

2014 Taiwan Market Report

Asian Securities Forum

19th Annual General Meeting

November 5-7, 2014

I. Executive Summary

In July 2014, the Taiwan Business Indicators showed that the domestic economy continued its steady growth. Among the indicators compiled by the National Development Council, the trend-adjusted leading index decreased by 0.12%, the trend-adjusted coincident index increased by 0.27% from the previous month, and the overall monitoring indicator flashed the "green" signal for the sixth consecutive month.

In the same month, Taiwan's exports and imports expanded by 5.8% and 9.5%, respectively, on July, 2013. Moreover, the annual growth rate of export orders and industrial production index were 5.7% and 6.1%, respectively. The annual change of CPI, compared with the same month of last year, rose 1.75%, mainly because the price of food climbed 4.27%. Compared with the previous month, the unemployment rate rose by 0.10 percentage points to 4.02% in July. On the financial side, the month's M2 monetary aggregate grew by 5.63%, and the stock price index averaged 9,474 points.

The global economy seems set for a moderate pace of recovery, but concerns about issues such as the trends of U.S. interest rates, Euro zone deflation and high unemployment rate, Mainland China's economic policy direction in the second half year of 2014, Japan's sales-tax increase, and the geopolitical risks of the situation in the Middle East and Ukraine may weigh on global economic trends, and even influence Taiwan's exports.

	Historical Data				Data for recent months			
	2010	2011	2012	2013	May	Jun.	Jul.	Jan.-Jul.
% change on previous year								
GDP	10.76	4.19	1.48	2.09	-	3.74 ^a	-	-
CPI	0.96	1.42	1.93	0.79	1.62	1.64	1.75	1.29
Exports	34.8	12.3	-2.3	1.4	1.4	1.2	5.8	2.5
Imports	44.1	12.0	-3.9	-0.2	-2.3	7.5	9.5	2.2
Export orders	26.1	7.2	1.1	0.4	4.7	10.6	5.7	5.5
Industrial production index	24.2	4.4	-0.3	0.7	5.4	8.6	6.1	4.7
Monetary aggregate(M2 ^b)	4.53	5.84	4.18	4.78	5.91	5.74	5.63	5.86
Unemployment rate(%)	5.21	4.39	4.24	4.18	3.85	3.92	4.02	3.98
TWSE Stock Index ^c	7,950	8,156	7,481	8,093	8,936	9,229	9,474	8,819

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 Statistic(DGBAS).

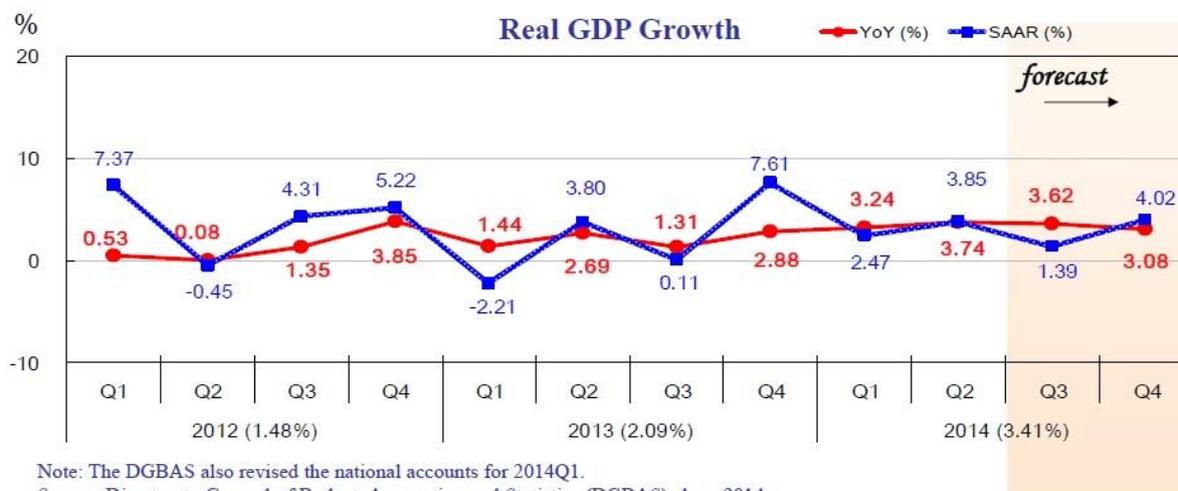
II. Economic Performance and Projections

Taiwan's Economic Situation and Outlook is designed to give domestic and foreign readers a concise analysis of Taiwan's current economic situation, including its economic growth, foreign trade, domestic demand, industrial production, employment, prices, and financial aspects. It also provides prospects for 2014 and 2015.

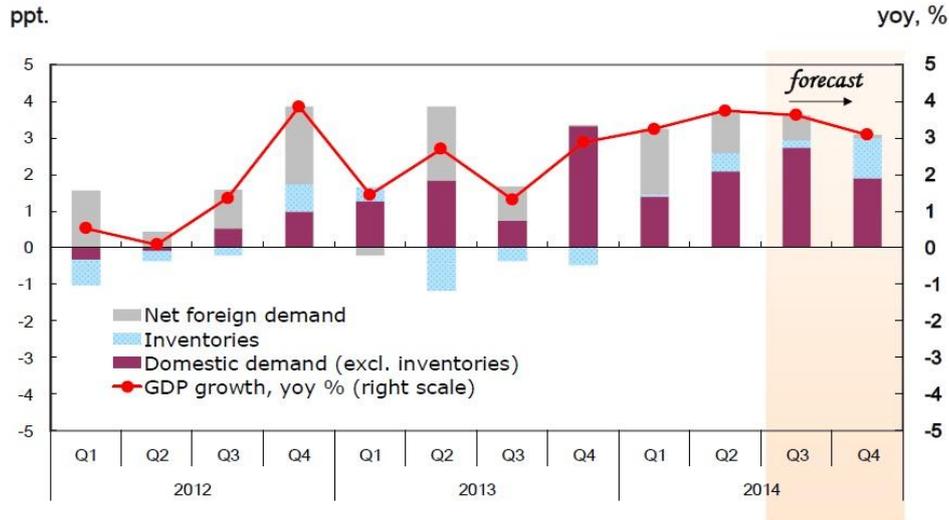
Mainly due to the domestic economy doing better than expected in the first half of 2014, plus upward revision of exports and private investment, the 2014 real GDP growth forecast has been revised to 3.41% in the DGBAS's latest estimation, up 0.43 percentage points on May's forecast of 2.98%. In the whole of 2015, real GDP is forecast to grow by 3.51%.

1. Economic Growth

In Q2 2014, due to the significant increase of travel and merchant revenues, Taiwan's commodity and service exports increased. Associated with the steady expansion of private consumption, real GDP grew at a year-on-year rate of 3.74%, higher than the 2.79% previously projected by the Directorate-General of Budget, Accounting and Statistics (DGBAS). The seasonally adjusted annual rate (SAAR) was 3.85%.



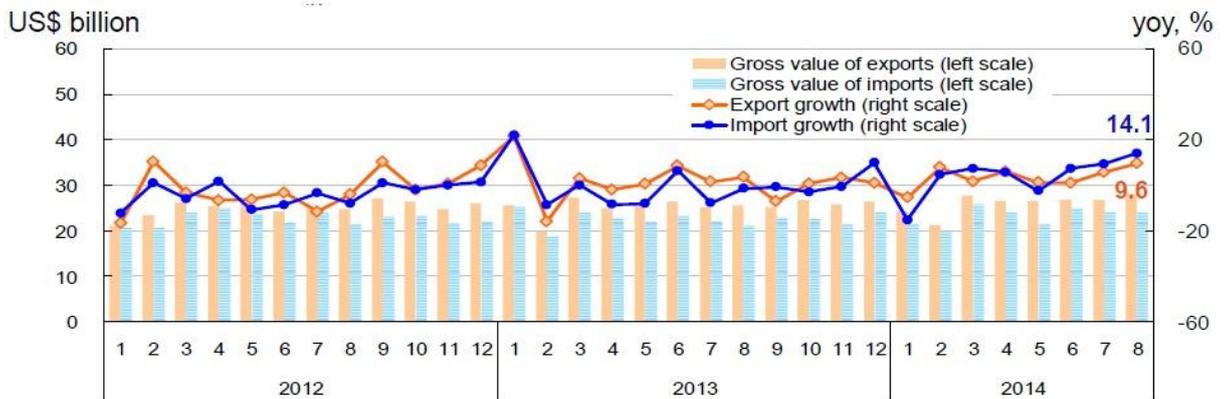
Contributions to GDP Growth (in percentage points)



2. Foreign Trade

In August 2014, total exports expanded 9.6% year on year, mainly due to increased export of electronic products, machinery, and basic metals & articles thereof. However, imports raised by 14.1% from a year earlier, with basic metals & articles thereof the main contributors to the increase. The month's foreign trade yielded a balance of US\$4.11 billion in Taiwan's favor.

Exports for the January through August 2014 period were up 3.4% on the same period a year ago.



Note: Trade data 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, Sep. 2014.

Major trade partners

Compared with the same period last year, exports for the first 8 months of 2014 to Europe, USA, Mainland China (including Hong Kong) and Japan grew by 7.5%, 5.8%, 4.1% and 3.4% respectively.

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

	Exports						Imports					
	Total	USA	Japan	Europe	China (incl. Hong Kong)	ASEAN 6*	Total	USA	Japan	Middle East	China (incl. Hong Kong)	ASEAN 6*
2004	21.1	8.3	11.1	14.7	28.8	33.0	31.8	28.2	33.6	34.6	47.7	16.2
2005	8.8	1.3	9.4	-0.8	12.2	13.8	8.2	-2.8	5.3	36.5	16.2	3.8
2006	12.9	11.2	7.9	10.5	14.8	13.8	11.0	7.1	0.5	30.1	20.1	10.4
2007	10.1	-0.9	-2.2	9.7	12.6	16.7	8.2	17.0	-0.8	11.7	11.9	1.7
2008	3.6	-4.0	10.2	4.6	-0.8	7.3	9.7	-0.7	1.2	39.9	10.2	8.0
2009	-20.3	-23.5	-17.4	-24.6	-15.9	-21.5	-27.5	-31.0	-22.1	-42.2	-22.3	-22.8
2010	34.8	33.6	24.2	30.1	37.1	37.2	44.1	39.8	43.3	39.4	47.1	45.6
2011	12.3	15.6	1.2	6.2	8.1	22.7	12.0	1.5	0.5	14.7	20.5	13.4
2012	-2.3	-9.3	4.2	-7.8	-4.4	9.8	-3.9	-8.4	-8.9	20.2	-3.8	-3.9
2013	1.4	-1.2	1.2	-3.5	2.2	3.9	-0.1	6.8	-9.2	0.6	1.6	3.4
2014 Jan.-Aug.	3.4	5.8	3.4	7.5	4.1	2.8	3.6	8.0	-3.2	-4.2	12.8	8.3

*ASEAN 6 refers to Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam.

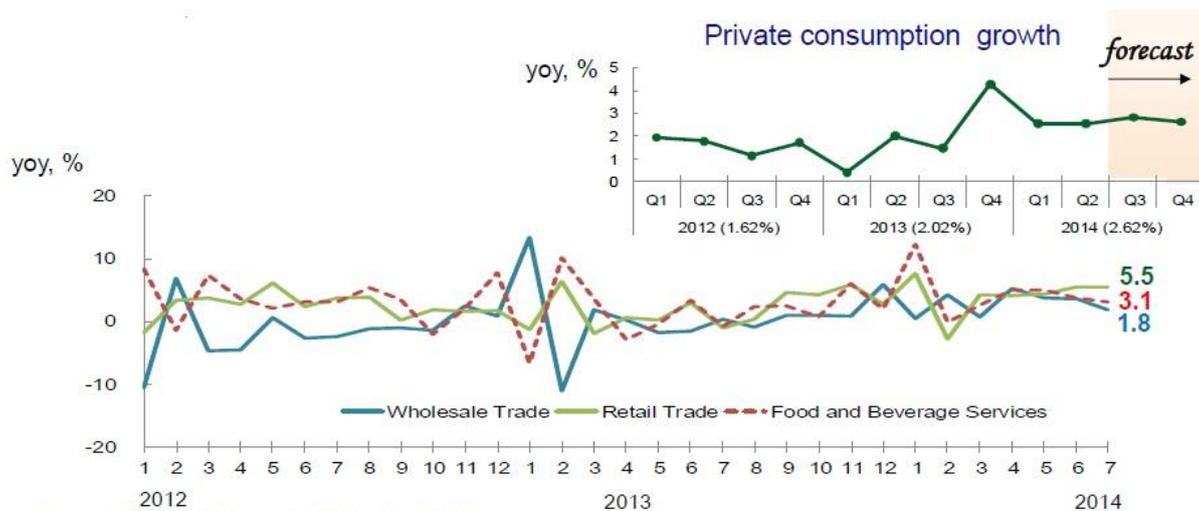
Source: Ministry of Finance, Sep. 2014.

3. Domestic Consumption and Investment

a. Domestic Consumption

In Q2 2014, private consumption grew 2.53% on a year earlier, with consumer sentiment improving significantly due to better feelings about the employment situation, more willingness of enterprises to raise salaries and a stable revival in stock market activity. Government consumption increased 1.05% .

In July 2014, sales of trade and food services posted an annual increase of 2.8%. Wholesale trade, retail trade and food & beverage services increased 1.8%, 5.5%, and 3.1% respectively.

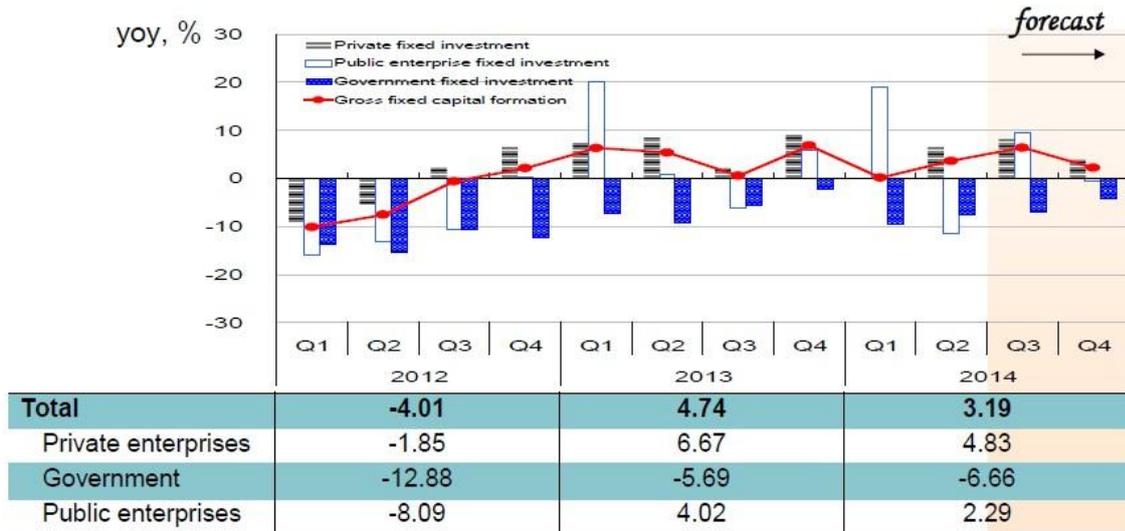


Source: Ministry of Economic Affairs, Aug. 2014.

b. Domestic investment

In Q2 2014, gross fixed capital formation was up 3.69% yoy, with private enterprise gross fixed capital formation increasing 6.58%. The increase was mainly generated by new investment in semiconductor production, 4G network building, and aircraft purchasing.

The DGBAS has projected that gross fixed capital formation will increase by 3.19% in 2014.

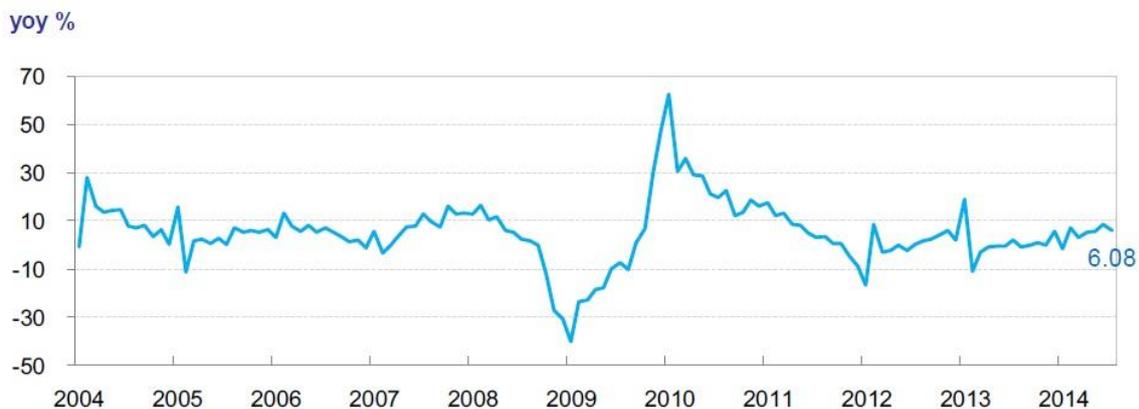


Source: DGBAS, Aug. 2014.

4. Industrial Production

In July 2014, the industrial production index (IPI) posted an annual increase of 6.08% following an increase of 8.61% in June.

Manufacturing output, which makes up more than 90% of the IPI, rose by 6.77% year on year in July, growing for the sixth consecutive month. The growth came largely from increasing demand for electronic parts & components, computers, electronics and optical products, and machinery and equipment.



Source: Ministry of Economic Affairs, Aug. 2014.

5. Unemployment Rate and Labor Force Participation Rate

In July 2014, the unemployment rate stood at 4.02%, up by 0.10 percentage points on the previous month. In contrast, the seasonally adjusted unemployment rate declined by 0.02 percentage points to 3.95 %.

The labor force participation rate increased by 0.18 percentage points from the previous month to 58.63%, and up 0.08 percentage points on a year earlier.



6. Prices

In August 2014, Taiwan's CPI rose by 2.07% on the same month last year. The food index went up 5.60%, mainly due to the surging indexes for meat, fruit, and food away from home. Core prices (excluding fruit, vegetable and energy prices) increased by 1.67%.

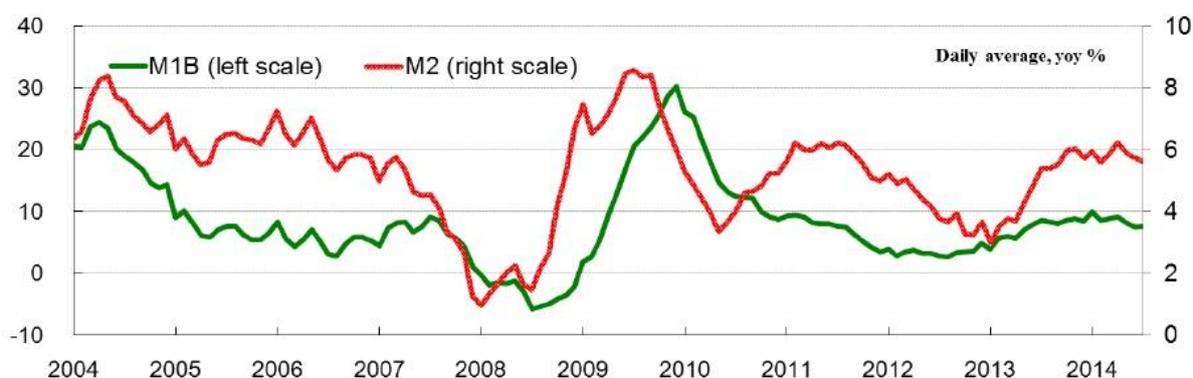
In the same month, the WPI increased by 0.12% year on year, mainly because, the indexes for water supply, electricity, and natural gas climbed. However, the indexes for computers, electronic, and optical products decreased.



7. Money Supply

In July 2014, the annual growth rates of M1B increased to 7.65%, mainly owing to rising demand deposits induced by brisk trading in the stock market. The annual growth rate of M2 decreased to 5.63%, mainly due to decreased net foreign capital inflows.

For the first seven months of this year, the average annual growth rates of M1B and M2 were 8.53% and 5.85%, respectively.



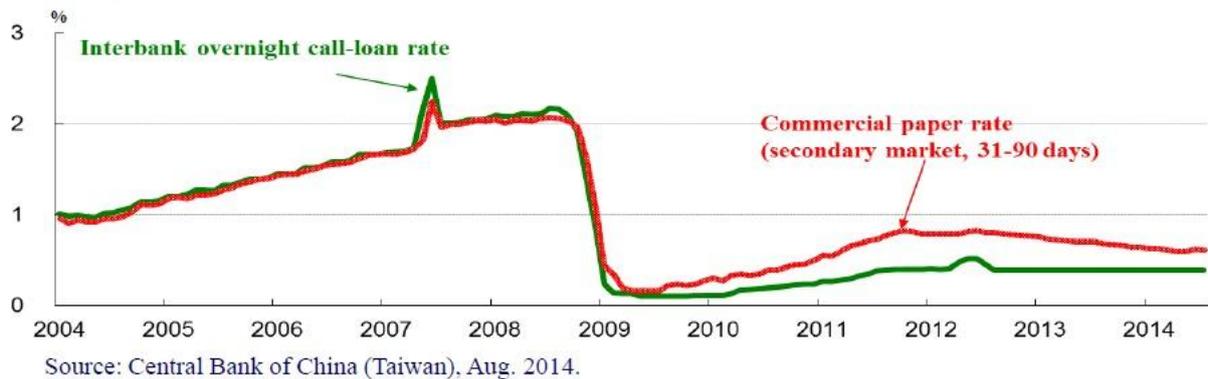
Source: Central Bank of China (Taiwan), Aug. 2014.

8. Short-term Interest Rates

In July 2014, the interbank overnight call-loan rate stood at 0.387%, and the commercial paper rate decreased to 0.61%, both reflecting that domestic interest rates were broadly stable.

Considering the combined factors of stable inflation outlook and domestic actual output remaining lower than the potential level, plus lingering uncertainties in the global economy, the CBC decided to keep policy rates unchanged in June 2014. The discount rate, the rate on accommodations with collateral, and the rate on accommodations without collateral will remain at 1.875%, 2.25%, and 4.125%,

respectively.



9. Stock Price

The TAIEX average closing price for the month of August was 9,266, down by 2.2% on July 2014, while up by 16.8% on August 2013.



III. Taiwan Securities Markets

1. Securities Market Infrastructure Overview

The Taiwan stock market, with its fully automated trading systems and book-entry mechanism, is known as one of the most active securities markets in the Asia-Pacific region. The Taiwan Stock Exchange (TWSE) is the primary equities market in Taiwan. In addition to the TWSE, there are two other regulated markets, i.e. the Gre-Tai Securities Market (GTSM), the market for bonds and small-and-medium sized enterprises (SMEs); and the Taiwan Futures Exchange (TAIFEX), the 55 principal derivatives market in Taiwan. Every trade is cleared and settled by the relevant market. The Taiwan Depository and Clearing Corporation (TDCC) provide the custodian and book-entry service.

- Market Structure by Products

<p>Taiwan Stock Exchange & Gre-Tai</p> <p>Securities Market</p> <p>Equity Cash</p> <ul style="list-style-type: none"> ➤ Stocks <p>Main Board: Taiwan Stock Exchange</p> <p>SME Board: Gre-Tai Securities Market</p> <ul style="list-style-type: none"> ➤ Warrants ➤ Taiwan Depository Receipts (TDRs) ➤ ETFs ➤ REITs <p>Fixed Income</p> <ul style="list-style-type: none"> ➤ Government Bonds ➤ Corporate Bonds <p>Convertible Bonds</p> <p>Straight Bonds</p> <ul style="list-style-type: none"> ➤ Foreign Bonds 	<p>Taiwan Futures Exchange</p> <p>Equity Derivatives</p> <ul style="list-style-type: none"> ➤ Index Futures ➤ Single Stock Future ➤ Index Options ➤ Equity Options <p>Other Derivatives</p> <ul style="list-style-type: none"> ➤ Bond Futures ➤ Interest Rate Future ➤ Gold Futures ➤ Gold Options <hr/> <p>Gre-Tai Securities Market</p> <p>Over-the-Counter Products</p> <ul style="list-style-type: none"> ➤ Convertible Bond Asset Swaps ➤ NTD Interest Rate Derivatives ➤ Bond Derivatives ➤ Structured Notes ➤ Equity Options ➤ Credit Derivatives
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2. Securities Market

2.1 Taiwan Stock Exchange (TWSE)

TWSE was established in 1961, and is the primary equities market in Taiwan. TWSE has enjoyed a reputation for having maintained an orderly market and a cost-effective trading capability since its inception.

TWSE has implemented many reform measures in the past few years in order to bring it in line with international practice, and to better reflect investors' diversified needs. The Taiwan market is set to continue making progress towards liberalization and internationalization.

The Taiwan stock market is one of the world's most active securities markets. At the end of July 2014, total market capitalization of 846 listed companies on the TWSE amounted to US\$ 888 billion. The average daily trading value was US\$ 3.32 billion, translating into a market turnover rate of 52.65% of July 2014.

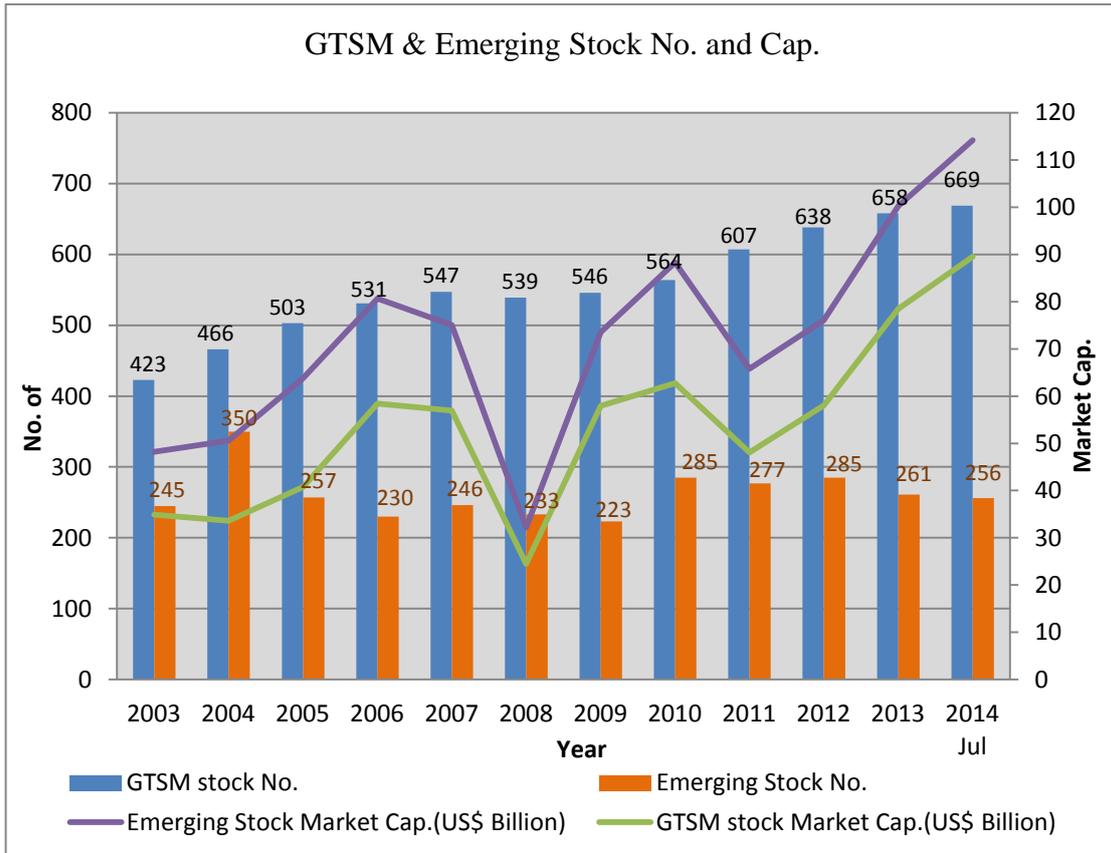


2.2 GreTai Securities Market (GTSM)

GreTai Securities Market (GTSM) is a diverse financial service center in Taiwan that offers the trading of stocks, bonds and derivatives. Founded in 1994, GTSM is a public interest entity aiming to promote the development of Taiwan's securities market. Since its inception, GTSM has been playing an active role in helping emerging high-tech industries and small and medium enterprises list stocks and raise funds on capital market and in the expansion of Taiwan's securities market.

In a move to help foster the multitude of micro and small innovative enterprises in Taiwan and add value to innovation, the GTSM unveiled the Go Incubation Board for Startup and Acceleration Firms (GISA) on January 3, 2014. This new board adds another level to the capital market and emboldens innovative companies to bring fresh vitality to the economy and create more job opportunities. At the same time, it is hoped that the integrative counseling mechanism of the GTSM that comes with the launch of GISA will become an active force that propels industrial transformation and upgrading and further drives the rapid evolution of the creative industry.

According to the statistics as in December 2013, the GTSM ranked 39th among the 62 members of WFE in terms of market capitalization, 25th in terms of trade volume, and 2nd in terms of turnover rate. At the end of July 2014, total market capitalization of 669 listed companies on the GTSM amounted to US\$ 89.5 billion; total market capitalization of 256 listed companies on the GTSM amounted to US\$ 24.7 billion.



2.3 Taiwan Futures Exchange (TAIFEX)

Taiwan Futures Exchange (TAIFEX) was established in September 1997 and opened for business on 21 July, 1998. Since the inception, TAIFEX has effectively developed the hedging function, successfully created a more diversified environment offering the choice in investing and managing funds. The priority objective is to establish a more efficient, lower cost trading environment with core competency. TAIFEX have also actively promoted international exchanges and cooperation, a step-by-step move marching toward the goal of “world-class futures exchange.”

In 2013, the Taiwan futures market enjoyed total trading volume of 153,225,238 contracts and average daily trading volume of 622,867 contracts. Both figures were largely unchanged from those of the previous year. Some 109, 311,515 TAIEX Options traded on the year, accounting for 71.34% of the market’s total trading volume. According to FOW TradeData, TAIEX Options were the world’s sixth-most-traded index options in 2013. By participant, individuals accounted for approximately 51.54% and institutional investors for roughly 48.46% of total trading volume. Foreign institutional investors accounted for 10.85%.

2.4 Taiwan Depository & Clearing Corporation (TDCC)

Established in October 1989, the Taiwan Securities Central Depository (TSCD)

started its operation in January 1990. The company was renamed as Taiwan Depository & Clearing Corporation (TDCC) in March 2006 after the merger of TSCD and Debt Instruments Depository and Clearing Co., Ltd. (DIDC). TDCC is the only central securities depository (CSD) in Taiwan, providing securities depository, clearing, and settlement services for equities, fixed income, and money market. Different from most of the other CSDs in the world, TDCC's depository account features a two-tier legal structure with one-tier operational processing. TDCC maintains over 2,200 participants' accounts as well as 15 million investors' accounts.

With over 25 years experience, TDCC demonstrates the ability to deliver quality services while forging ahead with the market and the competent authorities to create a secure and efficient market environment. Today, as our participants and marketplaces continue to extend around the world, TDCC will actively participate in global events and cultivate good relationship with other CSDs to acquire necessary knowledge and skills to ensure safety and soundness of the local market infrastructure.

IV. Regulatory Developments and Prospects for the securities industry

1. Important Financial Policies

In order to stimulate market activity, the Taiwan Financial Supervisory Commission's (FSC) has a significant relaxation of the financial policies. The move is part of the FSC so-called "three arrows," a trio of policies aimed at stimulating market volume and activity from a persisting slump.

(1) Short Sales and Book Transfers of Securities Eligible for Margin Purchases and Short Sales Now Permitted at Prices Below the Previous Day's Close

In conjunction with the expansion of the range of securities that may be sold short at prices below the previous day's close to all securities eligible for margin purchase or short sale, in September 2013, the Financial Supervisory Commission (FSC) extended the securities eligible to be sold short at prices below the previous day's close from the beneficial certificates of domestic and foreign ETFs, the beneficial certificates of offshore ETFs, the equities comprising the Taiwan 50 Index, the equities comprising the Taiwan Mid-Cap 100 Index, and the equities comprising the Taiwan Technology Index to all securities eligible for margin purchases and short sales.

(2) Securities Dealers Allowed to Give Quotes for the Purchase (or Sale) of Securities at Limit-Up (or Limit-Down) Price

To improve securities dealers in undertaking hedging trades and trading flexibility, the Financial Supervisory Commission (FSC) on 9 March 2014 allowed securities dealers to give quotes for purchases (or sale) of securities at their limit-up (or limit-down) price.

(3) Investors Allowed to Engage in Sell-first Day Trading

The FSC announced that investors will be allowed to engage in sell-first day trading from 30 June 2014. With the prerequisite that securities firms have established a sound risk control mechanism to make sure there is a sufficient source of lendable securities, investors will be allowed to engage in long (sell-first) day trading of totaling 200 stocks, which are limited to the components stocks of the Taiwan 50 Index, the Taiwan Mid-Cap 100 Index, and the GreTai 50 Index. This deregulatory measure provides a counterbalance to the short (buy-first) day trading system, and affords investors an additional trading strategy to choose from, thus building out our securities trading mechanisms, attracting more participants into the capital market, and spurring greater momentum for Taiwan stock market.

2. Push for the use of OSU platform to expand business operations

To equip securities firms with the ability to succeed, it is necessary to allow them to establish Offshore Securities Units (OSU) in order to conduct offshore securities and foreign exchange business, which will enable the OSU to provide comprehensive investment services. Securities firms will no longer be required to confine their operations to the fiercely competitive local markets and can move their focus gradually to overseas markets. Securities firms will then be given greater control to establish leading international underwriting capacity among Taiwan securities dealers. Securities firms can also utilize their own funds to conduct foreign exchange financial instruments-related businesses and to help customers with the following investment and trading activities: exchange rates, interest rates, commodities and equities. In addition, customized products can also be designed to cater to customers' needs and requirements.

3. Free Economic Pilot Zone (FEPZs) program

In August 2013, Taiwan kicks off first stage of free economic pilot zone (FEPZs) program. In the area of financial services, the FEPZ plan calls for loosening restrictions on the range of services and products that firms can offer, with the loosening to be achieved through deregulation and simplification of procedures.

In recent years, a great deal of capital has flowed out of Taiwan to Hong Kong and Singapore, and many financial professionals have likewise relocated. The principles underlying deregulation of financial services in the FEPZ plan are (a) that such services need not be tied to the NT dollar, and (b) that the financial products and activities offered will be targeted mainly at foreign clients. The goal is to encourage capital to return by ensuring that any financial activities that can be conducted in Hong Kong or Singapore can also be conducted in Taiwan.

On this day Taiwan government granted certificates to 12 securities companies in Taiwan to conduct new types of international business through their offshore securities units (OSU). An OSU is an independent account set up in Taiwan for international securities business such as brokerage, underwriting and proprietary trading, and the OSU milestone is part of the government's push to carry out the Free Economic Pilot Zones (FEPZ) plan. According to the FSC, the overseer of Taiwan's financial institutions, the sector will need roughly 20,000 additional workers this year due to the deregulation of the securities business.

The FSC plans to launch Offshore Insurance Units (OIU) to develop the country into an international wealth management centre. Under the OIU scheme, international companies with Taiwan-based operations can avoid the complications involving fulfilling insurance requirements through domestic carriers and purchase policies denominated in the local currency, as foreign-currency denominated policies could be purchased. Foreign nationals working or visiting Taiwan can also take advantage of the OIU arrangement by availing of medical and travel insurance policies, denominated in the currency of their country of origin. The OIU arrangement is poised to be a vital addition to the offshore banking unit (OBU), and offshore securities unit (OSU) schemes that aids domestic financial institutions in expanding towards markets abroad. The draft OIU regulations and scheme expected to be launched by end of 2014.

Taiwan's financial sector moves toward liberalization, through the development of OBU, OSU and OIU, both the capital and personnel could flow back, while its banking and securities sectors expect to generate an additional US\$1 billion and US\$1.33 billion in revenue respectively within five years, according to government estimates.

4. Cross-strait Economic Cooperation Framework Agreement (ECFA)

The relax restrictions aid securities firms to go into the Mainland China market as well. In accordance with the provisions of the Cross-Strait Service Trade Agreement under ECFA, Taiwan's securities firms are permitted to establish fully licensed securities firms in Mainland China as joint ventures, and may own up to a percentage of 49% and 51%. Currently, the majority of Taiwan's securities firms is actively seeking partners and are searching for suitable locations for establishing and investing in their future securities operations. These plans, however, still require legislative approval in Taiwan. TSA request that the competent authority coordinate with Legislative Yuan to pass the Cross-Strait Service Trade Agreement under ECFA as soon as possible, preferably in the first half of this year. In addition, we ask that the competent authority announce to the securities industry the audit principles and practices applicable to joint ventures, the purpose of which is to improve the success rate of investing and establishing operations in Mainland China through review and guidance conducted in advance.

V. Conclusion

It has been said that "the capital market is a window into the country's economy; it also represents a country's national strength." To stimulate Taiwan stock market, the Taiwan FSC this year has a significant relaxation of the financial policies, such as permitting day trading, short-sales below the previous day's closing price, and dealers to buy and sell securities at trading halts due to price limits. On the other hand, in order to assist the securities industry in establishing overseas operations, the FSC eased restrictions on securities firms' overseas investments, to encourage securities firms to set up the well-known Asian regional securities company.

Given the rapidly changing nature of the international economic environment, uncertainty is an intrinsic part of global capital markets. Nonetheless, through the establishment of a fair, efficient, secure, friendly, and attractive investing environment for foreign enterprises and funds, we look forward to seeing Taiwan to be one of the region's finest international fundraising platforms, and in so doing usher in a new era of financial discipline, efficiency and globalization into Taiwan's capital markets.