Corporacion America Airport

First Quarter 2018 Earnings Conference Call

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CORPORATE PARTICIPANTS

Gimena Albanesi – *Head of Investor Relations*

Martin Eurnekian - *President and Chief Executive Officer*

Raul Francos – *Chief Financial Officer*

PRESENTATION

Operator

Good morning and welcome to the **Corporación América Airports** First Quarter 2018 earnings call. A slide presentation accompanies today's webcast and is available in the Investor section of Corporación América Airports' investor relations website, http://investors.corporacionamericaairports.com. As a reminder, all participants will be in listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. As a reminder, today's conference call is being recorded.

At this time, I would like to turn the call over to Gimena Albanesi, Investor Relations. Please go ahead.

Gimena Albanesi

Thank you. Good morning everyone and thank you for joining us today. Speaking during today's call will be Martin Eurnekian, our Chief Executive Officer and Raul Francos, our Chief Financial Officer. Also with us today is Jorge Arruda, Finance and M&A Manager. All will be available for the Q&A session.

Before we proceed, I would like to make the following Safe Harbor statement. Today's call will contain forward-looking statements and I refer you to the forward-looking statement section of our earnings release and recent filings with the SEC. We assume no obligation to update or revise any forward-looking statements to reflect new or changed events or circumstances.

With that being said, I would now like to turn the call over to our CEO, Martin Eurnekian

Martin Eurnekian

Thank you, Gimena. Hello everyone and thank you for joining us today. It's a pleasure to welcome you to Corporación America Airports' first quarter 2018 earnings conference call.

I will begin my presentation with a discussion of the highlights of the quarter and then, Raul will take you through our financial results. Afterwards, I will provide an update on our key business segments and our view for the remainder of year. We will then open the call to your questions.

Starting with slide 3. We had a strong start to the year with revenues up 10.5% and Adjusted EBITDA growth of 12.5% YoY driven by positive dynamics in our key operating metrics. More importantly, this is the result of successful execution across the organization.

Total passenger traffic was up 7.6% in the first quarter with almost 20 million passengers travelling through our 52 airports globally. Cargo volume was up 14%.

Overall positive economic conditions in the majority of the countries where our airports are located, along with our focus on adding new routes, frequencies and airlines were the key factors driving traffic growth.

To further strengthen our platform for long-term success we made capital investments of $50 million in Q1. – These investments were mainly focused on Argentina, and lo a lesser degree in Brazil and Italy, keeping with our strategy of enhancing the infrastructure of our airports.

Moving on to our regional performance on slide 4, we reported robust traffic growth across the majority of our countries of operations.

Argentina, our core business segment with over 10 million passengers in the quarter, posted strong passenger traffic growth – up over 11% year-on-year.

We continue to be encouraged with the 4% growth in traffic at Brasilia Airport in 1Q18 contributing to total traffic of 5 million passengers in Brazil, reflecting the inicipient economic recovery.

In other markets, Italy continues to report steady traffic growth up 2% year-on-year. We are also pleased to see our business in Ecuador show signs of recovery with a moderation in traffic declines. In the quarter, traffic was almost flat, declining 0.5%. This was a significant improvement from the 7% drop in the fourth quarter of last year.

I will now hand off the call to Raul Francos, who will review our operations and financial results. Please Raul, go ahead.

Raul Francos, Chief Financial Officer

Thank you, Martin. Good day everyone. I am pleased to be discussing our good performance during the first quarter of the year.

Turning to slide 5, we reported healthy growth with total revenues up almost 10.5% YoY. Excluding construction revenue and a one-time fee adjustment in Italy, total revenues would have increased a healthy 6.4% YoY.

Let me provide some details on what drove our good performance.

First, Aeronautical revenues were up almost 10% in the quarter, mainly driven by solid growth in Argentina, Uruguay and Armenia.

Second, commercial revenues were up over 4%, thanks to a good performance from our Armenian operations driven by higher fuel demand and prices. This was further supported by higher commercial revenues in Italy resulting from commercial initiatives and the appreciation of the Euro against the US dollar.

Other Revenue had some puts and takes in the quarter. On the positive side, we reported a $4.9 million one-time benefit related to the CPI inflationary effect of airport fees at Florence airport in Italy for the period 1999 through 2008 as per the Ministry of Economy and Finance. This was partially offset by $3.0 million related the reclassification in marketing support expenses in Italy from a change in the advertising agreement, which are deducted from Other Revenues, whereas in the past we had recorded these expenses in SG&A. Marketing support expenses in 1Q17 for an approximately similar amount are reported under SG&A expenses.

Moving down the P&L to slide 6, total operating costs and expenses increased almost 9% YoY to 288 million dollars.

Excluding construction costs and one-time IPO expenses of around 800,000 dollars, costs and expenses were up 4.5% YoY, which was below revenue growth.

Cost of services, excluding construction, were up slightly over 5.2% in the period. This was mainly due to higher cost of fuel in Armenia, higher salaries in Brazil from collective wage agreements and in Italy, from the appreciation of the Euro against the US dollar. Costs also reflect the impact of inflation on maintenance expenses in Argentina.

Although reported SG&A rose 1.2% YoY, excluding the one-time IPO expense, SG&A would have declined 0.6%. Note that SG&A this quarter reflects the reclassification of marketing support expenses in Italy from SG&A to Other revenues as I just explained. However, this decrease was partially offset by a $1.1 million increase in professional fees we incurred as a result of being a publicly-traded company and a $0.8 million increase in Brazil, mainly due to larger bad debt provisions and higher professional services fees.

Now, moving on to our profitability on slide 7.

Adjusted EBITDA was up almost 13% YoY reaching $137 million in the quarter.

However, there are a few one-time items worth mentioning. Excluding construction revenues and costs, along with the one-time IPO expense and concession fee gain I just discussed, comparable Adjusted EBITDA would have increased slightly over 9% YoY to $132 million. This represented a margin expansion of 98 basis points to 39% in the first quarter 2018.

This was principally driven by good results in Argentina supported by low double digits increase in passenger traffic in the period, with modest contributions from Armenia and Uruguay.

In terms of the balance sheet on slide 8, with a solid financial profile that provides the flexibility to pursue our growth plans.

Total net debt at the end of this quarter was approximately $950 million, down from $1.2 billion at December 2017 principally reflecting loans repaid by our Brazilian subsidiaries and by our holding company.

Our net debt to trailing 12 months adjusted EBITDA ratio improved to 1.99 times at the end of the quarter, compared with 2.74 times at year-end 2017.

Importantly, we have a healthy maturity profile, with only 8% of our debt maturing this year, and a balanced currency mix. At the end of the quarter, 57% of our debt was in US dollars, 28% in Reais and 15% in Euros.

Let me know turn the call back to Martin who will go over performance at our key business segments and will comment on our outlook.

Martin Eurnekian

Thanks Raul, I will now provide more details on our main business segments, **starting with Argentina on slide 9**

Revenues ex-construction were up almost 6% mainly driven by a 9% increase in aeronautical revenues.

We added new routes and airlines over the past twelve months supporting increased connectivity through the country as well as internationally. Some of the airlines driving international traffic, include, the daily flight to NY operated by United Airlines and several regional flights by Avianca. Let me also highlight low cost carrier Norwegian's direct route to London and the four weekly flights to Barcelona launched by Level, among others.

Servicing the domestic market, Aerolíneas Argentinas and Latam added more frequencies to existing routes in Argentina, and Flybondi, a low-cost carrier, started flying to several domestic destinations beginning in February of this year.

Now moving to profitability, higher traffic and cost dilution from the Argentine peso depreciation resulted in Adjusted segment EBITDA growth of almost 10% to $93.0 million in this quarter with adjusted EBITDA margin ex-IFRIC, expanding 170 basis points.

We were also busy in the quarter making improvements to our airports in Argentina. We invested almost $45 million in Argentina, mainly for the construction of a new terminal building and improvements to the runway and pre-boarding area at Ezeiza Airport, the remodeling of the terminal at Aeroparque Airport, the construction of a new terminal building and the expansion of the parking at Comodoro Rivadavia Airport, as well as runway improvements and parking expansion at Iguazú airport and the remodeling of the terminal at El Palomar Airport.

Moving forward, despite recent macroeconomic events in Argentina, we remain committed to investing in our airports to absorb expected passenger traffic growth. While the depreciation of the Argentine peso will likely impact domestic traffic, we expect international traffic demand to remain relatively stable over time. Our past experience shows that when the peso depreciates, over time we experience an increase in traffic from foreigners in Argentina that offsets the decline in residents going out of the country. Keep in mind also that in average around 85% of our revenues in Argentina are denominated in US dollars or dollar- linked while most of our operating costs are in Argentine pesos, which supports profitability.

Finally, we continue to work with the government to develop the capex program for the next years to satisfy this anticipated increase in passenger traffic.

Moving to Brazil, on slide 10, traffic increased 2.4% supported by continued signs of economic recovery from the recession we have experienced in the country in the past two years.

In line with our strategy, in the quarter we added new international and domestic routes and more frequencies to existing domestic destinations, which also contributed to this improved performance.

Keep in mind that growth was mainly driven by a good performance at our Brasilia Airport where traffic grew 4% YoY. Brazilia accounts for almost 87% of the total traffic in our Brazilian operations.

Revenues increased almost 1% YoY driven by passenger traffic and commercial initiatives and was partially offset by the depreciation of the Brazilian Real.

Adjusted Segment EBITDA remained stable at $4.2 million in the quarter, while margin declined 22 bps to 13.1%, reflecting higher salaries from collective wage agreements and bad debt provisions, partially offset by lower concession fees due to an increase in the discount rate used to calculate this fee. In local currency, Adjusted EBITDA margin expanded more than 200 basis points reaching low teens.

This quarter we invested $1.4 million for project structuring and completing the new firefighting system in Brasilia Airport and repair of the glass façade in Natal Airport.

Finally, taking a look at Italy on slide 11, we delivered strong revenue growth of 20.6% YoY.

Excluding construction and the one-time gain from the concession fee adjustment discussed before, revenues would have increased almost 7%, above steady traffic growth of 2%, driven by a couple of factors:

First, aeronautical revenues were up almost 16% mainly reflecting the appreciation of the Euro against the U.S. dollar.

Second, commercial revenues were increased over 30% driven by new advertising and ground transportation contracts along with higher revenues from the recently redesigned VIP lounge.

Note that revenues this quarter are net of $3 million in marketing support expenses as Raul just explained, while for the year ago quarter these costs were included within SG&A.

Moving to profitability, Adjusted Segment EBITDA was up $5.1 million, to $6.6 million. However, excluding construction services and the one-time concession fee gain, Adjusted Segment EBITDA margin contracted 51 basis points to 4.2% mainly due to lower cost dilution from the Euro appreciation.

Finally, we invested $2.3 million in the quarter mainly in the reconfiguration of the terminal at Florence Airport and Master plan development. We remain on track with our investment program and construction schedule at both airports, which is expected to start in the second half of this year

Looking ahead, we are cautiously optimistic that we will continue to see healthy dynamics in our markets, although we expect slower domestic passenger traffic growth in Argentina given the recent currency depreciation experienced in the country

By contrast, following the currency depreciation of the Argentine peso, international traffic in Argentina tends to remain relatively stable over time as the weaker currency makes traveling to the country more attractive, offsetting lower traffic from residents.

In terms of adjusted EBITDA margin, we benefit from this currency depreciation given that the majority of our revenues are denominated or linked to US dollars, while most our operational costs are in argentine pesos.

In Brazil, we are closely monitoring the macro environment and up-coming presidential elections and if these events could have an impact on our operations.

We have a clear vision for growth in our portfolio. A key component of this is further route development and added frequencies, and you heard us discuss the progress we made in recent months. Additionally, we are focused on expanding capacity in Argentina to absorb expected passenger traffic growth while in Brazil we remain focused on driving higher commercial revenues at Brasilia airport.

Furthermore, we are committed to making investments to strengthen our platform for long-term success while providing the best experience to passengers traveling through our airports. At the same time, we continue to assess new projects within our concessions, which we look forward to sharing with you as they materialize. Importantly, we have the financial resources to support this growth.

We are now ready to take questions please. Operator, please open the call for questions.

QUESTIONS AND ANSWERS

Operator

Yes, thank you. We will now begin the question-and-answer session. To ask a question, you may press *1 on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press *2. In order to allow all listeners to participate, please limit yourself to one question and one follow-up question. At this time, we will pause momentarily to assemble our roster.

And the first question comes from Stephen Trent from Citi. Please go ahead.

Stephen Trent

Hi. Good morning everybody, and thanks for taking my question. I actually was curious, just wanted to follow up on what you guys are seeing on the M&A side. So you had recently mentioned the airport auction in Jamaica as well as some potential to acquire some assets in Italy and I know you've done one of the two, I believe, taking an additional stake in your Italian concession. Just wondering if these are the two geographic spots we should continue to watch or if you are seeing opportunities in other parts of the world. Thank you.

Martin Eurnekian
Thank you, Stephen. This is Martin again. Well, as we discussed before, we are in the public process in Jamaica and we continue to analyze the situation. And we will make a decision whether or not to make a bid closer to the bid submission date. As for geographies in Italy, we remain with our opportunistic focus looking at different geographies but mainly focused in the areas where we feel more comfortable within the Americas and in Southern and Eastern Europe we still see some opportunities upcoming in [technical difficulty] but none that we see materializing in the near future. But we will continue to work on it and keep everyone posted as [technical difficulty].

Stephen Trent
Okay, Martin, appreciate that. Thanks very much.

Operator
And the next question comes from Bruno Amorim from Goldman Sachs. Please go ahead.

Bruno Amorim
Hi, good morning and thanks for the call. So, I have three questions if I may. The first one relates to your comments on the depreciation of the peso and the potential positive impacts on EBITDA going forward, which make all the sense. My question is just if as of the next tariff revision this could imply that tariffs in dollar terms would be reduced so that your returns are not much higher than the previously agreed return on investments?

The second question relates to margins in Brazil. EBITDA margin was 13% in the first quarter. I'd like just to understand what's your expectation going forward? Should it increase only through operational leverage as traffic grows or is there any other factor that could boost profitability in Brazil?

And the third question, you have mentioned a potential increase in traffic related to foreigners traveling into Argentina as a result of the currency depreciation. Is it possible to share with us the breakdown of inbounds versus outbound traffic in your international operations in the country? Thank you very much.

Martin Eurnekian
Well, thank you for your questions. On the depreciation side, yes, that creates an [unintelligible] increase for operations in Argentina. Regarding a tariff review, we cannot comment on what the government [technical difficulty] and the way they take all the calculations to arrive to the tariff provision. But I wouldn't expect an increase in the context of where we are deploying capital in Argentina where we are today. So, yes, we expect the margin increase but although [technical difficulty] of the process for the tariff provision, that wouldn't be expected.

Regarding margins in Brazil, the main game changer for our scenario out of the projects we are taking on regarding boosting commercial [technical difficulty] would have an effect on commercial revenues. We are constantly working on that major developments will come with the projects that are expected to be completed in about two years' time. Regarding traffic in Argentina, we usually give monthly traffic reports for all our operations. We have the overall traffic data coming from reliable sources. The breakdown from international versus domestically-generated traffic comes from different sources that are out of our control in surveys that we make. So, we do not [technical difficulty].

Bruno Amorim
Thank you very much.

Operator
And the next question comes from Ian Zaffino from Oppenheimer. Please go ahead.

Mark
Hi, good morning guys. This is Mark signing on for Ian. Thanks for taking our question. Just a quick one on, in terms of your balance sheet's trend and your sound financial flexibility and [unintelligible], what are some…

Martin Eurnekian
I'm sorry, can you speak louder or away from the microphone? I get a blurry sound that I cannot understand. Sorry.

Mark
Oh, yeah, I'm sorry. I was just wondering in terms of your balance sheet and financial flexibility, is there is any additional capital allocation strategy that you could share in terms of, you know, maybe like additional M&A or deleveraging. Anything around there would be much appreciated. Thank you.

Martin Eurnekian
Thank you. The sound was not good but as far as I understand, you were asking about capital allocation and how that profile is going to look and [technical difficulty] deleveraging or those sorts of strategies. What I can tell you is that most of our debt is at the OpCo levels and is amortizing debt. So, we, what we expect is to keep the amortizing schedule that we have today, and we do not foresee major (technical difficulty] debt profile in the near term.

Mark
Okay, great. Thank you very much.

Martin Eurnekian
Comments we also have, what we might do is take additional debt required by the Capex program that we have discussed previously in the preoperations or business [technical difficulty] plans for Capex expansions such as Argentina, Brazil, and Italy, where we have two-year Capex programs that we are currently executing.

Mark
Okay, great. Thank you very much.

Operator
And once again, if you would like to ask a question please press star (*) then one (1).

And the next question comes from Gabriela Benjamin from NFL. Please go ahead.

Gabriela Benjamin
Hi, yes. My question is in regard to the negotiations with the Argentine government and two-fold. Will there be a tariff revision this year in both the domestic and the dollar-denominated international tariff? And if so, when would that be? And the second question is in regard to the

Capex for the extension of the contract, if there is a date of when those negotiations are going to conclude? Thank you.

Martin Eurnekian
Can you repeat the first part of the question please?

Gabriela Benjamin
Sure. The first part of the question is if there will be a tariff adjustment this year and if so, when. For the domestic and international tariffs; the domestic to re-pass inflation and the international to adjust for the FX.

Martin Eurnekian
Okay. So, regarding tariff revisions, we expect that to happen, but we cannot say when. It's up to the regulatory body to finish their work and come up with the result of the revision with a possible tariff increase. The tariff will reflect the framework of the contract we have in Argentina [technical difficulty] some relationship with inflation and currency exchange. But it's not directly linked to that, so we would expect the government to finish their work and publish the results.

Gabriela Benjamin
Okay, great. And what...

Martin Eurnekian
Capex?

Gabriela Benjamin
Yeah, yes, the Capex.

Martin Eurnekian
Okay, can you repeat that please? The sound is [technical difficulty]. Speak slowly.

Gabriela Benjamin
Yeah, the line on your line is also breaking up occasionally. It's regard to the Capex that you are negotiating with the Argentinian government to possibly have an extension of the contract, if there's any timing on that?

Martin Eurnekian
Well, the timing, it is available to discuss. It is available to discuss. [Technical difficulty] has taken by hiring a consultant to do work for them regarding our concession. That work is expected to end in three to four months as far as we know. And after that, we hope a new negotiation table will be created to begin this process. But as far as we can see through the process, it will not begin for the next three to four months.

Gabriela Benjamin
Okay. Thank you.

Operator
And once again, if you have a question please press star (*) then one (1).

And the next question is a follow up from Stephen Trent. Please go ahead.

Stephen Trent

Thanks again, everybody. Just one other from me. With the dislocation we're seeing in the markets recently, I know there's several airlines that are still launching operations within the region. And I'm aware of only maybe Latin America Wings, which has maybe shut down its operations, and I'm wondering what you're seeing in the ebb and flow of new airlines. Are they generally sticking to their plans or do you sense any of these folks taking a more conservative view on their growth trajectories?

Martin Eurnekian
Well, as far as the contracts we have with airlines, most of them have expressed interest to set up operations in Argentina are continuing with their work. The only one that has expressed the need for some delay in beginning operations is Norwegian that has kept their workforce in Argentina and continued to do work towards establishing a domestic airline in Argentina but has said that [technical difficulty] a delay regarding issues on their programming at the headquarter level. The rest of the companies that have set up or are setting up, we see movement and activity that does not signal a stop or a change in that sense.

Stephen Trent
Okay. Got it, appreciate that. Thanks for the color, Martin.

Operator
And once again, if you have a question please press star (*) then one (1).

And this concludes our question-and-answer session. I would like to turn the call back to Martin Eurnekian for any closing remarks.

CONCLUSION

Martin Eurnekian
Well, thank you everybody for joining us today. Thank you all for your questions and we remain available as a team and will keep our work focused mainly on execution of our business plans in the current business segments. [technical difficulty] If we have some more news to share with you. Thank you very much.

Operator
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.