

2016 Taiwan Market Report

21st Asian Securities Forum AGM

November 21, 2016

A. Taiwan Economic Outlook

Taiwan's Economic Situation and Outlook offers domestic and foreign readers a summary of the current economic situation in Taiwan, including economic growth, foreign trade, domestic demand, industrial production, employment, and prices aspects, in addition to the country's prospects for 2016.

	Historical Data				Data for Recent Months			
	2012	2013	2014	2015	Jun.	Jul.	Aug.	Jan. -Aug.
% Change over previous year. (yoy)								
GDP	2.06	2.20	3.92	0.75	0.70 ^a	-	-	-
Exports	-2.10	1.60	2.80	-10.9	-2.10	1.20	1.00	-6.60
Imports	-3.70	0.30	1.40	-15.8	-10.0	-0.20	-0.80	-8.10
Export orders	1.10	0.40	6.70	-4.40	-2.40	-3.40	8.30	-5.00
CPI	1.93	0.79	1.20	-0.31	0.91	1.23	0.57	-1.38
Industrial Production Index	-0.30	0.70	6.40	-1.80	1.10	-0.40	7.70	-0.80
Monetary Aggregate (M2) ^b	4.18	4.78	5.66	6.34	4.42	4.70	4.51	4.75
Unemployment rate (%)	4.24	4.18	3.96	3.78	3.92	4.02	4.08	3.93
TWSE Stock Index ^c	7,481	8,093	8,992	8,959	8,595	8,900	9,094	8,545

Note : ^a Q2 Preliminary Estimation; ^b Daily Average; ^c Monthly Average TAIEX

Sources : The Central Bank of China (CBC), Financial Supervisory Commission (FSC), Directorate-General of Budget, Accounting and Statistics (DGBAS).

In August, 2016. Taiwan's exports increased by 1.0%, Year-on-Year (Y-o-Y) while imports decreased by 0.8%. The annual growth rate of export orders and Industrial Production Index were 8.3% and 7.7% Y-o-Y, respectively. The Consumer Price Index (CPI) annual growth rate increased by 0.57% and the unemployment rate rose from 4.02% in July to 4.08% in August. On the financial side, August's M2 monetary aggregate increased by 4.51%, while the stock price index averaged 9,094 points.

In the same month, the overall monitoring indicator flashed the "green" signal for the second consecutive month, and the trend-adjusted leading index increased by 0.82%, while the trend-adjusted coincident index increased by 1.13% from the previous month.

Given that the global economy remains fragile and faces several downside risks which may weigh on Taiwan’s economic recovery, the government will build a “New Model for Economic Development” for Taiwan. This will be done by reinforcing Taiwan’s global and regional connections, and by promoting a “New Southbound Policy”. Furthermore, the government will prioritize to promote five major innovative industries, with the goal of reshaping Taiwan’s global competitiveness. Moreover, to improve investment climate, the government will actively implement the “Investment Expansion Program” by investing more in public and state-owned enterprises and spurring private-sector involvement. These initiatives should help endow Taiwan with a vigorous and sustainable economy.

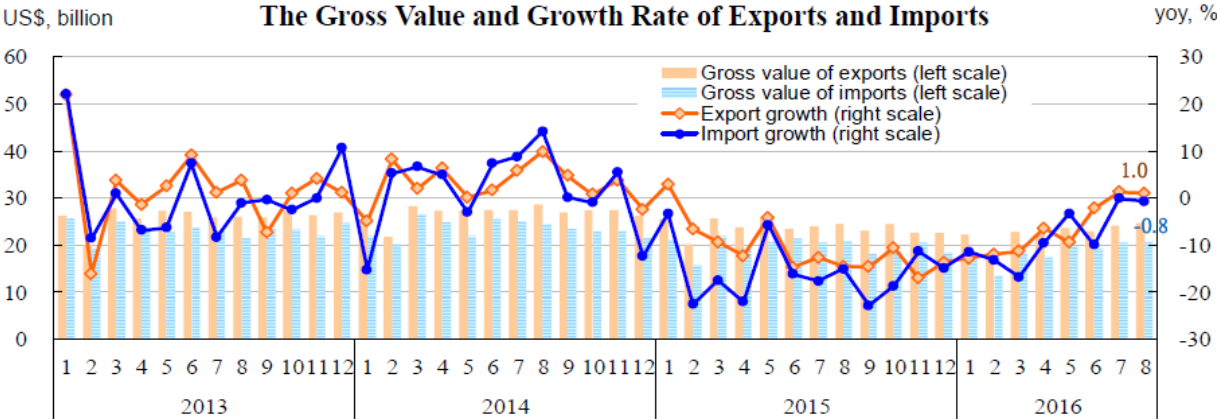
Economy has some good news, showing a sign of recovery

According to the DGBAS’s latest estimation in August 2016, GDP growth rate in 2016 is forecast to be 1.22%, up 0.16 percentage points on May 2016’s forecast, mainly due to better than expected performance of exports and private consumption in the first half of this year. In 2017, GDP is expected to rise by 1.88%, reflecting the gradual recovery of Taiwan’s economy.

1. Foreign Trade Momentum Increases Slightly

Total exports increased by 1.0% year-on-year in August 2016, mainly due to the strong demand for semiconductors, while Taiwan’s semiconductor manufacturing has benefited from its advanced technology and the rising global demand for mobile devices.

Imports fell by 0.8% on a year earlier, with mineral products the main contributors to the decrease. Exports for the January through August 2016 period were down 6.6% on the same period a year ago.

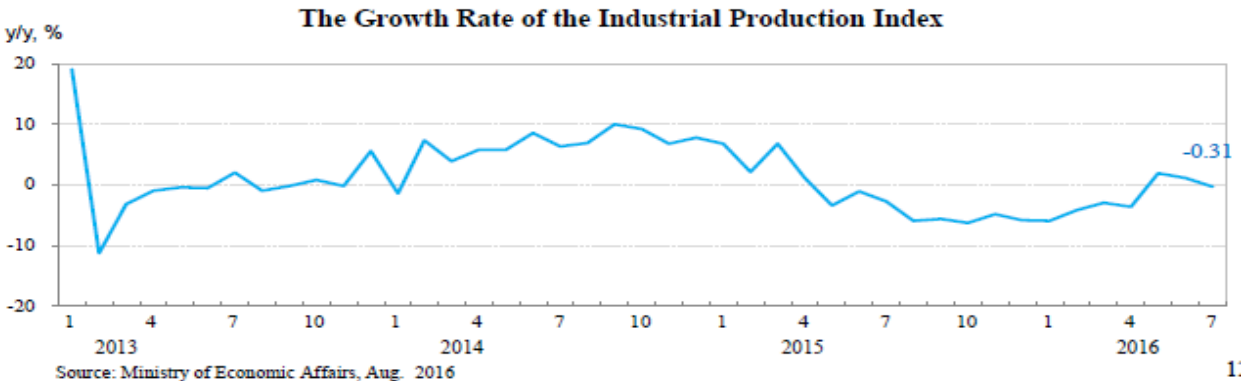


Note: Since FY2016, the general trade system is applied for compilation of external trade statistics and the historical data has been revised to FY2001.
Source: Ministry of Finance, Sep. 2016

2. Industrial Production Declines Slightly

The Industrial Production Index (IPI) posted an annual decrease of 0.31% in July 2016, mainly due to fact that building construction had a higher base period in July 2015 as a result of several major construction projects obtaining Building Use Permits during that period.

Manufacturing output, which makes up more than 90% of the IPI, rose by 0.65% year-on-year in July. The increase in manufacturing output came largely from increased production of electronic parts and components, and chemical material.

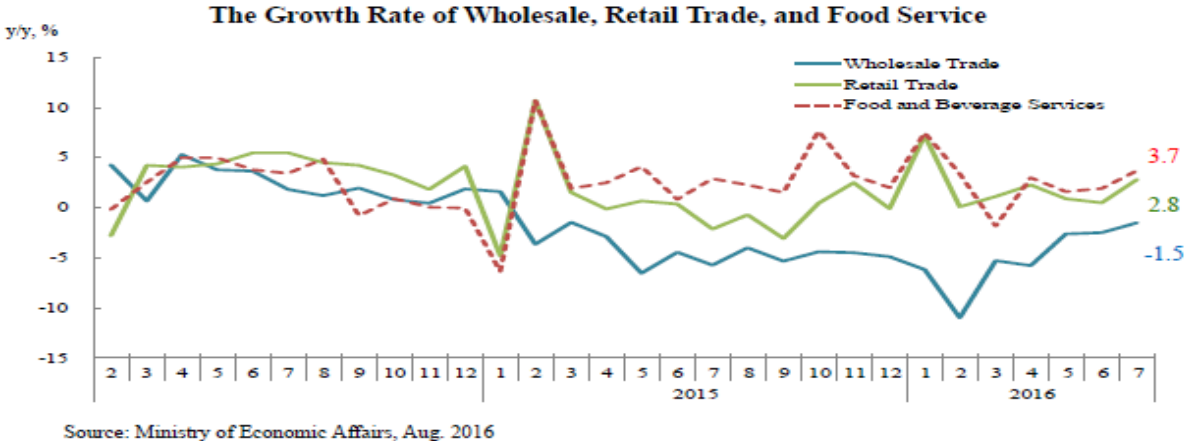


3. Retail Trade Solid

In July 2016, wholesale trade decreased by 1.5%, as global conditions remained weak.

Retail trade rose by 2.8%, driven mostly by stronger general merchandise store sales as demand increased during the Ghost Festival and hot weather in July.

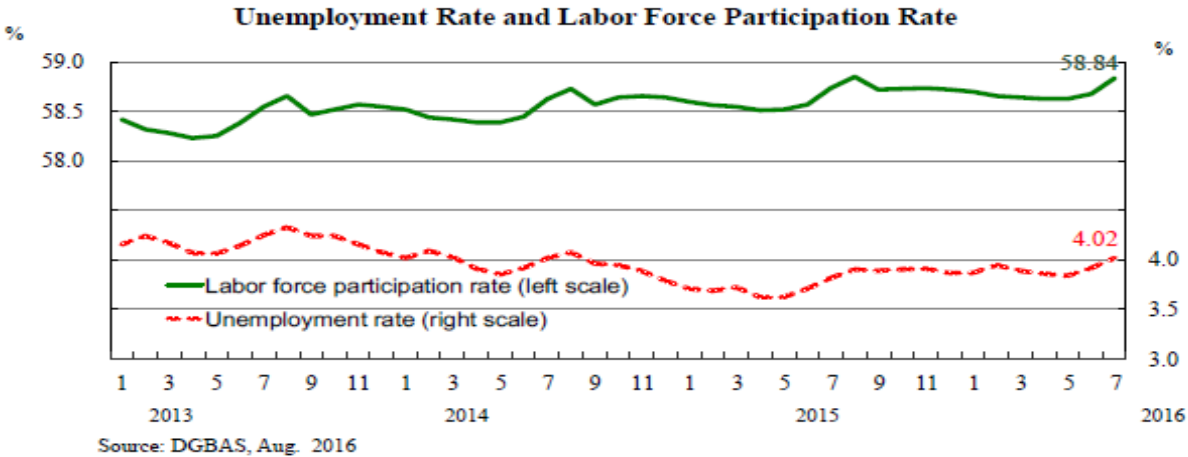
Food and beverage services increased by 3.7% in July 2016.



4. Employment Remains Steady

The unemployment rate rose from 3.92% in June to 4.02% in July 2016. The seasonally adjusted unemployment rate held steady at 3.96%.

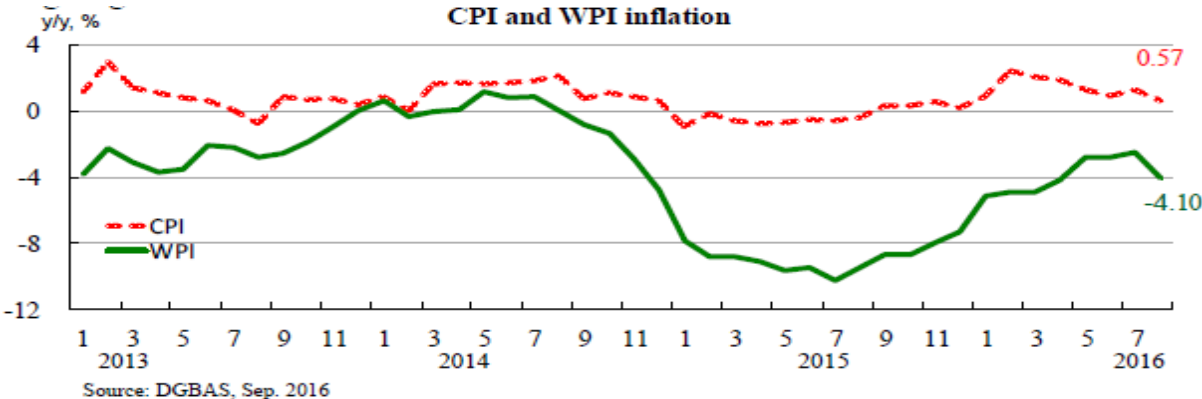
The labor force participation rate rose from 58.68% in June to 58.84% in July, up 0.10 percentage points compared with a year earlier.



5. Prices Up Slightly

Taiwan’s CPI in August 2016 moved up 0.57% compared with the same month last year, mainly due to the 23.02% increase in the fruit index. In addition, prices of fish and seafood also went up 5.33%, and prices of food eaten outside the home increased 1.31%. Core prices (excluding fruit, vegetable and energy prices) increased by 0.77%.

The WPI decreased by 4.10% year-on-year, due to prices of petroleum and coal products dropping 15.57%, and prices of crude petroleum and natural gas going down 13.41%

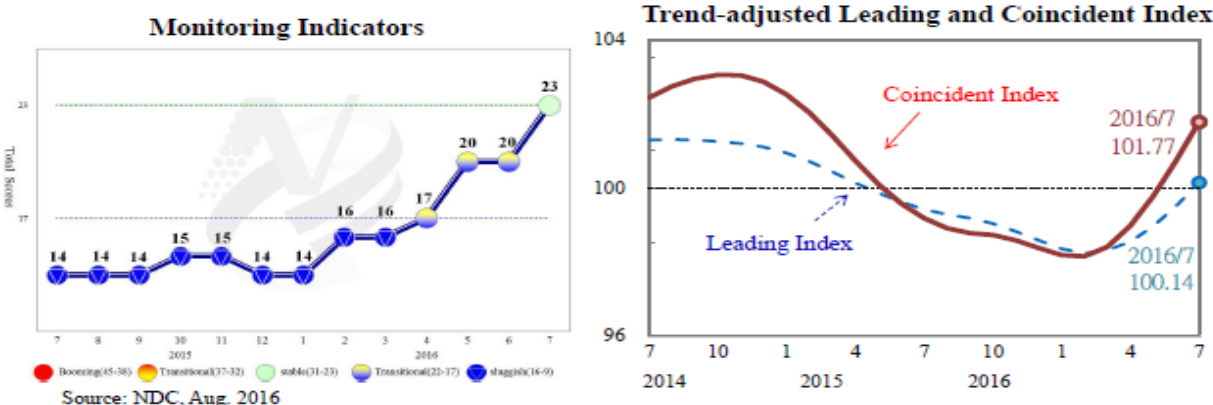


6. Monitoring Indicators Showing “Green” Signal

In July 2016, the trend-adjusted leading index increased by 0.63% to 100.14, and the trend-adjusted coincident index was up by 1.04% to 101.77.

Total score of the monitoring indicators in July 2016 increased by three points to 23, flashing the “Green” signal for the first month.

Taiwan Business Indicators showed some scattered signs of economic improvement.



B. Taiwan Securities Market Outlook

The following sections will introduce various aspects of Taiwan’s centralized securities market, namely the: (1) primary market of equity; (2) secondary market of equity; (3) primary market of bond market; (4) secondary market of bond market

1. The Primary Market of Equity

(1) Equity on the Taiwan Stock Exchange

Products listed on the Taiwan Stock Exchange include Taiwan depositary receipts (TDRs), call (put) warrants, stocks, and exchange traded funds (ETFs). Currently, the most heavily traded product is stocks. In terms of market scale, there were 22 foreign secondary-listed companies with TDR issuance, 10,602 warrants, 874 domestic and foreign primary-listed companies, and 36 ETFs as of the end of 2015. There were a total of 11,534 listed

products, providing investors with a diversified selection of products. The total listed companies are 883 (including TDRs) as of September 2016.

(value in NT\$ Billion)

Items	Stock	TDR	Warrant	ETF
No. of Listing	874	22	10,602	36
Daily Trading value	82,752	91	2,643	6,698

(2) Market Capitalization

The total market capitalization of TWSE-listed stocks amounted to NT\$27.05 trillion as of September 2016.

The total capital invested by all listed companies was NT\$7 trillion as of the end of September 2016, representing an increase of NT\$50 billion from 2015.

In terms of fundraising, the amount raised in 2016 (as of September) through stocks by listed companies totaled NT\$98.4 billion. The total operating revenue of domestic listed companies as of August 2016 was NT\$ 18.87 trillion, a decrease by 1.29% compared to the same period last year.

(value in NT\$ Billion)

Items	2013	2014	2015	2016.09
No. of listing companies	838	854	874	883
Total Market Capitalization	24,520	26,892	24,504	27,045
Capital issued	6,610	6,783	6,951	7,034
Amount of fund raised	576.7	407.9	349.3	~
Operating revenue of domestic listed companies	26,875	28,391	28,061	~

(3) PE Ratio

In 2015, TWSE stocks traded at a price-to-earnings ratio of 13.46, whereas markets in Hong Kong, Singapore, and South Korea were trading at valuations ranging between 10 and 15, while those in London, Shanghai, Tokyo, and New York were between 17 and 19. In September 2016, price-to-earnings ratio has return to 17.28, which is considered

globally competitive.

P/E Ratio of Listed Stocks

year	2011	2012	2013	2014	2015	2016.09
P/E ratio	15.76	23.62	18.04	15.42	13.46	17.28

(4) Dividend Yield

TWSE-listed companies distributed NT\$1.0939 trillion in dividends to investors in 2015, up 17.74% from 2014, with an overall dividend yield of 4.60%. The dividend yield generated a comparatively higher rate of return than those of bank time deposits and exceeded yields of the major exchanges of New York, London, Tokyo, Shanghai, Hong Kong, and South Korea. The average stock dividend yield from 2011 to 2015 was 4.24%.

Dividend Yield of Listed Stocks

year	2011	2012	2013	2014	2015
Dividend Yield (%)	5.66	4.12	3.26	3.55	4.60

2. The Secondary Market of Equity

(1) The Taiwan Stock Exchange Capitalization Weighted Stock Index (TAIEX)

The TAIEX fell to a low of 7,627 in January, and slowly rose from February to 9,166 in September, and pushed up to 9,285 in October this year. In 2016, The Taiex topped to the range between 9,000-9,285 points, which is a relatively high point during the past years.

Taiwan Stock Exchange Weighted Index (TAIEX)

year	2011	2012	2013	2014	2015	2016.11.04
Stock index (point)	7,072	7,699	8,611	9,307	8,338	9,068

(2) Overview of Transactions

The annual trading value of the centralized market decreased by 2.34% from 2014 to NT\$22.51 trillion in 2015. The average daily trading value edged down slightly by 0.73% from the previous year to NT\$92.23 billion. Just like other places around the world, the daily trading value does not perform well which dropped from 92.23 billion of 2015 to 80.72 billion as of September 2016, a decrease of 12.5%. With regard to the daily trading value, Taiwan's regulators and related securities agencies are promoting stimulus plans hoping to regain investors' confidence.

(value in NT\$ Billion)

year	2011	2012	2013	2014	2015	2016(1-9)
Total trading value	26,996	20,789	19,603	23,043	22,505	14,529
No. of transactions (million)	220.1	183.8	184.235	208.3	211.9	141.8
Daily trading value	109.3	83.16	79.69	92.92	92.23	80.72
Growth (%)	-5.04	-23.92	-4.17	16.60	-0.74	-12.48

Margin trading accounted for 13.32% of the total stock market trading value. Margin trading dropped from nearly 30% in 2012 to closely 20% in 2015 and in 2016 (as of September), which affects the profitability of Taiwan's securities companies.

Day trading accounted for 3.67% of the total stock market trading value, has been increasing every day, to 7.13% in 2015, and 9.77% as of September 2016. It is hoped to boost it up to 20% from stimulus plan in the near future.

year	2011	2012	2013	2014	2015	2016(1-9)
Margin trading (%)	29.24	29.65	25.69	23.08	19.17	15.58
Day trading (%)	~	~	~	3.67	7.13	9.77

Foreign shareholdings and share trading have reached to record high every year. As of the end of September, 2016, foreign shareholdings were 39.15%, and share trading reached 30.40%. This indicative of how international capital continues to favor exceptional listed companies in Taiwan's centralized market. However, two uncertain possibilities may affect foreign holding in the market: (1) The MSCI may include China A share next year, which may affect Taiwan's weightings in indexes. (2) Some analysts worried that if the US Federal

Reserve raises interest rates, it would send foreign investors in Taiwan's stock market fleeing.

Foreign juridical investor

year	2011	2012	2013	2014	2015	2016(1-9)
Foreign Institutional Investor Holding (%)	31.10	32.62	33.14	36.43	36.69	39.15
Foreign Institutional Investor Trading (%)	21.80	22.60	24.60	23.80	28.40	30.40

TWSE's turnover rate of 77.55% ranked it above major markets such as Hong Kong, Singapore, and London, placing Taiwan's centralized market among the middle-to top-level global exchanges. These indicators are a clear testament to the TWSE's ability to meet the trading needs of the investing public.

Turnover Ratio in terms of trading value

year	2011	2012	2013	2014	2015	2016(1-9)
Turnover (%)	119.87	97.33	82.64	84.64	77.55	50.25

As the economy stagnates, and the Fintech continues developing, the securities companies are taking the chance to review their business models during this transformation period. Therefore, the numbers of securities companies and branches have been decreasing every year.

Securities companies

year	2011	2012	2013	2014	2015	2016(1-9)
Securities companies	130	121	120	119	120	117
Branches	1,028	1,033	993	964	965	941

3. The Primary Market of Bond

In Taiwan, bond trading mainly deals in the TPEX and OTC market, only a few bond trading prosecutes on the main market. In order to make bond trading more smoothly and safely, TPEX sets up all kinds of regulations to standardize the market.

The yield required by investors to loan funds to governments reflects inflation expectations and the likelihood that the debt will be repaid. The September economic indicators published by the National Development Council (NDC) on September 26 showed that the August economic monitoring indicator flashed green, while the economic composite score increased 2 points from July to 25 points, and the rises in both economic leading indicator and coincident indicator signal signs of gradual economic recovery. The yield on 10-year bond at the end of September rose 4bp from the end of August to close at 0.71%.

Bond issuance which includes government bond, financial debenture, beneficiary securities corporate bond, and foreign bond at the end of Sept. of 2016 amounted to NT\$8,911.22 billion. Government bonds accounted for the largest share of the total, amounted to NT\$5,524.37 billion, followed by corporate bonds amounted to NT\$1,865.46 billion.

Highlights of Bond issuance on TPEX Market

(value in NT\$ Billion)

year	Total	Government bond	Financial debenture	Beneficiary securities corporate bond	Corporate bond	Foreign bond
End of Sept. of 2016	8,402.22	5,524.37	991.92	12.46	1,864.46	9.01

4. The Secondary Market of Bond

The 5-year and 10-year benchmark bond yield closed around 0.56% and 0.71% at the end of September (as compared to 0.53% and 0.67% at the end of August). The daily turnover in the bond market averaged NT\$216.4 billion for the month of September (excluding International Bonds). The daily average of outright trade amounted to NT\$26.7 billion (12%) and that of RP/RS trade was NT\$189.7 billion (88%). The daily average of market

turnover increased 5% as compared to that in August (the daily market turnover in the month of August averaged NT\$205.4 billion (excluding International Bond); it amounted to NT\$28.8 billion (14%) for outright trade and NT\$176.6 billion (86%) for RP/RS trade).

Taiwan Government Bond 10Y



Trading Value of Bonds

(value in NT \$ Billion)

year	2011	2012	2013	2014	2015	2016(1-9)
Total Bond trading	71,562	65,200	51,895	50,450	52,239	37,444

C. Regulatory Development and Prospects for the securities industry

1. Financing Incentives to Support Real Economy

Integrating financial resources, the FSC has put forward the “**Financial Sector Supporting the Real Economy-Four Supports with Three Powers Project**” to achieve the objective of promoting the development of the real economy. This project got the Executive Yuan’s approval on 1 September, 2016.

The project is aimed to provide 3 power (fund, financial advice and business practice) into 4 categories: Commerce and industry, start-ups, innovation, and employment. Among them, with regard to fund, it plans to create two Funds:

- **Entrepreneurship Fund**

The Entrepreneurship Fund will be jointly funded by securities and futures related institutions and industry associations and will assist domestic startups in later stage and enhance links to the capital markets.

FSC will thus promote the Fund in unison with the National Development Council, the Ministry of Economic Affairs and related resources to build an entrepreneurship ecosystem that can develop sustainably and promote the transformation and development of the real economy.

- **Angel Fund**

To integrate power to jointly assist funding to domestic startups in seed stage, in the initial fund raising period banks and insurance related institutions will jointly donate the Angel Fund to help entrepreneurs realize their ideals and enhance the relationship based on mutual benefit and co-prosperity of the financial industry and other industries. In addition to providing capital, the Angel Fund will also attach importance to providing suggestions and sharing experience and will tap the expertise of the MOEA and MOST to jointly work for the development of entrepreneurship in Taiwan.

To effectively guide capital into main innovative industries, including green energy technology, Asian Silicon Valley, bio-pharmaceuticals, national defense industry, and smart machinery, innovative agriculture and recycled economy.

FSC encourages banks, with risk management in place, to provide more loans or guarantee to the main innovative industries. The maximum bank guarantee coverage for innovative industries has been increased from 80% to 90% to support their operation.

As in 2015, the total outstanding amount of loans extended to the creative industry reached NTD 258.2 billion, increasing by NTD 76.5 billion over that in 2014.

2. Sound Corporate Governance

Since the FSC launched the "Corporate Governance Roadmap 2013," we have achieved the following five goals, including cultivating corporate governance culture, promoting shareholder activism, enhancing board functions, disclosing material corporate governance

information and improving regulatory practices, which has received positive recognition from international institutions of cooperate governance.

The Asian Corporate Governance Association (ACGA) and Credit Lyonnais Securities Asia (CLSA) released its “CG Watch 2016” on September 29 2016, Among 11 Asian Markets, Taiwan corporate governance has ranked 4th, second only to Singapore, Hong Kong, and Japan. Comparing to the previous ranking in CG Watch 2014, Taiwan rises in the rank from no. 6 to no. 4, with the biggest improvement.

(1) Regulation

Taiwan Stock Exchange has designed “Stewardship Principles for Institutional Investors,” which has successfully gotten many signatories by encouraging institutional investors to sign on to the principles. The Stewardship Principles require the listed companies to conduct corporate social responsibility, adopt GRI G4 structure and so on. There are 87% of the listed companies which have independent directors, and 35% have audit committee.

(2) Enforcement

The Principles encourage Institutional Investors to participate in corporate governance through active attendance at shareholders' meetings, exercise of voting rights, engagement in appropriate dialogue and interacting with management, including board of directors or executives, of the investee company.

(3) Political and Legal Environment

Besides that the FSC launched the 5-year "Corporate Governance Roadmap 2013" providing clear policy plans and guidelines, and set up the Corporate Governance Centre integrating information and making regulations and enforcement easier and more accessible to the public.

(4) Adopting IFRS

Taiwan ranks third in accounting and auditing among the Asian countries. According to Taiwan regulator’s accounting and auditing report.

(5) Corporate Governance Culture

Many aspects of governance culture of listed-companies have greatly improved- such as companies adopting independent directors and audit committees are increasing; companies adopting e-voting, voting by poll are increasing; companies providing more disclosure in English. On the other hand, the Taiwan Stock Exchange conducts CG evaluation, and hosts propagation and promotion, seminars, and training, which enhance the quality of CG.

3. Prevent Money Laundering and Counter the Financing of Terrorism

(1) FSC adopts rules governing measures by financial services firms to prevent money laundering and counter the financing of terrorism.

In order to strengthen the regime of anti-money laundering and countering terrorism financing (AML/CTF) in Taiwan, and to enhance internal control and audit systems of financial institutions, the FSC has issued several AML/CTF guidelines (namely: "Directions Governing Anti-Money Laundering and Countering Terrorism Financing of Banking Sector," "Directions Governing Anti-Money Laundering and Countering Terrorism Financing of Insurance Sector," and "Directions Governing Anti-Money Laundering and Countering Terrorism Financing of Securities Sector"). These guidelines require banks, insurers, and securities firms to conduct customer due diligence and keep transaction records, and also require their risk management and internal control systems to contain the mechanism of assessment of risks associated with money laundering and financing of terrorism, as well as to devise the plan for preventing these risks

(2) FSC established the Task Force for Continuous Promotion

FSC established the Task Force for Continuous Promotion of Anti-money Laundering Activities and Combating the Financing of Terrorism, which consists of financial institutions and relevant parties invited by the Taiwan bankers association and the FSC. There are two working groups in this task force: "System Planning and Promotion" and "Risk Assessment". These two working groups have operated successfully and made a significant contribution to improvement of the domestic AML/CFT mechanism.