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

TELEFONICA CELULAR DEL PARAGUAY S.A.E.
As the three-month period ended 31 March 2020

We believe in better. We believe in tigo

1. Overview

We are a leading provider of telecommunications services, including the affiliates companies, in mobile telephony, broadband internet, pay television, and other related products, such as Mobile Financial Services (MFS) and digital media. We hold the number one position in the mobile market with approximately 3.48 million mobile customers, while our Hybrid Fiber-Cable (HFC) network passes more than 779 thousand homes. In the three-month period ended 31 March 2019, we generated revenue of PYG 672 billion and EBITDA of PYG 236 billion.

2. Recent Developments

Bonds issuance

On January 2020, Telefónica Celular S.A.E. has made a retap of the Unsecured Senior Notes due 2027 by $ 250 million with an interest rate of 5.875%. This issuance was totally subscribed with a successful demand and we got $ 15,937 million of premium proceed, resulting in an effective interest rate of 4.81%. $ 2.7 million of related unamortized costs were recognized and the Redeemed Notes were classified as current liabilities.

Additionally, on January 2020, we have refinanced our outstanding PYG 103.08 billion loan with Banco Itaú Paraguay S.A. with an additional credit of PYG 51.54 billion. We kept the fixed rate at 9% with maturity of 5 years.

On February 2020, Telecel, IPS (Instituto de Previsión Social) and IIC (Interamerican Investment Corporation) signed an agreement to cancel the outstanding credit facility with the Paraguayan Social Security Entity (IPS) paying the principal plus cumulate interests by an amount of PYG 319,232 million.

Finally, on February 2020, Telecel completed the issuance of the remaining program with the following series: PYG 15,000 million at a 9.25% rate, due by January 29th, 2027; and PYG 20,000 million at 10%, due by January 31st, 2030.

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 described below:

Revenue

We generate revenue mainly from fees associated with communication, entertainment, data, and information services that we provide to our customers, including: airtime and data usage fees, roaming fees, interconnection fees, connection fees, monthly subscription fees, broadband internet, VoIP, data transmission, cable TV, sale of content and other services and sales of equipment, cloud and ICT. We generally seek to increase our revenue through the growth of our customer base as well the increase of traffic/usage and the introduction of new products and value-added services. Our results of operations are therefore dependent on our customer base, the ARPU and the number of services that each customer uses.

Drivers for revenue growth

We are building state-of-the-art fixed and mobile networks to deliver services for consumers and businesses. We intend to rapidly increase the digital capabilities of our mobile network, extending our 4G/LTE network coverage – a technology that increases the speed of data services that can be delivered to our mobile customers. We are also expanding the footprint of our HFC fixed network, passing homes and business premises and connecting them to our infrastructure, with our affiliate SPM.

We intend to monetize the substantial investment we make in fixed and mobile networks by providing high quality, secure connectivity as well as innovative, compelling value-for-money services that consumers and business demand.

Mobile

On the mobile front, we continue to focus on increasing our customer base through portability and new customers with segmented plans to increase traffic per user and on expanding coverage and capacity of our 4G/LTE network. As of March 31, 2020, we had approximately 1.4 million customers on 4G/LTE, an increase of 38% compared to March 31, 2019. Our mobile subscriber base increased by 8.1% to 3.48 million during the same period. At March 31, 2020, 4G/LTE customers accounted for 41% of the total mobile customer base compared to 32% at March 31, 2019.

Home

As of March 31, 2020, our HFC network (including SPM the affiliate company) covered approximately 779,000 homes in Paraguay (a 16.7% increase from March 31, 2019), and we provided services to around 524,000 RGUs, a 11.4% increase from March 31, 2019. Our home customers can choose from a complete suite of services, including pay-TV, internet, and other digital services. Our pay-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 strategy is to expand our HFC network faster and more cost-effectively than our competitors, increasing our homes passed, homes connected, and revenue. We continue to invest to provide faster and more reliable broadband connectivity around the country. As we are growing our HFC network (in SPM) this impact our Wimax customers which are been migrated to HFC and WTTX.

In 2014, we launched Tigo Sports, a multiplatform sports content producer and differentiator of Tigo pay-TV service. The service is also available as a value-added service for mobile phone subscribers, allowing access to content through an app for smartphones. This represents an important component of our strategy to increase client loyalty by offering exclusive content to our customers in the pay-TV and mobile areas and a significant enhancement to the value of the Tigo brand, as it differentiates us from our competitors and provides our customers with sought-after premium content. For instance, through Tigo Sports, we own the rights to broadcast the Paraguayan national football championship until December 2020.

New products and services

We use our LTE network to provide fixed telecom services such as high-speed internet in cities where we do not offer HFC coverage. Also, since 2019 we offer our home streaming service named "ONE TV" have the possibility to watch cable television and video content on a single platform, with the same control and from any screen. In the mobile business in November 2019 we launched "Roaming like Home" where our customers can be able to call and traffic in other countries in post-paid and pre-paid segment. Our Tigo Business unit also looks for ways to grow through innovation, with the first UPTIME Tier 3 certified data center to help us expand into business services such as co-location and cloud solutions. This data center allows us to offer services such as virtualization, cloud, storage, backup and housing to our business customers.

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

We consistently seek to 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 infrastructure. Spending 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 increases 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.

Balance sheet capital investment totalled PYG 12.5 billion during the period ended March 31, 2020, compared to PYG 34.4 billion during the period ended March 31, 2019. The latter period included the UHF 3500Mhz extension approved, for the next six months.

Competitive and regulatory pressures on pricing

The market in which we operate is competitive in nature. 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. We seek to sustain our market leadership position by providing innovative services on fast and reliable networks, and by leading with significant positive initiatives that reflect our commitment to sustainability.

The regulatory environment has become more challenging in our market. Over the past year, new regulation has allowed customers to roll over their unused minutes, SMS bundles and data balances at the end of the month rather than losing these. These changes in regulation have hindered revenue recognition and have affected the profitability of our mobile services, forcing us to quickly adapt our pricing models as needed to achieve our desired margin and return targets.

Effect of exchange rate fluctuations

The exchange rate for the Paraguayan Guaraní fluctuates in relation to the U.S. dollar and such fluctuations may, from time to time, have a material adverse effect on our earnings, assets, liability valuation and cash flows. Moreover, currency movements can also affect our financial leverage, as some of our debt is denominated in U.S. dollars. See “Risk Factors—Certain factors relating to Paraguay—Fluctuations of the Guaraní relative to the U.S. dollar or the implementation of restrictive currency exchange control policies by the Paraguayan government could result in an increase in our cost of financing and limit our ability to make timely payments on foreign currency-denominated debt.”

The PYG/$ exchange rate moved from PYG 6,181 as of March 31, 2019 to PYG 6,563 as of March 31, 2020. This variation impacted our 2020 Net Profit PYG 12,833 million, mainly due to higher interest expense, as most of our debt financing is denominated in U.S. dollars. Additionally, there is a significant part of our operating costs and capital investments that are also denominated in foreign currency and therefore impacted by currency devaluation.

4. Results of Operations

Period ended 31 December 2020 and 2019

PYG million	Period ended March 31		Percent change
	2020	2019	
Revenue	672,020	721,666	(6.9%)
Cost of sales	(133,319)	(131,987)	1.0%
Gross profit	**538,701**	**589,679**	**(8.6%)**
Sales and marketing	(207,613)	(165,565)	25.4%
General and administrative expenses	(94,940)	(86,414)	9.9%
Operating expenses	(302,553)	(251,979)	20.1%
EBITDA	**236,148**	**337,700**	**(30.1%)**
Depreciation	(90,949)	(83,933)	8.4%
Amortization	(53,215)	(50,714)	4.9%
Other operating income (expenses), net	4,337	5,673	(23.6%)
Operating profit	**96,321**	**208,726**	**(53.9%)**
Interest expense	(95,315)	(147,158)	(35.2%)
Interest and other financial income	(52,594)	12,867	(508.8%)
Exchange gain (loss), net	(12,833)	(34,192)	(62.5%)
Profit before tax	**(64,421)**	**40,243**	**(260.1%)**
Income tax expense	7,947	(15,311)	(151.9%)
Net profit/(loss) and comprehensive income for the period.	**(56,474)**	**24,932**	**(326.5%)**

Operating Data:			
Number of mobile subscribers	**3,478,135**	**3,218,510**	**8.1%**
Postpaid	921,963	904,143	2.0%
Prepaid	2,556,172	2,313,367	10.5%
Monthly churn %			
Postpaid handset	2.2%	2.5%	-0.3%
Postpaid datacard	3.4%	3.5%	-0.1%
Total postpaid	2.2%	2.5%	-0.3%
Prepaid handset	3.6%	3.4%	0.2%
Prepaid datacard	4.5%	5.7%	-1.2%
Total prepaid	3.6%	3.4%	0.2%
Total monthly churn(1)	3.2%	3.1%	0.1%
Monthly ARPU(2)			
Postpaid	92.2	99.2	(7.0%)
Prepaid	30.6	36.7	(16.6%)
Total monthly ARPU(3)	47.0	54.2	(13.3%)
Number of employees	**1,032**	**1,068**	**(3.4%)**

(1) Our total monthly churn is individually calculated by reference to our aggregate prepaid and postpaid customers.
(2) ARPU in local currency is expressed in thousand
(3) Our total ARPU is individually calculated by reference to our aggregate prepaid and postpaid customers.

Revenue

Revenue decreased by 6.9%, year-on-year to PYG 672 billion for the period ended March 31, 2020 primarily as a result of lower handset sales in our mobile business and by the ongoing trend of declining revenue from voice and SMS services, partly offset by continued growth from data services, consistent with trends seen in many mobile markets globally. Mobile data revenue decreased by 4.9% in 2020, while voice revenue fell by 8%, due to increased price competition impacting ARPU and the legacy of SMS and voice. Mobile data accounted for 67% of total mobile service revenue for the period ended March 31, 2020, compared to 67% in 2019, with the share of voice and SMS in the mix correspondingly increased to 31% in 2020 from 29% in 2019.

Fixed service revenue with our affiliate SPM increased by 9% year-on-year in B2C and 5% in fixed B2B revenue. In Telecel decrease in revenue of 7% is due to migration from legacy UHF network to HFC mainly, from SPM.

Cost of sales

Cost of sales increased by 1% year-on-year, to PYG 133.3 billion for the period ended March 31, 2020.

Gross profit margin decreased to 80.2% for the period ended March 31, 2020 from 81.7% for the period ended March 31, 2019.

Sales and Marketing

Increased by 25.4% year on year to PYG 207.6 billion for the period ended March 31, 2020 from PYG 165.5 billion for the period ended March 31, 2019, as a result of our plan to recover customer base, increase salesforce and focus in portability since Q2 2019.

General and administrative expenses

Increased by 9.9% year on year to PYG 94.9 billion for the period ended March 31, 2020 from PYG 86.4 billion for the period ended March 31, 2019 mainly due to exchange rate variance in contracts, Consultancy fees, Value Creation fee since 2020.

Operating expenses

Operating expenses increased by 20.1% for the period ended March 31, 2020 to PYG 302.5 billion from PYG 251.9 billion for the same period in 2019. The increase stems primarily from higher programming costs and sponsorship costs. As a percentage of revenue, operating expenses increased to 45% for the period ended March 31, 2020 from 35% in 2019.

EBITDA

PYG million	Period ended March 31	
	2020	2019
EBITDA [1]	236,148	337,700
EBITDA margin [2]	35.1%	46.8%
Net debt to LTM EBITDA [3]	15.63	2.13
Total debt to LTM EBITDA [4]	20.13	2.21

(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 year ended 31 December 2019.
(4) We calculate Total debt to EBITDA by dividing our total borrowings by our LTM EBITDA.

EBITDA decreased by PYG 101.5 billion (30% year-on-year), and EBITDA margin decreased by 11.7 percentage points year-on-year, due to the decline in revenue and the increase in operating expenses.

Operating profit

Operating profit decreased by 53.9% for the period ended March 31, 2020 to PYG 96.3 billion from PYG 208.7 billion for the same period ended March 31, 2019 as a result of the above. The operating margin decreased from 28.9% for the period ended March 31, 2019 to 14.3% for the period ended March 31, 2020. The year-on-year variation reflects the lower EBITDA, as described above.

Net finance costs

Net finance costs, which include interest expense, net of interest income, increased by 10.1% for the period ended March 31, 2020 to PYG 147.9 billion from PYG 134.2 billion for the period ended March 31, 2019. This increase was mainly due to corporate fees (Value Creating Fee).

Exchange gain (loss)

Exchange loss, net, for the period ended March 31, 2020 was a net loss of PYG 12.8 billion compared to a net loss of PYG 34.2 billion for the period ended March 31, 2019. Exchange gains and losses were primarily a result of movements in the PYG/$ 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/$ exchange rate increased from PYG 6,181 as of March 31, 2019 to PYG 6,563 as of March 31, 2020.

Income tax expenses

The charge for taxes decreased by 151.9% to PYG 7.9 billion for the period ended March 31, 2020, from PYG 15.3 billion for the period ended March 31, 2019, due primarily to a lower profit before tax.

Net profit

Net result for the period ended March 31, 2020 decreased by 326.5% to PYG 56.4 billion (loss), compared to a net profit of PYG 24.9 billion for the period ended March 31, 2019, as a result of the above.

Liquidity and Capital Resources

We rely primarily on cash from operations and external bond and bank financings to fund our operations, capital expenditures and working capital requirements.

We believe that our sources of liquidity are sufficient for our present requirements.

Financing

Our total outstanding indebtedness and other financing for the periods ended March 31, 2018, March 31, 2019 and March 31, 2020 was PYG 2,687 billion, PYG 3,034 billion and PYG 4,753 billion respectively.

Our interest expense for the periods ended March 31, 2018, March 31, 2019 and March 31, 2020 was PYG 65.4 billion, PYG 147.1 billion and PYG 95.3 billion respectively.

Cash Flows

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

Period ended March 31	2020	2019
	(in millions of PYG)	
Net cash provided by operating activities	146,027	232,100
Net cash used by investing activities	(775,903)	(366,632)
Net cash used by financing activities	1,501,440	100,166
Net (decrease) increase in cash and cash equivalents	**880,534**	**(32,126)**
Cash and cash equivalents at the end of the period	1,067,675	115,645

For the period ended March 31, 2020 cash provided by operating activities was PYG 146 billion compared to PYG 232,1 billion for the period ended March 31, 2019. The decrease was mainly to a less performance vs prior year due to a decrease in trade receivables and payables, and a decrease in taxes paid.

For the period ended March 31, 2020 cash used by investing activities was PYG 775,9 billion compared to PYG 366,6 billion for the period ended March 31, 2019, mainly due to Intercompany loan receivables.

For the period ended March 31, 2020 cash used by financing activities was PYG 1,501.4 billion compared to PYG 100.2 billion for the period ended March 31, 2019. The change in cash used for financing activities during the period ended March 31, 2020 is the net effect between repayment of debt and financing and proceeds from issuance of debt and other financing.

The net increase in cash and cash equivalents for the period ended March 31, 2020 was PYG 880.5 billion compared to PYG 32.1 for the same period of 2019. We had closing cash and cash equivalents of PYG 1,067.7 billion as of March 31, 2020, compared to PYG 115.6 billion as of March 31, 2019.

6. Subsequent events

COVID-19

The recent outbreak of a novel and highly contagious form of coronavirus (“COVID-19”), which the World Health Organization has declared to constitute a pandemic, has resulted in numerous deaths, adversely impacted global commercial activity and contributed to significant volatility in certain equity and debt markets. The global impact of the outbreak is rapidly evolving, and many countries have reacted by instituting quarantines, prohibitions on travel and the closure of offices, businesses, schools, retail stores and other public venues. Businesses are also implementing similar precautionary measures. Such measures, as well as the general uncertainty surrounding the dangers and impact of COVID-19, are creating significant disruption in supply chains and economic activity and are having a particularly adverse impact on transportation, hospitality, tourism, entertainment and other industries. The impact of COVID-19 also led to significant volatility and declines in the global public equity markets and it is uncertain how long this volatility will continue. We are monitoring the potential impact of the recent outbreak of COVID-19, which could negatively impact our global business and results of operations in future reporting periods which, as a consequence, could trigger potential asset impairments. As COVID-19 continues to spread, the potential impacts, including a global, regional or other economic recession, are increasingly uncertain and difficult to assess.

Tax impact

Due to the state of sanitary emergency due to the COVID-19 pandemic, the Tax Administration of Paraguay has determined some extensions of tax due dates and / or payment facilities that are:

- Extension of the Corporate Income Tax corresponding to the 2019 financial year, from April to June and payment in 4 (four) consecutive installments.
- Extension of the Value Added Tax corresponding to the month of March, from April to May.
- Extension of the 4 (four) Advances of Corporate Income Tax 2020, from May, July, September and November to July, September, November and December respectively.

The Financial Statements publication has been also postponed to July 31, 2020 by the Tax authority, due to the COVID-19 pandemic.

Consolidation entities

In April 2020, and as a result of shareholding restructuring, Telecel’s shareholder, Millicom International III N.V., will increase its participation in the Company by endorsing in favour of Telecel the 99 shares owned by it in Mobile Cash. As a result, Telecel will become the majority shareholder of Mobile Cash (with the 99 shares transmitted by endorsement).

Commitments

In April 2020, intercompany loans were agreed between Telecel and Servicios y Productos Multimedios (SPM) for $ 35 million and between TELECEL and Mobile Cash Paraguay (MFS) for $ 5 million.

Others

In April 2020, the following dividends were paid: Telecel for $ 29.5 million (net of taxes), SPM (advance) for $ 31.5M (net) and MFS (advance) for $ 8.3 million (net).