

# COVID mystery: a new era in liner shipping?

Container Owners Association, 2020

22<sup>nd</sup> October, 2020

Tim Power  
Managing Director, Drewry

# The COVID-19 mystery

---

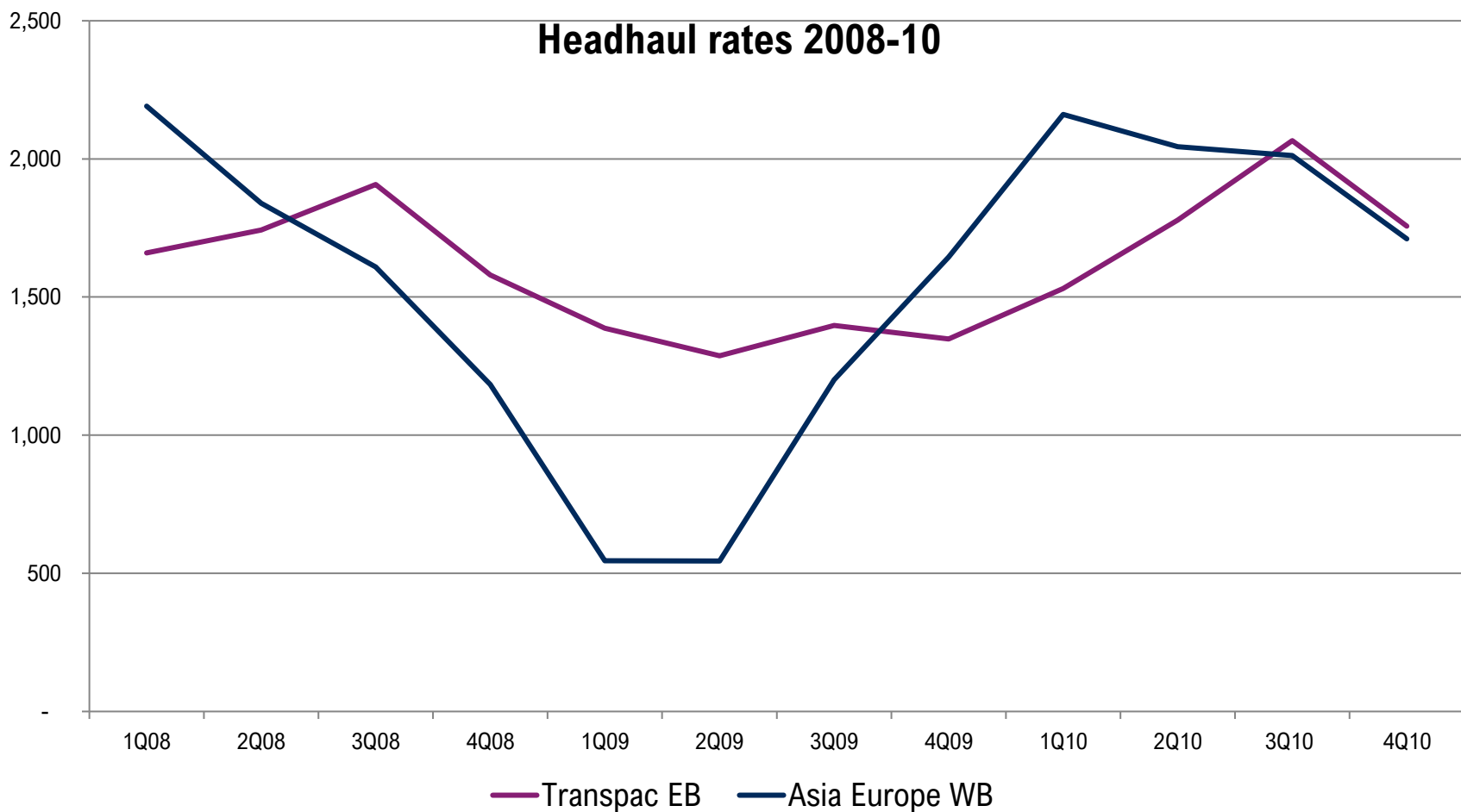
How is it that, after a decade of financial disappointment, lines are now making record profits despite the volume downturn caused by the COVID-19 pandemic?

# 2009 and 2020: compare and contrast

---

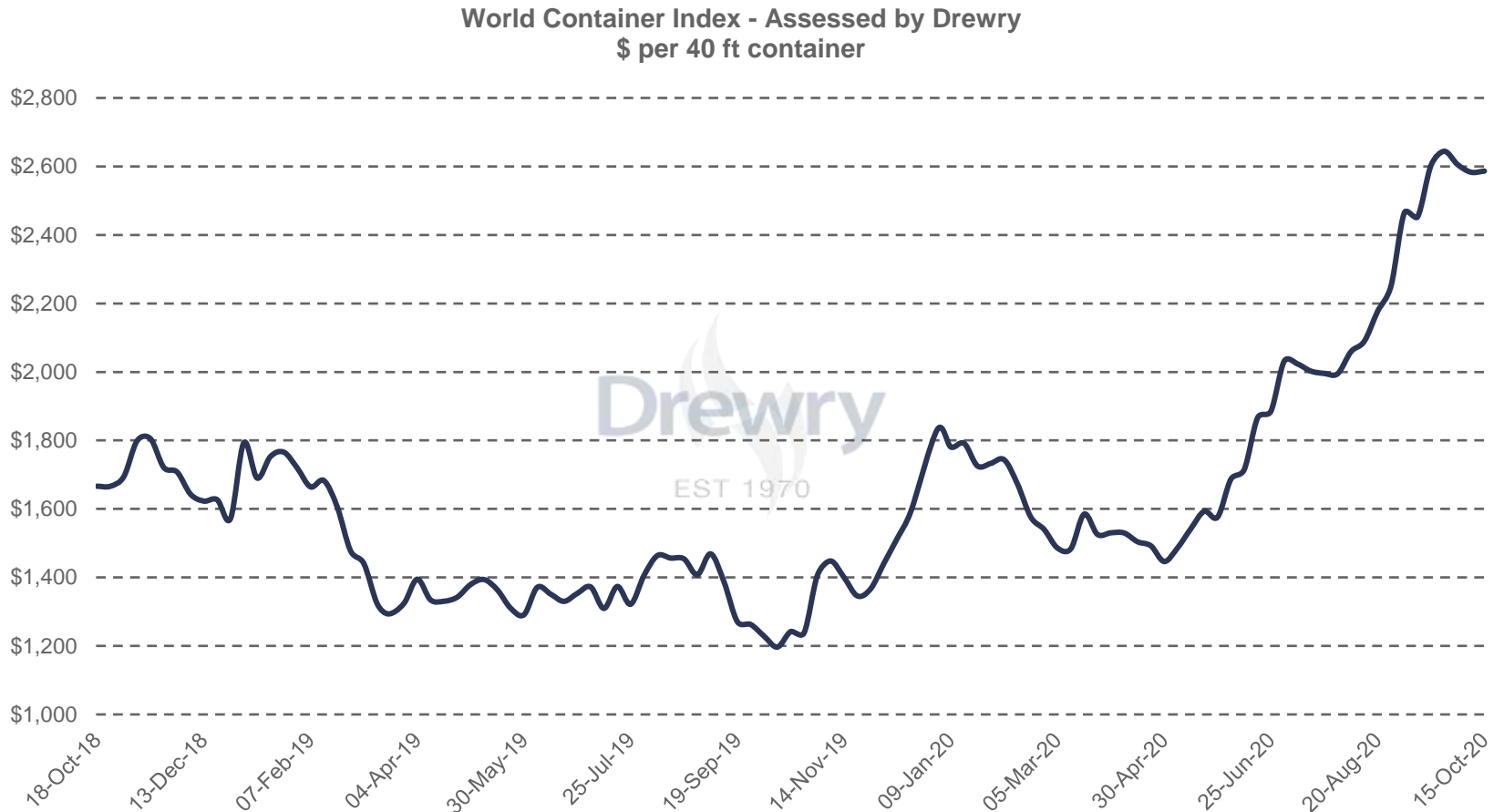
# Freight rates: 2008-10

In 2009, freight rates collapsed on the Asia – Europe trade and fell by 32% on the Transpacific trade



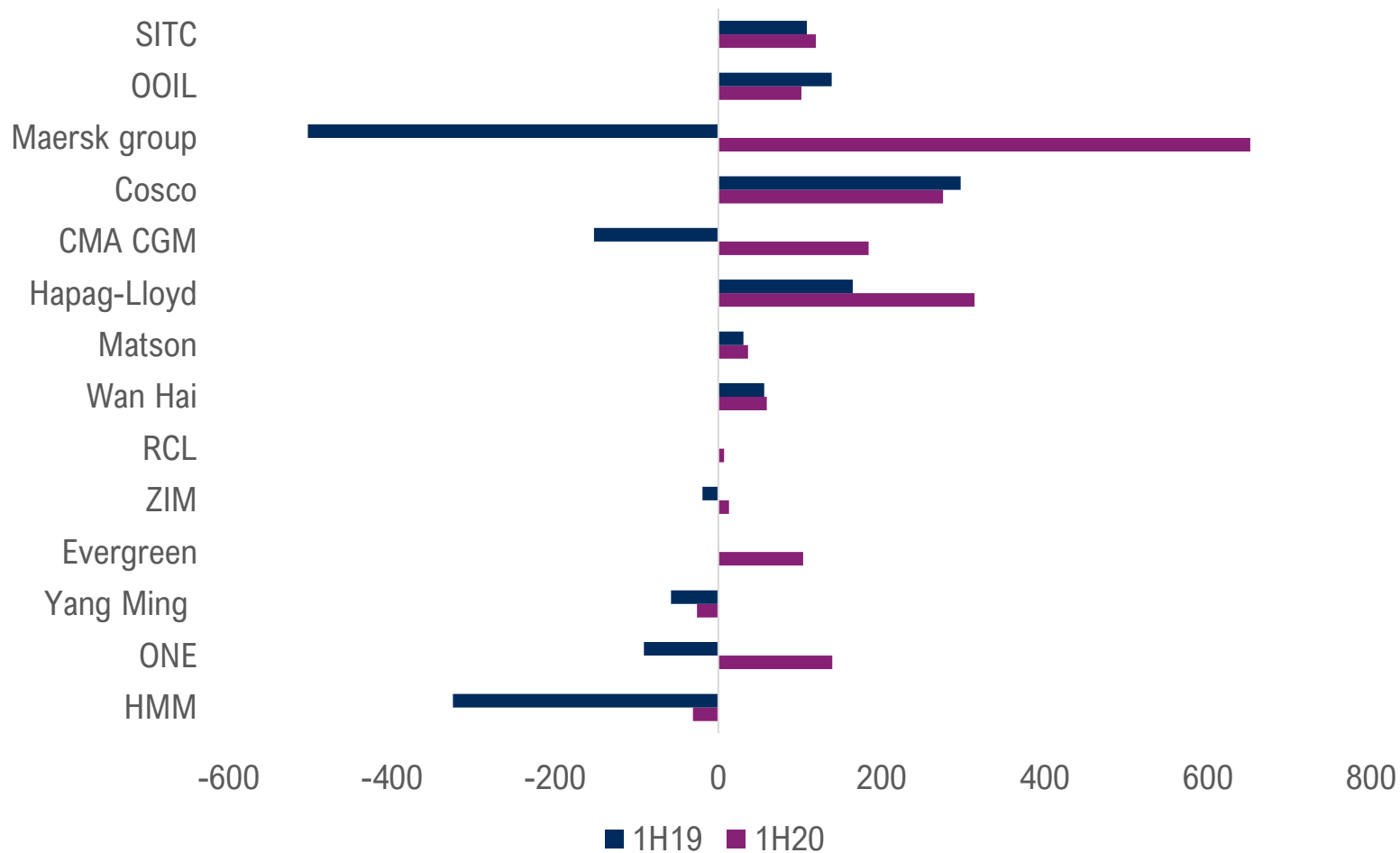
# 2020: spot the difference

Asia – Europe rates rose sharply in Q4 2019 before eroding to Q2 2020 and recovering. Transpacific rates were stable and are now rising rapidly



# Financials

Aggregate profit of 14 carriers approx. USD 2bn in 1H20 (vs. negative USD 351mn in 1H19)



Source: Company, DMFR

# Container shipping fundamentals

---

# Liner fundamentals

The liner industry has been unable to make sustainable profits...

Factor	Effect	Comments
Economies of scale	Structural overcapacity	Lines always build bigger vessels to exploit economies of scale. This leads to continual overcapacity
Perishability	Push for short-run contribution – rate erosion	Unused capacity cannot be stored. Lines cut rates in order to boost utilisation
High operational gearing	Push for short-run contribution – rate erosion	Lines' networks represent a high fixed cost burden. The logical response is to maximise utilisation
Commoditised service offering	Limited differentiation of product; price competition	Price is the principal competitive weapon
Fragmented industry	No coordination of capacity development, intense competition	Too many carriers and no dominant carriers to establish market stability
Inelastic demand curve	Falling rates have a limited effect on demand	Seafreight is a negligible element in the landed cost of manufactured goods and makes no difference to end market demand



# Liner fundamentals

...but it could, with two changes. Have these changes happened?

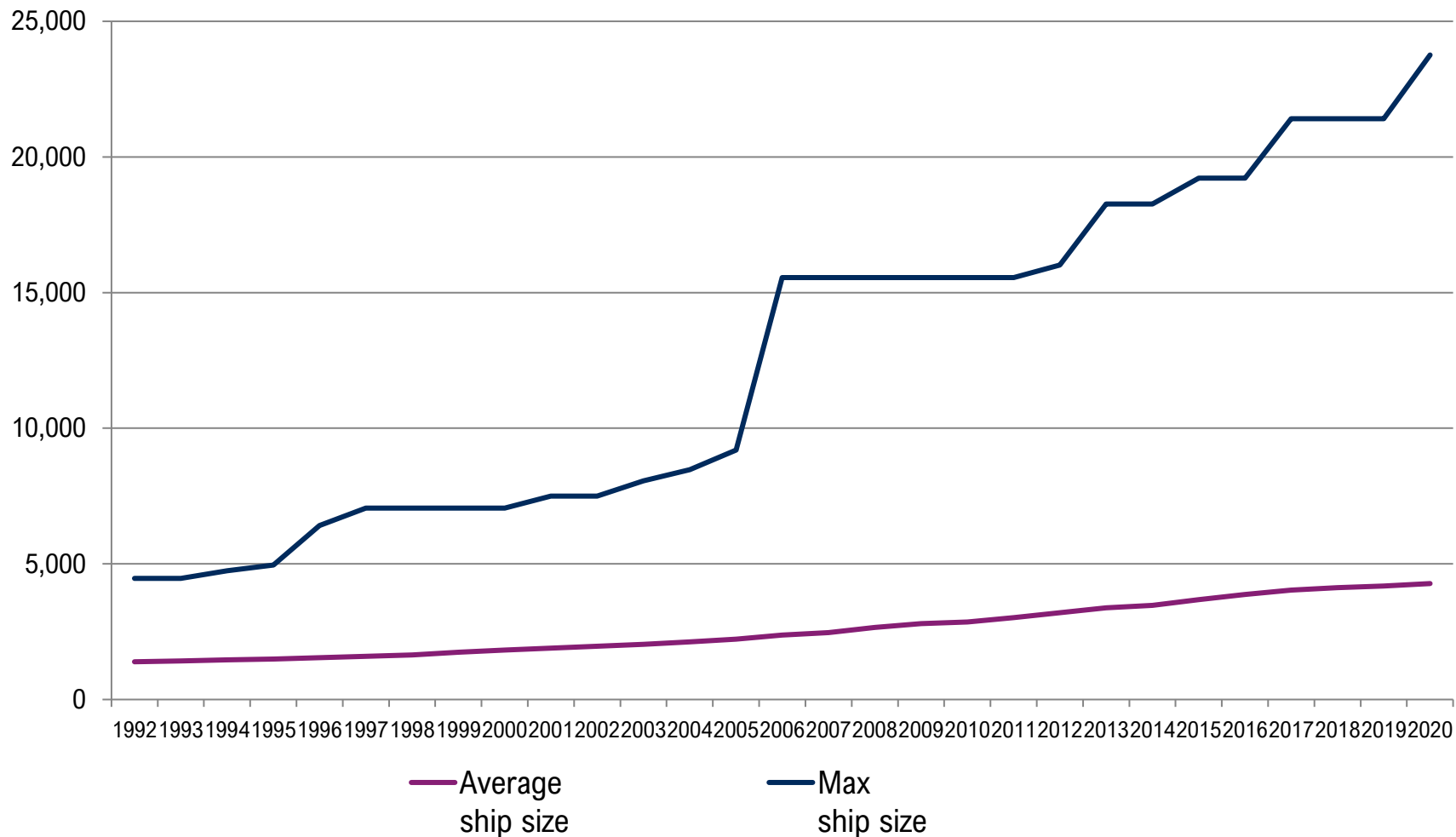
Factor	Effect	Change?	Comment
Economies of scale	Structural overcapacity	<b>Economies of scale run out</b>	<b>Lines will build to match demand not to chase economies of scale. Pursuit of share is less important</b>
Perishability	Push for short-run contribution – rate erosion	No	Unchanged
High operational gearing	Push for short-run contribution – rate erosion	No	Unchanged
Commoditised service offering	Limited differentiation of product; price competition	Unlikely	Unchanged
Fragmented industry	No coordination of capacity development, intense competition	<b>Industry consolidation</b>	<b>A small number of large carriers is able to match capacity to demand and promote increased tariffs</b>
Inelastic demand curve	Falling rates have a limited effect on demand	No	<b>Rising rates have a limited effect on demand, supporting profitability</b>

# What has changed

---

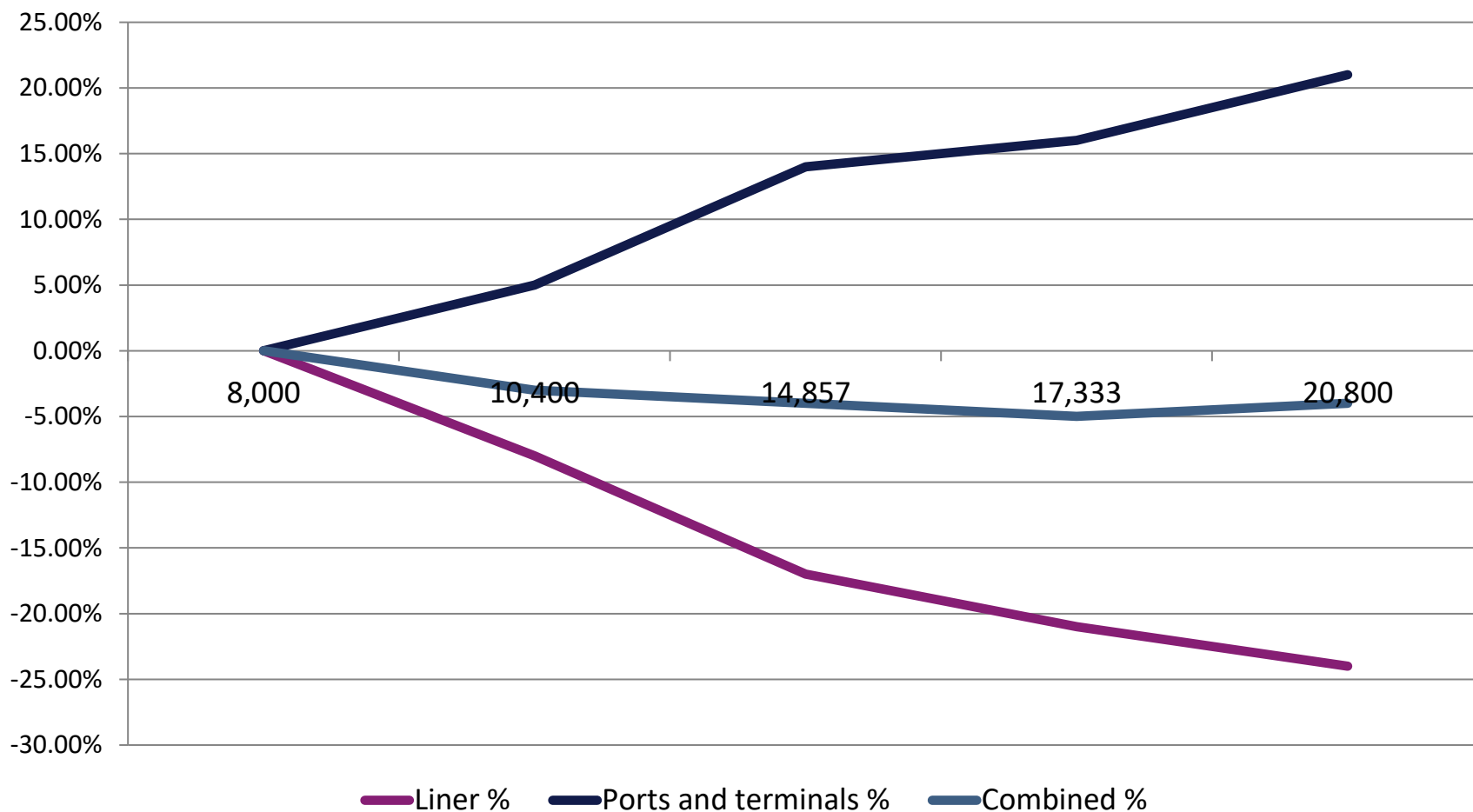
# Economies of scale: vessel sizes

## Maximum vessel sizes have rocketed since 2005



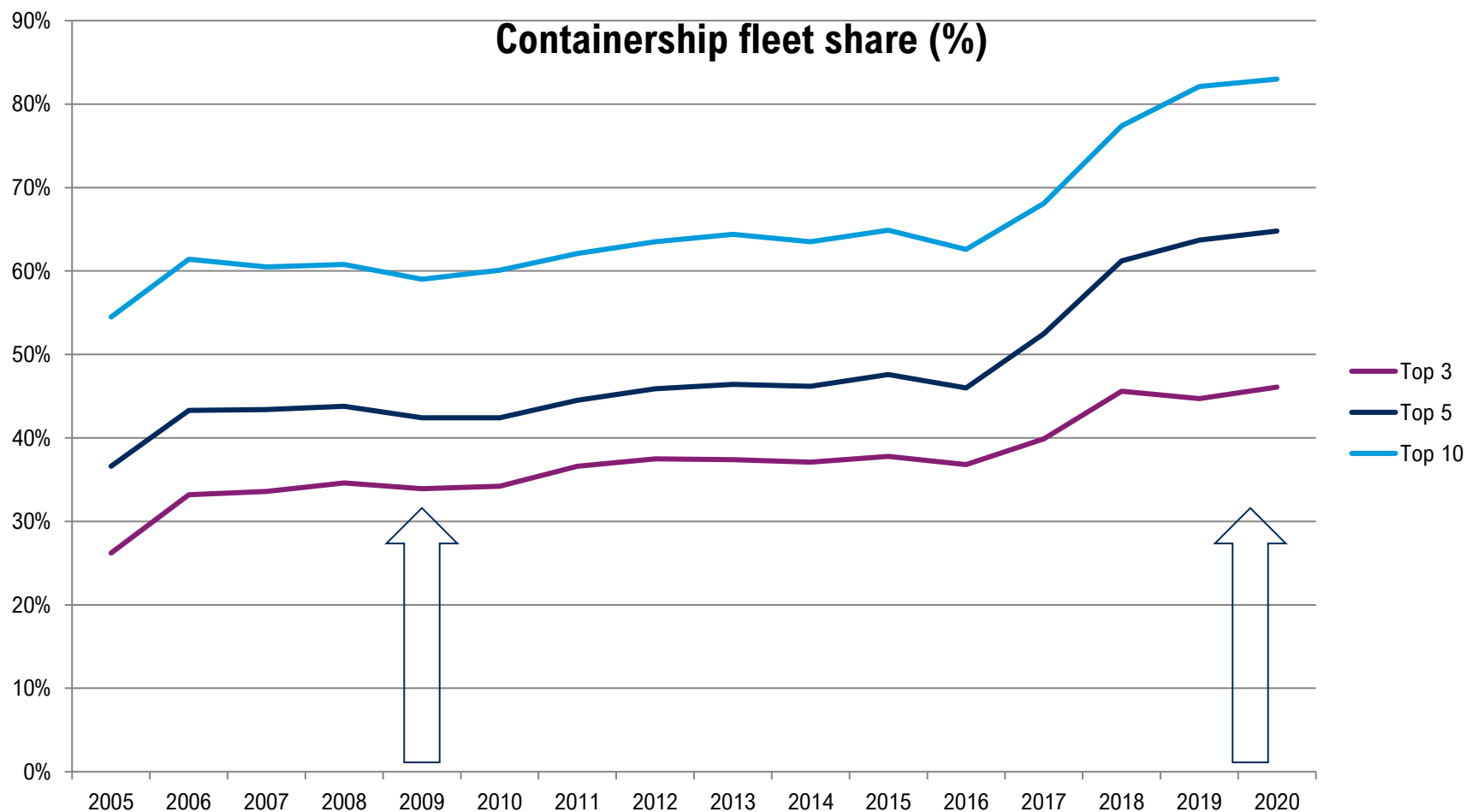
# Economies of scale: costs

Scope for vessel economies of scale in 2009 was large; now looks much less. Total system costs show no economies of scale.



# Market concentration: lines

Substantial increase in market concentration since 2016, 50% at the level of Top 5.



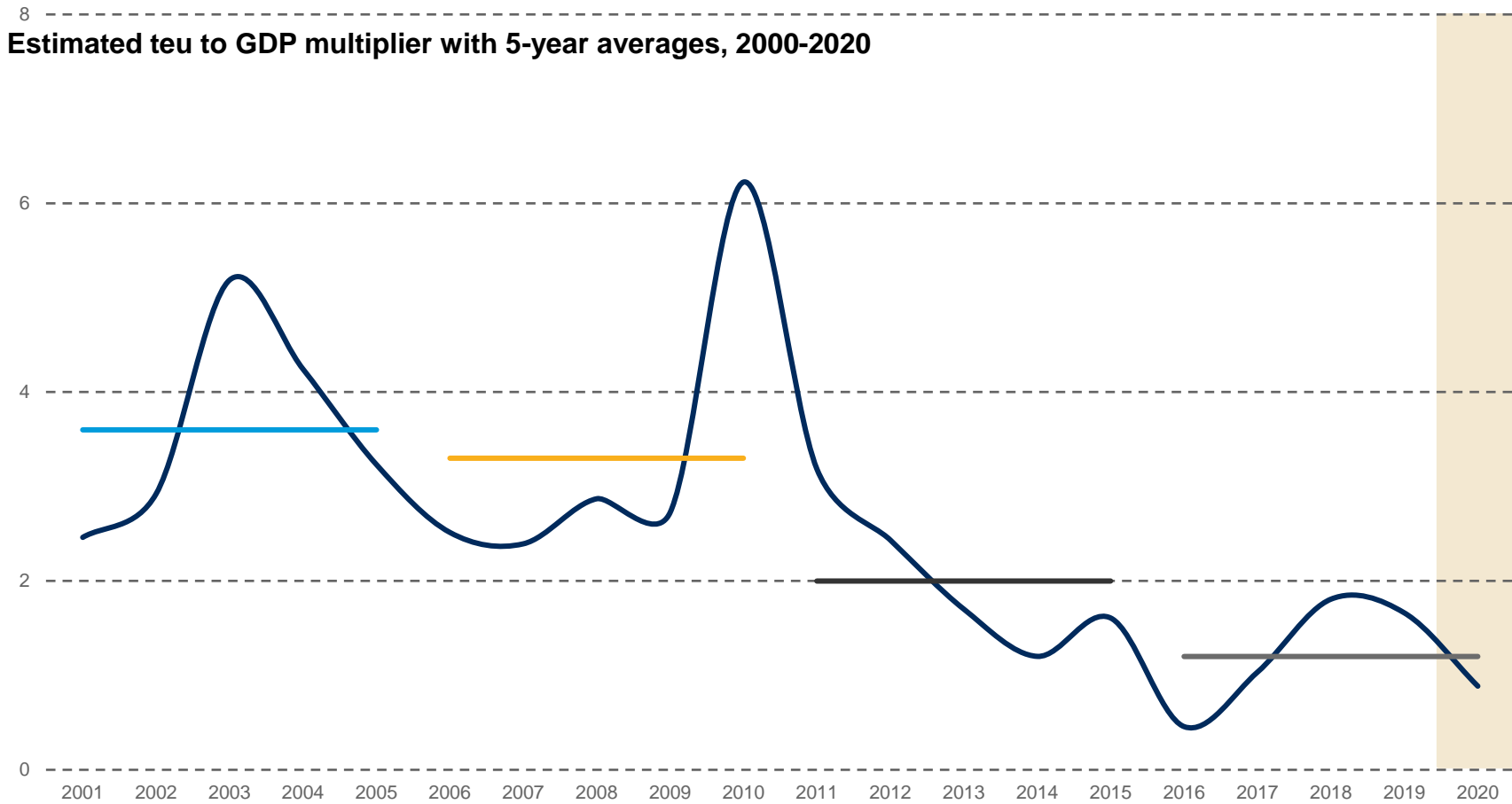
# Market concentration: alliances

The concentration of major lines into the three alliances on the main East – West trades has created the structure for effective capacity management

Shipping Lines	Previous Alliances	2016	Shipping Lines	New Alliance
Maersk	P3 Alliance (denied)	2M Alliance	Maersk	2M Alliance (with mergers)
MSC			MSC	
CSCL	CSCL / UASC	Ocean 3	Hamburg Süd	
UASC			CMA CGM	
NYK Line	Grand Alliance	G6 Alliance	COSCO	Ocean Alliance (with mergers)
OOCL			CSCL	
Hapag-Lloyd			OOCL	
NOL			Evergreen	
MOL	New World Alliance	NOL		
APL		APL		
Hyundai		Hapag-Lloyd		
COSCO	CKYH Alliance	CKYHE Alliance	UASC	THE Alliance (with mergers)
K-Line			Yang Ming	
Yang Ming			MOL	
Hanjin			NYK Line	
Evergreen	Independent	K-Line		
			<b>HMM</b>	
Hamburg Süd	Independent	Independent	<del>Hanjin</del>	

# Liner growth rate

GDP multiplier has declined steadily since 2000 and is no longer a driver of container volume growth. Long term outlook growth is modest with downside risks



# Conclusions

---



# Conclusion

---

## Fundamentals have improved but demand growth outlook is uncertain

- Scope for economies of scale is now limited. The liner arms race will abate
- Concentration at the company level and in major alliances has created the conditions in which capacity can be matched effectively to demand
- Stable utilisation will promote higher rates and margins
- Likely changes in trade patterns pose significant risks to growth in deep-sea liner trades
- Low growth should make lines more cautious about capacity expansion

## Maritime Research

Robust, objective market analysis and forecasts to inform business decisions

### Market Sectors

Container Shipping  
Ports and Terminals  
Dry Bulk  
Gas Shipping  
Tanker Shipping  
Specialised Shipping  
Ship Management  
Logistics Management  
Intermodal Transport

## Maritime Advisors

Bringing together the expertise, insight and resources clients need to achieve their commercial ambitions

### Advisory Expertise

Market Analysis  
Strategy and Planning  
Market Entry Analysis  
Operational Due Diligence  
Technical Due Diligence  
IPO Support

## Supply Chain Advisors

Tools, resources and tailored advice to support every stage of the ocean freight procurement process

### Advisory Expertise

Ocean Freight Cost Benchmarking  
Ocean Freight Procurement Support  
Network Design and Optimisation  
Commercial Due Diligence  
Hinterland Logistics Analysis

## Maritime Financial Research

A truly independent investment research and advisory service on companies operating within the maritime industry

### Market Sectors

Container Shipping  
Container Manufacturing  
Ports and Terminals  
Dry Bulk  
Gas Shipping  
Tanker Shipping

### Advisory Expertise

Credit Analysis  
Bond Analysis

### UNITED KINGDOM

15-17 Christopher Street  
London  
EC2A 2BS  
United Kingdom  
**T +44 20 7538 0191**

### INDIA

4th Floor, Tower C  
Pioneer Urban Square  
Sector 62, Gurugram  
122102 India  
**T +91 124 497 4979**



### CHINA

Unit D01, Level 10,  
Shinmay Union Square  
Tower 2, 506 Shangcheng Rd  
Pudong District, Shanghai  
China, 200120  
**T +86 21 5081 0508**

### SINGAPORE

#13-02 Tower Fifteen  
15 Hoe Chiang Road  
Singapore 089316  
**T +65 6220 9890**

