China / Hong Kong Company Update

China Southern Airlines

Bloomberg: 1055 HK Equity | 600029 CH Equity | Reuters: 1055.HK | 600029.SS

Refer to important disclosures at the end of this report

DBS Group Research . Equity

12 Jan 2022

H: BUY

Last Traded Price (11 Jan 2022):HK$4.94(**HSI :** 23,739)
Price Target 12-mth: HK$5.70 (15.4% upside) (Prev HK$6.30)

A: BUY

Last Traded Price (11 Jan 2022):RMB7.11(**CSI300 Index :** 4,798)
Price Target 12-mth: RMB8.30 (16.7% upside) (Prev RMB7.90)

Analyst
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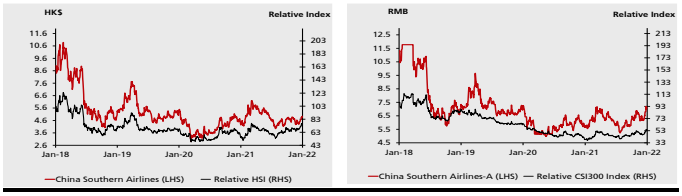
What's New

- Omicron will likely lead to more domestic lockdowns as China sticks to its COVID-zero strategy
- International travel may only resume towards the end of 2022 or 2023
- We now project CSA to remain unprofitable in FY22F; cut FY23F net profit estimate by 63%.
- Maintain BUY but with a lower TP of HK$5.70

Price Relative



Forecasts and Valuation (H Shares)

FY Dec (RMBm)	2020A	2021F	2022F	2023F
Turnover	92,561	104,422	119,313	143,965
EBITDA	19,761	20,156	28,959	35,345
Pre-tax Profit	(15,195)	(11,195)	(3,059)	2,660
Net Profit	(10,847)	(7,801)	(2,100)	2,003
Net Pft (Pre Ex) (core profit)	(6,875)	(7,601)	(2,100)	2,003
Net Profit Gth (Pre-ex) (%)	N/A	(10.6)	72.4	N/A
EPS (RMB)	(0.71)	(0.51)	(0.14)	0.13
EPS (HK$)	(0.87)	(0.62)	(0.17)	0.16
Core EPS (RMB)	(0.45)	(0.50)	(0.14)	0.13
Core EPS (HK$)	(0.55)	(0.61)	(0.17)	0.16
EPS Gth (%)	N/A	28.1	73.1	N/A
Core EPS Gth (%)	N/A	(10.6)	72.4	N/A
Diluted EPS (HK$)	(0.87)	(0.62)	(0.17)	0.16
DPS (HK$)	0.00	0.00	0.00	0.03
BV Per Share (HK$)	5.55	4.93	4.76	4.89
PE (X)	nm	nm	nm	30.9
CorePE (X)	nm	nm	nm	30.9
P/Cash Flow (X)	23.0	4.6	2.4	2.1
P/Free CF (X)	nm	nm	18.6	10.3
EV/EBITDA (X)	12.7	12.8	8.8	7.0
Net Div Yield (%)	0.0	0.0	0.0	0.6
P/Book Value (X)	0.9	1.0	1.0	1.0
Net Debt/Equity (X)	2.0	2.4	2.4	2.3
ROAE(%)	(16.2)	(11.9)	(3.5)	3.3
Earnings Rev (%):		n.m.	(266)	(63)
Consensus EPS (RMB)		(0.53)	0.10	0.30
Other Broker Recs:		B:18	S:1	H:3

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

More resilient against Omicron

Investment Thesis

Shorter recovery timeframe compared to peers. China Southern Airline (CSA)'s earnings are set to normalise before its peers given its leading position in the domestic market, stronger cost control, and larger freighter operations.

International travel to restart from late-2022 and stage a significant rebound in FY23F. We anticipate a meaningful turnaround in CSA's international passenger volumes in FY23F, as China should reopen its international borders sometime in late 2022 to 2023. CSA's total air passenger volumes should reach pre-COVID-19 levels by early-2024.

Attractively priced relative to peers. Despite its more favourable recovery profile, CSA is only priced at 0.9x P/BV (FY23F), which is considerably below the peer median of 1.2x.

Valuation:

Our TP of HK$5.70 is based on 1.2x (+1.0 standard deviation of 5-year average) FY22/23F book value. Our A-share TP is based on a 75% valuation premium to the H shares.

Where we differ:

Our FY22/23F net earnings projections are below consensus, as we expect international travel activity to improve at a more gradual pace.

Key Risks to Our View:

1) Resurgence of COVID-19 in China, 2) prolonged reopening of international borders, 3) substantial depreciation of the RMB, 4) a further spike in jet fuel prices ahead of recovery in passenger traffic.

At A Glance

Issued Capital - H shares (m shs)	4,275
- Non H shrs (m shs)	13,883
H shs as a % of Total	24
Total Mkt Cap (HK$m/US$m)	141,837 / 18,194
Major Shareholders (%)	
China Southern Air Holding Co. Ltd.	67.9
Major H Shareholders (As % of H shares)	
China Southern Air Holding Co. Ltd.	53.3
American Airlines Group Inc	6.3
H Shares-Free Float (%)	40.3
3m Avg. Daily Val. (US$m)	5.14
GICS Industry: Industrials / Transportation	

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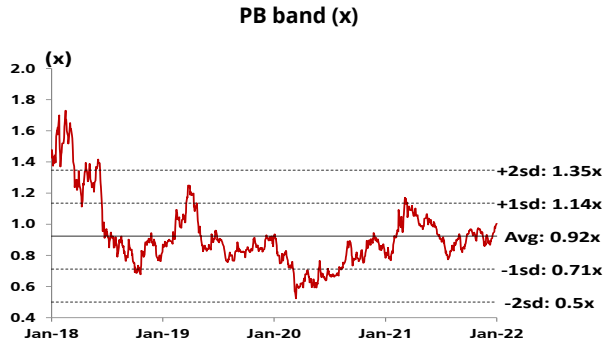
Company Background

China Southern Airlines (CSA) was established in 1989 and debuted on the New York and Hong Kong exchanges in 1997. In 2003, the company was also listed on the Shanghai Stock Exchange. CSA is based in Guangzhou, Guangdong Province with Baiyun International Airport as its main hub.

Historical PB band



Source: Thomson Reuters, DBS HK

Key Assumptions

FY Dec	2019A	2020A	2021F	2022F	2023F
ASK (m p-km)	344,061.9	214,756.6	227,765.6	248,806.6	322,402.4
RPK (m p-km)	284,920.8	153,422.9	166,409.3	185,046.7	253,527.2
Passenger Load Factor (%)	82.8	71.4	73.1	74.4	78.6
Passenger Yield (RMB cts per rpk)	48.6	46.0	48.2	53.6	50.1
All-in jet fuel price (US$/bbl)	85.8	59.2	79.5	87.4	95.2

Source: Company, DBS HK

Segmental Breakdown (RMB m)

FY Dec	2019A	2020A	2021F	2022F	2023F
Revenues (RMB m)					
Passenger	138,502	70,534	80,281	99,198	127,109
Cargo and Mail	9,615	16,493	18,053	13,906	10,522
Others	6,205	5,534	6,087	6,209	6,333
Total	154,322	92,561	104,422	119,313	143,965

Source: Company, DBS HK

Income Statement (RMB m)

FY Dec	2019A	2020A	2021F	2022F	2023F
Revenue	154,322	92,561	104,422	119,313	143,965
Cost of Goods Sold	(148,608)	(105,094)	(114,998)	(121,338)	(140,679)
Gross Profit	5,714	(12,533)	(10,576)	(2,025)	3,286
Other Opng (Exp)/Inc	5,124	4,686	4,500	4,750	5,000
Operating Profit	10,838	(7,847)	(6,076)	2,725	8,286
Other Non Opg (Exp)/Inc	(1,477)	3,485	800	0	0
Associates & JV Inc	187	(467)	350	400	450
Net Interest (Exp)/Inc	(5,771)	(6,394)	(6,069)	(6,184)	(6,075)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	278	(3,972)	(200)	0	0
Pre-tax Profit	4,055	(15,195)	(11,195)	(3,059)	2,660
Tax	(971)	3,368	2,672	761	(486)
Minority Interest	(444)	980	722	197	(172)
Preference Dividend	0	0	0	0	0
Net Profit	2,640	(10,847)	(7,801)	(2,100)	2,003
Net Profit before Except.	2,362	(6,875)	(7,601)	(2,100)	2,003
EBITDA	34,168	19,761	20,156	28,959	35,345
Growth					
Revenue Gth (%)	7.4	(40.0)	12.8	14.3	20.7
EBITDA Gth (%)	57.2	(42.2)	2.0	43.7	22.1
Opg Profit Gth (%)	22.9	(172.4)	(22.6)	(144.8)	204.0
Net Profit Gth (%)	(8.8)	N/A	28.1	73.1	N/A
Margins & Ratio					
Gross Margins (%)	3.7	(13.5)	(10.1)	(1.7)	2.3
Opg Profit Margin (%)	7.0	(8.5)	(5.8)	2.3	5.8
Net Profit Margin (%)	1.7	(11.7)	(7.5)	(1.8)	1.4
ROAE (%)	4.1	(16.2)	(11.9)	(3.5)	3.3
ROA (%)	1.0	(3.4)	(2.5)	(0.7)	0.7
ROCE (%)	3.4	(2.8)	(2.2)	1.0	2.6
Div Payout Ratio (%)	0.0	N/A	N/A	N/A	20.0
Net Interest Cover (x)	1.9	(1.2)	(1.0)	0.4	1.4

Source: Company, DBS HK

Balance Sheet (RMB m)

FY Dec	2019A	2020A	2021F	2022F	2023F
Net Fixed Assets	277,221	269,618	264,536	260,701	258,091
Invts in Associates & JVs	6,446	5,674	6,024	6,424	6,874
Other LT Assets	6,523	12,106	12,106	12,106	12,106
Cash & ST Invts	1,849	25,419	6,923	7,248	9,885
Inventory	1,893	1,760	1,986	2,269	2,737
Debtors	3,152	2,525	2,611	2,983	3,599
Other Current Assets	9,844	9,281	9,281	9,281	9,281
Total Assets	306,928	326,383	303,467	301,012	302,574
ST Debt	57,541	61,029	61,029	61,029	61,029
Creditors	2,317	1,782	2,010	2,297	2,772
Other Current Liab	35,632	32,870	30,248	32,802	35,114
LT Debt	127,713	138,417	126,417	123,418	120,419
Other LT Liabilities	6,396	7,154	7,154	7,155	7,156
Shareholder's Equity	64,106	69,584	61,783	59,683	61,285
Minority Interests	13,223	15,547	14,825	14,628	14,799
Total Cap. & Liab.	306,928	326,383	303,467	301,012	302,574
Non-Cash Wkg. Capital	(23,060)	(21,086)	(18,382)	(20,567)	(22,268)
Net Cash/(Debt)	(183,405)	(174,027)	(180,523)	(177,199)	(171,563)
Debtors Turn (avg days)	7.2	11.2	9.0	8.6	8.3
Creditors Turn (avg days)	6.8	9.3	7.7	8.2	8.1
Inventory Turn (avg days)	5.3	8.3	7.6	8.1	8.0
Asset Turnover (x)	0.6	0.3	0.3	0.4	0.5
Current Ratio (x)	0.2	0.4	0.2	0.2	0.3
Quick Ratio (x)	0.1	0.3	0.1	0.1	0.1
Net Debt/Equity (X)	2.4	2.0	2.4	2.4	2.3
Net Debt/Equity ex MI (X)	2.9	2.5	2.9	3.0	2.8
Capex to Debt (%)	7.8	4.0	10.7	11.9	13.2
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

Cash Flow Statement (RMB m)

FY Dec	2019A	2020A	2021F	2022F	2023F
Pre-Tax Profit	4,055	(15,195)	(11,195)	(3,059)	2,660
Dep. & Amort.	24,620	24,590	25,082	25,835	26,610
Tax Paid	(369)	(563)	(462)	2,672	761
Assoc. & JV Inc/(loss)	(187)	467	(350)	(400)	(450)
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	4,619	(1,873)	429	274	454
Other Operating CF	(1,563)	(4,728)	0	0	0
Net Operating CF	31,175	2,698	13,504	25,323	30,036
Capital Exp.(net)	(14,427)	(8,000)	(20,000)	(22,000)	(24,000)
Other Invts.(net)	0	0	0	0	0
Invts in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	0	(49)	0	0	0
Net Investing CF	(14,427)	(8,049)	(20,000)	(22,000)	(24,000)
Div Paid	0	0	0	0	(401)
Chg in Gross Debt	(21,833)	14,192	(12,000)	(3,000)	(3,000)
Capital Issues	0	15,951	0	0	0
Other Financing CF	0	(1,198)	0	0	0
Net Financing CF	(21,833)	28,945	(12,000)	(3,000)	(3,401)
Currency Adjustments	6	(24)	0	0	0
Chg in Cash	(5,079)	23,570	(18,496)	323	2,635
Opg CFPS (RMB)	2.16	0.30	0.85	1.63	1.93
Free CFPS (RMB)	1.37	(0.35)	(0.42)	0.22	0.39

Source: Company, DBS HK

H Share - Target Price & Ratings History

S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	12-Apr-21	HK$5.71	HK$6.90	Buy
2:	28-Jul-21	HK$4.14	HK$6.40	Buy
3:	6-Sep-21	HK$4.56	HK$6.40	Buy
4:	3-Nov-21	HK$4.56	HK$6.30	Buy

Source: DBS HK

Analyst: *Paul YONG, CFA*

A Share - Target Price & Ratings History

S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	12-Apr-21	RMB6.80	RMB8.60	Buy
2:	6-Sep-21	RMB6.01	RMB8.00	Buy
3:	3-Nov-21	RMB6.43	RMB7.90	Buy

Source: DBS HK

Analyst: *Paul YONG, CFA*

DBS HK recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

**Share price appreciation + dividends*

Completed Date: 12 Jan 2022 13:29:38 (HKT)
Dissemination Date: 12 Jan 2022 14:44:10 (HKT)

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