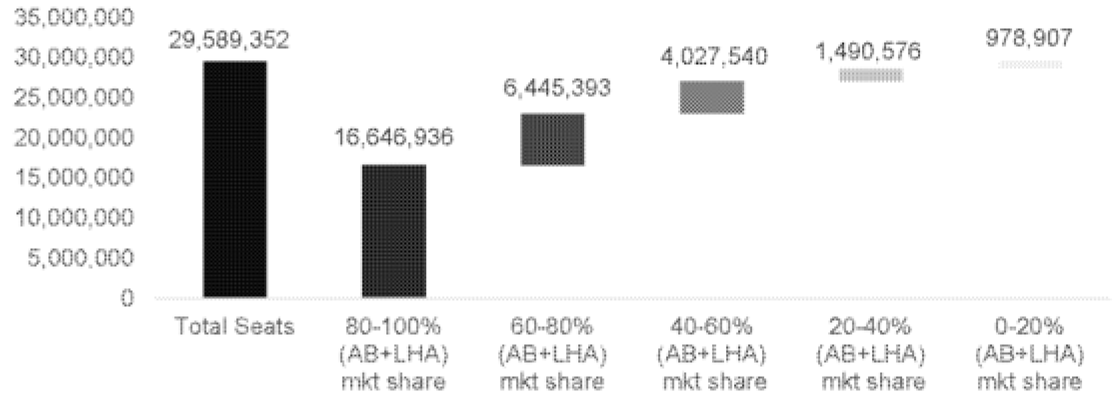
Deutsche Bank

# 30 Deutsche Lufthansa – Anand Date, BUY, close €30.7, €36.2 tgt, 18% upside

- **The Air Berlin acquisition is an excellent deal.** >50% of Air Berlin flown capacity on routes where Lufthansa + Air Berlin would have combined 80-100% market share, creating capacity and revenue management opportunities.
  - The combined group would have a number of strong positions at severely and slightly constrained airports. Our August 2017 note ("Finding a sweet slot") highlighted the benefits of such positions, in terms of network flexibility, better pricing power and tangible slot value.
- **Airline M&A has historically been highly accretive**, generally yielding synergies of 3-7% of combined revenues (3/4 revenue, 1/4 cost).
- **Lufthansa is not inheriting legacy costs**, only purchasing assets at market rates. It has guided that the deal should reduce unit costs.
- **We see a ROCE of 25-35% on a three year view** based on a €1.5bn investment in the deal.
- **The market is not reflecting this in forecasts.** We forecast incremental EBIT of €470m by 2019, leaving us 22% ahead of consensus.
- **Antitrust risk is limited:** 1) Lufthansa is providing much of Air Berlin bridge financing; 2) EC did not block the Lufthansa-Swiss Air deal despite similar local market dominance
- **Shares should trade up on earnings growth and consensus revisions.** Currently trades on 6.5x 1yr fwd P/E. With 5% and 18% adjusted EBIT growth in 18E/19E, we see consensus upgrades as likely as the deal is priced in.

**Related DB Research:**
Lufthansa: AB Fab. Upgrade to BUY (Date)
Transportation Outlook 2018: Going Places (Chu)

### Combined AB + LHA has over half its capacity on routes with >80% share




Source: Deutsche Bank, Diio Mi

### Airline M&A has historically yielded material synergies

| Date | Acquirer / Candidate | Total Synergies | % of Revenue |
|---|---|---|---|
| Sep 2010 | Southwest / AirTran | US$400 million | 3% |
| Aug 2010 | LAN / TAM[a] | US$400 million[b] | 4% |
| May 2010 | UAL / Continental[a] | US$1.2 billion | 4% |
| Nov 2009 | British Airways / Iberia[a] | US$600 million[c] | 3% |
| Apr 2008 | Delta / Northwest[a] | US$2.0 billion | 6% |
| Apr 2005 | America West / US Airways | US$680 million | 7% |

NB: Unless notes, all of the above synergy totals reflect an annual run rate and were expected to be achieved by year three following transaction close. (a) Transaction structured as a merger of equals, (b) In early 2012, LAN and TAM revised their synergy forecast to $600 - $700 million beginning four years after completion of the transaction and representing 4.5% - 5.0% of LTM combined revenue, (c) At the time of the announcement, BA and Iberia identified €400 million of annual synergies (after five years) which we converted to US$ at the time of the announcement. Source: Deutsche Bank, Company Data