

BCP Research: Liberty Latin America (LILAK) - 4Q19 Results, Positive - maintain 'Outright - Neutral'

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Summary: Caribbean and LatAm telecom company, Liberty Latin America (“Lilak”) released 4Q19 results, showing RGU and mobile subscriber growth, while ARPU contracted, primarily as a result of f/x fluctuation, impacted by political unrest in Chile. Revenue and Adjusted OIBDA grew y/y and sequentially, exceeding guidance. Free cash flow was positive US\$214 mm, benefitting from strong adjusted OIBDA performance, positive working capital and Lilak’s interest payment cycle. We highlight capex to revenue expanded in the quarter to 16% (3Q19: 14%). At 4Q19, LILAK had net debt of US\$7.1 bn and LTM net leverage of 4.7x, with a portion of the debt expansion attributable to the acquisition of AT&T Puerto Rico and USVI. We highlight the company refinanced ~US\$2.5 bn in debt between 4Q19 and 1Q20, pushing 90% of its maturity profile past 2024.

LILAK currently trades at a premium to comps (7.4x vs. 5.3x TEV / FY19 EBITDA). We recognize modestly higher expected growth (9% in FY20-21 v. peers Millicom 3%, America Movil 4% and Oi 5%, based on BBG consensus). Assuming the company achieves BBG consensus adj. OIBDA projections of ~US\$1,695 mm would imply 6.7x TEV / FY21 BBG consensus adj. OIBDA, still a significant premium to comps and implying fair value in line with the current mid-price of 103c on the convert. Given the narrow volatility spread (100D 30% v 28% IVOL), and unfavorable upside vs downside on an outright basis, we maintain our ‘Outright – Neutral’ opinion on LILAK 2% 24s. In the EM HY universe, we currently prefer Caribbean competitor, Digicel, offering more attractive risk vs. reward, with DIFL 24s (102c) rated ‘Market Outperform’ as part of our Top Picks, as well as DGL2 8.25% 22s (29c) DL 6% 21s (80c) rated ‘Positive’ as part of our more speculative High Octane Priority List.

	Issuer Name	Amt Out (US\$ MM)	Ratings (M/SP/F)	Mid Price	Mid YTM	Rank
VTRFIN 6.875% 1/15/2024	VTR Finance BV	1,260	B1/ B+/ BB-	102.4	6.18%	1st lien
CWCLN 7.5% 10/15/2026	C&W Senior Financing DAC	500	B2/ B+/ B+	107.8	6.05%	Sr Unsecured
CWCLN 5.75% 9/7/2027	Sable International Finance Ltd	550	Ba3/ BB-/ BB-	106.2	4.76%	Secured
CWCLN 6.875% 9/15/2027	C&W Senior Financing DAC	1,220	B2/ B+/ B+	109.3	5.37%	Sr Unsecured

	Issuer Name	Amt Out (US\$ MM)	Mid Price	Mid YTW	Implied Vol	Cheapness (par)	Delta (par)	Conv. Price	LILAK US Equity
LILAK 2% 7/15/2024	Liberty Latin America Ltd	403	102.5	1.4%	28.4%	0.7%	60.7%	\$22.23	\$17.64

* Source: Equity information sourced from Bloomberg. Convertible pricing as of close February 25th 2020.

4Q19 Results:

- Homes passed increased 5% y/y and 1% q/q to 7.52 mm
- RGUs increased 6% y/y and 1% q/q to 6.05 mm, while LILAK’s subscriber base grew y/y and remained stable q/q. We highlight the company added 139k total subscribers in one of its main markets, Jamaica, in 2019, capturing from its main competitor, Digicel

- Broadband internet +9% y/y, +2% q/q to 2.61 mm
 - Video subscribers +4% y/y and flat q/q at 1.98mm, fixed line telephony +5% y/y, +1% q/q at 1.46 mm
- Mobile subscribers increased 4% y/y but decreased 1% q/q at 3.66 mm, with y/y growth attributable to new value propositions in Jamaica for C&W, and continued consistent subscriber growth at VTR
- Mobile ARPU contracted 2% y/y and q/q to US\$14.20
 - C&W's ARPU was 1% lower y/y but 1% higher q/q at US\$13.95
 - VTR's ARPU decreased 15% y/y and 9% q/q to US\$17.11, with f/x impacted by ongoing political unrest in Chile
- Revenue grew 3% y/y and 1% q/q to US\$975 mm, split between C&W (63%), VTR/Cabletica (26%) and Liberty Puerto Rico (11%)
 - C&W: Strong B2B and fixed residential performance was offset by a 2% y/y decline in mobile revenues
 - Geographically, the company derives the majority of revenues from Chile (23%), Panama (16%), Puerto Rico (11%), Jamaica (10%) and Other LatAm & Caribbean (15%).
- Adjusted OIBDA was down 5% y/y but up 8% q/q at US\$409 mm, split between C&W (65%), VTR/Cabletica (26%) and Liberty Puerto Rico (13%)
 - Y/y performance was lower as a result of a US\$64 mm insurance recovery benefit realized in 4Q18
- Adjusted OIBDA margins contracted 324 bps y/y but expanded 264 bps q/q to 42%
- Free cash flow was positive US\$214 mm benefitting from strong adjusted OIBDA, positive working capital and LILAK's interest payment schedule, which outweighed heavy capex
 - Interest payments were 47% lower q/q at US\$74 mm, in line with the lower end of company's interest payment cycle
 - The company generated US\$66 mm in working capital, primarily due to an decrease in trade receivables partially offset by a decline in payables
 - The company had robust collections from C&W operations at year end including earlier-than-anticipated collections from its larger B2B and government customers
 - This is expected to result in some WK needs in 1Q20
 - Capex expanded 15% q/q to US\$157 mm, with capex-to-revenue at 16%, compared to 14% in 2Q19
- Gross debt expanded 18% q/q to US\$8,370 mm following refinancing of certain debt and the issuance of a US\$1 bn 6.5% LIBOR +5% term loan facility, US\$1.2 bn in 6.75% 2027 senior secured notes and a US\$125 mm 2025 RCF

- New debt was used to refinance US\$923 mm, comprised of a 1st lien term loan due 2022, 2nd lien term loan due 2023 and fund a portion of the AT&T acquisition
- In January 2020, the company also refinanced its US\$1.64 bn term loan under C&W with a US\$1.5 bn 2028 term loan and US\$150 mm in sr. secured notes
- 90% of LILAK's debt is now due to mature 2024 or later
- Liquidity also expanded 18% q/q to US\$1,184 mm
- Net debt was US\$7.186 mm, up 18% q/q resulting in LTM net leverage (incl. finance lease obligations) expansion to 4.7x

LILAK (US\$MM)	4Q19	3Q19	4Q18	y/y	q/q	2019	2018	y/y
Homes passed (mm)	7.52	7.45	7.16	5%	1%	7.52	7.16	5%
Revenue generating units (RGUs, mm)	6.05	5.99	5.70	6%	1%	6.05	5.70	6%
Broadband internet subscribers	2.61	2.57	2.40	9%	2%	2.61	2.40	9%
Video subscribers	1.98	1.98	1.91	4%	0%	1.98	1.91	4%
Fixed line telephony subscribers	1.46	1.45	1.39	5%	1%	1.46	1.39	5%
ARPU (USD):	48.47	50.35	50.27	(4%)	(4%)	48.45	51.27	(6%)
C&W	46.79	47.18	45.23	3%	(1%)	47.06	45.62	3%
VTR/Cabletica	43.04	46.12	48.05	(10%)	(7%)	46.13	52.16	(12%)
Liberty Puerto Rico	76.43	76.87	72.76	5%	(1%)	38.33	36.63	5%
Mobile subscribers (mm)	3.66	3.68	3.50	4%	(1%)	3.66	3.50	4%
Mobile ARPU (USD):	14.20	14.52	14.55	(2%)	(2%)	14.37	15.32	(6%)
C&W	13.95	13.87	14.11	(1%)	1%	13.93	14.82	(6%)
VTR	17.11	18.78	20.18	(15%)	(9%)	18.87	22.36	(16%)
Revenue	975	967	949	3%	1%	3,867	3,706	4%
Operating income	167	(70)	(385)	(143%)	(339%)	354	(24)	(1599%)
Impairment, restructuring and other operating items, net	23.8	208.3	585.1	(96%)	(89%)	259.1	640.5	(60%)
Share-based compensation expense	12	15	13	(5%)	(19%)	58	40	44%
Depreciation & amortization	206	226	215	(4%)	(9%)	871	830	5%
Adjusted OIBDA	409	380	428	(5%)	8%	1,541	1,487	4%
<i>Adjusted EBITDA margin</i>	<i>42%</i>	<i>39%</i>	<i>45%</i>	<i>(324 bps)</i>	<i>264 bps</i>	<i>40%</i>	<i>40%</i>	<i>(25 bps)</i>
Interest paid	(74)	(139)	(71)	4%	(47%)	(445)	(418)	6%
Taxes paid	(30)	(41)	(33)	(10%)	(26%)	(130)	(146)	(11%)
Working capital	66	(222)	(102)	-	-	(164)	(133)	23%
Capex	(157)	(137)	(183)	(14%)	15%	(589)	(776)	(24%)
Free cash flow	214	(158)	39	446%	(235%)	214	13	1531%
Gross debt (incl. finance lease obligations)	8,370	7,088	6,682	25%	18%	8,370	6,682	25%
Cash and equivalents	1,184	1,004	631	88%	18%	1,184	631	88%
Net debt (incl. finance lease obligations)	7,186	6,084	6,051	19%	18%	7,186	6,051	19%
LTM Gross leverage	5.4x	4.5x	4.5x	0.9x	0.9x	5.4x	4.5x	0.9x
LTM Net leverage	4.7x	3.9x	4.1x	0.6x	0.8x	4.7x	4.1x	0.6x

FY20 Guidance (excl. AT&T Assets):

- Negative impact of f/x exposure in certain markets (esp. Chile) is expected to persist
- Nonetheless, anticipated Adj. OIBDA growth in the low-to-mid single digits
- 18% to 20% capex-to-revenue in FY20, compared to 15% in FY19
- Adj. FCF of US\$150 mm, heavily weighted towards 2H20 and inclusive if f/x headwinds in Chile and WK changes as a result of aforementioned collection activities
 - Working capital expected to be negative in 1Q20
 - Capex less back-end weighted than FY19
- AT&T's Puerto Rico and US Virgin Islands transaction expected close in 2Q20
 - Integration costs to be incurred within the first 18 months of operation, with synergies coming through ~1 year after closing (est. US\$70 mm benefit to OCF)
- Planned expansion of The company plans to expand its fixed footprint via the building or upgrading of ~½ million homes in FY20
- Additionally, the new operational center in Panama is expected to ramp up in the year

Convertible Description and Valuation:

We evaluate LILAK converts at a spread of 470 bps (based on avg. spread to UST of subsidiary bonds) and a 100D realized share volatility of 30%, yielding an implied volatility on the common of 28%. Fair value is 104c vs. current mid price of 103c and an 85c bond floor.

CONVERTIBLE BOND		LIBERTY LATIN AMERICA
Country of Risk		CentAm/Carib
Industry Group		Telecom
Ticker		LILAK
Coupon		2.00%
Maturity		7/15/2024
Amount Out (mm)		403
Rank		Sr Unsecured
Mid Price		102.5
Mid YTM		1.4%
Share Conversion Price		22.23
Parity		79.3
Premium		23.2

EQUITY	LILAK US
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Share Price as of 02/26/2020 (USD)	17.64
Current Market Cap (US\$ bn)	3.2
Last Reported Earnings	4Q19
Net Leverage (Net Debt / LTM EBITDA)	4.7x
BCP Credit Spread Estimate	470
Realized Share Volatility (100D)	29.7%
Implied Volatility	28.4%
Fair Value (vs 100D realized vol)	103.7
(Rich)/Cheap %	0.7%
Delta	60.7%
Bond Floor	84.9
Implied Share Volatility (ATM 30D listed calls)	35.1%

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"Market Perform" – The bond's total return is expected to be in line with the total return of the CEMBI Broad Diversified High-Yield Index over the next 3 – 6 months.

"Market Underperform" – The bond's total return is expected to be below the total return of the CEMBI Broad Diversified High-Yield Index over the next 3 – 6 months.

"Not Rated" or no comment – Currently, the analyst does not have adequate conviction about the bond's total return relative to the CEMBI Broad Diversified High-Yield Index over the next 3 – 6 months.

Quasi Sovereign Universe

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"Market Weight" – The spread of the bond to its similarly duration sovereign controller bond is expected to remain unchanged over the next 3 – 6 months.

"Market Underweight" – The spread of the bond to its similarly duration sovereign controller bond is expected to increase over the next 3 – 6 months.

"Not Rated" or no comment – Currently, the analyst does not have adequate conviction about the bond's spread to its similarly duration sovereign controller bond over the next 3 – 6 months.

High Octane Universe

"Speculative Buy" – Bonds that in our view have an equity investment risk profile and we think risk/return is significantly skewed to the upside

"Positive" – Bonds that in our view have an equity investment risk profile and we think risk/return is skewed to the upside

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"Negative" – Bonds that in our view have an equity investment risk profile and we think risk/return is skewed to the downside

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