FIIG | Factsheet

Qantas Airways Ltd

21 September 2022

Sector: Corporate
Sub-sector: Transportation
Country: Australia
Ownership: Public

Disclaimer

This bond or financial product has not been reviewed or recommended by FIIG research nor should this document be considered as credit research. This Factsheet is only a summary document, designed to assist Investors identify the key elements of the company bond or financial product referred to in this document and should be read in conjunction with the other offering documentation available in relation to the financial products. This Factsheet is not complete information concerning any financial product and should not be relied on as such.

Issuer Outline

Qantas Airways Limited (Qantas, Group) is Australia's largest domestic and international airline, underpinned by a dominant position in Australia's domestic aviation market, where the airline's dual brands comprise about 65% of domestic capacity.

Qantas' main business is providing regional, domestic, and international air transportation under the Qantas and low cost subsidiary Jetstar Airways brands. The group also operates subsidiary businesses, including other airlines, loyalty and freight services.

Qantas is listed on the ASX and had a market capitalisation of ~AUD10bn as at 20 September 2022.

Key Financials (AUDm)

LTM (30 Jun)	2022
Revenue	9,108
Underlying EBITDA	281
Net Interest Expense	(301)
Total Assets	19,653
Net Debt	3,937
Cash	3,343
Net Debt / EBITDA	11.9x
EBITDA / Interest Expense	0.9x

Source: Company, FIIG Estimates

Summary Bond Details

ISIN	Issue Amount	Ranking	Coupon	Coupon Frequency	First Call[1]	Maturity Date
AU3CB0240059	AUD 250m	Senior Unsecured	4.40%	Semi-Annual	N/A	10 Oct 2023
AU3CB0240109	AUD 300m	Senior Unsecured	4.75%	Semi-Annual	N/A	12 Oct 2026
AU3CB0283182	AUD 500m	Senior Unsecured	3.15%	Semi-Annual	27 Jun 2028	27 Sep 2028
AU3CB0268357	AUD 425m	Senior Unsecured	2.95%	Semi-Annual	27 Aug 2029	27 Nov 2029
AU3CB0274280	AUD 500m	Senior Unsecured	5.25%	Semi-Annual	9 Jun 2030	9 Sep 2030

[1]Excludes potential terms that would allow the issuer to redeem prior to the maturity date through a make-whole call.

The fixed income experts

Qantas Airways Ltd

Strengths

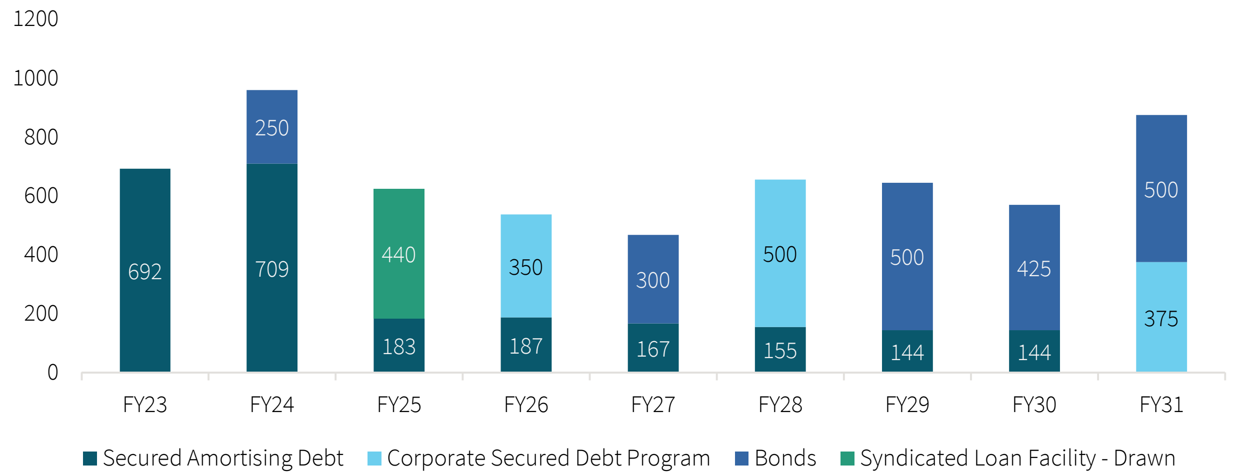
- Dominant market position, supported by relatively high barriers to entry: Qantas retains a dominant position in the Australian domestic airline sector with a market share of approximately 65% across both its Qantas and Jetstar brands. Barriers to entry are high, while a lack of suitable alternatives between Sydney and Melbourne (one of the world's busiest air routes), and to a lesser extent, Sydney and Brisbane, ensures a relatively dominant position in the normal course of business. Qantas' international operations are unmatched in the Australian market (but less so on a worldwide basis) and enjoys a more-than-dominant position.

  Qantas has benefited from Virgin Australia's repositioning as a mid-market carrier following its re-emergence from voluntary administration (but in a much more limited capacity). With Virgin now owned by private equity, the focus on profitability and the need to generate an adequate return should ensure that competition in the domestic market remains rational with respect to both capacity and pricing. The emergence of Rex Airlines will also increase competition. Qantas is now the only airline with a full-service and low-cost offerings in Australia, and is well-positioned to leverage the recovery in travel demand post COVID-19.

- Dual brand strategy captures multiple customer sets: The successful differentiation between the Qantas and Jetstar brands allows Qantas to hold the largest market share in the business, premium, and low cost segments of the Australian market simultaneously. This dual brand strategy enables the Group to allocate aircraft capacity based on targeted customer segments, which typically results in the Qantas brand being used for routes with high business traffic, and the Jetstar brand used for routes primarily servicing tourism destinations.

  Strong balance sheet provides financial flexibility: Prior to the pandemic, Qantas had a strong balance sheet with Net debt/EBITDA of around 1.4x for the twelve months ended 30 June 2019, significantly below its rating threshold of 2.5x. Although Net debt/EBITDA has easily exceeded this threshold during since the pandemic, it is expected the Company will revert toward pre-pandemic levels through a combination of debt reduction (Three-Year Recovery Plan) and more normalised earnings. In the interim, Qantas continues to retain significant flexibility in its financial position, funding strategies and fleet plans which has allowed it to continue to raise funds and generate liquidity in the face of changing market conditions. Total liquidity sits at AUD4.6bn as at 30 June 2022 (with Qantas benefiting from the issue of long-dated term debt during the pandemic) while the Company's debt maturity more broadly is well-staggered (see Figure 1), with both factors contributing to minimal refinancing risk.

  Figure 1: Debt maturity profile as at 30 June 2022 (millions)



Source: Company

Qantas Airways Ltd

- Commitment to maintaining investment grade credit rating: Qantas' publicly articulated financial framework triggers pre-emptive actions to fortify its balance sheet in the event of significant operational weakness. An example of this was its actions throughout the pandemic, where Qantas suspended shareholder distributions, reduced capital expenditure and raised equity, all of which helped to preserve cash. Although its leverage metrics are still above the threshold for its current rating, Qantas' publicly announced balance sheet repair initiatives to reduce net debt, headlined by the sale of Mascot land more recently and Three-Year Recovery Plan, has been sufficient to maintain its investment grade credit rating.
- Asset rich business: Qantas is an asset rich business, with a number of significant entities and opportunities to reduce debt levels through asset sales if needed. A recent example of this was the Mascot land sale in October 2021 for gross proceeds of AUD802m, which assisted (although not solely) the Company in returning its level of net debt below its target range of AUD4.5bn-AUD5.6bn in FY22 (currently AUD3.94bn). Unencumbered assets (prior to the sale of Mascot) were at AUD2.5bn, including 41% of the Qantas fleet, land, spare engines and other assets. Maturing secured debt facilities in FY23 to FY25 (see Figure 1 above) will further unencumber mid-life aircraft.

Risks

- Exposure to highly cyclical and confidence-sensitive industry: The nature of the airline industry presents a risk for bond holders due to it being cyclical, capital intensive, exposed to 'force majeure' events such as terrorism and global pandemics, as well as the cost of jet fuel which fluctuates with movements in the underlying commodity. While the worst of the COVID-19 pandemic has passed, material uncertainty remains around the length of time to recover to pre-pandemic levels. Qantas has the ability to defer significant capital expenditure, which can provide further cash or liquidity to meet short-term liquidity needs in response to cyclical factors. Increasing contribution from loyalty and freight services, which are likely to be less-susceptible to cyclical factors, should also provide an increasing proportion of earning with recurring characteristics.
- International business exposed to strong competitive dynamics : Qantas' international business has underperformed financially in recent years due in large part to the increase in competition which has come with the deregulation of routes, and heightened competition from state-sponsored competitors, who are unlikely to have the same financial hurdle rates compared with Qantas. An output of Qantas' Three-Year Recovery Plan (see below for more details) has been a significant improvement in the Group's cost base and unit cost performance (particularly within its domestic and international segments), which has improved its competitive position and yield premium compared with its competitors. While continuing pandemic effects are causing the international segment to underperform Qantas' domestic operations, as international travel gradually resumes, stronger returns from the international segment should emerge.
- Exposure to fuel and foreign exchange risks: Qantas, as is the case for all airlines, has a high exposure to oil price and foreign exchange. This is because fuel costs represent a material portion of total costs and these costs, together with aircraft purchases and aircraft leases, are typically denominated in US dollars. To mitigate these risks to the greatest extent manageable, Qantas has historically maintained significant level of hedging. Rising fuel prices will act as a drag on Qantas in the short-term with the Company expecting total costs to reach AUD5.0bn in FY23. Although hedging will play a part, Qantas will also pass on the price increases to customers in an attempt to reduce its exposure to higher costs.
- High level of execution risk associated with its recovery plan and balance sheet repair initiatives: In response to the grounding of Qantas' fleet in March 2020 due to the pandemic, Qantas announced a three-year plan for recovery, looking to produce AUD15.0bn in cost savings by 2023, along with AUD1.0bn in annual (structural) cost savings from 2023. This included a reduction in its workforce of ~6,000 personnel. An inability to deliver the cost reductions as planned or longer than expected pre-pandemic recovery (noting international travel, including freight, accounts for 40% of pre-COVID revenues), could materially negatively impact Qantas' earnings over the coming years. We note that progress to-date is ahead of target (Qantas has delivered structural savings of AUD920m and is on track for at least AUD1bn from 2023) also helped by improved capacity levels (50% in 2H22 from 18% in 1H22, 63% in 4Q22). Qantas is committed to restoring its credit profile, and has the liquidity to mitigate any timing risk.

Qantas Airways Ltd

Summary Financials

The financial summary below represents the consolidated operations of Qantas Airways Ltd (AUDm, FYE 30 June).

Income Statement	FY18	FY19	FY20	FY21	FY22
Revenue	17,128	17,966	14,257	5,934	9,108
Underlying EBITDA	3,062	3,115	2,437	410	281
Net Interest Expense	(150)	(250)	(242)	(279)	(301)
Depreciation & amortisation	(1,528)	(1,996)	(2,045)	(1,929)	(1,801)
Exceptional Items	(43)	(65)	(1,805)	(568)	(41)
Net income	953	840	(1,964)	(1,728)	(860)
Balance Sheet	FY18	FY19	FY20	FY21	FY22
Cash	1,694	2,157	3,520	2,221	3,343
Goodwill & intangibles	1,113	1,225	1,050	849	778
Net property, plant, and equipment	12,186	13,412	12,404	10,888	11,181
Total assets	18,647	20,535	20,026	17,880	19,653
Total debt	4,748	6,889	8,535	8,229	7,232
Total equity	3,955	3,014	1,526	516	(190)
Cash Flow Statement	FY18	FY19	FY20	FY21	FY22
Cash flow from operating activities	3,413	3,164	1,083	(386)	2,670
Cash flow from investing activities	(2,201)	(1,563)	(1,571)	(722)	(240)
Debt Issued / (Repaid)	(134)	(52)	1,163	(239)	(1,307)
Equity Issued / (Repurchased)	(913)	(735)	894	58	(2)
Credit Metrics	FY18	FY19	FY20	FY21	FY22
Net Debt/EBITDA	1.0x	1.5x	2.1x	14.7x	11.9x
EBITDA/Net Interest Expense	20.4x	12.5x	10.1x	1.5x	0.9x
Debt / (Debt + Equity)	55%	70%	85%	94%	103%

Source: S&P Capital IQ, Company, FIIG Estimates.

Qantas Airways Ltd

The contents of this document are copyright. Other than under the Copyright Act 1968 (Cth), no part of it may be reproduced or distributed to a third party without FIIG's prior written permission other than to the recipient's accountants, tax advisors and lawyers for the purpose of the recipient obtaining advice prior to making any investment decision. FIIG asserts all of its intellectual property rights in relation to this document and reserves its rights to prosecute for breaches of those rights.

Certain statements contained in the information may be statements of future expectations and other forward-looking statements. These statements involve subjective judgement and analysis and may be based on third party sources and are subject to significant known and unknown uncertainties, risks and contingencies outside the control of the company which may cause actual results to vary materially from those expressed or implied by these forward looking statements. Forward-looking statements contained in the information regarding past trends or activities should not be taken as a representation that such trends or activities will continue in the future. You should not place undue reliance on forward-looking statements, which speak only as of the date of this report. Opinions expressed are present opinions only and are subject to change without further notice.

No representation or warranty is given as to the accuracy or completeness of the information contained herein. There is no obligation to update, modify or amend the information or to otherwise notify the recipient if information, opinion, projection, forward-looking statement, forecast or estimate set forth herein, changes or subsequently becomes inaccurate.

FIIG shall not have any liability, contingent or otherwise, to any user of the information or to third parties, or any responsibility whatsoever, for the correctness, quality, accuracy, timeliness, pricing, reliability, performance or completeness of the information. In no event will FIIG be liable for any special, indirect, incidental or consequential damages which may be incurred or experienced on account of the user using information even if it has been advised of the possibility of such damages.

FIIG provides general financial product advice only. As a result, this document, and any information or advice, has been provided by FIIG without taking account of your objectives, financial situation and needs. FIIG's AFS Licence does not authorise it to give personal advice. Because of this, you should, before acting on any advice from FIIG, consider the appropriateness of the advice, having regard to your objectives, financial situation and needs. If this document, or any advice, relates to the acquisition, or possible acquisition, of a particular financial product, you should obtain a product disclosure statement relating to the product and consider the statement before making any decision about whether to acquire the product. Neither FIIG, nor any of its directors, authorised representatives, employees, or agents, makes any representation or warranty as to the reliability, accuracy, or completeness, of this document or any advice. Nor do they accept any liability or responsibility arising in any way (including negligence) for errors in, or omissions from, this document or advice. Any reference to credit ratings of companies, entities or financial products must only be relied upon by a 'wholesale client' as that term is defined in section 761G of the Corporations Act 2001 (Cth). FIIG strongly recommends that you seek independent accounting, financial, taxation, and legal advice, tailored to your specific objectives, financial situation or needs, prior to making any investment decision. FIIG does not make a market in the securities or products that may be referred to in this document. A copy of FIIG's current Financial Services Guide is available at www.fiig.com.au/fsg.

An investment in notes or corporate bonds should not be compared to a bank deposit. Notes and corporate bonds have a greater risk of loss of some or all of an investor's capital when compared to bank deposits. Past performance of any product described on any communication from FIIG is not a reliable indication of future performance. Forecasts contained in this document are predictive in character and based on assumptions such as a 2.5% p.a. assumed rate of inflation (unless otherwise stated), foreign exchange rates or forward interest rate curves generally available at the time and no reliance should be placed on the accuracy of any forecast information. The actual results may differ substantially from the forecasts and are subject to change without further notice. The information in this document is strictly confidential. If you are not the intended recipient of the information contained in this document, you may not disclose or use the information in any way. No liability is accepted for any unauthorised use of the information.