

focus



Global Supply Chains: Containing the Issue

With modern-day shopping reduced to a few clicks of a button it can be easy to forget the logistical challenge involved in delivering a package to your doorstep within a few days – not to mention sourcing all the raw materials to produce the product. March's Suez Canal blockage, caused by the jammed 400m-long *Ever Given*, brought the importance of global supply chains to the attention of many. Supply chains, however, were already stretched to the limit long before this.

...When COVID-19 struck...supply chains were thrown off balance...

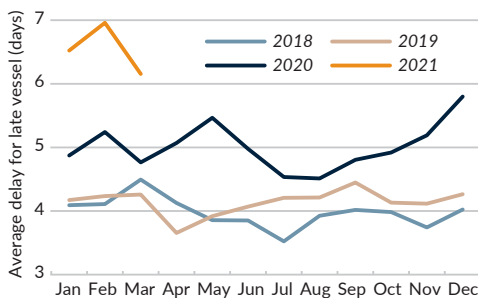


Caught in a vicious cycle

An (understandably) lesser considered impact of COVID-19 has been the effect on global trade. With increased globalisation, trade routes have become incredibly complex and interconnected. A system which requires balance. Where an issue in one link of the chain propagates throughout the entire system. When COVID-19 struck, causing countries to enter and emerge from lockdowns at different times, supply chains were thrown off balance.

VESSEL DELAYS ARE WELL ABOVE

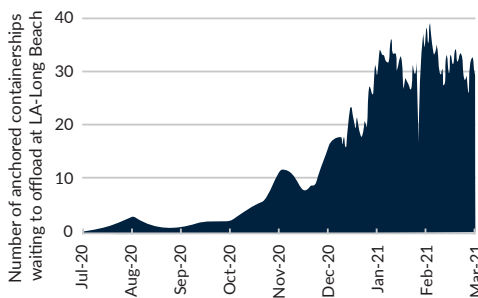
TYPICAL LEVELS



Source: Sea-Intelligence, Forsyth Barr analysis

PORTS ARE FACED WITH SUBSTANTIAL

BUILD UPS OF VESSELS



Source: Marine Exchange of Southern California & Vessel Traffic Service LA/Long Beach, Forsyth Barr analysis

Comprising 80% of global freight volume, containerised shipping plays an extremely important role in the vast global trade network. Due to congestion in the system some container vessels are now backed up waiting (sometimes for over a week) to offload at ports, with the cost to freight sky-rocketing and reliability plunging. What caused this to happen? At a (very) simplistic level:

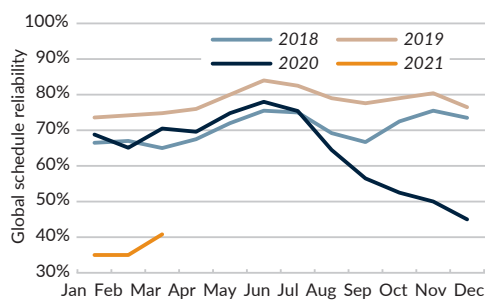
- 1) Pandemic waves caused factories to close and disrupted the normal flow of trade
- 2) Carriers reduced the number of vessels out at sea leading to cancelled services
- 3) COVID-induced labour shortages caused by absenteeism and social distancing measures impacted port productivity and slowed landside transportation
- 4) Asian economies emerged earlier from the pandemic and recommenced exporting
- 5) Economies such as the US and UK were accepting imports, but not exporting at their usual rates causing empty containers to build-up at the wrong places
- 6) More economies emerged from lockdowns with strong demand levels

The reliability of scheduled shipping services has tumbled. Making it increasingly difficult for those dependent on the cargo to plan ahead. Recent data provides some encouraging news, with March 2021 representing the first month-on-month improvement since June 2020. However, at ~40% schedule reliability, six of every 10 ships are still arriving behind schedule.



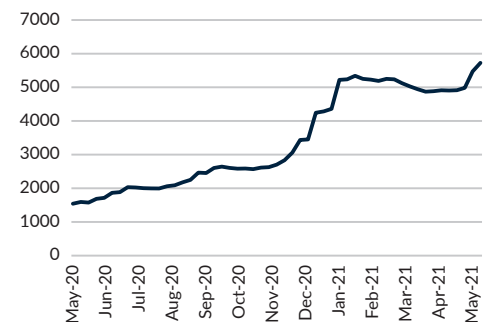
**...Ports of Auckland...has
faced issues of their own...**

**RELIABILITY SHOWS AN INITIAL
SIGN OF RECOVERY**



Source: Sea-Intelligence, Forsyth Barr analysis

**FREIGHT COSTS SOAR
(DREWRY WORLD CONTAINER INDEX)**



Source: Drewry, Forsyth Barr analysis

Despite the reduction in reliability, a combination of strong demand, scarcity of containers, and the costs of relocating empty containers has caused a dramatic spike in the price of transporting goods. The Drewry World Container index, which is designed to measure the costs of transporting goods via container, has risen over 260% since May last year.

In response to increased costs and congestion issues the average speed of shipping vessels has increased by 5.5% since June 2020, with the cost of an extra day's vessel hire now a greater concern than higher fuel costs. Shipping lines and freight forwarders appear to have successfully passed costs on and are generating excess profits. This cannot last forever. As congestion subsides and capacity is added to the system prices should normalise. In the interim, we expect these costs will ultimately be passed on to consumers.

New Zealand is no exception

Vessel delays mean that our ports and businesses are facing the same issues as those around the world. Unfortunately, the perishable nature (e.g. fruit and meat) of many of our exports is an added strain. These goods require special, refrigerated containers and are more difficult to store. Businesses, already hurting from the pandemic, may face further set-backs from spoiled goods if they have insufficient storage facilities and/or if they are unable to secure containers. To add to these troubles New Zealand's main port for imports (Ports of Auckland) has faced issues of their own. Staff shortages and delays to their automation project have impacted available capacity and amplified congestion. Meanwhile New Zealand's largest port, Port of Tauranga, has been unable to fill the gap given its own capacity constraints.

For many exporters 'price' is no longer the key consideration for the supply chain, with service 'availability' now taking precedence.

...it does highlight the vulnerability of businesses' reliance on long and skinny global supply chains...



Recovering from this backlog is no easy fix, but there is light at the end of the tunnel

Whilst there remains a high-degree of uncertainty of when congestion subsides, empty containers will eventually be repositioned (find themselves in the right place at the right time) to meet demand. Six months ago some shipping lines were expecting this to happen by April 2021. This was probably unlikely even without the Suez 'crisis', which compounded and extended the global congestion issue. Now the industry expects congestion will persist for much of the remainder of the year.

Many businesses have faced significantly higher costs throughout the pandemic. Increased freight costs and other logistical challenges have been a large contributor to this. The good news is this will abate with time. But, in today's integrated world, it does highlight the vulnerability of businesses' reliance on long and skinny global supply chains. We believe one legacy of COVID-19 will be businesses looking to build more resilient supply chains including reshoring (bringing production back from offshore closer to market), increased diversity of supply across multiple suppliers and countries, and carrying greater inventory.

Understanding that sudden changes in financial markets can cause concern or indicate opportunity, your Forsyth Barr Investment Adviser is available to provide you with advice and assistance at any time.



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