

**Taiwan Mobile**  
**3Q15 Results Conference Call**  
**October 29, 2015**

**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 start with the mobile operating performance.

**Continuous 4G Business Expansion**

The 4G service take-up rate reached 35% of the postpaid installed base as of the end of 3Q15. As 4G postpaid ARPU was 1.6x the company's postpaid ARPU, a rising 4G postpaid subscriber number helped mobile postpaid ARPU grow by 3% YoY in the quarter, hitting a record high of NT\$870. As such, mobile service revenue would have grown by 1.3% YoY in 3Q15, if we had adopted the same accounting principles, i.e. residual value method, as our peers.

Please turn to the next page for our CATV operations.

**Steady Growth in the CATV Business**

The YoY growth in pay-TV related revenue was resilient at 1%, underpinned by continual increases in digital TV service adoption. Our cable broadband also benefited from a rising mix of the high-speed service, i.e. above 50Mbps, up to 35% in 3Q15 from only 25% a year ago.

Overall, rising total revenue and effective cost controls supported a 3% YoY increase in cable TV business's EBITDA in 3Q15.

**Retail Business**

For the first three quarters of this year, momo derived 66% of its revenue from the online shopping business which registered a 15% YoY growth. However, its TV home shopping business remained lackluster.

momo's EBITDA margin contraction was due to 1) decelerated overall revenue growth, 2) higher channel costs for its TV home shopping business and 3) lower revenue mix from its higher-margin TV home shopping business.

Having said that, momo's cumulative net profit for the first three quarters was underpinned by 1) more equity income from overseas affiliates in Thailand and China, 2) higher interest income and 3) no similar loss from its discontinued cosmetic store operations in the same period of 2014.

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

### **Results Summary**

#### **Rosie Yu, CFO & Spokesperson:**

Regarding our third quarter results, a steady increase in 4G subscriber base has resulted in a YoY rise in telecom service revenue. The lowered handset subsidy level and our aggressive expense controls led to a brisk 3% QoQ and 6% YoY growth in EBITDA in 3Q15.

EBIT and net income in 3Q15 both also registered healthy growth as the strong rise in EBITDA was far more than sufficient to mitigate the increase in 4G related D&A.

Our 3Q15 top line came in lower than our forecast, due largely to lower-than-expected sales of high-end phones and weaker momo's retail revenue. However, with strict expense discipline, we still managed to beat our EBITDA and EPS targets by 1% and 13%, respectively.

For the first three quarters, YoY growth in EBITDA was less than the increase in D&A. Our net income remained stable compared to the same level it was a year ago as a result of having a big YoY decrease in non-operating expenses.

### **Performance by Business**

This slide provides revenue and EBITDA breakdown by products for your reference.

I would like to highlight that the EBITDA of the telecom business grew 9% YoY, which suggest a steadily improved 4G profit profile for 3Q15.

### **Balance Sheet Analysis**

On the asset front, as of the end of 3Q15, cash balance remained at a healthy level of NT\$7.28bn after cash dividend payments. Other current assets rose QoQ and YoY due to the counter-security deposit we provided to the Taipei District Court associated with a lawsuit with FET and momo's increased time

deposits following its rights issue in 4Q14, respectively. PP&E did not further grow as new addition in 4G equipment was smaller than the overall depreciation incurred for the quarter.

On the liabilities & shareholders' equity, gross debt balance rose to NT\$65.77bn mainly to finance the dividend payments in 3Q15. Nonetheless, other current liabilities decreased QoQ due to the \$15.24bn cash dividend payments made in 3Q15.

On the ratio analysis, the ratio of net debt to EBITDA increased in the quarter because of cash dividend payments. The ROE remained intact at 30%, supported by our high dividend payout policy.

### **Cash Flow Analysis**

In 3Q15, our working capital cash outflow decreased QoQ mainly due to more corporate income tax and handset payables paid in 2Q15. This, coupled with higher cash earnings, resulted in the sequential rise in operating cash flow.

In terms of 3Q15 investing cash flows, apart from the close to NT\$3bn capex, we set aside NT\$927mn as a counter-security deposit that I just mentioned in the previous section. To participate in the upcoming 2.6GHz spectrum auction, we provided a NT\$1bn deposit to the regulator.

Other investment activities in the quarter included 1) the receipt of NT\$0.5bn from THSR for its cancellation of preferred shares, 2) momo's NT\$0.19bn money market fund redemption, 3) NT\$0.11bn cash from the disposal of an unused property in the quarter and 4) NT\$80mn investment in Media Asia Group Holdings Limited made by momo.

On the financing front, a total of NT\$11.08bn in borrowings was raised in the quarter to fund the NT\$15.24bn cash dividend payment.

Aided by higher operating cash flow and lower capex, we registered higher FCF compared to a quarter ago. In addition, 3Q15 FCF also improved YoY, arising from capex reductions.

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

### **Event Update**

**James:** On the new product front, we launched an annual upgrade program for iPhone 6s customers to cater to their needs to have the latest iPhone without bearing a standard two-year contract. In addition, they are also entitled to a worry-free handset warranty for an additional charge of only NT\$258 per month.

The lower part of this page lists the awards and recognition we've received in the third quarter of 2015 for your reference.

### **Key Message**

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

The 6% and 11% YoY growth in EBITDA and net profit for 3Q15 reflects our solid execution of 4G strategy. We will continue to scale up our 4G business and strengthen our LTE network leadership through sensible spectrum investments aimed at enhancing both customer experience and shareholder value.

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

### **Q & A**

**Danny Chu, Macquarie:** *First question is related to the momo business. You mentioned in the presentation that the TV home shopping business revenue has slowed down during the period. Going forward, should we expect this to be a one-off trend or this is going to be a structural change that the TV home shopping business will continue to decline?*

*Second question is also related to the momo business. In terms of the declining EBITDA margin, going forward, what kind of EBITDA margin level should we expect for the momo business overall?*

*Third question is related to the counter-security deposit you made regarding the lawsuit with FET. Is there any rough timeline that we should expect for it to be resolved, within 12 months, 18 months, 24 months?*

**Rosie:** Regarding momo's trend, the retail market is not doing very well, but they would come up with some strategy to cope with the weak economy here in Taiwan. You know momo is a listed company already, so I don't think we can disclose more details to you, but definitely they will be doing something about it. And we believe next year, the situation may improve. As to their EBITDA levels, to be frank, since we haven't released our guidance, I don't think we can provide you with any more clue than what we have here.

On the counter-security deposit we provided to the court, the dispute between FET and us is now up to the courts to decide. We don't know when the whole issue could be resolved. But we strictly followed the spirit of the agreement. So, we shall see.

**James:** As you know, in Taiwan, the judicial process normally takes a long time. So, no one can really

foresee when it will end.

**Danny:** *If I can, I would like to ask one follow-up question. It's related to the telecom business. I understand the EBITDA margin of the telecom division improved during 3Q. But, given that, the iPhone was launched in Taiwan in October, so should we expect the EBITDA margin to decline a little bit in the 4Q to take into account the iPhone launch or will certain measures be put in place in order to keep the EBITDA margin for the telecom division same as current level for the 4Q?*

**James:** Well, as you know, the iPhone 6s is selling very well at Taiwan Mobile in October. So, as you just said, there will be some declines in the bottom line. But, if you compare the 4Q this year with the 4Q last year when the iPhone 6 launched in the end of September, I would expect the 4Q15 EPS to decline QoQ, but not as serious as last year.

**Danny:** *Do you mind elaborating a little bit on the point you just mentioned that EBITDA will decline, but not as seriously as one year ago? Are there any particular reasons behind why you think the EBITDA decline related to iPhone launch this year will be smaller than last year?*

**James:** I think the total handset sold in terms of the volume will be around the same as the same period last year. However, the subsidy per handset is slightly lower than last year. And, also, we already accumulated a large base of 4G subscribers, so I will say the top line will increase. As such, in terms of the 4Q15 EPS, it will perform a little better year over year. For the full year, we should be able to meet or even exceed what we forecasted in EPS.

**Gopa Kumar, Nomura:** *First question is regarding the iPhone upgrade program that you have launched. In your estimate, what could be the net impact from this on your bottom line?*

*Secondly, I know the data consumption in Taiwan is very high at around 10GB per user per month. Given how your capex is trending, are you comfortable with that sort of usage level or would you be taking steps to reduce the usage per user?*

**James:** To answer your first question, I think for this iPhone upgrade program, the take-up rate has reached 27%, which is much higher than I expected. And one thing I have to mention is that not every iPhone subscriber is entitled to this program. For last year's iPhone 6 customers, their contract periods are not due yet, therefore they are not entitled to this program. So, I would expect for the coming months, there will be more and more iPhone subscribers who will be entitled to this program. And I think that will boost the take-up rate to reach 30%.

In terms of the 2<sup>nd</sup> question, the 4G data usage reached 13GB, but on average, it is around 10GB if 3G

and 4G are blended. I think we are still quite comfortable at this point because the network capacity right now is sufficient enough to support further growth. In terms of network utilization, right now it is only about 20% or 30%, so I think we should have sufficient capacity for further growth in the 4G subscribers.

**Gopa:** *I have a few follow-up questions. One is regarding of the iPhone upgrade, what could be the net impact on EBITDA considering the higher subsidies you would have to offer with this program? And, secondly, you mentioned the average usage is 13GB per user per month. On a longer term, would you still be comfortable with this, or probably in the middle of next year, would you be taking steps to reduce this?*

**James:** I think fully withdrawing unlimited tariff really depends on the peers, especially CHT. CHT mentioned a couple of months ago that they will probably stop the unlimited tariff sometime around the 1<sup>st</sup> half next year. So, if that is the case, then we will follow CHT to stop the unlimited tariff as well.

**Rosie:** The new iPhone upgrade program will bring some benefit to our EBITDA line. But, the number of new iPhone 6s users is still limited, so you will gradually see a pick-up if more and more people are adopting this new program because they are required to pay an additional NT\$258 per month.

**Jack Hsu, Sinopac:** *First question is do you still have any 2G spectrum right now? Because you have just returned back the 2G GSM 900 spectrum to NCC, but right now I don't know if there is any 2G spectrum left on your hands. Second question is about the dispute between the company and FET. Will this dispute end by the end of this year?*

**James:** For the first question, we have two blocks of 2G spectrum, 5MHz in in the 900MHz frequency band, and another block in the 1800MHz frequency band. The 2G spectrum we have on the 900MHz band is idle after we moved all of our 2G subscribers to the other 2G spectrum on the 1800MHz frequency band. So, if the NCC approves our return of the idle 2G spectrum on 900MHz, we still have to keep the 5MHz spectrum on the 1800 band to serve the remaining 2G users. And, according to the regulations, 2G service will be terminated in June 2017.

Regarding the dispute with FET, as Rosie said, since it's under the judicial process right now, it's hard to say whether it will end at the end of this year, which I really doubt, because it's a lengthy process. So, it probably won't even end next year. Who knows?

**Peter Milliken, Deutsche Bank:** *First question is regarding the iPhone upgrade program. If almost all users were to upgrade in a year's time, is that a bad thing for your profitability at that point in time or does the way the whole thing is structured, it doesn't really matter if they upgrade or not?*

***Second question is on cable TV and whether that is being held back by the unlimited 4G plans causing people to hold back or switch out of fixed broadband?***

**James:** I think for the upgrade program the subscriber has to pay an extra NT\$258 and this definitely will help to raise the ARPU. So, I think this program is good for the bottom line.

Secondly for the cable TV, the unlimited 4G programs affect the fixed broadband a little bit, but not as serious. So far I haven't seen serious impacts on our cable broadband business.

**Neale Anderson, HSBC:** *First question is regarding cable broadband. The growth has been 5-6% in the last couple of years. I was wondering what the driver for this was, are you taking shares from a competitor or are you persuading customers to upgrade to a higher speed and higher price?*

*That's my first question. The other one is more generally about pay TV market in Taiwan and your HBG group. In other markets we are seeing a lot more competition from over-the-top providers and also some pressure from cable TV suppliers to unbundle for more a-la-carte individual channels. Are you seeing anything like that in Taiwan or do you expect that might come about or any broader changes in the way pay TV is sold to the public?*

**James:** For your first question, I think for the cable modem and fixed broadband services, we are still gaining market share right now mainly from CHT ADSL subscribers, because most of the MSOs offer a very competitive pricing, which helps a lot. From CHT's report, as far as I know, they are losing market share in terms of fixed line broadband a little bit to the cable operators.

Secondly regarding the OTT service, for pay TV, we have two sectors, analog pay TV and digital pay TV. For the analog pay TV, yes, it stayed flat or didn't grow, but it didn't decline in terms of the subscribers. So far, I haven't seen a lot of impact from the OTT business. Once again, most of the MSOs have been prepared to provide OTT services as well, maybe launching new products sometime next year as a supplementary service with different programs. I think, you're right, OTT is a trend right now and the MSOs will not miss this market.

**Rosie:** And, just to elaborate a bit on the competition between our cable broadband and 4G, I believe you know our cable broadband has been very successful in increasing the mix of the higher speed services, which is above 50Mbps. So, that won't be affected by our 4G services.

**James:** Actually, our cable sector provides a free upgrade for the low-speed fixed broadband subscribers from 10 to 20Mbps. By paying a bit more premium, they can upgrade to 50Mbps service,

so that will not compete with our 4G services.

**Livia Wu, Yuanta:** *What's your D&A expenses this year and next year?*

**James:** In terms of capex for next year, I believe it will decrease because most of the capex needs for base stations have already been fulfilled. Next year, the capex for the mobile sector will be significantly reduced. So, the depreciation and amortization for next year will not significantly increase. The amortization of 2.6GHz spectrum won't start until the spectrum is being deployed. As I mentioned, the 2.6GHz is only a supplementary spectrum, so we will not start the 2.6G deployment anytime soon.

**Jack Hsu, Sinopac:** *First question is what is your bidding strategy for the 2.6GHz spectrum? My second question is will you need to buy new base stations for the 2.6GHz spectrum?*

**James:** In terms of bidding strategy for the 2.6GHz, 2.6GHz is only a supplementary spectrum to enhance the capacity. For instance, especially in metropolitan areas where there are capacity issues, we might use small cells on the 2.6GHz spectrum to enhance capacity. So, that will not be extensively deployed. In addition, it won't be used for coverage purposes. So, I will expect the capex for the 2.6GHz will be very insignificant for next year.

Regarding the second question, we don't need to build new base stations, but, as I mentioned, 2.6GHz is for capacity enhancement. So, we might use small cells or picocells to improve the indoor penetration. That will be good enough for 2.6GHz deployment.

**Jack:** *One follow-up question, will you change your financial forecast for 2015?*

**Rosie:** No.