

3. Banking Sector

A Drop in the Number of Depository Institutions

At the end of 2006, the number of depository institutions was 383, a decrease of seven from the previous year-end. Of which, the number of domestic banks decreased by two while the number of medium business banks decreased by one, as a result of the conversion of a medium business bank into a domestic bank and three merger cases of domestic banks. The number of foreign banks decreased by three as the UFJ Bank was merged into the Bank of Tokyo-Mitsubishi and the Toronto Dominion Bank and Union Bank of California closed their branches in Taiwan. The number of credit cooperatives decreased by one because a credit cooperative was merged by a domestic bank.

The numbers of financial holding companies and money market mutual funds remained at 14 and 2 at year-end 2006, respectively.

Market Shares of Deposits and Loans

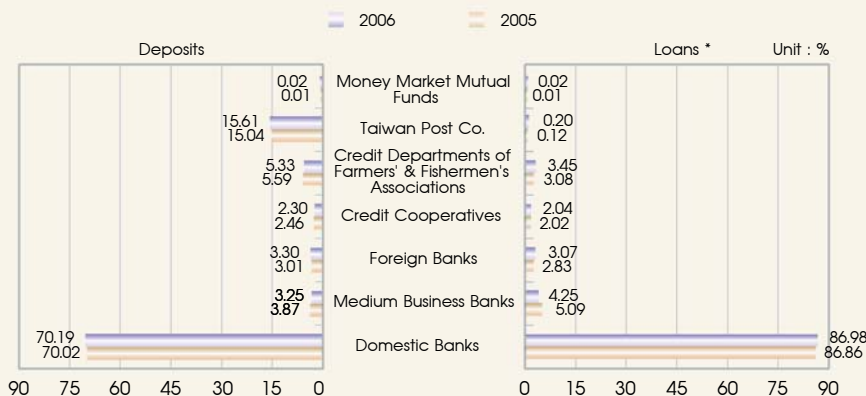
Domestic banks have played a major part in the market of deposits and loans. At the end of 2006, domestic banks' market shares of deposits and loans increased to 70.19 percent and 86.98 percent, respectively. The increase was mainly due to the conversion of a medium business bank and a merger of a credit cooperative into domestic banks. While focusing on

Number of Depository Institutions by Category

	End of 2006	End of 2005	Annual Change
Combined Number of Main Offices	383	390	-7
Domestic Banks	40	42	-2
Medium Business Banks	3	4	-1
Foreign Banks	33	36	-3
Credit Cooperatives	28	29	-1
Credit Departments of Farmers' and Fishermen's Associations	278	278	0
Department of Savings and Remittances of Taiwan Post Co.	1	1	0
Combined Number of Branches	5,961	5,938	23
Local Branches	5,815	5,789	26
Overseas Branches	80	79	1
Offshore Banking Units	66	70	-4

Sources: 1. *Financial Statistics Monthly*, CBC.
2. *Department of Financial Inspection*, CBC.

Market Shares of Deposits and Loans by Category of Depository Institutions



Note: * Including data for securities acquired under reverse repurchase agreements.
 Source: *Financial Statistics Monthly*, CBC.

their foreign exchange related business, foreign banks' market shares of deposits and loans increased slightly to 3.30 percent and 3.07 percent, respectively, despite that two foreign banks closed their branches. As for the Department of Savings and Remittances of the Taiwan Post Co., its market share of deposits continued to show an upward trend to 15.61 percent at the end of 2006. Its share of total loans, however, due to the restrictions on the Taiwan Post Co.'s loan business, only edged up to 0.20 percent, higher than that of the previous year.

Depository Institutions' Sources and Uses of Funds

The composition of the sources of funds was broadly unchanged. Owing to successive rises in non-transaction deposit interest rates and the widening interest rate differentials between the foreign currency deposits and the NT dollar deposits during this year, part of transaction deposits were shifted to non-transaction deposits. The share of non-transaction deposits, especially for foreign currency deposits, edged up in 2006, while the share of transaction deposits edged down. At the year-end, the shares of transaction deposits and non-transaction deposits were 27.44 percent and 64.62 percent, respectively.

With respect to the uses of funds, banks shrank their consumer finance business due to rising credit and cash card debt defaults. As a result, the share of bank loans in the uses of funds dropped down from the previous year's 66.47 percent to 64.69 percent at the end of 2006. Meanwhile, the share of net foreign assets increased from 0.57 percent to 1.73 percent. With banks' efforts in reducing excess funds and containing their investment risk, banks increased their purchases of government-issued securities. As a result, the share of bank portfolio

Sources and Uses of Funds in Depository Institutions

Unit: NT\$ Billion

	End of 2006		End of 2005		Annual Change	
	Amount	Share (%)	Amount	Share (%)	Amount	Share (%)
Sources:						
Transaction Deposits **	7,464	27.44	7,141	27.67	323	-0.23
Non-transaction Deposits***	17,576	64.62	16,625	64.42	951	0.20
Government Deposits	717	2.63	729	2.82	-13	-0.19
Borrowings from CBC	151	0.56	122	0.47	29	0.08
Other Items (Net)	1,293	4.75	1,193	4.62	99	0.13
Total	27,200	100.00	25,810	100.00	1,390	0.00
Uses:						
Net Foreign Assets *	472	1.73	148	0.57	324	1.16
Loans	17,594	64.69	17,154	66.47	440	-1.78
Portfolio Investments****	2,555	9.39	2,202	8.53	353	0.86
Purchases of CDs Issued by CBC	3,683	13.54	3,444	13.34	240	0.20
Deposits with CBC	2,896	10.65	2,863	11.09	34	-0.44

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, and repurchase agreements.

**** Being measured at original costs.

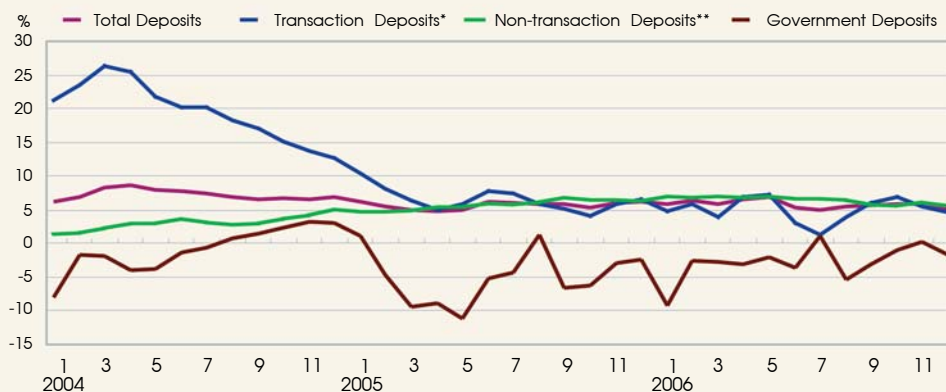
Source: *Financial Statistics Monthly*, CBC.

investments in the uses of funds increased from 8.53 percent to 9.39 percent. The share of holdings of certificates of deposit issued by the Bank also increased slightly from the previous year, while the share of deposits with the Bank decreased.

Downtrend in the Growth of Deposits

Total deposits of depository institutions at the end of 2006 grew by 5.10 percent, lower than the rate of 6.19 percent recorded in 2005. The decline was mainly caused by slower growth in the banks' loans and investments, a deceleration in foreign capital inflow, as well as a surge in overseas financial investments by residents. The monthly changes in the annual growth rate of deposits were as follows. Due to the continuous slowdown in the expansion of bank credit, the annual growth rate of deposits trended down to 5.86 percent at end-March. Afterwards, the annual growth rate of deposits climbed up to 6.82 percent at end-May following the rebound in the growth of bank credit and an increase in foreign capital inflow. In June and July, slower growth of bank credit, increased overseas portfolio investments by residents, coupled with foreign capital outflow, pushed the annual growth rate of deposits down to the year low of 5.03 percent at end-July. From August to October, deposits growth went up as a

Annual Growth Rate of Deposits by Type



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*, CBC.

result of the continued increase in foreign capital inflow. From November onwards, mostly due to the base effect, the annual growth rate of deposits dropped despite a significant increase in foreign capital inflow. Deposits growth declined to 5.10 percent at the year-end.

Among different types of deposits, the annual growth rate of transaction deposits fell from the previous year's 6.61 percent to 4.53 percent at the end of 2006, and its share in total deposits edged down from 29.14 percent to 28.98 percent. This was mainly due to the rising interest rates on time deposits and favorable interest rates on foreign currency deposits. At the end of 2006, non-transaction deposits at all depository institutions grew by a smaller pace of 5.65 percent, lower than the rate of 6.42 percent recorded last year-end, while its share in total deposits edged up from 67.88 percent to 68.24 percent.

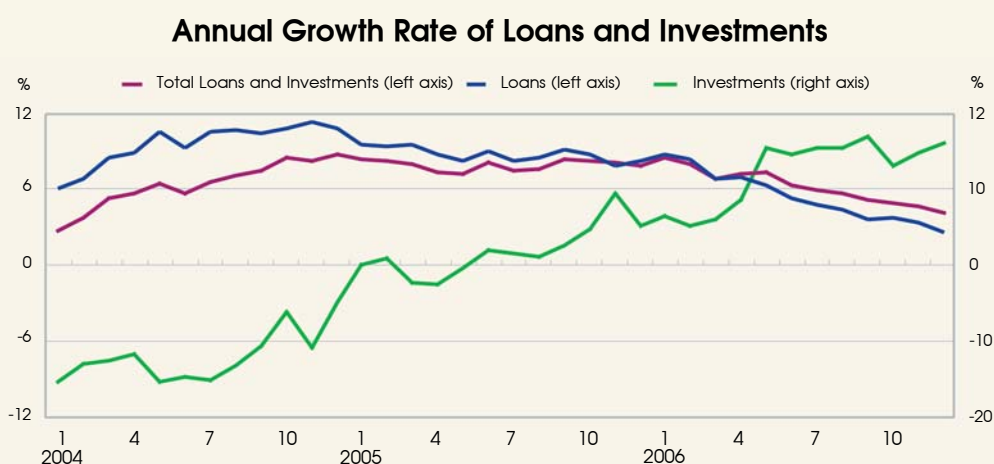
When compared among different types of non-transaction deposits, the annual growth rate of time deposits rose from the previous year's 4.87 percent to 7.45 percent at the end of 2006, and its share in total deposits edged up from 12.32 percent to 12.60 percent. The annual growth rate of time savings deposits declined largely from the previous year's 4.81 percent to 0.53 percent at the end of 2006, and its share fell from 31.65 percent to 30.28 percent. The postal savings deposits dropped to 9.34 percent while its share increased from 14.94 percent to 15.54 percent. Foreign currency deposits expanded from 13.99 percent to 18.59 percent due to the widening interest rate differential. Its share also rose from 6.15 percent to 6.94 percent. As for the outstanding amount of the repurchase agreements, it grew by an annual rate of 4.16 percent while its share dropped to 1.99 percent. NT dollar deposits held by foreigners

rose by 14.33 percent while its share edged up to 0.87 percent. The outstanding amount of money market mutual funds significantly grew by an annual rate of 175.98 percent over the previous year, however, its share remained relatively small when compared with other deposits

Government deposits in depository institutions contracted 1.73 percent in year-end 2006, compared to a 2.47 percent contraction at the previous year-end, and its share dropped from 2.98 percent to 2.78 percent.

Slower Growth in Banks' Loans and Investments

As a result of weak demand for funds caused by the slower consumption growth and sluggish investments in the private sector, the annual growth rate of loans and investments of depository institutions fell to 4.08 percent at year-end 2006, compared to the 7.77 percent recorded in the previous year. Of which, loans posted an annual growth rate of 2.54 percent at the end of 2006, lower than that of 8.13 percent a year earlier, while the annual growth rate of investments rose to 16.04 percent in 2006 from a 5.04 percent reported in 2005.



Source: *Financial Statistics Monthly*, CBC.

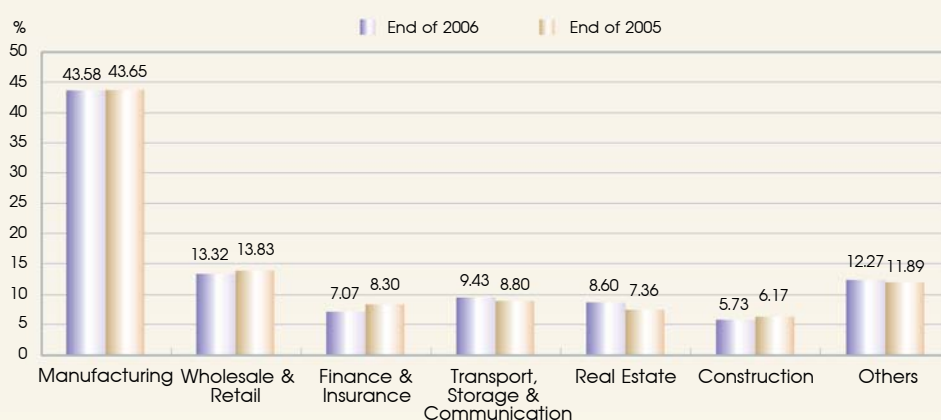
Loans by Sector

Mainly owing to the stronger demand for funds in the booming real estate market, loans extended to the private sector commanded the lion's share of 87.85 percent of total loans at the end of 2006, higher than that of 86.36 percent recorded a year earlier. The share of total loans extended to government agencies and public enterprises decreased to 9.16 percent and 2.99 percent, respectively, from 10.39 percent and 3.25 percent at the previous year-end.

Loans by Industry

The share of loans extended to real estate ascended from the previous year-end's 7.36 percent to 8.60 percent as the real estate market remained active; while the share of loans extended to finance and insurance descended from the previous year-end's 8.30 percent to 7.07 percent. The shares of loans to other industries were largely unchanged.

Share of Loans by Industry



Source: Financial Statistics Monthly, CBC.

Consumer Loans

Of consumer loans, revolving credit balance of credit cards and cash card loans shrank in this year, while home mortgages increased. At the year-end, the outstanding consumer loans extended by domestic banks, local branches of foreign banks, and medium business banks recorded an annual increase of NT\$65.8 billion or 0.99 percent of total loans from the previous year-end.

Share of Loans by Currency

At year-end 2006 the share of foreign currency loans to total loans remained the same of 2.98 percent as a year earlier. The corresponding share of NT dollar loans to total loans was therefore 97.02 percent. Moreover, the NT dollar loan-to-deposit ratio decreased to 71.22 percent at the end of 2006 from 72.38 percent a year earlier.

Investments

Portfolio investments by depository institutions measured at fair values showed an annual

increase of NT\$492.0 billion. After deducting revaluation adjustments of NT\$138.8 billion, portfolio investments measured on a cost basis recorded an annual increase of NT\$353.2 billion or 16.04 percent. Measured on a cost basis, government bonds accounted for the largest share of depository institutions' total investment of 55.54 percent in 2006, up from 53.29 percent a year ago, mainly due to the massive purchase of government bonds by the Department of Savings and Remittances of the Taiwan Post Co. Corporate bonds, second to government bonds in total investment shares, jumped to 13.66 percent from 12.45 percent a year earlier as banks increased their purchases to reduce excess liquidity. During the year, the share of commercial paper also leaped to 10.12 percent from 9.91 percent. Stocks, in contrast, dropped to 15.16 percent from 19.40 percent.

Increasing Share of Indirect Finance

Based on the flow data, the total amount of funds raised during the year by the non-financial sector, comprising enterprises, households, and the government, decreased from the previous year's NT\$1,961.6 billion to NT\$1,215.4 billion. The share of direct finance to total funds raised decreased from 9.24 percent to negative 12.73 percent as the growth of asset-backed securities shrank and the outstanding amount of short-term securities, corporate bonds and offshore bonds decreased. As for the share of indirect finance, that is, those borrowed from financial institutions including depository institutions, investment and trust companies, and life insurance companies, rose from 90.76 percent in 2005 to 112.73 percent in 2006.

Indirect Finance vs. Direct Finance*

Unit: NT\$ Billion

Year	Total Funds Raised (3)=(1)+(2)	Indirect Finance(1)			Share (1)/(3)(%)	Direct Finance(2)	
		Amount	Loans	Investments		Amount	Share (2)/(3)(%)
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	45	42.69	961.1	57.31
2004	2,129.3	1,815.9	1,569.7	246.2	85.28	313.4	14.72
2005	1,961.6	1,780.3	1,458.5	321.8	90.76	181.3	9.24
2006	1,215.4	1,370.2	833.2	537.0	112.73	-154.8	-12.73

Notes: * Measured in terms of flow data.

- (1) Refers to loans and investments (measured on a cost basis) made by depository institutions, trust and investment companies, and life insurance companies, after taking account of their reclassifying of non-accrual loans and bad loans written-offs.
- (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, and short-term bills and asset-backed securities directly held by the non-financial sectors.

Source: *Financial Statistics Monthly*, CBC.

Decline in the Non-Performing Loan Ratio

With the efforts made by local banks to speed up their disposal of non-performing loans (NPLs), the book value of accumulated NPLs sold recorded an increase of \$172.2 billion in 2006. Owing to the impact of rising cash card debt defaults, the average NPL ratio of financial institutions (including banks, community financial institutions, and trust and investment companies) as a whole trended up during the first four months. Afterwards, as local banks kept writing off

Non-Performing Loan Ratios of Financial Institutions*



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

** Including loans under surveillance.

Source: Department of Financial Inspection, CBC.

Non-Performing Loan Ratios by Type of Financial Institutions



Source: Department of Financial Inspection, CBC.

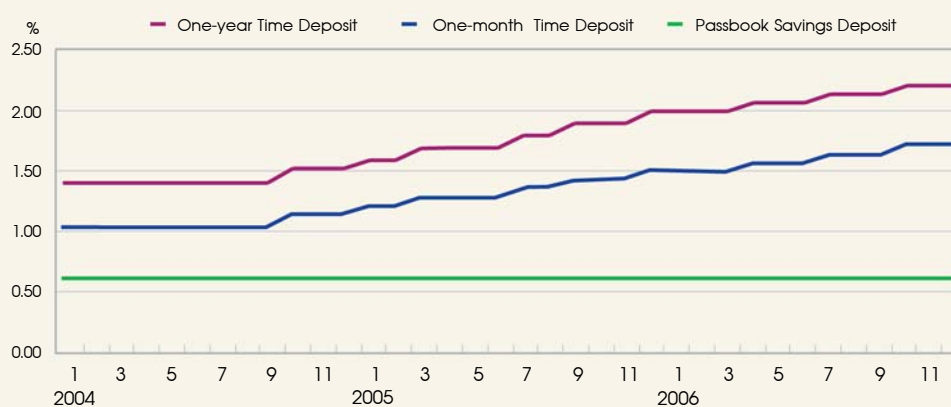
bad loans, the NPLs ratio began to decline and recorded 2.38 percent at the end of the year, lower than the previous year's 2.59 percent.

The corresponding NPL ratio for domestic banks and medium business banks combined (including their offshore banking units and overseas branches) increased from 2.24 percent at year-end 2005 to 2.54 percent at the end of April, 2006, then dropped to 2.13 percent at year-end 2006. The NPL ratios for community institutions declined from the previous year's 8.90 percent to 6.94 percent at year-end 2006.

Increase in Bank Interest Rates

Bank interest rates moved up steadily throughout 2006 along with increases in the 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 moved upward to 1.71 percent and 2.20 percent by the end of 2006, respectively, from 1.50 percent and 1.99 percent at the previous year-end. In the same period, the average base lending rate rose to 4.12 percent from 3.85 percent.

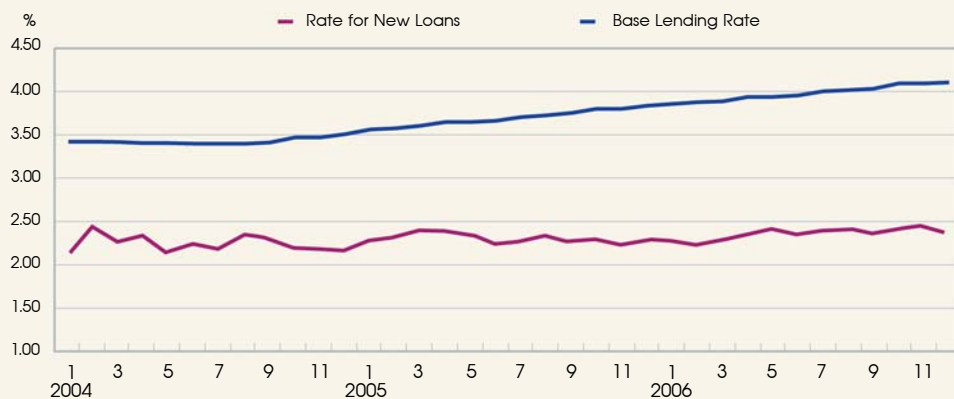
The Average Deposit Rates of the Five Major Domestic Banks*



Note: * The five major domestic banks are the Bank of Taiwan, the Taiwan Cooperative Bank, the First Commercial Bank, the Hua Nan Commercial Bank and the Chang Hwa Commercial Bank.
Source: *Financial Statistics Monthly*, CBC.

The increase in the weighted average interest rate of new loans extended by the five major domestic banks was relatively modest as compared with the increase in the base lending rate. This was mainly due to the increase in low interest rate loans to the government and enterprises with good credit records, and the increase in mortgages that preferential loan rates were applied during the initial periods of the loans. On the whole, the weighted average lending rate slightly increased from 2.31 percent in 2005 to 2.37 percent in 2006. Not counting government loans, the lending rate was 2.41 percent for 2006 from 2.34 percent in 2005.

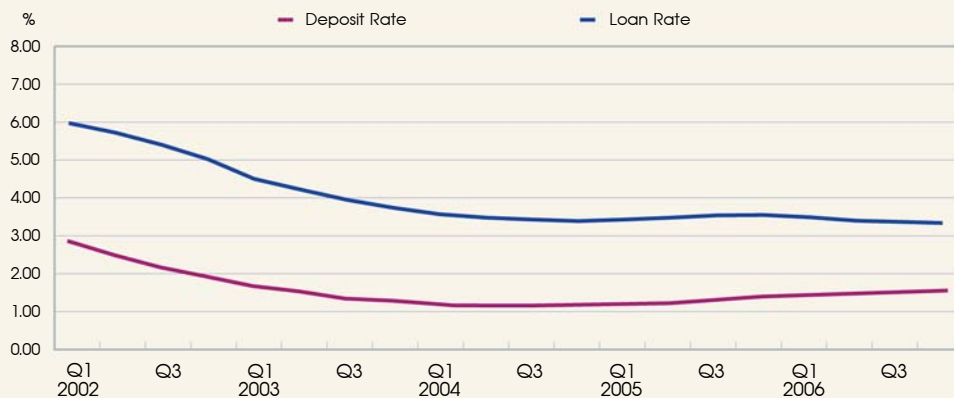
The Average Lending Rate of the Five Major Domestic Banks*



Note: * The five major domestic banks are the Bank of Taiwan, the Taiwan Cooperative Bank, the First Commercial Bank, the Hua Nan Commercial Bank and the Chang Hwa Commercial Bank.
 Source: *Financial Statistics Monthly, CBC.*

The weighted average rates of deposits and loans of domestic banks exhibited a different trend during 2006. With base lending rate climbing smoothly, the weighted average deposits rate rose to 1.54 percent in the fourth quarter of 2006 from 1.38 percent in the same quarter of 2005. On the contrary, the weighted average loans rates moved downward from 3.55% to 3.31% during the same period, mainly because banks cut down extensions of high interest rate consumer loans and provided lower credit card interest rate for cardholders with good creditworthiness following the FSC's new measure regarding the adoption of differential interest rates on credit and cash cards. For 2006, the weighted average rates of deposits and loans are 1.47% and 3.39%, respectively. The interest rate spread between deposits and loans continuously shrank to 1.92 percent in 2006, lower than the 2.21 percent in 2005.

The Weighted Average Interest Rates of Domestic Banks



Source: *Financial Statistics Monthly, CBC.*

A Shrinkage in Banks' Profitability

Affected by rising card debt defaults, the profitability of banks shrank significantly during 2006. The combined pre-tax earnings of all depository institutions fell by NT\$103.6 billion to NT\$12.9 billion, resulting from a decrease in banks' net interest earnings and a sizable writing off of their bad loans. Of this amount, the pre-tax earnings of domestic banks and medium business banks combined plunged by NT\$86.0 billion and posted a loss of NT\$7.3 billion. This was primarily attributed to banks' writing off of bad loans and a loss from the sale of bad assets. The pre-tax profits of foreign banks dropped by NT\$15.8 billion, mainly due to a rise in provisions for credit and cash card defaults. As for the credit cooperatives and the credit departments of farmers' and fishermen's associations, pre-tax earnings rose as banks' provisions for bad loans dwindled, owing to an improvement of their asset quality. In addition, the pre-tax profit of the Department of Savings and Remittances of the Taiwan Post Co. dropped by NT\$2.4 billion, owing to a decrease in interest income and a rise in personnel costs.

A Decrease in ROA and ROE

The average return on assets (ROA) and return on equity (ROE) for all depository institutions fell to 0.04 percent and 0.65 percent in 2006, respectively, from 0.34 percent and 5.95 percent a year earlier. Among depository institutions, the Department of Savings and Remittances of the Taiwan Post Co. remained ahead in terms of ROAs and ROEs. Except for the credit departments of farmers' and fishermen's associations, ROAs and ROEs for all other depository institutions were lower than those of the previous year.

Profitability of Depository Institutions by Type

Unit: NT\$ Billion

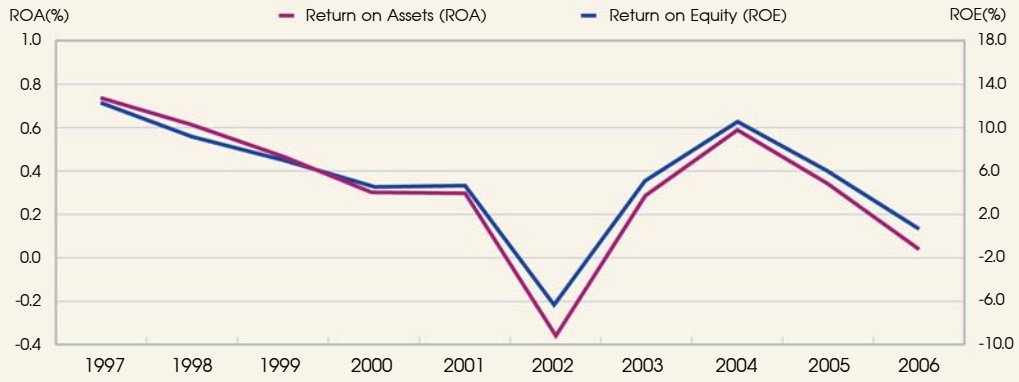
	Profit before Tax			Return on Assets (%)*			Return on Equity (%)**		
	2006	2005	Annual Change	2006	2005	Annual Change	2006	2005	Annual Change
Domestic Banks and Medium Business Banks	-7.3	78.7	-86.0	-0.03	0.29	-0.32	-0.42	4.55	-4.97
Foreign Banks	4.3	20.1	-15.8	0.18	1.10	-0.92	8.61	37.88	-29.27
Credit Cooperatives	1.3	1.5	-0.2	0.21	0.23	-0.02	3.07	3.75	-0.68
Credit Departments of Farmers' and Fishermen's Associations	3.7	2.9	0.8	0.25	0.19	0.06	4.37	3.48	0.89
Department of Savings and Remittances of Taiwan Post Co.	10.9	13.3	-2.4	0.26	0.35	-0.09	13.88	24.90	-11.02
Total Depository Institutions	12.9	116.5	-103.6	0.04	0.34	-0.30	0.65	5.95	-5.30

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

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

Source: Department of Financial Inspection, CBC.

The Return on Assets and Equity of Depository Institutions



Source: Department of Financial Inspection, CBC.

