

Air China (753.HK)

Buy Opportunity Arose in Slack Season

Hong Kong | Air | Update Report

25 MAY 2016

Net income in 2016Q1 Surged by near to 50%

According to Air China's First Quarterly Report 2016 (China Accounting Standards), it recorded a revenue of RMB26.39 billion in 1Q16, up 4.38% Y-o-Y. Its net profit attributed to the parent company rose by 44.8% to RMB2.33 billion, and EPS was RMB0.20. More rapid growth in revenue than that in oil cost, with less input in marketing and financial expenses mainly contributed to such substantial increase.

FY2015 Results Soared by 83.7%

A plunge in the crude oil cost led to an annual growth of 83.7% in attributable net income in 2015, though the total revenue increased only by 4%. Meanwhile, over RMB5 billion exchange loss caused by renminbi's depreciation offset part of the profit. Excluding that offset, the company could have registered a 182% year-on-year increase in final results.

Aviation data Maintained Steady Growth

In 2016, Air China continued to accelerate the deployment of transport capacity for international routes. International ASK in the first four months of 2016 had grown by 26% year-on-year, leading to a 25.7% Y-o-Y increase in international passenger turnover, far higher than 4.6% and 4% Y-o-Y increase respectively in its domestic routes. Remaining stable on the whole, Passenger Load Factor dropped by 0.3ppts to 79.9%.

Direct selling continued to enjoy a bigger share. Throughout the first quarter, sales on the official website have reached 26.6% proportion of its total ticket booking, representing a Y-o-Y increase of 12.8 percentage points. Additional four jets were bought to join a fleet of 594 airplanes in total during 2016Q1.

The management of Air China made it clear that they will carry forward the strategy of hub network and innovation of business pattern to strengthen service competitiveness with respect to digital and Internet-based service. In the meantime, they will optimize the debt structure and increase direct selling for more tangible gains.

Valuation & Investment thesis

Currently, the company is burdened with US dollar-denominated debt of 67.3%, down by 6.2 percentage points, year-on-year. The debt burden is expected to drop to 60% by the end of 2016. We hold that the two-way volatility RMB rate is becoming a notable trend, which is likely to become stable in mid-term. Since the second quarter, international oil price has climbed up by 30% compared with the first quarter, yet there was no remarkable growth compared with last year's average. We will continue to track the fuel cost since it takes a huge proportion in total cost of airlines. After the slack season of June, then will comes the traditional peak season. It is advisable to invest in the aviation sector before the slack season ends. The target price is maintained at HKD7.09, and P/E estimates 8.3x/7.2x in 2016/2017. "Buy" rating is given. (Closing price as at 23 May 2016)

BUY (upgrade)

CMP: HKD 5.36

(Closing price as at 23 May 2016)

TARGET HKD 7.09 (+32%)

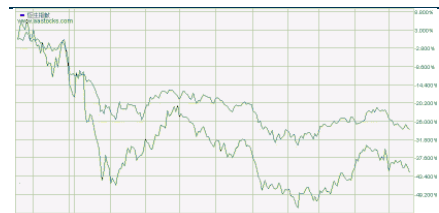
COMPANY DATA

O/S SHARES (MN) :	12294
MARKET CAP (HKD MN) :	24456
52 - WK HI/LO (HKD):	10.18/ 4.3

SHARE HOLDING PATTERN, %

China National Aviation Holding Company	53.37
Cathay Pacific Airways Limited	20.13

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY14	FY15	FY16E	FY17E
Net Sales	105965	110057	117635	123358
Net Profit	3852	7063	8836	10234
EPS, CNY	0.31	0.57	0.72	0.83
P/E, x	13.6	7.8	6.2	5.4
BVPS, CNY	4.39	4.86	5.44	6.15
P/BV, x	1.0	0.9	0.8	0.7
DPS (CNY)	0.05	0.11	0.14	0.15
Div. Yield (%)	1.2%	2.4%	3.0%	3.3%

Source: Company reports, Phillip Securities Est.

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Net profit by quarterly (100millionRMB)



Source: Company, Phillip Securities Hong Kong Research

USD/CNY trend



Source: Wind, Phillip Securities Hong Kong Research

Fuel trend



Source: Wind, Phillip Securities Hong Kong Research

Financials

FYE DEC	FY11	FY12	FY13	FY14	FY15	FY16F	FY17F
Valuation Ratios							
P/E (X), adj.	7.5	11.3	15.9	13.6	7.8	6.2	5.4
P/B (X)	1.1	1.1	1.0	1.0	0.9	0.8	0.7
Dividend Yield (%)	2.7%	1.4%	1.1%	1.2%	2.4%	3.0%	3.3%
Per share data (RMB)							
EPS, reported	0.582	0.382	0.265	0.311	0.574	0.719	0.832
EPS, adj.	0.582	0.382	0.265	0.311	0.574	0.719	0.832
DPS	0.118	0.059	0.045	0.052	0.107	0.136	0.150
BVPS	3.79	4.09	4.37	4.39	4.86	5.44	6.15
Growth & Margins (%)							
Growth							
Revenue	19.3%	3.8%	-1.3%	7.9%	3.9%	6.9%	4.9%
EBIT	-47.0%	4.3%	-43.9%	64.3%	111.6%	5.9%	8.9%
Net Income, adj.	-41.0%	-36.1%	-32.2%	18.0%	83.3%	25.1%	15.8%
Margins							
EBIT margin	8.8%	8.8%	5.0%	7.7%	15.6%	15.5%	16.1%
Net Profit Margin	7.9%	4.8%	3.3%	3.6%	6.4%	7.5%	8.3%
Key Ratios							
ROE (%)	17.23%	10.02%	6.29%	7.13%	12.39%	13.95%	14.36%
Income Statement (RMB mn)							
Revenue	95,821	99,473	98,181	105,965	110,057	117,635	123,358
Operating expenses	(92,151)	(91,064)	(94,063)	(98,708)	(94,505)	(100,825)	(104,925)
-Jet fuel cost	(34,703)	(35,640)	(33,722)	(34,542)	(24,043)	(26,327)	(27,617)
Profit from operations	6,949	8,409	4,118	7,257	15,552	16,810	18,433
Financial costs	1,767	(1,890)	(423)	(2,981)	(7,817)	(6,271)	(6,208)
Share of profits and losses of associates	1,329	391	823	859	1,620	1,372	1,372
Profit before tax	10,203	6,909	4,518	5,135	9,355	11,911	13,597
Tax	(2,241)	(1,607)	(903)	(801)	(1,846)	(2,025)	(2,311)
Profit for the period	7,962	5,302	4,368	4,334	7,509	9,886	11,285
Minority interests	421	486	351	482	446	1,050	1,051
Net profit	7,541	4,816	3,264	3,852	7,063	8,836	10,234

Source: PSR

(Financial figures as at 23 MAY 2016)

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

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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