

2017 Central Government Budget Overview

Forward

On May 20, 2016, Taiwan experienced the third transfer of governing power in a democratic process. In the face of escalating domestic and international challenges, people hold great expectations towards the new cabinet, hoping the government to launch policies which would lead the country out of the economic stagnation as soon as possible. In order to shape new governance models and policy objectives, the Executive Yuan will steer Taiwan's economic development in a new direction outlined in the president's administrative blueprint, whose core values are "innovation", "employment" and "fair distribution", to break through the constraints of the current situation and maximize the effectiveness of policies with limited resources.

In this year, global economy continues to be sluggish as in the past few years. As the main economies, such as Euro Area, Japan and China, have already taken monetary easing policies or fiscal stimulus measures, the recovery remains subdued. According to the projections of IHS Global Insight in Aug 2016, the global economic growth of next year is estimated at 2.8%, slightly better than 2.4% of this year, but lower than 3% for six consecutive years. In addition, the uncertainties caused by the effects of main economies' future monetary and interest policies on financial markets, as well as the aftermath of Brexit, have all cast shadows over the global economy.

As we look forward, while the gradual rebound of global economy and trade volume would help enhance Taiwan's exports in the short term, the slowdown of global demand for mobile devices and the expansion of China's domestic supply chain may still cloud Taiwan's long-term export prospect.

In terms of domestic demand, as the growth of private consumption is relatively suppressed as a result of flat employment and wages, the expansion in the advanced production capacity of semiconductors, as well as the efforts of the government to promote innovative industries, will both facilitate private investment. Overall, Taiwan's economy is expected to be slightly better in next year.

After years of economic slowdown, high youth unemployment, widening wealth gap, shift of jobs overseas, stagnant wages, low birthrate, and aging population, the new cabinet needs to think outside the box, from economic, social and other different aspects, to address the challenges at this stage.

The cabinet will focus on the six major administrative directions, which are 'accelerate industrial upgrading, create a new innovation-driven economy', 'strengthen a social safety net, forge a new just society', 'improve public infrastructure quality, foster a new environment of sustainable development', 'strengthen government management and efficiency, inject new vigor into rural regions', 'enrich educational and cultural content, seek a new equality for all ethnicities', 'bolster national safety, create new space for international and cross-strait relations'.

The government will, with teamwork and pragmatism, spare no efforts to promote policies beneficial to long-term national development and well-being of citizens, so as to

fulfill the vision of freedom, democracy, fairness, justice, prosperity and sustainability.

In order to make a budget consistent with the administrative policies and better utilize public resources, the Executive Yuan required all agencies not only to earn more and spend less, but also to review the priorities and performances of all administrative policies, and to utilize all budget resources based on the zero-based principle when approving the medium-term budget envelopes (2017-2020) for government agencies in April, 2016. Meanwhile, the cabinet requested each agency to identify at least 10% of discretionary spending (excluding personnel expenses) as savings to be reallocated to policy initiatives. Furthermore, all policy priorities should be fully financed within approved budget envelope set for each agency, or otherwise be funded by extra revenues sought by the agency.

After the new government took office, the Executive Yuan issued executive orders to command agencies take further austerity measures, add in new thoughts and means to achieve targets at least cost, re-evaluate priorities of policies, and reorganize the budget allocation within the original envelopes, so as to reshape a budget that reflects the president's commitments made in the campaign and the new government's core values of innovation, employment and fair distribution.

After agencies submitted their budget proposals in mid-June, the Executive Yuan held a cabinet meeting to deliberate on the budget allocation within limited resources and set guidelines to the 2017 Central Government Budget as follows: (1) the expenditure can only grow at a rate less than that of the revenue; (2) the deficit should not be higher than the previous year; (3) the debt growth of central government

can't exceed 3-year-average nominal GDP growth. To sum up, the government hopes to attain the administrative objectives, such as reforms and upgrades of the industries and improvements of the social care systems, while maintaining a sound public finance.

In terms of the overall budget arrangement, key policies of the current administration have been contained in the Budget, including:

- (1) Accelerating industrial upgrading and creating an innovation-driven economy. The Budget provides NT\$46.2 billion to support innovative industries.
- (2) Improving infrastructure quality and facilitating regional balance. The infrastructure spending is NT\$186.9 billion, NT\$5.7 billion (or 3.1%) higher than 2016. After factoring in NT\$15.7 billion from Special Budget of the Comprehensive River Basin Management Plan, the overall infrastructure expenditure amounts to NT\$202.6 billion, NT\$7.3 billion (or 3.7%) higher than 2016.
- (3) Improving the quality of education and cultivating talent. The education expenditure is NT\$285.3 billion, NT\$18 billion (or 6.7%) higher than 2016.
- (4) Expediting technology innovation and creating value added. The spending on technology programs is NT\$106.2 billion, NT\$4.1 billion (or 4%) higher than 2016. After factoring in NT\$7.7 billion of defense research expenditure and NT\$19.4 billion of R&D expenditure of SOEs and nonprofit special funds, it comes to a total of NT\$133.3 billion, NT\$5.5 billion (or 4.2%) higher than 2016.
- (5) Enriching cultural content and promoting ethnic equality. The culture expenditure is NT\$31.4 billion,

NT\$2.6 billion (or 8.8%) higher than 2016. The budget of Council of Indigenous Peoples is NT\$7.82 billion, NT\$0.22 billion (or 2.9%) higher than 2016. The budget of Hakka Affairs Council is NT\$2.81 billion, NT\$0.26 billion (or 10.2%) higher than 2016.

- (6) Improving access to and quality of long-term care services. The long-term care service expenditure, including NT\$13.8 billion from the general fund and NT\$6.5 billion from nonprofit special funds, net of NT\$2.5 billion of appropriation from the general fund to Long-Term Service Development Fund, is NT\$17.8 billion, NT\$11.1 billion (or 167%) higher than 2016.
- (7) Reinforcing food safety and protecting the public health. The food safety spending is NT\$3.65 billion, NT\$0.65 billion (or 21.9%) higher than 2016. After factoring in NT\$0.3 billion from nonprofit special funds, it totals NT\$3.95 billion, NT\$0.72 billion (or 22.4%) higher than 2016.

The preparation stage of the 2017 Budget has come to an end. The revenue is estimated to be NT\$1,845.7 billion, which increases by NT\$23.3 billion (or 1.3%) compared with 2016. The expenditure is set at NT\$1,998 billion, which increases by NT\$22 billion (or 1.1%) compared with 2016. The balance is estimated to be a deficit of NT\$152.3 billion. After taking into account the debt repayment of NT\$74 billion, NT\$226.3 billion will be financed by borrowing.

The Budget has been prepared with thorough planning and review. The expenditure expands moderately at a rate of 1.1%, less than 1.3% of the revenue. The increase of expenditure is mainly used to promote innovative industries, education and long-term care services. The deficit is NT\$152.3 billion, a decrease of NT\$1.3 billion compared with

2016.

The ratio of annual borrowing to expenditure is 11.3% in 2017, less than the loan cap of 15% regulated by the Public Debt Act. It decreases by 0.2pp compared with 2016. In terms of public debt dynamics, the debt outstanding is estimated to increase by 2.79%, less than the 3-year-average nominal GDP growth rate of 3.68%, and the debt to 3-year-average GDP ratio is 33.9%, 0.2pp less than 2016. It shows the government's determination to uphold fiscal discipline.

As for expenditures by function, Social Welfare expenditure of NT\$477.3 billion takes up the largest share of 23.9% ; Education, Science and Culture expenditure of NT\$415.4 billion takes the second place of 20.8% ; Defense expenditure of NT\$310.2 billion takes the third of 15.5% ; Economic Development expenditure of NT\$267.8 billion takes the fourth of 13.4%.

The main causes of the expenditure increase of NT\$22 billion include that:

- (1) Education, Science and Culture expenditure increases by NT\$27.5 billion, mainly due to higher educational expense and innovative industry plans.
- (2) Social Welfare expenditure increases by NT\$16.7 billion, mainly because of higher expenditure on the 10-year long-term care 2.0 plan, appropriation to Long-Term Service Development Fund, the government's contributions to National Health Insurance to meet the statutory floor set by the National Health Insurance Act, and premium subsidies for labor insurance and employment insurance.
- (3) Public Debt Transaction expenditure is slashed by

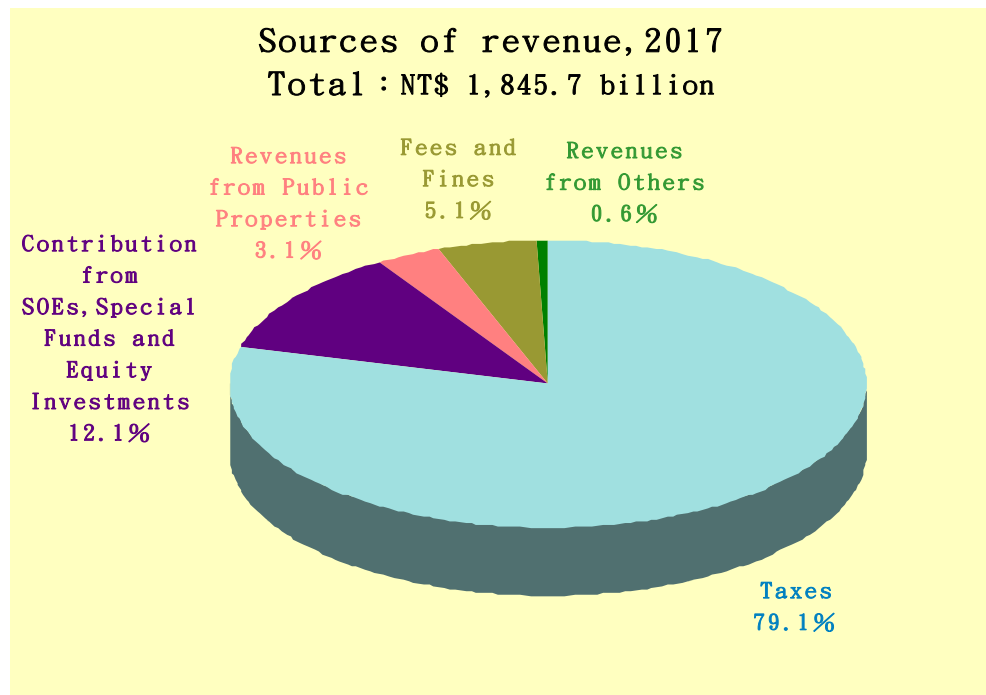
NT\$10.9 billion as a result of dropping interest rates.

- (4) Retirement and Survivor Relief expenditure is slashed by NT\$6.7 billion, mainly due to a declining number of veterans and the cut to repayment for arrears of the overdue preferential deposit interest subsidies, which was fully repaid in the previous year.

Based on the Budget arrangement mentioned above, the government estimates that the 2017 GDP will reach NT\$17.3 trillion, equivalent to US\$551.1 billion; the GDP per capita will be US\$23,395 and the economic growth will be 1.9%. Meanwhile, domestic prices maintain stable, with a moderate CPI increase of 0.8%. All these demonstrate that the Budget has strived to pursue a balance between economic development and fiscal soundness.

Analysis of Revenue and Expenditure

1.Revenue



Composition and Changes of Revenue

NT\$ billion

Item	2017		2016		Change	
	Amount (A)	%	Amount (B)	%	Amount (A-B)	%
Total	1,845.7	100.0	1,822.4	100.0	23.3	1.3
1. Taxes	1,459.3	79.1	1,440.0	79.0	19.3	1.3
Income Taxes	817.3	44.3	808.1	44.3	9.2	1.1
Business Tax	215.5	11.7	214.9	11.8	0.6	0.3
Commodity Tax	167.5	9.1	160.4	8.8	7.1	4.4
Customs Duties	115.3	6.2	114.3	6.3	1.0	0.9
2. Revenues from Surplus of Public Enterprise	224.0	12.1	238.3	13.1	-14.3	-6.0
3. Fees and Fines	93.7	5.1	79.0	4.3	14.7	18.5
4. Revenues from Public Properties	57.3	3.1	51.9	2.9	5.4	10.5
5. Revenues from Others	11.4	0.6	13.2	0.7	-1.8	-13.6

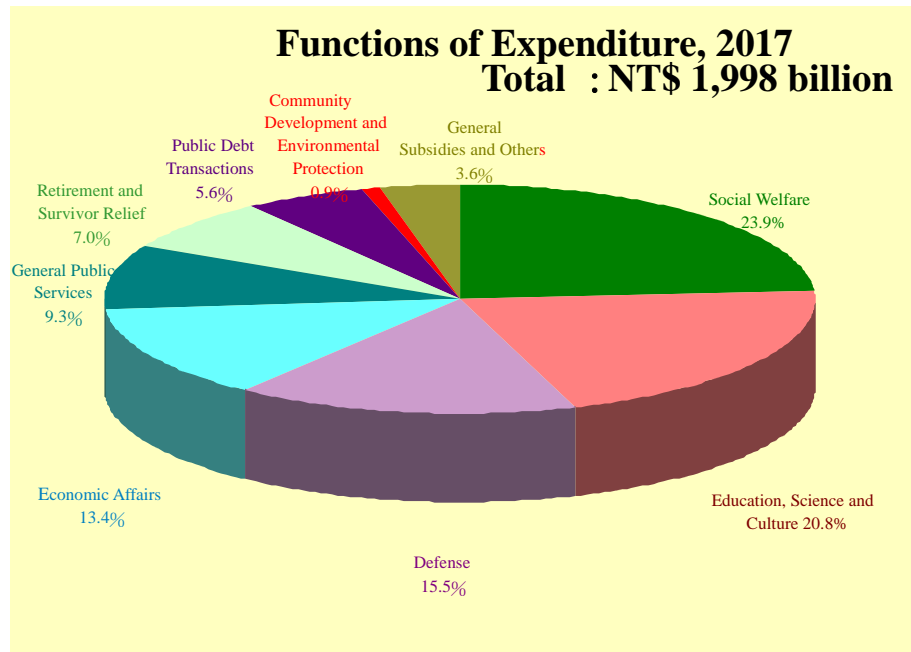
The revenue for 2017 is projected to be NT\$1,845.7 billion, NT\$23.3 billion (or 1.3%) higher than 2016, and is comprised of five major sources:

(1) Taxes. 79.1% of revenue comes from taxes, which goes up from NT\$ 1,440 billion in 2016 to NT\$1,459.3 billion in 2017, an increase of NT\$19.3 billion (or 1.3%). This increase is mainly from higher Income Taxes of NT\$9.2 billion, Commodity Tax of NT\$7.1 billion, Customs Duties of NT\$ 1 billion, and Business Tax of NT\$0.6 billion.

- (2) Revenues from Surplus of Public Enterprise.** 12.1% of revenue is contributed from SOEs, special funds and equity investments, which goes down from NT\$ 238.3 billion in 2016 to NT\$224 billion in 2017, a decrease of NT\$14.3 billion (or 6%). This decrease is mainly due to NT\$3.1 billion reduction of revenue from surplus of SOEs, such as Taiwan Financial Holdings and Land Bank, and NT\$11.5 billion decrease of revenue from National Development Fund, a result of declining shares released.
- (3) Fees and Fines.** 5.1% of revenue derives from fees and fines, which goes up from NT\$ 79 billion in 2016 to NT\$93.7 billion in 2017, an increase of NT\$14.7 billion (or 18.5%). This increase is mainly a result of the NT\$15 billion higher proceeds from auctions of broadband licenses for fourth generation mobile phones.
- (4) Revenues from Public Properties.** 3.1% of revenue stems from public properties, which goes up from NT\$ 51.9 billion in 2016 to NT\$57.3 billion in 2017, an increase of NT\$5.4 billion (or 10.5%). This increase is primarily because of NT\$11.5 billion increment of sales of shares, such as Mega Holdings and China Steel, and higher rental income from real estate of NT\$0.2 billion, offset by NT\$7 billion decrease of capital reduction of Housing Fund to the Treasury.
- (5) Revenues from Others.** 0.6% of revenue comes from others, which goes down from NT\$ 13.2 billion in 2016 to NT\$11.4 billion in 2017, a decrease of NT\$1.8 billion (or 13.6%). This decrease is mainly from the declining refunds of military equipment

purchases in prior years.

2. Expenditure



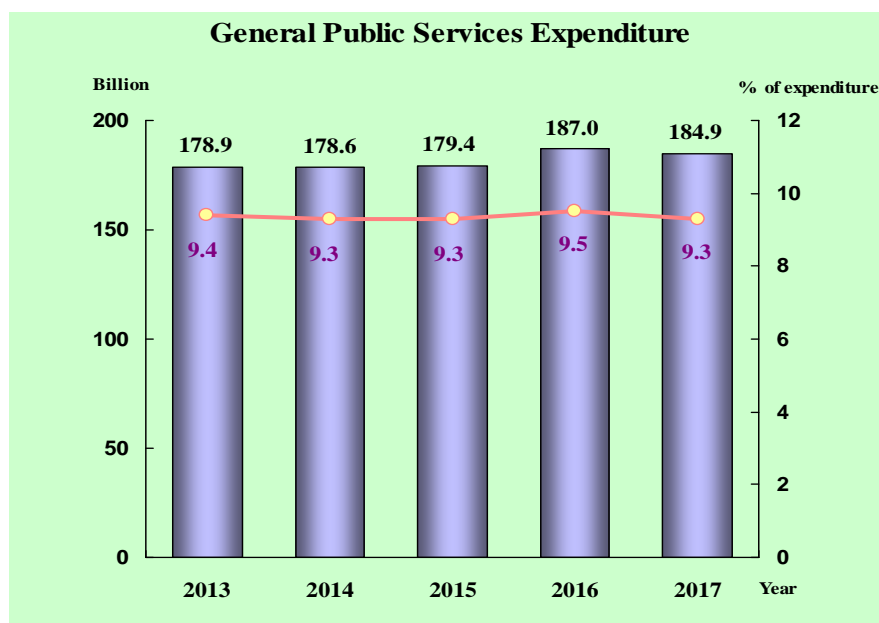
Composition and changes of Expenditure

NT\$ Billion

Item	2017		2016		Change	
	Amount (A)	%	Amount (B)	%	Amount (A-B)	%
Total	1,998.0	100.0	1,976.0	100.0	22.0	1.1
1.General Public Services	184.9	9.3	187.0	9.5	-2.1	-1.1
2.Defense	310.2	15.5	309.8	15.7	0.4	0.1
3.Education, Science and Culture	415.4	20.8	387.9	19.6	27.5	7.1
4.Economic Affairs	267.8	13.4	267.3	13.5	0.5	0.2
5.Social Welfare	477.3	23.9	460.6	23.3	16.7	3.6
6.Community Development and Environmental Protection	17.7	0.9	18.0	0.9	-0.3	-1.4
7.Retirement and Survivor Relief	140.5	7.0	147.2	7.5	-6.7	-4.6
8.Public Debt Transactions	112.4	5.6	123.3	6.2	-10.9	-8.8
9.General Subsidies and Others	71.8	3.6	74.9	3.8	-3.1	-4.0

The expenditure of 2017 is expected to be NT\$1,998 billion, NT\$22 billion (or 1.1%) higher than 2016. The composition and changes of expenditures by function are briefly presented as follows.

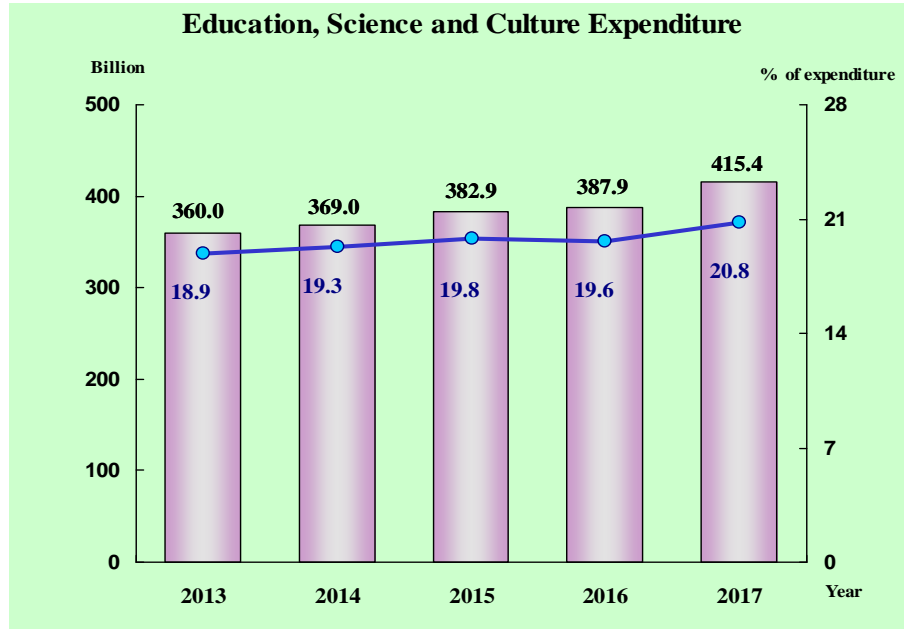
(1) General Public Services expenditure is expected to be NT\$184.9 billion (or 9.3% of the expenditure), NT\$2.1 billion (or 1.1%) lower than 2016.



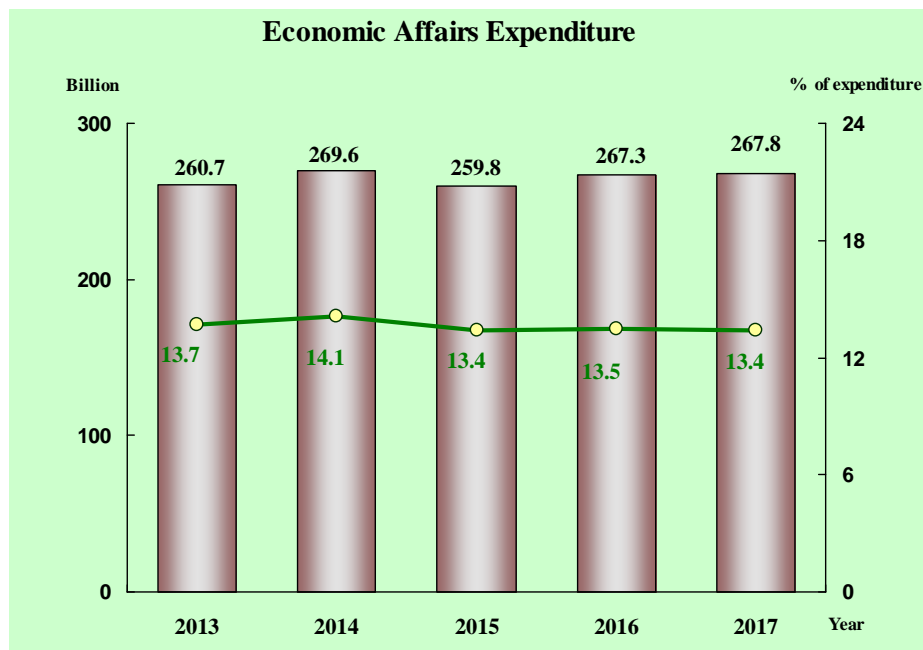
(2) Defense expenditure is expected to be NT\$310.2 billion (or 15.5% of the expenditure), NT\$0.4 billion (or 0.1%) higher than 2016.



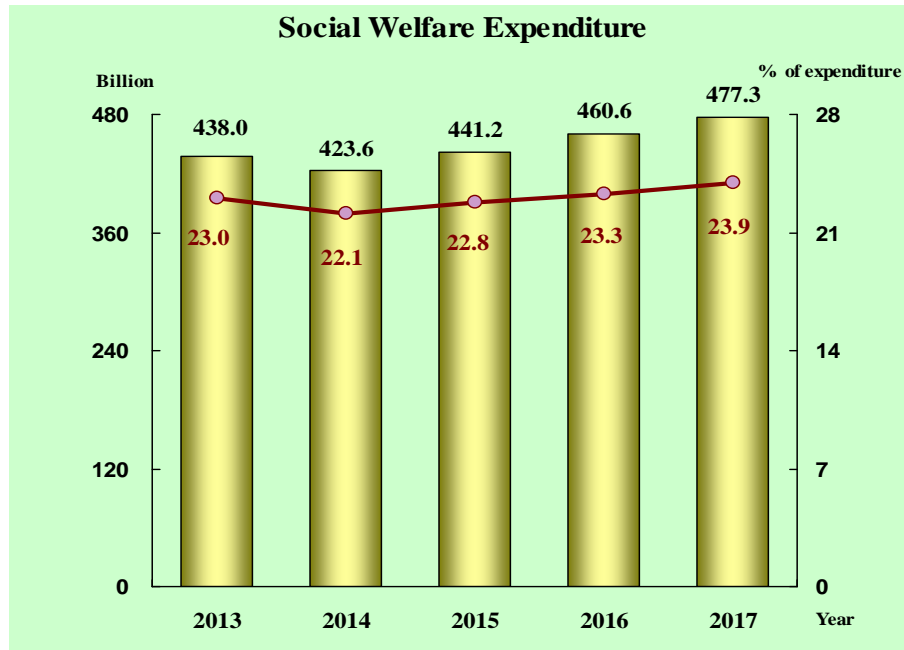
(3) Education, Science and Culture expenditure is expected to be NT\$415.4 billion (or 20.8% of the expenditure), NT\$27.5 billion (or 7.1%) higher than 2016.



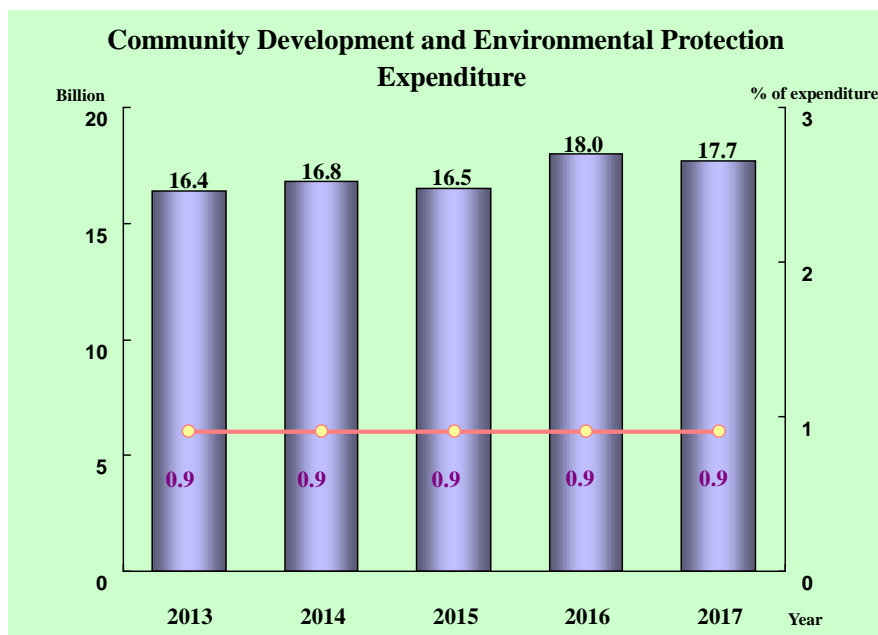
(4) Economic Affairs expenditure is expected to be NT\$267.8 billion (or 13.4% of the expenditure), NT\$0.5 billion (or 0.2%) higher than 2016.



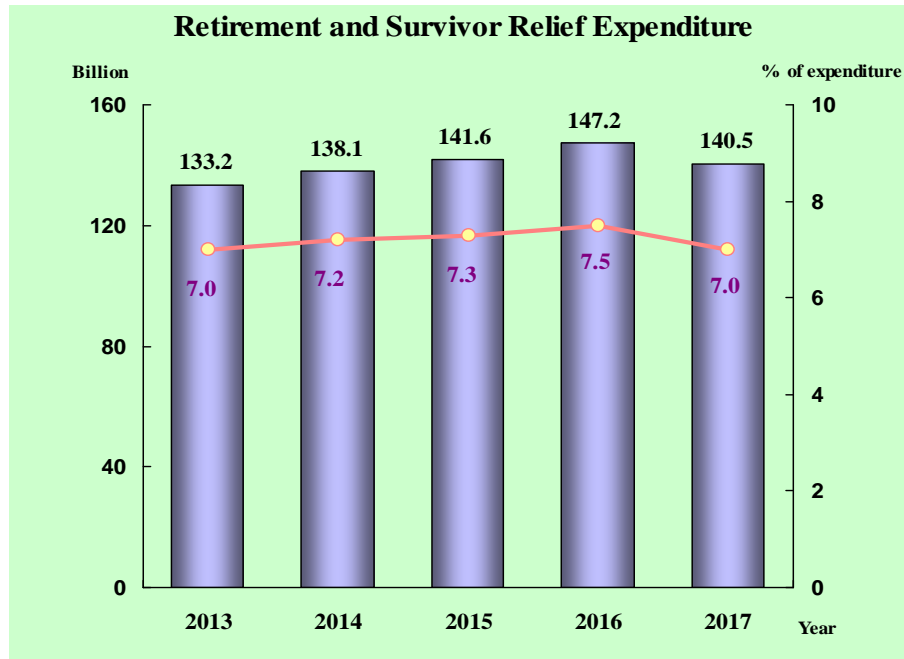
(5) Social Welfare expenditure is expected to be NT\$477.3 billion (or 23.9% of the expenditure), NT\$16.7 billion (or 3.6%) higher than 2016.



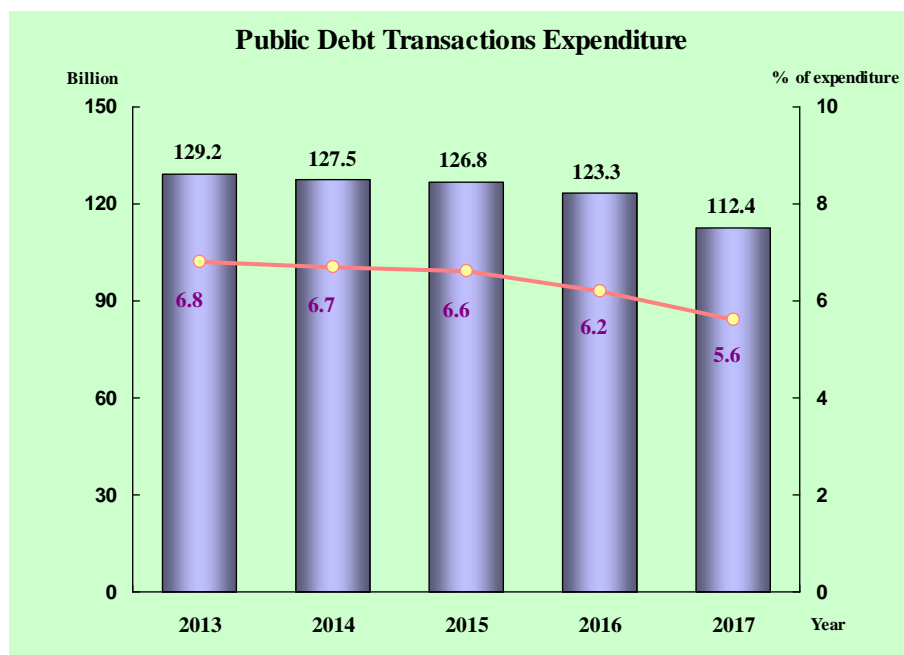
(6) Community Development and Environmental Protection expenditure is expected to be NT\$17.7 billion (or 0.9% of the expenditure), NT\$0.3 billion (or 1.4%) lower than 2016.



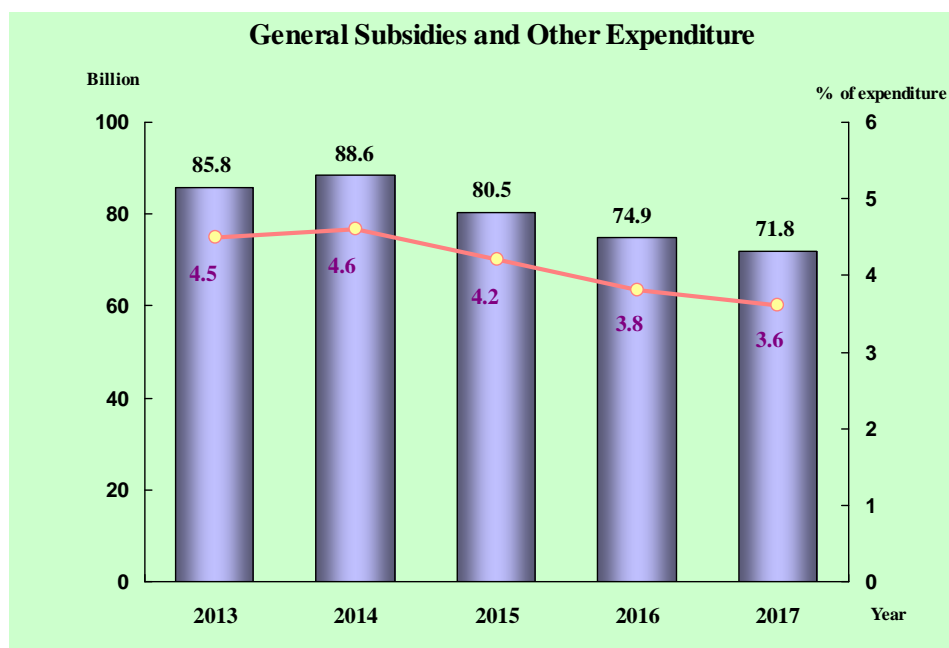
(7) Retirement and Survivor Relief expenditure is expected to be NT\$140.5 billion (or 7% of the expenditure), NT\$6.7 billion (or 4.6%) lower than 2016.



(8) Public Debt Transactions expenditure (principal repayments are excluded) is expected to be NT\$112.4 billion (or 5.6% of the expenditure), NT\$10.9 billion lower than 2016, mainly as a result of dropping interest rates.



(9) General Subsidies and Other expenditure is expected to be NT\$71.8 billion (or 3.6% of the expenditure), NT\$3.1 billion (or 4%) lower than 2016.



3. Financing Need

Composition and Changes of Financing Need

NT\$ Billion

Item	2017		2016		Change	
	Amount (A)	%	Amount (B)	%	Amount (A-B)	%
1. Deficit	152.3	67.3	153.6	67.8	-1.3	-0.8
2. Debt Repayment	74.0	32.7	73.0	32.2	1.0	1.4
3. Financing Need	226.3	100.0	226.6	100.0	-0.3	-0.1
(1) Bond Issuance and Borrowing	226.3	100.0	226.6	100.0	-0.3	-0.1
(2) Appropriation from Previous Year's Surplus	-	-	-	-	-	-

The balance of the 2017 Budget is expected to be a deficit of NT\$152.3 billion, NT\$1.3 billion (or 0.8%) lower than 2016. In addition, debt repayment is set at NT\$74 billion (or 5% of tax revenues). This is in compliance with Article 12 of

the Public Debt Act, which requires the central government allocate at least 5% of tax revenues for repayment of principal on debt. As a result, the financing need is expected to be NT\$226.3 billion and will all be covered through bond issuance and borrowing. It is equivalent to 11.3% of the expenditure, which is under the 15% loan cap regulated by Article 5 of the Public Debt Act.

At the end of 2015, the public debt incurred by the central government is NT\$5,301.2 billion. After taking into account the estimates of borrowings and debt repayments in the 2016 and 2017 Budgets, the central government debt outstanding is projected to be NT\$5,617 billion on December 31, 2017, which is 33.9% as a percentage of the 3-year-average GDP. It is below the 40.6% debt ceiling regulated by Article 5 of the Public Debt Act. As for the public debt incurred by local governments, NT\$833.5 billion has been accumulated at the end of 2015.

The statistics of the above-mentioned public debts is based on the definition of the Public Debt Act, which means the non-self-redeeming public debts with a maturity of 1 year or above incurred by governments through the general budgets, special budgets, and special funds other than SOEs or trust funds.

Meanwhile, for responding to the increasing concerns raised by items not included in the definition of the Public Debt Act but will lead to large amounts of public spending in the future or may incur significant financial obligations of government, the central government started to disclose and clarify these items, also known as future contingent obligations, in the Financial Statement from 2009 onwards. As of the end of June 2016, the actuarial present values of these future contingent obligations are estimated to be NT\$13,054 billion for the central government and NT\$4,538.3 billion for

the local governments, which total NT\$17,592.3 billion for all levels of government.

These future contingent obligations are either statutory spendings in the future, which should be provided for by annual budget for each corresponding year, or possible payments for underfunded social insurances, which could otherwise be compensated by premium adjustments or other pension reforms. They are distinct from the public debts raised to finance deficits, which are governed by the Public Debt Act.

Future Contingent Obligations

June 30, 2016

NT\$ Billion

Item	Total	Central Govern-ment	Local Govern-ment
Total	17,592.3	13,054	4,538.3
1.Unfunded Pension For Public Service (before 1995)	5,539.5	2,382.2	3,157.3
2.Public Service Pension Fund(after 1995)	2,329.5	1,003.6	1,325.9
3.Labor Insurance	8,928.3	8,928.3	-
4.Government Employee and School Staff Insurance	109	109	-
5.National Pension Insurance	469.2	469.2	-
6.Military Personnel Insurance	58.3	58.3	-
7.Farmer Health Insurance	103.4	103.4	-
8.Arrears incurred by local governments in the overdue health insurance premium and preferential deposit interest for retiree.	55.1	0	55.1

Highlights of the Budget :

1. Accelerating industrial upgrading and creating a new innovation-driven economy.

To drive industrial growth momentum, the government creates local, global and future links to make better use of the strength of local industries and establish innovative industry clusters throughout the country. The Budget provides NT\$46.2 billion to support innovative industries, including NT\$11.3 billion for Asia Silicon Valley, NT\$4.6 billion for smart machinery, NT\$5 billion for green energy, NT\$10.3 billion for biotech & pharmaceutical industry, NT\$1.6 billion for defense industry, NT\$5.8 billion for new agricultural industry, NT\$2.3 billion for high-value material industry zone (renamed as “economic recycling area”), and NT\$5.3 billion for other innovative industries.

2. Strengthening a social safety net and forging a new just society.

In response to the threats of low birthrate and aging population, the Budget provides NT\$13.8 billion for promoting long-term care services. After factoring in the spendings from nonprofit special funds, it comes to a total of NT\$17.8 billion, NT\$11.1 billion (or 167%) higher than 2016.

Given that food safety is crucial to the health of citizens, the government has adopted five major policies to build a food safety system from farm to table. The food safety spending is NT\$3.65 billion. After taking into account NT\$0.3 billion from nonprofit special funds, it totals NT\$3.95 billion, NT\$0.72 billion (or 22.4%) higher than 2016.

3. Improving infrastructure quality and facilitating regional balance

In order to improve infrastructure, ignite momentum of economic growth, and realize regional balance, the Budget

provides NT\$186.9 billion for infrastructure, NT\$5.7 billion (or 3.1%) higher than 2016. After taking into account NT\$15.7 billion from Special Budget of the Comprehensive River Basin Management Plan, it totals NT\$202.6 billion, NT\$7.3 billion (or 3.7%) higher than 2016.

4. Improving the quality of education and enhancing the industry-university-research cooperation

The key to Taiwan's success in driving the new economic model lies on the talents. The education expenditure of the Ministry of Education is set at NT\$ 235.3 billion in 2017. After factoring in NT\$ 50 billion of education block grants from the central government to local governments, it comes to a total of NT\$ 285.3 billion, NT\$ 18 billion (or 6.7%) higher than 2016.

Innovation is not only the core value to lead economic development, but also the key to reforms and upgrades of industries in Taiwan. The spending on technology programs is NT\$106.2 billion, the highest budget in history and NT\$4.1 billion higher than 2016. After factoring in NT\$7.7 billion of R&D expenditure of defense research expenditure and NT\$19.4 billion of SOEs and nonprofit special funds, it comes to a total of NT\$133.3 billion, NT\$5.5 billion (or 4.2%) higher than 2016.

5. Enriching cultural content, promoting ethnic equality

For encouraging the public to participate in cultural activities and promoting the cooperation with foreign countries through the power of culture, the Budget provides NT\$31.4 billion for culture, NT\$2.6 billion (or 8.8%) higher than 2016. After taking into account NT\$5.1 billion from National Cultural Institutions Operation Fund, National Institutions for Social Education Operation Fund, and Sports Development Fund, it totals NT\$36.5 billion, NT\$2.8 billion higher than 2016. The above-mentioned spending is beneficial for elevating the content and strength of culture.

To spread Hakka culture and enhance ethnic harmony, the budget of Hakka Affairs Council provides NT\$2.81 billion to consistently implement Hakka policies, NT\$0.26 billion (or 10.2%) higher than 2016. In order to start the Hakka renaissance and inject new life into Hakka communities, NT\$0.82 billion of above-mentioned spending is used to promote the “Romantic Provincial Highway 3” project to link cultural landmarks, ecology and local industries along the route.

For improving indigenous people’s socioeconomic status and promoting their quality of life, the Budget provides NT\$26.27 billion for indigenous people, NT\$3.85 billion (or 17.1%) higher than 2016. After factoring in NT\$3.65 billion of Indigenous People’s Development Fund, Employment Security Fund, and Agriculture Special Revenue Fund, it comes to a total of NT\$29.92 billion (net of NT\$2.04 billion of appropriation from the general fund to special funds.)

6. Bolstering national safety, creating new space for international and cross-strait relations

Maintaining the status quo will be the government’s core value for ensuring peaceful and stable cross-strait relations. Following the principles of transparency, public participation, and legislative monitoring, the government will spend NT\$2 billion on cross-strait interactions to consistently promote cross-strait economic and trade exchanges on a basis of equality and dignity.

While maintaining the cross-strait peace and stability, the government still needs to show self-defense determination. The budget of Ministry of National Defense is NT\$321.7 billion, NT\$1.6 billion (or 0.5%) higher than 2016.

Furthermore, in order to strengthen the mutual interactions with ASEAN and South Asia in various fields, the New Southbound Policy spending in 2017 is set at NT\$ 2.11 billion, including :

- (1) The Ministry of Education provides NT\$1 billion for professionals cultivation and technical training.
- (2) The Ministry of Foreign Affairs provides NT\$0.26 billion for mutual interactions and cooperations with ASEAN and South Asia.
- (3) The Ministry of Science and Technology provides NT\$0.28 billion for the bilateral cooperations in science and technology with Southeast Asia and participation in international organizations.
- (4) Overseas Community Affairs Council provides NT\$0.2 billion for overseas youth technical training classes.