

## II. Financial Developments

### 1. Overview

In 2013, in view of global uncertainties, moderate domestic growth and mild inflationary pressures, the CBC maintained a moderately accommodative policy stance and kept the policy rates unchanged to ensure price and financial stability. Interest rates on deposits and loans also stayed at stable levels. The money market rate exhibited a downward trend owing to ample liquidity, whereas bond yields, affected by the anticipation of US Fed's decision to reduce the pace of its asset purchases (quantitative easing, or QE), exhibited an upward trend. Owing to a gradual recovery in the domestic economy, growth in loans and investments of monetary financial institutions picked up. This, combined with net foreign capital inflows, boosted the growth in M2. With respect to the exchange rate, the NT dollar against the US dollar depreciated, reflecting the influence of the Fed's asset purchase decision. In the stock market, supported by purchases by foreign investors and government measures, market indices swung higher.

#### **Growth in Monetary Aggregates Rose**

The annual growth rate of reserve money rose dramatically in 2013, mainly because stock market rallies induced by net foreign capital inflows boosted demand deposit growth. In addition, the uptrend in growth in currency issued also led to an increase in the growth rate of reserve money. The monetary aggregate M2, measured on a daily average basis, recorded a yearly growth rate of 4.78 percent in 2013, rising from 4.17 percent in 2012, and was still within the CBC's 2.5 percent to 6.5 percent target range for the year. The annual growth rate of M1B, measured on a daily average basis, accelerated to 7.27 percent in 2013 from 3.45 percent in 2012.

#### **Average Growth in Bank Loans and Investments Increased**

Compared with the end of 2012, the annual growth rate of loans and investments decreased from 5.69 percent to 4.59 percent at the end of 2013. The decrease was mainly because of an investment slowdown under banks' more conservative investment strategies to cope with the effect of Fed's decision to "taper off" its asset purchase program. On the other hand, growth in bank loans accelerated, mainly owing to individuals' growing demand for funds boosted by higher trading activities in the stock market and the real estate market. For the year as a whole, the average annual growth rate of loans and investments of monetary financial institutions increased from 5.08 percent in 2012 to 5.60 percent in 2013. If the loans and investments of life insurance companies, non-accrual loans reclassified, and bad loans written off by monetary financial institutions, as well

as funds raised directly from capital markets, were all taken into account, the total funds raised by the non-financial sector would register an annual growth rate of 4.78 percent at the end of 2013, higher than the 4.55 percent recorded at the end of the previous year.

### **Non-performing Loan Ratio Continued to Improve**

The asset quality of Taiwan's banks remained sound, mainly owing to their limited exposure to highly uncertain global financial markets. The overall non-performing loan ratio of monetary financial institutions decreased from 0.45 percent at the end of 2012 to 0.41 percent at the end of 2013. However, because the capital increases conducted by some banks in 2013 have not been fully reflected in their profits yet, the average return on equity was 10.04 percent, decreasing from 10.06 percent the year before. The average return on assets was 0.58 percent in 2013, the same level as that in 2012.

### **Average Interest Rates on Deposits and Loans Decreased Modestly**

The CBC, in view of greater uncertainty surrounding the global economy and mild domestic inflation, has kept policy rates unchanged in 2013 to maintain price and economic stability. As a result, domestic banks kept their posted interest rates on deposits and loans at a steady level throughout 2013. The average fixed rate on one-year time deposits of the five major domestic banks stayed at the same level as that at the end of 2012, while the weighted average rate on their new loans increased slightly because of an upswing in rates on loans for working capital. The weighted average interest rate on deposits decreased slightly, mainly because net foreign capital inflows caused an increase in the weight of demand deposits. The weighted average interest rate on loans also decreased slightly, mainly because the rate on long-term secured loans edged down.

### **Money Market Rates Decreased Slightly; Bond Yields Rose**

The CBC has continued to manage market liquidity to maintain excess reserves of banks at an appropriate level. The interbank overnight call loan rate remained at a stable level in 2013. With regard to the bills market, easy funding conditions led the average rate to exhibit a downtrend, which in turn induced an increase in the issuance of commercial paper.

In 2013, the yield on the benchmark 10-year government bond, influenced by the anticipation that the Fed would reduce its asset purchases, recorded an uptrend. The rise in bond yields, likely to push up the funding cost of the national treasury, caused some government bond auctions to be cut off despite falling short of the issue targets. Therefore, the total amount of government bonds issued declined compared to the previous year. Corporate bond yields also exhibited an upward trend, denting corporate bond issues even for key issuers like Taiwan Power Company. The total issue amount of corporate bonds decreased as a result.

## Exchange Rate Depreciated

At the beginning of 2013, the NT dollar against the US dollar appreciated on net foreign capital inflows. The interbank closing exchange rate reached a yearly high of 29.039 on January 11. Afterwards, the NT dollar softened because the market expected that Asian currencies might begin competitive devaluations after the yen weakened further as a result of the BOJ's monetary stimulus expansion. After mid-May, market concerns over possible US QE withdrawal caused the US dollar to appreciate, and thus the NT dollar reached 30.350 on June 24, the lowest rate of 2013. From mid-September, the US dollar turned to depreciate, owing to the US Fed's announcement to maintain its asset purchasing policy. The NT dollar started to appreciate and reached 29.425 on October 23, the highest rate in nine months. In mid-December, after the US Fed announced it would gradually reduce the size of its QE, the US dollar rebounded and the NT dollar depreciated again. At the end of 2013, the NT dollar depreciated against the US dollar by 2.72 percent compared to the end of the previous year. On an annual average basis, the NT dollar depreciated by 0.52 percent in 2013.

## Stock Indices Edged Up

During the period from January to early March 2013, the domestic stock market's mainboard index, the TAIEX, gradually gained from its yearly low of 7,617 points on January 17, bolstered by the robust performance of international stock markets, as well as progress in cross-strait financial cooperation. Afterwards, the TAIEX took a dip because of heightened tension between North and South Korea and the outbreak of bird flu in China. From mid-April, as the US stock market continued to hit record highs, and the Ministry of Finance released a new version of tax regulations regarding capital gains on securities transactions, foreign investors crowded into the stock market and pushed up the TAIEX to 8,399 points on May 22. However, after the Fed's talk of QE tapering, the TAIEX fell again and reached 7,663 points on June 25. Then, as the Legislative Yuan passed the amended version of the capital gains tax, the US Fed announced that QE would continue, and the Financial Supervisory Commission adopted measures to revitalize the stock market, the TAIEX was boosted to hit its yearly high of 8,623 points on December 30. On a daily average basis, the TAIEX was 8,093 points in 2013, increasing by 8.2 percent from 7,481 points the previous year.