



So you want to be an Intra-Asia Trade player?

Niels K Balling, 12 March 2010

Container veteran Niels K Balling contributed this think piece on Intra-Asia containers. We leave his title in place as it reminds us of the song by the Byrds, and later sung by Patti Smith (So You Wanna Be a Rock and Roll Star). Mr Balling notes, in passing, that the intra-Asia market is so big and complex that trying to boil it down in this fashion perhaps does not do it justice, so he apologizes in advance...

The Southeast Asia/North Asia countries comprising the core Intra-Asia market have become the largest container trade in the world, by far (despite some over-counting a few years back in a now infamous looking at the market by a well-known report we refer to sometimes). We exclude the Asia/Australia and Asia/India and Middle East trades as they are independent trades served by independent assets.

Key issues:

- Total REAL profit pool of the core Intra-Asia trade is destined to remain miniscule
- Only niche operators will be able to cover the cost of dedicated capital deployed to this theatre
- Roughly 1/3rd of the trade volume is handled by main line operators on trunk routes
- Rest evenly split between dedicated major services, feeder services, niche operations and domestic protected trades

The Main Line Operators (MLOs) provide negative marginal pricing to offset equipment positioning needs they have anyhow, and to build container terminal volumes that generates lower total terminal handling cost. In other words sunk cost discounted to zero (or less), combined with marginal pricing for growth purposes to achieve lower variable cost. That's not entirely crazy as the volume gain often will generate more value through terminal handling discounts than the real Yield of Intra-Asia cargo. And the discount may apply to the TOTAL volume thus leveraging the discounted Intra-Asia business to great effect.

Any dedicated operator (as some of the traditional Intra-Asia shipping companies will tell you) can never recover the cost of normal operations against such network economics.

Next come feeder (about 15% of Intra-Asia volumes) and the quasi feeder operations. The latter comprises about 55% of dedicated Intra-Asia services. These are services deployed for combined Intra-Asia trade and MLO network purposes. The feeder and quasi feeder operations work on the same discounted cost basis.

The only reason for existence of 3rd party feeder operators is that they can do it cheaper than the main line operators despite the latter counting on their own sunk cost. How can the 3rd party operators survive? In most cases it comes down to lower asset and capital costs - for as long as it lasts.

In other words on a net, net basis a relatively large part of the major Intra-Asia trades are served based on dedicated shipping services to their operational scope without any hope of rate or cost differentiation

against the main line operators' network economics. They cannot bring specific financial value to the table that can support a dedicated operation. And they die – and get reborn – regularly.

Overall Intra-Asia has a negative profit pool due to the sunk cost approach by main line operators. That's a great trade facilitator and may continue to support rapid volume expansion of Intra-Asia container volumes.

But where's the money for the shipping investors?

There's a lot of money available in this profit pool. If one knows where to look. There are several niche opportunities as well as classic arbitrage windows available.

The niches are fairly obvious, especially within the Refrigerated foodstuff area. This is becoming an interesting niche because of slow steaming by main line operators. Certain products, like bananas, are highly transit-time sensitive and need fast, reliable transport. The arbitrage opportunities are however an even more interesting and growth opportunity generating.

The Intra-Asia trade to a large extent is an outgrowth of the coastal economic development within Asia. Part of the success of Asia is that logistics costs were always low. This is no more a given. Redistribution within Asia is becoming more costly, though sea represents the cheaper option and contributes to reducing costs. Just think of haulage cost in Japan to outlier areas. Or Taiwan, Korea cost for trucking to other consumer areas. And/But...China is now joining the game.

The Intra-Asia trade regionally is essentially similar to domestic haulage in the US and Europe. There are no major green issues yet except Japan, where basic economics already make it very compelling to distribute to say Southern Japan via China by ship rather than paying huge costs over road and ferry via Tokyo or Kobe. In other words, use shipping to avoid domestic land based transport.

Intra-Asia will continue to provide growing opportunities for transport arbitrage opportunities, for new entrants. And Intra-Asia transport costs will continue to remain low based on intelligent MLOs going beyond normal yield management to leverage their network for ever better marginal cost throughout their global operations.

For both types of operators Intra-Asia will continue to expand in value.

For new entrants the advice is that deep understanding of their market of choice will make the difference between survival and quick demise.