Securities

AFFIN HWANG CAPITAL

Out think. Out perform.

The Korean Makeover

Century Logistics is on the cusp of transforming from a total integrated logistics pure play to an emerging parcel delivery provider by leveraging CJ Korex's strong parentage as Korea's largest logistics provider. Riding on the exponential growth potential in e-commerce and the digitization of Malaysia's retail economy, Century aims to differentiate itself with high service quality and superior efficiencies in automation. The merger with CJ Korex's Malaysian operations could yield significant synergies, increase product offerings and expand its client base to underpin near-term earnings growth for its core operations. We initiate coverage with a BUY and a 12M TP of RM1.70.

Expansion into Parcel Delivery Services

Leveraging on CJ Korex's technical competencies and established track record, Century is set to introduce its Parcel Delivery Services in 2018 to complement CJ Korex's strategy in extending its supply chain with last-mile delivery for logistics operations in Malaysia. With a strong go-to-market strategy, a readily available demand offtaker amid surging demand for Korean products and CJ Korex's affiliation with local e-commerce players like CJ WOW Shop, we project a strong 71% revenue CAGR on the back of 53% CAGR in sorting capacity for FY18-20E. We expect the segment to scale quickly and become Century's second largest EBIT contributor by 2022.

Warehouse expansion to underpin earnings

Tapping into the operational strength of CJ Korex, we see room for sales expansion via the development of new client base with concerted marketing efforts to Korean MNCs. The possible merger between CJ Malaysia and Century could also yield significant synergies via combined competency and cost control, aside from expanded product offerings and economies of scale. With the expansion of the new multi-storey warehouse in 2018, Century is set to increase its storage footprint by 16% to 2.7m sq ft, enhancing its appeal as one of Malaysia's largest storage solutions provider.

Initiate coverage with a BUY and TP of RM1.70

We are excited with the emergence of CJ Korex as a major shareholder in Century, and its vision to transform Century with the new venture into Parcel Delivery Services, at the same time strengthening its core logistics offerings via operational consolidation to achieve scale and expansion in client base. We value Century using a DCF-methodology, and derive a 12M TP of **RM1.70**. CJ Korex's entry price of RM1.45 should also provide support for near-term valuations. We initiate coverage on the stock with a **BUY** rating, for a potential upside of 43% from the current levels.

Earnings & Valuation Summary

FYE 31 December	2015A	2016E	2017E	2018E	2019E
Revenue (RMm)	297.9	300.3	304.6	328.5	361.5
EBITDA (RMm)	41.6	38.7	43.6	47.6	55.4
Pretax profit (RMm)	40.9	25.5	31.3	33.1	37.2
Net profit (RMm)	31.9	20.1	25.6	27.0	30.4
EPS (sen)	8.1	5.1	6.5	6.9	7.8
PER (x)	14.5	23.0	18.1	17.1	15.2
Core net profit (RMm)	22.5	22.5	25.6	27.0	30.4
Core EPS (sen)	5.8	5.7	6.5	6.9	7.8
Core EPS growth (%)	39.6	(0.3)	13.9	5.5	12.5
Core PER (x)	20.5	20.6	18.1	17.1	15.2
Net DPS (sen)	5.2	3.9	2.6	2.8	3.1
Dividend Yield (%)	4.4	3.3	2.2	2.3	2.6
EV/EBITDA (x)	11.1	11.4	12.4	12.0	10.9
Chg in EPS (%)			-	-	-
Affin/Consensus (x)			1.1	1.0	0.9

Source: Company, Affin Hwang forecasts, Bloomberg

Initiation of Coverage

Century

CLH MK

Sector: Transport & Logistics

RM1.19 @ 18 May 2017

BUY

Upside: +43%

Price Target: RM1.70

Previous Target: N/A

Price Performance

	1M	3M	12M
Absolute	+2.6%	+35.6%	+40.4%
Rel to KLCI	+1.1%	+29.6%	+29.7%

Stock Data

Issued shares (m)	392.1
Mkt cap (RMm)/(US$m)	470.5/108.4
Avg daily vol - 6mth (m)	2.0
52-wk range (RM)	0.80-1.27
Est free float	70.1%
BV per share (RM)	0.78
P/BV (x)	1.53
Net cash/ (debt) (RMm)	22.3
ROE (2017E)	9.0%
Derivatives	No
Shariah Compliant	Yes

Key Shareholders

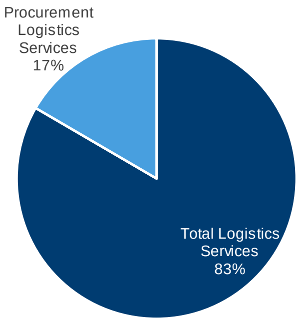
CJ Korea Express	30.8%
Teow Choo Hing	11.2%
Datin Lee Hay Hun	6.7%

Source: Affin Hwang, Bloomberg

Aaron Kee CFA
(603) 2146 7612
aaron.kee@affinhwang.com

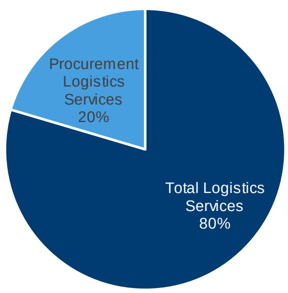
Focus Charts

Fig a: FY16 revenue breakdown



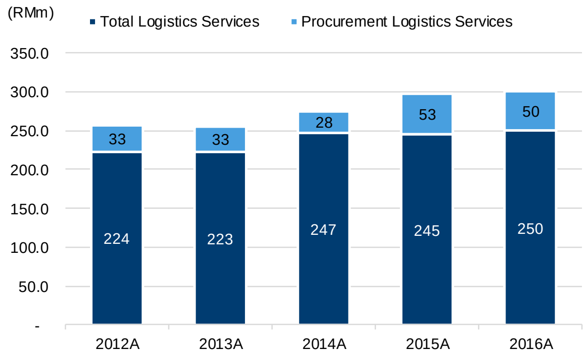
Source: Company

Fig b: FY16 Operating profit breakdown



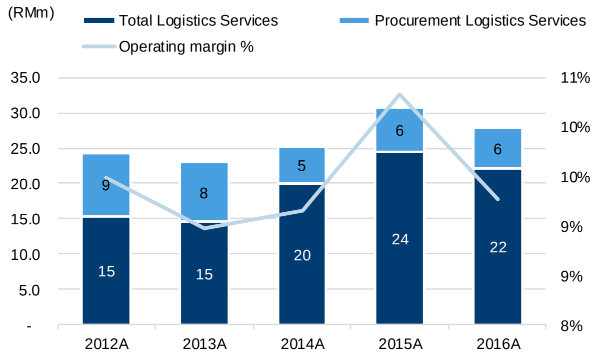
Source: Company

Fig c: Segmental revenue breakdown



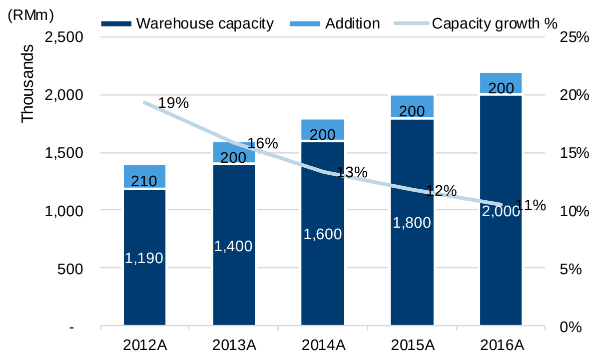
Source: Company

Fig d: Segmental operating profit breakdown



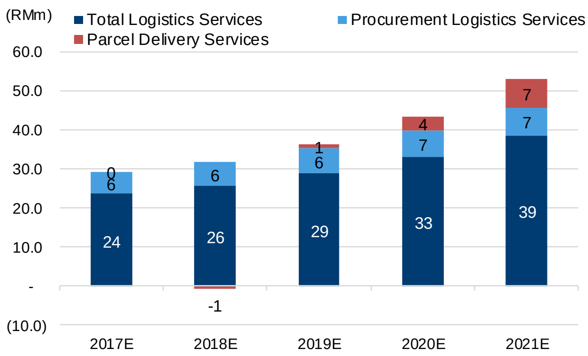
Source: Company

Fig e: Warehouse storage space expansion



Source: Company

Fig f: Projected operating profit for Century



Source: Company, Affin Hwang forecasts

Riding on CJ Korex's strong parentage

Emergence of CJ Korex

We believe the entry of CJ Korea Express Asia Pte Ltd (CJ Korex) as Century's single largest shareholder with a 31% stake in the Company will be a game changer for Century, as the former seeks to disrupt the rapidly-growing parcel delivery services in Malaysia through expansion via Century's existing infrastructure and facilities. New business expansion aside, we believe there are also merits for CJ Korex to consolidate its Malaysia logistics operations under Century to achieve economies of scale, before introducing its Parcel Delivery Services to capitalize on the growing e-commerce delivery demands, and to leverage on CJ Korex's existing presence in the retailing sector to generate demand.

Leading logistics provider in South Korea

As a backstory, CJ Korex is the largest logistics provider in South Korea with a diversified business portfolio, offering integrated logistics solutions to both local and global customers, akin to what Pos Malaysia is to the Malaysian market here. As a total integrated logistics solution provider, CJ Korex has competency offerings throughout the supply chain, including contract logistics, freight forwarding, shipping and parcel delivery that allows it to cater to all manner of goods and services transportation. Having established its dominance in the South Korean market, CJ Korex has branched out globally with 78 overseas strongholds in 22 countries, as CJ Korex capitalized on the rising globalization of Korea's manufacturing prominence back in the 80s.

Presence in Malaysia

As a matter of fact, CJ Korex has an existing presence in Malaysia via CJ Logistics Malaysia Sdn Bhd (CJ Malaysia). According to the company website, CJ Malaysia now provides three logistics solutions:

(i) Parcel delivery – a small but growing business, CJ Malaysia can now provide cash on delivery management and value added services such as installation service and drop point pick up service.

(ii) Freight forwarding – CJ Malaysia is connected with 72 global networks in 21 countries and provides integrated freight forwarding solutions for import/export of goods.

(iii) CJ Malaysia has different warehouses specializing in general FMCG, cold chain and container yard to cater for various storage needs.

CJ Malaysia is relatively a small player among the local players, but it does provide a comprehensive set of logistics solutions, mostly to Korean MNCs operating in Malaysia.

Strategy forward

Leveraging on the operational strength of CJ Korex, Century has laid out a three-pronged strategy which will be shaping its business strategies for years to come:

(i) Sales expansion via development of new multi-national and Korean customers utilizing CJ Korex TES (technology, engineering, system and solution) and their combined operational strengths. The tie-up would hopefully lead to expansion in Century's client base and create additional sales opportunities for its existing business in Total Logistics Services.

(ii) Profit maximization via combined competency and cost control, which will include integration of operational and administration activities while avoiding duplication. This initiative largely relates to internal efficiencies, which can be improved with better automation and knowledge sharing.

(iii) Expansion into parcel delivery business as a new core activity, where Century will ride on the momentum of the booming e-commerce in Malaysia, as well as leverage on CJ Korex's strong relationship with prominent e-commerce players.

New pivot into Parcel Delivery Services

CJ Korex's pivot into Parcel Delivery Services via Century does not come as a surprise, as it also serves as a vertical integration to ensure complete solutions throughout the supply chain. To kick-start the integration process, we believe it would be ideal for Century to acquire CJ Malaysia, thereby consolidating all the overlapping businesses, mainly freight forwarding and warehousing businesses, between the two. We believe there are merits to the transaction, largely arising from the synergies, economies of scale and immediate floor space expansion in an enlarged entity. CJ Malaysia also has a small presence in the Parcel Delivery Services. Assuming the merger does happen, an ideal way for the acquisition may be in the form of new share issuance in lieu of cash consideration, which would entail a minority shareholders' approval for the transaction, as well as exemption from having to make a mandatory general order (MGO) given CJ Korex is only 2% shy of the 33% threshold. More crucially, it will also mean that Century's existing cash balance could be preserved for future investment needs. There's also another consideration of cash-funded merger, but we are not too positive on that given the need to conserve cash for the expansion into the Parcel Delivery Services.

Possibility of rebranding?

EPS dilution would be a major concern as CJ Malaysia is loss-making currently. That said, we believe the prospects of turning around the Malaysian entities are good, as we understand that the Malaysian entities are actually operationally profitable. With the introduction of an enlarged entity, we believe this could enable Century to tap on a wider market for their Total Logistics Services, creating higher demand for their freight forwarding business and warehouse storage supply by taking advantage of CJ's branding. We also do not discount the possibility of Century being rebranded to reflect CJ's identity as part of the integration processes to ensure proper assimilation and brand coordination.

The pie is still growing

With an enlarged balance sheet and riding on the strong parentage of CJ Korex, we believe Century could have the necessary financial strength and cash flow generation ability to fund the acquisition of an existing parcel delivery player, if the need arises, as part of its expansion plan into the Parcel Delivery Services.

As a background, Malaysia's parcel delivery market is dominated by a few notable incumbents which have established presence with superior connectivity and nationwide reach. That said, Malaysia parcel delivery demand has been growing at a breakneck pace, primarily underpinned by the surge in e-commerce retailing which drove the demand for B2C (business-to-customers) delivery. We believe Malaysia's e-commerce retail sales have been growing in excess of 30% yoy, while e-commerce penetration remains low as a percentage of total retail sales.

Pos Malaysia (POSM MK; Not-rated) and GDEX (GDEX MK; Not-rated) have recorded revenue CAGR averaging 20% in FY13-FY16, being the top two parcel delivery players riding on the upsurge in e-commerce deliveries. Based on the data compiled by The Edge, both Pos Malaysia and GDEX controlled more than two thirds of the total market, as of December 2015. While incumbents are still expanding sorting capacity, we believe the supply is still playing catch up to demand growth.

Entry via brownfield acquisition

As in any expansion, Century could venture into the Parcel Delivery Services via brownfield acquisition of an established player, or it could opt for greenfield expansion where it builds its operations, infrastructure and facilities from the scratch. Naturally, we would prefer the first route, as a brownfield acquisition would cut short the time to market, as well as give Century immediate footprint and network presence in major locations with the supporting infrastructure (i.e. bikes, trucks, branch offices, staff etc). However, brownfield acquisition may come with its pitfalls, most notably culture integration difficulties, unrealistic valuations, extended period for deal completion, and overstated synergies. Greenfield entry, on the other hand, provides increased control over the business, and the avoidance of intermediary and transaction costs. But greenfield expansion is often associated with steep learning curve and slowing market entry time.

Fig 1: Actual site location

Source: Company

Fig 2: Proposed warehouse design

Source: Company

Expansion in storage capacity

While Century has yet to announce its entry strategy for the Parcel Delivery Services, we think it will likely utilise the incoming multi-storey warehouse that is being constructed in Setia Alam as its designated sorting hub. To recap, the expansion was first proposed in 2015 for a total space of 450,000 sq ft in storage space. The land measuring 8.2 acres was acquired in 2015 at a total cost of RM40m. We believe with the shift in business growth strategy, Century could re-designate a portion of the warehouse, with up to projected total sorting capacity of 35,000 parcels/day, by our estimates. Accordingly, the warehouse storage space could shrink from 450,000 sq ft to 350,000 sq ft.

Robust volume demand

We have projected for an initial sorting capacity of 15,000 packages/day for FY18, before rising to 35,000 packages/day by FY20. Our projection has not taken into account the possibility of integration with potential acquisition target, which could scale up their sorting capacity substantially. We have assumed for an average delivery fee (ADF) of RM5/parcel, which we derived by averaging Pos Malaysia and GDEX's revenue based on their guided sorting capacity. While the ADF has been on a downward trend for the past few years, largely due to some fare slashing by Pos Malaysia to stave off competition, the volatility has somewhat stabilized while the surge in volume is more than enough to make up for the shortfall in lower prices. In terms of margin projection, we have assumed an initial LBIT margin of 5%, as we expect higher start-up costs and teething problems to crimp margin in the near-term. But we do expect the division to churn an EBIT margin of 5% in 2019, before normalizing to 15% by 2021, as the operating leverage effect should kick in by then coupled with the exhaustion of one-off upfront costs in beginning period.

Fig 3: Projected sorting capacity

Sorting capacity	FY17E	FY18E	FY19E	FY20E
Packages/day				
Beginning	-	5,000	15,000	25,000
Addition	-	10,000	10,000	10,000
End	-	15,000	25,000	35,000
Avg capacity	-	10,000	20,000	30,000
Growth (%)	-		+100%	+50%
Utilisation rates (%)	-	70%	70%	70%
Total packages per annum(m)	-	2.56	5.11	7.67

Source: Affin Hwang estimates

Fig 4: Projected financials for parcel delivery services

Projected financials	FY17E	FY18E	FY19E	FY20E
Avg delivery fee (RM)	-	5.00	4.95	4.90
Growth	-	-	-1%	-1%
Revenue (RMm)	-	12.8	25.3	37.6
EBIT (RMm)	-	(0.6)	1.3	3.8
EBIT margin	-	-5%	5%	10%

Source: Affin Hwang estimates

Fig 5: Peers comparison

FY16	Pos Malaysia	GDEX
Express delivery revenue (RMm)	577.0	214.0
Yoy growth (%)	16%	14%
EBITDA (RMm)	78	49
EBTIDA margin (%)	14%	23%
Est sorting capacity (packages/day)	300,000	120,000
Average delivery fee (RM)	5.30	4.90

Source: Affin Hwang estimates, Company

Leveraging on CJ Korex

We believe it would not be difficult for Century to fill up its sorting capacity given its affiliation with CJ Korex, as there is a readily-available catchment market for Century to tap into the rising Korean influence in the e-commerce market in Malaysia. To put into perspective, a few of the major e-retailers already have existing Korean affiliations in one way or another, and with CJ Korex being their dominant delivery partner in Korea, we believe Century could leverage on CJ Korex network by providing the last mile delivery point for goods in Malaysia.

Fig 6: E-commerce players with Korean affiliation

E-commerce players	FY16 Revenue	Products sold	Remarks
11street	na	na	70% owned by a Korean company
Astro Go Shop	RM261m	1,500,000	40% owned by a Korean company
CJ WOW Shop	RM62m*	319,000*	49% owned by CJ Korea
Qoo100	na	na	49% owned by a Korean company

** From April to December 2016*
Source: Affin Hwang, Company data

Consolidating the Korean goods

Case in point, 11street is 70%-owned by SK Planet, which is Korea's leading e-commerce platform and digital content provider. Astro GO Shop is a 60:40 partnership with GS Home Shopping Inc, a leading Korea-based company engaged in the home shopping business. Despite being a relatively new marketing method via TV channel, Astro GO Shop has made tremendous inroads with impressive growth in their advertised products sale. With a total customers of 912,000, Astro Go Shop sold more than 1.5mn products in FY16 alone, which is a 53% yoy growth over the 983,000 products sold in FY15. We believe a shorter-term target for delivery orders fulfillment would be through CJ WOW Shop, which is a joint venture launched by CJ Korea (the ultimate holding company of CJ Korex) and Media Prima. CJ WOW Shop also reported strong growth of its own, with 319,000 products sold in 9 months since the inception in April 2016. Going by CJ Korea's ownership in CJ WOW Shop, we believe that a significant portion of the delivery packages can be assigned to Century as its designated Malaysia delivery partner, provided that certain threshold and service quality level can be adhered to. This would in turn, provide an immediate uptick and utilisation of its sorting capacity.

Tapping into Lazada

Korea affiliation aside, we believe Century could also tap into CJ Korex's relationship with Lazada. To recap, CJ Korex has entered into an international delivery service contract with Southeast Asian online retailer Lazada Group SA, which operates in Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam. Under the deal, CJ Korex would be in charge of delivery goods made in Korea that customers buy in the regional markets via Lazada's website. According to media reports, high popularity of Hallyu, or Korean wave, and K-Pop music has contributed to a surge in sales of Korean products overseas, particularly beauty products like face mask, facial care, makeup products etc. With the establishment of the parcel delivery partner in Malaysia via Century, we believe CJ Korex could redirect most of the parcels through in-house delivery.

Automation technology sharing from CJ Korex

With the strong support from CJ Korex, Century is set to enter a multi-phase sales growth for parcel delivery services. Despite mounting competition, we do see differentiating attributes by Century with the deployment of CJ Korex's efficiencies and automation to raise the service quality level and reduce delivery time. CJ Korex is a highly automated parcel delivery player in Korea. To this end, CJ Korex has invested close to 123bn won (RM470m) to fully automate its parcel sorting process for its sub-terminal throughout South Korea. As part of the automation, CJ Korex has installed wheel sorter, which is a system that automatically sorts parcels on the conveyor into designated areas.

CJ Korex is currently operating one mega hub terminal in Daejeon, four hub terminals and over 200 sub-terminals. The company's five hub terminals are already sorting parcels through automated sorting systems, and the remaining 200 sub-terminals will be fully automated by April 2018. While the scale of Century's initial sorting capacity is unlikely to be big enough to justify the implementation of a wholly-automated sorting system, we do believe that CJ Korex could introduce some of its best-in-class standards that can be incorporated as part of Century's operational procedures.

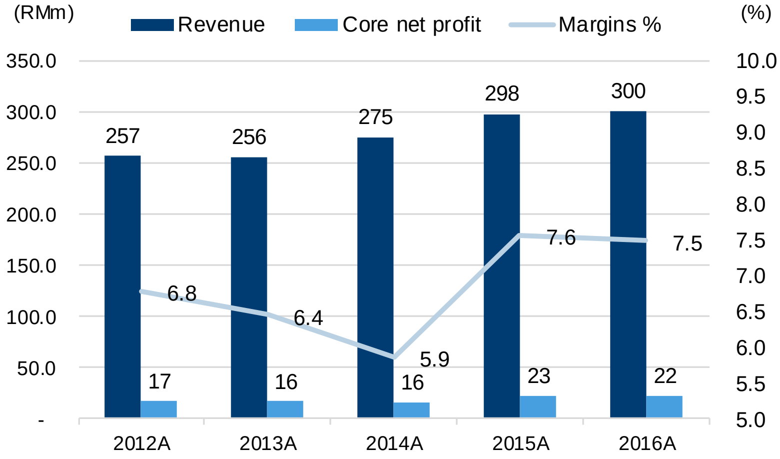
Regional expansion in the horizon

We believe the establishment of the parcel delivery services through Century will be a stepping stone to CJ Korex's regional ambition to expand presence across ASEAN. The lack of a strong inter-regional postal players despite the strong emergence of e-commerce awareness creates a huge gap yet to be filed. ASEAN lacks the equivalent of DHL or UPS that could provide a seamless delivery experience at competitive prices, largely due to the outdated undeveloped network and infrastructure, as well as the vast demographics scattered across the countries. The formation of a strong regional transshipment hub in Malaysia could be a precursor for a wider expansion, by leveraging on Malaysia's efficient sea ports and air freight facilities to deliver goods across.

That said, we also see tremendous challenges in making this work, as even incumbents like Pos Malaysia is finding difficulty in penetrating other countries due to first mover advantage established by the respective domestic players. Nonetheless, we believe the regional ambition is likely a longer-term strategic plan, and near-term focus would be on developing Century into a dominant parcel delivery player capable of mounting a strong challenge to the incumbents with its superior efficiencies via automation and differentiated service level.

Strengthening the core

Fig 7: Century financials breakdown



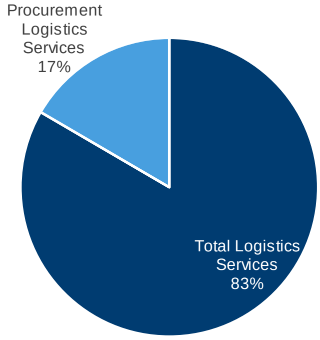
Source: Company

Turning the page

Century's revenue is relatively resilient with an uptrend bias, despite intensifying competition within the logistics sector. Overall revenue crossed the RM300m mark the first time in FY16, with revenue registering a 3% CAGR from FY12-16. Core profitability also rose at 7% CAGR, in line with the revenue growth during the same period. Despite stiff competition and increased cost of doing business, Century managed to maintain its core margins between 6% and 7.5%.

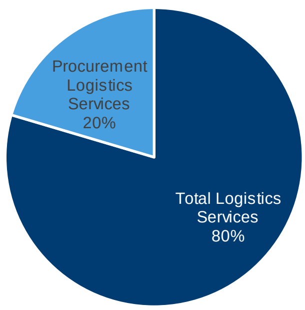
Earnings growth, for the large part has been unexciting, partly due to the unfavourable product mix, and the tepid expansion plans. Having said that, Century remains a sound and well-managed logistics company with a reputable brand name, and strong track record without any recorded losses since listing.

Fig 8: FY16 revenue breakdown



Source: Company

Fig 9: FY16 Operating profit breakdown

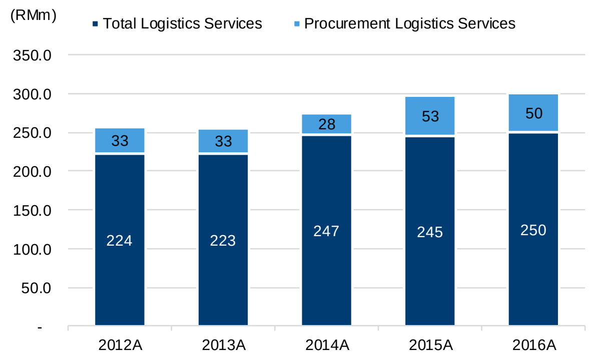


Source: Company

Leveraging on CJ Korex's superior operational strength

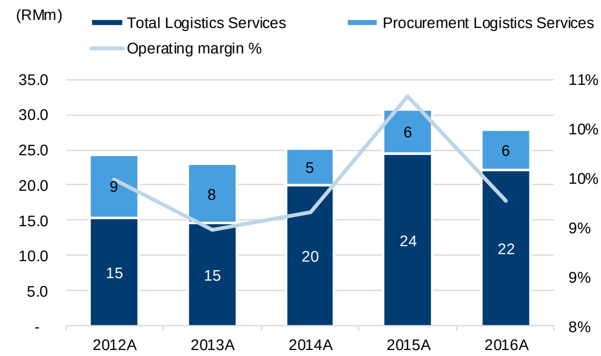
With the integration of CJ Korex's branding and expertise, we expect Century's core businesses in Total Logistics Services to stage an earnings rebound underpinned by synergistic operational improvement, expansion in client bases, improved revenue mix, and recovery in domestic sentiment to drive revenue growth. Century would be able to leverage on CJ Korex's operational strength including its technology, systems and solutions. In addition, CJ Korex and Century could integrate their logistics and administrative activities, particularly for CJ Malaysia's operations, which would result in a larger network and more cost-efficient operations with increase in scale. CJ Korex and Century could also benefit through the sharing of key logistics hubs and networks, cross-selling and new business opportunities.

Fig 10: Segmental revenue breakdown



Source: Company

Fig 11: Segmental operating profit breakdown



Source: Company

An integrated logistics solutions provider

To recap, Century is an integrated logistics solutions provider that aims to enhance its customers' supply chain effectively. Century has the competencies, networks and logistics facilities to provide complete logistics supply chains solutions in a timely, efficient, and cost competitive manner. Century primarily runs two major business streams. Under its Total Logistics Services, Century offers highly customized and competitive supply chain solutions to its customers. The Group's domestic customers comprise a varied mix of customers and industries, from fast moving consumer goods to paper products.

Fig 12: Century operates a sizeable truck fleet

Source: Company

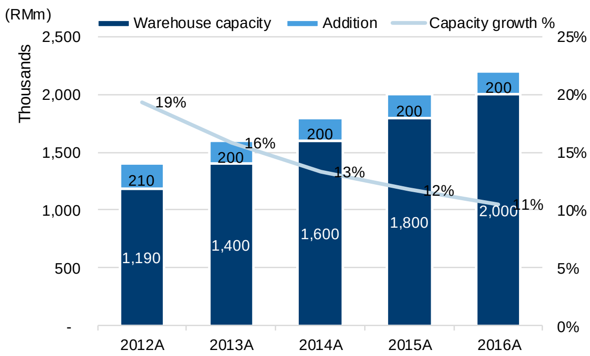
Fig 13: Storage of fast moving consumer goods

Source: Company

Warehouse spaces are running scarce

As at FY16, Century managed a logistics facility portfolio of 2.2m sq ft in seven warehouses scattered across Port Klang, Subang, Shah Alam and Pelabuhan Tanjong Pelepas (PTP). Out of the total, 1.5m sq ft facilities are self-owned, while the remaining are leased from third-parties. To complement its storage capacity, Century also runs a fleet of 70 conventional trucks, 75 hauler primer movers, 13 side loader trailers and 448 trailers. With the expansion of the three-storey warehouse-cum-HQ in Setia Alam, we expect Century's storage capacity to increase to 2.7m sq ft by 2018. The warehouses include a mixture of general warehouse, bonded warehouse (in PTP), as well as temperature-controlled warehouse. We do not anticipate any difficulties in filling up the warehouse utilization rate despite the significant increase in capacity, as most of its facilities are running close to maximum capacity. On top of that, warehouse storage spaces are running scarce, especially for premium locations in Klang Valley.

Fig 14: Warehouse storage space expansion



Source: Company

Fig 15: Breakdown of warehouse owned

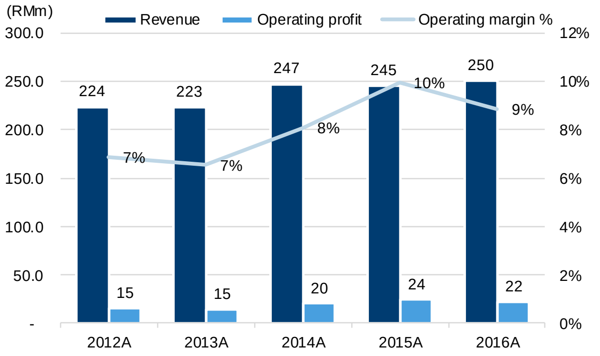
Location	Storage capacity	Purposes
Port Klang, Lot 8	277,000	Storage and HQ
Port Klang	286,000	Procurement logistics
PTP, Plot D12	161,000	Bonded warehouse
PTP, Plot D14	101,000	Bonded warehouse
PTP, Plot 16 & 17	192,000	Bonded warehouse
PTP, Plot D28	401,000	Bonded warehouse

Source: Company

Beneficiary of crude volatility

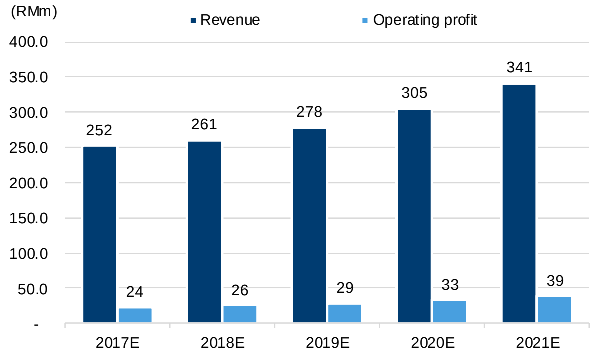
As part of the Total Logistics Services, Century also provides Oil Logistics Services via ship-to-ship transfer for fuel and crude oil to vessels located near PTP. We are unable to assess the financials of the Oil Logistics Services, as the numbers are consolidated under the Total Logistics Services within the segmental breakdown. But we gathered that the Oil Logistics Services are profitable with strong margins, largely due to the limited competition and attractive price points denominated in Ringgit. Crude oil storage remains in high demand and is a relatively resilient business, with Century making margins purely on storage charges and does not take any position in crude oil prices. Generally, lower volatility in crude oil prices creates higher throughput.

Fig 16: Historical financials for Total Logistics Services



Source: Company

Fig 17: Projected financials for Total Logistics Services



Source: Company, Affin Hwang estimates

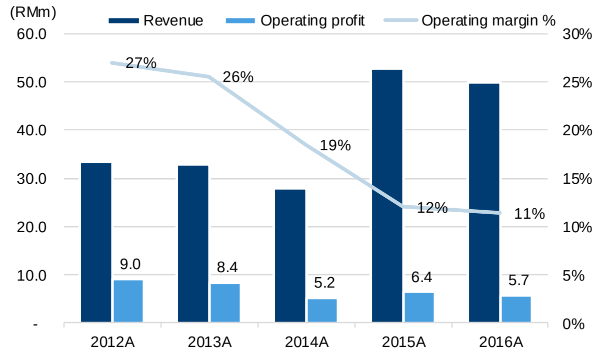
Slow and steady growth for Total Logistics Services

The Total Logistics Services revenue has been growing at a 3% CAGR for FY12-16, largely underpinned by the higher storage capacity to meet the growing demand for strategic warehousing space, but weighed by overall declining rates due to competition. Century has, in particular, leveraged on the close proximity between PTP and Singapore, as well as its competitive rates to lure Singapore corporates to utilize its warehouses at PTP. Operating margin for the segment is relatively stable, and has ranged from 7% to 10% in the past few years. We are projecting a revenue growth of 7% for Century for FY17-19, primarily underpinned by the higher storage warehouse capacity with the commencement of the multi-storey warehouse in FY18, and stable operating margins of 9%. As of now, Century provides logistics services for notable local players like Celcom, F&N, Hartalega, Press Metal and Mycron Steel.

OEM assembly services

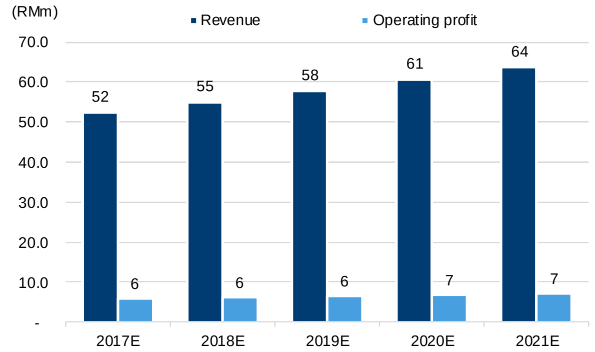
Century's second business stream involves the Procurement Logistics Services, which offers original equipment manufacturing (OEM) solutions to locally-based electrical and electronic products manufacturers and traders. Leveraging on the long-term relationship with its logistics customers, Century soon realized that customers are outsourcing more of their supply chain to third party logistics providers to include procurement, assembly and repackaging services, as manufacturers are moving away from manufacturing activities to focus more on products R&D. Century primarily assembles white goods such as televisions, washing machines, refrigerators, freezers, vacuum cleaners as well as microwave ovens.

Fig 18: Historical financials for Procurement Logistics Services



Source: Company

Fig 19: Projected financials for Procurement Logistics Services



Source: Affin Hwang estimates

Margin pressure in Procurement Logistics Services

That said, the Procurement Logistics Services has had difficulties of its own, primarily due to the fast-paced changes in the technological space, which would entail consistent capex investment into the business, engineers retraining and production process restructuring to ensure relevance and efficiencies within the industries. The Procurement Logistics Services' margins have been trending down from a high of 27% in FY12 to a low of 11% in FY16, despite the 11% in revenue CAGR over the same period. We believe the declines in margins are likely due to the increased scope and complexities in the assembly space, compounded by the changing requirements of customers. This has dragged assembly efficiencies to a low and led to the increase in overhead costs, while assembly rates are also on a downtrend due to lower selling prices for white goods in general.

Fig 20: Assembly lines

Source: Company

Fig 21: Pre-shipment delivery inspection

Source: Affin Hwang estimates

Korean connection could open doors

While Century will still retain its core competencies within the Procurement Logistics Services, we believe any significant investment or substantial expansion for the assembly services are unlikely, given the declining returns and high upfront cash costs, which could be deployed in other divisions. We project a conservative 5% revenue growth for the Procurement Logistics Services, as we see room for Century to capitalize on its Korean-connection to secure higher value work scope. Margins are likely to have bottomed at 11%, in our view, given the pace of decline has started to slow. We project the operating margin to stabilize at 11% for FY17-19E. As of now, Century does assembly services for notable MNCs like Haier, Philips, Midea and Hisense.

Fig 22: Century's major client base

Source: Company

A holistic view

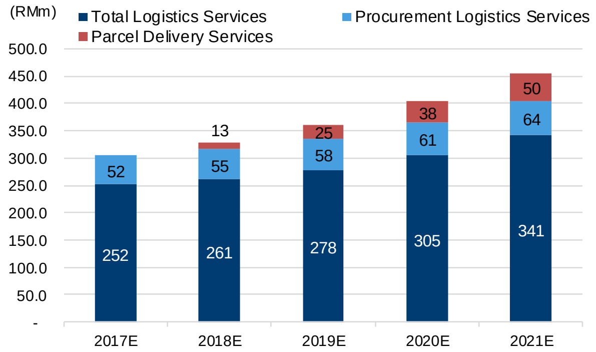
Positive outlook ahead

Bringing it all together, we expect Century's existing core businesses in the Total Logistics Services and the Procurement Logistics Services to fare better after rebounding from a low earnings base in FY16. With the entry of CJ Korex as a major shareholder, we believe there are more business opportunities with expanded client base. There could be upside to operating margins as well, leveraging on the synergistic operational improvement with knowledge sharing and consolidation of non-core activities like finance or human resources, while fixed costs can be spread over higher units with the increase in scale.

New revenue stream

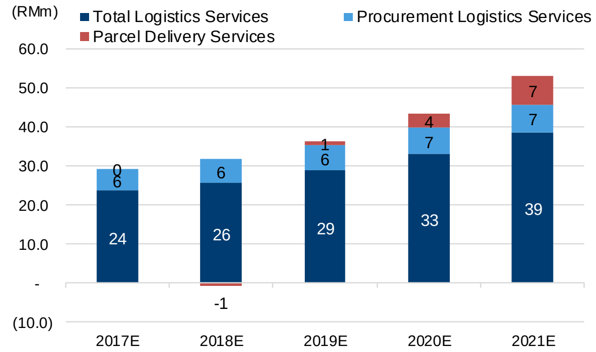
Meanwhile, the introduction of a new business stream in the form of Parcel Delivery Services should mark another growth phase for Century, as it seeks to capitalize on the booming e-commerce industry. While initial contributions are likely to be immaterial, we believe Century could scale up quickly with the combination of CJ Korex's technical competence, greenfield expansion complemented with brownfield acquisitions of established players. On the whole, we are projecting 9% in revenue CAGR and 10% core net profit CAGR for FY17-19E.

Fig 23: Projected revenue for Century



Source: Affin Hwang estimates

Fig 24: Projected operating profit for Century

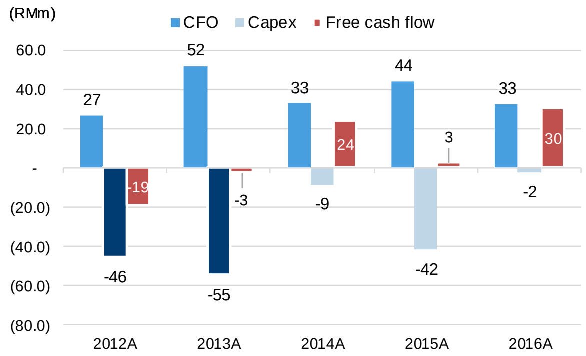


Source: Affin Hwang estimates

ITA to lower effective tax rate

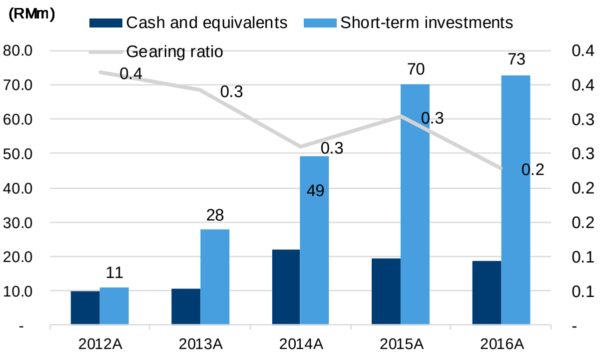
We also see opportunities for higher earnings in FY17-19E due to lower effective taxes as Century accelerates its warehouse expansion, which would quality for investment tax allowance (ITA). To recap, Century was granted the ITA for five years beginning in 2016 for capex relating to its logistics business which can be offset against statutory income. Century has budgeted approximately RM150m in capex for the construction of the warehouse to be incurred for the next three years, which would lower its tax bills significantly. For conservative reasons, we have assumed an effective tax rate of 18% for FY17-19E. A lower effective tax rate could yield significant upside risk to our earnings projection.

Fig 25: Century turned free cash flow positive in 2014



Source: Affin Hwang estimates, Company

Fig 26: Solid cash position



Source: Affin Hwang estimates, Company

Strong cash position

Century turned net cash in FY14, and has held that position for three consecutive years. As of December 2016, Century held close to RM90m in cash, with a substantial portion of it invested in money market. With the change in business strategy, we believe Century would turn more aggressive in its cash deployment with the expansion of its warehouse and the brownfield acquisition of a parcel delivery player. Century has solid free cash flow generation ability, with positive free cash flow recorded in four out of the five previous financial years. This was also boosted due to some disposal of assets which increased cash balances, while capex was also minimal relative to its operations in certain years. Century also has a highly efficient working capital management initiative in place, as evident in the sharp decline in total receivables days, which fell from 113 days in FY12 to 85 days in FY16. Typically, Century pays out more than 50% of its earnings as dividends, with yields averaging at 3%. We do see near-term downside risk to prevailing yields, as we expect Century to lower its payout ratio to fund its future expansion. We have assumed a lower payout ratio of 40% in our projection, giving yields of 2.5% in FY17.

Valuations and recommendation

DCF to capture long term growth

We valued Century using a discounted cash flow (DCF) method, as we believe this is the most appropriate methodology to capture Century's long-term intrinsic value. We expect Century to slip into negative free cash flow for FY17-19E, largely due to the hefty upfront capex investment for the expansion into Parcel Delivery Services, as well as due to its warehouse expansion. Century should turn free cash flow positive by FY20, along with the ramp up in new revenue stream and the completion of the warehouse expansion which would reduce the capex commitment.

Initiate with a BUY call

We derive a 12M TP of RM1.70 for Century, offering 43% potential upside from the current levels. We believe Century is set to enter a multiphase expansion with the venture into Parcel Delivery Services. Its core businesses in the Total Logistics Services and Procurement Logistics Services should resume growth path, in line with the recovery in consumer sentiment. We are especially excited with the collaboration between Century and CJ Korex, as it would open doors for more business opportunities and synergistic operational improvement, and could be a stepping stone for its regional ambitions. We are initiating coverage on Century with a **BUY** rating.

Fig 27: WACC assumptions

Risk free rate (Rf)	4.0%
Market return (Rm)	10.0%
Equity risk premium (ERP)	6.0%
Beta	1.00
Cost of equity (Ke)	10.0%
Proportion of debt financing	23.9%
After-tax cost of debt (Kd)	4.2%
Weighted average cost of capital (WACC)	8.6%

Source: Affin Hwang estimates

Fig 28: Target price calculation

Terminal growth	2.0%
Sum of PV of FCF (RMm)	164.1
PV of Terminal Value (RMm)	582.7
Enterprise value (RMm)	746.8
Add: Net cash/(debt) (RMm)	(80.4)
Equity value (RMm)	666.4
No of shares (m)	391.9
Equity value per share (RM)	**1.70**

Source: Affin Hwang estimates and forecasts

Favourable comparison against peers

Valuation-wise, our TP implies 26x forward PER. We have also included parcel delivery peers like Pos Malaysia and GDEX for comparison purposes, although we concede that they are far more established players with skewed valuations.

The valuation of logistics companies and parcel delivery companies have expanded tremendously on the introduction of the Digital Free Trade Zone (DFTZ) and the establishment of Alibaba's regional distribution hub in Malaysia. We believe currently the sector is undergoing multiple expansion and PER rerating, riding on the back of the commencement of DFTZ and booming growth of the e-commerce retail which are set to drive up logistics demand.

Still room for upside

All the logistics stocks have, on average, seen their share prices increased by 41% since the start of the year. Similarly, Century's share price has also increased in tandem with the sector rerating. We believe there is still room for further upside, given that CJ Korex bought into Century at RM1.45, which is still a 22% premium to last close. We believe at the very least, this should form the floor price for Century in the near-term, as CJ Korex would have to offer the same acquisition price should it decide to increase its stake in Century beyond the 33% MGO threshold.

Fig 29: Peer comparison table

	Bloomberg Code	Rating	Price (RM)	TP (RM)	Mkt Cap (RMm)	Year end	PE (x) CY17E	PE (x) CY18E	EPS growth (%) CY17E	EPS growth (%) CY18E	P/B (x) CY16A	ROE (%) CY17E	ROE (%) CY18E	Div. Yield (%) CY17E	Div. Yield (%) CY18E	EV/EBITDA (x) CY17E	EV/EBITDA (x) CY18E
Pos Malaysia Berhad	POSM MK	N/R	5.75	N/R	4,462	Mar	35.8	27.3	31.5	30.9	1.8	8.2	10.3	2.9	3.2	14.5	11.5
Gd Express Carrier Bhd	GDX MK	N/R	2.98	N/R	3,931	Dec	106.4	85.1	5.3	25.0	6.0	10.0	11.1	1.2	1.4	73.2	57.6
Tiong Nam Logistics Holdings	TNL MK	BUY	1.78	1.90	728	Mar	7.4	6.6	42.0	11.9	1.0	12.8	12.9	4.0	4.6	7.2	6.7
Century Logistics Holdings B	CLH MK	BUY	1.19	1.70	467	Mar	17.8	14.8	15.1	20.2	1.1	8.4	9.8	3.3	3.0	0.0	0.0
Tasco Bhd	TASCO MK	N/R	2.59	N/R	492	Mar	14.3	10.6	24.1	34.8	0.9	11.8	13.2	4.0	5.6	7.8	6.5
Freight Management Holdings	FMH MK	N/R	1.40	N/R	266	Dec	10.4	9.3	19.6	11.1	0.9	10.4	10.7	4.5	5.4	5.9	5.3
Nationwide Express Holdings	NATH MK	N/R	0.57	N/R	69	Mar	0.0	0.0	nm	0.0	4.1	0.0	0.0	0.0	0.0	0.0	0.0
Average					**10,415**		**57.8**	**45.7**	**22.9**	**19.1**	**3.3**	**8.8**	**9.7**	**2.8**	**3.3**	**15.5**	**12.5**

Source: Affin Hwang estimates, Bloomberg

Risks to recommendation

Moderating global growth and slowing domestic sentiment

Performance of logistics firms are highly correlated to global growth due to Malaysia's open economy, as well as domestic sentiment. While global growth has been on an uptrend, the macro economy remains exposed to political risks and the surge in trade protectionism, which would exert downside pressure to global growth. That aside, the domestic sentiment could also affect demand for logistics, as private consumption remains a key growth driver for Malaysia's GDP.

Breakdown in relationship with major shareholder

Our investment thesis hinges on the long-term successful collaboration between CJ Korex and Century. There is always the risk of integration failure, given the differences in culture and work ethics, as well as the lack of realized synergies. The exit of CJ Korex, assuming the worst case scenario, could lead to significant change in business direction away from the Parcel Delivery Services.

Prolonged competition

The parcel delivery market is highly competitive. While demand growth has been strong, many players have been incurring losses due to fees subsidization to gain market share. Even the major players are experiencing margin erosion, largely due to the pricing competition. Our investment thesis hinges on the ability of CJ Korex to introduce best-in-class efficiencies to automate and maximize Century's parcel sorting and delivery capabilities. There is no certainty that Century could establish a strong presence and branding in the market, given its nescient track record. A prolonged pricing competition could also be harsh on bottomline, which could drag Century into losses as seen in cases like Nationwide Express.

1Q17 Results Review

Fig 30: Results Comparison

FYE Dec (RMm)	1QFY17	QoQ % chg	YoY % chg	1Q comments
Revenue	71.0	(4.8)	2.1	1Q revenue increased 2% yoy largely due to higher contribution from Total Logistics Services (+3% yoy) as the division recorded higher activities but this was weighed down by the Procurement Logistics Services contribution (-3% yoy) that recorded lower activities due to absence of export sales.
Op costs	(61.2)	(4.9)	1.4	
EBITDA	9.8	(4.6)	6.7	EBITDA inched up 6% in line with the higher revenue. Segmental-wise, Total Logistics Services operating profit grew 29% yoy on the back of higher freight rates and higher transportation demand. On the other hand, the Procurement Logistics Services operating profit fell 46% yoy due to smaller work-scope, lower charge rates and less favourable work mix.
EBITDA margin (%)	*13.8*	*-*	*+0.6ppts*	
Depn and amort	(2.6)	(1.9)	(7.3)	
EBIT	7.2	(5.6)	13.0	
EBIT margin (%)	*10.1*	*-0.1ppts*	*+1.0ppts*	
Int expense	(0.8)	3.6	(21.5)	Lower interest expenses and higher interest income due to the higher cash balance registered during the quarter.
Int and other inc	0.5	(77.5)	24.3	
EI	-	na	na	
Pretax profit	**6.8**	4.2	20.2	
Tax	(2.0)	>100	63.9	
Tax rate (%)	*28.8*	*+24.0ppts*	*+7.7ppts*	Tax rate climbed higher due to absence of tax credit. Expect tax rate to gradually come down due to the availability of investment tax allowance.
MI	-	na	na	
Net profit	**4.9**	(22.1)	8.4	
EPS (sen)	1.2	(22.1)	8.4	
Core net profit	**4.9**	(43.8)	8.4	Core net profit of RM4.9m is within our estimate and in line with consensus expectations.

Source: Affin Hwang, Company data

CENTURY – FINANCIAL SUMMARY

Profit & Loss Statement

FYE 31 Dec (RMm)	2015A	2016A	2017E	2018E	2019E
Revenue	**297.9**	**300.3**	**304.6**	**328.5**	**361.5**
Operating expenses	(256.3)	(261.6)	(261.0)	(280.8)	(306.0)
EBITDA	**41.6**	**38.7**	**43.6**	**47.6**	**55.4**
Depreciation	(10.8)	(10.9)	(14.3)	(16.5)	(19.0)
EBIT	30.7	27.7	29.3	31.1	36.4
Net interest income/(expense	(2.8)	(1.4)	(0.8)	(1.1)	(2.6)
Associates' contribution	-	-	-	-	-
EI	9.4	(2.4)	-	-	-
Pretax profit	**40.9**	**25.5**	**31.3**	**33.1**	**37.2**
Tax	(9.0)	(5.3)	(5.6)	(6.0)	(6.7)
Minority interest	-	(0.1)	(0.1)	(0.1)	(0.1)
Net profit	**31.9**	**20.1**	**25.6**	**27.0**	**30.4**

Balance Sheet Statement

FYE 31 Dec (RMm)	2015A	2016A	2017E	2018E	2019E
PPE	267.2	257.9	304.6	353.7	407.0
Other non-current assets	1.4	1.4	1.4	1.4	1.4
Total non-current assets	**268.7**	**259.4**	**306.0**	**355.2**	**408.5**
Cash and equivalents	19.4	18.7	19.0	20.0	19.8
Inventory	3.3	3.9	3.7	4.0	4.3
Trade receivables	7.4	2.6	4.8	5.1	5.6
Other current assets	139.8	150.2	149.8	150.4	151.1
Total current assets	**170.0**	**175.4**	**177.3**	**179.5**	**180.9**
Trade payables	17.5	18.0	18.7	20.1	21.9
Short term borrowings	20.9	18.8	17.6	17.6	17.6
Other current liabilities	33.9	36.7	39.0	41.9	45.6
Total current liabilities	**72.3**	**73.5**	**75.3**	**79.6**	**85.1**
Long term borrowings	49.8	69.4	51.8	81.8	111.8
Other long term liabilities	26.8	(10.6)	38.3	38.9	39.8
Total long term liabilities	**76.6**	**58.8**	**90.0**	**120.7**	**151.6**
Shareholders' Funds	**288.8**	**301.5**	**316.8**	**333.1**	**351.3**

Cash Flow Statement

FYE 31 Dec (RMm)	2015A	2016A	2017E	2018E	2019E
PAT	31.9	20.2	25.7	27.1	30.5
Depreciation & amortisation	10.8	10.9	14.3	16.5	19.0
Working capital changes	7.3	(1.1)	1.4	3.8	4.8
Others	(5.7)	2.6	-	-	-
Cashflow from operations	**44.4**	**32.7**	**41.4**	**47.5**	**54.3**
Capex	(41.8)	(2.3)	(60.9)	(65.7)	(72.3)
Others	1.8	(13.2)	-	-	-
Cash flow from investing	**(40.0)**	**(15.5)**	**(60.9)**	**(65.7)**	**(72.3)**
Debt raised/(repaid)	12.4	(18.8)	30.0	30.0	30.0
Equity raised/(repaid)	4.5	6.7	-	-	-
Dividends paid	(20.4)	(15.3)	(10.2)	(10.8)	(12.2)
Others	4.6	3.8	-	-	-
Cash flow from financing	**(8.1)**	**(31.2)**	**19.8**	**19.2**	**17.8**
Free Cash Flow	**2.6**	**30.4**	**(19.5)**	**(18.2)**	**(18.0)**

Source: Company, Affin Hwang forecasts

Key Financial Ratios and Margins

FYE 31 Dec (RMm)	2015A	2016A	2017E	2018E	2019E
Growth					
Revenue (%)	8.2	0.8	1.4	7.8	10.0
EBITDA (%)	18.2	(7.0)	12.9	9.1	16.4
Core net profit (%)	39.6	(0.3)	13.9	5.5	12.5
Profitability					
EBITDA margin (%)	14.0	12.9	14.3	14.5	15.3
PBT margin (%)	13.7	8.5	10.3	10.1	10.3
Net profit margin (%)	10.7	6.7	8.4	8.2	8.4
Effective tax rate (%)	22.0	20.9	18.0	18.0	18.0
ROA (%)	7.3	4.6	5.3	5.1	5.2
Core ROE (%)	7.8	7.4	8.1	8.1	8.6
ROCE (%)	8.7	5.6	6.3	5.9	6.0
Dividend payout ratio (%)	63.9	76.2	40.0	40.0	40.0
Liquidity					
Current ratio (x)	2.4	2.4	2.4	2.3	2.1
Op. cash flow (RMm)	44.4	32.7	41.4	47.5	54.3
Free cashflow (RMm)	2.6	30.4	(19.5)	(18.2)	(18.0)
FCF/share (sen)	0.7	7.7	(5.0)	(4.6)	(4.6)
Asset management					
Inventory turnover (days)	6.1	7.1	5.0	5.0	5.0
Receivables turnover (day	77.7	84.8	89.3	89.3	89.3
Payables turnover (days)	29.9	30.0	31.5	31.5	31.5
Capital structure					
Net Gearing (x)	net cash	net cash	0.3	0.3	0.4
Interest Cover (x)	11.1	19.9	36.1	29.4	14.2

Quarterly Profit & Loss

FYE 31 Dec (RMm)	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17
Revenue	**69.5**	**82.6**	**73.5**	**74.6**	**71.0**
Op costs	(60.4)	(71.9)	(65.0)	(62.8)	(61.2)
EBITDA	**9.2**	**10.7**	**8.6**	**11.8**	**9.8**
Depn and amort	(2.8)	(2.7)	(2.7)	(2.7)	(2.6)
EBIT	6.3	7.9	5.9	9.2	7.2
Net int income/(exp)	(0.7)	0.1	(0.7)	(0.2)	(0.3)
EI	-	-	-	(2.4)	-
Inc from associates	-	-	-	-	-
Pretax profit	**5.7**	**8.0**	**5.2**	**6.5**	**6.8**
Tax	(1.2)	(2.6)	(1.2)	(0.3)	(2.0)
MI	-	-	-	-	-
Net profit	**4.5**	**5.4**	**4.0**	**6.2**	**4.9**
Core net profit	4.5	5.4	4.0	8.6	4.9
Margins (%)					
EBITDA	13.2	12.9	11.6	15.9	13.8
PBT	8.2	9.7	7.1	8.8	9.6
PAT	6.4	6.6	5.4	8.3	6.8

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

This report is intended for information purposes only and has been prepared by Affin Hwang Investment Bank Berhad (14389-U) ("the Company") based on sources believed to be reliable. However, such sources have not been independently verified by the Company, and as such the Company does not give any guarantee, representation or warranty (express or implied) as to the adequacy, accuracy, reliability or completeness of the information and/or opinion provided or rendered in this report. Facts, information, views and/or opinion presented in this report have not been reviewed by, may not reflect information known to, and may present a differing view expressed by other business units within the Company, including investment banking personnel. Reports issued by the Company, are prepared in accordance with the Company's policies for managing conflicts of interest arising as a result of publication and distribution of investment research reports. Under no circumstances shall the Company, its associates and/or any person related to it be liable in any manner whatsoever for any consequences (including but are not limited to any direct, indirect or consequential losses, loss of profit and damages) arising from the use of or reliance on the information and/or opinion provided or rendered in this report. Any opinions or estimates in this report are that of the Company, as of this date and subject to change without prior notice. Under no circumstances shall this report be construed as an offer to sell or a solicitation of an offer to buy any securities. The Company and/or any of its directors and/or employees may have an interest in the securities mentioned therein. The Company may also make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

Comments and recommendations stated here rely on the individual opinions of the ones providing these comments and recommendations. These opinions may not fit to your financial status, risk and return preferences and hence an independent evaluation is essential. Investors are advised to independently evaluate particular investments and strategies and to seek independent financial, legal and other advice on the information and/or opinion contained in this report before investing or participating in any of the securities or investment strategies or transactions discussed in this report.

Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data.

The Company's research, or any portion thereof may not be reprinted, sold or redistributed without the consent of the Company.

The Company, is a participant of the Capital Market Development Fund-Bursa Research Scheme, and will receive compensation for the participation.

This report is printed and published by:
Affin Hwang Investment Bank Berhad (14389-U)
A Participating Organisation of Bursa Malaysia Securities Berhad

22nd Floor, Menara Boustead,
69, Jalan Raja Chulan,
50200 Kuala Lumpur, Malaysia.

T : + 603 2146 3700
F : + 603 2146 7630
research@affinhwang.com

www.affinhwang.com