

2Q17

Quarterly Management Report
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Topics in This Report:

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

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

	<u>2Q17</u>	<u>1Q17</u>	<u>2Q16</u>	<u>QoQ</u>	<u>YoY</u>
EPS (NT\$ per common share)	2.56	3.38	2.80	-24.4%	-8.6%
(US\$ per ADR unit)	0.42	0.54	0.43	-24.4%	-8.6%
Net Revenue	213.86	233.91	221.81	-8.6%	-3.6%
Gross Profit	108.71	121.49	114.33	-10.5%	-4.9%
Gross Margin	50.8%	51.9%	51.5%		
Operating Expenses	(25.37)	(26.16)	(23.01)	-3.0%	10.2%
Other Operating Income and Expenses	(0.08)	0.02	(0.00)		
Operating Income	83.26	95.35	91.32	-12.7%	-8.8%
Operating Margin	38.9%	40.8%	41.2%		
Non-Operating Items	2.86	2.47	2.09		
Net Income Attributable to Shareholders of the Parent Company	66.27	87.63	72.51	-24.4%	-8.6%
Net Profit Margin	31.0%	37.5%	32.7%		
Wafer Shipment (kpcs 12 inch-equiv.)	2,533	2,473	2,297	2.4%	10.3%

*Note: Diluted weighted average outstanding shares were 25,930mn units in 2Q17***Financial Highlights:****Second Quarter 2017**

- Net revenue was NT\$213.86 billion, representing an 8.6% decrease from NT\$233.91 billion in 1Q17 and a 3.6% decrease from NT\$221.81 billion in 2Q16.
- Gross margin was 50.8%, 1.1 percentage points lower than 1Q17 and 0.7 percentage point lower than 2Q16.
- Operating margin was 38.9%, down 1.9 percentage points from 1Q17 and down 2.3 percentage points from 2Q16.
- Non-operating items were a gain of NT\$2.86 billion, compared to a gain of NT\$2.47 billion in 1Q17 and a gain of NT\$2.09 billion in 2Q16.
- Net income attributable to shareholders of the parent company was NT\$66.27 billion, down 24.4% from 1Q17 and down 8.6% from 2Q16. Net profit margin was 31.0% and diluted EPS was NT\$2.56.

I. Revenue Analysis

Wafer Revenue by Application	2Q17	1Q17	2Q16
Computer	8%	9%	8%
Communication	58%	61%	59%
Consumer	9%	9%	12%
Industrial/Standard	25%	21%	21%

Wafer Revenue by Technology	2Q17	1Q17	2Q16
10nm	1%	0%	0%
16/20nm	26%	31%	23%
28nm	27%	25%	28%
40/45nm	13%	13%	15%
65nm	10%	11%	12%
90nm	5%	4%	5%
0.11/0.13um	3%	2%	2%
0.15/0.18um	11%	11%	11%
0.25um and above	4%	3%	4%

Net Revenue by Geography	2Q17	1Q17	2Q16
North America	60%	63%	61%
Asia Pacific	14%	13%	18%
China	11%	11%	10%
EMEA	7%	6%	6%
Japan	8%	7%	5%

Revenue Analysis:

In the second quarter, revenue decreased 8.6% quarter-over-quarter, primarily attributable to supply chain inventory management, mobile product seasonality, and an unfavorable foreign exchange rate.

By application, Communication, Computer and Consumer decreased 10%, 14%, and 7% respectively, while Industrial/Standard increased 9%.

By technology, 10nm process technology contributed 1% of total wafer revenue in 2Q17. The combined 16/20nm contribution was 26% of total wafer revenue. Advanced technologies (28nm and below) accounted for 54% of total wafer revenue.

From a geographic perspective, revenue from customers based in North America accounted for 60% of total net revenue, while revenue from Asia Pacific, China, EMEA (Europe, Middle East, and Africa) and Japan accounted for 14%, 11%, 7%, and 8% of total net revenue, respectively.

II. Profit & Expense Analysis

II - 1. Gross Profit Analysis

(In NT\$ billions)	2Q17	1Q17	2Q16
Cost of Revenue	105.15	112.42	107.48
Gross Profit	108.71	121.49	114.33
Gross Margin	50.8%	51.9%	51.5%

Gross Profit Analysis:

Gross margin was 50.8% in 2Q17, 1.1 percentage points lower than 1Q17, mainly attributable to an unfavorable foreign exchange rate during the second quarter.

II - 2. Operating Income Analysis

(In NT\$ billions)	<u>2Q17</u>	<u>1Q17</u>	<u>2Q16</u>
Total Operating Expenses	(25.37)	(26.16)	(23.01)
Research & Development	(19.06)	(19.41)	(16.90)
SG&A	(6.31)	(6.75)	(6.11)
Other Operating Income and Expenses	(0.08)	0.02	(0.00)
Operating Income	83.26	95.35	91.32
Operating Margin	38.9%	40.8%	41.2%
Total Operating Expenses as % of Net Revenue	11.9%	11.1%	10.3%

Operating Income Analysis:

Total operating expenses decreased NT\$0.79 billion and represented 11.9% of net revenue in 2Q17.

II - 3. Non-Operating Items

(In NT\$ billions)	<u>2Q17</u>	<u>1Q17</u>	<u>2Q16</u>
L-T Investments	0.62	0.67	0.89
SSMC	0.43	0.39	0.48
Others	0.19	0.28	0.41
Net Interest Income (Expenses)	1.64	1.29	0.84
Other Gains and Losses	0.60	0.51	0.36
Total Non-Operating Items	2.86	2.47	2.09

Non-Operating Items:

Total non-operating items were a gain of NT\$2.86 billion in 2Q17, compared to a gain of NT\$2.47 billion in 1Q17.

II - 4. Net Profit and EPS

(In NT\$ billions)	<u>2Q17</u>	<u>1Q17</u>	<u>2Q16</u>
Income before Income Tax	86.12	97.82	93.41
Income Tax Expenses	(19.85)	(10.20)	(20.88)
Effective Tax Rate	23.2%	10.5%	22.6%
Net Income Attributable to the Parent Company	66.27	87.63	72.51
Net Profit Margin	31.0%	37.5%	32.7%
EPS (NT\$ per common share)	2.56	3.38	2.80

Net Profit and EPS:

Net income attributable to shareholders of the parent company was NT\$66.27 billion, down 24.4% from 1Q17, reflecting higher income tax expenses during the second quarter, which included the 10% tax on undistributed retained earnings.

III. Financial Condition Review

III - 1. Liquidity Analysis (Balance Sheet Items)

(In NT\$ billions)	<u>2Q17</u>	<u>1Q17</u>	<u>2Q16</u>
Cash & Marketable Securities	658.95	659.32	667.86
Accounts Receivable	110.33	109.03	111.72
Inventories	61.01	50.39	60.71
Other Current Assets	7.76	6.92	12.23
Total Current Assets	838.05	825.66	852.52
Short-term Loans	54.74	54.67	38.74
Accounts Payable	75.99	81.92	71.25
Current Portion of Bonds Payable and Bank Loans	79.87	44.91	22.01
Dividends Payable	181.63	0.00	155.70
Accrued Liabilities and Others	131.28	140.08	111.04
Total Current Liabilities	523.51	321.58	398.74
Current Ratio (x)	1.6	2.6	2.1
Net Working Capital	314.54	504.08	453.78

Liquidity Analysis:

At the end of 2Q17, cash and marketable securities remained essentially flat at NT\$658.95 billion, as cash increased by NT\$5.74 billion (please refer to page 5) while marketable securities decreased by NT\$6.11 billion.

Total current liabilities increased by NT\$201.93 billion, mainly reflecting the accrual of NT\$181.63 billion for cash dividends and an increase of NT\$34.96 billion in the current portion of bonds payable.

Net working capital was NT\$314.54 billion and current ratio was 1.6x.

III - 2. Receivable/Inventory Days

(In Number of Days)	<u>2Q17</u>	<u>1Q17</u>	<u>2Q16</u>
Days of Receivable	47	47	43
Days of Inventory	52	44	54

Receivable and Inventory Days:

Days of receivable remained at 47 days in 2Q17.

Days of inventory increased 8 days from 44 days in 1Q17 to 52 days in 2Q17, mainly due to a higher level of work-in-process inventories, driven by 10nm ramping.

III - 3. Debt Service

(In NT\$ billions)	<u>2Q17</u>	<u>1Q17</u>	<u>2Q16</u>
Cash & Marketable Securities	658.95	659.32	667.86
Interest-Bearing Debts	(233.93)	(233.79)	(242.05)
Net Cash Reserves	425.02	425.53	425.81

Debt Service:

Net cash reserves remained essentially flat at NT\$425.02 billion in 2Q17, as both cash & marketable securities and interest-bearing debts remained largely unchanged during the quarter.

IV. Cash Flow

IV - 1. Quarterly Cash Flow Analysis			
(In NT\$ billions)	2Q17	1Q17	2Q16
Income before Income Tax	86.12	97.82	93.41
Depreciation & Amortization	57.99	60.17	55.28
Other Operating Sources/(Uses)	(40.71)	3.02	(42.01)
Total Operating Sources/(Uses)	103.40	161.01	106.68
Capital Expenditures	(105.19)	(102.51)	(73.59)
Marketable Financial Instruments	5.18	(7.53)	(22.07)
Other Investing Sources/(Uses)	1.79	0.81	0.95
Net Investing Sources/(Uses)	(98.22)	(109.23)	(94.71)
Increase (Decrease) in Short-term Loans	(0.04)	(0.25)	3.96
Other Financing Sources/(Uses)	(0.60)	(11.66)	(12.06)
Net Financing Sources/(Uses)	(0.64)	(11.91)	(8.10)
Exchange Rate Changes and Other	1.20	(16.39)	0.51
Net Cash Position Changes	5.74	23.48	4.38
Ending Cash Balance	570.47	564.73	622.36

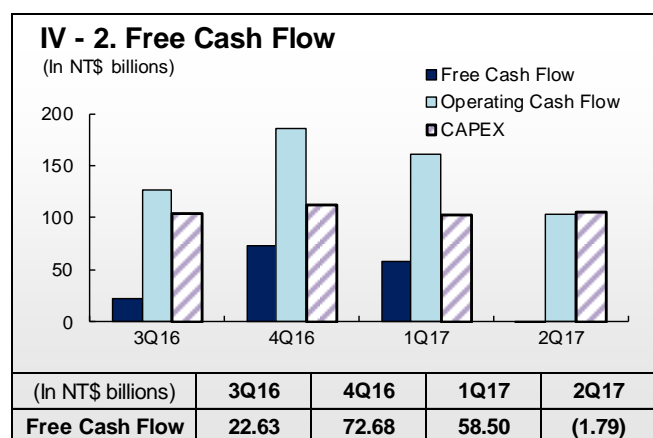
Summary of Cash Flow:

During the second quarter, cash generated from operating activities totaled NT\$103.40 billion, including (1) NT\$86.12 billion from income before income tax, (2) NT\$57.99 billion from depreciation & amortization expenses and (3) NT\$40.71 billion for other operating uses, which included income tax payment of NT\$38.79 billion.

Net cash used in investing activities was NT\$98.22 billion in 2Q17, mainly reflecting capital expenditures of NT\$105.19 billion, partially offset by a net decrease of NT\$5.08 billion in fixed income securities.

Net cash used in financing activities was NT\$0.64 billion.

As a result, net cash position increased NT\$5.74 billion to NT\$570.47 billion at the end of 2Q17.



Operating and Free Cash Flow:

Free cash flow was an outflow of NT\$1.79 billion in 2Q17, as capital expenditures were slightly higher than operating cash flow during the quarter.

V. CapEx

V. Capital Expenditures			
(in US\$ billions)	2Q17	1Q17	YTD
Capital Expenditures	3.47	3.29	6.76

Capital Expenditures:

Capital expenditures for TSMC on a consolidated basis totaled US\$3.47 billion in 2Q17. The Company maintains its full year capital budget to be about US\$10 billion.

VI. Recap of Recent Important Events & Announcements

- TSMC Board of Directors Sets June 26 as Ex-dividend Date and July 2 as Record Date for Common Share Dividends (2017/06/08)
- TSMC Shareholders Approve NT\$7 Cash Dividend and Elect Dr. Mark Liu and Dr. C.C. Wei as Board of Directors (2017/06/08)
- TSMC Promotes Dave Keller to President, TSMC North America (2017/06/07)
- TSMC Board of Directors Approved the Establishment of TSMC Charity Foundation with Donation of NT\$30,000,000 as Its Initial Capital (2017/05/09)