Protect, Restore and Maximize Value

EUROPEAN TRAVEL UPDATE – Q3 2020

UNCERTAINTY CONTINUES – M&A VOLUMES REMAIN LOW

Travel Update – Overview

Welcome

Welcome to Duff & Phelps' inaugural quarterly travel update – launched at a time when the industry has never faced greater challenges, so many good people have been made redundant and M&A volumes have never been lower.

In this quarter's European Travel Update, we will focus on sector updates, M&A activity and related themes. Each edition will include a guest feature from one of our other service lines at Duff & Phelps – this edition includes an update from our European Debt Advisory team.

COVID-19 Impact on M&A Activity

Unsurprisingly, M&A activity in the travel sector has almost stalled since the COVID-19 pandemic. Six months into an unprecedented lockdown and post-lockdown, significant uncertainty remains over how the industry will look and what the new "normal" will be. The knock-on impact on M&A has been to significantly reduce activity – see next page.

What Comes Next?

We anticipate that deal volumes will increase over the next six to nine months, driven by a combination of offensive and defensive plays.

Q3 2020 has been a difficult mix of returning optimism and hopes dashed. The hopes of finding treatment and learning to "live with the virus" have generally been positive for the longer term and the opening and closing of countries to travel has driven the optimism and then created the reality that the uncertainty brought by COVID-19 is with us for some time.

This ever-changing quarantine landscape makes it hard for customers to make plans, and the threat of a second wave only serves to add to the uncertainty. However, there have been several surveys which point to strong demand for travel (both domestic and overseas).

With uncertainty comes opportunity, and we expect to see M&A activity increase as the economy and the sector restarts, with a mix of companies facing short-term liquidity issues, and others looking to acquire strategically important businesses that may not have been available to them previously.

Travel Update – M&A Overview

Q2 2020 has seen the lowest volume of completed deals over the past five years and is below the same period in 2019, which was impacted by uncertainty resulting from Brexit.

Transactions that had launched going into March 2020 have largely been paused, and there has been limited accelerated M&A to date with the furlough and government loan schemes reducing the impact for those that are eligible.

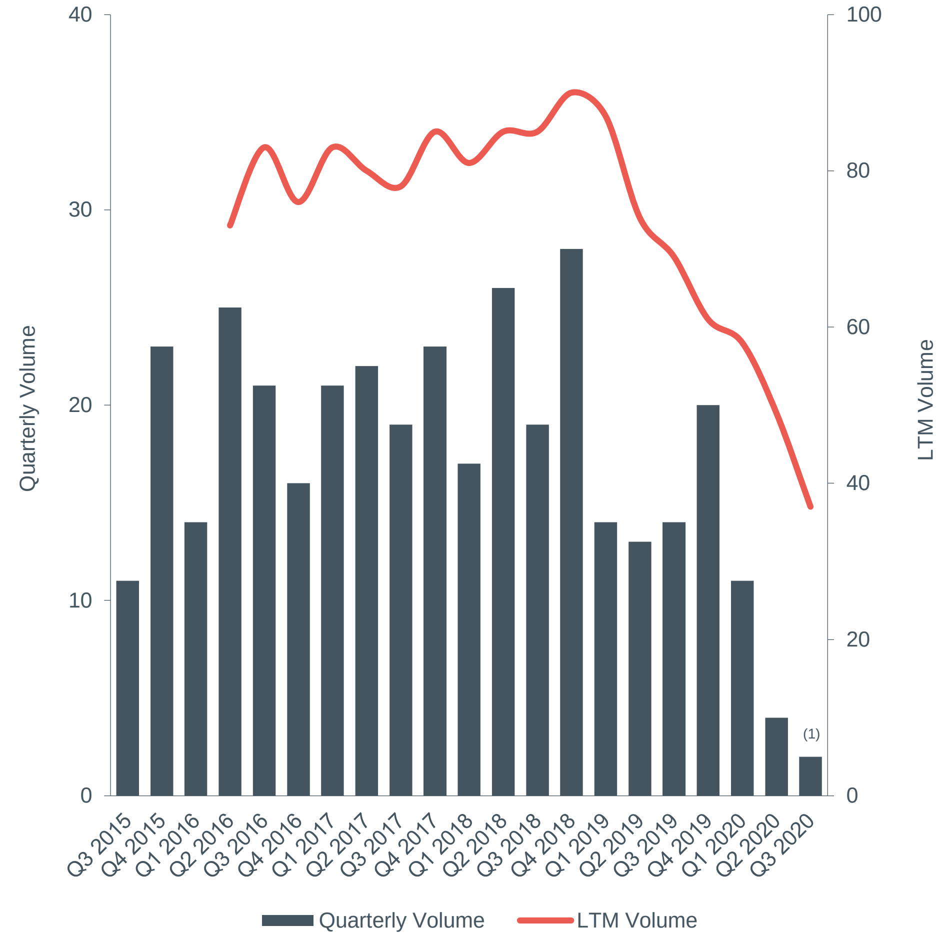
Only a handful of deals were announced in Q2 2020 and Q3 2020, and only a few of these deals would fall into the definition of "traditional" M&A.

The merger of Globalia's and Barcelo's agencies was originally announced in November 2019 (competition clearance was received in May 2020) and addresses a strategic imperative on both sides to add scale; Lufthansa's bailout by the German government is a function of the crisis.

In perhaps more "traditional" deals of the quarter, Comtravo acquired BTO24 in April 2020 in a move to enhance its technology offering in the German TMC market. KKR invested in the staycation market through its acquisition of Roompot from PAI Partners in June 2020. In both instances, COVID-19 may have been a catalyst with Comtravo recognizing an accelerating shift away from offline channels whilst KKR foreseeing increased demand for domestic tourism.

Q3 2020 got off to a slow start with two deals announced in the first two months. Both seem to be of opportunistic nature with Royal Caribbean Cruises acquiring the remaining 33% stake in Silversea Cruises and Der Touristik acquiring a 50% stake in Aldiana from LMEY Investments, the previous sole owner.

European Travel M&A Volumes



Note: (1) Q3 2020 data includes deals announced between 01 July 2020 and 31 August 2020
Source: MergerMarket, D&P Intelligence

Travel M&A Update

We are seeing M&A interest and activity falling into two broad buckets: offensive and defensive. Below we explore some of the drivers and factors at play for both acquirers and targets.

- For industry players with a well-capitalized balance sheet, there will be opportunities to acquire weaker competitors.
- As restrictions relax and government support falls away, there should be opportunities to acquire at attractive valuations though we expect attractive valuation will not be sufficient to persuade a buyer; the target will have to be such that they would have bought it irrespective of COVID-19.

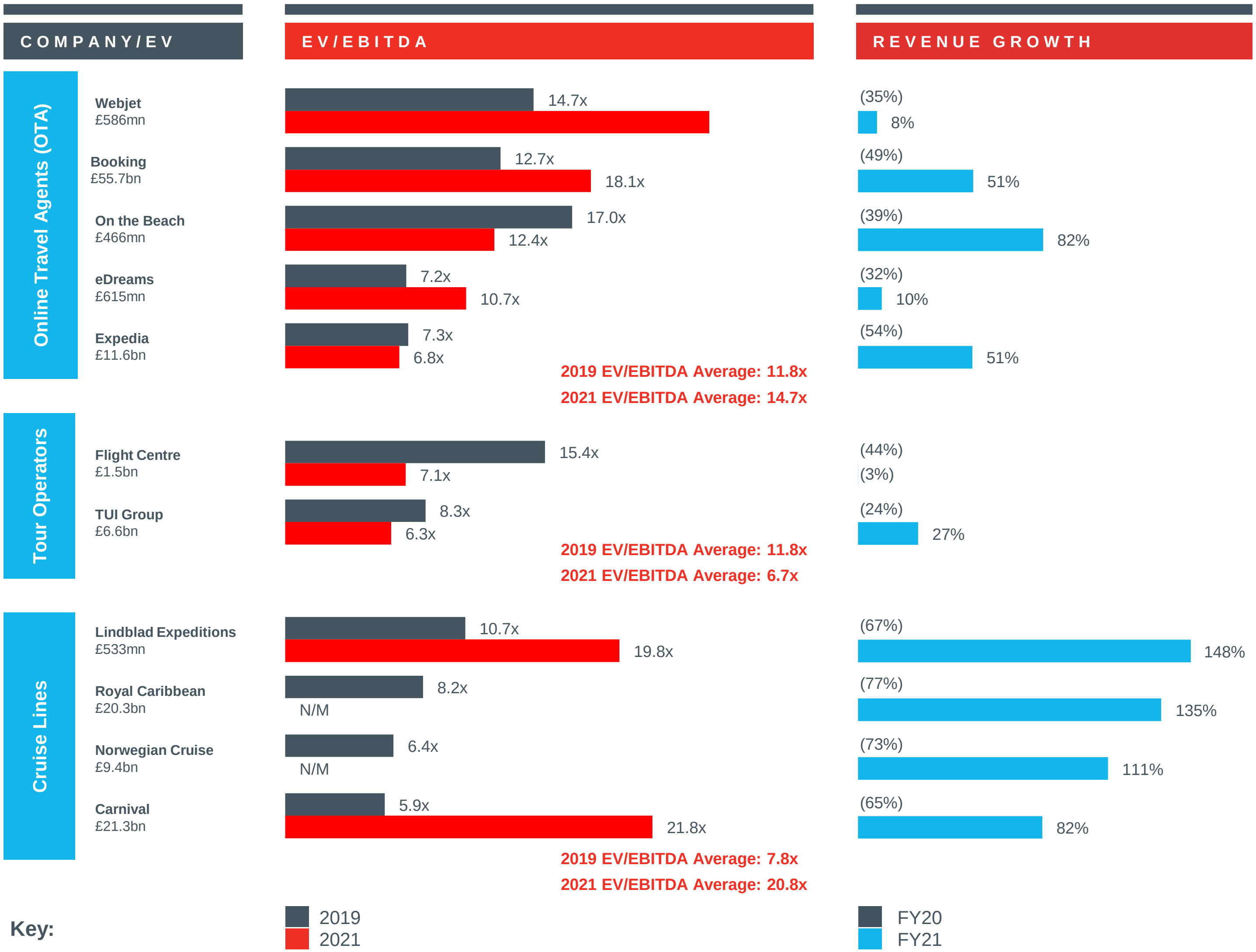
- The challenges of COVID-19 will have affected different teams in different ways. Some might decide that priorities have changed and exiting is now on the agenda, whilst some might find that financial stress is sufficient that they have no option but to seek a larger partner.
- Well-funded players should revisit those strategically attractive businesses that have not historically been open to a conversation.

- As the market begins to open up, many operators may find that this adds to the stress on their business.
- If consumers do not travel in the required volumes, already stressed margins will be tested further, and with government support schemes falling away, any further outbreaks or impacts from the virus will cause issues through the supply chain.

- For some, the crisis will be an opportunity to reposition their portfolios, dispose of non-core operations and allow management teams to focus on higher priority businesses.
- For others, non-core disposals may be critical in raising short-term liquidity, and we expect to see portfolio reviews leading to several corporate carve-outs.

Valuation Update

Optimism varies by sub-sector.



Observations

- On the whole, quoted valuations are performing well considering the backdrop. Current year (2020 multiples) are abnormally high due to the impact on the current year trading and we have used 2021 as an indicator of anticipated recovery instead.
- OTAs (on average) continue to trade on multiples above 10x EBITDA both on a historical and forecast basis. The outlook is mixed with some expected to trade ahead of 2019 in 2021, whilst others are expected to take longer to recover. The picture is similar for the Tour Operators with TUI Group expected to exceed its 2019 performance during 2021.
- The outlook for cruise operators is less optimistic, reflecting both the average age of the customer and the COVID-19-related headlines around the Diamond Princess (and others).

Notes: As at 28/08/2020, Calendarised to 31-December; SPOT exchange rate as at 28/08/2020
Source: CapitalIQ, ThomsonOne, Broker Notes

European Debt Mid-Market Update

The pandemic caused a temporary sharp reduction in activity, but sentiment has since improved in line with the wider community. However, lenders remain cautious for the sector.

H1 2020 Market Summary

In line with the wider financial markets, COVID-19 created a sudden shutdown in the European debt mid-market, and this was further evidenced by yields in the secondary market for large cap names spiking to 600-700bps, compared to a typical trading yield of 200-300bps (throughout 2019). The appetite from alternative lenders, especially in the travel sector, has been low.

Whilst the market has shown some solid signs of increased activity for new deals, the risk appetite is certainly less than it was pre-pandemic. This is further evidenced when looking across the market where we are seeing higher pricing of roughly 50-200bps and reduced leverage in the region of 0.5-1.0x EBITDA.

Some Market Themes

1 Early Requests for Payment Holidays and Covenant Waivers

Lenders are seeing approaches from borrowers for Revolving Credit Facility drawdowns, capital and interest payment holidays/rolling up and covenant waivers/renegotiations. While lenders seem amenable to repayment and covenant waivers, interest poses more difficulty. Most lenders seem keen to focus on short-term fixes only.

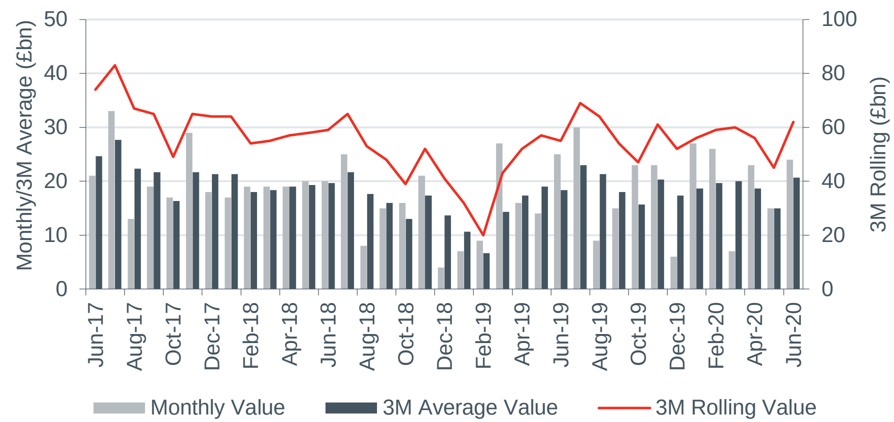
2 Leveraged Loan Market Gathers Steam and Rebounds in June

After a quiet period in April and May, activity picked up in June as sentiment improved, the secondary markets continued to move higher, and countries took steps to emerge from COVID-19-related social restrictions. Despite the increased activity in the latter part of the quarter, Q2 2020 ended with deal flow down dramatically from Q1 2020 levels.

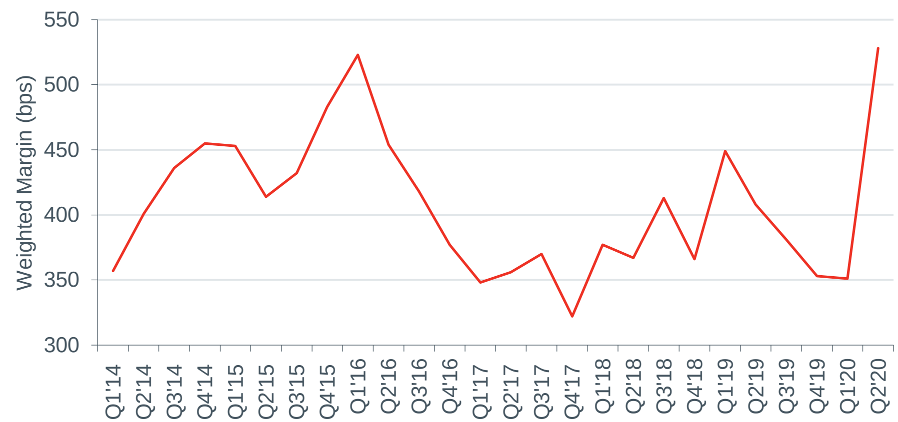
3 Travel and Leisure Remain Difficult

Travel and leisure remain challenging, with most deals being rescue financing opportunities to strengthen balance sheets. In these instances, companies are looking to either restructure or put in place financing package to ensure the business can trade through an extended period of little or no travel.

Leveraged Loans Bounce Back in June but Still Comparatively Lower



Quarterly Weighted Margin Sharply Up in Q1 2020



Source: Debtwire, European Monthly Insights Report, Q2 2020 European Leveraged Insights

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