STOCKS DOWN UNDER

20 SEP 2022

Emerging Stocks Down Under

Opportunities always look bigger after they have passed.

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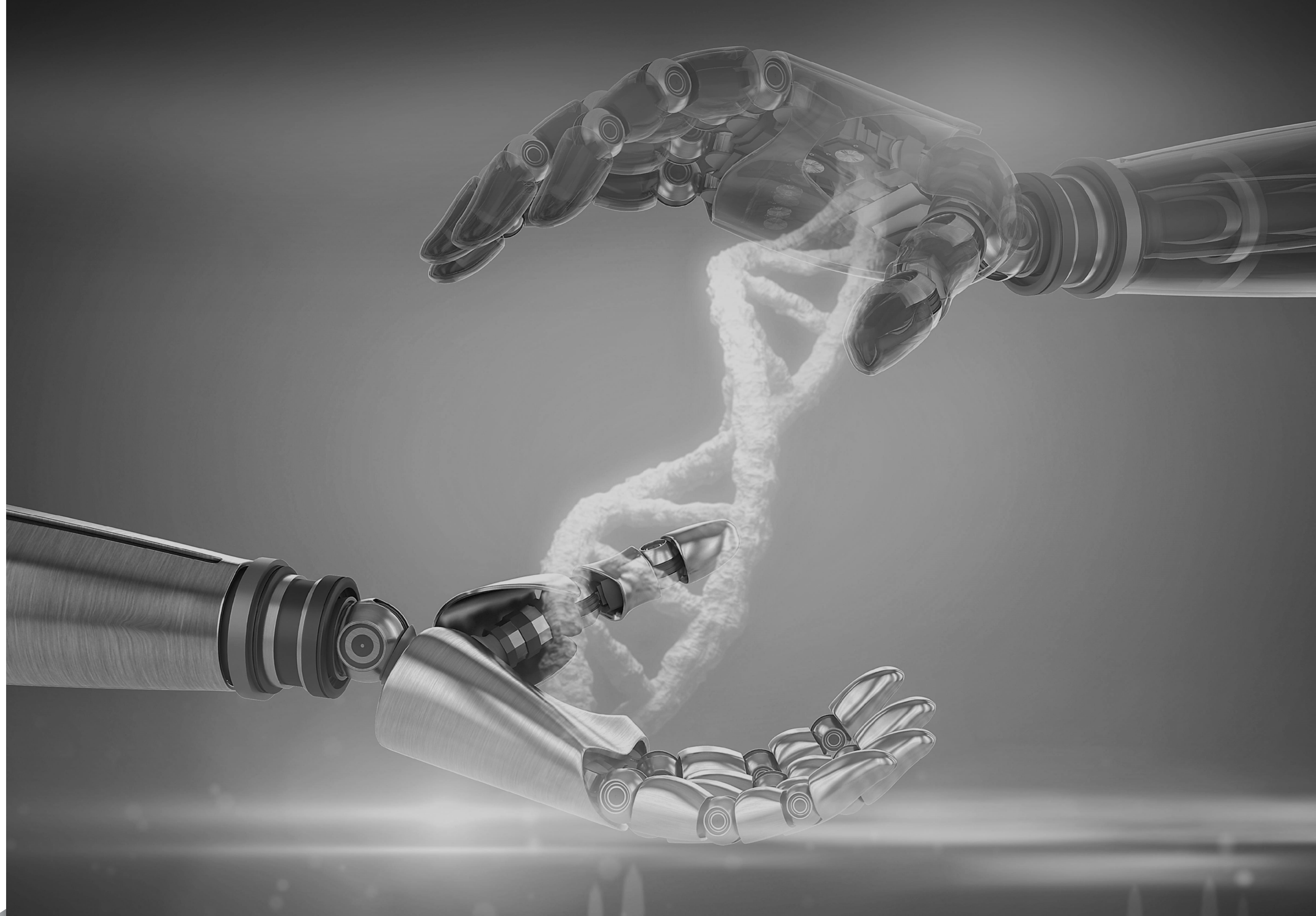

SILK LOGISTICS

Still smooth as silk?

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Stocks Down Under rating: ★★★★

ASX: SLH
Market cap: A$173.8M

52-week range: A$1.84 / A$2.68
Share price: A$2.20

Silk Logistics is a port to door logistics outfit that takes freight off big cargo ships, stores it in warehouses and then distributes the goods to wherever the customer wants. That may not sound like a particularly interesting industry, but it is more important than ever since the COVID-19 pandemic. And Silk's industry is one that made the company nearly $400m in revenue and a $15m+ profit.

Share price chart

Source: Tradingview

Missed out on Toll and WiseTech? Here's a chance

Silk began a decade ago through the merger of Kagan Logistics and Hoffman Transport, then owned by Gresham Private Equity. After a stint in the hands of Rich Lister Tony Gandel's private investment company, the current management team bought it out, undertaking a national expansion strategy and eventually listing on the ASX in July 2021 at $2 per share. Since listing, it has fluctuated, but never been below its IPO price.

Obviously, it helped that Silk was a profitable company, unlike many others that have listed since the pandemic. Also, the company's management had significant skin in the game - Brendan Boyd and CCO John Sood own 28% of the company between them. But logistics has been a great space to be in during the pandemic due to the growth in eCommerce. Silk is far from the only company in this industry, but investors have been starved for logistics companies since Toll was taken private in 2015. WiseTech (ASX: WTC), which provides logistics software, is one of the few companies left on the Australian bourse and has performed well since its own listing a few years ago.

Silk has some unique aspects compared to its competition. It has technology that tracks deliveries through a single visibility layer and consolidates multiple freight streams to a vehicle. Through this process, it collects data that customers can analyse to help strip out inefficiencies and costs. It targets recession-proof industries, such as agriculture, food and fast-moving consumer goods. Silk has 518 customers and employs 1,442 people across all five Australian mainland states. It has grown its total warehouse and container hardstand area significantly since the pandemic, to 426,973 and 171,047 square meters respectively.

Delivering the goods

Silk Logistics reported its FY21 results barely two months after listing, generating $323.3m in revenues (up 29%), an NPAT of $8.4m (up $12.7m) and a ROCE (return on capital employed) of 50.8% (up 2.6%). All of these figures were ahead of the company's prospectus forecasts. Another bumper result came last month, for FY22, with $394.7m in revenue (up 22%) and an NPAT of $15.8m (up 45%). It paid a dividend of 8.5cps, representing a yield of 4.2%.

There were plenty of other things to like in its results, including 23% revenue growth from its top 20 customers, $46.6m in new business wins and a 21-point improvement in its Net Promotor Score (NPS). And while some businesses with multiple segments can have results inflated by one or two divisions, this was not the case with Silk. Strong growth was recorded across its three divisions – Port Logistics, Contract Logistics and SLH Group. We note that Contract Logistics saw the greatest growth in revenue, although it also saw the biggest growth in expenses. EBITDA and EBIT margins fell by 4 and 1.3 basis points respectively whereas margin growth was recorded amongst its other divisions.

The company also recorded solid revenue growth across all states, although Victoria lagged the other states in recording just 11% growth whereas NSW recorded 30% and the others made 25% each.

We think it will deliver, but when will investors take note?

Of course, navel gazing at companies' past performance is all well and good, but ultimately pointless if solid performances cannot be continued into the future. Silk has told investors that it expects a further increase in revenue and earnings in FY23 subject to no adverse changes in the current market and economic conditions, but it did not provide specific guidance. Consensus estimates for FY23 broadly reflect management's view, but have been slightly braver, estimating $426.1m in revenue (up 8%) and EBITDA of $77.8m (up 11% from the $70.4m made in FY22). The company's valuation multiples look very reasonable at just 4.1x EV/EBITDA, 6.9x P/E and 0.2x PEG.

While investors are not sitting on losses, like many shareholders of other companies that listed in 2021 are, they might be forgiven for wanting more growth in the company's share price. We think more investors will recognise the company if it can deliver again in FY23 and show that the increase in global freight during the pandemic is permanent and not just temporary. Silk has done little Investor Relations work relative to its peers, but rather management have been just doing their job.

We note that the company has been acquiring further warehouse space to cater for increased demand, including a $31.4m deal to acquire Fremantle Freight Services – which will generate $29m in annual revenue.

There is the risk that this company may not deliver the goods, which could be caused by a number of factors including a decline in global freight volumes and potential industrial action – freight is one of the more union-intensive industries and has high staff turnover. But in relation to the latter risk, the company has long tenure (average of over 5 years) and low turnover (less than 3%).

ESG investors may not like the company at first glance, but it has some things going for it, including a gradual transition to electric vehicles and a target of increasing female appointments to management and other key roles (without setting specific targets). For investors just concerned about whether or not it can grow, we think they won't be disappointed in the period ahead. Four stars.

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