

# China Eastern Airlines

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Refer to important disclosures at the end of this report

DBS Group Research . Equity

18 Jan 2024

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

Last Traded Price ( 17 Jan 2024): HK\$2.06 (HSI : 15,277)

Price Target 12-mth: HK\$2.80 (35.9% upside) (Prev HK\$3.00)

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

Last Traded Price ( 17 Jan 2024): RMB3.78 (CSI300 Index : 3,229)

Price Target 12-mth: RMB4.40 (16.4% upside) (Prev RMB4.70)

Analyst

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## What's New

- Upgrade to BUY from HOLD with revised TP of HK\$2.80
- Stellar earnings outlook for next two years on capacity growth and wider margins from a low base
- Trim FY24F EBITDA forecast on more gradual resumption of international passenger capacity, partially offset by higher yields
- Trading at more than 2SD below five-year pre-pandemic average; valuations warrant a second look at the counter

## Phenomenal earnings growth at compelling valuations

### Investment Thesis

**State-owned airline with strong foothold in the Shanghai hub.** China Eastern Airlines (CEA) is one of the three major airlines in China with dual core hubs in Beijing and Shanghai, China's main international hubs, which places the group in a solid position to benefit from the resumption of international flights post reopening. The airline has a particularly strong presence in the Shanghai hub, garnering the largest market share in terms of international capacity from Shanghai, the domestic route between Beijing-Shanghai, and regional routes to Japan and South Korea, amongst the three Chinese airlines.

**Stellar earnings outlook on capacity growth from a low base.** CEA is approaching an earnings inflection point, marking a turnaround in its four years of pandemic-induced losses. With the Asia Pacific region reopening much later than others and with more headroom for recovery, we expect CEA to meaningfully ramp up international passenger capacity over the next two years. Moreover, the group is poised to achieve wider margins owing to a significant improvement in unit costs on economies of scale. Consequently, CEA is on the cusp of robust earnings growth, notably surpassing its pre-pandemic levels of profitability.

**Attractive valuations; stronger-than-expected cash flows to enable swift deleveraging.** We believe that its valuations are significantly more compelling, at more than 2SD below its five-year pre-pandemic average, particularly with the expectation of unmatched earnings growth over the next two years, following a >30% correction of the company's share price over the past year. Though the group's balance sheet remains stretched, a stronger-than-expected generation of cash flows will enable the group to deleverage swiftly and bolster its financial health.

**Upgrade CEA to BUY with revised TP of HK\$2.80** (HK\$3.00 previously), based on 7.0x EV/EBITDA (FY24F), which is 1SD below its five-year pre-pandemic average. The upgrade in our recommendation reflects CEA's phenomenal earnings recovery over the next two years on attractive valuations. Our A-share TP is derived by applying a 70% valuation premium to its H-share.

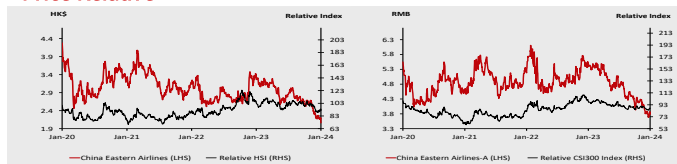
### Key Risks

**Macroeconomic headwinds** could curtail CEA's passenger traffic recovery and keep a lid on yields, while **elevated jet fuel prices** could weigh on operating margins.

### At A Glance

Issued Capital - H shares (m shs)	5,177
- Non H shrs (m shs)	17,115
H shs as a % of Total	23
Total Mkt Cap (HK\$/US\$m)	80,789 / 10,330
Major Shareholders (%)	
China Eastern Air Holding Company Limited	51.3
Major H Shareholders (As % of H shares)	
China Eastern Air Holding Company Limited	52.0
Juneyao Airlines Co., Ltd.	10.8
Delta Air Lines, Inc.	9.0
H Shares-Free Float (%)	28.2
3m Avg. Daily Val. (US\$m)	1.74
GICS Industry: Industrials / Transportation	

### Price Relative



### Forecasts and Valuation (H Shares)

FY Dec (RMBm)	2022A	2023F	2024F	2025F
Turnover	49,724	121,003	140,829	152,566
EBITDA	(9,836)	25,743	36,874	39,887
Pre-tax Profit	(40,154)	(5,958)	5,863	8,744
Net Profit	(37,386)	(4,581)	4,391	6,548
Net Pft (Pre Ex) (core profit)	(37,386)	(4,581)	4,391	6,548
Net Profit Gth (Pre-ex) (%)	(206.1)	87.7	N/A	49.1
EPS (RMB)	(1.68)	(0.21)	0.20	0.29
EPS Gth (%)	(159.2)	87.7	N/A	49.1
DPS (HK\$)	0.00	0.00	0.00	0.00
BV Per Share (HK\$)	1.53	1.30	1.52	1.84
PE (X)	nm	nm	9.6	6.5
P/Cash Flow (X)	nm	1.9	1.3	1.2
P/Free CF (X)	nm	4.5	2.4	2.1
EV/EBITDA (X)	nm	9.2	5.9	5.0
Net Div Yield (%)	0.0	0.0	0.0	0.0
P/Book Value (X)	1.3	1.6	1.4	1.1
Net Debt/Equity (X)	6.2	7.1	5.5	4.0
ROAE (%)	(88.0)	(15.8)	15.2	19.0
Earnings Rev (%)		Nil	(21)	New
Consensus EPS (RMB)		(0.15)	0.26	0.39
Other Broker Recs:		B:12	S:1	H:4

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

## China Eastern Airlines

### WHAT'S NEW

#### Phenomenal earnings growth at compelling valuations

Our 2024 outlook report for the [airline sector](#) highlights that macroeconomic indicators still largely favour the sector, though we expect to see a diverging earnings outlook across regions and business segments. This underpins our expectation of global passenger traffic hitting 105%-110%/115%-120% of 2019's level in 4Q24/4Q25. Across the three major regions, we are most positive about airlines in Asia Pacific, as we expect them to demonstrate stronger earnings momentum, underpinned by relatively higher capacity growth and wider margins, with the Chinese airlines likely to see the biggest upswing in earnings. While valuation multiples for Asian airlines might appear high, they are commensurate with the region's stronger earnings potential. Our top picks are Cathay Pacific (CX) and China Southern Airlines (CSA).

However, we lowered our FY24F net profit estimates by 10-20% for the three Chinese airlines, reflecting a more moderate resumption of international passenger capacity and a more gradual improvement in unit costs owing to slower capacity growth. Nonetheless, we expect the Chinese airlines to deliver strong earnings growth ahead. Following a stellar performance in 3Q23, marking their first profitable quarter since the pandemic, the Chinese airlines are poised to sustain and amplify this upswing, potentially leading the sector in earnings growth, in our view.

We upgrade CEA to BUY, as we roll over our valuation base to FY24F and adjust our valuation peg due to the multiple contractions in the airline sector. Our new TP of HK\$2.80 is based on 7.0x EV/EBITDA (FY24F), which is 1SD below its five-year pre-pandemic average. CEA's share price has corrected more than 30% over the past year and we believe that its valuations are significantly more compelling, at more than 2SD below its five-year pre-pandemic average, particularly with the expectation of unmatched earnings growth over the next two years.

#### Company Background

Incorporated in China in 1995, China Eastern Airlines (CEA) was publicly listed on the New York, Hong Kong, and Shanghai stock exchanges in 1997. The major hubs for CEA are Shanghai Hongqiao International Airport and Shanghai Pudong International Airport. CEA also has hubs in Kunming and Xi'an.

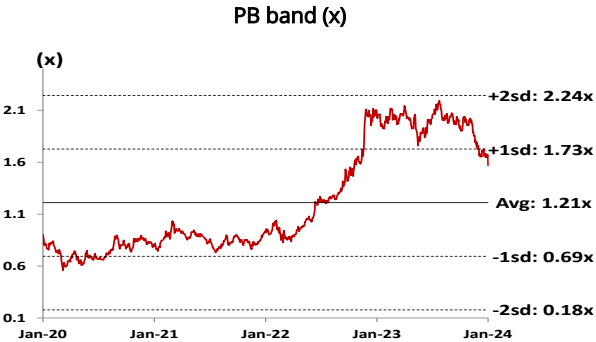
#### Valuation table

(in RMB millions unless specified otherwise)	Value	Comments
EBITDA	36,874	FY24F
EV/EBITDA multiple peg (x)	7.0	1 standard deviation below five-year pre-pandemic average
Enterprise value	252,585	
Less: net debt	(199,617)	As at June 23
Less: minority interests	(1,058)	As at June 23
Add: JVs and assocs	2,717	
Equity value	54,992	
Number of shares outstanding (m)	22,291	
Value per share (HK\$)	2.80	

Source: DBS Bank estimates

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Historical PB band



Source: Thomson Reuters, DBS HK

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### Key Assumptions

FY Dec	2021A	2022A	2023F	2024F	2025F
ASK (m p-km)	160,690.4	96,210.9	244,974.7	279,466.1	311,376.6
RPK (m p-km)	108,803.7	61,287.7	182,324.7	222,042.7	253,118.3
Passenger Load Factor (%)	67.7	63.7	74.4	79.5	81.3
Passenger Yield (RMB cts per rpk)	53.1	60.2	60.1	57.6	54.9
All-in jet fuel price (US\$/bbl)	80.2	130.5	117.7	107.0	112.4

Source: Company, DBS HK

### Segmental Breakdown (RMB m)

FY Dec	2021A	2022A	2023F	2024F	2025F
<b>Revenues (RMB m)</b>					
Passenger	54,105	35,004	106,039	122,325	133,350
Cargo	8,309	7,770	3,998	4,049	3,872
Others	4,713	3,337	5,339	6,941	7,635
Other operating income	6,079	3,613	5,627	7,514	7,709
<b>Total</b>	<b>73,206</b>	<b>49,724</b>	<b>121,003</b>	<b>140,829</b>	<b>152,566</b>

Source: Company, DBS HK

## China Eastern Airlines

## Income Statement (RMB m)

FY Dec	2021A	2022A	2023F	2024F	2025F
Revenue	73,206	49,724	121,003	140,829	152,566
Cost of Goods Sold	(86,724)	(81,359)	(119,240)	(129,133)	(139,115)
<b>Gross Profit</b>	<b>(13,518)</b>	<b>(31,635)</b>	<b>1,764</b>	<b>11,696</b>	<b>13,451</b>
Other Opng (Exp)/Inc	0	0	0	0	0
<b>Operating Profit</b>	<b>(13,518)</b>	<b>(31,635)</b>	<b>1,764</b>	<b>11,696</b>	<b>13,451</b>
Other Non Opng (Exp)/Inc	1,619	(2,687)	(1,400)	0	0
Associates & JV Inc	(141)	(197)	100	300	300
Net Interest (Exp)/Inc	(5,473)	(5,635)	(6,422)	(6,133)	(5,007)
Dividend Income	0	0	0	0	0
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>(17,513)</b>	<b>(40,154)</b>	<b>(5,958)</b>	<b>5,863</b>	<b>8,744</b>
Tax	4,229	254	1,013	(1,114)	(1,661)
Minority Interest	1,070	2,514	364	(358)	(534)
Preference Dividend	0	0	0	0	0
<b>Net Profit</b>	<b>(12,214)</b>	<b>(37,386)</b>	<b>(4,581)</b>	<b>4,391</b>	<b>6,548</b>
Net Profit before Except.	(12,214)	(37,386)	(4,581)	4,391	6,548
EBITDA	9,200	(9,836)	25,743	36,874	39,887
<b>Growth</b>					
Revenue Gth (%)	13.6	(32.1)	143.4	16.4	8.3
EBITDA Gth (%)	9.3	N/A	N/A	43.2	8.2
Opg Profit Gth (%)	(2.3)	134.0	(105.6)	563.1	15.0
Net Profit Gth (%)	(3.2)	(206.1)	87.7	N/A	49.1
<b>Margins &amp; Ratio</b>					
Gross Margins (%)	(18.5)	(63.6)	1.5	8.3	8.8
Opg Profit Margin (%)	(18.5)	(63.6)	1.5	8.3	8.8
Net Profit Margin (%)	(16.7)	(75.2)	(3.8)	3.1	4.3
ROAE (%)	(22.2)	(88.0)	(15.8)	15.2	19.0
ROA (%)	(4.3)	(13.0)	(1.6)	1.6	2.4
ROCE (%)	(5.2)	(12.0)	0.7	3.9	4.7
Div Payout Ratio (%)	N/A	N/A	N/A	0.0	0.0
Net Interest Cover (x)	(2.5)	(5.6)	0.3	1.9	2.7

Source: Company, DBS HK

## Interim Income Statement (RMB m)

FY Dec	1H2021	2H2021	1H2022	2H2022	1H2023
Revenue	34,710	32,417	19,354	26,757	49,425
Cost of Goods Sold	(40,183)	(40,462)	(35,070)	(42,676)	(52,022)
<b>Gross Profit</b>	<b>(5,473)</b>	<b>(8,045)</b>	<b>(15,716)</b>	<b>(15,919)</b>	<b>(2,597)</b>
Other Oper. (Exp)/Inc	0	0	0	0	0
<b>Operating Profit</b>	<b>(5,473)</b>	<b>(8,045)</b>	<b>(15,716)</b>	<b>(15,919)</b>	<b>(2,597)</b>
Other Non Opng (Exp)/Inc	827	792	(1,410)	(1,277)	(1,327)
Associates & JV Inc	14	(155)	(23)	(174)	12
Net Interest (Exp)/Inc	(2,648)	(2,825)	(2,846)	(2,789)	(3,054)
Exceptional Gain/(Loss)	0	0	0	0	0
<b>Pre-tax Profit</b>	<b>(7,280)</b>	<b>(10,233)</b>	<b>(19,995)</b>	<b>(20,159)</b>	<b>(6,966)</b>
Tax	1,882	2,347	21	233	389
Minority Interest	190	880	1,238	1,276	328
<b>Net Profit</b>	<b>(5,208)</b>	<b>(7,006)</b>	<b>(18,736)</b>	<b>(18,650)</b>	<b>(6,249)</b>
Net profit bef Except.	(5,208)	(7,006)	(18,736)	(18,650)	(6,249)
<b>Growth</b>					
Revenue Gth (%)	38.0	(3.4)	(44.2)	(17.5)	155.4
Opg Profit Gth (%)	(36.2)	53.0	187.2	97.9	(83.5)
Net Profit Gth (%)	39.0	(112.7)	(259.8)	(166.2)	66.6
<b>Margins</b>					
Gross Margins (%)	(15.7)	(15.8)	(24.8)	(81.2)	(59.5)
Opg Profit Margins (%)	(15.7)	(15.8)	(24.8)	(81.2)	(59.5)
Net Profit Margins (%)	(9.8)	(15.0)	(21.6)	(96.8)	(69.7)

Source: Company, DBS HK

## China Eastern Airlines

**Balance Sheet (RMB m)**

FY Dec	2021A	2022A	2023F	2024F	2025F
Net Fixed Assets	93,242	89,208	78,538	69,169	58,542
Invt in Associates & JVs	2,261	2,064	2,164	2,464	2,764
Other LT Assets	165,377	169,299	168,490	167,681	166,872
Cash & ST Invt	12,950	17,541	12,005	14,510	19,401
Inventory	1,799	1,626	2,308	2,424	2,634
Debtors	974	754	1,923	2,051	2,229
Other Current Assets	12,187	7,492	11,000	14,000	14,000
<b>Total Assets</b>	<b>288,790</b>	<b>287,984</b>	<b>276,427</b>	<b>272,299</b>	<b>266,441</b>
ST Debt	61,349	82,622	82,622	82,622	82,622
Creditors	2,454	2,310	3,846	3,809	4,139
Other Current Liab	22,088	21,514	28,026	33,026	33,026
LT Debt	132,918	136,326	122,726	107,726	92,726
Other LT Liabilities	12,829	12,869	11,810	12,969	14,699
Shareholder's Equity	53,615	31,322	26,741	31,131	37,680
Minority Interests	3,537	1,021	657	1,015	1,549
<b>Total Cap. &amp; Liab.</b>	<b>288,790</b>	<b>287,984</b>	<b>276,427</b>	<b>272,299</b>	<b>266,441</b>
Non-Cash Wkg. Capital	(9,582)	(13,952)	(16,641)	(18,360)	(18,302)
Net Cash/(Debt)	(181,317)	(201,407)	(193,343)	(175,838)	(155,947)
Debtors Turn (avg days)	5.2	6.3	4.0	5.1	5.1
Creditors Turn (avg days)	16.2	14.6	11.8	13.4	12.9
Inventory Turn (avg days)	11.0	10.5	7.5	8.3	8.2
Asset Turnover (x)	0.3	0.2	0.4	0.5	0.6
Current Ratio (x)	0.3	0.3	0.2	0.3	0.3
Quick Ratio (x)	0.2	0.2	0.1	0.1	0.2
Net Debt/Equity (X)	3.2	6.2	7.1	5.5	4.0
Net Debt/Equity ex MI (X)	3.4	6.4	7.2	5.6	4.1
Capex to Debt (%)	(0.5)	3.0	6.1	7.9	8.6
Z-Score (X)	NA	NA	NA	NA	NA

Source: Company, DBS HK

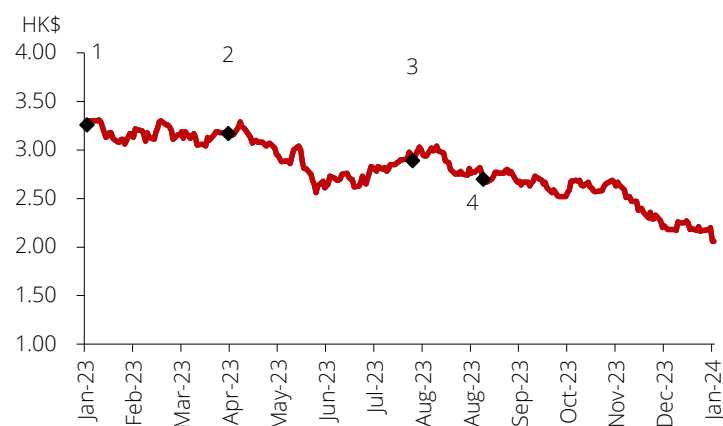
**Cash Flow Statement (RMB m)**

FY Dec	2021A	2022A	2023F	2024F	2025F
Pre-Tax Profit	(17,513)	(40,154)	(5,958)	5,863	8,744
Dep. & Amort.	22,718	21,799	23,979	25,178	26,437
Tax Paid	(136)	(312)	(46)	46	68
Assoc. & JV Inc/(loss)	141	197	(100)	(300)	(300)
(Pft)/ Loss on disposal of FAs	0	0	0	0	0
Chg in Wkg.Cap.	(3,016)	4,399	2,689	1,719	(58)
Other Operating CF	(2,809)	2,360	1,400	0	0
<b>Net Operating CF</b>	<b>(615)</b>	<b>(11,711)</b>	<b>21,964</b>	<b>32,505</b>	<b>34,891</b>
Capital Exp.(net)	943	(6,624)	(12,500)	(15,000)	(15,000)
Other Invt.(net)	0	0	0	0	0
Invt in Assoc. & JV	0	0	0	0	0
Div from Assoc & JV	0	0	0	0	0
Other Investing CF	1,212	(668)	0	0	0
<b>Net Investing CF</b>	<b>2,155</b>	<b>(7,292)</b>	<b>(12,500)</b>	<b>(15,000)</b>	<b>(15,000)</b>
Div Paid	0	0	0	0	0
Chg in Gross Debt	(7,948)	20,597	(15,000)	(15,000)	(15,000)
Capital Issues	11,103	14,998	0	0	0
Other Financing CF	626	(12,010)	0	0	0
<b>Net Financing CF</b>	<b>3,781</b>	<b>23,585</b>	<b>(15,000)</b>	<b>(15,000)</b>	<b>(15,000)</b>
Currency Adjustments	(22)	9	0	0	0
Chg in Cash	5,299	4,591	(5,536)	2,505	4,891
Opg CFPS (RMB)	0.13	(0.72)	0.86	1.38	1.57
Free CFPS (RMB)	0.02	(0.82)	0.42	0.79	0.89

Source: Company, DBS HK

## China Eastern Airlines

### H Share - Target Price & Ratings 12-mth History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	19-Jan-23	HK\$3.26	HK\$3.40	Hold
2:	11-Apr-23	HK\$3.18	HK\$3.50	Hold
3:	27-Jul-23	HK\$2.96	HK\$2.80	Hold
4:	6-Sep-23	HK\$2.77	HK\$3.00	Hold

Source: DBS HK

Analyst: Paul YONG

### A Share - Target Price & Ratings 12-mth History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	19-Jan-23	RMB5.39	RMB5.00	Hold
2:	11-Apr-23	RMB5.40	RMB5.20	Hold
3:	27-Jul-23	RMB4.77	RMB4.40	Hold
4:	6-Sep-23	RMB4.38	RMB4.70	Hold

Source: DBS HK

Analyst: Paul YONG

## China Eastern 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)

**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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Sources for all charts and tables are DBS HK unless otherwise specified.

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## China Eastern Airlines

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