CASE STUDY

VALUATION MASTER CLASS

by

A.Stotz INVESTMENT RESEARCH

Can **Carnival** sail safely through the **hurricane**?

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What's interesting about Carnival is that its debt has swollen by 200% compared to pre-pandemic level

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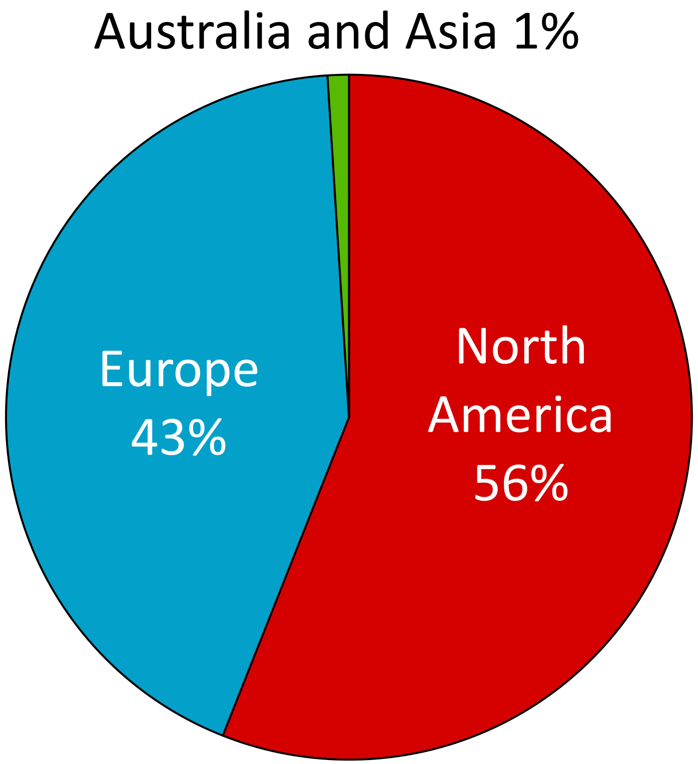
The world's largest cruise operator with 91 ships

Revenue by segment

Passenger tickets
(operates under 10 brands)
52%

Onboard services
(beverages, entertainment and dining
48%

Revenue by geographic areas



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External events caused Carnival to struggle

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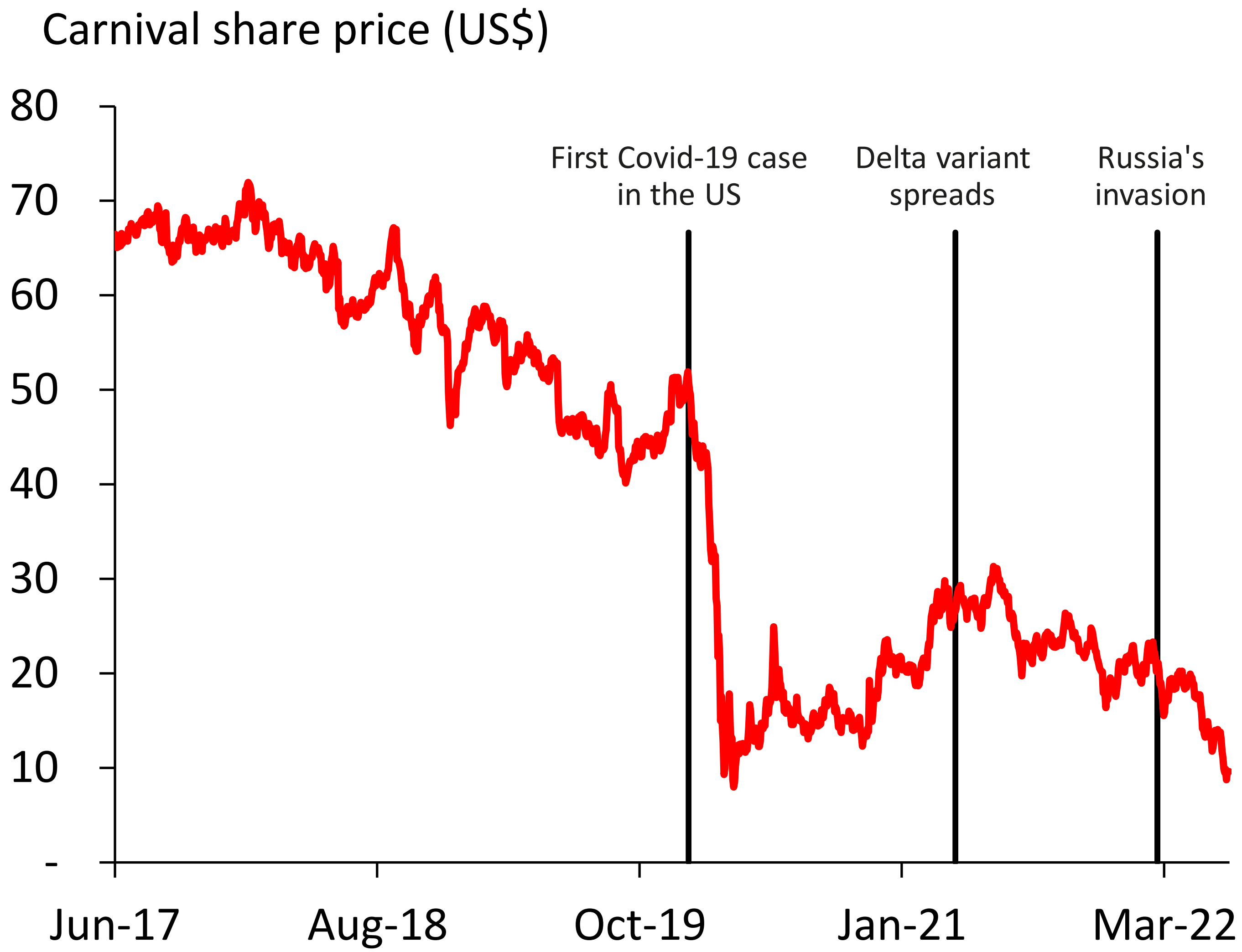

- Carnival continues to face a tough recovery
  - **Due to the pandemic it had to stop its operations, while costs remained high**
  - **On top of that, people might continue to avoid large crowds during holidays**
- The outbreak of the Russian war led to additional cost pressures
  - **Fuel price have surged massively, which should result in further net losses during 2Q22 and onwards**

Sources: A. Stotz Investment Research, Refinitiv

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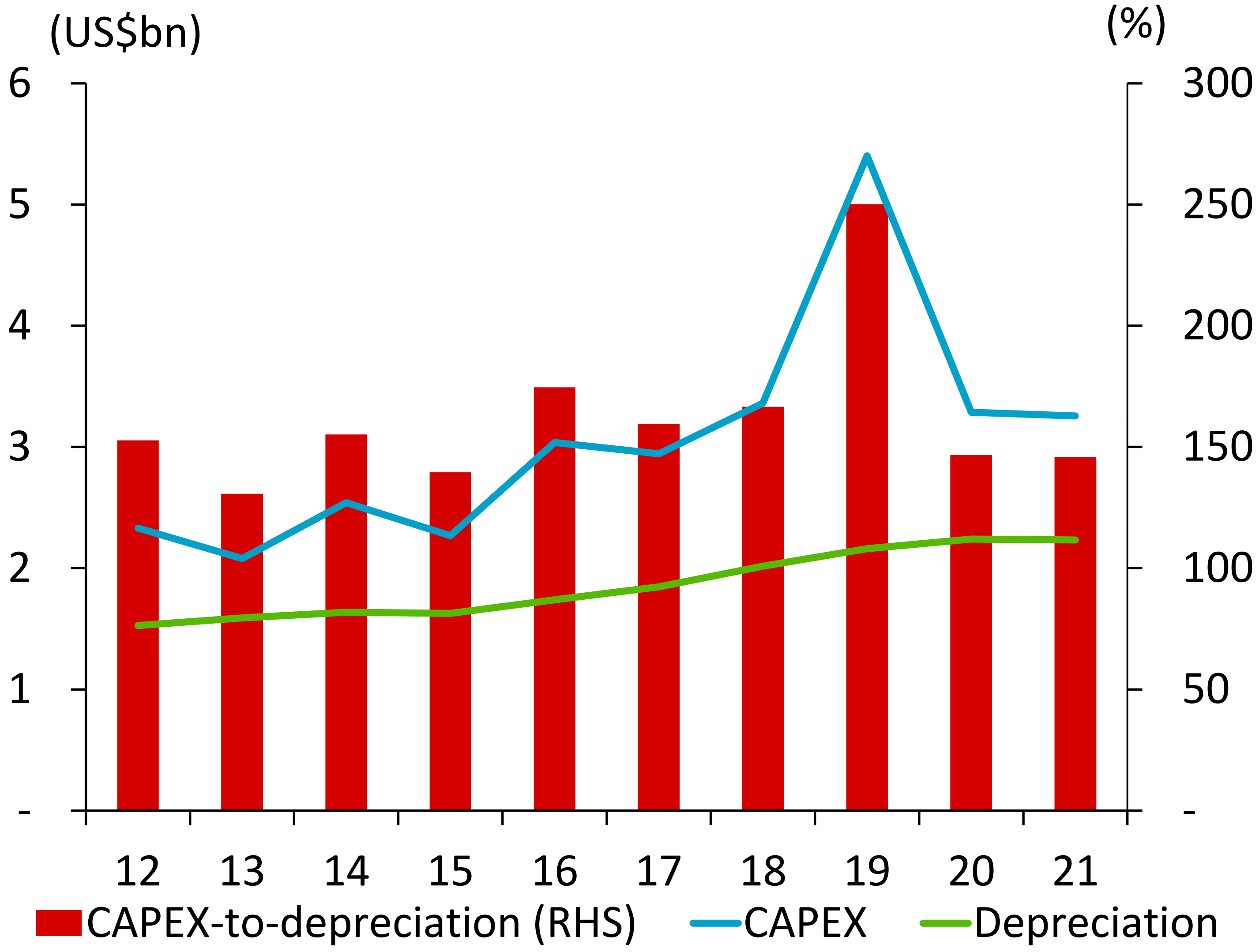
The business is very capital intensive



- In the past, CAPEX-to-depreciation ratio has averaged around 150%
  - **Both maintaining its current fleet and building larger ships require a massive amount of funding**
- In 2020 and 2021, the company faced net losses
  - **Hence, currently there is no way to fund its CAPEX internally**
  - **The company was forced to take on a huge amount of debt to keep its operations alive**

Sources: A. Stotz Investment Research, Refinitiv

Accumulation of debt could be a burden for the future

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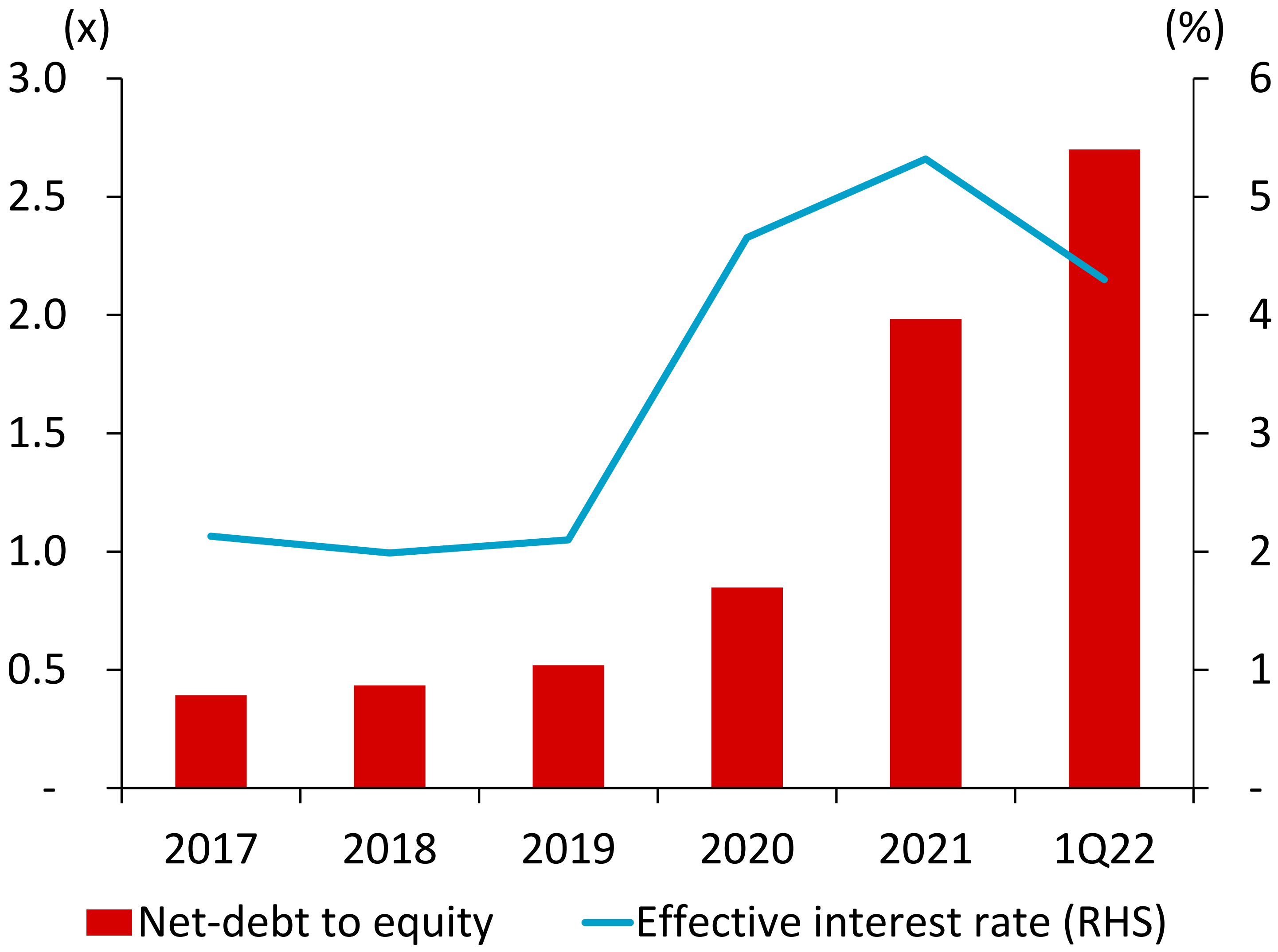

- Carnival's net debt has swollen to over 2.7x, which we consider very high leverage
  - **Given the CAPEX requirements, there is not much of the operating cash flow left to repay its debt quickly**
- Plus, its lenders require a higher interest rate on the debt, increasing the interest burden for the company

Sources: A. Stotz Investment Research, Refinitiv

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NOTE 5 — Debt

(in millions)	Maturity	Rate (a) (c)	November 30, 2021	November 30, 2020
Secured Debt				
Notes				
Notes	Apr 2023	11.5%	$ —	$ 4,000
Notes	Feb 2026	10.5%	775	775
EUR Notes	Feb 2026	10.1%	481	508
Notes	Jun 2027	7.9%	192	192
Notes	Aug 2027	9.9%	900	900
Notes	Aug 2028	4.0%	2,406	—
Loans				
EUR fixed rate	Jul 2024 – May 2025	5.5 – 6.2%	98	136
EUR floating rate	Jun 2025 – Oct 2026	EURIBOR + 2.7 – 3.8%	951	1,026
Floating rate	Jun 2025 – Oct 2028	LIBOR + 3.0 – 3.3%	4,137	1,855
Total Secured Debt . .			9,939	9,393
Unsecured Debt				
Revolver				
Facility	(b)	LIBOR + 0.7%	2,790	3,083
Notes				
EUR Notes	Feb 2021	1.6%	—	429
EUR Notes	Nov 2022	1.9%	622	658
Convertible Notes	Apr 2023	5.8%	522	537
Notes	Oct 2023	7.2%	125	125
Notes	Mar 2026	7.6%	1,450	1,450
EUR Notes	Mar 2026	7.6%	566	598
Notes	Mar 2027	5.8%	3,500	—
Notes	Jan 2028	6.7%	200	200
Notes	May 2029	6.0%	2,000	—
EUR Notes	Oct 2029	1.0%	679	718
Loans				

★ Recent issued debt comes at a high cost

- **Some contracts require the company to pay more than 10% interest rate**
- **Higher interest burden to drag on the net margin in the future**

Accumulation of debt could be a burden for the future

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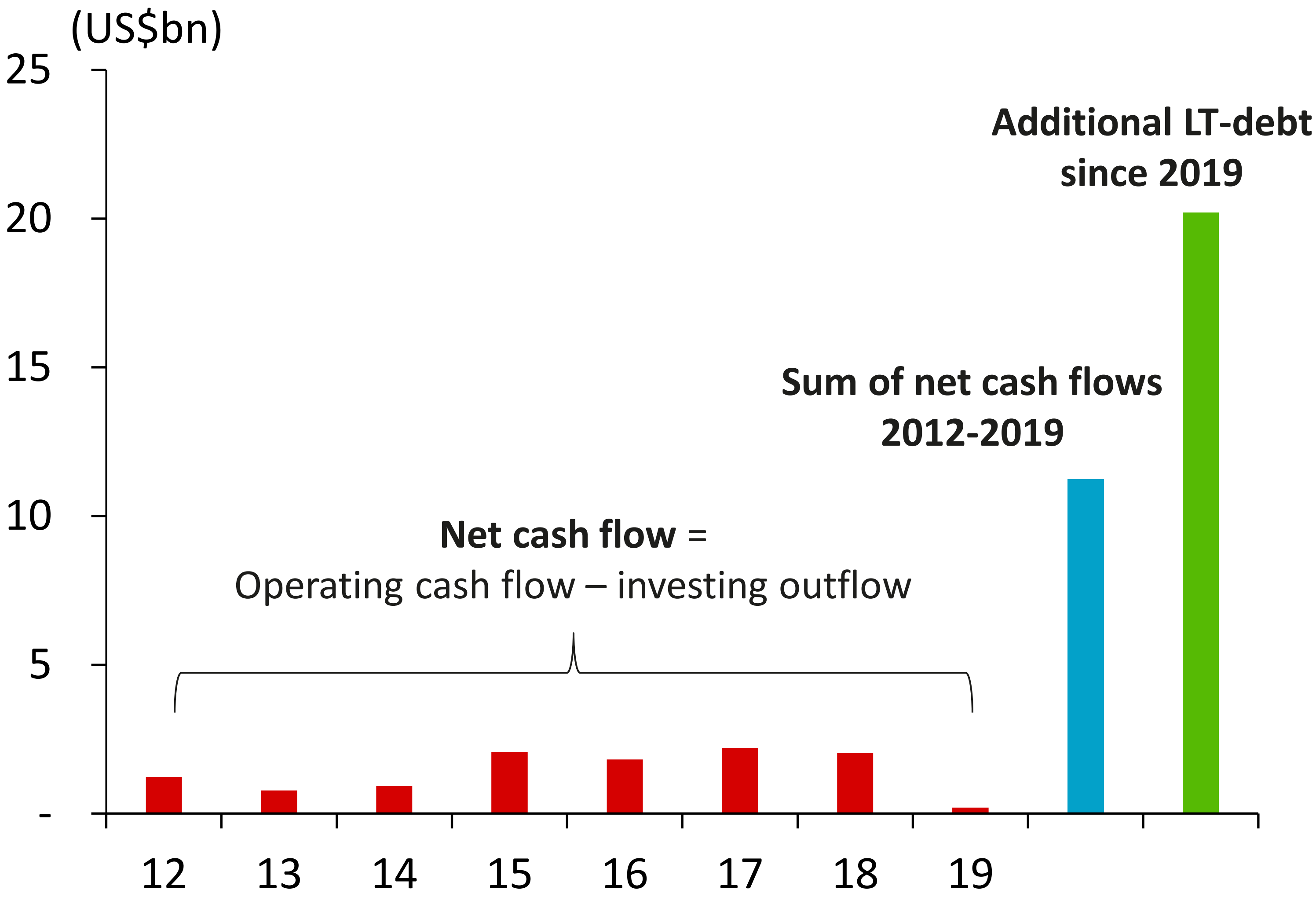
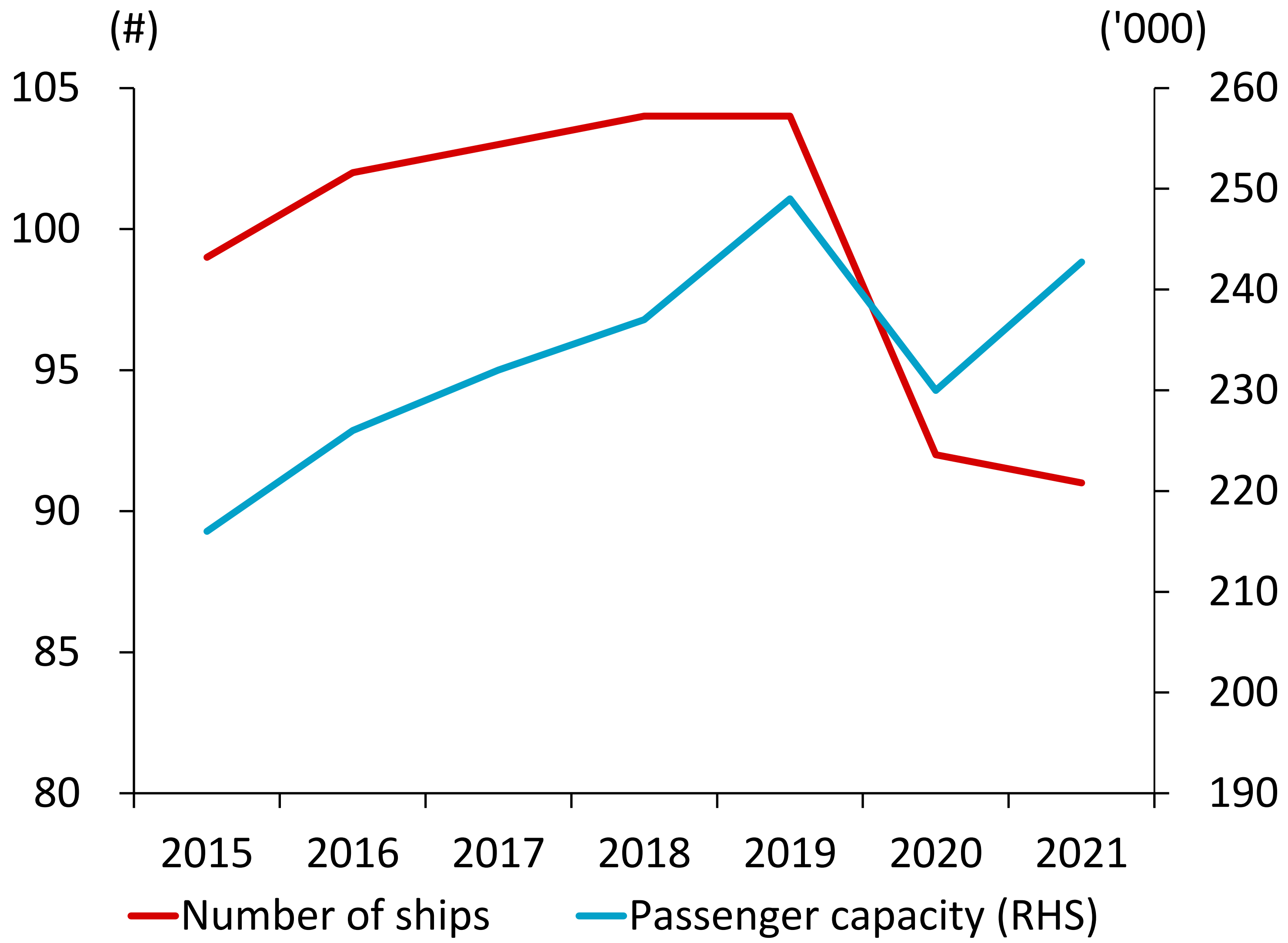


★ To measure the ability to repay its debt, we can calculate the net cash flow, which is the remainder of the operating cash flow after deducting all investing outflows
  - **In the 8 years prior the pre-pandemic, Carnival generated in total US$11bn in net cash flow**
  - **This is just half of the additional US$20bn in long-term debt**
  - **Hence, it will probably take the company very long time to repay its debt**

Sources: A. Stotz Investment Research, Refinitiv

Cost pressures require restructuring of its fleet



- During the pandemic, Carnival has sold around 10% of its fleet size in its attempt to get rid off inefficient ships
- The future focus will be on the construction on larger and more efficient ships to keep costs low

Sources: A. Stotz Investment Research, Refinitiv

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Rumors to sell one of its brands showcases how much it struggles

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TRANSPORTATION

Saudi fund in early talks to potentially buy Carnival’s ultra-luxury Seabourn brand

PUBLISHED TUE, MAY 24 2022•4:03 PM EDT

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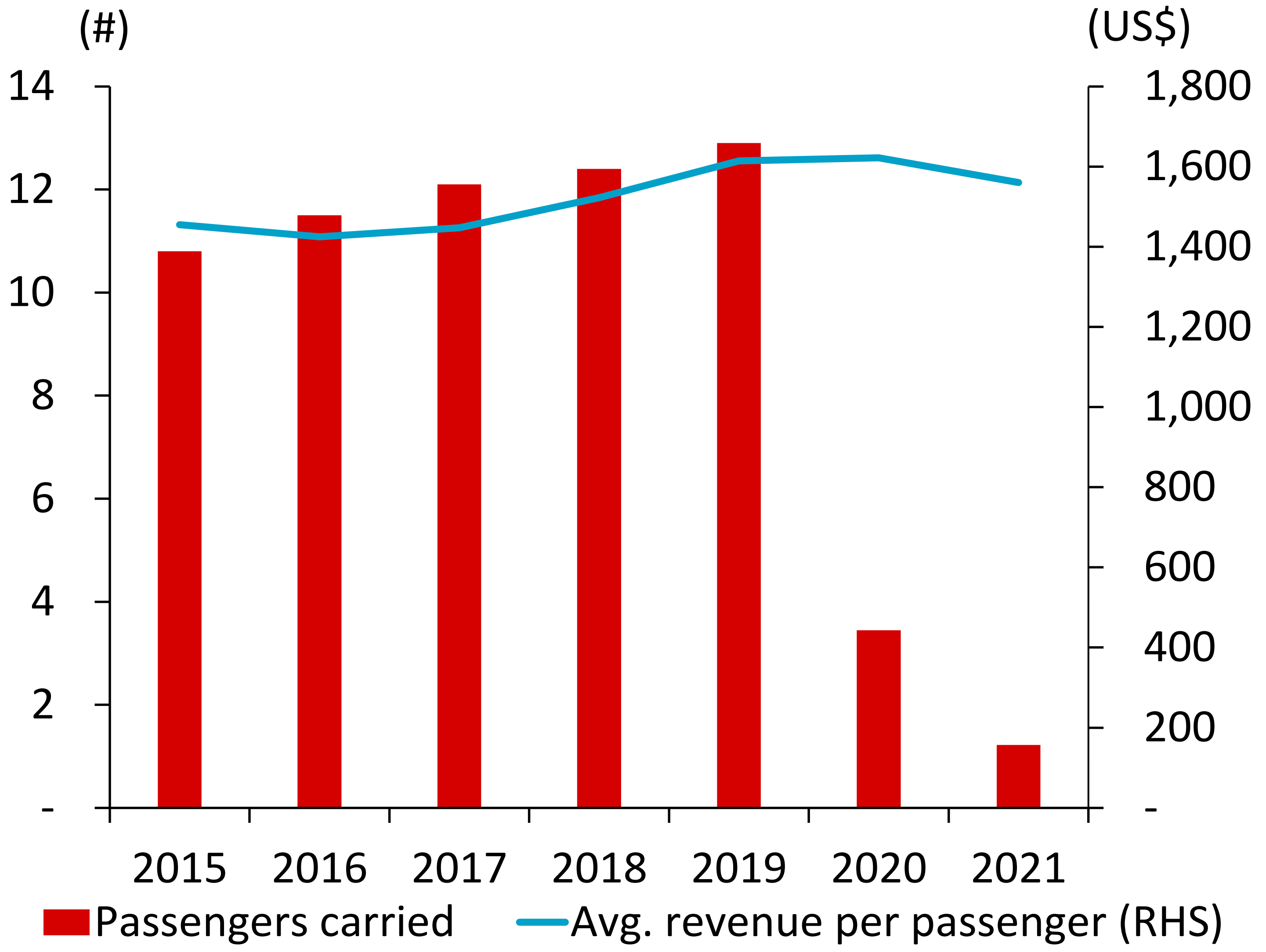
Struggling With Gargantuan Debt of $35,000,000,000 and Still Evolving COVID-19 Pandemic, Carnival In Discussions to Sell Seabourn Brand

- Recent news published the rumor that Carnival considers the sale of its luxury brand Seabourn to the Saudi Sovereign Wealth fund, which holds a 5% stake in the company
  - **High CAPEX requirements and the pressure to serve its debt might require the company to reduce its fleet further**
  - **It could be a desperate attempt to raise further capital to survive**

Carnival needs its passengers to return urgently



- ★ The main driver of its revenue constitutes the number of passengers
  - **The average revenue it generates per passenger has remained more and less flat**
- ★ While the company records increased bookings, it is still far away from returning to full occupancy

Sources: A. Stotz Investment Research, Refinitiv

How does consensus access Carnival?

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Recommendation	Mar-22	Apr-22	May-22	Current
Strong buy	4	3	3	3
Buy	3	3	3	3
Hold	10	11	11	12
Sell	3	4	4	4
Strong sell	-	-	-	-
Average score	**2.6**	**2.8**	**2.8**	**2.8**

Price target	Mar-22	Apr-22	May-22	Current
Median	25	23	22	21
Mean	17	26	24	22

- Most analysts stay cautious and have issued a HOLD
- Over the past 4 months, analysts consistently decreased their target price
  - **Still, the median target price still sees a 120% upside compared to the current share price**

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