SingPost's Q1 FY18/19 Results Analyst Briefing, 3 August 2018

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 (Vice President, Investor Relations):

Good morning. Welcome to SingPost's results briefing for the first quarter of FY2018/19. I am Jason from Investor Relations. With me today is our Group CEO Mr Paul Coutts, as well as our Deputy GCEO (Corporate Services) and Group CFO Mr Mervyn Lim.

I'll now hand over the session to Mervyn.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Good morning and welcome to our results briefing. Let me first share some highlights of our Q1 results. Revenue rose 3.3%, driven by eCommerce-related activities. We recorded strong free cash flow, up 93.9% year-on-year. Operating profit before exceptional items rose 1.2% year-on-year. On a quarter-on-quarter basis, it rose 22.5% against Q4. Underlying net profit was lower by 9.8%. On a quarter-on-quarter basis, it rose 60.4% against Q4.

We shall now move on to the P&L statement. Revenue rose 3.3%, driven by International mail and Property. In Q1, the Group recorded an exceptional loss of S$6.0 million due mainly to fair value loss on warrants from an associated company, compared to an exceptional gain of S$4.0 million last year due mainly to fair value gain of the same warrants. Income tax expense rose 38.8% to S$11.6 million largely due to an additional tax provision for a foreign subsidiary. Consequently, reported net profit declined 40.4%. Excluding exceptional items, underlying net profit declined 9.8% as the improved operating profit before exceptional items was offset by lower associates' contribution and higher taxes.

Total expenses increased 2.7% in Q1, lower than revenue growth of 3.3%. The higher expenses were largely due to the increase in volume-related expenses, as the Group seeks to grow eCommerce volumes to benefit from economies of scale from operating leverage. Volume-related expenses remain the largest cost component for the Group, and rose 6.2% in Q1 due largely to higher International mail terminal dues. Labour and related expenses declined by 5.5% on cost management initiatives. Administrative and other expenses rose 10.7%, largely due to higher insurance and property tax expenses.

Let me share some highlights for the quarter. We have made significant progress in Winning in our home market. Parcel sorting utilisation at the Logistics Hub was 24% for the quarter ended 30 June 2018, up from 16% last year. Average volumes sorted per day were up 47% year-on-year.

With respect to Extracting full value from investments, Quantium Solutions delivered a good turnaround, as we narrowed losses by 45% compared to last year. We are reshaping the QS business,

enhancing capabilities and capacity, to better serve eCommerce businesses. This was aided by new customers wins, including our contract with Specialized bicycles for an end-to-end Southeast Asian logistics and warehousing solution.

Under our Drive to cost leadership initiative, we have reduced costs for non-volume related expenses by 2.2%.

Our eCommerce related revenues continue to grow. For Q1, eCommerce-related revenue rose 8.8% year-on-year, driven by higher eCommerce deliveries across our network, such as cross-border mail, as well as Singapore parcel deliveries. eCommerce-related revenues now represents 53.7% of total Group revenue.

Let me now move on to the Cash flow and Balance sheet. Net cash inflow from operating activities for the quarter ended 30 June 2018 rose to S$71.3 million, from S$58.4 million in the same period last year. With the completion of the SingPost Centre retail mall redevelopment, capital expenditure declined to S$9.2 million for the quarter, compared to S$26.4 million in the corresponding period last year. As such, free cash flow improved significantly to S$62.1 million.

We now move to the balance sheet and financial indicators. Our cash and cash equivalents stood at S$377.6 million as at 30 June 2018, compared to S$314.1 million as at 31 March 2018. This was largely contributed by cash from operations. Total borrowings rose marginally from S$244.0 million as at 31 March 2018 to S$248.2 million as at 30 June 2018. The group was in a net cash position of S$129.4 million as at 30 June 2018. EBITDA excluding exceptional items was S$50.1 million for Q1 FY18/19. Our interest coverage ratio remains strong at 21.1 times.

We will now move on to the segmental results. From 1 April 2018, SingPost has reclassified the reporting of certain business units into 4 key business segments, namely Post and Parcel, Logistics, eCommerce and Property.

Post and Parcel segment comprises the core Postal and Singapore Parcel delivery business of the Group. This includes Domestic mail, International mail, vPost, products and services transacted at the Post Offices, as well as the Singapore Parcel delivery business SP Parcels.

Logistics segment comprises the Logistics businesses of the Group. This includes Quantium Solutions, Couriers Please and Famous Holdings.

The comparative period last year had included SP Parcels, General Storage Company and other logistics businesses, which have accordingly been reclassified.

eCommerce segment comprises the front-end related eCommerce businesses. This includes SP eCommerce in Asia Pacific, as well as our US eCommerce businesses.

Property segment includes commercial property rental, as well as the self-storage business of General Storage Company.

This slide provides an overview of the various segments' contribution to Group revenue and operating profit performance for the quarter. The Post and Parcel segment remains the largest contributor to group operating revenue, followed by the Logistics and eCommerce segments. Property revenue consists of commercial rental and self-storage revenue from GSC.

Post and Parcel is the largest contributor to Operating profit at S$41.8 million, followed by the Property segment at S$13.2 million. The Logistics segment reported a positive contribution of S$0.1 million for Q1, compared to a S$2.5 million loss last year. Next, we will take a closer look at each of the segments.

In the Post and Parcel segment, International mail and SP Parcels revenue rose due to higher eCommerce deliveries for both cross-border and domestic Singapore respectively. This helped offset the impact of lower domestic letter mail volumes. For International mail, the Group had implemented measures which helped mitigate the adverse impact of higher terminal dues. However, margins were lower compared to last year. Consequently, Post and Parcel operating profit declined 3.8%.

In the Logistics segment, revenue declined 2.2% in Q1, largely due to lower volumes recorded in the freight forwarding business. The Logistics segment registered operating profit of S$0.1 million compared to operating losses of S$2.5 million last year, due largely to the turnaround in Quantium Solutions, which narrowed its losses by 45% compared to the corresponding quarter last year. Earnings contribution from Famous Holdings and Couriers Please also rose.

In the eCommerce segment, revenue declined 4.3% largely due to the US businesses, as pricing pressures resulted in the price per order declining compared to last year. Operating losses rose to S$9.3 million compared to S$4.8 million in the prior year. This was largely due to the US Businesses, which experienced pricing pressures, as well as a change in sales mix with a decline in fulfillment revenue with higher gross margins, and growth in freight revenue which had a significantly lower gross margin. Further, there was an increase in technical labour cost to support business integration efforts.

This chart shows the impact of various segments on underlying net profit. Contributions from the Property and Logistics segments rose. However, these were offset by a decline in eCommerce, Post & Parcel. We also incurred higher taxes due to an additional provision for a foreign subsidiary. As a result, underlying net profit for the quarter declined 9.8%.

Let me now move on to a Summary of our results. In Q1, revenue rose 3.3%, driven by International mail and Property. Net profit was down 40.4% due largely to exceptional fair value losses from warrants in an associated company. Excluding exceptional items, underlying net profit declined 9.8% as the improved operating profit performance before exceptional items was offset by lower associates' contribution and higher taxes. Free cash flow improved to S$62.1 million with lower capital expenditure, while net cash position improved to S$129.4 million as at 30 June 2018. The Board has declared an interim dividend of 0.5 cent per share.

With that, I conclude my presentation. Thank you, I will hand you back to Jason.

Mr Jason Lim (Vice President, Investor Relations):

Thank you, Mervyn. We are now ready for the Q&A session, operator please start the session.

Operator:

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. Your first question comes from the line of Sachin Mittal from DBS. Please ask your question.

Mr Sachin Mittal (DBS):

Good morning and thanks for the opportunity. Just two questions; firstly on the turnaround of the U.S operations in the eCommerce segment, it seems to be going in the reverse direction rather than in the right direction and you have pointed out all those pricing pressures and different margin mix. So what I am trying to understand is – what are the levers in terms of trends going forward? Because those issues are not going to go away anytime soon and what happened in the last one or two quarters suddenly that caused such a drastic change? That's question number one, why couldn't you see it one, two quarters back and seeing it now?

Secondly, when I look at the eCommerce-related revenue it's only 9% growth year-on-year; last quarter was 27% growth so is it something to do with the accounting change or it's pointing out something else? Thank you.

Mr Paul Coutts (Group CEO):

Sachin, hi it's Paul here and thanks for the questions. The U.S situation – let me address that first and foremost. So yes, you're right. We have talked about the fact that we have obviously got a turnaround plan and also that we have been on track with that turnaround plan, and even Q4 FY2017/18 we were actually still on track with the turnaround plan. Q1 – when you look at the numbers for Q1 so let me just talk about that specifically for a minute. April and May we were still on track with the turnaround plan, also that period was kind of a low season period but we have certainly experienced in June – so April and May on track, in June the volumes that we experienced were certainly lower than we expected. This is a scale business with a fixed infrastructure in place so when your volumes get to a lower level then obviously that will have an impact in terms of your profitability. So we saw a lower than expected volumes and that had an implication for us.

Also, the product mix was certainly an issue as well where we saw a lot more of the volumes that we did have – a lot less of that were going through what we call pick and pack operations which is quite a high margin business, and a lot more were going through the freight business and that freight business tends to be lower margin in nature.

In addition we had integration costs which we have talked about where we are integrating the businesses there, and the integration costs obviously have an influencing factor and we expect to get the synergy benefits from those integration costs in time as well. But we did have some of those costs in there.

I think the other thing I would say in terms of the U.S losses while we are talking about it – some of the influencing factors where we obviously made a public announcement last year in our full year results that we have lost two customers which made up about 40% of the business there. We still had one of the customers in Q1 FY2017/18 and obviously not this year and while we have won a lot of new customers in between which has helped us progress we also still had to rebuild some of that into Q1.

We will continue to invest as well, ahead of growth in the U.S and that includes more automation and also this year we have introduced and invested in robotics in the warehouse – that's going to help us in the peak season coming up and that's obviously an investment that we are making to reduce dependency on labour in a high labour cost market, it's also going to improve our service performance, productivity and efficiency in the U.S business.

So we were still largely on track in April and May; June was off in terms of the volumes in particular and we also had a customer programme scheduled for June which was deferred by a couple of months and that was a bit of a contributing factor as well where we were off. Right now we are actively working our way around all of those influencing factors and we are monitoring the volumes going into July and August, and adjust accordingly as we need to.

In terms of eCommerce-related revenues, the biggest influencing factor on the eCommerce piece has been around International mail volumes so in terms of the revenue increase, it still rose 13.0% in Q1 versus – you're right, 39.0% in Q4 FY2017/18 which then have an influence in the overall eCommerce-related revenues. A couple of things there – so we talked about one of the influencing factors around terminal dues and also what influence that may have in terms of growth for the business. We have got a lot of mitigating measures in place to obviously try and make sure that we are reducing the risk for us and I've stressed previously; it's a very confused view, it's a multidimensional view because it's about volume mix, it's about weight mix, it's about geographical mix and product mix. All those are moving pieces within terminal dues environment so the focus is really to be making sure that we are continuing to carry traffic that we believe is profitable, that we can add value for our shareholders, add value for our customers so we are watching the EBIT line and the slowdown in revenue percentage growth is partly an outcome of those influences. So that's one of the key things in the International mail piece which is obviously impacted upon it; it's something that we continue to monitor but the final view is still emerging because of those different components which are there. it's going to take some time to come through and actually for us to be able to establish a trend going forward.

Mr Sachin Mittal (DBS):

Whatever happened in U.S – is it an industry issue or was it a company specific issue for us? You might not have the data but what is your sense on that? One more follow-up question if I may – one more question on cost, what's happening on the cost mitigation measures? By what time frame could these cost mitigation measures show some results if at all?

Mr Paul Coutts (Group CEO):

Sachin, I just want to make sure that I understand your question accurately. When you talk about cost mitigation measures, are you specifically talking about the U.S?

Mr Sachin Mittal (DBS):

I am talking of – you had cost reduction programme in place, redesigning of whole processes.

Mr Paul Coutts (Group CEO):

Sure, so you are talking about the Cost Leadership Programme. In terms of the U.S, whether this is kind of an industry issue, at this point in time as I have said, it's kind of isolated to June so a bit early to be able to forecast and to be able to say accurately whether this is an industry issue, whether this is just sort of a customer – in terms of those programmes that I mentioned earlier, they are having a bit of a catch up with the business that we lost last year. So this year our focus is really on seeing how July is going to look like, what is August going to look like. In the meantime, we are gathering information obviously in terms of what's happening in the rest of the industry; we have nothing else

at this point. In terms of the Cost Leadership Programme, Mervyn could maybe talk on that – he's got a firm hand on the moving pieces of that programme.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thank you, Paul. Hi Sachin, so basically our Cost Leadership Programme is well in motion; it's on track and you can see the results in fact in two particular indicators within the Q1 results. The first would be in terms of going into our total expense line – very happy that our non volume-related expenses have come down by 2.2%, which shows the kick-in of the Cost Leadership Programme effects. When you go into labour related costs in the expense page, you will see that coming down very nicely by 5.5% which means there is a reduction of S$4.5 million in headcount as part and parcel of our Cost Leadership Programme. So long and short is it's going well on track.

Mr Sachin Mittal (DBS):

OK great, thank you.

Operator:

Your next question comes from the line of Colin Tan from CIMB. Please ask your question.

Mr Colin Tan (CIMB):

Hi, thanks for the opportunity. I have three questions, first one on the postal business. Margins have come down to 22.5%, just want to know whether we can expect to see stabilisation around this level or how should we see – how can we expect the trend going forward?

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Yes Colin, just to get the question right. You're looking at the Post and Parcel segment where the operating profit margin has come down roughly by 2%, very much so this is the effect of the dynamic change in the revenue mix; Paul have given a bit more colour on the nature of that revenue mix changing but it doesn't change the story in terms of our gradual transformation moving to more eCommerce-related activities which you can see are clearly coming out from the growth in our eCommerce-related revenues – 8.8%, and it's growing every quarter and so as we move there you'll find that the margins will continue to blend downwards and so this is the result of the transformation journey.

Mr Paul Coutts (Group CEO):

Let me just add to that, Colin. In terms of the mix, obviously as we talked about before and no surprise there being that Domestic mail is in decline; it's a high margin business but our strategy is about winning in our home market where we need to start thinking and acting about Singapore as last-mile infrastructure. That's part of the reason why we are putting post and parcel together in Singapore to operate as one; so we are combining the strengths of our postal and our commercial last-mile delivery network to drive synergy benefits and create new products and services specifically for eCommerce, and also for the broader community. There are segments of the markets are growing quickly in terms of the parcels market within Singapore and obviously we are capitalising on those segments which will help mitigate some of the Domestic letter mail decline – but also in movements in terms of the profile of product that we are moving; the margins are tied to those that causes the postal margin influence and the influence is obviously a deteriorating factor at the moment, so we are

trying to make sure that we are putting as much volumes through, leveraging our infrastructure that we have in place to be able to compensate for that, mitigate for that.

Mr Colin Tan (CIMB):

For the Logistics segment, can we get some updates on Quantium Solutions Hong Kong, whether have we seen any new customers and what else has been done that could lead to further improvement in the operating profit?

Mr Paul Coutts (Group CEO):

Sure. So as we talked about in previous quarters, we have got a new team in place in Hong Kong; they have got a turnaround plan which is very much in progress but we also signposted that that will take some time to come through. They are winning some new customers and that's encouraging. It's still early days in terms of the turnaround plan. Overall in terms of Quantium Solutions, I think we have made progress. I am just going to try and talk about specifically where our focus has been.

The first thing is about improving the financial performance of the business; I call that a kind of tactical focus and that has been really about re-engineering of our cost base. We have been reviewing and renegotiating pricing for some of our customer contracts that also included potential exits from loss-making businesses as well; we were clear about that in the previous quarter.

The third piece is about building new businesses obviously, and new revenue streams. We have had some good wins and also as Mervyn talked about earlier in the presentation, we announced that we have won Specialized which has moved into our eCommerce Logistics Hub. We continue to grow our business with Lazada in our eCommerce Logistics Hub as well, and also we are seeing encouraging signs coming through in terms of the improvement of the financial performance.

At a strategic level which is our second key focus, it's really about making sure we reshape Quantium Solutions. By reshaping it we are talking in terms of its scope, its business model, capabilities, go-to market strategy and value proposition and that's very much utilising EDGE technology as a front-end. It's a proprietary technology that we believe sets us apart and gives us the edge over the competition.

But critically, that Joint Venture with Alibaba is obviously – we want to make sure that that's set up for future success and certainly that future model better serves both Alibaba and also Alibaba's extended ecosystem of Cainiao, 4PX, Lazada in this part of the world; perhaps Tokopedia in the future, and satisfy their ambitions but also our own eCommerce ambitions for the future. So we are making good progress there.

Mr Colin Tan (CIMB):

OK, if I can follow-up further moving on to the eCommerce segment. I wasn't really able to get quite a clear picture on what's been said. Just wanting to get some colour really on what led to pricing pressures, whether are we seeing more shifts in the sales mix towards the smaller items or – just want to get a sense on what's the true picture of the pricing pressures that was mentioned.

Mr Paul Coutts (Group CEO):

The pricing pressures were actually more of a product mix issue. The pricing piece has made an influence obviously in terms of margin mix. What we are seeing was – we priced the pieces for warehousing and fulfilment operations which we call "pick and pack" operations, so that's basically

retrieving products from stock and then making sure that we pack those products into an order and then obviously we ship that order. When we ship that order, that becomes freight so the cycle turn of stocks within that warehousing and fulfilment piece is a higher margin business than the freight business.

In addition to that, we also carry a lot of products for customers which are not necessarily pick and pack operations; it's actually just freight forwarding, freight operations so we had less pick and pack operations so less orders actually transacted through the warehouse environment within the month of June. There were a lot more packages moving through last-mile delivery through the freight piece and that's obviously priced at a different point, so therefore that had a margin compression in June. So we saw volume compression and margin compression for June.

Mr Colin Tan (CIMB):

Alright, thank you.

Operator:

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

Mr Varun Ahuja (Credit Suisse):

Hi, good morning everyone. I have got a few questions. Firstly if you look at SingPost's story, your legacy of domestic business has been facing problems and hence you are moving out and developing new businesses. But if you look at current point, it's rather your new businesses are creating more problems that your domestic business; Domestic mail decline is just 2.5% but losses from your new businesses like eCommerce or even the International mail to an extent because of terminal dues – so just wanted to hear how does the management see it in this environment? How should we think about the new businesses when they are creating more problems than your domestic business? That's my perception but I may be wrong so I would want to hear your views on that, that's number one.

Number two is again going back to International mail business. Just wanted to understand is it largely because of the terminal dues that you have not taken some traffic and that's why given it's a scale business, the losses have continued to widen? Because if you look at the growth in the expenses in the volumes side, it is just 7.3% while your revenue grew by 13.0% – so just wanted to see whether you rejected volumes and hence tried to go on that front? Because last quarter I heard you saying that the industry as a whole has taken effort and passed on the higher terminal dues so I was surprised to see losses continue to widen on that front. Just want to hear the view on the terminal dues and hence the impact on the Post and Parcel business.

Thirdly you have been talking about winning in the home market, but if you look at your SP Parcels revenue growth is just 3.0%, 4.0% so not sure if eCommerce is growing so strongly. Just by 3.0%, 4.0% which is your main home market parcel business; are you gaining market share there? What is your thought process on that? That would be helpful, that's number three.

Number four on tax, can you give some more colour on that? Are those non cash related provisions? If it is it a one-off, why didn't you exclude from core income calculations? That will be helpful.

Fifthly on capital expenditure, is it sustainable? The $9.2 million seems pretty low versus S$50 million, S$60 million that you have been guiding so just want to hear on that. Those are the questions that I have, thank you.

Mr Paul Coutts (Group CEO):

Thanks Varun for the questions you were asking earlier. I will try and answer these in order. In terms of the domestic business you are right, obviously we have talked about the fact that the domestic business will continue to be challenged structurally and obviously we are trying to reposition ourselves to be able to compensate for that, mitigate for that and actually more importantly build for the future within the environment. We can touch upon that when we get to that on winning in our home market.

In terms of the new businesses that have come on board, we have obviously embarked on this transformation journey and we have always signposted that it will take time for us to realise the full benefits of that transformation journey. What we have to make sure is that we understand what our strengths are and where our capabilities are, and continue to build on those and mitigate any of the weaknesses that we have within our portfolio and also within our infrastructure and our capabilities. That's an on-going transformation and we want to position our business for the future. We do believe that SingPost is uniquely well-positioned to be successful but we have to address some of the issues with the business. We talked about some of that through the earlier questions and it's no secret we are in turnaround and so on.

The other thing actually is that the eCommerce logistics business is a scale business and volumes are very critical for profitability, but we don't want to go after volume for volume sake. We want to make sure that we can bring value to our customers and deliver value for our shareholders. Therefore we are going to be particularly careful in terms of the customer contracts that we take on and we have to go through a process of – some of the businesses that we have acquired, the new businesses that you were talking about, we are re-engineering those and part of the re-engineering is about making some of those customer contracts more profitable for the business.

The other core element in terms of repositioning our businesses for profit is around our Cost Leadership Programme. Those cost optimisation efforts will improve our profitability as a business and we believe that we will do that materially and it will enhance our competitiveness as we transition to that competitive eCommerce logistics industry.

On International mail, the International mail side – just to clarify a couple of things. When we talk about scale business, International mail from a fixed infrastructure business is not really a scale business because what we are actually doing with International mail is that we are leveraging off other postal operators' scale. Terminal dues are attached to the destination post office delivery infrastructure, and that's the cost that we pick up for instance when we deliver mail into U.K via international mail then we get rebilled by Royal Mail in the U.K. That's what terminal dues are about and that's their scale, their infrastructure. So it's not a scale issue in terms of processes. In terms of the growth expenses, that is directly derived through the terminal dues and just to talk about the influence on particular product segments, there are products to certain geographies, certain weight breaks that we were previously carrying that we have – sad to say that we are not going to carry some of those products in the future because terminal dues just make it unprofitable for us to do so, but that's not a big drop in volumes and therefore having a scale issue; they are actually separate

things. I do want to clarify one thing or actually more importantly I will ask Mervyn to clarify one thing, and that's on the profitability of International mail.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thank you, Paul. Hi Varun, Mervyn here. Just want to clarify the point that International mail is profitable. It is not loss-making, it is profitable. However, where you looked at it I think it was the 3.8% fall in profits and that is again brought about by individual parts of Post and Parcel but still it is profitable.

Mr Paul Coutts (Group CEO):

The final thing I would say in terms of the industry, the influence on the industry – I think it'll be fair to say that all the postal operators are grappling with the same issue at the moment and some may have slightly different strategies. We believe our strategy is the right strategy and that's where we are following through.

If I move in to that third question about winning in our home market, in terms of volume growth around the Speedpost parcels business, our volumes have actually grown significantly. The volumes sorted at the eCommerce Logistics Hub rose 47% year-on-year which is well above market rate. The SP Parcels revenue, just to be clear is not just however, about Singapore last-mile delivery. It also includes inbound traffic from overseas to be delivered through the Speedpost parcels infrastructure and also handles some international volumes which actually are through a product which is called the Express Mail Service. Certainly the Express Mail Service volumes on that international piece were weaker for the quarter which obviously had a revenue influence as well. But in terms of winning in the home market, the domestic market, we are seeing volumes as well in advance of the market. Secondly, some of those volumes – there are actually benefits for our postal business which then helped our postal infrastructure and obviously that is helping us mitigate some of that decline in terms of the domestic business.

Tax and capital expenditure I am going to leave to Mervyn.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thank you, Paul. In terms of taxes, the increase in amount was due to tax provisioning that is done to review the provision accounts for all our subsidiaries, entities within the SingPost group and as part of the review at the end of Q1 we have taken up the provision for tax for a foreign subsidiary by that amount so you see that 38.8% increase of S$3.2 million. The increase comes from a number of subsidiaries – coming from one particular foreign subsidiary and so that is in respect to tax which is part and parcel of the audit closing.

In terms in the capital expenditure, I think in our previous conversations we have always been messaging that we would need about S$60 million just to keep our infrastructure clean, open, well-maintained and so that has not changed. What you see now of S$9.2 million in Q1, I think you need to have a better clarity positioning around the full year. We don't see that change; it would still be kept around S$60 million and so S$9.2 million in Q1 has therefore contributed towards a very nice increase in free cash flow. Our free cash flow has increased from S$32.0 million to S$62.1 million so that's in respect of capital expenditure.

Of course if I can on a broader basis also give an overview and I know this is not one of your questions, but it could also help you to understand the overall performance of the group. So if I can address the key position that was in our media release which is net profit declining to S$18.7 million – I think we need to understand that there were two non-business factors that contributed to this effect and one particular factor that's associated with investing for growth. Allow me to go into the three items.

The first item comprises exceptional items and this really is related to market volatility; market volatility in terms of fair value change in one of our associates, in particular for warrants and so if you look at it in July we would have made a gain so it's very much a function of volatility where it follows very much the index and the mother share. The volatility of the underlying security to warrant of course has a bit of volatility and so we see that coming out on the fair value change, and so you see a huge swing from $4.0 million to $6.0 million which is $10.0 million.

The other one if you strip out the exceptional items – another one would be as you rightly pointed out Varun, and that is the taxation provision which is normal provision which has gone up S$3.2 million. The third item is more a business so-called related but from a good point of view that we are investing for growth in anticipation of higher volumes, eCommerce volumes and it is in respect of the associates and so you see share of associates going up from S$2.8 million to $3.5 million which is a 24.0% increase in losses. A large part comes from an associate that has invested in warehousing infrastructure in anticipation of higher eCommerce volumes.

So if you strip all these three out, our operating profit before exceptional items has already gone up 1.2% and so from that point of view I think it would be a good starting point to then evaluate the performance of the group and that's where perhaps the waterfall chart could help you to see 1.2% increase coming mainly from standard performance from Property. If you look at Property in the bar chart in the slide deck or in the SGXNET announcement, you will see that Property has increased operating revenue very nicely by 32.7% year-on-year whereas in the case of the operating profit line it has increased 67.1% so that largely comes from Property and also coming from a very good performance in terms of Logistics, because all three units of Logistics have improved, in particular Quantium Solutions which we have articulated in the commentary – it has improved 45% whereas the other two entities Couriers Please and Famous have improved their EBIT performance also. So these are the two main reasons but of course this has been offset and as Paul has spoken about it, by U.S performance for specific reasons. So overall the line should actually be how the performance of the group has increased by 1.2% which is at the operating profit line without the non-business factors interfering with the performance. Thank you, Varun.

Mr Varun Ahuja (Credit Suisse):

Thank you very much for your answer.

Operator:

Your next question comes from the line of Rachael Tan from UBS. Please ask your question.

Ms Rachael Tan (UBS):

Hi good morning, I have three questions. I will just run through them one by one. I just noticed that in the financial statements based on the restatement the elimination has actually come down, could you

elaborate on what these eliminations are right now and what were before? So that's the first question, I will wait for the answer then follow-up with the next one.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Yes, in fact this is more in terms of relooking at the overall intercompany transactions, in terms of eliminating them on group consolidation we don't go into details on that Rachael but these have been fully audited for and it's part and parcel of the audit process. Of course the intercompany eliminations is part and parcel of normal year end of quarter end group consolidation.

Mr Jason Lim (Vice President, Investor Relations):

Rachael do you need the number?

Ms Rachael Tan (UBS):

I don't need the number, I just want to know what explains the difference that's why.

Mr Jason Lim (Vice President, Investor Relations):

Because as we move an entity from one segment to the other, the way we treat the revenue and expense is different and that reflects in the elimination line.

Ms Rachael Tan (UBS):

OK, which segment is this involved?

Mr Jason Lim (Vice President, Investor Relations):

Well there are several that we have changed but the biggest one would be moving SP Parcels from Logistics to Post and Parcel.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Perhaps Rachael if I can help on that point – one of the things that we have articulated in the slide deck is that the segments have been reclassified a bit and so just to reiterate again that Logistics in the comparative period comprised or contained two particular units which have now been pushed out of Logistics into two other entities or two other segments. The first within Logistics was SP Parcels and that is now residing within Post and Parcel, the second is General Storage Company and this has been taken out from Logistics and placed within Property so this way you are able to see the full effects of Property at the unit whereas for SP Parcels is as what Paul has discussed – the integration between two units, Post and Parcel to get synergies from the two of them.

Ms Rachael Tan (UBS):

OK, thank you. My second question would be on your domestic market. You mentioned that average volumes were up 47% which was quicker than the market growth, could you elaborate on what sort of activities, what sort of strategies have you been pursuing in order to win market share as well as what is the value proposition you offer that is superior to your competitors?

Mr Paul Coutts (Group CEO):

Sure, so let me try and answer that Rachael. So I think there are a couple of things, we started with a position and when we worked around our strategy almost this time last year where we estimated that we have about a 20% market share in the commercial market in Singapore for last-mile delivery. We felt that with our investments in infrastructure and capability as well as existing infrastructure and capability within the postal sector that we have a big opportunity to bring those together as one infrastructure and leverage off of that infrastructure. The analysis that we did pointed to the fact that we also had the lowest cost position, that we were the lowest cost provider in the industry and therefore that would give us the ability to go and grow our market share, therefore the key focus is about growing the market share. So some of the things that we have done around that is to have a look at those customers where there are high volume business and go after some of these customers more aggressively and that's not more aggressively just on price but certainly price was a key component, but secondly was also going after customers more aggressively in terms of a more broader solution around how we can get those products to their consumers. That may mean for instance a last-mile delivery through a postman, it may mean last-mile delivery via post office, it may mean a last-mile delivery via our locker infrastructure, it may mean last-mile delivery through the Speedpost courier so in other words we have actually widened our solutions to those customers. Our go-to-market strategy is giving them a number of different pick-up and delivery points for their consumers, making it easier for the customers to satisfy their demand. Those have really been the key areas that have been helping us drive the volume growth; but also not only the volume growth but keeping our service levels up and that's something that we are going to continue to invest in.

As you know, we are taking part in the Federated Lockers – part of Singapore's smart nation strategy and we are starting the trial in the next couple of months or so in Punggol. We have a plan to continue to expand our locker infrastructure throughout Singapore and expand our capabilities here and we are investing quite heavily in this area.

Ms Rachael Tan (UBS):

OK, thanks for that. The second question would be on the associates, you mentioned that the key one would be investing for future growth. When do you expect this growth to come through and what sort of businesses is this associate targeting right now?

Mr Paul Coutts (Group CEO):

The associates business, this is really about 4PX which is obviously a Joint Venture partner between ourselves and Alibaba and Cainiao. That particular associate because of the growth in Alibaba's and Cainiao's businesses, has been investing over the last 12 months or so in terms of infrastructure and capabilities in key market segments. The whole thing about eCommerce is that you continually – you are investing ahead of the curve and the predicted growth that you expect particularly for the peak season so you tend to see investments happening earlier in the year to be able to handle the predicted volumes on peak. We have seen some of those investments obviously come through in the Q1 numbers and some of the investments in Q4 as well, and we are obviously making some of those investments ahead of the curve and the curve is really about the uptake in peak season, and we obviously have to wait to see what the benefits will be based on volumes that we experience during that peak season.

Ms Rachael Tan (UBS):

OK, have these investments been completed or still on-going?

Mr Paul Coutts (Group CEO):

It's an on-going investment in terms of the timing of them and also as I mentioned earlier we are investing ahead of the curve for peak season; peak season tends to demand full focus on processing of the volumes and handling the volumes, so that's something that we just have to get the timing right and synchronisation right but we will continue to invest as necessary for volumes for the future.

Ms Rachael Tan (UBS):

When is the peak season typically like for 4PX?

Mr Paul Coutts (Group CEO):

So it starts to pick up in October; you don't necessarily see it coming through in a full month in October because you get Golden Week in October but you would see a three-week activity in October. We will start to see an increase at that point in time and then accelerate through those big sales programmes – we are talking about the Double Eleven et cetera, so November and the first few weeks in December are the critical points in the peak season and some of that actually continues into the first couple of weeks in January because you see a lot of the reverse logistics taking place, a lot of them coming back after the Christmas period.

Ms Rachael Tan (UBS):

OK, so I guess the question will also be on how should we see profitability of this company? So should we see this entity continuing to lose money via investing all the way say until maybe the fourth quarter of the year, where it will peak into profit then after that it will improve into low profitability? Or should we see a more steady growth in earnings going forward?

Mr Paul Coutts (Group CEO):

I will get Mervyn to touch upon that.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thank you, Paul. Rachael we can't give any profit guidance here but suffice to say that 4PX remains a critical part of our overall Southeast Asia strategy, and so we will continue to work on that associate with our partners in progressing the eCommerce volumes.

Ms Rachael Tan (UBS):

OK, thank you.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thanks Rachael.

Operator:

Your next question comes from the line of Low Pei Han from OCBC. Please ask your question.

Ms Low Pei Han (OCBC):

Hi, thanks for the opportunity. I think that the Logistics segment is near breakeven level and the eCommerce segment saw wider losses quarter-on-quarter and it may take some time to see a turnaround. So just wondering how would you describe this year? Is it still a year of transformation, year of recovery or is it more suitable to call next year the year of recovery? Thank you.

Mr Paul Coutts (Group CEO):

So let me try and deal with that. The key thing for us is the turnaround plan in the U.S so we have had a very clear focus on that and as I mentioned we were still on track in April and May, June we saw a bit of a blip, at this point in time we could consider a blip. But I have also made mention earlier during the call that we need to have a look at what July is, what August is so we will adjust accordingly.

In terms of when the transformation, in terms of the timing, will lead to full recovery and so on, we haven't set firm deadlines for some of those businesses to get to profitability. We are more interested in terms of progressing our plans, making sure that we are executing our plans well and that leads to progress and that progress will lead to us repositioning the company successfully over a period in time. So that's where the key focus points for us will continue to be.

Ms Low Pei Han (OCBC):

OK, thank you.

Operator:

Your next question comes from the line of Colin Tan from CIMB. Please ask your question.

Mr Colin Tan (CIMB):

Hi, just a quick follow-up question on the tax provisions, whether we can expect to see any further provisions ahead? Thanks.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thank you, Colin. Tax provisions would be a function of the performance of the entity so this is something that of course we will drive in terms of performance, improving it, of course improving the performance of the various entities. So I can't give you a very firm indication of that but very much follows the performance of these various entities.

Mr Colin Tan (CIMB):

OK.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thank you, Colin.

Operator:

There are no further questions at this time.

Mr Jason Lim (Vice President, Investor Relations):

Thank you everyone for joining the call. If you have any follow-up questions you have my contact details, so I think we will end the call here, thanks.

Mr Paul Coutts (Group CEO):

Thank you.

Mr Mervyn Lim (Deputy GCEO (Corporate Services) and GCFO):

Thank you, everyone.

Operator:

Thank you for dialling in to this briefing.

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