Condition and Performance of Domestic Banks

Third Quarter 2006

■ *Summary of Condition and Performance*

In the third quarter of 2006, although the declining oil price and improving international market conditions, Taiwan was still plagued by the domestic political dispute, resulting in an adverse effect to the domestic economy. In addition, the private consumption caused by the negative impact of credit card and cash cards' insolvency dragged the real domestic demand. Nevertheless, the continuous economic expansion in key export markets helped to boost Taiwan's export-oriented economy. Fueled by the strong international demand in consumer electronics, Taiwan's domestic economy still remained stable. Moreover, supported by the falling unemployment and firmer price index, there would not be obvious deterioration in consumption. According to the statistics of Directorate-General of Budget, Accounting and Statistics, Executive Yuan, the preliminary real GDP growth rate was 5.02% in third quarter , increasing by 0.78 percentage points compared with the year-earlier period.

Due to the continuing write-offs and stable economic conditions, the delinquencies of the unsecured consumer loan have declined. Moreover, most banks have adequate capital buffers to cover write-offs. The average ratio of NPLs was 2.40% , 0.01 percentage points up from 2.39% as of the end of previous quarter. The average provision coverage ratio was 43.93% , 2.82 percentage points up from 41.11% at the previous quarter's end. Generally speaking, the domestic banks under a stable outlook still need to further enhance their risk management to keep pace with future expansion into new geographic and product markets. The annual growth rate of deposits, loans and investments went up continuously.

■ *Key Trend*

The net revenues other than interest including the credit card provisions showed a sharp decrease compared with the first nine months of 2005. Higher provisions against unsecured consumer loans apparently hit profits. The major income components are tabulated as follows.

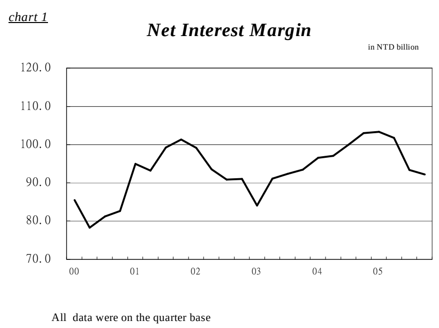
Major income components

NT$ billion

	Jan.-Sep 2005	Jan.-Sep. 2006	% Change
Income			
Net interest income	300.1	287.3	-4.3
Net revenues other than interest	145.4	64.4	-55.7
Expense			
Loan loss provision	126.1	119.1	-5.6
Other expense	196.3	197.6	0.7
Net income	123.1	35.1	-71.5

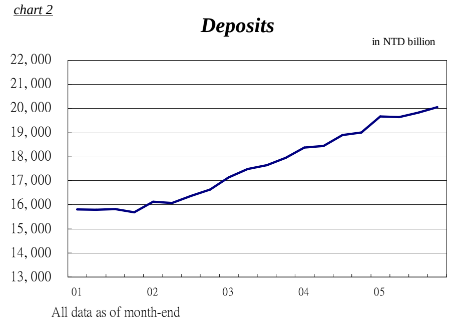
Net Interest Margin（NIM） decreasing

The NIM was NT$92.2 billion during this quarter, decreasing by NT$1.2 billion（-1.3%） compared with the previous quarter due to a shrinking card lending market and lower interest rates on restructured loans. *（chart 1）*



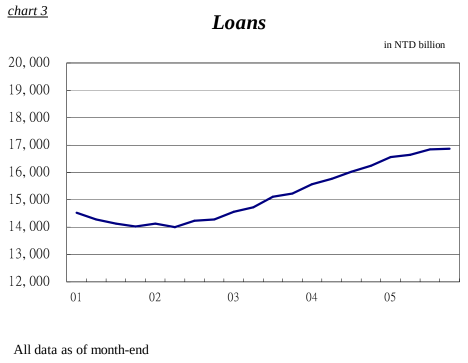
Deposits increased slightly

Total deposits as of the third quarter's end of 2006 were NT$20,060.2 billion, increasing by NT$229.8 billion (1.16%) compared with the preceding quarter. The slight increase was mainly due to the increase in net foreign capital inflows. The annual growth rate of total deposits at this quarter was 6.03 %, 0.99 percentage points down from 7.02% a year earlier. (Chart 2)



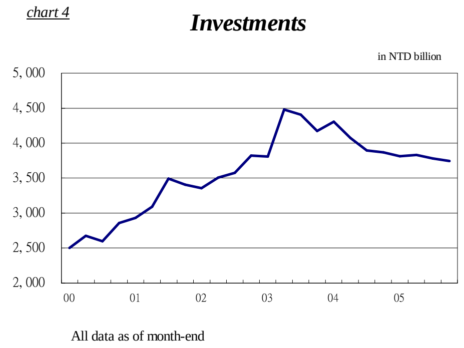
Loans grew slightly

The total loans were NT$ 16,873.0 billion at this quarter's end, increasing by NT$36.1 billion (0.21%) compared with preceding quarter. The slower growth rate was mainly due to the shrinkage of consumer loan demand from the private sector. The annual growth rate of this quarter was 5.51%, 1.05 percentage points down from 6.56% as of the previous year. (Chart 3)



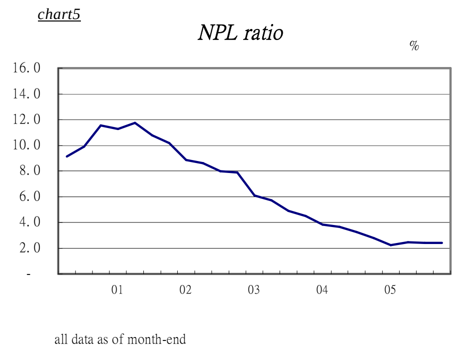
Investments decreased slightly

The investments were classified to be in line with new norms since the beginning of 2006 according to the Statements of Financial Accounting Standards No.34 "Financial instruments：Recognition and Measurement" issued by the Accounting Research and Development Foundation of the R.O.C. The total investments amounted to NT$3,741.9 billion, decreasing by NT$38.3 billion (-1.01 %) compared with the previous quarter. However, the annual growth rate of investment was 9.31%, increasing sharply by 8.17 percentage points from 1.14% as of the third quarter's end at previous year owing to the ample liquidity. (Chart 4)



Asset quality remained stable

Several banks had stung by the rising unsecured consumer loan delinquencies. The average ratio of non-performing loans at this quarter went by 0.01 percentage points up to 2.40 %. Nevertheless, most of banks have adequate capital buffers to cover write-offs. Therefore, the average provision coverage ratio was 43.93%, 2.82 percentage points increased from 41.11% as of previous quarter, reaching the required target. (Chart 5)

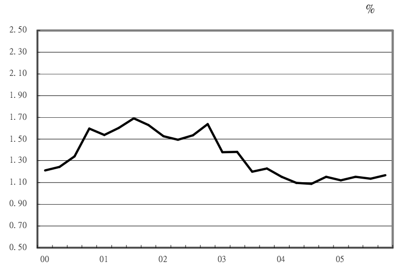


Provision-to-loan ratio on a slight rising trend

The provision-to-loan ratio was 1.17％ , slightly up from 1.13％ at the end of preceding quarter. The increased provision-to-loan ratio was mainly due to the increase of loan loss provisions. It showed the prudential trend of credit policies. （Chart 6）

chart 6

Provision-to-loan ratio

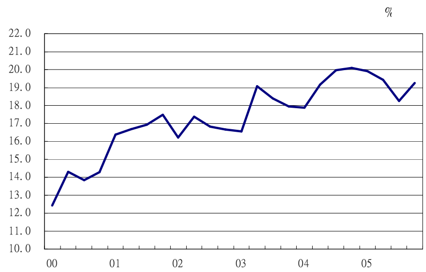


All data as of month-end

Liquidity Ratio increasing slightly

The liquidity ratios of all domestic banks were over the statutory minimum ratio (7%) in September 2006. The average liquidity ratio was 19.26%, increasing by 1.01 percentage points from 18.25 % in June 2006. As a whole, the domestic banking sector has satisfactory liquidity levels. (Chart 7)

chart 7 **Liquidity Ratio**



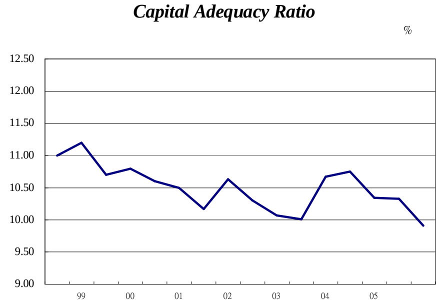
All data were in terms of the average of the last month of quarters.

Average Capital Adequate Ratio decreased

The average BIS capital adequacy ratio was 9.91% as of the end of September 2006, decreasing by 0.42 percentage points from 10.33% at the end of June 2006. Taken as a whole, most of the domestic banks have adequate capitalization. The average BIS capital adequacy ratio will be disclosed quarterly since the third quarter of this year. The data disclosed at each first quarter and third quarter’s end were based on unaudited basis. (Chart 7)

chart 8

Capital Adequacy Ratio



All data as of month-end