

Notes to the Unaudited Condensed Consolidated Interim Financial Statements

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 unaudited condensed consolidated interim financial statements were approved for issue on 22 August 2006.

2 BASIS OF PREPARATION

These unaudited condensed consolidated interim financial statements are prepared in accordance with Hong Kong Accounting Standard (“HKAS”) No. 34 “Interim Financial Reporting” issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”). These unaudited condensed consolidated interim financial statements should be read in conjunction with the annual financial statements for the year ended 31 December 2005.

The accounting policies adopted are consistent with those of the annual financial statements for the year ended 31 December 2005. 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. The Group has assessed the impact of these New Standards and concluded that the adoption of these New Standards will not have a material impact on the Group’s financial statements.

3 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 six months ended 30 June 2006 was as follows:

	Six months ended 30 June	
		(restated)
	2006	2005
	US\$'000	US\$'000
Turnover		
Freight and charter-hire	232,793	222,355
Ship management income	6,647	6,563
	239,440	228,918
Bunkers, port disbursements and other charges	(88,544)	(66,907)
Amounts payable to other pool members (<i>Note</i>)	(10,499)	(21,096)
Time charter equivalent earnings	140,397	140,915

Note: Amounts payable to other pool members relate to freight and charter-hire, net of bunkers, port disbursements and other charges of US\$7.8 million (2005: US\$10.9 million) and 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's business is dominated by the provision of dry bulk shipping services, accordingly business segment information is not presented.

3 **TURNOVER AND SEGMENT INFORMATION (continued)**

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.

4 **CAPITAL EXPENDITURE AND DISPOSAL**

During the six months ended 30 June 2006, capital expenditure on vessel additions was US\$97.5 million (2005: US\$77.6 million) and on other property, plant and equipment was US\$1.1 million (2005: US\$2.1 million). No vessel and newbuildings were disposed of during the period, compared with the same period in 2005 when vessels and newbuildings with a net book value of US\$92.1 million were sold, resulting in a net profit of US\$12.2 million.

5 DERIVATIVE ASSETS AND LIABILITIES

	30 June 2006 US\$'000	31 December 2005 US\$'000
Derivative assets		
Derivative assets that do not qualify for hedge accounting:		
Interest-rate swap contracts (<i>Note (a)(i)</i>)	340	709
Bunker swap and forward contracts (<i>Note b</i>)	5,356	4,280
Forward freight agreements (<i>Note c</i>)	3,851	–
Cash flow hedge:		
Interest-rate swap contracts (<i>Note (a)(iii)</i>)	181	–
Total	<u>9,728</u>	<u>4,989</u>
Less: non-current portion:		
Bunker swap and forward contracts (<i>Note b</i>)	(1,202)	(3,382)
Forward freight agreements (<i>Note c</i>)	(368)	–
	<u>(1,570)</u>	<u>(3,382)</u>
Current portion	<u>8,158</u>	<u>1,607</u>
Derivative liabilities		
Derivative liabilities that do not qualify for hedge accounting:		
Bunker swap and forward contracts (<i>Note b</i>)	172	–
Forward freight agreements (<i>Note c</i>)	7,496	180
Cash flow hedge:		
Forward foreign exchange contracts (<i>Note d</i>)	1,126	1,360
Total	<u>8,794</u>	<u>1,540</u>
Less: non-current portion:		
Forward freight agreements (<i>Note c</i>)	(1,113)	–
Forward foreign exchange contracts (<i>Note d</i>)	(997)	(1,360)
	<u>(2,110)</u>	<u>(1,360)</u>
Current portion	<u>6,684</u>	<u>180</u>

5 DERIVATIVE ASSETS AND LIABILITIES (continued)

(a) Interest-rate swap contracts

At 30 June 2006, the Group had agreements with banks to hedge against six-month floating LIBOR ("Floating Rate") in connection with the Group's long term bank loans, detailed as follows:

- i) Effective from 2 January 2007, a notional amount of approximately US\$40 million with the Floating Rate swapped to a fixed rate of approximately 5.0% per annum. This fixed rate reverts to the Floating Rate minus approximately 1.0% per annum if the Floating Rate exceeds 6.0%. This agreement expires in January 2017.
- ii) Effective from 2 January 2007, a notional amount of approximately US\$20 million with the Floating Rate swapped to fixed rate of approximately 5.6% per annum. This agreement expires in January 2017. This instrument qualifies for hedge accounting. The change in the fair value was recognised directly in other reserves, under hedging reserve.

(b) Bunker swap and forward contracts

At 30 June 2006, the Group had outstanding bunker swap and forward contracts to buy approximately 69,400 (31 December 2005: 82,900) metric tonnes ("mt") of bunkers, and which expire through December 2007. The commitments were entered into to hedge against fluctuations in bunker prices in connection with the Group's long term cargo contract commitments.

(c) Forward freight agreements

At 30 June 2006, the Group had outstanding forward freight agreements to buy approximately 1,000 (31 December 2005: 90) days of Baltic Supramax Index, and which expire through December 2007. The Group also had outstanding forward freight agreements to sell approximately 1,000 (31 December 2005: Nil) days of Baltic Supramax Index, and which expire through December 2007. The Group enters into forward freight agreements as a method of managing its exposure to both its physical tonnage and cargo with regard to handysize and handymax vessels.

5 DERIVATIVE ASSETS AND LIABILITIES (continued)**(d) Forward foreign exchange contracts**

At 30 June 2006, 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 the acquisition of a vessel denominated in Japanese Yen. These contracts expire through December 2007. These instruments qualify for hedge accounting. The change in the fair value was recognised directly in other reserves, under hedging reserve.

6 TRADE AND OTHER RECEIVABLES

	30 June 2006 US\$'000	31 December 2005 US\$'000
Non-current		
Finance lease receivables – gross	18,647	20,063
Less: unearned finance lease income	(5,989)	(6,730)
Finance lease receivables – net	12,658	13,333
Current		
Finance lease receivables – gross	3,083	3,444
Less: unearned finance lease income	(1,539)	(1,635)
Finance lease receivables – net	1,544	1,809
Trade receivables – gross	11,524	10,531
Less: provision for impairment	(583)	(841)
Trade receivables – net	10,941	9,690
Other receivables	6,812	5,028
Prepayments	8,181	4,909
Amounts due from jointly controlled entities	482	3,607
	27,960	25,043

6 TRADE AND OTHER RECEIVABLES (continued)

At 30 June 2006, the ageing analysis of trade receivables is as follows:

	30 June 2006 US\$'000	31 December 2005 US\$'000
Less than 30 days	9,316	7,636
31 – 60 days	1,071	603
61 – 90 days	98	593
Over 90 days	456	858
	10,941	9,690

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.

7 TRADE AND OTHER PAYABLES

	30 June 2006 US\$'000	31 December 2005 US\$'000
Trade payables	9,314	2,869
Accruals and other payables	27,042	31,780
Receipts in advance	16,248	9,918
	52,604	44,567

7 TRADE AND OTHER PAYABLES (continued)

At 30 June 2006, the ageing analysis of trade payables is as follows:

	30 June 2006 US\$'000	31 December 2005 US\$'000
Less than 30 days	7,215	1,437
31 – 60 days	318	248
61 – 90 days	490	326
Over 90 days	1,291	858
	<u>9,314</u>	<u>2,869</u>

8 LONG TERM BORROWINGS

	30 June 2006 US\$'000	31 December 2005 US\$'000
Non-current		
Finance lease liabilities (Note a)	294,041	301,973
Secured bank loans (Note b)	61,208	–
	<u>355,249</u>	<u>301,973</u>
Current		
Finance lease liabilities (Note a)	15,442	14,912
Secured bank loans (Note b)	9,635	–
	<u>25,077</u>	<u>14,912</u>
Total long term borrowings	<u>380,326</u>	<u>316,885</u>

8 LONG TERM BORROWINGS (continued)

- (a) The maturities of the Group's finance lease liabilities are as follows:

	30 June 2006 US\$'000	31 December 2005 US\$'000
Not later than one year	15,442	14,912
Later than one year but not later than five years	73,490	71,074
Later than five years	220,551	230,899
	309,483	316,885

- (b) The bank loans are secured, inter alia, by the following:

- (i) Mortgages over certain owned vessels of net book value totalling US\$146,299,000 (2005: Nil);
- (ii) Assignment of earnings, insurances and requisition compensations in respect of the vessels; and
- (iii) Charges over the shares of certain vessel-owning subsidiaries.

The maturities of the Group's bank loans are as follows:

	30 June 2006 US\$'000	31 December 2005 US\$'000
Not later than one year	9,635	—
Later than one year but not later than two years	5,644	—
Later than two years but not later than five years	17,064	—
Later than five years	38,500	—
	70,843	—

9 SHARE CAPITAL

	Number of shares of US\$0.1 each	30 June 2006 US\$'000	31 December 2005 US\$'000
Authorised	3,600,000,000	360,000	360,000
Issued and fully paid			
At 1 January	1,282,540,608	128,184	126,701
Shares issued upon exercise of share options under the LTIS (<i>Note a</i>)	5,075,000	508	1,573
Shares purchased by trustee of the LTIS (<i>Note b</i>)	(2,465,000)	(1,217)	(2,252)
Shares transferred to employees upon granting of restricted share awards under the LTIS (<i>Note b</i>)	2,795,408	1,365	2,162
Shares transferred back to trustee upon lapse of restricted share awards under the LTIS (<i>Note b</i>)	(133,333)	(60)	—
At 30 June/31 December	1,287,812,683	128,780	128,184

9 SHARE CAPITAL (continued)

(a) Share options

Share options under the Company's Long Term Incentive Scheme ("LTIS") were granted to Directors, senior management and certain employees.

Movements in the number of share options outstanding during the six months ended 30 June 2006 and their related weighted average exercise prices are as follows:

	2006		2005	
	Average exercise price in HK\$ per share	Number of options '000	Average exercise price in HK\$ per share	Number of options '000
At 1 January	2.654	44,770	2.500	55,500
Granted	–	–	3.875	5,000
Exercised	2.500	(5,075)	2.500	(15,730)
Cancelled ¹	3.875	(5,000)	–	–
At 30 June/ 31 December	2.500	34,695	2.654	44,770

¹ Please refer to the Other Information section in this Interim Report for details.

The related weighted average share price at the time of exercise was HK\$3.58 (2005: HK\$3.87) per share.

9 SHARE CAPITAL (continued)**(b) Restricted share awards**

Restricted share awards under the LTIS were granted to Directors, senior management and certain employees. During the six months ended 30 June 2006, the trustee of the LTIS (which under Hong Kong Financial Reporting Standards is regarded as a special purpose entity of the Company) acquired 2,465,000 shares of the Company on the Stock Exchange at a total cost of US\$1,217,000. During the period, 133,333 shares formerly transferred to an employee lapsed and 2,795,408 restricted share awards were granted to certain employees. The shares granted were then transferred to the employees with the remaining 2,926 shares held by the trustee at 30 June 2006.

Movements in the number of unvested restricted share awards during the six months ended 30 June 2006 are as follows:

	2006 '000	2005 '000
At 1 January	4,311	–
Granted	2,795	4,800
Vested	(871)	(489)
Lapsed ¹	(133)	–
At 30 June/31 December	6,102	4,311

¹ Please refer to the Other Information section in this Interim Report for details.

9 SHARE CAPITAL (continued)

(b) Restricted share awards (continued)

The fair value of the restricted share awards granted during the six months ended 30 June 2006 was determined with reference to the market price of those shares at the grant date.

10 DIRECT COSTS

	Six months ended 30 June	
	2006	2005
	US\$'000	US\$'000
Charter-hire expenses on vessels	42,182	11,877
Vessel operating costs	16,787	14,176
Depreciation on vessels	14,309	15,351
Shore-based overheads	10,685	10,111
Cost of marine products sold and consulting services	911	1,884
	<u>84,874</u>	<u>53,399</u>

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

11 OPERATING PROFIT

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

	Six months ended 30 June	
	2006	2005
	US\$'000	US\$'000
Depreciation for		
– owned vessels	7,021	15,351
– leased vessels	7,288	–
– other owned property, plant and equipment	626	324
Bunkers consumed	38,514	20,859
Lubricating oil consumed	1,244	1,166
Employee benefit expenses including directors' emoluments	12,712	11,875
Operating lease expenses on		
– vessels	42,182	11,877
– land and buildings	793	825
Interest income ²	(1,868)	(107)
Gains on derivative instruments not qualifying as hedges		
– bunker swap and forward contracts ¹	(5,157)	(6,524)
– forward freight agreements ²	(4,650)	–
Losses on derivative instruments not qualifying as hedges		
– bunker swap and forward contracts ¹	1,771	58
– forward freight agreements ³	8,757	–

¹ Included in "Bunkers, port disbursements and amounts payable to other pool members"

² Included in "Other operating income"

³ Included in "Other operating expenses"

12 FINANCE COSTS

	Six months ended 30 June	
	2006	(restated) 2005
	US\$'000	US\$'000
Interest on bank loans	501	7,344
Interest on finance leases	10,626	–
Other finance charges	247	193
Fair value gains on interest rate swap contracts	(549)	(427)
Fair value losses on interest rate swap contracts	800	683
	<u>11,625</u>	<u>7,793</u>

13 TAXATION

Hong Kong profits tax has been provided at the rate of 17.5% (2005: 17.5%) on the estimated assessable profit for the period.

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

The amount of taxation charged to the unaudited condensed consolidated income statement represents:

	Six months ended 30 June	
	2006	2005
	US\$'000	US\$'000
Current taxation		
Hong Kong profits tax	319	425
Overseas tax	177	95
	<u>496</u>	<u>520</u>

14 DIVIDENDS

	Six months ended 30 June	
	2006	2005
	US\$'000	US\$'000
<hr/>		
<i>Dividends attributable to the previous financial year, approved and paid during the interim period:</i>		
Final dividend in respect of the year ended 31 December 2005 of HK 35 cents or US 4.5 cents per share (in respect of the year ended 31 December 2004: HK 16 cents or US 2.0 cents per share)	58,109	25,990
<i>Dividends attributable to the interim period, declared and paid after the interim period:</i>		
HK 20 cents or US 2.6 cents per share (2005: HK 30 cents or US 3.9 cents per share) (Note)	33,230	49,482
	<hr/>	<hr/>
	91,339	75,472
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Note: The interim dividend was declared on 22 August 2006 and was not reflected as a dividend payable in these unaudited condensed consolidated interim financial statements, but will be reflected as an appropriation of retained profits for the year ending 31 December 2006.

15 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 six months ended 30 June 2006, excluding the shares held by the trustee of the Company's LTIS (Note 9).

	Six months ended 30 June	
	2006	2005
Profit attributable to shareholders (US Dollars in thousands)	<u><u>36,385</u></u>	<u><u>85,503</u></u>
Weighted average number of ordinary shares in issue (in thousands)	<u><u>1,285,107</u></u>	<u><u>1,266,600</u></u>
Basic earnings per share	<u><u>US 2.83 cents</u></u>	<u><u>US 6.75 cents</u></u>
Equivalent to	<u><u>HK 21.95 cents</u></u>	<u><u>HK 52.30 cents</u></u>

15 EARNINGS PER SHARE (continued)
(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 shares in issue during the six months ended 30 June 2006 after adjusting for the number of potential dilutive ordinary shares to be issued upon the exercise of share options granted under the Company's LTIS but excluding the shares held by the trustee of the Company's LTIS (Note 9).

	Six months ended 30 June	
	2006	2005
Profit attributable to shareholders (US Dollars in thousands)	36,385	85,503
Weighted average number of ordinary shares in issue (in thousands)	1,285,107	1,266,600
Adjustments for share options (in thousands)	10,600	17,000
Weighted average number of ordinary shares for diluted earnings per share (in thousands)	1,295,707	1,283,600
Diluted earnings per share	US 2.81 cents	US 6.66 cents
Equivalent to	HK 21.77 cents	HK 51.61 cents

16 COMMITMENTS

(a) Capital commitments

	30 June 2006 US\$'000	31 December 2005 US\$'000
Contracted but not provided for in relation to		
– vessel acquisitions and shipbuilding contracts	283,149	158,878
– investment in a jointly controlled entity	–	1,792
– land and buildings	–	907
	<u>283,149</u>	<u>161,577</u>

(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 30 June 2006			
Not later than one year	986	102,300	103,286
Later than one year but not later than five years	685	146,162	146,847
Later than five years	–	31,759	31,759
	<u>1,671</u>	<u>280,221</u>	<u>281,892</u>

16 COMMITMENTS (continued)
(b) Commitments under operating leases (continued)
(i) The Group as the lessee (continued)

	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
	<u>2,241</u>	<u>223,114</u>	<u>225,355</u>

(ii) The Group as the lessor

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

	30 June 2006 US\$'000	31 December 2005 US\$'000
Not later than one year	33,778	34,196
Later than one year but not later than five years	<u>17,611</u>	<u>26,208</u>
	<u>51,389</u>	<u>60,404</u>

17 SIGNIFICANT RELATED PARTY TRANSACTIONS

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

(a) Purchases of services

	Six months ended 30 June	
	2006	2005
	US\$'000	US\$'000
Insurance premium paid to Sun Hing Insurance Brokers Limited ("Sun Hing") (Note i)	275	247
Amounts payable to China Line Shipping Limited (Note ii)	2,523	3,496

- (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 non-executive 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 disbursements and other charges which were calculated based on the vessel's pool points.

(b) Sales of services

	Six months ended 30 June	
	2006	2005
	US\$'000	US\$'000
Charter-hire income received from Asia Logistics Group Limited (Note i)	—	2,462
Charter-hire income received from Fujairah Bulk Shipping Limited (Note ii)	2,388	—

17 SIGNIFICANT RELATED PARTY TRANSACTIONS (continued)

(b) Sales of services (continued)

- (i) The Group leased out certain vessels to Asia Logistics Group Limited, a jointly controlled entity, in 2005.
- (ii) The Group leased out certain vessels to Fujairah Bulk Shipping Limited, a jointly controlled entity during the period.

(c) Directors and senior management compensation

	Six months ended 30 June	
	2006	2005
	US\$'000	US\$'000
Directors' fees	127	120
Salary and bonus	2,496	2,942
Retirement benefits costs	68	44
Share-based compensation	677	776
Termination benefits	273	–
	3,641	3,882

18 COMPARATIVES

Certain comparative figures have been reclassified to conform with the presentation adopted in the annual report for the year ended 31 December 2005 in order to achieve a fairer presentation of the Group's activities. They include turnover, bunkers, port disbursements and amounts payable to other pool members, and finance costs.