



Ternium S.A. (TX)

Updated August 3rd, 2022 by Quinn Mohammed

Key Metrics

Current Price:	\$34	5 Year CAGR Estimate:	7.7%	Market Cap:	\$6.7 B
Fair Value Price:	\$84	5 Year Growth Estimate:	-15.0%	Ex-Dividend Date:	05/05/2023
% Fair Value:	40%	5 Year Valuation Multiple Estimate:	20.0%	Dividend Payment Date:	05/11/2023
Dividend Yield:	5.3%	5 Year Price Target	\$37	Years Of Dividend Growth:	0
Dividend Risk Score:	C	Retirement Suitability Score:	B	Rating:	Hold

Overview & Current Events

Ternium is the leading flat steel producer in Latin America, and has operating facilities in Mexico, Brazil, Argentina, Colombia, the southern U.S., and Central America. The company's steel products are sold to customers in the automotive, home appliances, HVAC, construction, capital goods, container, food, and energy industries. The company operates a fully-integrated production system, from the mining of iron ore to the manufacturing process of steelmaking and producing high value added products. Ternium S.A. trades on the NYSE under the ticker symbol TX as an American Depository Share (ADS). Ternium has a market capitalization of \$6.7 billion. TX has roughly 20,000 employees.

On August 2nd, Ternium released second quarter 2022 results for the period ending June 30th, 2022. Ternium's steel shipment fell 4% over Q2 2021 to 2.957 million tons. Iron ore shipments also fell by 8% compared to the previous year, to 837 thousand tons. The company achieved net sales of \$4.4 billion, a 13% increase over 2021's \$3.9 billion. Operating income decreased 16% to \$1.07 billion. Adjusted EBITDA of \$1.2 billion resulted in an adjusted EBITDA margin of 28%, much lower than the prior year's 36%. Adjusted EBITDA per ton was down from \$463 million in the prior year to \$414 million in Q2 2022. Earnings per ADS of \$4.07 was a 22% decrease over the prior year's \$5.21 per ADS.

Leadership anticipates continued solid performance in 2022, however steel prices are decreasing significantly now. Costs for the steel industry had increased following the Russian invasion of Ukraine, which had previously caused a surge in steel prices. However, steel prices are now unwinding.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$0.72	\$2.32	(\$1.01)	\$0.04	\$3.03	\$4.51	\$7.67	\$2.87	\$3.97	\$19.49	\$12.95	\$6.83
DPS	\$0.75	\$0.65	\$0.75	\$0.90	\$0.90	\$1.00	\$1.10	\$1.20	\$0.00	\$2.90	\$1.80	\$2.77
Shares¹	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.0

Ternium's results have been cyclical, so earnings have been bumpy over the past decade, but the company has remained healthy overall over this time period. Increased demand for steel products has put TX in a good spot, as it set record 2021 earnings per ADS of \$19.49. Given the cyclicity of TX's earnings, certain year-over-year comparisons can be heavily skewed. Even so, over the last nine and five years on average, TX has produced earnings growth of 44% and 45% annually, respectively. Since the company is expected to report very strong results in comparison to its historic average, we believe earnings will shrink by about 15% from these cyclical highs.

Ternium can grow its earnings by increased production through ramping up existing facilities or investing in new ones. Additionally, the increased demand and limited supply of steel products has caused a massive increase in the steel prices. Margin improvements across the vertically-integrated business could also boost the bottom line. The company has maintained its number of outstanding shares over the last decade quite steadily.

¹ In millions

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	10.0	50.0	11.6	15.3	50.0	7.1	6.4	3.8	13.1	5.9	2.6	6.5
Avg. Yld.	6.1%	4.1%	2.8%	5.3%	4.9%	3.5%	3.3%	5.1%	2.7%	3.5%	5.3%	7.4%

Given the strong outperformance for TX's earnings in 2022, the company has come to trade at a price-to-earnings ratio of 2.6, extremely below its average, even when excluding the 2013 and 2016 outliers. We estimate the company's fair value to be at roughly 6.5 times earnings. This would result in massive valuation gains of 20%, which will be offset by the estimated decline in earnings out to 2027. The company's yield is above the average 4.1%. To note, Ternium pays an annual dividend, considerably less frequent than the quarterly dividend most companies pay.

Safety, Quality, Competitive Advantage, & Recession Resiliency

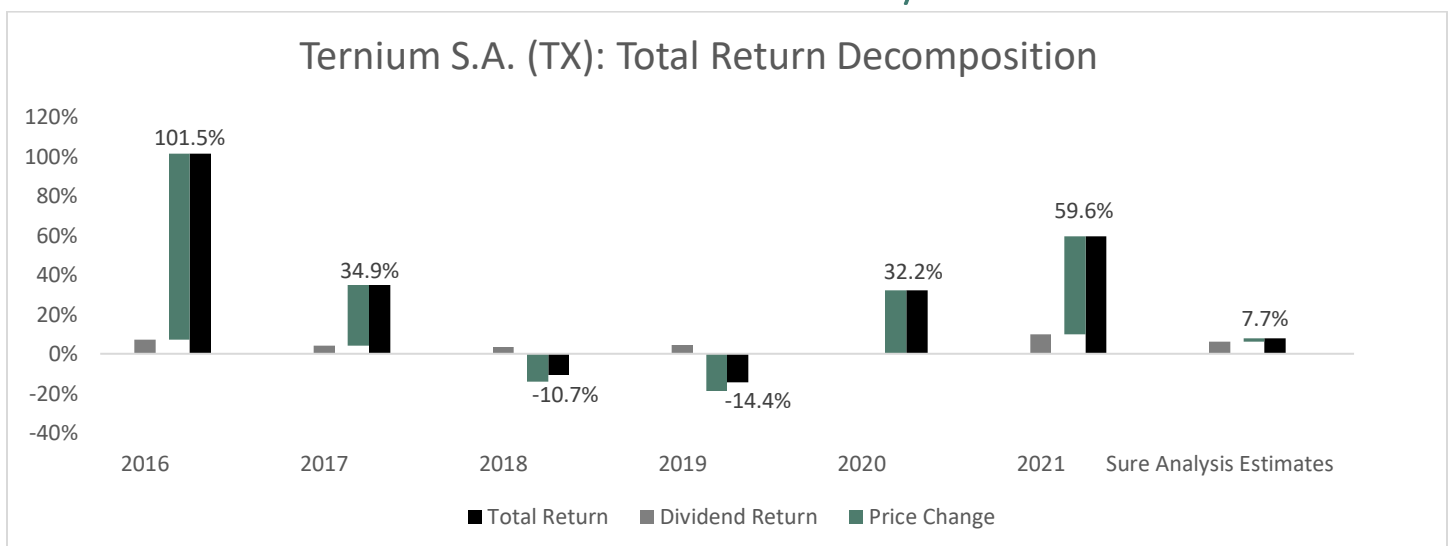
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	104%	28%	-74%	-	30%	22%	14%	42%	0%	15%	14%	48%

The cyclical nature of the company has shone through in the payout ratio where in at least three years out of the past decade, the company could not cover the dividend with earnings. The company did not pay a dividend in 2020 amidst the COVID-19 pandemic, but then paid a dividend in 2021 which was nearly double the size of the 2019 dividend. The company had no net debt at the end of the quarter. The lack of leverage reduces the risk profile of the company, but we don't believe them to be recession resistant given a decrease in demand for their steel products would hit the company. Ternium's Mexican facilities have logistical advantages within the Gulf Coast and a large portion of the West Coast. Additionally, TX's value-added services, including technical assistance related to steel use and production, and development of new steel products, is a competitive advantage.

Final Thoughts & Recommendation

Ternium is a highly cyclical company dependent on the demand and pricing of steel. Today the company appears to be on a downtrend from its cyclical top. We estimate a 15% decrease in earnings over the intermediate term. Combined with the 5.3% yield and estimated 20.0% in annual valuation expansion, we estimate total annualized returns of 7.7% and rate TX as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	8,608	8,530	8,726	7,877	7,224	9,700	11,455	10,193	8,735	16,091
Gross Profit	1,742	1,930	1,801	1,400	1,840	2,297	2,971	1,740	1,636	6,196
Gross Margin	20.2%	22.6%	20.6%	17.8%	25.5%	23.7%	25.9%	17.1%	18.7%	38.5%
SG&A Exp.	634	641	627	586	542	629	668	654	572	729
Depr. & Amort.	371	377	415	434	407	474	589	661	631	592
Operating Profit	921	1109	1,056	639	1,142	1,457	2,108	865	1,079	5,271
Operating Margin	10.7%	13.0%	12.1%	8.1%	15.8%	15.0%	18.4%	8.5%	12.4%	32.8%
Net Profit	142	455	-199	8	596	886	1,507	564	778	3,825
Net Margin	1.7%	5.3%	-2.3%	0.1%	8.2%	9.1%	13.2%	5.5%	8.9%	23.8%
Free Cash Flow	33	209	62	857	664	-26	1,219	595	1,201	2,154
Income Tax	261	349	339	207	412	337	369	197	291	1,397

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	10,867	10,373	9,690	8,063	8,323	12,123	12,548	12,936	12,856	17,098
Cash & Equivalents	559	306	213	151	183	338	248	520	538	1,277
Accounts Receivable	735	671	720	511	634	1,007	1,128	950	918	1,767
Inventories	2,000	1,941	2,134	1,579	1,648	2,551	2,690	2,158	2,002	3,908
Goodwill & Intang.	887	1,057	845	787	740	988	913	820	770	750
Total Liabilities	4,432	4,035	4,055	3,260	3,156	6,270	5,063	5,221	4,413	4,863
Accounts Payable	762	756	565	568	603	898	904	877	1,049	1,126
Long-Term Debt	2,424	2,003	2,165	1,521	1,219	3,222	2,037	2,189	1,723	1,479
Shareholder's Equity	5,369	5,340	4,697	4,033	4,391	5,010	6,393	6,612	7,286	10,535
LTD/E Ratio	0.45	0.38	0.46	0.38	0.28	0.64	0.32	0.33	0.24	0.14

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	1.3%	4.3%	-2.0%	0.1%	7.3%	8.7%	12.2%	4.4%	6.0%	25.5%
Return on Equity	2.6%	8.5%	-4.0%	0.2%	14.1%	18.9%	26.4%	8.7%	11.2%	42.9%
ROIC	1.6%	5.3%	-2.5%	0.1%	9.4%	11.5%	16.2%	5.8%	7.8%	32.0%
Shares Out.	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.3	196.3
Revenue/Share	43.85	43.45	44.45	40.13	36.80	49.41	58.35	51.92	44.50	81.97
FCF/Share	0.17	1.06	0.32	4.36	3.38	-0.13	6.21	3.03	6.12	10.97

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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