Chief Executive's Review

Our robust customer-focused business model, high laden utilisation, global office network, experienced people, larger owned fleet and competitive cost structure position us well for the future

Financial Results

Our results for the first half of 2019 were supported by our robust customer-focused business model and competitive cost structure, but adversely affected by markedly weaker dry bulk freight market conditions. We made a net profit of US$8.2 million (2018: US$30.8 million), an underlying loss of US$0.6 million (2018: US$28.0 million profit), and EBITDA of US$101.1 million (2018: US$99.3 million), although EBITDA was positively affected by new lease accounting standards. Basic EPS was HK1.4 cents.

As our underlying result was at the break-even level, the Board has declared no interim dividend for the period, but will consider a dividend of 50% of net profit for the full year in line with our policy.

Market Recovering Following a Weak Start

2019 started weaker than the last two years with a more pronounced Chinese New Year dip, followed by a partial recovery. The US-China trade war and African Swine Fever impacted soybean imports to China, flooding in the Mississippi River impeded grain exports from the United States, and damage to mining infrastructure disrupted Brazilian iron ore exports while severe weather disrupted Australian iron ore exports.

Global dry bulk capacity grew by 1.6% net during the half year which is similar to a year ago, but was undermined by faster growth in Panamax capacity and was still not small enough to offset demand side weakness.

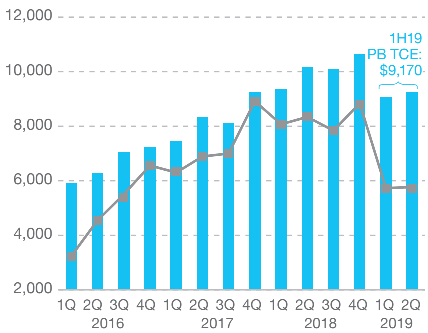
On a positive note, some of the key negative demand disruptions are easing, demand for minor bulks continues at a healthy level and dry bulk activity is typically seasonally stronger in the second half of the year.

Pacific Basin Continues to Outperform

While our average Handysize and Supramax daily TCE earnings of US$9,170 and US$10,860 per day net were down 6% and 7% year on year, our outperformance over the BHSI and BSI indices increased to 59% and 39% respectively.

PB Handysize Performance

US$/day net*



Pacific Basin Handysize quarterly TCE Performance

Baltic Handysize Index (BHSI)

* excludes 5% commission

Source: Pacific Basin, Baltic Exchange

Our ship operating expenses ("Opex") of US$3,990 per day, general and administrative ("G&A") overheads of US$730 per day and favourable financing costs of US$820 per day are also very competitive by industry standards.

Our TCE premium and competitive costs are driven by our ability to draw on our experienced commercial and technical teams, global office network, strong cargo support and large fleet of high-quality interchangeable ships in ways that optimise ship and cargo combinations for maximum utilisation and by generating scale benefits and other efficiencies from good systems, optimisation and strict cost control.

Positive Growth Initiatives

In the first half of 2019, we took delivery of four modern secondhand vessels (one Handysize and three Supramax), three of which we committed to purchase in 2018, and we completed the sale of an older, small Handysize. Two further modern Supramax acquisitions delivered into our fleet in July, expanding our owned fleet to 115 ships. Including chartered ships, we operated an average of 230 Handysize and Supramax ships overall during the first half of the year.

Strong Balance Sheet

In May we closed a new US$115 million syndicated 7-year reducing revolving credit facility secured against 10 of our previously unmortgaged ships, raising fresh capital at a competitive interest cost of LIBOR plus 1.35%. The new facility further enhances our funding flexibility and reinforces our already competitive vessel break-even levels.

During the period, holders of our convertible bonds due in 2021 exercised their right to redeem US$122.2 million of the convertible bonds on 3 July 2019, and on the same date we exercised our option to redeem all the remaining bonds totalling US$2.8 million on 2 August 2019.

As at 30 June 2019, we had cash and deposits of US$314 million, providing sufficient liquidity to repay the US$125 million convertible bonds in full. We had net borrowings of US$687 million, which is 37% of the net book value of our owned vessels at mid-year.

DRY BULK OUTLOOK
Possible market drivers in the medium term

OPPORTUNITIES

- Continued strong industrial growth and infrastructure investment in China (boosted by economic stimulus) and other emerging markets, enhancing demand for minor bulk shipping
- Easing of US-China trade tensions resulting in improved sentiment and dry bulk trade activity
- Environmental policy in China encouraging shift from domestic to imported resources
- Limited newbuilding ordering and deliveries in our segments supporting tighter supply in the medium term
- Environmental maritime regulations encouraging increased ship scrapping from current minimal levels and discouraging new ship ordering
- Supply contraction due to scrubber installations ahead of IMO 2020 and slower operating speed of ships burning more expensive low-sulphur fuel
- Easing of recent export disruptions in Brazil and the United States, resulting in stronger exports of iron ore and grain

THREATS

- Slowing global economic growth, especially in China, affecting the trade in dry bulk commodities
- Environmental policy in China encouraging greater shift to renewable energy, possibly impacting coal imports
- Worsening 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
- African Swine Fever undermining Chinese demand for imported soybean

Environmental Regulations Impacting Vessel Investment Decisions

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

To comply with the Ballast Water Management Convention, 30 of our owned ships are now fitted with ballast water treatment systems (BWTS), and we have arranged to retrofit our remaining owned Handysize and Supramax vessels by the end of 2022.

The IMO 2020 global 0.5% sulphur limit takes effect on 1 January 2020, and we expect the majority of the global dry bulk fleet, especially smaller vessels such as our Handysize ships, will comply by using more expensive low-sulphur fuel. We are preparing thoroughly for this, including cleaning our fuel tanks, securing availability of good quality compliant fuel and training our crews to ensure compliance and seamless service delivery to our customers.

Some owners of larger vessels with higher fuel consumption, including some Supramaxes, are planning to comply by continuing to burn cheaper heavy fuel oil in combination with installing exhaust gas cleaning systems or "scrubbers". We have chosen a balanced approach, with scrubbers successfully fitted and operational on ten of our Supramaxes so far, and we have arrangements in place with repair yards and scrubber makers to install scrubbers on a majority of our owned Supramax vessels. However, we are not fitting scrubbers on our larger fleet of 82 owned Handysize ships. Including chartered-in ships, we expect 85%-90% of our combined Handysize and Supramax fleet will comply by burning low-sulphur fuel. The future fuel price differential is uncertain, but having 10%-15% of our overall fleet scrubber fitted provides us some optionality in how we manage our fuel needs to comply with the new rules.

We are also carefully following the developments of IMO's ambitious longer-term strategy to cut CO_2 and total greenhouse gas emissions from shipping.

We believe that these environmental regulations will discourage new ship ordering until new, lower-emissions ship designs become available. This will improve the supply-demand balance and benefit larger, stronger companies with high quality fleets that are better positioned to adapt and cope both practically and financially with compliance and new technology.

Market Outlook

The IMF expects the global economy to gradually strengthen in the second half of the year and into 2020, partly as a result of Chinese economic stimulus and continued loose monetary policy in the United States and Europe. As published in July, the IMF forecasts global economic growth of 3.2% in 2019 and 3.5% in 2020.

Uncertainty over new environmental regulations and the gap between newbuilding and secondhand prices continue to discourage new ship ordering, and the small Handysize orderbook continues to be a positive factor for the health of our segments in the medium term.

The dry bulk freight market is expected to benefit in the second half of 2019 and early 2020 from many larger ships being taken out of service for several weeks for scrubber installation. We believe the market for smaller dry bulk ships like ours will benefit also over the longer term, as they will consume more expensive low-sulphur fuel and therefore tend to operate at slower speeds which reduces supply.

Clarksons Research estimates combined Handysize and Supramax net fleet growth of around 2.3% for 2019 and 1.3% for 2020 despite limited scrapping, while minor bulk tonne-mile demand is expected to grow more than 4% in 2019 and 2020.

We expect to see seasonally stronger freight market conditions in the second half of 2019, although with continued volatility influenced by further uncertainty about the US-China trade war, slower economic growth than in recent years and the impact of African Swine Fever on soybean imports to China.

Key catalysts for improvement on the demand side are expected to include the onset of the Black Sea grain export season and a return to normal levels of grain traffic out of the Mississippi River and iron ore exports from Brazil. Market rates have been firming, especially in the Atlantic.

Well Positioned for the Future

We still see upside in secondhand vessel values and will continue to look opportunistically but cautiously at acquiring good quality secondhand ships where prices are attractive.

2019 is a year heavily influenced by preparations for new environmental regulations. At the same time, several one-off market disruptions caused a pause in market momentum during the first half of the year. We have chosen to position many of our owned ships for dry docking this year to install ballast water treatment systems on our Handysize and Supramax vessels and scrubbers on a majority of our Supramaxes to set us up for what we believe will be stronger years ahead. We think the market momentum will return and we are well positioned to benefit.

Thank you for your interest in Pacific Basin and your continued support of our business.