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SectorVector

August 2022

Reading the topical trends

Course correction ahead

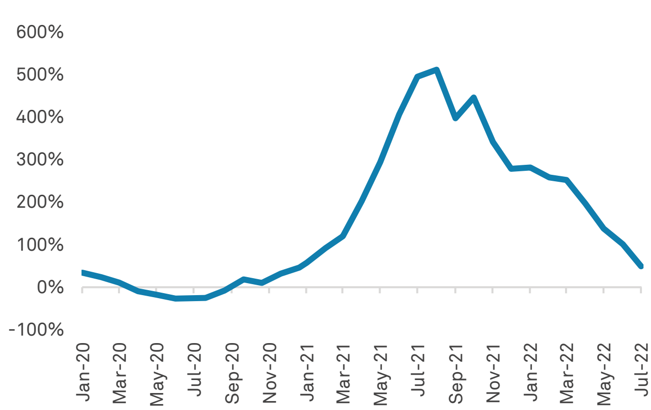
As container charter rates start to sink, shipping margins set to shrink

Container shipping charter rates are set for a course correction after touching historical highs in 2021 and staying elevated so far this year.

Charter rates were up 156% on-year for the first seven months of this year. Over the remaining months, however, the rates are expected to decline, though still ending the year 40-70% higher.

A widely anticipated recessionary environment is expected to weigh on demand in key consumption countries in the West towards the end of the year. A pick-up in the pace of container production post the Chinese New Year and the Winter Olympics has tamped rates, too.

Container charter rates on downward trajectory after peaking in August 2021



Note: Container charter rate growth is on on-year basis
Source: CRISIL Research

CRISIL Research expects charter rates to slide a further 30-50% in 2023 on account of the expected recessionary environment in majority of the consumption economies and consequent fall in demand for discretionary goods.

To be sure, a large part of the demand pick-up in 2021 — and thereby the runup in charter rates — had also stemmed from a rise in demand for discretionary goods in major consumer countries in the West, which is seen reversing now.

The other reasons included:

- **Lack of enough containers:** The turnaround time for containers at ports increased substantially because of local restrictions and subsequent labour shortage and local supply chain disruptions in China, the EU, and the US. Containers are stacked at ports and inland depots for extended durations, thereby affecting availability of empty containers

- **Consecutive festive seasons:** The subsiding of Covid-19 infection rates in the second half of 2020 coincided with the pick-up in demand in the West owing to the Christmas holiday season and then in the East on account of the Chinese New Year. This increased demand for container shipping without the corresponding increase in fleet availability, which were stuck at ports for a longer duration

- **Rising personal consumption expenditure:** As was the case during the Global Financial Crisis in 2008, personal consumption expenditure in the US declined in 2020 as well following the outbreak of Covid-19, which affected container traffic. However, container traffic rose in the subsequent year, and is expected to sustain in 2022 to some extent

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Improvement in personal consumption expenditure in the US supported high charter rates post 2020

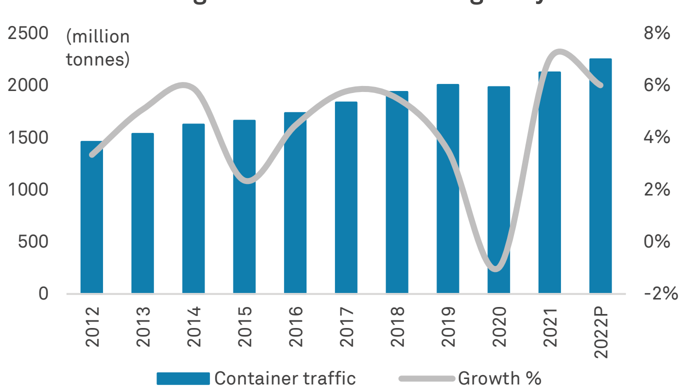
Source: US Bureau of Economic Analysis, CRISIL Research

- **Curtailing of container fleet due to the pandemic:** Many shipowners decided to retire or stop sailing some of their fleet due to underutilisation in the aftermath of Covid-19. This translated into higher charter rates in the second half of fiscal 2021 as fleet supply was lower vis-à-vis the sudden surge in demand caused by the pickup in the festive seasons. And while shipowners began deploying fleet with the uptick in demand, it was highly disproportionate to the increase in demand, and thereby widened the demand-supply gap

- **Slower production of new containers:** Container production in China slowed as companies in the country shifted production to infrastructure activities because of the government's stimulus towards infrastructure

Given all these, while trade has sustained so far, the growth rate in 2022 is expected to be lower on-year due to inflationary pressures crimping demand for discretionary goods in the second half.

Container trade growth rate to slow marginally in 2022

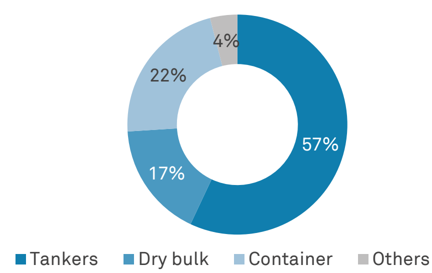


P: Projected
Source: United Nations Conference on Trade and Development, CRISIL Research

Margins of Indian shipping companies to contract this fiscal

The Indian shipping industry largely comprises tanker vessels, which account for ~57% of the overall fleet pie. While the container segment is the next largest, it accounts for a distant 22% share. Hence, the Indian shipping players profitability is largely swayed by the tanker segment.

Tankers form a lion's share of Indian shipping fleet

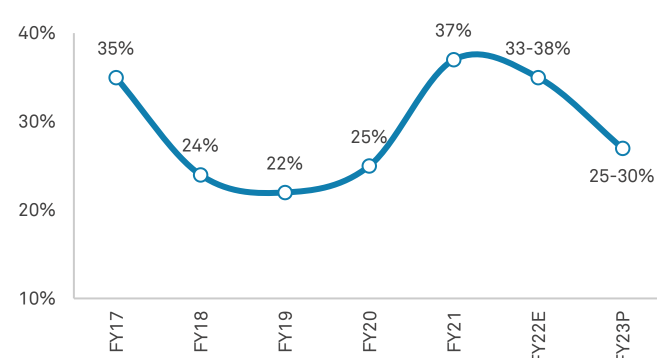


Note: Split of vessels by category is as of March 2022
Source: DG Shipping, CRISIL Research

However, the industry's high margins in fiscals 2021 and 2022 were because of historically high charter rates in the container and dry bulk segments, though charter rates in the tanker segment declining slightly in fiscal 2022.

The outsized impact of the lower share container segment will percolate into fiscal 2023 as well, with limited ship movement on account of likely decline in trade leading to a slight contraction in overall industry margins. That said, the margins will still be higher than the pre-pandemic level owing to favourable dynamics, which have lowered the variable expenses of shippers.

Operating margin of industry to decline in fiscal 2023



E: Estimated; P: Projected
Note: Aggregate results of standalone numbers for GE Shipping, Shipping Corporation of India, and Shreyas Shipping and Logistics
Source: Company reports, CRISIL Research

The correction in charter rates across segments is also expected to affect player revenues to some extent.

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