

AirAsia Group Berhad

(5099 | AAGB MK) Main | Consumer Products & Services

Capacity crunches ahead

KEY INVESTMENT HIGHLIGHTS

- **FY19 earnings were below expectations**
- **Healthy load factors did not come at the expense of average fares**
- **RPK growth outgrew expansion in ASK target which helped maintained a healthy load factor**
- **Capacity cuts for TAA and MAA inevitable**
- **Implementation of crack spread hedging has started**
- **Earnings estimates adjusted downwards**
- **Maintain NEUTRAL with a revised TP of RM1.14 per share**

Below expectations. The AAGB recorded a FY19 normalised net loss of -RM345.7m (vs the RM77.1m net profit in FY18) missing ours and consensus' expectations by a variance of more than 10%. The negative variance was due to the substantial increase in finance costs-lease liabilities and depreciation of right of use of asset following the MFRS16 adoption which was more than what we had expected. In addition, there was higher maintenance expense due to higher number of leased aircraft following leasor requirements. Moving forward, FY19 will serve as a new base with regard to the impact of the MFRS 16 adoption.

RPK growth outgrew expansion in ASK....AAGB's FY19 revenue was up by +12.5%yoy to RM12.0b. The robust growth was due to another record breaking number of passengers carried in 4QFY19 of 13.2m which was supported by the year-end festive season. As a result, the number of passengers carried in FY19 grew by 16.0%yoy to 51.6m. With strong growth in passengers carried, the 13.3%yoy growth in RPK to 63,381m outpaced the ASK growth rate of 12.6%yoy in MFY19.

....which helped maintained a healthy load factor. As such, the load factor in FY19 remained robust at 85.7%. This was despite the 17.6%yoy increase of international routes for its AOCs (Indonesia and the Philippines) and net addition of 23 aircraft. More importantly the strong load factor did not come at a cost at a lower average fares. In fact, there was a +2.9%yoy increase in average fares for FY19.

Beefing up its non-airline businesses. The increase in passengers which contributed to higher FY19 ticket sales of +20.3% to RM9.2b, also resulted in airline related ancillary income revenue to grow by +11.5%yoy. As for non-airline ancillary segments, total revenue more than doubled to RM697.0m. Most of the contribution for non-airline ancillary revenue came from Teleport at 69.0% which also exceeded its RM400m revenue target. While logistics will face headwinds from the Covid-19 outbreak, Teleport will be focusing more on 'teleport.social' and parcel delivery business.

Maintain NEUTRAL

Revised Target Price: RM1.14
Previously RM1.20

RETURN STATISTICS

Price @ 27 th Feb 2020 (RM)	1.11
Expected share price return (%)	+2.70
Expected dividend yield (%)	+1.60
Expected total return (%)	+4.30

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-26.0	-23.7
3 months	-34.7	-31.7
12 months	-41.4	-33.6

KEY STATISTICS

FBM KLCI	1,505.59
Syariah compliant	Yes
Issue shares (m)	3341.97
Estimated free float (%)	53.79
Market Capitalisation (RM'm)	3,709.59
52-wk price range	RM1.1 - RM2.15
Beta vs FBM KLCI (x)	1.52
Monthly velocity (%)	67.90
Monthly volatility (%)	16.62
3-mth average daily volume (m)	23.16
3-mth average daily value (RM'm)	30.12
Top Shareholders (%)	
TUNE LIVE SDN BHD	16.73
Tune Air Sdn Bhd	15.45
Employees Provident Fund Board	4.77

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New prudent hedging policies ahead to mitigate oil price volatility. For FY19, the group experienced a +12.8%yoy rise in opex, partly attributable to the +7.5%yoy increase in aircraft fuel expenses amidst capacity expansion in FY19. Nevertheless, the increase was not as profound in FY18 when fuel expenses increased by +39.5%yoy. The lower magnitude of increase in aircraft fuel expenses occurred despite the 14.9% rise in Singapore jet kerosene during FY19; and (ii) the 15.5%yoy increase in the number of flights for the same period. This indicates that AAGB's conservative hedging strategy came to fruition. For 4QFY19, the average hedge ratio of AAGB was at ~86.0% at a Brent crude oil price of USD60.72pb of compared to just ~15.0% in the whole FY18. In light of low oil prices, AAGB has started to implement 18-21% crack hedges from 1QFY20 to 3QFY20, ranging from USD8.42 to USD11.89. Usual crack spreads range from USD13.00 to USD15.00. This should mitigate the average Brent hedging losses if oil prices were to remain below USD60pb for an extended period.

Actions taken in the wake of Covid-19 outbreak. The capacity catered for destinations in china by AAGB make up around 13.0% of Malaysia AirAsia's (MAA) total capacity. Thus far, all flights to Wuhan under AAGB have been cancelled while MAA has reduced capacity to certain parts of mainland China and enabled passengers on such routes to obtain a credit account or full refund. Overall in 1Q20, AAX has slashed overall capacity for MAA and Thailand Airasia (TAA) by -10% and -23% respectively in light of the Covid-19 outbreak. Meanwhile, AAGB carried out the RM12 Malaysia domestic campaign which resulted in 30.0% incremental revenue on a monthly basis. Discounts of up to 30.0% were also offered across AAGB network but we opine that it will be less effective as travellers are becoming increasingly cautious from the spread of the Covid-19.

Impact to earnings. As the Covid-19 has spread further in countries outside of China, global travel demand will continue to wane, prompting further capacity cuts across AAGB's network. Following this, we are now expecting a decline instead of a smaller growth in RPK especially for MAA and TAA which will drag down load factors below 80.0%. As a result our earnings estimates for FY20 and FY21 have been reduced to RM244.5m (previously RM444.5m) and RM381.6m (previously RM540.8m). We are also introducing our FY22 earnings estimates.

Target price. We revised our **target price to RM1.14 per share** (from RM1.20 previously) as we roll forward our valuation base year and revise our earnings estimates downwards. Our target price is derived via pegging our FY201F EPS of 11.4sen to an unchanged target PER of 10x. The target PER is a discount to the average PER of AAGB's global peers of 13x to reflect the tough operating environment following its exposure to China.

Maintain NEUTRAL. While passengers carried are bound for a temporary decline during a virus outbreak, AirAsia Indonesia and AirAsia India will partially buffer the shortfall in MAA and TAA. Aside from that, AAGB's efforts in its non-airline business represented by Teleport, BigPay, AirAsia.com and RedBeat Ventures will continue growing. Teleport is expected to remain strong as it solidifies its 'teleport.social' platform and parcel delivery operations. All in, we maintain our **NEUTRAL** amidst the overall tough operating environment. 

INVESTMENT STATISTICS

Financial year ending 31 st Dec (in RM'm, unless otherwise stated)	2018A	2019E	2020F	2021F	2022F
Revenue	10,638.3	11,964.9	11,605.9	12,144.6	13,112.8
EBITDA	1,803.7	2,730.6	2,321.2	2,671.8	2,884.8
EBIT	1,218.9	742.9	812.4	935.1	1,125.1
PBT	1,335.2	(549.8)	568.7	720.1	877.6
Reported Net Profit	1,695.4	(412.3)	244.5	381.6	570.4
Core Net Profit	767.1	(345.7)	244.5	381.6	570.4
Core EPS (sen)	23.0	(10.3)	7.3	11.4	17.1
Core EPS growth (%)	-41.3%	-145.1%	-170.7%	56.1%	49.5%
PER (x)	5.6	-12.4	17.5	11.2	7.5
Net Dividend (sen)	64.0	102.0	0.0	2.0	2.0
Net Dividend Yield (%)	50.0%	79.7%	0.0%	1.6%	1.6%

Source: Company, MIDFR

Note: *Special dividend of RM0.40 and two interim dividend of RM0.12 per share in FY18

** Includes special dividend of RM0.90 to be paid on 29 August 2019

AirAsia: 4QFY19 RESULTS SUMMARY

<i>All in Rm'm unless stated otherwise</i>	Quarterly Results					Cumulative		
FYE Dec	4Q19	3Q19	4Q18	%QoQ	%YoY	12M19	12M18	%YoY
Revenue	3,212.0	2,945.2	2,725.0	9.1	17.9	11,964.9	10,638.3	12.5
-ticket sale	2,567.9	2,261.8	2,067.0	13.5	24.2	9,207.7	7,656.8	20.3
-ancillary income	490.7	588.9	550.5	-16.7	-10.9	2,104.5	2,132.6	-1.3
-lease income	153.4	94.5	107.5	62.3	42.7	653.9	848.9	-23.0
Operating exp.	(3,267.7)	(2,867.6)	(3,315.3)	-13.9	1.4	(11,631.6)	(10,308.5)	12.8
Total EBITDA	593.7	753.1	(36.7)	-21.2	1718.9	2,730.6	1,803.7	51.4
Depreciation	(557.5)	(488.8)	(151.6)	-14.1	-267.7	(1,987.6)	(584.7)	239.9
EBIT	36.2	264.3	(188.3)	-86.3	119.2	742.9	1,218.9	-39.0
Interest income	31.4	16.1	39.8	94.7	-21.2	71.6	63.3	13.0
Interest exp.	(215.8)	(216.5)	(71.9)	0.3	-200.2	(787.0)	(474.8)	65.8
Forex	174.6	(112.0)	69.5	255.9	151.2	154.9	126.8	22.1
Contr.of JV and assoc.	(225.7)	(61.8)	(54.8)	-265.4	-312.2	(481.6)	(11.0)	4264.4
Others	(33.1)	(237.7)	(165.8)	86.1	80.0	(247.6)	(200.2)	23.7
Pre-tax profit	(232.5)	(347.6)	(371.4)	33.1	37.4	(549.8)	1,335.2	-141.2
PATAMI	(384.4)	(51.4)	(395.0)	-647.3	2.7	(303.7)	1,967.0	-115.4
E.I.	(441.0)	125.7	(130.5)	-450.8	-237.8	42.0	(1,199.9)	-103.5
Core PATAMI	56.5	(177.1)	(264.4)	131.9	121.4	(345.7)	767.1	-145.1
Operating stat	4Q19	3Q19	4Q18	%QoQ	%YoY	12M19	12M18	%YoY
Passenger carried ('000)	13,169.2	13,002.2	12,109.1	1.3	8.8	51,559.1	44,437.4	16.0
Capacity ('000)	16,021.0	15,501.6	14,380.1	3.4	11.4	60,884.6	52,537.0	15.9
RPK (m)	15,916.0	16,021.0	14,962.0	-0.7	6.4	63,381.0	55,964.0	13.3
ASK (m)	19,185.0	19,024.0	17,870.0	0.8	7.4	74,642.0	66,261.0	12.6
Load factor (%)	83.0%	84.2%	83.7%	-1.25	-0.77	84.9%	84.5%	0.5
average fare (RM)	190.0	176.0	171.0	8.0	11.1	177.8	172.8	2.9
Fuel Expenses	(1,095.5)	(1,066.5)	(1,110.2)	2.7	-1.3	(4,204.8)	(3,909.8)	7.5
Unit fuel cost (USD/b)	83.0	85.0	92.0	-2.4	-9.8	84.5	89.8	-5.8
% fuel cost of OPEX	33.5%	37.2%	33.5%	-3.67	0.04	35.8%	38.4%	-6.6
RASK (sen/km)	16.1	15.0	14.8	7.1	8.6	15.4	14.8	4.4
CASK (sen/km)	16.4	15.3	16.6	7.1	-1.3	15.5	14.6	6.5
USD/MYR	4.2	4.2	4.2	-0.4	-0.3	4.1	4.0	2.6
RASK-CASK	(0.3)	(0.3)	(1.8)	3.7	-84.1	(0.1)	0.2	-147.0
Ancillary per pax	37.3	45.3	45.5	-17.7	-18.0	163.3	169.5	-3.6
Unit passenger revenue	234.0	215.0	218.0	8.8	7.3	220.8	218.8	0.9
Aircraft	149.0	147.0	141.0	1.4	5.7	141.0	141.0	0.0
Average stage length	1,207.0	1,224.0	1,240.0	-1.4	-2.7	1,225.8	1,254.0	-2.3
Number of flights	88,175.0	85,403.0	79,394.0	3.2	11.1	335,399.0	290,461.0	15.5
Yields (Rev/RPK)	19.2	17.8	17.5	8.0	9.8	17.8	17.5	2.0

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.