

## The hard way

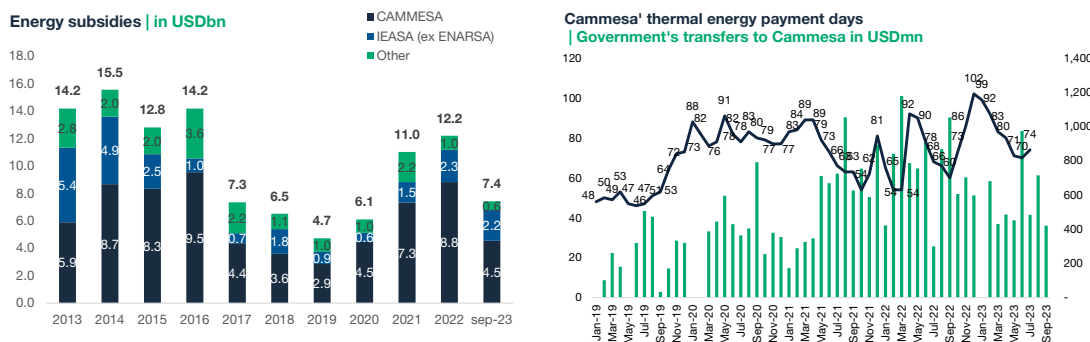
With Milei as the new President, we expect a faster correction of energy prices than if Massa had been elected. As Juan Manuel Pazos' said in *Do you have a clue what happened now?* report, the biggest issue will be the transition. Argentina's energy prices are lagging behind inflation. The more time the government delays its correction, the higher will be the rates of increases, and thus, the higher the negative impact on households' disposable income. Among energy prices, we believe YPF's gasoline and diesel prices are the easiest to adjust. According to a local media, Horacio Marin would be appointed as the new President and CEO of YPF. Considering that Mr. Marin was Exploration and Production President in Tecpetrol, we expect him to improve YPF's downstream profitability through local prices corrections, in order to boost cash generation for ramping-up the Upstream business. For this reason, we expect the O&G sector to be the outperformer.

The increase in natural gas and electricity tariffs paid by households are not an easy task. The Macri administration wrestled to implement energy price corrections. In April 2016, water and natural gas prices increased on avg. 300%. In September 2016, the Supreme Court of Argentina put on hold a further rise in natural gas for residential users until the public hearings. In 2017, new reference prices in power and natural gas in all the chain, generation, transportation, and distribution, were agreed with the Integral Tariff Review (RTI). In this way, there was a virtuous circle, in which Cammesa's liquidity position improved, reducing transfer needs from the government. Companies were paid in a timely manner, which helped them to carried out their expansionary projects.

Eduardo Chirillo will be the new Energy Secretariat. He is of the opinion that power should be valued using marginal costs, like in the 90s or currently in Chile. Changing the current framework to marginal costs would drive a material improvement in companies that sell electricity in the spot market or Energia Base. However, the implementation of the marginal cost framework faces various problems. The first one is that companies would have to purchase natural gas or fuel oils to produce energy. Currently, Cammesa pays for it. Most natural gas production is under Plan Gas contract. The question is what would happen with those contracts. Second, Energia Base has helped the government to maintain energy costs down. Consequently, the correction in household bills would be more aggressive than with the current framework.

Next year, we expect the new government to push for the new RTI that should have taken place in 2022. With 2023 annual inflation heading to 175%, we believe Milei will face a more vulnerable macro scenario than Macri did. Considering the low acceptance of Macri's tariff increases by the general public, it is difficult to say if Milei will have enough support to overcome the social unrest. We cannot rule out the opposition wreaking havoc, which could lead to the slowing of the pace of price corrections or sabotage regulatory changes. For this reason, we are moderately optimistic about the power generation sector.

**Figure 1: The rate of tariff adjustment will denote Milei's power.**



Source: ASAP, MSU Energy's presentation

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