

III. Central Bank Operations

1. Overview

Taiwan's domestic demand was fragile at the start of 2009. During the first two months of 2009, as the inflationary pressure remained largely subdued, the Bank twice lowered policy rates by a total of 75 basis points to boost domestic demand. Despite economic activity regaining momentum from March onwards, the CBC left the rates unchanged to further support the economy.

Meanwhile, to provide ample liquidity to the market and to promote financial stability, the CBC continued to create a favorable financial environment. As economic and financial conditions improved from April onwards, the CBC adjusted its quantitative easing policy by increasing open market operations, bringing the net excess reserves in the banking system down to NTD 39.9 billion in December, from NTD 154.1 billion in April. The annual growth rates of reserve money and M2 monetary aggregates also trended downwards from the second half of 2009.

In terms of foreign exchange management, the CBC also lifted restrictions on various foreign exchange regulations, and continued its efforts to encourage banks to engage in the foreign exchange derivatives business. To strengthen consumer protection, the CBC also reasserted that banks have to fully disclose the attendant risks to customers. This year, the CBC also allowed many financial institutions and designated places to provide Chinese RMB exchange services to accommodate the needs of increasing tourists from the mainland China as a result of the improvement in cross-strait relations.

To assure the smooth operations of the payment system, the CBC closely monitored domestic payment systems and urged each settlement institution to set up backup facilities and adequate contingency plans to provide business continuity. The CBC also established the central government bond buyback system, which not only enhanced the liquidity of the central government bond market, but also strengthened its management efficiency and lessened the interest burden of the government.

To promote the sound operation of financial institutions and safeguard financial stability, the CBC has established an off-site review system and a framework for financial stability to ensure that any potential risks to the financial system are effectively managed.