Pampa Energía Q2 2019 Conference Call

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Presenting:
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Gabriel Cohen, CFO
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Good morning everyone and thank you for joining our conference call.

I will briefly go through every business segment reviewing the quarter's key figures and the latest events since our last call in May. Our CEO Mr. Gustavo Mariani and CFO Mr. Gabriel Cohen are joining us for Q&A session.

Last April, Pampa adopted the US Dollar as functional currency, therefore transactions are recorded in US Dollar since January of this year. For the comparative period of 2018, according to IFRS figures are reported in Pesos adjusted by inflation as of December 31, 2018 and shown in US Dollar at closing FX. This comparison might be difficult to read as inflation outpaced devaluation by 20%. Therefore, for a like-for-like basis, to analyze the performance organically we are considering nominal figures reported last year Q2 and converted to dollars at average FX.

In the case of Refinor and our utilities Edenor, Transener, TGS and OldelVal, which are mostly Peso-linked businesses, they continue to have functional local currency, so they keep reporting in pesos adjusted by inflation, figures are shown in US Dollar converted at June 2019's closing FX. In order to analyze the performance organically and to be in line with their reporting, the comparative figures is in Pesos adjusted by inflation until the end of June and shown in US$ at June's 2019 closing FX.

So, having made this clarifications, we can start. On slide 5, we wanted to make a quick stop by reviewing the quarter's financial highlights. Revenues fell year on year by 3%, mainly because of lower gas prices, reduced legacy power plants' remuneration and the impact of devaluation higher than inflation in our Peso-linked businesses. These negative effects were offset by the commissioning of new capacity since June 2018, adding more than 400 MW to the grid, higher sales due to gas pass through at power generation and one-time sales billed to the Federal Gov't regarding to shantytowns consumption and reimbursement of social tariff benefits at Edenor. On the other hand, quarter on quarter revenues improved by 12%, mainly because of higher gas production, new wind farms and gas turbines online since last May and this one-time sales I mentioned before at Edenor.

EBITDA also fell year on year by 11%, mainly explained by lower gas prices and the expiration of Plan Gas at E&P, reduced legacy power plants' remuneration and devaluation effect on our Peso inflation-adjusted utilities, partially offset by Edenor's lagged revenues recorded last May and lower peso-link expenses due to deval. Quarter on quarter, EBITDA keeps improving, having increased by 22% mainly because of higher gas production, billing of new PPAs at our wind farms PEPE 2 and 3 and Edenor's lagged sales.

As we show on right below, oil and gas share keeps at one-third of Pampa's consolidated EBITDA given the current pricing environment at E&P, while electricity, led by power generation, takes the other two-thirds. Also, it is worth to highlight that almost 60% of Pampa's consolidated EBITDA is dollar-link, mainly from gas and power.

Moreover, as shown in the chart left below, in the second quarter of this year our capex decreased 12% compared to the same period of last year, mainly explained by lower expansion capex in oil and gas segment and because on Q2 2018 we commissioned Mario Cebreiro wind farm, partially offset by further investment on Genelba's closing to CCGT ongoing project and Edenor's maintenance and catch up investment plan. If we compare to the last quarter, capex increased 21%, mainly driven by capex for the commissioning of PEPEs wind farms, increased gas production mainly at El Mangrullo block.

So, as you can see on slide 6, the adjusted EBITDA in the second quarter of 2019 recorded 266 million dollars, 11% less compared to an EBITDA of 300 million dollars recorded in the same period of 2018, mainly explained by decreases of 34% in oil and gas, 21% in holding and others and 6% in power generation, partially offset by increases of 17% in electricity distribution, and to a lower extent, to petrochemicals.

Moving to power generation segment, during the second quarter of 2019 we posted an adjusted EBITDA of 100 million dollars, 6% lower than Q2 2018, mainly given by a reduction in legacy thermal remuneration as per Resolution 1, effective from March 2019, by which capacity payments during autumn season of April and May have been reduced around 40% in dollars for Güemes' steam turbines and Piedra Buena, as they are the lowest dispatch rate units in our portfolio. The impact on our highest load factor units under thermal legacy – Genelba and Loma CCGTs – is smoother but still 20% lower during off-peak season. These effects were partially offset mainly by commissioning of Mario Cebreiro and PEPE wind farms with PPAs, as well as Genelba Plus' gas turbines, and to a lesser extent, increased dispatch at our thermal and renewable power plants. Quarter on quarter, PEPE wind farms with business to business PPAs contributed to the slight increase in EBITDA.

Generation was slightly higher year on year mainly due to the operation of wind farms, which ranks senior in the dispatch priority because its variable cost is close to zero, and the addition of gas turbines at Genelba Plus thermal power plant that are part of the closing to CCGT project, as well as higher dispatch at Piedra Buena because we managed to get cheap gas and therefore, competitive Variable Production Cost (aka CVP) to get dispatched. These effects were partially offset by lower load factor at Güemes, Piquirenda and Pilar thermal power plants, caused by a higher CVP from the partial recognition of imported gas, therefore placing them behind in the dispatch priority in the grid, plus a lower water level at our dams, mainly affecting Los Nihuiles hydro unit that also is going through an overhaul. Quarter on quarter, power generation decreased mainly because of lower electricity demand in the grid as weather is milder, partially offset by commissioning of gas turbines at Genelba and PEPE windfarms.

The availability rate in the second quarter of 2019 was 95.4% with an installed capacity of 4.8 GW that includes the operation of recently acquired Ensenada de Barragán thermal power plant, slightly lower than to the 98.2% availability achieved in the same quarter last year and similar rate compared to Q1 2019.

Moving to news in power generation, on June 26 we were jointly awarded with YPF Ensenada Barragán, a 567 MW thermal power plant located close to Buenos Aires city, with a PPA running until April 2022. This power plant also has expansion project to close the cycle, increasing 280 MW more its capacity, with a PPA for 10 years as the project is finished, which is estimated by Q1 2021 with a total investment estimated at 200 million dollars. The acquisition price amounted to 282 million dollars, of which 200 was equally contributed by Pampa and YPF, and the balance through a syndicated loan of 170 million dollars' non-recourse to Pampa and YPF as long as we finish the project by the end of 2021. On top of that, the underlying asset carried existing debt of 229 million dollars with 2 years of grace, so we can focus this power plant's cash flow proceeds first to complete the CCGT's works and later to repay the debt.

Regarding the expansions, we have in the pipeline, we are currently in the midst of the closing to CCGT of 383 MW at Genelba, as you can see in the picture on slide 8. We increased current gas turbine number 3 capacity by 19 MW as from June, and also CAMMESA granted the commercial commissioning of the new gas turbine number 4 for 188 MW, 12 days earlier than the committed date. They are billing as legacy capacity until the closing to CCGT begins operations. Additionally, we have been advancing with the rest of the infrastructure works, which are ahead of the original schedule.

Moving on briefly to the distribution segment which was reviewed by our CFO at Edenor Leandro Montero yesterday in their earnings call, as shown in slide 9 during the second quarter of 2019 the EBITDA increased by 17% compared to the same period of 2018, amounting to 71 million dollars in the quarter, mainly because of the lagged sales of 33 million dollars to Federal Government regarding the consumption at shantytowns and reimbursement of social tariff benefits. Now that Edenor's license was transferred to the City and the Province of Buenos Aires, this sales to shantytowns and social tariff will be borne by local governments.

The accrual of this lagged sale was triggered as a consequence of the settlement for regulatory liabilities agreement signed last May, by which it offset certain legacy regulatory debts Edenor held since 2012 with a lawsuit Edenor filed back in 2013 and regularized unpaid penalties between 2006 and 2015 of around 3 billion pesos by deploying additional capex within the next five years, on top of the Investment Plan timely committed under the tariff review. Though this settlement recorded a one-time profit of 308 million dollars before income tax, we haven't considered this in our EBITDA as it is non-cash effect, but it does set an income tax payment next year that, added to the additional capex and other stuff, the outflow for the next five years is estimated at a total of 7.6 billion pesos.

Year on year, during Q2 2019 we experienced lower demand of electricity by 9% due to mild weather, downturn in the economic activity and price-demand elasticity. Moreover, this quarter's EBITDA was negatively affected by the FX variation higher than the Own Distribution Cost update (aka CPD), which is over weighted in the salary index, that also lags CPI and PPI, in addition to higher operating costs and energy losses.

Energy losses reached 19.2% rate in the second quarter 2019, 60 basis higher than the 18.6% for the same period 2018 and 180 basis above last quarter, identified in residential end-users, especially low income users that do not have access to gas distribution grid, partially offset by lower volume of energy demand. We are targeting at users that steal electricity from us by performing market discipline actions and installing customized pre-charged meters. Therefore, we are increasing our customer base, but this is being offset by plugging offs at SMEs and large users due to the GDP recession. Energy cost increased by 19% in AR$ net of inflation, but decreased 40% in dollars year on year, due to the gradual subsidies removal, but still subsidized compared to the full cost of generation, currently at a half.

As you can see on slide 10, during Q2 2019 in the oil and gas segment we posted an adjusted EBITDA of 53 million dollars, 34% lower than in Q2 2018, mainly because it is still reflecting the downward trend in gas sale prices, lower oil prices year on year and the expiration of Plan Gas second generation in July 2018, partially offset by 6% higher production of gas, driven by intersegment gas sales to power generation for fuel self-procurement and lower expenses that are peso-linked. On the other hand, quarter on quarter EBITDA improved by 11%, mainly explained by higher gas production due to better pricing as seasonal demand started on June.

Our overall production in Q2 2019 increased 6% year on year and 4% quarter on quarter, reaching to 48.5 thousand barrels of oil equivalent per day, of which 90% is composed by natural gas.

On the oil side, production level year on year remained unchanged at 4.8 thousand barrels per day, but quarter on quarter oil production decreased by 10% as **Chirete**, an exploratory block that we recently made oil discovery, it is in the process of facilities accommodation since April 2019. During Q2 2019 the crude oil sales price decreased year on year by 3 dollars, but increased quarter on quarter 6 dollars, reaching 60 dollars per barrel, because the domestic price follows the Brent and this international price rebounded by the end of 2018 and Escalante heavy oil, that is 62% of our oil production, is sweet and given the current clean fuels trend, narrows Medanito prices.

Please turn to slide 11, where we want to explain in deeper detail the situation in gas. Regarding the gas production, the quarter reached an average of 262 million cubic feet per day, 6% increase year on year and

5% quarter on quarter, mainly explained by the production increase at **El Mangrullo**, a block in which gas evacuation capacity was expanded since the end of last year, and is fully operated by us. By June 2019, the gas production level of **El Mangrullo** reached 151 million cubic feet per day, 55% higher than in June last year. These positive effects were partially offset by lower production in other gas-bearing blocks because of lack of visibility on sale prices, which was affected by excess of supply of gas driven by the disruption of shale developments, specifically backed up by the Unconventional Gas Plan Resolution 46, kind of affected by the economic downturn and, especially during winter period, bottlenecks at the main transportation pipelines. These effects negatively impacted on **Rincón del Mangrullo** block with a lower drilling rate and natural decline, and a minor decrease at **Sierra Chata**, **Aguaragüe** and **Parva Negra Este** blocks. In the case of **Sierra Chata**, it is awaiting the completion of the wells drilled during Q2 2019, and **Río Neuquén** maintained same production level year on year.

During second quarter 2019, our accrued weighted average sale price for gas was 3.1 dollars per million BTU, 43% lower year on year and similar to last quarter, mainly due to a 36% decline in end-users' sale price compared to second quarter 2018. The lower sale price to end-users was mainly driven by a reduction on the reference price for gas fired at power plants and the gas tenders on an interruptible basis conducted by CAMMESA, which reflected the demand seasonality and excess of supply in April and May, also impacting negatively the commercialization in industrial segment. In June gas prices rebounded as it marked the beginning of the winter period, with a 37% increase in dollars at power plants reference price by CAMMESA and higher spot prices due to seasonal demand. Moreover, Q2 2018 price accrual of 5.5 dollar per million BTU included Plan Gas second generation compensation, which expired by the end of June 2018, and represented 60 cents per million BTU.

The fuel self-procurement for our power generation helped to recover gas production levels, we are destining almost all our production there. Though it does not improve pricing, it helps to have a certain offtake especially during weak demand periods and to monetize some synergies between power and gas businesses. As you can see on the slide 11, the average gas prices that we recorded to demand have been plunging since August 2018, falling to the lowest point in years and hardly covering the marginal breakeven cost. Winter season picked up prices but as evidence showed in the past, the domestic production was not enough to cover the domestic gas demand, needing to cover the 22% deficit of gas consumed in June with gas imports from LNG and Bolivia with much higher prices than those paid to domestic producers.

Moving on to the news update in the segment, the Government Secretariat of Energy announced deferrals of 22% of the residential gas bills issued between July and October, to be recovered in five monthly installments since December bills, aiming at smoothening residential users' seasonal bills due to higher winter consumption. The financing cost would be borne by the Federal Government as a subsidy. Our E&P exposure to residential segment have been diminished and therefore the impact of this measure is marginal to Pampa.

On the other hand, in June we increased our equity stake at OCP, our subsidiary in Ecuador by 4.49%, amounting to a total of 16%, and recording a provisional profit of 22 million dollars, subject to changes as we are assessing OCP's fair value.

Before I move on from oil and gas, I wanted to give you a quick update of our operations. During the second quarter of 2019, 13 wells were drilled and 5 wells were completed. Our focus is the development of blocks with tight gas reservoirs. During Q2 2019 we drilled 1 shale gas well and 1 tight gas well at **El Mangrullo** and 2 horizontal tight gas wells at **Sierra Chata**.

Since beginning of last year, we began with shale gas exploratory activity at Vaca Muerta reservoir. We built the side tracks for two Vaca Muerta wells at **El Mangrullo** block, each with a horizontal extension of 8.2 thousand feet. These are the first horizontal wells to Vaca Muerta we operate and there are estimated to be completed soon, in which approximately 36 hydraulic fractures are estimated to be performed in each objective. Additionally, since July we are drilling one shale oil well at **Rincón de Aranda**, an exploratory block operated by us with 55% of stake, partnered with Total. As of today, we are finishing the vertical section with a depth of approximately 9.2 thousand feet, and will continue with the drilling of the horizontal branch, targeting Vaca Muerta formation.

In petrochemicals, we posted an adjusted EBITDA of 3 million dollars during the second quarter of 2019, higher year on year and quarter on quarter, mainly because of optimization of fixed costs, lower Peso-linked costs due to deval plus lower costs of gas purchased. These effects were partially offset by the downward trend in international prices in US$, weaker demand, export duties and higher costs of imported virgin naphtha.

In operating terms, total sales volume of our petrochemicals segment remained unchanged year on year in Q2 19, totaling 95 thousand tons, but quarter on quarter increased 15%.

Finally, our holding and others segment presented an adjusted EBITDA of 40 million dollars in the second quarter of 2019, 21% lower than the same period of 2018 but similar to last quarter. This is mainly due to the lower income from fees collected at holding, in addition to lower EBITDA adjusted by our ownership from our affiliates TGS and Transener mainly because the peso depreciation outpaced the cost variation adjustments.

I'm going to only briefly review **TGS** as they just had their earnings call last Thursday; TGS's EBITDA adjusted by our indirect stake of 25.5% contributed to Pampa 33 million dollars in the quarter from an implicit total of 129 million dollars, 10% lower than Q2 18, mainly due to FX variation higher than lagged-granted PPI that covers cost variation for gas transportation business, the drop in references prices denominated in US$ for NGLs, lower natural gas processing volumes and higher export duties, partially offset by lower cost of gas per MBTU.

In relation to the expansion of main gas transportation pipeline, on July 30, 2019, the Government Secretariat of Energy launched the public tender for a new pipeline from Neuquina Basin to the Province of Buenos Aires. First, from Neuquina Basin to the town of Salliqueló with an initial capacity of 530 million cubic feet per day, and from Salliqueló to the City of San Nicolás with a capacity of 700 million cubic feet per day. In order to allow the repayment of investments, the first 17 years of the concession are under Temporary Special Regime, so remuneration will be freely negotiated with large users (not residential), among them CAMMESA that requires take or pay transportation of 353 million cubic feet per day for 15 years. The total license period is for 35 years, extendable for additional 10 years and the opening of the proposals is scheduled for September 12, 2019. TGS is analyzing the bid terms and its participation.

As per **Transener**, its EBITDA adjusted by our indirect shareholding of 26.3% contributed 11 million dollars in the second quarter of 2019, from an implicit total of 42 million dollars, 7% lower than same period in 2018, mainly because the lagged cost variation update was lower than FX variation, partially offset by lower operating costs, mainly due to higher awards for quality service and lower charges of penalties.

Regarding the power outage that occurred in the morning of June 16, 2019, it was due to the concurrence of multiple shortcomings within the grid, including a specific technical problem in the transmission system under Transener's responsibility not related to lack of investment and maintenance, but to improper adjustment of the auto-disconnect generation system following the configuration change of certain lines in the Littoral Corridor. The high-voltage lines recovered immediately and within 8.5 hours 75% of the country's demand was restored.

In mid-June we suspended the 2019 buyback program as quoted prices exceeded the repurchase cap, so total treasury shares under buyback program reached 79.8 million, representing 4.2% of total issued capital stock. However, given the market's volatility and the gap between the value of our assets and the quoted price, plus our strong cash position, yesterday the Board of Pampa approved a new share buyback program for 50 million dollars. We consider the value of our assets will be materialized as soon as market turmoil goes away. In the meantime, we consider repurchasing our own shares one of the best investments and accretive actions towards shareholders that we are undertaking.

In terms of net income attributable to the owners of the Company, Pampa reported a consolidated gain of 394 million dollars in the second quarter of 2019, whereas in the same period of 2018 a loss of 72 million dollars was recorded, mainly explained by the settlement of Edenor's regulatory liabilities, which is non-cash and lower accrual of losses from FX difference as a result of change in the reporting methodology, as I explained at the beginning of this call.

Finally, moving to slide 15, we must highlight the low and well spread leverage of the Company, as well as a solid cash position held compared to other peers in the industry and in Argentina. We have always been very proactive towards the cash and liability management, especially after witnessing volatility, high yields and narrow window in the international financing market. We continued redeeming the short term facilities, highlighting that so far this year Pampa redeemed at maturity and pre-cancelled roughly 225 million dollars.

The consolidated gross debt including affiliates at ownership increased to 2.5 billion dollars, 462 million higher than March 2019, mainly because we issued a 10 year bond last month at 9 3/8, plus we are adding Ensenada's debt at ownership, a power plant we acquired last June, all offset by debt cancellations. Consolidated gross debt is 99% is denominated or linked with US dollar, bearing an average interest rate of 7.2% and 75% is placed at the parent.

Consolidated cash amounted to 863 million dollars, which is higher than the 704 million dollars in March 2019, mainly because of the bond proceeds and the acquisition of Ensenada. Closing Q2 2019, we were holding 70% of our cash in US dollars, but as of last week more than 90% was dollarized. Therefore, net debt slightly increased to 1.7 billion dollars, and net debt to last twelve months EBITDA remained low at 1.7 times. We also show here stand-alone key debt figures for our bondholders.

Even after cancelling roughly 225 million dollars, the principal maturities belonging to Pampa stand-alone that are left in 2019 and combined with 2020 and 2021's, amounts to 316 million dollars, which is by far exceeded by the 682 million dollars' cash position at the parent.

The 682 million includes the 300 million dollars proceeds from 10-year bond issuance we successfully placed at 9 3/8 last July, as well as last week we executed with CAMMESA an agreement to settle all legacy receivables aka inciso c and debts destined to major maintenances. After applying an 18% haircut on the balance and waiving all submitted and potential claims related to it, we collected 38 million dollars. We estimate that this will trigger a profit before taxes for approximately 3.4 billion pesos in the Q3 2019's P&L.

Also, last month Pampa was credited the remaining principal amount owed from Plan Gas second generation and after quarter closing, 15 million dollars have already been collected.

So this concludes our presentation. Now, I will turn the word to the operator, who will open the floor for questions. Thank you.