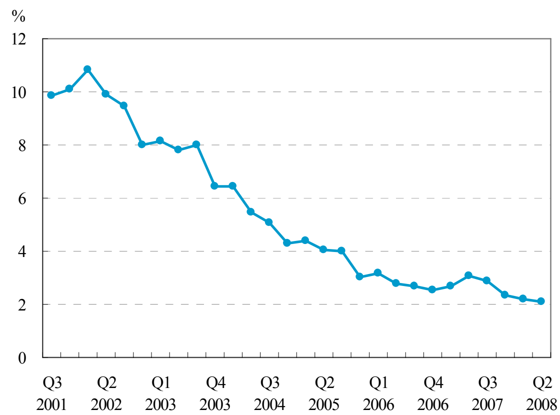
The credit quality of loans to the corporate sector remained satisfactory, but default risk rose

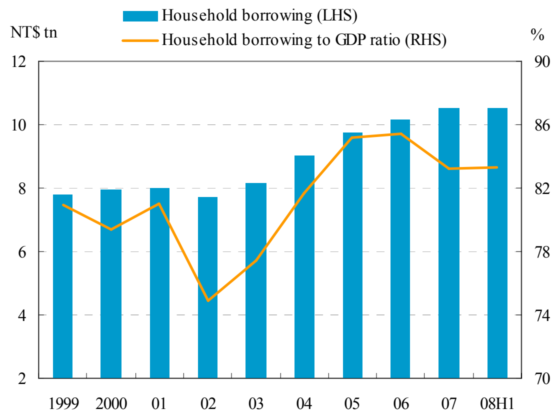
The non-performing ratio of loans to the corporate sector kept falling to 2.11% in June 2008 (Chart 6.6), demonstrating that its credit quality remained satisfactory. Thereafter, however, profitability of the corporate sector might be undermined by several adverse factors, including increasing downside risks to domestic economic growth, declining consumer expenditures due to inflation, and a heavy slump in stock market prices, as well as increasing commodity prices and rising operational costs in China. In addition, affected by the global credit crunch arising from the US subprime crisis, domestic financial institutions became more conservative in extending credit. Enterprises with an unsound financial structure, or SMEs with insufficient transparency in financial reporting might face the pressure of rising financing costs and increasing refinance difficulty, thus increasing their default risk.

Chart 6.6 NPL ratio of corporate loans



Note: End-of-period figures.
Source: JCIC.

Chart 7.1 Household borrowing to GDP



Note: Household borrowing data are end-of-period figures.
Sources: CBC, JCIC and DGBAS.

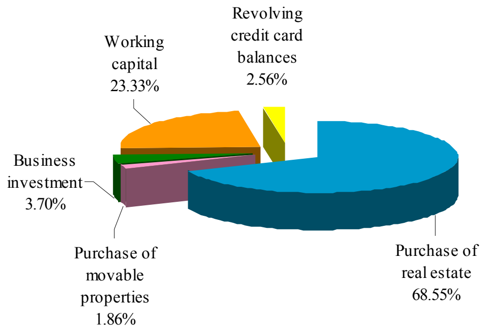
7. Household sector

For the household sector, prior to the end of June 2008, borrowing growth moderated and short-term debt servicing capacity strengthened, but debt burdens remained heavy. The credit quality of loans to households continued to be satisfactory. Thereafter, the assets and real income of households might be undermined as the global stock market slumped, domestic economic growth declined, and the unemployment rate rose. Furthermore, debt repayment pressures for borrowers increased as their interest-only periods of high loan-to-value mortgages successively expired. These joint developments could have adverse impacts on the credit quality of loans to households.

Growth in household borrowing decelerated

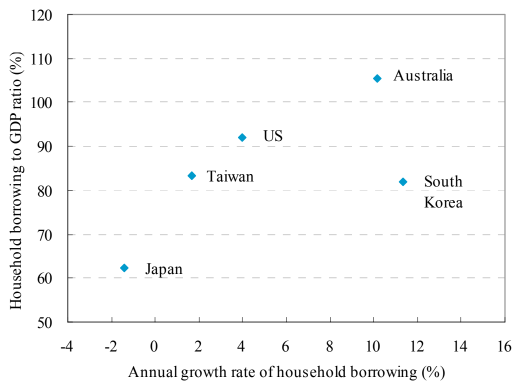
By the end of June 2008, total household borrowing[63] reached NT$10.55 trillion (Chart 7.1) on year-on-year growth of 1.65%, down from 11% in 2004 and lower than the 3.29% registered at the end of 2007. This was a result of the slowing growth in real estate loans due to the sluggish housing market. The single largest share of household borrowing went for the purchase of real estate (68.55%), followed by working capital loans[64] (23.33%), while revolving balances on credit cards accounted for only 2.56% (Chart 7.2). Compared to the end of 2007, all shares of loans declined, excluding loans for purchasing real estate, which continued to rise.

Chart 7.2 Household borrowing by purpose



Note: Figures are end-June 2008.
Sources: CBC and JCIC.

Chart 7.3 Household indebtedness in selected countries



Note: Figures are end-June 2008.
Sources: Fed, BEA, BOJ, Cabinet Office of Japan, BOK, ABS, IMF, DGBAS, CBC, and JCIC.

The ratio of household borrowing to GDP was 83.34% as of the end of June 2008, growing slightly by 0.10 percentage point in the first half of the year, mainly due to a much slower pace in GDP growth (Chart 7.1). Compared to other Asian countries, the US, and Australia, total household borrowing in Taiwan grew at a faster annual rate than in Japan, but much slower than in the US, Australia, and South Korea. As a percentage of GDP, household borrowing in Taiwan was lower than in the US and Australia, about the same as in South Korea, but higher than in Japan (Chart 7.3).

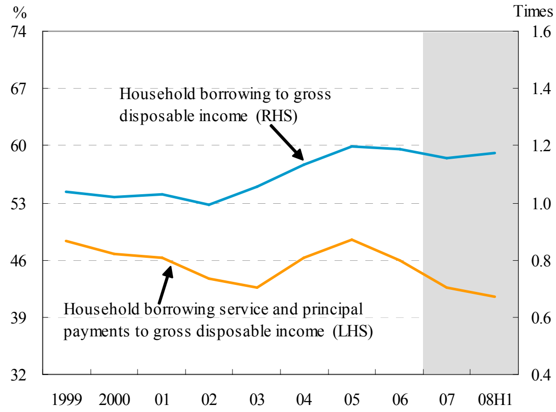
[63] The term "household borrowing" as used in this section refers to outstanding loans and revolving credit card balances taken out by households from the following financial institutions:
(1) Depository institutions: Domestic banks (including medium business banks), local branches of foreign banks, credit cooperatives, credit departments of farmers' associations, credit departments of fishermen's associations, and the Remittances & Savings Department of Chunghwa Post Co.
(2) Other financial institutions: Trust and investment companies, life insurance companies, securities finance companies, and securities firms.

[64] The term "working capital loans" includes outstanding cash card loans.

Household debt burden remained heavy

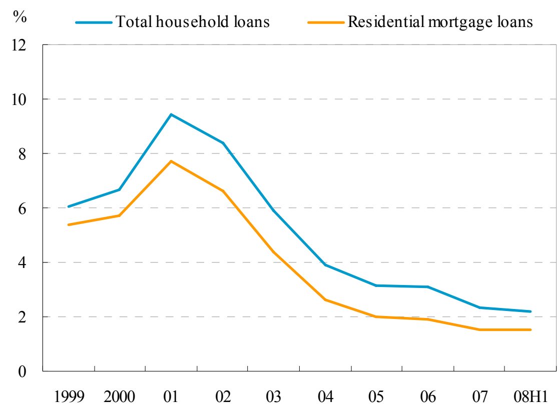
As of the end of June 2008, the ratio of household borrowing to gross disposable income[65] increased to 1.17 times, slightly higher than the 1.16 times seen at the end of 2007, reflecting the continued heavy household debt burden. Nevertheless, the household debt servicing ratio declined to 41.48% from 42.56% in 2007, the lowest since 1999. Although long-term real estate borrowing continued to grow, short-term household borrowing slowed and even contracted, alleviating the pressures from principal and interest payments in the near future. This indicated that household debt servicing capacity continued to improve gradually (Chart 7.4).

Chart 7.4 Household debt servicing ratio



Note: Gross disposable income in shadow area is CBC estimate.
Sources: CBC, JCIC and DGBAS.

Chart 7.5 NPL ratio of household loans



Note: End-of-period figures.
Source: JCIC.

The household NPL ratio[66] continued falling to 2.18% as of the end of June 2008, the lowest in nine years. This came about primarily because the non-performing ratio for residential mortgage loans, accounting for the largest share of loans to households, remained low (Chart 7.5). The credit quality of loans to households remained satisfactory. Thereafter, the slumping global stock market, slowing domestic economic growth, declining real income, and the rising unemployment rate might reduce household assets and real income. In addition, debt repayment pressure for borrowers strengthened as their interest-only periods of high loan-to-value mortgages successively expired. These joint developments may adversely impact the quality of loans to households.

[65] Gross disposable income = disposable income + rental expenses + interest expenses. Gross household disposable income in 2007 and the first half of 2008 were estimated using parameters based on DGBAS data for household disposable income and national disposable income and by carrying out "linear interpolation," which yielded better results through "trend detection" (e.g. performance under various interpolations, such as nearest, linear, spline, pchip, and cubic interpolation).

[66] Household NPL ratio excludes data from the Remittances & Savings Department of Chunghwa Post Co. and all securities firms.