

IENOVA

Quarterly Report

October 28, 2019

Marine gas pipeline begins operations

- **Ienova's results fell slightly short of estimates at the EBITDA level. Sales decreased 13.0% yoy to USD 355 million, but Adjusted EBITDA decreased by only 3.0% yoy to USD 231 million**
- **Despite revenue deferment at the Guaymas-El Oro gas pipeline and the Ecogas Mexicali tariff adjustment in 2018, the Texas-Tuxpan marine gas pipeline made a very favorable contribution**
- **3Q19 results were expected to be neutral, but the outlook remains very bright given the contribution of the marine gas pipeline and the 2020 start-up of the storage terminal operations**

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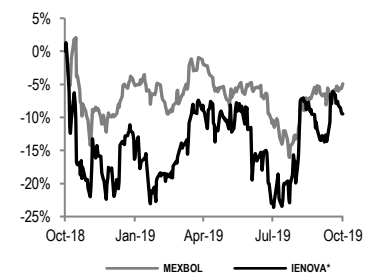
BUY

Current Price	MXN\$82.29
PT2019	MXN\$92.80
Dividend 2019	MXN\$ 3.00
Dividend (%)	4.3%
Upside Potential	16.5%
Max – Min LTM	92.81-64.61
Market Cap (USD\$m)	6,606.4
Shares outstanding (m)	1,534
Float	33.0%
Daily Turnover (MXN\$m)	205.8
Valuation Metrics LTM *	
FV/EBITDA Adj	11.1x
P/E	16.0x

Favorable contribution from the Texas-Tuxpan marine gas pipeline.

3Q19 results were in line with our estimates in terms of sales, which decreased 13.0% yoy to USD 355 million impacted by lower prices and natural gas volumes, the unfavorable effect of maximum high energy prices in 2018 at the Mexicali Thermoelectric power plant due to market conditions, and revenue deferment at the Guaymas-El Oro gas pipeline. This situation was partially offset by the start-up of the Pima and Rumorosa solar energy generation facilities. Even so, Adjusted EBITDA decreased by only 3.0% to USD 231 million (slightly below our estimate) thanks to the favorable contribution of the Texas- Tuxpan marine gas pipeline that began operating in mid September. This resulted in the EBITDA margin improving 6.7pp to 65.1%. The company reported a USD 111 million net profit, or stable yoy. The net debt to EBITDA ratio rose to 3.7x vs 3.5x in 2Q19. Thus, the FV/EBITDA multiple remains at 11.1x. We will shortly be releasing our 2020 outlook, but reiterate our BUY rating on the stock.

Relative performance to MEXBOL (LTM)



Financial statements

	2017	2018	2019E	2020E
Revenues	1,167	1,369	1,435	1,745
Operating Income	563	536	644	703
Adjusted EBITDA	759	876	911	1,287
EBITDA Margin	65.0%	64.0%	63.5%	73.7%
Net Income	354	431	373	470
Net margin	30.4%	31.5%	26.0%	26.9%
Total Assets	8,164	8,769	9,233	9,894
Cash	38	52	145	272
Total Liabilities	3,647	4,015	4,302	4,672
Debt	2,790	3,092	3,356	3,756
Common Equity	4,517	4,740	4,931	5,222

Source: Banorte

Valuation and financial metrics

	2017	2018	2019E	2020E
FV/EBITDA	12.3x	11.0x	10.2x	7.5x
P/E	18.7x	15.6x	16.3x	14.6x
P/BV	1.5x	1.4x	1.3x	1.3x
ROE	7.8%	9.1%	7.6%	9.0%
ROA	4.3%	4.9%	4.0%	4.7%
EBITDA/ Interest expen	34.5x	9.1x	11.4x	9.4x
Net Debt/EBITDA	3.6x	3.5x	3.5x	2.7x
Debt/Equity	0.6x	0.7x	0.7x	0.7x

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IENOVA –3Q19 Results

USD, Million

Concept	3Q18	3Q19	Var %	3Q19e	Diff % vs Estim.
Revenue	408	355	-13.0%	368	-3.5%
Operating Income	173	156	-9.8%	165	-5.2%
Ebitda	238	231	-3.0%	248	-6.9%
Net Income	112	111	-0.9%	94	18.2%
Margins					
Operating Margin	42.5%	44.1%	1.6pp	44.8%	-0.8pp
Ebitda Margin	58.4%	65.1%	6.7pp	67.4%	-2.3pp
Net Margin	27.5%	35.5%	8.1pp	25.5%	10.0pp
EPS	\$0.07	\$0.07	-0.9%	\$0.06	18.2%

Income Statement (Million)

Year	2018	2019	2019	Var%	Var%
Quarter	3	2	3	% YoY	% QoQ
Net Revenue	408.0	316.7	355.1	-13.0%	12.1%
Cost of goods sold	135.6	68.7	100.2	-26.1%	45.7%
Gross profit	272.5	247.9	254.9	-6.4%	2.8%
General expenses	99.1	89.1	98.5	-0.6%	10.5%
Operating Income	173.4	158.8	156.5	-9.8%	-1.5%
Operating Margin	42.5%	50.1%	44.1%	1.6pp	(6.1pp)
Depreciation	35.1	38.8	39.2	11.7%	1.0%
EBITDA	238.2	224.6	231.0	-3.0%	2.8%
EBITDA Margin	58.4%	70.9%	65.1%	6.7pp	(5.9pp)
Interest income (expense) net	10.1	(19.3)	(39.7)	N.A.	105.8%
Interest expense	32.3	33.0	33.0	2.4%	0.2%
Interest income	7.0	7.8	9.8	38.6%	25.8%
Exchange Income (loss)	(0.1)	(0.1)	(0.1)	1.4%	
Unconsolidated subsidiaries	35.4	6.0	(16.3)	N.A.	N.A.
Unconsolidated subsidiaries	(14.2)	5.2	27.0	N.A.	415.7%
Net Income before taxes	169.2	144.7	143.8	-15.0%	-0.7%
Provision for Income taxes	57.1	32.2	33.0	-42.2%	2.5%
Discontinued Operations					
Consolidated Net Income	112.1	112.6	110.8	-1.2%	-1.6%
Minorities	0.0	(0.0)	(0.3)	N.A.	>500%
Net Income	112.1	112.6	111.1	-0.9%	-1.3%
Net Margin	27.5%	35.5%	31.3%	3.8pp	(4.3pp)
EPS	0.073	0.073	0.072	-0.9%	-1.3%

Balance Sheet (million)

Total Current Assets	500.1	502.9	503.7	0.7%	0.2%
Cash & Short Term Investments	45.9	100.9	62.5	36.1%	-38.1%
Long Term Assets	8,217.2	8,685.2	8,833.0	7.5%	1.7%
Property, Plant & Equipment (Net)	4,052.6	4,329.2	4,446.5	9.7%	2.7%
Intangible Assets (Net)	193.2	185.8	183.3	-5.1%	-1.3%
Total Assets	8,717.3	9,188.1	9,336.7	7.1%	1.6%
Current Liabilities	1,457.2	1,588.3	1,627.7	11.7%	2.5%
Short Term Debt	1,141.7	1,294.9	1,354.9	18.7%	4.6%
Accounts Payable	176.2	199.3	179.0	1.6%	-10.2%
Long Term Liabilities	2,560.6	2,671.8	2,689.2	5.0%	0.7%
Long Term Debt	1,903.0	1,988.9	1,982.3	4.2%	-0.3%
Total Liabilities	4,017.8	4,260.1	4,316.9	7.4%	1.3%
Common Stock	4,699.5	4,928.0	5,019.8	6.8%	1.9%
Minorities	13.1	13.3	13.0	-0.9%	-2.3%
Total Equity	4,686.4	4,914.7	5,006.8	6.8%	1.9%
Liabilities & Equity	8,717.3	9,188.1	9,336.7	7.1%	1.6%
Net Debt	2,998.7	3,182.9	3,274.8	9.2%	2.9%

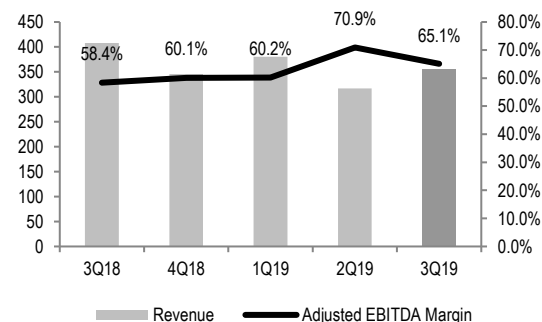
Cash Flow

Cash Flow from Operating Activities	505.1	424.1	586.5
Cash Flow from Investing Activities	(454.9)	(269.0)	(454.8)
Cash Flow from Financing Activities	(10.3)	3.6	18.2
Increase (decrease) in cash	(4.4)	84.2	54.6

Source: Banorte, MSE

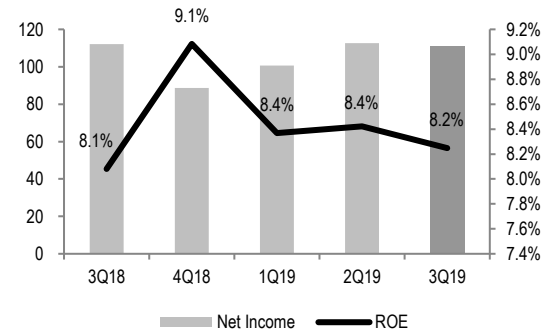
Revenue & EBITDA Margin

USD, million



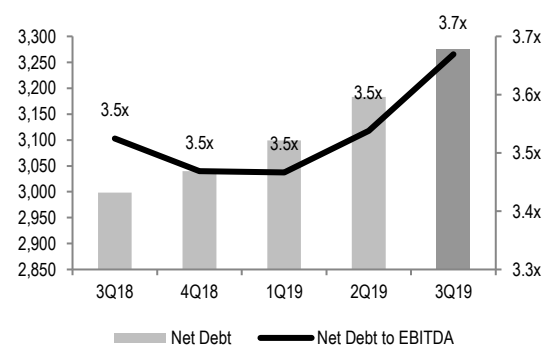
Net Income & ROE

USD, million



Net Debt & Net Debt to EBITDA

USD, million



Operating Information per Business Segment

USD, Million

	Revenue			ADJUSTED EBITDA			ADJUSTED EBITDA MARGIN		
	3Q18	3Q19	Var	3Q18	3Q19	Var	3Q18	3Q19	Var
Gas	306.4	264.0	-13.8%	169.0	149.2	-11.7%	55.2%	56.5%	1.4%
Electricity	101.1	90.6	-10.4%	48.3	47.5	-1.7%	47.8%	52.4%	4.7%
Corporate	0.5	0.5	0.0%	-3.8	-0.6	NA			
TOTAL	408.0	355.1	-13.0%	213.5	196.1	-8.1%	52.3%	55.2%	2.9%
Adjusted JV's				24.7	35.1	42.1%			
ADJUSTED TOTAL				238.2	231.2	-3.0%			

Source: Ienova

Gas segment. This division's revenues dropped 13.8% yoy to USD 264.0 million owing to a 28.5% yoy drop in the average price of natural gas from US\$ 3.86 MMBtu in 3Q18 to US\$2.76 MMBtu in 3Q19, lower sales volumes, revenue deferment at the Guaymas-El Oro gas pipeline and the 2018 non-recurring adjustment of distribution tariffs at Ecogas Mexicali corresponding to the previous year. Nevertheless, the decrease in EBITDA was less than the decrease in revenues, or 11.7% yoy to USD 149.2 million, resulting in a yoy increase of 1.4 pp in the margin at 56.5%.

It should be recalled that in August, Ienova signed a Contract Suspension Agreement with CFE pertaining to the transportation service contracts of the Guaymas – El Oro pipeline as part of necessary steps to resume operation of the pipeline and avoid termination of the contract. In September, Ienova signed an agreement with CFE to establish the new tariff structure and extend the term of the contracts by 10 more years, although the Guaymas - El Oro contract extends the suspension term until January 15, 2020.

Electricity Segment. Revenues decreased 10.4% yoy to USD 90.6 million, but EBITDA decreased only marginally by 1.7% to USD 47.5 million, resulting in a 4.7 pp increase in the margin to 52.4%. This can be attributed to maximum high energy prices at the Mexicali Thermoelectric power station in 3Q18 owing to market conditions, partially offset by the operations of the Pima and Rumorosa solar energy facilities.

JV adjustment. The third quarter saw the formal start-up of the Texas-Tuxpan marine gas pipeline operations under the new CFE tariff scheme which lasts 35 years. Despite less than 15 days of operations, the pipeline contribution was around US\$ 10 million (above our US\$ 8 million forecast) and so combined business EBITDA rose 42.1% yoy. We therefore believe that this project could make an annual contribution of more than US\$ 200 million, adding slightly more than 20% to estimated 2019 EBITDA and underpinning very good 2020 prospects.

Stable net profit yoy. The company reported net profit of US\$ 111 million, which is a marginal decrease of just 0.9% yoy, topping our estimate, and was due to a less adverse than expected forex effect.

Slight increase in Net Debt to Ebitda. Regarding the company's financial situation, net debt to EBITDA was 3.7x in 3Q19, slightly above the prior quarter's 3.5x. Net debt closed the quarter at US\$ 3.3 billion, 2.9% above 2Q19.

Project pipeline on track. Back in September, Ienova entered into two electricity supply agreements with *Circle K y Liverpool* with a 15-year term, which is on top of the agreement signed with *Liverpool* announced in February, 2018. Furthermore, in October, the company signed a long-term electricity supply contract with *Envases Universales*. The energy involved in these contracts will be generated by the *Border Solar* facility located in the municipality of Juárez, Chihuahua, which will come on line in 2H20. The project will have a 150MW installed capacity and a US\$ 160 million investment. The storage terminal projects in Veracruz, Puebla and Mexico City are scheduled to come on stream at the beginning of 2020.

We will publish our 2020 estimates in the coming weeks. Our rating is BUY. In our view, 3Q19 results should be neutral for the share price. However, prospects for the company are favorable and include a large contribution from the Texas-Tuxpan marine gas pipeline and beginning of the storage terminal operations in 2020. We are currently revising our 2020 estimates and will shortly publish our outlook. For now we have a BUY rating on the stock.

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, 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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	Reference
BUY	<i>When the share expected performance is greater than the MEXBOL estimated performance.</i>
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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Historical PT and Rating

Stock	Date	Rating	PT
IENOVA *	January 16, 2019	BUY	MXN\$92.80
IENOVA *	October 25, 2017	BUY	MXN\$118.00
IENOVA *	July 26, 2017	HOLD	MXN\$99.00
IENOVA *	October 27, 2016	BUY	MXN\$99.00

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