FINANCIAL REVIEW

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 undertook a reorganisation during 2004 as described more fully in Note 1 to the accounts in this report which should be read in conjunction with the following commentary.

The Group's profit and loss account therefore consists of results for the twelve months ended 31 December 2004 in the case of the companies subject to the Exchange of Shares, and consolidated results for the nine-month period from 1 April to 31 December 2004 for the companies acquired through the Further Acquisitions. The comparative profit and loss account for the twelve months ended 31 December 2003 consists only of the consolidated results of the companies subject to the Exchange of Shares.

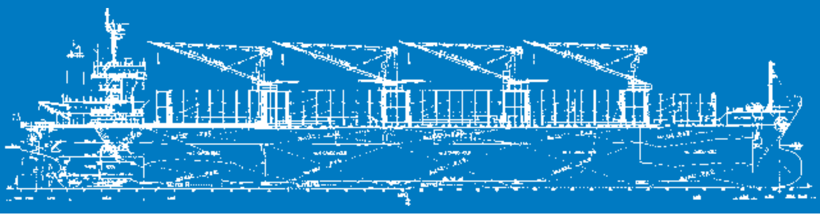
Review of Income

Total turnover increased to US$234.3 million in 2004 from US$54.2 million in 2003. Approximately 95.9% of total turnover was generated from the employment of vessels in the owned and chartered fleet and the remaining 4.1% by ship management revenues derived from the provision of commercial and technical management services for third-party vessels and revenues from marine service businesses. Net profit attributable to shareholders increased to US$103.5 million from US$22.7 million.

Following the Group's reorganisation on 31 March 2004, turnover is shown gross of voyage-related expenses. These expenses relate primarily to commissions, ships' bunkers and port-related costs. The total amount of voyage related expenses deducted from turnover was US$45.4 million, leaving US$188.9 million as turnover on a time charter equivalent basis.

The average daily rate which the vessels achieved increased 82.6% to approximately US$17,900 in 2004 from US$9,800 in 2003.

The average number of owned vessels grew from 13 in 2003 to 22 in 2004, an increase of 69.2%, as a result of the delivery of six vessels acquired pursuant to the reorganisation, the delivery of two newbuildings in May and further deliveries of 11 vessels after the Listing (including four vessels acquired conditional upon the completion of the Listing and seven vessels acquired after the Listing and before the year end). The average number of chartered-in vessels increased from approximately two in 2003 to approximately six in 2004. This expansion in chartered-in vessels gave rise to an increase of US$30.7 million and US$17.3 million in the Group's consolidated turnover and net profit attributable to shareholders respectively.



Review of Expenses

Direct costs increased to US$70.7 million in 2004 from US$26.2 million in 2003. Direct costs include crew costs, vessel operating expenses, drydocking expenses, depreciation, operating lease expenses on vessels chartered in and cost of marine products sold. An overhead allocation of US$11.0 million has been included in direct costs for the first time in 2004 following the acquisition of the management companies pursuant to the reorganisation. This represented shore-based costs of staff, offices and related expenses directly attributable to the employment and operation of the owned and chartered fleet.

Charter-hire expenses on vessels increased to US$18.7 million in 2004 from US$5.2 million in 2003. This was due to the increase in the average number of vessels chartered in to approximately six in 2004 from approximately two in 2003. The average daily charter rate increased to approximately US$8,500 in 2004 from approximately US$6,700 in 2003.

Direct costs for operating the Group's owned vessels, including crew costs, depreciation, drydocking expenses and direct cost following the reorganisation, were US$45.2 million in 2004, up from US$21.0 million in 2003. In part this reflects the expansion in the number of the Group's owned vessels by 69.2%. However, included within these costs were drydocking expenses on the larger fleet of US$4.5 million (2003: $0.6 million) relating to 12 vessels dry-docked in 2004 as compared to three in 2003.

General and administrative expenses were US$6.9 million in 2004 as compared to US$0.5 million in 2003. This was the result of the acquisition (pursuant to the reorganisation) of the management companies, effective 31 March 2004, and represents nine months of costs which include Directors, senior management and administrative staff costs of US$3.6 million, amortisation of goodwill of US$1.3 million, travel and marketing expenses of US$0.5 million, audit and other professional fees of US$0.5 million and other administrative and office expenses of US$1.0 million.

Finance costs consisted of interest payments on bank borrowings of US$7.8 million used to finance the Group's owned vessels, loan arrangement and commitment fees of US$1.5 million, and net cost of swap contracts of US$0.9 million. Interest payments on bank borrowings increased by 62.5% to US$7.8 million in 2004 from US$4.8 million in 2003. Bank loans in 2004 carried interest rates (including swaps) which ranged from approximately 2.5% to 5.0%, as compared to approximately 2.5% to 3.9% in 2003.

Liquidity and Sources of Capital

Net cash generated by operating activities was US$125.7 million in 2004 and US$35.8 million in 2003.

Net cash used in investing activities was US$268.8 million in 2004, primarily as a result of purchases of vessels of US$269.3 million. Net cash used in investing activities was US$27.3 million in 2003, primarily as a result of purchases of vessels of US$27.1 million. The increase in cash used in investing activities in 2004 was primarily due to an increase in the number of vessels acquired, of which 15 vessels were delivered in 2004, as compared to two vessels delivered in 2003.

Net cash provided by financing activities was US$178.9 in 2004, primarily as a result of additional bank loans for the acquisition of vessels of US$189.8 million, net IPO proceeds of $71.7 million, considerations paid to the then shareholders of the Company before the reorganisation of US$24.2 million and dividend payments of US$49.8 million paid to the shareholders of the group companies prior to the Listing. Net cash used in financing activities was US$8.8 million in 2003, primarily as a result of dividend payments of US$13.9 million.

As at 31 December 2004, the Group had working capital of US$18.3 million excluding long-term bank loans repayable within one year of US$36.1

million and the primary source of liquidity was US$41.7 million of bank balances and cash. The Group's primary short-term liquidity need is to fund general working capital requirements while long-term liquidity needs are primarily associated with expansion of the fleet and other capital expenditure. The Group's current policy is to borrow from banks approximately 60% of the fair market value of vessels acquired.

The indebtedness of the Group solely comprises bank borrowings which the Group monitors closely to ensure a smooth repayment schedule to maturity. As at 31 December 2004, the Group had total outstanding borrowings of approximately US$371.0 million, comprising the current portion of long-term secured bank borrowings of approximately US$36.1 million and long-term secured bank borrowings of approximately US$334.9 million all expiring in the year 2012.

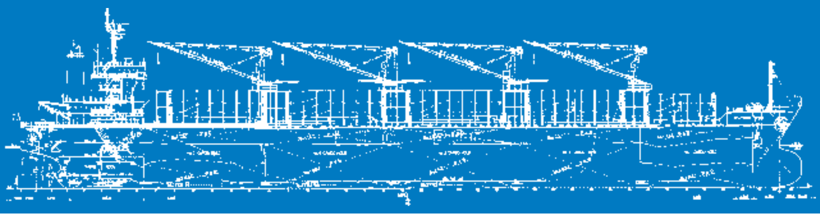
The Group is exposed to interest rate fluctuations on its bank borrowings. As at 31 December 2004, a total of US$181.8 million of bank borrowings was hedged by way of interest rate swap and cap arrangements with banks. The term of these hedging arrangements ranges from three to five years.

As at 31 December 2004, the Group's banking facilities were secured by mortgages over vessels and vessels under construction with a total net book value of approximately US$533.3 million and fixed deposits of approximately US$6.1 million, assignments of earnings and insurances in respect of the vessels and charges over the shares of certain vessel-owning subsidiaries.

The Group's gearing measured as total bank borrowings net of cash as a percentage to fixed assets was 59.4% (2003: 68.6%). This drop in gearing ratio is primarily due to the increase in cash balances as a result of the inclusion of the cash held by the companies acquired at the reorganisation and the cash generated from operations during the year.

At 31 December 2004, the Group had an outstanding foreign exchange contract with a bank to buy approximately Yen4.0 million and simultaneously to sell US$38,400 for operating expenses denominated in Japanese Yen.

At the year end, the Group had bunkers hedging contracts to buy approximately 96,500 metric tonnes of bunkers at fixed prices which will expire through December 2007. These commitments were made to hedge for fluctuations in bunker prices in connection with the Group's long-term cargo contract commitments.



Capital Expenditure

In 2004, capital expenditure on vessel additions, including instalments on newbuildings, were US$269.3 million.

As at 31 December 2004, the Group had non-cancellable commitments for the acquisition of one modern Handysize vessel and the construction of four Handysize vessels and one Handymax vessel for delivery between January 2005 and November 2006, with an aggregate unpaid cost of approximately US$105.7 million. Unpaid costs are net of progress payments and prepayments. Scheduled payments will be funded in 2005. Finance for such vessel commitments will come from cash generated from operations and additional long-term debt, as required.

Directors' Opinion on the Working Capital Available to the Group

The Directors are of the opinion that, taking into consideration the financial resources available to the Group, including internally-generated funds and the available banking facilities, the Group has sufficient working capital to satisfy its present requirements.

Staff

As at 31 December 2004, including the Executive Directors, the Group employed a total of 217 full-time shore-based employees based in Hong Kong, London, Manila, Melbourne, Seoul, Shanghai, Singapore and Tokyo.

Remuneration of the Group's employees includes basic salaries, bonuses and long-term incentives. The Group incurred total staff costs of approximately US$11.7 million for the year ended 31 December 2004, representing 5.0% of the Group's turnover for that year.

Personnel are remunerated on a fixed-salary basis and are entitled to a discretionary bonus based on both the Group and individual performance of the year and/or to performance-related bonuses if certain financial targets, which are set annually by the Board, are achieved.

The Group's principal retirement benefit scheme is the Mandatory Provident Fund Scheme (the "MFP Scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for those staff employed under the jurisdiction of the Hong Kong Employment Ordinance. The MPF Scheme is a defined contribution scheme.

Under the MPF Scheme, the employer and its employees are each required to make contributions to the scheme of 5% to 10% of the employees' relevant income, with the employees' contributions subject to a cap of monthly relevant income of HK$20,000. The Group's contributions to the scheme are expensed as incurred. Where employees leave the scheme prior to the full vesting of the employer's contributions, the amount of forfeited contributions is used to reduce the contributions payable by the Group.

The Company has also adopted a share option scheme, the terms of which were approved by a written resolution of the shareholders of the Company dated 17 June 2004. The detailed terms of the scheme were disclosed in the prospectus of the Company dated 30 June 2004 (the "Prospectus"). Up to the date of this report, options have been granted (on 14 July 2004) for 55,500,000 shares at HK$2.50 per share. All options may be exercised over a period of 10 years and vest over a period of three years.

Pacific Basin Shipping Limited

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