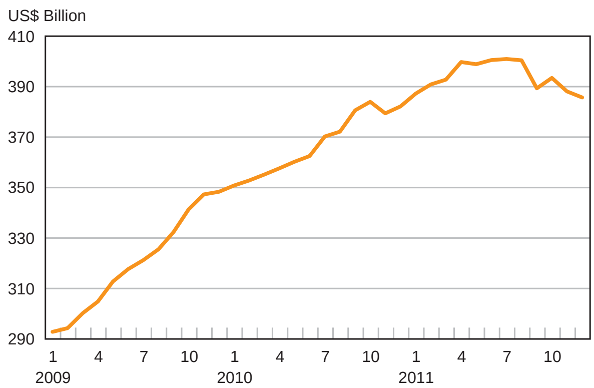
3. Foreign Exchange Management

For the year 2011, the Bank followed the established managed float regime to maintain an orderly foreign exchange market. Sufficient seed funds were provided by the Bank for foreign currency swaps and call loans. The Bank's foreign exchange reserves increased by US$3.5 billion due to a higher return on investment. The Bank also loosened regulations regarding foreign exchange remittances. Moreover, the FSC and the Bank jointly issued provisions for Taiwanese banks to manage renminbi business.

Foreign Exchange Market Management

Taiwan's exchange rate is in principle guided by market mechanism, the Bank only steps in when there is excessive exchange rate volatility, and a managed float regime is adopted.

Foreign Exchange Reserves



Source: Department of Foreign Exchange, CBC.

In 2011, the Bank continued to implement the Real-Time Reporting System for Large-Amount Foreign Exchange Transactions to keep the market in order. Moreover, monitoring efforts were reinforced to insure that forward transactions were based only on actual transactions. The Bank also urged authorized banks to enhance their exchange rate risk management. In addition, the Bank strengthened target examinations related to foreign exchange activities.

Management of Foreign Currency Call-Loan and Foreign Exchange Swap 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 seed funds[1] for the Taipei Foreign Currency Call-loan Market.

Furthermore, the Bank continued to carry out foreign currency swap transactions with banks and extended foreign currency call loans to banks so as to facilitate smooth corporate financing. During 2011, the volume of foreign exchange call-loan transactions reached US$1,856.2 billion, while that of foreign currency-NT dollar swap transactions reached US$ 968.0 billion.

---

[1] The seed funds include US$20 billion, €1 billion and ¥ 80 billion.

Foreign Exchange Reserve Management

In 2011, the Bank's foreign exchange revenues amounted to US$1,088.6 billion, while foreign exchange expenditures were US$1,085.1 billion. At the end of 2011, total foreign exchange reserves stood at US$385.5 billion, a US$3.5 billion gain from the end of 2010. The increase was mainly attributable to a higher return on investment from foreign exchange reserves.

Capital Flow Management

The Bank's foreign exchange management mainly relies on the market mechanism, and capital can flow freely in and out of Taiwan. As of 2011, foreign currency capital not involving NT dollar conversion can flow freely; there is also no restriction on financial flows involving NT dollar conversion for commodity and service trade, as well as direct and securities investments approved by the authorities. However, regulation exists for short-term remittances: annual remittances for an individual resident within 5 million USD, a juridical person within 50 million USD and a nonresident within 0.1 million USD can be settled by banks directly; annual remittances above these amounts require the approval of the Bank. Key measures with regard to the management of foreign exchange in 2011 included:

(1) In order to promote the internationalization of Taiwan's capital market, the Bank agreed to the following in 2011:

(i) the issuance of overseas depository receipts by 3 corporations with a total of US$1.1 billion, the issuance of European Convertible Bonds by 14 corporations with a total of US$3.1 billion and the issuance of European Exchangeable Bonds by 1 corporation with a total of US$0.1 billion;

(ii) 30 foreign corporations may raise funds from Taiwan's stock markets via TWSE listing or GTSM listing, with the total amount reaching NT$13.4 billion;

(iii) the issuance of Taiwan Depository Receipts (TDRs) by 19 foreign corporations, with the total amount reaching NT$18.8 billion.

(2) The Bank agreed to an increase in residents' investments in foreign securities as follows:

(i) domestic securities investment trust companies were allowed to raise public funds via 48 securities investment trust funds domestically to invest in foreign securities with a total of NT $558 billion raised;

(ii) domestic securities investment trust companies were allowed to raise 3 private trust funds domestically to invest in foreign securities with a total of NT$9 billion raised;

(iii) life insurance companies were given consent to invest in foreign securities with the amount totaling US$4.6 billion through non-discretionary money trusts managed by financial institutions, while their insurance products-related foreign securities investment interests can be hedged by selling forward exchange contracts totaling US$2.0 billion;

(iv) four major government pension funds, including Labor Pension Funds, invested in foreign securities with the total amount reaching US$5.1 billion.

(3) The Bank loosened the following regulations regarding foreign exchange remittances. The amended *Points to Be Noted for Banks to Guide Customers to Declare Foreign Exchange Receipts and Disbursements or Transactions* went into force on August 25, with the following key points:

(i) to simplify banking reports to the Bank, the verifying documents will be preserved by banks, without the need to send a photocopy to the Bank;

(ii) according to various market-opening measures adopted by the FSC, points to be noted were added for banks to take the following declaration of remittances and settlements:

① the securities investment remittances to Mainland China by investment trust companies and investment consulting companies as qualified institutional investors (QFIIs) for Mainland China;
② foreign currency-denominated international debt repayment remittances underwritten by securities firms;
③ the purchase or buyback remittances of offshore Exchange Traded Funds either entrusted or undertaken by securities firms;

(iii) the practice where the Bank would issue official letters to banks to require confirmation documents for the following remittances and settlements was also incorporated in the amended Points:

① remittance outflows and inflows to Mainland China;
② wage remittance declaration by private employment service organizations acting on behalf of foreign laborers.

Management of the Foreign Exchange Business of Financial Institutions

(1) At the end of 2011, there were 2,342 authorized foreign exchange banks in total, which included 38 head offices and 2,232 branches of domestic banks, 72 branches of 28 foreign banks, as well as 2,003 authorized money exchangers, postal offices and financial institutions authorized to engage in basic foreign exchange business. In 2011, the Bank approved the issuance of 16 new foreign exchange derivative products. To maintain the stability of bank management, on

March 14 the Bank revised the regulations for authorized banks to apply to conduct Credit Default Swap and Credit Default Option business.

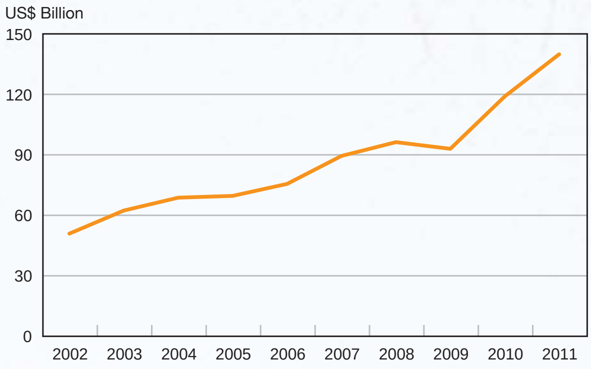
(2) In response to the needs of Mainland Chinese tourist consumption in Taiwan and Taiwanese tourist consumption in Mainland China, renminbi cash has been allowed to be exchanged in Taiwan since June 30, 2008. Along with the gradual opening of cross-strait activities, plus the opening of Mainland Chinese free and independent travel in June 2011, banks' exchange of renminbi cash apparently increased. Between June 30, 2008, and the end of 2011, the government approved 224 financial institutions (with a total of 3,704 branches) and 209 authorized money exchangers to conduct RMB cash exchange business. The total amount of renminbi purchased was RMB17.26 billion, while the total sale was RMB19.57 billion.

(3) Up to the end of 2011, 19 insurance companies were allowed to engage in foreign currency investment-linked insurance business, and 19 insurance companies were permitted to conduct business in relation to traditional foreign currency insurance products.

(4) Up to the end of 2011, the Bank allowed one securities firm to be an agent for foreign bond trading, two securities firms to be entrusted as agents for foreign securities trading, three securities firms for making outright purchases and sales of foreign securities not belonging to investment with their own funds or for hedging needs, two securities firms to manage warrants linked to foreign securities or indexes, five securities firms to conduct wealth management business, eight securities firms to manage onshore foreign currency bills. The Bank also permitted three investment trust or investment consulting firms to conduct foreign currency discretionary investments in foreign securities, four administration agencies to raise offshore private trust funds, one securities firm to raise domestic mutual funds or private foreign currency funds.

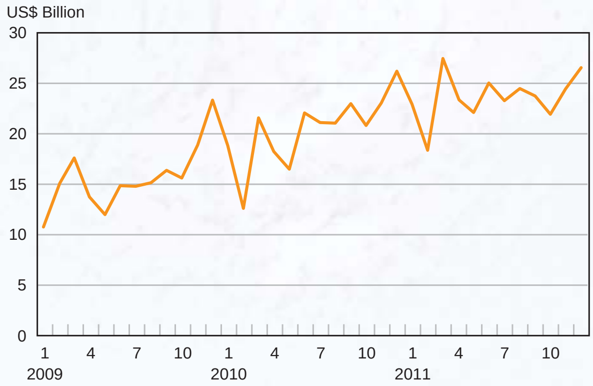
(5) In order to meet the need for cross-border renminbi settlement of overseas Taiwanese businessmen, on July 21, 2011, the FSC and the Bank jointly promulgated *Directions for Banks in Taiwan Area Conducting Renminbi (RMB) Business*, opening the channel for banks' OBUs and overseas branches to apply for renminbi business. Along with the expansion of OBU business, its asset scale also continued to grow. Up to the end of 2011, total OBU assets amounted to US$145.1 billion, an increase of 18% from the previous year. As for remittances, since June 2001, OBUs have been approved to conduct cross-Strait remittances. Steady growth has gradually turned OBUs into funding centers for overseas Taiwanese business. In 2011, cross-Strait remittances increased from US$243.3 billion in the previous year to US$282.8 billion, an increase of 16.2 percent.

OBU Assets



Source: Department of Foreign Exchange, CBC.

Cross-Strait Remittances through OBUs



Source: Department of Foreign Exchange, CBC.