

A Primer  
for  
Appropriately  
Evaluating  
Zayo  
Performance

Robert Gotto has 17 years experience in Telecom. Most recently from 2011 until 2015 at Zayo Group, with stints as Business Unit CFO for Lit, Colo, and Europe. Prior to that, for 3 years, he was VP of Viridian Investments, a data center, tower, and fiber focused PE fund. Prior to that, for 6 years, he was VP or Corporate Development of Conversent Communication (for 1 year its acquirer One Communications), a northeast US facilities-based CLEC that generated 25%+ IRRs to investors and full repayment of all debt and a time when the predominant number of industry participants went through Chapter 11. Prior to that, he was with Fanch Communications, a top 20 MSO acquired by Charter Communications. Robert started his career in the Chicago office of investment bank Houlihan Lokey. Robert has an MBA from the Kellogg School of Management at Northwestern University and a BSBA in Finance from the University of Denver.

Robert is currently long ZAYO stock.

All figures in this deck are based on externally reported Zayo figures. In a couple cases, where noted, assumption have been made.

# Framework and Output

- Evaluating and valuing ZAYO should require and prioritize:
  - Separating speculative projects that are skewing underlying performance and fundamentals analytics
  - Strong weighting towards AFFO and AFFO growth rates
- Speculative projects for Zayo currently internally self-funded and should be viewed as a use of excess cash flow in lieu of share buybacks, dividends, or increase in dry power for future acquisitions
  - For point of reference, since beginning of 2014, Spec Deals totaling \$680m estimated expenditures on \$467m initial Contract Value or 69% of expenditures (w/ high probability of renewal), of which ~\$175m spent as of Mar-16 (~24%) and minimal installs to date (~\$300k MRR&MAR as of Mar-16)
  - Worst case scenario being even if assume no chance of renewal, or incremental value from any follow-on deals or tax offset from related depreciation, all being incredibly unlikely ... – i.e. just like burning the money --- negative cash impact would total \$212m, or less than \$1.00 per share
- Zayo non Speculative Sales (Bookings) and Net Installs levels generating a 7% revenue growth rate (5% w/ Canada), 14 mos average Payback, with estimated IRRs of >35%
  - Consistent with pre IPO levels
  - Thus Speculative projects materially skewing overall totals reported in Earnings Release package
- Zayo estimated run rate Mar-16 adjusted pro forma AFFO of \$614m or 32% margin on ~\$2B total annualized revenue demonstrates lucrative cash generating profile of run rate business
- High incremental margin nature of Zayo business results in AFFO growth rate of 14% (12% w/ Canada)
  - Reasonable to assume Zayo can scale EBITDA/AFFO at 75% incremental margin, based on 93% direct margins of new deals
  - A 9% top-line growth rate gets AFFO growth rate to 20%

# Bookings and Net Installs Metrics- **excl. Spec**

- Sales (Bookings) and Net Install activity (**excl. Spec**) generating 7% recurring revenue growth rates- (excl Canada)
  - Recent P&L impacted by noise of Fx changes and non recurring revenue Qtr over Qtr movements
  - Excluding Jun-15 results that has 2 deals that are part of Zayo's Major Project grouping
- Overall payback ratios on non Spec deals averaging < 14 months with estimated 35%+ IRRs
  - 7 months payback when excluding Network Capacity capex
  - vs the 33 month 5 Qtr avg reported in Earnings Release that includes of Speculative Deals
- Annual capital program of \$498m (Estimated Expenditures + Network Capacity) to achieve 7% revenue growth
  - Net capital program of \$276m after taking into account IRU and Upfront payments
  - As compared to ~\$1B level using (\$720m net) level reported when including the Spec deals

NON SPECULATIVE DEALS (<12 mo. + > 12 mo.)												
	Post Latisys										Run Rate (excl. Jun-15)	Annzld
	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16			
Net New Sales Bookings	\$ 5.1	\$ 6.0	\$ 5.4	\$ 5.2	\$ 6.3	\$ 6.5	\$ 6.1	\$ 5.9	\$ 6.6	\$ 6.2		
Contract Value	\$ 344.7	\$ 492.6	\$ 484.0	\$ 225.0	\$ 414.9	\$ 479.8	\$ 386.5	\$ 336.6	\$ 336.2	\$ 368.6		
Ratio of CV to Sales	67x	82x	90x	44x	66x	74x	63x	57x	51x	59x		
Estimated Bookings less NetEx %	94%	95%	92%	92%	94%	91%	93%	93%	94%	93%		
<b>Payback - Direct</b>	<b>12</b>	<b>14</b>	<b>16</b>	<b>13</b>	<b>9</b>	<b>33</b>	<b>10</b>	<b>17</b>	<b>19</b>	<b>14</b>		
Estimated IRR of Overall Deals	---	---	---	---	---	---	---	---	---	> 35%		
Estimated Capex	\$ 101.5	\$ 107.2	\$ 102.3	\$ 47.3	\$ 75.6	\$ 210.8	\$ 88.2	\$ 90.6	\$ 99.3	\$ 88.4	\$ 353.7	
Estimated Upfront Expenditures	\$ 0.3	\$ 2.5	\$ 1.2	\$ 1.1	\$ 1.2	\$ 0.6	\$ 0.6	\$ 0.2	\$ 0.9	\$ 0.7	\$ 2.9	
Estimated Expenditures	\$ 101.8	\$ 109.7	\$ 103.5	\$ 48.4	\$ 76.8	\$ 211.4	\$ 88.9	\$ 90.8	\$ 100.2	\$ 89.1	\$ 356.6	
Net New Sales (Bookings) - IRU and Upfront	\$ (75.0)	\$ (62.6)	\$ (54.5)	\$ (25.7)	\$ (73.5)	\$ (63.1)	\$ (65.0)	\$ (53.9)	\$ (29.4)	\$ (55.4)	\$ (221.7)	
Net Capital	\$ 26.8	\$ 47.1	\$ 49.0	\$ 22.7	\$ 3.3	\$ 148.3	\$ 23.9	\$ 36.9	\$ 70.8	\$ 33.7	\$ 134.9	
Network Capacity	\$ 20.1	\$ 23.8	\$ 20.6	\$ 33.7	\$ 42.7	\$ 21.5	\$ 22.8	\$ 41.6	\$ 34.2	\$ 35.3	\$ 141.3	
Total Net Capital, incl. Network Capacity	\$ 46.9	\$ 70.9	\$ 69.6	\$ 56.4	\$ 46.0	\$ 169.8	\$ 46.7	\$ 78.5	\$ 105.0	\$ 69.1	\$ 276.2	
Gross Installs (not incl. Major Project)	\$ 5.1	\$ 5.3	\$ 5.4	\$ 5.5	\$ 5.9	\$ 6.3	\$ 6.0	\$ 6.2	\$ 5.8	\$ 6.2		
Churn Processed	\$ (3.6)	\$ (3.6)	\$ (3.9)	\$ (3.7)	\$ (4.2)	\$ (4.0)	\$ (3.8)	\$ (4.2)	\$ (3.7)	\$ (4.2)		
<b>Net Installs</b>	<b>\$ 1.5</b>	<b>\$ 1.7</b>	<b>\$ 1.5</b>	<b>\$ 1.8</b>	<b>\$ 1.7</b>	<b>\$ 2.2</b>	<b>\$ 2.2</b>	<b>\$ 2.2</b>	<b>\$ 2.1</b>	<b>\$ 2.1</b>		
Sales to Gross Installs - Cum post Latisys (1 Qtr lag)	---	---	---	---	---	100%	96%	97%	98%	98%		
Ending MRR&MAR (non Canada)	\$ 92.8	\$ 98.8	\$ 103.7	\$ 104.8	\$ 115.0	\$ 117.4	\$ 119.8	\$ 123.5	\$ 125.8			
Churn Rate	---	1.3%	1.3%	1.2%	1.3%	1.2%	1.1%	1.2%	1.0%	1.1%		
MRR&MAR Annual Growth Rate (Constant Currency)	---	7%	6%	7%	7%	8%	8%	8%	7%	7%		

# Calculating Zayo Mar-16 Run Rate AFFO

- Existing Zayo earnings release package allows for fairly accurate AFFO calculation
  - Below table includes estimated remaining unrealized synergies from Allstream and Viatel
  - Zayo level of stock compensation expense looks to be roughly 2x higher than TowerCos and DataCenters (via looking at ratio of recent post IPO stock compensation expense as % of total expenses)
  - External reporting does not allow to isolate non-cash straight-line revenue and expense, or non cash amortized costs
- AFFO margin of 32%, or \$614m annually, excl. Speculative program
- Annual Levered FCF of \$320m a year. 16% of revenue, excl. Speculative program

CALCULATION OF ZAYO AFFO									
				Pro forma Adj Run Rate (Mar-16)			% of Revenue		
				Non Canada	Canada	Total	Non Canada	Canada	Total
Revenue	[[from P&L+Canada deck]]			\$ 1,528	\$ 420	\$ 1,948			
Expenses				\$ (629)	\$ (346)	\$ (975)			
EBITDA	[[from P&L+Canada deck]]			\$ 898	\$ 74	\$ 972	59%	18%	50%
Remaining Unrealized Synergies (Viatel and Allstream)	[back into based on reported figures]			\$ 7	\$ 35	\$ 42			
PF EBITDA		RR	Adjust	\$ 906	\$ 109	\$ 1,015	59%	26%	52%
Adjustment - Stock Comp Expense		\$ 104	50.0%	\$ (52)	\$ -	\$ (52)			
Adjusted PF EBITDA				\$ 854	\$ 109	\$ 963	56%	26%	49%
Capex - non Spec	[<12+>12mo annzld avg]			\$ (357)	\$ (6)	\$ (363)			
Capex - Network Capacity	[Quasi Spec capex as not specific deal related]			\$ (141)	\$ (54)	\$ (195)			
+ Upfront Customer Payments	[<12+>12mo annzld avg]			\$ 222	\$ 4	\$ 225			
-MAR	[[from P&L]]			\$ (95)	\$ -	\$ (95)			
+MAC	[not externally reported]			\$ -	\$ -	\$ -			
+/- Straight-line Rev (Exp)	[not externally reported]			\$ -	\$ -	\$ -			
UnFCF - non Spec-related				\$ 482	\$ 53	\$ 535	32%	13%	27%
Interest Expense	[[from P&L]]			\$ (197)	\$ (18)	\$ (215)			
<b>Lev FCF - non Spec-related</b>				<b>\$ 285</b>	<b>\$ 35</b>	<b>\$ 320</b>	<b>19%</b>	<b>8%</b>	<b>16%</b>
per Share				\$ 1.17	\$ 0.14	\$ 1.31			
Adj PF EBITDA				\$ 854	\$ 109	\$ 963			
-MAR				\$ (95)	\$ -	\$ (95)			
+MAC				\$ -	\$ -	\$ -			
+/- Straight-line Rev/Exp				\$ -	\$ -	\$ -			
Maintenance Capex	[from reported figures]			\$ (30)	\$ (8)	\$ (38)			
Churn Replacement Capex - net of NRR	[very likely higher customer upfront payments -vs- related capex]			\$ -	\$ -	\$ -			
Interest Expense				\$ (197)	\$ (18)	\$ (215)			
<b>AFFO</b>				<b>\$ 531</b>	<b>\$ 83</b>	<b>\$ 614</b>	<b>35%</b>	<b>20%</b>	<b>32%</b>
per Share				\$ 2.18	\$ 0.34	\$ 2.52			

# Zayo Growth Profile –vs- Comps

- At 93% direct margin on new deals, reasonable to assume Zayo can scale annual EBITDA at 75% incremental margins and thus AFFO should also scale at close to an incremental 75% margin level
- Data Centers forecasted to scale EBITDA at incremental margins of 58% and TowerCos at 77%, with 95% to 97% of this dropping to the AFFO level
- Zayo, with a 7% revenue growth rate (5% assuming no near term Canada growth), should result in a 14% AFFO growth rate (12% with Canada)
- Zayo's ratio of incremental AFFO margin to existing AFFO margin is 2.4x vs 1.5x for DCs and 1.32x for TowerCos which means that for every 1% revenue growth rate, Zayo gets 1.32x to 1.55x the impact to it's AFFO growth rate, relative to the Comps
- **Thus Zayo's non Canada growth rate of 7% is equivalent to a 9% TowerCo rate or a 10% DataCenter rate if attempting to isolate what the impact is to the AFFO growth rate**
- Zayo AFFO growth rate of 14% (12% w Canada) vs 12% for TowerCos and 20% for DCs
- A 9% Zayo growth rate would get to a 20% AFFO growth rate

Zayo Growth Rates as Compared to Internet Infrastructure Comparables						
	ZAYO			Street Mean '16/'17 Forecasts		
	Non Canada	Canada	Total	TowerCos	DCs	LVLTL
Incremental EBITDA Margin (assumed)	75%	75%	75%	77%	58%	65%
RR AFFO Margin	35%	20%	32%	43%	38%	26%
'Rule of Thumb' Ratio of Incr Margin to AFFO Margin	2.2	3.8	2.4	1.8	1.5	2.5
Zayo - RuT Ratio as % of Comparables	---	---	---	1.32x	1.55x	0.95x
Rev Growth Rate	7%	0%	5%	7%	13%	3%
	Zayo - as % of Comparables					
Normalizing Zayo Rev Growth Rate - to TowerCos'	9%	0%	7%	96%	---	---
Normalizing Zayo Rev Growth Rate - to DCs'	10%	0%	8%	---	60%	---
Normalizing Zayo Rev Growth Rate - to LVLTL's	6%	0%	5%	---	---	148%
AFFO Growth Rate	14%	0%	12%	12%	20%	8%
	Zayo - as % of Comparables					
Ratio of AFFO Growth Rate to Revenue Growth Rate	2.1	---	2.3	1.7	1.5	2.3
check: Ratio as % of 'Rule of Thumb' Ratio further above	97%	---	97%	95%	97%	94%
Zayo - RuT Ratio as % of Comparables	---	---	---	1.35x	1.55x	0.99x
Zayo AFFO Growth Rate - to TowerCos'	---	---	---	99%	---	---
Zayo AFFO Growth Rate - to DCs'	---	---	---	---	60%	---
Zayo AFFO Growth Rate - to LVLTL's	---	---	---	---	---	153%

Zayo Revenue Growth Rate to Achieve 100% of DC AFFO Growth Rate				
	Total	Street Mean '16/'17 Forecasts		
		TowerCos	DCs	LVLTL
Rev Growth Rate	9%	7%	13%	3%
Normalizing Zayo Rev Growth Rate - to TowerCos	11%	160%	---	---
Normalizing Zayo Rev Growth Rate - to DCs	13%	---	100%	---
Normalizing Zayo Rev Growth Rate - to LVLTL	8%	---	---	246%
AFFO Growth Rate	20%	12%	20%	8%
Zayo AFFO Growth Rate - to TowerCos'	---	164%	---	---
Zayo AFFO Growth Rate - to DCs'	---	---	100%	---
Zayo AFFO Growth Rate - to LVLTL's	---	---	---	254%

# Zayo Valuation – an AFFO Approach

- At \$29.21 per share (close price as of 8/25), Zayo trading at 11.6x RR AFFO vs 21.1x for TowerCos and 20.6x for DCs
- Using CY 2017E AFFO, Zayo trading at 9.7x vs 18.1x for TowerCos and 17.4x for DCs

<b>ZAYO: VALUATION SUMMARY</b>							Comparables		
	Current	@ Higher ZAYO Share Prices					TowerCos	DCs	LVL
<b>Price per Share</b>	\$ 29.21	\$ 32.50	\$ 35.00	\$ 37.50	\$ 40.00	\$ 42.50			
Appreciation from 8/24 Close-->>		11%	20%	28%	37%	46%			
Shares Outstanding	243.9								
<b>Equity Value</b>	\$ 7,124	\$ 7,927	\$ 8,537	\$ 9,146	\$ 9,756	\$ 10,366			
AFFO - Pro forma Adj Run Rate (Mar-16)	\$ 614								
Price / RR AFFO	11.6x	12.9x	13.9x	14.9x	15.9x	16.9x	21.1x	20.6x	8.3x
Price / CY 2017E AFFO	9.7x	10.8x	11.6x	12.4x	13.3x	14.1x	18.1x	17.4x	7.6x
RR AFFO Yield	8.6%	7.7%	7.2%	6.7%	6.3%	5.9%	4.7%	4.8%	12.0%
RR UnL FCF-non Spec Yield	4.5%	4.0%	3.7%	3.5%	3.3%	3.1%			
Net Debt	\$ (3,881)								
Net Leverage Ratio	3.9x						6.3x	3.7x	3.6x
<b>Total Enterprise Value</b>	\$ 11,005	\$ 11,808	\$ 12,417	\$ 13,027	\$ 13,637	\$ 14,247			
TEV / LQA Jun-16E EBITDA	11.0x	11.8x	12.4x	13.0x	13.6x	14.2x			
TEV / CY 2017E EBITDA	9.5x	10.2x	10.8x	11.3x	11.8x	12.3x			