Taiwan Mobile 2Q09 Results Conference Call

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Rosie Yu, Finance VP & Spokesperson: Good afternoon, ladies and gentlemen. Welcome to our 2Q results release. Harvey will share the meeting. Let me turn this over to Harvey.

Harvey Chang, CEO & President: Good afternoon and thank you for attending this conference call. We are going to present our 2Q results 2009 and, before we begin our presentation, let me state:

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Results Summary

With this statement, we will begin our presentation. If you turn to the slide of result summary, as you can see that we met our 2Q revenue guidance primarily due to we have better-than-expected performance from our HBG.

Despite the lack of revenue in telecom, particularly voice service, our 2Q09 EBITDA surpassed the guidance, this is primarily due to marketing expense control and network cost management. 2Q selling expense came in 12% lower than our guidance.

On the non-operating items, as network consolidation was slightly behind schedule, our asset write-off is NT$384mn, which is lower than our original projected NT$435mn, meanwhile we still maintain our full-year write-off number to be around NT$1.6bn.

To sum up, 2Q09 net income reached 102% of our guidance. And net profits for the first half of this year totaled NT$6.86bn, representing NT$2.31 in EPS, which is reaching 50% of our full-year target.

2Q Divisional Performance

If you go to the next page, which gives you the performance of our three major business groups, the biggest continues to be our CBG.

CBG staged a sequential improvement in EBITDA margin in 2Q09 based on continuous expense control coupled with gradual revenue recovery.

EBG's EBITDA in 2Q09 was up YoY basis, which is up around 8%, this primarily due to savings from advertisement, customer service, and personnel expense.

HBG posted the highest YoY EBITDA growth, which is around 15%, amongst three business divisions. This is primarily due to very impressive growth from our cable broadband services, actually on YoY basis, cable broadband, in terms of subscribers, grew 40%. And our additional revenue from content aggregation business also helped to boost up our EBITDA.

Wireless Peer Comparison

The next page is a quick comparison with our peers primarily on the wireless communication side. You can see, our mobile subscriber number rose 2.7% YoY, coming largely from 114K data card subscriber additions.

In terms of mobile EBITDA, EBITDA margin and total subscriber number, widening the gap between TWM and our closest competitor as shown in this chart. As you can, in the 2Q our EBITDA margin reached 43.5% while our competitor falls to 39%.

VAS and 3G

The next page talks about non-voice services as far as 3G. Our VAS revenue growth was 26% in 2Q, this is the most pronounced among the three major operators. This was mainly aided by 69% revenue increase in mobile internet. In 2Q, revenue from data card users went up to 16% of total data revenue, vs. 3% a year ago.

Our 3G post-paid subscriber number in 2Q09 exceeded 2.7m, up 66%YoY, and making up 49% of total subscriber base. And our 3G data revenue was up 1.2 times from a year ago.

And also you look at our 3G devices adoption now, 41% are adopting 3G devices, this is up 2x on YoY basis. These are fairly satisfactory results.

And now, with a quick summary of business performances, I will turn the mic to Rosie to talk about our financials.

Balance Sheet Analysis

Rosie: The 2Q09 cash level rose sequentially from the previous quarter on the back of stable operating cash inflows if you look at our balance sheet analysis.

Net PP&E balance at the end of 2Q09 was down sequentially. The 2G's net book value was reduced to NT$19.02bn as of the end of 2Q09.

On the liability side, gross debt reduced to NT$15.5bn from NT$16bn a quarter ago, because we paid down NT$0.5bn of short-term borrowings. Other current liabilities increased QoQ in 2Q, largely from NT$14bn cash dividend payable which was paid on July 24.

We had NT$12.37bn capital surplus and NT$13.94bn legal reserve on our balance sheet, which could be the source of cash dividend for the future if Taiwan's legislation passes the revision of the Company Act. Additionally, we had NT$2.27bn un-appropriated earnings and NT$3.35bn special reserve, which had been used partially to top up our cash dividend received in July this year.

Cash Flow Analysis

If you look at our cash flow analysis on the next page, our main operating cash flow in the quarter was affected by the payment of corporate income tax, which was none event in 1Q09. Cash payment of corporate income tax in 1H was a result of taxable income of the previous year. Taxable income in 2008 is higher than that in 2007 because of the huge asset write-down in '07, this resulted in lower operating cash inflows in 2Q09.

On investing cash flow, it was mainly for capex.

In terms of financing activities, we repaid short-term borrowings of NT$0.5bn in this quarter as previously mentioned. NT$0.36bn cash inflows were from the sale of treasury shares to employees in 2Q09.

I will turn this over back to Harvey for 3Q forecast.

3Q09 Forecast

Harvey: Let's look at our 3Q forecast number. Our mobile and cable related service revenue is expected to edge up sequential basis, containing YoY revenue drop in 3Q09.

Adding in content aggregation cost to 3Q guidance, our cash cost will trend up to reflect higher revenue and utility cost of base stations. That being said, cost will be down YoY due to network cost management.

On the expense front, we expect to sign up more new subscribers in 3Q, leading to a QoQ rise in selling expense. However, we will continue our SG&A expense control to achieve our 3Q EBITDA target.

Our main non-operating item in 3Q is expected to be NT$387m in asset write-off.

Event/ Regulatory update

Next page just gives you an event update on the regulatory front and peer update.

The first one is the China Mobile – FET deal. So far, we have not seen any sign that the Taiwan's authority is going to approve it.

The second is on our fight with CHT on the IP peering price. CHT has finally agreed to lower the price of IP peering, which is retroactive from January 2009. That will help us manage our cost.

The cabinet has proposed a revision of Company Act, by lowering the structure of dividend distribution from capital surplus and legal reserve; this is subject to approval by our legislative body.

The Legislative Yuan passed the Income Tax Act to reduce corporate statutory tax rate from 25% to 20%, effective 2010.

And continue to next page on awards and recognitions. There is a survey done by *Business Next* Magazine here in Taiwan and *Business Week* in the US, they have done a survey called "Info Tech 100 Taiwan" and TWM was ranked #6 in this survey. We are certainly way ahead of our other telecom rivals.

From Reader's Digest, for the sixth year in a row, we received the "Gold Trusted

Brand" award.

Key Message

Our key message for this quarter is, with on-going economic recovery, Taiwan Mobile's revenue is expected to be stable. Continuous growth in mobile value-added service, driven largely by data cards, and our expanding HBG business, particularly in cable broadband and content aggregation, together with discipline over spending is expected to help meet our 3Q guidance. We remain optimistic on this.

Q & A

Anand Ramachandan, Citicorp HK: ***First, CHT's 3Q guidance did come as a surprise to the market and it talked about much higher handset subsidies for the 3Q. Does that mean the market environment could worsen and any assumptions related to that reflected in the 3Q guidance of yours at all?***

2nd question on the cabinet proposal to lower the threshold of dividend distribution, capital surplus and legal reserve, if that passes does that change the way you think about capital management? I ask simply b/c you already have enough buffer to pay on top of what is a solid ?, does that you have some incentive to pay out more? Does that really change anything for that one mobile because the buffer was already there?

My 3rd question is on taxes, as taxes went from 25% to 20%, should we look at all the benefit change through to the PnL or there something else you should be aware of in terms of any deferred credits or liabilities?

Harvey: On the CHT 3Q guidance, we have quickly caught own attention that they have posted a much higher handset subsidy. I can certainly tell you we don't intend to follow them. For them, I think they have made a lot of commitments to vendors. I think there are certain pressures on CHT. And, as usual, really believe in market share, market power and they have to pay a price on that.

Secondly, on the dividend distribution, it is true that once the new law has been passed, we do have more buffers and it might change how we look at capital management if we have this buffer. But, right now we don't have any specific thoughts in terms of how we're going to do this. But it certainly gives us more flexibility in terms of cash dividend payout.

Third one is on tax, so maybe Rosie can talk about that**.**

Rosie: It will lower our cash expense from next year on; but, for this year there might be some impacts because of the lower rate upcoming starting next year, but the impact will be mitigated by some of our tax buffer which we have reserved already. So, the impact will be minimal.

Harvey: For this year.

Rosie: Yes, for this year.

Harvey: From next year on, then it's more positive.

Anand: *And, just to confirm, in your 3Q guidance, life is normal. It does not assume a more competitive market because CHT has something.*

Harvey: I think yes and no. Actually, we look at this handset market a little bit differently. We still felt there are clear segments in terms of customer preference for handset. CHT is primarily trying to shift more people from the middle tier to higher tier handset segment. That's why they are increasing subsidy. And this is not going to be easy.

Tim Story, JP Morgan: ***I want to touch on the state of the cable industry in Taiwan, discussion in the past on possibly acquiring on more assets have definitely happened, but it's been very hard to see a deal. I'm just wondering given the environment that we're now in, which is hopefully a recovery environment, does that make it even more difficult for you to have expectations of being able to acquire further cable assets? Just what's your confidence to execute on a cable transaction?***

Secondly, if you are not able to acquire cable assets, what's your strategy in terms of the treasury shares? Is there anything differently that you would do if you felt there was no chance of doing an acquisition?

More of an operational question, is it possible to get a breakdown of capex for this year in terms of where the money is being spent?

Harvey: The economic recovery does change the outlook for cable industry revenue. But, we are still optimistic in terms of our ability to complete the transaction. We cannot tell you too much about it, but we are not at such a stage that we have to consider other alternatives for our treasury shares.

On the third one, Rosie can you please.

Rosie: I'll give you the breakdown of CAPEX. NT$4.7bn will be earmarked on mobile business, NT$1.2bn for enterprise business and NT$ 0.6bn for cable business.

Tim: *If I go back to the 1st two questions to follow on, is there anything on the regulatory front, things like the market share cap, for example, that maybe revisited by the government and may make transactions more justifiable that you feel that's a very likely scenario over the next year or two in terms of regulatory changes that are at all out there?*

And, secondly, I'm curious on what your thoughts on FET's revenue diversification strategy, which seems to be buying into China-based VAS companies and albeit the relationship with China Mobile is there on the one hand, but that's not necessarily a requirement to do those types of investments and can you comment on TWM interest in doing something outside of Taiwan perhaps along the lines of FET or something completely different?

Harvey: Regulatory change will offer a more of a level playing field in terms of competition. I think, as far as we are concerned, we would love to see the change taking place, but we are not dependent on this change to happen for us to go ahead with our plans.

As far as FET is concerned, we try not to make comments on our competitors. We're not in the business of pleasing them, but we also don't try to be in the position of offending them.

Tim: *Do you want comment on the interest level you may have on making acquisitions outside of Taiwan?*

Harvey: We have actually looked at several markets in the past and did not find anything appealing. We still remain interested but would be selective in making investments outside Taiwan.

Tien Doe, GIC Singapore: ***Just one question regarding the IP peering rates, would you be able to tell us what the rates that CHT has agreed now vs. the old rates and what would the financial impact on TWM?***

Harvey: We had a NDA among us, that's one of the terms when they finally agreed to a more favorable rate. I'm afraid I can not give a specific number, but it's helpful. It will not make us rich, but is helpful in terms of maintaining our cost.

Kathy Chen, Goldman Sachs: ***First, on the 3Q guidance, can you give some breakdown in terms of revenue among the 3 different segments and where we're seeing more improvement in terms of YoY or QoQ growth?***

Secondly, in terms of the recent StarTV agreement, could you talked more about your content aggregation strategy going forward? How should we expect the amount of content aggregation you do evolve over time?

Lastly, on the digital TV side, can you give an update on the rollout and, looking a few years out, when can we expect the revenue to become more meaningful?

Harvey: Let me talk about StarTV, content aggregation as well as the digital TV. These are primarily our content business. We are quite happy that we have finally reached an agreement with people in HK to be agent for StarTV. As far as overall content aggregation strategy is concerned, we in the past were not a significant player in the content aggregation business. But starting this year, we decided to shift gears and we are going to be more active and want to be a significant player in the content aggregation business, so StarTV is the first step that we are able successfully to conclude. We will strive to win more content aggregation agency from other content players. So, that will give us a more competitive position in terms of these cable TV services. On the digital TV, we launched a service on July 1 in two of our service areas. We will launch (in) the other three in September. The 1st month of July, I would say "so far, so good". We see some favorable response from our cable TV subscribers. It will take awhile to build the momentum up.

Rosie: On the revenue guidance for the 3Q, we expect to see the growth coming from wireless broadband and cable primarily. The mobile revenue is expected to go up by 1% q/q while VAS by 28% y/y. So, these are our expectations.

Kathy: *Is fixed line during the quarter or EBG increasing YoY in the quarter or decreasing?*

Harvey: I think EBG is on the flat to upward trend.

Neil Anderson, HSBC HK: ***Three queries related to the data card growth that TWM is seeing. Firstly, on the subsidy-side, are you more focus on smartphones or wireless broadband data card connections in the 3rd quarter?***

Secondly, specifically on wireless broadband, are you seeing more interest in netbook bundles or stand-alone data cards?

Finally, obviously there is quite a bit of growth coming through from this service, are you seeing a material impact on both radio capacity and backhaul as a result of the growth of wireless broadband?

Harvey: Primarily, I see that because we took a lead on providing netbook to our customers, that have really helped us to build up the momentum. And, so far, I tend to think because our strategy to subsidize the netbook has won a lot of customers, we expect the trend to continue for a while. Rosie, do you have anything to add?

Rosie: On the data card issue which affected our radio capacity, that will increase our burden a bit, we have already started changing our backhaul to be more IP based to lower the burden.

Harvey: We have a 2 year plan to restructure our overall backhaul, try to use more IP transmission then the traditional ATM type of transmission. And that plan is ongoing. And it's a part of our network cost management program.

Neil: *To follow up on my first point, I guess, was regarding subsidies, do you see more of that going towards data cards and netbooks or is it really a handset focus in the 3rd quarter?*

Harvey: Netbook has accounted for a significant part and will probably continue that way.

Arthur Pineda, RBS Singapore: ***With regards to your guidance, given the likely increase in subsidies by CHT in the 3Q, don't you see pressure to match this on the***

part of TWM unless you want to face subscriber migration? Has this been factored into your margins as well?

With regards to the cable acquisition, is there a deadline for you to walk away from the deal and actually explored other areas of investment or cash return?

Harvey: I think we're foolish to set a deadline for us to do that. So, there is no deadline. We have already talked about subsidy. Basically, we look at the thing a bit differently. We tend to think that there are clear customer segmentations. So, we are not going to copy what CHT is doing.

Arthur: *So, you're not too concern that there might be some migration as a result of them trying to migrate customers?*

Harvey: Yeah, there will be, but we will try to use other marketing scheme to counter that. We are not going to copy what they are going to do; that is to dramatically increase handset subsidy.

Shirley Tse, UBS HK: ***Just want to confirm on your forecast that the StarTV aggregation is not w/in the Q3/4 forecast right now and if we add that in, that would be pre-div to both the EBITDA and revenue for your Q3 numbers.***

Sounds from your answers earlier that you are looking into become a bigger player in the content aggregation side and I recall that one of the key rationales for doing a cable acquisition in the past was that you wanted to derive more synergy from maybe content cost savings, does that mean that if you succeed from this new strategy that the priority in terms of doing cable acquisition could come off?

And, thirdly, on the better margins from lower selling expenses, how much of that was due to a subscriber as coming in lower than your expectation vs. a lower customer acquisition cost per sub?

Harvey: Ok, let me be brief to your answers, the 1st question is yes, the 2nd question is no and the third question is also no. (laughs) Of course, I think we try to exercise some discipline in terms of acquiring customers. It's really how we'll manage our customers. The churn managmenet, we do a better job.

Shirley: *As follow up to the 1st question, if the margin on the StarTV business, will* *you be able to give us some color on that, is that quite low compared to your overall margin?*

Harvey: Of course, of course. Do you think we are highway robbers of that? (Laughs) No, we can't do that. It is not an affect margin business, but I think it helps us to position ourselves in the market place.

Rosie: Shirley, on the selling expense, the quantity decline is about 11% q/q and the price decline is about 10%.

John Kim, Merrill Lynch Korea: ***First, regarding your macro outlook, if the macro conditions improve, would it be fair for us to expect TWM's operating profit to recover some expense next year or do you feel like other factors such as competition intensifying that this is going to offset your earnings recovery and we can not expect a meaningful rebound? I'm not looking for a number, but some guidance and direction would be very helpful.***

If you can just provide some rough guidance or idea on your asset write-off for the next year or two, that would be great.

Harvey: All of this is probably going to be quite vague. Our operating structure remains status quo; meaning there was no significant acquisition that concluded. I don't think you will see a significant rebound in operating profit. Operating profit did not drop that much because of the slowdown in the economy in the first place. Since it didn't drop that much, we don't see the potential of rebound as well. And then, on the asset write-off, at this point, we don't see a significant change from this year.

Helen Gee, Goldman Sachs HK: ***Following up on John's question regarding the economic recovery, you said in the presentation that as the economy improving, the revenue is expected to stabilize. Looking at the some of the monthly data, the MOU has been reasonably stable and the main reason why there has been some revenue pressure on the mobile side seems to be just that the price per minute has declined pretty significantly since 12 to 18 months ago. Do you think that's a function of competition or a function of economy recovery? And do you expect at the current level of NT3.2, NT3.3/ minute that this is reaching some kind of stable level so that if you did have some additional data ARPU contribution that it would drive an inflection point in your mobile revenue?***

Harvey: The drop in revenue per minute is primarily a reflection of the competition. I think it is stabilizing, but I don't see a significant inflection point that we are going to grow as quickly.

Helen: *Are you starting to see some signs that the overall usage, the MOU, is increasing b/c of the economic recovery?*

Harvey: Slightly.

Helen: *You also mentioned the VAS contribution, contribution from data cards, netbooks, etc. since you're being more aggressive on that than some of your competitors, what do you think is a reasonable target for your data ARPU contribution to revenue in the next one or two years? And are you targeting to get to a higher percentage than FET?*

Harvey: Certainly that is the goal.

Helen: *But do you think 15% or high teens is a realistic one-to-two year target?*

Rosie: Helen, according to growth pace of close to 13% in data, it's close to 15% this year already.

Helen: *So you do expect that the rate continue, right?*

Rosie: Yes.

Helen: *Are you seeing that the payback period on the subsidy for the data cards and netbooks is comparable to the normal handset? I'm talking about subsidy as percentage of the committed revenue. I understand that duration of the contract is longer, like, three years instead of two. But are you seeing that the subsidy divided by the committed revenue over the three years, that ratio is higher, lower or similar to what you would be seeing for the handsets?*

Harvey: I think the ratio is slightly better than what we did on the voice side.

Helen: *Ok, so slightly lower. Finally, if you do expect data revenue will continue to grow at that kind of pace, do you think there are any kind of risk you have to* *increase your capex budget in order to meet some of the demands of data taking up much more of the capacity?*

Harvey: Not significantly, as I have just mentioned. We're looking at our overall core network. Actually, we have several programs going all-IP and then we're also looking at other possibility. I think all these programs are meant for us to minimize our CAPEX as well as OPEX.

Maybe I should also mention, at the end of the week, our current CTO is going to retire. And we actually have James Cheng, who is head of HBG and has strong technical background, concurrently acting as the CTO. I expect James will make more contribution to how to restructure our network.

Moderator: Rosie, there seems to be no further questions at this point.

Harvey: Ok, ladies and gentlemen, thank you very much for attending this call. We will see you next time on the phone. Thank you.

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