

**Taiwan Mobile**  
**4Q16 Results Conference Call**  
**January 25, 2017**

**James Jeng, President:** Good afternoon. Before I start our presentation, I'd like to direct your attention to our disclaimer page, which states:

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For the business overview, I would like to highlight our growth areas.

**Mobile Growth Leading the Pack**

TWM's mobile growth led the pack in various metrics for the year of 2016. In terms of total subscribers, even though the mobile market remained competitive in 4Q, TWM still outperformed in terms of sustaining its mobile subscriber base.

The 4G service take-up rate reached 64% of the postpaid installed base and helped mobile postpaid ARPU grow by 2% YoY in 2016. As a result, TWM was the only one among the big three to report a positive YoY increase of 1.1% in mobile service revenue, on a like-for-like basis.

TWM also stood out in telecom EBITDA growth, aided by an industry-leading top-line growth and contained marketing spending.

**Online Shopping - A Bright Spot**

With a 22% YoY top-line growth, online shopping remained the brightest spot for momo. Online shopping business also posted a 17% revenue increase compared to a quarter ago, performing much better than its closest competitor in Taiwan.

For 4Q, momo's 21% YoY increase in EBITDA came not only from revenue growth in its online shopping business but also from its TV home shopping business turnaround in China.

Let me turn the presentation over to Rosie for the financial overview section.

## **Performance by Business**

**Rosie Yu, CFO & Spokesperson:** EBITDA increases in telecom business and momo were already elaborated on earlier by James.

On the cable front, drops in 4Q revenue and EBITDA were mainly due to the price competition from the new entrants in the Taipei County service area. However, we expect competition to subside by the end of 2017 given the new entrants' financial constraints.

Despite our CATV operations encountering headwind, we still managed to grow our consolidated EBITDA by 5% YoY in 4Q, supported by 5% growth in telecom EBITDA and 21% increase in momo's EBITDA.

## **Results Summary**

### **4Q16**

In spite of a sequential decrease resulting from a full-quarter impact associated with iPhone 7, 4Q16 EBITDA grew 5% compared to a year ago, credited to savings in handset subsidies and disciplined network opex and marketing expenses.

### **2016 Full-Year**

For full-year 2016, the respective 5% and 7% YoY increases in EBITDA and EBIT, both the highest among peers, reflected our better 4G spectrum investment and network deployment strategies. We also posted a healthy 6% increase in pre-tax income for the year. But the one-off corporate tax reversals in 2015 resulted in a 2% dip in 2016 EPS. That said, EPS for 2016 still came in at NT\$5.63 surpassing our 2016 target by 9%.

## **Balance Sheet Analysis**

Gross debt balance fell to NT\$56.52bn, following a NT\$4.25bn debt repayment made in the quarter. After being partially replaced by the 5-year NT\$10bn zero-coupon convertible bond issued in November of last year, short-term borrowings only accounted for 24% of gross debt from 45% a quarter ago.

The equity component (share option) of the convertible bond issued in 4Q16 increased TWM's capital surplus sequentially.

With short-term debt repayment made in 4Q16, current ratio went up while the ratios of net debt to equity and net debt to EBITDA both came off.

## **Cash Flow Analysis**

## 2016 Full-Year

Operating cash inflow increased 23% YoY with stronger cash earnings arising from fewer handset subsidies.

Investing cash outflow decreased from a year ago as both 4G network roll-out and spectrum purchases peaked in 2015, despite the receipt of NT\$0.5bn in proceeds from Taiwan High Speed Rail preferred share redemptions in that year.

NT\$4.8bn in total debt was paid down in 2016 aided by rising free cash flow.

In 2016, the ratio of total capex as a percentage of revenue dropped to 9% from 11% a year ago. Full-year FCF netted NT\$21.34bn, up 62% YoY, attributed to higher operating cash inflow and reduced 4G related spectrum and capex spending, translating into an annualized FCF yield of 6%.

Let me turn the presentation back to James for the 2017 Guidance and Event Update.

### **2017 Guidance**

#### **James:** *Telecom business*

TWM's mobile business will continue benefiting from rising 4G adoptions. Additionally, value-added services are estimated to grow by 13% and make up 8% of mobile service revenue in 2017. 4G rate plan and handset subsidy rationalization in an aim to raise 4G investment return will be the focus in 2017. As such, we expect a stable ex-roaming telecom EBITDA in 2017.

In view of APT's (Asia Pacific Telecom) plan to reduce its reliance on TWM's 3/4G networks in compliance with regulations, we anticipate a declining contribution from APT in 2017. We have also factored in a new initiation of the mobile termination rate cut to be implemented by the regulator into our 2017 forecast.

#### *Other businesses*

The combined EBITDA of the CATV, momo and other businesses will increase by 1% YoY in 2017 and represent 16% of our total EBITDA.

To sum up, EPS for 2017 is forecasted to come in at NT\$5.28, negatively affected by our projected declining roaming revenue from APT, primarily. Ex-roaming EPS in 2017, however, is projected to rise by 1% YoY.

## **Event Updates**

TWM's board approved a capex budget of NT\$8.5bn for 2017 with the breakdown details shown in the slide.

For 2017, telecom capex will be down by 17% YoY and that as a percentage of service revenue is forecasted to trend down to 9%. Regarding cable TV, investments in digital set-up-boxes will continue to achieve 100% installed base in 2017. momo's capex associated with the new logistic center is tapering off and will be completed this year.

The lower part lists the awards and recognition we've received in the fourth quarter of 2016 for your reference.

## **Key Message**

To wrap up our presentation, this slide summarizes the key message that we would like to deliver:

Our advantage in 4G spectrum and infrastructure investments delivered solid EBITDA growth in 2016. In 2017, we still expect to grow our free cash flow as we continue to invest for growth. Looking ahead, we're committed to sustaining the long-term health of our business so we can deliver above-market returns to our shareholders.

Now I would like to open the floor for the Q&A section.

## **Q & A**

**Varun Ahuja, Credit Suisse: *Can you comment on the mobile competitive dynamics? Your competitors have said the focus is moving to tiered pricing. So, just wanted to see what you're seeing in terms of competition. And how has been the take-up of the plans of NT\$1399 and above?***

***How much is the roaming contribution from APT? And will it completely go away in 2017 or will some still be left in 2017?***

***Regarding handset subsidies, given that analysts expect iPhone 8 is going to have a better demand than iPhone 7, so in your forecast, how did you factor that?***

***Can you comment on the mobile termination rate cuts? My understanding is that on voice, it has ended, but the government is proposing more MTR cuts in ADSL charges. Given that you made comment in your forecast that you're factoring in MTR cuts, so***

*just wanted to hear what's the latest status on that?*

**On spectrum auction, could you comment what is happening on that front and when should we expect that spectrum auction?**

**James:** In 2016, competition was very keen, especially with the Big 3 introducing the NT\$699 unlimited rate plan. I believe in 2017, this kind of cut-throat competition will come to an end. From TWM's standpoint, we would like to stop this as soon as possible.

**Rosie:** On the roaming contribution, it will not go away entirely. But we cannot comment more on that. I would like to share that ex-roaming telecom service revenue for 2017 is forecasted to grow by roughly 1%.

**James:** For the iPhone 8, we view it as a big seller in 4Q of this year. With the iPhone 7, we viewed it as a transitional product and, in fact, it didn't perform very well in 2016 in terms of the number of handsets we sold. In terms of subsidies, we expect it to reduce by 3% this year even if with the iPhone 8. That's mainly due to a significant drop in the mid- to low-end handset subsidies as we believe in 2017 the NT\$699 tariffs will be discontinued. However, given that the iPhone 8 is a high-end handset, the handset subsidies in terms of total amount will increase slightly in 4Q.

Mobile termination rate cut has not yet been officially announced by the NCC. However, we expect the NCC will announce fairly soon. We have already factored it in our 2017 forecast.

**Varun:** *Are you expecting the MTR cut in voice or somewhere else?*

**James:** Voice.

**Rosie:** It's expected to be down from NT\$1.15 to NT\$1.04. It could be a 4-year round cut to reduce it to NT\$0.70 per minute by 2020.

**Varun:** *On the adoption of the NT\$1399-and-above plans, how are you seeing from the ground given that a lot of 4G customers will be up for renewal this year? And its impact on financials?*

**James:** In 2016, the NT\$1399 unlimited rate plan performed quite well. In addition to bundling the plan with high-end handsets, we also bundled it with other electronic devices as substitutes. In 2016, in terms of retention and acquisition, close to 30% of those customers

chose NT\$1399. So, we are quite encouraged with this outcome.

**Jack Hsu, Sinopac:** *What is your subscriber target by the end of 2017? What is your strategy in the 2.1GHz spectrum auction?*

**James:** Our projection for the 4G penetration by the end of 2017 will reach 72% for postpaid.

Our strategy for 2.1GHz spectrum auction is that we will go for this spectrum since our 3G services is located there.

**Jack:** *Do you have details about the 2.1GHz spectrum auction regarding when the government will start the bidding?*

**James:** Right now, there is no official announcement yet, but we believe it will be during the 3Q of this year.

**Neale Anderson, HSBC:** *On the cable business, you mentioned higher competition from some of the new entrants in the Taipei area. How long do you expect that to continue for? And, in terms of the impact on margins, do you expect margins in the cable business to return to mid-50s, 53, 54, where it's been in previous years, or do you expect them to come down as a result of that new competition?*

**James:** For the past two years, ever since the government opened up the franchise areas, the competition from the new entrant has been quite keen. Most of the pricing in cable TV has been irrational. And that did affect our cable TV margins a little bit. However, the affected area is only limited to our one SO in the Taipei county area. While the impact in that area was severe, for Taiwan Mobile as a whole, it isn't that significant. But, as Rosie mentioned earlier, we believe this type of competition will end this year, maybe as early as 1Q or 2Q, because we have discovered those new entrants are facing some financial difficulties. We've noticed that, since December of last year, there has been a significant reduction in their marketing activities.

**Neale:** *Regarding the guidance for the other businesses on page 6 of the management report, combined EBITDA for CATV, momo and other businesses is guided to increase by 1% YoY. That reflects a rather cautious forecast for momo given that momo had a good 4Q, thus I was a little surprised it was just 1% for those combined businesses.*

**Rosie:** Yes, it is a very conservative estimate based on our experience.

**James:** Yes, in fact, this also came up this morning in our Board meeting, but, again, the management team promises it will deliver a much better result than this.

**Neale:** *Regarding the 2.1GHz auction, it seems like you were vindicated for not bidding for the 2.5GHz and 2.6GHz. Any thoughts on what the competition will be like for the 2.1GHz auction? Previously, operators bid for spectrum that was owned by other companies and it didn't work out so well. Do you think it's more likely the companies will bid to renew their current spectrum?*

**James:** It's really hard to say. Currently, there are four operators that offer 3G service on the 2.1GHz spectrum, the Big 3 and Taiwan Star. But APT is quite interested in this spectrum because, like Taiwan Mobile, they did not bid for 2.6GHz FDD. So, it's hard to say, but what I know for sure is Taiwan Mobile will definitely bid on it.

**Rosie:** It also has something to do with the financial condition of each company. For the smaller companies, even though they may want to be disruptive in the bidding process, but given the auction rules we have seen, it will be very risky for them to be too aggressive. So, we don't think it will be as aggressive as before. But let's see how the government will set the rules.

**James:** For the 2.1GHz auction, the government is going to change the rules. They are going to divide the spectrum into small pieces, 5MHz as one unit. So, it will require a different strategy.

**Jack Hsu:** *Will you issue the CB in 1Q17?*

**Rosie:** It's already listed.

**Jack:** *Will the dividend policy be the same as 2016?*

**Rosie:** As you know, we are always very committal to a stable dividend policy. It will be decided in April this year. We expect it to be stable.

**Varun:** *Your FCF has been increasing and if you look at your dividends, they have been stuck at NT\$5.6 for the last 3 years. Should we expect to see some increase in dividend payouts given that the FCF has been very strong?*

**Rosie:** Well, the potential is always there, but it's still up to the Board to decide. Sorry, I can't give you any clarity on this.

**Jack Hsu:** *What is the EBITDA margin trend in 2017 given that you will join the 2.1GHz spectrum auction and that you will try to increase your 4G subscribers?*

**Rosie:** The EBITDA margin is trending downwards, as we mentioned earlier, because of two factors. One is less roaming revenue from APT and the other is we have already factored in the next round of mobile termination rate cuts. But if we look at the ex-roaming telecom EBITDA, it will still remain stable.