

### III. Central Bank Operations

Pursuant to the Central Bank of China Act, the Bank has four operational objectives, namely, to promote financial stability, to guide sound banking operations, to maintain the stability of the internal and external value of the currency and, within the scope of the above-mentioned objectives, to foster economic development.

The Board of Directors, consisting of fifteen members, is the highest decision making body of the Bank and meets four times a year. Starting from the end of the year 2000, the Board decided to adopt a policy of monetary easing to add momentum to the recovery of the domestic economy. Under the precondition of price and financial stability, in order to stimulate the economy, the Bank cut the discount rate 14 times between December 2000 and the end of 2002. Moreover, to help boost the real estate market and traditional industries, during the year 2002 the Bank and the Ministry of Finance coordinated local banks to conduct the programs of preferential housing loans and preferential loans to traditional industries.

For the year 2002, although domestic demand remained weak, exports became the driving force behind the economic activity. The economic growth rate rose to 3.54 percent. The price level remained stable, with a negative 0.2 percent CPI inflation rate and a 0.69 percent core CPI inflation rate.

Following the Board's decision, the M2 target range for 2002 was revised downward to between 3.5 percent and 8.5 percent. The average M2 growth rate was 3.55 percent, which remained within the target range but was close to the lower bound. In respect of the foreign exchange market, the NT dollar exchange rate exhibited dynamic stability throughout 2002.

At the March meeting, considering the stable domestic economic situation in the first quarter, the Board did not further loosen its monetary policy stance. However, at the June meeting, in view of the volatility in international financial markets and weak domestic demand, the Board decided to lower the discount rate by 25 basis points. Meanwhile, the Board decided to cut the required reserve ratio on foreign currency deposits from 2.5 percent to 0.125 percent in response to the excess supply of US dollars in the foreign exchange market and the relatively low short-term interest rates on US dollar deposits compared with those on NT dollar deposits. At the September meeting, taking into account the moderate recovery of the domestic economy and stable prices, the Board decided to leave interest rates unchanged. On November 12, in view that the recovery was mainly driven by export while domestic demand

needed further boosting, the Bank, after ad hoc consultation with the Board, cut the discount rate further by 25 basis points. At the December meeting, the Board decided to leave the discount rate unchanged. However, to increase flexibility for open market operations, the Bank allowed the overnight call-loan rate to move around the discount rate, instead of above it as previously did. The Board also urged to strengthen the function of the Small and Medium-sized Enterprise Credit Guarantee Fund.

Institutional reforms were actively implemented in 2002. Due to the downward rigidity of prime rates in the local banking system, efforts were made to induce banks to adopt the adjustable rate mortgages and the new market interest rate-linked prime lending rate regime. As pricing transparency was improved, banks' mortgage rates and prime rates were substantially lowered to the benefits of borrowers. A major payment system reform in 2002 was the adoption of the real-time gross settlement mechanism in the CBC Inter-bank Funds Transfer System, which eliminated the settlement risk and the systemic risk of large financial transactions. On the bank supervisory front, the Bank collaborated with the Ministry of Finance and the Central Deposit Insurance Corporation to devise various on-site examination material and off-site monitoring indicators to enhance the supervision of financial holding companies. Moreover, the Bank issued new denominations of NT\$2,000 and NT\$200 notes in 2002.

