

Alaska Air Group

2024 outlook in-line excluding 737 MAX 9 grounding; maintain Buy

Reiterate Rating: BUY | PO: 50.00 USD | Price: 37.42 USD

2024 outlook in-line despite 737 MAX 9 grounding

ALK reported 4Q23 EPS of \$0.30, beating our/Visible Alpha consensus of \$0.18/\$0.20. For 2024, ALK's EPS outlook of \$3.00-\$5.00 was largely in line with our forecast after factoring in a nearly \$1 impact (\$150M pre-tax) from the 737 MAX 9 grounding (we had forecasted \$5.02 and Visible Alpha consensus was \$4.95). Similar to some other airlines this earnings season, ALK did not provide 2024 guidance building blocks, only tightening 2024 capacity growth to the low end of the +3-5% range. We maintain our Buy rating.

Gradual return to service through next week

ALK will gradually return its 737 MAX 9 fleet to service through the first week of February. After 3,000 grounding-related cancellations in January, ALK now expects 1Q24 capacity growth to be down mid-single digits year-over-year, while targeting +3% growth in 2024 vs our prior forecast of +5%. Management noted the likelihood of delays for ALK's 2024 MAX deliveries which may risk the growth target, while we think capacity constraints could be somewhat offset by higher yields.

Book-away presents a revenue risk; corporate could offset

ALK's \$150M pre-tax impact from the grounding pertains to lost revenue from flight cancellations with limited cost offsets. In our view, the near-term risk could stem from customer book away as the MAX 9 returns to service, a figure we quantified in our [note following the grounding](#) at \$40-50M. That said, ALK noted momentum in corporate travel into 2024, with business revenues now within 5% of 2019 levels and 26% growth in tech-company related travel. We think a continued strengthening of corporate demand into ALK's capacity constraints could help to offset any potential book away.

Lower estimates on the grounding; \$50 PO unchanged

We are lowering our 2024E EPS to \$4.21 from \$5.02 to reflect the impact of the grounding. However, ALK expects to eventually be compensated for the lost profits from Boeing, but a figure and timing is uncertain right now. As such, we add back the lost profits in our valuation analysis, which results in an unchanged \$50 Price Objective that remains based on 5.5x our 2024E EBITDAR.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	4.34	4.53	4.21	5.36	5.30
GAAP EPS	1.36	5.48	12.63	10.72	10.59
EPS Change (YoY)	NM	4.4%	-7.1%	27.3%	-1.1%
Consensus EPS (Bloomberg)			5.00	6.15	7.17
DPS	0	0	0	0	0
Valuation (Dec)					
P/E	8.6x	8.3x	8.9x	7.0x	7.1x
GAAP P/E	27.5x	6.8x	3.0x	3.5x	3.5x
EV / EBITDA*	6.8x	6.1x	6.1x	5.3x	5.2x
Free Cash Flow Yield*	-5.4%	-16.3%	-5.9%	-2.9%	-2.9%

* For full definitions of [IQmethod™](#) measures, see page 4.

26 January 2024

Equity

Key Changes

(US\$)	Previous	Current
2024E Rev (m)	10,732.1	10,465.9
2025E Rev (m)	11,354.7	11,273.7
2026E Rev (m)	NA	11,928.6
2024E EPS	5.02	4.21
2025E EPS	5.34	5.36
2026E EPS	NA	5.30

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Stock Data

Price	37.42 USD
Price Objective	50.00 USD
Date Established	9-Jan-2024
Investment Opinion	B-1-9
52-Week Range	30.75 USD - 57.18 USD
Mrkt Val (mn) / Shares Out (mn)	4,718 USD / 126.1
Free Float	99.6%
Average Daily Value (mn)	157.37 USD
BofA Ticker / Exchange	ALK / NYS
Bloomberg / Reuters	ALK US / ALK.N
ROE (2024E)	12.3%
Net Dbt to Eqty (Dec-2023A)	86.0%
ESGMeter™	Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to ["BofA ESGMeter Methodology"](#).

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Timestamp: 26 January 2024 05:00AM EST

iQprofileSM Alaska Air Group

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	0.9%	3.3%	5.6%	6.6%	6.2%
Return on Equity	14.6%	14.7%	12.3%	13.9%	12.1%
Operating Margin	0.7%	3.8%	7.2%	8.3%	7.6%
Free Cash Flow	(253)	(769)	(280)	(139)	(138)

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	2.6x	1.8x	2.3x	2.0x	2.1x
Asset Replacement Ratio	4.0x	4.0x	3.1x	2.8x	2.6x
Tax Rate	26.6%	27.2%	25.0%	25.0%	25.0%
Net Debt-to-Equity Ratio	92.7%	86.0%	75.1%	60.7%	55.4%
Interest Cover	0.7x	4.2x	7.8x	10.7x	12.1x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	9,646	10,426	10,466	11,274	11,929
% Change	56.2%	8.1%	0.4%	7.7%	5.8%
Gross Profit	NA	NA	NA	NA	NA
% Change	NA	NA	NA	NA	NA
EBITDA	1,556	1,737	1,733	1,998	2,042
% Change	210.6%	11.6%	-0.2%	15.3%	2.2%
Net Interest & Other Income	9	(71)	(41)	(44)	(31)
Net Income (Adjusted)	556	584	534	670	654
% Change	NM	4.9%	-8.6%	25.6%	-2.5%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	116	470	1,067	670	654
Depreciation & Amortization	415	451	491	530	570
Change in Working Capital	555	(336)	152	105	84
Deferred Taxation Charge	(5)	22	44	56	54
Other Adjustments, Net	337	443	(534)	0	0
Capital Expenditure	(1,671)	(1,819)	(1,500)	(1,500)	(1,500)
Free Cash Flow	-253	-769	-280	-139	-138
% Change	NM	-204.0%	63.6%	50.4%	0.7%
Share / Issue Repurchase	0	(95)	(100)	(100)	(100)
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	(384)	194	(56)	(296)	(296)

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	338	281	345	361	27
Trade Receivables	296	383	383	383	383
Other Current Assets	2,406	2,041	1,541	991	791
Property, Plant & Equipment	8,823	9,583	10,592	11,562	12,493
Other Non-Current Assets	2,418	2,325	2,325	2,325	2,325
Total Assets	14,281	14,613	15,187	15,622	16,018
Short-Term Debt	523	511	511	511	511
Other Current Liabilities	3,989	3,948	4,100	4,205	4,289
Long-Term Debt	3,352	3,307	3,251	2,955	2,659
Other Non-Current Liabilities	2,601	2,734	2,778	2,834	2,889
Total Liabilities	10,465	10,500	10,640	10,505	10,348
Total Equity	3,816	4,113	4,547	5,117	5,670
Total Equity & Liabilities	14,281	14,613	15,187	15,622	16,018

* For full definitions of iQmethodSM measures, see page 4.

Company Sector

Airlines

Company Description

Alaska Air Group is the 5th largest airline in the U.S. based on revenue passenger miles and flies to more than 120 destinations throughout North America. Alaska focuses on primarily longer stage-length routes and contracts with Horizon and SkyWest Airlines, Inc. for shorter-haul capacity. Further, ALK focuses on point-to-point traffic on the West Coast with its mainline capacity as follows: 24% on the West Coast, 40% transcon/midcon, 18% Hawaii/Costa Rica/Belize, 12% Alaska, and 6% Mexico.

Investment Rationale

ALK is an exceptionally well-run airline, in our view, with a strong cost focus and solid balance sheet. ALK's net debt is significantly lower than 2019 levels and it did so without issuing equity during the pandemic. ALK has accelerated its fleet consolidation and expects to remove all of the less efficient Airbus aircraft by 2023. By returning to its low cost roots with solid cost controls, we believe ALK is well positioned to capitalize on strong travel demand.

Stock Data

Average Daily Volume 4,205,406

Quarterly Earnings Estimates

	2023	2024
Q1	-0.61A	-0.86E
Q2	3.00A	1.86E
Q3	1.83A	2.08E
Q4	0.30A	1.15E

Price objective basis & risk

Alaska Air Group (ALK)

Our \$50 price objective for ALK is based on approximately 5.5x our 2024E EBITDAR. Our target multiple is approximately at the middle of its historical 3-7x middle range. We believe this is reasonable given its balance sheet strength and cost focus.

Downside risks to our price objective are higher fuel prices, general economic weakness, unfavorable government regulation/taxes, safety concerns, and terrorism/geopolitical events.

Analyst Certification

I, Andrew G. Didora, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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US - Airlines and Cruise Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Air Canada	YAC	AC CN	Andrew G. Didora, CFA
	Air Canada	ACDVF	ACDVF US	Andrew G. Didora, CFA
	Alaska Air Group	ALK	ALK US	Andrew G. Didora, CFA
	Carnival Corporation	CCL	CCL US	Andrew G. Didora, CFA
	Carnival Plc	CUKPF	CCL LN	Andrew G. Didora, CFA
	Delta Air Lines	DAL	DAL US	Andrew G. Didora, CFA
	United Airlines Holdings	UAL	UAL US	Andrew G. Didora, CFA
NEUTRAL				
	Frontier Airlines	ULCC	ULCC US	Andrew G. Didora, CFA
	Norwegian Cruise Line Holdings	NCLH	NCLH US	Andrew G. Didora, CFA
	Royal Caribbean Group	RCL	RCL US	Andrew G. Didora, CFA
	Southwest	LUV	LUV US	Andrew G. Didora, CFA
UNDERPERFORM				
	Allegiant Travel Company	ALGT	ALGT US	Andrew G. Didora, CFA
	American Airlines Group	AAL	AAL US	Andrew G. Didora, CFA
	JetBlue Airways	JBLU	JBLU US	Andrew G. Didora, CFA
	Spirit Airlines	SAVE	SAVE US	Andrew G. Didora, CFA
RSTR				
	Hawaiian Holdings	HA	HA US	Andrew G. Didora, CFA



iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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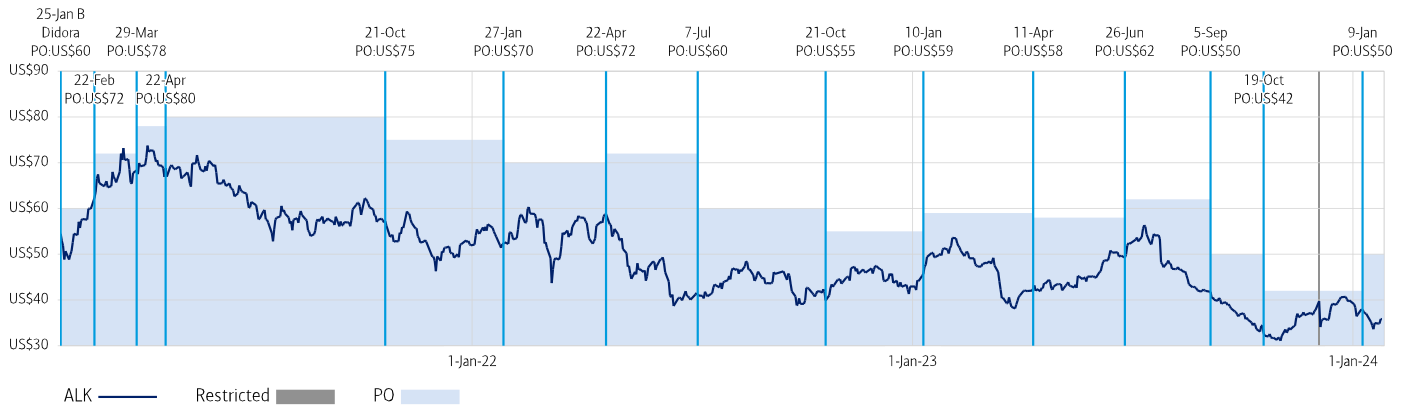
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Important Disclosures

Alaska Air Group (ALK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Transport/Infrastructure Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	67	50.38%	Buy	44	65.67%
Hold	31	23.31%	Hold	13	41.94%
Sell	35	26.32%	Sell	17	48.57%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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