

Industrials
Airlines
Equity – Hong Kong

Hold

Target price (HKD)	21.10
Share price (HKD)	18.62
Upside/Downside (%)	13.3

Performance	1M	3M	12M
Absolute (%)	-4.8	14.0	28.1
Relative ^A (%)	-1.6	2.0	11.9

Index^A HANG SENG INDEX

RIC 0293.HK
 Bloomberg 293 HK

Market cap (USDm) 9,445
 Market cap (HKDm) 73,248

Enterprise value (HKDm) 120036
 Free float (%) 25

11 June 2015

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Cathay Pacific (293 HK)

Hold: May passenger loads strong; cargo again lacklustre

- ▶ **Record May passenger load factor and y-t-d performance above forecast; softness in long-haul premium volumes**
- ▶ **Cargo volume rebound continues, but load factor stalls; mainland business facing intense competition**
- ▶ **Maintain Hold at an unchanged target price of HKD21.1**

Record May passenger loads, but cargo softens. May's passenger load factor was 85.9%, up 2.9ppts y-o-y (vs +2.5ppts y-o-y in April). Passenger traffic (RPK) grew 11.2% y-o-y (vs 7.4% y-o-y in April). May's cargo load factor was 62.1%, down 0.9ppts y-o-y (vs -0.6ppts y-o-y in April). Cargo traffic (FTK) rose 9.5% y-o-y (vs +6.3% y-o-y in April).

Commentary remains positive, but long-haul premium performance softer. In its commentary, Cathay stated on passenger: "Passenger demand remained robust in most key markets during May... demand out of the key Hong Kong market was strong, buoyed by the public holidays ... Japan remained hugely popular ... and we saw high loads in the economy cabin on many other routes. A higher proportion of connecting traffic and lower-than-expected premium traffic on long-haul routes both had a negative impact on yield." On cargo, Cathay stated: "...business got off to a slow start in May due to the long public holiday in Mainland China at the beginning of the month. Demand picked up steadily as factories reopened... our mainland business continued to face pressure from intense competition and we saw less benefit from the congestion in the seaports on the West Coast of the USA demand into and out of the Indian subcontinent was one of the bright spots in our cargo network in May."

Y-t-d growth remains above our forecast. Passenger volumes remained robust; indeed, this was a record passenger load factor for May. Y-t-d, passenger volumes are up 9.7% y-o-y, above our 2015 forecast of +8%; the passenger load factor is up 2.5ppts y-o-y, versus our model assumption of flat y-o-y. In contrast, the cargo performance softened, and capacity risks again seem to be rising in parts of China. Y-t-d, cargo volumes are up 12.2% y-o-y compared to our model assumption of +11%; the cargo load factor is up 1.5ppts, versus +1.2ppts y-o-y in our model.

Maintain Hold rating and TP of HKD21.1. Since 2000, Cathay Pacific has traded at an average one-year forward book value of 1.25x and given our forecast of normalising ROE, we believe Cathay's PB level should return to this average, which gives our fair value target price of HKD21.1.

Financials & valuation

Financial statements

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Profit & loss summary (HKDm)				
Revenue	105,991	110,261	116,180	121,918
EBITDA	13,029	16,914	20,026	20,514
Depreciation & amortisation	-8,594	-8,537	-9,006	-9,428
Operating profit/EBIT	4,435	8,378	11,019	11,087
Net interest	-1,158	-1,408	-1,429	-1,143
PBT	4,049	8,483	11,533	11,887
HSBC PBT	4,049	8,483	11,533	11,887
Taxation	-599	-1,045	-1,439	-1,492
Net profit	3,150	7,115	9,747	10,019
HSBC net profit	3,150	7,115	9,747	10,019

Cash flow summary (HKDm)

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Cash flow from operations	23,984	6,490	15,522	17,875
Capex	-12,130	-12,100	-7,100	-10,100
Cash flow from investment	-16,123	-12,100	-7,100	-10,100
Dividends	-1,418	-2,988	-4,240	-4,258
Change in net debt	4,801	655	-8,934	-5,102
FCF equity	4,449	-2,871	11,008	8,700

Balance sheet summary (HKDm)

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Intangible fixed assets	0	0	0	0
Tangible fixed assets	98,471	102,034	100,128	100,800
Current assets	33,467	32,776	42,372	48,541
Cash & others	21,098	20,443	29,376	34,903
Total assets	171,974	175,945	185,055	193,318
Operating liabilities	35,980	31,560	33,564	35,179
Gross debt*	89,529	89,529	89,529	89,954
Net debt*	68,431	69,086	60,153	55,051
Shareholders funds	51,722	63,791	74,049	81,821
Invested capital*	90,994	102,942	103,193	104,818

*Includes capitalised operating leases

Ratio, growth and per share analysis

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Y-o-y % change				
Revenue	5.5	4.0	5.4	4.9
EBITDA	14.9	29.8	18.4	2.4
Operating profit	18.0	88.9	31.5	0.6
PBT	13.1	109.5	36.0	3.1
HSBC EPS	20.2	125.9	37.0	2.8

Ratios (%)

Year to	12/2014a	12/2015e	12/2016e	12/2017e
Revenue/IC (x)	1.1	1.1	1.1	1.2
ROIC	5.4	9.0	10.7	10.7
ROE	5.5	12.3	14.1	12.9
ROA	2.6	5.0	6.3	6.0
EBITDA margin	12.3	15.3	17.2	16.8
Operating profit margin	4.2	7.6	9.5	9.1
EBITDA/net interest (x)	11.3	12.0	14.0	17.9
Net debt/equity	132.0	107.5	80.4	66.3
Net debt/EBITDA (x)	5.3	4.1	3.0	2.7
CF from operations/net debt	35.0	9.4	25.8	32.5

Per share data (HKD)

Year to	12/2014a	12/2015e	12/2016e	12/2017e
EPS reported (fully diluted)	0.80	1.81	2.48	2.55
HSBC EPS (fully diluted)	0.80	1.81	2.48	2.55
DPS	0.36	0.76	1.08	1.08
Book value	13.15	16.22	18.82	20.80

Key forecast drivers

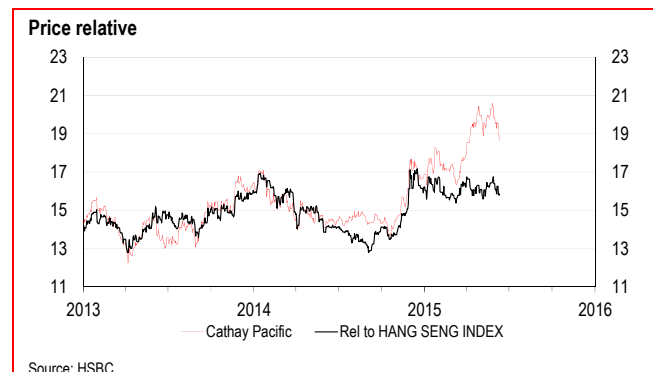
Year to	12/2014a	12/2015e	12/2016e	12/2017e
Capacity growth (ATK) %, y-o-y	8	9	5	5
Traffic (RTK) %, y-o-y	10	9	6	5
Overall load factor	72.9	73.5	74.2	74.2
Change in overall yield %, y-o-y	-3.5	-6.0	-0.8	-0.4
Change in unit costs per ATK %	-2.6	-8.1	-1.9	0.3
Spot jet fuel price (USD/bbl)	117	80	80	80

Valuation data

Year to	12/2014a	12/2015e	12/2016e	12/2017e
EV/sales	1.1	1.1	0.9	0.9
EV/EBITDA	7.5	6.0	4.8	4.4
EV/IC	1.3	1.2	1.1	1.0
PE*	23.3	10.3	7.5	7.3
P/NAV	1.4	1.1	1.0	0.9
REP**	1.7	1.0	0.8	0.7
Dividend yield (%)	1.9	4.1	5.8	5.8

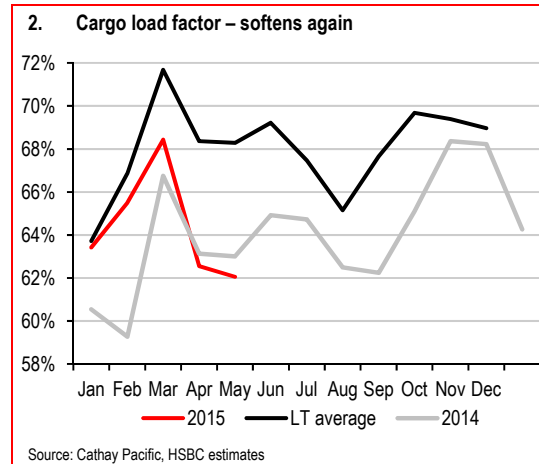
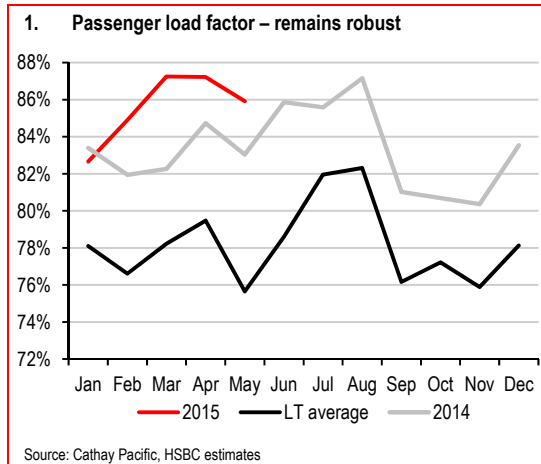
Note: * = Based on HSBC EPS (fully diluted)

** REP = EV/IC divided by WACC



Note: price at close of 10 Jun 2015

May load factors



Valuation and risks

Our fair value target price for Cathay is HKD21.1 and is based on a 1.25x one-year forward book value, which is the average level at which the shares have traded since 2000. Given our forecast of normalising ROE, we believe Cathay's PB level should return to this average. We argue that Cathay Pacific's strong home base, which we believe is the best positioned gateway into Southern China, and its greater exposure to North America, mean that the carrier has a stronger medium-term outlook than its Asian competitors.

Downside risks to our rating and forecasts include lower-than-expected Asian and global GDP growth, a sharp decline in business confidence and a further material strengthening of the US dollar. **Upside risks** include greater-than-expected cargo yield increases and a weakening of the US dollar.

Disclosure appendix

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

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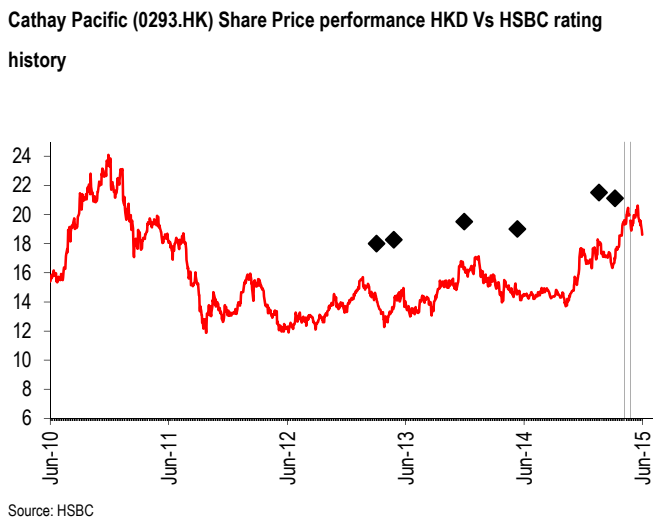
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Share price and rating changes for long-term investment opportunities



Recommendation & price target history

From	To	Date
Overweight	Buy	16 April 2015
Buy	Hold	03 May 2015
Target Price	Value	Date
Price 1	18.00	13 March 2013
Price 2	18.25	06 May 2013
Price 3	19.50	09 December 2013
Price 4	19.00	21 May 2014
Price 5	21.50	28 January 2015
Price 6	21.10	18 March 2015

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
CATHAY PACIFIC	0293.HK	18.62	10-Jun-2015	7

Source: HSBC

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