



Annex

IV. Annex

Cross-Strait Currency Clearing Mechanism

The volume of trade in goods and services across the Taiwan Strait is quite substantial. Since this trade is not always in balance, there are bound to be gaps in the demand and supply of the NT dollar (NTD) or the renminbi (RMB) if the transactions are settled in either of the two currencies. As neither the NT dollar nor the renminbi is an international reserve currency, it is necessary to establish a currency clearing mechanism in order to convert the surplus NT dollars or renminbi into international reserve currencies.

In an effort to further promote bilateral trade and finance, the two respective central banks across the Taiwan Strait signed the *Memorandum on Cross-Strait Currency Clearing Cooperation* (hereafter in the Annex the “*Memorandum*”) on August 31, 2012. On this foundation, a mechanism was inaugurated for currency clearing and settlement between the NT dollar and the renminbi.

1. Cross-Strait Currency Cooperation Before the Memorandum

(1) Currencies Exchange

Prior to the inking of the Memorandum, currency exchange between Taiwan and Mainland China was limited to that of cash notes. The Bank of China in the mainland area first accepted NT dollar notes in several designated branches in 1988 and then offered NT dollar notes in 2004. On the other hand, Taiwan's renminbi exchange services were launched in Kinmen and Matsu islands in 2005 on a trial basis. Furthermore, to meet the needs of tourists from both sides and to prevent the unlawful circulation of renminbi in Taiwan, the Bank authorized financial institutions in Taiwan to exchange renminbi banknotes in 2008.

(2) Direct Supply of RMB Banknotes

Financial institutions in Taiwan used to be able to purchase renminbi banknotes only from HSBC Hong Kong or the Bank of America. As those two institutions sourced their renminbi banknotes from offshore markets, the banknotes were often in poor condition and more costly to procure while the supply was erratic.

After several rounds of negotiations, the Bank and the People's Bank of China (PBC) reached an agreement for the Bank of Taiwan and Mega International Commercial Bank to procure renminbi banknotes from Bank of China (Hong Kong) directly. Through this channel, brand-new renminbi banknotes have been supplied to financial institutions throughout Taiwan at a lower cost than before since October 26, 2010.

(3) RMB Business at Hong Kong Branches of Taiwanese Banks

Under the prerequisite for conducting renminbi business, 19 Hong Kong branches of 17 Taiwanese banks signed the renminbi clearing and settlement agreement with Bank of China (Hong Kong) on September 24, 2009. As of February 1, 2013, 18 Hong Kong branches of Taiwanese banks conducting renminbi business have taken a total of RMB15 billion deposits.

(4) Offshore Banking Units (OBUs) and Overseas Branches Approved for Renminbi Business

To facilitate the settlement of cross-border trade for Taiwanese companies, the Bank authorized the OBUs and overseas branches of Taiwanese banks to conduct renminbi business on July 21, 2011. As of January 31, 2013, 51 OBUs in Taiwan conducted renminbi business with deposits totaling RMB26.9 billion.

2. Establishing a Cross-Strait Currency Clearing Mechanism

The Bank started to discuss the currency clearing mechanism with the PBC in October 2010. After several rounds of negotiations, the aforementioned Memorandum was signed on August 31, 2012, with the following key elements:

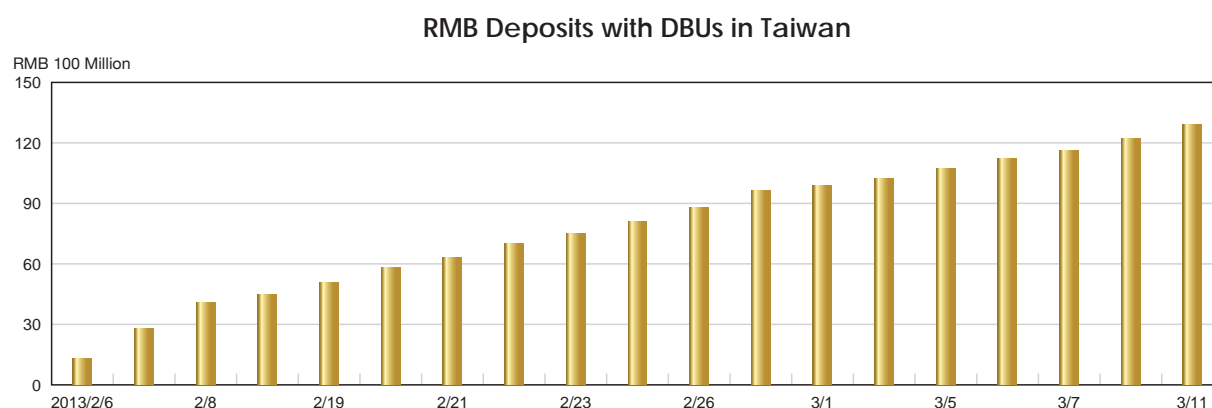
- (1) Based on the framework established in the Memorandum, the two central banks would separately designate one currency clearing institution to provide clearing and settlement services.
- (2) The Bank and the PBC agreed to coordinate the supervision of the two designated currency clearing institutions, including information sharing, protection of confidentiality, business examination, crisis management, and means of communication.

A chronology of events that mark the development of the clearing mechanism are as follows.

RMB Business in Taiwan

Date	Event
Dec. 11, 2012	The PBC designated the Taipei Branch of the Bank of China as the renminbi clearing bank in Taiwan.
Jan. 25, 2013	The PBC and the Taipei Branch of the Bank of China signed the renminbi clearing agreement.
Jan. 28, 2013	The Bank consented to the designation of the Taipei Branch of the Bank of China as the renminbi clearing bank in Taiwan.
Jan. 30, 2013	The Bank and the Taipei Branch of the Bank of China co-hosted a seminar on the regulations governing renminbi business and the clearing of renminbi.
Feb. 6, 2013	Authorized foreign exchange banks in Taiwan officially launched renminbi business.
Feb. 8, 2013	The Bank approved Chinatrust Commercial Bank to issue renminbi bonds in Taiwan.
Mar. 9, 2013	The Bank approved Deutsch Bank to issue renminbi bonds in Taiwan.
Mar. 12, 2013	Chinatrust Commercial Bank began to sell renminbi bonds (three-year bonds of up to RMB1 billion at a coupon rate of 2.9 percent) in Taiwan.

As of March 11, 2013, 53 authorized foreign exchange banks in Taiwan (a.k.a. domestic banking units, DBUs) had commenced renminbi business, taking in deposits totaling RMB12.92 billion and processing 4,181 remittances worth RMB1.87 billion. The single-day amount of cross-border renminbi settlement in Taiwan was RMB2.14 billion on March 11, 2013.



NTD Business in the Mainland Area

Date	Event
Sep. 17, 2012	The Shanghai Branch of the Bank of Taiwan was selected as the NT dollar clearing bank in the mainland area by the Bank.
Jan. 4, 2013	The Bank approved the designation of the Shanghai Branch of the Bank of Taiwan as the NT dollar clearing bank in the mainland area.
Jan. 9, 2013	The Bank gave consent to the customs authority for the export and import of NT dollar banknotes.
Feb. 4, 2013	China's State Administration of Foreign Exchange granted the customs authority permission for the import and export of NT dollar banknotes.
Apr. 2, 2013	The Shanghai Branch of the Bank of Taiwan commenced the business of exchanging NT dollar banknotes.

3. Benefits of the Mechanism for Cross-Strait Currency Clearing

- (1) The newly-established mechanism will remove the barrier of settling cross-strait trade and investment in the respective local currencies. It helps reduce transaction and settlement costs and mitigate exchange rate risks associated with remittances, trade, and investment for either households or the corporate sector. Companies may open accounts, make deposits, take loans, make remittances, and engage in trade and investment in renminbi. With the increased number of currencies to be used for cross-strait transactions, the mechanism will also make funding more flexible for companies.

- (2) The mechanism is consistent with the government's "Program to Develop Financial Services with Cross-Strait Characteristics." It will also meet growing demand from the wealth management business, facilitating the launch of renminbi business at local financial institutions, issuance of RMB-denominated bonds in Taiwan, availability of other renminbi financial products, etc.
- (3) The mechanism will bolster Taiwan's efforts to thrive as an offshore renminbi financial center. For instance, a greater demand for funds to support the enormous trade volume across the Taiwan Strait may be met with renminbi debt financing. Renminbi corporate bonds issued on the Taiwan market not only lower the funding cost for companies but also give investors a greater variety of product choices. In addition, Taiwan's financial institutions may offer renminbi derivatives to help companies hedge against exchange rate or interest rate risks. By allowing foreign financial institutions to participate in the local renminbi clearing system, Taiwan is in a good position to become an offshore hub for renminbi business.

4. Conclusion

Taiwan has a conducive environment and great advantages for becoming an offshore renminbi market but still needs to reinforce its effort with more renminbi financial products and a better mechanism to recycle renminbi back to Mainland China. Moreover, the Bank has started to discuss with the PBC the establishment of a reciprocal RMB/NTD currency swap arrangement in order to maintain renminbi liquidity in Taiwan's financial markets.