

BCP Research: Liberty Latin America (LILAK)-1Q20 Results-Swap CWCLNN 27s for LILAK 24 Converts on Top Picks

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Summary: Caribbean and LatAm telecom company, Liberty Latin America (“Lilak”) released soft 1Q20 results, showing RGU growth matched by a slight contraction in mobile subscriber growth. ARPU contracted as a result of persistent f/x weakness, particularly in Chile. Revenue and Adjusted OIBDA contracted y/y and sequentially. The company reported cash burn of US\$19 mm on capex, interest payments and WK use. Capex to revenue remained flat in the quarter at 16%. At 1Q20, LILAK had US\$1.6 bn in cash, US\$7.4 bn in net debt and, thus, LTM net leverage of 4.8x. We highlight the company refinanced ~US\$2.5 bn in debt between 4Q19 and 1Q20, pushing 93% of its maturity profile past 2024. LILAK has a current market cap of US\$1.8 bn and TEV/LTM Adj. OIBDA of 6.5x.

Though the company claimed no material impact on 1Q20 results, it does expect subsequent weakness in the coming quarters, particularly in Caribbean markets under subsidiary Cable & Wireless (C&W), as a result of COVID-19. C&W’s substantial cash balance – including US\$687 mm in cash and US\$426 mm in undrawn facilities at 1Q20 – should be ample cushion for OpCo to weather the environment. Bonds have rallied since our upgrade, and we think prices now reflect liquidity buffers and medium-term business resilience tempered by near term weakness in results.

Meanwhile, we see dislocation between subsidiary and HoldCo bonds. LILAK 2% 24 converts have normally traded through (on a YTM basis) to opco bonds (CWCLN, VTRFIN), but are now wider. LILAK bonds are subordinated in the HoldCo and rely solely on OpCo cash flow. Nevertheless, the telecom continues to produce solid consolidated OIBDA margins (39%) and recently extended debt amortization schedule (as mentioned, 93% of debt now matures after 2024). Moreover, the liquidity buffers are ample with a consolidated US\$1.6 bn in cash, US\$1.3 bn in escrow to fund the AT&T acquisition and US\$650 mm in aggregate unused borrowing capacity. The fundamental strength does not appear to be reflected in the current bond price, trading below the bond floor at 74c with YTM of almost 10%.

Thus, we are downgrading CWCLN 6.875% 27s to ‘Neutral’ on our Top Picks following a 14% rally to 99c from 87c at the time of our April 6th upgrade. In exchange, we upgrade LILAK 2% 24s to ‘Market Outperform’, 15% cheap to the model with solid liquidity, 10% YTM offering a virtually free option on the equity.

	Issuer Name	Amt Out (US\$ MM)	Ratings (M/SP/F)	Mid Price	Mid YTM	Rank	Recommendation
VTRFIN 6.875% 1/15/2024	VTR Finance BV	1,260	B1/ B+/ BB-	100.2	6.82%	1st lien	-
CWCLN 7.5% 10/15/2026	C&W Senior Financing DAC	500	B2/ B+/ B+	101.1	7.27%	Sr Unsecured	-
CWCLN 5.75% 9/7/2027	Sable International Finance Ltd	550	Ba3/ BB-/ BB-	100.8	5.65%	Secured	-
CWCLN 6.875% 9/15/2027	C&W Senior Financing DAC	1,220	B2/ B+/ B+	98.9	7.08%	Sr Unsecured	Neutral

	Issuer Name	Amt Out (US\$ MM)	Mid Price	Mid YTM	Implied Vol	Cheapness (par)	Delta (par)	Conv. Price	LILAK US Equity	Recommendation
LILAK 2% 7/15/2024	Liberty Latin America Ltd	403	73.9	9.76%	n/a	15.02%	55.0%	\$22.23	\$9.40	Market Outperform

* Source: Equity information sourced from Bloomberg. Convertible pricing as of May 7th 2020.

1Q20 Results:

- Homes passed increased 5% y/y and 1% q/q to 7.58 mm
- RGUs increased 6% y/y and 1% q/q to 6.10 mm, while LILAK's subscriber base grew y/y and remained stable q/q. The company added 60k total subscribers, primarily attributable to broadband subscriber growth
 - Broadband internet +8% y/y, +2% q/q to 2.66 mm
 - Video subscribers +3% y/y and flat q/q at 1.99mm, fixed line telephony +4% y/y and flat q/q at 1.46 mm
- Mobile subscribers increased 3% y/y but decreased 1% q/q at 3.62 mm, with mobile organic losses totaling 39k in 1Q20
- Mobile ARPU contracted 5% y/y and 6% q/q to US\$13.32
 - C&W's ARPU was 4% lower y/y and 6% lower q/q at US\$13.07
 - VTR's ARPU decreased 20% y/y and 6% q/q to US\$16.07, the result of continued f/x weakness in Chile
- Revenue contracted 1% y/y and 4% q/q to US\$931 mm, split between C&W (63%), VTR/Cabletica (26%) and Liberty Puerto Rico (11%)
 - Geographically, the company derives the majority of revenues from Chile (22%), Panama (15%), Puerto Rico (11%), Jamaica (10%) and Other LatAm & Caribbean (10%).
- Adjusted OIBDA was down 1% y/y and 4% q/q at US\$364 mm, split between C&W (64%), VTR/Cabletica (26%) and Liberty Puerto Rico (14%)
- Adjusted OIBDA margins expanded 28 bps y/y but contracted 283 bps q/q to 39%
- Free cash flow was negative US\$19 mm as a result of working capital use and heavy interest and capex
 - Interest payments were 95% higher q/q at US\$144 mm, in line with the upper end of company's interest payment cycle
 - The company used US\$77 mm in working capital, in line with the company's expectations of WK deployment in 1Q20 related to collections received from B2B and government customers in 4Q19
 - Capex decreased 5% q/q to US\$149 mm, with capex-to-revenue at 16%, flat compared to the prior quarter

LILAK (US\$MM)	1Q20	4Q19	3Q19	2Q19	1Q19	y/y	q/q
Homes passed (mm)	7.58	7.52	7.45	7.34	7.23	5%	1%
Revenue generating units (RGUs, mm)	6.10	6.05	5.99	5.93	5.78	6%	1%
Broadband internet subscribers	2.66	2.61	2.57	2.53	2.45	8%	2%
Video subscribers	1.99	1.98	1.98	1.96	1.92	3%	0%
Fixed line telephony subscribers	1.46	1.46	1.45	1.44	1.40	4%	0%
ARPU (USD):	47.37	48.47	50.35	47.64	47.34	0%	(2%)
C&W	47.62	46.79	47.18	47.67	46.46	2%	2%
VTR/Cabletica	40.74	43.04	46.12	47.62	48.42	(16%)	(5%)
Liberty Puerto Rico	75.69	76.43	76.87	-	76.79	(1%)	(1%)
Mobile subscribers (mm)	3.62	3.66	3.68	3.67	3.51	3%	(1%)
Mobile ARPU (USD):	13.32	14.20	14.52	14.43	14.08	(5%)	(6%)
C&W	13.07	13.95	13.87	14.03	13.58	(4%)	(6%)
VTR	16.07	17.11	18.78	19.50	20.07	(20%)	(6%)

Revenue	931	975	967	983	943	(1%)	(4%)
Operating income	108	167	(70)	144	113	(5%)	(35%)
Impairment, restructuring and other operating items, net	18.8	23.8	208.3	6.5	20.5	(8%)	(21%)
Share-based compensation expense	24	12	15	15	15	62%	93%
Depreciation & amortization	214	206	226	222	217	(2%)	4%
Adjusted OIBDA	364	409	380	387	366	(1%)	(11%)
<i>Adjusted OIBDA margin</i>	<i>39%</i>	<i>42%</i>	<i>39%</i>	<i>39%</i>	<i>39%</i>	<i>28 bps</i>	<i>bps</i>
Interest paid	(144)	(74)	(139)	(77)	(155)	(8%)	95%
Taxes paid	(13)	(30)	(41)	(38)	(22)	(42%)	(58%)
Working capital	(77)	66	(222)	11	(19)	310%	(218%)
Capex	(149)	(157)	(137)	(136)	(160)	(7%)	(5%)
Free cash flow	(19)	214	(158)	147	11	(276%)	(109%)
Loans, bonds and finance lease obligations	8,830	8,370	7,088	7,033	6,748	31%	5%
Operating lease liabilities	191	187	165	168	167	14%	2%
Gross debt	9,021	8,557	7,253	7,201	6,915	30%	5%
Cash and equivalents	1,593	1,184	1,004	957	569	180%	35%
Net Debt	7,428	7,374	6,249	6,244	6,346	17%	1%
LTM Gross leverage	5.9x	5.6x	4.6x	4.7x	4.6x	1.3x	0.3x
LTM Net leverage	4.8x	4.8x	4.0x	4.0x	4.2x	0.6x	0.0x
Capex-to-revenue	16%	16%	14%	14%	17%	(90 bps)	(9 bps)

- Gross debt expanded 5% q/q to US\$9,021 mm following refinancing 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
 - 93% of LILAK's debt is now due to mature 2024 or later
- Liquidity expanded 35% q/q to US\$1,593 mm and net debt was US\$7,428 mm, up 1% q/q resulting in a slight q/q expansion of LTM net leverage (incl. finance lease obligations) to 4.8x
 - LILAK has US\$562 mm in cash standalone and under unrestricted subsidiaries (US\$507 mm LILAK, US\$56 mm unrestricted subs.) – we assume the entirety of this will be used to fund the remaining portion of the AT&T acquisition
 - Subsidiary cash was split between C&W (US\$687 mm), VTR Finance (US\$211 mm), Cabletica (US\$14 mm) and Liberty Puerto Rico (US\$119 mm)
 - Aggregate unused borrowing capacity under subsidiaries various RCFs totaled US\$650 mm at 1Q20

LTM 1Q20 (US\$MM)	LILAK (Consolidated)	LILAK (Standalone)	Cable & Wireless	VTR/Cabletica	VTR (Standalone)	Cabletica (Standalone)	Liberty Puerto Rico
Ownership (%)			100%	100%	100%	100%	100%
Revenue	3,855	(9)	2,408	1,037	663	374	418
Adjusted OIBDA	1,540	(56)	970	420	257	163	206
<i>Adjusted OIBDA margin</i>	<i>40%</i>	-	<i>40%</i>	<i>40%</i>	<i>39%</i>	<i>44%</i>	<i>49%</i>
Gross Debt	9,021	813	4,519	1,452	1,382	71	2,237
Cash and Equivalents	1,593	563	687	225	211	14	119
Net Debt	7,428	250	3,832	1,228	1,171	57	2,117
LTM Gross leverage	5.9x	n/a	4.7x	3.5x	5.4x	0.4x	10.9x
LTM Net leverage	4.8x	" "	4.0x	2.9x	4.6x	0.3x	10.3x

* Gross debt includes operating and finance lease obligations

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- AT&T Acquisition: The US\$1.95 bn AT&T Puerto Rico and US Virgin Islands acquisition will be funded by a mix of cash on hand at LILAK (US\$507 mm), and cash on hand (US\$119 mm), undrawn facilities (US\$63 mm) and cash in escrow (US\$1,260 mm) at Liberty Puerto Rico. The acquisition is expected to close in 2H19
 - The company has said the transaction is expected to be accretive on a cash flow basis. We look forward to seeing fundamentals of AT&T Puerto Rico and US Virgin Islands to better understand its financial impact at both the Liberty Puerto Rico and LILAK levels
- Following the expected cash outflow from the AT&T acquisition, consolidated pro-forma cash at LILAK would be US\$967 mm, with an estimated US\$ 587 mm remaining in undrawn facilities, and pro-forma LTM net leverage of 5.2x
 - We expect LILAK's cash standalone will be US\$56 mm, and consist only of unrestricted subsidiary cash, resulting in pro-forma LTM net leverage of 5.8x
 - Liberty Puerto Rico's pro-forma LTM net leverage would increased to 10.9x

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