



中華電信
Chunghwa Telecom

CHT 2Q2014 Results July 30, 2014 at 4:00 P.M. (Taipei Time)

Fufu: Thank you. Thank you. This is Fufu Shen, the Director of Investor Relations for Chunghwa Telecom. Welcome to our second quarter 2014 earnings results conference call. Joining me on the call today are Dr. Tsai, Chairman, Mr. Shih, President and Mr. Chen, CFO.

During today's call, management will first discuss business, operational and financial highlights then we will move on to the Q&A session.

Before I turn it over to today's speakers, I would like to remind you that a number of forward-looking statements will be made during this conference call. Forward-looking statements are any statements that are not historical facts. These forward-looking statements are based on the current expectations of Chunghwa and there can be no assurance that such expectations will prove to be correct. Because forward-looking statements involve risks and uncertainties, Chunghwa's actual results could differ materially from these statements.

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Before we continue, please note our safe harbor statement on **slide 2**. Now I would like to turn the call over to Chairman Tsai.

Dr. Tsai, Chairman and CEO:

Thank you, Fufu. Hello everyone, this is Rick Tsai. Thank you for joining our second quarter 2014 conference call.

Before getting started with recent business developments in the second quarter, I would first like to introduce to all of you our new CFO, Mr. Bo Chen. Prior to becoming Chunghwa's CFO, Mr. Chen served as Vice President and CFO of TSMC Solid State Lighting and TSMC Solar. He holds an MBA degree from the University of Pittsburgh. We are confident that his outstanding ability and robust experience will enable him to excel in the CFO role, as we strive to improve our performance in terms of finance, accounting and investments going forward.

Now, let's get back to the business' developments. Since joining Chunghwa six months ago, my team and I have made a lot of effort reviewing the company's operational strategies and promoting business development, with an emphasis on 4G, fiber broadband, MOD and the enterprise business.

We also focused on enhancing our operating and financial efficiency by reallocating and leveraging resources for the company's long-term growth.

At the end of May, Chunghwa launched 4G services and became the first 4G operator in Taiwan. We accelerated our 4G deployment and capital expenditure investment to offer users a better and faster experience, and to gain a slight advantage against our ever intensifying competition. We are confident that we will meet our year-end market share target of 40% and expect to reach more than 90% population coverage by the end of 2015.

Finally, after reviewing our capital expenditure and resource allocation carefully, we believe a lower-than-budgeted capital expenditure and higher operational efficiency will be realized this year. We will optimize handset subsidies in our smart device profile to control expenses. The resource integration among businesses will enhance the manpower and equipment utilization efficiencies.

Now, President Shih would like to lead you through our business overview.

Chunghwa Telecom Overview

Thank you, Chairman Tsai.

Moving onto slide 4, regarding our second quarter operating results, we continued to outperform our competitors in attracting mobile internet subscribers. At the end of June 2014, our mobile internet subscriber base had reached 4.6 million, representing 36.4% market share. We believe the growth momentum and market leadership will continue, due to our efforts on our promotional plans, 2G to 3G migration, and the 4G service launch.

We continued promoting our convergence plans combining broadband and MOD services. The broadcasting of FIFA games helped the broadband and MOD subscriptions, especially for high speed fiber services. The 100Mbps fiber service subscribers increased more than 500% and MOD subscribers increased 6.3% year over year at the end of June 2014.

Number One Mobile Services Provider

Slide 5 provides an update on our mobile business.

During the second quarter, mobile data revenue grew by 23.7% year over year, mainly driven by the 32.5% increase in mobile internet revenue.

Entering into the new 4G era, our mobile business strategies are focusing on 4G service promotion, followed by expanding the 4G device profile from high tier to mid and low tier. The migration of 2G customers to the 3G network is also part of the strategies to promote data service. Meanwhile, we will accelerate 4G network deployment to cater to customers' demand.

Smartphone-Value Driver for Mobile

Moving on to slide 6.

Our promotional initiatives targeting mid-to-low tier smartphone users continued to boost our smartphone penetration rate to 58% at the end of the second quarter of 2014.

Net add to mobile internet subscribers are more than 700 thousand for the first half of 2014. While we targeted an increase of 1.1 million mobile internet subscribers this year, the growth rate has been much higher than expected.

ARPU for the second quarter decreased QoQ mainly due to the continuous promotional plan. During the quarter, the plan was successful with regards to attracting new subscribers, but at the same time caused some temporary downward pressure on ARPU. We expect the ARPU to recover in the third quarter this year.

Fixed Broadband Internet Services

Slide 7 shows the results for our broadband business.

During the second quarter, we continued to see a steady migration of subscribers to higher speed fiber services. We witnessed more than 500% year-over-year growth in subscribers opting for connection speeds of 100Mbps or higher, reaching about 627,000 by the end of June 2014.

We will continue to encourage our subscribers to migrate to higher speed fiber offerings. As mentioned, the fiber convergence plan combining broadband with MOD family packages stimulated both fiber migration and MOD subscription. We are also targeting SMEs and machine-to-machine applications to stimulate further broadband usage.

MOD/IPTV Service

Moving on to slide 8.

Our IPTV revenue in the second quarter 2014 increased by 8.8% year over year. Moreover, the household TV usage rate continued to increase over the past quarters, demonstrating our success in boosting customer stickiness on our platform.

In addition to the fiber convergence plan which boosted IPTV subscriptions, we will continue enriching local contents and VOD programs. We also focus on optimizing the MOD cost structure to enhance capital efficiency.

As 4G service has already been launched, we are planning to offer a convergence plan so that 4G subscribers who also subscribe to MOD service can enjoy MOD programs over their smart devices.

ICT and Cloud Computing Initiatives

Please see slide 9 for an update on our ICT and cloud initiatives.

In the first half of 2014, our cloud and information security business revenues increased by 6.8% year over year. In the second quarter, we continued winning ICT projects, including the data system project for Department of Land, the host computer leasing project for Ministry of Labor, the cloud computing system for National Police Agency and an ICT project for a hospital. We will continue to leverage our core telecom infrastructure and services to expand our ICT and cloud business.

Financial Overview

Thank you President Shih. And thank you Chairman Tsai for the kind introduction. I am excited to join the Chunghwa Telecom team, and look forward to working with all of you.

Now I will review our financial results in detail, beginning on slide 11.

Income Statement Highlights

On slide 11 are our income statement highlights.

For the second quarter of 2014, total revenues decreased by 0.1% and operating costs and expenses increased by 0.6% year over year. Our income from operations and net income decreased by 2.6% and 0.3%, respectively. In addition, the EBITDA margin increased from 36.88% to 37.38% in the second quarter as compared to the same period in 2013.

Business Segment Revenues

Please refer to slide 12 for an update on our business segment revenue.

For the second quarter of 2014, the year over year decline in the total revenue was driven by the decrease in fixed and mobile voice revenue and the ICT project revenue, which offset the increase in mobile VAS revenue and handset sales. However, we expect handset sales will be deferred to the second half this year along with the 4G service launch.

Costs and Expenses

Moving on to Slide 13, our second quarter operating costs and expenses increased by 0.6% year over year, mainly due to the increasing depreciation and amortization expenses and personnel expenses, which were partially offset by a decreasing interconnection fee expense. To be more specific, the increase in depreciation expense was mainly from 3G maintenance and cloud and IDC equipment investment while amortization expense was mainly from the amortization of the 4G license fee.

Cash Flow & EBITDA Margin

On slide 14, in the second quarter of 2014, cash flow from operating activities decreased 4.95 billion NT dollars compared to the same period of 2013. This was mainly due to the higher operating cash flow in the second quarter of 2013 resulting from the delay of bill collection from the first quarter to the second quarter associated with the holiday season. Moreover, to accelerate fiber and mobile network deployment, the higher payment for spare parts also explained part of the decrease.

Cash and cash equivalents at the end of the period decreased year-over-year mainly due to the 39.1 billion NT dollar payment for acquiring the Mobile Broadband License in the fourth quarter of 2013. As of June 30, 2014, we had 28.1 billion NT dollars of cash and cash equivalents. The increase in EBITDA margin was primarily due to lower high-tier smart phone sales, which have a lower EBITDA margin than traditional telecom services.

Forecast & Operating Results

Slide 15 shows our 2014 second quarter and half-year results as compared to our guidance.

Our revenue and costs and expenses are lower than expected mainly due to lower handset sales and lower cost of goods sold. However, our operating income, net income and EBITDA all exceeded our second quarter guidance. We expect our full year net income will slightly outperform our guidance.

Effective and Efficient Capital Expenditure

Lastly, on slide 16.

Our capital expenditure continues to focus on 4G network deployment, fiber broadband construction, service platforms and cloud deployment which includes data center construction. We will continue reviewing our capex budget and execution plan carefully on a regular basis, and focus on making the most cost-effective spending decisions possible. Therefore, a 5 to 10% reduction in budgeted capex for this year could be expected.

Thank you for your attention and now we would like to open up for questions.

- Q&A Session -