

Taiwan Mobile
3Q17 Results Conference Call
November 3, 2017

James Jeng, President: Good afternoon. Welcome to Taiwan Mobile's third quarter investor conference call. 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 will start with the mobile operating performance.

Telecom Business – Out from the Pack

Overall, our telecom business in 3Q still stood out of the pack. If we exclude domestic roaming business, our mobile service revenue would have dropped by 4% YoY in Q3. Focusing on product differentiation and value added services led to a QoQ postpaid ARPU recovery.

In Q3, our good spectrum investment strategy let us achieve spectrum yield of NTD156 million per Mega Hertz, which continued to outperform our peers.

On a recurring basis excluding domestic roaming, our telecom EBITDA improved by 2% YoY, thanks to our ongoing cost-control efforts. Our telecom EBIT continued to expand at a robust 6% YoY growth, aided by the 3% YoY decline of telecom D&A on back of our better CAPEX strategy.

In addition, our Q3 EPS also still stayed at a high level, beating our guidance by 6 %.

CATV – Sequential Improvement

On the cable TV business:

The industry dynamics in New Taipei City has become more favorable.

This September, we launched a Sharp TV bundle plan. This bundle plan has differentiated us

from our competitors, and benefited our subscriber growth and blended ARPU for cable TV. As such, this quarter, we post our first quarterly revenue growth for the past 5 quarters since Q3 2016. On a sequential basis, CATV revenue also went up 2% QoQ .

momo E-commerce - Stellar Growth

For momo, the company continued gaining ground in B2C, e-commerce business.

In Q3, e-commerce revenue reported a 31% YoY growth and EBITDA also enjoyed a strong 37% growth, compared to the same period last year.

Of note, e-commerce already made up 81% of momo's Q3 revenue, and continued to serve as the company's growth engine.

Also, we are encouraged to see the mobile commerce contribution increased to 52% of total e-commerce revenue this quarter. There is a growing trend of consumers increasingly shopping on mobile sites or through mobile APPs. Hence, the increasing contribution from mobile commerce bodes well for our future e-commerce growth.

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

Performance by Business

Rosie Yu, CFO & Spokesperson:

We believe that the recurring numbers excluding the domestic roaming business better reflect our performance in 3Q.

In the quarter, our consolidated EBITDA increased by 1% YoY, of which telecom EBITDA went up 2% YoY while momo's EBITDA jumped 6%, on a recurring basis.

Results Summary

In 3Q17, mobile device sales, telecom service revenue, CATV revenue, and momo revenue all trended up from the previous quarter.

Owing to a QoQ rise in revenue, our operating costs and expenses went up sequentially this quarter. Amortization costs edged up from 2Q as we gained access to an incremental spectrum on the 1.8GHz frequency band.

At the non-operating level, non-operating expense increased QoQ as we incurred 2G asset write-off losses after the end of 2G service in 3Q17.

Net net, on the back of the sequentially improving business momentum and one-off investment tax credits, 3Q EPS rose 4% from a quarter ago. Compared to our guidance, our net income in 3Q beat expectation by 6%, with cost savings more than offsetting revenue shortfalls.

Year to September, accumulated EPS stayed resilient from a year ago and reached 82% of our full-year target.

Balance Sheet Analysis

Now let's move on to balance sheet analysis.

On the asset front, major YoY changes seen in 3Q included PP&E and concession reductions. PP&E continued decreasing as new additions in 4G equipment were smaller than the overall depreciation incurred for the quarter. Concession was amortized over the period.

On the liability front, our current liabilities decreased from 2Q due to the payment of \$NT15.24bn in cash dividends in 3Q17, leading to a QoQ rise in current ratio.

Net debt to EBITDA increased sequentially in the quarter because of raising cash to pay dividends through bank borrowings. However, the ratio in 3Q17 was lower than last year's level.

ROE at the end of 3Q remained at a high of 28%.

Cash Flow Analysis

3Q17 operating cash inflow decreased YoY mainly due to lower roaming revenue from the domestic roaming business in the quarter which also resulted in a mobile capex reduction. Meanwhile, the QoQ decrease in operating cash inflow was caused by changes in accounts receivable and accounts payable, which led to a decrease in net working capital.

Investing cash outflow increased QoQ as we provided a NT\$1bn deposit to the NCC for participating in the upcoming spectrum auction while capex remained well-contained in the quarter.

On the financing front, a total of NT11.7bn in short-term borrowings was raised in the quarter to fund the NT\$15.24bn cash dividend payments.

For the first three quarters, FCF netted NT\$14.78bn, translating into an annualized FCF yield of 7%.

Let me turn the presentation back to James for the event updates..

Event Updates

Let me brief you on the important events of this quarter.

First, we would like to highlight that:

Following Taiwan Mobile's termination of its 4G heterogeneous network service for 2G users at the end of August, TWM has expanded its LTE 1800MHz spectrum to a contiguous 15MHz. Accordingly, 4G network download speed rose sequentially.

Second, the first stage of the LTE 1800/2100 MHz spectrum auction starting October 31 has just finished, with TWM gaining 4 blocks in the 2100 frequency band at a reasonable cost of NT\$8.6bn. Compared to the NT\$10.3bn we paid in 2002 for 15MHz on the same spectrum for 3G, that's a savings of 37% per 5MHz.

For other events, please refer the slide for details.

Next, let's move to the Awards and Recognition page.

Awards and Recognitions

This page lists the awards and recognition we've received in the third quarter of 2017 for your reference.

Key Message

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

The end of 2G service and the expected rational pricing of the government's licensing of the 1.8/2.1GHz spectrum will alleviate pressure on our depreciation. A more benign cable industry outlook coupled with the potential revenue acceleration aided by the completion of momo's automated distribution center is expected to continue bolstering our profit growth.

Free cash flow stability and exploring service/product differentiations remains our main areas of focus. The new bundled iPhone8/X offerings with the monthly fee adjusting upward to a minimum of NT\$1,399 for unlimited data usage should bode well for healthy industry growth.

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

Q & A

Peter Milliken, Deutsche Bank HK: *Two questions. First, year to date, you've done better than you expected in profitability with operating expenses, in particular, being below where you expected them. Now, this presumably is due to handset costs coming in low this year. Can you give us some details on why they have come in so lower than you expected? And can this continue?*

Secondly, on the spectrum auction, any thoughts as why two of the blocks went unsold when the pricing was about a third lower than in 2005?

James: In response to your first question. For telco, the main expense is in the handset subsidy and channel commission. And this year because the unlimited rate went from NT\$1399 to NT\$699, we decided to significantly reduce the handset subsidy and channel commission. That's the main reason. In addition to that, another factor is our internal control of expenses.

Regarding auction outcome, the results met my expectation. As I mentioned before, as an operator, we focus more on spectrum efficiency instead of spectrum quantity. As you can see on slide 4, Taiwan Mobile has a very sound spectrum strategy with spectrum cost efficiency much better than our peers. I believe our peers also noticed that and since top-line growth has become more and more difficult and in order to keep the bottom line at a healthy level, not only does there need to be expense and cost control, but D&A needs to be maintained at a certain level. Thus, I believe that's the main reason why this auction has become more sensible. Actually, it really met my expectation.

In terms of the 1800 band, there are two blocks that didn't receive any bids. And that's a little surprising to me. APT decided to drop out of the auction. In my original planning, they were the company I thought would be interested in bidding for those blocks. But they decided to drop out and, thus, that's why those two blocks remain unsold.

Ronny Zhu, UBS Shanghai: *I have two questions. The first is related to the auction, but I think Peter already asked it. My second question is regarding the cable TV business. We've noticed that the competitive landscape in Taipei has become more and more favorable. I was wondering why our EBITDA margin declined?*

James: There are two reasons. EBITDA comes from two major products, cable TV and fixed broadband. Due to competition from the new entrants in cable TV, the monthly tariff in some areas besides Taipei City slightly dropped to gain market share. In fixed broadband, the competition with CHT has been quite keen. Also, CHT, due to the NCC tariff cut for the circuit to lower their tariff for the ADSL and in response to that, we had to lower our fixed broadband and cable modem. And this probably reduced some of our EBITDA margin.

Another factor is the channel leasing to the TV shopping. Since TV shopping has been impacted by the internet business, more and more TV shopping companies have dropped out of this market and that has directly affected some of the channel licensing revenue.

Ronny: *Regarding the spectrum auction, there are two rounds and the results have already come out for the first round. Do we expect the second round to be just as rational as the first?*

James: The second round for the positioning of the spectrum. And from my understanding right now, it seems everyone has gotten some blocks overlapped with their existing ones. So, I don't expect there will be a second round auction.

Neale Anderson, HSBC HK: *Regarding the roaming revenue from APT, is there any more revenue decline that we should expect from that? What's the status going into next year?*

James: The drop in domestic roaming revenue was reflected in our budget projection from the beginning of the year and basically it has met our projection. And, as for next year, we will see, but I think 70% of the traffic has already moved back to APT's own network. Thus, 30% of the data traffic is still with TWM and I expect it will remain there until the end of next year.

Neale: *So, there's no further requirement from the NCC that they move that traffic back to their network? They've already met their obligation, have they?*

James: I think APT needs certain roaming for their customers because their 4G coverage is not as good as TWM's. So, when their customers move out of APT's coverage, they will be automatically switched onto TWM's network. And that's why there is still 20%-30% traffic that remains at TWM's network.

Rosie: According to the NCC, by the end of next year, they will have to move all of their traffic back to their network.

Gary Yu, Morgan Stanley HK: *Two questions. One is for your CAPEX outlook. How should we look at your capex from next year onwards given that you've recently won some new spectrum?*

Secondly, with improving cash flow and EBITDA and lower-than-expected spectrum cost, how should we look at your dividend upside going forward?

James: For your first question, we are currently working on the budget for 2018. I personally don't expect there will be a significant capex increase because the new spectrum we just acquired, they will end by the end of 2018. Right now, the operators are still using the original spectrum for their 3G services. So, next year, I don't expect there will be a significant capex for this new spectrum.

Rosie: Regarding dividends, we will pass your message to the board for approval in the second quarter of next year.

Peter Milliken, Deutsche Bank HK: *Two more questions. One is on the roaming revenue, should we assume that 70% of the roaming revenue has gone away?*

And the other one is churn has been a bit elevated, is there any reason behind that?

Rosie: The churn rate has been coming down.

Peter: *On the month-to-month basis, yes, but, for the quarter, it was relatively high compared to a year ago.*

James: Our postpaid did lose some market share, but in general we are performing the best compared to the other two major operators in terms of the churn of the postpaid customers. I think it's a current trend where more and more people are getting rid of the 2nd SIM card due to a new handset or because of 4G service can serve both data and voice. Thus, much of churn rate for the industry as a whole is a result of people dropping the 2nd SIM card.

Peter: *And the roaming revenue?*

James: As I mentioned earlier, the 70% already moved back to APT at the beginning of this year and it's already been reflected in our budget plan this year. Even though we lost quite a lot of domestic roaming revenue, our performance up to the 3rd quarter in terms of the bottom line has been pretty good. And the main reason for this is our value-added services is doing

quite well and, secondly, is the expense and cost control.

Rosie: We have also provided differentiated products for our customers, which has also helped us to a certain degree.

Amber Wu, Yuanta Taiwan: *Does it make sense if we expect a slight flat YoY D&A given no significant capex next year and the spectrum might be deployed in 2019?*

Rosie: Amortization-wise, actually we got 5MHz back in the 4Q. Yes, it could be kind of flattish.

Amber: *Flattish and slight increase on YoY basis?*

Rosie: Could be.

Ronny Zhu, UBS Shanghai: *A follow-up question on SIM card consolidation. I've noticed that SIM card consolidation has lasted for more than a year. I've just noticed that your mobile subscriber base by the end of 3Q is similar to what it was at the end of the 2Q. Can we assume that the SIM card consolidation is reaching the end?*

James: I wouldn't say the end, but I think it will slow down in the next year.

Ronny: *So, it will still continue?*

James: Yes, probably.

Varun Ahuja, Credit Suisse Singapore: *A few questions regarding the auction side. The four blocks of the 2100MHz that you won, are those contiguous? Because from what I saw on the NCC site, it shows as everyone being non-contiguous spectrum band as of now.*

Rosie: The auction spots that you see from the NCC website is not the positions we will be getting in the future. Through some negotiations, we can get what we want if successful.

James: This time the auction is quite different from what we've had before. We call it two-process auction. Through negotiation, if everyone can reach a consensus, we don't need to bid for the second auction. And, from what I saw, everybody got their own. So, I don't expect a second auction.

Varun: *Can you give a little more detail?*

James: Right now, in our 3G, we are in E6, 7, and 8. Taiwan Star has two blocks next to us, but this time they only bid for one. So, I would expect E5, 6, 7, 8 probably will be the blocks we get. Taiwan Star has E4. And FET has 3 blocks in E1, 2, 3. From what I've seen, everyone got their own.

Varun: *And CHT has four blocks.*

Rosie: Four blocks in the 2100 frequency band and one in the 1800 frequency band.

Varun: *So, Taiwan Star lost two blocks of spectrum.*

Rosie: Taiwan Star just got one, in the 2.1GHz. Yes, they lost one block.

James: And that's the one we will probably pick up because it's next to us.

Varun: *If I heard you correctly, the earlier three blocks cost you NT\$10.7bn.*

Rosie: NT\$10.3bn roughly.

Varun: So, the amortization cost should come off in 2018. When does the license period end?

Rosie: Do you mean new spectrum or the old 3G license? The 3G license will become due at the end of 2018.

Varun: So, the benefit will flow into 2019?

Rosie: Yes.

Jack Hsu, Sinopac Taiwan: *Two questions. First, could you give us how many 4G subscribers at the end of the 3Q? Secondly, regarding the 4G spectrum auction, you had some good results. What kind of impact do you see these good results having for TWM? Such as will it benefit subscriber growth in the future, etc.?*

James: Right now, our 4G penetration rate as of the end of the 3Q is 75%. Regarding the 2nd question, with this 4 new spectrum, in 2019, one or two blocks will be for the original 3G

voice and some 3G data services. The other two blocks will be used for 4G. Thus, we can provide 3 band carrier aggregation to increase our upstream and downstream speeds. That's the original plan, but the good part is that there might be a chance that we use one block for 3G data plus voice and the other three blocks with 15MHz will be used for 4G services. So, that will enhance our 4G speed even more.

Jack: *When you start the new spectrum, will carrier aggregation improve the quality voice and data transmission?*

James: Yes and no. Yes, theoretically, if you have 3 band carrier aggregation, of course it will improve the download speed. No, in the sense that in the market, only less than 10% of users have 3 band carrier aggregation handset. That's something we need to figure out is when is the right time to widely deploy 3 band carrier aggregation because those handsets are not ready yet. So, even though your network has 3 band carrier aggregation, the user can't experience the higher speed because the handset lack the capability. So, if you want to widely deploy your network to accommodate 3 band carrier aggregation, you have to see if the handsets are ready.

Jack: *Will the new spectrum be helpful in developing the IoT business?*

James: Well, not necessarily. Basically, we will use narrow band IoT. I would prefer to have IoT services on the lower frequency band because of its good penetration and coverage. So, next year, we will fully deploy our IoT network, probably on the 700MHz frequency band, not on the new spectrums we just got.

Jack: *When the new spectrum launches, will customers who are using the 700 originally be able to use more spectrums on the 1800 and 2100?*

James: Right now, we have widely deployed 2 band carrier aggregation with a coverage of 85%. So, once your handset has 700MHz and 1800MHz capabilities, you can enjoy 2 band carrier aggregation. As I mentioned, for 3 band carrier aggregation, we have to wait and see if the customer's handset is ready for 3 band carrier aggregation.

Jack: *Are you optimistic about the sales of the iPhone X?*

James: Of course, the first lot of shipment was gone in seconds. So, yes, I expect the iPhone X to sell well if the supply is enough. Right now, the problem is on the supply side.