

NEMAK

Quarterly Report
October 18, 2019

Efficiencies offset lower volume

- **Nemak reported lower than expected volumes for Nafta and the Rest of the World. However, operating efficiencies translated into higher profitability**
- **Volume decreased 13.8% (-7.7% vs. BNTE) and revenues fell 16.4% to US\$ 963 million (vs. -9.7%e), while EBITDA declined 13.1% to US\$ 139 million with a 50bp expansion of the margin to 14.4%**
- **The company reported a US\$ 2 million net loss following recognition of a US\$ 33 million one-time charge from the eventual closure of its Windsor, Canada, plant. We reiterate our HOLD rating on the stock**

Another weak quarter but on track to meet guidance. Nemak's report was neutral showing greater-than-expected weakness in Nafta and Rest of the World volumes and revenues, but higher profitability on the back of operating efficiencies. Volumes were lower across regions taking the consolidated indicator to 10.6m equivalent units (-13.8% yoy vs. BNTE -6.1%), due to a less favorable Nafta product mix and less demand from Ford in China. Thus, revenues decreased 16.4% yoy to US\$ 963 million (vs. BNTE US\$ 1.040 billion), also due to lower aluminum prices and euro depreciation. Meanwhile, EBITDA decreased relatively less than revenues (-13.1% to US\$ 139 million), as operating efficiencies in Nafta and the Rest of the World offset pressures related to severance expenses in Europe. Consequently, the EBITDA margin rose 50 bps yoy to 14.4% (vs. 14.1%e). Nemak reported a US\$ 2 million net loss after recognizing a US\$ 33 million impairment charge from the eventual closure of the Windsor, Canada, plant. As the company is on track to meet its guidance, we reiterate our HOLD rating. We will shortly be publishing our PT2020.

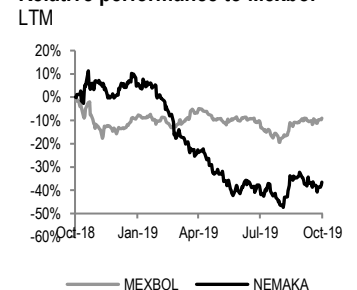
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HOLD

Current Price	P\$9.30
PT 2019	P\$10.00
Dividend 2019	P\$0.21
Dividend Yield (%)	2.3%
Upside Potential	9.8%
Max – Min LTM (P\$)	15.74 – 7.11
Market Cap (US\$m)	1,492.4
Shares Outstanding (m)	3,076.9
Float	19.24%
Daily Turnover (P\$ m)	8.3
Valuation metrics TTM	
EV/EBITDA	4.2x
P/E	10.8x

Relative performance to Mexbol

Financial Statements

MXN, million	2017	2018	2019E	2020E
Revenues	84,779	90,327	83,419	93,204
Operating Income	7,015	7,823	6,132	7,122
EBITDA	13,547	13,916	12,384	13,909
EBITDA Margin	16.0%	15.4%	14.8%	14.9%
Net Income	3,691	3,464	3,060	3,847
Net Margin	4.4%	3.8%	3.7%	4.1%
Total Assets	96,690	93,258	91,433	92,399
Cash	3,757	3,555	3,571	4,629
Total Liabilities	58,267	57,154	57,045	57,579
Debt	29,461	29,187	31,522	32,202
Common Equity	38,423	36,104	34,388	34,819

Source: Banorte with data from MSE

Valuation and financial metrics

	2017	2018	2019E	2020E
EV/EBITDA	3.8x	3.7x	4.4x	3.9x
P/E	7.1x	7.5x	8.5x	6.8x
P/Book	0.7x	0.7x	0.8x	0.7x
ROE	9.8%	9.3%	8.7%	11.1%
ROA	3.8%	3.7%	3.3%	4.2%
EBITDA/ Interest exp	6.9x	6.9x	6.9x	6.9x
Net Debt/EBITDA	1.9x	1.8x	2.3x	2.0x
Debt/Equity	0.8x	0.8x	0.9x	0.9x

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Document for distribution among public

NEMAK – Results 3Q19

MXN, million

Concept	3Q18	3Q19	Chg %	3Q19e	Diff% vs Estim.
Revenue	21,864	18,700	-14.5%	20,216	-7.5%
Operating Income	1,297	841	-35.1%	266	216.8%
Ebitda	3,026	2,703	-10.7%	2,843	-4.9%
Net Income	941	-29	N.A.	-146	-79.8%
Margins					
Operating Margin	5.9%	4.5%	-1.4pp	1.3%	3.2pp
Ebitda Margin	13.8%	14.5%	0.6pp	14.1%	0.4pp
Net Margin	4.3%	-0.2%	-4.5pp	-0.7%	0.6pp
EPS	\$0.31	-\$0.01	N.A.	-\$0.05	-79.8%

Income Statement (Million pesos)

Year	2018	2019	2019	Change	Change
Quarter	3	2	3	% yoy	% qoq
Net Revenue	21,864	19,325	18,700	-14.5%	-3.2%
Cost of goods sold	19,203	16,429	15,877	-17.3%	-3.4%
Gross profit	2,661	2,896	2,824	6.1%	-2.5%
General expenses	1,539	1,307	1,337	-13.1%	2.3%
Operating Income	1,297	1,731	841	-35.1%	-51.4%
Operating Margin	5.9%	9.0%	4.5%	(1.4pp)	(4.5pp)
Depreciation	1,716	1,588	1,299	-24.3%	-18.2%
EBITDA	3,026	3,325	2,703	-10.7%	-18.7%
EBITDA Margin	13.8%	17.2%	14.5%	0.6pp	(2.8pp)
Interes income (expense) net	63	(376)	(447)	N.A.	19.0%
Interest expense	360	376	411	14.0%	9.1%
Interest income	18	25	17	-6.0%	-30.5%
Other income (expenses)	12	125	(15)	N.A.	N.A.
Exchange Income (loss)	394	(149)	(38)	N.A.	-74.2%
Unconsolidated subsidiaries	9	(24)	26	174.8%	N.A.
Income before taxes	1,369	1,331	420	-69.4%	-68.5%
Income taxes	428	522	449	4.8%	-14.0%
Discontinued operations					
Consolidated Net Income	941	809	(29)	N.A.	N.A.
Minorities				N.A.	N.A.
Net Income	941	809	(29)	N.A.	N.A.
Net margin	4.3%	4.2%	-0.2%	(4.5pp)	(4.3pp)
EPS	0.306	0.263	(0.010)	N.A.	N.A.

Balance Sheet (Million pesos)

Total Current Assets	28,488	26,689	25,055	-12.1%	-6.1%
Cash & Short Term Investments	2,865	4,267	4,830	68.6%	13.2%
Long Term Assets	61,729	66,423	65,131	5.5%	-1.9%
Property, Plant & Equipment (Net)	48,880	50,467	50,129	2.6%	-0.7%
Intangible Assets (Net)	4,958	5,361	5,554	12.0%	3.6%
Total Assets	90,217	93,112	90,186	0.0%	-3.1%
Current Liabilities	25,248	26,205	24,767	-1.9%	-5.5%
Short Term Debt	2,638	4,231	3,925	48.8%	-7.2%
Accounts Payable	21,931	21,377	20,399	-7.0%	-4.6%
Long Term Liabilities	30,019	30,798	30,443	1.4%	-1.2%
Long Term Debt	26,056	26,515	25,988	-0.3%	-2.0%
Total Liabilities	55,267	57,002	55,210	-0.1%	-3.1%
Common Stock	34,950	36,109	34,976	0.1%	-3.1%
Noncontrolling Interest				N.A.	N.A.
Total Equity	34,950	36,109	34,976	0.1%	-3.1%
Liabilities & Equity	90,217	93,112	90,186	0.0%	-3.1%
Net Debt	25,828	26,479	25,083	-2.9%	-5.3%

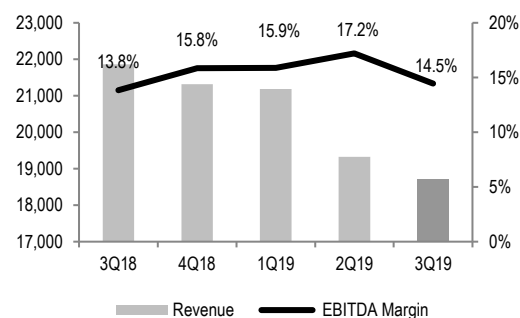
Cash Flow (Million pesos)

Cash Flow from Operating Activities	2,203.1	2,631.8	3,585.6		
Cash Flow from Investing Activities	(1,390.4)	(1,318.1)	(877.6)		
Cash Flow from Financing Activities	(1,185.7)	(646.0)	(2,169.5)		
FX differences in cash & equivalents	(218.6)	(34.0)	24.8		
Change in Cash Balance	(591.6)	633.8	563.4		

Source: Banorte, MSE.

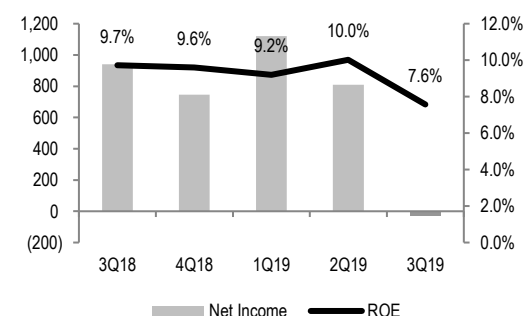
Revenue & EBITDA Margin

MXN, million



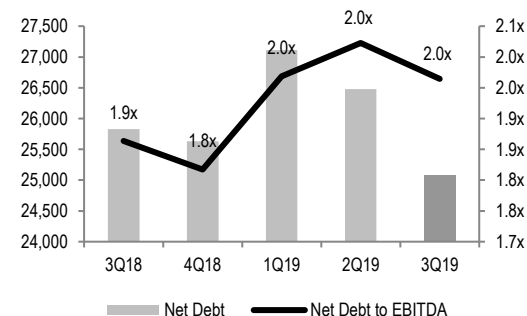
Net Income & ROE

MXN, million



Net Debt & Net debt to EBITDA ratio

MXN, million



Larger-than-expected decreases in North America and the Rest of the World. 3Q19 consolidated volume decreased 13.8% yoy to 10.6 million equivalent units, sharper than our -6.1% estimate owing to double-digit volume decreases in Nafta and the Rest of the World. Regarding Nafta, the company faced a less favorable product mix amid an environment of lower vehicle production by the Detroit Big Three, as some platforms went out of production, resulting in a 16.0% decrease in volume in that region to 6.3 million vehicles (-10.1% vs. BNTe). In Europe, volume decreased 2.9% yoy to 3.3 million, in line with our -3.5% estimate, due to lower sales to Jaguar Land Rover, while in the Rest of the World, there was a sharp 28.6% decrease to 1 million vehicles (vs. -15%e). Weakness in that region can mainly be attributed to softer demand from Ford in China associated with lower vehicle production in that country.

Lower aluminum prices and euro depreciation impacted revenues. Nematik posted revenues of US\$ 963 million for the quarter, or a 16.4% yoy decrease (far higher than our -9.7% forecast). It should be pointed out that this was not only due to the abovementioned lower volume, but also to the effect of lower aluminum prices (-13.4% yoy) and a 4.4% depreciation of the euro, which resulted in the average price per unit decreasing 3.6% yoy. As a result, variations by region were as follows: North America, -16.7% to US\$ 555 million, Europe -13.2% to US\$ 323 million, and the Rest of the World -25.4% to US\$ 85 million.

Profitability rose more than expected on the back of operating efficiencies. Although we had already expected a yoy improvement in profitability (EBITDA margin +0.2%e to 14.1%), Nematik surprised with a yoy increase of 50bps to 14.4%, a remarkable feat, especially in light of lower volume and operating deleverage, reflecting evidence of effective operating efficiencies in North America and the Rest of the World that more than offset pressure on margins in Europe derived from severance expenses in the quarter. As a result, the gross margin rose 2.9 pp yoy to 15.1%, offsetting a 30 bps increase in expenses as a percentage of revenues. Thus, EBITDA decreased 13.1% yoy to US\$ 139 million (-4.8% vs. BNTe US\$ 146 million), due to declines of 12.5% in North America (vs. -8.8%e) and 18.8% in Europe (-13.6% vs. BNTe), partially offset by a 28.6% increase in EBITDA in the Rest of the World.

Non-recurring US\$ 33 million charge from the eventual closure of the Windsor, Canada plant impacted net profit. Nematik reported a US\$ 2 million net loss for 3Q19, mainly due to an accounting charge (non-recurring asset impairment) for US\$ 33 million related to the scheduled closure of the Windsor plant in Canada. As it is virtual, the amount had no impact on EBITDA, but did impact operating profit (-37.7% yoy). Furthermore, the company reported a CFC of US\$ 23 million, comparing unfavorably with a US\$ 3 million result in 3Q18 due to a US\$ 2 million forex loss (vs. a forex gain of US\$ 21 million in the same year-earlier period).

Stable leverage qoq. Debt remained stable qoq at 2.0x ND/EBITDA, as a qoq cash increase of MXN 563 million and a MXN 834 million decrease in debt with cost offset lower LTM EBITDA.

No impact on valuation. Based on 3Q19 figures, Nemak's valuation remained at 4.2x FV/EBITDA. Nevertheless, the P/E ratio rose to 10.8x from 7.9x previously.

Performance by Region

North America (Nafta)								
	3Q18	Margin	2Q19	Margin	3Q19	Margin	% YoY	% QoQ
Volume	7.5		6.5		6.3		-16.0%	-3.1%
Revenues	\$ 666	100%	\$ 557	100%	\$ 555	100%	-16.7%	-0.4%
EBITDA	\$ 104	15.6%	\$ 100	18.0%	\$ 91	16.4%	-12.5%	-9.0%

Europe								
	3Q18	Margin	2Q19	Margin	3Q19	Margin	% YoY	% QoQ
Volume	3.4		3.7		3.3		-2.9%	-10.8%
Revenues	\$ 372	100%	\$ 368	100%	\$ 323	100%	-13.2%	-12.2%
EBITDA	\$ 48	12.9%	\$ 59	16.0%	\$ 39	12.1%	-18.8%	-33.9%

Rest of the World								
	3Q18	Margin	2Q19	Margin	3Q19	Margin	% YoY	% QoQ
Volume	1.4		1		1.0		-28.6%	0.0%
Revenues	\$ 114	100%	\$ 87	100%	\$ 85	100%	-25.4%	-2.3%
EBITDA	\$ 7	6.1%	\$ 16	18.4%	\$ 9	10.6%	28.6%	-43.8%

Consolidated								
	3Q18	Margin	2Q19	Margin	3Q19	Margin	% YoY	% QoQ
Volume	12.3		11.2		10.6		-13.8%	-5.4%
Revenues	\$ 1,152	100%	\$ 1,012	100%	\$ 962	100%	-16.5%	-4.9%
EBITDA	\$ 159	13.8%	\$ 175	17.3%	\$ 139	14.4%	-12.6%	-20.6%

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, Luis Leopoldo López Salinas, Jorge Antonio Izquierdo Lobato and Leslie Thalia 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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History of PT and Ratings

Stock	Date	Rating	PT
NEMAK A	17/07/2019	Hold	\$10.00
NEMAK A	25/02/2019	Sell	\$13.00
NEMAK A	14/01/2019	Buy	\$17.00
NEMAK A	18/04/2018	Buy	\$16.00

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