

# Corporacion America Airports

## Fourth Quarter 2018 Earnings Conference Call

Thursday, April 11, 2019, 9:00 AM Eastern

### **CORPORATE PARTICIPANTS**

**Martín Eurnekian** - *Chief Executive Officer*

**Raúl Francos** - *Chief Financial Officer*

**Jorge Arruda** - *Finance and M&A Manager*

## **PRESENTATION**

### **Operator**

Good morning and welcome to the Corporacion America Airports Fourth Quarter 2018 Earnings Call. A slide presentation accompanies today's webcast and is available in the Investor Section of Corporacion America Airports Investor Relations website at <http://Investors.corporacionamericaairports.com>. As a reminder, all participants will be in listen-only mode. There will be enough opportunity for you to ask questions at the end of today's presentation.

As a reminder, this call is being recorded. And at this time, I would like to turn the call over to Gimena Albenesi of Investor Relations. Please go ahead.

### **Gimena Albenesi**

Thank you. Good morning, everyone, and thank you for joining us today. Speaking during today's call will be Martín Eurnekian, our Chief Executive Officer, and Raúl 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.

I also would like to remind you that following the categorization of Argentina as a highly inflationary economy in accordance with IFRS, commencing July 2018, we began applying IFRS rule IAS 29. This rule applies retroactively starting January 1st of 2018. For comparison purposes, in addition to presenting As Reported results, we are also disclosing the isolated impact of the adoption of hyperinflation accounting in Argentina, and our results excluding rule IAS 29.

Additional information in connection with the application of rule IAS 29 can be found in our earnings report. Note that for comparison purposes and a better understanding of the underlying performance, in our presentation today we will be discussing results, excluding hyperinflation accounting in Argentina.

Now, let me turn the call over to our CEO, Martín Eurnekian.

### **Martín Eurnekian**

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

I will begin my presentation with a discussion of the highlights of the quarter, and then Raúl 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 the year. We will then open the call to your questions.

Starting with Slide 3, 2018 was a challenging year, with travel dynamics and results impacted by the unfavorable macro environment and the sharp devaluation in Argentina, our largest market, and to a lesser extent in Brazil.

Beyond these headwinds, we served over 81 million passengers across our airport network, up 6 percent year-on-year, as we continued to add new routes and airlines--and began operations at El Palomar, our newer airport targeting low-cost airlines in Argentina. Excluding inflation accounting, adjusted EBITDA margin ex-IFRIC for the year expanded 190 basis points to almost 37 percent, and adjusted EBITDA increased by low-single digits.

Looking at the fourth quarter specifically, adjusted EBITDA ex-IAS 29 declined almost 19 percent and margin ex-IFRIC contracted approximately 330 basis points year-on-year, impacted by the difficult economic conditions in Argentina, as inflation in the country is catching up with currency depreciation, reducing the strong operating leverage experienced in the third quarter.

This more than offset the strong performance in other markets. For example, Brazil delivered a nearly 61 percent increase in comparable adjusted EBITDA, excluding one-time items, while Italy reported 40 percent growth in adjusted EBITDA. These good results were further supported by the majority of our other countries of operations.

With the goal of positioning the company for expected future growth and further enhancing the passenger experience, we continued to advance our capex program during the year. During the fourth quarter, we made capital investments of nearly US\$70 million with full year spending reaching US\$257 million. Investments were largely focused on our airport infrastructure, mainly in Argentina and Italy.

Key investments for the full year included the start of the construction of the new departure terminal and multilevel parking at Ezeiza Airport in Argentina, expected to begin operations this year, and the start of the expansion of Aeroparque Airport. We also undertook the expansion of regional airports, including the Jujuy, San Juan, Comodoro Rivadavia, and Iguazú Airports.

In Brazil, on the back of the four new international flights announced by Gol, we made capital investments at our Brasilia Airport to expand the international boarding, baggage claim, and duty-free areas. We also invested in the construction of runway safety areas.

Let me take a moment to give you an update on our commercial project at Brasilia Airport. We have redefined the project originally contemplated for this airport and are now planning a lower capital-intensive model. This new commercial space will be funded and operated by third parties with the airport receiving a percentage of the net operating income of the complex.

We have also been busy in Italy. We are particularly pleased with the conclusion of the environmental and urban impact studies and approvals with respect to our expansion plans at the Florence Airport. We are awaiting the final approval by the Ministry of Transport and expect to initiate works in the fourth quarter of 2019. We also started the expansion of the terminal building at Pisa Airport, aiming to accommodate expected passenger growth.

An important event in the year was the agreement we entered into with Investment Corporation of Dubai to jointly identify and develop new opportunities in the airport sector in Italy, Eastern Europe, and the Middle East.

Finally, in our other markets, note that we have successfully extended by five years our concession agreement in Ecuador, which we executed last July. Additionally, this month we extended for another 14 years the concession agreement in Punta del Este, Uruguay.

Moving to Slide number 4, traffic growth for the fourth quarter slowed to nearly 4 percent year-on-year, mainly driven by Argentina, negatively impacted by difficult macro conditions and sharp FX volatility, as already mentioned.

Passenger traffic in Argentina continued to decelerate, up to 4 percent from almost 6 percent in the third quarter, reflecting the overall slowdown in travel demand. We also continued to see a mix shift in traffic, with more affordable domestic travel up 12 percent year-on-year, while international traffic declined over 8 percent. In Brazil, traffic growth decelerated to nearly 3 percent year-on-year, from over 5 percent in the third quarter.

Italy posted a strong performance with traffic up 5 percent compared to 3 percent in the prior quarter. The addition of new routes and airlines drove a pick-up in international traffic, more than offsetting the softer domestic travel demand.

In Uruguay, traffic contracted almost 3 percent year-on-year as performance remains affected by softer travel demand from Argentina. However, we saw a seasonal improvement from the 5 percent drop experienced in the prior quarter.

Traffic in Armenia remains strong, up close to 12 percent, mainly due to the addition of new frequencies to destinations in Russia. Ecuador continued to post a strong performance with traffic up over 7 percent, reflecting the addition of new routes in the year, while Peru posted a slowdown in traffic growth following the suspension of operations of a low-cost airline.

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

### **Raúl Francos**

Thank you, Martín. Good day, everyone.

As Gimena noted at the beginning of our presentation, for a better understanding of our performance, we will discuss our results, excluding the impact of hyperinflation in Argentina.

Note, however, that in the fourth quarter 2018 the application of IAS 29 resulted in a positive impact in reported numbers when compared to the previous accounting, given that the indexation effect exceeded the translation impact from using the closing exchange rate as opposed to using the average rate for the reported period.

Starting with the top line on Slide 5, total revenue declined close to 13 percent year-on-year to nearly \$363 million, and 9 percent when also excluding construction revenues.

Consolidated revenues were impacted the mix shift from international to domestic traffic as well as lower travel demand in Argentina. Revenues were also affected by the FX translation impact from the strong currency depreciation of both the Argentine peso and the Brazilian real.

Aeronautical revenue declined 7 percent, mainly due to weaker international traffic in Argentina and currency depreciation in Brazil. By contrast, we are very pleased with the results we are seeing in Ecuador and Armenia, posting another quarter of revenue growth.

Finally, in Italy traffic increase is not entirely reflected in the revenue line, given that again this quarter marketing support expenses are deducted from revenues while in the year-ago quarter they were included in SG&A.

Commercial revenue declined 12.4 percent year-on-year, mainly reflecting lower demand in Argentina and the FX translation impact in both Argentina and Brazil. In local currency, commercial revenues in Brazil increased 16 percent, benefiting from higher VIP lounge and advertising revenues, together with higher cargo volume.

In Italy, our initiatives to enhance our service offering, coupled with higher traffic growth, are showing positive results, while Armenia continued to perform well with growth mainly driven by higher fuel demand and prices.

Turning to our cost structure in Slide 6, this quarter we saw lower cost dilution, particularly in Argentina, our largest market, as inflation is catching up with the strong currency depreciation we experienced through the year. The mix shift in revenue from international to domestic also contributed to lower cost dilution.

While cost of services ex-IFRIC 12 declined almost 5 percent year-on-year, as a percentage of revenue we saw an increase of over 300 basis points. This was mainly due to lower labor cost dilution arising from salary increases, reflecting both growth in the employee base, mainly in Argentina, inflation adjustments, as well as higher maintenance costs.

SG&A in turn, was down slightly over 1 percent year-on-year but increased as a percentage of revenue, impacted mainly by the increase in bad debt charges in Brazil related to Avianca Brazil receivables, partially offset by lower sales taxes in Argentina. SG&A included one-time items in both quarters: IPO expenses in the fourth quarter 2017 and the write-off of the commercial project in Brazil due to its recent redefinition this quarter, as Martín just mentioned.

Moving on to profitability, on Slide 7 adjusted EBIDTA ex-IFRIC declined 18.6 percent to \$87 million in the quarter. Growth in Italy, Armenia, and Uruguay was more than offset by the weak performance in Argentina and, to a lesser extent, in Brazil.

In addition, adjusted EBITDA margin ex-IFRIC contracted over 330 basis points to almost 28.1 percent from 31.4 percent in the same quarter of last year. As we anticipated in our last earnings call, the strong margin expansion we saw in our previous quarter moderated as inflation is catching up with the currency depreciation in Argentina, reducing the benefits from the currency devaluation on costs.

In addition, as I mentioned in the previous slide, non-recurring items in Brazil also impacted the margin. More details of this non-recurring items are included in the earnings release published this morning.

Moving to the bottom line, despite lower operating results, our net income showed a significant increase due to a positive variance in non-cash foreign exchange gains in Argentina, mainly arising from the U.S. dollar denominated debt as the peso appreciated during the quarter. This was partially offset by higher income tax expenses recorded in the quarter.

As shown on Slide 8, we continue to maintain a healthy balance sheet that provides financial flexibility to continue developing our strategic initiatives. Total debt at the close of the quarter was relatively stable at \$1.1 billion. Our net debt to last 12 months adjusted EBITDA ratio slightly decreased to 2.0 times from 2.1 times in the prior quarter.

Importantly, we maintain a conservative maturity profile with around 10 percent of our debt maturing within the year and an adequate currency mix with about 60 percent of our debt denominated in U.S. dollars, 20 percent in reals, and 14 percent in Euros.

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

### **Martín Eurnekian**

Thank you, Raúl. Starting with Argentina on Slide 9, revenues ex-IFRIC declined 16 percent year-on-year despite the 4 percent increase in passenger traffic, impacted by several factors. We continue to experience overall slower travel demand, along with a mix shift from international to lower-price domestic destinations. This resulted in a 12 percent increase in domestic traffic and an 8 percent drop in international travel.

As the country is experiencing a challenging macro environment, we are seeing a sustained increase in activities from low-cost airlines. For example, during the fourth quarter, Norwegian Air Argentina started local operations with five domestic routes, while Chilean low-cost carrier JetSmart launched international operations from El Palomar, designated an international airport last October, and Flybondi added routes to Paraguay and Punta del Este.

At the same time, aeronautical revenues from domestic passengers and a portion of our commercial revenues that are peso denominated remain affected by the FX translation impact from the sharp peso depreciation that took place in the third quarter. We are also seeing lower commercial revenues from international passengers, particularly in duty-free. Revenues were also negatively impacted by the mix shift in cargo volume, with higher export activity and the sharp reduction in higher-margin imports.

Against this backdrop, adjusted Argentine segment EBIDTA declined nearly 27 percent and ex-IFRIC 12 margin contracted approximately 514 basis points to 35.7 percent. Differently from the third quarter and as anticipated in our prior earnings call, the impact from higher inflation on cost of services more than offset the benefit from the currency depreciation on our peso-based costs as inflation is catching with the peso depreciation.

We continued to advance our capex program in the country and invested \$56 million in Argentina. Funds were mainly allocated to the construction of the new departures terminal building and multilevel parking at the Ezeiza Airport, the repavement of the runway and new terminal building at Comodoro Rivadavia Airport, the construction of new terminal buildings in Iguazu and Jujuy Airports, as well as several other investments across other airports in our concession, as I mentioned earlier.

Our capex program is targeted to absorb future passenger traffic growth. We continue supporting the government's Airplane Revolution Plan and plan to invest between \$250 million to \$300 million this year to be funded with cash flow from operations. This is in line with the capex program we are developing closely with the government.

Now, please turn to Slide 10 for a discussion about Brazil. Total traffic in Brazil increased nearly 3 percent year-on-year--although a slowdown from the prior quarter. Along with the gradually improving macro environment, growth was supported by the addition of new domestic and international routes opened by Gol in the fourth quarter of 2018, partially compensating the fleet adjustment at the leading Latin American airline and difficulties at a Brazilian airline.

Local currency revenues were up nearly 12 percent year-on-year, driven by the growth in both aeronautical and commercial revenues. We are very pleased with the good performance in commercial activities resulting from the new commercial agreements and higher cargo volumes. On a reported basis, however, revenues declined almost 5 percent, impacted by the FX translation effect from the depreciation of the Brazilian real.

Adjusted segment EBITDA, in turn, was down 80 percent to \$2 million, with the margin contracting to almost 6 percent from 27 percent in the prior-year quarter. This was mainly due to a nearly \$4 million bad debt charge in connection with a Brazilian carrier and a \$3 million write-off resulting from our decision to no longer deploy capital to construct the new commercial area at Brasilia Airport and instead develop a lower-risk model, as I explained earlier. This was partially offset by lower SG&A.

We invested over \$4 million during the quarter for the expansion of the international boarding areas, together with the construction of runway safety areas and engineering projects at Brasilia Airport.

Now moving to Italy on Slide 11. Traffic trends remain strong, up 5 percent year-on-year, driven by international traffic growth. Comparable revenues ex-IFRIC, and excluding marketing support expenses, remained flat in the quarter. We posted a good performance at our new retail and duty-free stores at Florence Airport as well as higher car rental revenues from new areas opened in November.

Adjusted segment EBITDA was up an impressive 40 percent, and adjusted segment EBITDA margin ex-IFRIC expanded by over 526 basis points to 16.6 percent in the quarter. We invested over \$7 million in the quarter, mainly for the expansion of the terminal at Pisa Airport and master plan development at Florence Airport.

Now that we have concluded the environmental and urban impact studies, we expect to obtain final approval in the next few months and to start construction of the Florence Airport expansion in the fourth quarter of 2019.

Now, please turn to Slide 12. To wrap up our presentation, while 2018 was a challenging year marked by significant macro and FX volatility in Argentina and to a lesser extent in Brazil, which impacted our results, we continue to make progress on our strategic initiatives, further strengthening our airport platform for when the macro environment improves.

Looking into the current year, we expect travel trends in Argentina to remain impacted by the difficult economic dynamics in the country in addition to the added uncertainty of this being a presidential election year. While we expect the macro backdrop to improve gradually in the second half of the year, given the lag between the purchase decision and the actual travel date, an overall pick-up in international traffic trends in Argentina is anticipated to flow into our results in early 2020.

Domestic travel is expected to continue to improve throughout the year as connectivity continues to increase in the country. We also expect to see an ongoing gradual pick-up in inbound international traffic as traveling to Argentina becomes more affordable on the back of the weak peso but not fully offsetting the fall-off in outbound traffic by locals. Taking these factors into account, we expect to see a single-digit increase in total passenger traffic growth in Argentina for the year.

By contrast, in Brazil we expect to see the economy continue its improving trend with traffic growth continuing throughout the year. This is mainly the case for international passenger traffic, which is benefiting from the recent opening of international routes. We see a similar positive trend in Italy, complemented by solid traffic trends in our other markets.

We remain fully committed to elevating the travel experience across our airports, developing new routes and frequencies. We are continuing to expand infrastructure, mainly in Argentina and Italy, further strengthening our global platform for long-term success.

This is the end of our prepared remarks. We are now ready to take questions. Operator, please open the line for questions.

**Operator**

We will now begin the question-and-answer session. If you would like to ask a question, please press star, then one, on your telephone keypad. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star, then two. We ask that you limit yourself to one question and one follow-up. You may re-queue for additional questions. And at this time, we will pause momentarily to assemble our roster.

And our first question today comes from Roberto Otero with Bank of America. Please go ahead.

**Pedro Mariani**

Hi, gentlemen. Actually, this is Pedro here. Thanks for taking my question. I have one quick question from our side and (unintelligible) on AA2000. Could you give us any update on the ongoing negotiation with the government regarding the concession 10-year extension. In your view, how should the upcoming election impact your negotiation, and if you could give us a sense of timing. Should we expect any final terms happening in 2019, or maybe it will be more conservative to assume this happening only in 2020 onwards? That's my question. Thanks.

**Martín Eurnekian**

Hello, this is Martín Eurnekian. Thank you for your question. It would be difficult for me to give you an idea on when the government will be ready. We are engaging with them as often as possible to understand, when can we officially launch a negotiation. To be honest, the fact that we have entered the election mode in Argentina has, at least in our perception, shifted the administration's priorities in terms of what they need to achieve because, as you probably understand, everybody goes into election mode once we start getting closer to the primaries and presidential elections.

So, this is the feel that I can give you. Although not impossible to do a negotiation this year, I think that the fact that everybody is focusing on elections puts a little bit of strain in that possibility of being able to really close before the end of the year.

**Pedro Mariani**

All right, Martín. Thanks for taking my question.

**Operator**

And our next question comes from Ian Zaffino with Oppenheimer. Please go ahead with your question.

**Mark Zhang**

Hey, good morning, guys. This is Mark on for Ian. Thanks for taking our question. So, if you guys could provide a little bit more detail on the sort of the time line of the capital spend, particularly at A2000, it would be much appreciated. Can you potentially give us a sense of when Ezeiza will open in 2019, just like a first-half or second-half event, and what sort of the time line on the Aeroparque expansion? That would be much appreciated. Thank you.

**Martín Eurnekian**

We have a set of inauguration, Mark, set for this year, Ezeiza being the main one. As of today, the set date for the inauguration of the new terminal in Ezeiza is the end of September, but that will be fine-tuned with the group that is doing the actual capex and the government as well. For the rest, we have a calendar for opening of the works that we've been doing so far, and we can definitely provide that to you, but it will publicly announced each time we decide on an exact date for the openings that we have this year.

**Mark**

Terrific. That's very helpful. Thank you guys very much.

**Operator**

And once again, if you would like to ask a question, please press star, then one. And our next question comes from Bruno Amorim with Goldman Sachs. Please go ahead.

**Bruno Amorim**

Yes, hi. Good morning. I have two questions. So, the first one is out of the additional \$1 billion dollars in capex expected to be included in the concession agreements in Argentina, how much have you already done so far? And also has the regulator recognized or authorized this investment, or is it something to be discussed only when the additional \$1 billion is approved by the regulator?

And the second question is when should we expect to see the next tariff revision in Argentina? Is this negotiation tied with the discussion around concession renewal and additional investments for \$1 billion dollars, or are those separate discussions? Could we see tariffs being adjusted before the final decision on the extension? So, those are my two questions, please.

**Martín Eurnekian**

Thank you. First, the two things are totally separate. According to our current contact, the tariff revisions should be done yearly. The regulator is a little bit late as far as we know and for the interactions we have. They are getting ready to finish the exercise to be able to publish it. It's not a negotiation. They have to run the numbers and do the adjustments. So, it's not linked to any negotiation or anything else whatsoever.

Regarding the capex question, as the discussion we are having end of 2018, we were either at the number agreed in the concession contract in terms of total capex for the concession or a little bit or slightly beyond that number. So, for 2018, that is the fact. For 2019 is where we are going beyond that number. But, everything we do is approved by the regulator and taken into account into the regulatory accountancy of the concession contract.

**Bruno Amorim**

Very clear. Thank you very much.

**Operator**

And this will conclude our question-and-answer session. I would like to turn the conference back over to Martín Eurnekian for any closing remarks.

## **CONCLUSION**

### **Martín Eurnekian**

Well, thank you very much for joining us today. We really appreciate your interest in our company. We look forward to meeting more of you over the coming months and providing financial and business updates the next quarter. In the meantime, the team remains available to answer any questions that you may have.

Thank you again, and enjoy the rest of your day.

### **Operator**

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