

China / Hong Kong Company Update

Air China

Bloomberg: 753 HK EQUITY | 601111 CH Equity | Reuters: 0753.HK | 601111.SS

Refer to important disclosures at the end of this report

DBS Group Research . Equity

26 Apr 2022

H: HOLD (Downgrade from Buy)

Last Traded Price (25 Apr 2022): HK\$5.22 (HSI : 19,869)

Price Target 12-mth: HK\$5.20 (0.4% downside) (Prev HK\$6.30)

A: HOLD

Last Traded Price (25 Apr 2022): RMB9.37 (CSI300 Index : 3,815)

Price Target 12-mth: RMB7.60 (18.9% downside) (Prev RMB9.20)

Analyst

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What's New

- Downgrade to HOLD with a lower TP of HK\$5.20
- Domestic passenger traffic will be hurt by an increasing frequency of domestic lockdowns
- Air China will be most adversely impacted by the slow reopening of China's international borders
- Elevated jet fuel prices will severely erode Air China's operating margin

Turning neutral on the stock

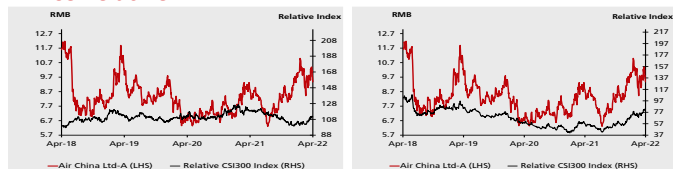
Investment Thesis

FY22F will be another year of substantial losses. We now anticipate the airline to post a net loss of RMB14.0bn in FY22F vs RMB4.0bn earlier due to the combination of rising wages, expensive jet fuel and domestic lockdowns occurring more regularly. Consequently, Air China may need to raise equity to mend its balance sheet.

Longer recovery trajectory compared to regional peers. Despite its exposure to the world's second largest domestic market, it will take longer for Air China's earnings to reach pre-crisis levels, given its relatively higher dependence on international flights, protracted drag from Cathay Pacific at the associate level, and stiffer competition at its key Beijing Hub with the addition of more aircraft slots at the new Beijing Daxing Airport.

Valuation aligned with dimmer recovery prospects. Air China is trading in line with the regional peer median at 1.3x P/BV (FY22F), which is justified, in our view.

Price Relative



Forecasts and Valuation (H Shares)

FY Dec (RMBm)	2020A	2021A	2022F	2023F
Turnover	73,861	78,602	92,498	129,902
EBITDA	6,850	4,492	8,362	30,369
Pre-tax Profit	(18,466)	(21,826)	(18,545)	2,633
Net Profit	(14,403)	(16,635)	(14,005)	1,968
Net Pft (Pre Ex) (core profit)	(14,403)	(16,635)	(14,005)	1,968
Net Profit Gth (Pre-ex) (%)	N/A	(15.5)	15.8	N/A
EPS (RMB)	(0.99)	(1.15)	(0.96)	0.14
EPS (HK\$)	(1.20)	(1.38)	(1.16)	0.16
EPS Gth (%)	N/A	(15.5)	15.8	N/A
Diluted EPS (HK\$)	(1.20)	(1.38)	(1.16)	0.16
DPS (HK\$)	0.00	0.00	0.00	0.03
BV Per Share (HK\$)	6.44	5.10	3.94	4.10
PE (X)	nm	nm	nm	31.9
P/Cash Flow (X)	nm	8.8	9.6	2.5
P/Free CF (X)	nm	20.5	nm	11.6
EV/EBITDA (X)	32.6	52.2	28.9	7.8
Net Div Yield (%)	0.0	0.0	0.0	0.6
P/Book Value (X)	0.8	1.0	1.3	1.3
Net Debt/Equity (X)	1.8	2.5	3.5	3.2
ROAE (%)	(16.8)	(24.0)	(25.8)	4.1
Earnings Rev (%)			n.m.	(21)
Consensus EPS (RMB)			(0.44)	0.28
Other Broker Recs:		B:13	S:2	H:6

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

Valuation:

Our H-share TP of HK\$5.20 is based on 1.2x FY22/23F book value, which is 1.0 standard deviation (SD) above its five-year average. Our A-share TP is derived by applying a 75% valuation premium to the 'H' shares.

Where we differ:

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

Key Risks to Our View:

1) Domestic air traffic stabilising ahead of expectations, 2) mass international air travel resuming before 2023, and 3) cost pressures subsiding ahead of expectations

At A Glance

Issued Capital - H shares (m shs)	4,563
- Non H shrs (m shs)	9,962
H shs as a % of Total	31
Total Mkt Cap (HK\$m/US\$m)	135,493 / 17,266
Major Shareholders (%)	
China National Aviation Holding Co. Ltd.	59.7
China National Aviation Corp (Group) Limited	13.4
Major H Shareholders (As % of H shares)	
Cathay Pacific Airways Ltd	57.7
H Shares-Free Float (%)	42.3
3m Avg. Daily Val. (US\$m)	12.87
GICS Industry: Industrials / Transportation	



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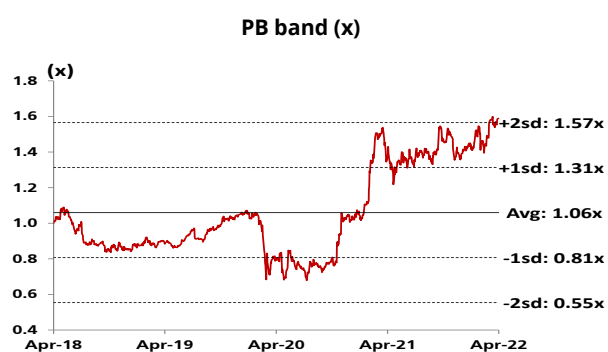


Air China

Company Background

Founded in 1988 and headquartered in Beijing, Air China is the sole flag carrier of China and completed its listing on the Hong Kong and London Stock Exchanges in 2004. Air China joined the Star Alliance in 2007, with its main hub in Beijing and secondary hubs in Shanghai and Chengdu.

Historical PB band



Source: Thomson Reuters, DBS HK

Air China

Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
ASK (m p-km)	287,787.6	156,080.7	152,444.5	167,117.8	248,724.8
RPK (m p-km)	233,176.1	109,830.1	104,625.6	118,003.7	190,014.7
Passenger Load Factor (%)	81.0	70.4	68.6	70.6	76.4
Passenger Yield (RMB cts per RPK)	53.4	50.7	55.7	60.3	59.3
All-in Jet Fuel Price (US\$/bbl)	85.8	55.9	80.8	111.2	102.6

Source: Company, DBS HK

Segmental Breakdown (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenues (RMB m)					
Passenger	124,525	55,727	58,317	71,162	112,747
Cargo	5,732	8,553	11,113	11,594	6,845
Others	9,983	9,580	9,172	9,743	10,311
Total	140,240	73,861	78,602	92,498	129,902

Source: Company, DBS HK

Income Statement (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	140,240	73,861	78,602	92,498	129,902
Cost of Goods Sold	(125,598)	(85,030)	(95,465)	(104,785)	(121,331)
Gross Profit	14,642	(11,169)	(16,862)	(12,286)	8,571
Other Opng (Exp)/Inc	0	0	0	0	0
Operating Profit	14,642	(11,169)	(16,862)	(12,286)	8,571
Other Non Opg (Exp)/Inc	(1,211)	3,604	1,235	500	(600)
Associates & JV Inc	475	(5,993)	(816)	(1,205)	404
Net Interest (Exp)/Inc	(4,786)	(4,908)	(5,383)	(5,554)	(5,742)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
Pre-tax Profit	9,120	(18,466)	(21,826)	(18,545)	2,633
Tax	(1,856)	2,650	3,003	3,121	(401)
Minority Interest	(843)	1,413	2,187	1,419	(264)
Preference Dividend	0	0	0	0	0
Net Profit	6,420	(14,403)	(16,635)	(14,005)	1,968
Net Profit before Except.	6,420	(14,403)	(16,635)	(14,005)	1,968
EBITDA	35,185	6,850	4,492	8,362	30,369
Growth					
Revenue Gth (%)	(0.5)	(47.3)	6.4	17.7	40.4
EBITDA Gth (%)	29.3	(80.5)	(34.4)	86.2	263.2
Opg Profit Gth (%)	2.1	(176.3)	51.0	(27.1)	(169.8)
Net Profit Gth (%)	(12.7)	N/A	(15.5)	15.8	N/A
Margins & Ratio					
Gross Margins (%)	10.4	(15.1)	(21.5)	(13.3)	6.6
Opg Profit Margin (%)	10.4	(15.1)	(21.5)	(13.3)	6.6
Net Profit Margin (%)	4.6	(19.5)	(21.2)	(15.1)	1.5
ROAE (%)	6.9	(16.8)	(24.0)	(25.8)	4.1
ROA (%)	2.4	(5.0)	(5.7)	(4.8)	0.7
ROCE (%)	5.1	(4.4)	(6.5)	(4.8)	3.0
Div Payout Ratio (%)	10.0	N/A	N/A	N/A	20.0
Net Interest Cover (x)	3.1	(2.3)	(3.1)	(2.2)	1.5

Source: Company, DBS HK

Balance Sheet (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	221,535	215,886	220,415	214,062	212,068
Invt in Associates & JVs	16,191	12,520	12,220	11,015	11,419
Other LT Assets	31,664	35,888	35,349	35,349	35,349
Cash & ST Invt	9,664	6,575	17,044	8,598	8,992
Inventory	2,099	1,854	2,050	2,027	2,135
Debtors	5,998	2,943	2,991	3,675	5,338
Other Current Assets	7,057	8,364	8,312	8,312	8,312
Total Assets	294,206	284,030	298,381	283,038	283,614
ST Debt	36,591	53,191	54,737	54,737	52,237
Creditors	16,578	12,511	12,591	12,671	16,015
Other Current Liab	24,803	14,896	24,292	24,292	24,292
LT Debt	103,185	107,738	129,467	129,467	126,967
Other LT Liabilities	11,719	11,921	11,463	11,463	11,463
Shareholder's Equity	93,459	77,541	61,369	47,364	49,332
Minority Interests	7,871	6,232	4,463	3,044	3,308
Total Cap. & Liab.	294,206	284,030	298,381	283,038	283,614
Non-Cash Wkg. Capital	(26,228)	(14,246)	(23,530)	(22,949)	(24,522)
Net Cash/(Debt)	(130,113)	(154,354)	(167,160)	(175,606)	(170,212)
Debtors Turn (avg days)	14.8	22.1	13.8	13.2	12.7
Creditors Turn (avg days)	54.8	82.2	61.5	55.3	52.7
Inventory Turn (avg days)	7.0	11.2	9.6	8.9	7.6
Asset Turnover (x)	0.5	0.3	0.3	0.3	0.5
Current Ratio (x)	0.3	0.2	0.3	0.2	0.3
Quick Ratio (x)	0.2	0.1	0.2	0.1	0.2
Net Debt/Equity (X)	1.3	1.8	2.5	3.5	3.2
Net Debt/Equity ex MI (X)	1.4	2.0	2.7	3.7	3.5
Capex to Debt (%)	8.6	7.4	2.2	8.1	11.2
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

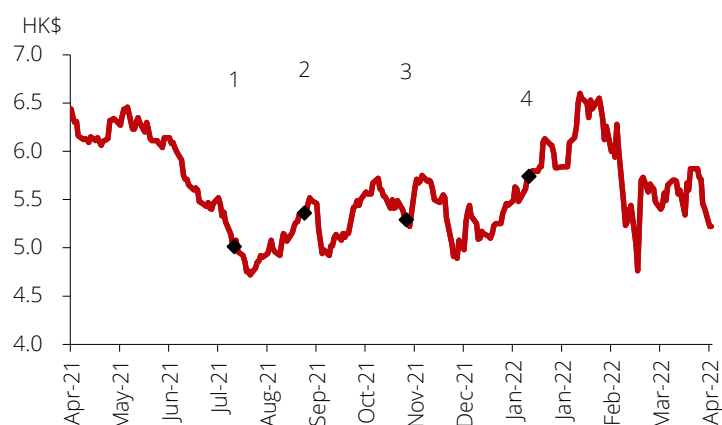
Cash Flow Statement (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	9,120	(18,466)	(21,826)	(18,545)	2,633
Dep. & Amort.	21,279	20,408	20,935	21,353	21,994
Tax Paid	(1,856)	(939)	3,003	3,121	(401)
Assoc. & JV Inc/(loss)	(475)	5,993	816	1,205	(404)
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	4,012	(11,089)	9,325	(580)	1,572
Other Operating CF	1,519	75	(5,122)	0	0
Net Operating CF	33,599	(4,017)	7,130	6,554	25,395
Capital Exp.(net)	(11,967)	(11,905)	(4,061)	(15,000)	(20,000)
Other Invt.(net)	0	(2,957)	0	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	7	2	0	0
Other Investing CF	0	(1,010)	(394)	0	0
Net Investing CF	(11,967)	(15,865)	(4,453)	(15,000)	(20,000)
Div Paid	(1,500)	(740)	(27)	0	0
Chg in Gross Debt	(18,010)	21,152	7,005	0	(5,000)
Capital Issues	0	0	0	0	0
Other Financing CF	0	(3,524)	491	0	0
Net Financing CF	(19,510)	16,888	7,469	0	(5,000)
Currency Adjustments	50	(103)	(49)	0	0
Chg in Cash	2,172	(3,097)	10,097	(8,446)	395
Opg CFPS (RMB)	2.04	0.49	(0.15)	0.49	1.64
Free CFPS (RMB)	1.49	(1.10)	0.21	(0.58)	0.37

Source: Company, DBS HK

Air China

H Share - Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	28-Jul-21	HK\$5.03	HK\$6.80	Buy
2:	6-Sep-21	HK\$5.34	HK\$7.00	Buy
3:	3-Nov-21	HK\$5.31	HK\$6.50	Buy
4:	12-Jan-22	HK\$5.72	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:	6-Sep-21	RMB7.56	RMB8.80	Buy
2:	3-Nov-21	RMB8.47	RMB8.70	Hold
3:	12-Jan-22	RMB9.74	RMB9.20	Hold

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

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