2021 Interim Results Presentation Transcript
29 July 2021

Speaker: Mats Berglund

Slide 1 – Introduction

Welcome ladies and gentlemen and thank you for attending Pacific Basin's 2021 Interim Results earnings call. My name is Mats Berglund, CEO of the Company for the last nine years, and I am joined by my successor Martin Fruergaard who has already been with us for a one-month handover, and he takes over from me as CEO at the end of this week. We are also joined by our CFO, Peter Schultz.

Please turn to slide 2.

Slide 2 – Our Best Half-Year Result in 13 Years

During the first half of 2021, we made an underlying profit of 150.4 million, a net profit of US$160.1 million and EBITDA tripled compared to last year to US$244.6 million. EPS was HK26.4 cents, return on equity was 28% and total shareholder return 114%. The Board has decided to pay an interim dividend of 14 HK cents per share, in line with our dividend policy of paying out at least 50% of our net profits.

While this is our strongest half-year result in 13 years, it is important to note that our profitability improved progressively over the period. Our underlying result for June alone was US$53 million, the Company's highest monthly underlying result ever. Our cover rates for July and August are even higher, while the costs of our core fleet remain substantially fixed, clearly indicating that our monthly results continue to go up.

Slide 3 – Exceptionally Strong 2021 Market

Slide 3 shows how positively spot Handysize and Supramax rates have developed. As you can see, market rates are continuing to increase with the market now driven by the northern hemisphere grain season as is typical in the third quarter.

Slide 4 – Market TCE Rates Now Well Above 2010 Levels

To give you a longer historical perspective, **slide 4** shows average market rates for the last 15 years. We will make a few comparisons with 2010 in this report, as that is the last year with healthy freight rates. You have heard us say before that in 2010 we made about US$100 million profit but, if we got back to the same market rates now, we would make about US$ 400 million per year due to our now much larger owned fleet and our competitive cost structure. As you can see from this graph, we are now at monthly levels well above 2010 average rate levels.

Please turn to **slide 5.**

Slide 5 – The Positive TCE Trend Continues

This shows our monthly actual achieved TCEs for our Handysize and Supramax ships. Our underlying results are getting progressively better every month primarily due to:

- continuously increasing market freight rates;
- the one to three-month lag between fixing and execution of voyages means that it takes a few months before the progressively higher rates show in our P&L;
- the gradual expiry of lower paying cargo contracts;

- our larger core fleet with substantially fixed costs;
- the enlarged proportion of Supramax vessels in our fleet, which benefit from larger upside in strong markets; and
- our stronger operating activity performance from the second quarter onwards. On average, our operating activity generated a margin of US$1,320 net per day over 9,080 operating days in the first half.

But, our large core business with substantially fixed costs is of course now the main driver of our profitability. You can estimate our current profitability by following appendix slide 39 ("How to Model PB") and inserting our July/August cover rates of US$22,000 per day for Handysize and US$33,190 for Supramax, and our core fleet's substantially fixed costs of about US$8,600 for Handysize and 10,200 for Supramax, as represented by the dotted lines on these graphs.

Alternatively, you can just take the incremental daily increase in July and August rates versus the June rates and multiply that dollar per day increase by about 90 core Handysize ships and about 45 core Supras, assume 30 days per month, and add that incremental profit margin to the US$53 million we made in June to get a feel for our forward underlying monthly results assuming all other factors are unchanged.

Please turn to slide 6.

Slide 6 – Loading Data Explains the Strong Start to 2021

It is primarily strong demand for our two most important commodity groups – minor bulks and grain – that is driving up freight rates in our markets. Indicative global minor bulk loadings in the period were up 13% and grain was up by 9% year on year.

Strong Chinese import growth in the first quarter was followed by increased minor bulk loadings to non-Chinese destinations in the second quarter, including strong US demand for steel, cement and other construction material. We see it as an advantage that minor bulk demand is broad based and diverse, both geographically and in terms of commodities and customers.

Growth in grain loadings was supported by strong soybean trade and an encouraging new trend towards significant corn imports into China. The northern hemisphere grain season is just starting, with Black Sea, European and North American exports gradually requiring tonnage, which often makes the third quarter the strongest quarter of the year for our dry bulk segments.

With world GDP improving and continued stimulus in many countries, the demand forecast for the rest of the year is positive.

Slide 7 – Demand Fundamentals Have Driven the Market

Slide 7 lists demand factors in more detail and I won't go through all of it here other than to mention that our segments are also benefiting marginally from a few developments. One is exceptionally strong container rates which are driving some commodities to be shipped in geared bulkers. Another is fleet inefficiencies caused by congestion, the pandemic and by China not importing coal from Australia but from further afield. Also Australia has shifted more of its coal exports to smaller vessel types. However, these factors are not substantial and it is the fundamentally stronger demand and supply balance that drives our markets higher.

Moving to the supply side, please turn to **slide 8**

Slide 8 – Net Fleet Growth Well below 2% in 2022

This shows that net fleet growth continues to reduce, and we are expecting slow growth also in the second half of this year and well below 2% growth for next year. This means that our markets can remain healthy even if there is a slowdown in economic growth and demand.

Slide 9 – All Time Low Dry Bulk Orderbook

The dry bulk newbuilding orderbook as a percentage of the existing fleet is at an all-time low, and **slide 9** shows how significant this advantage is relative to other shipping segments. This bodes well for the future demand and supply balance and means that the probability for sustained healthy freight rates is higher for dry bulk relative to other shipping segments – especially for the smaller geared segments that we are in.

Please turn to **slide 10**

Slide 10 – Why Supply is Likely to Remain Moderate

While strong freight rates have historically lead to increased new ordering, we believe that dry bulk supply growth this time can remain at moderate levels. This is because new decarbonisation rules result in uncertainty and shorter expected economic lives for newbuildings with conventional fuel oil engines, making it more attractive to instead buy second-hand ships with prompt delivery, shorter payback time and lower residual value risk.

Also, it will be several more years before new technology ships become commercially viable and the requisite fuelling infrastructure is built out globally. This means that, other than a few prototypes operating on fixed lines, it will still be many years before such ships are ordered for the tramp shipping sectors.

Slide 11 – New IMO Rules Leading to Lower Speeds from 2023

Another positive for the supply side are the new IMO carbon intensity reduction rules adopted in June described on **slide 11**. EEXI technical rules will cap maximum engine power limits, and CII operational rules will require gradually improving carbon efficiency ratings based on actual fuel consumption and distance travelled, leading to gradually lower speeds from 2023-2024 onwards.

The EU has also announced its intention to include shipping in the EU Emissions Trading System effective 2023 which, subject to further development of these rules, will mean higher costs for emissions, also incentivising lower speeds.

Slide 12 – Improved Rates Support Vessel Values

Slide 12 shows how the stronger market freight rates have led to increases in both second-hand and newbuilding prices. But note that second-hand values remain well below newbuilding prices and also well below 2010 second-hand values in spite of freight rates now being well above the 2010 freight levels.

Slide 13-14 – Current Handysize/Supramax Values and Earnings vs 2010

In slide 13 and 14 we illustrate how strong the returns currently are, especially for second-hand ships, and how significant the remaining upside is for such ships just to return to the equivalent ship values of 2010.

Note that as is typical in strong markets, both the returns and asset value upside are larger for 10-15-year old ships than for younger vessels. For example, 10-year old Handy and Supramax vessel values still have 30-50% upside remaining before getting to 2010 levels, and they are paid down to scrap value in less than two year years based on current one-year timecharter rates. Hence we see significant additional remaining upside both in the earnings and market value of our fleet of 119 owned, quality, second-hand ships with an average age of 10.9 years.

Slide 15 – We Continue to Buy Ships in Line With Our Strategy

For this reason, and as shown on **slide 15**, we have continued to buy quality second-hand Ultramaxes and large Handysize ships that are highly suitable for our customers and trades. All the eight ships listed on this slide – including two previously unannounced acquisitions – were committed at very attractive prices between US$13 and US$17 million each.

Slide 16 – Significant Leverage from Our Larger Owned Fleet

The graph on **slide 16** shows how we have grown our owned fleet significantly over the years of historically low rates and asset values, and this means that we are now really well positioned to take advantage of the good market.

We have worked hard to streamline our Company, focusing only on our core segments and making our cost structure even more competitive while maintaining our ships in excellent condition. The market outlook is positive and this is what our teams both ashore and on board have worked so hard to set ourselves up for. It is really satisfying to now see the results come through.

We have strategically grown our owned Supra/Ultramax proportion of our fleet and now benefit from the larger earnings upside that these ships enjoy in strong markets.

In addition to our much larger core fleet, we have developed a significant and complementary Operating Activity business that matches our customers' spot cargoes with short-term chartered in ships even when our core ships are unavailable, thereby providing a service to our customers and making a margin and positive contribution to our results both in weak and strong markets. We currently have about 270 ships on the water overall, which is the biggest fleet we have ever controlled.

I would be remiss not to emphasize how grateful we are to our seagoing staff who, throughout the pandemic, have demonstrated continued professionalism in maintaining safe operating practices while Covid restrictions sometimes keep them at sea for longer than expected.

I thank my Pacific Basin colleagues – ashore and at sea – as well as our shareholders and all stakeholders for your excellent support over the years, and I ask that you extend the same great support and friendship to my successor, Martin Fruergaard.

Martin comes with impressive, lifelong maritime experience and proven leadership credentials. The Board and I are excited about Martin joining the Company and are confident that Pacific Basin's leading position in the minor bulk segments will continue to develop and prosper under his leadership.

Martin will make some remarks shortly, but before that, I hand you over to our CFO, Peter Schulz, for some comments on our financials.

Speaker: Peter Schulz

Slide 17-18 – Our Best Half-Year Result in 13 Years

Thank you very much Mats. Good afternoon ladies and gentlemen. Please turn to **slide 18**.

The Group posted an EBITDA of US$244.6 million and a net profit of US$160.1 million in the first half of 2021 as a result of the strong market conditions. This is equivalent to a 28% return on equity. This is our strongest half year result in 13 years.

The Group achieved US$203.9 million operating cash flow which has further strengthened the balance sheet. Net borrowings to NBV is down 6 percentage points since the end of 2020 at 31% and available liquidity is at US$417.1 million.

The board recommends an interim dividend of 14 Hong Kong cents per share in line with our dividend policy of paying out at least 50% of our net profits.

Slide 19 – Financial Results

On **slide 19** we set out our interim P&L in more detail. Comparison with the first half of 2020 is impacted by the impairment we took in June that year.

Please turn to **slide 20.**

Slide 20 – Handysize and Supramax Contribution

Our core Handysize TCE earnings per day were over US$6,700 higher than our core blended costs per day, which yielded a contribution of US105.2 million in the first half of 2021.

Our core Supramax TCE, boosted by the scrubbers on 32 of our vessels, was over US$9,100 per day higher than the core blended cost which yielded an overall Supramax contribution of US$65.9 million.

Our Operating activity contribution was a strong US$11.9 million or $1,320 per day.

Slide 21 – Handysize – Costs Well Controlled and Slightly Lower

On **slide 21**, our Handysize owned vessel costs reduced to US$7,270 per day mainly due to lower depreciation costs because of the impairment made on 30th June last year. This was partially offset by an increase in operating expenses due mainly to the high cost of repatriating seafarers amidst Covid-19 travel restrictions.

Slide 22 – Supramax – Well Controlled

Our Supramax owned vessel daily costs increased slightly to US$8,960 per day mainly due to the same increase in travel-related operating costs as Handysize.

Please turn to **slide 23.**

Slide 23 – Cash Inflow and Outflow in 1H2021

The operating cash flow for the first half of 2021 was US$203.9 million, inclusive of all long and short-term charterhire payments. This was US$126.4 million higher than the same period last year.

We received US$16 million in proceeds from the sale of four Handysize vessels.

Our borrowings decreased due to net repayments of US$143.9 million partly offset by the drawdown of US$45 million on new committed facilities.

Capex consisted mainly of US$96.4 million paid for four second-hand Ultramaxes that we committed to purchase in November 2020, one additional second-hand Ultramax and one second-hand Handysize and US$18.2 million in dry dockings and ballast water treatment systems. We docked 12 vessels during the period.

Slide 24 – Strengthening Balance Sheet and Available Liquidity

Onto **slide 24**. Our available liquidity was US$417.1 million at the end of the period – a significant number. Strong operating cash flow has driven a reduction in net borrowings to NBV to 31% which is a 6%-point decrease on the end of 2020 and well below our KPI of maximum 50%.

Our capital allocations priorities are to de-lever the balance sheet in line with our amortisation profile, being careful about new leverage following recent increase in vessel values. We will maintain our strong available liquidity position for investments and continue to distribute dividends to our shareholders in line with our stated policy.

I now hand you over to Martin.

Speaker: Martin Fruergaard

Slide 25-26 – Introduction to our new CEO Martin Fruergaard

Good afternoon or good morning ladies and gentlemen, my name is Martin Fruergaard, and it's a pleasure to be speaking to you for the first time. Starting with **slide 26**, I have a few bullets with which I want to introduce myself and to assure you of my intention as Mats' successor to maintain our commitment to the strategy that has worked very well for Pacific Basin in recent years.

I am from Copenhagen in Denmark where I spent the last six years as CEO of gas tanker owner and operator Ultragas. I previously spent 26 years with A.P. Moller-Maersk, including as senior director of Maersk Bulk Carriers – where I was for 10 years – and senior vice president of Maersk Tankers, among other roles in the Maersk group.

Since joining Pacific Basin on 2nd July, my focus has been on getting to know the PB organisation and ensuring a smooth transition between CEOs. I am grateful to the senior managers - and Mats in particular - for the excellent preparation and time they have invested in the process to help facilitate a good handover at the helm.

Please turn to **slide 27**.

Slide 27 – Strategy Remains Unchanged

In past earnings calls, Mats explained the Company's strategy which still holds true today. Here I lift out some of the strategic priorities that I will be particularly guided by.

We want to stay specialised in minor bulk and the ship types that we know so well, and stick to our customer and cargo focused business model.

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 aim to always keep our balance sheet and liquidity strong.

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

Slide 28 – With Special Focus On…

On slide 28, you will see that I want in the short term to ensure our teams are equipped and supported in such a way that they will continue to deliver a quality service to our customers while maximising our earnings in the current strong market.

As before, we want to be the first choice partner for customers contemplating longer-term cargo contracts, and that means lending them our support as they consider their coming freight needs.

Health and safety is always a priority, especially during the challenging pandemic when crew-change restrictions and related complications take their toll on seafarers.

We embrace IMO's carbon-intensity reduction goal for 2030 and greenhouse gas reduction goal for 2050, and will enhance our focus on optimising our environmental performance and longer-term decarbonisation efforts.

We will use our expanding in-house data to improve decision-making and our operational, cost and environmental performance to the benefit of our customers and other stakeholders.

Last but not least, I want to ensure that our teams are empowered, trained and supported for a fulfilled, engaged and efficient workforce.

From what I have seen so far, the Company is already very much on the right track.

Slide 29 – Well Positioned for the Future

Wrapping up on **slide 29**, although some uncertainty remains over the path of the pandemic and the longevity of continued policy support, the demand outlook is positive with vaccines and economic stimulus leading the demand recovery. The dry bulk orderbook is at an all-time low and we expect that fleet growth can remain at moderate levels.

Thanks to our much larger core fleet, our efficient cost structure and our strong team, we have tremendous leverage to take advantage of the current strong freight market.

Before we move on to questions, I would like to take this opportunity on behalf of all of us at Pacific Basin to thank Mats for his excellent contribution to the Company over the past nine years. He oversaw the streamlining of our Company and the significant growth of our core Handysize and Supramax fleet that positions us so well today.

Tomorrow evening, we will bid Mats a sad farewell with all our best wishes for a safe and happy return to Sweden and a fulfilling retirement and next chapter in his life.

Speaker: Mats Berglund

Thank you Martin for your kind words. 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 session]

I'd like to thank you again for joining us today and for your continued support of Pacific Basin.