

# Air China (753.HK)

## 18Q4 Result Beat

Hong Kong | Air | Update Report

11 April 2019

### Investment Summary

#### The 18Q4 Result Turns from Loss and the Year-round Net Profit Is Basically Flat Which Is Better than Expected

Air China reported revenues of RMB136.77 billion in 2018, up by 12.7% yoy. The net profit attributable to parent company was RMB7.34 billion, up by 1.3% yoy. Its EPS was RMB0.53 basically, down by 1.85% yoy due to the dilution of A share's private placement. Dividend per share was RMB0.1033, with the dividend rate of 19.5%.

The result of Air China in the 2018Q4 was better than expected, turning from a loss of RMB1.04 billion in the same period last year to a profit of RMB399 million. It was the main force to stop the downs and maintain the flat in the whole year (the net profit of the company in the first three quarters fell 16% yoy). We believe the main reason making the fourth-quarter result better than expected are:

- 1) Revenue: due to the market-oriented increase in ticket prices for key routes and the company's optimization strategy for capacity allocation, the Air China's RPK increased by 6% in the fourth quarter yoy, while its revenue rose largely by 14.6%.
- 2) Cost: although the fuel cost price increased by 35% yoy, the financial expense increased RMB767 million due to the devaluation of RMB. The operating costs increased by 13.1% yoy due to the good cost control, which was less than revenue growth.
- 3) The results of affiliated business turned well, which increased the investing revenue by RMB450 million, and other revenue and non-operating revenue increased by RMB655 million annually.

#### The 2018FY Result Is Under Pressure of the Rising Oil Prices and the Exchange Losses

The result of Air China's cost was still significantly depressed due to the oil prices and exchange in the whole 2018. The fuel cost increased by 35.5% (or RMB10.07 billion) yoy. The exchange loss recorded RMB2.38 billion, while it recorded a profit of RMB2.94 billion in the same period last year. Fortunately, the market-oriented increase in ticket prices, the structure optimization of aircraft allocation under the control of transport capacity, cost control and other measures improved the company's profitability of its main business. The revenue of RPK and unit freight per ATK increased by 2.9% and 5.4% to RMB0.5461 and RMB1.4312, respectively.

In addition, because the result of Cathay Pacific turned from loss to profit. The Company recognized the investing incoming of RMB202 million, and the losses in the same period of last year was RMB986 million.

At the end of the period, the Company's asset-liability ratio decreased by 1 ppts to 58.75%. The cash and cash equivalents reached RMB6.76 billion, accounting for 28% of current assets. The proportion of dollar liability in interest-bearing debts continued to decline from 41% on the end 2017 to 30%.

### Accumulate (Upgrade)

CMP HKD 10.24

(Closing price as at 9 April 2019)

TARGET HKD 11 (+7.4%)

#### COMPANY DATA

O/S SHARES (MN) :	14525
MARKET CAP (HKD MN) :	46722
52 - WK HI/LO (HKD):	11.2/ 5.87

#### SHARE HOLDING PATTERN, %

China National Aviation Holding Company	51.7
Cathay Pacific Airways Limited	18

#### PRICE VS. HSI



Source: Phillip Securities (HK) Research

#### KEY FINANCIALS

CNY mn	FY17	FY18	FY19E	FY20E
Net Sales	124026	140883	153083	162437
Net Profit	7245	7351	11179	12921
EPS, CNY	0.54	0.54	0.77	0.89
P/E, x	15.9	17.0	11.8	10.2
BVPS, CNY	6.39	6.78	7.07	7.79
P/BV, x	1.3	1.3	1.3	1.2
DPS (CNY)	0.12	0.12	0.17	0.19
Div. Yield (%)	1.3%	1.3%	1.8%	2.1%

Source: Company reports, Phillip Securities Est.

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### The Trend of Tight Balance between Supply and Demand Is More Obvious and The External Conditions Are Generally Positive in 2019

From the perspective of transport capacity in the industry, in order to ensure the punctuality rate of flights and the safety of aviation, the regulatory authorities still maintained strict control over the time limits of civil aviation resources. However, the grounding of Boeing 737MAX aggravated the trend of further contraction of industry supply. The May Day holiday and Beijing International Horticultural Exposition this year will have a positive pulling effect on aviation demand. Under the circumstance of tight balance between supply and demand, the prosperity of the industry is expected to continue to rise.

At present, the international oil price has fallen sharply compared with the same period, and the pressure of fuel cost of aviation enterprises has been greatly alleviated. The trend of rapid depreciation of RMB has been curbed. And Air China's dollar liabilities have fallen to 30%, and flexibility of exchange rate has continued to drop.

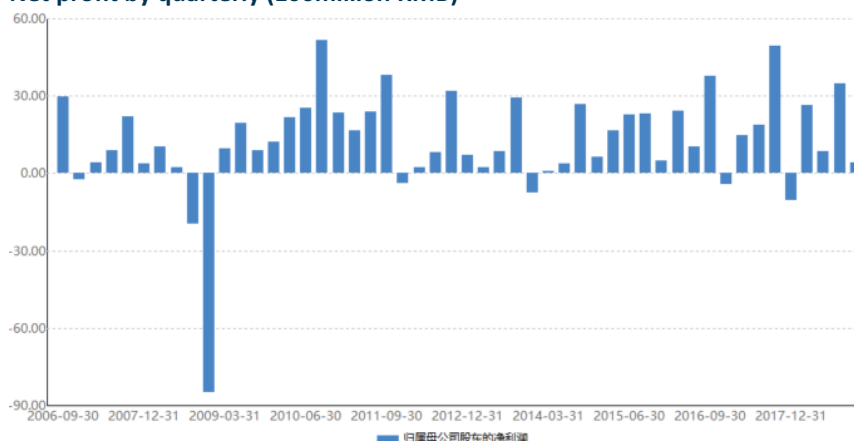
### Valuation & Investment thesis

According to the latest hypothesis of the oil cost and exchange rate, we revised our estimate 2019/2020 net profit of AC to be 11.18/12.92 billion RMB. The target price is adjusted to HKD11, estimates 12.7/11x P/E and 1.38/1.26x P/B in 2019/2020. "Accumulate" rating is given. (Closing price as at 9 April 2019)

### Risk

- Traffic demand languished for the deterioration of macro-economy;
- The depreciation of the RMB against USD would bring exchange loss;
- Oil prices rose exceeded forecast.
- War, terrorist attacks, SARS and other emergencies;
- Highspeed railway diversion

Net profit by quarterly (100million RMB)



Source: Wind, Phillip Securities Hong Kong Research

### Historical BEst P/E, P/B trend



Source: Bloomberg, Phillip Securities Hong Kong Research

### Historical ICE oil price trend



Source: Wind, Phillip Securities Hong Kong Research

### Historical RMB/USD trend



Source: Wind, Phillip Securities Hong Kong Research

## Financials

FYE DEC	FY15	FY16	FY17	FY18	FY19F	FY20F
<b>Valuation Ratios</b>						
P/E (X), adj.	14.9	16.5	15.9	17.0	11.8	10.2
P/B (X)	1.8	1.7	1.33	1.34	1.29	1.17
Dividend Yield (%)	1.3%	1.2%	1.3%	1.3%	1.8%	2.1%
Dividend payout ratio (%)	18.6%	19.4%	21.4%	21.5%	21.4%	21.4%
<b>Per share data (RMB)</b>						
EPS, reported	0.57	0.55	0.54	0.54	0.77	0.89
EPS, adj.	0.57	0.55	0.54	0.54	0.77	0.89
DPS	0.107	0.108	0.115	0.115	0.165	0.190
BVPS	4.86	5.30	6.39	6.78	7.07	7.79
<b>Growth &amp; Margins (%)</b>						
<b>Growth</b>						
Revenue	3.9%	4.6%	7.7%	13.6%	8.7%	6.1%
EBIT	111.6%	2.2%	-35.2%	32.7%	19.8%	10.9%
Net Income, adj.	83.3%	-3.6%	6.4%	1.5%	52.1%	15.6%
<b>Margins</b>						
EBIT margin	15.6%	15.2%	9.2%	10.7%	11.8%	12.3%
Net Profit Margin	6.4%	5.9%	5.8%	5.2%	7.3%	8.0%
<b>Key Ratios</b>						
ROE (%)	12.39%	10.90%	9.36%	8.20%	11.54%	11.28%
<b>Income Statement (RMB mn)</b>						
<b>Revenue</b>	<b>110,057</b>	<b>115,145</b>	<b>124,026</b>	<b>140,883</b>	<b>153,083</b>	<b>162,437</b>
<b>Operating expenses</b>	<b>(94,505)</b>	<b>(97,612)</b>	<b>(112,270)</b>	<b>(126,537)</b>	<b>(135,989)</b>	<b>(143,487)</b>
-Jet fuel cost	(24,043)	(21,982)	(28,409)	(38,481)	(42,868)	(46,512)
Profit from operations	15,552	17,533	11,756	14,346	17,094	18,950
Financial costs	(7,817)	(7,342)	107	(5,118)	(2,668)	(2,375)
Share of profits and losses of associates	1,620	22	(376)	749	985	1,102
Profit before tax	9,355	10,213	11,486	9,977	15,411	17,677
<b>Tax</b>	<b>(1,846)</b>	<b>(2,454)</b>	<b>(2,845)</b>	<b>(1,762)</b>	<b>(3,082)</b>	<b>(3,535)</b>
Profit for the period	7,509	7,759	8,642	8,215	12,329	14,142
Minority interests	446	950	1,397	864	1,150	1,221
<b>Net profit</b>	<b>7,063</b>	<b>6,809</b>	<b>7,245</b>	<b>7,351</b>	<b>11,179</b>	<b>12,921</b>

Source: PSR

(Financial figures as at 9 April 2019)

### 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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