BCP Research: Copa Holdings S.A. (CPA) - 4Q20 Results, Positive - Anticipated Weakness Heading into 1Q21

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Summary: International Panama-based airline, Copa released positive 4Q20 results, with RPMs down 76% y/y at an improved LF of 75%. Revenues increased sequentially, driven by holiday demand, and adj. EBITDA remained negative, though improved q/q. Reported cash burn was -US$18 mm, a significant improvement from prior quarter's -US$109 mm cash burn. Cash increased to US$890 mm (111% LTM revenues) and net debt decreased to US$505 mm, while LTM net leverage expanded to 9.4x, reflecting weakened LTM adj. EBITDA. The company ended the quarter with US$1.3 bn in liquidity (157% LTM revenues).

Management anticipates weakness heading into 1Q21, guiding to an estimated -US$120-135 mm cash burn, with sequential revenue improvements outweighed by lagging capacity adjustments, working capital use, and delayed 4Q20 costs. Nevertheless, Copa appears equipped to weather the storm, with reported total current available liquidity of US$1.4 bn as of February 12, 2021 expected to further increase as new financing and credit lines are raised.

We remain 'neutral' on 169c CPA 4.5% 25s, as upside and downside cases appear roughly balanced amid limited spread between IVOL of the convert (42%) v. volatility of 100D (65%) and listed calls (52%) on the common. Meeting BBG consensus '23 adj. EBITDA estimates of ~US$810 mm (+13% v. FY19) implies 55% upside on the shares using past multiples (7.1x TEV/FY19 adj. EBITDA), and 38% upside on the bonds, compared to 47% downside to our estimated bond floor. Consensus estimates reflect margin expansion assumptions vs. pre pandemic levels.

			Amt Out (US$ MM)	Mid Price	Mid YTM	IVOL	Cheapness (par)	Delta (par)	Strike Price	CPA US Price
CPA	4.5%	4/15/2025	350	168.5	(8.78%)	41.81%	2.38%	88.73%	$51.66	$77.78

** Prices sourced from BBG as of February 12, 2021*

4Q20 Operating and Financial Results:

- Consolidated fleet totaled seventy-five (75) aircraft, a 26% reduction y/y v. FY19
  - Aircraft include seven (7) Boeing 737 MAX 9s and sixty-eight (68) Boeing 737-800s
  - In line with industry standards, the company has transitioned to power-by-the-hour operating leases
  - Five (5) of Copa's fourteen (14) previously sold (excl. from fleet count) Embraer 190s (E190) were delivered in the quarter
- Passenger traffic (RPMs) was 1,267 mm (-76% y/y, +2,123% q/q) and capacity (ASMs) was 1,684 mm (-73% y/y, +1,673% q/q), resulting in a load factor of 75% (-1,004 bps y/y, +1,524 bps q/q)
  - The company ended the quarter with service to 51 destinations, up 240% from 15 destinations in 3Q20
  - We note capacity recovered to 27% of 4Q19, expanding m/m from 15% of October '19, to 28% of November '19 and closing at 39% of December '19 ASMs

Copa Holdings S.A. (US$MM)	4Q20	3Q20	2Q20	1Q20	4Q19	y/y	q/q
RPMs (mm)	1,267	57	15	4,473	5,244	(76%)	2,123%
ASMs (mm)	1,684	95	31	5,491	6,149	(73%)	1,673%
Load Factor	75.2%	60.0%	48.4%	81.5%	85.3%	(1,004 bps)	1,524 bps

- Revenue was down 77% y/y but increased 390% q/q, as demand accelerated in line with increased holiday (VFR) and leisure travel
  - We note revenue was comprised primarily of passenger revenues (US$148 mm), including flown passenger revenue and unredeemed ticket revenue

- Adjusted EBITDA, while improved q/q, remained negative at -US$27 mm
- Management reported cash burn (excl. extraordinary expense) improvements, reaching -US$18 mm (US$0.2 mm / day) in 4Q20 v. -US$109 mm (US$1.2 mm / day) in the prior quarter, and driven primarily by top-line growth and working capital inflow, as a result of higher receivables
    - Management highlighted reintroduction of travel restrictions in the second half of Dec. '20 resulted in deterioration of cash burn improvements, as capacity changes lagged reductions in demand in the latter end of 4Q20
- Cash (cash and equivalents + ST investments) increased 3% q/q to US$890 mm (111% of LTM revenues)
- Liquidity (cash + A/R) increased 4% q/q to US$1,258 mm (157% of LTM revenues)
- Net debt decreased 19% q/q US$505 mm, reflecting a 3% increase in cash, alongside a 7% reduction q/q in loans and borrowings, and 5% reduction q/q in lease liabilities
- LTM net leverage jumped to 9.4x, reflective of three sequential quarters of operating losses, mitigated slightly by reduced net debt

Copa Holdings S.A. (US$MM)	4Q20	3Q20	2Q20	1Q20	4Q19	y/y	q/q
Revenue	**159**	**32**	**15**	**595**	**682**	**(77%)**	**390%**
EBIT	**(95)**	**(107)**	**(358)**	**99**	**18**	**-**	**(11%)**
Depreciation & Amortization	64	63	68	66	70	(9%)	2%
EBITDA	**(31)**	**(44)**	**(290)**	**165**	**88**	**-**	**(30%)**
EBITDA margin	-	-	-	*27.7%*	*12.9%*	-	-
Unredeemed ticket revenue provision	-	-	12	-	-	-	-
Fleet impairment	4	-	187	-	89	*(95%)*	-
Expected loss on Embraer assets held for sale	(1)	-	50	-	-	-	-
Adjusted EBITDA	**(27)**	**(44)**	**(40)**	**165**	**178**	**-**	**(38%)**
Adjusted EBITDA margin	-	-	-	*27.7%*	*26.0%*	-	-
Cash and equivalents	119	222	307	340	159	(25%)	(46%)
Short-term investments	771	644	741	673	692	11%	20%
Cash	**890**	**866**	**1,048**	**1,013**	**851**	**5%**	**3%**
Accounts receivable	63	36	29	50	130	(51%)	77%
Committed undrawn facilities	305	305	150	-	-	-	0%
Liquidity	**1,258**	**1,207**	**1,227**	**1,062**	**981**	**28%**	**4%**
Loans and borrowings	1,164	1,249	1,325	1,169	1,061	10%	(7%)
Lease liabilities	231	242	270	297	305	(24%)	(5%)
Gross Debt	**1,394**	**1,490**	**1,596**	**1,467**	**1,365**	**2%**	**(6%)**
Net Debt	**505**	**624**	**548**	**454**	**514**	**(2%)**	**(19%)**
LTM Revenue	**801**	**1,324**	**2,000**	**2,631**	**2,707**	**(70%)**	**(40%)**
LTM Adj. EBITDA	**54**	**258**	**508**	**702**	**718**	**(93%)**	**(79%)**
LTM Adjusted EBITDA margin	*6.7%*	*19.5%*	*25.4%*	*26.7%*	*26.5%*	*(1,982 bps)*	*(1,282 bps)*
LTM Adj. Gross Leverage	**26.0x**	**5.8x**	**3.1x**	**2.1x**	**1.9x**	**24.1x**	**20.3x**
LTM Adj. Net Leverage	**9.4x**	**2.4x**	**1.1x**	**0.6x**	**0.7x**	**8.7x**	**7.0x**
Cash / Revenue	**111%**	**65%**	**52%**	**38%**	**31%**	**7,966 bps**	**4,567 bps**
Liquidity / Revenue	**157%**	**91%**	**61%**	**40%**	**36%**	**12,084 bps**	**6,592 bps**

Liquidity Breakdown:

For clarification, we compare our cash and liquidity calculation v. Copa's

Copa Available Liquidity (US$MM)	4Q20	3Q20	2Q20	1Q20	4Q19	y/y	q/q
BCP Calculated Liquidity:							
Cash and equivalents	119	222	307	340	159	(25%)	(46%)
Short-term investments	771	644	741	673	692	11%	20%
Cash	**890**	**866**	**1,048**	**1,013**	**851**	**5%**	**3%**
Accounts receivable	63	36	29	50	130	(51%)	77%
Committed undrawn facilities	305	305	150	-	-	-	0%
Liquidity	**1,258**	**1,207**	**1,227**	**1,062**	**981**	**28%**	**4%**
Copa Reported Liquidity:							
Cash and equivalents	119	222	307	340	159	(25%)	(46%)
Cash	**119**	**222**	**307**	**340**	**159**	**(25%)**	**(46%)**
Short-term investments	771	644	741	673	692	11%	20%
Long-term investments	120	140	95	114	134	(11%)	(14%)
Committed undrawn facilities	305	305	150	-	-	-	0%
Liquidity	**1,314**	**1,311**	**1,293**	**1,127**	**985**	**33%**	**0%**

Company Guidance and Pro-Forma Balance Sheet:

- Fleet:
  - One of the fourteen (14) E190s was sold to a third party as of end-Jan ’21. The remaining eight (8) E190s are expected to be delivered by June ‘21
  - Under its revised fleet plan, Copa expects to receive eight (8) MAX 9s in 2021, and five (5) MAX 9s in 2022
    - As of January ’21, Copa has taken delivery of four (4) of the seven MAX 9s, with the remaining three (3) expected to be delivered by end-1Q21
- Traffic:
  - Management guided to 2.6 bn in ASMs in 1Q21, or 40% of 1Q19 capacity
  - The company expects load factor to contract, given the delay in capacity reductions to meet declining demand, which began in the latter half of Dec. ‘20
- Revenue: 1Q21 total revenue guidance of US$170-200 mm, implies sequential improvement, at an average 17% increase q/q, and slightly y/y improvement, relative to the prior quarter at -73% (4Q20 -77%)
- Cash Burn:
  - Cash burn is expected to deteriorate to -US$120-135 mm (US$1.3 – 1.5 mm / day) in 1Q21, reflecting depressed demand on reintroduction of travel restrictions, and working capital use, as well as delayed costs (~US$10 mm) from amounts carried over from 4Q20 and due in 1Q21
  - We note cash burn includes capex and payments of financial obligations, and excludes asset sales and extraordinary financing activities
- Liquidity:
  - Total Available Liquidity was US$1.4 bn as of February 12, 2021, including the addition of a US$40 mm committed credit facility
  - Liquidity is expected to improve further throughout the course of 1Q21, with additional proceeds from aircraft pre-delivery reimbursements, aircraft sales and other items
    - Copa received final commitment in Dec. ’20 for a guaranteed loan of up to US$327.9 mm from Export-Import Bank of the United States (EXIM Bank)
      - Proceeds will replace existing pre-delivery deposits made by Copa for seven (7) 737 MAX 9, expected to be delivered through FY21
    - A compensation agreement was reached with Boeing in January ‘21, though terms (incl. compensation amount) were not disclosed

Pro-Forma Balance Sheet (US$MM)	Copa
Mgmt. Estimated 1Q21E Cash Burn / Day	(1.4)
Mgmt. estimated 1Q21E Cash Burn / Month	(43)
4Q20 Months of Liquidity Runway	**30**
4Q20 Years of Liquidity Runway	**2.5**
4Q20 Liquidity	**1,258**
(-) 4Q20 Accounts Receivable	63
(-) Undrawn Committed Facilities	305
4Q20 Cash and Equivalents	**890**
(-) 1Q21E Cash Burn	(128)
BCP Calculated Pro-Forma 1Q21E Cash (1)	**762**
(-) Undrawn Committed Facilities	345
(+) 1Q21E Pro-Forma Accounts Receivable	63
BCP Calculated Pro-Forma 1Q21E Liquidity (1)	**1,171**

Pro-Forma Months of Liquidity Runway	**28**
Pro-Forma Years of Liquidity Runway	**2.3**
BCP Est. Pro-Forma 1Q21E Debt (1)	1,394
BCP Est. Pro-Forma 1Q21E Net Debt (1)	**632**
BCP Est. Fully Recovered Revenue (2)	2,707
BCP Est. Fully Recovered EBITDA (2)	718
BCP Est. Fully Recovered EBITDA margin (2)	27%
BCP Est. Pro-Forma Net Leverage (1)(2)	**0.9x**
BBG Consensus '23 Revenue (3)	2,648
BBG Consensus '23 EBITDA (3)	809
BBG Consensus '23 EBITDA margin (3)	31%
BBG Consensus '23 Pro-Forma Net Leverage (1)(3)	**0.8x**

(1) Accounts for 1Q21E cash burn guidance and US$40 mm addtl. financing already acquired. Excludes anticipated additional liquidity inflow from aircraft pre-delivery reimbursements, aircraft sales or other items, est. proceeds not disclosed.
(2) Fully Recovered in line with 2019 Adj. EBITDA. Net leverage = BCP Est. 2020 Pro-Forma Net Debt divided by BCP Est. Fully Recovered EBITDA
(3) Net Leverage = BCP Est. 2020 Pro-Forma Net Debt divided by BBG Consensus EBITDA for 2023

Equity Upside/(Downside) Case:

Copa Holdings S.A. (US$MM)	
Current Market Cap	**3,288**
Current Enterprise Value (EV)	**3,793**
Current EV / EBITDA	**14.7x**
Scenario 1:	**Base Case**
2019 EV / EBITDA	7.1x
Fully Recovered EBITDA (1)	718
Minority Interest	-
EV	5,075
Pro-Forma Net Debt	632
Implied Market Cap	4,443
Equity Upside/(Downside) Potential	**35%**
Implied Stock Price '22	105.09
CPA '25s current px	**168.5**
FV	**203.5**
Cheapness	16.93%
Bond Floor	**89.9**
Upside - CPA '25s	**21%**
Downside – CPA '25s	**(47%)**
Scenario 2:	**Upside Case**
2019 EV / EBITDA	7.1x
BBG Consensus '23 EBITDA (2)	809
Minority Interest	-
EV	5,719
2020 Pro-Forma Net Debt	632
Implied Market Cap	5,087
Equity Upside/(Downside) Potential	**55%**
Implied Stock Price '23	120.34
CPA '25s current px	**168.5**
FV	**232.9**
Cheapness	27.42%
Bond Floor	**89.9**
Upside – CPA '25s	**38%**
Downside – CPA '25s	**(47%)**

(1) Fully recovered in line with 2019 adj. EBITDA
(2) BBG consensus 2023 EBITDA

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"Market Perform" – The bond's total return is expected to be in line with the total return of the CEMBI Broad Diversified High-Yield Index over the next 3 – 6 months.

"Market Underperform" – The bond's total return is expected to be below the total return of the CEMBI Broad Diversified High-Yield Index over the next 3 – 6 months.

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"Positive" – Bonds that in our view have an equity investment risk profile and we think risk/return is skewed to the upside

"Neutral" – Bonds that in our view have an equity investment risk profile and we think risk/return is balanced

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