PEFINDO affirms "BBB+" rating to PT Garuda Indonesia (Persero) Tbk

PEFINDO has affirmed its "BBB+" ratings on PT Garuda Indonesia (Persero) Tbk (GIAA) and its outstanding Bond I 2013, despite the Company's weak financial performance in 1H2017. GIAA booked a net loss of USD281.9 million in 1H2017 due to a weaker seasonal demand amid intense competition and its participation in the government's tax amnesty program that led to a breach in its global sukuk terms as well as other conditions as stated in the Company's short-term and long-term loans agreements. On August 18, 2017, GIAA obtained a consent to amend certain terms on its USD500 million global sukuk due in 2020. Affirmation on ratings is backed by our expectation that GIAA's financial performance will improve in the upcoming quarters following several short-term strategies that are underway, including contract renegotiation with lessees, manufacturers, suppliers, and service providers, as well as routes optimization. These initiatives, are expected to reduce costs and hence, easing the pressure on passenger yields. Excluding the one-off costs from the tax amnesty program and a legal fine concerning GIAA’s participation on price fixing by the Australian Competition and Consumer Commission (ACCC), its operating loss in the 2Q2017 was USD56.9 million, a significant improvement compared to operating loss in 1Q2017 of USD112.7 million. The outlook for the Company's corporate rating is "stable".

An obligor rated "BBB+" has an adequate capacity to meet its long-term financial commitments relative to that of other Indonesian obligors. However, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitments.

The ratings reflect our view on the strong support provided by the government to the Company, GIAA’s strong business position in the domestic airline industry, and its comprehensive route network. However, the ratings were constrained by GIAA’s high financial leverage, intense competition which weakened its profitability, and its participation in the highly cyclical airline industry.

We see a very limited likelihood the rating will improve over the next 12-18 months. Nonetheless, the rating could be raised if GIAA is able to improve its financial profile substantially, indicated by improvement in its profitability and increased debt repayment, resulting in its adjusted leverage ratios to reduce to less than 5.0x on a prolonged basis. However, we could lower the rating if we view that there is a reduction in government support, such as through material divestment of the government’s ownership. We could also lower the rating if GIAA’s financial profile deteriorates stemming from weaker pricing power, impaired demand environment, a significant and sustained loss of market share, and its inability to effectively hedge exposure related to rise in fuel prices. The rating could also be under pressure if it incurs larger-than-expected debt-funded capital expenditure without being compensated with stronger revenue.

Originally founded in 1949, GIAA is the national flag carrier of Indonesia, providing air passenger, air cargo, and airline related services, with its main hub at the Soekarno-Hatta International Airport, near Jakarta. GIAA operates a full-service carrier (FSC) through its main brand Garuda Indonesia, and low-cost carriers (LCC) through its wholly-owned subsidiary PT Citilink Indonesia. The maintenance, repair, and overhaul (MRO) of its aircrafts are also carried out by its subsidiary, PT Garuda Maintenance Facility Aero Asia (GMFAA), Ground services, reservations and ticketing, and in-flight catering services, are provided by GIAA also through its principal subsidiaries. As of June 30, 2017, the Government of Indonesia owned 60.5% of GIAA’s shares, followed by Trans Airways (24.6%), and public including key management of the Company (14.9%).

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