ApexAfrica CAPITAL LTD
Part of AXYS Group

August 2018

Kenya Airways 1H18 Earnings Update
“Gradual climb to recovery”

Kenya Airways Plc (KQ) announced a 30.8% y/y improvement in 1H18 earnings to a loss before tax of KES 4.0B compared to KES 5.8B reported in the same period in FY17. The advancement in the bottom-line was attributed to a 6.6% y/y increase in passenger numbers to 2.3M and a 20.4% y/y decline in the airline’s overheads.

Top-line expansion steady

KQ’s total income rose 3.1% y/y to KES 52.2B in on the back of a 6.6% y/y increase in passenger numbers to KES 2.3M. Cabin factor improved by 280bps to 75.9% y/y. The national carrier launched three new destinations flying 3x and 4x weekly to Cape Town and Mauritius respectively. Bookings for the highly anticipated direct flights to the US have soared in the past few months to 900 bookings per week. The new routes coupled with strategic partnerships with other airlines worldwide are expected to bolster the topline expansion going forward.

Increase in fuel prices piles pressure on costs

Kenya Airway’s direct operating costs hiked 13.9% y/y to KES 36.9B attributable to increased pressure on global fuel prices which inflated KQ’s fuel costs by 16.0% y/y. Fuel price per barrel sky-rocketed 55.3% y/y to USD 74.4 with projections by IATA estimating a further 25.9% increase on FY17 prices to USD 84.0 per barrel. Total operating costs were up 3.7% y/y to KES 53.2B despite a 20.0% y/y decline in overhead costs to KES 9.7B combined with reduced fleet costs of 2.0% y/y to KES 6.6B. Consequently, the company posted a 40.0% y/y surge in its operating loss to KES1.0B.

Loss before tax improves 30.8% y/y to KES 4.0B

KQ’s bottom-line displayed an impressive resurgence improving 30.8% y/y to a 1H18 loss of KES 4.0B, mainly buoyed by a sharp decline in other operating costs which fell 41.4% y/y to KES 3.0B. The airline, which underwent a successful debt restructuring process in FY17, saw a significant decrease in its finance costs which is expected to cushion the bottom line going forward.

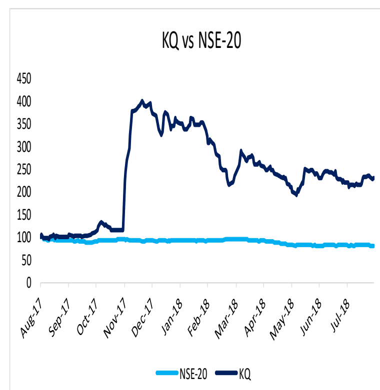
Future outlook

The national carrier is set to face stiffer competition going forward following the revival of regional airlines. Nonetheless, management is keen on implementing its strategic partnerships strategy aimed at increasing passenger traffic and further strengthening the topline. The recovering airline is also facing a financial viability hurdle ahead of its direct flights to the US. However, management is confident that Nairobi’s growing popularity as a regional hub will boost passenger numbers especially on the New York-Nairobi flight which may give the airline a competitive advantage over its peers. KQ is in ongoing talks with the government pursuant to implement a PPP model between KQ and KAA that will see consolidation of the two entities’ operations. If/when this plan materializes, KQ is set to unlock new revenue streams in running JKIA’s operations which is anticipated to uplift the airline’s financial position. The Board has also approved the implementation of fuel hedging strategies that will cushion the airline against fuel price volatility going forward. Hedging may be rolled out to other areas of the company’s operations such as currency exchange and interest

Bloomberg Ticker	KNAL KN
Reuters Ticker	KQNA.NR

Share Statistics	
Price	10.55
Market Cap (KES B)	59.5
Market Cap (USD M)	595
Year end	31-Dec
Float (%)	36.7
Foreign Ownership (%)	8.7
3-Month D. Avg Trading Val (USD)	10,494

Price Trend



Source: (Bloomberg)

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rates thereby minimizing the effect of market shocks associated with the volatility of these instruments. Finally, KQ has embarked on an intensive journey to revamp its customer experience. Effectively, the airline has introduced a new menu on all its flights, upgraded its lounge at the JKIA and is looking to roll out its own frequent flier program in addition to launching its newly redesigned uniform at the onset of the direct US flights. Though the recovery strategies put in place may revive the airline, the turnaround times of the strategies are poised to test the patience of investors.

Financials(KES M)		(9 months)		
Income statement	**1H17**	**FY17**	**1H18**	**y/y chng (%)**
Total income	50601	80799	52193	3.1
Total operating costs	(51,333)	(79,493)	(53,218)	3.7
Operating profit/ (loss)	**(732)**	**1,306**	**(1,025)**	40.0
Other costs	(5,099)	(7,275)	(2,990)	-41.4
Interest income	60	-	23	-61.7
Loss before tax	(5,771)	(5,969)	(3,992)	-30.8
Loss for the period	**(5,668)**	**(6,081)**	**(4,035)**	-28.8
Gain/(loss) on hedged exchange differences	(365)	1,250	1,074	-394.2
Total comprehensive loss for the period	(6,033)	(4,831)	(2,961)	-50.9
Basic loss per share	**(15.16)**	**(1.04)**	**(0.69)**	-95.4
Diluted loss per share	(15.16)	(0.81)	(0.54)	-96.4
Statement of financial position				
Non-current assets	118,214	118,214	113,149	-4.3
Current assets	21,892	21,892	21,386	-2.3
Total assets	**140,106**	**140,106**	**134,535**	-4.0
Non-current liabilities	87,635	87,635	84,816	-3.2
Current liabilities	52,001	52,001	53,615	3.1
Total equity and liabilities	140,106	140,106	134,535	-4.0
Net assets	**470**	**470**	**(3,896)**	-928.9
Statement of Cash flows				
Net cash from operating activities	2,121	6,661	345	-83.7
Net cash (used in)/generated in investing activities	2,152	(2,197)	3,438	59.8
(Decrease) in cash and cash equivalents	(1,084)	(2,830)	(392)	-63.8
Cash and cash equivalents at the end of the period	**8,777**	**6,356**	**5,964**	-32.0
Ratios				
Net margin (%)	(11.2)	(7.5)	(7.7)	
Operating margin (%)	(1.4)	1.6	(2.0)	

Source: Company Filings & ApexAfrica Research

Appendix

Investment ratings

- **Buy:** A total return is anticipated in excess of the market's long-term historic annual rate (approximately 10%). Total return expectations should be higher for stocks that possess greater risk.

- **Hold:** Hold the shares with neither a materially positive total return nor a materially negative total return anticipated.

- **Sell:** Stock should be sold as materially negative total return is anticipated.

Disclaimer

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