3. Foreign Exchange Management

Foreign Exchange Market Management

Taiwan's exchange rate regime is a managed float, where in principle the exchange rate is determined by supply and demand in the foreign exchange market. If the market is disrupted by seasonal or irregular factors (e.g. large flows of short-term capital), causing the exchange rate to become excessively volatile, the Bank may step in to maintain an orderly foreign exchange market.

To monitor market activities, the Bank continued to implement the Real-Time Reporting System for Large-Amount Foreign Exchange Transactions. In addition, the requirement that forward transactions should be made only upon real transactions, such as trade and financing, was reinforced in order to curb foreign exchange speculation. The Bank also urged authorized banks to enhance their exchange rate risk management so as to lower their risk exposures and systemic risks. Moreover, the Bank strengthened target examinations to maintain an orderly foreign exchange market.

Management of Foreign Exchange Swap and Foreign Currency Call Loan Business

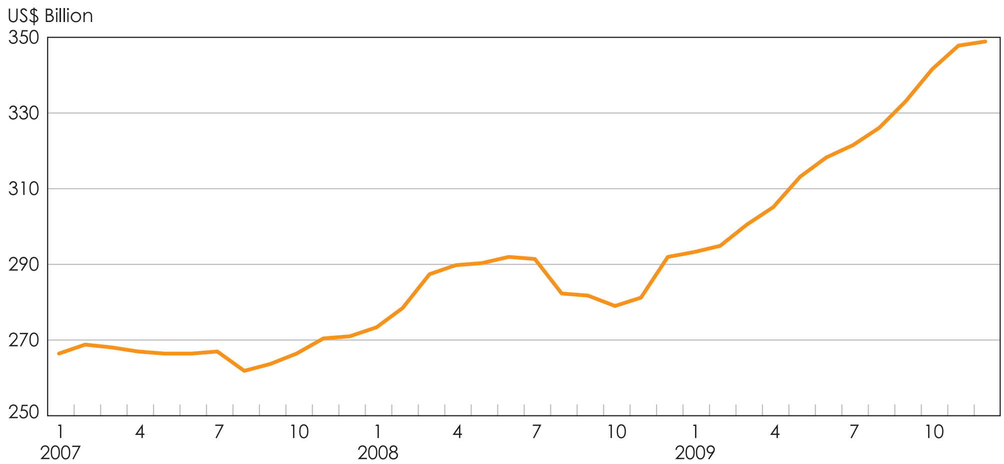
In order to provide the financial system with sufficient foreign currency liquidity to meet funding needs, including corporate needs to venture into overseas markets, the Bank provided US$20 billion, €1 billion and ¥80 billion as seed funds for the Taipei Foreign Currency Call-Loan Market.

Meanwhile, the Bank continued to carry out foreign currency swap transactions with banks and extended foreign currency call loans to banks so as to facilitate corporate financing smoothly. During 2009, foreign exchange call loan transactions reached US$1,473 billion, while foreign currency-NT dollar swap transactions reached US$703.4 billion.

Foreign Exchange Reserve Management

In 2009, the Bank's foreign exchange revenues amounted to US$825.8 billion, while foreign exchange expenditure was US$769.3 billion. At the end of 2009, total foreign exchange reserves stood at US$348.2 billion, a US$56.5 billion increase from the end of 2008. The increase was mainly attributable to a higher return on investment of foreign exchange reserves, and the appreciation of the euro and the British pound against the US dollar.

Foreign Exchange Reserves



Source: Department of Foreign Exchange, CBC.

Capital Flow Management

With the progress of financial liberalization and internationalization, the Bank has gradually deregulated capital movement restrictions since 1980s. In general, capital can flow freely in and out of Taiwan. As of 2009, restrictions only remained on a few short-term financial transactions involving the conversion of the NT dollar. For example, a domestic company or a resident can each conduct inward and outward remittances up to US$50 million and US$5 million, respectively, within one year. A non-resident may remit up to US$100 thousand per transaction. For remittances exceeding the respective ceilings, transactions may be made with the approval in advance from the Bank.

Key measures with regard to the management of foreign exchange in 2009 included:

(1) Having consulted with the Financial Supervisory Commission about a broader scope for foreign securities investment, the Bank agreed to the following measures: (i) Agreed June 9, foreign investors would be allowed to invest in beneficiary certificates of futures trust funds; (ii) Agreed September 10, foreign investors would be allowed to invest in separable warrants issued with corporate bonds or preferred stocks of TSE and OTC listed companies.

(2) In order to promote the internationalization of Taiwan's capital market, the Bank agreed to the following in 2009: (i) The issuance of overseas depository receipts by 11 corporations with a total of US$2.94 billion and the issuance of European Convertible Bonds by 6 corporations with a total of US$1.43 billion ; (ii) The issuance of Taiwan Depository

Receipts (TDRs) by 18 foreign corporations with the total amount reaching NT$34 billion; (iii) BNP Paribas and Deutsche Bank may raise and issue foreign currency corporate bonds up to US$1 billion each.

(3) The Bank agreed to an increase in residents' investments in foreign securities, as follows: (i) Securities investment trust companies were allowed to raise 37 securities investment trust funds domestically to invest in foreign securities worth a total of NT$315 billion; (ii) Life insurance companies were given consent to invest in foreign securities with the amount totaling US$0.98 billion, while their investment-linked insurance products invested a total of US$2.39 billion in foreign securities through non-discretionary money trusts managed by financial institutions; (iii) Three major government pension funds and the Postal Savings Fund invested in foreign securities with the total amount reaching US $2.20 billion.

(4) The Bank loosened the following regulations regarding foreign exchange remittances: (i) On May 25, the Bank notified authorized foreign exchange banks that, effective from June 1, banks would be allowed to conduct foreign exchange settlement related to foreign workers' salaries as consigned to employment agencies with proper documents; (ii) On June 15, the Bank notified financial institutions undertaking non-discretionary money trust for investment in foreign securities that, effective from June 17, the types and scope of such investments shall comply with the FSC rules and regulations, instead of relevant circulars issued by the Bank prior to September 19, 2005; (iii) In light of improved cross-Strait relations, the FSC amended the regulations governing cross-Strait remittances; the Bank also made relevant amendments regarding documents to be confirmed about remittances to or from Mainland China, effective from June 30; (iv) The Bank announced that overseas donations for Typhoon Morakot relief would be exempted from the declarer's annual accumulated amount of foreign exchange settlements, effective from August 17.

Management of the Foreign Exchange Business of Financial Institutions

(1) At the end of 2009, there were 1,478 authorized foreign exchange banks in total, which included 36 head offices and 1,346 branches of domestic banks, 96 branches of 32 foreign banks, as well as 2,558 authorized money exchangers, postal offices and financial institutions authorized to engage in basic foreign exchange business.

(2) In 2009, the Bank permitted the issuance of 20 foreign exchange derivative products in order to expand the scope of banking services. However, for investor protection, the Bank notified all banks in June of the need to formulate and implement the principle of Knowing Your Customers in managing foreign currency margin transactions and

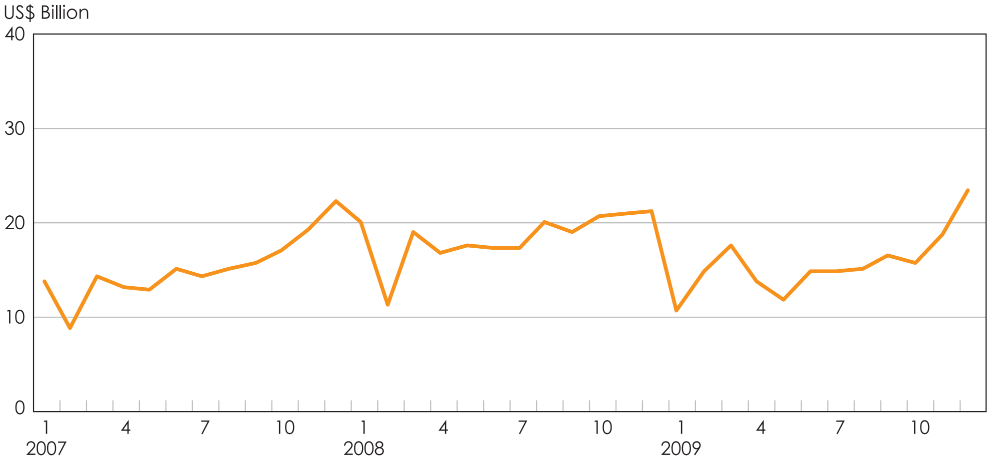
structured products, and to fully disclose related risks, so as not to mislead customers.

(3) Up to the end of 2009, 15 insurance companies were allowed to engage in foreign currency investment-linked insurance business, and 9 insurance companies were permitted to conduct business in relation to traditional foreign currency insurance products.

(4) In 2009, the government approved 44 financial institutions (with a total of 3,103 branches) and 156 authorized money exchangers to conduct the Chinese renminbi (RMB) cash exchange business. The total amount of renminbi purchased was RMB 5.71 billion, while the total sale was RMB 7.08 billion.

(5) Since June 2001, OBUs have been approved to conduct cross-Strait remittances. The steady growth had gradually turned OBUs into funding arrangement centers for overseas Taiwanese businessmen. In 2009, due to the global financial crisis, cross-Strait remittances amounted to US$185.2 billion, a decrease of US$33.9 billion, or 15.5 percent, from last year.

Cross-Strait Remittances through OBUs



Source: Department of Foreign Exchange, CBC.