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Reefer market reverts to type

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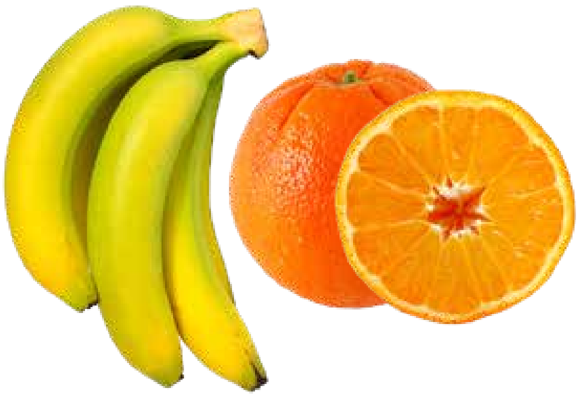
After an extraordinary two years of unprecedentedly high reefer rates and record returns to vessel operators and owners, the market for the specialised mode has settled effortlessly back into its pre-pandemic peak-and-trough routine.

d'après photo © Seatrade

Given that for the 24-month duration of the global Covid pandemic, the strength of the reefer market was determined principally by the availability of dry vans and the reliability of carrier services, it should come as no surprise that timecharter (TCE) yields have declined steeply since the start of the year (see charts 1 and 2). This is because container port congestion has eased, container line services have normalised and more dry vans and reefer equipment are where they are needed.

However, while reefer rates have fallen, there is good reason to believe that the market will not weaken to pre-pandemic levels. Demand remains good: in absolute terms, the reefer mode will likely transport as much, and possibly more, reefer cargo in 2023 than it did in 2022 and 2021 – even if the dry goods and general cargo move back to the container lines. No reefer vessel has been demolished year-to-date and the fleet at the end of June was fully operational. However, in relative terms, the reefer will lose market share - this is because although the total seaborne reefer trade has risen, led by the rise in intra-Asian meat and fish cargoes, this increase is in trade lanes where the specialised mode does not operate!

In the first six months of the year, reefer business was good for reefer operators: although there were fewer specialised reefer voyages from New Zealand as a result of Cyclone Gabrielle damaging the pipfruit and kiwifruit crops, the mode loaded five times more Chilean cherries into China than in 2021/22 and more Chilean table grapes this season than last, despite a lower grape export crop. The Seatrade Rayo service loaded more bananas from Ecuador into the UK and northern Europe year-on-year. The Cool Carriers/Seatrade Reefer Alliance doubled the volume of South African citrus loaded into the Netherlands and the Baltic. After a successful pilot season, operator GreenSea retained the share of Brazilian melon exports it won from the carriers in 2022. Likewise, Seatrade retained its share of the Chilean citrus business into the east coast of the United States. Neither of these two contracts was won on price - both were awarded as a result of cargo and/or customers becoming frustrated with the service level offered by the carriers.



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Bananas and citruses, demand drivers

However, the most significant factor continuing to underpin demand for the specialised mode and therefore supporting rates, is the trade for bananas and citrus into Russia. For as long as Cool Carriers can continue to exploit the absence of competitive carrier services sailing into St. Petersburg (i.e. for as long as the special military operation is under way, or President Putin is in power), the entire reefer fleet will be well, if not fully, employed. Unlike the only other shipping line sailing into St. Petersburg MSC, which transships into feeder vessels, Cool Carriers offers fast, dedicated and direct services from Ecuador, Durban and Cape Town in South Africa and Campana in Argentina.

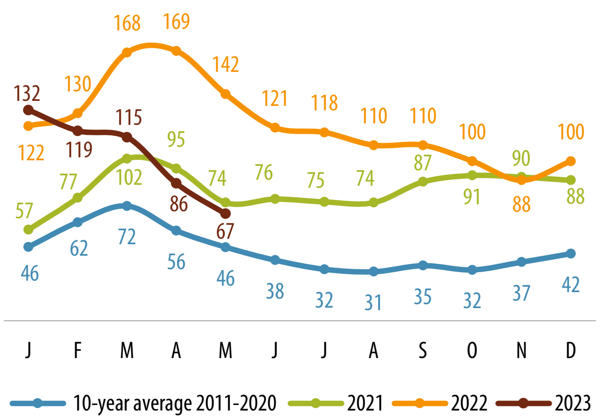
The demand from Russia, COAs and seasonal cargo has offset the reduction in banana volumes transported on the reefer. Indeed, the historically and commercially important reefer vessel/banana shipper symbiosis appears to have come to an end. With the reefer now commanding a miserly 15% share of Ecuadorian banana exports, according to industry association Acorbanec figures, and the banana multinationals switching to their own, or third party, carrier services, the reefer market is becoming ever less relevant to the banana business. The largest change has been in the trade of spot banana cargoes: for a number of largely commercial reasons, cargo and receiver appear no longer to need the reefer alternative. The number of spot banana cargoes fixed since the start of 2020 can be counted on the fingers of two hands. Likewise, the reefer can no longer afford to charter out to banana cargoes when there are better paying alternatives elsewhere!

Although the TCE yield may not be quite as spectacular for operators in 2023 as it was in 2021 and 2022, the reduction in top line revenue is partially offset by the 50% reduction in bunker costs year-on-year. But after a highly profitable 24 months, the medium-term future for the mode remains uncertain and contingent on the performance of the carriers. Given the high charter rates paid by the container lines to secure tonnage during the past 24 months, the container lines cannot afford a race to the bottom on rates for dry/general cargo. Despite a slowdown in the demand for dry goods and the tsunami of newbuilds still to be delivered, the argument is that rates will have to rise for business to be sustainable. Should it happen, the combination of a return to pre-Covid rates and higher costs will hit the carriers hard, no matter how large their current bank balances.

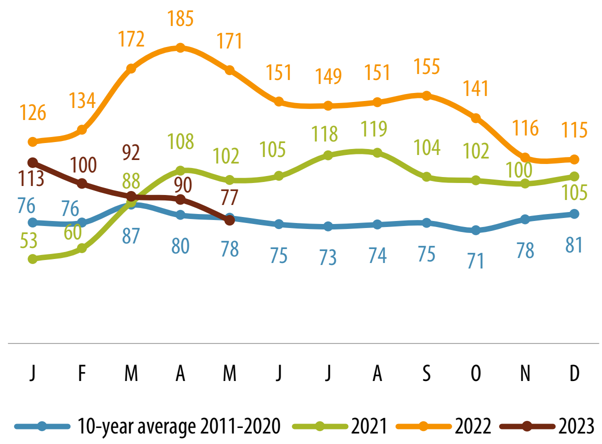
Under these circumstances, will the container lines treat reefer cargo differently to dry? Will the carriers price reefer as a contribution to voyage costs or will the rates charged reflect the higher costs the carriers have to bear? Two decades ago, container rates were priced at a discount to reefer rates. This is now reversed, so that reefer rates are priced at a premium to the rates set by the carriers. The logic therefore is that if the carriers enter a price war, reefer services will have no choice but to operate at unsustainable levels - unless cargo can be convinced of the inherent value that the reefer offers.

If the mode can tough out the rest of 2023, next year should be better for reefer operators largely because of greater cargo pressure: there will be more cargo and therefore demand will be stronger. There will be significantly more New Zealand kiwifruit and more South African citrus during the northern hemisphere summer months – and both will need reefers. On the supply side of the equation, there is a total of 39 units operated by Cool Carriers and Seatrade that are now over 30 years old. Ten of these vessels are chartered in. If rates do deteriorate to unsustainable levels, these ships will be scheduled for a final destination on the beaches of the Indian subcontinent, not temporary accommodation in Greek or Cornish waters.

Sea freight - Evolution of large reefers
(US cents/cbft TCE | source: Reefer Trends)



Sea freight - Evolution of small reefers
(US cents/cbft TCE | source: Reefer Trends)



Small vessels lost momentum

Meanwhile, after a strong start to the year, the market for small vessels lost momentum in mid-February and hadn't recovered by the end of June. While the business model for operators of large units has become more liner and Contract of Affreightment (COA) oriented, the smaller ships still depend on what remains a vibrant spot market, dominated by the supply and demand for frozen fish. After two good years, when operators were able to take advantage of the same conditions that underpinned the market for the larger vessels, expectations were high early in 2023, not least because of the massive 80% increase in quota (to 1.4m MT) for the Faroe Island blue whiting catch.

However, despite the heavy haul, market demand in West Africa could not match supply. This was largely because trade with and within Nigeria was affected by chaos caused by a currency issue. At the end of October 2022, Naira in circulation was N3.29 trillion before the Nigerian Central Bank began its Naira redesign policy. This resulted in a scarcity of banknotes - the amount of money in circulation had decreased by 70% to N982.09bn in February 2023 and this led to hoarding and a loss in value. This in turn led to a rising influence of the US dollar in the Nigerian economy. Many companies and individuals in Nigeria now choose to transact in U.S. dollars due to the Naira's restricted availability.

There are various effects of the U.S. dollar's influence on Nigeria's economy. First, it has increased the demand for dollars, which has caused the value of the Naira relative to the dollar to decline significantly. As a consequence, Nigerians now pay more for imported goods and services, there is inflation, and purchasing power has decreased. Additionally, Nigeria has become more sensitive to outside shocks: the value of the Naira can be considerably impacted by changes in international trade policy and fluctuations in the price of oil, which can have an effect on Nigeria's economy and the cost/standard of living for the majority of Nigerian citizens who still transact in Naira. The market for the small segment will strengthen only when the currency chaos is resolved ■