AirAsia Group Berhad

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

Downward pressure on passengers carried expected albeit for a short period

***Maintain* BUY**

***Revised* Target Price: RM1.86**
(Previously RM2.04)

KEY INVESTMENT HIGHLIGHTS

- **4QFY19 preliminary ASK and RPK inched higher due to additional frequencies and routes**
- **Still expecting a normalized PAT of RM199.2m for FY19 due to MFRS16 impact**
- **Passengers carried to and from China expected to face temporary headwinds due to the pandemic outbreak**
- **Adjusting earnings downwards to reflect lower RPK**
- **Maintain BUY with revised TP of RM1.86 per share**

4QFY19 preliminary ASK and RPK inched higher. In 4QFY19, AAGB's consolidated AOCs (Malaysia, Indonesia and Philippines) recorded a preliminary RPK growth of 6.0%, Meanwhile, the ASK grew slightly higher by 7.0% during the same period. As such, the load factor remained healthy above 80.0% at 82.0% in 4QFY19. The growth seen in these operational statistics was partially attributable to the launch of the Kuala Lumpur to Da-Lat, Vietnam route and the commencement of flights utilizing the first Airbus A321neo in late 2019 by AirAsia Malaysia. Apart from that, Airasia Indonesia launched six new routes while AirAsia Philippines added frequencies to popular destinations such Bangkok, Cagayan de Oro and Caticlan.

Expecting a solid 4QFY19 financial performance. Following the year-on-year improvement in operational statistics for 4QFY19, we are expecting AAGB to record a normalized profit after tax of more than RM50m in the same period. This is in contrast with the >RM200m loss recorded in 4QFY18 caused by the +48.4%yoy increase in fuel price expense to RM3.9b and higher operating lease expenses due to the completion of AAGB's sale and leaseback transaction with BBAM. All in, we are still estimating a normalised profit after tax (PAT) of RM199.2m for FY19. Although normalized PAT in FY19 is expected to be lower than in FY18, FY19 should be viewed as a new base following the effects of the implementation of MFRS16 beginning January 2019.

Potential impact from coronavirus outbreak. According to past figures during the 2003 SARS outbreak, MAHB's passenger traffic growth in Malaysia took a breather that year to fall by just -1.5%yoy to 33.5m. In addition, total international passengers at KLIA Main Terminal travelling to and from China declined by -10.7%yoy during the same period. Henceforth, it would be apt to consider any potential impact that the coronavirus outbreak towards the passengers carried by AAGB. Management guided that the AAGB's ASK for China routes contributes approximately 10% to 15% of the total ASK. In comparison with AAGB's long-haul affiliate, AAX, we opine that the ASK for China routes is higher given the non-exposure to ASEAN.

RETURN STATISTICS	
Price @ 29th Jan 2020 (RM)	1.48
Expected share price return (%)	+25.70
Expected dividend yield (%)	+8.10
Expected total return (%)	**+33.80**

SHARE PRICE CHART

Share price performance (%)	Absolute	Relative
1 month	-13.5	-10.1
3 months	-12.9	-21.1
12 months	-30.9	-24.7

KEY STATISTICS	
FBM KLCI	1,550.47
Syariah compliant	Yes
Issue shares (m)	3341.97
Estimated free float (%)	52.02
Market Capitalisation (RM'm)	4,946.12
52-wk price range	RM1.4 - RM2.25
Beta vs FBM KLCI (x)	1.55
Monthly velocity (%)	49.2
Monthly volatility (%)	16.62
3-mth average daily volume (m)	6.46
3-mth average daily value (RM'm)	11.25
Top Shareholders (%)	
TUNE LIVE SDN BHD	16.73
Tune Air Sdn Bhd	15.45
Employees Provident Fund Board	6.54

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Worst-case scenario analysis. We understand that passengers flying to or from destination in mainland China are given an option for a credit account or full refund. Assuming a worst case scenario where all affected passengers in its mainland China routes opted for a full refund, we estimate that RPK could decline by as much as 10% to 20%, lowering the load factor below 80.0% assuming capacity remains unchanged. This in turns reduces AAGB profit after tax by 7.0%. Nevertheless, it was noteworthy that the passenger traffic at MAHB's Malaysian airports rebounded +17.8%yoy in 2004. Similarly, international passengers from China at KLIA Main Terminal recorded a whopping +75.8%yoy growth in 2004.

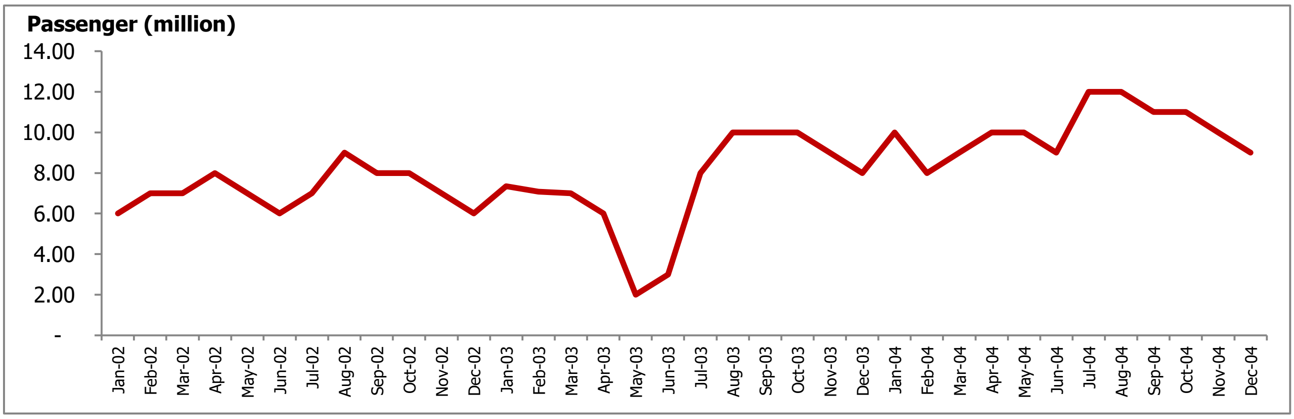
Table 1: Growth in Passengers to and from China at KLIA Main Terminal

Year	Total Passengers to and from China at KLIA Main Terminal (million)	% growth
2002	0.64	N/A
2003	0.57	-10.7
2004	1.00	+75.8
2005	1.25	+24.7

Source: MAHB

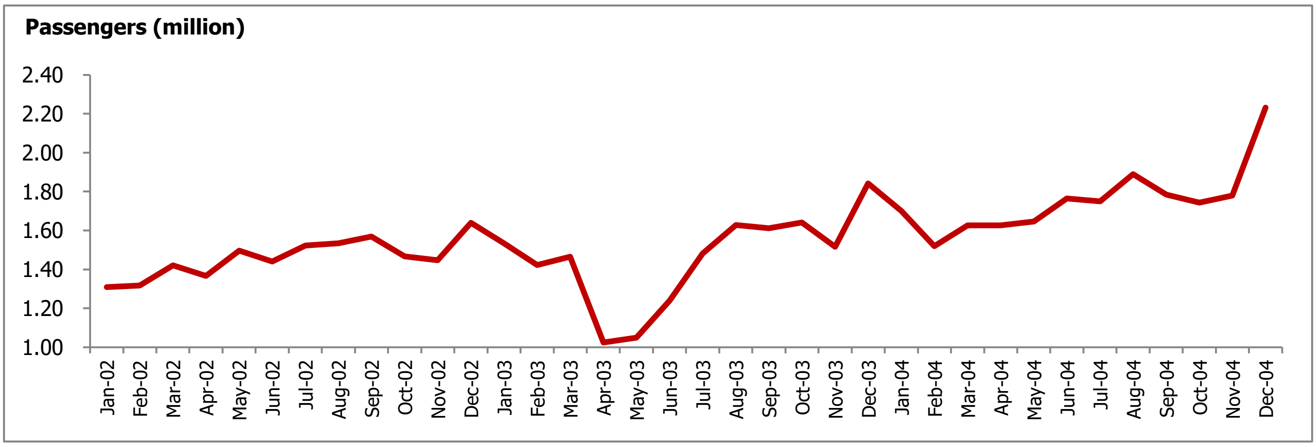
SARS outbreak in 2003 saw a quick recovery in monthly passenger growth. Moreover, we found that during the SARS outbreak between November 2002 and July 2003, passenger traffic took an average of two to three months to normalise. For instance in Malaysia, April 2003 saw a huge -30.1%mom drop to reach the lowest point that year of 1.02m passengers before increasing +18.1%mom in June 2003 and another +19.6%mom increase in July 2003 to reach back a normal level of 1.48m passengers. As for China, May 2003 saw a -66.7%mom decrease in passengers before advancing +50.0%mom in June 2003 and another +166.7%mom gain in July 2003. Given that this was nearly 20 years ago, we believe that technological advancements in the healthcare sector will likely contain the disease better.

Figure 1: Monthly Passenger Traffic in China during SARS Outbreak



Source: CEIC Data

Figure 2: Monthly Passenger Traffic in Malaysia during SARS Outbreak



Source: MAHB

Earnings estimates. The expected temporary disruption to its China routes warrants a downward revision in our RPK growth assumptions, albeit only a slight one given that we expect the passenger carried will normalized within 2 to 3 months based on past experience. We are now imputing a lower RPK growth of 4.0% (previously 6.0%) for FY20. As a result, our earnings estimates for FY20 and FY21 have been reduced by -2.0% and -4.0% from RM453.7m to RM563.6m to RM444.5m and RM540.8m respectively.

Target Price. Following the revision in our earnings estimates**,** we are adjusting our target price to **RM1.86 per share** (RM02.04 previously). Our target price is derived via pegging our FY20F EPS of 13.3sen to a target PER of 14x. The target PER is premised on AAGB's regional peers which are trading at a 12-month trailing PER of 14x on average.

Maintain BUY. We believe that Air Asia's operation continue to remain sound. We continue to like Air Asia as the company continues enhance its cost structure, along with its efforts of rationalising revenue and cost via digitalisation efforts. Our positive outlook on the AAGB also hinges on: 1) its more prudent hedging policy 2) stable operations with added capacity and 3) continuous improvement to drive its non-airline ancillary business.

Meanwhile, the adoption MFRS 16 will be a headwind in the next coming years as the majority of AAGB's fleet are leased. Nonetheless, AAGB is expected to gain from lower amount of interest beyond the fifth year of the lease term. Risks to our call are: (i) lower-than-expected travel demand and (ii) unfavourable revision of passenger service charges especially for klia2.

INVESTMENT STATISTICS

Financial year ending 31st Dec (in RM'm, unless otherwise stated)	**2017A**	**2018A**	**2019E**	**2020F**	**2021F**
Revenue	**9,709.7**	**10,638.3**	**10,974.9**	**11,433.1**	**12,162.2**
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
Core Net Profit	**1,307.9**	**543.6**	**199.2**	**444.5**	**540.8**
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)	3.8	9.1	24.8	11.1	9.1
Net Dividend (sen)	12.0	64.0	102.0	12.0	12.0
Net Dividend Yield (%)	8.1%	43.2%	68.9%	8.1%	8.1%

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*

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (197501002077 (23878-X))
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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 *rise* 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 *fall* 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.