ALPEK

Quarterly Report

July 18, 2019

Figures in line, with sequential improvements

- **Alpek's results were weak, but in line with our estimates, affected by volatility in feedstock prices, but with sequential improvements in both business segments**
- **Revenue fell 8.0% yoy and EBITDA contracted by 34.0% yoy. Despite the latter, greater stability in polyester margins is observed, with qoq upgrades, and a solid Polypropylene (PP) performance**
- **We have downgraded our PT2019 to MXN$30.00, assuming a more conservative stance, but reiterate a BUY rating, as current valuation levels (FV/EBITDA 5.2x) still seem highly attractive**

Weak figures as expected, but with sequential improvement in profitability. During 2Q19, Alpek's results were weak, but in line with our estimates. Sales fell 8.0% yoy to MXN$31.4 billion, hit mainly by weakness in prices, while EBITDA contracted by 34.0% yoy to MXN$3.0 billion. This result was impacted by inventory losses adjustments, given a weaker than expected feedstock context, particularly for *paraxylene*, and despite the sequential recovery of oil prices. On a comparable basis, excluding non-recurring adjustments and benefits, EBITDA would have declined just 14.8% yoy to MXN$3.6 billion. The greatest weakness was reported in the Polyester segment, although with improvement in profitability for both business segments qoq. After incorporating these results, the FV/EBITDA multiple increases from 4.7x to 5.2x, yet still stands far below the median for comparable companies (6.9x). By assuming a more conservative position in terms of valuation, in view of the prevailing local uncertainty and a drop in investors' confidence, we have downgraded our PT2019 to MXN$30.00, representing a 5.7x 2019e FV/EBITDA. We reiterate BUY.

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BUY	
Current Price	MXN$23.54
PT2019	**MXN$30.00**
Dividend 2019	MXN$ 1.30
Dividend (%)	5.5%
Upside Potential	33.0%
Max – Mín LTM	32.99-21.77
Market Cap (USD$m)	2,622.3
Shares outstanding (m)	2,118
Float	17.9%
Daily Turnover (MXN$m)	42.8
Valuation Metrics LTM *	
FV/EBITDA Adj	5.2x
P/E	4.6x

Relative performance to MEXBOL
(LTM)

Financial statements

MXN, Million	2017	2018	2019E	2020E
Revenues	98,998	134,523	135,742	148,391
Operating Income	-2,854	21,202	14,767	12,962
Adjusted EBITDA	7,484	20,607	17,891	15,955
EBITDA Margin	7.56%	15.32%	13.18%	10.75%
Net Income	-5,487	13,633	7,385	6,158
Net margin	-5.54%	10.13%	5.44%	4.15%
Total Assets	93,778	119,897	125,232	131,237
Cash	8,795	4,168	10,800	10,602
Total Liabilities	62,114	76,734	74,474	75,301
Debt	35,073	41,464	43,944	46,108
Common Equity	31,664	43,163	50,758	55,936

Source: Banorte

Valuation and financial metrics

	2017	2018	2019E	2020E
FV/EBITDA	10.8x	4.5x	4.9x	5.7x
P/E	-9.1x	3.7x	6.8x	8.0x
P/BV	1.9x	1.3x	1.1x	1.0x
ROE	-20.4%	35.8%	16.2%	12.6%
ROA	-5.9%	11.4%	5.9%	4.7%
EBITDA/ Interest expen	5.6x	11.9x	15.1x	10.8x
Net Debt/EBITDA	3.5x	1.8x	1.9x	2.2x
Debt/Equity	1.1x	1.0x	0.9x	0.8x

ALPEK –2Q19 Results
MXN, Millions

Concept	2Q18	2Q19	Var %	2Q19e	Diff % vs Estim.
Revenue	34,143	31,425	-8.0%	33,074	-5.0%
Operating Income	3,933	2,099	-46.6%	2,421	-13.3%
Ebitda	4,662	3,077	-34.0%	3,134	-1.8%
Net Income	2,752	1,064	-61.3%	1,330	-20.0%
margins					
Operating Margin	11.5%	6.7%	-4.8pp	7.3%	-0.6pp
Ebitda Margin	13.7%	9.8%	-3.9pp	9.5%	0.3pp
Net Margin	8.1%	3.4%	-4.7pp	4.0%	-0.6pp
EPS	$1.30	$0.50	-61.3%	$0.63	-20.0%

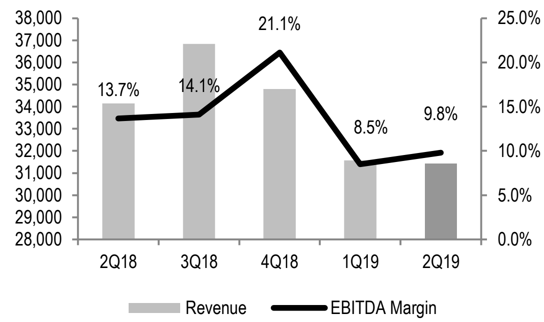
Income Statement (Millions)					
Year	**2018**	**2019**	**2019**	**Var%**	**Var%**
Quarter	**2**	**1**	**2**	**% YoY**	**% QoQ**
Net Revenue	**34,142.8**	**31,567.3**	**31,425.0**	**-8.0%**	**-0.5%**
Cost of goods sold	28,966.2	28,909.6	28,460.1	-1.7%	-1.6%
Gross profit	5,176.6	2,657.7	2,964.9	-42.7%	11.6%
General expenses	1,243.2	935.2	866.3	-30.3%	-7.4%
Operating Income	3,933.4	1,722.5	2,098.6	-46.6%	21.8%
Operating Margin	11.5%	5.5%	6.7%	**(4.8pp)**	**1.2pp**
Depreciation	715.9	960.9	978.3	36.6%	1.8%
EBITDA	**4,662.0**	**2,684.0**	**3,077.0**	**-34.0%**	**14.6%**
EBITDA Margin	13.7%	8.5%	9.8%	**(3.9pp)**	**1.3pp**
Interest income (expense) net	(217.0)	(429.1)	(354.4)	**63.4%**	**-17.4%**
Interest expense	454.6	551.8	568.4	25.0%	3.0%
Interest income	27.2	33.8	40.0	47.1%	18.6%
Exchange Income (loss)	(46.0)	34.1	43.4	N.A.	27.3%
Unconsolidated subsidiaries	256.4	54.8	130.6	-49.1%	138.4%
Unconsolidated subsidiaries	(0.5)	(3.8)	(0.7)	56.9%	-81.3%
Net Income before taxes	3,716.0	1,289.5	1,743.5	**-53.1%**	**35.2%**
Provision for Income taxes	640.5	524.6	419.5	-34.5%	-20.0%
Discontinued Operations					
Consolidated Net Income	3,075.5	765.0	1,324.0	-57.0%	73.1%
Minorities	323.5	247.6	259.9	-19.6%	5.0%
Net Income	**2,752.0**	**517.3**	**1,064.0**	**-61.3%**	**105.7%**
Net Margin	**8.1%**	**1.6%**	**3.4%**	**(4.7pp)**	**1.7pp**
EPS	**1.300**	**0.244**	**0.503**	**-61.3%**	**105.7%**

Balance Sheet (MXN, million)					
Total Current Assets	**45,896.5**	**45,500.8**	**44,526.4**	-3.0%	-2.1%
Cash & Short Term Investments	4,426.2	4,447.2	5,493.2	24.1%	23.5%
Long Term Assets	63,793.1	71,584.0	70,650.9	10.8%	-1.3%
Property, Plant & Equipment (Net)	**49,254.2**	**47,094.8**	**46,823.9**	-4.9%	-0.6%
Intangible Assets (Net)	3,591.6	3,940.7	3,836.4	6.8%	-2.6%
Total Assets	**109,689.6**	**117,084.8**	**115,177.3**	**5.0%**	**-1.6%**
Current Liabilities	31,641.9	36,386.6	33,679.4	6.4%	-7.4%
Short Term Debt	6,506.8	14,997.0	13,718.7	110.8%	-8.5%
Accounts Payable	24,024.6	20,194.4	19,257.8	-19.8%	-4.6%
Long Term Liabilities	**44,465.0**	**40,549.7**	**40,913.3**	-8.0%	0.9%
Long Term Debt	**31,143.4**	**32,887.1**	**33,336.3**	7.0%	1.4%
Total Liabilities	**76,106.9**	**76,936.3**	**74,592.6**	**-2.0%**	**-3.0%**
Common Stock	33,582.7	40,148.5	40,584.7	20.8%	1.1%
Minorities	4,951.8	4,541.6	4,707.3	-4.9%	3.6%
Total Equity	**28,630.9**	**35,606.9**	**35,877.4**	**25.3%**	**0.8%**
Liabilities & Equity	**109,689.6**	**117,084.8**	**115,177.3**	**5.0%**	**-1.6%**
Net Debt	**33,223.9**	**43,436.9**	**41,561.9**	**25.1%**	**-4.3%**

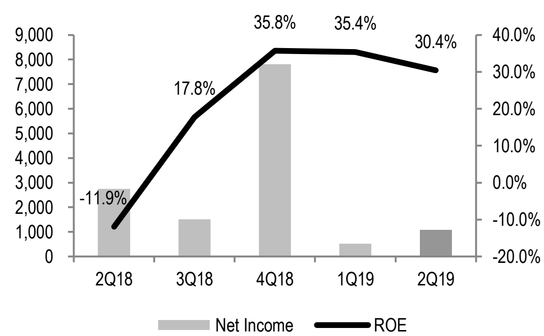
Cash Flow					
Cash Flow from Operating Activities	5,207.9	2,227.0	7,042.6		
Cash Flow from Investing Activities	(9,261.8)	(1,221.4)	(1,743.3)		
Cash Flow from Financing Activities	745.1	(65.5)	(2,210.3)		
Increase (decrease) in cash	(4,080.9)	358.0	1,370.3		

Source: Banorte, MSE

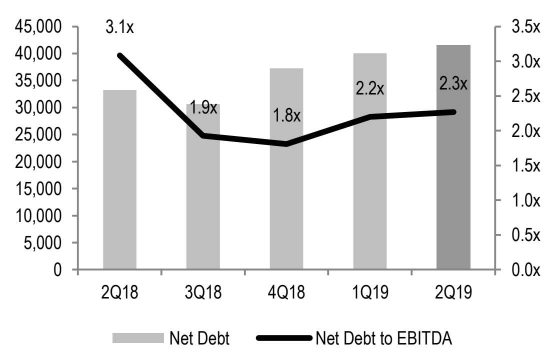
Revenue & EBITDA Margin
MXN, million



Net Income & ROE
MXN, million



Net Debt & Net Debt to EBITDA
MXN, million



Polyester reflects temporary distortion in margins, given weakness in *paraxylene* prices, but with qoq improvements. This quarter, sales from the Polyester business fell 7.3% yoy to MXN$23.7 billion, resulting from a 5.0% yoy decline in average prices and the 3.0% year-on-year drop in sales volumes. In terms of EBITDA, it reflects a 42.1% yoy contraction having reached MXN$1.8 billion, affected by this segment's temporary margin distortion. Although oil prices posted a sequential recovery during the quarter, a disparity was seen in *paraxylene* reference prices, because of new capacity additions in China, causing a negative feedstock cost carry over effect, and reflecting a temporary margin distortion. On a comparable basis, excluding extraordinary items and inventory adjustments, EBITDA would have fallen just 16.3% yoy to stand at MXN$2.3 billion, reflecting a 1.1pp contraction in EBITDA margin yoy, but a significant sequential improvement which translates into a 45.7% qoq growth in EBITDA and correspondingly, a 3.1pp expansion in the corresponding margin to 9.9%. It should be mentioned that if paraxylene prices continue to stabilize as they did in June, the second half of the year could offset accumulated losses reported during the first half from this effect.

Polyester
MXN, Million

	2Q18	Margin	1Q19	Margin	2Q19	Margin	% yoy	% qoq
Revenue	25,615	100.0%	23,823	100.0%	23,749	100.0%	-7.3%	-0.3%
EBITDA	3,159	12.3%	1,541	6.5%	1,830	7.7%	-42.1%	18.8%
EBITDA*	2,809	11.0%	1,614	6.8%	2,352	9.9%	-16.3%	45.7%

* Inventory and non – operating (non – recurring) gains/losses are not included
Source: Alpek

Plastics and Chemicals boosted by a better-than-expected performance in *polypropylene (PP)*. This quarter, revenue from this segment fell 15.9% yoy to MXN$7.1 billion due to the 14% year-on-year drop in peso-denominated average prices and an almost 2% yoy decline in sales volume. As for EBITDA, a 23.6% yoy contraction was reported, yet by excluding inventory impairment charges, on a comparable basis, EBITDA would have declined just 18.9% yoy, given weakness in prices. On a sequential basis, revenue remained practically stable while EBITDA rose 12.1% qoq due to higher-than-expected *polypropylene* margins, which were partially offset by the ongoing weakness in *caprolactam.*

Plastics and Chemicals
MXN, Million

	2Q18	Margin	1Q19	Margin	2Q19	Margin	% yoy	% qoq
Revenue	8,522	100.0%	7,229	100.0%	7,168	100.0%	-15.9%	-0.8%
EBITDA	1,526	17.9%	1,040	14.4%	1,166	16.3%	-23.6%	12.1%
EBITDA*	1,462	17.2%	1,120	15.5%	1,185	16.5%	-18.9%	5.8%

* Inventory and non – operating (non – recurring) gains/losses are not included
Source: Alpek

Net profit affected by operating weakness. In terms of net profit, the company reported MXN$1.0 billion, short of expectations and representing a 61.3% yoy decline, given the weak operating performance and higher-than-expected financial costs. Paid interests increased 25.0% year-on-year given a higher debt level and FX gains plunged 49.1% yoy due to a less favorable FX effect than what had been expected.

Alpek maintains a solid balance sheet despite the implementation of IFRS 16. The company's net debt by the end of the quarter amounted to MXN$41.5 billion, down 4.3% over that reported in 1Q19, given a favorable variation in working capital and the recovery of tax credits by Suape/Citepe in Brazil. It should be stated that in view of the adoption of IFRS 16 accounting standards on leasing, as of January of this year, MXN$3.2 billion were reported as lease liability this quarter, which represents 7.5% of the company's interest-bearing debt. The Net Debt/ /EBITDA ratio increases to 2.3x in 2Q19 vs 2.2x in 1Q19, with an 8.1x interest coverage ratio. Despite the latter, once the resources from the cogeneration power plants are received, expected by 3Q19, this ratio should scale down again to levels below 2.0x.

Investments. During this quarter, the company invested US$38 million primarily to finish the construction of the co-generation plant in Altamira and Minor asset replacements and capital projects. Thus, so far investments now accumulate US$107 million, nearly 34% of the amount scheduled for 2019 (US$310 million).

Pending the resources from the sale of the cogeneration power plants. The company commented that the sale process of the two cogeneration power plants continued to move forward, with the sale expected to have favorably concluded in the next months. Once the company receives the corresponding proceeds from this sale, Alpek plans to distribute an extraordinary dividend of US$143 million, equaling roughly MXN$1.30 per share, a 5.5% *yield.*

We have downgraded our PT 2019 to MXN$30.00 but reiterate our BUY recommendation. Despite this quarter's weakness, we consider that current valuation levels have already priced-in such results, and we expect these will improve by the second half of the year. After incorporating these figures, the FV/EBITDA multiple increases from 4.7x to 5.2x. However, this level still stands far below the average of comparable companies (8.9x) according to the Bloomberg consensus, but also lower than the 6.9x median. In any case, given the prevailing local uncertainty, we have decided to assume a more conservative position, lowering our long-term growth forecasts and adjusting the multiple we use for the terminal value in our DCF valuation model to 6.0x (previous 6.5x). Accordingly, we have downgraded our PT 2019 to MXN$30.00 from MXN$35.00, which would represent a 5.7x 2019e FV/EBITDA multiple, above the current multiple that we mentioned standing at 5.2x. We must consider that the outlook moving forward is better, considering higher expected stability in global-wide reference margins and significant financial strength upheld by Alpek, even more so considering the upcoming resource inflow from the sale of the co-generation power plants. Therefore, we reiterate our BUY recommendation.

Valuation. Our target price has been estimated using a discounted cash flow valuation model, through a 9.11% discount rate (WACC), which assumes a 12.5% cost of equity, through an 8.4% risk-free rate (the 10-year Mexican bond estimate), a 0.75 beta and a 5.5% market risk premium. The average debt cost is 7.5%, and the debt-capitalization ratio stands at 46.5%. For the terminal value (perpetuity), we are considering a 6.0x FV/EBITDA multiple, below the median for global-wide comparable companies (6.9x) according to the Bloomberg consensus. We would rather be conservative with our valuation given the prevailing local uncertainty and lower confidence among investors.

Discounted Cash Flows Model

MXN, million

	2019e	2020e	2021e	2022e	2023e	2024e	2025e	Perpet.
(+) EBITDA	17,891	15,955	16,434	16,927	17,434	17,958	18,496	
(-) Change in working capital	(786)	(2,325)	(1,972)	(2,031)	(2,092)	(2,155)	(2,220)	
(-) Capex	(3,375)	(3,300)	(3,300)	(3,399)	(3,501)	(3,606)	(3,714)	
(-) Taxes	(4,285)	(3,084)	(3,615)	(3,724)	(3,836)	(3,951)	(4,069)	
(=) Free cash flow	9,445	7,246	7,546	7,773	8,006	8,246	8,493	
(+) Perpetuity	0	0	0	0	0	0	0	114,307
(=) Total cash flow	9,445	7,246	7,546	7,773	8,006	8,246	8,493	114,307

			YE19
Risk - Free rate (RF)	8.4%	(+) Present value of cash flows	34,974
		(+) Present value of perpetuity	62,075
Equity risk premium (ERP)	5.5%	**= Firm value**	**97,049**
Beta	0.75		
CAPM	**12.48%**	(-) Net debt	(33,144)
Debt cost	7.50%	**(=) Equity value**	**63,905**
Tax rate	30%	Shares outstanding	2,118
Net cost of debt	**5.25%**		
Debt / Capitalization	46.5%	Price Target MXN$	**30.17**
WACC	**9.11%**		
Terminal Value	6.0x		

Source: Banorte estimates

Relative Valuation

ISSUER	PRICE	Market Cap (US$MM)	Enterprise Value (US$MM)	P/BV	P/E	P/E 2019E	P/E 2020E	FV/EBITDA	FV/EBITDA 2019E	FV/EBITDA 2020E	DIVIDEND YIELD
AMERICA											
LYONDELLBASELL INDU-CL A	USD 85.73	31,748	42,583	4.3x	8.3x	8.2x	7.0x	6.4x	6.7x	6.0x	4.9%
EASTMAN CHEMICAL CO	USD 77.96	10,820	17,372		10.1x	9.2x	8.4x	8.0x	7.8x	7.4x	3.2%
CELANESE CORP-SERIES A	USD 0.00										
BRASKEM SA-PREF A	BRL 35.90	7,637	14,848	5.4x	10.1x	17.4x	11.6x	4.9x	6.2x	5.8x	
MEXICHEM SAB DE CV	P$ 41.54	4,575	469		11.9x	12.0x	10.7x	6.5x	6.4x	5.7x	
	Average	*13,695*	*18,818*	*4.8x*	*10.1x*	*11.7x*	*9.4x*	*6.4x*	*6.8x*	*6.2x*	*4.0%*
	Median	*9,228*	*16,110*	*4.8x*	*10.1x*	*10.6x*	*9.5x*	*6.5x*	*6.5x*	*5.9x*	*4.0%*
EUROPA & ASIA											
BASF SE	€ 60.78	62,675	87,116	2.8x	15.8x	14.5x	12.7x	8.7x	9.1x	8.1x	5.3%
FORMOSA PLASTICS CORP	TWD 102.00	20,891	19,109	1.7x	16.6x	14.1x	12.8x	19.0x	18.9x	17.5x	5.7%
NAN YA PLASTICS CORP	TWD 72.60	18,525	19,291	1.5x	17.1x	15.9x	15.1x	15.0x	16.7x	16.2x	6.9%
FORMOSA CHEMICALS & FIBRE	TWD 97.10	18,311	19,032	1.5x	15.8x	13.8x	14.0x	10.9x	12.3x	12.8x	6.4%
PETRONAS CHEMICALS GROUP BHD	MYR 7.92	15,399	13,384	2.1x	13.4x	15.2x	13.4x	8.2x	8.9x	7.9x	4.0%
SOLVAY SA	€ 89.56	10,646	17,388		12.4x	10.7x	10.0x	7.7x	6.7x	6.4x	4.2%
HONAM PETROCHEMICAL CORP	KRW 0.00										
MITSUBISHI CHEMICAL HOLDINGS	JPY 752.40	10,501	32,192	6.7x	6.3x	6.7x	6.3x	7.4x	6.7x	6.4x	
SUMITOMO CHEMICAL CO LTD	JPY 491.00	7,531	16,159	1.2x		8.3x	7.9x	6.8x	5.5x	5.3x	4.5%
INDORAMA VENTURES PCL	THB 40.75	7,408	12,192	2.3x	9.7x	10.1x	8.9x	8.2x	8.2x	7.5x	0.9%
SINOPEC SHANGHAI PETROCHE-A	CNY 5.15	6,788	5,195	1.8x	13.6x	14.0x	13.6x		6.2x	6.4x	
LANXESS AG	€ 54.14	5,315	7,145	4.7x	29.3x	13.5x	12.1x	7.7x	6.2x	5.9x	1.7%
MITSUI CHEMICALS INC	JPY 2,568.00	4,866	9,164	1.0x	6.7x	7.4x	7.0x	6.9x	6.6x	6.2x	3.9%
SUMITOMO SEIKA CHEMICALS CO	JPY 3,365.00	436	507	0.7x	76.8x						3.0%
	Average	*14,561*	*19,836*	*2.3x*	*19.5x*	*12.0x*	*11.1x*	*9.7x*	*9.3x*	*8.9x*	*4.2%*
	Median	*10,501*	*16,159*	*1.8x*	*14.7x*	*13.7x*	*12.4x*	*8.2x*	*7.5x*	*6.9x*	*4.2%*
GLOBAL	*Average*	*14,357*	*19,597*	*2.7x*	*17.1x*	*11.9x*	*10.7x*	*8.8x*	*8.7x*	*8.2x*	*4.2%*
	Median	*10,501*	*16,159*	*2.0x*	*12.9x*	*12.8x*	*11.1x*	*7.7x*	*6.7x*	*6.4x*	*4.2%*
ALPEK SA DE CV	**Ps 23.54**	**2,614**	**97,829**		**4.6x**	**9.2x**	**10.1x**	**4.2x**	**6.4x**	**6.7x**	**5.6%**

Source: Bloomberg

Certification of Analysts.

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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Last-twelve-month activities of the business areas.

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Over the course of the last twelve months, Grupo Financiero Banorte S.A.B. C.V., has not obtained compensation for services rendered by the investment bank or by any of its other business areas of the following companies or their subsidiaries, some of which could be analyzed within this report.

Activities of the business areas during the next three months.

Casa de Bolsa Banorte, Grupo Financiero Banorte or its subsidiaries expect to receive or intend to obtain revenue from the services provided by investment banking or any other of its business areas, by issuers or their subsidiaries, some of which could be analyzed in this report.

Securities holdings and other disclosures.

As of the end of last quarter, Grupo Financiero Banorte S.A.B. of C.V. has not held investments, directly or indirectly, in securities or derivative financial instruments, whose underlying securities are the subject of recommendations, representing 1% or more of its investment portfolio of outstanding securities or 1 % of the issuance or underlying of the securities issued.

None of the members of the Board of Grupo Financiero Banorte and Casa de Bolsa Banorte, along general managers and executives of an immediately below level, have any charges in the issuers that may be analyzed in this document.

The Analysts of Grupo Financiero Banorte S.A.B. of C.V. do not maintain direct investments or through an intermediary person, in the securities or derivative instruments object of this analysis report.

Guide for investment recommendations.

	Reference
BUY	*When the share expected performance is greater than the MEXBOL estimated performance.*
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.*

Even though this document offers a general criterion of investment, we urge readers to seek advice from their own Consultants or Financial Advisors, in order to consider whether any of the values mentioned in this report are in line with their investment goals, risk and financial position.

Determination of Target Prices

For the calculation of estimated target prices for securities, analysts use a combination of methodologies generally accepted among financial analysts, including, but not limited to, multiples analysis, discounted cash flows, sum-of-the-parts or any other method that could be applicable in each specific case according to the current regulation. No guarantee can be given that the target prices calculated for the securities will be achieved by the analysts of Grupo Financiero Banorte S.A.B. C.V, since this depends on a large number of various endogenous and exogenous factors that affect the performance of the issuing company, the environment in which it performs, along with the influence of trends of the stock market, in which it is listed. Moreover, the investor must consider that the price of the securities or instruments can fluctuate against their interest and cause the partial and even total loss of the invested capital.

Historical PT and Rating

Stock	Date	Rating	PT
ALPEK	July 17, 2019	BUY	MXN$30.00
ALPEK	January 14, 2019	BUY	MXN$35.00
ALPEK	July 19, 2018	BUY	MXN$39.50
ALPEK	February 14, 2018	BUY	MXN$31.80

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