12 Jul 2018 15:00:00 ET │ 30 pages

Shipping
Asia │ Thailand

Precious Shipping (PSL.BK)

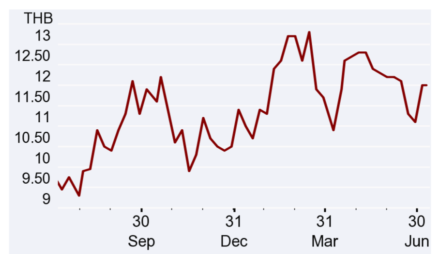
Initiate at Buy: A Pure Dry-Bulk Play into Freight Rates Up-cycle

■ Initiation of Coverage

- **A proxy for dry-bulk freight rates up-cycle –** We initiate coverage on Precious Shipping (PSL), a dry-bulk ship owner, with a Buy rating and a target price of Bt14.2 based on 1.8x 2020E PBV and 14% est. core ROE, discounted back to YE2019E at 10.5% Ke. We see PSL as a direct proxy to our bullish view on dry-bulk freight rates into 2020E, driven by potential supply tightness post expected implementation of *International Maritime Organization* (IMO)'s sulfur cap on marine fuel. In the near-term, we expect seasonally rising freight rates into 4QE peak to be the key share price driver.
- **Key beneficiary of IMO 2020's sulfur cap –** PSL's young fleet (avg age 6 years) of 36 Handysize and Supramax is capable of burning low-sulfur-fuel-oil per IMO's 2020 sulfur cap. Moreover, 83% of PSL's capacity is on the spot market during 2018E–2020E. This is important as we believe most shipping sub-sectors including dry-bulk would see a strong rate uplift following the sulfur cap implementation in Jan'2020 driven by higher scrapping rates, as ship owners will likely find installation of scrubbers uneconomical, while charterees will likely slow-steam to save fuel expenses. See IMO 2020 update report dated 25 June 2018 for details.
- **Rising tides pushing core ROE to 14% in 2020E from -0.4% in 2017 –** We forecast PSL's avg. daily revenue per ship to reach US$14,668 in 2020E, a 15% CAGR from 2017, compared to est. total daily costs of US$10,095. These translate to core ROE of 14% in 2020E from -0.4% in 2017. Our expectations for freight rate increases are in-line with our *Baltic Dry Index* (BDI) forecasts of 1,300, 1,625 and 2,113 over 2018E–20E from 1,145 in 2017 (23% CAGR). We expect higher rates to be driven by 0.3–1.9% demand/supply positive spreads over the period.
- **Downside risks to our bullish view –** The key risk is dry-bulk industry supply tightening not coming through ie. limited enforcement from port / flag states or non-compliance by bulkers. Our sensitivity indicates that 2020E industry's demand / supply balance could flip to –ve 1.1% from +1.9% in our base case, leading to 2020E BDI to average c1,300. That implies roughly a breakeven core-ROE of PSL, leading to a coinciding valuation of 1.1x PBV ie. YE2019E fair-value of Bt8.4.

Buy	**1**
Price (12 Jul 18 17:00)	Bt12.10
Target price	Bt14.20
Expected share price return	17.4%
Expected dividend yield	1.2%
Expected total return	**18.5%**
Market Cap	Bt18,867M
	US$566M

Price Performance
(RIC: PSL.BK, BB: PSL TB)



Statistical Abstract

Year to 31 Dec	Net Profit (BtM)	Diluted EPS (Bt)	EPS growth (%)	P/E (x)	P/B (x)	ROE (%)	Yield (%)
2016A	-1,448	-0.93	3.9	-13.0	1.4	-9.6	0.0
2017A	-51	-0.03	96.5	na	1.5	-0.4	0.0
2018E	447	0.29	978.2	42.2	1.5	3.6	1.2
2019E	1,023	0.66	128.7	18.4	1.4	8.0	2.7
2020E	1,850	1.19	80.9	10.2	1.4	13.9	6.9

Source: Powered by dataCentral

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PSL.BK: Fiscal year end 31-Dec — **Price: Bt12.10; TP: Bt14.20; Market Cap: Bt18,867m; Recomm: Buy**

Profit & Loss (Btm)	**2016**	**2017**	**2018E**	**2019E**	**2020E**
Sales revenue	3,690	4,333	4,605	5,117	5,945
Cost of sales	-2,486	-1,990	-1,934	-1,966	-2,019
Gross profit	1,204	2,342	2,671	3,151	3,927
Gross Margin (%)	32.6	54.1	58.0	61.6	66.0
EBITDA (Adj)	**850**	**1,934**	**2,276**	**2,755**	**3,524**
EBITDA Margin (Adj) (%)	23.0	44.6	49.4	53.8	59.3
Depreciation	-1,366	-1,170	-1,139	-1,113	-1,109
Amortisation	0	0	0	0	0
EBIT (Adj)	**-516**	**764**	**1,137**	**1,641**	**2,415**
EBIT Margin (Adj) (%)	-14.0	17.6	24.7	32.1	40.6
Net interest	-933	-825	-692	-610	-543
Associates	3	10	11	14	18
Non-Op/Except/Other Adj	-1,217	-78	0	0	0
Pre-tax profit	**-2,663**	**-129**	**457**	**1,045**	**1,890**
Tax	0	0	-9	-21	-38
Extraord./Min.Int./Pref.div.	-2	0	0	-1	-2
Reported net profit	**-2,665**	**-129**	**447**	**1,023**	**1,850**
Net Margin (%)	-72.2	-3.0	9.7	20.0	31.1
Core NPAT	-1,448	-51	447	1,023	1,850
Per share data	**2016**	**2017**	**2018E**	**2019E**	**2020E**
Reported EPS (Bt)	-1.71	-0.08	0.29	0.66	1.19
Core EPS (Bt)	-0.93	-0.03	0.29	0.66	1.19
DPS (Bt)	0	0	0.14	0.33	0.83
CFPS (Bt)	0.44	1.29	1.35	1.75	2.22
FCFPS (Bt)	-1.94	0.47	1.24	1.65	2.12
BVPS (Bt)	8.76	7.91	8.05	8.38	8.74
Wtd avg ord shares (m)	1,559	1,559	1,559	1,559	1,559
Wtd avg diluted shares (m)	1,559	1,559	1,559	1,559	1,559
Growth rates	**2016**	**2017**	**2018E**	**2019E**	**2020E**
Sales revenue (%)	-13.3	17.4	6.3	11.1	16.2
EBIT (Adj) (%)	29.6	248.0	48.9	44.3	47.1
Core NPAT (%)	-12.4	96.5	978.2	128.7	80.9
Core EPS (%)	3.9	96.5	978.2	128.7	80.9
Balance Sheet (Btm)	**2016**	**2017**	**2018E**	**2019E**	**2020E**
Cash & cash equiv.	2,676	1,854	1,013	969	936
Accounts receivables	140	193	202	217	252
Inventory	0	0	0	0	0
Net fixed & other tangibles	29,108	26,489	25,374	24,419	23,469
Goodwill & intangibles	0	0	0	0	0
Financial & other assets	391	298	323	340	369
Total assets	**32,316**	**28,833**	**26,911**	**25,945**	**25,026**
Accounts payable	38	70	70	78	80
Short-term debt	887	802	690	615	540
Long-term debt	17,146	14,988	13,101	11,676	10,251
Provisions & other liab	586	637	491	505	527
Total liabilities	**18,657**	**16,498**	**14,352**	**12,873**	**11,397**
Shareholders' equity	13,659	12,335	12,559	13,071	13,626
Minority interests	0	0	0	2	3
Total equity	**13,659**	**12,335**	**12,560**	**13,072**	**13,629**
Net debt (Adj)	**15,357**	**13,937**	**12,778**	**11,322**	**9,855**
Net debt to equity (Adj) (%)	112.4	113.0	101.7	86.6	72.3

Valuation ratios	**2016**	**2017**	**2018E**	**2019E**	**2020E**
PE (x)	-13.0	na	42.2	18.4	10.2
PB (x)	1.4	1.5	1.5	1.4	1.4
EV/EBITDA (x)	39.9	17.3	14.2	11.2	8.4
FCF yield (%)	-16.0	3.9	10.3	13.7	17.5
Dividend yield (%)	na	na	1.2	2.7	6.9
Payout ratio (%)	0	0	50	50	70
ROE (%)	-17.7	-1.0	3.6	8.0	13.9
Cashflow (Btm)	**2016**	**2017**	**2018E**	**2019E**	**2020E**
EBITDA	850	1,934	2,276	2,755	3,524
Working capital	-98	112	-180	-12	-39
Other	-59	-35	2	-7	-19
Operating cashflow	**693**	**2,010**	**2,099**	**2,736**	**3,466**
Capex	-3,717	-1,281	-158	-158	-160
Net acq/disposals	682	77	0	0	0
Other	2,230	-433	134	0	0
Investing cashflow	**-806**	**-1,637**	**-24**	**-158**	**-160**
Dividends paid	0	0	-224	-511	-1,295
Financing cashflow	**2,356**	**-949**	**-2,916**	**-2,622**	**-3,339**
Net change in cash	**2,223**	**-823**	**-841**	**-44**	**-33**
Free cashflow to s/holders	**-3,024**	**730**	**1,941**	**2,578**	**3,306**

For definitions of the items in this table, please click here.

Contents

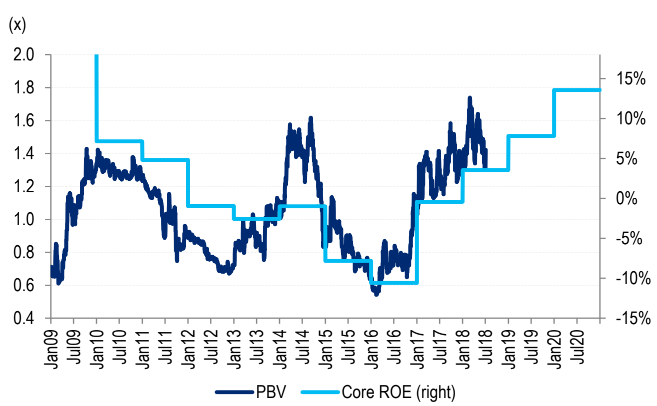
Initiate at Buy, TP of Bt14.2

We initiate coverage on Precious Shipping (PSL), a dry-bulk shipping pure play, with a Buy rating and a target price of Bt14.2 based on 1.8x 2020E PBV and 14% 2020E core ROE, discounted back to YE2019 at 10.5% Ke. Key points for our bullish investment theses are:

- PSL is **a pure play dry-bulk** ship owner in the rising freight rates environment. Its fleet consists of 19 Handysize and 17 Supramax with an average fleet age of only 6 years as of 1Q18 with no outstanding order book ie. capex obligation.
- **Earnings turnaround** expected. A significant portion ie. 83% of PSL capacity is on spot freight market during 2018E–2020E. We forecast PSL's average revenue per shipday to reach US$14,668 in 2020E (vs US$10,095 est. total daily costs) from US$9,747 achieved in 2017 or 15% CAGR. This translates to 2020E core earnings of Bt1.85bn (28% above consensus) from a breakeven level in 2017.
- We see **upsides to PSL valuation** to 1.8x PBV by 2020E compared to 1.5x currently. Our bullish sector view on BDI rising from 1,145 in 2017 to 1,300, 1625 and 2,113 over 2018E–2020E (23% CAGR) indirectly implies PSL's core ROE to reach 14% in 2020E. At this level of ROE, PSL should trade at 1.8x PBV (Figure 1). Note that slower rates growth at PSL compared to BDI is primarily a function of PSL's Handysize and Supramax segments, which are less volatile.
- In principle, we expect only a moderate demand growth of 1.9% CAGR over the next three years. Hence, **higher freight rate hikes are supply driven.** We expect **supply** to grow 2.5% and 1.7% during 2018E–2019E then drop-off to **-1.6% in 2020E.** We expect scrapping rates to reach 4.5% in 2020E compared to 1–1.5% run rates. A deep dive IMO 2020 Update by Citi's commodity team points to higher scrapping rates, as ship owners will likely find installation of scrubbers uneconomical while charterees will likely slow-steam to save fuel expenses.

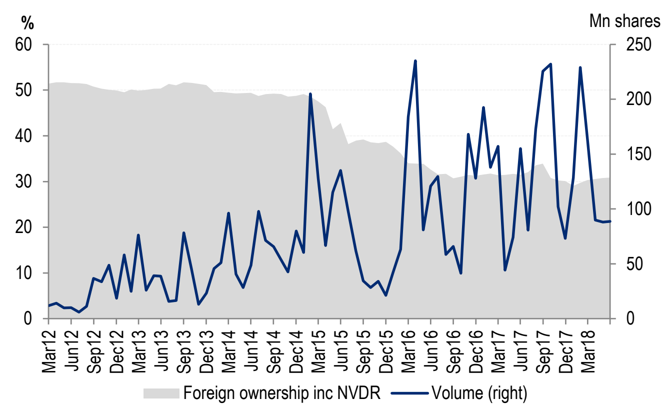
Year 2020 and IMO sulfur cap is our benchmark valuation as it is what market focuses on, in our view. PSL stock saw renewed interests among Thai based investors (Figure 2) from 4Q16 as IMO members agreed on October 27th 2016 to implement a global fuel sulfur cap of 0.5% on all vessels from January 2020.

Figure 1. PSL: Fwd. PBV vs. core ROE 2020E



Source: Citi Research, Bloomberg

Figure 2. Foreign ownership vs. share trading volume

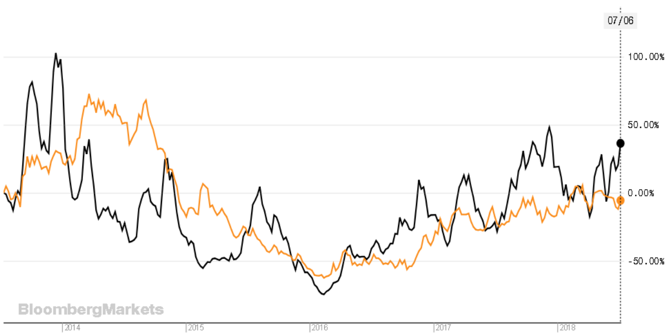


Source: Citi Research, Bloomberg

This was in addition to an update from *Marine Environment Protection Committee*'s meeting in October 2016 that **Ballast Water Management (BWM) Convention** will enter into force from September 2017, which was later delayed to September 2019 for existing fleet servicing international water. PSL's share price barely pulled-back, which probably indicates that investors in PSL were looking ahead to Sep19/Jan20 implementations of two key IMO regulations.

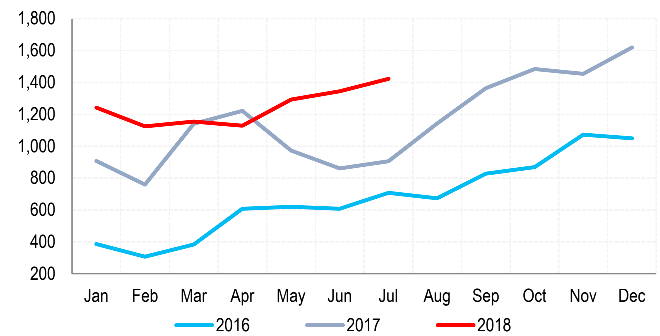
In addition to BDI movements which primarily drive near-term share price volatilities (not entirely fundamentally correct), we expect incremental news on enforcements of sulfur cap to be key structural catalysts to PSL. These include **(i)** incremental scrubber orders at key OEM suppliers such as *Wartsila* and *Alfa Laval* signaling preparations of ship owners for compliance, **(ii)** introductions of level and coordinated significant fines for "noncompliance". PSL guided that IMO is seeking to pass a new law in March 2019 that would make it illegal for any ship to have non-compliance fuel on board ships not fitted with pollution abatement technologies and **(iii)** clear guidelines on waivers of compliance fuel where supply is limited that ships cannot take advantage of.

Figure 3. PSL's share price vs Baltic Dry Index



Source: Citi Research, Bloomberg, Baltic Exchange

Figure 4. BDI seasonality: 2016-to-date



Source: Citi Research, Clarkson, Baltic Exchange

Key risks to our bullish view

We believe the delay to implementation of IMO 2020 sulfur cap is unlikely as IMO's Marine Environment Protection Committee (MEPC 70), in October 2016, decided that the 0.50% limit should apply from 1 January 2020. Hence **key risk is dry-bulk industry supply tightening not coming through or significantly delayed** ie. limited enforcement from port / flag states or non-compliance by shipping industry. These are the opposite of upcoming catalysts **(ii)** and **(iii)** above.

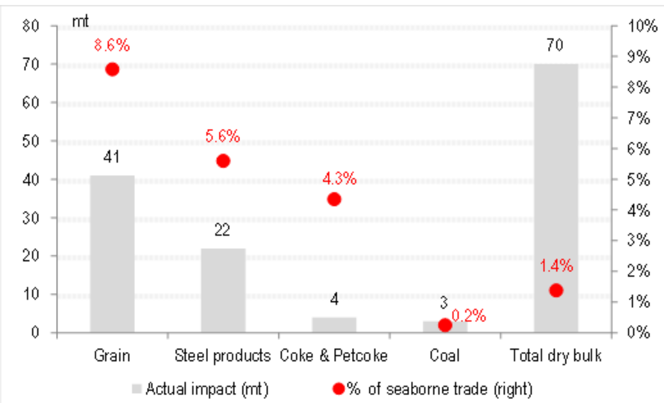
Assume 2020E scrap rates remain at 1.5% of YE2019 fleet rather than 4.5% assumed, 2020E industry's demand / supply balance will flip to –ve 1.1% from +1.9% in our base case. Our sensitivity indicates that should BDI retreat to c1,300, PSL would deliver roughly a breakeven core-ROE, which should coincide with 1.1x PBV. This translates to YE2019E fair-value of Bt8.4.

Note that we pay less importance on BWM Convention as the requirements to install new ballast water treatment systems on <u>existing vessels</u> is upon their special surveys ie. every 5th birthday, hence positive impact to industry's supply dynamic is on a <u>rolling basis</u> in comparison to January 2020 hard deadline on IMO sulfur cap. BMW Convention already took effect on new vessels keel-laid from September 8th 2017 onward, in comparison to September 2019 for existing ships.

Trade-war has been catching headlines recently. *Clarkson Research* estimates 70mt of global seaborne trade could be affected by "trade-friction" announced by US/ China up to Jun 18, or 1.4% of global seaborne trade. Grain is the key focus as the majority of effected volume is US-China. However, we believe this is manageable to dry-bulk freight markets as China still needs to consume grains and it has to source from less optimal export locations ie. South America, which may increase the ton-mile demand.

At a macro level, it is undeniable that Chinese exports value (a proxy for trade) has some positive correlation with Chinese seaborne iron ore import (most important dry-bulk uplifted product) from a function of global economy. However, we see Chinese Fixed Asset Investment (FAI) as a more relevant end demand indicator and is more domestic driven ie. infrastructure and property sector growth, where we already factor in Chinese steel demand to peak in 2018E and flat thereafter.

Figure 5. Est. % of seaborne trade could be effected by trademark



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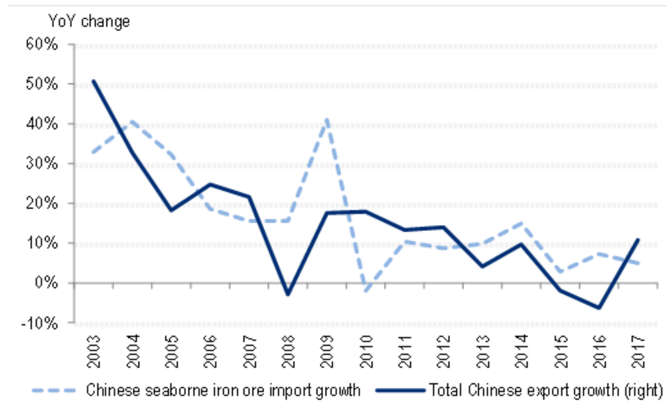
Source: Citi Research, Clarkson

Figure 6. YoY - Chinese seaborne iron ore imports vs China exports



Copy Chart/Table, then double click to insert

Source: Citi Research, Clarkson

Expected ROE uplifts justify higher valuation

Our Bt14.2 target price is based on 1.8x 2020E PBV and 14% 2020E core ROE, discounted back to YE2019 at 10.5% Ke. We see PBV in relation to expected ROE as a suitable valuation method as: **(i)** profitability of dry-bulk shipping industry is highly cyclical, **(ii)** PSL owns 100% of fleet ie. no chartered-in, **(iii)** the relationship between PBV multiples in relation to core ROE builds in local and stock-specific aspects such as scarcity of dry-bulk sector proxy.

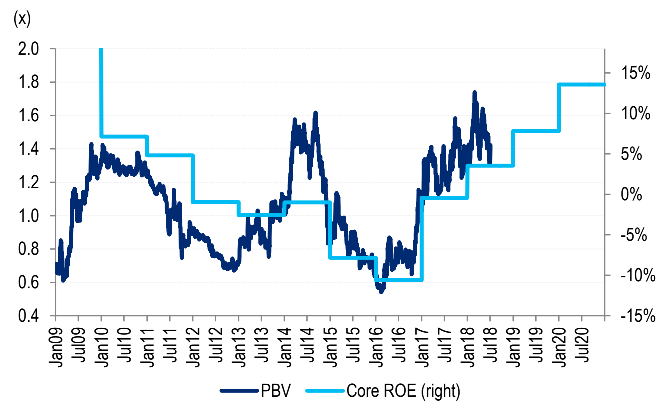
We see 1.8x 2020E PBV as suitable in relation our 14% 2020E core-ROE based on historical PBV / core ROE trading relationship over the past three years. Higher est. core ROE justifies higher PBV multiples, in our view, ceteris Paribas. Hence we believe PSL deserves to trade at a premium to current levels considering the expected increase in ROE from -0.4% in 2017 to ~14% in 2020E.

Year 2020E and IMO sulfur cap is our benchmark valuation as it is what market focuses on, in our view. Our 10.5% Ke used to discount PSL's fair-value back to YE2019 is based on 3% Rf, 8% Rp and 0.94x market Beta.

Year 2020, owing to implementation of IMO's sulfur cap on marine fuel, is our benchmark year of valuation as it is what market is focusing on, in our view. Our 10.5% Ke used to discount PSL's fair-value back to YE2019 is based on 3% Rf, 8% Rp and 0.94x market Beta.

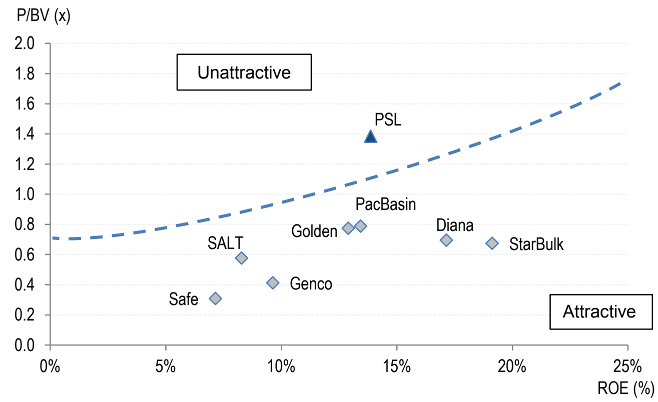
We highlight that our Buy rating on PSL could be considered tactical, especially to investors with mandates broader than ASEAN. PSL's valuation premium to global dry-bulk peers, even on 2020 basis, is undeniable (Figure 8). However, we do not think that PSL's share price could significantly decline in the near-term purely on valuation. This is because the stock ownership appears to be dominated by local investors (Figure 2), who tend to be shorter term / catalyst-focused and benchmarked against SET Index. Hence, we don't expect a significant valuation gap-down as long as IMO 2020 sulfur cap implementation remains intact. This is in addition to the scarcity of dry-bulk sector proxies among ASEAN mandated funds.

Figure 7. PSL: Fwd. PBV vs. core ROE 2020E



Source: Citi Research, Bloomberg

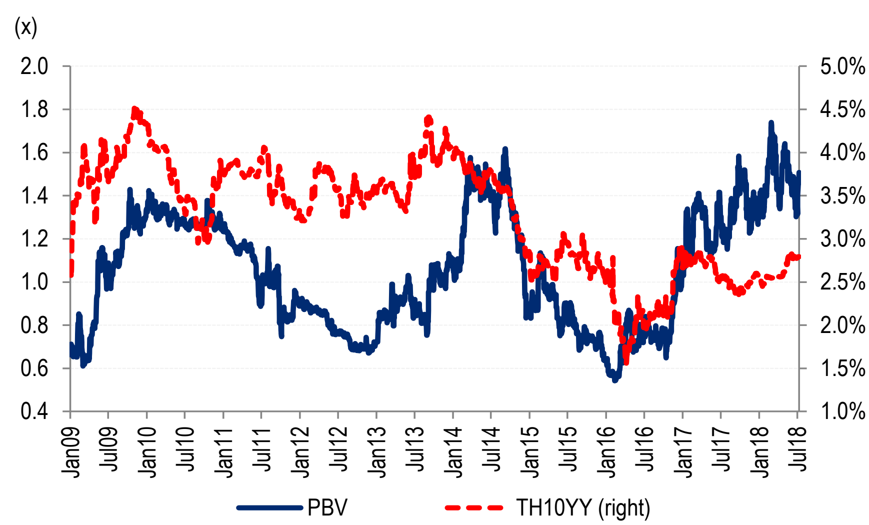
Figure 8. Global dry bulk carriers: 2020E PBV vs. 2020E ROE



Source: Bloomberg except PSL and Safe, which are based on Citi Research

One may argue why PSL should trade at higher PBV multiples into 2019E–2020E, in spite of similar core ROE to 2009–2010. Ceteris paribus, we believe c150bps lower risk free rates currently increase risk appetite in risky assets. Our economist sees TH10YY at 2.8% by YE2018 and 3% by YE2019 given benign inflation and moderate investment growth.

Figure 9. Lower risk free supports PSL's higher PBV multiples, ceteris paribus



Source: Citi Research Estimates, Bloomberg

We believe that comparing PSL to global dry-bulk carriers sector peers rather than Asia Pacific region based shipping peers is more relevant given limited shipping comparable in the listing domicile and differences in shipping segment's business cycles.

Figure 10. Global dry-bulk valuation comparables

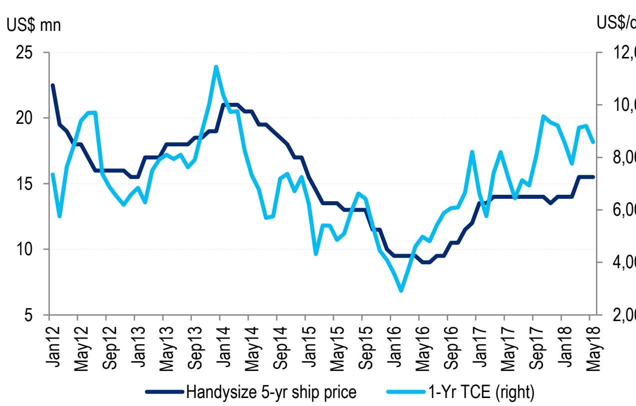
Company 9-Jul-18	BBG Code	Rating	FX	Share Price	Target Price	Mkt cap $mn	P/B 2018	P/B 2019	P/B 2020	ROE 2018	ROE 2019	ROE 2020	P/E 2018	P/E 2019	P/E 2020	EV / EBITDA 2018	EV / EBITDA 2019	EV / EBITDA 2020
Precious Shipping	PSL.TB	Buy	THB	12.1	14.2	571	1.5	1.4	1.4	4%	8%	14%	42.2	18.4	10.2	14.2	11.2	8.4
Pacific Basin	2343.HK	NR	HKD	2.13	NR	1,220	0.9	0.9	0.8	6%	11%	13%	14.7	7.8	5.9	8.0	6.4	5.6
Scorpio Bulkers	SALT.US	NR	USD	7.35	NR	558	0.6	0.6	0.6	1%	5%	8%	45.7	11.1	7.0	10.8	8.4	7.2
Eagle Bulk	EGLE.US	NR	USD	5.48	NR	400	0.8	0.7	n/a	3%	8%	n/a	26.2	8.6	4.3	4.9	3.5	2.8
Safe Bulkers	SB.US	Sell (3H)	USD	3.53	2.75	358	0.6	0.4	0.3	4%	7%	7%	17.0	7.3	5.0	7.3	4.4	2.3
Star Bulk	SBLK.US	NR	USD	13.2	NR	849	1.0	0.8	0.7	9%	14%	19%	10.4	5.6	3.5	6.4	4.3	3.3
Diana Shipping	DSX.US	NR	USD	4.96	NR	526	0.8	0.8	0.7	1%	9%	17%	55.1	8.5	4.1	11.4	7.4	5.2
Genco Shipping	GNK.US	NR	USD	15.8	NR	654	0.6	0.5	0.4	4%	7%	10%	16.2	7.7	4.3	7.5	5.7	4.4
Golden Ocean	GOGL.NO	NR	USD	8.68	NR	1,252	0.8	0.8	0.8	5%	8%	13%	16.5	9.4	6.0	10.1	8.6	7.0
Average							**0.8**	**0.8**	**0.7**	**4%**	**9%**	**13%**	**27.1**	**9.4**	**5.6**	**8.9**	**6.7**	**5.1**

Source: Bloomberg except PSL and Safe Bulkers, which are based on Citi Research

We are aware that second-hand vessel markets are highly liquid and volatile where the second hand prices move in tandem with freight rates (Figure 11–12). This means PBV multiples on a standalone basis are irrelevant as PSL often recognizes gains / losses from marking-to-market asset value during disposal.

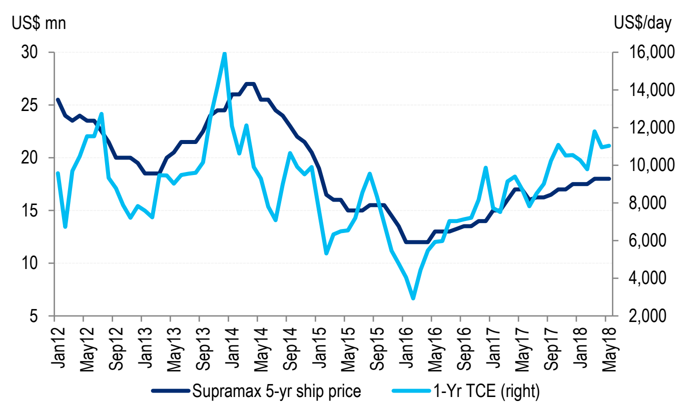
However, our valuation method of assigning PBV target multiple in relation core ROE est. already factors in the variations in second ship value. Higher freight rates translate to higher core ROE, which essentially translate to higher PBV multiples that capital market should be willing to pay for…as well as physical markets.

Figure 11. Handysize 5-Yr ship price vs. 1-Yr TCE rates



Source: Citi Research, Clarkson, Baltic Exchange

Figure 12. Supramax 5-Yr ship price vs. 1-Yr TCE rates



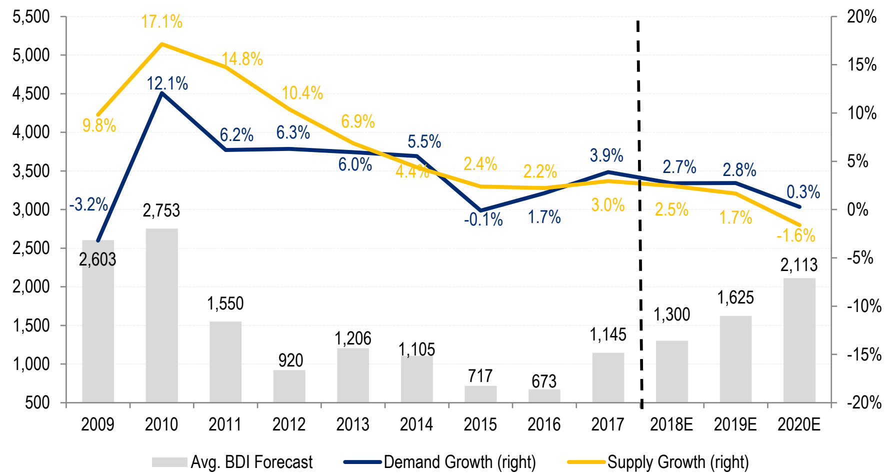
Source: Citi Research, Clarkson, Baltic Exchange

BDI set to improve over 2018E–2020E

We are positive on dry-bulk freight rates over 2018E–2020E driven by moderate demand growth, relative supply discipline during 2018E–2019E and negative supply growth in 2020E on higher scrapings post implementation of IMO 2020 sulfur cap. We forecast BDI to average 1,300 in 2018E (1,233 YTD), 1,625 in 2019E and 2,113 in 2020E, compared to 1,145 achieved in 2017.

The current YTD index remains at around industry's NPAT breakeven level (c1,200) and hence we expect industry profitability to remain weak, which should continue to support shippers' discipline in vessel expansion even without upcoming IMO regulations. However, the YTD is well above the cash breakeven level (c600) thus we don't expect any sharp pull-back in supply either.

Figure 13. Global dry bulk carriers Demand vs. Supply and Avg. BDI



Source: Citi Research Estimates, Clarkson

Our global dry bulk demand / supply assumptions summaries are shown in Figure 21 below, which indicates positive balance over 2018E–2020E as we foresee +1.9% demand CAGR over +0.8% supply CAGR over the period.

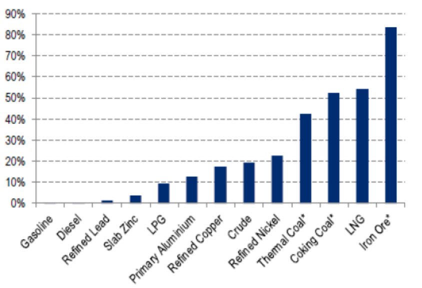
Our 2018E assumptions are based on Clarkson while 2019E-2020E are based on a combination of Citi's Global Commodity team (Global Commodities Focus: 2Q 2018) and European Machinery team outlook on shipping orders and Citi's APAC Transport team's assumptions.

Moderate demand growth expected

We forecast seaborne dry-bulk commodity demand to grow 2.7% in 2018E, 2.8% in 2019E and 0.3% in 2020E compared to 3.4% CAGR achieved over 2012–2017.

- **Iron ore (29% of uplifted demand):** Citi's commodity team forecasts Chinese demand for steel to grow 1.5% in 2018E then flat during 2019E-2020E as steel consumption is expected to be challenged by China's gradual shift away from its FAI driven economic model. Iron ore wise, we expect seaborne demand to peak in 2019E and turn negative 3.4% in 2020E primarily due to cutbacks of low-grade production.
- **Thermal coal (19%):** Expect slowing seaborne demand growth as falling capex should limit incremental supply under Adani (ADE IN, non-rated)'s flagship Carmichael project entering the market in 2022E–2023E.
- **Coking coal (5%):** Moderate 1-2% growth expected on the back of flat Chinese steel demand from 2019E and decline from 2020E onward.
- **Grain (9%) and minor bulks (38%):** We forecast 2–3% stable growth over 2018-2020E, in-line with global GDP growth given relatively stable end-consumption nature.

Figure 14. North Asian imports as % of world (Est. 2017)



*Global seaborne demand rather than total

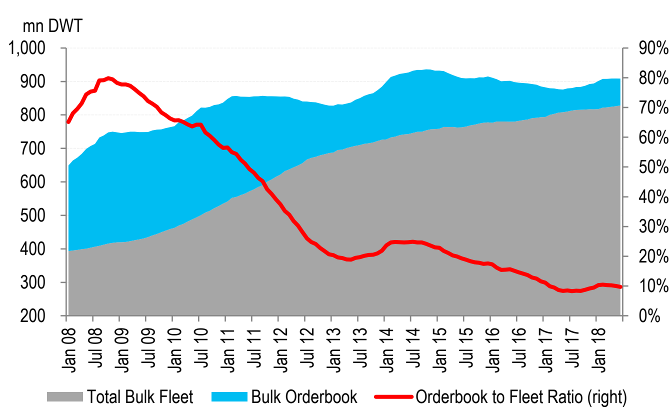
Source: Citi Research

Year 2020E, wildcard period where supply should shrink

The dry-bulk industry supply growth looks manageable (+2.5% in 2018E and +1.7% in 2019E) following nearly five consecutive years of losses as indicated by **(i)** orderbook as % of active fleet running at decade's low with **(ii)** projected supply growth slowing down, despite **(iii)** slowing demolition as cash +ve freight rates incentivize ship owners to milk assets for longer and coinciding with **(iv)** lower slippage rates into higher freight rates.

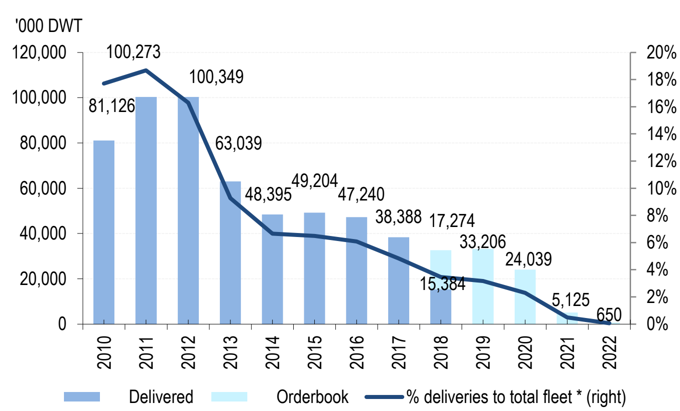
Investors should be aware that below industry numbers are not static ie. new orders will likely jump along with lower demolition if freight rates surge….and vice versa.

Figure 15. Orderbook to fleet is shrinking



Source: Citi Research, Clarkson

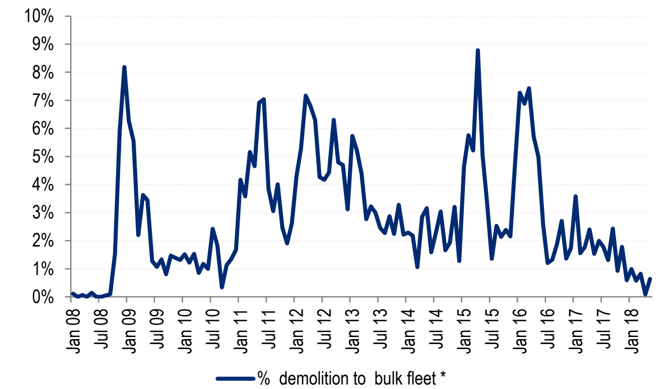
Figure 16. Deliveries as a % of total fleet is slowing



Note: For 2018, we assume 25% slippage on orderbook to arrive at estimated deliveries. We assume 20% slippage for 2019–22 on orderbook as a % of 2018 fleet. Lower slippage is on the back of higher rates

Source: Citi Research Estimates, Clarkson

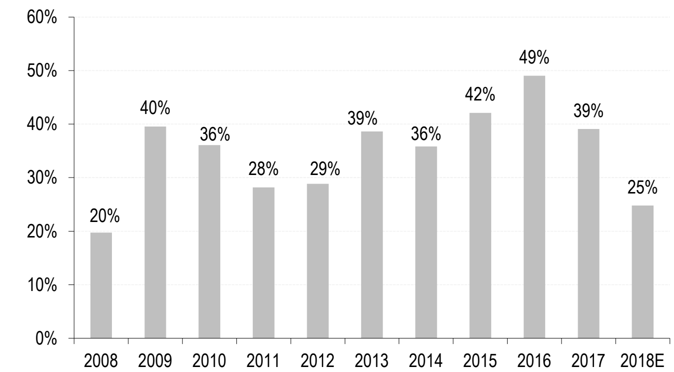
Figure 17. Demolitions as % of beginning fleet size*



* annualized

Source: Citi Research, Clarkson

Figure 18. Bulk carriers delivery slippage % estimated by Clarkson



Source: Citi Research, Clarkson

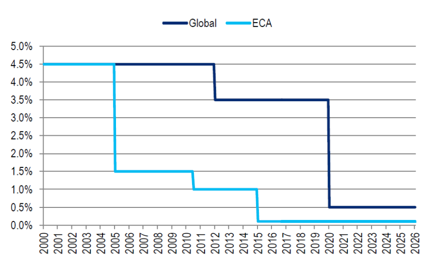
IMO 2020 sulfur cap – background, compliance options and impact

The milestone 2020 is when we expect industry's supply growth to turn negative 1.6%, driven by higher scrapping rates, upon the implementation of IMO 2020 sulfur cap on marine bunker fuel. We are segmenting our arguments down to background, compliance options, costs for noncompliance and likely end effect on dry-bulk shipping industry to derive at our assumptions.

Background: The IMO sulfur rule was announced a while back, but until more recently, there have been some hopes that it would be deferred (may be to 2025). The IMO confirmed in October 2016 that the rule would come into effect as originally stated on January 1, 2020.

Under the International Convention for the Prevention of Pollution from Ships (MARPOL) Annex VI, sulfur caps have evolved over time, most stringently first in the emission control areas (ECAs) ie North America and Northwest Europe; the global cap stayed relatively high, but 2020 makes a sharp change down to 0.5%.

Figure 19. IMO sulfur caps on marine fuel



Source: Citi Research, IMO

Two key compliance options: A switch to low-sulfur fuels (MGO, ULSFO, alternatives like LNG) or installing scrubbers for compliant use of high-sulfur fuel oil (HSFO) are two key options. We think a switch to low-sulfur fuels with slower steaming appears as the most optimal option.

- A switch to low-sulfur compliant fuels should cost cUS$400/t (cUS$60/bbl) more in Citi's base case; or cUS$3,500 per day of additional fuel cost charterees would have to pay for PSL's Handysize / Supramax vessel size. Our most recent IMO 2020 Update report dated 25 June 2018 suggests that fleet owners / charterees will likely slow steam in the face of rising fuel costs post-2020. Citi's sensitivity analysis suggests that a 2.2 knots slower steaming (c18% speed reduction and ton-mile supply) saves c50% of annual fuel volume consumption by bulk carriers.
- Installation of scrubbers does not appear as an optimal solution in our view. Fleets' abilities to run at slower speeds likely will provide material offset against scrubbers' payback period (vs using low sulfur oil) compared to their 2–3 year window of maximum utility. This is given slower steaming, middle distillate refining capacity buildout and adoptions of LNG fuel.

The costs to noncompliance: Level and coordination of fines across jurisdictions are still in discussion; one concern is that if the size of fines is small, it may be "worth" not complying, compared to sourcing what could be expensive low-sulfur fuels ie. US$1,500 fines vs additional US$100,000 costs on compliance fuel.

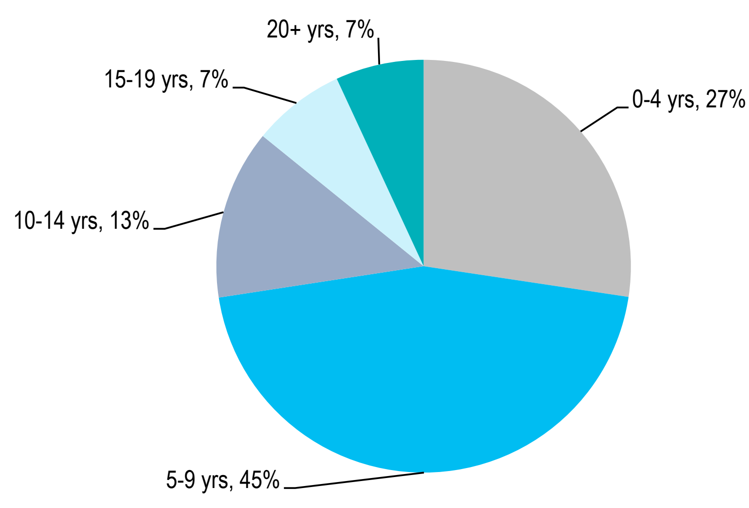
However, other than monetary penalties, another material punishment is detention of vessels. This could be coordinated across groups of port states. Other deterrents include shipping clients which do not want to be subjected to risks of shipments being detained, nor the reputational and legal risks. Non-compliance would also risk problems with financial institutions, lenders, insurers.

A surge in scrapping from 2020 as the likely end effect: Our view is based on two interrelated rationales. Older ships i.e. > 15 years old, are 15-25% less fuel efficient compared to younger fleet. This could create a two-tiered market in favor of new tonnage as charterees bare fuel expenses under time-charter model.

Secondly, the economics of scrubber installations on older ships are not attractive. Using the example of Handymax, the residual value of a 15-year is currently US$10m vs new-build prices at $26m (40% of new build price). With the total cost (including dry-docking) in the $3-6m range for open loop models, and $6m-$12m for hybrid/closed loop models, this represents 56% and 73% of the residual values respectively; an incentive to scrap for new build.

How we derive 4.5% scrappage assumption in 2020: Assuming no significant change to fleet age mix by end of 2019, 14% of global dry-bulk fleet is subjected to scrapping economics. We assume that the whole dry-bulk shipping value chain takes three years to adopt new sulfur standard in-line with expected refinery capacity buildout (fines establishment, charterees not taking risks and global availability of lower sulfur marine bunker fuel), which will work out to be 4.5% of scrappage rate per year (14% / 3 years).

Figure 20. Dry bulkers fleet age profile – June 2018



Source: Citi Research, Clarkson

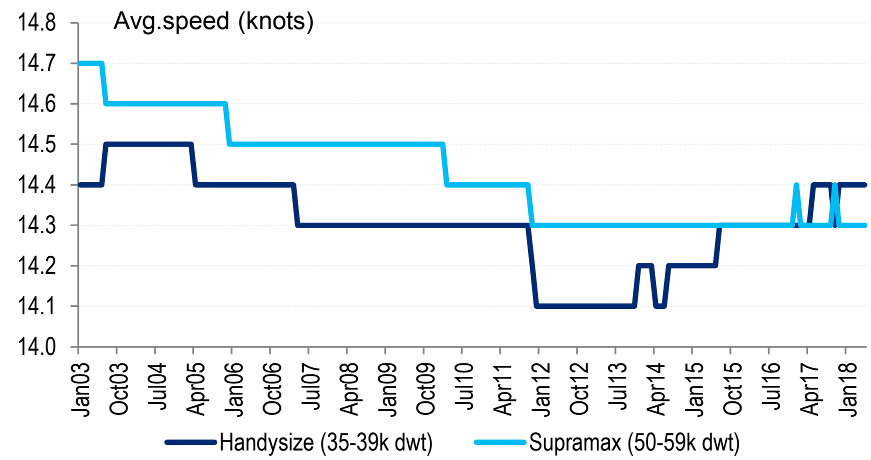
Figure 21. Global dry bulk carriers demand and supply outlook

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018E	2019E	2020E
Demand (mn tons)													
Iron ore	837	897	990	1,050	1,107	1,188	1,340	1,364	1,418	1,473	1,512	1,574	1,520
Thermal Coal	594	619	698	780	886	924	960	892	896	949	967	978	978
Coking Coal	196	185	228	218	225	259	256	245	246	256	264	266	270
Grains	285	298	318	316	345	363	408	429	450	478	485	495	503
Minor bulks (inc Bauxite & Alumina)	1,602	1,402	1,577	1,682	1,737	1,822	1,844	1,873	1,875	1,919	1,985	2,044	2,099
Total seaborne	**3,514**	**3,401**	**3,811**	**4,046**	**4,300**	**4,556**	**4,808**	**4,803**	**4,885**	**5,075**	**5,213**	**5,357**	**5,372**
Demand growth													
Iron ore	6.4%	7.2%	10.4%	6.1%	5.4%	7.3%	12.8%	1.8%	4.0%	3.9%	2.6%	4.1%	-3.4%
Thermal Coal	3.3%	4.2%	12.8%	11.7%	13.6%	4.3%	3.9%	-7.1%	0.4%	5.9%	1.9%	1.2%	0.0%
Coking Coal	-1.0%	-5.6%	23.2%	-4.4%	3.2%	15.1%	-1.2%	-4.3%	0.4%	4.1%	3.1%	0.6%	1.8%
Grains	-6.9%	4.6%	6.7%	-0.6%	9.2%	5.2%	12.4%	5.1%	4.9%	6.2%	1.5%	2.0%	1.8%
Minor bulks (inc Bauxite & Alumina)	-1.5%	-12.5%	12.5%	6.7%	3.3%	4.9%	1.2%	1.6%	0.1%	2.3%	3.4%	3.0%	2.7%
Total demand growth	**0.6%**	**-3.2%**	**12.1%**	**6.2%**	**6.3%**	**6.0%**	**5.5%**	**-0.1%**	**1.7%**	**3.9%**	**2.7%**	**2.8%**	**0.3%**
Uplifted commodity breakdown													
Iron ore	24%	26%	26%	26%	26%	26%	28%	28%	29%	29%	29%	29%	28%
Thermal Coal	17%	18%	18%	19%	21%	20%	20%	19%	18%	19%	19%	18%	18%
Coking Coal	6%	5%	6%	5%	5%	6%	5%	5%	5%	5%	5%	5%	5%
Grains	8%	9%	8%	8%	8%	8%	8%	9%	9%	9%	9%	9%	9%
Minor bulks (inc Bauxite & Alumina)	46%	41%	41%	42%	40%	40%	38%	39%	38%	38%	38%	38%	39%
Total seaborne	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**
Supply (mn DWT)													
Fleet size	417.3	458.3	536.8	616	680	726.8	758.6	776.7	794	817.5	837.6	851.5	837.9
Deliveries - a	24.3	43.1	80.3	98.6	98.8	62.7	48.1	49.3	47.2	38.1	27.3	26.5	24.7
Scrapping	-5.5	-10.6	-6.5	-23.2	-33.4	-23.2	-16.3	-30.6	-29.2	-14.5	-7.0	-12.6	-38.1
Dry-dock / Laid up balance	6.0	8.5	4.7	3.8	-1.4	7.3	0.0	-0.6	-0.7	-0.1	-0.2	-0.1	-0.1
Total supply growth	**6.3%**	**9.8%**	**17.1%**	**14.8%**	**10.4%**	**6.9%**	**4.4%**	**2.4%**	**2.2%**	**3.0%**	**2.5%**	**1.7%**	**-1.6%**
Orderbook development													
Beginning orderbook	225.9	323.2	303.4	301.9	240.3	141.5	158.7	173.7	134.5	88.8	84.2	80.4	74.8
Deliveries - a	-24.3	-43.1	-80.3	-98.6	-98.8	-62.7	-48.1	-49.3	-47.2	-38.1	-27.3	-26.5	-24.7
New orders	114	37	103	42	26	91	65	41	48	74	24	31	37
Delays / cancellations (net)	0	-14	-24	-15	-16	0	-11	-33	-44	-44	0	-9.6	-9.0
Prior Year Delays (net)	8	0	0	0	0	2	0	0	0	0	0	0	0
Ending orderbook	**323.2**	**303.4**	**301.9**	**230.6**	**141.5**	**171.0**	**177.1**	**131.8**	**87.9**	**80.5**	**80.4**	**74.8**	**77.8**
Supply ratios - %													
Deliveries as % of T-1 fleet	6.2%	10.3%	17.5%	18.4%	16.0%	9.2%	6.6%	6.5%	6.1%	4.8%	3.3%	3.2%	2.9%
Scrapping as % of T-1 fleet	1.4%	2.5%	1.4%	4.3%	5.4%	3.4%	2.2%	4.0%	3.8%	1.8%	0.9%	1.5%	4.5%
Orderbook to fleet %	77%	66%	56%	37%	21%	24%	23%	17%	11%	10%	10%	9%	9%
Deliveries as % of beginning order	11%	13%	26%	33%	41%	44%	30%	28%	35%	43%	32%	33%	33%
Summary forecasts													
Demand growth	0.6%	-3.2%	12.1%	6.2%	6.3%	6.0%	5.5%	-0.1%	1.7%	3.9%	2.7%	2.8%	0.3%
Supply growth	6.3%	9.8%	17.1%	14.8%	10.4%	6.9%	4.4%	2.4%	2.2%	3.0%	2.5%	1.7%	-1.6%
Demand - Supply	**-5.7%**	**-13.0%**	**-5.1%**	**-8.6%**	**-4.1%**	**-0.9%**	**1.2%**	**-2.5%**	**-0.5%**	**0.9%**	**0.3%**	**1.1%**	**1.9%**
BDI YoY	-11%	-59%	6%	-44%	-41%	31%	-8%	-35%	-6%	70%	14%	25%	30%
Avg. BDI Forecast	**6,341**	**2,603**	**2,753**	**1,550**	**920**	**1,206**	**1,105**	**717**	**673**	**1,145**	**1,300**	**1,625**	**2,113**

Source: Clarkson estimates for 2018, Citi Research Estimates for 2019E – 2020E

We see a soft BDI ceiling of 2,700–3,000 as industry's ROIC will likely approach mid-teen. The level will likely trigger ordering activities as well as slow steaming reversal as higher freight rates incrementally offset fuel saving benefits.

Figure 22. Global Handysize and Supramax have gradually been slower steaming



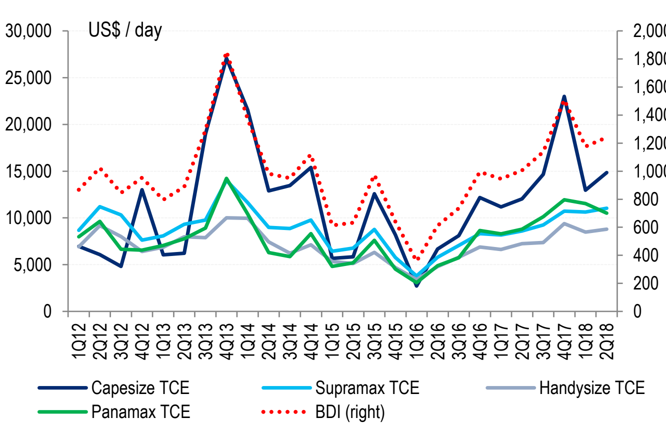
Source: Citi Research, Clarkson

BDI movements should incrementally reflect PSL's freight rates

We highlighted earlier in our investment these section that BDI volatilities as key catalyst for PSL stock is not entirely correct fundamentally. This is because BDI (equal weighting among four ship classes) is mostly driven by Capesize vessels (Figure 23), which primarily carry iron ore where PSL has no direct exposure to Capesize segment and has limited iron ore uplift (Figure 24).

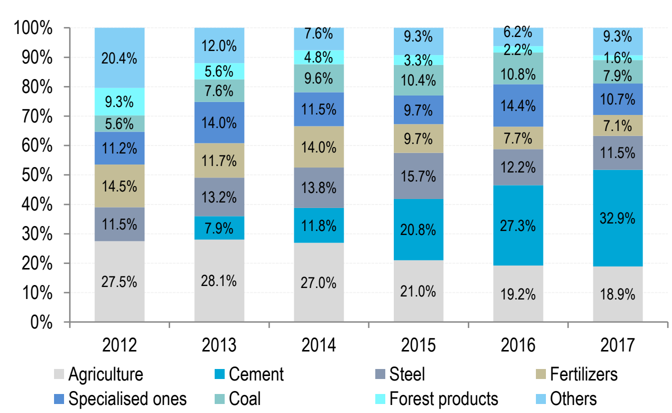
However, freight rates tend to move together given cascading substitution effects between adjacent ship classes to some degree. Hence, we apply a 0.8x factor to PSL's spot freight rate changes to our BDI forecasts. This primarily explains the differences in our 23% BDI CAGR expected over 2017–2020E in comparison to PSL's 15% CAGR on average revenue per shipday over the same period.

Figure 23. TCE daily rates VS Baltic Dry Index



Source: Citi Research, Baltic Exchange, Clarkson

Figure 24. PSL's uplifted commodity breakdown by tonnage



Source: Citi Research, PSL's annual reports

Financial forecasts

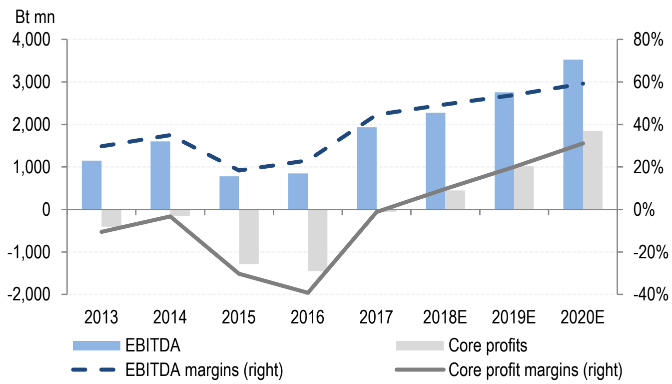
Expect profitability to sail higher over 2018E–2020E

We forecast PSL to turn profitable at core earnings from 2018E, from a slight loss in 2017, and sail higher into 2020E. This is purely driven by our expectation of higher freight rates as PSL has no ship on orderbook or official plan to further dispose vessels. On the same time scale, we forecast EBITDA to grow 22% CAGR over 2017–2020E.

Our forecasts imply that EBITDA margins should improve to nearly 60% by 2020E from 45% achieved in 2017 while core profit margins should reach 31% by 2020E from a mare breakeven in 2017. This is not a surprised given a very high operating leverage nature of the shipping (and other assets heavy) industry.

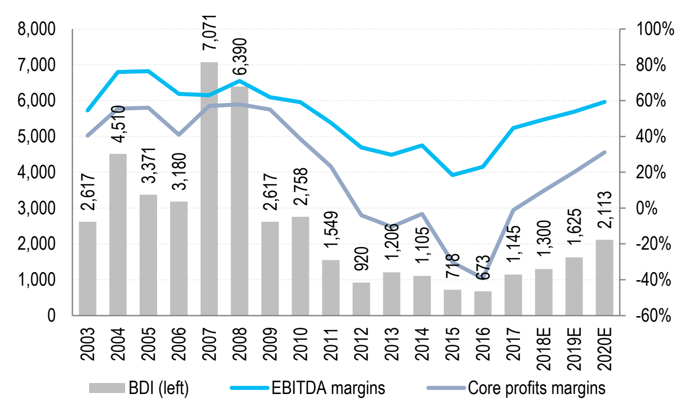
The 60% EBITDA margins were achieved back in 2009–2010 when BDI averaged 2,617 and 2,768 respectively which were higher than our 2,113 estimates for 2020E. However, it is worth noting that PSL's average fleet age were 17 and 14 years old respectively compared to 6 years currently (or 8 by 2020E), reflecting lower day rates and EBITDA margins.

Figure 25. PSL – earnings and margins forecasts



Source: Citi Research Estimates, Company Reports

Figure 26. Reference points: BDI vs PSL profitability



Source: Citi Research Estimates, Company Reports, Baltic Exchange

In comparison to consensus, our core earnings estimates are 14% and 6% below during 2018E–2019E respectively. This is more likely due to our less bullishness on freight rates as our forecasts are lower from top-line down. We are 28% above in 2020E, most likely due to our expectation of PSL's strong FCF to pay down debt leading to lower interest expenses.

Figure 27. Citi vs. consensus estimates (2018E-20E)

	2018E			2019E			2020E		
	Citi	Consensus	Diff	Citi	Consensus	Diff	Citi	Consensus	Diff
Sales	4,605	5,003	-8%	5,117	5,694	-10%	5,945	6,276	-5%
EBITDA	2,276	2,509	-9%	2,755	3,159	-13%	3,524	3,542	0%
EBIT	1,137	1,362	-16%	1,641	1,975	-17%	2,415	2,316	4%
Reported profits	447	518	-14%	1,023	1,094	-6%	1,850	1,442	28%
Core profits	447	518	-14%	1,023	1,094	-6%	1,850	1,442	28%

Source: Citi Research Estimates, Bloomberg consensus

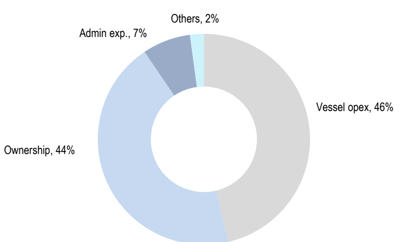
We forecast PSL's average revenue per shipday to reach US$14,668 in 2020E from US$9,747 achieved in 2017 or 15% CAGR. This is slightly lower than 23% CAGR in BDI expected over the same period as PSL operates less volatile Handysize / Supramax ship segment in addition to 17% of shipdays are already on fixed time-charter contracts.

Figure 28. Key revenue assumptions (2013-2020E)

	2013	2014	2015	2016	2017	2018E	2019E	2020E
Total shipday	15,533	15,550	18,272	16,040	13,147	13,140	13,140	13,176
Avg. BDI	1,206	1,105	719	673	1,145	1,300	1,625	2,113
YoY change	31%	-8%	-35%	-6%	70%	14%	25%	30%
Avg. TC per shipday (US$)	8,048	9,048	6,756	6,509	9,747	11,067	12,538	14,668
YoY change	-20%	12%	-25%	-4%	50%	14%	13%	17%

Source: Citi Research estimates, Company reports, Baltic Exchange, Clarkson

Figure 29. Expenses breakdown – 2018E



Source: Citi Research Estimates

We expect total cost per shipday (US$) to reach US$10,095 in 2020E from US$9,946 in 2017 (0.5% CAGR) and expect cash opex per shipday to increase by 3.5% CAGR over the same period to reach US$5,986 in 2020E.

We think increases in daily cash opex per shipday, slightly ahead of inflation, are realistic as PSL has fully completed its fleet rejuvenation program hence average age will increase from now in addition to potentially higher staff compensations into higher freight rates / profitability environment.

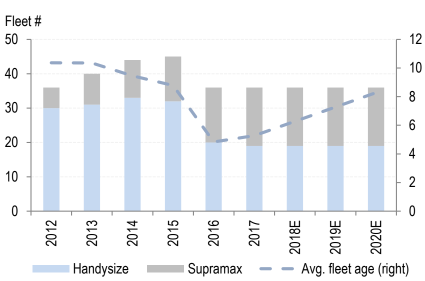
Our USD/THB assumptions are 31.6 for 2018E and 31.0/30.7 for 2019E/2020E, generally in line with our house view. These are less sensitive as PSL operates in international water where most of revenue and expenses are USD denominated.

Figure 30. Key cost trends & assumptions (2013-2020E)

	2013	2014	2015	2016	2017	2018E	2019E	2020E
Total costs per shipday (US$)	8,999	9,389	8,833	9,167	9,946	10,061	10,057	10,095
Cash opex per shipday (US$)	5,671	5,895	5,525	5,019	5,402	5,608	5,800	5,986
Daily costs per shipday - yoy	-15.3%	4.3%	-5.9%	3.8%	8.5%	1.2%	0.0%	0.4%
Cash opex per shipday - yoy	-15.6%	3.9%	-6.3%	-9.2%	7.6%	3.8%	3.4%	3.2%
USD / THB	30.9	32.5	34.4	35.3	33.8	31.6	31.0	30.7

Source: Citi Research estimates, Company reports, Bloomberg

Figure 31. PSL's fleet rejuvenation completed

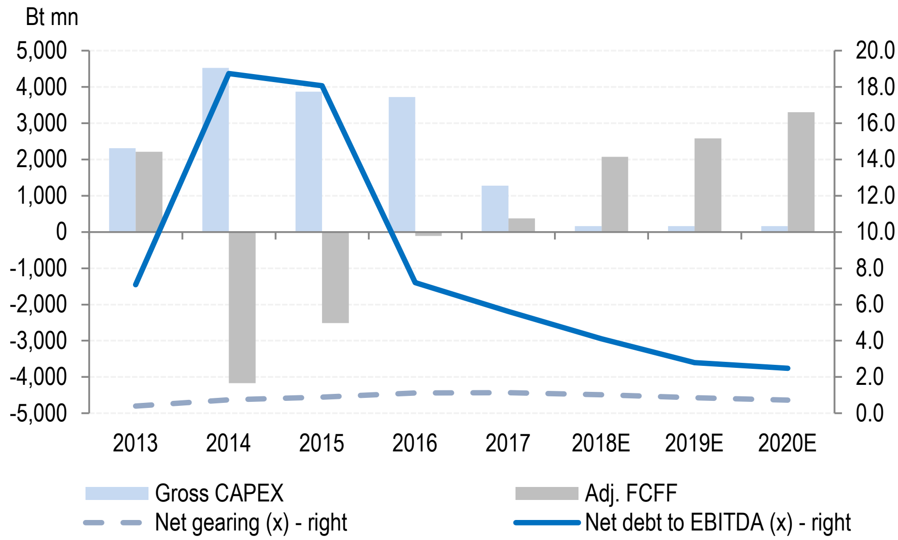


Source: Citi Research Estimates, Company data

PSL's free cash flow turned positive in 2017 following three years of fleet rejuvenation cycle against weak freight environment. The capex cycle is now behind with no outstanding orderbook into rising freight rate, translating to robust FCF outlook and ability to pay down debt.

We understand that PSL may gradually divest up to 11 ships out of 36 current fleet size into higher freight rates / second hand ship prices. The intension is to turn PSL debt free, which we think could be possible should BDI sustainably heads above 2500 beyond 2020 assuming limited slow steaming reversal.

Figure 32. FCF, capex and gearing trends



*PSL has 2 debt covenants namely (i) 2x net gearing and (ii) 6x net debt to EBITDA

Source: Citi Research estimates, Company reports

Earnings sensitivity

Revenue per shipday is the most sensitive factor to PSL's profitability given the industry's high operating leverage nature. According to our estimate, a 100bps increase in revenue per shipday could increase 2019E core earnings by 4% after incorporating the fact that PSL has already fixed 17% of 2018E – 2020E capacity on long-term charter contracts.

PSL is arguably 100% naturally hedged to FX. It operates in international waters where nearly all of revenues and expenses are USD denominated. At a balance sheet level where financing is in non-USD denominated debt, PSL swaps the principal and/or interest into USD to mitigate the FX risks.

Figure 33. Sensitivity analysis to earnings

		Rev / Cost (Btmn)			% of EBITDA			% of core profits		
1% increase in factors	**Impact**	**2018E**	**2019E**	**2020E**	**2018E**	**2019E**	**2020E**	**2018E**	**2019E**	**2020E**
Revenue per shipday incl fixed time-charter	↑	38.2	42.6	49.4	1.7%	1.5%	1.4%	8.4%	4.1%	2.6%
Cash opex per shipday	↓	-23.3	-23.6	-24.2	-1.0%	-0.9%	-0.7%	-5.1%	-2.3%	-1.3%
Total Cost per shipday	↓	-41.8	-41.0	-40.8	-1.8%	-1.5%	-1.2%	-9.2%	-3.9%	-2.2%

Source: Citi Research Estimates, Company reports, Baltic Exchange

Bull/Bear: Precious Shipping (PSL.BK)

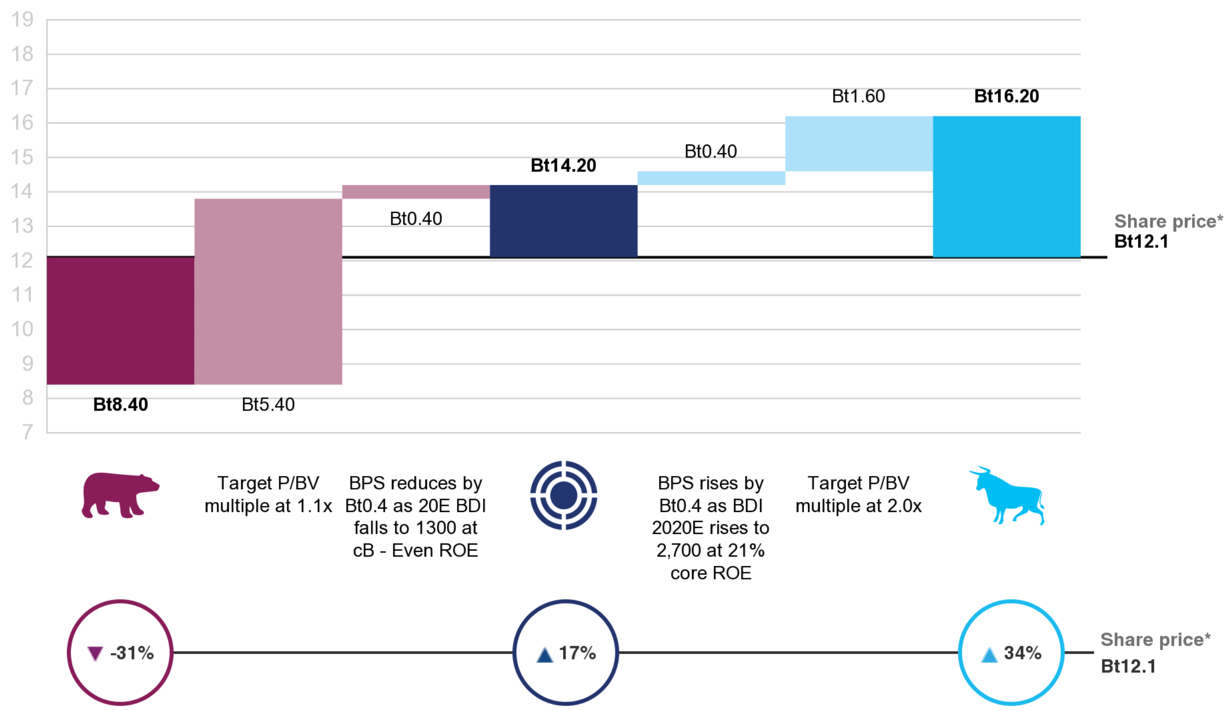
Bull/Bear: Precious Shipping (PSL.BK)

Bt14.2 target price

17% expected share price return

Buy rating

65pp Bull/Bear Spread



Source: Citi Research

***Share price as of 12 Jul 2018 17:00**

Bt16.2

- Scrappage rises to 7% in 2020e as dry-bulk fleet over 15 years old is scrapped over 2ys vs 3yrs in our base case. 2020E D&S balance increases to +4.4%. 2020E BDI increases to 2,700, translating to 21% core ROE and 2x P/BV.

Bt14.2

- Assume scrapping rate of 4.5% in 2020E with D&S balance of +1.9%. BDI reaches 2,113 in 2020E translating to PSL's core ROE of 14%, a level that reflects 1.8x P/BV. Our 2020E fair value is discounted back to YE2019E at 10.5% Ke.

Bt8.4

- We assume 2020E scrappage rates remain at 1.5% of YE2019E fleet, D&S balance flips to –ve 1.1% from +1.9% in our base case. 2020E BDI retreats to 1,300 and PSL delivers a breakeven core-ROE translating to 1.1x P/BV.

Figure 34. PSL Financial summary

Financials (Bt mn)	2013	2014	2015	2016	2017	2018E	2019E	2020E
Profit & Loss Statement								
Time charter	2,618	3,308	2,920	2,878	3,692	3,906	4,341	5,043
COA	1,240	1,267	1,329	805	637	689	766	890
Vessel operating income	**3,858**	**4,575**	**4,249**	**3,682**	**4,329**	**4,595**	**5,107**	**5,933**
Service income	11	10	8	7	4	9	10	12
Total operating revenue	**3,869**	**4,585**	**4,257**	**3,690**	**4,333**	**4,605**	**5,117**	**5,945**
Vessel running exp.	-1,665	-1,980	-2,256	-2,011	-1,677	-1,586	-1,612	-1,655
Vessel disbursements	-172	-208	-333	-243	-138	-155	-157	-161
Bunker consumption	-548	-536	-495	-232	-176	-193	-197	-202
Total vessel ops. Costs	**-2,386**	**-2,724**	**-3,084**	**-2,486**	**-1,990**	**-1,934**	**-1,966**	**-2,019**
Cost of services	-5	-5	-5	-5	-5	-4	-4	-4
Administrative exp.	-218	-173	-289	-260	-322	-307	-307	-311
Management remuneration	-109	-79	-97	-88	-82	-84	-86	-88
Total operating expenses	**-2,718**	**-2,981**	**-3,475**	**-2,840**	**-2,399**	**-2,329**	**-2,363**	**-2,421**
EBITDA	**1,151**	**1,605**	**782**	**850**	**1,934**	**2,276**	**2,755**	**3,524**
Depreciation & Amortization	-1,137	-1,267	-1,515	-1,366	-1,170	-1,139	-1,113	-1,109
Operating EBIT	**14**	**338**	**-734**	**-516**	**764**	**1,137**	**1,641**	**2,415**
Exchange gains	13	4	-25	45	-12	0	0	0
Gain / loss on disposal / novation	935	67	-1,115	-1,244	-74	0	0	0
Bad debts	-2	-2	-6	-25	8	0	0	0
Other gain/loss	2	0	10	7	0	0	0	0
EBIT reported	**963**	**407**	**-1,870**	**-1,733**	**686**	**1,137**	**1,641**	**2,415**
Interest income	9	5	2	47	23	19	10	10
Interest expenses	-459	-500	-565	-980	-848	-711	-621	-553
Associates income	32	8	8	3	10	11	14	18
Earnings before tax	**545**	**-80**	**-2,424**	**-2,663**	**-129**	**457**	**1,045**	**1,890**
Income tax	-8	-2	-2	0	0	-9	-21	-38
NPAT to company	**537**	**-82**	**-2,426**	**-2,663**	**-129**	**448**	**1,024**	**1,852**
Minorities	-9	2	0	-2	0	0	-1	-2
NPAT to PSL TB	**528**	**-80**	**-2,426**	**-2,665**	**-129**	**447**	**1,023**	**1,850**
Core profits	**-408**	**-151**	**-1,289**	**-1,448**	**-51**	**447**	**1,023**	**1,850**
Reported EPS	0.51	-0.08	-1.82	-1.71	-0.08	0.29	0.66	1.19
Core EPS	-0.39	-0.15	-0.97	-0.93	-0.03	0.29	0.66	1.19
BVPS	15.04	14.70	12.37	8.76	7.91	8.05	8.38	8.74
DPS	0.40	0.30	0.00	0.00	0.00	0.14	0.33	0.83
EBITDA Margin (%)	30%	35%	18%	23%	45%	49%	54%	59%
Operating EBIT Margin (%)	0%	7%	-17%	-14%	18%	25%	32%	41%
Core Profit Margin (%)	-11%	-3%	-30%	-39%	-1%	10%	20%	31%
Revenue Growth (%)	11%	19%	-7%	-13%	17%	6%	11%	16%
EBITDA Growth (%)	-3%	39%	-51%	9%	127%	18%	21%	28%
Core Profit Growth (%)	n/m	n/m	n/m	n/m	n/m	n/m	129%	81%

Source: Citi Research estimates, Company reports

Figure 35. PSL Financial summary

Financials (Bt mn)	2013	2014	2015	2016	2017	2018E	2019E	2020E
Balance Sheet								
Cash and equivalents	2,942	535	454	2,676	1,854	1,013	969	936
Bunker oil	102	115	143	41	56	72	72	72
Accounts receivable	1,074	318	241	140	193	202	217	252
Other current assets	818	205	192	244	148	157	174	202
Total current assets	**4,936**	**1,173**	**1,029**	**3,101**	**2,251**	**1,443**	**1,432**	**1,463**
Property, plant and equipment	18,670	22,071	25,330	25,672	23,475	22,494	21,539	20,589
Other non-current asset	1,905	4,665	6,099	3,543	3,108	2,974	2,974	2,974
Total assets	**25,510**	**27,909**	**32,458**	**32,316**	**28,833**	**26,911**	**25,945**	**25,026**
Account payable	22	128	99	38	70	70	78	80
Other payable (accrued exp.)	200	283	335	270	394	223	227	232
Other liabilities	385	300	439	315	243	268	278	295
Interest Bearing Liabilities								
Short term	654	812	5,604	887	802	690	615	540
Long term	8,619	11,101	9,495	17,146	14,988	13,101	11,676	10,251
Equities of PSL	**15,621**	**15,285**	**16,488**	**13,659**	**12,335**	**12,559**	**13,071**	**13,626**
Minorities	10	-1	-2	0	0	0	2	3
Total Liabilities and equities	**25,510**	**27,909**	**32,458**	**32,316**	**28,833**	**26,911**	**25,945**	**25,026**
Cash Flow								
Cash flows from operations	1,013	1,346	1,046	693	2,010	2,099	2,736	3,466
Cash flows from investment	1,200	-5,512	-3,561	-806	-1,637	-24	-158	-160
Cash flows from financing	-1,289	1,778	2,259	2,356	-949	-2,916	-2,622	-3,339
Net change in cash	1,041	-2,407	-81	2,223	-823	-841	-44	-33
Ratios								
Core ROE	-3%	-1%	-8%	-11%	0%	4%	8%	14%
Net gearing (x) – 2x covenant	0.4	0.7	0.9	1.1	1.1	1.0	0.9	0.7
Net debt (Bt mn)	6,331	11,378	14,645	15,357	13,937	12,778	11,322	9,855
EBITDA coverage	2.5	3.2	1.4	0.9	2.3	3.2	4.4	6.4
Net debt to EBITDA (x) – 6x covenant	5.5	7.1	18.7	18.1	7.2	5.6	4.1	2.8

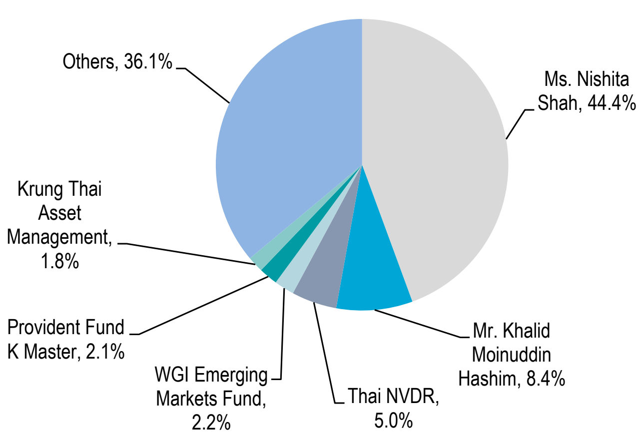
Source: Citi Research estimates, Company reports

Company description

Established in 1989, Precious Shipping (PSL) is a dry-bulk ship owner operating with 36 ships in the Handysize, Supramax and Ultramax segments. Along with a network of shipping agents worldwide, PSL operates mainly in the handysize sector wherein primary cargos include agricultural products, cement, steel, fertilizers, ore and concentrates, coal and forest products.

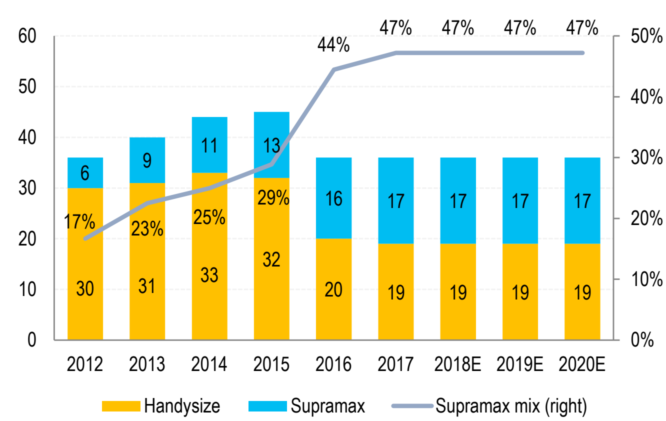
Company charters its ships either through time charter (charterer pays charter hire to PSL to operate the vessel for a specified time) or voyage charter (charterer pays freight to PSL to transport a particular cargo between different ports).

Figure 36. PSL – shares ownership structure



Source: Citi Research, Company report, Bloomberg

Figure 37. PSL – fleet size and fleet mix



Source: Citi Research Estimates, Company data

Figure 38. PSL's fleet profile – YE2017

No.	Type	Vessel Name	Year Built	Avg. Age	DWT	Net Book Value (US$mn)	Insured Value (US$mn)
1	Handysize	Rattana Naree	2002	15	28,442	9.30	9.5
2	Handysize	Rojarek Naree	2005	12	29,870	14.40	12.0
3	Handysize	Nalinee Naree	2005	12	31,699	15.16	12.5
4	Handysize	Chamchuri Naree	2005	12	33,733	13.82	11.5
5	Handysize	Charana Naree	2005	12	33,720	13.84	11.5
6	Handysize	Mookda Naree	2009	8	30,162	14.51	12.0
7	Handysize	Mayuree Naree	2008	9	30,193	13.82	11.5
8	Handysize	Mallika Naree	2008	9	30,195	12.94	10.5
9	Handysize	Lanna Naree	2012	5	33,843	16.31	13.5
10	Handysize	Latika Naree	2012	5	33,869	16.65	14.0
11	Handysize	Ananya Naree	2011	6	33,857	23.80	20.5
12	Handysize	Benjamas Naree	2012	5	33,780	24.24	21.0
13	Handysize	Chintana Naree	2013	4	33,945	20.55	18.0
14	Handysize	Vipha Naree	2015	2	38,851	20.81	18.5
15	Handysize	Viyada Naree	2016	1	38,716	21.41	18.5
16	Handysize	Apinya Naree	2014	3	21,136	21.88	30.0
17	Handysize	Boonya Naree	2014	3	21,159	22.38	29.5
18	Handysize	Chanya Naree	2014	3	21,114	22.12	29.5
19	Handysize	Danaya Naree	2015	2	21,149	22.89	32.0
20	Supramax	Kanchana Naree	2011	6	56,920	21.37	18.5
21	Supramax	Kirana Naree	2011	6	56,823	21.42	18.5
22	Supramax	Warisa Naree	2010	7	53,839	11.42	9.5
23	Supramax	Wariya Naree	2011	6	53,833	12.27	10.0
24	Supramax	Wikanda Naree	2013	4	53,857	14.77	12.5
25	Supramax	Apiradee Naree	2012	5	56,512	23.70	20.5
26	Supramax	Baranee Naree	2012	5	56,441	23.87	20.5
27	Supramax	Chayanee Naree	2012	5	56,548	23.26	20.0
28	Supramax	Daranee Naree	2012	5	56,588	23.54	20.0
29	Supramax	Inthira Naree	2014	3	63,468	25.17	22.5
30	Supramax	Issara Naree	2014	3	63,516	25.35	22.5
31	Supramax	Sarita Naree	2015	2	62,964	24.81	22.5
32	Supramax	Sarika Naree	2015	2	63,023	24.65	22.5
33	Supramax	Savitree Naree	2016	1	63,016	24.65	24.0
34	Supramax	Savita Naree	2016	1	62,970	24.92	24.0
35	Supramax	Sunisa Naree	2016	1	63,007	25.12	24.0
36	Supramax	Sarocha Naree	2017	0	63,047	26.07	25.0
				5.3	**1,585,805**	**717**	**673**

Source: Citi Research, Company Reports

Precious Shipping

Company description

Established in 1989, Precious Shipping (PSL) is a dry-bulk ship owner operating with 36 ships in the Handysize, Supramax and Ultramax segments. Along with a network of shipping agents worldwide, PSL operates mainly in the handysize sector wherein primary cargos include agricultural products, cement, steel, fertilizers, ore and concentrates, coal and forest products. Company charters its ships either through time charter (85% of revenue) or voyage charter (15% of revenue).

Investment strategy

Our Buy rating on Precious Shipping (PSL) is anchored on our expectation of rising dry-bulk freight rates driven by supply tightening over the next three years, especially post implementation of IMO sulfur cap regulation from January 2020. PSL stands to benefit directly given (i) 83% of its capacity is on spot market over 2018E–2020E, (ii) its 36 vessels with an average fleet age of 6 years is in-full compliance to IMO sulfur cap, and (iii) robust FCF given no new build orderbook. We forecast PSL's avg. daily earnings per ship to reach US$14,668 in 2020E, a 15% CAGR from 2017, compared to est. total daily costs of US$10,095 in 2020E. Our 2020E earnings are 28% above consensus. These translate to core ROE of 14% in 2020E (from -0.4% in 2017), which coincides with 1.8x PBV representing valuation upsides from the current level.

Valuation

Our Bt14.2 target price is based on 1.8x 2020E PBV and 14% 2020E core ROE, discounted back to YE2019E at 10.5% Ke. We see PBV in relation to expected ROE as a suitable valuation method as: (i) profitability of dry-bulk industry is highly cyclical, (ii) PSL owns 100% of fleet ie. no chartered-in capacity, (iii) the PBV vs core ROE relationship builds in local and stock specific aspects such a scarcity of dry-bulk sector proxies.

We see 1.8x 2020E PBV as suitable in relation our 14% 2020E core-ROE based on historical PBV / core ROE trading relationship over the past three years. Higher est. core ROE justifies higher PBV multiples, in our view, *ceteris paribas*. Hence we believe PSL deserves to trade at a premium to current levels considering the expected increase in ROE from -0.4% in 2017 to ~14% in 2020E.

Year 2020E and IMO sulfur cap is our benchmark valuation as it is what market focuses on, in our view. Our 10.5% Ke used to discount PSL's fair-value back to YE2019 is based on 3% Rf, 8% Rp and 0.94x market Beta.

Risks

Key downside risks that could cause PSL shares to trade below our target price include: (1) dry-bulk industry supply tightening not coming through ie. limited enforcement from port / flag states or non-compliance by bulkers. Assume 2020E scrap rates remain at 1.5% of YE2019E fleet rather than 4.5% assumed, 2020E industry's demand / supply balance will likely flip to –ve 1.1% from +1.9% in our base case. Our sensitivity indicates that should BDI retreat to c1,300 PSL would deliver roughly a breakeven core-ROE coinciding with 1.1x PBV and translating to YE2019E fair-value of Bt8.4; (2) macro risks such as trade war or slowing China economic growth.

Safe Bulkers Inc

(SB.N; US$3.41; 3H; 10 Jul 18; 16:00)

Valuation

Our rounded $2.75 target is based on a modest discount to our NAV/share estimate. In the current dry bulk market trough, depressed vessel values and a levered balance sheet effectively marginalize most of the value in shares. However, the liquidity risk has been dampened following effective debt facility re-negotiations, which delay cash payments.

Risks

We rate Safe Bulkers High Risk due to the following economic cyclicality, competitive market, customer concentration, regulatory, operational and financial risk factors.

Economic cyclicality. The shipping industry is subject to cyclical factors, including economic conditions, customers' businesses conditions, credit markets, and seasonal patterns, which may adversely affect shipping volumes, freight demand, and charter demand.

Competitive market. Charter rates may be subject to significant competitive pricing pressures from other shipping providers.

Customer concentration. Loss of major customers may adversely affect operating results, since a significant portion of Safe Bulkers' revenue is derived from a relatively small number of charterers.

Highly regulated industry. The shipping industry is subject to various laws and regulations that govern industry-related and environmental activities. Changes or violations of these laws and regulations could adversely affect operations.

Operational and financial risks. Operating results may be adversely affected by operational risks, including damage, loss, or detainment and piracy, which may not be adequately covered by insurance. The availability of financing could limit or support new construction and adversely or positively affect the supply/demand balance and day rates.

Unstable global economy. Negative changes in global economic conditions, particularly in China, may reduce demand for and production of dry bulk products.

High Levels of Vessel Scrapping. In reaction to the chronic vessel oversupply that has depressed charter rates in the last several years, industry operators have proceeded to scrap older vessels at a higher rate than the historical average, to right size the global fleet. Should scrapping activity continue to progress at these levels, vessel charter rates could rebound faster than we anticipate, creating upside to our estimates.

Vessel Valuations Normalizing. Over the past few quarters, secondary market vessel values have started to recover, backed by strengthening underlying commodity demand and a moderated level of vessel oversupply. Should these trends continue, they would support higher NAV-based equity valuations and thereby could cause the shares to exceed our target price.

Appendix A-1

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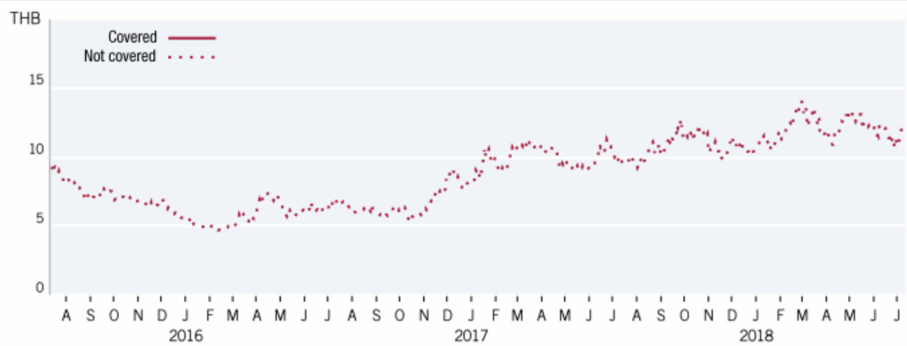
The research analysts primarily responsible for the preparation and content of this research report are either (i) designated by "AC" in the author block or (ii) listed in bold alongside content which is attributable to that analyst. If multiple AC analysts are designated in the author block, each analyst is certifying with respect to the entire research report other than (a) content attributable to another AC certifying analyst listed in bold alongside the content and (b) views expressed solely with respect to a specific issuer which are attributable to another AC certifying analyst identified in the price charts or rating history tables for that issuer shown below. Each of these analysts certify, with respect to the sections of the report for which they are responsible: (1) that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc. and its affiliates; and (2) no part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

Precious Shipping (PSL.BK)

Ratings and Target Price History
Fundamental Research



*Indicates Change

Rating/target price changes above reflect Eastern Time

Safe Bulkers Inc (SB)

Ratings and Target Price History
Fundamental Research

Analyst: Christian Wetherbee

	Date	Rating	Target Price	Closing Price
1	13-Oct-15 06:55:29	3H	*2.50	3.39
2	09-Nov-15 23:12:40	3H	*2.00	3.01
3	04-Jan-16 04:01:42	3H	*0.50	0.75
4	10-Feb-16 22:08:14	3H	*0.25	0.41
5	03-Jun-16 08:51:17	3H	*0.50	1.06
6	19-May-17 12:32:38	3H	*1.50	2.13
7	27-Jul-17 00:48:58	3H	*2.00	2.41
8	01-Nov-17 14:59:58	3H	*2.50	3.40
9	15-Feb-18 17:05:20	3H	*2.75	3.65

*Indicates Change

Rating/target price changes above reflect Eastern Time

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	12 Month Rating			*Catalyst Watch*		
Data current as of 30 Jun 2018	**Buy**	**Hold**	**Sell**	**Buy**	**Hold**	**Sell**
Citi Research Global Fundamental Coverage	53%	36%	11%	5%	93%	2%
% of companies in each rating category that are investment banking clients	65%	64%	55%	64%	64%	66%

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