Brief Overview:

easyJet are a low-cost European travel company operating in the airline industry. Utilising a fleet of 308 aircrafts provides travellers with over 900 routes across 34 countries. Typically known as a budget airline, the company has managed to efficiently cut costs, whilst simultaneously providing excellent customer service.

In addition to the point-to-point airline operations easyJet have also diversified into providing holiday packages. By bundling their airline travel with other holiday services (accommodation, car hire) easyJet have encouraged customers to spend more on their website, rather than going for the same services on third-party websites.

Analyst ratings:

The current analyst consensus is that the company is overweight, suggesting that the company stock price will improve in the future. Of the 20 analysts covering this company, 16 recommend a Buy or overweight, 2 recommend a hold whilst only 2 analysts recommend a Sell. *(WSJ Market Data)*

The average analyst price target is 573.47p, with a low of 310p and a high of 805p. From current levels, the analyst average suggests the company is undervalued by 60%, from current levels.

Investment thesis:

EasyJet accrued 3,816 (£million) in passenger revenue for the financial year of 2022 and this makes up the 66% of the company's total revenue. The company maintained their focus on expanding their network to major tourist destinations, including winning 18 slots at Lisbon Airport.

Just under a third of total revenue is made up of ancillary sales, typically involving extra baggage and in-flight; entertainment, food and internet. Netting 1,585 (£million) EasyJet has enhanced their ancillary services and have improved their revenue by 59% since 2019.

EasyJet holidays, is the company's fastest growing and highest margin aspect of their business model and accrued for 6% of the total revenue. After being newly launched in 2019, the project increased their profits by 400% (£8m to £38m) and is on track to meet £100m profits in the medium-term.

The company is showing positive signs to a return to normal post-Covid, with a 242% increase in passengers since 2021, from 20.4 million passengers to 69.7 million. This is still a 27% reduction since 2019, but looks to be improving as the fears of Covid and business travels return.

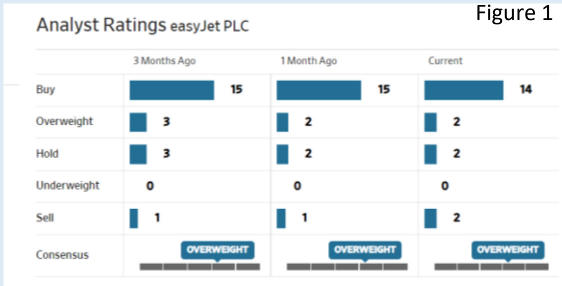

Figure 1

Source: WSJ Markets

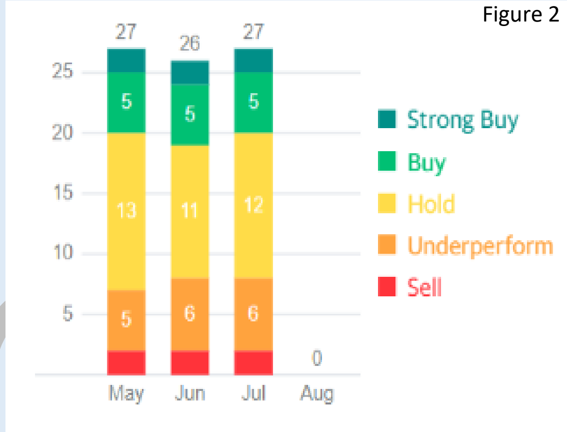

Figure 2

Source: Yahoo Finance

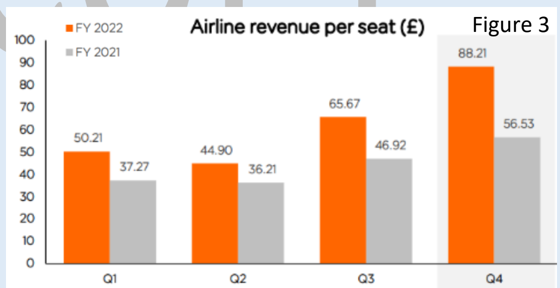

Figure 3

Source: EasyJet Results Centre

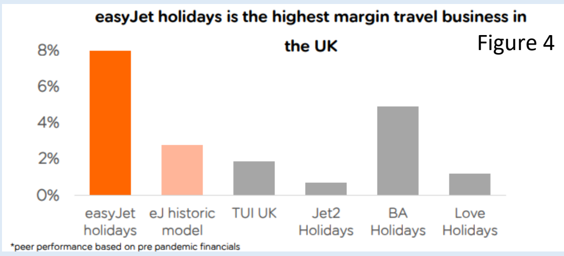

Figure 4

Source: EasyJet Results Centre

Recent developments:

As the company attempts to return to full capacity, they have faced many challenges, which has diminished investor confidence, resulting in a reduction in the share price.

The CEO, Johan Lundgren, attributed the company's staff shortages to Brexit. The company rejected 8000 applicants from the EU, due to more stringent policies, who now do not have the right to work in the UK. *(The Independent)*

Valuation and Earnings analysis:

The Price-Earnings (PE) ratio for easyJet, Pegasus Airline and Ryan Air is 11.99, 13.4 and 15.77 respectively. Of the three direct competitors, easyJet has a below average PE ratio implying the company is currently undervalued with respect to its competitors.

EasyJet had a reported loss of 208 (£million) in 2022, down significantly from 2021 which reported a loss of 1,036 (£million). It is clear that as Covid-19 restrictions begin to be relieved and consumer confidence returns, revenue will continue to increase. RyanAir also reported a similar improvement in their losses, from 1,015 (€million) to 355 (€million).

Risk:

The airline industry is capital intensive, a rise in debt to finance everyday operations can be inherent and unavoidable, yet a recent reduction in the ratio seems to depict a positive outlook to normal business operations.

Throughout 2015 to 2019 the company averaged a debt-equity (DE) ratio of 0.32. The company maintained a steady and slow increase in debt and along with a volatile, but comparatively higher equity levels, easyJet maintained a lower DE ratio.

Due to the pandemic, borrowing increased by approximately 150% and along with a large reduction in equity, the DE ratio rose significantly to 1.91 by late 2021. This ratio has slowly improved due to an improvement of equity and a slight reduction in debt. RyanAir, a competitor budget airliner operating within Europe, also saw their DE ratio increase, by 72%, since 2019. However, the company throughout the past decade has maintained a DE ratio of 1, financing the majority of their operations with debt.

Overall, easyJet achieved a credit rating of *BBB-* and this reaffirms that the company can adequately meet its financial commitments.

Fair valuation:

The discounted cash flow (DCF) valuation method is a very popular method in assessing the fair value of a company. Using an estimated earnings per share (EPS) of 34.55p for 2023, the fair value share price is 497.91p. This suggests the company is currently undervalued by approximately 26.7%.

The estimated EPS value is calculated using the average growth of previous EPS, from the past two years and so there is a possibility that the company experiences higher than expected earnings, as travel demand rises further. With easyJet predicting a return to normal, a best case DCF is calculated, yielding a share price of 1,278.29p.

Finally, the worst case scenario is that the company continues to experience no growth and this can be attributed to countries demanding vaccine passports, higher jet fuel prices and simply a lack of travel confidence. Although unlikely, the DCF calculation results in a share price of 248.59p and this suggests that the current stock price is overvalued by 58.1%.

Industry analysis:

The airline industry was severely impacted on both the demand and supply side, due to the pandemic. Throughout the past decade the industry experienced significant passenger growth, however, the pandemic resulted in a 75% reduction in passengers boarded from 4.1 billion to 1.8 billion. By the end of 2022 the industry saw a revival of passengers and a return of confidence for travellers.

The Russia-Ukraine war has created some fluctuations with jet fuel prices and with the future political space looking uncertain between the two countries, it could have some effects on the airline industry. On the one hand, those tickets sold when jet fuel prices are low, may result in a reduction in profit margins. However, on a long-term horizon, airline companies are able to levy the additional costs on their customers without severely impacting their capacity. Furthermore, the majority of airliners hedge the price of jet fuel, easyJet being amongst them. This means that irrespective of volatile fuel prices, the company will continue to make money through swaps and option contracts. In-fact European airlines netted a total €5 billion, as a result of the Russia-Ukraine war, with easyJet making a €824 million gain on fuel derivatives. *(Eurofinance)*

Management:

easyJet made a complete restructure to their directors board in the summer of 2022, letting go of Nick Leeder, a former Google executive, with Julie Southern and Andreas Bierwirth stepping down from their current roles.

Three additions to the company included; Harald Eisenächer, Detlef Trefzger and Ryanne Van der Eijk. Holding executive positions for Lufthansa, Kuehne + Nagel International AG and KLM respectively, the three appointees can help grow easyJet with their extensive knowledge in the airline and transportation industry.

Ryanne van der Eijk
Independent Non-Executive Director

Harald Eisenächer
Independent Non-Executive Director

Detlef Trefzger
Independent Non-Executive Director

Appendix

Financial Performance:

Figure 5	FY22 £ m	FY21 £ m	Change[1]
Passenger revenue	3,816	1,000	282%
Ancillary revenue	1,585	424	274%
Holidays revenue[2]	368	34	982%
Group revenue	**5,769**	**1,458**	**296%**
Headline costs:			
Airline EBITDAR Costs ex fuel	(3,596)	(1,595)	(125%)
Fuel	(1,279)	(371)	(245%)
Holidays EBITDAR costs[2]	(325)	(43)	(656%)
Group headline EBITDAR	**569**	**(551)**	**203%**
Airline depreciation, amortisation & dry leasing costs	(562)	(482)	(17%)
Holidays depreciation & amortisation[2]	(4)	(3)	(33%)
Group headline EBIT	**3**	**(1,036)**	**100%**
Group interest and other finance charges and income	(117)	(110)	(6%)
Balance sheet revaluations	(64)	10	(740%)
Group headline loss before tax	**(178)**	**(1,136)**	**84%**
Non-headline items	(30)	100	(130%)
Group loss before tax	**(208)**	**(1,036)**	**80%**

Source: EasyJet Results Centre

Balance Sheet:

£m Figure 6	30 September 2022	30 September 2021
Goodwill and other intangible assets	582	582
Property, plant and equipment	4,629	4,735
Derivative financial instruments	442	203
Equity Investments	31	30
Other assets (excluding cash and money market deposits)	1,022	619
Unearned revenue	(1,043)	(846)
Trade and other payables	(1,685)	(1,128)
Other liabilities (excluding debt)	(775)	(646)
Capital employed	3,203	3,549
Cash and money market deposits	3,640	3,536
Debt (excluding lease liabilities)	(3,197)	(3,367)
Lease Liabilities	(1,113)	(1,079)
Net debt	(670)	(910)
Net assets	**2,533**	**2,639**

Source: EasyJet Results Centre

Bibliography

1. https://www.wsj.com/market-data/quotes/UK/EZJ/research-ratings *(WSJ Market Data)*

2. https://www.independent.co.uk/travel/news-and-advice/brexit-flight-cancelled-easyjet-staff-b2104884.html (*The Independent)*

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Notes:

Methodology for DCF calculation:

Due to the current EPS value being negative, it was necessary to calculate an estimated EPS value for the upcoming year. This value is calculated by taking the average growth from the previous year and applying the percentage growth onto the 2022 EPS.

2021: EPS = -166.9

2022: EPS = -19.6

2022 EPS percentage growth: 88.26%

The assumption is that all growth is from an EPS of 0 and there is exists a margin of safety of 20% on the calculated share price.

Worst case: easyJet experiences no additional growth from the previous year and so use the EPS growth of 88%. So EPS for 2023 is 17.25.

Base case: easyJet experiences an EPS growth of an average between the 2019 EPS and the 2022 EPS. easyJet has made estimates that the company will return to full capacity by 2023 and so taking an average between the "normal" EPS value in 2019 and the 2022 value provides an EPS of 34.55.

Best case: easyJet returns back to full capacity and therefore returns an EPS of 88.7.