SingPost's Q3 & 9M FY18/19 Results Analyst Briefing, 1 February 2019

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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 (Vice President, Investor Relations):

Good morning. Welcome to SingPost's results briefing for the third quarter and nine months of FY2018/19. I am Jason from Investor Relations. With me today is our GCEO Mr Paul Coutts, as well as our GCFO Mr Richard Lai.

I'll now hand over the session to Richard to bring you through our results.

Mr Richard Lai (Group CFO):

Good morning and welcome to our results briefing. Let me first share an overview of our Q3 results.

We recorded good revenue growth over the peak season, as group revenue rose 7.6% to S$441.4 million on strong volumes. However, due to intensifying competition and rising customer bankruptcies in the US, profit on operating activities declined 8.5% to S$42.2 million. Excluding the US businesses, profit on operating activities would have rose 9.8%. Net profit rose 15.6% to S$50.2 million, due largely to an exceptional gain on dilution of our stake in 4PX.

I will provide more details on our financials over the next few slides. The Board has declared an interim Q3 dividend of 0.5 cent per share, same as last year. This brings total dividends for the year to 1.5 cents.

Revenue increased 7.6%, driven by growth across all of our 4 business segments. Profit on operating activities also rose in 3 of our business segments - Post & Parcel, Logistics and Property respectively. However, these were largely offset by higher losses in the US, which led to a 8.5% decline in the Group's Profit on operating activities. In Q3, we have ceased equity accounting for 4PX and ITL, and consequently the share of associated companies and JV was S$17,000. As previously announced, 4PX ceased to be an associated company after the issuance of additional shares to Cainiao, which diluted the Group's shareholding down to 19.75%. We have entered into an sale agreement for our shares in ITL, and therefore it has been reclassified as an Asset Held for Sale.

The Group recorded an exceptional gain of S$31.8 million in Q3, largely due to the gain on dilution of interest in 4PX, partly offset by fair value loss on warrants from GD Express. Income tax expense for Q3 was S$9.4 million, compared to S$2.9 million last year. The lower tax expense last year was due to an one-off adjustment of deferred tax of S$6.9 million arising from a reduction in the US corporate tax rate. Net profit attributable to equity holders rose 15.6%, largely due to the exceptional gain. Excluding exceptional items and one-off tax adjustments, underlying net profit declined 7.5% due to higher losses from the US businesses.

Operating expenses rose 8.8% in Q3, due to higher volume-related expenses with the increase in volumes handled. With increased volumes came increased disputes. We have taken prudential action by making provisions for some of these disputes in the US, leading to an increase in admin expenses. Labour and related expenses declined 3.1%, as our productivity enhancement and cost management plans led to lower contracted labour services as well as lower staff costs.

Moving on, let me share some operating highlights for the quarter.

We are making good progress in Winning in our Home Market, and achieved strong volumes in Q3. Parcel sorting volumes at the Logistics Hub rose 15% year-on-year to 23,900 parcels daily. The highest volume achieved in a single day was 47,000 parcels, compared to 33,000 last year.

In November, SingPost unveiled a new proprietary logistics software Last Mile Platform, or LaMP for short. It is a one-of-its-kind technology that consolidates various last-mile delivery services, such as courier services, parcel lockers, and brick-and-mortar collection points, onto a single platform across Southeast Asia. As mentioned in an earlier press release, we are in advanced talks with an Indonesian last-mile operator with 1,500 collection points across 58 cities.

SingPost recognised a gain on dilution of our interest in 4PX, which amounted to S$28.2 million excluding non-controlling interests. Cainiao's further investment in 4PX will allow deeper business integration between 4PX, Alibaba Group and SingPost for cross-border eCommerce volumes.

This chart shows the impact of the various business segments on underlying net profit. Profit on operating activities from the Post & Parcel segment rose S$4.3 million, while the Property segment earnings grew S$2.1million. Logistics continued its turnaround, and profit was up S$0.7 million. However, eCommerce segment losses widened by S$8.9 million, largely due to the US. Consequently, underlying net profit declined 7.5%.

Let me now move on to the Cash flow and Balance sheet.

For the nine months ended 31 December 2018, Operating cash flow before working capital changes rose 4.5% to S$159.0 million, from S$152.2 million last year. Working capital movement was negative S$27.0 million for the period due to the timing of receivables in respect of international eCommerce deliveries. As a result, net cash inflow from operating activities for the nine months ended 31 December 2018 declined to S$99.3 million, from S$146.5 million last year. Capital expenditure declined to S$25.4 million, compared to S$52.9 million last year, with the completion of the SingPost Centre retail mall redevelopment. Consequently, free cash flow amounted to S$73.9 million.

We now move to the financial indicators. Cash and cash equivalents stood at S$345.9 million as at 31 December 2018. Total borrowings rose to S$293.2 million, as the Group switched from an intercompany loan for a foreign subsidiary, to an external loan for better matching of currency. The group was in a net cash position of S$52.7 million as at 31 December 2018, compared to S$70.1 million as at 31 March 2018. This was largely due to higher working capital requirements during the period. EBITDA for the 9M period rose to S$180.5 million, due to higher profit on operating activities as well as exceptional items. Notwithstanding the increased debt, interest coverage ratio stands at 25.2 times, compared to 20.3 times last year.

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

Mr Jason Lim (Vice President, Investor Relations):

Thank you, Richard. This slide provides an overview of the various segments' contribution to Group revenue and profit on operating activities.

For Operating revenue, the Post and Parcel segment remains the largest contributor, followed by the Logistics and eCommerce segments. Post and Parcel is also the largest contributor to Operating profit at S$47.6 million, followed by the Property segment at S$13.9 million. The Logistics segment continued its improvement, reporting operating profit of S$1.8 million for Q3. eCommerce segment losses widened to S$13.4 million due to challenges in the US businesses. In the Others segment, we recorded unfavourable movements in trade-related foreign currency translation differences of around S$2.9 million.

Next, we will take a closer look at each of the segments.

In the Post & Parcel segment, revenue rose 9.0% in Q3, driven by both domestic and international eCommerce deliveries over the peak season. Domestic mail revenue rose 1.6%, as increased eCommerce deliveries on the domestic postal network helped offset the decline in traditional letter mails. For International mail, revenue rose 16.3%, lifted by cross-border volumes from the Alibaba Group, through 4PX, for the Double Eleven event in November. Profit on operating activities rose 10.0% in Q3. Domestic margins improved as the Group reaps operating synergies from the ongoing integration of our last mile delivery capabilities in the Post and Parcel divisions. International mail contributed to earnings growth on the back of higher volumes over the peak season. For 9M, revenue and profit on operating activities rose 5.6% and 3.7% respectively.

In the Logistics segment, revenue rose 3.6% in Q3, driven by the freight forwarding business under Famous Holdings. At Quantium Solutions, there is an ongoing review of unfavourable customer contracts and revenue declined marginally with the exit of some unprofitable customers. Profit on operating activities rose 67.4% in Q3 to S$1.8 million, largely due to a reduction in losses at Quantium Solutions, which was successful in improving profitability of its customers. For 9M, revenue rose 0.6%, while operating profit was S$2.2 million, a turnaround from a loss position last year.

Revenue rose 8.7% in Q3, as volumes rose over the peak season in the US. Operating loss rose year-on-year to S$13.4 million in Q3, largely due to the US businesses. Competitive pressures have intensified in the US and the industry has seen an increase in bankruptcies. While the US businesses recorded higher revenue during the quarter, costs also rose significantly to support these businesses, including freight and outsourced services, resulting in compressed margins and a loss during the critical peak season. For 9M, eCommerce segment revenue rose 2.1%, while operating loss widened to S$33.9 million.

The Property segment comprises commercial property rental and the self-storage business. In Q3, revenue rose 4.0% and Profit on operating activities rose 18.2% respectively, due to rental income from the SingPost Centre retail mall, which commenced operations in October 2017 after a period of redevelopment. Committed occupancy for the mall was 98.5% as at 31 December 2018, compared to 85.9% a year ago. For 9M, revenue rose 17.9% while profit on operating activities rose 42.9%.

Let me now hand over back to Richard for the Outlook.

Mr Richard Lai (Group CFO):

Thank you, Jason. I think all of you would probably have read Paragraph 10 of the exchange announcement so I won't go into it again. It's sufficient to say that while the Group has a lot of potential for further growth especially in the Post and Parcel business and Property side, the eCommerce business in the US continues to pose a significant challenge. So we are actually taking a very close look at the business; we will probably be able to comment more about it in the next quarter. Thank you.

Mr Jason Lim (Vice President, Investor Relations):

With that, we conclude our presentation. We are now ready for Q&As, operator 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. Your first question comes from the line of Azita Nazrene from Macquarie. Please ask your question.

Mr Neel Sinha (Maybank Kim Eng):

Good morning everyone, thanks for the presentation. I have three questions – the first is trying to understand the big picture perspective. Your revenue for the quarter grew 7.6% and your volume-related expenses grew 14.6% and that's a quarter where oil prices were coming off, so I am trying to understand what's going on there. I mean what's influencing volume-related expenses to grow at double the run rate of revenue growth.

The second question is again – I think you touched on this. For the US the higher business level in similar tone, roughly S$7.0 million increase in revenue for the eCommerce business in the US is offset by S$9.0 million odd increase in costs at the profit level roughly right? So again, is it legacy contracts that are unprofitable et cetera? Because if I take a step back which is driving to my third question, this is a quarter which is usually the best quarter for volumes right? If volume-related costs are running ahead in what is traditionally an operating leverage driven business, what needs to be done or am I missing something here? Because it's not all in the US from what I can gather, the operating volume-related costs have gone up faster than revenue elsewhere as well.

And finally is there some inflexion point that we can expect? You mentioned, Richard, on Quantium Solutions that there is some exit of unprofitable customers. At what stage – is it another one or two quarters before you finish the process or is it largely done? Thanks very much.

Mr Paul Coutts (Group CEO):

Thanks Neel, first of all for the questions. It's Paul here. So yes, I think there is a correlation to some extent between what you are seeing and you picked up on what you are seeing at the US side and then in terms of the revenue at the Group side. A couple of things – there are a couple of dimensions there, a large part of that revenue increase on the US side is in the freight business and the freight business is a product which has been very tight in terms of margins and it's under increasingly competitive pressure and we have reported that previously. So margins are being squeezed in that particular area and we are also seeing through the peak period as well. We operate within a very tight labour environment in Cincinnati and whilst it's true that in peak times your volumes are obviously increasing, you are also seeing an increase in terms of the hourly costs and labour costs for a lot of the contracted staff that we have who are processing those volumes, and so we are not necessarily seeing the benefit of that in our bottom line and that's also got a correlation there on the Group results.

The other dimension on the Group results we need to take into account is that the volume increases from a Group perspective are also influenced by the terminal dues rates which are for the International mail business – and saw significant increases in revenue coming through which was good but we also know that the terminal dues increases that took place through 2018 obviously has an impact on our cost base. So if you look at International mail as a standalone, the result is good, it's positive but nonetheless we have obviously seen terminal dues increases and that combined with the US means it's not a direct correlation between the revenue side and what we are seeing on the volume side.

I would also add one thing here, it comes back to the US – Richard mentioned that earlier and certainly we clearly continue to face challenges in the US and we currently have a task force in the US which is conducting a further detailed review of the business. We are very cognisant about generating long term shareholder value and so that's a priority for us and also we need to make sure that we are looking at all possibilities to improve our business in the US, but also consider all possibilities in terms of how we move forward with the business strategically. As Richard mentioned, we will update you further in the next quarter.

On the inflexion point for Quantium Solutions, we have obviously gone through that process of renegotiation with customers and so on, we are through that process now and we are very much in the business building mode, we have been on with a clear business development strategy for the business to replace any of the businesses that we have exited from but also on a more profitable level.

Mr Neel Sinha (Maybank Kim Eng):

Thanks Paul.

Mr Richard Lai (Group CFO):

Neel, just to add on to that, your question was also in relation to at a time when you are seeing oil prices dropped right?

Mr Neel Sinha (Maybank Kim Eng):

Yes, they have moderated through the fourth quarter on a year-on-year basis right?

Mr Richard Lai (Group CFO):

So in reality, that doesn't always get translated to lower freight prices because it's also a function of demand and supply and seasonality and so forth. In the States in particular, there are only a few large freight providers effectively, maybe two. So in effect during the peak season, you end up pretty much being a price taker – you have very little room to negotiate in your pricing because everybody will be using them to try and move their stuff around. So as a result it doesn't really get translated into lower freight prices for us.

Mr Paul Coutts (Group CEO):

It's also as you know, we move a lot of our volume by air for cross-border, and we have to lock in well in advance what the rates are going to be with the airlines so therefore we don't necessary get the benefit but nor do we get the pain if fuel prices actually rise so that's locked in well in advance on a forward basis.

Mr Neel Sinha (Maybank Kim Eng):

Alright, thanks very much. I just have a quick follow-up on that consolidated revenue and volume-related costs. If you have to ballpark that at a number, stripping out the US business impact and, my bad, yes there was that year-on-year terminal dues impact, would the volume-related expenses be closer in line with revenue growth or slightly higher as opposed to double where it stands now?

Mr Richard Lai (Group CFO):

Certainly so, yes.

Mr Neel Sinha (Maybank Kim Eng):

Alright, thank you.

Mr Jason Lim (Vice President, Investor Relations):

So the other way you can see it as we disclosed in the slides, if you strip out the US business, operating profit is actually up 9.8%, so that indicates an expansion of margins in the other businesses other than the US business.

Mr Neel Sinha (Maybank Kim Eng):

Thanks Jason.

Operator:

Your next question comes from the line of Siward Ludin from Goldman Sachs. Please ask your question.

Mr Siward Ludin (Goldman Sachs):

Hi, thanks for taking my questions. I got two questions here, first one is on the US eCommerce business, could you share a bit more on the competitive landscape going forward and is it still going to be this competitive, or are you seeing a better landscape in the next one or two years for example?

Second question is on Quantium Solutions. Is the customer review still ongoing and could you share a bit more colour on this? When do you expect this process to be finalised and you can start rebuilding the business? Thanks.

Mr Richard Lai (Group CFO):

Let me have a go at this. To your first question, I don't think we could say that the US eCommerce industry is going to get any less intense in competition. In fact, conversely it's true – it's getting more intense in competition and therefore it may eventually lead to greater consolidation in the US market as the small players get marginalised by the bigger players, so I think the prognosis for the near term doesn't look great in terms of the industry. We are seeing increasing number of customer bankruptcies, we are seeing increasing number of retailers going under and some of these are very big ones too. So I think from our point of view we just don't think that this is going to change anytime soon.

The other question on Quantium Solutions review, customer review. The Quantium Solutions customer review took place for some of our bigger Quantium Solutions presence, we have sorted that out so we are moving forward, but for the business as a whole there is always something we can continue to look at from where we could fine-tune so we are past that part about reviewing the customers and we are now in the phase of building up pipelines for that business. But there are still fine tweaks we are doing in respect to some of our smaller presence in some of the other countries; the fringe markets and so forth, whether or not we are going to keep those presence and things like that. Those are finer tweaks that we are doing to the organisation and those will be an ongoing process.

Mr Siward Ludin (Goldman Sachs):

Thank you. Just a follow-up question on the US businesses as well – the customer bankruptcies, do you have any particular concentration of any customers? Could you explain a bit more on that? Just want to check whether there is any concentration risk here on your clients. Thanks.

Mr Richard Lai (Group CFO):

Probably what I can say is that we do have quite a fair bit of customers in the apparel section. Apart from that, there is nothing more I can comment about that.

Mr Siward Ludin (Goldman Sachs):

Got it, thank you.

Operator:

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

Mr Sachin Mittal (DBS):

Thank you. My question is with regard to expectations of revenue growth, if we strip out the eCommerce business and look at Logistics and Post and Parcel, we are looking at probably high single digit kind of growth because there seems to be some terminal dues impact on International mail. So my question is if that is the expected growth rate in the future, or around there, what is the main driver for improvement? For example, your margin at 22.3% or 22.0% – do you expect margins to improve going forward for segments like Post and Parcel and Logistics? Or do you think that it has to be driven by higher growth rate in the revenues rather than margin improvement? I think this is my first question.

Mr Richard Lai (Group CFO):

Good question, I would say that some years back we looked at the Post and Parcel business and we all thought that that business is going to shrink very quickly and die off altogether, but what the truth has been so far – what we have seen is that the business has been more resilient than we have originally expected. So I think the end of it is going to be a combination of two, one obviously is there's still room for revenue growth in the Post and Parcel area while Domestic mail may continue to shrink slowly, they have been more than offset to a large degree by increase in parcels, going through the Domestic mail system. There are still process improvements that we can do to try and improve our margin, there are still possibilities for further automation, so there is still room for those stuff for improvement in terms of productivity and so forth.

So naturally we are going to continue to focus in those areas while not trading that off – we are not going to trade that off against service quality which is something very close to heart for all of us here in Singapore.

Mr Paul Coutts (Group CEO):

I think there's a couple of things which I would add to that, Sachin. Good morning to you and thanks for your questions. So the first thing is if you go back to our strategy which we set out about 18 months ago or just over 12 months ago when we announced in November 2017. We talked very clearly about our first key theme which is Winning in our Home Market, and we are certainly seeing some of the signs of that focus, a more focused strategy in our home market; we are seeing signs of growth in that area as Richard has talked about, we are kind of compensating for any decline that's taking place in the Domestic mail letters business.

At the same time, we have also talked about the fact that we are now more focused from a Quantium perspective in terms of bringing in new customers and growing our business in the Quantium division. We do have expectations of reasonable growth in that area and just to underpin what Richard said in terms of the International mail side, we believe that we can play successfully in that particular segment but we are going to pick the markets that we believe where we can add value and get value for our shareholders in return, and that's where our key focal point is going to be for International mail.

Mr Sachin Mittal (DBS):

If I summarise what you said, in the past SingPost was mainly about growth, heavy growth and lower margins but now are we talking about slightly slower growth in terms of revenue? Are we talking about stable to improved margins overall, excluding the eCommerce portion? Is that the right understanding I have on the margins?

Mr Paul Coutts (Group CEO):

Sorry, are you talking about postal Domestic and International or – ?

Mr Sachin Mittal (DBS):

I am talking about margins for maybe Post and Parcel and the Logistics segments, I am not talking about eCommerce because that's something difficult to predict even because of all these uncertainties. I am talking about these two segments, is the margin profile something which has potential to improve from where we are right now?

Mr Richard Lai (Group CFO):

Yes, it's like I said earlier, it's something that we continue to look at improving on. So there is still something that we think we could try and squeeze on the profit margin to get more out of it.

Mr Sachin Mittal (DBS):

OK, that's clear. Secondly, this is a housekeeping question. What are the carrying values of your eCommerce businesses, the US businesses right now which you are highlighting if there is a risk of possible impairment?

Mr Richard Lai (Group CFO):

Well, it's somewhere between S$90.0 million and S$100.0 million.

Mr Sachin Mittal (DBS):

OK, that's very clear. Thank you.

Mr Richard Lai (Group CFO):

Just to be clear, that's in Singapore dollars. Not to be confused with US dollars.

Operator:

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

Mr Low Horng Han (CLSA):

Hi, good morning everyone. Thank you for the presentation. I have just a few questions if you could bear with me. The first is on the last mile delivery, I understand that in the Logistics segment you have been making quite a bit of headway in the space here. I just want to know the revenue contribution from last mile, is there any way you could give us some number and where you see the potential going forward in Singapore given that you have the advantage of infrastructure in Singapore itself?

Mr Jason Lim (Vice President, Investor Relations):

Sorry, our revenue from last mile where again Horng Han?

Mr Low Horng Han (CLSA):

Last mile delivery related businesses, how much revenue contribution is there?

Mr Richard Lai (Group CFO):

Horng Han, not a very easy answer to that question simply because it's hard to segmentise that because of the way things are. Post and Parcel, if you look at it you would say that a large chunk of it is last mile delivery right? You can also look at it from the perspective of eCommerce by itself – also has a last mile component so it's not an easy way of dividing it or segmentising it but if you must, then take a look at our Post and Parcel as an indication. In Australia we have Couriers Please as well as our last mile delivery.

Mr Low Horng Han (CLSA):

I understand Richard, but maybe if we focus on Singapore – I asked this question because it seems like Post and Parcel, and Logistics, some of the better momentum that you have the last quarter was also partly driven by last mile. Is there any number for Singapore itself you could share and the kind of potential you see in terms of market share expanding?

Mr Richard Lai (Group CFO):

No, we don't measure in that way. If you look at Domestic mail as a business that's last mile, you can consider that entirely as last mile. We don't segmentise it in that way, Horng Han.

Mr Low Horng Han (CLSA):

OK, no worries. Second question here would be your capex for the first nine months, how much of the capex is actually attributed to the investment in the US eCommerce, the automation you have been doing?

Mr Richard Lai (Group CFO):

Capex – the amount that we have done so far?

Mr Low Horng Han (CLSA):

Yes, I'm just trying to segregate between US and non-US capex.

Mr Richard Lai (Group CFO):

Not that much actually. I think we have done some for the automation but even that has been mainly on leasing model as opposed to actual outright capex. We did have automation but they were all on leasing model so most of the capex hasn't been in the US. Part of the reason is because of the availability of leasing companies so it makes it possible for you to lease as opposed to spending the capex.

But having said that, part of the reason we are doing this deep dive is to evaluate whether or not we should be putting in more money which would probably involve capex as well, or not, among other things; we are taking a very holistic look at this.

Mr Low Horng Han (CLSA):

Got it, thank you very much. Thank you, Richard.

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. Thanks for taking my questions, I have got a few questions so I'll just go one by one. I want to come back to US businesses, if my memory serves well this is probably your third, fourth review over the last few years in the US businesses. So what difference shall we expect as an investor from this review? And I just want to go back again to my question from the last quarter – do you see US as very critical or central to your long term plans or vision for the company? Because it seems based on the commentary that has been made, business is tough, the environment is getting worse so I know you may not be answering that question in that review but any thoughts – how you see this business, is it critical or do you want to let it go and you are fine with that? So I'll appreciate more colour on the strategy for the US businesses, so that's number one.

Mr Paul Coutts (Group CEO):

Do you want to take it one at a time? OK, so thanks for the question. We obviously have a turnaround plan for the US and if you go back several quarters, we talked about that and generally speaking we were on track with that turnaround plan. However, as Richard mentioned earlier as well, there's definitely some increasing competitive pressures, some structural changes taking place within the industry and that combined had basically kind of knocked us off track which we saw in quarter one of the current financial year which we then set out to address. So it's clear that we have to have a further detailed review of the business; our goal really is to make sure that if we are going to stay in the US market, which we still see as being an attractive market, we have to make sure that we are confident that we have a viable and sustainable business and that's for the benefit of our shareholders. So that process that we are working through, that's the objective of the task force so we shouldn't get too far ahead of ourselves and we want to make sure that we are in a position to make a more strategic decision as we get closer to the next quarter.

Mr Varun Ahuja (Credit Suisse):

OK, so is selling the whole business or shutting it down – is it on the table? Is it one of the options? Or is it to narrow down losses to meet and improve efficiencies?

Mr Paul Coutts (Group CEO):

So again, we come back to what we said earlier – our goal is to make sure that we are generating value in the long term for our shareholders in any business that we have and also we need to make sure that it's doing so, and if it's not doing so, then we need to consider all possibilities, we need to be open to that.

Mr Varun Ahuja (Credit Suisse):

OK, that's helpful. Secondly I just want to go to another business, Quantium Solutions. If I remember correctly when you first started the business of acquiring the objective was a little more to tap into growth opportunities in the ASEAN region, but seems to me it's become more become Hong Kong, China centric and you've made very little progress on the ASEAN eCommerce front so what is the strategy of this business? Is it supposed to be a gateway into ASEAN wherein you have some assets? But doesn't look like – it's mostly now problems in Hong Kong and China and there's hardly any growth so what do you want to do with this business?

Mr Paul Coutts (Group CEO):

So we go back to what we said earlier – the starting point for us is to understand what is the business, who are the customers that we have today, are those customers profitable or not profitable? Obviously if you go back to the losses that we are incurring in the previous financial year, that was a huge cause of concern for us so we have to go about first and foremost resynchronising our business and obviously try to reduce those losses that we saw – significant level from the year before. I think we have made progress in doing that; we have had to exit some non-profitable customers, in that process we have reshaped the businesses I mentioned and we have started to bring on new customers who are more profitable. One of the things that we are extremely conscious of and we've talked about this again in previous times is that we need to make sure that the strategy that we've built for Southeast Asia is a market-by-market play, but one of the things that's common in there in those markets is that you need a very extensive last mile infrastructure and ecosystem to be able to tap into. Hence the reason also why we are focusing very much in not only developing but executing our last mile platform which is our technology platform, and also we will officially launch that within the next quarter with a live customer and then we will look to expand that very quickly in Southeast Asia which will get us that infrastructure which we will then need to be able to fire up that engine for growth in Southeast Asia.

Mr Varun Ahuja (Credit Suisse):

Sorry, were you looking at partnerships for last mile now in Southeast Asia? Is Indonesia part of that as in you put in technology and partner with the locals?

Mr Paul Coutts (Group CEO):

We'll look at partnering with other postal operators of course, it's part of our ASEAN version of the UPU but in addition to that we are also partnering with other domestic express operators within that sector.

Mr Varun Ahuja (Credit Suisse):

OK, lastly I just want to come back to the domestic Post and Parcel business. So the third quarter is supposed to be good in terms of eCommerce volumes but still the parcel business revenue growth is pretty weak, and in the mail segment I understand it's a mix of both your legacy business and the eCommerce growth. So can you give a little bit more clarity – how much is the legacy business in the mail segment what is the reason why SP Parcels is still very lacklustre during this quarter where the volumes are supposed to be strong? Is it the competitive pressures – the volume growth was good but because of pricing? Any more colour on that would be helpful. Thank you.

Mr Jason Lim (Vice President, Investor Relations):

OK Varun, so what has happened in this space is that Domestic mail and SP Parcels is in a way we have merged it operationally so it needs to be taken together as a whole. So if you look at the Domestic mail revenues they have actually traditionally declined about mid-single digit percentages, but we have actually seen Domestic mail revenue growing 1.6% as a result of increased eCommerce deliveries. So when you allude to the weakness in SP Parcels it's the fact that a lot of the items are now booked under the Domestic mail revenues and the reason for that is because we are already integrating our last mile delivery, post and parcel capabilities in Singapore. And there's two functions of that, one is that the market itself – many of the platforms actually are opting to use postal mail to deliver eCommerce items and it's because in a way they might not need high specifications, they might not need tracking, they might not need doorstep delivery so they are diverting some of these volumes to Domestic mail. So for what we have reported based on 23,900 parcels, the number would actually have been higher if we had included some of these eCommerce customers who are actually delivering on the postal network rather than traditionally the SP Parcels network.

Mr Varun Ahuja (Credit Suisse):

OK, hear you. Jason, any colour on how much is now the traditional mail business, legacy business now in the total?

Mr Jason Lim (Vice President, Investor Relations):

I think a bit of colour on that. A vast majority of Domestic mail is still traditional letters, way above 50% is still traditional. There's a small portion of revenues that are attributed to eCommerce but small portion.

Mr Varun Ahuja (Credit Suisse):

OK, thank you very much.

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 was just wondering if your Singapore business how do you plan to – Singapore as well overseas businesses, how do you plan to mitigate impact?

Mr Jason Lim (Vice President, Investor Relations):

Sorry, you are a bit muffled Rachael. We can't really hear you.

Ms Rachael Tan (UBS):

OK, I was just wondering amid the trade dispute driven slowdown, how much of your business potentially do you see impacted by that?

Mr Richard Lai (Group CFO):

OK, let me try. Rachael, from our standpoint here we don't see a lot of fallout from the trade by itself but there's definitely some evidence that's coming through now to suggest that there's a slowdown in the global economy. That one is one that has a greater impact on the flow of business as opposed to any suggestion of a trade war between China and the US affecting trade.

Ms Rachael Tan (UBS):

OK, did you see any of that kind of – I know the International mail volumes were good, but was there any disappointment or slowdown on that front or were you starting to see, or you haven't noticed it yet?

Mr Richard Lai (Group CFO):

Actually, the buying pattern is something we obviously have noticed but apart from that we've been quite happy with this time round – our handling of the peak season. In terms of volumes it's been wonderful, we've been quite happy with what we have. We were quite happy with what we have seen as generated in terms of values from China as well. So I think the difference however is that the online purchasers are now more prepared to buy higher value items online as opposed to the past, where you would see a lot of purchase of only the low value items. So that is starting to see a bit of shift in that buying pattern.

Ms Rachael Tan (UBS):

OK, so what I am guessing from this here, just to be clear is that you don't see a direct impact of the trade slowdown on your business but if the economy slows down then there should be some commensurate impact on your business. Is that right?

Mr Richard Lai (Group CFO):

Yes. If there is a more serious global slowdown, yes, it will affect not just our business but all businesses will be affected; Singapore will certainly be affected.

Ms Rachael Tan (UBS):

OK certainly. Thank you.

Operator:

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

Mr Sachin Mittal (DBS):

Sorry I'm back on this question on the margins for Post and Parcel. You have been integrating SP Parcels and Domestic mail so how long have you been doing it and what percentage has kind of been integrated now? Because it is difficult for me to imagine that the margins can go up because growth is coming from International mail which is a lower margin business, so trying to think through it. What could be the reasons for the margins to either stabilise or improve in Post and Parcel. Is it just integration or is it anything else? Some colour on that please.

Mr Richard Lai (Group CFO):

Sachin, a year and a half ago when Paul first came on board, the thinking is that you can't get anything else out of Post and Parcel, you can't get anything else out of Singapore, and I think we've proven that so far that's not true. We undertook a cost leadership programme that led to a reorganisation, restructuring of some of our businesses to improve the process flow which led to greater efficiencies. All these do translate ultimately to better margins at the end of the day, so it's not just driven by postal rates, it's also driven by the costs to manage that segment. But having said that, obviously with the rise in parcels, the handling of parcels and things like that, obviously these are growing pains for any postal agency in coping with this shift in dynamics. We will probably have to continue to invest into our infrastructure so that we could better handle all these things. Now, with that it also potentially means that there is still the potential for improvement in margin from that point of view, but I think there is the matter of priorities – which one comes first? We would ideally like to be able to get everything all at the same time but we have to be mindful of the fact that first and foremost our service quality has got to be kept up there, at a certain standard level. So I think we are trying to manage such that our spending, our investments give us at the same time – maintains the sort of service quality that everybody expects of us, so that is on that front.

Notably, International mail does suffer from terminal dues increase but having said that, the team has done very well in terms of managing its freight costs and Paul alluded to that earlier that we locked in a lot of these freight early on to avoid any increase, potential increase in freight costs and the sort of things. So a lot of studies and the monitoring of markets are done by the team to ensure that they get the best rates that they can and this takes a pretty fluid and nimble team to be able to do that. so again, you have all these dynamics running to try and better manage the cost front so obviously that's where we are looking at to manage the margins.

On the revenue side, the question on the continued growth of the eCommerce market – so long as the market continues to grow and even if we were to maintain our market share, we ought to see growth and obviously we are hoping to get more of the market share but that's a separate topic altogether.

Mr Sachin Mittal (DBS):

Just to follow-up on the logistics hub, I hear about a lot of stress in the logistics space especially in the start-up space; a lot of disappointment in these start-ups. Do you see any of your big competitors pulling back or not yet? I mean you have been rationalising your business, have you seen similar kind of rationalisation from any of your key competitors?

Mr Richard Lai (Group CFO):

Well, look, it's all over the press there's some sort of new consolidation going on in the industry right? Even among big players and so forth, so I think you also have to understand that in the logistics spectrum – it may come surprising but there's a fairly wide spectrum within logistics itself. You got the B2C, you got the B2B, you've got those that are doing more of the haulage side, freight side so it's a pretty wide spectrum when we say "logistics" because it's a very generic term. From where we are currently, obviously I would say we need to increase the scale of our logistics business for it to become profitable. That's for certain, and I don't think we are at this point in time seeing a slowdown in terms of logistics requirements if that's the case. But definitely industry wide there is some consolidation going on amongst some of the big players and I don't know whether Paul wants to add anything.

Mr Paul Coutts (Group CEO):

Look, I mean Sachin, we're definitely seeing some concerns and amongst the logistics community with regards to what they are seeing currently – now that we are past the peak season, what they are seeing currently and also what the norm will be. If you look at some of the comments that have been made by FedEx in recent weeks around the fact that the express growth is slowing up, and also DHL and UPS are also talking about the fact that they are very much going to focus on the cost base again and kind of re-engineer to make sure that they are hitting their maximum efficiencies for their operations. I think you are starting to see a lot of signals from the integrators that the winds are definitely shifting. I think the other thing is you're also going to see a period of consolidation taking place in the freight forwarding sector.

There is obviously an announcement fairly recently about DSV looking to go on to their next phase of growth; they're looking at doing that more via acquisitions rather than organic ways so again looking to acquire Panalpina obviously as one of the frame for that, and I think that will be a consolidation within the top 10 forwarding community as well, some of that is driven by competitive pressures and industry pressures. Another thing I think I do believe is playing out particularly in the start-up community – we have talked about this before and it's that the last five years in particular have been great for start-ups because there's been a lot of cash available, it's been a liquid market and lots of people are prepared to invest in capitalising on the growth that's taking place, cost of cash has been cheap but that backdrop has changed pretty significantly in the last six months or so and I think it will become even more acute in the next six to twelve months and also many of the start-ups at this point have yet to get to again, what I've talked about as being a viable and sustainable model. So I think that you'll start to see some perhaps consolidation happening there and also some rationalisation happening there in terms of the players in the market - I mean that's my personal view in terms of what will happen.

Mr Sachin Mittal (DBS):

OK, that's comprehensive. Thank you.

Operator:

Your next question comes from the line of Ngoh Yi Sin from CIMB. Please ask your question.

Ms Ngoh Yi Sin (CIMB):

Hi Paul, Richard and Jason, thanks for taking my questions. I have two questions here, one is on the US eCommerce operations. Given the challenges the company is still facing there, just wondering what else can be done should the management decides to retain the business? And I also understand that there could be impairment risk, would that specifically for TradeGlobal and what else should we consider in trying to assess the impairment impact? Second question is in relation to the recent lapses in service standards for public mail, I am just trying to understand what's happening there and any solution management will be coming up with?

Mr Paul Coutts (Group CEO):

Yes, so I'll handle the US ones and give you a bit more colour around that, and I'll also handle the last one. So in terms of the US, as I mentioned – thanks for your questions. The task force is there at the moment and the task force has a number of work streams that are attached to the scope of work that they are actually doing there and that scope of work covers every single part of the business in the US, from operational infrastructure through to business development, through to procurement and so on, through to products, through to pricing so it touches every part of the organisation. So as I said, we've got a process in place for that and it's very much kind of a deep dive; we have asked the task force to very clearly describe the options open to us so we can be, we've got to take a radical approach perhaps, and we need to understand what that radical approach may look like in terms of investment, return on investment, risk and so on, and also what the mitigation plan would be so it's very, very comprehensive. And again, we shouldn't get too far ahead of ourselves but that's the process that we are going through and we feel comfortable that that will give us a very clear indication of what we need to do to basically change the outcome.

I think the part around recent service quality lapses which have been well reported in media and in social media as well. I'll be honest with you, it'll be fair to state that we have very clearly failed to live up to our customers' expectations but also our expectations of ourselves. We are taking a very deep and serious look at the issues that we have faced particularly in terms of what is the root cause analysis actually telling us. We're also trying to address all those non-conformances and close the gaps of those non-conformances as quickly as we possibly can. The team is obviously working very hard on service recovery and we have set up a special hotline as well for our customers; customer contact and customer feedback. We obviously continue to monitor the media response and we're also clearing the backlog that we've also had at some of the post offices. We do have an instigated Crisis Management Task Force for postal service that's in place and we're discussing the next steps which will come out of that management task force to ensure that we overcome the current situation and get our service levels to where they need to be, so that the customer base and community more importantly – so that we can re-establish any trust that's been lost. So that's where we are focused on and I can't say it often enough, we are only as good as our last delivery and if we fail in our last delivery we have to take that personally, we have to take that seriously and we have to fix it.

Mr Richard Lai (Group CFO):

Yes and on your other question, I guess you want to know how much is the impairment and where the impairment is going to be. Short answer to you is that I don't have the information for you at this point in time, it's too early to say so. The reason why we have actually indicated that there is a risk of impairment is quite simply because the US businesses as a whole, has underperformed against our own hopes and aspiration – I should say, our turnaround plan. So obviously I think the more obvious point to that is having seriously underperformed, it is quite safe to say why are we not impairing it? I think if we don't impair it everybody will be asking us why are we not impairing it as well. The US task force is there doing a deep dive, taking a very holistic view. Arising from this we will then be able to make a very clear assessment as to what shape it might take and what form it might take going forward, and then we will be in a better position to talk about – OK, on that basis of that, what sort of value is left and what sort of impairment we need to take. So I can't even say if it's going to be just TradeGlobal or Jagged Peak or whatever because at this juncture it's just too early to comment about it. We should have a much better idea when we are announcing our next quarter results.

Ms Ngoh Yi Sin (CIMB):

OK, thank you. Just one follow-up question, what sort of reasonable time frame that we can expect to hear more from the task force for the Singapore last mile delivery and also the US businesses?

Mr Richard Lai (Group CFO):

As I have said, you will hear more from us by the next quarter results announcement.

Mr Paul Coutts (Group CEO):

Yes that's for the US and on our actions around the other piece – the postal piece you'll probably hear before you'll hear about the US, and so I'll remind you that you'll start to hear some things from our perspective in terms of what we are going to do over the course of the next few weeks and months before we get to the US announcement.

Ms Ngoh Yi Sin (CIMB):

OK, thank you so much.

Mr Jason Lim (Vice President, Investor Relations):

Operator, we just have time for one last question.

Operator:

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

Ms Rachael Tan (UBS):

Hi, just wondering in your plans to increase your market share locally, will you try to extend into different kinds of business segments such as two-hour delivery or are you just happy to try to win market share within your existing capabilities? Thanks.

Mr Paul Coutts (Group CEO):

Thanks again for the question, Rachael. Look, the first priority really for us is about fixing our current service level so that's a key focal point for us right now. In terms of continuing to grow our market share, we've certainly intended to still go forward and see significant growth in this particular area and that might mean expansion into what we might describe as other adjacencies, other areas of last mile delivery requirements and that's something that we are reviewing on an ongoing basis and it's part of our strategic focus, it's part of Winning in our Home Market. So nothing is ruled out in that particular sector and we will continue to consider all options.

Mr Jason Lim (Vice President, Investor Relations):

OK, thank you all for dialling in. I think we've reached the end of our call, just like to take this chance to wish all of you a prosperous Happy Chinese New Year ahead. Thank you.

Mr Paul Coutts (Group CEO):

Thanks everybody.

Mr Richard Lai (Group CFO):

Thank you.

End of transcript