

AGUA: 1Q23 Results

Record profitability levels due to price strategy and lower raw material costs; positive

AGUA*	BUY
Target Price (MXN\$)	\$ 44.00
Current Price (MXN\$)	\$ 25.71
Min / Max (L12M)	\$ 21.00 - 34.71
Expected Dividend (MXN\$)	\$ 0.50
Expected Return	73.1%
Market Cap (MXN\$ Mn)	12,501
Enterprise Value (MXN\$ Mn)	15,965
Outstanding Shares (Mn)	486.2
Float	23.7%
ADTV (MXN\$ Mn)	\$ 8.37

Opinion and recommendation

AGUA posted positive 1Q23 results with revenues and EBITDA exceeding our projections and net income slightly below our expectations.

AGUA adjusted its guidance for the year due to the strength of the Mexican peso. It now expects a 10% revenue growth (previously it was above 15%) with the same profitability (EBITDA margin of 16.0-17.0%), leverage (less than 2.0x) and ROIC (equal to WACC + 150 bps). We believe this guidance is achievable taking into account the FX level.

After having updated our model, we are maintaining our BUY recommendation and we are adjusting our target price to MXN\$44.0/share, from MXN\$45.00/share.

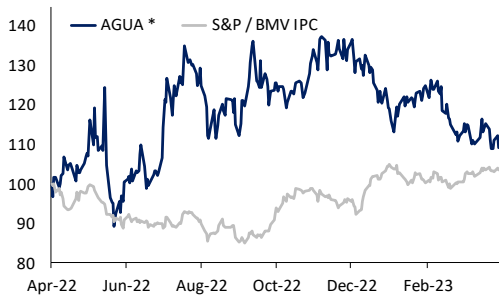
Revenues

Revenues were up 3.2% YoY to MXN\$2.75 billion, due to a 1.4% increase in the products business and 54.1% in the services business, mainly in Mexico. Excluding the appreciation of the Mexican peso, total revenues would have risen 7.9%.

Profitability

The gross margin expanded 750 basis points to a record level of 47.7%, supported by a competitive pricing strategy, as well as the reduction in the resin cost.

EBITDA grew 71.9% to MXN\$553 million. The margin also experienced a significant 800 bps improvement, reaching 20.1% due to the company's expense control.



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However, net profits declined 58.4% to MXN\$37 million due to an accounting loss in the mark-to-market of currency hedges, given the appreciation of the FX rate in the quarter. ROIC improved 300 bps to 16.1%, it was 410 bps higher than the cost of capital and exceeded the guidance for the year.

Financial structure

The net debt to EBITDA ratio remained stable at 1.6x. Net debt increased 30.7% due to a reduction in cash levels which was offset by the significant EBITDA growth.

Performance by region

Mexico revenues advanced 10.0% thanks to a double-digit rise in water flow and improvement, the recovery of the water treatment and recycling plant business, the continued growth of *Bebbia*, which had 92,000 users at the end of the quarter, and the expansion of *Rieggio*. The EBITDA margin reached 30.5% supported by the commercial policy, lower raw material costs and the reduction of losses in the services platform.

In the United States, sales decreased 15.9% due to the change in the digital platform, in addition to excessive snow and rain in certain states. However, the company mentioned that the operational issues have already been resolved. Profitability remained in negative territory.

In Argentina, revenues were virtually flat due to the appreciation of the Mexican peso against the Argentine peso, which offset the increase in sales in local currency. The EBITDA margin contracted to 12.9% as a result of higher expenses and the fact that the drop in raw material costs has not yet been reflected.

In the other countries, sales were up 2.1% fueled by the improvement category in Peru. Meanwhile, Brazil's project portfolio continued to grow due to new legislation supporting the private model. Profitability rose significantly (+950 bps in the EBITDA margin to 19.2%) due to lower raw material costs, a stronger performance in Brazil and expense control.

ESG

AGUA was included in S&P Global's "Sustainability Yearbook" for the second year in a row, forming part of the top 8 best rated companies in ESG issues within the industry. It received the distinction of "Company Committed to the Labor Inclusion of People with Disabilities" granted by Éntrale. It launched the national call in partnership with the United Nations Development Program (UNDP) for the 2023 to flow program, which focuses on benefiting municipalities with the greatest lack of access to water and sanitation.

(Figures in Millions of MXN\$)	1Q23	1Q23E	Diff.	1Q22	Change
Revenues	2,746	2,766	-0.7%	2,660	3.2%
Adjusted EBITDA	553	443	24.9%	322	71.7%
EBITDA Margin	20.1%	16.0%		12.1%	
Financial Gains	31	24	28.6%	41	-25.9%
Financial Cost	-441	-290	52.2%	-196	125.3%
Pre-Tax Profit	27	64	-57.2%	68	-59.9%
Income Tax & Profit Sharing	9	-23	n.a.	20	-53.1%
Tax & Profit Sharing Rate	-34.5%	36.0%		-29.5%	
Net Profit	37	41	-10.0%	88	-58.4%
ROIC	16.1%	15.7%		13.1%	

Discounted Cash Flow Model

(Figures in Millions of MXN\$)	2024E	2025E	2026E	2027E	2028E	Perp.
OPERATING PROFIT	2,401	2,870	3,316	3,780	4,246	4,456
Tax Rate	30%	30%	30%	30%	30%	30%
Tax Shield	-720	-861	-995	-1,134	-1,274	-1,337
NOPLAT	1,681	2,009	2,321	2,646	2,972	3,120
Depreciation	496	532	568	604	604	634
Working Capital Changes	-285	69	-306	-337	-371	-390
CAPEX	-772	-850	-936	-1,031	-1,135	-1,191
FCFF	1,120	1,760	1,647	1,882	2,070	2,173
Perpetuity Growth Rate						5.0%
PV of Explicit Period (2024 - 2028E)						6,111
Perpetuity Value						35,995
PV of Perpetuity Value						19,249
Enterprise Value						25,360
Net Debt						3,828
Minority Interest						140
Market Value						21,392
Outstanding Shares						486
Target Price						P\$ 44.00
Current Market Price						P\$ 25.64
Potential Return Incl. Dividends						73.3%
Forward EV/EBITDA						8.8x
Forward P/E						18.1x
Average Cost of Debt						8.9%
LT Tax Rate						30.0%
After-Tax Cost of Debt						6.2%
Cost of Equity						14.9%
Market Risk Premium						6.0%
Risk-Free Rate						8.8%
Beta						1.02
% Total Debt						39.9%
% Capital						60.1%
ESG Adjusted WACC						11.0%

Sensitivity Analysis, EV/EBITDA vs. EBITDA

	-10%	-5%	<i>Original</i>	+5%	+10%
Projected EBITDA	2,615	2,752	2,897	3,042	3,194
Target EV/EBITDA					
7.3x	30.83	32.89	35.06	37.23	39.50
7.8x	33.52	35.72	38.04	40.35	42.78
8.3x	36.21	38.55	41.02	43.48	46.07
8.8x	38.90	41.38	44.00	46.61	49.35
9.3x	41.59	44.21	46.98	49.74	52.64
9.8x	44.28	47.04	49.95	52.87	55.92

Sensitivity Analysis, P/E vs. Net Profit

	-10%	-5%	<i>Original</i>	+5%	+10%
Projected Net Profit	1,064	1,120	1,179	1,238	1,300
Target P/E					
15.1x	33.14	34.88	36.72	38.56	40.48
16.1x	35.33	37.19	39.14	41.10	43.16
17.1x	37.52	39.49	41.57	43.65	45.83
18.1x	39.71	41.80	44.00	46.20	48.51
19.1x	41.90	44.10	46.42	48.74	51.18
20.1x	44.08	46.40	48.85	51.29	53.85

(Figures in Millions of MXN\$)

INCOME STATEMENT	2022	2023E	2024E	2025E	2026E	2027E	2028E
Revenues	12,774	14,022	15,440	17,000	18,719	20,611	22,695
Cost of Sales	-7,331	-7,815	-8,590	-9,441	-10,377	-11,405	-12,536
Gross Profit	5,444	6,207	6,850	7,559	8,342	9,206	10,159
<i>Gross Margin</i>	42.6%	44.3%	44.4%	44.5%	44.6%	44.7%	44.8%
General Expenses	-3,859	-4,374	-4,449	-4,689	-5,026	-5,426	-5,914
Operating Profit	1,584	1,833	2,401	2,870	3,316	3,780	4,246
<i>Operating Margin</i>	12.4%	13.1%	15.6%	16.9%	17.7%	18.3%	18.7%
Adjusted EBITDA	1,982	2,287	2,897	3,402	3,884	4,384	4,850
<i>EBITDA Margin</i>	15.5%	16.3%	18.8%	20.0%	20.8%	21.3%	21.4%
Financial Gains	198	94	147	208	362	520	698
Financial Cost	-966	-1,080	-873	-866	-953	-999	-1,021
Pre-Tax Profit	817	846	1,685	2,224	2,739	3,314	3,937
Income Tax & Profit Sharing	-61	-236	-505	-667	-822	-994	-1,181
<i>Tax & Profit Sharing Rate</i>	7.5%	27.9%	30.0%	30.0%	30.0%	30.0%	30.0%
Net Profit	756	610	1,179	1,557	1,917	2,320	2,756
Outstanding Shares	486	486	486	486	486	486	486
EPS	P\$ 1.51	P\$ 1.33	P\$ 2.58	P\$ 3.40	P\$ 4.19	P\$ 5.07	P\$ 6.03
BALANCE SHEET	2022	2023E	2024E	2025E	2026E	2027E	2028E
TOTAL ASSETS	12,528	13,416	15,073	17,045	19,304	22,055	24,981
Current Assets	4,685	5,184	6,143	7,373	8,839	10,734	12,698
Cash & Temp. Inv.	673	561	1,081	2,210	3,182	4,534	5,901
LT Assets	7,843	8,232	8,930	9,671	10,466	11,321	12,283
P, P & E	3,272	3,540	4,216	4,934	5,702	6,529	7,459
TOTAL LIABILITIES	6,101	6,876	7,587	8,225	8,780	9,412	9,771
ST Liabilities	1,502	2,269	2,980	3,117	3,173	3,305	3,163
LT Liabilities	4,600	4,608	4,608	5,108	5,608	6,108	6,608
TOTAL DEBT	4,009	4,389	4,945	5,412	5,781	6,207	6,340
NET DEBT	3,337	3,828	3,864	3,202	2,599	1,673	439
TOTAL CAPITAL	6,427	6,610	7,556	8,891	10,595	12,713	15,281
Stockholder's Equity	6,291	6,471	7,397	8,703	10,371	12,445	14,958
Minority Interest	136	140	159	188	224	268	322
CASH FLOW STATEMENT	2022	2023E	2024E	2025E	2026E	2027E	2028E
PRE-TAX PROFIT	756	856	1,685	2,224	2,739	3,314	3,937
Inv. Related Activities	1,118	824	602	638	674	710	710
Pre-Tax Cash Flow	1,925	585	239	621	908	1,224	1,511
Working Capital Changes	-927	-750	-285	69	-306	-337	-371
Operating Cash Flow	998	-165	-46	691	602	886	1,140
Investment Cash Flow	-601	-485	-530	-548	-479	-416	-342
Financing Cash Flow	-1,073	801	1,359	1,249	1,113	1,145	831
Net Incr. (Decr.) in Cash & Temp. Inv.	-956	86	783	1,392	1,235	1,615	1,629
Beg. of Period Cash and Temp. Inv.	1,629	673	561	1,081	2,210	3,182	#iREF!
End of Period Cash and Temp. Inv.	673	561	1,081	2,210	3,182	4,534	5,901

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