3Q 2016 Trading Update Transcript

6 October 2016

Operator introduction

Slide 1 – Cover Slide

Ladies and gentlemen, thank for standing by and welcome to Pacific Basin Shipping's Q3 2016 Trading Update Conference Call. Today's call will be presented by Mr. Mats Berglund, Chief Executive Officer for Pacific Basin. At this time, all participants are in a listen-only mode. There will be a presentation followed by question-and-answer session. This conference is being recorded today, Thursday, 6th October 2016. I now hand the conference over to your speaker, Mr. Mats Berglund. Thank you, please go ahead.

Mats H. Berglund, Chief Executive Officer:

Thank you, welcome everyone. Thanks for calling in and for your interest in our company. I would like to give you a brief update on the Company and market developments in the third quarter. I am accompanied by our CFO, Andrew Broomhead, who will join me in answering any questions after I have talked you through the slides.

Slide 2 – Freight Market Improves From a Very Low Base

The dry bulk freight market indices for all bulk carrier types have improved from the historically low base recorded in the first quarter.

Handysize and Supramax market index rates averaged about US$5,500 and US$6,700 per day net respectively in the third quarter. These average market rates represent a more than 20% improvement on the previous quarter, but an 8% and 20% decline compared to the same period last year, illustrating that freight conditions remain depressed and are still challenging for shipowners.

Slide 3 – Our 3Q16 Performance

In the context of the improved but still depressed market conditions, we generated average Handysize and Supramax daily TCE earnings of about US$7,000 and US$7,400 per day net in the third quarter.

Year-to-date our average Handysize and Supramax TCE earnings have outperformed the BHSI and BSI spot market indices by 44% and 21% respectively.

We have covered 74% of our contracted Handysize revenue days in the final quarter of 2016 at around US$8,000 per day net, and 75% of our contracted Supramax days at around US$7,500.

For next year, we have so far secured cover for 18% of our Handysize revenue days in 2017 at around US$9,500 per day net, and 27% of our contracted Supramax days at around US$11,400.

Slide 4 – Our 3Q16 Update

While our outperformance figures and business model remain robust, the dry bulk market continues to be challenging with average industry freight earnings at loss-making levels, and we are continuing to manage our business for a weak market in the medium term.

We are continuing our various initiatives to further reduce our costs, including reducing vessel operating costs through scale benefits, without compromising safety and maintenance.

In the first half of 2017, we will be relocating our Hong Kong headquarters out of Hong Kong's central business district, which will lead to a significant cost saving while allowing us to create a modern and efficient working environment in a newly revitalised part of Hong Kong Island.

We are establishing a new commercial office in Rio de Janeiro towards the end of 2016 to help grow our cargo volumes and to support our many customers on the east coast of South America.

We have substantially completed our exit from non-dry bulk activities, but the significant reduction in oil, gas, mining and Middle East construction activity is causing a deterioration in tug and barge values, which creates a challenging backdrop for the disposal of our limited remaining towage assets. At the end of June, our towage assets had a net book value of approximately US$18 million, since which time we have agreed the sale, subject to completion, of further towage assets. This is expected to generate cash proceeds of over US$3 million, but result in a book loss of about US$2 million. Based on these expected losses, additional disposal losses or impairments on our remaining towage assets are possible at the year end. However, none of our remaining towage assets are mortgaged, and any disposals contribute cash to the Company.

Slide 5 – Global Dry Bulk Demand

What's driving the market?

The table on the left summarises Clarksons Platou's full-year 2016 forecast for global dry bulk volumes which are expected to grow about 1% year on year.

Overall effective dry bulk demand – reflecting tonne-mile changes, congestion and other effects – is estimated to have increased by about 1.5% in the year to date, with a forecast 1.8% increase for the full year.

A strong South American agricultural exports season in the first half of the year was followed by seasonally strong US export volumes in the third quarter – and you can see in the table 5% growth in soybeans and 2% in grain and growth in other cargoes we carry such as copper, sugar, cement, et cetera, is also robust.

Year-to-date Chinese dry bulk imports have increased 6.5% compared to the same period last year, with growth most notable in iron ore and coal imports – the latter due to China's reduced domestic coal production.

Logs-fitted ships like ours benefitted from a year-on-year increase in logs volumes, but Chinese steel exports softened in the third quarter having peaked at historic high levels in June.

Slide 6 – Self-Correcting Supply Factors

On the supply side, new ship ordering activity was basically zero during the third quarter, and that is very good news for the future.

Fleet growth is reducing and we expect the global dry bulk fleet in the full year to grow 2% - its lowest rate in 13 years.

While scrapping was very high in the first half of the year, scrapping reduced in the third quarter.

We expect new ship deliveries of about 6% and scrapping of about 4%, resulting in approximately 2% net growth in global dry bulk capacity for the full year 2016.

Slide 7 – Dry Bulk Supply & Demand

Summarising the fundamentals for 2016, it looks like effective demand growth will be around 1.5 to 2% and net fleet growth about the same, hence offsetting each other.

Going forward, a few factors are expected to impact the supply-side for the better:

Firstly, fewer and fewer new ships delivering from the yards in 2017 and 2018.

Secondly, higher oil prices are positive for the freight market as this allows freight rates room to recover without being undermined by faster speeds which increase supply.

And thirdly, the entry into force of the ballast water management convention in September 2017 will add to existing pressures on owners to scrap older and poorly performing ships, rather than invest in costly ballast water treatment systems and dry-dockings. That will help to shrink the oversupply.

Slide 8 – Handysize Vessel Values

The significant gap between newbuilding and secondhand prices continues to discourage new ship ordering activity, which has basically come to a stop.

As you can see in the graph, there is some life in secondhand values, and Clarksons Platou estimate values of benchmark five year old Handysize bulk carriers to have increased to US$10.5 million representing a 13% improvement from the market low values recorded in the second quarter. Newbuilding prices have held at US$19.5 million.

Slide 9 – Borrowings & Capex

At the half year, we had a cash position of US$ 406 million.

This will reduce since, as expected and planned for, the holders of all our $124 million 2018 convertible bonds exercised their put option right in September, and the 2018 convertible bonds will be repaid on 24 October 2016.

The redemption payment obligation is covered by the net proceeds of US$143 million raised through our rights issue in June.

A number of efficient, well-designed new ships are currently delivering into our fleet, and the last of our newbuildings delivers to us in the second quarter of 2017. This is shown in the graph by the US237m of capex commitments spread over the second half of 2016 and first half of 2017, which will be funded by our remaining undrawn Japanese export credit facilities of US$238m, and the ability to draw down a further $34 million of other secured borrowing facilities.

Slide 10 – Our Outlook & Strategy

In closing, while the dry bulk freight rates have improved from the historically low base in the first quarter, the market remains oversupplied and conditions are still challenging for shipowners. Average industry freight earnings are still at loss-making levels.

Self-correcting supply-side dynamics are at work, but it will take some more time and more scrapping for the market to return to a healthier balance.

Hence, we are continuing to manage our business for a weak market in the medium term. That means continuing our efforts to further reduce our costs without compromising safety and maintenance, and it means conducting our business efficiently and astutely combining ships and cargoes to maximise our margins.

Thank you for calling in, and I now invite you to ask any questions.