

# China / Hong Kong Company Update

## Kerry Logistics Network

Bloomberg: 636 HK Equity | Reuters: 0636.HK

Refer to important disclosures at the end of this report

DBS Group Research . Equity

13 Jul 2022

### BUY

Last Traded Price (12 Jul 2022): HK\$16.76 (HSI : 20,845)  
Price Target 12-mth: HK\$21.90 (31% upside)

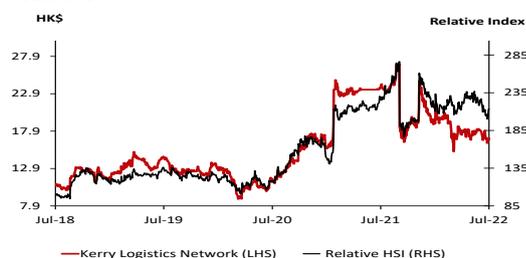
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### What's New

- International freight forwarding continues to be the growth engine
- Higher margins earned for offering supply chain solutions
- Expect higher core profit from continued operations for FY22
- BUY with HK\$21.90 TP

#### Price Relative



#### Forecasts and Valuation

FY Mar (HK\$ m)	2020A	2021A	2022F	2023F
Turnover	53,361	81,771	86,627	74,357
EBITDA	5,469	8,490	8,376	8,185
Pre-tax Profit	4,240	10,391	5,841	5,359
Core Net Profit	1,828	3,692	3,484	3,331
Core Net Profit Gth (%)	33.1	101.9	(5.6)	(4.4)
EPS (HK\$)	1.03	2.05	1.93	1.84
EPS Gth (%)	28.3	98.8	(5.9)	(4.4)
PE (X)	16.3	8.2	8.7	9.1
P/Cash Flow (X)	5.9	4.5	3.3	3.6
EV/EBITDA (X)	5.7	3.7	3.7	3.8
DPS (HK\$)	0.49*	7.99*	0.58	0.58
Div Yield (%)	2.9	47.7	3.5	3.5
Net Gearing (%)	3	CASH	CASH	CASH
ROE (%)	7.2	15.2	15.8	13.7
Earnings Rev (%)			Nil	Nil
Consensus EPS (HK\$)			1.76	1.70
Other Broker Recs:		B:7	S:0	H:5

\*Include special DPS of HK\$0.14 and HK\$7.28 for FY20 and FY21 respectively

Source of all data on this page: Company, DBS Bank (Hong Kong) Limited ("DBS HK"), Thomson Reuters

## Quality choice during challenging times.

### Investment Thesis

**Buy with HK\$21.90 TP.** The stock is trading at a PE of 8.7x and 9.1x for FY22 and FY23 respectively, against its five-year average of 13.3x. Valuation is attractive. Potential synergy with S.F. Holding should bolster its long-term growth, adding to its investment appeal.

### International freight forwarding to underpin growth.

International freight forwarding thrived in 1H22. The prolonged supply chain disruptions enable Kerry Logistics Network (KLN), which can fulfill urgent and complicated orders from clients, to earn better margins. Disregarding contributions from Hong Kong warehouse and Taiwan operations that were sold in 2H21, KLN should see higher core profit in FY22 backed by improved earnings from international freight forwarding.

### Synergies with S.F. Holding to drive long-term earnings.

KLN is the international arm of its controlling shareholder, S.F. Holding. It is the principal service provider outside Mainland China for S.F. Holding's international express business, and serves as the exclusive cargo General Sales Agent (GSA) for S.F. Airlines from 2Q22. Synergies flowing from the integration with S.F. Holding are expected to come through from FY23 and should drive its long-term growth.

### Valuation:

Our TP is based on 11.9x FY23 PE, 0.5 SD below its average PE over the past five years.

### Where we differ:

We are more positive over the company's long-term growth supported by its integration with S.F. Holding, and stronger network coverage for international freight forwarding business.

### Key Risks to Our View:

Delayed retail consumption recovery and recurring pandemic and lockdowns in China would drag the integrated logistics business in Hong Kong. Failure to execute on the M&A strategy and weaker-than-expected synergy with S.F. Holding would undermine growth prospects. Freight rate volatility could lead to lower earnings visibility.

### At A Glance

Issued Capital (m shrs)	1,807
Mkt Cap (HKm/US\$m)	30,285 / 3,858
Major Shareholders (%)	
S.F. Holding Co. Ltd.	51.5
Kerry Properties Ltd	20.8
Kerry Group Ltd.	12.0
Free Float (%)	15.6
3m Avg. Daily Val. (US\$m)	1.70
GICS Industry: Industrials / Transportation	



Watchlist the stock on Insights Direct to receive prompt updates



## Kerry Logistics Network

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### WHAT'S NEW

#### International freight forwarding thrived

**International freight forwarding continues to thrive.** The lockdowns in Shanghai did not impact the international freight forwarding business as Kerry Logistics Network (KLN) had diverted its business to other airports from the Pudong airport. The company also benefitted from the sudden reduction in airfreight capacity led by the Russia-Ukraine conflict in 1H22. Trading volume between Asia and Europe/US and within Asia were higher with high freight rates sustained. With its extensive network coverage in Asia, KLN's international freight forwarding should record strong segment profit growth in 1H22.

**Higher margins amid supply chain complexity.** The Western and ASEAN countries have adopted the "living with COVID" policy. This has resulted in more infections which in turn has led to labour shortages. The prolonged disruptions to supply chain plays to KLN's strength as the company is capable of delivering flexible solutions to fulfil urgent and complicated orders from clients. This should allow KLN to command better margins during challenging times.

#### Mixed performance for integrated logistics business.

Thanks to additional pandemic-related contracts granted by the government, integrated logistics business in Hong Kong is expected to enjoy higher margins and deliver positive profit growth in 1H22.

The pandemic-induced lockdowns in China have severely disrupted manufacturing activities and thus logistics demand. This should result in lower profit contributions from integrated logistics in China in 1H22.

Kerry Express Thailand remains in the red but losses have been narrowing. It is expected to achieve break even by end-2022. Overall, the Asia integrated logistics business should remain an earnings drag in FY22.

KLN intends to increase the proportion of fixed rate loans to mitigate the earnings risk led by interest rate volatility.

#### Profit growth from continued operations should continue.

Strong international freight forwarding business should underpin KLN's good profit growth in 1H22. Disregarding the contributions from the Taiwan and Hong Kong

warehouse operations sold in 2H21, KLN's full-year core profit for FY22 should also be higher even allowing for the recent retreat in freights rates for routes between China and the US.

**Risks ahead.** Faced with prolonged supply chain disruptions led by differing policies to control COVID infections around the globe and potential demand contraction caused by growing inflationary pressure, most multinational corporates have been cutting back on production. This could translate into potentially lower business volume for KLN in the future.

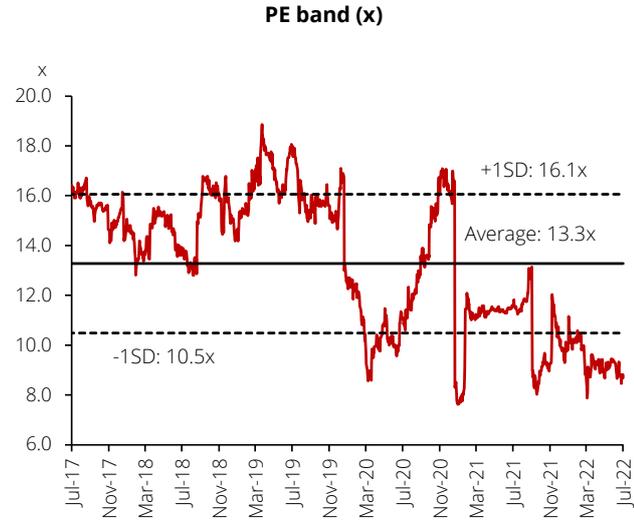
The stock is trading at 8.7x and 9.1 x FY22 and FY23 earnings, against its five-year average of 13.3x. Valuation is attractive even allowing for normalization of freight rates from 2023 onwards. Potential synergy with S.F. Holding could add to its long-term earnings growth. Maintain BUY with HK\$21.90 TP. This implies 31% upside from the current level.

#### Company Background

Kerry Logistics Network (KLN) is the largest international logistics company listed on Hong Kong Stock Exchange. Its business comprises two components namely integrated logistics, which involves a wide range of logistics and ancillary services primarily across Asia, and international freight forwarding, referring to air freight, ocean freight and cross-border road freight forwarding services across Asia and the globe. In 2021, S.F. Holding became the controlling shareholder of KLN. KLN is now become the international arm of S.F. Holding, serving as its principal service provider for its business outside China and is the exclusive cargo General Sales Agent for S.F. Airlines. The recent acquisitions of Top Ocean and remaining stake in K-Apex has further consolidated its position in the IFF sector, being the largest non-vessel ocean common carrier for the Asia to US trade lanes.

**Kerry Logistics Network**

**PE band**



Source: Thomson Reuters, DBS HK

## Kerry Logistics Network

### Segmental Breakdown (HK\$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
<b>Revenues (HK\$ m)</b>					
Integrated Logistics	19,512	17,821	19,796	19,458	20,832
International freight forwarding	21,627	31,796	59,159	67,169	53,526
Discontinued operations	0	3,743	2,816	0	0
<b>Total</b>	<b>41,139</b>	<b>53,361</b>	<b>81,771</b>	<b>86,627</b>	<b>74,357</b>

Source: DBS HK

### Income Statement (HK\$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
Turnover	41,139	53,361	81,771	86,627	74,357
EBITDA	4,686	5,469	8,490	8,376	8,185
Depr / Amort	(1,921)	(2,149)	(2,261)	(2,487)	(2,736)
<b>EBIT</b>	<b>2,765</b>	<b>3,320</b>	<b>6,229</b>	<b>5,889</b>	<b>5,449</b>
Associates Inc	86	118	159	182	155
Interest (Exp)/Inc	(317)	(265)	(243)	(230)	(245)
Exceptionals	2,414	1,067	4,247	0	0
<b>Pre-tax Profit</b>	<b>4,947</b>	<b>4,240</b>	<b>10,391</b>	<b>5,841</b>	<b>5,359</b>
Tax	(605)	(771)	(1,365)	(1,344)	(1,259)
Non-controlling Interest	(554)	(574)	(1,087)	(1,014)	(769)
<b>Net Profit</b>	<b>3,788</b>	<b>2,896</b>	<b>7,939</b>	<b>3,484</b>	<b>3,331</b>
<b>Core Net Profit</b>	<b>1,374</b>	<b>1,828</b>	<b>3,692</b>	<b>3,484</b>	<b>3,331</b>
Sales Gth (%)	8	30	53	6	(14)
Net Profit Gth (%)	55	(24)	174	(56)	(4)
EBITDA Margins (%)	11	10	10	10	11
EBIT Margin (%)	7	6	8	7	7
Tax Rate (%)	12	18	13	23	24

Source: DBS HK

## Kerry Logistics Network

### Balance Sheet (HK\$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
Fixed Assets	21,652	23,196	9,466	10,067	10,160
Long-term Investments	343	365	593	593	593
Other LT Assets	3,986	4,766	4,348	4,348	4,348
Intangibles Assets	4,765	4,772	4,303	7,533	10,877
Deferred Tax Asset	74	98	156	156	156
Associates/JVs	1,387	1,971	2,281	2,281	2,281
Bank Balance/Cash & Liquid	5,846	8,485	9,096	8,822	8,317
ST Investments	469	470	817	817	817
Inventory	505	405	375	375	375
Debtors	10,154	12,362	16,663	17,663	15,663
Other Non Cash Current	25	10	64	64	64
<b>Total Assets</b>	<b>49,204</b>	<b>56,900</b>	<b>48,162</b>	<b>52,720</b>	<b>53,652</b>
ST Debt	2,182	4,163	3,848	3,848	3,848
Creditors	7,426	9,297	11,863	13,863	12,363
Other Current Liab	1,373	1,449	2,129	2,129	2,129
LT Debt	6,174	5,069	2,262	2,262	2,262
Deferred Tax Liabilities	656	744	406	406	406
Other LT Liabilities	4,319	3,698	2,817	2,817	2,817
Non-controlling Interests	4,061	4,997	3,793	4,293	4,442
Shareholder's Equity	23,013	27,483	21,044	23,102	25,384
<b>Total Cap. &amp; Liab.</b>	<b>49,204</b>	<b>56,900</b>	<b>48,162</b>	<b>52,720</b>	<b>53,652</b>
Share Capital (m)	1,712	1,775	1,803	1,807	1,807
Net Cash/(Debt)	2509	747	(2,986)	(2,713)	(2,207)
Working Capital	6,018	6,823	9,174	7,901	6,895
Net Gearing (%)	10	3	CASH	CASH	CASH

Source: DBS HK

### Cash Flow Statement (HK\$ m)

FY Mar	2019A	2020A	2021A	2022F	2023F
EBIT	2,765	3,320	6,229	5,889	5,449
Tax Paid	(602)	(699)	(921)	(1,344)	(1,259)
Depr/Amort	1,921	2,149	2,261	2,487	2,736
Profit or loss on disposal of FAs/subsidiaries/investment	(2,115)	(59)	(2,197)	0	0
Chg in Wkg.Cap	(521)	(128)	(1,671)	1,000	500
Other Non-Cash	1,756	(256)	2,072	(300)	(350)
<b>Operating CF</b>	<b>3,204</b>	<b>4,326</b>	<b>5,773</b>	<b>7,733</b>	<b>7,076</b>
Net Capex	1,490	(1,285)	11,786	(3,089)	(2,829)
Investments	205	12	(1,173)	0	0
Associates & JVs	82	(544)	33	0	0
Associates' Dividends	76	170	99	182	155
Others	75	66	57	70	105
<b>Investing CF</b>	<b>1,927</b>	<b>(1,581)</b>	<b>10,802</b>	<b>(2,836)</b>	<b>(2,569)</b>
Net Chg in Debt	(1,412)	725	53	0	0
Non-controlling interests	27	1,487	(71)	(2,730)	(3,195)
New Capital	118	46	103	0	0
Dividend	(1,450)	(1,306)	(14,523)	(2,440)	(1,818)
Other Financing CF	(984)	(1,208)	(1,281)	0	0
<b>Financing CF</b>	<b>(3,701)</b>	<b>(256)</b>	<b>(15,719)</b>	<b>(5,170)</b>	<b>(5,013)</b>
Chg in Cash	1,430	2,489	856	(273)	(506)

Source: DBS HK

## Kerry Logistics Network

### Target Price & Ratings History



S.No.	Date	Closing Price	12-mth Target Price	Rating
1:	8-Jul-22	HK\$16.52	HK\$21.90	Buy

Source: DBS HK

Analyst: Jeff Yau, CFA  
Percy Leung

## Kerry Logistics Network

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**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

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**FULLY VALUED** (negative total return, i.e., > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

\*Share price appreciation + dividends

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