

**Taiwan Mobile**  
**3Q18 Results Conference Call**  
**November 1, 2018**

**James Jeng, President:** Good afternoon. Welcome to Taiwan Mobile's 3rd 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 operating performance of our telecom business.

**Steady Increase in Cash Flows**

For telecom service revenue and telecom EBITDA, we provide investors with our YoY changes on both a pre-IFRS and a reported basis. Despite the adoption of IFRS15 starting this year, **we think the pre-IFRS numbers better reflect our operating results and cash generation capabilities.**

Year to 3Q, our pre-IFRS telecom service revenue declined 7% YoY, mainly due to the increased take-up of the \$499 SIM-only plan in May as well as the continuous drop in both domestic roaming and mobile MOUs.

Aided by savings in handset subsidies and channel commission, **our pre-IFRS telecom EBITDA for the first 3 quarters increased 3% YoY.** Thus, we still generated a steady operating cash flow. Through further capex discipline, we also managed to grow our accumulated free cash flow by 7% YoY.

**Cross-Selling Supporting Growth**

For the **video streaming** business, we have been expanding our target customers from mobile users to fixed broadband users through our partnership with leading cable MSOs.

Aided by cross-selling, we expanded our monthly active video user number **by 182% YoY in**

**3Q.** On top of the existing SVOD, TVOD, and freemium business models, we also started an AVOD business model in the quarter, adding another source of revenue to our video streaming business.

For the **fixed broadband** business, our effective bundling drove our fixed broadband subscriber base to steadily **increase by 6% YoY**. In 3Q, our fixed broadband penetration rate reached **39%**. That is to say, the remaining 61% of pay-TV customers suggest further growth potential for our fixed broadband business. The expanding fixed broadband subscriber base also paves the way to our video streaming service.

#### **Enterprise Business – The Bright Spot**

As to **enterprise business**, there are some bright spots namely cloud, IoT, and ICT businesses. In particular, **revenue of cloud value-added services grew more than 50% YoY in 3Q, not to mention 24% rise in IoT revenue.**

#### **momo E-commerce – Crown Jewel**

In **3Q**, momo's **total revenue** rose **22% YoY**. The growth momentum came from the strength in E-commerce revenue, which grew 29% YoY and made up 85% of momo's total revenue. In addition, momo's revenue generated through mobile devices rose 49% YoY and climbed to 60.4% of e-commerce revenue.

**Year to September**, total revenue saw an increase of 27% YoY. Accumulated EBITDA grew 15% YoY to NT\$1.2bn, ahead of the company's forecast.

#### **Performance by Business**

**Rosie Yu, CFO & Spokesperson:** In 3Q, **consolidated revenue, benefiting from our diversification, decreased by 2% YoY**, with momo's revenue growth largely offsetting the declines in other businesses.

While momo's operating costs went up arising from its expanding business scale, reductions in mobile commission and handset subsidies kept our consolidated costs & expenses stable from a year ago. As a result, our **pre-IFRS 15 EBITDA saw only a 3% YoY decline.**

On the other hand, downward adjustments to 3Q EBITDA under IFRS, which had no cash flow impacts, were enlarged by NT\$415M from a year ago due mainly to capitalized commission amortization. This caused the **reported EBITDA YoY** decline in the quarter.

#### **Results Summary**

**Year to September**, our revenue was 4% lower than the Company's expectations, owing to the \$499 unlimited offers in the market. That said, through relentless efforts in cost and expense rationalization, both our operating and net income are on track to meet company guidance.

Separately, our **year-to-3Q reported net income**, inclusive of handset bundle sales and the capitalization of commission accounting treatments, showed a 10% YoY decrease. As such, this reported net income decrease does not reflect our year-to-date 3% YoY rise in pre-IFRS telecom EBITDA and the 7% growth in free cash flow.

### **Balance Sheet Analysis**

Now let's move on to balance sheet analysis.

On the **asset front**, the major YoY change seen in 3Q was the reduction in other current assets and the increase in concession. The YoY drop in other current assets was because of the reductions in guarantee deposits this year, while the concession increase resulted from the spectrum acquisition on the 2.1GHz frequency band in 4Q17.

On the **liability front**, our current liabilities decreased from a quarter ago due to the payment of NT\$15.24bn in cash dividends in 3Q, leading to a QoQ rise in current ratio.

On the financial ratios, **net debt to EBITDA** in 3Q rose sequentially to pay dividends through bank borrowings, but the ratio remained similar to last year's level. Also, our **ROE** at the end of 3Q still stood above 20%.

### **Cash Flow Analysis**

In 3Q, **operating cash inflow** remained stable compared to a year ago.

**Investing cash outflow decreased YoY** mainly due to a higher capex one year ago and the NT\$1bn deposit we made in 3Q17 to the regulator related to the 1.8 and 2.1GHz spectrum auctions in 4Q17.

**On the financing front**, a total of NT\$7.72bn in short-term borrowings was raised in the quarter to fund the NT\$15.24bn cash dividend payments.

**Net net, accumulative FCF** netted NT\$15.8bn, up 7% YoY and translating into an annual FCF yield of 7%.

Let me turn the presentation over to James for awards and recognition and key message.

### **Awards and Recognition**

**James:** Next page lists the recognitions we've received in the 3rd quarter of 2018 for your reference. I would like to make mention of the 1<sup>st</sup> line item where TWM was selected for the 2018 Dow Jones Sustainability World Indices and #1 in global telecommunications, which is quite an achievement for TWM.

### **Key Message**

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

- Growing e-commerce business as well as cross-selling among telecom, content, and internet services to stimulate higher spending per customer is our focus.
- The fast growing momentum of the enterprise segment, including the IoT, cloud, and ICT businesses, bring additional promise for future telecom revenues.
- Rationalizing costs and optimizing efficiency to ensure steady streams of cash flows remain our commitment.

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

### **Q&A**

**Patrick Chen, Nomura: I have a question regarding your enterprise business. Do you have a rough breakdown of the cloud, IoT, and ICT part of the business? How much does the aggregate of these three account for your total business? How would you expect the rollout of 5G services to expedite the growth for the enterprise business?**

**James:** The cloud business mainly consists of cloud value-added services for the enterprise sector. And, with regards to IoT, we saw strong growth from the connected car business as well as the metering business for the government sector. Starting this year, the government has started to install smart metering for water, gas, and electricity. Thus, quite a few big tenders have come out and TWM has done quite well securing a significant number of those tenders. With ICT, it's mainly related to system integration for the enterprise sector as well as the government sector.

In this coming year, when the pre-5G construction really starts picking up, I expect cloud and IoT to be fast-growing businesses. For ICT, a major factor is the big government tenders. For

example, in the beginning of this year, TWM and two other partners won a government tender for an AI platform for the National Computing Center and that will be finished by the end of this year. So, if everything goes smoothly, the ICT revenue will go up in 4Q largely because of this project. Overall, since the government has been very aggressive with its pre-5G build-out, there will be a lot of opportunities for growth in the cloud, IoT, and ICT businesses in the coming year.

Regarding the 5G spectrum auction, the government is targeting for the auction to start in 2020. Yesterday, the Executive Yuan had a meeting where it claimed that only two or three 5G licenses will be released due to limited spectrum. This will encourage the operators to form alliances to co-build or share the spectrum and network resources, which will significantly reduce the 5G infrastructure investment. In the beginning, since the 5G business will mainly be B2B, the government will initiate quite a few big tenders for the government sector. So, next year, the B2C business such as mobile connectivity will remain resilient. However, in the enterprise and government sectors, there will be strong growth.

**Patrick:** So, I'm guessing the aggregate contribution of these three on the enterprise side is still below 10% of total revenue?

**James:** The total revenue of our enterprise business group accounts for more than 10% of our revenue. The enterprise contribution is growing quite quickly.

**Jack Hsu, Sinopac:** You have just mentioned you will work with the government in the enterprise business. Can you give a view regarding what your strengths are when developing the enterprise business? Also, you mentioned the project that will take off in 4Q18, can you give us more color regarding that? What is TWM's role for this project?

**Regarding the NT\$499 plan, will you extend this type of low tariff plan in 2019?**

**James:** The tender we won is for an AI platform, GPU Nvidia platform. We foresee the AI business contributing in every sector such as government, home, individual, and in areas such as deep learning and big data. And, this platform has the capabilities to contribute a lot. Since it's a government platform, the government already decided that half of the capacity must be reserved for educational purpose. The other half of the capacity will be available for TWM and its business partners to release to the enterprise and private sectors for business opportunities. While it's a new business, I think this is a very important platform for the future growth of big data and deep learning. I'm pretty optimistic about the big data, AI and cloud platforms and these are what we will focus on next year.

In terms of the NT\$499 tariff next year, I think all the operators have learned a costly lesson with these types of tariff plans and it's my hope next year we will see the end of these types of plans.

**Jack:** The NT\$499 seem to come from two smaller operators as a means to stimulate their business in the beginning. But then the big 3 started offering similar plans. Thus, do you think the two smaller operators will feel compelled to continue to offer these types of plans into 2019?

**James:** The NT\$499 didn't start from the two smaller peers. In fact, those operators have offered NT\$288, NT\$388 plans from day one and it didn't have any effect on the market. The NT\$499 plans started from the bigger operators. Before, the NT\$499 plan operated below the line for the enterprise sector. But, suddenly when it operates above the line, there is chaos. Frankly said, we don't worry about the low tariff plan competition from the smaller players because they have been launching low tariff plans since day one and it never affected the competitive landscape.

**Jack:** What kind of impact do you think the new iPhone will have in 4Q18 and even 1Q19?

**James:** The iPhone does help the operator to raise their ARPU because most subscribers who got the iPhone subscribed to a higher tariff such as above NT\$999 or NT\$1,399. It's still too early to say, but the new iPhone at this point is not selling as well as we expected because the initial supply of the iPhone XR was not sufficient enough. Once the supply increases, the sales will have a chance to get a boost. But right now it's a little bit slow.

**Varun Ahuja, Credit Suisse: Regarding the government projects, I want to understand the market share dynamics. For example, if, in a particular quarter, the government comes out with an order of \$100, how much market share are you capturing compared to your competition especially CHT, who has a much better fixed-line network coverage, or does the coverage not make a difference when you bid for these government projects?**

**Can you elaborate a little bit more on the monetization abilities of the myVideo service? Is it currently given free with the broadband customers or are you charging for your mobile customers? I just wanted to understand how the monetization is happening on this myVideo service.**

**Lastly, momo's EBITDA margins slipped this quarter. Is it because of competition from Shopee? The revenue growth was good, but the EBITDA growth was muted because of margins.**

**James:** myVideo has been a successful product for TWM. We already have close to 5 million registered users and our MAU is close to 2.5 million. Also, it has the highest number of paying subscribers in the Taiwan OTT market. In fact, myVideo's paying subscriber base is even higher than iQiyi's. Currently, myVideo's revenues and profitability have actually exceeded our expectations. Right now, the key is how to bundle myVideo services into our fixed broadband business and our mobile broadband business because myVideo increases the stickiness of the mobile broadband and significantly increases the fixed broadband business. Uniqueness of this product is that myVideo is not only available on mobile devices, but also available at home through the cable set-top box. And we just found that household customers are more willing to pay for content, which has led to significant increases in paying subscribers and revenue. And we will work with our cable partner, Kbro, to speed up the sales of these bundles, which will benefit both parties. In terms of monetization, I think we are doing extremely well with myVideo and fixed broadband.

Regarding government projects, according to the media, the government has stated that, in terms of 5G, AI and IoT will be the main focuses of strategic investments in the coming 2, 3 years. Thus, in 4Q18, there will be many government tenders coming out for next year. Along with the AI platform and IoT businesses, the cloud business is also booming. The growth of the cloud business comes from the demand of the enterprise sector such as the gaming industry, financial sector and even live broadcasting, which is very hot in Taiwan and the rest of Asia right now. I expect the cloud business' growth rate next year to be even higher than this year.

**Rosie:** Regarding momo's competitive strategy for growth, if you look at the numbers year-to-date, their growth margin has declined by roughly 0.8%. So, to grab more market share, their strategy is to squeeze out those smaller players and major competitors by enlarging their market share at the expense of their margins and that's been already reflected in the numbers.

I think Shopee's impact is not very visible at this stage because momo is very strong in their B2C business and we believe their strategies will pay off in the long term.

**Amber, Yuanta: What are the margins like in the enterprise segment compared to your aggregate margin? With the revenue of the business getting higher, now with over 10% of the top-line contribution, how should we look at the trend of the margins? Is it more**

**like a growth trajectory or the other way?**

**James:** For the first question, the profit margins for the customized enterprise solutions are, in general, higher than those of the consumer segment. Right now, the competition in the B2C business is very keen and thus the margins are lower as what we expected. In the enterprise sector, what we have to offer is not a product, we have to offer a solution. For example, with IoT in the government sector, we have to build an ecosystem and work with our strategic alliances partners to offer solutions to the enterprise sector. Next year, we expect the enterprise segment will contribute more not only in the revenue side, but also in the EBITDA side.

**Jack Hsu, Sinopac: What is your capex plan for 2018 and 2019 in terms of amount and what areas of the business?**

**Rosie:** The 2018 capex has already been disclosed in our guidance. The 2019 will be disclosed early next year, probably end of January after our board meeting.