

American Airlines Group

2024 Investor Day: focused on long-term margin and FCF generation

Maintain Rating: UNDERPERFORM | PO: 12.00 USD | Price: 14.81 USD

Investor day focused on long-term margin, FCF targets

AAL hosted an investor day in New York this afternoon. The presentation avoided any near-term updates, instead focusing on long-term margins, free cash flow, and balance sheet goals. AAL's EBITDAR margin targets of 14-16% and 15-18% in 2025 and 2026, respectively, were ahead of both our and Street expectations, with targets predicated on a positive unit revenue/unit cost spread in 2025-2026. This dynamic only occurred at AAL in 2018/2019 last cycle, and our current estimates for AAL and peers are more conservative.

EBITDAR margin targets ahead of Street expectations

As mentioned, AAL's 2025/2026 margin guidance exceeded both our and Street estimates, each around 13%. Business re-engineering initiatives are the key driver of cost savings (about \$1B worth) and could result in unit cost ex-fuel growth sub-inflation assuming conservative capacity growth of 3-4%. Premium products and loyalty are an integral component of margin expansion as well, with AAL assuming the partial closing of the renumeration gap versus peers on its co-brand credit card, particularly in 2026.

Smooth capex plans with FCF generation prioritized

In addition to the investor day, AAL announced orders for 260 new narrowbody aircraft from Boeing, Airbus and Embraer, with deliveries beginning in 2027. With an average age of 13 years old, AAL has no replacement capex needs this decade, signaling steady aircraft capex. Non-aircraft capex should remain largely consistent at \$800-1,100M, however, there may be modest variability year to year as AAL retrofits some aging sub-fleets beginning in 2025. A mild capex profile should strengthen AAL's free cash flow generation, supporting the \$15B debt reduction goal from peak levels in 2Q21 in 2025.

Achieving targets could yield over \$5 in EPS

AAL's long-term targets assume a moderate rate of capacity growth around 3.5% in 2025 and 2026, which we think implies cost growth in the 1-2% range (in-line with AAL's sub-inflation guide). If we assume current fuel, margin targets imply unit revenue growth of 2.0% in 2025/2026, and 2026 EPS over \$5.00. Consensus is currently \$4.10 and likely assumes more conservative revenue assumptions. Our forecasts also reflect this, and we maintain our Underperform rating on AAL's premium valuation.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	0.53	2.65	2.65	2.66	2.10
GAAP EPS	0.25	1.21	2.65	2.66	2.10
EPS Change (YoY)	NM	400.0%	0%	0.4%	-21.1%
Consensus EPS (Bloomberg)			2.52	3.24	4.10
DPS	0	0	0	0	0
Valuation (Dec)					
P/E	27.9x	5.6x	5.6x	5.6x	7.1x
GAAP P/E	59.2x	12.2x	5.6x	5.6x	7.1x
EV / EBITDA*	13.9x	9.1x	9.2x	9.4x	9.9x
Free Cash Flow Yield*	-3.4%	11.0%	17.7%	6.7%	4.2%

* For full definitions of *IQmethod*SM measures, see page 4.

04 March 2024

Equity

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Stock Data

Price	14.81 USD
Price Objective	12.00 USD
Date Established	26-Jan-2024
Investment Opinion	C-3-9
52-Week Range	10.86 USD - 19.08 USD
Mkt Val (mn) / Shares Out (mn)	11,019 USD / 744.0
Free Float	98.5%
Average Daily Value (mn)	492.51 USD
BofA Ticker / Exchange	AAL / NAS
Bloomberg / Reuters	AAL US / AALQ
ROE (2024E)	NA
Net Dbt to Eqty (Dec-2023A)	NA
ESGMeter™	High

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Timestamp: 04 March 2024 10:00PM EST

iQprofileSM American Airlines Group

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	2.5%	5.7%	7.5%	6.9%	5.8%
Return on Equity	NM	NM	NM	NM	NM
Operating Margin	3.3%	5.7%	7.1%	6.2%	5.0%
Free Cash Flow	(373)	1,207	1,953	739	464

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	5.7x	2.0x	2.7x	2.7x	3.2x
Asset Replacement Ratio	1.1x	1.2x	1.4x	1.8x	1.6x
Tax Rate	31.7%	26.8%	25.0%	25.0%	25.0%
Net Debt-to-Equity Ratio	NM	NM	NM	NM	NM
Interest Cover	0.8x	1.4x	2.1x	2.2x	2.1x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	48,972	52,788	54,710	56,851	58,854
% Change	63.9%	7.8%	3.6%	3.9%	3.5%
Gross Profit	3,586	4,970	5,882	5,731	5,417
% Change	273.9%	38.6%	18.3%	-2.6%	-5.5%
EBITDA	4,104	6,267	6,198	6,047	5,733
% Change	NM	52.7%	-1.1%	-2.4%	-5.2%
Net Interest & Other Income	(1,421)	(1,912)	(1,422)	(1,062)	(1,013)
Net Income (Adjusted)	381	1,907	1,905	1,912	1,509
% Change	NM	401.0%	-0.1%	0.4%	-21.1%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	127	822	1,857	1,860	1,461
Depreciation & Amortization	2,300	2,254	2,299	2,504	2,771
Change in Working Capital	1,149	904	337	155	145
Deferred Taxation Charge	59	300	619	620	487
Other Adjustments, Net	(1,462)	(477)	0	0	0
Capital Expenditure	(2,546)	(2,596)	(3,160)	(4,400)	(4,400)
Free Cash Flow	-373	1,207	1,953	739	464
% Change	NM	NM	61.8%	-62.2%	-37.2%
Share / Issue Repurchase	(21)	0	0	0	0
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	(2,683)	(2,896)	(3,535)	(2,900)	(3,519)

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	586	681	1,598	2,437	883
Trade Receivables	2,138	2,026	2,097	2,179	2,255
Other Current Assets	12,545	10,865	8,384	5,407	3,928
Property, Plant & Equipment	38,294	38,574	39,435	41,331	42,960
Other Non-Current Assets	11,153	10,912	10,293	9,673	9,186
Total Assets	64,716	63,058	61,807	61,026	59,212
Short-Term Debt	4,739	4,941	4,941	4,941	4,941
Other Current Liabilities	16,757	17,121	17,548	17,807	18,050
Long-Term Debt	38,948	35,722	32,187	29,286	25,768
Other Non-Current Liabilities	10,071	10,476	10,476	10,476	10,476
Total Liabilities	70,515	68,260	65,152	62,510	59,234
Total Equity	(5,799)	(5,202)	(3,345)	(1,484)	(23)
Total Equity & Liabilities	64,716	63,058	61,807	61,026	59,212

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

Company Sector

Airlines

Company Description

American Airlines Group is the holding company for American Airlines. Together with wholly owned and third-party regional carriers operating as American Eagle, the airlines operate an average of nearly 6,700 flights per day to 350 destinations in 50 countries from its hubs in Charlotte, Chicago, Dallas/Fort Worth, Los Angeles, Miami, New York, Philadelphia, Phoenix and Washington, D.C. and partner gateways, including in London, Madrid, Seattle/Tacoma, Sydney and Tokyo.

Investment Rationale

AAL's elevated leverage compared to peers drives our Underperform rating. We see a long road for balance sheet repair coming out of the pandemic with management focused on gross debt reduction rather than net debt reduction. Higher fuel prices and inflationary cost pressures makes it difficult to generate meaningful free cash flow in the near term.

Stock Data

Average Daily Volume 33,255,526

Quarterly Earnings Estimates

	2023	2024
Q1	0.05A	-0.17E
Q2	1.92A	1.53E
Q3	0.38A	0.72E
Q4	0.29A	0.54E

Price objective basis & risk

American Airlines Group (AAL)

Our \$12 PO is based on approximately 5x our 2024E EBITDAR. Our target multiple is in line with AAL's legacy peers. We believe the network carriers can trade towards the middle of their historical valuation ranges (4-6x).

Upside risks to our price objective are better than expected pricing, a faster than expected resolution of labor contracts, and a stronger macro backdrop.

Downside risks to our price objective are significant moves in fuel, general economic weakness, government regulation/taxes, safety concerns, and terrorism/geopolitical events.

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US - Airlines and Cruise Coverage Cluster

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	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

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

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

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

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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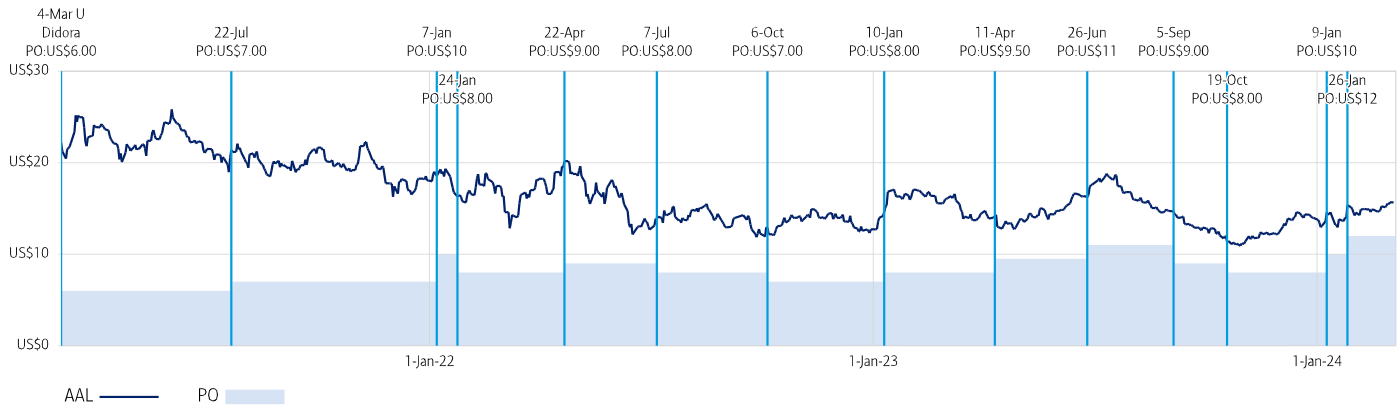
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American Airline (AAL) Price Chart



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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