

2. Monetary Management

Keeping Policy Rates Unchanged to Maintain Price and Financial Stability

While the global economy was clouded by many uncertainties in 2018, the domestic economy experienced a moderate recovery. The output gap remained negative, and inflation expectations were mild. Meanwhile, domestic nominal and real interest rates registered around the middle range among major economies. Against this backdrop, the Bank kept policy rates unchanged throughout the course of the year so as to maintain price and financial stability and achieve sustained economic growth.

At the end of 2018, the discount rate, the rate on accommodations with collateral, and the rate on accommodations without collateral were kept unchanged at their current levels of 1.375%, 1.75%, and 3.625%, respectively.

Conducting Open Market Operations to Sustain Steady Monetary Growth

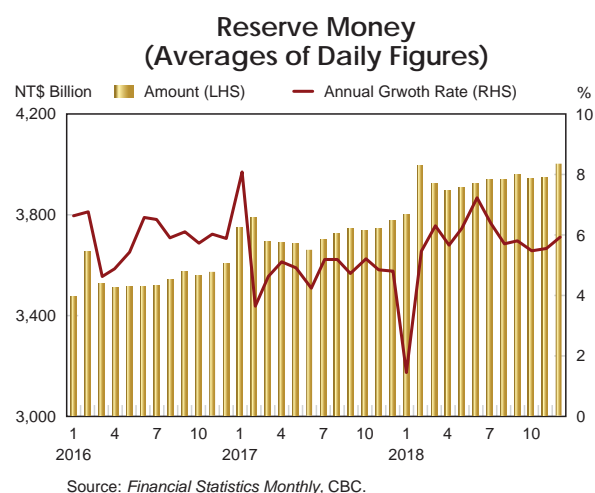
In 2018, the Bank managed market liquidity through open market operations by issuing certificates of deposit (CDs) in response to domestic economic conditions, which helped maintain reserve money, monetary aggregates and the overnight call loan rate at appropriate levels.

(1) Managing Market Liquidity

The Bank continued to conduct open market operations by issuing CDs. At the end of the year, the total outstanding amount of CDs issued by the Bank was NT\$7,817 billion.

(2) Higher Growth in Reserve Money

Reserve money grew at a moderate pace for the year of 2018, recording a growth rate of 5.61%, 0.57 percentage points higher than the previous year's figure. In terms of the monthly movements of reserve money, the annual growth rates of reserve money for January and February are often more volatile as the exact timing of the Lunar New Year holidays shifts on the Gregorian calendar each year. In 2018, reserve money posted an average annual growth rate of 3.50% during this period. Monthly figures of



annual reserve money growth remained relatively stable from March onwards and reached a yearly high of 7.25% in June and a yearly low of 5.51% in October.

On the demand side, reserve money, measured on a daily average basis, increased by NT\$209 billion over the previous year. Of the components, net currency increased by NT\$135 billion and the annual growth rate slightly increased to 7.60% from 7.00% the previous year; reserves held by financial institutions expanded by NT\$74 billion, with the annual growth rate increasing to 3.80% from 3.32% the previous year. 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. Meanwhile, the overall growth rate of banks' reserves increased compared to the previous year as higher growth in transaction deposits raised banks' demand for reserves.

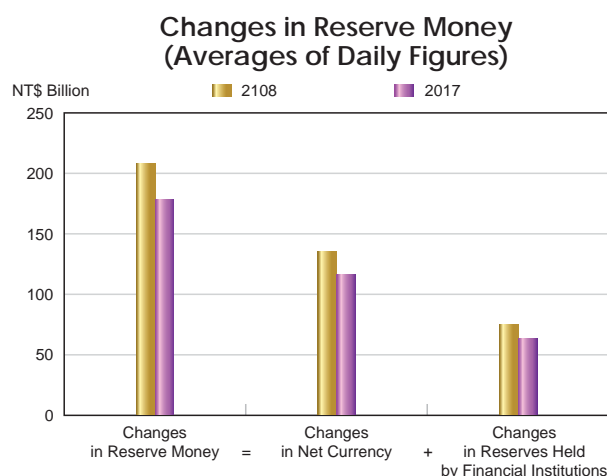
From the supply side perspective, reserve money increased by NT\$278 billion at the end of the year. The balance sheet of the Bank revealed the sources of changes in reserve money. The increase was mostly attributable to the growth in foreign assets held by the Bank and in claims on financial institutions, as well as the decrease in the issuance of CDs.

(3) Overnight Call Loan Rate Broadly Stable

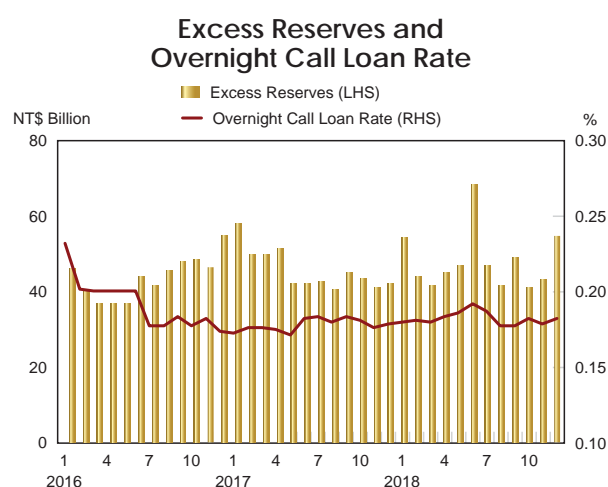
In 2018, the Bank continued to conduct open market operations to maintain excess reserves and the overnight call loan rate at appropriate levels. The annual average excess reserves of financial institutions reached NT\$48 billion, slightly higher than the NT\$46 billion of the previous year. The annual average overnight call loan rate remained broadly stable at around 0.180%.

(4) M2 Growth Slower but Within Target Range

The M2 growth target range for 2018 was set at 2.5% to 6.5%, same as the previous year. M2 recorded an annual growth rate of 3.52%, down by 0.23 percentage points from the previous year. The annual growth rates of M2 in every month of the year remained within the Bank's target range.



Source: *Financial Statistics Monthly*, CBC.



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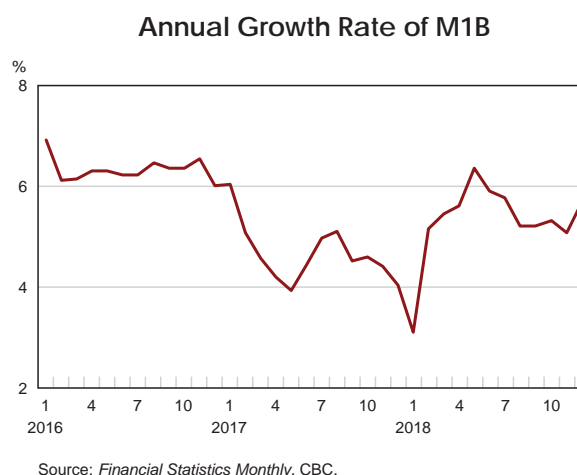
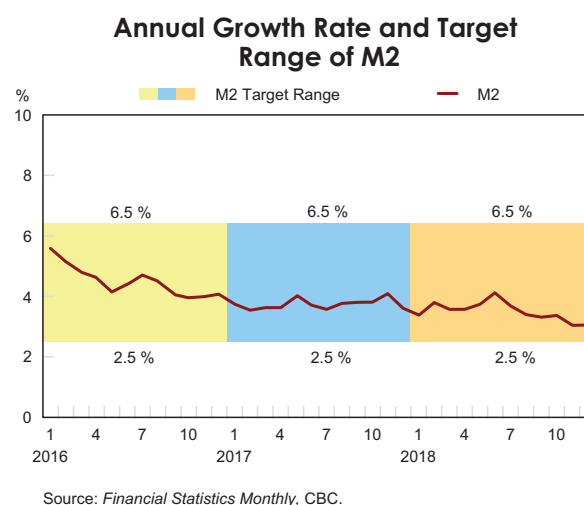
With regard to the monthly movements in 2018, the M2 growth rate trended upward for the first quarter, reflecting continuous growth in bank loans and investments, and reached 3.60% in March. Afterwards, despite net foreign capital outflows, stronger expansion in bank loans and investments lifted the pace of monthly M2 growth to its yearly high of 4.10% in June.

However, the M2 growth rate moved down to 3.68% in July, caused by slower growth in bank loans and investments and larger net foreign capital outflows. The M2 growth rate dropped further to 3.34% in September on account of softened growth in bank loans and investments and in foreign currency deposits. After slightly rising to 3.39% in October as growth in transaction deposits accelerated, the M2 growth rate declined in subsequent months and recorded an all-year low of 3.07% in December, dragged down by weaker growth in transaction deposits and net foreign capital outflows.

The monetary aggregate M1B rose at an annual rate of 5.32% in 2018 (on a daily average basis), 0.67 percentage points higher than the previous year's figure, primarily because of faster growth in transaction deposits.

As for the monthly movements of M1B, its annual growth rate reached a yearly low of 4.03% in January on account of diminished growth in bank loans and investments and a higher base effect with the Lunar New Year holidays falling in January in 2017. The M1B growth rate exhibited a steady uptrend from February to May owing to faster growth in transaction deposits and bank loans and investments and hit an all-year high of 6.35% in May.

From June onwards, the M1B growth rate moved downward as a result of softer growth in transaction deposits, slower expansion in bank loans and investments, and net foreign capital outflows. After ticking up in September and October, the M1B growth rate slid to 5.09% in November. Later, stronger growth in passbook savings deposits brought the M1B annual growth rate up to 5.69% in December.



Implementing the Net Stable Funding Ratio

To be in line with international standards and practices, the Financial Supervisory Commission (FSC) and the Bank jointly promulgated the net stable funding ratio (NSFR) regulations, effective from January 1, 2018. The introduction of the NSFR aims to strengthen the liquidity risk management of domestic banks. The NSFR is defined as the amount of available stable funding relative to the amount of required stable funding, and its statutory minimum standard is set at 100%. For the first three quarters of 2018, the NSFR of domestic banks averaged 133%, and all individual domestic banks' NSFRs met the minimum requirement during the period.

Continuing with Macroprudential Policy on High-Value Housing Loans

In 2018, housing prices fluctuated within a narrow range and home buyers remained cautious about the housing market outlook. However, given that largely volatile high-value housing prices could still raise banks' real estate-associated credit risks, the Bank kept the loan-to-value (LTV) ratio capped at 60% on high-value housing loans.

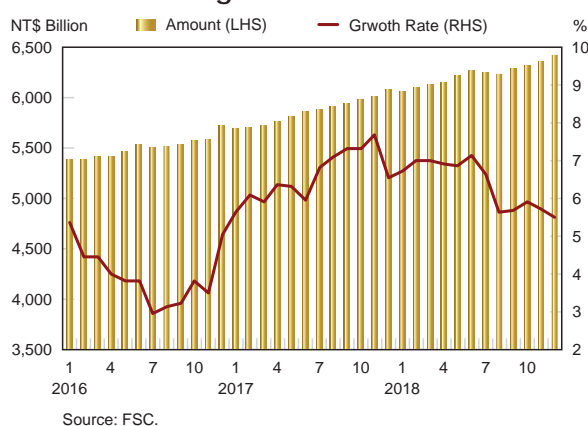
Looking ahead, the Bank will continue to keep a watchful eye on financial institutions' management of risks associated with real estate lending and developments in the housing market. Appropriate monetary policy actions will be adopted in a timely manner so as to ensure financial stability.

Facilitating SME Funding

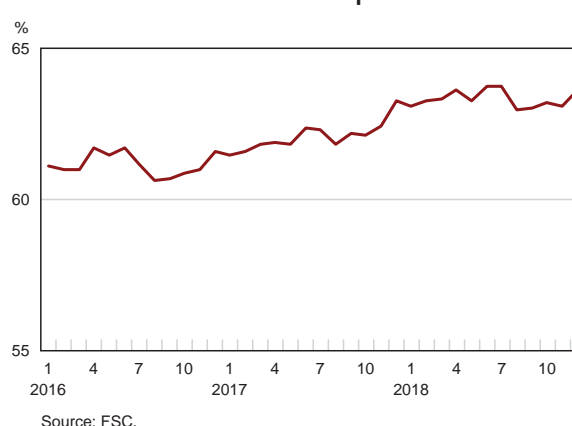
To sufficiently meet SMEs' funding needs, the FSC continued to encourage lending to SMEs by domestic banks, while the Bank also urged commercial banks to increase lending to SMEs.

At the end of 2018, the outstanding loans extended to SMEs by domestic banks amounted to

Outstanding Loans Extended to SMEs



Ratio of Outstanding Loans Extended to SMEs to Those Extended to Private Enterprises



NT\$6,438 billion, increasing by NT\$336 billion from the end of the previous year and far exceeding the annual target of increased lending of NT\$270 billion. Furthermore, the ratio of outstanding SME loans to those extended to private enterprises rose slightly from 63.28% at the end of 2017 to 63.63% at the end of 2018.

Accepting Redeposits from Financial Institutions

Accepting redeposits from Chunghwa Post, the Agricultural Bank of Taiwan and commercial banks is another instrument for the Bank to influence banks' reserve positions to promote financial stability. At the end of 2018, the outstanding redeposits of Chunghwa Post and the Agricultural Bank of Taiwan stayed broadly unchanged at NT\$1,624 billion and NT\$165 billion, respectively. Commercial banks' redeposits also remained unchanged at NT\$364 billion.