

## Alaska Air Group, Inc. (ALK)

**\$37.00** (As of 07/17/20)

Price Target (6-12 Months): **\$39.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Neutral**

(Since: 05/15/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**3-Hold**

Zacks Style Scores:

VGM:D

Value: B

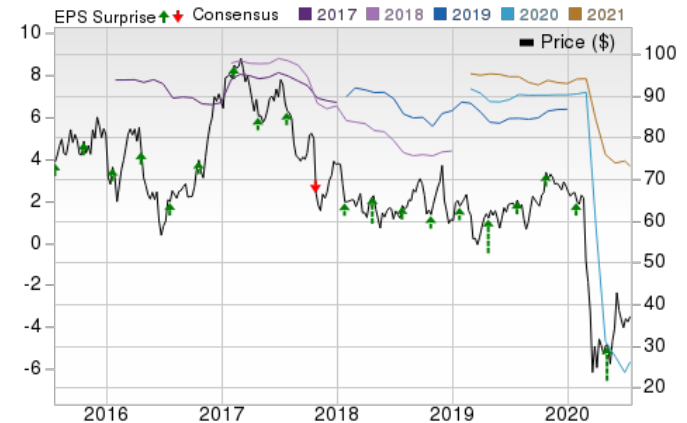
Growth: F

Momentum: F

### Summary

Shares of Alaska Air have plunged 47% since the beginning of February due to drop in air-travel demand in the wake of the coronavirus outbreak. Owing to waning demand, the carrier reduced April and May capacity by 78% and 79% respectively. In June, capacity is anticipated to have declined 70% year over year. The company anticipates second-quarter loss to be greater than the first. The recent spike in coronavirus cases in the United States adds uncertainty to the carrier's recovery. However, the carrier's cost-cutting measures to combat the crisis are noteworthy. The company's June cash burn rate is expected to have reduced to approximately \$150 million, from \$165 million in May. By the year end, Alaska Air hopes to break even. Additionally, the airline is generating substantial cost savings from low fuel prices.

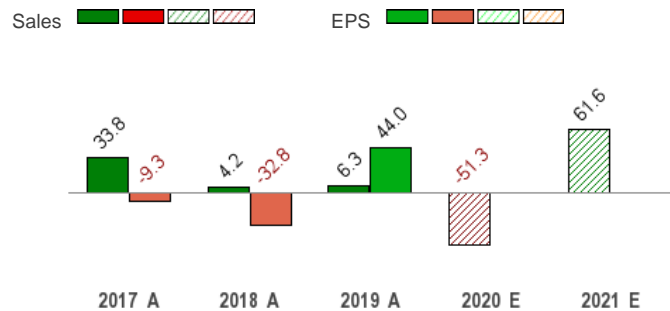
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	\$72.22 - \$20.02
20 Day Average Volume (sh)	2,634,096
Market Cap	\$4.5 B
YTD Price Change	-45.4%
Beta	1.51
Dividend / Div Yld	\$0.00 / 0.0%
Industry	<a href="#">Transportation - Airline</a>
Zacks Industry Rank	Bottom 14% (217 out of 251)

### Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	35.4%
Last Sales Surprise	-3.3%
EPS F1 Est- 4 week change	1.9%
Expected Report Date	07/23/2020
Earnings ESP	16.3%
P/E TTM	6.8
P/E F1	NA
PEG F1	NA
P/S TTM	0.5

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,452 E	1,892 E	2,080 E	2,003 E	6,903 E
2020	1,636 A	308 E	893 E	1,435 E	4,272 E
2019	1,876 A	2,288 A	2,389 A	2,228 A	8,781 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.02 E	\$1.44 E	\$1.60 E	\$0.92 E	\$3.66 E
2020	-\$0.82 A	-\$3.39 E	-\$1.14 E	-\$0.31 E	-\$5.66 E
2019	\$0.17 A	\$2.17 A	\$2.63 A	\$1.46 A	\$6.42 A

\*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 07/17/2020. The reports text is as of 07/20/2020.

## Overview

Alaska Air Group, together with its partner regional carriers, serves more than 100 cities across North America. The carrier's mainline operating fleet includes multiple B737 and Airbus A320 family jets. Its regional operations include flights operated by Horizon Air, which was acquired in 1986, SkyWest and PenAir. The carrier's mainline and regional fleet strength at the end of 2019 was 237 and 95 respectively. The carrier serves 115 destinations.

Horizon Air, which serves nearly 7 million passengers annually, sells its entire capacity to Alaska Airlines under a capacity purchase arrangement. Alaska Airlines was founded in 1932. The regional fleet operated by SkyWest had 32 E175 planes at the end of 2019.

Alaska Air Group, through its mainline operations, covers western United States, Canada and Mexico. It also offers passenger and cargo services to/within Alaska.

Furthermore, the company operates on long-haul east/west routes to Hawaii and multiple cities in the mid-continental and eastern United States, primarily from Seattle.

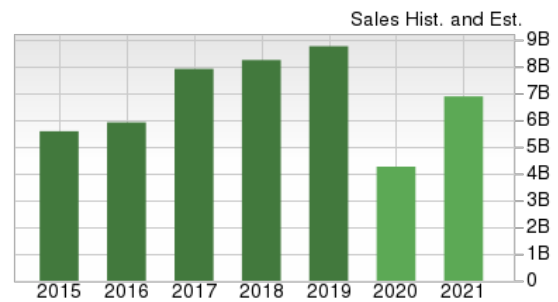
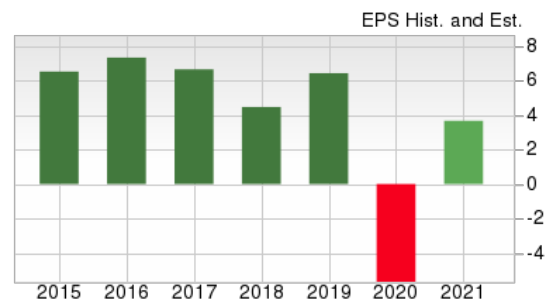
Along with a strong fleet of passenger jets (mainline), the company boasts contracts with Horizon, SkyWest Airlines and Peninsula Airways, that are responsible for the company's regional operations. The company's objective of entering into such contracts is to receive the entire passenger revenue from such operations.

The bulk of the company's revenue is generated through passenger operations. In 2019, passenger revenues contributed 92% (of which 84.3% came from mainline operations) to the company's top line of \$8,781 million. Mileage Plan and cargo and other revenues contributed 5% and 3% respectively to the company's top line in 2019.

Through its frequent flier partnerships, Alaska Air Group offers mileage credits and redemptions for members of its Mileage Plan scheme. Apart from frequent flier partnerships, the carrier also has codeshare and Interline agreements with other carriers.

Such customer-friendly arrangements boost the top line of Alaska Air Group. The acquisition of Virgin America, completed in Dec 2016, has significantly expanded Alaska Air Group's presence.

Alaska Air Group is based in Seattle, WA. The company's fiscal year coincides with the calendar year.



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## Reasons To Buy:

▲ Amid the coronavirus concerns, low fuel costs are a boon to Alaska Air as fuel expenses comprise a major chunk of airline expenditures. Notably, fuel prices declined 9.4% year over year in the first quarter. The savings on fuel costs should support the bottom line and thus help in offsetting the adversities to some extent.

Low fuel prices are a boon for Alaska Air amid coronavirus concerns.

▲ With consistent cost-reduction measures, the company has reduced its monthly cash burn rate to \$165 million in May from \$400 million in April. The company's June cash burn is expected to have decreased to approximately \$150 million. Alaska Air hopes to breakeven by the year-end. Additionally, the carrier reduced discretionary and overhead spending by approximately \$50 million per month. For the current year, Alaska Air has deferred capital expenditures worth approximately \$600 million. With this, the carrier's expected capital expenditures for 2020 is below \$175 million.

▲ The ratification of two five-year agreements with 5,200 airline staffs (clerical, office and passenger service employees as well as ramp service employees and store agents), represented by the International Association of Machinists and Aerospace Workers, is a positive for the company. Prior to the coronavirus outbreak, Alaska Air made consistent efforts to expand its presence along the West Coast. We expect the carrier to resume such initiatives once the crisis is over.

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## Reasons To Sell:

- ▼ Alaska Air started witnessing the impact of coronavirus in late February. The downfall aggravated in March with cancellations exceeding bookings. Consequently, the carrier incurred an adjusted pre-tax loss of \$102 million in the first quarter due to a 14% decline in passenger revenues. The company anticipates second-quarter loss to be much greater. The airline reduced its April and May capacity by 78% and 79% respectively. The carrier expects its June capacity to have declined approximately 70% year over year. Total revenues plunged 87% and 83% in April and May respectively. The company anticipates total revenues to have dropped approximately 80% in June. Substantial loss of passenger revenues due to significantly low travel demand is expected to get reflected in second-quarter performance. Results will be available on Jul 23. The recent spike in coronavirus cases in the United States and the resultant quarantine rules add uncertainty to the carrier's recovery. Alaska Air was seeing week-over-week improvement in demand with easing travel restrictions. However, similar to other airlines, demand might have slowed down in recent times with customers wary of traveling amid quarantine rules imposed in some parts of the United States.
- ▼ Escalating operating expenses are a concern for the carrier, given that the bottom line is already stressed due to low passenger revenues. Notably, operating expenses rose 6% year over year in the first quarter with costs on wages and benefits increasing 10%. Moreover, adjusted non-fuel unit costs inched up 1.8%. Additionally, the carrier's return on equity (ROE) of 16.3% compares unfavorably with 18% for the S&P 500 index, of which Alaska Air is a member. The unfavorable reading undercuts its growth potential.
- ▼ The company's total debt to total capital ratio stood at 0.97 at the end of the first quarter of 2020, comparing unfavorably to the reading of 0.74 at the end of the fourth quarter of 2019. The increasing debt to capitalization ratio indicates that the proportion of debt to finance the company's assets is on the rise. Moreover, Alaska Air received \$992 million via the payroll support program under the CARES Act. While \$725 million of the above amount will be through grants (it doesn't have to be paid back), \$267 million will be via loans. The company has also applied for \$1.1 billion in federal loan funding through a separate program under the CARES Act. This is likely to worsen its debt profile.

Alaska Air reduced April and May capacity by 78% and 79% respectively due to the coronavirus-induced demand slump. Escalating operating expenses are an added concern.

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## Last Earnings Report

### Alaska Air Q1 Loss Narrower Than Expected

Alaska Air incurred a loss of 82 cents per share (excluding \$1.05 from non-recurring items) in the first quarter of 2020, narrower than the Zacks Consensus Estimate of a loss of \$1.27. In the year-ago quarter, the company reported earnings of 17 cents. The downturn is due to unprecedented drop in air travel demand in the wake of the coronavirus outbreak.

Having started in February, the downfall aggravated in March, with cancellations exceeding bookings. Demand is around 90% below the normal level.

Revenues came in at \$1,636 million, missing the Zacks Consensus Estimate of \$1,691.1 million. The top line also declined approximately 13% year over year. Passenger revenues — contributing 90.5% to the top line — were down 14% on a year-over-year basis.

Quarter Ending **03/2020**

Report Date	May 05, 2020
Sales Surprise	-3.26%
EPS Surprise	35.43%
Quarterly EPS	-0.82
Annual EPS (TTM)	5.44

### Operating Statistics

Consolidated traffic, measured in revenue passenger miles, declined 14.4% year over year in the reported quarter. Capacity (measured in available seat miles) dropped 1.3%. Load factor (percentage of seats occupied by passengers) deteriorated 1,070 basis points to 69.6% as traffic declined more than the amount of capacity contraction.

Total revenue per available seat mile (RASM: a key measure of unit revenues) fell 11.7% year over year to 10.69 cents in the quarter under discussion. Meanwhile, yield inched up 0.9% to 13.9 cents.

### Operating Expenses & Income

In the first quarter, total operating expenses (on a reported basis) were up 6% year over year to \$1,957 million, with expenses on wages and benefits increasing 10%. Fuel price (economic) was \$1.93 per gallon, down 9.4% year over year.

The company reported operating loss of \$321 million in the first quarter against operating income of \$25 million in the year-ago quarter. Consolidated cost per available seat mile — excluding fuel and special items — inched up 1.8% to 9.22 cents.

### Liquidity

At the end of the first quarter, the company had \$2,125 million in cash and marketable securities compared with \$1,521 million at the end of 2019.

The company exited the quarter with long-term debt of \$1,203 million compared with \$1,264 million at the end of 2019. Adjusted debt-to-capitalization ratio was 48% compared with 41% at the end of December 2019.

## Recent News

### Boosts Los Angeles Service by Adding New Routes — Jul 16, 2020

Alaska Air announced plans of adding total 12 new destinations to meet the gradually increasing demand amid COVID-19. The carrier plans to add seven new routes from Los Angeles International Airport ("LAX") to boost connectivity between Southern California and key markets around the country.

### Embraer 175 Jets to Operate in Alaska From October — Jun 23, 2020

Alaska Air announced plans of flying the Embraer 175 jet aircraft in few selected markets of Alaska from October 2020. Given its smaller size compared with Alaska Air's flagship Boeing 737s jets, the airline will increase the daily frequency between Anchorage and Fairbanks up to seven times a day. Moreover, the carrier will offer year-round service to King Salmon and Dillingham. The utilization of the Embraer 175 jets will enable the carrier serve small markets more efficiently, where the usage of larger planes are not the best option.

## Valuation

Alaska Air shares are down 45.4% and 41.1% in the year-to-date period and over the trailing 12-month period respectively. Stocks in the Zacks sub-industry and the Zacks Transportation sector are down 42.6% and 7.9% in the year-to-date period respectively. Over the past year, the Zacks sub-industry and the sector are down 42.6% and 4.8% respectively.

The S&P 500 index is up 0.3% in the year-to-date period and 8.8% and in the past year.

The stock is currently trading at 6.8X trailing 12-month price to earnings, which compares to 9.86X for the Zacks sub-industry, 17.03X for the Zacks sector and 20.81X for the S&P 500 index.

Over the past five years, the stock has traded as high as 16.46X and as low as 3.66X, with a 5-year median of 11.99X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$39 price target reflects 7.16X trailing 12-month earnings.

The table below shows summary valuation data for ALK

Valuation Multiples - ALK					
		Stock	Sub-Industry	Sector	S&P 500
P/E TTM	Current	6.8	9.86	17.03	20.81
	5-Year High	16.46	13.19	19.57	22.25
	5-Year Low	3.66	7.45	11.63	15.98
	5-Year Median	11.99	10.58	15.55	19.13
EV/EBITDA TTM	Current	4.92	4.73	7.68	11.98
	5-Year High	10.29	7.03	11.21	12.86
	5-Year Low	3.03	3.19	5.45	8.25
	5-Year Median	6.49	5.9	7.38	10.87
P/S F 12M	Current	0.79	0.71	1.3	3.58
	5-Year High	1.89	0.98	1.42	3.58
	5-Year Low	0.33	0.38	0.85	2.53
	5-Year Median	0.98	0.76	1.2	3.02

As of 07/17/2020

## Industry Analysis Zacks Industry Rank: Bottom 14% (217 out of 251)



## Top Peers

Company (Ticker)	Rec	Rank
American Airlines Group Inc. (AAL)	Neutral	3
Allegiant Travel Company (ALGT)	Neutral	3
Delta Air Lines, Inc. (DAL)	Neutral	4
Hawaiian Holdings, Inc. (HA)	Neutral	3
JetBlue Airways Corporation (JBLU)	Neutral	3
Southwest Airlines Co. (LUV)	Neutral	3
Ryanair Holdings PLC (RYAAY)	Neutral	4
Spirit Airlines, Inc. (SAVE)	Neutral	3

Industry Comparison Industry: Transportation - Airline				Industry Peers		
	ALK	X Industry	S&P 500	JBLU	LUV	SAVE
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	D	-	-	D	D	C
Market Cap	4.54 B	2.33 B	22.62 B	2.92 B	17.37 B	1.21 B
# of Analysts	6	4.5	14	7	11	6
Dividend Yield	0.00%	0.00%	1.82%	0.00%	2.11%	0.00%
Value Score	B	-	-	B	C	B
Cash/Price	0.49	0.51	0.07	0.63	0.33	0.74
EV/EBITDA	3.29	3.69	13.05	2.75	3.58	4.67
PEG Ratio	NA	4.78	2.99	NA	NA	NA
Price/Book (P/B)	1.13	0.68	3.13	0.67	1.91	0.54
Price/Cash Flow (P/CF)	3.73	2.32	12.20	2.86	5.02	2.07
P/E (F1)	NA	23.82	22.02	NA	NA	NA
Price/Sales (P/S)	0.53	0.39	2.34	0.37	0.81	0.32
Earnings Yield	-15.30%	-26.77%	4.28%	-35.40%	-13.04%	-31.57%
Debt/Equity	0.64	0.83	0.75	0.60	0.38	1.45
Cash Flow (\$/share)	9.91	4.15	6.94	3.79	6.80	8.51
Growth Score	F	-	-	D	F	F
Hist. EPS Growth (3-5 yrs)	-5.75%	2.29%	10.85%	-4.34%	4.95%	1.76%
Proj. EPS Growth (F1/F0)	-188.19%	-253.95%	-9.37%	-301.73%	-204.13%	-209.20%
Curr. Cash Flow Growth	28.26%	12.07%	5.51%	14.33%	-3.22%	19.78%
Hist. Cash Flow Growth (3-5 yrs)	7.14%	8.55%	8.55%	14.43%	8.55%	15.50%
Current Ratio	0.69	0.69	1.30	0.61	0.69	1.00
Debt/Capital	39.10%	56.38%	44.33%	37.48%	27.38%	59.14%
Net Margin	6.24%	1.05%	10.59%	3.32%	8.46%	6.71%
Return on Equity	16.29%	9.01%	15.74%	8.63%	18.92%	10.59%
Sales/Assets	0.65	0.61	0.54	0.67	0.81	0.54
Proj. Sales Growth (F1/F0)	-51.35%	-45.36%	-2.44%	-53.15%	-52.03%	-48.94%
Momentum Score	F	-	-	F	B	B
Daily Price Chg	-0.75%	-1.48%	0.36%	-1.81%	-0.23%	-2.49%
1 Week Price Chg	-2.08%	-1.29%	-0.41%	-0.66%	-2.64%	0.75%
4 Week Price Chg	-1.20%	-5.64%	2.56%	-10.13%	-4.80%	-11.51%
12 Week Price Chg	31.21%	18.18%	15.49%	35.08%	13.24%	49.24%
52 Week Price Chg	-42.51%	-48.64%	-3.93%	-43.70%	-34.92%	-65.66%
20 Day Average Volume	2,634,096	149,178	2,236,294	13,503,082	15,973,280	17,602,746
(F1) EPS Est 1 week change	4.23%	0.00%	0.00%	0.00%	4.86%	3.47%
(F1) EPS Est 4 week change	1.88%	0.00%	0.01%	-7.46%	7.58%	12.74%
(F1) EPS Est 12 week change	-295.00%	-112.49%	-5.24%	-404.32%	-4,375.35%	-353.13%
(Q1) EPS Est Mthly Chg	-46.95%	0.00%	0.00%	-45.24%	6.18%	1.65%

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## Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

### Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

### Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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### Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	<b>B</b>
Growth Score	<b>F</b>
Momentum Score	<b>F</b>
VGM Score	<b>D</b>

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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