ROUTING THROUGH THE RED SEA

Cascading risk in a maritime crisis zone.

By Alexandra Walsh

Maritime shipping is under pressure at a few different chokepoints around the world. Vying for the most serious stress test are attacks on cargo ships in the Gulf of Aden and the Red Sea, an essential route for vessels transiting the Suez Canal.

Disruptions caused by the Red Sea crisis most directly affect supply chains connecting Asia and Europe. The alternative transit routes incur higher shipping costs and many days of delay for Cape of Good Hope sailings around Africa, while the slower roundtrip routes may require additional shipping capacity.

Wasted Time

The impact of risky and reduced shipping via the Red Sea and the Suez Canal is not just limited to Europe-Asia supply chains. Shipping rates for container routes from North Asia to the U.S. East and West Coasts, and the east coast of South America, have increased by a similar degree to Europe-bound routes.

These same ports in the Americas have also been directly impacted by reduced shipping capacity on the Panama Canal because of its historically low water levels. Liners looking to reduce their exposure to the Panama Canal once would have considered shipping via the Suez Canal as a back-up option. Now, using the Cape of Good Hope instead of the Suez Canal will also add many days to an Asia-U.S. East Coast route.

"The reason why the Red Sea is so crucial to trade is really very simple," says Cyrille Filott, Global Strategist Consumer Foods, Packaging & Logistics at Rabobank. "It takes eight to 15 days longer, depending on where freight needs to go, to get around Africa instead of passing through it," he says. "Mediterranean markets will be impacted more as shipping times are longer."

Filott noted also that occasionally the weather around the Cape of Good Hope can be bad in the spring leading to potentially more delays.

"Looking at the big picture, I am worried about the downstream equipment flow – a lot of mainly empty containers are passing through the Suez Canal, or stuck in the wrong locations," says Thomas Eskesen, Founder of Eskesen Advisory. "These kinds of disruptions might not be obvious now, but they will hit downstream, and the cascading effect could be pretty significant. Every week it goes on, the worse it will get."

Eskesen warns customers that have not logged in their pricing and space/equipment commitments might be in for a surprise because of the scarcity of containers now that they can't be moved around as freely as they once could.

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The Administration and Congress are considering a wide range of policies that could impact the cold chain in 2024. Key issues:

FARM BILL

- GCCA will be actively engaging with Congress to advance cold chain industry initiatives and priorities.

CLIMATE CHANGE

- Pursuing aggressive policies to address climate change, through both executive action and legislation
- Implementation of the AIM Act to phase down HFCs

TAXES

- Increasing the corporate tax rate, phasing out deductions for pass-through entities
- Raising the top marginal income-tax rate

LABOR

- Strengthening worker organizing, collective bargaining and unions through executive action and legislation such as the PRO Act
- NLRB advancing labor initiatives, like 'micro-unit' organizations and joint employer policies

BURDENSOME REGULATIONS

- Revising EPA's Risk Management Program (RMP) regulation and making additional requirements
- Changes to OSHA's Process Safety Management regulation
- Implementation of FDA's Food Traceability Rule

THERE IS SOMETHING YOU CAN DO.

To learn more about how you can contribute contact Lowell Randel (lrandel@gcca.org) or visit advocacy.gcca.org. Visit ADVOCACY.GCCA.ORG for more information.

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Economic Fallout

"We have seen the spot price on dry goods go up from China and to and from key markets," says Eskesen. "We think that the bottom of the reefer rates has been reached and then rates come up again."

Filott notes there were a lot of stories on how the additional costs may impact inflation; but Rabobank believes that it may not be that bad. "Yes, the additional costs will add to the cost price of some products, however unless the product has a low price per kilogram, then the impact will be small," he says. "The one thing that may keep people awake at night is what if the Strait of Hormuz becomes part of this as well; then some of the energy supply to Europe might come into jeopardy."

"The Red Sea crisis is a pretty massive event, probably the event the shipping lines were fearing most from the perspective of crew safety," says Eskesen. "For mankind, hopefully this is over soon, but it has already done enough damage to impact the second quarter, and we should all be concerned."

Eskesen notes there have been product shortages in the Middle East, which means if a retail customer is accustomed to buying bananas in the supermarket in Saudi Arabia or Dubai, some of those bananas will come from the Philippines. "On the surface that seems fine but then the goods that come through the Suez Canal from Ecuador or Costa Rica, don't make it to the market, and that means we see commodity prices more than doubling because of shortages." Eskesen adds, "As things become the new normal we are seeing more consistent supplies."

Eskesen says he was interested to see how the stock market reacted through the initial crisis. "The stock market reaction has been very positive with some shipping company shares up more than 25% since the crisis happened," says Eskesen. "So, the stock market thought that this would actually be a good thing, and that bottlenecks are good for shipping lines as they tie up capacity of ships and equipment." He adds, Maersk has made it public it does not expect a longer term positive benefit as it incurs additional fixed costs for vessels and containers, and since then, the share price went back to where it was before the crisis.

Shelf Impact

Filott says Rabobank looked at how alternate shipping routes are impacting food prices and product availability in the Netherlands. "The largest product imported in terms of value is palm oil followed by coconut oil. Also ginger, grapes and cashews come from Asia and are therefore impacted. Frozen products coming from the East are for example shrimp and other seafood," he says. "And don't forget – Europe also exports frozen products to the Middle East and Asia, including pork and frozen bakery."

Eskesen says he recently spoke to banana exporters who told him the travel time from Ecuador to the Middle East has gone from 35 to 50 days. He points out that impact for commodities with limited shelf life could destroy businesses completely. "Picture you're a farmer in Kenya and your transit time to the end market can't take more than two to three weeks – the shelf life of your product. Or a grape exporter in India, with a primary market in Europe, who now has to add two weeks to shipping time and hope that multiple shipments don't get backed up and arrive at the same time." Eskesen adds, "That cascading effect in delivery to retail is horrible."

Eskesen says the banana exporters are shifting operations from Ecuador eastward. "In all fairness, they didn't ask for this, but they also don't blame the shipping line," he points out. "What they're all looking for now is stability and predictability, and what they value is service providers that are honest and transparent with them and actually plan for such contingencies."

Lessons Learned?

Industry analysts are wondering if cold storage and logistics companies are likely to be more resilient to the Red Sea crisis having experienced and learned from other recent supply chain shocks … like a global pandemic.

"I do know for sure, many in the broader food industry have elevated the role of supply chain officer to a management team role," notes Filott. "Making sure supply chains function is still more critical than it was in 2019. So probably the answer is yes, they are more resilient."

The Red Sea crisis is very different from the pandemic, believes Eskesen. "The bottleneck is different as the congestion during the pandemic was at the ports, now the primary problem is shipping times are getting longer. The pandemic actually generated activity for the shipping industry as we all added home offices and new kitchens."

Eskesen says what is similar is that crews were at risk during the pandemic as they are during the present crisis. "One of the primary reasons for diverting ships away from the Red Sea is to protect the crew's welfare and avoid anyone getting shot," he says. "But in the pandemic, people were stuck on ships and couldn't get off for months, if not years, and it was very dramatic from a crew welfare perspective."

On the Horizon

The Red Sea crisis is directly responsible for cargo shipping delays and price increases in the short term. While the attacks on vessels are tied to an unpredictable conflict in the Middle East – shipping experts expect delays and cost increases are highly likely to continue as shipping firms plan for a protracted conflict.

Eskesen says whenever you prepare contingency plans in the shipping line, it's for the worst case scenario … such as the blocking of the Panama Canal or the Suez Canal. "The shipping lines are in crisis mode, I don't think they could have done anything to prevent the delays, but they've seen similar scenarios before, and they know they have to be forceful in rerouting ships as soon as possible."

Looking to the rest of 2024, Eskesen says geopolitics with two "regional wars" is the biggest threat to global trade and carriers' positioning of refrigerated equipment will be hampered by the Suez Canal diversions, even after stabilization.

Eskesen says the question of when the Red Sea crisis will end is on everyone's mind at industry conferences. "It's political, it's emotional, it's fueled by so many things, absolutely no one has any idea," he says. "But, if you were a food importer/exporter asking for the truth, I would tell you to brace yourself for a much longer contingency as it doesn't look like the crisis is going away anytime soon. The Saudi's fought with the Houthis for more than six years and they are still around, arguably with even more credibility as defenders of a Palestinian state."

Filott says he cannot comment on what the future holds for the Red Sea, "If only I knew…"

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