

# Banking sector in taiwan research paper example

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The banking sector in Taiwan has continued to perform well despite the effects of the Asian crisis which rocked the Asian region in 1997 (Chiu 295). This crisis caused violent fluctuation of interest rates, share prices and exchange rates. However, the effect of the crisis was not extensive in Taiwan as compared to other countries like South Korea and the rest of Asia. Taiwan's strong foundations on economic fundamentals that have a flexible capital market reduced the financial crisis on this country. Furthermore, the conservative financial policies in Taiwan have strengthened the financial system of Taiwan against crisis.

In this paper, focus shall be on the developments that Taiwan's banking system has undergone over the years and the effects that the Asian crisis had on the country's banking unit. The banking infrastructure that was developed during the colonial time of Taiwan has had a great bearing on the evolution of the banking system into a complicated domestic credit system. The banking system in Taiwan is predominantly owned by the state. These conservative policies were developed after World War Two when the Japanese surrendered. This left Taiwan with a localized complicated banking system. Taiwan's banking system was influenced by the Japanese as it was a Japanese colony till end of WW2. The Japanese had introduced the western system of banking to Taiwan (Lester and Mitchell 449).

Currently, there are four categories of banks in Taiwan; banks established in Taiwan when it was a Japanese colony from 1895 to 1945, banks that were re-established in Taiwan with their origin in mainland China, banks founded in Taiwan after 1949 and finally the new privately owned commercial banks established after 1992. Taiwan banks, before 1992, were exclusively owned

by government agencies or by persons that had a close connection with the policy makers of the country (Lester and Mitchell 450).

Tough administrative controls were set up to replace the regulations on the banking industry due to stressing on the government owned banking policy. There was a series of fraudulent scandals experienced in the banking sector in the 1980s due to this lack of supervision. The distortion of the functions of the market and the nature of the banking system in Taiwan hindered further developments in the banking system despite the accelerated economic growth of Taiwan. In the late 1980, Taiwan was forced to restructure their banking sector due to the escalated rate of banking scandals.

With the globalization of banking systems, Taiwan had to liberalize its banking system to meet the international financial regulations and standards. This financial liberalization has impacted positively on the growth of this industry. Taiwan's formal financial banking segment is made up of the local banks most are owned by the state while others being semi-government institutions. This formal sector also comprises of local branches of international banks. These international banks' assets amounted to 7.8 percent in 1987 and a further reduction to 5.5 percent as of 1996 (Lester and Mitchell 449). The banking sector is segmented into local foreign banks and domestic banks. The local foreign banks serve mostly the internationally trading institutions. These banks rely mostly on the money market instead of the deposits for their contribution of finances since the country's policies allow them to have one bank branch in addition to their headquarters. It was not until the 1980s that other international institutions were allowed to set up in Taiwan. However, the local banking sector had its interest rate

regulated by the government. This led to the banks rationing their credits to serve the private sectors and the government enterprises.

The informal banking sector is structured into many different forms, that is; The Rotating Savings and Credit Associations-ROCA, underground money shops, unsecured loans from the privately owned sectors, postdated checks among others. In 1964, informal financing was at 48% of the total loans by the clandestine enterprises (Chiu 295). This informal financial banking is credited for allowing the consumers to prevail over credit constraints. This can be shown by the high home ownership that is very high in spite of the high price of purchasing the homes and this is uniform all through the country. Taiwan has seen gradual liberalization of the banking industry since the 1980s. These include deregulations measures in banking, liberation of foreign exchange, creation of the money markets, and the creation of a high end financial monitoring system (Jaw-ling 295). The deregulation measure included the removal of the direct control on the bank interest rest, privatization of the state owned banks, allowing international banks to invest and the expansion of the existing banks to open new branches.

### **Effects of the Asian Financial Crisis on Taiwan**

The stock price index in Taiwan had risen exponentially before the financial crisis set in. share prices had been going up gradually and steadily during the first half of 1997. This was from 7, 135 points end of January to 9, 890 point closing in the month of August. This was an abnormally high stock market index rate. Therefore, when the financial crisis hit the country, there was a violent fluctuation of interest rates, exchange rates and the stock price index. This crisis set in unexpectedly to the government, the banking system

and to the people of Taiwan in general. As this crisis deepened in the Asian countries, there was a decline in the world stock prices. The Central Bank began a foreign exchange intervention by creating a shortage of funds. This resulted in a sharp decline of the Taiwanese stock price by close of business in August 1997 (Jaw-ling 295). Despite this, as the financial crisis began to subside, New York prices responded by recovering very fast. By December of 1997, the stock prices experience a gradual rise.

During this time, exchange rates policies were changed frequently to conform to the prevailing conditions. During this time of crisis, the exchange rates for the Taiwanese dollar fell very fast against the US dollar. The fall was from NT\$ 27. 9 to NT\$ 28. 7. This was by end of the month of July. The government then had to step in to try and protect the Taiwanese dollar from further dropping its value. The government allowed the exchange rates to be wholly driven by the market forces for the days consecutively as from July 29th. This led to a depreciation of the Taiwanese dollar to a lower level which made it easier for the Central bank to defend it. Stabilization of the NTS\$ was achieved by the central bank by raising the interest rate and the rediscount rate. The Central Bank further intervened to safe guard the foreign exchange market (Hsiao 1986).

Luckily for Taiwan, there was a financial stabilization of the markets. Ever since then, the banking systems of Taiwan have been extremely sensitive to any changes in the international arena. The Central bank occasionally has to intervene to stabilize the financial markets when there is an unjustified decline of the Taiwanese dollar.

## **Current Banking Trend in Taiwan**

Taiwan banking industry has been argued to be one of the most crowded sectors. Some renowned international banking giants are considering exiting the banking industry in this country. Banks had bet that the growing good relationship between china and Taiwan would have a great catch in the region and therefore many banks had flocked into Taiwan in the last decade. Despite the improved relationship between china and Taiwan, their individual banking sectors still encounter tough limitations across the Taiwan Strait. As a matter of fact, the investors in this country are encountering a decline in valuation and restrictive regulatory hurdles (Tornell 18).

Intense competition among the banks in Taiwan is a major impediment to profit making. Today, there are close to 40 domestic banks and another 30 foreign owned banks which are fighting for customers in a country of 23 million inhabitants. There was a great expectation that the improve ties between China and Taiwan would lead to a more open market whereby Chinese banks would be permitted to buy considerable stakes in Taiwanese lender.

There is also the issue of declining valuation. Potential bank buyers are not ready to shell out what the equity private firms expect. Most of the domestic banks in Taiwan today are experiencing great difficulty in making money today (Jaw-ling 295). The government demands that more stringent definitions of capital adequacy ratio be implemented. The state owned banking institution still command about have of the market in relations to assets they own. This include the partially government banking institution and those that are wholly owned by the sate like the Bank of Taiwan and

Corporate Bank. Taiwan's domestic banks have been shut out of the booming economy that is being witnessed in China (Tornell 18). It is unable to follow its customers across the borders to continue servicing them with loans.

## **Conclusion**

The Asian financial crisis is as a result of several factors. These factors include the macroeconomic factors and the real sector factors which have many emerging issues within their operations. The financial crisis of Asia caused damages in Taiwan but the extent was not felt like in other Asian countries. Taiwan policies need to be changed to be at par with the changing financial situation in order to be able to handle future developments (Hsiao 1986).

Although Taiwan's financial market has grown very fast into international financial market, it still faces great challenges in overseeing the fast growing international banking industry. Therefore Taiwan should focus on liberalization, banking discipline and internationalization.

There is an increasing fragile situation in international banking. Banking in Taiwan is considered to be a very high risk business venture. The monitoring and eradication of potential risks in the banking industry should be addressed through the collaboration of international and domestic banking policy makers. The growing competition demands that Taiwan must enforce compliance to its regulations and foster discipline in the financial market (Hsiao 1986). For Taiwan to meet its needs in the banking reforms and economic developments, the task force that is given the mandate to oversee reform agenda in the banking sector should come up with measure that will

liberalize the financial markets and leads to an increase in efficiency in the financial markets.

## **Work Cited**

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