The Pakistan Credit Rating Agency Limited

Rating Report

Pakistan National Shipping Corporation

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
26-Dec-2019	AA	A1+	Stable	Maintain	-
27-Jun-2019	AA	A1+	Stable	Maintain	-
27-Dec-2018	AA	A1+	Stable	Maintain	-
29-Jun-2018	AA	A1+	Stable	Maintain	-
29-Dec-2017	AA	A1+	Stable	Maintain	-
13-Feb-2017	AA	A1+	Stable	Upgrade	-
16-Feb-2016	AA-	A1+	Stable	Maintain	-
17-Feb-2015	AA-	A1+	Stable	Maintain	-
17-Jan-2014	AA-	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect PNSC's strong ownership - majority owned by the Government of Pakistan (89.13%) - and its strategic significance as the country's national flag carrier. The Corporation operates on a "One Vessel One Company" basis. PNSC's business profile has gained significant strength in recent years on account of efficient fleet utilization and cost management measures taken by the management. Business volumes are a mix of liquid and dry cargo, with liquid cargo bearing a higher weightage. Lately, the Corporation's business volumes with PSO took a dip owing to reduction of furnace oil imports in the country. The foregone share in topline is, however, covered by initiation of white oil transportation projects through expansion of the managed tanker fleet; thereby, two new oil tankers (LR-1) have joined the Corporation's managed fleet bringing up the total fleet number to eleven (11) and dead-weight tonnage capacity to 831,711DWT – being highest in the history. The Corporation also operates through chartered-hire vessels to stimulate business volumes. PNSC further plans to acquire one more Aframax oil tanker in FY20. Based on the international shipping practices, procurement of ships is 90% financed through external debt. On the other hand, additions in managed fleet are expected to boost up the revenue base and generate better profit margins than from chartered-hire vessels business. This factor, put along with the Corporation's on-balance sheet liquidity, is a support to the overall risk profile.

The ratings are dependent on the Corporation's ability to generate envisaged cash flows post-expansion. Meanwhile, prudent financial discipline alongside growth trajectory is imperative.

Disclosure

Name of Rated Entity	Pakistan National Shipping Corporation
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-19),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-19)
Related Research	Sector Study | Shipping(May-19)
Rating Analysts	Muhammad Usman | muhammad.usman@pacra.com | +92-42-35869504

Profile

Legal Structure The Pakistan National Shipping Corporation (herein referred to as the "PNSC" or "the Corporation") is an Autonomous Corporation, functioning under the control of the Ministry of Maritime Affairs, Government of Pakistan. The Corporation is listed on the Pakistan Stock Exchange since 1980, and has nineteen subsidiaries and one associate concern.

Background PNSC came into existence by the merger of National Shipping Corporation (NSC) and Pakistan Shipping Corporation (PSC) in 1979 through Pakistan National Shipping Corporation Ordinance, No XX, 1979. The Corporation is entirely autonomous and is managed by its Board of Directors (BoD).

Operations PNSC, being the national flag carrier of Pakistan, is involved in the transportation of dry bulk and liquid cargoes globally through managed and chartered vessels. The Corporation manages a fleet of 11 vessels, consisting of 6 tankers and 5 bulk carriers. The cargo carrying capacity of PNSC stands at ~831,711 DWT as at End-Sep'19. A small portion of PNSC's operations also comprises income from real estate business.

Ownership

Ownership Structure PNSC is majorly owned by the Government of Pakistan (GoP) (87.3%), through the Ministry of Maritime Affairs, followed by PNSC Employees Empowerment Trust (1.83%), bringing the total GoP holding to 89.13%.

Stability Stable ownership structure exists, with the GoP possessing majority stakeholding in the Corporation since its formation.

Business Acumen The Corporation was formed under constitutional protection with an objective of providing the country with a national flag shipping service. Major stakeholder in the Corporation is the GoP. Business acumen is, therefore, considered strong.

Financial Strength Financial strength of the owners is considered strong.

Governance

Board Structure The Corporations's BoD is constituted members nominated by the Federal Government and minority shareholders. A seven member board of directors exists, with five of these directors (including the Chairman) nominated by the GoP. Two directors are elected by the shareholders.

Members' Profile The Board is chaired by Mr. Rizwan Ahmed. He joined PNSC in December'17. He is also the Federal Secretary - Ministry of Maritime Affairs. Prior to his association with PNSC, Mr. Rizwan had served on various key positions in the federal and provincial governments. He has brought with him vast professional experience in administration, finances, management, human resource, law enforcement and public procurement.

Board Effectiveness The Board has formed two sub-committees, namely (i) Audit & Finance Committee & (ii) HR and Remuneration Committee.

Financial Transparency The Corporation complies with the Listed Companies (Code of Corporate Governance) Regulations 2019, applicable on listed entities, which strengthens its overall governance framework. In FY19, the Corporation was jointly audited by the EY Fort Rhodes, Chartered Accountants and KPMG Taseer Hadi & Co., Chartered Accountants, two of the big four firms. The Corporation is being audited by Grant Thornton Anjum Rehman Chartered Accountants and KPMG Taseer Hadi & Co., Chartered Accountants, from FY20.

Management

Organizational Structure PNSC has a well-defined organizational structure with a professional management team.

Management Team Seasoned professionals, having long association with PNSC hold the key management positions in the Corporation. Mr. Rizwan Ahmed, the Board Chairman, also acts in the capacity of the CEO as per the PNSC Ordinance, 1979.

Effectiveness In order to keep an effective oversight of the business operations, twelve management committees are in place constituting various key management personnel.

MIS PNSC deploys Enterprise Resource Planning (ERP) software – "Ship Management Expert System" (SES) – for its MIS reporting. The system provides online link between vessel and head office. The Corporation employs 'Purple Finder' – an international satellite system, to track its vessels with the help of equipment trackers that have been installed in the fleet.

Control Environment The Corporation relishes on strong governance practices and discrete management system. A tall organization structure with clearly defined lines of responsibilities exist. This is accompanied by an integrated well-versed information system to support functions pertinent to a shipping corporation.

Business Risk

Industry Dynamics Pakistan's total seaborne trade in FY19 reached to ~111mln DWT (FY18:~100mln DWT), out of which ~80mln DWT constituted dry bulk trade and the rest accounted for liquid bulk trade. Liquid bulk comprises import of black and white oil variants by the oil and gas sector of the country. In white oil products, MOGAS is largely imported which is expected to benefit PNSC in the future as it has lately added clean oil tankers to its fleet. On the contrary, furnace oil consumption has dropped to ~18% of the total country fuel consumption in FY19 (FY18: ~29%).

Relative Position The Corporation's share in Pakistan's seaborne trade was recorded at ~9% during FY19 (FY18:~13%). In liquid bulk cargo, PNSC has a considerable share (~26%), whereas in dry bulk, the Corporation possesses a share of ~3.0%. PNSC operates as a global sea-freight operator and is privileged of being the sole national flag carrier of Pakistan comprising 100% of the country's total fleet.

Revenues PNSC's revenue emanates from income earned from managed and charter vessels. During FY19, mix in liquid cargo and dry bulk was recorded at 60:40 ratio. Dry bulk can further be subdivided into slot charter and bulk cargo. A small contribution in topline comes from rental income too. During FY19 and 3MFY20, PNSC's topline reflected an upward trend, overcoming the hurdles faced due to restrictions imposed on import of furnace oil. In FY19, the shipping revenue clocked in at PKR~10,694mln (FY18: PKR~9,718mln) up by ~10% on a Year-on-Year basis. During 3MFY20, revenue clocked in at PKR~3,060mln, depicting a (annualized) growth of ~14% compared to FY19. The implementation of the latest International Maritime Organization (IMO) regulations and white oil opportunities are expected to have a positive impact on PNSC's revenue in the future.

Margins During FY19 and 3MFY20, PNSC's margins regained their pattern after witnessing a contraction during FY18, owing to improved freight rates and better volumes. Since shipping industry is indexed, AFRA rates directly impact the freight rate charged by PNSC to refineries. Both AFRA rates and Bulk Dry Index (BDI) represented an uptick in FY19, as global shipping industry is regaining its momentum. Gross Margin for 3MFY20 clocked in at ~28% (FY19: ~25%, FY18: ~21%). In FY19, PNSC's net profitability margins also rose to ~21% (FY18: ~17%), while decreasing to ~16% in 3MFY20, mainly as a result of a rise in finance costs.

Sustainability PNSC – being a Sovereign ownership, is a sustainable corporation. Business volumes and margins are dependent on the global shipping market indicators as well as country level sea trade dynamics. However, as the Corporation is expected to operate as a Sovereign Asset, this would mitigate its susceptibility to commercial competition in the domestic landscape. PNSC has, lately, embarked on projects for 'white oil' imports. After successfully inducting two new tankers on board in FY19, PNSC is moving towards further fleet expansion. Accordingly, one more Aframax Tanker is planned for procurement in FY20.

Financial Risk

Working Capital In line with the Shipping Industry dynamics, PNSC's working capital management comprises need for funding receivable and payable days only. PNSC meets working capital needs from internal cash flow generation. A well-balanced cash conversion and payment cycle exists within the business model, as evident from its impressive gross working capital days (3MFY20: 4 days, FY19: 7 days, FY18: 10 days) and net working capital days (3MFY20: -5 days, FY19: -9 days, FY19: -13 days).

Coverages FCFO - a function of EBITDA - remained strong through sanguine profits (3MFY20: PKR~1,027mln, FY19: PKR~3,371mln, FY18: PKR~2,350mln). Debt coverages, therefore, remained in a comfortable zone (3MFY20: 1.5x, FY19: 1.5x, FY18: 1.6x).

Capitalization PNSC paid dividend worth PKR~198mln in FY19. Although increasing, the Corporation has a comfortably leveraged structure (3MFY20: ~21%, FY19: ~22%, FY18: ~9%). As of Sep'19, quantum of long term borrowings with respect to purchase of new vessels clocked in at PKR~8,544mln. The same is expected to be pushed upwards as debt for acquisition of new vessels is obtained. Going forward, change in capital structure remains critical.

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Financial Summary
PKR mln

Pakistan National Shipping Corporation Limited	Sep-19	Jun-19	Jun-18	Jun-17
Shipping	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	29,687	29,981	22,241	23,242
2 Investments	6,330	6,481	7,208	6,848
3 Related Party Exposure	2,426	2,474	2,835	2,492
4 Current Assets	6,295	6,120	5,332	5,071
a Inventories	-	-	-	-
b Trade Receivables	*142*	*116*	*296*	*233*
5 Total Assets	44,738	45,055	37,616	37,652
6 Current Liabilities	2,366	2,653	2,720	3,061
a Trade Payables	*305*	*280*	*664*	*550*
7 Borrowings	8,544	9,083	2,954	4,154
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	724	711	601	592
10 Net Assets	33,104	32,608	31,341	29,845
11 Shareholders' Equity	33,104	32,608	31,341	29,845
B INCOME STATEMENT				
1 Sales	3,060	10,694	9,718	12,286
a Cost of Good Sold	*(2,203)*	*(8,013)*	*(7,660)*	*(8,832)*
2 Gross Profit	857	2,681	2,057	3,455
a Operating Expenses	(259)	(1,113)	(1,064)	(1,007)
3 Operating Profit	598	1,568	994	2,447
a Non Operating Income or (Expense)	*247*	*1,337*	*1,111*	*985*
4 Profit or (Loss) before Interest and Tax	845	2,905	2,104	3,432
a Total Finance Cost	*(303)*	*(450)*	*(250)*	*(330)*
b Taxation	*(47)*	*(260)*	*(213)*	*(625)*
6 Net Income Or (Loss)	495	2,194	1,641	2,477
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,027*	*3,371*	*2,350*	*3,796*
b Net Cash from Operating Activities before Working Capital Changes	*729*	*2,966*	*2,105*	*3,471*
c Changes in Working Capital	*(672)*	*(948)*	*(831)*	*(970)*
1 Net Cash provided by Operating Activities	57	2,018	1,274	2,502
2 Net Cash (Used in) or Available From Investing Activities	219	(7,825)	118	(319)
3 Net Cash (Used in) or Available From Financing Activities	(540)	6,049	(1,461)	(1,471)
4 Net Cash generated or (Used) during the period	(264)	241	(69)	712
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	14.4%	10.0%	-20.9%	-0.7%
b Gross Profit Margin	28.0%	25.1%	21.2%	28.1%
c Net Profit Margin	16.2%	20.5%	16.9%	20.2%
d Cash Conversion Efficiency (EBITDA/Sales)	37.6%	37.0%	29.9%	36.2%
e Return on Equity (ROE)	6.0%	6.9%	5.4%	8.6%
2 Working Capital Management				
a Gross Working Capital (Average Days)	4	7	10	24
b Net Working Capital (Average Days)	-5	-9	-13	5
c Current Ratio (Total Current Assets/Total Current Liabilities)	2.7	2.3	2.0	1.7
3 Coverages				
a EBITDA / Finance Cost	3.9	8.9	11.8	13.6
b FCFO / Finance Cost+CMLTB+Excess STB	1.5	1.5	1.6	2.5
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	2.9	3.1	1.4	1.2
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	20.5%	21.8%	8.6%	12.2%
b Interest or Markup Payable (Days)	16.8	44.0	38.6	39.7
c Average Borrowing Rate	13.5%	7.4%	6.9%	6.9%

Rating Scale | Corporate

2019

Credit Rating Scale & Definitions

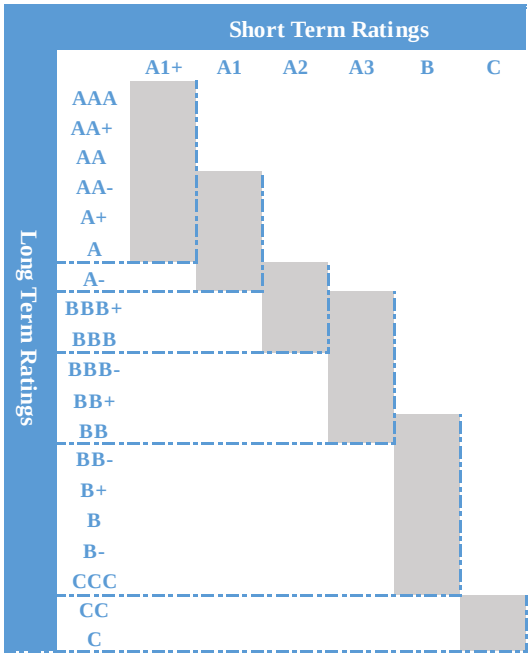
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High 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	**Very high credit 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.



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'.

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. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

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, e) the entity/issuer defaults., or/and f) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest
(12) 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 fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is 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 | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) 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 | Chapter III | 14-(f-VII)
Proprietary Information