Pacific Basin

2020 Annual Results Presentation Transcript

25 February 2021

Speaker: Mats Berglund

Slides 1-2 – Introduction

Welcome ladies and gentlemen, and thank you for attending Pacific Basin's 2020 Annual Results earnings call. My name is Mats Berglund, CEO of Pacific Basin, and I am joined by our CFO Peter Schulz.

Please turn to slide 3.

Slide 3 – A Remarkable Recovery

This is a 2020 results presentation but, as you can imagine, it's a lot more fun to talk about 2021, and you can understand why when looking at the graphs on this slide. We will get back to this later.

2020 was a year of two very different halves for dry bulk shipping. Measures to contain the Covid outbreak initially in China and then elsewhere around the world severely impacted the dry bulk market in the first half, driving Handysize and Supramax index rates down to their lowest second-quarter average in 50 years.

However, dry bulk demand and freight earnings started to improve significantly from May 2020 and have continued to strengthen into 2021. Handysize and Supramax market freight rates have quadrupled since May to 10-year highs.

While the recent very sharp increase in spot rates is not expected to continue going up, it does demonstrate that demand and supply is finely balanced and, when the current extreme tightness eases, we believe that rates will settle at substantially higher levels than in recent years.

A vaccine and stimulus-powered strengthening of economic activity coupled with reducing dry bulk fleet growth make us optimistic about the freight market in 2021 and the years ahead.

Slide 4 – 2020 was A Year of Two Halves

Please turn to slide 4. We delivered a positive EBITDA of US$184.7 million and an underlying loss of US$19.4 million in 2020.

Our TCE earnings were below break-even in the first half of the year resulting in an underlying loss for the period. Our net profit was further impacted by a non-cash US$198 million impairment of our Handysize core fleet, primarily our smallest and oldest Handysize vessels. Our TCE earnings recovered in the second half of the year resulting in an underlying profit of US$7.2 million for the period.

We also improved our available liquidity to US$362.5 million and net gearing reduced to 37% from 41% in June.

Slide 5 – Continued Strong Outperformance

Slide 5. Our <u>core fleet</u> generated average Handysize and Supramax daily TCE earnings of US$7,860 and US$11,140 net per day. While down 18% and 5% year on year, these TCE earnings outperformed the Handysize and Supramax spot market indices by US$1,140 and US$3,360 respectively in the year.

Our outperformance narrowed in the second half, which is typical in a rising freight market due to the effect of existing cargo contracts committed earlier at lower levels and the lag between spot market fixtures and execution of voyages.

Our Supramax outperformance was particularly strong due to our successful management of our scrubber-fitted ships and the bunker price spread that was especially wide early in the year. So far, we have recovered 44% of our original scrubber investment including realised bunker price spread hedges.

Our Supramax outperformance also benefited from a relatively stronger Atlantic market where the majority of our Supramaxes are trading.

Our <u>operating activity</u> generated a healthy margin of US$1,080 net per day over 15,500 operating days in the year.

Slide 6 – Positive TCE Trend Continues

Slide 6 shows the positive development of market rates and our earnings from loss-making levels in the first half of 2020 to breakeven levels in the third quarter and into profitable levels in the fourth quarter and more substantial profitability in early 2021. The dotted line across the chart illustrates the indicative breakeven level after G&A on our core fleet.

We have currently covered 94% and 100% of our Handysize and Supramax vessel days for the first quarter of 2021 at US$10,150 and US$13,380 per day net respectively.

The red bars show last night's Handysize and Supramax index rates to give you a sense of the current very attractive spot market levels.

Slide 7 – Market Rates at 10-Year Highs

Please turn to slide 7.

The solid blue lines represent 2020 and note the recovery in market freight rates over the last 7 months of last year. The red lines show the remarkable and unseasonal further strengthening in 2021 to date.

Handysize and Supramax rates have quadrupled since May 2020 to 10-year highs.

The recovery is driven by:

1. strong Chinese dry bulk imports which grew 8% year on year overall in spite of the pandemic;
2. global shipments of grain which grew by more than 8%;
3. recovering demand for Asian coal (Indian coal in particular) and construction material; and
4. unlike the fourth quarters of 2018 and 2019 that were negatively impacted by US tariffs and swine fever in China, US grain exports (including to China) were very strong in the fourth quarter. This has continued into 2021 and is partly why Atlantic rates are significantly above Pacific rates.

Recent market strength has also been supported by slowing net fleet growth since the second half of 2020 and fleet inefficiencies due to Covid quarantines, trade tensions and a fleet imbalance between the Atlantic and Pacific basins.

Slide 8 – Significant Leverage from Our Larger Owned Fleet

Please turn to slide 8.

In view of the generally much improved conditions and outlook, we resumed our strategy to grow and renew our owned fleet with the acquisition in November of four high-quality 2015-built Ultramax ships, followed by another second-hand Ultramax early this month. On the back of the improving freight market, asset values have rebounded by around 15% since the lows of last year, so we consider our five recent Ultramax acquisitions to have been well timed.

We have grown our owned fleet significantly in recent years. In particular, we have grown our Supramax fleet with the acquisition of Ultramax vessels, and we continue to sell our smaller, older Handysize vessels to trade up to newer Handysizes with larger carrying capacity. Supramax and Ultramax vessels offer a larger earnings upside in strong markets and this, combined with our overall fleet growth, gives us really good leverage to the market improvement we are currently seeing.

Slide 9 – All Commodity Groups were Up in December YOY, Strong Start to 2021

On slide 9, we show indicative cargo loading data for each of the main dry bulk cargo sectors, which supports some of the points I made in slide 7 about drivers of the recovery.

Grain volumes grew strongest at over 8% compared to 2019, as people and animals need to eat in spite of the pandemic.

Minor bulks were down 2% compared to 2019 due primarily to weak demand for construction materials in the first half, but loadings have recovered strongly since June.

Healthy iron ore volumes out of Brazil and Australia drove a 3% increase in ore shipments year on year, driven by strong Chinese economic activity and domestic steel production.

Coal was the weakest performer in 2020, affected by lower energy consumption due to the pandemic, but coal volumes – Indian coal in particular – have gradually recovered since July.

All four commodity groups were up year on year in December, and our two key cargoes, minor bulks and grain, have started 2021 strongly.

Slide 10 – Dry Bulk Orderbook is at a Multi-Decade Low and is Set to Decline Further

Slide 10. New ship ordering in 2020 remained concentrated in the Panamax and Capesize segments but was significantly lower than in recent years.

The overall dry bulk orderbook at 5.7% of the existing fleet is now the smallest it has been in decades, which means continued support from fundamentals in the next few years.

The combined Handysize and Supramax orderbook is even lower at 4.6%.

Slide 11 – Supply Growth is Expected to Slow

Please turn to slide 11.

Scheduled newbuilding deliveries for 2021 are 30% lower compared to actual deliveries in 2020.

We expect new ship ordering to remain muted despite stronger freight rates, discouraged primarily by the uncertainty around environmental regulations and future technology. And our segments continue to benefit from lower fleet growth than larger vessels.

Slide 12 – Significantly Improving Demand / Supply Balance

Slide 12. IMF projects global GDP to rebound from a 3.5% contraction last year to growth of 5.5% in 2021.

And Clarksons estimates minor bulk demand to rebound from a 1.5% contraction last year to growth of 4.9% in 2021 and 3.7% in 2022, while the combined Handysize and Supramax fleet is expected to grow by only 1.8% in 2021 and 0.4% in 2022.

This tighter supply and demand balance is already benefiting the dry bulk market.

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

Speaker: Peter Schulz

Slide 13-14 – Weak First Half of 2020 and Fleet Impairment Negatively Impacted our Annual Results

Thank you very much Mats. Good afternoon ladies and gentlemen. Please turn to slide 14.

The weak freight market in the first half of the year coupled with the Handysize fleet impairment in June negatively impacted our annual results in 2020.

However, the performance in the second half of the year was considerably stronger and in this period we returned to positive underlying and net profits.

Opex and G&A were very well controlled in 2020 and Handysize depreciation reduced in the second half due to the effect of the impairment.

Since the Group posted a loss for the full year, the Board has decided not to declare any dividend.

Slide 15 – Supramax Outperformed in 2020

Slide 15. Our core Handysize fleet posted a negative annual contribution in 2020, albeit with the second half of the year showing a significant improvement over the first half as rates recovered.

However, our core Supramax fleet, boosted by the scrubbers on 28 of our vessels and our higher share of vessels in the Atlantic, achieved almost US$2,000 per vessel per day profit yielding an overall positive Supramax contribution of US$25 million in 2020. This is an extraordinary result in what was generally a very weak dry bulk year and validates the investments we have made in growing our Supramax fleet in recent years.

Our Operating activity contribution was a strong US$17 million or $1,080 per day – a continued improvement over recent years.

Slide 16 – Handysize – Costs Well Controlled

Please turn to slide 16. Our Handysize core business costs are well controlled and blended costs reduced by US$370 per day or 5%.

Our owned vessel costs reduced by US$270 per day mainly due to lower depreciation from the mid-year impairment, while opex was well controlled and remained the same as 2019.

The cost per day of the long-term chartered ships also reduced as legacy contracts expire and we replace them with primarily owned ships at lower breakeven levels and with short and medium-term chartered-in ships.

Slide 17 – Supramax – Blended Costs Reducing and LT Charters Redeliver

Slide 17. The overall blended cost per day of our core business Supramaxes reduced year on year as the daily long term charter costs decreased in 2020 as we redelivered more expensive chartered ships.

Our Supramax owned vessel daily costs increased by US$240 per day mainly because a large proportion of the Supramax fleet trades in the Atlantic and costs increased due to more expensive crew changes and spares deliveries from Asia. Finance cost per day also increased slightly partly due to a cost reallocation between our Handysize and Supramax fleets following the Handysize impairment.

Slide 18 – Cash Inflow and Outflow in 2020

Please turn to slide 18.

The operating cash flow for 2020 was US$181.5 million, inclusive of all long and short-term charter hire payments. Despite lower TCE rates this was higher than 2019 due to positive movements in working capital.

Our borrowings decreased due to net repayments of US$178 million offset by drawing down US$166 million on committed facilities.

Capex consisted of US$38 million paid for three vessels delivered in the first half of 2020 and US$65 million in dry dockings, scrubbers and ballast water treatment systems. We docked some 32 vessels in the year.

Including the net interests and the dividend payment in May 2020, our cash position increased to US$235 million at the end of the year. In addition, we have US$128 million of undrawn committed facilities.

Slide 19 – Strong Balance Sheet – Headroom to Grow

Slide 19. We ended 2020 with a strong balance sheet as evidenced by the US$362.5 million of cash and committed liquidity as well as lower net debt compared to the beginning of the year – and this despite the market volatility.

We achieved this through careful managing of our liquid resources and the leveraging of our sector-leading access to funding. During the year, we raised a total of US$63 million in new secured borrowings from banks and owners and renewed our US$50 million unsecured 364-day facility at very competitive cost.

We have the capital resources to continue our strategy of growing and renewing our fleet when we see attractive opportunities.

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

Speaker: Mats Berglund

Slide 20-21 – Our Strategic Direction and Priorities

Please turn to slide 21.

We are continuing to develop our somewhat unique business model of having both a core, asset heavy model with owned and in-house managed ships and an asset light model where we use short-term chartered-in ships to provide a service to our customers while making a margin – important especially in weaker markets. But in rising and strong markets that we are currently enjoying, it is of course our now much larger core fleet that is the engine and provides the leverage and profitability.

We continue to assess opportunities to acquire second-hand vessels at attractive prices, and our plan is to continue to grow primarily our owned Supramax fleet, while in Handysize we continue to sell our smaller, older vessels and trade up to newer Handysizes with larger carrying capacity.

Like most other shipowners, we are not contracting newbuildings with existing technology as second-hand ships yield higher returns, and because of the uncertainty over new regulations and technology. We will wait until low-emission ships become technically and commercially viable.

We are investing in further optimisation, systems and process improvement on our ships and in our offices.

Slide 22 – We Are On Track to Meet Our Carbon Intensity Targets

Please turn to slide 22. Our owned fleet's carbon intensity continues to reduce and is on course to meeting our IMO-aligned target of a 40% improvement by 2030.

Customers prefer freight partners who own and operate their own fleets and, while always focusing on safety, we are progressing our decarbonisation initiatives, including:

1. maintaining our high laden-to-ballast ratio;
2. continuing to modernise our fleet by gradually trading up to younger, larger, more energy-efficient ships; and
3. investing in fuel-efficiency technologies and operating practices such as slow steaming, engine tuning, weather routing technologies, trim and draft optimisation and many other optimisation initiatives.

We are also neutralising our carbon emissions from our global shore-side activities by carbon offsetting.

We have an outstanding technical team and are actively involved in the industry-wide discussion about how shipping will decarbonise and meet the IMO's longer-term goals.

There is no doubt in our minds that IMO's decarbonisation rules will lead to lower speeds supporting the demand/supply balance.

And it is comforting to know that, as the world decarbonises, we will continue to carry the non-fossil fuel commodities that will be the mainstay of future trade

Slide 23 – Well Positioned for the Future

Wrapping up on slide 23.

Although some Covid-related uncertainty remains, the demand outlook is positive with vaccines and economic stimulus expected to lead the demand recovery.

The dry bulk orderbook is now the smallest it has been in decades and fleet growth is expected to slow further because of the effect of environmental regulations on new ship ordering and on vessel operating speeds.

All this presents real potential for a continued beneficial demand/supply balance in the next few years, from which we are very well positioned to benefit.

I'll finish up with a reminder that our now much larger owned fleet has largely fixed costs, and change in freight rates will directly impact the underlying profit. We say that for each US$1,000 change in daily TCE, the underlying profit and operating cash flow of the Group will change between US$35-40 million.

I really encourage you to do the math with the strong rates we are seeing. But remember the lag between fixing ships in the spot market and the execution of voyages. It takes a few months before the current strong rates show up in our P&L.

Before we move on to questions, I would like to mention that this is my last annual results presentation with Pacific Basin. As announced in January, I have decided to retire at the end of July and return to my native Sweden. I am very proud of the way we as a team have developed and positioned our business during my nine-year tenure as CEO, and it has been an honour serving with the Company over this period.

I do look forward to speak to you again at the 2021 interim results announcement in July. I think it will be an exciting interim report, and we will then also introduce you to my successor Martin Fruergaard who I am confident will be an excellent new CEO for Pacific Basin.

Ladies and gentlemen, I will now hand over to the operator who will open the lines for any questions you may have. Operator, over to you.

[Q&A]

I'd like to thank you again for joining us today and for your continued support of Pacific Basin.