Sharekhan by BNP PARIBAS

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Mahindra Logistics Ltd

Weak Q2; Retain Buy on expected growth revival

Logistics	Sharekhan code: MAHLOG

Reco/View: Buy	↔	CMP: Rs. 362	Price Target: Rs. 455	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

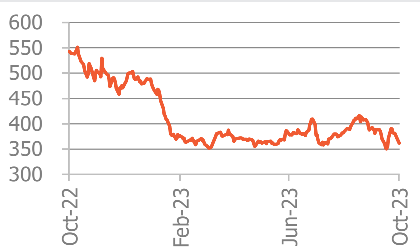
Company details

Market cap:	Rs. 2,604 cr
52-week high/low:	Rs. 559/347
NSE volume: (No of shares)	1.4 lakh
BSE code:	540768
NSE code:	MAHLOG
Free float: (No of shares)	3.0 cr

Shareholding (%)

Promoters	58.0
FII	12.1
DII	14.6
Others	15.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-7.9	-4.1	-1.0	-33.4
Relative to Sensex	-4.9	-0.6	-7.5	-41.0

Sharekhan Research, Bloomberg

Summary

- We retain a Buy on Mahindra Logistics Limited (MLL) with an unchanged PT of Rs. 455, rolling forward our valuation to September 2025 earnings and factoring lowered estimates.
- Consolidated revenues marginally missed mark in Q2, while weak operational performance and net loss widened q-o-q. Freight forwarding and express businesses disappointed.
- Company expects 3PL growth momentum to continue although challenges in freight forwarding and express business are expected to continue in the near term.
- Express business is eyeing an EBITDA breakeven by Q4FY2024 although it could get delayed if the company is not able to ramp up volume shortfall.

Mahindra Logistics Limited (MLL) reported a marginally lower consolidated revenues at Rs. 1,365 crore (up 3% y-o-y) led by consolidation of Rivigo's express business (absent in the base quarter) and sequential recovery (up 8% q-o-q, down 5% y-o-y) in its core standalone business (mainly 3PL). Consolidated OPM at 3.9% (-117 bps y-o-y) came in much lower than our estimate of 5.3%. stayed in line with expected operating losses of the Express business. Operating loss in freight forwarding (softening ocean freight rates and volume deferment from Telecom players related to 5G rollout), higher operating loss in express business (lower utilization and high transportation costs to maintain service levels) and a sequential dip in 3PL margins (mix change and one-time impairment) led to negative surprise on consolidated OPM. Overall, it reported a 21% y-o-y dip in operating profit and q-o-q rise in net loss to Rs. 15.9 crore. MLL's 3PL business is expected to maintain momentum although challenges in freight forwarding and express business are expected to continue in the near term.

Key positives

- MLL added Rs. 100 crore annualized business in Q2FY2024 maintaining momentum (Rs. 130 crore/ Rs. 100 crore annualised business added in Q1FY2024/Q4FY2023) in the contract logistics segment.
- Mobility business registered a 35% y-o-y growth in revenues. The segment remained PAT positive in Q2FY2024 in line with its target of being PAT positive for FY2024.

Key negatives

- Express business continued to report operating and net losses on lower volumes and higher transportation costs incurred to maintain service levels. It hopes to break even by Q4FY2024-end, which may get delayed.
- Freight forwarding business reported 50% y-o-y dip in revenues along with operating loss.

Management Commentary

- The 3PL business is expected to maintain positive momentum. It has completed mobility business turnaround. The last mile business is on improving trajectory. The freight forwarding and Express businesses are facing key challenges which will be overcome through focus on volume growth.
- For the Express business, it hopes to break even at operating level by Q4FY2024 end. It has to do 20-25% volume recovery (average 4-5% m-o-m growth) in H2FY2024.
- Its warehouse expansions in Chakan, Kolkata, Nasik, and Guwahati are on track and is expected to add 2.3 msf over the next 15 months.

Revision in estimates – We have lowered our earnings estimates materially for FY2024-FY2025 factoring operating losses in express business and slower recovery in freight forwarding business.

Our Call

Valuation – Retain Buy with an unchanged PT of Rs. 455: MLL is expected to benefit from healthy momentum in its core 3PL business although near-term challenges persist in freight forwarding and express business. It remains focused on improving volumes in its freight forwarding and Express business which would lead to an improvement in operational profitability. Further, it targets to increase the share of solutions business in 3PL vertical, which would provide better margins. It remains committed on adding 2.3 msf of warehousing capacities in the next 15 months. We have introduced our FY2026E earnings in this note. The stock has seen a correction of over 10% over the trailing two months. We believe the current valuation at a P/E of 46x/24x its FY2025E/FY2026E earnings aptly factors its transitioning-related uncertainties providing an opportunity to Buy. Hence, we retain Buy on the stock with an unchanged PT of Rs. 455, rolling forward our valuation multiple to September 2025 earnings and factoring downwardly revised estimates.

Key Risks

Weakness in the automobile industry's outlook is a key downside risk to our call.

Valuation (Consolidated) Rs cr

Particulars	FY23	FY24E	FY25E	FY26E
Revenue	5,128.3	5,780.9	6,475.6	7,257.3
OPM (%)	5.1	4.9	5.8	6.4
Adjusted PAT	26.3	(4.0)	56.4	109.4
% YoY growth	49.6	-	-	93.9
Adjusted EPS (Rs.)	3.6	(0.6)	7.8	15.2
P/E (x)	99.1	-	46.1	23.8
P/B (x)	4.1	4.1	3.8	3.3
EV/EBITDA (x)	9.1	8.3	6.4	5.1
RoNW (%)	4.7	(0.7)	9.6	16.4
RoCE (%)	5.8	5.2	11.5	16.7

Source: Company; Sharekhan estimates

Weak Freight forwarding and express business widens net loss q-o-q

Mahindra Logistics reported a 2.9% y-o-y rise (up 5.5% q-o-q) in consolidated revenues at Rs. 1365 crore which was 3% lower than our estimate. Standalone revenues (Supply chain management business) showed an improvement q-o-q (up 8% q-o-q, down 5% y-o-y) while Mobility (up 9% q-o-q), Express (up 3% q-o-q) and 2x2 Logistics (up 3% q-o-q) improved sequentially. Freight forwarding business was weak (down 50% y-o-y, down 32% q-o-q) owing to softness in freight rates and global uncertainty. The company's OPM at 3.9% (-117 bps y-o-y, -123bps q-o-q) was much below our estimate of 5.3%. OPM expansion in standalone and mobility businesses was offset by operating losses in express business and freight forwarding. Consequently, the consolidated operating profit declined by 20.7% y-o-y (down 19.6% q-o-q) to Rs. 53.6 crore, which was 28% lower than our expectation. Weak operational performance along with higher depreciation (up 19% y-o-y) and higher interest expense (up 54% y-o-y) led to consolidated net loss of Rs. 15.9 crore as against net profit of Rs. 12.2 crore in Q2FY2023 and net loss of Rs. 8.6 crore in Q1FY2024. Its warehouse space under management stood at 19 million sq ft in the 3PL business. The expansions in Chakan, Kolkata, Nasik, and Guwahati remain on track. It launched 6.5 lakh sq. ft. multi-client warehouse in Bhiwandi, Mumbai to manage the fulfilment and distribution for automotive, e-commerce and FMCG industries.

Key conference call takeaways -

- **Outlook:** The 3PL business is expected to maintain positive momentum. It has completed mobility business turnaround. The last-mile business is on improving trajectory. The freight forwarding and express business are facing key challenges, which will be overcome through focus on volume growth. The EBITDA breakeven target for express business may get delayed from Q4FY2024 end if it is not able to recover volumes. It is not looking for any inorganic growth.

- **End-user sector outlook:** Within Auto, passenger vehicles grew 9% y-o-y to 1.8 million vehicles in H1FY2024 while commercial vehicles is seeing some uptick in sentiments. For consumer durables, it was a mixed quarter. Rising temperature and weaker monsoon led to RAC demand while lighting and fans remained weak. Premium kitchen appliances kept growing. In FMCG, rural market did not see significant change although it was expected to see uptick. Distribution restructuring, expanding network and rise in omnichannel presence are positive signs. E-commerce segment has been witnessing some slowdown in the recent past although greenshoots were seen in this quarter.

- **3PL:** Contract logistics volumes remained robust leading to 6% q-o-q growth. The churn impact in E-commerce due to mid mile consolidation was overtaken. The company received Rs. 100 crore order intake in Q2 continuing momentum from Q1. It commissioned 6.5 lakh sq ft Bhiwandi warehouse during Q2. It has an 18.1 msf warehousing capacity in 3PL alone. Cost reduction helped improvement in GMs y-o-y although change in revenue mix (warehousing stayed flat q-o-q) and one-time impairment (~20-25 bps impact on GMs) related to foreclosure of site in E-com business affected GMs q-o-q.

- **Freight forwarding:** The business had a tough quarter. Pressure on ocean freight, high competitive intensity and deferment of volumes from Telecom sector related to 5G roll-out affected the segment. It focuses on volume growth. It commenced air charter services in Dubai from September 1, 2023. It expects domestic pricing bottoming out.

- **Express business:** Revenues were stable and realisations per kg were stable q-o-q. It delivered 3% q-o-q volume growth. It signed new contracts during fag-end, which would have led to 9% q-o-q growth. It added seven new retail partners and twelve new customers. It invested in getting service level back by reducing turnaround around time (TAT) while loads were not there leading to increase in transportation costs significantly. It has to get back 30% volumes to get back to EBITDA breakeven. It hopes to break even at operating level by Q4FY2024 end. It has to do 20-25% volume recovery (average 4-5% m-o-m growth) in H2FY2024.

- **Mobility:** During H1FY2024, domestic air passenger traffic grew 142% y-o-y to 113 million passengers. B2C saw strong traction in air traffic movement. Return to work from office is also aiding volumes. The company has 20-22% market share in seven cities it operates. The company operates 6000 cabs in 14 cities and has 350 business partners. The segment reported PAT positive in Q2. It remains on track to achieve PAT positive for FY2024.
- **Warehouse expansion:** Its expansions in Chakan, Kolkata, Nasik, and Guwahati are on track and is expected to add 2.3 msf over the next 15 months

Results (Consolidated) — Rs cr

Particulars	Q2FY2024	Q2FY2023	y-o-y%	Q1FY2024	q-o-q%
Net sales	**1364.8**	**1326.3**	**2.9%**	**1293.2**	**5.5%**
other income	6.6	3.4	96.4%	6.2	6.5%
Total income	1371.3	1329.7	3.1%	1299.4	5.5%
Total expenses	1311.2	1258.7	4.2%	1226.6	6.9%
Operating profit	**53.6**	**67.6**	**-20.7%**	**66.6**	**-19.6%**
Depreciation	51.8	43.6	18.9%	54.5	-4.9%
Interest	16.5	10.7	53.9%	17.8	-7.0%
Exceptional items	0.0	0.0		0.0	
Profit Before Tax	**-8.2**	**16.6**	**-**	**0.6**	**-**
Taxes	7.3	4.7	53.8%	8.9	-17.8%
PAT	-15.5	11.9	-	-8.3	-
Minority Interest	0.3	-0.9	-	0.1	-
Adjusted PAT	**-15.9**	**12.2**	**-**	**-8.6**	**-**
EPS (Rs.)	-2.2	1.7	-	-1.2	-
			BPS		**BPS**
OPM (%)	3.9%	5.1%	-117 bps	5.2%	-123 bps
NPM (%)	-1.2%	0.9%	-	-0.7%	-
Tax rate (%)	-	28.5%	-	-	-

Source: Company Data, Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Strong growth outlook led by changing consumer preferences and macro pick-up

The logistics industry had been one of the key sectors which showed a strong revival post-COVID-19 pandemic that affected the overall trade environment domestically and globally. Domestic indicators such as e-way bill generations, FASTag collections, Indian rail volumes, domestic port volumes, and foreign trade are showing clear signs of revival. Further, organised domestic logistics players have improved their business, led by user industries' preferences towards credible supply chain management in the wake of the impact of COVID-19 on supply chain operations. Further, the third-party logistics (3PL) industry has seen faster improvement in operations, led by segments such as e-commerce, pharma, and FMCG. Hence, we have a positive view of the sector.

■ Company Outlook – On growth recovery path

MLL continues to focus on improving the margin profile of its network services businesses post the acquisitions in various sub-segments. However, its 3PL business remains on a healthy growth trajectory with mid-teen revenue CAGR expectations over the next 2-3 years. It has been able to bag new order intakes in the contract logistics businesses which is expected to start contributing post 3-6 months' time for deploying services. Further, its freight forwarding business is on a recovery path, with a healthy volume growth while the same gets partially offset by weaker pricing environment in the near term. Overall, we believe the company is on track to regain higher growth trajectory over the next 2-3 years.

■ Valuation – Retain Buy with an unchanged price target of Rs. 455

MLL is expected to benefit from healthy momentum in its core 3PL business although near-term challenges persist in freight forwarding and express business. It remains focused on improving volumes in its freight forwarding and Express business which would lead to an improvement in operational profitability. Further, it targets to increase the share of solutions business in 3PL vertical, which would provide better margins. It remains committed on adding 2.3 msf of warehousing capacities in the next 15 months. We have introduced our FY2026E earnings in this note. The stock has seen a correction of over 10% over the trailing two months. We believe the current valuation at a P/E of 46x/24x its FY2025E/FY2026E earnings aptly factors its transitioning-related uncertainties providing an opportunity to Buy. Hence, we retain Buy on the stock with an unchanged PT of Rs. 455, rolling forward our valuation multiple to September 2025 earnings and factoring downwardly revised estimates.

Peer Comparison

Particulars	P/E (x)		EV/EBITDA (x)		P/BV (x)		RoE (%)	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Mahindra Logistics	46.1	23.8	6.4	5.1	3.8	3.3	9.6	16.4
TCI Express	25.3	21.2	17.6	14.7	5.7	4.7	25.3	24.4

Source: Sharekhan Research

About the company

MLL is a portfolio company of Mahindra Partners, the $1 billion private equity division of the $ 19 billion Mahindra Group. MLL is an integrated third-party logistics (3PL) service provider specialising in supply chain management and people transport solutions. Founded over a decade ago, MLL serves over 300 corporate customers across various industries, such as automobiles, engineering, consumer goods, and e-commerce. The company pursues an asset-light business model under which assets necessary for its operations, such as vehicles and warehouses, are owned or provided by an extensive network of business partners on lease rentals. At the same time, MLL largely invests in logistics technology. The company provides customised and technology-enabled solutions across the supply chain and people transport operations.

Investment theme

MLL has gathered pace in both of its key verticals, viz. M&M SCM and non-M&M SCM businesses are expected to sustain going forward. The company continues to focus on providing integrated logistics solutions and has been able to add new clients and warehousing capacities each quarter. Further, MLL's venture into last-mile small package deliveries through EV would capture the strong growth in the express delivery segment. The company continues to generate strong cash flows following its asset-light model.

Key Risks

- Slowdown in the automotive industry can affect financials due to its high dependency.
- Changes in the supply chain strategy of Mahindra Group can negatively affect its financials due to its high dependency.
- The industry is highly competitive and fragmented, with low entry barriers.

Additional Data

Key management personnel

Anish Shah	Chairman
Rampraveen Swaminathan	Chief Executive Officer & MD
Ruchie Khanna	Company Secretary & Compliance Officer

Source: BSE

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mahindra & Mahindra Ltd	58.4
2	Reliance Capital Trustee Co Ltd	4.7
3	First State Investments ICVC	3.9
4	Goldman Sachs Group Inc/The	2.5
5	Invesco Trustee Private	1.9
6	Bhanshali Akash	1.9
7	Motilal Oswal FOC Emerg FD	1.3
8	Federated Hermes	1.0
9	Motilal Oswal Asset Management	0.9
10	Frostrow Capital LLP	0.9

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/ weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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