



11 February 2015

Companies Announcement Office  
Australian Securities Exchange  
20 Bridge Street  
SYDNEY NSW 2000

Dear Sir/Madam

**Announcement from Standard and Poor's**

Please see attached announcement from Standard and Poor's that replaces the previously released document which was incomplete.

Yours faithfully

Andrew Finch  
Company Secretary



Qantas Airways Limited ABN 16 009 661 901  
10 Bourke Road Mascot NSW 2020 Australia  
Telephone +61 2 9691 3636

**qantas.com**

# RatingsDirect®

---

## Research Update:

# Qantas Airways Outlook Revised To Stable On Improved Operating Environment; 'BB+' Ratings Affirmed

### Primary Credit Analyst:

Graeme A Ferguson, Melbourne (61) 3-9631-2098; [graeme.ferguson@standardandpoors.com](mailto:graeme.ferguson@standardandpoors.com)

### Secondary Contact:

May Zhong, Melbourne (61) 3-9631-2164; [may.zhong@standardandpoors.com](mailto:may.zhong@standardandpoors.com)

## Table Of Contents

---

Overview

Rating Action

Rationale

Outlook

Ratings Score Snapshot

Recovery Analysis

Related Criteria And Research

Ratings List

## Research Update:

# Qantas Airways Outlook Revised To Stable On Improved Operating Environment; 'BB+' Ratings Affirmed

## Overview

- We expect Qantas' credit metrics to benefit from more-benign domestic operating conditions; lower oil prices; and a lower Australian dollar. However, we expect weak underlying demand conditions to persist.
- In our view, the immediate threat to the 'BB+' corporate credit rating on Qantas has receded.
- As a result, we have affirmed the 'BB+' corporate and issue credit ratings on Qantas and revised the outlook to stable from negative.
- Qantas' resilience to variable demand conditions, competitive tensions, volatile fuel costs, and exogenous shocks, will be key ongoing rating considerations.

## Rating Action

On Feb. 11, 2015, Standard & Poor's Ratings Services revised the rating outlook on Australian airline Qantas Airways Ltd. to stable from negative. At the same time, we affirmed the 'BB+' long-term issue rating on Qantas and the airline's senior unsecured debt, and the 'B' short-term rating on Qantas. The recovery rating on the debt is also affirmed at '3', indicating our expectation of meaningful (50%-70%) recovery for creditors in the event of a payment default.

## Rationale

The outlook revision to stable reflects our view of the meaningful improvement in Qantas' operating environment which we expect to translate to improved credit metrics. We therefore believe that the immediate threat to the 'BB+' corporate credit rating on Qantas has receded. However, we expect underlying demand conditions to remain weak for the Australian airline industry. In our opinion, Qantas remains somewhat vulnerable to sudden changes in its operating environment that are a common and recurring feature of the airline industry.

Underpinning the corporate credit rating on Qantas is its strong domestic market position. Qantas is currently benefiting from more-benign domestic market conditions, including more-measured capacity growth. However, we view Qantas' competitive position within the Australian market to have structurally deteriorated over the past few years. Competition from Virgin Australia Holdings (B+/Stable/--) has highlighted its susceptibility to periodic bouts

of aggressive competition. Despite Qantas conceding some market share, we expect the airline to retain its dominant position within the Australian market. However, we assess underlying demand conditions to remain weak, weighing on Qantas' yield and load.

We expect the recent steep decline in oil prices to enable Qantas to recover its credit metrics at a much faster pace than our previous base-case expectations. We view Qantas to have competently managed its fuel price risk and currency exposure. Although the airline may not immediately experience the full benefit of lower prices, we expect Qantas' risk management framework to continue to be effective in absorbing some short-term price volatility whilst also allowing participation in favorable price movements. Over time, we believe that Qantas will capture a more lasting benefit of lower oil prices through its domestic operations, where it faces less price competition compared with its international operations.

The relationship between Qantas' profitability and the Australian-U.S. dollar exchange rate is complex. Nevertheless, we assess recent movement in the value of the Australian dollar to be of net benefit to the airline. We expect Qantas' international operations to be the main beneficiary of a lower exchange rate via the division's increased competitiveness. However, we continue to view Qantas' international operations as facing significant challenges, notwithstanding the more-favorable exchange rate and lower fuel price.

Qantas is midway through a transformation program aimed at addressing the airline's legacy and underlying structural issues. In our opinion, this is imperative given unpredictable industry conditions and that we do not forecast a demand-led recovery. We view the initial results to be favorable: improved unit cost differential between Qantas and its major competitors provides evidence of progress. However, we are mindful of the size and complexity of the restructuring task that remains ahead. Moreover, the task must be achieved without impairing Qantas' ability to attract a yield premium. This includes customer satisfaction, particularly among business travelers, safety, route network, and on-time performance. In addition, Qantas' transformation program relies heavily on improved labor cost, productivity, and flexibility. We note that Qantas operates within a complex industrial relationship framework.

We continue to view Qantas as having a successful dual-brand strategy covering full-service and low-cost segments. In addition, we believe that stable cash flows generated by Qantas' frequent flyer business will continue to partially offset the more-volatile cash flows generated from its traditional airline operations.

Qantas has strong financial flexibility and a good track record of responding to earnings pressure through managing costs and deferring capital expenditure. At June 30, 2014, the weighted average age of Qantas' fleet was 7.7 years, providing the airline with meaningful scope with which to manage its capital expenditure schedule. We anticipate that Qantas' improved financial metrics will provide it with increased flexibility to modestly accelerate its fleet

strategy while limiting pressure on its balance sheet. In addition, the airline has the capacity to divest sizable assets at its discretion. We believe these measures should provide near-term relief to Qantas' balance sheet and liquidity position during periods of elevated financial stress.

### **Liquidity**

We consider Qantas' liquidity to be strong. We expect that sources of liquidity in the next 12 months will exceed uses by at least 1.5x. We expect that liquidity sources will continue to exceed uses, even if EBITDA were to decline by 30%. The company has a manageable debt-maturity profile in the next two years. We note that none of Qantas' debt facilities have financial covenants. We expect Qantas will continue to hold a sizable unrestricted cash balance of about A\$2 billion.

### **Outlook**

The stable outlook reflects our view that competition across Qantas' route network will be contained and that the airline will maintain its dominant domestic market position. We also expect Qantas to maintain its meaningful financial flexibility and strong liquidity position. The rating incorporates our expectation that Qantas will realize an enduring benefit from previously announced restructuring initiatives while limiting pressure on its balance sheet. We do not forecast a demand-led recovery. However, structurally lower fuel prices, a more-benign domestic market environment, and a lower Australian dollar should translate into improved credit metrics for the airline.

### **Downside scenario**

We could lower the ratings if Qantas fails to accomplish its previously announced restructuring initiatives or if the efforts do not provide the airline with sufficient flexibility to respond to sudden changes to its operating environment. This would be evidenced by the airline's funds from operations (FFO)-to-debt falling to less than 20%. A weakening of Qantas' liquidity position will also put downward pressure on the rating, particularly if we assess Qantas' unrestricted cash and available liquidity were to decline to less than A\$2 billion.

### **Upside scenario**

The rating is not likely to be raised for at least the next 12 to 18 months. Over the medium-to-long term, positive rating action would require evidence of a more robust and versatile operating platform. Credit metrics are likely to be less important than the context through which they were achieved. We could ultimately raise the rating if we expect Qantas to sustain FFO-to-debt at more than 45% under a range of variable demand conditions, competitive tensions, volatile fuel costs, and exogenous shocks.

## **Ratings Score Snapshot**

Corporate Credit Rating: BB+/Stable

Business risk: Fair

- Country risk: Low
- Industry risk: High
- Competitive position: Satisfactory

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: bb

Modifiers

- Diversification/portfolio effect: Neutral
- Capital structure: Neutral
- Liquidity: Strong
- Financial policy: Neutral
- Management and governance: Satisfactory
- Comparable rating analysis: Positive

Stand-alone credit profile: bb+

## **Recovery Analysis**

The long-term issue rating on Qantas Airways Ltd.'s senior unsecured debt is 'BB+', in line with the corporate credit rating. The recovery rating of is '3', indicating our expectation of meaningful (50%-70%) recovery for creditors in the event of a payment default. Supporting the issue and recovery ratings is our valuation of Qantas Airways as a going concern in a hypothetical default scenario. The ratings reflect our view of the airline's leading domestic market position, the enduring value of the Qantas brand, and our assessment that the business would retain more value as a reorganized operating entity than in liquidation.

## **Related Criteria And Research**

### **Related Criteria**

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Key Credit Factors For The Transportation Cyclical Industry, Feb. 12, 2014
- Group Rating Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012

*Research Update: Qantas Airways Outlook Revised To Stable On Improved Operating Environment; 'BB+' Ratings Affirmed*

- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

#### Related Research

- Standard & Poor's Revises Its Crude Oil And Natural Gas Price Assumptions, Jan. 10, 2015

## Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Qantas Airways Ltd. Corporate Credit Rating	BB+/Stable/B	BB+/Negative/B

Ratings Affirmed

Qantas Airways Ltd.

Senior Unsecured

AUD1.63 mil Loan Note Facility BB+  
tranches due 2010, 2011, 2014

Recovery Rating 3

US\$513.6 mil 6.05% nts due BB+  
04/15/2016

Recovery Rating 3

AUD250 mil 6.50% nts ser QANT04 due BB+  
04/27/2020

Recovery Rating 3

AUD300 mil 7.75% med-term nts ser BB+  
QANS02 due 05/19/2022

Recovery Rating 3

AUD400 mil 7.50% med-term nts ser BB+  
QANS03 due 06/11/2021

Recovery Rating 3

Complete ratings information is available to subscribers of RatingsDirect at [www.globalcreditportal.com](http://www.globalcreditportal.com) and at [www.spcapitaliq.com](http://www.spcapitaliq.com). All ratings affected by this rating action can be found on Standard & Poor's public Web site at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

Standard & Poor's (Australia) Pty. Ltd. holds Australian financial services licence number 337565 under the Corporations Act 2001. Standard & Poor's credit ratings and related research are not intended for and must not be distributed to any person in Australia other than a wholesale client (as defined in Chapter 7 of the Corporations Act).

Copyright © 2015 Standard & Poor's Financial Services LLC, a part of McGraw Hill Financial. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, [www.standardandpoors.com](http://www.standardandpoors.com) (free of charge), and [www.ratingsdirect.com](http://www.ratingsdirect.com) and [www.globalcreditportal.com](http://www.globalcreditportal.com) (subscription) and [www.spcapitaliq.com](http://www.spcapitaliq.com) (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at [www.standardandpoors.com/usratingsfees](http://www.standardandpoors.com/usratingsfees).