

Foreword

In 2006, Taiwan's economy registered a steady growth of 4.62 percent, higher than the 4.03 percent in the previous year. The major driving force was exports, fuelled by a pickup in external demand for consumer electronics, which more than offset the weakness in private consumption caused by credit card defaults. Meanwhile, inflation remained low and stable. Surging oil prices fed through to electricity and transportation prices; yet vegetable prices declined markedly due to a higher base effect. Taken together, consumer prices edged up 0.6 percent and CPI excluding fresh fruits and vegetables increased 1 percent.

In the context of solid economic growth, subdued inflation and low real interest rates, the Bank adopted fine-tuning measures to help promote efficient fund allocation and financial stability. The Bank raised the discount rate four times during 2006, each time by 12.5 basis points, and ten times from October 2004 to the end of 2006 by a total of 137.5 basis points. Market rates were gradually guided upwards. Under the Bank's prudential policy, excess reserves, reserve money, bank credit and monetary aggregates all followed a reasonable course of growth. M2 grew by 6.22 percent for the year, staying within the Bank's 3.5 to 7.5 percent target zone.

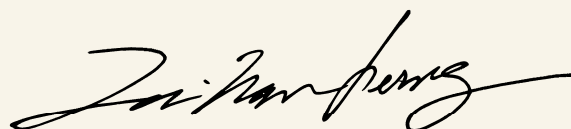
On the foreign exchange front, the NT dollar exhibited dynamic stability, closing at 32.596 against the US dollar at the end of the year, a moderate appreciation of 0.78 percent. Balance of payments remained in good shape. Foreign exchange reserves built up to US\$266.1 billion at the year-end, representing an increase of US\$12.9 billion year on year.

With respect to institutional reform, the Bank continued promoting the transparency of the interest rate pricing mechanism. From January 2006 onwards, financial institutions are required to link prime rates to base rates. The Bank also effectively combated counterfeit money. Payments systems functioned smoothly. To enhance settlement efficiency in capital markets, the Bank began incorporating funds transfers involving stock, bond and bills transactions into the Interbank Funds Transfer System.

In addition, the Bank continued to promote financial liberalization and internationalization. New financial products were introduced to the domestic market, cross-border capital movements were further facilitated, and local financial institutions began extending NT dollar loans to non-residing foreigners. Moreover, cross-Strait remittances grew substantially in recent years, further enhancing the OBU's of domestic banks as a funding center for Taiwanese businesses operating overseas.

Many challenges still lie ahead as globalization and financial innovation complicate the task of carrying out monetary policy. Based on our legal mandate, the Bank will continue to implement appropriate monetary policy, devote itself to maintaining price and financial stability, ensure the sound operation of payments systems, and help promote sustainable development of the economy.

Finally, my sincere appreciation goes to my colleagues for their dedication during 2006. Together, we will work hard to meet the challenges in the year ahead.



Fai-nan Perng
Governor
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