

Dry Bulk Shipping

Position for the coming high tide, Buy PSL & TTA

Share Price Performance



Source: SET

Share performances

	1M	3M	12M
Absolute			
PSL	5.9	4.7	(2.2)
TTA	10.6	9.2	(14.1)
Relative			
PSL	(1.5)	(9.1)	(6.4)
TTA	3.2	(4.7)	(18.3)

Source: SET

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- **The BDI pullback** — The Baltic Dry Index has plunged 43% from the Jun09 peak (Chart 1), closing at 2,462 pts. The pullback is mainly driven by the sharp fall in rates for larger vessels: Capesize was 56% off peak and Panamax 26% off peak. While Handysize index (small vessels), has turned up a slight 0.3%, the segment accounts for ~18% of the Index (Chart 2). TTA and PSL operate handysize ships.
- **BDI poised for a rebound** — The correction in the Capesize index is mainly due to low cargo movement in the iron ore sector. After China Iron & Steel Association rejected Rio Tinto Group's proposed price of US\$61/ton FOB for high grade iron ore, a 33% cut YoY, Chinese buyers pulled back from the market. Now they are reportedly waiting for the spot prices to correct 40%YoY before resuming buying. The "desired" strike price represents a further 18% drop from current levels.
- **Likely turnaround in 4Q09** — Currently the spot price of iron ore is nearly on par with the price agreed upon with Rio Tinto by Japanese and South Korean buyers. Recent price reports quote iron ore landed in China at about US\$77/ton. Netting freight costs of ~US\$12/ton, FOB is about US\$65/ton. More importantly, the landed price is now ~20% lower than the domestic price in China, and this gap, in our view, already gives significant cost advantage to crude steel makers that rely on imported iron ore. Demand for iron ore has been improving as indicated by crude steel production. China, as before the 2008 crisis, led the world in terms of growth. Beyond China, there are signs of gradual recovery (see Chart 5), lending weight to the belief the current spot price level is becoming attractive to Chinese importers. We thus expect recovery in iron ore cargoes, resulting in Capesize rates turning around and BDI rising, as the segment accounts for about 60% of the index.
- **Resilience in rates for smaller vessels will be sustained** — The freight rate for Handysize vessels is more resilient than the rate of capsize vessels (Chart 4). For instance, from the Jun 09 peak Handysize freight rate corrected by 11% while the Capesize rate corrected 51%. We think one of the reasons for the resilience is the higher cargo movement in the agri-bulk sector as we are in the harvest season, especially in Asia. The recent BDI pullback has less impact on the rates of operators of smaller vessels such as PSL and TTA. We are convinced the continued high traffic of bulk agricultural cargoes will support Handysize rates. The drought in South Asia especially India, which is a substantial grain consuming nation, will result in imports of bulk agricultural items.
- **Reiterate buy PSL and TTA** — As iron ore cargo picks up, BDI could become positive and this would entice investors into the sector. This will be positive for Handysize rates as well. We reiterate our Buy recommendation for PSL with a 12M PT of Bt22 and TTA of Bt31. Since August 21, PSL rose by 11% and TTA by 10%, tracking closely the 7% rebound in the Handysize index. At current levels, PSL and TTA are trading at 7x and 10x FY09E PE and 1.1x and 0.6x PBV, respectively. PSL also offers high yield at 5.7% for FY09.

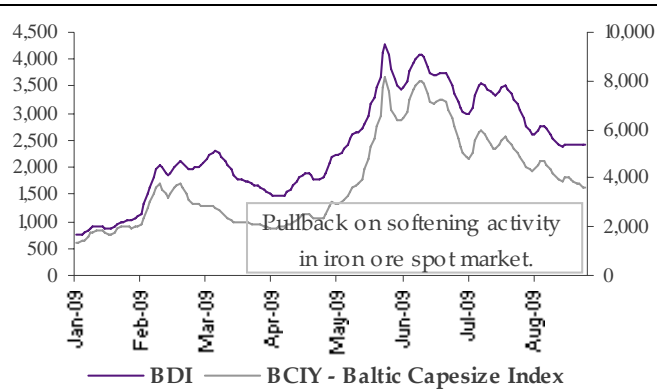
Valuation summary

	Rating	Target (Bt)	Price (Bt)	Expected total return (%)	SCBS PBV			SCBS PBV at TP			SCBS PE		
					08	09F	10F	08	09F	10F	08	09F	10F
PSL	Buy	22	17.9	29	1.2	1.1	1.0	1.4	1.3	1.2	3.8	6.9	8.9
TTA	Buy	31	25	26	0.6	0.6	0.5	0.7	0.7	0.7	1.8	10.3	18.4

Source: SCBS Investment Research

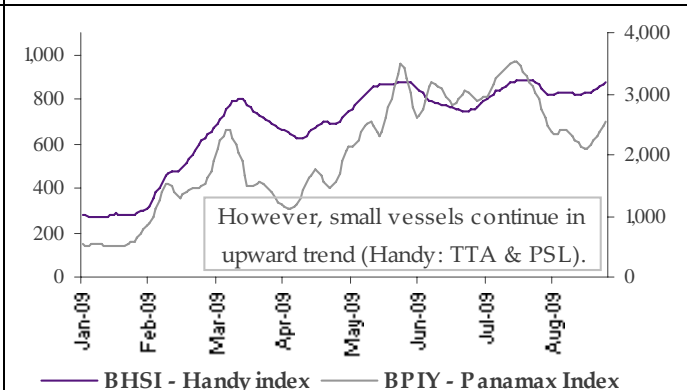
APPENDICES

Chart 1: BDI pullback on correction in the capesize index.



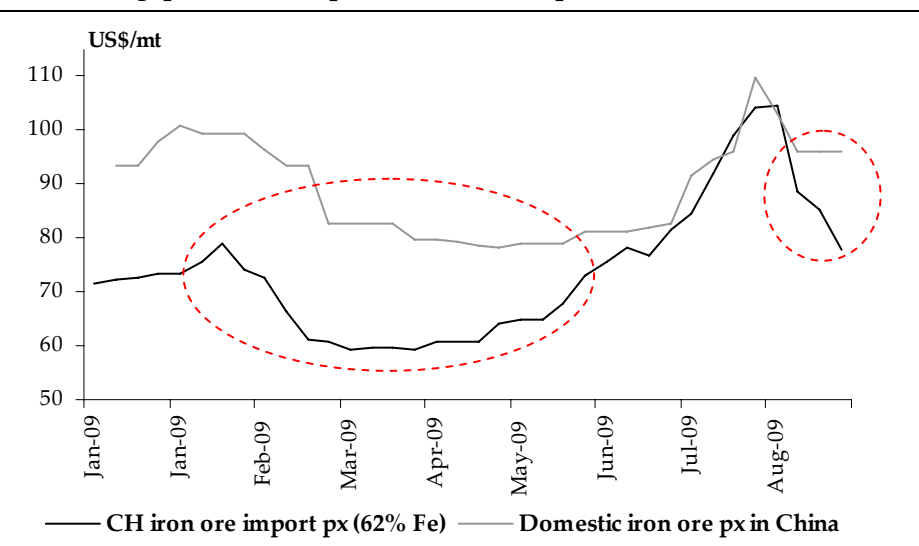
Source: Bloomberg, SCBS Investment Research

Chart 2: ...but small vessel rate continue in upward trend



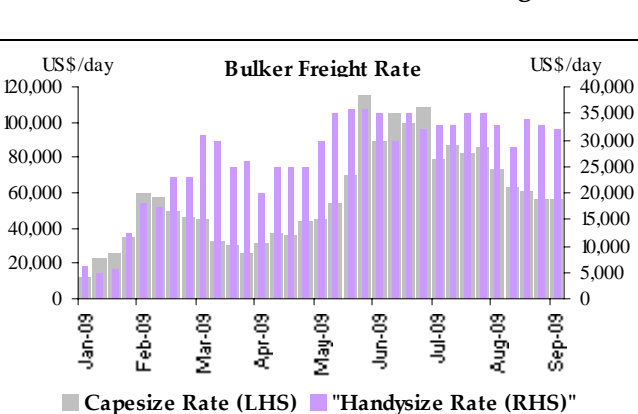
Source: Bloomberg, SCBS Investment Research

Chart 3: Potential restoration in iron ore import activities in China, given the wider gap between import and domestic prices.



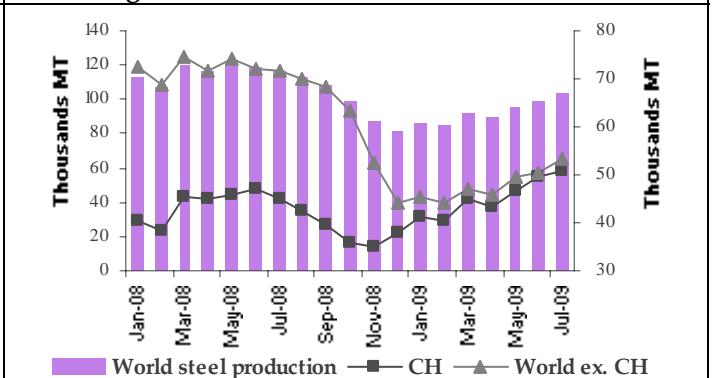
Source: Bloomberg, SCBS Investment Research

Chart 4: Smaller vessel, more resilient freight rate



Source: Fearnleys, SCBS Investment Research

Chart 5: Production of crude steel is gradually recovering



Source: IISI, SCBS Investment Research