Santosh Patil tries to fathom how carriers managed to get into such an oversupplied situation.

Having been a part of and watching developments in the container shipping industry with interest over the last two decades or so, I never seemed to have come to terms with how the container shipping industry has got itself into this oversupply situation.

In my early shipping days at the beginning of the century, I was always curious to understand the calculations behind the demand projections and the projected need to supply tonnage commensurate to the demand.

During my interactions with the shipping lines in my feeder days, I often used to come across top lines announcing at seminar after seminar – the need to go for bigger tonnage in the pursuit to achieve lower costs per teu which was only possible through the acquisition of larger container vessels. Most in the audience (yours truly included) nodded
heads in agreement, often because it came from the ‘big lines’ and the big lines ‘knew things’.

However, as days passed I came to realise there was a limit to what one could achieve by just deploying bigger tonnage and often wondered where will this stop – 25000, 30,000 or even 50000 teu?

Post-2008, I often asked executives of the top lines on how this ordering spree would pan out given the suppressed demand scenario. The almost condescending response always was that the lines ‘knew’ what they were doing. Some executives at the biggest lines would even snob around saying their management could never go wrong in their calculations. This ‘blind’ faith left me perplexed in how could I ‘not’ see what they could? Perhaps I was way too low down on the pecking order to understand the ‘strategies’ and unable to comprehend the complexities of the global scenario.

However, as a student of economics, I believe it was a simple case of supply and demand, and supply, as it was being pumped in or under construction, was clearly well beyond the projected demand. Add in the fact that there were a good number of vessels laid up and that the excess tonnage simply couldn’t be wiped out in a jiffy. This is further complicated by new regulations on ship recycling, which do not really help the overall scenario.

One of the common explanations dished out for the tonnage addition was to gain market share and creating capacity which would render small lines incapable of putting up a fight, ultimately leading to several M&As – which I admit has turned out largely true. Shipping today is a largely oligopolistic market with few shipping lines controlling significant market share. However, you can fight for market share all you want, but in an asset heavy industry with asset lifespans of 25-30 years, creation of large capacity has its downsides as you cannot just prune your assets to correct supply demand imbalances.

The underlying assumption in this capacity creation was that once the marketshares were reached and dominant positions established, lines will be able to raise freight rates where profits could be derived making the owners and shareholders happy. Unfortunately, this scenario is yet to be seen. A decade since the market crash we are still in a situation where lines are struggling even those who are amongst the largest.

Now this excess capacity has come to bite the lines who created it in the first place. The situation has been worsened by state support to create capacity for some lines, throwing a spanner in the other lines’ works. Impending changes expected in trade patterns with possible trade wars et al adds to the uncertainty over how the situation will emerge.

So, has the gamble paid off? I am not quite sure. Perhaps the lines have been successful in reducing competition in some measure and reported profits in a few quarters, however in the process there are long term structural issues which will have a significant impact on the industry.