

THE ROAD ONCE TRAVELLED

Road Transport Economic & Benchmarking Analysis

Presented by Tim Suffield at the
Freight2020 VISION user group conference
Rydges Melbourne – Wednesday 22 March 2017



KEY FINDINGS



Demand is growing.... So why are we making less money?



The future is coming? Consolidation, Driverless Trucks, Delivery Drones, Truck Uber- Are you ready?



Should you invest outside your core competencies?



Leverage is increasing but CAPEX is down- why?



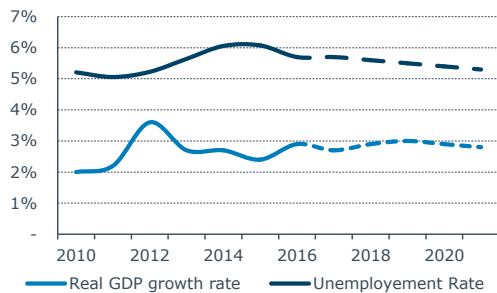
The trucking industry will require over \$3.5Bn in capital over the coming 5 years, or ~\$50k in equity per business on average

AUSTRALIAN ECONOMY

Steady as she goes...

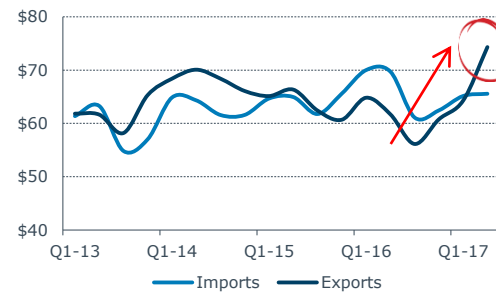
The Australian economy remains robust in-light of the slow down in mining...

GDP, UNEMPLOYMENT & BUSINESS CONFIDENCE INDEX



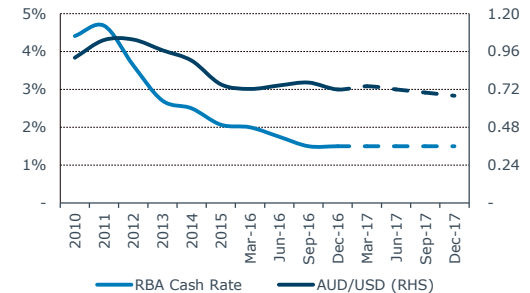
- GDP has increased since 2014 with steady growth of ~3% expected over the medium term
- Unemployment has also remained low at close to 6% and is expected to fall over the medium term

IMPORTS AND EXPORTS TRADE VALUE (A\$Bn)



- Exports (dark blue line) have increased sharply on the back of the recent commodity price rally
- Imports are expected to remain relatively steady in the medium term
- Trade activity is a key driver for trucking revenue

RBA CASH RATE & AUD/USD EXCHANGE RATE

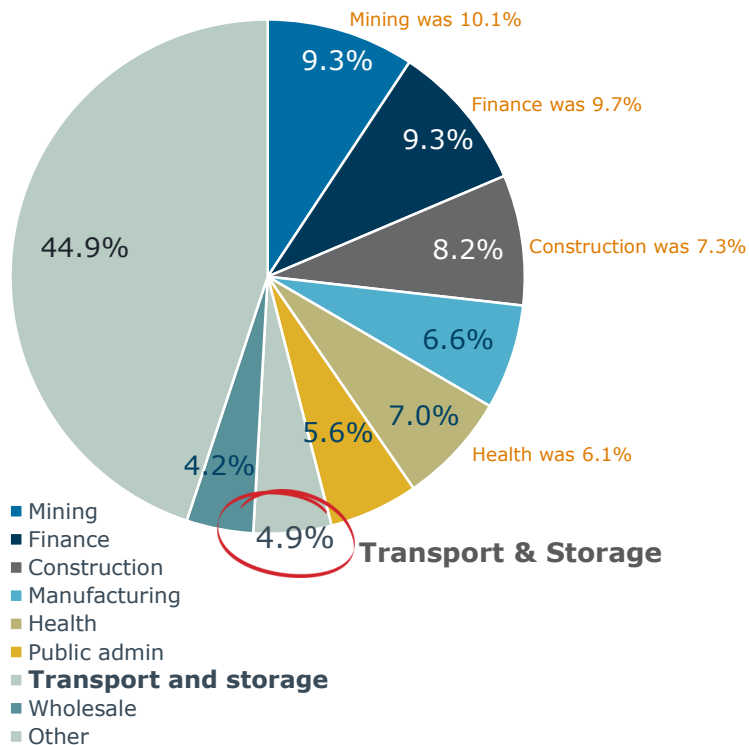


- Cash rate stable at 1.5%
- Historically low interest rate environment globally, with the USA beginning to increase rates
- Markets recently began to price in a 25bps increase over the coming 12 months
- AUD remains resilient and above market expectations

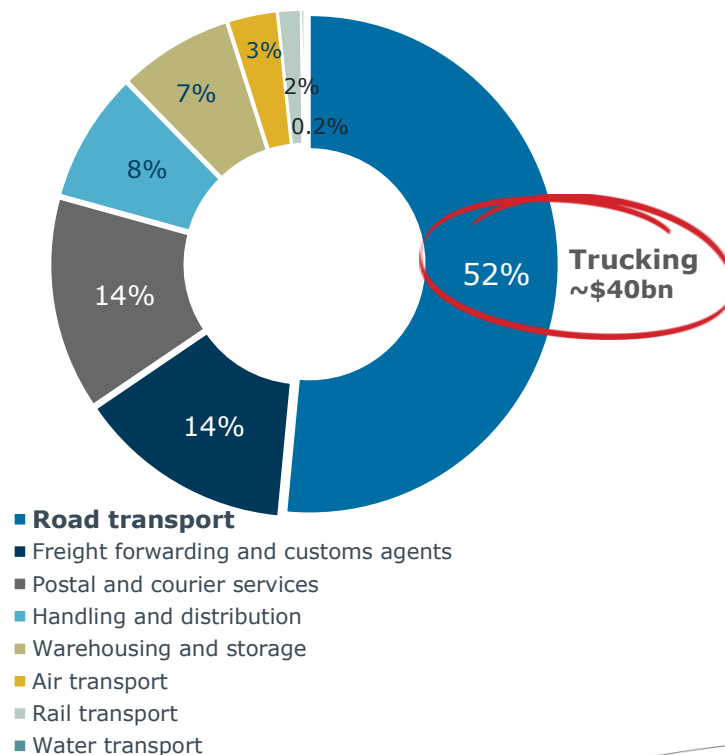
TRUCKING RELATED ECONOMIC UPDATE

Road transport is a large and significant portion of the Australian economy...

CONTRIBUTION TO GDP BY INDUSTRY



TRANSPORTATION SEGMENTATION BY SERVICE



WHO SAID TRUCKING WAS A SIMPLE BUSINESS?

What does the future hold for us?

PROS:

- ✓ **Growing** and steady demand
- ✓ Increasing merchandise imports and exports (trade liberalisation vs. Trump)
- ✓ Australia is conveniently located beside world's manufacturing hub
- ✓ No immediate trucking substitutes
- ✓ Decreasing fuel costs
- ✓ Increasingly **complex supply chains** which rely on trucking activities
- ✓ Corporate Australia continues to demand **on-time inventory management** which leads to road transport having to respond with shorter lead times
- ✓ Increasing safety
- ✓ **Innovation** - drones & driverless cars (?)

CONS:

- ✗ Intense **competition** to continue
- ✗ Profit continues to be pinched as a result of increased access, safety and licensing costs
- ✗ Fuel-surcharges coming off
- ✗ **Consolidation** of industry- who will survive?
- ✗ Skill-shortage driving increased wages
- ✗ Mining industry transitioning from development/capex to production
- ✗ Restrictions in vehicle size
- ✗ Trucking can be a political game- regulation versus efficiency versus profitability
- ✗ President Trump hindering trade?

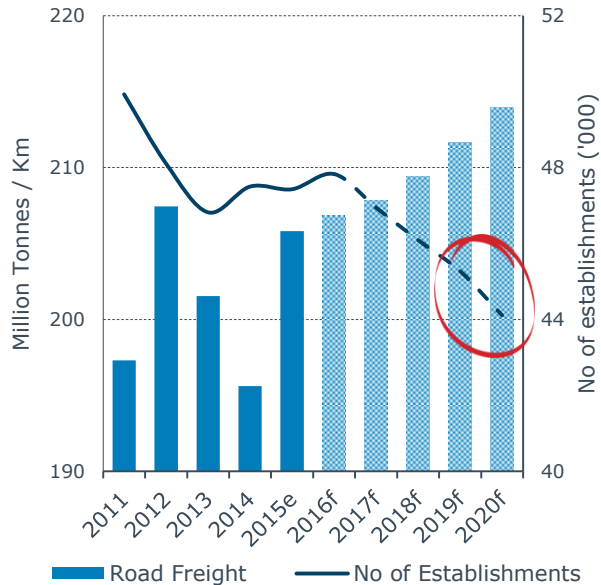


GROWTH AND EFFICIENCY

A consolidating industry grasping with efficiency gains

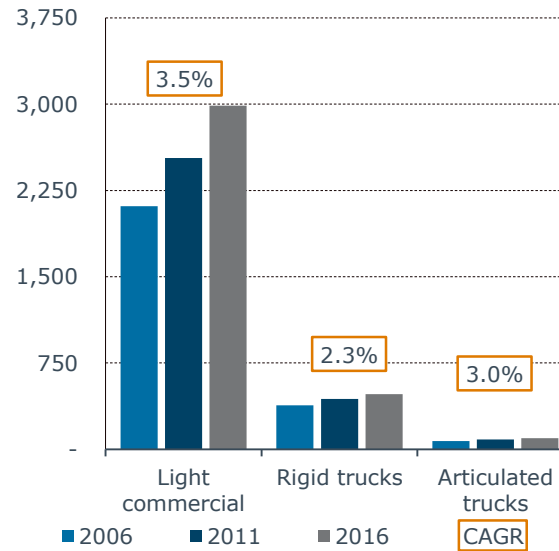
Demand for trucking services will continue to be strong, but the landscape will change...

TRUCK ROAD FREIGHT vs NUMBER OF TRUCK BUSINESSES



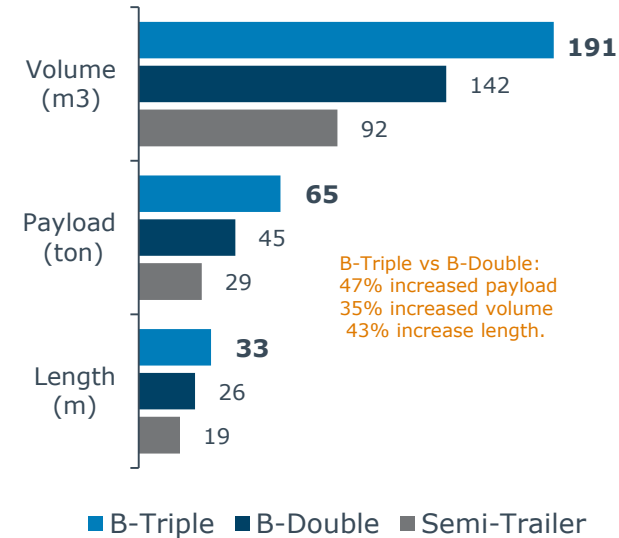
Reducing number of trucking businesses

REGISTERED VEHICLES BY TYPE¹



Articulated trucks represent only 0.5% of registered vehicles in Australia

ARTICULATED PRODUCTIVITY COMPARISON



Where will the next round of efficiencies come from? Safety regulations & road network considerations

Note 1: Vehicle registrations are as of January month each year
Sources: BMI, ANZ Analysis, BITRE- yearbook statistics, Transport NSW & IBIS World

DEEP DIVE ANALYSIS

Setting the scene

ANZ analysed **30 Australian trucking companies** which were categorised as follows...

1

General Cargo

57% of sample
17 companies

Transporting goods of a general nature, which do not require specialist equipment or regulatory approvals

VS.

Specialised Cargo

43% of sample
13 companies

Focus on cargo which is more difficult to transport such as hazardous, heavy and refrigerated loads

2

Truck-owners

70% of sample
21 companies

Companies that have invested in owning trucks. Larger wages compared to sub-contractor expenses

VS.

Sub-contractor

30% of sample
9 companies

Large sub-contracting requirements and expenses. Relatively small plant and equipment

3

Private

87% of sample
26 companies

Road transport companies which are not listed on the ASX

VS.

Public

13% of sample
4 companies

Public companies which are listed on the ASX with access to public equity raisings

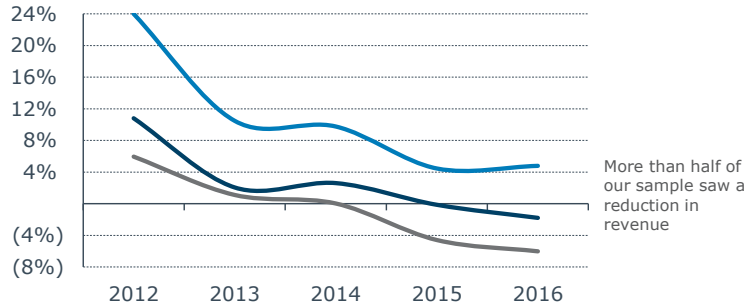
ANZ's sample of 30 companies generate sales over \$11bn, representing ~27% of the industry

TOTAL SAMPLE OVERVIEW

Concentrated competition hurting revenue and returns...

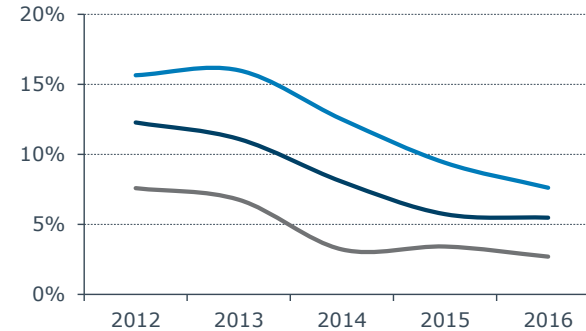
Increasing price competition causing revenue and margin compression

REVENUE GROWTH



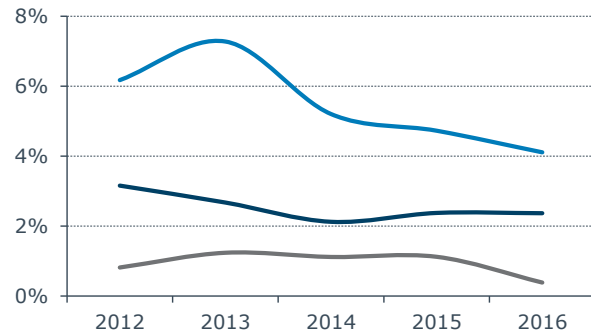
Only top quartile performers were able to increase revenue growth, whilst most of the industry saw a reduction in revenue

EBITDA MARGIN



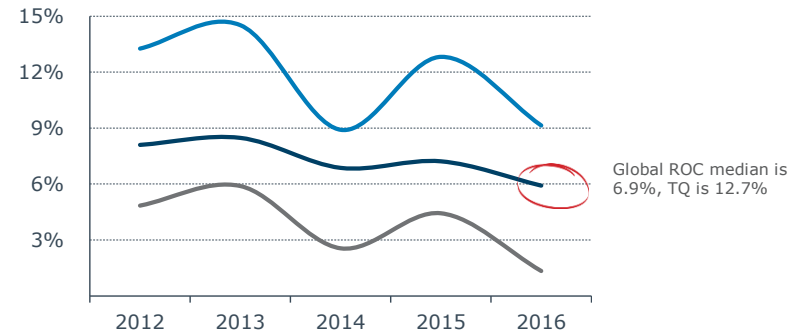
Continuing theme of margin compression, with top quartile performers reducing from 9.4% to 7.6%

NET INCOME (PROFIT) MARGIN



The median net income margin held steady at 2.4%. Top quartile performance continued to decline with a drop from 4.7% to 4.1%

RETURN ON CAPITAL



In line with revenue and net income, the Return on capital has reduced across all quartiles

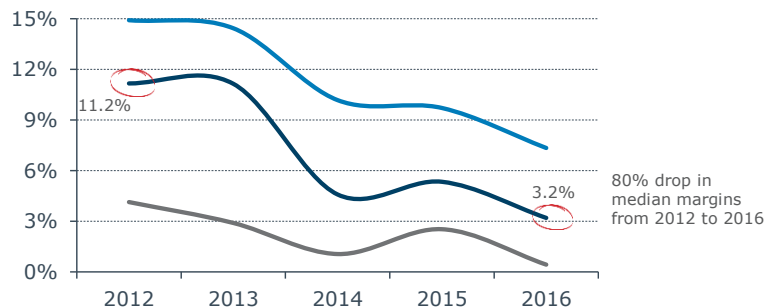
— Top Quartile — Median — Bottom Quartile

GENERAL VS SPECIALISED CARGO

Does it pay to invest into specialised cargo transport?

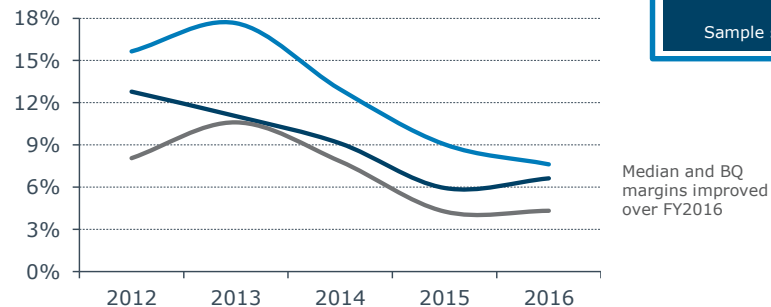
Companies that transport general cargo have seen a drop in margins and returns

GENERAL CARGO : EBITDA Margin



All quartiles have decreased with the median general cargo operator's EBITDA margin reducing from 5.3% to 3.2%

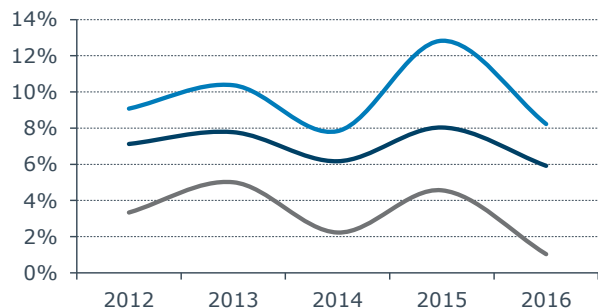
SPECIALISED : EBITDA Margin



Specialised cargo EBITDA margins beginning to converge slightly above 6%

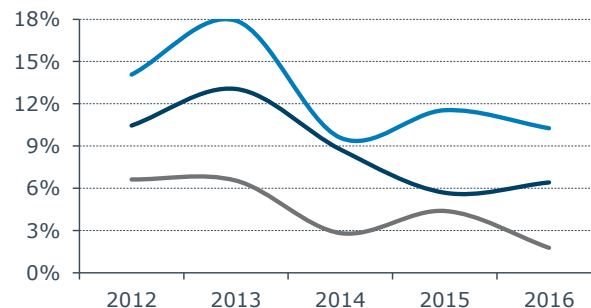
GENERAL CARGO Sample size 17
VS.
SPECIALISED CARGO Sample size 13

GENERAL CARGO : Return on capital



In line with General cargo operators' EBITDA margin, return on capital across all quartiles has sharply reduced

SPECIALISED CARGO : Return on capital



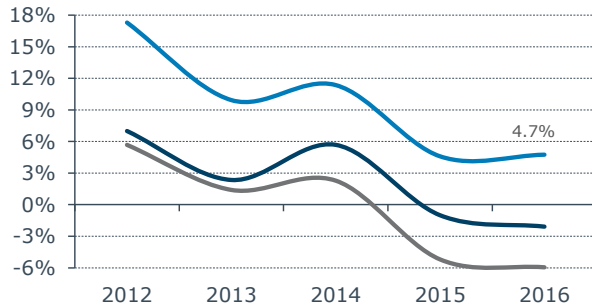
Return on capital varies from bottom quartile at 1.8% to top quartile performance at 10.3%

TRUCK OWNING BUSINESSES VS. SUB-CONTRACTOR RELIANT

To sub-contract or not??

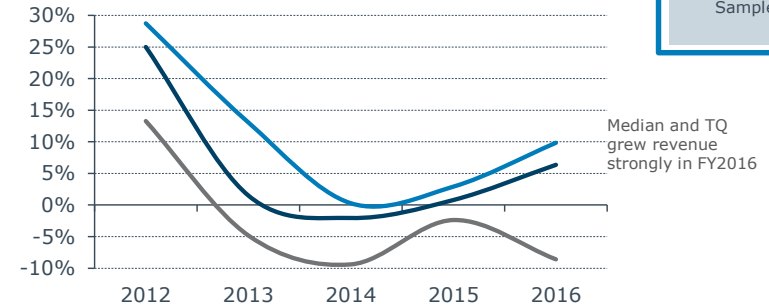
In general, businesses that largely employ sub-contractors are beginning to increase market share by undercutting the market

TRUCK OWNERS : Revenue growth



Businesses that invest in their own trucks and people are experiencing revenue compression

SUB-CONTRACTORS : Rev. growth



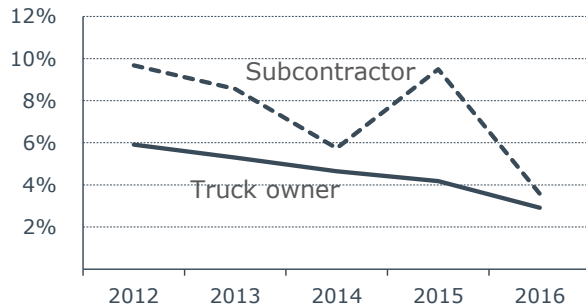
Most businesses that heavily rely on sub-contractors are seeing growth in revenue

TRUCK OWNERS
Sample size 21

VS.

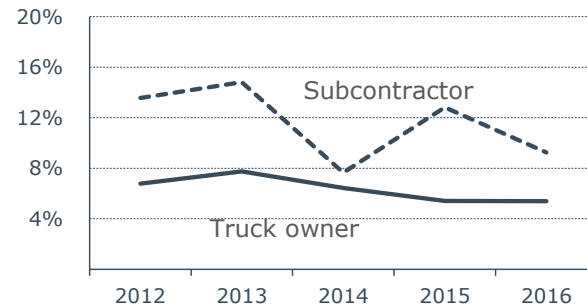
SUB-CONTRACTOS
Sample size 9

EBIT margin (median)



Sub-contracting business saw a noticeable drop in margins over the past 12 months

Return on capital (median)



Truck owners have higher capital requirements and as a result often see lower returns on capital

PRIVATE COMPANIES VS. PUBLIC COMPANIES

Private companies typically have more pressure to grow revenue...

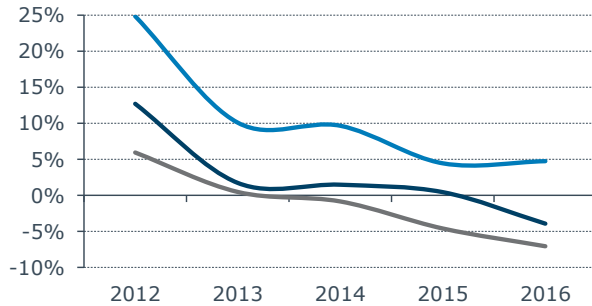
ASX listed trucking companies have seen increasing revenue, however their return on capital has suffered due to margin contraction

PRIVATE COMPANIES
Sample size 26

VS.

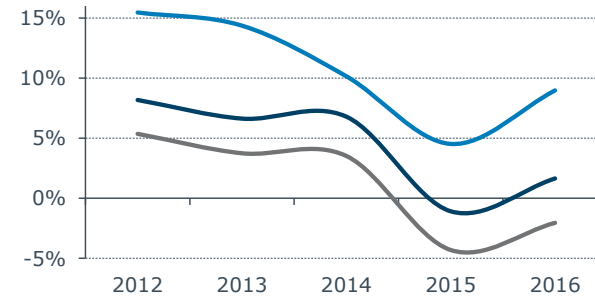
PUBLIC COMPANIES
Sample size 4

PRIVATE : Revenue growth



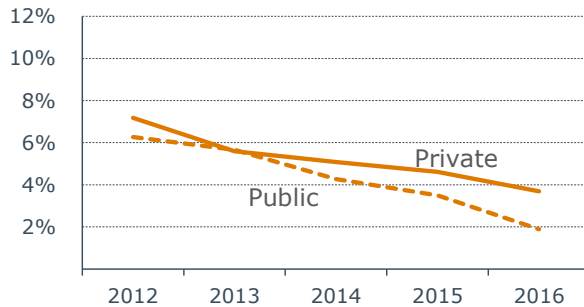
The median private business saw a drop in revenue in FY16, whilst the top quartile performers experienced growth above 5%

PUBLIC : Revenue growth



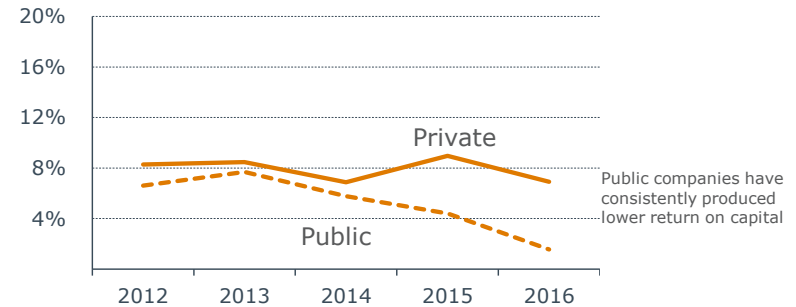
All quartiles of public trucking companies experienced an uptick in revenue, with top quartile growth close to 10%

EBIT margin (median)



Margins continued to deteriorate for both Private and Public companies, however public companies saw a larger decline to a median of 1.9%

Return on capital (median)



Similar to EBIT margins, return on capital dropped across both Private and Public companies

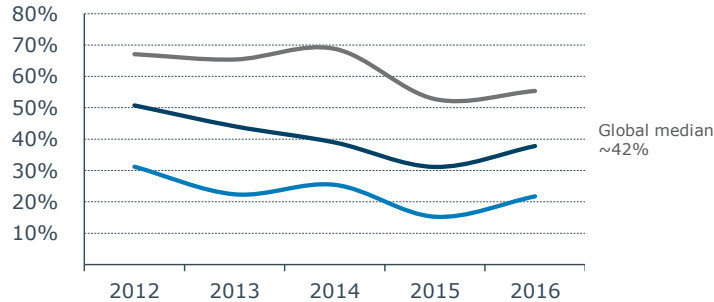
Public companies have consistently produced lower return on capital

TOTAL SAMPLE - LEVERAGE & CAPEX

Worrying trends will drive further separation between the successful and stragglers

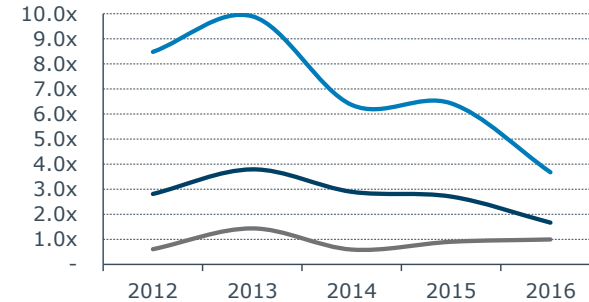
The national average fleet continues to age (at record levels) whilst companies are increasingly relying on debt.... this trend is not sustainable!

Debt / Capital



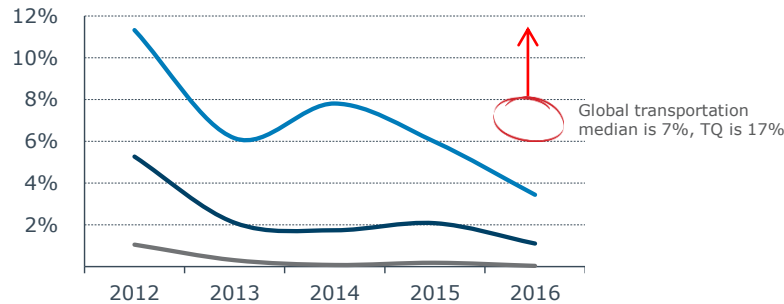
Debt/Capital has increased across all quartiles with the median increasing from 32% to 38%

Debt Service Coverage Ratio (DSCR)



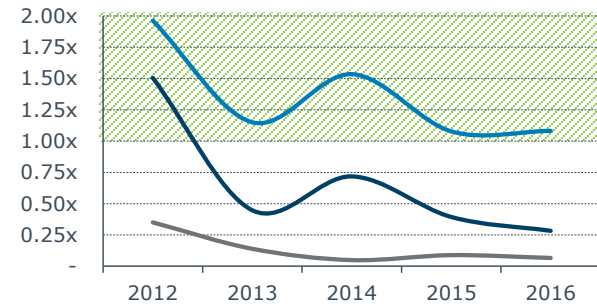
DSCR measures the ability of a business to service and meet debt repayments. A 1x metric results in the business only just meeting debt obligations

Capex / Sales



Capex in the industry has continued to contract, leading to an average national fleet age of over 14 years

Capex / Depreciation



Capex/Depreciation is a proxy for investment. Above 1x indicates a growing asset base

ROAD TRANSPORT NOW & IN THE FUTURE...

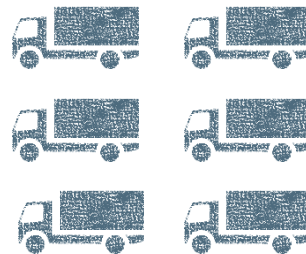
Trucking is the largest and the most critical component of the transport and logistics industry in Australia...

What about trucking in 20 years?



\$85bn

~~\$40bn~~
REVENUE



33k

~~41k~~ **BUSINESSES**
Small business ~ 50%



\$17bn

~~\$8bn~~ **WAGES**
20% of revenue
Av. Salary=\$56k



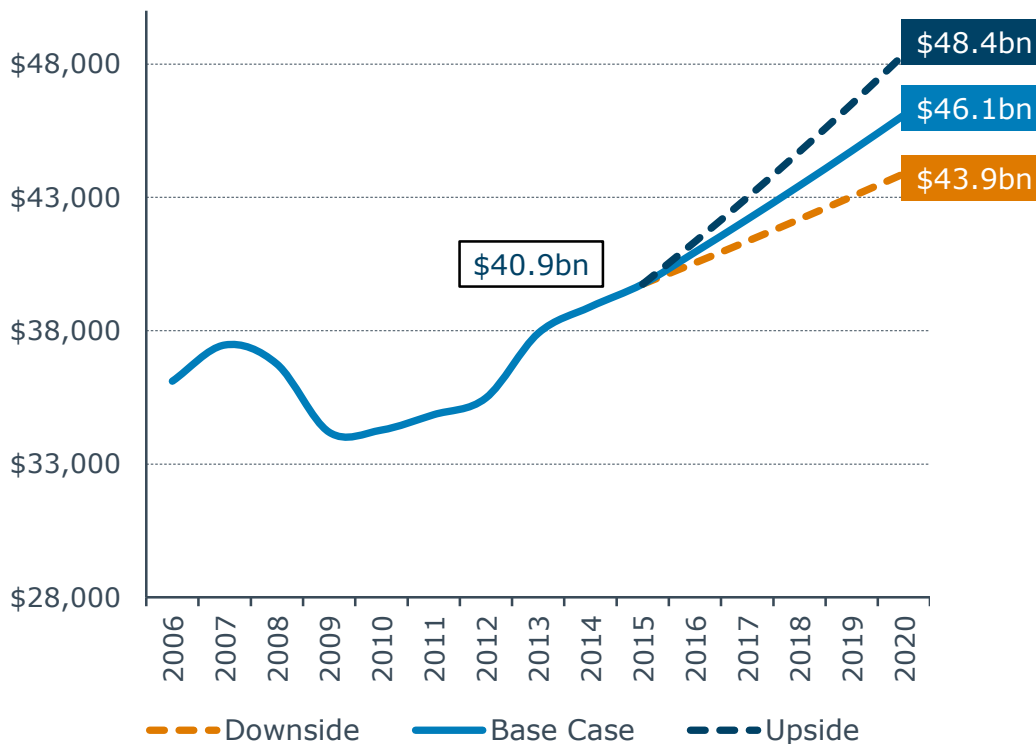
\$12bn

~~over \$6bn~~
FUEL: 10% to 30% of revenue

Sources: Bureau of Infrastructure, IMF, IBIS World, ANZ analysis

IMPENDING FUNDING GAP

ANZ analysis indicates the Trucking Industry will require in excess of \$3.5bn over the coming 5 years to meet expected demand...



UPSIDE SCENARIO \$4.8bn in Capital
Debt \$2.2bn & Equity \$2.6bn
Equity per operator = \$68k

BASE CASE \$3.5Bn in Capital
Debt \$1.6Bn & Equity \$1.9Bn
Equity per operator = \$49k

DOWNSIDE CASE \$2.3Bn in Capital
Debt \$1.0Bn & Equity \$1.3Bn
Equity per operator = \$34k

Sources: Bureau of Infrastructure, IMF, IBIS World, ANZ analysis
Assumptions: Each \$1 of incremental revenue will require 0.56c of capital (Asset Turnover 5 yr av. = 1.8x)
Debt/Capital remains at 5 year average ~45%.
2020 # of business = 38,354

HOW CAN ANZ HELP?

ANZ is Australia and NZ's leading financier to the transport Industry and we are here to help...

ASSET FINANCE SOLUTIONS:

ANZ has market-leading equipment finance capabilities, including interest rate management and cost centre reporting through its recently-deployed Global Asset Finance system

WORKING CAPITAL SOLUTIONS:

A variety of working capital solutions are available either to meet short term funding gaps, or improve the efficiency of your collection and payment practices

FIXED INTEREST RATE SOLUTIONS:

Long term interest rates are at record low levels which provide an opportunity to lock in or restructure existing swaps

How exposed is your business when interest rates rise?

ACQUISITION FINANCE:

As the industry continues to consolidate, how prepared is your business to act on such opportunities?



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