Qantas Report

Danyang Dai

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Equity Research Association

Qantas Airways Limited (ASX: QAN)

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Research Analysts

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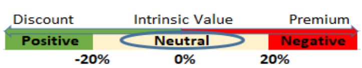
Basic Information

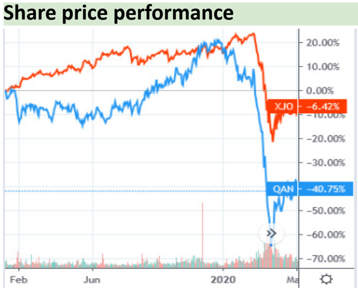
Rating	Neutral
Price (06-May-2020)	$3.50
Market Cap	$5.22b
# shares outstanding	1.49b
52 weeks high/low	$2.03 - $7.46



Key Financials

	2018A	2019A	2020E	2021E	2022E
Revenue($m)	17128	17966	13593	15006	18820
% growth	*6.67%*	*4.89%*	*-24.34%*	*10.40%*	*25.41%*
EBITDA ($m)	3062	3115	1358	2055	3759
% margin	*17.88%*	*17.34%*	*9.99%*	*13.69%*	*19.97%*
Net Profit($m)	953	853	(409)	35	1188
% growth	*6.96%*	*-10.49%*	*-147.95%*	*108.58%*	*3286.33%*
EPS($)	0.544	0.546	-0.274	0.024	0.797
Dividend($)	0.17	0.25	0.00	0.00	0.27
P/E	5.48	6.12	-12.76	148.70	4.39
EV/EBITDA	3.64	3.58	8.20	5.42	2.96

Share price performance



Introduction

We initiate a coverage for Qantas in an objective manner. The estimates in our research are derived from our research framework which takes into account the domestic and international aviation industry conditions, competitive advantages, and past financial performance. The in-depth analysis of our research has also factored in management capabilities, catalysts, and possibilities for Qantas. We have also considered the impact of COVID-19 on Qantas and forecasted its future performance accordingly.

Highlights

- Current Situation (05/05 update): secured $1.6bn total debt funding in response to COVID-19, total short-term liquidity $3.5bn (inc. $1bn undrawn credit facility); currently operating around 5% of its pre-crisis domestic network and 1% international network on ASK basis; incurred hedging losses from large decline in oil prices and closed over-hedged position.
- Qantas maintains powerful competitiveness domestically, especially in the areas of high customer satisfaction, strong brand recognition, low operating costs, effective load management and dominant frequent flyer program, along with 58% market share.
- Qantas International remains a weakness of the group, being threatened by increasing price-based competition, and lack of advantages in operating cost and customer satisfaction. While Qantas' international foothold could be strengthened should Project Sunrise be successfully implemented.
- Qantas boasts strong foundational measures taken in response to the challenges faced by the industry in the future. These measures revolve around the four global forces that Qantas believes are likely to have the biggest impact on their operations.
- We predict a full capacity recovery by Jan 2021. While the lower demand and seat factor (down to 50%) in FY20 & FY21 are expected to dampen the profit margins. Post-COVID-19, Qantas is expected to strengthen the grip of domestic market share as Virgin enters administration but experience a fall in business travel demand due to the behavioural impact of COVID-19.
- The lower fuel cost and more efficient aircrafts are estimated to enhance profit margins by 3.4% from FY22 onwards (relative to FY19). We predict that an increase in gross Capex from 10.71% of revenue in FY19 to 14.22% in FY22 is necessary to replace several old models of aircrafts.

Valuations

We estimate the intrinsic value of Qantas to be **$4.24/share** through a DCF model. The current share price of $3.50 represents a **17.5% discount**. Currently trading at trailing P/E 6.12 and EV/EBITDA 3.58, Qantas' relative valuation is at appropriate level vs industry peers. Upon considering the valuation and all the factors discussed, we hold a **Neutral** outlook for Qantas.

Risks

- Inherent risks in the airline industry: volatility in fuel price and foreign exchange, increasing intensity of competition, exposure to the fluctuation of economy, irreducible risks arising from exogenous events.
- Direct impact of COVID-19: possibility of more prolonged crisis than expected, uncertainty of pace of recovery, significant labour surplus, increased debt load, uncertainty of further debt/equity raising.