

Global Watch

A Sea of Red

Red Sea – no regional war but no traffic either

Red Sea Developments have been playing out in line with our view of ongoing acute disruptions to shipping costs and supply chains that could persist for some time (see the report [Global rate cuts lost at \(Red\) Sea?](#)). Houthi disruption of maritime traffic has not stopped despite US and UK strikes. US pronouncements have highlighted that the strikes have not yet materially eroded Houthi offensive capabilities. US/UK warnings have led to more announcements of traffic being rerouted away from the Suez Canal. Despite volumes being down 30-40% year-to-date, the Suez Canal Authority pushed through a scheduled 15% increase in transit fees to recoup some hard currency.

Conference call: conflict likely confined to Red Sea area

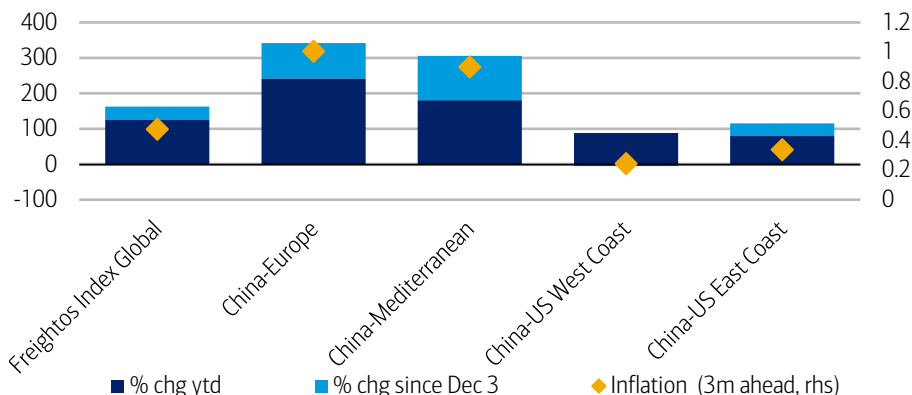
The key takeaway of our latest conference call is that our expert speaker sees a risk of continued tit-for-tat between US/UK forces and Houthis in the near-term. His base case is for tensions to remain confined around the Red Sea area. He suggests that lower Iranian logistical support to Houthis (through the withdrawal of a spy ship) may mean less sophisticated Houthi attacks, and that a redeployment of the spy ship could then be an escalatory gesture. The Houthi announcement that they would not target Saudi or UAE reduces the risk of a regional escalation, in our view.

Shipping costs continue to rise, posing inflationary risks

Since December, shipping costs have increased by up to 300% on routes from Asia to Europe. Based on recent literature, the observed doubling in freight costs in US-bound routes could lead to a relatively modest inflation pickup of about 0.3% over a quarter. However, the much larger increase in shipping costs on Europe-bound routes could drive an uptick in European inflation of closer to 1% over a quarter if disruptions were to persist. We continue to believe Inflation pressures should be more muted in Asia.

Exhibit 1: Increase in shipping costs and potential inflationary impact (%)

Shipping costs have soared in the past month, which could lead to renewed inflationary pressures



Source: BofA Global Research, Bloomberg, Carrière-Swallow et al. (2023)

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