Zacks Small-Cap Research

March 5, 2012
Ken Nagy, CFA

www.zacks.com
111 North Canal Street, Chicago, IL 60606

GRUPO TMM (TMM-NYSE)

TMM: New Opportunities and Utilization Well Above Average - OUTPERFORM

Current Recommendation	**Outperform**
Prior Recommendation	N/A
Date of Last Change	05/16/2010
Current Price (03/02/12)	$1.84
Target Price	**$4.50**

OUTLOOK

Grupo TMM is one of the largest integrated logistics and transportation companies in Mexico. The firm, through its subsidiaries provides maritime services, land transportation services, integrated logistics services, and ports and terminals management to international and domestic clients throughout Mexico. As part of its five-year growth strategy, the firm is committed to modernizing its fleet and increasing its penetration in Mexican Ports, which will in turn maximize margins. TMM's offshore and product tanker fleet generally work with long and medium-term contracts which has the effect of predictable cash flows.

SUMMARY DATA

52-Week High	**$2.96**
52-Week Low	**$1.32**
One-Year Return (%)	**-35.27**
Beta	**0.07**
Average Daily Volume (sh)	**5,631**
Shares Outstanding (mil)	**102**
Market Capitalization ($mil)	**$36**
Short Interest Ratio (days)	**8.85**
Institutional Ownership (%)	**9**
Insider Ownership (%)	**36**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-11.2**
EBITDA (%)	**57.0**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2011 Estimate	**N/A**
Zacks Rank	**3**

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

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2010	81 A	75 A	75 A	74 A	305 A
2011	66 A	70 A	69 A	65 A	269 A
2012	65 E	66 E	66 E	68 E	265 E

Earnings per Share

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2010	-$0.41 A	$0.14 A	-$0.27 A	-$0.26 A	-$0.79 A
2011	-$0.42 A	-$0.30 A	$0.90 A	-$0.04 A	$0.15 A
2012	-$0.64 E	$0.10 E	$0.15 E	$0.45 E	$0.06 E

*EPS is impacted by currency exchange rate changes between USD/ MXN

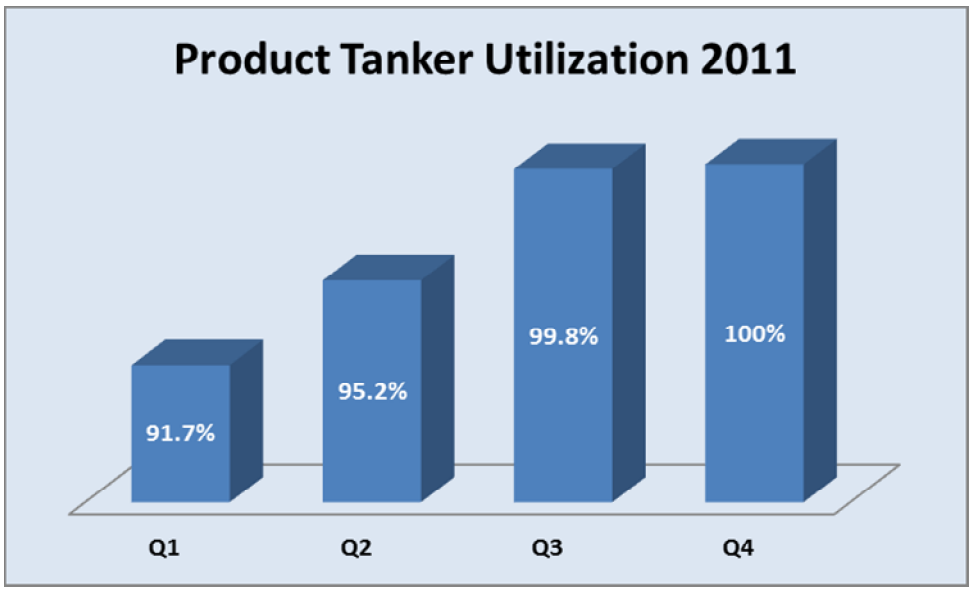
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WHATS NEW

Grupo TMM sees High Utilization and New Opportunities

On February 27, 2012, Grupo TMM reported financial results for its fourth quarter and fiscal year, ended December 31, 2011.

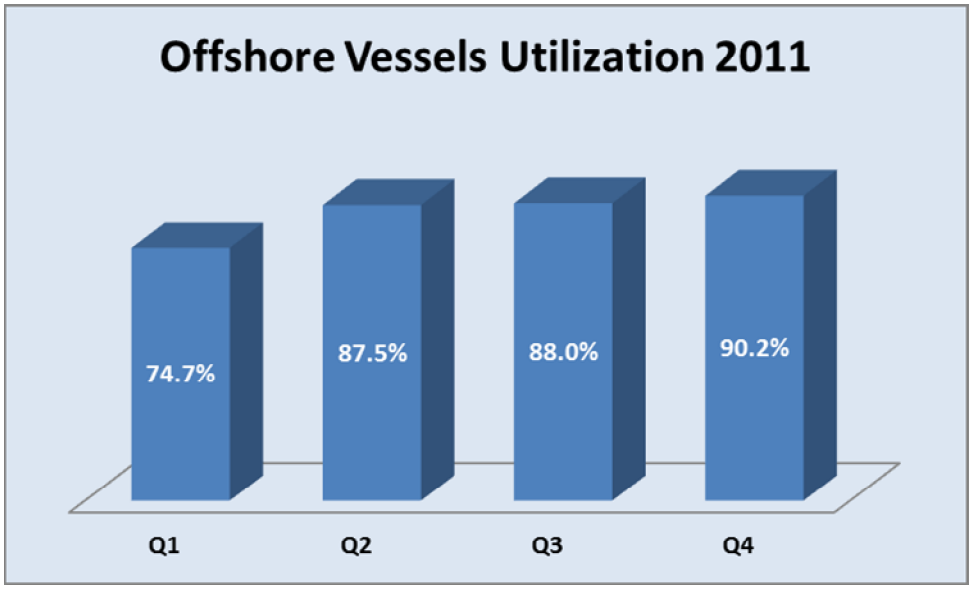
While the Company reported mixed results for the quarter due to continued challenging global economic conditions, we feel that if investors look beyond the surface they will like what they find. Grupo TMM continued to see higher than industry average utilization rates as well as recently acquiring a shipyard in the Gulf of Mexico.



In the 2011 full year, the Maritime segment revenue dropped 14.4% to $171.7 million compared to the 2010 full year due mainly to lower average daily tariffs and 17 vessels in dry dock. Maritime's EBITDA for the 2011 full year was $81.6 million compared to $100.4 million in the comparable 2010 period. However, EBITDA margin remained similar at 47.5 percent in 2011 versus 50 percent in 2010. Looking back investors can see the strength that 2011 was compared to. 2010 EBITDA and EBITDA margin were the highest in the last five years, despite a global recessionary economic climate. Grupo exited 2010 having grown its EBITDA for five consecutive years. EBITDA grew at a lofty 182% or a compounded yearly growth rate (CYGR) of 29.6%.

The segment's fleet utilization continued its sequential improvement in 2011. In the fourth quarter offshore fleet utilization was 90.2% and product tanker utilization was 100%. Offshore fleet and product tanker utilization continued to stay well above the industry average.

The Logistics segment revenue dropped $9.6 million or 12% to $70.6 million during fiscal 2011 compared to the previous year while revenues from the Ports and Terminals improved $2.3 million or 9.3% year over year to $26.9 million. At Logistics, the auto hauling segment improved year over year, with revenue increasing 21.3% and gross profit improving from a $0.4 million loss to a $0.6 million profit. Additionally, at Ports and Terminals, auto handling volumes at Puebla, Saltillo and Acapulco increased by 26% year over year.



The Company also made progress on reducing its net debt by $26.9 million in 2011 and ended the year with $3.6 million of cash flow. Additionally, the book value of its Trust Certificates debt was reduced $93.9 million from December 31, 2010, due to the depreciation of the peso versus the dollar in the 2011 full year. Finally, in the full year 2011, TMM prepaid principal and interests for a total amount of $121 million.

New Opportunities

Acquisition of Shipyard. In January 2012, Grupo TMM acquired a shipyard at the Port of Tampico which is strategically positioned in the Gulf of Mexico and currently working at full capacity. The Company anticipates generating approximately 32 percent of EBITDA margin from operations during its first year of the acquisition.

Similarly, Grupo TMM expects to provide service to more than 30 vessels per year. Approximately 37 percent of these serviced vessels are anticipated to be from TMM's own fleet which will result in reduced costs from increased efficiency in the maintenance, repair and positioning its vessels.

In the shorter term, the Company expects to have the necessary capabilities to build vessels at the Port of Tampico facility and added that the timing of this acquisition was in line with PEMEX's intention to add 32 offshore vessels to its fleet, of which 21 are required to be Mexican built vessels, supporting national integration. The Company anticipates PEMEX to announce bids for these 21 vessels in April, for 10-year time charter contracts, including 2 years to build the vessels.

Additionally, the Company announced that during the fiscal 2012 first quarter, it renewed two offshore contracts for a three-year period each and that it currently has a backlog of $192 million.

Grupo TMM also reported that it continues to work with selected, interested parties for the financial implementation of the development of a container and liquids terminal at the Port of Tuxpan and has made significant progress on a joint venture, expected to be announced soon. Additionally, Grupo TMM continues to work on the addition of specialized offshore vessels to its fleet.

A Closer Look at the TMM's Growth Plan.
The firm's five-year growth plan includes two projects. The first project consists of the development of a container and liquids terminal at the Port of Tuxpan, Veracruz. The container terminal will meet increasing demand for capacity in the Gulf of Mexico, taking advantage of organic growth in the Mexican market. The liquids terminal will address current and projected increased demand for imported gasoline and diesel fuel through the construction of a pipeline and a berthing position. Investors should be aware that the development of the facility could take up to two years. Along the same lines, the addition of specialized offshore vessels to TMM's fleet is anticipated to benefit the Company in meeting increased demand for deep water transportation.

INVESTMENT THESIS

- The firm's Maritime division is the dominant business at TMM. The fleet was renewed throughout 2008 and 2009, adding 10 offshore vessels and 3 tankers to its fleet. TMM is committed to continue to modernize its fleet as part of its five-year growth plan, which will in turn maximize margins.

- TMM prefers to compete for margin rich niche business and employs long to medium-term contracts.

- TMM is committed to taking advantage of strategic opportunities to add new vessels to its fleet and increase its penetration in Mexican ports. This should make the firm more efficient and more profitable in the long run.



- Despite revenue loss at Maritime, the division's EBITDA margin remained similar at 47.5 percent in 2011 versus 50 percent in 2010.

- The outlook for deep water drilling as well as the Mexican and American GDP looks promising.

Maritime Operations. (64% of Total Revenue)
The Maritime Operations division provides maritime transportation services, including offshore vessels that provide transportation and other services to the Mexican offshore oil industry, tankers that transport petroleum products within Mexican waters, parcel tankers that transport liquid chemical and vegetable oil cargos from and to the United States and Mexico, and tugboats that provide towing services at the port of Manzanillo, Mexico. The firm provides these services through its fleet of 41 vessels, which includes product tankers, a variety of offshore supply vessels, harbor tugs and chemical tankers.

Offshore Vessels
The offshore vessels unit has a fleet of 28 vessels mainly for transport of dry and liquid cargo, anchor handling tug vessels, crew boats, fire fighting vessels, four point mooring vessels and dynamic positioning vessels.





Product Tankers

This segment provides product tanker chartering services to PEMEX for the transportation of petroleum products, from refineries to various Mexican ports. The fleet is comprised of six product tankers, most of which are under medium-term contracts. The firm enjoys an advantage here as Mexican Maritime law establishes that cabotage services should be provided by Mexican flag vessels and Mexican companies are given priority.

Chemical Tankers

The firm currently operates two chemical vessels that transport chemicals, vegetable oils and molasses. Currently more than 90% of cargo is transported under a contract of Affreightment. This is a service contract under which a ship owner agrees to transport a specified quantity of fuel products or specialty products, at a specified rate per ton, between designated loading and discharge ports. This type contract differs from a spot or consecutive voyage charter in that no particular vessel is specified.



Harbor Towing

TMM is the sole provider of towing services at the port of Manzanillo since January 1997 and has a concession through January 2015, which is anticipated to be renewed when expired.

The firm currently has five vessels that service over 2,000 vessels per year. Major clients include, NYK, MSC, PEMEX and Hapag-Lloyd.

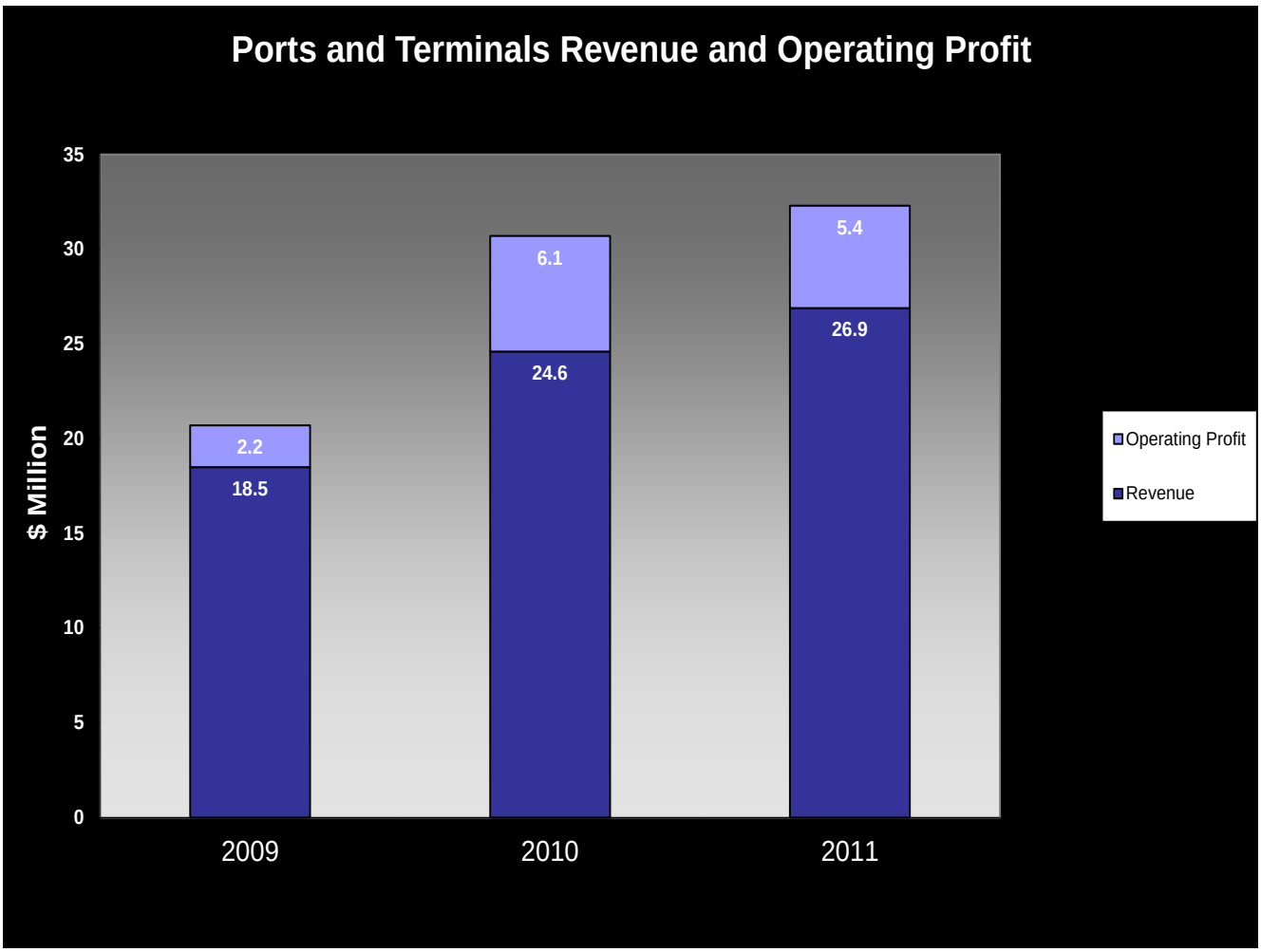


Ports and Terminals Operations. (10% of Total Revenue)

The firm presently operates two Mexican port facilities, Tuxpan and Acapulco, under concessions granted by the Mexican Government, which provide for certain renewal rights. This business unit also provides port agent services to vessel owners and operators in the main Mexican ports. At Acapulco, the

Company operates and manages an automobile terminal, a cruise ship terminal and an automobile warehouse with a capacity to store up to 2,000 automobiles.

The company owns approximately 2,000 acres of land in Tuxpan, and a multipurpose cargo terminal, currently handling only small volume of cargo. As stated above in this report, Grupo TMM has made significant progress on a joint venture to develop a container and a liquids terminal for oil products at this Port.



The Company's shipping agencies offer services including port agent services, cargo and multimodal supervision; ship chandler services and bunkering services.

The automotive segment provides value-added logistics services including storage and distribution of finished vehicles from auto yards to final distribution companies. The Company also offers services of maintenance and repair of containers to major international shipping companies at Mexico's main ports including, Manzanillo, Veracruz, Altamira, Ensenada and Mazatlán, as well as at intermodal and specialized terminals at Mexico City and Aguascalientes. In the second half of 2010, The Ports and Terminals division started offering stevedoring services for general cargo at Tampico.





Logistics Operations. (26% of Total Revenue)
TMM provides dedicated trucking services to major manufacturers, including automobile plants and retailers with facilities and operations throughout Mexico. The firm offers full-service logistical facilities in major industrial cities throughout Mexico, including Aguascalientes, Toluca, Puebla, Veracruz, Nuevo Laredo, Mexico City and Monterrey.

Services provided include consulting, analytical and logistics outsourcing, which encompass the management of inbound movement of parts to manufacturing plants consistent with just-in-time inventory planning practices; logistics network (order-cycle) analysis; logistics information process design; trucking, intermodal transport and auto haulage services; warehousing and bonded warehousing facility management; supply chain and logistics management; product handling and repackaging; local pre-assembly; and inbound and outbound distribution using truck transport.



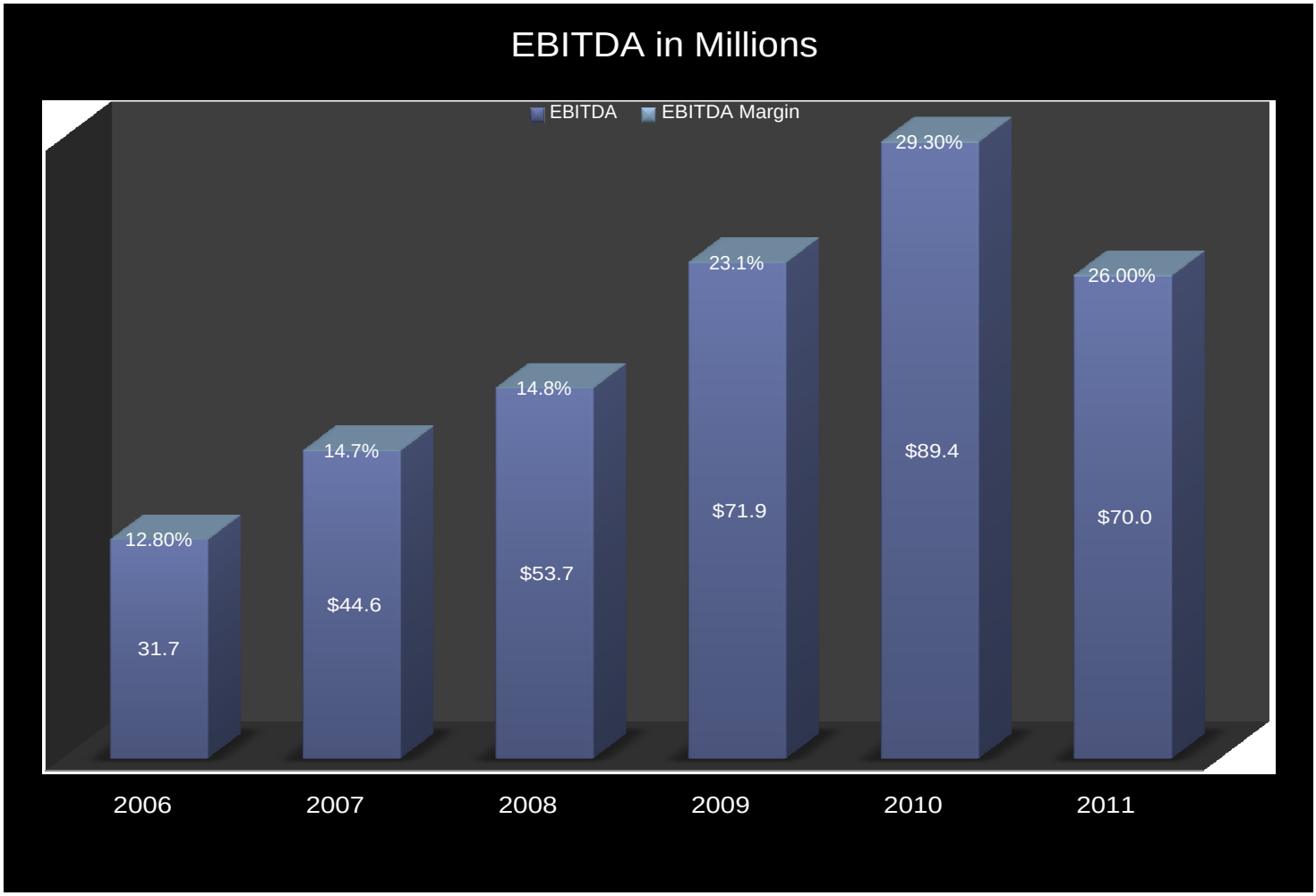
Growth Strategy

Grupo TMM is committed to expanding its Maritime Operations through a number of methods.

The company intends to increase its cabotage and offshore services with medium and long-term contracts. Its intent is to escalate these services by taking advantage of the Mexican Navigation Law which grants priority to Mexican ship owners performing cabotage (intra-Mexican movement between Ports) in Mexican waters. Furthermore, as part of their 5-year growth plan, Grupo TMM expects to continue its commitment of increasing the number of new generation, cost efficient vessels to its fleet and therefore developing higher margin revenues.

Additionally, Grupo TMM's intention is to increase its penetration into Mexican Ports. The company began a small operation of stevedoring services for general cargo during its 2010 Q4 at the Port of Tampico. Stevedoring services include the loading and unloading of ships. Furthermore, the Company owns 2,000 acres of land in Tuxpan and a multipurpose cargo terminal. This property in Tuxpan is uniquely positioned as a container and liquids terminal for oil products and already has a concession and the environmental permits to operate at this port. The Company is currently working on financing alternatives for the development of this site.





Deep Water Drilling Strength

Drilling rig contractors are bullish on the long-term outlook for the global ultra-deepwater drilling sector, with rig demand beginning to recover following the global financial crisis of 2008 and ultra-deepwater rig demand appearing outside the "Golden Triangle" markets of West Africa, Brazil and the U.S. Gulf of Mexico.

The number of deepwater discoveries has picked up again as the global financial recovery and sustainable oil prices have prompted national oil companies, majors and independents to begin spending again on exploration. Drilling companies are finding that operators are opting for high-specification rigs, including rigs with dynamic positioning (DP) capabilities to meet more challenging geological plays as well as increased safety and operational standards.

Noble Corporation also expects to see rig demand recovery over the next several years, with progressive growth toward the end of the decade. While deepwater and mid-water rig rates will remain under pressure in the near-term, the company noted that ultra-deepwater day rates are strong enough to encourage new build rig construction.

Mexican and US GDP Outlook

According to Capital Economics the increase in the Mexican IMEF manufacturing index last month suggests that the industrial sector has continued to benefit from stronger demand in the US. Data released on April 6, 2011 show that the IMEF manufacturing index rose to 54.1 last month, from 52.7 in February. That leaves the overall reading far above 50, which is the notional divide between expansion and contraction. Looking further ahead, demand from the US should remain strong in the near-term and Mexican industry, and therefore the economy, will perform correspondingly well. Capital Economics has projected an overall GDP growth of around 4.3% this year. The United States, with its debt issues faces a bit more of an unknown as most economic analysts look for growth in the range of 2.2%, 2.7%, and 3.1% for the years 2012, 2013, and 2014.

More recently Economists surveyed in October by the Bank of Mexico cut their estimates for economic growth for 2012, citing lower growth rates in the U.S. and persistent volatility in the international financial markets as the European debt crisis is still unresolved. For 2012, economists estimate GDP will grow by just 3.24%, compared with 3.50% previously. The survey of 26 banks and consultancy firms estimated U.S. growth of 2% in 2012, down from 2.1%.

VALUATION

The firm's industry position is quite unique in that it operates as a door to door provider of services, yet also at times enjoys niche markets and other times monopolistic markets. This has the potential to lead to higher margins than the competition. Despite the different segments, the firm is primarily a shipping firm which is set to take advantage of deep water drilling opportunities.

For investors with a time frame of several quarters this may be the best entry point in years as the firm is set to embark on a growth strategy that will improve the capital structure, (now highly leveraged) continue impressive utilization, and provide above average return on assets. When looking at several metrics (P/B, P/S) the firm looks undervalued. From an operational standpoint the firm has made impressive strides. (EBITDA margin and Utilization)

Management has effectively steered the company, for example it has kept its fleet of maritime assets modern with several purchases as well as selling off inefficient equipment. In our opinion investors should be more concerned with the top-line and EBITDA numbers given the large amount of debt denominated in Mexican pesos. This adds the complexity of exchange gains and losses to the bottom line. The firm looks undervalued when looking several ratios. We compared the firm against the transportation industry.

Price to book value ratio is used to compare a stock's market value to its book value. It is calculated by dividing the current closing price of the stock by the latest quarter's book value per share. The book value of equity is the difference between the book value of assets (original price – allowable depreciation) and the book value of liabilities. The market value of an asset in contrast to its book value reflects its earnings power and expected cash flows. The P/BV can very easily be compared across firms in the industry assuming accounting standards are consistent firm to firm.

$$\text{P/B Ratio} = \frac{\text{Stock Price}}{\text{Total Assets - Intangible Assets and Liabilities}}$$

Metric	Grupo TMM	Industry Average
Price/Book Value	0.34	2.03

While not as popular as Price/Earnings or Price/BV, Price/Sales is not influenced by accounting decisions in depreciation, inventory and extraordinary charges. P/S multiples are much less volatile than P/E multiples. However if the problem with the firm lies in cost control the P/S ratio will not reflect this flaw.

Metric	Grupo TMM	Industry Average
Price/Sales	0.14	1.76

According to the Price/Book Value and the Price/Sales models the firm appears undervalued compared to the industry.

Using a blend of these valuation metrics we arrive at a price of $4.50

PROJECTED INCOME STATEMENT

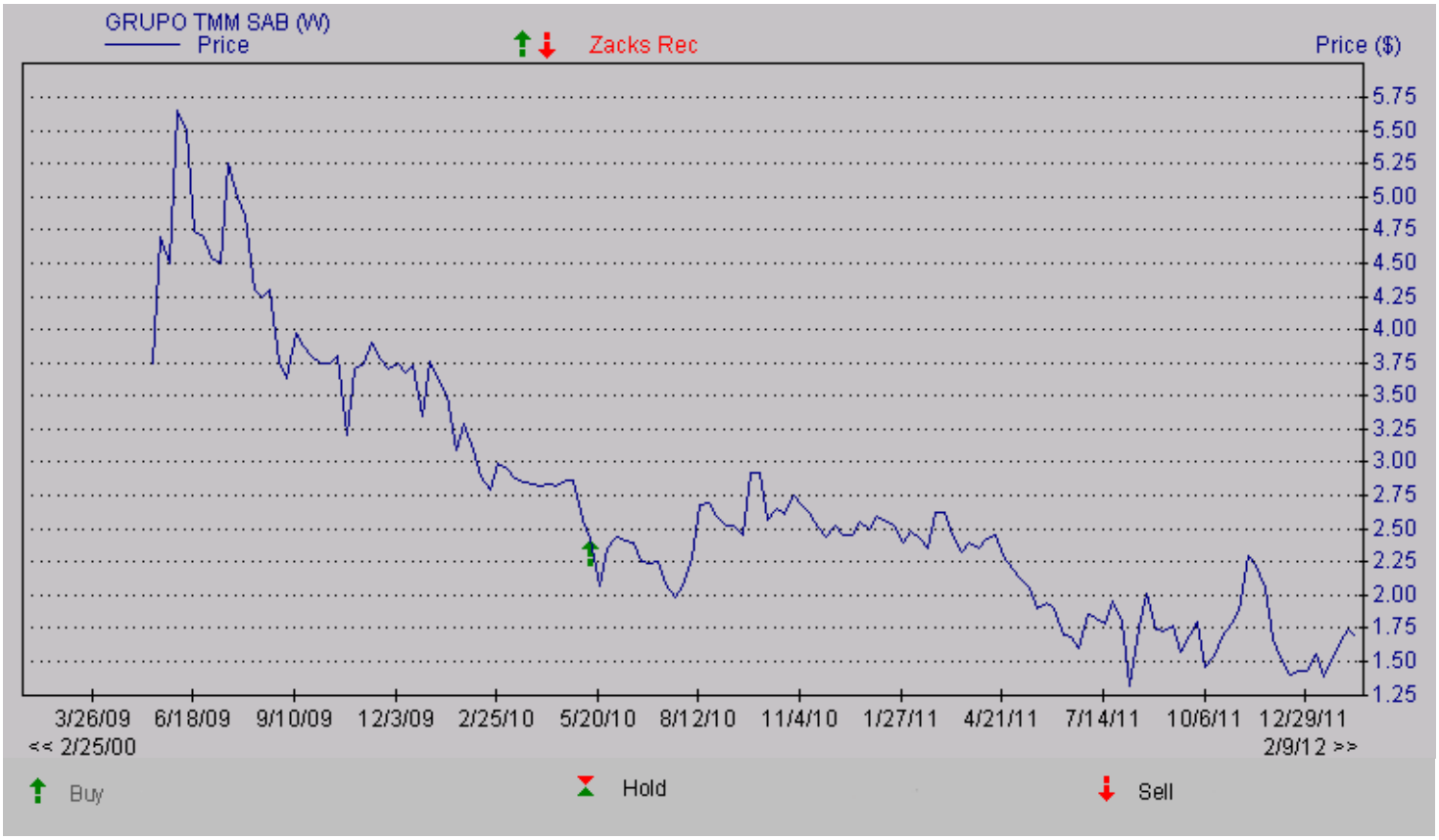
INCOME STATEMENT ($ Millions)	Dec-10 Q4 10	Mar-11 Q1 11	Jun-11 Q2 11	Sep-11 Q3 11	Dec-11 Q4 11	Mar-12 Q1 12 E	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012 E
REVENUE												
Net Revenue	**74.0**	**65.9**	**69.6**	**68.8**	**64.8**	**65.0**	**303.3**	**363.0**	**308.2**	**305.4**	**269.2**	**265.0**
Sequential Growth		*-11%*	*6%*	*-1%*	*-6%*	*0%*						
OPERATING EXPENSES												
Cost of Revenues	47.84	44.17	47.31	47.15	43.76	43.00	253.9	300.5	221.7	198.8	182.4	181.2
% of Revenue	*64.6%*	*67.0%*	*67.9%*	*68.5%*	*67.6%*	*66.2%*						
Gross Profit -	**26.2**	**21.8**	**22.3**	**21.7**	**21.0**	**22.0**	**49.4**	**62.4**	**86.5**	**106.6**	**86.8**	**83.8**
Proforma Gross Margin	*35.4%*	*33.0%*	*32.1%*	*31.5%*	*32.4%*	*33.8%*	*16.3%*	*17.2%*	*28.1%*	*34.9%*	*32.2%*	*31.6%*
Depreciation + Amort	18.89	13.08	13.64	12.71	24.61	12.00	25.7	33.8	44.6	59.5	64.0	63.0
% of Revenue	*25.5%*	*19.8%*	*19.6%*	*18.5%*	*38.0%*	*18.5%*	*8.5%*	*9.3%*	*14.5%*	*19.5%*	*23.8%*	*23.8%*
Corp Expenses	3.38	4.13	4.35	4.40	2.22	3.50	4.4	8.8	14.9	14	15	14
% of Revenue	*4.6%*	*6.3%*	*6.2%*	*6.4%*	*3.4%*	*5.4%*	*1.4%*	*2.4%*	*4.8%*	*4.6%*	*5.6%*	*5.5%*
Other Income (Expenses)-Net	(0.74)	0.79	6.39	1.47	(10.26)	-	-	-	0.48	3.09	(1.62)	(2.40)
% of Revenue												
Total Operating Expenses	23.01	16.42	11.60	15.64	37.09	15.50	30.01	42.55	58.92	70.40	80.74	79.82
% of Revenue	*31.1%*	*24.9%*	*16.7%*	*22.7%*	*57.3%*	*23.8%*	*9.9%*	*11.7%*	*19.1%*	*23%*	*30%*	*30%*
Operating Income -	**3.2**	**5.3**	**10.7**	**6.1**	**-16.1**	**6.5**	**19.3**	**19.9**	**27.5**	**36**	**6**	**4**
Operating Margin	*4.3%*	*8.1%*	*15.4%*	*8.8%*	*-24.8%*	*10.0%*	*6%*	*5%*	*9%*	*12%*	*2%*	*1%*
NON-OPERATING ITEMS												
Non operating Income/Expense	-31	-47	-38	89	10	-70	-48.5	75.6	-118.3	-108	14	-15
% of Revenue	*-41.97%*	*-70.93%*	*-54.73%*	*128.89%*	*14.89%*	*-107.69%*	*-16.00%*	*20.84%*	*-38.39%*	*-35.43%*	*5.02%*	*-5.66%*
Tax Provision	-2.1	0.4	2.4	3.2	-2.7	2.2	-0.84	20.09	1.7	1	3	-5
Effective Tax Rate												
Net Income -	**-25.78**	**-41.87**	**-29.76**	**91.63**	**-3.78**	**-65.70**	**-28.35**	**75.44**	**-92.46**	**-73.03**	**16.22**	**-6.04**
Net Income Margin	*-34.8%*	*-63.5%*	*-42.7%*	*133.1%*	*-5.8%*	*-101.1%*	*-9.3%*	*20.8%*	*-30.0%*	*-24%*	*6%*	*-2%*
EARNINGS PER SHARE												
EPS - Basic	-$0.26	-$0.42	-$0.30	$0.90	-$0.04	-$0.64	-$1.17	$1.47	-$1.43	-$0.79	$0.15	-$0.06
EBITDA (in Millions)	$22.08	$18.41	$24.37	$18.76	$8.52	$18.50	$44.99	$53.68	$72.09	$95.65	$70.05	$66.92

Ken Nagy, CFA Zacks Investment Research 3/1/2012

RISKS

- Despite medium and long-term contracts in place at the Maritime division, tariff volatility could impact operations
- The firm remains highly leveraged with $675 million in net debt.

HISTORICAL ZACKS RECOMMENDATIONS



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