



Copa Holdings, S.A. (CPA)

Updated May 13th, 2019 by Josh Arnold

Key Metrics

Current Price:	\$94	5 Year CAGR Estimate:	2.8%	Volatility Percentile:	88.8%
Fair Value Price:	\$77	5 Year Growth Estimate:	4.0%	Momentum Percentile:	16.7%
% Fair Value:	122%	5 Year Valuation Multiple Estimate:	-4.0%	Growth Percentile:	22.9%
Dividend Yield:	2.8%	5 Year Price Target	\$94	Valuation Percentile:	22.9%
Dividend Risk Score:	D	Retirement Suitability Score:	D	Total Return Percentile:	12.6%

Overview & Current Events

Copa Holdings was founded in 1947 in Panama City. The company was originally called the National Airline of Panama and since its humble beginning with just three flights, it has grown to an international airline with more than 300 daily flights to more than 30 countries. The company produces about \$2.7 billion in revenue annually and has a market capitalization of \$4 billion. As Copa is a Panamanian company, dividends are subject to a 10% tax to foreign investors.

Copa reported Q1 earnings on 5/8/19 and results were lower than expected. Total earnings-per-share came in at \$2.11 for the quarter, a one-third decline from the \$3.22 reported in the year-ago period.

Operating profit came in at \$113 million, representing a 24% decline from the \$148 million that was posted in last year's Q1. The decline came from a 7.7% decrease in unit revenues, defined as revenue per available seat mile, which was partially offset by a 3.2% improvement in unit costs, or costs per available seat mile. While Copa's focus on costs paid off in Q1, revenue per available seat mile was unexpectedly very weak. As a percentage of revenue, operating profits came in at 16.8% against 20.6% from the year-ago period.

Passenger traffic grew 2.3% while capacity expanded 1.9%, resulting in a consolidated load factor of 83.3%, a gain of 40bps year-over-year. Copa's load factor is fairly strong, so its sizable drop in revenue per available seat mile is that much more concerning.

In total, revenue declined 6% in Q1 as yield per passenger mile fell a staggering 8.8% thanks to the factors discussed.

We've cut our estimate for this year to \$7.00 in earnings-per-share from \$7.40 because of a much weaker than expected Q1 result.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$5.47	\$5.48	\$6.98	\$7.35	\$9.63	\$8.15	-\$5.13	\$7.90	\$8.72	\$6.52	\$7.00	\$8.52
DPS	\$0.37	\$1.09	\$1.64	\$4.35	\$1.46	\$3.84	\$3.36	\$2.04	\$2.52	\$3.48	\$2.60	\$3.15
Shares	43.4	43.6	43.9	44.0	44.1	44.0	44.4	42.1	44.7	42.5	42.0	40.0

Copa's earnings-per-share history has been quite volatile, as one would expect for an airline. Looking forward, we expect 4% earnings-per-share growth annually, reflecting the uncertain environment airlines are operating in today.

Copa will achieve this by continuing to increase capacity as well as its passenger miles flown. The company continues to buy more and more capacity as it is now has over 100 aircraft, and we expect it has a significant runway to acquire more capacity in the coming years. Passenger miles flown continue to increase but the company's declining load factor is a worry. In addition, fuel pricing is a wildcard for Copa. We cannot predict how fuel prices will fluctuate in the coming years, but it is likely to have a meaningful impact on Copa's earnings. Q1 earnings introduced a new risk of much lower yields as well, so we are more cautious.

The dividend is back down to \$2.60 per share and we expect it will grow with earnings, hitting \$3.15 per share over the next five years. Copa already has a nice yield but is not willing to distribute a majority of earnings as dividends. Thus, we see its strategy remaining stable as Copa uses cash to buy additional capacity, not significantly boosting the dividend.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	7.0	9.6	8.8	11.0	13.7	15.9	---	8.8	13.5	15.8	13.5	11.0
Avg. Yld.	1.0%	2.1%	2.7%	5.4%	1.1%	3.0%	4.2%	2.9%	2.1%	3.4%	2.8%	3.4%

The company's price-to-earnings multiple has moved around a lot over the years, which is typical of airline stocks given that they are very cyclical. Today, the stock trades for 13.5 times our earnings estimate for this year, which is meaningfully in excess of our fair value estimate. Therefore, we see a 4% headwind to total returns from a declining valuation. That could also help send the yield higher as we see it cresting 3% again in the coming years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	7%	20%	23%	59%	15%	47%	---	26%	29%	53%	37%	37%

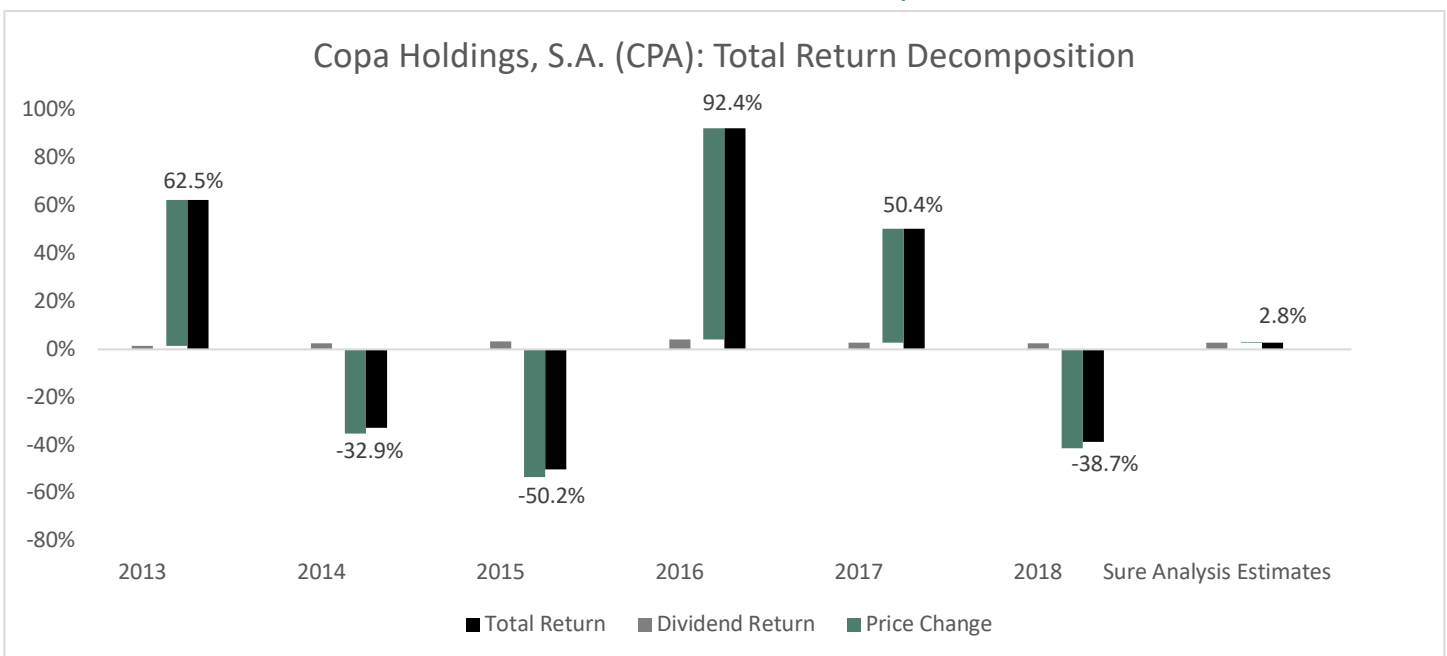
Copa's payout ratio was uncharacteristically high in 2018, but is around one-third of earnings for this year. We expect that is where it will stay in the coming years, particularly if weakness continues to characterize the company's results.

Copa's competitive advantage is in its strong financial situation, which allows it to acquire profitable growth. It will suffer during the next recession, however, as all airline stocks will, so that is something for investors to consider.

Final Thoughts & Recommendation

This stock tends to have boom and bust cycles, and given Q1 results, it would appear the company is trending lower at the moment. We see total returns of just 2.8% for Copa, comprised of 4% earnings growth, the 2.8% yield and a 4% headwind from the valuation. Given the risks to the company's fundamentals as well as the yield that has fallen well below 3%, along with a stock that is overvalued in our view, we're reiterating Copa at a sell recommendation. The stock is pricing in too much good news today so we think investors should avoid it for the time being.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	1256	1415	1831	2249	2608	2705	2254	2219	2522	2678
Gross Profit	689	1060	1284	1524	1825	1884	1650	1690	1949	1912
Gross Margin	54.9%	74.9%	70.1%	67.7%	70.0%	69.7%	73.2%	76.2%	77.3%	71.4%
SG&A Exp.	317	324	377	451	516	559	810	795	846	888
D&A Exp.	51	64	76	90	137	115	151	168	167	169
Operating Profit	322	290	385	403	518	521	253	265	424	334
Operating Margin	25.6%	20.5%	21.0%	17.9%	19.8%	19.3%	11.2%	11.9%	16.8%	12.5%
Net Profit	249	241	310	326	427	362	-241	323	364	88
Net Margin	19.8%	17.0%	17.0%	14.5%	16.4%	13.4%	-10.7%	14.6%	14.4%	3.3%
Free Cash Flow	80	101	367	360	736	259	216	492	599	288
Income Tax	27	19	36	40	61	37	33	38	49	35

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	2161	2556	3066	3480	3953	4080	3519	3641	4045	4087
Cash & Equivalents	263	208	244	76	139	221	205	332	239	156
Accounts Receivable	81	89	130	125	125	117	106	114	116	116
Inventories	27	46	42	51	57	60	62	75	82	87
Goodwill & Int. Ass.	66	69	72	87	54	57	69	70	81	101
Total Liabilities	1250	1446	1676	1943	2051	2005	2128	2004	2150	2247
Accounts Payable	51	66	93	105	95	125	219	104	117	125
Long-Term Debt	846	990	1068	1206	1070	1117	1301	1184	1175	1287
Shareholder's Equity	911	1110	1390	1537	1902	2075	1391	1637	1895	1841
D/E Ratio	0.93	0.89	0.77	0.78	0.56	0.54	0.94	0.72	0.62	0.70

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	12.1%	10.2%	11.0%	10.0%	11.5%	9.0%	-6.3%	9.0%	9.5%	2.2%
Return on Equity	32.3%	23.9%	24.8%	22.3%	24.9%	18.2%	-13.9%	21.4%	20.6%	4.7%
ROIC	15.1%	12.5%	13.6%	12.6%	15.0%	11.7%	-8.2%	11.7%	12.4%	2.8%
Shares Out.	43.4	43.6	43.9	44.0	44.1	44.0	44.4	42.1	44.7	42.5
Revenue/Share	28.61	32.16	41.15	50.65	58.76	60.93	51.37	52.39	59.45	63.07
FCF/Share	1.82	2.30	8.26	8.12	16.58	5.83	4.92	11.61	14.11	6.77

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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