

ALPHABET DE MÉXICO DE MONCLOVA, S.A. DE C.V.  
(Subsidiary of MSSL (GB) Limited)

Financial statements

Years ended December 31, 2018 and 2017  
with report of independent auditors

ALPHABET DE MÉXICO DE MONCLOVA, S.A. DE C.V.  
(Subsidiary of MSSL (GB) Limited)

Financial statements

At December 31, 2018 and 2017

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## INDEPENDENT AUDITORS REPORT

At the General Shareholders' Meeting  
Alphabet de México de Monclova, S.A. de C.V.

### Qualified opinion

We have audited the accompanying financial statements of Alphabet de México de Monclova, S.A. de C.V. which comprise the statement of financial position as at December 31, 2018, and the statement of income, statement of changes in stockholders' equity and statement of cash flows for the year then ended, and notes to financial statements, including a summary of significant accounting policies.

In our opinion, except for the possible effects of the issues described in the section "Foundations for qualified opinion", the accompanying financial statements present fairly, in all material respects, the financial position of Alphabet de México de Monclova, S.A. de C.V. as at December 31, 2018, and its financial performance and its cash flows for the year then ended in accordance with Mexican Financial Reporting Standards ("MFRS").

### Foundations for qualified opinion

1. As discussed in Note 1b) to the accompanying financial statements, for the years ended December 31, 2018 and 2017, the Company did not recognize the cumulative effects of inflation as required by Mexican Financial Reporting Standard (MFRS B-10 "Effects of inflation") through December 31, 2007. Nevertheless, management determined that it was not practical to calculate the inflation effects for each account of the financial statements as at December 31, 2018 and 2017. The lack of recognition of the effects inflation is considered a material deviation for the accompanying financial statements.
2. As discussed in Note 1n) to the accompanying financial statements, the Company did not recognize deferred taxes as at December 31, 2018 and 2017, as required by Mexican Financial Reporting Standard (Mexican FRS) D-4 Income tax. In accordance with Mexican FRS D-4, deferred taxes should be recognized on all temporary differences between the financial reporting and tax values of assets and liabilities at the reporting date. Nevertheless, management determined that it was not practical to calculate the Company's deferred taxes as at December 31, 2018 and 2017.

3. As discussed in Note 1k) to the accompanying financial statements, the Company did not recognize deferred employee profit sharing as at December 31, 2018 and 2017, as required by Mexican Financial Reporting Standard D-3 Employee benefits, since management determined that it was not practical to calculate the Company's deferred employee profit sharing as at December 31, 2018 and 2017.
4. As discussed in Note 1j) to the accompanying financial statements, the Company did not record a provision for its obligation related to termination benefits as at December 31, 2018 and 2017, which should be calculated using the projected unit credit method in accordance with Mexican FRS D-3 Employee benefits. The lack of recognition of such liability is considered a material deviation for the accompanying financial statements. In addition local management determined that it was not practical to calculate the Company's employee benefit obligation.

We conducted our audit in accordance with International Standards on Auditing ("ISA"). Our responsibilities under those standards are further described in the "Auditor's responsibilities for the audit of the financial statements" section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code") together with the ethical requirements that are relevant to our audit of the financial statements in Mexico according with the "Código de Ética Profesional del Instituto Mexicano de Contadores Públicos" ("IMCP Code"), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified opinion.

Responsibilities of management and those charged with governance for the financial statements

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

In preparing the financial statements, management is responsible for assessing the Company'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 Company or to cease operations, or has no realistic alternative but to do so.

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

## Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's 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 ISA 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 financial statements.

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

- Identify and assess the risks of material misstatement of the 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 Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the 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 auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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 to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

Mancera, S.C.  
A Member Practice of  
Ernst & Young Global Limited

A handwritten signature in blue ink, appearing to read 'Jaime De La Garza Villarreal', with a large, stylized flourish underneath.

Jaime De La Garza Villarreal

San Pedro Garza García, N.L., México.  
June 7, 2019.

ALPHABET DE MÉXICO DE MONCLOVA, S.A. DE C.V.  
(Subsidiary of MSSL (GB) Limited)

Statements of financial position

(Amounts in Mexican pesos)

	December 31,	
	2018	2017
Assets		
Current assets:		
Cash	\$ 6,119,304	\$ 7,951,175
Accounts receivable (Note 2)	5,488,938	5,309,094
Related parties (Note 3)	24,758,655	66,421,581
Prepaid expenses	5,401,982	3,358,351
Total current assets	41,768,879	83,040,201
Machinery, equipment and improvements, net (Note 4)	5,528,511	1,631,454
Total assets	\$ 47,297,390	\$ 84,671,655
Liabilities and stockholder's equity		
Current liabilities:		
Suppliers	\$ 1,035,209	\$ 3,721,797
Direct benefits to employees (Note 6)	11,503,697	10,285,982
Accrued expenses and other taxes	11,728,872	14,963,393
Taxes payable (Note 9)	545,260	-
Total current liabilities	24,813,038	28,971,172
Long-term liabilities:		
Labor obligation (Note 7)	5,321,055	4,166,965
Total long-term liabilities	5,321,055	4,166,965
	30,134,093	33,138,137
Stockholder's equity: (Note 8)		
Capital stock	50,000	50,000
Retained earnings	17,113,297	51,483,518
Total stockholder's equity	17,163,297	51,483,518
Total liabilities and stockholder's equity	\$ 47,297,390	\$ 84,671,655

The accompanying notes are an integral part of these financial statements.

Edgar Roberto García  
Comptroller

ALPHABET DE MÉXICO DE MONCLOVA, S.A. DE C.V.  
(Subsidiary of MSSL (GB) Limited)

Statements of income

(Amounts in Mexican pesos)

	For the years ended December 31,	
	2018	2017
Revenues:		
Maquila revenues (Note 3)	\$ 355,226,847	\$ 316,958,844
Other income, net	2,925,589	162,486
	<u>358,152,436</u>	<u>317,121,330</u>
Expense and cost:		
Expense of maquila	( 334,674,273)	( 297,908,736)
Operating income	<u>23,478,163</u>	<u>19,212,594</u>
Comprehensive financing cost:		
Interest income, net	3,239	2,141
Exchange gain (loss), net	91,848	( 309,044)
	<u>95,087</u>	<u>( 306,903)</u>
Income before taxes on profits	23,573,250	18,905,691
Taxes on profits (Note 9)	( 6,459,953)	( 7,419,718)
Net income	<u>\$ 17,113,297</u>	<u>\$ 11,485,973</u>

The accompanying notes are an integral part of these financial statements.

Edgar Roberto García  
Comptroller



ALPHABET DE MÉXICO DE MONCLOVA, S.A. DE C.V.  
(Subsidiary of MSSL (GB) Limited)

Statements of changes in stockholder's equity

For the years ended December 31, 2018 and 2017

(Amounts in Mexican pesos)

	Capital stock	Retained earnings	Total stockholder's equity
Balance as of December 31, 2016	\$ 50,000	\$ 39,997,545	\$ 40,047,545
Net income		11,485,973	11,485,973
Balance as of December 31, 2017	50,000	51,483,518	51,533,518
Dividends paid (Note 8)		( 51,483,518)	( 51,483,518)
Net income		17,113,297	17,113,297
Balance as of December 31, 2018	\$ 50,000	\$ 17,113,297	\$ 17,163,297

The accompanying notes are an integral part of these financial statements.

Edgar Roberto García  
Comptroller

ALPHABET DE MÉXICO DE MONCLOVA, S.A. DE C.V.  
(A Subsidiary of MSSL (GB) Limited)

Statements of cash flows

(Amounts in Mexican pesos)

	For the years ended December 31,	
	2018	2017
Operating activities		
Income before taxes on profits	\$ 23,573,250	\$ 18,905,691
Items in results of operations not affecting cash:		
Depreciation	752,006	933,646
Labor obligation	1,544,431	686,264
Accrued interest receivable	( 3,239)	( 2,141)
	25,866,448	20,523,460
Changes in operating assets and liabilities:		
Accounts receivable	365,416	( 8,916,415)
Related parties	41,662,926	( 10,444,555)
Prepaid expenses	( 2,043,631)	( 1,564,622)
Suppliers	( 2,686,588)	3,228,560
Direct employees benefits	827,374	3,079,747
Taxes payable	( 6,459,953)	( 7,419,718)
Accrued expenses and other taxes	( 3,234,521)	7,459,008
Net cash provided by operating activities	54,297,471	5,945,465
Investing activities		
Purchase of machinery, equipment and improvements	( 4,649,063)	( 90,842)
Net cash flows used in investing activities	( 4,649,063)	( 90,842)
Financing activities		
Interest paid	3,239	2,141
Dividends paid	( 51,483,518)	-
Net cash (used) provided in financing activities	( 51,480,279)	2,141
Net (decrease in) increase cash	( 1,831,871)	5,856,764
Cash at beginning of year	7,951,175	2,094,411
Cash at end of year	\$ 6,119,304	\$ 7,951,175

The accompanying notes are an integral part of these financial statements.

Edgar Roberto García  
Comptroller

ALPHABET DE MÉXICO DE MONCLOVA, S.A. DE C.V.  
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Notes to the financial statements

At December 31, 2018 and 2017

(Amounts in Mexican pesos, unless otherwise indicated)

1. Operations

Alphabet de México de Monclova, S.A. de C.V. (The "Company") started July 1, 2014 a subsidiary of MSSL (GB) Limited, (MSSL) it was founded in July 14, 2003, in accordance with Mexican law under the protection of the maquila program established by the Mexican Government. Its main activity is the design and manufacture of components, modules and electricity distribution systems and signals under a maquila agreement with MSSL Wiring System, Inc. (a related party).

The period of operations of the Company and the fiscal year, comprise from January 1 to December 31.

The issuance of the financial statements and the accompanying notes was authorized by Edgar Roberto García, Comptroller on June 7, 2019. These financial statements must be approved at a later date by the Board of Directors and the Stockholders. These bodies have the power to amend the accompanying financial statements. Subsequent events were considered to date.

Summary of significant accounting policies

a) Compliance with Mexican Financial Reporting Standards

Except as mentioned in paragraphs b), j), k) and n), the accompanying financial statements have been prepared in accordance with Mexican Financial Reporting Standards (Mexican FRS).

b) Basis of preparation

The financial statements as of December 31, 2018 and 2017 have been prepared on a historical-cost basis. The Company did not determine the effects of inflation on its financial information through December 31, 2007 as required under Mexican FRS. Nevertheless, management determined that it was not practical to calculate the inflation effects for each account of the financial statements as at 31 December 2018 and 2017.

From January 1, 2008 Mexico is considered to have a non-inflationary economic environment, as defined under Mexican FRS B-10 "Effects of Inflation". As at December 31, 2018 and 2017, Mexico's cumulative inflation rate for the three prior years was 26% (annual average of 8%), which represents the necessary condition for considering Mexico as having a non-inflationary economic environment.

2.

As determined based on the National Consumer Price Index (NCPI) published by the National Statistical and Geographical Information Agency (INEGI), Mexico's annual inflation rate for 2018 and 2017 is as follows:

	Cumulative inflation for 2017	Cumulative inflation for 2018	Inflation for the year
	(sum of inflation rates for 2015, 2016 and 2017)	(sum of inflation rates for 2016, 2017 and 2018)	(inflation rate for 2018)
Inflation rates	12.81%	14.96%	4.83%

c) Recognition of revenues

Maquila revenues are recognized at the moment in which the service is provided maquila. For the determination of income the company uses a factor of 6.02% profit on the costs and expenses incurred in the maquila process.

d) Use of estimates

The preparation of financial statements in accordance with Mexican FRS requires the use of estimates and assumptions in certain areas. The Company based its estimates on the best available information at the time the financial statements were prepared. However, the existing circumstances and assumptions about future events may change due to changes in the market or circumstances that are beyond the Company's control. Such changes are reflected in the assumptions as they occur.

The key assumptions used at December 31, 2018 and 2017, in determining estimates that involve uncertainty and may have a significant risk of causing adjustments relative importance on the carrying amount of assets and liabilities during the next financial year, are the following:

Impairment in the value of non-financial assets

Impairment exists when the carrying amount of an asset or a cash-generating unit exceeds its recoverable amount, which is the fair value less costs to sell or value in use, whichever is greater. The calculation of fair value less costs to sell is based on information available on similar sales operations, made in conditions between independent parties for similar assets or observable market prices less incremental costs of disposal of the property. The calculation of value in use is based on a model of discounted cash flows. Cash flows arising from the budget for the next five years or more considering that growth rates should not be for more than five years and do not include restructuring activities to which the Company still has not committed, or investments significant future that will increase well performance or cash-generating unit to be tested. The recoverable amount is very sensitive to the discount rate used for the model of discounted cash flows and the expected future cash income to the growth rate used for extrapolation purposes.

Other disclosures relating to impairment of non-financial assets of the Company are included in:

- Machinery, equipment and improvements in Note 4.

## Retirement benefits

The cost of defined benefits and the present value of the corresponding obligations are determined using actuarial valuations. Actuarial valuations involve a number of assumptions. These include determining the discount rate, future salary increases, mortality rates and future pension increases. Due to the complexity of the valuation, the underlying assumptions and its long-term nature, defined benefit obligations are very sensitive to changes in these assumptions. All assumptions are reviewed at each closing date of the reporting period.

To calculate the discount rate, management considers the interest rates of marketable securities in the corresponding currencies. These instruments must be at least AA rated, and management uses extrapolated maturities covering the expected duration of the defined benefit obligation. The underlying bonds are further assessed for quality, and those having excessive credit spreads are removed from the population of bonds on which the discount rate is based, due to their low quality.

The mortality rate is based on the country charts.

Future increases in wages and pensions are based on future inflation rates expected in the country.

Note 7 shows more detail on the assumptions used.

### e) Cash

Cash principally consist of bank deposits.

### f) Prepaid expenses

Prepaid expenses are recognized for the amount paid at the time this is always done and when it is estimated that the future economic benefit associated flow to the Company. Once the good or service is received, the Company recognizes the amount on prepayments as an asset or expense, depending on whether or not you have the certainty that the purchased goods will generate a future economic benefit.

The Company periodically evaluates the ability of prepaid expenses lose their ability to generate future economic benefits and the recoverability thereof, the amount deemed as unrecoverable is recognized as an impairment loss in income for the period.

### g) Machinery, equipment and improvements

Machinery, equipment and improvements, net are initially recognized at their acquisition value. In the case of assets that require a substantial period for use, comprehensive financing cost incurred during the construction and installation of the same is capitalized.

4.

The acquisition value of machinery, equipment and improvements includes costs that have been incurred initially to be acquired or constructed and subsequently incurred to replace or increase its service potential. If an item of machinery and equipment consist of several components with different estimated useful lives, important individual components are depreciated over their individual useful lives

The depreciation of machinery, equipment and improvements is computed on the carrying value, using the straight-line method (since management considers that this method best reflects the use of these assets), based on the estimated useful life, as follow:

	<u>Years</u>
Leasehold improvements	20
Machinery and equipment	10
Furniture and fixtures	10
Computer equipment	3

An item of machinery, equipment and improvements is derecognized upon disposal or when no future economic benefits are expected from their use or sale. Any gain or loss arising from derecognition of the asset (calculated as the difference between the net revenue from disposal and the carrying amount of the asset) it is included in the statement of comprehensive income when the asset derecognized.

The carrying amount of machinery, equipment and improvements is reviewed whenever there are indicators of impairment in the value of such assets. When the recoverable amount of an asset, which is the higher of the asset's expected net selling price and its value in use (the present value of future cash flows), is less than its net carrying amount, the difference is recognized as an impairment loss.

For the years ended December 31, 2018 and 2017, there were no indicators of impairment.

h) Other assets

Are composed mainly of security deposits delivered as part of the lease of the building where the plant is located.

i) Liabilities, provisions, contingent liabilities and commitments

Liabilities are recognized whenever (i) the Company has current obligations (legal or constructive) resulting from a past event, (ii) when it is probable the obligation will give rise to a future cash disbursement for its settlement, and (iii) the amount of the obligation can be reasonably estimated.

When the effect of the value of money over time is significant, the amount of the provision is the present value of the expenditures expected to be required to settle the obligation. The discount rate applied in these cases is pretax and reflects market conditions at the date of statement of financial position and, where appropriate, the risks specific to the liability. In these cases, the increase in the provision is recognized as an interest expense.

Contingent liabilities are recognized only when it is probable they will give rise to a future cash disbursement for their settlement. Also, commitments are only recognized when they will generate a loss.

The Company recognizes a contingent asset at the time the gain is realized.

j) Reserve for seniority premiums, termination benefits and other benefits

Seniority premiums are paid to workers as required by Mexican labor law. Under Mexican labor law, the Company is also obligated to make certain payments to workers who leave the Company or are dismissed in certain circumstances.

The premium costs seniority and termination benefits are recognized annually based on calculations by independent actuaries using the projected unit credit method using financial assumptions in nominal terms. The latest actuarial valuation was carried out in December 2018.

As at December 31, 2018 and 2017, the Company did not record a provision for its obligation related to termination benefits, which should be calculated using the projected unit credit method in accordance with Mexican FRS D-3 Employee benefits, because management determined that it was not practical to calculate the Company's employee benefit obligation.

k) Employee profit sharing

Current and deferred employee profit sharing is presented as part of costs or expenses in the statement of comprehensive income.

Deferred employee profit sharing is determined using the asset and liability method. Under this method, deferred employee profit sharing is calculated by applying the 10% rate to all temporary differences between the values of assets and liabilities for financial and tax reporting purposes. The Company periodically evaluates the possibility of recovering its deferred employee profit sharing assets and if necessary, creates a valuation allowance for those assets that do not have a high probability of being realized.

The Company did not recognize deferred employee profit sharing as at December 31, 2018 and 2017, as required by Mexican FRS D-3, Employee benefits, since management determined that it was not practical to calculate the Company's deferred employee profit sharing as at December 31, 2018 and 2017.

l) Foreign exchange

Transactions in foreign currency are recognized at the prevailing exchange rate on the day of the related transactions. Foreign currency denominated assets and liabilities are valued at the prevailing exchange rate at the date of the statement of financial position.

Exchange differences from the transaction date to the time foreign currency denominated assets and liabilities are settled, as well as those arising from the translation of foreign currency denominated balances at the date of the statement of financial position, are recognized in the statement of comprehensive income.

6.

See Note 5 for the Company's foreign currency position at the end of each period and the exchange rates used to translate foreign currency denominated balances.

m) Comprehensive income

The comprehensive income is the sum of the net profit or loss, Other Comprehensive Income (OCI) and participation in the OCI of other entities. For the years ended December 31, 2018 and 2017, comprehensive income equals net income for the year.

n) Taxes on profits

Current year taxes on profits

Current-year taxes on profits are presented as a current liability, net of prepayments made during the year

Deferred income taxes

Deferred income tax is calculated using the asset and liability method. Under this method, deferred income taxes are recognized on all temporary differences between financial reporting and tax values of assets and liabilities, applying the enacted income tax rate effective as of the date of the statement of financial position, or the enacted rate at the date of the statement of financial position that will be in effect when the temporary differences giving rise to deferred tax assets and liabilities are expected to be recovered or settled.

The Company periodically evaluates the possibility of recovering deferred tax assets and if necessary, creates a valuation allowance for those assets that do not have a high probability of being realized.

The Company did not recognize deferred taxes as at December 31, 2018 and 2017, as required by Mexican FRS D-4, Income tax, since management determined that it was not practical to calculate the Company's deferred taxes as at December 31, 2018 and 2017.

o) Statement of comprehensive income presentation

Costs and expenses in the statements of comprehensive income are presented according to their function, as this classification allows properly assess gross margins and operating income. Presenting operating income is not required; however, it is presented as it is an important performance evaluation indicator of the Company.

p) Concentration of risk

As at December 31, 2018 and 2017, the Company provides its maquila services exclusively to its related party MSSL Wiring System, Inc. under a maquila program. Accordingly, in the event that the related party no longer requires these services, the Company's operating results could be adversely affected.



q) New accounting pronouncements

1) Standards and Improvements to Mexican FRS issued but not yet effective

The standards that are issued but not yet effective up to the date of issue of the Company's financial statements are disclosed below.

The Company intends to adopt these standards, if applicable, when they become effective.

Mexican Financial Reporting Standard (Mexican FRS) D-5 "Leases" (effective as of January 1, 2019)

In December 2017, the CINIF issued the new Mexican FRS D-5 "Leases", which contains the following two critical lease accounting principles:

- a) Lessees must recognize an asset representing the right to use the leased underlying asset and a liability to make lease payments, unless the lease is a short-term lease or the underlying asset has a low value.
- b) Lessors must classify their lease agreements into operating or finance leases, depending on the degree to which substantially all of the risks and rewards of ownership of the underlying asset have been transferred to the lessee. Under a finance lease, the lessor derecognizes the underlying asset and recognizes a receivable. Under an operating lease, the lessor does not derecognize the underlying asset and recognizes lease payments received as accrued instead.

Mexican FRS D-5 sets out a single lessee accounting model that requires lessees to recognize assets and liabilities for all leases with lease terms of twelve months or more, unless the underlying asset has a low value. Lessees must recognize a right-of-use asset for the underlying asset and a liability representing the obligation to make lease payments.

The most important changes for lessees are as follows:

- At the lease commencement date, lessees must determine whether they obtain the right to control an identified asset or assets for a period of time.
- The new Mexican FRS D-5 eliminates the requirement for lessees to classify leases as operating leases or finance leases. Lessees now shall recognize a lease liability for the present value of the lease payments and an asset for an equal amount for the right to use the underlying asset.
- Lessees will no longer recognize operating lease expense on a straight-line basis, and will instead recognize the depreciation or amortization expense associated with the right-of-use asset and interest expense associated with their lease liabilities. The purpose of this change is to unify the treatment of lease expenses for all leases.

8.

- In the statement of cash flows, payments arising from operating leases shall no longer be recognized within operating activities and instead shall be recognized within financing activities.
- The recognition of the gains or losses resulting from the transfer of an asset by a seller-lessee to another entity or from sale-leaseback transactions shall no longer be based on the classification of the sale-leaseback agreement; instead, the seller-lessee will only recognize a sale for the rights transferred to the buyer-lessor that will not be returned to it (the unguaranteed residual value).

The new accounting Mexican FRS D-5 "Leases" contains significant changes to lessee accounting, but no significant changes to lessor accounting compared to the former Mexican accounting Bulletin D-5 "Leases" apart from additional disclosure requirements.

Mexican FRS D-5 replaces Bulletin D-5 "Leases" ("Bulletin D-5") and the supplementary application of IFRIC 4 "Determining whether an Arrangement contains a Lease" ("IFRIC 14"). MFRS D-5 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under Bulletin D-5. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset).

Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will be also required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset.

Lessor accounting under MFRS D-5 is substantially unchanged from today's accounting under Bulletin D-5. Lessors will continue to classify all leases using the same classification principle as in Bulletin D-5 and distinguish between two types of leases: operating and finance leases.

MFRS D-5 also requires lessees and lessors to make more extensive disclosures than under Bulletin D-5.

MFRS D-5 is effective for annual periods beginning on or after January 1, 2019. Early application is permitted, but not before an entity applies MFRS D-1. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs.

### Transition to MFRS D-5 “Leases”

The Company plans to adopt MFRS D-5 retrospectively. The Company will elect to apply the standard to contracts that were previously identified as leases applying Bulletin D-5 and IFRIC 4. The Company will therefore not apply the standard to contracts that were not previously identified as containing a lease applying Bulletin D-5 and IFRIC 4.

The Company will elect to use the exemptions proposed by the standard on lease contracts for which the lease terms ends within 12 months as of the date of initial application, and lease contracts for which the underlying asset is of low value. The Company has leases of certain office equipment (i.e., personal computers, printing and photocopying machines) that are considered of low value.

During 2018, the Company has performed a detailed impact assessment of MFRS D-5. In summary the impact of MFRS D-5 adoption is expected to be, as follows:

Impact on the statement of financial position (increase/(decrease)) as at 31 December 2019:

	MXN
Assets:	
Right-of-use assets	\$ 74,799,009
Liabilities:	
Lease liabilities	\$ ( 74,799,009)

Impact on the statement of profit or loss (increase/(decrease)) for 2019:

	MXN
Depreciation expense (included in administrative expenses)	\$ 12,295,735

Due to the adoption of MFRS D-5, the Company's operating profit will improve, while its interest expense will increase. This is due to the change in the accounting for expenses of leases that were classified as operating leases under Bulletin D-5.

### Improvements to Mexican FRS for 2019

The improvements that will give rise to accounting changes related to valuation, disclosures or presentation in the financial statements are as follows:

10.

(i) Mexican FRS B-9 Interim financial reporting

Mexican FRS B-9 Interim financial reporting introduces new disclosure requirements for condensed financial statements for an interim period related to the fair value of the Company's financial instruments and revenue from contracts with customers, such as changes in economic and business circumstances that affect the fair value of financial assets and liabilities, transfers between levels of the fair value hierarchy used in measuring the fair value of financial instruments, changes in the classification of financial assets as a result of a change in the purpose or use of those assets or changes in contingent liabilities or contingent assets, regardless of the date of the most recent annual financial report.

These improvements are effective for annual periods beginning on or after 1 January 2019. Any accounting changes arising from the adoption of these improvements are to be recognized prospectively.

The adoption of these new accounting standards had no effect on the Company's financial statements.

Improvements to Mexican FRS for 2018

The new financial reporting standards that will give rise to accounting changes related to valuation, disclosures or presentation in the financial statements are as follows:

(i) Mexican FRS B-2, Statement of cash flows

Mexican FRS B-2 introduces a new requirement that entities must now include in the notes to the financial statements, disclosures related to relevant changes in liabilities reported within financing activities that may or may not have required the use of cash or cash equivalents. In addition to the required disclosures, entities also need to include a reconciliation of beginning and ending balances for these items.

These improvements are effective for annual periods beginning on or after January 1, 2018, with early adoption permitted for annual periods beginning on or after January 1, 2017.

The adoption of this accounting standard had no effect on the company's financial statements.

(ii) Mexican FRS B-10, Effects of Inflation

Mexican FRS B-10 introduces a new requirement that the notes to the financial statements (whether restated for inflation or not) should, in addition to the cumulative inflation rate for the three prior years and the inflation rate used to determine whether the entity operates in an inflationary or not inflationary economic environment, state the following rates:

- The cumulative inflation rate for three years that includes the two prior years and the current year, which shall be the basis for determining whether the entity will operate in an inflationary economic environment in the following year.

- The inflation rate considered for purposes of preparing the financial statements.

The adoption of this accounting standard had no effect on the company's financial statements.

These improvements are effective for annual periods beginning on or after January 1, 2018, with early adoption permitted for annual periods beginning on or after January 1, 2017.

(iii) Mexican FRS C-6, Property, plant and equipment and Mexican FRS C-8, Intangible assets

These accounting standards establish that the method used for the depreciation or amortization of an asset should reflect the pattern of consumption of the expected future economic benefits and not the pattern of generation of expected future economic benefits.

The standards also establish that the use of a depreciation or amortization method based on the amount of revenue earned from the use of the assets is no longer appropriate, since the amount of that revenue can be dependent on factors other than the pattern of consumption of the economic benefits of the asset. However, unlike Mexican FRS C-6, Mexican FRS-8 does allow entities to use a revenue-based depreciation or amortization method under certain circumstances.

These improvements are effective for annual periods beginning on or after January 1, 2018.

The adoption of this accounting standard had no effect on the company's financial statements.

## 2. Accounts receivable

At December 31, 2018 and 2017, accounts receivable is as follows:

	2018	2017
Recoverable taxes	\$ 5,084,008	\$ 5,083,544
Other accounts receivables	404,930	225,550
	<u>\$ 5,488,938</u>	<u>\$ 5,309,094</u>

## 3. Related parties

The companies mentioned in this note are considered as affiliates, and the stockholders of these companies are also stockholders of the Company.

Balances with related parties at December 31, 2018 and 2017 parts are as follows:

	2018	2017
Receivable:		
MSSL Wiring System Inc. <sup>(a)</sup>	\$ 24,758,655	\$ 66,421,581
	<u>\$ 24,758,655</u>	<u>\$ 66,421,581</u>

12.

- (a) The company conducts its operations through a maquila's contract, which states that income will be calculated based on the costs and expenses incurred in the conduct of its operations plus a percentage of profit.

Operations with related parties performed in the normal course of business, were as follows:

	2018	2017
Revenue:		
Revenue for maquila service	\$ 355,226,847	\$ 316,958,844

4. Machinery, equipment and improvements, net

At December 31, 2018 and 2017, the balances of machinery, equipment and improvements, are integrated as follows:

	2018	2017
Machinery and equipment	\$ 8,071,220	\$ 7,963,278
Leasehold improvements	5,913,972	3,107,766
Computer equipment	1,678,903	1,678,903
Furniture and fixtures	972,621	972,621
Construction in process	1,810,850	90,842
Total fixed assets	18,447,566	13,813,410
Accumulated depreciation	( 12,919,055)	( 12,181,956)
Machinery, equipment and improvements, net	\$ 5,528,511	\$ 1,631,454

Depreciation for the year 2018 and 2017 that was recognized in the income statement amounted to \$752,006 and \$933,646, respectively.

5. Transaction in foreign currency

- a) At December 31, 2018 and 2017, the Company has assets and liabilities denominated in US dollars as follows:

	2018	2017
Dollars:		
Monetary assets	US\$ 155,936	US\$ 234,183
Monetary liabilities	( 5,173)	( 90,884)
Net monetary liability position	US\$ 150,763	US\$ 143,299

- b) The exchange rates used to convert amounts before national currency were \$19.65 and \$19.74 for the US dollar as of December 31, 2018 and 2017, respectively. At June 7, 2018, date of the financial statements, the exchange rate is \$19.70 per dollar.

## 6. Direct benefits to employee

At December 31, 2018 and 2017, the Company has the following accruals related to direct benefits to employee:

	2018	2017
Holidays and holidays bonus	\$ 5,060,699	\$ 3,770,872
Wages to paid	3,822,036	3,754,227
Employee profit sharing	2,620,962	2,760,883
	<u>\$ 11,503,697</u>	<u>\$ 10,285,982</u>

## 7. Labor obligations

Seniority premium consists of a single payment of 12 days per worked based on the last salary, limited to twice the minimum wage established by law year. The related liability and annual cost of benefits is calculated by an independent actuary on the basis defined in the plans using the projected unit credit method.

At December 31, 2018 and 2017, the net cost of the period, defined benefit obligations related to the retirement plan (Seniority premium retirement), are as follows:

## a) Net period cost:

	2018	2017
Integration net period cost:		
Labor cost of actual service	\$ 1,162,766	\$ 572,568
Net interest of liabilities (assets) net by defined benefit	397,378	251,784
Remediation recycling	( 15,713)	( 138,088)
Net period cost	<u>\$ 1,544,431</u>	<u>\$ 686,264</u>

## b) Defined benefit obligations are shown below :

	2018	2017
Provisions to:		
Obligations for Benefits Acquired (OBA)	\$ 354,629	\$ 62,333
Obligations for benefits not acquired	4,966,426	4,104,632
Defined benefit obligations, net	<u>\$ 5,321,055</u>	<u>\$ 4,166,965</u>

14.

c) The real interest rates used in the actuarial calculations were as follows:

	2018	2017
Discount benefit obligations:		
Projected present value	9.90%	7.85%
Salary increase	5.00%	5.00%

#### 8. Stockholders' equity

a) Capital stock at December 31, 2018 and 2017 is represented by \$50,000 registered shares with a value of \$1.00 each. Variable capital is unlimited. The minimum fixed capital is represented by nominative common and released representative of the fixed portion of capital without right of withdrawal. Both the fixed and the variable portion of capital are represented by shares of Series "B" with nominal value of one peso each and are fully subscribed by foreign investors, such shares will be freely subscribed.

b) According to the general law of commercial companies, the company must separate from the net income of each year at least 5% to increase the legal reserve until it reaches 20% of the share capital. At December 31, 2018 and 2017 the company has not created the legal reserve.

c) The earnings distributed in excess of the balances of the accounts CUFINRE and CUFIN (Net Tax Income Account), shall be subject to corporate income tax in force at the time of distribution rate. The payment of this tax may be credited against income tax.

d) At regular shareholders' meetings held on August 10, 2018, the shareholders declared dividends of Ps. 51,483,518 which comes from CUFIN. Such dividends were cash-paid in full on August 13, 2018.

Dividends to individuals and legal persons resident abroad are paid on profits generated from 2014, will be subject to a withholding tax of an additional 10%.

#### 9. Taxes on profits

##### a) Income tax

The Mexican Income Tax Law (MITL) establishes a corporate income tax rate for Mexico of 30% for fiscal years 2018 and 2017.

The profit margin of 6.02% for maquila services for 2018 was determined using the so-called Fast Track methodology approved by the Mexican Tax Administration Service (SAT) and the U.S. Internal Revenue Service (IRS). As part of the Fast Track program, the Company's advance pricing agreement will be resolved using this approach.



The MITL establishes new requirements and limits regarding certain deductions, including restrictions on the deductibility of payroll-related expenses that are considered tax-exempt for employees, contributions to create or increase pension fund reserves, and Mexican Social Security Institute dues that are paid by the Company but that should be paid by the employees. The MITL also establishes that certain payments made to related parties shall not be deductible if they do not meet certain requirements.

For the years ended at December 31, 2018 and 2017, the Company reported a taxable income of \$21,533,177 and \$24,732,393, respectively, on which correspond income tax of \$6,459,953 and \$7,419,718, respectively.

b) Employee profit sharing

The MITL establishes that as of January 1, 2014, entities are to calculate their employee profit sharing on the basis of their taxable earnings for the year determined for income tax purposes, plus or minus the effects of certain adjustments specified in the Law.

## 10. Commitments and contingencies

### I. Commitments

For the land and building used in the operation, the company has entered into a lease for a period of 7 years mandatory maturing in 2025; the expense rent in 2018 amount is \$12,694,589 and \$11,934,333 and 2017; and establishes the following minimum payments:

Years	Dollar amount
2019	<u>\$ 624,066</u>

### II. Contingencies

At December 31, 2018, the company has the following contingencies:

- a) There is a contingent liability derived labor obligations mentioned in Note 1j).
- b) In accordance with current tax legislation, the authorities are entitled to examine the five fiscal years prior to the last statement filed income tax.
- c) According to the Law on Income tax, companies that conduct transactions with related parties are subject to certain limitations and requirements, as to the determination of the agreed prices, as these must be comparable to those that would be used with arm's-length transactions. In the event that the tax authorities will review prices and reject the certain amounts may require, in addition to the collection of the tax, accessories corresponding (updating and surcharges), and penalties on unpaid taxes, which could become even 100% of the amount of contributions updated. The Company's policy is to conduct a transfer pricing study to evaluate the operations carried out with related parties.

16.

d) At December 31, 2018 and 2017, and the date of issuance of these financial statements, the Company as maquiladora industry has the following commitments inherent in the IMMEX program, which have been met:

- Conduct annual sales abroad for a value of USD \$ 500,000, or its equivalent in national or invoice exports of at least 10% of its total turnover currency.
- Allocate temporarily imported under IMMEX program authorized purposes goods.
- Foreign return the goods within the period determined under the provisions of the Customs Law or the maquila program. At December 31, 2018 and 2017, the Company had under custody temporarily imported inventory owned by his holding company with an approximate value of US\$4,471,207 and US\$5,008,556, respectively (unaudited amounts).
- At December 31, 2018, the Company had under custody temporarily imported assets owned by his holding company with an approximate value of \$149,621,239 (unaudited amounts).
- Maintain temporarily imported goods at the address registered in the program.
- Request of Secretary of Economy, following proceedings before Mexican Tax Authorities (SAT), registration of changes in the data given in the request for approval of the maquila program, such as company name, address and federal registration of taxpayers, and suspension of activities.
- Maintain a control of automated inventory with certain minimum information.
- Submit an annual report no later than electronically to the Secretary of Economy and the Mexican Tax Authorities (SAT) respect to total sales and exports for the fiscal year immediately preceding the last business day of the month of May of the following year.
- In addition, returning the materials and inputs imported temporarily, the maquiladora must pay import taxes corresponding to those materials whose country of origin has not signed a bilateral free trade, likewise, you must pay the VAT on imports machinery and equipment, once it is canceled the IMMEX program and these assets remain in Mexico.

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Comptroller