

2012 Taiwan Market Report

Asian Securities Forum

17th Annual General Meeting

November 22-24, 2012

I. Macroeconomic Overview

1. Economic Situation Summary

In July 2012, under the effects of the global economic slowdown, Taiwan's exports decreased by 11.6% from the same month in 2011, while imports decreased by 3.2%. Industrial production fell fractionally by 0.02% and export orders were down 4.4% year on year. Consumer prices (the CPI) climbed by 2.46%, and the unemployment rate rose slightly to 4.31% as a wave of new graduates entered the job market. On the financial side, July's M2 monetary aggregate growth declined to 3.8%, while the stock price index averaged 7,500 points. Although July's Taiwan Business Indicators showed some scattered signs of improvement, the economic situation still faced many challenges.

In order to actively respond to the impact of European economic weakness on Taiwan's economy, the government will continue to implement the "Economic Climate Response Program" featuring seven sets of strategies for stabilizing finance, holding down prices, increasing employment, promoting investment, helping industries, pepping up consumption, and boosting exports. At the same time, the government will closely monitor prices and take active price stabilization measures to avoid price fluctuation influenced by gasoline and electricity price adjustments.

Furthermore, the government will carry out the next wave of measures for reshaping Taiwan's economic structure, including strengthening technological innovation, bolstering cultural & creative enterprise, enhancing R&D and innovation, promoting the revitalization of traditional industries, and emphasizing the development of service industries, especially those that export services. At the same time, the government will promote the expansion of exports to emerging markets and diversification of export products. These initiatives should ensure that sound progress is kept up toward endowing Taiwan with a vigorous and sustainable new economy.

Table 1

% change on previous year	Historical Data				Current Data (2012)				
	2008	2009	2010	2011	Apr.	May.	June	July	Jan.-Jul.
GDP	0.12	-1.81	10.72	4.03	-	-	-0.16	-	-
CPI	3.53	-0.87	0.96	1.42	1.44	1.74	1.77	2.46	1.61
Unemployment rate	4.14	5.85	5.21	4.39	4.10	4.12	4.21	4.31	4.19
Exports	3.6	-20.3	34.8	12.3	-6.4	-6.3	-3.2	-11.6	-5.8
Imports	9.7	-27.5	44.2	12.1	2.1	-10.5	-8.4	-3.2	-5.4
Export orders	1.7	-8.3	20.6	7.2	-3.5	-3.0	-2.6	-4.4	-1.4
Industrial production	-1.8	-8.1	26.9	4.6	-2.3	-0.2	-2.4	-0.02	-2.6
Monetary aggregate (M2)	2.7	7.2	4.6	5.8	4.7	4.4	4.2	3.80	4.61
Stock market**	7,024	6,460	7,950	8,155	7,621	7,357	7,143	7,187	7,494

Note: * The DGBAS estimated that Taiwan's real GDP will grow 1.66% in 2012.

** Stock index (monthly average).

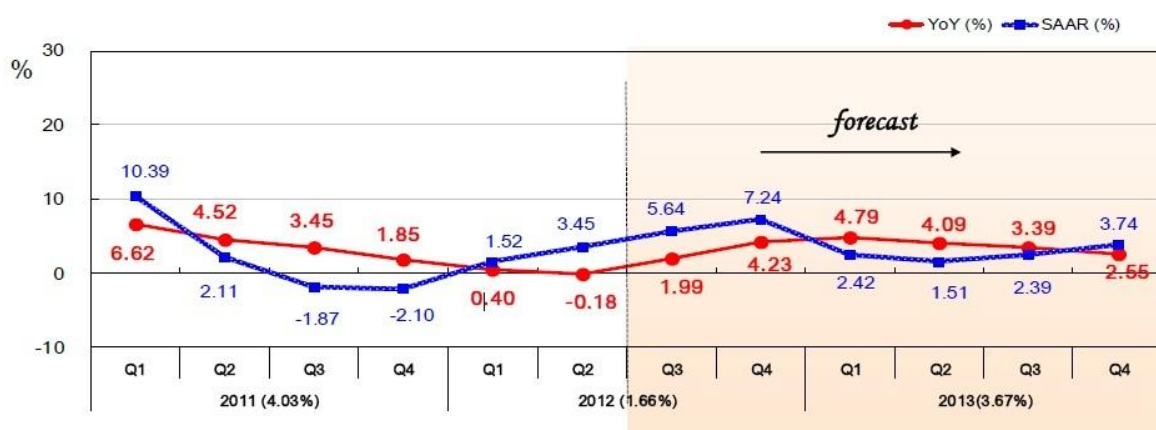
Sources: The Central Bank of China (CBC), Directorate-General of Budget, Accounting and Statistics

1.1 Economic Growth

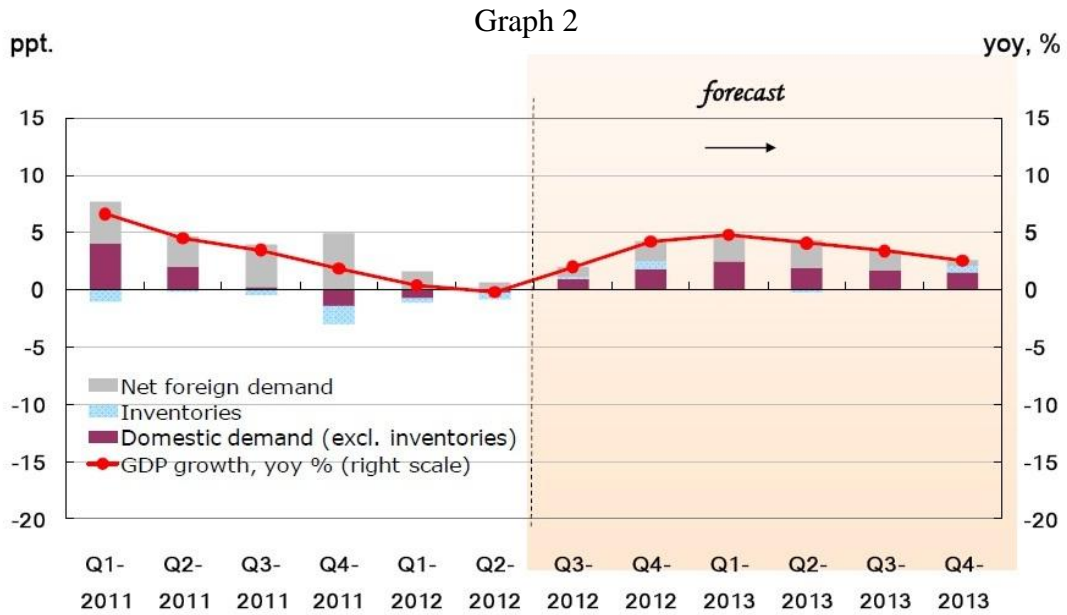
In Q2 2012, weakened external demand caused Taiwan's real exports of goods and services to shrink by 2.00%. With domestic demand also contracting slightly, GDP decreased by 0.18% from the same quarter of the previous year.

The seasonally adjusted annual rate (saar) of real GDP was 3.45% in Q2 2012.

Graph 1
Real GDP Growth



Source: Directorate-General of Budget, Accounting, and Statistics (DGBAS), August 2012.

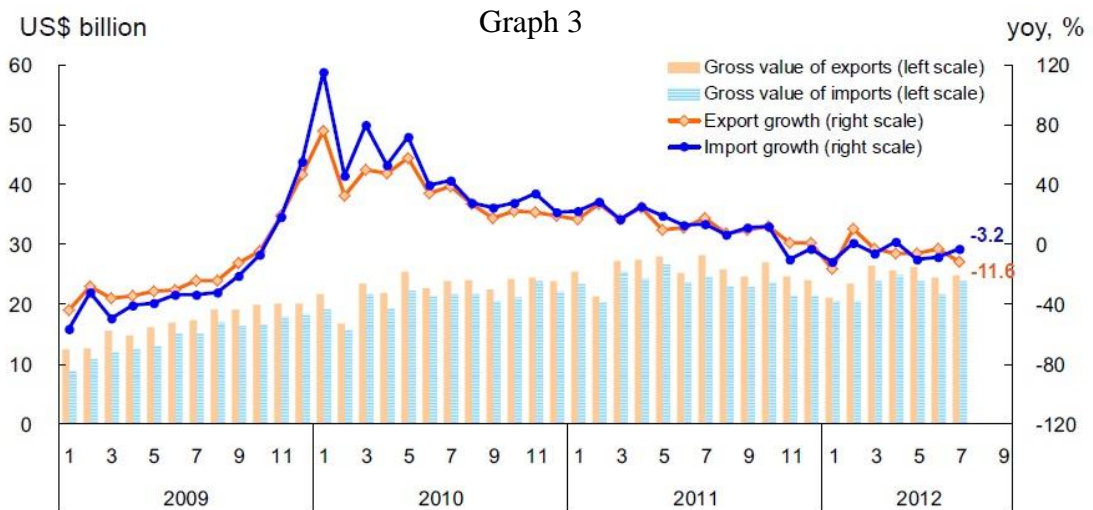


Source: Directorate-General of Budget, Accounting, and Statistics (DGBAS), August 2012.

1.2 Foreign Trade

In July 2012, exports declined by 11.6% year on year, mainly due to decreased export of ICT and electronic products. Imports decreased 3.2%, with most of the decrease in mineral products.

The month's foreign trade yielded a balance of US\$0.9 billion in Taiwan's favor.



Note: Trade data are adjusted according to the United Nations IMTS Compilers Manual (2004). Total exports include "exports" and "re-exports," and total imports include "imports" and "re-imports."
Source: Ministry of Finance, August 2012

Major Trade Partners

China (including Hong Kong) and ASEAN have become increasingly important trade partners to Taiwan since 2000.

Japan has remained Taiwan's largest supplier of imports, despite a narrowing share.

Table 2

Changes in Two-Way Trade with Major Trading Partners (yoy %)

	Exports					Imports				
	USA	Japan	Europe	China (incl. Hong Kong)	ASEAN 6*	USA	Japan	Middle East	China (incl. Hong Kong)	ASEAN 6*
2002	-2.7	-5.0	-5.9	29.4	7.4	-0.8	5.5	9.8	24.2	3.7
2002 Share	20.2	9.1	13.9	32.1	11.9	16.1	24.2	6.4	8.7	14.7
2003	-3.0	0.5	10.4	23.6	10.5	-6.9	19.6	43.7	30.9	5.2
2004	8.3	11.1	14.7	28.8	33.0	28.2	33.6	34.6	47.7	16.2
2005	1.3	9.4	-0.8	12.2	13.8	-2.8	5.3	36.5	16.2	3.8
2006	11.2	7.9	10.5	14.8	13.8	7.1	0.5	30.1	20.1	10.4
2007	-0.9	-2.2	9.7	12.6	16.7	17.0	-0.8	11.7	11.9	1.7
2008	-4.0	10.2	4.6	-0.8	7.3	-0.7	1.2	39.9	10.2	8.0
2009	-23.5	-17.4	-24.6	-15.9	-21.5	-31.0	-22.1	-42.2	-22.3	-22.8
2010	33.6	24.3	30.1	37.1	37.2	39.8	43.3	39.4	47.1	45.6
2011	15.6	1.3	6.3	8.1	22.7	1.5	0.6	14.7	20.5	13.5
2011 Share	12.2	6.8	10.2	40.7	14.8	10.2	21.7	12.8	15.3	11.8
2012 Jan-Jul	-12.4	-3.6	-8.2	-9.1	4.4	-10.3	-10.4	15.5	-6.3	-3.2

*ASEAN 6 refers to Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam. Source: Ministry of Finance.

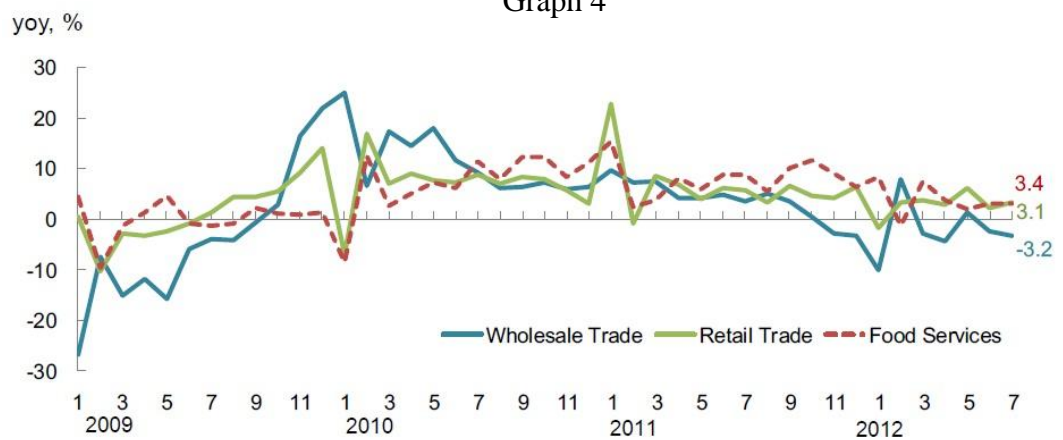
1.3 Domestic Consumption and Investment

1.3.1 Domestic Consumption

In Q2 2012, with the improving employment situation, private consumption grew by 0.76% from a year earlier, while government consumption increased by 2.41%. But domestic consumption momentum was offset by a lull in stock market activity and a sell-off of financial assets.

Sales growth of trade and food services has slowed, with a decrease in wholesale trade partially offset by a rise in retail trade and food & beverage services.

Graph 4

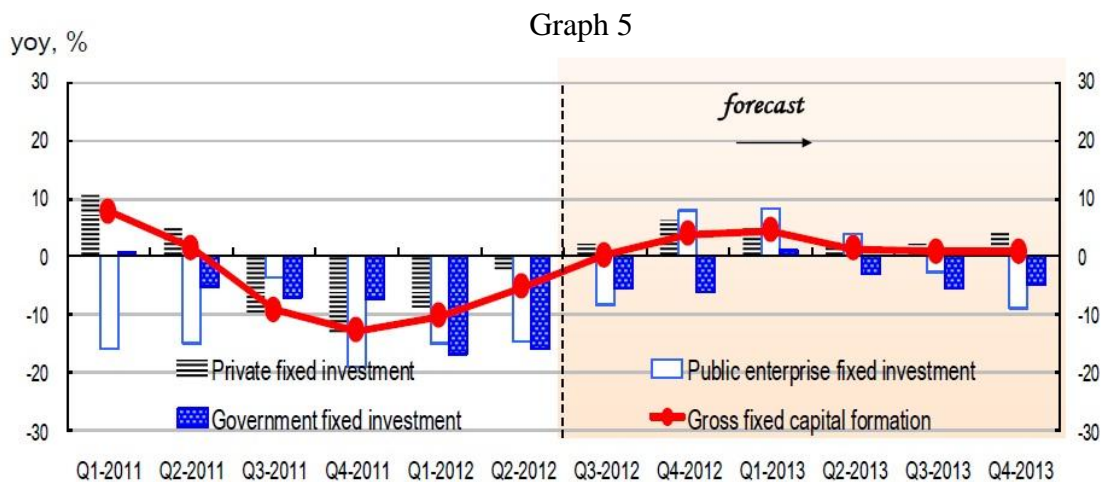


Source: Ministry of Economic Affairs, August 2012.

1.3.2 Domestic Investment

In Q2 2012, private fixed investment and gross fixed capital formation fell 2.21% and 5.24%, respectively. Gross fixed capital formation for Q1 2012 was revised to minus 10.24% from minus 10.54%.

This drop in private fixed investment was caused by investment plans being put on hold due to the weak economy, with imports of capital equipment continuing to decline.

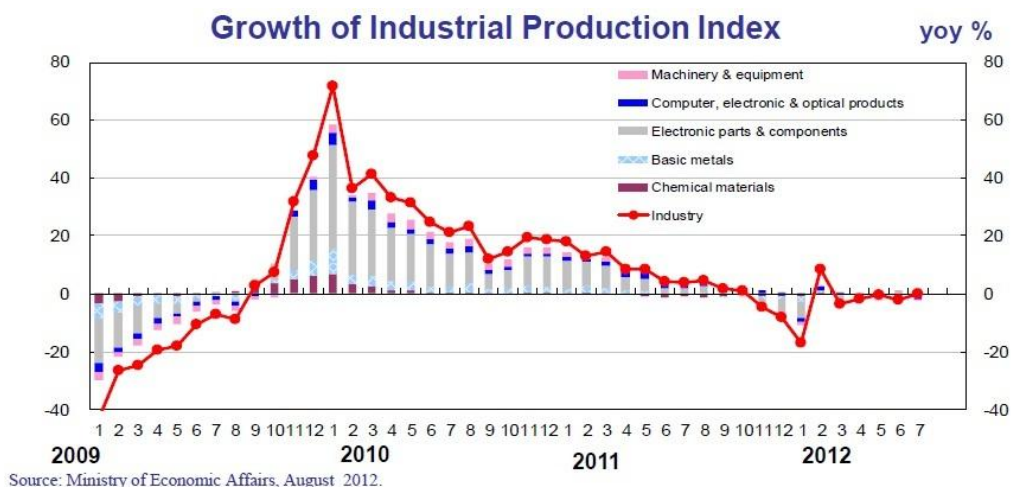


Source: DGBAS, August 2012.

1.4 Industrial Production

Industrial production index posted an annual increase of 1.89 % in August 2012. Referring to the production status of each industry, manufacturing increased 1.80%, mining & quarrying increased 6.04%, electricity & gas supply decreased 0.03%, water supply decreased 1.87%, and buildings construction increased 11.35%.

Graph 6

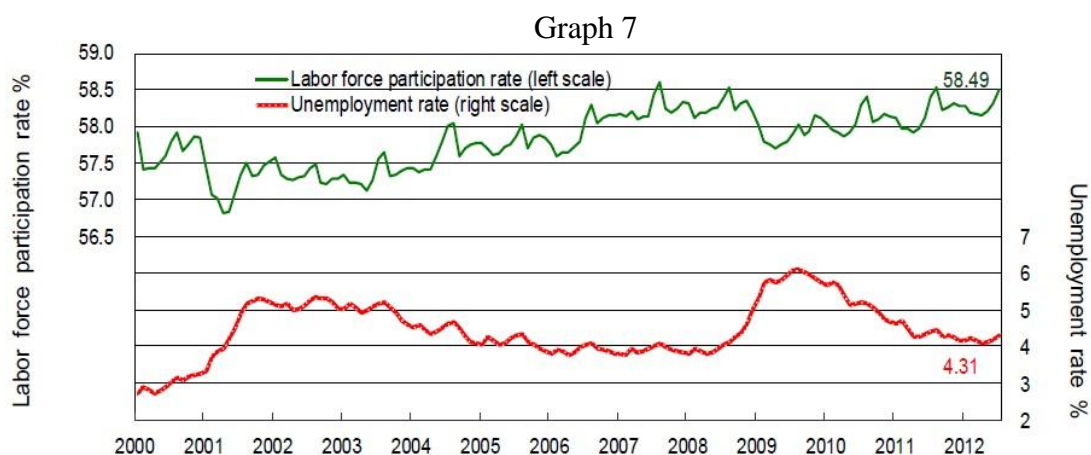


Source: Ministry of Economic Affairs, August 2012.

1.5 Employment and Labor Force

In July 2012, the unemployment rate stood at 4.31%, up 0.1 of a percentage point from the previous month, and 0.1 of a percentage point lower than a year earlier. The seasonally adjusted unemployment rate was 4.25%.

The labor force participation rate increased by 0.17 of a percentage point from the previous month to 58.49%, up 0.09 of a percentage point from a year earlier.

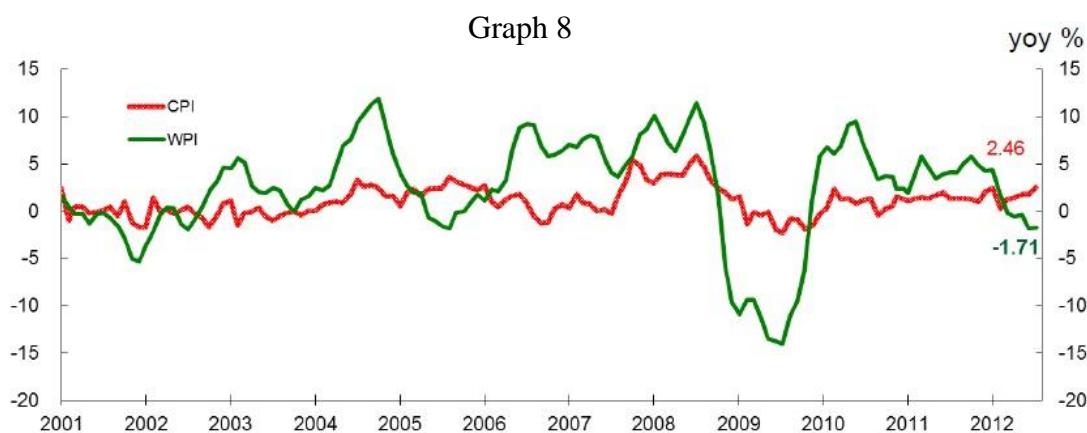


Source: DGBAS, August 2012.

1.6 Price

In July 2012, Taiwan's CPI increased by 2.46% from the same month last year. The most significant changes in CPI components were increases in the prices of vegetables and fruits. Core prices (excluding fresh food and energy prices) increased 0.96%.

The WPI in July fell by 1.71% year on year, due mainly to the decreasing prices of chemical materials and petroleum.



Source: DGBAS, August 2012.

1.7 Money and Interest rate

In July 2012, the annual growth rates of M1B and M2 declined to 2.88% and 3.80%, respectively, mainly due to net foreign capital outflows.

In July 2012, the monthly growth rates of M1B and M2, measured on a daily average basis, were 0.21% and 0.23% respectively.

Graph 9



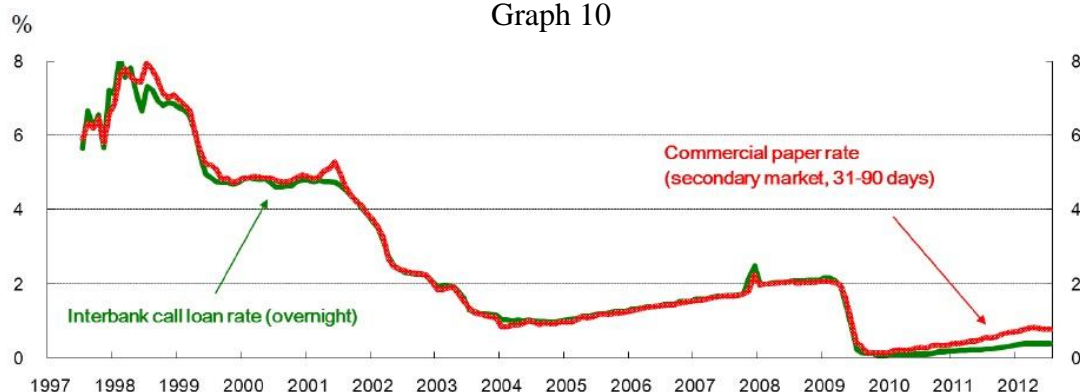
Note: The definition of M2 was changed in January 2012 to exclude structured products issued by banks. This historical data revision was retrospective to January 2001.
Source: Central Bank of China (Taiwan).

1.8 Interest Rates

In July 2012, interest rates remained at low levels, with the commercial paper rate at 0.8%, down from 0.82% in June, and the interbank rate at 0.445%, down from 0.513% in June.

To help Taiwan's economy maintain stable growth amid global economic uncertainties, and with the need to closely monitor price movements, the CBC decided to keep interest rates unchanged in July 2012.

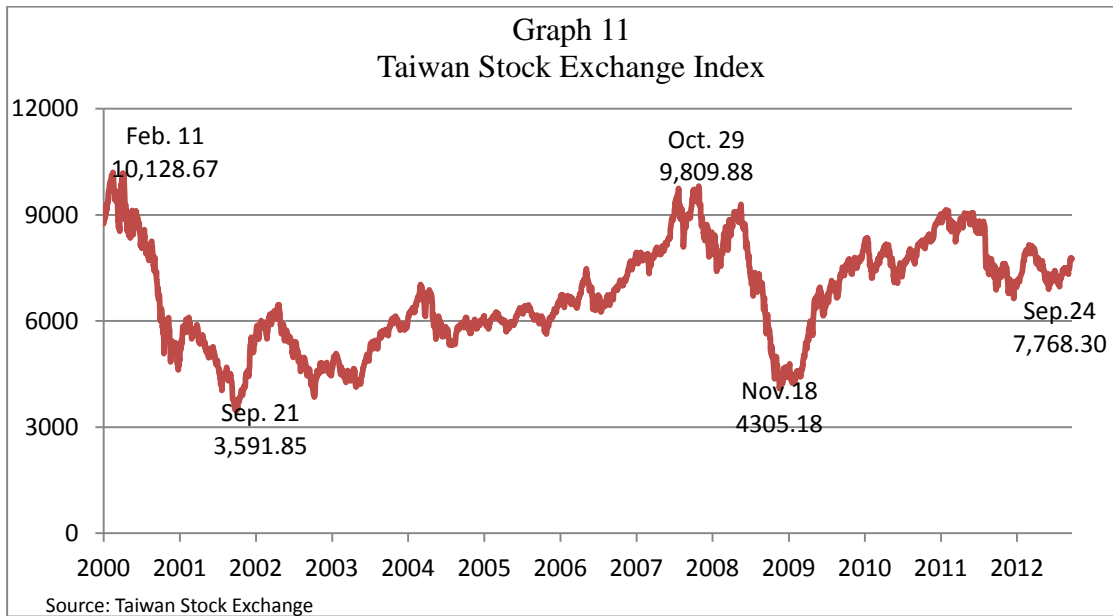
Graph 10



Source: Central Bank of China (Taiwan).

1.9 Stock Prices

In September 2012, the average closing level of Taiwan's stock exchange index was 7,768, up 5.5% from August. The rise was mainly a reflection of surging share prices on major international stock exchanges.



II. Outline of Taiwan's Capital Market

1. Securities Market

To cope with the changing global environment and the increasing global competition, the FSC and Taiwan's securities-related organizations endeavor to make the market internationally attractive and competitive. The aims are for the Taiwan securities market to become an important player in the international arena, to find a niche in the global capital markets, and to serve as a regional fund raising and asset management center.

The Taiwan stock market, with its fully automated trading systems and book entry mechanisms, is known as one of the most active exchanges in the Asia Pacific region. At the end of June 2012, the total market capitalization of the 797 companies listed on Taiwan Stock Exchange (TWSE) amounted to US\$666 billion. The ratio of Taiwan market capitalization to GDP was 139.80% in 2011. In 2011, the total trading value was US\$899.87 billion, representing a market turnover rate of 119.87%. The market P/E ratio of the Taiwan market was 15.76, fourth among primary Asia exchanges, making it an attractive marketplace for investors.

Over the past decade, the securities market in Taiwan has continued to grow on three fronts: the number of shares, the scale of the market and the share price. The overall market turnover rate has an even more impressive performance given its ranking as the number one or two of the Asia region. The ratio of market cap to GDP is comparable to those of the developed markets. All of the above factors clearly demonstrate that the enterprises listed in Taiwan enjoy the favor of the investors and the added-value from their active trading.

Table 3 Comparison of World's Major Securities Markets (Turnover Rate) Unit: %

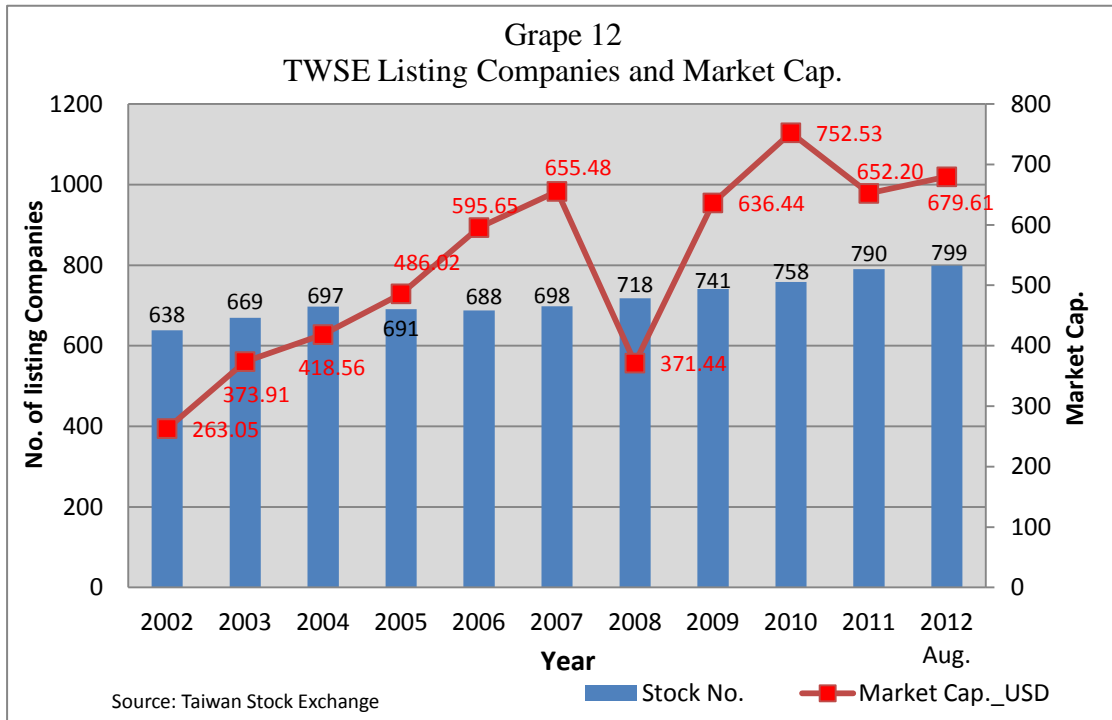
Year	Taiwan	New York	Tokyo	London	Hong Kor	Korea	Singapore	Shanghai
2002	217.41	94.80	67.90	97.30	39.70	254.40	53.80	60.33
2003	190.82	89.50	82.60	106.60	51.70	193.10	74.40	118.00
2004	177.46	89.80	97.10	116.60	57.70	147.20	60.80	87.00
2005	131.36	99.10	115.30	110.10	50.30	206.90	48.40	82.10
2006	142.20	134.30	125.80	124.80	62.10	171.40	58.20	153.80
2007	153.28	167.10	138.40	154.20	94.10	192.60	77.60	211.00
2008	145.45	240.16	151.20	152.73	86.04	196.27	63.67	118.01
2009	178.28	158.72	119.65	91.14	78.95	241.58	67.30	228.78
2010	136.74	130.19	109.64	76.13	62.17	176.31	53.30	178.47
2011	15.76	14.55	21.00	10.06	9.68	10.90	7.67	13.40

1.1 Taiwan Stock Exchange (TWSE)

Taiwan Stock Exchange (TWSE) was established in 1961, TWSE has kept pace with the market development and the most up-to-date technologies. TWSE works with competent authority, Financial Supervisory Commission (FSC), to deregulate

and liberalize Taiwan's stock market, and gears itself up more in line with major international market.

According to the website of the TWSE, the market capitalization of the TWSE has increased 70% from about US\$371 billion in 2008 to about US\$665 billion in July 2012.



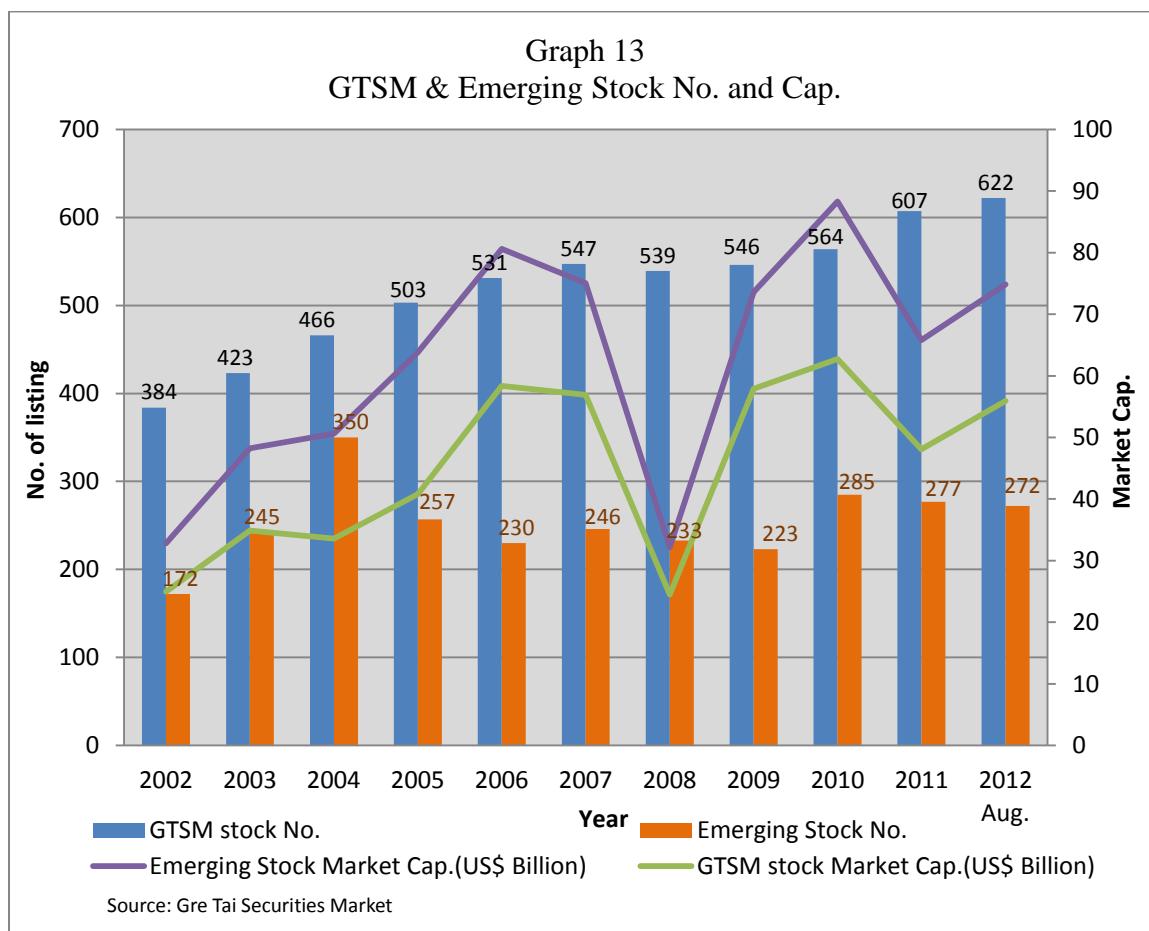
1.2 GreTai Securities Market

To further develop Taiwan's capital market, the SFB appointed a 20-member committee to set up the R.O.C. Over-the-counter Securities Exchange (ROSE) on July 21, 1994, which subsequently has been officially renamed the GreTai Securities Market (GTSM). The GTSM, as differentiated from the TWSE, assumes the role of fostering a robust capital market for less mature, but perhaps faster growing, small and mid-sized enterprises. The GTSM is organized as a non-profit organization with initial funding by donations and operational supports from Taiwan Securities Association, the Taiwan Stock Exchange Corporation, and the Taiwan Securities Central Depository Co.

The GTSM was upgraded from the OTC Trading Service Center, then under the direction of Taipei Securities Dealers Association. The GTSM has provided facilities for securities transactions and the trading information since mid 1994, and has also assumed market-monitoring responsibilities. The GTSM upgraded outdated payment and accounting systems, replacing them with computerized trade matching algorithm, centralized depository, and payment transfer systems. Moreover, to provide investors with accurate and continuous trading information,

the exchange implemented the “GreTai Index” on December 12, 1995.

As of August 2012, altogether 894 firms with total market capitalization of US\$74.84 billion were listed on the general board and the emerging market board of GTSM. In recent years, GTSM has been actively introducing new systems in the bond market and launching new financial products, planning the international bond market issuance system, constructing electronic over-the-counter derivatives trading system, and boosting the scale and international visibility of Taiwan’s bond market.



2. Bond Market

As the end of August 2012, 1,326 issues of bonds in the sum of NT\$7,311.89 billion and US\$0.86 billion were offered on GTSM, which showed continuing growth in the sum of issue. The bond products circulating on the market included 101 issues of government bond in the sum of NT\$4,864.15 billion; 417 issues of bank debenture in the sum of NT\$905.68 billion; 24 issues of beneficiary securities in the sum of NT\$43.17 billion; 448 issues of straight corporate bond in the sum of NT\$1,325.29 billion (including stripped corporate bonds); 331 issues of convertible (exchangeable) bond in the sum of NT\$170.61 billion; 2 issues of

foreign bond in the sum of NT\$3 billion; and 3 issues of Formosa bond in the sum of US\$0.86 billion.

3. Futures Market

To enhance Taiwan's position in the international financial market, the competent authority and relevant sectors took actions to build a domestic future market. The Futures Market Promotional Committee was established in December 1995, and the Exchange Preparatory Office was formally established in December 1996. The Future Trading Act passed through the legislative process in March 1997. With the completion of the legal framework and under the supports of all relevant parties, Taiwan Futures Exchange (TAIFEX) officially opened for business on July 21, 1998 and launched its first product—Taiwan Stock Exchange Capitalization Weighted Stock Index(TAIEX) Futures. This was followed later by Electronic Sector Index Futures, Finance Sector Futures, and Mini-TAIEX Futures.

In December 2001, the TAIEX options were introduced - expanding the product lines from the futures to the option markets, and thus expanding the range of hedging vehicles for investors. In January 2003, equity options were introduced - the first non-index-based product. In 2004, two interest rate products were introduced - 10-year Government Bond Futures and 30-day Commercial Paper Interest Rate Futures, and thus expanding the product lines from stock-price-based to interest-rate-based products.

In Commodities, TAIFEX Gold Futures was introduced in March 2006. In 2008 and 2009, TAIFEX NT Dollar Gold Futures and Gold Options were introduced, which provided additional risk hedging tools for cash market traders. Moreover, to provide stock investors with additional risk hedging and to reduce market tracking errors, single stock futures were introduced on January 25, 2010.

At present, TAIFEX has 19 products, including stock index futures, interest rate futures, single stock futures, equity options and commodities.

III. The Forecast of Taiwan’s Capital Market & Trends and Projections of Regulatory Policy

1. Important Financial Policy —Economic Stimulus Plan

Cross-strait financial operations have formally launched following the implementation of the cross-strait monetary clearance mechanism. On September 6, Taiwan government approved the plan “Financial Businesses with Cross-strait Characteristics,” which calls for the Financial Supervisory Commission (FSC), the Central Bank of the ROC, the Mainland Affairs Council, the Ministry of Economic Affairs and other related ministries to cooperate in its implementation.

The plan can be summarized as having “one axis, four levels, five cores and 10 highlights” and includes the launch of renminbi-denominated business operations across the board, a cross-strait modern financial transaction mechanism and businesses generating cash flows for e-commerce. It is expected to bring new business opportunities for Taiwan’s financial sector by carving a niche for it in the mainland Chinese market.

The 10 major points of this plan are as follows:

- (1) Launch renminbi-exchange operations at all domestic banking units
- (2) Establish a modern financial transaction mechanism
- (3) Kick-start businesses that facilitate cash flow for e-commerce
- (4) Allow credit and debit cards usable on both sides of the strait
- (5) Help Taiwanese financial institutions set up offices or branches on the Chinese mainland to serve Taiwanese businesses there
- (6) Allow sound mainland-based enterprises with Taiwanese backgrounds to be listed on the Taiwan Stock Exchange and GreTai Securities Market
- (7) Allow Taiwan’s publicly listed companies to issue renminbi-based bonds or other tools to raise capital
- (8) Develop asset and wealth management businesses in the Greater China region
- (9) Expand insurance-related businesses and services
- (10) Monitor and cooperate in the removal of obstacles to gain beneficial conditions for entry to the mainland market

The government anticipates that with the implementation of these points, Taiwan’s financial sector will be able to effectively collaborate with Taiwanese business operations in the mainland and increase its competitive edge in the Chinese market.

2. Closer-Strait Financial Market Opens More Widely

Since the Economic Cooperation Framework Agreement (ECFA) signed in June 2008, bilateral financial markets have become closer. The important cross-strait progress of financial market in the past year listed below:

October, 2011	<p>FHCs may set up VC management firms in mainland China FSC announced the opening of applications by financial holding companies, on behalf of wholly owned subsidiaries, for investment in the establishment of venture capital management companies in mainland China. Shareholding in the mainland Chinese companies, however, must exceed 25%.</p>
February, 2012	<p>Opening of business in RMB-denominated securities the offshore units of commercial banks allowed investing in marketable securities issued by government authorities and companies in the mainland area.</p>
April, 2012	<p>Taiwan and China pave the way for mutual establishment of economic and trade offices</p>
April, 2012	<p>Investment in China expanded for Taiwanese securities firms The FSC announced the opening of investment in mainland Chinese venture capital enterprises, venture management consulting companies, and financial consulting firms by Taiwanese integrated securities companies and their wholly owned subsidiaries. This relaxation will expand opportunities in China for Taiwan's securities houses and give their profitability a boost.</p>
July, 2012	<p>Warrants may be linked to Chinese securities issued overseas To give investors a more diverse range of investment choices and expand the size of the domestic warrant market, issuers to open up the issuance of call or put warrants linked to securities (such as N shares in the United States, H shares in Hong Kong, and S shares in Singapore) that are issued or managed by Chinese governments or companies in areas outside of China.</p> <p>FSC allows public companies to issue offshore RMB bonds, and encourages OBUs to invest in them FSC allowed public companies to issue offshore RMB bonds and permitting financial industry to invest in unrated Hong Kong RMB bonds (commonly called "dim-sum bonds").</p>

2.1 Investment Protection Agreement

Two years of negotiations have finally resulted in the signing of the Cross-Strait Investment Protection and Promotion Agreement between Taiwan and mainland China in August, 2012 formally establishing an institutionalized cross-strait mechanism that strengthens protection of the lives and property of investors. The agreement encompasses Taiwanese

businesses that invest through third areas, and marks a new milestone in cross-strait economic and trade relations.

Mainland China is the largest recipient of Taiwan's outward investment. For this investment, the Taiwanese investors need protection of their property and personal safety, preferably agreement-based.

This agreement is one of the most important fruit of ECFA, the cross-strait economic cooperation framework agreement. The agreement covers investments, investors, investment income, and relevant government provisions. The agreement is comprehensive. The wording is precise, and consistent with international standards. It establishes basic principles for investment protection. It emphasizes due process and non-discrimination. Besides protecting the security of investments, it specifies that investors must enjoy the same rights as local citizens, and calls for MFN treatment. The two sides pledged to improve treatment for investors, and a halt to new restrictive provisions. The current agreement is a giant step forward from what we had before.

2.2 Cross-strait currency clearing memorandum of cooperation signed

On August 31st, the Taiwan and China signed a Memorandum on Currency Clearing Cooperation Across the Straits. The two parties agreed to establish a cross-straits currency clearing mechanism based on principles and cooperation framework as defined in this Memorandum.

According to the Memorandum, each party will select a currency clearing institution to provide clearing and settlement service in its own currency. The selected institutions are authorized to transport and deliver cash according to related laws and regulations. The two parties have agreed for the two currencies to be used for payment and settlement in trade in goods and services, investments, and etc. The financial institutions may open accounts in either currency for settlements and other authorized business. Both parties, committed to the sound operation of the clearing mechanism, have put in place a supervisory cooperation mechanism, which consists of qualification requirements for currency clearing institutions, information exchange, confidentiality requirements, business examination, risk management, communication mechanism, and etc.

In the future, both the New Taiwan dollar (TWD) and yuan (renminbi) will be able to be used as a means of transaction on both sides, making it easier for business owners to manage their cash flow.

2.3 Offshore securities units (OSU)

To expand business for securities firms in Taiwan, the FSC is studying the feasibility of allowing such firms to run offshore securities units (OSU), which, once permitted, will bring back to Taiwan many offshore financial businesses including the popular RMB-based bonds floated by Taiwanese companies in Hong Kong.

The FSC will discuss with the Ministry of Finance and central bank the issue for allowing OSU involves issuing foreign exchange and tax preferences.

Overseas subsidiaries of Taiwanese securities firms are allowed to operate offshore financial businesses, whose scales are relatively small due to sizes of capitalization. If parent companies in Taiwan are permitted to handle offshore businesses, such business scale would accordingly be larger than those underwritten by subsidiaries.

3. Internationalization of Capital Market

3.1 Funding platform for hi-tech and innovative firms in Taiwan

The Fund-Raising Platform for Hi-Tech and Innovative Firms Action Plan which announced in 2010 designed to strengthen the competitiveness of Taiwan's high-tech and innovative enterprises and to attract international capital to the island.

To achieve this goal effectively, the government has accelerated work on related reforms, with ministries and other agencies engaging in the joint formulation of strategies. These include more competitive methods of levying taxes on new financial products and the provision, at a suitable time, of more liberal conditions for investment in Taiwan by qualified domestic institutional investors (QDIIs) in mainland China. Securities regulation has improved to provide a reasonable system with clear rules, and information transparency and adoption of International Financial Reporting Standards (IFRS) are being promoted so as to protect the rights of investors and come on line with the world.

3.2 Listed companies to start using IFRSs in 2012

The FSC is asking publicly listed companies in Taiwan to begin implementing the International Financial Reporting Standards (IFRSs) in January 2012, and to have the new standards fully in place in 2013. This will reinforce the transparency of information in the island's capital market and lower funding costs for enterprises.

IFRSs are becoming the general rules that govern accounting practices in capital markets worldwide. Companies that adopt IFRSs will not find their tax burden increased because of changes in financial reporting data; and, when they issue stocks, bonds, or depository receipts internationally, they will not have to recompile their financial reports.

Starting in January next year, companies that are listed on the Taiwan Stock Exchange or over-the-counter market, or are trading stock as “emerging stock” on the GTSM, and financial institutions governed by the FSC, will use a two track approach, using both the old and new systems.

They could self-evaluate their operating procedures, information systems, and internal controls, and gradually readjust and correct their company systems so as to produce IFRS compliant financial reports in 2013.

There are 110 capital markets around the world have already announced that they will adopt, or have already adopted, IFRSs. In Asia, Hong Kong, mainland China, and Singapore have already adopted the new standards, and Japan and the United States have announced that they will do so. It is extremely likely that IFRSs will become the generally accepted accounting principles worldwide.

IV. Conclusion

The IMF has revised the global economic growth to 3.5%, which is the lowest since 2008. Even though the European sovereign debt crisis is still on-going, facing the unstable global financial market, indicators show that economic growth in Asia region remains positive.

In Taiwan, we keep promoting “innovation” as the key component of our major competitiveness and have been approved by authoritative international ranking organizations. 2012 global competitiveness rankings by the Switzerland-based International Institute for Management and Development (IMD), Taiwan ranks top 8th in the world and top 3 in Asia for the past 3 years. In the “2011-2012 The Global Competitiveness Report” announced by World Economic Forum (WEF) , Taiwan’s development has upgraded from the stage of “Efficiency driven to innovation driven” onto the stage of “Innovation driven.”