Taiwan Mobile
3Q20 Results Conference Call
November 6, 2020

Jamie Lin, President: Good afternoon everyone. Welcome to Taiwan Mobile's third 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.

Alright, now let's turn to business overview. I will start with operational highlights for the third quarter.

3Q20 Operational Highlights

Since the launch of 5G commercial services in the beginning of the quarter, we have seen encouraging 5G sign-ups and ARPU lift among the upgraders despite limited 5G handset options and the lack of a 5G iPhone. On the other hand, amortization of 5G spectrum also started to kick in and has had a negative impact on our telecom business' bottom-line performance for the third quarter.

Meanwhile, competition in the telecom industry has remained rational since 5G service launch, as 4 out of 5 operators have set the baseline of 5G unlimited data plan at NT$1399 per month. Given the lengthening smartphone replacement cycle, TWM has led the market into offering 48-month handset bundle contracts for consumers, which is now emulated by both of our major peers. This movement will not only encourage users to upgrade to higher-end 5G phones at higher ARPU, but will also further rationalize the competitive landscape in the long-run.

As for momo, our e-commerce business delivered another set of solid results in the third quarter, as it took more market share and further strengthened its logistic capabilities. Going forward, we will continue to leverage group resources to support momo's business expansion.

Overall, our net income arrived 10% ahead of our third quarter guidance.

Now let's turn to slide 5 for a closer look at our telecom business.

Mobile Business in 5G Era

For the first three months of 5G service launch, the rate of adoption was 50% higher than that of 4G. Moreover, we have seen a healthy monthly fee lift in the users upgrading to 5G, to the tune of 22% in the third quarter, and it expanded to around 25% in October. 90% of all 5G sign-ups opted for $999 or higher rate plans and a healthy 58% of them opted for $1399 or higher plans. Excluding IoT subs, postpaid monthly fee already turned the corner and posted MoM growth in September. It's also worth noting that our mobile service revenue recorded its first QoQ stability since the $499 frenzy in the second quarter of 2018.

With the release of iPhone 12, increasing Android 5G handset options, as well as improving network coverage, handset bundle sales and device sales should pick up steam in the fourth quarter this year, boding well for ARPU.

In addition, our Double Play bundle (unlimited mobile data + high speed home broadband) posted a 44% QoQ surge in new sign-ups in the third quarter, with rising proportion in 1Gbps super high-speed fixed broadband which acts as a complementary indoor coverage service to 5G.

Now let's go to slide 6 for an update on our cable TV business.

CATV Business – propelled by Broadband

In the third quarter, we again fared better than our MSO peers in the YoY trends of basic TV subscriptions and broadband service penetration.

Supported by growth in TV content aggregation revenue and rising broadband momentum, CATV revenue went up by 3% YoY and EBIT was flat YoY amid competitive operating environment. As demand for faster home broadband access continued to increase, cable broadband related revenue expanded 9% YoY in the third quarter.

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

momo – the Growth Engine

Despite a sequentially slower quarter, momo's e-commerce business continued to outgrow its peers and delivered strong results, with the total number of transactions jumping by 30% YoY.

On the logistics side, in addition to expanding its in-house delivery fleet, two more satellite warehouses were added in the third quarter, taking the total number of satellite warehouses to 19, which is 6 more than a year ago.

As a result of increasing scale and operating leverage, momo's e-commerce operating margin improved meaningfully from a year ago. Payment processing fee as a percentage of revenue also dropped, aided by rising adoption of its private label credit card.

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.

In the 3rd quarter of this year, our consolidated revenue once again grew on a YoY basis, mainly driven by momo, which accounted for half of the Company's consolidated revenue. Telecom revenue and EBIT, on the other hand, recorded steeper YoY declines than the previous quarter, mainly due to soft high-end handset bundle sales, especially in contrast to the boost from iPhone 11 sales last year, as well as 5G spectrum amortization.

While CATV EBITDA dwindled YoY in 3Q, mainly attributable to competition in basic TV business, its EBIT was flat YoY. It was because of the falling depreciation of set-top boxes, though this tailwind has subsided.

momo continued on its growth trajectory propelled by its e-commerce business, posting a 26% surge in revenue and further expanding its EBIT by 38% in the quarter.

Let us move to Results Summary. Next page.

Results Summary

In the 3rd quarter, combined operating income of CATV and momo increased 15% YoY and helped mitigate the slide in telecom profits.

For the first 3 quarters of this year, total revenue tracked slightly behind. However, the muted telecom performance was offset by lower selling expenses and momo's operating leverage at the operating income level. Overall, our operating income for all major businesses achieved management expectations.

Net income also came in ahead on the back of lower-than-expected non-operating expenses brought about by higher dividends from investees, downward trend of interest rate, and momo's disposal gains. EPS for the period reached 83% of the Company's FY20 guidance. Let's move on to Balance Sheet Analysis.

Balance Sheet Analysis

On the asset side, PP&E rose YoY and QoQ on the back of the 5G network rollout, while the YoY surge in concession was a result from the acquisition of 5G spectrum in 1Q20.

On the liability front, gross debt increased QoQ to 73bn NTD at the end of the 3rd quarter as we bumped up short-term borrowing to fund our dividend payment. The YoY rise in net debt to EBITDA was associated with the incremental debt we took on for the acquisition of the 5G spectrum.

As for shareholders' equity, the YoY and QoQ changes in paid-in capital and capital surplus were insignificant as majority of our convertible bond had already been converted.

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

Cash Flow Analysis

In the 3rd quarter, the YoY drop in operating cash inflow was attributable to momo's inventory expansion if we exclude an impact of around NT$5bn from a couple of one-off factors.

Investing cash outflow narrowed QoQ and YoY, due to shrinking cash capex and the sale of Taiwan High Speed Rail shares.

On the financing front, short-term borrowings climbed QoQ to fund the dividend payments.

As 5G rollout is still under way, cash capex showed a YoY decline in the 3rd quarter. Cumulative free cash flow calculated with pre-IFRS 16 operating cash flow was NT$14.8bn for the first three quarters of this year, translating into an annualized free cash flow yield of 7.3%.

Okay, let me turn the presentation back to Jamie for Event Updates and Key Message.

Events, Awards, and Recognition

Jamie: Thanks Rosie. On page 14, we summarized the awards and recognitions we received during the quarter, for your reference.

<u>Key Message</u>

Finally, on slide 15, I would like to wrap up our presentation, with the key message we would like for you to take away.

The competitive landscape in Taiwan's mobile industry has become more benign, evidenced by the continued decline of ported numbers since 5G launch in July, as all operators introduced higher monthly fees for 5G unlimited data plans. Meanwhile, our 5G service is poised to gain momentum on the back of accelerated network rollout, iPhone 12 release, and a wider range of 5G Android phone options. Enhanced synergies from momo and cable broadband also give us an edge over our peers.

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

Q&A

Neale Anderson, HSBC: ***I have two questions on the wireless side. The first one is the 5G status relative to 4G. We're seeing a 25% increase in spend. How does that compare to the early phase of 4G? Is it any better or roughly the same? The second question relates to when we can start to see an improvement in the YoY trends. You pointed out QoQ stabilization but given what you can see now with stabilizing competitive dynamics and 5G uplift in revenue, when would you expect that to translate into a YoY improvement in telecom revenue and EBIT?***

Jamie: Let me answer the second question first. So in terms of the timing of revenue turning a corner, we're expecting it to happen in the next 6 to 12 months. In terms of that translating into bottom line, it's probably going to be a longer-term phenomenon, so anywhere from 12 to 36 months from now, depending on the competitive landscape.

Neale: Okay, that's great. In terms of the timeline you outlined, does that assume 5G pricing remains roughly stable? Is that the basis for that estimate?

Jamie: Yes. It looks like the competitive landscape is pretty rational right now. Also, the fact that all 3 major operators are offering 48-month plans will further stabilize the landscape in the mid to long term. But it still depends on how things play out 12 to 24 months from now.

Amber Lee, Yuanta Securities: ***Two questions here. The first one is a follow-up on Neale's. I think you mentioned around 20% increase in spending. Does this number compare SIM-only to SIM-only plans and bundle plans to bundle plans? Or is this a mix of SIM-only plans upgrading to 5G handset bundle plans? The second one is on the iPhone sales. For the sequential trends in mobile device sales that you mentioned, what kind of growth momentum should we be expecting? Is it substantially stronger compared to the seasonality in the third or fourth quarter of last year?***

Jamie: Amber, I'm sorry, can you repeat your second question?

Amber: Second one is on the device sales momentum. As you mentioned, there would be a strong sales growth in the fourth quarter. Just wondering, what kind of sales momentum should we be expecting? Would it be substantially stronger than the third and the fourth quarter of last year?

Jamie: Got it. In terms of monthly fee lift, we're observing a 25% lift from 4G to 5G upgrades in October. Right now, we're not separating the SIM-only plan versus handset bundle plans as more than 90% of the customers would opt for handset bundles. So if we're talking about SIM-only plan, the monthly fee lift is even higher. In terms of device momentum in the fourth quarter, based on the initial numbers we're observing, the demand is 2 to 3x higher than the previous year. But the problem is with supply; right now, we're not getting enough supply from Apple. On the other hand, our exclusive Google 5G phone, the Pixel 5, is also observing similar YoY trends but the problem is also with supply. Right now, we're affected by the global supply chain situation but other than that, some of the other Android phones are being provided to us healthily, so our momentum is still much better than we expected.

Amber: Do you expect the supply shortage problem to be resolved in the coming months?

Jamie: We're expecting it to be resolved in the next 2 to 4 weeks.

Sara Wang, Morgan Stanley Hong Kong: ***Just one question on the capex. What's our latest capex budget for the whole year? According to some news sources, it seems we have increased our capex budget for the full year. Would you please give us more details on the rationale behind this? Also, do we seek any partner on network sharing, especially after Far EasTone announced further network sharing with APT?***

Rosie: Overall capex for this year is TWD$20.4bn, which has been disclosed. As to our network sharing, Jamie will give you more color on that.

Jamie: I think the rationale behind the faster rollout, an accelerated rollout of our 5G base stations, is our thesis that most customers are not looking for the operator that provides the higher speed. Rather, they're looking for an operator that provides the best coverage. So Taiwan Mobile's strategy is to be that provider, where they can get a 5G signal in most areas they go to. Right now, based on our in-house estimate, we have built more 3.5GHz 5G base stations than any other operator here in Taiwan. We're at almost 4,000 base stations, and we're going to continue to build out towards 6,000 3.5GHz 5G base stations. I think that is contributing very well to our commercial side of the equation. That is why we're observing healthy take ups and healthy monthly fee lift. In terms of network sharing, we're keeping all the options open. If we have more developments, we'll be sure to update everyone.

Sara: Just one quick follow-up, so 6,000 is the target for 2020?

Jamie: Yes.

Billy Lee, Credit Suisse Hong Kong: ***I've got two quick questions. First one is a follow-up on base station. You said 6,000 is the target for this year. How many 5G base stations do we have right now? The second question also relates to capex. I noticed that across the first 9 months, cash capex was just roughly TWD$5bn. This looks quite small when you compare it with the overall full year capex guidance. Does that imply there will be around TWD$15bn capex coming in the fourth quarter?***

Jamie: Like I said, we have built almost 4,000 3.5GHz high-speed 5G base stations, which is much more than any of our peers. Some of our peers would claim similar 5G base station numbers but they have built a mix of 3.5GHz and 2.1GHz 5G base stations. So if you would compare apple-to-apple, only 3.5GHz of high-speed 5G stations, then we have almost 4,000; that is the largest among our peers by far. Towards the end of the year, we intend to build close to 6,000 3.5GHz 5G stations. In terms of capex, I'll have Rosie explain a little bit.

Rosie: As you know, the rollout is continuing so the payment will also be continuing. It will be slightly later and maybe some of them will be delayed until early next year.

Jack Hsu, SinoPac Securities: ***I have two questions. The first question is, do we have any 5G customer target in the end of 2020 and 2021? My second question is, I was informed that the 5G base station will need more power, more electricity in comparison to 4G, so will the electricity expense be higher in comparison with the 4G era and how will we control this added expense or cost?***

Jamie: We do have a 5G customer target but we're not sharing the number for now. All I can say is, we're ahead of the 4G era in terms of penetration and we expect it to remain the case throughout the rest of the year. Yes, with 5G base stations operating live, the cost of electricity will increase for us. Exactly how much it will increase, I think we'd rather keep it as confidential information.

Jack: Okay, another quick follow-up question is about outlook. Will we change our financial forecast in 2020?

Rosie: We do expect to reach our target for this year. We have no intention to change our guidance for now.

Sara Wang, Morgan Stanley: ***Just two questions. First one is that previously in the call, you mentioned 5G spending is 25% higher. Would you please elaborate more? What's the comparison? Is it for the same customer's 5G spending versus when he/she was on a 4G plan? The second question is, what's your longer term view on the market share dynamic? It seems competition remains a matter of concern. Going into 5G, what other factors do you think will drive a change in the market share?***

Jamie: When we talk about 25% monthly fee lift, yes, it's an existing customer renewing his/her contract from a 4G contract to a 5G contract. In terms of the competitive landscape in the longer run, it looks like things are cooling down, especially with a smaller operator working closely with one of the major operators. But things like this are really hard to predict. Generally, we feel that over the next 3 to 5 years, things will be a lot more rationalized than before.

Jack Hsu: *I have one question about the iPhone subsidy. Will 5G iPhone subsidy be higher than the 4G iPhone's?*

Jamie: It depends on which plan the customer chooses. If it's a shorter period contract, then it's similar. But if he/she chooses a longer period contract, for example a 48-month program, then of course it's going to be higher. You can view the subsidy as being spread out through a longer period.

Jack: Okay. I just want to clarify: if it's almost the same tariff and almost the same period, will 5G iPhone subsidies be higher than the 4G iPhone's?

Jamie: Apple-to-apple comparison, the subsidy is very similar.

Jack: One more question, what is the percentage of customers whose tariff plan is TWD999 and above?

Jamie: For 5G customers, around 90% of them chose TWD999 or up plans and 58% of them chose TWD1399 up plans. I don't think we're disclosing the number for the entire user base.