III. Non-financial sectors

The corporate sector, household sector, and real estate market constitute the main sources of risk for credit exposure of Taiwan's financial institutions. The degree of indebtedness and solvency in the corporate sector and household sector, as well as the real estate cycle, have far-reaching impacts upon the asset quality and profitability of financial institutions.

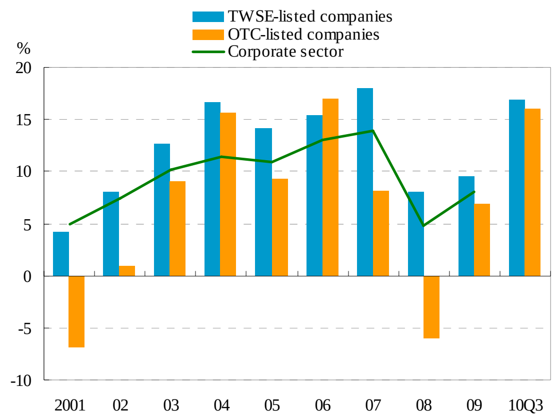
3.1 Corporate sector

From the second half of 2009 onward, overall profitability of the corporate sector improved amidst gradual recovery of the global and domestic economies. Driven by increased foreign and domestic demand, the performance of both Taiwan's export and industrial production was strong in 2010, which resulted in significantly increase of the profitability of TWSE-listed and OTC-listed companies for the first three quarters of 2010 compared to the same period of the previous year. The leverage ratio increased slightly due to rising liabilities caused by an expansion in production capacity, while the current ratio showed some decrease. However, the interest servicing capacity of corporate sector enhanced and the credit quality of corporate loans remained sound, as the NPL ratio continuously decreased. Nevertheless, the impact of the Japan's earthquake and the price hikes in energy and raw materials on the profitability of domestic corporations and supply chain requires continuous attention and timely responses.

Profitability increased continuously throughout 2010

The profitability of the corporate sector gradually increased amidst the recovery of the global economy and improvements in domestic economic indicators from the second half of 2009. The return on equity

Chart 3.1 Return on equity in corporate sector

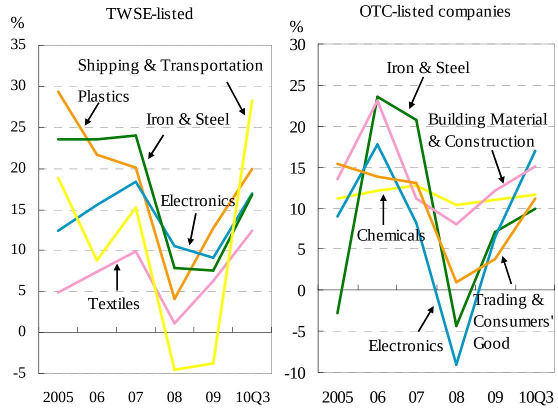


Notes: 1. Return on equity = net income before interest and tax / average equity.
2. The data are on an annual basis as 2010 Q3 figures are annualized results.
3. Latest data for the corporate sector is as of the end of 2009, while that for TWSE-listed and OTC-listed companies are as of the end of 2010 Q3.
Sources: JCIC and TEJ.

(ROE) for the corporate sector increased to 8.07% in 2009 as TWSE-listed and OTC-listed companies' ROEs rose to 9.58% and 6.91%, respectively. Thanks to the strong growth of emerging countries and increased demand from Europe and the United States, total export/import value, export orders, the industrial production index and its annual growth rate in 2010 all reached historical highs. All of these, together with a steady increase in private consumption, greatly enhanced the profitability of the corporate sector. The annual ROEs for TWSE-listed and OTC-listed companies rose to 16.95% and 16.01%, respectively, for the first three quarters of 2010, much higher than those reported in 2009 (Chart 3.1).

All major industries for TWSE-listed companies reported rebounding profitability for the first three quarters of 2010. Among them, the shipping and transportation industry stood out, returning to profit from loss and delivering an ROE that hit a 10-year high. For OTC-listed companies, the profitability of the electronics industry, which accounted for more than 75% of total revenue of OTC-listed companies, was the best. Other industries also saw better performance than in 2009 (Chart 3.2).

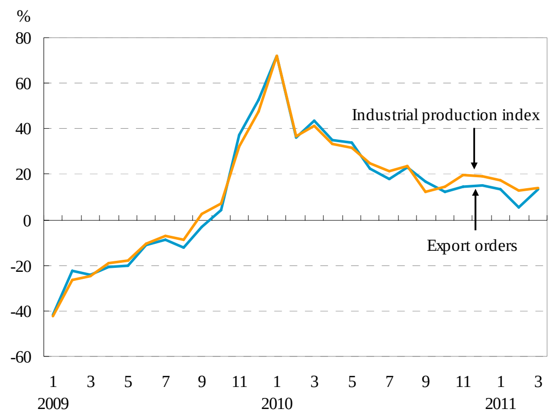
Chart 3.2 Return on equity of TWSE-listed and OTC-listed companies by major industries



Notes: 1. Return on equity = net income before interest and tax / average equity.
2. The data are on an annual basis as 2010 Q3 figures are annualized results.

Source: TEJ.

Chart 3.3 Annual growth rates of export orders and industrial production index



Note: Industrial production index in 2006 was 100.

Source: MOEA.

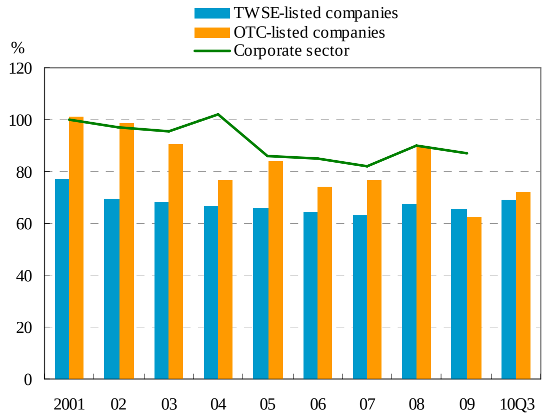
In 2010, driven by rising global demand, Taiwan's export orders and the industrial production index increased by 26.14% and 26.93%, respectively, for the whole year, and registered double-digit annual growth for each month. Moreover, underpinned by strong sales of smartphones and tablet computers, and the surging demand for inventory amid concerns over supply chain disruption caused by the Japan's earthquake, Taiwan's export orders and the industrial production index hit a record high in March 2011 with annual growth rates of

13.37% and 13.82%, respectively (Chart 3.3). Looking ahead, steady global economic growth, strong demand from Mainland China and tariff cuts on items included in the Early Harvest List under the Cross-Strait Economic Cooperation Framework Agreement (ECFA) that came into effect on 1 January 2011 are expected to support the profitability of the corporate sector in the future.

Rising leverage ratio for listed companies

For the corporate sector as a whole, the financial structure improved and the average leverage ratio fell to 86.88% at the end of 2009 as the recovery of profitability increased its equity. In 2010, with expectations of further economic recovery, domestic corporations expanded production capacity and in turn increased liability. As a result, the average leverage ratios for TWSE-listed and OTC-listed companies rose to 69.01% and 72.17%, respectively, at the end of September 2010, but still lower than those for the entire corporate sector in 2009 (Chart 3.4).

Chart 3.4 Leverage ratio in corporate sector

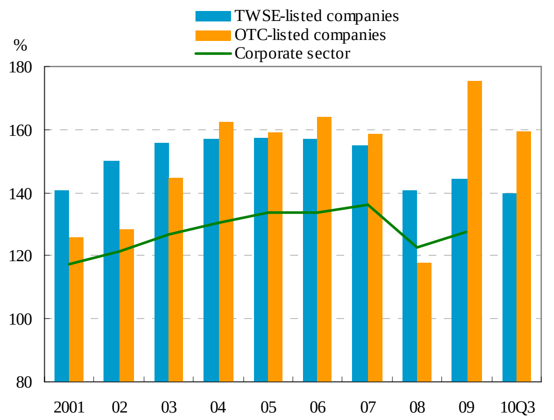


Notes: 1. Leverage ratio = total liabilities / equity.
2. End-of-period figures.
3. Latest figure for the corporate sector is as of the end of 2009, while those for TWSE-listed and OTC-listed companies are as of the end of 2010 Q3.
Sources: JCIC and TEJ.

Decreasing current ratio for listed companies, but interest servicing capacity remained strong

In 2009, short-term debt servicing capacity of the corporate sector as a whole improved with both the current ratio and the interest coverage ratio rising to 127.65% and 8.54, respectively, due to increases in current assets and income. The current ratios for TWSE-listed and OTC-listed companies fell to 139.71% and 159.69%, respectively, at the end of September 2010 as a result of increased short-term liabilities. Owing to the

Chart 3.5 Current ratio in corporate sector



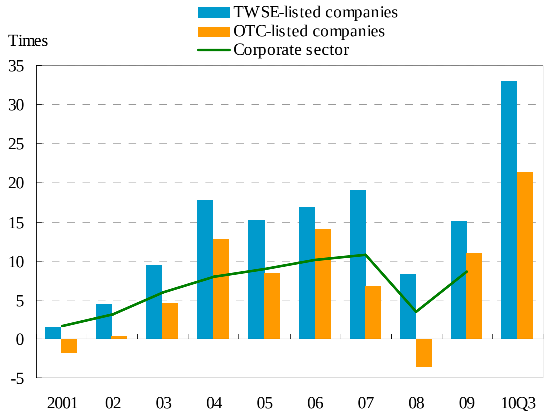
Notes: 1. Current ratio = current assets / current liabilities.
2. End-of-period figures.
3. Latest figure for the corporate sector is as of the end of 2009, while those for TWSE-listed and OTC-listed companies are as of the end of 2010 Q3.
Sources: JCIC and TEJ.

profitability boom in the first three quarters of 2010, however, the interest coverage ratios for TWSE-listed and OTC-listed companies leaped to 33.07 and 21.38, respectively, the highest levels since 2001 (Chart 3.5 & 3.6), reflecting that interest servicing capacity of corporate sector significantly improved.

Credit quality of corporate loans remained sound

The NPL ratio for corporate loans continued to decline to 0.88% at the end of 2010 due to a continuation of decreasing non-performing corporate loans (Chart 3.7). During the global financial crisis, Taiwan's government adopted several special financing measures in support of corporations, such as the Debt Renegotiation Relief Program and associated supporting arrangements that expired at the end of 2010. The expiration of the aforementioned program, which brought corporate financing back to the market mechanism, together with rising market interest rates that followed the policy rate rises of the CBC, resulted in doubts about whether some weaker or less competitive corporations may once again face financing and interest repayment pressures. This situation is worthy of close attention.

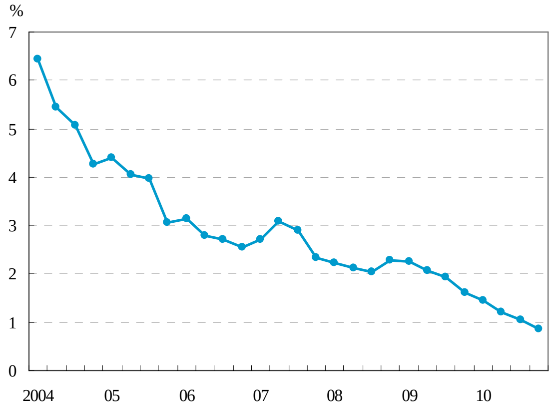
Chart 3.6 Interest coverage ratio in corporate sector



Notes: 1. Interest coverage ratio = income before interest and tax / interest expenses.
2. Figures are on an annual basis as 2010 Q3 referred to the accumulation from January to September 2010.
3. Latest figure for the corporate sector is as of the end of 2009, while those for TWSE-listed and OTC-listed companies are as of the end of 2010 Q3.

Sources: JCIC and TEJ.

Chart 3.7 NPL ratio of corporate loans



Note: End-of-period figures.
Source: JCIC.

Meanwhile, the recent price hikes on imported raw materials may put industries that consume a lot of energy or rely heavily on imported raw materials for production under pressure of rising costs and shrinking profits. In addition, the impact of the Japan's earthquake and nuclear plant crisis on domestic electronics and automobile industry's supply chains, the rise in the price of oil as a result of turmoil in North Africa and the Middle East, and the aggravated exchange rate volatility in emerging economies all contributed to an environment of elevated business risk for corporations, which warrants close attention and timely responses.

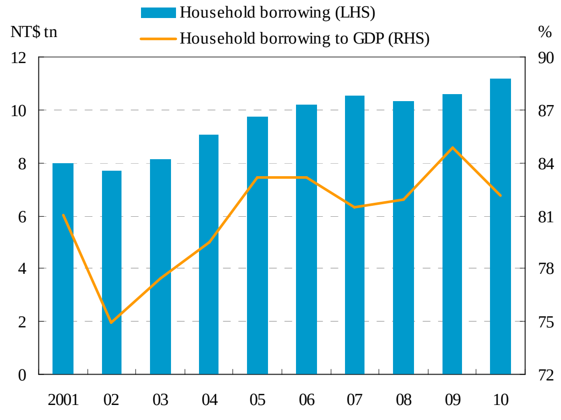
3.2 Household sector

The household debt burden eased and debt servicing capacity strengthened as disposable income expanded faster than borrowing. Overall credit quality of household borrowing also remained satisfactory. However, as interest rates gradually move upwards, highly leveraged households may face even heavier indebtedness. Thus, the debt repayment capacity for those households warrants close attention.

Household borrowing slightly increased

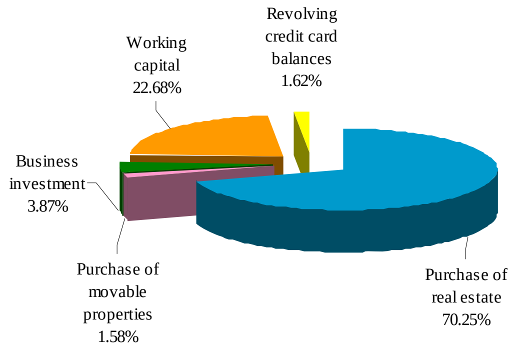
Following booming local stock and real estate markets, total household borrowing[44] at the end of 2010 reached NT$11.19 trillion (Chart 3.8) with an year-on-year growth rate of 5.69%. The largest share of household borrowing went for the purchase of real estate (70.25%), followed by working capital loans[45] (22.68%), while revolving balances on credit cards accounted for only 1.62% (Chart 3.9). Except for revolving credit card balances, the balances for every other kind of loan increased in 2010. Among them, business investment loans, mainly for margin purchases, had the greatest annual growth rate of 29.92%, while real estate purchase loans increased by 4.72%.

Chart 3.8 Household borrowing to GDP



Note: Household borrowing data are end-of-period figures.
Sources: CBC, JCIC and DGBAS.

Chart 3.9 Household borrowing by purpose



Note: Figures are as of the end of 2010.
Sources: CBC and JCIC.

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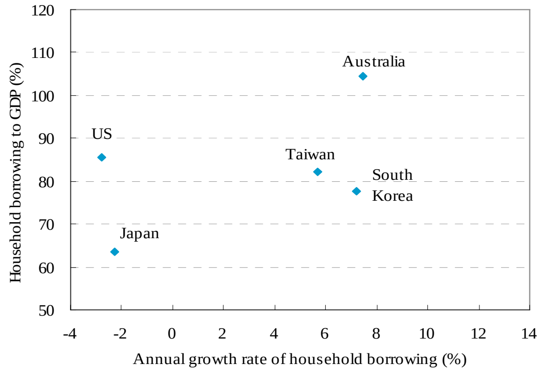
[44] The term "household borrowing" as used in this section refers to outstanding loans and revolving credit card balances taken out by households from the following financial institutions:
(1) Depository institutions: domestic banks (including medium business banks), local branches of foreign banks, credit cooperatives, credit departments of farmers' associations, credit departments of fishermen's associations, and the Remittances & Savings Department of Chunghwa Post Co.
(2) Other financial institutions: trust and investment companies, life insurance companies, securities finance companies, and securities firms.

[45] The term "working capital loans" includes outstanding cash card loans.

The ratio of household borrowing to GDP dropped to 82.17% at the end of 2010, mainly due to a much faster pace in GDP growth (Chart 3.8). Compared to other selected countries, the growth of total household borrowing in Taiwan, South Korea, and Australia remained positive and higher than the previous year. As a percentage of GDP, household borrowing in Taiwan was lower than in the US and Australia, but higher than in South Korea and Japan (Chart 3.10).

Chart 3.10 Household indebtedness in selected countries

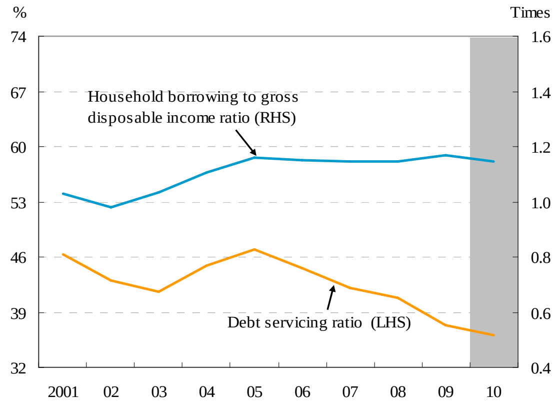


Note: Figures for Taiwan are as of the end of 2010. The others are as of the end-September 2010.
Sources: Fed, BOJ, BOK, ABS, IMF, DGBAS, CBC and JCIC.

Household short-term debt servicing capacity slightly improved

In 2010, as total household borrowing increased at a slower pace than disposable income,[46] the ratio of household borrowing to gross disposable income was brought back to 1.15 times, reflecting a slightly reduced debt burden.

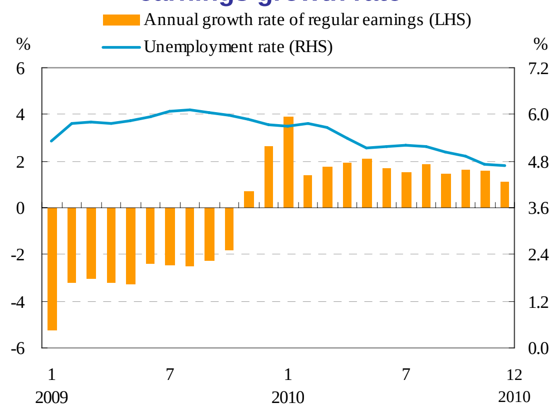
Chart 3.11 Household debt servicing ratio



Notes: 1. Gross disposable income in shadow area is CBC estimate.
2. Debt servicing ratio = borrowing service and principal payment / gross disposable income.
Sources: CBC, JCIC and DGBAS.

The debt servicing ratio decreased year by year and registered 36.12% at the end of 2010 due to the increase in household disposable income that was triggered by domestic economic recovery. Household short-term debt servicing capacity thus improved (Chart 3.11).

Chart 3.12 Unemployment rate and regular earnings growth rate



Source: DGBAS.

The fact that both the domestic unemployment rate gradually decreased and the regular earnings growth rate turned positive in 2010 helped to improve the debt servicing capacity of household sector (Chart 3.12). However, as the CBC raised interest

46 Gross disposable income = disposable income + rental expenses + interest expenses.

rates by 0.125% each time for four times from June 2010, inducing lending rates to move upward, the debt repayment pressures of highly leveraged households might increase and thus warrants close attention.

NPL ratio of household borrowing dropped to record low

At the end of 2010, the NPL ratio of household borrowing from banks was down from 1.41% a year earlier to 0.77%, the lowest level in ten years (Chart 3.13). The main reason behind this was that NPLs for real estate purchases, the largest share of household borrowing, contracted due to the real estate market rebound in 2010.

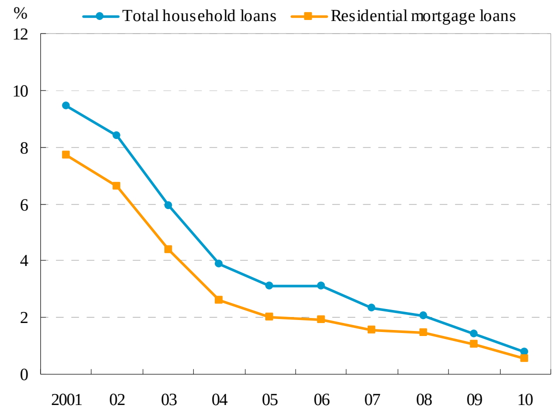
3.3 Real estate market

The real estate market continued to warm up in 2010, while house prices in specific areas surged and mortgage burdens elevated. Outstanding real estate-related loans continued to increase, albeit at a decreasing growth rate, as mortgage interest rates slowly rose. In response to surging house prices in specific areas and the concentration of banks' credit in the real estate market, the government implemented a series of measures and the housing market began showing signs of cooling starting February 2011. Its potential impact on the real estate-related business and asset quality of financial institutions is worth closer monitoring.

Real estate market rebounded

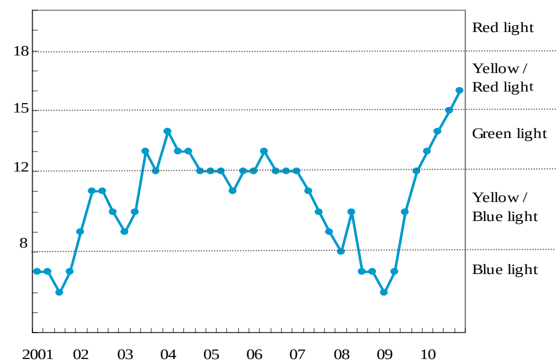
Taiwan's real estate cycle indicators [47] jumped to a 10-year high of 16 points in 2010 Q4, a yellow/red light indicating a

Chart 3.13 NPL ratio of household borrowing



Note: End-of-period figures.
Source: JCIC.

Chart 3.14 Real estate cycle indicators

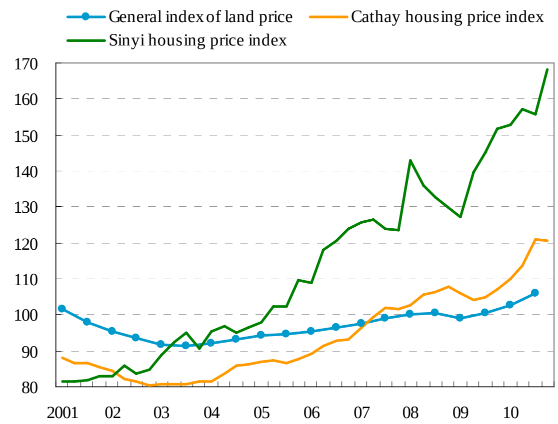


Sources: "Quarterly Report of Taiwan Real Estate Cycle Indicators," Architecture and Building Research Institute, Ministry of the Interior (MOI); Taiwan Real Estate Research Center.

[47] The real estate cycle indicators show five types of market outlooks with different colored lights. A red light indicates a "heated market," a yellow/red light indicates a "moderately heated market," a green light indicates a "stable market," a yellow/blue light indicates a "moderately declining market," and a blue light indicates a "sluggish market."

moderately heated market, compared to 6 points of blue light indicating a sluggish market in 2009 Q1 (Chart 3.14). The composite indices of leading indicators[48] and coincident indicators[49] also displayed upward trends, revealing that the real estate market was apparently warming up. However, the recent survey showed that sentiment of real estate firms regarding the property market in the first two quarters of 2011 turned weak as a result of the proposed implementation of the Specifically Selected Goods and Services Tax.

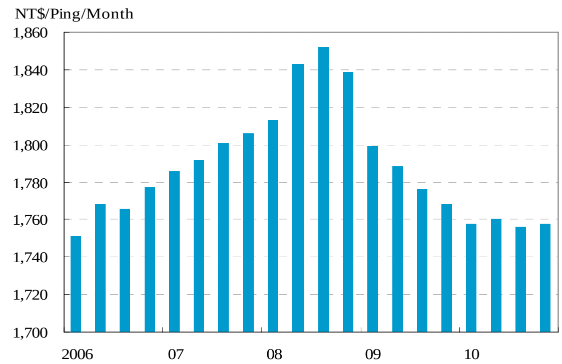
Chart 3.15 Land and house price indices



Note: General index of land price is released semiannually (i.e. in March and September).
Sources: MOI, Cathay Real Estate, and Sinyi Real Estate Inc.

House prices rose as the property market warmed up but turned cautious in February 2011

Chart 3.16 Average office rental rate in Taipei



Source: Colliers International "Taipei Office Market Overview."

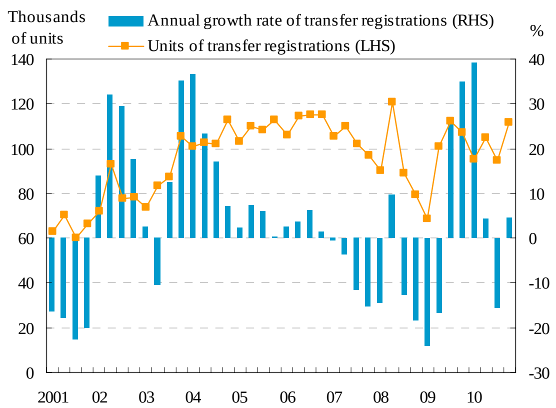
Inspired by an influx of short-term international capital, the signing of the ECFA and the upgrading of five cities, real estate prices continued to climb and indices repeatedly struck new highs in 2010. The Taiwan area land price index hit 105.93 in September 2010, dramatically rising by 5.53% year on year. In addition, the Sinyi housing price index (for existing buildings) reached 168.25 in the fourth quarter of 2010, up 10.91% year on year, with the sharpest increase coming in Taipei City and New Taipei City, while the Cathy housing price index (for new construction) also climbed to 120.77, up 12.95% year on year (Chart 3.15), with housing prices in several regions hitting new highs time and again. Starting from February 2011, however, as the CBC and the FSC implemented measures to strengthen the banks' risk management on real estate-related loans, and the MOF proposed to implement the Specifically Selected Goods and Services Tax, the house buyer bargaining power increased in the areas where construction projects has risen notably.

48 The composite index of leading indicators is made up of the following five components: GDP, monetary aggregate M2, construction sector's stock price index, changes of outstanding construction loans, and consumer price index.
49 The composite index of coincident indicators is made up of the following six components: undeveloped land transaction index, base lending rate, construction permit floor space, standard unit price for new construction projects, new loans for property purchases, and housing occupancy rate.

Despite surging house prices in Taipei in 2010, the momentum of rising office rentals weakened due to the release of new offices and declining office demand as financial firms' offices integrated and corporations moved out. The average office rental rate was NT$1,758 per ping (approximately 3.3 square meters) per month in 2010 Q4, a slight year-on-year decrease of 0.57% (Chart 3.16).

As for transactions in the housing market, market conditions were prosperous in the first half of 2010, but cooled down in Q3 as a result of measures that aimed to strengthen the risk management on real estate-related loans of banks, and then rebounded in Q4 as the market expected an upward movement of house prices. The number of building ownership transfers registered 407 thousand units for the whole year of 2010, up 4.74% year on year (Chart 3.17). The housing market continued to warm up in the first two months of 2011, as the number of building ownership transfers for those two months increased by 7.84% year on year. However, the market sentiment became cautious in March as a result of the proposed promulgation of the Specifically Selected Goods and Services Tax.

Chart 3.17 Building ownership registrations



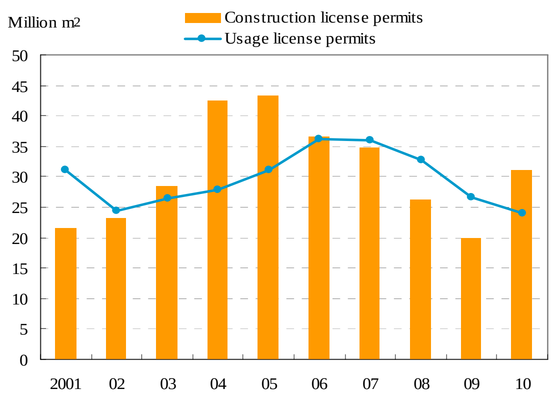
Source: Monthly Bulletin of Interior Statistics, MOI.

The supply outlook for new properties is expanding and residential property vacancies remain high

Affected by a decrease of new construction projects over the past few years, the total floor space of usage permits dropped by 9.5% in 2010 (Chart 3.18). Those for commercial and residential property both showed declines, with a higher decrease of 52.73% for commercial property.

In 2010, inspired by the buoyant housing market, the real estate industry acted more aggressively with regard to introducing new construction projects. Total floor space of construction license permits substantially increased by 56.53% year on year, with the largest increase of 65.92% for residential

Chart 3.18 Floor space of construction license permits and usage license permits



Source: Monthly Bulletin of Interior Statistics, MOI.

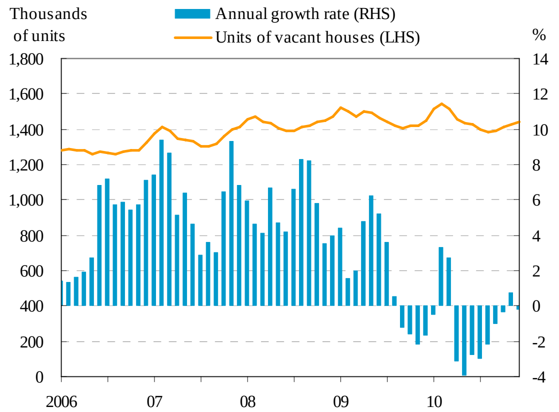
property. If analyzed by cities, Taichung City and New Taipei City saw the highest growth. Considering that the real estate industry competes to build new construction, new house supplies will increase in the future.

As estimated by the number of units consuming less electricity than the minimum service charge from the Taiwan Power Company, the average number of vacant residential properties in 2010 decreased 0.86% year on year, but still stood at the high level of 1.445 million units (Chart 3.19).

Mortgage burden kept increasing

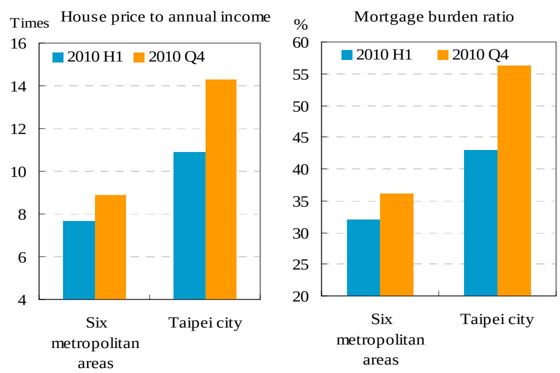
Following climbing housing prices, the mortgage burden continuously increased for house buyers. The average house price to income ratio for the six metropolitan areas reached 8.9 in 2010 Q4 as the average mortgage burden ratio registered 36.0%, both reaching new highs. Among the metropolitan areas, the mortgage burden was heaviest in Taipei City as the housing price to income ratio and mortgage burden ratio reached 14.3 and 56.2%, respectively (Chart 3.20).

Chart 3.19 Estimated units of vacant houses



Source: Taiwan Power Company.

Chart 3.20 House price to income ratio and mortgage burden ratio



Note: Mortgage burden ratio = monthly mortgage expenditure / household monthly income.
Source: "Taiwan Housing Demand Survey Report," MOI.

Real estate-related loans continued to grow but at a slower pace, while mortgage interest rates gradually increased

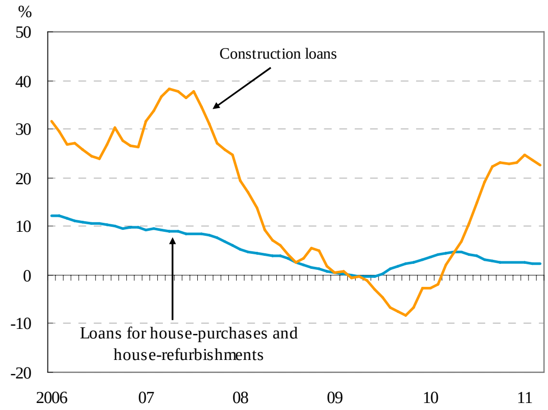
Outstanding loans for house purchases and house refurbishments granted by banks [50] continued to grow and reached a historical high of NT$5.83 trillion at the end of 2010. Although the annual growth rate of such loans continued to increase in the first two quarters of 2010, it turned to be more temperate in Q3

[50] Refers to domestic banks and the local branches of foreign banks.

and slid to 2.53% in December 2010 due to the effect of the CBC's measures to strengthen the risk management on real estate-related loans of banks. Construction loans steadily climbed and reached NT$1.29 trillion in December 2010 with the annual growth rate bouncing to 23.2% from -2.77% a year earlier. In 2011 Q1, the growth of loans for house purchases and house refurbishments continued to slow with an annual growth rate of 2.30% in March. Total outstanding construction loans repeatedly reached new highs, though the annual growth rate slightly moderated to 22.68% in March 2011 (Chart 3.21).

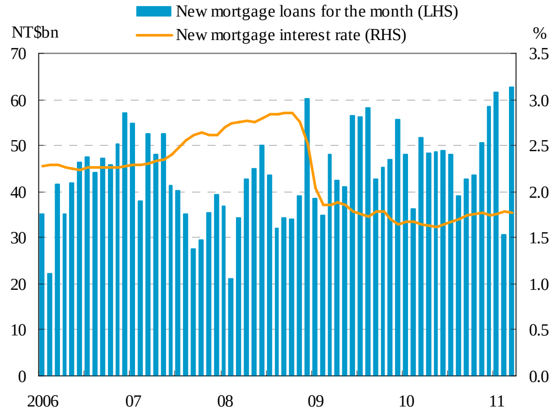
New loans for house purchases granted by the five largest banks remained at high levels in the first half of 2010. Due to the CBC's measures to strengthen mortgage risk management, new loans for house purchases contracted in the third quarter but resumed their climb in October and reached a new high of NT$62.6 billion in March 2011 as the property market warmed up. With respect to financing costs, the interest rate for new mortgages decreased to 1.62% in May 2010 and gradually rebounded to 1.77% in March 2011, following the CBC's policy rate hikes (Chart 3.22).

Chart 3.21 Annual growth rate of real estate-related loans



Source: CBC.

Chart 3.22 New mortgages – amount and interest rate



Source: CBC.

Government adopted a series of measures in response to surging house prices

In response to surging house prices in specific areas and banks' excessive concentration of credit in real estate related loans, the CBC, the Ministry of Finance, and the FSC have adopted the following measures to enhance the soundness of the housing market and financial stability:

1. The CBC has adopted a series of targeted prudential measures since October 2009, including moral suasion and the promulgation of the Regulations Governing the Extension of Land Collateralized Loans and Housing Loans in Specific Areas by Financial Institutions (Box 4) with the aim of discouraging property and land

speculation fueled by bank credit and urging financial institutions to enhance risk management associated with credit extension so as to protect depositors' rights and promote financial stability.

2. The MOF reinforced tax audits on speculative real estate transactions and proposed the Specifically Selected Goods and Services Tax, which imposes a tax of 10%~15% on the sale price of non-self-use residences and city land with building permits (land for construction in urban planning areas) that were bought less than two years ago, while not applicable to reasonable, ordinary or involuntary transfers of properties. The aforementioned statute was promulgated by the President on 4 May 2011 and took effect from 1 June 2011.

3. On 21 March 2011, the FSC announced three measures to supervise the real estate lending risks of banks, including: (1) clearly defining self-use residence loans and raising capital charges for non-self-use residence loans;[51] (2) requesting banks to strengthen concentration risk management of real estate lending, ascertain the purpose of loans and cautiously determine real estate values; (3) including the extension of real estate lending into one of the key items subject to financial examination.

In summary, the overall asset quality of real estate-related loans remained satisfactory, with the average NPL ratio staying low for the time being. However, as the property market has begun to show signs of cooling, it may undermine the real estate related credit extension business and asset quality of financial institutions and thus warrants close attention.

[51] The FSC issued a directive on 21 April 2011, allowing the use of either a 45% risk weight or 35%/75% risk weight under the LTV method for new self-use residence loans granted by banks, while non-self-use residence loans were assigned a risk weight of 100%. Self-use residence loans refer to loans applied for by nationals without domestic residence for the purpose of purchasing residences for self-use.

Box 4
The CBC's targeted prudential measures to stablize the property market

In view of a surge in housing prices in specific areas and excessive concentration of the loan portfolios of banks, the CBC successively launched a range of targeted prudential measures to safeguard the financial system and the development of the property market from October 2009. The measures included: (1) moral suasion to financial institutions; (2) improvement in the collection and analysis of statistics; and (3) regulations to govern real-estate loans in specific areas granted by financial institutions. With the aforesaid measures, the CBC aimed at urging banks to strengthen their risk management of real estate loans and promoting sound development of the property market.

1. Moral suasion to financial institutions and improvement in the collection and analysis of housing loan data from October 2009

Initially, the CBC adopted the following measures:

- Urged banks to rein in risks related to mortgage loans (October 2009);
- Addressed asset market problems in the Board meeting and reached a decision under which the Board will take asset prices into account in its monetary policy setting (December 2009);
- Requested the Bankers Association of the Republic of China to remind borrowers of preferential loans regarding the risk of increasing repayment and rising effective interest rates as soon as grace periods expire (January 2010);
- Used moral suasion to encourage 15 domestic banks with regard their investment-oriented borrowers to: (1) lower the loan to value (LTV) ratio (ceiling of 70%); (2) raise the interest rate higher than that of general housing loans; and (3) remove the grace period (March 2010); and
- Required banks to submit call reports regarding the extension of newly approved mortgage loans to general borrowers and investment-oriented borrowers by region every 15 days. Target examinations will be undertaken where necessary, so as to ensure banks' compliance with the aforementioned policies (April 2010).

2. Regulations to govern the extension of housing loans in specific areas by financial institutions in June 2010

Most banks adjusted their mortgage loan policies in the face of a range of moral suasions by the CBC. Nevertheless, concerns about the excessive concentration on real estate loans of banks lingered, and the house-purchase burden faced by homebuyers grew heavier on the back of the notable rise in housing prices in specific areas. Meanwhile, there was an increasing need for a uniform lending standard for housing loans among financial institutions. Against this backdrop, the CBC Board approved the promulgation of the Regulations Governing the Extension of Housing Loans in Specific Areas in June 2010. The key points of the Regulations included: (1) capping the LTV ratio on second (or more) housing loans for home purchases in specific areas at 70%; and (2) removing the grace period for such loans (Table B4.1).

Table B4.1 Regulations Governing the Extension of Housing Loans in Specific Areas by Financial Institutions

Scope	1. Financial Institutions referred to in the Regulations include domestic banks, local branches of foreign banks, credit cooperatives, Agricultural Bank of Taiwan, credit departments of farmers' and fishermen's associations, Chunghwa Post Co., and insurance companies. 2. The scope of "Specific Areas" prescribed in the Regulations includes Taipei City and ten districts in New Taipei City. 3. The "new housing loans" granted by financial institutions in the aforementioned areas.
New housing loans	Financial institutions shall, before extending new housing loans to individual borrowers against collateral located in specific areas, verify the borrowers' credit history related to housing loans with the Joint Credit Information Center. With regard to housing loans newly extended to borrowers who have other outstanding housing loans, financial institutions shall: 1. Limit new housing loans to no more than 70% of the appraisal value of the collateral; 2. Remove grace periods; and 3. Grant no additional loans against the same collateral for home refurbishments, as working capital, or for other purposes.
Effective date	The Regulations shall enter into force on 25 June 2010. Loans already approved by financial institutions on or before the cutoff date, may be disbursed in accordance with the original terms and conditions granted when the loans were approved.

Source: CBC.

3. Ongoing moral suasion and improvement in the collection of information regarding land collateralized loans in the second half of 2010

In addition to ongoing moral suasion, the CBC further enhanced the collection and analysis of land collateralized loans following the promulgation of the aforementioned regulations governing housing loans in specific areas. These measures included:

- Reminding financial institutions to be alert to activities stemming from massive purchases of existing houses by speculators who may take advantage of fake applicants to apply for housing loans, while urging financial institutions to curb such new loans in the hope of promoting effective risk management (July 2010);

- Using moral suasion to encourage banks to draw up appropriate criteria for land collateralized loans aimed at reinforcing risk management associated with land acquisition financing, whereby banks shall: (1) require borrowers to offer elaborate and concrete plans of construction projects; (2) set up reasonable LTV ratios and interest rates; and (3) adopt a package of measures (for example, withdrawal of loans or raising interest rates) to discipline borrowers who fail to commence construction on schedule (September 2010).
- Requiring banks to submit monthly call reports regarding the extension of newly approved land collateralized loans, so as to monitor the relevant credit extension of individual banks (October 2010).

4. The amendment of regulations to govern real estate loans granted by financial institutions (December 2010)

The CBC's policy measures to govern housing loans in specific areas showed promising results during the third quarter of 2010. Nonetheless, buoyant property transactions since October of that year have led to concerns about the increasing credit extension of banks' housing loans in other unregulated regions neighboring the specific areas. With regard to the enhancement of risk management for land collateralized loans granted by banks, there were mounting problems that mortgage risk management would be inconsistent between public banks and private banks in terms of various loan standards. As a result, the CBC Board approved the amendment of the Regulations Governing the Extension of Land Collateralized Loans and Housing Loans in Specific Areas in December 2010 (Table B4.2). This measure aimed primarily at dampening speculative activities in the property market fueled by bank credit, while urging financial institutions to reinforce their credit risk management so as to protect the interests of depositors and promote financial stability. The key points of the amendment are shown as follows:

- For housing loans in specific areas, the efforts included: (1) extending the coverage of specific areas; (2) lowering the maximum LTV ratio for second (or more) housing loans by individuals to 60%; and (3) encompassing housing loans by companies in specific areas to be subject to the applicable regulations.
- As for land collateralized loans, it tightened underwriting standards for real estate loans collateralized by residential or commercial land plots located in urban planning

districts. Financial institutions shall: (1) require borrowers to present concrete plans of construction projects; and (2) cap the LTV ratio at 65%, where 10% of the approved loan amount shall not be disbursed until the construction commences.

Moreover, in order to help financial institutions and the public understand more details about the foregoing regulations, further explanations and Q & A were provided on the CBC's website in January 2011.

Table B4.2 Regulations Governing the Extension of Land Collateralized Loans and Housing Loans in Specific Areas by Financial Institutions

Scope	1. Financial Institutions referred to in the Regulations include domestic banks, local branches of foreign banks, credit cooperatives, Agricultural Bank of Taiwan, credit departments of farmers' and fishermen's associations, Chunghwa Post Co., and insurance companies. 2. In addition to Taipei City and ten districts in New Taipei City, the scope of "Specific Areas" prescribed in the Regulations is amended to also include three other New Taipei City districts. 3. Pursuant to these amendments, land collateralized loans shall be governed by the Regulations.
Housing loans in Specific Areas	1. The loan-to-value ratio will be capped at 60%, down from 70%, for home purchases in specific areas by individuals who have taken out other outstanding real estate loans. Financial institutions shall, before extending new housing loans to individual borrowers against collateral located in specific areas, verify the borrowers' credit history related to housing loans with the Joint Credit Information Center. With regard to housing loans newly extended to borrowers who have other outstanding loans for real estate purchases, financial institutions shall: (1) Limit new housing loans to no more than 60% of the appraisal value of the collateral; (2) Remove grace periods; and (3) Grant no additional loans against the same collateral for home refurbishments, as working capital, or for other purposes. 2. Housing loans extended to companies shall be governed by the Regulations and shall conform to relevant rules in the sub-paragraphs (1) to (3) prescribed above.
Land collateralized loans	When extending collateralized loans against collateral of residential or commercial land plots located in urban planning districts (including but not limited to aforementioned specific areas), financial institutions shall: 1. Require borrowers to present concrete plans of construction projects; 2. Apply a maximum LTV ratio of 65% of the acquisition cost or the valuation price of the collateral, whichever is lower, where 10% of the approved loan amount shall not be disbursed until the construction commences; extend no additional credit for working capital or other purposes; and 3.Bills finance companies shall comply with the rules in the above two paragraphs when providing guarantees to bill issuance against collateralized residential or commercial land plots located in urban planning districts.
Effective date	The Regulations shall enter into force on 31 December 2010. Loans already approved by financial institutions before the cutoff date may be disbursed in accordance with the original terms and conditions granted when the loans were approved.

Source: CBC.

5. Ongoing target examinations to ensure the compliance of policies by financial institutions

To carry out the targeted macroprudential measures and contain the concentration of credit risks in financial institutions, the CBC will continuously analyze financial institutions' regular call reports and conduct target examinations for certain financial institutions where necessary.