

Flash Analysis

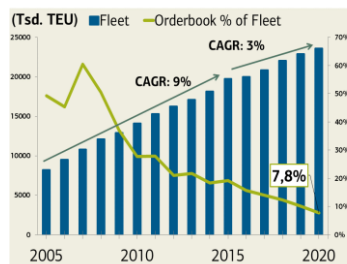
Credit Analysis

Maritime Industries

» Remarkable profits in the container shipping sector during the COVID-19 pandemic – but no surge of orders in sight.

February 2021 – Ralph Johann

Orders are at a record low,

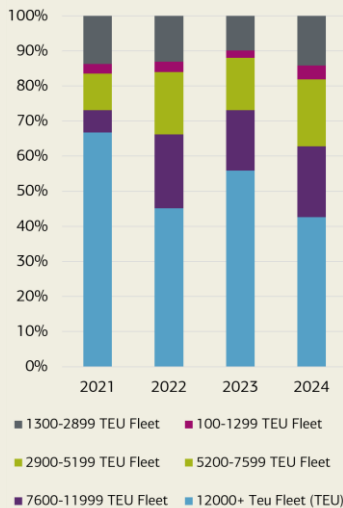


Compared with previous years, the order book in the container shipping sector is at a long-time low. The following numbers underpin the current situation: during the financial crisis, the orderbook stood at more than 60% of the existing fleet. Currently, it stands at around 10%. This comes at a time when a growing part of the operating fleet is about to approach scrapping age. Due to the shrinking order book the projected delivery of ships will further decline in the years ahead. Moreover, about 70% of the vessels scheduled to be delivered from 2020 to 2022 have a capacity larger than 10,000 TEU.

There have been meaningful orders of large container ships in 2018 to 2020:

& smaller ships are in vogue

Expected containership ordering for different vessel sizes

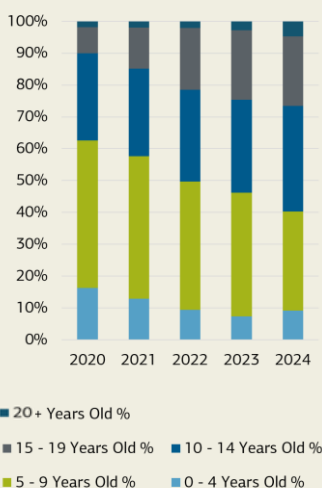


Carrier	Lessor, Tonnage Provider	Order placed	Order Time	Fuel Type
Evergreen	-	8x12k TEU, 10x24k TEU	2018/2019	Conventional/Scrubber fitted
MSC	- / BoComm	5x24k TEU, 4x24k TEU	2019/2020	Conventional/Scrubber fitted
MSC	Zodiac / Seaspan	14x15k TEU, 5x12k TEU	2018 / 2020	Conventional/Scrubber fitted
OOCL/COSCO	-	12x23k TEU	Mar/Oct 2020	Conventional/Scrubber fitted
HMM	-	8x15k TEU, 12x24k TEU	2018	Conventional/Scrubber fitted
ONE	Zodiac / Shoei Kisen	4x15k TEU, 6x24k TEU	late 2020	Conventional/Scrubber fitted
Hapag-Lloyd	-	6x23,5k TEU	Dec 2020	LNG
CMA CGM	Eastern Pac. / CMB Leasing	12x15k TEU, 5x15k TEU	2019/2020	LNG
Yang Ming	Costamare / Shoei Kisen	5x13k TEU, 21x11k TEU	2018/2019	Conventional/Scrubber fitted

What is striking among those orders: the Top-5 container liners (Maersk, MSC, COSCO, CMA CGM, Hapag-Lloyd) are predominantly reluctant to place big orders to increase their own fleets against the background of booming freight markets and an increasing scarcity of tonnage in the charter market. MSC e.g. rather charters and buys vessels on the secondhand market in large numbers. In the past few months, the liner bought 27 vessels worth almost USD 400m. On the one hand, this contradicts efforts aiming at higher environmental standards but having a positive influence on the supply-demand balance on the other hand.

...as the fleet is getting aged

Age structure of container fleet



After decades of losing money due to overcapacity and price wars, the liner companies for the first time exercised effective and concerted capacity management as a response of extremely volatile demand during the pandemic. This strategy change turned out to be more practicable as the supply side has become more concentrated (the TOP-10 liners will soon control almost 90% of the capacity).

This concentration and cohesive behavior is probably the main reason why liner companies have not returned to the yards for massive ordering, despite record breaking freight rates during the home office and “goods for services” box transportation boom. Since customers spend less on leisure and travel activities, they shift their spending habits to kitchen equipment or items of furniture.

But even in the more fragmented segment of the tonnage providers, there is still reluctance to place speculative orders (see recent orders that are mainly backed by liner charters). Besides the fact that in the past decades many investors lost money in the shipping cycles, and have therefore left the market (KGs, Private Equity, many traditional ship lenders), there are other crucial reasons why there is widespread hesitation to order new ships. First, there are many technologies available which offer an alternative to heavy fuel oil and marine diesel oil. But

Low order activity is due to technological uncertainty...

...as well as regulatory uncertainty.

Aged mid-sized workhorses need to be replaced.

Changing trade patterns will favor feeder and VLCVs for a more complex trade web

Outlook: More orders will come – especially in the small and intermediate sizes – to cater for new world trade demands

it's not clear thus far which one will be used in the future. One crucial point, which determines whether the technology prevails or not, is the infrastructure. The most sophisticated technology will not be successful if ships are not able to use it at an acceptable cost. And that point gives an edge to technologies which can be used within the already given infrastructure. Those alternative fuels are liquified natural gas (LNG) and liquified petroleum gas (LPG). Other alternatives are methanol, ammonia, hydrogen and biofuels.

There is a second aspect in terms of regulation. The EU will either impose a carbon tax on shipping or include the sector in the European Emission Trading System. This decision will also impact the profitability of some alternative fuels. The Chinese regulator is also acting and has recently announced the aim to be carbon neutral by 2060. Regulations like these have ramifications on the incentives to invest. Also, the IMO strives to reduce the carbon emission. The IMO goals for the decarbonization of shipping include a reduction in GHG emissions by 50% by 2050 (compared to 2008) and a reduction in \emptyset carbon intensity (CO₂ per ton-mile) by 40% by 2030 and by 70% by 2050 (relative to 2008). After all, one quarter of all tonnage under construction will use alternative fuels. This indicates a beginning change towards more environmental-friendly technologies.

Looking at the projected fleet and the orderbook reveals other crucial insights. First, the smaller the vessels, the older they are et vice versa. Overall, about 20% of the entire fleet is older than 15 years. In the size brackets up to 7,6k TEU almost 50% of the fleet is older than 15 years, which increases even to 60% in the 5,2k-7,6k TEU-bracket in 2024. With no big order plans in sight, this capacity needs to be replaced by existing vessels cascading down, placing increasing pressure on ports and infrastructure. Nevertheless, we believe 2021/2022 will bring about more new orders in the 4-7k TEU range in order to replace some of the ageing and less modern low-spec tonnage.

Second, the order book is heavily focused on the size ranges of small specialized vessels (1-3k TEU), the bigger size ships (10-15k TEU, "VLCVs") and the ultra large vessels (18-23k TEU), that together comprise more than 90% of the order book. This mirrors the future structure of the global container trade. Most demand is for ships that offer both size and flexibility (10-15k TEU). Additional flexibility will outweigh marginally higher slot cost. The pandemic has shown that supply chains will become even more complex and diversified, fostering transshipment hubs and larger feeders. The orderbook, therefore, represents a changing world post-COVID 19. The Asian countries are emerging from their role as producing and exporting economies as consumption markets. Intracontinental transportation between Asian economies as well as more sophisticated global supply chains become more relevant.

After all, the situation is paradoxical: In a period of dramatic economic decline, the carriers earn remarkable profits. Surprisingly, they do not re-invest the profits into new tonnage. Firstly, because it's not clear so far which technology will prevail. So, backing the wrong horse would be an expensive mistake. Secondly, the regulators have not decided yet to impose a carbon tax on shipping or include that industry into an Emission Trading System. If carriers have clarity about what their competitors in the liner oligopoly will order, they too will invest their money cautiously. Finally, there is great uncertainty about the speed of economic recovery in the aftermath of the pandemic. To sum up, these uncertainties lead to the reluctant investment activity currently observed and eventually higher investment pressure in the future. And with even more complex supply chains and a changing trade pattern will pressure will lead to a new investment cycle.