

Taiwan Mobile
2Q20 Results Conference Call
August 4, 2020

Jamie Lin, President: Good afternoon. Welcome to Taiwan Mobile's second quarter 2020 investor conference call. Before I start our presentation, I would like to direct your attention to our disclaimer page, which states:

The information contained in this presentation, including all forward-looking information, is subject to change without notice, whether as a result of new information, future events or otherwise, and Taiwan Mobile Co., Ltd. (the "Company") undertakes no obligation to update or revise the information contained in this presentation. No representation or warranty, either expressed or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein, nor is the information intended to be a complete statement of the Company, markets or developments referred to in this presentation.

Next let's turn to business overview. I would like to start with Operational Highlights for the second quarter.

2Q20 Operational Highlights

During the quarter, the telecom industry as a whole faced slight headwinds due to the lack of new premium phones being introduced to the market, customers' anticipation for more 5G phones to be unveiled, and to a lesser extent, impact on international roaming revenue caused by COVID travel restrictions.

On the other hand, our 5G infrastructure build-out continued smoothly and, as a result, we were one of the first Taiwanese carriers to launch commercial 5G services successfully, at midnight on July the first. I want to take a moment to thank all of our telecom business team members. They worked relentlessly and cohesively for months to make it happen. Kudos to all of them.

As for momo, it once again delivered a stellar quarter, as online shopping continued to thrive in this new normal.

Overall, our net income arrived 4% ahead of our second quarter guidance. On a pre-IFRS basis, net income remained flat YoY in the quarter. It's also worth mentioning that operating cash flow stabilized as well.

Let's turn to page 5 for a closer look at our telecom business.

Versatility in Telecom Business

In the second quarter, our Double Play, or in Chinese 好速成雙, mobile plus home broadband bundle continued to gain traction, providing healthy lift to our ARPU mix.

On the enterprise side, demand for IoT connectivity remained solid, yielding 40% YoY increase in the quarter.

The enterprise fixed services, which accounted for close to 10% of our telecom service revenue, posted a healthy 6% YoY growth. At the same time, cloud, ICT and IoT revenues grew by 35% YoY.

Let's turn to page 6 for an update on our cable TV business.

Resilience in Pay-TV Business

During the second quarter, we continued to fare better than our MSO peers in terms of decline in basic TV subscriptions and higher broadband & DTV penetration. As customers demand faster broadband speeds, the percentage of our subscribers using 100Mbps and higher plans grew by 6ppts from a year ago.

On the financial side, with 33% YoY decline in D&A, EBIT posted a 7% YoY increase in the second quarter.

Last but not least, let's take a look at our growth engine, momo, on page 7.

momo – the Growth Engine

Despite a traditionally slower second quarter, momo's e-commerce business continued to outgrow its peers and delivered strong results. Not only did the total number of transactions jump by close to 40% YoY, average ticket size also edged higher, with its private label credit card serving as a tailwind.

On the logistics side, momo further added two satellite warehouses in the second quarter, taking its total number of satellite warehouses to 17, which is 9 more than a year ago. Coupled with its build-out of in-house delivery fleet, momo continues to cut short delivery time and that in turn helps momo further widen its moat.

At the same time, thanks to increasing scale and operating leverage, momo's e-commerce

EBIT surged by 57% YoY in the second quarter.

Now let me turn the presentation over to Rosie for Financial Overview.

Performance by Business

Rosie Yu, CFO & Spokesperson: Hi, good afternoon. Let's start with Performance by Business on page 9.

In the 2nd quarter of 2020, our consolidated revenue once again grew on a YoY basis, mainly driven by momo, which accounted for more than half of the Company's consolidated revenue for the first time. Telecom revenue and EBIT, on the other hand, recorded steeper YoY declines than the previous quarter, mainly due to soft handset bundle sales.

While CATV EBITDA declined YoY in 2Q, mainly attributable to competition in basic TV business, its EBIT rose by 7% YoY, which was a function of the falling depreciation of set-top boxes.

Let us move to Results Summary on page 10.

Results Summary

In 2Q20, the 16% YoY increase in the combined operating income of CATV and momo helped mitigate the slide in telecom operating income. If we strip out the IFRS bundle sales adjustment swing factor, 2Q20 net income remained stable YoY.

In 1H20, while total revenue was slightly behind, the muted telecom performance was offset by lower selling expenses and momo's operating leverage at the operating income level. Overall, operating income for all major businesses achieved management expectations in 1H20.

Non-operating expenses tracked well below expectations, on account of higher-than-expected equity income, disposal gains realized by momo, and lower-than-expected financing costs.

Let's move to Balance Sheet Analysis on page 11.

Balance Sheet Analysis

On the asset side, the YoY surge in concession resulted from the acquisition of 5G spectrum in 1Q20 and has begun amortization since the commercial launch on July 1st, 2020.

On the liability front, gross debt dropped to 62bn NTD at the end of 2Q, following 5bn NTD repayment of short-term borrowings. Net debt to EBITDA also declined sequentially to 1.68x in 2Q.

As for shareholders' equity, the QoQ decline in 2Q was a result of AGM's approval to pay dividends.

Lastly let's look at Cash Flow Analysis on page 12.

Cash Flow Analysis

In 2Q20, the YoY increase in operating cash flow was a result of momo's rising payables. On a sequential basis, operating cash flow fell as we paid 2019 corporate taxes in 2Q.

As for investing cash outflow, apart from capex, the main activity in 2Q was the sale of Taiwan High Speed Rail shares. 75mn shares remain to be disposed of as of end of 2Q.

On the financing front, net cash outflows mainly came from debt repayment and cash dividend payments to momo's minority shareholders in 2Q.

The rise in cash capex was due to the expansion of momo's logistic capabilities. 2Q20 free cash flow calculated with pre-IFRS 16 operating cash flow reached 4.6bn NTD, translating into an annualized free cash flow yield of 5.9%.

Let me turn the presentation back to Jamie for Event Updates and Key Message.

Events, Awards, and Recognition

Jamie: Let's turn to page 14. As mentioned earlier, Taiwan Mobile launched commercial 5G services on July 1st. This page also summarizes the awards and recognitions we received during the quarter, for your reference.

Key Message

Finally, to wrap up our presentation, here is the key message we would like for you to take away:

Taiwan's big 3 mobile operators have entered the new era with restrained pricing and a consensus on 5G unlimited data plans starting from NT\$1,399 a month. As 5G iPhone and the likes arrive alongside continuous network build-out, we expect 5G service adoptions to

accelerate, and hence, increase bundle sales of high-end phones for our telecom business. At the same time, we expect momo to continue to thrive in this new normal and its investments into logistics should give it increasing advantage over its peers.

With that, I would open the floor up for Q&A session

Q&A

Neale Anderson, HSBC: *Just a question on momo, if I may. You mentioned cash capex is up because of investment in distribution on fulfillment. Can you give more color and comments about how that might look over the next couple of years, given the demand you're seeing at the moment? Anything else on the competitive environment relating to momo?*

Rosie: Cash capex for momo is there already. They expect to have greater plans for logistics expansion down the road so cash capex may be increasing for momo.

Jamie: In terms of competitive landscape, like we expressed during our presentation, we think momo in a virtuous circle right now. As they invest into shortening their delivery time and their logistics network, it's going to lend to their competitive advantage over peers so we continue to see momo performing better than the sector as a whole.

Neale: Got it. On the investment in the capex, would you characterize that as fairly lumpy; big investments in distribution and fulfillment centers and then a period of stability? Or is it more like a stable capital intensity relating to this part of the business?

Rosie: Currently, we wouldn't be able to comment because they have their plans and when they have a more concrete plan, they will bring it up to the Board for approval. Our guidance reflects what they have for this year.

Jamie: For the longer term, I think we expect momo to continue to invest into logistics because that will continue to provide them with long-term competitive advantage over their peers.

Amber Lee, Yuanta Securities: *2 questions here. Your peers shared with us their current 5G adoption progress and their targets for 5G penetration. Just wondering if Taiwan*

Mobile has similar information to share with us. Secondly, I also want an update on your capex outlook for the mobile business for the coming years.

Jamie: In terms of 5G adoption progress, I think it's still early in the game so we prefer to address the question somewhere down the road. In terms of our target, we have expressed that we aim to convert more than half of our subscriber base to 5G over a window of 3 years.

Rosie: For capex for the coming years, we will share that with you after the first Board meeting every year. Currently, I think we'll just stick to our guidance.

Jack Hsu, SinoPac Securities: ***My first question is about your Double Play strategy. What is the impact on your revenue? We also see your competitors adopting a similar strategy. What's your view on their strategy?***

Jamie: Double Play, like we said, has been providing a healthy tailwind to our ARPU mix. We're very happy to see other telecom companies trying to offer similar programs; I think it's going to be good for us and our peers, and the industry as a whole. We have no problem with our peers trying to put together similar programs.

Jack: When they try to do similar strategies, will these have a negative impact on TWM?

Jamie: Right now, if you look at the industry as a whole, churn rate is at a historical low for everybody. I think for most of us, it's mainly how we serve our existing customer base better and offer them products they want so that we can increase our ARPU. Our Double Play is mostly for existing customers. If Chunghwa or FET would like to offer similar programs to their existing customers, we're totally happy to see that. We'd like to have an industry that's growing and strong and vibrant. So that's good for everybody.

Jack: Okay. My second question, could you give us some color on your 5G base station development plan? Chunghwa says they will try to deploy almost 4,000 5G base stations by end of 2020. What's the target for TWM?

Jamie: Right now, the big three all have similar plans for the rest of the year. I think most of the numbers have been published so we have nothing more to add on that front.

Jack: One follow up question. Handset sales were very low in the first half of 2020. Will handset sales recover in the second half or will the recovery happen in 2021?

Jamie: Like we said in our takeaway, we see it going through a process of accelerating as more appealing 5G phones are introduced to the market. It's not going to be an overnight thing but we do expect things to heat up over time.

James Wang, UBS: *I just want to get a bit more detail about the Double Play strategy. Can I get an understanding of what proportion of your customers are currently on the Double Play and what the margin is for the Double Play business? Is it a higher margin compared to the existing business? Also, what is the churn rate for Double Play customers versus a single product customer? How does that translate to potential savings on sales and marketing?*

Jamie: Right now we're still in the early phase of introducing Double Play to the market so we prefer not to talk about the percentage of our customer base that's on the plan. In terms of the ARPU it generates, like we said, it's providing healthy tailwind to the ARPU mix. I would say it's accretive to the margin overall.

James: Do you have any data on churn rates for Double Play customers versus regular customers?

Jamie: We have only been offering this product for a little bit over a year. Most of the contracts are 24 months or longer so it's still too early to talk about the churn rate.

Billy Lee, Crédit Suisse AG: Any news you can share with us regarding any collaboration with the smaller players?

Jamie: As of now, we have nothing to share. When we have any exciting news, you can be sure you'll hear about us on the media.

Jack Hsu, SinoPac Securities: *I have another question: we have seen your financial results in the first half. Will you change your forecast for 2020?*

Jamie: We have no plans to change anything as of now. Right now, the plan is to stick to our guidance.

Kaz, Fidelity: *I have two questions. The first one is, could you give me a little more clarity about the IFRS 15 bundle adjustment? I know that pushed down your accounting earnings right? So I guess it doesn't affect the cash flow at all. Could you give me more clarity about what happened over there? Second question, how do you see the competitive environment for 5G? Given the fact that Taiwan Star is pushing NT\$699 plans, which is about 50% discount to big three's pricing, how do you see the competitive environment in the 5G era?*

Rosie: On the IFRS 15, as the handset sales decline, the adjusted increments in our overall revenue will also go down. So that's the impact.

Kaz: Okay. Just to make sure, on a cash basis, are you guys making profit from handset sales or are you making a net loss?

Rosie: On a cash basis, during the contract period, I think we are still making a profit.

Kaz: If you include monthly tariff you have to be making profit, right? But if we only look at your handset sales, are you making profit? When you sell one handset, are you making profit or are you making loss?

Rosie: Are you talking about bundled sales or just handset sales?

Kaz: About the bundle plan.

Rosie: No, not at the beginning. During the contract period, we are making a profit out of the service.

Kaz: So under IFRS 15, when you sell handsets under a bundle plan, you initially book a loss in P&L, and then later, you make profit from monthly tariffs?

Rosie: No.

Jamie: You amortize. So essentially, we subsidize handsets in the bundle sale situation and the subsidy will be amortized over the length of the contract under IFRS 15.

Kaz: Your competitors are conducting the same accounting standard, yet you are the only one who actually booked an accounting profit decline in the second quarter. It looks like it's because of the IFRS 15 bundle adjustment, as stated at the very top of your management

report. So I'd like to better understand what's really going on.

Rosie: Well, I think FET also experienced a decline in revenues during the second quarter and we also suffered from fewer handsets sold during the period.

Kaz: Okay. So overall, when you sell handsets on a stand-alone basis, you are making profit? Then because of COVID-19, handset sales overall declined a lot, therefore, that had a negative impact on your earnings?

Rosie: Because we are entering the 5G era, most of the subscribers are probably sidelined to wait for the launch of 5G and waiting for 5G handsets to be put on the market. So the overall handsets sold in the first half declined a lot.

Kaz: And did that negatively or positively impact your P&L?

Rosie: Negatively.

Jamie: In terms of 5G competitive environment, we see the big three being able to offer high-quality, wide coverage, good reception 5G networks. In terms of smaller players, if they don't engage in network sharing with the bigger players, we do not expect them to be able to offer the same network quality, in the short-run, without a lot of fundraising. Because of the quality difference, they would have to price the service differently and they would have to convince the market that a partial 5G service is what they want. There may be a percentage of the market that would want a service from that type of network but we see the vast majority of users to prefer a high-quality 5G network, which the big three are offering. The big three, like we said, have come to a very restrained consensus on pricing. That's what the competitive landscape is right now. Of course, nobody knows how it's going to turn out to be a few months from now, so we'll continue to navigate methodically and carefully.

Jack Hsu, SinoPac Securities: *My question is about cable TV. We see that it grew steadily QoQ and YoY. Could you give us some color on the cable TV business for the second half of the year?*

Jamie: We traditionally don't give our guidance on a specific subsidiary or business unit so I don't think there's much we can say about the outlook of the cable business in the second half of 2020.

Jack: Will the cable TV business grow in the second half of 2020?

Jamie: There are a few factors. For example, there's always a risk of new entrants into the marketplace. Another factor would be our ability to sign up more customers, especially in terms of broadband and DTV penetration. Our Double Play product is actually providing a tailwind to that. It's hard to gauge what the end result will be for the second half of 2020, so you'll have to wait for our next conference call to hear how things turn out in this quarter.

Jack: I see. About the Double Play strategy, they will combine mobile phone and cable TV so the Double Play synergy is a very good development. Does that also mean cable TV revenue will also grow in the future?

Jamie: We see the Double Play as a win-win situation for both our mobile business and our cable business. For our mobile business, in terms of 5G, we all know that indoor coverage is more challenging, so the ability to bundle home broadband helps the mobile business provide seamless coverage at home for our customers. On the other hand, our cable TV business is also looking to grow its broadband penetration. Therefore, we see Double Play as a product that provides a win-win for both of our businesses.