

Taiwan Mobile 4Q13 Results Conference Call
January 28, 2014

Moderator: Good morning, good afternoon, ladies and gentlemen. Welcome to Taiwan Mobile Conference call. Our chairpersons today are Mr. James Jeng and Ms. Rosie Yu. Ms. Yu please begin your call. I'll stand by for the question and answer session. Thank you.

Rosie, CFO & Spokesperson: Good afternoon. Before we begin our presentation, as some of you may already know from the announcement we made on January 6, Mr. James Jeng has been named as our new President. He was the CEO and Chairman of Kbro, CTO of Taiwan Mobile and the COO of our Home Business Group.

With that, let's welcome James to begin our presentation.

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

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Let's turn to business overview.

Healthy Mobile Revenue Growth

In the next three slides, I would like to highlight our growth areas.

First on the mobile business:

On a like-for-like basis with our peers, TWM's mobile service revenue in the fourth quarter was up 5% year on year basis, attributed to the increase in ARPU. TWM continued leading the pack with the highest ARPU for four consecutive quarters.

This is credited to healthy growth momentum in mobile data and contained declines in voice revenue.

Please turn to the next page.

Our Smartphone Strategy

Regarding our smartphone strategy:

Apart from the 29 exclusive smartphone models we currently have (listed on the slide), we also have around 66 smartphone and tablet products on the market.

In 4Q13, smartphone sales volume was up 39% from a year ago and accounted for 92% of total handsets sold.

Therefore, mobile data adoption rate went up to 54% of the postpaid installed base, from 42% a year ago. This led to a 34% YoY growth in mobile data revenue in the fourth quarter.

Please turn to next page.

CATV Growth Catalysts

On the cable TV business:

As indicated in the table, our internet subscriber base increase of 6% and DTV customer base growth of 65% were both higher than the 1% subscriber rise in analogue TV service in 4Q13, representing the trend of an expanding penetration rate in both the DTV and cable internet businesses.

Please turn to the next page.

New Products & Services

This page of new products and services we launched during the 4th quarter is for your reference.

Next will be financial overview.

Divisional Performance

CBG showed 8% revenue growth, coming from a 30% data revenue increase and another 30% rise in handset sales revenue. But its EBITDA remained flattish because we continued investing resources to add mobile data capacity, boost smartphone

adoptions, and extend company's own distribution network.

EBG benefited from healthy mobile revenue growth more than offsetting a single-digit YoY % dip in its fixed-line revenue in 2013. This coupled with stable costs/expenses led to an EBITDA increase for the year.

HBG's stable EBITDA was attributed to an up-lift on its blended ARPU, through upselling cable broadband and DTV services to the same households.

Despite its lackluster TV home shopping business, momo's online shopping business registered a strong 40%+ top line growth and close to 30% EBITDA increase in 2013.

Let me turn the presentation over to Rosie for income statement, balance sheet and cash flow analyses.

Results Summary

Rosie: In 2013, we reported total revenue of NT\$109bn, EBITDA of NT\$30.8bn, and EPS of NT\$5.79.

As James had just gone through the highlights of our core business financial results in 2013, I just want to say a few words on our 2013 actual results versus our guidance.

Our 2013 operating income reached 102% of our guidance. Better-than-expected operating profits came mainly from lower-than-expected mobile bundle packages sold.

On the non-operating front, in the wake of phasing in LTE services, we incurred more assets write-off losses associated with legacy equipment in 2013. Having said that, full-year bottom line still outperformed our guidance by 1%.

Please turn to the next page for our divisional performance.

Balance Sheet Analysis

Assets

The main increase in total assets in 4Q was due to the NT\$29.01bn increase in 4G concession.

The net PP&E balance increase in 2013 resulted mainly from the addition of the new

internet data center.

Liabilities & Shareholders' Equity

Gross debt increased by NT\$23.27bn QoQ as a result of 1) raising a NT\$22.27bn short-term bank loans and NT\$2bn commercial paper payable, 2) the repayment of a NT\$4bn matured corporate bond, and 3) a NT\$3bn 2-year bank borrowing with a 1.05% annual interest rate raised in the quarter.

To fund the LTE infrastructure while LTE service prepares to come on stream, we saw a rise in gearing and dips in current ratio and ROE.

Let's turn to the cash flow analysis.

Cash Flow Analysis

4Q13

Net cash inflow from financing activities of NT\$23bn in 4Q13 was mainly to finance 4G license fee and repay a NT\$4bn matured corporate bond.

2013

2013 full-year net investing cash outflow mainly comprised of 1) NT\$11.98bn in cash capex 2) NT\$29.01bn in 4G license fee payments 3) NT\$1.05bn in long-term investment acquisitions.

In contrast to paying down borrowings in 2012, we increased gearing to fund the 4G investment.

2013 cash capex increased from a year ago due to 1) higher mobile capex to meet growing 3G data traffic, 2) a one-time fixed-line expenditure related to making payments for the IDC construction completed in 2012, 3) procuring more set-top-boxes to meet government requirements in terms of DTV penetration, and 4) momo's investment in new studio facilities to produce digital programs and its office relocation.

Despite relatively stable operating cash flow, the aforementioned capex hike resulted in a short-term decrease in free cash flow in 2013.

Let me turn the presentation back to James for 2014 guidance, key message and event updates.

IQ14 Guidance

James: Let's turn to page 14. Before I start, you might have noticed that this year we will start doing quarterly guidelines. You might ask why not the full-year guidelines. I think basically 4G service will launch this year, however a lot of uncertainty and dependency is really based on the NCC's approval.

For IQ14, our revenue is forecasted to grow 5% YoY while EBITDA to be flattish.

Lower write-off losses and one-time land disposal gains of NT\$0.16bn will lead to a 3% YoY increase in EPS in 1Q.

Business Outlook & Key Message

For business outlook of 2014, we expect the mobile industry to continue benefiting from rising smartphone and mobile data adoptions. Taiwan Mobile estimates its mobile data penetration to reach 66% of the postpaid installed base by the end of 2014, up from 54% a year earlier.

Mobile revenue upside potential will also come from the new 4G service as well as online video/game/music/book services enabled by mobile solutions.

The above growth drivers are expected to grow our mobile postpaid ARPU by mid-single-digit in 2014.

We will focus on expense rationalization in an aim to maintain a stable EBITDA for telecom operations despite opex pressure from adding more 3G and 4G base stations and 4G commercial launch marketing campaigns.

Cable TV's EBITDA growth rate will be still maintained at low single-digit in 2014.

momo will be a bright spot with a more than 30% increase in EBITDA in 2014, aided by forecasted healthy growth in its online shopping business and cost cutting of its other business lines.

Taiwan Mobile's total D&A is expected to rise by around 23%, reflecting expanding telecom and digital TV businesses in 2014.

Non-operating expense in 2014 is expected to be much less than a year ago.

Event Update

Capex Guidance

The board today (January 28, 2014) approved a NT\$12.8bn capex for 2014, lower than the NT\$15.1bn expenditure budget in 2013, due to reductions in 3G expenditure expected to be larger than rises in 4G capex.

Regulatory Update

TWM is one of the first two operators to have received approval from the NCC to apply for the 4G network roll-out.

This slide lists the awards we have recently received for your reference.

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

Q & A

Chate Bencha, Credit Suisse Singapore: *I have several questions. The first question is related to average smartphone data usage. Can you give us some guideline on how the usage has changed over the year and what's the average monthly data usage right now?*

James: One by one, otherwise I will forget all your questions. Basically, our data usage will be about 30-35% annual growth in terms of data traffic. So, in 2014, we expect to keep the momentum around 30% growth in data traffic.

Rosie: Average smartphone usage is about 2.4GB per month.

Shirley Chu, Director of Investor Relations: That's the average for 2013.

James: Per user.

Chate: *The second question is related to your negotiations with FET regarding the 1800 MHz. I understand that from the previous quarter you mentioning some negotiations to allow you both to launch 4G on 1800 band. Please update us on where you are right now.*

James: I have no comment on this issue in terms of spectrum swap.

Chate: *You mentioned that you don't provide the full-year guidance partly because of the*

uncertainty around the timing of the 4G launch. I just want to elaborate on that, the timing would have a significant impact on which particular line like the cost related to marketing or the capex or what is the uncertainty about?

Rosie: The uncertainty is mostly related to the regulatory approval. There will be a lot of regulatory approvals down the road. That's why we can't predict the timing of the commercial launch.

Chate: *But you would still be quite confident to launch the services this year.*

James: Yes, I think no later than the third quarter.

Chate: *I understand the capex budget for this year is NT\$12.8bn. Any guideline or any key point for where we should look at the capex going forward as well? Is NT\$12.8bn the peak of the 4G rollout or should we expect it to be at the current level for the next few years?*

Rosie: Well, let me give you the breakdown of the capex first. For Taiwan Mobile, the overall capex will be NT\$9.6bn, which is about NT\$2.1 less than last year's. TFN's capex will be somewhere around NT\$2.1bn and cable will be roughly NT\$1bn. So, overall capex is NT\$12.8bn and we expect to continue a similar pace in capex in the coming year or maybe less down the road because the deployment pace for 4G will be very different from 3G. It will probably be higher in the first few years, but it will be lower in the later stage. For 3G, as you all know, we gradually deploy our infrastructure. So, that's the main difference.

Chate: *One last question. Within your 2014 outlook, you mentioned a material increase in the depreciation & amortization expense, is that mainly related to the 4G spectrum amortization?*

Rosie: Yes.

Lucy Liu, JP Morgan HK: *I just have two questions. Do you have any comment in terms of new entrant risk? Are you aware of any progress made by either Ting Hsin or Hon Hai on their future strategy? I'll ask one by one also. Thank you.*

James: For the 4G newcomer Ting Hsin, they have already merged with Vibo. We will see how they progress because right now Vibo does have 3G infrastructure, however how to migrate from 3G to 4G is still a lot of work ahead. In terms of Hon Hai, it will purely start from a greenfield. They don't have any 3G, 2G infrastructure nor fixed-line infrastructure. So it will

probably take them a little bit longer to launch 4G services. So this year, I think basically the three major operators will probably be the main competitors in terms of the 4G services.

Lucy: *As a follow-up to that, I understand that Vibo recently launched very aggressive pricing plans like offering almost unlimited data, unlimited on-net calls, and 200 minutes of off-net calls with a very cheap price. I'm not sure whether you think this will delay your data monetization probability after launching 4G because I think all three operators mentioned that you want to remove unlimited pricing and move to tiered pricing with the 4G launch, but are you afraid the new entrant or the competition will delay the process.*

James: I think that in terms of the key to the success of the 4G services or even the HSPA 3G services, one is the coverage, means the population coverage. Secondly is the speed. Even though Vibo provides very aggressive pricing, but due to the small coverage and its 3G technology, I will still say the competition is keen. But, at this point, I don't see the threat yet.

But for the 4G services, I think tiered pricing for the 4G services is a worldwide trend right now. If you see the major 4G services in the USA, Korea, Japan, it's all tiered pricing. So, I personally believe in Taiwan, tiered pricing is also the pricing strategy for the service operators. Meanwhile, the NCC commissioner also promised they would agree all the operators to utilize the tiered pricing strategy. So, I think it's quite promising.

Lucy: *So, the next question is on the probability impact from 4G. I think in your guidance, you mentioned that earning will be impacted in 2014 due to the 4G launch. I think probably in my view because you launch 4G in 3rd quarter and amortization, depreciation and all these will start first. But do you think the competition-related opex or cost will drag into 2015 or in other words, when do you think we will see the positive earnings impact from 4G?*

James: Well, we don't have the guideline for 2015. But you mentioned the opex, it might be related to the handset subsidy. But right now I have no precise detail for that in terms of opex in 2015.

Lucy: *Lastly, on dividend, any latest thoughts given the pressure on earnings. What kind of guideline can we give investors on the dividends?*

James: Well, in terms of dividends, in April, a board meeting will decide that. So far, I have no comment on it.

Rosie: But, as you know, we have a lot of reserves totaling NT\$29.7bn. So, we do have the

flexibility and ability to top-up our earnings if the board approves.

Alastair Jones, New Street Research UK: *I just wanted to come back to the question asked earlier regarding data traffic. You mentioned 30-35% annual growth in data traffic. Is that growth per user or was that total data traffic growth on your network?*

And related to that, on the 2.4GB per month for 2013 average you mentioned, can you give an indication what it was for Q4? Because I would imagine because it has been growing, it's probably higher in Q4.

James: Actually, the average 2013 is 2.4GB, but 4Q13 is 2.9GB, so we expect the data usage per user per month will be more than 3GB by end of year 2014.

Alastair: *And a separate question regarding your capex for 2014. What's your expectation for cash capex for 2014? You obviously spent just under NT\$12bn cash and I think your balance sheet spend was around NT\$15bn for 2013. Can you give a sort of guidance for cash capex for 2014?*

Rosie: Cash capex cannot be gauged easily at this stage because it has a lot to do with the completion of inspection of the capex done, so it's very hard to gauge at this point in time.

Alastair: *Is it likely to be higher than the NT\$12.8bn guidance that you've given?*

Rosie: Probably no because it normally takes a longer time for inspections.

Jack Hsu, Sinopac Securities Taiwan: *Capex for 4G, can you separate by different sectors like how much will be spent on base stations and for fiber, etc.?*

James: I cannot disclose that detailed right now, but, in terms of the capex, 4G definitely in 2014 is a major part of the capex. But we cannot give that detailed of a breakdown.

Chate Bencha, Credit Suisse Singapore: *On the cable side, I understand that the cable broadband has progressed well. But would you think there's anything you can do to actually speed up the subscriber growth and also to monetize the potential that you have from upgrading your paid TV subscribers to broadband subscribers, some price action or something along the way?*

James: Well, for Taiwan Mobile, the broadband cable penetration rate reached 31%. It's the

highest among all the MSOs right now. We expect subscriber for this year or the coming years remain about 6% to 7% annual growth. As you know, the fixed broadband is such a huge market in Taiwan, so the competition is very keen. However, we are doing pretty good in previous years. We expect for this year, we will remain the momentum with 6% growth.

Alastair Jones, New Street Research UK: *Just looking at the mix of smartphone sold during the quarter. You previously gave some indications as to what was high-end, what was mid- to-low-tier. I was wondering if you could give an update what that was in Q4 and also once you launch 4G if you would expect that mix to shift toward high-end, which would obviously have implications for EBITDA margins.*

James: In terms of high-end, mid-end, low-end distribution of smart devices, in 2013, our high-end was 46%, low-end was about 46%. And we expect for the year 2014, the high-end, because of the 4G service launch, will grow from 46% to 50something%.

Alastair: *And low-end, you said 46%. Is that right?*

James: Yes.

Peter Milliken, Deutsche Bank HK: *A question on momo, the 30% EBITDA growth forecasted for this year, that's impressive. Is that just low-base effect or is there some major change happening there?*

Rosie: Yes, they have some major changes. As you might be aware of, they have shut down a lot of their drug stores and they have sold their department store to the Breeze Group in Taiwan. In the past, physical channels were suffering quite a lot of losses and, starting from this year, you will see much less losses from this end. And also, as you all know, e-commerce business has been growing very rapidly and that's a main contributor to the growth.

Jack Hsu, Sinopac Securities Taiwan: *Will the company have any plans to borrow money or issue CBs in 2014?*

Rosie: No EPS dilution funding instruments will be considered.

Sydney Zhang, Merrill Lynch HK: *I have two questions. The first one is related to last year you made major efforts trying to build more direct stores, have a lot of transformations there. I was just wondering how many stores were built last year and how many new stores are you going to build this year and whether those new stores*

have been able to breakeven so far?

Rosie: We have added 77 stores for the past year, so our total number of direct stores reached 497. And this year, we expect further expansion to increase our channels because our own direct channels have done quite well. Of course, we will review their performance on a periodical basis to ensure they can contribute positively to our overall operations.

James: Just for your information, if you add up, for direct stores and the franchise stores, we have a total of 871 stores, which is 27% of the market share in Taiwan in terms of stores.

Sydney: *So, will be the number of new stores going to be significantly smaller given that you're going to spend the money on 4G?*

James: We expect this year probably 73 new stores. That's our plan.

Sydney: *I know you don't provide the 4G capex breakdown, but do you have a target by the time in the 3rd quarter when you launch the 4G services, what kind of coverage plan do you have in terms of how much population you're going to cover or how many base stations? Can you give any color?*

James: I do not have a very precise figure right now. But, as you know, for the 700 band, it has higher coverage in comparison to the 1800. I will say in comparison to the other operators, we will higher population coverage once we launch the service.

Sydney: *So, are 2,000 new cell sites on the 700MHz fair to cover Taiwan?*

James: You mean how many base stations will cover Taiwan? It depends on the technology. If you say 700 band, you will probably need only 4,500 or 5,000, but for the 1800MHz, you will need more than double.

Sydney: *So, 4,500 for 700 band and double for 1800 band.*

James: Yeah, roughly.