

## II. Financial Developments

### 1. Overview

In 2014, 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. Market interest rates on deposits and loans both stayed at stable levels. Most money market rates exhibited a downward trend owing to ample liquidity, whereas 10-year government bond yields, mainly affected by the US Fed's decision to withdraw from asset purchases, exhibited an upward trend on average. Amid a moderate recovery in the domestic economy, growth in loans of monetary financial institutions picked up, while growth in investments was subdued. 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 swung to depreciation, mainly because the Fed ended its asset purchase program and Asian currencies depreciated following the BoJ's additional easing. In the stock market, despite adverse factors including heightened international geopolitical tension and a series of domestic incidents including an aviation accident, gas explosions and food safety concerns, market indices swung higher, mainly driven by global economic recovery, better corporate profits, and strong buying by foreign investors.

#### **Growth in Monetary Aggregates Accelerated**

The monetary aggregate M2, measured on a daily average basis, recorded a yearly growth rate of 5.66 percent in 2014. This was higher than the 4.78 percent in 2013 and yet remained within the CBC's 2.5 to 6.5 percent target range for the year. The pickup was mainly a reflection of an increase in net foreign capital inflows. The annual growth rate of M1B, measured on a daily average basis, accelerated to 7.96 percent in 2014 from 7.27 percent in 2013. Meanwhile, the annual growth rate of reserve money decreased in 2014, mainly owing to slower growth in reserves deposited with the CBC as domestic funds moved towards foreign currency deposits.

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

The annual growth rate of loans and investments, compared with that at the end of 2013, increased from 4.59 percent to 5.20 percent at the end of 2014. The increase was due to expanded growth in bank loans, mainly driven by a growing demand for funds among the private sector and individuals amid an economic recovery and strong stock market activity. For the year as a whole, the average annual growth rate of loans and investments of monetary financial institutions dropped from 5.60 percent in 2013 to 4.96 percent in 2014. 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 4.13 percent at the end of 2014, lower than the 4.78 percent recorded at the end of the previous year.

### **Asset Quality of Monetary Institutions 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 dramatically from 0.41 percent at the end of 2013 to 0.27 percent at the end of 2014. Since the pre-tax profits of monetary financial institutions kept growing during the year, their average return on assets and return on equity were both higher than those of the previous year, rising respectively from 0.58 percent and 10.04 percent to 0.66 percent and 11.23 percent.

### **Average Rates on Deposits and Loans Decreased Slightly**

The CBC, in view of greater uncertainties surrounding the global economy and mild domestic inflation, kept policy rates unchanged in 2014 to sustain price and economic stability. As a result, domestic banks kept their posted interest rates on deposits and loans at steady levels throughout 2014. The average fixed rate on one-year time deposits of the five major domestic banks stayed generally at the same level as that in 2013, while the weighted average rate on their new loans decreased slightly because of a downswing in rates on loans for working capital and current operations.

The weighted average interest rates on deposits moved downward, mainly because transaction deposits made up a larger share in total deposits. Meanwhile, the weighted average interest rate on loans also declined slightly, mainly because of the increases in low-interest local government loans and syndicated loans.

### **Bills Market Rates Largely Declined; 10-Year Government Bond Yields Rose**

The CBC 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 2014. With regard to the bills market, easy funding conditions led money market rates to exhibit downtrends.

During the first few months of 2014, the yield on the benchmark 10-year government bond recorded a downtrend, mainly influenced by the Fed's gradual reduction of asset purchases and increased hedging demands for US bonds against geopolitical risks. The yield started to move upwards in June. However, by the end of October, as the Fed announced an end to asset purchases, coupled with monetary stimulus expansions in Europe and Japan and a plunge in international oil prices, the yield trended downwards again. For the year as a whole, the average yield rose as compared with that in the previous year. The rise in the bond yield, likely to push up the funding

cost of the national treasury, caused some government bond auctions to be cut off. However, the total amount of government bonds issued increased compared to the previous year.

### **Exchange Rate Depreciated**

At the beginning of 2014, the NT dollar depreciated against the US dollar, mainly influenced by better employment figures in the US and the Fed's tapering of bond purchases. The NT dollar reached a new low against the US dollar on March 21. Afterwards, the NT dollar appreciated because of continuous net foreign capital inflows and reached a yearly high on July 2. From October, the Fed concluded its asset purchase program, and Asian currencies softened as the yen weakened further following Japan's monetary stimulus expansion. These, combined with a steady economic recovery in the US and dramatic oil price falls, brought the NT dollar to depreciate again and hit a yearly low on December 24. At the end of 2014, the NT dollar depreciated against the US dollar by 5.57 percent compared to that at the end of the previous year. On an annual average basis, the NT dollar depreciated by 1.97 percent in 2014.

### **Stock Index Climbed**

During early 2014, the domestic stock market's mainboard index, the TAIEX, extended gains following a rally at the end of the previous year, whereas it was brought down to a yearly low of 8,264 points on February 5, mainly affected by plunges across international stock markets. Afterwards, the TAIEX trended up to hit an all-year high at 9,569 on July 15, mainly driven by the global economic recovery, better corporate profits, and continued net purchases by foreign investors. In the following months, some negative factors, including heightened international geopolitical risks, a plane crash on Taiwan's offshore island of Penghu, gas blasts in Kaohsiung and domestic food safety concerns raised by the tainted oil scandal, brought the TAIEX to swing downwards. On a daily average basis, the TAIEX was 8,992 points in 2014, rising by 11.11 percent from 8,093 points in the previous year.