Indian Road Logistic Industry

Trends & Credit Outlook

September 2020

Agenda

ICRA

Executive Summary

HIGHLIGHTS

- The two-month long lockdown imposed to curb the spread of the contagion in India had a debilitating effect on the road logistics sector in Q1 FY2021, with challenges surrounding it from all fronts. While supply side constraints in terms of driver availability were prevalent, the key constraining factor was the subdued freight availability due to restrictions on economic activity.

- The situation has eased to a large extent subsequently as the restrictions were lifted, and the country entered into Unlock phases. However, the economy is only gradually recovering, and most sectors are yet to revert to their pre-pandemic levels, despite completing one quarter of unlocking the economy. Accordingly, freight availability followed suit with freight volumes improving from historic lows of April-May 2020 in subsequent months, yet to reach pre-lockdown levels.

- Going forward, given the sharp moderation in revenues in Q1 FY2021, and the gradual recovery thereafter, ICRA expects the aggregate revenue of logistics companies (in its sample) to decline by 18-20% YoY in FY2021 despite sequential pickup as the year progresses.

- Credit metrics are also expected to moderate over the near-term as profitability metrics remain under pressure. In FY2021, ICRA expects the average Debt/OPBITDA of its sample of logistics companies to weaken to ~4.1x and interest coverage ratio to average at ~2.6x as compared to 2.5x and 4.9x respectively in FY2020.

- Accordingly, ICRA's outlook on the Indian road logistics industry remains Negative, given the continuing pressures on the credit profile.

EXECUTIVE SUMMARY

ICRA

Despite sequential recovery from historic lows of Q1 FY2021, domestic freight transportation revenues expected to contract by 18-20% in FY2021 owing to disruption caused by Covid-19 pandemic and its impact on economy

- The logistics sector, which was already witnessing subdued growth momentum prior to the pandemic, was impacted significantly by the rapid spread of the Covid-19 pandemic and consequent restrictive measures implemented by the Central and the state governments to contain the disease. The extended nation-wide lockdown imposed for the major part of Q1 FY2021 had a paralysing effect on the economic activity and accordingly, the freight availability also moderated significantly. This, coupled with restrictions on cross-border movement, shortage in availability of drivers and manpower due to large-scale migration and lack of availability of return load, significantly impacted the road logistics sector during Q1 FY2021. Accordingly, aggregate revenues of ICRA's sample of logistics companies contracted sharply by 35% during the quarter. This was also visible in the generation of E-way bills, which contracted by 49% during the quarter.
- In addition to the impact on the road logistics sector, the macroeconomic slowdown and lockdown also had a bearing on rail and seaways freight traffic that primarily comprises of bulk commodities like coal, cement, iron ore and crude oil. Accordingly, rail freight and seaways freight volumes contracted by 21.3% and 19.7% YoY, respectively, in Q1 FY2021.
- However, the situation has eased to a large extent during Q2 FY2021, with the restrictions on movement and industrial activity easing during the unlock phase. Accordingly, with the economy is gradually opening up and industrial, manufacturing and construction activities resuming, freight activity has also been gradually reviving. The E-way bill and Fastag data indicate that freight volumes have been recovering sequentially as the year progressed and improved to 85% of pre-Covid levels by July 2020. This has further improved in August 2020 (87% of pre-Covid levels for E-way bill and 95% for fastag) and has potential to increase further, going forward as the country gears up for the upcoming festive season.
- However, with ongoing intermittent lockdowns in various parts of the country and continued rapid spread of the pandemic constraining the pace of recovery in industrial activity, the logistic sector (including warehousing segment) is also likely to witness a gradual roadmap to recovery. Accordingly, with the sharp slowdown witnessed in Q1 FY2021 and gradual recovery expectations, ICRA expects the revenue of its sample of logistics companies to decline by 18-20% YoY in FY2021 in the backdrop of 9.5% contraction in GDP.

EXECUTIVE SUMMARY

ICRA

Profitability and credit metrics to be constrained by challenging demand environment in the near term

- In Q1 FY2021, OPM of ICRA's sample of key logistics players contracted sharply on account of the gross under-utilisation of assets during the lockdown phase, despite the implementation of cost-saving initiatives by several companies. The impact was severe for players operating on an asset-heavy model with owned fleet and warehousing space, while those operating on an asset-light business model, fared relatively better due to lower quantum of fixed costs. Although companies aggressively engaged in cost-control initiatives on expenses related to employees, rentals and administrative heads, it was grossly insufficient to compensate for the sharp contraction in revenues. Accordingly, aggregate OPM of ICRA's sample contracted by 600 bps on a sequential basis and nearly 900 bps on a YoY basis to 0.5% (9.5% in Q1 FY2020), highlighting the significant stress on operating profitability of logistics players during this period.
- In the near-term, ICRA expects that operating profitability of the sample would improve sequentially in Q2 FY2021, supported by improvement in freight availability boosting fleet utilisation. However, it is still expected to remain muted as economic activity is yet to revive completely, and diesel prices continue to remain firm. Accordingly, ICRA expects the aggregate operating profit margins of its sample to moderate to the range of 5.0-6.0% in FY2021, as against 8.3% in FY2020.
- While the RBI's forbearance initiative and toll exemptions provided some relief in the initial days of the lockdown, but limited fleet utilisation in view of subdued freight availability had an overwhelming impact on cash flows of fleet owners. Although earnings are expected to improve as the year progresses and freight availability improves, expiry of the moratorium period and consequent re-commencement of EMI payments from September 2020 would exert pressure on their cash flows.
- Overall, ICRA expects credit metrics of logistics companies to moderate over the near term with Debt/OPBITDA to average at ~4.1x and interest coverage to average at ~2.6x in FY2021, as compared to 2.5x and 4.9x respectively in FY2020. However, deferment of near-term debt funded capex/acquisition plans by major logistics players would help cushion the impact to some extent. Nevertheless, ICRA maintains a Negative outlook on the Indian road logistics industry, given the expectations of continued pressures on the credit profile.
- Given the subdued credit outlook, negative rating actions have been taken for select entities in the sector since March 2020, which include downgrades and outlook revision owing to weaker than anticipated financial performance and expected adverse impact of the pandemic.

Contact Details

Subrata Ray

Senior Group Vice President

subrata@icraindia.com

022- 6114 3408

Shamsher Dewan

Vice President

shamsherd@icraindia.com

0124 – 4545 328

Sruthi Thomas

Senior Analyst

Sruthi.thomas@icraindia.com

0124 – 4545 822

Business Development/Media Contact Details

L. Shivakumar

Executive Vice-President

shivakumar@icraindia.com

022- 6114 3406

Jayanta Chatterjee

Executive Vice-President

jayantac@icraindia.com

080 – 4332 6401

Naznin Prodhani

Head Media & Communications

communications@icraindia.com

0124 – 4545 860

Thank You!