Zacks Small-Cap Research

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Grupo Tmm Sab (GTMAY-OTC)

GTMAY: *Energy Reform – Long-Term Positive, Despite Short-Term Uncertainty*

OUTLOOK

Grupo TMM, one of Mexico's largest maritime transportation companies, is positioning itself to benefit from anticipated growth from energy reform legislation that Mexico's president signed on August 11, 2014. While in the near-term, the steep decline in oil prices could delay some of the anticipated growth, we remain optimistic about the long-term opportunity for TMM to benefit from the opening of Mexico's energy sector.

Current Recommendation	**Neutral**
Prior Recommendation	Outperform
Date of Last Change	04/07/2013
Current Price (2/25/15)	$1.30
Target Price	**$2.50**

SUMMARY DATA

52-Week High	**$2.91**
52-Week Low	**$0.82**
One-Year Return (%)	**38**
Beta	**NA**
Average Daily Volume (sh)	**2,841**
ADRs at 5:1 ord. shares (mil)	**20**
Market Capitalization ($mil)	**$26**
Short Interest Ratio (days)	**15.2**
Institutional Ownership (%)	**2**
Insider Ownership (%)	**36**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-6.5**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2014 Estimate	**N/A**
P/E using 2015 Estimate	**N/A**

Risk Level	**Average**
Type of Stock	**Small-Value**
Industry	**Maritime**

ZACKS ESTIMATES

Revenue
(in millions of $US)

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2012	63 A	49 A	54 A	50 A	215 A
2013	51 A	55 A	57 A	57 A	219 A
2014	53 A	49 A	54 A	57 E	213 E
2015					235 E

Earnings per ADR
($US EPS is operating earnings before non recurring items)

	Q1 (Sep)	Q2 (Dec)	Q3 (Mar)	Q4 (Jun)	Year (Jun)
2012	-$0.53 A	$0.82 A	-$0.38 A	-$1.25 A	-$2.97 A
2013	-$0.64 A	-$0.89 A	-$0.28 A	-$0.34 A	-$2.15 A
2014	-$0.43 A	-$0.12 A	$0.06 A	-$0.07 E	-$0.56 E
2015					-$0.15 E

Metrics Pro Forma; Quarters might not sum reflecting exchange rates

Zacks Projected EPS Growth Rate - Next 5 Years % **N/A**

Disclosures begins on page 7

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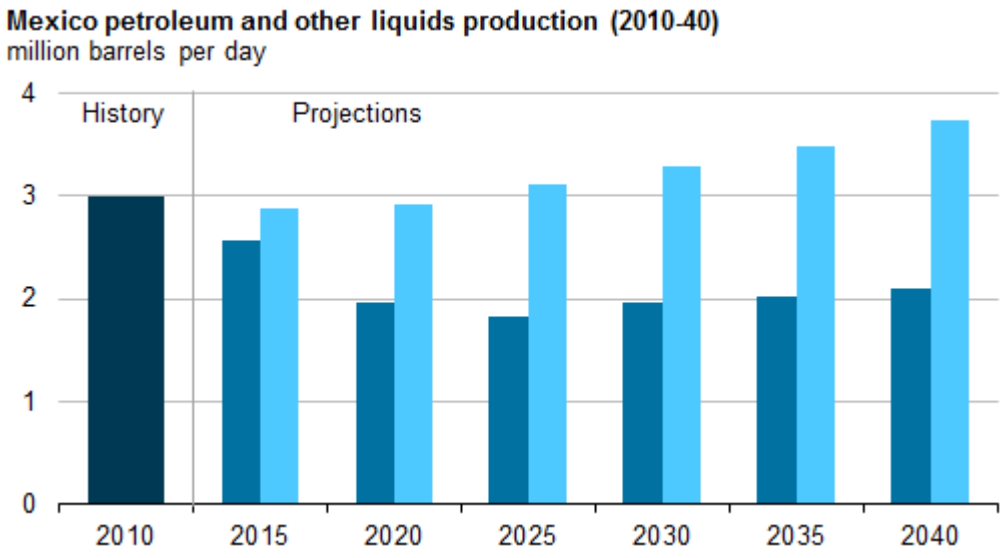
KEY POINTS

- We remain optimistic about the long-term opportunity for Grupo TMM (GTMAY-OTC) to benefit from Mexico's energy reforms.
- In the near-term, however, the steep decline in oil prices could delay some of the advances that the reforms are expected to fuel, in our opinion.
- Low oil prices have already led the government to reduce 2015 spending plans. Moreover, largely mirroring the steep decline in oil prices and potential decline in oil production, Mexico has reduced its economic growth forecast for 2015.
- On the other hand, TMM could benefit from recent and expected strength in the automobile sector.

ENERGY REFORM

On August 11, 2014, Mexico's President Enrique Peña Nieto signed energy reform legislation that is intended to open Mexico's oil and natural gas markets to foreign direct investment. A year earlier, Mexico had initiated reforms to allow international companies to explore energy opportunities. The legislative reforms are intended to open the Mexican energy sector to national and international competition. According to Pemex (Petróleos Mexicanos), energy reforms will alter how international companies participate in Mexico's energy sector and, in turn, boost oil production.

Industry insiders expect that the impact of these reforms could increase Mexico's oil production to as much as 3.0 million barrels per day by 2018 and 3.5 million to 4.0 million barrels per day by 2025. As a result of these legislative reforms, the U.S. Energy Information Administration (EIA) increased its preliminary projections for Mexico's oil production (see below). By increasing oil and natural gas production, the reforms are also expected to boost the availability of more affordable energy for the Mexican population.



Source: EIA *International Energy Outlook 2014*

Pemex's goal is to attract international companies interested in Mexico's untapped reserves. Mexico has the biggest unexplored crude area after the Arctic Circle and many within the industry believe Mexico's

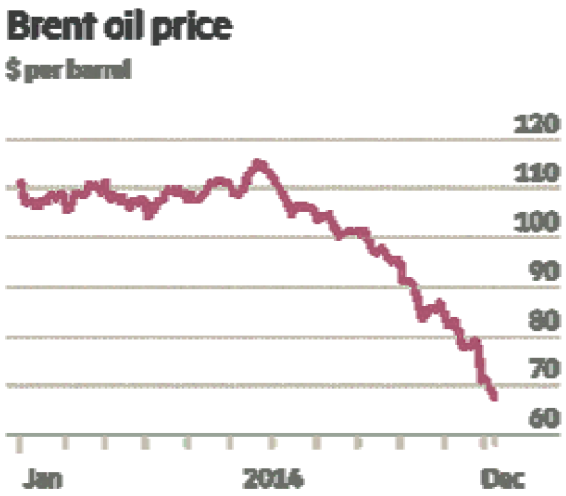
reserves are more accessible than reserves in other parts of the world. Energy reform is expected to increase foreign direct investment in Mexico by as much as $15 billion to $20 billion annually.

Mexico's deep-water prospects in the Gulf of Mexico are expected to be attractive to major oil companies. Major companies such as Noble Energy (NBL-not rated) and others have already indicated an increased interest in deep-water exploitation in the Gulf of Mexico. Reserves are estimated to be 60 billion to 120 billion barrels in the deep-water of the Gulf of Mexico. However, Pemex lacks the technical expertise to drill in deep waters and seeks foreign partners to lend their technical expertise. As a result, TMM expects demand for exploration and distribution services within Mexico to grow and believes that it, as one of the leading companies in Mexico, is well-positioned to benefit from this anticipated growth. For this reason, TMM intends to upgrade its fleet with higher-rated vessels and deeper-water capabilities.

LONG-TERM POSITIVE

We remain optimistic about the long-term opportunity for Grupo TMM (GTMAY-OTC) to benefit from Mexico's energy reforms. In the near-term, however, the steep decline in oil prices could delay some of the advances that the reforms are expected to fuel, in our opinion. The Mexican government has indicated plans to auction 169 oil and gas blocks for exploration and exploitation. Per the original schedule, the first contracts were slated to be awarded by July 2015. Mexico's Energy Secretariat expects to raise over $50 billion from the 169 blocks.

However, we believe the steep decline in global oil prices has created uncertainty about the schedule and about how much investment Mexico will attract near-term. Specifically, oil prices are at a six year low. After reaching $115 a barrel in 2014 (see figure below), oil prices dropped to roughly $44 / barrel last month, which represents the lowest level since April 2009. This has led the Mexican government to lower its 2015 budget by nearly 3%. Oil revenue contributes roughly 33% of the government's budget.



Source: Thomson Reuters

According to the National Hydrocarbons Commission, major energy companies such as Exxon Mobil (XOM-not rated), Chevron (CVX-not rated), BP (BP-not rated) and Shell (RDS-A-not rated) have indicated their interest in bidding on the Mexican blocks. However, industry insiders expect that the first bids for exploration contracts will be lower than originally expected and that some exploration projects are likely to be delayed. In fact, Mexico's Finance Secretary announced last month that Mexico would delay bidding for some fields that are expected to be particularly sensitive to oil price declines.

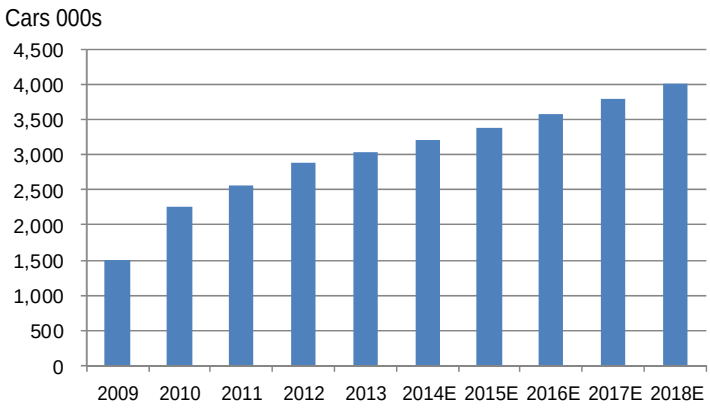
Low oil prices have already led the government to reduce its 2015 spending forecast. Revenue from oil makes up roughly 33% of the government budget. The government reduced some $8.4 billion, or roughly

3%, from its 2015 budget. Moreover, largely mirroring the steep decline in oil prices and potential decline in oil production, Mexico has reduced its economic growth forecast for 2015. The Bank of Mexico's revised estimate is that GDP growth will be 2.5% to 3.5% in 2015, which is lower than its original 3%-4% forecast.

AUTOMOTIVE SECTOR

On the other hand, TMM could benefit from recent and expected strength in the automobile sector, depending on export destination markets and mode of transport. Mexico is the 8th largest automobile producer globally, with the majority of exports going to the U.S. The Mexican Automobile Industry Association (AMIA) expects Mexican automobile production to increase by roughly 6% in 2015 and automobile exports to grow, as well. In December 2014, auto exports increased 21% year-over-year to 195,091, according to Bloomberg.

Mexican Auto Production, 2009-2018E



Source: Mexican Association of Automotive Industry (AMIA)

However, despite increased car shipments to the U.S., vehicle exports to South America and Asia were down in 2014 compared to 2013. This was a significant factor that led to lower revenue for TMM in its Ports and Terminals segment in the first nine months of 2014 compared to the same period of 2013. While many Mexican produced automobiles are transported by train, maritime transportation is also used, depending on export destination market.

RISKS

- Mexico's oil reforms might not have the impact that Pemex and the government expect and might be delayed, reflecting lower oil prices.
- The company's initiatives could take longer than expected to produce operating efficiencies.
- Despite medium and long-term contracts in place at the Maritime division, tariff volatility could impact operations.
- The global downturn in the product tanker business could impact Maritime's revenue and profit.

- The balance sheet remains highly leveraged.
- TMM's new projects could take longer than expected to complete.
- Given that roughly 94% of TMM's debt is peso denominated and that the company must supplement its peso generated revenue with dollar revenues to service its debt, TMM faces currency exchange risk.

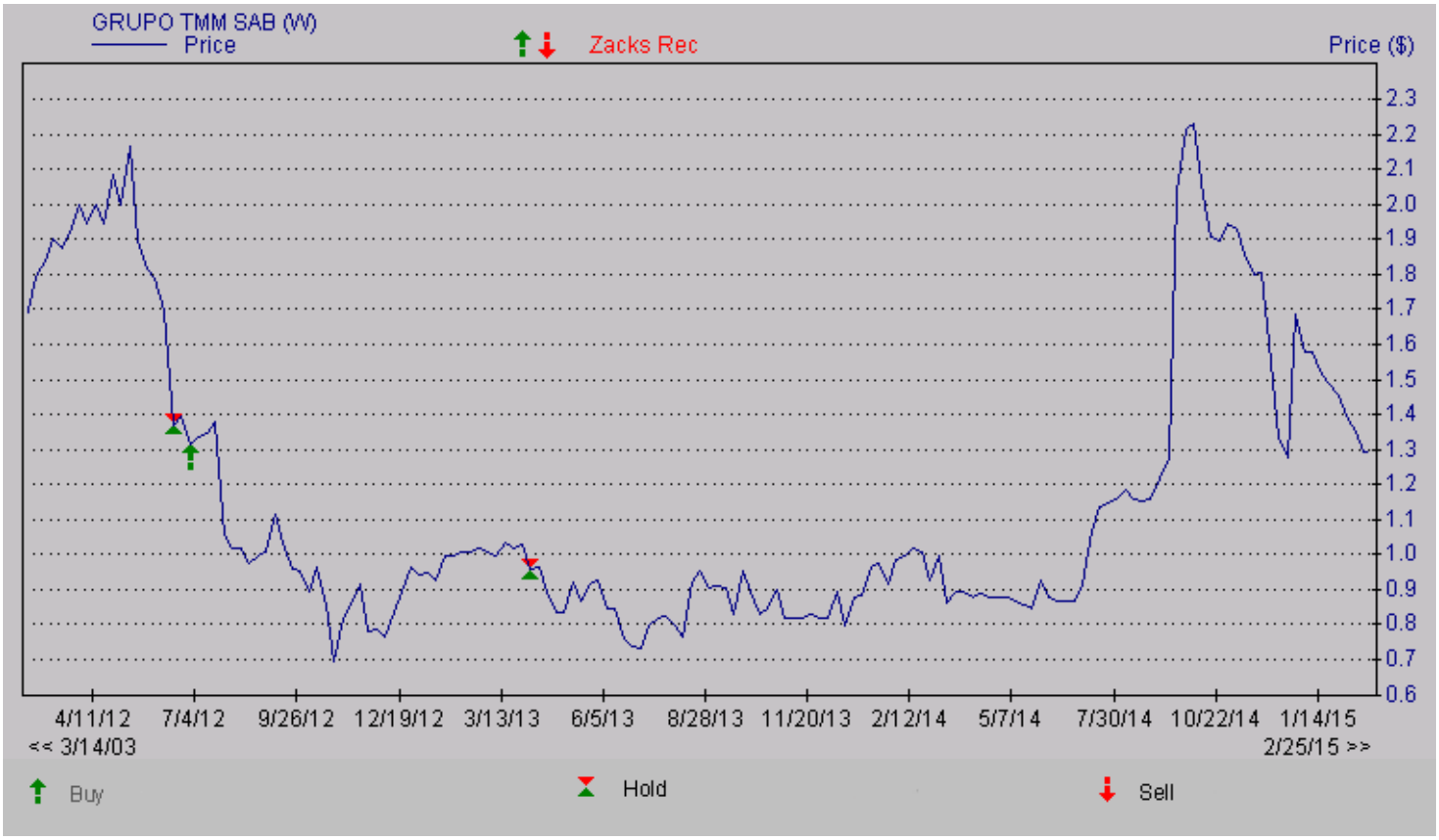
PROJECTED INCOME STATEMENT

Grupo TMM Quarterly Income Statements & Projections ($ Mexican Pesos millions)

	1Q13	2Q13	3Q13	4Q13	2013	1Q14	2Q14A	3Q14A	4Q14E	2014E	2015E
Ports & Terminals	97.7	92.2	76.6	66.2	332.7	74.3	77.7	58.5	49.7	260.2	262.8
Maritime	554.5	611.6	649.2	639.9	2,455.3	603.4	570.7	660.4	671.9	2,506.4	2,541.5
Corporate & others	12.6	12.6	12.7	12.7	50.6	12.7	17.3	18.5	12.8	61.3	61.9
Rev from freight & svcs	**P$664.8**	**P$716.4**	**P$738.5**	**P$718.8**	**P$2,838.6**	**P$690.4**	**P$665.7**	**P$737.4**	**P$734.3**	**P$2,827.8**	**P$2,866.1**
Ports & Terminals	(81.0)	(80.4)	(65.4)	(50.5)	(277.2)	(60.2)	(58.4)	(54.6)	(39.7)	(212.9)	(215.0)
Maritime	(297.2)	(334.8)	(360.1)	(381.7)	(1,373.8)	(321.3)	(315.1)	(389.3)	(356.1)	(1,381.8)	(1,395.6)
Corporate & others	(12.3)	(12.6)	(13.5)	(12.0)	(50.4)	(13.0)	(17.2)	(18.8)	(12.8)	(61.8)	(62.4)
Cost of freight & services	**(390.5)**	**(427.8)**	**(439.0)**	**(444.2)**	**(1,701.4)**	**(394.5)**	**(390.7)**	**(462.7)**	**(408.7)**	**(1,656.6)**	**(1,673.1)**
Ports & Terminals	(3.7)	(3.7)	(3.7)	(3.6)	(14.6)	(3.5)	(3.7)	(3.7)	(2.5)	(13.4)	(13.1)
Maritime	(142.2)	(139.8)	(140.6)	(139.7)	(562.3)	(142.6)	(144.5)	(149.8)	(161.3)	(598.2)	(610.0)
Corporate & others	(2.4)	(2.1)	(2.1)	(2.1)	(8.7)	(1.9)	(1.9)	(1.8)	(1.9)	(7.5)	(6.2)
Depreciation & amortization	(148.3)	(145.6)	(146.4)	(145.4)	(585.6)	(148.0)	(150.1)	(155.3)	(165.7)	(619.1)	(629.3)
Corporate expenses	(64.9)	(39.6)	(57.0)	(48.6)	(210.1)	(50.0)	(59.2)	(51.7)	(47.0)	(207.9)	(208.9)
EBIT											
Ports & Terminals	13.0	8.1	7.5	12.1	40.9	10.6	15.6	0.2	7.4	33.8	34.6
Maritime	115.1	137.0	148.5	118.5	519.2	139.5	111.1	121.3	154.5	526.4	535.9
Corporate & others	(2.1)	(2.1)	(2.9)	(1.4)	(8.5)	(2.2)	(1.8)	(2.1)	(2.0)	(8.1)	(6.8)
Other (expenses) income	10.5	(3.7)	25.6	31.6	64.0	23.9	(1.1)	254.0	26.9	303.7	300.0
Operating Income	**P$71.6**	**P$99.7**	**P$121.7**	**P$112.2**	**P$405.5**	**P$121.8**	**P$64.6**	**P$321.7**	**P$139.9**	**P$648.0**	**P$654.8**
EBITDA	**P$219.9**	**P$245.3**	**P$268.1**	**P$257.6**	**P$991.1**	**P$269.8**	**P$214.7**	**P$240.0**	**P$305.6**	**P$1,267.1**	**P$1,284.1**
Financial (expenses) income	(230.2)	(230.6)	(227.5)	(216.6)	(904.9)	(216.4)	(213.3)	(204.1)	(216.4)	(850.2)	(810.0)
Exchange gain (loss)	25.2	(30.6)	6.9	2.8	4.4	(3.1)	0.6	(22.7)	(3.1)	(28.3)	(12.0)
Net financial cost	(205.0)	(261.2)	(220.6)	(213.8)	(900.5)	(219.5)	(212.7)	(226.8)	(219.5)	(878.5)	(822.0)
Loss before taxes	**(133.4)**	**(161.5)**	**(98.9)**	**(101.6)**	**(495.0)**	**(97.7)**	**(148.1)**	**94.9**	**(79.6)**	**(230.5)**	**(167.2)**
Provision for taxes	(7.1)	(29.2)	32.4	(0.8)	(4.7)	(2.2)	(3.8)	(2.7)	(0.2)	(8.9)	(5.0)
Net Loss before discontinuing	**(140.5)**	**(190.7)**	**(66.5)**	**(102.4)**	**(499.7)**	**(100.0)**	**(151.9)**	**92.2**	**(79.9)**	**(239.6)**	**(172.3)**
Loss from discontinuing operatic	(25.3)	(44.4)	(8.2)	14.3	(63.5)	(14.7)	(12.0)	(12.8)	(12.7)	(52.2)	(50.0)
Net Loss for the period	**(165.8)**	**(235.1)**	**(74.7)**	**(88.1)**	**(563.2)**	**(114.7)**	**(163.9)**	**79.4**	**(92.6)**	**(291.8)**	**(222.3)**
Attributable to:											
Minority interest	2.4	0.4	0.2	2.0	5.0	(1.5)	0.8	(1.0)	0.5	(1.2)	(4.0)
GTMM Equity holders	**(168.2)**	**(235.5)**	**(74.9)**	**(90.1)**	**(568.2)**	**(113.2)**	**(164.7)**	**80.4**	**(93.1)**	**(290.6)**	**(218.3)**
LPS	**(P$1.65)**	**(P$2.30)**	**(P$0.73)**	**(P$0.88)**	**(P$5.56)**	**(P$1.11)**	**(P$1.61)**	**P$0.79**	**(P$0.89)**	**(P$2.83)**	**(P$2.10)**
Avg shares out (millions)	102.2	102.2	102.2	102.2	102.2	102.2	102.2	102.2	104.2	102.7	104.2

Source: Company reports, Zacks estimates

HISTORICAL ZACKS RECOMMENDATIONS



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