EKT 4.88% 28s

MARKET OUTPERFORM (MEXICO)

Summary: Grupo Elektra is a Mexican based leading retailer and provider of financial services focused on low-middle income households, and the largest company of Grupo Salinas with a US$14 bn mkt cap. Grupo Elektra´s financial segment is Banco Azteca, a regulated entity and part of Mexico's banking system. Issued with an IG rating, the EKT bonds were downgraded by Fitch on the basis of corporate governance concerns. Yet, we see Grupo Elektra well positioned with strong retail y/y growth, done well throughout the pandemic, strong liquidity with cash at US$1.9 bn and a net leverage below 1.0x on a consolidated basis. The bonds are secured by receivables owed by Western Union and two other US remitters of remittances paid upfront by NEM. US remittances have continuously grown y/y, and the monthly eligible reimbursements backing up the bonds add up to US$1.0 bn, an implied 93x debt service coverage ratio. Accordingly, we see EKT 28s as offering IG credit metrics with HY rating and very cheap to fundamentals. We note conflicts of interests, different treatments to creditors, and perception of weak corporate governance concerns are potential downside risks.

Description	Amt Out (US$ MM)	Ratings (M/SP/F)	Mid Price	Mid YTCnv
EKT 4.88% 1/15/2028	500	-/-/BB+	85.00	10.37%

Pros

- Mexican leading retailer and provider of financial services with 6,279 units in Mexico, Guatemala, Honduras and the US
    - Mexico is the primary market accounting for 88% of FY21 total revenue
- Grupo Elektra is a public company with a market cap of US$14.7 bn
- The bonds are secured by eligible reimbursements of remittances paid upfront by NEM
    - In February 2022, the eligible reimbursements were US$1 bn, an implied 93.2x monthly debt service coverage vs 10.0x minimum required
- In February 2022, US- Mexico remittances were 23% higher y/y, registering more than 2 years in positive territory. NEM has a market share close to 48%
- The bonds are also guaranteed by the Holdco
- Strong commercial recovery. FY21 commercial revenue increased by 25% y/y, 52% higher vs FY19
- FY21 financial revenue recovered, increasing by 12% vs pre-pandemic FY19
- FY21 loan portfolio grew 18% y/y to US$6.9 bn with NPLs relatively stable at 4.8%
- Banco Azteca's equity/assets of 17% is higher vs 12% avg. among peers
- FY21 EBITDA doubled vs FY20 to US$1.1 bn and increased by 14% vs pre-pandemic FY19
- Strong cash balance at MXN$38.6 bn (US$1.9 bn) and 0.3x net leverage
- Given the structure, the bonds were initially rated BBB-, downgraded to BB+ due to corporate governance concerns
- Compares favorably vs other Grupo Salinas companies
- Good relationship between the shareholder and AMLO

Cons

- Conflict of interests, different treatments to creditors, and perception of weak corporate governance
    - Fitch downgraded EKT 28s solely based on the selective default of TZA
    - Corporate governance could impact future funding availability
- Complicated bond structure
- Bonds start amortizing US$25 mm every quarter, starting on April 2023
- Potential MXN$18 bn deferred tax liability from "illegal" tax deductions from 2008 to 2012, still being discussed at the Supreme Court
- Recurrent local CEBURES refinancing. As of 4Q21, MXN$14 bn in local cebures was due in 12 months.
- Govt. and Mexico's Central Bank proposal of banking Mexican migrants in the US through state-owned "Banco del Bienestar", offering a better exchange rate. Yet, it's not seen as an imminent risk.
- Increased competition from new alternative methods of remitting cash to Mexico, such as Facebook Coin and cryptocurrencies, yet it's not a concern in the short-term.

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Company Overview

- Grupo Elektra is a leading retailer and financial services provider focused on the low-middle income households in Mexico
- Grupo Elektra is a public company with a market cap of US$14.7 bn and is the main company of Grupo Salinas
    - We highlight that Grupo Salinas companies are separate entities, as there is no Hold Co
    - The other relevant companies are Total Play (TOTALP) and TV Azteca (TZA)
- The retailer business accounts for 45% of total revenue
    - Also known as "Nuevo Elektra del Milenio" ("NEM"), operates the remittance business and the retail stores, which sell primarily electronics, appliances, furniture, etc
    - As of FY21, the remittance business accounted for 7% of commercial revenue, and 3% of the consolidated revenue
- The financial services account for 55% of total revenue
    - Comprised primarily of "Banco Azteca", the ninth largest bank in Mexico with an MXN$140.7 bn (US$6.9 bn) loan portfolio
    - Banco Azteca's equity/assets ratio is 17%, higher vs the avg. 12% at other Mexican banks

Recent Trends

- FY21 Revenue increased by 21% y/y, being 27% higher vs pre-pandemic levels at MXN$146 bn (US$7.2 bn)
    - Commercial revenue increased by 25% y/y to MXN$65.5 bn, driven by motorcycles and phones
    - Financial revenue was 18% higher y/y at MXN$80.4 bn, in line with 18% growth in the loan portfolio maintaining NPLs relatively stable at 4.8%
- EBITDA doubled y/y to MXN$22.0 bn (US$1.1 bn), being 14% above pre-pandemic levels
    - EBITDA growth was in line with higher revenue, partially offset by higher commercial costs
    - As a result, FY21 EBITDA margin contracted to 15% vs 17% in FY19, yet recovered vs 2020 due to lower financial costs
- FY21 FCF burn was MXN$2.5 bn driven by WK, which was from the strong growth in the loan portfolio
- Deposits increased to MXN$185 bn (US$9.0 bn), with the net debt & deposits to loans at 152%
- As of 4Q21, Grupo Elektra had a strong liquidity with MXN$38.6 bn (US$1.9 bn) in cash
    - Vs MXN$44.8 bn (US$2.2 bn) in total debt
- 2021 Net leverage stood at 0.3x

Grupo Elektra (MXN MM)	2018	2019	2020	2021
Financial Revenue	65,429	71,958	68,253	80,490
Commercial Revenue	38,447	43,215	52,254	65,529
Total Revenue	103,876	115,173	120,507	146,019
EBITDA	18,065	19,253	9,812	22,015
Interest Paid	(2,117)	(6,295)	(6,122)	(6,694)
Capex	(7,453)	(8,816)	(5,906)	(7,262)
Working Capital	50	13,488	(6,792)	(6,643)
Taxes Paid	(4,898)	(3,886)	(2,132)	(3,920)
FCF	3,646	13,744	(11,140)	(2,504)
Total Debt (incl. leases)	23,537	35,615	36,214	44,877
Cash & Equivalents	26,183	26,014	37,659	38,563
Net Debt	(2,646)	9,601	(1,445)	6,314
EBITDA margin %	17%	17%	8%	15%
Total Debt / LTM EBITDA	1.3x	1.8x	3.7x	2.0x
Net Debt / LTM EBITDA	-0.1x	0.5x	-0.1x	0.3x
Gross Loan Portfolio	97,578	110,897	119,105	140,706
Total Deposits	123,463	154,977	172,627	184,898
(Net Debt+Deposits) / Net Total Loans	136%	163%	158%	152%
Equity / Total Assets	30%	28%	25%	25%
NPLs %	4.1%	4.2%	4.7%	4.8%

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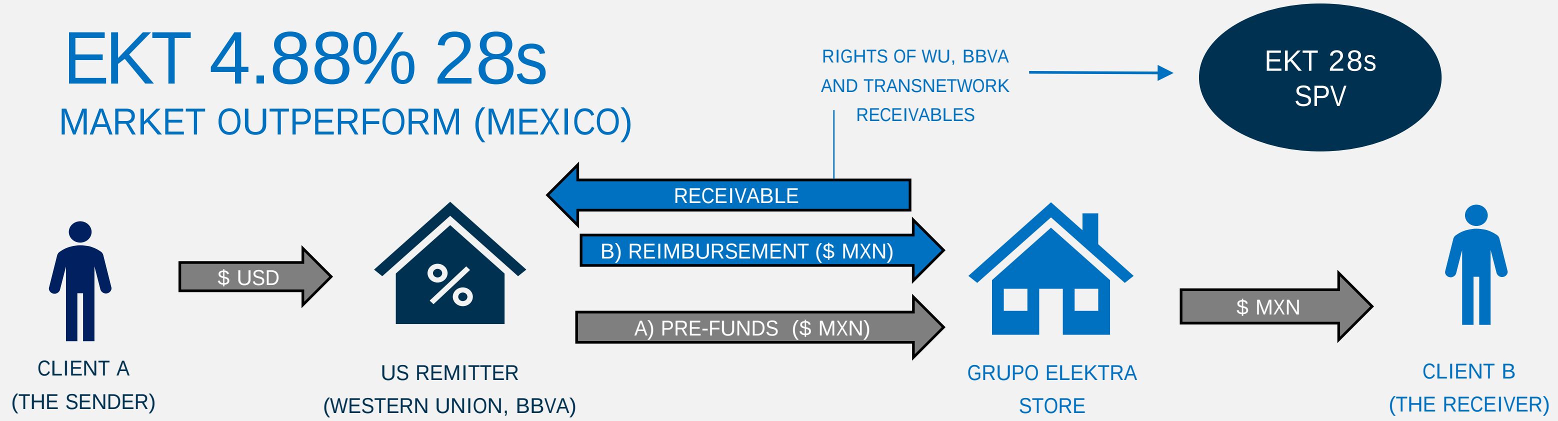
MARKET OUTPERFORM (MEXICO)



How the Remittance Business Works:

1. Client A walks into a remitter location in the US
2. The remitter determines the services fee and exchange rate
3. Client A makes the payment in USD to the remitter
4. Client B walks into a Grupo Elektra store and collects the money in MXN

- NEM (Elektra's Money Transfer Business) has two methods to pay Client B:

A) Prefunding Model:

NEM pays Client B with funds already received by the US remitter

- The US Remitter transfers in advance an estimate of funds to be used
- Around 42% of remittances

B) Reimbursement Model:

NEM pays Client B with its own funds and is later reimbursed by the US remitter

- The US remitter reimburses NEM on the following business day
- The rights on the receivables owed by Western Union, BBVA Transfer Service and Transnetwork are transferred to EKT 28s SPV
- Hence, the collateral are the full reimbursements from the three MTOs
- As of February 2022, the reimbursements / eligible collections were US$1 bn
- Resulting on a monthly debt service coverage of 93.2x
  - Well above the minimum required of 10.0x

In the Event of Default

- If NEM or Grupo Elektra were declared insolvent or in reorganization, it would trigger a cross-default with EKT bonds
- The B) Reimbursement Model will continue to operate
- The bonds' SPV has the rights on the eligible receivables and cannot be transferred to NEM
- NEM would pay Client B with its own funds using the credit line granted by Banco Azteca (does not have a specified amount)
- NEM still holds the obligation to pay the receiver, despite the rights on the eligible receivables being transferred to the SPV
- Considering February's monthly eligible collections, NEM would be able to paydown the bonds in full within two to three weeks

Additional Comments

- When Elektra uses the A) Prefunding Model, the funds flow directly to NEM
- We note the eligible collections exclude any commission, fee or other consideration payable to NEM
  - The commissions earned using either model flow directly to NEM
- If LTM eligible collections decrease by 60% y/y and the monthly debt service coverage is less than 15.0x, it would trigger an event of default

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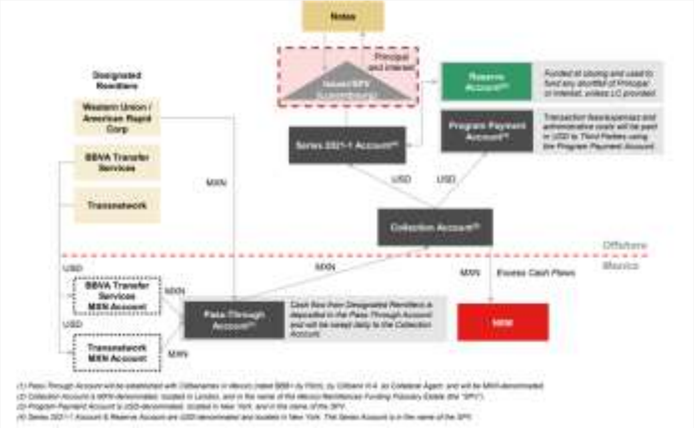
MARKET OUTPERFORM (MEXICO)

<u>How the SPV Structure Works:</u>

- It is applicable to the 2) Reimbursement Model

1. The eligible collections are deposited in the "Pass-through Account", held by the collateral agent (Citibanamex) in Mexico
    - The pass-though account cannot be changed by contract
    - If NEM wants to change the contract, they need prior approval from the bondholders
2. On each business day, the eligible collections are passed on to the "Collection Account" held in London
3. The collateral agent converts the funds into USD and transfers the funds to the Series 2021-1 Account held in New York
    - As well as paying the related maintenance fees and expenses
4. The Series 2021-1 Account pays EKT bonds interest
    - The DSRA will include the next amortization payment once it starts amortizing
    - EKT 28s will start amortizing US$25 mm every quarter starting on April 2023
6. Any excess cash flows are then transferred to NEM



<u>EKT 4.88% 1/15/2028</u>

- In 1Q21, NEM issued the 4.88% US$500 mm secured notes due in 2028 through an SPV
- Given the structure, the bonds were initially rate BBB-, a 1 notch uplift vs Grupo Elektra's corporate rating at BB+
- The bonds are secured by US remittance eligible reimbursements and guaranteed by the Holdco (Grupo Elektra)
- The Holdco's total debt is mainly comprised by local CEBURES (45%), followed by leases (27%), the USD bond (22%) and bank loans (5%)
    - We note local CEBURES are unsecured and structurally subordinated to the bonds
- The SPV should comply with a debt service coverage ratio of at least 10.0x
    - As of February 2022, the monthly debt service coverage ratio was 93.2x
    - The full monthly "reimbursements" that flow through the structure are eligible funds to pay the bonds

EKT (US MM) 2021	January	February	March	April	May	June	July	August	September	October	November	December
2021- Total Eligible Collections USD		763	1,068	969	1,013	1,146	1,025	1,129	1,023	1,055	1,147	1,154
Monthly Debt Service Coverage Ratio		73.6x	103.0x	93.5x	97.8x	110.6x	98.9	108.9x	108.9x	101.8x	110.7x	111.4x
2022 - Total Eligible Collections	964	966										
Monthly Debt Service Coverage Ratio	93.0x	93.2x										