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Mexican Real Estate

The best of times and the worst of times

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The best of times and the worst of times…

Mexico's real estate stocks are living an unusual moment. On the one hand, the sector has enjoyed quite a material rally and re-rating in 2019 (admittedly from valuation levels that hollowed out by the end of 2018). On the other, they are hounded by concerns on the outlook for the global and Mexican economies, rising protectionism, and long-term risks arising from e-commerce, automation, and the advent of electric vehicles. The sector continues to grapple with own foibles and risks with regards to corporate structure and governance, but we believe that, given still discounted valuations, these are somewhat in check. This report parses through all these risks and opportunities to provide an updated view on the sector.

Mexican real estate remains one of our preferred sectors, particularly industrial

A sector's valuation re-rating would normally be a cause for pause and a reason to reconsider past optimism. For Mexican real estate, however, the recent rally validates the view that valuations had reached levels that were simply too deeply discounted to be ignored by investors. Though significant uncertainties regarding global trade and Mexico's economy remain in place, many of the catalysts that have prompted the rally are also present in the form of declining global and domestic interest rates and the ensuing hunt for quality yield. Moreover, the industrial real estate segment offers exposure to what we see as the secular trend of Mexico entrenching itself as the workshop of North America and, in some industries, of the world.

Valuation is still at the heart of the investment case

In spite of the YTD rally, we believe that the valuation of Mexican real estate assets remains compelling. Our expanded nine-company sample (which includes seven FIBRAs and two C-Corps) trades at a P/NAV of 0.79x and implied cap rate of 8.8%, representing a spread over applicable sovereign yields of 460bps, arguably the highest in the world; the dividend paying FIBRAs yield 8.2% on average. Our DDM models for FIBRAs and DDM+Exit Cap Rate valuation exercise for C-Corps yield sufficient upside for six of the nine stocks under coverage to be rated Buys.

Buy on Vesta, Fibra MQ, and FUNO; downgrading Terra and FSHOP to Neutral

Of the stocks that we are reviewing, we eiterate our Buy ratings for Vesta (which is included in our Mexico 5SIM portfolio), Fibra MQ (our preferred FIBRA), and FUNO (still the sector's benchmark). Terra and FSHOP are downgraded to Neutral owing to an assumption in our DDMs that now stabilizes all FIBRA LTVs at 35% in 2023 in an effort to make them more comparable and to settle their balance sheets with leverage that is consistent with a prudent mid-cycle positioning. For both FSHOP and Terra this implies a reduction in the payout that would reduce their 42% and 41% LTVs to 35% by 2023, decreasing PTs to levels consistent with a Neutral rating.

Initiating Fibra PL, Danhos, and Fibra Monterrey as Buys; Planigrupo Neutral

We are expanding our Mexican real estate sample to nine stocks in this report with initiations on Fibra PL, Danhos, FMTY, and Plani. Though Fibra PL's valuations are at the higher end of the industrial spectrum, we believe this is justified by their sponsorship by Prologis and the exposure to Mexico's e-commerce growth implied by its expertise in logistics. Danhos, in spite of a premiere retail and office portfolio and bulletproof balance sheet, screens as one of the most attractively valued FIBRAs. FMTY's 9% dividend yield is the highest among USD earners and its internalized management platform sets it apart from its FIBRA peers, but low liquidity is an issue. Plani, which offers the only platform dedicated to mass market retail, and, as a C-Corp, also distinguishes itself, trades at valuations that seem fair relative to peers.

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The Best of Times and the Worst of Times....

"It was the best of times, it was the worst of times...It was the spring of hope, it was the winter of despair, we had everything before us, we had nothing before us, we were all going direct to Heaven, we were all going direct the other way..." - Charles Dickens in his introduction to A Tale of Two Cities

Considering Mexico's macro landscape, it would be difficult to imagine a more complex and uninspiring environment for owners and developers of real estate. Yet Mexico's FIBRA Index is up 35% YTD, with the industrial FIBRAs (Fibra MQ, Fibra PL, and Terrafina) all up on a total-return basis by over 43%. This is the best YTD FIBRA performance since inception. On the face of it, this contradiction doesn't seem to make much sense, but dig deeper and, in our view, this might be the best environment for investing in Mexican real estate securities since FUNO's IPO, which marked the birth of the sector in March 2011.

Let's start with the bad

Growth, which at an average of 2% for the past thirty years was hardly stellar to begin with, **is now forecast at close to a quarter of that** for 2019 and expectations of a rebound for 2020 are not especially hopeful. Following the much-maligned decision by then President-elect AMLO to cancel NAIM (Mexico City's formerly New Airport), **business confidence has plunged** and private investment slashed to a bare minimum. This has been exacerbated by the decision by the new **CDMX Government**, also from AMLO's Morena party, to suspend construction of dozens of ongoing real estate projects as it reviews their licenses, which has now gone on for months, contributing to the construction industry's dipping into recession and, many would argue, to the city's deteriorating crime statistics.

Banxico, in spite of having every cyclical reason to cut policy rates aggressively, has only recently and timidly begun to cut rates as external risks (i.e., US politics) and concerns around the possible fallout of domestic policy missteps are forcing it to keep front-end rates that are still the highest for any Investment Grade (IG) country in the world. And these same potential policy errors, including the *de facto* (if not *de jure*) suspension of Energy Reform, are leading to increasing concerns about the **potential loss of Mexico's IG rating**.

On the external front, **USMCA**, the recently negotiated replacement of NAFTA, has not yet been approved by the US Congress and, in spite of hopeful predictions by the Trump administration that it will be voted on by the House by year-end, seems, in our view, likely to gather dust until after the presidential election in November 2020. In the meantime, Mexico finds itself fully inserted (at an unusually early stage) into the US electoral process by the (for now) skirted threat by President Trump to slap **tariffs** on Mexico if its does not help to stem the flow of Central Americans migrants. And, though the **China-US trade war** should be positive for Mexico and its industrial real estate assets over the long-run, in the meantime it is contributing to anxiety over slowing growth globally.

Yet for all this monsoon of gloom there are just as many positives, perhaps even more of them

The global yield curve is shifting downwards, producing yet another global search for yield, which Mexican real estate assets offer in spades. Moreover, investors continue to anticipate additional FED cuts in 2019 and 2020, contributing further to this appetite for yield, which is likely eventualy to force Banxico's hand to cut policy rates more decidedly.

The uncertain outlook for growth discussed above has **dampened the appetite for development activity**, which is happening at what might be just the right time for retail, where there are some signs of oversupply or loose markets. For office, which is already oversupplied and bracing for additional inventory to hit the market through 2020, this is arguably happening too late. Fortunately, the office space is the least represented segment among publicly traded vehicles.

For the **industrial segment**, however, the drought in development activity happened much earlier, brought on by the ascent of Candidate Trump whose anti-Mexico and anti-trade vitriol spooked developers who, after the pain brought about by the Great Recession, were skeptical growers anyway. Though the on-the-ground dynamics in the industrial segment have done nothing but improve since then, these same "nervous Nellie" developers have been given reason after reason to stay put: Trump's surprise election, the onset of NAFTA negotiations, the ascent of Candidate AMLO, his landslide win, the cancellation of NAIM, Banxico tightening, plunging business confidence, the China-US a war, and the recent linkage by Trump of immigration and tariffs, to name a few. All of this has contributed not just to occupancies in stabilized portfolios **tightening** to levels above 95%, but also to **positive leasing spreads** in USD for the first time in many years.

Importantly, **the underlying macro gloom is also addressing**, at least temporarily, **many of the concerns around governance and potential misalignment of interests seemingly inherent to the FIBRA structure** that investors have long fretted over. The uncertainty pervading any investment decision is depressing the appetite for both development and acquisition, at least for now. Admittedly, if conditions continue to deteriorate there might be forced asset sales that could prove too attractive to ignore, but for now there seems to be little interest among FIBRA managements to allocate much capital towards growth. This reduces the risk, in our view, of capital misallocation, balance sheet overextension, and dilution.

In fact, more than just reducing the risk of capital misallocation, it might prompt some capital deployment decisions that could prove both accretive and balance sheet de-risking. For instance, more and more FIBRAs are directing some of their AFFO towards **CBFI repurchases**, which at this level of valuation is perhaps the best use of capital and will contribute to acceleration in per-CBFI metrics, including distributions. In other words, far from considering share issuance, which has been a major irritant for investors over the years, many FIBRAs are doing the opposite and have implemented buyback programs that have retired CBFIs at material discounts to NAV.

Similarly, the uncertainty on the macro front has prompted managements to seek to **de-risk their balance sheets** by reducing leverage and, where possible, improving debt maturity profiles. Part of this exercise has included **asset recycling** programs

that have led to the sale of assets (something that would have been previously unthinkable for many FIBRA managements), which has not only helped in improving balance sheets, but also in honing the focus and raising the quality of portfolios.

Finally, the lack of activity on the M&A front has refocused managements on extracting as much **value as possible from existing properties** rather than on simply growing their asset base. As such, maintenance, expansions, and brownfields have become the norm, which are a sure way to prolong the life of portfolios and of squeezing higher IRRs from an existing property base.

Underlying all of this, of course, is **valuation**, which while re-rating somewhat YTD, **remains heavily discounted on every metric**. Discounts to NAV still range in the 15–25% range, cap rate and yield spreads over risk free rates remain among the highest globally, and pricing relative to private transactions remain attractive, particularly on the industrial front.

We have therefore decided via this report to take stock of the industry, review the investment case for the five real estate names already under coverage (Fibra MQ, FSHOP, FUNO, Terrafina, and Vesta), round-out our sample by adding coverage of four more stocks (Danhos, Fibra PL, FMTY, and Planigrupo), and revise our rating system to, effectively, introduce somewhat of a forced ratings distribution on what is now a fuller sample of stocks.

With this in mind, we are reiterating our bullish view on Mexican real estate, particularly with regards to the industrial space, and maintain our Buy ratings on Vesta (currently part of our Mexico 5 SIM portfolio), Fibra MQ, and FUNO, downgrade Terra and FSHOP to Neutral, initiate Fibra PL, Danhos, and FMTY as Buys, and initiate Planigrupo as Neutral.

Table 1: BTG Pactual Mexican Real Estate Coverage

		Market Cap	BTG Pactual	Target	Current	ADTV (US$m)		Performance		Valuation (%)			
Name	Ticker	USD mm	Rating	Price (P$)	Price (P$m)	1 week	90 day	1 year	YTD	Cap	FFO	Div	P/NAV
Mexican FIBRAs													
Fibra Uno	FUNO11 MM	5,706	Buy	34	29	10.9	9.0	28.3%	41.2%	7.3%	8.0%	8.1%	0.78
Fibra Danhos	DANHOS13 MM	1,901	Buy	36	27	1.4	1.6	-0.8%	26.6%	10.3%	10.8%	9.1%	0.68
Fibra Prologis	FIBRAPL MM	1,329	Buy	46	41	0.8	0.8	15.7%	42.0%	7.0%	8.1%	6.0%	0.88
Terrafina	TERRA13 MM	1,224	Neutral	32	31	0.8	1.0	18.8%	41.0%	7.7%	9.6%	8.3%	0.88
Fibra Macquarie	FIBRAMQ MM	978	Buy	31	25	1.3	1.2	20.0%	48.6%	9.4%	12.6%	7.0%	0.69
Fibra Monterrey	FMTY14 MM	387	Buy	14	12	0.0	0.1	3.7%	7.1%	8.1%	10.7%	9.3%	0.85
Fibra Shop	FSHOP13 MM	214	Neutral	9	8	0.0	0.0	-8.5%	8.8%	8.7%	12.0%	10.3%	0.40
C-Corp													
Vesta	VESTA* MM	925	Buy	38	30	1.7	2.2	8.3%	16.5%	7.4%	6.0%	5.8%	0.83
Planigrupo	PLANI* MM	306	Neutral	22	19	0.0	0.0	0.0%	0.0%	8.3%	3.6%	-	1.13

Source: Company Data, Bloomberg BTG Pactual Estimates
Valuation on 2019E figures

The case for Mexican Real Estate

Valuation

Mexican real estate securities are cheap relative to any relevant peer group: This has been true for some time, for years actually. As we all know, however, when cheap stocks are in ready supply, valuation is a necessary but not sufficient condition for stocks to work and, until now, the other requisite ingredients were absent. But attractive valuation is an important ingredient for a rally and we believe that by any measure Mexican real estate stocks are cheap.

Our expanded sample (which now comprises nine stocks, up from five) trades at a 21% discount to NAV, at an 15% discount to our DDM-and-Exit cap rate-driven measures of intrinsic value (i.e., our price targets), at an average EBITDA cap rate of 8.1% and dividend yield of 8.2%. All these metrics screen as attractive relative to practically any peer group, be it real estate peers in developed markets, GEMs, or LatAm and to the broader sample of Mexican stocks, which for the past nine months have undergone a material de-rating.

Table 2: Mexican Real Estate Valuation - BTG Pactual Sample

	BTG Pactual	TP	Price	Total Return (%)	Market Cap	FFO Yield %			Dividend Yield %			Price / NAV			Implied EBITDA Cap Rate %			Implied NOI Cap Rate %			Cap Rate Spread
	Rating	(Local)	(Local)	(Local)	(US$mm)	LTM	2019E	2020E	LTM	2019E	2020E	LTM	2019E	2020E	LTM	2019E	2020E	LTM	2019E	2020E	2019E
Mexican FIBRAs																					
Fibra Uno	Buy	34	29	28%	5,706	8.0%	8.0%	8.6%	7.9%	8.1%	8.6%	0.78	0.78	0.78	7.2%	7.3%	7.6%	8.1%	8.1%	8.3%	4.2%
Fibra Danhos	Buy	36	27	43%	1,901	10.4%	10.8%	10.2%	8.8%	9.1%	6.5%	0.68	0.68	0.69	10.2%	10.3%	9.9%	10.5%	10.5%	10.2%	7.1%
Fibra Prologis	Buy	46	41	19%	1,329	8.0%	8.1%	8.7%	5.7%	6.0%	6.9%	0.87	0.88	0.89	7.0%	7.0%	7.4%	7.9%	7.9%	8.4%	3.9%
Fibra Terrafina	Neutral	32	31	12%	1,224	9.5%	9.6%	10.2%	8.7%	8.3%	8.7%	0.89	0.88	0.87	8.5%	7.7%	8.0%	8.5%	8.6%	8.9%	4.5%
Fibra MQ	Buy	31	25	33%	978	11.6%	12.6%	14.4%	6.7%	7.0%	8.2%	0.71	0.69	0.67	8.6%	9.4%	10.6%	9.1%	10.0%	11.2%	6.2%
Fibra Monterrey	Buy	14	12	24%	387	9.6%	10.7%	9.7%	9.0%	9.3%	2.2%	0.86	0.85	0.85	10.1%	8.1%	8.4%	11.3%	9.0%	9.4%	4.9%
Fibra Shop	Neutral	9	8	12%	214	12.2%	12.0%	9.4%	11.4%	10.3%	8.1%	0.40	0.40	0.39	9.4%	8.7%	8.8%	9.9%	9.1%	9.3%	5.5%
FIBRAs Average						***9.9%***	***10.3%***	***10.2%***	***8.3%***	***8.3%***	***7.0%***	***0.74***	***0.74***	***0.73***	***8.7%***	***8.3%***	***8.7%***	***9.3%***	***9.0%***	***9.4%***	***5.2%***
C-Corps																					
Vesta	Buy	38	30	31%	925	5.1%	6.0%	7.5%	5.8%	5.8%	5.8%	0.85	0.83	0.82	7.0%	7.4%	7.6%	7.9%	8.4%	8.6%	4.2%
Planigrupo	Neutral	22	19	13%	306	4.3%	5.0%	4.6%	-	-	-	1.16	1.13	1.08	7.9%	8.3%	8.9%	9.9%	10.3%	10.9%	5.2%
C-Corps Average						***4.7%***	***5.5%***	***6.0%***	***5.8%***	***5.8%***	***5.8%***	***1.00***	***0.98***	***0.95***	***7.5%***	***7.9%***	***8.2%***	***8.9%***	***9.4%***	***9.8%***	***4.7%***
Mexican Real Estate Average						***8.7%***	***9.2%***	***9.2%***	***8.0%***	***8.0%***	***6.9%***	***0.80***	***0.79***	***0.78***	***8.4%***	***8.2%***	***8.6%***	***9.2%***	***9.1%***	***9.5%***	***5.1%***

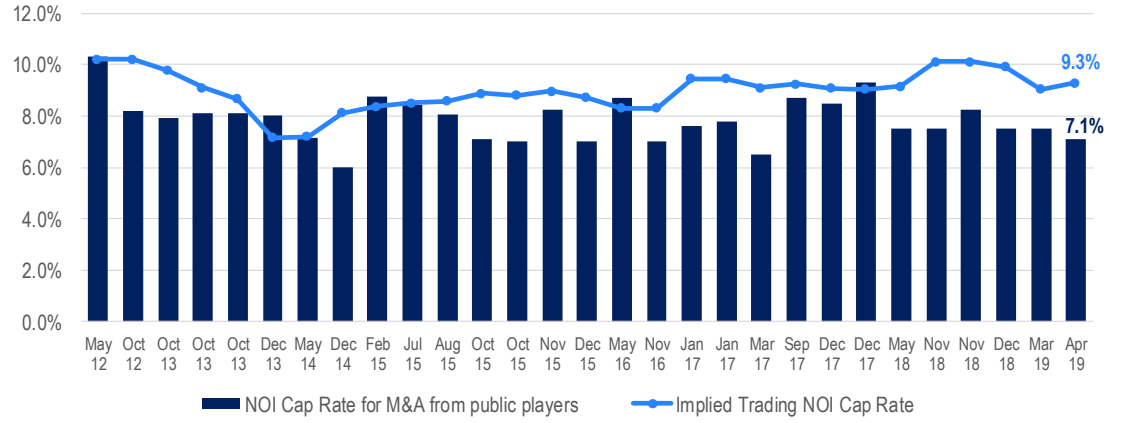
Source: Company Data, BTG Pactual Research

They are also attractively priced in the context of transactions in the private market: For some time now, Mexican real estate stocks have traded at discounts to the pricing of private market transactions. Given the diversification, tax benefits (for the FIBRAs), and liquidity that publicly traded securities offer, such discounts would not seem to make much sense. Some have posited that it is attributable to shortcomings on the governance front stemming from the original conception of the FIBRA structure (i.e., that they had to be externally managed), but it would not seem that this argument holds much water considering that listed C-Corps (Vesta, Planigrupo, GICSA, and Hoteles City) trade at discounts that are equal or even deeper than their FIBRA peers'.

However, what we find noteworthy is that while Mexican real estate stocks have de-rated significantly since the torrent of uncertainty that Mexico has suffered from over

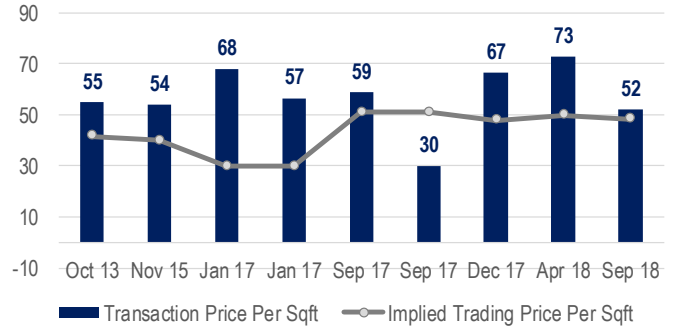
the past three years (the ascent of Candidate Trump, his election, the uncertainty surrounding NAFTA/USMCA, the ascent of Candidate AMLO, his election, the cancellation of NAIM, the Trump trade tirades, and Banxico's ensuing hawkishness), valuations in the private sector have mostly stayed pat. This is particularly true in the Industrial segment, where it would seem that nothing at all has happened. As a result, the discount of public to private valuations has expanded to one of its widest points since the de-rating of the FIBRAs began in 2016.

Chart 1: Mexican real estate stocks have traded at discounts to the pricing of private market transactions
Precedent Transactions from listed players 12MF NOI Cap Rate (%) vs Trading 12MF NOI Cap Rate (%)



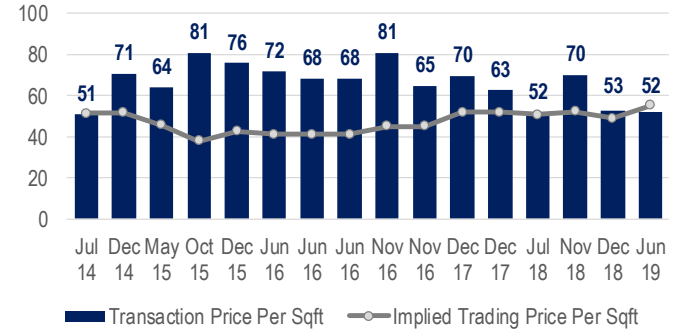
Source: Company Data, BTG Pactual Estimates
Notes: Only includes precedent transactions for large portfolios (>US$30m) in the industrial space for Fibra Uno, Terrafina, Fibra Macquarie, Fibra Prologis and Fibra Monterrey. Implied NOI Cap Rate is calculated as the aggregate cap rate for all of these players. Implied cap rate considers valuation at the exact date of M&A.
Please see Appendix 3 for more detail on these transactions.

Chart 2: Industrial FIBRAs trading below private market valuations
Terrafina - Transaction M&A vs Implied Valuation (Price per sqft)



Source: Company Data, BTG Pactual Estimates

Chart 3: Industrial FIBRAs trading below private market valuations
Fibra Prologis - Transaction M&A vs Implied Valuation (Price per sqft)



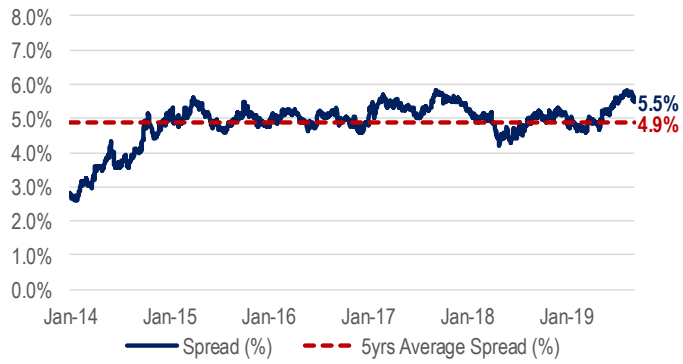
Source: Company Data, BTG Pactual Estimates

Spreads against applicable sovereign yields remain compelling: Since the sector's birth there has been debate as to what risk free rate (RFR) Mexican real estate stocks' yields should be measured against. We have argued that for those platforms that generate mostly MXN, the yardstick should be the 10-year UDIBONO yield (Mexico's equivalent of US TIPS or the UK's GILTs, currently yielding 0.1% and 0.5%, respectively) as these contracts are repriced yearly by Mexico's CPI.

For properties that are effectively USD-denominated (i.e., the bulk of Mexico's industrial real estate and much of its AAA office space, though the latter seems to be gradually shifting to MXN), we prefer to use the 10-year UMS yield (Mexico's sovereign USD-denominated bond, currently yielding 3.4%). One could argue that, since USD leases in Mexico also have annual US CPI escalations, a UMS-TIPS type of adjustment would be required, but we choose not to do that since both office and industrial contracts have historically tended to reprice upon expiration to levels similar to what was in effect when originally written (although in current conditions this is not the case for the industrial segments, where, because of tight market conditions, many contracts are being renewed at expiration level rents).

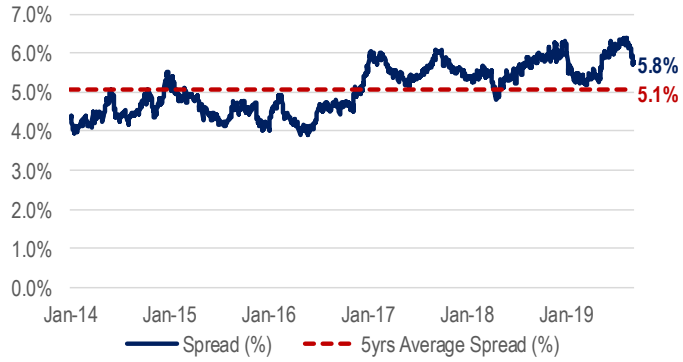
As can be seen in the charts below, segment cap rate spreads relative to the applicable sovereign yield remain at near all-time highs. And they remain below the level of their Brazilian peers.

Chart 4: Mexico – 12MF Industrial EBITDA Cap Rate vs. UMS Yield (%)



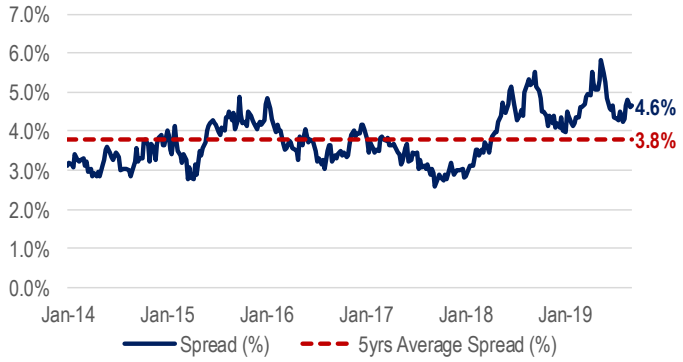
Source: Company Data, Bloomberg, BTG Pactual Estimates
Notes: Index includes FUNO; Terrafina, Vesta, Fibra MQ, Fibra PI, Fibra MTY. UMS - sovereign bond denominated in foreign currency.

Chart 5: Mexico - 12MF Retail EBITDA Cap Rate vs. UDIBONO Yield (%)



Source: Company Data, Bloomberg, BTG Pactual Estimates
Notes: Index includes Fibra Uno, Fibra Shop, Fibra Danhos, and Planigrupo. UDIBONO-bond linked to inflation shows Mexican long-term interest rate.

Chart 6: Brazil - 12MF Retaill EBITDA Cap Rate vs. NTNB'35 Yield (%)



Source: Company Data, Bloomberg, BTG Pactual Estimates
Notes: Index includes Multiplan, BR Malls, Iguatemi, and Aliansce. NTNB'35 - bond linked to inflation shows Brazilian long-term interest rate.

Global interest rate environment supportive

But, for a change, Mexican real estate stocks now actually seem to be working: Much of what we argue in the preceding points on valuation could have been said at any moment over the past three years to little avail since FIBRA performance was, for the most part, disappointing. But at the beginning of this year something changed and FIBRAs began to outperform; in fact, the industrial names have been among the best performers in Mexico. Though ordinarily one would hesitate to recommend stocks that have already worked, in this particular case we are actually encouraged since it suggests that the other, non-valuation ingredients required for a rally to take hold are present. As we argue below, those ingredients remain in place and should continue to, while the discount to valuation is so steep that, in spite of the YTD rally, there is still significant room for re-rating.

The global interest rate environment is supportive for Mexican real estate: Since the year began, the expectation for interest rates globally has shifted dramatically from anticipation of gradual tightening by the US FED to outright loosening. This has been reflected across the global yield curve, with UST 10-year bonds now paying 1.59% (from 2.65% at the beginning of the year) and an estimated total of US$15bn trillion worth of sovereign bonds globally now paying negative yields. This has led to a global hunt for yield, driving investors to bid up real estate assets around the world; Mexican real estate securities, by virtue of offering among the highest yields globally, have been no exception. With US FED expected to cut rates further in 2H19 and the world showing signs of deceleration, we expect this favorable backdrop to remain in place for some time.

Chart 7: US Treasury (10 Year Yield %)

Source: Bloomberg

Banxico's stance remains timid, but what matters is the long-end: In spite of the cuts in the August and September meetings, the call on Banxico's future policy stance is significantly less straightforward. From a cyclical standpoint, there is every reason for Banxico to cut much more aggressively: growth is well below target and slowing, inflation is declining and is now within the board's targeted range, and, at 7.75% (which translates into a real rate of almost 4%), Mexico has the highest front end rates of any Investment Grade (IG) credit by a country mile while much of the rest of the world is easing. For any country, these would seem to be ripe conditions

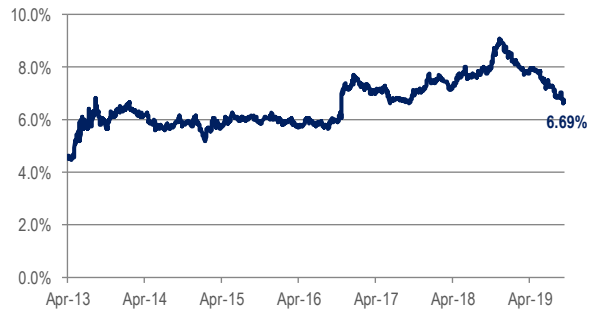
for easing vigorously and the Board's recent meeting minutes suggests that certain of its members are increasingly leaning in that direction.

However, Mexico is not "any country" and Banxico has made it clear for some time now that it is not managing policy rates only for cyclical concerns. Rather, it is using them to preempt against any volatility stemming from a number of non-cyclical factors that have been affecting Mexican financial markets for several years: the yet-to-be-resolved balance sheet challenges at Pemex triggered by the 2014 oil market crash; the ascent and subsequent victory of Candidate Trump; the NAFTA/USMCA negotiations and continued questions around its passage in the US Congress; the ascent and subsequent victory of Candidate AMLO; the fallout from the cancellation of NAIM; and ongoing concerns around the AMLO administration's ability to preserve Mexico's sovereign IG rating. Many of these risks are yet unresolved and there are sundry potential pitfalls down the road that make it impossible to rule out further unforced errors by the AMLO administration or additional hostility by Trump's.

Our base case is that, barring any major jitters stemming from the 2020 budget negotiations (which begin formally with the bill's introduction to Congress in September and passage by the end of November 2019), Banxico will be in a position to cut more freely by year-end 2019, to be followed by additional easing in 2020 if FX markets respond calmly. To ensure that they do remain calm, however, we believe Banxico will cut only grudgingly and do its best via its communications to dampen the market's enthusiasm on the potential for a prolonged easing cycle. And, of course, should FX markets not digest cuts well, Banxico will not hesitate to reverse course.

All of this said, we believe that what really should matter for the pricing of real estate assets and securities is the long-end of the curve, particularly the US long bond. And, as discussed above, these yields have already dropped materially and are likely to remain subdued for some time, potentially declining further. Mexican long rates have also declined, with the 10-year MBONO and UDIBONO (Mexico's inflation-adjusted bonds) now yielding 6.69% and 3.16%, some 251bps and 134bps, respectively, below their recent highs of November 2018. Easing by Banxico would help, however, especially among domestic investors, for whom short-term rates are a relevant metric for pricing any asset seen as a bond-proxy.

Chart 8: MBONO Generic 10 Yr (%)



Source: Bloomberg

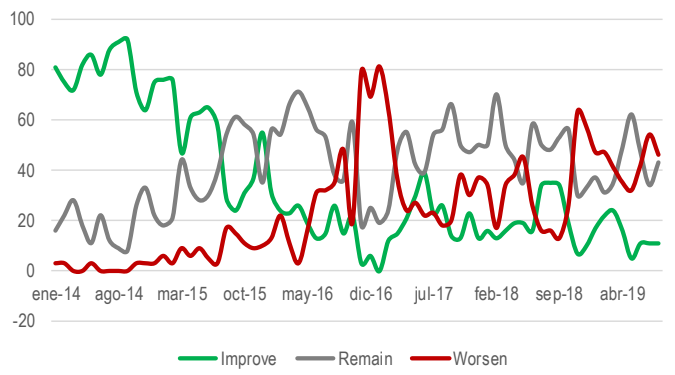
Chart 9: UDIBONO Generic 10 Yr (%)

Source: Bloomberg

A closer look at fundamentals for each segment

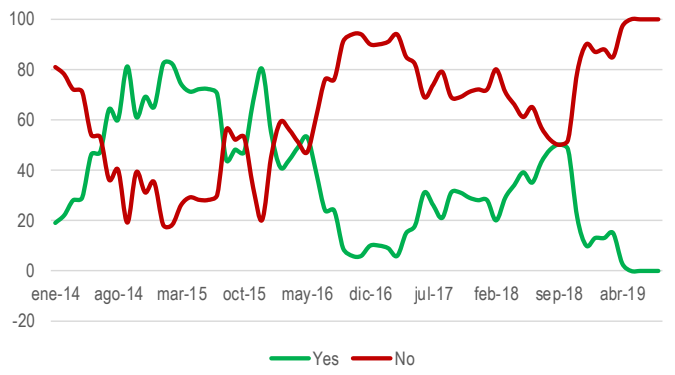
The plunge in business confidence has led to tighter markets, especially on the industrial front: Financial markets and Mexico's business sector was won over by the more moderate stance adopted by Candidate AMLO during his campaign. Their support for the incoming administration was not even fazed by the magnitude of his win, which granted him significantly greater legislative support than markets had anticipated going into the July 2018 election. But his somewhat surprising and difficult to comprehend decision to cancel NAIM brought this painstakingly constructed edifice of confidence tumbling down in one fell swoop. And, while there have since been a handful of short-lived episodes of a resurgence of market confidence in AMLO, his support among Mexico's business class has suffered from an uninterrupted and continuous erosion.

Chart 10: Perception of Business Climate in Mexico
How do you think the business environment in the private sector will evolve over the next six months vs. the previous six months?



Notes: Percentage of total participants in the survey
Source: Banxico, BTG Pactual Research

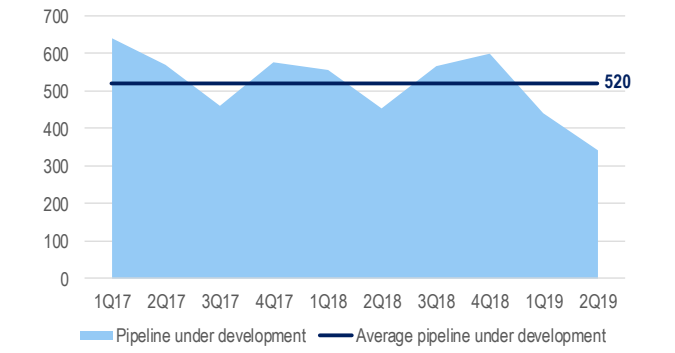
Chart 11: Economic strength vs. last year
Is the current economic environment better off today compared to last year?



Notes: Percentage of total participants in the survey
Source: Banxico, BTG Pactual Research

Exacerbated by the permitting issues in CDMX, this lack of confidence is also reflected among real estate developers, most of whom have committed to finishing existing projects and to halt the development pipeline of retail and office properties altogether. This lull in development activity is particularly evident in the industrial segment, where the halt began much earlier (with the rise of Candidate Trump in 1H16) and has not been lifted.

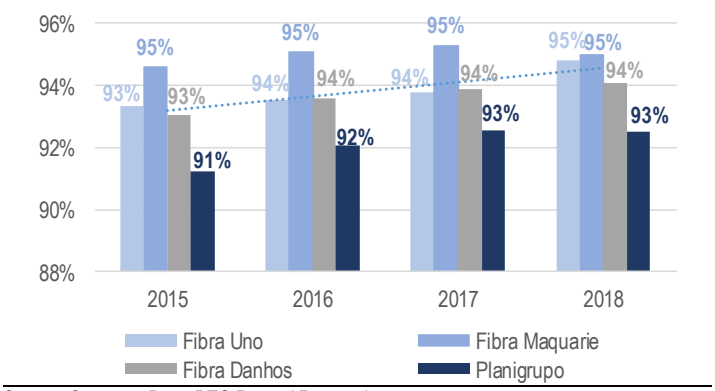
Chart 12: Mexico City – Industrial Pipeline Under Construction (sqm k)



Source: CBRE, BTG Pactual Research

This has contributed to healthy occupancies in retail and industrial...: With the exception of the office segment, where we would argue that there has been excess supply since 2016 and which shows no signs of abating, healthy demand dynamics and prudence on the supply front have led to tightening markets in the retail and industrial segments. Judging by the portfolios of the listed players, retail occupancies have increased on average by 150bps over the past three years and are now standing, on average, at 94.5%.

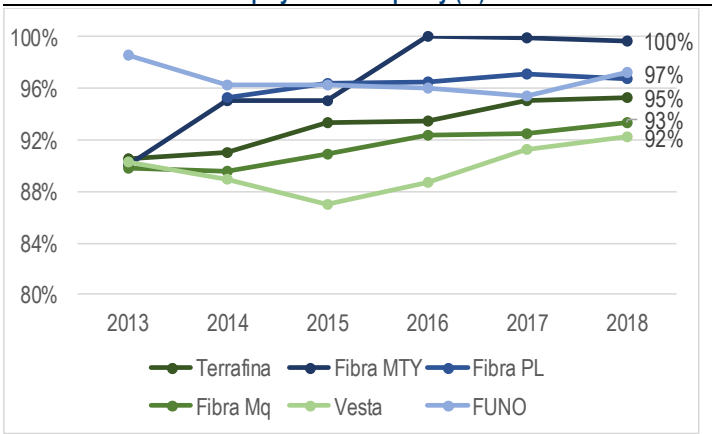
Chart 13: Retail Listed players - Occupancy (%)



Source: Company Data, BTG Pactual Research

On the industrial front, the same trends have taken hold, although the improvement in occupancies have likely been more pronounced. As discussed earlier, industrial developers, who were badly burnt by the Great Recession and its impact on an already loose Ciudad Juárez market, have had for almost four years a number of reasons to opt out of development opportunities. Yet, contrary to almost all expectations, FDI in Mexican manufacturing and, thus, demand for industrial space, has continued to grow almost unabated. This, as discussed above, has led to record high occupancies in almost every region, including Ciudad Juárez and Bajío.

Chart 14: Industrial Listed players - Occupancy (%)

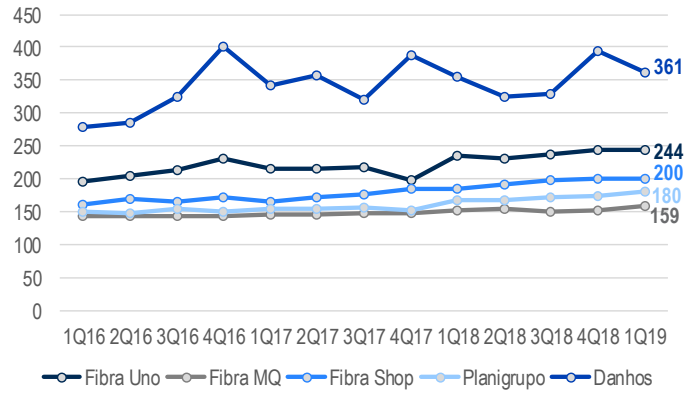


Source: Company Data, BTG Pactual Research

And has also contributed to rising rents: Rising occupancies has contributed to higher rents, particularly in the retail sector and, more recently, in the industrial space. Across our sample, retail rents have shown realized increases well above inflation

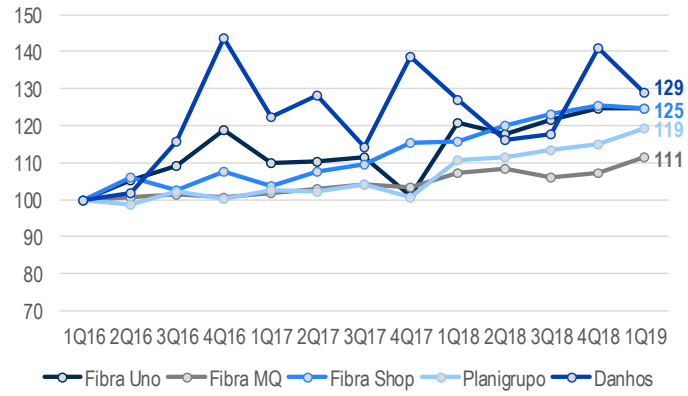
and, for those companies that disclose leasing rates on new contracts, spreads continue to be positive.

Chart 15: Retail Real Estate – Monthly Implied rents
(P$/sqm)



Source: Company Data, BTG Pactual Research

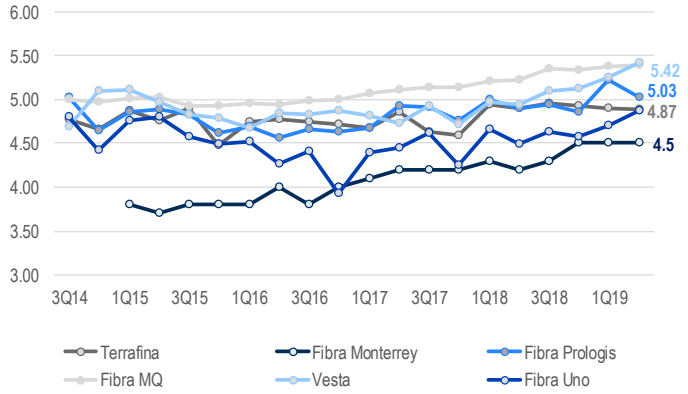
Chart 16: Retail Real Estate – Monthly Implied rents in MXN
Base 100



Source: Company Data, BTG Pactual Research

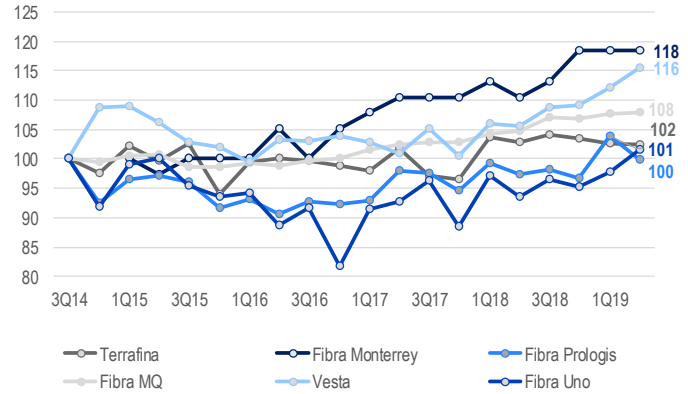
Even on the industrial front, USD rents and leasing spreads on new contracts have begun to rise. This is unusual since rents in the segment tend to be stickier given the greater elasticity of supply (i.e., new supply is quicker to react to strong demand) and because the Mexican market has historically tracked US industrial rents given a commonality of tenants and end-markets.

Chart 17: Industrial Real Estate – Annual Implied rents
US$/sqf



Source: Company data, BTG Pactual Estimates

Chart 18: Industrial Real Estate – Annual Implied rents in USD
Base 100



Source: Company data, BTG Pactual Estimates

Office is the smallest segment, representing only 15% of our sample's revenue and is no more than 47% for any one player: The one segment where neither occupancy nor rents are rising is the office segment. Office vacancy in Mexico City is 15% and will likely rise further given the amount of inventory slated to hit the market. This is particularly true if the economy continues to lose steam and if business confidence remains in the doldrums. Fortunately, however, office represents an average of only 15% of revenue among the nine names that we cover and, in fact, is completely absent from the majority of them. Among the names we cover, only FUNO

(19% of revenue), Danhos, (36%), FMTY (47%), and Fibra MQ (4%) have office exposure.

A favorable environment for owners of stabilized assets

What's good for the gander (i.e., owners of stabilized portfolios) isn't always good for the goose (i.e., developers): The current macro backdrop is arguably one that would be considered particularly unattractive for developers. On the external front, there is concern on the durability of the US cycle, anxiety on the global front on account of rising trade tensions between the US and China and, at the margin, on uncertainty on the final outcome to the Brexit saga and its impact on the EU/UK, and worries about US electoral politics spilling over into trade-related noise between Mexico and the US (e.g., Trump's recent threat to impose tariffs on Mexico should the latter not cooperate on stemming Central American immigration). On the domestic front economic growth is slowing, business confidence is in the doldrums, front-end interest rates are the highest among IG countries, and valuations of several potential buyers of assets are well below levels that would result in an active M&A market (though non-Mexican investors are beginning to become more active on the buy side). These have all been reasons for developers to remain on the sidelines and, at present, none would really seem near to abating.

But for owners of stabilized assets the environment, while still challenging, is somewhat more appealing (or, perhaps more precisely, less unappealing). The economy is slowing, but it is not by any means moving intro crisis, suggesting a reasonably healthy demand environment. Supply, on the other hand, remains under control and, given the outlook discussed above, there would seem to be little reason to believe that more inventory will hit the market any time soon. This is leading to the tight markets we discuss above and, recently, an uptick in rents, which is a combination that owners of existing assets should appreciate.

And FIBRA's less appetizing instincts seem also to be in check: Without a doubt, of all the issues presently frustrating FIBRA managers, the most irksome is the current level of valuation (which has been true for some time). This has reduced their ability to grow via acquisition at a time where there is likely to be a rising number of motivated sellers. But for minority owners of their CBFIs, this could be the icing on the cake of the FIBRA investment case, not just because current valuations represent a compelling entry point, but, perhaps more importantly, because it puts a check on some of the FIBRA managers' incentives that have been particularly loathsome to many of their investors. Specifically, we are referring to a historical tendency to issue equity to finance acquisitions that, while conducive to NAV growth that typically equates to greater fees, are not necessarily value-accretive and, frustratingly for investors, has led to recurrent dividend dilution.

The current discounts to NAV (on average in the 15-25% range) are sufficiently deep for most players that even if assets in the M&A market were available at wider discounts there is no real way that management would consider issuing equity at current prices. And, of course, in some cases (such as FUNO), there is an explicit pledge to shareholders not to issue equity even to sellers of assets at discounts to NAV. This all gives stocks significant room to run before the specter of dilution

appears. And in the present what this means is that per CBFI metrics are fully benefitting from all of the drivers that are boosting the top line and, therefore, growing at the same pace as the rest of the P&L.

Managements are gradually improving governance

In fact, managements are gradually improving governance and, in some cases, increasingly speaking about internalizing their structures: As is always the case with any restructuring of corporate governance, the devil is in the details. As can be seen in the chart below, governance in the sector is improving as companies make adjustments to their structures (this is true, particularly, in the degree of independence in their boards) or new ones are born without many of the sector's original sin (Vesta and Plani as C-Corps and FMTY among the FIBRAs). We would expect these improvements to continue.

Table 3: Mexican Real Estate - Corporate Governance Overview

	Fibra Uno	Fibra Danhos	Fibra Shop	Planigrupo	Terrafina	Fibra Prologis	Fibra MQ	Vesta	Fibra Monterrey
Ownership structure	The control trust owns 25% of CBFIs outstanding	The control trust owns 45% of CBFIs outstanding and the groups that constributed properties own ~39% (unclear how much is in the market)	The control trust owns 18% of CBFIs outstanding	Bross Family and Private Equity (Southern Cross) own 71% of shares outstanding	0%	The sponsor (Prologis Inc.) owns 47% of CBFIs outstanding	The sponsor (Maquarie Development Capital) owns 5% of CBFIs outstanding	Founder family owns 7% of shares outstanding	No Control Trust
What % of technical committee (board) independent?	33% (4 out of 12 members)	27% (3 out of 11 members)	45% (3 out of 7 members)	27% (3 out of 11 members)	75% (6 out of 8 members)	62% (5 out of 8 members)	80% (3 out of 5 members)	80% (8 out of 10 members)	71% (5 out of 7 members)
Related-Party Transaction Approval Method	Majority vote of the TC + Majority vote of the independent members. Transactions exceeding 10% of the FIBRA's equity must be approved by the shareholders.	Majority vote of the TC + majority vote of the 'Comite de Practicas' (comprised solely of independent members)	Majority vote of the TC + Majority vote of the independent members	Majority vote of the board and supervised by the Corporate Practices Committee	Majority vote of the independent members	Majority vote of the independent members	Majority vote of the independent members and transactions exceeding 10% of the FIBRA's equity must be approved by the shareholders	Majority vote of the board with the opinion of the Corporate Practices Committee	Majority vote of the TC (considering the opinion of the corporate practices committee) and transactions exceeding 10% of the FIBRA's patrimony must be approved by the shareholders
Internalized?	No	No	No	Yes	No	No	No	Yes	Yes
Removal of the advisor (without cause)	If the control trust maintains at least a 15% stake, they maintain control over the Advisor	Requires the approval of shareholders that represent 85% of the outstanding certificates + majority vote of indpendent members	Requires the approval of shareholders that represent 89% of the outstanding certificates + majority vote of indpendent members	NA	Requires the approval of 50% of shareholders (and requires 50% attendance)	Requires the approval of 66% of shareholders (and requires 66% attendance)	Requires the approval of 50% of shareholders excluding the advisor ownership (and requires 50% attendance)	NA	Given that the advisor is internalized, it cannot be removed. However, the technical committee can change the officers of the advisor.
Separate Chairman and CEO roles	Yes	Yes	No	Yes	No	No	No	Yes	Yes
Ordinary shareholder's meeting: Attendance and Voting requirement (% of participants)	Majority attendance and voting is required	Majority attendance and voting is required	Majority attendance and voting is required	Majority attendance and voting is required. The Chairma's vote has preference in the event of a tie	Majority attendance and voting is required	Majority attendance and voting is required	Majority attendance and voting is required	Majority attendance and voting is required	Majority attendance and voting is required
Sponsor Performance Fee / Executive Compensation Plan	No performance fee / ECP: CBFIs paid in function of (i) relative CBFI return and (ii) operating metrics (FFO/CBFI, Distributions)	No Performance Fee / No ECP	No Performance Fee / No ECP	Not disclosed	Sponsor Performance Fee: 10% of absolute CBFI performance over a 9% nominal hurdle rate, paid in shares, 6 month lock up / ECP: 0.5% in excess of total return on 9% nominal hurdle rate, 3-year lock up	Sponsor Performance Fee: CBFIs paid based on absolute CBFI performance over a 9% nominal hurdle rate / No ECP	Sponsor Performance Fee: Paid in CBFIs based on Fibra MQ's market cap (adjusted for distributions and buyback) / No ECP	No Performance Fee / ECP: Paid in Vesta stock, a function of (i) absolute return of stock and relative return vs. peers and (ii) operating metrics (NOI SSS growth / Occupancy)	No Performance Fee / ECP: Paid in CBFIs, a function of AFFO real growth
Significant transactions	Transactions that represent > 5% of the FIBRA's mkt value require the approval of the TC, those that represent >20%, must be approved by shareholders	Transactions that represent >19.9% of asset base must be approved by the TC	-	Transactions that represent >5% of their asset base must be approved by the board	Transactions that represent > 5% of the FIBRA's mkt value require the approval of the TC, those that represent >20%, must be approved by shareholders	Transactions that represent > 5% of the FIBRA's mkt value require the approval of the TC, those that represent >20%, must be approved by shareholders	Transactions that represent > 5% of the FIBRA's mkt value require the approval of the TC, those that represent >20%, must be approved by shareholders	Transactions that represent >5% of their asset base must be approved by the board with an absolute majority vote	Transactions that represent >20% of the Trust's Patrimony must be approved by the Holders's Meeting

Source: Company Data, BTG Pactual Research

Rightly or not, in the minds of minorities the holy grail from a FIBRA governance standpoint is internalization. While it would doubtless be positive, as we discuss in the risks section below, we see a non-trivial risk that a move to internalize, even if advanced with the best of sentiments, might actually aggravate the relationship with shareholders (after all, "the road to hell is paved with good intentions"). But the mere fact that managements are speaking about this is an indication that they understand how the external management structure and all that it implies is an irritant to shareholders that must eventually be addressed. This, in itself, is a positive.

All of this might lead to much-hoped for M&A in the publicly traded space: One of the frustrations of the FIBRA space is that these same governance shortcomings have led to a complete absence of M&A activity among publicly traded platforms. The impediments around removing management companies means not only that underperforming management teams stay on for much longer than they should, but they also represent a significant obstacle to sector consolidation given the very onerous buy-out terms these protections imply. One example is FSHOP: in any other

market, a stock with a 82% float would never have reached a 60%-plus discount to NAV, particularly in a market where private transactions are taking place near NAV. Worse, we understand that interest from potential buyers was widespread, but the general feeling was that management believed they were being misunderstood by the market and dug in their heels. The outcome is further stock de-rating, drying liquidity, and frustrated shareholders.

Should these governance improvements take hold and become more generalized, there should eventually be a floor to valuations in the form of M&A among publicly traded names. In addition to the removal of underperforming teams, the ability of good managements to reap the benefits of a value premium, and improvements in stock liquidity, the mere reduction in the number of available stocks would likely be a positive in itself.

Multi-family represents a massive opportunity for growth

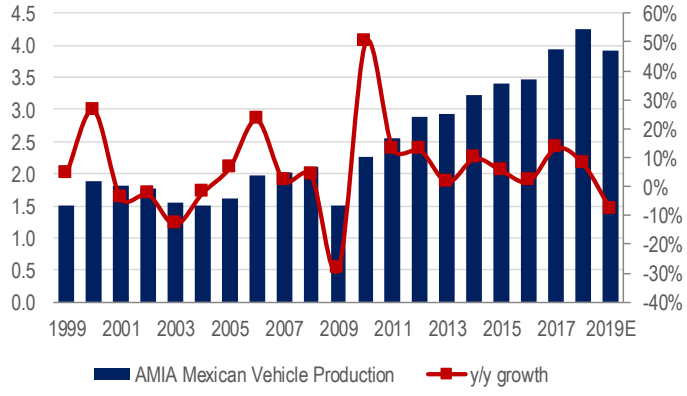
Multi-family is largely unexplored and represents a massive opportunity for growth: The largest segment among US REITs is the multi-family space (i.e., residential for rent). In Mexico, this sector represents literally zero of publicly traded NOI. Historically, the arguments against multi-family have been strong and based largely around the legal difficulties of evicting tenants. In the past few years, a number of private developers have ventured into the segment and, though the pace of progress remains timid, the initial read is positive. This, to us, represents the largest untapped source of growth for FIBRAs.

Industrial real estate remains our preferred segment

Industrial real estate remains our preferred segment: Throughout the discussion above we have highlighted what we see as the strengths of the industrial space from an occupancy and rents standpoint. This has to do with factors affecting both demand and supply, some of which are cyclical and temporary but many of which we see as long-term and secular. For these reasons, expanded on below, Mexican industrial real estate remains not only one of our preferred segments in the Latin American real estate space, but also one of our few high conviction buys in Mexico.

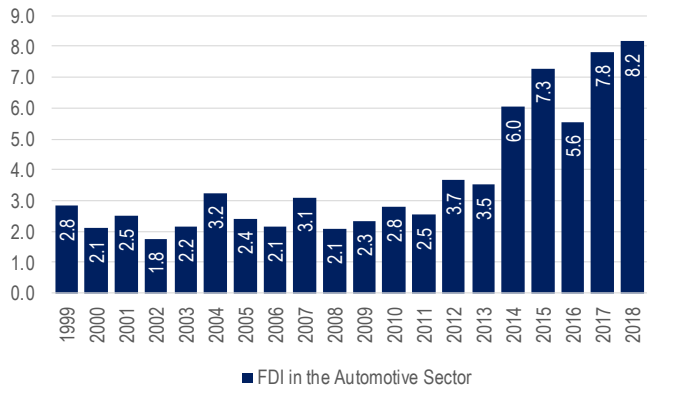
Mexico continues to establish itself as the workshop of North America...: We would argue that Mexico's establishing itself as the workshop of North America (and in some products such as autos one of the factories of the World) has been occurring at different speeds since the initial days of NAFTA in 1994. Mexico's becoming an integral part of the North American supply chain started at full throttle in the late 1990s, only to be interrupted for a decade by the entry of China into the WTO and the ensuing repositioning of global supply chains. However, various different issues, including demographics, a repositioning of the Chinese economy, and geopolitical factors, contributed to put Mexico back in the fast lane, which, in spite of a few speed bumps along the way, is where it remains today.

Chart 19: Mexican Auto Production (# of units in millions)



Source: AMIA, BTG Pactual Research

Chart 20: FDI in Mexican Automotive Sector Investments (US$m)



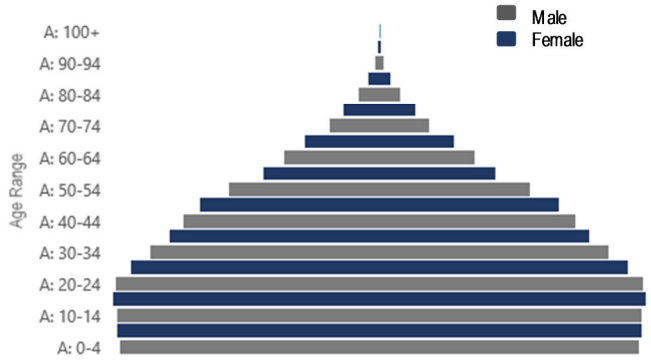
Source: Secretaria de Economia, BTG Pactual Research

...which might be reinforced by USMCA...: USMCA is not yet law and, in our base case, will likely not become so until after the US presidential elections in November 2020; depending on the outcome, this might require an additional round of negotiations aimed to fine-tune the agreement. However, we believe that in some shape or form and at some point in the not too distant future USMCA (or perhaps a more creatively-named version of NAFTA 2.0) will be implemented. Though USCMA presents some challenges for Mexico and its manufacturers relative to the original NAFTA, it also offers a number of opportunities. Most relevantly for the industrial real estate space, among these opportunities is what is likely to be additional production and supply chain integration as a result of the higher North American content requirements that the agreement imposes.

Thinking of how this could affect the auto industry, for example, it should increase both the scope and added value of production, along with widening the number of suppliers that OEMs bring with them to Mexico. It might also result in a greater share of R&D and other product development activities, which would have additional economy-wide benefits as well. This would mean that Mexico will not only likely continue to increase its share of North American auto production, but also raise its portion of the value of the average automobile produced in North America, compounding the effect on additional demand for space, particularly for the European and Asian OEMs using Mexico as their production hub for the North American market.

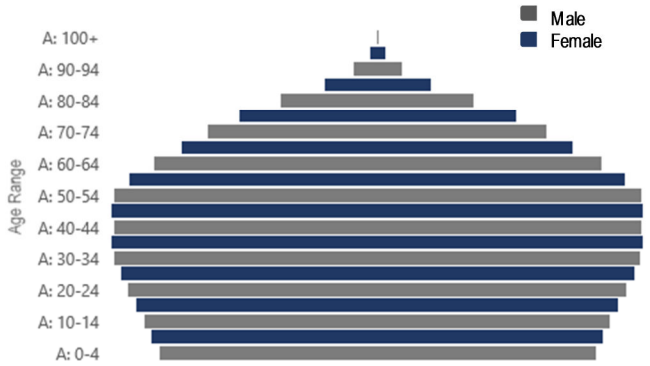
...demographics...: Dusting off our old Economics textbooks, we'll remember that for most goods demand can vary continuously while supply tends to be relatively sticky (at least in the short-term). Absent full cross-border mobility (which given the politics of immigration in most developed markets is increasingly a fantasy), there is no good where this is truer than labor. And the supply of labor is, in turn, determined by demographics. Again, absent immigration, demographic trends are determined by a plethora of different drivers that, in most countries, are difficult to manage and, where even possible, takes decades to have an effect.

Chart 21: Demographic Pyramid of Mexico 2018



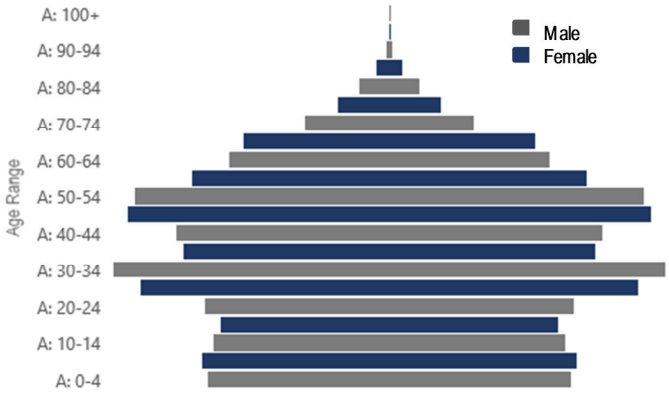
Source: Populationpyramid.net, BTG Pactual Research

Chart 22: Demographic Pyramid of China 2018



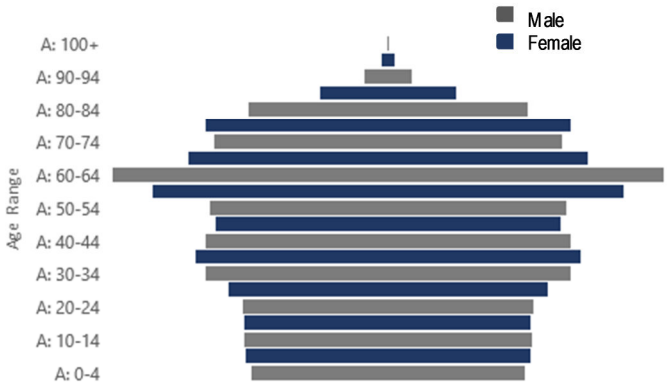
Source: Populationpyramid.net, BTG Pactual Research

Chart 23: Demographic Pyramid of Mexico 2050



Source: Populationpyramid.net, BTG Pactual Research

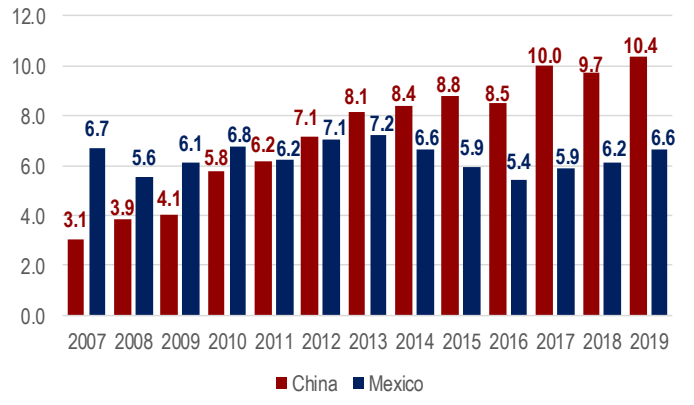
Chart 24: Demographic Pyramid of China 2050



Source: Populationpyramid.net, BTG Pactual Research

The demographics driving the labor forces of Mexico and China could hardly be more contrasting. While Mexico continues to boast the demographic profile that we have come to identify with Emerging Markets (a pyramid with a wide base that will translate into a growing pool of labor for many years to come), China's is reflecting the impact of the Single-Child policy introduced in 1979 in an effort to stem fertility rates and combat poverty. Though the effectiveness of the policy is likely to have contributed to the Chinese economic miracle of the past four decades, the fact is that today it has resulted in tightening labor markets that are unlikely to loosen up any time soon. This has resulted in many years of wage gains in China that, contrasted to Mexico's lackluster wage growth, has for some years now rendered Mexican manufacturing wage increasingly competitive.

Chart 25: Minimum Yearly Wage related to Automotive Manufacturing
(USD current prices)

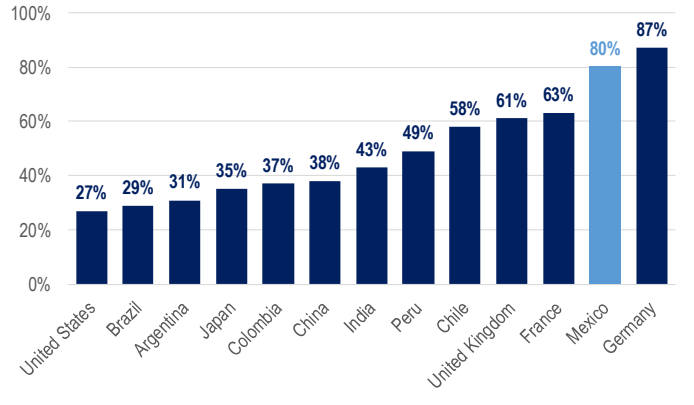


Source: CEIC Data

ecause demographic trends are unalterable in the medium-term, this competitiveness is likely to become more pronounced in the years to come, which is yet another long-term driver supporting the case for Mexican manufacturing (and, thus, industrial real estate).

...the optionality of operating in the most open trader in the world...: Mexico has FTAs with over 40 different countries, making it, along with Chile, the country with most such agreements in the world. It is the only country with FTAs with the US, the EU, and Japan; with the start of TPP, Mexico now trades freely with over 60% of the world's GDP.

Chart 26: Total Trade as a % of GDP – Select LatAm Countries & Other Large Countries

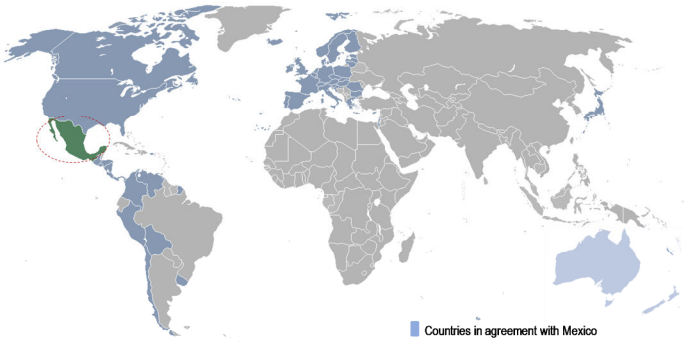


Source: World Bank

This has played to Mexico's benefit on two fronts. On the one hand, for many of these FTA partners, Mexico offers the prospect of access to the largest economic bloc globally, NAFTA, and, in particular, to the US market. On the other, however, for companies that establish manufacturing there, it offers the optionality of trading freely with many of the world's most important markets with relative ease given its access to both the Atlantic and Pacific oceans or to effectively source components from suppliers located in any of the countries with which Mexico has FTAs. This can mean

a continuity in supply chains or the optionality to optimize them further by establishing new chains altogether.

Chart 27: Mexico's Trade Agreements



Source: World Trade Organization, BTG Pactual Research

Chart 28: Mexico's Trade Agreements

Agreements	Date entered into force
NAFTA (Mexico, Canada, United States)	Jan 1 1994
Chile	Aug 1 1999
European Union (Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and United Kingdom)	Oct 1 2000
EFTA (Iceland, Liechtenstein, Norway and Switzerland)	Jul 1 2001
Uruguay	Jul 15 2004
Japan	Apr 1 2005
Colombia	Jan 1 2011
Israel	Feb 1 2012
Peru	Feb 1 2012
Central America (Costa Rica, El salvador, Guatemala, Honduras and Nicaragua)	Sep 1 2013
Panama	Jul 1 2015
CPTPP/TPP11 (Australia, Canada, Japan, Mexico, New Zealand and Singapore)	Dec 30 2018

Source: World Trade Organization, BTG Pactual Research

...and the ongoing Trump trade spats: Though the world as a whole is worse off as a result of a trade war between its two largest economies, many of Mexico's manufacturing strengths are reinforced by them. This might mean that Mexico is one of the few places that benefits relatively and absolutely from escalating trade disputes between China and the US. In a world in which access to the US market from anywhere in the world is uncertain (but particularly for the market that, from a manufacturing standpoint, competes most directly with Mexico), the visibility and guarantees for Mexico from a newly-minted USMCA and from the deep integration of the NAFTA economies render it a standout for any company seeking to establish a low-cost manufacturing base.

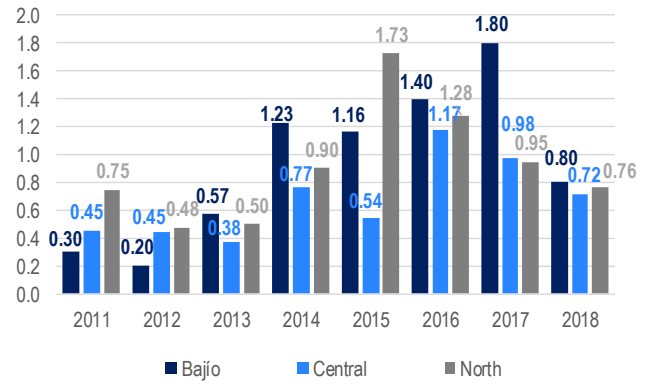
Largely immune to domestic economic sluggishness and potential future policy missteps: One of the reasons we like industrial real estate assets in Mexico is that, for the most part, they are largely immune from what happens domestically, for good or for bad. What's more, one could even argue that a soft domestic macro environment is actually beneficial to industrial real estate demand in as much as it it translates into either a weaker MXN or reduced wage pressure, both of which would boost Mexico's manufacturing competitiveness and, thereby, reinforce its business case.

Because, from the market's vantage point, what has been happening recently (specifically since AMLO's decision to cancel NAIM in October 2018) has tended to be negative (both in terms of growth and policy), this relative immunity has been a good thing and explains industrial real estate stocks' outperformance over recent months. And, given that there would seem to be more downside than upside risk for future policy decisions, this hedge (or, perhaps, outright negative correlation) seems particularly valuable at the moment.

The tightest segment by a country mile: As discussed throughout the preceding section, industrial real estate development activity screeched to a halt with the ascendancy of Donald Trump in the spring of 2016. Contrary to expectations, however, demand for industrial real estate from foreigners continued apace, resulting

in a market that has gradually tightened to levels not seen in recent memory. This is in sharp contrast to the blatantly oversupplied office space and to the more tenuous demand-supply balance in retail.

Chart 29: Net Absorption (sqm million)



Source: CBRE, BTG Pactual Research

Please see Appendix 6 for more data on industrial real estate in Mexico.

We like USD cash flows...safer and cheaper: Like the office segment, industrial real estate contracts are typically written in USD and adjusted by US CPI (at least for the light manufacturing portion of the market, which remains the bulk of what comprises listed companies' portfolios). Unlike the office segment, however, the tenant base either generates USDs or is part of the export chain, making USD the appropriate currency in which to write such contracts. This, to us, offers two distinct advantages to industrial real estate portfolios relative to commercial or office properties.

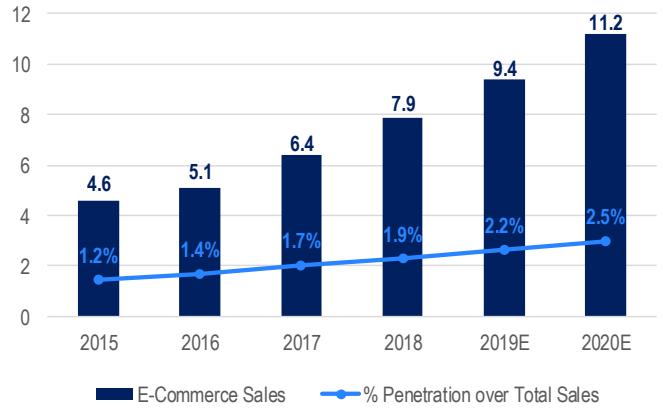
First, we see USD cash flow as a source of protection against MXN volatility. In effect, it makes industrial real estate a proxy to Mexico's large export economy, which, frustratingly, is difficult to gain access to via public equity markets. As the past five years have shown, the MXN can suffer periods of volatility and prolonged weakness, which given the outlook for policy under the AMLO administration is likely to persist. This serves as a double-barreled positive for industrial real estate stocks: on the one hand, it provides a natural hedge to MXN weakness; on the other, MXN weakness adds to the advantages of manufacturing in Mexico, reinforcing demand for additional space.

Second, and perhaps more importantly, generating USDs allows industrial portfolios to leverage up in the much deeper, cheaper, and stable USD real estate financing markets. With this, portfolios to support higher levels of debt, deliver higher equity returns to investors, and better manage their balance sheets, reducing volatility around their higher equity returns. In the parlance of portfolio managers, everything else being equal, industrial portfolios in Mexico should have better Sharpe ratios than their peers.

And, in the long-run, logistics is on the right side of the e-commerce debate: Logistics accounts for 28% of the industrial portfolios of the six stocks we cover with

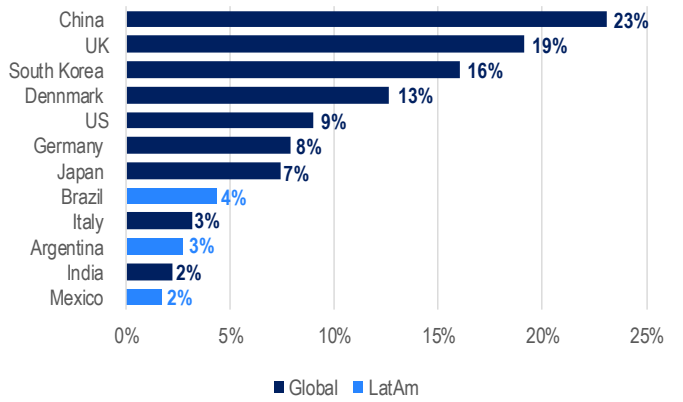
industrial exposure (Terra, Vesta, Fibra PL, Fibra MQ, FMTY, and FUNO, in declining order of sector exposure), so it remains small relative to the stock exposure to light manufacturing. Nevertheless, the share of GLA in the logistics space is increasing and, we would argue, will become instrumental to the development of e-commerce in Mexico, particularly given the distribution and logistical challenges that many cite as the main impediment to its growth. Unlike in the retail space, where there is a debate as to who the winners and losers will be, most would agree that however and at whatever speed e-commerce evolves in Mexico, it will ultimately lead to a greater need of logistics space, which should be positive for industrial portfolios with exposure to the segment or with land bank and properties in appropriate locations.

Chart 30: Chart 31: While online shopping is growing in Mexico…
E-Commerce sales (US$bn) and penetration



Source: eMerketer, BTG Pactual Research

Chart 32: … it remains low as a share of total retail sales…
E-Commerce penetration of total sales



Source: Euromonitor, BTG Pactual Research

Please see Appendix 1 for more data on e-commerce in Mexico.

What are the risks?

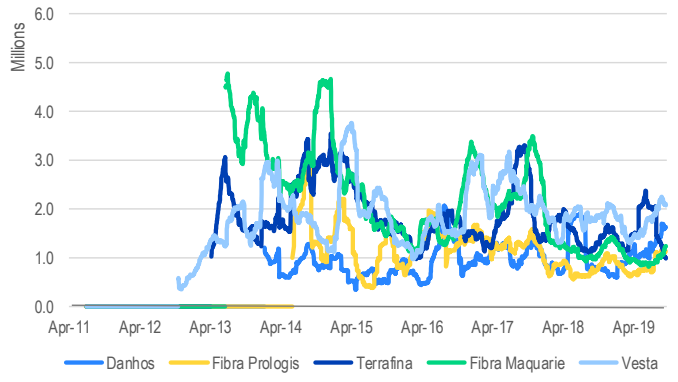
Outside of FUNO, the sector suffers from low-stock liquidity

The bullish view on Mexican real estate and preference for the industrial space that we express in this report is not new — it is a view that we have communicated at both the sector and Mexico Strategy levels since the beginning of 2019. An oft-repeated pushback from investors is that while the fundamental arguments are compelling, it is difficult to put them into action given how quickly stock liquidity falls off after FUNO. And, frustratingly yet similar to much of the Mexican market, this has been deteriorating as the year has progressed.

Chart 33: Mexican Real Estate – ADTV US$m (4 month trailing average)
Fibra Uno – In a league of its own...but still lower

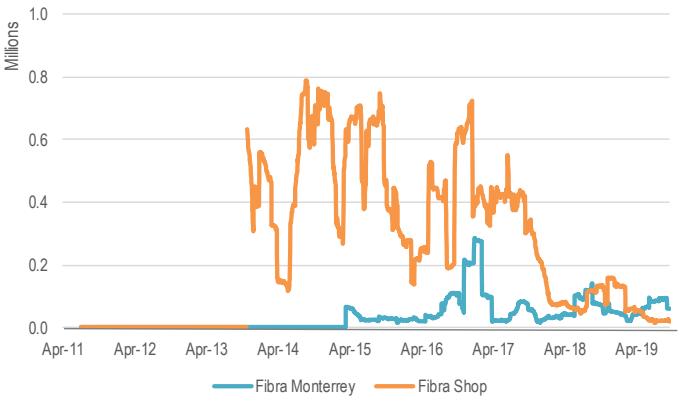
Source: Company Data, Bloomberg, BTG Pactual

Chart 34: Mexican Real Estate – ADTV US$m (4 month trailing average)
Liquidity has come down for the industrial FIBRAs



Source: Company Data, Bloomberg, BTG Pactual

Chart 35: Mexican Real Estate – ADTV US$m (4 month trailing average)
Fibra Shop and Fibra Monterrey



Source: Company Data, Bloomberg, BTG Pactual

"Paradox of choice" — there are simply too many names

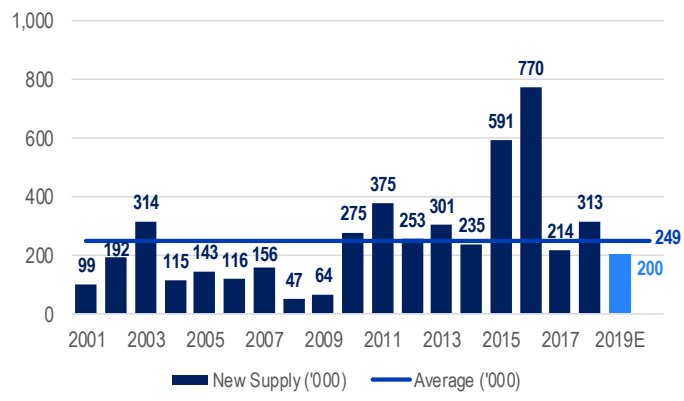
At last count, there are 14 publicly traded real estate FIBRAs, which rises to 18 stocks once adding the handful of C-Corps also listed. Only FUNO reliably trades above US$5 million per day, while another four (Vesta, Fibra PL, Fibra MQ, and Terra) trade US$1-2 million. The remaining 12 all trade well below US$1 million and some do not even reach US$100,000. This seems at a minimum inefficient and

produces rather a "paradox of choice" for investors that we believe leads to lower valuations, lower stock liquidity, and more intra-sector trading than would otherwise exist. As noted above, the rationalization of this offering is impeded by governance-related obstacles to consolidation. Until these are removed, or the discounts of underperforming assets become so large versus the better managed entities that a an undue consideration to management teams for the being made redundant is still economically viable, this paradox of choice will remain a thorn in the sector's side.

Office remains oversupplied

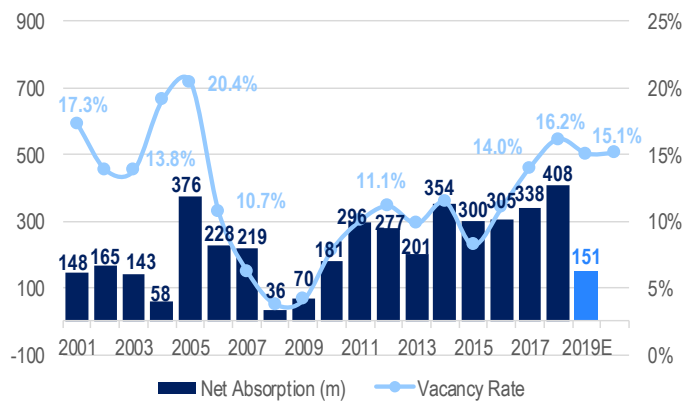
Of the three main segments represented in public equity markets, office remains by far the most challenged from a demand-supply standpoint. At 15% current vacancy, CDMX is already oversupplied even before it is faced with the entry of new inventory equivalent to 24% of existing GLA over the next two years. As mentioned above, office represents only 15% of our nine-company sample NOI, the smallest of the three segments. Among the companies we cover, FMTY has the most exposure to office with 47% of NOI (though only 3% of total NOI this is from offices in CDMX), followed by Danhos (36%), followed by FUNO (19%), and Fibra MQ (4%).

Chart 36: Mexico City Office Class A/A+ New Supply ('000 sqm)



Source: CBRE, BTG Pactual Estimates

Chart 37: Mexico City Office Class A/A+ Historical Net Absorption ('000 sqm)



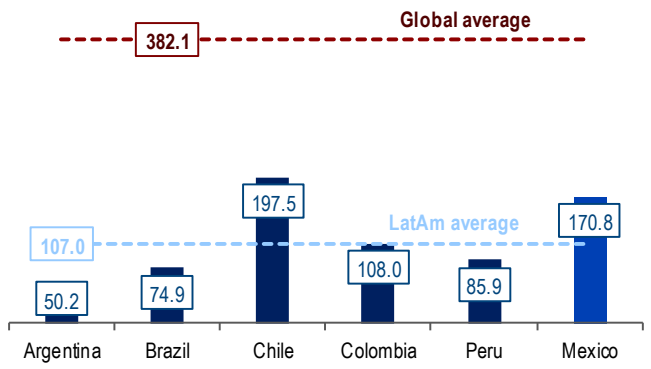
Source: CBRE, BTG Pactual Estimates

Please see Appendix 7 for more data on the Mexico City office space.

Mexican retail is arguably overpenetrated relative to regional and GEM peers

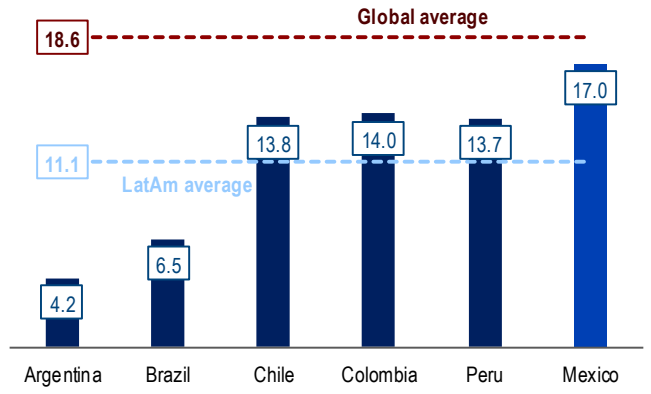
The Mexican consumer remains healthy, which has led to strong results from the retail portfolios in our sample. Occupancies have continued to tick higher and leasing spreads, for the most part, are rising well above inflation. However, as we have argued in past reports, relative to most large Latin American cities, **CDMX, Monterrey, and Cancún, which concentrate 60% of our sample's retail exposure**, are arguably close to being overpenetrated, which could make these markets vulnerable to a downturn. Among the companies we cover, FSHOP and Planigrupo are the most exposed to retail with 100% of their NOI, followed by Danhos (64%), FUNO (50%), Fibra MQ (18%), and FMTY (3%).

Chart 38: GLA/capita – LatAm countries vs. global average



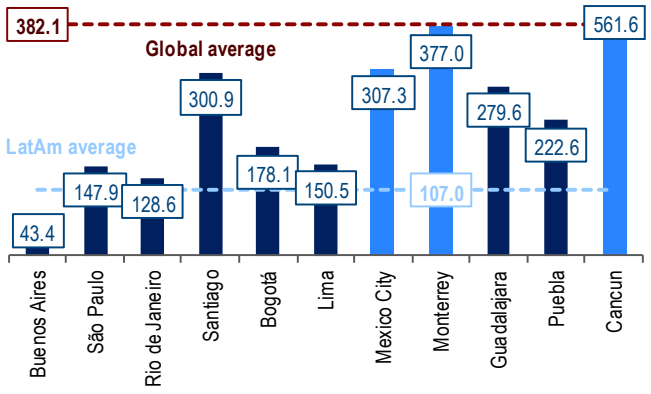
Source: World Bank, SCCA, ICSC, BTG Pactual

Chart 39: GLA/GDP – LatAm countries vs. global average



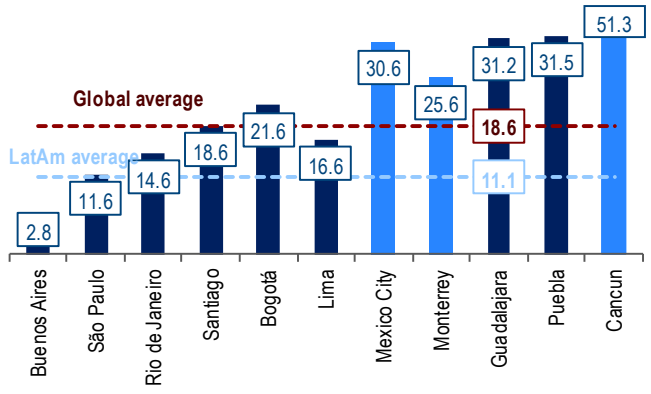
Source: World Bank, SCCA, ICSC, BTG Pactual

Chart 40: GLA/capita – Metropolitan regions vs. Global and LatAm



Source: World Bank, SCCA, ICSC, BTG Pactual

Chart 41: GLA/GDP – Metropolitan regions vs. global and LatAm



Source: World Bank, SCCA, ICSC, BTG Pactual

The Mexican macro situation could deteriorate further

Anybody who has followed the Mexican economy and market over the past year can attest to the ongoing deterioration in macro conditions and expectations. Expectations for GDP growth in 2019 were above 2% at the beginning of the year and have declined steadily to around 0.5%. At this point, estimates for 2020 are a bit better, but at 1-1.5% are hardly inspiring, especially if one assumes that they end up following the same downward path that growth expectations have followed in each of the past six years. Given the real possibility of escalating policy errors along with a more muddied growth outlook globally, there seems to be a real risk that GDP expectations slide further, which would be particularly negative for both the retal and office segments.

Could policy missteps take the shine off Mexico's manufacturing renaissance?

As we argue above, one of the characteristics that we like about Mexican industrial real estate assets is their relative immunity (and, perhaps, even negative correlation) to domestic economic growth and policy. Under most scenarios, this should remain the case, which is an important reason why industrial real estate has featured prominently in our Mexico 5SIM portfolio throughout 2019.

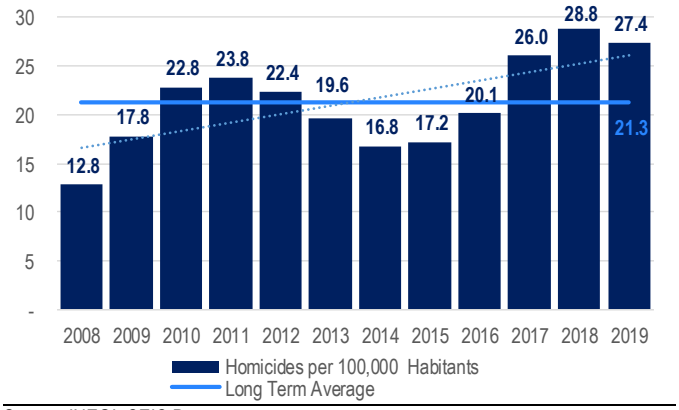
However, being largely immune is not the same as being completely immune, and we see a handful of areas where manufacturing could be derailed by domestic policy decisions. The most important is what a loss of Mexico's sovereign **IG rating** would mean for the availability and terms of real estate financing. We discuss this in detail below.

Beyond this, we would point towards taxes and public safety as the two areas where policy decisions could impair the attractiveness of Mexico as a global or regional manufacturing base. On **taxes**, it is generally expected that the AMLO administration will pursue a tax reform following the 2021 mid-term elections. Though details are naturally scant, it would appear that through a combination of measures at the local and federal level, Mexico would seek to raise additional revenue equivalent to at least 2% of GDP. Given the left-of-center tilt of the AMLO administration, we would assume that it would seek to avoid taxes on consumption or any levy that could be construed as regressive, meaning that the bulk of the burden is likely to fall on the corporate sector.

If so, this would widen the gap between Mexican and US corporate tax rates even further, negatively impacting Mexico's competitiveness vis-à-vis the US. To a certain degree, this already happened owing to the recent Trump tax cuts, but its effect on Mexican competitiveness was absorbed by the weak MXN. Presumably, the same would happen this time around, but it is not guaranteed, particularly with Banxico acting as a vigilant hawk.

One thing that cannot be solved through currency depreciation, however, is **worsening public safety**. This has been an issue that has plagued Mexico for over a decade now and, for the most part, it would seem that it has not been a major irritant for Mexican manufacturers. However, most statistics would suggest that, similar to what we have seen in other federal government transitions, crime rates are once again increasing (for instance, homicides in the first nine months of the AMLO administration are already higher than in all of 2018, which was the previous record). Thus far, it again does not seem to have impacted the industrial economy (though it seems to be affecting tourism flows at the margin, which is bad for retail and hotel properties in resort areas), but there is no guarantee that it won't do going forward. And policy decisions that negatively impact growth rates or that affect the way that the newly-minted National Guard is deployed (e.g., using it to stem Central American immigration instead of combating criminality) could eventually have an adverse impact.

Chart 42: Homicides per 100,000 Habitants



Source: INEGI, CEIC Data

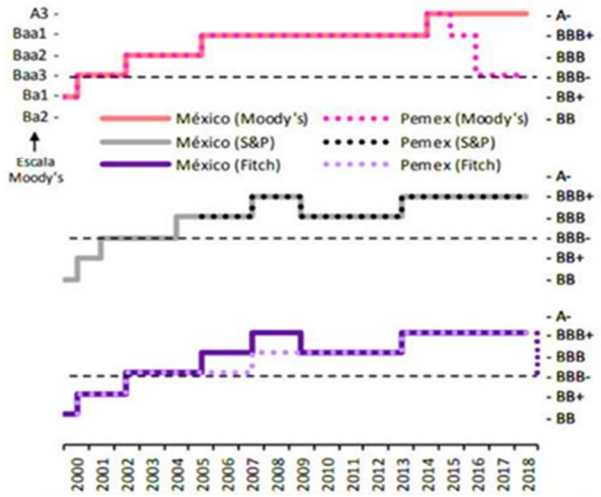
A loss of IG woud dent appetite for all Mexican assets, especially those that are interest rate sensitive

We see three levels of impact from a loss of IG. First, it would put **an additional damper on economic activity** given the damage it would do to the investment climate. Domestic private investment and FDI would likely suffer further as companies reconsider the wisdom of directing additional capital towards Mexico. This would affect all three segments, with retail suffering from lower consumption, office from a loss of business confidence, and industrial from the impact on FDI.

Second, it would likely send yields across the MXN curve significantly higher, **impairing valuations** of real estate assets in both private and public markets.

And third, the jump in **Mexico's cost of capital would make the financing of real estate portfolios that much more expensive**, reducing the amount of leverage that MXN-denominated assets could sustain. To a point, we have seen this already with the rise in yields seen in Mexico since the election of Donald Trump. FSHOP is a case in point: though they have continued to deliver significant increases in NOI, the rise in their funding costs has meant that a significantly lower share of these gains has reached equity holders. And this occurred during a period of time where operating drivers remain healthy. Should Mexico lose its IG rating, not only would the cost of funding rise, but economic activity would likely take a serious hit, squeezing profitability from both ends.

Chart 43: Mexico's debt credit rating evolution - Moody's, S&P and Fitch Credit Rating evolution on Mexican Debt Credit Rating



Source: Moody's and Fitch Credit

It is **not clear exactly what the long-term impact would be for industrial assets**. Initially, we would expect them to be caught up in the volatility, suggesting that active balance sheet management and de-risking today should be encouraged even for industrial players. Eventually, however, lenders would realize that their cash flows are in USD, that underlying economic exposure is global (and, primarily, US), and that the credit standing of most tenants would not be impacted by the Mexican yield curve. This would suggest that funding costs for industrial portfolios should eventually move back towards more normalized levels. However, even then we would expect that terms would be less generous and that financing would have to be asset-backed, leading to higher encumbrance and, therefore, reduced flexibility for borrowers.

USMCA is not yet law

We think that most of the NAFTA-related risks are behind us, but until USMCA is law, there is always a possibility that they could resurface, particularly given President Trump's and some leading Democratic presidential candidates' disdain for free trade. Our base case is that, given Democrats' likely reticence to hand President Trump any legislative victory, it is increasingly unlikely that USMCA will be ratified by the US Congress until after the November 2020 presidential elections (Mexico's Senate already has and nobody anticipates difficulties of its approval by Canada's Parliament). And, should a Democrat win, we would not rule out an additional round of negotiations aimed at further tightening up labor and environmental regulations, in what would essentially be a replay 27 years later of what happened to NAFTA when Bill Clinton defeated President Bush.

Labour unrest could hinder the case for manufacturing in Mexico

The beginning of 2019 brought with it a rise in labor unrest, perhaps in part because workers and their leaders felt emboldened by AMLO's rise to power and since Congress was set to debate a new Labor Law. One of the focal points of the unrest

was the Tamaulipas border region, which is a market that is relevant for a number of industries including autos but that features less prominently in publicly traded industrial real estate portfolios since, having been afflicted by high crime rates, it has been avoided.

AMLO seems to have taken a role in defusing the tension and the Labor Law, which was ultimately an exercise to comply with USMCA, was approved without further fanning of the flames. However, the spread of such labor dispute to other markets, particularly if encouraged by AMLO or his party, would certainly dampen enthusiasm for investment in Mexican manufacturing.

There continues to be the risk of a misalignment of interests between FIBRA managers and their equity holders…

As we argued earlier, these risks are mitigated at present by the depth of the discount at which publicly traded real estate stocks trade. However, should there be a re-rating that takes valuations to levels approaching NAV, it would be difficult to rule out a re-surfacing of the dilutive behavior that has so irked investors and dented the sector's reputation.

...and attempts to address this might make matters worse: We said earlier that the mere fact that FIBRAs recognize that their external management structure is a source of grief for shareholders is a positive. However, an ill-conceived effort to address this might have little impact (e.g., FINN) or, worse, represent a step back (e.g., FSHOP's partial internalization), particularly with regards to the issue of what consideration FIBRA owners should pay the management company to take it in-house. As long as stocks are trading at discounts to NAV, it is difficult to justify any transaction for the same reason that issuing stock for any purpose is presently questionable. But, once valuations normalize, both the manner and terms of the negotiation between the FIBRA and its managers is riddled with risks.

A US or global recession could reduce investment in manufacturing

This is an obvious risk and one that hardly needs highlighting, but suffice it to say that any global manufacturing hub would be impacted by a slowdown or outright contraction in growth. For Mexico, given that still some 80% of exports go to the US, a recession there would be particularly damaging. Yes, there is an argument that a recession would lead to a need to cut costs further, likely resulting in increased market share by Mexico in NAFTA manufacturing, particularly of autos. But it is difficult to deny that the initial impact of any slowdown in the US would be negative for Mexican exports and FDI into manufacturing activities.

Land is plentiful in both Ciudad Juárez and Bajío, suggesting tight industrial markets could quickly become loose ones

In our recent conversations with industrial developers and brokers, it is clear that appetite to develop, while improving, remains timid, highly selective, and largely opportunistic. However, as Mexico's key industrial markets continue to tighten, the incentives to begin developing more aggressively will grow. And it just so happens that Mexico's main industrial markets, Ciudad Juárez and Bajío, are both regions with good infrastructure and plentiful land. All in, it takes 18-24 months before inventory

hits the market, so a glut should become apparent ahead of time, but of the three segments it is the one with the **shortest development cycle and the lowest barriers to entry.**

Global liquidity conditions could turn at any moment

As we saw recently with the market's reaction to the FED's commentary following its August rate cut, markets can be somewhat whimsical when it comes to their stance on monetary policy. Enthusiasm about improved liquidity can suddenly turn into the deepest disappointment. Or, worse, inflation fears, now dormant, could re-surface, leading to tighter conditions almost overnight. Given signals that global growth is softening, this would seem a relatively remote risk at the moment. But it's worth reminding readers that as recently as nine months ago the expectation was that the FED would tighten two or three times in 2019.

Though limited, there are some regulatory and political risks

One of the reasons that we like the real estate space is that it offers interest rate sensitivity without the regulatory or political risks that infrastructure/concessions carry. Nevertheless, the risk is not nil. For instance, CDMX's local assembly recently attempted to pass legislation that would significantly increase the legal rights of squatters, reversing course only after significant public pressure and the leaning in of the AMLO administration. Similarly, CDMX halted construction on dozens of commercial and residential projects in February on account of a policy of revisiting environmental licenses. In spite of significant public pressure to restart construction given its effect on economic activity, work on the bulk of affected projects remains suspended. What's to say that a municipality in Chihuahua or Querétaro won't do the same on the industrial front?

There are specific FIBRA regulatory risks as well

Though the success of FIBRAs as an asset class is debatable among investors, for policy makers it is generally seen as a win. It has brought savers and investors together, channeling billions of USD into the market, sparking investment, and boosting economic activity. Moreover, it is likely to have brought many real estate assets into the formal sphere, increasing fiscalization via witholding taxes on dividends. Nevertheless, FIBRAs are certainly tax-enhanced vehicles that, while good for savers, are not at present investing heavily. For a government that is starved of revenue and in need of boosting investment, the wisdom of providing FIBRA owners with a number of tax incentives could come into question, particularly given that this administration is likely to pursue yet-another-tax reform following the 2021 midterm elections.

Trump, tariffs, and the US electoral cycle

It is well-known that President Trump has an animosity towards free trade and in particular multilateral agreements: NAFTA/USCMA is both. It is also well-known that he likes to use tariffs as a means of securing various ends, such as help on curbing immigration or, in the case of Europe, a pledge to raise defense spending. And it is also well-known that he is at his most comfortable when on the campaign trail, that

his base shares many of his misgivings on trade and immigration, and that the US electoral cycle is long, has already begun, and is often acrimonious. All of this means that it is likely that Mexico will feature prominently in the forthcoming presidential elections; it is also a good money bet that this prominence will not be flattering. It is therefore impossible to assume that threats such as those seen last May on tariffs will not be repeated.

Technological shifts — automation and EVs and the impact on industrial real estate

This is, arguably, the most important long-term risk for Mexican industrial real estate's investment case. Because of this, it is something that we will explore more deeply in a stand-alone report. Suffice it to say for now that the move towards automation and, more relevantly, away from the internal combustion engine is a material risk as it pertains to long-term demand for industrial real estate space in Mexico. To make an obvious point, automation levels the field when it comes to labor costs. Further, the move away from internal combustion engines considerably reduces the complexity of manufacturing a car, significantly decreasing the amount of parts required and, thus, the number of suppliers involved in the production chain. Offsetting this is the fact that the life of EVs is likely to be shorter than that of today's fleet, but it is unlikely to mitigate the risk entirely.

E-commerce and its impact on retail

Needless to say, technology is also impacting Mexico's retail space in the same way that it has elsewhere in the world. The proliferation of e-commerce, while still at a relative infancy in Mexico, will clearly not pass the country by. Yes, the complexity of distribution in Mexico is an impediment. Yes, the size of the informal economy and the prevalence of cash it produces is an impediment. And yes, the relative youth and positioning of retail assets as destinations and entertainment centers is a significant defense. But eventually e-commerce will make inroads and this will put certain retail properties at risk, while highlighting the value of others. And the risk that Mexican retail assets suffer a de-rating in line with retail assets in the US is not trivial.

The sharing economy is also impacting the office market

As is the case with e-commerce, the trends affecting the office segment in the rest of the world will not bypass Mexico. In fact, it is arguably happening at a faster pace than e-commerce as evidenced by the proliferation of WeWork offerings (which has selected FUNO as its partner of choice in Mexico and now has tenants such as ABI [Modelo] and Grupo Lala) since many of the roadblocks affecting e-commerce are not relevant in the office space. This could make a challenging situation in Mexico's office market even worse. However, as noted above, office's share of publicly traded NOI is small.

Valuation, Price target, and recommendation

We discussed many of the salient aspects of the sector's valuation and their current yields and cap rates at the beginning of this note, so some of what we say here might be repetitive. As argued above, Mexican real estate stocks are attractive through almost any prism, including discounts to NAV, cap rates and yields and the spreads they represent to base rates, and relative to the valuation of assets in private transactions. But unlike the introductory section in which we speak about the sector generically, in this section we bring it down to the stock-specific level as a way of understanding our relative preferences for stocks within the group.

Moreover, in this section we focus on the methodology behind our price targets as these lead to our recommendations on the stocks. We also compare the implied valuation metrics at our price target for each stock to its historical range as a sanity check to assess whether our price targets are realistic, particularly on an NAV basis. In addition to the sanity check it provides, it also helps to understand whether the risk of another round of equity issuance by FIBRAs is high in that we would expect most managements to avoid selling their own equity at a cap rate that is above what they would pay for assets.

C-Corps vs. FIBRAs and what this means for valuation

Before jumping into the numbers, we think that a brief discussion of the implications for relative valuations between C-Corps and FIBRAs is in order, particularly since this distinction has come up repeatedly throughout this report in the context of governance, alignment of interests, and capital allocation. As a reminder, a C-Corp is a real estate developer or owner/manager of assets that is set up as a corporation. This means that it has a fully internalized management structure and, importantly, has none of the tax benefits or ensuing obligations to distribute earnings of REITs or FIBRAs (we present a detailed discussion on these benefits and obligations, and what they mean for FIBRA investors, as an appendix to this report [Appendix 10]).

It also means that relative to the way most Mexican FIBRAs (i.e., with external management structures that pay their managers on the basis of NAV or NOI) are set up, C-Corps are more capable of achieving economies of scale and therefore internalizing for their shareholders the full benefits of growing their portfolios and operating platforms. From a governance standpoint, in general alignment is better for C-Corps, reducing the risks of making capital allocation decisions that do not fully represent the best interests of shareholders is lower.

For all these reasons, **we would expect C-Corps to trade at premiums to FIBRAs on P/NAV and on implied cap rates. In the case of Mexico, they do**: on a P/NAV basis, the two C-Corps we cover (Vesta and Plani) trade at 1x 2019 NAV, well above the 0.73x at which the seven FIBRAs that we cover trade. The same goes for implied NOI and EBITDA cap rates, where the C-Corps trade between 150-200bps inside of the FIBRAs.

The same is true for FFO and dividend yields, though at this level the difference in tax treatments becomes part of the conversation. C-Corps, as regular companies, pay taxes the way a normal company would, meaning that the FFO and

dividend yields they trade on are post-tax numbers. Moreover, because they are companies and not FIBRAs, once a C-Corp pays taxes it is at full liberty to use its earnings any which way it wants, including full retention if it so chooses.

FIBRAs, like REITs, do not pay corporate taxes and in exchange are obligated to pay a minimum 95% of its taxable earnings as dividends. Most Mexican FIBRAs, however, choose to pay more than this (since under normal circumstances their AFFO is likely to be twice the level of their taxable net income), in which case they are also "returning capital" to their investors. The investors that receive distributions from FIBRAs have to pay withholding taxes on the dividends they receive but collect capital returns free of taxes. How each of these is split will depend on the shape of the tax P&L of each particular FIBRA (in recent years, industrial FIBRAs, who have booked large FX losses on their USD debt, have mostly distributed capital returns, while the MXN-driven ones tend to pay a greater share of dividends).

Thus, when comparing FFO and dividend yields of C-Corps and FIBRAs, investors should take into account that the figures for C-Corps are after-tax numbers while those for FIBRAs are pre-tax yields that, depending on each case, they might have to pay taxes on upon receipt of distributions. Moreover, the payout ratios could be different, so some allowance for the potential additional growth and returns that C-Corps offer should be made as well.

As should be expected, our C-Corp sample does, indeed, trade on lower FFO and dividend yields than the FIBRAs (by some 500bps at the dividend yield level).

Bringing the conversation to the stock level, we would note that Vesta, a C-Corp, offers in many respects FIBRA-like levels of valuation on a P/NAV of 0.8x, implied EBITDA cap rate of 7.4%, and dividend yield of almost 6% with all the governance and growth benefits of being a C-Corp.

Mexican real estate remains among the cheapest globally

As a group, Mexican real estate stocks trade on 2019 implied EBITDA and NOI cap rates of 8.2% and 9.1%, which represents an average spread to their relevant base RFR of 510bps. On an EBITDA implied cap rate basis, Danhos's 10.3% is the cheapest among the stocks we cover, while Fibra PL's 7% is the tightest in the group.

The sample's average 2019 FFO yield basis stands at 9.2%, while the average dividend yield is 8%, a spread of almost 500bps to relevant base rates. On an FFO yield basis, relative valuations are similar, with Fibra MQ offering the highest at 12.6%, while Plani's 5.0% is the tightest. On a dividend yield basis, FSHOP's 10.3% is the most attractive (though, as we argue later in this report, we do not believe this is sustainable given its leverage levels), while Plani, being a C-Corp, has opted at present not to distribute dividends.

Finally, on a P/NAV basis, the average for 2019 is 0.79x, still some 20% below fair value as deemed by third party appraisers. Among the FIBRAs, the narrowest discounts to NAV are Fibra PL's and Terra's, while the widest is FSHOP. Vesta, in

spite of being a C-Corp, trades at a P/NAV valuation that is similar to the level seen by most of its industrial peer FIBRAs.

In our view, the best way to compare the Mexican real estate names to their international peers is on the basis of the cap rate spread they offer relative to their respective base rates. In the case of the Mexican names, we use the 10-year UDIBONO for the stocks that primarily generate MXN (FUNO, FSHOP, Danhos, and Plani) and the 10-year UMS for those who earn USD (Fibra MQ, Fibra PL, FMTY, Terra, and Vesta). For the US stocks we use the 10-year UST, while for those in Brazil and Chile we use 10-year real rates.

The conclusion is that across any meaningful sample of real estate stocks, the Mexican ones, relative to their own base rate, offer the highest spreads by a meaningful amount.

Relative to history, the Mexican real estate stocks still trade as a group at discounts to their long-term averages for implied cap rates, implied cap rate spreads, and P/NAV. There are some exceptions, namely Fibra PL and Danhos, that are trading above their long-term averages. That said, with the exception of FSHOP, all stocks have rebounded from the lows they reached at the end of 2018, which given lower global yields, monetary easing in Mexico, and the sheer magnitude of discount reached, some sort of bounce was clearly justified.

And, finally, the same can be said of the stocks' valuation level relative to real asset transactions. Though there are some outliers, the range for the bulk of transactions involving industrial assets has been 7-8%. Importantly, this has been consistent over time with that range holding true since 2012, regardless of both the global and the local interest rate environment. And this cap rate continues to be below the 8.8% NOI cap rate at which publicly traded vehicles trade in spite of the liquidity and diversification they offer. Moreover, as long as this continues to be the case, the decision for FIBRAs to raise capital to acquire portfolios, which in spite of the potential long-term benefits of a good acquisition brings with it the short-term irritant to shareholders of dilution, is rendered more difficult for managements to make.

What base rate to use?

Before moving onto the discussion of price targets and recommendations, one question that often comes up when speaking to investors is what base rate and what duration to use for assessing Mexican real estate assets.

Duration is, in our view, an easier one to answer, so we'll start there. Real estate assets, like equities, offer exposure to long-term cash flows. We therefore believe that the appropriate rate to discount them is at the longer end of the curve, which has led us to use the 10-year point, the same we do for our DCF valuations for regular equities.

Does this mean that what happens to short-term rates in Mexico is irrelevant for the FIBRAs and C-Corps under coverage? We have always said, and continue to believe, that investors should really focus on the long-end of the curve when thinking about real estate assets both for discounting cash flows and assessing cap rate or

yield spreads. This explains to us why, to a certain degree, FIBRA valuations began to re-rate before Banxico began easing since, following the spike in yields resulting from the NAIM decision, the long-term end of the curve began to normalize at the beginning of the year, in sympathy with rates elsewhere.

That, however, does not mean that short-rates are completely irrelevant. For one, because long-term yields are set by the market and base rates by central bank boards, the former tend to lead the latter, often in anticipation of expectations of easing. And the opposite is true when the market begins to anticipate tightening. This symbiosis between the ends of the curve necessarily means that what happens along the curve matters.

Second, there is also the more technical effect of opportunity cost, particularly at a moment in time when front-end rates are high and the yield curve still inverted. This can often make it difficult for investors who can invest in any asset to move out of short-term sovereign rates into an asset of longer duration with a lower yield. As front-end rates decline, the opportunity cost declines and duration risk becomes more palatable of switching into a longer-lived asset such as a FIBRA decrease.

The discussion around what base rate to use, however, has always been an area of debate. If we agree on the long-end being the benchmark, the first thought would be to use the 10-year MBONO, Mexico's equivalent of USTs. However, while this could be generically used for Mexican assets, the MBONO would seem to be imperfect for industrial or office assets (which generate USDs) or retail (the rents for which are indexed to inflation). We have therefore decided to use the 10-year UMS (USD-denominated Mexican government paper) rate for platforms that earn USDs and the 10-year UDIBONO (inflation adjusted Mexican sovereign paper) for retail assets.

A final question we are asked is, if industrial rents are also adjusted by US CPI during the life of the contracts, why not use an inflation-adjusted USD rate instead? The reason we have opted for a nominal yield is that Mexican industrial real estate rents have lagged US CPI over the long-run. This is not true in this environment of tight markets, but over the span of many years it has been, leading us to prefer to think of them as nominal, rather than real, USD earners. This stance is also true in the assumptions included in our long-term rent projections and in the terminal value of our DDMs, as discussed below.

Price target: DDMs for FIBRAs; DDM + exit cap rate for C-Corps

We are maintaining the same basic methodology for setting our PTs for FIBRAs and for C-Corps introduced when we initiated on Terra and Vesta in 2015: we use DDMs for valuing FIBRAs and a blended DDM+exit cap rate valuation for C-Corps (for a more detailed discussion please refer to *Industrious returns: Initiating on Terra and Vesta* from June 2015).

We have, however, introduced a few changes to the assumptions and the mechanics of each approach, explaining to a large degree the changes in the PTs for some of the companies under coverage. The main assumptions and changes include:

USD modeling and discounting for USD earners; MXN for MXN earners: Among the companies already covered, this affects Vesta, Terra, and Fibra MQ and FMTY and Fibra PL among the newly initiated stocks. These are all platforms that earn well over 50% of their NOI in USD, so instead of forecasting USD cash flows, converting them into MXN, and discounting them at a nominal MXN discount rate, we have decided to keep the USDs as USDs and to discount the dividends and cash flows on USD discount rates that kick off from the UMS 10-year yield as the RFR.

For MXN earners (FUNO, Danhos, FSHOP, and Plani) we have not changed our approach: we model in MXN and discount with an MXN cost of equity that kicks off the 10-year MBONO yield as the RFR.

For FIBRAs we project distributions on detailed cash flows through 2023 and generic distributions until 2038, at which time we discount the last year's dividend in perpetuity. The first stage of projections for our DDM valuations, through 2023, come straight from our model and include full P&L, cash flow, and balance sheet forecasts. The second stage runs on assumptions that directly drive the dividend (occupancy, rental growth, NOI and FFO margins, and payout ratios), and goes out the 20 years to 2038 by which time the existing asset base should be fully depreciated for purposes of tax accounting. The final stage, the terminal value of dividends calculation, capitalizes the 2038 dividend through a no-growth perpetuity on each FIBRA's estimated COE. Because the assets are fully depreciated, the assumption is that the entirety of the distribution is a dividend and, therefore, presumed to be taxed fully at a 30% withholding rate.

For C-Corps we project and discount dividends on detailed cash flows through 2025 and determine a terminal value based on an exit cap rate exercise in year 2026. Like with the FIBRAs, the first stage of our valuation comes straight from our model and reflects the stream of dividends as we expect it to actually occur. In 2025 we forecast the sale of all assets at a given cap rate (8% for Vesta and 8.5% for Plani, which are at the higher end of the range for precedent transactions in the private market), remove all liabilities, and discount the value to shareholders to the present on the companies' respective COEs.

Key operating assumptions: All our models consider existing GLA in addition to the development pipeline that has already been announced. We do not assume expansions beyond this nor do we model acquisitions. Occupancy rates are forecast to be more or less flat from existing levels and in Stage 1 of our projections we assume rental rates rising with inflation.

For the FIBRAs, our Stage 2 forecasts are slightly differentiated: for those that we model and discount in MXN, we assume zero leasing spreads and that rents rise in line with Mexican inflation, which we estimate at 3.5%. For those that we see as USD vehicles, in Stage 2 we assume zero leasing spreads and no inflation mark-ups. Though this might seem counterintuitive given how tight industrial markets are at the moment, over the long-run industrial rents in Mexico have been largely flat in USD terms. Though this could seem somewhat unfair to FMTY given that their USD exposure includes significant amount of office GLA, in the long-run we would argue that office rents have also remained flat in USD. Moreover, given the current state of

oversupply in the CDMX office market (which, admittedly, FMTY is not particularly exposed to) we would prefer not to assume any rental gains going forward.

The two exceptions to the zero Stage 2 rental growth assumptions among USD-denominated platforms are Fibra PL, where we assume they rise by 2% in nominal terms, and FUNO, where we assume leasing spreads of 0.5%. The exception for Fibra PL aims to make a consideration for the potential growth spurt from rising e-commerce penetration that its logistics exposure grants it. For FUNO, it aims to capture the upside to both its current rent levels (which the market strategically seeks to mark slightly below market) and the numerous redevelopment opportunities that much of its portfolio offers.

As for Stage 3, which is the terminal dividend discounted in perpetuity, we make similar assumptions for the FIBRAs: for MXN vehicles we have assumed 3.5% growth in nominal dividends, implying they remain constant in real, inflation-adjusted terms, while for those we see as USD-driven we have assumed zero nominal terminal growth (with Fibra PL once again being the exception, where we give it terminal growth in line with projected long-term US inflation of 2% to account for the growth potential from their logistics exposure).

Leverage assumptions: For the C-Corps, there is no real change in our methodology and the mechanics are pretty straightforward. Also, it is worth noting that by virtue of being regular companies and not FIBRAs, they do not face any regulatory restrictions or limits on leverage levels (FIBRAs can not exceed gross LTV of 50%), which gives them greater flexibility in terms of their balance sheet management. As a result, during Stage 1, net leverage declines or rises by the difference between AFFO, expansion capex, and distributions, which for Vesta means that it moves from 30% in 1H19 to 37% by 2023E and from 43% to 40% for Plani.

However, for the FIBRAs, the change to how we are dealing with long-term leverage in our models is probably the most deep-reaching and largely explains the downgrades of both Terra and FSHOP. We now assume that net LTV reaches 35% by the end of Stage 1 (i.e., 2023) for all FIBRAs we cover (with the one exception being Danhos, as discussed below). This means that for FIBRAs with net LTV levels below the stabilized level we assume the payment of an extraordinary dividend in 2023, while for those above the threshold we model a decline in payouts in 2022 and 2023.

Why are we doing this? Well, it is really intended to make the implied total returns to our DDMs for each of the FIBRAs under coverage more fully comparable. Because the DDM model simply discounts distributions during the life of the model and makes no adjustments for the ending capital structure, we were effectively rewarding companies with high leverage even if that leverage was above their target level or higher than one would like as a mid-cycle level. By stabilizing all FIBRAs at the same LTV, we feel that we are reaching price targets that are a truer gauge of the present value of the sustainable stream of distributions that each platform can deliver and normalize for any short-terms distortions of current balance sheet structures.

It's worth pointing out, however, that for the companies where the temporary reduction in dividends is material (e.g., FSHOP) the assumed payout in 2022 and 2023 may imply a distribution that is actually below regulatory requirements. We acknowledge that this not realistic and that in the real world a longer lead-time would be required for the balance sheet to stabilize. Because it's not clear that on a PV-basis this would have much of an effect and since we feel that it is better to have models that are truly comparable, we have decided we can live with this imperfection.

The one exception among the FIBRAs to all of this is Danhos, whose 10% net LTV is well below the 35% we have set. In this particular case, we have chosen to leave its leverage intact since its development pipeline is winding down to zero and management has been very clear that in the interest of prudence (arguably excessive) it is content with abnormally low levels of leverage. In spite of this lower net LTV, the P$36 price target that our DDM produces is enough to warrant a Buy rating (it yields a 34% total return). If we were to give it the same treatment as the others and assume a special dividend in 2023 that would take its net leverage to 25%, the resulting DDM target would be P$41, some 14% above our official PT and would imply a total return of 51% over current levels.

COE calculation: This one is fairly straightforward and the assumptions for each stock are outlined in Table 4 below. Most of the inputs are givens, though we make a few adjustments to account for qualitative factors that we think are important. For the RFRs we use the 10-year MBONO plus a 25bps spread (i.e., 7%) for MXN vehicles and the 10-year UMS plus a 25bps spread (i.e., 3.7%) for the USD vehicles.

We use **ERPs** of 500bps for all stocks except for 400bps for FUNO (owing to greater stock liquidity) among the FIBRAs and Vesta and Plani given the better alignment between management and minorities resulting from its C-Corp structure.

Finally, for **Betas** we use those produced by Bloomberg and then make adjustments if we feel that because of liquidity or other technical factors the observed Betas do not accurately reflect stock-specific risk. In general, for C-Corps we use a higher Beta of 1 to reflect the greater risk of development. Among the FIBRAs, we tend to assign higher Betas for companies that are more exposed to office and retail than to industrial to reflect our general segment preferences and to capture the greater cyclical risk of assets with greater exposure to the domestic economy at a time when its outlook is uncertain.

Table 4: Valuation and Price Target – Summary of BTG Pactual Coverage

In MXN

CAGR (19-23)	FUNO	Danhos	FSHOP	Planigrupo
Average GLA	1.4%	1.0%	1.5%	1.9%
Rental revenue/share (P$)	3.7%	0.3%	4.3%	6.3%
NOI (P$m)	3.7%	2.9%	4.5%	6.3%
EBITDA (P$m)	4.0%	3.2%	4.4%	6.4%
FFO (P$m)/sh	3.3%	3.5%	2.8%	11.9%

Model Assumptions	FUNO	Danhos	FSHOP	Planigrupo
Rents growth (%) DDM	3.5%	3.5%	3.5%	NA
Leasing Spreads (%)	0.5%	0%	0%	NA
Terminal Value Growth (%)	3.5%	3.5%	3.5%	3.5%
Net LTV (%) '23	35%	10%	35%	NA

Key Metrics	FUNO	Danhos	FSHOP	Planigrupo
P/NAV (P$)	0.78	0.68	0.40	1.13
P/NAV (US$) at target	0.94	0.91	0.40	1.28
Implied EBITDA cap rate (%)	7.3%	10.5%	8.7%	8.3%
EV/GLA (P$)	21,654	47,382	25,192	20,192

Cost of equity calculation	FUNO	Danhos	FSHOP	Planigrupo
Risk free rate (%)	7.0%	7.0%	7.0%	7.0%
ERP (%)	4.0%	5.0%	5.0%	4.0%
Beta (Bloomberg)	0.75	1.00	0.90	0.95
Cost of equity (%)	**10.0%**	**12.0%**	**11.5%**	**10.8%**

WACC calculation	Planigrupo
Cost of debt (%):	8.0%
Cost of equity (%):	10.8%
Tax rate (%)	30.0%
WACC (%):	**8.7%**
Exit Multiple (x)	**8.5%**

Valuation	FUNO	Danhos	FSHOP	Planigrupo
TP BTG Pactual (Old)	**36.5**	**NA**	**16.0**	**NA**
TP BTG Pactual (New)	**34.3**	**36.2**	**8.5**	**21.5**
Current Price (Today)	**28.7**	**27.1**	**8.4**	**19.0**
Upside (%)	20%	34%	2%	13%
(+) Dividend Yield (%)	8.1%	9.1%	10.3%	-
Upside inlcuding dividends (%)	**28%**	**43%**	**12%**	**13%**

In USD

CAGR (19-23)	Fibra MQ	Terra	Vesta	Fibra PL	Fibra MTY
Average GLA	0.3%	0.4%	6.4%	0.0%	0.4%
Rental revenue/share (US$)	1.0%	1.5%	7.9%	2.2%	1.3%
NOI (US$m)	1.6%	1.3%	8.0%	2.2%	1.2%
EBITDA (US$m)	0.7%	1.5%	7.8%	2.4%	1.0%
FFO (US$m)/sh	1.5%	2.1%	11.6%	4.7%	-1.6%

Model Assumptions	Fibra MQ	Terra	Vesta	Fibra PL	Fibra MTY
Rents growth (%) DDM	0.0%	0.0%	NA	2.0%	0.0%
Leasing Spreads (%)	0%	0%	NA	0%	0%
Terminal Value Growth (%)	0.0%	0.0%	0.0%	2.0%	0.0%
Net LTV (%) '23	35%	35.0%	NA	35%	35.0%

Key Metrics	Fibra MQ	Terra	Vesta	Fibra PL	Fibra MTY
P/NAV (US$)	0.69	0.88	0.84	0.88	0.86
P/NAV (US$) at target	0.87	0.91	1.05	0.99	0.98
Implied EBITDA cap rate (%)	9.4%	7.8%	6.5%	7.0%	8.0%
EV/GLA (US$)	569	569	688	638	914

Cost of equity calculation	Fibra MQ	Terra	Vesta	Fibra PL	Fibra MTY
Risk free rate (%)	3.7%	3.7%	3.7%	3.7%	3.7%
ERP (%)	5.0%	5.0%	4.0%	5.0%	5.0%
Beta (Bloomberg)	0.85	0.75	1.00	0.75	0.90
Cost of equity (%)	**7.9%**	**7.4%**	**7.7%**	**7.5%**	**8.2%**

WACC calculation	Vesta
Cost of debt (%):	6.0%
Cost of equity (%):	7.7%
Tax rate (%)	30.0%
WACC (%):	**6.4%**
Exit Multiple (x)	**8.0%**

Cost of equity calculation	Fibra MQ	Terra	Vesta	Fibra PL	Fibra MTY
	30.0	**30.0**	**33.0**	**NA**	**NA**
TP	**31.3**	**31.7**	**38.2**	**46.2**	**13.7**
Current (today)	**24.8**	**30.5**	**30.5**	**41.0**	**12.0**
Upside (%)	26%	4%	25%	13%	14%
(+) Dividend Yield (%)	7.0%	8.3%	4.6%	6.0%	9.3%
Upside inlcuding dividends (%)	**33%**	**12%**	**30%**	**19%**	**24%**

Source: BTG Pactual, Company Data, Bloomberg

Price targets and ratings

Putting all of this into the blender of DDM models for FIBRAs and DDM+Exit Cap rate exercises for C-Corps, we end up with 12-month price targets and total return projections as described in Table 4.

On the basis of the projected upside, among the companies under coverage **we maintain our Buy ratings on Fibra MQ, FUNO, and Vesta and downgrade Terra and FSHOP to Neutral. Among our expanded sample, we initiate coverage on Fibra PL, FMTY, and Danhos as Buys and on Plani with a Neutral**. As a result, of the nine stocks in the sector that we cover, two-thirds are rated Buy and one-third Neutral, which we find consistent with our favorable view on the space.

A sanity check: To verify that our PTs make sense and are consistent with historical valuations and other important markers, we have also shown in Table 4 the implied future P/NAV and 2020 implied EBITDA cap rates for the stocks under coverage compared to their existing level, the long-term average, and the peak level.

For all FIBRAs, the P/NAVs at our price target remain below 1x, which we believe makes sense since, unless we think there is something like a sudden and permanent shift in long-term interest rates that would drive a fundamental re-rating or de-rating of real asset valuation, we consider that externally managed structures should be

trading below NAV. Though this is a controversial assertion, if the underlying assets are properly appraised, we believe that a FIBRA's value should be its NAV less the PV of the fees charged to investors for managing those assets, which will be somewhere in the vicinity of 0.9-0.95x NAV.

For internally managed structures or C-Corps, however, where there is no fee structure that prevents scale benefits to accrue to shareholders, we believe that fair valuations could trade above NAV as each additional asset that is added to the platform enhances the value of every existing asset as well. Seen in this light, we are comfortable with the P/NAV range that our price targets imply for the stocks under coverage.

And the same is true for their implied cap rates as these are generally consistent with their own historical trading ranges and with valuations paid for comparable assets in the private market.

Fibra Uno (Buy): Still in a league of its own...

FUNO: in a league of its own

FUNO stands out from publicly traded peers across almost any metric: its market cap of US$5.3bn and ADTV of US$8.3m is equivalent to that of its four next competitors combined, while its GLA of 8.7m sqm and NOI of P$14.4bn is equal to the sum of Danhos, Terra, Fibra MQ and Fibra PL. From an operating standpoint, this size and diversification should mitigate risk, particularly since it also boasts many of the country's fortress properties. From an investment standpoint, its greater liquidity makes it the only feasible option for many investors in a sector that is our preferred in Mexico and one of our favorites regionally. Yet, as we discuss below, its valuation hardly reflects these advantages.

Bye bye dividend dilution - at least for now

For some time, the growth in FUNO's per CBFI metrics lagged its top line given the impact of several share offerings and share-based payments for assets. Because this affected distributions directly, it has been a source of frustration for investors and a constant reminder of their concerns on governance. However, as M&A activity has slowed, growth in per CBFI metrics has caught up to the top line, particularly since 4Q18. Going forward, the self-imposed issuance restrictions put into effect in 2017 should reduce dilution risk significantly (at least until the stock reaches a P/NAV of 0.9x, some 15-20% above current levels).

Key risk: governance of conflicts of interest...

There is nothing new here: this has been the stock's key risk since its IPO and will almost certainly continue to be as long as it remains externally managed, which is likely to be the case for the foreseeable future in spite of management's recognition that this should eventually be addressed. The irony is that the source of this risk - its relationship with its sponsor, E-Group - is also one of FUNO's main strengths, which in many ways means that it is structural to the investment case and one that minority investors will have to monitor permanently even as management does its best to mitigate it.

We reiterate our Buy rating on FUNO shares

In spite of all the advantages we discuss throughout, FUNO valuation has continued to de-rate even within its peer group to the point that its historical premium has morphed into a discount. Trading on a P/NAV of 0.78 and 2019E implied EBITDA cap rate and dividend yield of 7.3% and 8%, we find valuation compelling. With 28% total return to our DDM-driven P$34.3 PT, we reiterate our Buy rating on FUNO shares.

Investment case: The Positives....

In a league of its own in terms of size, diversification, and stock liquidity. Despite the listing of 12 FIBRAs and five C-corps since its IPO in 2011, FUNO remains far-and-away the largest, most diversified, and, importantly, most liquid property stock in Mexico. With a 2019E NOI of P$15.1 billion, it is 3x larger than its closest peer, Danhos; in fact, it is equal to its next four peers combined. It is the only listed player with exposure to retail, industrial, office, and hotels and, with presence in all of Mexico's 32 states, it is also the most diversified by region. Most importantly, however, its stock liquidity, which at US$8.3/day is 4.5x higher than its closest peer, Vesta, and equal to its next nine combined. This is important because it makes FUNO the only Mexican real estate game in town for many investors.

A portfolio that boasts some of Mexico's fortress assets, making FUNO the first choice for many strategic partners and tenants. In a portfolio as large as FUNO's (537 properties with 8.7m sqm of GLA), there is bound to be a bit of everything across the quality spectrum. However, of all the listed property portfolios, FUNO's without a doubt concentrates the largest number of flagship assets (we estimate 13% of FUNO's NOI stems from flagship properties). Though this is true across all segments, it is especially so in office, which in spite of its operating challenges renders FUNO's offering more defensive. It also explains why its retail portfolio has consistently outperformed peers on rental growth and leasing spreads. This overall quality, in our opinion, positions FUNO uniquely among its peers and makes it the first choice for many strategic partners and/or tenants (e.g., Reichmann, Hilton, etc.).

E-Group's sponsorship grants FUNO a great deal of flexibility and optionality for growth and portfolio construction. Though the relationship with E-Group is at the core of some of the governance concerns around the stock, the fact is that is also supplies FUNO both with a constantly renewed, high-quality acquisition pipeline and with development expertise that it regularly imports in-house. This is magnified by Helios, a development platform also sponsored by E-Group and capitalized by Mexican pension funds that serves as another feeder for FUNO while generating management fees for its shareholders, as has already been the case with Mitikah, Latin America's largest mixed-use project under development. All of this provides FUNO with an array of growth avenues that is simply not available at all, or to nearly the same degree, to any other of its listed peers.

Per CBFI metric growth has finally caught up to the top line... Until this year, FUNO shares had underperformed the market for an extended period of time due largely to the same macro and industry-wide issues that plagued the entire sector. However, there was one relevant idiosyncratic driver to this underperformance, which was the lag in per CBFI growth metrics, including distributions, derived from the dilution that stemmed from both equity issuance and payment of past acquisitions in shares. This drove a large gap between high levels of growth for revenue, NOI, FFO, and (controversially) fees and that of DPCBFI, which was often cited as a source of frustration by investors, particularly local pension funds. This came to an end with 4Q18 results, with per CBFI metrics now growing at a par with the top line and DPCBFI up 8.8% YoY in 1H19.

...with future dilution somewhat mitigated by self-imposed issuance constraints. Because of concerns around continuous dilution were exacerbated by worries that the company's fee structure (i.e., the existence of its M&A fee) and its sponsorship by E-Group (which still holds a number of assets that could eventually be transferred to FUNO) represented incentives to be overly acquisitive, FUNO bowed to investor demands during its last equity placement in 2017 that it restrain its own ability to issue shares to the market or to asset sellers. These constraints effectively prohibit FUNO from issuing any new shares at a price below 0.9x P/NAV, which at 15% above current levels (over 20% including the dividend), means that the stock has significant room to re-rate before investors need to worry about dilution.

Investment case: Negatives & Risks....

Governance concerns are always part of the conversation. The volume and frequency of investor concerns around FUNO's governance (independence of board, fee structure, and potential for conflicts of interest between FUNO and E-Group) naturally wax and wane depending on the stock's performance. But, though they might wane when investors are making money, they never fully disappear even then and are almost invariably the first "but" or "if" that investors counter our Buy rating with. This will likely not disappear until FUNO is fully internalized, which management has begun to discuss openly. But we fear that this is far off into the future and that until then the concerns will persist; in fact, they could actually increase further precisely because of some of the decisions and discussions that any internalization process will require.

It is so large that very little moves the needle; it also makes analysis difficult. As already discussed, FUNO is many times larger than any of its peers. While this is a positive when viewed through the lens of diversifying risk or of stock liquidity, it is a negative in that there is little that moves the needle operationally. This is true in in terms of an acquisition or development, but it has been apparent even more recently when it divests from assets. FUNO's sheer size also makes analysis difficult, both in terms of understanding the existing portfolio and assessing the contribution or performance of properties that are acquired or developed, which is used as fodder by the critics of its governance of conflicts of interest and how they play into incentives to seek growth for its own sake.

Largest office portfolio in Mexico: As discussed in the industry section of this report, we are not especially positive on the office segment given existing oversupply that is likely to worsen in the next several months. Though it represents only 19% of its NOI, with 91 properties and GLA of 959,000 sqm, FUNO's office portfolio is arguably the largest in the country and while its quality represents a meaningful buffer with top tier locations and FUNO's office rents are well below market rates, it cannot entirely escape the segment's current excess supply.

Mitikah in the spotlight: Mitikah has been caught up in the politics and press coverage of the new Mexico City government's decision to suspend construction on almost 90 developments on account of questions around licensing, particularly on the environmental front. This has attracted unflattering press for FUNO at large and, unfairly, has raised some concerns around the group's standing with the Morena

administrations in Mexico City and at the federal level. Thus far and notwithstanding press coverage to the contrary, construction on the project has continued largely unabated. Moreover, the downside of no single project moving the FUNO needle turns into a positive when dealing with situations like this one: Mitikah, in spite of its size and scope, is only 3-4% of FUNO's NAV at present (and 3% of our fair value). Nevertheless, given its prominence and symbolism as Latin America's largest mixed-use project, any coverage, positive or negative, will likely be magnified at the perception and stock levels.

FUNO's exposure to WeWork…a negative? FUNO is WeWork's largest landlord in Mexico. FUNO recently dedicated another 30k sqm of office space to WeWork in 1H19 to reach 80k sqm total as of today. FUNO plans to dedicate 100,000 sqm of office space to WeWork by the end of 2021 (i.e. expects to add another 20k sqm by 2021), reaching 8% of their total office space (1.2m sqm of total office space). On the back of its failed IPO and amid concerns over the sustainability of its business model, credit agencies have moved WeWork's credit rating well into junk territory (B- for S&P). WeWork's bonds due 2025 are down 20 points to 85.

Despite WeWork's steep losses, falling valuation and decision to halt new leasing activity, the company is expected to possess sufficient capital to continue operations. However, if their liquidity picture were to worsen, this would add stress to an office space that is already under pressure (vacancy has hovered at ~15% over the LTM). If WeWork were to go under, FUNO might have to negotiate directly with WeWork's 'enterprise' (i.e. single tenant) customers for them to stay as FUNO's tenant and will likely see a decrease in the average life of its rental contracts in the office space.

Valuation, price target, and recommendation

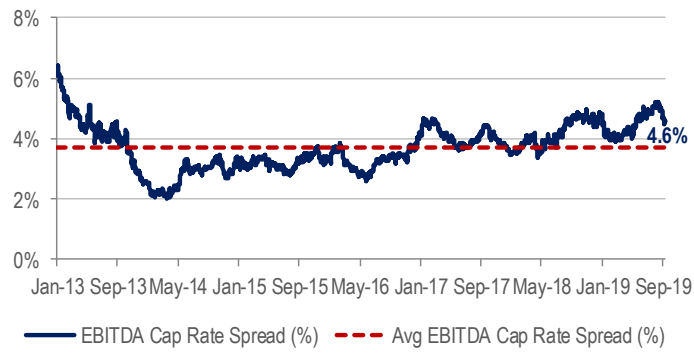
Valuation: Trading at 22% discount to NAV and at 2019E implied EBITDA cap rate and dividend yield of 7.3% and 8%, FUNO's valuation is compelling, particularly considering the quality of its portfolio, its flagship assets, and unmatched stock liquidity.

Table 5: Fibra Uno – Key Metrics

	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA (m sqm)	8,440	8,727	9,170	9,239	9,239	9,239
Rental revenue/share (P$)	3.9	4.3	4.5	4.7	4.8	4.9
NOI (P$m)	13,584	15,141	16,078	16,442	16,970	17,501
EBITDA (P$m)	12,013	13,739	14,736	15,060	15,580	16,101
FFO (P$m)	8,443	8,926	9,611	9,283	9,772	10,173
FFO/share (P$)	2.17	2.29	2.46	2.37	2.49	2.58
EPS (P$)	4.3	3.7	2.2	2.1	2.2	2.3
Total pre-tax DPS (P$)	2.14	2.32	2.46	2.29	2.33	2.42
NAV/BVPS (P$)	40.6	36.7	36.6	36.4	36.2	36.1
Valuation						
Price/CBFI (P$)	**28.7**					
# of CBFIs outstanding (m)	3,890	3,905	3,905	3,918	3,931	3,944
FX (MXN/USD):	19.1	19.4	19.4	19.4	19.4	19.4
Market cap (US$m)	5,832	5,763	5,763	5,782	5,801	5,820
Market cap (P$m)	111,451	111,867	111,867	112,240	112,614	112,987
Average net debt (P$m)	68,792	77,382	80,672	81,964	83,888	86,134
Other obligations net of refundable taxes (P$m)	(2,824)	(1,133)	348	359	370	380
Enterprise value (P$m)	**177,420**	**188,116**	**192,886**	**194,564**	**196,871**	**199,502**
Multiples						
EV/GLA (US$)	1,100	1,110	1,084	1,085	1,098	1,112
Implied NOI cap rate (%)	7.7%	8.0%	8.3%	8.5%	8.6%	8.8%
Implied EBITDA cap rate (%)	6.8%	7.3%	7.6%	7.7%	7.9%	8.1%
Rental revenue yield (%)	13.6%	14.9%	15.8%	16.4%	16.8%	17.2%
FFO yield (%)	7.6%	8.0%	8.6%	8.3%	8.7%	9.0%
Price/FFO (x)	13.2	12.5	11.6	12.1	11.5	11.1
Total dividend yield, pre-tax (%)	7.5%	8.1%	8.6%	8.0%	8.1%	8.4%
Earnings yield (%)	15.1%	12.8%	7.6%	7.3%	7.7%	8.0%
P/NAV (Book Value) (x)	0.70	0.78	0.78	0.79	0.79	0.79
Net LTV (%)	31.0%	32.0%	32.9%	33.0%	34.7%	35.2%

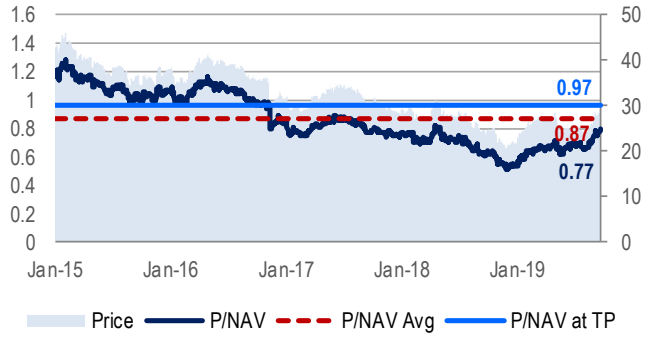
Source: Company Data, BTG Pactual estimates

Chart 44: FUNO 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 45: FUNO Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price target: Our DDM-driven price target of P$34.3/CBFI (vs. P$36.5/CBFI prior) implies an expected 28% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and dividend yield of 6.9% and 7.2%. Our DDM is based on a COE (in MXN) of 10.0% and assumes a terminal LTV of 35% by 2023.

Table 6: Fibra Uno – DDM Valuation Summary

Assumptions	
Stage 1: 2019E-2023E	
2023 AFFO (P$m)	10,142
Payout Ratio (%)	95%
2023 Dividends (P$m)	108
2023 Return on Capital (P$m)	9,527
Stage 2: 2024-2028	
Inflation (%)	3.5%
Leasing Spreads (%)	0.5%
Growth(%)	4.0%
Payout Ratio (%)	100%
Stage 3: 2029-2038	
Inflation (%)	3.5%
Leasing Spreads (%)	0.5%
Growth(%)	4.0%
Payout Ratio (%)	100%
Stage 4: Terminal Value	
Inflation (%)	3.5%
Terminal Leasing Spreads (%)	0.5%
Terminal Nominal Growth Rate(%)	4.0%
Perpetuity Dividends (P$m)	304,424

Cost of Equity Calculation	
Risk free rate, M10 (%)	7.0%
ERP (%)	4.0%
Beta	0.75
Cost of equity (%)	10.0%

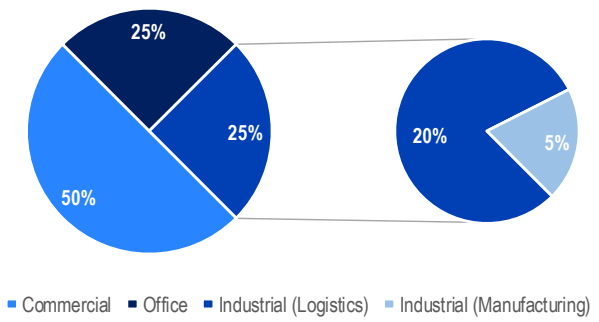
Valuation	
PV of future dividends (stage 1-stage3) (P$m)	104,729
PV of future dividends in perpetuity (P$m)	45,251
PV of future dividends (P$m)	149,980
DDM value/CBFI (P$)	38.4
DDM value/CBFI after-tax (P$)	**33.2**
(+) Potential accretion from Helios Fees + Sale (P$)	**1.1**
2019E Pro-forma official price target (P$)	**34**
12M Dividend Yield	8.1%
Upside/downside including dividends (%)	27.8%

Source: Company Data, BTG Pactual Estimates

Buy FUNO: If Mexican real estate is our favorite sector in Mexico and one of our preferred calls in Latin America, it would follow that FUNO, its benchmark stock and for many investors the only realistic option given liquidity, would naturally be a stock that we recommend. While we are cognizant of the risks, particularly when it comes to the governance of potential conflicts of interest, we would argue that the magnitude of the current discount to NAV, coupled with the self-imposed equity issuance restrictions of 2017, reduces this risk materially. And, at the moment, the impact of past dilution has passed as per CBFI metrics are now all growing alongside the top line. We therefore reiterate our Buy rating on FUNO shares.

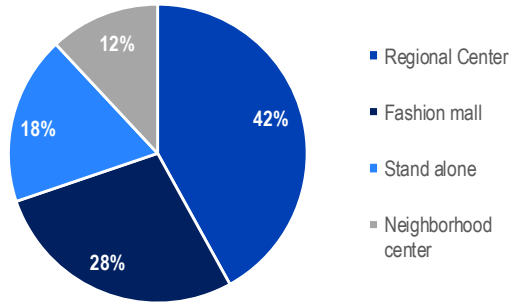
Fibra Uno – Company Description

Chart 46: Sector breakdown (as% of revenues)



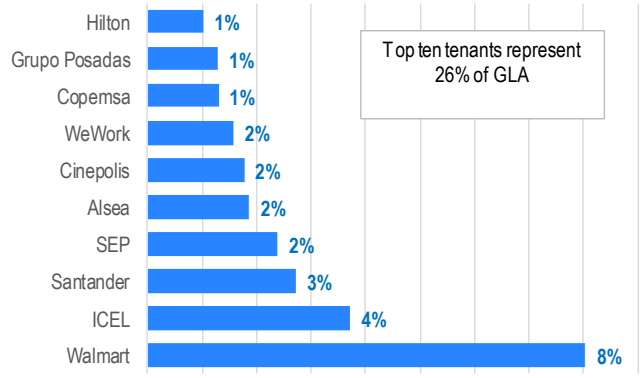
Source: Company Data, BTG Pactual Research

Chart 47: Commercial – breakdown per type of mall (as % of revenues)



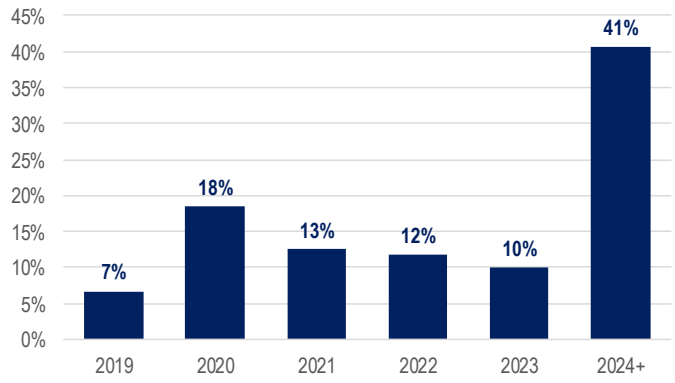
Source: Company Data, BTG Pactual Research

Chart 48: Top tenants (as % of GLA)



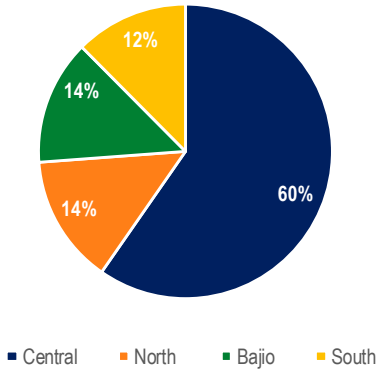
Source: Company Data, BTG Pactual Research

Chart 49: Contract expiration per year (as % of revenues)



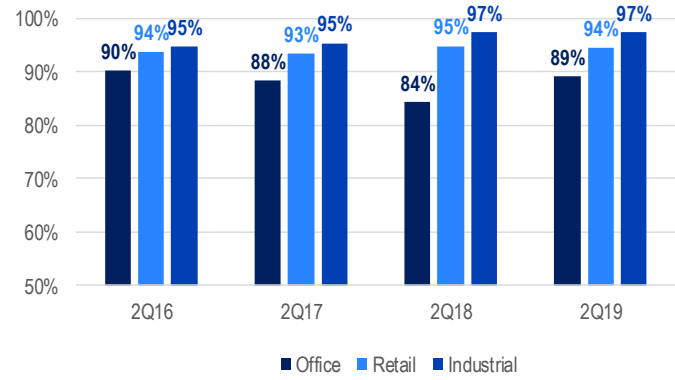
Source: Company Data, BTG Pactual Research

Chart 50: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

Chart 51: Occupancy by segment (%)



Source: Company Data, BTG Pactual Research

Fibra Danhos (Buy): Shopping on the High Street…

Highest-end retail among publicly traded vehicles

Danhos, which has been involved in the development and management of retail and office properties since 1976, is today the listed property vehicle that offers the best exposure to the high-end retail and office markets in Mexico, largely focused on CDMX and its metro area. Its portfolio of 15 owned and managed properties has a total GLA of 920K sqm and produced NOI in 2018 of P$4.2bn (US$210m), of which 65% is retail 32% is office and 3% is hotel.

The somewhat un-FIBRA FIBRA...

Danhos stands out as a FIBRA that, on many fronts, should not really be a FIBRA and, rather, a C-Corp. For one, it prefers to develop than acquire: since its IPO in 2013, it has added six properties, all developed. Partly because of this (since they do not issue CBFIs to pay for properties), the control group remains very much at the helm, owning 45% of CBFIs, the highest among the nine Mexican real estate vehicles we cover. Finally, Danhos's balance sheet also stands out: its LTV of less than 10% is about one-third the average level in our sample. This has allowed Danhos to bypass many of the dilution pitfalls that its peers have fallen into, explaining its 8% CAGR in AFFO and Distributions per CBFI since 2014, its first fully year as a public entity.

Key risk: offices and fees...

We have argued throughout this report that the office segment is the one we least like and, with 35% of NOI coming from office, Danhos is among the most exposed (behind FMTY but ahead of FUNO). Though their properties include some of CDMX's fortresses (e.g., Torre Virreyes), we still see the segment as vulnerable to a slowdown. We argued above that Danhos is in some ways the un-FIBRA FIBRA, but when it comes to fees it is. With an advisory fee of 1% of the value of investment properties and a leasing fee of 2% of revenue, Danhos shareholders pay 15% of NOI for the management of their portfolio, towards the higher end of our peer group.

We initiate Danhos with a Buy rating and P$36/CBFI price target

Danhos's retail and office properties are among the best in Mexico, its balance sheet is the strongest and its controllers have the most skin in the game of any stock we cover, its preference for development over acquisition reduces the risk of episodic, large-scale dilution, and it has effectively wound down its pipeline to zero at the right time from a macro visibility standpoint. Yet it trades at some of the most attractive valuations in the space: P/NAV of 0.68x and 2019 implied EBITDA cap rate and dividend yield of 10.3% and 9.1%, respectively.

Investment case: The Positives....

The most premier retail portfolio among listed real estate vehicles... Of Danhos's 920K GLA, almost 70% is in the retail space; of its 11 retail properties, 10 are located in CDMX and its metro area, representing 90% of its retail portfolio. Of these, there are a number of properties that would be considered among CDMX's best, including Duraznos, Toreo, and Reforma 222. Moreover, Danhos's is a young portfolio, with almost 70% of its GLA delivered within the last five years and only four properties (Duraznos, Alameda, Reforma 222 and the original Delta) at over 10 years of age and none greater than 20.

...and the same can be said for office. Danhos has eight office properties (there is some double-counting between retail and office given the mixed use nature of a few of them), all of which are in the CDMX metro area. Of Danhos's total 287K in office GLA, roughly 80% comes from three properties that would be considered among the fortress AAA buildings in CDMX (Reforma 222, Toreo, and, of course, Virreyes). And, like the retail portfolio, it is young: almost three-quarters is less than five years old.

Operating performance has been stellar. As of 2Q19, Danhos's total occupancy was 92%, comprised of 94% in retail and 87% in office. Its office occupancy is largely in line with CDMX-wide metrics, but it is weighed down by a 35% vacancy in Toreo A building, where Danhos is being patient with regards to lease-up. Excluding this property, Danhos's occupancy would stand at 93%, well above CDMX's and its public peers' average. Implied rents are rising at 6.5%, which is 250bps above trailing inflation and compares well against peers. Finally, leasing spreads were 6% in 2Q19, over 200bps above inflation, in line with trends seen over the past several quarters.

Development pipeline winding down at the right time; balance sheet a fortress too. The downside to a light development pipeline is that future growth is limited, but at a time like the present, when macro uncertainties abound, the timing for a winding down could prove opportune. At present, only 4% of Danhos's total GLA is under development and this should be completed by 2020. As recently as 2015, for instance, this was 28%; we would argue that, whether by design or fortune, winding development risk down to practically zero when there is oversupply in office and concerns about the sustainability of consumer strength is the right strategy. In this same vein, the company's LTV of 10%, while debatably inefficient, positions it on the right side of the risk spectrum ahead of a possible slowdown.

By many measures, Danhos is the un-FIBRA FIBRA. There are certain aspects to Danhos's governance that move it out from the FIBRA crowd; importantly, these minimize the dilution risks that are arguably precisely the feature of FIBRA governance that most irks investors. For one, it prefers to develop than acquire: since its IPO in 2013, it has added six properties, all developed. Partly because of this (since they do not issue CBFIs to pay for properties), the control group remains very much at the helm, owning 45% of CBFIs, the highest among the nine Mexican real estate vehicles we cover. Finally, Danhos's balance sheet also stands out: its LTV of less than 10% is about one-third the average level in our sample. This has allowed Danhos to bypass many of the dilution pitfalls that its peers have fallen into,

explaining its 8% CAGR in AFFO and Distributions per CBFI since 2014, its first fully year as a public entity.

Investment case: Negatives & Risks...

Office exposure at a time of material and rising oversupply. CDMX and its metro area as a whole currently has a vacancy rate among A-class and above office properties of 15%; Danhos's 13% is slightly below this. However, the expectation is for new inventory to come to CDMX through 2022 that surpasses the markets's ability to absorb new space, which should lead to additional vacancy. With 97% of its office GLA and 91% of its office NOI in the CDMX-metro area office space, any further weakness in the office space represents a risk for Danhos.

Retail exposure: cyclical risk and structural oversupply? The Mexican consumer has held its ground in spite of weakness in most other areas of the economy. One of the questions most frequently asked in Mexico's current context of expected GDP growth of only 0.5% is how long the consumer can hold out. As per the optimists, many of the drivers behind the strength in consumption over the past several years remain in place: employment continues to grow, wages are rising in real terms (driven, in part, by the 10% increase in minimum wage announced at the end of last year), remittances seem to hit a record every month, and inflation remains subdued (and, in fact, declining), giving Banxico an important reason to continue cutting rates and, perhaps, at an accelerated pace.

Pessimists, however, would point out that employment growth has slowed and, arguably, its quality has deteriorated. Remittances, while strong, are impacted by the strength in MXN (in so far as their conversion rate is less attractive), but are clearly at risk should the much-feared US recession occur. Finally, the overall level of economic growth, and in particular the recession now being suffered by the construction sector, is a cause for concern. All together, this could explain some of the weakness recently seen in consumption and, should it continue, presents risks for the retail space, Danhos's properties included.

More structurally, however, there is some data that would suggest that many of Mexico's large retail markets, including the CDMX metro area, are on the verge of being oversupplied. Or, at a minimum, they are oversupplied relative to other metro areas in the region, particularly those in Brazil and Argentina. This could magnify the risks of any cyclical weakness as described above. While Danhos's wind-down of its development portfolio to basically zero materially mitigates these risks from a capital allocation standpoint, it does not necessarily shield its existing portfolio from potential operating malaise.

Fee structure and the costs that it implies. As discussed above, there are features of Danhos's corporate governance, strategy, and ownership structure that mitigate the dilution risk that so vexes investors. Where, however, it is on the wrong side of the governance argument is on the fee and operating cost side, where its 1% of asset value fee translates into 15% of NOI, making its cost-to-operate among the more expensive of our sample.

Valuation, price target, and recommendation

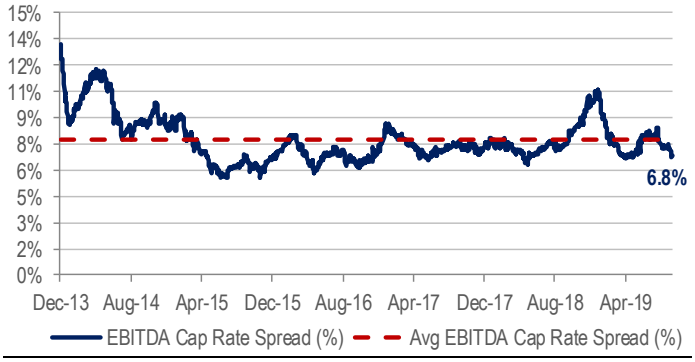
Valuation: Trading at a 32% discount to NAV and at 2019E implied EBITDA cap rate and dividend yield of 10.3% and 9.1%, Danhos's valuation is compelling, particularly considering that it boasts some of the best retail and office assets and the strongest balance sheet among all listed Mexican real estate vehicles. Further, its preference for development rather than acquisition renders the risk of episodes of significant dilution less likely.

Table 7: Fibra Danhos – Key Metrics

	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA (m sqm)	854	889	892	927	927	927
Rental revenue/share (P$)	3.7	4.0	3.9	4.0	4.1	4.1
Rental revenue (P$m)	3,575	3,937	4,031	4,310	4,504	4,664
Total revenue (P$m)	5,153	5,704	5,691	6,085	6,359	6,398
NOI (P$m)	4,152	4,587	4,574	4,890	5,110	5,142
EBITDA (P$m)	3,426	3,858	3,815	4,124	4,341	4,373
EBITDA Adjusted (P$m)	4,035	4,480	4,455	4,763	4,978	5,008
FFO (P$m)	3,171	3,507	3,432	3,748	3,979	4,027
FFO Adjusted (P$m)	3,780	4,128	4,072	4,387	4,616	4,663
FFO/share (P$)	2.27	2.48	2.33	2.49	2.58	2.57
EPS (P$)	2.8	2.4	2.3	2.5	2.6	2.6
Total pre-tax DPS (P$)	2.33	2.46	1.77	1.78	1.84	1.87
NAV/BVPS (P$)	40.2	39.9	39.3	39.1	39.0	39.1
Valuation						
Price/CBFI (P$)	27.1					
# of CBFIs outstanding (´000)	1,399	1,415	1,472	1,507	1,542	1,566
FX (MXN/USD):	19.1	19.3	19.8	20.2	20.5	20.8
Market cap (US$´000)	1,982	1,988	2,012	2,024	2,041	2,042
Market cap (P$´000)	37,876	38,311	39,852	40,782	41,741	42,397
Average net debt (P$´000)	4,872	5,261	5,038	4,552	4,000	3,496
Other obligations net of refundable taxes (P$´000)	20	40	42	43	45	47
Enterprise value (P$´000)	**42,768**	**43,611**	**44,931**	**45,377**	**45,786**	**45,940**
Multiples						
EV/GLA (US$)	2,620.4	2,545.0	2,543.4	2,429.8	2,415.4	2,387.7
Implied NOI cap rate (%)	9.7%	10.5%	10.2%	10.8%	11.2%	11.2%
Implied EBITDA cap rate (%)	9.4%	10.3%	9.9%	10.5%	10.9%	10.9%
Rental revenue yield (%)	13.6%	14.9%	14.3%	14.9%	15.2%	15.1%
FFO yield (%)	10.0%	10.8%	10.2%	10.8%	11.1%	11.0%
Price/FFO (x)	10.0	9.3	9.8	9.3	9.0	9.1
Total dividend yield, pre-tax (%)	8.6%	9.1%	6.5%	6.6%	6.8%	6.9%
Earnings yield (%)	10.3%	8.9%	8.6%	9.2%	9.5%	9.5%
P/NAV (Book Value) (x)	0.67	0.68	0.69	0.69	0.69	0.69
LTV (%)	10.3%	10.2%	10.0%	9.9%	9.7%	10%
EV/EBITDA	12.5	11.3	11.8	11.0	10.5	10.5

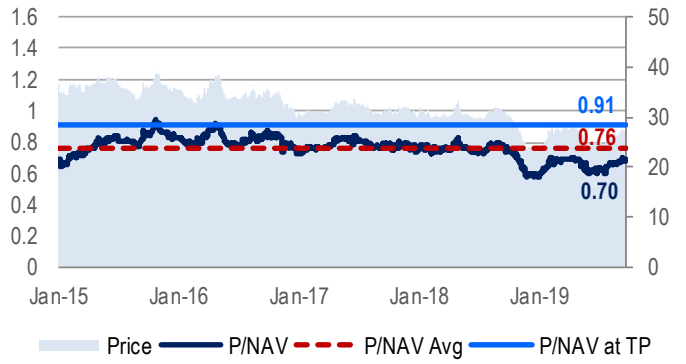
Source: Company Data, BTG Pactual Research

Chart 52: Fibra Danhos 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 53: Fibra Danhos Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price Target: Our DDM-driven price target of P$36/CBFI implies an expected 43% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and dividend yield of 7.7% and 6.9%. Our DDM is based on a COE of 12.0% (in MXN) and assumes a terminal LTV of 10% by 2023, consistent with its existing balance sheet. If we were to take its LTV to 25% (higher than its current 10% but still short of the 35% at which we stabilize FIBRA balance sheets in our DDM models), Danhos's DDM-driven fair value would be P$41/CBFI.

Table 8: Fibra Danhos – DDM Valuation

Assumptions	
Stage 1: 2019E-2023E	
2023 AFFO (P$m)	4,790
Payout Ratio (%)	80%
2023 Dividends (P$m)	1,546
2023 Return on Capital (P$m)	2,286
Stage 2: 2024-2028	
Inflation (%)	3.5%
Leasing Spreads (%)	0.0%
Growth(%)	3.5%
Payout Ratio (%)	90%
Stage 3: 2029-2038	
Inflation (%)	3.5%
Leasing Spreads (%)	0.0%
Growth(%)	3.5%
Payout Ratio (%)	90%
Stage 4: Terminal Value	
Inflation (%)	3.5%
Terminal Leasing Spreads (%)	0.0%
Terminal Nominal Growth Rate(%)	3.5%
Perpetuity Dividends (P$m)	84,976

Cost of Equity Calculation	
Risk free rate, M10 (%)	7.0%
ERP (%)	5.0%
Beta	1.00
Cost of equity (%)	12.0%

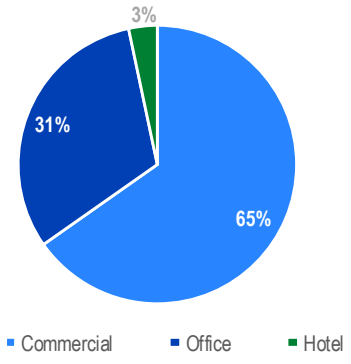
Valuation	
PV of future dividends (stage 1-stage3) (P$m)	53,087
PV of future dividends in perpetuity (P$m)	13,861
PV of future dividends (P$m)	66,948
DDM value/CBFI (P$)	42.1
DDM value/CBFI after-tax (P$)	**36.2**
2019E Pro-forma official price target (P$)	**36**
12M Dividend Yield	9.1%
Upside/downside including dividends (%)	42.8%

Source: Company Data, BTG Pactual Research

Buy Danhos: Danhos boasts one of the highest quality retail and office portfolios in Mexico, a controlling group with the highest stake among any of the stocks we cover, lower capital allocation risk given an overall preference to develop rather than acquire, and a relatively low risk growth profile given the almost total wind-down of its development pipeline at a time when economic uncertainty is high. Yet its valuation is among the most attractive of the nine Mexican real estate stocks under coverage: P/NAV of 0.68x, implied EBITDA cap rate of 10.3%, and dividend yield of 9.1%. While we acknowledge that liquidity is low and that this is not the best time from a cyclical perspective to be invested in office, we believe that these shortcomings are captured fully in valuation and that current prices represent a compelling entry point for a portfolio and management team of Danhos's quality.

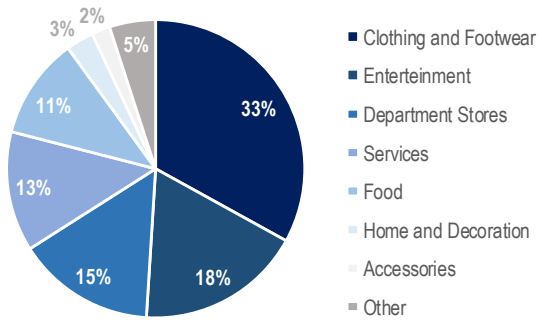
Fibra Danhos – Company Description

Chart 54: Sector breakdown (as% of revenues)



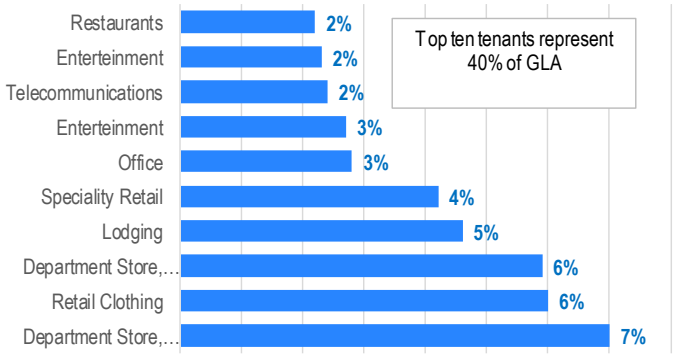
Source: Company Data, BTG Pactual Research

Chart 55: Tenant breakdown by industry (as % of GLA)



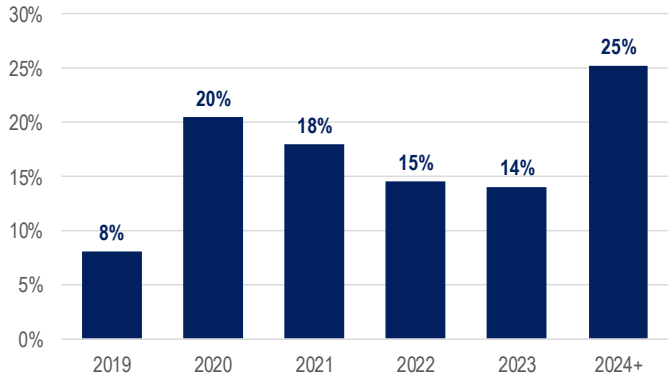
Source: Company Data, BTG Pactual Research

Chart 56: Top tenants (as % of GLA)



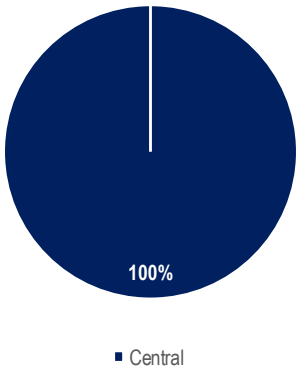
Source: Company Data, BTG Pactual Research

Chart 57: Contract expiration per year (as % of revenues)



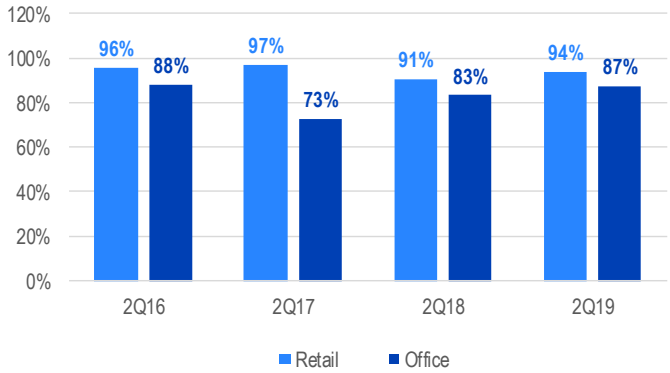
Source: Company Data, BTG Pactual Research

Chart 58: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

Chart 59: Occupancy by segment (%)



Source: Company Data, BTG Pactual Research

Fibra PL (Buy): Mexico's industrial High Street...

The industrial High Street #1: the best play on logistics

Of the nine Mexican real estate stocks that we now cover, three (Terra, Vesta, and Fibra PL) are entirely focused on industrial real estate, two are largely focused (Fibra MQ and FMTY), and one is somewhat focused (FUNO). In other words, two-thirds of the stocks we cover are industrial plays, limiting the scarcity value of any one stock — with one exception. That exception is Fibra PL, whose expertise in logistics and its ensuing exposure to the growth from rising e-commerce penetration sets it apart from the pack.

The industrial High Street #2: Prologis's sponsorship

Many of Fibra PL's competitors in the space have well-regarded and highly-experienced sponsors, but in the industrial space none has the credentials of Prologis, Fibra PL's sponsor. With a market cap of US$54bn and GLA of 145m sq ft, it is the largest industrial real estate developer and property manager in the world. It is present in 19 countries around the world, but its leading presence in the US with many clients that also run operations in Mexico is perhaps what matters most to Fibra PL. This extends into the logistics space, where Amazon stands out as Prologis's largest tenant globally and Prologis as Amazon's largest landlord, including in Mexico.

Key risk: the relationship with Prologis

Just as the main strength of superheroes can at once be their fatal flaw if mishandled, so it is with companies. We would argue that thus far, Fibra PL has managed this well and its reluctance to issue equity until the stock approaches NAV, in spite of the pipeline available to it, is the clearest example. But there is an argument to be made that the fees paid by Fibra PL to Prologis are heavy and that there is an underlying risk of value transfer as Fibra PL exercises on its right to purchase property from its parent.

We are initiating coverage of Fibra PL with a Buy rating and P$46/CBFI PT

Fibra PL trades a 12% discount to NAV and at 2019E implied EBITDA cap rate and dividend yield of 7% and 6%. Though we acknowledge that its valuations are on the higher end of the comp scale, we believe they are attractive in the context of the quality of its portfolio and tenant base, its sponsorship by Prologis, and the potential upside its logistics expertise offers as e-commerce gains traction in Mexico. Moreover, our DDM valuation, which results in sufficient upside to justify our Buy rating, still implies a small discount to NAV.

Investment case: The Positives....

The industrial High Street #1: the best play on logistics...Of the nine Mexican real estate companies under coverage, six have meaningful exposure to the industrial segment. But none has the logistics exposure of Fibra PL's, particularly considering the growth to this segment that the eventual exercise of its available pipeline from Prologis could produce. As of 2Q19, of Fibra PL's total GLA, some some 68% is in logistics, the highest share among the industrial names that we cover.

Over the long-run, the additional growth that this segment could produce is material, particularly considering that, for the size of its economy and level of purchasing power, Mexico's internet usage and e-commerce penetration, while growing, remain unusually low. As Mexican internet metrics normalize, demand for logistics space will increase, compounded by the growth in Mexico's population and its level of income.

But additional to this is the fact that e-commerce requires three times the logistical space of a typical brick and mortar operation since it entails last mile delivery, regional distribution and inventory assets, and a facility dedicated to handling returns. With the network that Prologis offers globally, nobody would seem better suited in Mexico than Fibra PL to profit from this. Relevantly, Amazon is Prologis's largest tenant globally and Prologis is Amazon's largest landlord. In Mexico, where e-commerce penetration is in a relative stage of infancy, Prologis is already landlord to both Amazon and Mercado Libre (as it happens, in the same park), the two companies that are leading the charge to develop the market. Once these properties are stabilized and Fibra PL builds the balance sheet space needed to tap into the pipeline available via Prologis, it is likely that these two tenants will become clients of Fibra PL as well.

The industrial High Street #2: Prologis's sponsorship... If you're going to be involved in the industrial space, particularly as it moves to the higher value-added services that logistics assets geared towards e-commerce will require, what better sponsor to have than the largest and most recognized developer, owner, and manager of industrial real estate assets in the world? As of 2018, Prologis owns and manages 438 properties with GLA of 145 million sqft in 19 countries, with Mexico accounting for about a quarter of its space. No company has developed more industrial space or created more value doing it than Prologis. The active engagement of its management, the company's 46% equity ownership, the transferral of best practices from both an asset management and corporate governance standpoint, the ability to exercise on its development pipeline in Mexico, and access to its global customer network are all advantages coming from Prologis that set Fibra PL apart from its peers.

The industrial High Street #3: Higher occupancies and sterling tenant base. And to a certain degree its existing metrics bear this out: higher occupancy (97% as of 2Q19) with a diversified and high-quality tenant mix (232 customers, of which 86% are multinational companies and of which the ten largest collectively represent less than 20% of total rents). In the end, this reflects the fact that AAA-customers care more about the quality and upkeep of a building than for a low rent; a building that

over the long run contributes to greater efficiencies and, therefore, reduced operating costs ultimately matter more than a cheap rent.

Investing adequately in its properties. An area of debate among FIBRA managements and their investors has been whether as a group they are investing the adequate amounts of capex to property maintain properties. This is especially so in the industrial space, where a general absence of prime locations renders the upkeep of properties paramount. In line with Prologis's practices in the US, Fibra PL is consistently among the industrial players that most reinvests in its properties.

Concentrated in Mexico's best logistics and industrial markets. As of 2Q19, some 37% of Fibra PL's GLA was located in the Mexico City metro area, followed by 16% in Guadalajara, 13% in Reynosa, 12% in Monterrey, 12% in Tijuana, and 9% in Ciudad Juárez. Of these, Mexico City, Guadalajara, and a good portion of the Monterrey GLA would be considered to be in the key logistics corridors, while the balance is located in industrial regions. Of these, Tijuana, Ciudad Juárez, and Monterrey are top of class, with Reynosa arguably being the one potentially problematic market in the portfolio (though it is a major auto hub, its ongoing public safety issue renders it less attractive than other industrial markets for potential tenants). Unlike many of its peers, Fibra PL has opted to stay away from Bajío, which at present seems like the right decision given the recent lull in leasing activity there.

The best of both worlds: Prologis and Acción/Opción. Before there was Fibra PL there was Grupo Acción and before that Fondo Opción. These were publicly-traded diversified real estate platforms founded and managed by Fibra PL CEO Luis Gutiérrez and COO Héctor Ibarzábal in the 1990s that were eventually purchased by Prologis, shed of their non-industrial assets, and formed the core of Prologis México and Fibra PL. This provides Fibra PL with the best of both worlds: Prologis's unparalleled expertise in the global industrial and logistical space along with its best in class governance and tenant network, combined with a management team that has been developing and managing Mexican real estate assets for some 30 years, some of which real doozies for property managers (1994/1995 and 2009/2010).

And all of which has paid off for investors. Fibra PL has delivered USD growth in NOI, EBITDA, FFO, and AFFO in each of the five years since its IPO. This has allowed for a 10% CAGR in DPCBFI since IPO, even as its LTV has hovered around 40%. As a result, its total return since IPO to September 2019 has been slightly in excess of 100%, surpassing its peers, but importantly almost evenly split between distributions and stock price appreciation (unmatched by any of its peers).

Investment case: Negatives & Risks...

Greater domestic and MXN exposure relative to peers: Fibra PL's exposure to logistics is one of the features that sets it apart from its peers and, in our view, the main reason, along with Prologis's sponsorship, of its premium valuation. Over the long-run, exposure to logistics will likely result in greater growth, contribute to building a portfolio in better real estate markets, and attach Fibra PL's fortunes to some of the most exciting companies in the world. In the short-run, however, it increases its

exposure to the rapidly slowing domestic economy and leads to a greater reliance on MXN cash flows.

A capital raise in the offing? To Fibra PL's credit, it has always maintained and stuck to its mantra of not raising capital at a material discount to NAV, the adherence to which we also believe features into its premiums as it contributes to its perception of being a good shepherd of its investors' capital. However, with the stock trading at almost 0.9x P/NAV, an LTV of 32% (which is close to the 35% top limit that Fibra PL has spoken about in the past) and assets with 5.2 million sqf (vs. 35.9m sqf for all of Fibra PL) that Prologis is in the process of stabilizing (already 86% leased up), it would appear that the conditions are right for a capital raise at some point in the medium term.

Issuing equity *per se* is not a bad thing if the assets acquired are high-quality and prove to be accretive, fit within the company's overall strategic blueprint, management minimizes the period of time in which per CBFI metrics are diluted, and stock liquidity improves. But given the sector's spotty track-record with the speedy and accretive allocation of capital, the possibility of an equity offering could cause some initial anxiety.

You get what you pay for — but not the cheapest platform. Like most of its FIBRA peers, Fibra PL is externally managed and, therefore, subject to a fee structure that pays for the platform's day-to-day and strategic management. Fibra PL pays Prologis a series of fees, some of which are for the property and portfolio management services it provides (property management fees of 3% of revenue, leasing fees when no brokers are involved, and a construction and development fee) and some for the management of the FIBRA itself (0.75% of appraised asset value and a 10% incentive fee above a 9% total return hurdle payable in CBFIs). In all, Fibra PL's management structure is the most expensive among its industrial peers and the third among our covered sample (behind FUNO and Danhos).

In the end, you get what you pay for and you pay for what you get. In other words, Fibra PL is arguably paying a premium for premium management and access to what many would consider the highest quality and most reliable industrial pipeline in Mexico. As discussed above, this has not come at the expense of shareholder returns; quite the opposite, in fact. But as the experience of some of its peers suggests, investors' willingness to pay up for management and expertise is tested when performance sags or if there is a perception of any mistreatment of minorities.

The risk of a strength: the relationship with Prologis. As can be seen in the comments above, we believe that the most important distinguishing feature of Fibra PL's performance and positioning is its relationship with Prologis. This is reflected in the quality of its portfolio, in the quality of its tenant base, in the quality of its management, and in the quality of its governance.

But the relationship with Fibra PL also carries two potential risks, in our view, that management must be very mindful to avoid. First, as discussed immediately above, the cost of its platform is on the more expensive end of the peer spectrum —

management must work to ensure that its minority shareholders feel they are getting their money's worth.

Second, Fibra PL and Prologis must make sure that any potential or perceived conflicts of interest, particularly those stemming from related party M&A, are handled fairly, transparently, and to the satisfaction of minority shareholders. To be fair, many of Fibra PL's shareholders own it precisely because of Prologis's sponsorship, a key component of which is access to its pipeline. Thus, we would argue that because investors are familiar with Prologis's own success and with that of Fibra PL since its IPO, they are happy underwriting the risk. But any change in the perception in the balance of the relationship may quickly undermine this willingness.

Valuation price target and recommendation

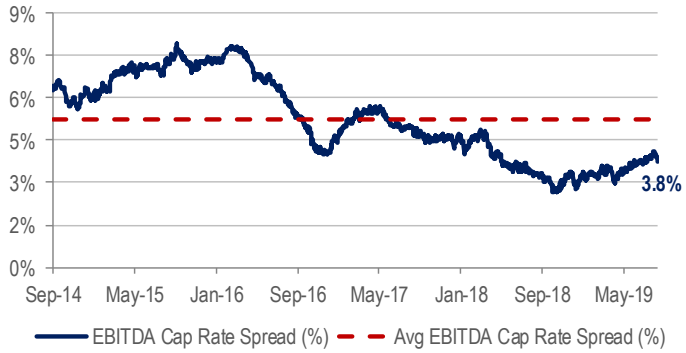
Valuation: Fibra PL trades a 12% discount to NAV and at 2019E implied EBITDA cap rate and dividend yield of 7% and 6%.

Table 9: Fibra Prologis – Key Metrics

Valuation Summary (In MXN$)	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA (sq m)	3,344	3,331	3,331	3,331	3,331	3,331
Rental revenue (P$)	3,280	3,367	3,479	3,604	3,750	3,862
Revenues(P$m)	3,673	3,815	3,926	4,067	4,231	4,358
NOI(P$m)	3,179	3,267	3,382	3,503	3,647	3,757
EBITDA (P$m) - Adjusted	2,806	2,902	2,986	3,107	3,251	3,366
FFO (P$m)	2,070	2,132	2,307	2,420	2,555	2,660
FFO/share (P$)	2.89	2.84	3.09	3.25	3.44	3.59
AFFO/share (P$)	2.49	2.74	2.94	3.10	3.28	3.42
EPS (P$)	4.61	3.20	3.09	3.25	3.44	3.59
Minimum pre-tax DPS (P$)	2.04	1.07	0.42	0.34	0.53	0.74
Total pre-tax DPS (P$)	2.25	2.47	2.84	3.06	3.23	3.38
NAV/BVPS (P$)	47.62	46.62	46.19	45.56	45.56	45.56
Valuation						
Price/CBFI (P$)	41.00					
# of CBFIs outstanding (m)	644.7	644.7	644.7	644.7	644.7	644.7
FX (MXN/USD):	19.11	19.43	19.61	19.87	20.17	20.47
Market cap (US$m)	1,383.2	1,360.1	1,347.9	1,330.4	1,310.8	1,291.4
Market cap (P$m)	26,432	26,432	26,432	26,432	26,432	26,432
Average net debt (P$m)	15,346.4	15,273.5	14,343.2	14,277.3	14,702.4	15,277.3
Other obligations net of refundable taxes (P$m)	-463.8	-402.5	-389.7	-404.7	-421.4	-434.1
Enterprise value (P$m)	41,314.1	41,302.6	40,385.1	40,304.2	40,712.6	41,274.8
Multiples						
EV/GLA (US$)	646.46	637.99	618.21	608.97	606.05	605.34
Implied NOI cap rate (%)	7.7%	7.9%	8.4%	8.7%	9.0%	9.1%
Implied EBITDA cap rate (%)	6.8%	7.0%	7.4%	7.7%	8.0%	8.2%
Rental revenue yield (%)	8.0%	8.2%	8.5%	8.8%	9.1%	9.4%
FFO yield (%)	7.8%	8.1%	8.7%	9.2%	9.7%	10.1%
Price/FFO (x)	12.8	12.4	11.5	10.9	10.3	9.9
AFFO yield (%)	6.1%	6.7%	7.2%	7.6%	8.0%	8.3%
Minimum dividend yield, pre-tax (%)	5.0%	2.6%	1.0%	0.8%	1.3%	1.8%
Total dividend yield, pre-tax (%)	5.5%	6.0%	6.9%	7.5%	7.9%	8.3%
Minimum dividend yield, after-tax (%)	3.6%	1.9%	0.7%	0.6%	0.9%	1.3%
Total dividend yield, after-tax (%)	4.1%	5.3%	6.6%	7.2%	7.5%	7.7%
Earnings yield (%)	11.2%	7.8%	7.5%	7.9%	8.4%	8.8%
P/NAV (Book Value) (x)	0.86	0.88	0.89	0.90	0.90	0.90
Net LTV (%)	34%	32%	31%	32%	34%	35%

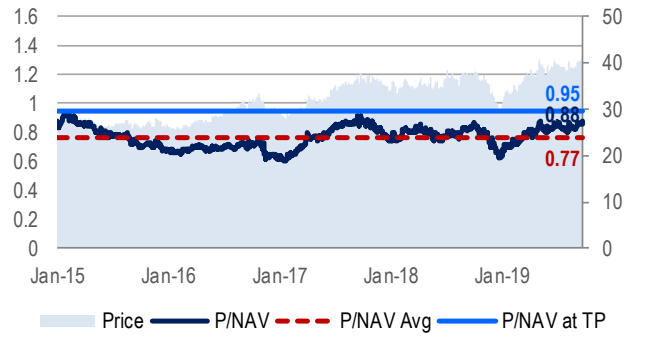
Source: Company data, Bloomberg, BTG Pactual Estimates

Chart 60: Fibra Prologis 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 61: Fibra Prologis Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price Target: Our DDM-driven price target of P$46/CBFI implies an expected 18% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and dividend yield of 6.8% and 6.2% and into a P/NAV of 0.99x. Our DDM is based on a USD COE of 7.5% and assumes a terminal LTV of 35% by 2023, largely consistent with its existing balance sheet.

Table 10: Fibra Prologis – DDM Valuation

Assumptions	
Stage 1: 2019E-2023E	
2023 AFFO (US$m)	108
Payout Ratio (%)	100%
2023 Dividends (US$m)	23
2023 Return on Capital (US$m)	84
Stage 2: 2024-2028	
Inflation (%)	2.0%
Leasing Spreads (%)	0.0%
Growth(%)	2.0%
Payout Ratio (%)	100%
Stage 3: 2029-2038	
Inflation (%)	2.0%
Leasing Spreads (%)	0.0%
Growth(%)	2.0%
Payout Ratio (%)	100%
Stage 4: Terminal Value	
Inflation (%)	2.0%
Terminal Leasing Spreads (%)	0.0%
Terminal Nominal Growth Rate(%)	2.0%
Perpetuity Dividends (US$m)	2,631

Cost of Equity Calculation	
Risk free rate, UMS (%)	3.7%
ERP (%)	5.0%
Beta	0.05
Cost of equity (%)	7.5%

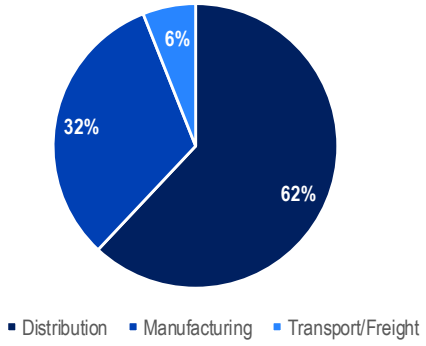
Valuation	
PV of future dividends (stage 1-stage3) (US$m)	1,198
PV of future dividends in perpetuity (US$m)	575
PV of future dividends (US$m)	1,773
DDM value/share (US$)	2.7
DDM value/share after-tax (US$)	2.4
DDM value/share after-tax (P$)	46.2
2018E Pro-forma official price target (US$)	**46**
12M Dividend Yield	6.0%
Upside/downside including dividends (%)	17.9%

Source: Company data, Bloomberg, BTG Pactual Estimates

Recommendation: We initiate coverage of Fibra PL with a Buy rating. Though we acknowledge that its valuations are on the higher end of the comp scale, we believe they are attractive in the context of the quality of its portfolio and tenant base, its sponsorship by Prologis (the largest industrial developer and asset manager in the world), and the potential upside its logistics expertise offers as e-commerce gains traction in Mexico. Moreover, our DDM valuation, which results in sufficient upside to justify our Buy rating, still implies a small discount to NAV.

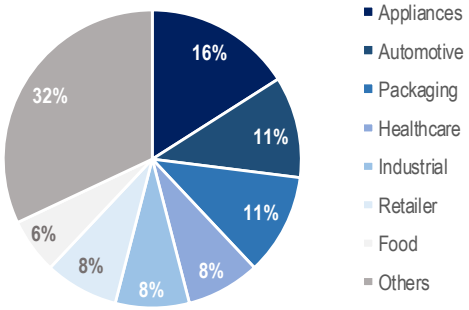
Fibra Prologis – Company Description

Chart 62: Sector breakdown (as% of revenues)



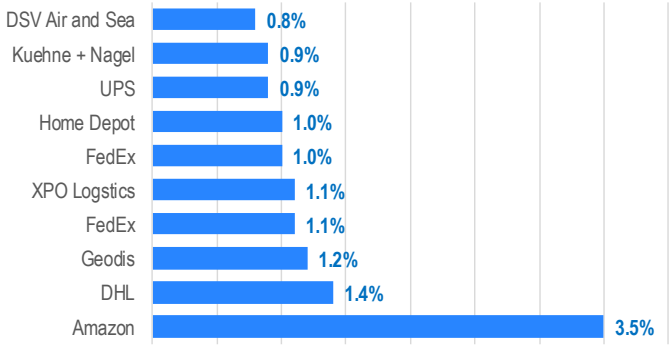
Source: Company Data, BTG Pactual Research

Chart 63: Tenants' industry breakdown (as% of GLA)



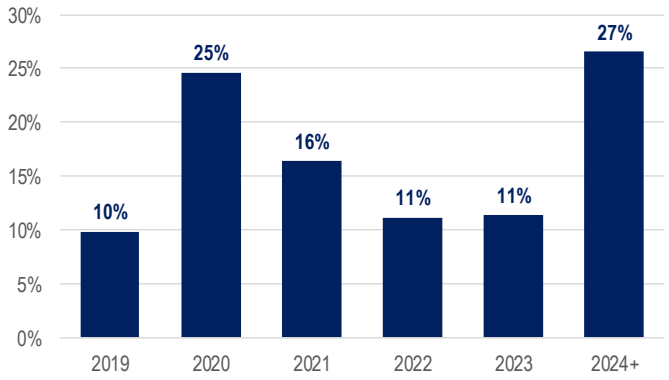
Source: Company Data, BTG Pactual Research

Chart 64: Top tenants (as % of revenues)



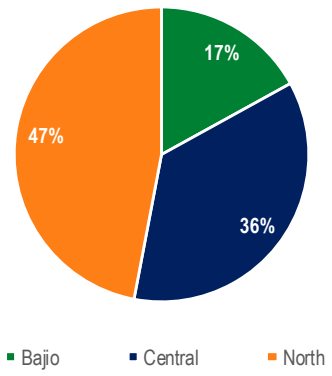
Source: Company Data, BTG Pactual Research

Chart 65: Contract expiration per year (as % of revenues)



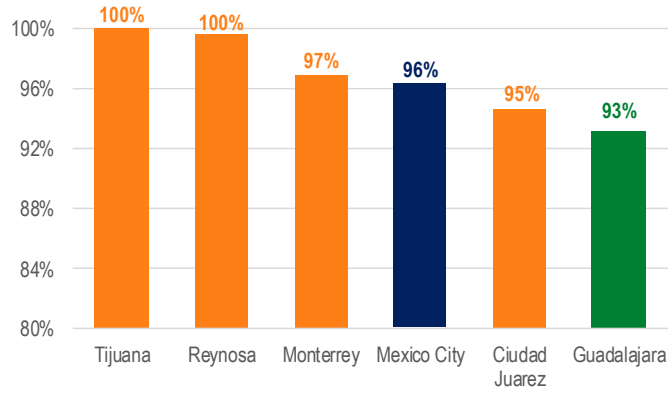
Source: Company Data, BTG Pactual Research

Chart 66: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

Chart 67: Occupancy by geography (%)



Source: Company Data, BTG Pactual Research

Terrafina (Neutral): Keeping it simple...

The no drama FIBRA

In a world where the extraordinary has become the mundane and the scandalous pedestrian anything that provides a sense of normality and predictability is somewhat of a treasure. The same is true in FIBRA world — and Terra stands out as an oasis of tranquility and visibility. Since its IPO in 2013, it has stuck to a simple strategy of focusing on the industrial segment, making opportunistic acquisitions of properties that fit nicely into the mould of its existing portfolio, executing on selective and manageable development and expansion opportunities, and distributing the entirety of its AFFO.

The purest play on manufacturing among FIBRAs

Among the FIBRAs, Terra is one of only two that are fully focused on the industrial segment. Of the two, however, it is the one with the greatest exposure to the manufacturing sector, making it the best FIBRA proxy to Mexico's manufacturing export economy (which is, frustratingly, not well-represented among its publicly traded companies). We have discussed a number of reasons why we believe that Mexico's manufacturing renaissance is secular in nature, which should enable Terra to continue reaping its rewards far into the future.

Key risk: a reduction in distributions or a capital raise?

Though it is consistent with its stated long-term goals, Terra's LTV of 41% is on the high end among the peer group, especially given concerns on the global cycle. Moreover, given the slowdown in Mexico and the potential for macro weakness globally, Terra would presumably want to be in a position to capitalize on any opportunities to acquire good properties or expand within their portfolios on the cheap. We therefore believe that some sort of capitalization would make sense, which can be accomplished immediately through a capital raise, partially through an asset sale, or gradually via a reduction in its current payout of 100% of AFFO.

We are downgrading Terra to Neutral on PT of P$32/CBFI (from P$36)

At 8.3% for 2019, Terra is the highest dividend yielder among the industrial FIBRAs, which is noteworthy considering that its dividend is effectively dollarized. Nevertheless, because of the de-leveraging assumption to 35% (from 41% in 1H19) that we have made in our DDM model, the total 12-month return implied by our new P$32 target of 12% is not enough to justify a buy rating. We are therefore reducing our rating to Neutral, though we will be looking for any opportunity to upgrade the stock since it is an asset and management team that we rate highly.

Investment case: The Positives....

Keeping it simple. In contrast to many of its peers, Terra has kept to a strategy of a focused industrial portfolio, concentrated in the North, and tilted towards light-manufacturing. It has also kept its messaging simple and steady by engaging in occasional M&A that is consistent with the shape of its portfolio, selectively undertaking small development and expansion opportunities, and distributing the entirety of its AFFO. This simplicity in a sector in which there is altogether too much drama given how predictable it ought to be has been welcomed and rewarded by investors at large.

11 consecutive quarters of ca. 95% occupancy; rents at record levels too. As one of two only FIBRAs fully exposed to industrial, Terra's performance is at once heavily influenced by, and a picture of, the health of industrial real estate markets. Accordingly, Terra just reported its 11th consecutive quarter of occupancy near 95% (95.5% in 1H19) and record rental rates of US$5.2/sqft, which given demand-supply dynamics in the sector would seem to be on pace for further increases going forward.

Northern exposure: from weakness to strength. When Terra became public in 2013, it was generally considered a weakness to be exposed to Ciudad Juárez and a strength to be in Bajío. That perception has now been turned on its head as the North in general, and Ciudad Juárez in particular, are back in vogue with Bajío taking a backseat. As of 1H19, the North represents 70% of Terra's properties, 67% of its tenants, 62% of its GLA, and is the region with its highest occupancy level (98% vs. 95.5% for the portfolio as a whole). Bajío, by contrast, is roughly one-third the size of the North by GLA and one-fourth by number of properties.

A rare export proxy for Mexico. Along with Chile, Mexico is the country with most FTAs in the world, trading freely with over 40 countries representing some 60% of global GDP. Total trade represents 80% of Mexico's GDP and its manufacturing exports are more than twice the rest of Latin America's combined. In sum, Mexico is arguably the only export-led economy in the Americas, comparable in many metrics to Asia or Germany. Yet, to the great frustration and chagrin of investors, it is extremely difficult to gain exposure to this export economy via the public equity markets as there are no more than two or three manufacturing exporters listed on the Bolsa. Terra, by virtue of being the only FIBRA and one of two stocks with over 70% of cash flows linked to the manufacturing sector, represents an attractive and rare proxy to this all important engine of the economy.

Investment case: Negatives & Risks...

A capital raise/distribution cut in the offing? A cyclical downturn presents both risks and opportunities for a FIBRA like Terra. Considering the increasing concern around slowing growth in Mexico, the US, and the world at large, it would seem that the risk of a cyclical downturn is growing. Though we remain confident in the secular drivers behind demand for Mexican industrial real estate, in the short run the cycle rules the day and Terra might be better prepared for both the risks and opportunities if its leverage were closer to the 30-35% vs. the 41% posted in 1H19. Getting to 33%, for example, would require a reduction in leverage of US$200 million. As of 2Q19, at

100% of AFFO, distributions are running at about US$100 million annually, implying both that there is room to cut them and that cutting them might not be enough to right size the balance sheet quickly, raising the risk of a capital raise.

Does the volatility in TIs or leasing commissions say something about the portfolio? A recurring theme when analyzing Terra's quarterly results is surprises in EBITDA margin related to volatility in Tenant Improvements (TIs) and Leasing Commissions (LCs). Management seems to have a difficult time predicting them and they do not seem correlated to other issues that would likely have some sort of linkage. In a sector where there are recurring concerns about management teams not ploughing back enough capital back into the maintenance of properties, questions of whether Terra's does invariably surface when there is an unexplained jump in TIs and LCs.

External property management model - too much distance from the market? Terra manages its properties externally, often granting contracts to developer-managers from whom they have bought assets in the past. Management believe that this gives them an edge from an M&A pipeline standpoint as they remain in constant contact with developers and are able to offer them an additional incentive in the form of a management contract, placing them at an advantage relative to other potential bidders both in timing and in terms.

This make sense, but is it enough to compensate for the disadvantage at the operating level from not internalizing the property management? We see four main disadvantages: i) it eliminates any chance of operating leverage at the property level since the payment is a percentage of rents; ii) it places distance between Terra and its tenants; iii) it places distance between Terra and the market; and iv) it introduces the possibility of a conflict of interests or of priorities by the managers if it manages properties not owned by Terra or is distracted by its own development activities.

Valuation, price target, and recommendation

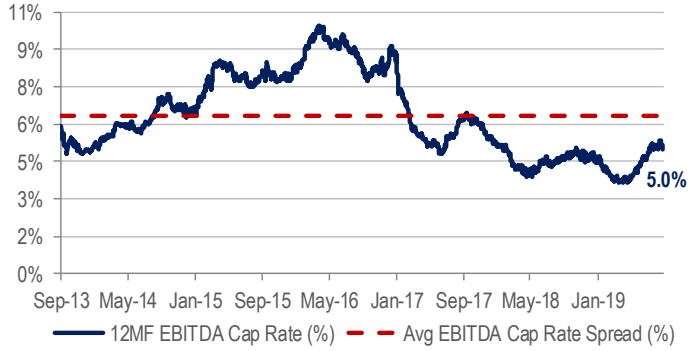
Valuation: Terra's cash-flow driven valuation metrics are attractive: 2019 implied EBITDA cap rate and dividend yield of 7.7% and 8.3%, respectively. However, its P/NAV of 0.89x is the highest in our sample of seven FIBRAs; the apparent disconnect between the highest dividend yield and the highest P/NAV valuations is explained by Terra's higher leverage.

Table 11: Terrafina – Key Metrics

	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA ('000 sqf)	39,388	41,230	41,671	41,820	41,840	41,840
Average GLA ('000 sqm)	3,659	3,830	3,871	3,885	3,887	3,887
Rental Revenue (P$m)	3,701	3,748	3,899	3,988	4,097	4,209
NOI (P$m)	3,622	3,668	3,807	3,890	3,989	4,095
EBITDA (P$m)	3,253	3,294	3,440	3,515	3,602	3,696
FFO/share (P$)	2.93	2.94	3.11	3.19	3.29	3.39
AFFO/share (P$)	2.66	2.53	2.69	2.77	2.85	2.94
EPS (P$)	1.41	2.27	2.58	2.64	2.72	2.80
Minimum pre-tax DPS (P$)	(0.88)	0.08	0.27	0.33	0.39	0.45
Expected pre-tax DPS (P$)	2.65	2.53	2.66	2.75	2.83	2.91
NAV/BVPS (P$)	36.09	34.79	35.64	36.50	36.41	36.99
Valuation						
Price/CBFI (P$)	30.5					
# of CBFIs outstanding EoP (m)	791	791	791	791	791	791
Market cap (P$m)	24,113	24,113	24,113	24,113	24,113	24,113
FX (MXN/USD):	19.1	19.4	19.6	19.9	20.2	20.5
Market cap (US$m)	1,262	1,242	1,227	1,209	1,191	
Average net debt (P$m)	17,803	18,033	17,999	17,705	17,734	17,883
(+) Other adjustments (P$m)	393	398	403	411	416	421
(-) Land Reserves (P$m)	227	227	227	227	227	227
Enterprise value (P$m)	**42,082**	**42,318**	**42,289**	**42,002**	**42,037**	**42,190**
Net LTV (%)						
Multiples						
EV/GLA (US$)	602	569	556	542	534	528
Implied NOI cap rate (%)	8.6%	8.7%	9.0%	9.3%	9.5%	9.7%
Implied EBITDA cap rate (%)	7.7%	7.8%	8.1%	8.4%	8.6%	8.8%
Rental revenue yield (%)	15.3%	15.5%	16.2%	16.5%	17.0%	17.5%
FFO yield (%)	9.6%	9.6%	10.2%	10.5%	10.8%	11.1%
AFFO yield (%)	8.7%	8.3%	8.8%	9.1%	9.3%	9.6%
Minimum dividend yield, pre-tax (%)	-2.9%	0.3%	0.9%	1.1%	1.3%	1.5%
Total dividend yield, pre-tax (%)	8.7%	8.3%	8.7%	9.0%	9.3%	9.6%
Minimum dividend yield, after-tax (%)	-2.0%	0.2%	0.6%	0.8%	0.9%	1.0%
Total dividend yield, after-tax (%)	9.6%	8.2%	8.4%	8.7%	8.9%	9.1%
Earnings yield (%)	4.6%	7.4%	8.5%	8.7%	8.9%	9.2%
P/NAV (Book Value) (x)	0.85	0.88	0.86	0.84	0.84	0.82
Net LTV (%)	37%	38%	37%	35%	36%	35%

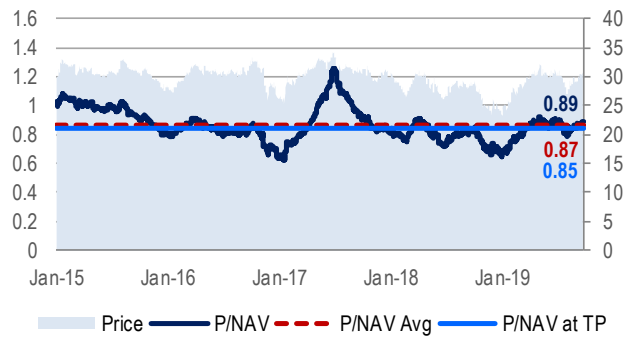
Source: Company Data, BTG Pactual estimates

Chart 68: Terrafina 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 69: Terrafina Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price target: Our DDM-driven price target of P$32/CBFI (vs. P$36/CBFI previously) implies an expected 12% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and dividend yield of 7.9% and 8.3%. Our DDM is based on a COE of 7.4% (in USD) and assumes a terminal LTV of 35% by 2023.

Table 12: Terrafina – DDM Valuation

Assumptions	
Stage 1: 2019E-2023E	
2023 AFFO (US$m)	113
Payout Ratio (%)	100%
2023 Dividends (US$m)	17
2023 Return on Capital (US$m)	96
Stage 2: 2024-2028	
Inflation (%)	0.0%
Leasing Spreads (%)	0.0%
Growth(%)	0.0%
Payout Ratio (%)	100%
Stage 3: 2029-2038	
Inflation (%)	0.0%
Leasing Spreads (%)	0.0%
Growth(%)	0.0%
Payout Ratio (%)	100%
Stage 4: Terminal Value	
Inflation (%)	0.0%
Terminal Leasing Spreads (%)	0.0%
Terminal Nominal Growth Rate(%)	0.0%
Perpetuity Dividends (US$m)	1,540

Cost of Equity Calculation	
Risk free rate, UMS (%)	7.4%
ERP (%)	5.0%
Beta	0.75
Cost of equity (%)	7.4%

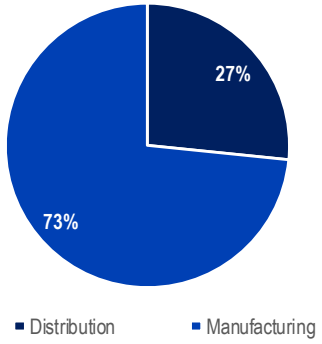
Valuation	
PV of future dividends (stage 1-stage3) (US$m)	1,536
PV of future dividends in perpetuity (US$m)	1,536
PV of future dividends (US$m)	3,072
DDM value/share (US$)	1.9
DDM value/share after-tax (US$)	1.6
DDM value/share after-tax (P$)	31.7
2018E Pro-forma official price target (US$)	**32**
12M Dividend Yield	8.2%
Upside/downside including dividends (%)	12.3%

Source: Company Data, BTG Pactual estimates

Downgrading Terra to Neutral (from Buy): We would very much like to keep Terra rated a Buy. After all, with the bulk of its exposure to the industrial sector rendering it a rare export proxy, almost 80% of cash flows in USD, most focused and straightforward equity story among the FIBRAs, and attractive cash flow valuations, it is an attractive story. However, as we discuss at length in the valuation section of this report, we are making our DDM models, which are the driver behind our FIBRA price targets, consistent by using the same 35% stabilized LTV. For Terra, this implies a reduction in the payout through 2023 that shaves P$4/CBFI from our price target, resulting in an expected total return that is consistent with a Neutral rating.

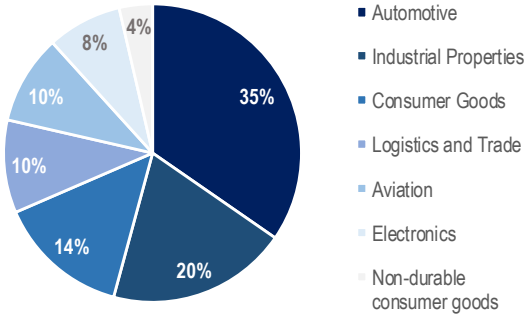
Terrafina – Business Description

Chart 70: Sector breakdown (as% of GLA)



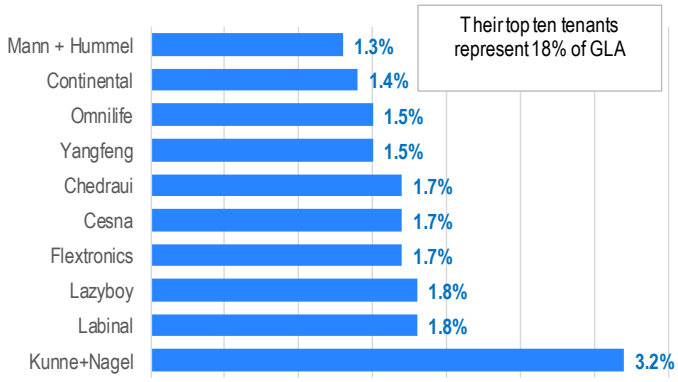
Source: Company Data, BTG Pactual Research

Chart 71: Tenants industry breakdown (as% of GLA)



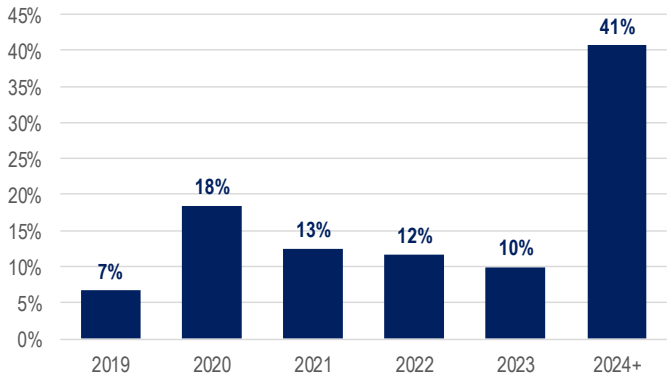
Source: Company Data, BTG Pactual Research

Chart 72: Top tenants (as % of GLA)



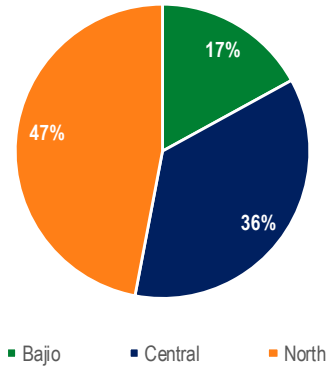
Source: Company Data, BTG Pactual Research

Chart 73: Contract expiration per year (as % of revenues)



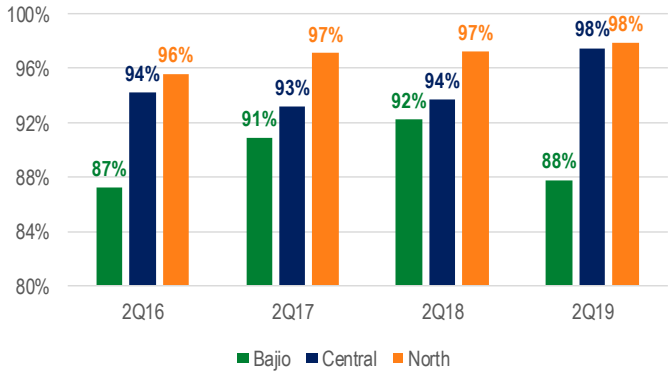
Source: Company Data, BTG Pactual Research

Chart 74: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

Chart 75: Occupancy by region(%)



Source: Company Data, BTG Pactual Research

Fibra MQ (Buy): Running a marathon, not a sprint...

Running a marathon, not a sprint...which the market is now appreciating

Unlike some peers, Fibra MQ has opted to fly under the radar: aside from its formation transactions, it has not executed on transformational acquisitions nor repeatedly tapped into capital markets to fund grandiose promises of growth. Yet it has taken a series of decisions that, while overlooked or even controversial at the time, have proven to be correct from operational, financial, or governance standpoints. None gave investors thrills, but they resulted in a steadier and more predictable ride, which recent stock performance suggests is being rewarding.

Among the best governance structures of externally-managed FIBRAs

Fibra MQ was the first to adopt many of the policies that its peers are imitating to varying degrees: a majority-independent (3 out of 5 members), non-staggered board; a properly-executed CBFI-repurchasing program; asset recycling; and reduction in payout to direct cash flows at maintenance, capex reserve, and debt-reduction. Moreover, while its market-cap linked fee was initially criticized, this has turned out to be the structure among externally-managed FIBRAs that is best aligned with shareholders and, at 5% of NOI, the cheapest among the stocks we cover.

Key risk: Lead us not into temptation...

Many of these decisions were initially unpopular (particularly the reduction in the payout) and investors showed their disapproval with their feet. Management has therefore expressed frustration from time to time, raising the risk that they fall into the traps that have ailed many peers. Fibra MQ's 48% rally YTD, however, has now taken it to all-time highs (dividend-adjusted), making it a material outperformer since its December 2012 IPO against the market as a whole and also relative to FUNO, the only listed FIBRA at the time.

We reiterate our Buy rating on Fibra MQ shares

Fibra MQ remains our preferred FIBRA: i) it is largely exposed to the industrial segment, our favorite in the industry; ii) the performance of its industrial portfolio has been among the best in the peer group; iii) 80% of its NOI is booked in USD; iv) its governance practices lead the pack; and v) valuation is compelling (2019E implied EBITDA cap rate of 9.4% and P/NAV of 0.69x). With an expected 12-month total return of 33% to our PT of P$31/CBFI (from P$30 prior), we reiterate our Buy rating.

Investment case: The Positives....

Industrial: Strong performance in the right segment. For a variety of reasons discussed in the introductory section of this report, the industrial segment remains our preferred space in Mexican industrial real estate. With over 82% of its NOI comes from its industrial portfolio Fibra MQ is very much a player in this segment (with an industrial NOI comparable to Terra's and Fibra PL's, only slightly behind FUNO's, and higher than Vesta's), and sensitive to the same dynamics that have benefited the sector. As a result, Fibra MQ has continued to post record occupancies, rental levels, and profitability, leading to a recently raised its 2019 AFFO guidance.

Retail: Better, but still underperforming. Fibra MQ's retail segment, now less than 20% of NOI, has been showing signs of improvement with regards to occupancies, same-store-performance, and rental rates. Yet, the truth is that it is underperforming other listed retail portfolios, including all those under coverage (FUNO, FSHOP, Plani, and Danhos). With industrial performing as well as it is and, if we are right, likely to continue to do so on a secular basis, it would seem that retail is, at this point, a distraction at best and therefore ripe for recycling.

Arguably the best governance among externally-managed FIBRAs... Fibra MQ has played the long game, making a series of adjustments and changes to governance that has strengthened its portfolio, balance sheet, governance, and overall investment case. For instance, Fibra MQ was among the first FIBRAs to put in place a truly independent board (3 out of 5 members are independent) comprised of truly independent individuals. It was also among the first to deliver on sizeable asset recycling, selling an aggregate of US$117.5 million representing 65% of its NOI and to execute on a CBFI buyback (it has now cancelled 5%, and is in process of cancelling another 0.4%, of its CBFIs outstanding). Finally, it was the first to pare back its payouts to retain cash for maintenance capex, development capex, debt reduction, and CBFI buybacks. Some of these have gone unnoticed and others were initially criticized by markets, but they have all proven in time to have been good decisions and validated by its recent outperformance.

...with the most minority-aligned incentive structure... When Fibra MQ first came to market, investors disliked the fee structure mostly because it included a performance fee (or promote, in real estate parlance) that whiffed to many of a hedge fund or private equity structure. In the event, it has proven, in our opinion, to be the best-aligned to shareholders. The performance fee has not been an issue since the hurdle rate (10% plus inflation) was set high enough to not have been triggered, while the market cap-linked fee reduced incentives to grow for the sake of growth, reducing risks of overextending the balance sheet or of making acquisition for the sake of NAV growth.

and cheapest fees too... In addition, this fee structure has rendered Fibra MQ the cheapest operating structure among the FIBRAs since the growth of revenues has materially outpaced that of the market cap. Fibra MQ's current 1% market cap fee (P$18 million annually at the current stock price) translates to a charge of 4.5% on rental revenue, below the average of 9.0% for the FIBRAs under coverage and cheaper even than some internally-managed structures.

Investment case: Negatives & Risks...

Retail detracts from the investment case. We argued earlier that Fibra MQ's retail portfolio is improving - and it is. But we also pointed out that it has consistently underperformed peers, which is also true. Moreover, these are assets management by third parties and in one portfolio held as a JV, where the partner, which also owns other portfolios outright, is the manager. Retail property management is much more laborious than industrial and Fibra MQ does not have the capacity to do it in-house. If the portfolio is small (less than 20% of NOI), is underperforming, and is managed by third parties, then why not sell it and recycle those cash flows into the more promising industrial segment, in which Fibra MQ actually has an edge, or return the cash to shareholders?

Questions continue to surface on the quality of the industrial portfolio. Since its IPO, the market has questioned the quality of Fibra MQ's industrial portfolio relative to those of its peers on the basis of age, location, and maintenance. Its average age of 15 years is a little older than Terra's 12.5 years, while its geographic and sector distribution is similar as well - and yet questions of this type rarely surface in discussions on Terra. Moreover, there is nothing in recent performance metrics that would suggest decay: 2Q19 occupancy of 97%, rental rates, and a 12-month retention rate of 87.5% are all be in line or above listed peers' results. Finally, between 2017 and 2018, Fibra MQ had a significant portfolio turnover (12% of its GLA) and we did not see an unusual rise in capex or tenant improvements, which is typically how any past underinvestment would make itself apparent. Nevertheless, the perception of a quality issue persists and we would be remiss not to discuss it.

Lead us not into temptation: As discussed, Fibra MQ has played the long game when it comes to managing its portfolio, governance structure, and capital. This has often left it on the outside looking in during periods of froth or of intense M&A activity, which combined with episodes of lackluster stock price performance, has sometimes led to frustration on the part of management and long-term shareholders and to questions on whether MQ should, too, be more aggressive. The recent performance of the stock, which we believe has validated this more cautious yet consistent approach, should put a damper on any such frustration, but as long as management is comprised of humans the temptation will be there.

Valuation, price target, and recommendation

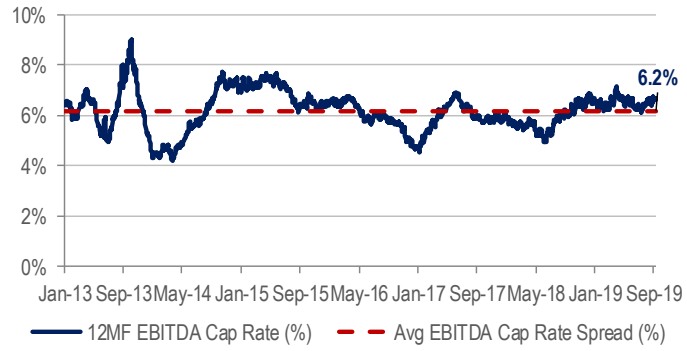
Valuation: Though not as discounted as it once was, Fibra MQ's valuation remains compelling in our view. It is trading at a P/NAV of 0.7 (the lowest among industrial peers and well below their 0.83x average) and 2019E implied EBITDA cap rate and FFO yield of 9.4% and 12.6%. Unlike that of some of its peers, with an AFFO payout ratio below 70% and an LTV of 35%, its 7% dividend yield, which is among the lower end of the spectrum, is fully underwritten by both cash flows and the balance sheet and, if anything, could rise going forward.

Table 13: Fibra MQ – Key Metrics

	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA ('000 sqm)	3,182	3,163	3,207	3,208	3,208	3,208
Rental revenue (P$)	3,320	3,505	3,751	3,679	3,776	3,855
NOI (P$m)	3,307	3,504	3,838	3,756	3,863	3,948
EBITDA (P$m)	2,962	3,164	3,412	3,302	3,385	3,444
Pro Forma EBITDA (P$m)	3,088	3,289	3,617	3,525	3,623	3,698
FFO/share (P$)	2.81	3.14	3.56	3.42	3.58	3.56
AFFO/share (P$)	2.46	2.71	3.11	2.97	3.12	3.09
EPS (P$)	2.49	1.65	2.91	3.01	3.15	1.92
Minimum pre-tax DPS (P$)	0.00	(0.57)	0.84	1.35	1.49	1.45
Expected pre-tax DPS (P$)	1.57	1.74	2.03	2.30	2.47	2.48
NAV/BVPS (P$)	34.98	35.91	37.10	37.71	37.71	37.71
Valuation						
Price/CBFI (P$)	**24.8**					
# of CBFIs outstanding (m)	788	771	770	770	770	770
FX (MXN/USD):	19.1	19.4	19.6	19.9	20.2	20.5
Market cap (US$m)	1,024	986	973	959	945	931
Market cap (P$m)	19,571	19,143	19,119	19,119	19,119	19,119
Average net debt (P$m)	15,603	14,753	13,824	12,760	13,219	14,750
Other adjustments plus JV debt (P$m)	1,172	1,207	1,234	1,234	1,234	1,234
Enterprise value (P$m)	**36,346**	**35,104**	**34,177**	**33,112**	**33,571**	**35,102**
Multiples						
EV/GLA (US$)	586	569	547	529	537	561
NOI Cap rate (%)	9.1%	10.0%	11.2%	11.3%	11.5%	11.2%
EBITDA Cap rate (%)	8.5%	9.4%	10.6%	10.6%	10.8%	10.5%
Rental revenue yield (%)	9.1%	10.0%	11.0%	11.1%	11.2%	11.0%
FFO yield (%)	11.3%	12.6%	14.4%	13.8%	14.4%	14.3%
AFFO yield (%)	9.9%	10.9%	12.5%	12.0%	12.6%	12.4%
Minimum dividend yield, pre-tax (%)	0.0%	-2.3%	3.4%	5.4%	6.0%	5.8%
Total dividend yield, pre-tax (%)	6.3%	7.0%	8.2%	9.3%	9.9%	10.0%
Minimum dividend yield, after-tax (%)	0.0%	-1.6%	2.4%	3.8%	4.2%	4.1%
Total dividend yield, after-tax (%)	6.3%	7.7%	7.2%	7.6%	8.1%	8.2%
Earnings yield (%)	10.0%	6.7%	11.7%	12.1%	12.7%	7.7%
P/NAV (Book Value) (x)	0.71	0.69	0.67	0.66	0.66	0.66
Net LTV (%)	35%	32%	30%	27%	33%	35%

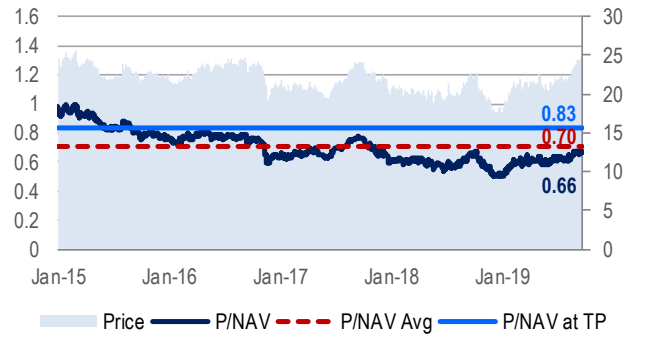
Source: Company Data, BTG Pactual estimates

Chart 76: Fibra MQ 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 77: Fibra MQ Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price target: Our DDM-driven price target of P$31/CBFI (vs. P$30 previously) implies an expected 33% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and dividend yield of 9.3% and 6.6%. Our DDM is based on a COE of 7.9% (in USD) and assumes a terminal LTV of 35% by 2023.

Table 14: Fibra MQ - DDM Valuation Summary

Assumptions	
Stage 1: 2019E-2023E	
2023 AFFO (US$m)	116
Payout Ratio (%)	80%
2023 Dividends (US$m)	54
2023 Return on Capital (US$m)	38
Stage 2: 2024-2028	
Inflation (%)	0.0%
Leasing Spreads (%)	0.0%
Growth(%)	0.0%
Payout Ratio (%)	100%
Stage 3: 2029-2038	
Inflation (%)	0.0%
Leasing Spreads (%)	0.0%
Growth(%)	0.0%
Payout Ratio (%)	100%
Stage 4: Terminal Value	
Inflation (%)	0.0%
Terminal Leasing Spreads (%)	0.0%
Terminal Nominal Growth Rate(%)	0.0%
Perpetuity Dividends (US$m)	1,466

Cost of Equity Calculation	
Risk free rate, M10 (%)	3.7%
ERP (%)	5.0%
Beta	0.85
Cost of equity (%)	7.9%

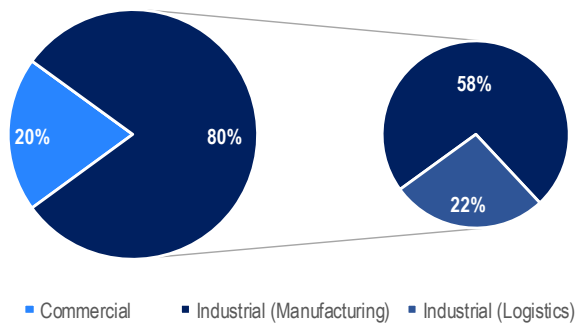
Valuation	
PV of future dividends (stage 1-stage3) (US$m)	1,552
PV of future dividends in perpetuity (US$m)	1,552
PV of future dividends (US$m)	3,103
DDM value/share (US$)	2.0
DDM value/share after-tax (US$)	1.6
DDM value/share after-tax (P$)	31.3
2019E Pro-forma official price target (P$)	**31.3**
12M Dividend Yield	7.7%
Upside/downside including dividends (%)	34%

Source: Company Data, BTG Pactual estimates

Buy Fibra MQ, our preferred fibra: With the bulk of its exposure to the industrial sector, almost 80% of cash flows in USD, leading governance among FIBRAs, sound capital allocation, and attractive valuation, Fibra MQ remains our favorite FIBRA. We thus reiterate our Buy rating.

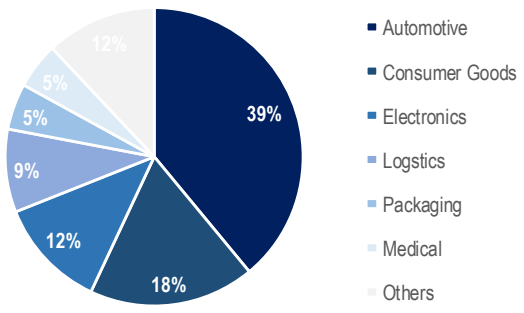
Fibra Macquarie – Company Description

Chart 78: Sector breakdown (as% of Revenues)



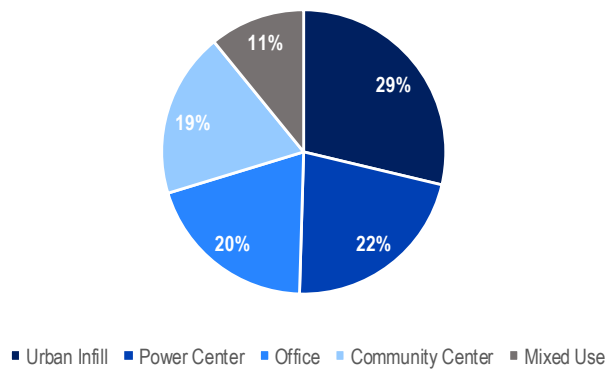
Source: Company Data, BTG Pactual Equity Research

Chart 79: Industrial – breakdown per type of industry (as % of revenues)



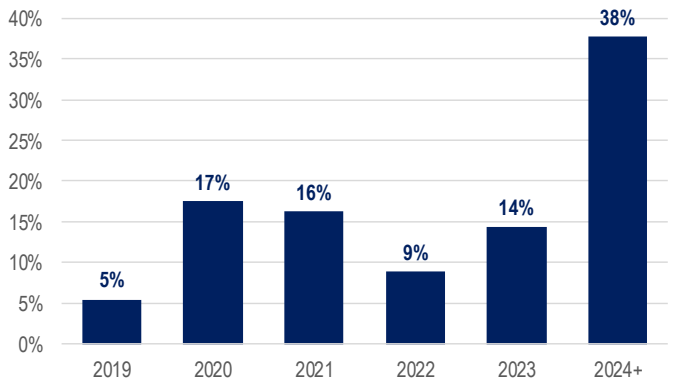
Source: Company Data, BTG Pactual Equity Research

Chart 80: Commercial – breakdown per type of mall (as % of revenues)



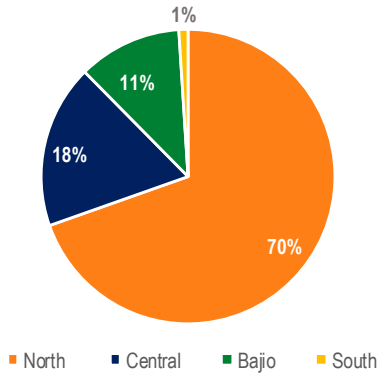
Source: Company Data, BTG Pactual Equity Research

Chart 81: Contract expiration per year (as % of revenues)



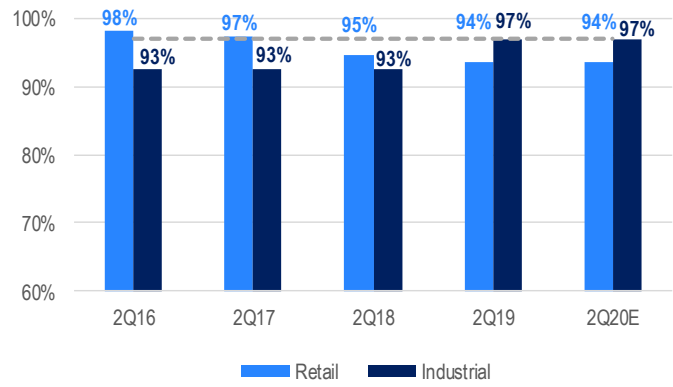
Source: Company Data, BTG Pactual Equity Research

Chart 82: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Equity Research

Chart 83: Occupancy by segment (%)



Source: Company Data, BTG Pactual Equity Research

Vesta (Buy): The Vest of both worlds...

Best in class and focused industrial portfolio boasting record occupancies

Vesta develops, owns, and manages one of the highest-quality industrial portfolios in Mexico. Starting life in 1997, Vesta has grown alongside Mexico's manufacturing base in the age of NAFTA, assembling a unique portfolio of AAA properties and tenants. Unlike most of its peers, however, Vesta was also the developer of almost the entirety of its portfolio, 30% via build-to-suit contracts. This, in our view, makes its tenant-base stickier and more loyal, enabling it to grow not only with the market but in hand with its most successful clients. Because of this quality and the underlying strength of the market, Vesta's same-store portfolio reached record occupancy of 98% in 1H19.

With none of the governance drama

Vesta is also unique among its industrial peers in that it is the only C-Corp in the pack. This frees it from the governance stigma inherent in the externally-managed FIBRA structure. Vesta has gone beyond this, however, to strengthen its governance, including assembling a highly independent and strong non-staggered board with a number of industry-experts from both Mexico and the US.

Key risk: Transitioning from high growth to balance

Vesta has long seen itself as a developer, emphasizing growth. This was true at the time of its IPO in 2012 and again in 2015 when it implemented its Vesta 20/20 strategy. To its credit, the company delivered growth in spades, but it is clear in its recently unveiled Level 3 strategy that it is transitioning to a model that better blends development growth with stabilized property portfolio management. This makes sense: the majority of its NAV is now stabilized, visibility on the global and Mexican cycles is deteriorating, and significant technological changes are underway that could dramatically change the landscape for industrial real estate over the next few decades. Executing on this downshift without entirely losing its identity as a developer will be key to Vesta's future success.

Growth optionality at FIBRA valuations: Buy Vesta (PT now P$38 from P$36)

Vesta has long been one of our favorite stocks in the Mexican real estate space and in Mexico more broadly (in fact, it is currently part of our Mexico 5SIM portfolio). We like its high-quality exposure to the industrial segment, governance and alignment, USD cash flows, a management focused on executing on a renewed and sensible strategy in Level 3, and targeted high-single digit USD FFO CAGR that should once again top its less "growthy" FIBRA peers. Yet this all comes at FIBRA-like valuations: P/NAV of 0.85x and 2019E implied EBITDA cap rate of 7.4% and dividend yield of 5.8%.

Investment case: The Positives....

Mission accomplished on Vision 20/20; Enter Level 3... In June 2019, Vesta unveiled its Level 3 initiative as the successor to its successful Vesta Vision 20/20,

which, rolled out in 2015, resulted in a doubling of GLA, stabilized occupancy of 97%, above USD-inflation rental rates, record EBITDA margin (85%), and a 16% 5-year CAGR in USD FFO/share. Having successfully established itself as a public company (Level 1) and delivered on a period of rapid growth (Level 2, Vision 20/20), Level 3 defines Vesta as a real estate company with a fully-integrated model: "a self-advised and self-managed real estate company which owns, manages, acquires, sells, develops, and re-develops properties."

Level's 3 2019-2024 targets are occupancy levels in excess of 96%, annual investments of US$120 million, recycling of US$1 for every US$2 invested, development of 16 million-plus sqf of GLA, and USD FFO/share CAGR of 8%

What's Past is Prologue: when more of the same is all you really need. While Level 3's targets are ambitious, they are no more so than what Vesta has delivered since its IPO in 2012 and particularly during the years of Vision 20/20. As such, our confidence level around management's ability to deliver on Level 3 is high as they represent a natural progression of the strategy and results achieved for the better part of the last decade.

Record operating metrics. Driven in part by the strength of the market but also due to its own ability to capitalize on the opportunities this strength provides, Vesta has continued to post record operating performance. Occupancy is at record levels, with same-store rates reaching a stunning 98% and consolidated NOI margin near 97%.

Right assets, right management, right time, and right segment. As expressed repeatedly throughout this report, we are bullish on the outlook for Mexican industrial real estate for cyclical reasons in the short term and for secular ones in the long run. With a 20-year trackrecord, almost half as a publicly traded company, Vesta has proven during both upcycles and downcycles that its assets have the quality to outperform operationally and financially, while its management has the capacity to take advantage of opportunities and to shield the company from risks. The quality of its tenant base is second-to-none, which in itself is the strongest endorsement of its assets and state of the portfolio. We therefore believe that, if our call on Mexico's industrial real estate proves correct, Vesta's operating and financial outperformance is poised to continue.

Born into strong governance. Since its birth in 1997, Vesta's founders and management have had to live with US private equity and institutional investors. This led to the immediate adoption of continuous and proper board oversight, high levels of governance, and US standards of financial management, disclosure, and reporting. As a result of this, Vesta's transition to the public sphere in 2012 was seamless and its permanent embrace of greater transparency and governance standards natural. This was tested in the 2018 transition at the helm between Lorenzo Berho Corona (founder and now Chairman) and his son, Lorenzo Berho Carranza, but with guidance from the board, Mr. Berho Corona's commitment to the governance he instilled in Vesta, and Mr. Berho Carranza's experience with and understanding of the Vesta culture, the handover took place without a glitch and much to investors' pleasing.

Owing to this history and aided by its C-Corp status, Vesta is squarely on the right side of the governance conversation that, because of the externally-managed status of its largest peers, is a recurring one among investors in the space. This does away almost immediately with the debate of whether its management and board's incentives are aligned with its shareholders'. Moreover, the strength of Vesta's set-up is magnified by the fact that, unlike those FIBRAs with NAV or NOI based fee structures, the benefits of growth (organic or inorganic) accrue directly to shareholders via the dilution of its fixed operating cost base, reinforcing the value of the development growth option.

Investment case: Negatives & Risks...

Managing the transition from Vision 20/20 to Level 3. Though the succession from one strategy to the next seems a natural evolution of Vesta's strategy, managing it carries some risks, particularly for a company that for the better part of 20 years has focused intently on growth. The greater flexibility brought by a wider array of options (including, asset sales, the first significant one of which was executed in 1H18) also implies a greater risk of error, particularly when it comes to capital allocation. Among the decisions that management will have to take during Level 3 will be the future shape of the portfolio between manufacturing and logistics, as well as what industries to emphasize and which to reduce exposure to. Not being a FIBRA, the list of temptations might include a foray abroad (already turned down at least once that we know of), particularly if growth begins to slow in Mexico.

Sometimes an orphan? As discussed, there are a number of advantages to Vesta's being a C-Corp rather than a FIBRA. There are, however, some disadvantages, with the obvious one being taxes, which, as a pass-through vehicle, the FIBRA structure is designed to minimize (though, ultimately, the recipient of its dividends pay them). Disadvantageous as this may be at the Vesta level, however, it is relatively straightforward for investors to put a price the burden of higher taxes, meaning that it likely becomes a wash at the end of the day.

What is more difficult to assess and manage is the effects of technical factors that seem irrelevant from a fundamental standpoint but have a real-world impact on stock performance. Specifically, we are referring to the fact that AFOREs (as Mexico's pension funds are known) have a regulatory allocation to FIBRAs that they have historically preferred for their real estate exposure, leaving them free to use their equities allotment to gain exposure to other sectors and, more typically, to hedge MXN via foreign equity indices (since AFOREs are prohibited from buying FX directly). This reduces somewhat the pool of potential Vesta buyers, increases its reliance on foreign investors relative to both FIBRAs and most Mexican equities, and explains why sometimes Vesta seems to trade in a world of its own.

Bajío exposure: from strength to weakness? Since its IPO, Vesta's exposure to Bajío, which represents almost half of GLA and is over twice as large as its next largest market, Central Mexico, has been considered a strength given that it is at the core of the second wave of NAFTA investments. This included the most recent wave of auto investments and a significant share of the aerospace investment, both of which are seen as more value-added and requiring greater domestic content than

much of what was seen in border regions in the early NAFTA years. Also, because of its more central location, greater proximity to Central Mexico, and the web of suppliers it was assembling, Bajío was seen as a promising market for logistics activity, which is typically seen as higher-quality than light manufacturing.

But, in recent quarters, Bajío, which is the one market where supply has continued to increase at the margin, has seen a slight slippage in occupancies and less traction in rents. This is true in particular when compared with the border markets of Ciudad Juárez (Mexico's largest industrial hub) and Tijuana. And the type of industry present in Bajío likely renders it more vulnerable to both a turn in the US cycle and, over the long-run, to the shift away from the internal combustion engine towards EVs.

Valuation, price target, and recommendation

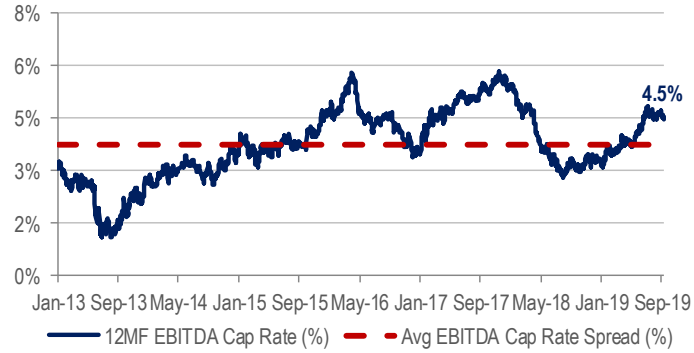
Valuation: Vesta is trading at a P/NAV of 0.84 and 2019E implied EBITDA cap rate and dividend yield of 7.4% and 5.8%, FIBRA-type valuations in spite of better growth prospects and stronger governance.

Table 15: Vesta – Key Metrics

	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA ('000 sqm)	2,654	2,776	2,890	3,174	3,367	3,560
Rental revenue (US$m)	133	146	157	174	186	199
NOI (US$m)	128	140	149	167	179	190
EBITDA (US$m)	113	124	131	147	157	167
FFO/share (US$)	0.09	0.09	0.12	0.12	0.13	0.14
EPS (US$)	0.15	0.18	0.10	0.10	0.11	0.12
Expected DPS (US$)	0.08	0.09	0.08	0.09	0.09	0.10
NAV/BVPS (US$)	1.78	1.87	1.88	1.89	1.91	1.93
Net LTV (%)	32%	28%	28%	31%	34%	37%
Avg. # of shares outstanding (m)	592	581	584	584	584	584
Valuation						
MXN/USD	19.7	19.5	19.8	20.1	20.4	20.7
Price / share (P$)	30.5					
# of shares outstanding (m)	592	581	584	584	584	584
Market cap (P$m)	18,053	17,701	17,780	17,780	17,780	17,780
Market cap (US$m)	919	908	912	912	912	912
Land Reserves Book Value (US$m)	62	62	62	62	62	62
Adj. Market cap (US$m)	857	846	850	850	850	850
Average net debt (US$m)	635	613	665	775	854	930
Enterprise value (US$m)	1,553	1,521	1,577	1,687	1,766	1,842
(-) Land Reserves Book Value (US$m)	62	62	62	62	62	62
(+) Deferred Tax Liability	215	226	235	240	245	250
Adj. Enterprise value (US$m)	1,707	1,685	1,750	1,865	1,949	2,030
Multiples						
EV/GLA (US$)	643,045	607,144	605,670	587,740	578,826	570,252
Implied NOI cap rate (%)	7.5%	8.3%	8.5%	9.0%	9.2%	9.4%
Implied EBITDA cap rate (%)	6.6%	7.3%	7.5%	7.9%	8.1%	8.2%
Rental revenue yield (%)	7.8%	8.7%	9.0%	9.3%	9.6%	9.8%
FFO yield (%)	6.4%	6.3%	8.0%	8.0%	8.8%	9.8%
Dividend yield (%)	5.1%	5.8%	5.0%	5.7%	5.8%	6.5%
Earnings yield (%)	9.5%	11.7%	6.4%	6.4%	7.2%	8.1%
P/NAV (Book Value) (x)	0.87	0.84	0.82	0.80	0.78	0.76

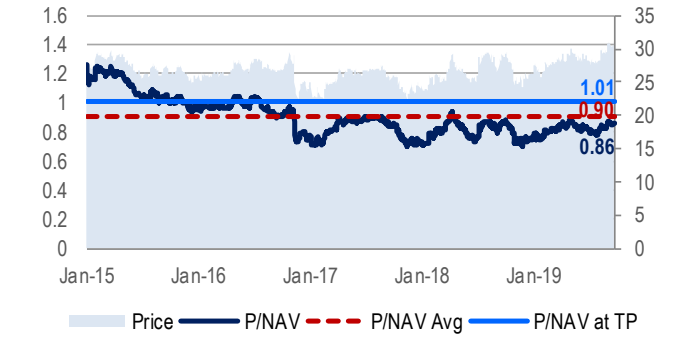
Source: Company Data, BTG Pactual Research

Chart 84: Vesta 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 85: Vesta Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price target: Our blended DDM and Exit cap rate-driven price target of P$38/share (vs. P$36 previously) implies an expected 30% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and dividend yield of 6.6% and 4.6%. We use a COE of 7.7% in USD and an exit NOI cap rate in 2026 of 8%.

Table 16: Vesta – Exit Cap Rate Analysis

Exit cap rate analysis (US$m)	
2026E NOI	201
Exit Cap Rate (%)	8.0%
2026E Real Estate EV	2,511
(+) 2026E Land Reserve	62
(=) 2026E EV	2,573
(-) 2026E Net Debt	980
(=) 2026E Equity Value	1,593
(-) 2026E Deferred Taxes	265
(=) 2026E Equity Value	1,328

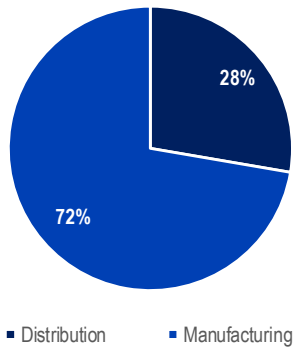
FCFE Valuation + Exit Cap Rate (US$m):	
PV of dividends through 2026	307
PV of Terminal Value	823
Fair equity value	**1130**
Fair equity value	**1130**
# of shares (fully diluted))	581
Per Share (US$)	2
Per Share (P$)	**38**
Dividend Yield (%)	3%
Upside (%)	4%

Source: Company Data, BTG Pactual Estimates

Buy Vesta: With one of the best industrial portfolios and tenant bases in Mexico, 85% of cash flows in USD, none of the governance-related concerns of externally-managed structures, and attractive FIBRA-like valuations in spite of inherently better growth prospects, Vesta remains our preferred Mexican real estate name and one of our favorite stocks in Mexico altogether. We thus reiterate our Buy rating.

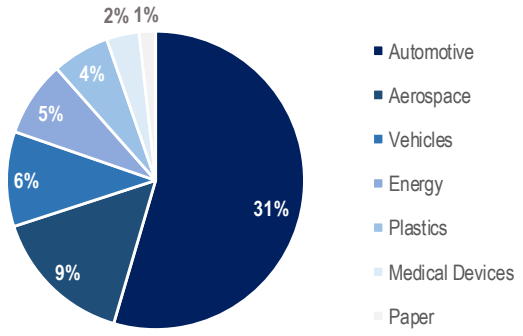
Vesta – Company Description

Chart 86: Sector breakdown (as% of GLA)



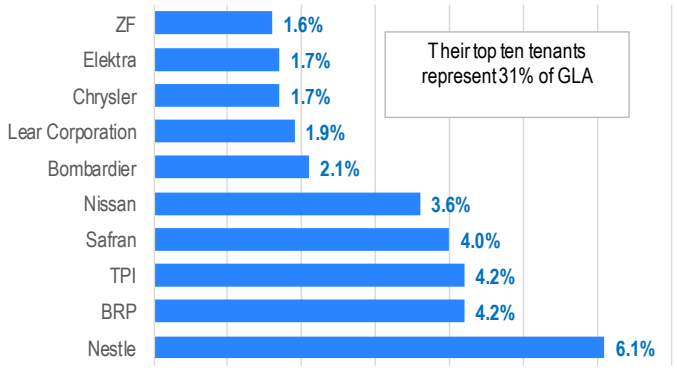
Source: Company Data, BTG Pactual Research

Chart 87: Tenants Industry Breakdown (as% of GLA)



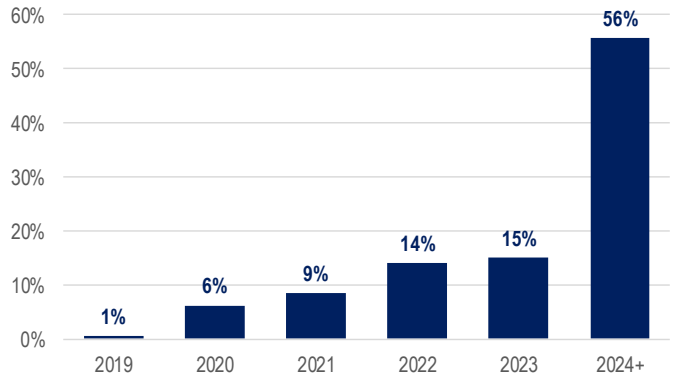
Source: Company Data, BTG Pactual Research

Chart 88: Top tenants (as % of GLA)



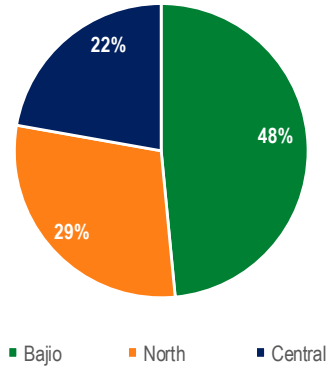
Source: Company Data, BTG Pactual Research

Chart 89: Contract expiration per year (as % of GLA)



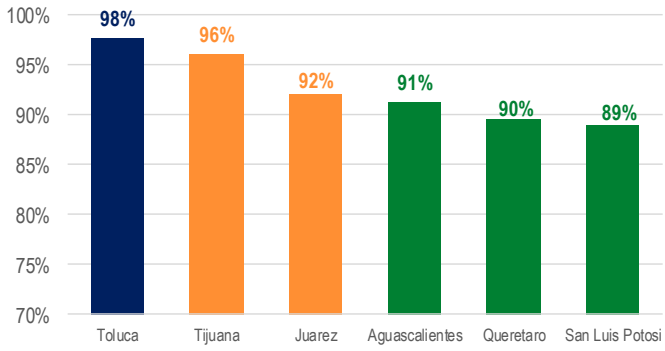
Source: Company Data, BTG Pactual Research

Chart 90: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

Chart 91: Occupancy by geography (%)



Source: Company Data, BTG Pactual Research

Fibra Monterrey (Buy): The Little Fibra that could

Unique governance structure among FIBRAs...

FMTY was the first FIBRA to have been internally operated and managed since the outset, setting it apart in investors' eyes from a governance standpoint. Further, there is no control trust (i.e., control lies in the float), it has an unstaggered board (almost three-fourths of which is comprised by independents), and is run by a professional and fully-dedicated management team that investors can remove without penalty or undue obstacles.

...combined with strong delivery set it aside among sector small caps

Though FMTY is in the process of raising equity for the third time since its IPO in December 2014, by doing so through rights offerings or via a pre-aproved ATM facility, in close consultation with its largest institutional shareholders, and with a clear and tangible use of proceeds that has, thus far, been executed on swiftly, it has managed to do so with a minimal effect on per CBFI metrics. FMTY has thus grown from a portfolio of nine properties with a GLA of 133K sqm and an NAV of P$2.8bn at the time of the IPO to one that as of 1H19 54 properties with GLA of 661K sqm and NAV of P$13.2 billion. This, along with the scale benefits of being internally managed, has produced growth AFFO/CBFI from P$0.82 in 2015 to an annualized P$1.17 in 2Q19 (10% CAGR).

Key risk: Will it manage to break out above the cloud cover?

The FIBRA space is not an easy one to stand out in: it is crowded (there are a total of 17 real estate FIBRAs plus C-Corps listed in Mexico), only a handful of stocks trade above US$1m/day (putting the bulk of the sector off most institutional investor radar screens), and most seem to be painted by investors with the same brush (especially the mid and small caps). Because of its superior governance and track record, FMTY punches above its weight (US$390m market cap and US$0.1m ADTV) with the AFORE investor base, but there is no guarantee that it will be able to tap into international institutional debt and equity markets with the same success.

Initiating FMTY with a Buy rating and a P$14/CBFI PT

Our DDM-driven price target implied 12-month total return of 24%. Given its low liquidity and size, FMTY is not for every investor, but it is for those who are happy owning small caps and growing alongside a management team that has embraced the concept of strong corporate governance and of partnership with minority investors, that has found a way to expand via the acquisition of assets off larger competitors' radar screens, and that is committed to growing consistently but accretively. Its 0.85x P/NAV is attractive for an internally-managed structure as are its 8.1% EBITDA cap rate and 9.3% dividend yield.

Investment case: The Positives....

Governance: born free of the sector's original sin... As discussed throughout this report, the external management structure that the FIBRA sector began its life with is the root cause of many of the market's reservations on its governance. It is therefore tantamount to its original sin, the first flaw from which all others flow. At the core of this structure was the initial interpretation by tax accountants that because FIBRAs are trusts they should be prohibited from having employees (the logic being that if trusts could have employees, all Mexican companies would soon transition to them to avoid taxes). Hence, the first batches of FIBRAs were all floated as externally-managed structures.

As the governance implications of this began to be reflected in share prices and the ensuing difficulties in raising capital, regulators reconsidered their stance towards the notion of internally-managed structures, provided they complied with a number of conditions set by tax authorities. Though a handful internalized fully (FINN) or partially (FSHOP) with varying degrees of success, FMTY was the first FIBRA to be fully internalized since inception and, it would seem from relative valuations, to have been more fully rewarded for it.

The internalization automatically eliminates three features common in externally managed structures that most irk investors: i) managements are not paid by fees — rather, they are paid a salary and incentives that more clearly align their interests with those of equity holders; ii) equity holders share more fully in the rewards of growth via the operating synergies and fixed cost dilution from adding properties to the management platform; and iii) it is easier for shareholders to remove underperforming management teams.

Governance: with other ribbons too... Though internalization is a first and key step towards adopting world-class REIT governance, it is not limited to this. And in this respect, FMTY has also set itself up since the outset as being on the right side of the debate. It has a board that is 71% comprised by independents and their tenure is unstaggered. Moreover, it has professional management that is appointed by the board and can be removed without penalty or undue obstruction. Similarly, there is no control group *per se*, rendering FMTY as an all too rare "market-controlled" entity on the Mexican Bolsa (especially now that the latest round of proposed governance changes will eliminate the board's vetting of equity stakes in excess of 10%). Finally, since its IPO, management has nourished a close proximity to its institutional shareholder base, consulting them and communicating clearly on all major capital raising and allocation decisions.

High-quality shareholder base with control in the float. FMTY's largest shareholder (with roughly 20%), Chairman of its Technical committee, and original sponsor and purveyor of much of the initial portfolio, Federico Garza Santos, is a successful real estate developer and investor from Monterrey who has been active in the space for over three decades and is well-regarded among business circles throughout the country. Another 11% is owned by other real estate developers/investors who received CBFIs in exchange for properties acquired by FMTY. And the rest is effectively owned by various institutional and individual

investors (including 34% owned by three of the largest AFOREs), putting the free float at almost 70% and placing control of the company squarely with the public.

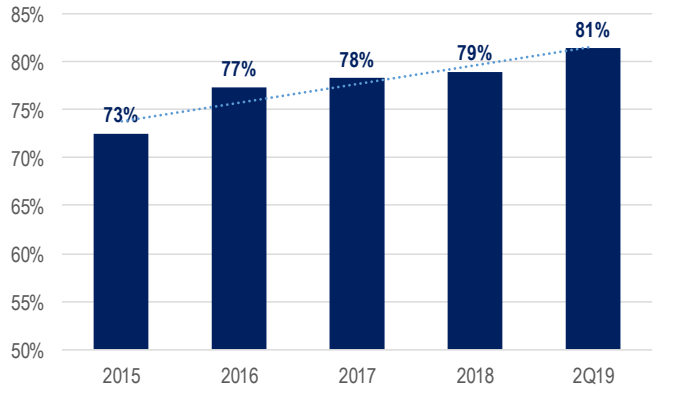
Execution: growth without dilution. FMTY is in the midst of executing its fourth equity offering since 2014, making it one of the most active among all FIBRAs on the capital raising front. For most FIBRAs, this level of activity would have become an irritant for shareholders as it would likely have translated into recurring dilution that effectively deferred the payout benefits from growing the size of the portfolio. In FMTY's case, however, this has turned out not to be the case, to some degree because of the advantages of being smaller but also because management has handled the raises intelligently. For instance, it would seem that more than any other FIBRA, FMTY has dealt with its largest institutional investors (i.e., the AFOREs) as partners, informing them on their expansion opportunities, consulting them on the timing of capital raises, and executing them in such a way that minimizes the dilution, cost, and disruption to equity holders (rights offerings and the ATM facility available to FIBRAs, etc.).

Moreover, by raising relatively manageable amounts and, because of its size, by focusing on properties or portfolios where the number of potential bidders is smaller (as the larger FIBRAs would typically look at larger tickets), the deployment of the capital raised has historically taken place rapidly (often immediately). This has significantly shortened the period of time during which per CBFI returns are diluted, contrasting sharply with peers for which the dilutive effects of arguably excessively large capital raises can linger on for several quarters.

Putting this into numbers, FMTY has grown its portfolio from nine properties with a GLA of 133K sqm and an NAV of P$2.8 billion at the time of the IPO to one that as of 1H19 had 54 properties with GLA of 661K sqm and NAV of P$13.2 billion. This growth has been compounded by the USD tilt of their portfolio and the scale benefits of internalization, with EBITDA margin rising from 72.5% in 2015 (FMTY's first full year in operation) to 81.4% in 2Q19, resulting in an almost four-fold increase in annualized NOI to P$1 billion (39% CAGR). All of this has produced growth AFFO/CBFI from P$0.82 in 2015 to an annualized P$1.17 in 2Q19, a 10% CAGR.

Turning a weakness into a strength #1: operating leverage. Since inception, FMTY's management has turned what would typically be considered a disadvantage into one of its key strengths: it's small size relative to peers. Part of this is a by-product of its internalization, which granted FMTY scale benefits as its portfolio grew that its externally-managed peers, despite being larger, lacked because of their NAV or NOI-based fees (the exception being Fibra MQ, where fixed cost dilution occurred as NOI growth outpaced that of market cap, the basis of its fee). Thus, even while smaller, FMTY managed to deliver on margin expansion in both NOI and (especially) EBITDA that has been largely unmatched by its FIBRA peers.

Chart 92: Fibra Monterrey – EBITDA Margin Evolution



Source: Company Data, BTG Pactual

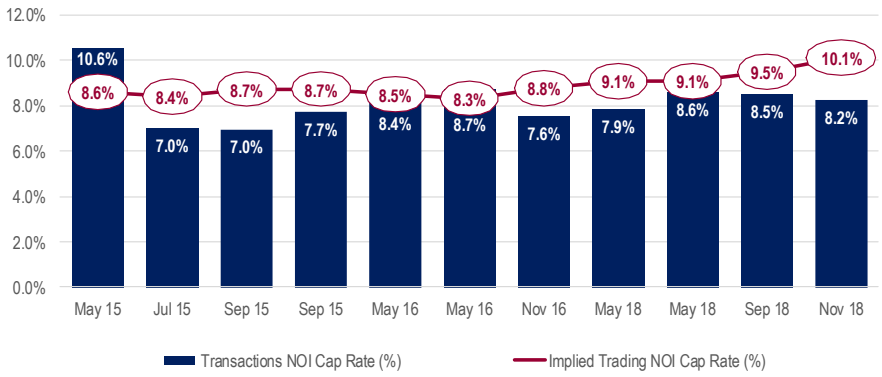
Turning a weakness into a strength #2: stealth property purchases... The second benefit from its smaller size is FMTY's ability to purchase portfolios or properties that are too small or laborious to be focused on by larger peers, who require chunkier tickets to move their needles. One representative example of this is its recent acquisition of Whirlpool facilities and headquarters outside of Monterrey (purchased in 2018), which was structured in the form of a tailor-made sale-and-lease back that was likely too small for any larger FIBRA to seriously consider given the work it implied despite the client's being a AAA, USD-paying tenant. This agility, borne of its smaller size, has allowed FMTY not only to add assets at accretive cap rates, but also to deploy its capital more rapidly, which together with the fixed cost dilution that its management structure allows for, combines for a materially shorter lead-time to per CBFI growth for its shareholders.

Chart 93: Fibra Monterrey M&A vs Trading Cap rates %

	Transaction Date	Region	GLA (sqf)	Transaction Value (US$m)	USD NOI Cap Rate (%)	Price per sqf (USD/sqft)
Portafolio Casona	May 15	North	426,250	18	10.6%	43
Catacha Industrial Building	Jul 15	North	62,431	3	7.0%	40
Milwaukee Portfolio (Binding agreement)	Sep 15	Bajio	64,583	5	7.0%	85
Santiago	Sep 15	Bajio	177,572	8	7.7%	44
Portfolio Nico 1	May 16	North	469,306	27	8.4%	57
Portafolio Providencia	May 16	North	1,072,214	47	8.7%	44
Catacha 2 (Industrial Development)	Nov 16	Bajio	58,125	3	7.6%	50
Portfolio Horizonte (Panamericana 1)	May 18	North	227,301	7	7.9%	32
Portfolio Horizonte (Panamericana 2)	May 18	North	254,738	17	8.6%	68
BTS in Santa Catarina, Nuevo León (Zinc)	Sep 18	North	206,667	10	8.5%	50
Whirpool Complex in Apodaca	Nov 18	North	1,599,300	135	8.2%	84
Average			419,863	25.5	8.2%	54.2

Source: Company Data, BTG Pactual Research

Chart 94: Fibra Monterrey M&A vs Trading Cap rates %



Source: Company Data, BTG Pactual Research

Largely industrial and primarily USD... At this point of this report, it is fair to say that we have discussed *ad nauseam* why we generally prefer both the industrial space and USD-denominated portfolios. As of 2Q19, FMTY ticks both boxes: its industrial portfolio accounts for 47% of its revenue (and likely more than half its NOI given the segment's higher margins) and USD leases represent 70% of the total. In fact, the underlying economic exposure to industrial is even likely greater as a significant share of the 3% of revenue that FMTY has in the retail segment comes from car dealerships, which are typically located on land parcels that would ultimately be more suitable for industrial or logistics activities.

Increasingly diversified by property and region, but Monterrey still the engine. Today, FMTY has over 54 properties with 120 tenants largely distributed among five states that jointly represent a little over 90% of revenue. Its largest client, Whirlpool, represents 20% of revenue, but this concentration drops quickly as its second largest, Crisa, is only 4%. Moreover, Nuevo León, home to Monterrey, still accounts for 63% of total revenue, which while admittedly concentrated, it is concentrated in the right place.

Strong operating and financial performance in 1H19. In 2Q19, FMTY reported occupancy of 96.9%, up 40bps YoY even as GLA grew 31% YoY to 661K sqm. USD rents rose 9% YoY in retail, 7% in industrial, 6% in back offices, and 2% in corporate offices, materially outpacing inflation. NOI and EBITDA margins expanded by 150bps and 210bps to 90.1% and 81.4%, respectively. AFFO/CBFI and Distributions/CBFI rose by 7% YoY to P$0.29. Net LTV ended 2Q19 at 29.0% vs. 31.0% in 4Q18 and 10.1% 2Q18

Investment case: Negatives & Risks...

Low stock liquidity. While from an operating and performance standpoint FMTY is comparable against the first division of the FIBRA space, from a liquidity standpoint it remains firmly in the second division. YTD its ADTV is US$100K, slightly below the US$107K of 2018. While this is significantly better than it was in past years (e.g., US$70K in 2017), it remains well below the threshold required for international institutional investors to seriously look at the stock. The forthcoming offering, which

seeks to raise ~P$3-4 billion (relative to a market cap of P$7.7 billion), should help somewhat.

Will it manage to break out without losing its edge? Arguably, FMTY's operating performance and its valuation suggest that it already is in the top flight of the FIBRA space, but from a liquidity standpoint it remains very much a minnow. To a large degree, this is the flip side of how well it has managed its capital raising exercises. By placing small, digestible amounts largely to its existing shareholders, the amount of stock that is truly available to trade remains limited. To truly break into the sector's top division, FMTY will at some point have to place a larger amount of CBFIs to new investors, ideally including to institutions outside of Mexico. This will present two challenges: i) it could strain the partnership it currently has with its AFORE shareholders and ii) FMTY could struggle to deploy a larger amount of capital with the same alacrity of the past, extending the burden of dilution.

Can it maintain its agility as it grows? This is essentially an extension of the question above. As FMTY becomes larger, the agility in purchasing small portfolios that is a hallmark of his success is likely to be compromised to a degree. For one, purchased portfolios will have to become larger and larger to move the needle. And, second, as targets become larger, FMTY's ability to fly under the M&A radar will be dented, forcing it to compete with its larger peers to the likely detriment of valuation and speed of delivery.

Among the least CDMX-metro area exposed. The CDMX-metro area accounts for only 4% of FMTY's revenues, which for a portfolio that is over 50% exposed to office and retail, is unusual — perhaps only Plani and FSHOP have comparable CDMX-metro exposure. But Plani and FSHOP are focused entirely on the retail segment and typically on B, C, and D demographics, which would justify focusing exposure outside of CDMX. For FMTY, the bulk of their non-industrial portfolio is office, in which the CDMX market and small slices of Monterrey and Guadalajara is arguably the only one with meaningful AAA-class properties. Though the bulk of the oversupply of office space is in CDMX, we would argue that second tier markets and cities are more likely to be vulnerable to a cyclical downturn, around which there continues to be concerns.

Office exposure...should we worry? Admittedly, the portion of FMTY's office portfolio that is linked to its industrial properties would be less susceptible (to the degree that the industrial space is more defensive) to cyclical downturns. And, as discussed above, the majority of the portfolio is outside of CDMX, which is where office segment oversupply is a concern. But office is the segment we like the least and, in spite of definite nuances, FMTY's portfolio is significantly exposed to it.

Valuation, price target, and recommendation

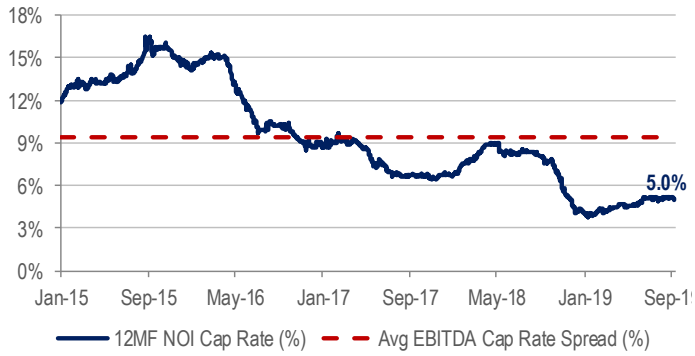
Valuation: FMTY is trading at a P/NAV of 0.86x and 2019E implied EBITDA cap rate and dividend yield of 8.0% and 9.3%, which find attractive considering its internalized management structure and the historical growth of its key metrics on a per CBFI basis.

Table 17: Fibra Monterrey – Key Metrics

Valuation Summary (In MXN$)	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA (sq m)	544	671	680	680	680	680
Rental revenue (P$)	945.82	1,194.00	1,233.26	1,273.86	1,301.02	1,328.83
NOI (P$m)	833.9	1,065.5	1,096.3	1,132.4	1,156.6	1,181.3
EBITDA (P$m)	744.2	956.8	977.9	1,010.0	1,031.6	1,053.6
FFO (P$m)	710.43	815.97	741.04	776.67	797.18	811.43
FFO/share (P$)	1.12	1.28	1.16	1.21	1.25	1.27
EPS (P$)	1.74	0.69	1.08	1.13	1.17	1.19
Minimum pre-tax DPS (P$)	1.55	(0.16)	(0.31)	0.25	0.30	0.33
Total pre-tax DPS (P$)	1.07	1.11	1.10	1.13	1.17	1.19
NAV/BVPS (P$)	13.93	13.97	14.09	14.24	14.24	14.24
Valuation						
Price/CBFI (P$)	12.0					
# of CBFIs outstanding (m)	636.2	640.0	640.0	640.0	640.0	640.0
FX (MXN/USD):	19.1	19.4	19.6	19.9	20.2	20.5
Market cap (US$m)	399.5	395.6	390.9	385.1	379.4	373.8
Market cap (P$m)	7,634.0	7,679.6	7,679.6	7,679.6	7,679.6	7,679.6
Average net debt (P$m)	2,237.5	4,100.4	4,063.9	4,096.6	4,355.3	4,719.4
Other obligations net of refundable taxes (P$m)	(239.0)	116.5	(48.3)	(53.0)	(61.1)	(65.8)
Enterprise value (P$m)	9,632.5	11,896.5	11,695.2	11,723.3	11,973.8	12,333.2
Multiples						
EV/GLA (US$)	0.93	0.91	0.87	0.86	0.87	0.88
Implied NOI cap rate (%)	8.7%	9.0%	9.4%	9.7%	9.7%	9.6%
Implied EBITDA cap rate (%)	7.7%	8.0%	8.4%	8.6%	8.6%	8.5%
Implied EV/EBITDA (x)	12.9	12.4	12.0	11.6	11.6	11.7
Rental revenue yield (%)	12.4%	15.5%	16.1%	16.6%	16.9%	17.3%
FFO yield (%)	9.3%	10.6%	9.6%	10.1%	10.4%	10.6%
Price/FFO (x)	10.7	9.4	10.4	9.9	9.6	9.5
Total dividend yield, pre-tax (%)	8.9%	9.3%	9.2%	9.4%	9.7%	9.9%
Total dividend yield, after-tax (%)	5.3%	9.6%	9.9%	8.8%	9.0%	9.1%
Earnings yield (%)	14.5%	5.7%	9.0%	9.4%	9.7%	9.9%
P/NAV (Book Value) (x)	0.86	0.86	0.85	0.84	0.84	0.84
Net LTV (%)	31.0%	28.3%	29.0%	28.4%	33.6%	35.0%

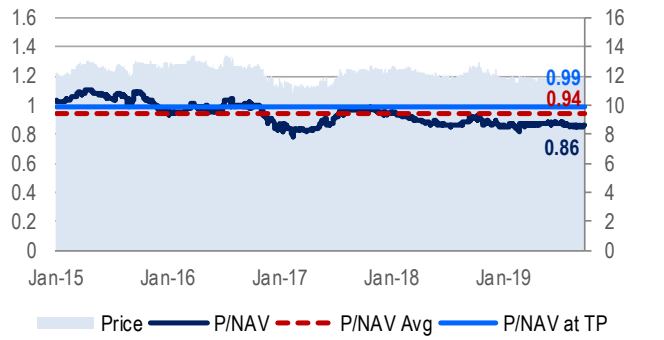
Source: Company Data, BTG Pactual estimates

Chart 95: Fibra Monterrey 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 96: Fibra Monterrey Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price Target: Our DDM-driven price target of P$14/CBFI implies an expected 24% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and dividend yield of 7.5% and 7.9%. Our DDM is based on a USD COE of 8.2% and assumes a terminal LTV of 35% by 2023.

Table 18: Fibra Monterrey – DDM Valuation Summary

Assumptions	
Stage 1: 2019E-2023E	
2023 AFFO (US$m)	37
Payout Ratio (%)	100%
2023 Dividends (US$m)	10
2023 Return on Capital (US$m)	27
Stage 2: 2024-2028	
Inflation (%)	0.0%
Leasing Spreads (%)	0.0%
Growth(%)	0.0%
Payout Ratio (%)	100%
Stage 3: 2029-2038	
Inflation (%)	0.0%
Leasing Spreads (%)	0.0%
Growth(%)	0.0%
Payout Ratio (%)	100%
Stage 4: Terminal Value	
Inflation (%)	0.0%
Terminal Leasing Spreads (%)	0.0%
Terminal Nominal Growth Rate(%)	0.0%
Perpetuity Dividends (US$m)	456.5

Cost of Equity Calculation	
Risk free rate, UMS (%)	3.7%
ERP (%)	5.0%
Beta	0.90
Cost of equity (%)	8.2%

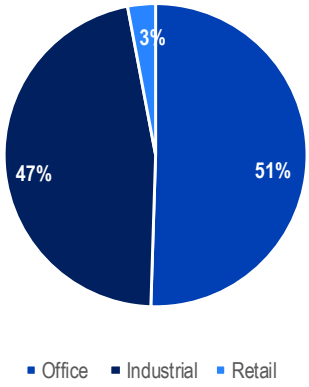
Valuation	
PV of future dividends (stage 1-stage3) (US$m)	416
PV of future dividends in perpetuity (US$m)	95
PV of future dividends (US$m)	512
DDM value/CBFI (US$)	0.8
DDM value/CBFI after-tax (US$)	**0.7**
DDM value/share after-tax (P$)	**13.7**
2019E Pro-forma official price target (US$)	**14**
12M Dividend Yield	9.3%
Upside/downside including dividends (%)	24.0%

Source: Company Data, BTG Pactual Estimates

Recommendation: When discussing Mexico Strategy, we often get asked about what small caps we would own in Mexico – FMTY would now feature prominently on that list. Given its low liquidity and size, FMTY is clearly not for every investor. But it is for those who are happy owning small caps and growing alongside a management team that has embraced the concept of strong corporate governance and of partnership with minority investors, that has found a way to expand via the acquisition of assets off larger competitors' radar screens, and that is committed to growing consistently but accretively. And, though low liquidity is an issue, this should improve somewhat with its forthcoming equity offering (slated for late October 2019) and is partially alleviated by a dividend yield above 9%.

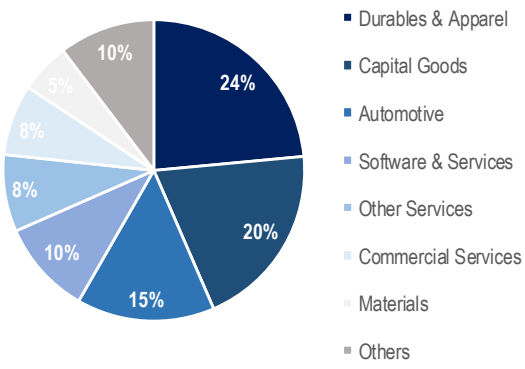
Fibra Monterrey – Company Description

Chart 97: Sector breakdown (as% of revenues)



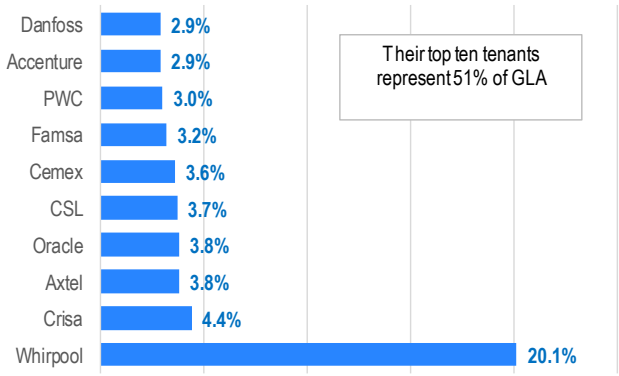
Source: Company Data, BTG Pactual Research

Chart 98: Tenants' industry breakdown (as% of revenues)



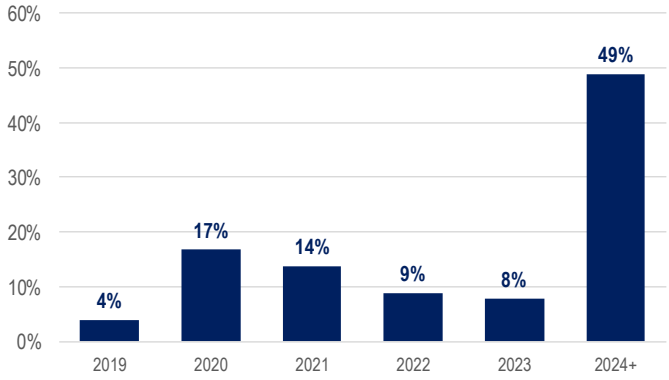
Source: Company Data, BTG Pactual Research

Chart 99: Top tenants (as % of revenues)



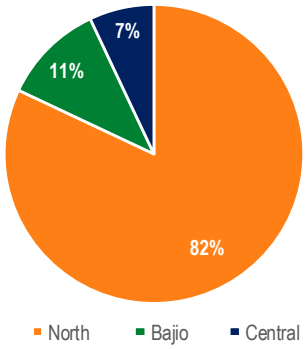
Source: Company Data, BTG Pactual Research

Chart 100: Contract expiration per year (as % of revenues)



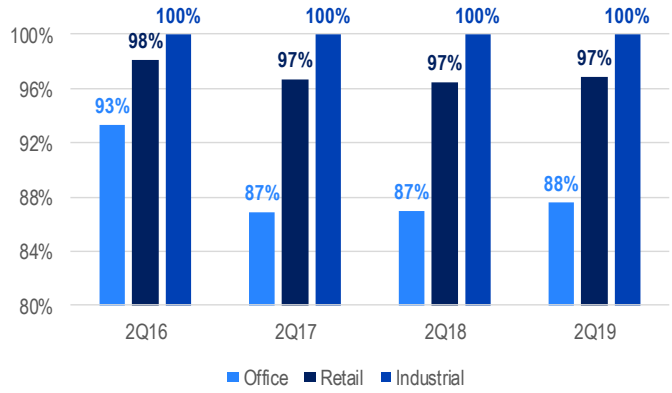
Source: Company Data, BTG Pactual Research

Chart 101: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

Chart 102: Occupancy by geography (%)



Source: Company Data, BTG Pactual Research

Fibra Shop (Neutral): Running to stand still

Outperforming operationally...

Contrary to what many thought at the time of its IPO, FSHOP has managed to hold its own with some of the best-positioned incumbent retail portfolios in the industry. Over the past three years, it has delivered revenue, NOI, and EBITDA growth of 17%, 19%, and 20%, with occupancy rates reaching a record level 96% in 1H19 and rental rates rising well above inflation and in line with its most successful peers.

...yet running to stand still

However, because the company was caught wrong-footed when Banxico's post-Trum tightening cycle began, almost all of that growth has been to the benefit of creditors: its FFO and distributions in the same timeframe have fallen by 1% and 2%. And while many of its capital allocation decisions in the interim would seem justified on a case-by-case basis - development, purchasing *La Victoria* in Querétaro, buying back CBFIs, selling UC Condesa - they have done nothing to meaningfully address the liability side of the balance sheet, the feeding of which has consumed most of its growth in NOI.

Key risk: caught in the whirlpool

This lack of traction and and its small size have translated into a dramatic decline in liquidity, feeding into its de-rating, which has in turn exacerbated low stock liquidity, all wrapped around the de-rating that global retail has suffered at the hands of e-commerce concerns. Though a loosening interest rate cycle might help FSHOP gradually reduce its cost of financing, it would seem at this point that the only quick-fix would be some sort of sale or merger, which management seems unwilling to contemplate and that its contract with the FIBRA leaves at its discretion.

Downgrading to Neutral on P$8.5/CBFI PT (from P$16 prior)

On a current valuation basis, FSHOP remains among the most attractively valued stocks in our now-expanded universe. But, though it is a key component, valuation is not the only driver behind our ratings and it is on the other fronts, such as liquidity or sustainability of distributions, that FSHOP ranks low. Our DDM-based PT reflects a sharp drop in FSHOP's modeled payout (from 82% in 2020 to 35% through 2023) to enable it to gradually recapitalize the balance sheet and reduce its LTV to the 35% level at which we have opted to stabilize by 2023 all stocks under coverage. On this basis, the 12-month total return implied by our PT is roughly 12%, consistent with a Neutral rating.

Investment case: The Positives....

FSHOP remains the only pure retail play among the FIBRAs. Though there are a number of FIBRAs with varying degrees of retail exposure, FSHOP remains the only pure FIBRA play on the segment (Planigrupo, also 100% retail focused, is a C-Corp, not a FIBRA). This has significantly reduced property-specific risk, which at the outset was significant with Kukulkán and Puerto Paraíso. Moreover, it should give FSHOP a modicum of scarcity in a sector where choice is abundant and increase its relative attractiveness as a target or merger partner.

FSHOP has successfully diversified since its IPO... When FSHOP was put together in 2013, there was a great deal of skepticism that a small, regional, and highly-concentrated portfolio stitched together by three sponsors who knew little of one another would be able to compete effectively. In the event, FSHOP has managed to increase its portfolio from 14 properties in 12 states at its IPO to 18 in 12 states today (with the largest property representing 14% and 17% of GLA and NOI).

...delivering operational results in spite of significant early skepticism. This footprint expansion compounded by record occupancies (96% in 1H19) and above-inflation rental growth (5% over since 2013) has driven revenue, NOI, and EBITDA growth since of 29%, 31%, and 31%, respectively, since 2013. This performance suggests that FSHOP, from an operating standpoint, has proven its skeptics wrong.

Recent balance sheet de-risking is positive....FSHOP issued P$2.4 billion in new debt securities in June, extending maturities and, at the margin, reducing its cost of financing. It has similarly entered into derivative contracts to fix the variable portion of its new debt, enhancing the visibility of its cash flows.

...as are recent adjustments to its distribution policy. Alongside the release of 4Q18 results in February 2019, FSHOP unveiled a new distribution policy that reduces the payout from the current 100% of FFO to one that establishes a yearly floor of P$0.80/CBFI. This is intended to allow FSHOP to direct resources towards 1) the establishment of a P$55 million capex reserve; ii) a portfolio-wide renewable energy project; and iii) a strategic capex reserve for expansions or greenfield developments. This is closer to best-practices among developed market peers and should be seen positively.

Investment case: Negatives & Risks...

Tough neighborhood in a tough neighborhood. The valuation of retail assets around the world has been under significant pressure over the past several years as the reality and fears of the long-term impact of e-commerce on the sector sink in. Though not all properties are equally vulnerable and, arguably, many of those in Latin America are developed precisely in the mould of the assets best-suited to fend off the e-commerce onslaught in developed markets, there is a risk that B and C class properties end up trading at the high cap rates now seen in the US for this type of asset. Some of FSHOP's properties are what we would consider A-type assets, but many are either B in quality or are the top properties in what might be considered B or C class markets. Compared to FUNO's or Danhos's retail portfolios, for instance, FSHOP's is significantly more exposed to secondary cities.

Running to stand still....working for its creditors. Because FSHOP was caught wrong-footed when Banxico began tightening after Trump's election in November 2016, most of the improvement in operating metrics over the past three years has been consumed by higher financing costs. To illustrate the reach of this, FSHOP is no longer cancelling newly re-purchased CBFIs in order to use their distributions to service the debt associated with their purchase, altogether defeating the purpose, in our opinion, of the repurchase. As a result, the growth in the size of the portfolio; its greater diversification; the expansion in operating profitability; the partial internalization completed in 2018 at what we saw as favorable financial terms for FSHOP; and CBFI buybacks have, from a stock-performance standpoint, been for naught since during that time-frame FSHOP has delivered the poorest stock returns among the stocks under coverage. This has placed it in a troubling spiral of de-rating and reduction in stock liquidity that has in turn let to further de-rating and additional losses in liquidity.

Leverage levels among highest in peer group... And though on their own and at the time many of the capital allocation decisions taken by FSHOP seemed reasonable (buying back shares at a steep discount to NAV; re-purchasing roughly half of its manager; acquiring *La Victoria* in Querétaro, which is now one of its trophy assets and established a partnership with Abilia, one of Mexico's leading developers; deploying cash towards expansions; and dipping their toes into development partnerships), the fact is that they took resources away from debt reduction, which in hindsight would have been the wiser use of capital. The end result is that FSHOP now has a reported 42% LTV (43% if adjusted pro-forma for the pending payment on *La Victoria*), which is the highest among all FIBRAs under coverage and not far from the 50% regulatory limit, which is too high for comfort at a moment when the macro situation is wobbly and the continued health of the consumer a question.

...putting distributions at risk... With M&A seemingly off the table, a capital raising unlikely at current valuations (and, even if pursued, difficult to accomplish given the recent stock performance), and market conditions likely not ideal for retail asset sales, it would seem the only option for leverage reduction is cutting distributions. FSHOP has already taken the first step in this direction by announcing earlier this year that it will no longer pay out 100% of FFO and, instead, committing to a minimum payment of P$0.80/CBFI (equivalent to 78% of 2018's distributions and to 80% of 2019E FFO). But the savings from this measure will be directed at capex reserve, renewable energy investments, and strategic expansions, also all worthy calls on cash flow in their own right. But in the end, if FSHOP is really to reach the 35% LTV that most MXN-earning FIBRAs think is the right leverage target, we believe that FSHOP must begin soon to direct more of its cash flows towards a gradual reduction in debt, which will require, in our view, further curtailments of distribution. As an illustration, if we leave the FFO payout intact at 80% for 2019 and 2020, a reduction in the payout to 35% in 2021, 2022, and 2023 will be needed to reach 35% LTV in a five-year time frame.

Higher cyclicality, tough neighborhood, low (and declining) liquidity, high leverage, at-risk-dividend, and off-the-M&A radar screen. We won't repeat these risks since they are all addressed above, but suffice it to say that it all makes for a

difficult equity investment case at the moment. This is particularly so if management has taken the possibility of selling itself or of merging off the table. And, though the stock's free float is 82%, the sponsorship group owns enough to block an unsolicited approach or minorities from requesting a sale, highlighting perhaps the most unsavory aspect of the governance shortcomings of the externally-managed arrangements now prevalent in Mexico's FIBRA universe.

Valuation, price target, and recommendation

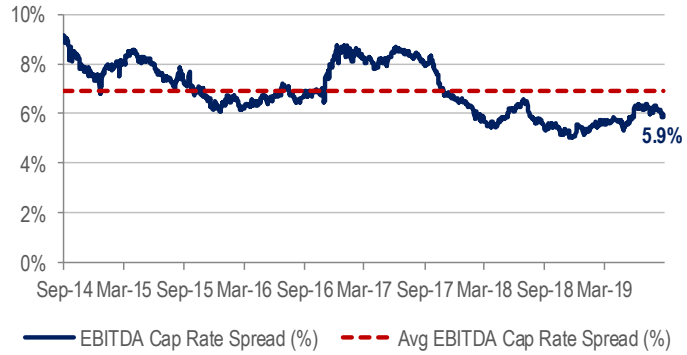
Valuation: On most current metrics, FSHOP stands out as being outrageously cheap: P/NAV of 0.40 and 2019E implied EBITDA cap rate of 8.7% and dividend yield of 10.3%. To downgrade a stock with these valuations would seem unusual, to say the least. However, as we argue in the risks section above, in spite of all of this, FSHOP shares have entered a downward dynamic that attractive valuation seems insufficient to reverse. Moreover, addressing these issues, which arguably all make themselves evident in rising leverage, may require a gradual capitalization via greater retention that would, at least temporarily, weaken the valuation argument on the dividend yield front.

Table 19: Fibra Shop – Key Metrics

	2018	2019E	2020E	2021E	2022E	2023E
Key metrics						
Average GLA (sq m)	502,727	507,094	508,803	537,653	537,458	537,653
Rental revenue/ share (P$)	2.38	2.56	2.68	2.79	2.91	3.02
NOI (P$m)	1,060	1,137	1,188	1,245	1,303	1,355
EBITDA (P$m)	1,007	1,080	1,129	1,182	1,236	1,286
FFO/ share (P$)	1.04	1.00	0.79	0.88	1.00	1.12
EPS (P$)	1.04	1.00	0.79	0.88	1.00	1.12
Expected pre-tax DPS (P$)	1.09	0.86	0.68	0.70	0.80	0.90
NAV/BVPS (P$)	21.28	21.15	21.25	21.87	21.87	21.87
Net LTV (%)	39%	39%	42%	40%	40%	35%
Valuation						
Price/CBFI (P$)	8.4					
# of CBFIs outstanding (m)	501	503	503	503	503	503
Market cap (US$m)	221	221	221	221	221	221
Market cap (P$m)	4,192	4,208	4,208	4,208	4,208	4,208
Average net debt (P$m)	6,901	8,093	8,475	8,458	8,513	8,408
Other adjustments (P$m)	136.1	146.5	153.2	159.4	165.8	172.5
Enterprise value (P$m)	**11,229**	**12,447**	**12,836**	**12,826**	**12,887**	**12,789**
Multiples						
EV/GLA (US$)	1,176	1,292	1,328	1,256	1,262	1,252
Implied NOI cap rate (%)	9.4%	9.1%	9.3%	9.7%	10.1%	10.6%
Implied EBITDA cap rate (%)	9.0%	8.7%	8.8%	9.2%	9.6%	10.1%
Rental revenue yield (%)	10.6%	10.3%	10.5%	10.9%	11.3%	11.9%
FFO yield (%)	12.5%	12.0%	9.4%	10.5%	12.0%	13.4%
Total dividend yield, pre-tax (%)	13.0%	10.3%	8.1%	8.4%	9.5%	10.7%
Earnings yield (%)	12.5%	12.0%	9.4%	10.5%	12.0%	13.4%
P/NAV (Book Value) (x)	0.39	0.40	0.39	0.38	0.38	0.38
LTV (%)	39%	39%	42%	40%	40%	35%

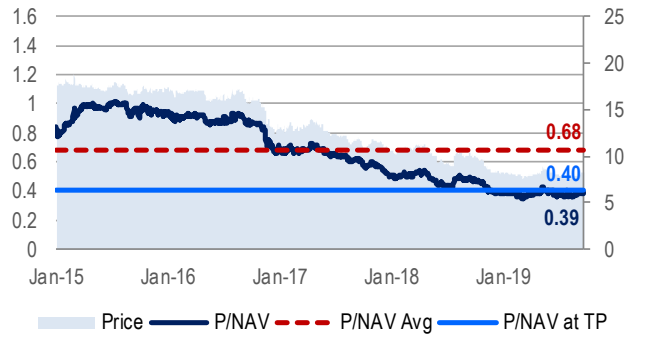
Source: Company Data, BTG Pactual estimates

Chart 103: FSHOP 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 104: FSHOP Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price target: Taking this into account, in setting our price target we have assumed in our DDM a temporary reduction in the payout to produce a gradual recapitalization to an LTV of 35% by the time we enter the terminal value phase in 2023 (which is consistent with what we do for all FIBRAs under coverage). This, plus a higher cost of equity assumption to 11.5% reflecting a higher observed beta (which makes sense fundamentally given its higher cyclical exposure and lower stock liquidity), has led us to slash our PT from P$16/CBFI (which, admittedly, had not been updated for some time) to P$8.5/CBFI. This results in a 12-month projected total return of 12% and in implied 2020E implied EBITDA cap rate of 8.7% and dividend yield of 8.0%.

Table 20: Fibra Shop – DDM Valuation Summary

Assumptions	
Stage 1: 2019E-2023E	
2023 AFFO (P$m)	563
Payout Ratio (%)	30%
2023 Dividends (P$m)	151
2023 Return on Capital (P$m)	18
Stage 2: 2024-2028	
Inflation (%)	3.5%
Leasing Spreads (%)	0.0%
Growth(%)	3.5%
Payout Ratio (%)	100%
Stage 3: 2029-2038	
Inflation (%)	3.5%
Leasing Spreads (%)	0.0%
Growth(%)	3.5%
Payout Ratio (%)	100%
Stage 4: Terminal Value	
Inflation (%)	3.5%
Terminal Leasing Spreads (%)	0.0%
Terminal Nominal Growth Rate(%)	3.5%
Perpetuity Dividends (P$m)	11,798

Cost of Equity Calculation	
Risk free rate, M10 (%)	7.0%
ERP (%)	5.0%
Beta	0.90
Cost of equity (%)	11.5%

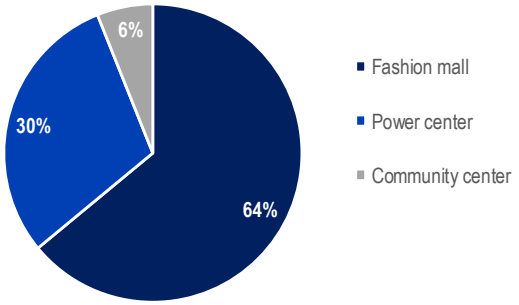
Valuation	
PV of future dividends (stage 1-stage3) (P$m)	3,681
PV of future dividends in perpetuity (P$m)	1,338
PV of future dividends (P$m)	5,018
DDM value/CBFI (P$)	10.5
DDM value/CBFI after-tax (P$)	**8.2**
Value/share after-tax @ YE 2019 (P$)	**0.3**
Total value/share after-tax (P$)	**8.5**
2019E Pro-forma official price target (P$)	**8.5**
12M Dividend Yield	10.3%
Upside/downside including dividends (%)	11.9%

Source: Company Data, BTG Pactual estimates

Downgrading to Neutral: While we recognize that our PT formulation is punitive, we believe that it is the only way to capture both the downward stock liquidity spiral the stock is on and the gradual recapitalization of the balance sheet that we believe will be required. With a total return to our PT of 12%, FSHOP's upside is at the lower end of our coverage range, leading us to downgrade an admittedly cheap stock to Neutral.

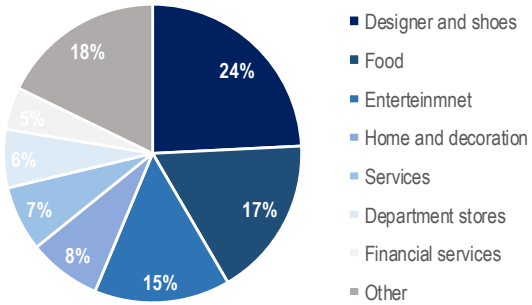
Fibra Shop – Company Description

Chart 105: Breakdown per type of mall (as % of revenues)



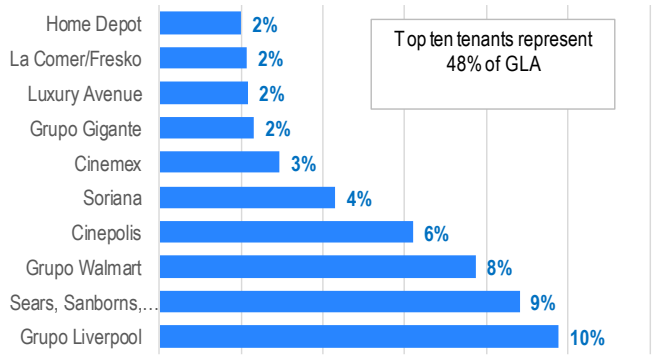
Source: Company Data, BTG Pactual Research

Chart 106: Tenants industry (as % of revenues)



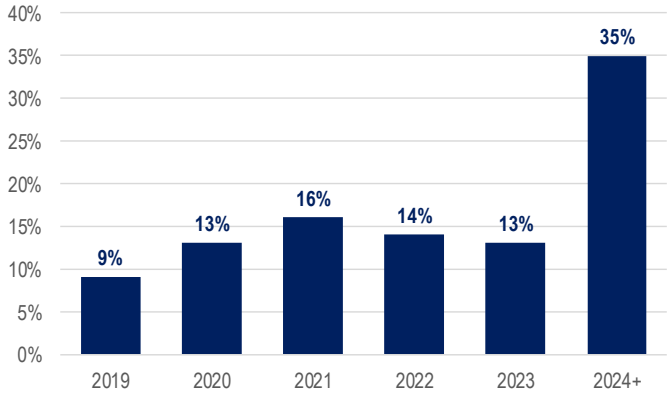
Source: Company Data, BTG Pactual Research

Chart 107: Top tenants (as % of GLA)



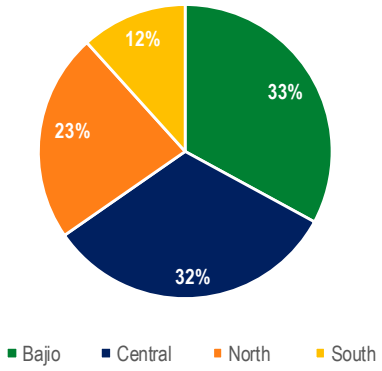
Source: Company Data, BTG Pactual Research

Chart 108: Contract expiration per year (as % of GLA)



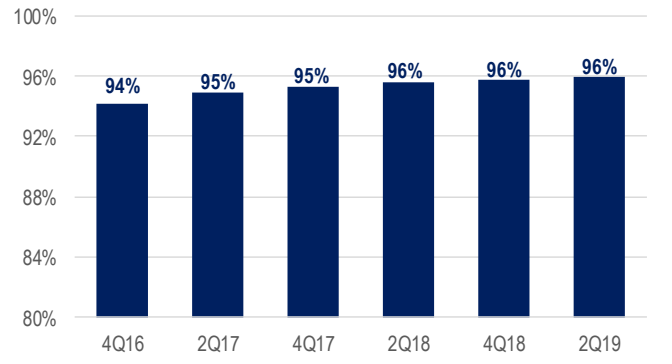
Source: Company Data, BTG Pactual Research

Chart 109: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

Chart 110: Historical Occupancy (%)



Source: Company Data, BTG Pactual Research

Planigrupo (Neutral): The mass market play...

The only retail play that caters fully to Mexico's mass market

Though several retail options exist, most listed portfolios service the A and B income segments. Plani, by contrast, is focused on serving the B, C, and D demographics, the bulk of Mexico's consumers. This not only means that its core market is the largest, it also renders it more defensive both to cyclical factors and the threat of e-commerce. Moreover, with 35 properties and over 800K sqm of GLA, Plani is a top 5 retail property player nationally and, present in 18 states, it is among the most geographically diversified.

Plani is a C-Corp with almost half-a-century of experience

In contrast to its FIBRA peers, the C-Corp structure provides Plani with greater financial and investment flexibility, cleaner governance, superior alignment with minorities, economies of scale, and internalization of development returns. Moreover, unlike FIBRAs, which have existed in their present form since 2011, Plani has been developing and managing retail real estate since 1975, making it the most experienced among its peers.

Key risk: global retail de-rating and stock liquidity

Following its cashless IPO in 2017, Plani was unsuccessful in its attempt to execute on a follow-on transaction, resulting in minimal stock liquidity. Until said offering occurs, liquidity is unlikely to improve in any material way. This likely exacerbates Plani's other main risk: the spillover from the global de-rating in cap rates for B and C assets. However, the e-commerce risk that is driving the de-rating in mature markets is of a very different nature in Mexico, where arguably the lower the income segment the greater the obstacles to e-commerce penetration. Please see Appendix 2 for data on the de-rating from US peers in two different retail segments (high-end shopping mall and neighborhood center).

Initiating Plani with a Neutral rating and P$21.5/share price target

There are many things we like about Plani: its management's track-record in a number of challenging periods, corporate structure, institutional ownership, diversification, and focus. However, its low levels of liquidity and valuation that seems fair in the context of comps, leads us to initiate with a Neutral rating that is validated by our DDM/Exit cap rate-driven PT of P$21.5/share, implying upside of 13%.

Investment case: The Positives....

The mass market and defensive play... Among listed peers, Plani is the only retail platform that offers exposure to Mexico's C, D+, and D demographics (according to the income ranking by AMAI), which constitutes 73% of Mexico's consumers and 30% of aggregate purchasing power. This, in our view, renders it more defensive to both a potential cyclical downturn and also to the longer term risks from e-commerce (particularly considering that over three-quarters of Plani's tenants sales are reportedly in the form of cash or debit cards, which says a lot about their end-client).

...via a diversified portfolio by asset, geography, and tenant... Plani's 35 properties spread over 18 states (out of 32 in Mexico) arguably renders it the only national player among listed retail property vehicles. No asset represents more than 7.5% of rents as of 1H19, while its largest exposure by state is to Nuevo León with 20%, which, as home to vibrant Monterrey, is a good thing. As for tenants, Walmex in all its formats is the largest with almost 30% of GLA (though it represents a much lower share of rents), followed by HEB from Texas with roughly 6%, and Home Depot, Cinemax and Cinépolis, each with 5%.

...that is delivering strong operational results. As of 1H19, Plani's occupancy rate is in excess of 94% and is 95% when considering only stabilized properties. On a LTM basis, Plani's traffic is 128 million, which is up 7% YoY and a touch above Mexico's population. In 2Q19, revenues rose 9% YoY to P$399 million, well above inflation, while NOI and EBITDA rose by 11% and 13% to P$321 million and P$261 million, respectively. This is a result of NOI and EBITDA margin expansion YoY of 110bps to 81.2% and 190bps to 66.1%, which compares to its 2016 NOI and EBITDA margins of 79.9% and 60.3%. The 600bps expansion in EBITDA margin underscores the economies of scale of being a fully internalized and integrated C-Corp, which is in sharp contrast to the performance of its retail FIBRA comps. Moreover while EBITDA margins compare favorably to Mexican comps, Plani's remain ~500 bps below its Brazilian peers, underscoring the potential upside should the asset base continue to grow.

Not a FIBRA...and lots of history... The FIBRA structure, for all its virtues, has a number of shortcomings from the governance/alignment of interests standpoint that have become all too familiar. We will not delve into them now, but suffice it to say that Plani, as a C-Corp, avoids most of them. Its property and platform management is internalized, it has greater flexibility from balance sheet and capital allocation standpoints (e.g., it is not subject to the 50% LTV regulatory maximum and can choose to distribute or retain cash flows), and a natural alignment of interests between management, controllers, and minorities.

Eduardo Bross, Plani's Chairman, founded the company in 1975, developing initially for clients and eventually for themselves; its CEO, Elliott Bross, has been employed at Plani since 1997 and navigated its evolution from a regional, family company to one with a national presence and institutional ownership. In total, Plani has developed close to 70 properties with GLA of over 1m sqm. In addition, it has acquired a total of 15 properties, most of them in the past 10 years. Moreover, it has raised private equity, a CKD (a private-equity instrument designed for Afores), and public equity.

And, in the over 40 years it has been operating, it has dealt with a number of financial crises (1976, 1982, 1987, 1995, and 2009) and dealt with a handful of recessions (1982-1983, 1986, 1995, 2001, and 2009), including four in which GDP contracted in excess of 4%. This is all to say that Plani is arguably the most experienced and tested developer and manager of retail assets in Mexico.

Institutional shareholder base feeds into strength of governance. Plani is controlled jointly by Southern Cross (55% of equity) and the Bross Family (16%), who founded the company in 1975 and has managed it continuously since. The float (29%) is in the hands of Afores that chose to swap their stake in Plani's CKD for common equity in a cashless IPO that took place in 2017. Southern Cross bought its stake in Plani in 2012, which was followed by the CKD placement, transforming Plani from a family company into one that is owned and managed institutionally with all of the governance implications that this entails.

Fully integrated platform internalizes development and enhances returns. Plani is fully integrated, engaged in development, design, construction, and asset management. Its proprietary approach to origination, underwriting, structuring, due diligence, and closing involves disciplined investment committees and vetting processes. This all delivers lower development costs, greater synergies across the chain, and, ultimately, higher returns. Similarly, it allows for Plani and its shareholders to benefit fully from the scale effects of adding assets to its platform, in contrast to FIBRAs that pay fees on the basis of asset size.

Investment case: Negatives & Risks...

Low stock-liquidity. The unsuccessful follow-on in 2017 has limited the float to the share of the company that Afores took in exchange for their stake in Plani's CKD, which has driven stock liquidity to a minimum. Until Plani is able to conduct this follow-on, which given the turn in Mexico's macro environment seems both less pressing and less likely, stock liquidity is likely to remain minimal.

Global real estate de-rating... In mature markets, retail real estate valuations have taken a significant hit largely due to concerns about the long-term impact of e-commerce. In the US, this has been particularly notable in B and C class properties, where cap rates have moved into the double digits in some markets. While the reality of the e-commerce threat in Mexico is not only less pressing but also differentiated on the income scale, the fact is that it is real, it will drive investment decisions, and will sooner or later make itself present.

E-commerce... Needless to say, this is a fundamental threat that recent data from Mexico suggests that it is growing rapidly. That said, Mexico's retail portfolios were designed from the outset as destination malls with entertainment at the core, which is exactly how mature markets are reacting to the e-commerce threat. Moreover, in sharp contrast to the US and other mature markets, the income demographic that would seem less immediately vulnerable to e-commerce are the lower income segments, which are Plani's bread and butter. *Please see Appendix 1 for more data on e-commerce trends in Mexico.*

Real estate is cyclical, so the economy matters. While retail sales have for the most part remained strong, real estate, particularly portfolios with exposure to the consumer cycle, are subject to macro performance and overall economic conditions. The consumer space has been the stellar performer in a sluggish economy, but there are questions around how much longer this can persist if overall economic performance is disappointing.

How Plani unwinds its CKD is still not clear. Plani has been a pioneer in how it has been able to finance its real estate investments. This has included the structuring of a CKD (a listed private equity vehicle that Afores can invest in), which has reached its maturity and that Plani has been looking to wind down. Its cashless IPO, in which some Afores swapped their stakes in the CKD for equity at the Plani level, addressed this to a large degree, enabling Plani to consolidate the CKD and take out the majority of its investors. However, a couple of Afores have so far opted to remain invested in the CKD, which has left a large minority stake at the Plani level and has left the question of the final wind-down of the CKD open. How this is ultimately addressed might imply future dilution, the sale of the CKD portfolio altogether, or additional capital deployed by Plani.

Is the balance sheet a constraint to growth? As of 1H19, Plani's LTV was 42%, close the FIBRAS's 50% regulatory level. Because Plani is a C-Corp and therefore not subject to such regulations, leverage levels are less relevant, but 6.0 times net debt/EBIDA might be seen as elevated.

Pipeline risk: diversification into offices and hotels... Plani has begun to consider diversifying into office and hotel properties. This is at this point limited to mixed-use properties and a good portion of the development activity is as a seller of property. However, the natural evolution is to seek to develop said properties for income, which in our view would change the company's risk profile.

Valuation, price target, and recommendation

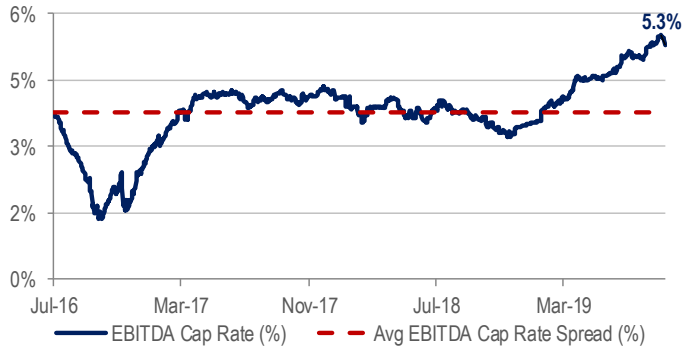
Valuation: On most current metrics, Plani screens as fairly valued This is partly explained by its C-Corp status, which we believe better aligns management's and minority shareholders' interests. Moreover, its low liquidity, which in normal circumstances would work against valuations, helps it this time since, by being very closely held, it has avoided much of the volatility that has plagued its peers in the past (though this works against it during rallies, as we have seen this year). Plani trades on a P/NAV of 1.1x and 2019E implied EBITDA cap rate of 8.3%.

Table 21: Planigrupo – Key Metrics

	2018	2019E	2020E	2021E	2022E	2023E
Key metrics - Proportional (Adj.)						
GLA EoP (sq m)	751,943	751,943	754,443	759,443	784,443	809,443
Adj. Rental Revenue (P$m)	1,458	1,548	1,611	1,714	1,838	1,970
Adj. Total Revenue (P$m)	1,473	1,573	1,636	1,741	1,868	2,002
Adj. NOI (P$m)	1,185	1,276	1,327	1,416	1,519	1,632
Adj. EBITDA (P$m)	945	1,027	1,084	1,167	1,261	1,363
Margins						
Adj. NOI Margin (%)	80.5%	81.1%	81.1%	81.3%	81.3%	81.5%
Adj. EBITDA Margin (%)	64.1%	65.3%	66.3%	67.0%	67.5%	68.1%
FFO Margin (%)	14.9%	19.4%	16.8%	19.4%	21.8%	23.9%
AFFO Margin (%)	11.3%	17.2%	14.6%	16.6%	19.0%	21.1%
Key metrics						
FFO (P$) - BTG	220	305	275	337	407	478
AFFO (P$) - BTG	166	270	239	288	355	422
Net Income (P$)	164	293	271	324	385	442
Dividend (P$)	0	0	25	30	35	41
NAV(P$)	5,034	5,333	5,215	5,277	5,333	5,333
Avg. # of shares outstanding (m)	318	318	318	318	318	318
Valuation						
Price per share						
# of shares	318	318	318	318	318	318
Equity Value (P$m)	6,039	6,039	6,039	6,039	6,039	6,039
Average net debt (P$m)	6,493	6,309	6,126	5,944	6,275	6,558
Enterprise value (P$m)	12,532	12,348	12,164	11,983	12,314	12,597
(-) Net Deferred Taxes (Liability) Asset	-330	-328	-352	-355	-358	-358
(-) Restricted Cash	119	121	121	121	121	121
(-) VAT Reimbursables	233	237	246	246	246	246
(-) Land Reserve/WIP	0.0	0.0	0.0	0.0	0.0	0.0
Adj. Enterprise value (P$m)	12,511	12,319	12,150	11,971	12,305	12,588
Multiples						
EV/GLA (US$)	871	850	836	818	814	807
Implied NOI cap rate (%)	9.5%	10.4%	10.9%	11.8%	12.3%	13.0%
Implied EV/EBITDA (x)	13.2	12.0	11.2	10.3	9.8	9.2
Implied EBITDA cap rate (%)	7.5%	8.3%	8.9%	9.7%	10.2%	10.8%
Rental revenue yield (%)	11.0%	11.9%	12.6%	13.6%	14.2%	14.9%
FFO yield (%)	3.6%	5.0%	4.6%	5.6%	6.7%	7.9%
P/FFO (x)	27.4	19.8	22.0	17.9	14.8	12.6
Dividend yield (%)	0.0%	0.0%	0.4%	0.5%	0.6%	0.7%
Earnings yield (%)	2.7%	4.9%	4.5%	5.4%	6.4%	7.3%
P/NAV (Book Value) (x)	1.20	1.13	1.16	1.14	1.13	1.13

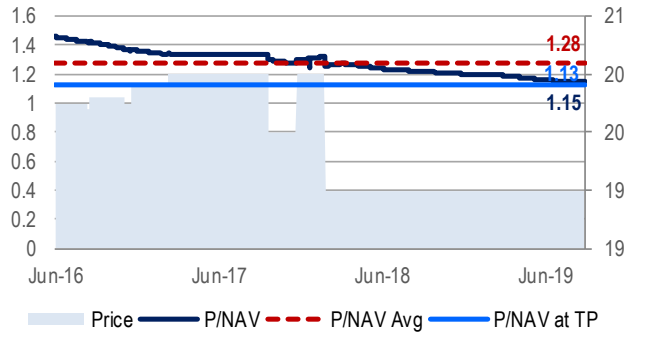
Source: Company Data, BTG Pactual Estimates

Chart 111: Planigrupo 12MF EBITDA Cap Rate Spread (%)



Source: Company Data, Bloomberg, BTG Pactual

Chart 112: Planigrupo Historical NAV (x)



Source: Company Data, Bloomberg, BTG Pactual

Price target: Our blended DDM and Exit cap rate-driven price target of P$21.5/share implies an expected 13% total return over the next 12 months and translates into 2020E implied EBITDA cap rate and P/NAV of 8.4% and 1.3x. We use a MXN COE of 10.8% and an exit NOI cap rate in 2025 of 8.5%.

Table 22: DCF + Exit Cap Rate Valuation Summary

DCF valuation (P$m):	
PV of CFs through 2024	2,710
PV of Terminal Value	12,075
Terminal growth rate (%)	3.5%
PV of cash flows	**14,784**
Less current net debt	5,982
Fair equity value	**8,802**
(+) VAT and restricted cash	366
(+) Net Investments (Tijuana)	725
(+) Net Deferred Taxes - Asset (Liability)	(358)
(+) Land Bank Available for Sale	-
(-) Net Assets attributable to holders and settlors	1,128
Fair equity value	**8,407**
# of shares (m)	318
Per Share (P$)	**26.5**

Exit cap rate analysis (P$m)	
2025E Proportional NOI	1,416
Exit Cap Rate (%)	8.5%
2025E Real Estate EV	16,665
(+) 2025E Land Reserve	-
(=) 2025E EV	16,665
(-) 2025E Net Debt	6,109
(=) 2025E Equity Value	10,556
(+) 2025E VAT + Restricted Cash	-
(+) 2025E Net Investments	-
(+) 2025E Net Deferred Taxes	-
(+) 2025E Land Bank Available for Sale	-
(-) Net Assets attributable to holders and settlors	1,128
(=) 2025E Equity Value	**9,428**

FCFE Valuation + Exit Cap Rate (P$m):	
PV of dividends through 2024	171
PV of Terminal Value	5,095
Fair equity value	**5,266**
Fair equity value	**5,266**
# of shares (m)	318
Per Share (P$)	**16.6**

WACC calculation (P$) (%):	
Normalized 10yr MBONO (%)	7.0%
Cost of debt (%):	8.0%
Plani Beta /1	1.0
LT leverage (%)	40.0%
Tax rate (%)	30.0%
Equity risk premium (%):	5.0%
Cost of equity (%):	12.5%
WACC (%):	**9.7%**

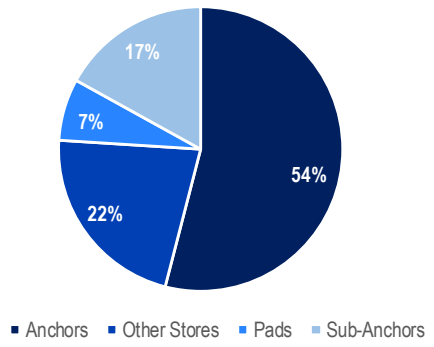
Blended Target (50% DCF + 50% Exit Cap), (P$/share)	21.5

Source: Company data, BTG Pactual estimates

Recommendation: There are many things we like about Plani: its management's track-record in a number of challenging periods, corporate structure, ownership, diversification, and focus. However, its low levels of liquidity and valuation that seems fair in the context of comps, leads us to initiate with a Neutral rating that is validated by our DDM/Exit cap rate-driven PT of P$21.5/share, implying upside of 13%.

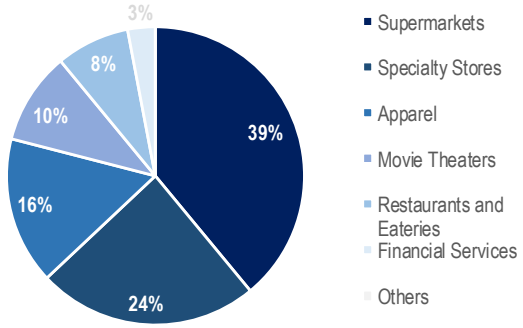
Planigrupo – Business Description

Chart 113: GLA breakdown by type of store



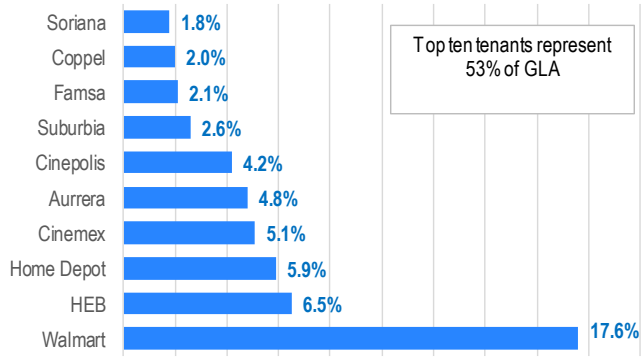
Source: Company Data, BTG Pactual Research

Chart 114: Tenants Industry Breakdown (as% of GLA)



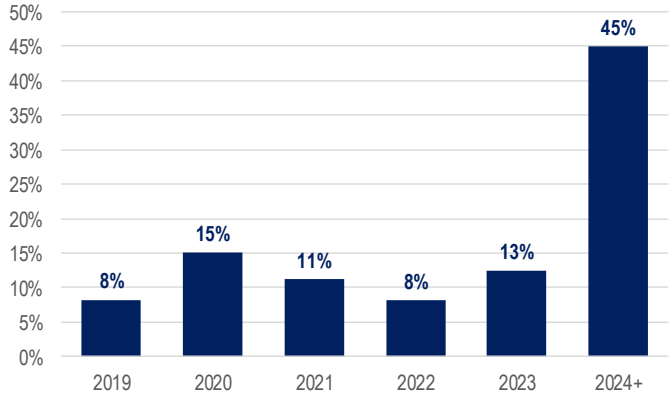
Source: Company Data, BTG Pactual Research

Chart 115: Top tenants (as % of GLA)



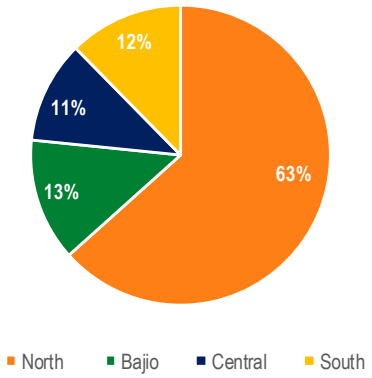
Source: Company Data, BTG Pactual Research

Chart 116: Contract expiration per year (as % of GLA)



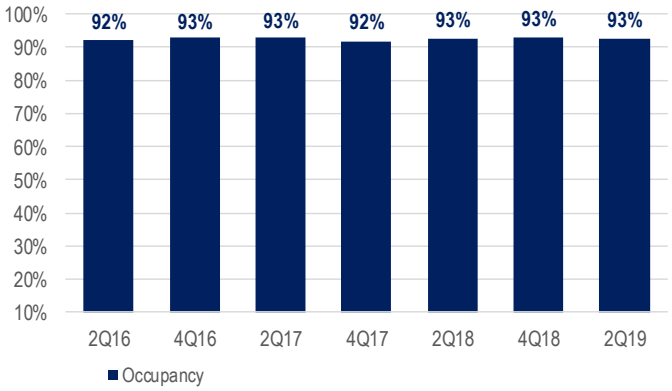
Source: Company Data, BTG Pactual Research

Chart 117: Geographic breakdown (as % of GLA)



Source: Company Data, BTG Pactual Research

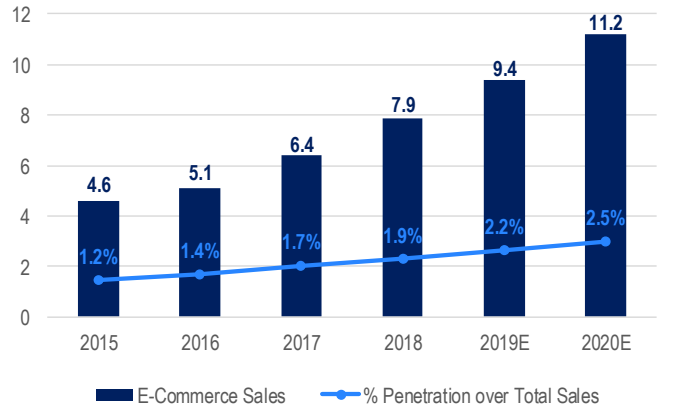
Chart 118: Occupancy evolution (%)



Source: Company Data, BTG Pactual Research

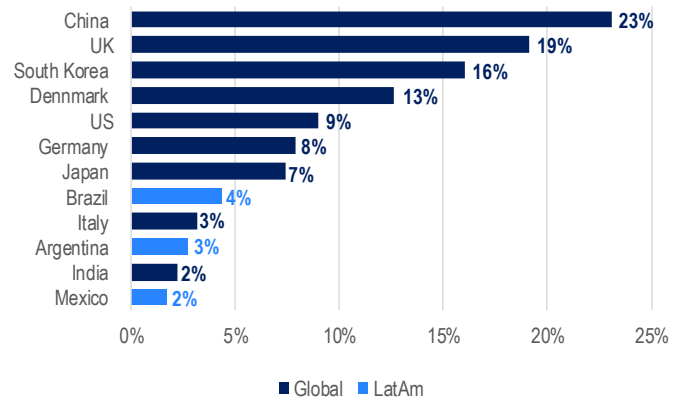
Appendix 1: E-Commerce in Mexico

Chart 119: While online shopping is growing in Mexico…
E-Commerce sales (US$bn) and penetration



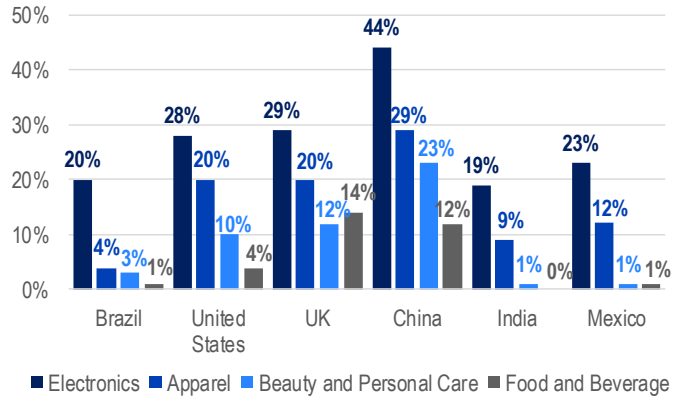
Source: eMerketer, BTG Pactual Research

Chart 120: … it remains low as a share of total retail sales…
E-Commerce penetration of total sales



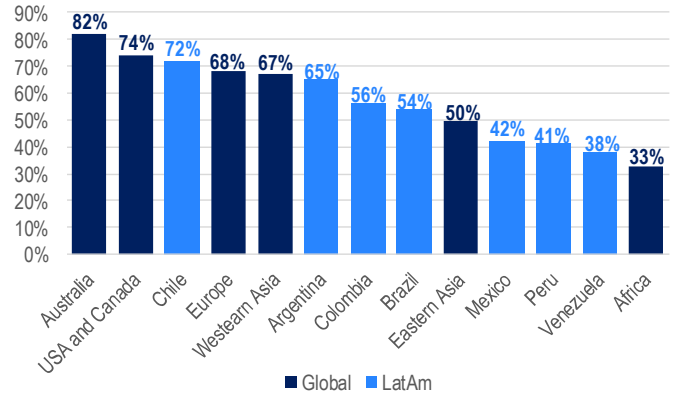
Source: Euromonitor, BTG Pactual Research

Chart 121: E-Commerce Penetration by Category as % of Total Sales



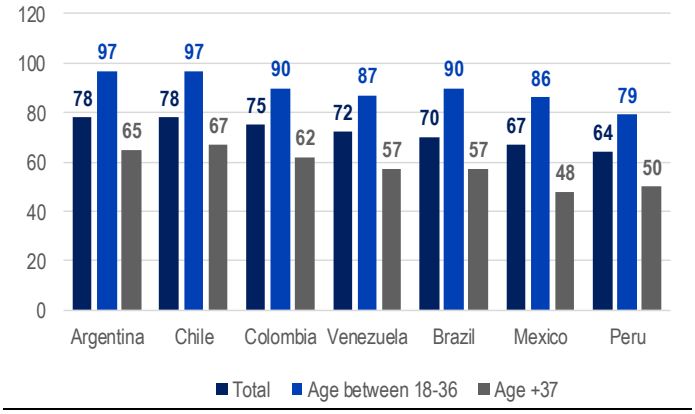
Source: Euromonitor, BTG Pactual Research

Chart 122: Percentage of adults who own a smartphone



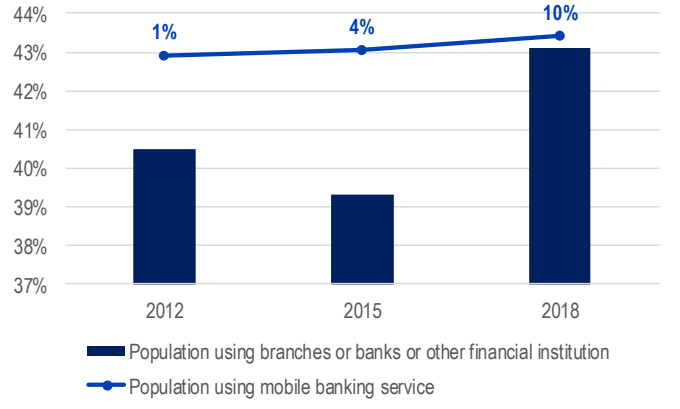
Source: Pew Research Center, BTG Pactual Research

Chart 123: Adults who use the internet at least occasionally or report owning a smartphone



Source: Pew Research Center, BTG Pactual Research

Chart 124: Population using branches or banks (% of the population)



Source: INEGI, ENIF, BTG Pactual Research

Appendix 2: De-rating of global retail

High-end shopping malls

Table 23: Simon Properties cap rate vs US Treasury Yield (%)

Notes: High-end malls and outlet centers. Source: Bloomberg, BTG Pactual Research.

Table 24: Taubman Centers vs US Treasury Yield (%)

Notes: High-end shopping malls. Source: Bloomberg, BTG Pactual Research

Grocery Anchored Community Shopping Centers

Table 25: Brixmor Property Group cap rate vs US Treasury Yield (%)

Source: Grocery anchored Community and Neighborhood shopping centers. Source: Bloomberg, BTG Pactual Research

Table 26: Regency Centers cap rate vs US Treasury Yield (%)

Source: Power and community centers. Source: Bloomberg, BTG Pactual Research

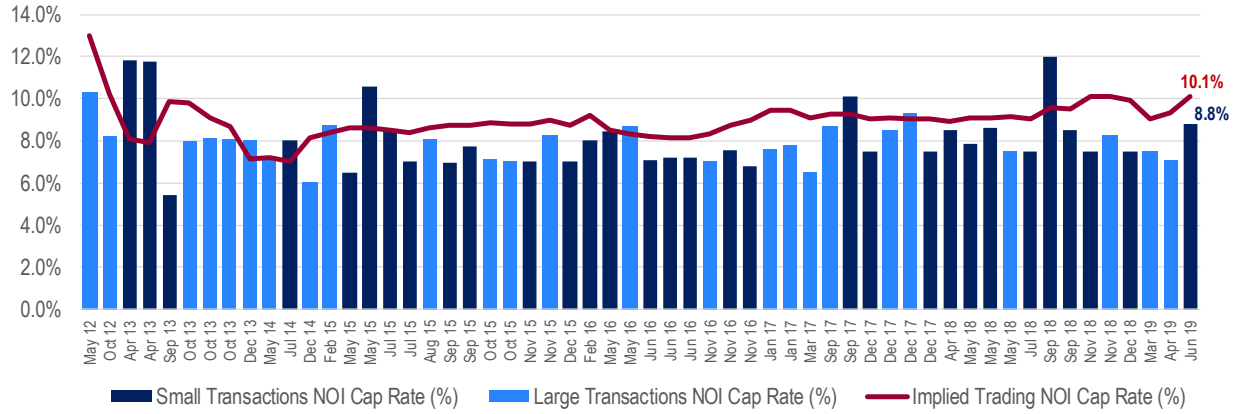
Appendix 3: Industrial Sector – Precedent transactions

Table 27: Industrial - Historical Transactions

	Buyer	Transaction Date	Region	GLA (sqf)	Occupancy (%)	# of properties	Transaction Value (US$m)	USD NOI Cap Rate (%)	Implied Trading NOI Cap Rate (%)
Fibra MQ Initial Portfolio	Fibra MQ	Oct 12	North	26,909,750	91.1%	245	1,459	8.2%	10.2%
PACE Industries	Fibra Uno	Apr 13	North	462,848	-	2	18	11.8%	8.1%
Tepotzotlan I	Fibra Uno	Apr 13	Central	705,035	92%	1	27	11.8%	7.9%
Cancun ER - Industrial	Fibra Uno	Sep 13	South	193,750	n.a.	1	14	5.4%	9.9%
Al-Kimco	Terrafina	Oct 13	North	11,000,000	92%	84	604	7.9%	9.8%
DCT Industrial Properties	Fibra MQ	Oct 13	Mixed	1,652,851	100%	15	86	8.1%	9.1%
Maine Portfolio (Hines)	Fibra Uno	Oct 13	Bajio	1,284,392	100%	5	87	8.1%	8.7%
Vermont Portfolio	Fibra Uno	Dec 13	North	5,597,228	97%	34	372	8.0%	7.2%
California Portfolio (Grupo GP / Clariond)	Fibra Uno	May 14	North	3,719,401	91%	29	275	7.2%	7.2%
Industrial Property	Fibra Prologis	Jul 14	Bajio	57,064	na	1	3	8.0%	7.0%
Class-A Logistics Portfolio	Fibra Prologis	Dec 14	Central	1,558,500	na	6	110	6.0%	8.1%
Ridge Property Trust II	Fibra MQ	Feb 15	North	637,223	100%	2	59	8.8%	8.4%
Class-A Logistics Facility	Fibra Prologis	May 15	Bajio	76,800	100%	1	5	6.5%	8.7%
Portafolio Casona	Fibra Monterrey	May 15	North	426,250	100%	5	18	10.6%	8.6%
Portfolio Nexxus	Fibra MQ	Jul 15	Bajio	438,091	100%	8	31	8.4%	8.5%
Catacha Industrial Building	Fibra Monterrey	Jul 15	North	62,431	100%	1	3	7.0%	8.4%
I0 Industrial Properties in the North	Fibra MQ	Aug 15	North	2,164,190	94%	10	108	8.1%	8.6%
Milwaukee Portfolio (Binding agreement)	Fibra Monterrey	Sep 15	Bajio	64,583	100%	1	5	7.0%	8.7%
Santiago	Fibra Monterrey	Sep 15	Bajio	177,572	100%	1	8	7.7%	8.7%
CuautiPark	Fibra Uno	Oct 15	Central	1,025,520	90%	1	48	7.1%	8.9%
Class A Logistics Portolio	Fibra Prologis	Oct 15	Central	796,000	100%	3	64	7.0%	8.8%
Rail-Served distribution facility	Fibra Prologis*	Nov 15	Central	1,093,000	100%	1	14	7.0%	8.8%
10 Properties	Terrafina	Nov 15	Mixed	1,100,000	96.3%	10	59	8.2%	9.0%
One single logistics building	Fibra Prologis	Dec 15	North	502,000	100%	1	38	7.0%	8.7%
Two Industrial Properties in Ciudad Juarez	Fibra MQ	Feb 16	North	379,966	na	2	22	8.0%	9.2%
Portfolio Nico 1	Fibra Monterrey	May 16	North	469,306	100%	1	27	8.4%	8.5%
Portafolio Providencia	Fibra Monterrey	May 16	North	1,072,214	100%	8	47	8.7%	8.3%
Logistics Building (El Salto, Guadalajara)	Fibra Prologis	Jun 16	Bajio	231,500	100%	1	17	7.1%	8.2%
Prologis Park Toluca	Fibra Prologis	Jun 16	Central	308,300	100%	1	21	7.2%	8.2%
Juarez Industrial Center	Fibra Prologis	Jun 16	North	210,200	92%	1	14	7.2%	8.2%
Logistics Building (Cuaututlan Izcalli)	Fibra Prologis	Nov 16	Central	616,800	100%	1	50	7.0%	8.3%
Catacha 2 (Industrial Development)	Fibra Monterrey	Nov 16	Bajio	58,125	100%	1	3	7.6%	8.8%
Two Class-A Logistics Buildings	Fibra Prologis	Nov 16	North	250,400	100%	2	16	6.8%	9.0%
Class A Industrial Portfolio	Terrafina	Jan 17	North	5,600,000	100%	45	381	7.6%	9.5%
Class A Industrial Portfolio	Terrafina	Jan 17	Bajio	725,000	96%	6	41	7.8%	9.5%
Frimax	Fibra Uno	Mar 17	Central	2,281,947	100%	1	104	6.5%	9.1%
Seven Industrial Properties	Terrafina	Sep 17	North	900,000	100%	7	53	8.7%	9.3%
Industrial Property	Terrafina	Sep 17	North	200,000	100%	1	6	10.1%	9.3%
Class A Facility in Prologis Park Toluca	Fibra Prologis	Dec 17	Central	143,400	100%	1	10	7.5%	9.1%
Class A Portfolio of 17 properties	Terrafina	Dec 17	North	2,700,000	100%	17	180	8.5%	9.1%
Industrial Portfolio in Tijuana	Vesta	Dec 17	North	1,300,000	100%	21	70	9.3%	9.0%
Class A Facility in Prologis Park Reynosa	Fibra Prologis	Dec 17	North	290,100	98%	1	18	7.5%	9.0%
2 Industrial properties (Class A)	Terrafina	Apr 18	North	330,000	100%	2	24	8.5%	8.9%
Portfolio Horizonte (Panamericana 1)	Fibra Monterrey	May 18	North	227,301	100%	1	7	7.9%	9.1%
Portfolio Horizonte (Panamericana 2)	Fibra Monterrey	May 18	North	254,738	100%	1	17	8.6%	9.1%
Sale of industrial Assets in the North	Fibra MQ	May 18	North	2,600,000	92%	37	87	7.5%	9.2%
Class-A Facility in Guadalajara	Fibra Prologis	Jul 18	Bajio	269,200	100%	1	14	7.5%	9.0%
BTS in Ciudad Juarez	Terrafina	Sep 18	North	265,000	100%	1	14	12.0%	9.5%
BTS in Santa Catarina, Nuevo León (Zinc)	Fibra MTY	Sep 18	North	206,667	100%	1	10	8.5%	9.5%
Prologis Park Los Altos and Apodaca	Fibra Prologis	Nov 18	Bajio/North	449,100	100%	2	32	7.5%	10.1%
Whirpool Complex in Apodaca	Fibra MTY	Nov 18	North	1,599,300	100%	1	135	8.2%	10.1%
Class-A Industrial building	Fibra Prologis	Dec 18	North	662,500	100%	1	35	7.5%	9.9%

Source: Company Data, BTG Pactual Estimates

Chart 125: Mexican real estate stocks have traded at discounts to the pricing of private market transactions
Precedent Transactions from listed players 12MF NOI Cap Rate (%) vs Trading 12MF NOI Cap Rate (%)



Source: Company Data, BTG Pactual Estimates
Notes: Includes precedent transactions for large portfolios (>US$30m) and small portfolios in the industrial space for Fibra Uno, Terrafina, Fibra Macquarie, Fibra Prologis and Fibra Monterrey. Implied NOI Cap Rate is calculated as the aggregate cap rate for all of these players.

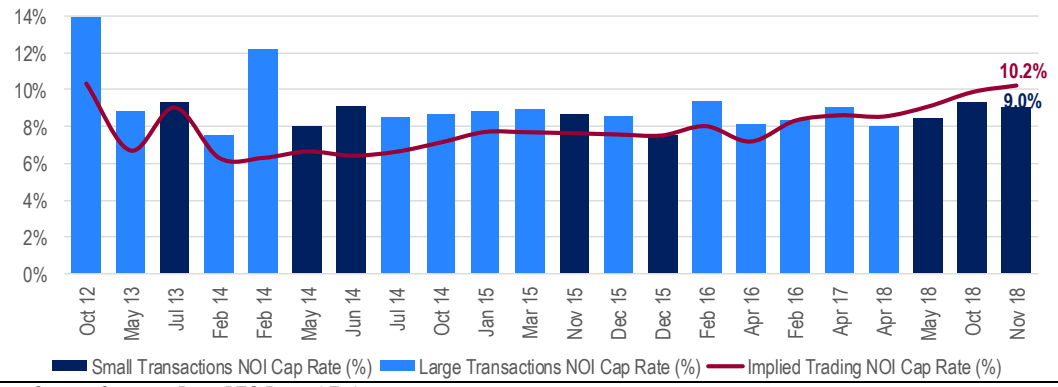
Appendix 4: Office Sector – Precedent transactions

Table 28: Historical transactions

Portfolio/Property	Buyer	Transaction Date	Location	GLA (m2)	Occupancy (%)	# of properties	Transaction Value (US$m)	NOI Cap Rate (%)	Implied Trading NOI Cap Rate (%)
Torre Mayor	Funo	Oct 12	Reforma	84,000	98%	3	175	9.0%	10.3%
Torre Diana	Funo	May 13	Reforma	63,000	NA	1	165	8.8%	6.7%
Grupo Posadas Office	Funo	Jul 13	Reforma	4,815	NA	1	15	9.3%	9.0%
P8	Funo	Feb 14	Mixed (Mx City)	80,000	94%	8	182	7.6%	6.3%
Colorado (Centro Bancomer)	Funo	Feb 14	Insurgentes	101,000	100%	1	160	12.2%	6.3%
Polanco (Mariano Escobedo)	Funo	May 14	Polanco	6,500	100%	1	25	8.0%	6.7%
Corporativo San Mateo	Funo	Jun 14	Periférico Norte	5,440	100%	1	9	9.1%	6.4%
Corporativo La Viga	Funo	Jul 14	Polanco	38,250	95%	1	32	8.5%	6.7%
P4	Funo	Oct 14	Insurgentes	19,986	98%	4	43	8.7%	7.1%
Utah Portfolio	Funo	Jan 15	Reforma-Lomas	16,348	100%	1	68	8.8%	7.7%
Florida Portfolio	Funo	Mar 15	Insurgentes	21,755	100%	1	43	8.9%	7.7%
Artificios 40	Funo	Nov 15	Constituyentes	2,603	95%	1	3	8.7%	7.7%
Alaska Portfolio	Funo	Dec 15	Mixed (Mx City)	127,626	99%	6	303	8.6%	7.6%
Prometeo	Fibra MTY	Dec 15	Monterrey	8,135	100%	-	27	7.5%	7.5%
Torre Cuarzo	Funo	Feb 16	Reforma	72,000	98%	1	179	9.4%	8.0%
Fortaleza	Fibra MTY	Apr 16	Interlomas	15,200	96%	1	38	8.1%	7.2%
Redwood	Fibra MTY	Feb 16	Guadalajara	11,605	100%	1	36	8.3%	8.3%
Saqqara	Funo	Apr 17	Monterrey	11,236	70%	1	43	9.1%	8.6%
Montes Urales	Funo	Apr 18	Reforma	5,760	95%	1	60	8.0%	8.6%
Edificio Vallarta	Fibra MTY	May 18	Jalisco	12,478	100%	1	23	8.4%	9.1%
Patria	Fibra MTY	Oct 18	Guadalajara	8,050	76%	1	13	9.3%	9.9%
Corporativo Arboledas (Portfolio HD	Fibra HD	Nov 18	State of Mexico	3,152	100%	1	4	9.0%	10.2%

Source: Company Data, BTG Pactual Estimates

Chart 126: Mexican real estate stocks have traded at discounts to the pricing of private market transactions
Precedent Transactions from listed players 12MF NOI Cap Rate (%) vs Trading 12MF NOI Cap Rate (%)



Source: Source: Company Data, BTG Pactual Estimates
Notes: Includes precedent transactions for large portfolios (>US$30m) and small portfolios in the industrial space for Fibra Uno, Fibra Danhos, and Fibra Monterrey. Implied NOI Cap Rate is calculated as the aggregate cap rate for all of these players.

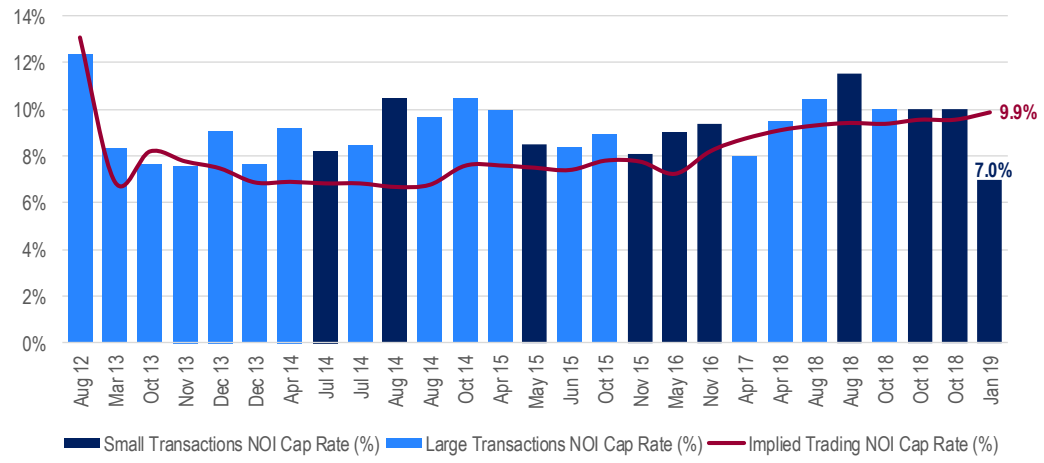
Appendix 5: Retail Sector – Precedent transactions

Table 29: Historical Transactions

	Buyer	Transaction date	Location	GLA (m2)	Occupancy (%)	# of properties	Transaction Value (P$m)	NOI Cap Rate (%)
Cartera Blanco	Fibra Uno	Aug 12	Mexico City	145,200	99.0%	1	735	12.3%
Kimco Portfolio	Fibra MQ	Mar 13	ND	192,006	90.1%	9	1,594	8.3%
Portfolio Maine - Commercial	Fibra Uno	Oct 13	Bajio of Mexico	26,850	98.0%	1	472	7.6%
Power Centers	Fibra MQ	Nov 13	Mexico City	134,246	98.7%	2	2,100	7.5%
Texcoco	Fibra Shop	Dec 13	State of Mexico	60,003	95.1%	1	936	9.1%
Apollo (MRP)	Fibra Uno	Dec 13	ND	970,000	92.0%	49	23,155	7.6%
Nima Shops	Fibra Shop	Apr 14	Puerto Vallarta	3,991	82.2%	1	114	9.2%
Cartera R-15 (Galerias Guadalaja	Fibra Uno	Jul 14	Bajio of Mexico	72,893	90.0%	1	3,459	8.2%
Cartera R-15 (Península Vallarta)	Fibra Uno	Jul 14	Puerto Vallarta	11,874	75.0%	1	260	8.5%
Juarez	Fibra Shop	Aug 14	Ciudad Juarez	51,128	86.1%	1	607	10.5%
Kimco Portfolio	Fibra Shop	Aug 14	ND	117,531	83.5%	3	1,551	9.7%
Las Misiones	Fibra Shop	Oct 14	Ciudad Juarez	58,185	86.1%	1	632	10.5%
City Center Bosque Esmeralda	Fibra Shop	Apr 15	State of Mexico	29,588	87.5%	1	405	10.0%
Kansas Portfolio (Stabilized)	Fibra Uno	May 15	ND	251,891	89.0%	10	8,712	8.5%
Oregon Portfolio	Fibra Uno	Jun 15	Mexico City	34,103	99.0%	3	1,626	8.4%
Puebla (Cruz del Sur)	Fibra Shop	Oct 15	Puebla	29,900	97.2%	1	519	8.9%
Monza	Fibra Monterrey	Nov 15	Chihuahua	4,600	100.0%	2	77	8.1%
Plaza Cedros - Cuernavaca	Fibra Shop	May 16	Cuernavaca	19,300	90.7%	1	370	9.0%
Apollo II	Fibra Uno	Nov 16	Mexico City	362,781	93.2%	18	10,800	9.4%
Puerta La Victoria	Fibra Shop	Apr 17	Queretaro	57,240	92.0%	1	2,762	8.0%
Portfolio HD17 - Comercial	Fibra HD	Apr 18	Mixed	56,380	95%	4	950	9.5%
A single property in Nogales	Fibra Plus	Aug 18	Sonora	25,936	100%	1	528	10.4%
Educational Portfolio	Fibra Educa	Aug 18	Mixed	143,687	100%	33	5,400	11.5%
Portfolio HD18 (I)	Fibra HD	Oct 18	Mexico City	6,266	100%	8	102	10.0%
Portfolio HD18 (II)	Fibra HD	Oct 18	Mexico City	3,252	100%	5	54	10.0%
Portfolio HD18 (II)	Fibra HD	Oct 18	Mexico City	4,141	100%	7	139	10.0%
Urban Center Condesa (sale)	Seris Retail	Jan 19	Mexico City	1,454	100%	1	115	7.0%

Source: Company Data, BTG Pactual Estimates

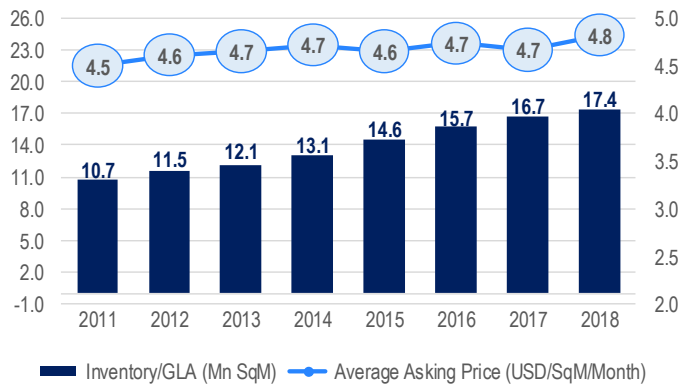
Chart 127: Mexican real estate stocks have traded at discounts to the pricing of private market transactions
Precedent Transactions from listed players 12MF NOI Cap Rate (%) vs Trading 12MF NOI Cap Rate (%)



Source: Source: Company Data, BTG Pactual Estimates
Notes: Includes precedent transactions for large portfolios (>US$30m) and small portfolios in the industrial space for Fibra Uno, Fibra Danhos, and Fibra Monterrey. Implied NOI Cap Rate is calculated as the aggregate cap rate for all of these players.

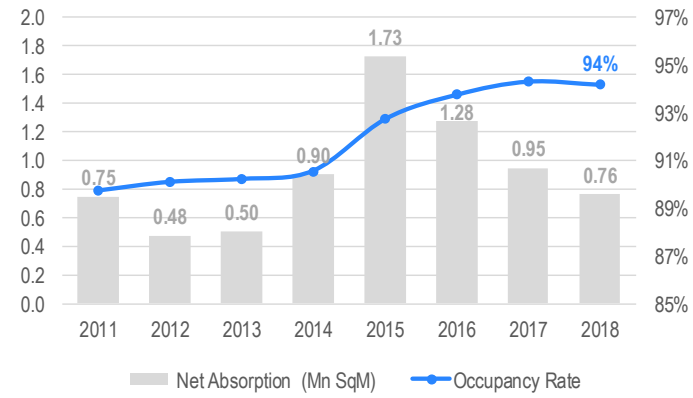
Appendix 6: Industrial Real Estate Sector

Chart 128: North Region – Inventory and rents



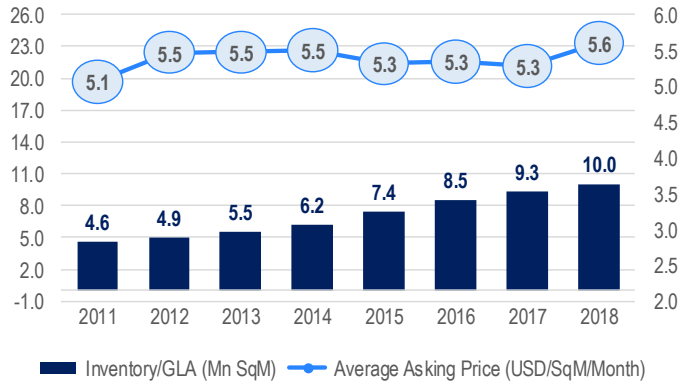
Source: CBRE

Chart 129: North Region – Net Absorption and Occupancy (%)



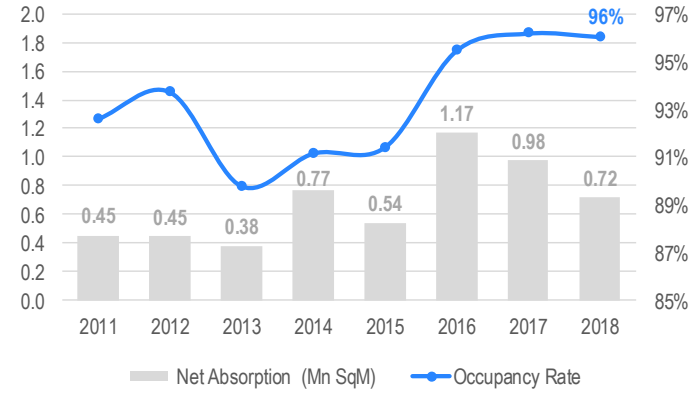
Source: CBRE

Chart 130: Central Region – Inventory and rents



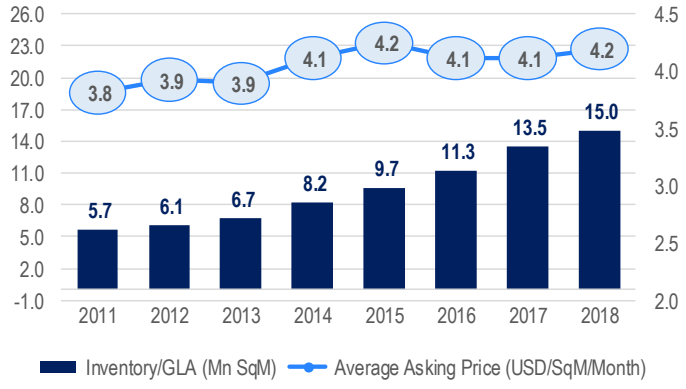
Source: CBRE

Chart 131: Central Region – Net Absorption and Occupancy (%)



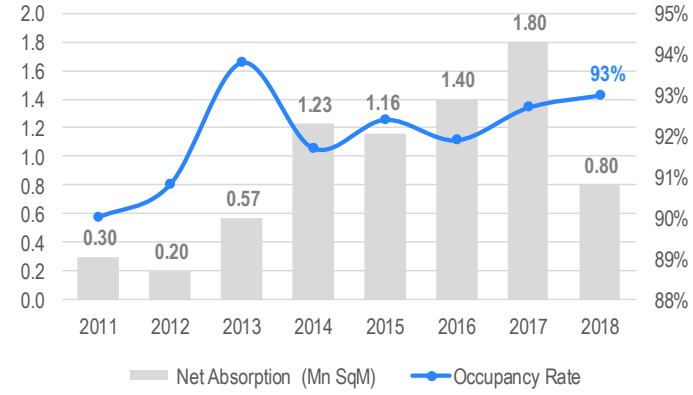
Source: CBRE

Chart 132: Bajio Region – Inventory and rents



Source: CBRE

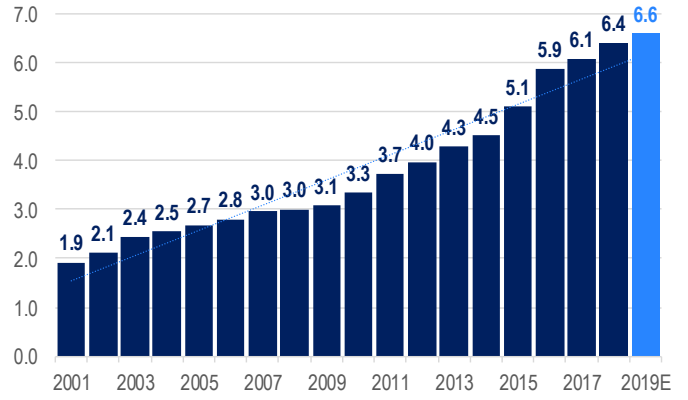
Chart 133: Bajio Region – Net Absorption and Occupancy (%)



Source: CBRE

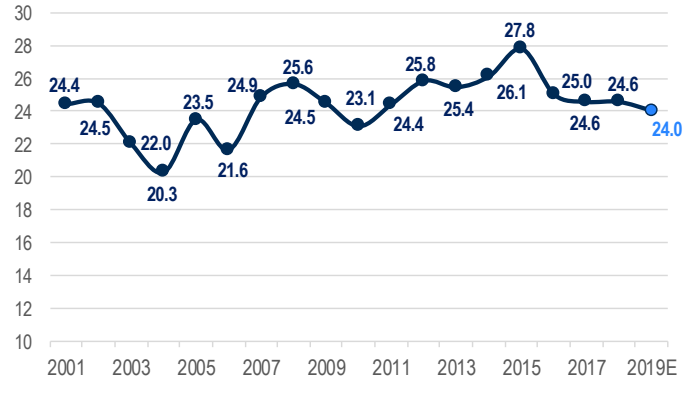
Appendix 7: Mexico City Office Real Estate Sector

Chart 134: Mexico City Office Class A/A+ Inventory (m sqm)



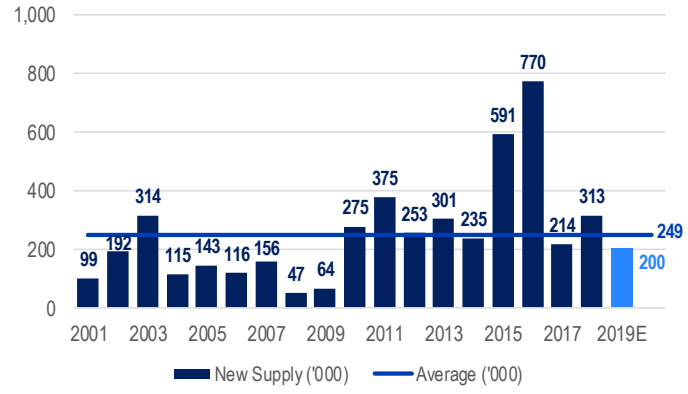
Source: CBRE, BTG Pactual Estimates

Chart 135: Mexico City Office Class A/A+ Rents per sqm



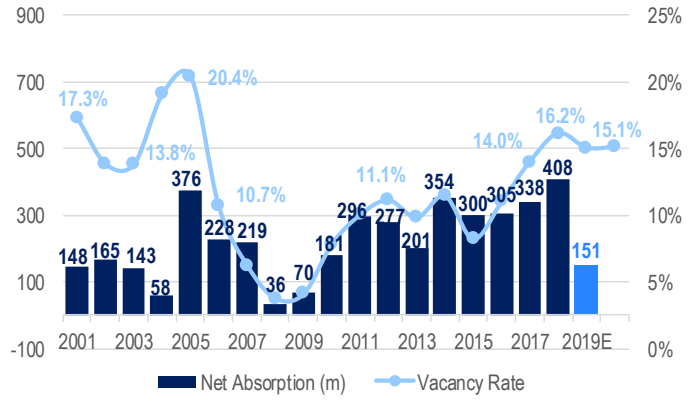
Source: CBRE, BTG Pactual Estimates

Chart 136: Mexico City Office Class A/A+ New Supply ('000 sqm)



Source: CBRE, BTG Pactual Estimates

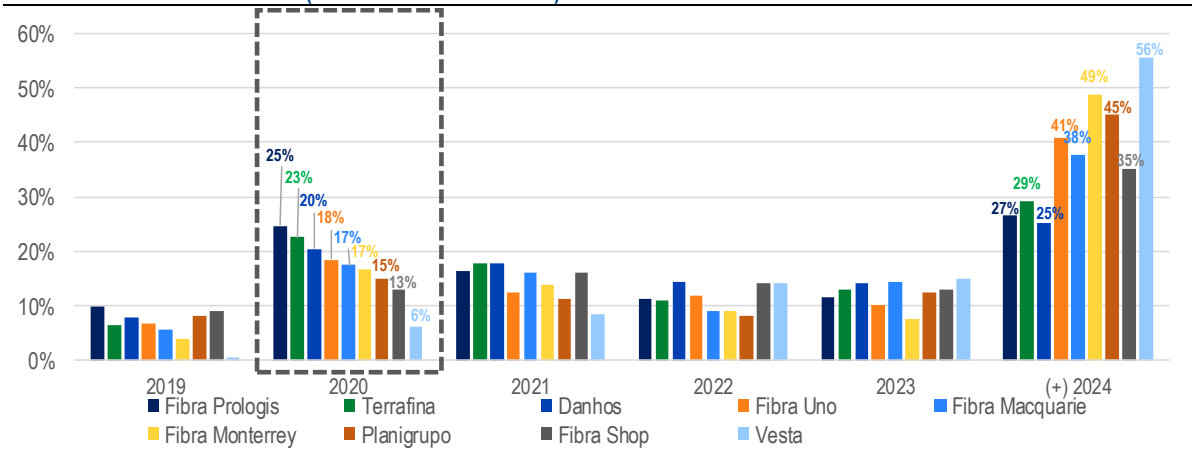
Chart 137: Mexico City Office Class A/A+ Historical Net Absorption ('000 sqm)



Source: CBRE, BTG Pactual Estimates

Appendix 8: Lease Expiration Profile

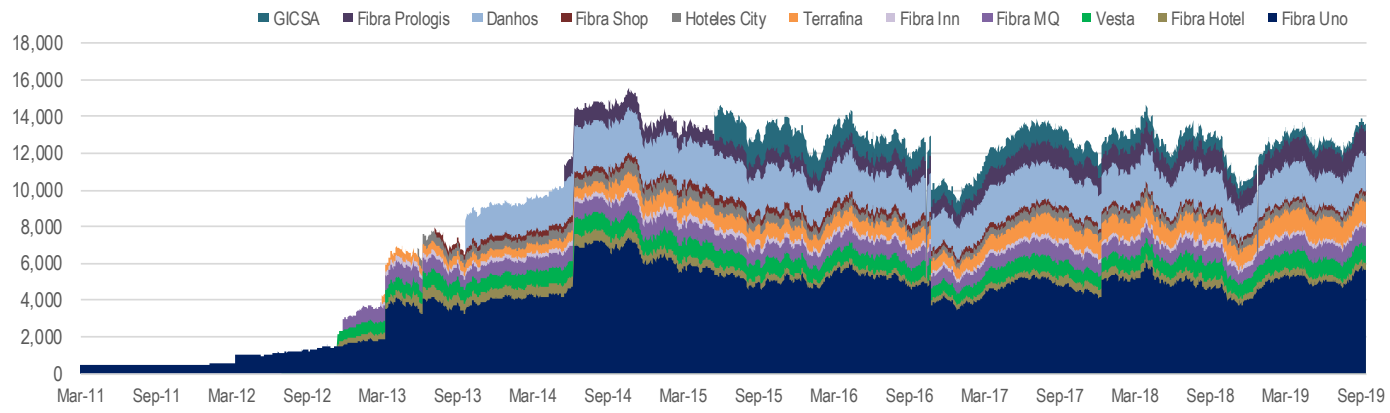
Chart 138: Mexican Real Estate (% of annualized base rent)



Source: Company Data, BTG Pactual Research

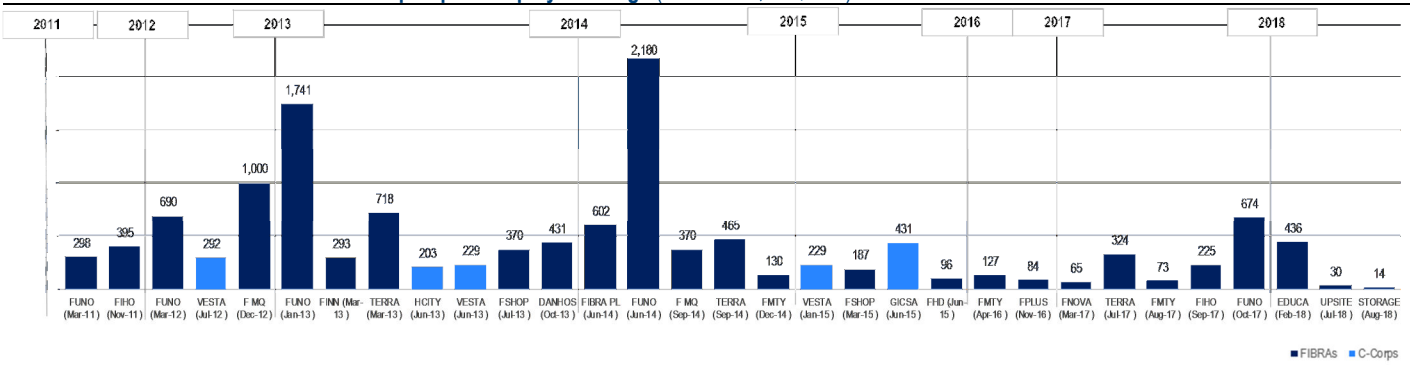
Appendix 9: Mexican Real Estate Equity Market Activity

Chart 139: Mexican Real Estate Market Capitalization Evolution (Market Capitalization, US$ mm)



Source: Company Data, Bloomberg, BTG Pactual Estimates

Chart 140: Evolution of the FIBRA & C-Corps Space: Equity Offerings (Deal Value, US$ mm)



Source: Company Data, Bloomberg, Pactual Estimates

Appendix 10: FIBRAs vs. C-Corps Overview

Chart 141: How do FIBRAs compare to C-Corps ?

FIBRAs

- **Distributions**
  - Distributes at least **95%** of taxable net income as dividends to shareholders annually.
  - FIBRAs operate as a pass-through vehicle, so there are no taxes at the corporate level (only at the investor level, subject to the investor's fiscal regime).
- **Investment Focus**
  - Must invest at least **70%** of total assets in real estate
  - All of the FIBRA's properties must be designed for leasing activities. These properties may not be sold or swapped within four years of their acquisition or development.
- **Growth options**
  - FIBRAs are subject to capital markets financing as their main source of capital to invest; either equity or debt.
  - FIBRAs leverage limit measured as LTV (loan to value) is 50%, as set by Mexican regulation
- **Compensation structure**
  - Mainly externalized management and subject to a fee structure

C-Corps

- **Distributions**
  - Not required by regulation to paid distributions.
  - There are taxes at the corporate level (corporate tax).
  - All distributions to shareholders are post income tax.
- **Investment Focus**
  - No rule on how assets must be invested.
  - No rule on the purpose for the assets
- **Growth options**
  - As C-Corps are not obligated by regulation to distribute dividends, they can reinvest their capital into their own pipeline
  - No leverage limit by regulation
- **Compensation structure**
  - Internalized management structure

Source: Source: BTG Pactual Research

Chart 142: FIBRAs - Distributions & Taxes

A discussion on the tax treatment of distributions made by FIBRAs

- FIBRAs benefit from an income tax-pass through at the property level (they do, however, pay a minor property tax – called *predial*, in Mexico).
- FIBRAs must distribute at least 95% of net income on the basis of tax accounts, which **differs from IFRS net income in that it reflects a depreciation charge**, making it somewhat lower than the number reported to investors.
- FIBRAs are free to make distributions in excess of its net income, which for accounting and tax purposes is considered a **return of capital** or **"payouts of depreciation"**.
- Once a FIBRA decides to return capital (i.e., make a distribution in excess of its minimum payout), the required payout on net income rises from 95% to 100%.
- A large portion of historical and projected distributions for FIBRAs are in the form of returns of capital because there is a "re-set" to the depreciable value of assets when transferred into the FIBRA structure.
- Investors must deal with the tax implications of the distributions as a function of their own particular conditions and although the **distinction between a dividend and a return of capital** would seem semantic (cash is cash, however you choose to call it), **their taxable treatment is materially different** and important to understand:

Taxes on dividends paid out of taxable net income

- **Mexican institutions** (***personas morales***) that comply with certain regulatory requirements (including, most importantly, **Afores**) receive dividends paid by FIBRAs **entirely tax-free**, in essence doubling their tax efficiency.
- **Mexican individual investors** (***personas fisicas***) pay a **28%** tax on dividends from FIBRAs.
- For **foreigners**, Mexico similarly garnishes **28% of dividends**.

Taxes on returns of capital or "payouts of depreciation"

- Any return of capital is **tax free**, regardless of one's domicile.
- This is important considering that for the next several years, a meaningful share of payouts will come from returns of capital, making the effective tax rate significantly lower than the 28% garnished on dividends.

Source: Source: BTG Pactual Research

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The figures contained in performance charts refer to the past; past performance is not a reliable indicator of future results.

BTG Pactual Rating	Definition	Coverage *1	IB Services *2
Buy	Expected total return 10% above the company's sector average.	57%	48%
Neutral	Expected total return between +10% and -10% the company's sector average.	39%	34%
Sell	Expected total return 10% below the company's sector average.	4%	22%

1: Percentage of companies under coverage globally within the 12-month rating category.

2: Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

Absolute return requirements

Besides the abovementioned relative return requirements, the listed absolute return requirements must be followed:

a) a Buy rated stock must have an expected total return above 15%

b) a Neutral rated stock can not have an expected total return below -5%

c) a stock with expected total return above 50% must be rated Buy

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Statement of Risk

Terrafina [MXTERRA] - Risks include but are not limited to: (i) increases in TIs and leasing commissions, (ii) a potential cut to the dividend payout to preserve capital and lower leverage, (iii) rising interest rates as it is a yield play, (iv) investor defections to other industrial Fibras.

Planigrupo Latam [PLANIMM] - Risks include (i) the spillover from the global de-rating in cap rates for B and C assets, (ii) faster than expected e-commerce penetration in Mexico, (iii) dilutive expansions abroad, (iv) low stock liquidity, (v) high leverage levels.

Fibra Monterrey [FMTYMM] - Risks include, but are not limited to: Low stock liquidity, among the least CDMX-metro area exposed, exposed to the office space, maintaining its agility (particuarly when it comes to smaller properties) as it grows.

Fibra Danhos [DANHOS] - Risks include, but are not limited to: office exposure at a time of material and rising oversupply; a cyclical downturn impcating retail exposure and structural oversupply; a high fee structure; among others.

Fibra Prologis [FIBRAPL] - Risks include, but are not limited to: 1. its greater exposure to the domestic economy and therefore more MXN cashflows and recent slowing of the domestic economy. 2. issuing equity at dilutive valuations to buy fully priced assets. 3. Any change in the balance of the relationship with Prologis (parent). 4. Higher interest rates, weaker GDP, a weaker MXN.

Fibra Uno Administracion, S.A. de C.V. [MXFUNO] - Risks: Office segment - A significant part of FUNO's pipeline comes from the office segment which is set to continue to see supply/demand dynamics worsen. Other risks include diltive M&A from thier pre-announced pipeline (higher CBFI payment vs. expectations given lower CBFI price), an increase in interest rates, less fees from Helios and a downturn in retail activity in Mexico (60% of NOI comes from retail portoflios).

Fibra Macquarie S.A. de C.V. [MXFIBMQ] - 1) Mexican economic cycles and demand for real estate; 2) Supply of new competing real estate; 3) Regulations, especially at the municipal level; 4) Security concerns as most of the portfolio is concentrated in northern cities; 5) U.S. economic performance and value of the U.S. dollar

Fibra Shop (Trust F/00854) [MXFSHOP] - 1) Mexican economic cycles and demand for real estate; 2) Supply of new shopping malls; 3) Regulations, especially at the municipal level; 4) Geographic concentration as both the Bajío region as well as Cancun & Cabo San Lucas represent sizeable portions of Fibra Shop's portfolio; 5) Potential value leakage from various management and advisory fees Fibra Shop pays its controllers; and 6) Potential value leakage from asset transfers from controllers.

Corporación Inmobiliaria Vesta, S.A.B. de C.V. [MXVESTA] - Investment risks include but are not limited to: (i) too lean of a management structure as Vesta plans on growing considerably in the coming years, (ii) financial instability from Bombardier, one of Vesta's key clients, (iii) lack of yield, (iv) macroeconomic instability as Vesta's clients are exposed to cyclical businesses and any potential risk from NAFTA negotiations.

Valuation Methodology

Terrafina [MXTERRA] - Our DDM-driven price target of P$31.7/CBFI id discounted on a CoE of 7.4% assuming a terminal LTV of 35% by 2023.

Planigrupo Latam [PLANIMM] - Our price target is derived via a DDM and exit cap rate blend. We use a COE of 10.8% and an exit NOI cap rate in 2025 of 8.5%.

Fibra Monterrey [FMTYMM] - Our DDM-driven price target of P$13.7/CBFI translates into 2020E implied P/NAV of 0.98x. Our DDM is based on a USD COE of 8.2% and assumes a terminal LTV of 35% by 2023.

Fibra Danhos [DANHOS] - Our P$36.2/CBFI valuation is based on a DDM analysis, discounted at a CoE of 12.0% and assumes a terminal LTV of 10% by 2023, consistent with its existing balance sheet.

Fibra Prologis [FIBRAPL] - Our DDM-driven price target of P$46.2/CBFI is discounted at a CoE in USD of 7.5%.

Fibra Uno Administracion, S.A. de C.V. [MXFUNO] - Our TP of P$34.3/CBFI is based on a DDM of FUNO's existing portfolio (P$33.2/CBFI) and the NPV of FUNO's 63.6% stake in Helios (P$1.1/CBFI). Our Ke is 10.0%.

Fibra Macquarie S.A. de C.V. [MXFIBMQ] - Our target price is based on a DDM that employs a COE of 7.9% (in USD) and assumes a terminal LTV of 35% by 2023.

Fibra Shop (Trust F/00854) [MXFSHOP] - Our target price is based on a A Dividend Discount Model (DDM) based on 20-year dividend projections for the base portfolio (the current asset base) which yields a TP of P$8.2/CBFI discounted at a cost of equity in MXN of 11.5%. We are also adding P$0.3/CBFI for equity investments in La Perla and Sentura.

Corporación Inmobiliaria Vesta, S.A.B. de C.V. [MXVESTA] - Our TP for Vesta is based on the sum of the DDM (present value of dividends paid through 2024) and the PV of an Exit Cap rate analysis assuming Vesta is able to sell their fully deployed portfolio in 2024. We use a COE of 7.7% (in USD) and an exit NOI cap rate in 2026 of 8.0%.

Company Disclosures

Company Name	Reuters	12-mo rating	Price	Price date
Danhos [1, 2, 4, 6, 18, 19, 20]	Danhos	Buy	MXN27.03	2-10-2019
Fibra MQ [1, 2, 4, 6, 18, 19, 20]	FIBMQ	Buy	MXN24.82	2-10-2019
Fibra MTY [18, 19, 20, 21, 22]	FMTY	Buy	MXN12.14	2-10-2019
Fibra Prologis [1, 2, 4, 6, 18, 19, 20]	FIBRAPL	Buy	MXN40.44	2-10-2019
Fibra Shop [1, 2, 4, 6, 18, 19, 20]	FSHOP	Neutral	MXN8.15	2-10-2019
Fibra Uno [1, 2, 4, 6, 18, 19, 20]	N.A.	Buy	MXN28.77	2-10-2019
Planigrupo [18, 19, 20, 21, 22]	PLANI	Neutral	MXN19.00	2-10-2019
Terrafina [1, 2, 4, 6, 18, 19, 20]	Terra	Neutral	MXN30.48	2-10-2019
Vesta [1, 2, 4, 6, 18, 19, 20]	N.A.	Buy	MXN29.92	2-10-2019

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