A legacy vs. Low-Cost Carriers ("LCCs") battle

Rapid growth is the most attractive point of the Vietnamese aviation market, with a CAGR growth of 17.4% in the last decade and an outstanding growth of approximately 30% in 9M2016 in term of passenger movements.

The double-digit growth is expected to continue in the next decade given (i) rising living standard, (ii) more affordable prices for air-travel, and (iii) the many advantages of air vs. ground travel. Given that, the upcoming listing of Viet Nam Airline ("HVN"), Vietnam’s flagship air carrier, and the IPO of Vietjet Air ("VJA"), the nation’s rising star LCC, will attract investors’ interest.

Among the five domestic airlines, Jetstar and VASCO are HVN-related while the newbie Vietstar which has yet to provide schedule flights, so the current air transportation market, basically, is a two-sided battle between HVN and VJA, which perfectly represents the traditional vs. low cost model, experienced vs. youth, and state-owned vs. private sector.

HVN defines itself as a full-service carrier in Vietnam, targeting mid- and high-end passengers on local routes and international passengers to/from Vietnam. We believe that the company’s new strategic partner ANA Holding Inc., who owns All Nippon Airways (one of the prestigious 5-star global airlines), will help HVN to improve its services. It was just certified as a 4-star airlines as expected while continue to maintain a presence in the LCC market through subsidiaries SkyViet/VASCO (51% stake) and JETSTAR (68.5% stake) as part of the dual brand strategy.

Founded in 2007, VJA flew its maiden voyage in 2012. Since then this private company has been orienting itself at the LCC segment. In contrast to HVN’s target customers, Vietjet’s are the majority of the Vietnamese population, the working class with low-to-medium incomes, whose demand for fast means of transportation at an affordable price has been rising along with living standards in recent years.

In terms of aircraft fleets, seat capacity, flight routes, passenger market shares and sales value, HVN is still the biggest player. However, it is likely that VJA will catch up given its ambitious expansion plan in the coming years.

In this brief aviation report, a quick description of current main conditions is mentioned to provide investors a general view of domestic air-transport market. In addition, a comparison between two biggest domestic airlines: Vietnam Airlines vs. Vietjet Air is focused to illustrate the dominating and current tendency of Vietnam’s airlines structure. Specific analysis reports over key players will be published later on.
Driving by rapid industry growth

For the last decade, in term of passenger movement at airports, Vietnam aviation industry has recorded a magnificent growth with double-digit CAGR of 17.4%. In the last 5 years, Vietnam aviation industry recorded a CAGR of 16.1% surpassing that of Asia-Pacific area (7.9%), indicating a lucrative air-travel market, which is still young and growing fast. For 2016, number of passenger in this market is estimated to reach ~81 million (+29% YoY), breaking its own previous high-record of 63.1mn in 2015 (+24% YoY).

![Passengers volume of air-travel by years](image)

Source: ACV

In comparison with other public transportation vehicles (OPV), including bus, ferry and railway, domestic aviation has been performing with a more vigorous and accelerating pace, referring its favorable roles in means of transportation. For the last 5 years, air-travel enjoyed a robust CAGR of 16.3%, beating the single-digit rate of 6.6% of OPV. In 2010, OPV still had an edge over air-travel when the sales of OPV and air-travel hit VND7.1trn and VND6.2trn respectively. However, it was reversed in 2015 with respective figures being VND9.8trn and VND13.3trn.

Given the more gradually affordable prices for air-travel nowadays, along with its perks, the spread between this type of transportation and the other is predicted to stretch out, with a forecast growth of air-travel to maintain at two-digit.

![Performance of airtravel vs others until 2015](image)

Source: ACV, Euromonitor, ACBS estimated
Market structure shifts toward LCCs

In the last 5 years, air-travel market in Vietnam has witnessed a remarkable footprint from the newcomer, along with the switch from traditional toward low-cost airlines. As we estimated, in 2011, the market was majorly belonged to HVN (79.9%) while the rest lied with Jetstar Pacific (12.3%) and others (7.6%). However, the big picture rotated in the following years when VJA kept increasing its volume from ~2.5mn in 2012 to ~9.3mn passengers in 2015 (3-year CAGR of 55.7%).

As a result, last year, it was estimated that Vietjet Air’s market share (total passenger volume that includes both foreign and domestic passengers) were up to 30.6%, while those of HVN and Jetstar were 57.1% and 11.8%, respectively. The phenomenon was explained mainly by the rising demand for an affordable air-transportation, the expansion in VJA’s fleet size, and newly-open routes with new destinations both in-bound and off-bound from this fast-growing LCC.

Notably, domestic passengers has become VJA’s key customer as this budget airline accounted for 37% market share in term of number of domestic flyers in 2015, directly competing with the national giant HVN (possessed 48% in the year). According to CAPA Centre for aviation, the race in dominating domestic market share will likely have its new winner in 2016 when HVN’s long lasting monopolistic position will finally be conquered by VJA. Preliminarily, as ACBS forecasted, domestic passenger volumes of HVN and VJA will likely be approximately 11.5mn and 12.5mn respectively, at minimum.
The restructuring of HVN’s fleet vs. expansion of VJA

HVN has the largest fleet in Vietnam, comprising 83 aircrafts and 15,632 seats with diversified model, accounting for over 60% of the country fleet. VJA owns the youngest fleet with an average age of 3.8 years, comprising 36 airplanes and 7,160 seats. Jetstar, the first LLC in Vietnam (since 2007) seem a bit dilatory and passive compared to the rival, has just 13 aircrafts of A320 family after divesting the Boeing 737 model.

<table>
<thead>
<tr>
<th></th>
<th>HVN</th>
<th>VJA</th>
<th>Jetstar</th>
<th>VASCO (SkyViet)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aircraft fleet</td>
<td>83</td>
<td>36</td>
<td>13</td>
<td>4</td>
</tr>
<tr>
<td>Average age (years)</td>
<td>5.6</td>
<td>3.8</td>
<td>7.0</td>
<td>11.0</td>
</tr>
<tr>
<td>Total seats of the fleet</td>
<td>17,957</td>
<td>6,660</td>
<td>2,340</td>
<td>272</td>
</tr>
<tr>
<td>Average aircraft size (seats/airline)</td>
<td>216</td>
<td>185</td>
<td>180</td>
<td>68</td>
</tr>
</tbody>
</table>

In the last two years, VJA aggressively expand the fleet by placing two important buy and leaseback transactions for a total 200 airplanes with Airbus and Boeing (100 airplanes each) which worth USD9.1mn and USD11.3mn respectively. In the meantime, HVN acquired 5 A350s and 10 Boeing 787s out of 14 A350 and 19 Boeing 787 scheduled to delivery in 2015-2019 period.

The leaseback model, which is actively used by LCCs, helps VJA to rapidly expand the fleet. HVN’ fleet master plans just stop at 2018 with 116 aircrafts; of which the company will acquire all Boeing 787s while use sell & leaseback for some A321s and A350s. Jetstar will raise the fleet to 30 aircrafts by 2020, which is still behind that of VJA with above 200 by 2023.

VJA threatening HVN’s leading position

In fact, with HVN and its affiliate not paying much attention at the low cost domestic flyers, VJA took the opportunity and grabbed a big share of this segment. Thanks to that, it is expected that VJA will overpass HVN in term of domestic flyers if Jetstar, the LCC subsidiaries of HVN, don’t have any efficient counter-attack.

In term of seat capacity, according to CAPA’s statistic, since the early of 2016, VJA already overtook HVN for the largest seat supply on Ho Chi Minh – Ha Noi route, the most crowded air traffic in Vietnam. In addition, VJA accounted for ~39% seat capacity on local routes while that of HVN retreated to ~43% since early 4Q2016.
In term of flight network, HVN, Jetstar and VJA’s destinations have almost covered all domestic airports (excluding type C airports that only serve ATRs) with each having about 30-40 routes at present. International network is still the biggest advantage of VNA, operating more than 57 routes and serving approximately 75% of international passengers to/from Vietnam.

**Load factor indicating room for LCCs’ organic growth**

Yearly increasing air-travel demand has enabled the top three airlines in Vietnam to record high load factor for years, in which those of LCCs distanced the giant HVN’s. Particularly, as of 2015, the ratios among top three domestic airlines HVN, VJA and Jetstar Pacific were 80.5%, 88.1% and 90.0%, respectively. Compared with the global load factor of 80.4% in 2015, reported by IATA, while the giant HVN has approached global level recently, LCCs in Vietnam shows prospective outlook, especially in term of fleet size expansion and growth in number of passengers.

<table>
<thead>
<tr>
<th></th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>HVN</td>
<td>76.6%</td>
<td>73.9%</td>
<td>76.3%</td>
<td>79.3%</td>
<td>79.9%</td>
<td>80.5%</td>
</tr>
<tr>
<td>Vietjet Air</td>
<td>-</td>
<td>n.a.</td>
<td>n.a.</td>
<td>88.2%</td>
<td>88.6%</td>
<td>88.1%</td>
</tr>
<tr>
<td>Jetstar</td>
<td>91.0%</td>
<td>91.0%</td>
<td>91.0%</td>
<td>90.0%</td>
<td>n.a.</td>
<td>90.0%</td>
</tr>
<tr>
<td>Global</td>
<td>78.7%</td>
<td>78.5%</td>
<td>79.4%</td>
<td>79.7%</td>
<td>79.9%</td>
<td>80.4%</td>
</tr>
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*Source: HVN, VJA, Jetstar, CAPA, Euromonitor, IATA*
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**BUY:** where we believe prospective 12 month VND total return (including dividends) will be 15% or more.

**HOLD:** where we believe it will be -15% to 15%.

**SELL:** where we believe it will be lower than -15%.

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