

Special briefing: What is the future for the Asia Pacific logistics market?

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The global logistics industry is going through an uncertain period. The US has so far borne the brunt of an economic slowdown which shows little sign of abating. Europe has proved more resilient, although consumer and manufacturer confidence is dropping. It has fallen to the Asia Pacific market to continue to drive forward growth rates which have proved, to date at least, to be extremely resilient. The question is, will that last?

Many economists believe the Chinese economy is set for a slowdown in the next few years. However, the true extent will be very difficult to gauge as any accurate forecast depends ultimately upon calculating the true nature and depth of the US recession. It also depends a lot on structural issues in China. However, recent forecasts have downgraded growth of the Chinese economy to around 9.7% to take account of that. Inflation is presently about 7.7%, down from a 12 year high in April of 8.5%. The pressure on food and fuel prices will have implications for the whole economy.

Japan, still the largest economy in the region, has for more than a decade been rooted firmly in an economic rut and although there were signs that it would finally return to higher levels of growth, that has not materialised. GDP growth is set to be around 1% for some time, although inflation is not something the country needs not to worry too much about.

Of the newer emerging economies, Vietnam has been one of the region's great success stories and as a result of opening up its markets has experienced average annual growth rates of 7.5% over the past ten years. However, the economy is now suffering from more financial instability than China, with inflation running at 25% and the Vietnam Dong depreciating significantly. Despite that, the country continues to attract outside investors and foreign direct investment has leapt over the past year from \$4.4bn in the first five months of 2007 to \$15.3bn in the same period this year.

South Korea, once one of the Asia 'tiger economies', is also faced with inflationary pressures, although not to the same extent as in Vietnam. Rising food and fuel prices have led to inflation increasing to 4.9% and economic growth is expected to be affected – falling to 4.4% in 2008. However, trade growth is strong (around 14%) and new bilateral free trade agreements, including one with the US, could see it grow further.

From this summary, it could be said that the macro-economic outlook for the Asia Pacific region is mixed. A major factor for growth prospects will be the future level of commodity prices. If, as some economists predict, they flatten out in 2009 and then slowly reduce, inflationary pressures will fall and stronger economic growth will return.

To obtain some further insight into the future, it is worthwhile looking at how the major Asia Pacific freight and logistics companies are performing at this time.

Shipping

The first quarter 2008 figures from Singapore-based global transportation and logistics group Neptune Orient Lines (NOL), which owns container shipping line APL, saw revenue grow by 27% to \$2.41bn whilst EBIT jumped 114% to \$137m.

NOL's figures showed that although transpacific trade into the North American west coast was depressed, volumes out of the US and into the east coast were buoyant, as were China-Europe and transatlantic traffic flows.

In the same quarter, Japanese shipping line NYK Line also delivered good results, helped by its bulk shipping business. Demand from China for coal and iron ore remained greater than the shipping sector's ability to deliver it, resulting in a 73% jump in operating profit.

Slightly more surprisingly, container trades also proved to be strong for NYK, producing a 21.4% increase in operating income. NYK hinted that uptrend was driven by the strength of Asia- Europe traffic rather than the transpacific market.

MOL, another Japanese shipping line, reported quite similar market conditions, with routes other than transpacific sectors driving up its container traffic. Bulk cargo volumes and car traffic were also very strong although profitability was hit by much higher fuel prices. The picture painted by 'K' Line was very similar, with strong demand for bulk commodities such as iron ore and coal, as well as car transport, supported by the continuing strength of container trades other than the falling transpacific market.

In their forecasts for the coming year, all three of these Japanese companies suggested continuing strong markets in shipping and other services except into the US. All expect European demand to continue to grow sufficiently to absorb excess capacity from transpacific trades, although MOL hit a note of caution about the continuing strength of demand from China after the Olympics.

Air freight

In the air freight sector, the IATA figures for the first five months of the year revealed a 1.2% growth in Asian carrier traffic set against a 1% increase in capacity. As demand slightly outstripped supply, that would suggest an increase in air cargo rates, in addition to the high levels of fuel surcharges presently being applied by all airlines. However, in May there was a drop in output resulting from the impact of the earthquake in China and weakness in the Japanese economy.

Latest figures from Hong Kong-based carrier Cathay Pacific show that demand has remained fairly robust in most markets, with the exception of northeast Asia. As with the IATA figures, its cargo tonnage growth has stayed ahead of capacity growth. However, the continued rise in jet fuel costs is having a serious impact on its bottom line.

Korean Air, one of the world's largest cargo airlines, said in its most recent financial release that the overall Korean air cargo market was growing at around 12%. The weakening Korean Won had triggered outbound cargo and traffic from US/Europe to China and South East Asia had shown strong growth. The airline believes that following the free trade agreement between Korea and US, air cargo will show a 10% annual growth.

Finally, in its latest quarter, Singapore-based SIA Cargo's freight traffic was 0.4% higher compared to last year. However, as capacity grew by a higher 1.6% during the quarter, the cargo load factor declined by 0.8 percentage points.

Express

In Deutsche Post World Net's 2008 first half interim results, its DHL Express division reported organic growth revenue growth – excluding currency effects and other non-operative items – of 13% in the Asia Pacific region. However, management commented that "economic momentum slowed somewhat in China". Also in the express sector, TNT reported that significant operational growth had been fuelled by "high double-digit" increases in China and India, presumably meaning growth in the region of 17-19%.

Growth in the region for UPS and FedEx is more difficult to quantify although it is known that the domestic Chinese express market is facing problems due to its hyper-competitive nature and rising fuel prices. UPS has reported more than 15% growth for the quarter in the region helped by good performances across all its business units. It had been particularly strong in China (growth of 30%) and India (almost 25%). The region delivered growth of nearly 20% for the 2007 full year. The numbers for FedEx are less certain although it is investing heavily in China, both in terms of infrastructure and, it is believed, in price cuts to make its services more competitive. It is planning a new Asia Pacific hub, which will open in 2009 in Guangzhou, and opened a domestic hub in Hangzhou at the end of 2007.

Conclusion

The range of macro-economic indicators and company performances just highlighted, show that the Asia Pacific market is still in good shape, although under pressure. Inflation is the big worry for many economies and that could have a detrimental effect on growth prospects if food, fuel and other commodity prices continue to rise. Fuel increases will no doubt have an impact on rebalancing the supply/demand equation in many logistics markets as a result of company failures. That will eventually lead to upward pressure on rates even in highly fragmented sectors such as road freight and domestic parcels. Fuel prices will also play a role in the shipping and air cargo sectors – not at this stage curtailing revenues, but reducing profits.

It would be too simplistic to conclude that the Asia Pacific logistics market's fortunes depend wholly on the price of oil. However, in some ways it is more vulnerable than its counterparts in Europe or North America. As a large proportion of production in the region is export-oriented, if oil prices remain at very high levels for a significant period of time, western manufacturing companies may decide it is in their interests to restructure their global supply chains. In part, that would be due to the increased cost of transporting goods from Asia Pacific to western markets, and in part due to the increased labour costs which are becoming apparent throughout the region.

In conclusion, as this brief analysis of the performance of key economies and logistics companies shows, it is far too early to discount continued strong growth in the market. The developing markets of Asia Pacific may well lead the world out of a global slowdown, positioning the region even more strongly for the future.

Global Distribution Strategies 2008 – Asia Pacific

These are just some of the issues which will be addressed at the [Global Distribution Strategies Conference – Asia Pacific](#), which will take place at the Langham Place Hotel, Hong Kong, December 2-4, 2008. Follow the link for more details.

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