

## Precious Shipping

### Key takeaways from management presentation at the SET Opportunity Day

Management is cautious on the near-term outlook but expects the industry supply growth to moderate. This supports our positive contrarian view—we expect the industry demand–supply growth balance to improve earlier than expected as the vessel orderbook is likely overstated. We assume coverage of PSL (OW, Jun-14 PT Bt22) – PSL provides a low-risk play on the sector recovery, given its cost-efficient fleet and strong balance sheet. PSL’s counter-cyclical strategy to acquire cheap vessels should provide a significant cost advantage over peers and substantial profit upside from future disposals.

- **Earnings outlook remains challenging this year...:** Opex fell 4% to \$4,318/day in 1Q13 vs 2012 full year but average TC rate fell more (-14%) to \$7,030/day. PSL’s Supramax earnings of \$9,023/day beat market rate by 12% while Handysize earnings of \$6,588/day underperformed by 4% in 1Q13.
- **... But will improve significantly from next year:** Industry supply growth is moderating, helped by continued vessel delivery slippage and scrapping. Mgmt expects sector supply growth to moderate from 10.2% to 5.08% this year and 1.05% in 2014E, assuming 30% slippage and 35m MT annual scrapping. Global ton-mile demand growth is expected to be higher in 2013-15 (+11% y/y pa) vs 2010-12 (+8% y/y), driven by rising US coal exports and China importing more raw materials from further locations (e.g. Americas rather than Australia).
- **Substantial earnings upside when rates recover:** Fixed only 22% of revenue days in 2013 (contract value \$35MM), 12% in 2014 (\$28MM) and 14% (\$35MM) per year from 2015 to 2017 which provide substantial upside when rates recover. Mgmt targets to achieve a 50% forward cover on a rolling 4 year basis when rates pick up. Signed contracts for 4 cement carriers with minimum 15 years (extendable to 20–25 yrs) time charter at \$15,000/day per ship.
- **Counter-cyclical strategy to acquire cheap and young vessels should provide a significant long-term cost advantage over peers:** Raised vessel fleet by 2 vessels q/q to 38 ships in 1Q13. PSL has bought 20 vessels so far and plans to purchase another 10-20 second-hand/newbuilding resale ships. Strategy for 2013-14 is to expand to a fleet of 60-65 ships while staying profitable.
- **Stronger balance sheet than peers:** Net debt-equity was 54%, up 5ppts due to vessel capex but still markedly below global sector average of 100%. Cash available at end 1Q13 after paying regular quarterly dividends was \$59MM.

## Overweight

PSL.BK, PSL TB

Price: Bt17.80

Price Target: Bt22.00

### Thailand Shipping

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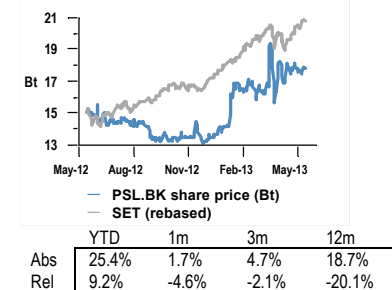
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### Price Performance



### Precious Shipping (Reuters: PSL.BK, Bloomberg: PSL TB)

Bt in mn, year-end Dec	FY11A	FY12A	FY13E	FY14E	FY15E
Revenue (Bt mn)	3,079	3,488	3,707	5,542	8,646
Net Profit (Bt mn)	719	141	322	828	2,459
EPS (Bt)	0.69	0.14	0.31	0.80	2.37
DPS (Bt)	0.55	0.40	0.08	0.20	1.18
Revenue Growth (%)	0.9%	11.5%	8.7%	34.8%	55.6%
EPS Growth (%)	-36.6%	-80.4%	128.2%	157.3%	197.0%
ROCE	5.5%	2.5%	3.6%	5.5%	10.7%
ROE	4.8%	0.9%	2.2%	5.5%	15.4%
P/E	25.8	131.2	57.5	22.3	7.5
P/BV	1.2	1.3	1.3	1.2	1.1
EV/EBITDA	11.7	17.2	14.2	10.5	6.3
Div Yield (%)	3.1%	2.2%	0.4%	1.1%	6.6%

Source: Company data, Bloomberg, J.P. Morgan estimates.

Company Data	
Shares O/S (mn)	1,040
Market Cap (Bt mn)	18,503
Market Cap (\$ mn)	623
Price (Bt)	17.80
Date Of Price	13 May 13
Free float (%)	40.0%
Avg daily volume (mn)	0.17
Avg daily value (Bt mn)	33.69
Avg daily value (\$ mn)	1.14
SET	1,618
Exchange Rate	30
Fiscal Year End	Dec

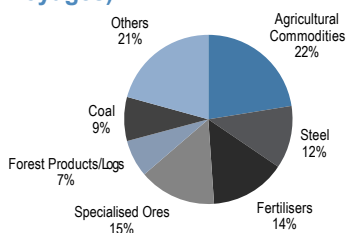
### See page 12 for analyst certification and important disclosures, including non-US analyst disclosures.

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## Company Description

- Core businesses are dry bulk shipping mainly in the Handysize vessel segment with c.1.0% global Handysize market share in capacity terms.
- Positive drivers:** rebound in dry bulk shipping volumes and freight rates, vessel delivery deferrals, locked-in long term time charters, Handysize segment faces less industry oversupply than the larger vessel segments, stable management team, stronger balance sheet versus peers, limited asset impairment risks.
- Negative drivers:** longer than expected industry overcapacity, weaker-than-expected global dry bulk shipping demand, counter-party risks, political risks.

## 2012 Commodities Carried Breakdown (Based on number of voyages)



Source: Company data.

## EPS: J.P. Morgan vs. Consensus

Bt	J. P. Morgan	Consensus
FY13E	0.31	0.40
FY14E	0.80	0.95
FY15E	2.37	1.34

Source: Bloomberg, J.P. Morgan estimates

## Peer Group Valuation Comparison Table

Company Name	Rec	Stock Code	Price 13-May-13 (LC)	P/E		P/BV (x)		ROE	
				2013E (X)	2014E (X)	2013E (X)	2014E (X)	2013E (X)	2014E (X)
China Cosco	OW	1919 HK	3.45	nm	13.3	1.2	1.1	-7.7	8.4
Pacific Basin Shipping	OW	2343 HK	4.39	33.1	8.0	0.8	0.8	2.7	11.0
Precious Shipping	OW	PSL TB	17.80	57.5	22.3	1.3	1.2	2.2	5.5
				<b>27.6</b>	<b>14.4</b>	<b>0.8</b>	<b>0.7</b>	<b>1.0</b>	<b>5.0</b>

Source: Bloomberg, annual reports, J.P. Morgan estimates.

## P&L Sensitivity Metrics

	EBIT impact (%)	EPS impact (%)
2013E		
Average TC rate (US\$/day)	7,399	7,399
Impact of each 5% change	+10%	+21%
Revenue days	16,702	16,702
Impact of each 5% change	+7%	+16%

Source: J.P. Morgan estimates. \*Large earnings sensitivity due to small profit base at the bottom of the cycle.

## Price Target & Valuation Analysis

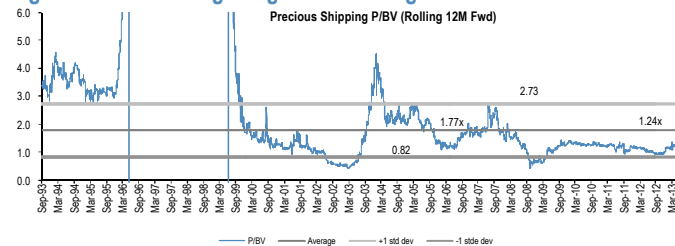
Our Jun-14 price target of Bt22 is based on 1.5x P/BV, a 15% discount to Precious Shipping's historical average valuation since listing as the near term industry outlook remains challenging. However, we expect the sector demand-supply growth to improve which will drive significant earnings recovery from 2014E.

## PB Table

Average	1.8
+1 Standard Deviation	2.7
-1 Standard Deviation	0.8

Source: Company reports, Bloomberg, J.P. Morgan estimates.

Figure 1: P/BV Trading Range Since Listing



Source: Company data, Bloomberg, J.P. Morgan estimates.

**Key downside risks:** 1) weaker than expected global dry bulk shipping demand, 2) prolonged industry oversupply, 3) counterparty risks, 4) political risks.

## Investment summary

We have a positive contrarian view on the dry bulk shipping sector. We expect the industry demand–supply growth balance to improve earlier than expected as the vessel orderbook is likely overstated and accelerated scrapping is helping to mitigate the industry oversupply.

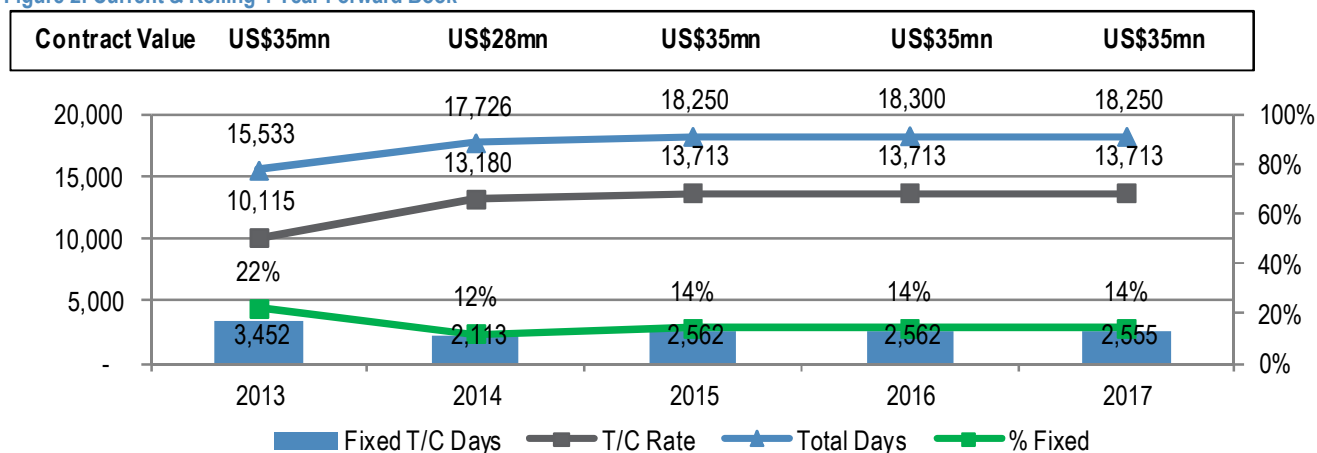
We assume coverage of PSL (OW, Jun-14 PT Bt22) – Precious Shipping provides a low-risk play on the sector recovery, given its cost-efficient fleet and strong balance sheet. PSL’s counter-cyclical strategy to acquire cheap vessels should provide a significant cost advantage over peers and substantial profit upside from future disposals.

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**Key positive drivers:** rebound in dry bulk shipping volumes and freight rates, vessel delivery deferrals, locked-in long term time charters, Handysize segment faces less industry oversupply than the larger vessel segments, stable management team, stronger balance sheet versus peers, limited asset impairment risks.

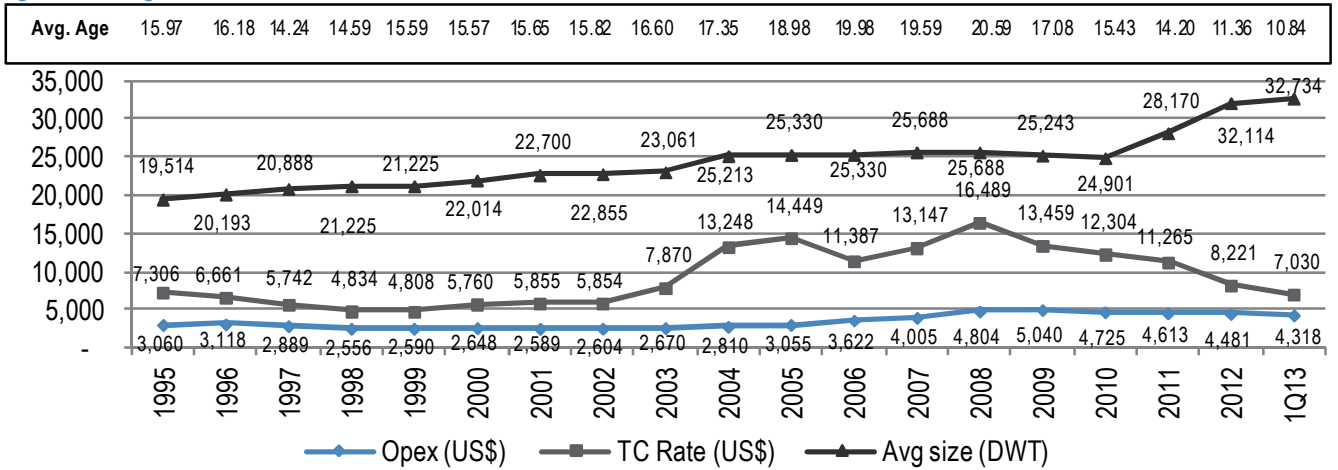
**Key risks:** longer than expected industry overcapacity, weaker-than-expected global dry bulk shipping demand, counter-party risks, political risks.

Figure 2: Current & Rolling 4 Year Forward Book



Source: Company reports. As at 1st April, 2013.

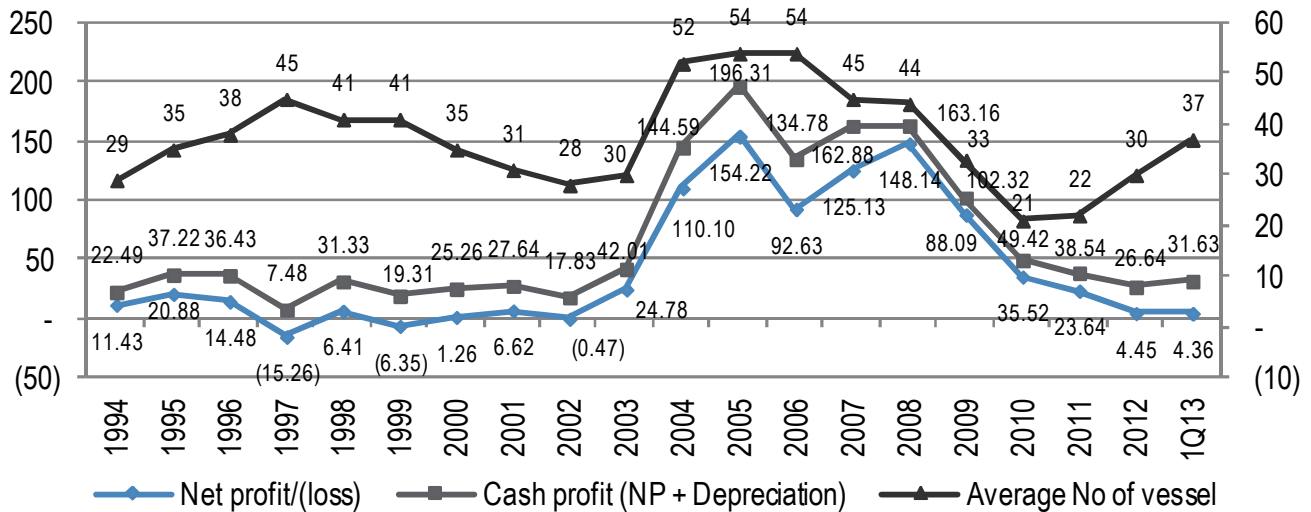
Figure 3: Average OPEX/TC Rates



Source: Company reports.

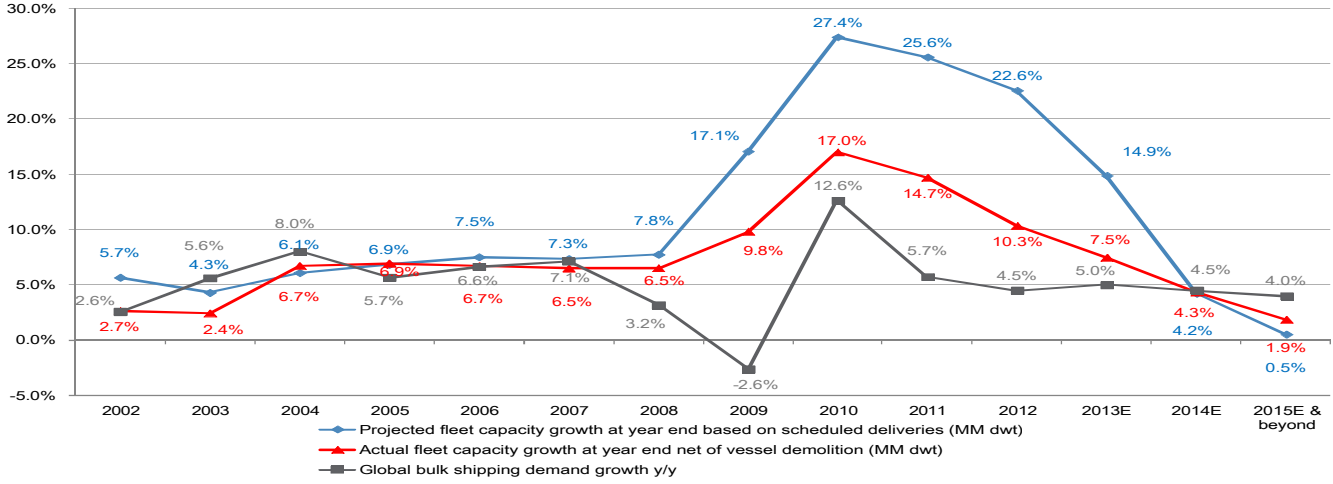
Figure 4: Net Profit/Cash Profit

US\$ in mn



Source: Company reports.

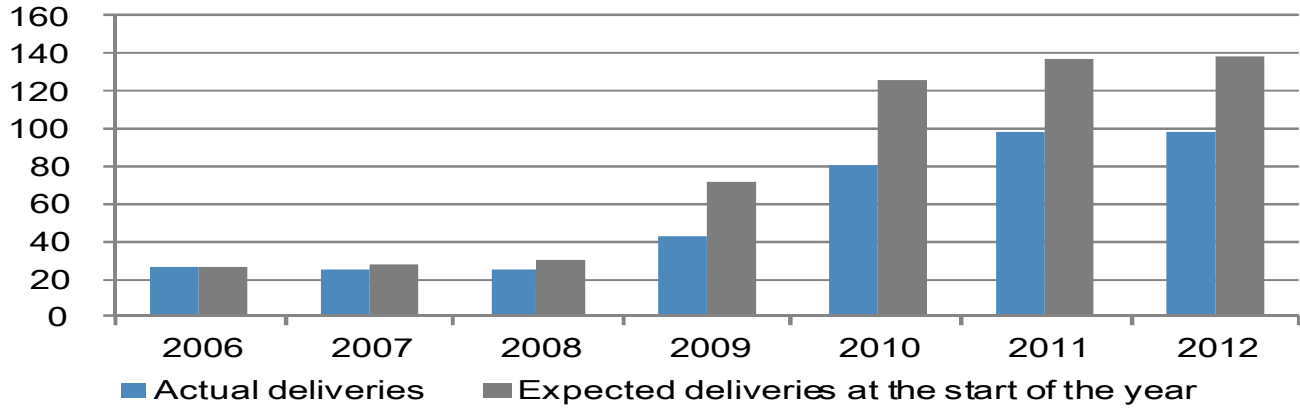
Figure 5: Dry Bulk Sector Demand & Supply Projection



Source: J.P. Morgan estimates, Clarksons (for historical data). Assumes: 1) actual vessel deliveries are 25% below scheduled in 2013E, 35% higher than scheduled in 2014E and 250% in 2015E & beyond, 2) 3.7% vessel scrapping in 2013E, 1.4% in 2014E and no scrapping in 2015 & beyond.

Figure 6: Newbuild Dry Bulk Vessel Deliveries (Actual vs Expected)

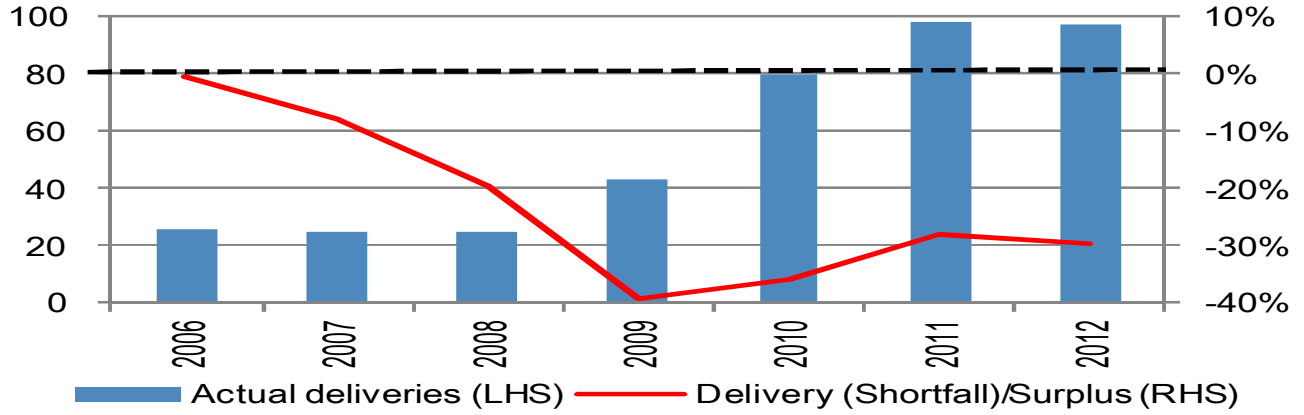
mn DWT



Source: Clarksons.

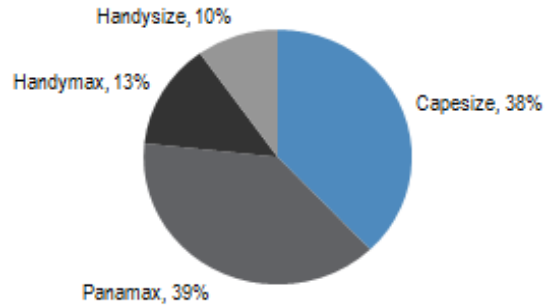
Figure 7: Historical Newbuild Bulkcarrier Delivery Slippages

mn DWT



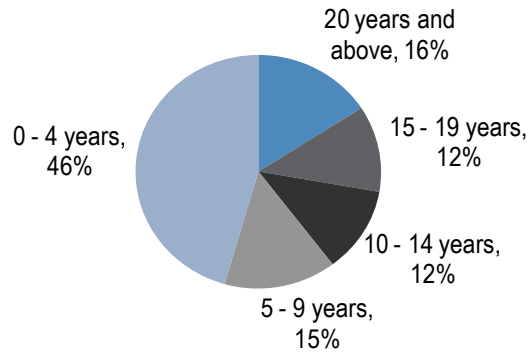
Source: Clarksons.

Figure 8: Distribution Of Orderbook By Vessel Type (in terms of capacity in million dwt)



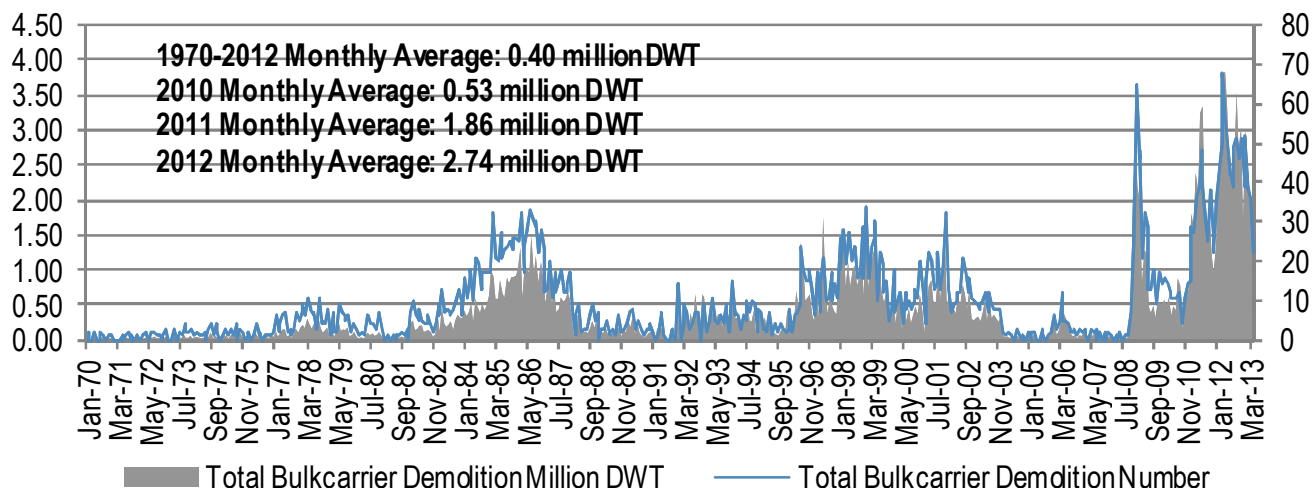
Source: Clarksons. Note: data as of 1st May 2013.

Figure 9: Age profile Of Current Dry Bulk Fleet



Source: Clarksons. Note: data as of 1st May 2013.

Figure 10: Substantial Vessel Demolition



Source: Clarksons.

## Financial analysis

We expect Precious Shipping's near term earnings outlook to remain challenging due to the current low freight rate environment and expect it to achieve a marginal net profit of Bt322MM in 2013.

However, PSL's earnings will improve significantly as the industry demand-supply growth balance improves and drives freight rate recovery. We expect a 157% y/y improvement in net profit to Bt828MM in 2014E, and tripling to Bt2.5B in 2015E, based on average TC rates returning to 2011 levels (which are still 10% below the historical average in the past 5 years).

This is driven by a 32% revenue growth per annum, driven by increased revenue days (+23% pa) and a 12% improvement in average freight rates. Vessel running costs are expected to grow c.17% pa based on our estimates.

We expect PSL's ROE to improve from 2% in 2013E to 15% by 2015E. Net debt-equity is expected to rise to 80% by 2015E as Precious Shipping targets to build up a fleet of cheap and young vessels to leverage on the industry up-cycle.

Due to PSL's strategy to expand its fleet to leverage on the upturn, we expect PSL to be free cashflow negative in 2013 and 2014 and start generating positive free cash flow of Bt536MM from 2015.

We have conservatively assumed a 25% dividend payout ratio in 2013-14 and (which is PSL's minimum payout) 50% in 2015 although its historical payout has averaged 80%.

**Table 1: Precious Shipping Management Summary**

Name	Designation	Profile
Khalid Hashim	Managing Director	Khalid Hashim, Managing Director of Precious Shipping, comes from a long family line of professionals engaged in the Dry Cargo Tramp Freight Markets. Khalid started his Shipping career with Tolani Shipping, Bombay. He then worked under the Hon. Ali Maniku, Minister of Shipping for the Maldives Government in Singapore. In 1984, Khalid joined the GP Group of companies setting up their Shipping division in Bangkok, and soon acquired the first of many ships in 1987. Precious Shipping was born soon after and came of age in 1991. Asia Money, in their December 2008, December 2009 and December 2010 issues conferred the Best Executive, Thailand and best Investor Relations Officer, Thailand titles on Khalid. In April 2012, Seatrade Asia awarded the 'Lifetime Achievement Award' to Khalid. In 1996 Khalid was elected to the Board of the Swedish Club, a 140 year old Marine Mutual Insurance company; Chairman of the Finance and Audit Committee in 1997, and was elected Deputy Chairman in 2007. Khalid holds a Masters Degree in Management Studies specializing in Finance from the University of Bombay.
Munir Hashim	Director - Commercial	Munir Hashim has a Master's Degree in Management Studies specializing in Marketing, University of Bombay. He is the Director (Commercial) and has more than 20 years of experience in the shipping sector.
Khushroo Kali Wadia	Director - Finance	Khushroo Wadia has a Bachelor's Degree in Science, University of Bombay and Chartered Accountant, Institute of Chartered Accountants of India. He is the Director (Finance) and has 25 years of experience in the finance role.
Jaipal Mansukhani	Director	Jaipal Mansukhani has done a Directorate of Marine Engineering Training and is the Director with more than 30 years of experience in the shipping sector.

Source: Company reports.



## SWOT analysis

<p><b>Strengths</b></p> <ul style="list-style-type: none"> <li>• <b>Exposure to the smaller vessel segments which face lower overcapacity risks:</b> Precious Shipping operates in the smaller Handysize and Supramax vessel segments where oversupply risks are lower.</li> <li>• <b>Counter-cyclical strategy to acquire cheap and young vessels should provide a significant long-term cost advantage over peers:</b> Raised vessel fleet by 2 vessels q/q to 38 ships in 1Q13. PSL has bought 20 vessels so far and plans to purchase another 10-20 second-hand/newbuilding resale ships. Strategy for 2013-14 is to expand to a fleet of 60-65 ships while staying profitable.</li> <li>• <b>Resilient balance sheet:</b> Net debt-equity was 54%, up 5ppts due to vessel capex but still markedly below global sector average of 100%. Cash available at end 1Q13 after paying regular quarterly dividends was \$59MM.</li> <li>• <b>Strong and stable management team:</b> Precious Shipping has a strong management team with extensive industry experience and a good track record of timing the sale &amp; purchase of vessels.</li> </ul>	<p><b>Weaknesses</b></p> <ul style="list-style-type: none"> <li>• <b>Weak earnings outlook near term as freight rates are at historical low levels:</b> Precious Shipping will likely be marginally profitable in 2013E as freight rates are at historical low levels due to the industry oversupply.</li> <li>• <b>Rising capex and financial leverage as fleet expands:</b> Precious Shipping will likely report negative free cash flow as it expands its shipping fleet.</li> <li>• <b>Political risks:</b> Political risks in Thailand and currency volatility could potentially impact share price performance.</li> </ul>
<p><b>Opportunities</b></p> <ul style="list-style-type: none"> <li>• <b>Moderating industry oversupply:</b> We expect improving demand-supply growth balance from mid-2013.</li> <li>• <b>Rebound in dry bulk volumes:</b> Global ton-mile demand growth is expected to rise, driven by rising US coal exports and China importing more raw materials from further locations (e.g. Americas rather than Australia).</li> <li>• <b>Substantial earnings upside when rates recover:</b> Fixed only 22% of revenue days in 2013 (contract value \$35MM), 12% in 2014 (\$28MM) and 14% (\$35MM) per year from 2015 to 2017 which provide substantial upside when rates recover. Mgmt targets to achieve a 50% forward cover on a rolling 4 year basis when rates pick up.</li> </ul>	<p><b>Threats</b></p> <ul style="list-style-type: none"> <li>• <b>Industry oversupply</b> – If industry oversupply prolongs longer than expected, it may hamper the freight rate recovery momentum.</li> <li>• <b>More new entrants</b> – Some cargo owners are growing their own fleet. Dry bulk shipping has relatively lower barriers to entry than other shipping segments and may attract speculative investors if financing becomes more easily available again.</li> <li>• <b>Ability to access cheap financing</b> – If Precious Shipping is not able to access competitive financing terms, it will limit its fleet expansion plans and/or raise financing costs.</li> </ul>

## Precious Shipping: Summary of Financials

Income Statement						Cash flow statement					
Bt in millions, year end Dec	FY11	FY12	FY13E	FY14E	FY15E	Bt in millions, year end Dec	FY11	FY12	FY13E	FY14E	FY15E
Revenues	3,079	3,488	3,707	5,542	8,646	EBIT	1,158	584	899	1,587	3,417
% change Y/Y	0.9%	11.5%	8.7%	34.8%	55.6%	Depr. & amortization	647	910	1,121	1,376	1,614
EBITDA	1,804	1,494	2,019	2,963	5,031	Change in working capital	-185	-320	-28	-124	-267
% change Y/Y	-17.4%	-17.2%	35.2%	46.7%	69.8%	Taxes	-4	-4	-7	-17	-51
EBIT	1,158	584	899	1,587	3,417	Cash flow from operations	1,051	751	1,955	2,772	4,659
% change Y/Y	NM	NM	54.0%	76.5%	115.3%	Capex	-2,301	-4,556	-4,312	-4,312	-3,312
EBIT Margin	33.7%	15.3%	21.6%	28.3%	39.1%	Disposal/(purchase)	2,169	1,729	0	0	0
Net Interest	-441	-434	-569	-731	-866	Net Interest	-441	-434	-569	-731	-866
Earnings before tax	724	148	334	861	2,556	Free cash flow	-1,251	-3,805	-2,356	-1,539	1,348
% change Y/Y	-40.9%	-79.6%	126.3%	157.3%	197.0%	Equity raised/(repaid)	-	-	-	-	-
Tax	-4	-4	-7	-17	-51	Debt raised/(repaid)	-2,456	-2,748	0	0	0
as % of EBT	0.5%	2.8%	2.0%	2.0%	2.0%	Other	4,251	4,680	80	207	1,229
Net income (reported)	719	141	322	828	2,459	Dividends paid	-644	-502	-80	-207	-1,229
% change Y/Y	-36.6%	-80.4%	128.2%	157.3%	197.0%	Beginning cash	-	-	-	-	-
Shares outstanding	1,040	1,040	1,040	1,040	1,040	Ending cash	4,375	1,901	1,924	2,496	3,802
EPS (reported)	0.69	0.14	0.31	0.80	2.37	DPS	0.55	0.40	0.08	0.20	1.18
% change Y/Y	(36.6%)	(80.4%)	128.2%	157.3%	197.0%						
Balance sheet						Ratio Analysis					
Bt in millions, year end Dec	FY11	FY12	FY13E	FY14E	FY15E	Bt in millions, year end Dec	FY11	FY12	FY13E	FY14E	FY15E
Cash and cash equivalents	4,375	1,901	1,924	2,496	3,802	EBITDA margin	52.5%	39.0%	48.5%	52.8%	57.6%
Accounts receivable	125	217	236	318	494	Operating margin	33.7%	15.3%	21.6%	28.3%	39.1%
Inventories	69	147	159	215	335	Net margin	20.9%	3.7%	7.7%	14.8%	28.2%
Others	1,453	677	677	677	677	Sales per share growth	0.9%	11.5%	8.7%	34.8%	55.6%
Current assets	6,022	2,941	2,996	3,705	5,308	Sales growth	0.9%	11.5%	8.7%	34.8%	55.6%
LT investments	120	113	118	123	128	Net profit growth	-36.6%	-80.4%	128.2%	157.3%	197.0%
Net fixed assets	9,446	16,213	19,404	22,339	24,036	EPS growth	(36.6%)	(80.4%)	128.2%	157.3%	197.0%
Total Assets	22,893	24,030	27,280	30,930	34,235	Interest coverage (x)	4.09	3.45	3.55	4.05	5.81
Liabilities						Net debt to equity	17.3%	49.5%	68.9%	81.9%	80.0%
Short-term loans	719	802	802	802	802	Sales/assets	0.16	0.16	0.16	0.19	0.27
Payables	33	2	2	3	4	Assets/equity	1.19	1.66	1.85	2.02	2.07
Others	296	316	319	332	360	ROE	4.8%	0.9%	2.2%	5.5%	15.4%
Total current liabilities	1,047	1,119	1,123	1,136	1,166	ROCE	5.5%	2.5%	3.6%	5.5%	10.7%
Long-term debt	6,308	8,265	11,265	14,265	16,265						
Other liabilities	182	161	161	161	161						
Total Liabilities	7,537	9,545	12,549	15,562	17,592						
Shareholders' equity	15,323	14,483	14,724	15,345	16,575						
BVPS	14.74	13.93	14.16	14.76	15.94						

Source: Company reports and J.P. Morgan estimates.

**JPM Q-Profile**

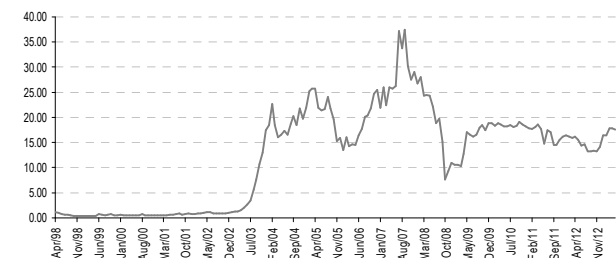
**Precious Shipping PCL (THAILAND / Industrials)**

As Of: 10-May-2013

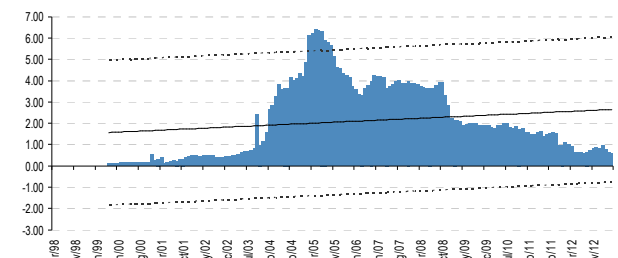
**Global Equity Quantitative Analysis**

Quant\_Strategy@jpmorgan.com

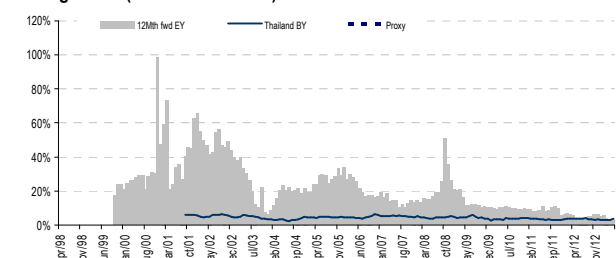
**Local Share Price** Current: 17.60



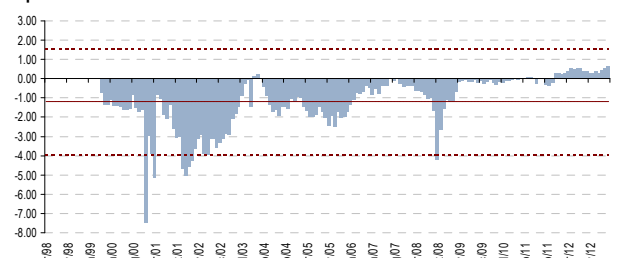
**12 Mth Forward EPS** Current: 0.59



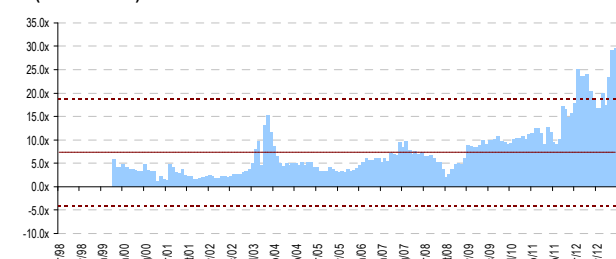
**Earnings Yield (& local bond Yield)** Current: 3%



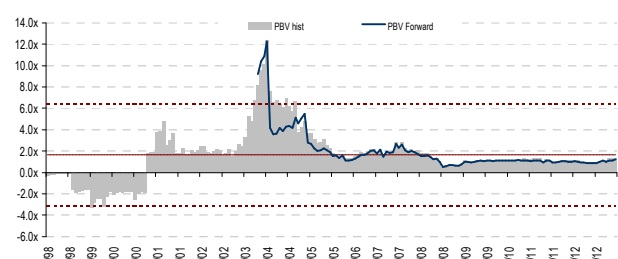
**Implied Value Of Growth\*** Current: 61.88%



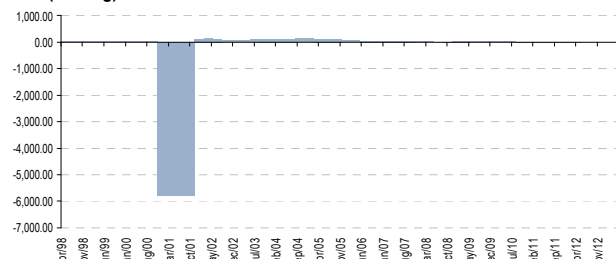
**PE (1Yr Forward)** Current: 29.7x



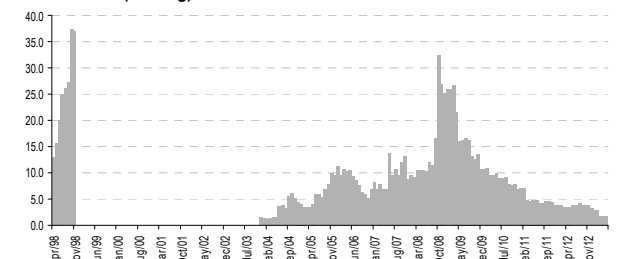
**Price/Book Value** Current: 1.3x



**ROE (Trailing)** Current: 3.18



**Dividend Yield (Trailing)** Current: 1.69



**Summary**

Precious Shipping PCL		SEDOL		6694526		As Of:		10-May-13			
THAILAND						Local Price:		17.60			
Industrials						EPS:		0.59			
	Latest	Min	Max	Median	Average	2 S.D.+	2 S.D. -	% to Min	% to Max	% to Med	% to Avg
12mth Forward PE	29.68x	1.01	29.68	5.24	7.40	18.78	-3.97	-97%	0%	-82%	-75%
P/BV (Trailing)	1.29x	-3.32	12.38	1.35	1.65	6.41	-3.12	-357%	856%	4%	27%
Dividend Yield (Trailing)	1.69	0.00	37.50	4.06	6.32	21.45	-8.81	-100%	2125%	141%	275%
ROE (Trailing)	3.18	-5799.91	178.88	18.31	-338.95	2572.24	-3250.14	-182575%	5528%	476%	-10764%
Implied Value of Growth	61.9%	-7.49	0.62	-0.90	-1.18	1.57	-3.93	-1310%	0%	-246%	-291%

Source: Bloomberg, Reuters Global Fundamentals, IBES CONSENSUS, J.P. Morgan Calcs

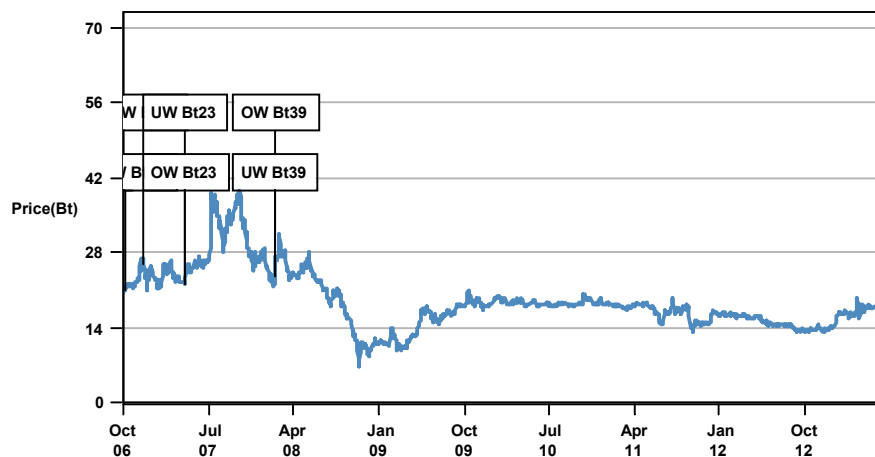
\* Implied Value Of Growth = (1 - EY/Cost of equity) where cost of equity = Bond Yield + 5.0% (ERP)

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Precious Shipping (PSL.BK, PSL TB) Price Chart



Date	Rating	Share Price (Bt)	Price Target (Bt)
05-Oct-06	OW	21.00	50.00
07-Dec-06	OW	26.00	59.00
16-Apr-07	OW	22.40	23.00
19-Apr-07	UW	22.20	23.00
30-Jan-08	UW	23.60	39.00
31-Jan-08	OW	23.60	39.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Oct 05, 2006.

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