

2. Monetary Aggregates

The Bank has selected the monetary aggregate M2 as the intermediate target since 1992. For the year 2012, M2 recorded an annual growth rate of 4.17 percent, lower than the previous year's 5.83 percent but still within the Bank's target range of 2.5 percent to 6.5 percent. Compared with the 1.26 percent GDP growth, the money growth indicated there was sufficient liquidity to support economic activity.

The annual growth rate of the narrow monetary aggregate M1B decelerated to 3.45 percent in 2012 from the previous year's 7.16 percent. The decline mainly resulted from a shift of funds from transaction deposits to non-transaction deposits and foreign currency deposits, and the shrinking trading volume in the stock market during the year.

Moderate Growth of Reserve Money

For the year 2012, reserve money grew at a slower pace, with the average annual growth rate falling from the previous year's 7.24 percent to 4.91 percent. As for the components of reserve money, bank reserves grew slower at 2.19 percent when compared with the previous year's 5.46 percent, while the growth of currency held by the non-bank public decreased to 8.74 percent from 9.84 percent one year earlier.

In terms of the monthly movements of reserve money, as the Chinese New Year holidays fell on different months in 2012 and 2011, the annual growth rates of reserve money for January and February were more volatile, which combined to average 5.63 percent. In subsequent months, the annual growth rates generally trended down and reached an all-year low of 4.14 percent in September. With the economic recovery and a lower base effect, the annual growth rates of reserve money turned upwards from October onwards.

On the demand side, currency held by the non-bank public grew moderately because the low interest rates paid on bank deposits enhanced the willingness to hold currency in hand. For banks, slower expansion of loans and the shift of money from transaction deposits to non-transaction deposits and foreign currency deposits both reduced banks' demand for reserves (time deposits are subject to a lower

Annual Growth Rate of Reserve Money



Source: Financial Statistics Monthly, CBC.

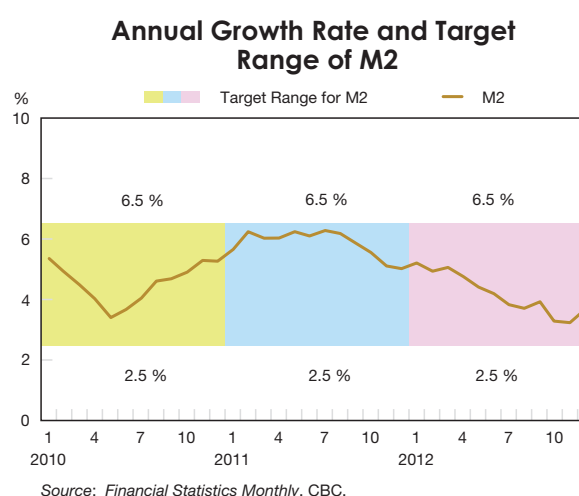
required reserve ratio, whereas there is no NT dollar reserve requirement on foreign currency deposits).

From the supply side perspective, the balance sheet of the Bank revealed the sources of changes in reserve money. The increase mostly resulted from the increase in foreign assets and the decrease in the issuance of certificates of deposit (CDs), while the decrease was mainly attributable to the decrease in claims on financial institutions.

Tepid Growth of M2

The monetary aggregate M2 is comprised of currency in circulation, deposits in banks' checking and passbook accounts, and quasi-money. The annual growth rate of M2 in 2012 was 4.17 percent, 1.66 percentage points down from the previous year's figure and slightly lower than the median of the Bank's target range.

The monthly movements of the M2 annual growth rate in 2012 were all within the Bank's target range and generally exhibited a downward trend. In January, M2 growth reached its all-year high of 5.22 percent because of the Chinese New Year factor and net foreign capital inflows. For the rest of the year, slower growth in bank loans and investments and re-allocation of funds towards non-deposit products such as insurance and mutual funds brought down the pace of monthly M2 growth. The M2 growth rate hit a yearly low of 3.26 percent in November.



Decline in M1B Growth

In the first three quarters of 2012, the stock trading volume declined and money shifted from transaction deposits to non-transaction deposits and foreign currency deposits owing to the global economic slowdown and the concern about the reintroduction of a capital gains tax. As a result, the M1B growth rates were driven down. In the fourth quarter, the trend reversed up as the economy mildly recovered. The average annual growth rate of M1B recorded 3.45 percent in 2012, 3.71 percentage points down from the previous year.

As for the monthly movements of M1B, the growth rates were greatly affected by the Chinese New Year factor in the first two months of the year. The annual growth rate of M1B rose to 3.47 percent in March because of a rally in the stock market. The M1B growth rate further went up to

3.77 percent in April. Between May and August, the M1B growth rate trended down owing to shrinking transactions in the stock market, the prolonged European debt crisis and the issue of the capital gains tax. The M1B growth rate hit a yearly low of 2.73 percent in August. From September onwards, the M1B growth rate trended up because of a rally in the stock market and net foreign capital inflows. The M1B growth rate reached a yearly high of 4.91 percent in December.

