AmInvestment Bank

Sector report
22 July 2020

TRANSPORTATION & LOGISTICS

Different recovery paths amongst segments

UNDERWEIGHT
(Maintained)

AmInvestment Bank
www.amequities.com.my
03-2036 2240

Rationale for report: Sector update

Investment Highlights

- We maintain our **UNDERWEIGHT** call on the transportation & logistics sector. The sector is recovering with the reopening of the economy both locally and globally. However, the speed and path of recovery vary amongst the different segments within the sector. The recovery of global trade augurs well for the port segment. However, the air travel industry faces a bumpy path given the uncertainties surrounding the opening of borders and recapitalisation plans of airlines. While the logistics segment is technically a beneficiary of the pandemic (particularly, parcel delivery on the back of the booming online shopping), it is weighed down by a crowded playing field with cut-throat competition.

- **Ports:** The International Monetary Fund (IMF) projects the global economy to rebound by 5.4% in 2021F (after contracting by 4.9% in 2020F). Already, business confidence globally as indicated in purchasing managers' indices (PMI) has shown upticks in recent months (Exhibits 3 & 4), as economies, businesses and borders reopen. The global economic recovery shall translate into more robust global trade, and hence higher throughput at the seaports. We also draw comfort from the absence of any major cancellation of shipbuilding orders thus far (Exhibit 8), indicating the players' optimism on the recovery in the global container shipping trade.

- We project container throughput at **Westports (HOLD, RM3.81)** and the ports of **MMC Corporation (BUY, RM1.13)** to bounce back by 10% and 8% respectively in 2021F (after contracting by 15% and 10% in 2020F), and shall return to the pre-pandemic levels in 2022F.

- Over the longer term, the outlook for ports in the region (Malaysia included) remains resilient, underpinned by rising investment in the manufacturing sector that generates tremendous inbound (feedstock) and outbound (finished product) throughput for ports. There have been significant relocations of manufacturing bases by multi-national companies out of China to other parts of the world, including the region as they rethink geographical diversification/supply chain concentration risk, coupled with the rising labour and land costs in China and the volatile US-China relations.

- **Air travel:** There have been green shoots of recovery in the air travel industry, as indicated in the increase in global daily commercial flights since Apr 2020 as tracked by real-time flight tracker, FlightRadar24 (Exhibit 11), on the back of the easing in travel restrictions globally (Exhibit 10). However, the flights were still at only about 40% (as at end-June 2020) of the level registered at the same time last year. We project passenger volume for **AirAsia (SELL, RM0.41)** to rebound by 35% in 2021F (after shrinking by 50% in 2020F, which is in line with the Malaysian Aviation Commission's (Mavcom) projection of 49–50% contraction in Malaysia's air traffic passengers in 2020F).

- However, the recovery of the air travel industry will be bumpy given the uncertainties surrounding the opening of borders. We understand that airlines are struggling to plan their flight schedules (to ensure that the seats are filled) as passengers now on average book their tickets only 0–3 days before departure, vs. 20 days and above previously. Not helping either, is the urgent need for airlines to recapitalise their balance sheets given the massive losses they have suffered amidst a collapse in air travel since the pandemic.

- Questions also arise if one airline will enjoy unfair advantages over other airlines, if the government of the country of the airline's incorporation offers more generous financial assistance as compared with those offered to the other airlines by their respective governments. As far as Malaysia is concerned, thus far, the media reported that the government has no plan to inject cash or offer soft loans to any Malaysia-based airlines, while they are free to tap into loans guaranteed by Danajamin.

- We maintain our view that **AirAsia**'s key strategy of aggressively growing its top line (to mitigate the high cost structure arising from the recent aircraft sale-and-leaseback scheme) has been thwarted by the collapse of the air travel market, and the expected long and winding recovery road of the industry.

- **Logistics:** We believe the parcel delivery segment is a winner of the current situation as the pandemic and the resultant social distancing accelerate the change in shopping habits of consumers from physical to online channels. Based on research data by e-commerce ecosystem player Commerce.Asia, the value of merchandise sold via e-commerce in Malaysia surged 149% YoY in 1Q2020 amidst the pandemic. The growth in e-commerce sales translates to rising volumes of parcels handled by parcel delivery companies such **Pos Malaysia (HOLD, RM0.90)** and **GDex (Unrated)**.

- However, the sector has low entry barriers. A crowded playing field (with 111 players as at June 2020) has given rise to cut-throat competition resulting in severe squeeze in margins. We believe the overcrowded situation could get worse in the short to medium term given more new entrants funded by venture capitalists who want to jump on the bandwagon of the e-commerce boom (Exhibits 19 & 20). According to McKinsey & Company, funding to logistics startups (largely in the courier, express and parcel segment) grew at a CAGR of 76% from 2014–2019.

- The incumbents are expanding too. For instance, **Pos Malaysia** has planned to double its daily automated parcel processing capacity by 2025 (currently at 500K), in order to achieve better economies of scale. It also plans to scale up its last-mile delivery through crowdsourcing and an entrepreneurship programme (which converts its existing delivery staff to third-party delivery partners). Meanwhile **GDex**, currently with an average sorting capacity of 130K parcels per day, has also allocated RM40mil for expansion of its automated sorting hub.

- Our top pick within the sector is **MMC Corporation**. We see **MMC Corporation** as a recovery play given the expected improvement in its port throughput over the next 6–12 months as economies reopen. We see value in **MMC Corporation** with its port business being valued at 12x forward P/E on a stand-alone basis (see Exhibit 2 for our sum-of-parts valuation for **MMC Corporation**).

EXHIBIT 1: VALUATION MATRIX

	Recomm.	Price	FV	Upside	Mkt Cap	FYE	EPS (sen)		EPS growth (%)		P/E (x)		P/B*	ROE*	NDPS*	Div Yield*
		(RM)	(RM)	(%)	(RMmil)		FY20F	FY21F	FY20F	FY21F	FY20F	FY21F	(x)	(%)	(sen)	(%)
AirAsia	SELL	0.71	0.41	-42.3	2,372.8	Dec	-50.7	6.3	457.1	-112.4	-1.4	11.3	0.5	-38.1	0.0	0.0
Pos Malaysia	HOLD	0.89	0.90	1.7	692.8	Dec	-11.5	-3.0	-24.6	-73.8	-7.7	-29.5	0.5	-6.1	0.0	0.0
Westports	HOLD	3.66	3.81	4.1	12,480.6	Dec	16.5	18.1	-4.6	9.7	22.2	20.2	4.5	35.5	12.4	3.4
MMC Corporation	BUY	0.72	1.13	56.9	2,192.5	Dec	6.8	8.0	-16.0	17.6	10.6	9.0	0.2	3.4	3.8	5.3
Simple Average									**103.0**	**-39.7**	**5.9**	**2.8**	**1.4**			
Weighted Average									**55.0**	**-8.9**	**16.4**	**15.7**	**3.3**			

**FY20*

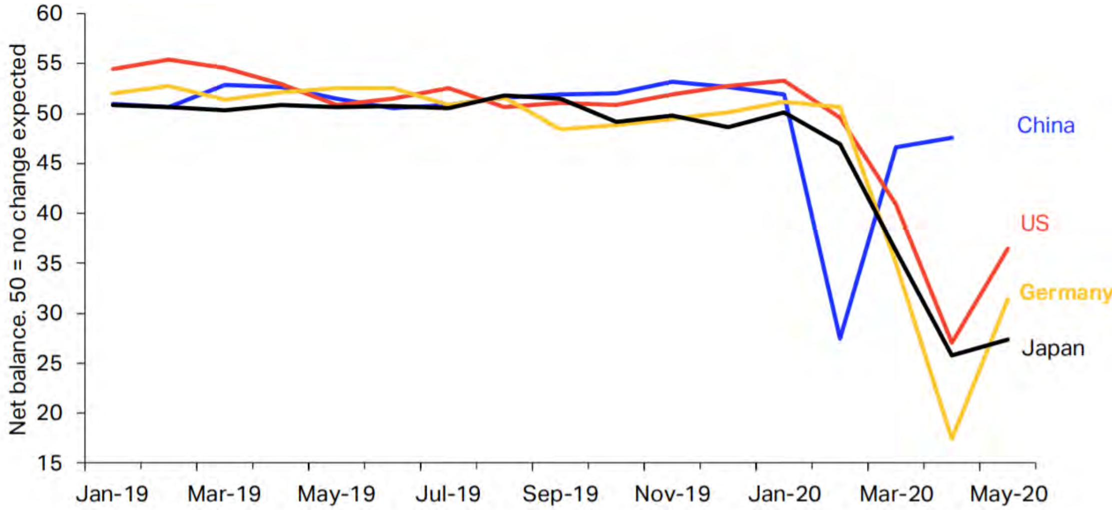
Source: company, AmInvestment Bank

EXHIBIT 2: MMC'S SOP VALUATION

FYE Dec	Value (RM mil)	Basis
Ports & Logistics		
Ports	4,678.2	16x FY21F earnings, a 30% discount to 23x of peers' historical average
Senai Airport	160.0	Book value as at Dec 2018
Engineering & Construction	406.5	Net profit from outstanding orderbook, discounted to NPV at a 10% discount rate
Energy & Utilities		
Malakoff (38.4%)	1,728.0	AmBank's FV @ RM1.00 with 10% holding company discount
Gas Malaysia (30.9%)	1,057.0	Consensus FV @ RM2.96 with 10% holding company discount
Aliran Ihsan Resources Berhad	487.0	Acquisition cost
Net Cash/(Debt)	(5,047.3)	As at 31 Dec 2019 (at the company level)
Total Value (RM mil)	**3,469.4**	
No of shares	**3,045.1**	
FV per share	**1.13**	

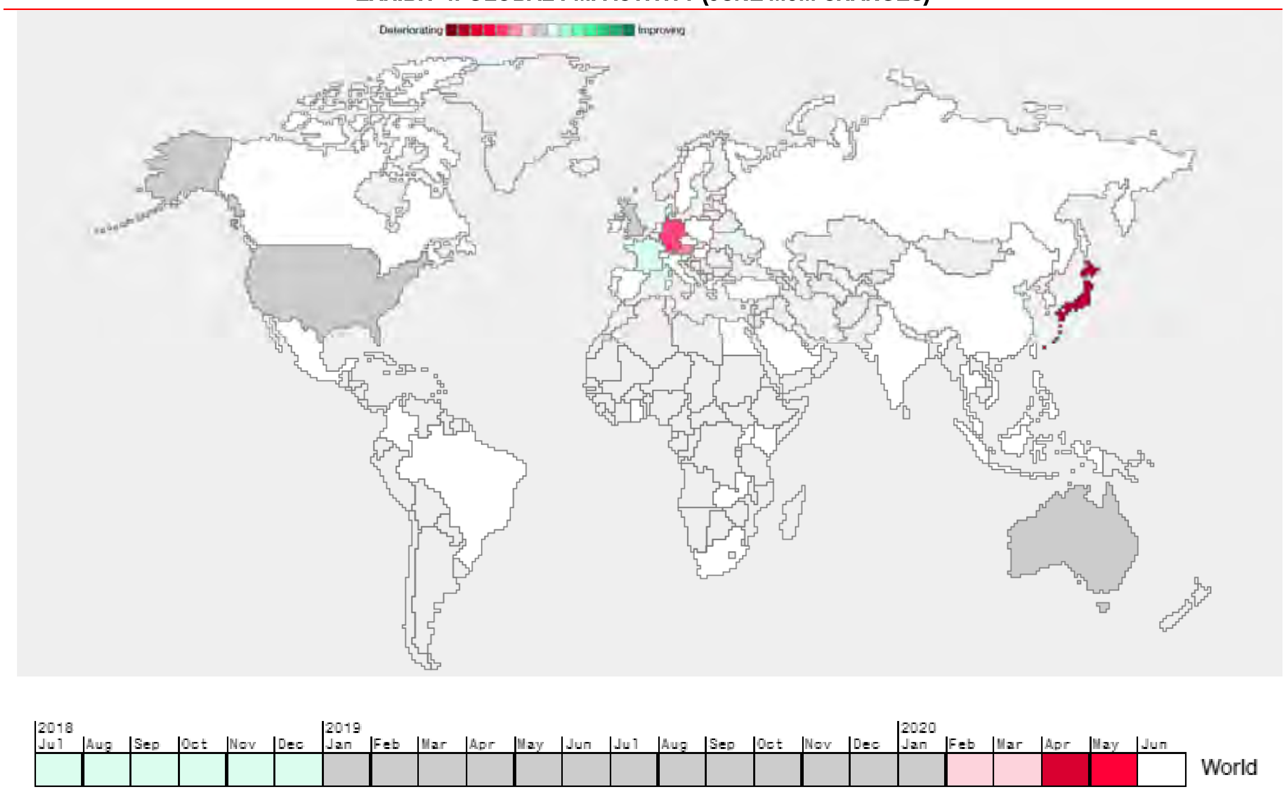
Source: company, AmInvestment Bank

EXHIBIT 3: BUSINESS CONFIDENCE (PMI) INDICES



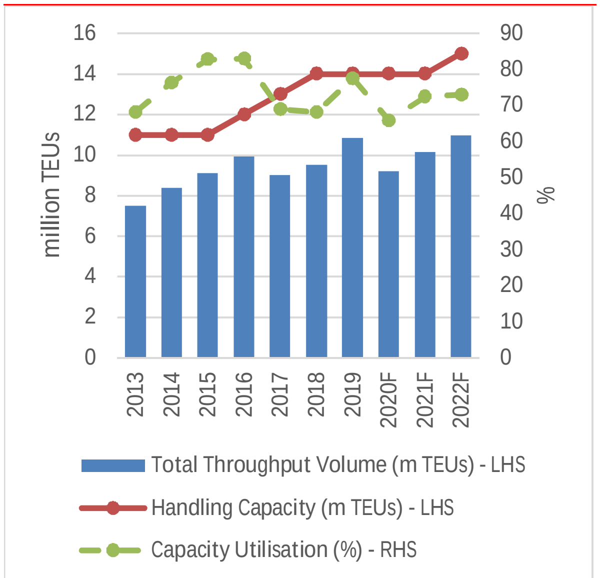
Source: IATA Economics, Markit

EXHIBIT 4: GLOBAL PMI ACTIVITY (JUNE MoM CHANGES)



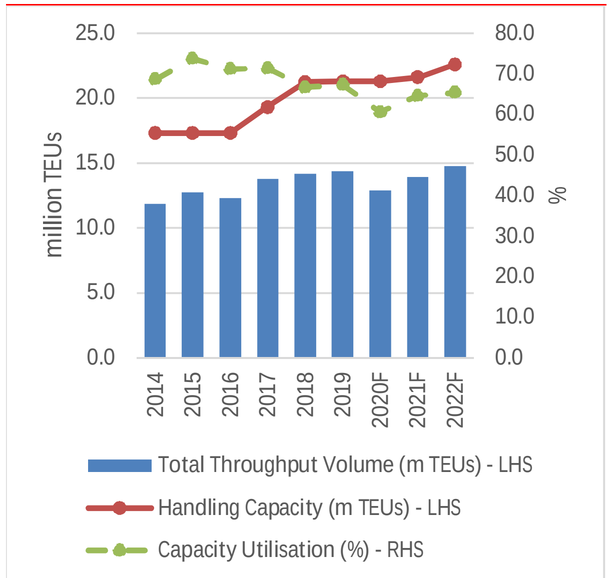
Source: Bloomberg

EXHIBIT 5: WESTPORTS' CONTAINER THROUGHPUT



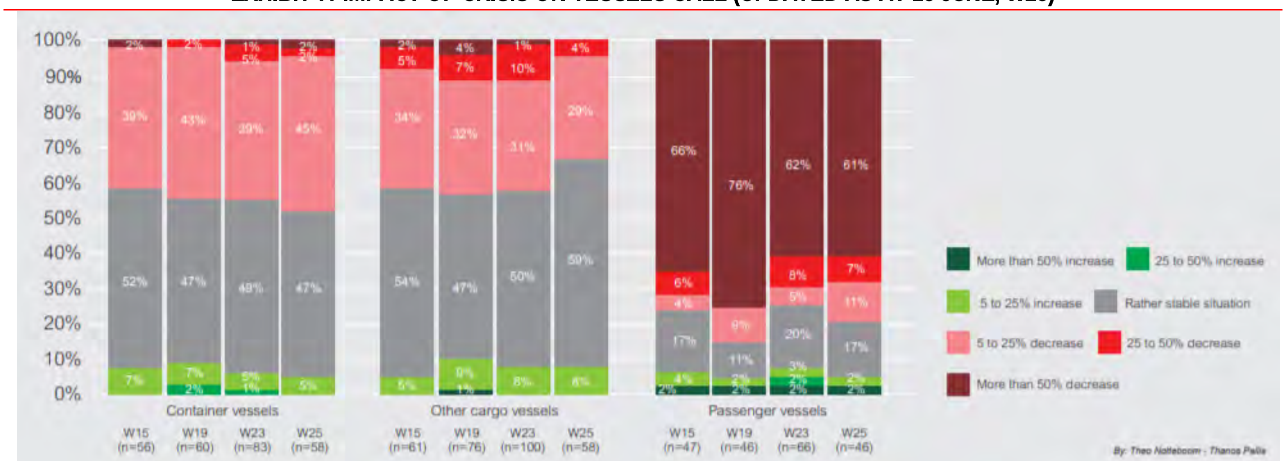
Source: Company, AmInvestment Bank Bhd

EXHIBIT 6: MMC'S CONTAINER THROUGHPUT



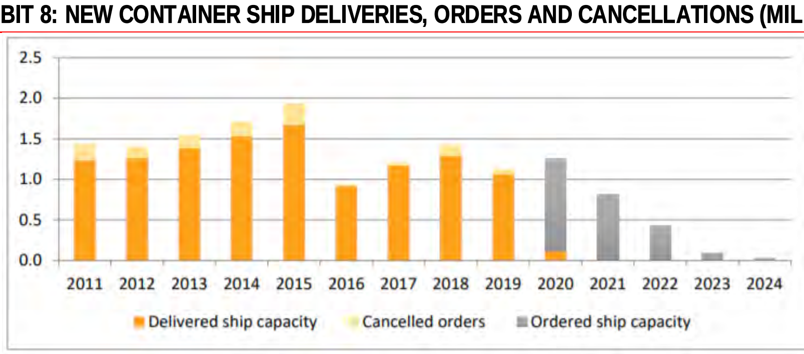
Source: Company, AmInvestment Bank Bhd

EXHIBIT 7: IMPACT OF CRISIS ON VESSELS CALL (UPDATED AS AT 15 JUNE, W25)



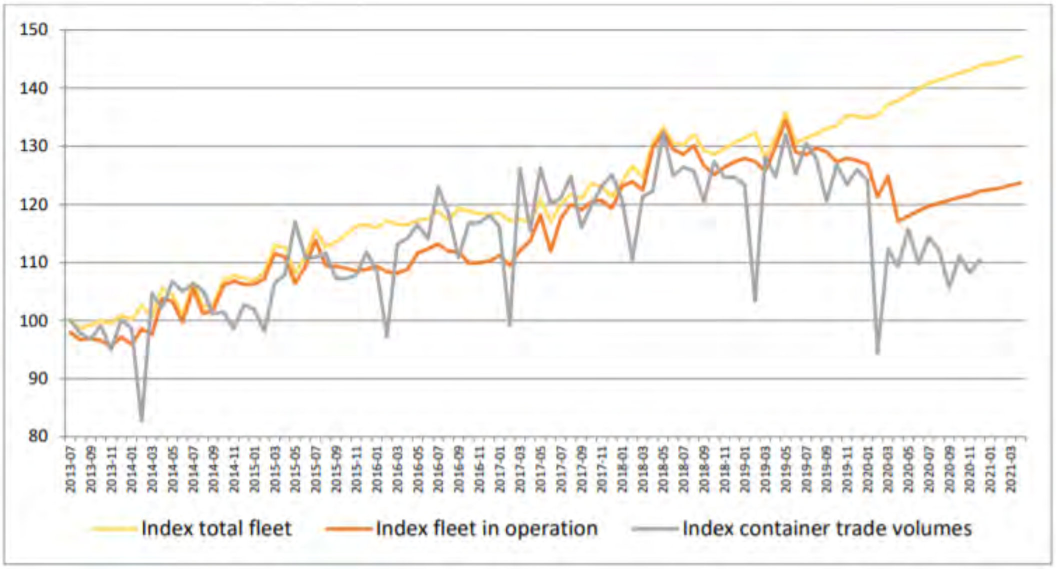
Source: IAPH-WPSP Port Economic Impact Baromete

EXHIBIT 8: NEW CONTAINER SHIP DELIVERIES, ORDERS AND CANCELLATIONS (MIL TEUs)



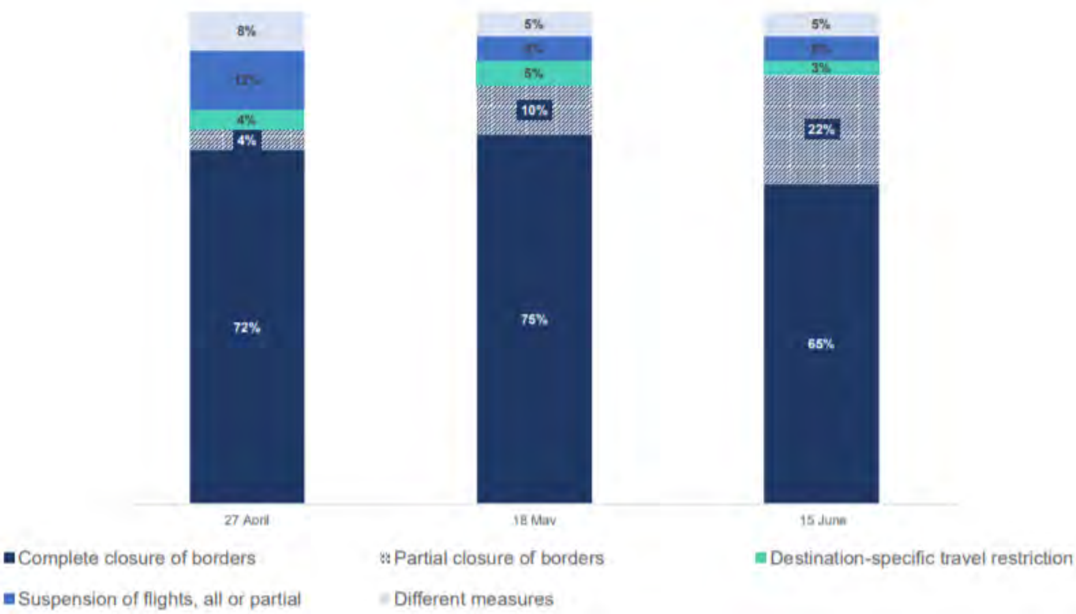
Source: International Transport Forum, IHS

EXHIBIT 9: CONTAINER SHIP CAPACITY AND TRADE DEMAND (2013–2021)



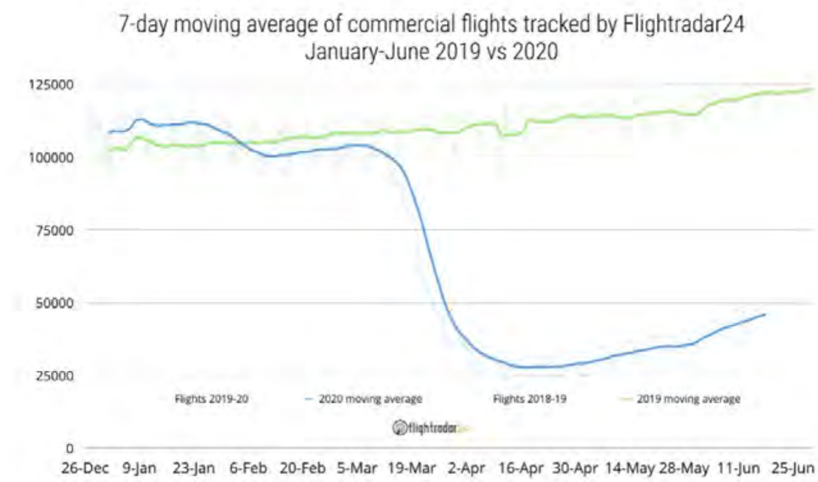
Source: International Transport Forum, HIS, Alphaliner, CTS

EXHIBIT 10: CHANGES IN TYPE OF RESTRICTIONS OVER TIME



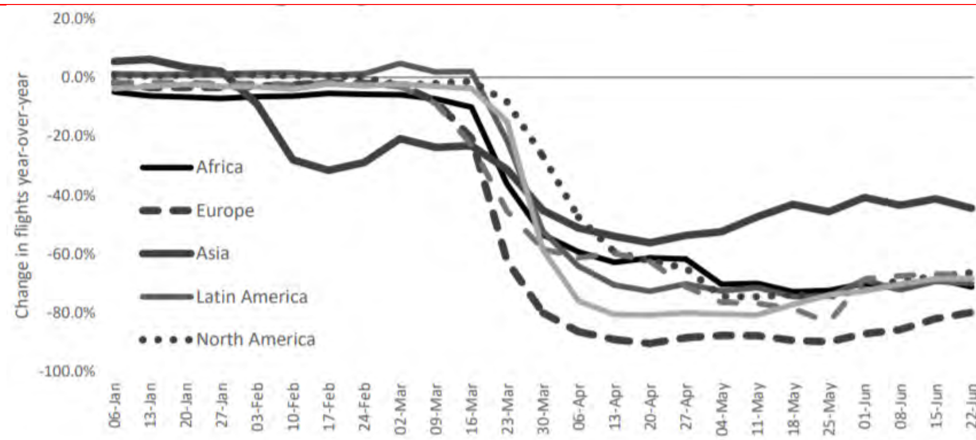
Source: UNWTO

EXHIBIT 11: GLOBAL COMMERCIAL FLIGHTS TRACKING



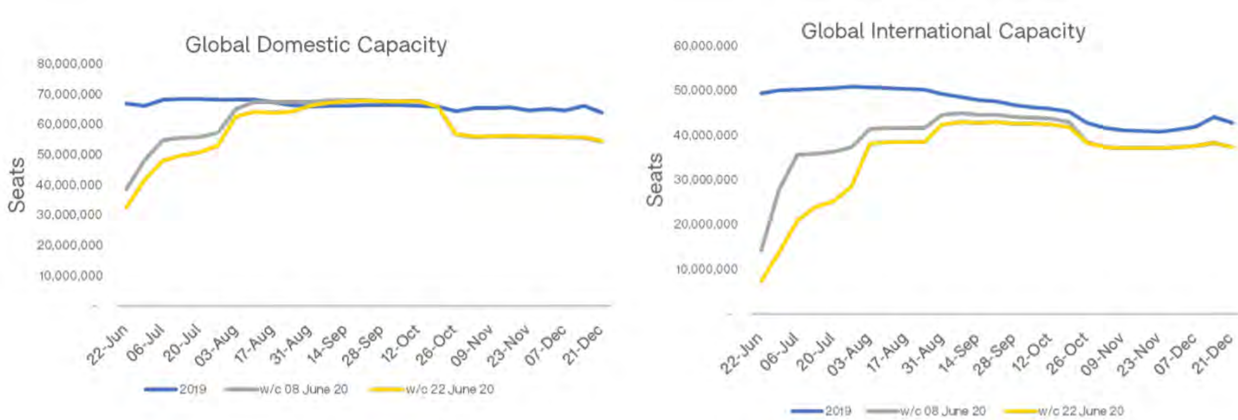
Source: Flightradar24

EXHIBIT 12: CHANGES IN FLIGHTS COMPARED TO THE SAME WEEK LAST YEAR



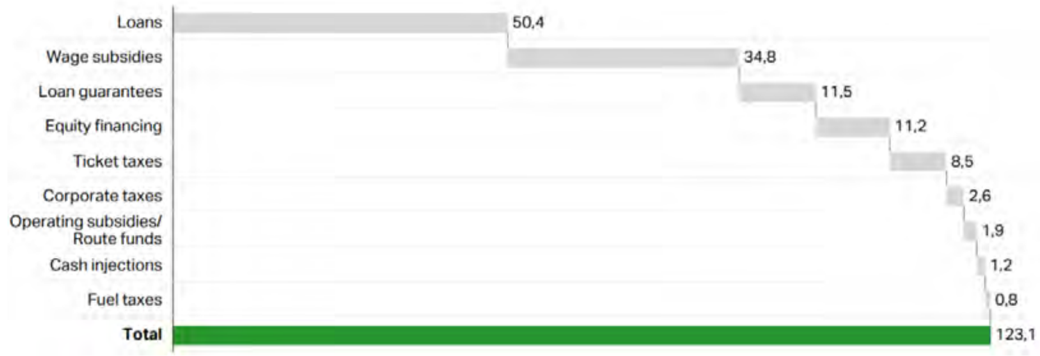
Source: OAG

EXHIBIT 13: GLOBAL AIR TRAVEL CAPACITY (2H20, AS AT 22 JUNE)



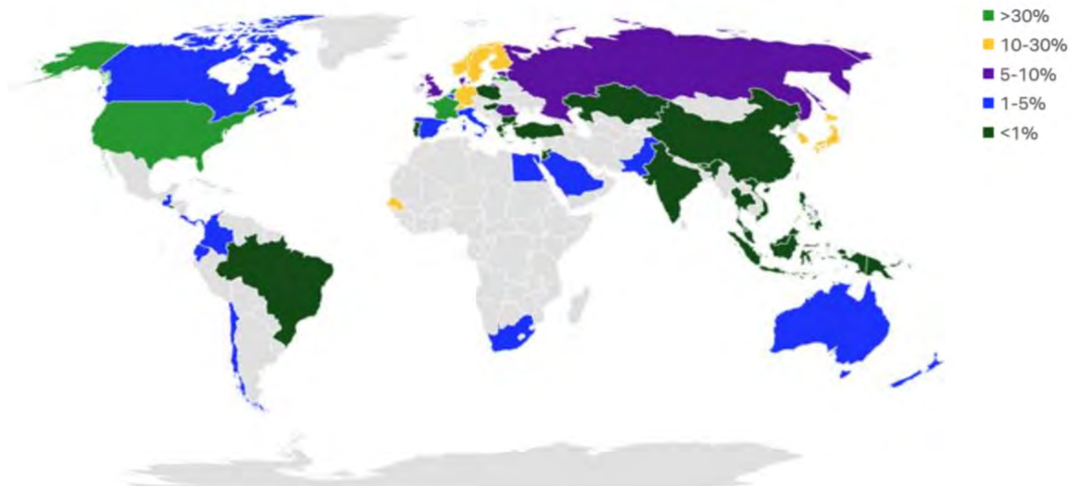
Source: OAG

EXHIBIT 14: GOVERNMENT AID MADE AVAILABLE TO AIRLINES (US$ BIL, AS AT 15 MAY)



Source: IATA Economics and various sources, including SRS Analyser, DDS, FlightRadar 24, TTBS, ACIC, Platts, Airline Analyst, Annual Reports

EXHIBIT 15: GOVERNMENT AID AS % OF AIRLINE TICKET REVENUES



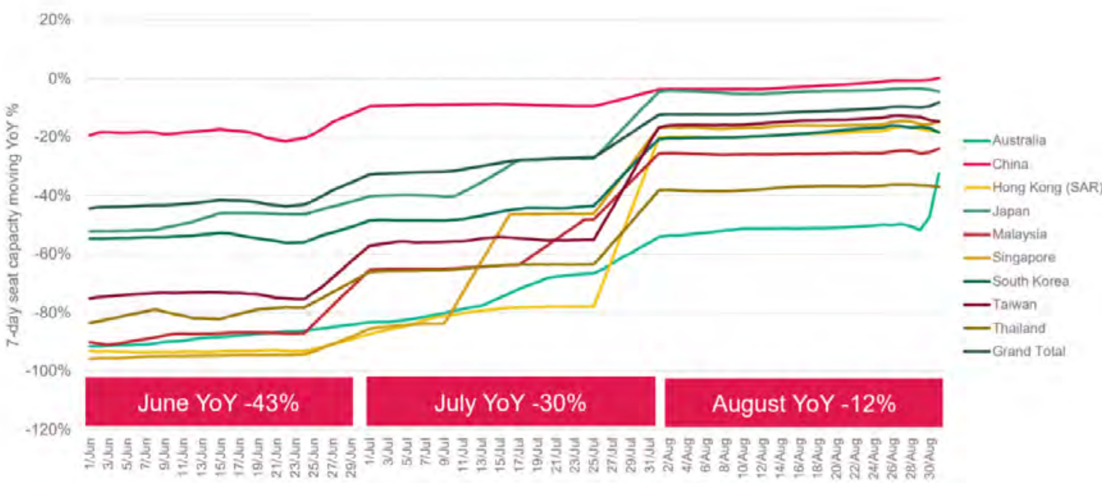
Source: IATA Economics and various sources, including SRS Analyser, DDS, FlightRadar 24, TTBS, ACIC, Platts, Airline Analyst, Annual Reports

EXHIBIT 16: APAC AIRLINES FINANCIAL AIDS

	Period	Air China	Cathay Pacific & Cathay Dragon	ANA	Singapore Airlines
YoY Seat Capacity Change / Load Factor	February	-53% / 52%	-30% / 53%	-4% / 64%	4% / 67%
	March	-44% / 57%	-77% / 49%	-11% / 35%	-33% / 56%
	April	-52% / 66%	-95% / 21%	-38% / 19%	-95% / 9%
Operating Loss (USD Million)	Q1	417	573*	549	522
Government Support		Government financial support in direct subsidy, discounted navigation fee, parking fee waiver, etc.	Announced **HK$39 bn ($5 bn)** recapitalisation plan including HK$27.3 billion from HKSAR government	Undertook **Y350 bn ($3.3 bn)** debt financing from DBJ	Completed its **S$8.8 bn ($6.3 bn)** rights with option to raise additional S$6.2 bn debt capital

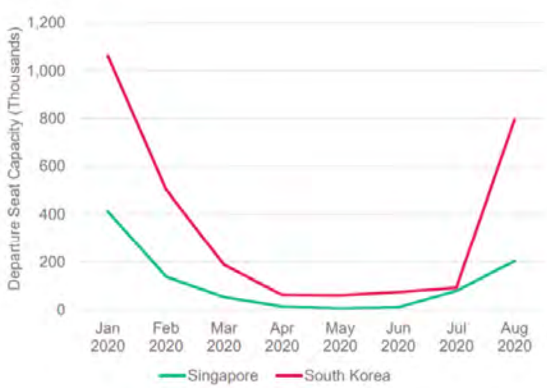
**YTD to April figure*
Source: Cirium Schedules, Airlines announcements

EXHIBIT 17: APAC SEAT CAPACITY (AS AT 21 JUNE)



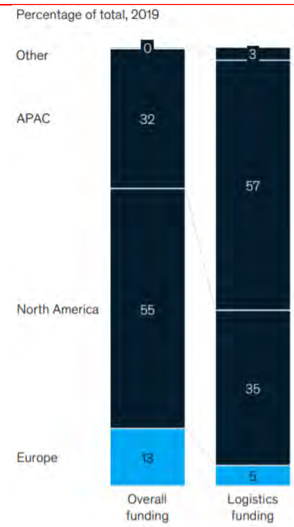
Source: Cirium Schedules

EXHIBIT 18: DEPARTING SEATS FROM CHINA (AS AT 21 JUNE)



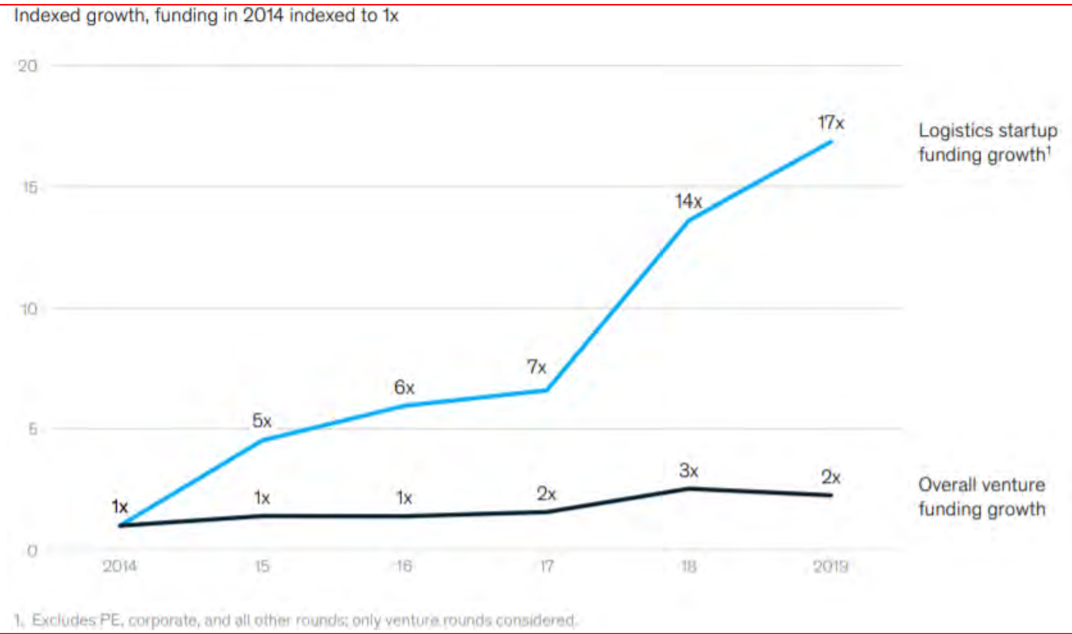
Source: Cirium Schedules

EXHIBIT 19: FUNDINGS IN LOGISTICS VS. OVERALL VENTURE FUNDING



Source: McKinsey, Crunchbase, PitchBook, IMF, Armstrong & Associates

EXHIBIT 20: VENTURE FUNDING GROWTH IN LOGISTICS VS. OVERALL VENTURE GROWTH



Source: McKinsey, Crunchbase, PitchBook

DISCLOSURE AND DISCLAIMER