

Sydney Airport shares COVID-19 pain the right way

Shareholders, tenants and staff will need to take their portion of the bitter medicine required to get through the aviation industry's recovery.



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It says all you need to know about the size of the hole Sydney Airport finds itself in that the biggest section of the 71-page investor presentation announcing a \$2 billion capital raising is the appendix detailing key risks.

Over the course of 12 pages, no less than 30 risks are listed, from the ever-present aircraft accidents and security issues through to longstanding litigation with the Danish tax authorities.

But at the top of the list are the three worries that have been keeping chief executive Geoff Culbert awake at night for nearly six months now – COVID-19 uncertainty, pandemic risks and plunging passenger and aircraft movements.

So much of the damage caused by the pandemic starts at airports' terminal gates.



Geoff Culbert insists Sydney Airport has a strong future beyond the pandemic. **Peter Braig**

The pain in aviation specifically and tourism generally, the hit to the education sector and the damage to international trade have all weighed heavily on a business that is not only one of Australia's most important pieces of infrastructure, but generates 7 per cent of the NSW gross state profit.

An airport that moved more than 44 million people to over 90 destinations in 2019 saw passenger numbers plunge 56.6 per cent to 9.4 million in the six months ended June 30 versus the first half of calendar 2019.

Only 400,000 passengers came through the airport in the June quarter, amid what Culbert described on Tuesday as the most stringent restrictions on movement since World War II.

This outlook leaves Sydney Airport little choice but to enter an even deeper form of hibernation than it foresaw in April.

Having pulled on a range of levers since March – raising \$850 million in fresh debt, cutting interest costs, slashing operating costs by about 25 per cent so far and reducing capital expenditure – Culbert now wants investors to fund what is essentially a \$2 billion insurance policy that will allow him to “confidently manage through the pandemic regardless of the shape and pace of the recovery”.

“Our job is now to get us through the current crises and put the company in the best position to thrive and to grow,” Culbert declared, sounding calm and determined during a call with investors and analysts.

“We will get back to the trajectory of consistent, long-term growth. We are in this for the long haul.”

Of course, when that recovery might happen is far from certain. International traffic was down 97.2 per cent in July, with domestic traffic down 88.2 per cent, and August looks likely to deliver broadly similar results.

Culbert is unhappy with the latest round of border closures, arguing they contradict federal health department advice. And he wants to see a more detailed plan about how the country – and particularly aviation – will actually live with COVID-19 under a range of circumstances, including a vaccine not being found.

"What we would like to see is a set of rules that are based around the advice of the federal health authorities, that are consistently applied across the country."

For now, though, he is taking some hope from the strong recovery in passenger numbers in countries where domestic travel has resumed, such as Vietnam, Taiwan and South Korea.

But the broad forecast from the International Air Transport Association, which sees a recovery in revenue to pre-COVID-19 levels not arriving until 2024 – has been adopted by Culbert and his team as a sort of base case, albeit one that has little relevance to short-term conditions.

This outlook leaves Sydney Airport little choice but to enter an even deeper form of hibernation than it foresaw in April, when Culbert's aim was to effectively buy the group six months in the hope he would have a better idea of the depth and length of the pandemic. And this hibernation will come with pain for everyone.

Pain will be felt across the board

The \$2 billion raising immediately reduces net debt from \$9.1 billion to \$7.1 billion, with liquidity of \$4.6 billion available to buttress the balance sheet over the next 18 months, and protect Sydney Airport's investment-grade credit rating.

But shareholders will also be hit by the abandonment of dividends for calendar 2020, and quite possibly much longer.

Culbert emphasised that Sydney Airport doesn't need to get back to pre-COVID-19 earnings levels to resume a dividend, but also made it clear there won't be a rush back to returns either.

“We will be cautious in our approach. We'll be carefully monitoring the situation to ensure that we don't want to get ahead of the recovery.”

Retail and property tenants at the airport have, and will continue, to share the airport's pain. Culbert says the group has aimed to be fair in its discussions with tenants, offering the biggest rent waivers to mum and dad operators.

Between April and June, \$52.9 million worth of rent waivers was offered, representing 62 per cent of what Sydney Airport would usually charge in rent.

Further negotiations will be conducted quarter by quarter – the rent waivers will continue, but quite reasonably Culbert will not be locked into long deals in such a volatile time.

The other group to share in the COVID-19 pain will be Sydney Airport's employees. Back in April, Culbert guaranteed the jobs of all of his 500-odd staff, but given the environment, that guarantee will end as scheduled on September 30. Job losses are inevitable if Culbert wants to achieve his target of bringing operational costs down by 35 per cent by April 2021.

There was no number placed on job cuts, and a complete review of how to restructure the business is under way.

“COVID-19 has enveloped us all in ways we couldn’t imagine,” says Culbert, who has already taken a 20 per cent pay cut.

Figuring out what that restructure will look like will not be easy. Without knowing what travel might look like in six months, Culbert wants to retain maximum flexibility.

“I can assure you we’ve thought of everything and we constantly reassess based on the news flow ... we’ve become very match fit and agile,” he says.

Sydney hasn’t yet followed the lead of Canberra Airport, which will now shut down on Saturdays, but it’s not off the table either.

Culbert’s aim on Tuesday was to emphasise Sydney Airport’s long-term strength, its short-term flexibility and its desire to approach difficult conversations with staff, tenants and investors in a principled way.

Indeed, we can only applaud the decision by Culbert, his board and advisers Adara Partners – the not-for-profit firm that now has a couple of up-and-comers in Matthew Grounds and Guy Fowler working with it – to use a fully underwritten pro-rata accelerated renounceable entitlement offer for its capital raising.

“We want to make sure our existing security holders, particularly our long-time, loyal security holders, are not diluted. That was very important for the board and very important for me as CEO,” Culbert says.

Despite renounceable rights issues being the fairest way of raising capital, it has been rarely seen in the rush of COVID-19 raisings, with most bankers quick to say it simply takes time in a volatile market.

But the fact that a business so dramatically whacked by the pandemic can take the time to treat investors with respect says a bit about this argument – and plenty about the long-term way Sydney Airport thinks about its shareholder base.

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