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Travel Sector Review 2021

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Summary

Travel sector stocks were among the worst affected by Covid-19. While many other FTSE stocks have shown a smart bounce back from the market crash last year, especially as vaccines were developed, some travel stocks are still struggling.

From airlines (International Consolidated Airlines and easyJet) to leisure travel stocks (Carnival and TUI) are still way below their pre-crash levels. But that could change soon.

As lockdowns are eased and the fear of the pandemic subsides, their demand will increase in the short-term. But over the longer-run too, they could be at the cusp of high growth. The IMF has just upped its global growth forecasts and with huge stimuli in place for the world's two biggest economies - the USA and China - a sustained growth boom could be seen in the next few years.

Yet, there are risks too. Travel companies have run up huge debts and there is always a possibility that Covid-19 variants send the world back into lockdown and low growth or worse, recession.

This report profiles how Covid-19 has already impacted 7 key travel stocks and how they could fare from here. Stocks like easyJet show promise because they are still trading at pre-pandemic levels, while demand for the company's services is on the rise. Also, InterContinental Hotels Group is less affected than others, which puts it in a better position to return to breakeven than others.

Company Profiles

Ryanair (RYA)

- **About:** Ireland based Ryanair operates ultra-low cost flights between Ireland, the UK, Continental Europe, Morocco and Israel.
- **Financials:** Before the pandemic, the company's revenues were growing steadily. It was also profit making, though it was getting squeezed, as evident from its declining profit levels for the full-year ending March 31, 2019 and March 31, 2020.
- **Covid-19 impact:** For the 9 months ending December 31, 2020, however, Ryanair's revenues had declined by 79% and it ran up a loss, as would be expected.
- **Share price trends:** Nevertheless, it has shown one of the sharpest recoveries among travel stocks. Its share price is now at multi-year highs, far higher than it was in the immediate pre-crash period.
- **Notable developments:** Ryanair intends to increase the number of flights to 80% of pre-pandemic levels by July, which could be a further positive for the share. It will also start flying on 26 new routes and is planning to extend its services to Germany as well.

International Consolidated Airlines Group (IAG)

- **About:** British Airways owner, IAG operates across 268 destinations and owns 573 aircrafts. It runs both full-service and budget airlines. The London headquartered company combines airlines across the UK, Spain and Ireland.
- **Financials:** IAG saw steadily rising revenues in the years preceding the pandemic. Its profits were less steady, but continuous.
- **Covid-19 impact:** For the full-year 2020, however, its revenue fell to nearly one-fourth its earlier level. It also flipped into a huge loss of around £6bn.
- **Share price trends:** The IAG share price has broadly been on the path to recovery since the vaccine discoveries took place in early November last year. However, it is still at half the levels seen pre-pandemic.
- **Notable developments:** At present it is flying at 20% capacity, and does not expect a meaningful increase before mid-May, when UK travel can resume. However, its airlines can increase their capacity to over 70% quickly, if demand does increase. To ensure that its finances are in place, if it does not, it has just raised $1.8bn.

InterContinental Hotels Group (IHG)

- **About:** The UK based FTSE 100 hotels group owns brands like Crowne Plaza and Holiday Inn. It operates around 6,000 hotels and has another 1,999 in the pipeline. Its pipeline focuses most on the Americas, followed by China and then EMEA.
- **Financials:** In the years just before the pandemic, IHG’s revenues were steadily increasing. In 2017, it crossed £4bn. It also earned over £500mn in net profits that year, though the number fell in the subsequent years.
- **Covid-19 impact:** For the full-year 2020, it turned a net loss, though at £0.2mn this is the smallest among all companies covered in this report and that have reported financials for much or all of 2020. Its revenue halved as well.
- **Share price trends:** IHG’s share price has bounced back well, and is now at December, 2019 levels. On the whole, its share price trend line is upwards sloping from mid-2020 onwards.
- **Notable developments:** Even though it expects a pickup in demand in the second-half of 2021, IHG does not expect to go back to pre-pandemic levels for the next several years. However, as more people get vaccinated and lockdowns are lifted, it expects budget leisure travel to grow for now and it will create packages that will tap into this demand.

easyJet (EZJ)

- **About:** Low-cost airline, easyJet, operates across 33 countries across Europe, Middle-East and North Africa. The London headquartered airline provides services across 1,000 routes.
- **Financials:** Like other airlines, in the pre-pandemic years, easyJet reported increasing revenues and largely steady profit levels.
- **Covid-19 impact:** However, its financials have taken a big hit in 2020. For the full-year ending September 29, 2020, its revenues halved from the year before. It also reported an over £1bn loss.
- **Share price trends:** The easyJet share price has recovered to a great extent from the pandemic. At the current price of £10, it is closer to its pre-market crash highs than the lows of around £4.5 it touched during the crash.
- **Notable developments:** A turnaround can happen for easyJet in the near future, though. Its flight bookings increased by 337% after the UK government announced the phased end to the lockdown. More recently, it said that new routes from Birmingham to continental Europe will be operated from the end of June.

Wizz Air (WIZZ)

- **About:** The Hungary registered company, operates across 380 routes and 112 destinations. It has a focus on Central and Eastern Europe, where it intends to expand further. It runs a fleet of 130 aircrafts across 38 countries.
- **Financials:** Its pre-pandemic revenues showed continuous growth for a number of years and its profits rose too, save in 2019 when they took a big dip. However, for the year ending March 31, 2020, it reported £0.2bn in net profit, an increase from 2018.
- **Covid-19 impact:** By the end of 2020, things looked very different for Wizz Air as it reported a 76% fall in revenue for the three months ending December 31, 2020. It also reported around £100mn in losses as the number of passengers it carried fell by 77%.
- **Share price trends:** Nevertheless, investors are positive on the stock. Upturn in its fortunes started in November 2020 on vaccine discoveries. The Wizz Air share price reached all time highs in February this year.
- **Notable developments:** Share price continues to remain elevated despite two disappointing developments. One, its largest shareholder Indigo Partners recently sold off almost half its stake in the company. It now owns 8.5% of it. Two, so far it continues to see weak passenger demand, with a 72.6% fall in numbers in March compared to last year.

TUI (TUI)

- **About:** The world's largest leisure, travel and tourism company, TUI is based in Germany. It runs 1,600 travel agencies, 5 airlines, over 400 hotels and 17 cruise liners.
- **Financials:** TUI was in a strong financial position before the pandemic, though its revenues were largely flat and its profits were declining.
- **Covid-19 impact:** It has reported the third biggest loss of £2.7bn for the year ending September 29, 2020 among these seven travel stocks, smaller than the loss of only Carnival and IAG. Its revenues fell by 58% from the year before.
- **Share price trends:** TUI's share price has now touched pre-pandemic levels. But it is worth underlining that its share price was falling even earlier, from late 2019 in fact, as its profits disappointed.
- **Notable developments:** With progress on vaccination slow in mainland Europe, TUI has scaled back its capacity levels from 80% of 2019 levels for July to 75% now. It does however expect enough cash flow this summer to make its debt plus interest costs manageable.

Carnival (CCL)

- **About:** The UK based cruise provider, Carnival operates throughout the world, including North America, Australia, Europe and Asia.
- **Financials:** It showed steady growth in revenues in the years prior to the pandemic, while its net profits were steady.
- **Covid-19 impact:** For the year ending November 30, 2020 however, it reported the largest loss of £7.4bn as the pandemic shut down leisure travel. Its revenues were affected significantly as well, falling to one-fourth their levels in 2019.
- **Share price trends:** Carnival's share price has inched up overtime and is now back to its pre-crash levels. However, the company's big share price crash pre-dates the stock market crash in the UK in March last year. One of its liners led to the spread of coronavirus early on, and before mid-February last year it had suspended Asian operations. Even before that though, the share price had been on the downtrend since early 2017.
- **Notable developments:** The company expects to show full-recovery only in two years' time. It also believes that it maybe sailing its full-fleet by the end of the year, but the fleet itself will be smaller than before.

What is next for travel stocks?

The environment that travel stocks operate in remains quite complex today. There are still a number of risks to them but the positives are also on the rise.

Risks to travel stocks

1. **Pandemic returns:** With vaccinations underway, the pandemic is receding. However, there are still at least three variants around, first reported in South Africa, the UK and Japan. And not all vaccines are equally effective against variants. This means that if there is enough risk of their spreading fast, then we can potentially be under lockdown again. This of course is a big challenge for travel companies,

2. **Increased debt levels:** Because of near business closures last year, travel companies have raised huge debts. According to data provider Dealogic, airlines have raised $16.6bn worth of debt in just 2021 and $42.6bn in all of 2020. IAG and easyJet raised bonds or around £1bn each. While investors so far have been willing to fund the companies, if the world to go back into lockdown funding may not be that easily available in the future.

3. **Slow return to growth:** Even after all business operations resume, the return of travel stocks depends on the demand. There may be some permanent decline in business travel as the pandemic has forced the adoption of digital communication as opposed to face-to-face meetings. Further, travel demand can pick up in the short-run as people go on vacations after over a year of Covid-19 led restriction. However, it needs to be sustained overtime to meaningfully impact travel stocks. If growth does not come back post-pandemic because businesses are impacted beyond repair, spending cuts on travel and tourism could be the first thing on consumers' minds.

Opportunities for Travel stocks

1. **Demand boom:** At the other end of the demand spectrum, is the possibility of a demand boom as the world economy returns to fast growth. The International Monetary Fund has just upped its forecasts. It now expects 6% growth in 2021, up from its earlier expectation of 5.2% increase. It would be somewhat slower but still strong 4.4% in 2022. This bodes well for consumer demand in any case. Additionally, data from the Office of National Statistics in the UK shows that the proportion of UK's household savings to its income is at record levels. This too means that there is greater likelihood of spending as lockdowns ease. Among other things, this is good for travel companies.Further, this demand may be sustained considering the ongoing policy support. In the US, a $1.9 trillion stimulus package can find its way into sustainable increasing income levels. Similarly, the Chinese government's public spending has already driven up demand for commodities last year. Some forecasters, including investment banks like JP Morgan and Goldman Sachs, have also said that there could be a long-term increase in these prices. This in turn could have spillover effects on other sectors, including travel.

2. **Cost efficiencies:** Because of the difficulties of 2020, many travel companies have had to resort to cost cuts. If continued these can result in cost efficiencies overtime. For example, IHG plans to cut salaries of both board members and executives and is relaxing brand standards. Other cost cutting measures like slowing down capital expenditure and renovation spends, however, maybe more temporary. Similarly, IAG has had to let go of 12,000 employees who were part of British Airways. It has managed to cut its operating costs by 30% as a result.

Conclusion

With the future of travel stocks is still uncertain, it is evident that both risks and opportunities are present. All the stocks mentioned here have strong credentials, which means that there is merit to them.

But three criteria can help in deciding their share price potential:

Extent of pandemic damage - the lesser the damage to revenues, the more likely it maybe able to recover in the future.

Cost management - Companies most likely to manage their costs wel at this time, including efficiency enhancing cost cuts and debt management, can come out ahead at the pandemic scales back.

(iii) Share price increase - If the share price is well below its pre-pandemic levels, then chances of increase are higher than if it is already at all time highs while still running losses.

Among airlines, easyJet looks best placed to take off from here, especially going by its high demand and still soft share price. Among other travel stocks, the InterContinental Hotels Group looks better among others for its cost management and the relatively small hit to its income. Its share price has run up quite a bit, though.

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