HOW IMPORTANT IS THE GROWING SIZE OF CONTAINER VESSELS?

ABOVE:
HMM Algeciras in the Port of Hamburg
(Photo: HHLA/ Dietmar Hasenpusch)

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Early 2020, the unaware pessimists were predicting total collapse of the container carriers, both on the revenue side and on the profit side. The bulk commodities, except for crude oil tankers, were seen as immune to the containerised trade. The first half of 2020 seemed to bear those pessimistic sentiments.

According to Clarksons Research, in May 2020 nearly 12% of the entire global fleet was idle. Meanwhile, the ocean-going ships in service struggled with impossibility of crew rotations stranding thousands of sailors at sea.

At the time of writing we are not at the end of 2020 yet, but then, one year does not mean much, especially when measured against three decades of ship's lifespan.

More big ships were added to the global container fleet in 2020 which will make the capacity game in years to follow very interesting. These new arrivals represent orders placed for 24,000 TEU vessels a few years ago. Major buyers then included HMM and COSCO, but other lines kept growing their fleets as well.

Carriers adding capacity should be good news for the shippers continuously yearning for lower shipping costs. But the wisdom of investing applies here as well. Past performance is not a reliable indication of future outcomes. This time around, the shippers should not expect the destructive miracle of near zero rates, the bane of the shipping industry a few years back. The culprit is the digitalisation. It has been talked to death in conferences, I know, but the results are finally showing up. This, and the concentration of supply within the three major alliances.

Fast forward to October 2020 and the reality demolished the pessimism abundant in March of 2020. The carriers acted much faster at reducing sailings and blanking capacity, in many markets much faster than the demand suggested. Better digital demand forecasting tools and some overabundance of caution took out too much capacity in some markets, but that has been quickly corrected. Alliances held well, as all carriers remined of the same mind – reduce capacity first, keep the rates steady. The yield optimization technology allowed some carriers to be very selective in which request they accepted and which ones got declined. The results, much better than expected may I say, were seen in the quarterly financial results throughout the year. As opposed to the sea of red ink, the profit/loss statement showed sea of black as far as an eye could see.

While the panic about immediate results evaporated, the fundamentals of the industry have not changed. An idling vessel is a drag on the balance sheet. An idling vessel does not cost much to operate, but it is not earning anything either. The fact that the industry has not earned its cost of capital for more than a decade is not going to be diametrically different just because of the windfall from high rates in 2020.

FLEET RENEWAL

With cash on hand, the carriers may also continue renewing their fleets replacing old bunker guzzlers with fuel-efficient units. The order book shows something of a trend that ports and shippers should keep in mind. At the cost of the medium-sized ships, the global container fleet is developing toward the mega-large container ships and the smaller feeder ships. At the top of the range, expect more of the 24,000+ TEU ships like the HMM Algeciras. It was in 2019, Maersk declared the end of vessel supersizing, but I am sure this trend still has a few years to run. At the bottom of the range, orders for 5,000-7,000 TEU ships are indicative of the strategy for the next decade.

The big ships are not going to call on many ports, so the rise of the port mega hubs with superb hinterland connectivity will continue. That is good news for the usual suspects like Shanghai, Shenzen, Rotterdam, Hamburg, Los Angeles/Long Beach, or New York. Ports of lesser importance and poorer connectivity which made infrastructure investments hoping for the ultra large vessels calls may not see those ultra large vessels, but it doesn't mean they will not see bigger ships.

That brings us to the mid-size ships. These are the ultra large ships of the last decade ranging between 12,000 TEUs and 18,000 TEUs. These ships are still on the books and have not paid for themselves to be shipped off to the breakers. This means that the carriers will continue cascading them to ports with markets more suitable to 8,000-12,000 TEU ships. Demonstration of this trend could be port of Charleston on the south-east coast of US becoming a regular port of call for CMA CGM 15,000 TEU ships. Port calls like this were once in a blue moon promotional itinerary event, but no longer.

CHANGING BUSINESS MARKETS

The mid-size are too clanky to execute shipping for the radically changed business and consumer markets. The smaller, energy-efficient ships mentioned earlier are much better suited for point-to-point specific spokes connecting the hubs served by the giants to promising hinterland gateways. The hub and spoke architecture seems to fit continuous rise of the e-commerce trade, even if caused by the carriers stocking up on the super-sized ships. For this system to operate efficiently and to provide highly competitive transit times, the carriers need to orchestrate the shipments with precision seen before only from express parcel aggregators like FedEx, UPS or DHL. This explains the reason for Maersk, CMA CGM and COSCO to bring logistics orchestration in house. If not for the sheer volumes generated by e-commerce and its demands for door-to-door speed and precision, the carriers would leave orchestration to the freight forwarders. Until now.

Rapid recovery in China, continuous strength of import volumes, cheap fuel – what could possibly go wrong for the shipping industry? As any sailor worth their salt knows, calm sea and smooth sailing are possible for a while, but a storm is never farther than the horizon.

FACING REGULATIONS

One dark cloud relates to fleet renewal and ship purchase financing. Newer ships promise compliance with emissions regulations and, in general, cheaper cost of ownership due to technological innovation of on-board systems. While buying new ships in light of regulation is a good ship owning argument, the bankers are much more cautious. The notorious volatility of shipping industry broke a lot of banking backs and depleted ranks of willing and able financiers. While not a complete credit crunch as far as the shipowners are concerned, the credit is and will remain tight. Any carrier going to the bank will need to have an incredible business model story for the cash spigot to open.

The other dark cloud relates to competition regulation. This affects both further consolidation among the carriers themselves, concentration of capacity power through alliances, and the developing vertical integration model. Many people heard Maersk talking about becoming the Amazon of the seaborne trade, but not many people had figured out what that meant. Up to now. By bringing supply chain planning capabilities of Damco in house and buying technology-based companies providing services necessary to keep the cargo moving with minimal friction, Maersk has shown how to become fully self-sufficient in serving needs of shippers through direct relationships. Their recent warning shot across the bow of DB Schenker has demonstrated how valuable that ownership of vertical integration components has become. If the "big 4+2" take the same route, will the competition bodies react or leave the carriers alone? It is not an easy question to answer.

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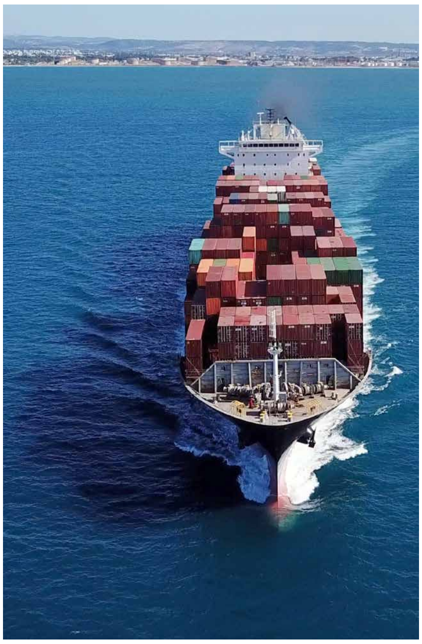

ABOUT THE AUTHOR

Kris Kosmala brings many years of extensive global experience as a business operations executive in the services and technology industries. He provides independent management consulting across many segments of maritime industries. Previously, he has held senior roles at global organisations specializing in supply chain and operations optimisation including Quintiq, Royal HaskoningDHV, and Oracle. He regularly speaks at industry events and features in industry media discussing application of the latest information technology and automation innovations in business and operations related to global supply chains.