COSCO Shipping International (Singapore) Co Ltd

14 October 2021

Non-rated (Initiation)

Price: S$0.28 (as at 11 Oct 2021)

BBG	COS SP
Market cap	S$671.8 m
Price (11 Oct 2021)	S$0.28
52-week range	S$0.179 – S$0.355
Target Price	Non-rated
Shares Outstanding	2,239.2 m
Free Float	42.3 %
Major Shareholder	China Ocean Shipping Company Limited (53.4%)

P/BV (06/21)	1.3x
Net Debt to EBITDA (06/21)	7.6x

Source: Company data, Bloomberg, SAC Capital

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Fine balancing act between returns and expansion

COSCO became an integrated logistics provider in Mar 2018 with the acquisition of Cogent Holdings, which manages 3.5m sf of warehousing space in Singapore (including 1.6m sf at owned Cogent 1.Logistics Hub), and offers transportation, container depot, ISO tank depot, container haulage and freight forwarding services. It acquired complementary logistics businesses in Malaysia, Indonesia and Vietnam to expand its regional footprint.

Logistics takes the lion's share of 70% of revenue and 115% of EBIT in FY20 (EBIT margin of 15.5%). Contributions from other businesses comprising ship-repair and property ownership and management were meagre.

On an expansion trail. The completion of the ~S$114m Jurong Island Chemical Logistics Facility added ~930,000 sf of warehouse space from April 2021. The facility offers space for chemical storage, container depot and ISO tank depot for the petrochemical industry. We expect higher costs from 2H21 while the facility ramps up its operations. COSCO is in talks to lease a piece of land at Port Klang for the construction of a ~300,000 sf warehouse.

According to JTC, warehouse occupancy rate peaked in 4Q20 and dipped 0.2% pt to 89.7% in 2Q21. Rental index edged higher from 4Q20 to 84.3 in 2Q21, but is still down yoy. About 737,149 sqm of space (+6.5%) will come onstream in the next 2 years. While higher e-commerce volume will fuel demand for warehouse and logistics, cutback in stockpiling and border re-opening will see space being free up.

Singapore's cargo throughput have yet to recover to pre-COVID level. Year to August, throughput at the Singapore ports rose 2.5% (FY20: -5.7%). Throughput fell 1.6% yoy in Aug.

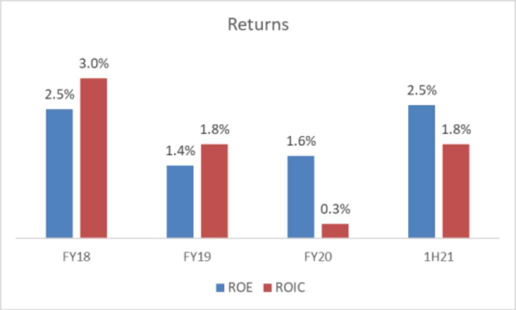
Valuation priced in strong parentage. We think the valuation (P/B 1.3x) is pricing in its strong parentage. At cost of debt of ~2%, and net gearing of 49%, COSCO needs higher returns to support its valuation. The planned divestment of a 60% stake in dry bulk shipping operations for S$57m could lift ROIC.

FY ended 31 Dec (S$m)	FY17A *	FY18A	FY19A	FY20A
Revenue	37.2	163.7	171.5	185.8
EBIT	(26.6)	26.2	19.6	19.5
Net profit	(27.2)	13.2	7.7	9.1
EPS (S cents)	(1.2)	0.6	0.3	0.4
Dividend per share (S cents)	-	-	-	-
Net cash / (debt)	58.5	(105.5)	(232.6)	(266.5)
Valuation				
EBIT margin (%)	(71.7)	16.0	11.4	10.5
ROIC (%)	(1.1)	3.1	1.8	0.3
EV/EBITDA (x)	701.9	15.0	13.6	16.8
P/E (x)	-	50.8	87.2	74.1
Dividend yield (%)	-	-	-	-

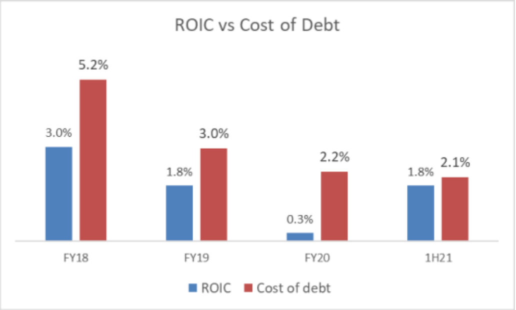
*excludes discontinued operations

Investment Summary

A fine balancing act between returns and expansion



Source: Company data



Source: Company data

COSCO faces a fine balancing act between expansion goals and returns. Thus far, returns have been low (below its cost of debt). This is par for the course given the following:

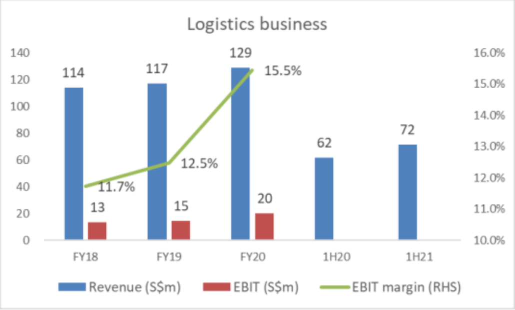
Asset under construction

About S$114m (~13% of net operating assets) has been invested in the Jurong Island Chemical Logistics Facility. The construction commenced in 2018 and obtained TOP in April 2021. While operation is being ramped up, depreciation and finance charges will also kick in from 2H21. We estimate the facility to be profitable from 2H22.

Acquisition of Cogent Holdings

In 2017, COSCO made an offer to acquire Cogent for S$488m, at a price-to-book of 3.4x. A goodwill of $99m still sits in COSCO's books. In FY2016, Cogent turned in S$136.7m in revenue and S$41.4m in EBIT(EBIT margin 30.3%). It is now a pale shadow of its former self, going by the revenue contribution from logistics business.

Post the acquisition of Cogent, COSCO further acquired complementary logistics businesses in Malaysia, Indonesia and Vietnam to expand its regional footprint. In FY20, logistics operations contributed S$129.1m in revenue and S$19.9m in EBIT, or an EBIT margin of 15.5%.



Source: Company data

More expansions in the cards

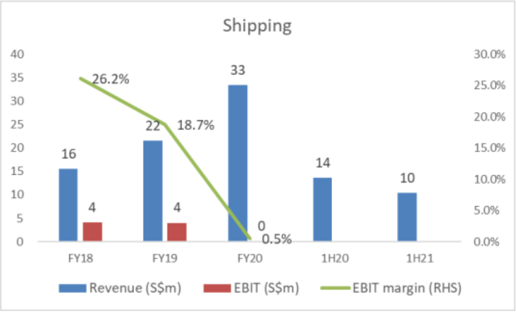
COSCO has plans to add to its Malaysia warehousing space at Port Klang. It is in discussions with Westports Malaysia to lease a piece of land for the construction of a 300,000 sf warehouse. No details have been disclosed on the estimated costs of this expansion.

Investment Summary

Low-yielding assets:

1. Shipping fleet

COSCO owns 3 large dry bulk vessels (Supramax) of total 163,000 tonnes at an average age of 15 years. These vessels are deployed on voyage or time charters. COSCO also charters in vessels to meet some of its shipping contracts.



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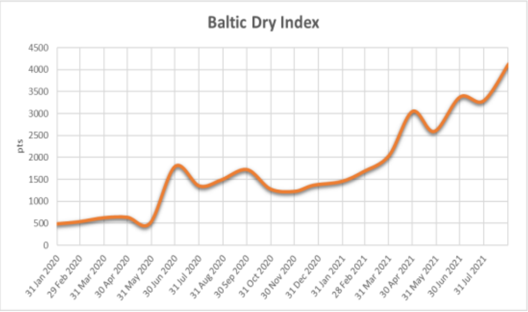


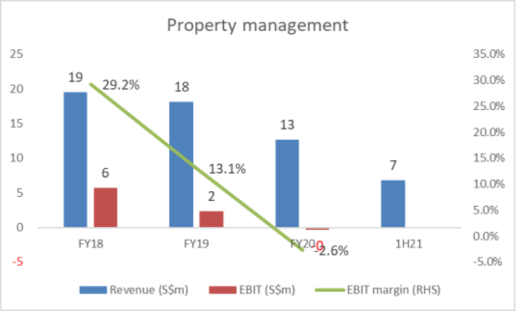
Source: Trading Economics

The shipping business lacks scale and performance has been subpar, in contrast with the strong rebound in dry bulk shipping market. Baltic Dry Index doubled in FY20 to 1530. Year to date, it more than tripled to 5650 due to a tight supply of cargo slots and delay at ports.

COSCO entered into an agreement to dispose of 60% of its shipping operations to a related company for S$57m. The book value of the shipping operations is S$66.8m. The gain on disposal is about S$18m. The deal is subject to shareholders' approval. COSCO will retain a 40% stake at a valuation of S$38m. We think this is a positive step towards lightening its balance sheet.

2. Property investment and management

Rental yields on its investment properties have been impacted by COVID-related rental waivers and rebates granted to the tenants. The investment properties, which comprised of 3 office units, 2 industrial properties, and the Grandstand at Turf City are carried in its books at S$38.5m as at end 2020. The fair value of these assets is S$63.6m according to FY20 Annual Report.



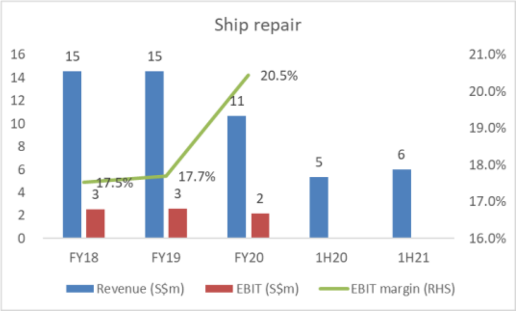
Source: Company data

Investment Summary

Ship repair and marine engineering

The yard in Singapore performs work mainly for owned fleet and jobs from the COSCO group, we believe. Parent China Ocean Shipping Company is the world's largest fleet owner, with a total fleet of 1371 vessels comprising of containers, dry bulkers and tankers with a total capacity of 113.7m DWT.

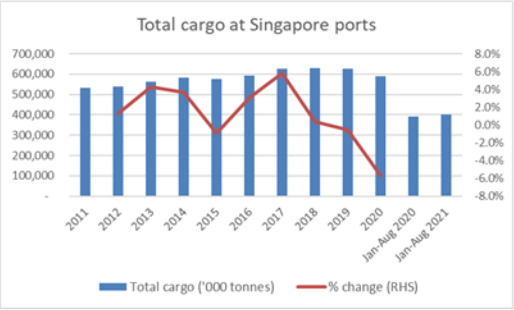
There is no explicit expansion plan for this segment. We believe the group will retain this operations unless the Singapore yard is sold or the lease is not renewed on expiry.



Source: Company data

Investment Summary

Higher expected cargo throughput

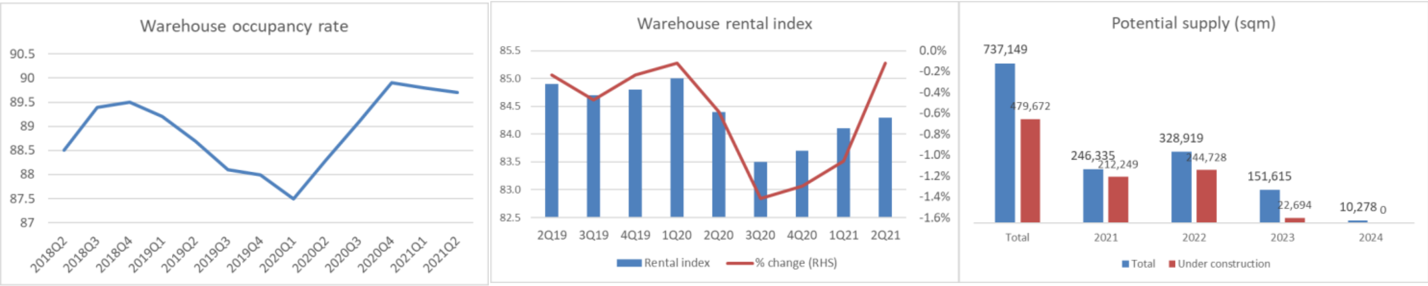


Source: Maritime and Port Authority of Singapore

Year-to-August, total cargo throughput at the Singapore ports rose 2.5%, after a decline of 0.6% in 2019 and 5.7% in 2020. For the month of August, however, total cargo volume was down 1.6%, mainly due to delays at ports.

Total trade growth is likely to be led by post-COVID recovery in global economy. The World Bank has projected that global economy will grow by 5.6% in 2021 and 4.3% in 2022. We expect cargo volume growth to rise in tandem, and port congestions to ease with lifting of COVID restrictions.

Cautious outlook for warehouse space



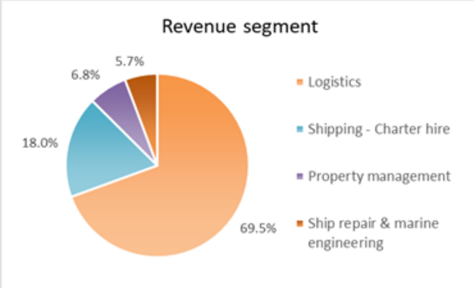
Source: JTC

Occupancy rates have improved from 2Q2021 due to surge in e-commerce transactions, national stockpiling and manufacturers seeking more space to hold inventory nearer to their customers or production plants. We do expect occupancy rates to ease as the borders re-open. Warehouse rents, however, have been falling, but the decline has levelled off to about -0.1% in 2Q21.

With a potential supply of 737,149 sqm coming onstream, or 6.5% of existing stock, we think rates and occupancy are likely to fall further in 2022.

Background

COSCO positions itself as an integrated logistics service providers in Southeast Asia. Logistic services form the main bulk of the Group's business and revenue. Its extensive portfolio of customers includes companies from petrochemical, consumer and construction chemical, oil & gas and marine industries. It also leases out its facilities to third party logistics service providers. COSCO has established an intensive logistics network across Singapore, Malaysia, Indonesia and Vietnam through its subsidiaries and associates.



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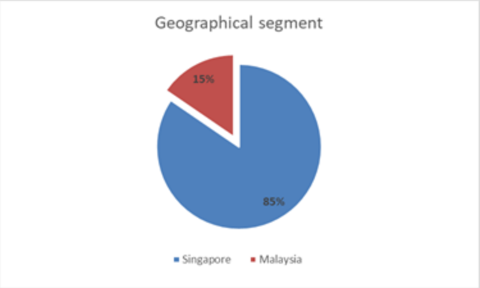


Source: Company data

Logistics operations in Singapore

Logistics services operate mainly out from Cogent 1.Logistics Hub which is owned by Cogent Holding. The hub is a 6-storey warehouse building with a gross floor area of over 1.6m sq metres. It holds 4 general warehouses, 4 NEA-controlled warehouses and 1 flammable material warehouse and a sky depot which can store more than 8500 TEUs of empty containers. Cogent 1.Logistics Hub is strategically located at 1 Buroh Cescent, in close proximity to Jurong Island, Jurong Port, Tuas Mega port and Pasir Panjang terminal. This allows Cogent to provide greater convenience to its customers at shorter transportation time and lower transportation costs. Additionally, as the hub holds both container depots and warehouses at the same location, Cogent can easily retrieve and return empty container from the container depot for loading/unloading of goods in the warehouses. This provides a seamless operational process which significantly improves operational efficiency in terms of reducing waiting and response time and optimizes operational costs.

On top of warehousing and transportation services, Cogent handles automotive logistics, project cargo and freight forwarding as well. It has a fleet of over 100 prime movers and 400 trailers to support its extensive logistics services.

Cogent has completed the construction of JICLF in 2021 and obtained temporary occupation permit for the facility. Located at Tembusu Crescent, Jurong Island, JICLF is an 8-storey general warehouse building with mezzanine offices, a chemical warehouse, an ISO tank depot and a few container depots. It has a gross floor area of over 87,500 sq metres with heavy floor loadings ranging from 20 to 180kN/m^2. This added capacity allows Cogent to cater to the growing demand for logistics services from petrochemical companies in the vicinity.

Background

Pursuing both organic and inorganic growth

The Group actively looks for strategic acquisitions and investments to expand its logistic network and enhance its presence in the region. Cogent acquired an 80% stake in 4 Malaysian logistics companies in Feb 2020. Cogent is also firming up a lease agreement with Westports Malaysia Sdn Bhd to lease a piece of land at Port Klang for the construction of a warehouse of approximately 300,000 sq ft. Port Klang is Malaysia's principal port and has links with over 500 ports around the world. In 2020, the port registered 13.4m TEU container throughput, ranking it in the 12th place for top ports in the world. Discussions are underway although it is temporarily delayed due to Movement Control Order.

Dry Bulk Shipping

COSCO leases its vessels to charterers for the transportation of raw materials such as grains, coal, iron ore and cement on time or voyage charter. It owns 3 Supramax vessels with a total tonnage of 163,000 tons and an average age of 14 years. Apart from its own fleets, COSCO also charters in bulk carriers at a thin margin to cope with additional demand. Orders usually come from long term regular customers.

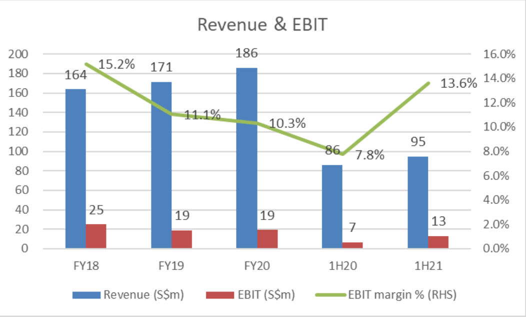
Property management

COSCO is a master tenant for The Grandstand, a 1m sq ft property located at 200 Turf Club Rd. The lease on the land has been extended to end in Dec 2023. It hosts retail outlets, enrichment and activity centers and one of the largest car mart in Singapore. Its subsidiary, Harington Property Pte Ltd also owns office units in Suntec City, with a total floor area of 1,336 sqm and are currently rented out to a key tenant. Rental revenue for FY20 is lower due to rental waiver granted to tenants under the Government Rental Relief Framework. Rental income has since improved in 1H21 with fewer rental concession and registered an operating margin of 25%, a turnaround from the red in FY20. However, rental rates has yet to improve as 1H21 rental rates were lower than 1H20 rental rates.

Ship repair & marine engineering

COSCO engages in ship repair & marine engineering activities including fabrication work services and provision of marine outfitting components. Located at 52 Penjuru Lane, the group has a ground floor steel fabrication workshop of about 1200m^2 and a warehouse of 10,000 sq ft for providing logistics support such as spare parts transit and equipment storage. Its yard measures at 7000m^2 with a waterfront of 80m. Its ship repair business has expanded beyond Singapore and to countries like Indonesia, Malaysia, Philippines, Vietnam, Thailand, Sri Lanka, India and Bangladesh with the help of business partners. COSCO also provides round the clock emergency services for all types of vessels. (e.g. oil tankers, bulk carriers and container liners)

Financial summary



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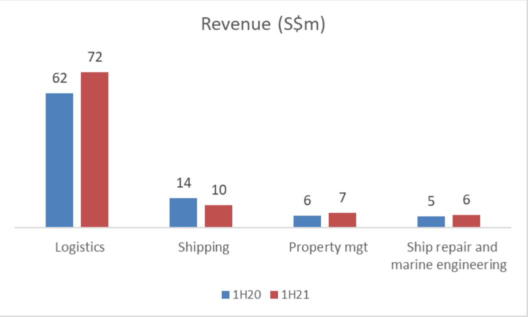

Source: Company data

FY2020 performance

Logistics operations remain the key earnings driver. The new Malaysian businesses acquired helped to lift revenue (+S$18.4m) in FY2020, without which revenue was hit by rental waivers and decline in demand for automotive logistics services. Shipping revenue rose 55% due to more chartered-in vessels, which are low-margined business.

Logistics contributed 115% of EBIT (S$20m). The other divisions contributed marginally to profit or were in the red.

Excluding government grants of S$12m, the group would have incurred a net loss of about S$4m.

1H21 performance

1H21 revenue were 10% higher yoy, but 5% lower than 2H20. Net profit of S$6.8m was 382% higher yoy due to lockdowns in 1H20, but were flat when compared with 2H20. The company does not disclose segmental breakdown for profits for 1H.

Net gearing as at 30 June 2021 was 49.4%, with net debt totaling S$273m. Proposed disposal of 60% in shipping operations will help to deconsolidate its debt book from the Group hence improving Cosco's overall gearing. Exact amount of debt carry by its shipping business is not disclosed.

Government grant (1H21: S$2m) will not recur in 2H21. Depreciation charge and finance costs for the Jurong Chemical Facility will also kick in from 2H21. We think COSCO might be able to book S$18m gain on disposal of 60% of the shipping company, which might help lift FY21 net earnings.

Comparables

COSCO's valuation, at 1.3x P/B and 74.1x FY20 PER, is way ahead of peers. We believe this is pricing in its strong parentage.

Name	YE	Mkt Cap	Revenue	EBITDA	EBIT	Net profit	EBIT margin %	Net margin %	ROE %	ROIC %	EV/EBITDA (x)	EBIT/EV %	PER (x)	PBR (x)
Cosco Shipping International (Singapore) Co Ltd (BBG: COS SP)	Dec 20	671.8	185.8	66.6	19.5	9.1	10.5	4.9	1.7	0.4	14.1	2.1	74.1	1.3
Vibrant Group (BBG: VIBG SP)	Apr 21	64.4	162.9	40.9	17.7	3.3	10.9	2.0	1.4	2.1	2.9	14.9	19.6	0.3
CWT International (BBG: 521 HK)	Dec 20	162.8	7594.5	212.8	89.7	11.6	1.2	0.2	1.6	-55.1	4.6	9.1	14.0	0.2

Source: Companies' data
Exch rate used: 1 HKD to 0.17 SGD

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