

Aramex

Equity Research Update

Sector - Transportation

Express growth still has legs; Upgrade to 'Outperform'

Aramex remains the best listed play on GCC's growing Ecommerce market

We upgrade Aramex to 'Outperform' and forecast group EPS to grow at a CAGR of 10.7% from AED 0.30/share in 2018 to AED 0.46/share in 2021. Although the ecommerce market in the GCC is not expected to grow at the breakneck pace achieved in the recent past, the industry's +17% CAGR expected over 2018-22 should translate into revenue growth for logistics partners such as Aramex. The company's cost cutting initiatives and technology advancement roadmap have paid off and is expected to shield margins amidst tighter competition in the market. Moreover, available FOL headroom brings liquidity back into the stock, and should provide support for Aramex's share price going forward.

Express segments growth to sustain despite competition

Express growth drivers have changed, as customer segments such as large regional retail family groups and direct international brands have become more stable sources of revenue growth. On the other hand, higher service level demands from e-tailer customers, newer competitors and migration risks are likely to intensify competition, and lead to lower margins, in our view. Nevertheless, KAMCO Research expects revenue growth for Aramex's Express segments to continue, albeit at a slower pace of 7.1% CAGR over 2018-2021 to reach AED 4.08 Bn in 2021, despite competition. For Domestic Express, the sale of India operations would result in lower revenues (~USD 17-18 Mn), but margins would improve going forward, as the business in India incurred annual losses of USD 3-4 Mn.

B2B segments back in focus; Logistics segment contribution to jump

Aramex is upgrading its service levels to compete further on its B2B business lines, with substantial improvement and investments being made on the last mile delivery services, clearance gateways, etc. B2B freight forwarding and contract logistics side investments were made by Aramex, and new verticals expertise and service levels were targeted for 2019 like aerospace, pharma, healthcare, automotive segments. The Logistics segment outlook remains strong in terms of revenues and margins, and the company's acquisition of the new warehouse designed for fashion ecommerce is incrementally positive, and would lead to a significant jump in revenues, and improve margins as well.

Valuation & Risks - TP of AED 5.90/share

Our revised target price of AED 5.90/share is based on a blend of DCF and relative valuation. Aramex currently trades at a FY19 P/E of 11.0x (Cons.), a 10.4% discount to its historic 12M forward P/E, and trades at a 43% discount to global peer group median. **Key Downside risks:** 1) Higher competition driving lower pricing and volumes from e-tailers, impacting express revenues 2) Slowdown in global & GCC economic growth and trade impacting B2B segments 3) Lower consumer confidence leading to lower B2C volumes 4) FX related risks

Key Financials	2017	2018	2019E	2020E	2021E
Revenue (AED Mn)	4,721	5,086	5,402	5,774	6,147
GP Margins (%)	54.2%	54.5%	54.7%	55.1%	55.7%
EBITDA (AED Mn)	656	804	844	920	1,005
EPS (AED)	0.30	0.34	0.38	0.42	0.46
Consensus EPS (AED)	0.30	0.34	0.39	0.43	0.48
PE (x)	16.5	12.3	12.4	11.5	10.5
EV/EBITDA (x)	11.6	8.0	8.3	7.6	7.0
Div. yield (%)	2.3%	3.4%	4.4%	4.8%	5.2%

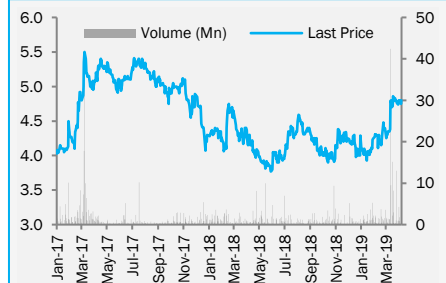
Sources: KAMCO Research, and Aramex

Outperform

CMP 09-Apr-19: AED 4.77

Target Price: AED 5.90

Upside/Downside: +23.7%



Price Perf.	1M	3M	12M
Absolute	9.7%	16.3%	10.9%
Relative	1.8%	6.2%	20.2%

Stock Data

Bloomberg Ticker	ARMX.DB
Reuters Ticker	ARMX.DU
Last Price (AED)	4.77
MCap (AED Mn)	6,984
MCap (USD Mn)	1,903
EV (AED Mn)	7,022
Stock Performance - YTD (%)	10.7%
PE - 2019E (x)	12.4
EV/EBITDA - 2019E (x)	8.3
Dividend yield - 2019E (%)	4.4%
52-Week Range (AED)	3.72 / 5.01

Sources: KAMCO Research & Bloomberg

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Valuation and Risks

Target price raised to AED 5.90/share; Upgrade to 'Outperform'

We revisited our model and our investment case after Q4-18 results and post speaking to Aramex's management. We now forecast the group EPS of Aramex to grow by 10.7% CAGR from AED 0.30/share in 2018 to reach AED 0.46/share in 2021 (2019: AED 0.38/share, 2020E: AED 0.43/share). Our EPS growth forecasts are driven by revenue growth from the ecommerce-led Express segments, strong B2B focus and initiatives targeting newer client verticals, and cost efficiency gains. Our revised TP of AED 5.90/share is based on a blend of DCF and relative valuation.

Weighted Average Fair Value

	Fair value per share (AED)	Weight (%)	Weighted Value (AED)
DCF	5.50	70%	3.85
Relative Valuation	6.83	30%	2.05
Weighted Average Fair Value per Share			5.90
Current market price			4.77
Upside/Downside			23.7%

Sources: KAMCO Research and Bloomberg

We upgrade Aramex to 'Outperform', as the company remains the best listed play on GCC's growing ecommerce market. The stock appears undervalued based on our DCF and relative valuation methodologies, warranting the rating change. In our DCF valuation, we have assumed a terminal growth rate of 2.0%, and average WACC of 9.8% over our forecast period, which we believe adequately represents the sustainable long-term growth rate for the company, given the nature of technological advancement and disruption in the sector. For the terminal value, we have assumed a return on new investment capital (RONIC) that is comparable to the terminal year WACC.

Despite the run-up in the stock (+10.7% YTD), Aramex appears cheap on a relative basis and is currently trading at a consensus 12M forward P/E of 11.0x, which represents a 10.4% discount to its historic trading average. Moreover, the stock trades at a 43% discount to global peer group median (FY19 P/E: 19.3x, see page 10), which in our view is excessive, given the company's growth potential.

FOL headroom gives trading liquidity much needed breathing space

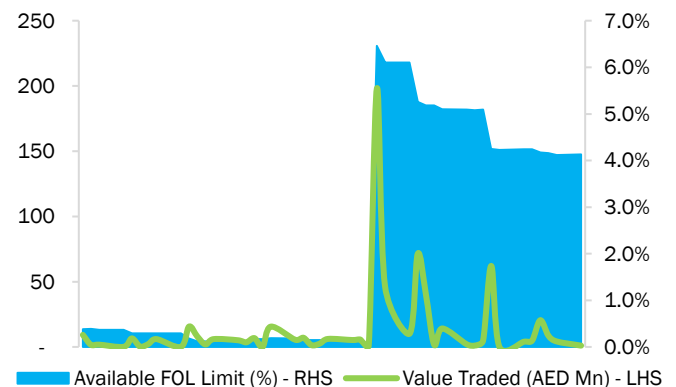
Following Aramex's divestment of its Australian JV, Australia Post sold around 10% of its stake in Aramex. The stake sale freed up available foreign ownership in the stock (maximum foreign ownership limit of 49%).

Aramex 12M Forward P/E



Sources: Bloomberg, KAMCO Research

Aramex Available FOL Limit (%) & Trading Activity



Sources: DFM, KAMCO Research, Available FOL Limit is based on end of day estimates on the DFM exchange

Trading activity on the stock has picked up since the stake sale, a trend we expect to see continue until the remaining FOL (~4.1%) is bought by foreign investors. Higher trading activity should alleviate the near-term liquidity concerns of institutional investors and should provide support for Aramex's share price going forward, in our view.

Downside risks to our rating & forecasts include:

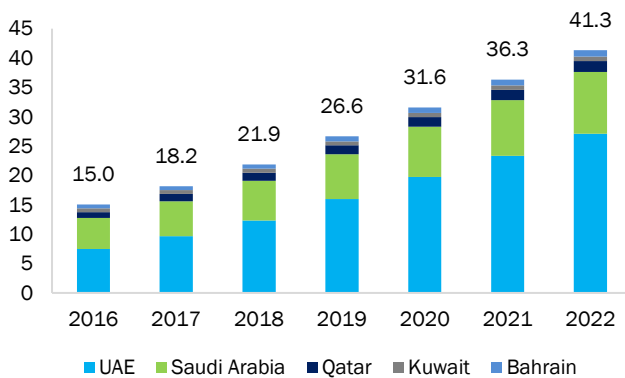
- Higher competition and resultant lower volumes and pricing from ecommerce retailers impacting express revenues
- Slowdown in global & GCC economic growth and trade, driving lower growth for B2B segments such as the freight forwarding industry
- Lower consumer confidence, leading to lower than expected B2C volumes
- FX related risks

Investment Thesis

E-commerce industry growth in the GCC still has room for growth

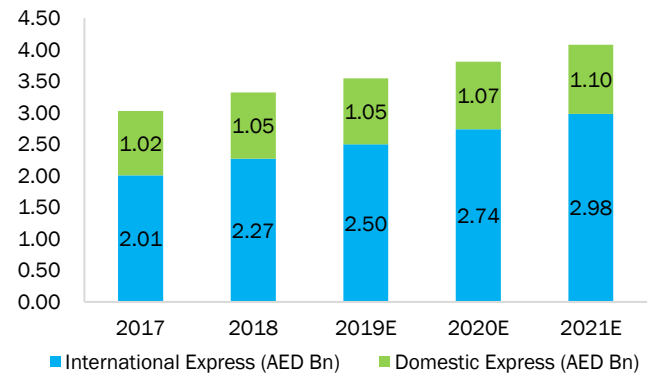
The main drivers for Aramex's revenue and earnings growth have been the significant growth from their high-margin express segments. Revenues for International Express and Domestic Express combined have almost doubled over 2013-2018 to reach AED 3.3 Bn in 2018, and contributed over 65% of group revenues, while margins for International Express (2018: ~65%) and Domestic Express (2018: ~51%) have remained high. Ecommerce remains the main catalyst of growth for these segments and contributes ~40% of the combined revenues of these segments. Ecommerce activity in the GCC rose significantly with growth estimated at above 20% per annum up until 2018. Although slowing marginally, ecommerce growth in the GCC is expected to continue at a CAGR of +17% over 2018-2022, as per Fitch Solutions. UAE and Saudi Arabia are expected to remain the major markets, growing at 21% CAGR and 11% CAGR respectively over 2018-22, and contributing a combined total of over 90% of the ecommerce sales in the region.

GCC e-commerce trends 2016-2022 (USD Bn)



Sources: Fitch Solutions, KAMCO Research

Express revenue contribution (2017-2021)



Sources: KAMCO Research, Aramex

Express segments growth to sustain, but margins compress from competition

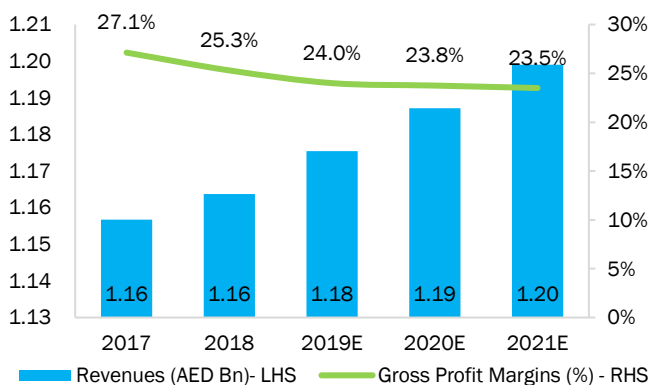
We expect revenue growth for Aramex's express segments to continue, albeit at a slower pace of 7.1% CAGR over 2018-2021 to reach AED 4.08 Bn in 2021, despite competition in the ecommerce market. The ecommerce market is witnessing competition, especially in the e-tailing space, as retailers in the region attempt to retain market share and offer excessive discounts to combat higher ecommerce purchases. Moreover, significant growth for logistics providers such as Aramex in the past came from e-tailers such as Amazon, Souq and Ali Express, as logistics costs for e-tailers typically account for around 20% of online retail revenues. Loyalty from such customers however remains low and their business models keep evolving, as they look to control logistics infrastructure and even consider owning their own last mile delivery services, as per Aramex. Higher service level demands from such customers would contribute to lower margins as well in our view. However, revenue growth and margins from customer segments such as large regional retail family groups and direct international brands are more stable in nature, would sustain and contribute to higher International Express and Domestic Express Revenues.

As a result, we forecast International Express revenues to grow at 9.5% CAGR over 2018-2022 to reach AED 2.98 Bn (2018: AED 2.27 Bn) while GP margins are expected to compress by around 100 bps in 2021 (2018: 65%). For Domestic Express, growth, the sale of India operations would result in lower revenues (~USD 17-18 Mn), but margins would improve going forward, as the India operations was loss making (USD 3-4 Mn). Accordingly, we expect Domestic Express revenues to reach around AED 1.10 Bn in 2021 (2018: AED: 1.02 Bn), while GP margins remain broadly stable at around 48%-49% over 2018-2021.

B2B segments back in focus; Logistics segment to post double digit growth

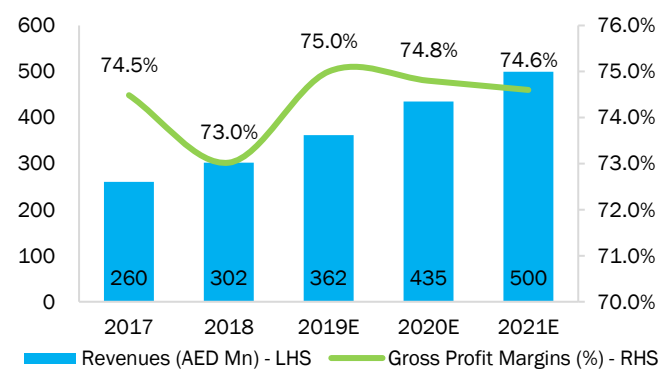
Aramex is upgrading its service levels to compete further on its B2B business lines, with substantial improvement and investments being made on the last mile delivery services, clearance gateways, etc. B2B freight forwarding and contract logistics side investments were made by Aramex, and new verticals expertise and service levels were targeted for 2019 like aerospace, pharma, healthcare, automotive segments. The company's expertise in handling large O&G sector customers should prove helpful in deriving revenues from these newer verticals in our view, however we expect all the upgrades in service delivery lines to impact margins marginally, which are reflected in our forecasts.

Freight forwarding revenues and gross margins



Sources: Aramex, KAMCO Research

Logistics revenues and gross profit margins



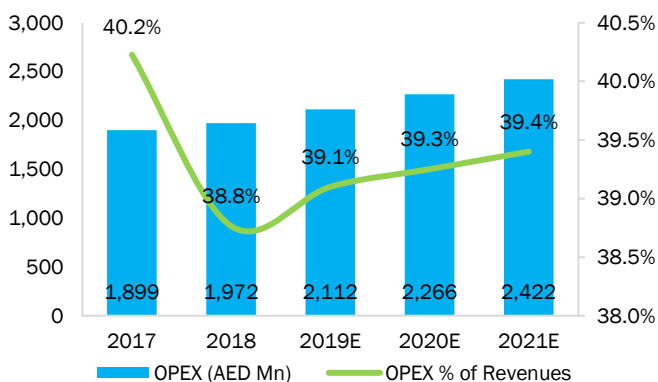
Sources: Aramex, KAMCO Research

The Logistics segment outlook remains strong in terms of revenues and margins. In Dubai logistics city, the 100,000 sq.m warehouse owned by Aramex is operating at full capacity utilization, and the market remains extremely tight in terms of available space. Moreover, the company's acquisition of the new warehouse of 15,000 sq.m, designed for Ecommerce and addressing the fashion industry is a significant positive, as per Aramex. The design of the new warehouse is expected to free up at least 40%-50% of the existing capacity, and lead to a significant jump in revenues, and improve margins as well. We therefore expect the Logistics segment revenues to grow at a CAGR of 18% over 2018-21 to AED 500 Mn, while margins should improve by from 73% in 2018 to over 74.5% over 2019-2021.

Cost cutting measures paid off; IFRS 16 impact on income statement minimal

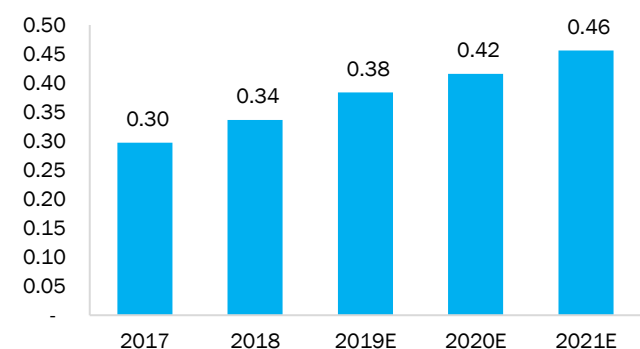
The restructuring and cost cutting initiatives undertaken by Aramex in 2018 paid off well and led to savings of over 140 bps of margins. However, similar gains are unlikely in 2019, as progress towards higher service levels, and higher B2B focus would result in limited overall cost savings.

Aramex operating expenses progression



Sources: Aramex, KAMCO Research

Aramex EPS forecasts (AED)



Sources: Aramex, KAMCO Research

Aramex in their Q4-18 conference call, mentioned that the focus on the streamlining of processes, realizing synergies and digital transformation would continue over the next 12-15 months.

The implementation of IFRS 16 – the accounting standard for leases, which came into effect from 1 January 2019 will have a significant impact on the balance sheet of Aramex, given the company's asset light business model. Income statement impact will be minimal, as the operating lease expense would be split into depreciation and interest expense. Nevertheless, our model and estimates do not incorporate the IFRS 16 changes yet, and we will wait for Q1-19, for more guidance on the changes.

Based on our current forecasts, we expect the group EPS of Aramex to grow by 10.7% CAGR from AED 0.30/share in 2018 to AED 0.46/share in 2021, driven by revenue growth from the ecommerce-led Express segments, strong B2B focus and initiatives targeting newer client verticals, and cost efficiency gains.

Guidance & Financial Forecasts

2019 Outlook – KAMCO Research forecasts 6.2% revenue growth

Aramex released specific revenue guidance for 2019 at the group level and for individual segments. The management guided for a double-digit increase in 2019 revenues. Our new forecasts are more conservative than management guidance, as we expect group revenues to grow by 6.2% y-o-y in 2019. Our detailed forecasts, assumptions and comparison of group level estimates vs. consensus are given below:

2019 KAMCO Forecasts vs. Aramex Guidance					
Revenues (AED Mn)	2018	2019 Guidance: Aramex	KAMCO Research Forecasts: 2019	Y-o-Y (%)	KAMCO Research Forecasts Rationale
Segmental					
International Express	2,273	Double-digit growth	2,500	10%	Double digit growth in GCC's e-commerce industry along with steady growth from direct international brands shipping to the region should drive growth. E-tailing related express volumes will grow despite competition
Freight Forwarding	1,164	Single-digit decrease	1,175	1%	B2B focus augurs well, but more visibility needed for acquisition of new contracts in pharma, healthcare, aerospace industries. Pricing pressure still prevalent.
Domestic Express	1,051	Single-digit growth	1,046	-0.5%	Exit from India operations will normalize growth given revenue contribution of around USD 17-18 Mn.
Logistics	302	Single-digit growth	362	12%	Acquisition of new warehouse, tailored for fashion ecommerce will lead to double digit revenue growth, in an already tight market.
Other	296	Single-digit growth	319	7.5%	In-line with management guidance
Group Revenues	5,086	Double-digit growth	5,402	6.2%	Express revenues would continue to buoy group revenues and register a high single digit y-o-y growth for 2017

Source: Aramex, KAMCO Research

2019 & 2020 Forecasts - KAMCO Research vs. Consensus Estimates						
Aramex - Group	2019			2020		
	KAMCO Estimates	Consensus	KAMCO vs. Consensus	KAMCO Estimates	Consensus	KAMCO vs. Consensus
Revenues (AED Mn)	5,402	5,545	-2.6%	5,774	5,969	-3.3%
Gross Margins (%)	54.7%	53.7%	0.9%	55.1%	53.4%	1.7%
EBITDA (AED Mn)	844	852	-0.9%	920	913	0.7%
Net Income* (AED Mn)	562	581	-3.2%	609	624	-2.3%
EPS*(AED/share)	0.38	0.39	-1.1%	0.42	0.43	-3.9%

Source: Aramex, KAMCO Research, *Net Income and *EPS are before any adjustments to maintain parity with consensus estimates

Aramex Financials						
Balance Sheet (AED Mn)	2016	2017	2018	2019E	2020E	2021E
Assets						
Cash and cash equivalents	701	728	837	1,200	1,625	2,102
Receivables	742	934	1,141	1,199	1,282	1,364
Total current assets	1,655	1,911	2,330	2,772	3,305	3,891
Net property, plant and equipment	840	912	950	982	1,013	1,042
Goodwill	1,139	1,164	1,125	1,125	1,125	1,125
Other assets	395	417	300	301	302	303
Total assets	4,029	4,404	4,704	5,179	5,744	6,360
Liabilities						
Current Liabilities	1,122	1,368	1,817	1,507	1,618	1,730
Long-term debt	362	293	219	667	754	850
Other Liabilities	271	224	237	187	191	195
Total liabilities	1,755	1,885	2,272	2,362	2,563	2,776
Shareholders' Equity						
Share capital	1,464	1,464	1,464	1,464	1,464	1,464
Retained earnings	958	1,113	1,317	1,637	1,937	2,270
Minority Interest	9	19	22	37	40	43
Other Equity	-156	-77	-371	-321	-260	-193
Total Shareholders Equity	2,275	2,519	2,432	2,817	3,181	3,584
Total liabilities and equity	4,029	4,404	4,704	5,179	5,744	6,360
Income Statement (AED Mn)	2016	2017	2018	2019E	2020E	2021E
Revenue	4,343	4,721	5,086	5,402	5,774	6,147
Cost of goods sold	(1,906)	(2,161)	(2,315)	(2,450)	(2,592)	(2,725)
Gross profit	2,437	2,560	2,771	2,953	3,182	3,423
General and administrative expenses	(1,085)	(1,118)	(1,121)	(1,194)	(1,282)	(1,371)
Other operating expenses	(787)	(781)	(850)	(918)	(984)	(1,051)
Other operational Income/Loss	(1.4)	(4)	4	4	4	4
EBITDA	564	656	804	844	920	1,005
Depreciation and amortization	(104)	(109)	(121)	(127)	(139)	(152)
EBIT	460	548	683	717	781	853
Finance costs	(27.2)	(24.7)	(27.6)	(22.4)	(32.0)	(36.9)
Interest/investment income	11.5	7.9	9.0	11.2	17.0	24.2
Other Income/Loss	20.2	6.5	-39.7	6.4	6.7	6.9
Net profit before taxes	464	537	624	712	773	847
Provision for Income Taxes	(61)	(81)	(100)	(114)	(124)	(136)
Net profit after taxes	403	456	524	598	649	711
Minority interest	(26)	(20)	(32)	(37)	(40)	(43)
Net profit attributable to parent	378	436	492	562	609	668
EPS (AED)	0.26	0.30	0.34	0.38	0.42	0.46
Cash Flow (AED Mn)	2016	2017	2018	2019E	2020E	2021E
Net cash from operating activities	612.8	508.2	494.5	774.5	799.2	873.9
Net cash (used in) from investing activities	(493.0)	(183.7)	(91.3)	(190.1)	(150.2)	(155.5)
Net cash from (used in) financing activities	(70.1)	(333.2)	(310.1)	(221.2)	(223.5)	(241.4)
Change in cash and cash equivalents	49.7	(8.7)	93.0	363.1	425.4	477.1
FX and other adjustments	(55.6)	35.1	16.0			
Cash at the end of the year	701	728	837	1,200	1,625	2,102

Source : KAMCO Research and Aramex

Key Financial Ratios						
Key Ratios	2016	2017	2018	2019E	2020E	2021E
Profitability Ratios						
Return on Average Assets (%)	10.3%	10.3%	10.8%	11.4%	11.2%	11.0%
Return on Average Equity (%)	17.4%	18.3%	20.1%	21.7%	20.6%	20.0%
ROIC (%)	18.3%	18.8%	23.2%	24.3%	25.9%	27.8%
Margins						
Gross profit margin (%)	56.1%	54.2%	54.5%	54.7%	55.1%	55.7%
EBITDA margin (%)	13.0%	13.9%	15.8%	15.6%	15.9%	16.3%
EBIT margin (%)	10.6%	11.6%	13.4%	13.3%	13.5%	13.9%
Net profit margin (%)	8.9%	9.2%	9.7%	10.4%	10.6%	10.9%
Market Data and Valuation Ratios						
Market Capitalization (AED Mn)	5,148	7,184	6,042	6,984	6,984	6,984
Enterprise Value (AED Mn)	5,627	7,640	6,399	7,022	7,022	7,022
Earnings Per Share (AED)	0.26	0.30	0.34	0.38	0.42	0.46
Book Value Per Share (AED)	1.55	1.72	1.66	1.92	2.17	2.45
Dividend Per Share (AED)	0.16	0.16	0.17	0.21	0.23	0.25
PE (x)	13.4	16.5	12.3	12.4	11.5	10.5
EV/EBITDA (x)	10.0	11.6	8.0	8.3	7.6	7.0
PB (x)	2.3	2.9	2.5	2.5	2.2	2.0
Dividend Yield (%)	4.6%	3.3%	4.0%	4.4%	4.8%	5.3%

Source : KAMCO Research and Aramex

Note : Forward Valuation ratios are based on current market prices and KAMCO Research estimates

ARAMEX GLOBAL PEERS VALUATION COMPARISON																					
Company Name	Country	M.Cap. (USD Mn)	EV			EBITDA (USD Mn)			Net Profit (USD Mn)			EBITDA CAGR		Net Profit	P/E (x)			EV / EBITDA (x)		Dividend Yield (%)	FCF Yield
			(USD Mn)	TTM	2019E	2020E	TTM	2019E	2020E	TTM	2019E	2020E	2015-17		2015-17	TTM	2019E	2020E	TTM		
Gulf Warehousing Co	Qatar	732	1,075	131	131	136	65	68	74	1.8%	7.2%	11.3	10.8	9.8	8.2	8.2	7.9	4.2%	11.9%		
United Parcel Service Inc	US	98,344	116,061	9,231	10,478	11,355	4,791	6,542	7,102	10.9%	21.8%	20.5	15.0	13.8	12.6	11.1	10.2	3.2%	6.5%		
FedEx Corp	US	49,483	65,027	7,929	8,462	9,138	3,636	4,057	4,328	7.1%	-2.7%	13.6	12.2	11.4	8.2	7.7	7.1	1.1%	2.8%		
Deutsche Post AG	Germany	41,655	57,216	7,618	8,369	9,099	2,451	3,027	3,399	9.3%	17.8%	17.0	13.8	12.3	7.5	6.8	6.3	4.0%	7.6%		
Kuehne + Nagel International AG	Switzerland	17,001	16,860	1,236	1,451	1,554	787	811	866	12.1%	4.9%	21.6	21.0	19.6	13.6	11.6	10.8	4.3%	2.2%		
CH Robinson Worldwide Inc	US	12,288	13,256	1,009	1,067	1,109	665	693	722	4.9%	4.2%	18.5	17.7	17.0	13.1	12.4	11.9	2.2%	6.1%		
Yamato Holdings Co Ltd	Japan	10,369	10,058	1,152	1,100	1,286	399	373	460	31.7%	67.1%	26.0	27.8	22.6	8.7	9.1	7.8	0.9%	n.a		
DSV A/S	Denmark	16,319	17,225	984	1,293	1,433	634	641	707	20.6%	5.6%	25.7	25.4	23.1	17.5	13.3	12.0	0.4%	3.5%		
Expeditors International of Washington	US	13,424	12,501	851	895	947	618	616	648	5.5%	2.4%	21.7	21.8	20.7	14.7	14.0	13.2	1.2%	3.9%		
Nippon Express Co Ltd	Japan	5,565	7,388	1,196	1,157	1,139	118	118	118	1.5%	165.5%	47.1	13.0	13.4	6.2	6.4	6.5	1.9%	n.a		
Panalpina Welttransport Holding AG	Switzerland	4,814	5,011	296	316	353	80	109	134	9.2%	29.5%	60.3	44.3	36.0	16.9	15.9	14.2	1.9%	1.8%		
Singapore Post Ltd	Singapore	1,742	1,990	165	153	164	88	77	82	7.0%	-6.1%	19.9	22.6	21.2	12.1	13.0	12.2	3.4%	4.8%		
Blue Dart Express Ltd	India	1,144	1,172	56	40	55	22	16	24	-1.0%	3.8%	51.0	71.3	47.3	21.1	29.1	21.5	0.4%	1.6%		
Sinotrans Ltd	Hong Kong	5,874	6,969	773	560	624	402	409	451	-1.1%	5.0%	14.6	14.4	13.0	9.0	12.5	11.2	1.7%	-3.4%		
Simple average										8.5%	23.3%	26.4	23.6	20.1	12.1	12.2	10.9	2.2%	4.1%		
Weighted average										10.3%	17.2%	20.5	16.9	15.4	11.3	10.2	9.4	2.5%	4.6%		
Median										7.0%	5.3%	21.1	19.3	18.3	12.3	12.0	11.0	1.9%	3.7%		

Source : Bloomberg and KAMCO Research

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