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Ocean carriers struggle to match capacity with plummeting demand

Ocean contract rates remain far above average spot market levels on both major east-west trade lanes out of Asia. Photo credit: DCT Gdansk.

Marine terminals | Container lines

Keith Wallis, Special Correspondent | Nov 29, 2022, 10:44 AM EST

Capacity discipline by ocean carriers is being severely tested by demand and rate levels that continue to plummet on the two major trades out of Asia, with little visibility on when the market slowdown will hit bottom.

While carriers are withdrawing significant amounts of capacity through a vigorous blank sailings program, they have not been able to match the rapid drop in demand on the Asia-Europe and Asia-US trade lanes.

“It is clear that the drop in volume — to a point where we are substantially below pre-pandemic levels — is driven by a collapse of some of the largest and longest deep-sea trades,” Sea-Intelligence Maritime Analysis noted in its weekly Sunday Spotlight newsletter. "This is not good news for the carriers, as this will further fuel an overcapacity problem in the near-term future.”

Carriers have announced blank sailings on Asia-North Europe and both the Asia-US West Coast and East Coast trade lanes in January, traditionally a peak shipping period ahead of factory closures for Chinese New Year that falls on Jan. 22 next year.

But the amount of capacity to be withdrawn compared with the total capacity is down significantly from previous months, Sea-Intelligence data shows. The 129,000 TEU to be withdrawn on Asia-North Europe in January 2023 is less than half the capacity cut in January this year, and sequentially represents 6.1 percent of the total capacity compared to 14.5 percent in December and 15.9 percent in November.

The 112,089 TEU set to be blanked to date in January next year on Asia-US West Coast routes is almost seven times less than the 744,180 TEU canceled this past January, and far off the 18.1 percent of capacity withdrawn in December and 26.5 percent cut in November, according to Sea-Intelligence.

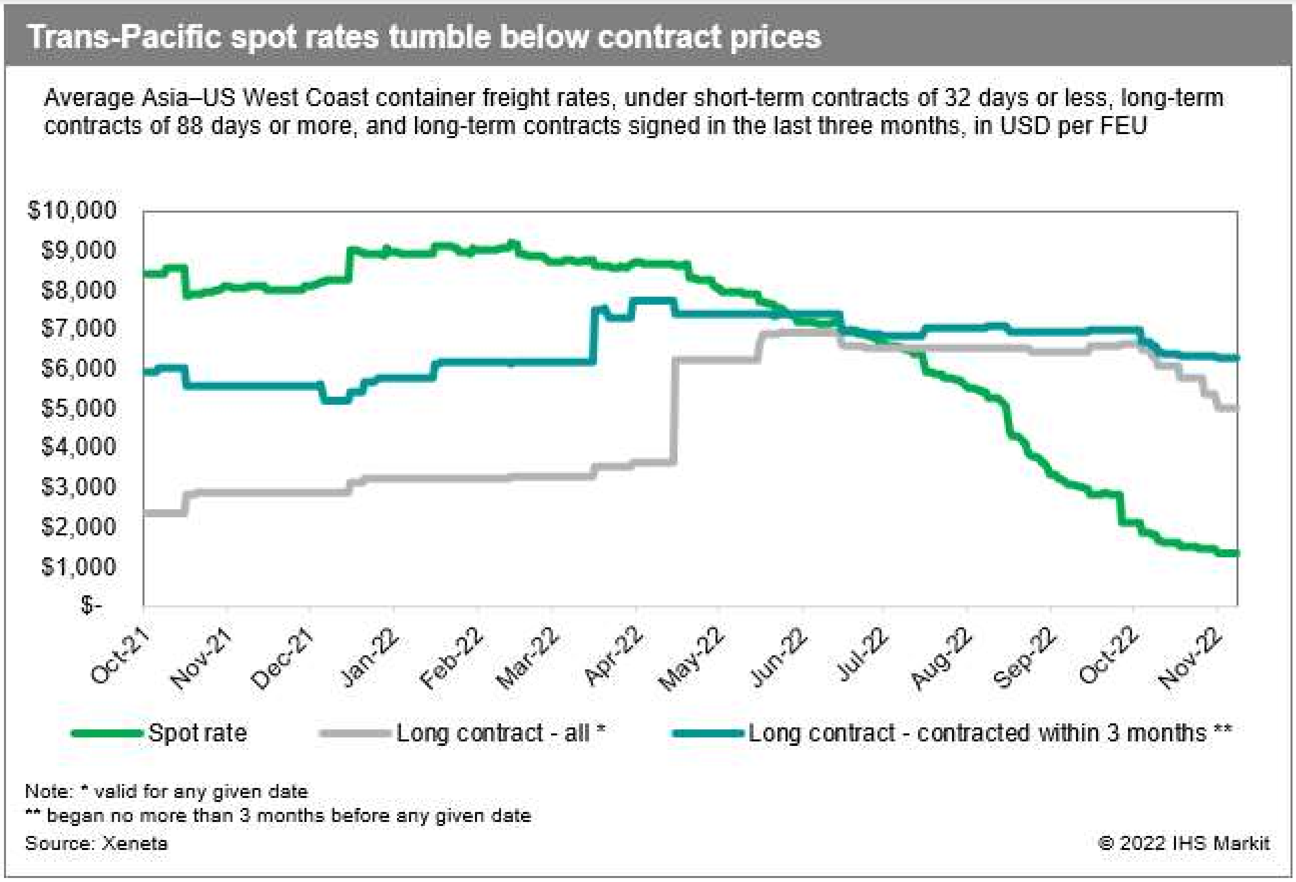
So far, the blank sailings have been unable to stop a rapid decline in spot rates on both trades out of Asia, with conditions ripe for a rate war.

Gap between spot and contract ‘too big’

A Europe-based logistics director for a global retailer said judging by the continuing collapse of spot rates, it appeared the major trades out of Asia were already engaged in a rate war.

“Carriers can't control volume, but they are obviously accepting rates that are at 2019 levels,” the source told JOC.com Tuesday. “With utilization continuing to slide, carriers with the lowest unit costs will sit it out for as long as they can, and that may as well be called a rate war.”

He added that while spot rates were declining rapidly, long-term contract rates on



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shows long-term rates on Asia-US West Coast on Monday of $5,471 per FEU were $3,620 per FEU higher than the spot rate, and up 60 percent year over year.

It was a similar picture on the Asia-North Europe trade, where average long-term rates of $4,547 per TEU were $3,000 per FEU above the spot market and 55 percent higher than contract rates during the same week last year.

“The higher rates currently being paid in the contract segment will not hold, simply because the differential with the spot market is too big,” the logistics director told JOC.com. “Chief executives will be asking questions and forcing their procurement folks to break into contracts and renegotiate. It’s already happening, and I think it will accelerate. It’s just a question of time.”

While shippers attempt to renegotiate existing agreements, the trans-Pacific contract negotiations in the first few months of next year will be difficult for all parties, according to Xeneta CEO Patrik Berglund.

“The carriers will be desperate for volumes, but, at the same time, the shippers won’t have the high volumes that unlock the best prices,” he wrote in a market update last week. “What we might see is that forwarders are the big winners, as they can find a

With a host of factors stacking up to reduce consumer demand for manufactured goods — war risk, skyrocketing energy costs, political instability, and general inflation — DHL expressed concern that a more structural change was developing within the container shipping markets.

“Liner shipping’s traditional peak season barely materialized in 2022 and many industry observers feel that the slump is structural, rather than seasonal, with fears of a global recession,” the forwarder noted in a November ocean freight update.

“The easing of COVID-related travel restrictions appears to have caused consumption patterns to shift back toward services — particularly travel and vacations — at the expense of shopping,” it added.

Marginal growth in 2023 demand

Containerized trade grew just 1.2 percent this year and will only marginally increase by 1.9 percent in 2023 in the face of strengthening macroeconomic headwinds and a slowing Chinese economy, according to the United Nations Conference on Trade and Development (UNCTAD).

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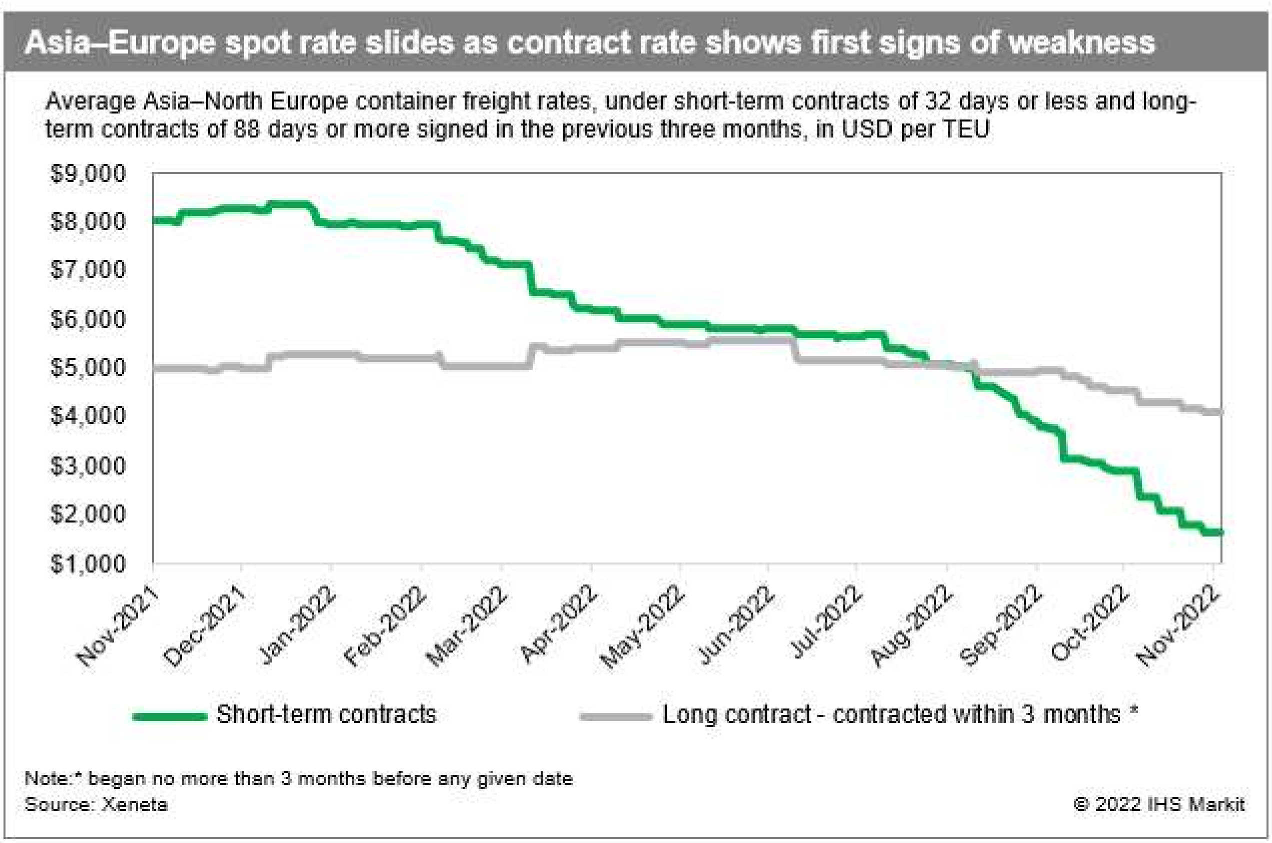

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which is the world's largest exporter, a zero-COVID policy triggered shutdowns and disrupted manufacturing, logistics, and supply chains."

Other issues affecting supply chains include the war in Ukraine, industrial action affecting ports and terminals, and severe weather across many regions, UNCTAD said.

"All these problems spell further trouble for global supply chains and logistics, and for maritime trade," it added. "By the fourth quarter of 2022, projected global economic growth had been revised downward, with fears that the world economy could slip into recession and stagflation."

World Trade Organization (WTO) economists predict global merchandise trade volumes will grow by 1 percent in 2023, down sharply from the previous estimate of 3.4 percent. The International Monetary Fund (IMF) estimates global economic growth of 2.7 percent in 2023, but gives a 25 percent probability that growth next year will be lower than 2 percent.

Based on the IMF economic outlook, shipping association BIMCO has forecast global volume growth in the range of 3 to 4 percent in 2023, falling to 1 to 2 percent if the IMF's downside scenario occurs.

Easing bottlenecks unlock capacity

Declining volume is not good news for carriers that are facing a significant oversupply of tonnage heading into the new year caused by easing supply chain congestion and a glut of new vessel deliveries.

Schedule reliability is steadily improving across trades out of Asia as port and inland logistics bottlenecks improve, releasing delayed capacity back into the market. Asia-North Europe on-time performance in October was at 44.3 percent, up from just 20.5 percent in the same month last year, according to Sea-Intelligence. Asia-US West Coast schedule reliability of 35.7 percent in October was a vast improvement on the 9.8 percent from October 2021.

The container shipping orderbook was just shy of 7 million TEU at the beginning of October, according to data from S&P Global, parent company of JOC.com. With more than 1.65 million TEU of new capacity set for delivery in 2023, Xeneta believes the net fleet growth will be 5.9 percent once scrapping has been factored in.

Drewry's estimate is for net fleet capacity to rise by as much as 11.3 percent next year, while BIMCO has forecast fleet growth of 7.8 percent.

Analysts and carrier executives are divided over how much of this excess capacity will be absorbed by new International Maritime Organization (IMO) environmental regulations that come into effect from Jan. 1.

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