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The 40% Hanjin Rate Spike Won't Last

Trans-Pacific shipping rates peaked one week into Hanjin bankruptcy, hitting a 56% spike. Prices have since stabilized yet remain high - about 40% higher than before Hanjin filed for bankruptcy.

But ocean liners aren't rejoicing yet, as they know that these price hikes will likely be short-lived. Despite this brief respite, the shipping industry knows still has rough waters ahead, with the potential for shipping rates to fall below pre-bankruptcy rates by early November. According to Freightos CEO, Zvi Schreiber:

"The only certainty going forward is volatility. Hanjin's bankruptcy only reiterates the extent of supply available in the industry – about 10% of the industry's capacity is unused, despite Hanjin's collapse and peak holiday season. Faster access to data and mode/route flexibility is critical for shippers moving forward."

Zvi Schreiber, CEO of Freightos

Here’s why ocean freight rates are going to drop:

Overcapacity

Efforts to reverse rampant overcapacity in the freight shipping industry have still proved to be ineffective. According to Alphaliner, the three leading carriers – Maersk, MSC, and CMA CGM – have seen their TEU capacity grow by a factor of 17x, 35x and 50x respectively, while the container market has only expanded by 6x. And this expansion in size of fleet is set to continue. According to Alphaliner, the industry’s top five carriers currently have an average of 20% fleet growth on their order books.

It gets worse. By the end of the year, a full 10% of the world’s container shipping capacity will have been taken off of the market, with 500,000 TEUs of capacity scheduled to be scrapped and an additional 1.5 million TEUs of capacity currently idle). Despite these changes, this contraction will still not have reduced supply enough to be more in sync with existing demand.

Even if Hanjin, which operates (operated?) 2.6% of the market’s TEU capacity, is completely removed from the market, there is more than enough available shipping capacity to compensate for the floundering South Korean company’s 547,606 TEU capacity.

This situation has been severely exacerbated by there currently being an incredible four times more idle capacity in the market than last year, driven by more ships – especially super-sized ships – coming into commission. With so much idle capacity, it’s tempting for hard-pressed CEOs of pressured carriers to grab the opportunity in Hanjin’s demise.

Overcompensation

And that's exactly what's happened.

Hanjin controlled over 8% of the trans-Pacific route. Carriers like Maersk are operating new routes, and COSCO and Evergreen are also responding to the sudden opportunity. The sudden boon from Hanjin's bust isn't limited to ocean – air carriers are benefitting. Bloomberg reported that Samsung Electronics may be forced to charter 16 airplanes to move cargo stuck on two Hanjin ships, paying at least $8.8 million dollars for the mode shift.

There is a downside to this. As more carriers swoop in to capitalize on the short-term backlog, the rush of additional ships operating along the lane are likely to lead to an overcompensation along these routes. This will, as expected, push the currently high prices back down again.

Global Shipping Recession

Over-capacity isn't new to carriers, which is why the pace of construction has slowed for the leading ocean liners. However, while TEU supply growth rate is finally at a low of 2.9%, shipping demand growth is also anticipated to be fairly flat, hovering between 2%-4%, according to a BCG director quoted in the Journal of Commerce. This is well-manifested at the Port of Hong Kong. Between 2011 and 2015, throughput of containers declined by 18%, from 24,834 containers to 20,073. This decline continued in the first two quarters of 2016: a 12% QoQ drop in Q1 followed by an 8% drop in Q2.

Seasonality

While the magnitude of the recent spike in trans-Pacific rates is unusual, its existence is not. September typically sees an increase in shipping rates along the trans-Pacific route, as companies gear up for Thanksgiving and Christmas shoppers. Consequently, that 40% spike is a likely conflation with general holiday increases, albeit higher than most year. The effect of holiday rate increases tends subside by the middle of October. This year should be no different.

The Bottom Line

In this light, businesses should reconsider re-negotiating their long term negotiated tariff contracts. With a clear direction of downward facing rates, no defined floor and increased volatility, spot quoting is looking a lot more attractive, and may well be on the rise.

For the next few months, rate volatility is likely the name of the game. The perfect storm of a potentially excessive over-supply along the trans-Pacific route, the elimination of the Hanjin-generated shipping backlog, the end of the holiday shipping season, depressed shipping demand and ongoing over-capacity woes all indicate that the Hanjin spike won't last.

Source: Freightos