DIVERSIFICATION POTENTIAL

The maritime industry is accused of being slow to change and not entrepreneurial enough. **JP Verschuure** feels that COVID-19 may change this situation

■ **COVID-19 has exposed the vulnerability of global supply chains – nearshoring is one alternative but diversification has to be seriously considered**

Even the most pessimistic scenarios agree that the COVID-19 pandemic will be over quicker than the time it takes to develop a port facility. Given that most investments in the port industry last for 30 years, coronavirus should be placed in a long-term perspective. However, re-start of economies and changes in industry will occur at an extreme pace and ports need to be ready to respond to these rapid changes. The question is, however, how much will actually change?

NEARSHORING? POSSIBLY - BUT HOW NEAR AND FOR HOW LONG?

The COVID-19 pandemic has underlined the vulnerability of global supply chains. However, the largest problem has really been that production in China stopped while demand in Europe was still up, and now when production is resuming in the Far East, weak demand is occurring in Europe and the Americas.

Clearly, the pandemic occurring out of sync across various continents has been more problematic than the actual impact of the virus on shipping of goods over long distances. Manning a ship only requires relatively few staff who have limited contact outside the other crew members. The only disruptions actually reported in the industry have been difficulties with crew changes happening. However, with clear protocols and increased testing of crews, shipping should continue almost as normal.

Few ports have actually reported full operational shutdowns during the "Great Lockdown" due to the tremendous commitment showed by the stevedores and port staff to keep the waterfront port of logistics chains running normally. In fact, the reverse might be true because trucking of goods has been more impacted than shipping with borders closed and long delays/congestion at ports. Nearshoring will struggle with these challenges.

Adopting digital applications to make supply chains more efficient and transparent, plus use of automated terminals, means operations can proceed normally during pandemic disruptions. In general, supply chain issues were not caused by them being global.

Even within Europe great differences are occurring in how the pandemic spreads, just moving production nearer may not solve the problem of production/consumption being disrupted at different moments. Also, it is not feasible to nearshore all supply chains to within trucking distance for all customers. The great variety of products and combinations of complex half products and raw materials will result in supply chains still spanning across countries even continents. So how near would nearshoring feasibly be?

The second question is how long this nearshoring trend will be advantageous. When the impact of the pandemic fades, the differential in the costs of the goods produced in global or local supply chains will still be there. This cost differential will have to be traded off against potential disruptions in supply chains from a resurgence of the current pandemic or a new pandemic. Producers with a cost advantage may have gained market share. A low growth environment in which each percentage point of margin may make the difference between business survival or not, saving money by adopting global supply chains may actually be even more attractive.

DIVERSIFICATION RATHER THAN NEARSHORING

An alternative to nearshoring, diversification of supply chains may offer a much better solution. Using other relatively cost competitive production locations, the exposure to local outbreaks may be sufficiently hedged. This could drive a further acceleration of shifting production from China to other Asian countries or alternatively to Africa, Central and Latin America.

This process was already ongoing by the dispute between China and the US, while the labour cost differential between China and other labour cost competitive countries such as Vietnam, Indonesia and India was diminishing before the outbreak and driving an economic reason for diversification.

These three factors will result in more fragmented trade flows across the world. Additional port facilities would be needed in new emerging markets and port facilities near current production clusters may face lower utilisation rates. As the shipping lines have invested heavily in very large container vessels for the current main trade route between the Far East and Europe (with port facilities upgraded to facilitate them), the cascading of vessels to secondary trades may pick up even more pace. This in turn will cause pressure on the port infrastructure in these emerging markets to upscale.

NEARSHORING RAW MATERIALS?

COVID-19 shows that for strategic and essential goods global supply chains are very fragile. Medication, hospital equipment and PPE were confiscated at borders in some cases and prevented to be shipped internationally. Goods where supply chain reliability are more important than costs savings offered by global supply chains are likely to be produced more locally.

New production methods, like 3D printing, make localised production more feasible. These local production facilities still require raw materials or half products to be shipped in, at the expense of less trade in finished goods. The trend in nearshoring will likely better suit more fragmented trade routes.

SHORT SEA TERMINALS BACK ON THE MAP

Supply chains will remain continental supply chains, rather than national ones due to requirements of specialisation and economies of scale. Reaching the end customer by trucking is expensive and generates road traffic. Many governments are trying to reduce use of road from a sustainability point of view. This could see greater use of short sea shipping. If oil prices stay low for longer, deploying small vessels and sailing shorter routes becomes more profitable as well. Ports close to either production clusters or population centres and with efficient rail yards will benefit, with interest in inland terminals and river facilities seeing increased popularity - strategies which international terminal operators are embarking on already.

STIMULUS PACKAGES FOR GREEN INITIATIVES AND MORE....

Huge stimulus packages have been announced to mitigate the initial fallout of the Great Lockdown trying to kickstart economies. Governments in Europe are keen to increase their power in the private sector on the back of the financial injections into the economy, with governments looking at port initiatives to help kickstart economic activity again while trying the make ports greener. Subsidies for more shore power initiatives, replacing diesel generated equipment with electrified ones and stimulus of intermodal transport are the most obvious candidates if it is up to the public sector. For the private sector spending most attention on keeping up with the fast changing market situation sustainability may not be top of their agendas, despite good intentions. It will help economies if governments can front load refurbishment programmes for facilities developed during the maritime boom of the 1980s and 1990s now that traffic is lower. Whether this trend will spread to emerging markets in the short term is questionable, but with the experience gained in Europe, this may trickle to other regions in a post COVID-19 world.

"NEW" WORLD OF INFLATION

A side effect of the tremendous stimulus packages is that inflation will likely come back with a vengeance in time. After a brief time of deflationary pressures, the macroeconomic conditions of stagflation as witnessed in the 1930s are increasingly likely to repeat themselves.

■ **Greater use of short-sea shipping could emerge in the post COVID-19 world**

For terminals, this means making sure tariffs are carefully linked to inflation being updated as frequently as possible. However, these new conditions may also offer an opportunity to actually increase the revenues. Dynamic pricing and other innovative pricing models in combination with further digitisation of processes, could lead to better aligning interests of shipping lines and terminals. At the same time dynamic pricing can ensure that tariffs are adjusted to volatile conditions.

The ability of port terminals to adapt to inflation, also results in investors retaining an interest in port terminals. In current volatile times, port assets are considered a safer option in comparison to other industries. They will be looking for any distressed shipping line terminal assets being offloaded to raise cash. However, with uncertain short-term economic outlooks it will require investors and governments to look beyond the timespan of COVID-19 to see upside potential when the maritime world has adapted to the new post COVID-19 reality.

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