Chief Executive's Review

Our robust customer-focused business model, global office network, experienced people, larger owned fleet and competitive cost structure position us well to benefit from the recovering market

Much Improved Financial Results

The minor bulk freight market strengthened again in the first half of 2018 which, combined with our high laden utilisation, continued outperformance and competitive cost structure, enabled us to record much improved positive results compared to the same period last year.

We made a net profit of US$30.8 million (2017: US$12.0 million net loss), an underlying profit of US$28.0 million (2017: US$6.7 million loss), and EBITDA of US$99.3 million (2017: US$56.6 million). Basic EPS was HK5.5 cents.

Recommencing Dividend Payments

In view of the recovering market conditions and our return to a meaningful level of profitability, we are recommencing dividend payments. The Board has declared an interim dividend of HK2.5 cents per share, in line with the dividend policy of paying out at least 50% of net profits excluding disposal gains for the full year.

Market Recovery Continues

The Handysize and Supramax freight market indices demonstrated continued year-on-year improvements to register the strongest first-half rates since 2014.

Significantly reduced newbuilding deliveries and only 1.6% net growth in the global dry bulk fleet helped to support a healthier demand-supply balance despite minimal scrapping of older vessels due to the improved freight rate environment.

Stronger minor bulk shipping demand in the Atlantic was driven most notably by growth in Brazilian and US agricultural bulk exports in the first and second quarters respectively, with Brazilian soybean exports reaching an all-time monthly high in May. US coal exports also grew strongly with April exports up more than 50% year on year and representing the highest monthly total in five years. Pacific demand benefited from increased trade in bauxite, nickel ore, copper concentrate and forestry products. Chinese imports of dry bulk commodities continued to be a key driver, especially thermal coal and the minor bulks in which we specialise which in the first half of 2018 are estimated to have increased around 8% year on year (excluding bauxite and nickel ore for which data is not yet available).

Pacific Basin Continues to Outperform

Our average Handysize and Supramax daily TCE earnings of US$9,750 and US$11,730 per day net were up 23% and 32% year on year and outperformed the BHSI and BSI indices by 19% and 11% respectively.

Our TCE premium and operating margins are driven by our ability to draw on our experienced teams, global office network, strong cargo support and large fleet of high-quality interchangeable ships in a way that optimises ship and cargo combinations for maximum utilisation.

We continue to maintain good control of our vessel operating expenses which averaged US$3,810 per day during the period. This contributes to a competitive overall cost structure and vessel breakeven level on our owned fleet.

Positive Growth Initiatives

In January 2018 we took delivery of the last of five vessels we acquired in a mainly equity-funded transaction announced in August 2017.

As announced in May 2018, we committed to purchase four more modern vessels for US$88.5 million to be 50% funded by equity. These partly equity-funded acquisitions enhance our operating cash flow, EBITDA and balance sheet strength, lower our P&L breakeven levels, and are expected to be accretive to our earnings per share.

In April we also acquired a secondhand vessel for cash.

Following the delivery of all these acquisitions, our owned fleet will grow to 111 ships.

Strong Balance Sheet

In June we closed a US$325 million 7-year reducing revolving credit facility secured over 50 of our owned ships, refinancing several of our existing credit facilities and raising fresh capital on previously un-mortgaged vessels at a competitive interest cost of LIBOR plus 1.5%. Supported by a syndicate of eight leading international banks, the new facility significantly extends our overall amortisation profile, further enhances our funding flexibility and reduces our already competitive P&L breakeven levels.

As at 30 June 2018, we had cash and deposits of US$317 million and net borrowings of US$657 million, which is 36% of the net book value of our owned vessels at mid-year.

Positive Market Outlook

The improvement in the market for minor bulk shipping in the first half of 2018 is encouraging. Supply side fundamentals look more positive with Clarksons Research estimating full-year net growth of 2.5% in global dry bulk capacity against 3.4% growth in dry bulk tonne-mile demand. Fundamentals are even more favourable for our Handysize and Supramax segments with minor bulk tonne-mile demand estimated to expand by 4% this year against combined Handysize and Supramax net capacity growth of about 2%. We are cautiously optimistic for a continued market recovery, although with some volatility along the way.

The trade conflict between the United States and several of its trading partners has escalated with the July roll out of fresh US tariffs on certain goods imported from China and retaliatory Chinese tariffs on imports from the US. Affected goods which could have an impact on cargo flows in our minor bulk segment include steel products and US agricultural products, primarily soybean.

Trade dispute actions to date impact only a small fraction of the trades in which Pacific Basin is engaged. Total US soybean exports to China in 2017 represented only about 0.6% of total dry bulk seaborne trade, and commodity trading patterns tend to shift rather than cease as a result of trade tariffs.

The conflict between the US and its key trading partners might get resolved but may also escalate. This uncertainty weakens sentiment which could undermine trade, and a global trade war could impact global GDP and dry bulk demand.

However, we continue to believe that any negative impact these protectionist actions have on the dry bulk trade will be largely outweighed by positive dry bulk supply fundamentals and continued global dry bulk trade growth overall.

Environmental Regulations Impacting Vessel Investment Decisions

Pacific Basin continues to assess and plan for three major environmental regulations high on the industry agenda.

The Ballast Water Management Convention requires ballast water treatment systems (BWTS) to be fitted on ships during docking surveys between 2019 and 2024 to substantially eliminate organisms from transferring between marine ecosystems. Following a comprehensive assessment of BWTS options, we have committed to retrofit 50 of our owned vessels with a system based on filtration and electrocatalysis, and nine of our ships are now fitted with BWTS. We are negotiating BWTS systems for our remaining 50+ owned vessels and remain well positioned to complete implementation across our owned fleet by 2023, one year ahead of the IMO's mandatory schedule.

The global 0.5% sulphur cap takes effect on 1 January 2020. We continue to assess the two main methods of compliance – low-sulphur compliant fuel oil versus exhaust gas cleaning systems or “scrubbers” – and are preparing ourselves for this significant change. Some owners of larger vessels, including some Supramax owners, are planning to install scrubbers. However, we expect the majority of the global dry bulk fleet, especially smaller vessels such as Handysize ships, will comply by using more expensive low-sulphur fuel, which would also lead to lower operating speeds and thereby contribute to a more favourable supply-demand balance.

In April 2018, the IMO announced an ambitious strategy to cut total greenhouse gas emissions from shipping by at least 50% by 2050 (compared to 2008) and improve average CO_2 efficiency by at least 40% by 2030 and 70% by 2050. The easiest first step to decrease carbon emissions is by reducing speed, but we believe these new IMO targets will in due course lead to the accelerated development of new fuels, engine technology and vessel designs that are not offered or practical today.

We believe that, combined, these regulations will over time encourage scrapping of poor quality ships and be positive for the supply-demand balance and benefit larger, stronger companies with high quality fleets that are better positioned to adapt and to cope practically and financially with compliance and new technology.

Well Positioned for a Recovering Market

The favourable outlook for widely-spread global GDP growth bodes well for dry bulk demand, and supply is expected to be kept in check by the continued gap between newbuilding and secondhand prices and the uncertain impact of new regulations on ship designs, both of which cause many shipowners in our segments to refrain from ordering new ships.

We see upside in secondhand vessel values and will continue to look at good quality secondhand ship acquisition opportunities as prices are still historically attractive, resulting in reasonable break-even levels and shorter payback times.

Our healthy cash and net gearing positions enhance our ability to take advantage of opportunities to grow our business and attract cargo as a strong partner. Our robust customer-focused business model, global office network, experienced people, larger owned fleet and competitive cost structure position us well to benefit from the recovering market.

We thank all our stakeholders for your continued support.

Mats Berglund

Chief Executive Officer

Hong Kong, 27 July 2018

Dry Bulk Outlook Possible market drivers in the medium term

Opportunities

- Strong industrial growth and infrastructure investment in China and beyond enhancing demand for dry bulk shipping
- Positive and widely spread growth outlook for all major economic areas
- Continued strong grain demand primarily for animal feed due to shift towards meat-based diet
- Environmental policy in China encouraging shift from domestic to imported supply of resources
- Environmental maritime regulations encouraging ship scrapping from current minimal levels and discouraging new ship ordering
- Low newbuilding deliveries in the medium term
- Periods of higher fuel oil prices encouraging slower ship operating speeds which decreases supply and emissions
- Expanding thermal coal imports into emerging south and south-east Asian countries

Threats

- Reduction in Chinese industrial growth and investments impacting demand for dry bulk shipping
- Environmental policy in China encouraging greater shift to renewable energy, possibly impacting coal imports
- Trade tariffs between US and its major trading partners resulting in short-term reduction in trade volumes while importers seek alternate commodity sources
- Escalating trade disputes impacting global GDP growth, weakening sentiment and undermining dry bulk demand
- Excessive new ship ordering if the price gap between newbuilding and secondhand ships closes
- Periods of low fuel prices supporting faster ship operating speeds which increases supply and emissions