Zacks Small-Cap Research

January 27, 2014
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GRUPO TMM (GTMAY-OTCQB)

GTMAY: TMM's Maritime Continues Positive Trend– Neutral

Current Recommendation	**Neutral**
Prior Recommendation	Outperform
Date of Last Change	04/07/2013
Current Price (01/24/14)	$0.92
Target Price	**$1.50**

OUTLOOK

Grupo TMM is one of the largest maritime transportation companies in Mexico. The firm, through its subsidiaries provides maritime services and ports and terminals management to international and domestic clients throughout Mexico. As part of its 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	**$1.07**
52-Week Low	**$0.70**
One-Year Return (%)	**29.33**
Beta	**0.61**
Average Daily Volume (sh)	**2,740**
Shares Outstanding (mil)	**102**
Market Capitalization ($mil)	**$19**
Short Interest Ratio (days)	**1.97**
Institutional Ownership (%)	**3**
Insider Ownership (%)	**N/A**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-7.5**
EBITDA (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2013 Estimate	**N/A**
Zacks Rank	**3**

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

Revenue
(in millions of Pesos)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2012	618.3 A	637.2 A	692.1 A	644.6 A	2,592.20 A
2013	664.9 A	716.4 A	738.4 A	744.3 E	2,864.00 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2012	-$1.36 A	-$2.10 A	-$1.00 A	-$3.24 A	-$7.70 A
2013	-$1.64 A	-$2.30 A	-$0.70 A	-$1.25 E	-$5.89 E

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WHATS NEW

Grupo TMM Maritime's Business Continues Growing Revenue, Operating Profit and Utilization

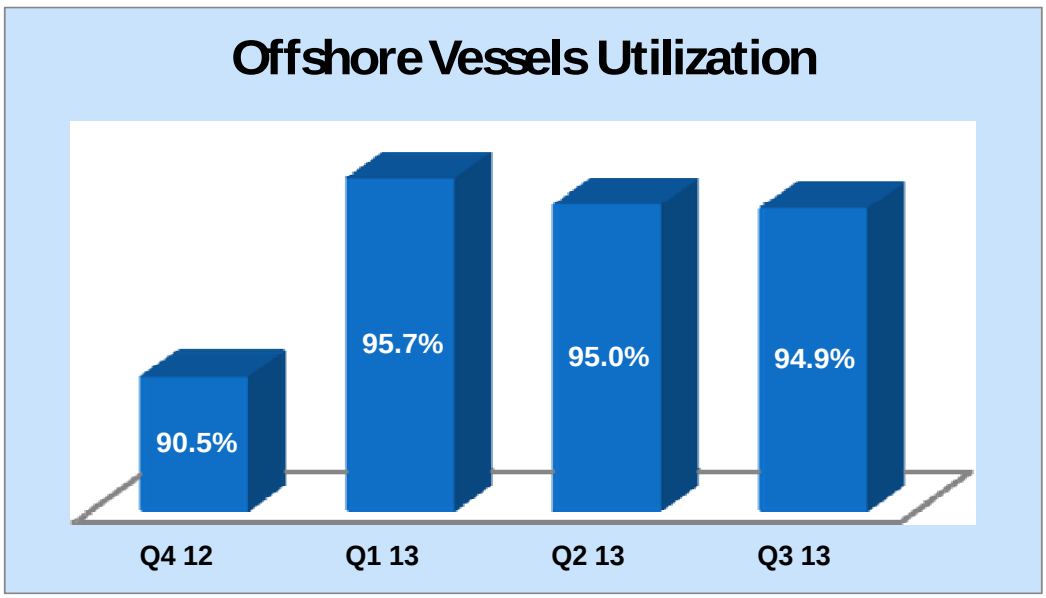
On October 25, 2013 Grupo TMM (OTC: GTMAY and BMV: TMM A) the Mexican maritime transportation and logistics company, released results for the third quarter and first nine months ended September 30, 2013.

Maritime's revenue, operating profit and EBITDA continued its trend of solid performance. Likewise, Maritime's offshore and product tanker fleet utilization sequentially improved throughout 2013.

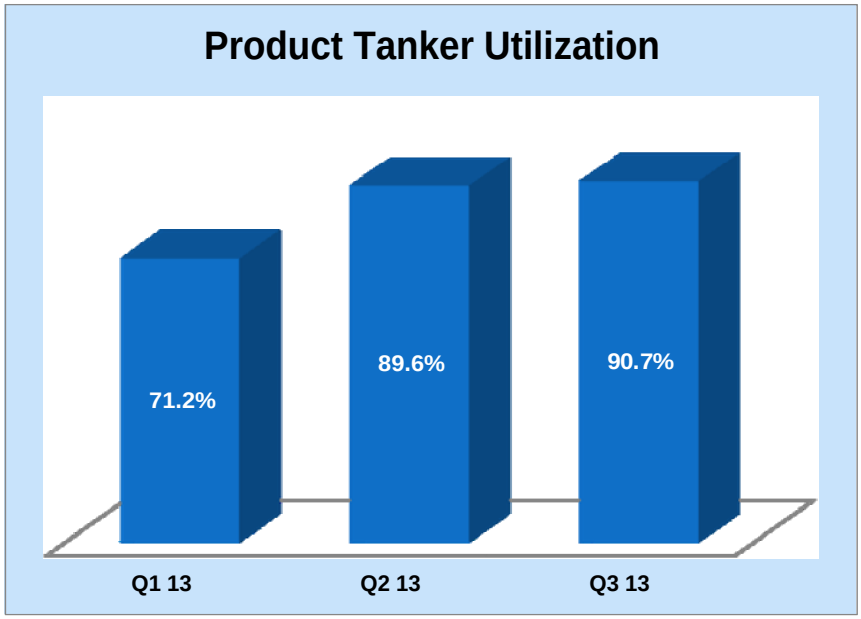
As a result, Grupo's consolidated revenue for the third quarter fiscal 2013 was sturdy at $738.4 million pesos, improving year over year by nearly 7 percent or $46.3 million pesos, from $692.1 million pesos for the comparable quarter of 2012.

The improvement in year over year sales was primarily due to a 10 percent revenue increase at Maritime as a result of revenue improvements at all business segments except for the shipyard, as well as to solid utilization of 94.9 percent in the third quarter. Additionally, product tanker utilization in the 2013 third quarter was 90.7 percent, sequentially improving from 89.6 percent during the second quarter and from 71.2 percent in the fiscal 2013 first quarter. Still, the improvement in Maritime revenue was offset by Grupo's Ports and Terminals revenue.

Grupo's Maritime revenue during the third quarter improved year over year by $59.7 million pesos to $649.2 million pesos. Third quarter 2013 Maritime operating profit increased year over year by over 7 percent or by $10.1 million pesos to $148.5 million pesos.



Consolidated revenue for the first nine months of fiscal 2013 improved year over year by nearly 9 percent or $172.1 million pesos, to $2,119.7 million pesos for the comparable period of 2012. The increase in year over year sales was driven by improvements at Maritime and Ports.



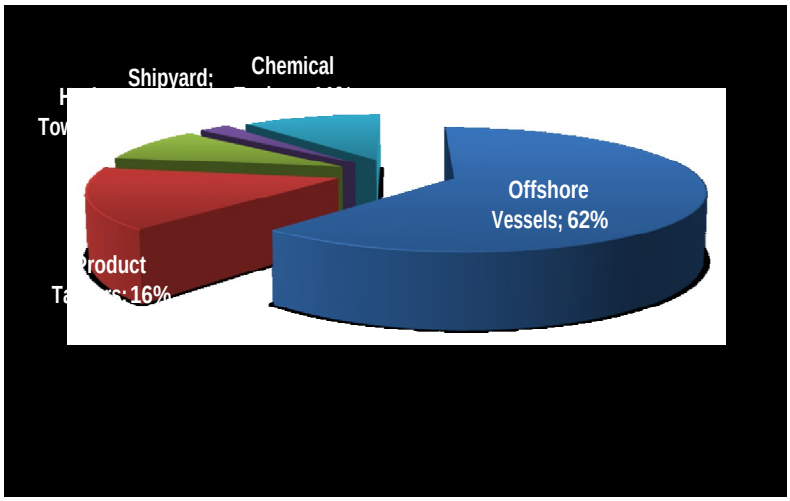
Grupo's Maritime revenue for 2013 the first nine months of fiscal 2013 grew year over year by over 9 percent or by $155.1 million pesos to $1,815.4 million pesos. The improvement was primarily a result of: a 7.8 percent revenue increase at offshore due to higher utilization; a 25.1 percent revenue improvement at chemical tankers as a result of operating one additional leased vessel during the 2013 first quarter and half of the second quarter to service higher freight volumes; 21.8 percent revenue growth at harbor tugs due to an improved revenue mix; and a 4.3 percent revenue increase at product tankers due to an improved revenue mix attributable to operating one vessel in the spot market in the second and third quarter of 2013. Higher revenue was partially offset by a 22.3 percent revenue reduction at the shipyard. Still, despite the shipyard business reporting lower revenue in the year-over-year comparisons, revenue sequentially improved during 2013, from $6.9 million pesos in the first quarter, to $9.8 million pesos in the second quarter and $18.4 million pesos in the third quarter.

Third-quarter 2013 consolidated operating profit decreased by $45.0 million pesos to $121.8 million pesos from $166.8 million pesos in the third quarter of 2012. Still, quarter over quarter, operating profit improved by $22.0 million pesos from $99.8 million pesos during the three months ended June 30, 2013.

Third-quarter 2013 other income net of $25.6 million pesos mainly included a profit of $25.3 million pesos of net tax recoveries. Third-quarter 2012 other income net of $73.5 million pesos mainly included a profit of $69.0 million pesos from the acquisition of a subsidiary in January 2012 and $4.8 million pesos of net tax recoveries.

Excluding the above, non-recurrent events, consolidated operating profit in the 2013 third quarter improved to $96.1 million pesos compared to $93.3 million pesos in the same period of 2012.

9 months ended September 30, 2013 Maritime Contribution



Third-quarter 2013 consolidated EBITDA was $268.1 million pesos, down 15 percent from $316.5 million pesos in the 2012. Sequentially, EBITDA improved from $245.4 million pesos in the second quarter of fiscal 2013.

Consolidated operating profit fell by $22.9 million pesos to $293.2 million pesos in the 2013 nine months from $316.1 million pesos in the 2012 period.

Nine-month 2013 other income net of $32.4 million pesos mainly included $28.5 million pesos of net tax recoveries and $2.8 million pesos from non-recurring fuel inventory income. Nine-month 2012 other income net of $96.0 million pesos mainly included $69.0 million pesos from the acquisition of a subsidiary in January 2012, $23.4 million pesos of cash dividends from affiliates, and $5.4 million pesos of net tax recoveries, partially offset by a $1.5 million pesos reserve for expenses associated with an arbitrage at the Maritime division.

Excluding the above, non-recurrent events, consolidated operating profit in the 2013 nine months increased to $260.8 million pesos compared to $220.1 million pesos in the 2012 period.

Net interest expense during the third quarter was $206.9 million pesos, resulting in free cash flow of $61.2 million pesos. This compares to free cash flow of $35.5 million pesos in the fiscal 2013 second quarter. Net interest expense in the 2013 nine months was $206.9 million pesos resulting in free cash flow of $108.5 million pesos.

As of September 30, 2013, TMM's total net debt was $9,781.3 million pesos compared to total net debt of $9,887.0 million pesos at the end of the second quarter of 2013. Of TMM’s total debt, only $247.9 million pesos, or 2.3 percent, is short term. In the nine months of 2013, the Company paid accrued interest of $784.9 million pesos and a capital prepayment of $5.0 million pesos for its Trust Certificates debt.

Divesting Logistics

The Company’s board of directors approved the sale of some of Grupo TMM’s non-core assets, which include the trucking, auto hauling and warehousing operations. Looking at the past two fiscal years, the aforementioned discontinued operations incurred in operating losses of $275.6 million pesos in 2011 and $161.6 million pesos in 2012.

In September 2013, the Company completed the sale of its trucking and auto hauling assets and operations. The sale of these non-strategic assets eliminated operating-related losses beginning in the third quarter, and will continue to lead to improved consolidated results. The Company’s warehousing business continues to be presented as a discontinued operation held for sale.

Management expects to continue to work on alternatives to improve the Company's balance sheet, while sharpening its focus on growing TMM's core businesses by targeting new business opportunities at its Maritime and Port divisions.

Strategy Change
Due to changes in the economic environment and to the fact that TMM's current operations are concentrated in Mexico; on February 2013, the Company changed its functional and reporting currency from the U.S. dollar to the Mexican peso effective January 1, 2012. This change eliminated the impact of exchange rate volatility in net financial cost and in turn in stockholders equity. Exchange rate volatility was significant over the past two years.

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.

While development of the facility could take up to two years, management believes it will reach an agreement for the financial implementation of the development of a container terminal. Still, when completed, the terminal will strategically position TMM in these lucrative markets.

The second project includes the addition of specialized offshore vessels to TMM's fleet to meet increased demand for deep water transportation. The Company's 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.

INVESTMENT THESIS

- The firm's Maritime division is the dominant business at TMM. In the 2012 third quarter the Company added two offshore vessels to its fleet. TMM is committed to continue to modernize its fleet with specialized offshore vessels. TMM prefers to compete for margin rich niche business and employs long to medium-term contracts.

- TMM is committed to increase its penetration in Mexican ports, particularly Tuxpan. This should make the firm more efficient and more profitable in the long run.

- The outlook for deep water drilling is promising.

- Mexico's new energy reform will benefit TMM's offshore business.

- TMM is evaluating the possibility to join forces with an international shipyard to allow for building capacities at its shipyard in Tampico.

BUSINESS DIVISIONS

Maritime Operations (85% 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 40 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 27 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.


ECO III

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 5 product tankers. 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.


Amatlán

Chemical Tankers
The firm currently operates 2 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.


Maya

Harbor Towing

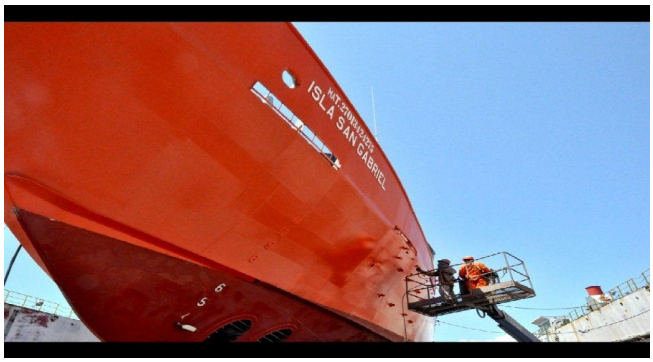
TMM is the sole provider of towing services at the port of Manzanillo since January 1997 and has a concession through January 2015, which is anticipated to be renewed when expired. The firm currently has 6 vessels that service over 2,000 vessels per year. Major clients include, NYK, MSC, Pemex and Hapag-Lloyd. Also, in March 2012, TMM began providing tug services to a new Liquefied Natural Gas, or LNG, terminal at Manzanillo, which has significantly improved the revenue mix of this division.



TMM Cuyutlán

Shipyard

In January 2012, TMM announced the acquisition of a shipyard at the Port of Tampico, Veracruz. The shipyard concentrates on ship repair and has in operation two, 3,000-ton lift capacity dry docks. In the longer term, the Company expects to have the necessary capabilities to build vessels at this facility, through the association of an international shipyard.



Shipyard- Gulf of Mexico

Ports and Terminals Operations. (13% of Total Revenue)

Grupo 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 shipping agencies services at major Mexican ports. At Acapulco, the Company operates and manages a cruise ship terminal and an automobile warehouse with a capacity to store up to 2,000 automobiles.



API Acapulco



Acapulco auto warehouse

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 expects to reach an agreement for the financing of the development of a container terminal at this Port. It is important to note that the Company has the required environmental permits to develop and operate at this port. The Company is also working on the financial implementation for a liquids terminal at Tuxpan.

This division shipping agencies offer services including port agent services, cargo and multimodal supervision; ship chandler services and bunkering services.

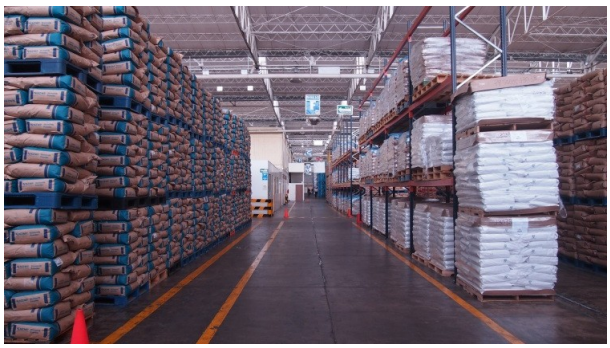
The automotive segment provides value-added logistics services including storage and distribution of finished vehicles from auto yards to final distribution companies.

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.



Maintenance and Repair of Containers ("M&R)

Warehousing Services (2% of Total Revenue)
In December 2006, Grupo TMM acquired a warehousing company offering services such as fiscal bonded warehousing services, fiscal habilitation of customers' own warehouse, verification and compliance unit, issuing of deposit certificates and pledge bonds, logistics, distribution and fiduciary services. This business is currently presented as a discontinued operation as it is being held for sale.



Warehousing Services

ENERGY REFORM

Grupo TMM Stands Ready to Benefit from an Oil Industry Overhaul

On August 2013, Mexico moved to end the country's 75-year-old monopoly on oil and gas production, potentially opening up some of the worlds biggest remaining untapped oil reserves to private companies and setting the stage for a new energy boom on the U.S. doorstep. Should the new energy reform go through it should benefit TMM going forward, specifically in its offshore related operations.

The proposed new energy reform, would allow for private and foreign investment in the oil industry. This new energy reform allows for larger private and foreign investment at Pemex, to increase deep water exploration and production. The new energy reform should benefit TMM going forward, specifically in its offshore related operations.

History

Mexico in 1938 was the first big oil producer to nationalize its oil industry—a move followed by other developing nations in the following decades.

State oil monopoly Pemex, the sole producer of oil and gas in Mexico, now pays a fee to service companies to do everything from exploration to drill wells. But that model has failed to attract interest from major oil companies and led oil production in Mexico to plummet.

Mexico's oil production has fallen by one quarter over the past decade to 2.5 million barrels a day and new resources are more expensive and more difficult to develop. Already Mexico imports gasoline and natural gas, spending half of every dollar it makes on crude oil and although Mexico has huge gas reserves, Pemex drilled only three gas wells in 2012.

Opportunity

Major oil companies that have struggled to find big new oil fields are likely to find appeal in the relatively familiar geology and operating conditions of Mexico versus the Arctic or some politically unstable regions of Africa and the Middle East, particularly those active on the U.S. side of the Gulf of Mexico.

Mexican officials hope the initiative, the biggest potential overhaul to the economy since the 1994 North American Free Trade Agreement, will spur economic growth by attracting billions of dollars in investment, improve competitiveness by lowering energy prices for manufacturers and spotlight Mexico as a rising power as other big emerging markets struggle.

How Would it Look?

The Energy Reform doesn’t, give private oil companies outright ownership of oil fields via concessions or give oil firms a share of the oil, but rather the cash equivalent of the oil they find and produce.

VALUATION

Despite the different segments, the firm is primarily a shipping firm which is set to take advantage of deep water drilling opportunities and is uniquely positioned for higher margins than the competition due to the nature of its medium and long term contracts, having less exposure to tariff volatility.

For investors with a time frame of several quarters this may be a good entry point 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 cash flow and EBITDA numbers. We compared the firm against the transportation industry.

Metric	Grupo TMM	Industry Average
EV/EBITDA	14.32x	7.59x

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	0.10x	3.95x

According to the Price/Sales model the firm appears undervalued and fairly valued using the enterprise model compared to the industry. Using a blend of these valuation metrics including a price to sales multiple well below the industry average we arrive at a price of $1.50.

PROJECTED INCOME STATEMENT

INCOME STATEMENT (MXP Millions)	FY 2011	FY 2012	FY 2013 E	FY 2014 E
REVENUE				
Ports & Terminals	**330.89**	**350.85**	**340.00**	**330.00**
Maritime	**2,133.40**	**2,188.81**	**2,474.00**	**2,500.00**
Others	**49.93**	**52.54**	**50.00**	**51.00**
Net Revenue	**2,514.22**	**2,592.20**	**2,864.00**	**2,881.00**
Sequential Growth				
OPERATING EXPENSES				
Ports & Terminals	252.18	280.75	275.00	263.00
Maritime	*1,115.74*	*1,206.87*	*1,353.10*	*1,300.00*
Others	*48.84*	*53.24*	*50.00*	*52.00*
Gross Profit -	**1,097.47**	**1,051.34**	**1,185.90**	**1,266.00**
Proforma Gross Margin	*0.44*	*0.41*	*0.41*	*0.44*
Depreciation and Amortization				
Ports & Terminals	*15.31*	*15.30*	*15.00*	*15.00*
Maritime	*521.14*	*561.86*	*550.00*	*570.00*
Others	*12.81*	*12.54*	*9.00*	*10.00*
Total D&A	***549.26***	***589.70***	***574.00***	***595.00***
Ports & Terminals	*63.40*	*54.79*	*50.00*	*52.00*
Maritime	*496.52*	*420.08*	*530.00*	*600.00*
Others	*(11.72)*	*(13.24)*	*(8.50)*	*(10.00)*
Corporate	*(187.59)*	*(172.00)*	*(175.00)*	*(220.00)*
Other Income (expense)	*(20.11)*	*(3.56)*	*12.00*	*15.00*
Operating Income	**340.51**	**286.08**	**408.50**	**437.00**
Proforma Operating Margin	*0.31*	*0.27*	*0.34*	*0.35*
Ports & Terminals	78.71	70.10	65.00	67.00
Maritime	1,017.66	981.94	1,120.30	1,200.00
Others	1.09	(0.70)	-	1.00
Corporate	(187.59)	(172.00)	(175.00)	(180.00)
Other Income (expense)	(20.11)	(3.56)	35.00	10.00
EBITDA	**889.77**	**875.78**	**1,045.30**	**1,098.00**
Non-Operating				
Loss from Discontinued Ops	(275.65)	(161.62)	(90.00)	(0.15)
Financial Cost	167.80	(896.80)	(906.00)	(915.00)
Min int	*12.50*	*5.30*	*4.00*	*4.00*
Tax Provision	41.10	8.80	10.00	15.00
Effective Tax Rate				
Net Income -	**179.06**	**(786.44)**	**(601.50)**	**(497.15)**
Net Income Margin	*0.07*	*(0.30)*	*(0.21)*	*(0.17)*
Adjustments for Disc Ops	-	-		
EARNINGS PER SHARE				
EPS - Basic	1.75	(7.70)	(5.89)	(4.87)
EPS - Diluted	1.75	(7.70)	(5.89)	(4.87)

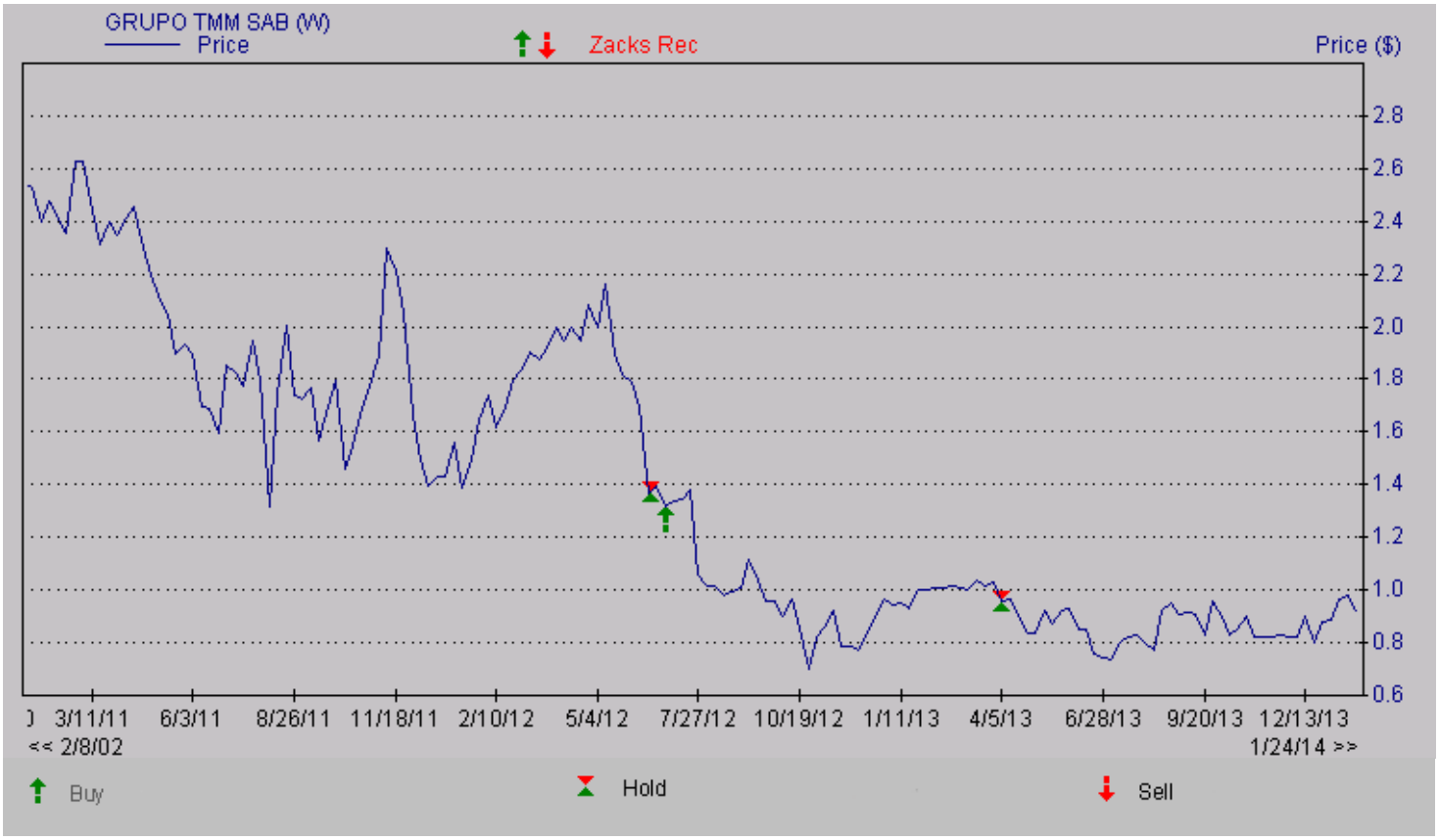
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** Model does not include new projects*

RISKS

- 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 firm remains highly leveraged with MXP 9,781.3 million in net debt.
- Should the firm not succeed in its new projects, it faces further pressure in Stockholders Equity.

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Hold/Neutral: The analyst expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters.
Sell/Underperform: The analyst expects the company will underperform the broader U.S. Equity market over the next one to two quarters.

The current distribution is as follows: Buy/Outperform- 16.7%, Hold/Neutral- 77.4%, Sell/Underperform – 5.2%. Data is as of midnight on the business day immediately prior to this publication.