



Speaker: David Turnbull

Slide 0 – Cover

Welcome ladies and gentlemen, and thank you for attending Pacific Basin's 2017 Annual Results conference call and live webcast.

My name is David Turnbull, Chairman of Pacific Basin, and I am joined by our CEO Mats Berglund and our CFO Peter Schulz. We are talking to you from our new headquarters on the south side of Hong Kong island where we are benefitting from a better, more energised and collaborative office with a significantly lower rent.

2017 was a much better year for dry bulk shipping compared to an extremely weak 2016.

There is still some way to go before the market sees more sustainable, healthy freight earnings. However, I think it's fair to say dry bulk shipping is largely out of the woods, and we are cautiously optimistic for a continued market recovery.

The stronger freight market and our outperformance of the market in terms of vessel earnings enabled us to generate significantly larger operating cash flows and our first, small positive P&L net result since 2013.

In view of the small US\$3.6 million profit we recorded, the Board recommends not to pay a dividend for 2017. However, we continue to target a pay-out ratio of at least 50% of net profits excluding disposal gains once we return to a more meaningful level of profitability.

Mats will now present our 2017 results and business initiatives, which have enhanced our position to capitalise on opportunities and improving market conditions ahead.

Peter will then talk you through the financials, and I will then invite you to ask questions.

Over to you Mats.

Speaker: Mats Berglund

Slide 2 – 2017 Annual Results Highlights

Good afternoon ladies and gentlemen. Please turn to slide 2.

In better but still challenging trading conditions in 2017, we generated EBITDA of US\$133.8 million and a net profit of US\$3.6 million, representing improvements of US\$111 million and US\$90 million respectively over our 2016 results.

In the first half of the year, we completed our owned vessel newbuilding programme with the delivery of seven newbuildings of modern, efficient designs which we committed to build in 2013.

We recommenced secondhand acquisitions using the still historically low asset values to purchase two high quality secondhand Handysize vessels. We also purchased a secondhand Supramax and sold an older, smaller Supramax, thereby trading up to a vessel of better design and longer life at an attractive price.

In August, we committed to acquire five modern, efficient dry bulk vessels funded mainly by a combination of new Pacific Basin shares issued to the sellers, and cash raised through a share placement. This innovative transaction enabled immediate equity financing and enhances our operating cash flow, EBITDA and balance sheet.

These acquisitions have increased our owned fleet to 106 ships on the water today and grown the proportion of our owned versus chartered ships, especially in Supramax.

With all except one ship paid for and delivered by year end, we had total cash and deposits of US\$245 million at 31 December.

Slide 3 – 2017 Performance & 2018 Cover

Slide 3. Our Handysize and Supramax net daily TCE earnings of US\$8,320 and US\$9,610 increased 25% and 43% year on year respectively, and outperformed the rising Baltic Handysize and Supramax spot market indices by 15% and 8%.

As part of our business model, we supplement our core fleet with ships we charter-in for short periods which we combine with cargoes to typically make a positive margin irrespective of whether the market is high or low.

If we exclude vessel days attributable to this short-term operating activity and factor the positive margin into the TCE results of our core fleet, then our restated 2017 Handysize and Supramax daily earnings would improve to US\$8,410 and US\$10,100 net respectively, although on fewer vessel days.

As at 23 February, we had covered 50% of our Handysize days for 2018 at about US\$9,280 and 69% of our Supramax days at about US\$11,400 per day – well above our owned vessel break-even levels which Peter will summarise shortly.

Slide 5 - Freight Market Continues to Improve

Please turn to slide 5.

Freight market indices in 2017 followed a similar seasonal pattern as in 2016, although at a significantly higher level.

Handysize and Supramax spot market rates averaged about US\$7,300 and US\$8,900 per day net respectively, representing a roughly 50% improvement in average spot market earnings year on year.

As significant as the market improvement was, the dry bulk market overall in 2017 was still in the bottom third of the 33 years since the dry bulk indices began.

2018 is so far following a similar seasonal pattern as the last two years, but as you can see in the graphs, the market again bottomed out at a significantly higher level during the Chinese New Year holiday, which occurred later this year than last. It is also encouraging to see the market turning positive with rates again increasing from last week, already before the holiday period had ended.

Slide 6 – Global Dry Bulk Demand Story

Slide 6. The market improvement last year was largely demand driven with stronger seaborne trade growth apparent across most dry bulk cargo categories.

Stronger Chinese industrial activity drove robust growth in coal and iron ore imports and, more importantly for us, in the trade in minor bulks.

The global trade in agricultural commodities expanded more than expected, primarily due to record South American grain export volumes.

Longer trade distances also supported stronger tonne-mile global seaborne demand which Clarksons Research estimates to have grown 5.1% in 2017.

Steel and cement shipments reduced primarily because of lower exports from China due to increased domestic demand and prices, which indicates how strong the Chinese domestic industrial activity is.

Looking ahead, a positive and widely spread growth outlook for all major economic areas bodes well for dry bulk shipping. Other positive trends include:

- continued strong grain and soybean demand primarily for animal feed as the world's growing middle class shifts to a more meat-based diet; and
- environmental policy in China encouraging a shift from domestic to imported supply of resources.

However, threats include the potential for reduced Chinese coal and ore imports, excessive new ship ordering and higher ship operating speeds.

Slide 7 – Newbuilding Deliveries Continue to Shrink

Slide 7. As expected due to the declining orderbook, newbuilding deliveries in 2017 reduced to about 38 million deadweight tonnes – or 4.7% of existing dry bulk capacity, the lowest level since 2003.

Scrapping reduced to 1.7% of existing capacity due to the much improved freight market conditions.

As a result, overall dry bulk capacity grew 3% in 2017.

New ship ordering in 2017 increased from a very low base in 2016, with most new orders being for larger VLOCs, Capesize and Kamsarmax ships.

Slide 8 – Handysize and Supramax Orderbook at Historically Low Levels

On slide 8, you will see that total dry bulk new ship deliveries in 2017 fell short of scheduled deliveries by 34%, and by 42% in our combined Handysize and Supramax segments.

Looking ahead, newbuilding deliveries are set to continue to shrink.

For 2018, scheduled deliveries are around 37% smaller than scheduled deliveries were for 2017 a year ago, and actual deliveries are expected to be around 26 million deadweight tonnes this year compared to 38 million last year.

In the right hand graph, you'll see that the combined Handysize and Supramax orderbook has reduced to 5.7%, its lowest level since the 1990s, and scheduled deliveries in our segments are significantly smaller than for dry bulk overall.

Slide 9 – Better Fundamentals for Handysize

On slide 9, we contrast in further detail both the orderbook and age profile of the smaller ships with the larger vessels. Handysize benefits from less than half the orderbook and more older ships – almost twice the percentage of ships 20 years or older – pointing to a better balance between new deliveries and scrapping going forward for the smaller ships.

Slide 10 – Favourable Dry Bulk Supply and Demand Outlook

In slide 10, we show Clarkson's yearly demand and supply levels combined in one chart. Tonne-mile demand growth of over 5% clearly outpaced the net supply growth of 3% in 2017.

And for 2018, Clarkson's somewhat slower estimated tonne-mile demand growth of about 3.7% (around world GDP growth levels) is still above the expected net fleet growth of 1.8% overall for dry bulk (which assumes 3.1% deliveries and 1.3% scrapping).

Slide 11 – Improved Outlook Supports Vessel Values

Slide 11. The improved freight market conditions supported sale and purchase activity and increased vessel values in 2017.

Clarksons Research currently values a benchmark five year old Handysize at US\$14 million – up significantly from the lows of 2016.

Newbuilding prices have also increased to US\$22.3 million for a Handysize today – up about 14% since the start of 2017.

The large gap between newbuilding and secondhand prices continues to discourage new ship ordering.

Note that the value of a typical 5-year old ship is still below the low of 2013 and nowhere near the price of a newbuilding which is typically the case in a strong market. Hence, we still see upside in secondhand values, in parallel with a continued gradual freight market recovery.

I will be back shortly with a wrap-up, but now hand you over to Peter who will present the financials.

Speaker: Peter Schulz

Slide 13 – Significant Improvement in 2017 Financial Results

Good afternoon ladies and gentlemen. Please turn to slide 13.

The Group's underlying profit improved to a positive US\$2.2 million in 2017 compared to a loss of US\$87.7 million in 2016.

The improvement in underlying profit was driven by higher TCE earnings benefitting from the significantly better market conditions.

Owned vessel costs and G&A overheads increased in absolute dollars during the year as we added more owned vessels to our fleet, but continued to reduce on a dollar-per-day basis.

Charter costs increased due to the increased cost of chartering in short-term vessels in a rising market.

The profit attributable to shareholders of US\$3.6 million was higher than our underlying profit due to:

- US\$5.4 million of non-cash mark-to-market income mainly on our bunker swaps, off-set by;
- US\$1.4 million from costs related to our head office relocation in Hong Kong and \$2.6 million in impairments and other losses relating to our now discontinued Towage business

Slide 14 – 2017 Improvement in Both Handysize and Supramax

Slide 14. Our Handysize revenue days increased by 12% and our TCE earnings improved by 25% to US\$8,320 per day, outperforming the market by 15% and resulting in a Handysize contribution of US\$31.4 million.

Our Supramax revenue days increased 17% and our TCE earnings improved by 43% to US\$9,610 per day resulting in a Supramax contribution of US\$19.7 million.

The Post Panamax contribution remained stable as the two vessels in this segment are on fixed rate long-term charter-out contracts.

Slide 15 – Handysize – Owned Vessel Costs Reducing

On slide 15, you can see our Handysize owned vessel costs were brought down to US\$7,480 per day, supported mainly by reductions in finance costs and operating expenses.

Our cost of inward chartered Handysize ships increased to US\$7,850 per day as the freight market improved.

The break-out table shows our chartered vessels daily cost split between short-term, long-term and index charters.

Our overall daily G&A overheads reduced by 9% to US\$600 per ship per day (for both our Handysize and Supramax ships) reflecting efficiencies and the increase in our vessel days in 2017.

Slide 16 – Supramax – More Owned Ships with Lower Daily Cost

Slide 16. Our acquisitions of Supramax vessels increased our owned Supramax vessel days by 28% to 7,800 days and reduced our owned vessel daily costs by US\$380 per day, mainly due to lower operating expenses and depreciation.

Our cost of inward chartered Supramax ships increased to US\$9,240 per day, again reflecting the improvement in the freight market.

Slide 17 – Competitive Owned Vessel Break-Even Levels

Slide 17 shows the current break-even level on our owned Handysize and Supramax ships of approximately US\$8,300 and US\$9,100 per day respectively including G&A overheads. We allocate \$840 in G&A overheads per day on our owned vessels.

Comparing these levels to our TCE earnings actually achieved in 2017, you can see that we were just above break-even for last year, while our covered rates so far in 2018 are well into profitable territory.

Slide 18 – Strong Balance Sheet and Liquidity

Slide 18. At the year-end we had vessel and other fixed assets of US\$1.8 billion, consisting of 80 Handysize vessels with an average book value of US\$15.3 million and an average age of 9.3 years, and 25 Supramax vessels with an average book value of US\$21.9m and an average age of 6.1 years.

Our vessels were financed by US\$881 million of interest bearing liabilities. Cash and deposits stood at US\$245 million, giving a net borrowings position of US\$636 million.

Our net gearing was 35% in relation to the net book value of our owned vessels.

We maintain as a KPI that net gearing should remain below 50%.

Slide 19 – No Newbuilding Capex

Slide 19. In 2017, the Group generated operating cash flows of US\$125 million and cash proceeds of US\$10 million from the sale of four towage vessels and one dry bulk vessel.

The share placement proceeds for the purchase of five vessels generated US\$38 million net.

We fully drew on all our committed facilities during the year which, net of scheduled amortisation, increased our borrowings by US\$52 million.

Capex of US\$220 million during the year included cash payments for both newbuildings and secondhand vessels. A total of 14 vessels were added to our fleet in 2017, and one older vessel was sold.

The scheduled vessel capital commitments of US\$21 million for 2018 represent one Supramax vessel, which delivered into our fleet in January 2018. After paying for this vessel, we have no more committed secondhand or newbuilding capex ahead.

In addition to our cash balances, after taking delivery and paying for the ship in January, we have 10 unmortgaged ships with a total market value of about US\$173 million.

I'll now hand you back to Mats for his wrap-up.

Speaker: Mats Berglund

Slide 21 – Our Business Model Continues to Outperform

To wrap up, I will start with a brief recap on slide 21 of our business model and the factors that enable us to outperform index rates. This is a strong platform and worthwhile emphasising.

Unlike the Capesize and Panamax segments, our Handysize and Supramax segments benefit from diverse cargoes, customers and trading geography.

These trades are operationally intense, and having skilled and experienced staff, a global office network and a large quality fleet of efficient, interchangeable ships really makes a difference.

Drawing on all these components of our business model, which we have developed and refined over many years, we typically achieve a laden versus ballast ratio of over 90%.

This is key to our generating an average Handysize and Supramax TCE premium of more than US\$1,800 and US\$1,200 per day respectively over index rates in the past five years.

Slide 22 – Well Positioned for a Recovering Market

Slide 22. We have worked very hard over several years to position ourselves well for a recovering market. We are out of all non-core businesses and have instead grown our core dry bulk fleet from 34 ships in 2012 to 106 ships today. Importantly the ships are all suitable for our trades, good quality and predominantly Japanese built.

We have also worked very hard to streamline our organisation and our cost structure. Primarily through scale benefits and other efficiencies, we have gradually reduced our daily vessel operating expenses by 12% from US\$4,370 in 2014 to US\$3,840 in 2017, without compromising safety or maintenance.

During the same period we have reduced our total G&A overheads by 28% from US\$76 million to US\$54 million despite operating a much larger owned fleet.

With our outperforming business model, including experienced staff, a much larger owned fleet and competitive cost structure, we are well positioned for a recovering market.

Being focused only on our core business, it is easier to run numbers on our business today. Based on our current fleet and commitments, a change of US\$1,000 per day in annual average TCE market rates would be expected to change our net results by about US\$35-40 million per year.

Slide 23 – New Regulations

Slide 23. There are two new regulations coming to our industry. The first requires the installation of Ballast Water Treatment Systems, and we are planning to start installing systems late this year and then gradually ship by ship over a five year period through 2023. More systems are being approved by the US Coast Guard and we do not foresee any further changes or controversy regarding this regulation.

The larger uncertainty and impact on the industry is around how to comply with the second new regulation – the Global Sulphur Cap coming into force in January 2020. To comply with the 0.5% sulphur emissions limit, shipowners can either burn more expensive low sulphur fuel, or install exhaust gas cleaning systems (so called “scrubbers”) and continue to burn the cheaper high sulphur fuel.

We do not think that sulphur scrubbers are an effective solution either technically or environmentally. There are also too many uncertainties over the price and availability of fuels, waste water management, potential transition periods before you can practically comply, etc. making a scrubber investment very difficult. We much prefer a mandate to use low sulphur fuel and the level playing field, lower speeds and lower emissions (including CO₂) this would support.

Whichever way the industry goes on this, we think the effect will be positive as the cost of complying with the new regulations will penalise poor performing and older ships while benefitting stronger companies with high quality fleets, like ours, that are better positioned to adapt and cope both practically and financially with compliance.

Slide 24 – We Will Not Order More Newbuildings Today

Please turn to slide 24. We do not intend to order newbuildings in the medium term, and will watch technological and regulatory developments closely. There remains extra capacity in the existing global fleet through potentially higher operating speed, and the market does not need more newbuildings.

What we shipowners need is a more reasonable level of profitability.

Moreover, today’s newbuildings offer only limited efficiency benefits over good quality Japanese-built secondhand ships and, in our view, the risk and payback time for newbuildings is currently excessive due to several uncertainties in our market, including those I just mentioned about how to comply with new environmental regulations.

Other uncertainties include:

- potential additional new regulations regarding, for example, NOx and CO₂ emissions; and
- faster and potentially more significant technological developments in the longer term.

These uncertainties, the attraction of low secondhand prices, and new accounting rules requiring time charters to be capitalised from 2019 are discouraging new ship ordering in our segment.

Slide 25 – Our Outlook and Strategy

Slide 25. The general market improvement since early 2016 is encouraging and, with supply and demand fundamentals now more positive, we are cautiously optimistic for a continued market recovery, although with some volatility along the way.

A positive global economic and commodity demand outlook and lower newbuilding deliveries, especially in our segment, bode well for the market in the medium term. Supply is expected to be kept in check by the continued gap between newbuilding and secondhand prices and the uncertain impact of new regulations.

Potential negative factors include a possible reduction in China’s industrial growth or its difficult-to-predict coal imports and, on the supply side, the risk of excessive new ordering and, importantly, increased ship operating speeds.

We will continue to focus on our world-leading Handysize and Supramax dry bulk business where our strategy is to be the best operator, maximising our fleet’s utilisation and TCE earnings by leveraging all the key attributes of our business model, such as our large fleet of interchangeable ships and worldwide office network.

We do not intend to order newbuildings for now, but we will continue to look at good quality secondhand ship acquisition opportunities as prices are still historically low, resulting in reasonable break-even levels and shorter payback times.

Our healthy cash and net gearing positions enhance our ability to take advantage of opportunities to grow our business and fleet, and attract cargo as a strong partner, all of which positions us well for a continued market recovery.

Thank you for joining us today, and thank you for your continued support.

Speaker: David Turnbull

Thank you Mats.

Ladies and gentlemen, that concludes the results presentation. Lines will now be open for any questions you may have.