

COMPANY NOTE

SITC International Holdings Co., Limited [1308.HK, HK\$8.30, NOT RATED] –

A defensive play in a volatile market

Analyst: Kelly Zou (kellyzou@chinastock.com.hk; Tel: (852) 3698 6319)

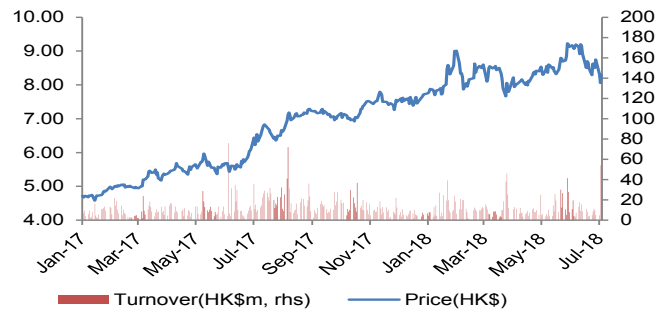
Event: We met SITC on 3 July as part of our initiative to explore key beneficiaries of China's industry transfer to overseas markets, especially to ASEAN to avoid a potential US trade war. SITC has a unique business model, as 1) it offers integrated sea freight and land-based logistics services, making it more of a logistics company than a shipping company; and 2) its business concentrates only on the intra-Asia trade market. Amid huge market volatility, SITC's share price still rose 7.6% CYTD. The market appreciates its unique value of business concentration in the intra-Asia market, which should be less affected by higher potential US trade tariffs. We expect steady intra-Asia trade volume growth, led by 1) the accelerating relocation of China industries to ASEAN countries, and 2) the Belt and Road initiative. We think the US trade war will push Chinese companies to accelerate their relocation pace to ASEAN countries. SITC management guided stable intra-Asia trade volume growth of 5-6% p.a. in 2018-2019E. Given tight industry supply, freight rates should remain firm, as SITC can easily pass fuel price hikes on to its customers. Consensus earnings growth is c15% p.a. in 2018-2019E. The stock currently trades at 13.0x 2018E and 11.3x 2019E PER, one standard deviation above its average trading forward PER. The share price is also supported by its high dividend yield of 5-6%.

Steady intra-Asia trade volume growth well supported by China's industry transfer: Intra-Asia trade volume growth is well supported by 1) free trade agreements and bilateral economic cooperation between China, Japan and ASEAN countries, 2) regional integration, and 3) direct investment by Japanese and Chinese companies in ASEAN countries. China's trade with other Asian countries grew at a CAGR of 12.8% from 2000 to 2017, accounting for >50% of its total foreign trade. We expect steady intra-Asia trade volume growth in the long term, driven by 1) more Chinese companies moving to ASEAN countries, and 2) the Belt and Road initiative. China's direct investment in the ASEAN market grew from US\$275m in 2009 to US\$3.5bn in 2016. The ratio of China's investment in ASEAN manufacturing as a percentage of its total investment in ASEAN countries rose from 10.2% in 2009 to 34.5% in 2016. Chinese companies have started to relocate to ASEAN countries, as they see 1) lower labour costs, and 2) greater potential penetration of local markets for their business. Given the potential US trade war, we expect Chinese companies to accelerate their relocation pace to ASEAN countries. Under the Belt and Road Initiative, the investment in infrastructure and local industries will further drive trade volume development in the intra-Asia trade market.

Better positioned to benefit from the rising intra-Asia logistics needs of Chinese companies: SITC focuses only on the intra-Asia trade market. It has a unique business model, offering integrated sea freight and land-based logistics services to its customers, which makes it more of a logistics company than a shipping company. It provides high-frequency container shipping services in its high-density intra-Asia route network (Fig 21), which gives it a competitive edge in building relationships with numerous Fortune 500 companies for their intra-Asia logistics needs. As at the end of 2017, SITC ran 77 vessels and operated 63 trade lanes. Its high-frequency sea-freight logistics services make 388 port calls per week. With its high-frequency service network and long track record in the intra-Asia market, it should benefit the most from the growing intra-Asia logistics transportation market as more Chinese companies relocate to ASEAN countries.

Favorable industry supply conditions to secure SITC's earnings growth in 2018-2019E: SITC reported total revenue growth of 10.9% YoY and net profit growth of 53.6% YoY in 2017, led by 1) container shipping volume

SITC International Holdings Company Limited



Market Cap: US\$2,819m; Free Float: 47.0%

US\$ m	2015	2016	2017	2018E	2019E
Revenue (m)	1,288	1,216	1,348	1,456	1571.5
YoY chg (%)	-6.5	-5.6	10.9	7.9	8.0
Gross profit (m)	186	200	252	306	340
GPM (%)	14.4	16.4	18.7	21.0	21.6
Operating profit (m)	139	133	182	210	233
Operating profit margin (%)	10.8	10.9	13.5	14.4	14.8
Net profit (m)	143	123	189	215	240
Net margin (%)	11.1	10.1	14.0	14.7	15.3
EPS (Rmb)	0.05	0.05	0.07	0.08	0.09
YoY chg (%)	17.8	-14.5	52.2	14.6	14.6
ROE (%)	16.9	14.0	19.7	21.2	22.7
Dividend yield (%)	3.2	3.1	4.8	5.4	6.2
PER (x)	19.4	22.6	14.9	13.0	11.3
PBR (x)	3.3	3.2	2.9	2.7	2.6

Source: Bloomberg, Company data, CGIS Research

growth, 2) freight rate hikes, and 3) improved operating efficiency. The Company guided that its shipping volume growth will remain stable at around 5-6% p.a. in 2018-2019E. Freight rates are also expected to remain firm in 2018-2019E, given tight industry supply conditions. Tougher global emission limits for shipping from 2020 will push a surge in the scrapping of older, less fuel-efficient vessels within the next 2 to 3 years, as the enhanced International Maritime Organization regulations come into force. For intra-Asia trade lanes, the number of vessels over 20 years old account for over 20% of total fleet capacity. Fuel price hikes will cause higher vessel charter costs and bunker costs. But with tight industry supply, SITC can easily pass through the cost hikes to its customers. Consensus revenue growth is around 8% p.a. in 2018-2019E, and consensus earnings growth is 14.6% p.a. in 2019-2019E.

Valuation: SITC's share price rose 63.6% in 2017, led by strong earnings growth recovery in 2017. The share price has risen 7.1% CYTD vs. a decline of 7.6% in the HSI Index during the same period. The share price didn't fall along with the market, as the market appreciates the unique value of SITC's business concentration in the intra-Asia market, which should be less affected by a potential US trade war. With or without a US trade war, Chinese companies have started to expand to ASEAN countries. Given a potential US trade war, their business relocation pace will become even faster. SITC should be a key beneficiary of the rising intra-Asia logistics transportation market. Based on consensus earnings estimates, the stock currently trades at 13.0x 2018E and 11.3x 2019E PER, about one standard deviation above its historical trading average PER. The share price is well supported by its high dividend yield of 5-6%. SITC will keep its dividend payout ratio at 60-70% in 2018-2019E.

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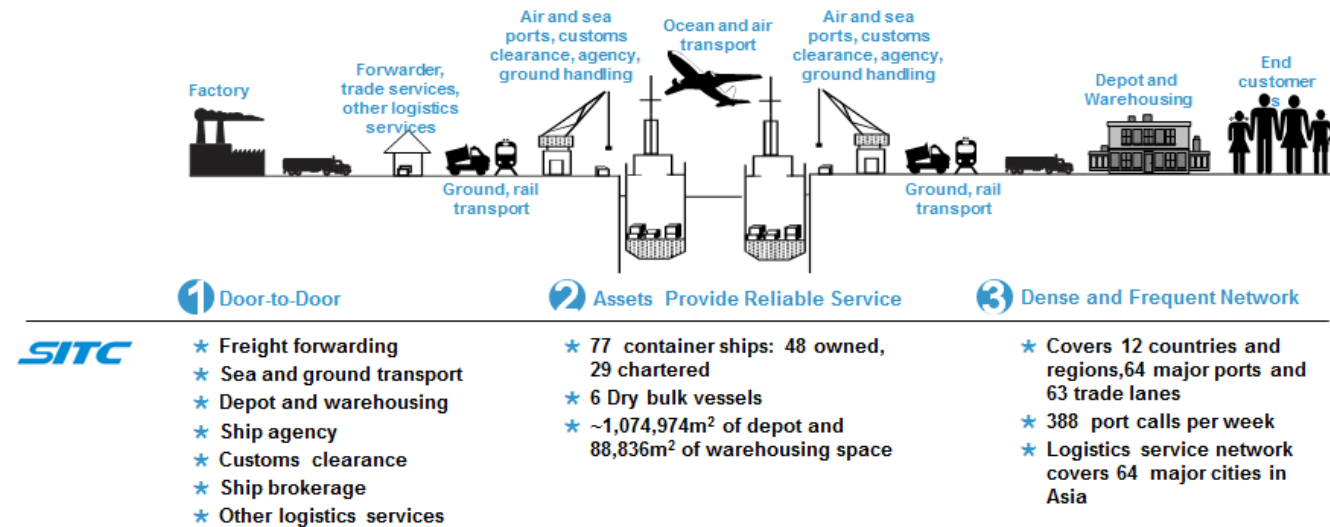
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Company profile

SITC International Holdings Co., Ltd. (SITC) is a leading container shipping logistics company, which provides integrated transportation and logistics solutions for the intra-Asia trade market. The Company, founded in 1991, started its business in freight forwarding. It moved up the value chain and started to provide container shipping services between China and Japan in 1992. Since then, it has become the leading container shipping service provider in the intra-Asia trade market. As at the end of 2017, SITC had 48 self-owned container vessels and 29 chartered container vessels, with total fleet capacity reaching 105,234 TEU, and operated 63 trade routes. At the end of 2017, the Company was ranked the 20th largest container shipping company in terms of shipping capacity. The Company has a unique market position in terms of its business concentration in the intra-Asia trade market. It is a key beneficiary of rising intra-Asia trading volume, led by 1) China's industry transfer to ASEAN countries, and 2) China's Belt and Road Initiative. Its integrated, high-frequency sea freight and land-based logistics services have helped it secure a stable business relationship with its customers and hence steady business growth. Compared to its peers, the Company also enjoys higher profitability because of 1) its unique services, integrating both sea freight and land-based logistics services, and 2) its single-type fleet structure.

Fig 1: SITC business model



Source: Company data, CGIS Research

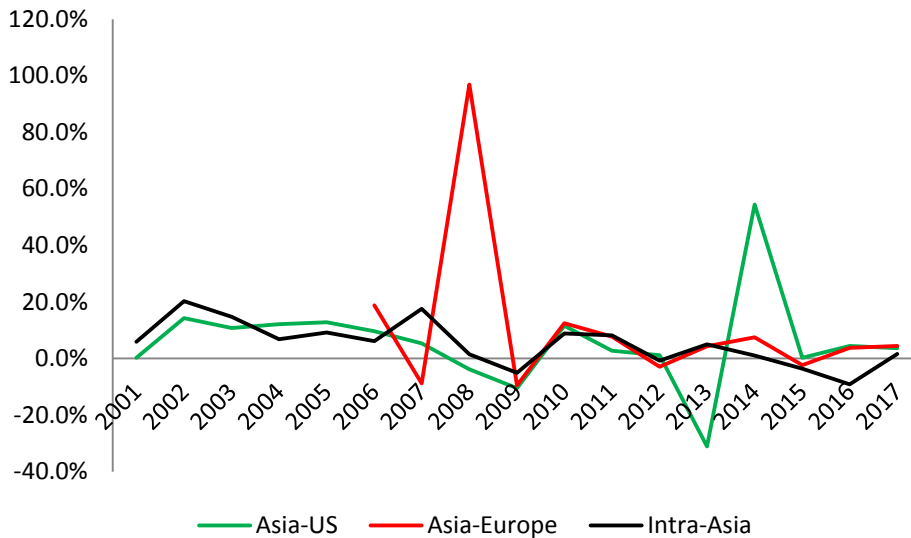
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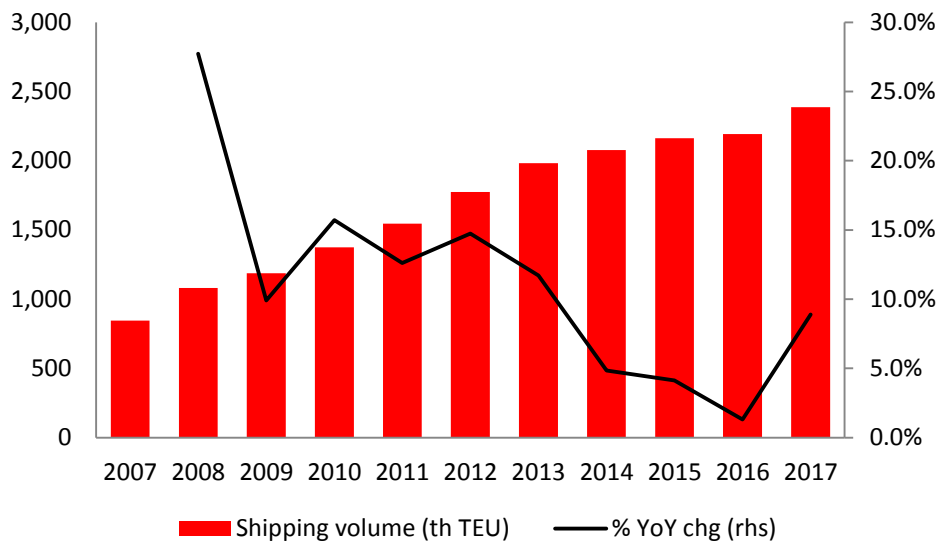
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Figure 2: Intra-Asia container shipping volume growth vs. Asia-US and Asia-Europe container shipping volume growth



Source: Japan Maritime Center, CGIS Research

Figure 3: SITC intra-Asia container shipping volume progression



Source: Company data, CGIS Research

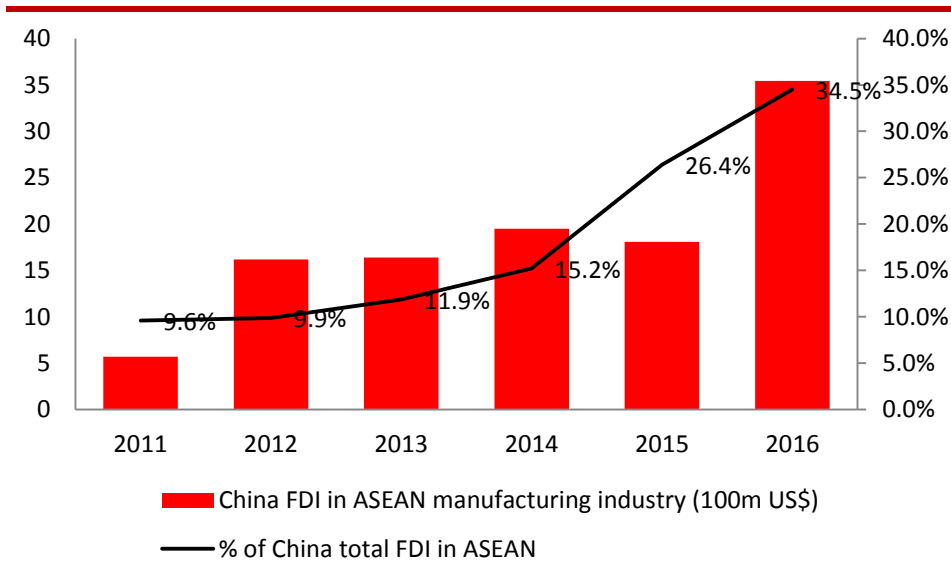
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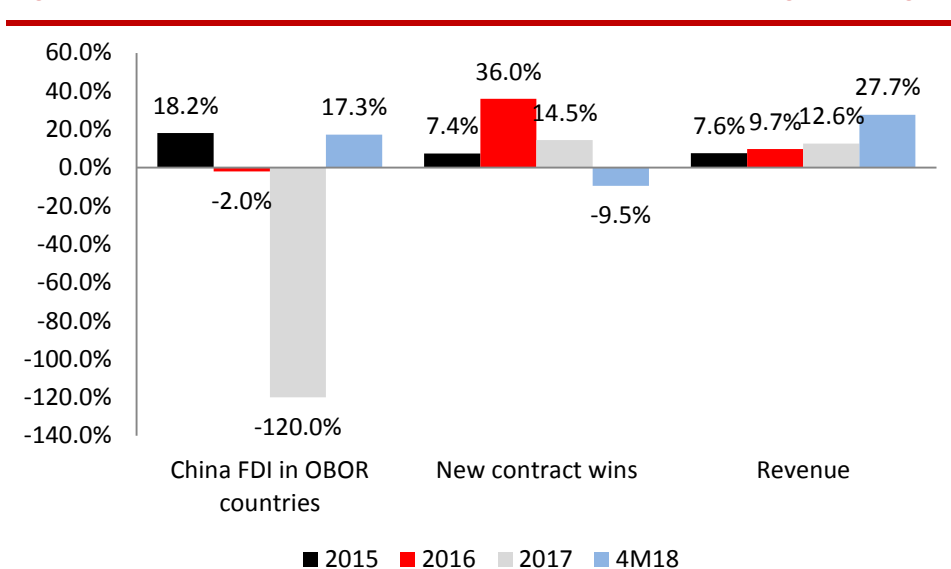
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Figure 4: China FDI in ASEA manufacturing industry in 2011-2016



Source: MOC, CGIS Research

Figure 5: China FDI, new contract wins and construction contracting revenue growth in OBOR countries (2015-4M2018)



Source: MOC, CGIS Research

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Figure 6: Sales and earnings growth, margins and ROE: SITC vs. other container shipping companies

	Ticker	Sales growth					EPS growth				
		2015	2016	2017	2018E	2019E	2015	2016	2017	2018E	2019E
H-share container shipping and logistics companies											
Cosco Shipping	1919 HK	-10.9%	21.6%	29.5%	12.2%	12.6%	40.8%	na	na	-43.5%	44.9%
OOIL	316 HK	-8.7%	-11.0%	15.3%	8.7%	7.5%	5.1%	na	na	5.0%	85.7%
SITC	1308 HK	-6.7%	-5.4%	10.9%	7.9%	8.0%	17.8%	-14.5%	52.1%	14.6%	14.6%
A-share logistics companies											
Cosco Shipping	601919 CH	-10.9%	21.6%	29.5%	13.5%	11.7%	40.8%	na	na	-8.1%	102.9%
Overseas container shipping and logistics companies											
Maersk	011200 KS	-14.9%	-20.5%	9.7%	na	na	na	-96.5%	19.2%	na	na
K Line	9107 JP	-8.0%	-17.2%	12.8%	-36.2%	2.0%	na	170.8%	na	-68.4%	95.6%
Nippon Yusen	9101 JP	-5.4%	-15.3%	13.5%	-17.2%	-0.4%	na	na	na	30.4%	36.0%
Mitsui OSK	9104 JP	-5.8%	-12.1%	9.8%	-27.2%	5.6%	na	na	na	na	49.2%
Evergreen Marine	2603 TT	-7.3%	-7.0%	21.0%	4.4%	5.9%	na	49.2%	na	-50.8%	35.4%
Wan Hai	2615 TT	-4.7%	-10.2%	6.0%	3.8%	-1.9%	-24.9%	-71.3%	125.5%	-9.6%	1.0%
Yang Ming	2609 TT	-5.4%	-9.5%	13.6%	2.3%	9.5%	na	92.3%	na	na	-71.3%
Hyundai Merchant	011200 KS	-14.9%	-20.5%	9.7%	na	na	na	-96.5%	19.2%	na	na
		Net profit margin					ROE				
		2015	2016	2017	2018E	2019E	2015	2016	2017	2018E	2019E
H-share container shipping and logistics companies											
Cosco Shipping	1919 HK	-1.0%	0.8%	-14.2%	2.9%	1.6%	1.8%	-42.3%	13.7%	19.0%	33.5%
OOIL	316 HK	4.1%	4.8%	-4.1%	2.3%	2.3%	6.0%	-4.7%	3.0%	3.0%	5.6%
SITC	1308 HK	11.1%	10.1%	14.0%	14.7%	15.3%	16.9%	14.0%	19.7%	21.2%	22.7%
A-share logistics companies											
Cosco Shipping	601919 CH	-1.0%	0.8%	-14.2%	2.9%	2.2%	1.8%	-42.3%	13.7%	12.2%	20.2%
Overseas container shipping and logistics companies											
Maersk	011200 KS	0.6%	-10.7%	-10.6%	-24.2%	na	na	-87.3%	na	na	na
K Line	9107 JP	2.0%	-4.1%	-13.5%	0.9%	0.5%	-12.9%	-48.5%	4.8%	1.3%	2.5%
Nippon Yusen	9101 JP	2.0%	0.8%	-13.8%	0.9%	1.5%	2.3%	-41.0%	3.8%	4.4%	6.1%
Mitsui OSK	9104 JP	2.3%	-10.0%	0.3%	-2.9%	2.4%	-25.7%	0.9%	-8.7%	5.5%	8.0%
Evergreen Marine	2603 TT	0.8%	-3.3%	-5.3%	4.7%	2.4%	-7.4%	-12.1%	12.2%	5.8%	7.9%
Wan Hai	2615 TT	7.8%	6.2%	2.0%	4.2%	4.2%	11.1%	3.3%	7.5%	7.2%	7.2%
Yang Ming	2609 TT	0.2%	-6.1%	-12.9%	0.2%	-2.5%	-22.5%	-63.7%	1.5%	-17.9%	10.4%
Hyundai Merchant	011200 KS	0.6%	-10.7%	-10.6%	-24.2%	na	na	-87.3%	na	na	na

Source: Company data, CGIS Research

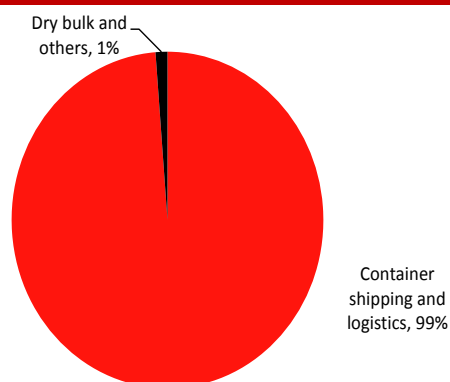
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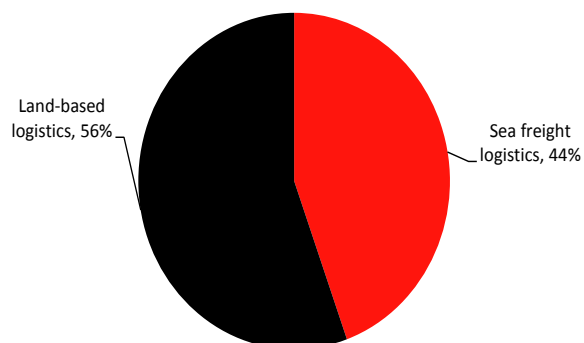
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Figure 7: SITC revenue mix in 2017



Source: Company data, CGIS Research

Figure 8: SITC revenue mix in 2016



Source: Company data, CGIS Research

Figure 9: SITC gross profit mix

	2016	2017		2015	2016
Container shipping and logistics	1,199	1,332	Sea freight logistics	990	969
Dry bulk and others	16	17	Land-based logistics	743	707
Total revenue	1,216	1,348	Inter-segment	-445	-460
			Total revenue	1,288	1,216
Container shipping and logistics	199	250	Sea freight logistics	61	79
Dry bulk and others	1	1	Land-based logistics	125	120
Total GP	200	252	Inter-segment	0	0
			Total GP	186	200
Container shipping and logistics	16.6%	18.8%	Sea freight logistics	6.1%	8.2%
Dry bulk and others	5.1%	7.4%	Land-based logistics	16.8%	17.0%
GPM	16.4%	18.7%	Inter-segment	0.0%	0.0%
			GPM	14.4%	16.4%

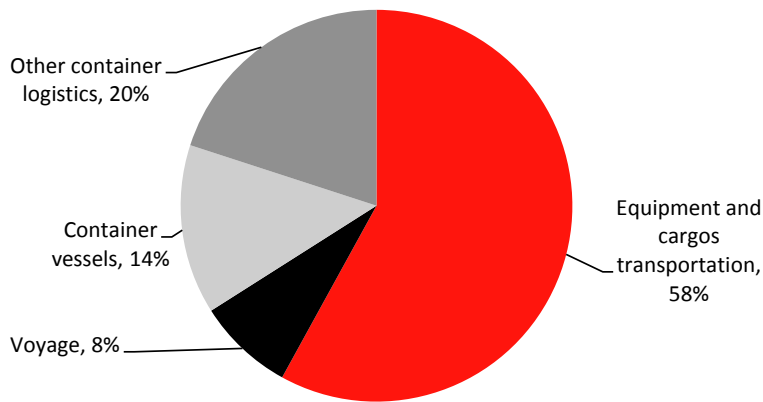
Source: Company data, CGIS Research

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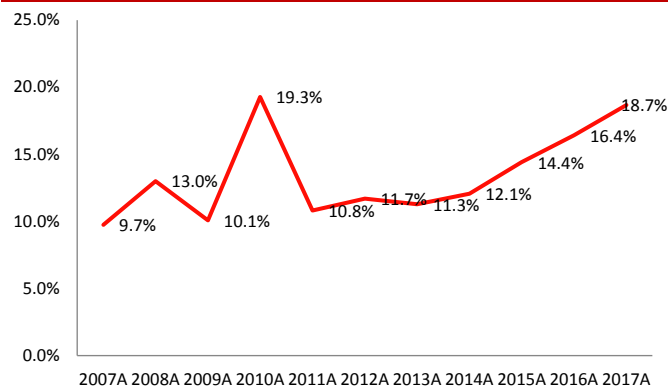
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Figure 10: SITC COGS structure



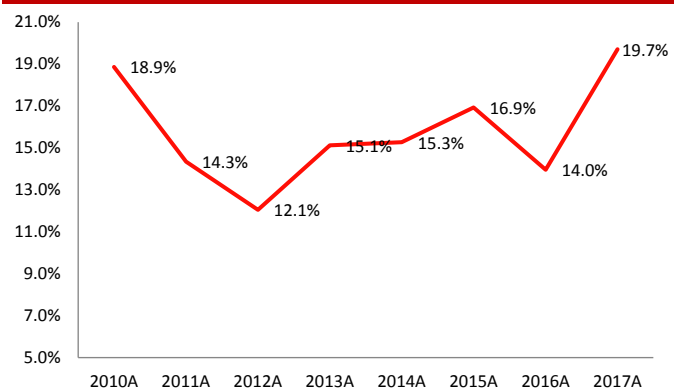
Source: Company data, CGIS Research

Figure 11: SITC gross profit margin trend



Source: Company data, CGIS Research

Figure 12: SITC ROE trend



Source: Company data, CGIS Research

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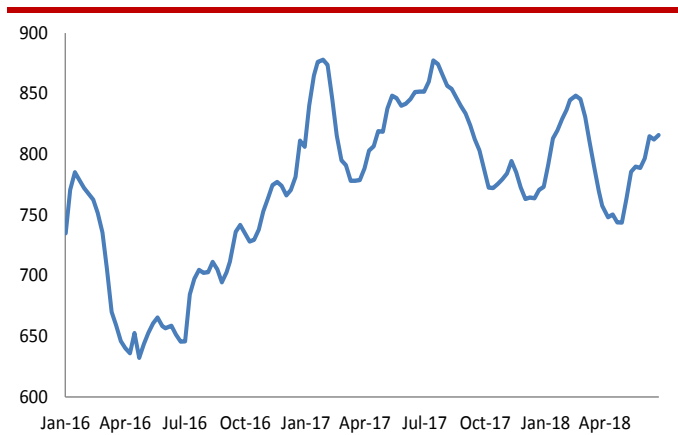
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Figure 13: WTI crude oil price (US\$/bbl)



Source: Bloomberg, CGIS Research

Figure 14: China Containerized Freight Index (US\$/TEU)



Source: Bloomberg, CGIS Research

Figure 15: JPYUSD exchange rate



Source: Bloomberg, CGIS Research

Figure 16: CNYUSD exchange rate



Source: Bloomberg, CGIS Research

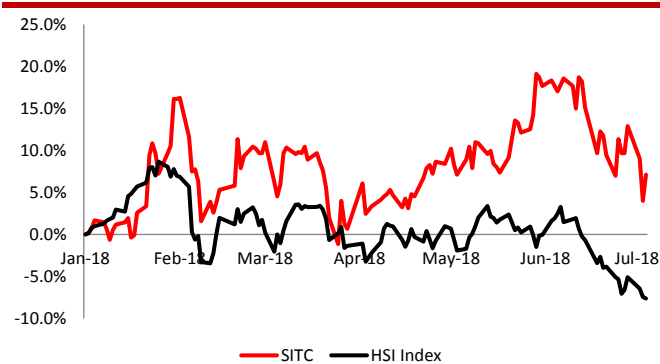
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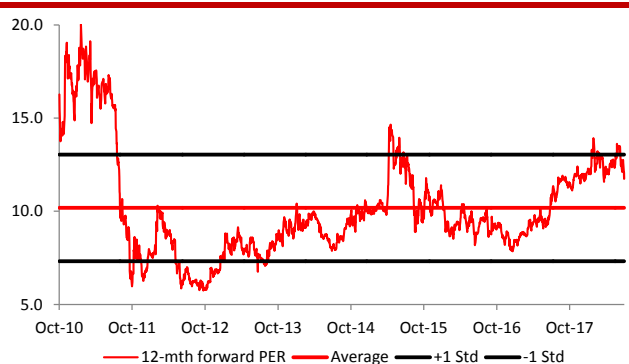
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Figure 17: SITC share price performance CYTD



Source: Bloomberg, CGIS Research

Figure 18: SITC 12-mth forward PER band



Source: Company data, Bloomberg, CGIS Research

Figure 19: Comp sheet

Ticker	Mkt cap	Price	PER			EPS growth			PEG	P/Bk			Dividend yield			ROE		
			2017	2018E	2019E	2017	2018E	2019E		2018E	2017	2018E	2019E	2017	2018E	2019E		
H-share container shipping and logistics companies																		
	US\$ m	(lc)																
Kerry Logistics	636 HK	2,297	10.62	8.5	11.9	10.8	12.6%	-28.5%	9.8%	-0.4	0.9	0.9	2.1%	2.3%	2.4%	11.1%	7.9%	8.1%
Cosco Shipping	1919 HK	6,566	3.35	10.9	19.3	13.3	na	-43.5%	44.9%	-0.4	1.4	1.2	0.0%	0.1%	0.3%	12.9%	6.5%	8.0%
OOIL	316 HK	6,232	78.15	45.5	43.4	23.4	na	5.0%	85.7%	8.7	1.3	1.3	0.0%	0.0%	0.0%	2.9%	3.0%	5.4%
SITC	1308 HK	2,819	8.30	14.9	13.0	11.3	52.2%	14.6%	14.6%	0.9	2.9	2.7	4.8%	5.4%	6.2%	19.7%	21.2%	22.7%
A-share container shipping and logistics companies																		
Cosco Shipping	601919 CH	6,566	4.75	18.3	19.9	9.8	na	-8.1%	102.9%	-2.5	2.3	2.1	0.0%	0.0%	0.0%	12.9%	10.4%	17.4%
S F Holding	002352 CH	28,534	42.91	38.3	36.1	28.9	5.7%	6.2%	24.9%	5.8	5.8	5.1	0.5%	0.5%	0.7%	15.1%	14.2%	15.5%
ZTO	ZTO US	14,722	20.22	30.4	23.9	19.1	45.7%	27.2%	25.0%	0.9	4.5	3.5	3.0	0.0%	23.3%	15.4%	14.6%	14.8%
YTO Express	600233 CH	5,075	11.90	23.3	19.0	16.0	-10.3%	22.6%	18.5%	0.8	3.6	3.1	2.6	0.9%	1.4%	1.6%	15.6%	16.1%
Yunda Holding	002120 CH	9,672	48.79	37.2	30.3	24.0	35.3%	22.7%	26.5%	1.3	11.4	6.1	4.9	0.5%	0.4%	0.4%	30.6%	20.2%
STO Express	002468 CH	3,794	16.45	17.0	13.8	11.7	-21.1%	22.7%	18.2%	0.6	3.7	2.9	2.3	1.2%	1.5%	1.7%	22.0%	20.7%
Best Inc	BSTI US	4,528	12.09	na	na	na	-96.5%	-83.1%	-769.4%	1.7	6.9	7.3	5.7	na	0.0%	0.0%	-28.0%	-5.1%
Overseas container shipping and logistics companies																		
Maersk	011200 KS	1,300	4,670	-0.7	na	na	19.2%	na	na	na	1.6	na	na	0.0%	na	na	na	na
K Line	9107 JP	1,607	1,893	17.0	54.0	27.6	na	-68.4%	95.6%	-0.8	0.8	0.8	0.8	0.0%	0.1%	1.0%	4.8%	1.5%
Nippon Yusen	9101 JP	3,194	2,078	17.4	13.3	9.7	na	30.4%	37.7%	0.4	0.6	0.6	0.6	1.4%	1.9%	2.4%	3.7%	4.7%
Mitsui OSK	9104 JP	2,805	2,573	-6.5	10.7	7.4	na	na	45.0%	-0.1	0.6	0.6	0.5	0.8%	1.8%	2.5%	-9.2%	5.4%
Evergreen Marine	2603 TT	1,694	12.90	6.5	13.3	9.8	na	-50.8%	35.4%	-0.3	0.8	0.8	0.7	1.6%	1.5%	2.4%	12.5%	5.9%
Wan Hai	2615 TT	1,220	16.80	14.6	16.2	16.0	125.5%	-9.6%	1.0%	-1.7	1.1	1.0	na	3.0%	4.8%	5.4%	7.5%	6.3%
Yang Ming	2609 TT	668	8.79	51.7	na	na	na	-75.7%	0.0	0.8	1.1	1.1	0.0%	0.0%	2.6%	1.5%	-14.4%	-3.6%
Hyundai Merchant	011200 KS	1,300	4,670	-0.7	na	na	19.2%	na	na	na	1.6	na	na	0.0%	na	na	na	na
Fedex	FDX US	60,821	227.61	13.6	13.0	11.4	49.4%	4.1%	14.4%	3.1	3.1	2.7	2.3	0.9%	1.1%	1.2%	23.1%	21.1%
UPS	UPS US	91,132	105.76	18.8	14.6	13.4	45.0%	28.4%	8.6%	0.5	90.8	21.8	12.8	3.1%	3.4%	3.6%	484.5%	149.0%

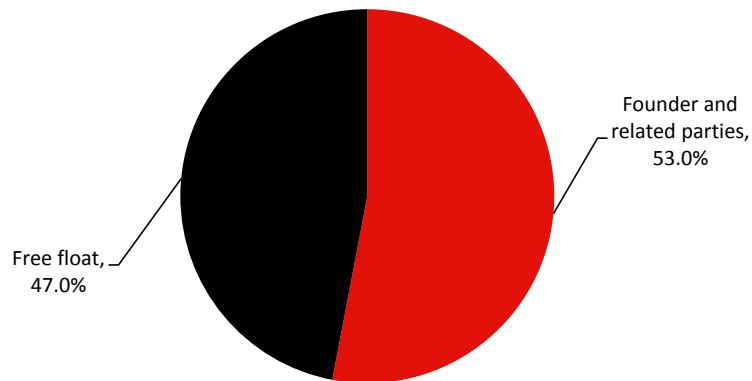
Source: Bloomberg, Company data, CGIS Research, Note: based on closing prices on 5 July 2018

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Figure 20: SITC shareholder structure as at the end of 2017



Source: Company data, CGIS Research

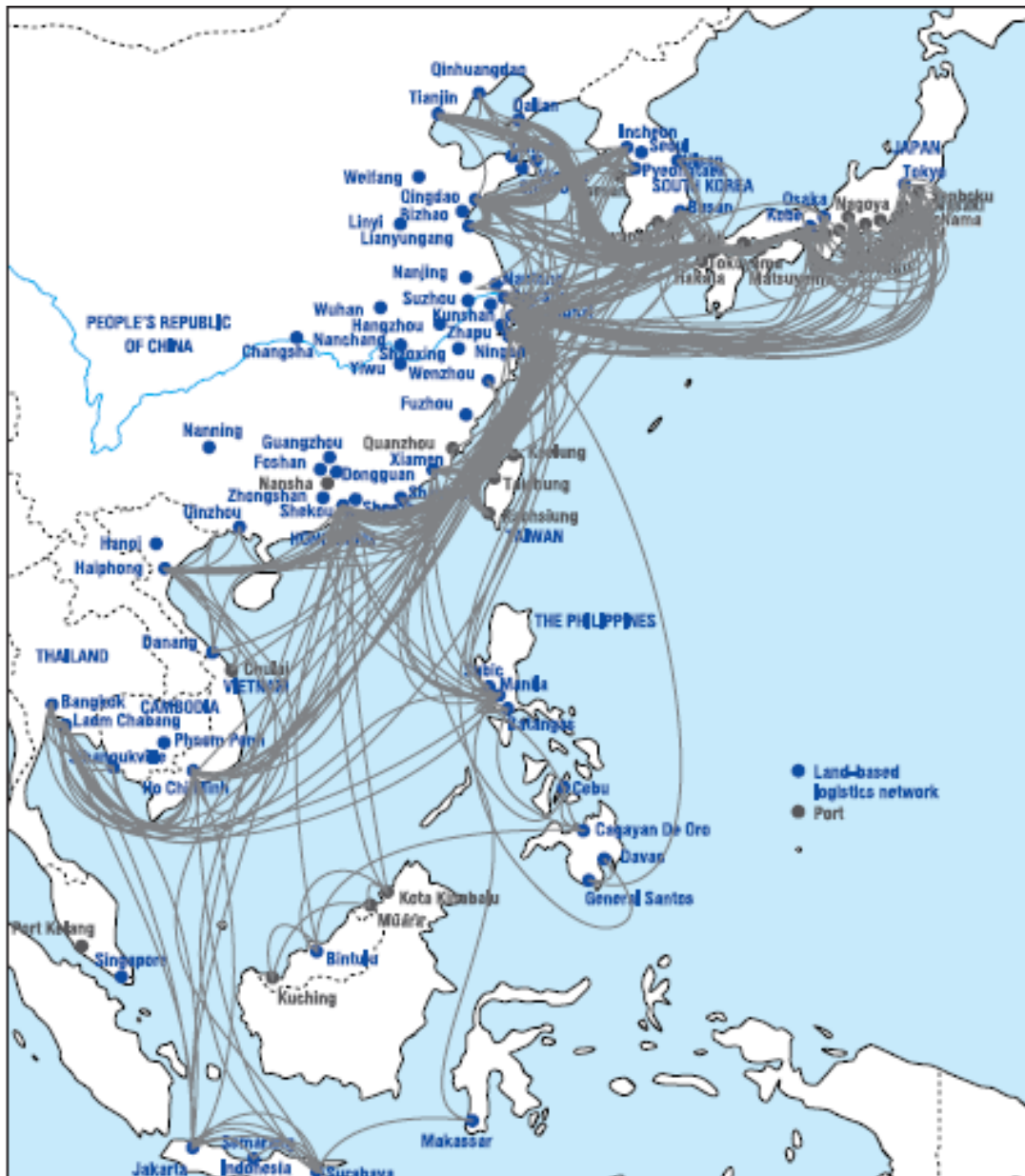
COMPANY NOTE

SITC International Holdings Co., Limited [1308.HK, HK\$8.30, NOT RATED] –

A defensive play in a volatile market

Analyst: Kelly Zou (kellyzou@chinastock.com.hk; Tel: (852) 3698 6319)

Figure 21: SITC's sea freight and land-based logistics service network



Source: Company data, CGIS Research

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20/F, Wing On Centre, 111 Connaught Road Central, Sheung Wan, Hong Kong. General line: 3698-6888.