



## The Cockpit View (Issue #15)

## OVERWEIGHT (Unchanged)

### 3Q15 looking very promising

- Expect record profits buoyed by low jet fuel prices, record load factors, and easing yield pressures.
- This coincides with rock bottom valuations and best ever balance sheets.
- Stay OVERWEIGHT, do we really need to say more?

#### What's New

3Q15 promises to be an interesting quarter filled with headline grabbing record profits. The US-based carriers have finished reporting their 3Q15 numbers and the industry recorded a stellar 53.5% YoY profit growth. The Asia Pacific carriers that have released their results delivered even more impressive performance than the US-based carriers.

#### What's Our View

Strong supply-demand dynamics have pushed load factors to record highs, which should ease the pressure on yield deterioration that has plagued the industry since late last year. Furthermore, the jet fuel price averaged USD66.1/bbl in 3Q15 (-44.6% YoY, -8.8% QoQ), which is the lowest level since 1Q09.

These stellar headlines have been our mainstay commentary for much of the year. Thus far, the sector has risen by 28% YTD and we think there is much more upside to be had given that the sector is delivering triple digit profit growth in 2015 and high double-digits in 2016. Valuations are cheap and balance sheets have never been stronger. We believe that ultimately the fundamentals will prevail and the share price will reflect it.

#### Hot Stocks of the Week

BPR AIRL Index was up by 2.3% last week. Japan and Thai based airlines enjoyed nice gains in stock prices. The Japanese carriers posted good 3Q15 results, and the latest Thai tourist arrival numbers continue to exceed expectations.

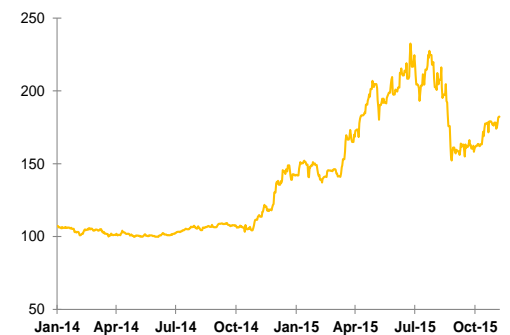
Notable underperformers were the Chinese state carriers, with the exception of Hainan Airlines. Qantas share price plunged by 6.1% last week as the CEO share sales have unnerved some investors.

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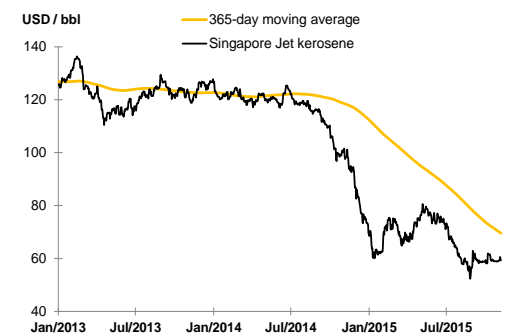
#### Bloomberg Asia Pacific Airline Index



Current trend: **Rising**

Spot	Last week	Last month	YTD (2014)
190	178	164	142
	2.3%	11.5%	28.0%

#### Jet fuel price



Current trend: **Range-bound**

Spot	YTD	2014
USD59.3/bbl	USD67.8/bbl	USD112.4/bb

#### Our recent reports

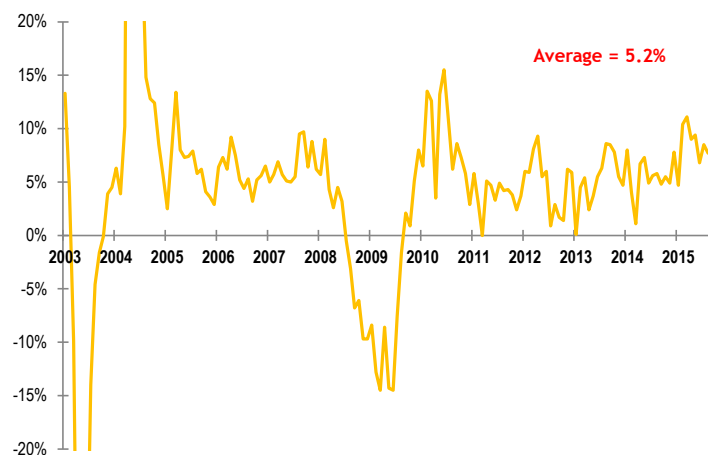
- MAHB -Cost fluctuation  
HOLD, Target price: MYR5.45 (28 Oct)
- SIA - D/G to HOLD, lacks catalyst  
HOLD, Target price: SGD11.80 (26 Oct)
- AirAsia - To be privatized?  
BUY, Target price: MYR2.05 (7 Oct)

## All the stars are aligned in 3Q15

### Mixed traffic growth

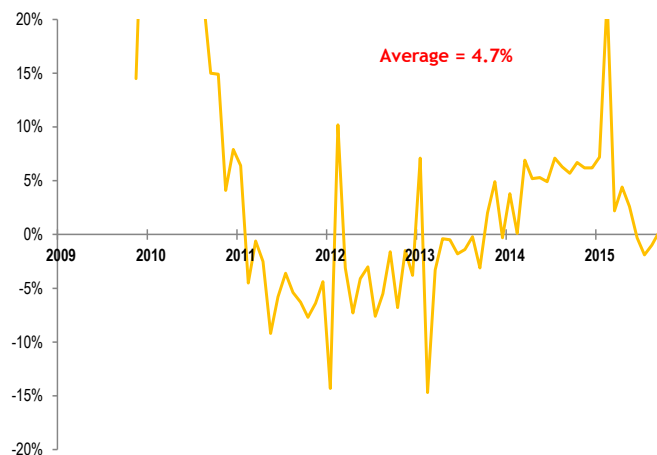
The passenger traffic growth for Asia-Pacific airlines grew by an average of 8.5% in 8M15. This is way above the long-term average of 5.2%. For cargo traffic however, the average traffic growth of 3.9% in 8M15 was below the historical average of 4.7%.

Asia-Pacific airlines' passenger traffic growth



Source: IATA

Asia-Pacific airlines' cargo traffic growth

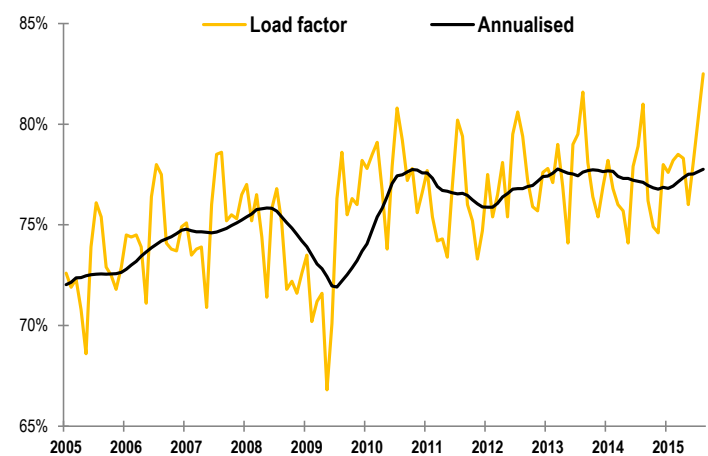


Source: IATA

### Strong load factors

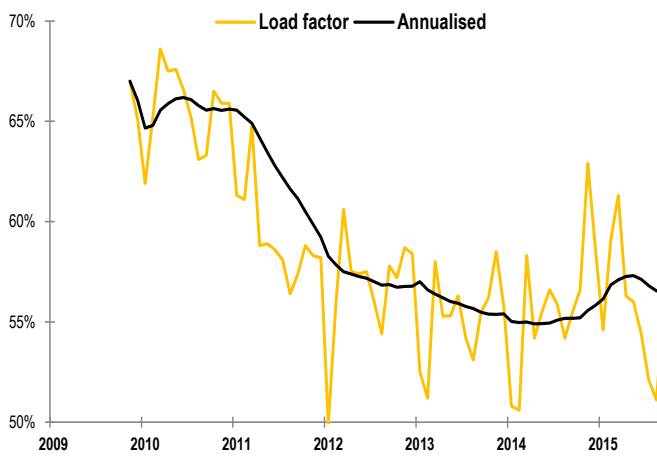
Load factors for Asia-Pacific passenger airlines are at record levels. This is despite the fact that airlines have accelerated capacity deployment in 2015, but it still trails demand growth. Clearly, the underlying demand is healthy and consumers are not cutting back their expenditures. For cargo, the load factors are well below the historical average, but we do note that there has been some incremental year-on-year improvement.

Asia-Pacific airlines' passenger load factor



Source: IATA

Asia-Pacific airlines' cargo load factor

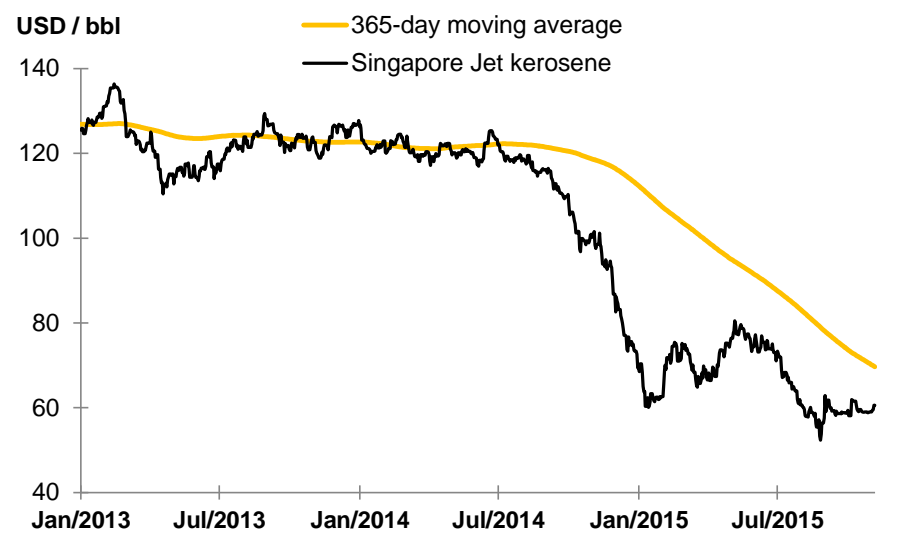


Source: IATA

## Fuel price declined by 44.5% YoY, and 8.8% QoQ

The average jet fuel price in 3Q15 was USD66.1/bbl, which is 44.5% lower than 3Q14's average jet fuel price of USD119.2, and 8.8% lower 2Q15's average jet fuel price of USD72.5/bbl. This will provide the industry with significant cost savings that will ultimately lift the profits.

### Singapore jet kerosene price (USD/bbl)



Sources: Bloomberg, Maybank KE

## Yield pressure should ease off

The average yield decline for Asia-Pacific passenger airlines in 2Q15 was 4.4% YoY and for cargo was down by 7.3% YoY for the same period, based on our calculations. Going into 3Q15, we believe that yield pressures should ease because airlines are able to fill up their aircraft to record levels and passenger demand is strong. We think YoY yields will still be in negative territory as airlines pass on some of the benefits of lower fuel prices to the customers, but the quantum of decline should be lower than that in 2Q15.

The table below shows the YoY yield movement in local currency for carriers that have already released their 3QCY15 results. Notice that most airlines have recorded respectable YoY yield performance.

### Selected Asia Pacific airlines YoY yield growth (local currency) in 3QCY2015

Airline name	YoY yield growth
Japan Airlines (domestic)	+2.2%
Japan Airlines (international)	+4.0%
All Nippon Airways (domestic)	+1.0%
All Nippon Airways (domestic)	(1.8%)
Tigerair	+8.2%
Garuda Indonesia	+2.8%
Singapore Airlines	(4.6%)
SilkAir	+0.2%
Scot Air	+1.9%

Sources: Respective airlines, Bloomberg

### Record profits galore

The table below shows the reported 3QCY15 net income numbers compared to a year ago. Notice how many of the US-based carriers are enjoying their best performance ever. Similarly, Asia-Pacific based carriers that have so far released their results all are showing strong performances. This is a good omen.

#### Selected airlines net profit in 3Q

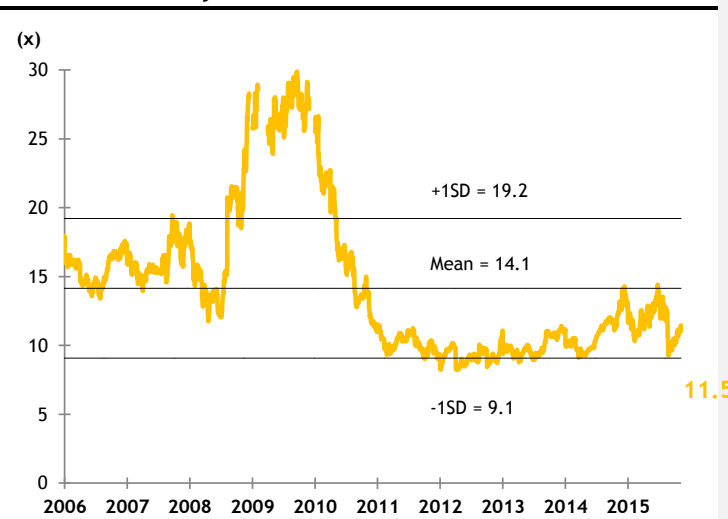
Name of airline	Net income (USD m)		YoY growth	Note
	3Q15	3Q14		
<b>US based carriers</b>				
Delta Air Lines	1,384	1,014	36.5%	
American Airlines	1,885	1,217	54.9%	Record quarter
United Continental	1,702	1,062	60.3%	Record quarter
Alaska Air	277	200	38.5%	Record quarter
Hawaiian Holdings	78	50	58.4%	
SouthWest Airlines	623	382	63.1%	Best 3Q in record
JetBlue Airways	198	91	116.6%	
Spirit Airlines	97	68	44.1%	Record quarter
Allegiant Travel	44	14	212.0%	
<b>Sub-total</b>	<b>6,289</b>	<b>4,098</b>	<b>53.5%</b>	
<b>Asia-Pacific carriers</b>				
Japan Airlines	580	344	68.3%	
All Nippon Airways	373	145	157.3%	
Tigerair	(9)	(146)	>>	
Garuda Indonesia	22	(8)	>>	
Singapore Airlines	154	73	111.6%	

Sources: Respective airlines, Bloomberg

### Sector really cheap, not reflecting strong fundamentals

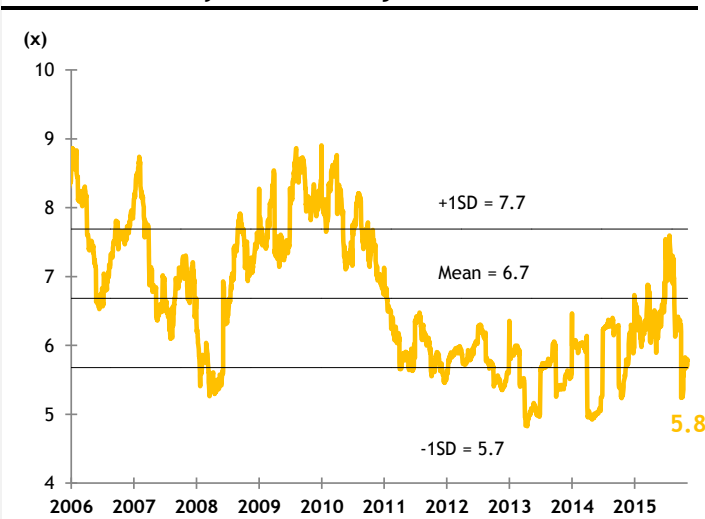
The graph below shows the BPRAIRL Index's 1-year forward P/E, currently at 11.5x. This is well below its mean of 14.1x. On an adjusted EV/EBITDAR basis, it is at 5.7x, or 1SD below its mean. Such valuations are not in sync with an industry enjoying triple-digit earnings growth with a bright outlook, in our view. We believe the sector is very cheap and maintain our OVERWEIGHT call.

BPRAIRL Index 1-year forward PER



Source: Bloomberg

BPRAIRL Index 1-year forward adjusted EV/EBITDAR



Source: Bloomberg

## Asia Pacific airlines share price movement

Company Name (alphabetical order)	Bloomberg Ticker	Price 6-Nov	Current share price versus			Comments
			1 week	1 month	1 year	
Air China	753 HK	7.16	-4.4%	15.3%	37.0%	Rebound of Chinese equity markets
Air New Zealand	AIR NZ	2.85	-2.1%	10.5%	47.7%	
AirAsia	AIRA MK	1.44	-2.7%	9.1%	-43.2%	In line with general market weakness
AirAsia X	AAX MK	0.21	0.0%	-2.4%	-67.3%	In line with general market weakness
All Nippon	9202 JP	371	2.4%	7.6%	45.2%	
Asia Aviation	AAV TB	4.80	3.9%	6.7%	12.1%	In line with general market weakness
Asiana Airlines	020560 KS	4,900	1.1%	-1.4%	14.2%	
Bangkok Airways	BA TB	20.00	-0.5%	0.0%		
Cathay Pacific	293 HK	15.32	-0.8%	2.1%	7.2%	Rebound of Chinese equity markets
Cebu Air	CEB PM	88.95	-0.3%	2.5%	15.5%	
China Airlines	2610 TT	11.75	0.9%	5.9%	-0.8%	Rebound of Chinese equity markets
China Eastern	670 HK	4.90	-2.2%	7.0%	57.1%	Rebound of Chinese equity markets
China Southern	1055 HK	6.36	-3.5%	14.4%	116.8%	Rebound of Chinese equity markets
EVA Airways	2618 TT	19.20	0.5%	5.8%	8.4%	Rebound of Chinese equity markets
Garuda Indonesia	GIAA IJ	319	-0.3%	1.3%	-38.7%	
Hainan Airlines	600221 CH	4.25	6.3%	9.8%	71.6%	
Japan Airlines	9201 JP	4,597	0.4%	6.3%	53.0%	Analysts cut target price
Korean Air Lines	003490 KS	31,000	0.5%	-2.2%	-11.8%	Analysts upgrade stock
Nok Air	NOK TB	7.55	-1.3%	5.6%	-44.1%	2Q15 results below market expectations
Qantas Airways	QAN AU	3.90	-6.1%	-0.5%	123.7%	Market reacted to weakening AUD/USD
Singapore Airlines	SIA SP	11.14	3.1%	4.7%	12.1%	
Thai Airways	THAI TB	10.30	2.0%	-1.9%	-27.5%	
Tiger Airways	TGR SP	0.41	41.4%	32.3%	56.4%	
TransAsia Airways	6702 TT	7.76	0.8%	13.3%	-30.0%	Rebound of Chinese equity markets
Virgin Australia	VAH AU	0.48	-1.0%	-1.0%	21.8%	Market reacted to weakening AUD/USD
<b>Average</b>			<b>1.5%</b>	<b>6.0%</b>	<b>18.2%</b>	

Sources: Bloomberg, Maybank KE

Airlines with notable gains last week were both the Japanese based carriers and the Thai based airlines. This is on the back of good 3Q15 results posted by the Japanese carriers, whereas Thai tourist arrival numbers for the month of August 2015 were exceptionally strong.

Notable underperformers are the Chinese state carriers, with the exception of Hainan Airlines. Qantas share price plunged by 6.1% last week as the CEO share sales have unnerved some investors.

## Asia-Pacific airline valuations

Company Name <i>alphabetical order</i>	Ticker	Our Rating	Price 6-Nov	Target Price	Up / (down)	MCAP (USD b)	PE (x)		EV/EBITDAR (x)		P / Book (x)		ROE (%)	Gearing (%)
							2015	2016	2015	2016	2015	2016		
<b>Full service carriers</b>														
Air China	753 HK	NR	7.16			17.4	8.3	7.7	6.9	6.7	1.32	1.20	14.1	177
Air New Zealand	AIR NZ	NR	2.85			2.1	5.8	7.1	3.8	4.2	1.63	1.43	17.0	51
All Nippon Airways	9202 JP	NR	371.1			10.6	19.3	16.5	6.7	6.2	1.59	1.54	7.3	62
Asiana Airlines	020560 KS	NR	4900			0.8	n.a	11.1	10.6	9.4	0.95	0.94	na.	322
Bangkok Airways	BA TB	BUY	20.0	28.0	40.0%	1.2	20.2	17.6	8.8	7.7	1.66	1.54	2.2	(1)
Cathay Pacific	293 HK	BUY	15.32	21.1	37.7%	7.8	8.4	7.2	5.8	4.9	1.10	1.06	9.5	86
China Airlines	2610TT	NR	11.75			2.0	8.2	8.3	6.1	6.0	1.16	1.10	11.6	211
China Eastern	670 HK	NR	4.90			14.4	7.4	7.0	7.3	6.8	1.52	1.27	24.2	304
China Southern	1055 HK	NR	6.36			12.2	7.9	7.0	5.6	5.5	1.32	1.25	17.5	219
EVA Airways	2618 TT	NR	19.2			2.3	8.6	9.3	6.2	6.1	1.51	1.45	6.8	143
Garuda Indonesia	GIAA IJ	NR	319			0.6	11.6	7.8	4.8	4.1	0.71	0.61	na.	80
Hainan Airlines	600221 CH	NR	4.25			8.2	12.0	9.9	8.0	6.6	1.72	1.73	9.1	178
Japan Airlines	9201 JP	NR	4597			13.5	9.8	9.2	5.1	4.7	2.00	1.82	22.4	(33)
Korean Airlines	003490 KS	NR	31000			2.0	n.a	8.6	7.7	7.1	0.93	1.07	na.	702
Qantas Airways	QAN AU	NR	3.90			6.0	7.0	6.7	4.3	4.3	2.48	1.93	19.4	77
Singapore Airlines	SIA SP	HOLD	11.14	11.80	5.9%	9.1	19.9	16.0	4.1	4.6	1.03	1.02	8.3	(28)
Thai Airways	THAI TB	SELL	10.30	12.0	16.5%	0.6	44.6*	8.2	7.0	6.5	0.71	0.81	1.6	384
Transasia Airways	6702 TT	NR	7.76			0.2	9.6	n.a	6.4	8.0	0.61	0.55	3.9	102
Virgin Australia	VAH AU	NR	0.48			1.2	18.3	11.9	6.4	5.8	1.55	1.53	1.8	170
<b>FSC average</b>							<b>11.4*</b>	<b>9.8</b>	<b>6.4</b>	<b>6.1</b>	<b>1.34</b>	<b>1.26</b>	<b>11.0</b>	<b>169</b>
<b>Low cost carriers</b>														
AirAsia	AIRA MK	BUY	1.44	2.05	42.4%	0.9	5.0	5.6	8.9	9.4	0.84	0.85	n.a	263
AirAsia X	AAX MK	HOLD	0.21	0.22	4.9%	0.2	n.a	39.5	6.2	4.6	1.02	1.01	n.a	214
Asia Aviation	AAV TB	BUY	4.80	6.50	35.4%	0.6	13.4	10.4	10.1	9.4	1.15	1.03	4.7	21
Cebu Air	CEB M	BUY	88.95	116.0	30.4%	1.1	6.1	5.7	5.3	4.5	2.02	2.00	17.7	139
NOK Airlines	NOK TB	HOLD	7.55	12.0	58.9%	0.1	9.9	5.7	7.2	6.6	1.30	1.08	n.a	(74)
Tiger Airways	TGR SP	NR	0.41			0.7	205.0*	21.6	16.2	12.1	5.3	4.56	n.a	(1)
<b>LCC average</b>							<b>8.6*</b>	<b>9.8</b>	<b>9.0</b>	<b>7.8</b>	<b>1.93</b>	<b>1.75</b>	<b>11.2</b>	<b>93</b>

Sources: Bloomberg, Maybank KE

\* figure excludes THAI Airways and AirAsia X as the number is way out of its normal peer group range

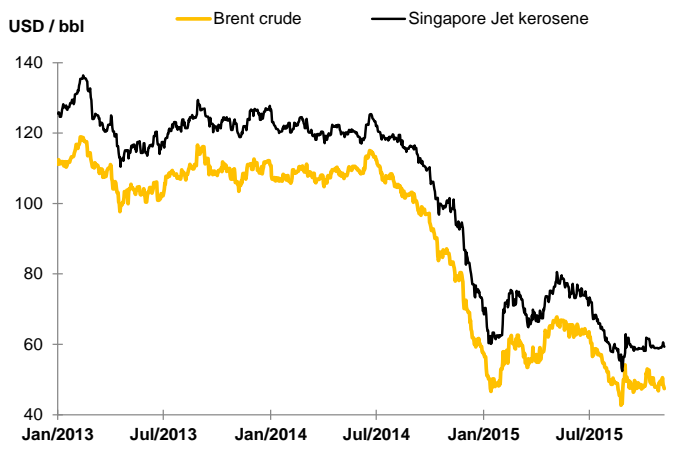
UR = Under Review

NR = Not Rated

\* All forward-looking estimates and multiples for companies not under Maybank's coverage, including companies currently under review, are from Bloomberg consensus.

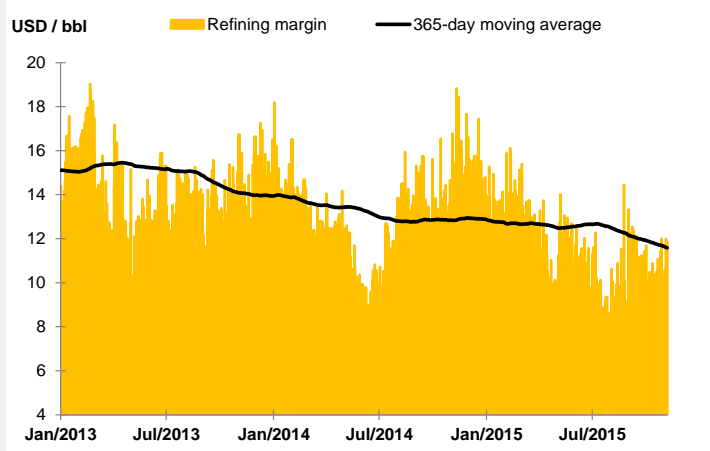
# Key graphs that matter

Figure A: Singapore Jet fuel and Brent Crude



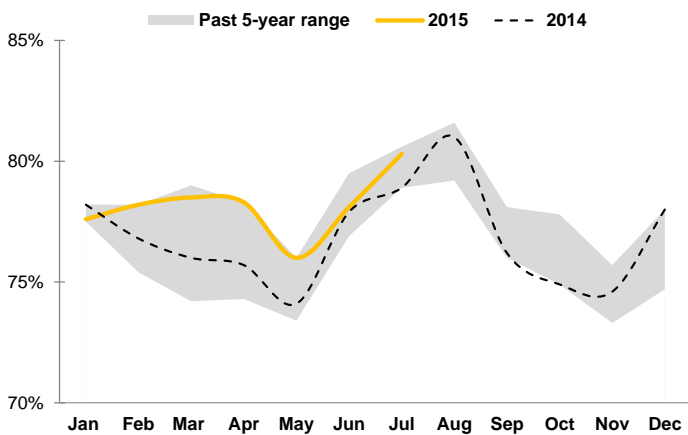
Sources: Bloomberg, Maybank KE

Figure B: Refining margin



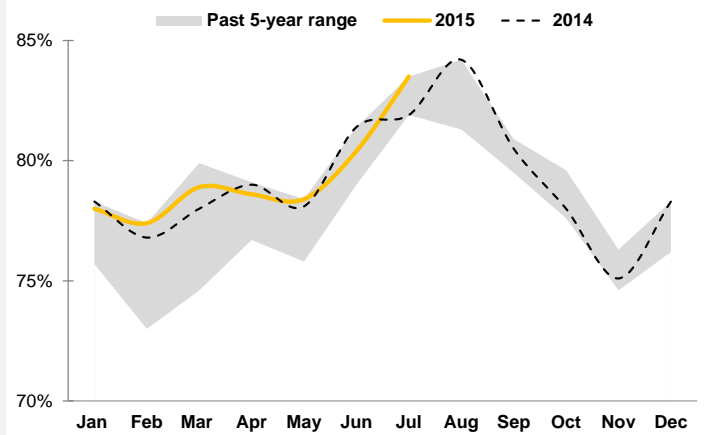
Sources: Bloomberg, Maybank KE

Figure C: Asia Pacific airlines passenger load factor



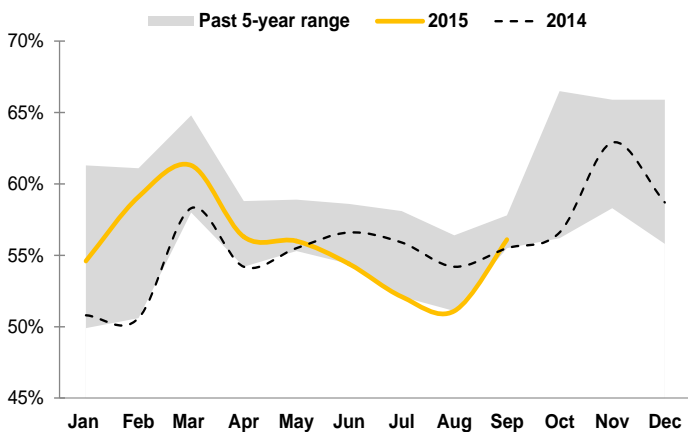
Source: IATA

Figure D: Global airlines passenger load factor



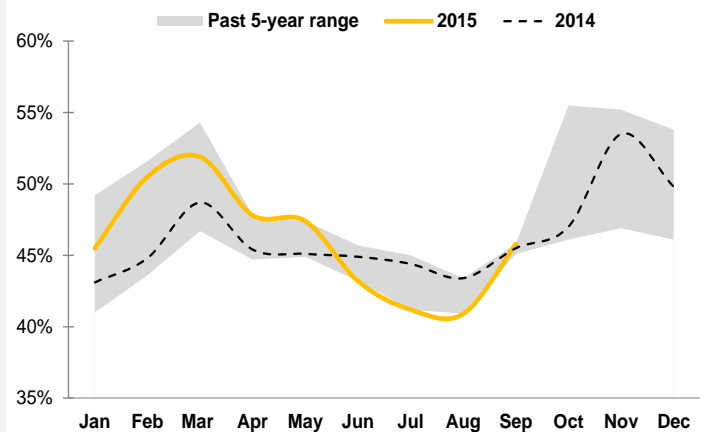
Source: IATA

Figure E: Asia Pacific airlines cargo load factor



Source: IATA

Figure F: Global airlines cargo load factor



Source: IATA

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