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TWM Consolidated

NT\$bn	<u>3Q17</u>	<u>2Q17</u>	<u>3Q16</u>	<u>QoQ</u>	<u>YoY</u>
Revenues	28.76	27.80	28.45	3%	1%
EBITDA	8.26	8.30	8.57	0%	-4%
Operating Income	4.82	4.89	5.09	-1%	-5%
Non-op. Income (Expenses)	(0.09)	(0.08)	(0.13)	20%	-27%
Pre-tax Income	4.73	4.82	4.97	-2%	-5%
(Income Tax)	(0.62)	(0.78)	(0.84)	-21%	-27%
(Minority Interest)	(0.15)	(0.21)	(0.14)	-27%	10%
Net Income	3.96	3.83	3.99	3%	-1%
EPS (NT\$)	1.46	1.40	1.46	4%	0%

Highlights of Operating Results
3Q17

In 3Q17, mobile device sales, telecom service revenue, CATV revenue, and momo revenue all trended up from the previous quarter. Our net income in 3Q17 beat our expectation by 6%, despite higher operating costs and expenses resulting from the QoQ increase in revenue. Separately, 3Q17 EPS rose 4% QoQ on the back of the sequentially improving business momentum and one-off investment tax credits.

1-3Q17

For the first nine months, momo's revenue is ahead of expectations and CATV revenue is on track. Nevertheless, mobile device sales for the period came in below expectations due to a lower take-up of high-end phones and rate plans during the period.

With expense discipline, lower-than-guidance voice traffic costs, and handset subsidies, our accumulated operating income achieved 105% of our guidance for the first three quarters. Year to September EPS of NT\$4.32 stayed resilient from a year ago and reached 82% of our full-year target.

Key Message

The end of 2G service and the expected rational pricing of the government's licensing of the 1.8/2.1GHz spectrum will alleviate pressure on our depreciation. A more benign cable industry outlook coupled with the potential revenue acceleration aided by the completion of momo's automated distribution center is expected to continue bolstering our profit growth.

Free cash flow stability and exploring service/product differentiations remains our main areas of focus. The new bundled iPhone8/X offerings with the monthly fee adjusting upward to a minimum of NT\$1,399 for unlimited data usage should bode well for healthy industry growth.

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I. Revenue Analysis

Table 1. Key Operational Data

Residual Value (NT\$bn)	3Q17	2Q17	3Q16	QoQ	YoY
Mobile Service Revenue	15.57	15.62	16.62	0%	-6%
Postpaid ARPU (NT\$)	848	842	885	1%	-4%
Blended ARPU (NT\$)	707	707	742	0%	-5%
Telecom Service Revenue	16.69	16.71	17.75	0%	-6%

Revenue (NT\$bn)	3Q17	2Q17	3Q16	QoQ	YoY
Telecom	19.07	18.46	20.01	3%	-5%
- Service	14.47	14.43	15.41	0%	-6%
- Device Sales	4.60	4.03	4.61	14%	0%
CATV	1.63	1.60	1.63	2%	0%
- Pay-TV Related	1.08	1.06	1.08	2%	0%
- Broadband	0.34	0.34	0.33	2%	5%
- Content & Others	0.21	0.20	0.22	4%	-5%
momo	8.02	7.69	6.76	4%	19%
- E-commerce	6.47	6.00	4.95	8%	31%
- TV Shopping & Others	1.55	1.70	1.81	-8%	-14%
Others¹	0.15	0.15	0.13	0%	12%

Note 1: Other revenue primarily consists of operating revenue from 49.9%-held Taipei New Horizon Co., Ltd., which became a consolidated entity on Feb 21, 2014.

	3Q17	2Q17	3Q16	QoQ	YoY
Mobile Subscribers (K)	7,324	7,340	7,479	0%	-2%
- Postpaid	5,832	5,868	5,974	-1%	-2%
Monthly Churn	3.0%	3.2%	2.6%		
-Postpaid	1.7%	1.7%	1.6%		
MOU (bn)	1.73	1.82	2.57	-5%	-33%
Pay-TV Subs (K)	584	583	582	0%	0%
Cable Broadband Subs (K)	212	208	202	2%	5%
DTV Subs (K)	220	214	196	3%	12%

CATV ARPU (NT\$)	3Q17	2Q17	3Q16	QoQ	YoY
Basic TV	466	467	470	0%	-1%
Broadband	529	530	530	0%	0%
DTV	123	124	127	-1%	-3%
Blended ¹	811	800	804	1%	1%

Note 1: Cable TV & broadband related revenue (excluding content agency) divided by CATV subscriber number

Telecom:

In 3Q17, telecom service revenue remained stable QoQ, but dropped by 6% YoY, primarily due to falling mobile MOU and a diminishing domestic roaming business. Excluding domestic roaming, the YoY decline in telecom service revenue narrowed to 3.7%, outperforming our peers on a like for like basis.

As TWM's product differentiation strategy and value added services have taken hold, TWM's postpaid ARPU recovered by 1% QoQ in 3Q17. Excluding domestic roaming, postpaid ARPU declined by 1.7% YoY, compared with a 2.5% decline in 2Q17.

In 3Q17, device sales increased by 14% QoQ thanks to a sufficient supply of the iPhone 8 upon its launch in September.

TWM's mobile subscriber base declined 2% YoY this quarter, mainly owing to the termination of its 2G service. Separately, market competition became tepid at the quarter end with Chunghwa taking the lead in lowering dealer commissions.

Cable:

The cable industry dynamics in New Taipei City has become relatively favorable. Also, the launch of the Sharp TV bundle plan as a differentiating factor in September has levelled up TWM's CATV subscriber growth and blended ARPU. As such, in 3Q17, CATV revenue registered its first yearly growth since 3Q16, and in the meantime rose 2% QoQ.

momo

In 3Q17, the e-commerce business reported a 31% YoY surge in revenue, surpassing the growth rate of its closest peer in Taiwan, and continued to serve as a growth engine for momo. As a result, e-commerce made up 81% of momo's total revenue.

II. EBITDA Analysis

Table 2. EBITDA Breakdown

NT\$bn	3Q17	2Q17	3Q16	QoQ	YoY
EBITDA	8.26	8.30	8.57	0%	-4%
- Telecom	6.98	6.95	7.26	0%	-4%
- CATV	0.84	0.83	0.87	2%	-3%
- momo	0.31	0.39	0.30	-21%	6%
- others	0.10	0.10	0.08	6%	23%
Margin	28.7%	29.8%	30.1%	-1.1ppts	-1.4ppts
- Telecom	36.6%	37.7%	36.3%	-1.1ppts	0.3ppts
- CATV	51.8%	51.8%	53.3%	0ppts	-1.5ppts
- momo	3.9%	5.1%	4.4%	-1.2ppts	-0.5ppts
- others	70.3%	66.5%	64.2%	3.8ppts	6.1ppts

D&A	3.44	3.40	3.48	1%	-1%
- Telecom	3.04	3.04	3.14	0%	-3%
- CATV	0.27	0.24	0.22	13%	22%
- momo	0.03	0.03	0.03	15%	19%
- others	0.05	0.05	0.05	0%	1%
EBIT	4.82	4.89	5.09	-1%	-5%
- Telecom	3.93	3.91	4.13	1%	-5%
- CATV	0.57	0.59	0.65	-3%	-11%
- momo	0.28	0.37	0.27	-23%	5%
- others	0.05	0.04	0.03	13%	58%

Note: The sum of each account of telecom, CATV and momo does not equal to the consolidated total number due to other revenue and minor adjustments / eliminations.

Table 3. Non-operating Item

NT\$bn	3Q17	2Q17	3Q16	QoQ	YoY
Non-Operating Revenues (Expenses)	(0.09)	(0.08)	(0.13)	20%	-27%
- Net Interest Expense	(0.11)	(0.10)	(0.13)	7%	-14%
- Write-off Loss	(0.07)	(0.04)	(0.04)	93%	78%
- Other Revenue (Expense)	0.09	0.07	0.05	41%	102%

EBITDA Analysis

Negatively affected by drops in domestic roaming and mobile voice revenue, telecom EBITDA decreased YoY in 3Q17. However, aided by continuous cost-control efforts, TWM successfully maintained a stable telecom EBITDA sequentially, even with a higher sales mix toward device sales. As such, telecom EBITDA improved by 2% YoY on a recurring basis excluding domestic roaming.

CATV business has showed signs of stabilizing. With a recovery in revenue, CATV EBITDA grew 2% QoQ in 3Q17. The CATV EBITDA YoY decline also became much milder, compared to one quarter ago.

In 3Q17, momo's QoQ contraction in EBITDA was mainly due to weak demand in its TV home shopping business, which has higher fixed costs. Revenue growth in e-commerce, particularly in consumer electronics, and the process of shifting from leased warehousing to newly-built automated distribution center weighed on its EBITDA margin in 3Q. That said, momo's strong revenue growth momentum more than compensated its margin dip and resulted in a healthy 6% YoY rise in EBITDA in 3Q.

D&A Analysis

The expanding digital set-top-box installed base (100% by 2017 year-end) led to an increase in CATV depreciation expenses. Nonetheless, total consolidated D&A edged down 1% YoY in the quarter, benefiting from the retirement of the 2G network.

Non-Operating Item Analysis

3Q17 non-operating expenses decreased YoY mainly due to lower interest expenses on the back of lower average loan balance and lower valuation losses of financial assets.

III. Income Statement Analysis

Table 4. 3Q17 Consolidated Results vs. Forecast

NT\$bnn	3Q17	QoQ	YoY	% of 3Q17 Forecast
Revenues	28.76	3%	1%	97%
Operating Costs	(19.80)	5%	4%	97%
Operating Expenses	(4.14)	4%	-4%	92%
Operating Income	4.82	-1%	-5%	105%
Non-op. Income (Expenses)	(0.09)	20%	-27%	74%
Pre-tax Income	4.73	-2%	-5%	106%
Net Income	3.96	3%	-1%	106%
EPS (NT\$)	1.46	4%	0%	106%
EBITDA	8.26	0%	-4%	102%
EBITDA margin	28.7%			

In 3Q17, mobile device sales, telecom service revenue, CATV revenue, and momo revenue all trended up from the previous quarter.

In the quarter, operating costs and expenses also went up sequentially due to the QoQ rise in revenue.

3Q17 amortization edged up from 2Q as we had gained access to an incremental spectrum in the 1.8GHz frequency band.

Non-operating expenses increased QoQ as we incurred 2G asset write-off losses after the end of the service in 3Q17.

3Q17 EPS rose 4% QoQ on the back of the sequentially improving business momentum and one-off investment tax credits. Separately, net income for the quarter came in 6% higher than expectations with cost savings more than offsetting revenue shortfalls.

Table 5. 1-3Q17 Consolidated Results vs. Forecast

NT\$bnn	1-3Q17	YoY	% of Full Year Forecast
Revenues	85.41	-1%	72%
Operating Costs	(58.36)	1%	71%
Operating Expenses	(12.26)	-7%	68%
Operating Income	14.79	-4%	80%
Non-op. Income (Expenses)	(0.34)	-30%	51%
Pre-tax Income	14.45	-3%	81%
Net Income	11.75	-1%	82%
EPS (NT\$)	4.32	-1%	82%
EBITDA	25.00	-3%	77%
EBITDA margin	29.3%		

For the three quarters, momo's revenue is ahead of expectations and CATV revenue is on track. Separately, mobile device sales for the period came in below expectations due to a lower take-up of high-end phones and rate plans during the period.

With expense discipline, lower-than-guidance voice traffic costs, and handset subsidies, our accumulated operating income achieved 105% of our guidance for the first three quarters.

Lower-than expected interest expenses benefited our profit level in 1-3Q17.

Year to date EPS of NT\$4.32 is resilient from a year ago and reached 82% of our full-year target of NT\$5.28.

IV. Cash Flow Analysis

Table 6. Cash Flow

NT\$bn	3Q17	2Q17	3Q16
Total Op Sces/(Uses)	6.98	7.87	7.89
Pre-tax Income	4.73	4.82	4.97
Depreciation	2.57	2.59	2.68
Amortization	0.86	0.81	0.80
Changes in Working Capital	(1.41)	(0.55)	(0.80)
Asset Write-off Add-backs	0.07	0.03	0.04
Other Add-backs	0.15	0.16	0.21
Net Investing Sces/(Uses)	(3.43)	(2.84)	(3.55)
Capex ¹	(2.46)	(2.43)	(3.05)
Divestment (Acquisition)	(0.08)	(0.58)	0.03
Other Financial Assets (Increase)	(0.00)	0.14	(0.66)
Refundable Deposits (Increase)	(0.99)	0.01	0.02
Others	0.11	0.02	0.11
Net Financing Sces/(Uses)	(3.75)	(6.78)	(5.31)
Short-Term Borrowings	6.70	(0.10)	4.65
Commercial Paper Payable Increase	5.00	0.00	5.50
Repayments of Bonds Payable	0.00	(2.90)	0.00
Long-Term Bank Loan	(0.14)	(3.04)	(0.14)
Dividends Payments	(15.24)	(0.62)	(15.24)
Others	(0.07)	(0.12)	(0.08)
Net Cash Position Chg.	(0.21)	(1.75)	(0.98)

1. Inclusive of prepayments for equipment and the acquisition of computer software & other intangible assets

Table 7. Capex & FCF

NT\$bn	3Q17	2Q17	3Q16
Cash Capex	2.46	2.43	3.05
- Mobile	1.48	1.28	2.18
- Fixed-line	0.41	0.24	0.29
- Cable MSO	0.26	0.57	0.26
- momo & others	0.32	0.34	0.33
% of Revenue	9%	9%	11%
Free Cash Flow	4.51	5.43	4.84

Cash Flow Analysis

3Q17 operating cash inflow decreased YoY mainly due to the negative impact of lower domestic roaming revenue, which also resulted in a mobile capex reduction. Meanwhile, the QoQ decrease in operating cash inflow was caused by changes in accounts receivable and accounts payable, which led to a decrease in net working capital.

The major investing activities in 3Q17 were a NT\$2.46bn cash capex and a NT\$1bn deposit provided to the regulator related to the upcoming 1.8/2.1GHz spectrum auctions.

On the financing front, a total of NT\$11.7bn in short-term borrowings was raised in the quarter to fund the NT\$15.24bn cash dividend payments. In 2Q17, we paid a NT\$0.62bn cash dividend to momo's minority shareholders and repaid NT\$2.9bn in corporate bonds carrying a 1.29% coupon.

Capex and Free Cash Flow Analysis

Cash capex decreased YoY attributed to lower 4G related capex spending. In 3Q17, FCF was less than a quarter ago due to lower operating cash flow. For the first three quarters, FCF netted NT\$14.78bn, translating into an annualized FCF yield of 7%.

V. Balance Sheet Analysis

Table 8. Balance Sheet

NT\$bn	3Q17	2Q17	3Q16
Total Assets	146.41	146.58	151.26
Current Assets	30.50	30.18	32.41
- Cash & Cash Equivalents	5.97	6.18	6.57
- Accounts Receivable	14.70	14.57	15.68
- Inventories	3.15	3.08	2.95
- Short-Term Investment	1.57	1.46	1.26
- Other Current Assets	5.10	4.89	5.95
Non- current Assets	115.92	116.39	118.85
- Long-Term Investment	6.22	6.47	5.54
- Property and Equipment	45.06	45.37	46.42
- Concession	35.82	36.53	38.53
- Other Non-current Assets	28.82	28.01	28.35
Liabilities	83.36	87.41	88.76
Current Liabilities	44.54	48.50	51.34
- ST Borrowings	21.86	10.16	27.82
- Other Current Liabilities	22.68	38.34	23.52
Non-current Liabilities	38.82	38.91	37.42
- Long-Term Borrowings	34.77	34.89	33.38
- Other Non-current Liabilities	4.05	4.02	4.04
Shareholders' Equity	63.06	59.16	62.50
-Paid-in Capital	34.21	34.21	34.21
-Capital Surplus	13.92	13.92	14.59
-Legal Reserve	26.14	26.14	24.61
-Treasury Shares	(29.72)	(29.72)	(29.72)
-Un-appropriated Earnings	0.63	0.63	0.63
-Non-controlling Interest	5.67	5.51	5.62
-Retained Earnings & Others*	12.21	8.48	12.57

* Including YTD profits and other equity items

Table 9. Ratios

	3Q17	2Q17	3Q16
Current Ratio	68%	62%	63%
Interest Coverage (x)	32.0	34.0	30.1
Net Debt (Cash) to Equity	80%	66%	87%
Net Debt (Cash) to EBITDA (x)	1.54	1.18	1.62
ROE (annualized)	28%	29%	28%
ROA (annualized)	11%	11%	11%

Assets

As of the end of 3Q17, cash balance decreased QoQ as explained in the cash flow analysis section.

The YoY decrease in accounts receivable was a function of a higher mix of mid-end handset bundled sales.

Both of the QoQ and YoY increases in inventory were mainly associated with the increase in momo's inventory, given the company's higher e-commerce revenue scale and its plan to increase product availability ahead of the traditional peak season.

Long-term investment increased YoY to reflect the mark-to-market value appraised on the investment in THSR (Taiwan High Speed Rail) and our increased investments into media and content made in 2Q17.

4G, CATV, and momo related PP&E increased YoY in 3Q17 for 4G capacity expansion, digital STB deployment, and momo's automated distribution center. But the overall net PP&E balance continued decreasing due to the retirement of 2G network and falling 3G equipment book value.

Liabilities & Shareholders' Equity

Gross debt balance rose to NT\$56.63bn compared to last quarter, mainly to finance dividend payments in 3Q17.

Nonetheless, other current liabilities decreased QoQ due to the NT\$15.24bn cash dividend payments made in 3Q17, leading to a QoQ rise in current ratio.

Ratio Analysis

Net debt to EBITDA increased QoQ because of raising cash to pay dividends through bank borrowings. However, the ratio in 3Q17 was lower than last year's level. Meanwhile, ROE remained at a high of 28%.

VI. Management Remarks

Key Message

- The end of 2G service and the expected rational pricing of the government's licensing of the 1.8/2.1GHz spectrum will alleviate pressure on our depreciation. A more benign cable industry outlook coupled with the potential revenue acceleration aided by the completion of momo's automated distribution center is expected to continue bolstering our profit growth.
- Free cash flow stability and exploring service/product differentiations remains our main areas of focus. The new bundled iPhone8/X offerings with the monthly fee adjusting upward to a minimum of NT\$1,399 for unlimited data usage should bode well for healthy industry growth.

Event

- Following Chunghwa Telecom's return of its 2G spectrum to the National Communication Commission (NCC) at the end of June and Taiwan Mobile's termination of its 4G heterogeneous network service for 2G users at the end of August, TWM hence has expanded its LTE 1800MHz spectrum to 15MHz contiguous. Accordingly, 4G network download speed rose sequentially since then.
- The first stage of the LTE 1800/2100 MHz spectrum auction starting October 31 has just finished, with TWM gaining 4 blocks in the 2100 frequency band at a reasonable cost of NT\$8.6bn.
- On November 1, the NCC announced a mobile interconnection rate reduction plan for voice calls, with a current upper limit of NT\$1.15 per minute call that will annually adjust downward from November 2017 to the end of 2020. Under the assumption that TWM's 2018 voice traffic will stay at similar level with 2017's, the negative impact from the new mobile interconnection rate on the company's 2018 EBITDA is estimated to be less than 1%.

Awards and Recognition

- Not only was Taiwan Mobile selected as a constituent of the prestigious Dow Jones Sustainability Index (DJSI) series for the sixth consecutive year, but this year for the first time Taiwan Mobile is listed among the companies in the DJSI World Index and is ranked 2nd among telecom companies worldwide.
- Honored with the 2017 Corporate Citizen Award from CommonWealth Magazine, the 10th Corporate Citizen Award since 2007.
- Recognized by the Sports Administration, Ministry of Education with the 2017 Sports Promoter Awards of the "Sponsorship Award Gold Class" and the "Long-Term Sponsorship Award".