

AXTEL

Quarterly Report

October 15, 2018

Stronger cost structure boosts profitability

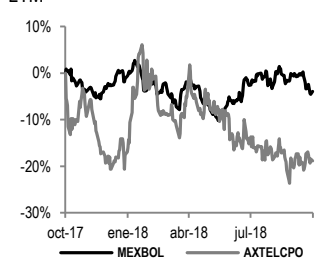
- 3Q18 earnings proved in line with our operating estimates but below our net projections. Axtel improved its financial structure, reducing the impact of foreign exchange volatility
- Excluding non-recurring revenue (MXN\$170 million) from the sale of the telecommunications towers in 3Q17, the company's EBITDA margin rose 3.8pp resulting from a stronger cost structure
- Incorporating this quarter's earnings, Axtel's Net Debt/Ebitda ratio fell from 3.6x to 3.4x. We expect more information on the progress of projects in order to monetize non-strategic assets

The sale of services with more added value drive profitability. We consider Axtel's earnings could be neutral for its stock price. By incorporating this quarter's results, the company's Net Debt /EBITDA ratio falls to 3.4x, derived from stronger financial structures; however, valuation benchmarks drop marginally (from 5.5x to 5.4x FV/EBITDA LTM). During the period, the company reported consolidated revenue worth MXN\$3.8 billion, up 1.7% YoY. During the quarter, network management and information technology services presented the highest growth rates. In addition, massive segment revenue continues to deteriorate, due to the cancellation of RGUs that used obsolete technology. The company reported MXN\$1.3 billion in EBITDA - 0.5% YoY, an 80bp margin drop to 34.2%. However, excluding non-recurring revenue from the sale of the telecommunications towers, EBITDA would increase 14.3% and the margin would expand 3.8pp. In terms of net results, Axtel reported a loss of MXN\$542 million, significantly below expectations, in view of lower profit from exchange rate fluctuations and greater tax provisions than anticipated.

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BUY

Current Price	\$3.64
PT 2018	\$5.30
Dividend 2018	0
Dividend Yield (%)	0%
Upside Potential	45.6%
Max - Min LTM (P\$)	4.89 - 3.52
Market Cap (US\$m)	559
Shares Outstanding (m)	2,893
Float	22%
Daily Turnover (P\$ m)	3
Valuation metrics TTM	
EV/EBITDA	5.3x
P/E	N.A.

Relative performance to Mexbol LTM

Financial Statements

	2016	2017	2018E	2019E
Revenue	13,937	15,513	15,309	15,650
Operating Income	-209	1,406	1,051	1,283
EBITDA	3,672	5,451	5,434	5,628
EBITDA Margin	26.4%	35.1%	35.5%	36.0%
Net Income	-3,601	62	-631	-1,416
Net Margin	-25.8%	0.4%	-4.1%	-9.0%
Total Assets	32,167	30,754	29,009	28,829
Cash	1,447	1,258	354	109
Total Liabilities	29,521	28,261	27,062	27,468
Debt	21,514	20,423	19,924	20,580
Common Equity	2,647	2,492	1,948	1,361

Fuente: Banorte

Valuation and Financial metrics

	2016	2017	2018E	2019E
EV/EBITDA	8.2x	5.4x	5.5x	5.5x
P/E	-2.8x	169.4x	-16.7x	-7.4x
P/BV	3.8x	4.2x	5.4x	7.7x
ROE	-136.1%	2.5%	-32.4%	-104.0%
ROA	-11.2%	0.2%	-2.2%	-4.9%
EBITDA/ Interest	2.0x	3.3x	2.9x	3.0x
Net Debt/EBITDA	5.5x	3.5x	3.6x	3.6x
Debt/Equity	8.1x	8.2x	10.2x	15.1x

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Document for distribution among public

AXTEL – Results 3Q18

MXN, million

Concept	3Q17	3Q18	Var %	3Q18e	Diff% vs Estim.
Revenue	3,764	3,829	1.7%	3,894	-1.7%
Operating Income	305	158	-48.1%	326	-51.5%
Ebitda	1,317	1,311	-0.5%	1,373	-4.5%
Net Income	-632	-542	-14.4%	21	N.A.
Margins					
Operating Margin	8.1%	4.1%	-4.0pp	8.4%	-4.2pp
Ebitda Margin	35.0%	34.2%	-0.8pp	35.3%	-1.0pp
Net Margin	-16.8%	-14.1%	2.7pp	0.5%	-14.7pp
EPS	-\$0.23	-\$0.19	-18.7%	\$0.01	N.A.

Income Statement (Million pesos)

Year	2017	2018	2018	Change	Change
Quarter	3	2	3	% YoY	% QoQ
Net Revenue	3,764.1	3,848.4	3,829.0	1.7%	-0.5%
Costs of goods sold	1,763.0	1,870.9	1,832.4	3.9%	-2.1%
Gross profit	2,001.1	1,977.5	1,996.6	-0.2%	1.0%
General expenses	1,783.1	1,737.1	1,835.3	2.9%	5.7%
Operating Income	305.0	298.1	158.2	-48.1%	-46.9%
Operating Margin	8.1%	7.7%	4.1%	(4.0pp)	(3.6pp)
Depreciation	1,004.7	1,079.7	1,136.7	13.1%	5.3%
EBITDA	1,317.4	1,415.5	1,311.3	-0.5%	-7.4%
EBITDA Margin	35.0%	36.8%	34.2%	(0.8pp)	(2.5pp)
Interest Income (Expense) net	(614.4)	(731.5)	(485.2)	-21.0%	-33.7%
Interest expense	399.6	471.1	473.0	18.4%	0.4%
Interest income	6.4	6.9	7.0	9.0%	2.0%
Other income (expense)	17.2	(2.7)	(7.1)	N.A.	159.0%
Foreign exchange gain (loss)	(238.4)	(264.5)	(12.2)	-94.9%	-95.4%
Unconsolidated subsidiaries				N.A.	N.A.
Income before taxes	(309.4)	(433.4)	(327.0)	5.7%	-24.5%
Income taxes	322.9	132.2	214.5	-33.6%	62.2%
Discontinued operations					
Consolidated Net Income	(632.3)	(565.6)	(541.5)	-14.4%	-4.3%
Non-controlling interest				N.A.	N.A.
Net Income	(632.3)	(565.6)	(541.5)	-14.4%	-4.3%
Net Margin	-16.8%	-14.7%	-14.1%	2.7pp	0.6pp
EPS	(0.230)	(0.196)	(0.187)	-18.7%	-4.3%

Balance Sheet (Million pesos)

	2017	2018	2018	Change	Change
				% YoY	% QoQ
Total Current Assets	5,685.6	6,415.6	5,813.2	2.2%	-9.4%
Cash & Short Term Investments	721.8	811.4	651.8	-9.7%	-19.7%
Long Term Assets	24,591.0	24,522.9	23,993.0	-2.4%	-2.2%
Property, Plant & Equipment (Net)	19,258.6	18,596.1	18,276.7	-5.1%	-1.7%
Intangible Assets (Net)	1,112.1	973.6	993.5	-10.7%	2.0%
Total Assets	30,276.6	30,938.4	29,806.2	-1.6%	-3.7%
Current Liabilities	6,491.9	8,155.6	7,675.2	18.2%	-5.9%
Short Term Debt	899.7	1,123.0	808.3	-10.2%	-28.0%
Accounts Payable	4,794.9	6,457.0	6,234.3	30.0%	-3.4%
Long Term Liabilities	20,144.2	20,058.1	19,829.4	-1.6%	-1.1%
Long Term Debt	18,617.1	19,442.9	19,180.1	3.0%	-1.4%
Total Liabilities	26,636.1	28,213.6	27,504.6	3.3%	-2.5%
Stockholders' Equity	3,640.5	2,724.8	2,301.6	-36.8%	-15.5%
Non-controlling interest				N.A.	N.A.
Total Equity	3,640.5	2,724.8	2,301.6	-36.8%	-15.5%
Liabilities & Equity	30,276.6	30,938.4	29,806.2	-1.6%	-3.7%
Net Debt	18,795.0	19,754.5	19,336.6	2.9%	-2.1%

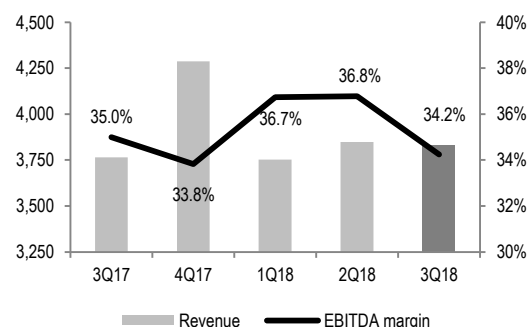
Cash Flow

FX difference in cash & equivalents	(7.5)	34.9	(17.9)		
CF from Operating Activities	809.8	1,088.0	952.8		
CF from Investing Activities	(605.0)	(533.9)	(706.4)		
CF from Financing Activities	(560.7)	(757.5)	(388.2)		
Change in Cash Balance	(363.3)	(168.5)	(159.7)		

Source: Banorte, BMV

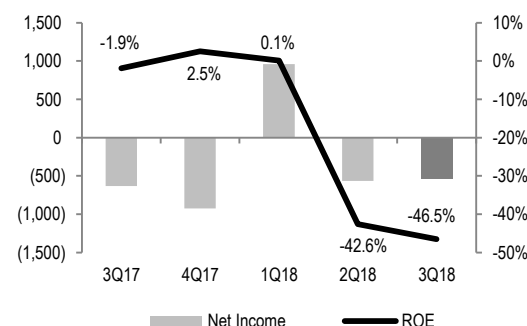
Revenue & EBITDA Margin

MXN, million



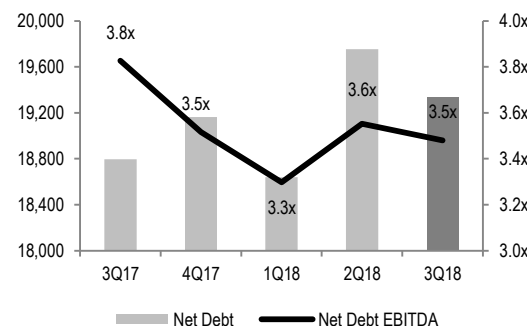
Net Income & ROE

MXN, million



Net Debt & Net Debt to EBITDA ratio

MXN, million



Good momentum on the sale of value-added services. During the third quarter of the year, reported consolidated sales for MXN\$3.8 billion, up 1.7% YoY and in line with our expectations. Breaking down this figure: (1) the Corporate segment contributed with 66.3% of consolidated revenue (over 65.9% in 3Q17) and posted a +2.3% annual variation; (2) the Government Segment contributed with 15.5% (vs 14.3%) and managed a 9.6% revenue increase YoY; and (3) massive market produced 18.2% (vs 19.7%) of total sales and reported an annual 6% decline. On the other hand, value added service revenue (Network Management and Information Technology Services) from the corporate and government segment contributed with 42.5% of Axtel's consolidated revenue over 3Q17's 38.2%. These added value services grew 13.3% YoY.

Within the corporate segment, Axtel reported 13% and 17% network management and information technology service increments, respectively. These gains offset the 16% voice service revenue reduction and stagnant growth of revenue from internet and data revenue. The drop reported in voice services is due mainly to a lower volume of calls to mobile phones and long-distance revenue. **As for the government segment,** the company reported an 11% increase in telecommunication service revenue, resulting from a 14% and 8% expansion of network Management and information Technology revenue, respectively. It is important to mention that during this period, 94% of revenue is recurring vs 87% in 3Q17. **For the massive market segment,** Axtel reported a 6.7% drop YoY of Revenue Generating Units (RGU), to stand at 892 thousand. Fiber optic technology RGU's rose 11.0% and represent 86.2% of the company's total base, while Wimax technology RGU's declined 53.2% YoY. Reduction of the RGU base caused the company's 6% reduction in sales.

Lower financial spending due to FX fluctuations. The company reported MXN\$485 million in financial spending, -21% vs 3Q17 due to lower exchange rate fluctuations which outweigh an 18.4% increase in paid interests. Axtel refinanced its US\$172 million debt to pesos, with which debt proportion in local currency rose to 51%, allowing the company to mitigate FX risk and its impact on cash flow.

We look forward to information on the sale of non-strategic assets during Alfa Day (15/11/18). As we had mentioned in our previous document, the company executed several projects to monetize non-strategic assets. It is worth remembering that the integration of Axtel and Alestra increased network coverage and redundancy, thus Axtel recently focused its efforts on traffic optimization, releasing several network segments for sale, whether on an independent basis or together with massive market operations. These initiatives give Axtel the possibility to monetize a parallel Long-Distance network with an approximate 9,300 kms extension in combination with 6,000 kms of metropolitan rings and 4 fiber optic threads.

Certification of Analysts.

We, Gabriel Casillas Olvera, Delia Maria Paredes Mier, Alejandro Padilla Santana, Manuel Jiménez Zaldivar, Tania Abdul Massih Jacobo, Katia Celina Goya Ostos, Juan Carlos Alderete Macal, Víctor Hugo Cortes Castro, Marissa Garza Ostos, Miguel Alejandro Calvo Domínguez, Hugo Armando Gómez Solís, Gerardo Daniel Valle Trujillo, José Itzamna Espitia Hernández, Valentín III Mendoza Balderas, Santiago Leal Singer, Francisco José Flores Serrano, Francisco Duarte Alcocer and Leslie Thalía Orozco Vélez, certify that the points of view expressed in this document are a faithful reflection of our personal opinion on the company (s) or firm (s) within this report, along with its affiliates and/or securities issued. Moreover, we also state that we have not received, nor receive, or will receive compensation other than that of Grupo Financiero Banorte S.A.B. of C.V for the provision of our services.

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HOLD	<i>When the share expected performance is similar to the MEXBOL estimated performance.</i>
SELL	<i>When the share expected performance is lower than the MEXBOL estimated performance.</i>

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PT and recommendation history

Issuer	Date	Recommendation	PT
Axtel CPO	16/10/2017	Buy	\$5.30
Axtel CPO	26/07/2017	Hold	\$5.10
Axtel CPO	24/04/2017	Hold	\$4.75
Axtel CPO	28/12/2016	Hold	\$4.15

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