SingPost's H1 FY20/21 Results Briefing, 6 November 2020

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Operator:

Ladies and gentlemen, thank you for holding. We are now ready for the briefing. I shall now hand over to the management of SingPost to begin the briefing. Thank you, please go ahead.

Mr Jason Lim (Head, Corporate Planning & Investor Relations):

Good morning everyone, my name is Jason from Corporate Planning & Investor Relations. Welcome to SingPost's results briefing for the first half of FY2020/21. With me today is our GCEO Mr Paul Coutts, GCFO Mr Richard Lai and CEO of Postal Services and Singapore Mr Vincent Phang. I'll now hand over to Richard to start the presentation. Richard, please.

Mr Richard Lai (Group CFO):

Thank you. Good morning and thank you for joining us today. SingPost delivered a resilient set of results for the first half of FY2020/21, amid a tough operating environment. Revenue rose 9.6% led by growth in the Post & Parcel and Logistics segments, with strong eCommerce volume growth across the group.

Notwithstanding the higher earnings contribution from eCommerce, COVID-19 related disruptions impacted profitability, leading to about 50% decline in Group's operating profit. Underlying net profit declined by about 40% due to COVID-19 related disruptions, partly offset by higher earnings contribution from eCommerce growth in Singapore and Australia, as well as the absence of losses from discontinued operations.

Let me now move on to Expenses. Volume-related expenses rose by nearly 27% due to higher eCommerce volumes, exacerbated by a spike in international conveyance costs as a result of severe flight disruptions. Labour & related expenses rose by slightly more than 6% due to increased eCommerce-related deliveries in line with volume growth, as well as higher costs to deal with COVID-19 disruptions such as health and safety arrangements, partially offset by JSS. Admin, Selling-related & other expenses rose by more than 8%, largely due to higher provisions for bad debt. These led to an overall increase in operating expenses by slightly more than 18%.

We now move on to an overview of the various segments' contribution to Group revenue and profit on operating activities. Revenue growth was contributed by the Postal and Logistics segments. For Profit on Operating activities, the improvement in Logistics was offset by declines in Postal and

Property. In the next slide, we will share more details on the various segment's profit on operating activities.

Post & Parcel profit on operating activities declined 67% to S$22.7m in the first half. There are 3 distinct components in this movement. The International business suffered from COVID-led conveyance cost impact and margins were largely eroded. This should recover over time. The Domestic letter business continues to decline, as expected. On the other hand, the Domestic eCommerce business has grown strongly, and points the way for us moving forward.

The Logistics segment recorded a strong turnaround with a profitable position, from higher adoption of eCommerce activities in Asia-Pacific. Our reengineering of processes also led to more customers for eCommerce logistics solutions, such as warehousing, fulfilment and front-end solutions.

Property earnings declined 11.4% largely due to rental rebates provided for eligible tenants which amounted to around S$3.2m, as well as lower car-park and atrium sales revenue. In the Others segment, expenses were higher by more than 10% due to reversals of one-off expenses amounting to S$1.2m last year. If we exclude this, the Others segment remained stable.

Let me now move on to the Cash flow and Financial indicators. For the half year ended 30 September 2020, operating cash flow rose strongly due to positive movements in working capital.

Due largely to the net repayment of bank term loans and fixed rate notes of S$101 million, our cash position declined by S$34.3 million. The repayment was largely for surplus cash drew from uncommitted working capital lines, that has since been replaced by committed working capital lines.

The Group remains in a net cash position as at September 2020. With the strong operating cashflows, our net cash position improved to S$195 million, compared to S$129 million at the start of the financial year. EBITDA to finance expense ratio was lower due to lower EBITDA generated during the year.

We will now provide an update on the contribution of eCommerce to the Group's business. Let me hand you over to Vincent.

Mr Vincent Phang (CEO, Postal Services and Singapore):

Thank you, Richard and good morning everybody once again. I will give a bit of colour and update around the Group eCommerce activities.

We've seen strong eCommerce volume growth across the Group in the first half of this financial year. Domestic Post and Parcel eCommerce continued to gain strong traction as volumes rose 43% to 17.8 million items shipped. CouriersPlease volumes also rose strongly, with consignment volumes rising 55%. International Post & Parcel business delivered a resilient performance as volumes rose 13% in the first half, despite the flight disruptions out of Changi as mentioned by Richard earlier. At the Group level, eCommerce-related revenues are now estimated to drive around 65% or around two-thirds of all revenue, compared to 57% in the same period last year.

The contribution from Domestic Post & Parcel eCommerce business has accelerated in recent months. eCommerce revenue contribution is now one-third of Domestic Post & Parcel revenue, up 14 percentage points from the same period last year.

There is a chart here that shows the rate of eCommerce revenue growth, compared to letter revenue decline in the Domestic Post and Parcel business. As you can see, there has been a strong uptick in recent quarters. The decline for letter mail will unfortunately continue as is expected for all postal operators. But with eCommerce revenue starting to increase, from an aggregate standpoint, we will start to approach what we term a replacement rate for revenue. I will explain a bit more in the next couple of slides.

This slide shows what our eCommerce businesses would look like if they had been standalone businesses by themselves. The indicators would show that these are very strong and robust businesses on their own.

In the Domestic space, eCommerce revenue rose 60% to S$34 million and our estimated market share here in Singapore is about 45%. Our International business delivers to around 200 territories globally, and for the half year, revenue grew 13% to S$276 million.

I will now talk a little bit more on the decline on the letters and printed papers. This continues to decline, as expected, with both revenue and volume down by 24% in the first half. Despite this and the COVID crisis, we have continued our focus on service levels and have been meeting consistently high service standards. As for Parcels, we have also put in significant investments to improve our service levels which have no doubt been recognized by our customers, leading to stronger volumes. We've got some charts there that show the SLA or service levels achieved by the postal and parcel businesses accordingly and we are ready and quietly confident of our execution as we move into the yearend peak season.

I will now talk about our international post and parcel business. Compared to pre-COVID periods, as you all know, the number of flights out from Changi Airport has reduced significantly. Reports put it at more than 90% reduction. Consequently, the conveyance costs ex-Singapore or the airfreight costs have surged by close to 3 times that we experienced in June this year and remains close to 2 times as at the end of September. These had the effect of largely eroding our profits at the International business despite moving all the volumes through.

We have put in place measures to work around this. We have started to use multi-modal ways to transport items as an example. But ultimately, the recovery of this business will have to depend on how fast Changi Airport flights will resume. Hopefully that gives you some explanation there about International business.

We will now move on to the segmental results and I will now hand you over to Jason.

Mr Jason Lim (Head, Corporate Planning & Investor Relations):

Thank you, Vincent. So I will just quickly cover some of the segment results. In the Post and Parcel segment, revenue rose 5.2%, due to International revenue growth, in particular for the first quarter of the financial year. As shared earlier in the presentation, International margins were largely eroded due to higher conveyance costs. As a result, you can see Profit on operating activities declining 67.1% to S$22.7 million. This was partly offset by growth in Domestic eCommerce contribution.

Moving on to the next slide in the Logistics segment, revenue rose 20.3% to S$293 million largely due to eCommerce logistics. In particular, CouriesPlease revenue rose 48% on strong volume growth in Australia. Quantium Solutions and SP eCommerce benefitted from process reengineering, leading to more customers for eCommerce logistics solutions. The Freight forwarding business was resilient despite challenges in the global trading environment. As such, the segment saw a strong turnaround to a profit of S$5.7 million.

Property & Self-storage revenue declined 7.8% or S$4.7million due to rental rebates provided to eligible tenants, and lower receipts from car-park and atrium sales. Consequently, Profit on operating activities was lower by 11.4% or S$3.0 million. SingPost Centre retail mall remained at close to full occupancy as at 30 Sep 2020 while committed occupancy for office/enrichment was 99.1%.

I shall now pass the time back to Richard to share some details on the retail mall's performance.

Mr Richard Lai (Group CFO):

Thank you, Jason. As can be expected, compared to the same period last year, footfall and tenant sales remain down, largely due to the Circuit Breaker period when many shops had to close as well as the Work From Home as the default setting means that not everyone is back to the office just about yet. However, there has been a gradual recovery since Singapore's gradual reopening, as shown in the chart on the right. Tenant sales have now recovered to 80% of the pre COVID-19 levels which is a very good sign.

Next, let me provide an update on leasing. Leases expiring in FY2020/21 for both the mall and office have been substantially renewed, and we have achieved a high renewal rate for our expiring leases. At the start of the year, there was a substantial amount of leases due for renewal during the year, in particular for the retail mall. Around 85% of these leases have since been successfully renewed, and consequently the lease expiry profile has been extended outwards.

We will now move on to the Outlook.

There remains significant uncertainty in the operating environment due to Covid-19. Group earnings and operating cashflows will continue to face headwinds from the disruptions to businesses as detailed above. The extent and duration of the headwinds will depend on when the global pandemic situation will ease up. The Group is carefully managing its expenses, cashflow and liquidity. Notwithstanding the immediate challenges, SingPost remains committed to its transformation efforts.

The Group is implementing the Future of Post initiative, which will reengineer the Postal business to capture the broader growing opportunities for smart urban logistics. A key component of this ecosystem, the world's first-ever "Smart Letterbox", will commence public trials before the end of the calendar year. Meanwhile, Property contribution from SingPost Centre retail mall and office is expected to remain relatively stable. With a relatively strong balance sheet, the Group will continue to seek out new opportunities that will strengthen its capabilities and competitiveness in key markets.

On 19 October 2020, the Group announced that it has entered into a conditional sale and purchase agreement to acquire an aggregate 38% equity interest in Freight Management Holdings Pty Ltd for an aggregate consideration of approximately A$85.0 million.

The acquisition will allow the SingPost Group to further scale its Business-to-Business-to-Consumer logistics capabilities in Australia, and capitalise on the growing eCommerce segment. Together with CouriersPlease and Quantium Solutions Australia, the Group aims to derive synergistic benefits, grow volumes and build scale. This provides a strong platform for the SingPost Group to drive revenue and earnings in Australia over the long term.

Let me move on to dividends. The outlook remains uncertain due to the ongoing COVID-19 situation, and the Group needs to adopt a prudent approach in managing cash flow. For the half year ended 30 September 2020, the Group has announced an interim dividend of 0.5 cent per ordinary share, which represents a payout ratio of 36% of the first half's underlying net profit.

Before we end the presentation, I would like to provide a recap on our strategy, based on our 3 key thrusts – Deploying Smart Urban Logistics to Dominate in Singapore, Building an Integrated B2B2C Network to Tap Growing Demand and a Renewed Focus on Property to Optimise and Grow Returns.

So with that, thank you. I will now hand you back to Jason.

Mr Jason Lim (Head, Corporate Planning & Investor Relations):

Thank you, Richard. We have now reached the end of our presentation, and thank you all for joining us.

We are now ready for the Q&A session. Operator, can you take over please?

Operator:

Thank you. Ladies and gentlemen, we will now begin the question and answer session. If you wish to ask a question, please press *1 on the telephone and wait for your name to be announced. If you wish to cancel your request, please press the '#' key. Once again, it is *1 to ask a question. Your first question comes from the line of Rachael Tan from UBS. Please ask your question.

Ms Rachael Tan (UBS):

Hi, good morning. This is Rachael from UBS, I have a couple of questions. Maybe these are a bit more qualitative in nature. The first question, who are the customers who are using the eCommerce element of DPP? Are they firms, businesses or consumers? And then on the second question, can you explain what FMH does and how will it complement your existing Quantium Solutions and CouriersPlease businesses in Australia? Thanks

Mr Vincent Phang (CEO, Postal Services and Singapore):

Thanks Rachael, this is Vincent. I will take the first question and maybe Paul and Richard can take the second one.

So as you said it's qualitative, I can't obviously disclose too much about the customer details but the Domestic Post & Parcel business has a growing eCommerce element as you know and as the bedrock of the postal service here we do ship and deliver to everyone in Singapore every day and we serve a multitude of customers. The growth that we see are a combination of platforms – there are brands, there are sellers, local eCommerce scenes, there is some C2C as well, a lot of B2C. So I would say that it's been quite a good sign to see that the eCommerce activities through this COVID period has actually ramped up and we are happy to see that that's directional and we have largely been able to serve the needs of Singaporeans – you know we are Essential Service, we continue to operate through the COVID situation.

Our service levels while initially affected by the WSH requirements placed on us, we have largely recovered that and we have been serving that pretty high service levels as you can see in the presentation earlier. I would say it's a broad base of customers, it's not limited to any particular segment and we are pretty excited about doing more business with the eCommerce space here in Singapore. Hopefully, that gives you some colour.

Ms Rachael Tan (UBS):

Just to follow up on that, you said broad base of customers for the eCommerce portion. Just wondering in terms of the partnerships – have you established any partnerships with major eCommerce platforms in Singapore and the region and how do you see the take up or traction? Just directionally.

Mr Vincent Phang (CEO, Postal Services and Singapore):

The short answer is yes, I believe we have partnerships with every single one of those platforms without naming names, and not just the local ones, the big platforms locally there are probably two or three that you know of. And also the international ones which are both from Asia and the West so we have those customers with us and directionally the trends for all of them have been moving the right way basically. All their sales and their volumes are growing on a tear and we've been part of that story together with them. Does that help, Rachael? Is there something else you were looking at?

Ms Rachael Tan (UBS):

Yes, that's good enough for me. Thanks, so maybe we move on to FMH?

Mr Richard Lai (Group CFO):

Let me try and explain it this way. One of our key thrusts is to build an integrated B2B2C network to tap the growing demands especially in the eCommerce field. So what the Group currently has is it has last mile delivery capabilities in Australia and of course in Singapore. It has some fulfilment and warehousing capabilities which is what the B2C element is and we have some front-end solutions as well. So if you think about it when you go to an online website or when you go onto the phone, when you go and buy something, typically what people sometimes don't realize is that the landing page on which they do that adding to cart and the sort of thing – some of these customers – they are actually managed by us. So from there it goes to the fulfilment and warehousing side of the business where we then pick and pack the stuff and then off to the last mile delivery which typically is us or somebody else, then they can send to you.

But what we are currently not terribly strong at is the B2B element, the part where you bring by bulk to a particular destination. So for example, we could be moving some things by bulk from U.K to Singapore or to Australia for that matter. At the moment, that is an area where we are a bit patchy on our capability, it's usually fulfilled by somebody else who is bigger in the B2B element. What we are trying to do is obviously to try and build our strength in that particular area as well so it's a very natural part or evolution of the business. If you are always doing the fulfilment and warehousing then there's obviously synergies to be had if you can do the B2B component instead of relying on somebody else to bring the goods in to break the bulk and supply you just enough so that you can do your fulfilment and warehousing.

So that's the intent behind building that B2B2C integrated network and when we invested into Freight Management Holdings, their business is more into the B2B side although they are actually looking at building up a B2C capability as well which is what we have in Australia but what we don't have is the B2B capability. So investing into them allows us to have that as well as to drive more volumes into

CouriersPlease which is the last mile deliverer for us in Australia. It also allows us to further scale up on a particular market which first, it's sizeable, in terms of this particular business it is in fact bigger than Singapore, but it is a business that we have not in the past built up a lot of scale ever since we bought CouriersPlease. So we thought that it is timely to build our scale on that, and if you have been following us, one of the biggest bugbear in the logistics side of the business has been the fact that it has been operating on a sub scale basis. And in this business, without scale you don't make money – the margins are thin relatively speaking so if your margins are relative thin, the only way is to get a lot of volumes and that's what we are trying to do and Australia makes a very sensible approach simply because of the fact that outside of Singapore, Australia is probably the next largest market that we have a decent presence in that we can leverage on and build up.

Typically the hardest part of this business, especially eCommerce, is the last mile delivery side. It's the most expensive one to build and if you have it, you can certainly leverage and build on that and we have that in Australia and Singapore so it makes sense to build on that – that's what we are actually doing in Australia and the investment in Freight Management Holdings is 38% today. It's a good start, we are adopting a rather cautious positioning on this. If the business turns out as well as we believe it should then there's nothing to stop us from developing further our shareholding in FMH. But for now, we are quite satisfied with what we have with them.

Ms Rachael Tan (UBS):

Actually can we take one step back? Maybe can you explain what FMH does to begin with? Because looking at the website, it looks very complex. Not quite sure what it does and how it fits into the business. Maybe that and we can start from that point.

Mr Richard Lai (Group CFO):

Well, let's take a step back then. They are a little bit about a 4PL hybrid sort of a model. So what does that mean? You know of 3PL right? 3PL is typically what we call third part logistics operators – you're familiar with that right? 4PL basically runs a bit like a control tower sort of a business where they move things through different 3PLs based on which one gives the most competitive pricing as well as maybe in terms of volumes and timing that's required to fulfil a particular order. So they are able to do that because they have over time developed a very strong ecosystem around a computer software which they have developed themselves called OneFlo. And with this software they are able to – it's not just a software, it's a whole ecosystem – but it is an ecosystem that's possible because of the software so they are able to pull together all the different 3PL players and to move their products from wherever to whichever place in Australia.

One of the things that they are obviously migrating to is that instead of just doing B2B which is you are brining from one business to another business, they are also looking at what if it was not just bringing from one business to another business – what If you are able to bring it directly to consumers? And that's what they are looking at. Meanwhile for us on the other side, we don't have a strong B2B component yet and we are looking to them to actually provide us with that strength on the B2B and we have the B2C capability. So can you see how the two dovetail in?

Ms Rachael Tan (UBS):

Yes, I see that and I guess for the middle part which is the warehousing and fulfilment, actually it doesn't necessarily need to funnel into your own things right? It's just to wherever the customer wants?

Mr Richard Lai (Group CFO):

That's true. Typically because the 3PLs have their own warehouses so typically they use their own warehouses but the B2B warehouse and the B2C warehouse – the needs and requirements are slightly different because not many are purpose-built for today, so there are subtle differences in terms of height and loading and how many you can stack and that sort of things – there are differences between a B2C capability and one for B2B. In theory you can put the two together but unless you have purpose-built a warehouse for that reason – usually it's not, it's two separate things. You can use a B2B warehouse for B2C just that it's a bit of waste of space because you don't need the height for B2C purpose and you don't need the floor loading so it's a little bit different in terms of scale and size and so forth. But you can put the two together in theory, just to answer that question of yours.

Ms Rachael Tan (UBS):

That's a bit clearer now.

Mr Paul Coutts (Group CEO):

Just to add a couple of things. I think Richard has done an admirable job of explaining the company in terms of the positioning and also what the synergies are for us as an organization and how that fits. But I just want to share a couple of things just to kind of underpin what we are trying to achieve here.

So one is very much about the strategy. Richard mentioned about developing a B2B2C solution and as part of that strategy we believe there's an opportunity to develop a second home market and that second home market being in Australia. Australia is an attractive country. One, it has got high penetration in eCommerce. Secondly, on top of operating as a sovereign country, it operates much in the same way as Singapore does as well which is good in terms of governance and structure. Certainly the one thing that we were very cautious of was the quality of the acquisition, quality of the target. We have done substantial due diligence operationally, financially, et cetera. We do believe that this is a quality asset and using a technology platform to develop the B2B and then potentially bolting onto Consumer solution. The other good news I was going to say was this is an organization that's not new to us, it's not a stranger, it's well-known, we have a long standing relationship with the company mainly because they are a fairly sizeable customer of CouriersPlease in Australia over a long period of time and therefore we have got to know them pretty well. And the last thing I would say is that the other reason why we are confident that we will be able to execute the strategy that we have set out to execute is because we actually have people within the executive team in SingPost also who have relationships and working experiences in the Australian market, particularly in this segment as well so you'll not only get myself, you'll get Vincent, you'll also get Jui-I and a lot of people in the team are very experienced in Australia. So we are confident that it meets our strategic ambitions and it will help us build that key B2B2C business and a second home market but using technology platform at the front-end.

Ms Rachael Tan (UBS):

Ok, maybe one final question. What is the kind of market share that you have and who are the key competitors? Are you able to elaborate a little?

Mr Richard Lai (Group CFO):

Are you talking about FMH?

Ms Rachael Tan (UBS):

Yes.

Mr Richard Lai (Group CFO):

Well, FMH is a unique type of business being in 4PL and there's not many 4PLs in Australia so there are no sizeable or direct comparable peers although in some parts of the business such as the freight business and so forth their competitors would be the likes of Toll, TNT, Australia Post. – these are their peers in that area.

Ms Rachael Tan (UBS):

Thank you, that's all I have.

Mr Jason Lim (Head, Corporate Planning & Investor Relations):

Thanks Rachael, maybe we can move on to the next question.

Operator:

Your next question comes from the line of Ahmad Maghfur Usman from Nomura. Please ask your question.

Mr Ahmad Maghfur Usman (Nomura):

Hi, I just want to ask on the conveyance costs for the airfreight side. I reckon you weren't able to pass on these costs to the customers?

Mr Vincent Phang (CEO, Postal Services and Singapore):

Hi Ahmad, this is Vincent. So that's your question right? Not sure if you have any more to it, your question on conveyance costs and whether we were able to pass it on to customers. So, it's difficult to, we do our best as much as we can. From a mail product standpoint, you understand how the mail supply chain actually works. Our mail product actually is carried on mostly passenger fleets, the bellies of passenger aircraft and when that traffic evaporated it posed significant challenges to us on two fronts. The first is even if we want to pay for it we couldn't get a flight because there's just one end and we had a significant backlog that started to build in Singapore. It was never meant to be an operation that was done that way, it was always immediate – transhipment came in, we processed it and it went out – it ended up sitting with us for weeks until we could get flights. The other issue is of course, capacity being so limited it led to a lot of surcharges and during the first part when COVID-19 hit, there was significant capacity that was in the Singapore term "choped" by all these healthcare players. They were shipping out the essential masks and stuff like that around and it made a very difficult thing for us to do. And while we've had a bit of success passing on some of these charges to our customers, we have a bit of success getting some bilateral work in to ensure that we come in as cost neutral as possible, the fact is, it was always going to be hard.

So on the balance of things, the answer is we did our best to do what we can but the cost was predominantly unable to be passed on and we had to soak up most of that just to make sure that the stuff we had continued to flow and we continued to have this business. Happy to report that the revenues are – you can see that the revenues are strong, the demand is there, there is an expectation that Singapore tries to get the air hub working again or if not some kind of alternative to ensure that this traffic continues to flow and we want to be in the game. We are making sure that we stay in the game, that we are represented in this market but the current cost structure for airfreight through Changi is a continued concern for us, at least it's a continued challenge for us at this moment. Hopefully that gives you some information.

Mr Ahmad Maghfur Usman (Nomura):

Thanks for the clarification. So because I also look at Pos Malaysia in Malaysia here, and what they are doing is they are pretty much ceasing international operations entirely and if you were to opt for that option, what would be the consequences in the future business? Would it be easy to gain back that market share if you restart the business again? I mean, if you have that example of what Pos Malaysia is doing.

Mr Vincent Phang (CEO, Postal Services and Singapore):

That's great that you brought it up, I think that's a very good highlight. Our strategic choice is to continue to be represented in this market. I think that we are just about able to do it at a price point, at a volume level, at a service level that continues to have us represented. It's very, very tough as we mentioned through the brief. The operation conditions are the toughest we have ever seen but we believe that the right way us as a company is to continue to stay represented in this supply chain, and we need to ensure that we continue to serve and be relevant to the 200 territories within the postal union that we continue to serve our customers. I don't think it's viable for us to cease the business altogether and the fortunes – as Richard and I have touched on in the presentation, our fortunes are in a way tied to the fortunes of the air hub status in Singapore and we know that there are concerted attempts by the government to ensure this is supported, this continues to be driven, we've got all those investments in the new terminal, we continue to want to drive this trajectory of Changi being relevant. So we believe our journey is tied to that so we will continue to make sure that we are represented, we will continue to make sure that the customers believe that this supply chain is viable and we believe that at some point in time, the traffic will return and things will stabilize.

Now, whether there is a permanent impact to the changes remains to be seen, but if we choose not to be represented in this it's extremely difficult to come back again because the supply chains will be diverted away from Singapore, away from Changi, away from SingPost and that makes it a bit more difficult so be patient with us as we navigate this. I guess it's important, be patient with us knowing that the operating circumstances are stacked against us. What used to be a very big advantage, Changi's perspective, Singapore's perspective, SingPost's perspective, has turned out to be very challenging at the moment. But we believe that the right thing to do is to stay engaged.

Mr Ahmad Maghfur Usman (Nomura):

Alright, that's all the questions I have. Thank you so much.

Mr Vincent Phang (CEO, Postal Services and Singapore):

Thank you so much.

Operator:

Your next question comes from the line of Low Horng Han from CLSA. Please ask your question.

Mr Low Horng Han (CLSA):

Hi, morning everyone. Thank you for this presentation. I have just this one question here for the Domestic Post & Parcel, the eCommerce segment. Can we try to understand the margins that you are getting for eCommerce side?

Mr Vincent Phang (CEO, Postal Services and Singapore):

Yes. Hi Horng Han, thanks for the question. So your question is about the eCommerce – domestically right? Domestic eCommerce margins correct?

Mr Low Horng Han (CLSA):

Yes, that's right.

Mr Vincent Phang (CEO, Postal Services and Singapore):

So the domestic business is – you know that we run a huge flagship operation called the postal service and with the postal service we reach every home, every postal code every day and as an Essential Service we continue to provide that as much as we can through all those disruptions. So the eCommerce business that we have, we see it in two parts. There's a big part of it that's tied in with the postal service so as you are aware, items that are small enough that can make it into a letterbox make it into – over the last few months, we've actually worked with customers, worked with the regulators that any tracked item like your registered item actually is being delivered into the letterbox instead for a contactless delivery so that's also a directional trend that we are starting to see.

So I think that's worked very favourably for us. We also have a more traditional eCommerce doorstep service which is our Speedpost service which is more in line with everyone else in the market. So there are various aspects, there are various elements of products that we have. Clearly, those margins are different so from a blended basis those margins are improving. I can't give exact numbers but those numbers are improving, we are starting to see – you saw from the presentation deck – 33% of our domestic revenues are made up of eCommerce-related shipments and accelerating. There is density impact, that density effect, there are those synergies of putting things that way, and we are also seeing predominant or some market behaviour behind customers making more discreet purchases. So rather than wait for amassing a big basket of items which then needs to be sent to the doorstep, customers are now more motivated perhaps in the sign of the times. There may be some directional moves here as well that they purchase singularly. If I need a pair of socks, if I need a T shirt I will just buy it and those can benefit us in a way of putting those items into infrastructure like

POPStations or letterboxes. So margins are different, the margins are all improving and that's the colour I can provide you.

Mr Low Horng Han (CLSA):

No. Ok I am thinking along this line because your cost structure for the postal network has been fixed, maybe you might have been trimming a little bit in terms of headcount or even growing because of the salary increment that you gave about a year ago. So you have a fixed cost structure and leveraging on this cost structure to do eCommerce, I would have thought that eCommerce perhaps could give you quite a little bit of positive operating leverage giving that the similar postman – he or she can do eCommerce and traditional post and parcel as well – is that how we should look at it going forward? That the room for margin expansion with higher volumes in eCommerce leveraging on the similar fixed cost structure network can give you that sort of uplift in margins?

Mr Vincent Phang (CEO, Postal Services and Singapore):

Absolutely, that's all I can say. Maybe Richard would like to add a few more points after I cover this off. Yes, you are right, operating leverage is a fantastic advantage to us but I think we have to be careful about this.

First of all, this is an Essential Service and anything that's essential that can make its way through this supply chain is our way of serving the country and that continues to be our mandate. The operating leverage is true, having been designated the Essential Service gives us the advantage within the market of being represented – like I said, every post code everyday but we have to make it work in our favour. That is actually going forward the basis of this Future Of Post project that maybe not from today, but as you start to see more of those revelations of what we are trying to put across to the market is built on this foundation – the foundation that operating leverage is the advantage for us, how do we continue to maximize margins as a result of this, how do we replace the rate of decline for letters. So while we say it's sunset, what other advantages that affords us and how do we carry this into the future.

I think we are connected in a way, without giving you too much of a quantitative explanation, qualitatively yes, directionally definitely the way to go and this is what we are working on.

Mr Richard Lai (Group CFO):

Horng Han, I think what Vincent is trying to say has been skirting around a particular issue we call the Future of Post. I think if you think about it, a lot of times people don't actually realize this – quite a fair bit of eCommerce volumes that come into Singapore in particular are actually being fulfilled by us into the mailbox and in particular for the low value items postal is still the cheapest way to go about doing it. The major constraint for us has been the size of our mailbox so obviously that is something that while we have operating leverage off, the fact that our postman does his beat, we have our sortation facility and things like that, ultimately it is still your mailbox that acts as a physical constraint and therefore that's why it's necessary for us to look into the possibility of reshaping how that particular element is holding up its constraint for us. If we could resolve that issue and we have plans on that, then you are right, it will open up a whole, entire new opportunity for us. So the long and short of it – you are right, operating leverage that we can certainly benefit off and the margins on that should be pretty decent. In fact, I would dare say that it is pretty decent even as it stands. It's just that it's currently being discoloured by or tainted by the fact that Domestic letter mail volumes continue to decline, so most of you guys are often seeing that side of the picture and not seeing the other side of the picture which should improve from volumes. So not entirely you guys' fault, we haven't gotten all the data points in order to decipher it as clearly as we would like to but certainly something we are planning to do in the coming months is to distil the information and make that a bit clearer as to which part of the business is the sunset side of it and how that is being replaced by the eCommerce side of things.

Mr Low Horng Han (CLSA):

Alright, just two more from me. Second last question is – are your competitors in this space loss making?

Mr Vincent Phang (CEO, Postal Services and Singapore):

I think the tricky answer is you have to ask the competitors, we can't answer that. But what I can say is, if you allow me, urban setting like Singapore – it makes absolutely no sense to be moving stuff to the door, it's going to be very labour intensive, it doesn't work to any of the metrics you think about. In terms of sustainability angle, we've got numbers to show that fleet will grow and fleet will actually outstrip growth of eCommerce for some strange reason. So the more you deliver, the more fleet you need and the more people you need and it will just end up becoming a truly, truly unsustainable situation.

So I'll give an anecdotal, qualitative indication of what it means to us. it takes six seconds on average to deliver something to a letterbox and if you take an urban high-rise Singapore context, we don't actually deliver to every single home – we deliver to the void deck, HDB or to a letterbox infrastructure at the bottom of a high-rise apartment – you reach one point, you reach a hundred homes right? So six seconds to a letterbox, six minutes to the door. You got to take the lift, you got to knock on the door, ring the doorbell and then there's this added directional shift towards contactless delivery. If you have been purchasing on eCommerce sites recently, you also realize that a lot of players start to offer this thing called contactless delivery; you don't actually open the door, you don't actually meet face to face and you find a way to securely deposit the item and make a delivery count. So in a sense, infrastructure is the way to go.

If we continue to price things in the way we are pricing in the industry, it doesn't take a lot to figure out that going to the door – even the best amongst us will find it very stretched to make any margin out of it. So I can't comment on how our competitors do – maybe they make a margin, maybe they don't – but what I can say is as you move forward, such things cannot be sustained. You can't possibly have more people, you can't possibly have more fleet and it's just we've got a van driving around delivering items is not the way we see it developing in Singapore so our direction is very clear as Richard mentioned. Our Future of Post direction is very clear, operating leverage counts on that, infrastructure counts on that. Make sure that we continue to leverage this, don't let it turn into a disadvantage. We actually now serve the country using letterboxes and in time to come we actually end up serving the country going to the doorstep – that doesn't make any sense at all. So hopefully that gives you some qualitative directional information.

Mr Paul Coutts (Group CEO):

It's Paul here, maybe just let me add a couple of points to what Vincent said. Vincent has given a lot of information there so that's great but there are also a couple of other things that I think may be worthwhile for you to start thinking about.

It will be true to say that in terms of eCommerce in particular, it's obviously been a boom for a lot of companies in the logistics business. So if you look at some of the companies who are benefiting from an eCommerce boom on the logistics side and also if you look at the integrators, it would be a good example of where that's definitely value accretive for them on an end-to-end supply chain, and you can see that from the results and they have talked about that publicly. So now I'm obviously talking about the DHL, the FedEx, and the UPS of the world.

At the same time however, even for those companies, they struggle with the last mile delivery piece of it. They make money off of all the transactions but in the last mile delivery piece it's probably not profitable if you look to that as a standalone element. But it's a bundled price so they are able to offset it. We have been pretty clear in terms of our strategic play in eCommerce, it has been consistent in the last few years. That is, there is a lot of volume out there that we can go after, there are certainly some of our competitors who have gone after volume with the primary goal of just getting market share and their idea is they get to a certain size and scale and then they get the economies and then they become profitable. But very, very few of those competitors have actually proved that that model works, that they are able to execute and get to profitability and we are very cautious about making sure that anything that we handle has to be value accretive for our organization, has to be value accretive for our shareholders as well, and that's where our key focus is.

So therefore when Vincent talked about creating the right infrastructure and executing the strategy of the Future of Post, it's built primarily with that purpose. It's got to make sure it's going to drive eCommerce volumes through the organization, we are going to gain market share through it. More importantly, it's value accretive for the business.

Mr Low Horng Han (CLSA):

Sure. Thanks so much, Paul. Now that you mentioned market share, what was SingPost's Domestic Post & Parcel eCommerce market share say, three years ago? Or two years back? If you do have any data on this.

Mr Paul Coutts (Group CEO):

Yes, so we estimated back then in terms of the eCommerce Post & Parcel we had roughly about a 20% market share. We felt that we weren't doing ourselves justice; we felt that we repositioned ourselves within the domestic environment and became more aggressive in some areas and make sure that we have the right infrastructure in place to handle the additional volumes and market share. But also that we can leverage off the market share we had, that we could grow our market share in a profitable way so we've expanded our market share so even just before pre-COVID, we had moved from 20% to roughly about 40% plus in terms of market share. We continue to do well, obviously Vincent has talked about that eCommerce has continued to expand in our business and I think we've done well in terms of increasing our market share in an increasingly competitive environment. So we are seeing the benefits of that.

Mr Low Horng Han (CLSA):

Thank you so much. Thanks for the clarity, Paul.

Operator:

Your next question comes from the line of Terry Ho from One Hill Capital. Please ask your question.

Mr Terry Ho (One Hill Capital):

Hi, good morning, Happy to hear that everyone is doing well. Conscious of time, so I just have one quick question. But before that, just want to thank management for the increased disclosure, really appreciate the increased visibility into the different businesses. So my question for the day really is just to ask about an update on the new pricing structure that was announced in September, and should have started in mid-October. So on that front is it possible to just share has there been any notable shifts in how services are consumed? And in particular, has there been any change in how the eCommerce platforms are consuming? Because on that end it's just that I noticed that with this update in pricing you are now priced more attractively than your competitors. Thanks.

Mr Vincent Phang (CEO, Postal Services and Singapore):

Thanks Terry and appreciate the feedback on what you talked about our increased disclosures. For pricing it's a bit early to say because you know that it was only launched 15 October and it took time to work through all the – it sounds easy, it's a rate change but there are a lot of back-end processes, and all the integrations with customers, with institutional customers. That took some time to get through so it remains to be seen, but how we got there was because of the feedback; we've been having some intense discussions with some of our largest customers, we also have been driving focus groups with consumers like those people at home, residents who receive things so we also can't ignore the fact that we also have a big C2C type of relationship so we've got to take care of small sellers, SMEs. You can't please everybody, but for the most part I think we did what we needed to do and we are moving things the right way.

The key principle behind the rate change is it's a lot more streamlined, there's a lot less breaks and that has been very deliberate. We wanted to clean it up. Will there be more? I think there will be more. We need to make things easy for customers to understand. Unfortunately, you also maybe – if I can put a word through, it's not so simple when it comes to a UPU environment because there are a lot of legacy systems and interactions with postal peers across the region so it takes time to try to move some of these things but we are very deliberate in streamlining to make it more cost effective, for customers to also make it more sensible, easy to select us. It's like you go to a restaurant and they give you a menu that has 15 pages. You will take forever to choose a dish, you might even leave the restaurant altogether so you want to make it very clear it's a fundamental service that you can procure.

What does that do to margin? We do believe that there is some headroom so in the long term we believe that we would want to move all our products or the majority of our products to a service level that is in line with customer expectations; customers expect trackability for eCommerce items. They may not expect that for letters but they certainly expect that for eCommerce items. But the postal service provides that at a cost that is low, attractive but doesn't provide that customer experience of trackability and hence, there is a bit of a gap and we are probably the only one that provides a nontracked option because of the fundamental mail service so we are narrowing that gap. In that sense, we are trying to see what we can provide on a very cost effective basis but at the same time understand that customers want trackability. So these are the steps that are continuously driven, it's in discussions with our major customers. They are obviously very positive about what we are doing and as we move along with these rate changes, simplifying the tariffs, you'll see that from an operating performance standpoint and also from a financial standpoint that that should continue to move the right way. Terry, is that what you wanted to get out of or is there something else that you wanted?

Mr Terry Ho (One Hill Capital):

I think this works as well. Anyway, it has only been two weeks since it was implemented.

Mr Vincent Phang (CEO, Postal Services and Singapore):

Maybe at the next update, the results can be a bit more obvious.

Mr Terry Ho (One Hill Capital):

Thanks.

Operator:

Your next question comes from the line of Varun Ahuja from Credit Suisse. Please ask your question.

Mr Varun Ahuja (Credit Suisse):

Hi, thanks for taking my question and I am pretty much cognizant of the fact that we don't have much time so just two questions. First on this International mail business, it has been almost four, five years since it has been there in the company, maybe a little bit longer but still continues to be challenging – sometimes when the cost increases happen in the International mail side you were not able to pass on and obviously COVID-19 is expected – and if I look at medium to long term, though the revenues have been growing the margin profile doesn't seem to be improving at all. So when do you think you will be to reach a stage wherein you can attain decent profit margin on that part of the business? Because revenue contribution is more but the margin I think is rather weak, obviously the pandemic has played a role but it hasn't shown much on the numbers.

That is number one and number two on the Domestic mail side, Richard, I heard you comment but I just wanted some clarification on that. Assuming you just do eCommerce delivery on the postal segment which I assume currently is a large part of it, your margins should be similar to the revenue being replaced by the eCommerce – mail has been replaced by eCommerce right? As long as the pricing would have been similar, it's more about a function of pricing and obviously if you don't do doorstep assuming the pricing is similar. So it's largely a function of pricing improvement or is it about some cost elements that we are missing? Thank you.

Mr Richard Lai (Group CFO):

Thank you, Varun. Let me try and address the question this way. I think if you were to remember a couple of years back there were some businesses that obviously took a big chunk of our profitability. Have we not gotten out of that, there would have been another S$50 million taken out of our numbers. That was just how big that it was not so long ago. The unfortunate part of COVID-19 is of course that it led to major disruptions, major costs have been incurred because of that. We estimate that it can come to a scale of nearly S$50 million in a year. If you add back the S$50 million to how we have been performing or half of that – S$25 million for the first half – you'll find that we would have performed better than last year. Unfortunately, it is what it is.

So your question is when will things get better? Logistics have improved as you would have seen and certainly a big chunk of the International Post & Parcel business is gone; we have the revenue, we no longer have the profitability on that. So would that return? We certainly think that at least the bulk of that should return, although we are under no illusion that when business returns it might be in different shapes and sizes and form. But we certainly are keeping our burners on because we believe that it will return. The Singapore government is doing all it can to try and increase the utilization of Changi and so forth so I am quite certain that it's a matter of time before we could get things going again. And not to just rely purely on Singapore government to do that, we are also trying to set up our own mini nodes in different parts of the world so that we could then deploy an ecosystem of continuing with our international business, so there are different plans and different things we are doing in respect to that.

To the question of whether or not if you do the same amount of revenue for eCommerce – whether you have the same amount of profitability as mail, the answer is no, you won't. The mail business obviously, if I were to consider the same volume taken up by letters, the same volume of letters compared to phone cases for example, the revenue you would get from that volume of letters as compared to phone cases will be more than what we would get from a phone case being delivered so you are right to some extent. It's a function of what you charge but it is also a reflection of the fact that the postal infrastructure is the cheapest way for them to move a lot of these low cost items throughout the world. And for that reason we have to recognize that unlike letters where in the past it was purely monopolistic in a sense, where the rates are all determined by the government and so forth, when it comes to eCommerce elements, there's less of that. I say less because there are still some parts of it that still has some of these elements, especially the very small ones. But it's a lot less of that so you are exposed more to the competitive nature internationally as well and that does eventually put a certain limit to what you can charge for some of these items. So it's not like you could just unabatedly charge whatever you want for it. There is still a demand and supply that we need to respect at the end of the day.

So in the long and short of it, for the same volumetric that you get for an eCommerce item, for that same space, it will not be as high of a margin as what a letter would have been and quite simply because the letter is a lot smaller and therefore the margin included in that has traditionally been a lot higher. In the past, at one time, letter margins could be as high as 30%, 40% right? In fact, it used to be at one time even higher but in our recent past it has been 30%, 40%. You can't get that for eCommerce; it would be lower than that. We ought to still be able to make decent margins even with the Future of Post when we roll that out, removing some of the postal infrastructure constraints that we currently have. We should still be able to make a decent margin out of it but it would be nowhere close to the margin that we used to make on letters. Hopefully that answers your questions.

Mr Vincent Phang (CEO, Postal Services and Singapore):

Maybe I just add on a couple more points to what Richard said. Richard covered most of it Varun, but maybe just to clarify a couple of points he made as well. I will talk about the Domestic Post & Parcel first. You do know that we still move despite the decline, we still move a lot more letters versus eCommerce items, the ratio is still something along the lines of 8:1 or 10:1 so that ratio will change through time and that ratio isn't the same as revenue. Revenue is one-third or 3:1 or 2:1 but it's not the same as the actual number of items that we ship. That's because the price of a letter is on average measured in S$0.30 to S$0.60 but the price of an eCommerce item is probably S$1.00 or S$2.00 kind of price point. So yes, it's a lot more complex than that. We have to rethink some of the cost elements because moving things that are bigger items will require bigger fleets, motorcycles, we have to change the back-end processing machines, we have a quite a few things that we are doing which we are trying to architect behind the scenes so there is a reset of margin expectations and what not. But if you think about it, the actual revenue per item for eCommerce is a lot higher than revenue per letter so with the change in the profile, at some point in time if you work through the math you will realize over the next couple of years there will be a switch in our time. So it requires density, it requires volumes and it requires that ratio to tip over and then you will see the contribution coming from eCommerce to be really, really significant. And then couple that with the operating leverage that we talked about, it's a major reset to the way we do things. At the moment, on an aggregate basis the margins may not look that positive but if you think about when the density comes through, that is really going to be moving the needle very significantly and that's how we should look at the domestic margins.

As for the International mail margins, I thought that I heard you say that you had the impression that the International margins were low. Maybe I can correct that – it's not, it hasn't been low. The revenue has been growing. Yes, we've had challenges with terminal dues which is an on-going thing, the revenues remain strong and the dollars from an earnings standpoint remains strong till COVID-19, so back to Richard's point – it remains to be seen when and how that comes back but we are making plans to ensure that when the day comes again we are able to get back on track with that kind of supply chain and the costs are manageable, we will be back to the same profitability level. So I just hope you don't go away thinking that the International business is a very low margin business; it's not.

Mr Varun Ahuja (Credit Suisse):

No, this is helpful. Where I am coming from is if you look at previous two, three years' earnings, the commentary was International was mid to high single digit margins compared to obviously, you mentioned Domestic at that time of the past, so postal was a lot higher around 20%, 25%, 30% kind of a range. So that was where I was coming at. Just a clarification Richard, you mentioned the cost was S$50 million due to COVID-19 and if you add back that cost, the profit would have been higher – is that what you said? Just a clarification on that.

Mr Richard Lai (Group CFO):

Yes, so Varun, just to give you some colour and this is purely based on estimation, we do reckon that the COVID-19 impact will amount to about S$50 million in a year so in half a year it's about S$25 million. So when you add that back to the numbers, obviously you'll come to the conclusion that we would have performed better but it is what it is.

Mr Varun Ahuja (Credit Suisse):

Got you. Did COVID-19 help you charge higher for your clients from Alibaba and AliExpress?

Mr Richard Lai (Group CFO):

No, I think it's not like we are able to charge everything higher. Just now I think Vincent has mentioned that a big part of the transhipment business in our International Post & Parcel business – you take orders, the goods arrive here and then Changi closes and then you are duty bound to get the items to the end point in other parts of the world – You are duty bound and therefore it's for us to find ways in moving that. You charter planes, you pay higher conveyance costs and we can't just turn around and say we want to charge you higher because of that. Yes, we could argue in some cases whether it was force majeure but I think in the parts of doing business, these are some of the things that you run that sort of risk. So I think there needs to be that understanding that even if you are the only one that's able to charge higher price, it does not happen overnight; it takes a bit of time to be able to do that and unfortunately for us, we've been hit double whammy in this first half of the year.

We had eCommerce growth, huge volume growth, but at the same time we have issues in moving some of these – a lot of it are the International Post & Parcel side – we had problem moving them out of Changi and so we had to pay a lot of money to move that because we are duty bound to do that contractually and so forth. The ones that do come into Singapore are less of an issue, but the ones that we have to move away from Singapore – that becomes more of an issue. So that's the thing about being a diversified business, you could say that had we not had that International Post & Parcel business, we would have been a lot more profitable but International Post & Parcel last year was a key profit contributor for the whole year.

So you got to take it good and bad times, it's not like they are costing us an arm and a leg for now. It did erode all of the profitability but it's not at the same time costing a massive loss like what the U.S used to be doing to us. So I think one has to see it from that perspective. Now, as things evolve and things move on, we have a new norm and with the new norm then things get adjusted along the way and I think that's where we are coming to. What we are saying is that we got to learn to live with the new norm, and as we learn to live with the new norm we will adapt in time to come, but a lot of these things – nobody would have ever dreamed of Changi being closed and when China was closed we were open, when China was open we were closed. So who would have imagined that sort of timing? Nobody would have imagined that magnitude of impact that it has had on the world. So the fact that we still make half that amount of profit that we made last year demonstrates a certain high degree of resilience in the business.

Mr Paul Coutts (Group CEO):

I was just going to add that – Richard, I think that's great – the one thing I would add for everybody's benefit as well is that I think one of the things that we are seeing within SingPost, particularly with all the challenges that have emerged through COVID-19 – we have had to adapt very, very quickly to very, very challenging circumstances. We won't go into all of that again. Every other business has had to do the same and so at the same time I have to say as the Group CEO of the company I am absolutely delighted with the way our organization has not only reacted to the challenges, but actually has picked up the challenges and attacked them full-on, and adapted very, very quickly to a completely and obviously a very different and increasingly challenging environment.

We are not through it yet, it's important to stress that. We are obviously still going to have some impact in COVID-19 but I am confident that we will continue adapt and continue to show the agility that we have shown and I think it's a remarkable commendation to everybody that worked for the organization, but particularly for our front-line troops that are there every day satisfying our customers. Just want to put that on record.

Mr Varun Ahuja (Credit Suisse):

Thank you very much for the detailed answer, very helpful.

Mr Jason Lim (Head, Corporate Planning & Investor Relations):

Varun, maybe let me just jump in on a bit of clarification with regards to the margins for International business. I think you mentioned something like low single digit margin for International Post & Parcel. Let me just give a bit of background. When we disclosed a couple of years ago, three years ago, when we were doing 30% odd margins for the overall postal business right, what we said was International was about one-third of Domestic. At the point in time, Domestic was probably in the 40%s so we start to give colour that International was around one-third of that. And if you look at it, the way we look at International is that it is lower margins relative to Domestic but if you pull International business across to any logistics business which is you are right – typically mid-single digit sort of margins – you can consider International Post & Parcel a high margin logistics business. I mean the way it is operating, the margins that we have there would be a very, very good logistics business in that sense. So that is the way the margin profile broadly looks like on a normalized basis before COVID-19 and all of that.

Mr Varun Ahuja (Credit Suisse):

Got it.

Mr Jason Lim (Head, Corporate Planning & Investor Relations):

We can do further clarifications if needed. I think we have extended the call by 20 minutes, I think that's all the time we have. Thank you all for dialling in and you know you can reach out to me if you have any other questions. Take care, stay safe.

Mr Paul Coutts (Group CEO):

Stay safe.

Mr Richard Lai (Group CFO):

Thank you.

Mr Vincent Phang (CEO, Postal Services and Singapore):

Thank you.

End of transcript