NOTES TO THE ACCOUNTS

1. GENERAL INFORMATION

Pacific Basin Shipping Limited (the "Company") and its subsidiaries (collectively the "Group") are principally engaged in the provision of dry bulk shipping services, which are carried out internationally, through the operation of a fleet of vessels.

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 is listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

These consolidated accounts have been approved for issue by the Board of Directors on 6 March 2006.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated accounts are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The consolidated accounts are prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS") issued by the Hong Kong Institute of Certified Public Accountants. The consolidated accounts have been prepared under the historical cost convention, as modified by the available-for-sale financial assets and financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss, which are carried at fair value.

The preparation of accounts in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity or areas where assumptions and estimates are significant to these consolidated accounts are disclosed in Note 4.

Certain new standards, amendments and interpretations to existing standards (collectively "New Standards") have been published by the HKICPA that are effective for accounting periods beginning on or after 1 January 2006 or later periods. The Group was not required to adopt these New Standards in the accounts for the year ended 31 December 2005. The Group has already commenced an assessment of the impact of these New Standards but is not yet in a position to state whether these New Standards would have a significant impact on its results of operations and financial position.

2.2 Adoption of new/revised HKFRS

With effect from 1 January 2005, the Group has adopted the new/revised standards and interpretation of HKFRS below, which are relevant to its operations. The 2004 comparatives have been restated as required.

(i) ***Fixed assets***

(a) *Vessel component costs*

Drydocking costs were previously charged to the profit and loss account when incurred. Under HKAS 16 "Property, Plant and Equipment", when a vessel is delivered, major components which are usually replaced or renewed in connection with a drydocking are depreciated over the estimated period to the first drydocking. The Group subsequently capitalises drydocking costs as they are incurred and depreciates these costs over their estimated useful lives. This change is applied to previous accounting periods.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.2 Adoption of new/revised HKFRS (continued)

(i) ***Fixed assets (continued)***

(b) *Residual values*

Previously, the residual value of a fixed asset was estimated at the date of acquisition and was not subsequently amended for changes in the estimated residual value. Under HKAS 16, the residual value and the useful life of an asset are reviewed at least at each year end and, if expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate.

(ii) ***Financial assets***

The adoption of HKAS 32 "Financial Instruments: Disclosure and Presentation" and HKAS 39 "Financial Instruments: Recognition and Measurement" has resulted in changes in the accounting policies relating to recognition and classification of (a) financial assets and liabilities at fair value through profit and loss, (b) available-for-sale financial assets and (c) loans and receivables. HKAS 32 is applied to previous accounting periods, whereas HKAS 39 is not. The effects of adopting HKAS 32 and HKAS 39 are set out below:

From 1 January 2004 to 31 December 2004, the Group classified its investments in securities, other than subsidiaries and jointly controlled entities, as investment securities, which were stated at cost less any provision for impairment losses. In addition, the Group's borrowings were stated at cost.

From 1 January 2005 onwards, the Group classifies its financial assets in the following three categories: (a) financial assets at fair value through profit or loss, (b) available-for-sale financial assets and (c) loans and receivables. The classification depends on the purpose of these financial assets. Management determines their classification at the time of initial recognition and re-evaluates their classification at every reporting date.

(iii) ***Share-based compensation***

In previous years, the provision of share options to employees did not result in an expense in the profit and loss account. Effective on 1 January 2005, the Group adopted HKFRS 2 "Share-based Payment" whereby the fair value of the employee services received in exchange for the grant of the share options and restricted share awards is recognised as an expense in the profit and loss account in the current period with an adjustment to the previous accounting period.

The total amount to be expensed over the vesting period is determined with reference to the fair value of the share options and restricted share awards granted. At each balance sheet date, the Company revises its estimates of the number of share options that are expected to become exercisable and the number of restricted share awards that are expected to become vested. It recognises the impact of the revision of original estimates, if any, in the profit and loss account, and a corresponding adjustment to equity in the balance sheet will be made over the remaining vesting periods.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.2 Adoption of new/revised HKFRS (continued)

(iii) ***Share-based compensation (continued)***

The proceeds received, net of any directly attributable transaction costs, are credited to share capital and share premium account when the share options are exercised.

(iv) ***Goodwill***

The adoption of HKFRS 3 "Business Combinations" and HKAS 36 "Impairment of Assets" has resulted in a change in the accounting policy for goodwill. Until 31 December 2004, goodwill on acquisitions was:

– Amortised on a straight-line basis over 15 years; and
– Assessed for indication of impairment at each balance sheet date.

In accordance with the provisions of HKFRS 3 and HKAS 36:

– The Group ceased amortisation of goodwill from 1 January 2005;
– Accumulated amortisation as at 31 December 2004 has been eliminated with a corresponding decrease in the cost of goodwill; and
– From the year ended 31 December 2005 onwards, goodwill is tested annually for impairment, as well as when there is an indication of impairment.

(v) ***Consolidation of special purpose entities***

A special purpose entity ("SPE") is an entity whose activities are being conducted on behalf of the Company and the Company has the decision making powers over the activities of the entity. Following the adoption of HKAS-Int 12 "Consolidation-Special Purpose Entities", the Group consolidates an entity when the substance of the relationship between the Company and that entity falls under the definition of a SPE.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.2 Adoption of new/revised HKFRS (continued)

(vi) ***Summary of effect on adopting new/revised HKFRS***

The following table sets out the increase/(decrease) in the consolidated profit and loss and the increase/(decrease) in the consolidated balance sheet items that have been made in these accounts following the adoption of new/revised HKFRS.

	Effect of adopting						
	HKFRS 2	HKFRS 3	HKAS 16		HKAS 39		
	Share-based compensation#	Goodwill amortisation^	Vessel component costs#	Residual values^	Financial instruments^	HKAS-Int 12 SPE#	Total
	US$'000	US$'000	US$'000	US$'000	US$'000	US$'000	US$'000
(a) Consolidated Profit and Loss Account							
Increase/(decrease) in profit attributable to shareholders							
For the year ended 31 December 2005:							
Turnover	–	–	–	–	–	56,048	56,048
Bunkers, port disbursements and amounts payable to other pool members	–	–	–	–	–	(56,048)	(56,048)
Depreciation of vessels	–	–	(5,121)	1,992	–	–	(3,129)
Drydocking costs	–	–	5,042	–	–	–	5,042
Share-based compensation	(3,990)	–	–	–	–	–	(3,990)
Fair value gains on financial instruments	–	–	–	–	4,617	–	4,617
Goodwill amortisation	–	1,772	–	–	–	–	1,772
Profit attributable to shareholders	(3,990)	1,772	(79)	1,992	4,617	–	4,312
Effect on earnings per share							
– basic (US cents)	(0.31)	0.14	(0.01)	0.16	0.36	–	0.34
– diluted (US cents)	(0.31)	0.14	(0.01)	0.16	0.36	–	0.34
For the year ended 31 December 2004:							
Turnover	–	–	–	–	–	67,978	67,978
Bunkers, port disbursements and amounts payable to other pool members	–	–	–	–	–	(67,978)	(67,978)
Depreciation of vessels	–	–	(2,802)	–	–	–	(2,802)
Drydocking costs	–	–	4,505	–	–	–	4,505
Share-based compensation	(1,660)	–	–	–	–	–	(1,660)
Profit attributable to shareholders	(1,660)	–	1,703	–	–	–	43
Effect on earnings per share							
– basic (US cents)	(0.15)	–	0.16	–	–	–	0.01
– diluted (US cents)	(0.15)	–	0.16	–	–	–	0.01

adjustments which take effect retrospectively

^ adjustments which take effect prospectively from 1 January 2005

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.2 Adoption of new/revised HKFRS (continued)

(vi) ***Summary of effect on adopting new/revised HKFRS (continued)***

	Effect of adopting					
	HKFRS 2	HKFRS 3	HKAS 16		HKAS 39	
	Share-based compensation#	Goodwill amortisation^	Vessel component costs#	Residual values^	Financial instruments^	Total
	US$'000	US$'000	US$'000	US$'000	US$'000	US$'000
(b) Consolidated Balance Sheet						
Increase/(decrease) in						
As at 31 December 2005:						
Fixed assets	–	–	(145)	1,992	–	1,847
Derivative assets/liabilities	–	–	–	–	3,449	3,449
Trade and other payables	–	–	–	–	(522)	(522)
Goodwill	–	1,772	–	–	–	1,772
Net assets	–	1,772	(145)	1,992	2,927	6,546
Reserves						
Share premium	1,691	–	–	–	–	1,691
Staff benefits reserve	3,959	–	–	–	–	3,959
Hedging reserve	–	–	–	–	(1,360)	(1,360)
Retained profits	(5,650)	1,772	(145)	1,992	4,287	2,256
Equity	–	1,772	(145)	1,992	2,927	6,546
As at 1 January 2005:						
Fixed assets	–	–	(66)	–	–	(66)
Derivative assets/liabilities	–	–	–	–	(330)	(330)
Net assets	–	–	(66)	–	(330)	(396)
Reserves						
Staff benefits reserve	1,660	–	–	–	–	1,660
Retained profits	(1,660)	–	(66)	–	(330)	(2,056)
Equity	–	–	(66)	–	(330)	(396)
As at 1 January 2004:						
Net assets – Fixed assets	–	–	(1,769)	–	–	(1,769)
Equity – Retained profits	–	–	(1,769)	–	–	(1,769)

adjustments which take effect retrospectively

^ adjustments which take effect prospectively from 1 January 2005

The adoption of HKFRS 2 resulted in a decrease in the Company's profit attributable to shareholders and a corresponding increase in the staff benefits reserve amounting to US$3,990,000 (2004: US$1,660,000).

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.3 Group accounting

(i) ***Consolidation***

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31 December.

Subsidiaries are those entities (including special purpose entities and unincorporated entities) in which the Company, directly or indirectly, controls more than one half of the voting power; has the power to govern the financial and operating policies; has the power to appoint or remove a majority of the members of the board of directors; or has the right to cast a majority of votes at the meetings of the board of directors.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from the effective date of acquisition or up to the effective date of disposal, as appropriate.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the profit and loss account.

All significant intercompany transactions, balances and unrealised gains or losses within the Group are eliminated on consolidation. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet, the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

(ii) ***Jointly controlled entities***

A jointly controlled entity is a contractual arrangement whereby the Group and other parties undertake an economic activity which is subject to joint control and none of the participating parties has unilateral control over the economic activity.

The Group's interests in jointly controlled entities are accounted for by the equity method. The consolidated profit and loss account includes the Group's share of the results of jointly controlled entities for the year, and the consolidated balance sheet includes the Group's share of the net assets of the jointly controlled entities and goodwill on acquisition.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.4 Fixed assets

(i) ***Vessels under construction***

Vessels under construction are stated at cost and are not depreciated. All direct costs relating to the construction of vessels, including finance costs on related borrowed funds during the construction period, are capitalised as cost of fixed assets.

(ii) ***Vessels and vessel component costs***

Vessels are stated at cost less accumulated depreciation and accumulated impairment losses. The cost of an asset comprises its purchase price and any directly attributable cost of bringing the asset to its working condition for its intended use. Cost may also include transfers from equity of any gains/losses on qualifying cash flow hedges of foreign currency purchases of vessels.

Subsequent costs are included in the vessel's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the profit and loss account during the financial period in which they are incurred.

Depreciation of vessels is calculated to write off their cost less accumulated impairment losses after allowing for their estimated residual values on a straight-line basis over their estimated useful lives of 25 years from the date of first registration.

Vessel component costs include the cost of major components which are usually replaced or renewed in connection with a drydocking when a vessel is delivered. The assets are stated at cost less accumulated depreciation and accumulated impairment losses. The vessel component costs are depreciated over the estimated period to the first drydocking. The Group subsequently capitalises drydocking costs as they are incurred and depreciates these costs over their estimated useful lives.

(iii) ***Other fixed assets***

Other fixed assets, comprising motor vehicles, leasehold improvements and furniture, fixtures and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. They are depreciated at rates sufficient to write off their cost less accumulated impairment losses over their estimated useful lives on a straight-line basis. The estimated useful lives are summarised as follows:

Furniture, fixtures and equipment	4 to 5 years
Leasehold improvements	5 – 6 years or the remaining period of the lease, whichever is shorter
Motor vehicles	4 years

Major costs incurred in restoring fixed assets to their normal working condition are charged to the profit and loss account. Improvements are capitalised and depreciated over their expected useful lives to the Group.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.4 Fixed assets (continued)

(iv) ***Residual values and useful lives***

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

(v) ***Gain or loss on disposal***

The gain or loss on disposal of fixed assets is the difference between the net sales proceeds and the carrying amount of the relevant assets, and is recognised in the profit and loss account.

2.5 Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition.

Goodwill is tested for impairment annually or if events or changes in circumstances indicating that it might be impaired and is carried at cost less accumulated impairment losses. Impairment losses on goodwill cannot be reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity being sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing.

2.6 Impairment of assets

Assets that have an indefinite useful life are not subject to amortisation, but are tested for impairment, at least annually and are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

2.7 Leases

(i) ***Operating leases***

(a) *Where the Group is the lessor*

When the Group leases out assets under operating leases, the assets are included in the balance sheet and, where applicable, are depreciated in accordance with the Group's depreciation policies as set out in Note 2.4 above. Revenue arising from assets leased out under operating leases is recognised on a straight-line basis over the lease periods.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.7 Leases (continued)

(i) ***Operating leases (continued)***

(b) *Where the Group is the lessee*

Leases where substantially all the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases net of any incentives received from the leasing company are charged to the profit and loss account on a straight-line basis over the lease periods.

(ii) ***Finance leases***

(a) *Where the Group is the lessor*

When vessels are leased out under finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivables and the present value of the receivables is recognised as unearned finance lease interest income.

(b) *Where the Group is the lessee*

Leases of assets where the Group has substantially all the risks and rewards of ownership are accounted for as finance leases. Finance leases are capitalised at the lease's inception at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Each lease payment is split between a repayment of the liability on the balance sheet and a finance charge. The corresponding rental obligations, net of finance charges, are included in current and non-current borrowings. The finance charge element of the rental obligations is expensed in the profit and loss account over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The assets accounted for as finance leases are depreciated over the shorter of their estimated useful lives or the lease periods. However, where there is a reasonable probability that the Group will continue to enjoy the economic benefits of those assets over their estimated useful lives, they are depreciated over this longer period.

(iii) ***Sale and leaseback transactions – where the Group is the lessee***

A sale and leaseback transaction involves the sale of an asset by the vendor and the leasing of the same asset back to the vendor. The lease payments and the sale price are usually interdependent as they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved and the economic and commercial substance of the whole arrangement.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.7 Leases (continued)

(iii) ***Sale and leaseback transactions – where the Group is the lessee (continued)***

(a) *Finance leases*

Sale and leaseback arrangements that result in the Group retaining the majority of the risks and rewards of ownership of assets are accounted for as finance leases. Any excess of sales proceeds over the carrying amount shall be deferred and amortised over the lease term. Each lease payment is allocated between the repayment of finance lease liabilities and finance charges so as to achieve a constant periodic rate of interest on the finance lease liability outstanding.

(b) *Operating leases*

Sale and leaseback arrangements that result in substantially all of the risks and rewards of ownership of assets being transferred to the lessor are accounted for as operating leases. Payments made under operating leases net of any incentives received from the leasing company are charged to the profit and loss account on a straight-line basis over the lease periods.

2.8 Financial assets

From 1 January 2004 to 31 December 2004:

The Group classified its investments in securities, other than subsidiaries and jointly controlled entities, as investment securities. These were stated at cost less any provision for impairment losses.

The carrying amounts of individual financial assets are reviewed at each balance sheet date to assess whether the fair values have declined below the carrying amounts. When a decline other than a temporary decline has occurred, the carrying amount of such securities is reduced to its fair value. The impairment loss is recognised as an expense in the profit and loss account. This impairment loss is written back to the profit and loss account when the circumstances and events that led to the write-downs or write-offs cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

From 1 January 2005 onwards:

The Group classifies its financial assets in the following three categories:

(i) Financial assets at fair value through profit or loss;
(ii) Available-for-sale financial assets; and
(iii) Loans and receivables.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.8 Financial assets (continued)

The classification depends on the purpose of these financial assets. Management determines their classification at the time of initial recognition and re-evaluates their classification at every reporting date.

Purchases and sales of financial assets are recognised on the date of trade, when the Group commits to purchase or sell the assets. Financial assets are initially recognised at fair value plus transaction costs, and are excluded when the rights to receive cash flows from the financial assets have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

The fair values of quoted investments and derivative financial instruments are based on current bid prices. If the market for a financial asset is not active, the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, and discounted cash flow analysis.

(i) ***Financial assets at fair value through profit or loss***

This category includes derivative financial assets that are initially recognised at fair value at the date the contracts are entered into and are periodically restated at their fair values. Realised and unrealised gains and losses arising from changes in the fair values are included in the profit and loss account in the period in which they arise, except where the derivatives qualify for cashflow hedge accounting or hedge the net investment in a foreign operation, in which case recognition of any resultant gain or loss depends on the nature of the item being hedged.

Assets in this category are classified as current assets if they are either held for trading or are expected to be realised within 12 months from the balance sheet date.

(ii) ***Available-for-sale financial assets***

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any other categories. They are stated at fair value and unrealised gains and losses arising from changes in the fair value are recognised in equity reserves in the balance sheet.

Assets in this category are included in non-current assets unless management intends to dispose them within 12 months from the balance sheet date.

(iii) ***Loans and receivables***

Loans and receivables are recognised initially at fair value, net of transaction costs incurred. Transaction costs are incremental costs that are directly attributable to the acquisition or repayment of a borrowing. Loans and receivables are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit and loss account over the period of the loans and receivables using the effective interest method.

Loans and receivables are classified as current assets if they are either held for trading or are expected to be realised within 12 months of the balance sheet date.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.8 Financial assets (continued)

(iii) ***Loans and receivables (continued)***

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivables. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. Loans and receivables are included in trade and other receivables in the balance sheet.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the profit and loss account – is removed from equity and recognised in the profit and loss account. Impairment losses recognised in the profit and loss account on equity instruments are not reversed through the profit and loss account.

2.9 Derivative financial instruments and hedging activities

From 1 January 2004 to 31 December 2004:

Derivative financial instruments are designated as "hedging" or "non-hedging" instruments. The transactions that, according to the Group's policy for risk management, are able to meet the conditions for hedge accounting are classified as "hedging" transactions; the others, although set up for the purpose of managing risk, have been designated as "trading" transactions. The Group records derivative financial instruments at cost. The gains and losses on maturity of derivative financial instruments are included in the profit and loss account to match the underlying hedged transactions where relevant.

For interest rate instruments designated as hedges, the interest rate differential is included in the profit and loss account, in financial income and expenses, offsetting the effects of the hedged transaction. Derivative financial instruments designated as trading instruments are valued at year end market value, and the difference between the nominal contract value and fair value is recorded in the profit and loss account under financial income and expenses. During 2004, the Group did not hold any derivative financial instruments designated as trading instruments.

From 1 January 2005 onwards:

Derivative financial instruments are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either: (i) hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedge); (ii) hedges of highly probable forecast transactions (cash flow hedges); or (iii) hedges of net investments in foreign operations.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.9 Derivative financial instruments and hedging activities (continued)

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions satisfy the effectiveness test in offsetting changes in fair values or cash flows of hedged items.

The fair values of various derivative instruments used for hedging purposes are disclosed in Note 11. Movements on the hedging reserve in shareholders' equity are shown in Note 19.

(a) ***Fair value hedge***

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the profit and loss account, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

(b) ***Cash flow hedge***

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the profit and loss account.

Amounts accumulated in equity are transferred to the profit and loss account in the periods when the hedged item will be recorded in the profit and loss account (for instance when the forecast cash flows that is hedged takes place). However, when the forecast transaction that is hedged results in the recognition of a non-financial asset (for example, inventory) or a liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the profit and loss account. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the profit and loss account.

(c) ***Derivatives that do not qualify for hedge accounting***

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the profit and loss account.

2.10 Inventories

Inventories mainly comprise bunkers on board vessels, lubricating oil and marine products. Inventories are stated at the lower of cost and net realisable value. Costs are calculated on first-in first-out basis. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.11 Trade and other receivables

Trade receivables represent freight and charter-hire receivables which are recognised initially at fair value and subsequently measured at amortised cost using effective interest method, less provision for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect the amount due according to the original terms of that receivable. The amount of the provision is recognised in the profit and loss account.

2.12 Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and deposits held with banks.

2.13 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

2.14 Employee benefits

(i) ***Bonuses***

The Group recognises a liability for bonuses when there is a contractual obligation and the amount can be estimated reliably.

(ii) ***Retirement benefit obligations***

Mandatory Provident Fund Scheme

The Group operates the Mandatory Provident Fund Scheme (the "MPF Scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for those employees employed under the jurisdiction of the Hong Kong Employment Ordinance. The MPF Scheme is a defined contribution scheme, the assets of which are held in separate trustee-administered funds.

Under the MPF scheme, the employer and its employees are each required to make contributions to the scheme at 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. 5% of relevant income vests immediately upon the completion of service in the relevant service period, while the remaining portion vests in accordance with the scheme's vesting scales. 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.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.14 Employee benefits (continued)

(ii) ***Retirement benefit obligations (continued)***

Other defined contribution schemes

The Group also operates a number of defined contribution retirement schemes outside Hong Kong. The assets of these schemes are generally held in separate administered funds. The retirement benefit schemes are generally funded by payments from employees and by the relevant Group companies, taking into account the contribution rates according to local statutory requirements.

The Group's contributions to the defined contribution retirement schemes are expensed as incurred and are reduced by contributions forfeited by those employees who leave the schemes prior to contributions fully vesting.

(iii) ***Share-based compensation***

The fair value of the employee services received in exchange for the grant of the share options and restricted share awards is recognised as an expense in the profit and loss account.

The total amount to be expensed over the vesting period is determined with reference to the fair value of the share options and restricted share awards granted. At each balance sheet date, the Company revises its estimates of the number of share options that are expected to become exercisable and the number of restricted share awards that become vested. It recognises the impact of the revision of original estimates, if any, in the profit and loss account, and a corresponding adjustment to equity in the balance sheet will be made over the remaining vesting periods.

The proceeds received, net of any directly attributable transaction costs, are credited to share capital and share premium accounts when the share options are exercised and when the restricted share awards are vested.

2.15 Share capital

Ordinary shares are classified as equity. Costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Where any Group company purchases the Company's equity share capital, the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.16 Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Transaction costs are costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability, including fees and commissions paid to agents, advisers, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Borrowings are subsequently stated at amortised costs; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit and loss account over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

2.17 Contingent liabilities and contingent assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

Contingent liabilities are not recognised but are disclosed in the notes to the accounts. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group.

Contingent assets are not recognised but are disclosed in the notes to the accounts when an inflow of economic benefits is probable. When an inflow is virtually certain, an asset is recognised.

2.18 Revenue recognition

(i) ***Ship chartering***

The Group generates revenue from shipping activities, the principal source of which is derived from the International Handybulk Carriers ("IHC") Pool which is regarded as a special purpose entity of the Group.

Revenues from the IHC Pool are derived from a combination of voyage charters, time charters and contracts of affreightment and are recognised on an accruals basis.

(ii) ***Ship management***

Ship management income is recognised when the services are rendered.

(iii) ***Others***

Interest income is recognised on a time-proportion basis using the effective interest method.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.18 Revenue recognition (continued)

(iii) ***Others (continued)***

Finance lease interest income is recognised over the term of the lease using the net investment method, based on a constant periodic rate of return.

Dividend income is recognised when the right to receive payment is established.

2.19 Translation of foreign currencies

(i) ***Functional and presentation currency***

Items included in the accounts of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated accounts are presented in United States Dollars, which is the Company's functional and presentation currency.

(ii) ***Transactions and balances***

Transactions in foreign currencies are translated into the functional currency using the exchange rates prevailing at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account, except when deferred in equity as qualifying cash flow hedges.

(iii) ***Group companies***

For all the Group's entities that have a functional currency different from the presentation currency, their balance sheets are translated at the rates of exchange ruling at the balance sheet date whilst their profit and loss accounts are translated at average rates. Exchange differences are dealt with as movements in reserves.

2.20 Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction, or production of an asset that necessarily takes a substantial period of time to get ready for its intended use are capitalised as part of the cost of that asset.

All other borrowing costs are charged to the profit and loss account in the year in which they are incurred.

2.21 Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

NOTES TO THE ACCOUNTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.22 Dividends

Dividend distributions to the Company's shareholders are recognised as liabilities in the Group's accounts in the period in which the dividends are declared.

The dividend declared after the year is not reflected as a dividend payable in the accounts, but will be reflected as an appropriation of retained profits for the following year.

3. FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Group's financial risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.

Under the Group's risk management programme, each department identifies and documents their key tasks and the risks associated with their tasks. The risks are summarised in a risk register where they are graded by likelihood and consequence and where the procedures and controls for managing the risks are recorded.

(a) ***Market risk***

(i) *Foreign exchange risk*

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to United States Dollars. Foreign exchange risk arises from future commercial transactions, assets and liabilities and net investments, denominated in foreign currencies. To mitigate risks arising from fluctuations in exchanges rates, forward foreign exchange contracts are used to hedge the currency exposure of the Group.

(ii) *Price risk*

The Group's result may be significantly affected by the fluctuation of bunker prices which are a significant cost to the Group. The bunker prices are determined by the market demand and supply. To mitigate risks arising from fluctuations in bunker prices, forward bunker contracts are used to hedge the exposure of the Group.

(b) ***Credit risk***

The Group has no significant concentrations of credit risk. It has policies in place to ensure that sales of services are provided to customers with an appropriate credit history. No credit terms are normally given to customers. In relation to voyage-related trade receivables, the due date depends on the date of completion of the voyage and the finalisation of post disbursements and other voyage-related charges.

The Group manages its exposure to derivative counter-parties by taking into account their financial strength.

NOTES TO THE ACCOUNTS

3. FINANCIAL RISK MANAGEMENT (CONTINUED)

3.1 Financial risk factors (continued)

(c) ***Liquidity risk***

The Group manages its liquidity risk by ensuring it has sufficient liquid cash balances to meet its payment obligations as they fall due. The Group maintains good working relations with its ship finance banks and ensures compliance with the covenants as stipulated in the loans and finance lease agreements.

(d) ***Cash flow and fair value interest rate risk***

Long term borrowings at variable interest rates expose the Group to cash flow interest rate risk and those at fixed rates expose the Group to fair value interest rate risk.

The Group manages its cash flow interest rate risk by using certain interest rate hedging instruments from time to time. Details of long term borrowings and interest rate swaps, are set out in Note 11.

3.2 Fair value estimation

Financial instruments held by the Group are mainly over-the-counter derivatives which are not traded in an active market. The fair value of forward foreign exchange contracts is determined using forward exchange market rates at the balance sheet date. The fair value of other financial instruments is based on the market price quoted by dealers as at the balance sheet date.

The fair value of financial assets and liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next year are:

(i) Goodwill impairment

Note 7 contains information about the assumptions and their risk factors relating to impairment of goodwill.

NOTES TO THE ACCOUNTS

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

(ii) Residual values of fixed assets

The residual values of the Group's assets are defined as the estimated amounts that the Group would currently obtain from disposal of the assets, after deducting the estimated costs of disposals, as if the assets were already of the age and in the conditions expected at the end of their useful lives.

The Group estimates residual values of its vessels by reference to the lightweight tonnes of the vessels provided by the shipyard and the average demolition steel price of similar vessels, of the Far East market and Indian Sub-Continent market, over the preceding year.

(iii) Useful lives of vessels and vessel component costs

Useful lives of the Group's vessels and vessel component costs are defined as the period over which they are expected to be available for use by the Group. The estimation of the useful life is a matter of judgement based on the experience of the Group with similar vessels.

The Group estimates useful life of its vessels by reference to the average historical useful life of the same class of vessels, expected usage of the vessels, expected repair and maintenance programme, and technical or commercial obsolescence arising from changes or improvements in the vessel market.

The Group estimates the useful life of its vessel component costs by reference to the average historical periods between two drydockings of vessels of similar age, and expected usage of the vessel until its next drydocking.

(iv) Classification of leases

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership. The Group classifies its leases into either finance lease or operating lease taking account of the spirit, intention, and application of HKAS 17 "Leases".

Taking into account the market conditions at the inception of the lease, the period of the lease, the flexibility of exercising purchase options, if any, attached to the lease and on a balance of probability, management's assessment is that for those leases that they have ultimately treated as finance leases, the arrangements were such that they transfer ownership of the assets to the Group by the end of the term of the arrangements, or the purchase options, if any, attached to the arrangements, were sufficiently attractive as to make it reasonably certain that they would be exercised. On the contrary, for those leases that have been treated as operating leases, management's assessment is that the arrangements were such that the leases would not transfer ownership of the assets to the Group by the end of the term of the arrangements, or that it was not reasonably certain that the purchase options, if any, attached to the arrangements would be exercised.

NOTES TO THE ACCOUNTS

5. TURNOVER AND SEGMENT INFORMATION

The Group is principally engaged in the provision of dry bulk shipping services through the operation of a fleet of vessels. Turnover recognised during the year is as follows:

	2005 US$'000	(restated) 2004 US$'000
Turnover		
Freight and charter-hire	**422,638**	292,740
Ship management income	**11,066**	9,504
	433,704	302,244
Bunkers, port disbursements and other charges	**(131,492)**	(61,033)
Amounts payable to other pool members[1]	**(37,529)**	(52,328)
Time charter equivalent earnings	**264,683**	188,883

[1] This is net of bunkers, port disbursements and other charges of US$19.6 million (2004: US$15.7 million).

On 1 January 2005, the Group adopted HKAS-Int 12 "Consolidation-Special Purpose Entities" resulting in a change in the Group's accounting for the IHC Pool. Previously, revenues from the IHC Pool were based on the number of pool points attributable to the Group's owned and chartered-in vessels participating in the pool, whereas now the Group consolidates such activities in full. This change is applied to previous accounting periods but there is no change in the way time charter equivalent earnings are calculated.

In arriving at time charter equivalent earnings, the IHC Pool paid to other pool members freight and charter hire, net of bunkers, port disbursement and other charges which were calculated based on the number of pool points attributable to the vessels participating in the pool owned by the other pool members.

Primary reporting format – business segments

The Group previously presented two major segments: ship chartering and ship management. However, for the year ended 31 December 2005, the Group no longer presents a ship management segment as the Group's business is dominated by the provision of dry bulk shipping services. Ship management no longer forms a significant part of the Group's business.

Secondary reporting format – geographical segments

The Directors consider that the nature of the provision of dry bulk shipping services, which are carried out internationally, and the way in which costs are allocated, preclude a meaningful allocation of operating profit to specific geographical segments. Accordingly, geographical segment information is not presented.

NOTES TO THE ACCOUNTS

6. FIXED ASSETS

	Group					
	Vessels and vessel component costs US$'000	Vessels under construction US$'000	Leasehold improvements US$'000	Furniture, fixtures and equipment US$'000	Motor vehicles US$'000	Total US$'000
Cost:						
At 1 January 2004, as previously reported	218,013	3,075	–	–	–	221,088
Prior year adjustment for vessel component costs under HKAS 16	(121)	–	–	–	–	(121)
At 1 January 2004, as restated	217,892	3,075	–	–	–	220,967
Additions	245,633	28,145	22	577	70	274,447
Acquisition of subsidiaries	64,500	24,231	193	503	–	89,427
Write off of fixed assets	(2,750)	–	–	–	–	(2,750)
Disposals	–	–	–	(88)	(12)	(100)
Reclassification	35,700	(35,700)	–	–	–	–
At 31 December 2004, as restated	560,975	19,751	215	992	58	581,991
Accumulated depreciation:						
At 1 January 2004, as previously reported	20,311	–	–	–	–	20,311
Prior year adjustment for vessel component costs under HKAS 16	1,648	–	–	–	–	1,648
At 1 January 2004, as restated	21,959	–	–	–	–	21,959
Charge for the year	18,276	–	192	202	–	18,670
Write off of fixed assets	(2,750)	–	–	–	–	(2,750)
Disposals	–	–	–	(16)	–	(16)
At 31 December 2004, as restated	37,485	–	192	186	–	37,863
Net book value:						
At 31 December 2004, as restated	523,490	19,751	23	806	58	544,128
At 31 December 2003, as restated	195,933	3,075	–	–	–	199,008

NOTES TO THE ACCOUNTS

6. FIXED ASSETS (CONTINUED)

	Group					
	Vessels and vessel component costs US$'000	Vessels under construction US$'000	Leasehold improvements US$'000	Furniture, fixtures and equipment US$'000	Motor vehicles US$'000	Total US$'000
Cost:						
At 1 January 2005, as previously reported	559,341	19,751	215	992	58	580,357
Prior year adjustment for vessel component costs under HKAS 16	1,634	–	–	–	–	1,634
At 1 January 2005, as restated	560,975	19,751	215	992	58	581,991
Additions	67,390	51,436	1,764	651	–	121,241
Write off of fixed assets	(2,903)	–	(346)	(92)	–	(3,341)
Disposals	(142,104)	–	(12)	(157)	–	(142,273)
Reclassification	67,304	(67,304)	–	–	–	–
At 31 December 2005	550,662	3,883	1,621	1,394	58	557,618
Accumulated depreciation:						
At 1 January 2005, as previously reported	35,785	–	192	186	–	36,163
Prior year adjustment for vessel component costs under HKAS 16	1,700	–	–	–	–	1,700
At 1 January 2005, as restated	37,485	–	192	186	–	37,863
Charge for the year	28,701	–	516	335	12	29,564
Write off of fixed assets	(2,903)	–	(346)	(92)	–	(3,341)
Disposals	(10,676)	–	(5)	(96)	–	(10,777)
At 31 December 2005	52,607	–	357	333	12	53,309
Net book value:						
At 31 December 2005	498,055	3,883	1,264	1,061	46	504,309
At 31 December 2004, as restated	523,490	19,751	23	806	58	544,128

As at 31 December 2005, the aggregate cost and accumulated depreciation of the vessel component costs amounted to US$10,730,000 (2004: US$9,134,000) and US$4,416,000 (2004: US$2,279,000) respectively and were included in the vessels and vessel component costs.

As at 31 December 2005, the aggregate cost and accumulated depreciation of the vessels and vessel component costs held by the Group under finance leases amounted to US$310,083,000 (2004: US$Nil) and US$26,291,000 (2004: US$Nil) respectively.

NOTES TO THE ACCOUNTS

7. GOODWILL

	2005 US$'000	2004 US$'000
Cost:		
At the beginning of the year	26,585	–
Elimination of accumulated amortisation under HKFRS 3	(1,329)	–
Acquisition of subsidiaries	–	26,585
At the end of the year	25,256	26,585
Accumulated amortisation:		
At the beginning of the year	1,329	–
Elimination of accumulated amortisation under HKFRS 3	(1,329)	
Amortisation *(Note 22)*	–	1,329
At the end of the year	–	1,329
Net book value:		
At the end of the year	25,256	25,256
At the beginning of the year	25,256	–

The Group tests annually whether goodwill has suffered any impairment, in accordance with the accounting policy stated in Note 2.5. The Group's business is dominated by ship chartering. As a result, the carrying amount of goodwill acquired through acquisitions is solely allocated to this segment for impairment testing.

The recoverable amount of the ship chartering segment has been determined based on a value-in-use calculation which in turn is based on financial projections of the Group. The discounted rate applied to the cash flow projections is 7.7%.

Based on the impairment testing of goodwill, in the opinion of the Directors, no impairment provision is considered necessary for the balance of the Group's goodwill.

Key assumptions used in value-in-use calculations:

The following describes each key assumption on which management has based its cash flow projections to undertake impairment testing of goodwill:

(a) Budgeted turnover was projected with reference to i) the expected earnings from ship chartering, and ii) the expected number of revenue days of the Group's fleet.

(b) Budgeted operating expenses were projected with reference to i) the expected number of revenue days of the Group's fleet, and ii) the age of the Group's fleet.

(c) Budgeted finance costs were projected with reference to i) the expected future interest rates, ii) the expected size of the Group's fleet, and iii) the expected borrowings.

(d) For the business environment, there will be no material change in the existing political, legal, regulatory, fiscal or economic conditions, bases or rates of taxation or duties in Hong Kong, or any of the countries in which the Group operates or in which the Group companies are incorporated or registered.

NOTES TO THE ACCOUNTS

8. SUBSIDIARIES

	Company	
	2005	2004
	US$'000	US$'000
Non-current		
Unlisted investments, at cost	**223,931**	130,762
Loans advanced to subsidiaries *(Note a)*	**–**	101,257
	223,931	232,019
Current		
Amounts due from subsidiaries *(Note b)*	**121,280**	39,750
	345,211	271,769

(a) As at 31 December 2004, the loans advanced to subsidiaries were unsecured, interest free and were not repayable within one year.

(b) The amounts due from subsidiaries are unsecured, interest free and have no fixed terms of repayment. The carrying amounts approximate their fair values.

Details of principal subsidiaries of the Group as at 31 December 2005 are set out in Note 32.

9. INTERESTS IN JOINTLY CONTROLLED ENTITIES

	Group	
	2005	2004
	US$'000	US$'000
Share of net assets	**7,138**	8,338
Loan to a jointly controlled entity	**1,000**	500
	8,138	8,838

The carrying amount of the loan to a jointly controlled entity approximates its fair value. The loan is unsecured, non-interest bearing and not repayable within one year.

NOTES TO THE ACCOUNTS

9. INTERESTS IN JOINTLY CONTROLLED ENTITIES (CONTINUED)

Details of the jointly controlled entities of the Group at 31 December 2005 are as follows:

Name	Place of Incorporation/ operation	Issued and fully paid up share capital	Interest in ownership/ voting power/ profit sharing	Principal activities
Asia Logistics Group Limited (formerly Pacific Basin Logistics Limited)	The British Virgin Islands/Hong Kong	4 shares of US$1 each	50%/50%/50%	Vessel chartering
Pacific Basin Bulker (No. 103) Corporation	Republic of Liberia	200 class 'B' shares of US$21,917.8 each	63.5%/50%/63.5%	Investment holding
China Line Shipping Limited 中外船務有限公司	Hong Kong/ International	2 shares of HK$1 each	63.5%/50%/63.5%	Vessel owning and chartering
Oriental Maritime Shipping Limited	The British Virgin Islands	10 shares of US$1 each	50%/50%/50%	Investment holding
Oriental Maritime Chartering Limited	The British Virgin Islands/The People's Republic of China ("PRC")	10 shares of US$1 each	50%/50%/50%	Vessel chartering
Claire Shipping Limited	Hong Kong/ International	1 share of HK$1	50%/50%/50%	Vessel owning and chartering
Star Pacific Bulk Shipping Limited	The British Virgin Islands	100 shares of US$1 each	50%/50%/50%	Investment holding
Star Pacific Bulk Chartering (HK) Limited	Hong Kong	1 share of HK$1	50%/50%/50%	Vessel chartering
Star Pacific Bulk Chartering (UK) Limited	England and Wales	1 share of GBP1	50%/50%/50%	Vessel chartering
Tai Hua Ship Management (Shanghai) Limited 太華船舶管理(上海)有限公司	PRC	US$200,000 (registered capital)	50%/50%/50%	Provision of ship management services

NOTES TO THE ACCOUNTS

9. INTERESTS IN JOINTLY CONTROLLED ENTITIES (CONTINUED)

Name	Place of Incorporation/ operation	Issued and fully paid up share capital	Interest in ownership/ voting power/ profit sharing	Principal activities
Tai Hua Ship Management (HK) Limited 太華船舶管理(香港)有限公司	Hong Kong	2 shares of HK$1 each	50%/50%/50%	Provision of ship management services
Pacific Basin Projects Limited	The British Virgin Islands	100 shares of US$1 each	50%/50%/50%	Provision of material supply and marine transportation activities

All jointly controlled entities are held indirectly by the Company.

An analysis of the Group's effective share of assets, liabilities, income and expenses of the jointly controlled entities is set out below:

	2005 US$'000	2004 US$'000
Assets:		
Non-current assets	**11,851**	15,895
Current assets	**5,734**	2,763
	17,585	18,658
Liabilities:		
Long term liabilities	**(5,867)**	(9,871)
Current liabilities	**(4,580)**	(449)
	(10,447)	(10,320)
Net assets	**7,138**	8,338
Income	**28,257**	4,204
Expenses	**(24,766)**	(1,710)
Share of profits less losses	**3,491**	2,494

NOTES TO THE ACCOUNTS

10. AVAILABLE-FOR-SALE FINANCIAL ASSETS/INVESTMENT SECURITIES

	Group	
	2005	2004
	US$'000	US$'000
Non-current assets		
Unlisted equity securities	**–**	200
Current assets		
Unlisted equity securities	**200**	–

The carrying amount of available-for-sale financial assets approximates its fair value.

There were no additions, disposals or impairment provisions on available-for-sale financial assets in 2005.

The investment securities were reclassified as available-for-sale financial assets in accordance with HKAS 32 "Financial Instruments: Disclosure and Presentation".

11. DERIVATIVE ASSETS AND LIABILITIES

	Group 31 December 2005	
	Assets	**Liabilities**
	US$'000	**US$'000**
Derivatives that do not qualify for hedge accounting:		
Interest rate swaps *(Note a)*	**709**	**–**
Bunker swap and forward contracts *(Note b)*	**4,280**	**–**
Forward freight agreement *(Note c)*	**–**	**180**
Cash flow hedge:		
Forward foreign exchange contracts *(Note d)*	**–**	**1,360**
Total	**4,989**	**1,540**
Less: non-current portion of		
Bunker swap and forward contracts	**(3,382)**	**–**
Forward foreign exchange contracts	**–**	**(1,360)**
Current portion	**1,607**	**180**

(a) Interest rate swaps

At 31 December 2005, the Group had agreements with banks to hedge against three-month floating rate LIBOR payments in connection with the Group's long term bank facilities, detailed as follows:

(i) A notional amount of approximately US$110 million (2004: US$121 million) with the floating rate capped at approximately 4.9% per annum. These agreements expire in July 2007; and

NOTES TO THE ACCOUNTS

11. DERIVATIVE ASSETS AND LIABILITIES (CONTINUED)

(a) Interest rate swaps (continued)

(ii) A notional amount of approximately US$55 million (2004: US$61 million) with the floating rate swapped to fixed rates of approximately 3.5% per annum. These fixed rates are knocked out to the floating rate if the floating rate exceeds 5% but are capped if the floating rate reaches 7%. These agreements expire in July 2009.

At 1 January 2005, the total fair values of interest rate swaps were liabilities of US$306,000.

(b) Bunker swap and forward contracts

At 31 December 2005, the Group had outstanding bunker swap and forward contracts to buy approximately 82,900 (2004: 96,500) metric tonnes ("mt") of bunkers at prices which range from US$182 to US$322 per mt (2004: range from US$165 to US$223 per mt), and which expire through December 2008. The commitments were entered into to hedge for fluctuations in bunker prices in connection with the Group's long term cargo contract commitments.

At 1 January 2005, the total fair values of bunker swap and forward contracts were liabilities of US$24,000.

(c) Forward freight agreement

At 31 December 2005, the Group had an outstanding forward freight agreement to buy the 90 days Baltic Handymax Index at a price of approximately US$19,194 per day, and which expires on March 2006. The commitment was entered into to hedge for fluctuations in freight revenues in connection with the Group's expected cargo contract commitments.

(d) Forward foreign exchange contracts

At 31 December 2005, the Group had outstanding forward foreign exchange contracts with a bank to buy approximately Yen2.5 billion and simultaneously to sell US$24.8 million for an acquisition of a vessel denominated in Japanese Yen. These contracts expire through December 2007.

Gains and losses in equity on forward foreign exchange contracts as of 31 December 2005 will be released to the profit and loss account in two years from the balance sheet date.

NOTES TO THE ACCOUNTS

12. TRADE AND OTHER RECEIVABLES

	Group	
	2005	2004
	US$'000	US$'000
Non-current receivables		
Finance lease receivables – gross	**20,063**	–
Less: unearned finance lease income	**(6,730)**	–
Finance lease receivables – net *(Note a)*	**13,333**	–
Current receivables		
Finance lease receivables – gross	**3,444**	–
Less: unearned finance lease income	**(1,635)**	–
Finance lease receivables – net *(Note a)*	**1,809**	–
Trade receivables – gross	**10,531**	7,850
Less: provision for impairment of trade receivables	**(841)**	(195)
Trade receivables – net *(Note b)*	**9,690**	7,655
Other receivables	**5,028**	6,434
Prepayments	**4,909**	4,081
Amount due from a related company *(Note c)*	**–**	118
Amounts due from jointly controlled entities *(Note c)*	**3,607**	1,820
	25,043	20,108

The carrying amounts of trade and other receivables approximate their fair values.

(a) At 31 December 2005, the Group leased out a vessel under finance lease. Under the terms of the lease, the charterer has the obligation to purchase the vessel at the end of the lease period.

The effective interest rate for the finance lease receivables was fixed for the lease period at approximately 11.3%.

The gross receivables, unearned finance income and the net receivables from finance lease as at 31 December 2005 are as follows:

	Group	
	2005	2004
	US$'000	US$'000
Gross receivables from finance leases:		
Not later than one year	**3,444**	–
Later than one year but not later than five years	**10,048**	–
Later than five years	**10,015**	–
	23,507	–
Less: unearned future finance income on finance leases	**(8,365)**	–
	15,142	–

NOTES TO THE ACCOUNTS

12. TRADE AND OTHER RECEIVABLES (CONTINUED)

	Group	
	2005	2004
	US$'000	US$'000
Net receivables from finance leases:		
Not later than one year	**1,809**	–
Later than one year but not later than five years	**5,101**	–
Later than five years	**8,232**	–
	15,142	–

(b) At 31 December 2005, the ageing analysis of trade receivables is as follows:

	Group	
	2005	2004
	US$'000	US$'000
Less than 30 days	**7,636**	4,717
31 – 60 days	**603**	1,978
61 – 90 days	**593**	347
Over 90 days	**858**	613
	9,690	7,655

No credit terms are normally given to customers. In relation to voyage-related trade receivables, the due date depends on the date of completion of the voyage and the finalisation of port disbursements and other voyage-related charges.

There is no concentration of credit risk with respect to trade receivables, as the Group has a large number of customers, internationally dispersed.

(c) The amounts due from a related company and jointly controlled entities are unsecured, interest free and have no fixed terms of repayment.

NOTES TO THE ACCOUNTS

13. INVENTORIES

	Group	
	2005	2004
	US$'000	US$'000
Bunkers	**7,606**	5,078
Lubricating oil	**1,512**	1,462
Marine products	**20**	24
	9,138	6,564

The carrying amounts of inventories approximate their fair values.

14. PLEDGED/RESTRICTED BANK DEPOSITS

	Group	
	2005	2004
	US$'000	US$'000
Non-current assets		
Restricted bank deposits *(Note a)*	**1,200**	4,150
Current assets		
Pledged bank deposits in connection with:		
Forward foreign exchange facility *(Note b)*	**130**	130
Restricted deposits *(Note c)*	**300**	1,780
	430	1,910

(a) Bank deposits are pledged to lending banks as securities for facilities granted to the Group *(Note 17(b))*.

(b) The amount was held as security with a bank in connection with a forward foreign exchange facility line of US$1,000,000 granted to the Group.

(c) The 2005 amount was pledged for a bank guarantee issued to a forward freight agreement counter party with effective interest rate of 3.9% (2004:1.9%) and average maturity of 165 days (2004: 65 days). The 2004 amounts were retained by certain banks in relation to loan repayments.

The carrying amounts of pledged/restricted bank deposits approximate their fair values.

15. UNPLEDGED BANK BALANCES AND CASH

At 31 December 2005, US$21,000,000 (2004: US$Nil) of the unpledged bank balances and cash of the Group were placed on short term deposits with effective interest rate of 4.1% and an average maturity of 7 days.

At 31 December 2005, none (2004: Nil) of the unpledged bank balances and cash of the Company were placed on short term deposits.

NOTES TO THE ACCOUNTS

16. TRADE AND OTHER PAYABLES

	Group 2005 US$'000	2004 US$'000
Trade payables	**2,869**	3,730
Accruals and other payables	**31,780**	24,179
Receipts in advance	**9,918**	7,406
	44,567	35,315

At 31 December 2005, the ageing analysis of trade payables is as follows:

	Group 2005 US$'000	2004 US$'000
Less than 30 days	**1,437**	2,225
31 – 60 days	**248**	346
61 – 90 days	**326**	392
Over 90 days	**858**	767
	2,869	3,730

The carrying amounts of trade and other payables approximate their fair values.

17. LONG TERM BORROWINGS

	Group 2005 US$'000	(restated) 2004 US$'000
Non-current		
Finance lease liabilities *(Note a)*	**301,973**	–
Secured bank loans *(Note b)*	**–**	334,103
	301,973	334,103
Current		
Finance lease liabilities *(Note a)*	**14,912**	–
Secured bank loans *(Note b)*	**–**	36,021
	14,912	36,021
Total long term borrowings	**316,885**	370,124

The carrying amounts of long term borrowings approximate their fair values.

NOTES TO THE ACCOUNTS

17. LONG TERM BORROWINGS (CONTINUED)

(a) At 31 December 2005, the Group leased vessels under finance leases. Under the terms of the leases, the Group has options to purchase the vessels at any time throughout the charter periods. Lease liabilities are effectively secured as the rights to the leased vessels revert to the lessors in the event of default.

The effective interest rates on finance lease payables were fixed for the leases periods which range from approximately 6.6% to 7.0%.

The gross liabilities, future finance charges and net liabilities under finance leases as at 31 December 2005 are as follows:

	Group	
	2005	2004
	US$'000	US$'000
Gross liabilities under finance leases:		
Not later than one year	**36,138**	–
Later than one year but not later than five years	**144,465**	–
Later than five years	**294,499**	–
	475,102	–
Less: future finance charges on finance leases	**(158,217)**	–
	316,885	–

	Group	
	2005	2004
	US$'000	US$'000
Net liabilities under finance leases:		
Not later than one year	**14,912**	–
Later than one year but not later than five years	**71,074**	–
Later than five years	**230,899**	–
	316,885	–

NOTES TO THE ACCOUNTS

17. LONG TERM BORROWINGS (CONTINUED)

(b) Bank loans as at 31 December 2005 have been fully prepaid. The bank loans as at 31 December 2004 were secured, inter alia, by the following:

(i) Mortgages over all the Group's vessels and one vessel under construction of net book value totalling US$534,200,000 and certain bank deposits of US$4,150,000;

(ii) Assignment of earnings, insurances and requisition compensation in respect of the vessels; and

(iii) Charges over the shares of certain vessel owning subsidiaries.

The maturity of the Group's bank loans is as follows:

	Group	
		(restated)
	2005	2004
	US$'000	US$'000
Within one year	–	36,021
In the second year	–	33,521
In the third to fifth year	–	97,869
After the fifth year	–	202,713
	–	370,124

18. SHARE CAPITAL

Authorised share capital

	No. of shares of US$0.10 each					
	Class A	Class B	Class C	Ordinary shares	Total	US$'000
Upon incorporation	–	–	–	120,000	120,000	12
Conversion of shares	53,333.40	63,999.96	2,666.64	(120,000)	–	–
Increase in share capital on 15 March 2004	533,280,666.60	639,935,600.04	26,663,733.36	–	1,199,880,000	119,988
Increase in share capital on 1 April 2004	1,066,668,000.00	1,279,999,200.00	53,332,800.00	–	2,400,000,000	240,000
Conversion of shares on 14 July 2004	(1,600,002,000.00)	(1,919,998,800.00)	(79,999,200.00)	3,600,000,000	–	–
At 31 December 2004 and 2005	–	–	–	3,600,000,000	3,600,000,000	360,000

NOTES TO THE ACCOUNTS

18. SHARE CAPITAL (CONTINUED)

Issued share capital

	No. of shares of US$0.10 each					
	Class A	Class B	Class C	Ordinary shares	Total	US$'000
Allotted and issued nil paid	53,333.40	63,999.96	2,666.64	–	120,000	–
Issue of shares upon the exchange of shares completed on 30 March 2004	353,341,281.00	424,008,738.00	17,666,881.00	–	795,016,900	79,502
Repurchase of shares	(53,329.40)	(63,990.96)	(2,682.64)	–	(120,003)	–
Conversion of shares on 14 July 2004	(353,341,285.00)	(424,008,747.00)	(17,666,865.00)	795,016,897	–	–
Issue of shares for acquisition of subsidiaries	–	–	–	221,993,712	221,993,712	22,199
Issue of shares upon initial public offering on 14 July 2004	–	–	–	250,000,000	250,000,000	25,000
At 31 December 2004 and 1 January 2005	–	–	–	1,267,010,609	1,267,010,609	126,701
Shares purchased by trustee of the LTIS *(Note b)*	–	–	–	(5,000,000)	(5,000,000)	(2,252)
Shares transferred to employees under the LTIS *(Note b)*	–	–	–	4,799,999	4,799,999	2,162
Shares issued under the LTIS *(Note a)*	–	–	–	15,730,000	15,730,000	1,573
At 31 December 2005	–	–	–	1,282,540,608	1,282,540,608	128,184

(a) Share options

Share options were granted to Directors, senior management and certain employees on 14 July 2004 and 5 April 2005. The exercise prices of the granted options are equal to the market prices at the respective dates of grant. The options granted vest over three years and five years respectively, as follows:

Date of grant	Number of share options	Exercise price in HK$ per share	Vesting conditions	Expiry date
14 July 2004	55,500,000	2.500	in equal amounts on 14 July 2005, 2006 and 2007	14 July 2014
5 April 2005	5,000,000	3.875	in equal amounts on 5 April 2006, 2007, 2008, 2009 and 2010	5 April 2015

NOTES TO THE ACCOUNTS

18. SHARE CAPITAL (CONTINUED)

(a) Share options (continued)

Movements in the number of share options outstanding during the year and their related weighted average exercise prices are as follows:

	2005 Average exercise price in HK$ per share	2005 Number of options '000	2004 Average exercise price in HK$ per share	2004 Number of options '000
At 1 January	**2.500**	**55,500**	–	–
Granted	**3.875**	**5,000**	2.500	55,500
Exercised	**2.500**	**(15,730)**	–	–
At 31 December	**2.654**	**44,770**	2.500	55,500

Out of the 44,770,000 outstanding options (2004: 55,500,000 options), 5,170,000 options (2004: Nil) were exercisable at a price of HK$2.50. Options exercised in 2005 resulted in 15,730,000 shares (2004: Nil) being issued at HK$2.50 each (2004: HK$Nil). The related weighted average share price at the time of exercise was HK$3.87 (2004: HK$Nil) per share.

The fair value of options granted during the year determined by an independent third party valuer using the binomial model was US$0.8 million (2004: US$5.9 million).

Key assumptions used in the valuation of the options granted on 14 July 2004 and 5 April 2005 include (i) an expected dividend yield of 8% per annum, (ii) volatility of share price of 50% per annum, (iii) a risk-free rate of interest of 4% and 4.1% per annum on the respective grant dates, (iv) that the employees will exercise their share options if the share price is 100% above the exercise price, and (v) an expected rate of leaving service of eligible employees after the vesting date of 0.4% per annum.

(b) Restricted share awards

Following the approval of shareholders at a special general meeting on 8 June 2005, the Company's share option scheme (now called the "Long Term Incentive Scheme" or "LTIS") was amended to allow the Company to award restricted shares and restricted units as an alternative or in addition to granting share options. The trustee of the LTIS (which under New HKFRS is regarded as a special purpose entity of the Company) subsequently acquired five million shares of the Company on the Stock Exchange at a total cost of US$2,252,000 of which 4.8 million share awards were granted to certain employees on 8 June 2005. The shares granted were then transferred to the employees leaving 0.2 million shares held by the trustee at 31 December 2005.

The awards granted vest over a period of three or five years as follows:

Date of grant	Number of share awards	Vesting conditions
8 June 2005	3,333,333	in equal amounts on 5 April 2006, 2007, 2008, 2009 and 2010
8 June 2005	1,466,666	in equal amounts on 30 November 2005, 2006 and 2007

The fair value of the restricted share awards granted during the year was determined with reference to the market price of those shares at the date of grant.

NOTES TO THE ACCOUNTS

19. RESERVES

	Group						
	Share premium US$'000	**Merger reserve** US$'000	**Staff benefits reserve** US$'000	**Hedging reserve** US$'000	**Exchange reserve** US$'000	**Retained profits** US$'000	**Total** US$'000
Balance at 1 January 2004							
As previously reported	–	(56,606)	–	–	–	15,988	(40,618)
Prior year adjustment for the adoption of HKAS 16 for vessel component costs *(Note 2.2(vi))*	–	–	–	–	–	(1,769)	(1,769)
As restated	–	(56,606)	–	–	–	14,219	(42,387)
Exchange differences arising on translation of the accounts of foreign subsidiaries	–	–	–	–	54	–	54
Premium on issue of shares for acquisition of subsidiaries	59,114	–	–	–	–	–	59,114
Premium on issue of shares upon initial public offering	55,128	–	–	–	–	–	55,128
Share issuing expenses	(8,448)	–	–	–	–	–	(8,448)
Share-based compensation *(Note 23)*	–	–	1,660	–	–	–	1,660
Profit attributable to shareholders	–	–	–	–	–	103,555	103,555
Dividends paid *(Note 27)*	–	–	–	–	–	(62,807)	(62,807)
Balance at 31 December 2004, as restated	105,794	(56,606)	1,660	–	54	54,967	105,869
Representing:							
2004 Proposed final dividend						25,990	
Others						28,977	
Retained profits as at 31 December 2004, as restated						54,967	

NOTES TO THE ACCOUNTS

19. RESERVES (CONTINUED)

	Group						
	Share premium US$'000	Merger reserve US$'000	Staff benefits reserve US$'000	Hedging reserve US$'000	Exchange reserve US$'000	Retained profits US$'000	Total US$'000
Balance at 1 January 2005							
As previously reported	105,794	(56,606)	–	–	54	56,693	105,935
Prior year adjustment for share-based compensation under HKFRS 2 *(Note 2.2(vi))*	–	–	1,660	–	–	(1,660)	–
Prior year adjustment for the adoption of HKAS 16 for vessel component costs *(Note 2.2(vi))*	–	–	–	–	–	(66)	(66)
Opening balance adjustment arising from the initial adoption of HKAS 39 *(Note 2.2(vi))*	–	–	–	–	–	(330)	(330)
As restated	105,794	(56,606)	1,660	–	54	54,637	105,539
Exchange differences arising on translation of the accounts of foreign subsidiaries	–	–	–	–	(56)	–	(56)
Shares transferred to employees under the LTIS to staff benefits reserve *(Note 18)*	–	–	(2,162)	–	–	–	(2,162)
Shares issued under the LTIS *(Note 18)*	5,159	–	(1,691)	–	–	–	3,468
Fair value losses of cash flow hedges *(Note 11(d))*	–	–	–	(1,360)	–	–	(1,360)
Share-based compensation *(Note 23)*	–	–	3,990	–	–	–	3,990
Profit attributable to shareholders	–	–	–	–	–	147,143	147,143
Dividends paid *(Note 27)*	–	–	–	–	–	(75,472)	(75,472)
Balance at 31 December 2005	110,953	(56,606)	1,797	(1,360)	(2)	126,308	181,090
Representing:							
2005 Proposed final dividend						57,948	
Others						68,360	
Retained profits as at 31 December 2005						126,308	

NOTES TO THE ACCOUNTS

19. RESERVES (CONTINUED)

	Company			
	Share premium US$'000	**Staff benefits reserve** US$'000	**Retained profits** US$'000	**Total** US$'000
Balance at 10 March 2004 (date of incorporation)	–	–	–	–
Premium on issue of shares for acquisition of subsidiaries	59,114	–	–	59,114
Premium on issue of shares upon initial public offering	55,128	–	–	55,128
Share issuing expenses	(8,448)	–	–	(8,448)
Share-based compensation *(Note 23)*	–	1,660	–	1,660
Profit attributable to shareholders	–	–	56,060	56,060
Dividends paid *(Note 27)*	–	–	(31,342)	(31,342)
Balance at 31 December 2004, as restated	105,794	1,660	24,718	132,172
Representing:				
2004 Proposed final dividend			25,990	
Others			(1,272)	
Retained profits as at 31 December 2004, as restated			24,718	
Balance at 1 January 2005, as previously reported	**105,794**	**–**	**26,378**	**132,172**
Prior year adjustment for share-based compensation under HKFRS 2	**–**	**1,660**	**(1,660)**	**–**
As restated	**105,794**	**1,660**	**24,718**	**132,172**
Shares transferred to employees under the LTIS to staff benefits reserve *(Note 18)*	**–**	**(2,162)**	**–**	**(2,162)**
Shares issued under the LTIS *(Note 18)*	**5,159**	**(1,691)**	**–**	**3,468**
Share-based compensation *(Note 23)*	**–**	**3,990**	**–**	**3,990**
Profit attributable to shareholders *(Note 26)*	**–**	**–**	**155,074**	**155,074**
Dividends paid *(Note 27)*	**–**	**–**	**(75,472)**	**(75,472)**
Balance at 31 December 2005	**110,953**	**1,797**	**104,320**	**217,070**
Representing:				
2005 Proposed final dividend			**57,948**	
Others			**46,372**	
Retained profits as at 31 December 2005			**104,320**	

As at 31 December 2005, distributable reserves of the Company amounted to US$104.3 million (2004: US$24.7 million).

NOTES TO THE ACCOUNTS

20. OTHER INCOME

	2005 US$'000	2004 US$'000
Bank interest income	392	78
Finance lease interest income	343	–
Dividend income from investment securities	–	227
Other income	–	126
	735	431

21. DIRECT COSTS

	2005 US$'000	(restated) 2004 US$'000
Vessel operating costs	31,900	19,298
Charter-hire expenses for vessels	29,459	18,659
Depreciation of vessels	28,701	18,276
Shore-based overheads	20,727	11,017
Cost of marine products sold and consulting services	3,965	1,762
	114,752	69,012

Vessel operating costs comprise all technical expenses that are incurred in operating the owned and finance leased vessels. These include crew expenses, stores and spare parts, repairs and maintenance expenses, insurance and other miscellaneous running costs.

NOTES TO THE ACCOUNTS

22. OPERATING PROFIT

Operating profit is stated after charging/(crediting) the following:

	2005 US$'000	(restated) 2004 US$'000
Auditors' remuneration		
– Audit	660	252
– Non-audit	293	74
Amortisation of goodwill	–	1,329
Bunkers consumed	48,894	22,882
Cost of marine products sold	2,085	1,762
Depreciation for		
– owned vessels	26,241	18,276
– leased vessels	2,460	–
– other owned fixed assets	863	394
Employee benefit expenses including directors' emoluments *(Note 23)*	23,439	13,364
Lubricating oil consumed	2,269	1,509
Net exchange losses	77	74
Operating lease expenses for		
– vessels	29,459	18,659
– land and buildings	1,662	585
Provision for impairment of trade receivables[1]	646	195
Realised gains on derivative instruments not qualifying as hedges:		
– Bunker swap and forward contracts	(2,863)	–
Unrealised (gains)/losses on derivative instruments not qualifying as hedges:		
– Forward freight agreement	180	–
– Bunker swap and forward contracts	(4,304)	–

[1] Included in "General and administrative expenses"

NOTES TO THE ACCOUNTS

23. EMPLOYEE BENEFIT EXPENSES (INCLUDING DIRECTORS' EMOLUMENTS)

	2005 US$'000	(restated) 2004 US$'000
Directors' fees	**235**	124
Salaries and bonus	**18,528**	11,334
Share-based compensation	**3,990**	1,660
Retirement benefit costs	**686**	246
	23,439	13,364

(a) Directors' emoluments

The Company's Board is currently composed of five non-executive Directors and four executive Directors.

The aggregate amount of emoluments payable to the Directors of the Company during the year was US$5.0 million (2004: US$2.6 million). Details of Directors' remuneration are disclosed in sections 2, 3 and 4 of the Remuneration Report on pages 48 and 49.

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include four (2004: three) Directors whose emoluments are reflected in note (a) above and amounted to US$4.8 million (2004: US$2.5 million). The emoluments payable to the remaining individual (2004: two) during the year were US$0.8 million (2004: US$1.1 million). Further details are disclosed in section 6 of the Remuneration Report on page 50.

24. FINANCE COSTS

	2005 US$'000	2004 US$'000
Interest on bank loans	**11,548**	8,670
Interest on finance leases	**4,161**	–
Loan arrangement fees	**1,657**	1,188
Other finance charges	**588**	357
Fair value loss /(gain) on interest rate swaps contracts:		
– realised	**1,001**	–
– unrealised	**(1,015)**	–
	17,940	10,215

NOTES TO THE ACCOUNTS

25. TAXATION

Hong Kong profits tax has been provided at the rate of 17.5% (2004: 17.5%) on the estimated assessable profit for the year.

Taxation on overseas profits has been calculated on the estimated assessable profit for the year at the rates of taxation prevailing in the countries in which the Group operates.

The amount of taxation charged to the consolidated profit and loss account represents:

	2005	2004
	US$'000	US$'000
Current taxation		
Hong Kong profits tax	**548**	406
Overseas tax	**231**	79
	779	485

Below is the reconciliation between taxation in the consolidated profit and loss account and the aggregate tax at the domestic rates applicable to profits in the respective territories concerned.

	2005	2004
	US$'000	US$'000
Profit before taxation	**147,922**	104,040
Aggregate tax at the rates of taxation prevailing in the countries in which the Group operates	**751**	813
Income not subject to taxation	**(333)**	(549)
Expenses not deductible for taxation purposes	**361**	221
Taxation charge	**779**	485

There was no material unprovided deferred taxation at 31 December 2005 (2004: US$Nil).

26. PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The profit attributable to shareholders is dealt with in the accounts of the Company to the extent of US$155,074,000 (Period from 10 March 2004 (date of incorporation) to 31 December 2004: US$56,060,000).

NOTES TO THE ACCOUNTS

27. DIVIDENDS

	2005 **US$'000**	2004 US$'000
Dividends attributable to the previous year, approved and paid during the year:		
Final dividend paid in 2005 in respect of the year ended 31 December 2004 of 16 HK cents (equivalent to 2 US cents) per share	**–**	25,990
Dividends attributable to the year:		
Proposed final dividend declared and payable after the year ended 31 December 2005 of 35 HK cents (equivalent to 4.5 US cents) per share *(Note a)*	**57,948**	–
Interim dividends declared and		
– paid in 2005 of 30 HK cents (equivalent to 3.9 US cents) per share	**49,482**	–
– paid in 2005 of 8 HK cents (equivalent to 1 US cent) per share	**–**	12,995
– paid in 2004 to shareholders of the Company immediately prior to listing of 2 US cents per share *(Note b)*	**–**	18,347
Dividend declared and paid in 2004 by companies now comprising the Group to the then shareholders prior to listing	**–**	31,465
	107,430	88,797

(a) The dividend, which was declared on 6 March 2006, was not reflected as a dividend payable in these accounts, but will be reflected as an appropriation of retained profits for the year ending 31 December 2006.

(b) On 14 July 2004, the Directors declared an interim dividend of 2 US cents per share to the Company's shareholders on the morning of the date of listing, not including the public shareholders.

NOTES TO THE ACCOUNTS

28. EARNINGS PER SHARE

(a) Basic earnings per share

Basic earnings per share are calculated by dividing the Group's profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year, excluding the shares held by the trustee of the Company's LTIS.

	2005	(restated) 2004
Profit attributable to shareholders (US Dollars in thousands)	**147,143**	103,555
Weighted average number of ordinary shares in issue (in thousands)	**1,270,944**	1,079,319
Basic earnings per share	**US 11.58 cents**	US 9.59 cents
Equivalent to	**HK 89.72 cents**	HK 74.80 cents

(b) Diluted earnings per share

Diluted earnings per share are calculated by dividing the Group's profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year after adjusting for the number of potential dilutive ordinary shares granted under the Company's LTIS.

	2005	(restated) 2004
Profit attributable to shareholders (US Dollars in thousands)	**147,143**	103,555
Weighted average number of ordinary shares in issue (in thousands)	**1,270,944**	1,079,319
Adjustments for share options (in thousands)	**12,483**	4,925
Weighted average number of ordinary shares for diluted earnings per share (in thousands)	**1,283,427**	1,084,244
Diluted earnings per share	**US 11.46 cents**	US 9.55 cents
Equivalent to	**HK 88.79 cents**	HK 74.49 cents

5,000,000 share options under the LTIS were not included in the calculation of diluted earnings per share as they are antidilutive for the year.

NOTES TO THE ACCOUNTS

29. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of operating profit to cash generated from operations

	Group	
		(restated)
	2005	2004
	US$'000	US$'000
Operating profit	**162,371**	111,761
Adjustment for:		
Interest income	**(735)**	(78)
Depreciation	**29,564**	18,670
Gain on disposal of fixed assets	**(23,516)**	–
Amortisation of goodwill	**–**	1,329
Dividend income from investment securities	**–**	(227)
Exchange differences	**(56)**	54
Unrealised gains on derivatives that do not qualify for hedge accounting excluding interest rate swaps	**(4,124)**	–
Share-based compensation	**3,990**	1,660
Operating profit before working capital changes	**167,494**	133,169
Increase in inventories	**(2,574)**	(1,449)
Decrease/(increase) in trade and other receivables	**176**	(2,205)
Increase in trade and other payables	**8,924**	1,437
Cash generated from operations	**174,020**	130,952

(b) Analysis of cash and cash equivalents

	Group	
	2005	2004
	US$'000	US$'000
Bank balances and cash	**83,711**	47,711
Less: restricted and pledged bank deposits	**(1,630)**	(6,060)
	82,081	41,651

(c) Major non-cash transaction

In 2005, the Group leased out one of its owned vessels on a long term basis, which was classified as a finance lease. The carrying value of the vessel at the inception of the transaction was US$13.7 million with a corresponding finance lease receivables recognised in the balance sheet of US$15.5 million.

NOTES TO THE ACCOUNTS

30. COMMITMENTS

(a) Capital commitments

	Group	
	2005	2004
	US$'000	US$'000
Contracted but not provided for in relation to		
– vessel acquisitions and shipbuilding contracts	**158,878**	105,705
– investment in a jointly controlled entity	**1,792**	–
– land and building	**907**	–
	161,577	105,705

Capital commitments that fall due not later than one year amounted to US$52.6 million.

(b) Commitments under operating leases

(i) ***The Group as the lessee***

The Group had future aggregate minimum lease payments under non-cancellable operating leases as follows:

	Land and buildings US$'000	**Vessels US$'000**	**Total US$'000**
At 31 December 2005			
Not later than one year	**1,134**	**52,824**	**53,958**
Later than one year but not later than five years	**1,107**	**129,613**	**130,720**
Later than five years	**–**	**40,677**	**40,677**
	2,241	**223,114**	**225,355**

	Land and buildings US$'000	Vessels US$'000	Total US$'000
At 31 December 2004			
Not later than one year	960	17,600	18,560
Later than one year but not later than five years	1,663	16,733	18,396
	2,623	34,333	36,956

NOTES TO THE ACCOUNTS

30. COMMITMENTS (CONTINUED)

(b) Commitments under operating leases (continued)

(ii) The Group as the lessor

The Group had future aggregate minimum lease receipts under non-cancellable operating leases of vessels as follows:

	2005 US$'000	2004 US$'000
Not later than one year	34,196	22,772
Later than one year but not later than five years	26,208	17,859
	60,404	40,631

31. SIGNIFICANT RELATED PARTY TRANSACTIONS

Significant related party transactions, which were carried out in the normal course of the Group's business, were as follows:

(a) Purchases of services

	2005 US$'000	2004 US$'000
Insurance premium paid to Sun Hing Insurance Brokers Limited ("Sun Hing") *(Note i)*	245	199
Amounts payable to China Line Shipping Limited *(Note ii)*	6,204	5,175

(i) The Group entered into certain insurance contracts through Sun Hing, a related company in which 35% of its shareholding was held indirectly by Lee Kwok Yin, Simon, a Director and a shareholder of the Company.

(ii) The Group paid to China Line Shipping Limited, a jointly controlled entity freight and charter hire, net of bunkers, port disbursement and other charges which were calculated based on the vessel's pool points.

(b) Sales of services

	2005 US$'000	2004 US$'000
Charter hire income received from Asia Logistics Group Limited *(Note i)*	3,476	4,415
Commission income received from Asia Logistics Group Limited *(Note ii)*	211	–

(i) The Group leased out certain vessels to Asia Logistics Group Limited, a jointly controlled entity.

(ii) The Group derived commission income from fixing of vessels for Asia Logistics Group Limited, a jointly controlled entity.

NOTES TO THE ACCOUNTS

31. SIGNIFICANT RELATED PARTY TRANSACTIONS (CONTINUED)

(c) Key management compensation (including Directors' emoluments)

	2005	2004
	US$'000	US$'000
Directors' fees	**235**	124
Salary and bonus	**4,613**	3,226
Retirement benefit costs	**11**	6
Share-based compensation	**2,090**	753
Termination benefits	**154**	–
	7,103	4,109

32. PRINCIPAL SUBSIDIARIES

At 31 December 2005, the Company has direct and indirect interest in the following subsidiaries:

Company	Place of incorporation/ operation	Issued and fully paid share capital	Interest held 2005 %	Interest held 2004 %	Principal activities
Shares held directly:					
PB Management Holding Limited	The British Virgin Islands	12,313 shares of US$1 each	**100**	100	Investment holding
PB Vessels Holding Limited	The British Virgin Islands	101,118,775 shares of US$1 each	**100**	100	Investment holding
Shares held indirectly:					
Abbot Point Limited	Hong Kong/International	1 share of HK$1	**100**	100	Vessel owning and chartering
Beckley (HK) Limited	Hong Kong/International	3,000,010 ordinary shares of US$1 each	**100**	100	Vessel owning and chartering
Bernard (BVI) Limited	The British Virgin Islands/ International	5,100,100 shares of US$0.01 each	**100**	100	Vessel owning and chartering
Cape Knox Limited	Hong Kong/International	1 share of HK$1	**100**	100	Vessel owning

NOTES TO THE ACCOUNTS

32. PRINCIPAL SUBSIDIARIES (CONTINUED)

Company	Place of incorporation/ operation	Issued and fully paid share capital	Interest held 2005 %	Interest held 2004 %	Principal activities
Delphic Shipping (BVI) Limited	The British Virgin Islands/ International	100 shares of US$0.01 each	**100**	100	Vessel owning and chartering
Eastern Venture Corporation	The Republic of Liberia	10 Class 'A' shares of US$1 each, 58 Class 'B' shares of US$50,000 each	**100**	100	Investment holding
Everclear Shipping (BVI) Limited	The British Virgin Islands/ International	3,100,100 shares of US$0.01 each	**100**	100	Vessel owning and chartering
Flinders Island Limited	Hong Kong/International	1 share of HK$1	**100**	100	Vessel owning and chartering
Foreview (HK) Limited	Hong Kong/International	10 Class 'A' shares of US$1 each, 2,500,000 Class 'B' shares of US$1 each	**100**	100	Vessel owning and chartering
Foreview Holdings Limited	Hong Kong	2,500,000 ordinary shares of US$1 each	**100**	100	Investment holding
Gold River Shipping Limited	Hong Kong/International	1 share of HK$1	**100**	100	Vessel owning and chartering
Gwenyth Shipping (BVI) Limited	The British Virgin Islands/ International	100 shares of US$0.01 each	**100**	100	Vessel owning and chartering
IHC Chartering (UK) Limited	England & Wales	2 shares of GBP1 each	**100**	100	Provision of shipping management services
International Handybulk Carriers Management Limited	The British Virgin Islands/ Hong Kong	10 shares of US$1 each	**100**	100	Provision of shipping management services

NOTES TO THE ACCOUNTS

32. PRINCIPAL SUBSIDIARIES (CONTINUED)

Company	Place of incorporation/ operation	Issued and fully paid share capital	Interest held 2005 %	Interest held 2004 %	Principal activities
Judith Shipping (BVI) Limited	The British Virgin Islands/ International	3,800,100 shares of US$0.01 each	**100**	100	Vessel owning and chartering
Mount Rainier Limited	Hong Kong/International	1 share of HK$1	**100**	100	Vessel owning and chartering
Oak Harbour Limited	Hong Kong/International	1 share of HK$1	**100**	100	Vessel owning and chartering
Pacific Basin Chartering Limited	The British Virgin Islands/ Hong Kong	10 shares of US$1 each	**100**	100	Vessels chartering
Pacific Basin Ship Management Limited	Hong Kong	1 share of HK$1	**100**	100	Provision of ship management services
Pacific Basin Shipping (HK) Limited	Hong Kong	2 shares of HK$10 each	**100**	100	Provision of ship agency services
Pacific Basin Shipping (Australia) Pty Ltd	Australia	1 share of AUD1	**100**	100	Provision of shipping consulting services
Pacific Basin Shipping (UK) Limited	England & Wales	2 shares of GBP1 each	**100**	100	Provision of shipping consulting services
Pacific Basin Shipping (USA) Inc. [1]	The United States of America	100 shares of US$10 each	**100**	100	Provision of shipping management services
Pacific Basin Shipping Consulting (Shanghai) Limited [1 & 2]	PRC	US$200,000 (registered capital)	**100**	100	Provision of shipping consulting services

NOTES TO THE ACCOUNTS

32. PRINCIPAL SUBSIDIARIES (CONTINUED)

Company	Place of incorporation/ operation	Issued and fully paid share capital	Interest held 2005 %	Interest held 2004 %	Principal activities
PacMarine Services (HK) Limited	Hong Kong	2 shares of HK$1 each	**100**	100	Provision of surveying and consultancy services
PacMarine Services (UK) Limited [1]	England & Wales	1,000 shares of GBP1 each	**100**	100	Provision of surveying and consultancy services
PacMarine Services Pte. Ltd.	Singapore	1,000 shares of S$1 each	**100**	100	Provision of surveying and consultancy services
PMS Services Co., Ltd.	Korea	10,000 shares of 5,000 Won each	**100**	100	Provision of survey services
Taylor Shipping (BVI) Limited	The British Virgin Islands/ Hong Kong	10 shares of US$1 each	**100**	100	Vessel chartering
Union Bay Limited	Hong Kong/International	1 share of HK$1	**100**	100	Vessel owning
Verner Shipping (BVI) Limited	The British Virgin Islands/ Hong Kong	100 shares of US$0.01 each	**100**	100	Vessel chartering
Wharton Shipping Limited	The British Virgin Islands/ International	100 shares of US$0.01 each	**100**	100	Vessel owning and chartering
Bright Cove Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Crescent Harbour Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Eaglehill Trading Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering

NOTES TO THE ACCOUNTS

32. PRINCIPAL SUBSIDIARIES (CONTINUED)

Company	Place of incorporation/ operation	Issued and fully paid share capital	Interest held 2005 %	2004 %	Principal activities
Famous Time Group Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Future Sea Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Lake Joy Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Lake Stevens Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Good Shape Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Widen Holdings Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel owning and chartering
Pacific Basin Bulk Chartering Limited	The British Virgin Islands	1 share of US$1	**100**	–	COAs for non-handysize business
Pacific Basin Bulk Chartering (UK) Limited	England and Wales	1 share of GBP1	**100**	–	COAs for non-handysize business
Pacific Basin Chartering (No. 1) Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel chartering
Pacific Basin Chartering (No. 2) Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel chartering
Pacific Basin Chartering (No. 3) Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel chartering
Pacific Basin Chartering (No. 4) Limited	Hong Kong/International	1 share of HK$1	**100**	–	Vessel chartering

NOTES TO THE ACCOUNTS

32. PRINCIPAL SUBSIDIARIES (CONTINUED)

Company	Place of incorporation/ operation	Issued and fully paid share capital	Interest held 2005 %	Interest held 2004 %	Principal activities
Pacific Basin Chartering (No. 5) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 6) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 7) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 8) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 9) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 10) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 11) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 12) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 13) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 14) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 15) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 16) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering
Pacific Basin Chartering (No. 17) Limited	Hong Kong/International	1 share of HK$1	100	–	Vessel chartering

NOTES TO THE ACCOUNTS

32. PRINCIPAL SUBSIDIARIES (CONTINUED)

Company	Place of incorporation/ operation	Issued and fully paid share capital	Interest held 2005 %	2004 %	Principal activities
Pacific Basin Shipping (Canada) Limited	Province of British Columbia, Canada	1 common share without par value	**100**	–	Provision of shipping consulting service
Pacific Basin Shipping (Germany) GmbH	Germany	1 share of EUR25,000	**100**	–	Provision of shipping consulting and advisory service
PB Markets Limited	The British Virgin Islands	1 share of US$1	**100**	–	Forward freight agreement chartering party
IHC Chartering Limited	The British Virgin Islands	10 shares of US$1 each	**100**	100	Provision of shipping management services
Pacific Basin Agencies Limited	Hong Kong/International	1 share of HK$1	**100**	100	Holding company of a branch in Japan

[1] The accounts of these subsidiaries have not been audited by PricewaterhouseCoopers. The aggregate net assets and losses for the year attributable to the shareholders of the Group amounted to approximately US$66,000 (2004: US$71,000) and US$91,000 (2004: US$191,000) respectively.

[2] Pacific Basin Shipping Consulting (Shanghai) Limited is a wholly foreign-owned enterprises established in the PRC, with registered capital of US$200,000 fully paid up by the Group.