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S&P Global China Ratings

Express Delivery Industry: Financial Risk is Increasing

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In our view, overall financial risk in the express delivery industry is significantly higher in 2021 as a fierce price war eats away at profitability. As this race to the bottom continues with no end in sight, players would struggle to resolve the dilemma through raising prices.

We highlight two types of risk in this situation: firstly, where gross profit per delivery comes close to or even drops below zero, leading to a significant decline in cash flow to debt coverage; secondly, where demand for capital expenditure reaches a large enough level that debt pressure may increase significantly.

Many express delivery companies, such as ZTO and Yuantong, have recently announced that delivery fees will increase by 0.1 RMB from September 1, 2021. Players have stated that the price increases are mainly aimed at improving salaries and conditions for delivery drivers and workers, and additional revenue will be used to subsidize delivery franchises.

We expect these measures are being implemented to meet regulatory requirements, and don’t anticipate major improvements to profitability. In July 2021, seven government departments jointly issued guidance on protecting delivery drivers and workers’ legitimate rights and interests, underlining that this is the responsibility of their employers.

With such high-level intervention, efforts to safeguard the rights of delivery staff will continue to advance. We expect this may raise barriers to entry in the express delivery industry, effectively regulating how players treat their employees and somewhat dampening down the industry’s ongoing price competition.

Although regulations are targeting the price war, we see overall financial risk as still being on the rise, and risks may emerge among some players in the next two years. The increase in financial risk can be put down to pressure from two sides.

On the one hand, the price war has put pressure on overall profitability in the industry. This is reflected in the gradual decline in delivery fees in the past few years, with gross margins per delivery dwindling rapidly, or even falling below zero. For some companies, the coverage of cash flow and profits to debt has weakened significantly.

On the other hand, in response to the fierce competition top players may continue to increase capital expenditure to maintain their market shares, further expanding their debt. We continue to view the express delivery sector as an industry where economies of scale are important. With strong scale advantages, courier firms can effectively reduce their delivery fees and accept low revenue per delivery as their market shares increase. Therefore, as delivery volume in the industry continues to grow steadily, we expect some express delivery companies to increase capital expenditure. While such investment would aim to expand market share, further dilute costs and consolidate their market positions, it may also lead to an increase in overall financial risk.

This report does not constitute a rating action.