

# AirAsia Group Berhad

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

## Double whammy on AAGB

### KEY INVESTMENT HIGHLIGHTS

- **Capacity cuts are inevitable amidst coronavirus outbreak**
- **International flight license in India to possibly face headwinds**
- **AAGB began to hedge for crack spread in light of weak oil prices**
- **Co-founders of AAGB have relinquished their executive roles following the alleged Airbus corruption case**
- **Earnings estimates unchanged**
- **Downgrade to NEUTRAL with revised TP of RM1.20 per share on adjustment to valuation**

**Capacity cuts are inevitable.** As highlighted in our report dated 30 January 2020, we have slashed earnings forecast for AAGB following a more conservative capacity assumption in light of the coronavirus outbreak. Recall that AAGB's capacity to China stands at around 13% of overall capacity. With capacity management being in focus to manage load factors, we understand that this could result in a delay for the 12 net additions of new aircraft for (6 A321neos, 6 A320 neos) in FY20. Nevertheless, AAGB may renew its lease contracts for five aircraft that are expiring in 2020. This would lead to cheaper lease rates, cushioning the ongoing impact of the MFRS 16. On a broader scale, AAGB noted that the delays of the Boeing 737 Max coming back into service had a neutral impact towards the overall leasing market.

**Expansion plans for India expected to stay on track.** We gathered that AirAsia India may stick to the current capacity expansion plans given growth prospect in the Sub Continent. Meanwhile, AAGB is still in the midst of obtaining the international flight license from the government. We foresee granting of international flight license to drag for another few months as the overall travel sentiment particularly in Asia is already badly affected following the coronavirus. The overseas permit was expected to be granted to AirAsia India by October 2019 after the Delhi High Court refused a plea to stop the award of overseas permit to the company.

**Slight changes in hedging policy.** In light of the sharp drop in Brent crude oil to below USD60pb, AAGB recently began to hedge the crack spread (difference between Brent price and jet fuel price) at around USD10pb (crack spread is usually USD12pb to USD14pb), representing roughly 15% of fuel requirements. As a result, AAGB's current effective jet fuel price is approximately USD70pb, lower than was previously budgeted.

**Potential questions on corporate governance issues may arise.** Another concern which had arisen lately is the alleged Airbus corruption case which court documents state involve two executives of AAGB and AAX. AAGB has denied these allegations against both AAGB and AAX. Meanwhile, the Malaysian Anti-Corruption Commission (MACC) announced that investigations with the authorities in the U.K have begun while MAVCOM will assess if there is any contravention of the MAVCOM Act 2015 (Act 771) and the Commission's Guidelines on Fit and Proper Person.

## Downgrade to NEUTRAL

(from BUY)

**Revised Target Price: RM1.20**

(Previously RM1.86)

### RETURN STATISTICS

Price @ 3rd Feb 2020 (RM)	1.28
Expected share price return (%)	-6.25
Expected dividend yield (%)	+6.30
Expected total return (%)	-0.05

### SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-24.3	-19.8
3 months	-24.7	-29.5
12 months	-38.5	-31.9

### KEY STATISTICS

FBM KLCI	1,521.95
Syariah compliant	Yes
Issue shares (m)	3341.97
Estimated free float (%)	52.25
Market Capitalisation (RM'm)	4,277.73
52-wk price range	RM1.27 - RM2.25
Beta vs FBM KLCI (x)	1.60
Monthly velocity (%)	49.20
Monthly volatility (%)	16.62
3-mth average daily volume (m)	6.85
3-mth average daily value (RM'm)	11.68
Top Shareholders (%)	
TUNE LIVE SDN BHD	16.73
Tune Air Sdn Bhd	15.45
Employees Provident Fund Board	6.31

**Analyst(s)**

**ADAM** Mohamed Rahim  
adam.mrahim@midf.com.my  
03-2772 1686

The timeline of the investigation on the alleged corruption case by the MACC and MAVCOM could not be estimated given the lack of precedence of such cases in the country. Until the outcome of the investigations are known, precautions have to be taken in valuing the company as any adverse findings could pose an impact to the airline's reputation and potential financial penalties. Nevertheless, if the allegations are found to be untrue, this will serve as a golden opportunity for both co-founders to strengthen their trustworthiness back in the company and subsequently, the airline industry. In response to this alleged case its co-founders have decided to relinquish their executive roles in the airlines but retained as advisors, effective from 3 February 2020 for a two-month period. In the interim, AAGB's deputy group CEO for airlines business, Tamarulingam Kanagalingam has been appointed as the acting CEO.

**Earnings estimates.** No changes made to our earnings estimates.

**Target Price.** While we are maintaining our estimates, we are adjusting our target price to RM1.20 per share (RM1.86 previously). Our target price is derived via pegging our FY20F EPS of 13.3sen to a target PER of 9x (previously 14x). We are lowered our valuation premised on the ongoing uncertainties from the coronavirus outbreak and Airbus case. However, the lower adjusted target PER is still a discount from AAGB's regional peers which are trading at a 12-month trailing PER of 14x on average.

**Downgrade to NEUTRAL (from BUY).** Operationally, we view that AAGB's efforts in its non-airline business represented by Teleport, BigPay, AirAsia.com and RedBeat Ventures to continue growing. Teleport is on track to meet the RM400m target in FY19 enhanced via 'teleport.social' while AirAsia.com effectively intensifies competition with other Online Travel Agents (OTAs). Notwithstanding, the recent corruption case allegedly involving AAGB could be an overall sentiment dampener to the company especially in an operating environment that is already facing headwinds. All in, we are downgrading AAGB to **NEUTRAL** from **BUY**. 

## INVESTMENT STATISTICS

Financial year ending 31 <sup>st</sup> Dec (in RM'm, unless otherwise stated)	2017A	2018A	2019E	2020F	2021F
<b>Revenue</b>	<b>9,709.7</b>	<b>10,638.3</b>	<b>10,974.9</b>	<b>11,433.1</b>	<b>12,162.2</b>
EBITDA	3,024.8	1,803.7	2,195.0	2,286.6	2,675.7
EBIT	2,160.8	1,218.9	482.9	731.7	936.5
PBT	2,087.8	1,335.2	265.6	592.7	721.1
Reported Net Profit	1,571.4	1,695.4	199.2	444.5	540.8
<b>Core Net Profit</b>	<b>1,307.9</b>	<b>543.6</b>	<b>199.2</b>	<b>444.5</b>	<b>540.8</b>
Core EPS (sen)	39.1	16.3	6.0	13.3	16.2
Core EPS growth (%)	-4.7%	-58.4%	-63.4%	123.2%	21.7%
PER (x)	3.3	7.9	21.5	9.6	7.9
Net Dividend (sen)	12.0	64.0	102.0	8.0	8.0
Net Dividend Yield (%)	9.4%	50.0%	79.7%	6.3%	6.3%

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

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### MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

#### STOCK RECOMMENDATIONS

<b>BUY</b>	Total return is expected to be >10% over the next 12 months.
<b>TRADING BUY</b>	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.
<b>NEUTRAL</b>	Total return is expected to be between -10% and +10% over the next 12 months.
<b>SELL</b>	Total return is expected to be <10% over the next 12 months.
<b>TRADING SELL</b>	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

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