Rassini Business Update Call

Eugenio Madero, Chief Executive Officer
November 15, 2016
10:30 a.m. Mexico City Time

Operator: Good morning and welcome to Rassini's business update call. At this time all participants are in a listen only mode. Following prepared remarks there will be 20 minute quick question and answer session. Please note that this conference is being recorded. If you have any questions or would like to reach the Rassini investor relations team please send an email to rassini@rassini.com.

With that, I will now turn the call over to Eugenio Madero, Chief Executive Officer of Rassini. Please go ahead sir.

Eugenio Madero: Good morning everybody, sorry for the delay we had technical difficulties somewhere in the bridge. Thank you operator. With me today, our company two people in investor relationships Emma Bocanegra and Edgar Landeros and I would like to begin.

Over the past year we have received many questions about what the 2016 U.S. presidential election would mean for Rassini. Now that election is over and Donald Trump has been elected, many of you have asked what does this mean for the Rassini team? What effect will Trump administration have on the U.S./Mexico trade relations? Will president elect Trump attempt to renegotiate NAFTA?

First and foremost I would like to say that we had a strong and profitable business in the United States for quite some time. We're confident that this will continue to be the case as we have said to many of you before. We have a very optimistic view of Rassini's continued growth and the future of the automotive industry in North America, and this includes a deep and abiding relationship between the United States and Mexico.

We have very successful operations in our three facilities in Ohio and Michigan which enable us to provide products for U.S. automotive customers including GM, Ford, Fiat-Chrysler and closely integrate with them on research, design, innovation and the engineering operations. We also source currently more than $125 million of goods annually from the United States which range from steel to utilities and others to support our Mexico based operations. We remain committed to maintaining our strong presence in the United States through our U.S.-based operations.

One of the biggest questions we have received in the past week is how president elect Trump's policies are expected to impact NAFTA. We have been very active the past 15 months in conversations around this issue and we have engaged vigorous members of the U.S. Congress and Senate, the USDR and other U.S. and Mexican trade related governments. So we have, we are very active that's the point OK. And we also have contacted over 10 leading think tanks in Washington and other different business groups and we will continue to do so.

On the subject of NAFTA, I would like to share with you the following points. First, NAFTA is a not a one way street for the United States or Mexico. Continued strong relationships within our countries are in the best interest of both sides. In fact probably 90 percent of all the U.S. Fortune 500 companies have investments in Mexico. That's a lot. More than half of the trade between our countries takes the form of intra company transfers of parts, components and raw materials creating a sophisticated supply chain operation which if disrupted would impact business operations in both countries.

Mexico is the second largest destination of exports for the U.S., a destination for U.S. exports behind Canada. Between the border of Mexico and the United States we have over 57 crossings and every day 1 million people cross the border by foot and over half a million vehicles which transport in goods and people as well. Trade between the U.S. and Mexico has risen almost 400 percent since the inception of NAFTA. By the way, also most of the major states of the United States have Mexico as their first or second trading partner and over 6 million jobs in the United States are dependent in trade with Mexico.

Although president elect Trump has commented that he may end NAFTA, we believe this is highly unlikely. However in the event that NAFTA were to be repealed, Mexico would revert back to its most favored nation status as we did before NAFTA. The implications of this for commerce will be a matter of tariffs and for the auto industry the highest tariff could be charged according to World Trade Organization is 2.5 percent. In the unlikely event that this event will occur, we believe this would cost – this cost will eventually be passed to the end customer.

Some people have the idea that president elect Trump might even encourage the United States to leave the World Trade Organization. That is something that the president alone cannot decide and instead will require congressional support. We are confident that the newly elected republican Congress will remain focused on trade partners and will recognize that leaving the WTO will reduce the credibility of the United States as well as the strength in the world of commerce. We consider this to be something that will be very hard to accomplish.

Rassini's long term investment in the U.S. market is grounded in the belief that leaders in all three countries understand and remain committed to the unique economic and diplomatic partnership between our nations. We will not speculate on how the U.S. trade policies would evolve under the president elect Trump administration and a republican Congress. However, we remain optimistic that the United States and Mexico will encourage to engage in a relationship that benefits both our economies and which helps all three partners including Canada to compete globally.

In closing, I will emphasize again that we're confident that we will continue to benefit from strong business and trade relations with the United States. Independent of any particular administration in the coming months, we will watch the development of trade policies as we always do and ensure our business is best positioned to continue to succeed in this evolving political and economic landscape. We have a long story of responding quickly to our customers' needs and being flexible in what and where we produce to meet our customers' changing needs. We will apply this same flexibility and responsiveness to our business as a whole as the political landscape continues to evolve.

I would just like to close with some macroeconomic points. And as you know last October the SAR closed at 17.9 million vehicles being sold. We're very confident in employment of less than five percent in the United States. Also the new housing continues to grow and we see the United States being economically independent on 10 million barrels of oil per day which is the same as Saudi Arabia.

I think for Rassini we have had a record quarter. We have one of our strongest positions in cash year to date over $80 million, our net debt to EBITDA ratio is one of our lowest in our history at 0.40 and our interest coverage ratio is 10 times. With that, I'm happy to open to any questions operator. Thank you very much.

Operator: [OPERATOR INSTRUCTIONS] Your first question comes from the line of Hector Vasquez.

Eugenio Madero: Hello Hector, good morning.

Hector Vasquez: Good morning is what could we expect as a net impact if a tariff is imposed and if the company faces decreasing taxes. Is the company still being competitive against other auto parts producers?

Eugenio Madero: I have no answer to that because it's not in my scenario right now and I would not go ahead and answer it before there's any particular change in tariffs or laws. So I just do not have any information to answer that. But we see the company is profitable under any scenario.

Hector Vasquez: OK perfect. Thank you very much.

Operator: We have a question from the line of Pablo Carrillo.

Pablo Carrillo: Yes, hi. Hector already asked my question so thank you.

Eugenio Madero: Thank you Pablo.

Operator: You have a question from the line of Nicolas Prado.

Nicolas Prado: Just a quick question on use of cash generation. The company right now has a pretty strong balance sheet and considering how much shares have come down since the U.S. election, have you considered or discussed a share buyback program as another way of returning cash to shareholders and take advantage of the particularly favorable valuation level of your shares?

Eugenio Madero: The answer is no Nicolas.

Nicolas Prado: And would it be something that you would consider I mean in besides the distribution of dividends?

Eugenio Madero: No, we will not and we don't even have a stock repurchase program approved by the board of directors.

Nicolas Prado: OK, thank you very much.

Operator: You have a question from the line of Jose Vasquez.

Jose Vasquez: My question is quick. The 2.5 percent tariff that you mentioned is per unit or what? This will impose for the total value of the car or which would be the rationale behind this tariff? Thank you.

Eugenio Madero: I will comment on the best of my ability on the knowledge that I have today but what it would mean exactly is that if you have ceiling because of the World Trade Organization we are a member country, so if they were able to want to impose tariffs I think they would put like a maximum of 2.5 percent I guess in whatever we ship to our end customer. But some, most of what we do deliver over 68 percent of what we sell is point of delivery at the plant and the customer and the customer takes it from there. So I think they would be most probably the customer will have to be dealing with that directly more than Rassini itself.

Jose Vasquez: OK, perfect. Thank you.

Operator: You have a question from the line of Pablo Liman.

Pablo Limon: Hi, good morning Eugenio and the rest of the team. Thanks for the call, very helpful. If you're able to maintain your business as usual but assuming that the FX remains up over 20 pesos, where would you expect Rassini's margins to go for the next three years? I'm expecting you should see a benefit in profitability, is that correct?

Eugenio Madero: Pablo can you please repeat your question again? I heard about the 20 pesos and the rest kind of was (inaudible). Can you repeat your question?

Pablo Limon: Assuming that the FX remains about let's say about 20 pesos, where would you expect Rassini's margins to go for the next three to four years? Do you see a – are you expecting a benefit in profitability?

Eugenio Madero: I'm not, I will try to answer it in the best of my ability and again your question was kind of broken up. But I think Rassini has always been working for the customer independent of the exchange rate. Sometimes, most of the time we have it against us. I think at this point if you look at today, for us we don't like also exchange rate to be as high, we also from some of the things that we are put in our products also come are in dollar terms even though we serve in dollar terms but extremes are not good.

Now for if I understood the second part of your question I think it was on profit for the next three years. Is that correct?

Pablo Limon: Yes. Let's assume EBITDA margin now what level, what level do you feel comfortable guiding for the next three to four years?

Eugenio Madero: Usually we don't go ahead so far you know this kind of conversation but we would expect our EBITDA to remain stable around 18 percent depending on Rassini, you know.

Pablo Limon: OK, that's good enough. Thank you very much.

Operator: You have a question from the line of Ingrid Costillo.

Ingrid Costillo: Hi good morning, thank you for the call. Some of the concerns that we've been getting from clients is that if there is any way that the contracts or the fine prints that you have with, in the contracts with your clients allows them to force you to switch production capacity from Mexico to the United States. Is that a possibility? Is that something that can actually be done or do the contracts actually guard you guys for you know the question now on where to assemble your products?

Eugenio Madero: Ingrid thank you for your question, I think it's an excellent question. I think the answer is no. When we have an offer and purchase order we produce where we want. The small print doesn't tell you that we have to switch countries in production to do this. As I mentioned at the beginning of our phone calls, we have plans not only in the Unites States, Mexico and Brazil.

So we have been producing in the United States for over 12 years and our second plant came into production about two and half years ago. But we're not – our customers don't require us to change production in the middle of the contract. But thank you for your excellent question Ingrid.

Ingrid Costillo: Perfect, thank you. Could I just do a follow up, actually another question that was asked before? In terms of your buybacks, buybacks is not a priority in terms of use of cash. What would be your priority in terms of use of cash going forward? Would it be to hold cash in you know in a defensive way in terms of risk or would you like to make further investments, diversify your portfolio? How could we look at that? Thank you.

Eugenio Madero: I think the least important for us is using cash to repurchase stock. I think that's the farthest it can be. I think for us it's always constantly to study opportunities as they appear and be you know ready. And if that were to be the case that would be a proper use of cash or adjust the current CAPEX. Thank you, Ingrid.

Ingrid Costillo: OK, thank you.

Operator: You have a question from the line of Bernhard Aubin.

Bernhard Aubin: Hi, I have two questions actually. First question relates to the facilities in the U.S., what is their share of production of the total of Rassini and by how much could it be expanded? And the second question relates to the tariffs. If tariffs were introduced how long would it take to pass it on to the end customers?

Eugenio Madero: Your first part of the question was capacity in the United States?

Bernhard Aubin: Yes, how much is the capacity in the United States as a total of Rassini's capacity?

Eugenio Madero: All right, well very well. On capacity in the United States it's less than 11 percent of our total revenues. Yes it could be expanded but we're not looking for it at this point. It depends on the products. And the second question was on the tariffs how quickly, that I do not know.

Bernhard Aubin: OK, thank you.

Operator: You have a question from the line of Fernando Ramos.

Fernando Ramos: Hi, thank you very much for the conference. I think it's very important to be close to investors at this time. My questions have already been answered but now that you're on the line can you walk us a little bit where we are right now in the cycle and what do you expect for next year?

Eugenio Madero: Fernando thank you, good morning. Excellent question. The cycle, well you know I think as we have read a lot I think the sales most of the past year have reached many people in the industry like a healthy drop, OK. We will expect of revenues and production to remain at 18.5. This is being supported on I think, what we see the health of the U.S. economy.

You have also heard a lot of the reports over the last two to three months that crossover vehicles, sport utilities, minivans, pickups and light trucks in general have been selling better than cars, around seven percent better than cars and the cars the small cars have dropped in sales. You have also heard comments like the Toyota, from the Toyota company saying the Toyota Prius which is a hybrid car is selling 60,000 less cars because they see themselves in Toyota that sport utility vehicles, crossovers and pickups are being the choice of the customers currently. So I will like to tell you that we feel (inaudible) robust and confident as we are. We are not going to see the growth of the double digit that Mary Barra from GM has said or the industry in general. I think those times that we were coming back in 2008 to where we are now I think we're going to see growth between two percent yearly.

Fernando Ramos: Thank you.

Operator: You have a question from the line of Nicolas Prado. Your line is open.

Nicolas Prado: Yes hi, hello it's me again. Forgive me for insisting on this point but I would just like to understand why is the company not considering share buybacks considering the current valuation? It's a matter of alignment of interests with shareholders. How do you expect investors to buy your shares if the company itself which is you know management and controlling shareholders and board members who are the ones who know the asset as best as they can are not doing it? Whatever you buy in terms of M&A, in terms of other assets is probably going to be more expensive than where your shares are trading right now.

So more – it's rather than a question it's more of a comment and a request for you to discuss this internally because it makes absolutely no sense for you not to be discussing this internally right now. It's really best practice and common sense. So please reconsider the use of your cash to repurchase your shares.

Eugenio Madero: Nicolas, thank you again for your comment. I think you have a good comment. We'll study it and if there's a change we'll comment later. But I think as you see the stock, I think the whole world is preoccupied with the president elect Donald Trump is not alone himself.

President Obama today is currently in Greece, he's also approaching the European partners. They are holding dearly for the whole Pax Americana for those meetings from the NATO Alliance, China. We're not alone, everybody is in the same boat. So you see the peso exchange rate some stocks having dropped more like ours. I think ours dropped the first day 11 percent then seven and then the past two days they have been going north. So we will consider what you said and again thank you for that comment.

Operator: You have a question from the line of Fernando Rivera.

Fernando Rivera: Yes, hi. So the question is on NAFTA. So you mentioned the possible 2.5 percent increase on tariffs which on surface doesn't, that doesn't seem as terribly bad. You know beyond the 2.5 percent what are – what are the things that you see as you know risky in relation to the repeal of NAFTA? Kind of beyond that 2.5 percent what do you see in the overall environment that would be impacting Rassini?

Eugenio Madero: Well, we have studied this a lot. I think NAFTA had been already for 25 years. I think there's, there have been labor mobility in the United States. More in the case of Mexico there's more energy, more openness. I think Rassini has is able today more than 25 years ago to have more utilities from not only importing raw materials from the United States but also utilities.

What I know now, you know I think we're a net exporter. I don't see other things, people have not – people who are experts in this subject have not told me anything else at this point that I can tell you more than what I already spoke here today.

Operator: You have a question from the line of Alejandro Azar.

Alejandro Azar: Hi, everyone and thank you for taking my question. Regarding the tariffs or any increases, if the three percent will not go directly to the consumer if Rassini would take part on that, is there any competition in the U.S. that would take the production or in terms of would any competitor would be more efficient than you guys making those parts? Are there any capacity left to cover those products with lower cost? Thank you.

Eugenio Madero: OK, thank you. I understand your question is if there's like a threat of competitors in the United States that could take market share of this away from Rassini? Yes, in many of the things that we do currently either we're the number one or the number two supplier or producer of these goods. In most of these goods we also have very high market shares. So I don't at this point I would not expect other people to come in and do a change in the short term, middle term.

I think over the next 12 months I will not expect any quick change on these customers switching from Rassini to other people because of this. And I repeat, we do have a good market share in the products. The customers appreciate the quality, the service, the engineering of the product. So the replacing the product is not just as simple as that you know. But we are always we today and the past 15 years we're always looking at possible competitors anywhere and we're always studying where we think their costs are, where are they sourcing the materials, their labor, the utilities. So this something that independent of this thing that's happening here today, we are always studying who and where and what and why and how could a competitor threaten Rassini's market share.

Alejandro Azar: OK, thank you.

Eugenio Madero: In this continent and all others, OK from Asia everywhere.

Alejandro Azar: OK, thank you.

Operator: You have a question from the line of Luciano Bayo.

Luciano Bayo: Yes, hello. Thanks Eugenio for the call. Actually my question was kind of the same that was asked before in terms of capacity in the U.S. and if you – so a quick follow up on that. Assuming your contracts are they have a maturity averaging four, five, six years.

Would you consider then moving your capacity or expanding your capacity in the U.S. in our scenario where you know Donald Trump dissolves NAFTA or impose really tough tariffs on Mexico? And how long would it take to you to build the capacity to attend the U.S. market from the U.S. market? Thank you.

Eugenio Madero: All right, thank you. Excellent question Luciano. I think we're not considering at this time, number one. Number two, I think we have proven that we're very successful manufacturers anywhere and in particular in the United States we have a plant in Ohio that has been there for more than 40 years and we source products from raw materials locally. I think to build a new plant it takes more than a year and a half. I think we will not be considering at this point to open more U.S. plants at this point unless things change and we will evaluate it at that point and not before.

Luciano Bayo: Thank you.

Operator: And we do have time for one more question. You have a question from the line of Roberto Lampl.

Roberto Lampl: Hi there, good afternoon. Thank you for the call. A couple of questions, the first one is if you can disclose a bit about the you were talking about the intra trade between Mexico and the U.S. Within the contents, within your production in Mexico how much is U.S. content that you then you know can create a finished product and re-export – and export back to the U.S. if you can you know give us some disclosure on that?

Eugenio Madero: I will tell you that I will try to answer the question at the best of my ability. But once we produce a product we ship it. And what might happen is that a customer might get it in the United States and send it back across the border basically an average of a couple of three times.

In our paper example, we do import some raw materials in the case of our plant in Piedras Negras Mexico. Pemex have never sourced a molecule of gas there for the past 35 years so there's not a pipeline of Pemex that brings the gas molecule to Piedras Negras where we are. So we have always been importing from companies in the Houston ship channel. So I guess that would be like a border crossing. You're crossing energy to produce a product and then we ship it.

So there are several things that – we bring some steel from Wisconsin, we bring some steel from Nebraska so that's what I mean. People you know we bring some steel from Canada so that's the thing I would say. For us is more of the building the product, once it's finished we ship it.

Roberto Lampl: So if I can ask it a different way, from your supply chain content how much is imported cost versus cost that is you know is generated and domiciled from Mexico or originates from Mexico?

Eugenio Madero: I think we'll give you like an average. More or less between 60 percent import. Between 50 and 60 percent.

Roberto Lampl: OK.

Eugenio Madero: Between 50 and 60.

Roberto Lampl: Right. And the overall duration of your contracts what does that look like at the moment of the platforms that you're supporting?

Eugenio Madero: Just on the tail end of the last question, I think this is the whole purpose of NAFTA. NAFTA was built as helping North American productivity in integrated supply chain. That is just not the case for Rassini, the bigger you go the more integration there is. So if you go to our end customers they're very invested in Mexico and for them you know it's part of their supply chain.

When you go to most of the companies that we supply to they have a person called North American operations and they don't see the plants in Mexico as Mexican plants, they see them as part of their North American operations. They will see the Chinese plants as Chinese plants or European plants or Brazilian, South American plants. But Mexico for them is no longer a country, it's a part of their North American integration of the chain.

Our contracts I think we have is called open purchase orders which you know they never give you a definitive amount of volume but every 60, 90 days they'll give you the release of how much are they going to be producing. So most of the products that we sell to usually the best-selling line for products to our customers like if I mention pickup trucks as I said before they are like seven percent above market on the sales. And so you know it is not that they will cancel a contract. Actually we just have received for the past two years over $248 million of new purchase orders, real new purchase orders on the life of this contract. So we're very firm and solid on this, no surprises at this point.

Roberto Lampl: OK.

Eugenio Madero: And this industry is very linear so when they plan they plan long time ahead. They don't do changes every three months. They don't cancel a contract every three months or they don't – we have never had a contract cancelled.

Roberto Lampl: Super, great. And probably my last follow up question then, how have your customers, your partners in the U.S. been reacting? Have they joined you in this lobbying effort and consultation effort with congressmen and so forth that you mentioned at the beginning?

Eugenio Madero: On the past 15 months when the TPT was beginning we decided to actively participate and do that on the back room and we participated with U.S. authorities, Mexican authorities because it was in our interest. So we went from the USDR in Washington which is reports to the White House, we went to the secretary of economy in Mexico, we talked to – we've talked to people from the states who participated in the United States like Ohio and Michigan. We went to all you know what these congress people the staffers and the senators and staffers again what this meant and I think they saw the big picture, OK.

With our customers I think they have decided at this point to act internally but to be quiet on the outside because I think some of these things are better to work behind scenes and quiet than being public and frontal. You know what I mean? Sometimes being public and frontal is very defiant and if you work on the on silence it's you're better off.

We have also influenced a lot on more than 10 think tanks like the Hudson, Harry Touch, Cado and many others. So again we have been participating on this. We have approached also the business roundtable in Washington which is a confederation of companies. So I think you know we have been hearing and talking but on the people that we think are the people that can participate better than Rassini in U.S. policy.

Operator: This will end our Q&A session. Mr. Madero, do you have any closing remarks?

Eugenio Madero: I appreciate all of your participation. I think you very much for it. I think at this point you know we don't have anything else to add, we appreciate your time. Thank you very much.

Operator: This concludes today's conference. You may now disconnect.

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