

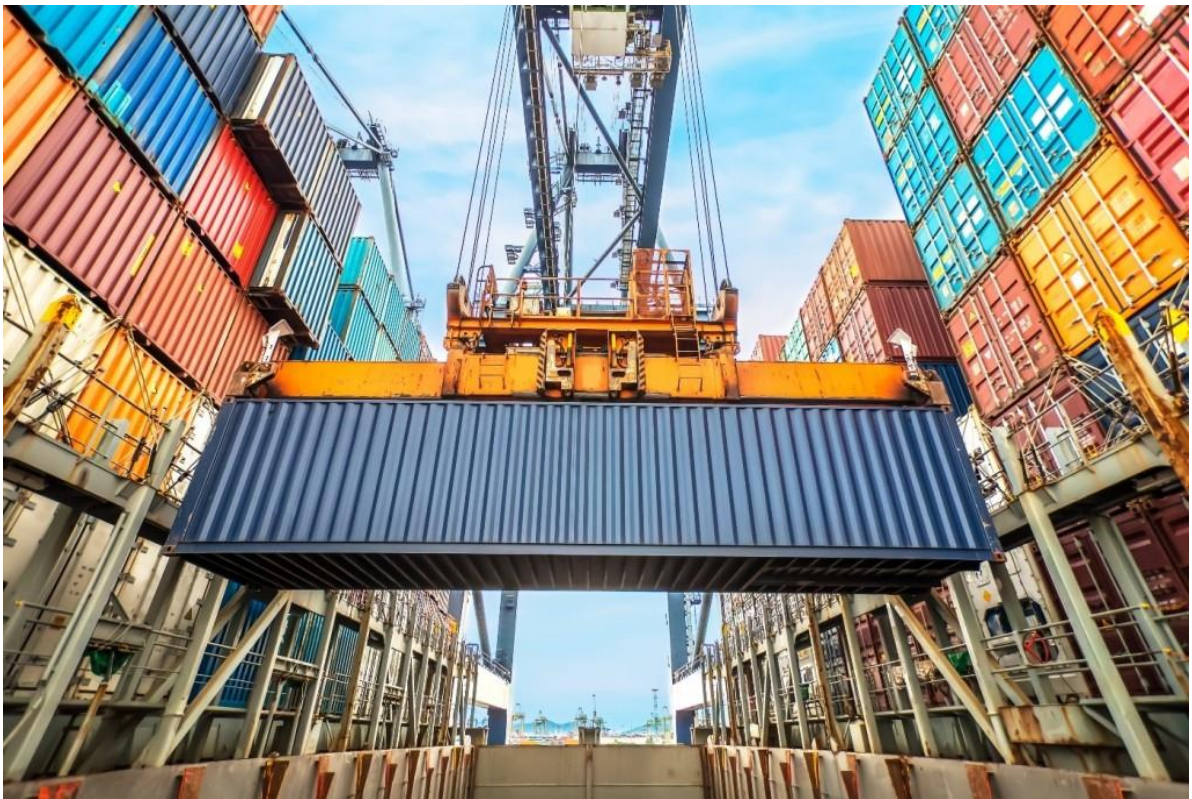


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The ASEAN logistics industry

A growing connectivity hub



The ASEAN logistics industry: A growing connectivity hub

The ASEAN nations collectively – if considered a nation – would be the seventh largest economy in the world. Their combined Gross Domestic Product (GDP) is about USD2.4 trillion (as of 2015)¹. ASEAN has a consumer base of more than 600 million, an expanding labor force and a rising E-commerce industry. There is a growing need to streamline industrial inventories and develop an efficient logistics industry to aid increasingly complex supply chains². Will ASEAN's logistics industry rise to the challenge?

The growing wealth of ASEAN economies³

With rising costs in China, creeping political turbulence around the world and slower global growth, ASEAN is being seen as a haven of tranquillity by investors. ASEAN's business sphere is not mature, dominated as it is by small and medium-sized enterprises. But the abundance of natural resources and cost-effective skilled labor has lured many companies to carry out manufacturing processes in this region.

For instance, Thailand and Indonesia are now playing host to labour-intensive manufacturing processes, especially for the automotive and electronics sector, due to lower labor costs compared to China's. Favorable trade policies and agreements have led to greater regional integration, aiding the economy's growth.

Why does the ASEAN logistics industry matter?

The ASEAN region is attracting a great deal of attention in the global logistics community. Some of the reasons for this include:

Strong economic growth

Home to more than 600 million people, the region has the third largest labor force in the world behind India and China. The population is

¹ ASEAN Logistics – Full steam ahead, LinkedIn Pulse, Scott Tan, 2 November 2015

² ASEAN Logistics: Refining transportation networks, Peerless Media LLC, Patrick Burnson, 1 February 2016

³ Southeast Asia's Rising Logistics Market, ASEAN Logistics, Jones Lang LaSalle Company, 2013

larger than that of North America and the European Union⁴. Moreover, the GDP growth forecast for the next decade (from 2013) is at 5 per cent per annum⁵ – an enviably stable and decent level of economic growth in this day and age.

Demographic profile⁶

ASEAN's young demographic continues to attract MNCs to invest heavily in the region. ASEAN's working population constitutes (as at 2013) 67.6 per cent of the total population, where an additional 55 million people are forecasted over the next decade (2012-2023).

A surging middle-class⁷

ASEAN's middle income bracket is expected to grow at an average of 10.9 per cent per annum from 2012 to 2023. About 84.4 per cent of households fall in the income bracket of USD 10-15,000 per annum. A higher proportion of this group is expected to shift into the income bracket of USD15-50,000 per annum by 2023.

Trade⁸

ASEAN trade volume is expected to increase by 130 per cent and be valued at USD5,653 billion by 2023. The expansion in trade volumes will mainly be driven by a rise in demand for goods and services in China as well as India – the world's big and growing consumer bases which are driving trade in the region.

Moreover, the recent crystallization of the ASEAN Economic Community (AEC) in 2015 and other free trade agreements have resulted in what many now see as a single market and production base that allows a greater volume of goods to be made and to pass

⁴ Global Trade – Association of Southeast Asian Nations, MTS Logistics, Sheng Mou, 28 March 2016

⁵ Ibid

⁶ Ibid

⁷ Ibid

⁸ Ibid

through. It has also led to an increasingly transparent legal and regulatory framework for intra-ASEAN trade.

Maritime network

Given the geographic location of the ASEAN nations, quality shipping lanes are crucial to achieve an effective supply chain network. A changing global shipping landscape demands larger ports with improved cargo handling capacity⁹.

Under the ASEAN Connectivity Masterplan, 19 ports in Indonesia will be constructed accommodating ships with capacity of 5,000 twenty foot equivalent units (TEU).

Among the ASEAN-6 (Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand), port quality is excellent in Singapore for handling the largest volume of goods¹⁰. But ports in Malaysia and Thailand are not far behind while ports in Indonesia and Vietnam are catching up. Under the ASEAN Connectivity Masterplan, 19 ports in Indonesia will be constructed accommodating ships with capacity of 5,000 twenty foot equivalent units (TEU)¹¹.

Road transport and railways

Some ASEAN nations are archipelagos, making sea transport of paramount importance. But rail and road are still relevant. Current scheduled investments in ASEAN's rail network amount to USD200 billion (as of 2013), set to benefit peninsular economies the most¹².

⁹ Ibid

¹⁰ Ibid

¹¹ Analysis: Opportunities and challenges in the maritime sector, PT Niskala Media Tenggara, Mamay Sukaesih, 18 March 2015

¹² Ibid

It is further estimated that an annual investment of USD60 billion (as of 2016) would be required for water, power, rail, road and other infrastructure in ASEAN to meet projected future demand¹³.

Transport by air

ASEAN's combined investment plan is to invest USD34 billion (as of 2013)¹⁴ in air transport. Moreover, its Open-Skies Policy removes tariffs and has allowed airline carriers to freely operate across the ASEAN market. This has led to the growth of private sector low cost air carriers, with an estimated 101,000 technicians and 95,000 pilots by 2034¹⁵.

What factors are responsible for the ASEAN logistics industry boom?¹⁶

ASEAN is witnessing a growing middle class with increased spending power. This will drive the demand for logistics as consumers demand more, better and more varied products and services, often to be delivered to their doorstep. The factors that will enhance the growth potential of logistics players are:

Low cost outsourcing

China's strategic shift towards domestic consumption has led to a diversion of manufacturing processes to ASEAN – a low-cost labor supplier.

Inefficiencies in ASEAN supply chains

Deficiencies in skilled human capital, lack of technical know-how and R&D has led to inefficiencies in ASEAN's supply chain and logistics infrastructure. The solutions to such inefficiencies are provided by foreign logistics service providers, which have created a market opportunity.

¹³ Asean insurance sector's pivotal role in infrastructure financing, Southeastern Globe Communications Co. Ltd., Evelina F. Pietruschka, 1 November 2016

¹⁴ Ibid

¹⁵ ASEAN open skies create huge market for aviation industry, PT Niskala Media Tenggara, Anton Hermansyah, 25 April 2016

¹⁶ Ibid

Demand for sophisticated Third Party logistics (3PLs)

Third-party logistics providers (3PLs) provide innovative solutions to logistics problems. The establishment of multi-brand and single-brand retailers in the region has led to the demand for professional logistics service providers to ensure speedy and safe delivery processes. Some of the more active and promising players in the region are Panalpina, Toll, Sinotrans, UPS International, Fedex and Yamato Transport.

What investment opportunities beckon?

This rising need for the growth and integration of logistics service providers¹⁷ presents a huge market opportunity to logistics companies that can succeed in ASEAN's complex and ever-changing environment.

However alongside the opportunities are pitfalls. Not least among these, new players are quickly commoditizing last-mile delivery using the kind of low-cost delivery techniques practiced by China and India players like Taobao.

Having said that, some emerging opportunities include:

Mergers and Acquisition (M&A)¹⁸

There is a growing recognition that the key to unlocking ASEAN's logistics jigsaw is M&A that integrates international best practices with local logistics assets and expertise.

For instance, the acquisition of APL Logistics (Singapore) by Japan's Kintetsu World Express in 2015 (at USD1.2 billion); the merging of Franklin Templeton PE with Indo-Trans Logistics, one of the top 3 logistics companies in Vietnam; and the acquisition of Singapore's Tidiki Logistics by Japan's Yamato Transport; these are a few of the logistics M&A deals that have taken place recently.

3PLs¹⁹

¹⁷ Ibid

¹⁸ Ibid

¹⁹ Ibid

With more global players focusing on the ASEAN region as their manufacturing hub, the demand for 3PL players that can knit together transportation, clearance and customs is bound to rise.

Cross-border trucking²⁰

With the advent of the AEC, domestic truck companies can cross international borders with little hindrance, seamlessly connecting Singapore, Malaysia, Thailand, Laos and Vietnam.

Origin Cargo Management (OCM)²¹

OCM businesses manage and source international supply chains in addition to functions like preventing overstocking in warehouses, arranging domestic transportation, improving stock availability and managing storage and warehouses, to name a few. Many global textile players like Nike, Adidas and H&M are opening up factories in ASEAN, to further streamline shipping expenses to ASEAN customers. With OCM, logistics companies have the opportunity to seize the entire back-end supply chain and extract value.

Project cargo logistics²²

With more investment pouring into infrastructure and the formation of the Asian Infrastructure Investment Bank, new projects are easier to finance. This also paves the way for the rise of Project Cargo logistics to support infrastructure development.

Companies that are involved in the handling of Project Cargo – large, heavy, high value, critical pieces of equipment that need assembly and disassembly before and after shipment – can gain from this infrastructure boom in ASEAN.

²⁰ Ibid

²¹ Ibid

²² Ibid

Cold chain logistics

The cold chain sector in ASEAN is presently dominated by unorganized players²³. One of the rising trends in the ASEAN region is consumption of processed food and increased concern about hygiene standards. There are thus enormous opportunities for new players to enter the market in areas like refrigerated vehicle manufacturing, temperature control equipment supply and cold chain consulting²⁴.

The cold chain sector in ASEAN is presently dominated by unorganized players.

Emerging ASEAN logistics markets in Asia

Even though Singapore remains the top ASEAN Logistics hub for the tenth consecutive year (as of 2016)²⁵, Thailand's Logistics industry is on the upswing and is giving Singapore a run for its money²⁶.

A few emerging markets to watch for are:

Indonesia

Indonesia's logistic sector is expected to grow by 15.4 per cent in 2020 due to the growing economy. Strong growth factors include the rise in export of manufactured products, high domestic consumption, and improvement in infrastructure investment along with regional trade integration²⁷.

The Indonesian government plans to invest in the construction of 24 new seaports, 15 new airports, 3,600 kilometers of new roads, the expansion of the railway network by 3,258 km and improve public transportation in 29 cities²⁸.

²³ Your gateway to ASEAN Cold Logistics Market, Manch Communications, July 2015

²⁴ Cold Chain: seas of opportunities for emerging markets, Asia Cold Chain Show, 13 March 2015

²⁵ Singapore remains top ASEAN Logistics Hub for 10th consecutive year: 2016 LPI Report, Black Stump Publishing, John Le Fevre, 29 June 2016

²⁶ Thailand tipped to emerge as key ASEAN Logistics Hub, Thailand Board of Investment, September 2016

²⁷ Indonesia Transportation and Logistics Industry continued economic growth momentum supports transport infrastructure investment and development, Frost & Sullivan, 2 March 2016

²⁸ Indonesia's Logistics sector; making connections, Global Business Guide Indonesia, 2016

Malaysia

With a fourth place ranking in the 2016 Agility Emerging Markets Logistics Index²⁹, Malaysia is considered to be an attractive location for new logistics entrants. The logistics sector is expected to contribute 4.3 per cent to the country's GDP in 2020 from the current 3.6 per cent³⁰.

Amongst its Southeast Asian counterparts, Malaysia boasts a vastly developed transport infrastructure which consist of five major ports, neatly constructed highways, five port container terminals (rails), five international airports and four inland ports (as of 2015)³¹.

Thailand

Considered ASEAN's emerging logistics hub, the nation's logistics revenues are forecasted to reach USD96.5 billion by 2019³². With the establishment of the AEC and Thailand's strategic position in ASEAN at the nexus of ASEAN, China and India, Thailand is emerging as a logistics hub for MNC's globally³³.

The government is further encouraging growth for logistics operations by integrating e-logistics across the borders of the Greater Mekong Sub-region and establishing a one stop Export Service Center to reduce time to obtain export consultations and documentation. This center comprises 17 private and public export-related organizations³⁴.

Vietnam³⁵

The logistics sector accounts for 20-25 per cent of Vietnam's GDP, with a projected growth of 12 per cent through the year (as of 2016). It is expected to add USD632 billion worth of trade by 2020. Rising foreign

²⁹ Malaysia leaps to world's No.4 emerging market, Agility, 18 January 2016

³⁰ Beefing up Malaysia's logistics sector, New Straits Times Press, Jalil Hamid, 11 September 2016

³¹ Logistics sector in Malaysia, Ministry of Transport, Noor Aishah Kamarzaman, 15 June 2015

³² Thailand poised to emerge as ASEAN logistics center, Air Cargo World, 7 January, 2016

³³ Ibid

³⁴ Ibid

³⁵ Vietnam loading up on logistics, Oxford Business Group, 31 March 2016

investment, rising agricultural output and growing manufacturing are driving trade growth.

Although existing port infrastructure needs to be better leveraged to achieve consistent growth, the passing of goods through Vietnam's ports is set to increase by 10 per cent (as of 2016) to 470 tons.

The Philippines

The Philippines logistics sector is expected to grow (annually) by 15.6 per cent by 2020 – to reach a market size valued at USD6.77 billion³⁶. Growth has been driven by e-commerce services, 3PLs and express deliveries. The domestic express delivery sector is growing briskly as more customers now value timely deliveries³⁷.

Challenges ahead

The ASEAN logistics industry is not yet fully developed. What challenges and potential pitfalls should investors consider?

Lack of structural reforms in the CLM countries

The Philippines, Indonesia and Vietnam are rapidly upgrading their road, rail, maritime and air cargo infrastructure in line with AEC frameworks. However, the much smaller economies of ASEAN – Cambodia, Laos, and Myanmar – are still substantially lagging behind³⁸.

Political and environmental disruptions³⁹

The region is prone to frequent disruptions such as natural disasters (typhoons, tsunamis to name a few), power outages and poor infrastructure – not to mention the occasional media panic caused by

³⁶ Philippines: Consumer growth ignites opportunities in logistics, PricewaterhouseCoopers LLP, Raoul A. Villegas, 13 August 2015

³⁷ Philippines Logistics market outlook 2015-2019 – Growth driven by Express delivery, 3PL and E-commerce Logistics Services, PR Newswire Association LLC., 6 January 2016

³⁸ Ibid

³⁹ Ibid

a terrorist attack. Furthermore, complexity around bureaucracy, corruption and rampant red tape often results in high import taxes and heavy documentation requirements – strong deterrents’ to foreign investors.

Uneven port and airport infrastructure

As the largest economy in the AEC, Indonesia spends the highest share of its GDP on logistics – 26 per cent. Limited facilities at sea ports worsen congestion. Land transport of products takes more time than processing in the ports. Moreover, poor infrastructure and closure of roads, especially in rural areas, increase transport time⁴⁰.

As the largest economy in the AEC, Indonesia spends the highest share of its GDP on logistics – 26 per cent.

Maritime transport is also a bottleneck for ASEAN. With nine countries having only 47 ports in 2015, most ports are congested. Apart from Malaysia, Thailand and Singapore, cargo-handling capabilities are uneven and sometimes unstable⁴¹.

Moreover, while many ASEAN nations have improved air ports to handle passenger and non-perishable air freight adequately, some airports do not meet international standards for basic perishable freight handling⁴².

Low-tech supply chains⁴³

In the rural areas of Indonesia and Malaysia, telecom infrastructure is underdeveloped, making cargo tracking difficult. Less organized regional players are unable to adopt advances like Transportation Management Systems and Global Positioning Systems due to high initial

⁴⁰ Boosting supply chain performance in ASEAN, Supply Chain Asia, Max Ward, 7 October 2016

⁴¹ Ibid

⁴² ASEAN Logistics: Exploring the new frontier, EH Publishing, Inc., Patrick Burnson, 1 March 2015

⁴³ Ibid

cost of implementation. Inefficient custom practices and inspections are another bottleneck. Most ASEAN nations are developing economies and hence the government discourages foreign participation.

The future outlook for ASEAN Logistics⁴⁴

The gradual liberalization of ASEAN logistics services will increase competitiveness and foreign participation, thereby introducing more logistics players into the market. But initially there may be more pitfalls than opportunities, as competition forces prices to be cut and over-supply looms. However, the industry should soon stabilize as mergers and acquisitions between global and local players take root.

To support an orderly development of the logistics industry, governments will need to build adequate port, airport, road, rail and IT infrastructure for sophisticated supply chain processes. To overcome infrastructural bottlenecks, individual ASEAN government, as well as ASEAN as a whole, must ensure timely completion of transport related projects and other agreements related to transport facilitation, such as the ASEAN Single Window Policy, which integrates the National Single Windows of the member states to ensure faster cargo clearance and improved transparency.

Much of the most exciting growth opportunities in logistics will come in the countries with less well developed logistics industries. Thailand, Singapore, Malaysia, and the Philippines are already using 'e-customs' tools. Indonesia, Vietnam and other ASEAN countries need to follow to ensure ASEAN's success as an integrated supply base.

⁴⁴ Logistics-Moving at a better pace, Invest in ASEAN, the official investment promotion website of ASEAN