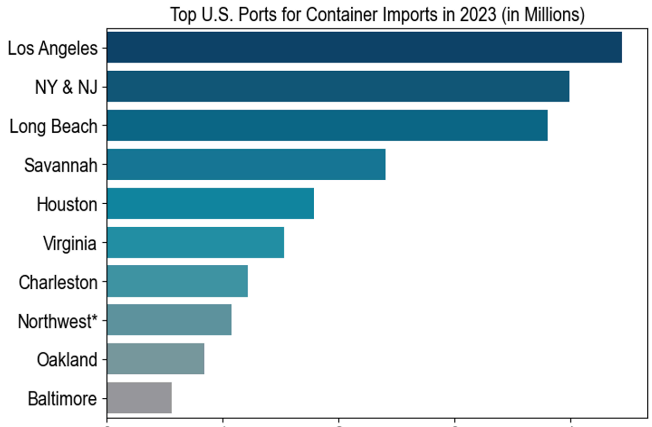
April 22, 2024

Special Edition Economic Insight: A Closer Look: Disruptions and Costs of Shipping

Economic INSIGHT

BALTIMORE BRIDGE COLLAPSE

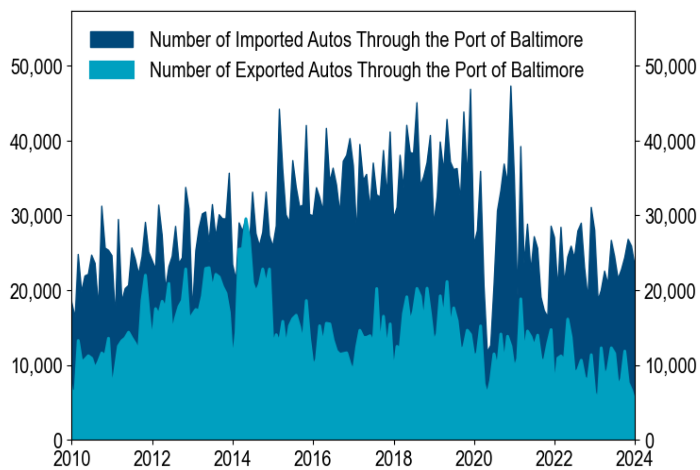
Supply chains are back in focus after Dali, a massive 95,000-ton container ship, collided with the 1.6-mile Francis Scott Key Bridge in Baltimore on March 26. The incident resulted in the tragic loss of six lives and the indefinite suspension of commercial shipping traffic through the Baltimore port. The bridge crosses the only water route in and out of the harbor where the port is located. Additionally, the 3,600 commercial trucks that crossed the bridge each day prior to the collapse have also been disrupted. As maritime officials continue to search for answers as to the cause of the accident, market analysts are working to quantify the extent of the economic fallout.



*Northwest Seaports includes ports in Seattle and Tacoma, Washington
Source: Pacific Merchant Shipping Association/ WSJ

TOPLINE STRENGTH OVERSTATED?

Baltimore is the ninth largest U.S. port by trade volume. It handles the nation's largest volume of automobiles, as well as goods such as sugar, coal, gypsum, and lumber. Last year, a record 52.3 million tons traveled through the port with total trade amounting to $80.8 billion, or about 1.6% of total U.S. goods trade volume. According to reports, every one-day closure of the Baltimore port results in an estimated loss of $217 million and impacts more than 15,000 direct jobs and 139,000 indirect jobs.



Source: Maryland Department of Transportation Port Administration/Bloomberg

According to the U.S. Army Corps of Engineers, a limited access channel 280 feet wide and 35 feet deep is expected to reopen in the coming weeks (by the end of April). This would allow one-way traffic in and out of the port for barge container service and some roll on/roll off vessels that transport automobiles and farm equipment. A reopening of the entire 700-foot-wide by 50-foot-deep channel is not expected until the end of May,

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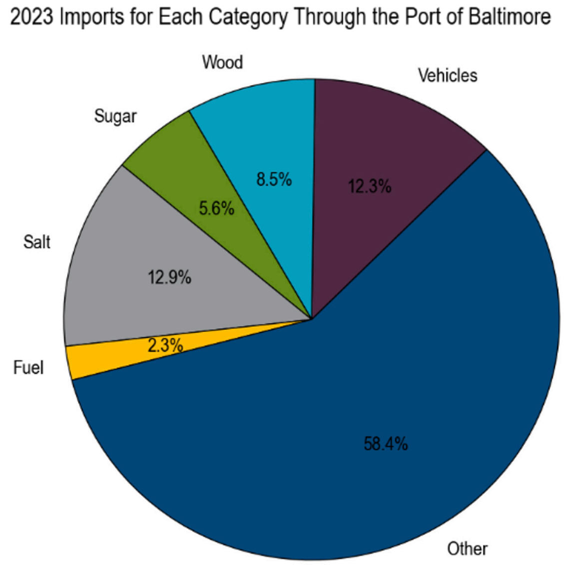
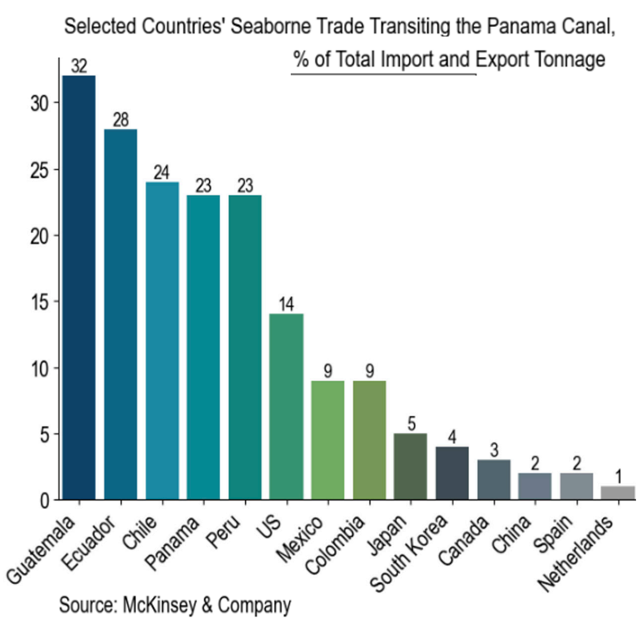
delaying a restoration of port access to normal capacity by at least nine weeks.[1] In the meantime, a temporary channel has been opened for smaller vessels. Larger ships are being rerouted to nearby ports including the Port of Philadelphia and the Port of Virginia, as well as larger operators on the East Coast, such as the Port of New York and New Jersey.



The Francis Scott Key Bridge, which spans the mouth of the Port of Baltimore, is also no longer an option for commuter traffic or ommercial truckers. The bridge is a key transportation link between Baltimore, Washington D.C., Philadelphia and New York, and is an important corridor for cars, trucks, and oversized vehicles that are not permitted to take more direct routes such as through the Baltimore Harbor Tunnel and Fort McHenry Tunnel. For example, any vehicle over 13 feet 6 inches, or wider than 8 feet, along with all double trailers are prohibited from crossing in and out of the Baltimore Harbor Tunnel. Additionally, materials such as propane or butane, along with radioactive and hazardous materials are also prohibited from using the Baltimore Harbor Tunnel or Fort McHenry Tunnel. Without access to the bridge, many drivers will now have to drive an additional 30 miles around the Baltimore Beltway (695), adding to delivery times and costs.

GLOBAL SHIPPING DISRUPTIONS

The Baltimore bridge catastrophe comes on the heels of other disruptions to major shipping routes, including the Panama Canal and Egypt's Suez Canal. An extreme drought in Panama, for example, has led to the lowest water levels in more than 100 years. As a result of decreased water flows, authorities have limited the number of shipping vessels allowed to pass through the canal each day to 18 as of February, down from 36.



The Panama Canal links the Pacific and Atlantic Oceans and as such, acts as a major corridor for trade between Asia and the U.S. East and Gulf Coasts. An estimated 2.5% of global sea trade travels through the Panama Canal on an annual basis, with 14% of U.S. seaborne trade moving in and out of the waterway. Due to extended delays and traffic

[1] Link to source: https://www.usace.army.mil/Media/News-Releases/News-Release-Article-View/Article/3731723/us-army-corps-of-engineers-develops-tentative-timeline-to-reopen-fort-mchenry-c/

GLOSSARY

FEU – Forty-Foot Equivalent Unit

IEA – International Energy Agency

MoM – Month over Month

NBER – National Bureau of Economic Research

PCE – Personal Consumption Expenditures

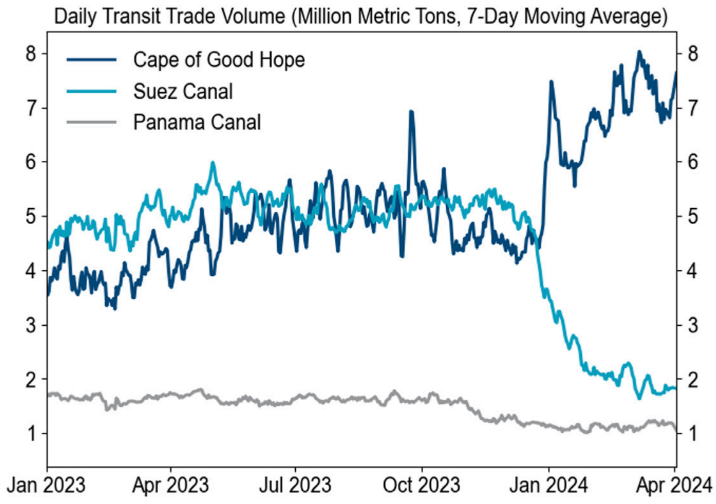
WSJ – Wall Street Journal

WTI – West Texas Intermediate

YoY – Year over Year

disruption, some vessels have been rerouted, although not without substantial costs and danger. According to McKinsey & Company data, alternative routes (away from the Panama Canal) could increase costs by 5% or an estimated $1.1 billion a year, while those routed through Egypt's Suez Canal risk ongoing exposure to attacks by Houthi militants in the Red Sea, despite retaliatory measures by the U.S. and Britain.

Together, the Red Sea and Suez Canal provide the fastest and shortest route between Egypt and Asia. In 2023, 12% of global trade travelled through the Suez Canal alone. Following the recent attacks, however, some ship operators have indefinitely suspended voyages, while other vessels have been rerouted around South Africa's Cape of Good Hope, raising both travel time and costs. According to market reports, the alternative route can add up to two weeks, 3,000 to 6,000 nautical miles, and nearly a million dollars to each voyage![2]

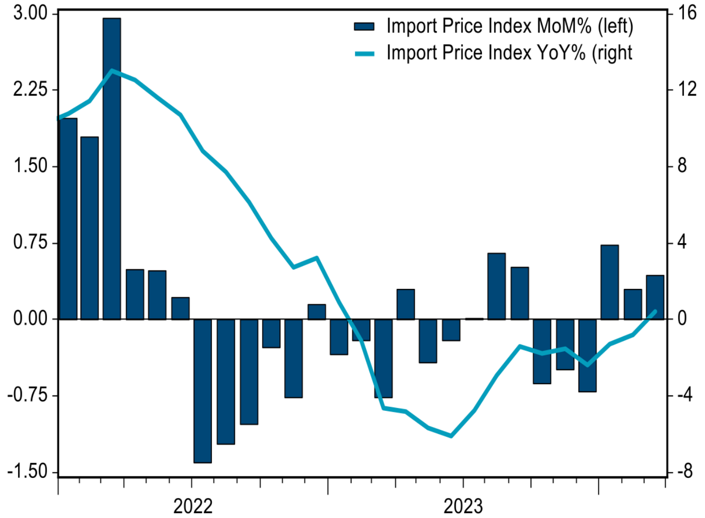


Source: IMF PortWatch

INFLATIONARY IMPLICATIONS

According to the National Bureau of Economic Research , containerized seaborne trade accounts for 46% of international trade. With container ships operating on a very specific fixed itinerary, even the smallest congestion can lead to substantial delays and increased costs. Thus, the rerouting of cargo ships is already causing inflationary ripples through the global – and domestic – economy at a time when consumers and policy makers alike are desperate to reinstate price stability.

According to data from Freightos, shipping costs have already climbed more than 150% from $1,048 Forty-Foot Equivalent Unit (FEU) to $2,720 FEU due to disruptions in the Red Sea. If sustained, these costs will expectedly result in a further backup in import prices and filter through to final consumer goods.



Source: Bureau of Labor Statistics/Haver Analytic

[2] Link to source: https://interactive.aljazeera.com/aje/2024/mapping-red-sea-shipping-attacks/

Last week, import prices rose 0.4% in March, the third consecutive month of increase. Furthermore, over the past 12 months, import prices increased 0.4%, the first annual gain since January 2023.

Last month's rise was largely concentrated in rising energy prices, with a 4.7% gain in fuel costs and a 6% gain in petroleum prices. In fact, with disruptions to the Suez Canal alone resulting in near-record volumes of oil in transit as well as higher fuel demand stemming from alternative shipping routes, global supply disruptions have led to a near 20% rise in WTI since the start of the year.[3]

Excluding petroleum, import prices were flat (0.0%) at the end of the first quarter and declined 0.2% over the past 12 months, suggesting that outside of energy, the impact of higher shipping costs has been relatively muted to date. That being said, goods prices are already gaining momentum. While down from earlier peak levels, since July, annual goods inflation has been uneven at best. Services inflation, on the other hand, has maintained a downward trend since peaking in February 2023.

While the causes of the disturbances to major trade routes range from force majeure to drought to geopolitics, the interconnectedness of global supply chains is increasingly evident and fragile. A prolonged disruption to any one – or portion – of the world's major shipping corridors will continue to exacerbate inflationary pressures, potentially undermining the progress already made in terms of slowing the pace of – producer – prices.

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[3] "At nearly 1.9 billion barrels as of end-February, oil on water hit its second highest level since the height of the Covid-19 pandemic," according to IEA's "Oil Market Report – March 2024." The IEA also upped its forecast for global oil demand due to the rising fuel needs of rerouted ships, increasing its forecast by 110,000 barrels per day to 1.3 million barrels per day.

Link to Report: https://www.iea.org/reports/oil-market-report-march-2024

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