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

TELEFONICA CELULAR DEL PARAGUAY S.A.

As at and for the three month period ended 31 March 2017

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 31 March 2017, we had over 3.84 million mobile customers, provided cable services to 377.7 thousand households (HFC only) and had 1.31 million MFS customers. In the three-month period ended 31 March 2017, we generated Gs.782.9 billion in revenue and an EBITDA of Gs.353.5 billion.

2. Recent Developments

2.1 Acquisitions or disposals

During the three month period ended 31 March 2017 and 2016, the Group did not make any significant acquisition or disposal.

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 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, increased from $8.8 in March 2016 to $9.5 in March 2017 mainly due to 2% lower foreign exchange rate. ARPU increased 5.6% 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 31 March, 2017, 2016 and 2015 were as follows:

In millions	Period ended 31 March		
	2017	2016	2015
Mobile customers at the end of the period	3.57	3.84	3.94

As of 31 March 2017, our total mobile customer base decreased by 7.2% to 3.57 million from 3.84 million as of 31 March 2016. Prepaid customers accounted for 75.6%, or 2.7 million, of the total mobile customers as of 31 March 2017.

Cable customers

As of 31 March, our cable business covers approximately 436.6 thousand homes in Paraguay, and we provide services to approximately 277.4 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 three month period ended 31 March 2017, VAS as a percentage of our total revenue increased to 62%, compared to 56.8% and 53.4% during the same period of 2016 and 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 grew by 10% and 93.8%, respectively, from March 2016 to 2017. 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, which attracted additional customers. In the year ended 31 December 2016, we invested Gs.820 billion in capital expenditure, which represented an amount equal to 26.3% of our total revenue.

Competitive and regulatory pressures on pricing

The markets in which we operate are 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 42.6% of our revenue in March 2015, 36.2% in 2016 and 31.4% in 2017) 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, and since this year, it also applies to data balances, 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 produced cost savings and efficiencies in 2016. In fiscal year 2017, we adjusted the accrued income and accrued expenses, as part of a review and analysis of accounts compositions. As of 31 March 2017, our costs decreased 20.2% which slightly increased our gross margin and EBITDA by 4.3pp and 4.9pp, respectively.

EBITDA in the quarter includes a benefit from a $6 million one-time provision reversal. Excluding this impact, EBITDA would have grown 9% on an organic basis, and the EBITDA margin would have been 45.6% in the quarter.

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 not affected significantly our Net Profit as of 31 March 2017.

Results of Operations

Three month period ended 31 March, 2017 and 2016

PYG millions	Year ended 31 March		Percent change
	2017	2016	
Revenue	761,058	782,947	(2.8%)
Cost of sales	(151,244)	(189,566)	(20.2%)
Gross profit	**609,814**	**593,381**	**2.8%**
Operating expenses	(229,093)	(239,882)	(4.5%)
Depreciation	(94,610)	(84,014)	7.7%
Amortization	(32,295)	(28,723)	12.6%
Other operating income (expenses), net	1,857	(17)	(100.0%)
Operating profit	**255,673**	**240,745**	**6.2%**
Interest expense	(51,236)	(46,764)	9.6%
Interest and other financial income	1,805	2,696	(33.0%)
Exchange loss, net	(12,264)	69,477	(117.7%)
Profit before tax	**193,978**	**266,154**	**(27.1%)**
Income tax expense	(22,109)	(42,545)	(48.0%)
Net profit and comprehensive income for the period.	**171,869**	**223,609**	**(23.1%)**

Operating Data:			
Number of mobile subscribers	**3,568,841**	**3,844,312**	**(7.2%)**
Postpaid	871,717	894,802	(2.6%)
Prepaid	2,697,124	2,949,510	(8.6%)
Monthly churn %			
Postpaid handset	1.9%	2.8%	(30.5%)
Postpaid datacard	4.2%	5.0%	(15.9%)
Total postpaid	2.0%	2.9%	(30.8%)
Prepaid handset	6.8%	3.5%	91.9%
Prepaid datacard	16.7%	5.3%	213.4%
Total prepaid	6.8%	3.5%	92.8%
Total monthly churn (1)	5.5%	3.4%	63.7%
Monthly ARPU (US$) (2)			
Postpaid	19.1	18.7	2.3%
Prepaid	6.5	5.8	12.1%
Total monthly ARPU (3)	9.6	8.8	8.9%
Number of employees	**1,148**	**786**	**46.1%**

(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 5,638 and 5,629 to US$1.00 in 31 March, 2017 and 2016, respectively.

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

Revenue

Total revenue decreased by 2.8% for the three month period ended 31 March 2017 to Gs.761.1 billion from Gs. 782.9 billion for the same period of 2016. The decrease was due to less voice (13.4%) revenue compensated with higher revenue from value-added services (6.0%). Our recurring revenue from value-added services represents 68.3% of total recurring revenue for the three month period ended 31 March 2017, versus 63.8% in the same period of 2016.

The cable TV business has contributed revenue of Gs.66.3 billion during the three month period ended 31 March 2017 in comparison to Gs.70.7 billion for the same period in 2016.

Customer base

As of 31 March 2017, our total mobile customer base was 3,568,841, which represents a decrease of 7.2% from 3,844,312 as of 31 March 2016, with prepaid customers accounting for 75.6% or 2,697,124 of our total mobile customers at such date. The decrease was due to a criteria modification on the customer base report policy, on September 2016. Nevertheless, 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 decreased by 20.2% for the three month period ended 31 March 2017 to Gs.151.2 billion from Gs. 189.6 billion for the same period in 2016. Our cost of sales is affected by higher T&E costs due to strong campaigns to push adoption of smartphones and mobile data during 2016. Decrease in cable TV programing costs in line with reduced revenue from Tigo Home. Interconnection costs decreased 4.7% YoY due to regulatory measures. Bad debt decreased by 1.2% YoY. Some costs such as voice and SMS decreased in line with the decrease of revenue related to those services.

Gross profit margin increased to 80.1% for the three month period ended 31 March 2017 from 75.8% for the same period of 2016.

Operating expenses

Operating expenses decreased by 4.5% for the three months ended 31 March 2017 to Gs.229 billion from Gs. 240 billion for the same period in 2016. The main reason for the decrease was a one off adjustment related to accrued expenses. As a percentage of revenue, general and administrative expenses decreased to 30% for the period ended 31 March 2017 from 31% in 2016.

EBITDA

	Year ended 31 March,	
	2017	2016
EBITDA (1)	380,721	353,499
EBITDA margin (2)	50.0%	45.1%
Net debt to LTM EBITDA (3)	1.36	1.47
Total debt to LTM EBITDA (4)	1.67	1.63

(1) We define EBITDA as our earnings before interests, taxes, depreciation and amortization.

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

(3) We calculate Net debt to LTM EBITDA by dividing our total borrowings, less cash and cash equivalents, by our EBITDA from the three months ended 31 March 2017.

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

Operating profit

Operating profit increased by 6.2% for the three month period ended 31 March 2017 to Gs.256 billion from Gs. 241 billion for the same period ended 31 March 2016. The operating margin increased from 30.7% at end of 31 March 2016 to 33.6% in 31 March 2017. This increase was mainly because of reduced technical service fees in other operating expenses and the other expenses remaining relatively constant, and a one off adjustment related to accrued income.

Net finance costs

Net finance costs, which include interest expense, net of interest income, increased by 12.2% in the three month period ended 31 March 2017 to Gs.49 billion from Gs.44 billion for the same period ended 31 March 2016. 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 78% denominated in US Dollars.

Foreign exchange gain (loss)

Exchange gain, net, decreased by 118% at the end of March 2017 to a net loss of Gs.12.2 billion from a net gain of Gs.69.4 billion at the end of March 2016. Exchange gains and losses resulted primarily as a result of movements in the PYG/USD exchange rate resulting in the revaluation 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 5,767 as of 31 December 2016 to 5,638 as of 31 March 2017.

Charge for taxes

The charge for taxes decreased by 48%, to Gs.22.1 billion for the three month period ended 31 March 2017, from Gs. 42.5 billion for the same period ended 31 March 2016, due primarily to a lower profit before tax. The effective tax rate for the period ended 31 March 2017 was 11.4% compared to 16% for the same period ended 31 March 2016.

Net profit for the period

Net profit at the end of 31 March 2017 decreased by 23% to Gs.171.9 billion compared to a net profit of Gs.223.6 billion at the end of 31 March 2016 as a result of the above effects.

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, cable TV and music and video streaming. In the three month period ended 31 March 2017, value-added services represent 68.3% of recurring revenue, versus 63.8% in the same period ended 31 March 2016. 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 5.9% in the year 31 March 2017 to Gs. 82.9 billion from Gs. 88.2 in 31 March 2016. 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 three month period ended 31 March 2017 and 2016 amounted to Gs.33,5 billion and Gs.365 billion, respectively.

Financing

As of 31 March 2017, our total outstanding indebtedness and other financing was Gs.2,315 billion. As of 31 December 2016, our total outstanding indebtedness and other financing was Gs.2,354 billion.

Our interest expense for the period ended 31 March 2017 was Gs.51.2 billion and for the same period ended 31 March 2016 was Gs.46.8 billion.

Cash Flows

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

PYG millions	Year ended 31 March	
	2017	2016
Net cash provided by operating activities	257,646	384,587
Net cash used in investing activities	(118,597)	(295,109)
Net cash used in financing activities	(22,805)	(65,725)
Net (decrease) increase in cash and cash equivalents	**116,244**	**23,753**
Cash and cash equivalents at the end of the period	427,166	227,737

For the three month period ended 31 March 2017 cash provided by operating activities was Gs.257.6 billion compared to Gs.384.5 billion for the same period ended 31 March 2016. The decrease was mainly due to an increase of payments made to suppliers, compared to the same period last year.

For the three month period ended 31 March 2017 cash used by investing activities was Gs. (118) billion compared to Gs. (295) billion for the same period ended 31 March 2016, mainly due to lower investments in CAPEX than in the previous year.

For the three month period ended 31 March 2017 cash used by financing activities was Gs. (22.8) billion compared to Gs. (65.7) billion for the same period ended 31 March 2016. The variation of cash used for financing activities during the three month period ended 31 March 2017 is mainly due to lower repayment of financial debt compared to the same period last year.

The net increase in cash and cash equivalents for the three month period ended 31 March 2017 was Gs 116.7 billion compared to Gs. 23.7 billion for the same period of 2016. We had closing cash and cash equivalents of Gs.427.2 billion as of 31 March 2017 compared to Gs. 227.7 billion as of 31 March 2016.

Subsequent events

Dividend distribution

In May, 2017 Telecel Board has proposed to the Annual General Meeting of Shareholders the distribution of a dividend of USD 116 million, to be paid out of Telecel´s profits for the year ended 31 December 2016.

Tower sale and leaseback

On 26 April, 2017, the Group announced an agreement to sell approximately 1,400 wireless communications towers to a subsidiary of American Tower Corporation (“ATC”). As a result of this transaction, Telecel will receive approximately Gs700 billion, equivalent to USD 125 million, in cash.

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