

# China / Hong Kong Company Update

## China Southern Airlines

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

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DBS Group Research . Equity

14 Sep 2022

**H: HOLD** (Downgrade from BUY)

Last Traded Price ( 13 Sep 2022):HK\$4.23(HSI : 19,327)

Price Target 12-mth: HK\$4.50 (6.4% upside) (Prev HK\$5.10)

**A: HOLD** (Downgrade from BUY)

Last Traded Price ( 13 Sep 2022):RMB6.68(CSI300 Index : 4,111)

Price Target 12-mth: RMB7.30 (9.3% upside)

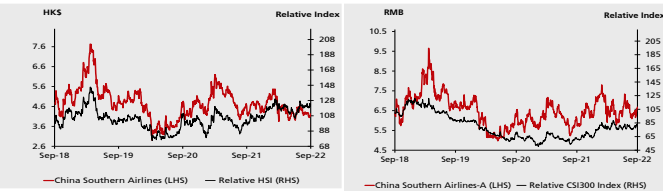
Analyst

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### What's New

- Downgrade to HOLD with lower TP of HK\$4.50
- 1H22 net loss of RMB11.5bn was better than peers
- CSA was the only airline among the big three to have positive EBITDA and operating cash flow in 1H22; net gearing ratio remains fairly stable
- Cut FY22/23F net profit estimates to reflect slower recovery in passenger traffic

### Price Relative



### Forecasts and Valuation (H Shares)

FY Dec (RMBm)	2020A	2021A	2022F	2023F
Turnover	92,561	101,644	92,989	131,884
EBITDA	19,761	18,781	6,946	29,030
Pre-tax Profit	(15,195)	(13,910)	(22,356)	(1,750)
Net Profit	(10,847)	(12,106)	(18,104)	(1,414)
EPS (RMB)	(0.71)	(0.75)	(1.02)	(0.08)
Core EPS (RMB)	(0.45)	(0.57)	(1.02)	(0.08)
EPS Gth (%)	N/A	(6.0)	(35.8)	92.5
Core EPS Gth (%)	N/A	(26.9)	(79.7)	92.6
Diluted EPS (HK\$)	(0.80)	(0.85)	(1.15)	(0.09)
DPS (HK\$)	0.00	0.00	0.00	0.00
BV Per Share (HK\$)	5.14	4.53	3.43	3.35
PE (X)	nm	nm	nm	nm
CorePE (X)	nm	nm	nm	nm
P/Cash Flow (X)	21.2	7.8	29.6	2.9
P/Free CF (X)	nm	nm	nm	nm
EV/EBITDA (X)	12.5	13.5	38.9	9.4
Net Div Yield (%)	0.0	0.0	0.0	0.0
P/Book Value (X)	0.8	0.9	1.2	1.3
Net Debt/Equity (X)	2.0	2.1	2.6	2.6
ROAE(%)	(16.2)	(17.6)	(29.1)	(2.5)
Earnings Rev (%)			n.m.	(181)
Consensus EPS (RMB)			(0.76)	0.12
Other Broker Recs:		B:10	S:5	H:1

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

## Grounded for now

### Investment Thesis

In a better position to weather near-term turbulence. While we project China Southern Airlines (CSA) to remain in the red in FY22/23F, we believe that it will continue to outperform the other two Chinese flag carriers in terms of the bottom line.

Shorter recovery timeframe compared to domestic peers.

CSA's earnings are set to normalise ahead of other Chinese airlines, given its leading position in the domestic market, stronger cost control, and larger freighter operations.

Risk-to-reward is neutral. CSA is currently priced at 1.2x forward P/BV, which is at 1.0SD above its five-year average. Considering its recovery prospects, we view this as fair.

### Valuation:

We downgrade our recommendation on CSA to HOLD with a lower TP of HK\$4.50, reflecting our negative earnings revision. Our TP of HK\$4.50 is based on 1.2x (+1.0SD of its five-year average) FY22/23F book value. Our A-share TP is based on a 100% valuation premium to the H-shares.

### Where we differ:

Our FY22/23F net earnings projections are considerably below the 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)	4,644
- Non H shrs (m shs)	12,673
H shs as a % of Total	27
Total Mkt Cap (HK\$m/US\$m)	115,601 / 14,727
Major Shareholders (%)	
China Southern Air Holding Co. Limited	67.9
Major H Shareholders (As % of H shares)	
China Southern Air Holding Co. Limited	57.0
American Airlines Group Inc	5.8
H Shares-Free Float (%)	37.1
3m Avg. Daily Val. (US\$m)	5.64
GICS Industry: Industrials / Transportation	



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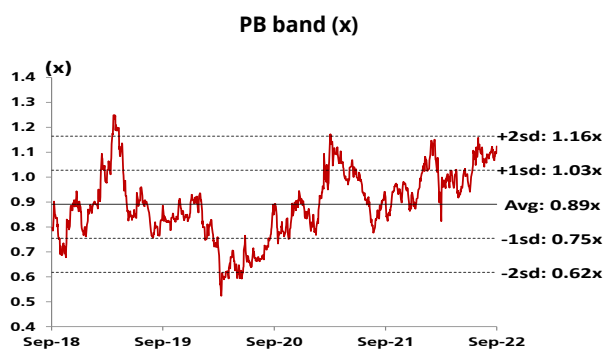
Live more, Bank less

## China Southern Airlines

### 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

## China Southern Airlines

### Key Assumptions

FY Dec	2019A	2020A	2021A	2022F	2023F
ASK (m p-km)	344,061.9	214,756.6	213,921.8	172,047.6	268,995.5
RPK (m p-km)	284,920.8	153,440.1	152,426.3	115,090.1	206,704.0
Passenger Load Factor (%)	82.8	71.4	71.3	66.9	76.8
Passenger Yield (RMB cts per rpk)	48.6	46.0	49.5	55.5	52.6
All-in jet fuel price (US\$/bbl)	85.8	55.7	83.4	117.6	106.4

Source: Company, DBS HK

### Segmental Breakdown (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
<b>Revenues (RMB m)</b>					
Passenger	138,502	70,534	75,392	63,908	108,809
Cargo and Mail	9,615	16,493	19,887	22,881	16,751
Others	6,205	5,534	6,365	6,200	6,324
<b>Total</b>	<b>154,322</b>	<b>92,561</b>	<b>101,644</b>	<b>92,989</b>	<b>131,884</b>

Source: Company, DBS HK

### Income Statement (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	154,322	92,561	101,644	92,989	131,884
Cost of Goods Sold	(148,608)	(105,094)	(113,726)	(111,658)	(133,198)
<b>Gross Profit</b>	<b>5,714</b>	<b>(12,533)</b>	<b>(12,082)</b>	<b>(18,669)</b>	<b>(1,314)</b>
Other Opng (Exp)/Inc	5,124	4,686	4,767	4,500	5,000
<b>Operating Profit</b>	<b>10,838</b>	<b>(7,847)</b>	<b>(7,315)</b>	<b>(14,169)</b>	<b>3,686</b>
Other Non Opg (Exp)/Inc	(1,477)	3,485	1,575	(3,000)	0
Associates & JV Inc	187	(467)	280	359	400
Net Interest (Exp)/Inc	(5,771)	(6,394)	(5,527)	(5,615)	(5,836)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	278	(3,972)	(2,923)	69	0
<b>Pre-tax Profit</b>	<b>4,055</b>	<b>(15,195)</b>	<b>(13,910)</b>	<b>(22,356)</b>	<b>(1,750)</b>
Tax	(971)	3,368	2,894	4,353	473
Minority Interest	(444)	980	(1,090)	(100)	(137)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>2,640</b>	<b>(10,847)</b>	<b>(12,106)</b>	<b>(18,104)</b>	<b>(1,414)</b>
Net Profit before Except.	2,362	(6,875)	(9,183)	(18,173)	(1,414)
EBITDA	34,168	19,761	18,781	6,946	29,030
<b>Growth</b>					
Revenue Gth (%)	7.4	(40.0)	9.8	(8.5)	41.8
EBITDA Gth (%)	57.2	(42.2)	(5.0)	(63.0)	317.9
Opg Profit Gth (%)	22.9	(172.4)	(6.8)	93.7	(126.0)
Net Profit Gth (%)	(8.8)	N/A	(11.6)	(49.5)	92.2
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	3.7	(13.5)	(11.9)	(20.1)	(1.0)
Opg Profit Margin (%)	7.0	(8.5)	(7.2)	(15.2)	2.8
Net Profit Margin (%)	1.7	(11.7)	(11.9)	(19.5)	(1.1)
ROAE (%)	4.1	(16.2)	(17.6)	(29.1)	(2.5)
ROA (%)	1.0	(3.4)	(3.7)	(5.7)	(0.5)
ROCE (%)	3.4	(2.8)	(2.5)	(5.0)	1.3
Div Payout Ratio (%)	0.0	N/A	N/A	N/A	N/A
Net Interest Cover (x)	1.9	(1.2)	(1.3)	(2.5)	0.6

Source: Company, DBS HK

## China Southern Airlines

### Balance Sheet (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Net Fixed Assets	277,221	269,618	261,382	257,626	256,682
Invt in Associates & JVs	6,446	5,674	5,978	6,337	6,737
Other LT Assets	6,523	12,106	17,985	17,985	17,985
Cash & ST Invt	1,849	25,419	22,748	11,705	11,477
Inventory	1,893	1,760	1,652	1,511	2,143
Debtors	3,152	2,525	2,858	2,325	3,297
Other Current Assets	9,844	9,281	10,608	10,608	10,608
<b>Total Assets</b>	<b>306,928</b>	<b>326,383</b>	<b>323,211</b>	<b>308,096</b>	<b>308,930</b>
ST Debt	57,541	61,029	78,718	78,718	78,718
Creditors	2,317	1,782	1,328	1,215	1,723
Other Current Liab	35,632	32,870	30,944	27,232	28,834
LT Debt	127,713	138,417	120,298	120,298	120,298
Other LT Liabilities	6,396	7,154	7,415	7,415	7,415
Shareholder's Equity	64,106	69,584	67,851	56,461	55,047
Minority Interests	13,223	15,547	16,657	16,757	16,894
<b>Total Cap. &amp; Liab.</b>	<b>306,928</b>	<b>326,383</b>	<b>323,211</b>	<b>308,096</b>	<b>308,930</b>
Non-Cash Wkg. Capital	(23,060)	(21,086)	(17,154)	(14,003)	(14,509)
Net Cash/(Debt)	(183,405)	(174,027)	(176,268)	(187,311)	(187,539)
Net Debt/Equity (X)	2.4	2.0	2.1	2.6	2.6
Net Debt/Equity ex MI (X)	2.9	2.5	2.6	3.3	3.4

Source: Company, DBS HK

### Cash Flow Statement (RMB m)

FY Dec	2019A	2020A	2021A	2022F	2023F
Pre-Tax Profit	4,055	(15,195)	(13,910)	(22,356)	(1,750)
Dep. & Amort.	24,620	24,590	24,241	23,756	24,944
Tax Paid	(369)	(563)	(462)	(743)	(58)
Assoc. & JV Inc/(loss)	(187)	467	(280)	(359)	(400)
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	4,619	(6,359)	(1,315)	1,944	1,037
Other Operating CF	(1,563)	(242)	(586)	0	0
<b>Net Operating CF</b>	<b>31,175</b>	<b>2,698</b>	<b>7,688</b>	<b>2,243</b>	<b>23,773</b>
Capital Exp.(net)	(14,427)	(8,213)	(16,147)	(20,000)	(24,000)
Other Invt.(net)	0	0	0	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	337	263	0	0
Other Investing CF	0	(173)	64	0	0
<b>Net Investing CF</b>	<b>(14,427)</b>	<b>(8,049)</b>	<b>(15,820)</b>	<b>(20,000)</b>	<b>(24,000)</b>
Div Paid	0	0	0	0	0
Chg in Gross Debt	(21,833)	9,415	3,711	0	0
Capital Issues	0	19,753	1,128	6,714	0
Other Financing CF	0	(223)	(653)	0	0
<b>Net Financing CF</b>	<b>(21,833)</b>	<b>28,945</b>	<b>4,186</b>	<b>6,714</b>	<b>0</b>
Currency Adjustments	6	(24)	(17)	0	0
Chg in Cash	(5,079)	23,570	(3,963)	(11,043)	(227)
Opg CFPS (RMB)	2.16	0.59	0.56	0.02	1.22
Free CFPS (RMB)	1.37	(0.36)	(0.52)	(1.00)	(0.01)

Source: Company, DBS HK

## China Southern Airlines

### H Share - Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	3-Nov-21	HK\$4.56	HK\$6.30	Buy
2:	12-Jan-22	HK\$4.94	HK\$5.70	Buy
3:	26-Apr-22	HK\$4.23	HK\$5.10	Buy

Source: DBS HK

Analyst: Paul YONG

### A Share - Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	3-Nov-21	RMB6.43	RMB7.90	Buy
2:	12-Jan-22	RMB7.11	RMB8.30	Buy
3:	26-Apr-22	RMB6.50	RMB7.30	Buy

Source: DBS HK

Analyst: Paul YONG

## China Southern Airlines

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)

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## China Southern Airlines

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