

III. Financial system assessment

3.1 Financial markets

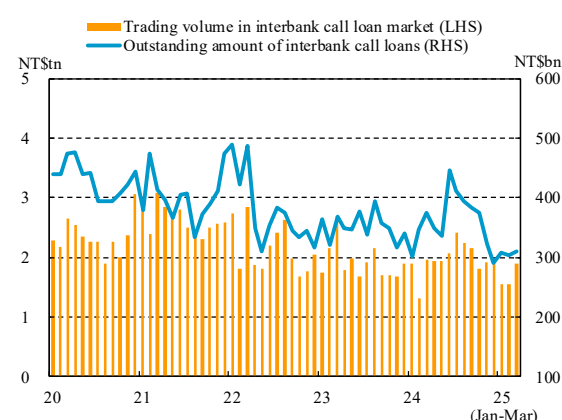
In 2024, both the outstanding amount and trading volume of interbank call loans rebounded, while the market conditions remained stable. Owing to a significant rise in the issuance of CP, the outstanding amount of bill issuance also increased. CP continued to constitute the largest share of the bill trading volume in the secondary market, with the market size steadily expanding, thereby facilitating short-term corporate financing. Meanwhile, the outstanding amount of bond issuance and trading volume in the secondary market continued expanding. Domestic stock indices repeatedly reached record highs and trading was notably active, while the NT dollar showed a moderate depreciation trend in 2024. From the beginning of 2025, driven by uncertainty surrounding US tariff policies and shifting market expectations, equity and FX markets have experienced heightened volatilities. Nevertheless, these markets have begun to stabilize, while the money and bond markets have remained stable.

3.1.1 Money and bond markets

Both the outstanding amount and the trading volume of interbank call loans shifted to an uptrend

In 2024, the average daily outstanding amount of interbank call loans was NT\$360.8 billion, an increase of 2.49% year on year, primarily because of banks increasing short-term financing in response to liquidity management needs, which led to a rise in call loan lending.³⁰ Meanwhile, greater funding demand from bills finance companies also contributed to a

Chart 3.1 Interbank call loan market



Note: Outstanding amount is the monthly average of daily data.
Source: CBC.

³⁰ In 2024, the average daily outstanding amount of interbank lending from domestic banks increased by 7.72% year on year.

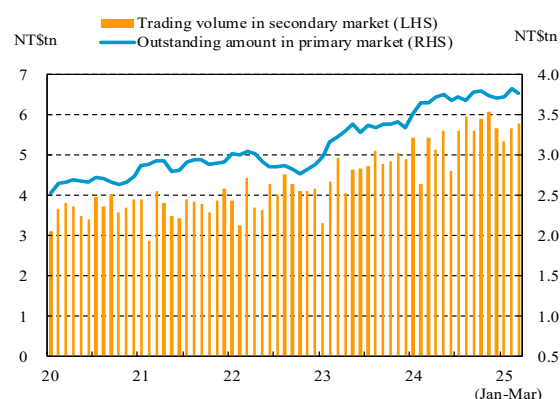
concurrent increase in call loan borrowing.³¹ Owing to the heightened market demand for funds, financial institutions raised the amount of funds allocated for liquidity management. Consequently, the trading volume of interbank call loans rose by 2.11% year on year. In 2025 Q1, the average daily outstanding amount of interbank call loans dropped by 9.93% year on year, mainly because bill finance companies reduced their borrowing in the call loan market, while shifting to increased use of short-term repurchase and outright transactions. As a result, the trading volume of interbank call loans also decreased by 3.27% (Chart 3.1).

Both the outstanding amount of bill issuance and the bill trading volume in the secondary market expanded year on year

The outstanding amount of bill issuance in the primary market reached NT\$3.71 trillion by the end of 2024, showing an increase of NT\$365.3 billion or 10.91% year on year. This was mainly driven by higher corporate funding needs, which led to a large increase of NT\$271.7 billion in the outstanding amount of CP issuance. Moreover, bank-issued NCDs increased by NT\$94.1 billion, while treasury bills remained largely unchanged. In 2025 Q1, the outstanding amount of bill issuance rose by 3.13% year on year as the issuance of CP increased (Chart 3.2).

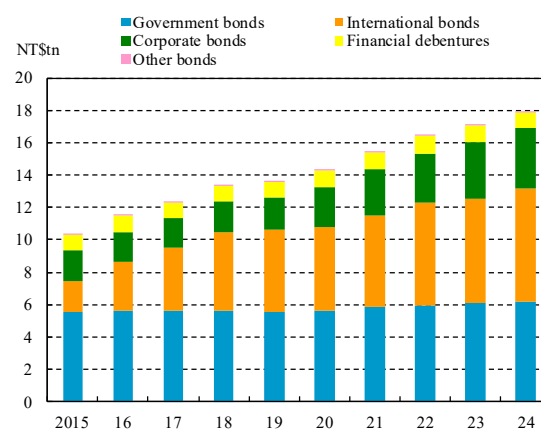
In 2024, as the outstanding amount of bill issuance expanded, the trading volume in the secondary market rose by 17.94% year on year to NT\$65.36 trillion. Among these instruments, CP continued to constitute the largest share of 94.48%, representing a slight decrease from a year earlier. Boosted by seasonal demand ahead of the Lunar New Year, the bill trading volume

Chart 3.2 Primary and secondary bill markets



Source: CBC.

Chart 3.3 Bonds outstanding in the primary market



Note: Other bonds include beneficiary securities and foreign bonds.

Source: FSC.

³¹ In 2024, the average daily outstanding amount of interbank borrowing from bills finance companies increased by 11.97% year on year.

in 2025 Q1 increased significantly by 10.76% compared with the same period of the previous year (Chart 3.2).

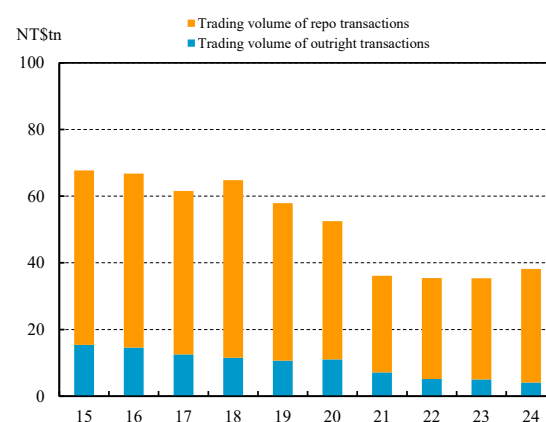
The outstanding amount of bond issuance and the trading volume continued to expand; however, the turnover rate of outright bond transactions remained at a low level

The outstanding amount of bond issuance hit a historical high of NT\$17.93 trillion at the end of 2024, an increase of 4.75% over the end of the previous year. Corporate bond issuance contributed to a 7.74% rise, owing to strong funding demands from corporations. Meanwhile, as US interest rates declined, the outstanding amount of international bonds issued by foreign entities increased by 7.70% compared to the end of the previous year. However, the outstanding amount of government bonds³² increased merely by 1.88% (Chart 3.3).

On the other hand, the trading volume in the secondary bond market reached NT\$38.14 trillion in 2024, expanding by 7.71% year on year (Chart 3.4). By trading type, outright transaction volume dropped by 18.27% year on year, while repo transaction volume increased by 11.96% year on year. Nevertheless, the overall trading volume has remained at a lower level in recent years.

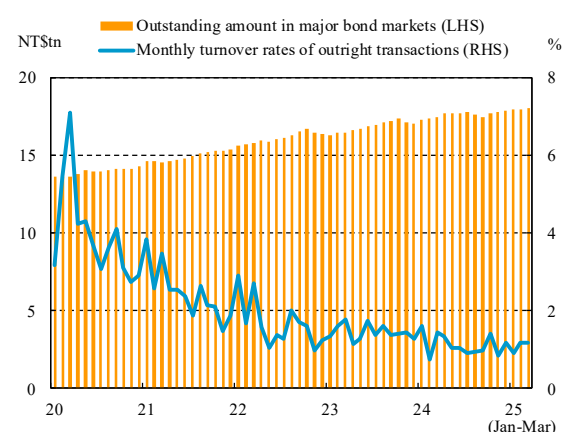
As a result, the average monthly outright turnover rate of major bonds continued on a downward trend, falling to 1.13% in December 2024, and further declining to a record low of

Chart 3.4 Outright and repo transactions in the bond market



Source: CBC.

Chart 3.5 Outstanding amount in major bond markets and monthly turnover rates of outright transactions



Notes: 1. Major bonds include government bonds, corporate bonds, financial bonds, and international bonds.
2. The monthly turnover rate for outright transactions = (total value of outright transactions in the month) / (average outstanding issuance), where the average outstanding issuance = (the outstanding issuance at the end of the current month + the outstanding issuance at the end of the previous month) / 2.

Source: FSC.

³² Includes central and local government bonds.

0.90% in January 2025. However, it bounced back to 1.09% in March, though still at a relatively low level (Chart 3.5).

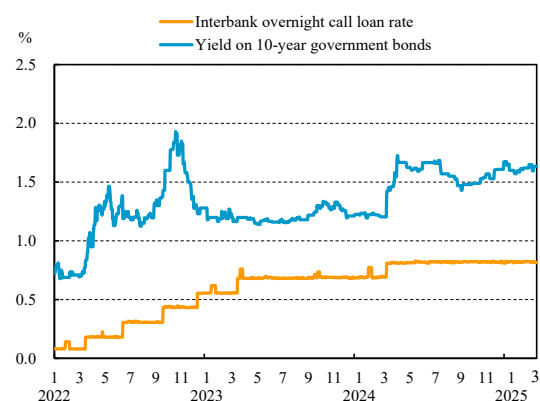
Long-term and short-term market rates increased

In terms of short-term market rates, to curb domestic inflation expectations, the Bank raised the policy interest rates in March 2024. As a result, the interbank overnight call loan rate began to trend upwards and later leveled off. In the second half of 2024, the Bank raised the reserve requirement ratios on NT dollar deposits twice, while foreign investors net sold TWSE stocks and remitted funds outwards. The interbank overnight call loan rate climbed slowly and then fluctuated in a narrow range around 0.820% (Chart 3.6), yet overall market liquidity remained ample.

As for long-term market rates, influenced by the Bank's policy rate hike and the rebound in US government bond yields, domestic 10-year government bond yields rose and reached a two-year high of 1.725% on April 17. Afterwards, following the decline of US government bond yields, domestic 10-year government bond yields gradually trended downwards, hitting a low of 1.430% on September 20 before rebounding (Chart 3.6). In 2025 Q1, domestic 10-year government bond yields reached a high of 1.677% and then trended downwards.

Considering the rising uncertainties surrounding US tariff policies, inflation might be pushed higher and affect market confidence. In addition, factors such as global geopolitical risks and monetary policy divergences among major central banks could lead to heightened market risk aversion in the near future. The volatility of global bond yields will likely intensify, which may affect domestic 10-year government bond yields. Therefore, the interest rate risks of bond investments held by domestic financial institutions are worthy of close attention.

Chart 3.6 Interbank overnight rate and 10-year government bond yield



Source: Bloomberg.

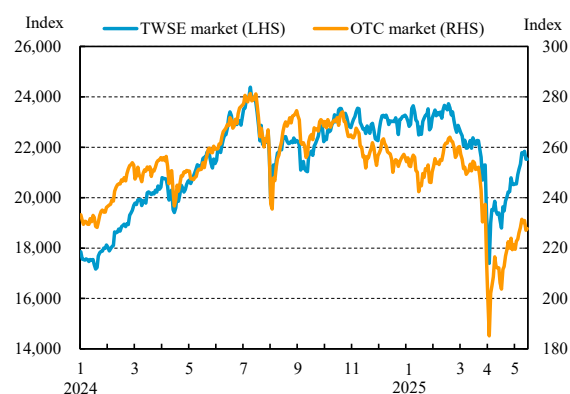
3.1.2 Equity markets

Stock indices repeatedly reached historical highs and trading was notably active in 2024

Stock indices repeatedly reached historical highs

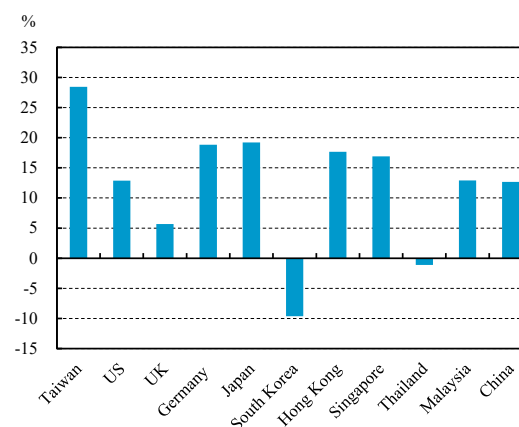
In the first half of 2024, bolstered by favorable factors such as the rallies in international stock markets, continued net buying of TWSE stocks by domestic securities investment trust enterprises, and the popularity of high-dividend equity exchange-traded funds (ETFs), the TAIEX of the TWSE market fluctuated upward, reaching a historical high of 24,390 on July 11. However, owing to a decline in US stock indices and heightened geopolitical tensions in the Middle East, the TAIEX plummeted to a low of 19,831 in August. Subsequently, the TAIEX fluctuated upward to 23,035 at year end (Chart 3.7), posting an increase of 28.47% year on year and surging higher than the major indices in other international stock markets (Chart 3.8). The Taipei Exchange Capitalization Weighted Stock Index (TPEX) of the OTC market closely tracked the movements of the TAIEX during the first three quarters of 2024, though small and mid-cap stocks underperformed in Q4. The TPEX registered 256 at year end and posted an increase of 9.33% year on year.

Chart 3.7 Taiwan's stock market indices



Sources: TWSE and TPEX.

Chart 3.8 Major stock market performance



Notes: 1. Changes are figures at the end of 2024 compared to those at the end of 2023.
2. Market performance is based on TWSE Weighted Index for Taiwan, DJIA Index for the US, FTSE-100 Index for the UK, DAX Index for Germany, NK-225 Index for Japan, KOSPI Index for South Korea, Hang Seng Index for Hong Kong, Straits Times Index for Singapore, SET Index for Thailand, Kuala Lumpur Composite Index for Malaysia, and SSE Composite Index for China.

Source: TWSE.

The significant expansion of ETF issuance bolstered the rise in the TAIEX in 2024

In the TWSE market, foreign investors posted net sales of NT\$695.1 billion in 2024, mainly driven by profit-taking amid successive record highs in the TAIEX and the depreciation of the NT dollar against the US dollar. Local securities dealers also registered net sales of NT\$823.8 billion as they adjusted their shareholdings or took hedging positions. However, as securities investment trust enterprises ramped up their issuance of ETFs, they passively invested in index constituents, resulting in net purchases totaling NT\$832.1 billion for the year, which became a major force supporting the TAIEX's uptrend (Chart 3.9).

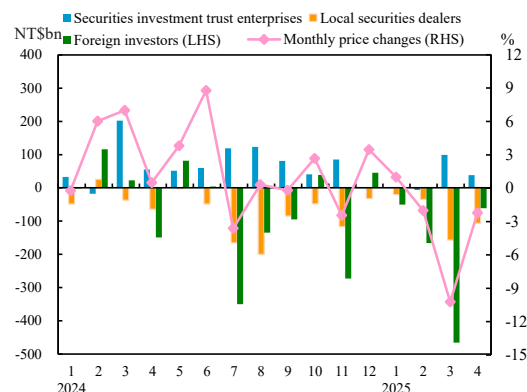
Volatility in the stock markets increased before stabilizing

Impacted by rising uncertainty surrounding the US economy and geopolitical risks in 2024, the volatility in both the TWSE and OTC markets gradually increased, reaching relatively high levels in Q3. Subsequently, it stabilized amid a mix of negative and positive developments, ending the year at 15.23% and 14.25% in the respective markets (Chart 3.10).

The price-to-earnings (P/E) ratio of the TAIEX rose, reflecting positive market expectations for Taiwan's technology sector

The domestic stock market is dominated by technology stocks, with electronics industry stocks – particularly in semiconductors, electronic components, telecommunications, and information technology services – accounting for over 70% of the TAIEX. The application of AI has fueled

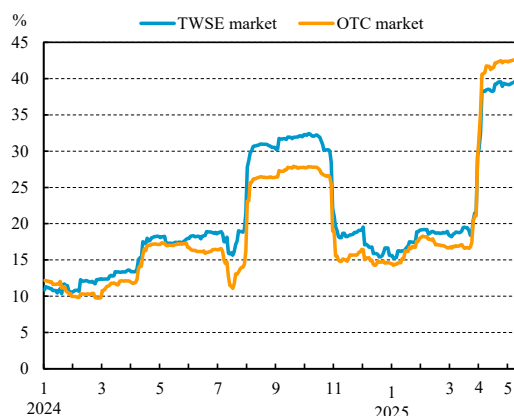
Chart 3.9 Net buying/selling amount by institutional investors and monthly price changes in the TWSE market



Note: Institutional investors are divided into securities investment trust enterprises, local securities dealers, and foreign investors.

Source: TWSE.

Chart 3.10 Stock price volatility in Taiwan's markets



Note: Volatility refers to the annualized standard deviation of 60-day daily index returns.

Sources: TWSE, TPEx, and CBC.

strong demand across related supply chains, boosting the earnings of semiconductor and other electronics-related companies in recent years. As a consequence, the P/E ratio of the TAIEX climbed from 10.39 at the end of 2022 to 21.29 at the end of 2024 (Chart 3.11), likely reflecting optimistic investor sentiment toward the future prospects of Taiwan's technology sector. Nevertheless, multiple factors such as underlying fundamentals, industry trends, and domestic and global macroeconomic conditions warrant continued close attention.

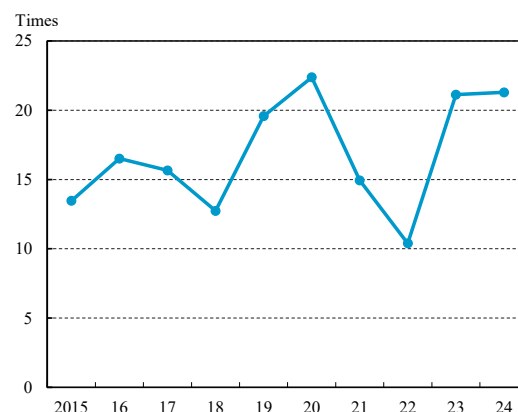
Trading value surged and turnover rates trended upwards

Encouraged by strong interest from resident investors, trading activity in the domestic stock markets was vibrant in 2024. The monthly average trading value in both the TWSE and the OTC markets reached NT\$7.69 trillion and NT\$1.94 trillion in 2024, respectively, marking increases of 46.10% and 38.02% year on year. As a consequence, the annual turnover rates in terms of trading value rose to 135.40% and 360.49% in the TWSE and the OTC markets (Chart 3.12), respectively, surpassing those in most major international stock markets (Chart 3.13). This indicated that trading in Taiwan's stock markets remained highly active and liquidity remained ample.

Domestic ETF market expanded significantly

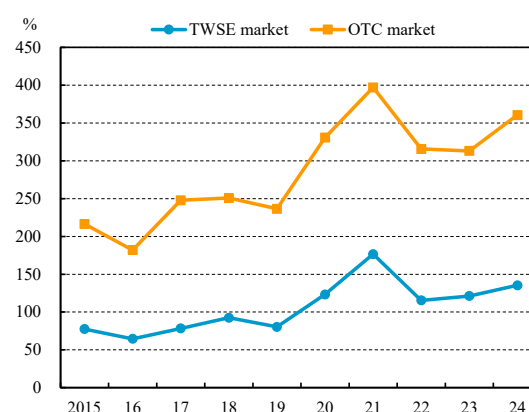
Driven by the strong performance of domestic

Chart 3.11 Price-to-earnings ratio of the TAIEX



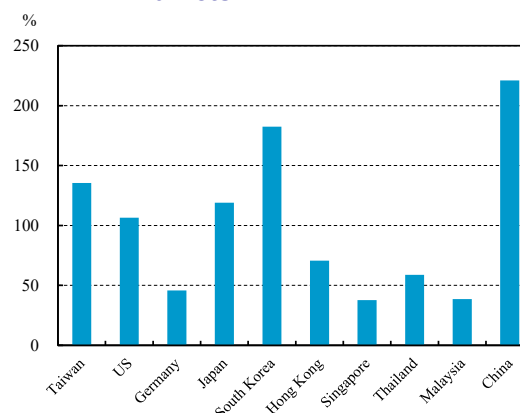
Source: TWSE.

Chart 3.12 Annual turnover rates in Taiwan's stock markets



Sources: TWSE and TPEx.

Chart 3.13 Turnover rates in major stock markets



Note: Figures refer to accumulated turnover rates in 2024.
Source: TWSE.

stock markets and the appeal of high-dividend yields, the size of equity ETFs expanded significantly in 2024. In addition, increased market optimism about interest rate cuts by major central banks around the world contributed to a substantial rise in bond ETFs investing in foreign bonds. The total size of ETFs reached NT\$6.4 trillion at the end of 2024, representing a year-on-year increase of 65.11%. The number of ETF funds and total beneficiaries also rose to 260 and 14.37 million, respectively, both hitting historical highs.³³

In December 2024, the FSC amended relevant regulations to officially allow the issuance of active ETFs and passive multi-asset ETFs, thereby providing investors with more diversified investment options. Nevertheless, considering that ETFs may contribute to stock price co-movements and pose systemic risks, close attention should be paid to market developments and their potential impacts on the financial system (Box 2).

Domestic stock markets have become increasingly volatile amid uncertainty surrounding US tariff policies from the beginning of 2025 onwards

Stock indices experienced sharp volatility and a notable retreat

From January to March 2025, domestic stock markets continued to fluctuate and consolidate. However, following the announcement of the US reciprocal tariff policies on April 2, global stock markets plunged, and the TAIEX and the TPEX also tumbled for several consecutive days. Subsequently, as market sentiment gradually stabilized and foreign investors increased their holdings of domestic stocks, both indices rebounded quickly, closing at 21,526 and 228, respectively, on May 20 (Chart 3.7).

Heavy net selling by foreign investors and local securities dealers triggered steep declines in the stock market

Since the beginning of 2025, mounting uncertainty surrounding US tariff policies has exerted significant funding pressure on the TWSE market. Driven by heightened risk aversion sentiment, foreign investors offloaded and short-sold their holdings of domestic stocks, leading to net sales of NT\$743.6 billion by the end of April (Chart 3.9), surpassing the total amount of 2024. Local securities dealers also recorded net sales of NT\$318.2 billion. Although securities investment trust enterprises posted net purchases of NT\$130.4 billion, the TAIEX continued on a downward trend, suggesting that market confidence remained fragile amid uncertainty

³³ Offshore ETFs, futures ETFs, and leveraged/inverse futures ETFs were not included.

surrounding US tariff policies.

Volatility in the stock markets surged to a multi-year high

The domestic stock markets remained relatively stable in 2025 Q1, while market sentiment deteriorated sharply in April following the announcement of the US reciprocal tariff policies, which pushed up the VIX index and triggered heightened volatility in domestic stock markets. Volatility levels in the TWSE and the OTC markets surged to multi-year highs and remained elevated, registering 39.63% and 42.64%, respectively, on May 20 (Chart 3.10). This reflected sustained caution among market participants amid uncertainty surrounding the Trump administration's policies.

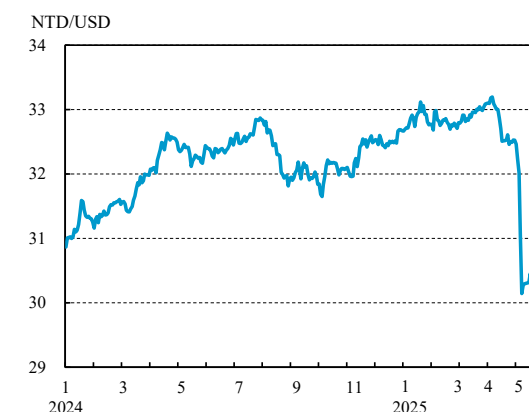
Domestic stock markets are highly correlated with international stock markets. Given the recent uncertainties arising from the ongoing effects of US tariff policies and escalating geopolitical risks, which may disrupt global economic prospects and international stock market performance, as well as adversely affect domestic stock markets, close attention is warranted.

3.1.3 FX market

The NT dollar appreciated after an initial depreciation against the US dollar, while FX market trading volume increased

In 2024, most major Asian currencies depreciated against the strong US dollar except for the MYR. The NT dollar exchange rate stood at 32.781 against the US dollar at the end of 2024 (Chart 3.14), depreciating by 6.24% from the end of the previous year. The extent of the NT dollar depreciation was moderate compared to other Asian currencies (Chart 3.15). From January to April 2025, the NT dollar appreciated following a period of depreciation against the US dollar, and remained relatively stable compared to other major currencies. Nevertheless, driven by foreign capital inflows into domestic stock markets and market expectations for NT dollar appreciation, which boosted US dollar supply, the NT dollar appreciated sharply in early May and closed at 30.179 against the US dollar on May 20.

Chart 3.14 NTD/USD exchange rate



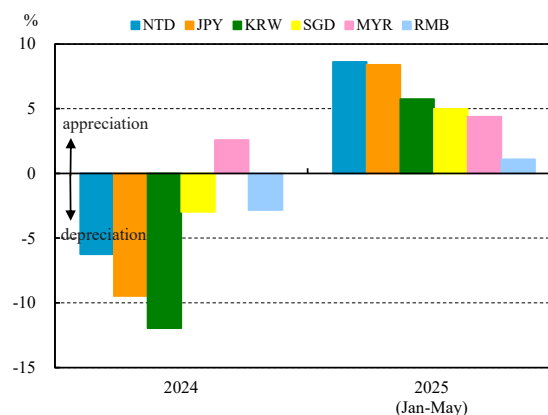
Source: CBC.

The average daily trading volume in Taiwan's FX market amounted to US\$44.6 billion in 2024, marking a 17.90% rise compared to a year earlier, primarily because of an increase in interbank transactions (Chart 3.16). In March 2025, the average daily trading volume amounted to US\$48.6 billion, up by 5.68% over the same period of the previous year.

NT dollar exchange rate volatility increased, but remained relatively stable over the long term

The volatility of the NT dollar exchange rate against the US dollar fluctuated between 2.27% and 5.74% in 2024, with an annual average of 3.97%, which was relatively low compared to those of other major currencies. From January to April 2025, the volatility of the NT dollar exchange rate ranged between 1.92% and 5.73% (Chart 3.17). Driven by foreign capital inflows and market expectations, the volatility of the NT dollar surged in early May. Nevertheless, the average volatility of the NT dollar for the period from January 1 to May 20 was 5.32%, still lower than that of other major currencies, indicating that the NT dollar remained relatively stable over the long term.

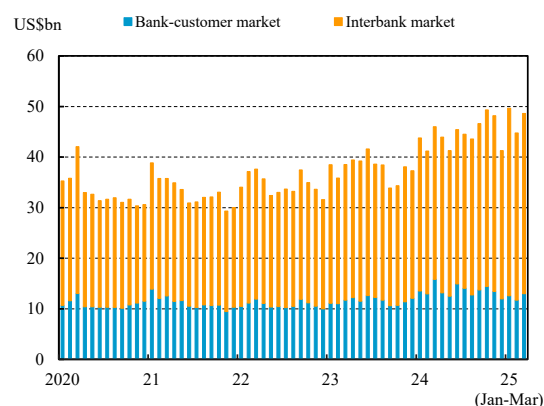
Chart 3.15 Exchange rate changes of major Asian currencies against the US dollar



Note: Changes in 2024 are figures at the end of the year compared to those at the end of 2023; changes in the period of Jan-May 2025 are figures on May 20 compared to those at the end of 2024.

Source: CBC.

Chart 3.16 FX market trading volume



Notes: 1. Trading volume is the monthly average of daily data.
2. The latest data for trading volume are as of March 2025.

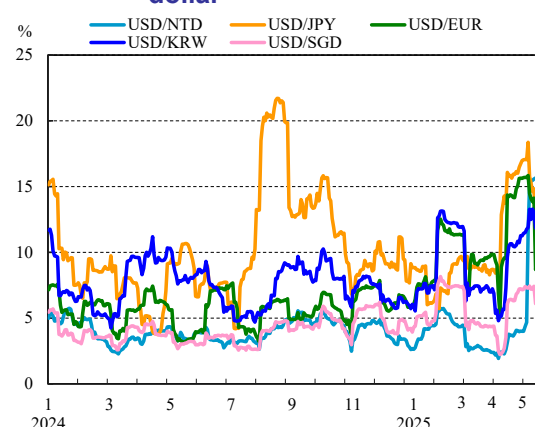
Source: CBC.

The nominal and real effective exchange rate indices of the NT dollar fluctuated within a narrow range

In 2024, as foreign investors repatriated funds for profit-taking and dividend distributions, the NEER index of the NT dollar declined to 101.10 at year end, a decrease of 1.89% from 103.05 at the end of 2023. The NEER of the NT dollar fluctuated within a narrow range and remained relatively stable compared to other major Asian currencies. From 2025 onwards, the NT dollar appreciated significantly against the US dollar. The NEER of the NT dollar rose to 105.85 on May 20, registering an increase of 4.70% compared to the end of 2024 (Chart 3.18).

During the same period, the real effective exchange rate (REER) index of the NT dollar also fluctuated within a limited range. It stood at 98.77 in December 2024, a decrease of 0.65% from 99.42 in December 2023. The volatility of the NT dollar's REER remained relatively mild compared to other major Asian currencies. In April 2025, the NT dollar's REER declined to 96.32, a decrease of 2.48% compared to December 2024.

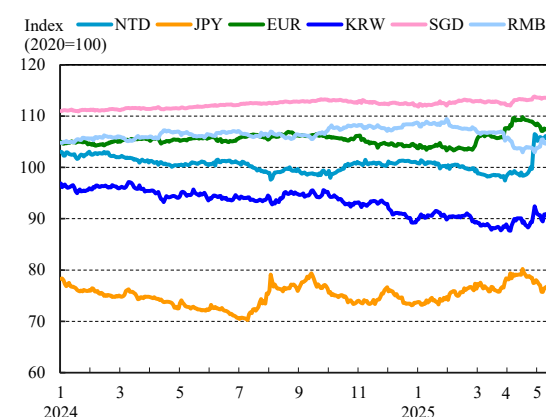
Chart 3.17 Exchange rate volatility of various currencies versus the US dollar



Note: Volatility refers to the annualized standard deviation of 20-day daily returns.

Source: CBC.

Chart 3.18 NT dollar NEER index



Source: BIS.

Box 2

The development and supervisory issues of Taiwan's ETF market

The development of Taiwan's ETF market began more than two decades ago. In recent years, the market expanded rapidly, driven by repeated record highs in the domestic equity markets, the appeal of high dividend yields, and expectations of US policy rate cuts. In particular, high-dividend ETFs saw a surge in fundraising that even led some retail investors to terminate time deposits or take out loans to invest in ETFs. This increasingly drew attention across sectors, including from the regulators. This box outlines the development of Taiwan's ETF market, highlights potential risks to investors and the financial system, and analyzes recent market challenges and regulatory responses, in the hope of providing a useful reference for policy deliberation.

1. ETF market development in Taiwan

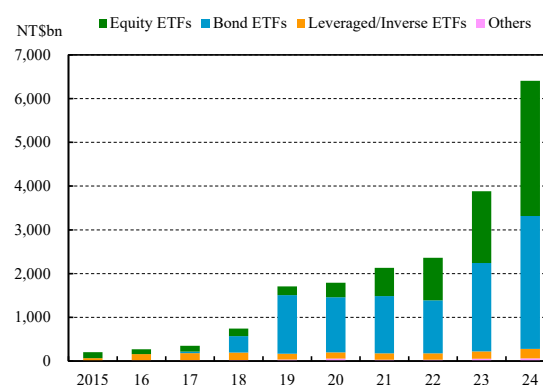
1.1 ETFs have grown rapidly since 2018, initially driven by bond ETFs and more recently by equity ETFs

The first ETF listed on the TWSE was the Yuanta/P-shares Taiwan Top 50 ETF issued in June 2003. Following the gradual easing of related regulations, the ETF market began to develop, albeit at a slow pace. In 2018, the market experienced a breakthrough as a deregulation move excluded investments by life insurance companies in NTD-denominated bond

ETFs from their overseas investment cap. This policy change attracted significant inflows and fueled rapid growth in bond ETFs. In more recent years, repeated record highs in the domestic stock markets and the rising popularity of high-dividend equity ETFs among investors have led to substantial growth in the equity ETF market (Chart B2.1). Meanwhile, expectations of Fed rate cuts starting from the second half of 2023 further boosted demand for overseas bond ETFs.

As of the end of 2024, the fund size of ETFs reached NT\$6.4 trillion, representing a remarkable growth of approximately 32 times compared with that of NT\$202.1 billion at the end of 2015. The number of ETFs increased sharply from 34 to 260 over the same period, and that of ETF investors also expanded substantially from 240,000 to 14.37

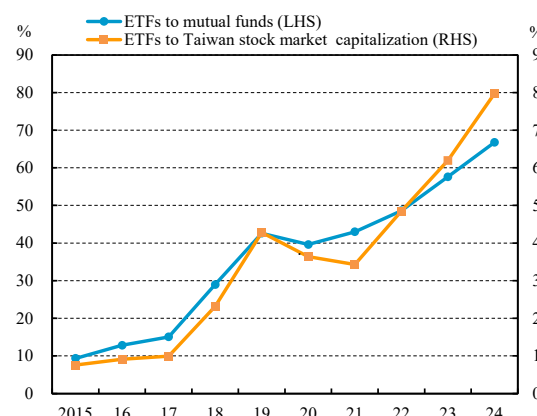
Chart B2.1 Types and Sizes of ETFs in Taiwan



Sources: FSC and SITCA.

million, reflecting an increase of 60 times.¹ Since March 2023, the fund size of ETFs has officially surpassed that of regular mutual funds issued by domestic securities investment trust enterprises (SITEs). The share of ETFs in Taiwan stock market capitalization has also continued to rise (Chart B2.2), showing that ETFs have become one of the major investment products in Taiwan's capital market.

Chart B2.2 Comparison of the fund size



Sources: FSC and SITCA.

1.2 Trading value increased, but overall turnover rate was relatively low

The trading value of domestically listed ETFs was NT\$6.7 trillion in 2024, representing a huge increase of 4.1 times compared to NT\$1.6 trillion in 2015. However, over the past three years, the average annual turnover rate by trading value in the ETF market stood at 106.3%, which was lower than that of 124.0% in TWSE stock trading, reflecting not only the rapid expansion of the ETF market but also the fact that, unlike in the stock market, ETF investors usually prefer a “buy and hold” strategy that resulted in a lower frequency of transactions.

1.3 Domestic equity ETFs showed a high concentration in technology stocks

As of the end of 2024, many domestic equity ETFs tracking broad-market indices or adopting high-dividend strategies exhibited a high allocation to technology-related sectors (e.g., electronics and semiconductors), reflecting a notable industry concentration. For example, the top three ETFs by total assets under management were the Yuanta/P-shares Taiwan Top 50 ETF (0050, NT\$436.1 billion), the Cathay MSCI Taiwan ESG Sustainability High Dividend Yield ETF (00878, NT\$376.3 billion), and the Yuanta/P-shares Taiwan Dividend Plus ETF (0056, NT\$363.8 billion). The abovementioned funds allocated 70.7%, 56.0%, and 61.0% of their assets, respectively, to electronics or semiconductor stocks.² The high concentration of these industries in domestic equity ETFs may weaken portfolio diversification, thus warranting close attention.

1.4 The recent regulatory approval of active ETFs and passive multi-asset ETFs has contributed to greater product diversification in the ETF market

To promote the development of the asset management market in Taiwan, provide impetus

for asset management business growth, and support the policy objective of establishing Taiwan as an “Asian asset management center,” the FSC amended relevant regulations in December 2024 to formally permit the issuance of active ETFs and passive multi-asset ETFs. In early May 2025, the first active ETF in Taiwan, the NEXT FUNDS – Nomura Taiwan SMART Select Active ETF (00980A), was listed. More active ETFs are expected to be introduced into the market in the future. However, investors should be aware that the performance of active ETFs is highly dependent on fund managers’ investment capabilities and generally involves higher operational risk compared to passive ETFs. In addition, passive multi-asset ETFs may carry different levels of risk depending on their allocation strategies and equity-bond proportions. Investors should carefully evaluate their risk tolerance and select ETF products that align with their investment objectives and styles, ensuring both portfolio security and performance.

2. Potential risks of ETFs and market challenges in Taiwan

ETFs are widely favored by investors for such advantages as risk diversification and trading convenience. However, they may still involve certain risks. Moreover, the rapid expansion of the ETF market may also pose potential impacts to overall financial stability, which warrants close attention.

2.1 Potential risks to investors

- (1) Discount/Premium risk:** ETF prices in the secondary market are determined by market supply and demand. The prices may deviate from their net asset value, resulting in premiums or discounts that affect investors’ actual returns.
- (2) Tracking error risk:** Tracking error refers to the difference between the returns of an ETF and those of its underlying index. Common causes of tracking errors include fund expenses, exchange rate differences between the trading currency and the denominated currency, etc.
- (3) Liquidation risk:** If an ETF is delisted upon regulatory approval, investors who purchased the ETF at a premium may be exposed to potential losses due to fund liquidation.
- (4) Liquidity risk:** ETF market makers are responsible for providing bid and ask quotes. If they fail to properly fulfill their quoting obligations or cease to perform such obligations, investors may face the risk of being unable to buy or sell ETFs.

2.2 Potential risks to the financial system

- (1) Systemic risk:** The “basket-trading” feature of ETFs may lead to more synchronized

volume and price movements among constituent securities. This can increase the frequency of simultaneous mass buying or selling, thereby weakening the effect of risk diversification and potentially amplifying systemic risk in the financial market.

(2) Stock price co-movement risk: During the periods of excessive market optimism or heightened uncertainty, herd behavior may emerge as some investors mimic the behavior of others, leading to concentrated buying or selling, thus exacerbating short-term price volatility.

(3) Concentration risk: If the underlying assets are concentrated in a limited number of companies, it may result in excessive correlation among constituent stocks, making the price movements across constituent stocks more aligned and thus reducing the diversification benefits of ETF portfolios.

2.3 Challenges of the ETF market in Taiwan

The recent investment surge in equity ETFs was driven by expectations of Fed rate cuts, domestic stock market rallies and high dividend yields. Meanwhile, repeated record highs in stock markets, combined with aggressive marketing campaigns by SITEs, have triggered a frenzy of buying among investors. Moreover, in order to boost distribution rates to attract investors, some SITEs misused the funds' income equalization reserves or even rebalanced their holdings frequently. Such practices may increase investment costs and erode returns, thereby potentially undermining the long-term interests of investors.

3. Regulatory framework and supervisory enhancements in Taiwan

To safeguard ETF market stability and protect investor interests, the TWSE strengthened product standards and information disclosure requirements for ETFs. The FSC also introduced multiple supervisory measures to promote sound development of Taiwan's ETF market.

3.1. ETF product regulation

Taiwan has not yet enacted dedicated regulations for ETFs. Instead, relevant provisions are dispersed across various regulations governing securities investment trusts, securities exchanges and the self-regulatory rules of the Securities Investment Trust and Consulting Association (SITCA). In addition, the TWSE has imposed eligibility criteria and standards on the components of the underlying indices. These include: (1) the components must be listed on domestic or foreign stock exchanges, (2) the components must be sufficiently diversified, with no single component security exceeding 30% of the index and the cumulative weight of the top five component securities not exceeding 65%,³ and (3) the

components must meet certain liquidity requirements. The TWSE also sets different liquidity standards based on the component characteristics of the index to ensure that ETFs are equipped with reasonable trading and arbitrage mechanisms.

3.2. Reinforcement of index compilation review mechanisms

The FSC required the TWSE and the TPEx to examine past performance when reviewing index compilation, so as to assess whether the constituent securities of an index are likely to be changed frequently. By managing the replacement rate of an index's constituent stocks through retrospective review, it would help to stabilize the investment structure of ETFs.

3.3 Disclosure of dividend sources and distribution orders

The FSC required SITEs to disclose the composition of sources of ETF dividends, so as to enhance market discipline. Furthermore, the distribution order shall be dividends from constituent securities, capital gains, and finally, income equalization reserves. These requirements aim to promote market self-discipline and information transparency, thus preventing investors from being misled.

3.4. Regulation of advertising and marketing activities

The FSC required the SITCA to develop a governance mechanism for advertising collaborations between SITEs and financial influencers and to formulate relevant self-regulatory guidelines. In addition, ETF advertisements are prohibited from using dividend payout rates or distribution amounts as the main headline or the primary promotional message. Moreover, high-dividend ETFs are required to include warning statements such as “no guaranteed income or dividends” to remind investors of ETFs' product nature and associated risks.

3.5. Wide-ranging enhancement of market supervision

The FSC strengthened its oversight of the ETF market through the following measures: (1) Supporting and monitoring SITEs in enhancing their assessment of the concentration and liquidity of constituent securities in the ETFs they issue and the indices they track, in order to keep stock prices and market liquidity from being excessively affected during position building and massive subscription or redemption; (2) Overseeing the TWSE and the TPEx in regular evaluation of ETFs' holdings and in building transaction databases to support stable market operations; (3) Drawing on the *Good Practices Relating to the Implementation of the IOSCO Principles for Exchange Traded Funds – Final Report* published by the International Organization of Securities Commissions (IOSCO) to

enhance supervisory measures in the following three aspects, namely product structure, information disclosure, and liquidity provision; (4) underscoring ETFs as a focus in financial examinations, with the findings to serve as a reference for amending relevant regulations and self-regulatory practices.

4. Conclusion

Owing to their strengths in risk diversification, trading convenience, and cost efficiency, ETFs have emerged as an increasingly important tool for asset allocation. In recent years, as the size and the number of participants in Taiwan's ETF market have grown rapidly and product diversity has increased gradually, ETFs have gained significant and undeniable influence on the local financial market. However, rapid market expansion and growing capital concentration may also pose potentially adverse implications for the financial market, such as heightened market volatility, risk contagion, and excessive industry concentration, all of which warrant close attention. In line with its macroprudential supervision duties, the Bank will continue to conduct relevant research and monitor new developments as well as potential risks in Taiwan's ETF market. Additionally, the Bank will, as warranted by changes in the market, share its research findings through the supervisory communication platform in a timely manner, and work jointly with the FSC to safeguard financial stability.

- Notes: 1. The number of funds and that of beneficiaries exclude offshore ETFs, futures ETFs, and leveraged/inverse futures ETFs.
2. Data on allocations to electronics and semiconductor stocks were collated from SITE websites as of January 2025.
3. In February 2025, the FSC indicated that if the proposed rule amendments by TWSE are deemed appropriate, the 30% cap on individual securities' weights in ETF underlying indices may be lifted.