FINANCE FOCUSED

Equity Research Report

RYANAIR

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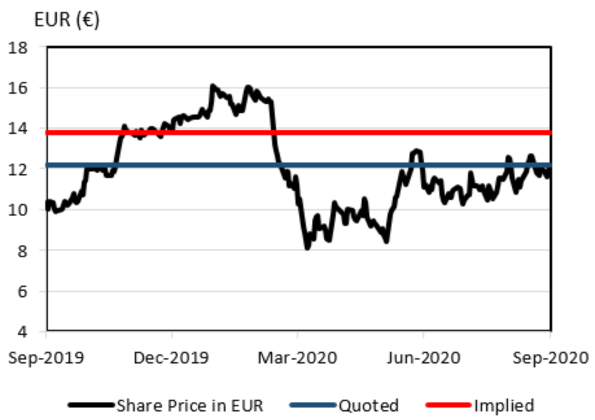
Airline Industry

RYA – LON October 31, 2020

Stock Rating	**HOLD**
Implied Share Price	**€13.77**
Upside (%)	
Share Price (31/10/2020)	€11.98
52-Week Range	€8.14 – €16.10
Shares O/S	1,089,181,737

Share Price



Key Statistics & Valuation

Terminal Growth	1.75%
WACC (%)	5.59%

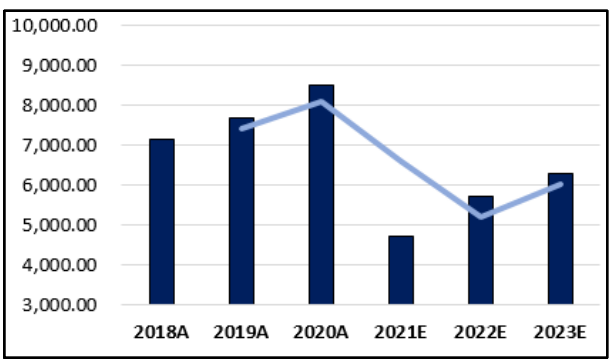
DCF Analysis (Avg.)

Enterprise Value	25,637,000,000
Less: Net Debt	(1,746,000,000)
Equity Value	23,891,000,000
Implied Share Price	**€21.93**

Comparable Companies Analysis

EV/EBITDA Multiple	5.98x
Ryanair EBITDA (LTM)	1,354,700,000
Enterprise Value	8,098,060,000
Less: Net Debt	(1,746,000,000)
Equity Value	6,099,660,000
Implied Share Price	**€5.60**

Revenue Projections



Cheap Tickets, No Perks Unless You Are Willing To Pay!

Overview

Covid 19 has meant that airlines have not been able to operate at full capacity, with much of the future now relying on a vaccine, for normal service to return.

Ryanair Holdings plc provides scheduled airline services across Europe, to destinations from Madrid to Paris. Further services provided consist of ancillary services such as in-flight services, hotel services, car services and travel insurance, through its website and mobile app.

In the airline industry, Ryanair competes as a price leader aiming to be able to offer the lowest price available. As of 30th June 2020, Ryanair is able to offer 2,500 scheduled short flights a day, which serve 242 airports across Europe. Before Covid-19, they were carrying 149 million guests a year.

The company was founded in 1984, and prior to 1990, it aimed to provide a competitive service, built on good customer experiences. Decreasing profits in 1990 led to Michael O Leary, the CFO at that time, restructuring the business model to a similar one to Southwest Airlines. The Southwest airline aims to minimise prices through minimising costs, which involves a quick turnaround at the airport and flying from less popular airports. Ryanair then was able to benefit from the expanding size of the EU, by offering new routes, which led to the company becoming profitable. Through establishing an online service early in 2000, within a year 75% of their bookings were directly from there, reducing the costs imposed by travel agents. A successful business model and constant innovation has led Ryanair to become one of the most successful low-cost airlines in the world.

Business Model

Low cost of operations, low cost to customers, but added ancillary revenue

Ryanair's business model essentially is designed to capture low end budget consumers that expect lower quality of travel and luxury but are attracted to the initial value proposition of the cheap fares and are willing to pay for additional services like check-in luggage, meals, and extra baggage.

The business model originated and copied from an US based airline called Southwest Airlines, but travel services are focused purely on short-haul and inter-European journeys. Typical fare prices range from €6 onwards per passenger versus €9 and €17 for competitors EasyJet and AirBerlin and has a 96% seat fill rate.

Ryanair has a standard hierarchical structure with functional heads reporting directly to the CEO, Michael O'Leary, making it easy for O'Leary to communicate his aggressive cost cutting strategy to divisional heads – short hierarchy with easy access to the CEO with main decisions taken in Ireland.

Operating Model

Innovation by Subtraction

Ancillary revenues is the main reason behind Ryanair's growth and profitability. These include airport check-in penalties, baggage fees, priority boarding and in-flight food and beverage sales.

Airports

Ryanair flights are based predominantly from small secondary airports located further away from city centres, e.g. Bristol, Luton, Newcastle, and Newquay Cornwall, which reduces airport taxes in a bid to keep costs down. By focusing on smaller secondary airports, Ryanair can secure subsidies from local city councils looking to attract more tourists – key factor in quick turnaround time and high fleet utilisation.

Point-to-point Routes

Ryanair's model is a point-to-point model which reduces customer transfer costs from the Hub-and-Spoke Model used by traditional airlines, which has central global airports, hubs, and secondary on route airports, spokes, which are terminals with planes that fly to hub location.

Online Sales Distribution

Online direct to customer sale which eliminates expensive intermediary travel shops and agency costs.

Labour Utilisation and Salaries

Majority of Ryanair's pilots are subcontracted third party pilots that are not on salaries which means Pilots are only paid when they are effectively flying and fully utilised, rather than paying an outright Salary. Standard employees are on Irish labour contracts which allows Ryanair to avoid rules on wages and social benefits that are required by European countries.
Employee compensation includes professional fees which incentivises employees to use low cost hotels and transport methods

Aircrafts

Ryanair only uses the Boeing 737 for its entire fleet which allows Ryanair to reduce its maintenance, repair and overhaul costs, reduced staff training costs, and increase flexibility in staff allocation.

Strategic Analysis

Competitive advantage allows companies to produce a product that offers value through either low price or high quality. From Porter's 3 strategies of competitive advantage, Ryanair specialises in cost leadership, as opposed to focusing on product differentiation or niche strategies. Cost leadership has meant Ryanair strives to have the lowest costs in the industry so they can offer the lowest price while maintaining high-profit margins.

Ryanair offers a no-frills travel service, aiming to provide the basic service to fulfil minimum expectations of customers. CAPA – Centre of Aviation found that Ryanair had the lowest unit costs of any European airlines under several different measures, which include cost per seat and cost per passenger. Innovative methods such as online check-ins, hand luggage only and automated bag drops have meant Ryanair requires fewer employees for their operations. Efficient processes such as minimising time their airplanes are parked in airports, which reduces the rent they incur. Minimising costs has allowed Ryanair to be flexible with their prices and has enabled them to attract a large number of different demographics. Through being able to always compete on price, Ryanair are able to combat any competitors who also try to adjust their price of travel. This strategy has meant that Ryanair has been able to offer prices 30-50% lower than full-service carriers.

Other strategies such as product differentiation could be seen as a possible long-term opportunity. Offering more specialised services such as business travel packages or more in-flight facilities such as entertainment or food could be part of this strategy. Given the nature of Ryanair's current low-end reputation, it would require vast improvements, for this to be effective. These added extras may increase costs, reducing Ryanair's margins, with additional revenue not being able to maintain the previous margins. Ryanair remains coy on remaining a cost leader, as seen with their recent new planes being designed with no reclining chairs and safety cards stuck on the back of seats.

Corporate Social Responsibility

"Everybody knows that when you fly Ryanair you enjoy the lowest fares. But do you know you are travelling on the airline with Europe's lowest emissions as well?" is the tagline behind most of Ryanair's adverts and promotions. According to their annual report, they have invested heavily in environmental programs and have made significant progress, which include being the first airline to publish monthly CO2 statistics, removing 82% of non-recyclable plastics, and continued investments in Verified Carbon Standard and Gold Carbon Standard projects.

However, the claims made by Ryanair was on the basis of CO2 released per passenger kilometre, not overall emissions. If we consider overall carbon footprint, it displays a completely different outlook. According to EU Emissions Trading System registry, nine of the top 10 CO2 emitters are coal-fired power plants. The tenth is Ryanair which released 9.9 megatons of greenhouse gases in 2018 - a 6.9% increase from 2017.

How did Ryanair come to this very different conclusion from EU ETS? They used CO2 per passenger instead of total carbon footprint. In a report released by Ryanair in 2020, they claim themselves to be Europe's Cleanest and Greenest Airlines Group. While the targets listed therein are promising, they are only effective if the route to reaching them is through decreasing Carbon footprint and investing in fuel efficient new aircrafts and improved technologies instead of increasing their passenger load capacity.

In 2014, Ryanair launched its "Always Getting Better Customer Charter" which underpins their relentless drive towards improving all aspects of Ryanair's customers and to maintain transparency. Through charitable partnerships not limited to the environmental sector, Ryanair is helping give back to the community. Ryanair encourages its passengers to contribute towards environmental charities and NGOs towards which 2% of their passengers have made a contribution. Other measures include paperless practice at Ryanair's Green Dublin Practice, consumables recycling etc. While Ryanair has the best CO2 per passenger, it has a long way to go for actually reducing its carbon footprint and recycling activities as well as investment in cleaner fuel needs to not only continue, but also accelerate.

Risk Analysis

Competition

Given that Ryanair's business model only conducts business in Europe, its top competitors are primarily Eurocentric focused include the following, Finnair, easyJet, Flybe, Norwegian Air Shuttle, Pegasus Airlines and Wizz Air. Ryanair will likely remain very competitive in its industry, given the lowest travel ticket prices, lowest unit costs of any European airlines under several different measures. It is main competitor will be assumed as EasyJet which serves a mere 30 bases, 159 airports, and 1051 routes compared to Ryanair's 86 bases, 219 airports and 2100 routes. Ryanair also has a 200% higher average online website visits compared to EasyJet for the 2H19 period. Therefore, from a competitor, and a direct rival point of view, Ryanair competitor risks remain slim compared to other substantial material risks such as Covid-19.

Covid-19

Covid-19 and the recent resurgence in European, including UK regional, locations will likely continue to have material adverse impact on the aviation industry as a whole. As the UK continues to add countries such as the Greek Islands and Portugal to the quarantine list, European countries which Ryanair predominantly conducts its business in, will impact the bottom line. Ryanair suffered substantial decline in international and domestic related flights during the quarter ending March 31, 2020 and has taken necessary action to accompany reduced demand. This includes, reducing limiting flight schedules, grounding a substantial portion of its fleet, reducing CAPEX, and renegotiating contracts with personnel, airports, and vendors.

Furthermore, as a result of Covid-19, the airline industry will face additional COVID related costs such as enhanced aircraft cleaning equipment, alongside with potential further cleaning and safety measures, which may be costly and time intensive, further increasing overall operating costs. Ryanair, as well as the entire industry as a whole, will be subject to Covid-19 related risks for the intermediate term, and recovery in business will depend on disease moderation, possible second winter wave, and other future Covid-like breakouts in the future.

Debt and Contractual Agreements (Funding Risks)

Ryanair, as quoted in the annual report, "has a significant amount of debt and fixed obligations, and insufficient liquidity may have material adverse effect on the Company's financial conditions". Historically the company has been able to generate sufficient cash flow from operations to service these debts, Covid-19, as highlighted above may be an external shock significant enough to prevent that. Since Covid-19, Ryanair has seen an increased demand in customer refunds which reduces cash flow. Coupled by increasing travel corridors prevents demand from picking up. However, from a corporate bond perspective, funding via capital markets, especially given lower funding costs due to the ECB CSPP programme can be a backstop method to refinance debt. Ryanair has also reduced CAPEX and halted its strategic growth plans in a bid to keep liquidity buffers reasonable.

Commodity markets and raw materials

Global dollar depreciation, and the combination of WTI and Brent crude rallying post April negative territories, and the likely forecast of increasing oil prices as global activity picks up, will be contributing factors towards increasing costs of raw materials, i.e. jet fuel. Ryanair will be subject to, indirectly, on the growing geopolitical tensions in the middle east, potential terrorist attacks, and any bipartisan political pressures such as the Russia-Saudi oil dispute earlier this year.

Industry Analysis

The global low-cost carrier industry is one of which offers to fulfil the customers primary fundamental objective – travel to and from point A to point B for as little cost as possible. The pioneering firm, of the low-cost air travel business model, was Southwest Airlines, founded in 1967, which aimed to provide scheduled budget intrastate flights within the state of Texas, and eventually branched out to wider states by the 1990s.

Since the founding of Southwest Airlines, other US based budget airlines followed included JetBlue Airways and Frontier Airlines, with the first EU based budget airline being founded in 1984 which ultimately became to be Ryanair. Since Ryanair, other prominent EU based airlines were founded, most notably EasyJet, and by 2019 the LCC industry inhabited 49 individual airlines globally. By 2017, the low-cost airline market accounted for 31% of the world's total airline seat capacity, and as of 2020, the LCC industry is worth an estimated $163bn with a projection of $247bn by 2025. Between 2019 and 2005, the LCC market is projected to expand at a CAGR of 8.62%

The industry business model is largely homogenous, with point-to-point travel being inherently hard to differentiate, and as standard fares are pegged very low, starting at €6 per passenger with Ryanair, the quality of transport provided is also largely similar. Therefore, the main sources of revenue for this industry comes from customer add-ons, generating ancillary revenue, and greater volume of consumer travel from price competition compared to the standard Full-Service Carrier (FSC) airlines. Customers will be expected to pay for services such as carry-on baggage, hospitality and drinks, seat assignment and extra leg room. Product differentiation, as mentioned, is minimal but due to the growing competition in the LCC industry, airlines such as JetBlue offers satellite television and Air India express offers complementary meal and beverages.

Combined with the minimal features of budget travel, the LCC industry costs are kept to a minimal due to online ticket sales and check-ins which eliminates fixed physical costs of intermediaries and agents, standardized fleet of Boeing 737s and Airbus A320s, operations in regional or secondary cities, high aircraft utilisation rates and point-to-point travel. The main fleet supplier consists only of Boeing and Airbus which means the industry is exposed to the same supplier costs and external factors. Furthermore, since only 737s and A320s are the desired fleet of choice, maintenance and on-aircraft training costs are kept to a minimal compared to having a diverse fleet. Other common practises include hiring staff through third-party agencies which means pilots are only paid for airtime only.

Regionally, LCCs account for 32% of seat capacity in North America, 20% in Europe, 26% in Asia pacific and 54% in southwest Asia. In Europe, airline seat capacity was up by 3.1% in 2019 compared to a 6.6% increase in 2018 with seat growth in Europe being the lowest since 2013 but still higher than FSC seat growth. Despite the slowing down in Europe, the rise in internet access and growing middle-class in Asia pacific and southwest Asia, has led to the strongest growth rate in the LCC industry. Asia pacific alone accounts for 600mm seats, or 35% of global LCC seats in 2018. In Malaysia, LCCs now account for 50% of the market, giving it one of the highest international penetration rates in the world.

Porters 5 Forces

Competition in the Industry → High

Ryanair focuses on Short-haul flight routes in Europe. Easy Jet, Wizz Air, Finnair, and Norwegian Air Shuttle are some of its competitors. While we saw Ryanair's competitive advantage as low fares, the competition to cover a maximum number of routes at the least cost is very high. Competition in this industry makes companies aim to provide most affordable prices to retain customers.

There are some barriers to enter, but there are quite a lot of low cost competitors entering the market each year. For customers, whose choice is mainly governed by fares, switching costs between companies are low, which further influences rivalry.

Potential of new entrants into the industry → Moderate

With a lot of capital investment required, this industry is an expensive industry to enter for new entrants. The entry barriers are high. Ryanair focuses on a model where a proportion of its aircrafts are leased. For new entrants, purchasing or even leasing jets is expensive. Restricted slot availability for a new airline makes it difficult to find suitable airports.

Ryanair has been able to utilise economies of scale and with experience, developed low operational costs. Thus, in the LCC industry, a lot of such factors restrict an airline from being profitable. Thus, the threat of new entrants is not high for Ryanair.

Power of Suppliers → High

Ryanair purchases or leases its planes from Boeing. There are only two manufacturers of airplanes: Boeing and Airbus. The Duopoly has enabled the manufacturers to charge high prices for the aircraft. Since Ryanair became the biggest purchasing customer of Boeing in Europe, it opened the doors for better than market rates to Ryanair from Boeing. The overall capital costs still remain high.

The price of aviation fuel is closely dependent on the oil price. Ryanair aims to reduce that risk by hedging. Unlike in case of bargaining with Boeing, Ryanair cannot attempt to bargain the prices of fuel from the suppliers. Therefore, the bargaining power of the suppliers is high against Ryanair.

Power of Customers → High

Because of the nature of the LCC industry, customers are attracted not to specific airlines, but only to cheap fares. The lower the price, larger the customer base. The demand elasticity of price thus is high.

All low fare airlines are working towards reducing their operating expenses and offering the flyers with greater facilities. Further, the profit Ryanair makes is heavily dependent on the volume of passengers and the seat load factor. This makes the bargaining power of the customers higher.

Threat of Substitute Products → Low

Ryanair focuses on short-haul routes in Europe where one can also travel using trains, ferries, cars, and buses. These alternatives take a longer time, and oftentimes are more expensive than a Ryanair flight's price. Since Ryanair falls in the LCC industry, the customer cares about the low cost and not brand loyalty.

Ryanair effectively compares their rates with train fares etc on their website to utilise their competitive advantage - lowest costs.

Financial Analysis

Revenues

Ryanair operates solely in Europe and includes airlines such as Buzz in Poland, Lauda in Austria and Germany and Malta Air in Italy and France. Ryanair's Revenue is broken down into Scheduled Revenue and Ancillary Revenue. Scheduled Revenue comprises of scheduled passenger bookings for flights and made up 66% of Ryanair's total revenue in FY20. Ancillary Revenue comprises of non-flight scheduled operations, in-flight sales and internet-related services and made up 34% of total revenue.

Total Revenue grew by 10.4% from €7,697m in FY19 to €8,495m in FY20. The compound annual growth rate between FY18-FY20 was 9% signalling in FY20 Ryanair outperformed. This was due to an increase in ancillary spending by 16% per passenger, with addition to a 4% increase in passenger traffic. Ancillary Revenue has been increasing at a large growth rate over the last few years with growth of 20% from FY19-FY20 and was the same rate in FY18-FY19. The fast growth can be attributed to the successful launch of Ryanair Rooms, where they advertise hotel and accommodation services which they then receive a commission from.

COVID-19 impacted Ryanair's last quarter of FY20 (Jan20-Mar20), where EU governments tried to limit the spread of the disease, leading to a 12% reduction in booked passengers. The impacts of COVID-19 on travel can be on full display in Ryanair's first-quarter report (Apr-June) of FY21, where there was a 95% reduction in revenue from Q1 FY20. It is still unclear how this current fiscal year will be affected by the restrictions in place from COVID-19.

Expenses

Fuel and Oil costs increased by much less as compared to last year - only by 300m. The major reasons were higher hedged fuel prices and an increase in flight hours. Depreciation increased by 100m approximately in absolute terms and can be attributed to higher capitalized maintenance and the impact of IFRS 16 (€59m) which was adopted from April 2019. Aircraft rentals decreased to 40m which had previously remained stable at around 80m. This is seen as a consequence of holding leases with a duration of less than 12 months for which the company availed itself of practical expeditions on adoption of IFRS 16 in April 2019.

Finance expenses increased by 420 million to 480 million, recording a big increase primarily due to an increase in gross debt by €567m to €4211m due to a new €750m low cost syndicated bank facility and the impact of IFRS 16 (€246m), offset by debt repayments and lease liability payments.
Effective tax rate for fiscal year 2020 was 3.2%, as compared to an effective tax rate of 6.7% previously, reflecting the recognition of a deferred tax asset in respect of property, plant and equipment and net operating loss incurred in other jurisdictions.

Ratios	2017	2018	2019	2020
Gross Profit Margin	59.31%	59.37%	53.50%	55.29%
Net Profit Margin	21.25%	18.62%	10.28%	3.49%
Return On Equity	33.56%	29.34%	15.56%	3.97%

While Gross Profit margin has remained in the same range, major changes in the shares of revenues being converted to operating profits is mainly due to changes in Fuel and Oil costs, among operating costs.
The net profit margin has been decreasing over the years, reflecting an increase in their finance and other costs and subsequently a decreasing proportion of their revenue from sales being translated into profit as a percentage.
Return on Equity (ROE) measures how much profit Ryanair generates with the money shareholders have invested. Positive ROE implies that assets exceed liabilities, and Ryanair's ROE has decreased 2017 onwards, seeing the biggest decline in the year ending 30th June 2020.

Balance Sheet

Ryanair has a BBB rating from both Fitch Ratings and S&P. In the last quarter till 30th June 2020, Cash increased by €128 million. This has happened due to its focus on preserving cash, in pursuit of which it also plans to complete the sale of 7 of its oldest B373s this winter.

Between FY19-20, Ryanair saw an increase in Current assets mainly due to an increase in cash and cash equivalents by approximately €900 Million. Cash generated from operations has been the principal source of cash requirements, supplemented primarily by general corporate purposes debt capital market issues. Further, as a cash flow hedge to hedge jet fuel, capital expenditure and maintenance contracts in US dollars, Ryanair keeps some foreign currency exchange contracts. This strength of Ryanair's cash flows allows the group to lease aircrafts at attractive rates. The company's current aircraft purchase program is ongoing till March 31, 2024 and the cash projections meet the requirements for the same.

Shareholders' Equity decreased by €248.2 M in the quarter due to a net loss of €185.1 M and IFRS hedge accounting treatment for derivatives of €69.9M. Total liabilities increased by 22% in FY20. Major increase was seen in the derivative financial instruments. Ryanair uses various derivative financial instruments, including cross currency swaps, interest rate swaps. These derivative financial instruments are generally held to maturity and are not actively traded. These instruments help manage commodity risk, interest rate risks, and currency exposures.

The Debt to Equity Ratio measures a company's financial leverage, displaying a breakdown of how a company is financing operations through debt and equity. Ryanair's Debt to Equity ratio has remained below 1 from 2018-2020. It is competitors such as Wizz Air saw an increase in the Debt to Equity Ratio to above 1 during FY19-20. Lower leverage ratios indicate lower risk, and Ryanair's board periodically reviews the proportion of debt and equity. The airlines has been able to generate sufficient revenue from operations to meet its non-aircraft acquisition related working capital needs. We believe that a low/moderate debt to equity ratio helps mitigate against risks and unforeseen events, as well as provide more market confidence.

Ryanair's Current ratio has been falling since 2018 while some of its other competitors like Wizz Air have managed to maintain strong current ratios above 1. Liquidity concerns have been heightened in light of Covid-19. There has been an increase in demand for refunds and/or waivers. For Ryanair, if liquidity is materially diminished, it may not be able to pay aircraft leases or debts timely or fail to meet its contractual obligations. While liquidity has been adversely impacted, it has become more difficult for airline companies specifically to raise more capital.

Outlook

Revenues

The revenue growth for Ryanair in the near term, i.e. FY21, will remain in a significant negative territory, especially on the back of a potential 'Black Winter' with increasing COVID-19 cases and regional lockdowns/circuit breakers, but we expect this to normalise after FY22 where we would encounter superficially high growth in revenue, for both ancillary and scheduled, due to the significantly negative figures projected in the near term.

The base case for Ryanair will likely be one of flat year-on-year growth, with little deviation in its growth path over the next five-year time horizon. The low-cost carrier industry is the least likely, at the margin, to be significantly affected by a reduction in demand compared to the overall airline industry, especially given that the value of the total travel package is drastically cheaper than premium long haul-travel, which may play a crucial role in a world where household incomes have taken an exogenous negative shock and continue to do so. Factors positively affecting Ryanair's revenue growth is the potential likelihood of a COVID-19 vaccine in 2021. European peripheral countries adversely impacted by the loss of tourism, i.e. Portugal and Spain, will be more accommodative to airlines such as Ryanair which will reduce the cost of airport and handling charges. One may also argue that as regardless of whether a vaccine is discovered and mass manufactured, public perception of COVID is dramatically changing and the likelihood of a shutdown of air travel is highly unlikely without significant bailouts or public outcry. These are some factors positively affecting Ryanair.

However, one should also consider some negative factors which may impact both scheduled and ancillary revenue. For example, marketing and distribution costs will likely rise especially as the airline industry will be inclined to raise awareness of safe travel, as well as route charge costs may increase given the recent tilt in Brexit negotiations if trade talks break down. Furthermore, Ryanair's business model is sensitive to seasonal travel to European peripheries, and in realistic case where a vaccine is discovered, but cannot be widely distributed, then travel to these peripheries over the summer period may be impacted further which would further impact FY21 revenues.

Expenses

Ryanair claims to have the lowest operating costs among any other European scheduled passenger airline group. While Ryanair has strategically hedged against the rise in some operating costs, Ryanair's costs are sensitive to the Covid cases in Europe in the near future.

The major proportion of costs, made by Oil and fuel costs, are directly related to the number of flight hours. The increase in these fuel and oil costs over 2019-20 were much lower than in 2018-19, primarily due to decrease in flight hours and hedging of fuel prices. As an impact of IFRS 16, Depreciation increased in absolute terms and is expected to stay the same in the near future - FY21. Aircraft rental costs have decreased to €40 million from €80 million and we expect it would stay the same in the near future, perhaps decline to €35 million if there is a decrease of air travel within Europe.

In the scenario where the air travel improves as lockdowns ease and Covid cases decrease within Europe, we can expect the air travel and oil and fuel costs to go up, although not directly proportional to the number of cases because of the hedges in place by Ryanair. Air rental costs are also likely to go up if air traffic improves.

In the negative scenario where air travel remains low or falls further even as cases worsen, the fuel cost would decline, and air rental costs would decrease marginally. However, the overall costs would be higher in proportion with the revenues such that the profits decline going further in this negative scenario. Overall, for the near future i.e. until mid-2021, we expect the expenses to remain stable albeit increasing slightly due to tax expense increase.

Valuations

Comparable Companies Analysis ('Trading Comps')

Our comparables consist of Air France, EasyJet, and Wizz Air. We have carefully chosen the competitors with a criteria of serving European Customers and being a low cost carrier airline. The analysis is done at a time where the airline industry is still suffering the impact of Covid-19. Thus, although the metrics are good for comparison with each other, they should be looked at as an indicator of competitor's future performance with greater scrutiny.

Comparable Companies	Share Price	Equity Value	Enterprise Value	EV/EBITDA Multiple	P/E Ratio
Air France	€ 2.91	1,243.39	10,470.39	2.69x	4.61x
Wizz Air	€ 40.22	3,435.85	3,985.05	7.37x	12.22x
Easy Jet	£4.82	2,201.54	2,133.54	7.87x	6.79x
			Mean	**5.98x**	**7.87x**
			Median	**7.37x**	**6.79x**

We have made use of the EV/EBITDA multiple, where EV is the result of net debt deducted from market capitalization. We then take the ratio of EV and EBITDA, both of which are obtained from the comps' financial statements. Here, upon taking the average for Air France, Wizz Air and EasyJet, 5.98x was obtained as the multiple. We calculate Ryanair's implied enterprise value by multiplying this multiple with Ryanair's EBITDA.

As shown in the calculation, we then account for debt and capital lease to come up to Ryanair's Equity Value. Upon dividing this by the number of shares outstanding, we get Ryanair's implied share price to be €5.60.

EV/EBITDA Multiple	5.98x
Ryanair LTM EBITDA	1,354.70
Implied Enterprise Value	**8,098.06**
Plus: Cash and Cash Equivalents	2840.90
Less: Capital Lease	(252.70)
Less: Debt	(4,586.60)
Implied Ryanair Equity Value	**6,099.66**
Total Shares Outstanding	1,089,181,737
Implied Ryanair Share Price	**€ 5.60**

Discounted Cash flow Analysis ('DCF Analysis')

The DCF valuation method is predicated on deriving the Present Value (PV) of future Free Cash Flows (FCF), discounted at an appropriate WACC rate. The outlook section helped derive our projections for forecasting the cash flows used in our DCF model. The calculation of the WACC rate and a more detailed breakdown of the DCF analysis process is provided in the subsequent sections below.

Weighted Average Cost of Capital (WACC) Calculation

WACC is the cost of capital to the firm, indicating the rate at which the company pays its security holders. In order to calculate the return on equity for shareholders the Capital Asset Pricing Model (CAPM) is used to estimate an expected return. The risk-free rate represents the 10-year UK Treasury Bond yield, and the figure used is a 3-year average. The market risk premium is the difference between the returns on the market (FTSE100) and the risk-free rate. The Beta is a measure of Ryanair's volatility in relation to the market, and as the figure is slightly above 1, Ryanair is considered to be slightly more volatile than the market. The cost of debt is calculated by using the interest incurred/total debt. There are tax deductions available on interest, which means the cost of debt is reduced due to the tax shield. In order to calculate the WACC, the two figures of Cost of Equity and Cost of Debt are apportioned in relation to the breakdown of the total capital. The table below shows how the WACC was calculated in the case of Ryanair.

Cost of Debt		
Interest Expense (mm)	€	72.90
ST Debt (Neglible, mm)		
LT Debt (m)	€	3,583.00
Income Tax Expense	€	21.60
Income before Tax	€	670.30
Cost of Debt (%)		2.03%
Effective Tax Rate (%)		3.22%
Cost of Debt After Tax		**1.97%**
Cost of Equity		
Cost of Equity (%)		**6.54%**
Weight of Debt and Equity		
Total Debt (mm)	€	3,583.00
Market Cap (mm)	€	13,630.00
Total	€	17,213.00
Weight of Debt		**20.82%**
Weight of Equity		**79.18%**
WACC		**5.59%**

Free Cash Flow (FCF) Calculations & Projections

From the forecasted revenues (discussed in the outlook section), we deduct the projected cost of revenues and other expenses, to arrive at the Earnings Before Interest and Tax (EBIT). Thereafter, Net Operating Profit After Tax (NOPAT) is calculated by EBIT * (1 – t), where t is the marginal tax rate and is 3.2% for Ryanair. Since it is cash flow we are interested in, rather than income, we need to make a few adjustments for non-cash items, such as Depreciation & Amortization, Changes in Working Capital, Stock-based compensation. Additionally, Capex must be deducted here since it is a cash expense but not recorded as an expense on the Income Statement. Through all these adjustments, we obtain the firm's future FCFs, which must now be discounted using the WACC rate of 5.59%.

The Terminal Value can be calculated in two different methods. The perpetuity method assumes that Ryanair will operate and grow at a certain rate, indefinitely. To account for this in our valuations, we set a Terminal Growth rate, which is set between the historical inflation rate and average GDP growth rate, and consequently we decided on 1.75%. The PV of all future FCFs beyond the projection period is calculated as the Terminal Value (TV) and this accounts for the majority of the company's valuation.

The Exit multiple approach uses an EBITDA multiple which has been obtained from our comps calculations. The multiple is then multiplied by our projected EBITDA in 2025. The future value is then discounted by a factor equal to the number of years.

The relevant calculations and adjustments are provided in the table below.

Unlevered Free Cash Flows	0 2020A	Projection Period 1 2021E	2 2022E	3 2023E	4 2024E	5 2025E
Operating Income/ EBIT	**1,127.40**	**989.36**	**1,296.23**	**1,469.27**	**1,668.29**	**1,898.34**
Tax on EBIT	36.08	31.66	41.48	47.02	53.39	60.75
Tax rate	3.20%					
Net Operating Profit After Tax (NOPAT)	**1,091.32**	**957.70**	**1,254.75**	**1,422.26**	**1,614.90**	**1,837.59**
Depreciation & Amortization	748.70	442.22	442.57	447.42	454.65	464.57
Stock based compensation	7.00	-	-	-	-	-
Changes in NWC	5.60	444.44	(160.19)	(93.85)	(109.19)	(127.40)
CAPEX (enter as -)	(725.80)	(449.75)	(546.27)	(602.16)	(666.95)	(742.34)
Unlevered FCF	**1,126.82**	**1,394.61**	**990.86**	**1,173.67**	**1,293.41**	**1,432.42**
Year Proportion	0.439	1	1	1	1	1
FCF to firm	494.55	1394.61	990.86	1173.67	1293.41	1432.42
PV of FCF	482.88	1320.78	888.73	996.96	1040.51	1091.34
Sum of all PV of FCF	**5821.19**					

The summation of all discounted future FCFs gives us Ryanair's Enterprise Value (EV). As mentioned under the comparables section, deducting Net Debt from EV, gives us Equity Value and dividing this by the number of shares outstanding will provide us the with implied share price for both methods. We then get the average DCF share price of €21.93.

Valuation	Perpetuity	EBITDA
Enterprise value	**34,739**	**16,583**
Net debt	1,746	1,746
Equity value	**32,993**	**14,837**
Shares outstanding	1,089,181,737	1,089,181,737
Equity value per share	**€30.29**	**€13.62**

Discussion, Sensitivity Analysis & Recommendation

We have derived our final implied share price by combining the results from the DCF analysis and the Trading Comps, equally weighted. Both methods, as mentioned in the previous Netflix report, have limitations, and must be looked at with precaution. The DCF analysis is based on Free Cash Flows (FCF), which is derived after accounting for Capex, which creates an issue where the more investments you carry out, the less FCF you will have. A negative FCF is not necessarily bad since it indicates high Capex which is good for growth (i.e. Tech and Start-up firms), although other reasons may exist.

Similarly, relative valuations have their own issues. For one, it assumes that the comparable companies are fairly priced by the market, however then, why is then the target firm also not considered to be fairly priced? Companies also tend to have different accounting methods, measures of profitability and are not always exactly the same, as we see in the case of Netflix, which although has some direct competitors, others are not and do not emphasise ancillary revenue to such an extent.

Based on all our calculations, the intrinsic share price arrived at is €13.78 (breakdown is shown in the table above). This represents an upside of 15%, but, given the recent headwinds surrounding further imminent COVID-19 lockdowns and the uncertainty that this brings, among other reasons mentioned in this report, we will recommend a HOLD rating for Ryanair.

Implied Share Price		
Comps	€ 5.60	50%
DCF	€ 21.96	50%
Final Share Price	**€**	**13.78**

Equity Value Per Share Sensitivity (Perpituity Growth)						
		WACC				
	€ 30.29	5.49%	5.54%	5.59%	5.64%	5.69%
Perpituity Growth	1.35%	28.401	28.043	27.692	27.350	27.016
	1.55%	29.703	29.311	28.928	28.554	28.189
	1.75%	31.145	30.713	30.292	29.881	29.482
	1.95%	32.749	32.271	31.805	31.353	30.912
	2.15%	34.545	34.013	33.495	32.993	32.504

Equity Value Per Share Sensitivity (EBITDA Multiple)						
		WACC				
	€ 13.62	5.49%	5.54%	5.59%	5.64%	5.69%
EBITDA Multiple	4.98x	12.026	11.999	11.973	11.947	11.920
	5.48x	12.856	12.828	12.799	12.771	12.743
	5.98x	13.687	13.656	13.626	13.596	13.565
	6.48x	14.517	14.485	14.452	14.420	14.388
	6.98x	15.347	15.313	15.279	15.244	15.210