

SF Holding-A (002352 CH)

Further earnings downside risk; Wait for a better entry point

We like SF's long-term strategy to consolidate its networks, strengthen its position in the time-definite business, boost the supply chain solution business and expand overseas (through the acquisition of **Kerry Logistics [636 HK, NR]**). That said, we believe continuous spending and fierce competition will put pressure on the near-term profitability. We slash our earnings forecast in 2021E/22E by 48%/45%, after the latest management comments that SF will accept lower profit margin over the coming 1-2 years in return for long-term sustainable growth. We downgrade SF to **HOLD** from Buy with new TP of RMB77, and suggest that investors should wait for a better entry point.

- What's changed?** SF unexpectedly released a profit warning last week stating that it will report a net loss of RMB0.9-1.1bn in 1Q21, versus net profit of RMB0.9bn in 1Q20, due to higher cost as well as increase in spending on new businesses such as integrated logistics and supply chain solution. This is far below expectations as SF's parcel volume / revenue grew 54% / 32% in 2M21. During the shareholders meeting last Friday, WANG Wei (the Chairman) revealed that SF will be profitable in 2Q21E but the full year earnings will be unlikely to return to the level in 2020.
- Network integration to improve operating efficiency.** SF is in progress to streamline its network, including the consolidation of the infrastructure and resources for the four networks, namely the main network, Fengwang (network partner model), freight and warehouse. The integration will help improve the operating efficiency over the coming quarters. On the other hand, SF will continue to enhance the product segmentation.
- Valuation.** We roll over our target base year to 2022E as earnings in 2021E is distorted by 1Q net loss. We maintain our target P/E (55x, 38% above historical average) as we believe SF deserves a valuation premium, due to its scarcity value in infrastructure and network, diversifying revenue stream and increasing data/technology-driven business model. Our new TP is set at RMB77.
- Upside risks:** (1) Better-than-expected profit in 2H21E; (2) recovery of parcel shipment ASP. **Downside risks:** (1) prolonged price war; (2) further increase in operating cost; (3) delay of new business development.

Earnings Summary

(YE 31 Dec)	FY19A	FY20A	FY21E	FY22E	FY23E
Revenue (RMB mn)	112,193	153,987	185,074	224,747	269,852
YoY growth (%)	23	37	20	21	20
Core Net income (RMB mn)	4,948	6,883	4,828	6,390	9,495
Core EPS (RMB)	1.12	1.54	1.06	1.40	2.08
YoY growth (%)	32.2	37.2	-31.3	32.3	48.6
Consensus EPS (RMB)	n/a	n/a	2.06	2.57	n/a
EV / EBITDA (x)	30.5	24.1	29.3	23.3	17.6
P/E (x)	64.7	47.2	68.6	51.9	34.9
P/B (x)	7.6	5.9	5.5	5.1	4.5
Yield (%)	0.4	0.5	0.3	0.4	0.6
ROE (%)	12.5	13.9	8.3	10.2	13.7
Net gearing (%)	Net cash	Net cash	0.6	3.2	1.7

Source: Company data, Bloomberg, CMBIS estimates

HOLD (Down)

Target Price: **RMB77.00**
 (Previous TP: RMB114.00)
 Up/Downside: **+6%**
 Current Price: **RMB72.72**

China Express Delivery

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Stock Data

Mkt Cap (RMB mn)	331,344
Avg 3 mths t/o (RMB mn)	2,304
52w High/Low (RMB)	124.7/43.53
Total Issued Shares (mn)	4,448

Source: Bloomberg

Shareholding Structure

Shenzhen Mingde	59.30%
Shenzhen Zhaoguang Inv.	5.85%
Ningbo Shunda Fengrun VC	3.03%
Others	31.82%

Note: Shenzhen Mingde is owned by WANG Wei

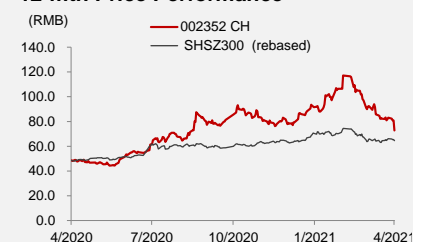
Source: Company data

Share Performance

	Absolute	Relative
1-mth	-11.3%	-11.8%
3-mth	-11.8%	-5.2%
6-mth	-0.5%	-10.7%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

**Auditor: PricewaterhouseCoopers
 Zhong Tian LLP**

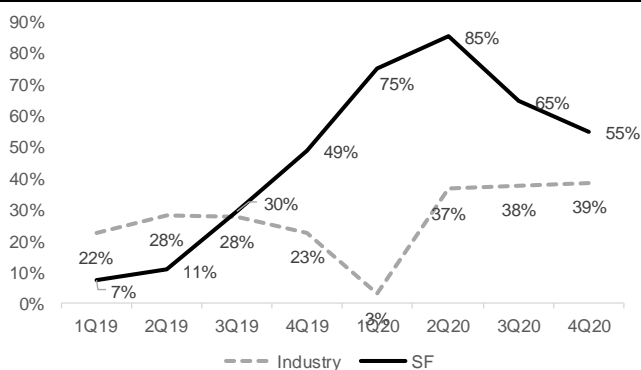
Related report:

China Express Delivery Sector – Bloody battle to end soon; War for market share to continue; BUY winners in the respective playing fields – 14 Oct 2020

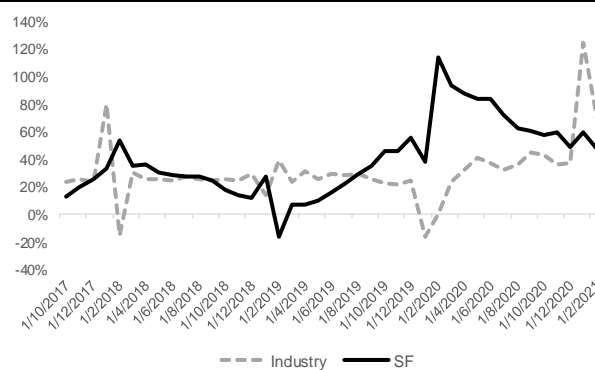
Figure 1: Changes in key assumptions

(RMB mn)	Old		New		Change	
	2021E	2022E	2021E	2022E	2021E	2022E
Shipment volume (mn units of parcel)	10,024	12,530	10,741	13,426	7.1%	7.1%
Growth (YoY)	25.0%	25.0%	32.0%	25.0%	0.3	0.0
ASP (RMB/unit)	17.7	17.5	16.0	15.4	-9.4%	-11.9%
Growth (YoY)	-1.5%	-1.0%	-10.0%	-3.7%	5.7	2.7
Unit cost (RMB/unit)	15.7	15.5	15.0	14.6	-4.4%	-6.1%
Growth (YoY)	-1.4%	-1.2%	-5.2%	-2.9%	2.6	1.5
Unit gross margin (RMB/unit)	2.0	2.0	1.0	0.8	-49.1%	-57.3%
Growth (YoY)	-1.9%	0.3%	-48.8%	-16.0%	24.3	(55.9)
(RMB mn)						
Revenue						
Revenue from express logistic	176,975	219,007	171,831	206,842	-2.9%	-5.6%
Revenue from supply chain	8,262	9,915	10,656	14,919	29.0%	50.5%
Express logistic & supply chain	185,238	228,922	182,487	221,760	-1.5%	-3.1%
Sales of goods	989	1,137	1,417	1,701	43.3%	49.6%
Others	1,155	1,189	1,169	1,286	1.3%	8.1%
Total revenue	187,381	231,248	185,074	224,747	-1.2%	-2.8%
Revenue growth						
Revenue from express logistic	23.1%	23.8%	18.8%	20.4%	(4.3)	(3.4)
Revenue from supply chain	20.0%	20.0%	50.0%	40.0%	30.0	20.0
Express logistic & supply chain	23.0%	23.6%	20.3%	21.5%	(2.7)	(2.1)
Sales of goods	15.0%	15.0%	20.0%	20.0%	5.0	5.0
Others	3.0%	3.0%	10.0%	10.0%	7.0	7.0
Total revenue	22.8%	23.4%	20.2%	21.4%	(2.6)	(2.0)
Gross margin						
Blended gross margin	16.0%	15.9%	12.9%	13.0%	(3.1)	(3.0)
S&D expense ratio	1.7%	1.6%	1.6%	1.6%	(0.1)	0.0
Admin expense ratio	7.8%	7.3%	7.3%	7.0%	(0.5)	(0.3)
R&D expense ratio	1.1%	1.1%	1.1%	1.1%	0.0	0.0
Net profit	9,237	11,608	4,828	6,390	-47.7%	-45.0%

Source: Company data, CMBIS estimates

Figure 2: SF's quarterly parcel shipment volume versus industry

Source: The State Post Bureau, Company data, CMBIS

Figure 3: SF's monthly parcel shipment growth versus industry

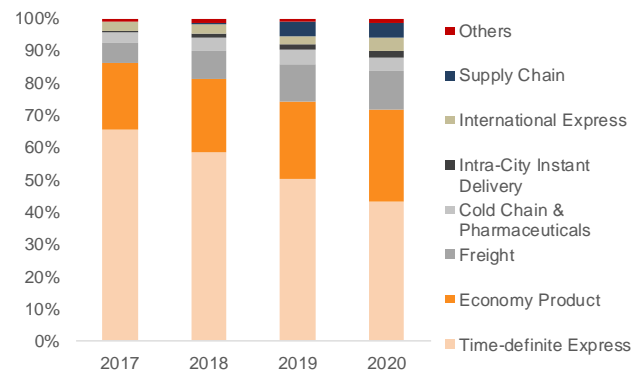
Source: The State Post Bureau, CMBIS

Figure 4: SF's ASP change versus industry



Source: Company data, CMBIS

Figure 5: SF's revenue breakdown



Source: Company data, CMBIS

Figure 6: Key operating assumptions

	2017	2018	2019	2020	2021E	2022E	2023E
Shipment volume (mn units of parcel)	3,052	3,839	4,831	8,137	10,741	13,426	16,514
Growth (YoY)	18.3%	25.8%	25.8%	68.4%	32.0%	25.0%	23.0%
ASP (RMB/unit)	23.1	23.3	21.9	17.8	16.0	15.4	14.9
Growth (YoY)	4.5%	0.5%	-5.7%	-19.0%	-10.0%	-3.7%	-3.5%
Unit cost (RMB/unit)	18.6	19.4	19.2	15.8	15.0	14.6	14.1
Growth (YoY)	4.2%	4.3%	-1.4%	-17.5%	-5.2%	-2.9%	-3.3%
Unit gross margin (RMB/unit)	4.5	3.8	2.8	1.9	1.0	0.8	0.8
Growth (YoY)	5.5%	-15.1%	-27.6%	-29.5%	-48.8%	-16.0%	-7.2%
(RMB mn)	2017	2018	2019	2020	2021E	2022E	2023E
Revenue							
Revenue from express logistic	70,609	89,276	105,983	144,639	171,831	206,842	245,511
Revenue from supply chain	0	400	4,918	7,104	10,656	14,919	20,886
Express logistic & supply chain	70,609	89,677	110,901	151,743	182,487	221,760	266,397
Sales of goods	79	406	491	1,181	1,417	1,701	2,041
Others	585	860	801	1,063	1,169	1,286	1,414
Total revenue	71,273	90,943	112,193	153,987	185,074	224,747	269,852
Revenue growth							
Revenue from express logistic	23.6%	26.4%	18.7%	36.5%	18.8%	20.4%	18.7%
Revenue from supply chain	-	-	1129.5%	44.5%	50.0%	40.0%	40.0%
Express logistic & supply chain	23.6%	27.0%	23.7%	36.8%	20.3%	21.5%	20.1%
Sales of goods	287.1%	413.3%	21.0%	140.4%	20.0%	20.0%	20.0%
Others	82.3%	47.0%	-6.9%	32.7%	10.0%	10.0%	10.0%
Total revenue	24.0%	27.6%	23.4%	37.3%	20.2%	21.4%	20.1%
Gross margin							
Blended gross margin	20.2%	17.9%	17.4%	16.4%	12.9%	13.0%	13.8%

Source: Company data, CMBIS estimates

Figure 7: Earnings sensitivity to ASP and unit outsourcing cost

2021E Net profit (RMB mn)	ASP (RMB/unit)				
	15.20	15.68	16.0	16.32	16.80
-10.17	-5,384	-1,709	741	3,191	6,866
-9.88	-2,932	743	3,193	5,643	9,318
Unit outsourcing cost (RMB/unit)	-9.69	-1,297	2,378	4,828	7,278
	-9.49	338	4,013	6,463	8,913
	-9.20	2,790	6,465	8,915	11,365

Source: Company data, CMBIS estimates

Figure 8: Earnings sensitivity to ASP and unit transportation cost

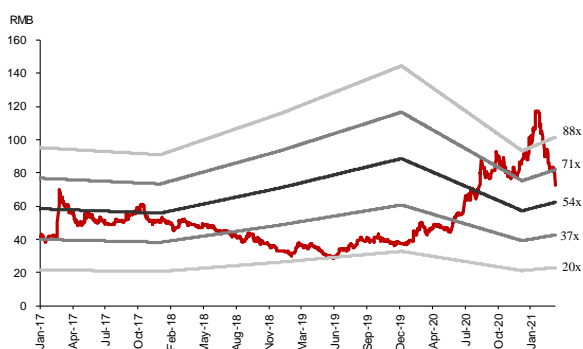
2021E Net profit (RMB mn)	ASP (RMB/unit)				
	15.20	15.68	16.0	16.32	16.80
-1.80	-2,022	1,653	4,103	6,553	10,228
-1.75	-1,587	2,088	4,538	6,988	10,663
Unit transportation cost (RMB/unit)	-1.72	-1,297	2,378	4,828	7,278
	-1.68	-1,007	2,668	5,118	7,568
	-1.63	-572	3,103	5,553	8,003

Source: Company data, CMBIS estimates

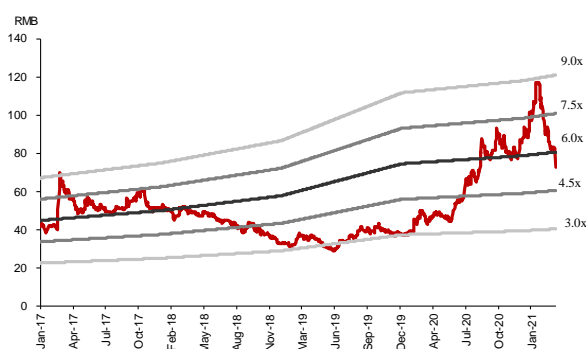
Figure 9: Earnings sensitivity to ASP and unit employee cost

2021E Net profit (RMB mn)	ASP (RMB/unit)				
	15.20	15.68	16.0	16.32	16.80
-1.43	-1,872	1,803	4,253	6,703	10,378
-1.39	-1,527	2,148	4,598	7,048	10,723
Unit employee cost (RMB/unit)	-1.36	-1,297	2,378	4,828	7,278
	-1.34	-1,067	2,608	5,058	7,508
	-1.29	-722	2,953	5,403	7,853

Source: Company data, CMBIS estimates

Figure 10: SF's P/E band

Source: Bloomberg, Company data, CMBIS estimates

Figure 11: SF's P/B band

Source: Bloomberg, Company data, CMBIS estimates

Recap on the acquisition of Kerry Logistics (636 HK, NR)

According to the plan, Kerry Logistics will first sell the Hong Kong warehouse business (the heavy assets) to KGL, the parent company of Kerry Logistics, for a consideration of HK\$13.5bn. After the disposal of the Hong Kong warehouse business, Kerry Logistics will return the cash to the existing shareholders through special dividend of HK\$7.28 per share. If the disposal of the warehouse is not completed before SF's acquisition, the total consideration per share will become HK\$26.08 (i.e. HK\$18.8 + HK\$7.28).

Meanwhile, Kerry Logistics plans to sell the Taiwan business and related loans to KGL. Therefore, the aforementioned acquisition does not include the Kerry Logistics Taiwan business.

On 8 Apr, the antitrust approval has been released by the State Administration for Market Regulation. The transaction is still subject to the approval of HKSFC, HKEX, NDRC, Ministry of Commerce of China, as well as the US Authority.

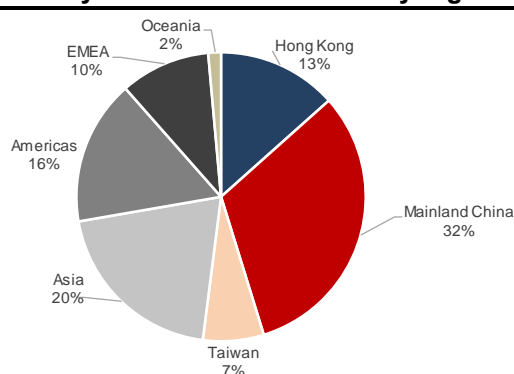
Kerry Logistics offers a broad range of supply chain solutions from integrated logistics, international freight forwarding, industrial project logistics, to cross-border e-commerce, last-mile fulfilment and infrastructure investment. The controlling stake in Kerry Logistics will enable SF to enhance its capability of offering integrated logistics solution and freight forwarding. Upon a successful acquisition, Kerry Logistics will become a platform for SF to expand overseas business. On the other hand, Kerry Logistics will be able to share SF's aircraft capacity.

Figure 12: Potential change in shareholding structure of Kerry Logistics

Before			After		
Shareholder	No of shares (mn)	% of total	Shareholder	No of shares (mn)	% of total
			SF	931	51.5%
KGL	1,134	63.1%	KGL	576	31.8%
Others	663	36.9%	Others	301	16.7%
Total o/s shares	1,797	100.0%	Total o/s shares	1,808	100.0%

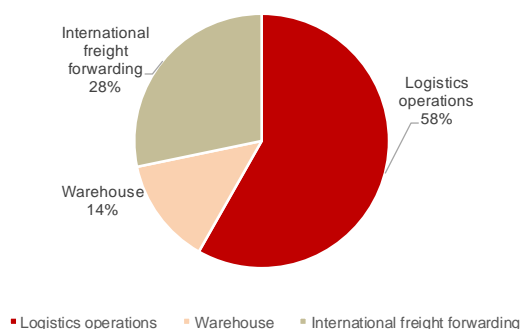
Source: Company data, CMBIS

Figure 13: Kerry's revenue breakdown by region



Note: Based on figures in 2020
Source: Company data, CMBIS

Figure 14: Kerry's segment profit breakdown



Note: Based on figures in 2020
Source: Company data, CMBIS

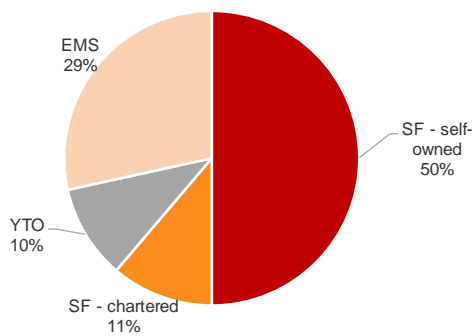
Ezhou Airport project to solidify SF’s core competitive edge in the long run

The construction of Hubei International Logistics Hub project (including Ezhou Airport) is currently in progress. Ezhou airport is jointly invested by Hubei provincial government, Shenzhen Hongyin Airport Investment (深圳市农银空港投资) and SF (equity ratio: 49%/5%/46%). The hub is expected to commence operation in early 2022E. It is estimated that cargo / mail throughput and passenger throughput will reach 2.45mn tonnes and 1mn in 2025.

SF will be able to expand the geographical coverage for its time-definite business through adopting the hub-and-spoke network model. The parcels will first be congregated at the hub and then distributed to the final destinations. According to SF, large aircrafts will be deployed to cover the large cities while small planes (such as Boeing 737) will be used for smaller cities. SF will be able to cover 200 cities upon the commencement of the airport.

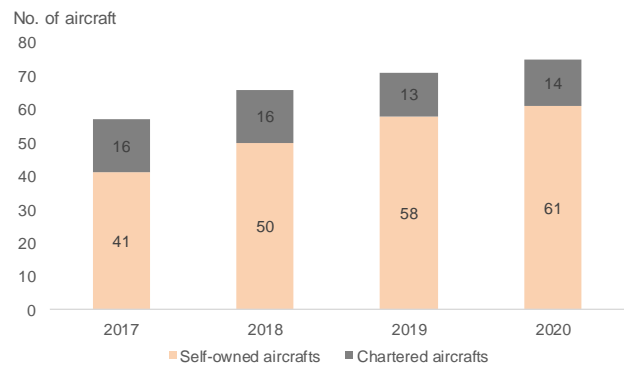
Given that air transportation is more effective with a distance of >800km, we believe the commencement of Ezhou Airport will help SF further expanding to the cities in the North and West regions. Besides, it will strengthen SF’s international business.

Figure 15: SF accounted for >60% of the total no. of all-cargo aircrafts for express delivery in China



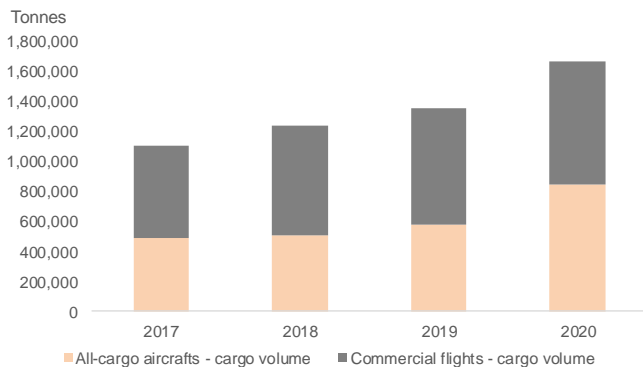
Note: 2019 figures
Source: The State Post Bureau, Company data, CMBIS

Figure 16: SF’s fleet of all-cargo aircrafts



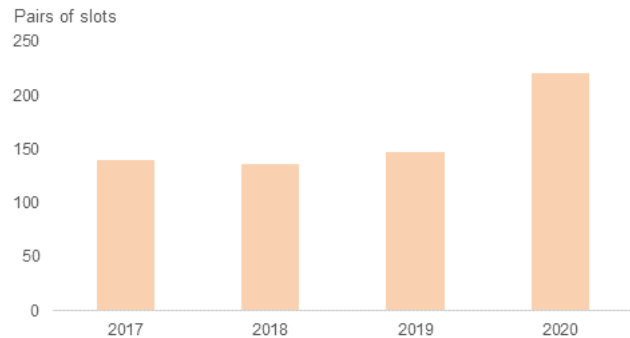
Source: Company data, CMBIS

Figure 17: SF’s air cargo volume

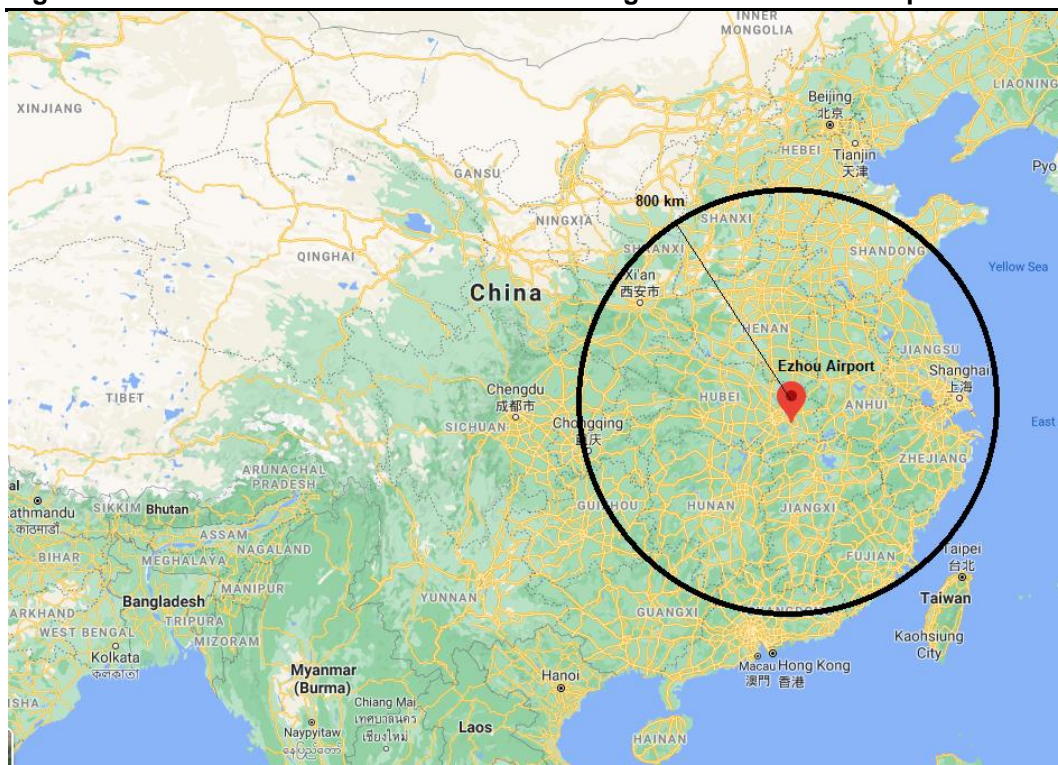


Source: Company data, CMBIS

Figure 18: SF’s total pairs of slots



Source: Company data, CMBIS

Figure 19: Location of the Hubei International Logistic Hub – Ezhou Airport


Source: CMBIS

Equity fund raising exercise

SF plans to raise a total of RMB22bn through issuing new A-share. The new shares will be no more than 10% of the total o/s shares. The shares will be issued to a maximum of 35 institutional investors. According to the regulation, the placement price will be no less than 80% of the average trading price 20 days before the actual day of new share issuance. Lock-up period will be six months. The proposed placement plan is subject to the approval of shareholders and CSRC. The fund raised will be used to finance the capex over the coming two to three years.

Figure 20: Investment projects and use of proceed from A-share placement

Project		Total budget	Use of proceed from placement
		RMBmn	RMBmn
Upgrade of equipment automation	速运设备自动化升级项目	6,238	6,000
Construction of sorting hub in Ezhou Airport	新建湖北鄂州民用机场转运中心工程项目	11,529	5,000
Supply chain digitalization project	数智化供应链系统解决方案建设项目	3,211	3,000
Road transportation capacity	陆路运力提升项目	2,072	2,000
Aircraft component maintenance project	航材购置维修项目	2,084	2,000
Working capital	补充流动资金	4,000	4,000
Total		29,133	22,000

Source: Company data, CMBIS

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	112,193	153,987	185,074	224,747	269,852
Cost of sales	(92,650)	(128,810)	(161,139)	(195,608)	(232,688)
Gross profit	19,544	25,177	23,935	29,139	37,164
Surcharge	(280)	(379)	(370)	(449)	(540)
S&D expenses	(1,997)	(2,252)	(2,961)	(3,596)	(4,857)
Administrative expenses	(9,699)	(11,600)	(13,510)	(15,732)	(18,350)
R&D expense	(1,193)	(1,742)	(2,036)	(2,472)	(2,968)
Impairment loss	(449)	(520)	(740)	(899)	(1,079)
EBIT	5,925	8,684	4,317	5,990	9,369
Net finance income/(cost)	(683)	(853)	(721)	(768)	(776)
Finance income	288	209	153	99	94
Finance expenses	(971)	(1,062)	(874)	(867)	(870)
Other gains/(losses)	2,282	2,229	2,591	3,146	3,778
Share of profit of JV & associates	(98)	(22)	(19)	(44)	49
Pretax profit	7,426	10,039	6,168	8,324	12,419
Income tax	(1,802)	(3,107)	(1,480)	(1,998)	(3,018)
After tax profit	5,625	6,932	4,687	6,326	9,401
MI	172	394	141	63	94
Net profit	5,797	7,326	4,828	6,390	9,495
Core net profit	4,948	6,883	4,828	6,390	9,495
D&A	4,503	4,503	6,538	7,648	8,665
EBITDA	10,429	13,188	10,855	13,637	18,034

Cash flow summary

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Pretax profit	7,426	10,039	6,168	8,324	12,419
Finance cost	892	981	874	867	870
Interest income	(288)	(209)	(153)	(99)	(94)
Profit or loss of associates	98	22	19	44	(49)
Provision for impairment	417	508	0	0	0
Depreciation & amortization	4,533	5,376	6,538	7,648	8,665
Income tax paid	(1,802)	(3,107)	(1,480)	(1,998)	(3,018)
Change in working capital	(664)	(1,579)	(1,194)	(804)	(1,970)
Others	(1,491)	(707)	0	0	0
Cash flow from operation	9,121	11,324	10,772	13,982	16,825
Net capex on PP&E & intangibles	(6,372)	(12,202)	(13,500)	(12,500)	(12,000)
Investment in JV/associates	(245)	(1,523)	(500)	(500)	(500)
Investment in subsidiaries	(5,168)	(74)	0	0	0
Interest received	288	209	153	99	94
Others	(2,552)	(1,295)	(1,368)	(926)	(1,439)
Cash flow from investing	(14,049)	(14,884)	(15,215)	(13,827)	(13,846)
Equity financing/(repurchase)	204	687	0	0	0
Net bank borrowings	9,625	2,648	(500)	0	100
Dividend paid	(926)	(1,189)	(1,500)	(990)	(1,310)
Interest paid	(992)	(1,082)	(892)	(885)	(888)
Others	(540)	268	0	0	0
Cash flow from financing	7,372	1,332	(2,892)	(1,874)	(2,098)
Change in cash	2,444	(2,229)	(7,335)	(1,719)	881
Cash at beginning of the year	16,131	18,521	16,418	9,083	7,363
Exchange gains/(losses) & others	(54)	126	0	0	0
Cash at the end of the year	18,521	16,418	9,083	7,363	8,245

Balance sheet

YE 31 Dec (RMB mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Non-current assets	49,638	59,483	68,517	74,745	80,431
PP&E	18,904	22,357	28,755	33,252	36,443
Investment properties	2,020	2,219	2,219	2,219	2,219
Investment in JV/associates	2,222	3,647	4,128	4,584	5,133
Long term prepaid expense	1,714	1,861	2,554	2,805	3,570
Goodwill	3,565	3,377	3,377	3,377	3,377
Long term trade receivables	466	607	813	788	1,134
Intangible assets	10,008	10,633	11,890	12,937	13,773
AFS investments	4,934	5,027	5,027	5,027	5,027
Others	4,741	8,215	8,215	8,215	8,215
Deferred tax assets	1,066	1,539	1,539	1,539	1,539
Current assets	42,897	51,677	47,913	51,617	57,248
Inventories	882	987	1,309	1,264	1,669
Trade and bills receivables	12,045	16,849	19,659	24,675	28,556
Other receivables	2,190	2,721	3,161	3,613	4,076
Advances to suppliers	2,654	3,177	3,177	3,177	3,177
AFS investments	2,910	6,277	6,277	6,277	6,277
Others	3,495	5,248	5,248	5,248	5,248
Cash	18,722	16,418	9,083	7,363	8,245
Current liabilities	30,982	41,809	43,394	47,489	50,714
Trade and bills payables	11,988	15,485	18,067	22,662	25,788
Other payables	4,707	7,531	7,531	7,531	7,531
Bank borrowings	8,145	10,942	9,942	9,442	9,542
Tax payable	1,139	1,855	1,855	1,855	1,855
Advanced from customers	670	28	30	30	30
Others	4,332	5,968	5,968	5,968	5,968
Non-current liabilities	19,060	12,592	13,092	13,592	13,592
Bank borrowings	17,138	10,291	10,791	11,291	11,291
Deferred tax liabilities	1,388	1,688	1,688	1,688	1,688
Long term employee benefits	204	146	146	146	146
Others	330	467	467	467	467
Shareholders' equity	42,420	56,443	59,768	65,168	73,354
MI	74	317	176	113	19

Key ratios

YE 31 Dec	FY19A	FY20A	FY21E	FY22E	FY23E
Sales mix (%)					
Revenue from express logistic	94%	94%	93%	92%	91%
Revenue from supply chain	4%	5%	6%	7%	8%
Sales of goods	0%	1%	1%	1%	1%
Others	1%	1%	1%	1%	1%
Total	100%	100%	100%	100%	100%
Profit & loss ratio (%)					
Gross margin	17.4	16.4	12.9	13.0	13.8
EBITDA margin	9.3	8.6	5.9	6.1	6.7
EBIT margin	5.3	5.6	2.3	2.7	3.5
After tax profit margin	5.0	4.5	2.5	2.8	3.5
Growth (%)					
Revenue	23.4	37.3	20.2	21.4	20.1
Gross profit	19.9	28.8	(4.9)	21.7	27.5
EBITDA	26.6	26.5	(17.7)	25.6	32.2
EBIT	25.3	46.6	(50.3)	38.7	56.4
Net profit	32.0	39.1	(29.9)	32.3	48.6
Balance sheet ratio					
Current ratio (x)	1.4	1.2	1.1	1.1	1.1
Receivable turnover days	33	36	37	37	37
Inventory turnover days	3	3	3	2	2
Payable turnover days	39	39	38	38	38
Net debt / total equity (%)*	Net cash	Net cash	0.6	3.2	1.7
Profitability (%)					
ROA	7.1	7.2	4.2	5.3	7.2
ROE	12.5	13.9	8.3	10.2	13.7
Per share data					
EPS (RMB)	1.32	1.64	1.06	1.40	2.08
Core EPS (RMB)	1.12	1.54	1.06	1.40	2.08
BVPS (RMB)	9.61	12.39	13.12	14.30	16.10
DPS (RMB)	0.27	0.34	0.22	0.29	0.43

*Net cash includes financial investment Source: Company data, CMBIS estimates

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