

MANAGEMENT DISCUSSION AND ANALYSIS

INTRODUCTION

The Company was incorporated in Bermuda on 10 March 2004 as an exempted company with limited liability under the Companies Act 1981 of Bermuda.

The Company became the holding company of PB Vessels Holding Limited and all its subsidiaries through an exchange of shares (the “Exchange of Shares”) of the Company with IDB Carriers (BVI) Limited, Dry Bulk Shipping (BVI) Limited and Plymouth Shipping Investments Limited as detailed in the prospectus of the Company dated 30 June 2004 (the “Prospectus”), which was completed on 30 March 2004.

The Exchange of Shares is accounted for using merger accounting as permitted by the Hong Kong Statement of Standard Accounting Practice (“SSAP”) No. 27 “Accounting for group reconstructions” issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”). The condensed interim accounts of the Group for the period ended 30 June 2004, including comparative figures, are prepared as if the Company had been the holding company of the Group from the beginning of the earliest period presented.

Following the Exchange of Shares, the Company acquired additional businesses effective on 31 March 2004 (the “Further Acquisitions”) to complete the group reorganisation (the “Reorganisation”) in preparation for the listing of the shares of the Company. These further acquisitions comprise primarily interests in certain vessel holding companies and ship management companies as set out in the Prospectus and were completed on the Listing Date of the Company. The results of these companies are included in the condensed profit and loss account from the effective date of acquisition, being 31 March 2004.

The shares of the Company were listed on the Main Board of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) on 14 July 2004 (the “Listing Date”).

The Group’s interim profit and loss account therefore consists of results for the six months ended 30 June 2004 in the case of the companies subject to the Exchange of Shares, and consolidated results for the three



month period from 1 April to 30 June 2004 for PB Management Holding Limited and its subsidiaries and the vessel holding companies acquired through the Further Acquisitions. The comparative profit and loss account for the six months ended 30 June 2003 consists only of the consolidated results of the companies subject to the Exchange of Shares.

REVIEW OF INCOME

During the six months ended 30 June 2004, the Group's consolidated turnover was US\$71.6 million as compared with the corresponding period last year of US\$21.1 million. The Group is principally engaged in the provision of ship chartering services and ship management services. Ship chartering services contributed to the Group's turnover and segment results of US\$68.0 million and US\$44.5 million respectively for first half 2004. Net profit attributable to shareholders increased to US\$43.1 million from US\$7.1 million.

The average number of owned vessels grew to 16 in the first half of 2004 from 12 in the first half of 2003 as a result of the acquisition of three vessels pursuant to the Reorganisation and the delivery of two newbuildings into the Group in May 2004.

The average number of chartered-in vessels in the first half of 2004 was five as compared to two in the first half of 2003. This fleet expansion gave rise to increases of US\$13.7 million and US\$7.7 million in the Group's consolidated turnover and net profit attributable to shareholders respectively.

The average daily charter rate of approximately US\$18,000 in the first half of 2004 was more than double that of approximately US\$8,300 in the first half of 2003.

REVIEW OF COSTS

Direct costs in the first half of 2004 were US\$24.3 million (2003: US\$11.3 million). Direct costs include crew costs, vessel operating expenses, drydocking expenses, depreciation, vessel operating lease expenses and cost of marine products sold.

Vessel operating lease expenses increased to US\$6.9 million in the first half of 2004 from US\$2.2 million in the first half of 2003. This increase was firstly a result of the increase in the number of vessels chartered in, and secondly a result of the increase in the average daily charter hire rate to approximately US\$7,815 in the first half of 2004 from approximately US\$6,520 in first half 2003.

The increase in other vessel operating costs, including crew costs and depreciation, of US\$6.7 million reflects the expansion in the number of the Group's owned vessels.

Five vessels were dry-docked during the six months to 30 June 2004 as compared to just one in the same period in 2003, thus giving rise to a US\$1.6 million increase in docking costs.

General and administrative expense was US\$2.4 million in first half 2004 as compared with US\$0.1 million in the same period in 2003. This was the result of the acquisition (pursuant to the Reorganisation) of the PB Management Holding Limited group, effective 31 March 2004 and represents three months of costs which include Directors, senior management and administrative staff costs of US\$1.4 million, amortisation of goodwill of US\$0.4 million and other administrative and office expenses of US\$0.6 million.

Finance costs, predominantly interest payments on bank borrowings, were US\$2.4 million in 2004 as compared to US\$2.5 million in 2003. These bank loans carried floating interest rates which ranged from approximately 2.5% to 3.4% in the first half of 2004, as compared to 2.7% to 3.9% in the first half of 2003.

LIQUIDITY, FINANCIAL RESOURCES AND CAPITAL STRUCTURE

Net cash flow from operating activities during the six months ended 30 June 2004 amounted to US\$62.9 million. As at 30 June 2004, the Group had US\$46.8 million of cash and cash equivalents, primarily denominated in United States Dollars. However, in July 2004, dividends of US\$12.6 million and US\$18.3 million were paid to the shareholders of the Company prior to the Reorganisation and to the shareholders of the Company prior to the Listing respectively.



The indebtedness of the Group solely comprises bank borrowings which the Group monitors closely to ensure a smooth repayment schedule to maturity. The Group's bank borrowings increased to US\$214.3 million as at 30 June 2004 from US\$145.9 million as at 31 December 2003. The increase was due to the acquisition of three vessels pursuant to the Reorganisation and a further delivery of two newbuildings in May 2004. The Group's bank borrowings are floating-interest bearing and denominated in United States Dollars. Subsequent to 30 June 2004, we hedged US\$186 million of our interest rate exposure at the end of July as follows:

- (a) US\$124 million over three years through caps at approximately 4.9%; and
- (b) US\$62 million over five years through a knock out swap at 5% with a cap at 7% at a fixed rate of approximately 3.5%.

At 30 June 2004, the Group's assets with a net book value of US\$289 million were pledged to banks to secure the above-mentioned bank borrowings.

Subsequent to 30 June 2004 and up to the date of this report, the Group has drawn down bank borrowing facilities of US\$285.2 million, of which US\$195.8 million was used to settle existing bank borrowings, US\$30.7 million was used to settle part of the consideration for the acquisition of the vessel companies as part of the Reorganisation, and US\$58.7 million was used for the acquisitions of five vessels delivered in July and August 2004.

As at the date of this report, the Group has unutilised committed bank borrowing facilities of US\$56.6 million. The facilities will be used to finance the Group's newbuilding commitments and other vessel acquisitions to which the Group is committed.

At 30 June 2004, the Group's gearing ratio expressed as net debt (calculated as total bank borrowings net of cash) as a percentage to fixed assets (based on net book values) was 0.51:1 (2003: 0.69:1). This drop in gearing ratio is due to the increase in cash balances held by the companies acquired through the Further Acquisitions and the cash generated during the period.

As at 30 June 2004, the Group had a foreign exchange facility of US\$11.0 million which was for a newbuilding contract denominated in Japanese yen and was secured by pledged bank deposits of US\$2.0 million.

At 30 June 2004, the Group had outstanding bunkers swap contracts to buy approximately 53,000 metric tonnes ("mt") of bunkers at fixed prices, which will expire through December 2005. These commitments were made to hedge for fluctuation in bunker prices in connection with the Group's long-term cargo contract commitments.

STAFF

Including the Executive Directors, the Group employed a total of 181 full-time shore-based employees as at 30 June 2004. Personnel are remunerated on a fixed salary basis and are entitled to a discretionary bonus based on both the Group and individual performance of that year and/or to performance related bonuses if certain financial targets, which are set annually by the Board, are achieved.

The Company has also adopted a share option scheme, the terms of which were approved by a written resolution of the shareholders of the Group dated 17 June 2004 subject to the Stock Exchange granting permission of listing of the shares of the Group. The detailed terms of the scheme were disclosed in the Prospectus. Subsequent to 30 June 2004 and up to the date of this report, options to subscribe for 56,700,000 shares at HK\$2.50 per share were granted on 14 July 2004. All options may be exercised over a period of 10 years and vest over a period of three years.

PURCHASE, SALE OR REDEMPTION OF SHARES

Pursuant to a resolution passed on 11 May 2004, the Company re-purchased 53,329.40 Class A shares, 63,990.96 Class B shares and 2,682.64 Class C shares at purchase prices of US\$1 per class of shares.

No pre-emptive rights exist under Bermuda Law in relation to the issue of new shares by the Company.



DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES AND DEBENTURES OF THE COMPANY OR ANY ASSOCIATED CORPORATION

At 30 June 2004, the interests and short positions of each Director and the Chief Executive in the shares, underlying shares and debentures of the Company and its associated corporations, as recorded in the register maintained by the company under Section 352 of the Securities and Futures Ordinance ("SFO") or as notified to the Company were as follows:

		Numbers of Shares Held							Approximate percentage of Issued Capital
		Personal Interests	Family Interests	Corporate Interests	Trusts and Similar Interests	Persons acting in Concert	Other Interests	Total Interests	
Christopher R. Buttery	Long Positions	4,800,000	—	—	12,110,348	—	—	16,910,348	1.33%
	Short Positions	—	—	—	1,044,683	—	—	1,044,683	0.08%
Mark M. Harris	Long Positions	4,800,000	—	—	—	—	—	4,800,000	0.38%
	Short Positions	—	—	—	—	—	—	—	—
Paul C. Over	Long Positions	4,800,000	—	—	12,110,348	—	—	16,910,348	1.33%
	Short Positions	—	—	—	1,044,683	—	—	1,044,683	0.08%
Brian P. Friedman	Long Positions	—	—	242,209,708	—	—	—	242,209,708	19.12%
	Short Positions	—	—	20,893,890	—	—	—	20,893,890	1.65%
Simon K. Y. Lee	Long Positions	—	—	—	36,682,374	—	—	36,682,374	2.89%
	Short Positions	—	—	—	2,994,027	—	—	2,994,027	0.24%

At no time during the period was the Company, its subsidiaries, or its associated companies a party to any arrangement to enable the Directors and Chief Executive of the Company to hold any interests or short positions in the shares or underlying shares in, or debentures of, the Company or its associated corporation.

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN THE SHARES, UNDERLYING SHARES OF THE COMPANY

The register of substantial shareholders maintained under section 336 of the SFO shows that as at 30 June 2004, the Company had been notified of the following substantial shareholders' interests and short positions, being 5% or more of the Company's issued share capital. These interests are in addition to those disclosed above in respect of the Directors and Chief Executive.

Name	Capacity/Nature of Interest		Number of Shares	Approximate Percentage of Issued Share Capital⁽¹⁾
Dry Bulk Shipping (BVI) Limited	Beneficial Owner	Long Positions	290,651,104	22.93%
		Short Positions	25,072,621	1.98%
IDB Carriers (BVI) Limited	Beneficial Owner	Long Positions	242,209,708	19.12%
		Short Positions	20,893,890	1.65%
Nassau Capital Real Estate Partners III L.P. ⁽²⁾	Interest of a controlled corporation	Long Positions	290,651,104	22.93%
		Short Positions	25,072,621	1.98%
Furman Selz Investors II L.P. ⁽³⁾	Interest of a controlled corporation	Long Positions	242,209,708	19.12%
		Short Positions	20,893,890	1.65%
FS Private Investments LLC ⁽³⁾	Interest of a controlled corporation	Long Positions	242,209,708	19.12%
		Short Positions	20,893,890	1.65%
James Luikart ⁽⁴⁾	Interest of a controlled corporation	Long Positions	242,209,708	19.12%
		Short Positions	20,893,890	1.65%
Pembroke	Beneficial Owner	Long Positions	180,180,833	14.22%
		Short Positions	—	—

Notes:

1. Assuming that the Over-allotment Option (as defined in the Prospectus) would not be exercised (it has subsequently been exercised in part).



2. Nassau Capital Real Estate Partners III L.P. is interested in approximately 40% of the registered capital of Dry Bulk Shipping (BVI) Limited and is deemed or taken to be interested in these Shares and to hold this short position (which are beneficially owned by and attributable to Dry Bulk Shipping (BVI) Limited respectively) for the purposes of the SFO.
3. Furman Selz Investors II L.P. is interested in approximately 88.2% of the registered capital of IDB Carriers (BVI) Limited, and FS Private Investments LLC is the manager of Furman Selz Investors II L.P. with power to control the exercise of voting rights attached to these Shares. Therefore, Furman Selz Investors II L.P. and FS Private Investments LLC are deemed or taken to be interested in these Shares and to hold this short position (which are beneficially owned by and attributable to IDB Carriers (BVI) Limited respectively) for the purposes of the SFO. FS Private Investments LLC does business under the name of Jefferies Capital Partners.
4. Mr. Luikart is a managing member of FS Private Investments LLC, which is the manager of each of Furman Selz Investors II L.P., FS Employee Investors LLC and FS Parallel Fund LP, being the members of IDB Carriers (BVI) Limited. Under these arrangements, Mr. Luikart is entitled, as a managing member of FS Private Investments LLC, to exercise or control the exercise of rights conferred by the holding of all the shares in IDB Carriers (BVI) Limited. Accordingly, Mr. Luikart is taken to be interested in these Shares and to hold this short position (which are beneficially owned by and attributable to IDB Carriers (BVI) Limited respectively) for the purposes of the SFO.

COMPLIANCE WITH THE CODE OF BEST PRACTICE

None of the Directors are aware of any information that would reasonably indicate that the Company is not, or was not, in compliance with the Code of Best Practice as set out in Appendix 14 of The Rules Governing the Listing of Securities on the Stock Exchange (the “Listing Rules”), during the accounting period covered by these interim results except that the Non-Executive Directors of the Company are not appointed for a specific term but are subject to retirement by rotation and election of the annual general meeting of the Company in accordance with the provisions of the Company’s Bye-laws.

AUDIT AND REMUNERATION COMMITTEES

The Company established an audit committee on 10 June 2004 (the “Audit Committee”) with written terms of reference, comprising exclusively the three Independent Non-Executive Directors of the Company, namely

The Rt. Hon. The Earl of Cromer, Patrick Blackwell Paul (chairman) and Robert Charles Nicholson. The primary duties of the Audit Committee are to review and supervise the financial reporting process and internal controls of the Company. A meeting of the Audit Committee was held to review the Group's interim results for the period ended 30 June 2004 before they were presented to the Board of Directors for approval.

The Company established a remuneration committee on 10 June 2004 (the "Remuneration Committee"). The Remuneration Committee shall consist of not less than three members, a majority of whom shall be independent. The Remuneration Committee initially comprised the three Independent Non-Executive Directors of the Company, namely The Rt. Hon. The Earl of Cromer, Patrick Blackwell Paul and Robert Charles Nicholson (chairman). At a board meeting held on 15 September 2004, Lee Kwok Yin, Simon and Brian Paul Friedman, both Non-Executive Directors were appointed as members of the Remuneration Committee in addition to the three Independent Non-Executive Directors. The terms of reference of the Remuneration Committee were approved by the Board of Directors on 15 September 2004. The primary duties of the Remuneration Committee are to make recommendations to the Board on the Company's policy and structure for all remuneration, including specifically that of Directors and senior management, and on the establishment of a formal and transparent procedure for developing policy on such remuneration.

ADOPTION OF CODE OF CONDUCT REGARDING DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding Directors' securities transactions on terms no less than the required standard set out in Appendix 10 — Model Code of Securities Transactions by Directors of Listing Companies of the Listing Rules. The Directors have complied with such code of conduct throughout the accounting period covered by these interim results.



INTERIM REPORT AND DISCLOSURE OF INFORMATION ON STOCK EXCHANGE'S WEBSITE

The announcement of interim results containing all the information required by paragraphs 46(1) to 46(9) of Appendix 6 of the Listing Rules is published on the Stock Exchange's website at www.hkex.com.hk and on the Pacific Basin website at www.pacbasin.com.

The Company's 2004 Interim Report will be circulated to shareholders by 30 September 2004. An electronic copy of the Interim Report will also be available on the Company's website at www.pacbasin.com from the date when the printed copy is dispatched to shareholders.

The Interim Report has been reviewed by our auditors, PricewaterhouseCoopers, in accordance with the Statement of Auditing Standards 700 issued by the Hong Kong Institute of Certified Public Accountants.

DIRECTORS

As at the date of this report, the Executive Directors of the Company are Christopher Richard Buttery, Mark Malcolm Harris and Paul Charles Over, the Non-Executive Directors of the Company are Lee Kwok Yin, Simon, James John Dowling and Brian Paul Friedman, and the Independent Non-Executive Directors of the Company are Robert Charles Nicholson, Patrick Blackwell Paul and Rt. Hon. The Earl of Cromer.

By Order of the Board
of Pacific Basin Shipping Limited
Christopher R. Buttery
Chairman

Hong Kong, 15 September 2004