

REPORT PREPARED BY THE BOARD OF DIRECTORS OF EUSKALTEL, S.A. RELATING TO THE ACQUISITION OF PARSELAYA, S.L.U., AND INDIRECTLY OF TELECABLE DE ASTURIAS, S.A.U., WHICH IS SUBMITTED FOR APPROVAL OF THE SHAREHOLDERS AT THE ORDINARY GENERAL SHAREHOLDERS' MEETING OF THE COMPANY CALLED FOR 26 JUNE 2017, ON FIRST CALL, AND FOR 27 JUNE 2017, ON SECOND CALL

I. OBJECT OF THE REPORT

This Board of Directors of Euskaltel, S.A. has prepared this report (the “**Report**”) in order to provide the Company’s shareholders with the information necessary for them to form a reasoned opinion regarding the acquisition by Euskaltel of the business of Telecable de Asturias, S.A.U. (“**Telecable**”) by means of the indirect acquisition of 100% of the share capital of Telecable (the “**Transaction**”), and which the Board of Directors submits for approval of the shareholders at the Ordinary General Shareholders’ Meeting of the Company, which is expected to be held on 26 June 2017 on first call and on 27 June 2017 on second call, pursuant to the provisions of Section 160.f) of Royal Legislative Decree 1/2010 of 2 July approving the consolidated text of the Companies Act (the “**Companies Act**”), under item five of the agenda.

The Transaction will occur through the acquisition from the British entity Zegona Limited (“**Zegona**”) of all of the equity interests representing the share capital of the company Parselaya, S.L.U., the indirect holder of 100% of the shares into which the share capital of Telecable is divided.

For these purposes, the Report describes:

- (i) the essential terms and conditions of the Transaction to acquire the business of Telecable by Euskaltel;
- (ii) the history of Telecable and its current circumstances; and
- (iii) the rationale for the Transaction.

This Report will be made available to the shareholders of the Company as from the call to the Ordinary General Shareholders’ Meeting at which the proposed approval of the Transaction is submitted. A more detailed description of the Transaction is set out below.

II. REPORT

1. Background

On 14 March 2017, Euskaltel informed the CNMV, by means of a notice of significant event (*hecho relevante*), of having commenced conversations for the possible acquisition of Telecable. Subsequently, on 16 May 2017, as a continuation of the aforementioned significant event, it reported that an agreement between Euskaltel and Zegona had been reached for the acquisition of Telecable by Euskaltel, valuing Telecable at approximately 686 million euros (enterprise value).

2. Description of Transaction

By virtue of the Transaction, and subject to the terms and conditions thereof, Euskaltel would acquire from Zegona 100% of the share capital of Parselaya. Parselaya, in turn, is the holder of 100% of the shares of Telecable Capital Holding, S.A.U., which in turn is the holder of all of the shares into which the share capital of Telecable is divided.

The reference value of Telecable for purposes of the Transaction has been set at 686,100,000 euros, including approximately 245,000,000 euros of estimated net debt of Telecable (which will be refinanced by Euskaltel), which results in an equity value of 441,100,000 euros for 100% of the share capital of Parselaya, including intragroup debt. The consideration is subject to customary adjustments of net debt and working capital for these types of transactions.

The Transaction will be implemented by means of (i) the purchase of 1.5% of the equity interests of Parselaya for 186.5 million euros (less the net amount of the debt from intragroup transactions, which is subject to a number of adjustments); and (ii) an increase in capital paid for by means of a non-monetary contribution in an amount initially set at 254.6 million euros, such that Zegona subscribes all of the increase in capital by means of the contribution of 98.5% of the equity interests of Parselaya. This increase in capital will be submitted to the shareholders at the Ordinary General Shareholders' Meeting under item six of the agenda.

The consummation of the Transaction is subject to the following conditions, among others:

- (i) that the National Markets and Competition Commission (*Comisión Nacional de los Mercados y la Competencia*) (“CNMC”) approves the Transaction;
- (ii) that there is no material adverse change (“MAC”) between the date of execution of the private purchase agreement for all of the equity interests into which the share capital of Parselaya is divided and the closing date of the Transaction, on the terms and conditions set forth in said private purchase agreement; and
- (iii) that the shareholders acting at the General Shareholders' Meeting of Euskaltel:
 - (a) authorise the Transaction, pursuant to the provisions of Section 160.f) of the Companies Act;
 - (b) approve the amendment of certain articles of the Company's Bylaws, on the terms and conditions set forth in item seven of the agenda for the Ordinary General Shareholders' Meeting;
 - (c) set at 12 directors the number of members of Euskaltel's Board of Directors, which will be submitted for approval of the shareholders at the Ordinary General Shareholders' Meeting under item eight of the agenda;
 - (d) approve the appointment, at Zegona's request, of a new proprietary director, which will be submitted for approval of the shareholders at the Ordinary General Shareholders' Meeting under item nine of the agenda;
 - (e) approve the appointment of a new independent director, with the proposed appointment being submitted to the shareholders at the Ordinary General Shareholders' Meeting under item nine of the agenda; and

- (f) resolve to approve an increase in capital by means of non-monetary contributions in an amount initially set at 254,600,000 euros, with a delegation of powers to the Board of Directors, with express power of substitution, including, among others and pursuant to the provisions of Section 297.1.a) of the Companies Act, the power to set the date on which the increases must be implemented and to amend article 6 of the Bylaws.

3. Description of Telecable

Telecable is the leading telecommunications operator in Asturias, offering television, internet, mobile and fixed telephony services. Established in 1995, it was initially made up of Telecable de Oviedo, Telecable de Gijón and Telecable de Avilés, and since then has grown to become the principal telecommunications company in the Principality of Asturias.

Over the years, Telecable has evolved by virtue of the expansion of the services it offers, mainly on the basis of the technological advantage provided by some 3,000 kilometres of next-generation fibre optic network, which does not require significant additional investments and which covers all of the main urban centres in Asturias. In the residential market, the company has a 68% share of pay-TV, 31% of fixed, 39% of broadband, and 16% of mobile.

The company is recognised not only for its major penetration in Asturias, but also for its high levels of service quality and customer service. Specifically, it currently has 39 authorised sales points throughout the Principality of Asturias, which, together with an extensive network of direct sales stores, means a highly developed sales force.

Telecable currently employs approximately 180 people.

Finally, Telecable obtained turnover of 138 million euros during financial year 2016, with adjusted EBITDA reaching 65 million euros.

4. Rationale for the Transaction

The Company's Board of Directors believes that the Transaction is of the highest strategic importance in the telecommunications industry in northern Spain, constituting a fundamental and definitive step toward the consolidation of the three main cable operators in the north. This will give the Company greater strength and efficiency, shared synergies, and capacity for growth, among other things.

Along these lines, the local nature of Euskaltel and of Telecable is expected to be maintained, which will translate into the continuity of the respective brands, local structures and management teams, given that all of the foregoing as a whole is considered to be a key element for the success and expansion of these operators in recent years.

The acquisition of the Telecable business will entail a strengthening of the Company's positioning and stability in the telecommunications market, creating a group that, on a pro forma basis, would have reached combined billings of more than 700 million euros, adjusted EBITDA of around 350 million euros, and a significant cash flow of more than 220 million euros in 2016, taking into account that the networks of both companies are already quite developed in their respective territories and the investments to be made in this infrastructure are not very high.

Thus, the combination of Euskaltel and Telecable will permit:

- the creation of synergies such as (i) better access to and ability to negotiate regarding products, services and content, (ii) combining systems and technologies, (iii) optimisation of contractual relations with suppliers, and/or (iv) harmonisation of growth strategies, among others;
- the maximisation of the value of their customers, based on the leadership position held in their respective markets, the loyalty of their respective customers, the high value of their brands and the positioning of the companies; and
- increasing their size and significance in the Spanish telecommunications market, while simultaneously maintaining their local strength in the Basque Country (Euskadi), Galicia and Asturias.

In sum, the Transaction will make the Company stronger, more efficient and with higher growth potential in order to compete in a demanding market as a leading operator within its geographical areas in the north of the country, and of greater significance in the Spanish and European market, while at the same time maintaining its strong position and commitment in the Basque Country, Galicia and Asturias, where these companies have strong roots and prestige.

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In Derio (Biscay), on 24 May 2017