

Grupo Herdez, S. A. B. de C. V. and subsidiaries

# CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2019 AND 2018

(With Independent Auditors' Report Thereon)  
(Translation from Spanish Language Original)

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# INDEPENDENT AUDITORS' REPORT

(Translation from Spanish Language Original  
To the Board of Directors and Stockholders  
Grupo Herdez, S. A. B. de C. V.  
(Thousands of Mexican Pesos)

## OPINION

We have audited the consolidated financial statements of Grupo Herdez, S. A. B. de C. V. and subsidiaries (“the Group”), which comprise the consolidated statement of financial position as at December 31, 2019 and 2018, the consolidated statements of income and other comprehensive income, changes in equity and cash flows for the years then ended, and notes, including significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of Grupo Herdez, S. A. B. de C. V. and subsidiaries as at December 31, 2019 and 2018, and of its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

## BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the consolidated financial statements section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Mexico, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## KEY AUDIT MATTERS

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

## GOODWILL

Amount of goodwill \$1,270,788 associated with Grupo Nutrisa. See note 11 to the consolidated financial statements.

Key Audit Matter	How the key matter was addressed in our audit
<p>Within the frozen segment, there is a risk in the goodwill book value amount of the Cash-Generating Unit (CGU) of Grupo Nutrisa, which is significant due to the budgeted results and financial projections of this CGU have not been historically reached in a way that allows the Group to obtain the recoverable value of the long-lived assets including the goodwill allocated to this cash-generating unit.</p> <p>Due to the inherent uncertainty involved in forecasting and discounting future cash flows, which are the basis to assess the goodwill recoverability of this CGU, entails, it becomes a key audit matter</p>	<p>Our audit procedures to address this key audit matter, included the review of historical figures as of December 31, 2019, compared to the projections of previous years, to analyze business performance of the last 7 years; the normalization of 2019 figures and the assumptions of the 2020 budget, as well as the review of the reasonability of the projections of the future periods based on the Group's Management strategy, in particular those related to projected income growth and profit margins, on which the primary assumptions of the discounted cash flow model are based. In this regards with the involvement of our own valuation specialists; we evaluated, among other aspects, those related to assumptions, discount rates and the methodologies used by the Group.</p> <p>We compared the assumptions of the CGU with external data obtained, as well as our own valuations related to the main elements, such as comparable companies, projected growth, competition, cost growth and discount rates. We compared the sum of discounted cash flows at the valuation date, as well as valuation exit multiples against the book value of the total assets of CGU and the value of goodwill and the brands recognized in the Group's books.</p>

## OTHER INFORMATION

Management is responsible for the other information. The other information comprises the information included in the Group annual report of December 31, 2019 which should be filed to the National Banking and Securities Commission and the Mexican Stock Exchange (Annual report) but does not include the consolidated financial statements and our auditors' report thereon. The annual report is expected to be made available to us after the date of this auditors' report.

Our opinion on the consolidated financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

When we read the annual report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

## RESPONSIBILITIES OF MANAGEMENT AND THOSE CHARGED WITH GOVERNANCE FOR THE CONSOLIDATED FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, and for such internal control as Management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, Management is responsible for assessing the Group's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

## AUDITORS' RESPONSIBILITIES FOR THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.


- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient and appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

KPMG Cárdenas Dosal, S. C.



Mario J. Carrillo Villalpando

Mexico City, March 24, 2020.

Grupo Herdez, S. A. B. de C. V. and subsidiaries

## CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

December 31, 2019 and 2018 (Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original  
and for the convenience of foreign/ English speaking readers.*

Assets	2019	2018
Current assets:		
Cash and cash equivalents	\$ 2,309,507	2,026,625
Trade receivables (notes 6 and 9)	3,173,045	2,895,444
Debtors (note 9)	141,493	204,712
Value-added tax receivable	967,471	683,002
Income tax receivable	7,286	-
Related parties (note 7)	247,305	228,860
	4,536,600	4,012,018
Inventories (note 8)	3,990,972	3,627,400
Derivative financial instruments (note 5)	52,860	53,609
Prepayments	84,716	84,683
Total current assets	10,974,655	9,804,335
Property, machinery and equipment (note 10)	5,540,290	5,448,592
Right-of-use assets (note 16)	864,509	-
Equity-accounted investees (note 12)	7,186,573	6,971,663
Intangible assets and goodwill (note 11)	7,372,705	6,752,467
Deferred income tax (note 18)	1,077,563	619,298
Other assets	65,139	43,640
Total assets	\$ 33,081,434	29,639,995

See accompanying notes to consolidated financial statements.

Grupo Herdez, S. A. B. de C. V. and subsidiaries

# CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

December 31, 2019 and 2018 (Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original and for the convenience of foreign/ English speaking readers.*

Liabilities and stockholders' equity	2019	2018
Current liabilities:		
Bank loans (note 14)	\$ -	200,000
Suppliers	2,455,053	2,157,650
Accounts payable	1,549,629	1,121,686
Related parties (note 7)	77,432	55,334
Derivative financial instruments (note 5)	19,245	103,050
Income tax payable	170,649	21,331
Lease liabilities (note 16)	303,818	-
Employees' statutory profit sharing payable	52,095	44,730
Total current liabilities	4,627,921	3,703,781
Total current liabilities		
Notes payable (note 14)	7,960,373	6,403,477
Long-term debt (note 14)	7,644	34,782
Lease liabilities (note 16)	587,208	-
Deferred income tax (note 18)	1,273,795	932,955
Taxes under tax consolidation (note 18)	113,013	146,407
Employee benefits (note 17)	263,824	168,946
Total non-current liabilities	10,205,857	7,686,567
Total liabilities	14,833,778	11,390,348
Stockholders' equity (note 19):		
Capital stock	575,625	575,625
Reserve for repurchase of shares	453,150	616,506
Retained earnings	6,282,338	6,443,803
Legal reserve	141,862	141,862
Premium on the subscription of shares	135,316	135,316
Cumulative financial instrument valuation effect	44,683	( 6,303 )
Cumulative translation effect	340,995	443,036
Capital attributable to controlling interest	7,973,969	8,349,845
Capital attributable to non-controlling interest	10,273,687	9,899,802
Total stockholders' equity	18,247,656	18,249,647
Contingencies and commitments (notes 27 and 28)		
Subsequent events (note 29)		
Total liabilities and stockholders' equity	\$ 33,081,434	29,639,995

Grupo Herdez, S. A. B. de C. V. and subsidiaries

# CONSOLIDATED STATEMENTS OF INCOME

Years ended December 31, 2019 and 2018

(Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original and for the convenience of foreign/ English speaking readers.*

	2019	2018
Net sales (note 20)	\$ 22,420,369	20,970,683
Cost of goods sold (note 21)	13,787,485	12,720,979
Gross profit	8,632,884	8,249,704
Operating expenses:		
Selling (note 22)	4,960,707	4,579,470
Administrative (note 22)	825,232	786,227
	5,785,939	5,365,697
Income before other income	2,846,945	2,884,007
Other income, net (note 23)	142,957	112,856
Operating income	2,989,902	2,996,863
Financial result:		
Interest earned and exchange gain (note 24)	308,390	450,901
Interest paid and exchange loss (note 24)	( 920,518 )	( 941,502 )
Financial result, net	( 612,128 )	( 490,601 )
Equity investment in associates (note 12)	775,933	916,111
Income before income taxes	3,153,707	3,422,373
Income taxes (note 18)	929,665	998,614
Consolidated net income for the year	2,224,042	2,423,759
Net income attributable to controlling interests	1,014,497	1,156,258
Net income attributable to non-controlling interests	1,209,545	1,267,501
Consolidated net income for the year	2,224,042	2,423,759
Basic earnings per common and diluted share in Mexican pesos (note 26)	\$ 2.475	2.717

See accompanying notes to consolidated financial statements.



Grupo Herdez, S. A. B. de C. V. and subsidiaries

# CONSOLIDATED STATEMENTS OF OTHER COMPREHENSIVE INCOME

Years ended December 31, 2019 and 2018

(Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original and for the convenience of foreign/ English speaking readers.*

	<b>2019</b>	2018
Consolidated net income for the year	\$ 2,224,042	2,423,759
Items that will not be reclassified to statement of income:		
Actuarial losses on employee benefit obligations	( 57,551)	15,215
Items that will be or could be reclassified subsequently to statement of income:		
Foreign currency translation results	( 184,215)	( 43,594)
Change in valuation of derivative financial instruments	142,219	( 75,655)
Effects of equity-accounted investments	50,635	16,521
Consolidated comprehensive income	<u>2,175,130</u>	<u>2,336,246</u>
Comprehensive income attributable to non-controlling interest	1,200,371	1,208,516
Comprehensive income attributable to controlling interest	974,759	1,127,730
Consolidated comprehensive income	<u>\$ 2,175,130</u>	<u>2,336,246</u>

See accompanying notes to consolidated financial statements.

Grupo Herdez, S. A. B. de C. V. and subsidiaries

# CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDER 'S EQUITY

Years ended December 31, 2019 and 2018 (Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original  
and for the convenience of foreign/ English speaking readers.*

	Capital stock	Reserve for repurchase of shares	Retained earnings	Legal reserve
<b>Balances as of December 31, 2017</b>	\$ 575,625	497,253	6,088,047	141,862
Increase in repurchase fund	-	400,000	( 400,000 )	-
Repurchase of outstanding shares (note 19(b))	-	( 280,747 )	-	-
Decree of dividends (note 19(d))	-	-	( 425,987 )	-
	-	119,253	( 825,987 )	-
Comprehensive income (note 3):				
Net income for the year	-	-	1,156,258	-
Effect of translation	-	-	-	-
Change in valuation of derivative financial instruments, net of tax	-	-	-	-
Effects of equity-accounted investees, net of tax	-	-	16,521	-
Actuarial losses on employees' benefit obligations, net of tax	-	-	8,964	-
Comprehensive income for the year	-	-	1,181,743	-
<b>Balances as of December 31, 2018</b>	575,625	616,506	6,443,803	141,862
Increase in repurchase fund	-	737,423	( 737,423 )	-
Repurchase of outstanding shares (note 19(b))	-	( 900,779 )	-	-
Decree of dividends (note 19(d))	-	-	( 449,856 )	-
Non-controlling interests capital stock decrease (note 19(c))	-	-	-	-
	-	( 163,356 )	( 1,187,279 )	-
Comprehensive income (note 3):				
Net income for the year	-	-	1,014,497	-
Effect of translation	-	-	-	-
Change in valuation of derivative financial instruments, net of tax	-	-	-	-
Effects of equity-accounted investees, net of tax	-	-	50,635	-
Actuarial losses on employees' benefit obligations, net of tax	-	-	( 39,318 )	-
Comprehensive income for the year	-	-	1,025,814	-
<b>Balances as of December 31, 2019</b>	\$ 575,625	453,150	6,282,338	141,862

See accompanying notes to consolidated financial statements.

Grupo Herdez, S. A. B. de C. V. and subsidiaries

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY

Years ended December 31, 2019 and 2018 (Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original and for the convenience of foreign/ English speaking readers.*

Premium on the subscription of shares	Cumulative financial instrument valuation effect	Cumulative translation effect	Capital attributable to controlling interest	Capital attributable to non-controlling interest	Total stockholders' equity
135,316	25,913	464,833	7,928,849	9,412,948	17,341,797
-	-	-	-	-	-
-	-	-	(280,747)	-	(280,747)
-	-	-	(425,987)	(721,662)	(1,147,649)
-	-	-	(706,734)	(721,662)	(1,428,396)
-	-	-	1,156,258	1,267,501	2,423,759
-	-	(21,797)	(21,797)	(21,797)	(43,594)
-	(32,216)	-	(32,216)	(43,439)	(75,655)
-	-	-	16,521	-	16,521
-	-	-	8,964	6,251	15,215
-	(32,216)	(21,797)	1,127,730	1,208,516	2,336,246
135,316	(6,303)	443,036	8,349,845	9,899,802	18,249,647
-	-	-	-	-	-
-	-	-	(900,779)	-	(900,779)
-	-	-	(449,856)	(813,418)	(1,263,274)
-	-	-	-	(13,068)	(13,068)
-	-	-	(1,350,635)	(826,486)	(2,177,121)
-	-	-	1,014,497	1,209,545	2,224,042
-	-	(102,041)	(102,041)	(82,174)	(184,215)
-	50,986	-	50,986	91,233	142,219
-	-	-	50,635	-	50,635
-	-	-	(39,318)	(18,233)	(57,551)
-	50,986	(102,041)	974,759	1,200,371	2,175,130
135,316	44,683	340,995	7,973,969	10,273,687	18,247,656

Grupo Herdez, S. A. B. de C. V. and subsidiaries

## STATEMENTS OF CONSOLIDATED CASH FLOWS

Years ended December 31, 2019 and 2018

(Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original and for the convenience of foreign/ English speaking readers.*

	2019	2018
Operating activities:		
Income before income taxes	\$ 3,153,707	3,422,373
Adjustments for:		
Depreciation and amortization	827,625	519,880
Fishing equipment maintenance application	119,433	107,602
(Profit) loss on sale of property, machinery and equipment	( 88,401)	1,155
Net period cost for employee benefits	33,706	31,252
Interest income	( 145,955)	( 120,372)
Investment in associates	( 775,933)	( 916,111)
Gain on sale of shares	-	( 8,282)
Other expenses (income) without cash flow	35,028	( 26,132)
Employees' statutory profit sharing	52,920	53,722
Interest expense	724,314	598,228
Subtotal	3,936,444	3,663,315
Increase of accounts receivable	( 214,382)	( 395,891)
Increase of inventories	( 363,572)	( 406,439)
Decrease (increase) in related parties, net	3,652	( 70,466)
Increase in advanced payments and recoverable taxes	( 291,788)	( 204,360)
Increase in suppliers	297,404	311,441
Decrease in other accounts payable and creditors	338,185	300,360
Income tax paid	( 1,010,076)	( 1,083,328)
Net cash from operating activities	2,695,867	2,114,632
Investing activities:		
Equity interest in subsidiaries	416	( 38,947)
Sale of shares	-	18,113
Acquisition of business	( 324,749)	-
Dividends collected	446,447	570,423
Interest collected	145,955	120,962
Acquisition of property, machinery and equipment	( 754,269)	( 496,480)
Collections on sale of property, machinery and equipment	138,679	24,610
Acquisition of intangible	( 271,288)	( 27,025)
Net cash from investing activities	( 618,809)	171,656

Grupo Herdez, S. A. B. de C. V. and subsidiaries

## STATEMENTS OF CONSOLIDATED CASH FLOWS

Years ended December 31, 2019 and 2018

(Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original and for the convenience of foreign/ English speaking readers.*

	2019	2018
		Continúa >
Financing activities:		
Issues of domestic bonds	-	1,000,000
Long-term bank loans obtained	2,400,000	900,000
Long-term bank loans paid	( 830,000)	( 1,400,000)
Domestic bonds payment	( 200,000)	( 200,000)
Other long-term liabilities	( 40,241)	( 12,526)
Acquisition of non-controlling interest	( 13,068)	-
Repurchase of shares	( 900,779)	( 280,747)
Interest paid	( 599,943)	( 602,110)
Dividends paid	( 1,263,274)	( 1,147,649)
Payment of lease liabilities	( 338,373)	-
Net cash from financing activities	( 1,785,678)	( 1,743,032)
Increase in cash and cash equivalents	291,380	543,256
Effect from exchange rates on cash and cash equivalents	( 8,498)	( 1,431)
Increase in cash and cash equivalents	282,882	541,825
Cash and cash equivalents:		
At beginning of the year	2,026,625	1,484,800
At end of the year	\$ 2,309,507	2,026,625

*See accompanying notes to consolidated financial statements.*

Grupo Herdez, S. A. B. de C. V. and subsidiaries

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2019 and 2018 (Thousands of Mexican pesos)

*These financial statements have been translated from the Spanish language original and for the convenience of foreign/ English speaking readers.*

## 1. Reporting entity

Grupo Herdez, S. A. B. de C. V. (the “Company”), is a company located in Mexico, which trade shares on the Mexican Stock Exchange. The Company’s registered office is at Calzada San Bartolo Naucalpan 360, Argentina Poniente, Mexico City, 11230. These consolidated financial statements comprise the Company and its subsidiaries (collectively “Group” and individually “Group companies”) and the Group’s share on related entities and jointly controlled. The Company is a 51% subsidiary of Hechos con Amor, S. A. de C. V., it is exposed to and has rights to variable returns.

The Group is mainly engaged in the manufacture, purchase, distribution and marketing of canned and packed food products in Mexico and ice cream, as well as food products targeted at the Mexican food segment within the United States of America (USA).

The entities of Grupo Herdez, S. A. B. de C. V. manufacture and commercialize products under the following trademarks: Aires de Campo, Barilla, Búfalo, Carlota, ChiChi’s, Del Fuerte, Don Miguel, Doña María, Embasa, Herdez, La Victoria, McCormick, Wholly, Yemina, Nutrisa, Helados Nestle, Cielito Querido Café and Moyo, among others. For such purposes, Grupo Herdez, S. A. B. de C. V. have forged alliances with leading companies worldwide, such as: McCormick and Company Inc., Hormel Foods Corp., Barilla G. e. R. Fratelli S. p. A. and Grupo Kuo, S. A. B. de C. V. (Grupo Kuo).

## 2. Basis of preparation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as issued by the International Accounting Standards Board (“IASB”).

On February 27, 2020, the Board of Directors authorized the issuance of the accompanying consolidated financial statements and notes thereto.

In accordance with the Mexican Corporations Law (LGSM by its Spanish acronym) and the bylaws of Grupo Herdez, S. A. B. de C. V., the stockholders are empowered to modify the consolidated financial statements after issuance. The accompanying consolidated financial statements will be submitted to the next Stockholders’ Meeting for approval.

Details of the Group’s accounting policies including changes in the financial year, are included in note 3.

### a) *Basis of measurement*

The consolidated financial statements have been prepared on the historical cost basis except for following items, which are measured on an alternative basis on each consolidated financial statements:

- The defined benefit liability is recognized as the fair value of plan assets, less the present value of the defined benefit obligation, limited as explained in note (3(i)).
- Derivative financial instruments are measured at fair value and recognized in the other comprehensive income when these are effective within the accepted range and classified as hedge, otherwise these instruments are recognized in the income statement.

b) *Functional and reporting currency*

These consolidated financial statements are presented in Mexican pesos, which is the Company's functional currency. All amounts have been rounded to the nearest thousands of Mexican pesos, unless otherwise indicated.

In the case of the foreign entities of the joint venture in the U.S.A., their financial statements are presented in the local currency which is their functional currency and they are converted to Mexican pesos allowing the Company to recognize their participation in such entities.

c) *Use of judgments and estimates*

In preparing these consolidated financial statements according to IFRS, Management has made judgments, estimates and assumptions that affect the application of the Group's accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively.

Information about judgments made in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements and estimates with a significant risk of resulting in a material adjustment in the next financial year are described below:

i) *Consolidation of entities on which there are no majority shareholding*

The Group analyzes the existence of control over those entities on which it does not have majority shareholding, evaluating if it is exposed or has rights to the variable yields from its involvement with the entity, and has the ability to affect yields through its power over the entity. If as a result from the analysis, the Group determines that it exercises control of these entities, they are consolidated within the Group. If there are no signs of the existence of control on the entities, the investment in those associated and joint venture companies are recognized by the equity method.

ii) *Fair values determination*

The Group applies the guidelines of IFRS 13, *Fair Value Measurement* ("IFRS 13") to determine the fair values of financial assets and financial liabilities recognized or disclosed at fair value. IFRS 13 does not require fair values in addition to those required or allowed by other IFRS and is not required to establish valuation standards or affect valuation practices outside of financial reporting. Under IFRS, the fair value represents the "Selling Price", which would be received from selling an asset or would be paid for transferring a liability in an orderly transaction between market participants as at the date of valuation, considering the credit risk of the counterparty in the valuation.

The concept of selling price is based on the assumption that there is a market and participants in such market for the specific asset or liability. When there is no market and/or participants to form the market, the IFRS 13 establishes a fair value hierarchy that organizes the entry data in the valuation techniques used to determine fair value. The hierarchy of highest priority is unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority is that of the calculations that have to do with entry data that are significant but unobservable (level 3 measurement). The three levels of hierarchy are as follows.

- Level 1 inputs are active market prices (unadjusted) for identical assets and liabilities that the Group has the ability to negotiate on the measurement date.
- Level 2 inputs are different from market prices, but are directly or indirectly observable for the asset or liability.
- Level 3 inputs are those that are unobservable for the asset or liability.

The fair value of assets for disposal along with the unobservable inputs are estimated by independent specialized firms engaged for each asset.

iii) *Fair value of derivative financial instruments*

The fair values of derivative instruments traded on recognized markets are determined based on quotations issued by these markets. In those cases in which the instruments are traded on OTC market (“*Over The Counter*”), the fair value of the financial instruments is estimated on the basis of valuation technical models recognized in the financial area, mainly using to expected future cash flows discounted at present value and based on market information available at the valuation date.

In order to determining the fair values, conditions and assumptions are used, mainly based on rate models based on TIIE 28, the Mexican Average Interbank Interest Rate (TIIE per its Spanish acronym) and exchange rate MXP/USD available at the valuation date.

The Group has conducted the effectiveness tests required to comply with hedge accounting, which fall within the ranges allowed under IFRS.

iv) *Useful lives of property, machinery and equipment*

The Group determines the useful lives of its assets based on their best estimate of the periods during which economic benefits are expected to be obtained derived from such assets.

v) *Impairment of goodwill and other intangible assets with undefined useful lives*

In the case of goodwill and intangible assets with undefined useful lives, the impairment test is performed at each reporting date. For the evaluation of the value in use, estimated future cash flows are discounted at their present value, using a discount rate before taxes that reflects the market evaluations for the value of the money over time, taking into account the specific risks inherent to the asset. For impairment testing purposes, assets that cannot be tested individually are integrated in smaller groups of assets that generate cash inflows from on-going use and that are, for the most part, independent from the cash inflows of other assets or groups of assets (the “cash generating unit”). For impairment testing purposes, the goodwill is assigned to the operational divisions of the group and monitored in terms of the Group’s operative segments (operative division) and reports the lowest level at which the goodwill is monitored for internal reporting purposes. Impairment losses are recognized in the income statement. Impairment losses recorded with respect to the cash generating units are distributed first to reduce the carrying value of any goodwill distributed to the units and subsequently to reduce the carrying value of other assets in the unit (group of units) on a pro rata basis. No goodwill-related impairment loss is reverted.



vi) *Determination of employee benefits*

Direct benefits are applied in the income statement as they arise and the related liabilities are stated at their nominal value, due to their short-term nature. The Group's net obligations with respect to defined benefit pension plans are calculated separately for each plan, estimating the amount of the future benefit earned by employees in return for their services in the current and past periods; this benefit is discounted to determine its present value and the fair value of plan assets is deducted. The discount rate is calculated on the basis of zero coupon government bonds with maturity term resembling those of the Group's obligations and that are determined in the same currency in which the benefits are expected to be paid. The calculation is performed annually by a qualified actuary, using the projected unit credit method.

vii) *Impairment of accounts receivable*

The Group uses two variables to segment the portfolio according to the business model and which consistently encompass the accounts; these variables are the type of channel and the collection period. Grupo Herdez's policy considers all those accounts within the period of 1-30 days as not past due. The data used to determine the expected loss percentage are the default status and the actual experience of credit loss in the last two years, incorporating macroeconomic factors from the last five years. As of December 31, 2019, the following factors were applied to accounts receivable.

	31-60 days	61-90 days	More than 90 days
Weighted average factor	1.64%	2.63%	4.58%
Weighted average factor including macroeconomic factors	1.52%	2.44%	4.25%

viii) *Leases*

The periods to quantify the number of future lease payments are defined according to the lesser between the term of the contract and the remaining useful life of the contract, if the Group is reasonably sure of exercising extension options. The options considered by the Group for extension are the following:

- In the case of transportation equipment, simulations are not carried out for renewal of expired contracts.
- The renewal simulations for contracts in the process of being signed, were for the same number of periods as the most recent contract in force, analyzing the certainty of permanence in the leased location.

The discount rate is defined when a new contract is agreed and there are renewals from contract termination.

At inception of the leases need to be considered future payments in the calculation.

### 3. Significant accounting policies

The following accounting policies set out have been applied consistently to all the periods presented in these consolidated financial statements, and have been applied consistently by the Group's entities, except if mentioned otherwise:

#### a) *Basis of consolidation*

##### i) *Businesses combinations*

The Group accounts for businesses combinations using the purchase method when control is transferred to the Group (see (a)(iii)).

The consideration transferred in the acquisition and the identifiable net assets acquired are generally measured at fair value. Any goodwill that arises is tested annually for impairment (see (h)(iii)). Any gain on a bargain purchase is recognized in the income statement, immediately.

Transaction costs are expensed as incurred, unless they relate to the issuance of debt or equity instruments (see (v)).

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are recognized in the income statement.

Any contingent consideration is measured at fair value at the date of acquisition. In other cases, subsequent changes in fair value of the contingent consideration are recognized in the income statement.

##### ii) *Non-controlling interest*

For each business combination, the Group measures any non-controlling interest in the investee at:

- Fair value, or
- The proportionate share of the acquires identifiable net assets at the date of acquisition, which are generally at fair value.

Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as interest non-controlling transactions, therefore any effect is recognized in equity.

##### iii) *Subsidiaries*

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases.

Following shows the detail of the Group's significant subsidiaries and joint ventures, as well as the ownership percentage it has on each of them:

	Country where it was incorporated	December 2019	December 2018	Note
<b>Foods</b>				
Herdez Del Fuerte y subsidiarias (HDF) - Subsidiary	Mexico	50%	50%	1
<b>Herdez Del Fuerte-</b>				
<u>Manufacturing and trading:</u>				
Herdez, S. A. de C. V. - Subsidiary	Mexico	100%	100%	1
Hersea, S. A. de C. V. - Subsidiary	Mexico	100%	100%	1
Compañía Comercial Herdez, S. A. de C. V. - Subsidiary	Mexico	100%	100%	1
Alimentos Del Fuerte, S. A. de C. V. (Alimentos Del Fuerte) - Subsidiary	Mexico	99.95%	99.95%	1
Saben a Cine, S.A.P.I. de C. V. - Subsidiary	Mexico	100%	50%	1, 6
Intercafé, S. A. de C. V. - (Intercafé) - Joint Venture	Mexico	50%	50%	2
Aires de Campo, S. A. de C. V. - Subsidiary	Mexico	92.62%	92.62%	1
Buenos de Origen Services, S. A. de C. V. - Subsidiary	Mexico	92.62%	92.62%	1
Incubadora Orgánica, S. A. de C. V. - Joint Venture	Mexico	50%	50%	2
Authentic Acquisition Corporation (AAC) - Subsidiary	USA	100%	100%	1, 3
Authentic Speciality Foods (ASF) - Subsidiary	USA	100%	100%	1, 3
Megamex Foods, LLC - Joint Venture	USA	50%	50%	2, 3
Megamex Holding Inc. - Joint Venture	USA	50%	50%	2, 3
Don Miguel Foods Corp. - Joint Venture	USA	50%	50%	2, 3
Avomex Inc. - Negocio conjunto	USA	50%	50%	2, 3
Avomex Internacional, S. A. de C. V. - Joint Venture	Mexico	50%	50%	2, 3
Avomex Service, S. de R. L. de C. V. - Joint Venture	Mexico	50%	50%	2, 3
Avomex Importación y Export Limitada - Joint Venture	Chile	50%	50%	2, 3
<u>Services provider:</u>				
Campomar, S. A. de C. V. (Campomar) - Subsidiary	Mexico	100%	100%	1
Hersail, S. A. de C. V. (Hersail) - Subsidiary	Mexico	100%	100%	1
Herventa, S. A. de C. V. (Herventa) - Subsidiary	Mexico	100%	100%	1
<b>Manufacturing and trading:</b>				
McCormick de México, S. A. de C. V. (McCormick) - Subsidiary	Mexico	50%	50%	1
Barilla México, S. A. de C. V. (Barilla México) - Subsidiary	Mexico	50%	50%	1
Serpasta, S. A. de C. V. (Serpasta) - Subsidiary	Mexico	50%	50%	1
Herpons Continental, S. A. de C. V. (Herpons Co.) - Subsidiary	Mexico	100%	100%	1

	Country where it was incorporated	December 2019	December 2018	Note
Grupo Nutrisa y subsidiarias - Subsidiary	Mexico	99.84%	99.84%	1
Grupo Nutrisa				
<u>Trading:</u>				
Nutrisa, S. A. de C. V. (Nutrisa) - Subsidiary	Mexico	100%	100%	1
Ubongo, S. A. P. I. de C. V. - Subsidiary	Mexico	100%	50%	1
Alimentos Benefits, S. A. de C. V. (Benefits) - Subsidiary	Mexico	100%	100%	1
Nutrisa USA, LLC. (Nutrisa USA) - Subsidiary	USA	100%	100%	1
Olyen Coffee, S. A. de C. V. - Subsidiary	Mexico	100%	100%	1
Coordinadora RC, S. A. de C. V. – Subsidiary	Mexico	100%	-	1, 5
RC Operadora de Cafeterías, S. A. de C. V. – Subsidiary	Mexico	100%	-	1, 5
<u>Services:</u>				
Servinutrisa, S. A. de C. V. (Servinutrisa) – Subsidiary	Mexico	100%	100%	1
Servibenefits, S. A. de C. V. – Subsidiary	Mexico	100%	100%	1
Helado de Yogurt, S. A. de C. V. – Subsidiary	Mexico	100%	100%	1, 4
Nutriservicios la Colmena, S. A. de C. V. – Subsidiary	Mexico	100%	100%	1, 4
Prestadora de Servicios de Grupo Café Caffé, S. A. de C. V. – Subsidiary	Mexico	100%	-	1, 5
<u>Real-Estate Group:</u>				
Promociones Inmobiliarias Naturistas, S. A. de C. V. (Promociones) - Subsidiary	Mexico	100%	100%	1
<u>Services:</u>				
Corporativo Cinco, S. A. de C. V. (Corporativo) – Subsidiary	Mexico	100%	100	1
Seramano, S. A. de C. V. (Seramano) - Subsidiary	Mexico	100%	100%	1
Fábrica de Envases del Pacífico, S. A. de C. V. - Joint Venture	Mexico	50%	50%	2
<u>Real-Estate Group:</u>				
Herport, S. A. de C. V. (Herport) - Subsidiary	Mexico	50%	50%	1
Alimentos HP, S. A. de C. V. (Alimentos) - Subsidiary	Mexico	100%	100%	1
Comercial de Finanzas Netesa, S. A. de C. V. (Netesa) - Subsidiary	Mexico	100%	100%	1
Energía Para Preserves, S. A. de C. V. - Subsidiary	Mexico	89.75%	89.75%	1
Quicolor de México, S. A. de C. V. (Quicolor) - Subsidiary	Mexico	100%	100%	1
Promotora Hercal, S. A. de C. V. (Hercal) - Subsidiary	Mexico	100%	100%	1

<sup>(1)</sup> Consolidated entity.

<sup>(2)</sup> Entity recognized under the equity method.

<sup>(3)</sup> Financial statements from December 3, 2018 to December 1, 2019.

<sup>(4)</sup> Entities created on March 22, 2018 and beginning operations in July, 2018.

<sup>(5)</sup> In accordance with the Second Amending Agreement from November 28, 2019, a purchase agreement of the companies Coordinadora RC, S. A. de C. V., RC Operadora de Cafeterías, S. A. de C. V., and Prestadora de Servicios de Grupo Café Caffé, S. A. de C. V.; was entered; as the selling party, it was subscribed by Progreso de Oriente, S. A. de C. V. and Administra, S. A. de C. V. and as the purchasing party it was subscribed by Olyen Coffee, S. A. de C. V. and Grupo Nutrisa, S. A. de C. V.

<sup>(6)</sup> On October 1, 2019, a purchase agreement was entered for the remaining 50% of the shares of the capital stock owned by Saben a Cine, S. A. P. I. de C. V.; Operadora Comercial de Desarrollo, S. A. de C. V. was entered as the selling party and Herdez Del Fuerte, S. A. de C. V. and Herdez, S. A. de C. V. as the purchasing parties.

iv) *Loss of control*

When the Group loses control over a subsidiary, it derecognizes the assets and liabilities of the subsidiary, and any related non-controlling interest and other components of equity. Any resulting gain or loss is recognized in the income statement. Any interest retained in the former subsidiary is measured at fair value when control is lost.

v) *Investments in associated entities and jointly controlled entities (equity method)*

Associated are those entities in which the Group has a significant influence, but not control or joint control, over the financial and operating policies. A joint venture is an arrangement in which the Group has joint control over its activities, through which the Group is entitled to the net assets of the agreement and not entitled to its assets and obligations for liabilities, established by contractual agreement and unanimous consent to take financial decisions and strategic operations.

Investments in associated entities and joint venture are recognized for using the equity method, and are initially recognized at cost. The investment cost includes the transaction costs.

The consolidated financial statements include the interest of the Group in the profits or losses and other comprehensive income of investments accounted by the equity method, after performing the adjustments to align the accounting policies with those of the Group, until the date on which significant influence or joint control ceases.

When the portion of losses of the Group exceeds its interest in an investment recognized by the equity method, the carrying amount of that interest, including any long-term investment, is reduced to zero and the recognition of more losses is discontinued except if the Group has an obligation or has made payments on behalf of the company it participates in.

vi) *Transactions eliminated in the consolidation*

Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated. Unrealized profits arising from transactions with companies which investment is recognized by the equity method are eliminated from the investment in the proportion of the Group's participation in the investment. Unrealized losses are eliminated in the same way as unrealized profits, but only to the extent that there is no evidence of impairment.

vii) *Discontinued operations*

A discontinued operation is a component of the Group's business, the operations and cash flows of which can be clearly distinguished from the rest of the Group and which:

- Represents either a separate major line of business or geographical area of operations.
- Is part of a single coordinated plan to dispose the purpose of a separate major line of business or geographic area of operation; or
- Is a subsidiary acquired exclusively with the purpose of re-sale.

Classification as a discontinued operation occurs at the earlier of disposal or when the operation meets the criteria to be classified as held-for-sale.

When an operation is classified as a discontinued operation, the comparative statement of income statement and other comprehensive income is presented as if the operation had been discontinued from the start of the comparative year.

b) *Foreign currency*

i) *Foreign currency transactions*

Transactions in foreign currency are translated into the respective functional currency of Group companies at the exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the exchange rate at the consolidated financial statements date. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency at the exchange rate when the fair value was determined. Non-monetary items that are measured based on historical cost in a foreign currency are translated at the exchange rate at the date of the transaction. Foreign currency differences are generally recognized in the income statement.

Foreign currency differences arising from translation of the following items are recognized in other comprehensive income:

- Available-for-sale equity investments (except for impairment, in which case foreign currency differences that have been recognized in other comprehensive income are reclassified to the income statement).
- A financial liability designated as a hedge of the net investment in a foreign operation to the extent that the hedge is effective; and
- Qualifying cash flow hedges to the extent that the hedges are effective.

ii) *Foreign operations*

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into Mexican pesos at the exchange rates at the consolidated financial statements date. Revenues and expenses of foreign operations are translated into Mexican pesos at the exchange rates at the date of transactions.

Foreign currency differences are recognized in other comprehensive income and accumulated in the translation reserve, except when the translation difference is allocated to non-controlling interest.

When a foreign operation is disposed of in its entirety or such that control, significant influence or joint control is lost, the cumulative amount in the translation reserve related to that foreign operation is reclassified to profit or loss as part of the gain or loss on disposal. If the Group disposes of part of its interest in a subsidiary but retains control, then the relevant proportion of the cumulative amount is reattributed to non-controlling interest.

When the Group disposes only part of an associate or joint venture while retaining significant influence or joint control, the corresponding proportion of the cumulative amount is reclassified to the income statement.

c) *Financial instruments*

IFRS 9 Financial Instruments- hedging relationships with derivative financial instruments.

As of January 1, 2019, the Group decided to adopt the criteria and requirements specified in Chapter 6 of IFRS 9 related to Hedge Accounting derived from the fact that as of January 1, 2018 IFRS 9 did not release the Macro Hedge component, no impacts were identified for hedging relationships.

IFRS 9 sets out requirements for recognizing and measuring financial assets, financial liabilities and some contracts of buying or selling non-financial items. This standard replaces IAS 39 "Financial Instruments: Recognition and Measurement".

As a result of the adoption of IFRS 9, the Group did not identify a significant impact on the classification derived from the impairment losses on trade receivables recognized under IAS 39.

IFRS 9 contains three measurement categories of financial assets:

- Measured at amortized cost.
- Fair value through other comprehensive income (FVOCI).
- Fair value through profit or loss (FVTPL).

The classification of financial assets under IFRS 9 is based on the business model in which a financial asset is managed and its contractual cash flow characteristics and they are listed as follows. IFRS 9 eliminates the previous IAS 39 categories.

	<b>Classification under IFRS 9</b>
<b>Financial assets</b>	
Cash and equivalents	FVTPL
Trade receivables	Amortized cost
AUA Private Equity Parallel Fund, LP*	FVOCI
AUA Indulge Corp	FVOCI
Anteris Capital Venture Lending Fund I, LP	FVOCI
Yaax Capital Private Equity	FVOCI
<b>Financial hedging assets (liabilities)*</b>	
* Hedge relationships with derivative financial instruments is recognized under the guidelines of IFRS 9	
Forwards on Exchange rate hedging	FV- Cash flow hedge
Swaps on interest rate hedging	FV- Cash flow hedge
Commodities futures hedging	FV- Cash flow hedge
<b>Financial liabilities</b>	
Bank loans in Mexican pesos	Amortized cost
<b>Debt issues</b>	
CEBURES HERDEZ 13	Amortized cost
CEBURES HERDEZ 17	Amortized cost
CEBURES HERDEZ 17-2	Amortized cost
CEBURES HERDEZ 18	Amortized cost

i) *Non-derivative financial instruments assets and financial liabilities – Recognition and derecognition*

The Group initially recognized loans and trade accounts receivable issued on the date when they were originated. All the other financial assets (including assets designated at fair value with changes in the statement of income) were initially recognized on the trade date when the Group became part to the instrument's contractual provisions.

The Group derecognized a financial asset when the contractual rights to the cash flows from the asset expire, or when it transferred the rights to receive the contractual cash flows of financial asset in a transaction in which substantially all of the risks and rewards of ownership of the financial asset were transferred, or it neither transferred nor retains substantially all of the risk and rewards of the ownership and did not retain control over the transferred asset. Any interest in such derecognized financial assets created or retained by the Group was recognized as a separate asset or liability.

The Group derecognized a financial liability when its contractual obligations were paid or cancelled, or expired.

A financial asset and a liability would be subject to be offset being the net amount presented in the statement of financial position when the Group has a legal right to offset the amounts and intends to settle the net amount or to realize the asset and settle the liability simultaneously.

ii) *Non-derivative financial assets*

*Loans and accounts receivable*

Loans and accounts receivable are financial assets with fixed or determinable payments that are not traded in an active market.

These assets were initially recognized at fair value, plus any directly attributable transaction cost to initial recognition, loans and accounts receivable are measured at amortized cost, less impairment losses for account receivables. Loans and accounts receivable include trade account receivables and other accounts receivable.

*Cash and cash equivalents*

Cash and cash equivalents include cash balances and deposits with original maturities of three months or less from the date of acquisition subject to exchange effects in fair value and are used by the Group in the Management of its short-term commitments.

The amount of cash and cash equivalents in the balance sheet includes restricted cash and investments, comprised of deposits in margin accounts that guarantee several of the Group obligations, to the extent that the restriction will be lifted in less than three months from the consolidated statement of financial position. When the restriction period is greater than three months, such restricted cash and investments are not considered cash equivalents and are included within short-term or long-term "Debtors" as appropriate.



iii) *Non-derivative financial liabilities*

Initially, the Group recognizes the debt securities issued at the date on which they are generated. All the other financial liabilities are initially recognized on the contracting date on which the Group becomes a party to the instrument's contractual provisions.

The Group eliminates a financial liability when its contractual obligations are cancelled, or expired.

The Group classifies non-derivative financial liabilities in the category of other financial liabilities.

Non-derivative financial liabilities are initially recognized at fair value less any directly attributable transaction costs. Subsequent to initial recognition, these liabilities are measured at amortized cost at the effective interest rate.

Other financial liabilities integrate notes payable, suppliers, other accounts payable and domestic bonds.

iv) *Derivative financial instruments and hedge accounting*

The Group holds derivative financial instruments to hedge its foreign currency and interest rate risk exposures.

In addition, the Group holds derivative to hedge the price of the raw materials (*Commodities*), which are designated in a formal hedging relationship.

In the initial designation of the hedge, the Group formally documents the relationship between the hedging instrument(s) and the item(s) covered, including the risk management objectives and strategy when entering the hedging transactions, as well as the methods to be used in assessing the effectiveness of the hedge relationship.

On January 1, 2019, the Company proceeded to adopt Chapter 6 "Hedge Accounting" of IFRS 9, given that it previously remained under the requirements of IAS 39 associated with Hedge Accounting.

IFRS 9 indicates that the objective of hedge accounting is to represent in the financial statements the effect of the risk management activities of an entity that uses financial instruments to manage exposures that arise from specific risks that could affect the profit or loss for the period.

As of December 31, 2019 and 2018, the Group's Management has evaluated the effectiveness of all hedging relationships, concluding that such relationships are highly effective, and that meet the hedging relationship established for each one, in compliance with the requirements of IAS 39 for hedge relationships.

Derivatives are initially recognized at fair value; any directly attributable transaction costs are recognized in the income statement as incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are generally recognized in the income statement; in case they are designed in a cash flow hedge, changes are recognized in other comprehensive income.

*Cash flow hedges*

When a derivative is designated as a cash flow hedging instrument, the effective portion of the changes in the fair value of the derivative is recognized in other comprehensive income and accumulated in the hedging reserve. Any ineffective portion of the changes in the fair value of the derivative is recognized immediately in the income statement.

When the hedged item is a non-financial asset, the amount accrued in the stockholders' equity is maintained in other comprehensive income and it is reclassified to income statement in the same period when the hedged item affects the income statement. In other cases, the amount accrued in stockholders' equity is reclassified to the income in the same period when the hedged item affects the income statement.

If the hedging instrument is no longer expected to occur, the hedge no longer meets the criteria, expires or is sold, terminated or exercised, or the designation is revoked, then hedge accounting is discontinued prospectively. If the forecast transaction is no longer expected to occur, then the amount accumulated in equity is reclassified to the income statement.

*Embedded derivatives*

Embedded derivatives are separated from the main contract and recorded separately if:

- The characteristics and risks of the main contract and the embedded derivative are not closely related.
- A separate instrument with the same terms as the embedded derivative could meet the characteristics of a derivative.
- The combined instrument is not measured at fair value through with changes in income statement.

*Derivative financial instruments not designated as hedging*

When a derivative financial instrument is not designated for a hedging qualifying relationship all changes in fair value are immediately recognized in income statement.

v) *Equity**Ordinary shares*

Ordinary shares are classified in stockholders' equity. Incremental costs directly attributable to the issue of ordinary shares, net of any tax effects, are recognized as a deduction from equity.

*Repurchase and reissuance of ordinary shares (treasury shares)*

When shares recognized as stockholders' equity are repurchased, the amount of the consideration paid, which includes directly attributable costs, net of any tax effect, is recognized as a deduction from equity. Repurchased shares are presented in the treasury shares reserve. When treasury shares are sold or reissued subsequently, the amount received, as well the surplus or deficit on the transaction are recognized in stockholders' equity.

Capital stock, the reserve for the purchase of shares, the legal reserve, the premium on the subscription of shares and accrued profits are stated as follows: i) movements made as from January 1, 1998 at their historical cost, and ii) movements made prior to January 1, 1998 at their restated historical values by indexing derived from the NCPI until December 31, 1997.

d) *Property, machinery and equipment*

i) *Recognition and measurement*

Items of property, machinery and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses.

The cost includes expenses directly attributable to acquisition of the asset. The cost of assets built by the entity include the following:

- The cost of materials and direct labor.
- Any other costs directly attributable to making the asset suitable to a working condition for its intended use.
- When the Group has an obligation to remove the asset or restore the site, an estimate of the costs of dismantling and removing the items and restoring the site where they are located.
- The capitalized loan costs.

At December 31, 2019 and 2018, there are not qualifying assets where capitalized financing cost exist. Acquired software, which is part of the functionality of the related equipment is capitalized as part of such equipment.

If significant parts of an item of property, machinery and equipment have different useful lives, they are accounted for as separate items (major components) of property, machinery and equipment.

Any gain or loss on the disposal of an item of property, machinery and equipment (determined as the difference between the profits obtained from the sale and the book value for such item) are recognized in the income statement.

ii) *Subsequent expenditures*

Subsequent expenditures are capitalized only if it is probable that the future economic benefits associated with the expenditure will flow to the Group.

Continuous repairs and maintenance are expensed in income statement as incurred.

iii) *Depreciation*

Items of property, machinery and equipment are depreciated from the date on which they are installed and ready for their use or in the case of assets internally built, from the date on which the asset is completed and ready to be used.

Depreciation is calculated to write-off the cost of items of property, machinery and equipment less their estimated residual values using the straight-line method over their estimated useful values, and is generally recognized to the income statement. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term. Land is not depreciated.

The estimated useful lives of property, machinery and equipment for current and comparative periods of the significant items are as follows:

	<b>Years</b>
Buildings	20 - 33
Machinery and tools	10 - 14
Fishing equipment	14 - 17
Furniture and office equipment	12
Stowing and transportation equipment	4 - 10
Electronic data processing equipment	4

Depreciation methods, useful lives and residual values are reviewed at each reporting date of the consolidated financial statements and adjusted if appropriate.

e) *Intangible assets and goodwill*

i) *Goodwill*

Goodwill arising from the acquisition of subsidiaries is measured at cost less accumulated impairment losses.

ii) *Subsequent measures*

Goodwill is valued at cost less accumulated impairment losses. In relation with the investments recognized by the equity method, the book value of goodwill is included in the book value of the investment, and any impairment loss is distributed to the book value of the investment recognized by the equity method as a whole.

iii) *Intangible assets with defined life*

Intangible assets acquired by the Group consisting of non-competition agreements, licenses, developed technology and customer relationships that have defined useful lives are recorded at cost, less accumulated amortization and accumulated impairment losses. The aforementioned does not refer to intangible assets internally developed as they arise from acquisitions made.

iv) *Intangible assets with undefined useful lives*

Intangible assets with undefined useful lives correspond to patents and trademarks, involving no legal, regulatory, contractual, economic or other factors that might limit their useful lives, and which are expected to generate future cash flows, which are not conditioned to a limited period of time, and are thus subject to impairment testing at each reporting date under IFRS.

v) *Subsequent expenditures*

Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditures, including expenditures on internally generate trademarks and goodwill, are recognized in income statement as incurred.

vi) *Amortization*

Amortization is calculated to write-off the cost of intangible assets less their estimated residual values by using the straight-line method over their estimated useful lives, and is generally recognized in the income, goodwill is not amortized.

The estimated useful lives are as follows:

	<b>Years</b>
Non-competition agreements	2 - 3
Developed technology	8 - 20
Customer relationships	13 - 20
Lease rights and software	3

Amortization methods, useful lives and residual values are reviewed at each date of the consolidated financial statements and adjusted if appropriate.

f) *Leases IFRS 16*

IFRS 16 introduced a single, on-balance sheet lease accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

*Policy applicable from January 1, 2019*

At inception of a contract, the Group assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Group uses the definition of a lease in IFRS 16.

i) *As a lessee*

At commencement or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component on the basis of its relative stand-alone prices. However, for the leases of property the Group has elected not to separate non-lease components and account for the lease and non-lease components as a single lease component.

The Group recognizes a right-of-use asset and lease liability at the lease commencement date. The right-of-use asset initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct cost and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term, unless the lease transfers ownership of the underlying asset to the Group by the end of the lease term or the cost of the right-of-use asset reflects that the Group will exercise a purchase option. In that case the right-of-use asset will be depreciated over the useful life of the underlying asset, which is determined on the same basis as those of property and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rates as the discount rate.

The Group determines its incremental borrowing rate by obtaining interest rates from various external financing sources and makes certain adjustments to reflect the terms of the lease and type of the asset leased.

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments, including in-substance fixed payments;
- variable lease payments that depend on an index rate, initially measured using the index or rate as at the commencement date;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that the Group is reasonably certain to exercise, lease payments in an optional renewal period if the Group is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Group is reasonably certain not to terminate early.

The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Group's estimate of the amount expected to be payable under a residual value guarantee, if the Group changes its assessment of whether it will exercise a purchase, extension or termination option or if there is a revised in-substance fixed lease payment.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

#### *Short-term leases and leases of low-value assets*

The Group has elected not to recognize right-of-use asset and lease liabilities for leases of low-value assets and short-term leases, including IT equipment. The Group recognizes the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

ii) *As a lessor*

At inception or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component on the basis of their relative stand-alone prices.

When the Group acts as a lessor, it determines a lease inception whether each lease is a finance lease or an operating lease.

To classify each lease, the Group makes an overall assessment of whether the lease transfers substantially all of the risk and rewards incidental to ownership of the underlying asset. If this is the case, then the lease is a finance lease; if not, then it is an operating lease. As a part of this assessment, the Group consider certain indicators such as whether the lease is for the major part of the economic life of the asset.

When the Group is an intermediate lessor, it accounts for its interest in the head lease and the sub-lease separately. It assesses the lease classification of a sub-lease with reference to the right-of-use asset arising from the head lease, not with reference to the underlying asset. If a head lease is a short-term lease to which the Group applies the exemption described above, then it classifies the sub-lease as an operating lease.

If an arrangement contains lease and non-lease components, then the Group applies IFRS 15 to allocate the consideration in the contract.

The Group applies the derecognition and impairment requirements in IFRS 9 to the net investment in the lease (see Note 3(h)). The Group further regularly reviews estimated unguaranteed residual values used in calculating the gross investment in the lease.

The Group recognizes lease payments received under operating leases as income on a straight-line basis over the lease term as part of 'other income'.

Generally, the accounting policies applicable to the Group as a lessor in the comparative period were not different from IFRS 16 except to the classification of the sub-lease entered into during current reporting period that resulted in a finance lease classification.

*Lease payments*

Payments made under contracts other than those within the scope of IFRS 16 Lease are recognized in profit or loss under the straight-line method for the term of the lease.

iii) *Adoption*

The Group initially applied IFRS 16 on January 1, 2019, using the modified retrospective approach. Consequently, the cumulative effect of adopting IFRS 16 was recognized as an adjustment to the beginning balance of accumulated earnings as of January 1, 2019, without restating the comparative information.

The Group applied the practical solution to adopt the definition of lease at the time of transition. This means that IFRS 16 applies to all contracts signed before January 1, 2019 and identified as leases in accordance with IAS 17 and IFRIC 4.

g) *Inventories*

Inventories are measured at the lower of cost and net realizable value. The cost of inventories is based on the first-in-first-out principle and includes disbursements incurred for the acquisition of inventories, production or manufacturing costs and other costs incurred to transport them to their site and current conditions.

In the case of manufactured inventories and work in progress, costs include an appropriate share of production overheads based on normal operating capacity.

The cost of inventory may also include transfers from equity of any gain or loss on the rated flow hedges of inventory purchases in foreign currency.

Net realizable value is the estimated sale price in the ordinary course of business, less the costs of completion and the estimated necessary costs to close the sale.

h) *Impairment*

i) *Non-derivative financial assets*

Financial asset not classified as at fair value through income statement, including an interest in an equity accounted investee, are assessed at each reporting date to determine if there is an objective evidence of impairment.

Objective evidence that financial assets are impaired includes:

- Default or non-compliance of a debtor;
- Restructuring of an amount due to the Group on terms that the Group would not consider otherwise;
- Indications that a debtor or issuer will declare bankruptcy;
- Adverse changes in the payment status of borrowers or issuers;
- The disappearance of an active market for an instrument; and
- Observable data indicating that there is a measurable decrease in the expected cash flows from a group of financial assets.

For an investment in an equity security, objective evidence of impairment will include a significant or prolonged fair value decrease below its cost. The Group considers a decline of 20% is significant and a period from 9 months is prolonged.

ii) *Financial assets measured at amortized cost*

The Group considers evidence of impairment for these assets measured at amortized cost (loans and receivables and financial assets held to maturity) both an individual assets and a collective level. All receivables and investment securities held to maturity individually significant are assessed for specific impairment. Those who are not specifically impaired are evaluated for collective impairment that has been incurred but not yet identified. Assets that are not individually significant are collectively assessed for impairment by grouping assets with similar risk characteristics.

In assessing collective impairment, the Group uses historical information on the timing of recoveries and the amount of loss incurred, and makes an adjustment if current economic and credit conditions make probable that the actual losses are likely to be greater or lesser than suggested by historical trends.



An impairment loss is calculated as the difference between an asset's carrying amount and the present value of estimated future cash flows, discounted at the asset's original effective interest rate. Losses are recognized in income statement and reflected in an allowance account. If the amount of impairment loss subsequently decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, then the previously recognized impairment loss is reversed through income statement.

iii) *Non-financial assets*

At each consolidated financial statement date, the Group reviews the carrying amount of its non-financial assets, excluding employee benefits, inventories and deferred tax assets, to determine whether there is any indication of impairment exists. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill and intangible assets with undefined useful lives are tested at each reporting date for impairment.

For impairment testing, assets that cannot be individually tested are integrated in smaller groups of assets that generate cash inflows from on-going use and that are, for the most part, independent from the cash inflows of other assets or groups of assets. Goodwill acquired in a business acquisition is distributed to the group of cash-generating units (CGU) expected to benefit from the synergies of the combination.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less selling cost. Value in use is based on the estimated future cash flows, discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit.

An impairment loss is recognized if the carrying amount of an asset or cash-generating unit exceeds its recoverable amount.

The Group's corporate assets do not generate cash inflows separately. If there is any indication that a corporate asset may be impaired, the recovery value of the cash-generating unit to which the corporate asset pertains is then determined.

Impairment losses are recognized in the income statement. They are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit, and then to reduce the carrying amounts of the other assets in the cash-generating unit on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. For other assets, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

i) *Employee benefits*

i) *Short-term benefits*

Short-term employee benefits are expensed as the related service is provided. A liability is recognized for the amount expected to be paid if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

ii) *Defined benefit plans*

The Group's net obligations in respect of defined benefit plans are calculated separately for each plan by estimating the amount of the future benefit that employees have earned in the current and prior periods, discounting that amount and deducting the fair value of any plan assets.

The costs for prior services not yet recognized and the fair value of plan assets are deducted. The discount rate is calculated on the basis of zero-coupon government bonds with maturity term resembling those of the Group's obligations and that are determined in the same currency in which the benefits are expected to be paid.

The calculation is performed annually by a qualified actuary, using the projected unit credit method. When the result of the calculation is a benefit for the Group, the asset recognized is limited to the net total of prior-service costs not yet recognized and the present value of the economic benefits available, in the form of future reimbursements of the plan or reductions in future contributions to the plan. In calculating the present value of the economic benefits, the minimum funding requirements applied to any of the Group's plan. The resulting increase in labor cost of the benefit obligation and expenditure by employees in the year are recognized in operating expenses.

The financial cost associated with increased liability over time, as well as the expected return on the period of plan assets are recognized in the financial results. An economic benefit is available to the Group if it is realizable during the life of the plan, or liquidation of the obligations of the plan. When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognized in the income statement by using the straight-line basis over the average period until the benefits are delivered. To the extent that the benefits are immediately delivered, the expense is immediately recognized in the income statement.

The Group recognizes the actuarial gains and losses arising from defined benefit plans in other comprehensive income and all expenses related to the defined benefit plans in the expenses for benefits to the employees in consolidated statement of income.

When having reductions or settlements in a defined benefit plan, the Group shall recognize gains or losses arising there from. These gains or losses shall include any change that could result in the present value of the defined benefit obligations incurred by the entity, and any changes in the fair value of plan assets, any actuarial gains and losses and past service costs that had not been previously recognized.

j) *Allowances*

An allowance is recognized if: it is a result of a past event, the Group has a present legal or assumed obligation that can be reliably estimated, and will probably require the use of economic resources to settle the obligation.

The long-term allowances are determined by discounting future cash flows at a pre-tax rate that reflects current market evaluation of the book value attributable to the time factor and risks specific to the liability. The unwinding of the discount is recognized as a financial cost.

*Restructuring*

The Group recognizes allowances for restructuring, when restructuring plans have been properly completed and approved by the Management, and have been reported to the third parties involved and/or affected before the date of the consolidated financial statements.

*Contingencies and commitments*

Obligations or losses related to contingencies are recognized as a liability when there is a present obligation resulting from past events and it is likely that the effects will materialize and can be measured reliably; otherwise they are qualitatively disclosed in the consolidated financial statements. The effects of long-term commitments established with third parties, as in the case of supply contracts with suppliers or customers, are recognized in the financial statements considering the substance of the agreements based on what was incurred or accrued. Relevant commitments are disclosed in the notes to the financial statements. No income, profits or contingent assets are recognized.

*k) Revenue*

Income is measured based on the consideration specified in a contract with a client. The Group recognizes revenues when it transfers control over a good or service to a client.

*l) Donations*

To the extent the Group donations to social programs benefit the community in general, they are applied to income as incurred.

*m) Finance income and finance costs*

Financial income includes interest income on invested funds and changes in the fair value of financial assets at fair value in the income statement, as well as exchange gains. Interest income is recognized at amortized cost, using the effective interest method.

Financial costs comprise the interest expense on loans, exchange losses, changes in the fair value of financial liabilities at fair value through the income statement and lease liabilities.

Costs of loans that are not directly attributable to the acquisition, construction or production of an asset that qualifies, are applied to income statement by the effective interest method.

Gains and losses on foreign currency for financial assets and financial liabilities are presented according to their profit or loss position.

*n) Income tax*

Income tax expense comprises current and deferred taxes. It is recognized in income statement except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

*i) Current tax*

Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to tax payable on receivable in respect of previous years. It is measured using tax rates enacted or substantively enacted at the consolidated statements of financial position date. Current tax also includes any tax arising from dividends.

ii) *Deferred tax*

Deferred taxes are recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is not recognized for:

- Temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- Temporary differences related to the investments in subsidiaries, associates and joint ventures to the extent that the Group is able to control the timing of the reversal on the temporary differences and it is probable that they will not be reversed in the foreseeable future; and
- Taxable temporary differences arising on initial recognition of goodwill.

Deferred tax assets recognized for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that the future taxable profits will be available against which they can be used.

Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized; such reductions are reversed when the probability of future taxable profits improves.

Unrecognized deferred tax assets are reassessed at each reporting date and recognized to the extent that it has become probable that future taxable profits will be available against which they can be used.

Deferred tax is measured at the tax rates expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the consolidated financial statement date.

The measurement of deferred tax liabilities reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period under review, to recover or settle the carrying amount of its assets and liabilities.

The effects of income taxes for uncertain tax positions are recognized when it is more likely than not that the position will be sustained on its technical merits and assuming that the authorities will review each position and have full knowledge of the relevant information. These positions are valued based on the accumulated probability model.

Each position is considered individually, without considering its relation to other fiscal procedure. The indicator of more likely than not is a statement from management that the Group is entitled to the economic benefits of the tax position. If a tax position is not considered more likely than not to be sustained, the benefits of the position are not recognized.

The Group recognizes interest and penalties related to unrecognized tax benefits as part of the income tax expense for in the consolidated income statements.

*o) Earnings per share*

The Group presents information on basic Earnings per Share (EPS), and the diluted earnings per share corresponding to its ordinary shares.

Basic EPS are calculated by dividing the profit or loss attributable to the holders of ordinary shares by a weighted average number of shares outstanding during the period, adjusted by own shares held (see note 26). As there are no dilutive effects, the basic earnings per share and diluted earnings is the same.

*p) Operating segments*

Segment results that are reported to the Group General Manager (highest authority in making operating decisions) include items directly attributable to a segment as well as those items that can be allocated on a reasonable basis. Unallocated items comprise mainly corporate assets (primarily the Company's headquarters), the cost of the central office, and tax assets and liabilities.

*q) Comprehensive income*

Comprehensive income is comprised of net income, the valuation of derivative financial instruments and investments (net of tax), translation effects and the results from actuarial losses on employee benefit obligations (net of tax), which are reflected in stockholders' equity, but which do not constitute capital contributions, reductions and/or distributions.

*r) Change in the significant accounting policies*

*a) IFRS 9 Financial Instruments- hedging relationships with derivative financial instruments*

As of January 1, 2019, the Group decided to adopt the criteria and requirements specified in Chapter 6 of IFRS 9 related to Hedge Accounting derived from the fact that as of January 1, 2018 IFRS 9 did not release the Macro Hedge component, no impacts were identified for hedging relationships.

The Group decided to adopt the criteria and requirements specified in Chapter 6 of IFRS 9.

*b) IFRS 16 Leases*

*Before December 31, 2018 - Leases*

*i) Determining whether an agreement contains a lease*

At inception of an agreement, the Group determined whether the agreement is or contains a lease.

The Group separated payments and other consideration required by the agreement, at the beginning of it or after making the proper review, between those derived from the lease and those derived from other elements, based on their relative fair values. If the Group concluded for a finance lease that it is impracticable to separate the payments reliably, then an asset and a liability would recognize at an amount equal to the fair value of the underlying asset, subsequently, the liability was reduced as payments are made, is recognizing the financial cost on the liability using the Group's incremental borrowing rate.

## ii) Leased assets

Assets held by the Group under leases that transferred to the Group substantially all of the risks and rewards of ownership were classified as financial leases. The leased assets were measured initially at an amount equal to the lower of their fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the assets were accounted in accordance with the accounting policy applicable to that asset.

Assets held under other leases were classified as operating leases and are not recognized in the Group's statement of financial position.

## iii) Lease payments

Payments made under operating leases were recognized in income statement on a straight-line basis over the term of the lease. Lease incentives received were recognized as an integral part of the total lease expense, over the term lease.

Minimum lease payments made under financial leases were apportioned between the finance expense and the reduction of liability balance. The financial expense were allocated to each period during the lease term in order to obtain a consistent interest rate on each period, over the remaining balance of the liability.

*Subsequent to January 1, 2019 - Leases*

The Group initially applied IFRS 16 Leases from January 1, 2019.

The Group applied IFRS 16 using the modified retrospective approach, under which the cumulative effect of initial application is recognizes in retained earnings as of January 1, 2019. Accordingly, the comparative information presented for 2018 is not restated- i.e. it is presented, as previously reported, under IAS 17 and related interpretations. The details of the changes in accounting policies are disclosed below. Additionally, the disclosure requirements in IFRS 16 have not generally been applied to comparative information.

## i) Definition of a lease

Previously, the Group determined at contract inception whether an arrangement was or contained a lease under IFRIC 4 "Determining whether an Arrangement Contains a Lease". The Group now assesses whether a contract is or contains a leased based on the definition of a lease, as explained in the policy. On transition to IFRS 16, the Group elected to apply the practical solution not to carry out the evaluation of which transaction correspond to leases. The Group applied IFRS 16 only to contracts that were previously identified as leases. Contracts that were no identified as leases under IAS 17 and IFRIC 4 were not reassessed for whether there is a lease under IFRS 16. Therefore, the definition of a lease under IFRS 16 was applied only to contracts entered into or changed on or after January 1, 2019.

## ii) As a lessee

As a lessee, the Group leases many assets including property, production equipment and IT equipment. The Group previously classified leases as operating or finance leases based on its assessment of whether the lease transferred significantly all of the risk and rewards incidental to ownership of the underlying asset to the Group. Under IFRS 16, the Group recognizes right-of-use assets and lease liabilities for most of these leases – i.e. these leases are on balance sheet.

At commencement or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component on the basis of its relative stand-alone price.

However, for leases of property, the Group has elected not to separate non-lease components and account for the lease and associated non-lease components as a single lease component.

## a. Leases classified as operating leases under IAS 17

Previously, the Group classified property leases as operating leases under IAS 17. On transition, for these leases, lease liabilities were measured at the present value of the remaining lease payments, discounted at the Group's incremental borrowing rate as of January 1, 2019 (see Note 16). Right-of-use assets are measured at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments: the Group applied this approach to all other leases.

The Group applied practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17. In particular, the Group:

- did not recognize right-of-use assets and liabilities for leases for which the lease term ends within 12 months of the date of initial application;
- did not recognize right-of-use assets and liabilities for leases of low value assets (e.g. IT equipment, pallets);
- excluded initial direct cost from the measurement of the right-of-use asset at the date of initial application.

## b. Leases classified as finance leases under IAS 17

The Group leases an equipment, which was classified as a finance lease under IAS 17. For this finance lease, the carrying amount of the right-of-use asset and the lease liability at January 1, 2019 were determined at the carrying amount of the lease and lease liability under IAS 17.

## iii) Operations as a lessor

The Group leases the own property and right-of-use. The Group has classified these leases as operating leases.

The Group is not required to make any adjustments on transition to IFRS 16 for leases in which it acts as a lessor, except for a sub-lease.

The Group has applied IFRS 15 Revenue from contracts with customers to allocate consideration in the contract to each lease and non-lease component.

## iv) Impact on financial statements

*Impact on transition*

When measuring lease liabilities for leases that were classified as operating leases, the Group discounted lease payments using its incremental borrowing rate as of January 1, 2019. The Group recognized additional right-of-use assets and additional lease liabilities, recognized the difference in retained earnings. As of the date of transition to IFRS 16, the Group recorded \$806 million of lease liabilities and \$807 million of right-of-use assets, with no effect on stockholders' equity. The impact on transition is summarized below:

	<b>January 1, 2019</b>
Commitments from operating leases as of January 1, 2019 as disclosed in the IAS 17 in the Group's consolidated financial statements	\$ 3,111,449
Commitments for services	( 844,943 )
Discounted an incremental interest rate as of January 1, 2019.	2,877,178
Finance lease liabilities recognized as of January 1, 2019	27,860
- Recognition exemption for leases of low-value assets	( 465,078 )
- Recognition exemption for leases whit less than 12 months of lease term at transition	( 788,069 )
Leasing liabilities recognized as of January 1, 2019	<u>\$ 806,948</u>

## i) IFRIC 23 Uncertainty over income tax treatments

IFRIC 23 clarifies as are applied the recognition and measurement requirements in IAS 12 Income tax when there is uncertainty over income tax.

Under IFRIC 23, uncertain tax liabilities or assets are recognized using the definition of currents or deferred liabilities or assets under IAS 12. Therefore, those tax balances are presented as currents or deferred assets or liabilities. Such balances are not presented as a provision and other lines as accounts receivable or payable.

No significant impacts have generated in the financial statements as of December 31, 2019 by this interpretation.



## 4. Standards issued but not yet adopted

A number of new standards and amendments to standards are effective for annual periods beginning after January 1, 2019. The following amended standards and interpretations are not expected to have a significant impact on the Group's consolidated financial statements.

- Amendments to references to conceptual framework in IFRS Standards
- The main changes to the Framework's principles have implications for how and when assets and liabilities are recognized and derecognized in the financial statements.
- Definition of a business (amendments to IFRS 3)
- Improve the definition of a business and helps entities to decide whether a transaction is a business combination or an asset group.
- Definition of material (amendment to IAS 1 and IAS 8)
- Establishes that the "information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions of the primary users of the financial statements".

## 5. Financial instruments

The Company's activities expose it to a variety of financial risks: market risk (including currency risk, the risk of interest rates and the risk of fluctuation in the prices of raw materials), credit risk, liquidity risk and operational risk. The overall risk management program considers the volatility of financial markets and seeks to minimize potential adverse effects on financial performance of the Group. The Group uses derivatives financial instruments to hedge certain risk exposures.

Financial risk management is carried out in the Management and Finance Office, in accordance with policies approved by the Boards of Directors. The entity identifies, evaluates and hedges financial risks in close cooperation with its subsidiaries. The Boards of Directors has approved general written policies regarding to the financial risks management, including the risk of prices for certain raw materials, exchange rate risk and risk on interest rate.

All derivative financial instruments contracted by the Group, are formally designated as hedging on the date of hiring under the cash flow model.

### *Derivative financial commodities (Commodities)*

As part of the hedging strategy on raw materials during 2019 and 2018, the Group used derivative financial instruments to reduce the risk of price fluctuations.

The total value of contracts for hedging purposes to purchase raw materials effective as at December 31, 2019 and 2018, are shown as follows:

December 31, 2019

Instrument	Counterparty	Notional amount		Expiration date	Position	Fair value	
		(USD)	(MXN)			(USD)	(MXP)
Futures	CME Clearing*	53,324	1,006,365 <sup>(1)</sup>	Several	Buy (long)	8,757	165,260

December 31, 2018

Instrument	Counterparty	Notional amount		Expiration date	Position	Fair value	
		(USD)	(MXN)			(USD)	(MXP)
Futures	CME Clearing*	56,499	1,110,582 <sup>(1)</sup>	Several	Buy (long)	(4,894)	(96,202)

\* Clearing Member authorized by Chicago Mercantile Exchange.

<sup>(1)</sup> Pounds covered at agreed price.

*Derivative financial instruments on exchange rate*

The Company is exposed in their raw material purchases and export sales of various products, both in foreign currency, to the fluctuation in the peso-U.S. dollar, reason why the Boards of Directors approved its strategy of risk management in order to limit the currency risk of such operations.

As at December 31, 2019 and 2018, the characteristics of the contracts designated as hedges are as follows:

December 31, 2019

Instrument	Counterparty	Notional amount		Expiration date	Position	Fair value
		(USD)	(MXN)			(MXN)
Forwards	National bank*	2,500	48,342	Several	Buy (long)	(641)
	National bank*	31,000	602,743	Several	Buy (long)	(10,525)
	National bank*	10,750	209,614	Several	Buy (long)	(4,191)
		44,250	860,699			(15,357)

December 31, 2018

Instrument	Counterparty	Notional amount		Expiration date	Position	Fair value
		(USD)	(MXN)			(MXN)
Forwards	National bank*	6,700	135,219	Several	Buy (long)	(2,154)
	National bank*	19,000	382,123	Several	Buy (long)	(1,558)
	National bank*	10,300	209,063	Several	Buy (long)	(3,136)
		36,000	726,405			(6,848)

\* AAA rated financial institutions, according to the national and issuers for long term debt.

As of December 31, 2019 and 2018, the Group's Management has evaluated the effectiveness of all hedge relationships, concluding that such relationships are highly effective, and that the hedge ratio in each of them is within the range established that coincides with that used to manage risk from the business view point.

#### *Derivative financial instruments on interest rates*

In order to reduce the risk of adverse movements attributable to the interest rate profile contracted with financial institutions engaged in long-term debt bearing interest at variable rate and are recognized in the consolidated financial statements, Company's Management entered into an interest rate swap agreement which converts variable to fixed rate profile.

The derivative financial instruments acquired in June 2017 were designated in hedge relationships under the cash flow model. The detail of these hedged derivative instruments are as follows:

As of December 31, 2019 and 2018, the Group had the following interest-rate swaps:

#### December 31, 2019

Instrument	Counterparty	Notional amount	Expiration date	Payable rate	Receivable rate	Fair value
		(MXN)				(MXN)
Swap	National banks*	\$ 500,000	May 26, 22	6.75%	TIIE 28	\$ (1,056)
Swap	National banks*	500,000	May 26, 22	6.90%	TIIE 28	(2,832)
		<u>\$ 1,000,000</u>				<u>\$ (3,888)</u>

#### December 31, 2018

Instrument	Counterparty	Notional amount	Expiration date	Payable rate	Receivable rate	Fair value
		(MXN)				(MXN)
Swap	National banks*	\$ 500,000	May 26, 22	6.75%	TIIE 28	\$ 27,977
Swap	National banks*	500,000	May 26, 22	6.90%	TIIE 28	25,632
		<u>\$ 1,000,000</u>				<u>\$ 53,609</u>

\* AAA rated financial institutions, according to the national and issuers debt long-term.

As at December 31, 2019 and 2018, the Group's Management has evaluated the effectiveness of all hedging relationships, concluding that these relationships are highly effective.

The net effect recorded on the capital stock including income tax deferred as at December 31, 2019 and 2018, from financial instrument hedging amounted to \$142,219 y \$(75,655), respectively. The amount included in comprehensive income in the stockholder's equity, will be recycled to income statement when the hedge item affects them; such amount is subject to changes due to market conditions.

Tables below show the periods in which the expected cash flows associated with the hedging relationships cash flows are expected to occur, and when it is expected to affect the income statement (which occurs simultaneously), as well as the book value to the hedging derivative financial instruments associated as at December 31, 2019 and 2018:

December 31, 2019

	Book value	Expected cash flows				
		Total	1 year	2 years	3 years	More than 3 years
Swaps on interest rates						
Liability	\$ (3,888)	(12,250)	7,054	(13,983)	(5,321)	-
Forwards on exchange rates						
Liability	\$ (15,357)	(6,824)	(6,824)	-	-	-
Futures on raw materials						
Asset	\$ 165,260	165,260	161,542	3,718	-	-

December 31, 2018

	Book value	Expected cash flows				
		Total	1 year	2 years	3 years	More than 3 years
Swaps on interest rates						
Asset	\$ 53,609	61,978	18,213	17,937	16,867	8,961
Forwards on exchange rates						
Liability	\$ (6,848)	(7,109)	(7,109)	-	-	-
Futures on raw materials						
Liability	\$ (96,202)	(96,202)	(95,892)	(310)	-	-

*Fair values versus book values*

The table, in the next page, shows the book values and the fair value of the derivative and non-derivative assets and liabilities, including its hierarchy. If the fair value of the financial assets and liabilities measured at fair value is not included, is because the book value is an approximation of fair value.

December 31, 2019

	Book value		Fair value			
	Derivative financial instruments hedging	Other financial liabilities	Level 1	Level 2	Level 3	Total
Non-derivative financial assets measured at fair value						
Cash and cash equivalent	\$ -	2,309,507	2,309,507	-	-	2,309,507
Non-derivative financial assets non-measured at fair value						
Trade receivables	\$ -	3,173,045	-	-	-	-
Non-derivative financial assets measured at fair value						
AUA Private Equity Parallel Fund, LP*	\$ -	105,536	-	-	105,536	105,536
AUA Indulge Corp	-	161,344	-	-	161,344	161,344
Anteris Capital Venture Lending Fund I, LP	-	18,004	-	-	18,004	18,004
Yaax Capital Private Equity	-	1,972	-	-	1,972	1,972
Total non-derivative financial assets measured at fair value	\$ -	286,856	-	-	286,856	286,856
Derivate financial Assets / Liabilities measured at fair value						
Forwards on Exchange rate hedging	\$ (15,357)	-	-	(15,357)	-	(15,357)
Swaps on interest rate hedging	(3,888)	-	-	(3,888)	-	(3,888)
Futures on commodities hedging (1)	52,860	-	165,260	-	-	165,260
Total derivative financial instruments measured at fair value	\$ 33,615	-	165,260	(19,245)	-	146,015
Total non-derivative financial liabilities non-measured at fair value						
Bank loans in MXP	\$ -	(1,978,449)	-	(3,036,204)	-	(3,036,204)
Total non-derivative financial liabilities non-measured at fair value	\$ -	(1,978,449)	-	(3,036,204)	-	(3,036,204)
Debt issues						
CEBURES HERDEZ 13	\$ -	(1,995,285)	-	(2,016,559)	-	(2,016,559)
CEBURES HERDEZ 17	-	(1,992,035)	-	(2,092,972)	-	(2,092,972)
CEBURES HERDEZ 17-2	-	(996,920)	-	(1,009,595)	-	(1,009,595)
CEBURES HERDEZ 18	-	(997,684)	-	(1,008,991)	-	(1,008,991)
Total debt issues	\$ -	(5,981,924)	-	(6,128,117)	-	(6,128,117)

(1) Fair value of the future positions in an amount of \$165,260 discounting cash movements in the margin account, associated with the goodwill of future equivalents to \$(112,400).

December 31, 2018

	Book value		Fair value			
	Derivative financial instruments hedging	Other financial liabilities	Level 1	Level 2	Level 3	Total
Non-derivative financial assets measured at fair value						
Cash and cash equivalent	\$ -	2,026,625	2,026,625	-	-	2,026,625
Non-derivative financial assets non-measured at fair value						
Trade receivables	\$ -	2,895,444	-	-	-	-
Non-derivative financial assets measured at fair value						
AUA Private Equity Parallel Fund, LP*	\$ -	71,897	-	-	71,897	71,897
AUA Indulge Corp	-	136,208	-	-	136,208	136,208
Anteris Capital Venture Lending Fund I, LP	-	11,603	-	-	11,603	11,603
Total non-derivative financial assets measured at fair value	\$ -	219,708	-	-	219,708	219,708
Derivate financial Assets / Liabilities measured at fair value						
Forwards on Exchange rate hedging	\$ (6,848)	-	-	(6,848)	-	(6,848)
Swaps on interest rate hedging	53,609	-	-	53,609	-	53,609
Futures on commodities hedging	(96,202)	-	(96,202)	-	-	(96,202)
Total derivative financial instruments measured at fair value	\$ (49,441)	-	(96,202)	46,761	-	(49,441)
Total non-derivative financial liabilities non-measured at fair value						
Bank loans in MXP	\$ -	(426,190)	-	(495,849)	-	(495,849)
Total non-derivative financial liabilities non-measured at fair value	\$ -	(426,190)	-	(495,849)	-	(495,849)
Debt issues						
CEBURES HERDEZ 13	\$ -	(1,994,279)	-	(1,859,377)	-	(1,859,377)
CEBURES HERDEZ 14	-	(199,789)	-	(199,934)	-	(199,934)
CEBURES HERDEZ 17	-	(1,991,316)	-	(1,877,915)	-	(1,877,915)
CEBURES HERDEZ 17-2	-	(995,833)	-	(1,005,655)	-	(1,005,655)
CEBURES HERDEZ 18	-	(996,070)	-	(1,006,268)	-	(1,006,268)
Total debt issues	\$ -	(6,177,287)	-	(5,949,149)	-	(5,949,149)

## 6. Financial risk management

### *General*

The Group has exposure to the following risks arising from financial instruments:

- Credit risk
- Liquidity risk
- Market risk
- Raw material price risk
- Capital management

This note presents information on the Group's exposure to each of the previously-mentioned risks, objectives, policies and processes of the Group for measuring and managing risks, as well as for managing its capital. More quantitative disclosures are included in the various sections of these consolidated financial statements.

### *Risk management framework*

The Group's board of directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board of Directors has established the Risk Management Committee, which is responsible for developing and monitoring the Group's risk management policies. The committee reports regularly to the Board of Directors on its activities.

The Group's risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls and monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its standards and procedures, aims to maintain a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Group Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures, and reviews the adequacy of the risk management framework in relation to the risk faced by the Group. The Group Audit Committee is assisted in its oversight role by the internal audit. Internal audit conducts both routine and special inspections of risk management controls and procedures, the results of which are reported to the Audit Committee.

#### i) *Credit risk*

Credit risk is defined by the loss that the Group could incur if a counterparty breaches the contractual obligations. In the case of the Group, the positions that are exposed to credit risk are: accounts receivable from customers and positions in derivatives in cash markets with a positive market value.

The Group assumes that the credit risk of a financial asset has increased significantly if it has a delay of over 90 days. In determining whether the credit risk of a financial asset has significantly increased since initial recognition in estimating expected credit losses, the Group considers reasonable and sustainable information that is relevant and available without undue cost or effort. This includes quantitative and qualitative information and analysis, based on the Group's historical experience and an informed credit assessment, including that related to the future.

The Group assumes that the credit risk of a financial asset has increased significantly if it has a delay of over 90 days and evaluates the delay when:

- The financial asset has a delay of 90 days or more.
- The borrower is not likely to pay the credit obligations in full to the Group due to delay or default by the debtor, indications that a debtor or issuer would file bankruptcy, adverse changes in the payment status of borrowers or issuers, observable data which indicate that there was a measurable decrease in the expected cash flows of a group of financial assets.

#### *Accounts receivable*

The credit risk represents the risk of financial loss for the Group, if a customer or counterparty of a financial instruments defaults on its contractual obligations, and arises mainly from the client account receivables.

The Risk Management Committee has implemented a credit policy under which each new customer is analyzed individually for credit-worthiness before the Group's standard payment and delivery terms and conditions are offered. The Group's review includes external ratings, if they are available, and in some cases bank references. Customers failing to meet the Group's credit reference requirements can only conduct operations with the Group through prepayments.

More than 91% of the Group's customers have been transacting with the Group for more than four years, and no impairment loss has been recognized against these customers. In monitoring customer credit risks, customers are grouped according to their credit characteristics, including whether they are an individual or a legal entity, whether they are a wholesaler, retail or an end-user customer, their geographic location, industry, years in business, maturity and existence of prior financial difficulties.

	Carrying amount	
	2019	2018
Wholesale customers	\$ 3,004,266	\$ 2,716,253
Retail customers	78,946	91,353
End-user customers	14,252	31,424
Others	75,581	56,414
Total	<u>\$ 3,173,045</u>	<u>\$ 2,895,444</u>

At December 31, 2019, the maximum exposure to credit risk for trade and other receivables by counterparty type was as follows:

- At December 31, 2019, the Group's most significant customer, accounted for 33% of the trade and other receivables carrying amount (27% in 2018).
- Customers classified as "high risk" identified with delinquency greater than 90 days, are included in a list of restricted customers within the legal customers and are monitored by the risk management committee.



At December 31, 2019 and 2018, the aging of trade and other receivables was as follows:

	2019	2018
Current	\$ 879,139	\$ 1,638,929
1-30 Past due	1,141,439	1,024,790
31-60 Past due	561,039	66,259
61-90 Past due	326,040	25,956
+90 Past due	265,388	145,164
Legal customers		19,366
Total	3,263,968	2,920,464
Impairment loss on trade receivables (*)	( 90,923 )	( 25,020 )
Total trade receivables	\$ 3,173,045	\$ 2,895,444

(\*) Trades payable impairment loss is included in the legal portfolio and portfolio over 90 days past due.

The allowance for impairment loss on trade receivables movement for the years ended December 31, 2019 and 2018, is as follows:

	2019	2018
Allowance as at January 1st	\$ 25,020	\$ 31,063
Plus, additions	65,903	2,844
Less, applications	-	8,887
Allowance as at December 31	\$ 90,923	\$ 25,020

At December 31, 2019 and 2018, the Company had certain accounts receivable that were not past due or impaired. The credit quality for said accounts receivable shows no signs of impairment, as income is obtained from a broad variety of customers ranging from supermarkets, marketers and stores. The Group's customer portfolio is mainly comprised of wholesalers and self-service stores, which entails similar credit risk conditions and account for 95% and 94% of portfolio total in 2019 and 2018, respectively.

At December 31, 2019 and 2018, Group Management has recognized an allowance impairment loss on trade receivables for accounts in legal process that could represent impairment.

#### *Cash and investment in securities*

The Group held cash and cash equivalents for \$2,309,507 and \$2,026,625 as at December 31, 2019 and 2018, respectively. The cash and cash equivalents are held with banks and financial institutions counterparties, which are rated between the rank AA and AAA.

### Guarantees

Cash and cash equivalents include restricted cash as follows:

Margin account held for commodities operation \$201,471 as at December 31, 2018.

Trust account by \$69,335 and \$61,213 as at December 31, 2019 and 2018, respectively.

### Derivatives

The derivative are entered into with bank and financial institution counterparties, which are rated between the range AA and AAA, according to various rating agencies.

The book value of derivative and non-derivative financial assets represents the maximum credit risk exposure of the Group. The maximum loss associated with credit risk, identified by the Group, is as follows:

#### December 31, 2019

	Book value
Derivative financial assets measured at fair value	
Futures on commodities <sup>(1)</sup>	\$ 52,860

<sup>(1)</sup> Fair value of the future positions in an amount of \$165,260 discounting cash movements in the margin account, associated with the goodwill of future equivalents to \$(112,400).

#### December 31, 2018

	Book value
Derivative financial assets measured at fair value	
Swaps on interest rate in MXP	\$ 53,609

#### ii) *Liquidity risk*

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivery cash or another financial asset. The Group's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when they are due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group uses activity based costing method to cost its products and services, which assist it in monitoring cash flow requirements and optimizing its cash return on investments.

Normally, the Group ensures that it has sufficient available cash to cover expected operating expenses for a 60-day period, which includes payment of its financial obligations. The aforementioned excludes the possible impact of extreme circumstances that are not reasonably predictable, such as natural disasters.

*Exposure to liquidity risk*

A table with a summary of the outstanding financial liabilities of payment, including interest payable each future expiration date corresponding to December 31, 2019 and 2018, is shown below:

December 31, 2019

	Book value	Expected cash flows					
		Total	2 months or less	2 months to 1 year	1 to 2 years	2 to 3 years	More than 3 years
Forwards on exchange rate	\$ (15,357)	(15,592)	-	(15,592)	-	-	-
Swaps on interest rate	(3,888)	(4,659)	-	2,244	(4,945)	(1,958)	-
	<u>(19,245)</u>	<u>(20,251)</u>	<u>-</u>	<u>(13,348)</u>	<u>(4,945)</u>	<u>(1,958)</u>	<u>-</u>
Bank loans in MXN	<u>(1,978,449)</u>	<u>(3,036,204)</u>	<u>-</u>	<u>(178,454)</u>	<u>(169,348)</u>	<u>(407,786)</u>	<u>(2,280,616)</u>
Debt issues							
CEBURES HERDEZ 13	(1,995,285)	(2,648,729)	-	(162,182)	(162,182)	(162,182)	(2,162,183)
CEBURES HERDEZ 17	(1,992,035)	(3,398,367)	-	(186,449)	(186,449)	(186,449)	(2,839,020)
CEBURES HERDEZ 17-2	(996,920)	(1,245,162)	(14,554)	(82,250)	(100,604)	(1,047,754)	-
CEBURES HERDEZ 18	(997,684)	(1,120,140)	(18,540)	(60,321)	(1,041,279)	-	-
Total debt issues	<u>\$ (5,981,924)</u>	<u>(8,412,398)</u>	<u>(33,094)</u>	<u>(491,202)</u>	<u>(1,490,514)</u>	<u>(1,396,385)</u>	<u>(5,001,203)</u>

December 31, 2018

	Book value	Expected cash flows					
		Total	2 months or less	2 months to 1 year	1 to 2 years	2 to 3 years	More than 3 years
Forwards on exchange rate	\$ (6,848)	(6,848)	(45)	(6,803)	-	-	-
Futures on commodities	(96,202)	(96,202)	-	(95,892)	(310)	-	-
	<u>(103,050)</u>	<u>(103,050)</u>	<u>(45)</u>	<u>(102,695)</u>	<u>(310)</u>	<u>-</u>	<u>-</u>
Bank loans in MXN	<u>(426,190)</u>	<u>(495,849)</u>	<u>(7,334)</u>	<u>(45,123)</u>	<u>(443,392)</u>	<u>-</u>	<u>-</u>
Debt issues							
CEBURES HERDEZ 13	(1,994,279)	(2,810,910)	-	(162,182)	(162,182)	(162,182)	(2,324,364)
CEBURES HERDEZ 14	(199,789)	(215,421)	(2,785)	(212,636)	-	-	-
CEBURES HERDEZ 17	(1,991,316)	(3,584,816)	-	(186,449)	(186,449)	(186,449)	(3,025,469)
CEBURES HERDEZ 17-2	(995,833)	(1,351,409)	(14,377)	(82,261)	(100,615)	(104,501)	(1,049,655)
CEBURES HERDEZ 18	(996,070)	(1,230,541)	(20,782)	(69,920)	(90,896)	(1,048,943)	-
Total debt issues	<u>\$ (6,177,287)</u>	<u>(9,193,097)</u>	<u>(37,944)</u>	<u>(713,448)</u>	<u>(540,142)</u>	<u>(1,502,075)</u>	<u>(6,399,488)</u>

The Group has account payable balances of \$335,464 and \$328,511 as at December 2019 and 2018, respectively, for discount of documents of account payable with Fideicomiso AAA Herfin, which is primarily intended to promote the economic development thereof.

iii) *Market risk*

Market risk is the risk that changes in market prices - such as foreign exchange rates, interest rates and materials costs - affect the Group's income or the value of its holdings of financial instruments. The purpose of market risk management is to manage and control market risk exposure within acceptable parameters, while optimizing the profitability.

The Group sells and buys derivatives and also incurs on financial liabilities to manage market risks. All such transactions are carried out within the guidelines set by the Risk Management Committee. Generally, the Group seeks to apply hedge accounting to mitigate volatility in income statement.

It is noteworthy that Grupo Herdez also has the risk of price changes in raw materials reason why the Company operates with future derivatives.

*Currency risk*

The Group is exposed to currency risk to the extent that there is a mismatch between the currencies in which sales, purchases and loans are denominated and the functional currency of the Group, which is the Mexican peso. The foreign currency in which these transactions are mainly denominated is the U.S.A dollar (USD).

Through hedging, the Group protects its estimated exposure to variations in exchange rates with respect to purchases projected with suppliers, denominated in foreign currency. The Group uses "forwards" exchange rate contracts to hedge its currency risk, most with maturities of less than one year as from the reporting date.

In respect to other monetary assets and liabilities denominated in foreign currencies, the Group's policy is to ensure that its net exposure is kept to an acceptable level by buying or selling foreign currencies at exchange rates of transactions in cash or "spot" to cover incidentals in the short-term.

*Exposure to currency risk*

The summary quantitative data about the Group's exposure to currency risk as reported to the Management of the Group is as follows.

	December 31, 2019		December 31, 2018	
	MXN	USD	MXN	USD
Cash, trade receivables and derivative financial instruments	\$ 527,813	27,967	739,717	37,632
Trade payable and notes payable	( 757,569 )	( 40,141 )	( 496,801 )	( 25,274 )
Net exposure	\$ ( 229,756 )	( 12,174 )	\$ ( 242,916 )	12,358

The following significant exchange rates have been applied during the year:

	Average exchange rate		Exchange rate at December 31,	
	2019	2018	2019	2018
U.S. dollar	19.2605	19.2402	18.8727	19.6566

#### Sensitivity analysis

A reasonably possible strengthening (weakening) of the Mexican peso and the US dollar, against all other currencies as at December 31, 2019 and 2018 would have affected the measurement of financial instruments denominated in a foreign currency, equity and income statement by the amounts shown below. This analysis assumes that all other variables, particularly on interest rates, remain constant and ignores any impact of forecast sales and purchases.

	Income statement		Equity, net of tax	
	Strengthening	Weakening	Strengthening	Weakening
<u>December 31, 2019</u>	19.8163	17.9291		
USD (5% Movement)	(241,244)	218,268	8,042	(8,042)
<u>December 31, 2018</u>	20.6394	18.6737		
USD (5% Movement)	255,062	230,770	8,502	(8,502)

#### Exposure to currency risk on financial liabilities

As of December 31, 2019 and 2018, there was no current position of financial liabilities in foreign currency.

#### Exposure to the exchange rate risk of derivative financial instruments

	Book value	
	2019	2018
Derivative financial instruments		
Forwards on exchange rate	\$ (15,357)	\$ (6,848)
Futures on commodities	165,260	(96,202)
Total	\$ 149,903	\$ (103,050)

The next table, shows a sensitivity analysis about assets and derivative liabilities and non-derivative instruments denominated in foreign currencies as at December 31, 2019 and 2018, if the Mexican peso increases or decreases +/- \$2.00, +/- \$3.50 , showing the changes applicable in exposure to this risk:

#### Derivative financial instruments

##### December 31, 2019

	Increase		Decrease	
	\$ 3.50	\$ 2.00	\$ (2.00)	\$ (3.50)
Derivative Financial Instruments				
Forwards on exchange rate	154,206	88,117	(88,117)	(154,206)
Futures on commodities	116,388	66,508	(66,508)	(116,388)
Total	270,594	154,625	(154,625)	(270,594)

##### December 31, 2018

	Increase		Decrease	
	\$ 3.50	\$ 2.00	\$ (2.00)	\$ (3.50)
Derivative Financial Instruments				
Forwards on exchange rate	118,109	64,538	(78,318)	(131,889)
Futures on commodities	(17,109)	(9,788)	9,788	17,109
Total	101,000	54,750	68,530	114,780

#### Interest rate risk

The Group adopts a policy of ensuring that its exposure to interest rate fluctuations on loans to be at a fixed rate and not variable rate. This is through a concentration of interest rate hedge operations (swaps).

In addition, the Group is exposed to fluctuations in rates on financial liabilities: Bank debt and debt issues.

#### Exposure to interest rate risk

The interest rate profile of the Group's interest-bearing financial instruments reported to the management of the Group is as follows, without considering hedging operations:

	Nominal amount	
	2019	2018
Fixed-rate instruments		
Financial liabilities in MXP	(4,000,000)	(4,000,000)
Variable-rate instruments		
Financial liabilities in MXP	(4,000,000)	(2,630,000)

### Sensitivity analysis of the amortizable cost of financial instruments

In the case of financial liabilities, which amount to \$4,000,000 and accrue a fixed interest rate, was determined that the amortized cost sensitivity to changes in the levels of interest rates is null, since there is no contingency that contractually modifies the agreed interest rate (fixed) and, therefore, that affects the amortizable cost of these liabilities.

With regard to liabilities whose interest payments are variable to changes in the levels of market interest rates, the sensitivity was estimated to parallel changes in the market reference rates (TIIE) on the interest paid in the reporting period. The sensitivity exercise consisted of determining the impact on the interest amount that would have been paid during 2019 with the financial liabilities at the reporting date and paid interests, with scenarios of parallel changes of: +/- 50 base points and +/- 100 base points <sup>1</sup>.

#### December 31, 2019

	Increase		Decrease	
	+100 pb	+ 50 pb	- 50 pb	-100 pb
Financial liabilities				
CEBURES HERDEZ 17-2	10,139	5,069	( 5,069)	( 10,139)
CEBURES HERDEZ 18	10,111	5,056	( 5,056)	( 10,111)
Total	20,250	10,125	( 10,125)	( 20,250)

#### December 31, 2018

	Increase		Decrease	
	+100 pb	+ 50 pb	- 50 pb	-100 pb
Financial liabilities				
Bank loans in MXP	7,961	3,980	( 3,980)	( 7,961)
CEBURES HERDEZ 14	4,044	2,022	( 2,022)	( 4,044)
CEBURES HERDEZ 17-2	10,111	5,056	( 5,056)	( 10,111)
CEBURES HERDEZ 18	4,667	2,333	( 2,333)	( 4,667)
Total	26,783	13,391	( 13,391)	( 26,783)

<sup>(1)</sup> It should be considered that the Increase and Decrease is regarding to the financial liability value, whereby an increase will mean a higher liability.

As at December 31, 2019 and 2018, the Group did not have a current position of derivative financial instruments exposed to Libor interest rate.

*Fair value sensitivity analysis for derivative financial instruments*

The Group is exposed to the rate risk of the different financial instruments held, a sensitivity analysis for each of them is shown below:

*Swap on interest rates*

## Local rate

December 31, 2019

	Increase		Decrease	
	+100 pb	+ 50 pb	- 50 pb	-100 pb
Derivative financial instruments				
Swaps on interest rate in MXP	19,593	9,842	( 9,936)	( 19,969)

December 31, 2018

	Increase		Decrease	
	+100 pb	+ 50 pb	- 50 pb	-100 pb
Derivative financial instruments				
Swaps on interest rate in MXP	21,109	10,684	( 10,954)	( 22,190)

*Currency forwards*

In accordance with the valuation model on currency forwards, part of the inputs are the local rate and foreign rate, these instruments are exposed to the fluctuation in those rates; therefore, the next table, shows a sensitivity analysis for each rates: (local or implicit rate and foreign rate):

## Local rate

December 31, 2019

	Increase		Decrease	
	+ 100 pb	+ 50 pb	- 50 pb	- 100 pb
Derivative financial Instruments				
Forwards on exchange rate	1,913	958	( 961)	( 1,926)

December 31, 2018

	Increase		Decrease	
	+ 100 pb	+ 50 pb	- 50 pb	- 100 pb
Derivative financial Instruments				
Forwards on exchange rate	1,970	987	( 991)	( 1,985)



## Foreign rate (Libor)

December 31, 2019

	Increase		Decrease	
	+10 pb	+ 5 pb	- 5 pb	-10 pb
Derivative Financial Instruments				
Forwards on exchange rate	(192)	(96)	96	192

December 31, 2018

	Increase		Decrease	
	+10 pb	+ 5 pb	- 5 pb	-10 pb
Derivative Financial Instruments				
Forwards on exchange rate	(200)	(100)	100	200

*Risk of raw material prices fluctuation*

The Group is exposed to the risk from the fluctuating prices of raw material; therefore, a sensitivity analysis was performed on the instruments that are affected by this risk considering scenarios of +/- 10% and +/-15%.

December 31, 2019

	Increase		Decrease	
	+15%	+10%	-10%	-15%
Derivative Financial Instruments				
Futures on commodities	175,665	117,110	(117,110)	(175,665)

December 31, 2018

	Increase		Decrease	
	+15%	+10%	-10%	-15%
Derivative Financial Instruments				
Futures on commodities	152,115	101,410	(101,410)	(152,115)

*Capital management*

The Group's policy is to maintain capital basis so as to maintain the investor, creditor and market confidence and to sustain future development of the business. The Board of Directors also monitors the returns on capital and as well as the level of dividends distributed to the stockholders of ordinary shareholders.

The Group monitors the Company performance by using key financial indicators that measure the margins of the income statement, net leverage, interest rate hedging, returns on capital and returns on equity investments.

During the reporting periods, there were no changes in the approach to the Group's policies on capital management.

The Group and its subsidiaries are not subject to externally tax capital requirements except what is mentioned in the note 14.

Periodically, the Group purchases its own shares on the Mexican Stock Exchange; the timing of such purchases depends on market situation. Buying and selling decisions are made by Management. The Group does not have a defined specific plan to repurchase shares.

Company Management has established the following rules for management of financial and capital risks:

- Not to reduce stockholders' equity to under \$10,000,000.
- Debt and its cash cost net (2) must not exceed than 3.5 times the EBITDA (1) as at December 31, 2019.
- Not to reduce interest hedge (EBITDA/net financing expenses) to less than 3 times.

<sup>(1)</sup> EBITDA – Operating Income plus depreciations, amortizations and other virtual parties.

<sup>(2)</sup> It is equal to the aggregate of bank loans and long-term debt less cash and cash equivalents.

## 7. Related parties

### *Parent and ultimate controlling party*

As mentioned in note 1, the Group is a subsidiary of Hechos con Amor, S. A. de C. V., which belongs to a group of investors that exercises control over it and with which there is a relationship, it is the main holding Company with 51% of the Group shares. The remaining 49% of the shares is owned by numerous stockholders.

*Related party transactions*

The main balances of accounts receivable and payable with related parties are shown below:

	2019		2018	
	Debtor	Creditor	Debtor	Creditor
Holding company:				
Hechos Con Amor, S. A. de C. V.	\$ 1,104	-	-	(4,949)
Joint ventures:				
Megamex Foods LLC	154,526	-	186,015	-
Intercafé, S. A. de C. V.	-	(9,735)	7,781	-
Avomex Inc.	1,000	-	438	-
Associated companies:				
Incubadora Orgánica, S. A. de C. V.	68,331	-	5,083	-
Other related parties:				
McCormick and Company, Inc.	-	(22,176)	-	(16,549)
Barilla G. e. R. Fratelli, S. p. A.	-	(31,544)	-	(21,388)
Barilla America Inc.	-	(719)	-	(2,557)
Suministradora de Combustibles y Lubricantes de Puerto Madero, S. A. de C. V.	4,860	-	-	(4,464)
Desc Corporativo, S. A. de C. V.	-	(2,680)	-	(2,434)
Fideicomiso AAA Herfin Nacional Financiera SNC	317	-	-	(1)
Herflot, S. A. de C. V.	-	(890)	-	(738)
Fábrica de Envases del Pacífico, S. A. de C. V.	145	-	145	-
Blemer, S. A. de C. V.	16,484	-	10,724	-
Ubongo, S. A. P. I. de C. V.	8	-	5,275	-
El Lado Suave, S. A. de C. V.	-	(4,939)	-	-
Others, neto	530	(4,749)	13,399	(2,254)
	<u>\$ 247,305</u>	<u>(77,432)</u>	<u>228,860</u>	<u>(55,334)</u>

During the years ended December 31, 2019 and 2018, operations conducted with related parties which were performed at market value are shown in the next page.

	2019	2018
<b>Holding company:</b>		
Lease expenses	\$ (48,426)	(48,076)
Other income	290	-
<b>Joint venture:</b>		
Commissions on sales	\$ 14,757	13,319
Interest collected	1,009	2,242
Sales of finished goods and materials	1,153,484	982,237
<b>Associated companies:</b>		
Purchase of materials	\$ (614,906)	(571,881)
Lease income	1,500	1,500
Other income	988	-
<b>Other related parties:</b>		
Lease expenses	\$ (72,509)	(49,211)
Interests earned	604	20
Royalties paid <sup>(1)</sup>	(348,278)	(325,073)
Commissions on sales	802	
Administrative services paid	(38,721)	(27,103)
Fuel purchase <sup>(2)</sup>	(97,219)	(182,249)
Payments for import of products <sup>(3)</sup>	(203,961)	(76,497)
Sale of finished goods and materials	443,663	443,294
Other expenses, net	(1,777)	(1,013)

<sup>(1)</sup> Payment for the use of trademarks McCormick and Barilla to McCormick and Company, Inc. and Barilla G. e. R. Fratelli, S. p. A.

<sup>(2)</sup> Purchases performed to the fuel terminal, mainly for the tuna fishing fleet to Suministradora de Combustibles y Lubricantes de Puerto Madero, S. A. de C. V.

<sup>(3)</sup> Increase in French's, Frank's and spices lines.

### Key management personnel compensation

The key management members received the following compensations, which are included in personnel costs under general expenses in the corresponding consolidated statements of income.

	2019	2018
Short and long-term direct benefits	\$ 31,049	\$ 46,710
Termination benefits	13,842	8,078
	<u>\$ 44,891</u>	<u>\$ 54,788</u>

## 8. Inventories

Inventories are comprised as follows:

	2019	2018
Finished goods	\$ 2,498,055 <sup>(1)</sup>	\$ 2,403,665 <sup>(1)</sup>
Semi-finished goods	610	1,012
Raw materials and packaging materials	939,999 <sup>(2)</sup>	744,378 <sup>(2)</sup>
Materials held by contract manufacturers or consignee and goods in transit	374,058	308,263
Spare parts warehouse	178,250	170,082
Total	<u>\$ 3,990,972</u>	<u>\$ 3,627,400</u>

Turnover of spare parts inventory is below 365 days (average 284 days), therefore, its cost of goods sold application is handled based on consumption.

<sup>(1)</sup> As of December 31, 2019, and 2018, the Company has recorded amounts of \$39,444 and \$41,901 for the allowance for obsolete inventory and the valuation allowance for finished goods, respectively.

<sup>(2)</sup> As of December 31, 2019, and 2018, the Company has recorded amounts of \$11,491 and \$17,174 for the allowance for obsolete inventory of raw and packaging materials, respectively.

## 9. Accounts receivable

Accounts receivable consist of the following:

	2019	2018
Customers	\$ 3,263,968	\$ 2,920,464
Impairment loss on trade receivables	90,923	25,020
	3,173,045	2,895,444
Debtors	141,493	204,712
Accounts receivable – Net	<u>\$ 3,314,538</u>	<u>\$ 3,100,156</u>

## 10. Property, machinery and equipment

At December 31, 2019 and 2018, property, machinery and equipment are comprised as shown in the following table:

	Balance at December 31, 2018	Additions	Disposals	Transfers	Reserve application	Others	Balances at December 31, 2019
Building	\$ 2,763,021	10,184	(6,412)	62,609	(44,514)	3,640	2,788,528
Machinery and tools	4,269,496	250,442	(53,910)	166,121	(51,387)	(30,350)	4,550,412
Fishing equipment	1,538,768	131,773	(164,904)	-	-	-	1,505,637
Office furniture and equipment	187,028	12,398	(2,838)	8,997	(294)	-	205,291
Stowing and transportation equipment	647,551	4,277	(20,666)	4,477	(1,066)	(6,880)	627,693
Electronic data processing equipment	280,490	14,232	(3,420)	47,155	(56)	-	338,401
Original investment (OI)	9,686,354	423,306	(252,150)	289,359	(97,317)	(33,590)	10,015,962
Accumulative depreciation	(4,743,271)	(480,698)	107,893	-	86,379	(5,453)	(5,035,150)
OI less depreciation	4,943,083	(57,392)	(144,257)	289,359	(10,938)	(39,043)	4,980,812
Land	379,074	10,138	-	-	-	1,662	390,874
Allowance for impairment	(89,813)	-	-	-	10,938	-	(78,875)
Impairment loss	(10,667)	-	-	-	-	-	(10,667)
Construction in progress	226,915	346,045	(25,455)	(289,359)	-	-	258,146
Total fixed assets	\$ 5,486,321	298,791	(169,712)	-	-	(37,381)	5,540,290

	Balance at December, 31, 2017	Additions	Disposals	Transfers	Reserve	Reserve applications	Balances at December 31, 2018
Building	\$ 2,645,484	2,122	(27,331)	145,083	(2,337)	-	2,763,021
Machinery and tools	3,812,814	86,482	(43,876)	413,080	6,216	(5,220)	4,269,496
Fishing equipment	1,514,615	123,223	(107,602)	8,532	-	-	1,538,768
Office furniture and equipment	176,386	9,420	(482)	1,781	(49)	(28)	187,028
Stowing and transportation equipment	630,522	7,069	(3,207)	13,167	-	-	647,551
Electronic data processing equipment	256,946	9,456	(1,087)	17,264	-	(2,089)	280,490
Original investment (OI)	9,036,767	237,772	(183,585)	598,907	3,830	(7,337)	9,686,354
Accumulative depreciation	(4,348,077)	(462,298)	59,726	-	1,240	6,138	(4,743,271)
OI less depreciation	4,688,690	(224,526)	(123,859)	598,907	5,070	(1,199)	4,943,083
Land	375,441	7,383	(3,750)	-	-	-	379,074
Allowance for impairment	(91,012)	-	-	-	-	1,199	(89,813)
Impairment loss	(10,667)	-	-	-	-	-	(10,667)
Construction in progress	580,255	251,326	(5,759)	(598,907)	-	-	226,915
Total fixed assets	\$ 5,542,707	34,183	(133,368)	-	5,070	-	5,448,592

During 2019 depreciation expense for \$480,698, \$291,310 was included in cost of sales, \$177,033 in selling expenses and \$12,355 in administrative expenses.

During 2018 depreciation expense for \$462,298, \$288,601 was included in cost of sales, \$162,063 in selling expenses and \$11,634 in administrative expenses.

#### *Allowance for unused fixed assets*

During 2014, as a result of the replacement occurred for the plant "La Corona", located on Los Mochis, Sinaloa, an allowance for unused fixed assets was recognized by the Group arising \$142,338 in relation with plant and equipment. The effect was charged within other expenses. During 2017, \$9,259 was applied to the reserve, leaving an amount of \$91,012 as of December 31, 2017. During 2018, \$1,199 was applied to the reserve, leaving an amount of \$89,813 as of December 31, 2018. During 2019, \$10,938 was applied to the reserve, leaving an amount of \$78,875 as of December 31, 2019.

#### *Construction in progress*

During 2019, the Group developed projects that will increase production capacity for \$346,045, which are estimated to be completed in 2020; in addition, the outstanding estimated investment related to such constructions in progress amounts to \$314,695.

## 11. Intangible assets and goodwill

Intangible assets as at December 31, 2019 and 2018, include the following:

	Goodwill	Patents and trademarks	Licenses	Computer programs	Defined life intangible assets <sup>(1)</sup>	Total intangible assets
Balance at December 31, 2017	\$ 4,259,263	1,923,735	313,976	148,133	138,377	6,783,484
Additions	-	-	-	23,040	3,985	27,025
Disposals	-	-	-	(460)	-	(460)
Amortization for the period	-	-	(18,319)	(14,682)	(24,581)	(57,582)
Balance at December 31, 2018	\$ 4,259,263	1,923,735	295,657	156,031	117,781	6,752,467
Additions <sup>(2)</sup>	-	200,000	7,003	29,284	147,451	383,738
Acquisition of business <sup>(3)</sup>	296,439	-	-	-	-	296,439
Amortization for the period	-	-	(19,535)	(20,242)	(20,162)	(59,939)
Balance at December 31, 2019	\$ 4,555,702	2,123,735	283,125	165,073	245,070	7,372,705

<sup>(1)</sup> Corresponds to non-competence contracts, developed technology, customer relationships and lease rights.

<sup>(2)</sup> Corresponds to the acquisition of the Moyo brand on November 29, 2019 (see note 15).

<sup>(3)</sup> Corresponds principally to the acquisition of Cielito Querido Café on November 29, 2019 (see note 15).

#### *Amortization*

Amortization of intangible assets for the years ended December 31, 2019 and 2018 was recognized under cost of sales, administrative and selling expenses in the consolidated statement of income.

*Impairment testing for cash-generating units containing goodwill*

For the purposes of impairment testing, goodwill has been allocated to the Group's cash-generating units and monitoring at operating segments level (operating division).

The following is a summary of goodwill assigned to each operating segment:

	Balance as at December 31,	
	2019	2018
Goodwill related to preserves segment	\$ 2,883,575	\$ 2,883,575
Goodwill related to frozen segment <sup>(1)</sup>	1,672,127	1,375,688
	<u>\$ 4,555,702</u>	<u>\$ 4,259,263</u>

<sup>(1)</sup> Include \$1,270,788 of Group Nutrisa.

Cash flows subsequent to that period are extrapolated using the estimated growth rates shown below, which do not exceed the average long-term growth rate for the business in which each CGU and/or segment operates.

The key assumptions used in estimation of value in use in 2019, are as follows:

	Preserves segment	Frozen segment
Gross margin	36%	64%
Long-term growth rate	3.65%	3.65%
Discount rate	9.94% <sup>(1)</sup> y 11.30% <sup>(2)</sup>	11.28%

<sup>(1)</sup> Applied rate for tuna fish CGU.

<sup>(2)</sup> Applied rate for the rest of preserve CGUs.

The key assumptions used in estimation of value in use in 2018, are as follows:

	Preserves segment	Frozen segment
Gross margin	37%	64%
Long-term growth rate	3.56%	3.56%
Discount rate	9.96% <sup>(1)</sup> y 11.60% <sup>(2)</sup>	11.60%

<sup>(1)</sup> Applied rate for tuna fish CGU.

<sup>(2)</sup> Applied rate for the rest of preserve CGUs.

These assumptions have been used for each CGU.

The gross margin has been budgeted based on past performance and on development expectations of each market.



As at December 31, 2019, the discount rate corresponds to a pre-tax measure that is estimated based on past experience and the weighted average cost of capital of the industry that is based on a possible range of debt leveraging of 30.3 percent at a market interest rate of 3.75 percent and the Tuna Fish CGU is based on a possible range of debt leverage of 44.7 percent at a market interest rate of 3.75 percent.

It was included five to ten years of cash flows in the model of discounted cash flow. A long-term growth rate in perpetuity was determined based on the estimate of the administration of long-term compound annual growth rate that, in the opinion of Management, was consistent with the assumption that it would make a market participant.

Budgeted EBITDA was based on expectations of future outcomes taking into account past experience, adjusted for anticipated revenue growth. Revenue growth was projected taking into account the average growth levels experienced over the past five, seven or ten years and the estimates sales volume and price growth for the next five, seven or ten years according to the line of business. It was assured that sales prices would grow at a constant margin above forecasted inflation over the next five or ten years, in line with information obtained from external brokers who publish a statistical analysis of market trends.

## 12. Equity-accounted investees

At December 31, 2019 and 2018, the investments in associates for \$7,186,573 and \$6,971,663, respectively, corresponding to the investment in Megamex by \$6,618,802 and \$6,446,423, respectively, and other investments for \$567,771 and \$525,240, respectively (see note 13).

The Group's profit share for the year ended as at December 31, 2019 of its associated entities recognized by the equity method amounted to \$775,933 and as at December 31, 2018 to \$916,111.

## 13. Associated parties

Megamex Foods, LLC (Megamex) was incorporated on October 21, 2009 in the United States of America. Megamex is a joint venture between Hormel Foods Corporation and Authentic Specialty Foods Inc. (ASF), which is a subsidiary of Herdez Del Fuerte. The recognition of this investment is recognized under the equity method in the results of Authentic Specialty Foods Inc.

Megamex carries out the production, distribution and sale of a variety of Mexican products, mainly to supermarkets, food service, distributors, retailers and convenience stores. Some of the products marketed by Megamex are produced by Herdez Del Fuerte in Mexico.

The following table summarizes the consolidated Megamex financial information included in its consolidated financial statements. The following table reconciles the summary financial information with the book value of the participation of ASF:

	<b>2019</b>	2018
Non-current assets	\$ 10,895,906	\$ 10,774,325
Current assets	3,913,047	3,679,549
Non-current liabilities	549,574	541,420
Current liabilities	1,022,040	1,019,866
Net assets (100%)	<u>\$ 13,237,339</u>	<u>\$ 12,892,588</u>
Group's shares of net assets (50%)	<u>\$ 6,618,802</u>	<u>\$ 6,446,423</u>
Net sales	\$ 13,792,681	\$ 13,257,822
Interest income	1,237	1,034
Profit and total comprehensive income (100%)	<u>\$ 1,512,205</u>	<u>\$ 1,774,374</u>
Group's share of earnings and other comprehensive income (50%)	<u>\$ 756,118</u>	<u>\$ 887,204</u>
Received dividends from MegaMex Foods	<u>\$ 426,837</u>	<u>\$ 560,491</u>

As at December 31, 2019 and 2018, the Group received dividends from its associate, Megamex Foods, LLC in the amounts of 22.5 and 30 million dollars, respectively.

The following is a summary of the financial information pertaining to the main associated entities recognized by the equity method, including the Company's shareholding percentage:

December 31, 2019

	Share holding	Investment
Incubadora Orgánica, S. A. de C. V.	50%	\$ (7,045)
Intercafé, S. A. de C. V.	50%	67,268
Fábrica de Envases del Pacífico, S. A. de C. V.	50%	220,692
		<u>\$ 280,915</u>

December 31, 2018

	Share holding	Investment
Incubadora Orgánica, S. A. de C. V.	50%	\$ 1,701
Intercafé, S. A. de C. V.	50%	55,449
Fábrica de Envases del Pacífico, S. A. de C. V.	50%	217,726
Ubongo, S. A. P. I. de C. V.	50%	30,656
		<u>\$ 305,532</u>

Other investments are comprised as follows:

**December 31, 2019**

	Investment
AUA Private Equity Parallel Fund, LP *	\$ 105,536
AUA Indulge Corp	161,344
Anteris Capital Venture Lending Fund I, LP	18,004
Yaax Capital, LP	1,972
	\$ 286,856

**December 31, 2018**

	Investment
AUA Private Equity Parallel Fund, LP *	\$ 71,897
AUA Indulge Corp	136,208
Anteris Capital Venture Lending Fund I, LP	11,603
	\$ 219,708

\* The Group has capital committed to investment of 12 million Mexican pesos as of 2022.

## 14. Loans and liabilities

This note provides information about the contractual terms of the Group's loans and liabilities bearing interest, which are valued at amortized cost in order to provide more information about Group's exposure to interest rate, foreign currency and liquidity risk (see note 6 ii)).

Notes payable as well as short- and long- term debts are analyzed as shown below:

	2019	2018
Bank loan in Mexican pesos with HSBC, maturing on May 15, 2020, with inter-est payable at the variable rate TIIE 28 plus 1.45%. Loan paid on October 30, 2019.	\$ -	\$ 380,000
Bank loan in Mexican pesos with HSBC, maturing on May 15, 2020, with inter-est payable at the variable rate TIIE 28 plus 1.45%. Loan paid on October 30, 2019.	-	50,000
Bank loan in Mexican pesos with Bancomext, maturing on October 29, 2029, with interest payable at the variable rate TIIE 91 plus 1.40%. Capital payments to begin in 2022.	2,000,000	-
Domestic bonds in Mexican pesos, maturing on June 17, 2021, with interest payable in monthly at the TIIE 28 plus 0.40%	1,000,000	1,000,000
Domestic bonds in Mexican pesos, maturing on November 4, 2019, (paid in the same date) with interest payable in monthly at the TIIE 28 plus 0.35%	-	200,000
Domestic bonds in Mexican pesos, maturing on May 26, 2022, with interest payable in monthly at the TIIE 28 plus 0.77%	1,000,000	1,000,000
Domestic bonds in Mexican pesos, maturing on May 20, 2027, with interest payable semiannual at the rate of 9.22%	2,000,000	2,000,000
Carried forward	\$ 6,000,000	\$ 4,630,000

	2019	2018
Brought forward	\$ 6,000,000	\$ 4,630,000
Domestic bonds in Mexican pesos, maturing on November 3, 2023, with interest payable semiannual at the rate of 8.02%	2,000,000	2,000,000
Total short- and long-term notes payable	8,000,000	6,630,000
Less current installments	-	200,000
Documentos por pagar a largo plazo, excluyendo vencimientos circulantes	8,000,000	6,430,000
Long term notes payable, excluding current installments	( 39,627 )	( 26,523 )
Cost of issuance of unamortized traded notes (domestic bonds and bank loans)	\$ 7,960,373	6,403,477

#### Long-term maturity - Net, excluding current installments

The main covenants are listed as follows:

- Not to reduce stockholders' equity to under \$10,000,000.
- Debt and its cash cost net must not exceed than 3.5 times the EBITDA as at December 31, 2019.
- Not to reduce interest hedge (EBITDA/net financing expenses) to less than 3 times.

At closing of December 2019, the Company has committed lines of credit in the amount of \$3,000,000 signed with financial institutions rated AAA. Interest is payable at the TIIE interest rate plus an applicable margin.

#### Long-term debt

At December 31, 2019 and 2018, the long-term debt is comprised as follows:

	2019	2018
Commercial sale contract and franchise rights	\$ 7,644 <sup>(1)</sup>	\$ 34,782 <sup>(1)</sup>
	\$ 7,644	\$ 34,782

<sup>(1)</sup> Franchise rights of Nutrisa and Alimentos Benefits ending amortization greater than one year.

<sup>(2)</sup> It relates to the quarterly payments made for the acquisition of machinery and equipment which have quarterly basis and it includes an agreement with GE capital with interest payable rate of 6.5% and a contract with Tetra Pak. Also included are Nutrisa franchise rights pending amortization greater than one year.

## 15. Acquisition of businesses and intangibles

On November 29, Grupo Herdez acquired Cielito Querido Café and the Moyo brand for a combined amount of \$505 million of Mexican pesos. These acquisitions are part of the growth and strengthening strategy of the Group's portfolio of brands. Together with Nutrisa and Lavazza, the Group now has more than 600 points of sale throughout the country.

Derived from the Cielito Querido Café Business Acquisition carried out in 2019, the Group is in the measurement period of the accounting for said acquisition, a quantification that will not extend beyond one year from the acquisition date according to the Second Amending Agreement dated November 28, 2019 of the stock purchase contract and considering the Contract for the Provision of Transitional Services in force during the year 2020, in accordance with IFRS 3 Business Combination regarding the measurement period.

For the month ended December 31, 2019, Cielito Querido Café contributed revenue of \$33,327 to the Group's results. If the acquisition had occurred on January 1, 2019, management estimates that consolidated revenue would have been \$22,796,879.

## 16. Lease

### *Impacts on financial statements*

As of the date of transition to IFRS 16, the Group recorded \$806 million of lease liabilities and \$807 million of right-of-use assets, with no effect on stockholders' equity.

When measuring lease liabilities, the Group discounted the payments using a discount rate as of January 1, 2019. The weighted-average rate applied was 11%.

### *Leases as lessee*

The Group leases principally property and transportation equipment. Information about leases for which the Group is lessee is presented below.

#### a) *Right-of-use assets*

	<b>Balance at January 1, 2019</b>	<b>Additions</b>	<b>Disposals</b>	<b>Depreciación</b>	<b>Others</b>	<b>Balance at December 31, 2019</b>
Property	\$ 684,223	360,283	( 320,477 )	-	278,635	1,002,664
Transportation equipment	122,725	49,272	( 23,175 )	-	11	148,833
Right-of-use	806,948	409,555	( 343,652 )	-	278,646	1,151,497
Property	-	( 19,640 )	17,232	( 258,668 )	24,773	( 236,303 )
Transportation equipment	-	( 3,655 )	6,236	( 53,265 )	( 1 )	( 50,685 )
Accumulative depreciation	-	( 23,295 )	23,468	( 311,933 )	24,772	( 286,988 )
Total Right-of-use	\$ 806,948	386,260	( 320,184 )	( 311,933 )	303,418	864,509

b) *Amounts recognized in income statement*

As a result of the initial enforcement of IFRS 16, the Group recognized depreciation, interest expense, instead of rental payment expense, as well as the corresponding tax provision and, if applicable, the corresponding non-controlling interest. As of December 31, 2019, the Group recognized the following figures:

	<b>Figures as of December 31, 2019</b>
Record of depreciation expense	\$ 286,988
Total lease payments	( 467,030 )
Record of interest expense	89,013
Expenses relating to short-term leases	7,586
Expenses relating to leases of low-value assets, excluding short-term leases of low value assets	121,071
Exchange fluctuation record	(839)
Tax provision	11,265
Others	542

c) *Lease liabilities*

Lease liabilities and Interest to accrue, as of December 31, 2019 and 2018, were as follows:

	<b>Lease liability</b>	<b>Interest to accrue</b>	<b>Lease liability, net</b>
Balance at January1, 2019	\$ ( 1,176,561 )	369,16	( 807,397 )
Additions	( 705,592 )	298,587	( 407,005 )
Disposals	635,693	( 292,028 )	343,665
Others	( 173,101 )	( 99,743 )	( 272,844 )
Exchange rate	2,194	1,001	3,195
Payments	338,373	( 89,013 )	249,360
Balance at December 31, 2019	\$ ( 1,078,994 )	187,968	( 891,026 )

## 17. Employee benefits

	2019	2018
Obligations in the statement of consolidated financial position arising from:		
Pension plan and seniority premiums:	\$ 453,826	( 350,847 )
Net defined benefit liability	( 263,824 )	( 168,946 )
Pension plan and seniority premiums:		
Net period cost	33,706	31,252
Actuarial losses recognized in the consolidated statement of comprehensive income for the period before income tax	69,143	17,685
Accumulative actuarial losses recognized in prior years in the consolidated statement of comprehensive income	\$ 72,448	\$ 3,305

### a) Employee benefits

Some entities of the Group offer their employees a pension plan of defined benefits in Mexico, on the basis of pensionable compensation and years of service of the employees. The Plan Assets (PA) that support these plans are held in trusts, foundations or similar institutions regulated under local laws and by each country's accepted practices, which also regulate the nature of the relationship between the Group and trustees (or equivalent) and their composition thereof.

The following is an integration of the PA defined benefit:

	2019	2018
Variable rent	\$ 44,573	\$ 44,480
Debt instrument	145,275	139,928
Fair value of plan assets	\$ 189,848	\$ 184,408

The amounts recognized in the consolidated statement of financial position, as at December 31, 2019 and 2018, are as follows:

	2019	2018
Defined benefit obligations	\$ ( 453,826 )	\$ ( 350,847 )
Fair value of PA	189,848	184,408
Variations in assumptions and adjustments	( 154 )	( 2,507 )
Net defined benefit liability	\$ ( 263,824 )	\$ ( 168,946 )

The changes in the defined benefit obligations during the years presented are as follows:

	<b>2019</b>	2018
As at January 1	\$ 350,847	\$ 347,827
Cost of current service	18,121	19,313
Financial cost	28,772	23,927
Actuarial losses	60,159	( 28,328 )
Benefits paid	( 4,073 )	( 11,892 )
	<hr/>	<hr/>
As at December 31	<u>\$ 453,826</u>	<u>\$ 350,847</u>

The entry in the PA fair value during the years presented are as follows:

	<b>2019</b>	2018
As at January 1	\$ 184,408	\$ 191,011
Real return on plan assets	16,420	7,569
Employer's contribution	-	200
Benefits paid from PA	( 10,980 )	( 14,372 )
	<hr/>	<hr/>
As at December 31	<u>\$ 189,848</u>	<u>\$ 184,408</u>

The amounts recognized in the consolidated statement of income are as follows:

	<b>2019</b>	2018
Cost of current service	\$ 18,120	\$ 19,313
Financial cost (a)	28,772	23,927
Expected return on PA (b)	( 13,186 )	( 11,988 )
	<hr/>	<hr/>
Net interest (a + b)	15,586	11,939
	<hr/>	<hr/>
Total included in personnel costs and expenses	<u>\$ 33,706</u>	<u>\$ 31,252</u>

The charge for the 2019 period of \$33,706 was included in the cost of sales for \$12,761, administrative expenses \$8,597 and selling expenses \$12,348.

The charge for the 2018 period of \$31,252 was included in the cost of sales for \$12,845, administrative expenses \$6,353 and selling expenses \$12,054.



b) *Defined benefit obligations*

i) *Actuarial*

The main variables used in the actuarial calculations were the following:

*Discount rate*

To determine the discount rate the actuary used a methodology in which a zero coupon government bond curve is constructed where each payment flow is discounted with the zero coupon rate, which are converted "Bootstrapping" to zero coupon bonds ("spot" rates) over a period from 6 months to 30 years. Each payment flow is discounted with the applicable "spot" zero coupon rate according to the time in which the payment is being made, then the discount rate represents the single rate whose present value of flows is equal to that obtained with the zero coupon rates, in this way, the recommended discount rate to determine the obligations at year-end 2019 and 2018 is 7.50% y 9.50% respectively.

*Long-term inflation rate*

Banco de México (Central Bank) established a goal for long-term inflation of 3.50%, which was considered for the valuation of the labor obligations.

*Salary increase rate*

Based on experience, it has been observe that the salary increases have been presented based on the annual inflation, thus a nominal rate of 4.50% was maintained, the same as in 2018.

*Expected return on plan assets*

The expected return rate on plan assets is consistent with the discount rate reported by the actuary and it was determined with the guidelines established in the most recent version of IAS 19.

See main actuarial variables assumptions used:

	2019	2018
Discount rate	7.50%	9.50%
Salary increase rate	4.50%	4.50%
Minimum wage increase rate	3.50%	-
Measurement and Update Unit (UMA) increase rate	-	3.50%
Long-term inflation rate	3.50%	3.50%

ii) *Sensitivity analysis*

Reasonably possible changes in the relevant actuarial assumptions at the balance sheet date, as long as other assumptions remain constant, would have affected the defined benefit obligation amounts included in the following table:

December 31, 2019

Seniority premium	Total	
	Increase	Decrease
<b>A. Defined benefit obligations</b>		
Discount rate (change of 1%)	\$ ( 5,744 )	6,599
Salary increase rate (change of 1%)	-	-
Future mortality (change of 1 year)	( 40 )	-

Pension plans	Total	
	Increase	Decrease
<b>A. Defined benefit obligations</b>		
Discount rate (change of 1%)	\$ ( 21,423 )	24,777
Salary increase rate (change of 1%)	25,285	( 22,187 )
Future mortality (change of 1 year)	( 635 )	691

December 31, 2018

Seniority premium	Total	
	Increase	Decrease
<b>A. Defined benefit obligations</b>		
Discount rate (change of 1%)	\$ ( 3,318 )	3,769
Salary increase rate (change of 1%)	255	( 299 )
Future mortality (change of 1 year)	45	( 42 )

Pension plans	Total	
	Increase	Decrease
<b>A. Defined benefit obligations</b>		
Discount rate (change of 1%)	\$ ( 15,316 )	17,536
Salary increase rate (change of 1%)	18,250	( 16,139 )
Future mortality (change of 1 year)	679	( 722 )

Although the analysis does not take account of the full distribution of cash flows expected under the plan, it does provide an approximation of the sensitivity of the assumptions shown.

## 18. Income taxes

### Income Tax (IT)

On December 11, 2013, a decree was published in the Official Gazette whereby several tax provisions were amended, supplemented, and repealed. This decree became effective as of January 1, 2014.

The Income Tax Law in force as of January 1, 2014 establishes an income tax rate of 30% for 2014 and beyond.

Further changes are set out in the scheme of deduction of expenditure for employee benefits in the Income Tax Law, IT on dividends, eliminating the simplified regime, changing the income tax rate, changes in the determination of the Employee Statutory Profit Sharing (ESPS) and the elimination of tax consolidation regime. For this reason, in 2014, the Group determined not to consolidate its taxable profit for income tax purpose.

Consolidated book and tax results differ mainly due to items taxed or deducted over time, differently for book and tax purposes, due to recognition of the effects of inflation for tax purposes and those items that only affect either book or tax results.

Following is a reconciliation of tax-consolidation-related income tax balances:

	Income tax liabilities	
	2019	2018
Opening balance at January 1 of every year	\$ 146,407	\$ 173,246
Increases:		
IT for loss on disposal of shares of subsidiaries	4,275	10,324
Decrease:		
Transfer to current liabilities	( 37,669) <sup>(1)</sup>	( 37,163) <sup>(1)</sup>
Closing balance at December 31	\$ 113,013	\$ 146,407

<sup>(1)</sup> This amount is included in the income tax payable.

### Amounts recognized in consolidated statement of income

The income tax expense, as at December 31, 2019 and 2018, are comprised as shown below:

	2019	2018
Current tax expense	\$ 1,134,618	\$ 957,462
Deferred tax expense	( 204,953 )	41,152
Total income tax	\$ 929,665	\$ 998,614

## Amounts recognized in other comprehensive income

	2019			2018		
	Before tax	Income tax effect	Net of tax	Before tax	Income tax effect	Net of tax
Remeasurements of defined benefit (liability) asset	\$ (49,930)	(7,621)	(57,551)	11,897	3,318	15,215
Foreign business-conversion effect	(184,215)	-	(184,215)	(43,594)	-	(43,594)
Derivate financial instruments	200,426	(58,207)	142,219	(103,180)	27,525	(75,655)
Valuation of investment funds	72,336	(21,701)	50,635	23,601	(7,080)	16,521
	<u>\$ 38,617</u>	<u>(87,529)</u>	<u>(48,912)</u>	<u>(111,276)</u>	<u>23,763</u>	<u>(87,513)</u>

## Effective tax rate reconciliation

The following table represents the reconciliation between the rates incurred and the effective IT rate:

	2019	2018
Income before taxes	\$ 3,153,708	3,422,373
Statutory rate	30%	30%
IT at the statutory rate	946,112	1,026,712
Plus (less) tax effect of permanent items:		
Inflationary effects	(6,471)	24,135
Results reported by associates and joint ventures, net of tax	(70,989)	(93,631)
Other permanent items, net <sup>(1)</sup>	48,641	10,268
Recognition of taxes from prior years	8,097	20,806
	925,390	988,290
IT for loss on disposal of shares of subsidiaries	4,275	10,324
Income tax recognized in income	<u>\$ 929,665</u>	<u>998,614</u>
Effective income tax rate	29%	29%

<sup>(1)</sup> Including non-deductible expenses and deferred asset cancelation from 2019 for \$67,617 (\$17,571 in 2018 of non-deductible expenses).

The main effects of temporary differences for which deferred income tax are analyzed are shown as follows:

*Movement in deferred tax balances*

	2019			2018		
	Asset	Liability	Net	Asset	Liability	Net
Deferred assets:						
Estimates and accruals	\$ 448,695	73,516	375,179	287,437	103,006	184,431
Tax losses	187,550	-	187,550	74,463	-	74,463
Investment in joint ventures	-	-	-	51,580	-	51,580
Employees benefits	35,477	-	35,477	25,175	-	25,175
Lease liabilities	267,308	-	267,308	-	-	-
Deferred tax asset	<u>\$ 939,030</u>	<u>73,516</u>	<u>865,514</u>	<u>438,655</u>	<u>103,006</u>	<u>335,649</u>

	2019			2018		
	Asset	Liability	Net	Asset	Liability	Net
Deferred liabilities:						
Inventories	\$ 14,321	80,177	( 65,856 )	17,076	49,929	( 32,853 )
Derivative financial instruments <sup>(1)</sup>	-	93,554	( 93,554 )	28,618	42,265	( 13,647 )
Prepayments	-	31,073	( 31,073 )	-	24,944	( 24,944 )
Other assets	-	134,375	( 134,375 )	-	109,168	( 109,168 )
Property, machinery and equipment, net	124,212	48,853	75,359	134,949	51,014	83,935
Right-of-use assets	-	259,353	( 259,353 )	-	-	-
Intangibles Nutrisa Trade-mark	-	300,360	( 300,360 )	-	300,864	( 300,864 )
Other trademarks	-	252,534	( 252,534 )	-	251,765	( 251,765 )
Deferred tax liability	<u>138,533</u>	<u>1,200,279</u>	<u>( 1,061,746 )</u>	<u>180,643</u>	<u>829,949</u>	<u>( 649,306 )</u>
Net deferred tax assets (liabilities)	<u>\$ 1,077,563</u>	<u>1,273,795</u>	<u>( 196,232 )</u>	<u>619,298</u>	<u>932,955</u>	<u>( 313,657 )</u>

<sup>(1)</sup> These effects are recorded as part of other comprehensive income.

The gross movement on deferred income tax is as follows:

	2019	2018
Opening balance	\$ ( 313,657 )	\$ ( 296,268 )
Valuation of financial instruments	( 79,907 )	20,445
Debit for components of other comprehensive income	( 7,621 )	3,318
Recorded in income statement	204,953	( 41,152 )
	<u>\$ ( 196,232 )</u>	<u>( 313,657 )</u>

Gross movement on the deferred tax asset and liability during the year is shown below:

Deferred assets	Estimates and provisions	Tax cost of joint venture shares	Employee benefits	Tax losses and incentives	Lease liabilities	Total
Balance at December 31, 2017	\$ 147,055	51,580	25,296	107,729 <sup>(1)</sup>	-	331,660
Credit for other comprehensive in-come components	-	-	3,318	-	-	3,318
Debit (credit) to statement of income	37,376	-	(3,439)	(33,266)	-	671
Balance as at December 31, 2018	184,431	51,580	25,175	74,463	-	335,649
Credit for other comprehensive in-come components	-	-	(7,621)	-	-	(7,621)
Debit (credit) to statement of income	190,748	(51,580)	17,923	113,087	267,308	537,486
Balance at December 31, 2019	\$ 375,179	-	35,477	187,550	267,308	865,514

Deferred liabilities	Inventories	Derivative financial instruments	Prepayments	Property, machinery and equipment	Intangible assets	Other assets	Right-of-use	Total
Balance at December 31, 2017	\$ (23,166)	(34,092)	(18,359)	102,606	(559,840)	(95,077)	-	(627,928)
Debit for other comprehensive income components	-	20,445	-	-	-	-	-	20,445
Debit (credit) to statement of income	(9,687)	-	(6,585)	(18,671)	7,211	(14,091)	-	(41,823)
Balance at December 31, 2018	(32,853)	(13,647)	(24,944)	83,935	(552,629)	(109,168)	-	(649,306)
Debit for other comprehensive income components	-	(79,907)	-	-	-	-	-	(79,907)
Debit (credit) to statement of income	(33,003)	-	(6,129)	(8,576)	(265)	(25,207)	(259,353)	(332,533)
Balance at December 31, 2019	\$ (65,856)	(93,554)	(31,073)	75,359	(552,894)	(134,375)	(259,353)	(1,061,746)

<sup>(1)</sup> Accumulated tax losses

	2019	Expiration date	2017	Expiration date
Accumulated tax losses expire as follows	\$ 625,167	2026-2029	\$ 248,211	2026-2028

*Unrecognized deferred tax assets*

At December 31, 2019, there was an unrecognized deferred tax assets of \$51,580 for temporary differences of \$171,933 related to intangible assets.

*Unrecognized deferred tax liabilities*

At December 31, 2019, there was a deferred tax liability of \$1,033,688 (\$953,719 in 2018) for temporary differences of \$3,949,597 (\$3,643,800 in 2018) related to investments in subsidiaries and joint ventures that were not recognized because the Company is able to control the timing of the reversal of the temporary difference associated with those investments, the liability is likely not be reversed in the foreseeable future.

## 19. Stockholders' equity and reserves

### a) Common shares

At December 31, 2019 and 2018, the Company's subscribed and paid-in capital stock totaled \$432,275, plus an increase of \$143,350, to express it in modified historical Mexican pesos, and is represented by 413,188,050 common nominative shares, with no par value.

In case of reduction of capital, the procedures established by the Income Tax Law (ITL) provide that any excess of stockholders' equity on the balance of the capital contributions is accorded the same tax treatment as dividends.

The Company decided to take the following measures in relation with the securities market outstanding shares:

- i) At the April 2019 Stockholders' meeting, the stockholders agreed on a maximum amount of \$1,000,000 of resources that the Company can set aside to repurchase own shares.

The stock repurchase fund showed its activity as follows:

	December 31, 2019		December 31, 2018	
	Number of shares	Amount	Number of shares	Amount
Purchases	(22,221,473)	(900,779)	(6,937,642)	(280,747)

At December 31, 2019 and 2018, the Company held 32,610,441 and 10,388,968 treasury shares, respectively.

b) *Nature and purpose of reserves*

*Reserve for repurchase of shares*

The Company may acquire shares representing its capital through the stock market in which it operates at the current market price, without giving effect to the prohibition as set forth in the first paragraph of Article One Hundred Thirty Four of the Mexican Corporate Law (Ley General de Sociedades Mercantiles, LGSM) and complying with the requirements of the Securities Market Law, the general provisions to that effect issued by the National Banking and Securities Commission and other applicable laws.

*Legal reserve*

In accordance with the LGSM, five percent of net income for the year must be appropriated to the statutory reserve, until it reaches one-fifth of capital stock. As of December 31, 2019 and 2018, the statutory reserve amounts to \$141,862 and has reached the required amount.

c) *Capital decreases*

On October 1, 2019, a purchase agreement was entered for the remaining 50% of the shares of the capital stock owned by Saben a Cine, S. A. P. I. de C. V.; Operadora Comercial de Desarrollo, S. A. de C. V. was entered as the selling party and Herdez del Fuerte, S. A. de C. V. and Herdez, S. A. de C. V. as the purchasing parties, decreasing the minority interest in the amount of \$13,068 that belonged to Operadora Comercial de Desarrollo, S. A. de C. V.

d) *Dividends*

On December 23, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$65,000 were decreed.

On November 14, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$20,000 were decreed.

On October 21, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$100,000 were decreed.

On September 17, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$30,000 were decreed.

On August 29, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$100,000 were decreed.

On July 30, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$66,815 were decreed.

On June 27, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$30,000 were decreed.

On April 15, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$71,603 were decreed.



On April 25, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$100,000 were decreed.

At the Ordinary General Meeting of Shareholders held on April 25, 2019, it was agreed to decree dividends of \$1.10 per share, the dividend is charged to retained earnings. The total dividends was \$449,856.

On March 29, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$30,000 were decreed.

On February 28, 2019, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$200,000 were decreed.

On December 21, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$30,000 were decreed.

On October 22, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$72,068 were decreed.

On September 28, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$30,000 were decreed.

On September 24, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$100,000 were decreed.

On July 30, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$100,000 were decreed.

On July 30, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$74,206 were decreed.

On June 29, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$30,000 were decreed.

On April 30, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$100,000 were decreed.

At the Ordinary General Meeting of Shareholders held on April 30, 2018, it was agreed to decree dividends of 1 peso per share, the dividend is charged to retained earnings. The total dividends was \$425,987.

On April 26, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$9,527 were decreed.

On March 28, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$75,861 were decreed.

On January 22, 2018, dividends in favor of the non-controlling shareholders in the Ordinary General Meeting of subsidiaries in the amount of \$100,000 were decreed.

Tax incurred is payable by the Company and may be credited against IT of the period or for the following two immediate periods. Dividends paid from previously taxed earnings are not subject to any tax withholding or additional tax payments.

It is also established that individuals residing in Mexico, as well as residents abroad, receiving dividends or profits that may have been generated starting from 2014, must pay an additional tax of 10%. In these cases, the companies that distribute or pay dividends to individuals residing in Mexico or residing abroad must withhold 10%. The 10% tax applies only to profits generated starting from 2014, therefore the company shall carry two separate accounts to identify the profits generated before and after 2014.

## 20. Income from ordinary activities

The earned income for the years ended December 31, 2019 and 2018, comes entirely from the sale of products.

### *Seasonality of operations*

Most of the products manufactured and traded by the Group are seasonal, increasing their sales in the last fourth months of the year in the preserves case. Additionally, consumption of certain products (mayonnaise, mole and tuna fish) increases during lent, and others increase such as tea and marmalades in the winter. Also, the sale of frozen products increases during the summer. Seasonality is also a factor in the harvest cycle of certain raw materials used by the Company. Due to this, during those periods, the Group increases its safety inventories.

### *Nature of the goods*

A description of the different types of products by business segment is presented below.

### *Frozen products*

The main products in this segment are ice cream and commercial products. For the sale of the frozen product segment, the company recognizes revenues to the extent that performance obligations are met. The performance obligations are met when control of the products sold is transferred, which occurs when they are received at the customer's warehouse and in case of sale to the general public immediately upon delivery of the product.

The Group does not grant a general right of return. However, sporadically, customers can return products with damaged packaging.

Customers have a different payment term, according to the distribution channel to which they belong.

- The payment terms granted to customers of the convenience and self-service channel go from 30 to 60 days, therefore, the amount of the consideration is not adjusted for the effects of a significant financing component. The payment conditions with wholesale customers usually include discounts for temporary price reduction and contributions to the brand.
- In the traditional channel most of the sales are to the general public in cash or with bank cards.

### *Preserves*

The products that the company sells in the preserves segment include the following jarred, canned and packaged foods: pasta, tomato puree, ketchup, tuna, mayonnaise, jelly, mustard, tea, dressings, spices, honey, homemade sauces and sauces, chilies, mole, and canned vegetables, mainly. For the sale of canned and jarred foods, the company recognizes revenues to the extent that performance obligations are met. Performance obligations are met when control of the products sold is transferred, which occurs when they are received at the customer's warehouse.

The Group does not grant a general right of return. However, sporadically, customers can return products with damaged packaging.

Customers have a different payment term, according to the distribution channel to which they belong.

The payment terms granted to customers of the wholesale or self-service channel go from 30 to 60 days, therefore, the amount of the consideration is not adjusted for the effects of a significant financing component. The payment conditions with wholesale customers usually include discounts for temporary price reduction and contributions to the brand.

### *Export*

The products the company sells in this segment include the following canned and jarred foods: fresh fish, mayonnaise, chili peppers, mole and homemade sauces, mainly. For the sale of jarred, packaged and canned foods, the Company recognizes revenues to the extent that performance obligations are met. Performance obligations are met when control of the products sold is transferred, which occurs when they leave the Group's warehouse.

The Group does not grant a general right of return. However, sporadically, customers can return products with damaged packaging.

Customers have a different payment term, according to the distribution channel to which they belong.

- The payment terms granted to customers of the wholesale or self-service channel go from 30 to 60 days, therefore, the amount of the consideration is not adjusted for the effects of a significant financing component. The payment conditions with wholesale customers usually include discounts for temporary price reduction and contributions to the brand, mainly.

### *Contract balances*

The balances of contracts with customers include mainly the amount of accounts receivable from customers that amounts to \$3,263,968 and \$2,920,464 as of December 31, 2019 and 2018, respectively (see note 9).

*Income segregation*

In the tables shown in the next page, income is segregated by main categories.

	<b>2019</b>			
	Preserves	Frozen	Export	Total
Main Categories				
Jarred	\$ 9,652,597	143,187	1,302,478	11,098,262
Packed	4,959,018	151,034	61,243	5,171,295
Cold	-	2,934,421	3,437	2,937,858
Canned	2,401,100	-	262,921	2,664,021
Refrigerated	220,409	-	-	220,409
Services	21,368	-	-	21,368
Other (mainly labels)	307,156	-	-	307,156
Total	\$ 17,561,648	3,228,642	1,630,079	22,420,369

	<b>2018</b>			
	Preserves	Frozen	Export	Total
Main Categories				
Jarred	\$ 8,408,026	100,694	1,183,332	9,692,052
Packed	5,291,002	194,579	237,523	5,723,104
Cold	-	2,689,484	9,008	2,698,492
Canned	2,515,433	-	99,809	2,615,242
Services	15,826	-	-	15,826
Other (mainly labels)	224,290	-	1,677	225,967
Total	\$ 16,454,577	2,984,757	1,531,349	20,970,683

*Contract costs*

The Group does not incur significant compliance costs that require capitalization.

## 21. Cost of goods sold

Cost of goods sold for the periods ended December 31, 2019 and 2018, is comprised as shown as follows:

	<b>2019</b>	2018
Direct cost of sales	\$ 12,850,599	11,764,243
Maintenance and conservation	444,376	502,136
Electricity	167,195	151,164
Expenses related to post-employment defined benefit plans	12,761	12,845
Depreciation and amortization	312,554	290,591
Total cost of sales	<u>\$ 13,787,485</u>	<u>12,720,979</u>

## 22. Operating expenses

	<b>2019</b>	2018
Employee benefits expenses	\$ 2,555,454	2,606,697
Distribution and associated expenses	2,206,734	2,052,667
Conservation and fuels	508,680	477,044
Depreciation and amortization	515,071	229,289
	<u>\$ 5,785,939</u>	<u>5,365,697</u>

## 23. Other income and other expenses

Other income incurred for the years ended December 31, 2019 and 2018 is comprised as follows:

	2019	2018
Other income:		
True up in equity investment	\$ 12,886	\$ 13,346
Inflationary effects of tax receivables balances	11,354	21,743
Claims recovery	3,115	3,734
Income from sale of fixed assets	88,401	3,225
Income from distribution alliances	31,648	34,355
Scrap and waste materials sales	19,918	11,372
Franchise income	6,024	14,366
Gain on sale of shares	-	8,282
Other income	39,808	16,288
	<hr/>	<hr/>
Total other income	213,154	126,711
	<hr/>	<hr/>
Impairment loss	58,939	-
True up in equity investment	-	758
Loss on sale of fixed assets	-	4,380
Unused productive plants	10,334	3,926
Other expenses	924	4,791
	<hr/>	<hr/>
Total other expenses	70,197	13,855
	<hr/>	<hr/>
	\$ 142,957	\$ 112,856
	<hr/>	<hr/>

## 24. Financial income and costs

	2019	2018
Earned interests:		
Bank interests	\$ 144,946	\$ 118,130
Related parties interests	1,009	2,242
	<hr/>	<hr/>
Total earned interests	145,955	120,372
Exchange rate profit	162,435	330,529
	<hr/>	<hr/>
Financial income	308,390	450,901
Interests paid:		
Bank interests paid	635,301	598,228
	<hr/>	<hr/>
Total interests paid	635,301	598,228
Interest IFRS 16	89,013	-
Exchange rate loss	196,204	343,274
	<hr/>	<hr/>
Financial costs	920,518	941,502
	<hr/>	<hr/>
Net financial result	\$ 612,128	\$ 490,601
	<hr/>	<hr/>

## 25. Operating segments

### Segmentation basis

The Group has three segments on which it should inform, as described on the next page, which correspond to the strategic divisions of the Group. The strategic divisions offer various products and services, and they are managed separately as they require different technology and marketing strategies. For each of the strategic divisions, the Company's CEO (responsible for making operational decisions) reviews the Management reports prepared internally at least quarterly. The summary shown in next page describes the operations of each reportable segment.

	<b>2019</b>			
	Frozen	Preserves	Export	Total
Net sales	\$ 3,228,642	17,561,648	1,630,079	22,420,369
Cost of sales	1,160,373	11,220,977	1,406,135	13,787,485
Gross profit	2,068,269	6,340,671	223,944	8,632,884
Operating expenses	1,952,253	3,719,484	114,202	5,785,939
Income before other income	116,016	2,621,187	109,742	2,846,945
Other income, net	(26,912)	169,869	-	142,957
Operating income	89,104	2,791,056	109,742	2,989,902
Depreciation and amortization	417,285	350,997	59,343	827,625
Financial result, net	56,067	556,061	-	612,128
Equity in associate's investment	-	775,933	-	775,933
Income before tax	33,037	3,010,928	109,742	3,153,707
Income tax	11,369	885,411	32,885	929,665
Consolidated net income	21,668	2,125,517	76,857	2,224,042
Net income from non-controlling interest	40	1,171,304	38,201	1,209,545
Net income from controlling interest	21,628	954,213	38,656	1,014,497
Total assets	4,286,615	26,195,153	2,599,666	33,081,434
Total liabilities	\$ 1,737,900	12,346,794	749,084	14,833,778

	2018			
	Frozen	Preserves	Export	Total
Net sales	\$ 2,984,757	16,454,577	1,531,349	20,970,683
Cost of sales	1,078,003	10,329,135	1,313,841	12,720,979
Gross profit	1,906,754	6,125,442	217,508	8,249,704
Operating expenses	1,781,736	3,491,089	92,872	5,365,697
Income before other income	125,018	2,634,353	124,636	2,884,007
Other income, net	28,911	83,945)	-	112,856
Operating income	153,929	2,718,298	124,636	2,996,863
Depreciation and amortization	177,742	297,371	44,767	519,880
Financial result, net	( 10,871 )	501,472	-	490,601
Equity in associate's investment	-	916,111	-	916,111
Income before tax	164,800	3,132,937	124,636	3,422,373
Income tax	62,526	899,465	36,623	998,614
Consolidated net income	102,274	2,233,472	88,013	2,423,759
Net income from non-controlling interest	160	1,224,221	43,120	1,267,501
Net income from controlling interest	102,114	1,009,251	44,893	1,156,258
Total assets	2,679,600	24,861,586	2,098,809	29,639,995
Total liabilities	727,310	10,108,701	554,337	11,390,348

### Major customer

At December 31, 2019 and 2018, the Company commercialized its products with a large number of customers, and only one (Wal-Mart de México, S. A. B. de C. V.) represented approximately 24% and 23% of the total revenues, respectively.

## 26. Earning per share

The calculation of basic earnings per share and diluted earnings per share at December 31, 2019 was based on the profit of \$1,014,497 attributable to controlling interest stockholders (\$1,156,258 in 2018) and a weighted average number of ordinary shares outstanding of 409,759 thousands of shares (425,496 thousands of shares in 2018).



## 27. Contingencies

- a) The Company is involved in a number of lawsuits and claims derived from the ordinary course of business. It is expected that the final outcome of these matters will not have significant adverse effects on the Company's financial position and future results of operations.
- b) In accordance with the Mexican tax law, the tax authorities are empowered to examine transactions carried out during the five years prior to the most recent income tax return filed.
- c) In accordance with the IT Law, companies carrying out transactions with related parties are subject to certain requirements as to the determination of agreed prices, which should be similar to those that would be used with or between parties in arm's-length transactions.
- d) There are contingent liabilities arising from tax differences, which the authorities attempt to collect in the event of an official review of the tax returns filed by some of its subsidiaries, if the criteria applied in interpreting the legal provision differ from those of the authorities.
- e) The Company has a protected processes related to disputing the resolutions issued by the tax authorities, whereby requests for refunds related to value added tax receivable ("VAT") balances were denied. To date, there is no final judgment that defines the situation in controversy (refund denial), of which the result does not contain a determination of omitted obligations, or contingencies or tax credits. The recoverable amount at closing of 2019 was \$278 million pesos.

In addition, the Company is subject to the exercise of verification powers for the years 2014 to 2016 in matters of VAT, without there being any official letters that determine any tax credit to date.

## 28. Commitments

- a) In the ordinary course of business, certain subsidiaries have undertaken commitments resulting from sales agreements, and for the purchase of machinery and equipment, which in certain cases, establish default penalties for cases of non-compliance..
- b) The Company has entered into contracts for the payment of royalties in which it is obliged to pay different percentages on sales of certain brands and in different terms. Payments for such royalties are with McCormick and Company Inc., Barilla G. e. R. Fratelli, S. p. A. and Société des Produits Nestlé, S. A.

## 29. Subsequent events

- i) On January 21, 2020, Megamex Foods, LLC dividends in favor of shareholders in the amount of 20 million dollars were decreed, which were paid on the same date.
- ii) On February 12, 2020 was registered a reduction of capital stock of 8 million dollars as part of investment registered in Authentic Speciality Foods (ASF).
- iii) On February 25, 2020, at the Ordinary General Meeting of McCormick de México, S. A. de C. V. dividends in favor of the shareholders in the amount of \$200,000 were decreed, which were paid on February 27, 2020.

- iv) On March 4, 2020, three purchase agreements of tuna fishing vessels were entered by Hersea, S. A. de C. V. for amount of 28 million dollars, which were paid on the same date.
- v) On March 4, 2020, three purchase agreements of helicopters were entered by Hersea, S. A. de C. V. for amount of 1 million dollars, which were paid on the same date.
- vi) Impacts from the COVID-19 pandemic that could have a significant adverse effect on the Company's operating results:

The Group's activities and operations could be affected by a pandemic called COVID-19 due to multiple factors, such as supply chain disruptions, increases in operating expenses, and falling revenue. In addition, the Company's performance could be affected by volatility in financial markets as a result of the worldwide effects of COVID-19.

As of the date of this report, the Company's Management is evaluating the necessary measures to minimize the impacts on these factors by the COVID-19 pandemic. The Group cannot guarantee that the effects of this pandemic will not have an adverse effect on future results.

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