

Ref.: 2017-012

28 April 2017

**To : The President of the Stock Exchange of Thailand**

**Subject : The 1<sup>st</sup> Quarter of 2017 Management Discussion and Analysis (MD&A)**

### **Our Key Performance Indicators:**

**The results**, reviewed by EY Office Ltd., show you the latest financial position of the Company. The net loss for Q1 2017 was USD 1.70 million. The earnings per day per ship during Q1 came in at USD 8,588, 79% higher than that in Q1 2016. Please take a look at the Market Segmentation report that shows you the performance of the PSL fleet's earnings per day per ship compared to the Index ships. In this quarter, daily operating costs were USD 4,208 which is lower than our target of USD 4,500 and lower than the actual for the previous year. The EBITDA was USD 11.26 million during Q1. The loss per share (eps) in Thai Baht stood at Baht 0.04 for this quarter.

<b>THE HARD FACTS</b>	<b>Q1, 2017</b>	<b>Q1, 2016</b>
Highest Earnings per day per ship in USD	15,000	15,000
Average Earnings per day per ship in USD	8,588	4,797
Operating cost per day per ship in USD	4,208	4,528
EBITDA in million USD	11.26	(1.51)
Net Profit/(Loss) in million USD (excluding Exchange gain (loss) and Non-recurring items)	(1.74)	(16.62)
Net Profit/(Loss) in million USD	(1.70)	(34.04)
Earnings(Loss) Per Share in Thai Baht (excluding Exchange gain (loss) and Non-recurring items)	(0.04)	(0.38)
Earnings (Loss) Per Share in Thai Baht	(0.04)	(0.78)

**Awards and Accolades: PSL won the Public Debt Deal of the Year for 2016** from Marine Money! It was truly amazing that in Q1 2016, when the BDI hit an absolute all time low of just 290 points on 10<sup>th</sup> February, we were able to get USD 100m from the Public Debt markets at such a low cost and at a time when shipping companies were defaulting and closing down all over the world. This award is testimony to the reputation, character, resilience and strength of PSL and its very hard working and dedicated staff! Attached is a copy of the awards article.

**The Fleet Rejuvenation Plan** is almost complete with 36 ships in the water (including 1 X 64K Ultra delivered by Sanfu Shipyard on 18<sup>th</sup> April 2017). We have sold 1 older ship which was delivered to her buyers on 24<sup>th</sup> April 2017, and that completes our disposal program. Another 1 X 64K brand new Ultra is due to be delivered in early 2018 which will complete the existing newbuilding program with Sanfu Shipyard.

**Market Segmentation:** During Q1, the Baltic Handy Size Index (BHSI) averaged 456 points derived from the average Time Charter (TC) rate of USD 6,636. Compared to that, our Handies earned USD 9,316 and beat the BHSI TC rate by 40.39%. During Q1, the Baltic Supramax Index (BSI) averaged 781 points derived from the average Time Charter (TC) rate of USD 8,171. Compared to that, our Supramaxes earned USD 6,701 and underperformed from the BSI TC rate by 17.99%. Our target is to outperform both the indexes.

**The SET Opportunity Day** where PSL will be presenting will be held at the SET building at 15:20 hours on Wednesday the 17<sup>th</sup> May 2017. We hope that many of you will attend this event where the Company will get a chance to thoroughly discuss the Q1 results. For those of you who cannot attend physically, the SET [live web casts](#) the presentation giving you a chance to be present via the web.

**Ship Scrapping** has been very disappointing with just 4.99 MDWT of ships being scrapped during Q1 2017 across all sectors in the dry bulk market as compared to 14.09 MDWT in Q1 last year. The existing age profile of the world fleet together with Regulatory pressures (BWM and Clean oil) should result in the world dry bulk fleet growing at a slower pace which will help redress the imbalance between supply and demand.

**Long Term versus short term Charters:** The long term charters already booked as of 31<sup>st</sup> March are shown in the chart below. As can be seen, our current and forward four year rolling book is currently at the 16.8% level with a visible revenue stream of USD 157.3 million.

Year	2017	2018	2019	2020	2021
<b>Total Available Days</b>	13,147	13,496	13,505	13,542	13,505
<b>Fixed T/C Days</b>	2,555	2,240	2,190	2,196	2,190
<b>%age Fixed T/C Days</b>	19%	17%	16%	16%	16%
<b>Av. T/C Rate/Day in USD</b>	13,713	13,849	13,875	13,875	13,875
<b>Contract value in million USD</b>	35.0	31.0	30.4	30.5	30.4

It is our intention to continue to charter out our ships on long term period contracts whenever practical and economically viable.

## **Our Read of the market:**

### **An explanation on why 2016 ended up much stronger than it started out:**

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- Forecast for 2016 was for Chinese Steel exports to be flat or drop by 2 to 3%.
- Chinese Steel exports in 2016 dropped to 108.46 MMT from 112.4 MMT in 2015.
- Forecast for Chinese Coal imports in 2016 to drop by 10% from 204 MMT to 180 MMT.
- Chinese Coal imports in 2016 actually rose 25.2% y-o-y to 255.51 MMT in 2016.
- Forecast for 2016 was for Chinese Iron Ore imports to be flat or up by max 2 to 3%.
- China imported 1,024.71 MMT of iron ore in 2016, up 7.5%: that's about 32.5 MT a second right through 2016!

### **Reasons behind China's strong Coal imports:**

- Smaller, inefficient mines in China produce poor quality coal resulting in pollution leading to protests.
- Smaller mines are unsafe and result in miners dying followed by protests.
- Chinese Government is very sensitive to protests.
- China has ordered the closure of up to 800 MMT of mining capacity by 2020 to avoid these unnecessary deaths, pollution and protests.
- About 290 MMT of mining capacity was shutdown in 2016.
- April 2016, Coal mines were told to work max 276 from normal 330 days.
- Due to closures and restricted work days imports started rising in SH'16.
- Coal prices rose from USD50 in April to about USD 115 by November, so policy was reversed back to 330 working days for Coal mines.
- Unintended consequence was that Coal mines, at their new reduced output, became profitable and were reluctant to increase production and consequently reduce prices and profitability.
- As a result Coal imports into China in the first two months of this year are 48% above the y-o-y figures from 2016.
- Policy on working days stays at 330 days and has not been reversed.
- Government has ordered closure of 150 MMT of mining capacity in 2017.

### **The million dollar question: Is China's import performance sustainable?**

The following factors make the case for sustainability:

**China wants to stop producing 'product' or normal Steel** by June this year and produce only high quality Steel. To do that you will need high grade iron ore and high grade coke, both available from imports.

**China has just slapped a ban on imports of Coal from North Korea.** This was about 23 MMT during 2016 with very low ton-mile impact. This will now have to be imported from much further away adding to the ton-mile demand side of the equation.

**Data points on:**

- Iron Ore imports in the first quarter of this year up 12.2% (to 271.1 MMT).
- Coal imports in the first quarter of this year up 33.4% (to 64.7 MMT).
- Steel production in the first quarter of this year up 4.5% (to 200.4 MMT).
- Steel inventories in the first quarter of this year up 4.42 MMT.
- Steel exports in the first quarter of this year down 25.5% (to 20.7 MMT).
- China has been consuming more Steel in first quarter of this year up 9.5% (to 184 MMT) likely due to their development of the One Belt, One Road project.

Then there is the potential effect of US President **Trump's proposed policy.**

- USD 1 Trillion infrastructure spending requires huge imports of Steel, Cement and Wood.
- Mexican border wall/Fence fall out is a possible ban of US Corn imports of 34 MMT, will be sourced from Brazil and Argentina, very ton-mile intensive!
- Reduction in taxes and increase in spending will result in fiscal budget deficit and increase in interest rates leading to:
  - Zombie companies being shutdown and allowing healthy companies to prosper
  - Savers and Pensioners to restart spending.

Now **look at the supply side.** Last year the dry bulk fleet grew by 18.51m DWT. In the first quarter of this year the dry bulk fleet has grown by 12.29 MDWT. Still the BDI has continued to go up! This can only mean that trade flows have increased more than the supply side or, conversely, that balance between supply and demand is not that far off. Further, the Ballast water management convention and the 'clean' oil convention should combine to put a massive dent in the supply side between the years 2018 and 2020 inclusive. **If scrapping isn't strong enough in 2018/2019 then we would be dependent solely on the demand side to create a sustainable market.**

**Key Supply Side Developments:**

**Supply Side developments** in the world bulker fleet makes for interesting reading. We started 2017 with 790.41 MDWT and have increased to 802.7 MDWT during Q1 2017. A further 4.23% (33.96 MDWT) is scheduled for delivery in the rest of 2017. If we were to apply a slippage factor of 50% (it was actually 47.5% in 2016) to these scheduled deliveries and further assume that scrapping reaches 22 MDWT (based on Howe Robinson Partners research) we would be left with a fleet growth of **+1.55%** (802.67 MDWT) in 2017. Due to the regulatory pressures from the Ballast Water Management Convention coming into force from 8th September 2017, we think that scrapping could increase significantly in 2018 to around 35/40 MDWT. If we were to apply a slippage factor of 50% and scrapping of 37.5 MDWT then we would get a negative fleet growth of **-2.23%** and a year ending fleet of 784.76 MDWT in 2018.

**Bulk carrier prices** have followed the BDI and increased significantly over the quarter. The Chinese built Kamsarmax resale M/V "BSI LENNOX" (81,600 DWT/Delivery 3/2017 from Hudong-Zhonghua SB in China) has reportedly been sold for \$26m to TMS (George Economou

Group) in Greece. The seller, investment group Berkeley Shipping of Malta, sold their sister vessel M/V "BSI CARDOGAN" (82,277 DWT/Built 1/2017) in December for \$19.5-20m. (Compass Maritime)

Eastern Pacific Shipping purchased the M/V "MOUNT MERU" (179,147 DWT/Built 2009 at Hyundai in Korea) in November 2016 from the Hanjin Shipping creditor Korean Development Bank for about \$18.75m and has reportedly flipped the vessel to the investor group Songa Bulk of Norway for just below \$28m! (Compass Maritime)

As late as February 2017 a **five year old** Cape was at a 23% discount to the “**replacement cost**” (newbuilding prices has been quoted about flat at USD42m since June last year), but through March, Clarkson has upped the quote for a 5 year old from USD25m to USD32.5m and now 1 year TC rates for Capes are quoted at USD17,000/day, up 184% from USD6,000/day one year ago. We believe this is only a first step in the expected recovery. The magic in vessel prices happened when TC rates passed USD13-14k/day which is the cash-break-even level using a resale price of USD38m (which was the average in February) and 50-60% leverage (15 year tenor) at 3-4% all-in interest cost. With the discount from secondhand to newbuilding prices now taken away, we need to prepare for newbuilding orders. However, and importantly, we do not expect any meaningful amount of new orders to be concluded on current quotes for newbuilding prices as these quotes have been standing still in a period of which yard costs have been increasing, steel in particular (but wage inflation in China is also in positive territory). For steel we find a 50% increase from June 2016 to now, a period of which newbuilding prices for a Cape has been stable at USD42. Concretely, the cost has increased by about USD4m without any compensation in selling prices and when interest in newbuilding orders now increases, we expect yards to quickly adjust prices as we find it unlikely that they are capable to make a profit on these levels. (DNB Markets)

Opinions vary on **scrapping forecasts** for this year as a decision to demolish a vessel is often linked to freight market levels, thus HRP’s forecast for 2017 is 12 MDWT as a low case and 26 MDWT as a high case leaving a medium figure of 19 MDWT. It does seem likely that if current freight market levels are maintained scrapping may be much closer to the 2014 level of 17 MDWT. (Howe Robinson Research)

**Chinese yards** have seen a sharp drop in new bulker orders, from 579 units in 2013, to just 25 units in 2016. Japanese yards have also seen their dry bulk orders fall from a sustained level of at least 250 new orders each year in 2013-2015, to just 9 orders in 2016. Shipyards are likely to remain under pressure this year, as they face much fewer new orders, low newbuilding prices, and higher material costs. However, if shipowners continue to exercise restraint from excessive newbuilding orders, the shipping market may finally be able to move towards rebalancing from its current vessel oversupply. (Banchemo Costa)

### **Regulatory Pressures:**

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The ratification of the **Ballast Water Management Convention (BWMC)** has significant implications for the shipping industry. **Compliant technology can be costly and older ships**

**are likely to be recycled**, especially given the current weak earnings environment. Even with increased demolition, thousands of existing ships are still estimated to require BWMSs and meeting this requirement will be challenging. Whether there is sufficient docking and engineering capacity is another concern, and the potential for installation ‘bottlenecks’ appears to be high. (Clarksons)

**PSL’s Compliance with the BWMC:** Our existing fleet has 14 ships that are already fitted with Ballast Water Management Systems (BWMS). Of the balance 22 ships, 18 of them will require BWMS to be fitted at their next Special Survey during 2022. However 4 ships will fit BWMS when they complete their respective Special Surveys during 2018. In anticipation of these regulatory hurdles, between Jun’15 and Apr’17, we have recycled 15 older/smaller ships and sold two older/smaller ships for further trading to others.

**Clean Oil from 1<sup>st</sup> January 2020.** We continue to believe that despite economics pointing towards scrubbers as the best solution, it is still highly likely that the median vessel in 2020 is a vessel without a scrubber which then needs to use a low-sulphur-fuel-oil priced at (at least, we would say) 2 times that of high-sulphur-fuel-oil. This, not only implies a significant cost saving for vessels equipped with scrubbers, but also **a ~10-15% speed reduction for the median vessel using expensive fuel which will reduce overall transportation supply**. Such a supply reduction should have a disproportionate opposite rate impact. (DNB Markets)

According to a Wood Mackenzie study, **global bunker fuel costs could rise** by up to \$60bn annually from 2020, in a full compliance scenario, when the International Maritime Organization’s (IMO) 0.5% sulphur cap for bunker fuels kicks in. A combination of higher crude prices and tight availability of marine gas oil (MGO) could take the price of MGO to almost 4 times that of fuel oil in 2016, the report claimed. (Splash247.com)

**PSL’s Compliance plan for the Clean Oil regime:** PSL plans to burn clean oil to begin with during 2020 unless Scrubbers get authenticated by statutory agencies before then AND drop significantly in price. This will allow us time to see if Scrubbers actually work, whether the manufacturers are financially solvent, and prices would come down over time from their current unaffordable levels. After a year we would be able to buy the latest, most efficient, tried and tested scrubber system from a financially solid manufacturer, at a reasonable price!

### **Key Demand Developments:**

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**The China Factor** continues to have a disproportionate impact on the dry bulk markets. **China’s GDP growth numbers** have been increasing steadily to 6.9% in Q1, higher than the target of around 6.5%. **China’s Iron Ore imports**, according to preliminary Custom’s data, was 271.1 MMT in Q1 2017 or about 12.2% higher than the 241.57 MMT in Q1 2016! Volume of imported Iron Ore in China during 2017 is contingent on import pricing parity versus domestic production and transportation costs. It is also dependent on China moving away from producing ‘normal’ steel to producing higher quality steels which require a much better quality of iron ore that can only come from imports. Provisional **Chinese steel production** for Q1 2017 was about 200.4 MMT or 4.5% more than the 191.72 MMT in Q1 2016. **China’s Coal imports**

totaled 64.7 MMT in Q1 2017 or 33.4% higher than the 48.46 MMT imported in Q1 2016. Coal imports are contingent on import pricing parity versus domestic coal production/transportation costs. It is also dependent on China strictly enforcing its stated goal of curbing pollution from burning 'poor' quality coal mined domestically and that would require much better quality of coal to be imported. In a country that currently produces and consumes some 3.7 BMT of Coal per annum even a small change in China's coal imports could have a significant impact on the Dry Bulk freight markets. **Chinese steel exports** have fallen by 25.5% to 20.7 MMT in Q1 2017 compared to the 27.83 MMT in Q1 2016 carried by geared ships from the Handy to the Ultramax sectors.

We expect **China's government priorities in 2017** to largely be domestic. Ensuring smooth government leadership transitions will take precedence over economic reform perceived as potentially risky. Actions to increase the control of the economy by the Party take precedence over market-based reforms. We will see incremental policy change, largely pushing on the same levers that worked for the government in 2016. But by the second half of 2017, we will see that consumer spending is not growing at the pace needed to deliver the promised GDP growth, leading to **a further boost in debt-funded infrastructure spending and property construction and a bumpier second half of the year.** (Gordon Orr, McKinsey)

**China's economy has shown signs of improvement** in the first two months of 2017 with little risk of a hard landing said Ning Jizhe, head of the National Bureau of Statistics. Industrial output in January and February grew more than 6%, and the services sector expanded over 8%, he said. Ning's remarks indicated that policy makers in the world's second-largest economy are more upbeat as they set a 2017 growth target of about 6.5%. Industrial activity also picked up, with electricity generation, power consumption and rail volume all posting steady growth, according to Ning. The country's campaign to cut overcapacity also appears to be bearing fruit. The coal and steel industries reported negative growth and property inventories in China's third- and fourth-tier cities declined in the first two months, he said. Domestic demand has been robust and the market expectation on China's economy has improved, the statistics chief said. (Bloomberg)

We estimate that a little less than 1,700 vessels totaling **54 MDWT are now in dedicated Chinese coastal trades**, equating to 15% in numerical terms of the total dry bulk fleet. Even though **a majority of vessels in Chinese cabotage trade are Handysize-Supramax**, this still equates to 7% of total fleet deadweight, so swings in domestic coal trade movement can have a significant yet largely unrecognized influence on market direction. The Chinese domestic fleet renewal program which took place in recent years is such that we estimate the average age of this large coastal fleet has come down to an average of just over 8 years, exploding the myth that only older vessels ply these trades. (Howe Robinson Research)

**China's top planning agency aims to control the output and import of low quality coal**, according to a statement posted on its website, the first official confirmation China is trying to rein in supply and reduce domestic overcapacity. This follows a sharp decline in coal imports in February, as shipments fell to a 12-month-low. The statement gave no details,

but a crackdown on low-quality imports could potentially reduce imports from producers such as Indonesia and Mongolia. Traders have already reported delays to their coal import cargoes due to quality control checks by customs. China's planner, the National Reform and Development Commission, also repeated a goal to stabilize coal prices, but said it sees difficulties in balancing the market this year due to uncertainties in temperature and high demand in some regions. (Reuters)

**Chinese coal inventories** are still low, reassuring for the dry bulk market that major power plant coal stockpiles in China now stands at 50.6 MMT, 23% less than was stockpiled at the start of this year and 13% down YOY. YTD coal import (including February) is up 48% and the low levels of coal inventories should continue to support coal import. (DNB Markets)

**China's consumption of coal** fell in 2016 for a third year in a row, according to the National Bureau of Statistics, as the world's top polluter increasingly grapples with its massive pollution challenges. Coal consumption fell by 4.7% last year, according to preliminary calculations. The bureau said the share of coal in China's total energy consumption mix fell to 62% in 2016 from 64% the year before. The production of coal fell by 9% to 3.41 BMT. China has for years been closing smaller, less efficient and more dangerous coal mines in a bid to boost productivity in the sector. (Associated Press)

**China's coal output fell 1.7% in the first two months of the year**, even after Beijing urged miners to ramp up output to replenish supplies during the cold winter months, reversing tough measures to cut the country's reliance on fossil fuels. Miners produced 506.78 MMT of coal in January and February, the National Bureau of Statistics said. That compares with 513.5 MMT in the first two months of 2016 and 546.5 MMT in 2015. (Reuters)

According to Premier Li's Government Work Report, **China has set 2017 capacity cut targets** of 50 MMT for steel and 150 MMT for coal as part of the continuation of supply side reform. This compares to a target of 45 MMT for steel and 250 MMT for coal in 2016. However, the actual cuts were >80 MMT for steel and 290 MMT for coal in 2016 but the majority of cuts were idle capacity (70% in case of steel and >90% in case of coal). Currently, more than 40 MMT of steel capacity and more than 160 MMT of coal capacity are idle. (JP Morgan)

**China's suspension of seaborne coking coal imports from North Korea** on 18 February, through year-end, would be positive for the dry bulk shipping market. China imported approximately 23 MMT of coking coal from North Korea in 2016. This amount would work out to roughly 766 shipments on Handysize bulk carriers. China is expected to substitute North Korean coking coal from several countries, including Australia, Russia and Canada, adding to ton-miles. (IHS Maritime)

**Chinese coal import volumes rebounded in 2016** after government imposed output curbs resulted in a shortage and surging domestic coal prices, forcing coal users to import the material. As a result, total raw coal output fell 9.4% year-on-year to 3.4 BMT, while China's imports increased 25.2% to 255.5 MMT. At the start of the year, the NDRC had announced that



800 MMT of “outdated” and inefficient annual coal capacity would be cut by 2020, while adding 500 MMT of “advanced” capacity. Given the significant efforts being made by the government in trying to tackle air pollution, the development of renewables, and the challenges coming from a slowing economy and shift from heavy industry to services, **peak coal production and consumption in the country has probably arrived.** Nevertheless, seaborne imports will still have (relatively) fair game competing against a high cost, inefficient and environmentally disastrous domestic mining industry. However, as China learns their lessons from the shortage and price surge that resulted from their output curbs in 2016, more carefully executed production cuts this year may curb import growth. (Banchemo Costa)

**China's National Development and Reform Commission (NDRC) announced** it would not revert to the 276-day rule which was introduced in April last year, but abandoned in November after Coal prices had almost doubled. (DNB Markets)

**Coal prices in Asia have rebounded** due to supply concerns triggered by a cyclone hitting mines in Australia and a graft probe by the Indonesian government at ports in the East Kalimantan province. The probe has led to severe delays for the 38 ships that are waiting to load. (Maersk Broker)

**Demand for coal from China is likely to remain the key uncertainty for dry bulk shipping in 2017** according to the Singapore Exchange (SGX). SGX noted in its monthly dry freight report that Chinese coal demand had been one of the main surprises for the market in 2016. “Looking forward, that same dark cloud of uncertainty is likely to linger over 2017,” the report said. “Our latest industry survey revealed widespread expectations that China’s 276-day production restrictions will likely be resumed from the spring, with uncertainty over the impact on import demand as central policymakers adjust production and prices to their desired levels.” (SeaTrade)

**China’s steel output has been rising,** and could hit 825 MMT this year, up from 806.7 MMT in 2016. (IHS Maritime)

**China unleashed its boldest reform plan so far for its bloated steel sector,** saying it will eliminate all production of low-quality steel products by the end of June 2017, a move analysts say could dent steel exports. (Reuters)

**China has boosted vessel demand** from new economies through its strategy of securing raw materials in return for steel and infrastructure development, said Clarksons dry cargo analyst John D’Ancona. China’s support of new economies helped to grow those new markets, in turn driving demand for ocean transportation. **The Southern Silk Road is replicating the astonishing growth that trade experienced in the 1950s with the post-war expansion of OECD trade.** This massive expansion in the burgeoning Southern Silk Road required an economic big brother to develop — which was China. The growth in regional trade was being boosted as China was investing overseas to secure supplies of raw materials from different

regions. In return for investment and infrastructure, oil, iron ore, coal, grain and other commodities were being shipped in increasing quantities to China. (Lloyd's List)

**China is the world's largest aluminium producer**, representing 54% of the global primary aluminium production in 2016. China's aluminium production has grown about 10% per annum on average over the past 5 years, although growth slowed quite drastically in 2016, decreasing 0.1% to 31.6 MMT in reaction to a late 2015 slump in prices. However, a steady price recovery has since incentivised restarts and new capacity additions, with production growth turning positive again since Sep 2016. In 2016, China's bauxite imports fell 7.2% year-on-year to 51.8 MMT. Guinea exported 11.9 MMT of bauxite to China in 2016, up from only 0.3 MMT in 2015. Guinea's export volume in Dec 2016 also exceeded Australia's for the first time. However, we could soon see the return of Indonesian supplies, after they unexpectedly relaxed their mineral export rules in Jan 2017. (Banchemo Costa)

**China imported 7.7 MMT of soybeans in Jan 2017**, an increase of 35.3% year-on-year. This represents the highest level for the month of January since at least 2010. Soybean imports in 2016 saw an increase of 1.9% year-on-year to 83.2 MMT, this was slightly disappointing compared to growth of 12.7% and 14.4% seen in 2014 and 2015 respectively. The **USDA currently still expects China's soybean imports to grow 3.3% year-on-year to 86 MMT**. U.S. soybean exports to China typically start to wind down after peaking in December, with Brazilian exports ramping up from March. Abundant supplies from the top 2 producers are expected to keep them competing closely for top spot. According to Informa Economics, Brazil's soybean production is expected to come in at a record 108 MMT, while the USDA expects U.S. production to reach 117.2 MMT. (Banchemo Costa)

**The Chinese government announced its plans to improve the country's transport infrastructure**. China's 13th Five-year Plan period (2016-2020) anticipates that by 2020, the nation will have 150,000 kilometers of railway lines, five million kilometers of roads, 260 airports and 2,527 berths for vessels over 10,000 tons. (Maritime Executive)

**Colombia's Ministry of Mines and Energy** expects the country's coal production to grow by 8% to 97.0 MMT in 2017. According to preliminary figures from the National Mining Agency (ANM), coal output in 2016 reached 90.0 MMT, up 5% compared with 85.5 MMT in 2015. (Howe Robinson Research)

**Mexico is looking for a new supplier of Corn**, after the diplomatic problems with the United States, caused by the American president, Donald Trump. This week, the Foreign Affairs Committee of the Mexican Congress has signaled that it intends to propose a bill to suspend the importation of corn from the United States and direct purchases to Brazil and Argentina. Mexico is one of the largest importers of corn in the world. According to the US Department of Agriculture report, Mexicans are expected to import nearly 14 million tons this season and the country's domestic consumption is over 38 million tons. (Howe Robinson Research)

After plentiful rains and favourable growing conditions **Australia has recorded a bumper wheat harvest**, expected to be around 35 MMT. Exports are also likely to hit record highs of 25 MMT up nearly 9 MMT on last year's figure. The Far East and South East Asia will take the lion's share of this additional wheat (last year's proportion was 70%); though imports to the Middle East are also set to rise from the 3 MMT in 2016. There is evidence of more wheat moving to East and West Africa whilst certain grades are destined for the Continent. Global wheat production is set to hit a record high of 751 MMT in the 2016/17 growing season with world consumption estimated at 741 MMT. (Howe Robinson Research)

**Brazilian soybean exports** for February at 3.5 MMT are up 72% y-o-y and herald another record breaking year for both harvests and exports. Mato Grosso area harvest estimates alone at 30 MMT are up 10% on last year with further evidence of the strong outlook reflected in soybean's May contract in Chicago closing down \$14.50 cents or 1.4% to \$10.37 per bushel on 10<sup>th</sup> March. (Howe Robinson Research)

**Vietnam's growing GDP**, an increasing urban population, and a shift to a more protein-rich diet have combined to boost meat production and a corresponding need for feedstuffs. In 2017, Vietnam poultry production is forecast up 5% and pork production up 2%, similar to 2016. The growing demand in the Vietnam livestock and aquaculture sector, coupled with favorable prices, has also encouraged Vietnam imports of soybean and soybean meal. In 2016, Vietnam imported over 1.5 MMT of soybeans and nearly 5.1 MMT of soybean meal, boosting total protein meal consumption by 13%. Soybean and soybean meal imports are forecast to continue their growth in 2017, raising total protein feed consumption 10%. (Howe Robinson Research)

**Vale posted record iron-ore output** for the full year of 348.8 MMT, a second straight record and at the upper end of its guidance range. Vale kept a forecast for 2017 of 360 to 380 MMT, and expects to reach a so-called base case of 400 MMT in 2018. (Bloomberg)

In January 2014, **Indonesia** introduced its ban on unprocessed mineral exports, including bauxite and nickel ore, in a bid to promote the country's processing industry. The emergence of alternative exporters such as the Philippines and Malaysia failed to fill the gap left by Indonesia, leading to an average 12% pa. drop in combined seaborne bauxite and nickel ore trade in 2014-16, compared to a 29% pa. rise in 2011-13. Then in January 2017, Jakarta unexpectedly relaxed its mineral export ban. Given ongoing disruptions to Malaysian and Philippine mineral exports, Indonesia's return may provide a well timed source of minor bulk trade growth. Looking forward, while the impact of Indonesia's return may at first be fairly gradual, it has the potential to change the minor bulk game. (Clarksons)

**Indian Iron ore cargo** through major ports has logged the sharpest growth among all commodities in April-December period. Till the end of December, iron ore shipments were up from 12.7 MMT to 32.4 MMT, a rise of 154%. (Business Standard)

**Japanese companies are planning to develop about 45 additional coal power plants** in the next decade, as the country gradually ramps up its nuclear power generation

following the Fukushima disaster in 2011, the US Energy Information Administration said. "The country is installing new, clean coal plant technologies, such as Ultra-supercritical units or integrated gasification combined-cycle technology, to meet environmental targets and to replace some of the decades-old coal power plants," EIA said. While no significant coal-fired capacity is expected to come online before 2020, the 45 new coal power plants are expected to add more than 20 GW of capacity in the next decade, it said. Coal's share in Japan's power sector was an estimated 23% before the Fukushima disaster in 2011 and rose to 31% by 2015. The government is now planning for coal to account for 26% of the market share by 2030, EIA said. Coal is also expected to displace some of the expensive oil-fired power generation, EIA said. "Oil remains the largest source of primary energy in Japan, although its share of total energy consumption has declined from about 80% in the 1970s to 42% in 2015," it said. Japan's increased requirement of coal will be met by imports, as the country's domestic coal production dwindled to virtually nothing by 2002 and it began importing all of its coal, primarily from Australia. "Imports [of coal] grew to 210 million short tons of coal in 2015 from 193 million short tons in 2011, after more coal-fired generation capacity came online," the EIA said. (Platts)

With most of 2016's data now collected, in our opinion it is fair to say that 2016 was a year with better than expected demand growth in the dry bulk segment. **We now estimate ton-mile growth of 4.1% for 2016e.** (DNB Markets)

Today (18<sup>th</sup> March 2017), almost ten years after the most severe financial crisis since the Depression, **a broad-based economic upswing is at last under way.** In America, Europe, Asia and the emerging markets all the burners are firing at once. But the political mood is sour. A populist rebellion, nurtured by years of sluggish growth, is still spreading. Globalisation is out of favour. An economic nationalist sits in the White House. The Fed raised rates for the second time in three months—thanks partly to the vigour of the American economy, but also because of growth everywhere else. Fears about Chinese overcapacity, and of a Yuan devaluation, have receded. In February factory-gate inflation was close to a nine-year high. In Japan in the fourth quarter capital expenditure grew at its fastest rate in three years. The euro area has been gathering speed since 2015. The European Commission's economic-sentiment index is at its highest since 2011; euro-zone unemployment is at its lowest since 2009. (The Economist)

**The dry bulk market appears to have turned a corner**, with much improved sentiments and rates mostly at their highest for this period since 2015. It seems **we may finally be seeing the light at the end of the tunnel, as long as demolition activity and limited ordering persists.** (Banchemo Costa)

Yours Sincerely,

Precious Shipping Public Company Limited

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Khalid Hashim  
Managing Director

# PRECIOUS CAPITAL

## PUBLIC DEBT DEAL OF THE YEAR

*Transaction: Precious Shipping Public Company Limited THB 3.59 Billion  
Unsubordinated Unsecured Bonds*

*Winner: Krung Thai Bank Public Company Limited*

**A**n equity raise via a rights issue in mid-2015 of around US\$ 63 Million from Precious Shipping (PSL) shareholders was considered to be enough to tide over the financing requirements of the company through the dry bulk downturn. But, then the already weak shipping markets continued to drop further and, barely 3 or 4 months later, PSL suffered its first ever negative cash flow in Q2 2015. This rapid drop from a relatively comfortable position to a challenging situation which PSL salvaged with a first-of-its kind, path-breaking bond issue (with USD swap) in the Thai Bond Market, is the story of Precious Shipping's Public Debt, Deal of the Year Award for 2016.

Precious Shipping Public Company Limited (PSL) was established in 1989 and listed on the Stock Exchange of Thailand in 1993. It is one of the largest pure dry cargo ship-owning companies operating in the geared (10,000 to 64,000 DWT) sector of the tramp freight market. PSL presently (as on 31st December 2016) operates 32 bulkers and 4 cement carriers, representing

1.54 million DWT. Principal cargoes handled by PSL are agricultural products, cement, steel, fertilizers, ore and concentrates, logs, coke and other items. Geographically, PSL estimates its business to be divided evenly across five regions: i) USA – Canada, ii) Europe, iii) Latin America – Africa, iv) Indian Subcontinent – Middle East, and v) South East & Far East Asia.

PSL operates the majority of its ships in difficult markets and ports that have limited infrastructure. This distinction provides a competitive advantage and allows PSL to enjoy stable charter rates compared to other operators. PSL's geared ships also have operational and economic advantages in the sense that the ships' equipment can easily discharge and/or load cargoes at a very economical cost. Geared ships are, therefore, preferred over larger, gearless ships, despite the latter's proven economy of scale. PSL also benefits from a young fleet, diversified revenue sources, a brand name, in-house technical and experienced management, exemplary governance, and considered risk management

practices. These skill sets distinguish the company and are invaluable.

PSL also recognized that long-term focus is required to compete in the volatile shipping business. Thus, PSL started moving towards the newly developed Ultramax design ships in 2013 by signing shipbuilding contracts for 24 Ultramax ships between 2013–2015 from two Chinese shipyards. During this period, PSL also signed shipbuilding contracts for two Eco design Handysize ships from a third Chinese shipyard.

It was the general consensus of the industry around this time that the shipping markets were set to have better days from 2015 onwards, but those better days have yet to come.

Immediately after placing the orders, PSL began securing financing for the newbuilding contracts by putting in place secured credit facilities from banks and financial institutions. However, it soon became apparent to PSL that one of the shipyards would not be able to deliver the vessels in accordance

with the shipbuilding contracts and the relevant technical specifications. PSL tried to negotiate an amicable settlement, but those efforts did not bear fruit, and a huge amount of cash was (and continues to be) tied up in arbitration.

This predicament was exacerbated when, in the latter part of 2015, contrary to the vast majority of the industry's expectations, the already weak shipping markets fell even farther, causing not only misery for owners but also for the very banks upon which they relied. With imminent cash requirements amidst a very weak market, in June 2015, PSL turned to its shareholders to raise cash through a rights offering. PSL offered one additional share for every two held, and raised USD 63 million without causing any dilution to its existing shareholders. The infusion of equity shored up PSL's finances and appeared sufficient at that time.

However, there continued to be tremendous downward pressure on PSL's earnings during the year 2015 and so, in Q2 2015, PSL suffered negative cash flow

for the first time in almost two decades. With the shipping markets — and particularly the dry-bulk sector — being so weak, funding avenues became even scarcer.

Pushed now to the brink, yet undaunted PSL, explored all of the following:

- Secured debt from traditional shipping banks
- Unsecured debt from Singapore MTN market
- International Bond Market – based on the shipping industry’s rating, the indicative coupon rate PSL would have had to pay was in double digits, which was absolutely unfeasible
- Norwegian Bond Market - but it was not available for the requisite amount or the required (long) tenor, and the pricing was also too high
- Sale and Leaseback – Available options were either too expensive or the amount of financing inadequate
- Equity – PSL had recently concluded a rights offering and, therefore, could not immediately return to existing shareholders for additional funds.

## A NEW UNTAPPED MARKET!

In Q4 2015, the continued weakness in the dry bulk sector triggered a breach of the “loan to value” covenant of certain existing secured loan facilities for which additional funds were required in order to remedy the breaches. PSL, with only a slim window of opportunity, then approached one of Thailand’s top three banks, Krung Thai

Bank Public Company Limited, to see if the bank would be interested in arranging a Thai Baht Bond in the Thai Bond Market.

The bank’s response was positive, but the path towards making a Thai Bond issue had multiple hurdles to overcome:

- Because of the existing secured loan facilities, PSL had little or no security to offer
- Credit rating – PSL would need to get a reasonable credit rating, which was not in itself a problem, but posed a hurdle due to the paucity of time
- Size – Companies of PSL’s size were usually unable to raise more than USD 50 million in the Thai Bond Market, about half of what PSL was targeting
- Pricing – was beyond PSL’s control, and would largely depend on the credit rating that PSL would receive, but a higher coupon would make the bond unworkable
- Tenor – PSL was looking for a tenor of at least five years, but companies of PSL’s size usually issued instruments with three-year tenors, and some even as low as one year
- Exchange risk – Any issue in the Thai Bond Market would be in Thai Baht, not US Dollars. Despite being a Thai company, PSL’s functional currency is US Dollars, so Thai bonds posed a serious exchange risk.

PSL partnered with the bank to overcome these hurdles through a Thai Baht bond program, with a tailor-made USD/Thai

### The main features of the transaction include:

<b>Issuer:</b>	Precious Shipping Public Company Limited
<b>Issue Date:</b>	22 January 2016
<b>Issue Size:</b>	THB 3,590 million (THB 3,500 million + THB 90 million oversubscription)
<b>Listing:</b>	Thai Bond Market Association:
<b>Bonds Offered:</b>	Unsubordinated Unsecured Bonds
<b>Arranger/Swap Provider:</b>	Krung Thai Bank Public Company Limited
<b>Coupon:</b>	5.25% p.a. USD
<b>Value after swap:</b>	USD 99.72 million with the USD fixed rate at 5.99% p.a.
<b>Restrictive Covenants:</b>	Standard & customary
<b>Use of proceeds:</b>	Refinance existing debt, investments and acquisitions, capital expenditure, working capital and/or general corporate purposes

Baht swap. PSL’s management, through extensive negotiations with the bank, ensured that the bank was not only the sole arranger for the program, but also firmly underwrote the entire planned issue amount, which mitigated the risk of failure in placement of the bonds.

PSL next secured an investment grade rating, not only for PSL as a company, but also for the planned bond issue. Thus, in January 2016, in the thick of the darkest phase in the history of the shipping industry, PSL was able to raise almost THB 3.6 billion through an unsecured bond issue on the following terms:

- Size – THB 3,590 million was just the right amount (about USD 100 million) which normally would not have been possible for a company of PSL’s size to raise. However, through the marketing strategy and rigorous marketing activities conducted in partnership and with the full support of the arranger, there was tremendous investor interest, which resulted in an oversubscription
- Pricing – With investment

grade rating, further supported by the aforementioned investors’ confidence in PSL and rigorous marketing activities, PSL managed to make the issue with a very competitive fixed coupon of 5.25% p.a.

- Tenor PSL - was successful in doing so, and managed to secure a tenor of five years, which is much longer than that of other companies of PSL’s size
- Exchange risk – Simultaneously with the bond issue, PSL signed off on a tailor-made USD/Thai Baht swap agreement. However, truly remarkable was that the pricing still remained at under 6% p.a. on the USD amount, less than half of what a shipping bond was expected to yield in the USD bond markets at the time.

For the wisdom to raise funds as soon as possible, and for this tremendous achievement given the unprecedented shipping market conditions and investor outlook towards the shipping industry in general at the time, we are delighted to give PSL our Public Debt Deal of the Year!!

