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TGSU2.BA - Q3 2018 Transportadora de Gas del Sur SA Earnings Call

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PRESENTATION

Operator

Good morning. My name is Tim, and I will be your conference operator today. At this time I would like to welcome everyone to TGS Third Quarter 2018 Results Earnings Conference Call. TGS issued its earnings report yesterday. If you did not receive a copy via e-mail, please do not hesitate to contact us in New York City at (646) 284-9435.

Before we begin the call today, I would like to remind you that forward-looking statements made during today's conference call do not account for future economic circumstances, industry conditions and company performance and financial results. These statements are subject to a number of risks and uncertainties. All figures included herein were prepared in accordance with International Financial Reporting Standards and are stated in nominal Argentine pesos, unless otherwise noted.

Joining us today from TGS in Buenos Aires is Alejandro Basso, Chief Financial Officer; Leandro Perez Castaño, IR and Finance Manager; and Carlos Almagro, Investor Relations Officer.

And now I would turn the call over to Mr. Basso. Sir, please begin.

Alejandro M. Basso - *Transportadora de Gas del Sur S.A. - CFO & VP of Administration, Finance & Services*

Thank you. Good morning, everyone, and thank you for joining us today on this conference call to discuss the third quarter earnings and highlights for Transportadora de Gas del Sur. Before I begin the discussion of our earnings, I would like to briefly talk about our relevant events occurred during the quarter.

First, the Board of Directors approved[dividend] payments for a total of ARS 3.7 billion, which corresponded to the earnings of 2016 and 2017. At the end of September, ENARGAS issued Resolution No. 265, which established a tariff increase of almost 20% to be effective as of October 2018 and which is lower than the Wholesale Price Index increase of 30.5%.

It is worth noting that for the semi-annual tariff adjustment Resolution 4362, issued by ENARGAS in March 2017, establishes that the Wholesale Price Index should be applied. However, the Regulatory decided to apply a lower tariff increase, resulting from the average wholesale price, together with the construction cost and the (inaudible) indexes. This decision was made based on some language containing Resolution 4362 for which ENARGAS understands that it may use other indexes under certain macroeconomic conditions. Nonetheless, TGS is evaluating what options will be taken forward to be compensated as a result of this lower tariff increase.

Moving on to the share buyback program. As you remember that we launched that program in May, which expired in September. So we have launched a new program for a period of [880]days and up to a maximum amount of ARS 1.8 billion. As of today, we have bought almost 2% of the total capital stock.

On other news, (inaudible) will reach a 10-year agreement with PBB Polisur, which will allow us to secure attractive margins in dollars for the sale of increasing volumes of ethane until the end of 2027.



Finally, we signed a Memorandum of Understanding with Excelerate Energy to jointly collaborate on the assessment of liquefaction project next to Cerri Complex in Bahía Blanca. The project aims to study the technical and commercial viability of liquefying and exporting natural gas during the summer season, allowing the gas producers to sell natural gas production when the local demand is lower. The study is expected to be completed by the end of 2018.

As we move on to the Slide 4, I will now give you a brief explanation of 2018 third quarter results. Figures are expressed in pesos, and comparisons are made with the same period of 2017. As you can see, we recorded a net income of ARS 784 million, an increase of 51% in this period. The increase is mostly explained by higher operating income of almost ARS 2.9 billion, which was partially offset by a negative variation of the financial results of ARS 2.6 billion.

Moving on to Slide 5. You see, we recorded higher Natural Gas Transportation revenues during the third quarter, increasing by 197% to almost ARS 3.5 billion compared to close to ARS 1.2 billion in the same period of 2017. The increase is mostly due to higher tariffs, which came into effect in April 2018 at 50% and in December 2017 at an average of 78%, both of which generated higher revenues of ARS 1 billion and almost ARS 900 million, respectively.

On Slide 6, you can see that the revenues generated by production and commercialization of Liquids almost tripled. To a greater extent, the main variation is related to a higher average U.S. dollar exchange rate, which increased by more than 80% and generated higher revenues of ARS 1 billion.

Secondly, we also exported higher volume of Liquids, more than 45,000 tons boosting our revenues by ARS 744 million. Additionally, higher (inaudible) local prices explained the ARS 479 million increase along with 11% increase in the volumes of ethane sold during the third quarter of 2018, which also had a positive effect of ARS 111 million.

As shown on Slide 7, Other Services revenues rose by 134% to ARS 504 million. This increase is mainly explained by a higher foreign exchange rate average, which generated higher revenues amounting to ARS 175 million. Furthermore, additional construction services rendered increased revenues by ARS 124 million. These construction services are (inaudible) to a joint venture under the national public bid, which we won last year to expand the gas network in the province of Santa Fe.

On Slide 8, we can see the variation in the cost of sales, which rose 135% to almost ARS 3.3 billion. This is primarily explained by higher cost of the natural gas used in the Liquids business, which rose ARS 1.3 billion. Of this total, ARS 845 million are related to higher natural gas prices in pesos mainly due to the huge increase in the average foreign exchange rate. The other ARS 459 million were related to a 22% increase in the volumes of natural gas purchase during the third quarter of 2018.

In addition, operating cost of the Natural Gas Transportation business segment rose by ARS 302 million and labor cost by ARS 121 million.

Moving on to the Slide 9, administrative and selling expenses rose by 119% to ARS 511 million. The increment is mostly attributable to an increase in turnover tax of ARS 141 million, which is mostly related to the higher regulated revenues along with higher labor cost of ARS 50 million.

In addition, starting September 1, a new tax on export regime was implemented by the Argentine government where a tax of ARS 4 per dollar is to be paid for exports. During the first month, we paid ARS 20 million.

On Slide 10, we can see the financial results for the third quarter showing a negative variation of ARS 2.6 billion. This variation is mainly explained by significant peso devaluation during the third quarter of 2018, during which the foreign exchange rate increased by 43%, impacting our net dollar-denominated liability, which resulted in a loss of more than ARS 3.1 billion compared to ARS 100 million in the third quarter of 2017. This negative effect was partially compensated with a higher interest income earned during the third quarter of 2018 as our total average financial investment denominated in pesos, and the average yield were much higher. This concludes our presentation.

I will now turn the call back to the operator, who will open the floor for questions. Thank you.



QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Bruno Montanari of Morgan Stanley.

Bruno Montanari - *Morgan Stanley, Research Division - Equity Analyst*

Just wondered if you could get -- to give us a little bit more color on the new contract you signed with (inaudible) in terms of volume, if there was any revision to the prices of ethane you're getting on that contract? So that would be great.

Alejandro M. Basso - *Transportadora de Gas del Sur S.A. - CFO & VP of Administration, Finance & Services*

Bruno, it's Alejandro Basso. Okay. The new contract with (inaudible) Chemical Company, it's a 10-year contract with higher volumes. Volumes -- current -- for last year, we have volumes of almost 800 tons per day. This new contract starts with 850 tons per day, going up to [1,850] tons per day in 5 years, okay? In terms of price, it's quite similar to the previous contract. So we're just expecting may be higher -- this just higher volumes, okay? The price...

Operator

Our next question comes from the line of Sofia Ordoñez of Bradesco.

Sofia Ordoñez - *Bradesco S.A. Corretora de Títulos e Valores Mobiliários, Research Division - Research Analyst*

I just wanted to ask you about the volumes of propane sold. I'm looking at the third quarter, and they were significantly higher than the third quarter of last year. So I was wondering if these higher volumes should be sustainable in coming quarters.

Alejandro M. Basso - *Transportadora de Gas del Sur S.A. - CFO & VP of Administration, Finance & Services*

Higher volumes in the Liquids side are due to the additional gas that the gas producers are injecting in our system due to the Vaca Muerta developing, okay? So we think that it should be sustainable in the future, okay?

Operator

(Operator Instructions) There are no further questions over the audio portion of the conference. I would like to turn the conference back over to management for closing remarks.

Alejandro M. Basso - *Transportadora de Gas del Sur S.A. - CFO & VP of Administration, Finance & Services*

Okay. Thank you for participating in TGS Third Quarter 2018 Conference Call. We look forward to speaking with you again when we release our fourth quarter 2018 results. However, if you have any questions in the meantime, please do not hesitate to contact our Investor Relations department with any questions. Have a good day.



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