

Ch.5 Operating Strategy

Macroeconomics

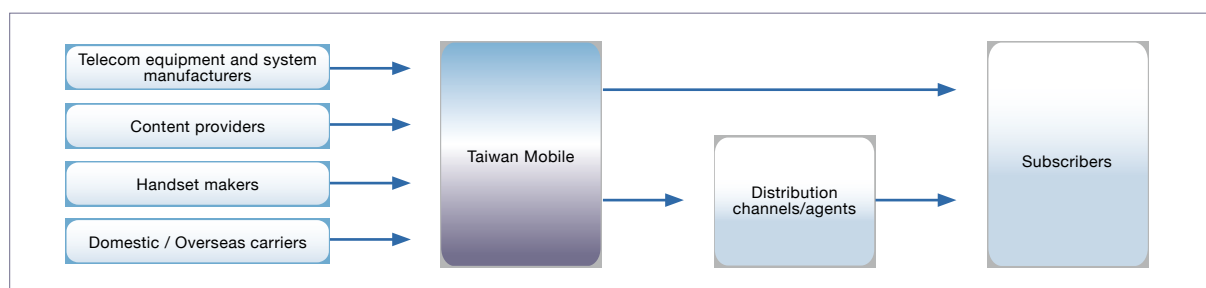
Consumer spending in communication and broadcasting related services is largely influenced by the macro-economic environment. Statistics released by the Directorate General of Budget, Accounting and Statistics (DGBAS) showed that private consumption rose 2.6% in 2007, from 1.8% in 2006, spurred by rising incomes, hefty cash dividends distributed by listed companies, and increasing labor employment and social welfare benefits. With DGBAS forecasting private consumption growth of 2.9% in 2008, the mobile market is likewise expected to experience a similar growth pattern.

Mobile Business

Industry Developments

1. The big three telecom operators continue to dominate the market, adopting market segmented rate plans to prevent cutthroat competition.
2. Growth in the 2G sector is likely to be capped by a high penetration rate. Competitive prices, together with improving handset features, functions and quality, have spurred the migration to 3G networks.
3. The rising need for high-speed Internet access, aggressive deployment of HSDPA (3.5G) infrastructure and promotion of various data content are expected to boost revenue from value-added services.
4. The National Communications Commission (NCC) released WiMAX licenses in July 2007, and winners have started building network infrastructure.
5. The NCC approved a three-year proposal requiring telecom operators to cut tariffs for selective 2G services, including prepaid calls, fixed-to-mobile calls and highest tariff rate plans, by 4.88% per annum starting in April 2007.
6. Telecom companies are positioning themselves to meet the challenges of digital convergence and the growth opportunities it offers.

Mobile industry value chain



Products and Services

The Company holds a GSM 1800 license and a 3G license to operate mobile phone services nationwide, covering Taiwan, Kinmen, Matsu and other outlying islands.

The Company provides mobile services with the following prefixes — 0935, 0939, 0922, 0920, 0918, 0952, 0953, 0958, 0914, 0961, 0970, 0987 — with services as categorized below:

| Type of service | Mobile phone | Phone card |
|-----------------|-----------------------|----------------------|
| | Postpaid subscription | Postpaid vouchers |
| | Prepaid subscription | Prepaid reload cards |

- (1) Basic telecommunication services, such as calling or receiving calls from local fixed line, domestic long distance, international direct dialing, mobile phone and pager services.

- (2) Value-added services, including voice mail, call forwarding, call waiting, conferencing, short messaging service (SMS), roaming, call barring, video calls, and multimedia & content services (e.g., ringtones, games, screensavers, MP3, video clips, video streaming) through GPRS/3G/HSDPA transmission.
- (3) Business solutions, such as enterprise package and mobile virtual private network (MVPN), mobile messaging service (a dedicated platform to deliver cost-effective, high-volume SMS), mobile data service (wireless Internet access via GPRS/ 3G/HSDPA, positioning tracking/fleet management via GPS/GPRS), and mobile office (BlackBerry email solutions)

Revenue breakdown by service

| | 2007 | | 2006 | |
|------------------------------------|-------------------|------------|-------------------|------------|
| | Amount (NT\$'000) | % of total | Amount (NT\$'000) | % of total |
| Telecommunications service revenue | 51,023,299 | 99.49% | 47,692,697 | 99.59% |
| Other revenue* | 261,557 | 0.51% | 198,592 | 0.41% |
| Total revenue | 51,284,856 | 100.00% | 47,891,289 | 100.00% |

* Includes revenue from handset sales and commissions from receipts under custody and payment on behalf of others.

Mobile subscriber number and revenue for the past two years

| | 2007 | | | 2006 | | |
|----------------------------|----------------------------|--------------------|--------------------|----------------------------|--------------------|--------------------|
| | Domestic | | Overseas | Domestic | | Overseas |
| | Average No. of subscribers | Revenue (NT\$'000) | Revenue (NT\$'000) | Average No. of subscribers | Revenue (NT\$'000) | Revenue (NT\$'000) |
| Telecommunication services | 5,175,916 | 51,023,299 | - | 4,806,275 | 47,692,697 | - |

Note: Average number of subscribers = (sum of monthly average number of subscribers)/12

Major Contracts

| Nature | Counterpart | Contract period | Description | Restriction clauses |
|--|--|---|---|---------------------|
| Sale & distribution | Synnex Technology International Corporation | 2005.02.01 ~ 2006.01.31 (contracts automatically renew upon expiration date) | Synnex is authorized to distribute TWM's mobile subscription services | Non-disclosure |
| | Aurora Telecom Corporation | 2007.06.01 ~ 2008.06.30 | Aurora is authorized to distribute TWM's mobile subscription services | Non-disclosure |
| Communication service agency agreement | TransAsia Telecommunications, Inc.(TAT) | 2006.01.01 ~ 2010.12.31 | Provides TransAsia telecommunication related service | Non-disclosure |
| | Mobitai Communications (Merged into TAT on Dec. 15, 2007) | 2006.01.01 ~ 2010.12.31 | Provides Mobitai telecommunication related service | Non-disclosure |
| Network interconnection | Chunghwa Telecom Co., Ltd. | 2005.01.01 ~ 2005.12.31 (under negotiation) (Note 1) | Network interconnection contract | Non-disclosure |
| | VIBO Telecom Co., Ltd. | 2006.01.16 ~ 2007.01.15 (under negotiation) (Note 2) | Voice and short message service contract | Non-disclosure |
| | New Century InfoComm Tech Co., Ltd. | 2005.05.01 ~ 2006.04.30 (under negotiation) (Note 1) | Network interconnection contract | Non-disclosure |
| | Taiwan Fixed Network Co., Ltd. | 2007.07.01 ~ 2008.06.30 | Network interconnection contract | Non-disclosure |
| | Asia Pacific Broadband Telecom Co., Ltd. | 2005.10.15 ~ 2006.10.14 (under negotiation) (Note 1) | Network interconnection contract | Non-disclosure |
| | Asia Pacific Broadband Wireless Communications, Inc. | 2003.07.23 ~ 2004.07.22 (under negotiation) (Note 1) | Voice and short message service contract | Non-disclosure |
| | TransAsia Telecommunications, Inc. | 2004.03.15 ~ 2005.03.14 (under negotiation) (Note 2) | Voice and short messaging service contract | Non-disclosure |
| | Mobitai Communications (merged with TransAsia on 2007.12.15) | 2004.09.13 ~ 2005.09.12 (under negotiation) (Note 2) | Voice and short message service contract | Non-disclosure |
| | Far EasTone Telecommunications Co., Ltd. | 2004.02.10 ~ 2005.02.09 (under negotiation) (Note 2) | Voice and short messaging service contract | Non-disclosure |
| | KG Telecommunications Co., Ltd. | 2004.03.01 ~ 2005.02.28 (under negotiation) (Note 2) | Voice and short messaging service contract | Non-disclosure |
| | First International Telecom Corp. | 2005.05.01 ~ 2006.04.30 (under negotiation) (Note 2) | Voice and short messaging service contract | Non-disclosure |

| Nature | Counterpart | Contract period | Description | Restriction clauses |
|-----------------------|--|---|--|--|
| Handset purchase | Synnex Technology International Corporation | 2004.05.01 ~ 2005.04.30 (contracts automatically renew upon expiration date) | TWM accepts Synnex's consignment to sell handsets and related products | Non-disclosure |
| Equipment acquisition | Nokia Corporation | 2006.09.26 ~ 2009.12.31 | Equipment contract for installation of 3G system | Non-disclosure |
| Customer service | Taiwan Teleservices & Technologies Co., Ltd. | 2006.01.01 ~ 2010.12.31 | TT&T to handle TWM, TAT, and MBT customer service and product sales | Non-disclosure, restriction on competition |

Note1: When the network interconnection contract expires, in the event that both parties are unable to conclude negotiations within three months thereafter, the process shall be as follows:

- (1) If both parties concur to continue negotiations, the original contract terms will continue to take effect until a new agreement is reached.
- (2) Either party can appeal to the Directorate General of Telecommunications for a ruling. Prior to the date of such a ruling, the original contract terms shall continue to take effect. Following the ruling, new contract terms will be formed based on the ruling.

Note2: Negotiations for the new agreement shall commence three months prior to the expiry date of the original agreement. If negotiations are not finalized prior to the expiry date, both parties agree to perform their obligations based on the original agreement until such time when negotiations are finalized by the parties

Note3: If both parties do not finalize signing of the new contract and the current contract has expired, the current contract shall remain valid.



△ Launched first “My Hour” rate plan to allow users to choose a time slot when they can make free intranet calls

Operating Status

1. Postpaid products and services

The Company continues to lead in offering postpaid rate plans. Following the launch of “myfone” rate plans in 2004, the Company introduced “My Zone 268/568” in 2006, allowing regional zone base users to enjoy half rates for both on-net and off-net calls, which became a major driving force in signing up new customers. To maintain its sales momentum and attract high-usage customers, “My Zone 968” was launched in January 2007. The percentage of mid-to-high rate plan subscribers to total new subscribers grew 2.5 times within the first quarter of launching “My Zone 968.” The “My Zone” series now accounts for about 60% of total monthly new subscribers and has surpassed the one million mark. The Company also introduced “My Hour” 688/988 rate plans last year, which allow customers to select and make free on-net calls during an 8 or 12-hour period.

The Company also has excellent loyalty programs in place to help secure its customer base and minimize churn rates. For high average revenue per user (ARPU) customers, the Company has an exclusive program called “my VIP.” It also offers a credit card program that allows customers to earn rebates based on their phone bills.

2. Prepaid products and services

As part of its commitment to offering better services and boosting usage, the Company was the first in 2007 to introduce 3G prepaid services, dubbed “3G Fun Heart Prepaid Card,” enabling prepaid users to enjoy 3G high-speed transmission and instantly accessible video content. The Company also launched discount plans for young people to hook up with their circle of friends and after-school low rates for teenagers. The Company plans to continue cultivating this younger demographic to maintain its market leadership. Late last year, the Company further introduced an innovative hybrid rate plan called “Zero Monthly Fee,” which combines the features of prepaid and postpaid services.

The Company has continued to expand its lead in the foreign workers’ market. To capture the Indonesian and Filipino workers’ market, the Company has teamed up with Telkomsel Telecom of Indonesia and Globe Telecom of the Philippines, both of which are members of the Bridge Mobile Alliance — the biggest mobile telecommunications alliance in the Asia-Pacific region. A competitive new product was introduced — the first transnational co-brand prepaid cards in Taiwan, called the “OK Simpati-Kagen Card” and the “OK Kababayan Card,” which boosted Taiwan Mobile’s share of these two market segments.

▽ Introduced “Zero monthly fee” rate plan combining features of prepaid and postpaid services



With the continuous introduction of new products and more flexible offerings in the prepaid card market, Taiwan Mobile has survived the fierce market competition and experienced growth in spite of a declining market. In 2007, the Company experienced a strong year-on-year growth in terms of the number of prepaid subscribers and revenue.

▽ Introduced Near Field Communication (NFC) Mobile Pay-Pass™ handsets



3. Value-added services

The Company has seen a sharp increase in its VAS user penetration and ARPU, led by mobile Internet, which posted a 44% rise in revenue, aided by the Company's bundling of competitive data tariffs and customized handsets. As a market leader in launching innovative products, the Company set several milestones in 2007: 1) the first Taiwanese operator to introduce Near Field Communication (NFC) Mobile PayPass™ handset in cooperation with MasterCard International; 2) the first Taiwanese operator to launch mobile video blog (Vblog) and mobile music video game; 3) provide 3G universal SIM cards that serve as a personal messaging center combining messaging, personal information management and phone book backup functions; 4) the first local operator to provide "set my ring back tone same as my friend's whether or not they are Taiwan Mobile subscribers"; and 5) launch ultra-



△ Number of downloads of mobile game "DAIKO: Drum Master" broke records

slim 3.5G data card and offer a single data rate for roaming charges in Bridge alliance member operators' areas.

The Company will continue to pursue its goal of providing simple and convenient mobile phone services by enhancing its "Catch" mobile Internet portal, offering easy to understand mobile Internet tariffs and easy to use customized handsets. With broadband and multimedia gaining in popularity, the Company is keen on developing and promoting diverse triple play services to address the different lifestyles and needs of all customer segments. This not only enables the Company to differentiate its products and increase customer satisfaction, but can also lead to exponential growth in data ARPU.

4. Enterprise customer services

The Company has developed several enterprise solution packages, including mobile communication and data services, to meet corporate telecommunication needs. Launched in December 2006, the globally popular BlackBerry email solution was designed to meet the demand for mobile office solutions by employees of multinationals. The service has already attracted about 700 enterprise clients by the end of 2007. As digital convergence takes off, the Company

plans to provide integrated communication services, offering a “one-stop shopping” service that combines fixed line, mobile and data solutions to fulfill the requirements of enterprises in different market segments.

Opportunities and Challenges

The overall macroeconomic environment remains favorable for growth in the telecommunications industry with the major positive and negative factors as well as countermeasures outlined below:

1. Positive factors:

- (1) 3G and 3.5G technologies enable high-speed and better quality transmission of mobile content, leading to higher subscriber usage and increased revenue for telecom operators.
- (2) The digital era has contributed to the convergence of information, communication and media industries, and telecom companies are poised to play a pivotal role in the delivery of multimedia content to customers.
- (3) Along with rapid development of the internet, many innovative technologies and business models have extended to mobile internet.

▽ Launched exclusively the wildly popular BlackBerry email solution



2. Negative factors:

- (1) New policies and regulatory revisions by the NCC have increased the uncertainty of future operations and profitability.
- (2) WiMAX technology offers comparable high-speed broadband access that can rival other wireless communication technologies.

3. Countermeasures:

- (1) The Company has completed the consolidation of Taiwan Fixed Network Co., Ltd. (TFN) and Telecommunication Network Services Co., Ltd. (TTN), expanding its market share in the wireless communication, information and media industries. This is expected to fuel growth in revenue and profitability.
- (2) The Company closely monitors changes and developments in regulatory policies to formulate countermeasures in advance.
- (3) HSDPA is a more mature technology and ready for commercialization. In addition to an all-out effort in deploying 3.5G network to provide high-speed broadband access, the Company will closely monitor the development of long-term evolution (LTE) technology.
- (4) The Company will introduce high-end technology, such as NFC (Near Field Communication) and LBS (Location Based Services) to promote value-added services.

4. Competitive Advantages and Strategies

- (1) Improving client portfolio
Due to changes in the scale of total new subscriber acquisitions, gross adds in new subscribers in 2007 was less than in 2006.

However, strategies to improve client portfolio helped raise the ratio of mid to high-usage customers as a percentage of gross adds and kept the churn rate low. As a result, mid to high-usage customers accounted for over 60% of total new acquired subscribers. This could translate into ARPU growth in the future.

(2) Diversity of sales channels

The Company expanded direct and franchised shops and improved the quality of service to increase the number of walk-in customers and sales. Faced with fierce competition in conventional sales channels, the Company ventured into direct mailing, e-commerce, and telemarketing to reach different market segments and target high-usage customers, thereby boosting sales, lowering cost and enhancing quality control over sales channels.

(3) Leading wireless broadband services

The Company took the lead in launching 3G services in 2005 and 3.5G services at the beginning of 2007. In addition to flexible rate plans, exclusive handsets and extensive value-added services, subscribers of the Company, TransAsia Telecommunications and Mobitai can be upgraded seamlessly. As of the end of 2007, the company's 3G subscriber base reached 1.24 million, with data

ARPU significantly surpassing that of 2G subscribers, spurring further development of value-added services.

(4) Expanding resources from international alliances

The Company is the sole Taiwanese member of the Bridge Alliance, the largest mobile alliance in Asia Pacific. The alliance consolidates the region's leading telecommunication operators – SingTel in Singapore, Maxis in Malaysia, CSL in Hong Kong, Bharti in India, Telkomsel in Indonesia, AIS in Thailand, Globe in Philippines, Optus in Australia, CTM in Macau, SKT in South Korea, and Taiwan Mobile in Taiwan – with a combined customer base exceeding 180 million. Having the advantage of economies of scale as well as a regional-based service platform, the Company occupies a leading position and possesses rich resources in procurement, content and new technologies.

5. Operating Results Review

As the Company continued to devote resources to developing new products and providing the best service for its customers, its total revenue still rose 1% YoY in 2007 despite a saturated market and keen competition. Sales were bolstered by growth rates of 19% and 23% in pre-paid and VAS revenues, allowing the Company to outperform and expand its share of the telecom service market.

With the deployment of its 3G network, depreciation and base station related expenses leveled up operating cost by 3% compared with the previous year. Nevertheless, efforts to reduce operating expenses helped to sustain operating income. Non-operating asset write-off of obsolete equipment weighed on net income in 2007, but this should translate into substantial savings in depreciation expense in 2008.

▽ Offered a single data rate for roaming charges in Bridge alliance member areas





△ Introduced "Ring Tone DIY" services

Fixed Line Business

Industry Developments

The paradigm shift in the telecom industry is continuing with players pursuing vertical integration through mergers and acquisitions throughout the value chain, incorporating television, broadband access, data, voice, media and mobile services to satisfy customers' diverse needs. A quick overview of the services is outlined below:

1. Local call service:

NCC data shows that the penetration rate of fixed line services was 57.9% in 2007, down 1ppt from 2006. Given the recent shift to data service, industry experts forecast little change in the number of subscribers ahead.

2. Long distance call service:

The rising popularity of VPN services, mobile phone services and VoIP services have cut into the market for long distance call services.

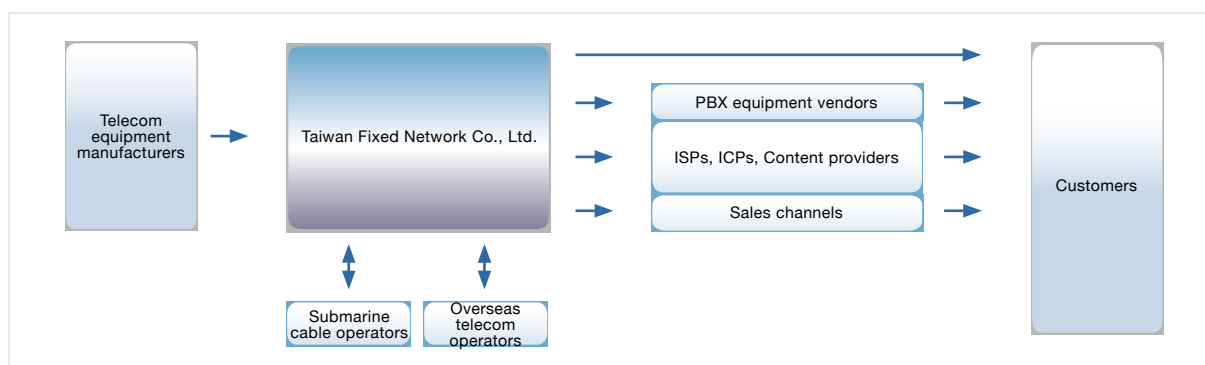
3. International direct dialing (IDD) service:

The rising demand for communication services across the Taiwan Strait, opening of the local market to foreign workers and the regionalization and globalization of Taiwan-based enterprises continue to support demand for IDD. However, overall market revenue is expected to shrink due to cutthroat pricing competition in the foreign workers' market.

4. Internet access services:

Total market revenue is expected to grow as enterprises become more dependent on the Internet, content services become more diverse, and fiber broadband services become widely accepted. Adding in the fact that telecom operators are aggressively promoting 3G/3.5G wireless services, and more integrated wireless and wired line markets emerge, revenues are expected to grow in spite of falling prices and a saturated market.

Fixed line industry value chain



Products and Services

The fixed telecommunication network service license, which was issued in 2000, grants the Company the right to provide Taiwan and the outlying islands, including Kinmen and Matsu, with the following services:

| Business Item | Produce / Service | Description |
|------------------|--|---|
| Voice Service | Local calls | We provide integrated voice solutions, including IDD, VoIP and intelligent network service (e.g., 080 domestic toll-free service and IDD prepaid cards), enabling users to save on huge calling costs. TFN continues to develop advanced technologies to enhance reliability and provide instant response to ensure customer satisfaction. |
| | Long distance calls | |
| | IDD (International Direct Dialing) | |
| | Audio conference | |
| | Centrex | |
| | VoIP for enterprise | |
| | Cable phone | |
| | IDD prepaid card | |
| | Super saving international card | |
| | 080 Domestic toll-free number | |
| | Foreign toll-free number | |
| | 0209 Voice information provision service | |
| Circuit Service | IPLC (International private leased circuit) | We offer different types of circuits for information transmission, including fixed-rate circuits and dedicated bandwidth for data transmission between two terminals. TFN offers the best transmission environment for various applications, including voice, data and multimedia information. |
| | International Metro Ethernet | |
| | ADSL | |
| | Leased line | |
| | Metro Ethernet | |
| | FTTx | |
| VPN Service | International IP-VPN | A virtual private network (VPN) is a communications network tunneled through another network and dedicated for a specific network. We offer VPN service to enhance communications security for popular applications such as POS systems, credit card transactions and ATMs. TFN also delivers total solutions, including Layer 2 VPN and IP VPN, to expand customers' business opportunities. |
| | IP-VPN | |
| | ADSL-VPN | |
| | ATM (Asynchronous transfer mode) | |
| | FR (Frame relay) | |
| Internet Service | Leased line access | We offer Internet access via fiber optics, copper wires or Metro Ethernet. The Company also provides Internet Data Center (IDC) services, including co-location, web hosting, super mail and domain name registration. TFN's hosting services not only cover carrier-level facilities, but also managing/maintenance services for customers. Enterprise customers are thus able to lower their IT expense and focus on their own core competence. |
| | Metro Ethernet access | |
| | ADSL access | |
| | Transit | |
| | Co-location | |
| | Web hosting | |
| | Super mail | |
| | Domain Name | |

Opportunities and Challenges

The Company believes that the overall macro environment remains favorable in terms of growth for the fixed line industry. The major positive and negative factors as well as countermeasures are outlined as follows:

1. Positive factors:

- (1) Strong demand for mobile data services: To meet consumer demand for more high-speed broadband services anytime anywhere, the Company can leverage off fixed line's backbone network to facilitate delivery of mobile services, such as mobile data cards.
- (2) Strong demand for integrated information services for enterprise clients: Future convergent products are aimed at consolidating intranet, broadband management, and information security into a one-stop shop for customers. The Company has the advantage of possessing resources for both mobile and fixed line services.
- (3) The telecom industry's demand for leased circuit is increasing due to expansion of 3G, WiMAX, and FTTx network deployment.
- (4) NCC ordered Chunghwa Telecom (CHT) to provide local loop services at cost to new telecom entrants in order to lower costs and resolve a service bottleneck.

2. Negative factors:

- (1) Local loop bottleneck is a major obstacle to fixed line operators' business expansion.
- (2) VoIP penetration has cannibalized fixed line operators' traditional voice revenue.

- (3) NCC pushed for rationalization of telecom tariffs and demanded all telecom operators lower retail rates gradually, but this only added to the difficulties of new players.

3. Countermeasures:

- (1) Raising ARPU: Target high-usage customers by providing services such as "Information and Communications Integrated Solution" that meet customers' varying needs, creating a win-win situation to enhance customer loyalty.
- (2) Providing high-quality services: Focus on IP VPN and Metro Ethernet solution to provide high-quality integrated platform infrastructure and take the lead in technology advancement.
- (3) Expanding cost and operation synergy: Strengthen internal controls and professional division of labor, upgrade IT system and support, revise IP policy and submarine cable strategy to ensure short, mid and long-term benefits and improve core competence to benefit shareholders.
- (4) Maintaining market leadership in broadband and multimedia application integrated services: Closely monitor industry developments in combining voice, image, data, mobile and IT services. The Company aims to surpass the success of its traditional business model by providing the best customer service quality through the Next Generation Network (NGN) framework, and synergize the resources of the group to the benefit and satisfaction of its customers.

4. Competitive Advantages and Strategies

(1) Brand new image

The Company works on the concept of providing quality “customer privileges” by utilizing its extensive experience and expertise in broadband technology. A new service, called “TWM Solution,” was launched at the end of 2007, integrating quality services provided by Taiwan Fixed Network, Taiwan Telecommunication Network Services and Taiwan Mobile.

(2) Professional management team and efficient support group

The Company leads the competition in achieving synergy from the integration of group resources, including mobile telephony, fixed network and cable TV network, with integrated back-office functions, e.g., network planning, operation and maintenance, information technology, and procurement, to support its frontline operations. This organizational matrix allows business units to focus on product planning and sales activities. As a result, corporate and enterprise customers are able to experience the professional service provided by “TWM Solution.”

(3) Effective direct and channel sales teams

Expand services through direct sales teams, channel partners, and retail chains across the nation.

▽ Providing integrated information and communication services to enterprise customers



△ Deployed broadband network to provide services for remote areas in Alishan

Operating Results Review

The Company endeavored to improve its product mix after the merger with TFN. As a result, total revenue from fixed-line business increased 9% YoY, aided by the 44% and 28% YoY growth in leased line and data services, respectively. As the Company consolidated its resources, operating income turned positive with operating cost and expense declining 10% YoY.

Due to TFN's superior enterprise customer base, the Company expanded its share of the enterprise market. Following the merger with TTN, the Company is looking forward to exploring the full potential of combining mobile and fixed-line resources in providing enterprise customers with more competitive and integrated telecom solutions.

Cable Business

Industry Developments

1. Mergers and acquisitions initiated by foreign investments and private placements

A wave of mergers and acquisitions swept across Taiwan's cable TV (CATV) in 2007, as foreign investments and private equity funds swamped the local industry. After a year of consolidation, TFN Media, the Company's CATV division, ranked as the fourth-largest multi-system (MSO) operator in terms of subscriber number. Chunghwa Telecom also ventured into the IPTV market, offering bundled FTTx broadband and multimedia on demand (MOD) services and effectively positioning itself as a major competitor in the CATV market.

As the CATV market nears saturation, CATV operators have employed different measures to provide customers with more diverse and value-added services in hopes of increasing revenue. To meet the challenges of digital convergence and better compete with CHT, the Company has built a fiber optic network in addition to continuous upgrade of network quality; conducted R&D for integrated technological solutions; and launched DTV, high-speed broadband surfing, and cable phone services to meet the demands of home customers.

2. NCC promulgates multiple policies

The National Communications Commission (NCC), the regulatory body which oversees the cable TV industry, promulgated several key policies as a means to accelerate the development of digital convergence. These include:

(1) Promulgation of "Guidelines for Applying

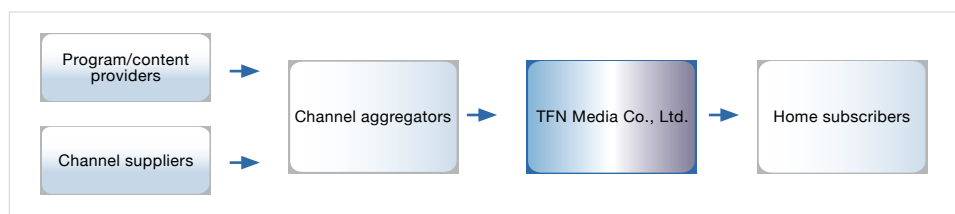
for Renewal of Permits & Licenses for CATV System Operators," advising CATV operators that intend to continue operations to submit a proposal on CATV migration from analog transmission to digital communication along with concrete plans for promotion of digital services.

- (2) Revision of "Regulations Governing Fixed Network Telecommunications Businesses," dated May 21, 2007, to include multimedia content transmission platforms. Local network operators are permitted to set up open transmission platforms, while CATV system operators are permitted to apply for operation of local network services within the regions where they offer CATV service.
- (3) On November 15, 2007, the NCC approved CHT's petition to charge subscribers NT\$89 as its platform service fee for transmitting multimedia content. As for service charges to channel suppliers for transmitting contents over the MOD platform, the maximum limit is set at NT\$800,000 per channel per month. NCC permitted CHT to offer MOD business, but not to take the initiative in assembling channels.
- (4) NCC planned to integrate the three major broadcasting laws (Cable Radio & Television Act, Satellite Radio & Television Act, and Radio & Television Act) into a single law – the Telecommunications Act. On December 9, 2007, it completed the draft of the Communications Administration Act to directly oversee its three main divisions: infrastructure, operation and content application. The draft proposes to remove the cap on subscriber market share and cable system operator (SO) market share as stated in Article 21 of

“Cable Radio and Television Act”, raise the ceiling on foreign shareholding percentage, and transfer the right to review monthly price caps from local governments to a central authority. All these are expected to benefit the industry. However, under the new structure, cable SOs are required to secure two additional business licenses – one for broadcast TV service and another for broadcast com-

munication network. Cable SOs also face more regulatory restrictions compared to telecom operators, which are expanding their video service footprint. The draft does not provide specific guidelines on new business areas, such as charges for subscribing to different programs or content and changes in operating regions, casting a cloud of uncertainty over the CATV business.

Cable industry value chain



Products and Services

In 2007, the Company strengthened customer loyalty and maximized revenue generation by focusing on local sustainability, taking the lead in launching landmark digital products and services, broadening its market share, and developing innovative digital products and value-added services. The Company has maintained its leading market position by continually providing diversified and integrated digital products to attract more subscribers.

TFN Media (TFNM), the cable division of the Company, holds a Type II telecommunications business license. Each of the seven subsidiary CATV operators of TFNM holds a CATV business license and is engaged in key products and services, including pay TV and Internet access services through cable broadband and fiber optic broadband. TFNM teamed up with Taiwan Fixed Network to launch cable phone (VoIP broadband phone) services, which are now available in Sinjhuang, Sijhih and Tamshui in Taipei County, Ilan County and Fengshan in Kaohsiung County.

TFNM's key products and services

| Target customers | Service category | Description | Highlights |
|-----------------------------|---------------------------|---|---|
| Households in licensed area | Pay TV | Cable TV | Using coaxial cables as the media, diverse and multifaceted data content such as TV programs as well as video services are transmitted to customer terminals. |
| | Broadband Internet access | Cable broadband | With the cable system operators paving the way for HFC networks, the Company will utilize this new cable modem technology and know-how to offer broadband Internet services to customers. |
| | | Optical fiber | Utilize optical fibers already installed in buildings to provide customers with FTTx broadband Internet services. |
| | Voice | Cable phone (VoIP broadband phone) services | Using the IP based HFC network system, the Company is able to offer voice services at very competitive prices. |

Opportunities and Challenges

The Company believes that the CATV industry will continue to evolve. Factors, both advantageous and disadvantageous, which may affect the CATV industry are outlined below:

1. Positive factors:

- (1) CATV MSOs have a virtual monopoly of the market in their respective regions. CATV operators have built up their brand names and service awareness locally, making them difficult to replace.
- (2) With the arrival of the digital era, the convergence of video, voice and data services has come to dominate the communications market. CATV operators have the “last mile” advantage, allowing them to develop and offer CATV hybrid fiber/coaxial (HFC) networks and multiple product and service technology solutions, including digital TV, video on demand, cable modem broadband services, FTTx optical fiber broadband services, IPTV and cable phone VoIP, offering customers a whole new range of possibilities.
- (3) The NCC completed a draft “Strategic Policies to Promote CATV Digitization Development” in early 2007 to guide the CATV industry in its digital transition and help it overcome longstanding bottlenecks. The policies also highlighted the government’s determination to focus and promote CATV digitization. The close communication and coordination between the government and the CATV industry should aid and benefit the industry’s development and progress.
- (4) Digitization of the CATV industry will boost broadband efficiency. The ad-

ditional broadband frequencies can be used to accommodate digital multimedia to create innovative services, e.g., sports lottery and optional video services. CATV may also be integrated into digital multiple-play platforms to provide diverse digital services. CATV operators will also be better equipped to crack down on piracy, control subscription revenue and provide more value-added services.

2. Negative factors:

- (1) CATV rates are reviewed by the local county/city governments on an annual basis. Given a slowing economy, several county governments have lowered the price cap for 2008 by 2%~5%, impacting MSO’s revenue.
- (2) Given the high penetration in the pay TV market, there is limited room for growth in the subscriber base.
- (3) The content of Chunghwa Telecom’s MOD services is not as rich and versatile as CATV channels’ offerings and cannot be viewed through an extension because of bandwidth restrictions. Nonetheless, Chunghwa Telecom remains a potential threat to traditional CATV operators given its expansive national network.

3. Countermeasures:

- (1) The Company will monitor regulatory revisions through continuous communication and lobbying and will map out appropriate plans and countermeasures.
- (2) The Company will push for the building of two-way optical fiber networks to upgrade network quality and signal stability. It will offer integrated technological solutions, develop new products and value-added services. Through such

efforts, it can maximize ARPU and revenue.

- (3) In line with the CATV digitization policies promulgated by the authorities, the Company will aggressively invest in manpower, technology, capital and marketing resources to design digital CATV products and services within the Company's operating regions, as well as coordinating measures in line with the time schedule of digitization.
- (4) The Company will aggressively explore merger and acquisition or investment opportunities of CATV to expand current market share.

4. Competitive Advantages and Strategies

- (1) Service commitment to the local community
CATV is normally confined to service within local communities. Given the Company's commitment to upholding "sustainability through dedicated service," it has held a variety of educational and training programs to upgrade employee capabilities and customer-service quality. Meanwhile, 24/7 customer service hotlines are available to serve customers' urgent needs. These efforts reflect the Company's service dedication and commitment to achieving customer satisfaction.
- (2) Two-way transmission network construction
To provide stable network quality and diverse products and services to its target customers, the Company has mapped out two-way HFC network systems and upgraded outmoded circuits to enhance the performance of existing circuits. TFN Media has finished construction of two-way networks in Sinjhuang, Taishan and Linkou in Taipei County, Ilan County, and Fengshan in Kaohsiung County. TFN Media is thus now in a strong

position to meet customer demand for digital products and services.

- (3) Launch of innovative products and services
CATV operators have the competitive advantage with their control over the "last mile" in all CATV channels. Through one cable channel, an operator can provide subscribers with a variety of products and services. With this in mind, the Company has aggressively invested in human resources, technological know-how and other resources to provide integrated technology solutions through its CATV channel. It is deeply committed to providing innovative products and services that meet customer needs. Services rendered by TFN Media include CATV, cable modem broadband surfing, FTTx broadband Internet, and cable phone VoIP. The Company expects to launch more forward-looking products and services that will boost overall performance.
- (4) Integration of group resources
The Taiwan Mobile Group provides mobile, fixed network, CATV and content services. By integrating the group's marketing resources and its strong technological support, the Company has become a formidable presence in this intensely competitive industry.

Operating Results Review

Cable business revenue mainly comes from pay TV revenue, with a small percentage derived from cable broadband service. Pay TV revenue grew 6% YoY in 2007 due to the steady increase in subscriber base, resulting in better economies of scale, lower costs and a higher operating income. The cable broadband business experienced significant growth in 2007, with revenue and the number of subscribers increasing 44% and 40% YoY, respectively. Revenue and operating income of the entire cable division rose 9% and 20% YoY, respectively.

Short and Long-term Business Development Plan

The Company has structured its operation into three business groups: Consumer, Enterprise and Household. Each group has its own distinct business focus and product portfolios as shown below.

Consumer Business Group (CBG)

CBG's target customers are individual consumers. Its primary services include voice, messaging, mobile Internet and video. This year Taiwan Mobile will continue to focus on developing high value customers and raising mobile Internet penetration and usage. It will also promote 3G/3.5G businesses through network expansion and launch of innovative products. Taiwan Mobile plans to fully maximize the potential of new technologies by launching GPS and NFC enabled services.

The Company's marketing thrust will be to enhance the quality of life by promoting new lifestyles with access to digital entertainment in the future. To this end, Taiwan Mobile plans on taking the following initiatives:

- Employ new technology that will deliver advanced multimedia services such as mobile TV, follow-me content, etc.
- Link mobile world with the Internet's Web 2.0 community and social network services.
- Provide segmented service packages that are more varied and cater to different customer needs.

Enterprise Business Group (EBG)

EBG focuses on network and data services for enterprise customers. Its key products include Mobile VPN, IP-VPN, IDC, VoIP, Fiber link, and IP transit. This year, EBG's focus will be to provide customers with key solutions through telecom products that support integrated information and communication services.

- TWM's vision is to expand its enterprise services from network-centric to ICT centric solution and services by taking the following directions:
- ICT solutions – Collaborate with IT or system integrator vendors that will help develop and deploy enterprise ICT solutions.
- Managing services – Advance managing services to support real-time system monitoring and measure performance as well as ensure end-to-end network reliability, availability, and security.

Household Business Group (HBG)

HBG focuses on cable-based services for households. Its key products include cable TV, cable modem, and cable phones. This year, HBG aims to increase its market penetration, offer convergent services, increase household ARPU, and build up its triple play business through the following measures:

- Complete two-way cable network upgrade and build up digital TV business.
- Construct FTTx networks outside of CATV zone for broadband and IPTV trial.
- Deploy TV portals to introduce intelligent home care and Internet services.



△ Enriching mobile data services by offering easy-to-use internet portal