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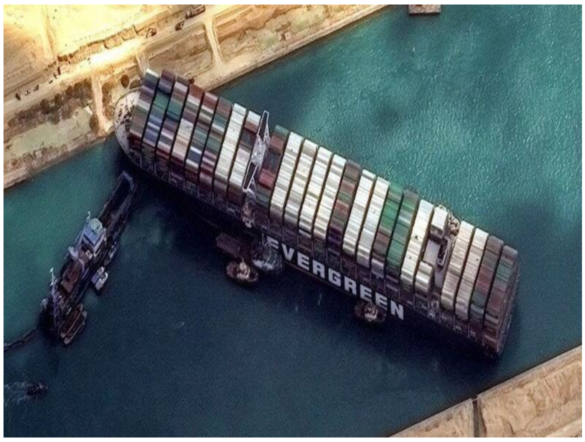
Record freight rates and delays.



Is this sustainable?

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Abstract

The world is living through unprecedented times, filled with numerous challenges imposed by Covid-19 pandemic, which started some 18 months ago to date. Currently, the container shipping prices have reached record highs, mainly due to the disruption of maritime logistics chains.

Highly congested ports around the world basically are running out of vessels and of empty containers, which due to supply chain disruption, again inflicted by the Covid-19 pandemic, are in the wrong place and not in Asia ready to be loaded.

As the world's economies are embarked on a gradual journey of economic recovery, a consistently increasing demand for goods is expected to dominate the global markets. The acceleration of demand, on top of lingering effects of the 6 days Suez canal blockage in March, closure of Yantian port for about a month, and limited availability of port equipment drove a further two digits increase on container freight rates and prices are climbing everywhere.

It is reported in the media that some shippers in the market over recent weeks, in order to comply with tough and critical deadlines, were willing to pay over $15,000 for a 40ft high-cube from China to the UK and it is likely the prices will continue to climb higher.

Apart from shipping rates skyrocketing, the schedule reliability is hitting record lows, causing immense operational challenges and additional cost to the supply chain and end users. The Asia-Europe transit times are deteriorating dramatically, with an average of delays up to nine days.

Covid-19 pandemic has changed consumers' habits, who during the lockdown stopped spending in restaurants and theatres or going on holiday and instead used their money to purchase goods, many of them imported from Asia. This e-commerce behaviour will stay for a while and will cause extra demand for shipping products from manufacturers to consumers' homes.

Some analysts are blaming the Covid-19, which disrupted worldwide supply chains, others are blaming the shipping companies on working in agreement to deliberately cause shipping rates and price's hike, while many are worried about the scale of negative and lasting impact of this situation on global trade. Ultimately, the next logical question is: how sustainable is the current situation?

Introduction

Ocean freight is the most common mode of transport that importers and exporters use, according to Freightos. Around 80% of the volume of international trade in goods is carried by sea, and the percentage is even higher for most developing countries[1]. The other international freight transport modes (courier, standard air freight, express air freight) are all faster, but they are also more expensive. Smaller shipments, and products with a high value, generally go by these other modes. If ocean freight is too slow, but air freight is too pricey, some freight forwarders are now offering a relatively new service, often called expedited freight[2].

COVID-19 pandemic has disrupted supply chains and wreaked economic havoc of unprecedented magnitude. It has impacted every business in the world, from small to large enterprises, which experienced unprecedented losses and disruptions that completely changed the mode of doing business.

Every country in the world has taken measures and eventually on different scales of success managed to overcome some of the challenges, there are a few one, associated with global effects that still persist. One of them is the skyrocketing shipping costs.

With ongoing uncertainties and pandemic-related restrictive measures, lockdowns, economic embargoes, travel restrictions, delays and closures, with with global retailers that want to restock the inventory, change of customers behaviour characterised with an increased demand for goods rather than services, non-stop increasing demand for ocean freight from countries across the world and a severe lack of capacity, ocean rates are still very elevated and transit times volatile.

With easining of restrictive measures by the governments worldwide, the demand for shipping goods has increased rapidly by almost 100-200 %. Since many companies have stopped supplying because the demands had dropped at the start of the pandemic in 2020, the whole world is now feeling the impact of shipping cost increase in 2021.

According to The Economist, in February 2021 the cost of shipping a container from Asia to the European region has increased from around $2,200 to a whopping $7,900[3].

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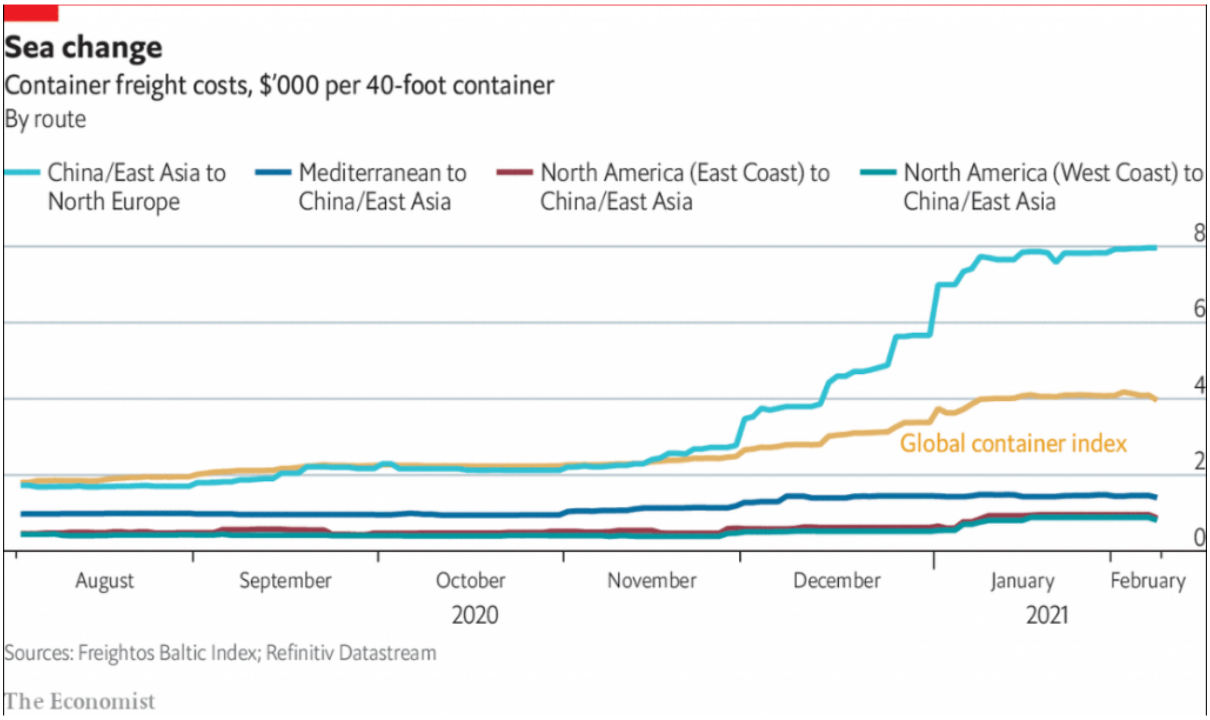
[1] https://unctad.org/topic/transport-and-trade-logistics/review-of-maritime-transport
[2] https://www.freightos.com/freight-resources/coronavirus-updates/
[3]https://www.economist.com/graphic-detail/2021/02/11/container-shipping-costs-have-surged-in-recent-months



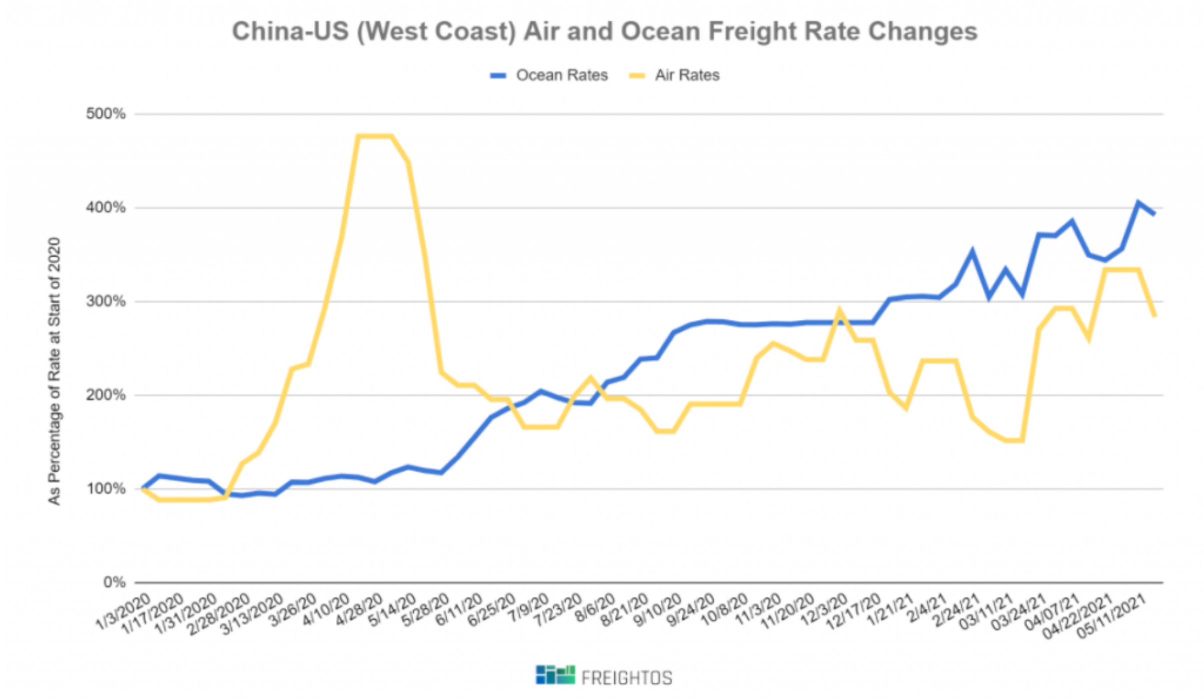
Freightos reports that in the beginning of June 2021, freight rates on the Asia-Europe trade lane recorded their highest-ever levels, breaching the $6,000 per TEU mark for the first time.

As high consumer demand and still-lagging inventory levels suggest no let up anytime soon, with additional demand expected from ocean's annual peak season in July, Freightos reports the following price increases:

- Asia-US West Coast prices increased 4% to $6,861/FEU, a rate 178% higher than the same time last year.
- Asia-US East Coast prices climbed to $10,002/FEU, 215% increase compared to rates for this week last year.
- Asia-North Europe and North Europe-US East Coast rates remained stable at $10,972/FEU and $5,193/FEU respectively.

Air cargo rates are also up as importers and exporters seek alternatives to sea freight. The below chart gives the correlation between ocean and air freight rates[4]:

[4] https://fbx.freightos.com/



Source: FBX

Another disturbing trend is schedule reliability, hitting record lows on multiple occasions this year, causing immense operational challenges and additional costs. The carriers are insistent on raising prices even further , while Asia-Europe transit times are deteriorating dramatically over the past three years. The average transit time from the ports of Yantian, Shanghai and Ningbo to the UK have increased on an average of nine days since 2018 as illustrated in the table below:

	Average Transit in Days to UK Base Port			
	2018	2019	2020	2021
Yantian	26	26	30	36
Shanghai	31	30	34	42
Ningbo	31	30	35	36

Many shippers are forced to cancel orders because the freight rates exceed their margins. Current freight rates are too excessive and will result in business failures, at a time when world economies are projected to grow. It seems consumer product costs and inflation is now inevitable, based purely on the cost of moving product from factories[5].

5 https://www.metroshipping.co.uk/news/china-to-uk-shipping-worst-transits-ever-at-highest-ever-cost-and-thats-a-fact/

Current freight shipping trends

With stronger than predicted growth of the world economy during the 2021[6], the operational challenges within container shipping that have now persisted for about a year and a half, are seemingly nowhere nearer to getting resolved.

It is common to hear nowadays ports closing or slowing down because of the pandemic, vessels put into quarantine because of COVID-19 infections among the crew, vessels unavailable because of mechanical failure, ports shut down because of weather or strike issues, or vessels afflicted by accidents such as fires.

Container shortage has inflicted the actual shipping crisis, which in turn has resulted from many other factors such as bottlenecks and port congestion, vessel shortages, equipment shortages, chassis shortages, rail shortages, and truck shortages. On top of that, shippers are attempting to cope with a massive boom in consumer demand for imported goods.

The pandemic dramatically has reduced the number of containers and ships available, as they are stranded somewhere and positioned not where they are needed. Now it takes much longer to move the cargos, which in turn reduces dramatically the portugal capacities. The companies are forced to pay premium rates to get back the containers faster.

According to JOC analysis,[7] the most pertinent elements of the container shipping market right now are:

- Spot rates are vastly exceeding any previous records. Flexport indicated that trans-Pacific spot rates, including equipment charges and space priority premiums, have risen to between $8,000 and $11,000 per FEU from Asia to the US West Coast and between $11,000 and $20,000 per FEU to the US East Coast.

- On the Asia–Europe trade, various spot rate indices are exceeding $10,000 per FEU, and this is before paying add-ons for equipment and capacity assurance. Increasing anecdotal evidence of rates approaching $14,000 to $15,000 per FEU from Asia to North Europe is emerging.

- Schedule reliability on both trades remains atrocious. The newest data from Sea-Intelligence Maritime Consulting show that despite improvements, 78 percent of vessels arriving at US West Coast ports are late, with an average delay of 10 days.

- According to Flexport, the transit time from cargo being ready for loading in Shanghai to delivery at warehouses in Chicago has risen from 35 days prior to the

[6]https://www.worldbank.org/en/news/feature/2021/06/08/the-global-economy-on-track-for-strong-but-uneven-growth-as-covid-19-still-weighs

[7]https://www.joc.com/maritime-news/container-lines/no-easy-recovery-ahead-container-shipping_20210602.html

COVID-19 pandemic to 73 days now because of delays at every possible hand-over point in the international and domestic supply chain.

With some countries to go into lockdown amid a new wave of the pandemic, the Port of Yantian closed for about a month because of a COVID-19 outbreak, and Rotterdam and Hamburg ports badly coping with the congestion, it appears the direction of the shipping market for now is to continue to increase the backlog of cargo.

Simply put, at the moment there is not enough capacity, manpower and equipment, to move the cargo in need of transportation. This is what has caused the extreme surge in freight rates as shippers weigh the choice between losing the sale of the cargo versus paying the highly elevated rates.

As a result, ship owners have never been in better shape. The Marseille-based CMA CGM container and shipping company for example posted a net profit of more than $2bn for the first quarter of 2021 alone, 40 times more than the previous year. Its Danish competitor AP Moller-Maersk announced an even higher net profit of $2.7bn for the first three months of the year -- 13 times what it saw last year[8].

However, it is expected the shipping companies will be using this profit to upgrade their fleet, by adding new vessels or renovating/upgrading the capacities of existing ones, thus contributing to building a better infrastructure to support the economic rebound in the post pandemic world and beyond.

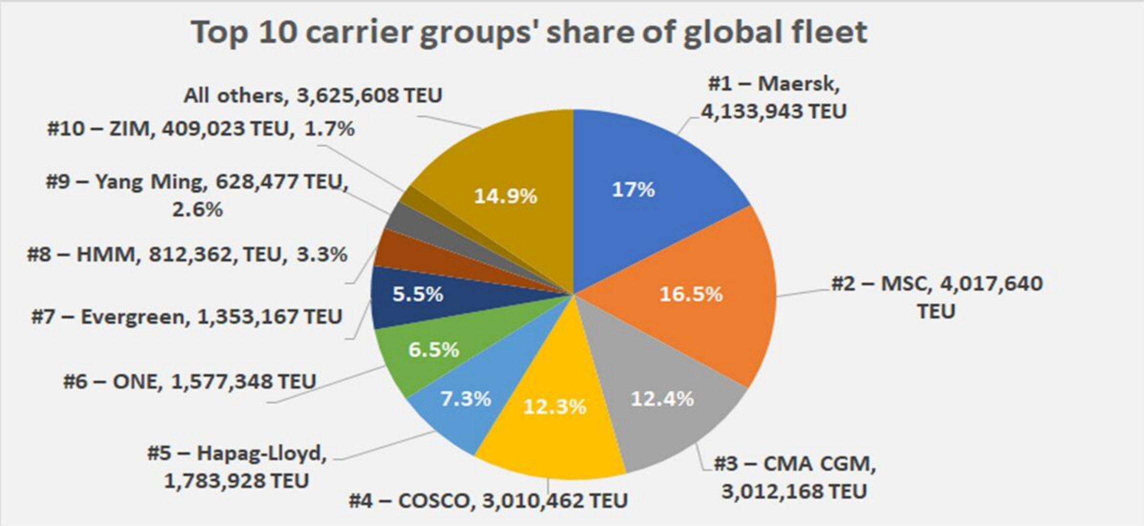
As the profit is growing, another trend is becoming more evident: the ongoing extreme consolidation within the container liner sector.

The latest data from Alphaliner highlights the extent of liner consolidation, how soon the rankings will change, and how newbuilding orders will render the carrier arena even more concentrated than it already is.

The top 10 carriers now operate 85% of global shipping capacity. Four groups — Maersk, MSC, CMA CGM and COSCO — control more than half of capacity (58%). The top seven, including Hapag-Lloyd, ONE and Evergreen, control 78%

This base level of fleet concentration is then greatly enhanced by the existence of three vessel-sharing alliances on the mainline East-West trades — 2M, the Ocean Alliance and THE Alliance — which count nine of the top 10 liner groups as members[9].

[8] https://www.rte.ie/news/business/2021/0704/1232980-container-shipping-maritime/
[9] https://www.freightwaves.com/news/top-10-liners-control-85-of-market-and-theyre-not-done-yet



TEU = twenty-foot equivalent unit (Chart: American Shipper based on data from Alphaliner)

The Switzerland-based carrier has been extremely active in the secondhand market, purchasing 49 vessels since August. It has also been busy in the charter market and very active in the newbuild market.

Including three secondhand ships it recently acquired, MSC just passed the 4 million-TEU (twenty-foot-equivalent unit) fleet milestone. Alphaliner noted that MSC's fleet has increased 4% from the beginning of this year alone.

Including newbuilds on order, MSC effectively surpassed Maersk months ago to become the world's largest carrier. Even in terms of ships on the water, it will take the crown soon[10].

[10] Ibid

Supply chain disruption

Covid-19 pandemic has disrupted the global supply chains as never before. During the first worldwide lockdown in 2020, companies across the globe, acting on the government's restrictive measures, were required to issue a postponement on all shipping orders.

As well, in a desperate move to control the virus spread, the ban on imports from several countries issued by various governments played a pivotal role in the reduction of demand.

The initial lockdown, associated with a high degree of fear and uncertainty, was characterised by a sharp fall in demand in goods and cargo and it resulted in many industries to stop operating. On the other hand, this resulted in a lot of the shipments being called off in advance. This created massive problems for the carriers, brokers, and businesses to continue performing as usual their daily activities.

In 2021, with anti-covid vaccines being made more available globally and the rising of hopes that pandemic will end soon, which in turn signalled a world economy bounce back, keeping up with the massive demand of shipments became a complicated task, as ports became increasingly overwhelmed.

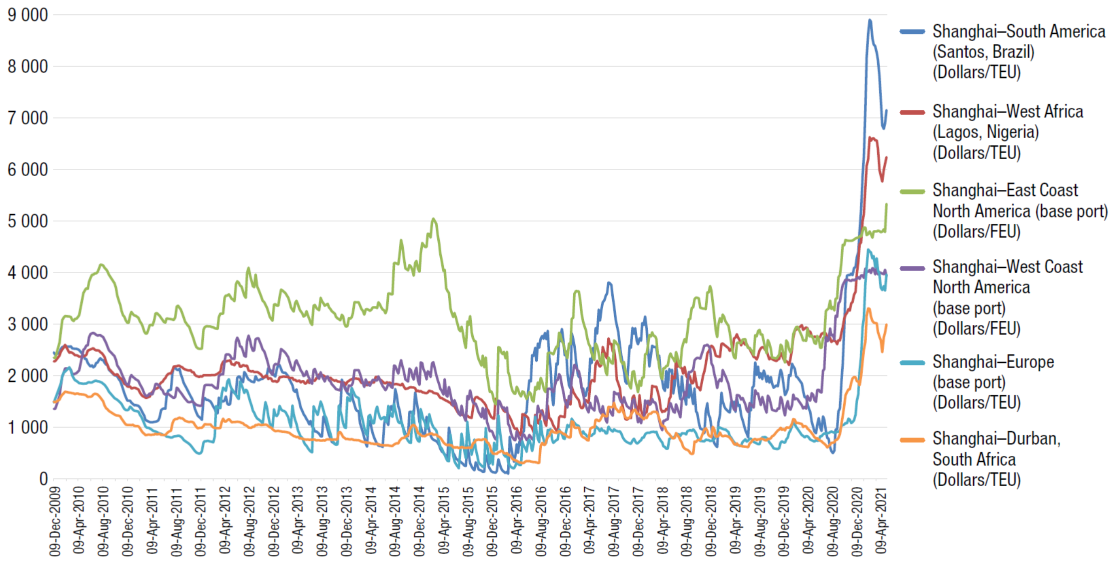
Ports were struggling already to cope with the unusual demand for medical equipment and protective equipment, and had limited capacities to address the rising demand for alternative goods.

Governments were suddenly expected to direct all their resources to house infected patients and provide the necessary resources and equipment to protect the general population. With uncertainty, danger, and warnings from WHO, governments all over the world had to balance out trade with the economy.

When the Ever Given megaship blocked traffic in the Suez Canal for almost a week in March, it triggered a new surge in container spot freight rates, which had finally started to settle from the all-time highs reached during the COVID-19 pandemic. The Ever Given incident reminded the world just how much we rely on shipping.[11]

According to UNCTAD, the global shortage of containers – an unprecedented challenge that drove shipping costs to an all-time high, has inflicted different changes to the shipping costs according to the length of routes, as the chart shows:

[11] https://unctad.org/news/shipping-during-covid-19-why-container-freight-rates-have-surged

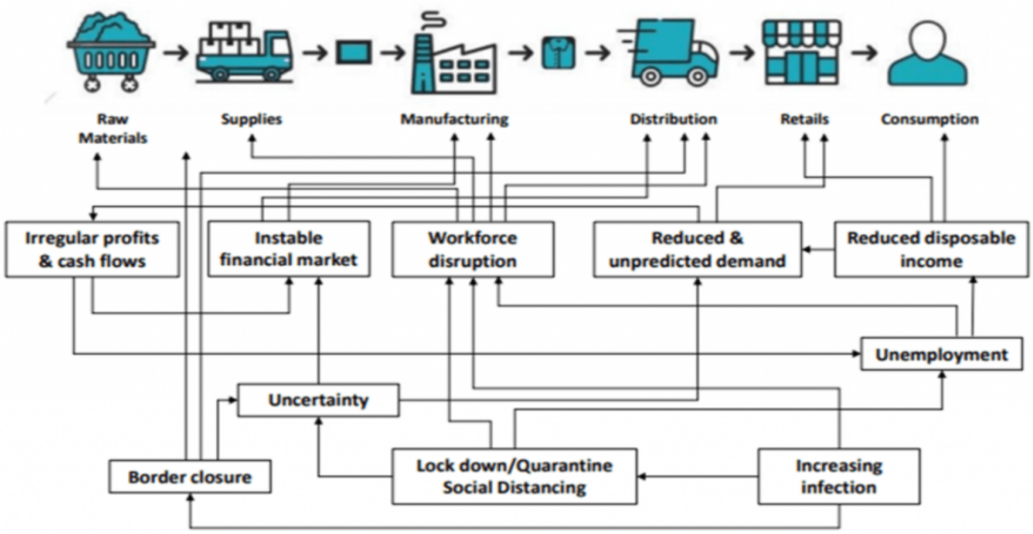


Shanghai containerized freight index, weekly spot rates, 18 December 2009–9 April 2021
Abbreviations: FEU, 40-foot equivalent unit; TEU, 20-foot equivalent unit.
Source: UNCTAD calculations, based on data from Clarksons Research, Shipping Intelligence Network Time Series.

The Institute for Supply Management (ISM) reports in the first 9 months of 2020, around 4,200 supply chain disruptions – a 14% increase from the 3,700 disruptions reported in all of 2019[12].

The Covid-19 pandemic affected not only supply chains, as it disruptions have caused far-reaching effects, spilling over into areas such as demand and price spikes, perfectly summarised in the diagram below prepared by International Economic Consulting:

12 https://www.ismworld.org/supply-management-news-and-reports/news-publications/inside-supply-management-magazine/blog/2020-10/a-historic-year-for-supply-chain-threats-even-without-covid-19/



Source: International Economics Consulting

Fearing of Covid-19 virus spread by shipping containers, government authorities around the world restricted the process of international trade in goods. When these additional and strict safety measures were introduced worldwide, during the first lockdown it became hardly possible to use any of the land logistics or airborne freight. With travel restrictions in place, global airlines suspended up to 90% of their passenger routes, which dramatically reduced air freight capacity to a low point that was never seen before.

As the World Health Organisation sounded the alarm on the shortage of emergency gear such as PPE, surgical masks, N95 respirators, hygiene-related products like sanitizers and soaps, the demand for such products skyrocketed. This was unprecedented and industries were not prepared to cope with such high demand in such a short time, as well as to ship out products in such volumes[13].

With governments restricting the movements of people to only essential trips, banning international or business travels, telling people to work from home, etc, it influenced a significant shift in customer behaviour. Customers now, not being able to use or order services, started to use e-commerce to order more goods, leading to an additional demand and spike in shipping costs across the globe.

[13]https://www.who.int/news/item/03-03-2020-shortage-of-personal-protective-equipment-endangering-health-workers-worldwide

Container Shortage

Covid-19 pandemic with its worldwide impact and restrictive measures, led to a global container availability crisis, which is unlikely to ease before the beginning of 2022 despite a record breaking new container production during 2021.

According to John Fossey, senior analyst of container equipment at Drewry Shipping Consultants, around 1.4m teu of new containers were delivered in the first quarter, around 10% more than in the final quarter of last year and 21% more than in Q1 20. Based on current activity, we believe the full-year 2021 production could be more than 4.7m teu. That would be a record year for container production, beating the 4.42m teu produced in 2018 and 52% up on the 3.1m teu delivered last year.[14]

The shortage is not in terms of numbers, there are enough containers for global trade, but they're just in the wrong places. As the world entered a complete lockdown within the first quarter of 2020, existing containers with supplies ready to be shipped out were left stranded in their departure ports. This trend has continued well into 2021, contributing to a container shortage that the world has never experienced before.

Another factor was the pandemic forced people to quarantine at their homes and promoted eCommerce for everything. People were left with no other alternative but to make their day-to-day purchases online, and not just daily groceries. People across the planet left with more money in their pockets, since they were not able to spend them on services.

During the lockdowns, people stuck in their homes placed massive orders for luxury goods from companies who primarily sourced their products from Chinese manufacturers. This increased the demand for shipping goods, which according to economics, the massive gap between demand and supply is bridged with increasing the price.

The container shortage was coupled with labor shortage, as more workers needed to self isolate. That resulted in more delays and setbacks in the loading/unloading of cargo, adding to the complexities of cargo shipping.

[14] https://theloadstar.com/there-are-enough-containers-for-global-trade-theyre-just-in-the-wrong-places/

Mitigation efforts

The current shipping crisis, associated with skyrocketing shipping costs and massive delays, is not going to disappear soon. The closure of Yantian port, a key South China port due to Covid-19 related measures (from 21 May 2021), sharply reduced capacity to move containers, resulting in major delays to global container shipping and therefore the backlog and prices continue rising.

The Yantian closure had a huge impact on global container shipping with hundreds of services omitting or diverting calls at the port, in a business disruption described by Maersk as being much bigger than the closure of the Suez Canal by the Ever Given grounding earlier this year. Delays for berthing at Yantian continue to be reported as 16 days or longer, and congestion is growing at the nearby ports of Shekou, Hong Kong, and Nansha, which Maersk reported as being two – four days on 21 June 2021. Even with Yantian resuming full operations on 24 June 2021, congestion and impact on container shipping schedules will take weeks to clear[15].

In the UK, businesses are thinking of finding alternative solutions. Britain's largest kitchen supplier, Howden Joinery, has started importing goods from China by train because of the rising cost of using maritime shipping containers to avoid the current delays[16].

The founder and managing director of the Midlands-based furniture retailer Peppermill Interiors, said that the cost of a 40 ft shipping container had increased from $2,800 before the pandemic to $14,000 in June 2021. This has resulted in businesses trying to push some of the added costs on to their end customers, and that some businesses may stop importing entirely[17].

The founder of start-up Houseof.com, which imports lighting from China, confirmed that in January 2021 she was quoted over £10,000 per container, compared to £1,600 per container in November. The rise in shipping costs means they are making a loss on what they sell. This is one of many UK importers facing soaring freight costs amid a global shipping crisis that may last months. As well, shipping lines have been trying to drive down demand from British importers by charging a premium for deliveries to the UK, or bypassing the country's ports altogether[18].

Companies are desperately trying to work around the higher costs. Some have stopped exporting to certain locations while others are looking for goods or raw materials from nearby locations. Some firms in Europe are resorting to extreme methods, like using truck

[15] https://www.seatrade-maritime.com/ports-logistics/yantian-port-resume-full-operations-24-june
[16] https://www.thetimes.co.uk/article/train-takes-strain-for-china-imports-as-sea-container-costs-rise-f7nscsqp p
[17] https://www.thetimes.co.uk/article/times-enterprise-network-surge-in-shipping-prices-pushes-importers-to-t he-edge-l0p7q2rnl
[18] https://www.bbc.co.uk/news/business-55740063

convoys to get products including automotive parts, bikes and scooters from China, said Espin at the European Shippers' Council[19].

With the end of lockdowns consumer demand is likely to shift to services from goods, but "the risk of course is that higher shipping costs persist — especially given ongoing shipping disruption — and that producers become more willing to pass these higher costs on to consumers[20].

Central bankers have so far been sanguine about the phenomenon, arguing that the rise in consumer prices tied to supply hiccups won't last. European Central Bank President Christine Lagarde said on June 10 that while supply-chain bottlenecks would push up production prices and the headline inflation rate is expected to rise further in the second half of this year, the effect will fade[21].

British International Freight Association, has announced that many organisations have called on the UK government, European Commission and others to intervene, but they share the opinion, there is nothing that they can do as container shipping lines and the customers they serve operate in a free market. The current elevated shipping costs are due to the increased demand and limited supply.

The European Shippers Council (ESC) and CLECAT, European associations grouping shippers and forwarders, recently criticised policies being pursued by shipping lines in a joint open letter addressed to the European Commission. Its representatives said they are aware of the market situation, adding that price hikes are mainly due to demand fluctuations arising from government measures to contain the Covid-19 outbreak.

They don't believe the hikes justify starting an investigation. They can only examine the situation when the formal review of the Consortia BER is relaunched, or if there is a legal complaint. The DG nevertheless acknowledged that the situation calls for a global overview and for renewed discussions with maritime competition authorities worldwide.

The EU Commission also suggested dialogue between market participants to find a common approach to problems. ESC and CLECAT are now considering whether there is a case to file an official complaint to the Commission.

Meanwhile, in the USA, the Federal Maritime Commission (FMC) is in the process of independently verifying allegations that carriers are refusing to carry export cargo in contravention of the US Shipping Act. The investigations into the carrier behaviour, following allegations from shippers has also extended to evaluating the alliance

[19] https://time.com/6073233/shipping-costs-surge-price-hike-goods/
[20] Ibid
[21] https://www.ecb.europa.eu/press/pressconf/2021/html/ecb.is210610~115f4c0246.en.html

agreements to understand how they are working and to check if there have been unreasonable practices[22].

According to a GEP senior research analyst[23], the next following months' situation in relation to the sea freight will be as follows:

North America West Coast to Asia: Container repositioning and securing empty containers in the U.S. will become easier by the end of Q3 2021. Containers that are stuck on ships awaiting berths, on quays awaiting transport, or log-jammed at other intermodal pinch points are expected to be released in the coming months. Because of lockdowns, the last few quarters witnessed an unplanned stockpiling of numerous essential commodities with the sudden growth in demands from various Asian regions; however, this trend is expected to end during the second half of 2021. The decrease in cancellation of sailings by carriers, along with reduction of blank sails in the North America West Coast to Asia lanes, will drive the reduction of ocean freight rates by the first quarter of 2022.

Southeast Asia to Oceania Region: Rates are not expected to decrease until the end of Q1 2022. With seasonal commodity demands, we will likely see continuing spot rate inflation until Q4 2021.

South Asia to China: Labor availability is expected to expand in China to address the volume of containers stuck at Chinese ports, which will add more volumes in the Southeast Asia market and lower the inflated rates by the end of Q4 2021. To contain ocean freight rates on Southeast Asia lanes, governments are planning[1] to force shipping lines and agents to provide "all-inclusive" freight rates. The Global Shippers Forum is backing India's push for "all-inclusive" ocean freight rates, claiming that carrier surcharges disproportionately impact cargo owners in developing countries.

Intra-Asia: Spot rates from Intra-Asia trades are expected to lower by the end of 2021 and in the first quarter next year because with the market mildly overcoming equipment shortages, port delays, and lack of capacity. Additionally, the decline of personal protective equipment (PPE) traffic out of China and Southeast Asia, coupled with new preventative measures and in-house developments in the U.S. and EU and vaccination programs, will support in controlling any growth in freight rates.

Northern Europe to Middle East Region: Blank sailings are expected to reduce in major European lanes. For lower freight volumes, companies have started considering niche Non-Vessel Operating Common Carrier to contain costs. Repositioning of empty containers back to China from Europe is also expected to increase, which will lead to the removal of repositioning surcharges and reduce freight rates by Q4 2021.

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[22] https://www.bifa.org/news/articles/2021/jan/container-shipping-market-dialogue-or-complaint

[23] https://www.dcvelocity.com/blogs/2-one-off-sound-off/post/51331-global-ocean-freight-rates-are-touching-the-sky-heres-what-to-do

Northern Europe to the Far East: Ocean freight spot rates in the European region may come down by the end of Q4 of this year because of the market overcoming the capacity bottlenecks and an increase in the availability of empty containers and other equipment. However, this benefit will be offset because shipping activity is likely to grow between Q3 and Q4 of 2021 because of an increase in seasonal demands of agricultural and perishable products in the Far East regions, creating minor inflation in the second half of this year.

Northern Europe to Oceania: Controlled European imports of e-commerce merchandise, home improvement goods, PPE, and other medical supplies will help to contain ocean freight rates. Carriers are expecting a slowdown in the number of new contracts during the last quarter of 2021. Ongoing service enhancements with less cargo rolling, improved container availability at load ports, and much better schedule reliability are expected to bring down ocean freight rates.

With so much economic activity coming back online, it only makes sense that container ship operators will see some of the biggest gains as a result.[24]

[24]https://www.forbes.com/sites/greatspeculations/2021/03/25/container-ship-operators-are-on-a-tear-as-freight-rates-skyrocket/

Is the current freight shipping situation sustainable?

Half a year has passed into 2021 and logistics companies and shippers have all but lost hope that the market will be anywhere close to normal this year, as rates continue to soar.The container market is strained by huge demand on goods from Asia to the US and Northern Europe in particular, which has generated a shortage of ships and equipment, such as containers, and pushed rates to unprecedented levels. Further, the lack of capacity causes delays and queues off several ports, a scenario that has been criticized several times by shippers.

Many shipping companies have found that the rapid development has only intensified the exceptional upward trend of freight rates that continue to break new records week after week. 2021 promises to be the best year for the container industry in several decades, which is due to several factors:

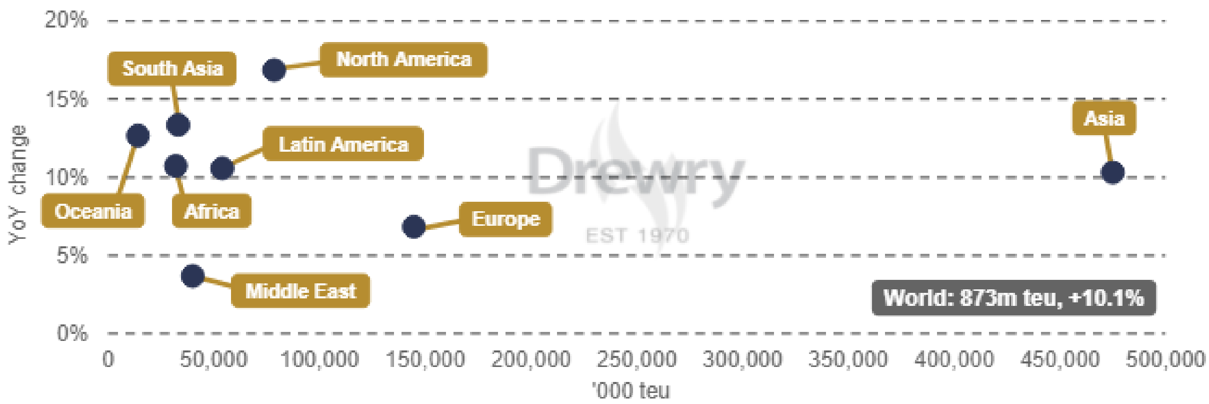
- The Covid-19 pandemic in several major nations sustains the current market situation since Summer 2020
- Huge aid packages are being pumped into the world economies like the US and most of European countries such as Italy and Spain
- OECD has raised its global growth forecast significantly this year to 5.8 percent
- The supply of container vessels is too low, which will take a couple of years to reverse
- There is a shortage of equipment such as containers
- There is continued port congestion around the world. In march, the Suez canal was blocked by the Ever Given ship for 6 days, causing a backlog of some 340 ships. Most recently, the major Chinese port Greater China Yantian was shut down for about a month due an outbreak of Covid-19, which caused port congestion in the nearby ports, as well ripple effects were felt even farther, like in the European ports, such as Hamburg, etc.

Although shippers and carriers in most cases have agreed in advance the rates in the long-term contracts, still this is a process that many shippers and carriers have completed recently and under a prolonged period of elevated shipping prices.

Companies will have to pay double what they usually spend on key routes between Asia and Europe, while a normalisation of the situation is expected in the fourth quarter this year or the first quarter next year. But according to all the forecasts available, sufficient capacity that will balance supply and demand will not be added until 2023[25].

The latest edition of Drewry's Container Forecaster finds that 2021 will be the first year in the history of container shipping when carrier profits approach $100 billion and average freight rates jump by 50%, against a background of huge operational disruptions to the port and ship systems.[26]

Figure 1: Drewry port throughput forecast, 2021

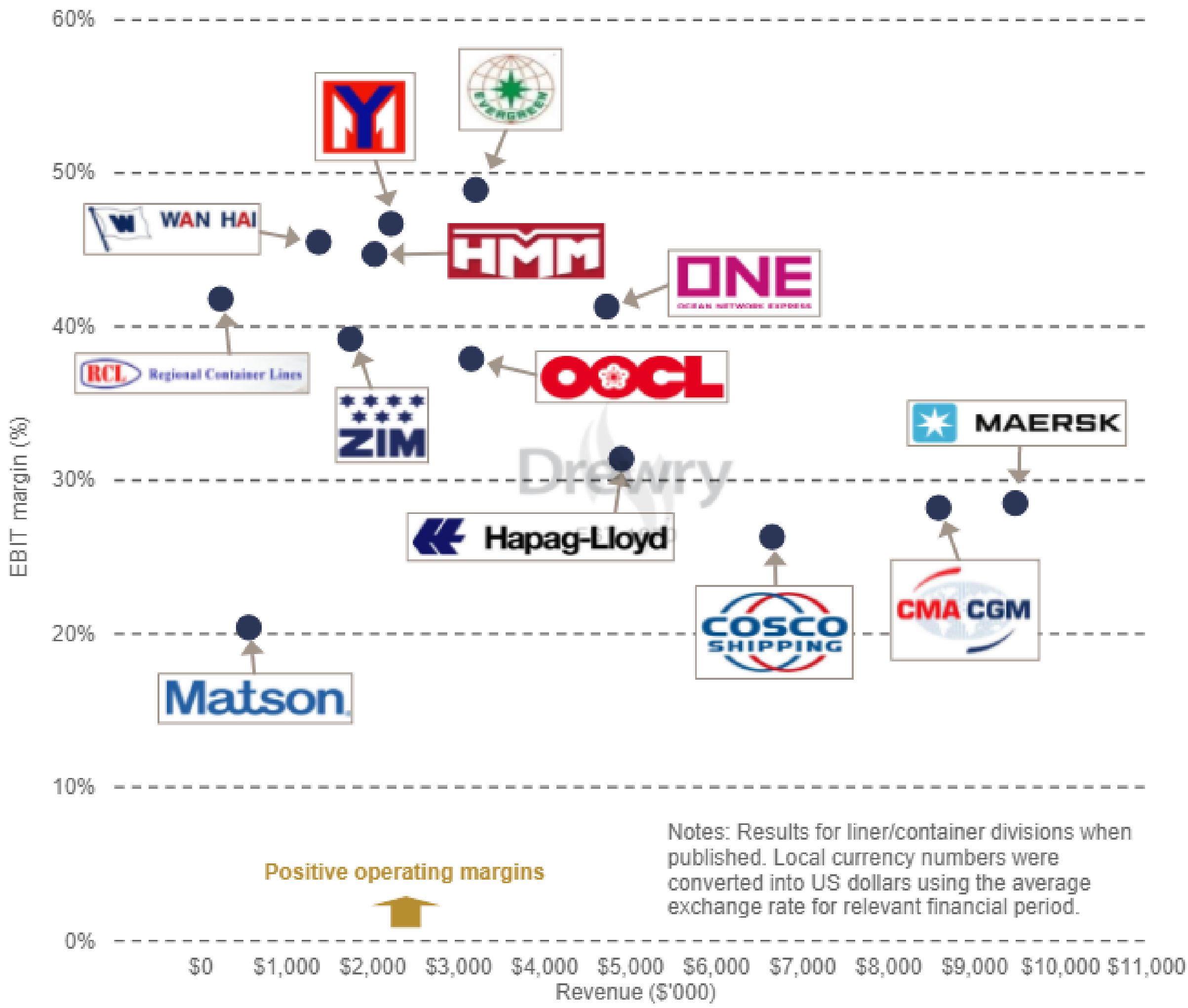


Source: Drewry Maritime Research

The extreme increases in freight rates have naturally translated into blockbusting carrier profits. Carriers posted a record EBIT result in 1Q21 of $27.1 billion, up from what now looks a miniscule $1.6bn in the same period one year ago. So impressive are the latest quarterly results, they even eclipsed the full-year 2020 EBIT of $25.4bn.

[25] https://shippingwatch.com/article13022620.ece
[26] https://www.seatrade-maritime.com/containers/container-line-profits-could-hit-100bn-2021

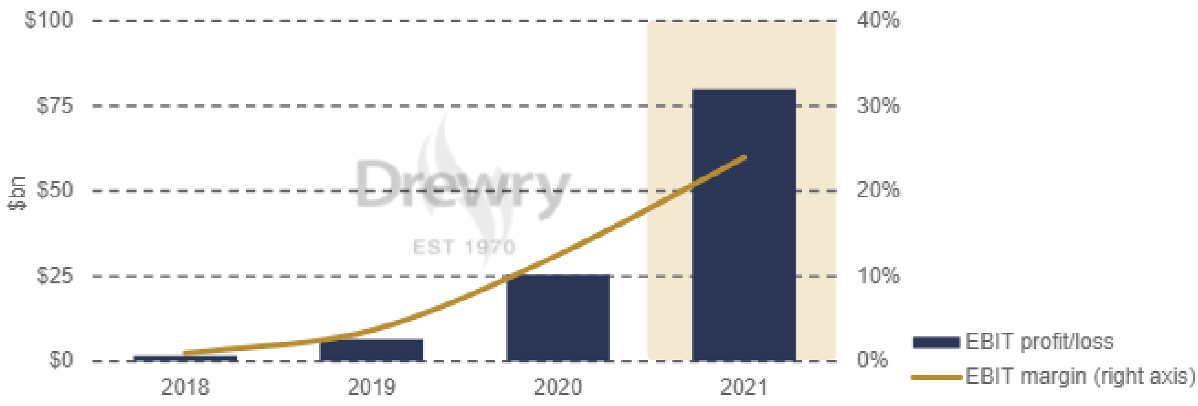
Figure 2: 1Q21 scorecard: comparison of ebit margins, revenue of selected carriers



Source: Drewry Maritime Research

Given the substantially higher freight rate forecast for this year, Drewry has made a major upgrade to our full-year 2021 industry EBIT outlook. They are now forecasting industry EBIT of approximately $80 billion for this year - up from our previous estimate of $35bn. If freight rates surpass expectations in the remainder of the year, we would not be surprised to see an annual profit line in the region of $100bn.

Figure 3: Forecast carrier industry ebit profit, margin



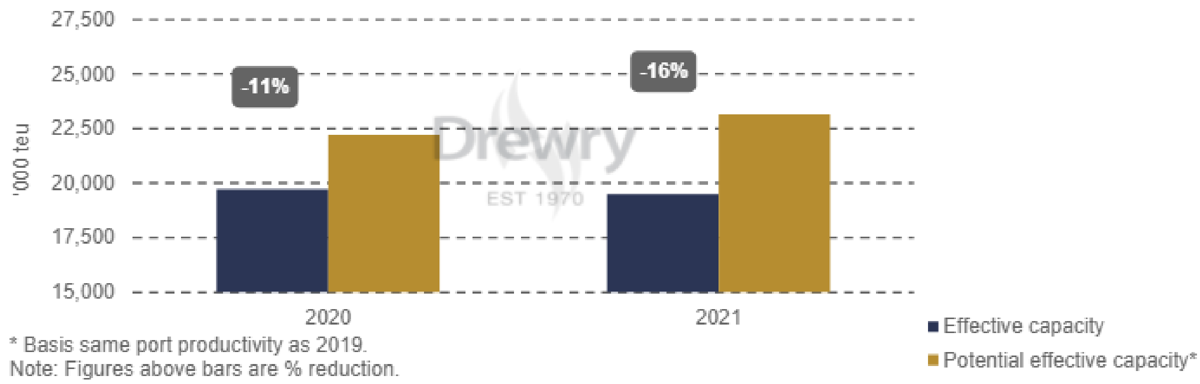
Source: Drewry Maritime Research

For 2022, they expect EBIT to drop by a bit more than one-third due to softening freight rates and rising costs that may stay higher for longer with many carriers locking into expensive longer-term charter fixtures. Nonetheless, it would represent another astonishing performance by historical standards.

Regrettably, Drewry is less optimistic about a solution being found to fix the supply chain disruption and thinks the market is facing medium-term (or extended) under-supply. Events at the South China port of Yantian (a Covid-19 outbreak in May hobbled operations for nearly a month, with knock-on congestion at nearby ports in Asia), and earlier in the Suez Canal, demonstrate just how fragile the container shipping eco-system is and how challenging it is to try and build in more resilience.

Supply side disruption has become the key driver of freight rates and remains the top sensitivity to our forecasts. Drewry now thinks lower port productivity will continue into 2022. Subsequently, Drewry expects the Global supply-demand index to average 105.7 in 2021, up 0.9 points on our previous assessment. Any reading above 100 indicates tightness of supply in the market.

Figure 4: Estimated impact of lower port productivity on effective capacity



Source: Drewry Maritime Research

Drewry estimates that 16% of worldwide effective capacity (the slots available to the market) will have been lost this year as a direct consequence of lower port productivity, following on from an 11% reduction last year.

Way forward

Current record freight rates and delays are the result of a system under pressure in the midst of Covid-19 pandemic. As the global economic recovery has progressed, global demand has recovered strongly, especially in the sectors which are most closely linked to international trade in goods. Competition for ocean freight capacity has intensified as economies open up further and inventories are rebuilt across the several links of supply chains. A lack of alternatives to ocean freight means it's hard to avoid surging transport costs at the moment. For higher value products, alternative modes of transportation would normally be an option, such as the shipment of electronic devices by air or via train[27]. Many believe that the main culprit of the current freight shipping crisis is the disruption of the supply chain and the shortage of the shipping containers.

Shippers are not to blame for congested port and terminals, shortages of rail, truck and warehouse capacity, the blockage of the Suez Canal or the outbreak of Covid-19 at Yantian. But, shippers must bear some responsibility for supply chain disruptions. The just-in-time supply chain permits cargo owners to avoid the cost of holding inventory, and they have chosen to invest in the cost of shipping rather than the cost of high inventories. Yet, shippers are responsible for the spot rates to climb so high because they deliberately were outbidding each other in a market where demand exceeds supply[28].

Relief from container scarcity is not just about increasing the production of the new ones, which currently is taking place with full steam.. Many containers have been held up in port congestion and by issues such as the Ever Given accident in the Suez Canal, or the closure of Yantian port. After a while, when such logjams will be finally cleared, it is expected more containers will become available. The bottleneck situation is likely to continue until trade slows, probably sometime at the end of this year or early next year when maybe the trade world starts to get back to normal[29].

Again, with the competition for ocean freight capacity set to remain, the unbalanced economic recovery of countries will continue to exacerbate some of the problems for world trade, including displaced empty containers. It all adds up to more pressure on freight rates in the near term[30].

The Suez Canal crisis has certainly raised some questions about some practices in the shipping industry (more specifically, about the size of the vessels). Many experts believe that

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[27] https://think.ing.com/articles/the-rise-and-rise-of-global-shipping-costs
[28] https://lloydslist.maritimeintelligence.informa.com/LL1137145/Dont-shoot-the-carrier
[29] https://www.freightwaves.com/news/no-relief-global-container-shortage-likely-to-last-until-2022
[30] https://think.ing.com/articles/the-rise-and-rise-of-global-shipping-costs

carriers would be better off with smaller vessels, as they pose smaller margins of error. This, in turn, may also drive down overall shipping costs[31].

The Global Shippers' Forum has long argued that the disruption in the supply chain and rising freight costs could lead to inflation as economies recover from the pandemic. One could equally argue that container shipping at below cost rates led to deflation that made shipping cheap goods halfway around the world possible[32].

According to Drewry[33], the emphasis should be given to calm and fix the supply chain, which in turn will get containers flowing as they should, in particular the following should take place:

- Port productivity needs to improve – dependent on avoiding Covid outbreaks and for less liner service disruption
- More reliable and predictable liner services to give ports a better chance to clear the backlog – likely dependent on improved port productivity
- A slowdown in Asia to US demand to promote more equal distribution of capacity and equipment

At Drewry Maritime Research analysts believe this is something of a circular problem. Shipping lines alone do not have the power to fix things, but the industry at large somehow needs to find a way to break the vicious circle.

They also have issued a warning, with increasing attention on shipping's environmental footprint and tax contributions, lines are in danger of being cast as profiteering villains, unsympathetic to the needs of their customers and hope they will be good global citizens and do more to help improve the efficiency of the supply chain.

[31] https://www.qafila.com/the-global-surge-in-shipping-costs-whos-responsible-what-to-expect/
[32]https://lloydslist.maritimeintelligence.informa.com/LL1137090/Shippers-renew-call-for-block-exemption-to-be-removed
[33]https://www.drewry.co.uk/container-insight-weekly/weekly-feature-articles/who-wants-to-be-a-multi-billionaire

Conclusion

The sharp and uneven rebound in global manufacturing activity during the 2021 year caused a strong rise in international orders and resulted in some supply bottlenecks. Small companies trading internationally are grappling with shipping prices that are between seven and ten times higher than a year ago. Soaring demand has combined with restricted supply to push up shipping prices and, for some products, transporting them via ocean & sea freight make the import of goods uneconomic, as it would suck any profit out of the sale of the product.

For those businesses that can still afford the cost, supply chain management has become a matter of poker, where every player wishes for some good luck. The global disruptions mean that the assurances you could order parts from China and have them delivered to a factory on a known day within two months of placing the order, are gone. This has a massive spillover effect for a range of economic sectors, throwing them into disarray.

Many are blaming the shippers for the current unsustainable situation with the record shipping rates and the profit they had for just two years that normally would have been achieved in decades. Yet, many easily forget the important role that ocean & sea freight shipping industry is playing in the support of international trade, as 80% of goods are being moved by the sea and oceans.

There is some evidence, although shippers are responsible for the spot rates to climb so high because they deliberately were outbidding each other in a market where demand exceeds supply.

UNCTAD shares the view that although the pandemic's disruptive nature is at the core of the container shortage, certain strategies by carriers may have delayed the repositioning of containers at the beginning of the crisis.

European Commision is of the view that there is not enough evidence to launch an investigation as the current shipping situation is a reflection of market economy in a moment characterised by high demand versus very short supply. Meanwhile in the US, the Federal Maritime Commission is investigating into whether the shippers have breached the fair competition laws.

Nevertheless, at this moment all the stakeholders need to promote transparency and encourage collaboration along the maritime supply chain to improve how port calls and liner schedules are monitored. And governments must ensure competition authorities have the resources and expertise needed to investigate potentially abusive practices in the shipping industry.

As the coronavirus vaccination programs are fast progressing worldwide, and pandemic restrictions are lifted, consumers will be starting to adapt to the new normal, including learning to live with the Covid-19 virus, and start diverting their spending to restaurants, hotels and other services again, relieving pressure on goods exporters.

At the same time, businesses are slowly beginning to resume their normal operations, and it is expected the supply chain will adjust to higher demand, will get more stable, thus resulting in freight costs to be reduced.

2020 & 2021 years have been filled with unprecedented and tough challenges that have tested resilience and our ability to cope in the face of emergencies. The surge in shipping costs might be what was needed to bring a perspective shift in the industry of logistics & shipping. The pandemic highlighted the need for a more resilient supply chain, which could be achieved by implementing advanced technology to increase automation and enable hands-free experience in as many as possible processes, as well as to refine supply-chain processes in trade.

It is expected that shippers will be using part of the colossal profit earned during 2020&2021 years to upgrade the fleet, increase container handling capacities, invest in automation and modern technology, thus creating the necessary infrastructure to support international trade and the next global economic boom. However, the extreme fleet consolidation within the container liner sector is something that should be watched carefully by the competition authorities.

Given the unpredictable state of the Covid-19 pandemic and uneven level of its economic impact on various countries, it is difficult to say with confidence how things might pan out in the future, as the world attempts to recover from the after-effects of the turbulences the year 2020 brought for it. There is some reassurance from the global analyst community that while the aftershocks of 2020 will likely linger all throughout 2021, and possibly also the years to come, this situation of a global surge in shipping costs is likely to be temporary, given its unsustainable nature.

Only time will tell.

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About us

Esharelife Think Tank is a non-profit, independent, non-governmental organization, not associated with any particular political parties or businesses. It promotes the philosophy of **sharing life in the digital era**, and serves as an open forum where like-minded people can freely share their ideas and knowledge on global development issues and the future of our planet.

Dr Maurizio Bragagni OBE, Chairman of Esharelife Foundation, is a senior business opinion leader, author and writer focusing on business, innovation and technology, politics, education and the economy. The earnings from the latest books "Brexit, Business and a better Britain'', "Insight to Hindsight - Money, Mistakes, Magic and Metamorphosis" and "From Roman Invasion to Unshakeable Bond: The Anglo Italian Relationship" he has donated to the Esharelife Foundation for educational projects in Kenya.
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