Funding

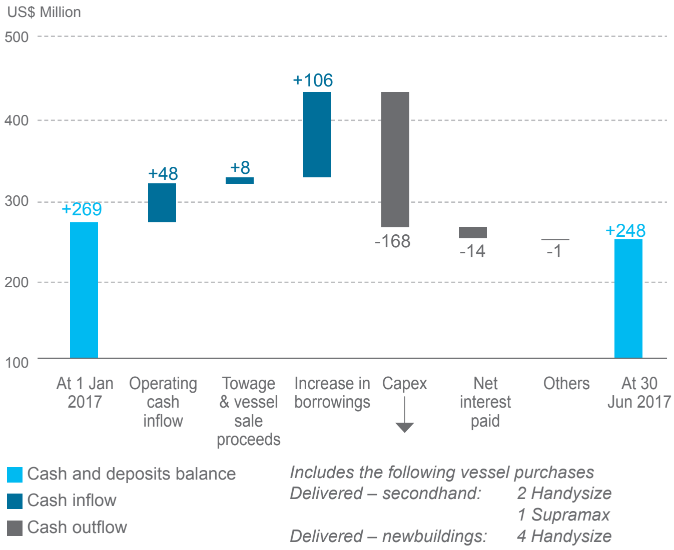
CASH FLOW AND CASH

The Group's four main sources of funds are operating cash flows, secured loans, convertible bonds and equity. The major factors influencing future cash balances are operating cash flows, purchases of dry bulk vessels, sale of assets, and drawdown and repayment of borrowings.

As part of the ordinary activities of the Group, the Treasury function actively manages the cash and borrowings of the Group to ensure sufficient funds are available to meet the Group's commitments and an appropriate level of liquidity is maintained during different stages of the shipping cycle.

Over the long term, the Group aims to maintain a consolidated net gearing of no greater than 50% – defined as the ratio of net borrowings to net book value of property, plant and equipment – which we believe is appropriate over all stages of the shipping cycle.

Sources and Uses of Group Cash in 1H 2017



Includes the following vessel purchases
Delivered – secondhand: 2 Handysize, 1 Supramax
Delivered – newbuildings: 4 Handysize, 3 Supramax

Current Position and Outlook

In the first half of 2017:

- Our operating cash inflow further improved to US$48 million, as compared with US$8 million in the first half of 2016 and US$50 million in full year 2016 on the back of a better dry bulk market conditions.
- Borrowings increased by US$106 million, after:
  - We drew down US$158 million, comprising US$140 million under our Japanese export credit facilities in respect of seven delivered newbuildings to fund the capital commitments of US$119 million during the period, and US$18 million of other borrowings on two existing vessels; and
  - Our net repayment of US$52 million of secured borrowings and revolving facilities.
- In June 2016, we raised US$143 million of cash, after expenses, through the issue of rights shares. US$124 million of such proceeds were used to repay the 2018 convertible bonds in October last year, and during 2017, we deployed the remaining proceeds of US$19 million to fund in part the purchase of two secondhand Handysize and one secondhand Supramax vessels with an aggregate consideration of US$31 million.

As at 30 June 2017:

- The Group's cash and deposits were US$248 million reflecting a 40% net gearing ratio.
- Our unmortgaged vessels comprise five dry bulk vessels with an aggregate net book value of US$90 million.
- Our committed banking facilities were fully drawn.

Cash and Deposits

The split of current and long-term cash, deposits and borrowings is analysed as follows:

US$ Million	30 June 2017	31 December 2016	Change
Total cash and deposits	**247.6**	269.2	-8%
Current portion of long-term borrowings	**(112.1)**	(95.7)	
Long-term borrowings	**(840.3)**	(743.5)	
Total borrowings	**(952.4)**	(839.2)	-13%
Net borrowings	**(704.8)**	(570.0)	-24%
Net borrowings to shareholders' equity	**68%**	55%	
Net borrowings to net book value of property, plant and equipment KPI	**40%**	34%	
Net working capital	**126.2**	160.6	-21%

Treasury is permitted to invest in a range of cash and investment products subject to limits specified in the Group Treasury Manual. These include overnight and term deposits, money market funds, liquidity funds, certificates of deposit and structured notes.

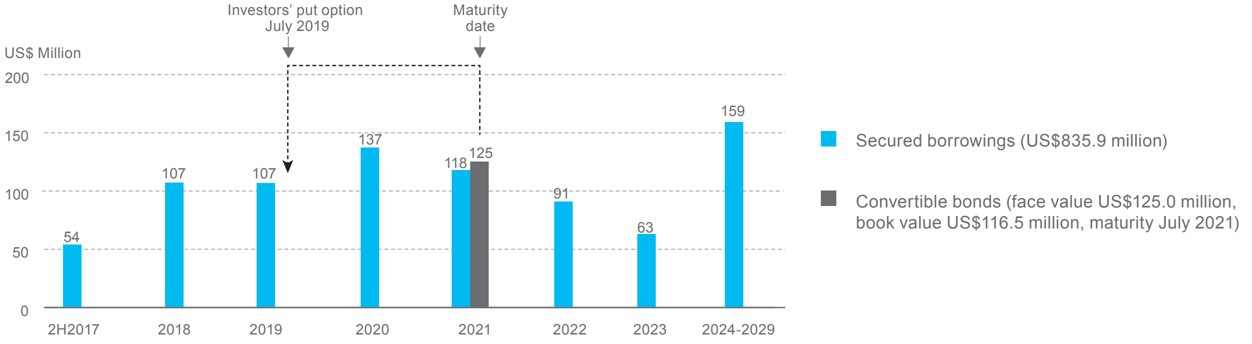
Treasury enhances Group income by investing in a mix of financial products, based on the perceived balance of risk, return and liquidity. Cash, deposits and investment products are placed with a range of leading banks, mainly in Hong Kong.

The Group's cash and deposits at 30 June 2017 comprised US$239.7 million in United States Dollars and US$7.9 million in other currencies. They are primarily placed in liquid deposits of three months or less and saving accounts. This maintains liquidity to meet the Group's vessel purchase commitments and working capital needs.

During the first half of 2017, Treasury achieved a 1.4% return on the Group's cash.

BORROWINGS

Schedule of Repayments of Borrowings



The Group's Treasury function arranges financing by leveraging the Group's balance sheet to optimise the availability of cash resources of the Group. The aggregate borrowings of the Group at 30 June 2017, which comprised secured borrowings and the liability component of convertible bonds, amounted to US$952.4 million (31 December 2016: US$839.2 million) and are mainly denominated in United States Dollars.

Secured Borrowings – US$835.9 million (31 December 2016: US$723.8 million)

Secured borrowings are in the functional currency of the business segment to which they relate. The overall increase in secured borrowings is mainly due to the drawdowns under our Japanese export credit facilities and other borrowings, partially offset by scheduled loan amortisation.

In the first half of 2017, we drew down all our remaining committed loan facilities, which comprise our Japanese export credit facilities of US$139.7 million secured on seven newbuildings which were delivered during the period and other borrowings of US$18.2 million in respect of two existing vessels.

The Group monitors the loans-to-asset value requirements on its bank borrowings. If the market values of the Group's mortgaged assets fall below the level prescribed by our lenders, the Group may pledge additional cash or offer other additional collateral unless the banks offer waivers for technical breaches.

As at 30 June 2017:

- The Group's secured borrowings were secured by 96 dry bulk vessels with a total net book value of US$1,666.3 million and an assignment of earnings and insurances in respect of these vessels.
- Our unmortgaged vessels included five dry bulk vessels with an aggregate net book value of US$90.3 million.
- The Group was in compliance with all its loans-to-asset value requirements.

P/L impact:

The increase in interest (after capitalisation) to US$13.9 million (1H 2016: US$10.3 million) was mainly due to an increase in average secured borrowings to US$798.9 million (1H 2016: US$520.5 million).

Certain secured borrowings are subject to floating interest rates but the Group manages these exposures by using interest rate swap contracts.

Convertible Bonds – Liability Component is US$116.5 million (31 December 2016: US$115.4 million)

As at 30 June 2017 and 31 December 2016, there remained the 3.25% p.a. coupon July 2021 convertible bonds with an outstanding principal of US$125.0 million and the prevailing conversion price of HK$3.07.

P/L impact:

The US$3.2 million (1H 2016: US$7.4 million) interest expense of the convertible bonds is calculated at an effective interest rate of 5.7% (1H 2016: 5.2%).

FINANCE COSTS

Finance Costs by Nature

US$ Million	Average interest rate P/L	Average interest rate Cash	Balance at 30 June 2017	Finance costs 1H 2017	Finance costs 1H 2016	(Increase)/ decrease
Secured borrowings (including realised interest rate swap costs)	3.5%	3.5%	835.9	**13.9**	10.3	(35%)
Convertible bonds (Note)	5.7%	3.3%	116.5	**3.2**	7.4	57%
	KPI 3.7%	KPI 3.4%	952.4	**17.1**	17.7	4%
Unrealised interest rate swap income				**–**	(0.8)	
Other finance charges				**0.3**	1.1	
Total finance costs				**17.4**	18.0	4%
Interest coverage (calculated as EBITDA divided by total gross finance costs) KPI				**3.3x**	N/A	

Note: The convertible bonds have a P/L cost of US$3.2 million and a cash cost of US$2.0 million.

The KPIs on which management focuses to assess the cost of borrowings are the average interest rates for different types of borrowings and the Group's interest coverage (see table above).

The Group aims to achieve a balance between floating and fixed interest rates on its long-term borrowings. This is adjusted from time to time, depending on the interest rate cycle, using interest rate swap contracts where appropriate. In the first half of 2017, all our interest rate swap contracts qualified for hedge accounting as cash flow hedges and US$0.6 million of interest rate swap costs were realised. As at 30 June 2017, 64% (31 December 2016: 65%) of the Group's long-term borrowings were on fixed interest rates. As at 31 December 2017 and 2018, we expect about 65% of the Group's existing long-term borrowings will be on fixed interest rates.

DELIVERED VESSELS

As at 30 June 2017, the Group had in operation owned dry bulk vessels with a net book value of US$1,757 million as follows:

	Number	Average size (dwt tonnes)	Average age (years)	Average net book value (US$ Million)	Total net book value (US$ Million)
Handysize	79	32,500	9.4	15.6	1,235
Supramax	21	55,800	6.3	22.8	478
Post-Panamax	1	115,500	6.0	44.3	44

Latest estimated fair market values published by Clarksons Platou are US$14 million and US$16 million for 5-year old 32,000 dwt Handysize and 56,000 dwt Supramax vessels respectively.

VESSEL COMMITMENTS

As at 30 June 2017, we had no vessel commitments.

As at 30 June 2017, the Group had options to purchase 11 Handysize, 3 Supramax and 1 Post-Panamax vessels at predetermined times and prices during the period of their leases. These options are not expected to be exercised under current market conditions.

VESSEL OPERATING LEASE COMMITMENTS

Vessel operating lease commitments stood at US$508.5 million (31 December 2016: US$549.4 million), comprising US$342.0 million for Handysize, US$140.1 million for Supramax and US$26.4 million for Post-Panamax.

Our Handysize operating lease committed days slightly decreased 3% to 33,960 days (31 December 2016: 35,140 days) while our Supramax operating lease committed days decreased 10% to 12,090 days (31 December 2016: 13,370 days).

Onerous Contract Provisions

The Group wrote back US$8.3 million and US$1.9 million for Handysize and Supramax onerous contract provisions made in the first six months of 2017 following the utilisation of the first six months of 2017 elements of the charters. At 30 June 2017, there remains a provision of US$31.8 million for Handysize and US$9.9 million for Supramax time charter contracts substantially expiring during a three-year period as charter rates are higher than the expected earnings during this period. The remaining provisions will be released back to the income statement in the periods in which the charter payments for these vessels are due (see adjacent table).

			US$ Million
Year	Handysize	Supramax	Total
2H17	8.2	1.9	10.1
2018	15.4	6.8	22.2
2019	5.3	1.2	6.5
2020	2.9	–	2.9
Total	31.8	9.9	41.7

Charter Hire Reduction by issuing new shares

In 2016, new shares were issued to 10 shipowners in return for a US$12.6 million reduction in charter-hire rates over a 24-month period on 10 of our existing long-term chartered ships (“Charter Hire Reduction”). The income statement still reflects the original contracted charter costs, but the cash payments in the 24-month period are reduced by the value of shares issued (see adjacent table).

			US$ Million
Year	Handysize	Supramax	Total
2016	0.7	0.4	1.1
1H17	2.1	1.0	3.1
2H17	2.2	1.0	3.2
2018	3.6	1.6	5.2
Total	8.6	4.0	12.6

Commitments Excluding Index-linked Vessels

The following table shows the average daily charter rates both on the cash basis and P/L basis for the total vessel days of our chartered-in Handysize and Supramax vessels during their remaining operating lease terms by year. Compared to the contracted charter-hire costs, i) the cash basis reflects the reduced payments following the issue of shares for charter-hire payments; and ii) the P/L basis cost reflects the reduction due to the write-back of onerous contract provisions.

	Handysize			Supramax		
		Average daily rate			Average daily rate	
Year	Vessel days	Cash basis (US$)	P/L basis (US$)	Vessel days	Cash basis (US$)	P/L basis (US$)
2H17	6,300	8,850	7,880	4,640	9,690	9,490
2018	7,790	9,940	8,430	2,790	12,370	10,560
2019	7,400	10,440	9,720	2,190	13,150	12,670
2020	4,460	10,640	9,990	1,650	13,120	13,120
2021	3,350	10,360	10,360	680	12,260	12,260
2022+	4,680	10,570	10,570	150	12,500	12,500
Total	33,980			12,100		
Aggregate operating lease commitments		US$342.0m			US$140.1m	

Commitments Including Index-linked Vessels

Our fixed rate and variable rate index-linked lease commitments charged to the income statement for first six months completed and for second half of 2017 and 2018 contracted can be analysed as follows:

	1H2017		**2H2017**		**2018**	
Handysize	Vessel Days	Average daily P/L rate (US$)	**Vessel Days**	**Average daily P/L rate (US$)**	**Vessel Days**	**Average daily P/L rate (US$)**
Long-term (>1 year)	4,570	7,990	**4,620**	**8,170**	**7,750**	**8,440**
Short-term	6,720	7,370	**1,680**	**7,080**	**40**	**6,350**
Index-linked	760	7,670	**520**	**Market rate**	**100**	**Market rate**
Total	12,050	7,620	**6,820**		**7,890**	
Supramax						
Long-term (>1 year)	1,400	11,710	**1,630**	**11,350**	**2,640**	**10,610**
Short-term	12,100	8,020	**3,010**	**8,480**	**150**	**9,520**
Index-linked	300	7,960	**550**	**Market rate**	**610**	**Market rate**
Total	13,800	8,400	**5,190**		**3,400**	

Certain long-term chartered-in vessels may be extended for short-term periods at market rates, but remain categorised as long-term charters.

Index-linked vessel operating lease commitments refer to leases with market-linked variable charter rates. The variable charter rates are linked to the Baltic Handysize Index or Baltic Supramax Index (as applicable) and adjusted to reflect differences in the vessels’ characteristics compared to Baltic indices reference vessels. Vessels we charter are typically larger and more fuel efficient than index reference vessels.