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Emma Powell ***Tempus***
Buy, sell or hold: today's best share tips

Easyjet stuck in a holding pattern

EASYJET

Market cap	Full-year loss
£3.01 billion	£208 million

If the challenges battering the aviation industry forces consolidation, the budget airline easyJet looks ripe for another takeover approach. A narrowing loss and a recovery in passenger numbers that has seen capacity creep further towards the pre-pandemic level might help to convince suitors that the risks facing the group are already accounted for in a cut-price market value.

Airline stocks have struggled to sustain momentum since travel restrictions began to ease as the war in Ukraine, a jump in fuel and staff costs, and fears that the cost of living crisis could cause a slump in bookings have deterred investors from buying into the recovery story.

EasyJet is the cheapest of them all, more lowly priced than British Airways' parent, IAG, which is saddled with a hefty debt load. An enterprise value of 3.6 times forecast earnings before tax and other charges is near the lowest level in at least a decade. A £1.2 billion rights issue just over 12 months ago only partly explains the airline's discount to London-listed rivals. Investors also factored in far less ambitious fleet expansion plans by easyJet than those of Wizz and Ryanair, with the number of aircraft barely expanding until at least 2026.

Analysts expect this financial year will finally mark the carrier's return to profitability, forecasting a pre-tax profit of £229 million, against a loss of £208 million last year.

Capacity is on track to hit 84 per cent of the 2019 level during the final three months of this calendar year and Johan Lundgren, chief executive, reckons it is on course to be at least in line with the pre-pandemic level by the three months to the end of September next year.

There are two risks to the airline hitting market expectations this year: costs inflating more than anticipated and consumers cutting back on holidays. The volume of trips booked in October half-term and Christmas are back to historic norms, but visibility over the second half of the year is low. EasyJet has hedged 74 per cent of its jet fuel exposure for the first half of the financial year but only 51 per cent for the six months to the end of September next year.

Jet fuel prices have come down by more than a quarter since peaking in June, according to the International Air Transport Association. Still, over the entire financial year easyJet's fuel bill will be almost two-thirds higher than last year, at about £2.11 billion, HSBC calculates.

Analysts at HSBC raised adjusted pre-tax profit forecasts for the current financial year to £197 million, from £138 million, in light of bullish guidance on bookings up until Easter. But HSBC cut its forecast for profit over the 12 months to the end of September 2024 to £233 million, from the £341 million it previously expected, reflecting cost inflation and macroeconomic weakness.

EasyJet is trying to win market share by taking business from legacy carriers at airports that it already uses by trying to compete on price. The upside to that strategy? It is more capital light than the fleet expansion strategy being pursued by Wizz. The downside? Competition, with Ryanair and Wizz launching new routes across two of easyJet's UK bases at Gatwick and Luton, which puts fares into sharper focus.

Half of fares on sale are priced under £50, according to easyJet, which could mean it benefits from consumers trading down. But rival carriers might also flex fares to win passengers. Its balance sheet is a strength, with net debt of about £670 million, equating to a leverage ratio of about 1.2, and an investment grade credit rating to boot. But in the face of consumers cutting back on spending and the need to prove the airport chaos that ensued this year won't be repeated, the shares may tread water in the near-term.

ADVICE Hold
WHY A cheap value compensates investors for the risks of cost inflation and weaker consumer spending

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