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Domestic Freight Transportation Services

Mixed quarter for logistics sector as healthy revenue growth was offset by rise in fuel costs

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Low-base of Q2 FY2018 and hike in freight rates supported the growth in the sector

Fuel pass-through clause helped the sector pass on adverse fuel movement to a large extent

Economic growth and infrastructure development to lead logistics sector growth over the medium term

Low base and hike in freight rates supports logistics sector growth

With the impact of GST implementation and related disruptions slowing down industrial and manufacturing activity during the previous fiscal, the economic growth recovered over the last few quarters, with growth picking up to 8.2% during Q1 FY2019 and 7.1% in Q2 FY2019. Aided by increase in freight rates, stabilization of economy post GST implementation, healthy demand from consumption-driven sectors like Auto Components, Consumer Durables and FMCG, and from bulk materials like Steel and Cement, the logistics sector (as represented by a sample of 12 companies) also reported healthy growth of 14.4% during Q2 FY 2019. However, with few sectors like Passenger Vehicles reporting a slow-down in growth, growth in freight demand is likely to moderate in upcoming months. Moreover, the waning low-base effect will also impact the growth going forward.

Rise in freight rates driven by sharp rise in fuel prices supported revenue growth in the sector

The continued upward trend in freight rates since H2 FY 2018 and healthy volume growth as indicated by real GDP growth of 7.1% in Q2 FY 2019 were the key drivers of revenue growth for the logistics sector in Q2 FY 2019. Consequently, ICRA's sample of 12 leading logistics companies reported an aggregate revenue growth of 14.4% during Q2 FY 2019. With many of the large organised fleet operators having built-in fuel pass through clauses in their agreements with customers, rise diesel prices have been passed on by the transporters to a large extent. This has moderated the impact of fuel costs (40-50% of the cost structure) on the profitability of the sector and the operating profit margin of the sector declined by only 80 bps to 7.3% during Q2 FY2019 on a YoY basis. The interest coverage ratio continues to remain at healthy levels at 9.4x in the quarter.

Within the logistics sector, the demand for Full-Truck Load (FTL), Less-Than Truck Load (LTL) and Express Cargo operators has picked up on the back of healthy demand from bulk materials and consumption-driven sectors. Similarly, with companies increasingly looking at consolidating their warehouses post implementation of E-way bill, demand for warehousing services and integrated logistics players have also increased. On the other hand, the e-commerce logistics sector continues to face high competitive intensity and pricing pressure. During Q2 FY 2019, increasing share of direct port delivery (DPD) continued to have an adverse impact on the profitability of CFS players.

Indian logistics industry to grow at 8-10% over the medium term buoyed by demand and supply side positives

With buoyancy in industrial activity and consumption-led sectors expected to continue to support freight demand over the medium term, ICRA expects the Indian logistics industry to grow by 8-10% p.a. going forward. The growth would be further supported by supply-side positives including emergence of integrated logistics players, investments in infrastructure development, and capacity augmentation being undertaken by large logistics players. In addition to the increasing preference in the country for organized logistics players, on account of increased compliance requirements with GST and E-way bill implementation, the industry, over the long term, would also be shaped by ongoing trends including focus on multi-modal offerings, increased PE interest in the space, emergence of e-commerce logistics requirements, focus on warehousing and cold chain services, and increased adoption of technology to improve service offerings.



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