Pacific Basin

2022 Interim Results Presentation Transcript

28 July 2022

Speaker: Martin Fruergaard

Slide 1 – Introduction

Welcome ladies and gentlemen and thank you for attending Pacific Basin's 2022 Interim Results earnings call. My name is Martin Fruergaard, CEO of Pacific Basin, and I am joined on the line by our CFO, Peter Schulz

Please turn to slide 3.

Slide 3 – OUR BEST INTERIM RESULTS EVER

In the first half of 2022, we generated our best interim results ever, producing an underlying profit of US$457.5 million, a net profit of US$465.1 million and an EBITDA of US$566.9 million. This yielded an exceptionally strong return on equity of 48%, with basic EPS of HK74.5 cents.

Our financial position continues to strengthen with available committed liquidity of US$698.6 million and a net cash position of US$68.9 million as at 30 June 2022.

In light of the strong earnings, cash position and our confidence in the longer-term outlook for minor bulk shipping, the Board has declared an interim basic dividend of HK35 cents per share, representing 50% of our net profit for the period, and an additional special dividend of HK17 cents per share, representing 25% of our net profit for the period.

The basic dividend and the special dividend together amount to a total of HK52 cents per share – equal to US$348.0 million or 75% of net profit

Please turn to slide 4.

Slide 4 – THE MINOR BULK MARKET REMAINS FIRM

The charts show how positively Handysize and Supramax spot rates have developed over the period. Minor bulk freight demand was the main supporter of rates in the year to date.

Freight rates saw a typical seasonal decline leading up to Chinese New Year, but otherwise remained firm over the period at higher levels than prior years, averaging US$22,000 and US$25,630 net per day for Handysize and Supramax respectively.

A softening in rates since May has been due to higher vessel availability as a result of a reduction in grain exports and demand weakness in China. However, the market seems to have found a floor over the past weeks.

Please turn to slide 5.

Slide 5 – MINOR BULK DEMAND SUPPORTING RATES

It has been a continuation of strong minor bulk demand which has supported rates over the period. In particular, demand for construction materials, aggregates, cement and clinker.

Coal loadings in the period were up 2%, with higher seaborne coal demand driven by a surge in global energy demand and energy security concerns, despite record Chinese domestic production, and the Indonesian coal export ban in January.

The conflict in Ukraine has also had a positive tonne-mile impact as coal is increasingly being sourced from non-Russian areas such as Australia, United States, Canada and Colombia.

Conflict in Ukraine continues to impact grain exports from the Black Sea and has been a contributing factor in lower year to date grain loadings of 6% compared to the first half of 2021. Global food security has become a major issue as typical buyers of Ukrainian grains are forced to source from locations which are further away.

Some lost volumes are being replaced by other producers, most notably the United States, Argentina, Brazil and Australia as higher grain prices have incentivised farmers around the world to increase plantings for export, with these volumes expected to benefit overall tonne-mile demand.

We continue to monitor recent news regarding an agreement to allow grain exports from the Black Sea – which we ultimately see as positive to demand if the agreement can be executed safely and efficiently.

Iron ore loading volumes declined 1% in the first six months due to seasonal weather impacting mining operations from key producers in Brazil and Australia.

Please turn to slide 6.

Slide 6 – TCE EARNINGS SIGNIFICANTLY HIGHER THAN 1H 2021

Our daily TCE over the period were substantially higher than prior years – driven by strong minor bulk demand and supply fundamentals

These charts show our quarterly actual achieved TCEs for our Handysize and Supramax ships. As you can see our earnings were significantly higher, with our Handysize and Supramax TCE rates in the first half of 2022 up 83% and 85% respectively, compared to the same period last year.

We have covered 81% and 85% of our Handysize and Supramax vessel days in 3Q22 at US$23,690 and US$28,970 per day net respectively.

Please note that our Supramax forward cover estimates excludes the scrubber benefit, which is currently about US$5,130 per day, across our 32 owned and 3 time-chartered Supramax vessels.

Market activity over the period was strong allowing us to take attractive cover, while maintaining sufficient spot market exposure.

Please turn to slide 7.

Slide 7 – OUTPERFORMANCE CONTINUES

In the period, both our Handysize and our Supramax delivered an exceptional performance and we outperformed the indices by US$4,370 per day and US$8,210 per day respectively. Our

performance continues to benefit from our diverse cargo and customer base and the close customer interaction facilitated by our extensive global office network.

It is worth noting that scrubbers fitted to our core Supramax vessels contributed US$2,120 per day to outperformance in the first half 2022.

Handysize and Supramax vessels have outperformed the index over the last 3 and 4 quarters respectively.

Our operating activity contributed US$30.7 million, generating a margin of US$3,330 net per day over 9,200 operating days in the first half. While margins varied over the period, they still remain historically high and our operating activity represents an ongoing opportunity to utilise Pacific Basin's commercial and operating skills, as well as our global presence close to our customers to generate supplementary earnings for the business.

Please turn to slide 8.

Slide 8 – HANDYSIZE – OUR COSTS REMAIN COMPETITIVE

On slide 8, our Handysize owned vessel costs remain competitive despite higher depreciation costs related to the reversal of a vessel impairment of US$152 million at the end of 2021.

Daily Opex costs increased by 17% compared to the full year 2021, as a result of higher crewing costs. Our Handysize vessels employ a higher proportion of PRC crew, and as a result of the pandemic we have had higher associated repatriation and crewing costs.

Repatriation costs are beginning to reduce as the process of returning our crews home begins to ease, and our reduced number of PRC seafarers. We expect second half 2022 seafarer repatriation costs to be lower than the first half of this year.

Please turn to slide 9.

Slide 9 – SUPRAMAX – OVERALL STABLE COSTS

On slide 9, our Supramax overall vessel costs remained at competitive levels in the industry.

Supramax long-term chartered vessel daily costs increased by 26% compared to the full year 2022, to US$14,400. This is due to strong market conditions which have increased charter costs, although they remain profitable in comparison to current market spot rates.

I will now hand you over to Peter who will present the financials, and I will be back afterwards with outlook and strategy summaries.

Speaker: Peter Schulz

Slide 11 – FINANCIAL RESULTS

Thank you very much Martin. Good afternoon ladies and gentlemen. Please turn to slide 11 were we set out our P&L in summary.

As you can see given the higher average TCE rates over the period, we generated our best interim result ever, despite higher owned and chartered costs – as Martin has explained.

Our G&A has increased mainly due to higher discretionary remuneration provisions. Our full year 2022 G&A costs are expected to be in line with full year 2021.

Below underlying profit, our net profit was further impacted by positive MTM changes in our hedging portfolio and gains on vessel disposals, partially offset by incentive fees paid to bondholders for the early conversion of our CB.

Please turn to slide 12.

Slide 12 – CASH FLOW

The operating cash inflow for the first half was US$486 million, inclusive of all long and short-term charter hire payments. This compares with the US$203.9 million in the first half 2021 and US$813.1 million in the full year 2021.

We had US$41 million in proceeds from the sale of 4 smaller Handysize vessels which were sold and delivered in the period – while the sale of our 5th smaller Handysize vessel was delivered in July and so will be reflected in our full year results.

Capex spending remains well controlled, and for the first half of 2022 totaledUS$35 million, of which we paid US$15.5 million for one second-hand Ultramax, and around US$20 million for dry dockings and Ballast Water Treatment Systems.

We expect capex expenditure for 2022 to be approximately US$60 million, predominately relating to dry dockings and Ballast Water Treatment Systems, and excluding any vessel purchases.

Despite paying our final dividend for 2021 of US$368 million in May, we still increased our cash balance by US$56 million during the period.

Please turn to slide 13

Slide 13 – STRENGTHENING BALANCE SHEET AND AVAILABLE LIQUIDITY

Strong operating cash flow and limited capital expenditure has increased our available committed liquidity to US$698.6 million and we are today US$68.9 million net cash positive.

During the period we made an offer to holders of our US$175.0 million convertible bond to incentivise early conversion. This resulted in a reduction of our outstanding convertible bond to US$70.1 million. This offer has allowed us to further optimise our capital structure by reducing net borrowings and increasing the Company's equity capital, thereby deleveraging our balance sheet while at the same time lowering our finance costs.

This offer is in line with our capital allocations priorities which firstly is to de-lever the balance sheet.

We will also maintain a strong available liquidity position for future investments whilst continuing to distribute excess cash through dividends to our shareholders. The 75% of profits total dividend payable for the first half of the year is a strong re-enforcement of this strategy.

I will now hand you back to Martin for his outlook and strategy slides.

Speaker: Martin Fruergaard

Thank you Peter,

Please turn to slide 15.

Slide 15 – FIRM DEMAND OUTLOOK, DESPITE SHORT-TERM HEADWINDS

Global GDP is slowing, with the IMF recently revising GDP growth forecasts down further to 2.9% in 2022, and 3.2% in 2023.

Widely adopted expectations are for a recession in both the US and Europe, while demand from emerging markets will be negatively impacted by inflation and a stronger US dollar.

China's growth has been restrained over the period due to continued Covid-19 containment measures and a struggling residential property sector.

We expect dry bulk demand in the second half to moderate somewhat from recent highs but remain relatively firm mainly due to seasonal factors in the grain market, elevated coal demand for electricity production and continued investment in global infrastructure.

In the longer-term we see upside demand from:

- Substantial infrastructure investments going forward – much of it driven by the green transition
- Geopolitical instability and increasing food and energy insecurity, which is likely to further drive tonne-mile demand for grain and coal
- And, the eventual relaxation of China's Covid mitigation controls, allowing improved contribution to a recovery in domestic and international economic activity

Please turn to slide 16.

Slide 16 – LOW ORDERBOOK AND UPCOMING IMO REGULATION REDUCING FUTURE SUPPLY

Dry bulk newbuild ordering in the first half of 2022 was 9.4m dwt, compared to 23.4m dwt in the first half of 2021, a reduction of 60% compared to the same period last year, and despite the strong rates environment we continue to enjoy.

The total dry bulk orderbook stands at 7.2% of the existing fleet, which is the smallest it has been in decades.

New ship ordering is expected to remain restrained until vessel designs for clean fuels (such as ammonia and methanol) and associated bunkering infrastructure become commercially available.

Please turn to slide 17

Slide 17 – NET FLEET GROWTH REDUCING

Despite very little scrapping, the global dry bulk fleet grew only 1.5% net during the half-year compared to 1.9% in the same period last year mainly due to slowing newbuilding deliveries.

Vessel speeds remain elevated leaving limited scope to increase vessel capacity through faster speeds, while Covid-related inefficiencies around the world, particularly in China, have further constrained the availability of tonnage to meet global demand for dry bulk shipping.

We expect IMO 2023 regulations will not start forcing slower speeds and higher scrapping until 2024 at the earliest.

These supply constraints, and limited scope for speeding up the global world fleet, provides structural long-term support for the dry bulk market.

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Slide 19 – STRATEGIC DIRECTION REMAINS UNCHANGED

Our strategy is unchanged, and at our core we will remain asset heavy, continuing to acquire – selectively and in a disciplined way – quality second-hand ships, while complementing our core fleet with mainly short-term chartered ships. We will continue to gradually sell our smaller, older ships when the time is right.

We have a world-class ship management team, and we are committed to keeping this function in-house, with the ambition to further improve our safety and environmental performance, our cost competitiveness, and our service quality and reliability for our customers.

We will maintain our high level of services to our customers, while ensuring our crews are healthy and safe, and our vessels continue to operate safely and efficiently.

We will not contract newbuildings until zero-emission-ready ships are available and commercially viable in our segments.

And, we will keep our balance sheet strong while distributing excess cash to shareholders.

Please turn to slide 20

Slide 20 – ON TRACK TO MEET OUR GHG REDUCTION GOALS

As many of you are aware the IMO adopted global regulations will come into effect from January 2023. Our ambition will be for our ships to achieve an AER rating of "C" or better.

From January 2023, IMO's global EEXI and CII regulations are expected to drive technical and operational measures to improve the carbon efficiency of existing ships.

We will continue to trade our ships efficiently for high laden-to-ballast utilisation, and will constantly seek, assess and implement energy-efficient operating measures – including looking for collaborative solutions with our customers, tonnage providers, ports and other stakeholders.

This will ensure that our existing ships running on conventional fuel oil can maintain sound Annual Efficiency Ratio (AER) ratings and continue to trade for the foreseeable future.

During the period, we committed to cooperate with Nihon Shipyard and Mitsui in investigating alternative green fuels and their availability, and to develop new zero-emission vessel designs and potentially invest in related bunkering infrastructure.

We are preparing ourselves for shipping's eventual inclusion in the European Union Emissions Trading System (EU ETS) among other EU initiatives to drive decarbonisation in shipping. The European "Fit for 55" package remains subject to negotiations between the European Council, Parliament and Commission, and is now likely to apply to shipping from 2024 onwards.

The consequences of these rules will include the progressive slowing of vessel speeds and, over time, accelerated scrapping as older and less-efficient ships become no longer fit for trading.

Please turn to slide 21

Slide 21 – OUR FLEET RENEWAL CONTINUES

We currently own 117 Handysize and Supramax ships and, including chartered ships, we currently have approximately 240 ships on the water.

As we stated in previously, we are selling our small older Handysize ships to take advantage of the historically high asset values, and further optimises our fleet.

So far this year we have sold five of our smaller older Handysize vessels.

Our vessel purchasing is expected to slow as asset prices approach historical highs however, our long-term growth and fleet renewal strategy continues, with a focus on large Supramax and Ultramax vessels.

Please turn to slide 22

Slide 22 – WE CONTINUE TO BE OPTIMISTIC ABOUT OUR MARKET

We have had a fantastic start to 2022, with first half average TCE earnings for Handysize and Supramax up 83% and 85% above 1H21 respectively.

We expect dry bulk fundamentals to remain relatively firm in the second half of 2022 despite slowing GDP growth, demand softness in China and the war in Ukraine. As we expect food and energy security issues and continued global infrastructure investment to moderate the impact.

We also see potential upsides in a lifting of the Black Sea grain embargo and China being able to better control its sporadic Covid-19 outbreaks

Given the supportive fundamentals of our industry, we are excited by the longer-term prospects of dry bulk shipping despite any short-term headwinds.

Our large and modern owned fleet of highly versatile Handysize and Supramax ships, combined

with our close customer partnerships, enhanced access to cargo opportunities, and high vessel utilisation, will enables us to outperform in this strong earnings environment.

Having significantly further strengthened our balance sheet in the first half of 2022, we anticipate that the still healthy dry bulk market, our strong cash generation and limited expected capital expenditure will enable us to continue to reward shareholders by returning capital and take advantage of opportunities to grow our fleet going forward.

As always, I would like to take this opportunity to thank all of our loyal and talented Pacific Basin seafarers and shore-based staff, as it is not without your commitment and professionalism that we can deliver these results and continue to improve our safety performance.

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. If you have any further questions, please direct them to our Investor Relations team who will be happy to answer.