Shipping - Asia-Pacific

Red Sea disruptions: How to think about possible earnings scenarios?

Industry Overview

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Red Sea disruptions & possible earnings scenarios

The Red Sea situation is fast evolving, and we are bracing for disruptions to persist for at least a few weeks until Operation Prosperity Guardian can stabilize the security situation. In this note we present earnings scenarios to our base case forecasts depending on average freight rates and the duration of disruptions. The scenarios show incremental earnings of up to 10-20% of market cap for Asia Pacific shipping companies on a two-month disruption on a CCFI range between 1,000-2,000.

Upside risk to freight rates on Red Sea disruptions

Red Sea disruptions should provide some near-term support for container spot rates. The longer sailing time around the Cape of Good Hope adds +9% to global tonne mile demand, while we estimate unit costs on the Asia-Europe route have increased by +10-15% with longer distance sailings (higher fuel & vessel) somewhat offset by lower canal charges. So disruptions should put upward pressure on the CCFI although freight rates are unlikely to hit CCFI COVID peaks of 3,000-4,000 with more slack now in the system from new vessel deliveries. At this stage, we test scenarios of the CCFI moving up to the range of 1,000-2000 (versus an average of 869 right now).

Duration of disruption depends on easing security risks

Our expert call with US Admiral Foggo suggests that a solution to the Houthi problem might take time with Operational Prosperity Guardian only just announced, the dynamic nature of the enemy, and a lack of political consensus around attacks in Yemen (for more see: Red Sea Call Takeaway: Adm. Foggo sees near-term challenges in restoring fluidity, 19 December 2023). We consider scenarios of Red Sea diversions continuing between 1-4 months with liners awaiting greater stability before returning to the Red Sea.

Profit scenarios depending on freight rates & duration

Our scenarios inside shows a disruption lasting two months could add incremental earnings of up to 10-20% of market cap across our Asia Pacific container liner universe depending on the extent of the rate increase. Our workings are based on the CCFI in the range of 1,000-2,000 and a reduction in volumes to factor the longer distance sailings.

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Earnings scenarios

Below presents incremental earnings for container liner names based on the duration of disruption and where average freight rates get to:

Exhibit 1: COSCO Shipping incremental EPS (HK$/share) based on CCFI average and months of disruption
Incremental boost to COSCO Shipping EPS based on CCFI average and months of disruptions

		Months of disruption			
		1	2	3	4
CCFI average	1,000	0.10	0.20	0.30	0.40
	1,250	0.30	0.60	0.89	1.19
	1,500	0.50	0.99	1.49	1.99
	1,750	0.70	1.39	2.09	2.78
	2,000	0.90	1.79	2.69	3.58

Source: BofA Global Research estimates

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Exhibit 2: ONE net income (US$mn) based on CCFI average and months of disruption
Incremental boost to ONE net income based on CCFI average and months of disruption

		Months of disruption			
		1	2	3	4
CCFI average	1,000	150	300	450	599
	1,250	452	904	1,356	1,808
	1,500	754	1,508	2,263	3,017
	1,750	1,056	2,113	3,169	4,225
	2,000	1,359	2,717	4,076	5,434

Source: BofA Global Research estimates

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Exhibit 3: NYK EPS (JPY/share) based on CCFI average and months of disruption
Incremental boost to NYK EPS based on CCFI average and months of disruption

		Months of disruption			
		1	2	3	4
CCFI average	1,000	19	38	56	75
	1,250	57	113	170	226
	1,500	94	189	283	377
	1,750	132	264	397	529
	2,000	170	340	510	680

Source: BofA Global Research estimates

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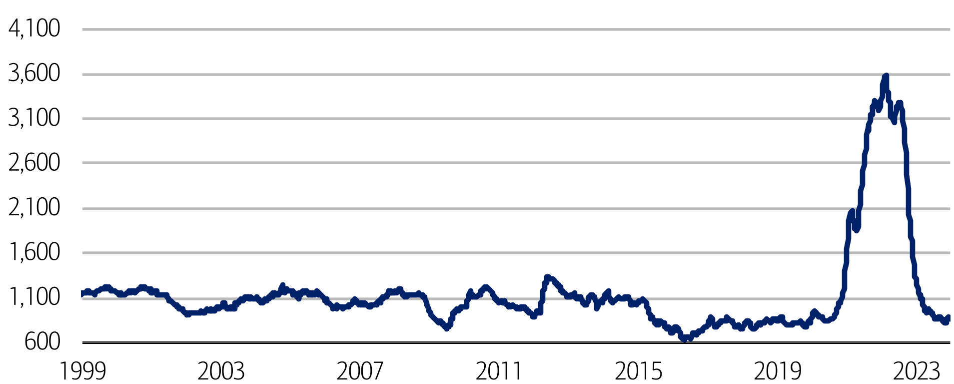
Exhibit 4: China Containerized Freight Index, 1999-2023
CCFI currently at 869



Source: Shanghai Shipping Exchange

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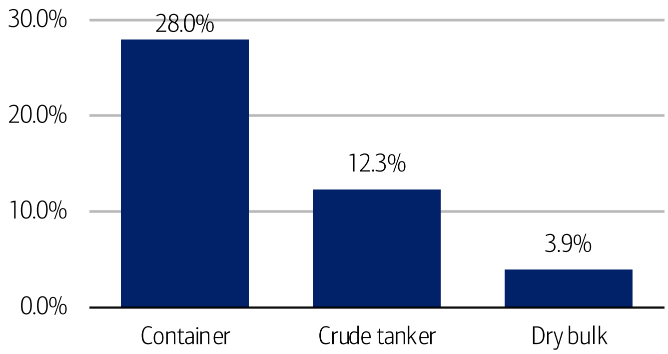
Risks around the Red Sea & Suez

Below we show some estimates of the potential demand boost from longer distance sailings should all sailings be diverted away from the Red Sea and Suez to the Cape of Good Hope. Container is most highly exposed to disruption from closure of the Suez Canal and the Red Sea with a demand boost of up to 9pct. We note that around 28% of the world container trade uses the Suez/ Red Sea (mainly Asia to Europe but also Asia to US East Coast and Middle East or India to Europe and USA). Alternate routing via the Cape of Good Hope would add an average of 30% to journey times for container.

Exhibit 5: Shipping volumes using Suez/Red Sea by segment

Container shipping is most exposed to disruption to Suez/Red Sea



Source: Clarksons, BofA Global Research estimates

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Exhibit 18: Boost to demand from Suez Canal & Red Sea closure

Container could see largest demand boost from sailings shifting from Suez

	% of volumes	Increase in distance	Demand boost
Container	28.0%	30%	8.52%
Crude tanker	12.3%	30%	3.68%
Dry bulk	3.9%	30%	1.16%

Source: Clarksons, BofA Global Research estimates

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