A Practical Inquiry into Chinese Taipei Banking Industry

Submitted by: Chinese Taipei
2010 APEC Seminar on the First Steps of Successful Reform in Doing Business

Getting Credit (II):
A Practical Inquiry into Chinese Taipei banking industry

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Oct. 6, 2010

Curriculum Vitae

○ Nan Yang
○ Current positions:
  » Secretary General, The Bankers Association, Chinese Taipei
  » Supervisor, Joint Credit Information Center (JCIC)
○ Education:
  » Bachelor of Business Administration, National Chengchi University
  » Law Research Center, National Chengchi University
○ Career:
  » Chief Secretary, Deputy Director-General, Banking Bureau, Financial Supervisory Commission (2004.08-2007.06)
  » Commissioner, Deputy Director, Dept. of Insurance, Ministry of Finance (1981.06-2004.07)
  » Director, Property Insurance Stabilization Fund (2002.03-2004.04)
  » Director, Trade-Van Information Services Co. (2004.02-2007.06)
  » Director, National Credit Card Center (2005.08-2006.12)
I. Financial Market is Fully Competitive

1. Before Opening to the Establishment of New Banks in 1991

Prior to 1991 Chinese Taipei’s financial system was strictly controlled. Except for a few private and foreign banks, participation in the market was largely limited to government-owned banks.

- Mainly government-owned banks, with a 65.15% share of the loan market.
- Relatively high bank profitability, with an ROA above 1% and an ROE above 11%.
- An oligopolistic “seller’s market,” with banks having the ability to determine prices.
I. Financial Market is Fully Competitive (Cont.)

2. Opening to new banks, conversion of trust companies and credit cooperatives into banks, and privatization of some government banks (1993-2010)

- Large increase in market share of private banks.
- Large decrease in banks’ profitability; ROA mostly under 0.5%, ROE mostly under 6%; in 2002, 2006, and 2008, in the negative range.
- Transformation to a fully competitive “buyer’s market,” with stronger customer price-negotiation ability and heightened ability to get credit.

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Trend in the Profitability of Chinese Taipei Banks, 1993-2010

Changes in Taiwan Banks’ Profitability, 1993–March 2010

Note: Increasingly intense competition in the banking market after the government opened up the establishment of new banks and the conversion of trust companies and credit cooperatives into commercial banks led to declining profitability.
II. The Development of Bank Lending

1. Primary emphasis on corporate banking in early times
   - Lacking in natural resources, we have always depended primarily on manufacturing and exports for its economic development. The finance industry has traditionally focused on assisting corporate operations through the corporate banking business.
   - In the initial stages of economic development, incomes among the general public were low and there was relatively little demand for consumer banking services.

II. The Development of Bank Lending (cont.)

2. Policy promotion of SME development strengthens SME financing capability
   - SMEs are the motive force behind Chinese Taipei's economic development and the main support for industrial development. They have the responsibility of promoting economic growth.
   - SMEs can generate large amounts of jobs. They play an important role in stabilizing employment.
   - Policy-type financial assistance institutions such as the Small and Medium Business Credit Guarantee Fund and the SME Joint Assistance Fund were set up to encourage banks to extend SME loans and support the development of SMEs.
II. The Development of Bank Lending (cont.)

◆ In April 2005, the Financial Supervisory Commission promulgated the Program to Encourage Lending by Domestic Banks to Small and Medium Enterprises, establishing targets and incentive measures and calling for the regular review of implementation by different banks with the aim of heightening the amount of loans to SMEs.

◆ As a result, the amount and ratio of bank loans to SMEs continuously increased.

II. The Development of Bank Lending (cont.)

Trends in Amount and Ratio of Loans to SMEs by Chinese Taipei Banks

Changes in Amount and Ratio of SME Loans

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount of SME Loans</th>
<th>Total Amount of Corporate Loans</th>
<th>Ratio of SME Loans in All Corporate Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>2,802,368</td>
<td>6,736,312</td>
<td>37.31%</td>
</tr>
<tr>
<td>2007</td>
<td>2,912,368</td>
<td>7,129,948</td>
<td>38.33%</td>
</tr>
<tr>
<td>2008</td>
<td>3,254,024</td>
<td>7,795,556</td>
<td>36.58%</td>
</tr>
<tr>
<td>2009</td>
<td>3,604,918</td>
<td>8,462,646</td>
<td>41.48%</td>
</tr>
<tr>
<td>2010</td>
<td>3,992,657</td>
<td>9,220,094</td>
<td>41.25%</td>
</tr>
</tbody>
</table>

Unit: NT$ million

II. The Development of Bank Lending (cont.)

3. Increase in domestic demand stimulates booming development of personal loans
   - The rapid expansion of Chinese Taipei’s economy and continuous accumulation of wealth by the people greatly boosted demand and purchasing power for real estate, automobiles, and all kinds of consumer goods.
   - To boost profitability, banks initiated a major expansion of their consumer banking business. All kinds of consumer banking, including home loans, home improvement loans, credit cards, and consumer loans, experienced rapid growth.
   - The amount and ratio of personal loans increased continuously.

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Trends in Amount and Ratio of Personal Loans by Chinese Taipei Banks

Changes in Amount and Ratio of Personal Loans

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount (NTN)</th>
<th>Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>5,415,134</td>
<td>44.02%</td>
</tr>
<tr>
<td>2003</td>
<td>5,945,314</td>
<td>46.13%</td>
</tr>
<tr>
<td>2004</td>
<td>6,944,883</td>
<td>47.30%</td>
</tr>
<tr>
<td>2005</td>
<td>7,725,500</td>
<td>47.30%</td>
</tr>
<tr>
<td>2006</td>
<td>7,871,243</td>
<td>46.09%</td>
</tr>
<tr>
<td>2007</td>
<td>8,088,181</td>
<td>47.37%</td>
</tr>
<tr>
<td>2008</td>
<td>8,187,607</td>
<td>46.38%</td>
</tr>
<tr>
<td>2009</td>
<td>8,358,325</td>
<td>48.64%</td>
</tr>
</tbody>
</table>

Source: Central Bank (“Loans and Discounts at All Banks, by Sector”; June 2010)
III. Healthy Credit Information System Facilities Lending to Individuals and Enterprises

1. Chinese Taipei’s Joint Credit Information Center enjoys high regard internationally
   - Chinese Taipei’s Joint Credit Information Center (JCIC) was established in 1975, and has been operating for 35 years, and so it possesses complete historical data.
   - JCIC was the first credit reporting institution in Asia to collect and file personal and corporate credit data, and to include both positive and negative information.
   - In 2004, JCIC won the first-place overall score in the World Bank’s “Public Credit Registry” global survey.

2. JCIC’s comprehensive credit information products reduce inconsistency of information between banks and their customers, easing the extension of personal and corporate loans
   - The data collected by JCIC is provided by all of the financial institutions, and users are limited to financial institutions. It is a closed system with strict management rules, and so it has a high degree of data quality and safety.
   - JCIC continuously develops new credit information products; in addition to loan information, these include a “Personal Credit Rating System” and “Real Estate Transaction Information and Valuation Information Platform”.
   - JCIC has high-performance information system equipment that allows it to provide real-time, accurate credit information on debtors, helping banks to strengthen their capability for, and confidence in, making loans.
III. Healthy Credit Information System Facilities Lending to Individuals and Enterprises (cont.)

3. The Taiwan Economic Journal (TEJ) provides corporate financial data and industrial information that helps banks reinforce their ability in credit analysis.
   - The TEJ was established in 1990, primarily to engage in the business of selling domestic and overseas financial, industrial, and macro-economic analytic data, and of providing related consulting services.
   - TEJ analyzes the financial, operational, industrial, and basic data (reinvestment, etc.) of public companies, and gives them a credit rating for banks to use as a reference in their credit analysis.

IV. A Discussion of “Getting Credit” Score

1. The content of our “Getting Credit” score
   * A comparison of Chinese Taipei’s score with overall scores in the Asia-Pacific and OECD countries

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Chinese Taipei</th>
<th>East Asia &amp; Pacific</th>
<th>OECD Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strength of legal rights index (0-10)</td>
<td>4</td>
<td>5.7</td>
<td>6.8</td>
</tr>
<tr>
<td>Depth of credit information index (0-6)</td>
<td>5</td>
<td>1.9</td>
<td>4.9</td>
</tr>
</tbody>
</table>

Source: “Doing Business 2010” scoring data on the World Bank website
IV. A Discussion of “Getting Credit” Score (cont.)

◆ The Legal Rights Index

<table>
<thead>
<tr>
<th>Strength of legal rights index (0-10)</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Can any business use movable assets as collateral while keeping possession of the assets, and any financial institution accept such assets as collateral?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>Does the law allow businesses to grant a non-possession security right in a single category of revolving movable assets, without requiring a specific description of the secured assets?</td>
<td>0 (No)</td>
</tr>
<tr>
<td>Does the law allow businesses to grant a non-possession security right in substantially all of its assets, without requiring a specific description of the secured assets?</td>
<td>0 (No)</td>
</tr>
<tr>
<td>May a security right extend to future or after-acquired assets, and may it extend automatically to the proceeds or replacements of the original assets?</td>
<td>0 (No)</td>
</tr>
<tr>
<td>Is a general description of debts and obligations permitted in collateral agreements, so that all types of obligations and debts can be secured by stating a maximum amount rather than a specific amount between the parties?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>Is a collateral registry in operation, that is unified geographically and by asset type, as well as indexed by the grantor’s name of a security right?</td>
<td>0 (No)</td>
</tr>
<tr>
<td>Do secured creditors have absolute priority to their collateral outside bankruptcy procedures?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>Do secured creditors have absolute priority to their collateral in bankruptcy procedures?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>During reorganization, are secured creditors’ claims exempt from an automatic stay on enforcement?</td>
<td>0 (No)</td>
</tr>
<tr>
<td>Does the law authorize parties to agree on out of court enforcement?</td>
<td>0 (No)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>4</strong></td>
</tr>
</tbody>
</table>

IV. A Discussion of “Getting Credit” Score (cont.)

◆ The Credit Information Index

<table>
<thead>
<tr>
<th>Depth of credit information index (0-6)</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Are data on both firms and individuals distributed?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>Are both positive and negative data distributed?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>Does the registry distribute credit information from retailers, trade creditors or utility companies as well as financial institutions?</td>
<td>0 (No)</td>
</tr>
<tr>
<td>Are more than 2 years of historical credit information distributed?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>Is data on all loans below 1% of income per capita distributed?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td>Is it guaranteed by law that borrowers can inspect their data in the largest credit registry?</td>
<td>1 (Yes)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>5</strong></td>
</tr>
</tbody>
</table>
IV. A Discussion of “Getting Credit” Score (cont.)

2. Analysis of Chinese Taipei’s score

◆ Chinese Taipei’s Credit Information Index score in terms of international standards
  Ø In the credit information index scoring in which the full score is 6 (6 items), Chinese Taipei scored 5. This was not only far higher than the Asia-Pacific average of 1.9 but even above the OECD average of 4.9.
  Ø Chinese Taipei did not receive a score for one item because the data that JCIC collects and distributes are limited to banking institutions. It is not open to non-banking institutions such as retailers and traders.

IV. A Discussion of “Getting Credit” Score (cont.)

◆ A Legal Rights Index score that is lower than the international average is a primary reason for Chinese Taipei’s lagging overall score
  Ø Chinese Taipei received a score of only 4 on the Legal Rights Index, out of a perfect score of 10. This is not only lower than the OECD average of 6.8 but even under the Asia-Pacific average of 5.7.
  Ø Chinese Taipei has not incorporated the “floating lien” in its movable collateral legal system. This is a major reason for the low Legal Rights Index score.
IV. A Discussion of “Getting Credit” Score (cont.)

3. Should We open JCIC to non-banking institutions?

- Types of Credit Registries in different countries
  - The German model
    Government-run credit information institutions are under the supervision of the competent financial authority, and the provision of credit information to it by banking institutions is compulsory. Private credit information institutions (such as Schufa Holding Co.) divide members by type, A and B, with type A members being limited to banking-related companies.

- The American model
  Credit report agencies are established in the commercial market for profit-making purposes. Participants include banking institutions and general enterprises.

- The Japanese model
  The banking and non-banking credit industries each set up credit information institutions with different members, but overdue debt information can circulate among all of them.
IV. A Discussion of “Getting Credit” Score (cont.)

- The United States is an exception, but most other advanced countries do not open their banking’s credit information databanks for use by non-banking institutions.
- Access to the current closed system of JCIC is restricted to financial institutions with a high degree of homogeneity, making it relatively easy for the competent authority to oversee. The banking and non-banking industries are subject to different degrees of regulatory oversight; if access to JCIC’s information were opened to non-banking institutions, it would make monitoring by the competent authority more difficult.

IV. A Discussion of “Getting Credit” Score (cont.)

- The new version of Chinese Taipei’s Personal Data Protection Act is stricter than the old one, and if the JCIC’s data were opened to non-banking institutions, any resulting inappropriate use of personal information would lead to major consumer disputes that would affect banking institutions.
IV. A Discussion of “Getting Credit” Score (cont.)

4. Should We adopt the “floating lien” system?
   - The “floating lien” mechanism encompasses unspecified assets to be added in the future, semi-finished products, and raw materials within the scope of movable collateral. This is inconsistent with Chinese Taipei’s legal system.
   - The “floating lien” presents practical difficulties in financial operations, and the lack of clearly registered collateral content and scope makes it easy for disputes to arise about creditor fraud and other issues. Whether or not it is an appropriate appraisal index remains to be discussed.

IV. A Discussion of “Getting Credit” Score (cont.)

- The guarantee effect of the “trust possession” system in Chinese Taipei’s movable collateral legal system has some of the “floating lien” effect.
IV. A Discussion of “Getting Credit” Score (cont.)

5. The Insolvency Act that is now being formulated may affect our score on the Legal Rights Index

- The Legal Rights Index contains a question asking whether the right of priority of secured creditors is affected by the bankruptcy system. Under our current bankruptcy law, the right of priority of secured creditors is not affected by the bankruptcy process. This conforms to the index item.
- Insolvency Act is formulated to replace the existing Bankruptcy Act, and whether this will restrict the security rights of secured creditors merits attention. If the right of priority of secured creditors is affected with the amendment, it might influence our score on the Legal Rights Index.

V. Conclusions and Suggestions

1. We have a mature financial market with a high degree of competition. This has helped enhance the ease of getting credit by individuals and SMEs (with relatively poor credit conditions).

2. JCIC should maintain its current system or, in reference to the German and Japanese models, clearly differentiate between the credit information databanks of banking and non-banking institutions so as to strengthen the protection of information related to individuals and company finance.
V. Conclusions and Suggestions (cont.)

3. Gradually guide the banks to provide their corporate customers’ financial information to JCIC in e-form, therefore enhance the time effectiveness in constructing industry financial ratios. JCIC can then provide banks with most up-to-date information for credit analysis.

4. It seems that the scoring items in “Getting Credit” should encompass other factors (such as the existence of an SME credit guarantee system, or the existence of an evaluation system, registry and trading platform for intangible assets) to make the scoring more objective.

5. To enhance the “getting credit” environment for individuals and enterprises, one of the most important factor is a healthy banking system (including raising banks’ core capital ratio and their profitability, etc.).
References

- “Doing Business 2010” scoring data on the World Bank website
- SME loan statistics on the website of the Banking Bureau, Financial Supervisory Commission
- “Loans and Discounts at All Banks, by Sector” and “Conditions and Performance of Domestic Banks” on the Central Bank website
- Explanatory information on the Joint Credit Information Center website
- Financial Research and Development Fund funded research plan “A Study of Adequate Scope and Regulatory Scheme on Gaining Access to JCIC by Non-Banking Institutions”