Equity Research
Mexico

AZTECA

Quarterly Report

February 19, 2019

Ended 2018 with sharp pressure on margins

- **TV Azteca reported weak quarterly results, below our estimates. In 4Q18, the company faced a downturn in advertising revenue and an increase in programing costs**
- **In 2019, a significant reduction in government advertising spending as well as a slowdown in economic activity is expected, which will have a negative effect on the generation of profits**
- **High leverage is a negative factor for the share's valuation. We have set a PT 2019 of MXN 1.60, which represents a 6.5x FV/EBITDA multiple. We have downgraded our recommendation to SELL**

Substantial profitability erosion in 4Q18 and a difficult 2019 outlook. We rate TV Azteca's earnings as weak, reporting below our expectations at operating level. The company experienced sluggish advertising demand and lower export revenue, falling 7.8% in consolidated revenue to MXN 3.6 billion. What's more, production and programing costs surged 11% yoy due to production efforts to create higher-quality programs and more elevated costs charged by soccer teams to broadcast their games. Against this backdrop, EBITDA plunged 31% to MXN 977 million and the margin fell 8.9pp to 26.5%. The broadcasting company reported MXN 109 million in net losses, which favorably compares to the MXN 1.3 billion loss in 4Q17. Within our projection model, we have incorporated these results, the expectation of lower advertising spending by the federal government, a slowdown in the Mexican economy (GDP 1.5%e) and an exchange rate depreciation to MXN 21.30 per U.S. dollar. Under this scenario, we have determined a PT 2019 of MXN 1.60 using a multiples valuation model (6.5x FV/EBITDA). We have revised our recommendation from Hold to **SELL.**

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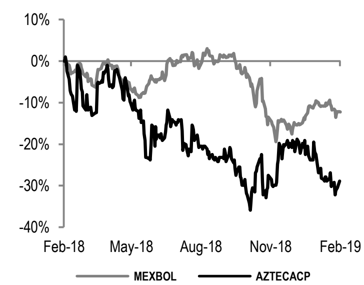
SELL

Current Price	$2.12
PT2019	**$1.60**
Dividend 2019	$0.01
Dividend (%)	0%
Upside Potential	-24.2%
Max – Min LTM	3.01 - 1.91
Market Cap (US$m)	239
Shares Outstanding (m)	2,987
Float	35%
Daily Turnover (MXN$m)	1
Valuation Metrics LTM *	
FV/EBITDA	6.6x
P/E	N.A

Relative performance to MEXBOL
(LTM)



Financial statements

USD, million	2017	2018	2019E	2020E
Revenues	13,829	14,534	13,622	13,997
Operating Income	2,554	1,579	1,811	1,955
Adjusted EBITDA	4,090	2,746	2,709	2,861
EBITDA Margin	29.6%	18.9%	19.9%	20.4%
Net Income	-1,163	-647	40	624
Net margin	-8.4%	-4.5%	0.3%	4.5%
Total Assets	28,033	28,408	28,382	29,082
Cash	2,783	1,752	1,746	2,248
Total Liabilities	23,794	25,013	25,752	26,340
Debt	13,740	13,663	14,314	14,444
Common Equity	4,238	3,395	2,630	2,742

Source: Banorte

Valuation and financial metrics

	2017	2018	2019E	2020E
FV/EBITDA	4.2x	6.6x	7.0x	6.6x
P/E	-5.4x	-9.8x	-9.8x	216.6x
P/BV	1.5x	1.9x	2.6x	2.6x
ROE	-27.4%	-19.1%	-26.4%	1.2%
ROA	-4.2%	-2.3%	-2.3%	0.1%
EBITDA/ Interest exp	2.9x	2.1x	2.1x	2.2x
Net Debt/EBITDA	2.7x	4.3x	4.7x	4.4x
Debt/Equity	3.2x	4.0x	5.9x	5.9x

AZTECA – 4Q18 Results

MXN, Million

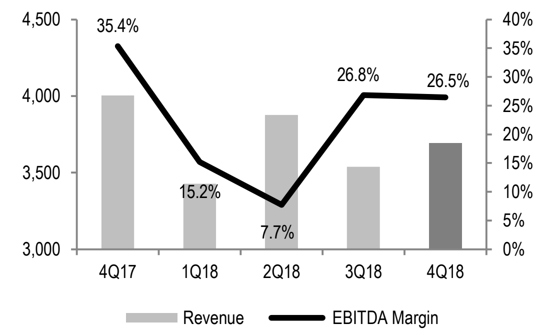
Concept	4Q17	4Q18	Var %	4Q18e	Diff % vs. Estim.
Revenue	4,005	3,693	-7.8%	4,080	-9.5%
Operating Income	643	561	-12.7%	952	-41.0%
Ebitda	1,416	977	-31.0%	1,197	-18.4%
Net Income	-1,319	-109	-91.7%	217	N.A.
Margins					
Operating Margin	16.1%	15.2%	-0.9pp	23.3%	-8.1pp
Ebitda Margin	35.4%	26.5%	-8.9pp	29.3%	-2.9pp
Net Margin	-32.9%	-3.0%	30.0pp	5.3%	-8.3pp
EPS	-$0.44	-$0.04	-91.7%	$0.07	N.A.

Income Statement (Million)					
Year	**2017**	**2018**	**2018**	**Change**	**Change**
Quarter	**4**	**3**	**4**	**% yoy**	**%qoq**
Net Revenue	**4,004.9**	**3,538.6**	**3,692.6**	**-7.8%**	**4.4%**
Cost of goods sold	2,251.1	2,301.3	2,475.0	9.9%	7.6%
Gross profit	1,753.7	1,237.3	1,217.5	-30.6%	-1.6%
General expenses	526.1	467.8	412.3	-21.6%	-11.9%
Operating Income	**643.0**	**683.6**	**561.4**	**-12.7%**	**-17.9%**
Operating Margin	**16.1%**	**19.3%**	**15.2%**	**(0.9pp)**	**(4.1pp)**
Depreciation	188.2	179.3	171.7	-8.8%	-4.3%
EBITDA	**1,415.9**	**948.8**	**976.9**	**-31.0%**	**3.0%**
EBITDA Margin	**35.4%**	**26.8%**	**26.5%**	**(8.9pp)**	**(0.4pp)**
Interest income (expense) net	**(929.0)**	**23.2**	**(554.6)**	**-40.3%**	**N.A.**
Interest expense	357.1	296.7	342.8	-4.0%	15.5%
Interest income	19.7	52.3	75.7	284.7%	44.8%
Other financial income (expense)	(112.7)	(70.3)	(17.7)	-84.3%	-74.8%
Exchange Income (loss)	(478.9)	337.9	(269.7)	-43.7%	N.A.
Unconsolidated subsidiaries	(44.5)	(49.4)	100.8	N.A.	N.A.
Net Income before taxes	**(330.5)**	**657.4**	**107.6**	**N.A.**	**-83.6%**
Provision for Income taxes	195.4	219.6	220.4	12.8%	0.3%
Discontinued Operations	(789.3)				
Consolidated Net Income	**263.4**	**437.7**	**(112.8)**	**N.A.**	**N.A.**
Minorities	3.3	(0.4)	(3.6)	N.A.	>500%
Net Income	**(1,318.6)**	**438.1**	**(109.2)**	**-91.7%**	**N.A.**
Net Margin	**-32.9%**	**12.4%**	**-3.0%**	**30.0pp**	**(15.3pp)**
EPS	**(0.442)**	**0.147**	**(0.037)**	**-91.7%**	**N.A.**
Balance Sheet (Million)					
Total Current Assets	**13,106.6**	**16,618.6**	**9,980.7**	-23.9%	-39.9%
Cash & Short Term Investments	2,782.9	4,897.2	1,752.4	-37.0%	-64.2%
Long Term Assets	**14,926.3**	**14,179.1**	**18,427.1**	23.5%	30.0%
Property, Plant & Equipment (Net)	3,755.0	3,558.1	3,542.9	-5.6%	-0.4%
Intangible Assets (Net)	5,679.0	5,672.6	9,615.9	69.3%	69.5%
Total Assets	**28,032.9**	**30,797.7**	**28,407.8**	**1.3%**	**-7.8%**
Current Liabilities	**8,866.1**	**12,787.0**	**9,639.9**	**8.7%**	**-24.6%**
Short Term Debt	36.8	78.8	62.0	68.4%	-21.3%
Accounts Payable	4,815.3	7,989.9	4,731.5	-1.7%	-40.8%
Long Term Liabilities	**14,928.4**	**14,735.2**	**15,373.4**	**3.0%**	**4.3%**
Long Term Debt	13,703.2	13,222.4	13,601.2	-0.7%	2.9%
Total Liabilities	**23,794.4**	**27,522.2**	**25,013.3**	**5.1%**	**-9.1%**
Common Stock	4,238.5	3,275.5	3,394.5	-19.9%	3.6%
Minorities	5.7	(3.4)	(7.0)	N.A.	108.3%
Total Equity	**4,232.8**	**3,278.9**	**3,401.5**	**-19.6%**	**3.7%**
Liabilities & Equity	**28,032.9**	**30,797.7**	**28,407.8**	**1.3%**	**-7.8%**
Net Debt	**10,957.1**	**8,362.9**	**11,910.7**	**8.7%**	**42.4%**
Cash Flow					
Cash Flow from Operating Activities	686.0	1,696.0	1,034.7		
Cash Flow from Investing Activities	(716.4)	(99.6)	(4,034.9)		
Cash Flow from Financing Activities	(3,305.8)	(557.1)	(144.6)		
Increase (decrease) in cash	**(3,336.2)**	**1,039.3**	**(3,144.8)**		

Source: Banorte, MSE

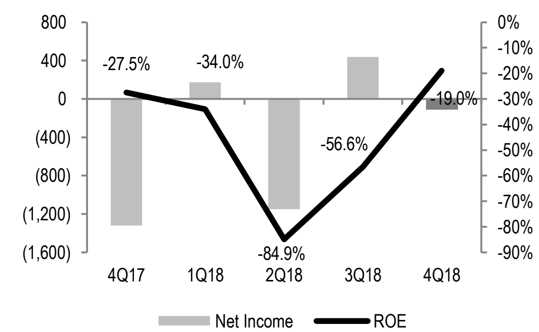
Revenue & EBITDA Margin

MXN, million



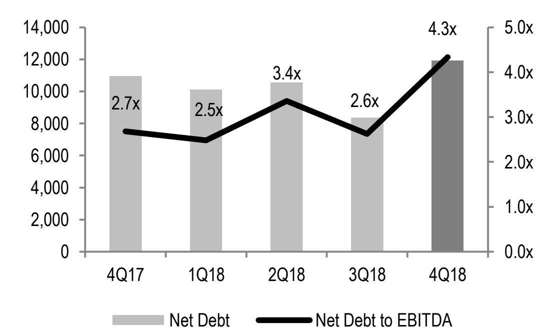
Net Income & ROE

MXN, million



Net Debt & Net Debt to EBITDA

MXN, million



Decline in EBITDA impacted valuation benchmarks. By incorporating this quarter's weak results, the ND/EBITDA ratio rose from 2.6x in 3Q18 to 4.3x and the FV/EBITDA multiple increased from 4.6x to 6.6x. In view of higher valuation benchmarks and greater leverage, we expect a negative reaction in the price of the share and a downward revision of estimates by analysts.

The company renewed television channel concessions for the next 20 years. It is worth mentioning that during the period, the Federal Telecommunications Institute (IFT) renewed the company's television channel concessions for 20 years, starting January 1st, 2022; therefore, TV Azteca paid MXN 3.9 billion for such concept, which had already been considered in our estimates and had contributed to a reduction of cash.

2019 Estimates. From our point of view, the company will face significant challenges during 2019. During the year, we expect a considerable reduction in government advertising spending, which according to the company represents approximately 15% of total advertising revenue. In addition, we anticipate a downturn in spending by advertisers, reflecting a slowdown in the Mexican economy and an impact of the exchange rate depreciation over the company's interest-bearing debt and over its earnings.

Based on the latter, we estimate a 6.3% annual drop in consolidated revenue to MXN 13.6 billion. During the past year, the company rose production costs in search of higher-quality content. However, in 2019 we expect greater control in costs and expenses to limit the impact of lower revenue over its margins. At EBITDA level, we estimate MXN 2.7 billion, which would represent a fall of 1.3% yoy and a 1pp expansion on the corresponding margin. This assumption could be slightly optimistic, thus posing a downside risk to this estimate.

As for Net Interest Expense, we estimate an annual 42% increase to MXN 1.7 billion, primarily from the impact of currency fluctuation over debt denominated in foreign currency. We forecast MXN 493 million in FX losses vs. MXN 34 million in FX profit in 2018 while as for interests paid, we estimate a 1% reduction.

On the other hand, we estimate a Capex amount of US$ 28 million, which would represent 4% of consolidated revenue; while for interest-bearing debt, we estimate an amount of MXN 14.3 million, up 4.8% yoy. The combination of higher interest-bearing debt and EBITDA reduction would result in a ND/EBITDA ratio increase to 4.7x.

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We, Gabriel Casillas Olvera, Delia Maria Paredes Mier, Alejandro Padilla Santana, Manuel Jiménez Zaldívar, 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, Francisco Duarte Alcocer, Jorge Antonio Izquierdo Lobato and Leslie Thalía 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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	Reference
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HOLD	*When the share expected performance is similar to the MEXBOL estimated performance.*
SELL	*When the share expected performance is lower than the MEXBOL estimated performance.*

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PT and recommendation history

Stock	Date	Recommendation	PT
Azteca CPO	24/07/2018	Sell	$2.50
Azteca CPO	20/02/2018	Hold	$3.80
Azteca CPO	25/10/2017	Hold	$4.50
Azteca CPO	19/07/2017	Hold	$4.50

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