MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

TELEFONICA CELULAR DEL PARAGUAY S.A.

As at and for the six-month period ended 30 June 2016

We believe in better. We believe in tigo

1. Overview

We are a leading multinational telecommunications and media group operating in Paraguay. We provide a wide range of mobile communications and cable services, as well as other related products, including MFS, digital media and e-commerce, to residential, business and wholesale customers. We hold the number one position in the market on our mobile business. As of 30 June 2016, we had over 3.79 million mobile customers, provided cable services to 389.8 thousand households (HFC only) and had 1.31 million MFS customers. In the six-month period ended June 2016, we generated PYG 1.583 billion in revenue and an EBITDA of PYG 717.1 billion.

2. Recent Developments

2.1 Acquisitions or disposals

On 27 February 2015 Telefónica Celular del Paraguay S.A. (The “Company” or “Telecel”) concluded the process of selling the fully-owned company Unicanal S.A. (99% of shares) to Grupo JBB, a Paraguayan multimedia group, by finishing the negotiations and transferring all the resources and facilities of this business unit to the buyer. The transaction amount was USD 3.65 million of which USD 2.5 million was collected in cash at the time of the transference in February 2015. The outstanding balance was collected on November 2015.

3. Key factors affecting the Telecel’s business

Our performance and results of operations have been and will continue to be affected by a number of internal and external factors. The key factors that have had or, in the future, may have an effect on the results of our operations are set forth below:

3.1 Drivers for revenue growth

We generate revenue mainly from fees associated with communication, entertainment, data, information and financial services that we provide to our customers, including: airtime and data usage fees, roaming fees, interconnection fees, connection fees, monthly subscription fees, broadband internet, fixed-line telephone, VoIP, data transmission, mobile money transfer and related financial services, cable TV, sale of content and other services and sales of equipment. We generally seek to increase our revenue through growth of our customer base and introduction of new products and VAS. Our results of operations are therefore dependent on our customer base and the number of services that each customer uses. Our monthly ARPU, calculated based on historical exchange rates for the applicable periods, decreased from $9.8 in June 2015 to $8.6 in June 2016 mainly due to 16.5% higher foreign exchange rate. ARPU increased 2.6% YoY in local currency due, in part, to higher revenue due the progressive smartisation of the base and its resulting increase in mobile data consumption which increase revenue.

Customers

Mobile customers

Our mobile customer numbers as of 30 June 2016, 2015 and 2014 were as follows:

In millions	Period ended 30 June		
	2016	2015	2014
Mobile customers at the end of the period	3.79	3.95	3.79

As of 30 June 2016, our total mobile customer base decreased by 4.1% to 3.79 million from 3.95 million as of 30 June 2015. Prepaid customers accounted for 76.6%, or 2.9 million, of the total mobile customers as of 30 June 2016. We continue to focus on attracting higher quality customers in these more penetrated markets and set subsidy levels that support and attract migration from voice to data services. In Paraguay, our total amount of mobile customers increased as a result of customer acquisition measures and improved Net Promoter Score (NPS) in relation to December 2014.

Cable customers

As of 30 June 2016, our cable business covers approximately 389.8 thousand homes in Paraguay, and we provide services to approximately 254.6 thousand RGUs (HFC only). Our cable customers are offered a full consolidated suite of services, including cable TV, internet and other digital services. Our cable TV services are generally the first point of entry into our customers' homes, which allows us to increase our penetration by offering internet and mobile services as well, which we believe creates a strong brand affinity. Our aim is to increase our customer take-up of services by investing in network upgrades so it becomes bidirectional (allowing both uploads and downloads over a communication line) and both broadband internet and cable TV can be accommodated within it.

New products and services

Innovation continues to be a major focus as we seek to grow revenue by developing and selling additional products and services through which we can gain a greater share of the disposable income of our customers. Selling new VAS, and other data services to our existing customers increases ARPU and decreases churn. The introduction of innovative or exclusive products and services also helps us to attract new customers, increasing revenue.

In order to improve our clients' level of satisfaction we have developed post-paid plans in bundle format that are tailored according to their consumption. These bundles, which were launched in August 2015, allow clients to make a better use of their credit and helped the company to improve ARPU and reduce the deferred revenue liability.

During the six month period ended 30 June 2016, VAS as a percentage of our total revenue increased to 57.3%, compared to 53.6% during the same period of 2015, respectively. Growth in our data revenues has outpaced revenue growth from voice and SMS usage. Our mobile data customers and revenue in local currency increased by 32.7% and 32.6%, respectively, from June 2015 to 2016. We expect innovation to be a key driver of growth in the years ahead as data and internet-related services make an increasingly substantial contribution to the business.

Capital expenditure to expand and improve our networks and increase our footprint

We consistently improve the quality and increase the coverage of our mobile and cable networks, which requires purchasing new licenses and spectrum, investing in new infrastructure, and modernizing and upgrading our networks and IT backbones. Spending money on capital expenditures ultimately increases our revenue and operating profit, but it also decreases our investing cash flows, our carrying value of property, plant and equipment and intangible assets, and increase depreciation and amortization expense. In addition, as customers increase their utilization of our networks, we incur higher operating expenses, including interconnection charges, network operation and maintenance costs, employee costs and selling, general and administrative expenses.

Capital expenditure during fiscal 2015 resulted in improvements in the quality of our networks and increased capacity and coverage. In the six month period ended 30 June 2016, we invested PYG 472.6 billion in capital expenditure, which represented an amount equal to 29.9% of our total revenue.

Competitive and regulatory pressures on pricing

The market in which we operate is competitive in nature, and we expect competition will remain high. Mobile telecommunications operators compete for customers principally on the basis of price, services offered, advertising and brand image, quality and reliability of service and coverage area. Price competition is significant on voice and SMS services, which still represent an important portion of our revenue (together they represented 47.5% of our revenue in June 2014, 40.7% in 2015 and 34.3% in 2016) but they are largely commoditized, as the ability to differentiate these services among operators is limited and penetration is high.

Pricing pressure has resulted in a decline in ARPU, since clients have been shifting from high margin products such as voice and SMS to mobile data products thanks to the variety of OTT services available to them, which constitutes a challenge to develop innovative products that could at the same time balance client satisfaction and profitability.

The prices we are allowed to charge our customers are also heavily regulated which may result in reduced profitability. For example, in Paraguay, we can no longer set an expiry date to our customer's balance of prepaid minutes or SMS bundles, which hinders revenue recognition and affects margins of mobile services. Changes such as these require us to monitor our pricing models and margins consistently to adjust them if required.

Effect of exchange rate fluctuations

The exchange rate for the Paraguayan Guarani fluctuates in relation to the U.S. dollar and such fluctuations may have a material adverse effect on our earnings, assets and liabilities valuation or cash flows. Exchange rates affects our earnings and cash flows due to U.S. dollar-denominated debt held at the local operational level, in a market where local currency borrowing facilities are either not available or cannot be obtained under commercially acceptable terms.

The effect of the increase in the PYG/USD exchange rate has greatly affected our Net Profit as of 31 December, 2015. However, during the six month period 30 June 2016, the US dollar decreased its value against Paraguayan Guarani by 1% which produced and exchange gain of PYG 99,432 as of 30 June 2016.

Results of Operations

Six month period ended 30 June 2016 and 2015

PYG millions	Year ended 30 June		Percent change
	2016	2015	
Revenue	1,582,725	1,559,983	1.5%
Cost of sales	(375,481)	(370,104)	1.5%
Gross profit	**1,207,244**	**1,189,879**	**1.5%**
Operating expenses	(490,184)	(560,560)	(12.6%)
Depreciation	(169,153)	(154,846)	9.2%
Amortization	(61,407)	(59,867)	2.6%
Other operating income (expenses), net	(991)	(12,346)	(108.0%)
Operating profit	**485,509**	**426,952**	**13.7%**
Interest expense	(91,689)	(60,197)	52.3%
Interest and other financial income	4,853	3,990	21.6%
Exchange loss, net	99,432	(201,470)	149.4%
Profit before tax	**498,105**	**169,275**	**194.3%**
Income tax expense	(66,581)	(27,702)	140.3%
Net profit and comprehensive income for the period.	**431,524**	**141,573**	**204.8%**

Operating Data:			
Number of mobile subscribers	**3,786,789**	**3,947,891**	**(4.1%)**
Postpaid	885,499	908,271	(2.5%)
Prepaid	2,901,290	3,039,620	(4.6%)
Monthly churn %			
Postpaid handset	2.2%	1.7%	34.4%
Postpaid datacard	5.1%	4.0%	27.6%
Total postpaid	2.3%	1.8%	30.3%
Prepaid handset	2.8%	2.1%	31.7%
Prepaid datacard	8.3%	8.4%	(1.5%)
Total prepaid	2.8%	2.1%	30.6%
Total monthly churn (1)	2.7%	2.0%	30.5%
Monthly ARPU (US$) (2)			
Postpaid	18.3	19.7	(7.0%)
Prepaid	5.6	6.2	(8.8%)
Total monthly ARPU (3)	8.6	9.3	(7.4%)
Number of employees	**1,076**	**785**	**37.1%**

(1) Our total monthly churn is individually calculated by reference to our aggregate prepaid and postpaid customers.

(2) ARPU is calculated based on a historical exchange rate of 5,708 and 4,898 to US$1.00 in 30 June 2016 and 2015, respectively.

(3) Our total ARPU is individually calculated by reference to our aggregate prepaid and postpaid customers.

Revenue

Total revenue increased by 1.5% for the six month period ended 30 June 2016 to PYG 1.583 billion from PYG 1.560 billion for the same period of 2015. The increase was due to higher VAS revenue (8.4%) compensated by lower revenue from voice revenue (-9.9%). Our recurring revenue from value-added services represents 65.1% of total recurring revenue for the six month period ended 30 June 2016, versus 60.8% in the same period of 2015.

The cable TV business has contributed revenue of PYG 142.9 billion during 2016 in comparison to PYG 153.6 billion in 2015.

Customer base

As of 30 June 2016, our total mobile customer base was 3,786,789, which represents a decrease of 4.1% from 3,947,891 as of 30 June 2015, with prepaid customers accounting for 76.6% or 2,901,290 of our total mobile customers at such date. Additionally we have been investing in improvements in the quality of our networks and increased capacity and coverage, something that we believe has helped to retain our customer base and keep it satisfied. Strengthening our network distribution has also helped making our products more accessible.

Cost of sales

Cost of sales increased by 1.5% for the six month period ended 30 June 2016 to PYG 375.5 billion from PYG 370.1 billion for the same period in 2015. Our cost of sales is affected by higher Data Direct costs due to strong adoption of smartphone, by customer base and increased mobile data usage in comparison to the previous year to smartphones and mobile data during 2015. Interconnection costs decreased 0.3% YoY due to regulatory measures. Bad debt increased by 37.9% YoY. Some costs such as voice and SMS decreased in line with the decrease of revenue related to those concepts.

Gross profit margin has maintained to 76.3% for the six month period ended 30 June 2016 from 76.3% for the same period of 2015.

Operating expenses

Operating expenses decreased by 12.6% for the six months ended 30 June 2016 to PYG 490 billion from PYG 560.6 billion for the same period ended 30 June 2015. The decrease was mainly attributable to savings in technical service fees, acquisition commission (40%) and phone subsidies (-10%). As a percentage of revenue, general and administrative expenses decreased to 31% for the period ended 30 June 2016 from 35.9% in 2015.

EBITDA

	Year ended 30 June	
	2016	2015
EBITDA	717,060	708,430
EBITDA margin (1)	45.3%	45.4%
Net debt to LTM EBITDA (2)	1.48	1.02
Total debt to LTM EBITDA (3)	1.57	1.50

(1) We define EBITDA Margin as our EBITDA divided by revenue. EBITDA Margin is not a recognized term or measure of performance under IFRS.

(2) We calculate Net debt to LTM EBITDA by dividing our total borrowings, less cash and cash equivalents, by our EBITDA from the six months ended 30 June 2016.

(3) We calculate Total debt to EBITDA by dividing our total borrowings by our LTM EBITDA.

Operating profit

Operating profit increased by 13.7% for the six month period ended 30 June 2016 to PYG 485.5 billion from PYG 427 billion for the same period ended 30 June 2015. The operating margin increased from 30.7% at end of 30 June 2015 to 27.4% in 30 June 2016. This increase was mainly because of reduced technical service fees and the other expenses remaining relatively constant. In Other operating income (expenses), net, the results from the sale of Unicanal improved our operating profit as of 30 June 2015, however in 2016 we did not sell any significant asset.

Net finance costs

Net finance costs, which include interest expense, net of interest income, increased by 54.5% in the six month period ended 30 June 2016 to PYG 86.8 billion from PYG 56.2 billion for the same period ended 30 June. This increase was mainly due to higher interest accretion from external debt and football rights and the effect of increased foreign exchange rate on our financial debt which is 76% denominated in US Dollars.

Foreign exchange gain (loss)

Exchange gain, net increased by 149% at the end of June, 2016 to a net gain of PYG 99.4 billion from a net loss of PYG 201.5 billion at the end of June, 2015. Exchange gains and losses arise primarily as a result of movements in the PYG/USD exchange rate which affect the valuation of our U.S. dollar borrowings, trade payables, receivables, supplier advances and cash and cash equivalents. The majority of our borrowings and cash and cash equivalents are denominated in U.S. dollars. The PYG/USD exchange rate moved from 5,807.9 as of 31 December, 2015 to 5,589 as of 30 June 2016.

Charge for taxes

The charge for taxes increased by 140.3%, to PYG 66.6 billion As of 30 June 2016, from PYG 27.7 billion for the same period ended 30 June 2015, due primarily to increased profit before tax produced by reduced operating expenses and foreign exchange gain. The effective tax rate for the period ended 30 June 2016 was 13.4% compared to 16.4% for the same period ended 30 June 2015.

Net profit for the period

Net profit at the end of 30 June 2016 increased by 205% to PYG 431.5 billion compared to a net profit of PYG 141.6 billion at the end of 30 June 2015.

Trend Information

Our strategy is to maintain our voice and SMS revenue and market share while growing our revenue in value-added products and services such as mobile internet access, content downloads, and music and video streaming. In the six month period ended 30 June 2016, value-added services represent 65.1% of recurring revenue, versus 60.8% in the same period ended 30 June 2015. Data usage is increasing among consumers as a result of an increasingly digital lifestyle. At the same time, smartphone market penetration is increasing as a result of lower prices and more phone options available to consumers. We expect innovation to be an important driver of growth in the years ahead. Although these new services tend to have lower profit margins than our core communications business, we aim to limit any drop in margins by controlling costs and through economies of scale. New competitors entering our markets and/or price competition could erode the profitability of our mobile operations.

Revenue from our cable business, which includes TV and broadband internet, decreased by 10.2% in the year 30 June 2016 to PYG 174.7 billion from PYG 194.6 in 30 June 2015. We expect increasing growth, especially in the broadband business, with the expansion of our network.

Liquidity and Capital Resources

Historically we have relied, and in the future we intend to continue to rely, primarily on cash from operations and external financings to fund our operations, capital expenditures and working capital requirements. The variation is related to the obtainment of the license to operate in the 4G/LTE technology in the first half of 2016.

We intend to continue to focus on investments in property, systems and equipment (fixed assets) and working capital management, including timely collection of accounts receivable and efficient management of accounts payable.

Capital Expenditures

Our capital expenditures on property, plant and equipment, licenses and other intangible assets for the six month period ended 30 June 2016 and 2015 amounted to PYG 472 billion and PYG 242 billion, respectively.

Financing

As of 30 June 2016, our total outstanding indebtedness and other financing was PYG 2,266 billion. As of 31 December, 2015, our total outstanding indebtedness and other financing was PYG 2,390 billion.

Our interest expense for the period ended 30 June 2016 was PYG 91.7 billion and for the same period ended 30 June 2015 was PYG 60.2 billion.

Cash Flows

The table below sets forth our cash flows for the periods indicated:

PYG millions	Year ended 30 June	
	2016	2015
Net cash provided by operating activities	587,186	319,432
Net cash used in investing activities	(556,718)	(377,107)
Net cash used in financing activities	(109,750)	(95,379)
Net (decrease) increase in cash and cash equivalents	**(79,282)**	**(153,054)**
Cash and cash equivalents at the end of the period	124,702	201,046

For the six month period ended 30 June 2016 cash provided by operating activities was PYG 587.2 billion compared to PYG 319.4 billion for the same period ended 30 June 2015. The increase was mainly due to higher financing obtained from suppliers and reduced operating expenses.

For the six month period ended 30 June 2016 cash provided by investing activities was PYG (556.7) billion compared to PYG (377.1) billion for the same period ended 30 June 2015, mainly due to increased addition of intangible assets related to the 4G/LTE license.

For the six month period ended 30 June 2016 cash provided by financing activities was PYG (109,8) billion compared to PYG (95.4) billion for the same period ended 30 June 2015. The variation is mainly due to repayment of loans, reduced proceeds from the insurance of debt and financing and decreased payment of dividends in the period.

The net decrease in cash and cash equivalents for the six month period ended 30 June 2016 was PYG (79.3) billion compared to PYG (153.1) billion for the same period of 2015. We had closing cash and cash equivalents of PYG 124.7 billion as of 30 June 2016 compared to PYG 201 billion as of 30 June 2015.

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