

The Central Bank of China

Annual Report 2004



Taipei, Taiwan
The Republic of China

Foreword

During 2004, Taiwan's external trade performed exceptionally well, driven by the global economic recovery. Domestic demand also picked up as a result of buoyant consumption and investment. However, during the second half of the year, surging oil prices, interest rate hikes by major countries and the high base of 2003 caused a drag on the pace of economic expansion. Nevertheless, GDP managed to grow by a brisk 5.71 percent for the year as a whole. Furthermore, consumer prices rose by 1.62 percent as international commodity prices increased and a harsh typhoon season pushed up fruit and vegetable prices.

In the wake of economic expansion, rising prices, and negative real interest rates, the Bank turned its low interest rate policy, adopted since the end of 2000, into a neutral monetary stance in October to curb inflationary expectations. By the end of 2004, the Bank had twice raised the discount rate, gradually leading market rates upwards. In addition, the Bank urged community financial institutions to adopt a base rate pricing system to improve the transparency of market rate adjustment. The Bank also continued promoting policy lending, including preferential housing loans and project finance for traditional industries.

Under the Bank's prudent policy, monetary aggregates expanded moderately throughout 2004. M2 grew by 7.45 percent on average. The NT dollar exhibited dynamic stability, trading at 31.917 against the US dollar at the end of 2004. This represented an appreciation of 6.46 percent over a year earlier. Foreign exchange reserves continued to build to US\$241.7 billion.

Meanwhile, the Bank promoted institutional reforms to foster sound development of financial markets. The Bank helped set up the Bills Depository and Clearing System and promoted the electronic processing of check payments by the Taiwan Clearing House, greatly improving payment efficiency. The Bank also continued its efforts in financial liberalization and globalization. It introduced more foreign exchange products, streamlined foreign investment application procedures, and promoted direct financial business across the Taiwan Strait. A milestone in Taiwan's financial supervisory history was reached when the Financial Supervisory Commission of the Executive Yuan was established in July 2004. The Bank no longer undertakes financial examination responsibilities except those related to the Bank's monetary, credit and foreign exchange policies.

Many challenges still lie ahead as globalization and financial innovation complicate the task of monetary policy formulation. The Bank's monetary policy will continue to focus on maintaining price and financial stability, and sustainable development of the economy.

Finally, my sincere appreciation goes to my colleagues for their continued dedication during 2004. Together, we will work hard to meet the challenges in the year ahead.



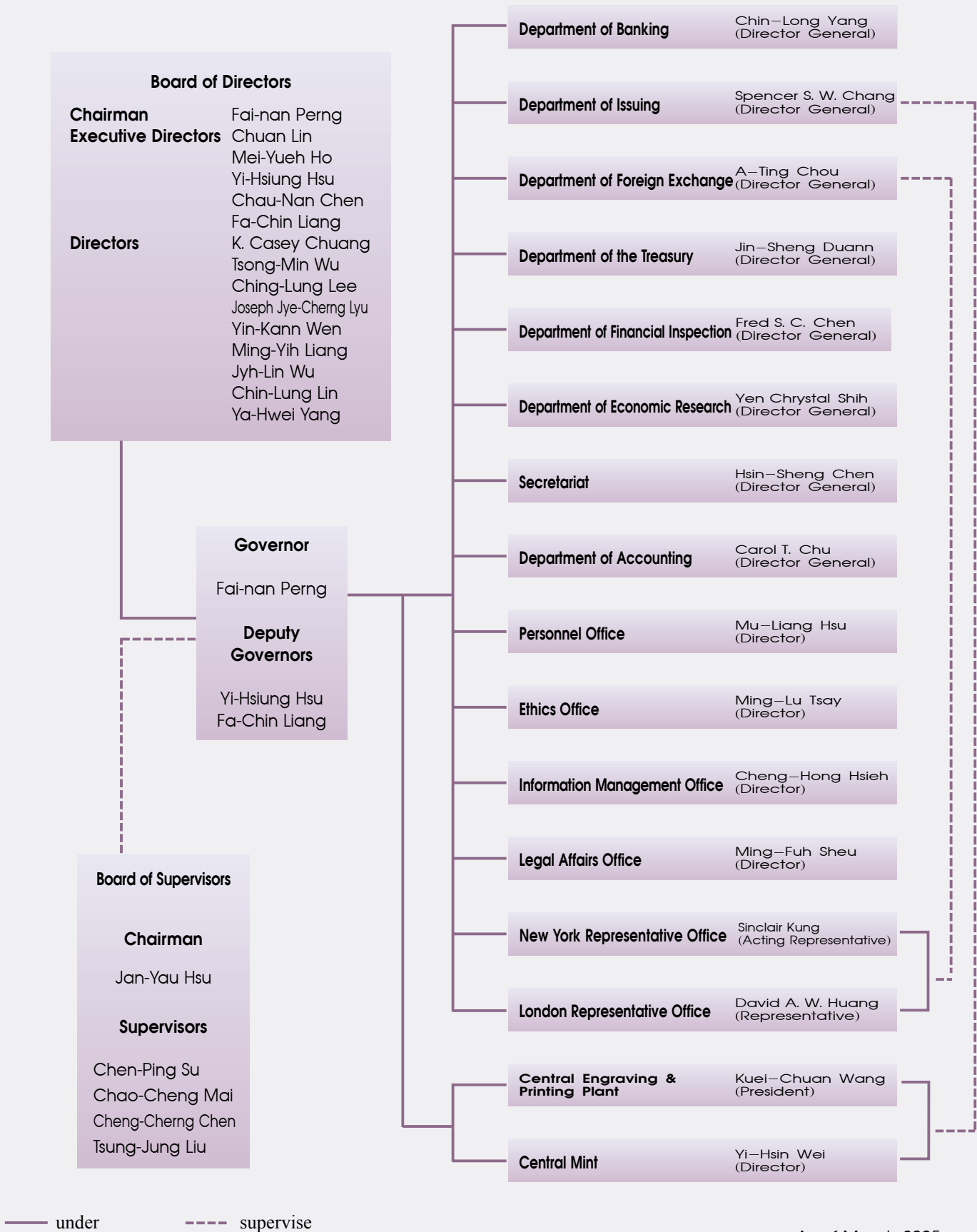
Fai-nan Perng
Governor

March 28, 2005

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Organization and Management of the Central Bank of China



As of March 2005



Chairman
Board of Directors
Governor Fai-nan Perng



Executive
Director Chuan Lin



Executive
Director Mei-Yueh Ho



Executive
Director
Deputy Governor Yi-Hsiung Hsu



Executive
Director Chau-Nan Chen



Executive
Director
Deputy Governor Fa-Chin Liang



Director K. Casey Chuang



Director Tsong-Min Wu



Director Ching-Lung Lee



Director Joseph Jye-Cherng Lyu



Director Yin-Kann Wen



Director Ming-Yih Liang



Director Jyh-Lin Wu



Director Chin-Lung Lin



Director Ya-Hwei Yang



Chairman
Board of Supervisors Jan-Yau Hsu



Supervisor Chen-Ping Su



Supervisor Chao-Cheng Mai



Supervisor Cheng-Cherng Chen



Supervisor Tsung-Jung Liu



I. DEVELOPMENTS IN THE REAL ECONOMY

- 1. Overview**
- 2. National Output and Income**
- 3. Balance of Payments**
- 4. Prices**
- 5. Public Finance of the Central Government**
- 6. Labor Market**

I. Developments in the Real Economy

1. Overview



According to the International Monetary Fund (IMF), global economic growth recorded a 28-year high of 5.1 percent in 2004. Global economic expansion accelerated during the first half of 2004 but slowed in the second half as international oil prices climbed to new highs and US rate hikes triggered a rising trend in global interest rates. As far as prices are concerned, rising oil and

commodity prices pushed up wholesale prices worldwide, while consumer price inflation was relatively benign due to intense competition in retail markets. The IMF estimated CPI inflation in developed economies rose from the previous year's 1.8 percent to 2.0 percent in 2004.

Driven by a robust global economy, Taiwan's external trade performed splendidly, leading to a rise in industrial output. In terms of domestic demand, private investment picked up pace in line with warming prospects, and private consumption also strengthened, fueled by active asset markets, improving job markets and income growth. The brisk pace of economic growth slowed during the second half of the year, affected by the slowdown in global economic expansion. Nevertheless, Taiwan economic growth reached 5.71 percent for 2004 as a whole, representing the highest rate since 2001.

With respect to prices, the deflationary pressure that had confronted Taiwan since 2001 was no longer present. As domestic fruit and vegetable prices rose as a result of poor weather conditions and international prices of crude oil and raw materials surged, the wholesale price index exhibited an annual growth rate of 7.03 percent in 2004. A highly competitive retail market and stable services prices, including residential rent, contributed to a much smaller increase of 1.62 percent in the CPI.

The job market gradually improved with better economic performance and continued implementation of the government's public employment project. The average unemployment

rate dropped to 4.44 percent in 2004, down by 0.55 of a percentage point from the previous year. Meanwhile, the average labor participation rate rose to 57.66 percent, up by 0.32 of a percentage point. Nevertheless, rising prices led to a 0.05 percent decrease in real regular earnings of the non-agricultural sector, the only decline on record.

Moreover, Taiwan's balance of payments was in good shape. The current account, which measures external commodity and services trade, remained in surplus. However, due to a greater increase of imports over exports, the current account surplus shrunk to US\$19.01 billion in 2004, representing a drop of 35 percent from the previous year, and a decrease in its share in GDP to 6.0 percent.

2. National Output and Income

Taiwan's economy reported a solid performance with a growth rate of 5.71 percent in 2004, up from 3.33 percent in 2003. The strong growth was mainly underpinned by a boom in exports supported by global economic recovery, as well as a steady acceleration in domestic demand driven by buoyant private investment.

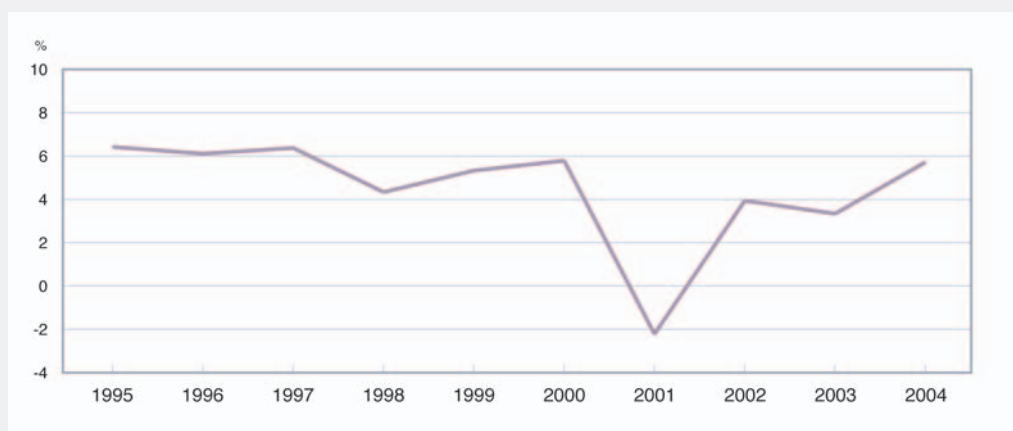
In year-over-year terms, real GDP grew by 6.72 percent in the first quarter and rose to 7.88 percent in the second quarter under the support of booming external trade and private investment. Thereafter, the momentum of GDP growth slowed somewhat, primarily due to the surge in oil prices, China's economic tightening, the interest rate hikes in major countries, and the higher base of the previous year. Real GDP growth decreased to 5.27 percent in the third quarter and 3.25 percent in the final quarter.

Per capita GNP in US dollars increased by US\$893 over the previous year to US\$14,032 in 2004.

Expenditure Components of GDP

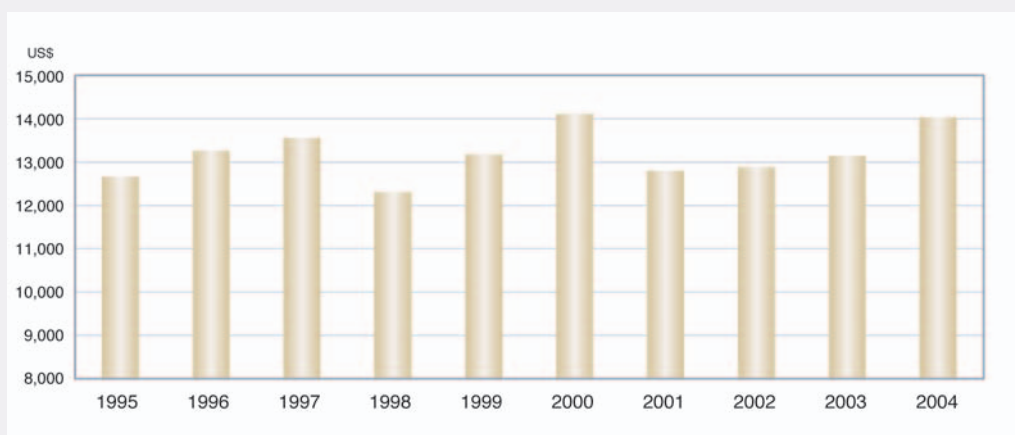
The major contributing factor to economic growth in 2004 was gross fixed capital formation, which made a contribution of 2.59 percentage points to real GDP growth. Private consumption made a positive contribution of 1.91 percentage points for the year. Among all the expenditure components, exports of goods and services expenditure accounted for the largest share, or 65.76 percent of GDP in 2004, followed by private consumption with 62.99 percent and gross

Economic Growth Rate



Source: *Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.*

Per Capita GNP



Source: *Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.*

fixed capital formation with 20.12 percent.

(1) Modest Acceleration in Private Consumption

Private consumption expenditure accelerated in the first half of the year due to the positive wealth effect from the rise in stock and real estate prices, coupled with the increase in household income reflecting improving employment conditions. The real growth rate of private consumption decelerated to 1.41 percent in the third quarter, hampered by surging oil prices, the expectation of rising interest rates, and a slack stock market. Later, as the expenditures on tourism and automobiles increased, private consumption regained its momentum in the

Expenditure on Gross Domestic Product

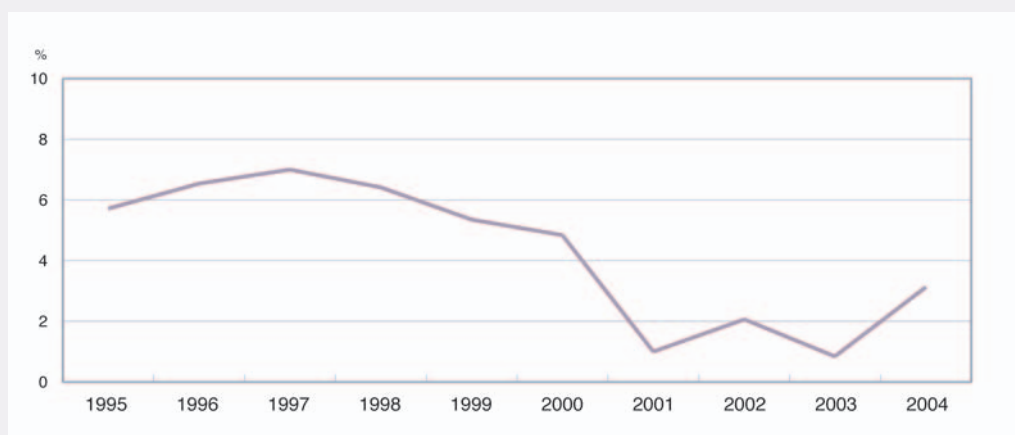
Unit: %

| | 2004 | | | 2003 | | |
|---|---------|------------------|--|---------|------------------|--|
| | Share | Real Growth Rate | Contribution to Real Growth Rate of GDP* | Share | Real Growth Rate | Contribution to Real Growth Rate of GDP* |
| Private Consumption | 62.99 | 3.13 | 1.91 | 62.53 | 0.84 | 0.53 |
| Government Consumption | 12.48 | -0.69 | -0.09 | 13.01 | 0.71 | 0.09 |
| Gross Fixed Capital Formation | 20.12 | 15.40 | 2.59 | 17.43 | -2.05 | -0.36 |
| Change in Inventory | 0.62 | — | 1.27 | -0.80 | — | 0.26 |
| Exports of Goods and Services | 65.76 | 15.27 | 8.89 | 58.42 | 10.94 | 5.93 |
| (Less : Imports of Goods and Services) | (61.96) | (18.56) | (8.88) | (50.59) | (6.72) | (3.11) |
| Expenditure on GDP | 100.00 | 5.71 | 5.71 | 100.00 | 3.33 | 3.33 |

Note: * Percentage point.

Source: *Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.*

Real Growth Rate of Private Consumption Expenditure



Source: Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.

fourth quarter. For the year as a whole, it grew by 3.13 percent in real terms, much higher than the rate of 0.84 percent registered a year earlier. Its contribution to economic growth rose to 1.91 percentage points from 0.53 of a percentage point in 2003.

With regard to the private consumption categories, the real growth rate of food consumption decreased to 1.36 percent from the 1.98 percent recorded in the previous year, while non-food consumption expenditure reached a real growth rate of 3.67 percent, a sharp increase when compared with the rate of 0.50 percent posted a year earlier. Among the components of non-food consumption expenditure, the category of recreation, entertainment, education and cultural services posted the largest growth, followed by furniture, furnishings and household equipment.

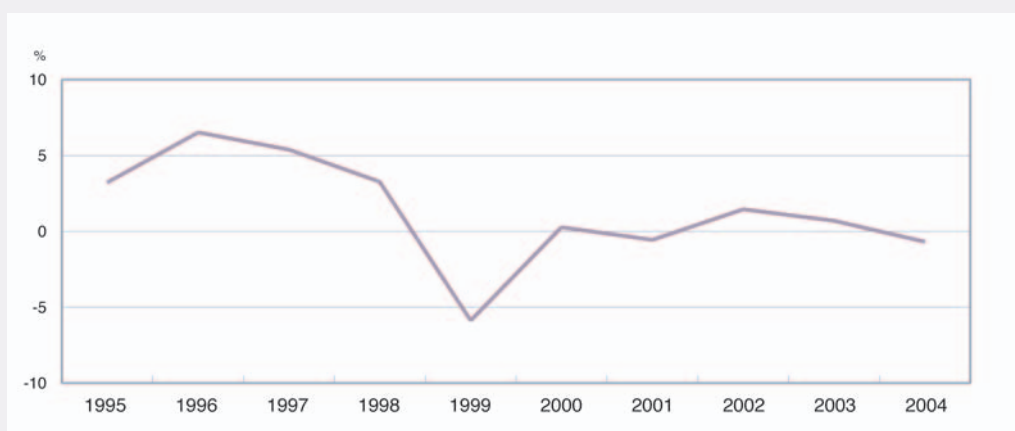
(2) Mild Decrease in Government Consumption

The growth of real government consumption fell further from the positive 0.71 percent recorded in the previous year to negative 0.69 percent in 2004, contributing a 0.09 percentage point contraction to the annual GDP growth. The reduction in government consumption mainly resulted from the government's expenditure-saving efforts in response to the unfavorable condition in public finances.

(3) Rapid Growth of Fixed Capital Formation

Due to the bright economic prospect and the low interest rate environment, the real growth rate of fixed capital formation rose dramatically from negative 2.05 percent in the

Real Growth Rate of Government Consumption Expenditure



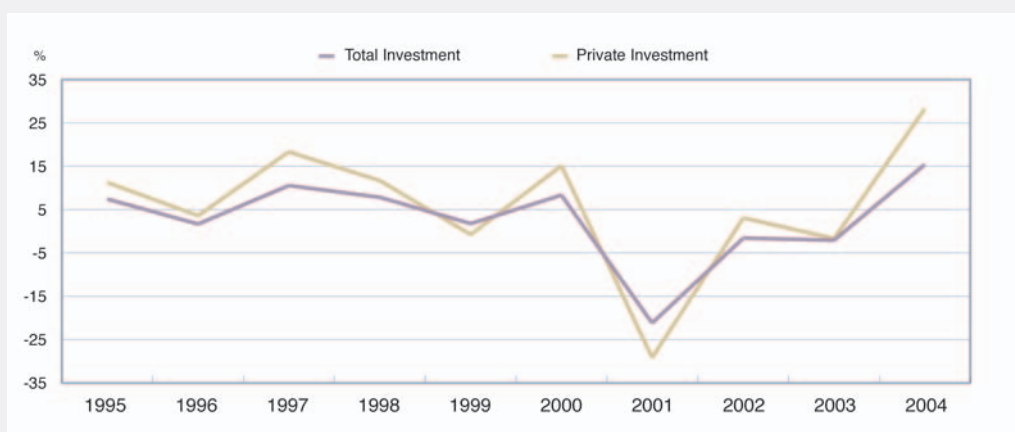
Source: Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.

previous year to 15.40 percent in the year 2004, resulting in a contribution of 2.59 percentage points to overall economic growth.

With respect to types of purchasers, real private investment expanded significantly from negative 1.62 percent in 2003 to 28.20 percent in 2004 while government investment and investment made by public enterprises declined by 4.22 percent and 15.13 percent in real terms, respectively. The contraction was because some large-scale construction projects had been completed.

In terms of different types of capital goods in fixed capital formation, the growth rate of investment in the construction sector turned to an increase of 2.11 percent from a decline of

Real Growth Rate of Investment



Source: Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.

2.85 percent in 2003, owing to the recovery in the real estate market. Investment in transportation equipment grew significantly and posted a record growth rate of 24.60 percent due to the increased procurement of fleet and aircraft and of motor vehicles for business usage. In addition, investment in machinery also registered a strong growth rate of 26.25 percent, a sharp increase when compared with negative 1.89 percent in 2003. The expansion mainly resulted from the massive capacity-expanding projects of the semi-conductor and thin film transistor-liquid crystal display (TFT-LCD) industries, and the large-scale investments by Formosa Plastics Corporation's phase IV of the Sixth Naphtha Cracking Project and Taiwan High Speed Rail Corporation's core system.

(4) Significant Rise in Exports

Against the backdrop of rapid expansion in the global economy, exports of optics equipment and electronics, basic metal products, and plastic and rubber products increased substantially. Therefore, exports grew at a rate over 20 percent during the first half of 2004. Later, export growth slowed as world economic growth was restrained by higher oil prices, China's tightening economic measures and rising interest rates in major countries. The expansion of export growth further slumped to below 5 percent in the fourth quarter due to the sluggish performance in the electronics industry and the higher base in 2003.

For the year as a whole, the real growth of exports of goods and services measured in NT dollars increased from 10.94 percent in 2003 to 15.27 percent in 2004. Exports of goods and services accounted for 65.76 percent of GDP for the year, contributing to economic growth by 8.89 percentage points.

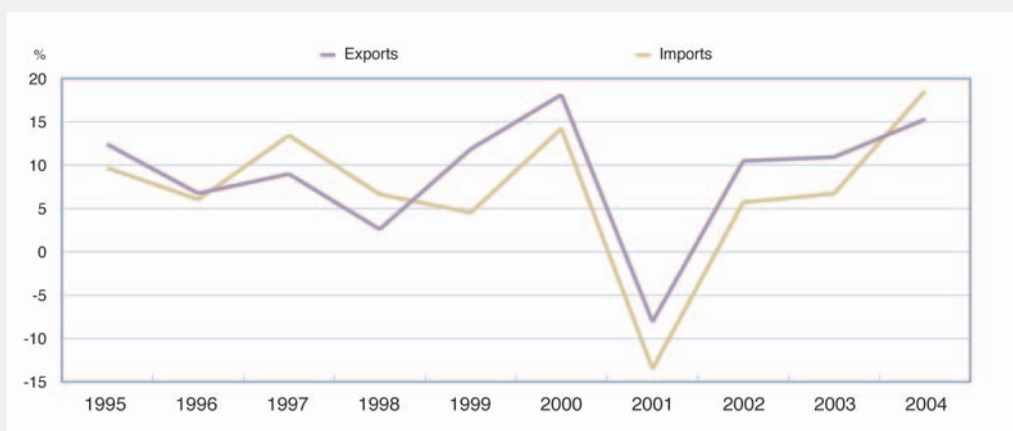
(5) Strong Expansion of Imports

Driven by the derived demand from the rapid growth of exports, import growth also experienced a similar expanding trend. However, the pace of import growth was much stronger than that of exports in the fourth quarter, which was fueled by buoyant investment activity.

Imports of goods and services also increased, causing the real growth rate, measured in NT dollars, to rise by 18.56 percent in 2004, a considerable increase compared with 6.72 percent in the previous year. Imports of goods and services accounted for 61.96 percent of GDP for the year, contributing negative 8.88 percentage points to economic growth.

Overall, foreign trade made a relatively small net contribution of 0.02 of a percentage point to GDP growth in 2004.

Real Growth Rate of Exports and Imports



Source: *Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.*

GDP by Sector of Production

For the year 2004, the industrial and services sectors both registered positive growth rates, while the agricultural sector posted a negative growth rate. The services sector remained the predominant driving force for the Taiwan economy during the year, contributing 3.19 percentage points to economic growth, up from the previous year's 1.91 percentage points. The contribution of industrial output to overall economic growth rose to 2.65 percentage points, owing to the improved business climate and a fast expansion of manufacturing production. The contribution of agricultural production to overall GDP reversed to negative for the year.

Regarding the share of each sector's output in GDP, the share of agricultural output continued to decrease and accounted for a mere 1.74 percent of total output in 2004. The share of industrial output in GDP continued its downward trend, standing at 29.54 percent for the year. In contrast, the services sector's share of total output continued to rise to 68.72 percent.

(1) Decrease in Agricultural Output

Owing to market liberalization, agricultural production contracted due to cost factors. In addition, the production of fruits, vegetables, fish and shellfish decreased as a result of heavy rain and severe typhoons. The real growth rate of agricultural production in 2004 declined sharply to negative 7.06 percent from the positive 0.20 percent achieved in the previous year.

(2) Growth in Industrial Output

Industrial production in 2004 was sustained by a stable economic recovery and increased manufacturing production. The real growth rate of industrial output reached 8.25 percent, 3.78 percentage points higher than the rate of 4.47 percent posted in the previous year. Boosted by the rising industrial production, the sector of electricity, gas and water grew by 4.54 percent in real terms, rising from a 3.53 percent growth rate registered in 2003.

Production in mining and quarrying, while still contracting, declined only 3.05 percent in real terms in 2004 as a recovery in the construction industry helped to boost the demand for construction materials.

Manufacturing production in real terms expanded by 9.36 percent, rising from the growth rate of 5.72 percent posted in the previous year. It registered a two-digit growth rate in the first half of the year, underpinned by the booming global economy. However, the expansion

Gross Domestic Product by Kind of Activity

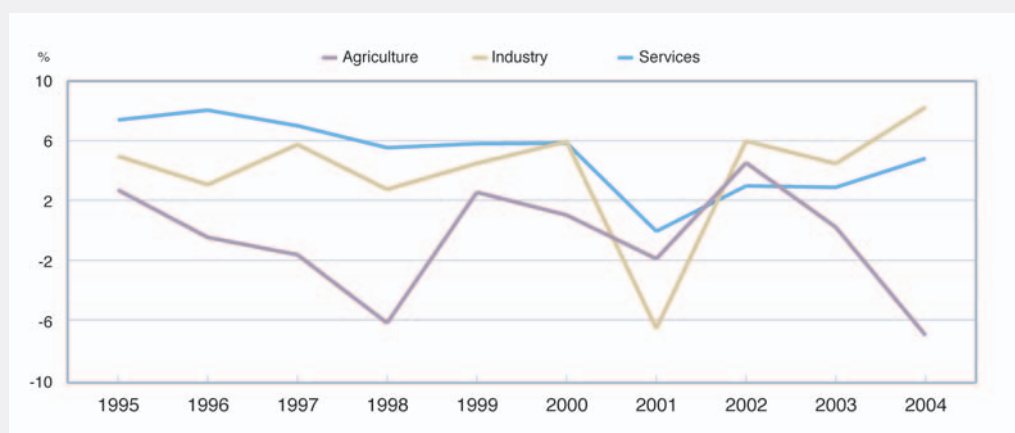
Unit: %

| | 2004 | | | 2003 | | |
|---|--------|------------------|--|--------|------------------|--|
| | Share | Real Growth Rate | Contribution to Real Growth Rate of GDP* | Share | Real Growth Rate | Contribution to Real Growth Rate of GDP* |
| Agriculture | 1.74 | -7.06 | -0.14 | 1.80 | 0.20 | 0.00 |
| Industry | 29.54 | 8.25 | 2.65 | 30.57 | 4.47 | 1.42 |
| Mining & Quarrying | 0.35 | -3.05 | -0.01 | 0.34 | -19.05 | -0.07 |
| Manufacturing | 25.53 | 9.36 | 2.54 | 25.77 | 5.72 | 1.51 |
| Construction | 1.72 | 1.13 | 0.03 | 2.25 | -3.49 | -0.10 |
| Electricity, Gas & Water | 1.93 | 4.54 | 0.10 | 2.22 | 3.53 | 0.08 |
| Services | 68.72 | 4.83 | 3.19 | 67.63 | 2.88 | 1.91 |
| Trade | 19.10 | 7.36 | 1.28 | 18.14 | 3.44 | 0.60 |
| Accommodation & Eating-drinking Places | 2.21 | 6.91 | 0.14 | 2.11 | 0.02 | 0.00 |
| Transport, Storage & Communications | 7.06 | 5.81 | 0.41 | 6.90 | 4.42 | 0.31 |
| Finance & Insurance | 11.57 | 4.48 | 0.50 | 11.40 | 5.49 | 0.60 |
| Real Estate & Rental & Leasing | 9.90 | 2.77 | 0.28 | 10.05 | 2.32 | 0.23 |
| Professional, Scientific & Technical Services | 2.51 | 2.32 | 0.06 | 2.50 | 2.86 | 0.07 |
| Educational Services | 1.97 | 1.32 | 0.02 | 2.00 | 3.20 | 0.06 |
| Health Care & Social Welfare Services | 3.14 | 1.90 | 0.06 | 3.13 | 1.94 | 0.06 |
| Government Services | 10.61 | 1.22 | 0.13 | 10.88 | 3.08 | 0.32 |
| Gross Domestic Product | 100.00 | 5.71 | 5.71 | 100.00 | 3.33 | 3.33 |

Note: * Percentage point.

Source: *Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.*

Real Growth Rate of Output by Sector



Source: *Statistical Abstract of National Income in Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.*

pace of manufacturing production dropped to 3.12 percent in the fourth quarter, constrained by the slowdown in the global economy. For the year as a whole, the contribution of manufacturing output to overall economic growth reached 2.54 percentage points, higher than last year's 1.51 percentage points. Within the manufacturing sector, the information and electronic, metal and machinery, and the chemical industries exhibited strong growth rates of 14.14 percent, 11.43 percent and 9.81 percent, respectively. The food, textile and other industry remained weak, yet its production rebounded to post a growth rate of negative 0.34 percent, a favorable level when compared with those in recent years.

The real estate market showed signs of a brisk recovery in the first half of the year, but the shortage of certain construction materials hampered its growth in the second half. However, construction permits still increased sharply by 50 percent for the year. The construction sector thus recorded a real growth rate of positive 1.13 percent in 2004, which reversed the contracting pattern of recent years.

(3) Rise in the Services Sector

Services output expanded by 4.83 percent in real terms for the year 2004, higher than the 2.88 percent posted in the previous year. The growth was mainly supported by rising activities in trade, finance and insurance, and transport, storage and communications. The 7.36 percent expansion in the trade sector benefited from buoyant external trade and private consumption. The accommodation, eating-drinking places sector and the transport, storage, and communications sector also exhibited strong growth. On the back of more consumers spending on tourism and

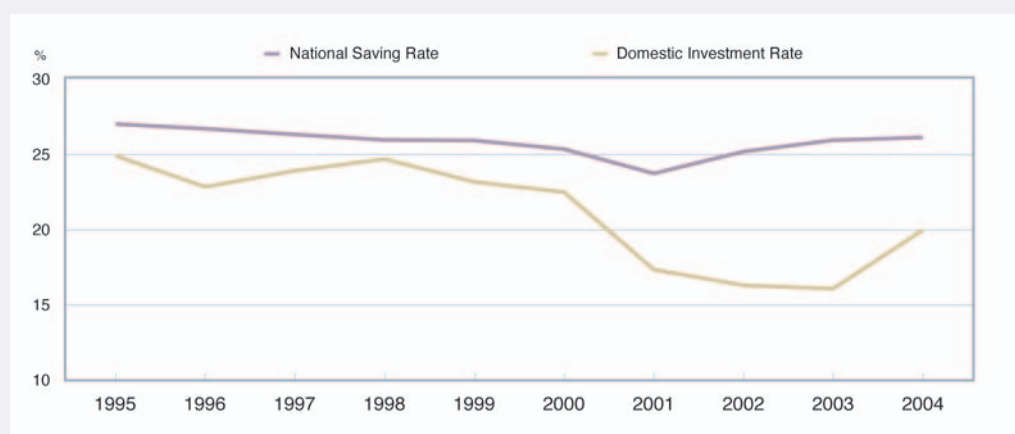
eating out, the accommodation and eating-drinking places sector registered a real growth rate of 6.91 percent. The growth of output in the transport, storage, and communications sector rose to 5.81 percent in real terms, owing to the expansion of the cargo flight business and the growing popularity of mobile phones and network communications. Most of the other industries within the services sector posted lower growth rates than those of the previous year. In particular, among the services sector, the government services sector recorded the smallest growth rate for 2004, reflecting the government's continued efforts to contain expenditure.

Slight Increase in National Saving Rate

The national saving rate (national saving to GNP measured at current prices) increased from 25.97 percent in the previous year to 26.15 percent in 2004 as national consumption (including both private consumption and government consumption expenditures) grew by a slower rate of 3.56 percent compared to the GNP growth rate of 4.05 percent. The slower growth of national consumption reflected the mild increase in private consumption and the slight decline in government consumption.

The excess saving (national saving less gross domestic investment) to GNP ratio dropped from 9.89 percent in the previous year to 6.16 percent in 2004 as a result of a much stronger growth rate of domestic investment than that of national saving.

National Saving Rate and Domestic Investment Rate



Source: *Statistical Abstract of National Income in Taiwan Area, the Republic of China*, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, March 2005.

3. BALANCE OF PAYMENTS

The balance of payments in Taiwan was characterized by a narrowing current account surplus and a net inflow in the financial account in 2004. The current account surplus shrank to US\$19,013 million, lower than the previous year's US\$29,266 million, and accounted for 6 percent of GDP. The capital account registered a small deficit of US\$77 million. The financial account exhibited a net inflow of US\$6,366 million. As a result, the foreign reserve assets held by the Bank at end-2004 increased by US\$26,595 million over a year earlier.

A Declining Current Account Surplus

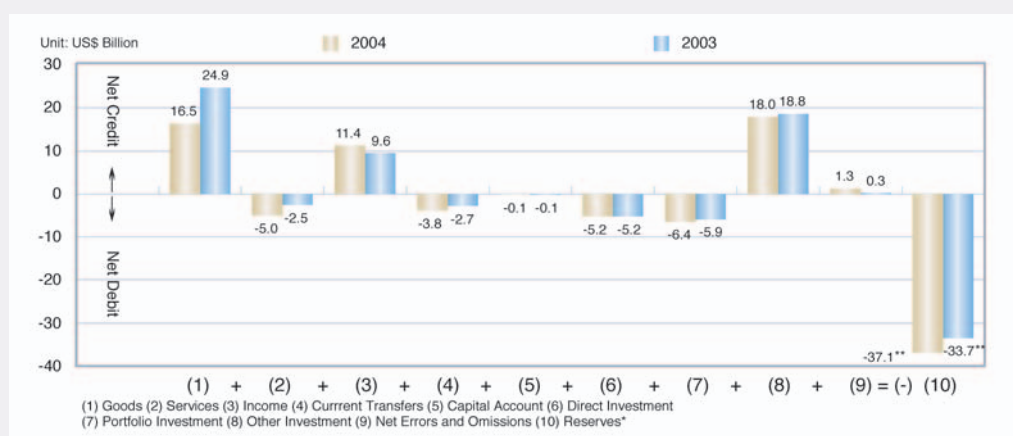
The components of the current account include goods, services, income and current transfers. The current account surplus decreased in 2004 mainly as a result of the decline in the trade surplus of goods and the widened deficits in services and current transfers.

(1) Goods

For the year 2004, both on a balance of payments basis and a customs basis, the value of exports and imports registered double-digit growth rates and hit historic highs. However, the trade surplus shrank as a result of a larger increase in imports than in exports.

On a balance of payments basis, the value of exports grew by 20.7 percent to US\$173,153 million, mainly driven by persistently steady growth in the global economy and in the information

Balance of Payments



Notes: * Excluding valuation changes in exchange rates.

**The minus sign(-) indicates an increase in foreign exchange reserves.

Source: *Balance of Payments, Taiwan District, Republic of China, Department of Economic Research, Central Bank of China.*

Balance of Payments

Unit: US\$ Million

| | 2004 | 2003 |
|----------------------------------|----------|----------|
| A. Current Account | 19,013 | 29,266 |
| Goods: exports f.o.b. | 173,153 | 143,447 |
| Goods: imports f.o.b. | -156,685 | -118,548 |
| Balance on Goods | 16,468 | 24,899 |
| Services: credit | 25,777 | 23,166 |
| Services: debit | -30,784 | -25,635 |
| Balance on Services | -5,007 | -2,469 |
| Income: credit | 15,305 | 12,991 |
| Income: debit | -3,927 | -3,436 |
| Balance on Income | 11,378 | 9,555 |
| Current transfers: credit | 3,170 | 2,673 |
| Current transfers: debit | -6,996 | -5,392 |
| Balance on Current transfers | -3,826 | -2,719 |
| B. Capital Account | -77 | -87 |
| Total, Groups A plus B | 18,936 | 29,179 |
| C. Financial Account | 6,366 | 7,630 |
| Direct investment abroad | -7,087 | -5,682 |
| Direct investment in Taiwan | 1,898 | 453 |
| Portfolio investment assets | -23,511 | -35,620 |
| Portfolio investment liabilities | 17,074 | 29,693 |
| Other investment assets | 327 | 4,456 |
| Other investment liabilities | 17,665 | 14,330 |
| Total, Groups A through C | 25,302 | 36,809 |
| D. Net Errors And Omissions | 1,293 | 283 |
| Total, Groups A through D | 26,595 | 37,092 |
| E. Reserves and Related items* | -26,595 | -37,092 |

Note: * Excluding valuation changes in exchange rates.

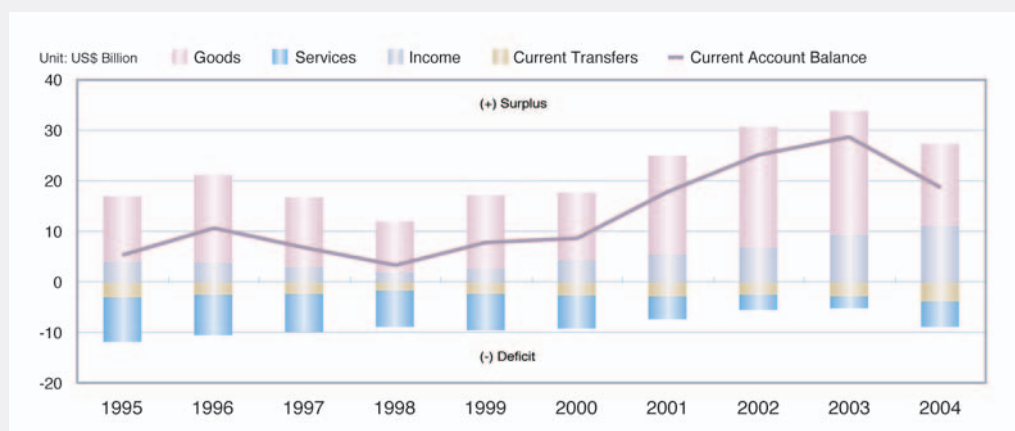
Source: Balance of Payments, Taiwan District, Republic of China, Department of Economic Research, Central Bank of China.

technology (IT) industry worldwide. The value of imports rose by 32.2 percent to US\$156,685 million. It was primarily led by stronger derived demand arising from the expansion in exports and the recovery in domestic investment, along with surging international oil and commodity prices. The trade surplus on goods decreased to US\$16,468 million for the year, a decrease of 33.9 percent from the previous year.

As indicated by the Taiwan Customs' statistics, the three major trading partners for Taiwan in 2004 were mainland China (including Hong Kong), the U.S. and Japan. Exports to these three countries accounted for 60.5 percent of total exports, while imports from these three countries made up a 50.1 percent of total imports.

In terms of Taiwan's trade with mainland China (including Hong Kong), exports totaled US \$63,846 million for the year, with a growth rate of 28.3 percent when compared with the previous

Current Account



year. The marked growth was attributable to mainland China's strong economic growth, as well as the rising demand for raw materials, IT products and parts from Taiwanese firms operating in mainland China. This increase appeared significant when compared with other major export markets, and the share of exports to mainland China (including Hong Kong) increased by 2.2 percentage points to 36.7 percent. Mainland China (including Hong Kong) remained Taiwan's largest export market in 2004.

Imports from mainland China (including Hong Kong) rose by 48 percent, and its share of total imports rose to 11.2 percent in 2004. The large increase stemmed from the increased demand for Chinese electronics, information products and related parts due to the division of labor between Taiwanese industries on either side of the Taiwan Strait. The opening to import items from mainland China after both economies joined the WTO contributed to this growth as well. The bilateral trade surplus with mainland China (including Hong Kong) climbed to US \$45,074 million, reflecting a 21.5 percent increase. Mainland China (including Hong Kong) remained the largest source of Taiwan's trade surplus.

With respect to bilateral trade with the U.S., exports to the U.S. increased by 8.4 percent in 2004, compared with a contraction of 3.1 percent in the previous year. The share of exports to the U.S. as a proportion of total exports has been decreased since 1998, and further decreased to 16.2 percent in 2004. The reasons behind the continuous declines were the increased trade activity between the U.S. and NAFTA (North American Free Trade Agreement) members, the competition from mainland China's low-priced products, and the continued outward relocation (mainly to mainland China) of local industries. Imports from the U.S. increased by 28.6 percent,

while its share of total imports declined slightly from 13.2 percent in 2003 to 12.9 percent in 2004. Because the increase in imports was more than that in exports, the bilateral trade surplus with the U.S. decreased to US\$6,490 million, representing a decline of 28.8 percent. The U.S. remained the second largest source of Taiwan's trade surplus.

Regarding bilateral trade with Japan, the recovery of the Japanese economy led to a rise in exports to Japan by 10.8 percent in 2004, and the share of exports to Japan further fell to 7.6 percent from 8.3 percent a year earlier. Imports from Japan increased by 33.7 percent compared with the previous year, with the share of total imports rising to 26.0 percent in 2004. Japan remained Taiwan's largest source of imports. As the increase in imports was more than that in exports, Taiwan's trade deficit with Japan registered a considerable increase of 46.8 percent to US\$30,428 million for the year, the highest in history.

Exports to Europe increased by 14.6 percent in 2004, with the share of total exports falling to 13.5 percent. Imports from Europe increased by 31.1 percent in 2004, with the share of imports decreasing slightly to 12.7 percent of total imports. As the increase of imports was more than that of exports, Taiwan's trade surplus with Europe decreased from US\$4,212 million in 2003 to US\$2,137 million in 2004.

Direction of Trade in Goods by Country

Unit: %

| | 2004 | | | 2003 | | |
|-------------------------------------|--------------------------|-------|------------------|--------------------------|-------|------------------|
| | Amount (US\$ Million) | Share | Annual Change | Amount (US\$ Million) | Share | Annual Change |
| Exports | | | | | | |
| Mainland China(including Hong Kong) | 63,846 | 36.7 | 28.3 | 49,771 | 34.5 | 22.0 |
| U. S. A. | 28,123 | 16.2 | 8.4 | 25,942 | 18.0 | -3.1 |
| Europe | 23,435 | 13.5 | 14.6 | 20,452 | 14.2 | 10.2 |
| Southeast Asia 6* | 22,821 | 13.1 | 33.7 | 17,073 | 11.8 | 10.0 |
| Japan | 13,204 | 7.6 | 10.8 | 11,913 | 8.3 | -0.6 |
| Rest of the World | 22,604 | 13.0 | 18.8 | 19,030 | 13.2 | 12.1 |
| Total | 174,034 | 100.0 | 20.7 | 144,180 | 100.0 | 10.4 |
| Imports | | | | | | |
| Japan | 43,632 | 26.0 | 33.7 | 32,635 | 25.6 | 19.6 |
| U. S. A. | 21,633 | 12.9 | 28.6 | 16,820 | 13.2 | -7.0 |
| Europe | 21,298 | 12.7 | 31.1 | 16,240 | 12.8 | 10.9 |
| Southeast Asia 6* | 20,229 | 12.0 | 16.1 | 17,431 | 13.7 | 5.3 |
| Mainland China(including Hong Kong) | 18,773 | 11.2 | 48.0 | 12,686 | 10.0 | 31.0 |
| Rest of the World | 42,331 | 25.2 | 34.7 | 31,436 | 24.7 | 19.6 |
| Total | 167,895 | 100.0 | 31.9 | 127,248 | 100.0 | 13.1 |

Note: * Including Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam.

Source: *Monthly Statistics of Exports and Imports, Taiwan District, Republic of China, Department of Statistics, Ministry of Finance.*

Owing to steady growth in Southeast Asia, exports to the six countries in the region, including Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam, increased by 33.7 percent. Exports to the Philippines grew by 69.3 percent, the highest among the six countries. The share of exports to these countries rose to 13.1 percent. Imports from these countries rose by 16.1 percent in 2004, with the share of imports declining to 12.0 percent. As the increase of exports was more than that of imports, Taiwan's trade surplus with the six countries increased to US\$2,592 million in 2004 from a trade deficit of US\$358 million in 2003.

(2) Services

In 2004, both service receipts and payments registered their highest amounts in history. With total service receipts increasing by US\$2,611 million to US\$25,777 million in 2004 and total service payments increasing by US\$5,149 million to US\$30,784 million, the service deficit widened to US\$5,007 million from the US\$2,469 million recorded in 2003.

Of the various components of the services account, net payments with respect to transportation increased from US\$2,327 million recorded a year earlier to US\$2,845 million in 2004, largely due to the increase in international freight expenses paid to foreign vessels, coupled with the expansion in imports. Total travel receipts surged by US\$1,063 million to US\$4,040 million, as the result of an increase in both the number and per person expenditure of nonresidents visiting Taiwan. Total travel payments for the year increased by US\$1,690 million to US\$8,170 million, due to an increase in overseas visits by residents. Net travel payments expanded to US\$4,130 million as a result of the increase in total travel receipts being less than that in total travel payments. Other services receipts and payments both hit historic highs. Total other services receipts increased by US\$639 million to US\$16,441 million, while total other services payments increased by US\$2,032 million to US\$14,473 million. As the increase in total other services payments was more than that in total other services receipts, the surplus in net total other services decreased from US\$3,361 million in 2003 to US\$1,968 million in 2004.

(3) Income

Total income receipts increased by US\$2,314 million to US\$15,305 million in 2004, the highest level ever recorded. Total income payments for the year amounted to US\$3,927 million, US\$491 million more than in 2003. The surplus on the income account increased from US\$9,555 million in 2003 to a new high of US\$11,378 million in 2004. The increase was mainly from residents' overseas investment income.

(4) Current Transfers

Total current transfer receipts amounted to US\$3,170 million in 2004, US\$497 million more than in the previous year. Total current transfer payments for the year expanded by US\$1,604 million to US\$6,996 million, reaching a historical high, on account of the sharp increase in outward remittances by residents to support their overseas relatives. Net current transfer payments increased from US\$2,719 million in 2003 to US\$3,826 million in 2004.

Shrinking Capital Account Deficit

The capital account includes capital transfers (debt forgiveness, ownership transfer of fixed assets and migrants' transfers), and the acquisition and disposal of non-produced, non-financial assets. In 2004, the capital account consistently exhibited a deficit, but the gap narrowed by US\$10 million to US\$77 million, the lowest figure recorded since 1990. The decline was the result of shrinking acquisitions of non-produced, non-financial assets.

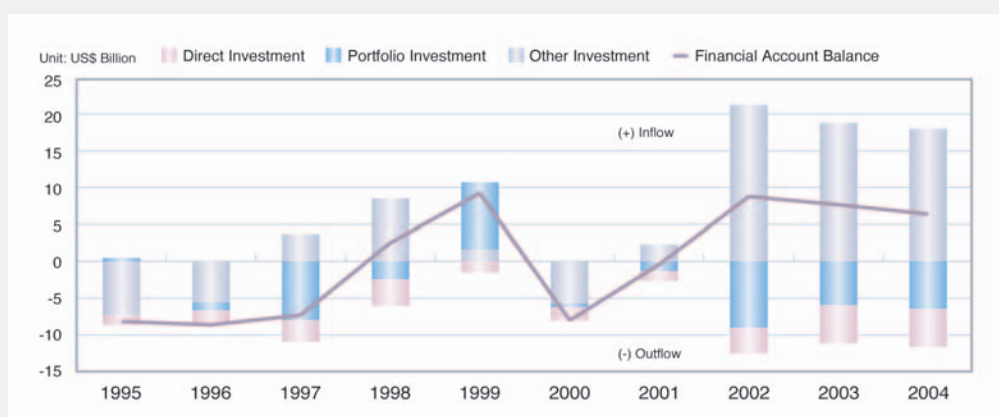
Net Inflow in the Financial Account

In 2004, the financial account presented a net inflow of US\$6,366 million. In terms of sub-categories, direct investment and portfolio investment posted a net outflow of US\$5,189 million and US\$6,437 million, respectively, while other investment posted a net inflow of US\$17,992 million.

(1) Direct Investment

Direct investment abroad by residents accounted for a net outflow of US\$7,087 million, the highest in history, and US\$1,405 million more than in the previous year. Mainland China

Financial Account



received the lion's share of Taiwanese direct investment abroad, which was perhaps driven by an expectation of an appreciation of the Renminbi. Direct investment in Taiwan by nonresidents registered a net inflow of US\$1,898 million, a sharp increase of US\$1,445 million or 3.19 times that of the previous year, indicating a recovery of foreign direct investment. The net outflow of direct investment declined to US\$5,189 million in 2004, compared to US\$5,229 million in 2003.

(2) Portfolio Investment

Portfolio investment abroad by residents recorded a huge net outflow of US\$23,511 million, the second highest level ever recorded. It showed that residents increased their holdings of foreign securities through the purchases of overseas mutual funds. Net inflow of local portfolio investment by nonresidents registered US\$17,074 million, also the second highest level ever recorded. The capital inflow in the domestic market can largely be attributed to the massive portfolio allocation of international funds in Asia and the expectation of better earnings outlooks for locally listed companies. In addition, domestic enterprises preferred to raise funds through the international market and therefore increased the issuance of European (offshore) convertible bonds and depository receipts overseas. As a result, portfolio investment posted a net outflow of US\$6,437 million in 2004.

(3) Other Investment

Other investment abroad by residents recorded a net inflow of US\$327 million, representing a decrease of other claims on nonresidents by residents. This inflow was mainly because of the withdrawal of residents' overseas claims, following the weakening of the US dollar in the international market. Other local investments by nonresidents stood at a net inflow of US\$17,665 million, representing an increase of residents' other liabilities to nonresidents. The inflow can be mainly attributed to the borrowings from abroad by the local non-bank private sector and banking sector in expectation of the NT dollar's appreciation against the US dollar. As a consequence, other investment exhibited a net inflow of US\$17,992 million in 2004.

Considerable Increase in Foreign Exchange Reserves

For the year as a whole, the foreign exchange reserve assets held by the Bank increased by US\$26,595 million to a historic high of US\$241.74 billion at year-end. Reserve assets posted sharp increases as a result of huge current account surpluses, as well as the net inflow in the financial account, which resulted from a massive inflow of funds from overseas branches to local banks and brisk foreign portfolio investment in Taiwan.

4. Prices

After three years of downward price pressure, Taiwan's consumer price index (CPI) inflation entered mildly positive territory in 2004 and rose by 1.62 percent, while core CPI (consumer prices excluding fresh fruits and vegetables, fish and shellfish, and energy) increased a modest 0.71 percent. Consumer prices grew due to a combination of factors, including an accommodative monetary policy, the recovery in domestic demand, and the rise in raw material prices internationally.

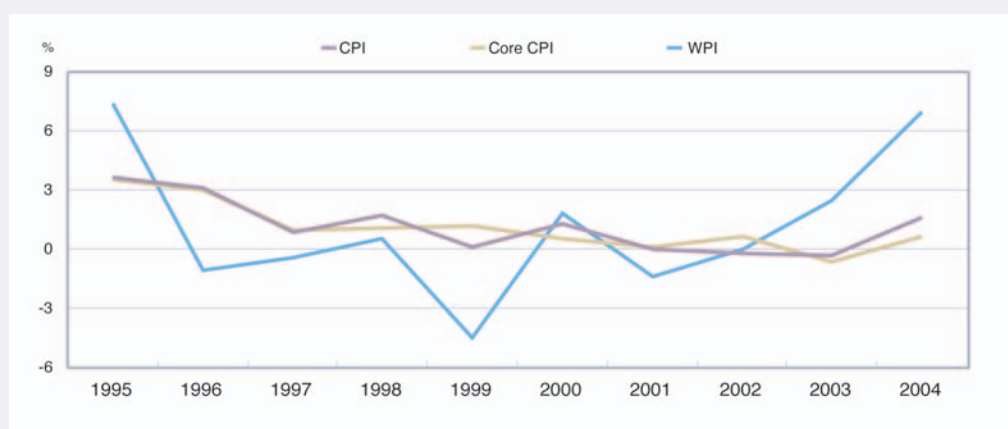
Food prices rose significantly in 2004 because of unfavorable weather conditions. In addition, rising international oil and commodity prices drove domestic wholesale prices up. The wholesale price index (WPI) in 2004 increased by 7.03%. However, intense competition in the domestic retail market made it difficult for firms to raise prices and pass on the extra costs to consumers.

Steep Increase in Wholesale Prices

The WPI soared during the first three quarters of 2004. The upward pressure abated in the last quarter due to stabilizing oil prices and a strengthening New Taiwan dollar.

As global economic recovery accelerated in 2004, the strong demand for crude oil, petrochemicals, and primary metal products pushed up commodity prices. Import prices rose by 8.57 percent despite the 3 percent appreciation of the NT dollar against the U.S. dollar. This, in turn, led to an increase in factory prices of products for domestic sale by 10.28 percent. As a result, the WPI rose to 7.03 percent in 2004, the highest since 1996.

Inflation Rate



Source: Price Statistics Monthly in Taiwan Area of the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan.

Moderate Increase in Consumer Prices

During the first half of 2004, the CPI inflation rate rose moderately. In the second half of the year, heavy rain and severe typhoons caused significant increases in food prices for four consecutive months from July. However, after October, this price pressure eased and annualized monthly price increases returned to less than 2 percent. Therefore, for the year as a whole, the CPI increased by 1.62 percent, while the core CPI edged up by only 0.71 percent.

The major factors leading to the CPI inflation include the weather-induced spike in food prices and the surge in oil prices. The food price index rose by 4.36 percent, contributing 1.10 percentage points to the CPI inflation rate, accounting for 68 percent of the overall advance in the CPI. In addition, the respective climb in oil and gas prices by 10 percent and 5.42 percent resulted in a 5.30 percent increase in the energy price index, contributing 0.29 percentage points to the CPI inflation rate, or 18 percent of the overall advance in the CPI.

Significant increases in commodity prices are typical as economic activity accelerates and capacity utilization rises, especially for products with relatively fixed supply in the short run. The prices of products for domestic sales increased 9.52 percent for the year 2004. Among the components, the prices of raw materials and intermediate materials rose 21.46 percent and 11.46 percent, respectively. However, a portion of these increases usually proves to be transitory. More importantly, cyclical swings in commodity prices tend to have a minor effect on overall inflation. The reason is that they account for a small share of total costs and that changes in commodity prices tend to be temporary and partly absorbed by firms, thus the

Major items of the CPI change in 2004

| Item | CPI inflation rate (%) | Contribution to CPI inflation rate (percentage point) |
|-------------------------------|------------------------|---|
| CPI | 1.62 | 1.62 |
| Food | 4.36 | 1.10 |
| Fruits | 16.42 | 0.38 |
| Vegetables | 9.61 | 0.26 |
| Meat | 7.07 | 0.18 |
| Energy | 5.30 | 0.29 |
| Oils | 10.00 | 0.23 |
| Gas | 5.42 | 0.05 |
| CPI Excluding Food and Energy | 0.33 | 0.23 |
| Durable Consumer Goods | -1.68 | -0.13 |
| Residential Rent | -0.64 | -0.13 |

Source: Price Statistics Monthly in Taiwan Area of the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan.

prices of finished goods only edged up 0.67 percent.

Other factors offsetting the CPI inflation include the decline in output unit labor cost driven by strong productivity and subdued upward pressure on retail prices due to intense market competition. Furthermore, falling rents for commercial property helped retard inflationary pressures. Among the components, the durable consumer goods price index continued its downward trend since 1997, the services index, which accounts for a sizable proportion of CPI, remained stable, and residential rent, a component of the services index, fell for the fourth year.

The price index for all items less food and energy advanced 0.33 percent in 2004, contributing 0.23 of a percentage point to the CPI inflation rate, or 14 percent of the overall advance in the CPI.

5. Public Finance of the Central Government

For 2004, central government finance improved mainly due to domestic economic expansion, the gradual recovery of the local stock and real estate markets, and the adoption of cost-saving and revenue-increasing initiatives. Central government revenue increased by NT\$46.6 billion while expenditure fell by NT\$52.9 billion. As a result, the central government deficit narrowed to NT\$197.6 billion, a substantial decline of 33.49 percent compared to the previous year.

Increase in Central Government Revenue

Central government revenue increased by 3.53 percent to NT\$1,367.6 billion in 2004 due to the recovery of the domestic economy and the substantial growth of 10.62 percent in tax revenue.

Tax revenues and surpluses of public enterprises and public utilities together account for 87.71 percent of total revenue. The portion of tax revenues in total revenue grew from 62.73 percent in 2003 to 67.02 percent in 2004. However, the surpluses of public enterprises and public utilities dropped by a substantial 13.32 percent due to a higher base in the previous year

Total Revenue and Expenditure of the Central Government

Unit: NT\$ Billion

| | Fiscal Year* | | | | | | | | | |
|--|--------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004** |
| Total Revenue | 937.4 | 996.8 | 1,025.2 | 1,251.5 | 1,228.6 | 2,030.8 | 1,417.2 | 1,304.7 | 1,321.0 | 1,367.6 |
| (Ratio of GDP : %) | 13.36 | 12.98 | 12.34 | 14.06 | 13.29 | 14.20 | 14.74 | 13.81 | 13.57 | 13.89 |
| Total Expenditure | 965.7 | 1,004.9 | 1,051.4 | 1,083.1 | 1,164.0 | 2,230.1 | 1,559.7 | 1,551.9 | 1,618.1 | 1,565.2 |
| (Ratio of GDP : %) | -0.40 | -0.11 | -0.32 | 1.89 | 0.70 | -1.39 | -1.48 | -2.62 | -3.05 | -2.01 |
| Surplus/Deficit | -28.3 | -8.1 | -26.2 | 168.4 | 64.6 | -199.3 | -142.5 | -247.2 | -297.1 | -197.6 |
| (Ratio to GDP : %) | -0.40 | -0.11 | -0.32 | 1.89 | 0.70 | -1.39 | -1.48 | -2.62 | -3.05 | -2.01 |
| (Ratio to Total Expenditure : %) | -2.93 | -0.81 | -2.49 | 15.55 | 5.55 | -8.94 | -9.14 | -15.93 | -18.36 | -12.62 |
| Debt Repayment | 31.0 | 80.2 | 100.4 | 103.9 | 118.0 | 193.4 | 122.2 | 55.5 | 46.5 | 56.1 |
| Financing: | 75.1 | 95.8 | 126.6 | 49.9 | 56.6 | 466.1 | 275.8 | 302.8 | 343.7 | 253.7 |
| Issuance of Government Bonds & Borrowing from Banks | 75.1 | 95.8 | 117.3 | 49.9 | 56.6 | 466.1 | 275.8 | 244.5 | 300.8 | 253.5 |
| Surplus of Previous Fiscal Years | - | - | 9.3 | - | - | - | - | 58.3 | 42.9 | 0.2 |
| Memorandum: | | | | | | | | | | |
| Debt Dependency Ratio*** (%) | 7.78 | 9.53 | 11.16 | 4.61 | 4.86 | 20.90 | 17.68 | 15.75 | 18.59 | 16.20 |

Notes: * Effective 2001, the calendar year is adopted as the fiscal year. As a transition, the fiscal year 2000 begins on July 1, 1999 and ends on Dec. 31, 2000, while the other fiscal years prior to 2000 run from July 1 of the preceding year to June 30 of the designated.

** The figures for the year 2004 are preliminary estimates.

***Debt dependency ratio is defined as the ratio of annual issuance of government bonds and borrowing from banks to total.

Sources: 1. Directorate-General of Budget, Accounting and Statistics, Executive Yuan.
2. Department of Statistics, Ministry of Finance.

caused by the addition of the dividends from the Executive Yuan's Development Fund and public enterprises. Another contributing factor was the lack of revenue generated through the privatization process of public enterprises due to a delayed schedule.

Decrease in Central Government Expenditure

Owing to enhanced cost analysis measures, more participation in public construction from the private sector, and a low interest rate environment favorable for interest-bearing government bonds, central government expenditure declined by 3.27 percent compared to the previous year. Among the components, spending on education, science and culture accounted for 19.3 percent, the largest share of total government spending and a record high for this category. Spending on social welfare accounted for the second largest share of 17.9 percent, followed by expenditure on national defense with a share of 15.9 percent.

In 2004, with more rigid control over government expenditure, the ratio of the fiscal deficit to total expenditure fell to 12.62 percent from the previous year's 18.36 percent. The ratio of the fiscal deficit to GDP also narrowed from 3.05 percent to 2.01 percent.

In addition to the Challenge 2008 - National Development Plan, the government has also

Total Revenue and Expenditure of the Central Government by Category

Unit: NT\$ Billion

| | Fiscal Year* | | | | | | | | | |
|--|--------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004** |
| Total Revenue | 937.4 | 996.8 | 1,025.2 | 1,251.5 | 1,228.6 | 2,030.8 | 1,417.2 | 1,304.7 | 1,321.0 | 1,367.6 |
| Taxes | 705.7 | 706.1 | 749.1 | 858.8 | 772.9 | 1,280.7 | 841.5 | 820.1 | 828.6 | 916.6 |
| Surpluses of Public Enterprises and Public Utilities | 113.9 | 151.6 | 149.5 | 239.9 | 284.1 | 442.4 | 335.8 | 250.6 | 326.5 | 283 |
| Fees, Fines and Indemnities | 25 | 31.9 | 32.7 | 34.9 | 29.1 | 103 | 72.5 | 123.3 | 73.3 | 75.8 |
| Revenues from Government-owned Monopolies | 39.9 | 36.4 | 37.8 | 37.4 | 35.9 | 77.3 | 57.5 | 0.4 | - | - |
| Proceeds from Sales of Properties and Recalled Capital | 31.4 | 40.7 | 31.1 | 60.5 | 91.9 | 88.4 | 80.9 | 73.9 | 65.8 | 70.4 |
| Others | 21.5 | 30.1 | 25 | 20 | 14.7 | 39 | 29 | 36.4 | 26.8 | 21.8 |
| Total Expenditure | 965.7 | 1,004.9 | 1,051.4 | 1,083.1 | 1,164.0 | 2,230.1 | 1,559.7 | 1,551.9 | 1,618.1 | 1,565.2 |
| General Administration | 93.1 | 104.8 | 108 | 112.7 | 134.6 | 234.9 | 167 | 162.3 | 167.3 | 164.2 |
| National Defense | 234.1 | 244.1 | 253.4 | 257.1 | 263.2 | 343.3 | 237.7 | 225.2 | 227.7 | 248.9 |
| Education, Science and Culture | 156.6 | 166.6 | 174.9 | 184.8 | 202.7 | 367.6 | 257.2 | 267 | 300.2 | 302.1 |
| Economic Development | 137.1 | 124.2 | 113.8 | 126.5 | 172.5 | 356.4 | 277.1 | 291.2 | 295.5 | 248.8 |
| Social Welfare | 134.2 | 143.7 | 150 | 150.2 | 157.6 | 411 | 293.3 | 262.2 | 284.4 | 280.1 |
| Community Development & Environmental Protection | 24.8 | 19.8 | 15.3 | 15.8 | 19.2 | 39.6 | 22.3 | 23.4 | 28.7 | 24.8 |
| Pensions & Survivors' Benefits | 95.9 | 108.6 | 139.5 | 139.8 | 129.3 | 195.4 | 122 | 124.3 | 125.4 | 123.1 |
| Interest payments | 56.7 | 61.2 | 58.9 | 63.5 | 80.3 | 249.6 | 151.2 | 152.2 | 144.6 | 127.1 |
| Others | 33.2 | 31.9 | 37.6 | 32.7 | 4.6 | 32.3 | 31.9 | 44.1 | 44.3 | 46.1 |

Notes: * Effective 2001, the calendar year is adopted as the fiscal year. As a transition, the fiscal year 2000 begins on July 1, 1999 and ends on Dec. 31, 2000, while the other fiscal years prior to 2000 run from July 1 of the preceding year to June 30 of the designated year.

** The figures for the year 2004 are preliminary estimates.

Sources: 1. Directorate-General of Budget, Accounting and Statistics, Executive Yuan.
2. Department of Statistics, Ministry of Finance.

launched the New Ten Projects. A total of NT\$36.5 billion has been appropriated this year for several smaller projects under the above two plans, which should contribute to the expansion of public investment.

Less Demand for Debt Financing

The demand for debt financing dropped in 2004 in line with the reduced fiscal deficit. The total amount of the fiscal deficit and debt repayment dropped to NT\$253.7 billion from the preceding year's NT\$343.6 billion. Of this amount, NT\$253.5 billion was raised through issuing government bonds and borrowing from banks, while the remaining amount was appropriated from surpluses of previous years.

Continued Increase in Debt Obligations

Despite the remarkable narrowing in the fiscal deficit, the debt obligation of the central government continued to increase in 2004. Total outstanding debt of the central government reached NT\$342.99 billion at the end of 2004, equal to a record high share of 34.84 percent of annual GDP.

The debt dependency ratio, an indicator to show the share of funds for financing government expenditure by the issuance of government bonds and borrowing from banks, fell to 16.20 percent from the previous year's 18.59 percent due to falling demand for debt financing. However, it is still double the figure in 1995. The recent widening of the fiscal deficit and the weak growth in tax revenue while the economy was expanding strongly highlight the increasingly pressing need for fiscal reform.

Public Debt of the Central Government

Unit: NT\$ Billion

| End of Fiscal Year* | Outstanding Debt | | | Outstanding Debt /GDP (%) |
|---------------------|------------------|------------|------------------------|------------------------------|
| | | Government | Borrowing from Banks** | |
| 1995 | 1,101.8 | 936.7 | 165.1 | 15.68 |
| 1996 | 1,224.9 | 1,020.4 | 204.5 | 15.94 |
| 1997 | 1,382.2 | 1,129.3 | 252.9 | 16.63 |
| 1998 | 1,381.7 | 1,078.0 | 303.7 | 15.52 |
| 1999 | 1,332.3 | 1,024.9 | 307.4 | 14.41 |
| 2000 | 2,475.0 | 1,362.8 | 1,112.2 | 17.30 |
| 2001 | 2,802.6 | 1,701.7 | 1,100.9 | 29.16 |
| 2002 | 2,892.6 | 1,957.9 | 934.7 | 30.62 |
| 2003 | 3,173.3 | 2,337.7 | 835.6 | 32.60 |
| 2004*** | 3,429.9 | 2,562.7 | 867.2 | 34.84 |

Notes: * Effective 2001, the calendar year is adopted as the fiscal year. As a transition, the fiscal year 2000 begins on July 1, 1999 and ends on Dec. 31, 2000, while the other fiscal years prior to 2000 run from July 1 of the preceding year to June 30 of the designated year.

** Including foreign debt.

***The figures for the year 2004 are preliminary estimates.

Sources: 1. Directorate-General of Budget, Accounting and Statistics, Executive Yuan.
2. Department of Statistics, Ministry of Finance.

6. Labor Market Conditions

Unemployment Rate Continued to Decline

The expansion of general economic activity during 2004 encouraged firms to hire more labor. The government also continuously promoted the *Public Service Employment Expansion Program* to help boost employment. Both factors reduced the unemployment rate. For the year 2004, the unemployment rate dropped to 4.44 percent, which was 0.55 of a percentage point lower than the year before.

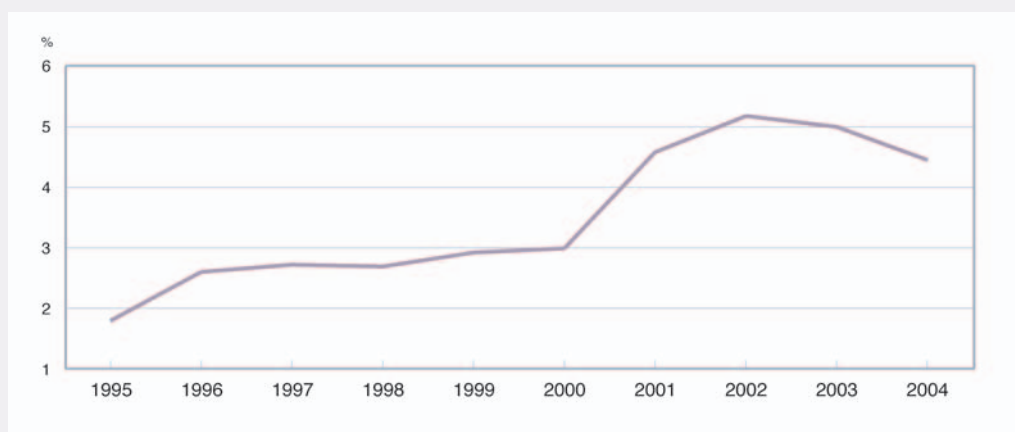
Total Employment Increased

Positively influenced by the economic recovery and the government's employment expansion plan, employment increased 2.22 percent from the year before, among which employment of white-collar, blue-collar, and sales workers grew by 4.38 percent, 0.28 percent, and 1.76 percent, respectively. The growth rate of the employment of white-collar workers was the highest since 1994. The employment of blue-collar workers declined between 1998 and 2003 as manufacturers relocated their production base overseas, mainly to China. However, the economic expansion in 2004 increased job opportunities for blue-collar workers, turning the growth rate of their employment positive.

Labor Participation Rate Rose

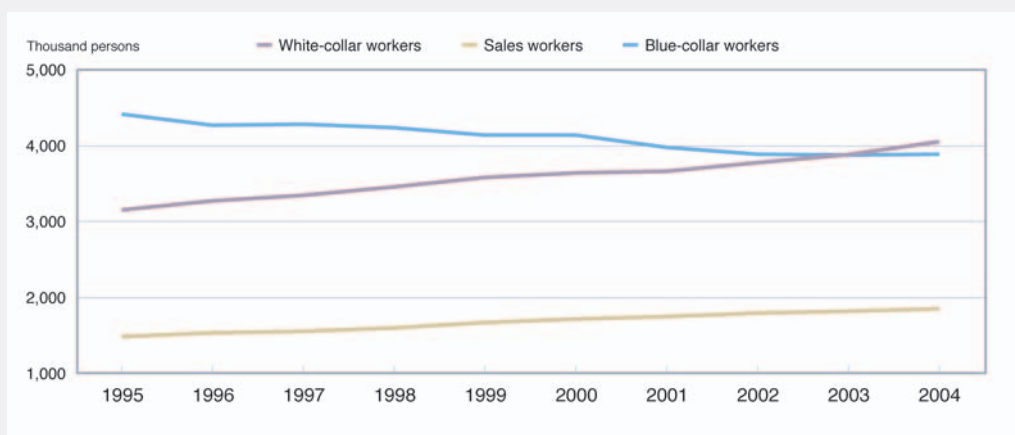
In the wake of the solid economic recovery, the overall labor participation rate increased.

Unemployment Rate



Source: *Monthly Bulletin of Manpower Statistics, Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan.*

Employment by Occupation



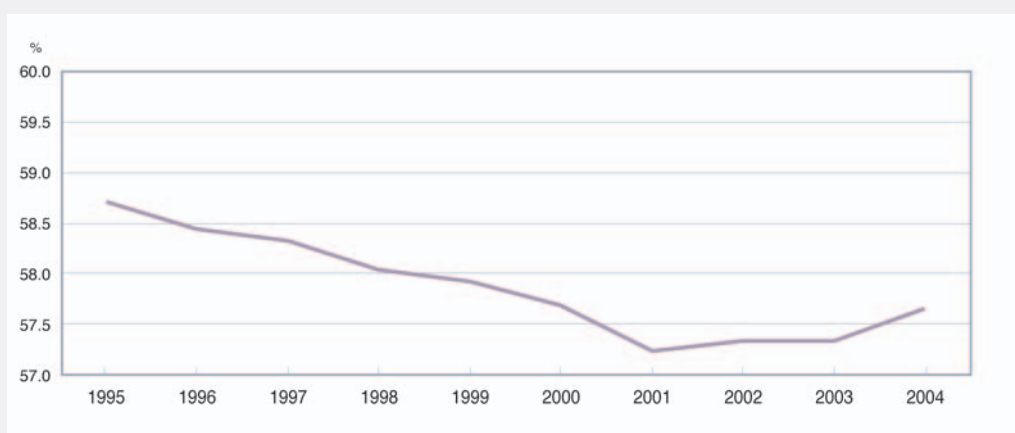
Source: Monthly Bulletin of Manpower Statistics, Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan.

The labor participation rate in 2004 was 57.66 percent, 0.32 of a percentage point higher than the year before. In terms of gender, the male labor participation rate increased slightly from 67.69 percent to 67.78 percent, while the female one increased more markedly from 47.14 percent to 47.71 percent.

Increase in Earnings of Non-agricultural Workers

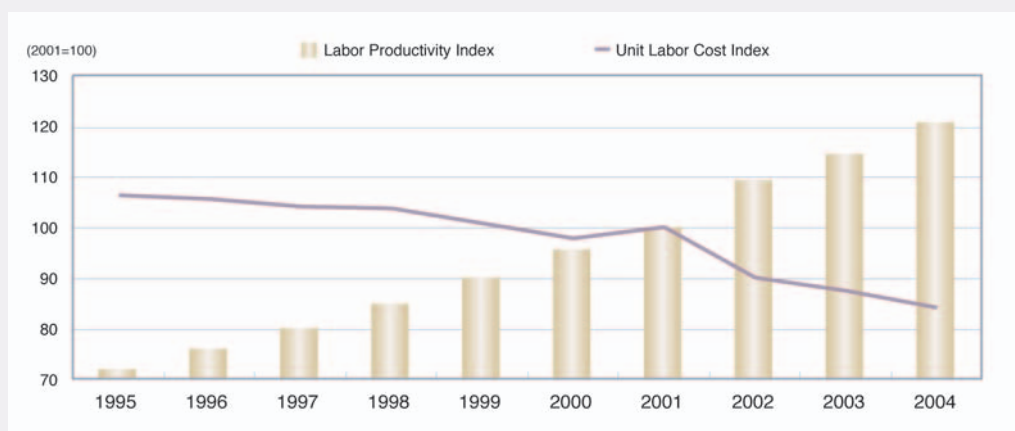
The average monthly earnings of non-agricultural sector workers, i.e. the workers hired in the industrial and services sectors increased by 1.74 percent to NT\$43,021 in 2004. The average monthly earnings (deflated by the CPI) of non-agricultural sector workers increased by 0.12 percent. The average monthly earnings of industrial workers increased by 2.34 percent and

Labor Participation Rate



Source: Monthly Bulletin of Earning and Productivity Statistics, Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan.

Labor Productivity and Unit Labor Cost Indices in the Industrial Sector



Source: Monthly Bulletin of Earning and Productivity Statistics, Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan.

real earnings by 0.71 percent. Average monthly earnings of services sector workers increased by 1.19 percent to NT\$45,064, while real earnings dropped by 0.43 percent.

Rising Labor Productivity in the Industrial Sector

As the increase in total production outpaced that in total working hours, the labor productivity index for the industrial sector rose by 5.45 percent in 2004. As the increase in total production exceeded that in total labor compensation, the index for unit labor costs in the industrial sector fell by 4.07 percent.



II. Financial Developments

- 1. Overview**
- 2. Monetary Aggregates**
- 3. Banking Sector**
- 4. Money Market**
- 5. Foreign Exchange Market**
- 6. Stock Market**
- 7. Bond Market**

II. Financial Developments

1. Overview



On the Financial Front, to prevent high oil prices from re-igniting inflation, developed countries started raising interest rates, reversing the monetary easing adopted in the previous three years. In foreign exchange markets, the U.S.'s gaping trade deficits, coupled with expectations of a renminbi revaluation, led to international capital flooding into Asia. The US dollar continually weakened, the euro broke new highs against the US dollar, and all major Asian currencies appreciated.

The Taiwan economy grew steadily, fuelling the demand for funds. This factor, in addition to banks' active promotion of their consumer finance business, resulted in loans and investments by major financial institutions growing by 8.65 percent. The expansion of bank credit, together with net capital inflows, led to an annual increase of 7.45 percent in the M2 monetary aggregate in 2004.

The continual economic expansion weighed on inflationary pressure. To curb inflationary expectations, the Bank raised the discount rate on two occasions, in October and December, guiding market rates gradually upwards. The interbank overnight call-loan rate and then trended up to 1.15 percent in December from a yearly low of 0.97 percent in May 2004. The five major domestic banks' average interest rate on one-year time deposits was 1.52 percent at the end of 2004, up by 0.12 of a percentage point from a year ago. However, long-term interest rates rose early in the year and declined afterwards.

The NT dollar hit a low of 34.199 against the US dollar on July 28 and then appreciated throughout the remainder of the year. The appreciation reflected a softening US dollar in the international market and a surge in net foreign inflows. The NT dollar stood at 31.917 against the US dollar at the end of 2004, showing an appreciation of 6.46 percent compared to the

previous year-end.

The stock market consolidated in 2004, affected by a mixture of domestic and international factors. After reaching a yearly nadir of 5,317 points on August 4, the TAIEX rose slowly over the remainder of 2004 as international stock markets rallied, Morgan Stanley Capital International Inc. (MSCI) raised Taiwan's weighting in its indices, and foreign investors sought net long positions. The TAIEX index reached 6,140 points at the end of the year, 4.23 percent higher than a year earlier.

Financial institutions generally saw their profitability improve for the year, as fee and commission income increased and funds needed to write off bad debts decreased markedly from the previous year. In addition, banks adopted a cautious attitude towards credit extension, contributing to a rise in the average capital adequacy ratio from 10.07 percent at the end of 2003 to 10.69 percent at the end of 2004. During the same period, the average non-performing loan ratio decreased from 4.33 percent to 2.78 percent. These figures clearly indicate banks' improved financial soundness.

2. Monetary Aggregates

Monetary aggregates increased markedly during 2004. The strong growth in the narrow aggregate M1B largely reflected a higher demand for transactions balances associated with the low level of interest rates and with an ongoing strengthening in economic activity.

On the strength of a substantial increase in bank credit to the private sector and considerable inflows of foreign capital, the broad aggregates M2 and M2 plus bond funds grew at annual rates of 7.45 percent and 8.14 percent, respectively, both above their respective target ceilings (target ranges were 2.5 to 6.5 percent and 4 to 8 percent) set for the year.

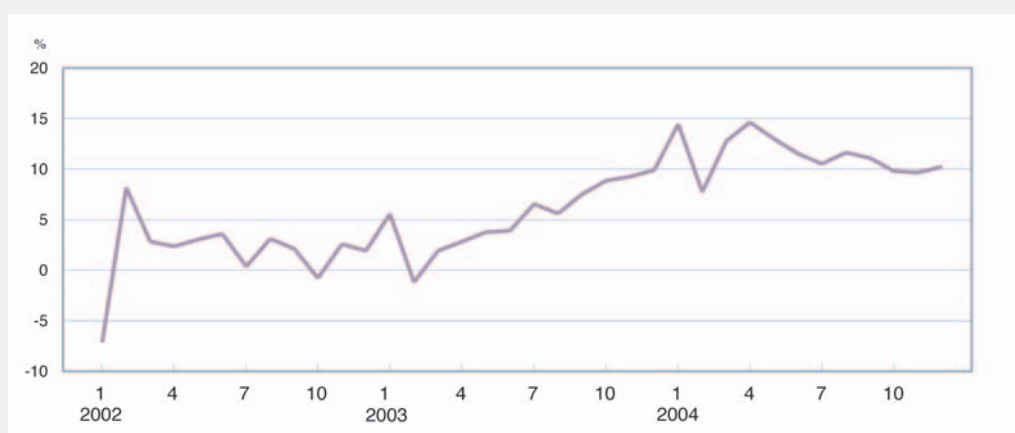
Strong Growth of Reserve Money

The average annual growth rate of reserve money rose to 11.38 percent in 2004, showing a sharp increase of 6.1 percentage points from that of the previous year. The acceleration in reserve money was mostly supported by the strong growth in net foreign assets of the Bank.

Of the various types of reserve money, currency held by the public increased by 12.44 percent and reserves held by financial institutions grew by 10.68 percent.

The annual growth rate of reserve money peaked in February, primarily reflecting the seasonal demand for currency during the Chinese Lunar New Year Holidays. In the subsequent months, except October and November, the growth rates of reserve money were higher than

Annual Growth Rates of Reserve Money



Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

10 percent. This mainly came from a pick up in the demand for funds associated with buoyant economic activity. Besides, the low cost of holding cash bolstered the public's demand for currency. As the interest rate spread between time deposits and transaction deposits remained at a low level, transaction deposits, which are subject to higher reserve requirements, increased at a relatively rapid pace and thus the demand for bank reserves also increased. All these factors contributed to the demand for reserve money.

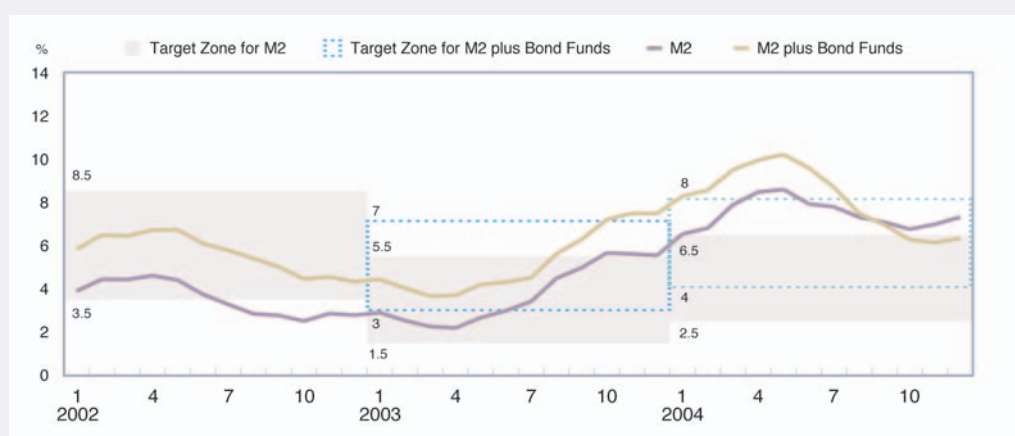
On the supply side, as Taiwan received large net inflows of foreign capital during the first and final quarters, the Bank attempted to moderate the speculative rise of the NT dollar by purchasing foreign exchange, which injected liquidity to the market. Although the Bank issued the certificates of deposit (CDs) to sterilize the resultant excess liquidity, the growth of net foreign assets of the Bank was higher than that of the CDs.

Vigorous Growth of M2 and M2 plus Bond Funds

The monetary aggregates M2 and M2 plus bond funds served as the Bank's two intermediate targets for monetary policy. After reviewing factors such as economic growth and price movements, the spread between domestic and foreign interest rates, and the impact of financial asset diversification on money demand, the Bank set the target range for M2 growth at 2.5 to 6.5 percent and for M2 plus bond funds growth at 4 to 8 percent for 2004.

The annual growth rate of M2 started to accelerate in January and peaked at 8.58 percent in May, mainly reflecting the rapid expansion in bank credit and massive foreign capital inflows.

Target Ranges and Annual Growth Rates of M2 and M2 plus Bond Funds



Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

After that, the M2 growth rates drifted downward due to foreign capital outflows and the high base of the same period last year. From August onwards, foreign capital inflows resumed. However, the M2 growth rates continued to decline as a result of the base effect and hit a low for the year in October as the foreign exchange expense for imports exceeded the foreign exchange income earned from exports. The annual growth rate of M2 edged higher in November owing to a surge of foreign capital inflows and increased to 7.31 percent in December, primarily reflecting seasonal demand for funds and banks' efforts to extend loans.

The annual growth rate of M2 plus bond funds kept rising from January to May in accordance with growth of M2 and steady demand for bond funds. The rising streak for the growth rates of M2 plus bond funds petered out as bond funds came under massive redemption pressure in the second half of July. The marked reduction in bond funds occurred as investors rushed to withdraw their money from a local securities investment company on fears of a technology company's possible default on its bond payment. This led to the local securities investment company to halt redemptions of its bond funds when it ran out of finances, which further triggered widespread redemptions affecting other bond funds. In addition, concerns over rising interest rates acted as another catalyst for investors' pulling money out of bond funds.

As investor confidence was gradually restored, the redemption pressure eased by December and helped push the annual growth rate of M2 plus bond funds a bit higher to 6.33 percent for the month.

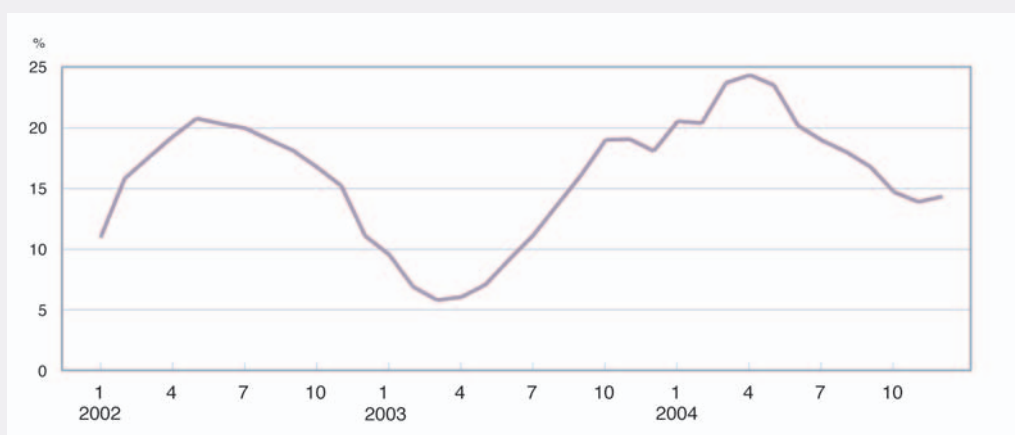
For 2004 as a whole, the annual growth rates of M2 and M2 plus bond funds both were above their respective target ceilings. This was partly attributable to the higher realized values of economic growth and price movements compared to their projected values forecast in December 2003 when setting the target ranges of M2 and M2 plus bond funds for 2004. Therefore, after taking into account such differences, the annual growth rates of M2 and M2 plus bond funds both would be within their revised target ranges.

Double-digit Growth of M1B

In 2004, the average annual growth rate of M1B reached 18.98 percent, higher than the 11.82 percent posted last year. Reflecting active stock market trading and large foreign capital inflows, the annual growth rates of M1B kept climbing and soared to a high of 24.39 percent in April. Largely because of a lackluster stock market and a reversal of capital flows, M1B growth rates followed a downward trend thereafter.

Although there was a surge in investors shifting funds out of bond funds holdings into transaction deposits from July, a higher base effect and a gradual shift of funds from transaction deposits to time deposits following the Bank's raising rates on October 1 were among the factors that pushed M1B growth rates lower. The annual growth rate of M1B hit a low of 13.90 percent for the year in November before bouncing back mildly in December.

Annual Growth Rates of M1B



Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

3. Banking Sector

Decrease in the Number of Depository Institutions

There were 398 depository institutions (including deposit money banks, the Department of Savings and Remittances of Chunghwa Post Co., and money market mutual funds) operating in Taiwan at the end of 2004, a decrease of 2 from the previous year. The decrease resulted from 1 medium business bank and 3 credit cooperative associations being taken over by domestic banks, one credit department of a farmers' association resuming its operations and 2 money market mutual funds being set up in 2004. As of the end of 2004, the number of financial holding companies remained at 14, as in the previous year.

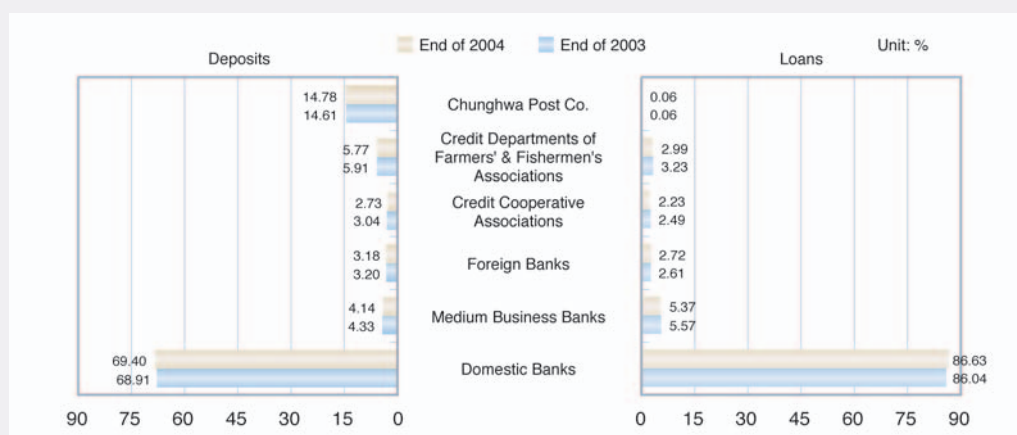
With respect to the market shares of deposits and loans by category of depository institutions at the end of 2004, domestic banks accounted for 69.40 percent of deposits and 86.63 percent of loans. Both were higher than those recorded in the previous year, mainly resulting from a medium business bank and some credit cooperative associations being merged into domestic banks. As for the foreign banks, although foreign currency deposits continued to grow, their market share of deposits dropped slightly. The share of loans, however, increased due to the marked growth in loans extended to private sectors. As for the Chunghwa Post Co. (Department of Savings and Remittances), its market share of deposits rose to 14.78 percent, and its market share of loans remained at 0.06 percent as in the previous year due to the government's restriction on its loan extension.

Number of Depository Institutions by Category

| | End of 2004 | End of 2003 | Annual Change |
|---|-------------|-------------|---------------|
| Combined Number of Main Offices | 398 | 400 | -2 |
| Domestic Banks | 45 | 45 | 0 |
| Medium Business Banks | 4 | 5 | -1 |
| Foreign Banks | 35 | 36 | -1 |
| Credit Cooperative Associations | 32 | 35 | -3 |
| Credit Departments of Farmers' and Fishermen's Associations | 279 | 278 | 1 |
| Department of Savings and Remittances of Chunghwa Post Co. | 1 | 1 | 0 |
| Money Market Mutual Funds | 2 | 0 | 2 |
| Combined Number of Branches | 5,911 | 5,923 | -12 |
| Local Branches | 5,761 | 5,772 | -11 |
| Overseas Branches | 80 | 81 | -1 |
| Offshore Banking Units | 70 | 70 | 0 |

Sources: 1. Financial Statistics Monthly, Taiwan District, the Republic of China, Central Bank of China.
2. Department of Financial Inspection, Central Bank of China.

Market Shares of Deposits and Loans by Category of Depository Institutions



Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

Sources and Uses of Funds

With respect to the sources of funds in depository institutions, owing to the continuous growth in bank lending and investments, both transaction and non-transaction deposits increased markedly. The share of transaction deposits in total sources of funds kept increasing,

Sources and Uses of Funds in Depository Institutions

| | End of 2004 | | End of 2003 | | Annual Change | |
|--------------------------------|---------------|---------------|---------------|---------------|---------------|-------------|
| | Amount | Share (%) | Amount | Share (%) | Amount | Share (%) |
| Sources: | | | | | | |
| Foreign Liabilities * | 1,390 | 5.39 | 1,071 | 4.48 | 319 | 0.91 |
| Transaction Deposits** | 6,698 | 25.98 | 5,945 | 24.85 | 754 | 1.13 |
| Non-transaction Deposits*** | 15,632 | 60.64 | 14,802 | 61.89 | 830 | -1.25 |
| Government Deposits | 748 | 2.90 | 773 | 3.23 | -26 | -0.33 |
| Borrowings from CBC | 208 | 0.81 | 277 | 1.16 | -69 | -0.35 |
| Other Items (Net) | 1,103 | 4.28 | 1,050 | 4.39 | 53 | -0.11 |
| Total | 25,778 | 100.00 | 23,917 | 100.00 | 1,861 | 0.00 |
| Uses: | | | | | | |
| Foreign Assets * | 1,532 | 5.94 | 1,571 | 6.57 | -39 | -0.63 |
| Loans | 15,868 | 61.56 | 14,302 | 59.80 | 1,566 | 1.76 |
| Portfolio Investments | 2,096 | 8.13 | 2,202 | 9.21 | -106 | -1.08 |
| Purchases of CDs Issued by CBC | 3,518 | 13.65 | 2,924 | 12.23 | 594 | 1.42 |
| Deposits with CBC | 2,764 | 10.72 | 2,918 | 12.20 | -154 | -1.48 |

Notes: * Excluding valuation changes in the exchange rate of the NT dollar against foreign currencies when calculating their annual change.

** Including checking account deposits, passbook deposits and passbook savings deposits.

***Including time deposits, time savings deposits, foreign currency deposits, postal savings deposits, non-residents NT dollar deposits, repurchase agreements, and money market mutual funds.

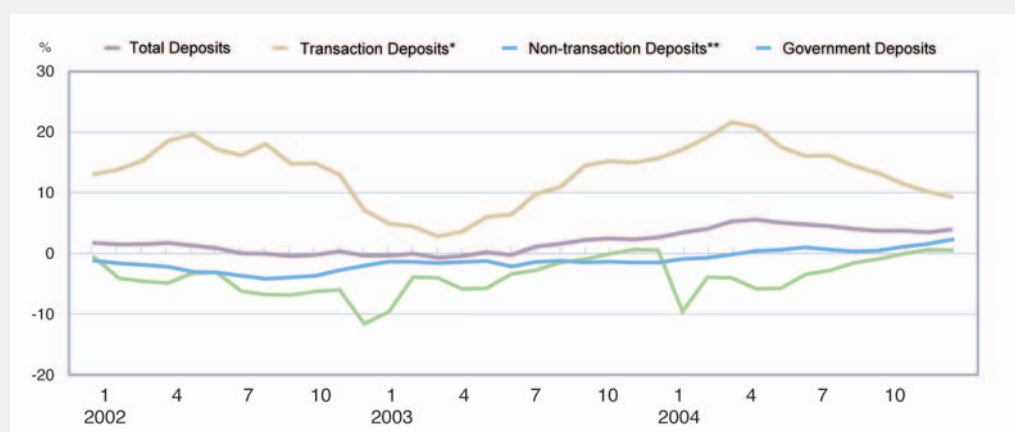
Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

whereas that of non-transaction deposits decreased slightly in 2004. With regard to the uses of funds by depository institutions, although the increments of funds raised directly from financial markets via the issues of corporate bonds and offshore bonds by enterprises shrank, the growth of loans increased significantly due to banks' aggressive attempts to expand their consumer finance business. The share of bank loans in the uses of funds rose. Portfolio investments regressed in both the amount and share of uses. However, the share of certificates of deposit issued by the Bank increased.

Uptrend in the Growth of Deposits

Total deposits of depository institutions as of the end of 2004 increased by an annual rate of 6.89 percent, higher than the rate of 5.48 percent a year earlier. All monthly growth rates of deposits exceeded 6 percent, with an annual average of 7.23 percent, significantly higher than 3.56 percent of the previous year. During the first four months of the year, bank loans and investments grew steadily and net foreign capital inflows continued. As a result, annual growth rates of deposits rose from 5.48 percent at the end of 2003 to an annual high of 8.64 percent in April. From May to July, foreign capital exhibited net outflows, leading to a decline in deposit growth. The decline persisted in August and September to reach an annual low of 6.58 percent due to the high bases of the previous year. From October onwards, net foreign capital inflows resumed, banks actively expanded consumer finance, and bank loans and investments grew further. Under these conditions, annual growth rates of deposits rebounded to 6.89 percent in December. In October 2004, the first domestic money market mutual fund

Annual Growth Rate of Deposits by Category



Notes: * Including checking account deposits, passbook deposits and passbook savings deposits.

** Including time deposits, time savings deposits, foreign currency deposits, postal savings deposits, non-residents NT dollar deposits, repurchase agreements, and money market mutual funds.

Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

was established. Because of their high convertibility and substitutability for bank deposits, money market mutual funds are included in time deposits of depository institutions.

In terms of the different types of deposits, the growth rates of transaction deposits trended upwards and then downwards over the course of the year. During the first three months of the year, transaction deposits growth rates increased from 19.75 percent at the previous year-end to 26.27 percent in March, the highest rate of the year. The increase was boosted by continuous net foreign capital inflows to the local stock market. From May onwards, transaction deposit growth rates dropped consecutively, affected by net foreign capital outflows, to record 20.12 percent in June. In July, massive redemptions of bond funds saw funds shifted to transaction deposits, pushing up their growth rate to 20.21 percent. Thereafter, due to the high bases of the previous year, the upward trend was reversed to hit the annual low of 12.68 percent in December. At the end of the year, the share of transaction deposits in total deposits rose from the previous year's 27.52 percent to 29.02 percent.

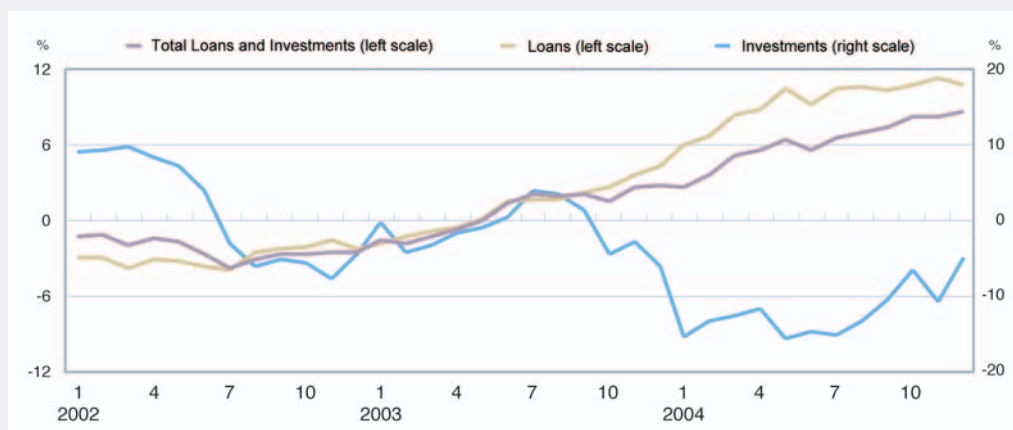
The growth rate of non-transaction deposits (including money market mutual funds) increased sharply from 0.79 percent at the end of 2003 to 5.11 percent at the end of 2004, while their share in total deposits decreased from 68.90 percent to 67.74 percent during the same period. Funds were shifted to non-transaction deposits because of the lackluster stock market and the increased interest rate spread between demand and time deposits, as banks raised time deposit rates from October onwards. In terms of different types of non-transaction deposits, the growth rate of time deposits returned to positive territory of 7.25 percent at the end of 2004 from negative 5.25 percent a year earlier. In addition, during the same period the growth rate of time savings deposits edged up from 0.30 percent to 1.26 percent. As for postal savings deposits, the growth rate rose from 1.70 percent to 6.82 percent. The growth rate of foreign currency deposits slightly increased from 12.36 percent to 12.88 percent. There were altogether 2 money market mutual funds with a total amount of NT\$1.5 billion at the end of the year.

Government deposits in depository institutions contracted 3.31 percent at the end of 2004 from a growth of 3.09 percent at the previous year-end. The ratio of government deposits to total deposits also declined from 3.58 percent to 3.24 percent.

Increasing Growth in Loans and Investments

Boosted by the significant domestic economic recovery and banks' aggressive promotion of consumer finance business, the annual growth rate of loans and investments continued to increase to 8.65 percent at the end of the year. Loans posted an annual growth rate of 10.71

Annul Growth Rate of Loans and Investments

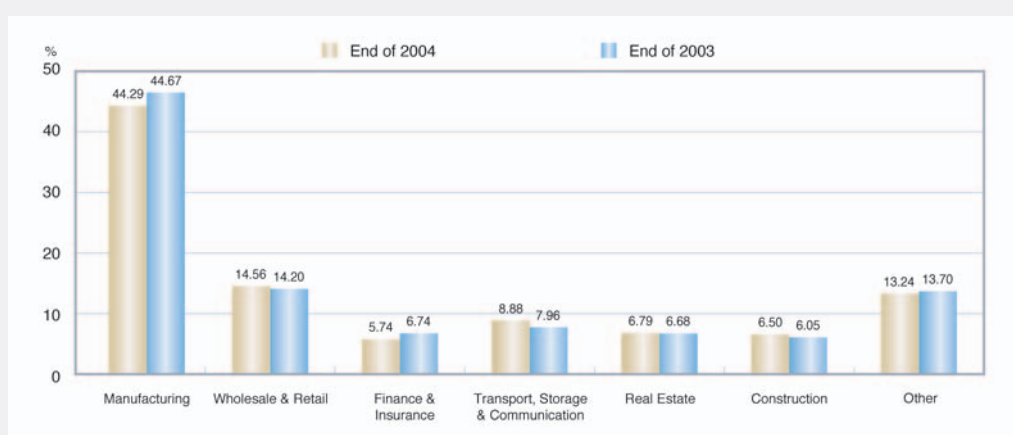


Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

percent at the year-end, compared to the 4.40 percent recorded a year earlier. The annual growth rate of investments rose to negative 4.81 percent from negative 6.15 percent of the previous year.

Loans extended to private enterprises and individuals accounted for 85.05 percent of total loans at the end of 2004, higher than the 83.39 percent recorded a year earlier. The share of loans extended to government agencies to total loans decreased to 12.08 percent from the previous year-end's 13.57 percent, mainly due to the central government's repayment of the loans contracted by the former Taiwan provincial government. The share of loans to public enterprises dropped from 2003's 3.04 percent to 2.87 percent at the end of 2004.

Composition of Loans by Industry



Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

Regarding the composition of domestic banks' loans by industry, due to the domestic economic recovery and the increasing demand for funds, outstanding loans to the manufacturing industry increased, while its share fell to 44.29 percent at the year-end from the previous year-end's 44.67 percent. Some securities firms raised funds directly from financial markets, replacing part of their borrowings from banks. Thus, the share of loans extended to the financial and insurance industries declined from the previous year-end's 6.74 percent to 5.74 percent. The revival in the real estate market triggered an increase in loans extended to the real estate and construction industries, with the share climbing up from the previous year-end's 6.05 percent and 6.68 percent, to 6.50 percent and 6.79 percent, respectively. Loans to the retail and wholesale industries continued to expand as well.

With regard to consumer loans, because of banks' aggressive attempts to expand the scope of the consumer finance business, consumer loans of domestic banks continued to trend upward and recorded an increase of NT\$856.1 billion or 18.03 percent from a year earlier.

With regard to loans by currency, the share of foreign currency loans to total loans rose to 3.53 percent at the end of 2004 from 3.50 percent at the previous year-end. The increase was mainly due to the strengthening of external trade and the rising expectations of the NT dollar's appreciation from the fourth quarter onwards. The corresponding share of NT dollar loans to total loans therefore contracted slightly from 96.50 percent to 96.47 percent. As for the NT dollar loan-to-deposit ratio, it increased to 68.76 percent at the end of 2004 from 66.39 percent recorded at the end of the previous year.

With respect to the composition of investments of depository institutions, government bonds accounted for the largest share, followed by commercial paper. In the case of domestic banks, government bonds accounted for 48.75 percent of their total investments, up from the previous year-end's 38.84 percent. This was mainly due to the increased issue of government bonds for financing the fiscal deficit, along with banks' efforts in reducing excess liquidity and the overall risk of their investments. The ratio of investment on commercial paper to their total investment dropped significantly to 11.41 percent from 19.15 percent a year earlier, primarily reflecting the decline in commercial paper issued by local firms.

Increased Share of Intermediate Financing

The total amount of funds raised during the year by the non-financial sector, comprising enterprises, households and the government as a whole, showed a marked increase from the previous year's NT\$1,677.1 billion to NT\$2,129.4 billion, the highest figure since 1998. With regard to the composition of the sources of funds, due to the significant increase in loans and

Intermediate Financing vs. Market Financing*

Unit: NT\$ Billion

| Year | Total Funds Raised (3)=(1)+(2) | Intermediate Financing(1) | | | | Market Financing(2) | |
|------|-----------------------------------|---------------------------|---------|-------------|-------------------------|---------------------|---------------------|
| | | Amount | | | Share (%) (1)/(3)(%) | Amount | Share (2)/(3)(%) |
| | | | Loans | Investments | | | |
| 1995 | 1,442.4 | 1,304.9 | 1,033.8 | 271.1 | 90.47 | 137.5 | 9.53 |
| 1996 | 1,625.9 | 1,372.6 | 721.4 | 651.2 | 84.42 | 253.3 | 15.58 |
| 1997 | 2,278.0 | 1,670.2 | 1,548.0 | 122.2 | 73.32 | 607.8 | 26.68 |
| 1998 | 1,935.4 | 1,404.4 | 886.5 | 517.9 | 72.56 | 531.0 | 27.44 |
| 1999 | 1,289.1 | 1,041.3 | 954.0 | 87.3 | 80.78 | 247.8 | 19.22 |
| 2000 | 1,377.1 | 1,203.2 | 1,053.2 | 150.0 | 87.37 | 173.9 | 12.63 |
| 2001 | 665.2 | 594.5 | 200.6 | 393.9 | 89.38 | 70.7 | 10.62 |
| 2002 | 807.5 | 424.8 | 71.7 | 353.1 | 52.61 | 382.7 | 47.39 |
| 2003 | 1,677.1 | 716.0 | 711.5 | 4.5 | 42.69 | 961.1 | 57.31 |
| 2004 | 2,129.4 | 1,825.2 | 1,579.0 | 246.2 | 85.71 | 304.2 | 14.29 |

Notes: * Measured in terms of flow data.

(1) Refers to loans and investments made by depository institutions, investment and trust companies, and life insurance companies, after taking into account their reclassifying of non-accrual loans and written-off bad loans.

(2) Refers to the total amount of new issues of various marketable securities, including government bonds, corporate bonds and stocks, offshore bonds and depository receipts, short-term bills and asset-backed securities directly held by the non-financial sectors.

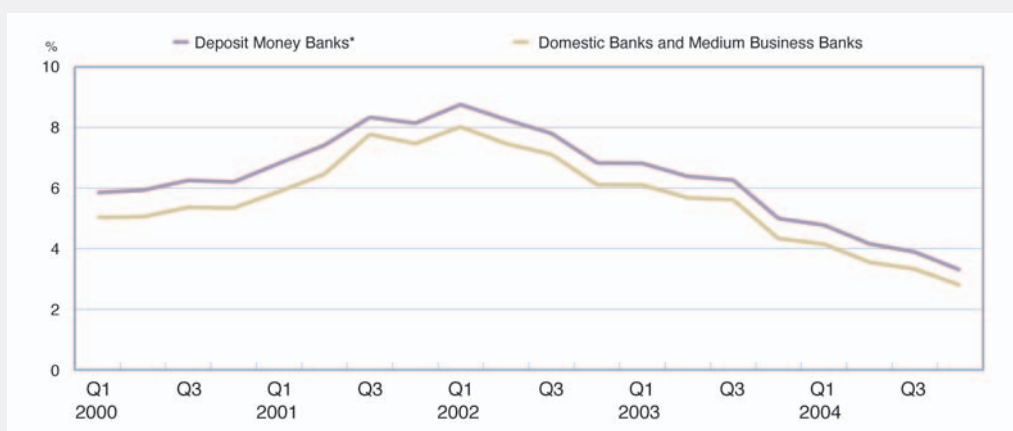
Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

investments, the share of intermediate financing, that is, those borrowed from financial institutions including depository institutions, investment and trust companies and life insurance companies, rose from 42.69 percent in 2003 to 85.71 percent in 2004. Conversely, the share of market financing, i.e., the funds raised directly from financial markets via the issues of various marketable securities by issuers to the general public without the involvement of financial institutions, decreased from 57.31 percent to 14.29 percent. The decline was mainly due to the decreasing issues of corporate bonds and offshore bonds.

Marked drop in the Non-performing Loan Ratio

With the efforts made by deposit money banks to speed up the disposal of non-performing loans (NPL), the book value of accumulated NPLs sold recorded an increase of NT\$181.5 billion during the year 2004. As local banks kept writing off bad loans with funds from their own earnings in order to improve their financial health and risk tolerance, the NPL ratio significantly declined during the year. The average NPL ratio of deposit money banks as a whole trended down quarter by quarter during 2004. As of the end of 2004, the ratio had declined to 3.28 percent from 5.00 percent recorded a year earlier. In the mean time, the corresponding NPL ratio for domestic banks and medium business banks combined (including their offshore banking units and overseas branches) also dropped from 4.33 percent at the end of the previous year to a low of 2.79 percent at the end of 2004.

Non-performing Loan Ratios of Banking Sector



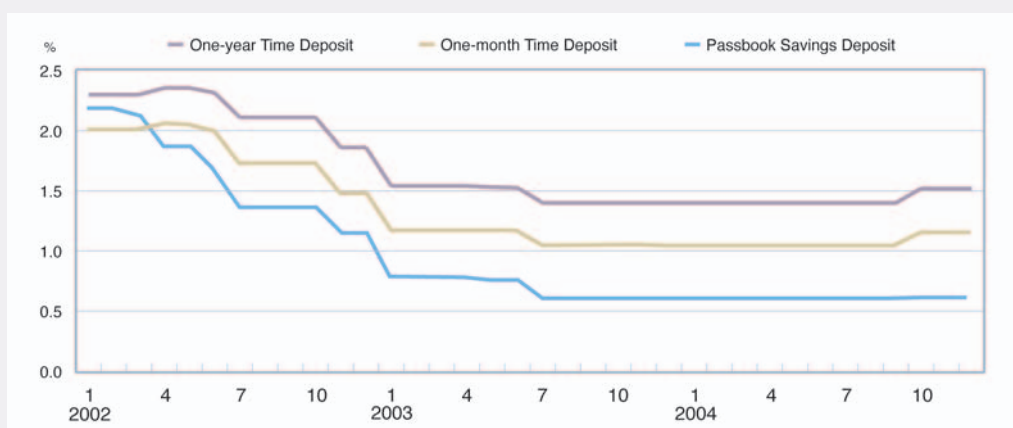
Note: * Including domestic banks, medium business banks, foreign banks, credit cooperatives and credit departments of farmers' and fishermen's associations.

Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

Increase in Bank Interest Rates

Banks' posted interest rates remained largely flat before October, and then began to rise, affected by an increase in the Central Bank's discount rate. In the case of the interest rates of the five major domestic banks, the average fixed rates on one-month and one-year time deposits were 1.05 percent and 1.40 percent, respectively, at the end of 2003. Both remained unchanged until the end of September 2004, and then increased to 1.15 percent and 1.52 percent at the end of 2004. The base lending rates of the five major domestic banks were

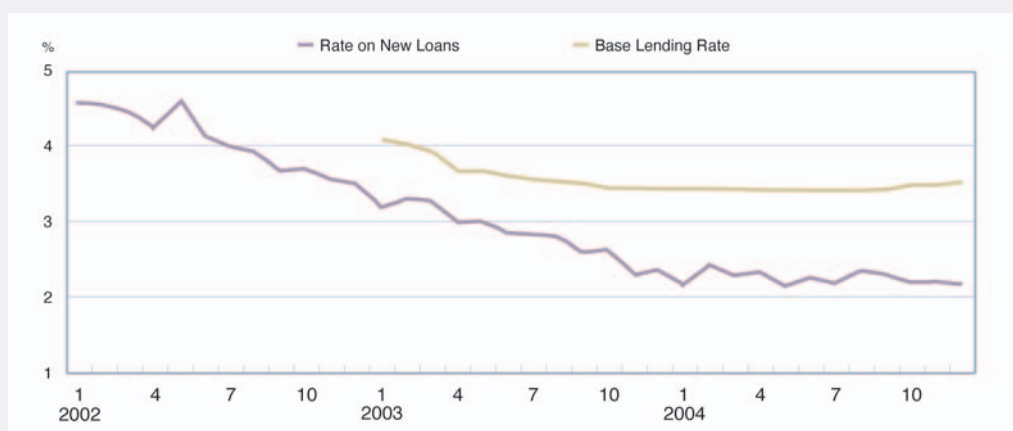
The Average Deposit Rates of the Five Major Domestic Banks*



Note: * The five major domestic banks include Bank of Taiwan, Taiwan Cooperative Bank, First Commercial Bank, Hua Nan Commercial Bank and Chang Hwa Commercial Bank.

Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

The Average Lending Rate of the Five Major Domestic Banks*



Note: * The five major domestic banks include Bank of Taiwan, Taiwan Cooperative Bank, First Commercial Bank, Hua Nan Commercial Bank and Chang Hwa Commercial Bank.

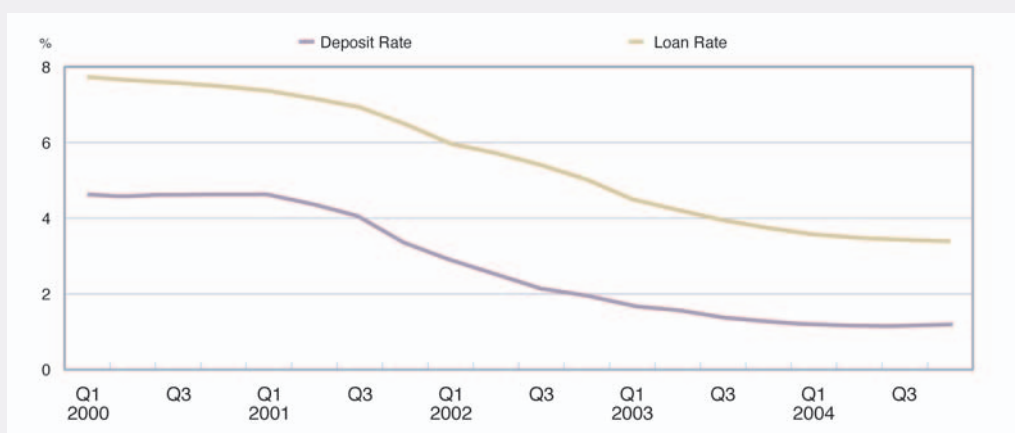
Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

lowered to 3.41 percent at the end of August, as compared with the 3.43 percent posted at the end of 2003, then increased to 3.52 percent at the end of December.

Against the backdrop of easy funding conditions and pursuant to the government's financial reform plan of lowering NPL ratios, banks expanded loans to government agencies and enterprises with good credit records at a lower rate. In addition, the government also implemented various policy-based loans with preferential rates. As a result, the weighted average rates on new loans of the five major domestic banks were between 2.14 percent and 2.80 percent throughout the year and hit a record low of 2.14 percent in May. The weighted average lending rate for the whole year dropped by 0.56 of a percentage point, from 2.80 percent in the previous year to 2.24 percent. The weighted average lending rate excluding the government's loans was 2.34 percent for the year as a whole.

The weighted average rates on both deposits and loans of domestic banks were lower in 2004 than in the previous year. The weighted average deposit rate continued to fall to 1.14 percent in the third quarter from 1.27 percent of the fourth quarter 2003, and then rose to 1.18 percent in the fourth quarter 2004. The weighted average deposit rate for the whole year was 1.17 percent, lower than the 1.47 percent recorded in the previous year. The weighted average lending rate declined from 3.74 percent to 3.39 percent between the fourth quarters of 2003 and 2004. The lending rate for the whole year declined from the previous year's 4.10 percent to 3.47 percent. Because the declines in lending rates were more rapid than in deposits rates during the first three quarters, the interest spread between deposits and loans continuously shrank. During the fourth quarter, deposits rates increased while lending rates dropped further,

The Weighted Average Interest Rates of Domestic Banks



Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

the interest spread between deposits and loans shrank to 2.21 percentage points in the fourth quarter, less than the 2.47 percentage points recorded in the fourth quarter of 2003.

Marked Improvement in Profitability

The profitability of banks increased significantly during 2004. The combined pre-tax earnings of all depository institutions grew by NT\$107.0 billion to NT\$193.8 billion, a marked improvement when compared with that of the previous year. Of this amount, the pre-tax earnings of domestic banks and medium business banks combined increased by NT\$104.9 billion to NT\$155.3 billion.

This improved earnings performance was primarily attributable to banks' lower provisions for bad loans as nonperforming loans were reduced, as well as increased fee income after banks started charging fees for various banking services. The pre-tax profit of foreign banks increased by NT\$1.8 billion, mainly due to gains from foreign exchange business. As for credit cooperative

Profitability of Depository Institutions by Category

Unit: NT\$ Billion

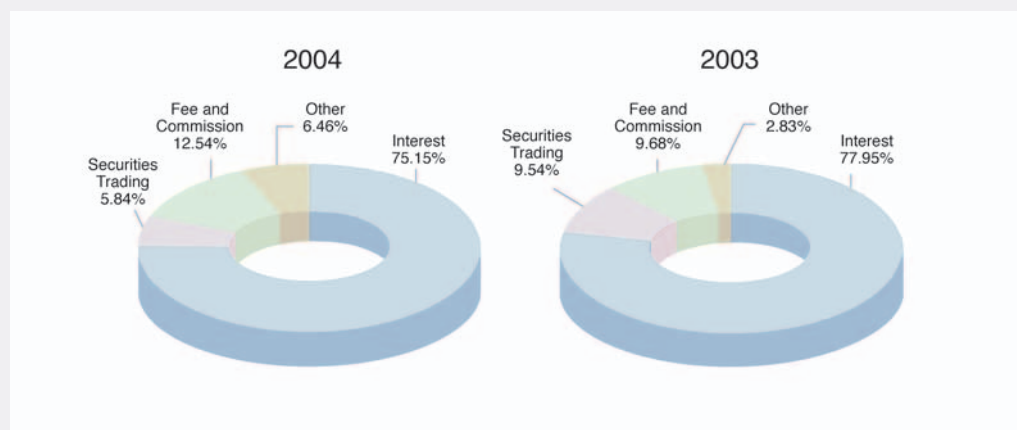
| | Profit before Tax | | | Return on Assets (%)* | | | Return on Equity (%)** | | |
|---|-------------------|------|---------------|-----------------------|-------|---------------|------------------------|-------|---------------|
| | 2004 | 2003 | Annual Change | 2004 | 2003 | Annual Change | 2004 | 2003 | Annual Change |
| Domestic Banks and Medium Business Banks | 155.3 | 50.4 | 104.9 | 0.61 | 0.22 | 0.39 | 9.79 | 3.49 | 6.30 |
| Foreign Banks | 22.8 | 21.0 | 1.8 | 1.18 | 1.31 | -0.13 | 37.45 | 38.06 | -0.61 |
| Credit Cooperative Associations | 1.2 | -2.0 | 3.2 | 0.17 | -0.29 | 0.46 | 2.87 | -4.87 | 7.74 |
| Credit Departments of Farmers' and Fishermen's Associations | 2.1 | 0.0 | 2.1 | 0.15 | 0.00 | 0.15 | 2.77 | -0.02 | 2.79 |
| Departments of Savings and Remittances of Chunghwa Post co. | 12.4 | 17.4 | -5.0 | 0.36 | 0.52 | -0.16 | 24.43 | 36.95 | -12.52 |
| Total Depository Institutions | 193.8 | 86.8 | 107.0 | 0.59 | 0.29 | 0.30 | 10.67 | 5.22 | 5.45 |

Notes: * Return on Assets = Profit before Tax / Total Assets

** Return on Equity = Profit before Tax / Net Worth

Source: Department of Financial Inspection, Central Bank of China.

Composition of Operating Income of Domestic Banks and Medium Business Banks



Source: Department of Financial Inspection, Central Bank of China.

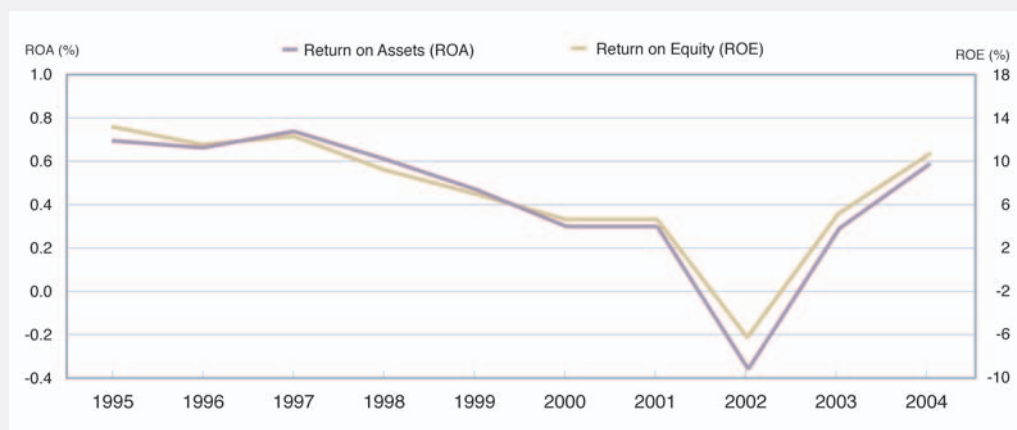
associations and the credit departments of farmers' and fishermen's associations, pre-tax earnings returned to positive territory because of a marked decrease in provisions for bad loans. However, owing to a considerable decrease in the revaluation gains from equity investments, the pre-tax profit of the Chunghwa Post Co. dropped, despite a decline in business and administrative costs.

In terms of the components of operating income of domestic banks and medium business banks combined, owing to successive decreases in banks' interest rates, the share of interest income to total operating income declined from the previous year's 77.95 percent to 75.15 percent. Affected by increases in fee income after banks started charging fees for various banking services, the share of fee and commission income rose from 9.68 percent to 12.54 percent this year. The share of earnings from securities trading fell to 5.84 percent from the 9.54 percent in the previous year, mainly due to a decline in gains from bills trading as interest rates turned to rise in the second half of the year.

Further Increase in Both ROA and ROE

The average return on assets (ROA) and return on equity (ROE) for all depository institutions rose to 0.59 percent and 10.67 percent in 2004, respectively, from 0.29 percent and 5.22 percent recorded a year earlier. Except for foreign banks and the Chunghwa Post Co., ROEs and ROAs for all other depository institutions were higher than those of the previous year. Foreign banks remained leaders in terms of ROEs and ROAs.

The Return on Assets and Equity of Depository Institutions



Source: Department of Financial Inspection, Central Bank of China.

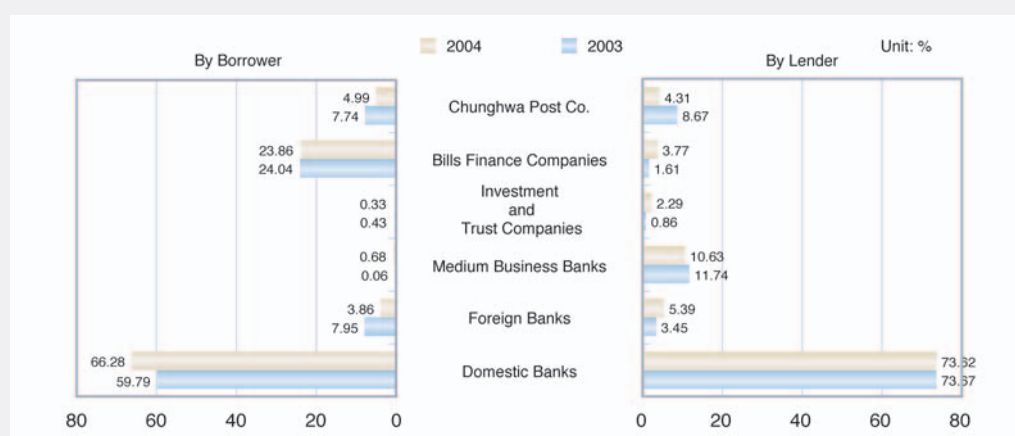
4. Money Market

Increase in Interbank Call-loan Market Transactions

Demand for funds gradually regained momentum as economic activity picked up throughout 2004, while the supply of funds was mainly affected by cross-border capital flows and bond fund withdrawals. In the first quarter, funding conditions in the banking system remained easy as a result of massive foreign capital inflows. However, in the second quarter, as the NT dollar started to depreciate in late April against the US dollar over expectations of Fed rate hikes, and the stock market weakened following mainland China's macroeconomic tightening, sharp increases in oil prices and political uncertainties surrounding Taiwan in the wake of the presidential election, foreign capital turned to a net outflow. In the second half of the year, funding conditions tightened slightly as bond funds faced tremendous withdrawals due to certain corporate bond defaults. For the year as a whole, with Taiwan's economy experiencing a recovery and banks expanding consumer finance, the increased demand for funds resulted in a rebound in the interbank call-loan market. The total annual turnover in the interbank call-loan market was NT\$10,199.4 billion, representing an increase of 16.21 percent compared to the previous year.

In terms of borrowers in the interbank call-loan market, domestic banks were the largest borrower during the year, accounting for 66.28 percent of total trading, a 6.49 percentage-

Composition of Interbank Call-Loan Market by Participant



point rise from the previous year. They were followed by bills finance companies, Chunghwa Post Co. and foreign banks, with shares of 23.86 percent, 4.99 percent and 3.86 percent, respectively. Among these borrowers, the share of foreign banks declined by 4.09 percentage points as foreign banks received sufficient NT dollar funds through large amounts of non-residents' NT dollar deposits and foreign currency swaps in the first half of the year. The share of bills finance companies dropped as well because their corporate clients shifted from the bills market to the banks for fund raising.

With regard to lenders, domestic banks continued to be the largest supplier of funds, accounting for 73.62 percent of total transactions, a slight decrease from a year ago. Following domestic banks were medium business banks, foreign banks and Chunghwa Post Co., with respective shares of 10.63 percent, 5.39 percent and 4.31 percent.

Regarding the maturities of interbank call loans, overnight interbank call loans remained the most actively traded in the market with a predominant share of 62.66 percent. Second to them were those with maturities of 1 week and 2 weeks, respectively accounting for 22.90 percent and 10.51 percent. Trading of those with maturities ranging from 2 months to 6 months accounted for a negligible share of 0.09 percent.

Less Active Short-term Bills Market

In 2004, new issues of short-term bills totaled NT\$6,888.8 billion, 8.7 percent less than in the previous year. Of new issues of short-term bills, commercial paper continued to account for

Short-term Bills Market

Unit: NT\$ Billion

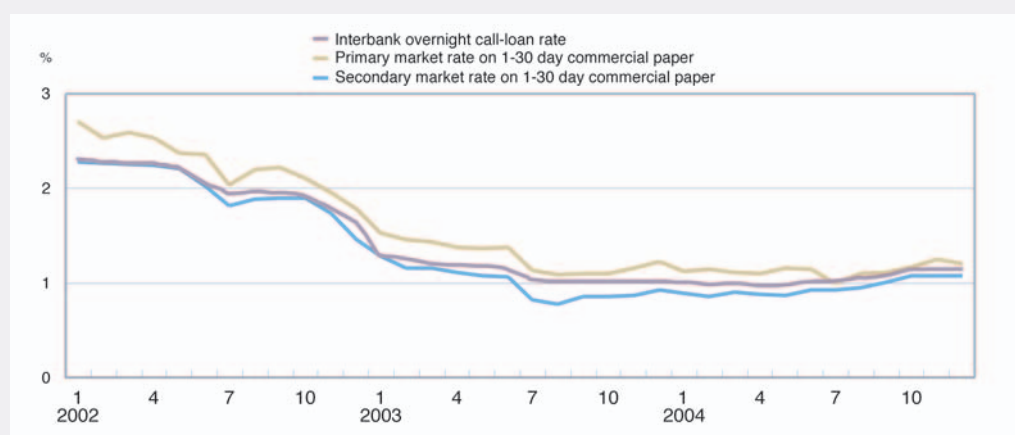
| Year | Total | | | Treasury Bills | | | Commercial Paper | | | Bankers' Acceptances | | | Negotiable Certificates of Deposit | | |
|-------------------|----------|------------|----------------------|----------------|------------|----------------------|------------------|------------|----------------------|----------------------|------------|----------------------|------------------------------------|------------|----------------------|
| | Issue | Redemption | Year-end Outstanding | Issue | Redemption | Year-end Outstanding | Issue | Redemption | Year-end Outstanding | Issue | Redemption | Year-end Outstanding | Issue | Redemption | Year-end Outstanding |
| 1995 | 9,093.7 | 8,870.9 | 1,406.9 | 15.0 | 25.0 | 5.0 | 6,140.5 | 6,029.4 | 647.5 | 1,707.3 | 1,625.3 | 274.2 | 1,230.9 | 1,191.3 | 480.2 |
| 1996 | 9,643.6 | 9,300.3 | 1,750.2 | 98.7 | 88.7 | 15.0 | 6,773.4 | 6,325.6 | 1,095.3 | 1,816.5 | 1,822.4 | 268.4 | 955.0 | 1,063.7 | 371.6 |
| 1997 | 11,348.9 | 11,056.8 | 2,042.2 | 57.3 | 52.3 | 20.0 | 8,872.1 | 8,670.8 | 1,296.5 | 1,018.7 | 1,155.2 | 131.9 | 1,400.7 | 1,178.5 | 593.8 |
| 1998 | 13,691.2 | 13,347.5 | 2,386.0 | 55.0 | 20.0 | 55.0 | 11,497.9 | 11,029.9 | 1,764.5 | 486.6 | 581.4 | 37.2 | 1,651.7 | 1,716.2 | 529.3 |
| 1999 | 10,676.5 | 11,029.2 | 2,033.3 | 315.0 | 220.0 | 150.0 | 9,390.6 | 9,663.8 | 1,491.3 | 66.0 | 90.0 | 13.2 | 904.9 | 1,055.4 | 378.8 |
| 2000 | 10,324.6 | 10,552.9 | 1,805.0 | 95.0 | 220.0 | 45.0 | 9,032.7 | 9,267.8 | 1,256.3 | 46.2 | 49.2 | 10.2 | 1,150.8 | 1,036.0 | 493.5 |
| 2001 | 9,901.5 | 10,218.8 | 1,487.8 | 85.0 | 80.0 | 50.0 | 8,926.8 | 9,080.6 | 1,102.4 | 36.1 | 38.1 | 8.3 | 853.6 | 1,020.1 | 327.1 |
| 2002 | 8,378.1 | 8,556.4 | 1,309.5 | 180.0 | 50.0 | 180.0 | 7,525.1 | 7,757.5 | 870.1 | 40.1 | 40.5 | 7.9 | 632.9 | 708.4 | 251.5 |
| 2003 | 7,547.7 | 7,662.8 | 1,194.3 | 60.0 | 180.0 | 60.0 | 6,815.1 | 6,876.3 | 808.8 | 34.5 | 35.6 | 6.8 | 638.1 | 570.9 | 318.7 |
| 2004 | 6,888.8 | 6,766.7 | 1,316.4 | 130.9 | 60.0 | 130.9 | 5,642.7 | 5,676.0 | 775.5 | 35.2 | 34.4 | 7.6 | 1,080.0 | 996.3 | 402.4 |
| 2003-2004 Changes | -658.9 | -896.1 | 122.1 | 70.9 | -120.0 | 70.9 | -1,172.4 | -1,200.3 | -33.3 | 0.7 | -1.2 | 0.8 | 441.9 | 425.4 | 83.7 |
| Growth rate (%) | -8.73 | -11.69 | 10.22 | 118.17 | -66.67 | 118.17 | -17.20 | -17.46 | -4.12 | 2.03 | -3.37 | 11.76 | 69.25 | 74.51 | 26.26 |

Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

the lion's share of 81.91 percent. Second to it were negotiable certificates of deposit, with a share of 15.68 percent. Treasury bills and bankers' acceptances made up marginal shares of 1.90 percent and 0.51 percent, respectively. Compared to the previous year, total new issues of short-term bills declined by 8.73 percent. Although the issues of negotiable certificates of deposit, Treasury bills and bankers' acceptances increased slightly, the issues of commercial paper declined significantly. The decline in the issues of commercial paper was mainly due to enterprises shifting to bank credit for fund raising as banks actively promoted their loan businesses and bank lending rates dropped to a record low in 2004. On the other hand, as banks increased their fund raising when expanding loan business, and some investors shifted their money from bond funds to negotiable certificates of deposit, negotiable certificates of deposit issued by banks in 2004 increased over the previous year. The Ministry of Finance (MOF) increased the issues of Treasury bills to meet short-term funding needs. As of the end of December 2004, total outstanding bills amounted to NT\$1,316.4 billion, 10.22 percent higher than the previous year-end.

In the secondary market, total turnover of short-term bills increased by 1.98 percent to NT\$48,829 billion. Of the total transactions, commercial paper still made up the largest share of 76.54 percent, though slightly lower than in 2003. It was followed by negotiable certificates of deposit with a share of 18.73 percent, which was higher than in 2003. Treasury bills accounted for 4.63 percent, a decline from the previous year. With respect to market participants, private enterprises remained the largest player in the market with a share of 42.09 percent, followed by banks with a share of 27.19 percent.

Money Market Interest Rates



Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

Money Market Rates Rebounded from Record Lows

In the first half of 2004, funding conditions in the domestic market remained easy due to the net inflow of foreign capital. Accordingly, the interbank overnight call-loan rate steadily declined from the beginning of the year, reaching a record low in May, while other major money market rates followed suit and also fell to the record lows. Thereafter, funding conditions tightened as foreign capital turned into a net outflow. Furthermore, bond funds witnessed considerable withdrawals in the second half of the year, contributing to the relatively tight funding condition. The Bank raised discount rates by 25 and 12.5 basis points in early October and late December, respectively, to ease the rise of inflationary expectations. In accordance with tighter funding conditions and the Bank's policy actions, the downward trend of money market rates had been reversed since May.

The above trend was reflected in the interbank overnight call-loan rate, which dropped from 1.03 percent of the previous year-end to a record low of 0.97 percent in May and gradually rose to 1.15 percent at the year-end. Over the same period, the secondary market rate on commercial paper with maturities of 1 to 30 days, declined from 0.93 percent to 0.87 percent between the previous year-end and May and then stepped up to 1.08 percent at the year-end. The average issuing rate on commercial paper with maturities of 1 to 30 days kept dropping during the first four months, rebounded slightly in May and June, then declined to the record low level of 0.99 percent in July, and moved upward to 1.20 percent at the year-end.

In 2004, measured on a daily average basis, the interbank overnight call-loan rate averaged 1.06 percent, representing a 0.04-percentage-point decrease from a year earlier. The average issuing rate and secondary market rate of commercial paper with maturities of 1 to 30 days also declined from 1.28 percent and 1.00 percent to 1.13 percent and 0.95 percent, respectively.

5. Foreign Exchange Market

Moderate Appreciation of the NT\$/US\$ Exchange Rate

Due to an increase in the US trade deficit, a recovery of the Japanese economy, coupled with foreign capital inflows to the Taiwan stock market, the NT\$/US\$ exchange rate appreciated from 33.976 at the beginning of 2004 to 32.798 by mid-April. In late April, the NT dollar started to depreciate, caused by the risk arising from China's macroeconomic tightening, expectations of rising US interest rates, and higher oil prices. The NT dollar declined to 34.199 against the US dollar on July 28, the lowest level of the year. After the middle of August, with the US trade deficit reaching historic highs, international funds returned to Asian countries. Consequently, the oversupply of foreign exchange led the NT dollar to appreciate. In December, due to further weakening of the US dollar, and the devastating tsunami in South and Southeast Asia on December 26, foreign funds flowed to Northeast Asia. The NT dollar finished 2004 at a yearly high of 31.917 against the US dollar.

Compared with the rate of 33.978 registered at the end of 2003, the NT dollar appreciated by 6.46 percent against the US dollar in 2004. On a daily average basis, the NT\$/US\$ exchange rate for 2004 was 33.422, representing an appreciation of 2.98 percent when compared with the previous year.

With respect to other major currencies, the NT dollar appreciated against the Japanese yen by 1.68 percent and depreciated against the euro by 1.15 percent, between the end of 2003 and 2004. When based on the trade-weighted average exchange rate against major

NT Dollar Spot Exchange Rate



Source: Taipei Forex Inc.

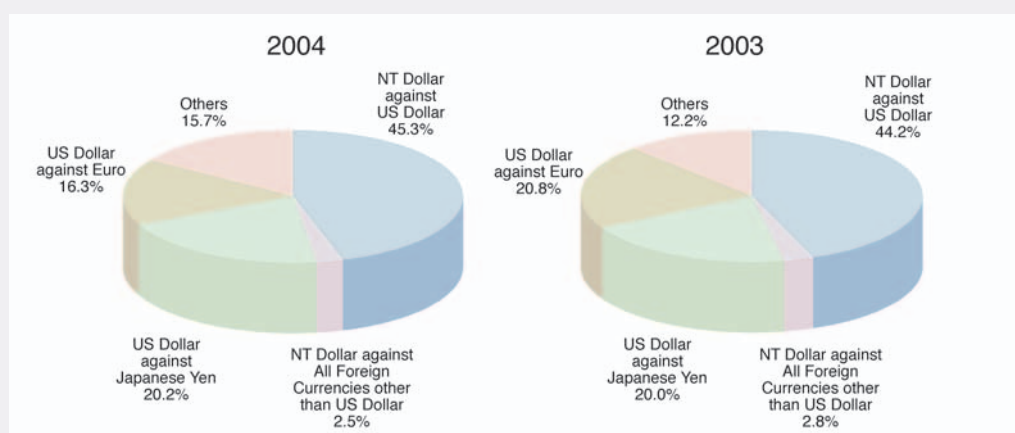
trading partners (weighted by the sum of imports and exports of goods), the NT dollar appreciated by 3.39 percent between the end of 2003 and 2004.

Active Trading in the Foreign Exchange Market

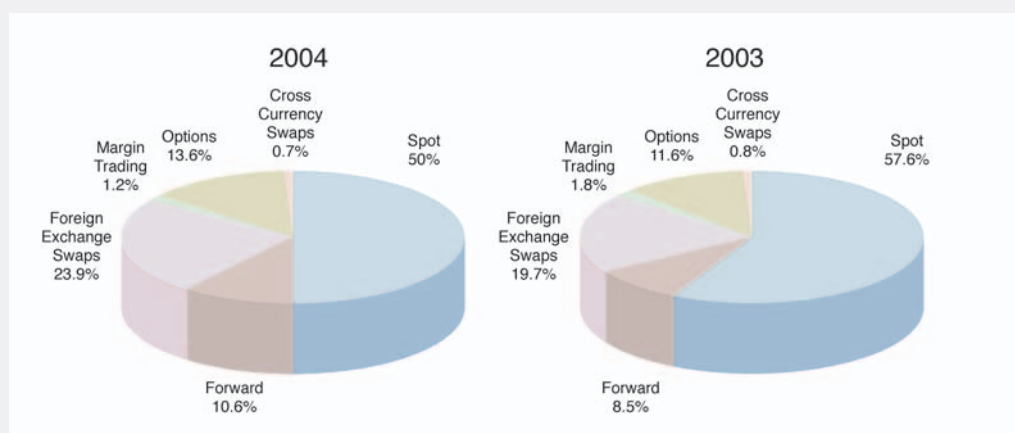
Trading in the Taipei foreign exchange market significantly increased in 2004. After deducting double counting on the part of interbank transactions, total net trading volume for the year increased by 40.4 percent from the previous year to US\$2,579.95 billion. The daily average turnover stood at US\$10.24 billion, representing an increase of 39.8 percent over the previous year. The increase in turnover mainly resulted from an expansion in external trade, and a marked rise in third currency transactions following the sharp appreciation of the euro and the Japanese yen against the US dollar.

In terms of trading partners, transactions between banks and non-bank customers accounted

Composition of Foreign Exchange Transactions by Traded Currency



Composition of Foreign Exchange Transactions by Product



Source: Department of Foreign Exchange, Central Bank of China.

for 32.5 percent of total net turnover. Interbank transactions made up a 67.5 percent share, including 20.8 percent for transactions among local banks and 46.7 percent for those between local banks and overseas banks.

As far as traded currencies are concerned, transactions in third currencies accounted for 52.2 percent of total trading volume, with trading in currency pairs of US dollar-Japanese yen and US dollar-euro accounting for shares of 20.2 percent and 16.3 percent, respectively. NT dollar trading against foreign currencies accounted for 47.8 percent of total trading volume, of which the share of NT dollars against US dollars was 45.3 percent.

With respect to types of transactions, spot transactions accounted for the highest share with 50 percent of total turnover, followed by foreign exchange swaps with 23.9 percent, options with 13.6 percent, forwards with 10.6 percent, margin trading with 1.2 percent, and cross currency swaps with 0.7 percent. Compared with 2003, except for a decrease in margin trading transactions, the trading volumes of foreign exchange swaps, options, and forwards all recorded growth rates of above 60 percent. This indicated the trend that banks tended to use the interbank swap market to adjust their currency composition, and that businesses inclined to utilizing financial derivatives to hedge the increasing risks they faced.

In 2004, turnover of forwards, swaps and options on foreign currency interest rates, commodity

Turnover of Major Products in the Taipei Foreign Exchange Market

Unit: US\$ Million

| Year | Spot | Forward | Forex Swaps | Margin Trading | Options | Cross Currency Swaps | Total |
|---------------------------|-----------|---------|-------------|----------------|---------|----------------------|-----------|
| 2000 | 793,024 | 99,702 | 176,299 | 20,056 | 112,485 | 3,536 | 1,205,104 |
| 2001 | 758,827 | 93,687 | 172,551 | 21,320 | 105,609 | 8,427 | 1,160,421 |
| 2002 | 872,844 | 114,341 | 238,807 | 25,869 | 149,630 | 8,875 | 1,410,366 |
| 2003 | 1,058,850 | 156,323 | 361,490 | 33,907 | 213,198 | 13,930 | 1,837,698 |
| 2004 | 1,289,872 | 273,931 | 617,577 | 30,299 | 350,514 | 17,764 | 2,579,955 |
| 2003-2004 Growth Rate (%) | 21.8 | 75.2 | 70.8 | -10.6 | 64.4 | 27.5 | 40.4 |

Source: Department of Foreign Exchange, Central Bank of China.

Turnover of Other Products in the Taipei Foreign Exchange Market

Unit: US\$ Million

| Year | Interest rate-related Products | | | | Commodity-related Products | | Stock Index Options | Credit Derivatives | Total |
|---------------------------|--------------------------------|---------------------|-----------------------|--|----------------------------|-------------------|---------------------|--------------------|---------|
| | Forward Rate Agreements | Interest Rate Swaps | Interest Rate Options | Foreign Currency Interest Rate Futures | Commodity Price Swaps | Commodity Options | | | |
| 2000 | 5,417 | 4,097 | 1,471 | 152 | 201 | 1,541 | 37 | -- | 12,916 |
| 2001 | 12,170 | 12,114 | 1,018 | 74 | 259 | 644 | 34 | -- | 26,313 |
| 2002 | 30,518 | 22,488 | 4,479 | 2,458 | 305 | 1,826 | 556 | -- | 62,630 |
| 2003 | 20,121 | 41,855 | 10,066 | 12,036 | 175 | 3,313 | 663 | -- | 88,229 |
| 2004 | 20,020 | 77,664 | 45,635 | 12,500 | 0 | 6,733 | 1,102 | 168 | 163,823 |
| 2003-2004 Growth Rate (%) | -0.5 | 85.6 | 353.4 | 3.9 | -100.0 | 103.2 | 66.3 | -- | 85.7 |

Source: Department of Foreign Exchange, Central Bank of China.

prices, stock price indices and credit amounted to US\$163.82 billion. Of this amount, interest rate-related derivatives accounted for the lion's share of US\$155.82 billion or 95.1 percent, representing an annual growth rate of 85.3 percent. This was mainly because of the sharp increase in euro convertible bond-related asset swaps, such as interest rate swaps and interest rate options.

Slightly Declining Transactions in the Foreign Currency Call-Loan Market

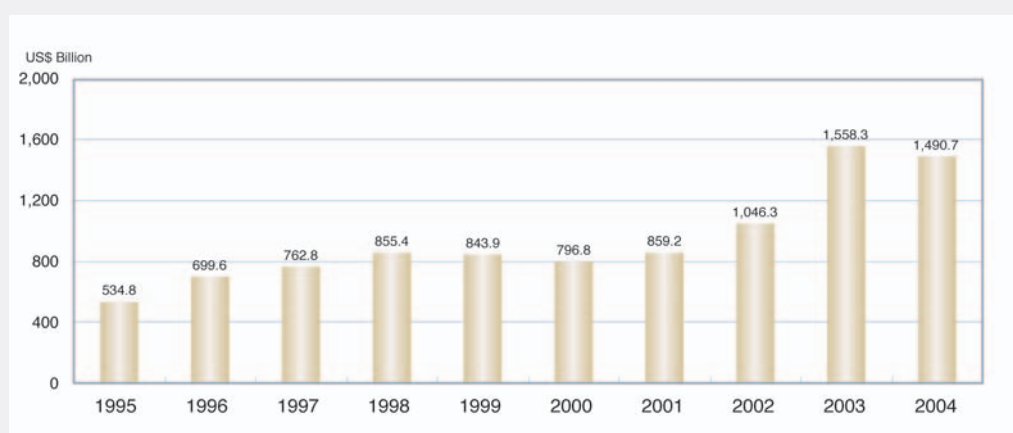
The transaction volume in the foreign currency call-loan market in 2004 was equivalent to US\$1,490.7 billion. Of this amount, US dollar transactions accounted for US\$1,488.9 billion, a reduction of 4.4 percent over 2003. The decrease was mainly because some banks raised interest rates on US dollar deposits to increase their sources of foreign currency funds, hence reducing their demand for foreign currency call loans.

Continued Expansion in the Assets of Offshore Banking Units

At the end of 2004, there were 70 offshore banking units (OBUs) in operation. Domestic banks operated 42 of the OBUs, while foreign banks ran the other 28. The combined assets of all OBUs totaled US\$69.22 billion at the end of the year, representing an increase of US\$6.7 billion or 10.7 percent from the previous year-end. This was a result of increases in loans to non-financial institutions and claims on financial institutions. Domestic bank OBUs accounted for US\$48.21 billion or 69.6 percent of these combined assets, and foreign bank OBUs accounted for US\$21.01 billion or 30.4 percent of the total.

The OBUs' main sources of funds were due to affiliated branches and deposits by financial institutions, which together accounted for 61.7 percent of total liabilities. These were followed

Transactions in the Taipei Foreign Currency Call-Loan Market



Source: Department of Foreign Exchange, Central Bank of China.

Consolidated Balance Sheet of Offshore Banking Units in Banking System

Unit: US\$ Million

| Year / Month | Loans to Non-financial Institutions | Portfolio Investment | Claims on Financial Institutions | Other Assets | Total Assets= Total Liabilities | Deposits of Non-financial Institutions | Due to Financial Institutions | Other Liabilities |
|--------------|-------------------------------------|----------------------|----------------------------------|--------------|---------------------------------|--|-------------------------------|-------------------|
| 2002/12 | 15,160 | 5,896 | 27,454 | 1,808 | 50,318 | 14,326 | 33,443 | 2,549 |
| 2003/12 | 15,939 | 7,648 | 37,420 | 3,541 | 64,548 | 16,307 | 44,288 | 3,953 |
| 2004/12 | 18,066 | 6,734 | 37,105 | 7,314 | 69,219 | 18,810 | 42,688 | 7,721 |
| 2004/ 1 | 16,383 | 7,684 | 35,043 | 3,851 | 62,961 | 16,212 | 42,571 | 4,178 |
| 2 | 16,506 | 7,913 | 35,146 | 5,334 | 64,899 | 15,920 | 43,232 | 5,747 |
| 3 | 16,981 | 7,830 | 35,131 | 6,542 | 66,484 | 16,426 | 43,224 | 6,834 |
| 4 | 17,347 | 7,906 | 36,344 | 7,275 | 68,872 | 16,475 | 44,533 | 7,864 |
| 5 | 17,790 | 7,790 | 36,247 | 7,352 | 69,179 | 16,583 | 44,589 | 8,007 |
| 6 | 18,528 | 7,624 | 38,643 | 6,725 | 71,520 | 16,629 | 47,458 | 7,433 |
| 7 | 18,322 | 7,593 | 34,645 | 6,243 | 66,803 | 17,002 | 42,879 | 6,922 |
| 8 | 18,380 | 7,311 | 35,660 | 5,890 | 67,241 | 17,633 | 42,950 | 6,658 |
| 9 | 18,192 | 7,121 | 35,170 | 6,042 | 66,525 | 18,233 | 41,641 | 6,651 |
| 10 | 18,406 | 7,012 | 35,284 | 6,196 | 66,898 | 18,337 | 41,813 | 6,748 |
| 11 | 18,426 | 6,752 | 37,157 | 7,258 | 69,593 | 18,557 | 43,212 | 7,824 |
| 12 | 18,066 | 6,734 | 37,105 | 7,314 | 69,219 | 18,810 | 42,688 | 7,721 |

Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

by deposits of non-financial institutions, which accounted for 27.2 percent of total liabilities. OBUs have been gradually developing into capital management centers for overseas Taiwanese firms. In terms of the geographical origin, 64 percent of funds came from Asia, and 20 percent from the Americas..

The OBUs' main uses of funds were due from affiliated branches and deposits with financial institutions. These accounted for the lion's share, or 53.6 percent of total assets. Second to these were loans extended abroad and locally with a share of 26.1 percent. Additionally, portfolio investments accounted for 9.7 percent of total assets. In terms of fund destination, 67 percent of funds went to Asia, and 20 percent to the Americas.

The forex-trading turnover of all OBUs in 2004 was US\$117.88 billion, of which US\$75.06 billion was for spot transactions, US\$23.1 billion for forward transactions, and US\$19.72 billion for foreign exchange swap transactions. Compared with 2003, forward transactions increased 3.2 times, mainly because Taiwanese firms in mainland China used non-deliverable forwards of the US dollar against the Chinese renminbi to hedge risks. Foreign exchange swap transactions also increased by 93 percent, mainly because the significant appreciation and large fluctuations of the euro and the Japanese yen against the US dollar led firms to use them to hedge risks. The total turnover of other derivative products, including margin trading, options, foreign currency interest rate swaps, financial futures, foreign currency forward rate agreements, cross currency swaps, commodity swaps, and credit derivatives, amounted to US\$62.95 billion, representing a slight increase of 6.5 percent over the previous year.

6. Stock Market

The Taiwan Stock Exchange (TSE) weighted stock price index (TAIEX) closed the year 2004 with an increase of 4.2 percent from the previous year-end. Most of the industrial group stock price indices went up, with construction shares posting the biggest gain for the second consecutive year. The daily average trading value for the year was NT\$95.5 billion, 16.9 percent higher than that of the previous year.

The GreTai Securities Market (GTSM, an over-the-counter market) weighted stock price index finished the year with a slight decrease of 1.3 percent from the year-ago level. Of all the industrial groups, construction shares recorded the biggest gain, while electronic shares registered the largest decline. The daily average turnover for the year reached NT\$13.9 billion, 68.1 percent higher than the previous year.

The TSE Market

Increase in the Number of Listed Companies

There were a total of 697 listed companies at the end of 2004, representing an increase

Major Statistics of the TSE Market

| | Stock price Index* (1966=100) | Daily Average Trading Value (NT\$ Billion) | Turnover Rate (%) | Market Capitalization* (NT\$ Billion) | Net Buying / Sale Positions** (NT\$ Billion) | | |
|---------|-------------------------------------|--|-------------------------|---|---|---|-----------------------|
| | | | | | Foreign Investors | Securities Investment and Trust Companies | Securities Dealers |
| 2002 | 4,452.5 | 88.2 | 217.4 | 9,095 | 27.9 | 6.9 | 2.3 |
| 2003 | 5,890.7 | 81.7 | 190.8 | 12,869 | 549.0 | -5.7 | 29.8 |
| 2004 | 6,139.7 | 95.5 | 177.5 | 13,989 | 284.0 | -14.1 | -15.4 |
| 2004/ 1 | 6,375.4 | 121.8 | 13.1 | 13,910 | 95.8 | -5.9 | 10.0 |
| 2 | 6,750.5 | 158.9 | 21.5 | 14,760 | 30.2 | -9.7 | 7.6 |
| 3 | 6,522.2 | 161.6 | 26.0 | 14,283 | -18.4 | -11.1 | -10.0 |
| 4 | 6,117.8 | 143.3 | 23.5 | 13,427 | -16.2 | -4.5 | -12.8 |
| 5 | 5,977.8 | 88.2 | 14.1 | 13,129 | -72.1 | -3.7 | -2.9 |
| 6 | 5,839.4 | 69.4 | 11.5 | 12,641 | 5.5 | 3.2 | -15.9 |
| 7 | 5,420.6 | 53.0 | 9.9 | 11,766 | -10.1 | -3.6 | -6.7 |
| 8 | 5,765.5 | 62.1 | 10.0 | 12,439 | 57.5 | 14.5 | 1.1 |
| 9 | 5,845.7 | 82.4 | 13.5 | 12,867 | 32.8 | 8.5 | 0.1 |
| 10 | 5,705.9 | 81.9 | 12.9 | 12,710 | 47.0 | -6.3 | -0.4 |
| 11 | 5,844.8 | 69.4 | 11.5 | 13,281 | 114.5 | 1.4 | 2.3 |
| 12 | 6,139.7 | 60.4 | 9.9 | 13,989 | 17.4 | 3.2 | 12.2 |

Notes: * Refers to end-of-period data.

** Minus sign "-" indicates net sale positions.

Source: Taiwan Stock Exchange Corporation.

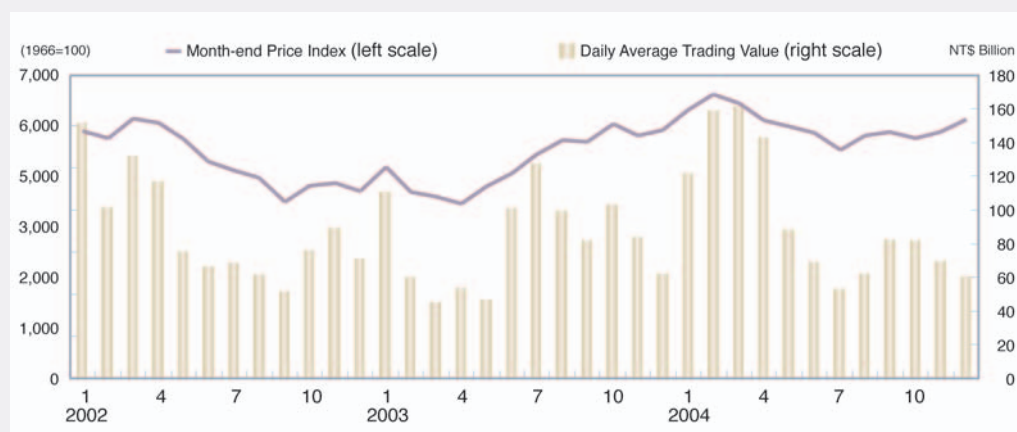
of 28 companies from the previous year-end. During the same period, the par value of total shares issued increased by 7.0 percent to NT\$5.1 trillion, while total market capitalization rose 8.7 percent to NT\$14 trillion.

Share Prices Decline After Early Gains

The TAIEX climbed higher early in the year, boosted by a recovery in both domestic and global economies, merger cases associated with financial holding companies, and a strong rebound in US technology shares. Stimulated by large net purchases by foreign investors, the TAIEX reached an annual high of 7,034 points on March 4. Afterwards, political uncertainties after the presidential election led to severe fluctuations in the stock market. From April to July, bearish sentiments overshadowed the stock market with China's macroeconomic tightening, surging international oil prices and a downgrade of the semiconductor sector by foreign securities firms all exerting downward pressure on the market. The TAIEX sank to an all-year low of 5,317 points on August 4. From then to the end of the year, international oil prices underwent a deep downward correction and Taiwan's weighting in the emerging market indices of Morgan Stanley Capital International Inc. (MSCI) was increased, both feeding through to large purchases by foreign investors in the local stock market. Furthermore, institutional investors actively engaged in year-end window dressing for their financial statements. All of these factors made the TAIEX gradually rally to conclude the year at 6,140 points, exhibiting a 4.2 percent increase when compared with the 5,891 points recorded at the end of the preceding year.

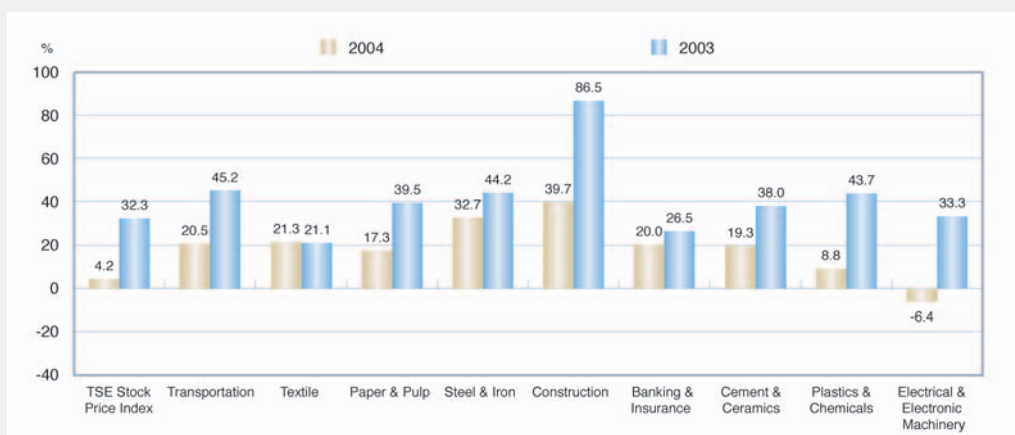
Most of the industrial group stock price indices advanced during the year. Construction shares, which recorded a gain of 39.7 percent, outperformed other shares due to a firm

TSE Stock Price Index and Trading Value



Source: TSEC Monthly Review, Taiwan Stock Exchange.

Changes in Industrial Group Stock Price Indices in the TSE Market



Source: TSEC Monthly Review, Taiwan Stock Exchange.

recovery in the property market. Steel and iron share prices recorded the second largest increase of 32.7 percent, reflecting a continuous rise in international steel prices. Transportation share prices advanced by 20.5 percent because a rise in international ocean freight rates increased profitability. Raw material-related shares, such as textile, paper and pulp, and cement and ceramics shares, performed well due to high international raw material prices. Banking and insurance share prices increased by 20 percent, mainly because of rising profitability after a substantial reduction of non-performing loan ratios and on-going mergers involving financial holding companies. In contrast, electrical and electronic machinery share prices fell by 6.4 percent, mainly because the prospects of this sector declined from its peak in the second half of the year, financial statement frauds successively occurred, and a sharp appreciation of the NT dollar in the fourth quarter caused foreign exchange losses in this export-driven sector.

Increase in Turnover

The daily average turnover for the year rose by 16.9 percent from the previous year's NT \$81.7 billion to NT\$95.5 billion, boosted by economic expansion and the expulsion of the severe acute respiratory syndrome (SARS) epidemic.

Net Buying Positions for Institutional Investors

Foreign investors registered a net purchase of NT\$284 billion in the TSE market, while local investment and trust companies and local securities dealers recorded a net sale of NT\$14.1 billion and NT\$15.4 billion, respectively.

In January and February, a rise in US technology shares and expectations of an NT dollar

appreciation led to large net purchases by foreign investors. The buying positions reversed between March and May due to China's macroeconomic tightening, mounting international oil prices, and the possibility of an earlier-than-expected US rate hike. Foreign investors returned to the TSE market in June due to a rebound in US technology shares and MSCI's announcement to increase Taiwan's weighting in two phases. However, a downgrade of the semiconductor sector and a plunge in US technology shares led to a net sale by foreign investors in July. For the five succeeding months from August, foreign investors remained net buyers mainly owing to a strong rally in US shares and lingering effects of MSCI's re-weighting of Taiwan.

Local investment and trust companies remained relatively conservative during the year, exhibiting net sales in seven months. In January and February, as share prices rose to a relatively high level, local investment and trust companies posted net sales on profit-taking. Net sales continued to May due to domestic political uncertainties, China's macroeconomic tightening and surging oil prices. June saw net purchases due to quarter-end window-dressing for financial statements. In July, the outlook of the electronics sector was dim, and investment and trust companies sold stocks to meet the cash demand for an upsurge of bond fund redemption, both leading to net sales. Investment and trust companies were net buyers of shares in August and September when share prices hovered around low levels, and net sellers again on profit-taking in October as the TAIEX approached 6,000 points. In November and December, encouraged by massive buying by foreign investors and motivated by the need of year-end window-dressing, local investment and trust companies showed net buying positions.

The GTSM Market

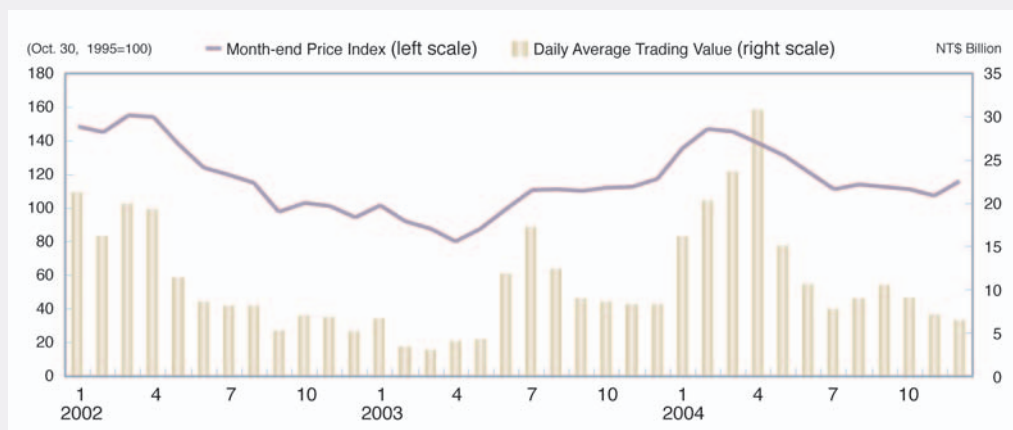
Increase in the Number of Listed Companies

The number of listed companies in the GTSM market increased to 466 at the end of 2004, an increase of 43 companies from the previous year-end. The par value of total shares issued amounted to NT\$626.1 billion at the end of 2004, 2.1 percent lower than that of the previous year-end. Market capitalization was valued at NT\$1.1 trillion at the end of 2004, recording a decline of 6.5 percent when compared with the previous year-end.

Share Prices Decline After Early Rally

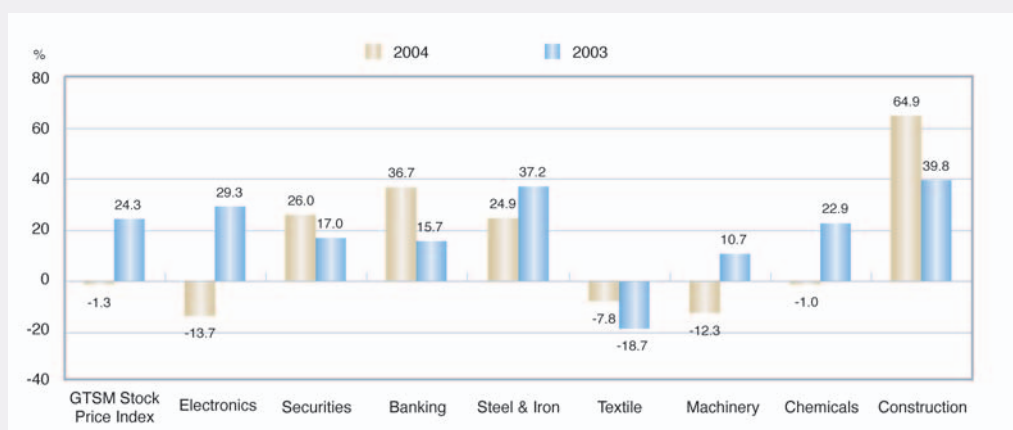
The GTSM stock price index rose early in the year and declined afterwards. From January to mid-April, a favorable economic outlook, government stimulus and continuous purchases by investment and trust companies drove up the index to an all-year high of 160.1 points on

GTSM Stock Price Index and Trading Value



Source: GTSM Monthly Review, Gre Tai Securities Market.

Changes in Industrial Group Stock Price Indices in the GTSM Market



Source: GTSM Monthly Review, Gre Tai Securities Market.

April 14. From then to mid-August, the index trended down on China's macroeconomic tightening, surging oil prices and defaults of several technology companies, hitting an annual low of 105.2 points on August 17. Thereafter, as purchases by foreign investors offset selling by domestic ones, the index entered a consolidation phase. In December, driven by year-end window-dressing needs, all institutional investors recorded net buying. The GTSM stock index closed the year at 115.8 points, down by 1.3 percent from the previous year-end.

Foreign investors and local securities dealers sold a net of NT\$12.7 billion and NT\$8.5 billion, respectively. On the other hand, local investment and trust companies bought a net of NT\$4.9

billion for the year.

Sharp Increase in Turnover

The daily average turnover in the GTSM market for the year was NT\$13.9 billion, a sharp increase of 68.1 percent from the previous year. The main reasons were the low base caused by the US-Iraq War and the outbreak of SARS during the previous year, as well as the domestic economic expansion during 2004.

7. Bond Market

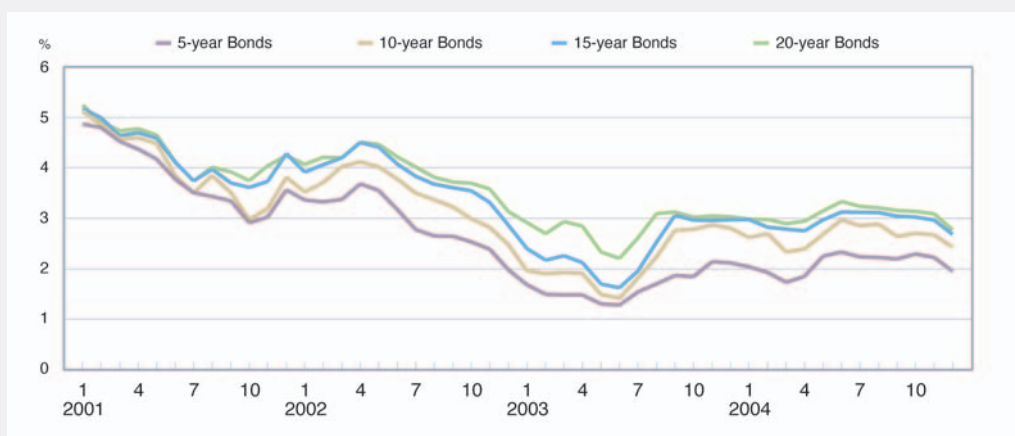
In 2004, new issues of bonds hit record highs, amounting to NT\$1,018.2 billion. Among them, issues of government bonds increased by large amounts in order to finance continuously rising budget deficits. Issues of corporate bonds diminished to a new low under the influence of rising interest rates and corporate scandals of some technology companies. Bank debenture issues increased significantly as banks managed to improve their capital adequacy ratios and strengthen their risk tolerance. NT dollar-denominated bonds issued by international financial institutions in Taiwan substantially decreased owing to rising issuance costs. Moreover, issues of asset securitization products successively increased, mainly due to their eligibility as liquidity reserves of banks, and a low withholding tax rate on investment returns relative to other similar financial products.

The total turnover of bonds in the secondary market also went up to a historic high in 2004, while bond yields fluctuated within a narrow range. In addition, bond funds shrank substantially this year because of the rise in interest rates and the massive redemption by investors. The bond fund market was overshadowed by negative sentiment in the second half of the year following the failure of the United Securities Investment Trust Corporation (USITC) in June.

Increase in Central Government Bond Issues

The Ministry of Finance issued central government bonds to a total value of NT\$ 465 billion

Yield Structure of Central Government Bonds with Different Maturities



Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

Issues and Outstanding Value in Bond Market by Category

Unit: NT\$ Billion

| Year/ Month | Total | | Central Government Bonds | | Local Government Bonds | | Corporate Bonds | | Bank Debentures | | Foreign Bonds* | | Beneficiary** Certificates | |
|----------------|---------|-------------|-----------------------------|-------------|---------------------------|-------------|-----------------|-------------|-----------------|-------------|----------------|-------------|-------------------------------|-------------|
| | Issues | Outstanding | Issues | Outstanding | Issues | Outstanding | Issues | Outstanding | Issues | Outstanding | Issues | Outstanding | Issues | Outstanding |
| 2002 | 962.0 | 3,748.6 | 426.2 | 2,124.1 | 10.0 | 90.4 | 285.8 | 1,007.2 | 214.0 | 377.3 | 26.0 | 149.6 | -- | -- |
| 2003 | 961.5 | 4,465.1 | 454.8 | 2,503.6 | -- | 84.9 | 278.8 | 1,176.9 | 182.5 | 541.2 | 45.0 | 158.5 | 27.0 | 11.8 |
| 2004 | 1,008.2 | 4,947.9 | 465.0 | 2,729.2 | 42.0 | 123.4 | 231.4 | 1,215.6 | 218.3 | 709.1 | 10.5 | 126.5 | 51.0 | 44.1 |
| 2004/1 | 100.4 | 4,494.8 | 80.0 | 2,524.2 | -- | 84.9 | 13.0 | 1,171.7 | 7.4 | 547.9 | -- | 154.5 | -- | 11.6 |
| 2 | 59.4 | 4,539.0 | 30.0 | 2,553.9 | -- | 84.9 | 19.9 | 1,178.9 | 9.5 | 555.5 | -- | 154.5 | -- | 11.3 |
| 3 | 126.3 | 4,640.4 | 40.0 | 2,593.6 | 15.0 | 99.9 | 7.6 | 1,171.8 | 49.4 | 602.0 | 5.0 | 153.5 | 9.3 | 19.6 |
| 4 | 79.2 | 4,706.6 | 40.0 | 2,633.2 | -- | 99.9 | 28.8 | 1,195.7 | 8.4 | 608.9 | 2.0 | 149.5 | -- | 19.4 |
| 5 | 88.2 | 4,802.1 | 35.0 | 2,608.2 | -- | 99.9 | 31.4 | 1,209.0 | 16.5 | 624.0 | -- | 149.5 | 5.3 | 23.3 |
| 6 | 101.4 | 4,752.2 | 35.0 | 2,643.1 | -- | 99.9 | 45.6 | 1,203.6 | 12.9 | 633.3 | 3.5 | 147.0 | 4.4 | 25.3 |
| 7 | 108.4 | 4,789.2 | 35.0 | 2,648.1 | 19.0 | 118.8 | 35.2 | 1,226.3 | 19.2 | 627.5 | -- | 143.5 | -- | 25.0 |
| 8 | 73.4 | 4,832.5 | 30.0 | 2,678.0 | -- | 118.8 | 18.0 | 1,222.9 | 15.5 | 641.0 | -- | 138.5 | 9.9 | 33.3 |
| 9 | 63.3 | 4,869.7 | 35.0 | 2,712.9 | -- | 117.9 | 9.6 | 1,217.6 | 13.6 | 649.5 | -- | 138.5 | 5.1 | 33.3 |
| 10 | 67.0 | 4,927.4 | 35.0 | 2,747.9 | -- | 117.9 | 9.0 | 1,217.9 | 23.0 | 672.2 | -- | 138.5 | -- | 33.0 |
| 11 | 54.9 | 4,868.4 | 35.0 | 2,694.6 | -- | 115.5 | 8.2 | 1,218.1 | 9.9 | 677.6 | -- | 129.5 | 1.8 | 33.1 |
| 12 | 96.3 | 4,947.9 | 35.0 | 2,729.2 | 8.0 | 123.4 | 5.1 | 1,215.6 | 33.0 | 709.1 | -- | 126.5 | 15.2 | 44.1 |

Notes: * Refers to both NT dollar-denominated and foreign currency-denominated bonds issued in Taiwan by international financial institutions.

** The outstanding beneficiary certificates exclude amount purchased back by originators for credit enhancement.

Sources: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

in 2004. The new issues registered a historic high, reflecting the government's tight fiscal position. The GreTai Securities Market (GTSM) has vigorously promoted the when-issued system to help discover prices of government bonds before issuance. The amount of when-issued trading for the year totaled NT\$14.8 trillion, which jumped 150.85 percent from NT\$5.9 trillion in 2003. Meanwhile, the Ministry of Finance also regularly issued re-opened government bonds with different maturities, namely 5, 10, and 20 years, in order to build an effective bond yield curve

Bond Transactions in the Over-the-Counter Market

Unit: NT\$ Billion

| Year/ Month | Total | Outright Transactions | | Repurchase Agreement Transactions | |
|----------------|-----------|-----------------------|-----------|-----------------------------------|-----------|
| | | Amount | Share (%) | Amount | Share (%) |
| 2002 | 134,399.0 | 60,659.0 | 45.1 | 73,740.0 | 54.9 |
| 2003 | 203,624.2 | 126,570.8 | 62.2 | 77,053.4 | 37.8 |
| 2004 | 205,925.2 | 123,445.6 | 59.9 | 82,479.6 | 40.1 |
| 2004/1 | 11,398.7 | 6,550.3 | 57.5 | 4,848.4 | 42.5 |
| 2 | 11,811.5 | 6,139.6 | 52.0 | 5,671.9 | 48.0 |
| 3 | 19,314.1 | 12,306.7 | 63.7 | 7,007.4 | 36.3 |
| 4 | 18,416.9 | 11,674.8 | 63.4 | 6,742.1 | 36.6 |
| 5 | 15,039.4 | 8,408.6 | 55.9 | 6,630.8 | 44.1 |
| 6 | 15,491.4 | 8,331.4 | 53.8 | 7,160.0 | 46.2 |
| 7 | 20,772.7 | 12,821.7 | 61.7 | 7,951.0 | 38.3 |
| 8 | 17,219.6 | 9,947.2 | 57.8 | 7,272.4 | 42.2 |
| 9 | 16,199.0 | 8,858.9 | 54.7 | 7,340.1 | 45.3 |
| 10 | 18,569.4 | 11,743.6 | 63.2 | 6,825.8 | 36.8 |
| 11 | 20,570.7 | 13,480.3 | 65.5 | 7,090.4 | 34.5 |
| 12 | 21,121.8 | 13,182.5 | 62.4 | 7,939.3 | 37.6 |

Source: *Taiwan Securities Exchange (TSE) & Gre Tai Securities Market (GTSM).*

and extend the duration of benchmark bonds. Moreover, since July 1, 2004, the government bond auction system has adopted a single-price (also called Dutch auction) instead of a multiple-price bidding process. Under this new auction method, all bidders settle at the highest winning rate thereby reducing volatility of bond yields in the secondary market.

Diminishing Amounts in Corporate Bond Issues

The new issues of corporate bonds were relatively active in the first quarter of 2004 mainly due to the large amount of convertible corporate bonds issued by many enterprises in response to the bullish stock market. In the second quarter, as local bond funds continuously expanded, the demand for corporate bonds strengthened. From the supply side, many enterprises were encouraged to issue corporate bonds to lock in low-cost funds in anticipation of a rise in long-term interest rates. Consequently, the issues of corporate bonds substantially increased in the second quarter. From the third quarter, under the influence of rising interest rates and a series of corporate scandals, new issues of corporate bonds started to decline. The issuance of corporate bonds was much muted during the second half of the year. For the year as a whole, total issues of corporate bonds were NT\$231.4 billion, a decline of 17 percent from the previous year.

Significant Increase in Bank Debenture Issues

Although in recent years the increasing diversity of bank debenture products has raised the issuing cost, domestic banks issued a record high of NT\$218.3 billion in bank debentures

Turnover in Bond Market by Category

Unit: NT\$ Billion

| Year/ Month | Total | TSE Market | Gre Tai Market | | | | | | |
|----------------|-----------|----------------------------------|----------------|---------------------|-----------------|-------------|------------------|--------------------|-----------------------------|
| | | Corporate Bonds (Convertible) | Subtotal | Government Bonds | Corporate Bonds | | Foreign Bonds | Bank Debentures | Beneficiary Certificates |
| | | | | | Nonconvertible | Convertible | | | |
| 2002 | 134,399.0 | 19.1 | 134,379.9 | 133,187.6 | 656.2 | 196.0 | 286.4 | 53.7 | -- |
| 2003 | 203,624.0 | 9.8 | 203,614.2 | 200,619.9 | 1,904.5 | 249.0 | 713.4 | 125.4 | 2.0 |
| 2004 | 205,925.2 | 4.6 | 205,920.6 | 202,015.2 | 2,328.5 | 441.1 | 636.1 | 457.2 | 42.5 |
| 2004/1 | 11,398.7 | 0.5 | 11,398.2 | 11,208.2 | 110.5 | 28.4 | 42.2 | 8.9 | -- |
| 2 | 11,811.5 | 0.6 | 11,810.9 | 11,552.2 | 139.8 | 43.6 | 56.7 | 17.3 | 1.0 |
| 3 | 19,314.1 | 0.4 | 19,313.7 | 18,990.5 | 174.6 | 54.8 | 74.8 | 16.0 | 3.0 |
| 4 | 18,417.0 | 0.5 | 18,416.5 | 18,133.9 | 155.5 | 46.8 | 65.2 | 14.1 | 1.0 |
| 5 | 15,039.4 | 0.4 | 15,039.0 | 14,785.1 | 146.4 | 36.9 | 50.8 | 15.6 | 4.2 |
| 6 | 15,491.4 | 0.2 | 15,491.2 | 15,210.1 | 145.9 | 30.4 | 50.7 | 46.0 | 8.1 |
| 7 | 20,772.7 | 0.3 | 20,772.4 | 20,388.1 | 248.9 | 31.2 | 58.1 | 43.5 | 2.6 |
| 8 | 17,219.6 | 0.6 | 17,219.0 | 16,907.4 | 195.5 | 28.8 | 52.1 | 29.5 | 5.7 |
| 9 | 16,199.0 | 0.6 | 16,198.4 | 15,775.0 | 235.4 | 46.2 | 50.5 | 85.6 | 2.3 |
| 10 | 18,569.4 | 0.2 | 18,569.2 | 18,170.5 | 255.0 | 32.5 | 34.8 | 74.1 | 2.5 |
| 11 | 20,570.6 | 0.2 | 20,570.4 | 20,182.1 | 274.6 | 29.7 | 37.6 | 43.9 | 6.4 |
| 12 | 21,121.8 | 0.1 | 21,121.7 | 20,711.8 | 246.4 | 31.8 | 62.6 | 62.7 | |

Source: Taiwan Securities Exchange (TSE) & Gre Tai Securities Market (GTSIM).

this year, an increase of 19.62 percent from the previous year. The increase was mainly because banks hurried to raise low-cost medium- and long-term funds before interest rates turned up, while at the same time improving capital adequacy ratios and strengthening risk tolerance.

Decrease in Foreign Bond Issues

In 2004, as bond yields rose, prices of foreign bonds traded by Cross Currency Swap (CCS) trended down. As a result, new issues of NT dollar-denominated bonds by international financial institutions dropped by 76.67 percent over the previous year to NT\$10.5 billion. Of these issues, the European Bank for Recovery and Development (EBRD) accounted for the largest share of NT\$7 billion, followed by the Central American Bank for Economic Integration (CABEI) with NT\$3.5 billion. The weighted average issuing interest rate on 5-year NT dollar foreign bonds ranged from 2.25 percent to 2.40 percent.

Gradually Growing Asset Securitization

In 2004, the total issuance of asset-backed securities amounted to NT\$51 billion. Although this amount accounted for only 5.01 percent of total bond issuance, it presents a jump of NT\$24 billion or 88.89 percent from that recorded in 2003. Of the components, the issues of Financial Asset Securities including Mortgage Backed Securities (MBS), Collateralized Loans Obligations (CLO), Obligatory Right of Auto Loans (ORAL), and Obligatory Right of Business Accounts Receivables (ORBAR) reached NT\$41 billion. The issues of Real Estate Securities, all of which belonged to Real Estate Asset Trust (REAT), amounted to NT\$10 billion. Most investors of securitization products were institutional investors, including banks, insurance companies, bills finance companies, and bond funds. The securitization products are welcomed by institutional investors mainly because banks are allowed to hold them as liquidity reserves and the interest payments distributed to investors are taxed separately at a low withholding tax rate of 6 percent.

Booming Transactions in the OTC Market

During the first half of the year, as economic recovery strengthened and expectations of rising interest rates prevailed, the bond market became bearish, pressing the yield on benchmark 10-year government bonds to rise from 2.33 percent to 2.97 percent. In the second half of the year, under the influence of rising interest rates and surging oil prices, economic growth apparently moderated. In addition, the failure of a local securities investment trust company, the USITC, triggered massive redemptions of bond funds. A large part of these funds, in turn,

Portfolio Composition of Bond Funds

Unit: NT\$ Billion

| Year / Month | Total | Outright Purchases | | Repurchase Agreements | | Bank Deposits | | Short-term Securities | |
|--------------|---------|--------------------|-----------|-----------------------|-----------|---------------|-----------|-----------------------|-----------|
| | | Amount | Share (%) | Amount | Share (%) | Amount | Share (%) | Amount | Share (%) |
| 2002 | 1,847.0 | 798.4 | 43.2 | 472.7 | 25.6 | 521.4 | 28.2 | 54.5 | 3.0 |
| 2003 | 2,107.6 | 1,066.9 | 50.6 | 611.5 | 29.0 | 354.8 | 16.8 | 74.4 | 3.6 |
| 2004 | 1,883.3 | 1,015.5 | 53.9 | 562.5 | 29.9 | 258.7 | 13.7 | 46.6 | 2.5 |
| 2004/ 1 | 2,260.2 | 1,105.9 | 48.9 | 668.6 | 29.6 | 385.3 | 17.1 | 100.4 | 4.4 |
| 2 | 2,317.1 | 1,119.6 | 48.3 | 694.3 | 30.0 | 395.4 | 17.1 | 107.8 | 4.6 |
| 3 | 2,204.9 | 1,118.4 | 50.7 | 623.1 | 28.3 | 376.8 | 17.1 | 86.6 | 3.9 |
| 4 | 2,384.2 | 1,176.1 | 49.3 | 693.3 | 29.1 | 404.3 | 17.0 | 110.5 | 4.6 |
| 5 | 2,409.7 | 1,182.4 | 49.1 | 706.8 | 29.3 | 399.8 | 16.6 | 120.7 | 5.0 |
| 6 | 2,281.7 | 1,162.9 | 51.0 | 635.8 | 27.9 | 382.3 | 16.7 | 100.7 | 4.4 |
| 7 | 2,097.8 | 1,149.7 | 54.8 | 517.1 | 24.6 | 364.7 | 17.4 | 66.3 | 3.2 |
| 8 | 2,073.2 | 1,114.5 | 53.8 | 558.1 | 26.9 | 340.1 | 16.4 | 60.4 | 2.9 |
| 9 | 1,938.3 | 1,068.7 | 55.1 | 511.3 | 26.4 | 313.1 | 16.2 | 45.1 | 2.3 |
| 10 | 1,932.9 | 1,045.1 | 54.1 | 545.3 | 28.2 | 293.3 | 15.2 | 49.2 | 2.5 |
| 11 | 1,924.5 | 1,014.2 | 52.7 | 585.8 | 30.4 | 273.6 | 14.2 | 50.9 | 2.7 |
| 12 | 1,883.3 | 1,015.5 | 53.9 | 562.5 | 29.9 | 258.7 | 13.7 | 46.6 | 2.5 |

Source: Securities Investment Trust & Consulting Association of R.O.C.

flowed to the government bond market for hedging purposes and the weighted average yield on 10-year government bonds gradually diminished from 2.97 percent to 2.43 percent.

Trading in the bond market remained relatively active and amounted to a record high of NT\$205.93 trillion in 2004, a marginal increase of 1.13 percent from the previous year. Of this amount, outright transactions decreased by 2.47 percent, and repurchase agreement transactions went up by 7.04 percent. Meanwhile, the share of outright transactions and repurchase agreements in total transactions were 59.9 percent and 40.1 percent, respectively.

Shrinkage in Net Assets of Bond Funds

Bond funds substantially expanded in the first half of the year as interest rates on bank deposits remained at record lows. As of the end of May, the net assets of local bond funds registered a record high of NT\$2,409.7 billion in total. During the second half of the year, the rise in interest rates, coupled with the failure of a local securities investment trust company, caused large redemptions of bond funds in general. However, in the following months prudent steps were taken to boost the credibility of bond funds, such as the strict control of investment positions in mid- to long-term bonds, increasing liquidity holdings, and raising the minimum rating requirement for fixed income vehicles. As a result, redemptions of bond funds were curbed and the net assets of local bond funds were NT\$1,883.3 billion at the end of the year.

Moreover, the newly revised *Regulations Governing Securities Investment Trust Funds* stipulated that the weighted-average duration of the portfolio held by bond funds must be one year or above. Nearly all the 92 bond funds met this criterion at the end of the year. Furthermore, outright purchases of bonds exceeded 50 percent of the portfolio held by all bond funds. With respect to portfolio allocation, local bond funds mainly invested in outright purchases of corporate bonds, repurchase agreements of government bonds, and bank time deposits. At the end of 2004, outright purchases of bonds accounted for 53.92 percent of total investment, representing an increase from the previous year-end, repurchase agreements increased to 29.87 percent, and deposits with financial institutions declined to 13.74 percent.



III. Central Bank Operations

- 1. Overview**
- 2. Monetary Management**
- 3. Foreign Exchange Management**
- 4. Banking Supervision**
- 5. Payment and Settlement Systems**
- 6. Currency Issuance**
- 7. Treasury Agency Function**
- 8. Participation in International Activities**

III. Central Bank Operations

1. Overview



In accordance with 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. It holds regular meetings four times a year. Starting from the end of the year 2000, the Board decided to adopt an accommodative policy stance to add momentum to the recovery of the domestic economy. To stimulate the economy, the Bank cut the discount rate 15 times between December 2000 and the end of 2003.

At the beginning of 2004, the economic expansion became increasingly well established as external trade and private consumption and investment were on the rise. Although the economic expansion slowed in the second half of the year, for the year 2004 as a whole, real GDP still grew from the previous year's 3.33 percent to 5.71 percent, the highest level since 2001. Inflation in consumer prices also picked up to 1.62 percent in 2004 from its declining trend in the past three years. At the same time, core CPI inflation increased from a negative 0.61 percent growth in 2003 to a positive 0.71 percent. With respect to the labor market, unemployment decreased throughout the year. The average unemployment rate for 2004 was 4.44 percent, declining by 0.55 of a percentage point from 2003.

Against the backdrop of solid economic expansion and rising prices, the Bank gradually steered its monetary policy toward a neutral stance. The discount rates were raised by a total of 37.5 basis points at the Bank's September and December Board meetings to preempt inflation expectations and to prevent the negative real interest rate from going down further, which may distort fund allocation and discourage long-term financial stability. At the end of the year, the discount rate, the interest rate on accommodations with collateral and the interest

rate on accommodations without collateral stood at 1.75 percent, 2.125 percent and 4.0 percent, respectively. In response to the policy actions, money market short-term interest rates also gradually trended up.

As Taiwan is a small and highly open economy, exchange rate movements impose significant influences on external trade and economic growth. With a managed float regime, the NT dollar exchange rate is in principle determined by market forces. However, in cases when seasonal or irregular factors such as a surge in short-term capital movements, result in excessive volatility in the exchange rate, the Bank will step in, as deemed appropriate, to maintain the dynamic stability of the NT dollar. In the year 2004, under the influences of both internal and external factors, the NT dollar appreciated against the US dollar by 6.46 percent. Its volatility, however, remained relatively low as compared with major currencies and other Asian currencies.

Institutional reforms were continuously implemented throughout 2004. To make loan pricing more market-sensitive and transparent, credit cooperatives all adopted adjustable rate mortgages and the market rate-linked base lending rate regime in the year to increase their competitiveness. The Bills Depository and Clearing System also started its operations with assistance from the Bank in April 2004. Moreover, the Bank continued its efforts in financial liberalization and globalization. It introduced new financial products, streamlined application procedures for foreign portfolio investment, as well as promoted direct cross-strait financial businesses. The Financial Supervisory Commission (FSC) was established on July 1, 2004 to consolidate the supervision and examination of the banking, securities and insurance industries under one roof. Since its inception, the Bank has no longer undertaken financial examination responsibilities. However, it still retains its authority to carry out target examinations related to the Bank's monetary, credit and foreign exchange policies. A milestone in Taiwan's financial supervisory history was reached after years of effort.

2. Monetary Management

Raising the Discount Rate

Economic recovery accelerated from the beginning of 2004, while inflation remained low and no significant improvement was seen in the labor market. The Bank thus maintained its discount rate unchanged in the first half of the year to ensure sustained economic growth. Inflation started to surge in the third quarter as domestic food and energy prices both soared. In light of the solid economic expansion and rising prices, the Bank switched its low interest rate policy adopted since the end of 2000 into a neutral monetary policy stance at its September meeting. The discount rate, the interest rate on accommodations with collateral and the interest rate on accommodations without collateral were adjusted upwards by 25 basis points, respectively. This action was aimed to preempt inflation expectations and to prevent the negative real interest rate from going down further, which may distort fund allocation and discourage long-term financial stability. The aforementioned three rates were each raised again by 12.5 basis points on December 31. At the end of the year, the three policy rates stood at 1.75 percent, 2.125 percent and 4.0 percent, respectively.

Lowering the Remunerative Rate on Banks' B Reserve Accounts

Since the remunerative rate on banks' B reserve accounts (55 percent of banks' required reserves were deposited in B accounts with the Bank) was adjusted down to 1.75 percent on March 21, 2003, market interest rate on deposits and loans both trended downward. In order to narrow the interest rate spread and reasonably reflect market interest rates, the Bank lowered the remunerative rate by a further 0.25 of a percentage point on March 29, 2004 to 1.50 percent.

Central Bank Interest Rates

Unit: %

| Effective Date | Discount Rate | Accommodation Rate with Collateral | Accommodation Rate without Collateral |
|----------------|------------------|--|---|
| 2002 / June 28 | 1.875 | 2.250 | 4.125 |
| Nov. 12 | 1.625 | 2.000 | 3.875 |
| 2003 / June 27 | 1.375 | 1.750 | 3.625 |
| 2004 / Oct. 1 | 1.625 | 2.000 | 3.875 |
| Dec. 31 | 1.750 | 2.125 | 4.000 |

Source: *Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.*

Conducting Open Market Operations

The Bank's certificates of deposit (CDs) remain the primary instrument for the Bank to manage banks' day-to-day reserves. Its interest rates also played an important role to guide market rates when they were issued on a fixed-rate basis. For the year as a whole, Taiwan experienced a net capital inflow creating ample liquidity in the banking system. The Bank therefore issued CDs mostly with a fixed-rate to drain excess liquidity and to stabilize market interest rates. At the end of the year, the outstanding amount of CDs issued by the Bank was NT\$3,563 billion, an increase of NT\$570 billion from a year earlier. In addition, foreign exchange swaps with banks were used extensively to absorb excess liquidity. To meet seasonal demand, the Bank occasionally arranged Repos on the Bank's CDs to inject funds into the banking system. During this year, the Bank purchased Repos worth NT\$618 billion, which were all due by the end of the year.

Decreasing Redeposits from Financial Institutions

Receiving redeposits from Chunghwa Post Co. and commercial banks is another instrument of the Bank to influence banks' reserve positions, although they are not used as frequently as open market operations. During the year 2004, Chunghwa Post Co. and commercial banks both shifted some of their redeposits to the Bank's CDs. At the end of the year, the outstanding postal savings redeposits and banks' redeposits declined to NT\$1,351 billion and NT\$383 billion, a decrease of NT\$18 billion and NT\$159 billion, respectively, from a year before. In addition,

The Bank's Open Market Operations

Unit: NT\$ Billion

| | Amount Absorbed | | | Amount Offered | | | Weighted Average Rates on CDs Issued (%) | | |
|----------|-----------------|-----------------------------------|---------------|----------------|----------------------|--------------------|--|-------------|-----------|
| | Total | Maturity of Repurchase Agreements | Issues of CDs | Total | Repurchase Agreement | Redemptions of CDs | 1-30 days | 92-182 days | 1-2 years |
| 2002 | 8,754 | 841 | 7,913 | 7,759 | 841 | 6,918 | 2.11 | 2.12 | 2.26 |
| 2003 | 7,399 | 1,371 | 6,028 | 6,354 | 1,371 | 4,983 | 1.15 | 1.18 | 1.40 |
| 2004 | 12,741 | 618 | 12,123 | 12,171 | 618 | 11,553 | 1.08 | 1.09 | 1.30 |
| 2004 / 1 | 888 | 25 | 863 | 733 | 28 | 705 | 1.03 | 1.08 | 1.30 |
| 2 | 867 | 97 | 770 | 400 | 109 | 291 | 1.04 | 1.08 | 1.30 |
| 3 | 809 | 184 | 625 | 800 | 177 | 623 | 1.03 | 1.08 | -- |
| 4 | 1,011 | 158 | 853 | 784 | 152 | 632 | 1.02 | 1.08 | -- |
| 5 | 839 | 29 | 810 | 922 | 25 | 897 | 1.00 | 1.08 | -- |
| 6 | 543 | 74 | 469 | 679 | 74 | 605 | 1.03 | 1.08 | -- |
| 7 | 755 | 3 | 752 | 931 | 4 | 927 | 1.03 | 1.08 | -- |
| 8 | 1,100 | 5 | 1,095 | 1,205 | 5 | 1,200 | 1.04 | 1.08 | -- |
| 9 | 1,528 | 43 | 1,485 | 1,678 | 44 | 1,634 | 1.06 | 1.08 | -- |
| 10 | 1,330 | -- | 1,330 | 1,222 | -- | 1,222 | 1.15 | 1.20 | -- |
| 11 | 1,235 | -- | 1,235 | 1,120 | -- | 1,120 | 1.15 | 1.20 | -- |
| 12 | 1,836 | -- | 1,836 | 1,697 | -- | 1,697 | 1.15 | 1.21 | -- |

Source: Financial Statistics Monthly, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

the three major domestic farmers' banks, namely the Taiwan Cooperative Bank, the Land Bank of Taiwan and the Farmers Bank of Taiwan, may receive deposits from community financial institutions and make redeposits with the Bank. At the end of the year, their outstanding redeposits remained at NT\$144.6 billion, the same level as in 2003.

Continuing to Promote Preferential Loans

To help boost the real estate market and relieve the mortgage burden of home buyers, the Bank, the Ministry of Finance and the Ministry of the Interior jointly initiated a preferential mortgage loan program in August 2000. This program consisted of NT\$120 billion in preferential loans and credit guarantees to the young buying their first homes, and NT\$200 billion in preferential loans to general home buyers. The government subsidized 0.85 of a percentage point of the annual interest rate, contributing to the popularity of the program. The program was expanded several times since the launch of the program, but with a lower interest subsidy.

In May 2004, the upper limit of the program was further raised by NT\$300 billion, with only 0.125 of a percentage point interest subsidy. The total amount of the program was thus increased to NT\$1,500 billion. By the end of 2004, a total of 686,943 households had obtained an amount of NT\$2,045 billion under this program. The amount included NT\$724 billion in parallel lending by banks applying ordinary interest rates.

The Preferential Loans and Credit Guarantees for Traditional Industries was another preferential loan program initiated by the Bank and the Ministry of Finance in October 2000.

The program with an initial upper limit of NT\$450 billion raised from the local banking system was provided to help traditional industries acquire the funds necessary for business operations.

The total amount of the preferential loans has been expanded continuously. In November 2004, its upper limit was lifted again by NT\$450 billion, bringing the total amount of this program to NT\$1,850 billion. By the yearend, a total of NT\$1,610 billion in loans were extended by banks to support 198,801 cases under this package.

During the year, the Bank continued to provide subsidies to victims of the earthquake in 1999 for their interest payments on mortgage loans. This subsidy also applied to banks assuming the mortgage assets of earthquake victims. By the end of 2004, a total of NT\$55.8 billion worth of loans had been approved for 32,206 housing units under this program. At the same time, the Bank also appropriated a total of NT\$2.66 billion from postal savings redeposits for banks to make loans for the reconstruction of quake-ravaged schools, medical institutions, shrines and temples, as well as historical sites.

Enhancing the SME Credit Guarantee System

To facilitate small and medium-sized enterprise (SME) financing, the credit guarantee system has been enhanced continuously by the Bank. Those SMEs whose loan applications are rejected by banks may look for assistance via a window at the SME One-Stop Solution Center of the Ministry of Economic Affairs, which coordinates relevant agencies to handle such cases. Since December 2002, the Bank has seconded staff to the Center to assist the operations. The work continued until March 2004. In June 2003, the Bank also started to monitor banks' performance on SME financing on a monthly basis. At the end of 2004, the guarantee balances and loans extended to SMEs by domestic banks were NT\$332.6 billion and NT\$2,983.6 billion, showing an increase of NT\$141 billion and NT\$ 341billion, respectively, as compared with the end of May 2003.

Promoting Adjustable Rate Mortgages and Flexible Base Rates

Since 2002, the Bank has actively promoted adjustable rate mortgages and flexible base rates pricing system to make banks' loan pricing more market-sensitive and transparent, thereby increasing the effectiveness of monetary policy transmission. The new pricing system was introduced to substitute downwardly rigid prime rates. At the same time, banks were urged to apply the new pricing system to their old loans. By the yearend, loans extended by domestic banks still using the old prime rates accounted for merely 5.8 percent of total loans. In view of the success of this pricing system, from April 2004, the Bank urged all community financial institutions to adopt the same pricing system to increase their competitiveness and to fairly protect the interests of both lenders and borrowers. At the end of the year, all credit cooperatives had adopted this new pricing system.

3. Foreign Exchange Management

Foreign Exchange Market Operations

The Bank kept on pursuing dynamic stability of the NTD exchange rate under a managed floating regime in 2004. During the year, the US dollar depreciated due to factors such as the deteriorating twin deficits in the US and the possible appreciation of the Chinese Renminbi. Meanwhile the NTD exchange rate against the USD appreciated due to factors such as the Asian currency appreciation, the raising of the weight of Taiwan in the basket of benchmark world stock market index compiled by the Morgan Stanley Capital International Co. (MSCI), and exporter's early sale of forward exchanges. At the end of the year, the NTD exchange rate was 33.978 per US dollar, an appreciation of 6.46 percent compared to the end of 2003. Over the same period, the euro appreciated by 8.07 percent, while the Korean won appreciated by 15.22 percent against the USD.

In order to enhance financial discipline and to promote the stable development of the local foreign exchange market, the Bank has implemented a real-time reporting system on large-amount foreign exchange transactions to monitor the market and facilitate the balance of demand and supply. In addition, the Bank ensured that forward transactions were made only upon real demand, conducted on-site examination and audit of abnormal transactions, and urged banks to enhance exchange rate risk management to effectively eliminate foreign exchange speculation and ensure sound functioning of the foreign exchange market.

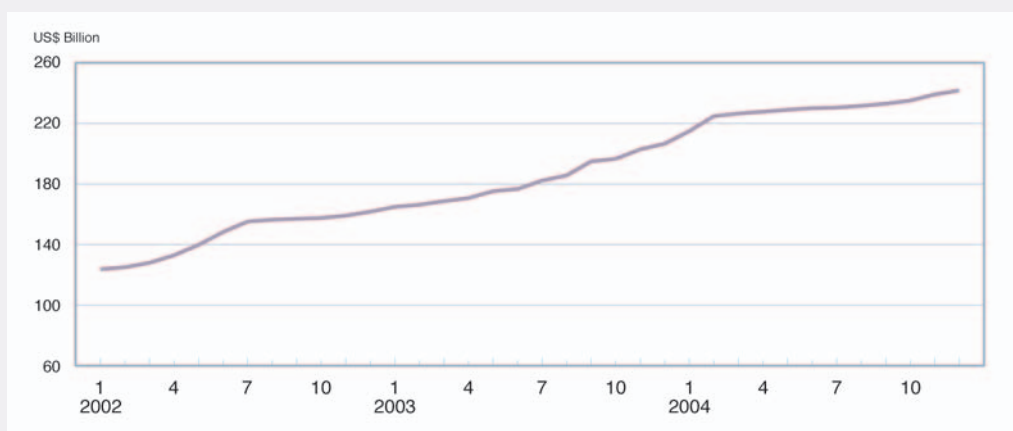
Foreign Exchange Market Management

The Bank approved 32 branches of local banks to do full-fledged foreign exchange business and another 51 branches to do limited business of buying/selling foreign currencies and traveler's checks in 2004.

New financial products were aggressively promoted in 2004. On May 26, 33 foreign exchange derivative products were allowed to be adopted with only ex post reporting requirements. On October 20, Regulations Governing the Discretionary Foreign Currency Margin Trading Business Conducted by Authorized Banks was promulgated to open discretionary margin trading business. For the year 2004, there were 180 new financial products adopted by banks.

In order to provide banks with sufficient foreign exchange liquidity to meet corporates' funding needs, the Bank appropriated seed funds of US\$20 billion, 1 billion euros and 15 billion

Foreign Exchange Reserves



Source: Department of Foreign Exchange, Central Bank of China.

yens for the foreign exchange call-loan market. Moreover, the Bank actively carried out foreign currency swap transactions. During the year, foreign exchange call loan transactions reached US\$1,491 billion, while foreign exchange-NT dollar swap transactions reached US\$199 billion, an 82.2 percent growth over last year.

Foreign Exchange Reserve Management

In addition to maintaining liquidity, security and profitability, the Bank's objectives of foreign reserve management also included promoting economic development and upgrading industries.

At the end of 2004, total foreign exchange reserves amounted to US\$241.7 billion, a US\$35.1 billion increase from the end of 2003. The main factors contributing to the increase included: (1) net foreign capital inflow; (2) exporters' earlier sale of forward exchange contracts; (3) the return from foreign exchange reserve investment; and (4) the increase of the US dollar value of euro- and yen-denominated reserve assets due to the appreciation of euro and yen against the US dollar.

Capital Flow Management

With the progress of financial liberalization and internationalization, the Bank manages the foreign exchange market according to the market mechanism. In general, bilateral capital movements can flow freely. As of 2004, restrictions only remained on a few short-term financial transactions involving the conversion of NTD. For example, overseas Taiwanese and foreign natural persons could invest in Taiwan securities up to US\$5 million; a foreign legal entity and a non-company fund could invest in Taiwan securities up to US\$50 million. Each domestic company and resident could conduct inward or outward remittances up to US\$50 million and

US\$5 million, respectively. Nonresidents could remit up to US\$0.1 million per transaction. For remittances exceeding the respective ceilings, applications could be made through authorized foreign exchange banks.

Key measures with regard to capital flows in 2004 included:

- (1) The Ministry of Finance (the competent authority has become the Financial Supervisory Commission of the Executive Yuan since July 2004), after consultation with the Bank, adopted the following measures in order to loosen restrictions on foreign investments in domestic securities: (i) effective February 3, foreign investors were authorized to invest in money market funds. This investment amount, plus the investment amount of repos, other money market instruments, margins on futures and time deposits, could not exceed 30 percent of total remittances; (ii) effective May 21, foreign investors were authorized to participate in the Bank's daylight overdraft facility; (iii) effective June 17, the Bank no longer reviewed foreigners' securities investment applications; and (iv) foreign investors were authorized to broaden the scope of securities borrowing and lending for strategic trading, including stock index securities investment trust funds (effective September 22), domestic and overseas exchangeable corporate bonds, the arbitrage/hedging of government exchangeable bonds, stock index securities investment trust funds, and borrowing securities during the transition period from convertible bonds to stocks (effective December 21).
- (2) The MOF, after consultation with the Bank, adopted the following measures in order to promote the internationalization of the domestic capital market and to improve relations with international financial organizations: (i) enterprises are allowed to issue overseas securities for funding purposes. In 2004, 11 corporations issued overseas depository receipts amounting to US\$3.26 billion; 59 corporations issued overseas corporate convertible bonds amounting to US\$7.01 billion; (ii) a Malaysian corporation was allowed to issue a Taiwan Depository Receipt (TDR) worth NT\$0.6 billion; and (iii) to reinforce Taiwan's relations with international financial organizations, the Council of Europe Development Bank (CEDB) was allowed to issue bonds with a ceiling of NT\$ 15 billion.
- (3) The MOF, after consultation with the Bank, adopted the following measures in order to loosen the restrictions on overseas securities investment: (i) 27 securities investment trust enterprises were allowed to invest a total of NT\$ 202 billion in foreign securities; (ii) 14 life insurance companies were allowed to invest a total of US\$6.9 billion in foreign securities with direct remittances, forex swaps or cross currency swaps; (iii) 7 life insurance companies

were allowed to invest a total of US\$0.58 billion in foreign securities through earmarked trust funds managed by financial institutions; (iv) 5 commercial banks are allowed to invest a total of US\$0.22 billion in foreign securities through assembled management accounts; and (v) the variety and scope of foreign securities allowed to be invested in by earmarked trust funds were revised to include offshore funds whose investments in the mainland China securities do not exceed 0.4 percent of the fund's net worth, and investments in mainland-China related securities not exceeding 5 percent of the fund's net worth. The minimum rating grade requirement for investible foreign bonds was lowered from A to BBB.

- (4) In order to facilitate capital movements, certain related remittance regulations were revised as follows: (i) the Regulation Governing the Declaration of Foreign Exchange Receipts and Disbursements or Transactions was revised on April 7, 2004 with the following major changes: (a) the regulations regarding the remittance documents to be certified by banks were revised to meet the requirement of the Financial Supervisory Commission on new international business such as allowing securities firms to conduct structured product transactions linked to foreign financial products; (b) forex declaration is required for investments in mainland China with an amount below US\$ 0.2 million; and (c) the declarant may apply for changing the content of the original declaration of foreign exchange receipts and disbursements or transactions with the submission of an accountant's opinion letter indicating no intentionally untruthful information; (ii) effective June 17, the Bank no longer reviews the remittance of investment principle and returns on domestic securities of foreign institutional investors; and (iii) effective October 20, banks can directly remit to mainland China with a ceiling of US \$0.1 million per transaction. However, if the remittance is made from mainland China, it should be subject to the Regulation Governing the Financial Business between the Taiwan Area and the Mainland Area.

Management of Authorized Foreign Exchange Banks

The Bank continued to approve banks' applications for becoming authorized foreign exchange banks and to approve authorized banks' applications for conducting derivative business. To maintain financial discipline, authorized banks that violate foreign exchange regulations were rectified and required to improve. By the end of 2004, there were 1,104 authorized foreign exchange banks, which included 43 domestic bank headquarters and 995 branches, and 66 foreign branches.

The Management of US Dollar Counterfeits

In July 2004, some banks incurred losses due to US dollar counterfeits and thus refused to accept US dollar bills. The Bank adopted the following measures to minimize counterfeit losses: (i) Notification letters were sent to banks purchasing/selling foreign currencies to remind them of the obligation to accept foreign currencies based on the listed prices, and requesting the reinforcement of counterfeit discriminating capabilities of bank employees and the purchase of new US dollar examination machines; and (ii) in order to enhance the detection method used by tellers at authorized foreign exchange banks, the Bank invited foreign experts on counterfeit discrimination to Taiwan twice in 2004 to give training courses on this subject.

Offshore Banking Business

Offshore banking units (OBUs) of local banks have been set up since December 1983 to enhance Taiwan's international financial activities and to establish Taipei as an Asian financial center. During 2004, the Bank promoted the Offshore Booking Center and cooperated with the Financial Supervisory Commission to promote financial business between the two sides of the Taiwan Strait, which stimulated the rapid growth of OBU business. Effective October 13, domestic banking units (DBUs) were allowed to act as agents on behalf of OBUs to conduct offshore forex deposit and inward remittance business.

4. Banking Supervision

To ensure the sound operations of financial institutions and maintain the stability of the financial system, the Bank conducted banking supervision in accordance with the mandate endowed by the Central Bank of China Act and consigned by the Ministry of Finance. Since the Financial Supervisory Commission commenced operations in July 2004, the Bank has ceased conducting regular banking supervision and has only conducted target examinations related to its policy in line with Central Bank of China Act.

Implementing On-site Examinations

During the first half of 2004, the Ministry of Finance, the Central Deposit Insurance Corporation and the Bank shared the responsibility to conduct on-site banking examinations. In addition, target examinations were conducted to accommodate the implementation of monetary policy, with information from off-site monitoring, major incidences and contingencies, and appeal and accusation cases serving as reference. In the second half of the year, the Bank only conducted target examinations related to its regulatory scope and monetary, credit and foreign exchange policy when necessary.

Supervising the Internal Auditing of Banks

During the first half of the year, the Bank strengthened the internal auditing of the banks under its supervision by reviewing their auditing reports and assessing their auditing performance in accordance with the guidelines evaluating the internal auditing of banks and bills finance companies.

Enhancing Off-site Monitoring

The Bank, when necessary, revised the reporting forms of financial institutions and adjusted the methods of auditing and reviewing these reports. The Bank also planned to establish additional report auditing systems for insurance companies, securities firms, futures commission merchants and bond funds.

Based on the reports submitted by financial institutions, the Bank assessed the operations, financial conditions and regulatory compliance of individual financial institutions by utilizing the report auditing system. The Bank then compiled analysis on various business practices and other information to serve as a reference for relevant supervisory agencies.

Adjusting Bank Examination Responsibilities

With the establishment of the Financial Supervisory Commission, existing banking supervisory responsibilities were integrated. The Bank accordingly adjusted the legal framework, organizational structure and duties of the Bank Examination Department. The Bank also invalidated 36 provisions it previously issued related to bank examination.

Other Important Measures

- (1) The Bank collaborated with the Financial Supervisory Commission and the Central Deposit Insurance Corporation to set up a single window for domestic banks, local branches of foreign banks and bills finance companies to submit banking supervision data. The Bank also streamlined the process for financial institutions to report to different departments of the Bank, eliminating duplicated procedures.
- (2) As some Internet banking customers found their savings illegally transferred, the Bank drew up measures for financial institutions to counter hacker attacks on Internet bank accounts.
- (3) To prevent currency forgery, the Bank regularly monitored the purchase and lease conditions of currency sorting machines by financial institutions.
- (4) The Bank seconded staff to the Financial Crime Investigation and Supervision Team under the Taiwan High Court to help investigate cases of financial crime.

5. Payment and Settlement Systems

Developments in the Payment and Settlement Systems

The Bank provides the final instrument of payment, namely New Taiwan dollar notes and coins. The Bank also supervises the clearing house system which handles the clearing and settlement of checks, promissory notes, and drafts among banks.

The two main subsystems under the CBC wire are the CBC Inter-bank Fund-transfer Settlement System (CIFS), and the Central Government Securities Settlement System (CGSS). The CIFS launched in May 1995 is an on-line, large-value fund transfer system. Since September 2002, the system has been operated in complete real-time gross settlement (RTGS). For the year 2004, the system handled a total value of NT\$193.6 trillion transactions, showing a 20.5 percent increase from 2003. The CGSS established in September 1997 is a real-time gross settlement system for the issuance, transfer, redemption, and interest payment of book-entry central government securities. Currently, the book-entry transactions of central government securities within a clearing bank can be made on a delivery-versus-payment (DVP) basis while those between clearing banks cannot. To reduce the settlement risk in inter-bank transactions, the Bank plans to link the CGSS with the CIFS to allow clearing banks to handle these settlements on a DVP basis as well.

Promoting the Bills Depository and Clearing System

The Debt Instruments Depository and Clearing Corporation (DIDC) was established in August 2003 to improve the efficiency and to reduce the settlement risk of short-term bills transactions.

With the help of the Bank, the Bills Depository and Clearing System was set up in April 2004 to replace the service of storing and delivering physical bills with an electronic funds transfer and reliable computerized book-entry facility. Since the system was linked with the Bank's CIFS at its inception, transactions of bills in a book-entry form have been processed on a DVP basis, which has greatly improved the settlement efficiency of bills transactions and reduced the default risk.

Enhancing the Check-Clearing System

In view of the common features shared by each check-clearing house business and their close relations, the Bank assisted the 16 district clearing houses around the country to consolidate themselves into a single juridical entity. The Taiwan Clearing House (TCH), consisting of the Taipei head office and 15 branch offices outside the Taipei area, was established in November

2002 to assume the check-clearing business. In 2004, the TCH handled a total value of NT\$26.6 trillion in the clearing of checks and bills, a decrease of 5.7 percent from 2003, mainly due to the popular use of inter-bank remittance transactions.

In order to promote the efficiency of check clearing and to facilitate funds management for enterprises, the Bank guided the TCH to enhance its computerized check-clearing operation. Through dividing the Taiwan area into north, middle and south exchange regions, the checks collected by clearing houses were exchanged in three processing centers located in Taipei, Taichung and Kaohsiung, respectively. The Bank then handles the final settlement for these processing centers. This quasi-centralized and electronic processing system is conducive to time-saving for check processing and reducing manual handling loads. It also facilitates funds management of both financial institutions and enterprises. Since January 2004, the 12 check clearing houses in western Taiwan area have all implemented this computerized operation. However, the branch offices in Ilan County, Hualien County, Taitung County, and Penghu County still process check clearing manually.

6. Currency Issuance

Increasing Currency in Circulation

According to Article 16 of the Central Bank of China Act, the NT dollar should be issued against a 100-percent reserve, in the form of gold and silver bullion, foreign exchange, and eligible bills and securities. The reserve remains in the special custody of the Bank.

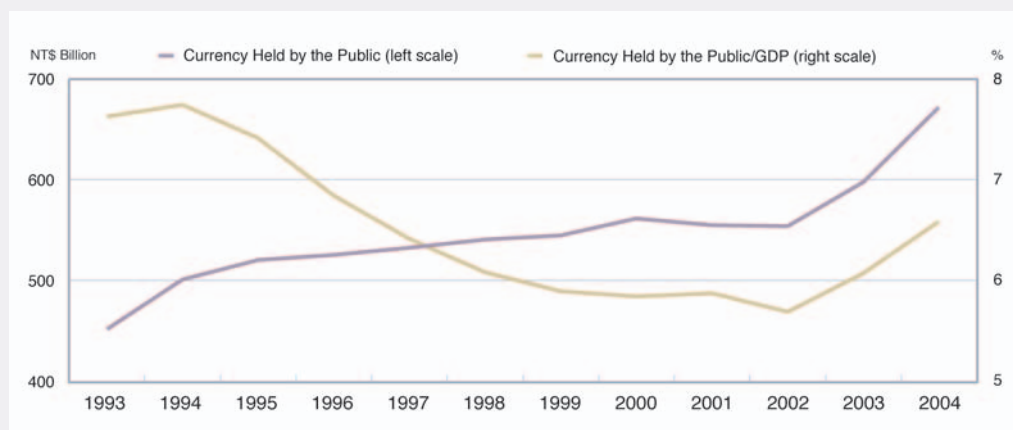
Although the traditional method of cash payment is being gradually replaced by plastic cards and other payment instruments, currency held by the public has exhibited a significant increase since 2003. The ratio of currency held by the public to nominal GDP rose from 5.7% at the end of 2002 to 6.6% at the end of 2004. The main reasons included the historically low interest rate which caused the public to hold more cash in their hands instead of depositing it in banks, and the rising demand for currency as economic activity gained momentum.

During the year 2004, the currency issued peaked at NT\$1,134 billion on January 20, the day before the Chinese Lunar New Year holidays, when there was a temporary seasonal surge in cash demand. The outstanding amount of currency issued at the end of 2004 was NT\$857 billion, which represented a 9.1 percent or NT\$72 billion increase from a year earlier.

With the release of several new notes in recent years, the Bank continued its efforts to raise public awareness of the new design and enhanced security features of the new notes.

At the end of 2004, the NT\$1,000 note constituted 85.1 percent of the total value of currency issued, while the NT\$100, NT\$500 and others (including the NT\$200 and NT\$2,000 notes) accounted for 6.1 percent, 4.9 percent, and 3.9 percent, respectively.

Currency Held by the Public and its Size Relative to GDP



7. Fiscal Agency Functions

Managing the Treasury Deposit Account

The Bank acts as the government's bank and manages the Treasury Deposit Account (TDA) on behalf of the MOF. All receipts and disbursements of the central government are made through this single account. Given only one head office, the Bank is allowed to delegate the businesses of treasury transactions to 15 financial institutions. The 346 nationwide and 5 overseas branches of these 15 financial institutions function as treasury agent institutions outside of Taipei city. There are another 4,408 tax revenue service offices over the country offering convenient services to government entities and the general public. In 2004, the Bank received a total of NT\$2,656 billion worth of treasury deposits, while it made NT\$2,637 billion government payments for the Treasury. As of the end of the year, the outstanding balance in the TDA was NT\$51 billion, an increase of NT\$19.5 billion from a year earlier.

Handling Central Government Institutions Deposits

Central government institutions are allowed to make their deposits with the Bank or other treasury agent institutions subject to the approval of the MOF. However, the delegated agent institutions are required to redeposit a certain percentage (currently the ratio is 60 percent) of the deposits with the Bank early each month, except those in interest-bearing accounts. At the end of the year, the balances of central government institutions deposits with the Bank and with other agent institutions amounted to NT\$126 billion and NT\$436 billion, respectively. Those redeposited by delegated agent institutions registered only NT\$22 billion.

Managing Central Government Securities

As a fiscal agent, The Bank on behalf of the MOF provides services related to the issuance, transfer, redemption, and interest payment of government securities. The auctions of central government bonds are conducted by the Bank. Currently, there are 77 domestic dealers qualified to submit tenders to the Bank in the auctions. In 2004, the Bank arranged 13 issues of central government bonds with a total amount of NT\$465 billion, of which 4 issues worth NT\$135 billion were auctioned on a reopen system. The reopen system was introduced by the Bank in April 2003 to establish benchmark yield curves and to increase bond market liquidity. In addition, the Bank paid a total of NT\$239 billion in principal and NT\$114 billion in interest payments for central government bonds during the year 2004. As of the end of the year, the outstanding amount of central government bonds was NT\$2,729 billion, an increase of NT\$25

billion from the end of 2003.

From September 1997 onwards, all new central government bonds were issued in book-entry form. The remaining outstanding physical bonds have also been gradually converted into book-entry form from January 1999. By the end of 2004, book-entry government bonds outstanding accounted for 99 percent of total outstanding central government bonds.

Treasury bills are sold at a discount through auctions. Participants in the auctions are limited to dealers, which includes banks, investment and trust companies, insurance companies, bills finance companies, and Chunghua Post Co. In 2004, the Bank arranged 6 issues of treasury bills with a total amount of NT\$131 billion. The outstanding amount of treasury bills at yearend 2004 was NT\$131 billion, an increase of NT\$25 billion from the end of 2003.

Adopting Single-price Auctions for Government Securities

Auctions can be conducted either in a single-price or multiple-price format. In a multiple-price auction, successful competitive bids are allotted in rising order of yield until the full amount of the issue is allotted, while in a single-price auction, successful competitive bids are allotted at the highest yield of accepted competitive bids. Previously, the Bank used multiple-price auctions to issue interest-bearing government bonds. To align with international standards and to encourage broader participation at auctions, given the premise that single-price auctions reduce the risks for less-informed bidders, the Bank changed its bonds auction system from the multiple-price format to the single-price format in July 2004. Due to the greater participation at the single-price auctions, the Bank can auction the bonds on more favorable terms so as to reduce the funding cost of the government. Furthermore, when the same price is applied to all accepted bids in the single-price auction, the volatility of bond yields in the secondary market is also reduced.

Planning the Issue of Exchangeable Government Bonds

To reduce government debt payment, the MOF plans to issue exchangeable government bonds, which can be swapped for shares in state-run or government-controlled companies.

The issue of exchangeable government bonds not only promotes the privatization of public enterprises, but also introduces a new financial product to the bond market. To ensure smooth transactions of exchangeable government bonds, the Bank has started the preparatory work from early this year, including the amendment of related regulations, development and test of computer systems, and personnel training. The necessary facilities were completed around the end of the year.

8. Participation in International Activities

The Republic of China is currently a full member of the Asian Development Bank (ADB), the Central American Bank for Economic Integration (CABEI), and the Conference of Governors of South East Asian Central Banks (SEACEN). The Bank attends the annual meetings, provides training courses, and hosts conferences so as to strengthen cooperation and relations with other member countries. In addition, the Bank also plays an active and extensive role in the Inter-American Development Bank (IDB), the European Bank for Reconstruction and Development (EBRD), and the Bank for International Settlements (BIS), among other international financial organizations.

In 2004, as a part of SEACEN activities, the Bank held a 4-day "Central Bank Internal Audit Workshop." There were 30 participants from 15 central banks. Lecturers came from the BIS, the Bank of Japan and other sources. The subject for the workshop included internal audit, corporate governance, risk management, application of information technology, legal impact, outsourcing of internal audit, and best practice of internal audit.





IV. ANNEX

- 1. Publication of Taiwan's International Investment Position Statistics**
- 2. Developments of the Offshore Banking Business in Taiwan**

IV. ANNEX

1. Publication of Taiwan's International Investment Position Statistics



Introduction

In line with the trend in international financial statistics and to enhance information disclosure, the Central Bank of China (CBC) started to disseminate Taiwan's international investment position (IIP) data in accordance with the Special Data Dissemination Standard (SDDS) of the International Monetary Fund (IMF) from June 2004 onwards. Yearend IIP data will be regularly released as of the end of next June*. In this annex, compilation of Taiwan's IIP is briefly introduced, which is followed by an analysis of its current situation and economic implication.

Definition of International Investment Position

The IIP is a new statistical statement introduced in the fifth edition of the *Balance of Payments Manual (BPM5)* of the IMF. IIP statistics show a country's stock of external assets and liabilities at the end of a reference period. The IIP and Balance of Payments (BOP) together constitute the set of international accounts for an economy. While the BOP financial account measures transactions in external assets and liabilities that have taken place during the reference period, IIP measures the stock of such assets and liabilities at the end of the period. IIP statistics reflect not only financial transactions, but also valuation changes and other adjustments that occurred during the specific period and affected the levels of external assets and liabilities.

Compilation of Taiwan's International Investment Position

The compilation of Taiwan's IIP statistics is in accordance with the guidelines contained in

* The data for Taiwan's IIP is available from the CBC website at www.cbc.gov.tw or the *Balance of Payments Quarterly, Taiwan District, the Republic of China*.

BPM5. The CBC uses existing stock data and revalues them at current market prices. If such stock data series are not available, the CBC will derive the corresponding stock value from flow data or other indirect data sources. Currently, the majority of data derived from indirect estimation are the stocks of external assets of the private non-bank sector. With respect to valuation methods, stock data valued at market prices are mostly available for assets and liabilities of portfolio investment. The aggregate stock data for direct investment abroad are mainly net worth estimates as most of the entities invested are not exchange-listed companies. Inward direct investment by non-residents is measured either at current market prices or net-worth, depending on the entities invested. The value of the stock of other investment is usually measured at book values.

Current State of Taiwan's International Investment Position

Due to a longstanding current account surplus, Taiwan's international investment registered net asset positions from 2000 onwards. Taiwan's net asset position reached US\$308.5 billion at

Taiwan's International Investment Position at Yearend

Unit: US\$ Billion

| | 2000 | 2001 | 2002 | 2003 |
|--|--------------|--------------|--------------|--------------|
| Assets | | | | |
| Direct investment abroad | 66.7 | 70.8 | 76.9 | 84.1 |
| Portfolio investment | 34.4 | 41.8 | 55.8 | 87.7 |
| Equity securities | 22.3 | 27.2 | 33.5 | 50.7 |
| Debt securities | 12.1 | 14.5 | 22.3 | 37.0 |
| Financial derivatives | 0.0 | 0.1 | 0.2 | 0.2 |
| Other investment | 92.7 | 100.5 | 95.6 | 100.1 |
| Trade credits | 2.0 | 1.6 | 1.8 | 1.7 |
| Loans | 26.0 | 32.7 | 30.3 | 32.2 |
| Currency and deposits | 35.4 | 38.7 | 35.0 | 36.7 |
| Other assets | 29.3 | 27.6 | 28.5 | 29.4 |
| Reserve assets | 111.4 | 126.6 | 166.0 | 211.1 |
| Total assets | 305.1 | 339.7 | 394.5 | 483.2 |
| Liabilities | | | | |
| Direct investment in Taiwan, R.O.C | 17.6 | 38.0 | 28.1 | 37.1 |
| Portfolio investment | 33.4 | 44.1 | 38.4 | 82.9 |
| Equity securities | 29.1 | 39.7 | 32.2 | 72.6 |
| Debt securities | 4.3 | 4.4 | 6.1 | 10.2 |
| Financial derivatives | 0.0 | 0.0 | 0.1 | 0.2 |
| Other investment | 32.0 | 35.4 | 43.2 | 54.6 |
| Trade credits | 2.1 | 1.7 | 2.1 | 2.5 |
| Loans | 8.4 | 9.5 | 12.0 | 12.3 |
| Currency and deposits | 19.6 | 22.8 | 27.2 | 37.4 |
| Other liabilities | 1.9 | 1.4 | 1.8 | 2.3 |
| Total liabilities | 83.0 | 117.6 | 109.7 | 174.7 |
| Net International Investment Position | 222.1 | 222.1 | 284.8 | 308.5 |

Source: Balance of Payments, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

The World's Top 10 Countries Ranked by International Investment Position at Yearend 2003

Unit: US\$ Billion

| Rank | Net Asset Position | | Assets | | Liabilities | |
|------|--------------------|---------|----------------|---------|----------------|----------|
| | Countries | Value | Countries | Value | Countries | Value |
| 1 | Japan | 1,613.6 | United States | 7,864.0 | United States | 10,515.0 |
| 2 | Switzerland | 469.0 | United Kingdom | 6,335.3 | United Kingdom | 6,428.8 |
| 3 | Hong Kong | 397.7 | Germany | 3,963.6 | Germany | 3,794.1 |
| 4 | Taiwan | 308.5 | Japan | 3,599.8 | France | 3,380.8 |
| 5 | Germany | 169.6 | France | 3,513.0 | Japan | 1,986.2 |
| 6 | France | 132.2 | Netherlands | 1,933.5 | Netherlands | 1,978.6 |
| 7 | Belgium | 127.5 | Switzerland | 1,760.1 | Italy | 1,643.7 |
| 8 | Singapore | 76.0 | Italy | 1,559.9 | Spain | 1,360.9 |
| 9 | Venezuela | 10.3 | Ireland | 1,282.7 | Ireland | 1,314.3 |
| 10 | Botswana | 5.6 | Belgium | 1,234.1 | Switzerland | 1,291.1 |
| ⋮ | ⋮ | | ⋮ | | ⋮ | |
| | | | Taiwan(14th) | 483.2 | Taiwan(25th) | 174.7 |

Sources : 1. Balance of Payments, Taiwan District, the Republic of China, Department of Economic Research, Central Bank of China.

2. International Financial Statistics, January 2005, IMF.

the end of 2003, the fourth highest figure in the world, after Japan, Switzerland, and Hong Kong.

Total external assets continued to rise since 2000 and amounted to US\$483.2 billion at yearend 2003, ranking 14th largest in the world. The CBC's reserve assets commanded the lion's share, accounting for 44 percent of the total value at yearend 2003. The increase in Taiwan's external assets was mainly driven by the expansion of the CBC's foreign reserve assets and residents' portfolio investment abroad. Portfolio investment abroad by residents continued its upward trend mainly due to the increased exposure to global investment tools and increased foreign security holdings through the purchases of overseas mutual funds. Insurance companies also expanded their investment in foreign securities with the aim of enhancing earnings.

Taiwan's total external liabilities amounted to US\$174.7 billion at yearend 2003, the 25th largest in the world. Portfolio investment by non-residents claimed the lion's share, accounting for 47 percent of the total value at yearend 2003. The increase in total external liabilities was primarily the result of an increase in inward portfolio investment, which was attributable to inflows of foreign capital, an increase in issues of offshore corporate bonds and depositary receipts by residents, as well as a considerable rise in local equity prices.

The Economic Implication of Taiwan's International Investment Position Statistics

1. The Rise of the Financial Openness Ratio in Taiwan as a Result of a Higher Degree of Financial Glob-

alization

Financial openness can be captured by the ratio of the stock of external assets and liabilities of direct investment and portfolio investment to GDP. The financial openness ratio for Taiwan has been rising over the past few years, from 0.49 at yearend 2000 to 1.02 at the end of 2003, reflecting the effects of financial liberalization and globalization in recent years.

2. Low Risk of Financial Instability in View of the High Ratio of Foreign Direct Investment Stock to External Debt

Direct investment is the least volatile among all kinds of capital flows. The high ratio of foreign direct investment to external debt implies a lower risk of financial instability in view of the reliable source of external finance. The ratio of foreign direct investment stock to external debt was 0.59 at yearend 2003, the 17th highest ranking compared with the IMF's 58 SDDS subscribing economies.

3. Low Liquidity Risk as Seen in the High Ratio of Reserve Assets to Short-term External Debt

Adequate reserve assets held by monetary authorities can maintain sufficient liquidity and provide confidence in authorities' commitment to support the value of the domestic currency. The higher the ratio to short-term external debt of reserve assets would translate into a lower probability of financial crisis and lessened impact should such a crisis occur. The ratio of reserve assets to short-term external debt for Taiwan stood at 4.4 at yearend 2003, higher than the average of 3.4 of developing countries.

4. Risk Assessment of the Structure of Assets and Liabilities

Taiwan has been standing as a net creditor. In such a context, risk primarily associates with a general fall in foreign asset prices or a depreciation of foreign currencies, which would lead to a decrease in the local dollar value of foreign currency denominated assets. Equity investment by the private non-bank sector was relatively larger than those of monetary authorities, government, or banks. As a result, external asset and liability positions of the private sector are more vulnerable to price revaluation driven by equity price movements, and in turn, changes of these positions will significantly affect investment and consumption decisions.

Conclusion

The rapid increase in the mobility and volume of cross border capital flows in Taiwan highlights the growing importance of regular and timely disclosure of IIP statistics for risk assessment practice and investment policy. Therefore, the regular publication of Taiwan's IIP statistics helps provide significant insights in sound economic policy-making, credit rating analysis, as well as corporate investment strategy.

2. Developments of the Offshore Banking Business in Taiwan

Introduction

The offshore banking business of local banks situated in Taiwan was first set up in 1983. Relaxation of financial regulations and growing overseas investment by local firms in recent years have increased the demand for offshore financial services. Over the years, the offshore banking units (OBUs) of banks have developed into one of the major financial channels for overseas subsidiaries of Taiwanese enterprises. This annex will provide a brief review of the developments of offshore banking business in Taiwan.

Origin of Offshore Banking Units

The Offshore Banking Act was promulgated in December 1983 to promote the integration of local banks into international financial markets. It authorized banks to set up offshore banking branches within Taiwan. The first OBU was set up in June 1984.

OBUs are permitted to undertake foreign currency denominated transactions only, offering services mainly to non-residents. OBUs are exempt from reserve requirements, business income tax, business tax, and stamp duties; the interest paid to non-residents is also exempt from withholding tax. Originally, OBUs were limited to accept deposits and extend credit in foreign currencies as well as conducting other foreign exchange transactions with overseas financial markets.

The early operation of Taiwan's OBUs was very limited due to the lack of competitiveness of domestic banks in international financial markets. Usually, OBUs obtained their loans from foreign financial institutions to extend credit to domestic financial institutions. They also took part in syndication loans, but predominantly those which were extended to large domestic companies in Taiwan or the latter's overseas subsidiaries. In short, both their size and operating profits were limited and they failed to play their expected role in international financial markets.

The Role of Offshore Banking Units in the Cross-Strait Business

With the emergence of China's economy and the increasing overseas investment activities by Taiwan's enterprises, the demand for funding overseas business and related financial services from domestic firms in Taiwan continued to grow. The majority of domestic firms set up their

offshore subsidiaries in a third country to facilitate their cross-strait business operations. In light of this, the government authorized OBUs to engage in trade-related banking business and offer services in financial derivative products to non-residents in May 1992. Since then, OBUs have served as a major channel enabling domestic companies to conduct cross-strait business operations through their offshore subsidiaries, facilitating the overseas operations of local firms.

For the past few years the government has made further efforts in expanding the lines of business of OBUs to encourage domestic firms to shift their funds overseas back to Taiwan and use the OBUs as their funding management centers. This has not only balanced the flows of funds across the Taiwan Strait but also strengthened the competitiveness of the domestic banking industry.

Recent Deregulation in Offshore Banking Business

One of the major deregulation efforts was to increase the access to offshore banking services. In the beginning, the offshore banking operations of domestic banks in Taiwan were conducted through independent branches. This is different from the international practice of maintaining separate accounting records rather than setting up branch offices. As there was only one OBU branch per bank and they were mostly located in Taipei, it was inconvenient for firms to access such services.

From the year 2000, the domestic branches of banks were allowed to act as agents on behalf of their OBUs to meet the offshore financial needs of local firms. The offshore businesses that domestic banking units (DBUs) may conduct on behalf of their OBUs have been gradually expanded to include import and export financing, deposits and loans in foreign currencies, and inward and outward remittances. There were around 70 OBUs as of year-end 2004 and more than 1,100 domestic branches of banks that may act as agents on behalf of their offshore units.

Initially, OBUs had to conduct trade financing and remittances through foreign financial institutions via a third country. But from June 2001, Taiwan's OBUs were allowed to engage in business directly with financial institutions in China. This significantly reduced the amount of time and fees involved. In November 2001, the Central Bank of China allowed offshore subsidiaries of local firms to make inward remittances for the usage of the parent company without being subject to the US\$50 million ceiling. This made it possible for parent companies to utilize the funds deposited at OBUs by their offshore subsidiaries. It also encouraged firms to transfer funding back to Taiwan through OBUs and establish Taiwan as the funding management

center for local enterprises.

Other measures adopted include allowing banks to provide credit and factoring services to Taiwanese enterprises operating in China from August 2002. In November 2004, OBUs were also permitted to extend credit in foreign currencies to the offshore subsidiaries of domestic firms to be used in China. In January 2005, offshore firms were allowed to obtain credit from OBUs by sharing their domestic parent firms' DBU credit lines secured by onshore assets. These measures greatly improved the availability of funding for firms.

In addition, OBUs also provided non-delivery forwards and options (NDFs and NDOs) businesses of US dollars against Chinese renminbi from August 2003 to offer firms with the financial products to hedge their foreign exchange exposure.

Current State of Offshore Banking Units

As a result of the above measures, OBU operations have grown steadily in recent years. As of the end of 2004, 70 banks in Taiwan were engaged in OBU operations. These include 42 domestic banks and 28 foreign banks. Total assets of all OBUs amounted to US\$69.2 billion at the end of 2004, triple those of 1991, and increasing 11 percent compared to the previous year.

Outstanding deposits and loans made by non-financial institutions also grew substantially. Deposits made by non-financial institutions at year-end 2004 amounted to NT\$18.8 billion, a 15-fold increase compared to that in 1991, and a growth of 15 percent compared to the previous year. Loans to non-financial institutions and non-residents reached NT\$15.3 billion, growing 18 percent compared to the previous year, or a 7-fold increase over 1991.

Total cross-strait remittances made through all OBUs reached NT\$8 billion in December 2004, a 22-fold increase compared to the NT\$0.35 billion in June 2001, when direct remittances were first authorized. The pre-tax earnings from the OBUs of domestic banks account for 10.3 percent of their total earnings in 2004.

Conclusion

The recent developments of the offshore banking business in Taiwan show that not only have OBUs become an important source of income for domestic banks, they have also developed into funding centers for Taiwanese enterprises in managing their overseas operations.

Looking forward, OBU operations will continue to provide firms with the services they require in setting up Taiwan as their global operating center. They will also provide vital sources of income for banks and facilitate their involvement in international financial markets.

Chronology of Important Events of the Central Bank of China in 2004

| Date | Events |
|---------|---|
| Feb. 3 | The Ministry of Finance and the Bank opened the market for foreign investors to invest in money market mutual funds. |
| Mar. 29 | The Bank lowered the remunerative rate on banks' required reserves (B account) from 1.75 percent to 1.5 percent. |
| Apr. 2 | The Bank assisted the Ministry of Finance to set up the Bills Central Depository and Clearing System with a direct link to the CBC Interbank Funds Transfer System (CIFS). |
| May 21 | The Ministry of Finance and the Bank allowed local financial institutions to offer intra-day overdraft facilities and temporary advances to foreign investors. |
| May 26 | The Bank amended the <i>Regulations Governing Foreign Exchange Business of Banking Enterprises</i> to allow authorized banks to conduct foreign exchange derivatives business not involving the New Taiwan Dollar by notifying the CBC after such business has commenced. |
| May 27 | The Ministry of Finance and the Bank allowed foreign investors to hedge their futures positions and repatriate proceeds from selling borrowed securities, effective June 30, 2005. |
| May 30 | The total amount of funds for local banks as a whole to extend preferential housing loans was further increased from NT\$1,200 billion to NT\$1,500 billion. |
| Jun. 30 | The Bank released Taiwan's International Investment Position (IIP) Statistics for the period between 2001 and 2003 in accordance with the Special Data Dissemination Standard (SDDS) of the International Monetary Fund. |
| Jul. 1 | The Financial Supervisory Commission of the Executive Yuan was established. |

(Continued)

| | | |
|-------|----|--|
| | | The Bank will no longer undertake the responsibilities of financial supervision except for those related to the Bank's monetary, credit and foreign exchange policies. |
| Sept. | 8 | Securities investment trust enterprises only needed to apply to the Bank for raising foreign currency denominated mutual funds with the required documents once. |
| Oct. | 1 | The Bank raised the discount rate, the rate on accommodations with collateral, and the rate on accommodations without collateral by 25 basis points to 1.625 percent, 2 percent and 3.875 percent, respectively. |
| Oct. | 13 | The Bank allowed domestic banking units (DBUs) to act on behalf of offshore banking units (OBUs) of the same bank in foreign currency deposit and foreign exchange inward remittance operations. |
| Oct. | 20 | The Bank allowed authorized banks to apply for offering discretionary foreign exchange-related margin trading services. |
| Oct. | 26 | The Bank allowed authorized banks to apply for permission to trade weather options. |
| Nov. | 8 | The total amount of funds for local banks as a whole to extend preferential loans to traditional industries was further increased from NT\$1,400 billion to NT \$1,850 billion. |
| Dec. | 31 | <p>The Bank raised the discount rate, the rate on accommodations with collateral, and the rate on accommodations without collateral by 12.5 basis points to 1.75 percent, 2.125 percent and 4 percent, respectively.</p> <p>The Bank set the intermediate target corridor for M2 growth in 2005 at 3.5 to 7.5 percent.</p> |

Financial Statements of the Central Bank of China

1. Balance Sheet

| Unit: NT\$ Million | | | | |
|--|---------------------|---------------------|-----------------|---------------|
| | December 31 2004 | December 31 2003 | Change | |
| | | | Amount | % |
| Assets | | | | |
| Foreign Assets | 7,832,744 | 7,178,834 | 653,910 | 9.11 |
| Deposits to Financial Institutions | 26,990 | 11,884 | 15,106 | 127.11 |
| Loans and Accommodations to Financial Institutions | 463,269 | 796,009 | -332,740 | -41.80 |
| Other Assets | 194,039 | 158,597 | 35,442 | 22.35 |
| Total Assets | 8,517,042 | 8,145,324 | 371,718 | 4.56 |
| Liabilities | | | | |
| Currency Issued | 856,951 | 785,164 | 71,787 | 9.14 |
| Reserve Deposits of Financial Institutions | 862,810 | 836,000 | 26,810 | 3.21 |
| Certificates of Deposit Issued | 3,562,885 | 2,992,365 | 570,520 | 19.07 |
| Redeposits of Financial Institutions | 1,900,870 | 2,081,698 | -180,828 | -8.69 |
| Government Deposits | 178,874 | 157,227 | 21,647 | 13.77 |
| Other Liabilities | 327,224 | 91,568 | 235,656 | 257.36 |
| Total Liabilities | 7,689,614 | 6,944,022 | 745,592 | 10.74 |
| Net Worth | 827,428 | 1,201,302 | -373,874 | -31.12 |
| Total Liabilities and Net Worth | 8,517,042 | 8,145,324 | 371,718 | 4.56 |

2. Income Statement

| Unit: NT\$ Million | | |
|---------------------------------|----------------|----------------|
| | 2004 | 2003 |
| Income | | |
| Interest Income | 329,141 | 322,213 |
| Fee Income | 113 | 97 |
| Subsidiaries Investment Income | 981 | 1,004 |
| Revenue from Trust Investment | 4,232 | 6,089 |
| Others | 9,178 | 2,383 |
| Total Income | 343,645 | 331,786 |
| Expenses | | |
| Interest Expenses | 85,320 | 80,170 |
| Fee Expenses | 15 | 14 |
| Expenses for Coin Issuance | 748 | 1,034 |
| Expenses for Bank Note Issuance | 2,390 | 2,988 |
| Operating Expenses | 1,765 | 1,735 |
| Administrative Expenses | 329 | 330 |
| Others | 52,025 | 1,892 |
| Total Expenses | 142,592 | 88,163 |
| Net Income | 201,053 | 243,623 |

Major Economic and Financial Indicators of Taiwan, R.O.C.

| Year / Month | I. Business Indicators | | II. National Income and Aggregate Demand | | | | | | | | | | |
|--------------------|---|---|--|------------------------------------|--------------------------------------|--|--|---|--|--|--|------------------------|---|
| | C.E.P.D. ⁽¹⁾ Monitoring Indicator (average) | T.I.E.R. ⁽²⁾ Manufacturing Business Climate Index (1991=100) (average) | Economic Growth Rate (%) | Per Capita GNP (US\$) | Unemploy- ment Rate (%) | Manufacturing sector | | | | | Annual Rate of Change of Industrial Production Indices(%) | | |
| | | | | | | Labor Productivity Index (2001=100) | Average Monthly Earnings Per Employee (NT\$) | Average Monthly Working Hours (hrs) | Capacity Utilization Rate (%) | Operating Profit Rate (%) | General Index | Manufacturing Index | Index of Building Construc- tion |
| | | | | | | | | | | | | | |
| 1994 | 32 | 102.53 | 7.11 | 11,806 | 1.56 | 67.58 | 30,803 | 202.40 | 78.34 | 6.00 | - | 5.72 | 23.90 |
| 1995 | 24 | 97.37 | 6.42 | 12,686 | 1.79 | 72.60 | 32,555 | 201.60 | 78.97 | 5.90 | - | 5.27 | -4.15 |
| 1996 | 20 | 96.11 | 6.10 | 13,260 | 2.60 | 76.36 | 33,911 | 201.10 | 78.25 | 5.10 | - | 2.67 | -17.46 |
| 1997 | 27 | 104.35 | 6.37 | 13,556 | 2.72 | 80.64 | 35,492 | 201.80 | 78.70 | 5.20 | 6.16 | 7.23 | -16.16 |
| 1998 | 20 | 94.58 | 4.33 | 12,307 | 2.69 | 84.93 | 36,546 | 198.00 | 78.84 | 4.90 | 3.39 | 3.18 | 0.55 |
| 1999 | 22 | 103.06 | 5.32 | 13,177 | 2.92 | 90.70 | 37,882 | 199.10 | 78.91 | 4.60 | 7.37 | 7.79 | 6.61 |
| 2000 | 26 | 100.29 | 5.78 | 14,114 | 2.99 | 96.36 | 39,080 | 198.70 | 80.35 | 4.80 | 6.92 | 8.06 | -14.65 |
| 2001 | 10 | 92.39 | -2.22 | 12,798 | 4.57 | 100.00 | 38,586 | 184.40 | 76.28 | 3.97 | -7.81 | -8.36 | -11.19 |
| 2002 | 24 | 106.89 | 3.94 | 12,884 | 5.17 | 109.55 | 38,565 | 187.60 | 77.02 | 4.69 | 7.92 | 9.39 | -20.66 |
| 2003 | 23 | 108.10 | 3.33 | 13,139 | 4.99 | 115.34 | 39,583 | 188.30 | 78.32 | 4.78 | 7.10 | 7.38 | 8.87 |
| 2004 | 33 | 100.74 | 5.71 | 14,032 | 4.44 | 122.13 | 40,611 | 190.70 | 80.08 | 5.04 | 9.85 | 10.55 | 4.93 |
| 2004/ 1 | 35 | 117.46 | | | 4.53 | 128.26 | 74,298 | 160.60 | 77.10 | 4.70 | -0.99 | 0.23 | -33.30 |
| 2 | 34 | 118.21 | | | 4.61 | 123.76 | 38,010 | 181.50 | 79.30 | 5.20 | 30.03 | 31.25 | 50.21 |
| 3 | 36 | 116.07 | 6.72 | 3,613 | 4.45 | 121.96 | 36,604 | 200.80 | 81.00 | 5.40 | 16.10 | 17.28 | 7.83 |
| 4 | 37 | 114.71 | | | 4.36 | 121.56 | 37,051 | 194.80 | 80.50 | 5.20 | 13.61 | 14.84 | -2.50 |
| 5 | 39 | 111.93 | | | 4.41 | 125.72 | 36,881 | 191.50 | 80.30 | 5.20 | 16.39 | 17.24 | 7.72 |
| 6 | 36 | 110.00 | 7.88 | 3,273 | 4.54 | 122.41 | 38,705 | 190.80 | 80.30 | 5.00 | 15.99 | 17.31 | -3.50 |
| 7 | 35 | 112.57 | | | 4.62 | 117.93 | 38,475 | 198.10 | 80.70 | 5.10 | 9.18 | 10.54 | -5.08 |
| 8 | 33 | 110.85 | | | 4.67 | 121.15 | 36,521 | 191.90 | 80.50 | 5.00 | 8.53 | 9.73 | -10.93 |
| 9 | 32 | 109.85 | 5.27 | 3,485 | 4.50 | 122.37 | 37,660 | 190.00 | 80.40 | 5.00 | 8.25 | 9.09 | -1.15 |
| 10 | 29 | 104.20 | | | 4.31 | 124.54 | 36,933 | 190.70 | 80.40 | 5.00 | 2.88 | 3.01 | 8.17 |
| 11 | 28 | 102.66 | | | 4.14 | 119.37 | 36,905 | 195.90 | 80.10 | 4.90 | 5.73 | 5.13 | 37.07 |
| 12 | 26 | 100.33 | 3.25 | 3,661 | 4.09 | 118.22 | 39,953 | 200.70 | 80.30 | 4.80 | -0.68 | -1.69 | 31.96 |

Notes:(1) C.E.P.D.: Council for Economic Planning and Development, Executive Yuan.

(2) T.I.E.R.: Taiwan Institute of Economic Research.

Sources: 1. Taiwan Business Indicators, the Council for Economic Planning and Development.

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6. Monthly Bulletin of Earnings and Productivity Statistics, Taiwan Area, the Republic of China, Directorate-General of Budget, Accounting and Statistics.

7. Monthly Statistics of Exports and Imports, Taiwan Area, the Republic of China, Ministry of Finance.

8. Monthly Statistics of Export Orders, Ministry of Economic Affairs.

9. Price Statistics Monthly in Taiwan Area of the Republic of China, Directorate-General of Budget, Accounting and Statistics.

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| Year / Month | II. National Income and Aggregate Demand | | | | | | | | | | | | | | |
|----------------------------|--|-------------------------------|----------------|---------------------------------|------------------------------------|---|----------------|--------|--------|--------|-------------------------------|-----------------------|------------------------------|--|-------------------|
| | Annual Rate of Change of Domestic Demand (%) | | | Gross National Savings Rate (%) | Gross Domestic Investment Rate (%) | External Trade of Goods (In US Dollars) | | | | | | | | | |
| | Private Consumption Expenditure | Gross Fixed Capital Formation | Private Sector | | | Annual Rate of Change of Exports | | | | | Annual Rate of | | Trade Balance (US\$ Million) | Annual Rate of Change of Export Orders (%) | |
| | | | | | | (%) | China and H.K. | U.S. | Japan | Europe | Southeast Asia ⁽¹⁾ | Change of Imports (%) | | | Capital Equipment |
| 1994 | 8.46 | 7.42 | 9.89 | 27.62 | 24.97 | 9.3 | 15.84 | 3.20 | 13.90 | 0.20 | 21.60 | 10.76 | 4.6 | 7,699 | 10.14 |
| 1995 | 5.71 | 7.38 | 11.25 | 27.04 | 24.93 | 20.0 | 23.78 | 8.50 | 28.80 | 21.64 | 30.48 | 21.33 | 23.9 | 8,108 | 20.05 |
| 1996 | 6.54 | 1.67 | 3.54 | 26.73 | 22.87 | 3.8 | 3.51 | 1.70 | 3.90 | 7.76 | 3.13 | -1.14 | 8.7 | 13,572 | 4.76 |
| 1997 | 7.00 | 10.57 | 18.34 | 26.35 | 23.94 | 5.2 | 6.94 | 10.00 | -14.30 | 8.68 | 5.12 | 11.78 | 18.4 | 7,656 | 4.07 |
| 1998 | 6.42 | 7.80 | 11.62 | 25.99 | 24.72 | -9.4 | -12.49 | -0.60 | -20.20 | 6.64 | -27.85 | -8.53 | 11.8 | 5,916 | -4.00 |
| 1999 | 5.35 | 1.77 | -0.80 | 25.95 | 23.19 | 9.9 | 11.28 | 5.20 | 27.80 | 3.48 | 20.22 | 5.76 | 20.3 | 10,901 | 7.26 |
| 2000 | 4.84 | 8.38 | 15.12 | 25.37 | 22.52 | 21.9 | 24.54 | 12.70 | 39.60 | 16.70 | 28.81 | 26.49 | 34.3 | 8,309 | 20.36 |
| 2001 | 1.00 | -21.14 | -29.12 | 23.76 | 17.36 | -17.2 | -10.82 | -20.50 | -23.10 | - | -19.23 | -23.41 | -31.6 | 15,628 | -11.54 |
| 2002 | 2.07 | -1.61 | 3.12 | 25.21 | 16.33 | 6.3 | 28.65 | -3.20 | -6.00 | -6.33 | 6.41 | 4.94 | -3.5 | 18,066 | 11.23 |
| 2003 | 0.84 | -2.05 | -1.62 | 25.97 | 16.09 | 10.4 | 22.10 | -3.10 | -0.50 | 10.20 | 9.97 | 13.10 | 0.4 | 16,931 | 12.64 |
| 2004 | 3.13 | 15.40 | 28.20 | 26.15 | 19.99 | 20.7 | 28.30 | 8.40 | 10.80 | 14.60 | 33.67 | 31.90 | 38.2 | 6,138 | 26.50 |
| 2004/ 1 | | | | | | 17.4 | 27.30 | -2.30 | 11.10 | 22.70 | 27.85 | 11.30 | 12.2 | 1,236 | 7.05 |
| 2 | | | | | | 34.3 | 62.20 | 2.80 | 15.30 | 28.10 | 52.25 | 56.40 | 55.8 | 39 | 34.68 |
| 3 | 3.68 | 13.63 | 21.78 | 23.57 | 16.38 | 17.0 | 22.90 | 7.40 | 4.70 | 21.80 | 24.64 | 29.00 | 36.8 | 671 | 27.81 |
| 4 | | | | | | 22.8 | 38.80 | -2.20 | 14.60 | 14.10 | 39.39 | 25.70 | 43.8 | 959 | 33.55 |
| 5 | | | | | | 39.4 | 55.20 | 23.50 | 16.60 | 34.10 | 48.62 | 52.50 | 66.0 | 1,193 | 25.88 |
| 6 | 4.32 | 19.44 | 33.13 | 27.66 | 20.70 | 24.4 | 36.40 | 15.30 | 0.60 | 13.90 | 36.27 | 42.20 | 54.8 | -210 | 28.01 |
| 7 | | | | | | 26.0 | 41.70 | 7.50 | 17.80 | 13.40 | 32.31 | 32.80 | 26.9 | 880 | 27.83 |
| 8 | | | | | | 19.9 | 22.40 | 12.80 | 14.20 | 15.50 | 34.45 | 33.60 | 38.4 | 847 | 25.54 |
| 9 | 1.41 | 13.72 | 26.44 | 24.80 | 18.56 | 19.0 | 22.60 | 6.30 | 17.30 | 9.30 | 41.99 | 29.40 | 45.8 | 731 | 26.61 |
| 10 | | | | | | 17.4 | 17.80 | 9.60 | 8.20 | 11.20 | 44.94 | 38.10 | 38.8 | 331 | 25.46 |
| 11 | | | | | | 12.4 | 11.70 | 15.50 | 8.50 | 2.80 | 15.37 | 20.70 | 31.5 | 559 | 30.11 |
| 12 | p 3.27 | 14.88 | 30.41 | 28.69 | 24.36 | 6.2 | 5.60 | 4.30 | 6.10 | 1.30 | 14.92 | 21.30 | 24.0 | -1,116 | 25.97 |

Note:(1) Only includes six major countries in the region, i.e., Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam.

(Continued)

| Year / Month | III. Prices | | | | | IV. Money, Banking and Finance | | | | | | |
|----------------------------|--|-------------------------|------------------------------|---------------------------------|---|---------------------------------|----------------------------|--|----------------------------------|-------|----------|-------|
| | Consumer Price Indices | | Wholesale Price Index | Import Price Index | Export Price Index | Unit Labor Cost Index | Reserve Money (average) | | Monetary Aggregates (average) | | | |
| | General Index | Core CPI ⁽¹⁾ | | | | | Amount | Adjusted Annual Growth Rate ⁽²⁾ (%) | M1B | | M2 | |
| | | | Amount (NT\$ Billion) | Annual Growth Rate (%) | Amount ⁽³⁾ (NT\$ Billion) | Annual Growth Rate (%) | | | | | | |
| | (Annual Rate of Change, %; 2001=100) | | | | | | | | | | | |
| 1994 | 4.10 | 3.24 | 2.17 | 5.11 | 0.57 | 2.73 | 1,620.7 | 13.46 | 2,897.5 | 16.94 | 10,926.0 | 16.29 |
| 1995 | 3.67 | 3.57 | 7.38 | 10.15 | 6.89 | -1.08 | 1,719.1 | 8.69 | 3,035.5 | 4.76 | 12,192.4 | 11.59 |
| 1996 | 3.08 | 3.07 | -1.01 | -2.49 | 1.67 | -0.61 | 1,641.9 | 5.63 | 3,160.8 | 4.13 | 13,318.3 | 9.23 |
| 1997 | 0.89 | 0.96 | -0.45 | -1.40 | 2.05 | -1.24 | 1,695.4 | 7.30 | 3,597.8 | 13.83 | 14,417.9 | 8.26 |
| 1998 | 1.69 | 1.07 | 0.60 | 0.74 | 5.57 | -0.18 | 1,646.0 | 4.78 | 3,688.5 | 2.52 | 15,680.5 | 8.76 |
| 1999 | 0.17 | 1.16 | -4.55 | -4.10 | -8.53 | -3.38 | 1,518.7 | 5.37 | 4,052.6 | 9.87 | 16,986.2 | 8.33 |
| 2000 | 1.26 | 0.60 | 1.82 | 4.63 | -0.88 | -2.63 | 1,566.8 | 5.00 | 4,481.5 | 10.58 | 18,182.6 | 7.04 |
| 2001 | -0.01 | 0.08 | -1.34 | -1.25 | 0.32 | 2.69 | 1,539.1 | 1.13 | 4,435.8 | -1.02 | 19,236.0 | 5.79 |
| 2002 | -0.20 | 0.69 | 0.05 | 0.40 | -1.49 | -10.28 | 1,417.4 | 1.78 | 5,190.4 | 17.01 | 19,918.3 | 3.55 |
| 2003 | -0.28 | -0.61 | 2.48 | 5.14 | -1.49 | -2.84 | 1,492.3 | 5.28 | 5,803.9 | 11.82 | 20,669.8 | 3.77 |
| 2004 | 1.62 | 0.71 | 7.03 | 8.57 | 1.61 | -4.26 | 1,662.2 | 11.38 | 6,905.4 | 18.98 | 22,209.3 | 7.45 |
| 2004/1 | 0.01 | 0.38 | 2.47 | 4.34 | -1.28 | 8.15 | 1,704.2 | 14.44 | 6,648.2 | 20.56 | 21,658.2 | 6.53 |
| 2 | 0.65 | -0.03 | 2.22 | 2.32 | -2.68 | -19.70 | 1,665.1 | 7.74 | 6,746.6 | 20.42 | 21,909.4 | 6.80 |
| 3 | 0.89 | 0.01 | 2.72 | 4.05 | -2.53 | -9.47 | 1,659.5 | 12.76 | 6,813.4 | 23.75 | 22,037.3 | 7.89 |
| 4 | 0.95 | 0.17 | 4.88 | 6.47 | -1.36 | -6.72 | 1,670.5 | 14.63 | 6,879.2 | 24.39 | 22,138.5 | 8.47 |
| 5 | 0.91 | 0.66 | 6.93 | 9.34 | 0.65 | -11.29 | 1,653.7 | 12.99 | 6,861.4 | 23.55 | 22,161.2 | 8.58 |
| 6 | 1.73 | 1.26 | 7.58 | 9.76 | 1.25 | -4.77 | 1,626.2 | 11.50 | 6,782.3 | 20.20 | 22,067.4 | 7.93 |
| 7 | 3.34 | 1.32 | 9.39 | 11.81 | 3.21 | -1.50 | 1,636.2 | 10.52 | 6,880.0 | 18.99 | 22,223.7 | 7.79 |
| 8 | 2.55 | 1.05 | 10.43 | 13.66 | 4.77 | -5.74 | 1,647.4 | 11.62 | 6,966.9 | 18.04 | 22,318.2 | 7.31 |
| 9 | 2.78 | 0.99 | 11.39 | 14.35 | 5.54 | -3.05 | 1,661.4 | 11.09 | 7,041.0 | 16.81 | 22,355.2 | 7.07 |
| 10 | 2.40 | 0.95 | 11.85 | 13.80 | 6.97 | 2.30 | 1,655.0 | 9.79 | 7,038.7 | 14.71 | 22,385.0 | 6.75 |
| 11 | 1.53 | 0.77 | 8.77 | 8.38 | 3.88 | -0.83 | 1,667.2 | 9.65 | 7,048.2 | 13.90 | 22,532.3 | 6.98 |
| 12 | 1.61 | 0.96 | 6.01 | 4.97 | 1.38 | 0.17 | 1,699.4 | 10.20 | 7,159.3 | 14.35 | 22,725.0 | 7.31 |

Notes: (1) Core CPI refers to CPI excluding the categories of fresh fruits & vegetables, fish & shellfish and energy.

(2) Adjusted for the required reserves ratios and banks' required reserves in the B account (with the Central Bank) promulgated on Oct. 4 and in Nov. 2001 respectively.

(3) The data has included the net present value of money market mutual funds since Oct. 2004.

(Continued)

| Year / Month | IV. Money, Banking and Finance | | | | | | | | | | | |
|----------------------------|---|------------------------------------|------------------------------|------------------------------------|---|--|--------------------------------|--|---|-------------------------------|-----------------|--------------|
| | Major Financial Institutions ⁽¹⁾ | | | | Non-Performing Loan Ratio of Domestic Banks ⁽²⁾ (%) | Interest Rates (%) | | | | | | |
| | Deposits | | Loans & Investments | | | CBC's Discount Rate (end of period) | Interbank Call-Loan Rate | 31-90 Day Commercial Paper Secondary Market Rate | Five Major Domestic Banks ⁽³⁾ | | Domestic Banks | |
| | Amount (NT\$ Billion) | Annual Rate of Change (%) | Amount (NT\$ Billion) | Annual Rate of Change (%) | | | | | Base Lending Rate ⁽⁴⁾ (end of period) | New Loan Rate (average) | Deposit Rate | Loan Rate |
| | | | | | | | | | | | | |
| 1994 | 12,031.4 | 15.08 | 10,955.6 | 15.19 | 1.82 | 5.500 | 6.13 | 6.77 | 7.94 | N.A. | 6.04 | 8.98 |
| 1995 | 13,130.9 | 9.14 | 12,100.3 | 10.45 | 2.85 | 5.500 | 6.19 | 6.68 | 7.67 | 8.53 | 6.06 | 8.88 |
| 1996 | 14,260.9 | 8.61 | 13,051.8 | 7.86 | 3.68 | 5.000 | 5.44 | 5.79 | 7.38 | 8.16 | 5.79 | 8.55 |
| 1997 | 15,421.3 | 8.14 | 14,352.0 | 9.96 | 3.70 | 5.250 | 6.85 | 6.83 | 7.50 | 8.12 | 5.36 | 8.25 |
| 1998 | 16,696.9 | 8.27 | 15,471.6 | 7.80 | 4.36 | 4.750 | 6.56 | 6.81 | 7.70 | 8.26 | 5.72 | 8.48 |
| 1999 | 18,064.2 | 8.19 | 16,024.9 | 3.58 | 4.88 | 4.500 | 4.77 | 4.88 | 7.67 | 7.10 | 5.00 | 8.03 |
| 2000 | 19,308.7 | 6.89 | 16,622.0 | 3.73 | 5.34 | 4.625 | 4.73 | 4.91 | 7.71 | 6.72 | 4.62 | 7.61 |
| 2001 | 20,160.7 | 4.41 | 16,489.3 | -0.80 | 7.48 | 2.125 | 3.69 | 3.69 | 7.38 | 5.75 | 4.09 | 6.99 |
| 2002 | 20,609.8 | 2.23 | 16,078.0 | -2.49 | 6.12 | 1.625 | 2.05 | 2.03 | 7.10 | 4.04 | 2.38 | 5.53 |
| 2003 | 21,746.9 | 5.52 | 16,535.1 | 2.84 | 4.33 | 1.375 | 1.10 | 1.05 | 3.43 | 2.80 | 1.47 | 4.10 |
| 2004 | 23,256.5 | 6.94 | 17,964.6 | 8.65 | 2.78 | 1.750 | 1.06 | 1.13 | 3.52 | 2.16 | 1.17 | 3.47 |
| 2004/ 1 | 22,010.0 | 6.66 | 16,630.8 | 2.67 | 4.34 | 1.375 | 1.01 | 0.96 | 3.43 | 2.16 | | |
| 2 | 22,202.5 | 7.14 | 16,693.2 | 3.67 | 4.29 | 1.375 | 0.98 | 0.91 | 3.43 | 2.44 | | |
| 3 | 22,395.7 | 8.37 | 16,886.4 | 5.16 | 4.14 | 1.375 | 0.99 | 0.94 | 3.43 | 2.28 | 1.19 | 3.57 |
| 4 | 22,445.3 | 8.54 | 17,019.9 | 5.62 | 3.82 | 1.375 | 0.97 | 0.92 | 3.41 | 2.33 | | |
| 5 | 22,417.5 | 8.22 | 17,169.3 | 6.41 | 3.71 | 1.375 | 0.97 | 0.92 | 3.41 | 2.14 | | |
| 6 | 22,546.6 | 7.92 | 17,204.3 | 5.62 | 3.54 | 1.375 | 1.02 | 0.96 | 3.41 | 2.26 | 1.16 | 3.48 |
| 7 | 22,632.0 | 7.34 | 17,309.3 | 6.52 | 3.53 | 1.375 | 1.02 | 0.96 | 3.41 | 2.18 | | |
| 8 | 22,647.2 | 6.82 | 17,380.0 | 7.02 | 3.45 | 1.375 | 1.05 | 0.90 | 3.41 | 2.35 | | |
| 9 | 22,651.4 | 6.40 | 17,455.4 | 7.33 | 3.31 | 1.375 | 1.08 | 1.03 | 3.42 | 2.29 | 1.14 | 3.43 |
| 10 | 22,752.7 | 6.59 | 17,471.4 | 8.30 | 3.32 | 1.625 | 1.14 | 1.11 | 3.48 | 2.19 | | |
| 11 | 22,854.3 | 6.42 | 17,628.2 | 8.19 | 3.22 | 1.625 | 1.14 | 1.10 | 3.48 | 2.20 | | |
| 12 | 23,256.5 | 6.94 | 17,964.6 | 8.65 | 2.78 | 1.750 | 1.15 | 1.12 | 3.52 | 2.16 | 1.18 | 3.39 |

Notes: (1) The data are from the consolidated balance sheet of the monetary institutions and the Chunghwa Post Co., Ltd.

(2) Includes the data of offshore banking units and overseas branches of domestic banks and medium business banks.

(3) Between 1993 and 2002, the figures represent prime lending rates.

(4) Includes Bank of Taiwan, Taiwan Cooperative Bank, Chang Hwa Commercial Bank, First Commercial Bank and Hua Nan Commercial Bank.

(Continued)

| Year / Month | V. Securities Market | | | | | VI. Balance of Payments and Foreign Exchange Market | | | | | | |
|----------------------------|--|---|------------------------------------|---------------|---|---|--------------------|----------------------|--|--|---|---|
| | TSE Stock Market | | OTC Bond Market | | | Balance of Payments | | | | Foreign Exchange Reserves (end of period) (US\$Billion) | Exchange Rate (End of period) NT\$ US\$ | Daily Average Value of Foreign Exchange Transactions (US\$ Million) |
| | Stock Price Index (1966=100) (average) | Total Trading Value (NT\$ Billion) | Outstanding (NT\$ Billion) | Trading Value | | Current Account | Capital Account | Financial Account | Change in CBC's Net Foreign Assets ⁽¹⁾ | | | |
| | | | | | Share of Outright Transactions (%) | | | | | | | |
| | | | | | | | (US\$ Million) | | | | | |
| 1994 | 6,253 | 18,812.1 | 962.7 | 15,980.5 | 6.51 | 6,498 | -344 | -1,397 | -4,622 | 92.45 | 26.240 | 2,964 |
| 1995 | 5,544 | 10,151.5 | 1,056.8 | 20,802.9 | 8.53 | 5,474 | -650 | -8,190 | 3,931 | 90.31 | 27.265 | 4,181 |
| 1996 | 6,004 | 12,907.6 | 1,339.6 | 28,297.7 | 9.30 | 10,923 | -653 | -8,633 | -1,102 | 88.04 | 27.491 | 4,407 |
| 1997 | 8,411 | 37,241.1 | 1,426.9 | 40,392.0 | 6.41 | 7,051 | -314 | -7,291 | 728 | 83.50 | 32.638 | 4,869 |
| 1998 | 7,738 | 29,619.0 | 1,655.3 | 54,957.7 | 13.02 | 3,437 | -181 | 2,495 | -4,827 | 90.34 | 32.216 | 4,722 |
| 1999 | 7,427 | 29,291.5 | 1,933.2 | 52,432.6 | 13.84 | 7,992 | -173 | 9,220 | -18,593 | 106.20 | 31.395 | 4,182 |
| 2000 | 7,847 | 30,526.6 | 2,279.3 | 68,843.1 | 24.25 | 8,851 | -287 | -8,019 | -2,477 | 106.74 | 32.992 | 4,886 |
| 2001 | 4,907 | 18,354.9 | 2,869.4 | 118,992.5 | 44.56 | 18,239 | -163 | -384 | -17,353 | 122.21 | 34.999 | 4,706 |
| 2002 | 5,226 | 21,874.0 | 3,599.1 | 134,399.0 | 45.13 | 25,630 | -139 | 8,750 | -33,664 | 161.66 | 34.753 | 5,608 |
| 2003 | 5,162 | 20,333.2 | 4,306.6 | 203,624.0 | 62.16 | 29,266 | -87 | 7,630 | -37,092 | 206.63 | 33.978 | 7,297 |
| 2004 | 6,034 | 23,875.4 | 4,777.3 | 205,925.2 | 59.95 | 19,013 | -77 | 6,366 | -26,595 | 241.74 | 31.917 | 10,243 |
| 2004/ 1 | 6,236 | 1,826.6 | 4,328.7 | 11,398.7 | 57.47 | | | | | 214.93 | 33.390 | 11,152 |
| 2 | 6,514 | 3,177.1 | 4,373.2 | 11,811.5 | 51.98 | | | | | 224.80 | 33.365 | 10,507 |
| 3 | 6,658 | 3,717.8 | 4,467.3 | 19,314.1 | 63.72 | 5,928 | -25 | 15,551 | -21,097 | 226.52 | 33.020 | 10,123 |
| 4 | 6,666 | 3,152.0 | 4,537.8 | 18,417.0 | 63.39 | | | | | 227.66 | 33.369 | 10,285 |
| 5 | 5,912 | 1,852.7 | 4,541.0 | 15,039.4 | 55.91 | | | | | 229.00 | 33.389 | 10,700 |
| 6 | 5,758 | 1,457.1 | 4,579.9 | 15,491.4 | 53.78 | 5,565 | -23 | 862 | -4,084 | 230.09 | 33.775 | 10,124 |
| 7 | 5,554 | 1,165.1 | 4,620.7 | 20,772.7 | 61.72 | | | | | 230.40 | 34.136 | 9,250 |
| 8 | 5,498 | 1,241.2 | 4,660.7 | 17,219.6 | 57.77 | | | | | 231.61 | 34.053 | 8,864 |
| 9 | 5,866 | 1,730.8 | 4,697.9 | 16,199.0 | 54.69 | 5,348 | -18 | -6,354 | 1,489 | 233.01 | 33.984 | 9,303 |
| 10 | 5,885 | 1,637.2 | 4,755.8 | 18,569.4 | 63.24 | | | | | 235.03 | 33.435 | 10,407 |
| 11 | 5,885 | 1,527.8 | 4,705.8 | 20,570.6 | 65.53 | | | | | 239.13 | 32.205 | 11,066 |
| 12 | 5,967 | 1,390.1 | 4,777.3 | 21,121.8 | 62.41 | 2,172 | -11 | -1,969 | -2,903 | 241.74 | 31.917 | 11,135 |

Note:(1) The minus sign represents an increase.

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