The Pakistan Credit Rating Agency Limited

PAKISTAN NATIONAL SHIPPING CORPORATION

	NEW [FEB-17]	PREVIOUS [FEB-16]
Long Term	AA	AA-
Short Term	A1+	A1+
Outlook	Stable	Stable
Action	Upgrade	Maintain

REPORT CONTENTS

FEBRUARY 2017

Profile & Ownership

- PNSC Group, with a fleet of nine vessels, is engaged in the business of shipping, charter of vessels, transportation of cargo and real estate.
- The Group constitutes PNSC holding company, its nineteen subsidiaries and an associate concern.
- Incorporated in 1979, as a result of merger of National Shipping Corporation and Pakistan Shipping Corporation.
- Listed on Pakistan Stock Exchange.
- Majority (85.16%) owned by Government of Pakistan (GoP) through the Ministry of Ports and Shipping.

Governance

- Board comprises seven members; five GoP nominees and two independent directors.
- The CEO, a GoP nominee, is vested with the authority of Chairman as per the governing Shipping Ordinance.
- For better governance and oversight of the company the board has formed three committees i) Audit Committee ii) Human Resource & Remuneration Committee and iii) Commercial Committee.
- Governance quality bode well owing to diversified experience and technical stature of board members.

Management

- The CEO, Mr. Arif Elahi, joined PNSC in Mar15. Mr. Elahi, a civil servant, has been associated with GoP in various capacities for more than 30 years.
- A tall organizational structure with a professional management team supported by ten committees.
- Experienced management with long association with PNSC.

Business and Operational Risk

- Strong technology infrastructure - employs SAP based ERP system and an international satellite system, Purple Finder, to track vessels.
- Remains in close co-ordination with Pakistan Navy, NATO and Combined Task Force for risky voyages.

Performance

- Liquid cargo dominates the topline (~66%) followed by Slot Charter (22%) and Bulk Cargo (12%)
- During FY16, overall revenues witnessed modest decline primarily on account of decline in liquid business with PSO.
- PNSC has signed Contract of Affreightment with four refineries. Share of revenue from refineries improved during the year (FY16: 40%, FY15: 35%).
- Overall margins improved on the back of reduced lubricant and charter hire expenses. (Gross margin: FY16: 28%, FY15: 20%).
- Reduction in finance cost also helped PNSC in registering higher net income YoY (FY16: PKR 2.3bln, FY15: PKR 2.1bln).
- Going forward, PNSC is planning to add two new vessels into its fleet alongwith two ferries.

Financial Risk

- PNSC's working capital needs orginate mainly from demurrage expenses receivable from the clients. Majority of the demurrage expenses are of PSO – PKR 1.3bln. The company meets working capital needs from internal cash flow generation.
- FCFO – a function of EBITDA – increased by 34% YoY. Resultantly, coverages improved (Interest Coverage: FY16: 6.3x, FY15: 3.9, Debt Coverage: FY16: 2x, FY15: 1.1x).
- Low leveraged capital structure (end-Sep16: 15.2%). Further loan to expand fleet size would increase leveraging; though likely to remain in comfortable range.

RATING RATIONALE

The ratings reflect PNSC's strong ownership - majority owned by Government of Pakistan - and its strategic significance as the country's flag carrier. On a stand-alone basis, PNSC's business profile has gained significant strength in recent years as exhibited by continuous improvement in business margins on account of efficient fleet utilization, better pricing strategy, and cost management measures taken by the management. The company is currently catering increasing business volumes through chartered-hire vessels. Considering the volatility in margins, the company aims to increase its own fleet size by acquiring two vessels – Aframax and Long-range I. The expansion also includes acquisition of two ferries. These expansions are expected to result in improved revenue base and higher margins, in turn, further fortification in business profile of the company. The acquisition of new vessels would be majorly financed through debt; thus higher leveraging. This would burden the financial profile; however, improving cash flows from existing business coupled with expectation of additional high margin business to be catered by new vessels is likely to generate commensurate cashflows to support debt service coverages. This, along-with on-balance sheet liquidity, supports overall risk profile of the company.

KEY RATING DRIVERS

The ratings are dependent on the Corporation's ability to generate envisaged cash flows post-expansion. Meanwhile, proactive management of financial profile while improving coverages remains important.

PKR mln

Pakistan National Shipping Corporation Limited

BALANCE SHEET	30-Sep-16	30-Jun-16	30-Jun-15	30-Jun-14
	1QFY16	Annual	Annual	Annual
Non-Current Assets	**24,146**	**24,300**	**25,276**	**22,658**
Investments (Incl. associates)	**54**	**50**	**54**	**54**
Equity	54	50	54	54
Debt				
Current Assets	**6,823**	**6,074**	**7,211**	**6,296**
Trade Receivables	811	621	1,028	2,564
Others	6,012	5,453	6,183	3,732
Total Assets	**36,983**	**36,538**	**36,270**	**32,384**
Debt	**5,052**	**5,352**	**7,450**	**5,886**
Short-term	-	-	-	-
Long-term (Inlc. Current Maturity of long-term debt)	5,052	5,352	7,450	5,886
Other shortterm liabilities	3,100	2,991	2,562	2,642
Other Longterm Liabilities	599	613	852	617
Shareholder's Equity	**28,231**	**27,582**	**25,407**	**23,238**
Total Liabilities & Equity	**36,983**	**36,538**	**36,270**	**32,384**
INCOME STATEMENT				
Turnover	**3,638**	**12,368**	**15,381**	**15,585**
Gross Profit	1,150	3,491	3,111	3,308
Other Income	74	509	810	460
Financial Charges	(91)	(559)	(670)	(549)
Net Income	**650**	**2,323**	**2,116**	**2,149**
Cashflow Statement				
Free Cashflow from Operations (FCFO)	1,162	3,476	2,601	2,855
Net Cash changes in Working Capital	(229)	662	123	(268)
Net Cash from Operating Activities	837	3,589	2,084	2,259
Net Cash from Investing Activities	(289)	(106)	(2,862)	(435)
Net Cash from Financing Activities	(299)	(4,653)	1,440	(2,958)
Net Cash generated during the period	249	1,169	663	(1,134)
Ratio Analysis				
Performance				
Turnover Growth	23.9%	-19.6%	-1.3%	28.5%
Gross Margin	31.6%	28.2%	20.2%	21.2%
Net Margin	17.9%	18.8%	13.8%	13.8%
ROE	9.3%	8.5%	8.8%	9.5%
Coverages				
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	3.0	2.0	1.1	1.5
Interest Coverage (x) (FCFO/Gross Interest)	12.8	6.3	3.9	5.2
Debt Payback-Years (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCI	1.2	1.8	3.9	2.6
Liquidity				
Short-term Total Leverage (Net Current Assets - STB) / Current Assets	55%	51%	64%	58%
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	54	50	33	15
Capital Structure (Total Debt/Total Debt+Equity)	15.2%	16.3%	22.7%	20.2%

The Pakistan Credit Rating Agency Limited

STANDARD RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

LONG TERM RATINGS

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Speculative.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**Highly speculative.** Significant credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**High default risk**. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

SHORT TERM RATINGS

A1+: The highest capacity for timely repayment.

A1:. A strong capacity for timely repayment.

A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.

A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved with in foreseeable future, but may continue if underlying circumstances are not settled.

Outlook (Stable, Positive, Negative, Developing)
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Suspension
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, or e) the entity/issuer defaults.

Regulatory and Supplementary Disclosure

Name of Issuer	Pakistan National Shipping Corporation Limited
Sector	Shipping
Type of Relationship	Solicited
Purpose of the Rating	Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
16-Feb-16	AA-	A1+	Stable	Maintain
17-Feb-15	AA-	A1+	Stable	Maintain
17-Jan-14	AA-	A1+	Stable	Maintain
16-May-13	AA-	A1+	Stable	Maintain
24-Apr-12	AA-	A1+	Stable	Maintain

Related Criteria and Research

Rating Methodology	Corporate Rating Methodology
Research:	Shipping Sector - Viewpoint | Feb-16

Rating Analysts

Aisha Khalid
aisha@pacra.com
(92-42-35869504)

Rana Nadeem
nadeem@pacra.com
(92-42-35869504)

Rating Team Statement

Rating Procedure
Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

Disclaimer

Rating Shopping
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PACRA has used due care in preparation of this document. Our information has been obtained directly from the underlying entity and public sources we consider to be reliable

but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information.

Conflict of Interest
PACRA, the analysts involved in the rating process, and members of its rating committee do not have any conflict of interest relating to the credit rating done by them
The analysts involved in the rating process do not have any interest in a credit rating or any of its family members has any such interest
The analysts and members of the rating committees including the external members have disclosed all the conflict of interest, including those of their family members, if any, to the Compliance Officer PACRA
The analysts or any of its family members do not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This is, however, not applicable on investment in securities through collective investment schemes. PACRA has established appropriate policies governing investments and trading in securities by its employees
PACRA may provide consultancy/advisory services or other services to any of its clients or to any of its clients' associated companies and associated undertakings that is being rated or has been rated by it. In such cases, PACRA has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities
PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and ii) fee mandate - signed with the payer, which can be different from the entity
PACRA ensures that the credit rating assigned to an entity or instrument should not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship

Surveillance
PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the rated entity/ issuer, the security arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer
PACRA reviews all the outstanding ratings on annual basis or as and when required by any stakeholder (including creditor) or upon the occurrence of such an event which requires to do so
PACRA initiates immediate review of the outstanding rating(s) upon becoming aware of any information that may be reasonable be expected to result in any change (including downgrade) in the rating

Reporting of Misconduct
PACRA has framed and implemented whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct relating to the credit rating by another employees of the company that came to his/her knowledge. The Compliance Officer reports to the BoD and SECP

Confidentiality
PACRA has framed a confidentiality policy to prevent abuse of the non-public information by its employees and other persons involved in the rating process, sharing and dissemination of the non-public information by such persons to outside parties
Where feasible and appropriate, prior to issuing or revising a rating, PACRA informs the issuer of the critical information and principal considerations upon which a rating will be based and provide the opportunity to clarify any likely factual misperception or other matter that PACRA would wish to be made aware of in order to produce a fair rating. PACRA duly evaluates the response. Where in a particular circumstance PACRA has not informed the entity/issuer prior to issuing or revising a rating, it informs the entity/issuer as soon as practical thereafter

Prohibition

Probability of Default (PD)

PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past