TRIS RATING
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# PRECIOUS SHIPPING PLC

No. 161/2019
8 October 2019

## CORPORATES

| | |
|---|---|
| **Company Rating:** | BBB- |
| **Issue Rating:** | |
| Senior unsecured | BB+ |
| **Outlook:** | Stable |

**Last Review Date:** 11/09/18

**Company Rating History:**

| Date | Rating | Outlook/Alert |
|---|---|---|
| 31/08/17 | BBB- | Stable |
| 26/08/16 | BBB- | Negative |
| 13/11/15 | BBB | Stable |


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## RATIONALE

TRIS Rating affirms the company rating on Precious Shipping PLC (PSL) at "BBB-" and affirms the rating on PSL's senior unsecured debentures at "BB+". The rating outlook is maintained "stable". The ratings reflect the company's high business risk profile, inherent in the highly volatile shipping industry and its high level of leverage. The ratings also take into consideration the favorable development in demand-supply fundamentals; however, the prolonged trade tensions remain a key risk hindering charter rate recovery.

## KEY RATING CONSIDERATIONS

### Modest supply growth supports the industry fundamental

PSL's high business risk profile is characterized by the highly volatile dry-bulk shipping industry. One major factor driving the volatility is a series of oversupply situations due to a lack of supply discipline, as the industry is highly fragmented and competitive. However, supply correction has been ongoing over the past two years, leading to more favorable market conditions for dry-bulk shipping operators.

Dry-bulk shipping capacity growth is expected to remain modest in the next 12-18 months. A key factor supporting the industry supply fundamental is the implementation of a sulphur emission cap (IMO 2020), becoming effective on 1 January 2020. To comply with the regulation, ship owners have a choice to retrofit scrubbers or use low sulphur oil. Both options result in lower capacity as retrofitting a scrubber requires several weeks of dry docking while burning expensive low sulphur oil will slow down ship speed. In addition, IMO 2020 will accelerate the scrapping rates of aged and uneconomical vessels as well as slow down new orderbooks as a result of design uncertainty relating to the regulation. According to PSL, net increase of dry-bulk shipping capacity is expected to be at 2%-3% per annum during 2019-2020, the lowest growth level in several years.

### Trade disputes pressure demand growth

The dry-bulk shipping industry relies largely on world economic conditions. The activity level in the industry is a function of demand for commodities, world economic growth, and trade flows. Historically, the industry trade volume tends to grow at a pace slightly faster than world gross domestic product (GDP). The escalated trade disputes, especially between the United States (US) and China, negatively impact the overall sentiment and hamper global GDP and trade flows, eventually slowing demand growth for dry-bulk shipping. The International Monetary Fund (IMF) forecasts world GDP to slow to 3.2% in 2019 and 3.5% in 2020, down from 3.6% in 2018. The prolonged and uncertain trade tensions remain a key risk factor further weighing down global economic dynamism.

### Operating cash flows tied to freight rate fluctuations

PSL's operating cash flows are volatile, reflecting the nature of the industry and freight rate fluctuations. For the first half of 2019, the Baltic Dry Index

(BDI) averaged 896 points, down from an average of 1,353 points in 2018. PSL's average time charter (TC) rate was US$9,113 per ship per day in the first six months of 2019, compared with US$10,866 per ship per day in the same period last year. The depressed dry-bulk freight rate in the first half of 2019 was due mainly to the Vale S.A. incident in Brazil and bad weather conditions in Australia which negatively impact iron ore production and exports. In addition, outbreak of African swine fever in China impacted soybean demand. Freight rates are expected to improve in the second half of 2019 as the one-time negative impacts ease and the BDI has strongly rebounded since July 2019.

TRIS Rating's base case scenario assumes PSL's average TC rate at US$9,700-US$10,200 per ship per day in 2019, taking into account the depressed TC rate in the first half of 2019. Based on supply rebalancing, we assume an average TC rate between US$10,600-US$12,000 per ship per day during 2020-2021. Our base case scenario also expects PSL to continue keeping its operating costs under control. We project PSL's operating profit margin (operating income before depreciation and amortization as a percentage of revenue) at 36%-42% during 2019-2021. Earnings before interest, taxes, depreciation, and amortization (EBITDA) is expected to range between US$50-US$62 million per annum and funds from operations (FFO) are expected to range between US$28-US$50 million per annum during 2019-2021.

### Improving leverage

PSL' leverage is high as most of its vessels are debt funded. At the end of June 2019, PSL's adjusted debt was US$370 million. For the first six months of 2019, the adjusted ratio of debt to EBITDA was 6.6 times and the adjusted FFO to total debt ratio was 8.4% (annualized, from the trailing 12 months).

Leverage is expected to remain high in 2019 due to weak operating cash flows in the first half of 2019. We expect the adjusted ratio of debt to EBITDA to stay around 7-7.5 times and the adjusted FFO to total debt ratio to stay below 8% in 2019. Afterward, we project the leverage ratios to improve. The adjusted ratio of debt to EBITDA is expected to stay around 4-5 times and the adjusted FFO to total debt ratio to stay at 15%-20% during 2020-2021. Our base-case scenario assumes that PSL's operating performance will improve along with the market uptrend. We also assume no major capital expenditures, such as the acquisition of new vessels during 2019-2021.

Our base-case scenario also assumes that, in 2020, PSL will receive a refund of US$56 million out of US$64 million in advance installments for newbuildings paid to a shipyard after arbitration with the shipyard is settled. However, if the arbitration results turn unfavorable to the company, it may lose advances for vessel construction of up to US$64 million plus an additional payment of about US$20 in related costs regarding the claims. PSL may have to pay additional unquantified damages, losses, interest and/or costs in accordance with the claims. TRIS Rating is of the view that the arbitration results will have a material impact on PSL's leverage profile. If PSL loses the case, its leverage will stay elevated, weakening its financial profile and adding a downside risk to its credit ratings.

### Manageable liquidity

We expect PSL to maintain sufficient liquidity to meet its obligations over the next 12-18 months. The funding uses are primarily capital spending of US$6-US$8 million and scheduled debt repayments of US$145 million. Sources of funds are FFO, forecast at US$50-US$60 million per annum, and cash and cash equivalents of US$47 million at the end of June 2019. PSL also plans to refinance its debts due with bank loans and debentures of US$80-US$100 million combined. Our base-case scenario includes US$56 million from a refund of advanced payments for vessels, expected to be received in 2020. We expect the company to actively manage and maintain ample liquidity to allow sufficient headroom for financial flexibility and to cushion against market volatility.

## BASE-CASE ASSUMPTIONS

- Average TC rate at US$9,700-US$10,200 per ship per day in 2019 and US$10,600-US$12,000 per ship per day during 2020-2021.
- Operating margin to stay at 36%-42% during 2019-2021.
- Capital spending is forecast at around US$8-US$10 million in total during 2019-2021.
- PSL will receive US$56 million of a refund from advanced payment for vessels in 2020.

## RATING OUTLOOK

The "stable" outlook reflects the improvement in the dry-bulk shipping market conditions and the expectation of TRIS Rating that PSL's operating performance will improve in line with the market uptrend. We also expect PSL to maintain prudent liquidity management.

## RATING SENSITIVITIES

PSL's ratings could be downgraded if the dry-bulk shipping market slumps or if PSL's financial profile is weaker than our base case expectation, either from deteriorating operating performance or higher financial leverage such that its adjusted ratio of FFO to debt stays below 10% on a sustained basis. The rating upside case could be driven by favorable market conditions, coupled with PSL's stronger-than-expected operating results over a sustained period of time, leading to its adjusted ratio of FFO to debt staying over 20% on a sustained basis.

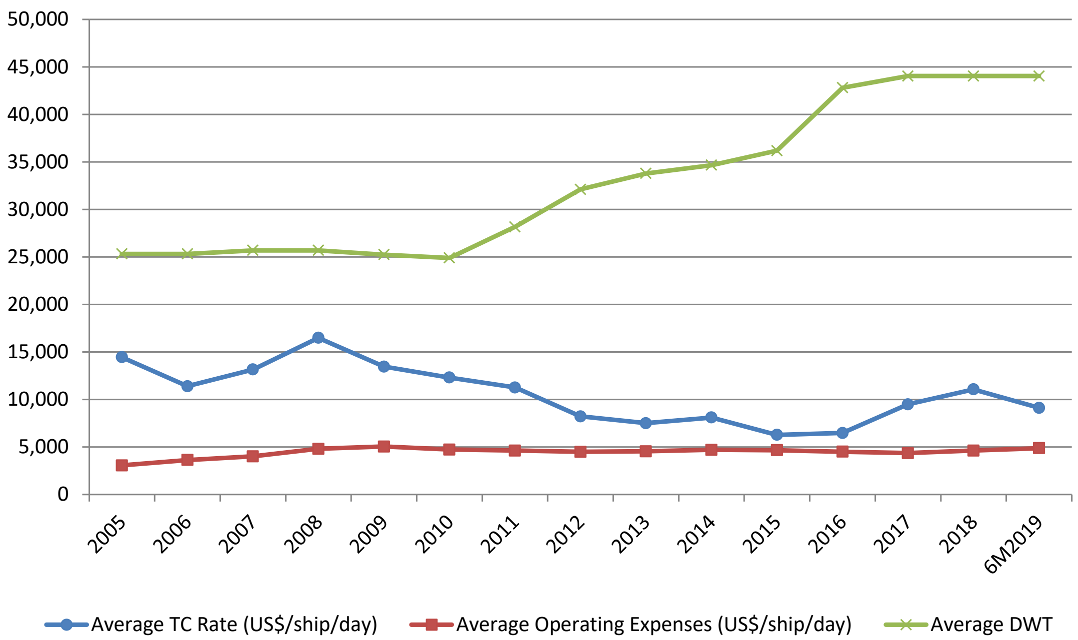
## COMPANY OVERVIEW

PSL was established in 1989 and listed on the Stock Exchange of Thailand (SET) in 1993. PSL is a shipping company, owning and operating dry-bulk ships as a tramp shipper. As of February 2019, PSL's major shareholders comprised Ms. Nishita Shah and group, holding 44.4% of PSL's shares, followed by Mr. Khalid Moinuddin Hashim, holding 8.4%.

As of August 2019, PSL had 36 vessels with a total of 1.59 million deadweight tonnage (DWT) in its fleet, comprising 15 handy size vessels, four cement carriers, nine supramax vessels, and eight ultramax vessels. The average age of the fleet is 7.28 years.

## KEY OPERATING PERFORMANCE

**Chart 1: Average TC Rate and Operating Expenses during 2005 to Jan-Jun 2019**




*Source: PSL*

## FINANCIAL STATISTICS AND KEY FINANCIAL RATIOS

*Unit: US$ million*

| | Jan-Jun 2019 | -------Year Ended 31 December 2018 | 2017 | 2016 | 2015 -------- |
|---|---|---|---|---|---|
| Total operating revenues | 62 | 152 | 128 | 105 | 123 |
| Operating income | 19 | 68 | 53 | 18 | 14 |
| Earnings before interest and taxes (EBIT) | 5 | 40 | 19 | (9) | (24) |
| Earnings before interest, taxes, depreciation, and amortization (EBITDA) | 20 | 70 | 49 | 23 | 11 |
| Funds from operations (FFO) | 8 | 44 | 24 | (4) | (5) |
| Adjusted interest expense | 12 | 26 | 25 | 28 | 16 |
| Capital expenditures | 2 | 3 | 21 | 73 | 118 |
| Total assets | 847 | 858 | 882 | 902 | 899 |
| Adjusted debt | 370 | 377 | 413 | 398 | 375 |
| Adjusted equity | 384 | 391 | 377 | 381 | 457 |
| **Adjusted Ratios** | | | | | |
| Operating income as % of total operating revenues (%) | 30.67 | 44.82 | 41.64 | 16.70 | 11.19 |
| Pretax return on permanent capital (%) | 3.32 | 4.78 | 2.16 | (1.07) | (2.88) |
| EBITDA interest coverage (times) | 1.69 | 2.74 | 1.96 | 0.84 | 0.67 |
| Debt to EBITDA (times) | 6.63 | 5.38 | 8.41 | 17.09 | 34.01 |
| FFO to debt (%) | 8.39 | 11.79 | 5.81 | (1.13) | (1.44) |
| Debt to capitalization (%) | 49.07 | 49.09 | 52.26 | 51.06 | 45.10 |

## RELATED CRITERIA

- Rating Methodology – Corporate, 26 July 2019
- Key Financial Ratios and Adjustments, 5 September 2018

## Precious Shipping PLC (PSL)

| | |
|---|---|
| **Company Rating:** | BBB- |
| **Issue Rating:** | |
| PSL211A: Bt3,590 million senior unsecured debentures due 2021 | BB+ |
| **Rating Outlook:** | Stable |

**TRIS Rating Co., Ltd.**
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