previous year as higher growth in transaction deposits raised banks' demand for reserves.



From the supply side perspective, reserve money increased by NT\$538 billion at the end of the year. According to the balance sheet of the Bank, which revealed the sources of changes in reserve money, the increase was mostly attributable to the growth in foreign assets held by the Bank and expanded claims on financial institutions, whereas the decrease was due to the Bank's issuance of CDs.

(3) Overnight Call Loan Rate Broadly Stable

In 2020, the Bank continued to conduct open market operations to maintain excess reserves and the overnight call loan rate at appropriate levels in the midst of the COVID-19 pandemic. In response to the pandemic, the Bank adjusted the issuance frequency of 7-day, 91-day, and 182-day NCDs and ceased to issue 14-day NCDs from April onwards to strengthen the effect of the NCD rates on the market rates. The annual average excess reserves of financial institutions reached NT\$63 billion, higher than the NT\$45 billion of the previous year. The annual average overnight call loan rate was at 0.180% before the policy rate cut in March, after which the overnight call loan rate stayed broadly stable



at around 0.080%.

(4) Conducting Regular Small-Scale Repo Operations

To improve operational readiness and ensure resilience of the open market operations, the Bank started conducting small-scale test repo operations with the counterparties from April onwards.

(5) Continuous Growth in Monetary Aggregates

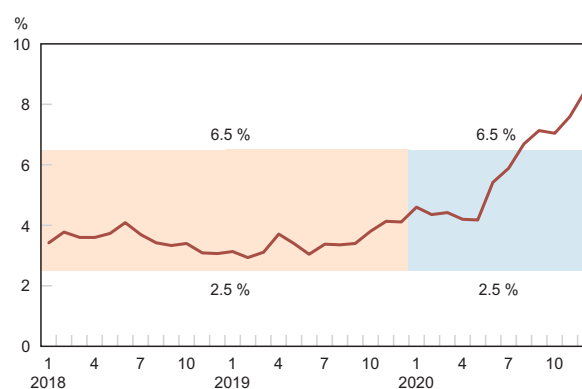
The M2 growth reference range for 2020 was set at 2.5% to 6.5%. For the year as a whole, M2 registered an annual growth rate of 5.84%, up by 2.38 percentage points from the previous year.

With regard to the monthly movements in 2020, net foreign capital inflows brought the M2 growth rate up to 4.60% in January. Later, it slipped to 4.35% in February owing to net foreign capital outflows. In March, despite an increase in net foreign capital outflows, faster growth in bank loans and investments brought the M2 growth rate up to 4.42%. Afterwards, continuous net foreign capital outflows dragged M2 growth down to its yearly low of 4.18% in May.

From June onwards, despite slower growth in foreign currency deposits sending the M2 growth rate down in October, net foreign capital inflows and stronger expansion in bank loans and investments led the M2 growth rate to display a steady uptrend and reached a yearly high of 8.45% in December.

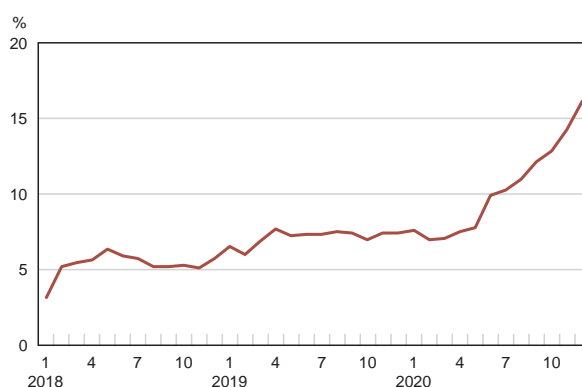
The annual growth rate of the monetary aggregate M1B, measured on a daily average basis, went up by 3.19 percentage points to 10.34% in 2020. The rise in M1B growth was primarily due to greater demand for funds amid a steady recovery in the domestic economy in the second half of the year, and an increase in transaction deposits accompanied by a booming stock market.

Annual Growth Rate of M2



Source: *Financial Statistics Monthly*, CBC.

Annual Growth Rate of M1B



Source: *Financial Statistics Monthly*, CBC.

As for the monthly movements, the annual growth rate of M1B registered 7.61% in January, and then was dragged down to the yearly low of 7.00% in February owing to a higher base effect with the Lunar New Year holidays falling in February 2019 and net foreign capital outflows. Driven by mild growth in bank loans and investments, the M1B growth rate slightly rose to 7.02% in March. Afterwards, with lower interest rates on time deposits leading to a buoyant stock market and an increase in transaction deposits, the M1B growth rate trended up steadily and reached an all-year high of 16.17% in December.

Launching a Special Accommodation Facility to Support Bank Credit to SMEs

In view of the economic impacts of the pandemic, the government introduced relief loan programs both for enterprises and for workers. The Bank also launched a special accommodation facility in March in order to enhance funding access for the SMEs. At the end of 2020, banks had received 195,075 applications with the amount totaling NT\$248.8 billion. As a result, the annual growth rate of SME loans extended by domestic banks rose considerably to 13.26% at the end of December.

Amending Targeted Macroprudential Measures Governing Real Estate Loans

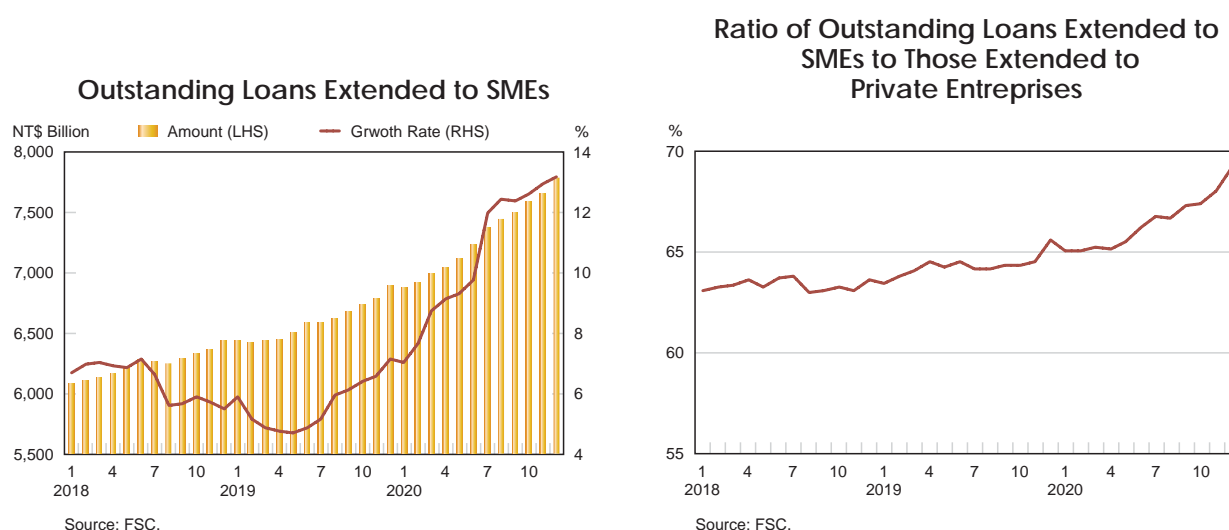
For the year 2020, to promote financial stability and sound banking operations by precluding an excessive flow of bank credit into the real estate market, the Bank adopted the following macroprudential policies:

- (1) In November, the Bank used moral suasion at meetings with major mortgage lenders and carried out on-site inspections. Meanwhile, the Bank issued official letters to financial institutions, requiring them to enhance risk management of housing loans and cautioning them against channeling excessive credit into the real estate sector.
- (2) The Bank made several amendments to the *Regulations Governing the Extension of Mortgage Loans by Financial Institutions*, effective December 8, 2020. In addition to keeping the loan-to-value (LTV) ratio capped at 60% on high-value housing loans, the Bank introduced additional LTV ratio caps on housing loans taken out by corporate entities, on the third (or more) housing loans by natural persons, on land loans, and on loans for unsold newly-built homes.
- (3) The Bank held meetings twice with major mortgage lenders in December, advising them to exercise caution in granting loans against land in industrial areas and to continuously practice self-discipline so as to prevent credit resources from being used for land hoarding or speculation in these areas.

Facilitating SME Funding

To sufficiently meet the funding needs of SMEs, the FSC continued to encourage lending by domestic banks to SMEs, while the Bank also urged commercial banks to increase lending to SMEs.

At the end of 2020, the outstanding loans extended to SMEs by domestic banks amounted to NT\$7,812 billion, increasing by NT\$915 billion from the end of the previous year and far exceeding the annual target of increased lending of NT\$300 billion set by the competent authorities. Outstanding SME loans recorded an annual growth rate of 13.26% at the end of 2020, higher than the 7.14% at the end of 2019. Furthermore, the ratio of SME loans to loans extended to all private enterprises rose slightly from 65.61% at the previous year end to 69.08% at the end of 2020.



Accepting Redeposits from Financial Institutions

Accepting redeposits from Chunghwa Post, the Agricultural Bank of Taiwan, and commercial banks is another instrument for the Bank to influence banks' reserve positions in order to promote financial stability. At the end of 2020, the outstanding redeposits of Chunghwa Post stayed broadly unchanged at NT\$1,624 billion, while the outstanding redeposits of the Agricultural Bank of Taiwan and of commercial banks were NT\$165 billion and NT\$354 billion, respectively.

Box

The Bank's Special Accommodation Facility to Help SMEs Affected by the Pandemic

As the COVID-19 outbreak quickly spread worldwide in the first few months of 2020 and battered the global economy, some industry sectors in Taiwan also took a hit from the impact. Given the importance of SMEs, which made up 98% of enterprises nationwide and 80% of the employed population,¹ their financial distress could have had adverse implications for the domestic economy and the labor market.

In order to help them stay afloat, the Bank implemented the Special Accommodation Facility to Support Bank Credit to SMEs ("the Facility"), effective April 1, 2020. The Facility would provide banks with additional funds so that they may, via secured loans backed by the government's Small and Medium Enterprise Credit Guarantee Fund of Taiwan (Taiwan SMEG), support the credit needs of the SMEs.

I. Introduction to the Facility

1. The legal foundation

- (1) Pursuant to Article 19 of *The Central Bank of the Republic of China (Taiwan) Act*, the Bank may provide accommodations to banks. Accordingly, the *Directions for the Central Bank of the Republic of China (Taiwan) Accommodations to Banks* (hereinafter the *Directions*) were promulgated.
- (2) With the aim of mitigating the pandemic-induced impacts on the macro-economy, the Bank considered it an imperative to help the SMEs through the difficulties by facilitating their access to funds under more preferential terms. Therefore, the *Directions* were also amended as follows, effective April 1:
 - A. Regarding Direction 14: The scope of the Bank's refinancing of secured loans for banks is expanded;
 - B. Regarding Direction 15: A set of operating rules are formulated in regard to banks' applications for the Bank's refinancing of secured loans;
 - C. Regarding Direction 17: The Facility's interest rate may be marked down from the Bank's interest rate on secured loan refinancing.

2. Key points of the Facility

The Bank's Facility provides banks with low-interest accommodations charged at 0.1% to help them offer SMEs loans under preferential terms. Then, based on the classes of collateral

¹ Small and Medium Enterprise Administration, Ministry of Economic Affairs, R.O.C. (2019), *White Paper on Small and Medium Enterprises in Taiwan, 2019*.

and types of applicants, the Facility offers three programs of different credit lines and durations for loans extended by financial institutions to applicable businesses.

The Bank's Special Accommodation Facility to Support Bank Credit to SMEs

Interest rate	The Bank's rate on refinancing of secured loans (1.5%) minus 1.4 percentage points; currently at 0.1%
Total amount	NT\$300 billion
Expiry date (with duration up to 360 days)	For applications prior to Aug. 9, 2020: until Mar. 27, 2021
	For applications between Aug. 10, 2020 and January 4, 2021: until June 30, 2021
	For applications after January 5, 2021: until Dec. 30, 2021

Source: Department of Banking, CBC.

SME Relief Lending under the Bank's Special Accommodation Facility

Loan type	Secured loans to the SMEs affected by the COVID-19 pandemic as assessed by banks receiving applications			
Loan purpose	To support business operations of the SMEs affected by the pandemic			
Eligible borrowers and loan terms	Program	A	B	C
	Borrower	SME*	SME*	Small-scale business entity**
	Guarantee/ Collateral	At least 90% guarantees covered by Taiwan SMEG	Other collateral (including at least 80% guarantees covered by Taiwan SMEG)	100% guarantees covered by Taiwan SMEG
	Amount	Up to NT\$4 million	Up to NT\$16 million	Up to NT\$0.5 million
	Interest rate	Capped at 1%	Capped at 1.5%	Capped at 1%
	Application time frame	2020.4.1-2021.6.30	2020.4.1-2021.6.30	2020.4.20-2021.6.30
	<p>*SME: A domestic business entity with proper company registration, business registration, limited partnership registration, or taxation registration, and whose paid-in capital is no more than NT\$100 million or which hires fewer than 200 regular employees may apply for loans under Program A or B.</p> <p>**Small-scale business entity: A business entity with proper taxation registration and whose monthly sales amount (in any month since from January 2020) does not reach the threshold for using uniform invoices may apply for loans under Program A, B or C.</p>			
Others	SMEs which take out loans under this Facility could also apply for other credit support measures implemented by the government.			

Source: Department of Banking, CBC.

II. Implementation of the Facility

1. Number and loan amount of applications

Between April 1, 2020 and December 31, 2020, banks have received more than 190 thousand applications, with 97.5% of them approved, and the total amount of applications exceeded

NT\$240 billion, with 95.8% of them granted, representing an effective effort to help the affected SMEs obtain the needed working capital.

Implementation of the Special Accommodation Facility (As of Dec. 31, 2020)

		Program A	Program B	Program C	Total
Applications	Number of cases	42,592	29,745	122,738	195,075
	Amount (NT\$ billion)	75.1	115.1	58.6	248.8
Cases approved	Number of cases	41,493	28,887	119,883	190,263
	Amount (NT\$ billion)	72.3	109.3	56.7	238.3

Source: Department of Banking, CBC.

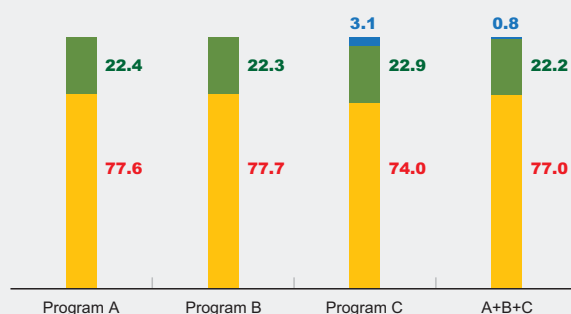
2. Implementation by type of financial institution

Among the applications, 77% of the amount went to government-owned banks² and 22.2% to private banks, while community financial institutions, extending such loans only via program C, made up a relatively small share of 0.8%.

Facility Implementation by type of financial institution (as of 2020/12/31)

Amount of loan applications

■ government-owned banks
 ■ private banks
 ■ community fin. institutions
 Unit: %

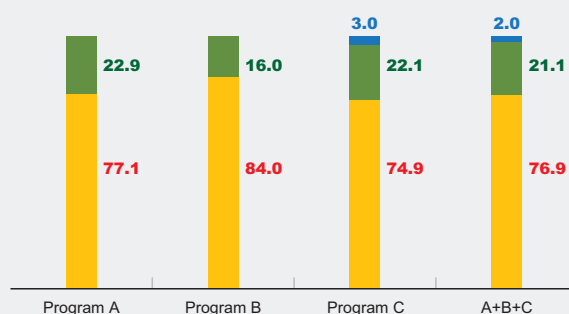


Note: The respective shares represent the amount of applications received by that type of financial institutions as a percentage of the total amount of applications to all financial institutions.

Source: Department of Banking, CBC.

Number of applications

■ government-owned banks
 ■ private banks
 ■ community fin. institutions
 Unit: %



Note: The respective shares represent the number of applications received by that type of financial institutions as a percentage of the total number of applications to all financial institutions.

Source: Department of Banking, CBC.

² Referring to domestic banks with full or partial government ownership.

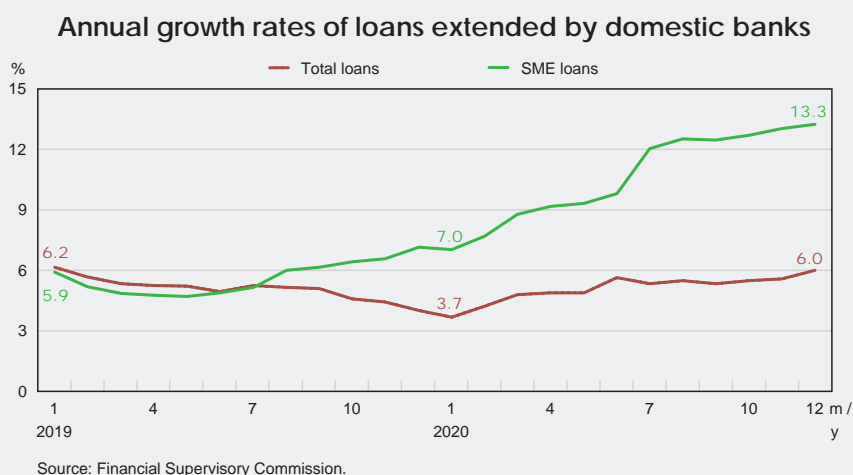
III. The Bank conducts a rolling review of the Facility as warranted by pandemic developments and corporate needs

When carrying out the Facility, the Bank has kept a close watch on the pandemic and the funding needs of SMEs. With a rolling review, the Bank made the following adjustments to the Facility: the amount of the Facility's accommodations was expanded from a total of NT\$200 billion to NT\$300 billion; the deadline for SMEs to apply for credit support was extended from Dec. 31, 2020 to June 30, 2021, and such loans that lenders approved on or after January 5, 2021 would continue to enjoy the facility's preferential interest rates until December 31, 2021. A longer duration for SMEs in need of assistance to enjoy the Facility's preferential interest rates would help lower the funding cost and support them in overcoming financial difficulties.

IV. Effective implementation of the Facility has helped ease the pandemic's economic impact and stabilize the financial system

1. SME lending rose markedly

As of the end of December 2020, domestic banks' lending to SMEs increased by 13.3% year on year, higher than the 6.0% annual increase of total lending. The Bank continued urging banks to reinforce their SME support under the Facility, thus effectively reducing the pandemic's impact on employment and the economy.



2. SMEG guarantee supported banks' role as financial intermediaries and buttressed asset quality

Loans extended by banks under the Facility are backed by the government's Taiwan SMEG. This not only boosts banks' confidence and interest in lending to SMEs but also could mitigate credit risk to banks. As of the end of December 2020, the non-performing ratio of SME loans extended by domestic banks stood at 0.34%, lower than the average ratio of 0.41% of the previous year.

3. By incorporating community financial institutions, the Facility is able to increase its reach and help more businesses

Some small businesses mostly go to credit cooperatives or credit departments of farmers' and fishermen's associations for banking services. By incorporating these community financial institutions, the Facility could also provide working capital assistance to this swath of business entities affected by the pandemic, helping 3,818 of them via this channel and a total of more than 190 thousand small-scale business entities through Program C, as of December 31, 2020.