

IV. ANNEX

1. The Provision of NT Dollar Loans to Non-Resident Foreigners in Taiwan



Introduction

Domestic banks have been prohibited from lending NT dollar funds to non-resident foreigners since 1990. However, following the large-scale opening in Taiwan's equity market, foreign investors' demand for NT dollar financing arose accordingly in recent years. To promote more foreign investment in Taiwan and to effectively use the loanable funds in the banking system, the Bank and the FSC in November

2006 allowed domestic financial institutions to provide NT dollar loans to foreigners without domicile in Taiwan. This annex aims to provide a brief introduction to this deregulation measure.

Prohibiting Foreign Investors Taking NT Dollar Loans in the 1990s

Over the past two decades, the Bank has consistently taken a gradual approach to liberalize its foreign exchange management. Since July 1987, Taiwan's residents have been able to freely hold and use their foreign exchange incomes. Capital account liberalization has been undertaken on a step-by-step basis as well. For instance, restrictions on long-term investment were lifted first, followed by portfolio investment. However, in September 1990, on concerns that large-scale capital account opening might jeopardize the stability of the financial system, the monetary authorities forbade domestic financial institutions to provide NT dollar loans to foreigners without domicile in Taiwan. In December 1990, to promote the development of local securities market, the government allowed the Qualified Foreign Institutional Investors (QFIIs) to invest directly in Taiwan's equity market. In March 1996, the market was further relaxed to Generalized Foreign Individual Investors (GFIIIs.) However, both QFIIs and GFIIIs were subject

to the restrictions on taking NT dollar loans from local financial institutions before the implementation of this new deregulation measure.

Gradual Removal of Restrictions on the Provision of NT Dollar Loans to Non-Resident Foreigners

To enlarge the scale and expedite internationalization of domestic securities market, the QFII system was abolished in October 2003. This policy move has attracted considerable foreign capital pouring into domestic securities market as foreigners' portfolio investment in Taiwan has been nearly completely liberalized.

Owing to the rapid growth of foreign investment into domestic equity market, foreign investors' demand for NT dollar funds arose simultaneously. The Bank has therefore relaxed several restrictions on extending NT dollar loans to non-residents in May 2004, to allow domestic financial institutions to provide intra-day credit to foreign investors with the ceiling not exceeding the amount required to complete the settlement.

In August 2006, the Bank convened the FSC and the local Bankers Association in regard to the deregulation for extending NT dollar loans to non-resident foreigners and agreed to designate the Bankers Association to draft the guideline. On October 26 2006, the Bankers Association stipulated the *Operation Guideline for Member Banks Providing NT Dollar Loans to Foreigners without Domicile in Taiwan*, which has been put into effect since November 2006.

Major Reasons for the Deregulation

There are three major reasons for the provision of NT dollar loans to non-residents:

First, Taiwan has enjoyed excess savings in recent years. After the government removed the ceilings on foreign portfolio investment, vast foreign capital flowed into local stock market. Coupled with the relatively low level of domestic investment, liquidity in the banking system remained ample. To allow domestic financial institutions to extend NT dollar loans to foreign investors will help to channel these excess funds more effectively.

Second, lifting the restrictions on the extension of NT dollar loans to foreign investors will not curb foreign investment; in the mean time, it will help reduce continuous foreign capital inflow and mitigate its impacts on the foreign exchange market.

Finally, because the scope of the deregulation is limited to portfolio, long-term equities, and real estate investments, the new loan business will not only help to increase the demand

for NT dollar funds from banks, but also increase incentives for foreign investments in Taiwan.

Current Regulations on Foreigners' NT Dollar Loans

Current regulation on the provision of NT dollar loans to foreigners in Taiwan are summarized as follows:

First, the new policy allows local financial institutions to extend NT dollar loans to non-resident foreign natural persons as well as foreign juridical persons.

Second, foreign investors can now take out NT dollar loans to finance their investment in domestic securities, long-term equities, real estates, or for any other purposes with the approval from the FSC and the Bank.

Third, to contain credit risk, these loans have to be secured by collaterals. The collateral margin requirement for loans secured by stocks is limited to 60% worth of loans.

Finally, the regulation requires that funds borrowed from a stock-secured loan should be directly disbursed to the seller's accounts or deposited at the accounts with the custodian bank, while the custodian bank is responsible for monitoring flows of fund. Funds derived from the sale of stocks shall be used exclusively for loan repayment.

In sum, recent deregulation on the provision of NT dollar loans to foreign investors intends to channel liquidity more efficiently and lessen the impact of foreign capital inflows on the foreign exchange market, thus leading to more foreign investment in Taiwan.