

Conference Call Transcript

ASR - Q2 2008 Grupo Aeroportuario del Sureste (ASUR) Earnings Conference Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Grupo Aeroportuario del Sureste Second Quarter 2008 Earnings Conference Call. My name is Michelle, and I will be your coordinator for today. At this time, all participants are in listen-only mode. We will be facilitating a question-and-answer session towards the end of this conference.

I would now like to turn the presentation over to your host for today's conference, Mr. Adolfo Castro, Chief Financial Officer. Please proceed.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Thank you, Michelle. Good morning, everybody. Thank you for joining us today for the conference call covering our second quarter results. Allow me to remind you that certain statements made during the course of our discussion today may constitute forward-looking statements,

which are based on management's current expectations and beliefs and are subject to a number of risks and uncertainties that could cause actual results to differ materially, including risks that may be beyond our Company's control. For an explanation of these risks, please refer to ASUR's filings with the Securities and Exchange Commission and the Mexican Stock Exchange.

Moving to the results, we are pleased to report another strong quarter with passenger traffic growth of 9.59%, even more so when we considering the tougher comparison this quarter as the Easter and Holy week holidays fell in the second quarter in 2007 while this year, they fell in the first quarter.

Domestic passenger traffic rose 8.37%, and international traffic was up by 10.53%. Total passenger traffic growth for the quarter at Cancun and Cozumel Airport was up by 10.88% as we continued to benefit from Cancun's strength as a tourist destination. Total passenger traffic rose year-over-year 5.3% in April, 13.2% in May and 10.5% in June.

International passenger traffic accounted 57.1% of total traffic for the quarter, up to 56.6% during the second quarter of 2007 as domestic passenger traffic this quarter faced the impact of increased airline fares as a result of higher fuel costs. Due to the increases in the oil price, some of the domestic carriers have diminished their routes and frequencies in order to improve load factors and increase the yield per flight.

One of the clearest examples of this is Aviacsa, which during the second quarter reported a 12.7% year-over-year decline in operations. Passenger traffic between Mexico, Canada and the United States represented 89.8% of total traffic, almost the same as the second quarter of last year.

Total revenues rose by 11.78% this quarter, mainly driven by the 21.43% increase in non-aeronautical revenues. Commercial revenues were up by 23.19% this quarter compared with the same quarter last year. Revenues from direct operations rose 45.6% this quarter, largely reflecting the opening of Terminal 3 at the Cancun Airport. Commercial revenues per passenger rose 12.66% to MXN49.29. Excluding the impact of the discontinuation of the direct commercial operations, revenue per passenger rose 9.09% year-over-year to MXN40.67.

Operating costs and expenses rose 4.81% year-over-year despite the higher costs related to the operation of Terminal 3 in Cancun as well as increase in administrative expenses resulting from the corporate reorganization implemented late March. Operating costs were low this quarter as we reversed a MXN34 million deferred provision following the corporate reorganization. Excluding this reversal, operation costs would have risen 13.2%, in line with our expectations, considering the operation of Terminal 3.

Operating profit for the quarter was up 20.73% to MXN382.1 million. As a result of this, EBITDA margin rose to 65.78% from 61.40% year-over-year.

In terms of taxes, this quarter we saw a decline in deferred income taxes, which mainly resulted from the elimination as of December 31, 2007, of the deferred income tax provision for the airport subsidiaries that are expected to pay IETU tax. During the quarter, we paid MXN61.1 million in IETU compared with the MXN35.8 million in nominal terms paid an asset tax for the second quarter 2007. If we exclude Cancun, the remaining Company's paid MXN16 million in IETU compared with the MXN23.8 million paid last year.

In accordance with Mexican accounting standards, Cancun Airport is recognizing deferred income tax and also paying IETU tax that cannot be credited against future income tax. Because of this, the effective tax rate presented for the quarter was 35.8%.

Finally, during the quarter, we made investments of MXN101.9 million, mainly on the second runway of Cancun Airport.

Now, let me open the floor for questions. Please, Michelle, go ahead.

QUESTION AND ANSWER

Operator

(OPERATOR INSTRUCTIONS).

And your first question comes from the line of Esteban Polidura from Merrill Lynch. Please proceed.

Esteban Polidura - Merrill Lynch - Analyst

Thank you, and good morning, Adolfo. Congratulations on your report, three questions if I may. First, are you expecting more reversals of cost provisions and employee transfer costs during the next quarters? Second, what are the kind of things you are doing to keep some of the expenses under control? And third, what are the latest news you've been hearing about Aero California? Thank you.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Okay. Thank you, for your kind words, Esteban. First, we do not expect any other cost reversals. In terms of expenses, we're doing many things in -- mainly in Cancun Airport in order to maintain our costs in the same level. And the third one, in terms of Aero California, I'm not hearing anything new. Probably, you saw what it was published yesterday in the Mexican papers that they were suspended because they are not paying to the government. In the case of ASUR, we do not have any flight with them.

Esteban Polidura - Merrill Lynch - Analyst

Perfect, thank you.

Operator

Your next question comes from the line of Nick Sebrell of Morgan Stanley. Please proceed.

Nick Sebrell - Morgan Stanley - Analyst

Good morning, Adolfo. Congratulations on no hurricanes, so quick questions. First, if you could just talk a little bit more about the second runway progress, other major projects that you guys have coming along in terms of CapEx and what they might cost? And then the second, regarding the tax rate, I mean, obviously tax is affected by IETU, if you can talk a little bit about what the future expected tax rate could be going forward, especially long-term? And I'll leave it there.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Okay. Good morning, Nick. In the case of the second runway, we are continuing working there. We expect to open this during the fourth quarter 2009. We do not have any other projects of the size like the second runway currently. You know that we are at our last year of our master development plan. You know that we are currently negotiating our next mass development plan for the years 2009/2013.

In the case of taxes, what we can expect is that Cancun will be paying IETU tax for the rest of the year and because of this, you will see an effective tax rate above the 28% because we have to consider apart from the IETU also the deferred income tax.

Nick Sebrell - Morgan Stanley - Analyst

Okay.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

That's what it consists.

Nick Sebrell - Morgan Stanley - Analyst

And then longer-term, maybe trending toward 28%?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Well, in the future, I think Cancun should be paying income tax [REDACTED], and then they will stop paying IETU tax. And then, you will not -- or, we will not have the duplication in the P&L.

Nick Sebrell - Morgan Stanley - Analyst

Got it. And income tax for Cancun would come in a year, or five years?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Of course, I cannot give you an answer on that because we will have to be predicting all the numbers in the Company, and it's something that we cannot do at this moment.

Nick Sebrell - Morgan Stanley - Analyst

Of course.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

I would say that in medium term, future.

Nick Sebrell - Morgan Stanley - Analyst

All right, thank you.

Operator

Your next question comes from the line of Gonzalo Fernandez of Santander. Please proceed.

Gonzalo Fernandez - Santander Central Hispano - Analyst

Hi, good morning Adolfo, and also congratulations on the results. Two questions, so eliminating the recovery of costs, you expect to cover more impact from the additional costs from Terminal 3 in Cancun, because we really haven't seen that significant hike in costs because of that? And the second question is that so far, have you seen further reductions in frequencies on routes by airlines? Or, do you think that the worst is behind?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Good morning, Gonzalo. Thank you for your words. In the case of the cost of Cancun, believe me, we are working really hard in order to try to control these controls, even up to the extreme, you can go today to the Terminal 2 in Cancun Airport and you will see that we are not using all the lamps or the complete lighting of the terminal because of the increase in the energy cost. This is just one thing of the things that we are doing, but just to give you the real effect that this can be.

In terms of reductions in frequencies, yes, we are continuing to see these reductions; the airlines are...the Mexican airlines are suffering. Of course, you can see that everywhere in the world, they are suffering because of the higher oil price, but some of them have taken measures. You can see the report of -- that it was published last -- yesterday of Southwestern. They made very nice EBITDA margin, and they increased profits during this quarter. No, I don't believe that we have seen the worst. I believe that the second half of this year is not going to be as good as the first one.

Gonzalo Fernandez - Santander Central Hispano - Analyst

Okay, thanks, Adolfo.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

You're welcome.

Operator

Your next question comes from the line of Steve Trent of Citigroup. Please proceed.

Steve Trent - Citigroup - Analyst

Good morning, Adolfo, and thank you as always for your time today. One or two questions for me, first of all, looks like Hurricane Dolly -- well, first of all, it was not a hurricane when it passed over northern Yucatan. It was just a tropical storm. Any color on that, it doesn't seem to be much at all, no evacuations, no closures, maybe just some flight delays?

Two other questions if I may. In terms of European traffic flow, are you seeing anything in terms of advanced bookings, for example, that would recommend a shift in that traffic pattern? And then finally, I wanted to see if you're able to offer any color as to what you are thinking on passenger growth in the second half. Thank you.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Hi, good morning, Steve. In terms of the hurricane, well, it -- finally, it was Hurricane Dolly. But you are right, it was a tropical storm. It was winds of 80 kilometers per hour when they passed in front of the Yucatan Peninsula. The problem of this tropical storm was that it had a lot of water. As a matter of fact, we closed Cancun Airport for some hours and some of the flights were deviated to Merida's airport and then they went back to Cancun. So in the case of this one, we didn't suffer at all.

In the case of the European traffic pattern, we are not seeing any change yet. I was expecting to have more Europeans during the summer and they're not coming yet. Probably all of them are in New York. In terms of the traffic growth for the second half of this year, the only thing that I can say is it's a feeling that we are seeing a decreasing growth trend. So, as you can see in our monthly passenger traffic figures, the beginning of the year was very good and it's getting bad during the year.

Nevertheless, we expect to have a very nice year, of course not comparable with the extremely good that we had last year. Remember that last year, the passenger traffic growth of the Company was more than 17%. And this, in my opinion, is not sustainable. I don't believe in double-digit passenger traffic growth in the medium to long term. So, we are coming back to normal and that's what I can say.

Steve Trent - Citigroup - Analyst

But certainly in terms of the second half, you're also talking more moderate growth on top of what had been a very good comp, it's not like you're expecting growth to go into the ground?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Well, of course, we don't know what is going to happen with the US economy. I think that the second half of this year is going to be tougher in terms of comparison numbers.

Steve Trent - Citigroup - Analyst

Fair enough. Thank you very much, Adolfo.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

You're welcome.

Operator

Your next question comes from the line of Vanessa Quiroga of Credit Suisse. Please proceed.

Vanessa Quiroga - Credit Suisse First Boston - Analyst

Thank you. Hi, Adolfo. My question is regarding provisions for doubtful accounts, do you expect to be doing any of these, at least in a significant manner, in the upcoming quarters? And then, I also have a question regarding the project that you had for helping build a fast train to connect the Mayan Riviera hotels with Cancun Airport, if there was any further effort in that sense. And if you could comment on any driver for commercial revenues in the second half of the year, if you expect to have any specific new living contract or anything that could drive commercial revenues in the second half. Thanks.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Okay. Hi, good morning, Vanessa. Provision for bad accounts, no, I don't expect to create any provision during the year. Normally, what we do is to be very close to the customer and to put some pressure when they don't pay on time. And today, we have some Mexican airlines that are not paying on time and we are making the necessary efforts in order to collect that money.

You saw what has happened yesterday with Aero California and also with Continental Express. I think that the Mexican government is starting to put some pressure on them also, because they will have to pay no matter what. So, I hope that we will not face that problem in the future.

In the case of the light train, yes, we are continuing making efforts on this project. This is a huge project; it's not something that you can do from day to night. The only thing that I can say to you is that what we are seeing is higher costs resulting from the strong euro against the US dollar. Some of this equipment is coming from Europe, so we're continuing analyzing this project up to today. I have to say that the project needs some external resources if we want to do this.

In terms of driver to commercial revenues, no, we do not see a major driver for commercial revenues. It's important to say that during the next quarter, we will not have the easy comps because Terminal 3 was opened May last year. Nevertheless, the best thing that we can do is to be close again to the customer and to know exactly what he's looking for, and then to provide the best service to him. And that should be the best driver for commercial revenues.

Vanessa Quiroga - Credit Suisse First Boston - Analyst

Thank you very much, Adolfo.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

You're welcome.

Operator

And your next question comes from the line of Nick Sebrell of Morgan Stanley. Please proceed.

Nick Sebrell - Morgan Stanley - Analyst

Hi Adolfo, thanks for taking the follow-up, two follow-ups. First, if you could talk about detail among the airports, in other words, we've seen Oaxaca recover it seems, even so much as to see some articles in the New York Times about Oaxaca as a favorite destination. Talk about which airports are strongest right now, which ones you expect to see weaker traffic. So, that's question one.

And then, the other one is just progress on other airports. I don't think the question has been asked yet on the call regarding the second airport in the Mayan Riviera. As well as potential opportunities in other parts of the country, do you think anything's going to happen soon? And how might the new Mexico Airport be managed? I mean, Texcoco, is that -- do you think, something that might be auctioned? Or do you think it's going to be kept under control by the government?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Okay. Well, details on the other airports, yes, we have nine airports and not just one. In the case of Oaxaca, the political problem and the dispute between the government and the teachers is still there, has not ended and probably will not end ever. In terms of that, they are not being so active during this quarter as they were before. We can say that there is some kind of recuperation. If you see the historical numbers of Oaxaca, we are not reached the peak of what we have before the public disputes of the teachers.

Some other comments on the airports, it's important that you can make an analysis on what -- of how many passengers we had at the end of the year 2005 compared with how many passengers we had at the end of the year 2007. Because then you will be able to see, on an airport basis, what was the real impact of local carriers, of course with the exception of Cancun because of the reasons that you know.

If you do this, you will find, more or less, a million passengers, a million passengers distributed by Veracruz, Villahermosa and Merida mainly. You can see that in the case of Veracruz during this year, basically we see no growth or very flattish. So, we think that Veracruz has reached a limit in that sense. And also, I have to say that in that specific case, we have reached a limit in terms of capacity for the terminal building. In our new master development plan, we should be considering to put a new terminal building there.

In the case of Villahermosa, it's growing even with the problems that we are seeing with the domestic airlines. Most of the traffic in Villahermosa is domestic, it's not international. Nevertheless, we're seeing some growth. Merida is suffering, I think, because of the increase in the rates.

In the case of the second airport of the Riviera Maya, the latest information that we have is that the Minister of Communications and Transport is willing to make the bidding process for this airport during the second half of this year. Mexico City, we need a new Mexico City airport, the one that we have is not enough. Some day in the future, the Mexican authorities will have to do something about it.

I really don't know if they're going to make this private or not. In my opinion, that would be the best alternative or the best option. It's going to be very hard for them to try to pay between \$3.5 billion to \$5 billion for this project. And in terms of location, I believe that it should be located in Texcoco.

Nick Sebrell - Morgan Stanley - Analyst

Okay. So, you said the Minister is talking about a second half '08 auction for some of the airports?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

That was the latest statement that he made to the media.

Nick Sebrell - Morgan Stanley - Analyst

Okay. And was that something recent? I guess I missed that.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Sorry?

Nick Sebrell - Morgan Stanley - Analyst

Was that recent? I mean, he said that in the last month? Or was that a while ago?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

That was three months ago.

Nick Sebrell - Morgan Stanley - Analyst

Okay. All right, Adolfo, thank you very much.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

You're welcome.

Operator

(OPERATOR INSTRUCTIONS).

And your next question comes from the line of Vivian Salomon of HSBC. Please proceed.

Vivian Salomon - HSBC - Analyst

Hi, Adolfo. My question has been answered, but it was just something else regarding the Riviera Maya Airport. Is there any news, I mean, there hasn't been nothing yet, but if you're going to be allowed to participate in the bidding, if the bidding takes place during the second half?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Yes, good morning, Vivian, and congratulations on your new task. Of course, we have been vying for this for many, many years. The only one that has that answer is the Antitrust Commission in Mexico. Not even the Minister of Communications and Transport will be able to say if we are or if we are not going to participate, or if we are going to be allowed to participate or not. The only one is the Antitrust Commission.

And the only thing that I can say is, if you go to the report that his CEO presented October last year, apparently, he's indicating that we should not participating. But that doesn't mean that we will not be allowed to participate. We will have to wait and see if they are willing to allow us or not.

Vivian Salomon - HSBC - Analyst

Perfect. Thank you very much, Adolfo.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

You're welcome.

Operator

And your next question comes from the line of Jose Ramirez of UBS. Please proceed.

Jose Ramirez - UBS - Analyst

Hi, Adolfo, just a quick question. Could you give us an idea of the size of the receivables that are behind schedule from the airlines? It's just because I heard yesterday the Minister of Communications gave a significant figure on this subject.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Well, I don't know what kind of details you want, but what I can say to you is that we have MXN361 million in accounts receivables. In terms of what is due, I can tell you that at least three domestic carriers are not paying on time.

I don't want to disclose who they are; I don't think it's appropriate for the moment. And it's not something that I'm really, really concerned about because I don't see them going to bankruptcy in the short term. So, they will pay us, that's what I believe.

Jose Ramirez - UBS - Analyst

Okay, thank you.

Operator

Your next question comes from the line of Mauricio Santos of GBM. Please proceed.

Mauricio Santos - GBM - Analyst

Hi, Adolfo, good morning, I had a couple of questions. The first one was regarding your net financial activities cash flow. While the total was MXN950 million, I was wondering MXN600 million were on the back of the dividend payment and what was the purpose of the other MXN350 million? And my second question would be a follow up on the Mayan Riviera. Is it possible that you adjust your maximum tariffs once the new PMD has started? Because he is waiting maybe the next -- the Riviera Mayan auction won't get the light until the second half of the year. Thank you.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Well, let me go to your first question that was not so clear, but what I believe is that the answer, taxes that we had to pay for the tax on dividends.

Mauricio Santos - GBM - Analyst

Okay, perfect.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

In the case of the Riviera Maya, your question was about maximum rate. Well, in accordance with the current regulation, if we are let's say between brackets affected by the Riviera Maya in the sense that we'd be losing some of our traffic, of course that will have an impact in the Mexican tax calculation.

Mauricio Santos - GBM - Analyst

Yes, the thing is that well, I suppose that you need to know, you need some visibility on the Mayan Riviera issue in order to determine those tariffs and my question was regarding the SCT can make. Let's say that you negotiate a new MDP and a year from now the new Mayan Riviera Airport is auctioned and you don't get it, can you adjust the tariffs like that?

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Well, we cannot adjust our tariffs unilaterally. It will have to go to the SCT and to tell them what the problem is because what they have done and then to try to renegotiate or to increase our rates because of this. Nevertheless, if we believe that they are going to make the auction after we close the deal on the MDP, that airport will have an impact on us probably at the very end of the next five years at the [REDACTED]. Even with that, the impact should not be significant.

Mauricio Santos - GBM - Analyst

Okay, thank you very much. And congratulations on the report, it was really great considering current conditions.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Okay, thank you, Mauricio

Operator

And your next question comes from the line of Allan Solis of Credit Suisse. Please proceed.

Allan Solis - Credit Suisse - Analyst

Yes, good morning, Adolfo, just to follow up on taxes. What are you expecting in terms of cash tax rate for '08? Thank you.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Well, that's a very tough question and I don't have the exact answer in the top of my head. But if you go back on what we have released and on what I have said during the conference, the airports that are -- actually with the exception of Cancun, are paying less, as we expected, are paying less compared with the asset tax. The problem is the Cancun IETU tax and we paid during this quarter MXN61 million.

It is important to understand, for the calculation of this tax, that this tax is related to the operational margin. So, if we try to calculate how much are we going to pay in the next two quarters, what I can say to you is that Cancun Airport will have to pay less on a quarterly basis on what we have paid during the first quarters.

Allan Solis - Credit Suisse - Analyst

Okay, thanks, Adolfo.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

You're welcome.

Operator

(OPERATOR INSTRUCTIONS).

And it appears you have no further questions, I'd now like to turn it back to Mr. Castro for closing remarks.

Adolfo Castro - Grupo Aeroportuario del Sureste - CFO

Okay, thank you again to all of you for taking the time to hear what we have to say. The hurricane season is not over, that overs at the end of October, so knock on wood that the first one it was the last. So, thank you again and we will hear you next conference call. Thank you, bye.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This does conclude the presentation, you may now disconnect. Have a great day.