

### In the process of integration

February 2, 2017

► **The contractual improvements will enable the synergies envisaged to be accelerated**

Last October, Masmovil signed a global agreement with Orange, which highlighted three points: **the expansion of its own mobile telephony network through the Orange network in all its frequencies, wholesale access to the optical fiber network (“FTTH”) and, consequently, the acceleration of the synergies envisaged** following the acquisitions of Pepephone and Yoigo.

Accordingly, it is expected that **the contractual savings envisaged by the Company on a gradual basis, totaling €60 million in 2019e**, will be foreseeably obtained in the next 18 months. This could be accompanied by a possible **reduction of the integration costs initially considered** (€50 million during the first three years).

► **Positive data for the mobile segment... awaiting official data on convergent offers**

Recent portability data in the mobile telephony segment was **highly positive for Masmovil and Yoigo**. In the second half of 2016, **cumulative net portability exceeded 116,000 users at Masmovil and 38,000 at Yoigo**. Despite Pepephone's negative performance in the same period, with cumulative losses of 26,450 users, we consider such data to be significant for two reasons:

- **Brand strategy.** The two brands that reported the best performance are positioned in different segments, which would indicate that the **new group is winning mobile telephony users in the low-cost segment (Masmovil) and in the greater value added segment (Yoigo)**.
- **Fall-off in the number of mobile telephony customers at other operators.** In the same period, worthy of mention were **net losses of 107,250 and 107,150 customers at Movistar and Vodafone**, respectively. In the next reports of the companies, it will be necessary to analyze whether growth in the second half of 2016 in convergent offers was offset by the drop in the number of mobile telephony customers.

Awaiting the first official data regarding the attraction of fixed broadband users, following the launch of the convergent offer, it is possible to verify Masmovil's positioning: **service without premium content at a basic price**. We consider that **it is the right strategy**, in a widespread context of convergent price rises.

► **Recommendation: BUY. Target price: €32.6/share (increase from 28.0€/share, previous price target with conversion)**

Our valuation of Masmovil assumes that the customer bases from Yoigo and Pepephone will not undergo any increases. Furthermore, we are also considering execution of the convertible instruments, since the market price is above the conversion price (Providence: €22.0/share.; Shareholders esp. of Yoigo: €25.0/share). In this scenario, our valuation assumes a WACC of 10.0% and a g of 1.5%. **At current prices (€28.2/share), the company trades at a 2017e EV/EBITDA multiple of 8.8x, with an increase potential of 14%.**

#### BUY

Target price (€)	32.6
Upside (%)	14%

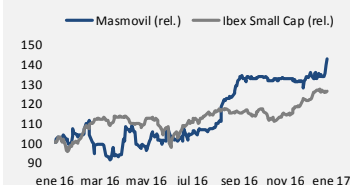
#### Market Data

Current price (€) (02/01/2016)	28.7
Shares Outstanding (Mn)	20.0
Market Cap (€Mn)	572.6
Net debt (€Mn)	738.9
Enterprise Value (€Mn)	1,311.5
1Yr Return (%)	43.2%
52-week low/high (€)	17,1 / 28,4

#### Key figures

(€Mn)	2016e	2017e	2018e
Sales	393	1,173	1,248
inc. %	201%	199%	6%
EBITDA	36	147	192
inc. %	243%	302%	31%
EBIT	-27	56	97
inc. %	n.a.	n.a.	75%
Net profit	-22	13	47
inc. %	n.a.	n.a.	276%
EPS (€)	-1.29	0.75	2.80
EV/EBITDA	34.1x	8.8x	6.5x
EV/CE	1.2x	1.2x	1.2x
P/BV	2.3x	2.3x	1.9x
ROCE	-2.6%	5.3%	9.3%
ND/EBITDA	19.8x	5.0x	3.6x

#### Evolución bursátil relativa



Fuente: Factset, Intermoney Valores

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## I. Agreements with Orange and Telefónica

### ► Accelerating the synergies and facilitating the change of network

As we highlighted in the previous note (“Global agreement with Orange”), last October, Masmovil reached an agreement with Orange which, in particular, highlighted **wholesale access to the whole optical fiber network (“FTTH”) of the French operator**. This was accompanied by the **agreement signed with Telefónica in December**, as a result of which Masmovil will also continue to use the **national roaming services** of Yoigo and Pepephone until 2019.

Both agreements will enable the company to **optimize its cost structure, increasing the marketing capacity of the mobile and convergent offer**, and to **facilitate the migration of the Telefónica network to the Orange network** in the coming years. Below, we review the main points of such agreements.

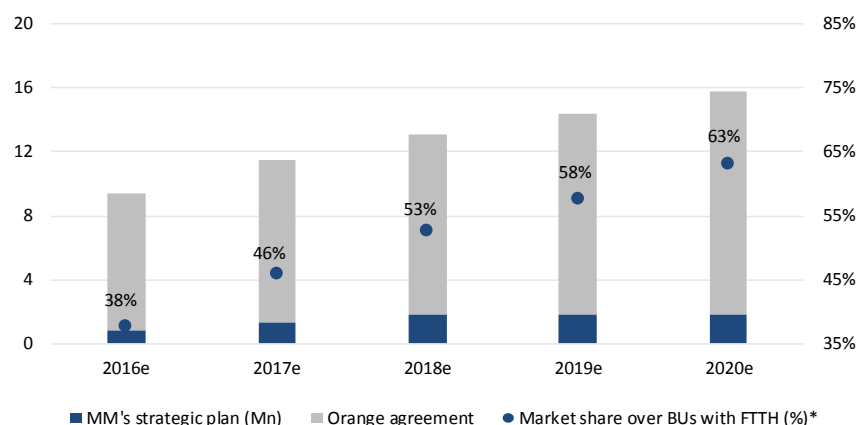
### ► Global agreement with Orange: acceleration of synergies

The most significant aspects of the agreement reached with the French operator last October were based on the **expansion of its own mobile telephony network through the Orange network** in all its frequencies, the **wholesale access to the optical fiber network** and, consequently, on the acceleration of the synergies envisaged following the acquisitions of Pepephone and Yoigo.

With respect to this last point, in the acquisition announcement of Yoigo, Masmovil estimated **contractual cost savings on a gradual basis, obtaining €60 million in 2019e**, in turn, **penalized by integration and transaction costs of €50 million** over the first three years. In this regard, following the agreement with Orange, **the company foresaw the acceleration of these synergies**, expectedly in the next 18 months, as well as **the reduction of the integration costs** initially considered.

As we analyze below, we consider that the key component of the agreement is the new optical fiber access base, placing Masmovil's FTTH coverage on an equal footing with that of Orange. Aside from the 800,000 property units with Masmovil's own optical fiber coverage, **from this year onwards, the company will have access to 8.6 million additional property units** (Orange's PUs at the close of 2Q16).

Masmovil's BUs (Mn) and market share over BUs with FTTH (%)

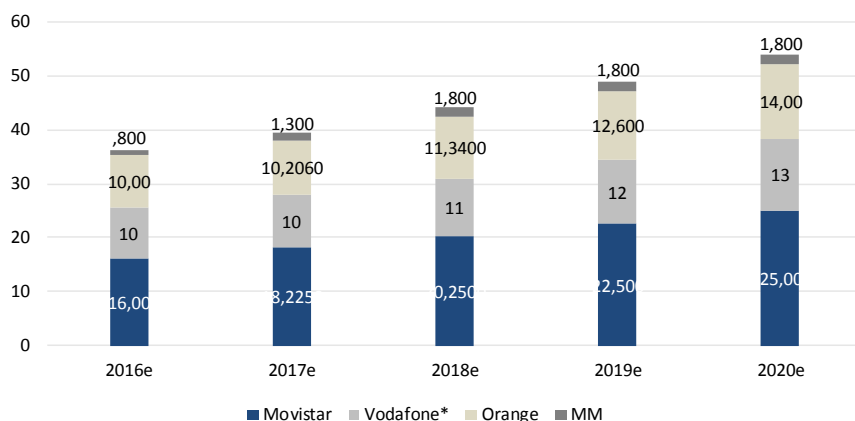


Source: Companies, Masmovil, Intermoney Valores

(\*) FTTH access of the main operators: Movistar, Vodafone and Orange

The graph above contains an estimate of access that could be achieved by the company in the coming years, together with its percentage of access through the agreement with Orange with respect to total FTTH access. This is a forecast based on the plans to expand the network of each operator until 2020e (for example, **Orange's objective is to exceed 14 million units**) and on the FTTH network co-deployment agreement between Masmovil and Orange, which will enable the Spanish operator to obtain 2.3 million BUs of access (own and shared) in the next three years. Consequently, **Masmovil would have access to 15.8 million FTTH units in 2020e**.

Estimate FTTH BUs per company 2020e (Mn)



Source: Companies, Intermoney Valores

\*Vodafone: CAGR 8,7% 2016e-2020e

#### ► Global agreement with Telefónica: a more flexible change of mobile network

The agreement signed with Telefónica last December is related with the two new group companies, Yoigo and Pepephone. Thus, **Telefónica will continue to provide national roaming services to both companies** during the migration phase to the Orange network. In addition, from the beginning of this year, **the service offered will be of the same quality as that offered by Telefónica to its customers**.

To complement the foregoing agreement, **both companies have resolved the legal conflicts existing between Yoigo and Telefónica** with respect to the national roaming service and the mobile interconnection service. As a result of the foregoing, **in the coming months, Yoigo will pay €11.1 million to Telefónica** for the friendly settlement of all prevailing legal conflicts. Accordingly, the Relevant Fact<sup>1</sup> specifies that it involves a previously provisioned amount.

We consider that the most significant point of the agreement is that **it ensures a more flexible transition to the Orange network for Yoigo and Pepephone users**, while improving the conditions of the service offered by Telefónica.

<sup>1</sup> RF of December 14, 2016: Global agreement with Telefónica

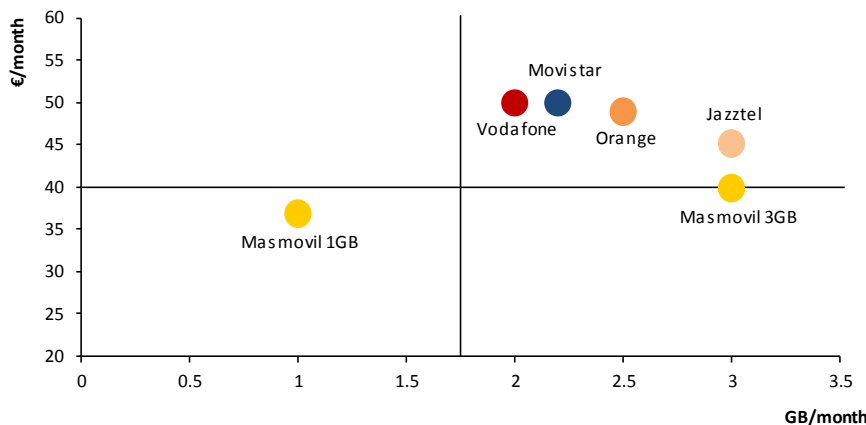
## II. Positioning in mobile and convergent offers

### ► The convergent offer strategy: price positioning

With the expectation that the company will submit a revised strategic plan which, aside from the growth and investment projections of the new group for the coming years, will reveal the final brand positioning, following the launch of the convergent offer in 2016 (fixed broadband + mobile + voice), it is possible to verify **the positioning favored by Masmovil: service without premium content at a very competitive price.**

In the following graph, we compare Masmovil's basic offer with that of the main national operators, with a combined plan that includes 50MB of download speed through optical fiber, a wireline telephone line and a mobile line with data. In this comparison, **Masmovil offers a price of €36.9/month (VAT incl.)**, comprising 1GB of mobile data and unlimited mobile telephone calls. It is a more competitive rate than that of the following operator, **Jazztel, which offers a price of €45.2/month (VAT incl.)**, **22.5% higher than Masmovil's tariff**, although it includes a higher mobile data consumption plan (3.0GB). However, Masmovil also has a package ("Masmovil 3GB") with greater mobile data consumption, at a price of €39.89/month (VAT incl.), **11.7% lower than Orange's rate.**

Comparison of the basic convergent offer (50MB) per company (€/month and GB/month) (01/26/2017)



Source: Companies, Intermoney Valores

The previous synopsis is similar in the FTTH convergent offer of 300MB. In this case, the 3GB Masmovil rate is **12.7%** lower than that of the main operator, Jazztel.

Fixed Broadband Bundles by company (300MB/200MB)

	Movistar	Vodafone	Orange	Jazztel	Masmovil 3GB
Speed (MB)	300	300	300	200	300
Voice (min.)	Unlimited	200	200	200	Unlimited
Mobile data (GB)	2.2	2.0	2.5	2.0	3.0
Price (€/month)	62.0	62.0	59.0	57.2	49.9

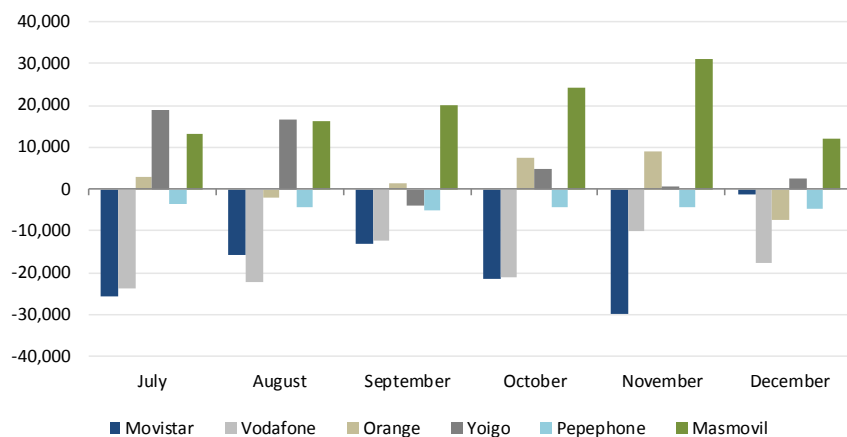
Source: Companies data, Intermoney Valores

The strategy of launching Masmovil's convergent offer is the right one, especially in a context of widespread rate rises by other operators. However, **the success of such strategy remains to be verified with the publication of the forthcoming official data.**

► **Mobile telephony portability is proving to be highly positive**

Waiting for growth to materialize in the attraction of fixed broadband users, **the latest portability data in the mobile telephony segment were highly positive for Masmovil and Yoigo**. Accordingly, **in the second half of 2016, cumulative net portability amounted to 116,400 users at Masmovil and to 38,900 users at Yoigo**. On a negative tone, of mention was the performance of **Pepephone, which lost 26,450 users in the same period**.

**Mobile telephony portability ('000 customers)**



Source: AdslZone, Intermoney Valores

We consider that **the recent mobile portability data are positive** for the new group, especially in light of the following:

- **Brand strategy.** The brands that have reported the best performance are positioned in different segments. Consequently, **while Masmovil's offer is centered on price, Yoigo's strategy offers higher value added joint voice and data tariffs** – for example, with a greater amount of data. Although a defined brand positioning still does not exist for the new group, we consider that this scenario will not change greatly in the future.

**Mobile bundles - Masmovil-Yoigo (voice and data)**

	Basic pack		Premium pack	
	Masmovil	Yoigo	Masmovil	Yoigo
Mobile data (GB)	1.0	1.2	4.0	5.0
Voice	Unlimited	Unlimited	Unlimited	Unlimited
Set up fee (cts.)	18.15	18.15	18.15	18.15
Price (€/month)	5.0	11.0	14.9	19.0

Source: Companies data, Intermoney Valores

- **Main operator statistics.** In the comparable period, two of the main mobile telephony operators, **Movistar and Vodafone, reported net losses of 107,250 and 107,150 customers, respectively**. Such performance could have two interpretations: on the one hand, the move of mobile customers to a convergent offer at these operators or, alternatively, the loss of total customers. In this regard, it will necessary to await the annual earnings of both companies, to analyze whether growth in the second half of 2016 in convergent offers was offset by the drop in the number of mobile telephony customers.

► **Approval of the new optical fiber wholesale offer**

As we have been indicating in previous reports, we considered the proposal of the CNMC (“Comisión Nacional de los Mercados y la Competencia”), which obliged Telefónica to offer a fixed broadband wholesale offer in non-rival areas, to be positive, since it was an option that **enabled Masmovil to expand its accessible optical fiber units’ base** without involving new network deployments. It is necessary to remember that this proposal aimed to enable the access of other operators to the Telefónica FTTH network in those areas in which there was not sufficient competition— considered to be at least three operators offering the same service.

Significant progress has been made in recent months in this regard. Following the approval of the initial proposal in 2016, **at the beginning of this year, the CNMC approved the new optical fiber wholesale offer**. The document highlights the **technical conditions of the new wholesale service** providing access to Telefónica's optical fiber network, known as NEBA (New Broadband Ethernet Service). Additionally, **the CNMC approved a decrease in wholesale prices due to capacity**, reducing the capacity price contracted at each access point by around 40%. Lastly, the regulating body also indicated **the need to offer the service to the other operators with the same speed available (300Mbps)**. The regulation of wholesale fiber access is expected to enter into force in 2018.

We consider that **such regulation will clearly favor operators with less-developed optical fiber networks** such as Masmovil. This fact, together with the agreement with Orange, should enable the new group to increase its market share and to attain its internal targets with greater ease.

### III. Acquisition of Llamaya

#### ► Expansion in the ethnic telephony segment

**Masmovil recently announced an agreement for the acquisition of Llamaya** (“Llamaya”), virtual mobile operator (VMO), **for an amount of €29.7 million to be paid in cash**. This assessment **implies a multiple of 2.9x EV/EBITDA**, in line with the EBITDA estimated by Masmovil (€10 million) after the integration. **The price could be increased by up to €12 million (to €41.7 million)**, based on the evolution of certain operating parameters, **payable, where appropriate, in 2018 and 2019**. Of this amount, €4.5 million would be paid in cash and the remainder in cash or shares at Masmovil's discretion.

Llamaya forms part of the assets comprising the business unit relating to the virtual mobile operator (VMO) activity of More Minutes Communications, S.L. (“More Minutes”). **The company began to operate in Spain in 2009**, through the Orange network.

**Llamaya will act as an ethnic operator, focusing mainly on the Central American market, mainly in the prepayment segment**. According to the Operation's Relevant Fact, the company generated **gross sales of €22.5 million in 2016 and has a portfolio of 170,000 active customers, with a monthly ARPU exceeding €10**.

With this operation, **Masmovil expects to expand its activity in the ethnic segment and to obtain synergies** with its international call termination business, which has 650 annual minutes of traffic.

As we detail below, **we have included Llamaya's incorporation in our estimates**, although, at global level, we foresee that **this operation should not significantly alter the new group's scenario at medium term** following the acquisition of Yoigo and Pepephone in 2016.



## IV. Our estimates

### ► Attainable growth targets

One of the key points at the new group will be the number of users attracted to a convergent offer. The possible success of the launch of the convergent offer will enable the company to increase its Average Revenue Per User (ARPU), and to improve its operating margins as a result of the combination of the three companies.

Our estimates once again assume a conservative scenario, especially if we consider the agreement reached by the company with Orange and whereby, as we have stated, Masmovil will expand its access to homes with optical fiber. We consider that it makes sense to base our estimates on a conservative scenario, since we continue seeing risks of execution and integration in the consolidation of the new group, especially, due to the level of debt assumed following both operations.

Considering the increased FTTH access of Masmovil, we continue assuming a penetration rate of 10% (5% in FTTH and 5% in xDSL) in Yoigo's current customer base (3.3 million) in 2020e. To these users, we can add our preliminary estimates for Masmovil and Pepephone users, around 1 million mobile telephony customers and 76,000 fixed broadband customers in 2016e. Additionally, we incorporate the 170,000 mobile telephony users originating from the acquisition of Llamaya. Hence, following the integration of the three companies, it is expected that the group will obtain c.4.5 million customers in the mobile segment and 244,000 fixed broadband customers in 2017e.

Once again, our foregoing estimates do not consider growth in the mobile telephony customer bases of Pepephone and Yoigo. In Masmovil's case, in line with the latest net portability data, we foresee a rise in users, to around 900,000 customers in 2020e. Furthermore, for 2016e, we have been assuming the consolidation of Pepephone since September and of Yoigo since October.

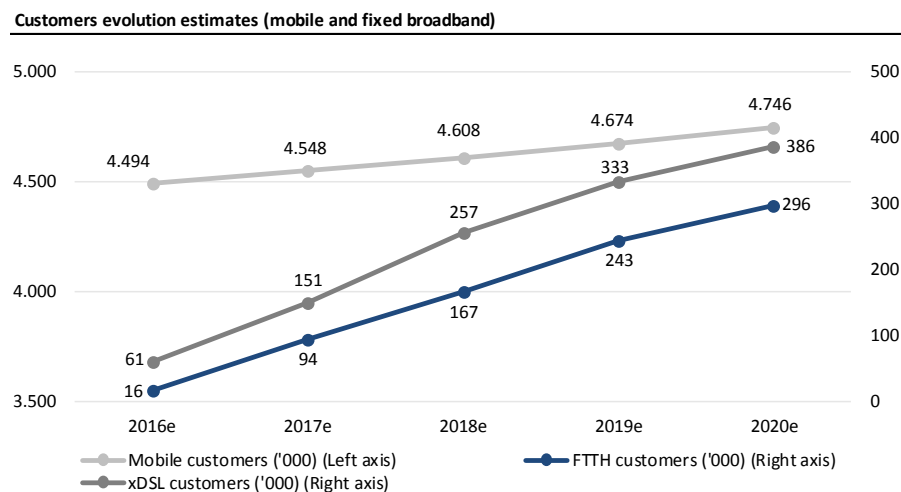
#### Intermoney estimates

	2016e*	2017e	2018e	2019e	2020e
<b>Mobile customers ('000)</b>	<b>4.494</b>	<b>4.548</b>	<b>4.608</b>	<b>4.674</b>	<b>4.746</b>
% var.	881,2%	1,2%	1,3%	1,4%	1,5%
Average ARPU (€/monthly)	14,0	14,0	14,0	14,1	14,1
<b>Mobile revenue (€Mn)</b>	<b>227</b>	<b>765</b>	<b>777</b>	<b>789</b>	<b>802</b>
<b>Fixed broadband customers ('000)</b>	<b>76</b>	<b>244</b>	<b>424</b>	<b>576</b>	<b>683</b>
% var.	305,5%	220,0%	73,7%	35,7%	18,5%
xDSL ('000)	61	151	257	333	386
% over BUs	0,3%	0,8%	1,4%	1,8%	2,1%
FTTH ('000)	16	94	167	243	296
% over BUs	0,1%	0,8%	1,3%	1,7%	1,9%
% FBB Customers/Mobile Customers	1,7%	5,4%	9,2%	12,3%	14,4%
ARPU xDSL (€/month)	25,0	25,3	25,5	25,8	26,0
ARPU FTTH (€/month)	30,0	30,3	30,6	30,9	31,2
<b>Revenue FBB (€Mn)</b>	<b>8,6</b>	<b>79,7</b>	<b>140,1</b>	<b>193,0</b>	<b>231,6</b>
Handset sales (€Mn)	57,4	229,5	232,5	235,8	239,5
Others (€Mn)	99,3	99,0	98,7	98,4	98,1
<b>Total revenue (€Mn)</b>	<b>392,5</b>	<b>1.173,2</b>	<b>1.247,9</b>	<b>1.316,0</b>	<b>1.370,7</b>

Source: Intermoney Valores

\* Pepephone consolidation since Sep-2016 and Yoigo since Oct-2016

These are attainable targets if we take into account that in the appendix to its half-yearly report, Masmovil announced that it expects to exceed 100,000 fixed broadband customers in 2016, and that **the percentage of fixed broadband customers over the total mobile customers implicit in our estimates would be approximately 15% in 2020e.**



Source: Intermoney Valores

Also, noteworthy was the fact that **the percentage of estimated customers with respect to accessible FTTH units would be 1.9% in 2020e (3.1% of current BUs)**, considerably down on the percentage reported at the main operators. As an example, **Telefónica's FTTH BUs penetration rate was 17.0% in 3Q16**, while at **Orange, such percentage was 14.5% in 2Q16** (latest figures available).

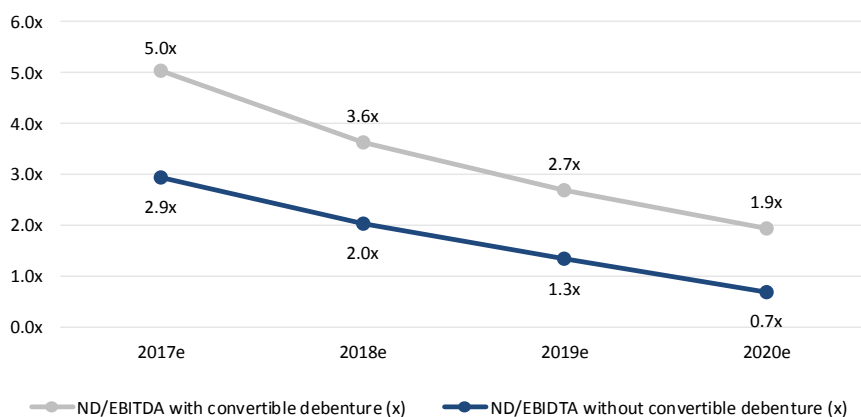
#### ► Issue of short-term promissory notes and expected level of debt

Alongside the announcements relating to the financing of the acquisition of Pepephone and Yoigo, the **€27 million financing agreement with the Chinese supplier ZTE and the issue of the €30 million bond of the subsidiary Masmovil Broadband**, on September 21, 2016, the company announced the **issue of promissory notes with an outstanding balance limit of €30 million**, placing a total of €10 million at three months at a nominal rate of 1.50% in the inaugural issue, and €20 million at a nominal rate of 1.75% in the six-month maturity tranches.

As we recalled in our previous report ("A new operator"), **we consider it appropriate to analyze the level of financial debt from 2017e**. Such analysis will reflect the company's new reality in a more objective manner, following the integration of the three companies.

Awaiting official news of the percentage of resources used to develop our own optical fiber network, our estimates envisage a **net financial debt at 2017e year-end of €738.9 million** (vs. €724.2 million in 2016e), which would be expressed by a **ND/EBITDA ratio of 5.0x**, which would gradually be reduced to 1.9x in 2020e. If we exclude the convertible instruments of Providence (€165.0 million) and of Yoigo's Spanish shareholders (€144.3 million) from the previous calculation, this level would be **2.9x in 2017e and 0.7x in 2020e**.

## Debt ratios estimates



Source: Intermoney Valores

Below is a summary of the company's financial structure following the acquisitions of Pepephone and Yoigo. **The total amount of the senior and intermediate debt would amount to €481.1 million**, which would represent a **ND/EBITDA ratio of 3.3x as a percentage of 2017e EBITDA** (€146.7 million).

## Summary of the company's financial structure

	Amount (€Mn)	Total debt (€Mn)	ND/EBITDA'17e	ND/EBITDA'18e
Financial debt	385.6	385.6	2.6x	2.0x
Subordinated debt	95.5	481.1	3.3x	2.5x
Convertible bond - Providence	165.0	646.1	4.4x	3.4x
Equity issue	160.0			
<b>Total acquisitions</b>	<b>806.1</b>			
<b>ND Masmovil'16e</b>	<b>78.1</b>	<b>724.2</b>	<b>5.0x</b>	<b>3.6x</b>
<b>ND Masmovil'16e s/c*</b>	<b>78.1</b>	<b>414.9</b>	<b>2.9x</b>	<b>2.0x</b>

Source: Intermoney Valores

\*Without the convertible debentures

## ► Summary of our estimates

In our earnings estimates, **we are assuming that contractual savings will be brought forward to 2018e**, together with the **cross-selling synergies with respect to Yoigo's current customer base (3.3 million)**. Also, we are not considering possible extraordinary savings in procurements, central services or the possible reduction of the customer care service as a result of the reduced exchange rate (churn rate) with a convergent offer.

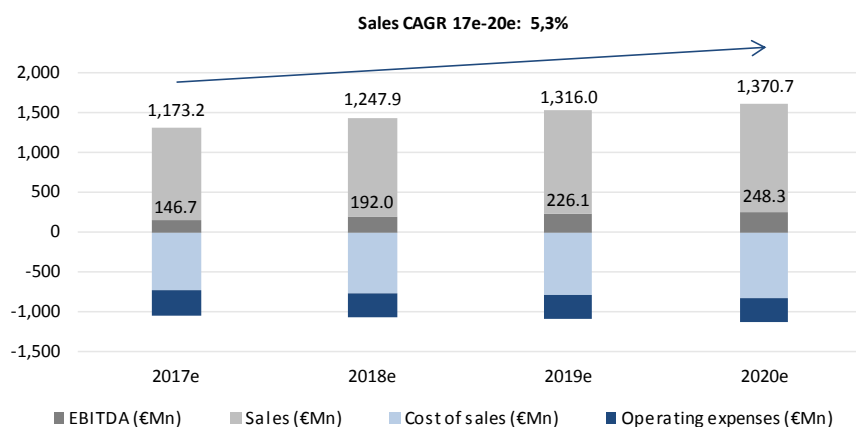
As we have indicated, we are not including growth in the mobile telephony customer base arising from the two acquisitions, and we envisage the following **average ARPUs: FTTH (€30.8/month), xDSL (€25.6/month) and mobile telephony (€14.0/month)**. With these variables, Masmovil would obtain a **sale of €1,173.2Mn in 2017e and an EBITDA of €146.7Mn**.

**Profit & Loss Statement estimates (€Mn)**

€Mn	2015	2016e	2017e	2018e	2019e	2020e	CAGR 17-20e
<b>Net revenue</b>	<b>130.2</b>	<b>392.5</b>	<b>1,173.2</b>	<b>1,247.9</b>	<b>1,316.0</b>	<b>1,370.7</b>	<b>5.3%</b>
% var.		201.4%	198.9%	6.4%	5.5%	4.2%	
<b>Gross Margin</b>	43.6	120.6	448.8	485.6	519.1	545.6	
<b>EBITDA</b>	<b>10.7</b>	<b>36.5</b>	<b>146.7</b>	<b>192.0</b>	<b>226.1</b>	<b>248.3</b>	<b>19.2%</b>
% var.		242.5%	302.0%	30.9%	17.8%	9.8%	
EBITDA margin	8.2%	9.3%	12.5%	15.4%	17.2%	18.1%	
<b>EBIT</b>	<b>0.5</b>	<b>-27.0</b>	<b>55.7</b>	<b>97.4</b>	<b>130.2</b>	<b>153.9</b>	
% var.		n.a.	n.a.	74.8%	33.6%	18.3%	
EBIT margin	0.4%	-6.9%	4.8%	7.8%	9.9%	11.2%	
Financial result	-2.5	-1.9	-41.0	-42.0	-39.0	-32.8	
Tax	0.5	07.2	(2.2)	(8.3)	(13.7)	(18.2)	
<b>Net Profit</b>	<b>-1.5</b>	<b>-21.7</b>	<b>12.5</b>	<b>47.1</b>	<b>77.5</b>	<b>103.0</b>	
Net margin	-1.2%	-5.5%	1.1%	3.8%	5.9%	7.5%	

Source: Masmovil, Intermoney Valores

With such estimates, the improved margins would be due to the increased weight of mobile telephone and fixed broadband users (4.3 million and 0.244 million in 2017e, respectively). Accordingly, we consider that the agreements indicated at the beginning of the note with Orange and Movistar would make such forecasts more feasible.

**Sales and EBITDA estimates (€Mn)**

Source: Intermoney Valores

In any case, it is necessary to highlight that these are temporary estimates, **awaiting an analysis of the first official data regarding the attraction of users with a convergent offer**, and that the company presents an updated strategic plan, incorporating the group's new structure.

## V. Valuation and recommendation

### ► Valuation considering the execution of convertibles

We have performed a valuation of Masmovil in terms of discounted cash flows, considering a **cost of equity (ke) of 15%**, a **capital cost (WACC) of 10.0%** and a **growth rate of 1.5%**, obtaining a **valuation of €32.6/share**. This involves an **increase potential of 14%** with respect to the current market price. In this valuation, we are assuming the execution of convertible instruments at a price of €22/share. (Providence) and €25/share (Spanish shareholders of Yoigo).

DCF	€Mn	2017e	2018e	2019e	2020e	2021e	Residual Value
<b>EBIT</b>		<b>56</b>	<b>97</b>	<b>130</b>	<b>154</b>	<b>169</b>	
Tax		(14)	(24)	(33)	(38)	(42)	
<b>NOPAT</b>		<b>42</b>	<b>73</b>	<b>98</b>	<b>115</b>	<b>127</b>	
D&A		91	95	96	94	91	
<b>Cash flow</b>		<b>133</b>	<b>168</b>	<b>194</b>	<b>210</b>	<b>217</b>	
WC change		13.1	1.3	1.1	0.9	0.8	
CAPEX		(131)	(104)	(111)	(78)	(91)	
<b>Free cash flow</b>		<b>15</b>	<b>65</b>	<b>84</b>	<b>132</b>	<b>127</b>	<b>1,547</b>
<b>DCF</b>		<b>14</b>	<b>54</b>	<b>64</b>	<b>91</b>	<b>79</b>	<b>968</b>
PV of FCF		302					
PV of RV		968					
<b>Enterprise Value</b>		<b>1,270</b>					
Net debt (2016e)		(724)					
Equity issue		160					
Convertible debentures Providence		165					
Convertible debentures Yoigo shareholders		161					
Fiscal credits (PV)		73					
<b>Market Cap</b>		<b>1,104</b>					
N. shares (Mn)		20.0					
N. shares Providence (Mn)		7.5					
N. shares Yoigo shareholders (Mn)		6.4					
N. shares (Mn)		33.9					
<b>Target price (€)</b>		<b>32.6</b>					
				WACC	10,0%		
				Growth rate	1.5%		

Source: Intermoney Valores

Furthermore, in the previous valuation, we included estimated tax assets for 2016e (around €310 million), discounted to present value. These assets mainly arise from the acquisition of Yoigo. Without taking them into account, the valuation would be €30.5/share. Additionally, in this scenario, we are not envisaging the payment of dividends for the coming five years.

Below we add a sensitivity table of our target price, assuming different scenarios for the growth rate ("g") and cost of capital (WACC):

#### Sensitivity analysis: WACC and "g"

	WACC				
	12.0%	11.0%	10.0%	9.0%	8.0%
2.5%	26.6	31.1	<b>36.8</b>	44.3	54.5
2.0%	25.3	29.4	<b>34.6</b>	41.3	50.1
<b>g</b> 1.5%	<b>24.1</b>	<b>27.9</b>	<b>32.6</b>	<b>38.6</b>	<b>46.4</b>
1.0%	23.0	26.6	<b>30.9</b>	36.3	43.3
0.5%	22.1	25.4	<b>29.4</b>	34.3	40.5

Source: Intermoney Valores

### ► Recommendation

We reiterate our **Buy recommendation, with a valuation of €32.6/share, assuming the execution of the convertibles**. The target price is 16.4% higher than the previous price, assuming the same scenario (€28.0/share).

With the expectation that the company will announce a new strategic plan in the coming months, we consider that **our recommendation is based on a conservative scenario**, once the integration of the three companies has been completed. Likewise, it will be vital to see the first official data regarding the attraction of users with a convergent offer, although **we are not assuming growth in the customer base arising from the two acquisitions**, and to foresee a **very low penetration rate with respect to FTTH property units** (1.9% in 2020e with network expansion and 3.1% of PUs currently available) with respect to the comparable companies.

On a complementary basis, **we are continuing to observe the leap to the Continuous Market as a catalyst for the company**, causing it to gain transparency and visibility, despite the fact that the process is being slower than initially estimated. Hence, we do not foresee novelties until the fourth quarter of the year.

### ► Risks

Alongside that set forth in previous reports, we consider it appropriate to highlight the possible risks faced by the new group following the incorporation of Pepephone and Yoigo:

1. **Financial leverage.** Despite the fact that it is logical to exclude convertible instruments from the group's current level of debt, the reality is that, at short term, the reduction of debt will be conditioned by the obtainment of the synergies envisaged and the success in attracting customers. Accordingly, we foresee a ND/EBITDA ratio of 5.0x in 2017e, which would become 2.9x without considering convertibles.
2. **The convergent offer commercial strategy.** We consider that the company's positioning with regard to convergent offers is the correct one, competing in terms of prices in a scenario of widespread rate rises by other operators. However, it will be necessary to analyze the success of the convergent offer commercial strategy with the publication of the first official data.

**Masmovil - Estimates**

(€Mn)	2015	2016e	2017e	2018e	2019e	2020e
<b>Sales</b>	<b>130.2</b>	<b>392.5</b>	<b>1173.2</b>	<b>1247.9</b>	<b>1316.0</b>	<b>1370.7</b>
Cost of sales	-89.5	-274.8	-727.3	-765.2	-799.9	-828.2
Others	2.8	2.9	2.9	2.9	3.0	3.0
Gross margin	43.6	120.6	448.8	485.6	519.1	545.6
SG&A and other operating expense	-17.9	-64.3	-270.9	-258.2	-256.5	-259.7
<b>EBITDA</b>	<b>10.7</b>	<b>36.5</b>	<b>146.7</b>	<b>192.0</b>	<b>226.1</b>	<b>248.3</b>
D&A	-10.2	-63.5	-91.0	-94.6	-96.0	-94.3
<b>EBIT</b>	<b>0.5</b>	<b>-27.0</b>	<b>55.7</b>	<b>97.4</b>	<b>130.2</b>	<b>153.9</b>
Financial result	-2.5	-1.9	-41.0	-42.0	-39.0	-32.8
<b>PBT</b>	<b>-2.0</b>	<b>-28.9</b>	<b>14.7</b>	<b>55.4</b>	<b>91.2</b>	<b>121.1</b>
Tax	0.5	7.2	-2.2	-8.3	-13.7	-18.2
<b>Net profit</b>	<b>-1.5</b>	<b>-21.7</b>	<b>12.5</b>	<b>47.1</b>	<b>77.5</b>	<b>103.0</b>
<b>Balance sheet</b>						
<b>Non current assets</b>	<b>234.2</b>	<b>1,029.5</b>	<b>1,067.8</b>	<b>1,071.7</b>	<b>1,060.7</b>	<b>1,032.5</b>
PPE	96.1	313.9	339.4	333.6	328.1	322.9
Intangibles	122.0	399.5	413.9	429.1	432.6	421.8
Others	16.2	316.1	314.6	309.0	299.9	287.8
<b>Current Assets</b>	<b>156.7</b>	<b>203.1</b>	<b>427.8</b>	<b>491.8</b>	<b>599.1</b>	<b>744.9</b>
Trade receivables	120.8	112.4	335.9	357.3	376.8	392.5
Cash	30.5	84.9	84.9	127.4	215.1	345.2
Others	5.4	5.8	7.0	7.1	7.2	7.3
<b>Total Assets</b>	<b>390.9</b>	<b>1,232.6</b>	<b>1,495.7</b>	<b>1,563.5</b>	<b>1,659.8</b>	<b>1,777.5</b>
<b>Shareholder's equity</b>	<b>90.7</b>	<b>229.0</b>	<b>241.5</b>	<b>288.6</b>	<b>366.1</b>	<b>469.1</b>
<b>Non current liabilities</b>	<b>134.0</b>	<b>865.2</b>	<b>877.9</b>	<b>875.9</b>	<b>873.9</b>	<b>872.0</b>
Financial debt	59.9	793.0	807.7	807.7	807.7	807.7
Others	74.1	72.2	70.2	68.2	66.2	64.3
<b>Current Assets</b>	<b>166.2</b>	<b>138.4</b>	<b>376.2</b>	<b>399.0</b>	<b>419.7</b>	<b>436.4</b>
Financial debt	123.7	16.0	16.0	16.0	16.0	16.0
Trade payables	39.7	119.6	357.4	380.2	401.0	417.6
Others	2.8	2.8	2.8	2.8	2.8	2.8
<b>Total Liabilities + Equity</b>	<b>390.9</b>	<b>1,232.6</b>	<b>1,495.7</b>	<b>1,563.5</b>	<b>1,659.8</b>	<b>1,777.5</b>
<b>Cash flow</b>						
Operating cash flow	8.3	41.8	137.9	180.9	213.7	235.3
WC investments	-2.4	4.4	13.1	1.3	1.1	0.9
CAPEX	-22.2	-68.0	-121.9	-104.0	-94.0	-78.3
Interest	-2.3	-1.9	-34.8	-35.7	-33.1	-27.9
<b>FCF</b>	<b>-18.5</b>	<b>-23.7</b>	<b>-5.8</b>	<b>42.5</b>	<b>87.7</b>	<b>130.1</b>
<b>Growth</b>						
Sales	69.1%	201.4%	198.9%	6.4%	5.5%	4.2%
EBITDA	190.0%	242.5%	302.0%	30.9%	17.8%	9.8%
Net profit	n.a.	1340.1%	n.a.	275.7%	64.6%	32.9%
<b>Margins</b>						
EBITDA / Sales	8.2%	9.3%	12.5%	15.4%	17.2%	18.1%
EBIT / Sales	0.4%	-6.9%	4.8%	7.8%	9.9%	11.2%
Net profit / Sales	n.a.	1340.1%	n.a.	275.7%	64.6%	32.9%
<b>Gearing</b>						
Net debt	43	724	739	696	609	479
Net debt / Equity	47.6%	316.2%	305.9%	241.3%	166.3%	102.0%
Net debt / EBITDA	4.0x	19.8x	5.0x	3.6x	2.7x	1.9x
Adjusted net debt / EBITDA	4.0x	11.4x	2.9x	2.0x	1.3x	0.7x
EBITDA / Financial result	4.8x	19.2x	3.6x	4.6x	5.8x	7.6x
<b>Valuation</b>						
EV/EBITDA	28.3x	34.1x	8.8x	6.5x	5.2x	4.2x
EV/CE	-14.6x	-1.2x	2.2x	0.6x	0.4x	0.3x
Number of employees	270	351	483	538	543	549

Source: Masmovil, Intermoney Valores

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