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When the dominoes start to tumble

Global crisis exposes the ties that bind shipping and commerce

SHIPPING, as I have stated many times, has little or no influence on the international trade that produces the cargoes that creates the demand for shipping services.

However, shipping can open up new markets and provide the supply chain for raw materials and finished goods. This supply chain opened Asian trade in the 19th and 20th centuries and enabled oil to move from remote parts of the Middle East and Asia to the centres of industrial and economic growth in Europe and the US.

Shipping prospered throughout the 20th century providing the materials for rebuilding war-torn nations after two world wars and opening new markets in Africa, Asia and South America.

This led to globalisation of world trade in the opening years of the 21st century, with an unforeseen surge in the Chinese economy that fuelled a shipping boom in the last decade.

Shipping was essential to this surge: China's appetite for raw materials, particularly for minerals of all types, seemed as insatiable as the appetite of consumers in Europe and the US for Chinese manufactured products. Both required large numbers of ships to feed economic expansion.

And so the dominoes of world trade were stacked against each other. Shipowners, predicting apparently endless demand for their services, launched a reckless programme of vessel orders for all classes of ships.

As China expanded its industrial base and built supporting infrastructure, it relocated millions of its people from rural areas to the expanding cities of the east and south; Shanghai, Guangzhou and Beijing.

This stacked up a second set of dominoes, creating soaring Chinese demand for energy products of all types from coal to oil and gas. This, again, required shipping services to deliver them. The chain of dominoes now stretched from China to Brazil, Australia, the Middle East and the US.

Shipping has never operated as a global industry. It comprises hundreds, or even thousands, of privately owned companies located all over the world. Only a few have publicly traded formats; even fewer are subsidiaries of large corporations.

There are few barriers to entry into ship ownership: money really is the only necessity. The markets for ordering new ships, buying secondhand ones and scrapping old ones are incredibly efficient, but are only a guide to the future in showing size of world fleets by type and related orderbooks for new ships.

Ships' employment, or charters, is mostly arranged by a global market of brokers, who arrange contracts for the movement of cargoes. However, the container sector provides regular services between ports and charges published rates for moving boxes that often include the land-based part of the journeys.

When all the sets of dominoes lined up,



Falling down: Chinese trade created a chain of dominoes that stretched to Brazil, Australia, the Middle East and Australia. Shutterstock

creating new demand for shipping, there was a rush from existing shipowners and from newcomers to order all types of new vessels. The shipbuilding market expanded too. Indeed, many orders were placed with shipyards to be built only once they had a predetermined number of orders in place.

This created a sharp increase in prices of new ships, and premiums for early delivery. This continued until late 2007, on the eve of the Lehman Brothers' collapse and the start of the global financial crisis.

By now, the world orderbook stood at 50% of current total capacity, rising as high as 70% in some sectors, had all the ships been delivered by the end of the decade.

Now, the dominoes formed a wall around world trade. And suddenly they began to fall.

Growth in demand for shipping slowed sharply, to be outstripped by the end of the decade by available tonnage and by yet-to-be-delivered orders.

As a result, nearly all the traded markets have collapsed. Numerous public and private shipowning companies have gone bankrupt or face insolvency. A huge number of ships are still being built.

The domino effect of one economic activity on others works in reverse too. But as many shipowners failed to recognise the interdependence of one trade on another, they also failed to see the negative effects that came from the financial crises and the near-collapse of the euro.

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Today we see the major economies of Europe face years of uncertainty as the US struggles to deal with its massive debts, which will have a strong negative effect on China.

The falling dominoes will continue to have an impact, declining US consumption of gasoline reducing imports of crude oil from outside North America, with serious implications for the tanker industry.

There is little hope that things will turn round in the near future. There is plenty of uncertainty that may well make things worse. Breakdowns and accidents are likely as shipping companies cut their costs to the bone to survive.

Shipping needs fewer shipowners in all sectors, larger well-capitalised companies focusing on long-term contracts with end-users for moving cargoes. Such consolidation is needed across all segments, from large tankers and dry bulk carriers to smaller ships of all types.

Single-industry focus or "pure play" has proved to be a figment of Wall St's imagination showing that the future lies with the large multi-trade shipping companies that dominated in the past.

China and its policies towards shipping are a constant concern. There appears to be no single plan; individual initiatives reflect support for shipbuilding on the one hand and support for cheaper shipping on the other. But China is itself a domino — a large one — whose fortunes depend on the ability of many other nations to supply its raw materials and buy its manufactured goods.

Shipping has lost its political muscle by moving most of its assets offshore. It needs to consider returning to centres of world trade such as the US and Europe to consolidate and deal with the threats that China poses.

Having a large fleet of ships is another domino. And bringing many big dominoes together can be an effective strategy. Now is a good time to make the move towards large multinational and multi-type shipping companies. ■