

3Q14

Quarterly Management Report  
Oct 16, 2014**CONTACT****Elizabeth Sun**

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**Topics in This Report**

- Revenue Analysis
- Profit & Expense Analysis
- Financial Condition Review
- Cash Flow
- CapEx & Capacity
- Recap of Recent Important Events & Announcements

**Operating Results Review:***(Amounts are on consolidated basis and are in NT\$ billions unless otherwise noted)*

	<u>3Q14</u>	<u>2Q14</u>	<u>3Q13</u>	<u>QoQ</u>	<u>YoY</u>
EPS (NT\$ per common share)	2.94	2.30	2.00	27.9%	46.9%
(US\$ per ADR unit)	0.49	0.38	0.34	27.9%	46.9%
Net Revenue	209.05	183.02	162.58	14.2%	28.6%
Gross Profit	105.58	91.19	78.89	15.8%	33.8%
<i>Gross Margin</i>	<i>50.5%</i>	<i>49.8%</i>	<i>48.5%</i>		
Operating Expenses	(21.14)	(20.25)	(19.26)	4.4%	9.8%
Other Operating Income and Expenses	(0.01)	(0.23)	(0.01)		
Operating Income	84.43	70.71	59.62	19.4%	41.6%
<i>Operating Margin</i>	<i>40.4%</i>	<i>38.6%</i>	<i>36.7%</i>		
Non-Operating Items	0.95	3.38	(0.27)		
Net Income Attributable to Shareholders of the Parent Company	76.34	59.70	51.95	27.9%	46.9%
<i>Net Profit Margin</i>	<i>36.5%</i>	<i>32.6%</i>	<i>32.0%</i>		
Wafer Shipment (kpcs 12 inch-equiv.)	2,267	2,053	1,864	10.42%	21.62%

*Note: Diluted weighted average outstanding shares were 25,930mn units in 3Q14***Financial Highlights:****Third Quarter 2014**

- Net revenues were NT\$209.05 billion, representing a 14.2% increase from NT\$183.02 billion in 2Q14 and a 28.6% increase from NT\$162.58 billion in 3Q13.
- Gross margin was 50.5%, up 0.7 percentage point from 2Q14 and up 2.0 percentage points from 3Q13.
- Operating margin was 40.4%, up 1.8 percentage points from 2Q14 and up 3.7 percentage points from 3Q13.
- Non-operating items were a gain of NT\$0.95 billion, compared to a gain of NT\$3.38 billion in 2Q14 and a loss of NT\$0.27 billion in 3Q13.
- Net income attributable to shareholders of the parent company was NT\$76.34 billion, up 27.9% from 2Q14 and up 46.9% from 3Q13. Net profit margin was 36.5% and diluted EPS was NT\$2.94.

## I. Revenue Analysis

<b>I. Revenue Analysis</b>			
Wafer Rev. by Application	3Q14	2Q14	3Q13
Computer	9%	11%	13%
Communication	59%	54%	53%
Consumer	10%	12%	14%
Industrial/Standard	22%	23%	20%
Wafer Rev. by Technology	3Q14	2Q14	3Q13
20nm	9%	0%	0%
28nm	34%	37%	32%
40/45nm	17%	19%	20%
65nm	13%	15%	15%
90nm	6%	7%	8%
0.11/0.13um	3%	3%	4%
0.15/0.18um	13%	14%	15%
0.25/0.35um	4%	4%	5%
0.50um and above	1%	1%	1%
Wafer Rev. by Customer Type	3Q14	2Q14	3Q13
Fabless/System	84%	85%	87%
IDM	16%	15%	13%
Net Rev. by Geography	3Q14	2Q14	3Q13
North America	69%	67%	70%
Asia Pacific	13%	14%	15%
China	6%	8%	5%
EMEA	6%	6%	7%
Japan	6%	5%	3%

### Revenue Analysis:

In the third quarter, strong wafer demand for mobile computing related applications drove our revenue growth. By application, Communication and Industrial / Standard increased 26% and 9%, respectively, while Computer and Consumer decreased 6% and 3%, respectively.

20nm process technology made its debut and contributed 9% of total wafer revenues in the third quarter. Advanced technologies (28nm and below) accounted for 43% of total wafer revenues, up from 37% in 2Q14.

Revenues from Fabless/System customers accounted for 84% of total wafer revenues in 3Q14.

From a geographic perspective, revenues from customers based in North America accounted for 69% of net revenues, while revenues from Asia Pacific, China, EMEA (Europe, Middle East, and Africa) and Japan accounted for 13%, 6%, 6%, and 6% of net revenues, respectively.

## II. Profit & Expense Analysis

<b>II - 1. Gross Profit Analysis</b>			
(In NT\$ billions)	<b>3Q14</b>	<b>2Q14</b>	<b>3Q13</b>
<b>Cost of Revenue</b>	<b>103.47</b>	<b>91.83</b>	<b>83.69</b>
<b>Gross Profit</b>	<b>105.58</b>	<b>91.19</b>	<b>78.89</b>
<b>Gross Margin</b>	<b>50.5%</b>	<b>49.8%</b>	<b>48.5%</b>

### Gross Profit Analysis:

Gross margin was 50.5% in 3Q14, 0.7 percentage point higher than 2Q14. Third quarter margin improvement was contributed by consistent cost improvement, partially offset by 20nm margin dilution at the early production stage. In addition, 2Q14 gross margin was impacted by an unfavorable inventory valuation adjustment, which was absent in 3Q14.

## II - 2. Operating Income Analysis

(In NT\$ billions)	<u>3Q14</u>	<u>2Q14</u>	<u>3Q13</u>
<b>Total Operating Expenses</b>	<b>21.14</b>	<b>20.25</b>	<b>19.26</b>
Research & Development	15.21	13.61	13.36
SG&A	5.93	6.64	5.90
<b>Other Operating Income and Expenses</b>	<b>(0.01)</b>	<b>(0.23)</b>	<b>(0.01)</b>
<b>Operating Income</b>	<b>84.43</b>	<b>70.71</b>	<b>59.62</b>
<b>Operating Margin</b>	<b>40.4%</b>	<b>38.6%</b>	<b>36.7%</b>
<b>Total Operating Expense as % of Net Revenue</b>	<b>10.1%</b>	<b>11.1%</b>	<b>11.8%</b>

## II - 3. Non-Operating Items

(In NT\$ billions)	<u>3Q14</u>	<u>2Q14</u>	<u>3Q13</u>
<b>L-T Investments</b>	<b>1.04</b>	<b>1.05</b>	<b>1.11</b>
SSMC	0.52	0.58	0.52
Others	0.52	0.47	0.59
<b>Interest Expenses</b>	<b>(0.82)</b>	<b>(0.80)</b>	<b>(0.73)</b>
<b>Other Gains and Losses</b>	<b>0.73</b>	<b>3.13</b>	<b>(0.65)</b>
<b>Total Non-Operating Items</b>	<b>0.95</b>	<b>3.38</b>	<b>(0.27)</b>

## III. Financial Condition Review

### III - 1. Liquidity Analysis (Balance Sheet Items)

(In NT\$ billions)	<u>3Q14</u>	<u>2Q14</u>	<u>3Q13</u>
Cash & Marketable Securities	290.34	314.59	218.16
Accounts Receivable	114.53	86.89	79.67
Inventories	65.34	50.95	36.92
Other Current Assets	6.02	6.77	3.46
<b>Total Current Assets</b>	<b>476.23</b>	<b>459.20</b>	<b>338.21</b>
Short-term Loans	35.88	34.71	18.05
Accounts Payable	50.40	56.35	73.45
Dividends Payable	0.00	77.79	0.00
Accrued Liabilities and Others	85.97	77.79	56.78
<b>Total Current Liabilities</b>	<b>172.25</b>	<b>246.64</b>	<b>148.28</b>
Current Ratio (x)	2.8	1.9	2.3
<b>Net Working Capital</b>	<b>303.98</b>	<b>212.56</b>	<b>189.93</b>

### *Operating Income Analysis:*

Total operating expenses represented 10.1% of net revenues in 3Q14, down from 11.1% in the prior quarter, reflecting the benefit from operating leverage.

### *Non-Operating Items:*

Total non-operating items were a gain of NT\$0.95 billion in 3Q14, compared to a gain of NT\$3.38 billion in 2Q14.

The change mainly reflected the absence of other gains in 2Q14, including (1) a disposal gain of NT\$2.03 billion from the sell-down of 5% of Vanguard International Semiconductor Corp. (VIS) shares and (2) dividend income of NT\$ 0.64 billion, mostly from ASML.

### *Liquidity Analysis:*

At the end of 3Q14, cash and marketable securities decreased by NT\$24.25 billion to NT\$290.34 billion, primarily due to the payment of NT\$77.79 billion cash dividends, partially offset by free cash flow of NT\$43.37 billion generated (please refer to page 5) and cash dividends of NT\$3.24 billion received mainly from SSMC, VIS, and VisEra during the quarter.

Total current liabilities decreased by NT\$74.39 billion, mainly attributed to the cash dividend payment during the quarter.

Net working capital was NT\$303.98 billion and current ratio was 2.8x.

### III - 2. Receivable/Inventory Days

(In Number of Days)

	<u>3Q14</u>	<u>2Q14</u>	<u>3Q13</u>
Days of Receivable	44	40	45
Days of Inventory	56	51	45

### *Receivable and Inventory Days:*

Days of receivable increased by 4 days to 44 days, back to the Company's average days of receivable level.

Days of inventory increased by 5 days to 56 days, mainly reflecting higher work-in-process inventories due to longer cycle time of 20nm.

### III - 3. Debt Service

(In NTS billions)

	<u>3Q14</u>	<u>2Q14</u>	<u>3Q13</u>
Cash & Marketable Securities	290.34	314.59	218.16
Interest-Bearing Debts	<u>(248.50)</u>	<u>(246.37)</u>	<u>(229.28)</u>
<b>Net Cash Reserves</b>	<b>41.84</b>	<b>68.22</b>	<b>(11.12)</b>

### *Debt Service:*

Net cash reserves decreased NT\$26.38 billion to NT\$41.84 billion in 3Q14, reflecting a decrease of NT\$24.25 billion in cash and marketable securities and a slight increase of NT\$2.13 billion in interest-bearing debts.

## IV. Cash Flow

### IV - 1.1 Quarterly Cash Flow Analysis

(In NTS billions)

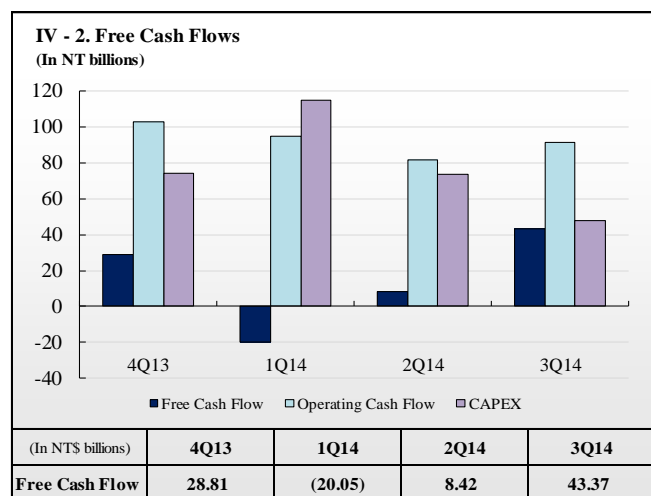
	<u>3Q14</u>	<u>2Q14</u>	<u>3Q13</u>
Income before Income Tax	85.38	74.10	59.35
Depreciation & Amortization	56.23	45.98	40.44
Other Operating Sources/(Uses)	(50.36)	(38.33)	(3.99)
<b>Total Operating Sources/(Uses)</b>	<b><u>91.25</u></b>	<b><u>81.75</u></b>	<b><u>95.80</u></b>
Capital Expenditures	(47.88)	(73.33)	(54.82)
Marketable Financial Instruments	0.48	2.42	0.33
Other Investing Sources/(Uses)	2.77	4.41	2.17
<b>Net Investing Sources/(Uses)</b>	<b><u>(44.63)</u></b>	<b><u>(66.50)</u></b>	<b><u>(52.32)</u></b>
Increase (Decrease) in Short-term Loans	1.39	10.40	(13.23)
Cash Dividends	(77.79)	0.00	(77.77)
Proceeds from Issuance of Bonds	0.00	0.00	41.20
Issuance of Long-term Bank Loans	0.00	0.00	0.04
Other Financing Sources/(Uses)	(1.86)	(0.05)	(1.74)
<b>Net Financing Sources/(Uses)</b>	<b><u>(78.26)</u></b>	<b><u>10.35</u></b>	<b><u>(51.50)</u></b>
<b>Exchange Rate Changes</b>	<b><u>2.47</u></b>	<b><u>(2.25)</u></b>	<b><u>(1.21)</u></b>
<b>Net Cash Position Changes</b>	<b>(29.17)</b>	<b>23.35</b>	<b>(9.23)</b>
<b>Ending Cash Balance</b>	<b>225.88</b>	<b>255.05</b>	<b>216.60</b>

### *Summary of Cash Flow:*

During the third quarter, cash generated from operating activities totaled NT\$91.25 billion, including (1) NT\$56.23 billion from depreciation & amortization expenses and (2) NT\$50.36 billion for other operating uses, which included an increase of NT\$27.64 billion in accounts receivable, an increase of NT\$14.39 billion in inventory, and the payment of 2013 employee profit sharing of NT\$12.24 billion.

The Company spent NT\$47.88 billion on capital expenditures, received NT\$3.24 billion cash dividends, and paid NT\$77.79 billion cash dividends.

As a result, our cash position decreased NT\$29.17 billion to NT\$225.88 billion at the end of 3Q14.



**Free Cash Flows:**

Free cash flow was NT\$43.37 billion in 3Q14, compared to NT\$8.42 billion last quarter, reflecting higher operating cash flow and lower capital expenditures during the third quarter.

**V. CapEx & Capacity**

V. Capital Expenditures and Capacity				
	<u>3Q14</u>	<u>2Q14</u>	<u>1Q14</u>	<u>YTD</u>
Capital Expenditures (in US\$ millions)	1,605	2,438	3,799	7,842
Capacity (kpcs 12 inch-equiv.)	2,175	1,949	1,870	5,994
Depreciation / Amortization (in NT\$ billions)	52.54	42.13	37.79	132.5

**Capital Expenditures and Capacity:**

Capital expenditures for TSMC on a consolidated basis totaled US\$1.61 billion in 3Q14.

Total capital expenditures in the first three quarters of 2014 were US\$7.84 billion.

Total capacity increased 11.6% to 2,175K 12-inch equivalent wafers in 3Q14.

On a full year basis, total capacity is expected to increase 11.8% year-over-year to reach 8,175K 12-inch equivalent wafers in 2014.

## VI. Recap of Recent Important Events & Announcements

- ARM and TSMC Unveil Roadmap for 64-bit ARM-based Processors on 10FinFET Process Technology ( 2014/10/02)
- TSMC and ARM set new Benchmarks for Performance and Power Efficiency with First Announced FinFET Silicon with 64-bit ARM big.LITTLE Technology ( 2014/09/30 )
- TSMC Launches Ultra-Low Power Technology Platform for IoT and Wearable Device Applications ( 2014/09/29 )
- TSMC Celebrates Upcoming Completion of Kaohsiung Gas Explosion Reconstruction Project ( 2014/09/27)
- TSMC Delivers First Fully Functional 16FinFET Networking Processor ( 2014/09/25 )
- TSMC Launches Fourth Quarter Recruitment Campaign ( 2014/09/24 )
- TSMC 28HPC Process in Volume Production ( 2014/09/12 )
- TSMC Named DJSI Industry Group Leader for Second Straight Year ( 2014/09/12 )