We recently interacted with private warehousing-based 3PL players to understand the current 3PL industry dynamics, market opportunity in non-auto based services and how listed players such as Mahindra Logistics (MLL) are targeting these segments. For MLL, our biggest positive takeaway was that its recent aggressive strategy in consumer sector warehousing might hit the bullseye given that the next leg of 3PL market creation is likely to be consumer sector driven. In our logistics coverage, MLL remains one of the top picks; retain ‘BUY’ with TP of INR520.

- **GST positives gradual; front-end consolidation bigger accelerator:** Post GST, consolidation in warehousing market was expected to be rapid. However, in reality, this continues to be gradual and is expected to remain so. Our interactions indicate that for 3PLs, front-end consolidation (of distributors/dealers) will be a much bigger driver. This consolidation typically compels back-end consolidation, creating market opportunities for organised logistics players such as MLL. A lean front-end allows entire truckloads pick-ups from factories, reducing need for smaller warehouses.

- **FMCG, retail and pharma next in line for front-end consolidation; auto already consolidated:** The auto industry’s front-end consolidated way before many other sectors and this fueled genesis of transportation-based 3PLs in India. Though in early stages, the move has started in FMCG, retail and pharma as well. For FMCG and retail especially, the high fragmentation is an opportunity, but a challenge as well, with a need of a warehouse every 300-350 kms in India currently.

- **MLL—Getting much more aggressive in FMCG and retail:** Our interactions indicate that MLL has been getting aggressive in FMCG and retail segments in the past one year. This is reflected in the company’s strong warehousing growth since FY18 and strategy-wise makes sense given that auto-related 3PL sales have been languishing. This also implies that MLL’s bottom-line growth will be much higher in ensuing years than top-line growth as warehousing margins are 10-20% (~4% for transportation).

- **Cost economics for warehousing 3PLs—20-25% ROCE, irrespective of margin:** In our earlier research, we had argued that 3PL players make 20-25% ROCE, irrespective of margin. This was validated during our discussions with private 3PL players. Margin range can be 10-20% depending on the quantum of value-added services involved, but complex services need higher capex as well. For instance, heavy-duty racking costs ~INR300/sq ft and dense racking ~INR500/sq ft.

- **Yields for Warehousing asset owners may remain range-bound:** For asset owners, ex-land cost of developing a warehouse is about INR1400-1500/sq. ft. for Grade A warehouse and rental yield for asset owners is ~8-9% - this likely will hold up.

**Top picks:** Within our coverage, we prefer relatively structural pockets such as road express and 3PL. Hence, our top picks are MLL and TCI Express (both ‘BUY’).
Logistics

Chart 1: MLL's warehousing consistently clocking 25-30% growth in the past quarters

Source: Company, Edelweiss research
Coverage group(s) of stocks by primary analyst(s): Logistics

Blue Dart Express, Container Corporation, Mahindra Logistics, TCI Express, Transport Corporation of India, VRL Logistics

Recent Research

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<th>Title</th>
<th>Price (INR)</th>
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<td>VRL Logistics</td>
<td>Growth eludes; Result Update</td>
<td>263</td>
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<tr>
<td>06-Nov-19</td>
<td>Transport Corporation of India</td>
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Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

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*1 stocks under review

Market Cap (INR)

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Rating Interpretation

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<td>Hold</td>
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<td>Reduce</td>
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One year price chart

- **Mahindra Logistics**
- **TCI Express**
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