

CEA (670.HK)

Brief review of its positive profit alert

Hong Kong | Air | Update Report

9 February 2015

• A positive profit alert, expecting to record a yoy increase of 40%-60% in net profit for 2014, namely EPS between RMB 0.275-0.3144.

• We predict that the contribution of the fuel oil cost reduction factor to the performance of CEA in the fourth quarter turning to positive may reach 40%.

• The capacity input of CEA was the most conservative among the big-three carriers, the growing rate of the amount of passenger traffic of CEA was also the lowest.

• Southeast Asia routes were in the downturn and the recovery of Japan and Europe routes was weaker than expected, both of which had the most obvious adverse effects on CEA's international routes.

• Shanghai Disney Park is opening soon, CEA will undoubtedly become the biggest beneficiary. In addition, the attempts of CEA in the fields of budget airline, E-commerce, freight logistics and so on also provide the space for the company's performance improvement.

Accumulate (Maintain)

CMP HKD3.65

TARGET HKD3.95 (+8%)

COMPANY DATA

O/S SHARES (MN) :	12674
MARKET CAP (HKD MN) :	15305
52 - WK HI/LO (HKD):	4.2/ 2.28

SHARE HOLDING PATTERN, %

China Eastern Air Group :	43.64
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PRICE PERFORMANCE, %

	1 个月	3 个月	1 年
CEA	-4.05	21.47	54.69
HIS index	-9.5	16.75	39.09

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY13	FY14E	FY15E	FY16E
Net Sales	88245	91823	95875	106984
Net Profit	2373	3556	4991	7612
EPS, CNY	0.20	0.28	0.39	0.60
P/E, x	14.3	10.3	7.3	4.8
BVPS, CNY	2.12	2.42	2.62	2.94
P/BV, x	1.4	1.2	1.1	1.0
DPS (CNY)	0.00	0.01	0.03	0.05
Div. Yield (%)	0%	0.3%	1.0%	1.7%

Source: Company reports, Phillip Securities Est.

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The performance of 2014 is predicted to increase by 40-60%

CEA has issued its performance predicted increase report: according to the Chinese Accounting Standards, it is predicted that until 2014, the annual net profit has increased by 40-60% every year. The company obtained RMB 2.376 billion of net profit in 2013, and the corresponding net profit should be between RMB 3.326 billion and RMB 3.8 billion in 2014, namely EPS would stand between RMB 0.275-0.3144. Because the results of the first three quarters of CEA have actually decreased on yoy basis, meaning that CEA has made a profit of RMB 1.268-1.742 billion during the fourth quarter comparing with the loss of RMB 1.036 billion during the same period in 2013, turning loss into gain. There are three main reasons why the company will have a better performance:

- 1) The drop of the price of fuel
- 2) The raise of operation and management efficiency
- 3) The adjustment of welfare policies for employees

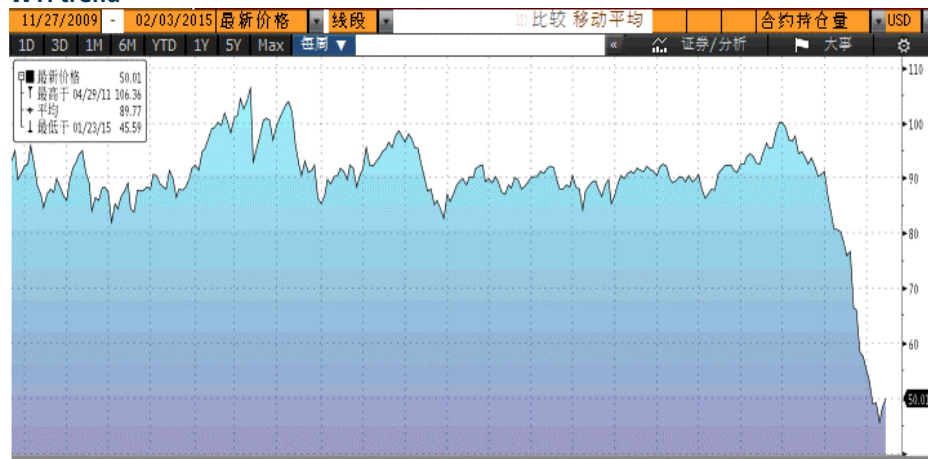
Investment Thesis

We revised EPS expectation of the Company to RMB 0.28, 0.39, 0.60 of 2014/2015/2016. And we accordingly revised the target price to 3.95, respectively 11/8/5x P/E and 1.3/1.2/1.1x P/B for 2014/2015/2016. We reiterate "Accumulate" rating.

The drop of fuel price is the most important reason

Since July 2014, the international crude oil price has dropped continuously and seriously from 100 dollars per bucket to around 50 dollars per bucket, with a decrease of 40-50%. Viewing from the data of 2013, the fuel oil cost of CEA was RMB 30.68 billion, accounting for 38.2% of the total operation cost. In H1 of 2014, the fuel oil cost of the company was RMB 14.95 billion, accounting for 38.07%. The big drop of oil price cost has an obvious impact on improving the performance. We predict that the contribution of the fuel oil cost reduction factor to the performance of CEA in the fourth quarter turning to positive may reach 40%.

WTI trend



Source: Bloomberg, Phillip Securities Hong Kong Research

Operation efficiency has been raised after controlling capacity input

The capacity input of CEA was the most conservative among the big-three carriers in 2014. Its ASK only increased by 5.57% yoy, while that of Air China and China Southern Airlines achieved double-digit yoy growth ratio, 10.2% and 12.3% respectively. However, what was corresponding to this was that the growing rate of the amount of passenger traffic of CEA was also the lowest. The increase of the passenger traffic and the number of passengers was 6% and 5.9% respectively on yoy basis. And the increase of passenger volume of domestic, international and regional routes was 6.5%, 4.4% and 9.5% respectively on yoy basis. Its increase in international routes was significantly slower than that of 14.6% of Air China and 20.2% of China Southern Airlines. We think it was mainly determined by the international route structure characteristics of CEA. Southeast Asia routes were in the downturn and the recovery of Japan and Europe routes was weaker than expected, both of which had the most obvious adverse effects on CEA.

On the other hand, benefited from the control of the capacity, the P L/F of CEA was the only one achieving the positive growth ratio among the big-three carriers, with the yoy increase of the overall P L/F of 0.33ppts in 2014, reaching 79.5%, while that of Air China and China Southern Airlines decreased respectively by 0.9 ppts and 0.03 ppts to 79.9% and 79.4%.

To be benefit from the coming Disney and layout of low cost air in the future

As the world's sixth Disney theme park, Shanghai Disney Park is opening soon, which is expected to bring at least 10 million passengers in 2016, among which, the newly added airline passengers are expected to reach 0.4 million. With the subsequent follow-up development advancing, the newly added airline passengers will increase to 1.2 million/year. With more than 40% market share in Shanghai, CEA will undoubtedly become the biggest beneficiary. Chinese United Airlines owned by the company announced to transform into a budget airline, which we think, is of great significance, helping CEA to obtain the domestic leisure and tourism passengers, who are more sensitive to the prices. In the trend of the competition normalization of High-speed Rail and the rapid development of the leisure tourism, the early layout of low cost airlines lays the foundation for the company to develop the subdivision sub-markets. In addition, the attempts of CEA in the fields of E-commerce, freight logistics and so on also provide the space for the company's performance improvement.

RMB/USD trend



Source: Bloomberg, Phillip Securities Hong Kong Research

Peer Comparison

Ticker	Name	Mkt Cap (HKD)	BEst P/B	BEst P/E 2FY	BEst P/E 1FY	BEst P/E 2FY	BEst EV/BEst	ROA P/B	ROA LF
AUD (2 securities)									
QAN AU Equity	QANTAS AIRWAYS LTD	31334	1.8	1.4	10.9	6.6	4.3	1.9	-15.2
VAH AU Equity	VIRGIN AUSTRALIA HOLDINGS	9390	1.3	1.2	N/A	23.7	9.2	1.5	-7.7
CNY (3 securities)									
600115 CH Equity	CHINA EASTERN AIRLINES CO-	69049	2.4	2.1	34.2	16.1	9.0	2.4	1.2
600029 CH Equity	CHINA SOUTHERN AIRLINES CO	53118	1.4	1.2	32.6	13.6	7.2	1.5	0.4
600221 CH Equity	HAIRAN AIRLINES CO-A	47743	N/A	N/A	N/A	N/A	N/A	1.4	1.6
EUR (1 security)									
AF FP Equity	AIR FRANCE-KLM	20051	1.9	1.6	N/A	12.0	5.6	N/A	-6.8
EIP (1 security)									
RYA ID Equity	RYANAIR HOLDINGS PLC	119018	3.7	3.1	16.4	14.5	9.4	3.3	8.5
GBP (2 securities)									
IAG LN Equity	INTL CONSOLIDATED AIRLINE-I	125652	3.2	2.6	17.4	11.5	6.0	3.4	3.3
EZJ LN Equity	EASYJET PLC	80532	2.8	2.4	13.1	11.5	8.0	3.2	10.1
HKD (4 securities)									
670 HK Equity	CHINA EASTERN AIRLINES CO-	69050	1.3	1.1	15.5	8.0	8.7	1.4	1.2
753 HK Equity	AIR CHINA LTD-H	109551	1.3	1.1	20.4	10.5	10.4	1.4	1.3
293 HK Equity	CATHAY PACIFIC AIRWAYS	68370	1.1	1.0	19.7	11.6	7.8	1.1	1.8
1055 HK Equity	CHINA SOUTHERN AIRLINES CO	53119	0.9	0.8	17.3	7.7	7.1	0.9	0.4
INR (1 security)									
JETIN IN Equity	JET AIRWAYS INDIA LTD	7193	N/A	N/A	N/A	10.1	14.6	N/A	-23.3
JPY (1 security)									
9202 JP Equity	ANA HOLDINGS INC	73398	1.4	1.3	26.5	21.2	6.8	1.4	1.7
KRW (2 securities)									
003490 KS Equity	KOREAN AIR LINES CO LTD	19405	1.3	1.1	N/A	9.8	9.0	1.1	-1.1
020560 KS Equity	ASIANA AIRLINES	11199	2.0	1.7	N/A	10.8	11.5	1.8	-1.8
MYR (1 security)									
AIRA MK Equity	AIRASIA BHD	16644	1.4	1.2	15.4	9.0	11.3	1.5	4.2
SGD (1 security)									
SIA SP Equity	SINGAPORE AIRLINES LTD	82091	1.1	1.1	37.4	19.9	5.2	1.1	0.9
THB (1 security)									
THAI TB Equity	THAI AIRWAYS INTERNATIONAL	7638	0.7	0.7	N/A	107.3	18.6	0.7	-4.7
TWD (2 securities)									
2618 TT Equity	EVA AIRWAYS CORP	21575	2.0	1.7	60.3	13.1	9.3	2.0	-0.3
2610 TT Equity	CHINA AIRLINES LTD	19063	1.6	1.4	N/A	10.5	9.6	1.6	-1.8
USD (4 securities)									
DAL US Equity	DELTA AIR LINES INC	301849	2.5	2.0	9.4	8.1	5.0	3.2	20.1
AAL US Equity	AMERICAN AIRLINES GROUP INC	270978	4.2	2.4	4.6	5.3	4.5	17.3	6.7
LUV US Equity	SOUTHWEST AIRLINES CO	234373	3.2	2.6	13.0	12.1	6.0	4.5	5.8
UAL US Equity	UNITED CONTINENTAL HOLDING	198560	3.2	1.9	6.4	6.3	4.3	6.6	3.3

Source: Company, Phillip Securities Hong Kong Research

Financials

FYE DEC	FY11	FY12	FY13	FY14F	FY15F	FY16F
Valuation Ratios						
P/E (X), adj.	7.3	10.7	14.3	10.3	7.3	4.8
P/B (X)	2.0	1.6	1.4	1.2	1.1	1.0
Dividend Payout Yield (%)	0.0%	0.0%	0.0%	3.6%	7.6%	8.3%
Dividend Yield (%)	0.0%	0.0%	0.0%	0.3%	1.0%	1.7%
Per share data (RMB)						
EPS, reported	0.41	0.27	0.20	0.28	0.39	0.60
EPS, adj.	0.41	0.27	0.20	0.28	0.39	0.60
DPS	0.00	0.00	0.00	0.01	0.03	0.05
BVPS	1.52	1.79	2.12	2.42	2.62	2.94
Growth & Margins (%)						
Growth						
Revenue	12.1%	2.1%	3.5%	4.1%	4.4%	11.6%
EBIT	-25.8%	4.8%	-63.4%	181.0%	34.4%	40.4%
Net Income, adj.	-7.7%	-32.9%	-22.8%	49.9%	40.4%	52.5%
Margins						
EBIT margin	6.5%	2.1%	3.2%	3.4%	4.8%	7.3%
Net Profit Margin	5.5%	3.6%	2.7%	3.9%	5.2%	7.1%
Key Ratios						
ROE (%)	28.2%	16.5%	10.1%	13.8%	16.5%	21.9%
ROA (%)	4.2%	2.6%	1.8%	2.5%	3.3%	4.8%
Income Statement (RMB mn)						
Revenue	83,465	85,253	88,245	91,823	95,875	106,984
Operating expenses	(79,292)	(82,745)	(89,394)	(90,319)	(92,771)	(101,733)
Profit from operations	4,173	4,228	1,576	4,523	6,080	8,559
Non-operating income/expense	106	133	65	90	122	150
Profit before tax	4,841	3,137	2,217	3,888	5,423	8,252
Tax	(264)	(207)	(124)	(225)	(293)	(446)
Profit for the period	4,576	2,929	2,093	3,662	5,130	7,807
Minority interests	(1)	142	280	(106)	(139)	(195)
Total capital share	11,257	11,277	12,674	12,674	12,674	12,674
Net profit	4,576	3,071	2,373	3,556	4,991	7,612

Source: PSR

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Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within \pm 5% from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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