

# Air New Zealand

## 1H21 Preview — Holding Pattern, Low on Fuel

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### NEUTRAL

Air New Zealand (AIR) is due to report significant underlying half year losses on 25 February 2021, reflecting the impact of border closures and other government restrictions on passenger travel. We estimate a pre-tax loss (PBT) of -NZ\$184m in 1H21, but recognise an abnormally high margin for error in this forecast. While AIR has provided (1) monthly cash burn guidance, (2) pax operating stats, and (3) details of cost reductions, the impact of working capital movements and revenue from airfreight and other non-pax sources will heavily influence the quantum of losses. Looking forward, the pax recovery profile has been pushed out by a combination of (1) new recent community cases on both sides of the Tasman, (2) the persistence of COVID-19 in beating border controls, (3) the NZ Government's unwavering stance of health first, and (4) the relative speed (slower than other countries including Australia) of NZ's vaccination programme. This will likely prolong AIR's losses deep into FY22 (downside risk to our forecasts persist) and further dent the outlook for net asset value (NAV).

NZX Code	AIR	Financials: Jun/	20A	21E	22E	23E	Valuation (x)	20A	21E	22E	23E
Share price	NZ\$1.54	NPAT* (NZ\$m)	-64.2	-200.5	59.8	121.5	PE	n/a	n/a	29.0	14.3
Target price	NZ\$1.60	EPS* (NZc)	-5.7	-17.9	5.3	10.8	EV/EBIT	n/a	n/a	46.7	27.1
Risk rating	High	EPS growth* (%)	n/a	n/a	n/a	n/a	EV/EBITDA	6.7	9.9	6.2	5.5
Issued shares	1123.0m	DPS (NZc)	0.0	0.0	0.0	10.0	Price / NTA	1.5	1.9	1.7	1.7
Market cap	NZ\$1,735m	Imputation (%)	100	100	100	100	Cash div yld (%)	0.0	0.0	0.0	6.5
Avg daily turnover	2,773k (NZ\$3,924k)	*Based on normalised profits					Gross div yld (%)	0.0	0.0	0.0	9.0

#### Key things to consider ahead of the result:

- Capital raise:** AIR has said that it will undertake an equity raise (with support from the Crown) to strengthen its balance sheet by the end of FY21. The total amount required to navigate COVID-19 remains uncertain.
- Cash burn:** Previous cash burn guidance was for monthly net outgoings of NZ\$65m–NZ\$85m. This suggests the company will now be ~NZ\$500m into the government's NZ\$900m loan facility.
- Airfreight offset:** AIR has said that airfreight has been around ~30% of the previous long haul business.
- Passenger revenue:** Monthly operating stats suggest pax revenue is down ~73% in 1H21 against the prior year.
- Recovery profile:** The prospect of NZ's border restrictions loosening (including a trans-Tasman bubble) ahead of mass inoculation appears increasingly remote. This will impact the capital needs of AIR and may result in further cost base initiatives.

#### Conference call

AIR will host a result conference call on 25 February 2021 at 10am. Register at: <https://edge.media-server.com/mmc/p/8pk6stwo>

**Figure 1. Summary of 1H21 forecasts (NZ\$m)**

	1H20	1H21E	Change
Sales revenue	3,015	1,139	-62.2%
EBITDRA	615	232	-62.3%
<b>Underlying PBT</b>	<b>198</b>	<b>(184)</b>	<b>-192.8%</b>
Reported NPAT	101	(127)	-225.9%
Underlying NPAT	149	(127)	-185.6%
Underlying EPS (cents)	13.1	(11.4)	-186.6%
Interim DPS (cents)	0.0	0.0	n/a

Source: Forsyth Barr analysis

**Figure 2. Revenue forecasts summary (NZ\$m)**

	1H20	1H21E	Change
Domestic	851	565	-33.5%
Tasman & Pacific Islands	688	45	-93.5%
International	1,038	94	-91.0%
Passenger revenue	2,576	704	-72.7%
Cargo	195	260	33.3%
Contract services & other	244	175	-28.3%
<b>Total revenue</b>	<b>3,015</b>	<b>1,139</b>	<b>-62.2%</b>

Source: Forsyth Barr analysis

## Air New Zealand Ltd (AIR)

Priced as at 19 Feb 2021 (NZ\$)

1.55

### 12-month target price (NZ\$)\*

1.60

Expected share price return

3.2%

Net dividend yield

0.0%

Estimated 12-month return

3.2%

### Key WACC assumptions

Risk free rate

1.30%

Equity beta

1.40

WACC

8.9%

Terminal growth

1.0%

### Spot valuations (NZ\$)

1. Net asset value plus loyalty

1.60

2. n/a

n/a

3. n/a

n/a

### DCF valuation summary (NZ\$m)

Total firm value

n/a

(Net debt)/cash

n/a

Less: Capitalised operating leases

n/a

Value of equity

n/a

Profit and Loss Account (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Sales revenue	5,785.1	4,836.2	2,333.3	3,635.3	4,656.3
<b>Normalised EBITDA</b>	<b>935.1</b>	<b>784.2</b>	<b>523.3</b>	<b>867.9</b>	<b>976.5</b>
Depreciation and amortisation	(567.0)	(841.0)	(754.4)	(753.1)	(778.9)
<b>Normalised EBIT</b>	<b>368.1</b>	<b>(56.8)</b>	<b>(231.1)</b>	<b>114.8</b>	<b>197.6</b>
Net interest	(31.0)	(69.0)	(101.6)	(70.8)	(67.9)
Associate income	37.0	39.0	39.0	39.0	39.0
Tax	(104.0)	22.5	93.2	(23.2)	(47.2)
Minority interests	0	0	0	0	0
<b>Normalised NPAT</b>	<b>270.1</b>	<b>(64.2)</b>	<b>(200.5)</b>	<b>59.8</b>	<b>121.5</b>
Abnormals/other	0	389.5	0	0	0
<b>Reported NPAT</b>	<b>270.1</b>	<b>(453.8)</b>	<b>(200.5)</b>	<b>59.8</b>	<b>121.5</b>
Normalised EPS (cps)	23.9	(5.7)	(17.9)	5.3	10.8
DPS (cps)	22.0	0	0	0	10.0

Growth Rates	2019A	2020A	2021E	2022E	2023E
Revenue (%)	5.5	-16.4	-51.8	55.8	28.1
EBITDA (%)	-12.2	-16.1	-33.3	65.8	12.5
EBIT (%)	-31.8	n/a	n/a	n/a	72.1
Normalised NPAT (%)	-30.8	n/a	n/a	n/a	>100
Normalised EPS (%)	-30.4	n/a	n/a	n/a	>100
Ordinary DPS (%)	0.0	-100.0	n/a	n/a	n/a

Cash Flow (NZ\$m)	2019A	2020A	2021E	2022E	2023E
<b>EBITDA</b>	<b>935.1</b>	<b>784.2</b>	<b>523.3</b>	<b>867.9</b>	<b>976.5</b>
Working capital change	245.0	0	(0.0)	0	0
Interest & tax paid	(135.0)	134.0	26.1	(54.0)	(69.7)
Other	(59.1)	(688.2)	(390.2)	127.3	226.7
<b>Operating cash flow</b>	<b>986.0</b>	<b>230.0</b>	<b>159.2</b>	<b>941.1</b>	<b>1,133.5</b>
Capital expenditure	(821.0)	(615.0)	(300.0)	(550.0)	(800.0)
(Acquisitions)/divestments	13.0	109.0	40.0	40.0	40.0
Other	(75.0)	(95.0)	(102.0)	(101.6)	(101.6)
<b>Funding available/(required)</b>	<b>103.0</b>	<b>(371.0)</b>	<b>(202.8)</b>	<b>329.5</b>	<b>271.9</b>
Dividends paid	(260.0)	(130.0)	0	0	(112.3)
Equity raised/(returned)	(14.0)	0	0	0	0
<b>(Increase)/decrease in net debt</b>	<b>(171.0)</b>	<b>(501.0)</b>	<b>(202.8)</b>	<b>329.5</b>	<b>159.6</b>

Balance Sheet (NZ\$m)	2019A	2020A	2021E	2022E	2023E
Working capital	60.0	89.0	99.0	95.1	92.0
Fixed assets	5,268.0	3,336.0	3,056.7	3,044.8	3,270.2
Intangibles	186.0	186.0	186.0	186.0	186.0
Right of use asset	0	2,357.0	2,430.0	2,514.9	2,583.7
Other assets	602.0	815.0	831.0	846.6	862.2
<b>Total funds employed</b>	<b>6,116.0</b>	<b>6,783.0</b>	<b>6,602.7</b>	<b>6,687.4</b>	<b>6,994.1</b>
Net debt/(cash)	1,542.0	1,025.0	1,210.1	844.0	653.4
Lease liability	0	2,238.0	2,413.0	2,588.0	2,763.0
Other liabilities	2,485.0	2,202.0	1,874.0	2,074.0	2,374.0
Shareholder's funds	2,089.0	1,318.0	1,105.5	1,181.4	1,203.7
Minority interests	0	0	0	0	0
<b>Total funding sources</b>	<b>6,116.0</b>	<b>6,783.0</b>	<b>6,602.7</b>	<b>6,687.4</b>	<b>6,994.1</b>

\* Forsyth Barr target prices reflect valuation rolled forward at cost of equity less the next 12-months dividend

Valuation Ratios	2019A	2020A	2021E	2022E	2023E
EV/EBITDA (x)	3.4	3.9	5.5	3.4	3.0
EV/EBIT (x)	8.7	n/a	n/a	25.7	14.9
PE (x)	6.5	n/a	n/a	29.1	14.3
Price/NTA (x)	0.9	1.5	1.9	1.7	1.7
Free cash flow yield (%)	9.5	-22.1	-8.1	22.5	19.2
Net dividend yield (%)	14.2	0.0	0.0	0.0	6.5
Gross dividend yield (%)	19.7	0.0	0.0	0.0	9.0

Capital Structure	2019A	2020A	2021E	2022E	2023E
Interest cover EBIT (x)	11.9	n/a	n/a	1.6	2.9
Interest cover EBITDA (x)	30.2	11.4	5.1	12.3	14.4
Net debt/ND+E (%)	42.5	43.7	52.3	41.7	35.2
Net debt/EBITDA (x)	1.6	1.3	2.3	1.0	0.7

Key Ratios	2019A	2020A	2021E	2022E	2023E
Return on assets (%)	4.7	-0.8	-3.1	1.5	2.5
Return on equity (%)	12.9	-4.9	-18.1	5.1	10.1
Return on funds employed (%)	n/a	n/a	n/a	n/a	n/a
EBITDA margin (%)	16.2	16.2	22.4	23.9	21.0
EBIT margin (%)	6.4	-1.2	-9.9	3.2	4.2
Capex to sales (%)	14.2	12.7	12.9	15.1	17.2
Capex to depreciation (%)	145	73	40	73	103
Imputation (%)	100	100	100	100	100
Pay-out ratio (%)	92	0	0	0	92

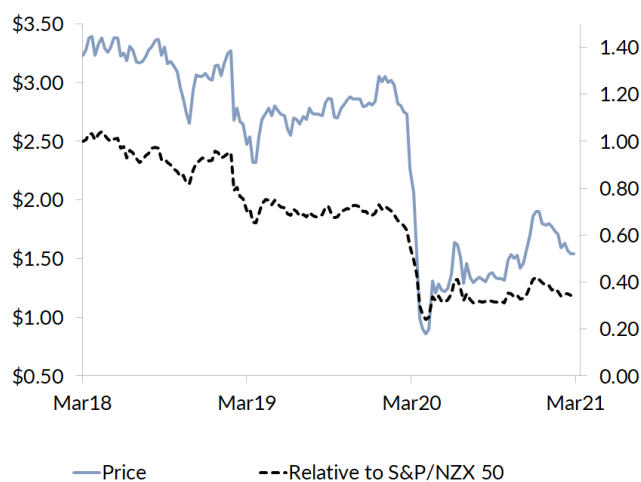
### Operating Performance

Available Seat Km (ASK)	2019A	2020A	2021E	2022E	2023E
Domestic	7,104	5,619	4,618	5,683	6,394
Tasman and Pacific	13,640	10,367	4,092	10,912	12,276
Long-haul	25,285	20,349	2,529	7,586	17,700
<b>Total</b>	<b>46,029</b>	<b>36,335</b>	<b>11,238</b>	<b>24,181</b>	<b>36,369</b>
Change (%)	4.0	-21.1	-69.1	115.2	50.4

RASK (cents per ASK)	2019A	2020A	2021E	2022E	2023E
Domestic	22.5	23.6	22.0	22.0	21.8
Tasman and Pacific	9.6	9.4	7.5	9.2	9.1
Long-haul	8.1	8.1	5.8	7.4	7.6
<b>Total</b>	<b>10.8</b>	<b>10.8</b>	<b>13.1</b>	<b>11.6</b>	<b>10.6</b>

Costs	2019A	2020A	2021E	2022E	2023E
Jet fuel (NZ\$m)	1,271	1,022	250	642	893
Unit fuel (cents/ASK)	2.8	2.8	2.2	2.7	2.5
CASK ex-fuel/forex (cents/ASK)	7.4	8.4	16.1	11.4	10.1

Normalised EBIT	368.1	(56.8)	(231.1)	114.8	197.6
Net interest	(31.0)	(69.0)	(101.6)	(70.8)	(67.9)
Associate income	37.0	39.0	39.0	39.0	39.0
<b>Normalised PBT</b>	<b>374.1</b>	<b>(86.8)</b>	<b>(293.7)</b>	<b>83.0</b>	<b>168.7</b>

**Figure 3. Price performance**


Source: Forsyth Barr analysis

**Figure 4. Substantial shareholders**

Shareholder	Latest Holding
NZ Govt	52.5%

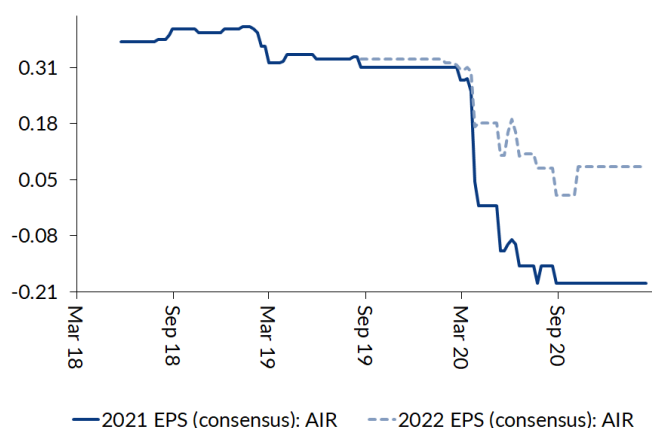
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

**Figure 5. International valuation comparisons**

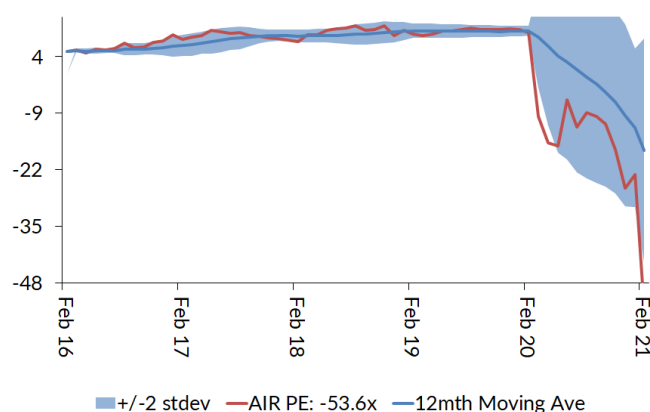
Company	Code	Price	Mkt Cap (m)	PE 2021E	PE 2022E	EV/EBITDA 2021E	EV/EBITDA 2022E	EV/EBIT 2021E	EV/EBIT 2022E	Cash Yld 2022E
(metrics re-weighted to reflect AIR's balance date - June)										
Air New Zealand	AIR NZ	NZ\$1.55	NZ\$1,735	<0x	29.0x	5.3x	3.2x	<0x	24.0x	0.0%
QANTAS AIRWAYS	QAN AT	A\$4.70	A\$8,864	<0x	14.6x	20.7x	4.6x	<0x	12.5x	1.7%
CATHAY PACIFIC AIRWAYS	293 HK	HK\$6.99	HK\$44,996	<0x	1.1x	<0x	10.4x	<0x	<0x	1.1%
SINGAPORE AIRLINES	SIA SP	S\$4.40	S\$13,046	<0x	<0x	<0x	7.7x	<0x	<0x	0.3%
DEUTSCHE LUFTHANSA-REG	LHA GY	€10.72	€6,405	<0x	8.8x	5.6x	10.2x	<0x	2.5x	0.1%
AIR FRANCE-KLM	AF FP	€4.78	€2,050	<0x	<0x	6.3x	6.5x	2.0x	5.6x	n/a
AMERICAN AIRLINES GROUP INC	AAL US	US\$17.65	US\$11,284	<0x	>50x	<0x	<0x	<0x	24.4x	0.0%
UNITED AIRLINES HOLDINGS INC	UAL US	US\$44.71	US\$13,939	<0x	5.2x	30.0x	38.1x	<0x	1.9x	n/a
Compco Average:				n/a	7.5x	15.7x	12.9x	2.0x	9.4x	0.6%
AIR Relative:				n/a	290%	-66%	-75%	n/a	157%	-100%

EV = Current Market Cap + Actual Net Debt

Source: \*Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (AIR) companies fiscal year end

**Figure 6. Consensus EPS momentum (NZ\$)**


Source: Forsyth Barr analysis

**Figure 7. One year forward PE (x)**


Source: Forsyth Barr analysis

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