TELEFONICA CELULAR DEL PARAGUAY S.A.

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

As at and for the nine-month period ended September 30, 2015

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 September 30, 2015, we had over 3.91 million mobile customers, provided cable services to 351.5 thousand households (HFC only) and had 1.34 million MFS customers. In the nine-month period ended September 2015, we generated Gs.2,361 million in revenue and an EBITDA of Gs.1.074 million.

2. Recent Developments

2.1 Acquisitions or disposals

On February 27, 2015 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 balance will be collected in November 2015.

3. Key factors affecting the Telefónica Celular del Paraguay S.A.'s business

Our performance and results of operations have been and will continue to be affected by a number of factors, including external factors. Certain of these key factors that have had, or 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 the communication, entertainment, data, information and financial services we provide to our customers, such as 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 the growth of our customer base and through the 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, which we measure using ARPU. Our monthly ARPU, calculated based on historical exchange rates for the applicable periods, as indicated in our interim condensed consolidated financial statements, decreased from $10.9 in September 2014 to $8.8 in September, 2015 mainly due to 19.2% higher foreign exchange rate. ARPU decreased 3.1% YoY in local currency due to due in part to pricing pressures and increased competition.

Customers

Mobile customers

Our mobile customer numbers as of September 30, 2013, 2014 and 2015 were as follows:

In millions	Period ended September 30,		
	2015	2014	2013
Mobile customers at the end of the period	3.91	3.84	3.91

As of September 30, 2015, our total mobile customer base increased by 1.6% to 3.91 million from 3.84 million as of September 30, 2014. Prepaid customers accounted for 76.6%, or 3 million, of the total mobile customers as of September 30, 2015. 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. In Paraguay, total mobile customers amount increased as a result of customer acquisition measures and improved Net Promoter Score (NPS) in relation to September 2014.

Cable customers

Our cable business covers approximately 351.5 thousand homes in Paraguay, and we provided services to approximately 236.8 thousand RGUs (HFC only). We offer our cable customers 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 stronger brand affinity. Our aim is to increase our customer take-up of services by investing in network upgrades so that they are bidirectional (allowing both uploads and downloads over a communication line) and both broadband internet and cable TV can be accommodated.

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 September 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 nine-month period ended September 30, 2015, VAS as a percentage of our total revenue increased to 54.2%, compared to 53.8% and 53.7% during the same period of 2014 and 2013, respectively. Growth in our data revenues has outpaced revenue growth from voice and SMS usage. Our mobile data customers and revenue in local currency grew by 17.1% and 36.6%, respectively, from September 2014 to 2015. 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 our 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, which attracted additional customers. In the nine-month period ended September 30, 2015, we invested Gs.413 million in capital expenditure, which represented an amount equal to 17.5% of our total revenue.

Competitive and regulatory pressures on pricing

The markets in which we operate are competitive in nature, and we expect that competition will continue to 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 the vast majority of our revenue (together they represented 51.9% of our revenue in September 2013, 46.8% in 2014 and 39.8% in 2015) but they are largely commoditized, as the ability to differentiate these services among operators is limited and penetration is high. Competition has resulted in pricing pressure, reduced margins and profitability, increased customer churn and the loss of revenue and market share.

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.

Cost optimization and efficiencies

In fiscal year 2014, we started to implement several restructuring and efficiency initiatives that we believe will result in future cost savings and efficiency but could also produce one-off costs and expenses that will be necessary to implement them. As of September 30, 2015, the measures adopted made our costs to decrease 7.4% and improved our gross margin and operating profit by 2pp and 11.7%, respectively.

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.

Results of Operations

Nine-month period ended September 30, 2015 and 2014

PYG millions	Nine months ended September 30,		Percent change
	2015	2014	
Revenue	2,360,895	2,389,127	(1.2%)
Cost of sales	(552,228)	(596,456)	(7.4%)
Gross profit	**1,808,667**	**1,792,671**	**0.9%**
Sales and marketing	(488,424)	(429,413)	13.7%
General and administrative expenses	(246,043)	(202,336)	21.6%
EBITDA	**1,074,200**	**1,160,922**	**(7.5%)**
Depreciation	(232,506)	(228,820)	1.6%
Amortization	(89,809)	(79,955)	12.3%
Other operating income (expenses), net	(74,053)	(245,498)	(69.8%)
Operating profit	**677,832**	**606,649**	**11.7%**
Interest expense	(100,343)	(87,931)	14.1%
Interest and other financial income	6,161	6,099	1.0%
Exchange loss, net	(350,483)	16,024	(2287.2%)
Profit before tax	**233,167**	**540,841**	**(56.9%)**
Income tax expense	(46,297)	(104,471)	(55.7%)
Net profit and comprehensive income for the period.	**186,870**	**436,370**	**(57.2%)**

Operating Data:			
Number of mobile subscribers	**3,909,557**	**3,846,778**	**1.6%**
Postpaid	914,096	888,785	2.8%
Prepaid	2,995,461	2,957,993	1.3%
Monthly churn %			
Postpaid handset	1.9%	1.3%	45.2%
Postpaid datacard	5.2%	4.4%	18.8%
Total postpaid	2.0%	1.5%	32.9%
Prepaid handset	1.7%	2.2%	(23.8%)
Prepaid datacard	7.9%	5.0%	57.6%
Total prepaid	1.7%	2.2%	(23.5%)
Total monthly churn (1)	1.8%	2.0%	(13.8%)
Monthly ARPU (US$) (2)			
Postpaid	20.0	22.0	(8.9%)
Prepaid	6.5	8.1	(20.4%)
Total monthly ARPU (3)	9.6	11.3	(14.8%)
Number of employees	**714**	**748**	**(4.5%)**

(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 5,636 and 4,492 to US$1.00 in September 30, 2015 and 2014, respectively.

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

Revenue

Total revenue decreased by 1.2% for the nine-month period ended September 30, 2015 to Gs.2,360,895 million from Gs.2,389,127 million for the same period of 2014. The decrease was due to less voice (-7.8%) and VAS (0.4%) revenue compensated with higher revenue from T&E revenue (+23.9%). Our recurring revenue from value-added services represents 61.4% of total recurring revenue for the nine-month period ended September 30, 2015, versus 59.5% in the same period of 2014.

The cable TV business has contributed revenue of Gs.236,470 million during Q3, 2015 in comparison to Gs.237,495 million in Q3, 2014.

Customer base

As of September 30, 2015, our total mobile customer base was 3,909,557, which represents an increase of 1.6% from 3,846,778 as of September 30, 2014, with prepaid customers accounting for 76.6% or 2,995,461 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 keep our customers during the period despite the high level of penetration in the Paraguayan market. Strengthening our network distribution has also helped making our products more accessible.

Cost of sales

Cost of sales decreased by 7.4% for the year ended September 30, 2015 to Gs.552,228 million from Gs.596,456 million for the same period in 2014. Our cost of sales is affected by higher T&E costs due to strong campaigns to push adoption of smartphones and mobile data during 2015. Increase in cable TV programing costs in line with incremental revenue from Tigo Home. Interconnection costs decreased 32.1% YoY due to regulatory measures, there is also a decrease in bad debt by 19.1%. Some costs such as voice and SMS decreased in line with the decrease of revenue related to those concepts.

Gross profit margin increased to 76.6% for the nine months ended September 30, 2015 from 75% for the same period of 2014, primarily from reduction of costs in the mobile business and higher revenue from TV business.

Sales and marketing

Sales and marketing expenses increased by 13.7% for the nine months ended September 30, 2015 to Gs.488,424 million from Gs.429,413 million for the same period ended September 30, 2014. Sales and marketing costs were comprised mainly of commissions to dealers for the sale of prepaid reloads (-6.1% YoY) smartphone subsidies aimed at obtaining and maintaining customers (+17% YoY), as well as general advertising and promotion costs (+43.2% YoY).

General and administrative expenses

General and administrative expenses increased by 21.6% for the nine months ended September 30, 2015 to Gs.246,043 million from Gs.202,336 million for the same period in 2014. The increase was mainly attributable to higher ERC, external services, billing costs and network maintenance costs as a result of our continued network expansion. As a percentage of revenue, general and administrative expenses increased to 10.4% for the period ended September 30, 2015 from 8.5% in 2014.

EBITDA

	Period ended September 30	
	2015	2014
EBITDA	1,074,199	1,160,922
EBITDA margin (1)	45.5%	48.6%
Net debt to LTM EBITDA (2)	1.12	0.76
Total debt to LTM EBITDA (3)	1.45	0.95

(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 twelve months ended September 30, 2015.

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

Operating profit

Operating profit increased by 11.7% for the nine-month period ended September 30, 2015 to Gs.677,832 million from Gs.606,649 million for the same period ended September 30, 2014. The operating margin increased from 25.4% at end of September 30, 2014 to 28.7% in September 30, 2015. This increase was mainly because of the savings performed in costs and reduced technical service fees in other operating expenses.

Net finance costs

Net finance costs, which include interest expense, net of interest income, increased by 15.1% in the nine-month period ended September 30, 2015 to Gs.94,181 million from Gs.81,832 million for the same period ended September 30. This increase was mainly due to higher interest accretion on financing of football rights and the effect of increased foreign exchange rate on our financial debt which is 87% denominated in US Dollars.

Foreign exchange gain (loss)

Exchange loss, net increased by 2287% at the end of September, 2015 to a net loss of Gs.350,483 million from a net gain of Gs.16,024 million at the end of September, 2014. Exchange gains and losses resulted primarily as a result of movements in the PYG/USD exchange rate resulting in a revaluation of our U.S. dollar borrowings, trade payables, receivables, suppliers 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 4,492 as of September 30, 2014 to 5,636 as of September 30, 2015.

Charge for taxes

The charge for taxes decreased by 55.7%, to Gs.46,297 million as of September 30, 2015, from Gs.104,471 million for the same period ended September 30, 2014, due primarily to profit before tax produced by higher financial expenses and net exchange loss which are tax-deductible. The effective tax rate for the period ended September 30, 2015 was 19.9% compared to 19.3% for the same period ended September 30, 2014.

Net profit for the period

Net profit at the end of September 30, 2015 decreased by 57% to Gs.186,870 million compared to a net profit of Gs.436,370 million at the end of September 30, 2014.

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 nine-month period ended September 30, 2015, value-added services represent 61.4% of recurring revenue, versus 59.5% in the same period ended September 30, 2014. 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, increased by 3.36% in the nine month period September 30, 2015 to Gs. 293,302 million from Gs. 283,756 in September 30, 2014. 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.

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 nine-month period ended September 30, 2015 and 2014 amounted to Gs.413,369 million and Gs.309,438 million, respectively.

Financing

As of September 30, 2015, our total outstanding indebtedness and other financing was Gs.2,133,817 million. As of December 31, 2014, our total outstanding indebtedness and other financing was Gs.1,571,118 million.

Our interest expense for the period ended September 30, 2015 was Gs.100,343 million and for the same period ended September 30, 2014 was Gs.87,931 million.

Cash Flows

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

PYG millions	Year ended September 30,	
	2015	2014
Net cash provided by operating activities	424,577	742,892
Net cash used in investing activities	(677,289)	(303,936)
Net cash used in financing activities	380,271	(764,090)
Net (decrease) increase in cash and cash equivalents	**127,559**	**(325,134)**
Cash and cash equivalents at the end of the period	481,659	310,333

For the nine-month period ended September 30, 2015 cash provided by operating activities was Gs.424,577 million compared to Gs.742,892 million for the same period ended September 30, 2014. The decrease was mainly due to reduced revenue and higher payments to suppliers.

For the nine-month period ended September 30, 2015 cash provided by investing activities was Gs.(677,289) million compared to Gs.(303,936) million for the same period ended September 30, 2014, mainly due to higher financing granted to related parties and higher investments in PP&E than the previous year.

For the nine-month period ended September 30, 2015 cash provided by financing activities was Gs.380,271 million compared to Gs.(764,090) million for the same period ended September 30, 2014. The variation of cash used for financing activities during the nine-month period ended September 30, 2015 is mainly due to 63% less dividends paid than in the previous year and new financing obtained during the current year.

The net increase in cash and cash equivalents for the nine-month period ended September 30, 2015 was Gs.127,559 million compared to Gs.(325,134) million for the same period of 2014. We had closing cash and cash equivalents of Gs.481,659 million as of September 30, 2015 compared to Gs.310,333 million as of September 30, 2014.

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