3Q23 Quarterly Trading Update
Presentation Transcript

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Slide 1 – Introduction

Welcome ladies and gentlemen and thank you for attending Pacific Basin's Third Quarter Trading Update call. My name is Martin Fruergaard, CEO of Pacific Basin, and I am pleased to have our CFO Michael Jorgensen with me today.

Assuming that you have already gone through the presentation, I will briefly highlight some of the key points discussed in it before we proceed with the Q&A session.

Please turn to slide 3.

Slide 3 – Strong Seasonal Recovery Freight Rates During September

During the third quarter of 2023, there was a seasonal improvement in market freight rates for Handysize and Supramax. Rates increased strongly from the middle of August and continued through September, ending the period at US$10,558 and US$13,339 net per day for Handysize and Supramax respectively.

The primary reasons for this being the East Coast South America grain season, specifically in Brazil, which led to a significant increase in grain exports, coupled with higher seasonal dry bulk demand.

This improvement in sentiment and demand was seen across all dry bulk segments which has supported significantly improving rates despite decelerating global growth, higher interest rates, and increased vessel supply.

Market spot rates for Handysize and Supramax vessels averaged US$7,660 and US$9,530 net per day respectively in the third quarter of 2023.

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Slide 4 – Record Total Dry Bulk Loadings – Supported By China Reopening

Minor bulk loadings in the third quarter were approximately 2% higher, due to increased loadings of steel, aggregates and bauxite. While forest products, cement and clinker and alumina were the largest detractors. According to the latest available Chinese National Statistics data, Chinese steel production and exports have increased 3% and 27% year-to-date August respectively.

Iron ore loadings increased 2% in the third quarter due to higher production in both Australia and Brazil. There was growing demand for steel across multiple sectors, including motor vehicle manufacturing, shipbuilding, infrastructure development, and power generation. Despite earlier predictions that Chinese steel production would remain stagnant due to stricter environmental regulations and limited investment in steelmaking capacity, China has seen a 3% increase in steel production and a 27% increase in steel exports in the year leading up to August.

In the third quarter of 2023, global **grain** loadings experienced a 5% decline compared to the same period in 2022. This decrease can be attributed to lower loadings from Argentina and the United States, as well as the Black Sea grain deal cancellation in July, which limited Ukraine's exports. However, Brazil emerged as a major contributor to grain loadings in the third quarter, loading an impressive 47.3 million tonnes of grains over three months, representing a significant increase of 19% compared to the same period in 2022.

A 1% decrease in global **coal** loadings in the third quarter of 2023 is attributed to a slowing of Indian imports. In contrast China has been facing low hydroelectric and energy security consumption concerns, despite record domestic coal production. As a result, China has needed to maintain high levels of coal imports during the third quarter.

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Slide 5 – Strong Seasonal Freight Rates Support 4Q23 And 1Q23 Earnings

Our **core** business generated average Handysize and Supramax daily TCE earnings of US$10,200 and US$11,540 net per day respectively in the third quarter of 2023, representing a decrease of 57% and 57% respectively compared to the much stronger third quarter of 2022.

For the fourth quarter of 2023 we have covered 70% and 86% of our core committed vessel days at US$11,250 and US$13,240 net per day for Handysize and Supramax respectively. Our P&L break-even (including General and Administrative Overheads) was US$9,600 and US$11,190 per day for Handysize and Supramax respectively in the first half of 2023.

For the full year 2024 we currently have cover for 22% and 25% of our core vessel days at US$8,590 and US$13,720 net per day for Handysize and Supramax respectively. Supramax cover rates exclude any scrubber benefit, currently about US$330 per day across our entire core Supramax fleet.

We are currently focused on optimising our short-term cover to maximise earnings over the first quarter of 2024, which is commonly a softer market during the northern hemisphere winter and Lunar New Year periods. For the first quarter of 2024 we have covered 29% and 33% of our core committed vessel days at US$9,470 and US$13,290 net per day for Handysize and Supramax respectively.

Forward Freight Agreements commonly referred to as FFA’s, are for the fourth quarter of 2023, at US$12,250 and US$13,510 per day for Handysize and Supramax respectively.

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Slide 6 – We Continue to Outperform And Maximise Operating Activity Earnings

Our Handysize and Supramax TCE earnings outperformed the spot market indices by US$2,540 per day and US$2,010 per day respectively in the quarter. Our Supramax outperformance continues to benefit from the 33 scrubbers installed across our owned fleet, with scrubbers contributing US$450 per day to our outperformance over the period.

Current value of Supramax scrubber benefits is approximately US$330 per day across our entire core Supramax fleet

Our **operating** activity also contributed positively, generating a positive margin of US$1,160 net per day over 6,810 operating days in the third quarter. Our third quarter operating days increased by 42% compared to the same period last year, and we currently have approximately 145 short-term chartered Handysize and Supramax vessels servicing customers.

Our operating activity provides us with an ongoing opportunity to leverage Pacific Basin's commercial and operational expertise, as well as our global proximity to our customers, to generate additional income for the business.

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Slide 7 – Counter Cyclical Growth While Renewing Our Fleet

During the third quarter of 2023, we sold three of our smaller, older Handysize vessels and one older Supramax vessel. This year, we have sold a total of six vessels, including five Handysize and one Supramax vessel, with an average age of 19 years. In light of existing and incoming decarbonisation regulations, we forsee older and less efficient vessels will become increasingly challenging to operate. Therefore, we gradually wish to divest ourselves of our least efficient vessels.

We believe asset prices for new and modern second-hand vessels will remain elevated due to increased newbuilding input costs and limited yard capacity.

To support the growth and renewal of our core fleet, we have entered agreements for the long-term inward charter of Handysize and Ultramax vessels. In July, we took delivery of a 40 thousand deadweight tonne Handysize, built in Japan, with two more scheduled to be delivered in November and December 2023.

In addition, four additional 40 thousand deadweight tonne Japanese built Handysize newbuildings, all with scrubbers, will be delivered by the first quarter of 2025.

As well as three newbuilding Ultramax vessels, with one scheduled to be delivered in 2024 and two in 2025. Furthermore, each of these timecharters comes with an option to extend the charter agreement at the fixed rate, and we have the option to purchase the vessels at a fixed price, which further expands our optionality.

Including all currently agreed sales and purchases, our Core fleet consists of 135 Handysize and Supramax vessels and, including chartered vessels in our Operating business, we currently have approximately 280 vessels on the water overall.

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Slide 9 – China Reopening Supporting Dry Bulk Demand

Despite the negative commentary surrounding China's post-Covid economic recovery, we see positive demand for commodities, which is supporting dry bulk demand through investments in infrastructure, manufacturing, commercial and industrial property construction and green transition initiatives.

While reduced construction of new domestic housing in China is still having a significant negative impact on the country's economic growth and to the demand for some minor bulk commodities. It is worth noting that new policy support is continuing to be implemented to further encourage domestic property construction and increase investment in infrastructure. This suggests that the Chinese government is taking proactive measures to improve economic growth.

China's import of coal as I have mentioned earlier, in combination with imports of iron ore, bauxite and other minor bulk commodities, as well as export of steel products, has been a significant supporter of the market.

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Slide 10 – Expect Increased Scrapping Due To Environmental Regulations

In the third quarter, there was an increase in the number of vessels scrapped, with a total of 2.3 million dead weight tonnes scrapped, contributing to a total of 4.9 million dead weight tonnes scrapped in the year so far.

As of the year-to-date 2023, there has been a significant increase in scrapping of both Handysize and Supramax vessels compared to last year. While scrapping levels have been relatively low, we expect an increase in scrapping as environmental regulations make it more difficult for older, less efficient vessels to compete and comply.

The average age of Handysize and Supramax vessels scrapped between 2019 and 2023 is over 30 years and could help to explain partly why we have seen only limited scrapping year to date despite the lower TCE rate environment. Clarksons Research reports that minor bulk vessels of over 25 years old, which are potential scrapping candidates, make up approximately 8% and 4% of the global Handysize and Supramax fleets respectively.

In regards to Handysize and Supramax vessels, Clarksons Research forecasts scrapping of 0.7% for the full year 2023, before increasing to 1.3% in 2024.

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Slide 11 – Limited Handysize And Supramax Newbuilding Deliveries From 2026

Newbuild ordering in dry bulk continues to be constrained with a near decades low of 8.1% of total fleet on order. In comparison to 2022, newbuild ordering of Handysize and Supramax vessels decreased approximately 30% year-to-date and 64% in the third quarter of 2023.

Dry bulk shipyard slots remain limited, resulting in a new order placed today unlikely to be delivered before 2027. With the majority of incremental new shipyard capacity concentrated on non-dry bulk vessels.

This provides us visibility on new vessel supply with 2024 being the peak for Handysize and Supramax vessel deliveries. While vessel deliveries can be delayed, it is difficult for the 2026 delivery forecast to be meaningfully increased.

We continue to believe that the high cost of newbuildings, uncertainty over new environmental regulations and the higher interest rate environment will continue to discourage any significant new dry bulk vessel ordering.

Continued low ordering, efforts to reduce carbon intensity and increased scrapping in the coming few years, could create a shortage of vessels and provide long-term structural undersupply to the market.

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Slide 12 – Regulatory Snowball Effect Will Put Significant Pressure On Conventional Vessels

It is our belief that as the implementation of decarbonisation policies continues, conventional vessels will face increasing pressure to comply. In our previous results call, we noted that the IMO in July, adopted a more ambitious greenhouse gas strategy, with the goal of achieving net-zero emissions for international shipping by approximately 2050. While we continue to be focused on optimising our fleet for compliance with these regulations, we would also like to mention the European Union Emissions Trading System (EU ETS), which is set to be implemented on January 1st, 2024.

This regulation will require shipping companies that emit carbon to buy and surrender EU Allowances for carbon emissions from voyages to, from and within the EU. With these carbon allowances currently costing approximately €80-100 per tonne.

This entails a three-year phase-in period, increasing in scope from 40% of emissions in 2024 to 70% in 2025 and 100% in 2026. This incremental cost will be included in our freight costs which will be covered by customers.

We expect that this regulation will also drive a faster pace of decarbonisation, with the near-term impact being that vessels speeds will reduce over time to limit carbon emissions and the associated cost of EU carbon emission allowances – with the benefit of lower vessel supply.

We expect that further decarbonisation regulations such as Fuel EU, US Clean Shipping Act, International Marine Pollution Accountability Act and an IMO carbon pricing measure will slow global average vessel speeds, increase scrapping and limit the appeal of conventionally-fuelled newbuilding vessels and further incentivise vessel owners over time to transition to green fuels.

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Slide 16 – We Remain Optimistic About The Supportive Fundamentals Of Our Industry

In the short term, we expect coal and grain to continue to support dry bulk demand for the remainder of the year due to seasonality, changes in trade flows and global issues of food and energy security.

In the longer term, we continue to believe that the high cost of newbuildings, uncertainty over new environmental regulations and the higher interest rate environment will continue to discourage any significant new dry bulk vessel ordering. The low orderbook and efforts to reduce carbon intensity will likely lead to lower speeds and increased scrapping in the coming few years, which could create a shortage of vessels and provide long-term structural undersupply to the market.

We are excited about the long-term prospects of dry bulk shipping given dry bulk demand which remains supported by strong supply side fundamentals and ongoing implementation of existing and new decarbonisation rules. We are optimistic about the future of the dry bulk market, and anticipate underlying demand and supply fundamentals will allow us to generate steadier and more sustainable earnings over the long-term.

Ladies and gentlemen, that concludes our Third Quarter Trading Update presentation.

I will now hand over the call to our operator for Q&A.

[Q&A]

I'd like to thank you again for joining us today and for your continued support of Pacific Basin. If you have any further questions, please contact Peter Budd from our Investor Relations department.