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Ocean Freight Market H2 2023

June 2023

Introduction: H1 2023 in Review

As we reach the halfway mark of 2023, there is a growing sense of optimism regarding the economy compared to the predictions made in the fourth quarter of 2022.

However, both consumers and companies are facing challenges as they contend with the repercussions of soaring inflation rates. In the United Kingdom, inflation remains at 8.7% in May 2023, while the United States experienced a notable inflation rate of 4%. Compounding the difficulties, interest rates have been on an upward trajectory, currently standing at 5% in the UK and approximately 5-5.25% in the US.

Although the UK has managed to avert a technical recession, the prevailing economic conditions have caused retailers to be on high alert in response to mounting cost pressures and the uncertain nature of demand.

In a low consumer demand environment, businesses are treading cautiously and adopting a risk-averse approach, which can be observed through reduced order volumes and a cautious stance towards carrier contracting. This cautious approach is driven by the absence of clear indicators and the need to navigate the uncertainties in the market.

The decline in order volumes has prompted carriers to maintain competitiveness by reducing their rates. This trend is a response to the challenging economic environment and the need to attract customers amidst weakened demand:

- Schedule reliability has improved with an overall increase to 64.2% in April 2023, reflecting a substantial year-on-year improvement of 29.9%. Despite this positive trend, shippers continue to grapple with challenges arising from sudden cancellations by carriers, which introduce disruptive elements into their operational processes.

- Carriers, grappling with the ongoing decline in container shipping spot rates, have seen a drop in their profits, which could potentially reshape the dynamics of the low-rate market. According to a recent report by Sea Intelligence, carriers experienced a 81% year-on-year drop in their EBIT (Earnings Before Interest and Taxes) for the first quarter of 2023. This substantial decrease further highlights the financial challenges faced by carriers and underscores the need for strategic adjustments to navigate the changing market conditions.

- Shippers are actively anticipating the arrival of a peak season this year, typically commencing in August. However, they have learned from the challenges faced last year when an early peak season led to overstocking due to low consumer demand. As a result, businesses are approaching this year's peak season with caution, mindful of the inventory imbalances experienced previously.

To navigate these complexities, businesses need to remain agile and prepared for the opportunities and challenges that lie ahead in the second half of 2023.

Key Trends for H2 2023

High inflation during the initial half of the year resulted in a decline in consumer spending and a sluggish market. To navigate these circumstances, businesses are closely monitoring economic indicators to determine the optimal timing for restocking. By doing so, businesses can efficiently manage inventory levels, fulfil customer demands, and maintain seamless operations within the supply chain.

Despite the drop in rates benefiting shippers through reduced container shipping costs, it's vital for businesses to consider additional trends. By doing so, shippers can enhance their freight strategies, ensuring competitiveness and resilience in the ever-evolving industry.

Let's explore some of these key trends below.

Is it time to lock into long term contracts?

Shippers are currently facing a decision regarding when to secure a long-term deal. Market indicators strongly suggest that rates have potentially reached their lowest point, presenting a highly favourable opportunity for shippers.

- Amid the current market scenario, businesses can seize the opportunity to secure capacity and meet restocking needs through long-term agreements. While rates may be slightly higher than historic spot market lows, the key benefit lies in the guaranteed level of service, absent in spot rates.

- This approach offers businesses a sense of confidence when it comes to inventory replenishment and capacity sourcing. However, it's important to note that the optimal decision varies for each business depending on their specific circumstances and requirements.

New container ships

During the pandemic, carriers witnessed their most profitable years, allowing them to invest their earnings in ordering new vessels that adhere to sustainable regulations, including IMO 2023 standards.

- In the coming years, the industry is poised to witness the introduction of new capacity, with 9% scheduled to come online in 2023, followed by an additional 9% in 2024. This strategic expansion plan reflects a balanced approach to meeting growing demand while maintaining supply stability.

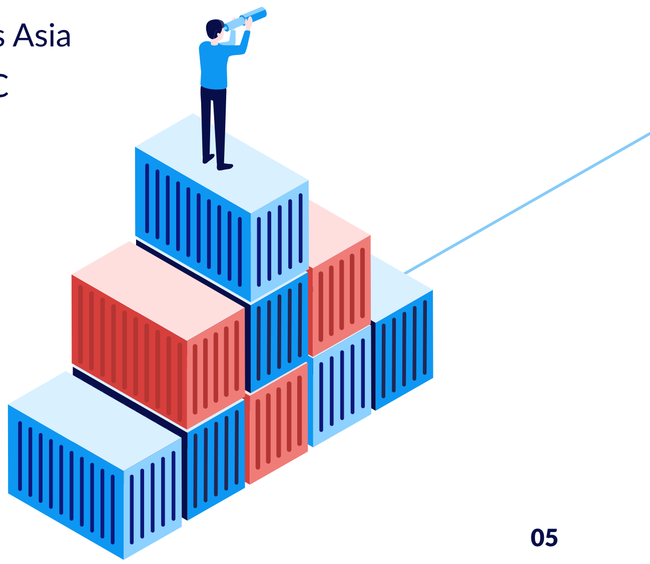
- Furthermore, the retirement or scrapping of older container ships will contribute to maintaining a steady supply. As a result, the overall supply dynamics are expected to remain stable in the industry.

Alliance changes

In a notable development this year, the 2M Alliance, which has been operating since 2015, announced its plan to split in 2025. The alliance, formed by Maersk and MSC, has helped the two companies capture more market share and develop complementary services.

- The potential impact of the 2M Alliance's separation on other alliances remains to be seen. However, one thing that is clear is that the split process will happen gradually over the course of several years leading up to 2025.

- The market has already witnessed movements in the market. For example, MSC has announced it will relaunch its Asia to North Europe Swan-service, as a standalone MSC service. The Swan service was originally a 2M service suspended in May 2020 but will relaunch on the 9th July.



Trade Lane Analysis

Asia - United States

Rates

-80.09%

Far East - US West Coast

Rates

-75.65%

Far East - US East Coast[1]

Key points:

- **ILWU negotiations** - Over the past year, US West Coast ports have been aiming to regain import volume that has been shifting towards the East Coast. However, recent data has unveiled that in April, only 36% of imported goods arrived through West Coast ports, marking the lowest proportion of US imports since mid-2021. Disruptions and the ILWU contract ending in July last year has prompted shippers to proactively redirect their cargo to alternative ports to avoid potential delays and mitigate associated risks.

  Fortunately, after a period of stalemate and disruption, negotiations between the Pacific Maritime Association (PMA) and the International Longshore and Warehouse Union (ILWU) have reached a positive outcome. On June 14th, both parties reached a comprehensive agreement that spans over a period of 6 years. This agreement covers 29 ports that play a vital role in handling a significant portion of US imports.

- **Contracting** - Shippers have been holding off from signing long term contracts in order to leverage the falling spot market. As a response to shippers' attempts to secure favourable rates, carriers introduced GRI to regain control over pricing; however these were largely not sustained by the market and have mostly eroded.

  Carriers may reconsider their strategies in the second half of the year as they grapple with the challenge of diminishing profitability. This evolving dynamic in rates contracting highlights the complex interplay between shippers and carriers in negotiating and adapting to market conditions.

- **Panama Canal** - Insufficient rainfall has caused water levels in the Panama Canal to decline, impacting one of the world's major shipping routes. In 2022, over 14,000 vessels carrying 518 million tonnes of cargo traversed the canal, which handles around 6% of global maritime shipping, primarily from the US, China, and Japan.

  Due to a 50% decrease in rainfall compared to recent averages between February and April, draft restrictions are being implemented resulting in certain boxships needing to transport 40% less cargo through the canal.

  As a response to these limitations, several global shipping companies have announced surcharges. Furthermore, shippers are actively exploring alternatives, with the Suez Canal emerging as a potential all-water route between Asia and the US East Coast. This redirection aims to mitigate the challenges posed by the Panama Canal's current conditions in the forthcoming months.

[1] Source: *Xeneta*. Date range 1st June 2022 vs 1st June 2023/ 40ft cube.

Trade Lane Analysis

Asia - Europe

Rates

-86.73%

Far East - North Europe[2]

Key points:

- **Carrier strategies** - The 2M partners, Maersk and MSC, have made a significant announcement by revealing their plans to deploy an additional 9 vessels on their Asia – Europe services. By increasing the number of vessels dedicated to this route, Maersk and MSC demonstrate their commitment to meeting the demand for cargo transportation between Asia and Europe.

  MSC has also reintroduced The Dragon Service (Asia - Med) that will connect Asia to Israel, Italy and the South of France. With this service, MSC will be the first carrier to offer a direct call to Naples, giving their clients access to the South Italian market.

- **Industrial action** - Rail strikes in Germany and vessel movement shut down at the Port of Hamburg have severely impacted rail freight and maritime operations, causing extensive delays and disruptions to the supply chain. In France, ongoing protests against the pension age increase have led to road blockades and disruptions, particularly in the Calais region. As a result, truck operations in the area have been significantly affected.

  These disruptions have caused extensive delays and interruptions in rail freight, maritime operations, and truck operations, leading to challenges in meeting delivery schedules and maintaining the efficiency of the supply chain. Shippers may need to explore alternative routes, modes of transportation, or adjust their logistics strategies to mitigate the impact of these disruptions and ensure the timely movement of goods.

- **Geopolitical and natural disasters** - The Ukraine-Russia conflict persists, affecting raw materials, energy, and supply chains. High oil and gas prices contribute to record inflation, while major shipping lines continue to suspend services to Russian ports.

  A recent earthquake in Turkey severely damaged transportation infrastructure, including roads, bridges, and the Port of Iskenderun. In response to the situation, carriers have imposed surcharges and redirected cargo to alternate Turkish ports to mitigate the impact of the damaged infrastructure. Shippers may need to adjust their logistics plans, explore alternative routes, and work closely with their carriers to minimise disruptions and ensure the efficient transportation of their goods.

[2] Source: *Xeneta*. Date range 1st June 2022 vs 1st June 2023/ 40ft cube.

Trade Lane Analysis

Europe - North America

Rates

-63.43%

Europe - US West Coast

Rates

-75.60%

Far East - US East Coast[3]

Key points:

- **Demand** - The US is experiencing a decline in demand, which is leading to lower rates and impacting imports of goods from the EU. In January, there was a notable 9% year-over-year increase in US import demand from North Europe. However, this trend reversed in February and March, with a decline of 5.7% and 16.3% respectively compared to the same months in 2022.

  This indicates a potential slowdown in business activity and consumer demand, which may affect the volume of shipments and overall trade flow. Shippers need to closely monitor market conditions and adjust their logistics plans accordingly.

- **Capacity vs spot rates** - Unlike the Transpacific and Asia-Europe trades, the Transatlantic trade does not show a strong correlation between capacity change and spot rates. The time lag between peaks of capacity loss and spot rates in the Transatlantic trade has increased from 5 months to 9-10 months.

  Additionally, spot rates in the Transatlantic trade remain significantly higher than pre-pandemic levels. The increase in spot rates has also been delayed compared to other trade lanes. Similar patterns are observed in other Transatlantic trades, such as the North Europe-North America East Coast trade. These findings suggest that factors beyond simple supply and demand dynamics affect freight rates in the Transatlantic trade.

[3] Source: *Xeneta*. Date range 1st June 2022 vs 1st June 2023/ 40ft cube.

Freight strategies

Demand remains low globally and shippers are keeping an eye out for the restocking period. Although freight strategies differ depending on industries and business models, they play a crucial role in optimising transportation operations and reducing costs for businesses.

Take a long term view of your rate strategy

Engaging in the spot market for the sake of rock-bottom prices may not be a sustainable long-term strategy, as it presents certain limitations.

- While spot markets do offer immediate cost advantages, businesses should prioritise long-term value considerations. Opting for long-term agreements, even with a slight premium over spot market rates, can provide the necessary assurance for restocking purposes and ensure the availability of capacity.

- It is important to acknowledge that decisions may vary depending on each business's unique circumstances. For low-value, low-margin commodities, pursuing the absolute cheapest rates may be the priority. However, other businesses may find it more beneficial to explore shorter-term contracts or strike a balance by utilising a combination of contract durations to optimise their logistics strategies.

Cost efficiency

Maximising profitability in a low-demand environment requires effort to control costs throughout the supply chain.

- Establishing robust visibility in the supply chain helps businesses to identify and address inefficiencies, bottlenecks, and areas requiring enhancement. By leveraging accurate and real-time information, businesses can optimise inventory levels, mitigate carrying costs, and avert stock outs or overstocking scenarios.

- Implementing a centralised platform within the supply chain facilitates seamless data sharing, collaboration, and visibility among all stakeholders. This approach streamlines communication, minimises expenses associated with manual tasks, delays, and risks of miscommunication.

Managing blanking strategies

Ever since the start of the year, carriers have increased the amount of blank sailings in their sailing schedules.

- It is crucial for shippers to recognize that blanking strategies have the potential to disrupt their intended shipping schedule. Therefore, shippers should take a proactive stance in adjusting their shipment plans and timelines accordingly.

- Through close collaboration with their freight forwarding partners, they can explore alternative options to minimise the impact, such as rescheduling shipments, consolidating cargo, or leveraging alternative shipping routes.

Setting up for success

In 2023, shippers must proactively prepare for continuing disruptions in the supply chain. Factors like industrial action and overstocking can lead to increased shipping costs, missed revenue opportunities, and dissatisfied customers.

Businesses also need to be ready with effective inventory management strategies for when the restocking period occurs. Good restocking involves accurate demand forecasting, optimised inventory levels, efficient logistics, and strong supplier relationships to ensure timely replenishment and meet customer demands effectively.

To grasp the opportunities and navigate the challenges, supply chain teams require a reliable freight forwarding partner to help them collect and understand their data to make the best decisions for an evolving market.

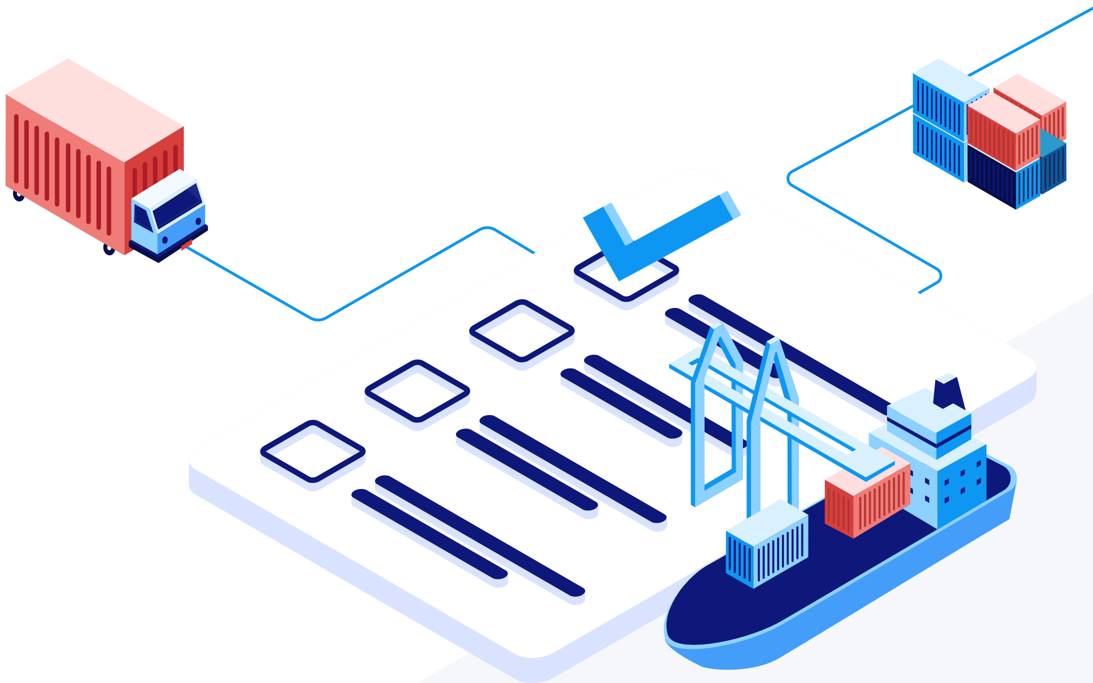
- End-to-end supply chain visibility: With Zencargo's platform, you can easily track individual SKUs throughout the entire process, from purchase order to delivery. Our automated exception management system ensures timely resolution of any issues, allowing you to align stakeholders and execute with confidence.

- Proactive solutions: We understand that the market is constantly changing and supply chains always need to keep up. By leveraging our platform analytics and our in-house expertise, Zencargo is dedicated to creating pro-active solutions for our customers to ensure that they stay ahead of the game.

- Extension of your supply chain team: Zencargo integrates seamlessly with your supply chain team with a combination of our platform and team of experts. We provide dedicated account management and advice whilst our technology enables real-time tracking, data-driven decision-making, and efficient collaboration.

Get in touch

To find out more about how Zencargo can support your team in 2023, **get in touch**



If you have any questions or would like to speak to our experts, please feel free to get in touch via our website

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