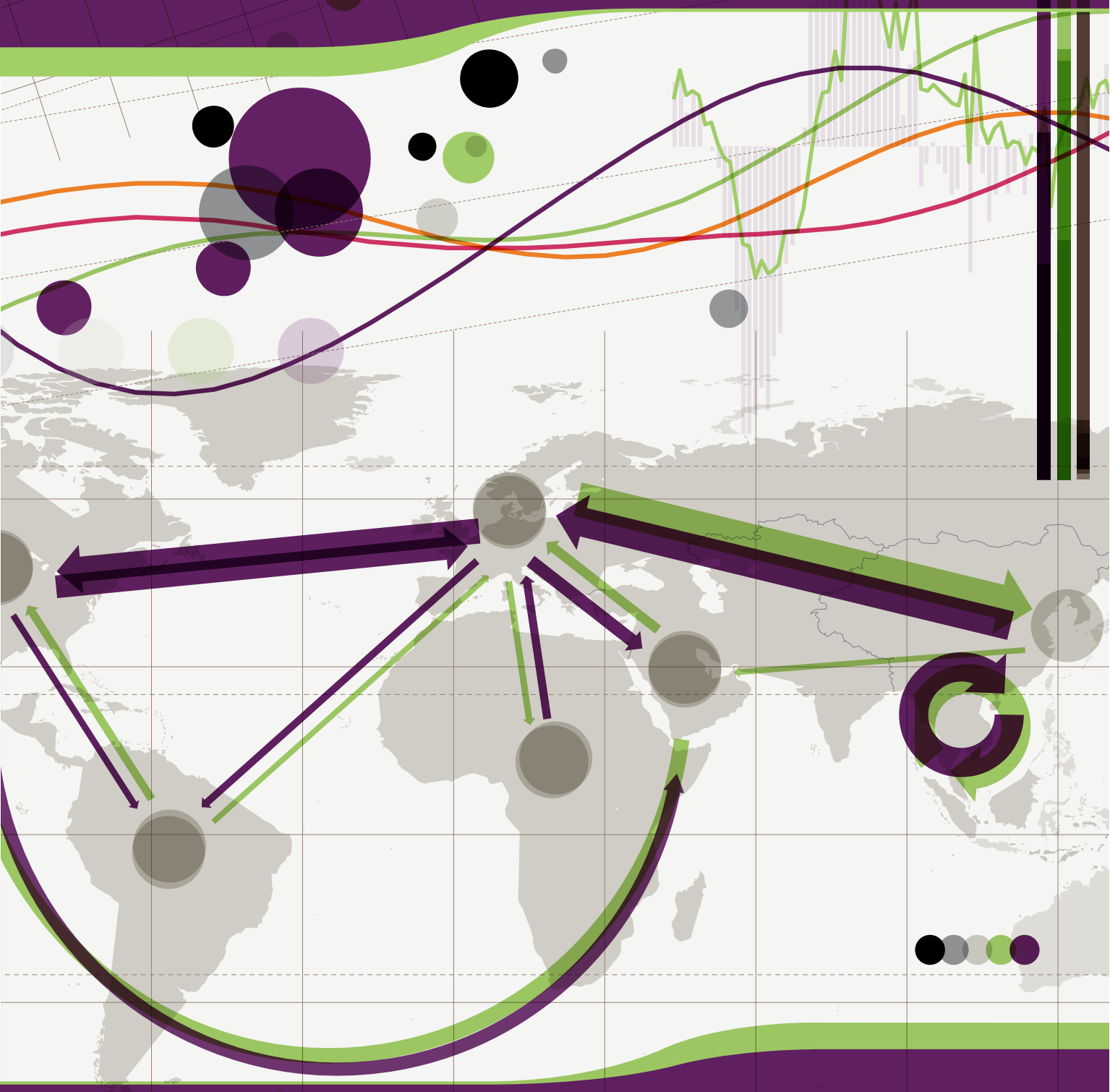
EXCLUSIVE

# Seabury's analysis of 2014



# A sigh of relief

2014 has seen marked improvement for the airfreight industry, with various countries and commodities flying high. Seabury's **Marco Bloemen**, senior vice president, and **Barend Buutfeld**, senior analyst, reveal the surprises of the year – and what to watch out for in the next

It's been a year of some small comforts for the airfreight industry; a window of relief from the market's stubborn refusal over the past few years to pick up. With the recent history of flat – or even contracting markets – 2014 finally brought some respite.

Pundits and analysts in 2013 were predicting better fortunes for this year; there were more positive outlooks than we've seen for some time. Nevertheless, 2014 has even surpassed the majority of those expectations.

While many carriers reported relatively mixed results at the start of the year, in actual fact the first few months were very strong. January to August year-to-date data reveals that global trade was up some 4% over last year – with the pace slowing a little as the year progressed. While the fourth quarter in 2013 was strong, it looks as if this year will slightly outperform the last. Overall? It looks as if 2014 will end with growth in the region of 4-4.5%.

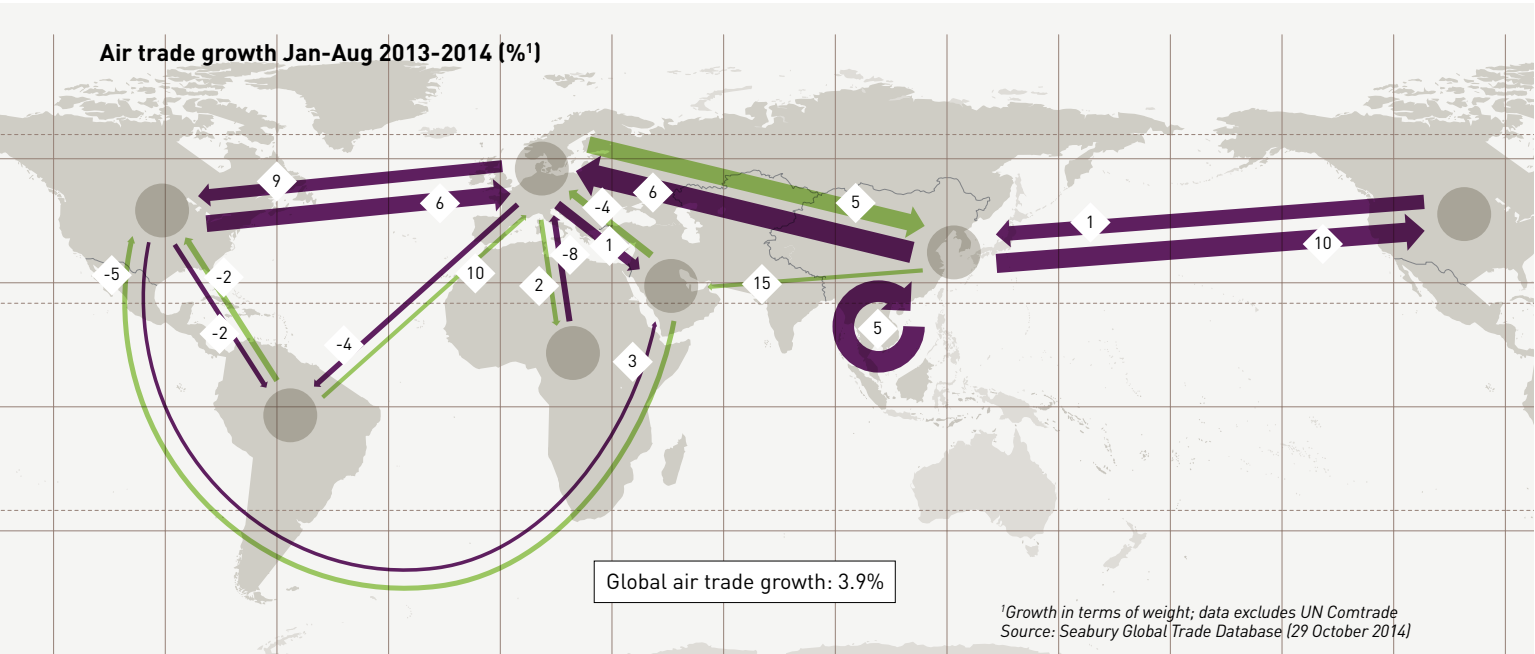
So, there has been trade growth around the globe, with a few exceptions to prove the rule. Perhaps most interestingly, the pockets of cheer did not always stem from the most obvious growth drivers. As well as bringing a year of comparative relief, 2014 also contained some surprises.

## Global oversight

Europe has arguably been the most closely watched continent since the eurozone crisis knocked both confidence and markets hard. After a relatively disappointing year in 2013, in which western Europe saw air trade growth hover over global levels at 0.8% versus 0.3%, this year Europe and its main trading partners saw higher levels of trade by air. That was true for almost all western European countries. The trend was driven by Germany, which steamed ahead with an 8.5% increase in air trade – amounting to an additional 24,000 tons in the first seven months of the year, the equivalent of 155 full 747-8Fs. The UK and the Netherlands, which tend to nestle in Europe's air trade top five, also saw similarly impressive growth rates.

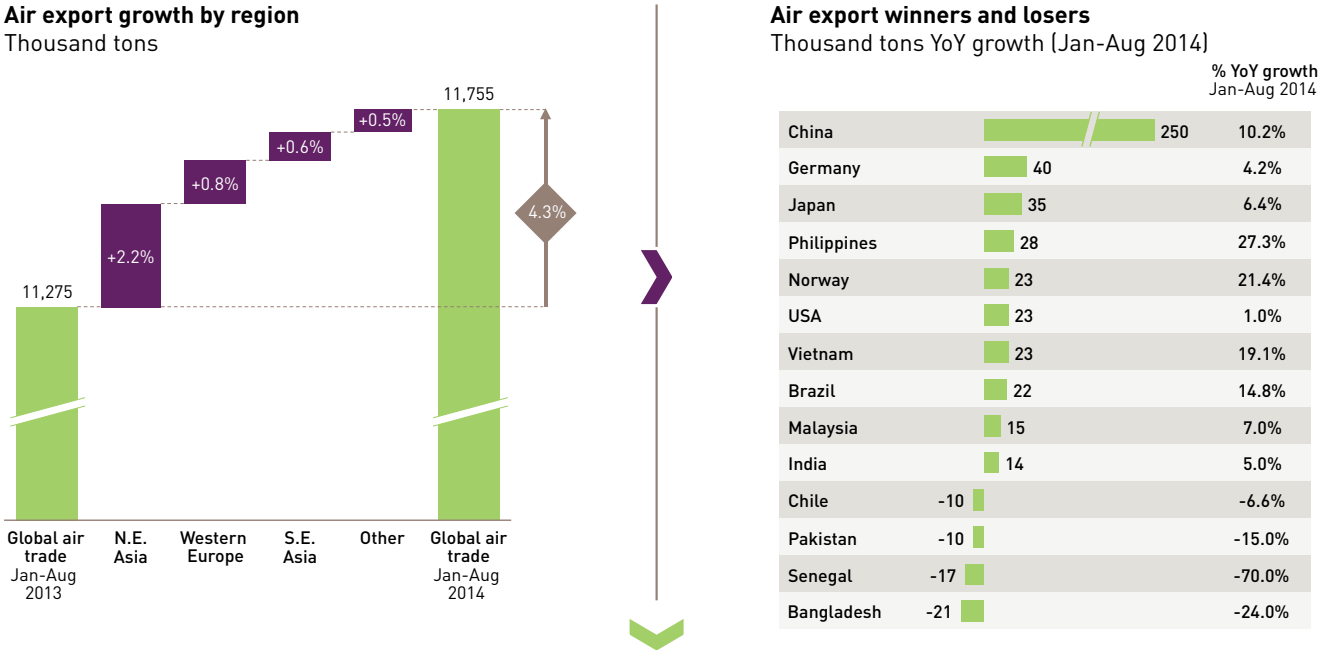
Even the Transatlantic – no cargo airline's favourite route in recent years, characterised as it is by belly overcapacity and a flattening in trade in 2012 and 2013 – has shown high, albeit single-digit growth, in both directions. This is attributable to the markets for industrial consumables, machine parts, automotive trade and even salmon picking up.

**Chart 1:** Air cargo market showing strong growth in 2014




[1]Growth in terms of weight; data excludes UN Comtrade
Source: Seabury Global Trade Database (29 October 2014)

**Chart 2:** Global growth driven by Northeast Asia and Europe




**China is the main air trade growth driver globally in 2014, largely driven by high-tech exports**

*Source: Seabury Global Trade Database, World Monthly dataset*

Europe-Asia, meanwhile, enjoyed a boost in the same commodities, racking up an impressive 9.5% growth rate, with the rise mainly driven by west to east trades – a relatively new trend, which not only saw percentage growth but also increases in absolute terms. Volumes going east now broadly match those going west, in another reprieve for carriers suffering from the previous imbalance in air trades.

Asia, of course, has its own 800lb gorilla – China – whose continued growth, albeit at hotly debated rates, marches on. In air volumes, the majority of the 10% export growth has been driven by the most popular commodities of the modern age: tablets, laptops and smartphones. But other commodities have also revealed healthy improvements. And the Go West policy continues year after year, more than bearing fruit: the region leapt 27% over 2013. The pace of its growth, which gives it volumes broadly matching southern China now, could also see it outgrow the north region, i.e. the markets around Beijing. The East, anchored by Shanghai, remains un-dimmed by its opposite's runaway success, however, and still at the top, it even rose some 12.5% in the first months of the year.

Intra-Asian trade has boosted prospects in Japan, which has grown its export market more than 6% over 2013, after years of continuous flat-lining – but its Northeast Asian neighbours are faring less well. South Korea, whose Incheon hub is the fourth busiest cargo airport in the world, has seen lacklustre volumes. While the country is keen to turn around this stagnant – and somewhat surprising – state of affairs, 2014 will not be a year to remember for the high-tech giant, which looks set to suffer the indignity of coming in even below the cautious 2% growth rate forecasted by Seabury last year. Taiwan, too, has nothing to boast about, with air trade near flat at 0.5% in the first half.

Again, there was disappointment further south where Indonesia, often touted as the next big thing, failed to deliver. It may well be the world's fourth most populous country, but its uninspiring contraction of 1.5% (year-to-date between January and July) failed to make it shine in trade terms. Its biggest decline – fashion exports – which tumbled 12% as labour costs rose, dragged down its overall growth as there were no standout commodities waiting in the wings to take apparel's place. High-tech exports, for example, are revealed by World Bank data to have fallen significantly as a percentage of total exports from the country.

But if Indonesia was the most disappointing country in Southeast Asia, its neighbours fared far better. Standout growth, perhaps surprisingly, was in the Philippines, which saw a rise of 30%, the greatest in the region in the first half, giving it greater growth volumes than even Vietnam, with sufficient extra tons to fill 270 747 freighters. This, however, may be an opportunistic move on the part of airfreight providers: severe port and road congestion in Manila has left many shippers stranded. Some 20,000 containers are stuck in the jam, which is expected to take months to clear.

Bustling Vietnam remains a beacon for air trade, its 18% growth rate in the first months surpassed even last year's impressive 11.5%. Both fashion and high-tech exports are in double digits, and the much-publicised May attacks on Chinese and other factories in protest at China's placing of an oil rig do not appear to have dimmed its glow. Both Malaysia and Thailand, which also suffered protests and investor doubts at the start of the year, showed relatively good levels of export growth at 7% and 5% respectively for the year-to-date to July. ▶

By comparison, North America was far duller. Its underwhelming 1.3% year-to-date export growth rate – much less than the global one – was mostly supported by two commodities: automotive and high tech. The auto trade flew both ways, with 30% more gearboxes than last year finding their way to Europe, while engine parts left Europe to land in North America. China, Japan and South Korea meanwhile, supplied the US with suspension parts.

But the biggest – and least surprising – sector was high tech, with Americans rushing to buy 56,000 tons more laptops, phones, tablets and computers than they did last year, almost entirely from China (though Europeans did not have the same consumerist quest, and the high-tech trade out of China actually decreased). But while Americans were busy enjoying their technological toys, they lost interest in fashion – the first half saw an unexpected and significant fall of 9% in fashion imports from all sourcing regions, apart from Europe. And the world seemingly lost interest in US healthcare products, triggering a big decline in US pharmaceutical exports by air.

There was also little to shout about in Latin America, whose biggest air trade partner is its northern neighbour, which has a good appetite for the perishables produced in the south. Chilean salmon continued to swim north at double-digit growth rates, while Peruvian asparagus similarly flourished. But Colombian flowers lost their bloom, with no growth in sales – possibly beaten off by higher demand for flowers from East Africa, where roses saw a 7.7% leap in volumes in the first seven months. Chile saw a sharp drop in the exports of agricultural seeds to the US, a decrease of more than 25,000 tons in total, preventing the country from securing a position among 2014's top exporting countries. And Latin Americans, despite hosting the FIFA World Cup, appeared to have diminished appetites for foreign goods, with overall imports flat and some flows dipping altogether.

## The commodity game

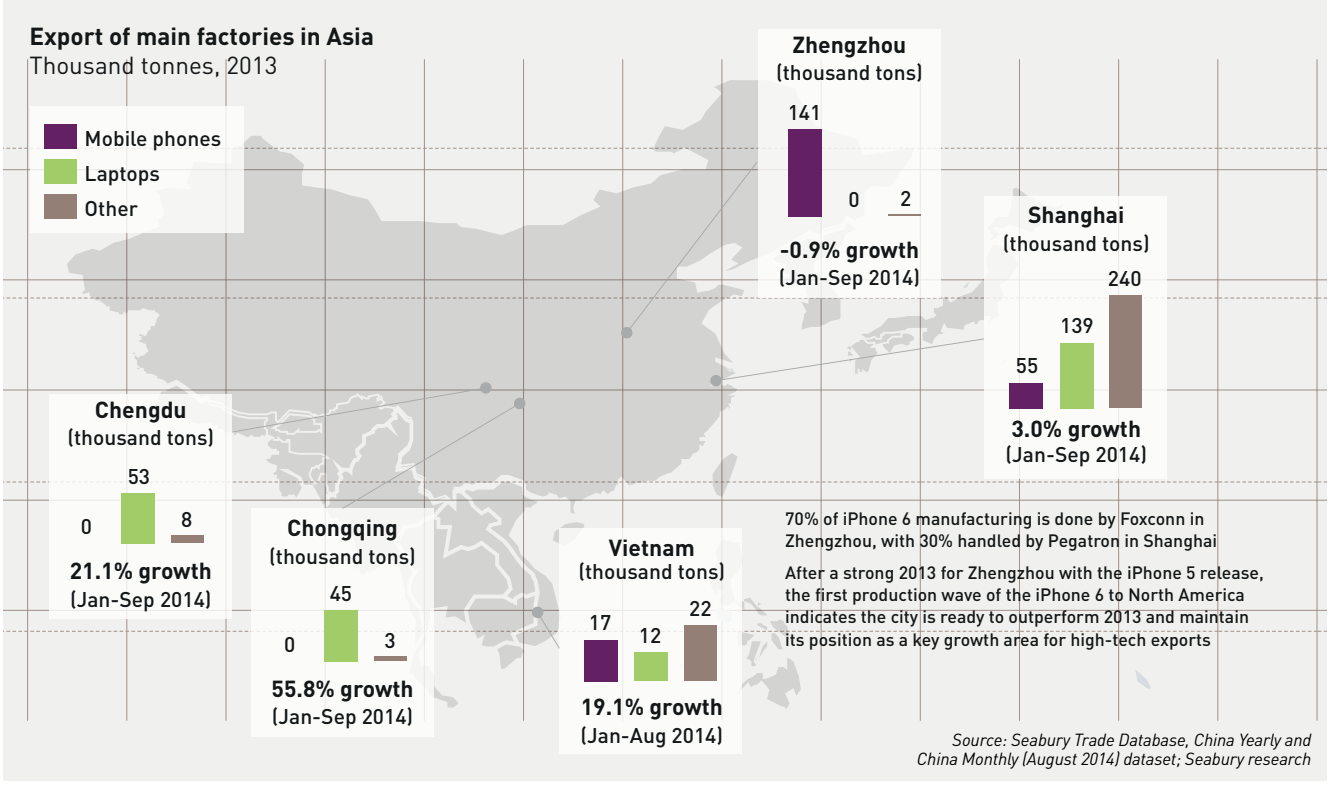
So while nations' demand for foreign goods has mostly risen, what were the most popular buys in 2014?

The car business remains key for airfreight, and it soared at the start of the year with gearboxes speeding both ways over the Atlantic. Europe also enjoyed rising trade with China, which has a newfound appetite for its auto parts from Germany, while the German auto business also fuelled the US.

Salmon is easily outswimming its perishable peers: strong results in previous years are now gaining even more ground, with Norway enjoying 18% growth to the US and Asia; Scotland celebrating a 38% rise in exports; and Chile selling 16% more to the US than it did last year. While salmon used to transit via Vietnam on its way to Hong Kong and China, it now appears to prefer a more direct route to its final destination.

Europe – or rather the luxury market of Italy and Inditex's home market of Spain – also benefited from a global love of its clothes, while some pockets of the world were also eager to buy clothes from China. While the Europeans disdained Chinese fashion, the Middle East and Africa were not so picky. Meanwhile there appears to be a global shift towards women's fashion travelling by air, while men are apparently happy to wait longer for the new trends – with their clothes switching to seafreight. ▶

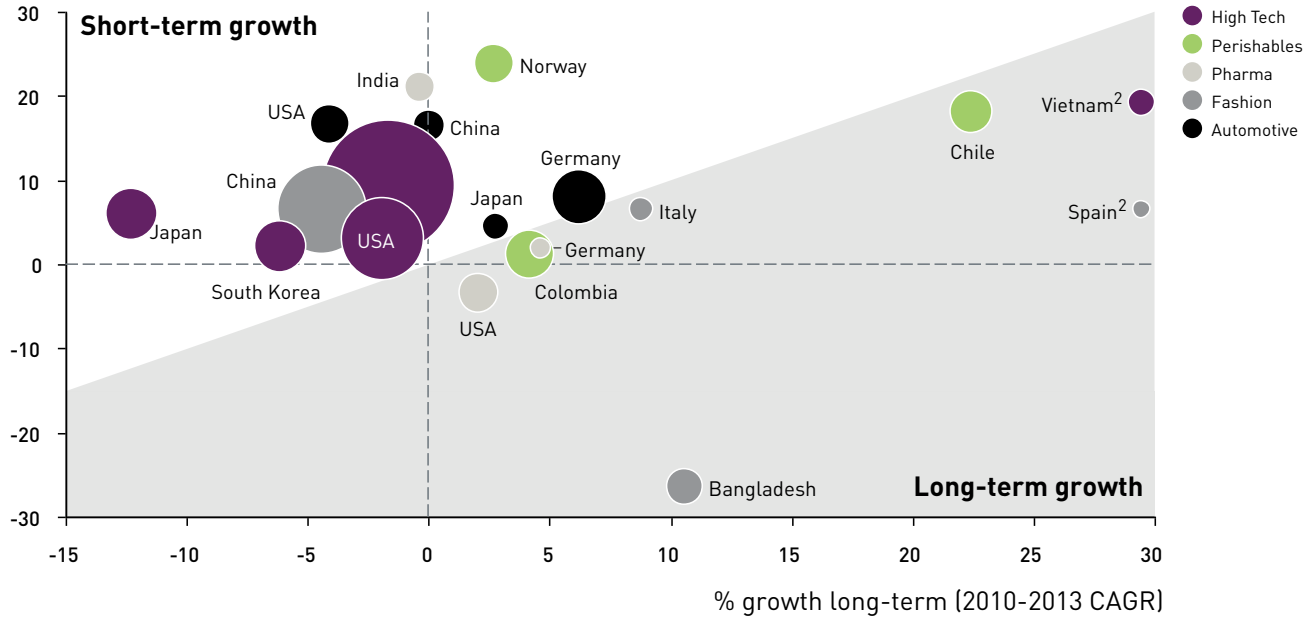
**Chart 3:** Catchment areas – China focus on different types of high tech




*Source: Seabury Trade Database, China Yearly and China Monthly (August 2014) dataset; Seabury research*

**Chart 4:** Short-term winners: turning the tide or temporary relief?

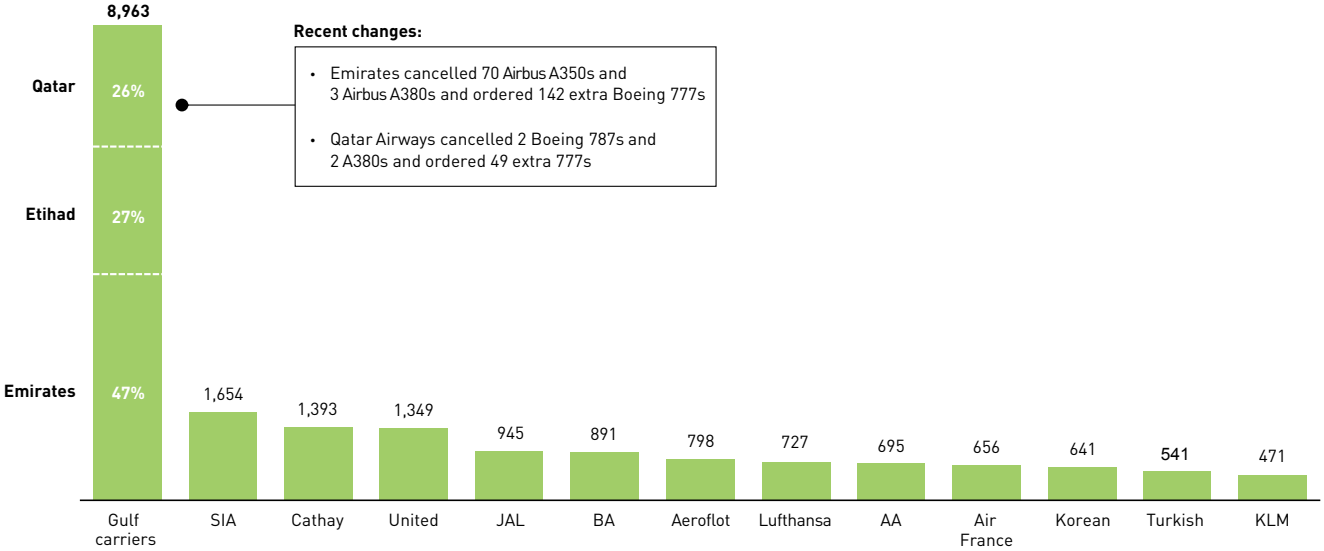
**Long-term vs short-term commodity growth by exporting country**
% growth short-term (Jan-Aug 2013-2014[1])




[1]2013-2014 Jan-Jul growth does not include UN Comtrade data;
[2]Original 2010-2013 growth rates for Vietnam High Tech (+49.3%) and Spain Fashion (+36.1%) are adjusted down for visual purposes;
Source: Seabury Global Trade Database, World Yearly & World Monthly dataset

**Chart 5:** Middle Eastern airlines dominate passenger aircraft orders

**Widebody belly capacity on firm order for 2014-2029 delivery**
Tonnes




| | Gulf carriers | SIA | Cathay | United | JAL | BA | Aeroflot | Lufthansa | AA | Air France | Korean | Turkish | KLM |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Age of fleet[1] | 7 | 7 | 9 | 15 | 10 | 14 | 3 | 9 | 15 | 11 | 11 | 6 | 13 |

[1]Average of fleet in service (widebody passenger aircraft); Note: Only firm OEM orders from airlines considered, except those for which the buying carrier has not yet been announced; data excludes optioned aircraft or LOI to order aircraft, e.g. excluding Qatar (59 aircraft), Etihad (51 aircraft) and Emirates (20 aircraft); Source: Ascend Fleet Database (Oct 2014); Seabury analysis

But while China did its best to dress the world, Bangladesh, famed for its apparel industry, saw its export market contract some 25%, as social and political unrest regarding garment workers' rights hindered the flow of exports.

Pharmaceuticals, meanwhile, the transport of which has seen significant investment from airlines, airports and handlers, was something of a disappointment in volume terms, with air movements flat. Only India celebrated a rise – and a healthy one – of 22% in the first seven months.

But by far the strongest commodity this year, which has been disappointing in previous years despite the hype, is high tech. While manufacturers continue to dip their toes in the waters of seafreight, air has had an exceptionally good year. Tech toys from China required an extra 43,000 tons of uplift, or some 400 747-8Fs, the majority of which flew transpacific to the US in just the first seven months.

> **"By far the strongest commodity this year, which has been disappointing in previous years despite the hype, is high tech"**
> Marco Bloemen, Seabury

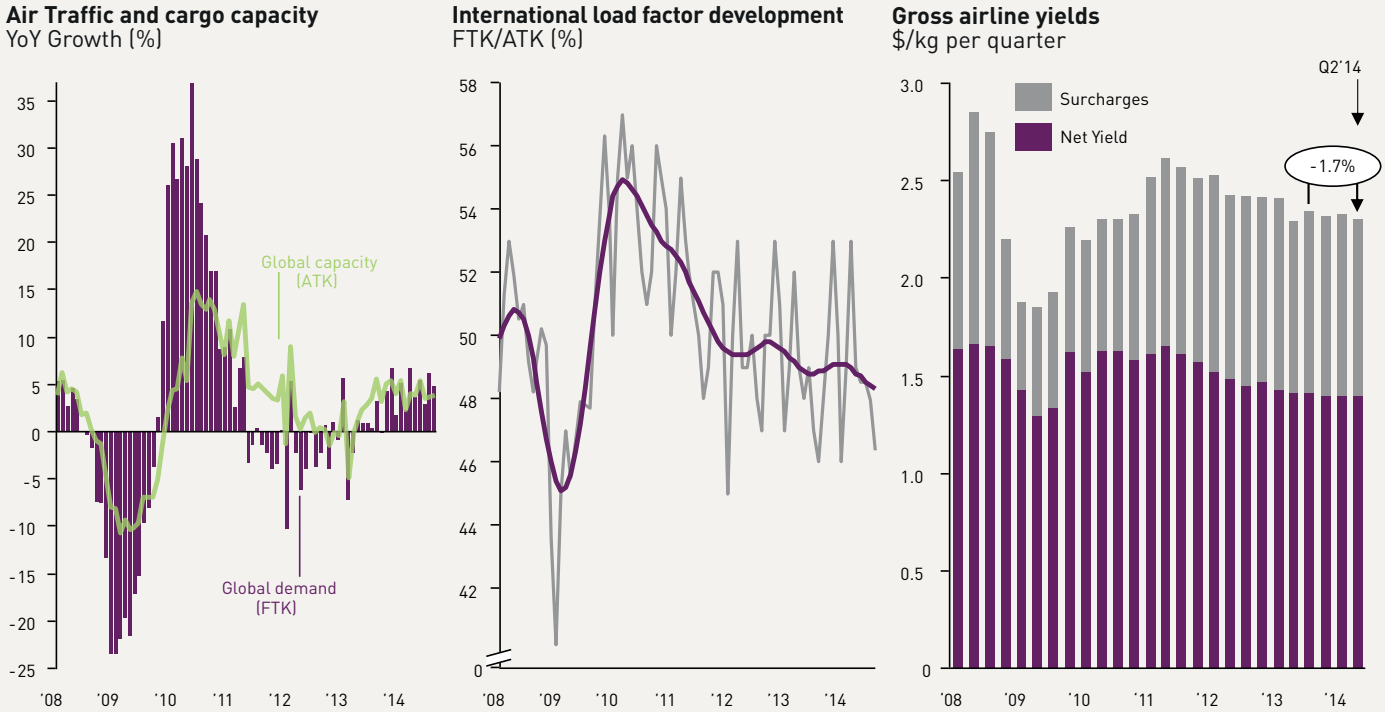
## Capacity

So it has been a year of respite, in various and sometimes surprising quarters. But, sadly, despite the clear global growth in trade this year, there can be no relaxing just yet for the air cargo industry.

The supply and demand imbalance has improved, but remains inequitable. The structural overcapacity has not yet been fully addressed, although this year has seen supply and demand growth falling better in step – revealed by the stabilisation of global weight load factors at about 50%, after years of consecutive falls. As a result, yields have remained level after last year's slight decline.

The better balance in supply and demand is largely due to two factors: an increase in global trade, combined with better capacity discipline from the carriers, which this year parked another 23 three and four-engined freighters. However, that good news was partly offset by the entry into the market of 14 new, large, widebody freighters.

**Chart 6:** The air cargo industry is expected to remain under pressure




**Historic capacity and demand imbalance, only recently giving way to more stable load factors and yields, is expected to continue**

*Source: IATA e-Chartbook; IATA Monthly Traffic Results; Seabury Surcharge Model; Seabury analysis (21 September 2014). FTK, ATK Actuals include August 2014; yields until June 2014*

But it's the bellies that tend to strike fear into the hearts of many in the industry. Lower deck capacity continues to grow – and is unlikely to stop any time soon. But, happily for some perhaps, this bellyache is somewhat regional. This winter will see additional capacity between Europe, the Middle East and south Asia grow in double figures.

But the transatlantic and Europe-Asia (direct) will grow in line with trade growth. Regional capacity growth trends are expected to continue as last summer's order bonanza of widebodied bellies by Gulf carriers reverberates around the industry.

## So what might 2015 bring?

Seabury were fairly positive that 2014 would be a solid year of relief for many carriers, even though last year's forecast of 3-4% will be just below actual for the full year.

For next year, however, the signs are not as good. Europe, the second-largest air trade export region, has already started to slow down as the year-end approaches.

As 2014 progresses, it appears there is two-tiered growth: Asia's role as the global growth driver has strengthened over the course of the year; but Europe is tailing off. Germany, the manufacturing and economic powerhouse of the continent, is expected to fall into a third consecutive quarter of economic contraction, creating a technical recession that analysts predict may last until the middle of next year – which does not bode well for air cargo.

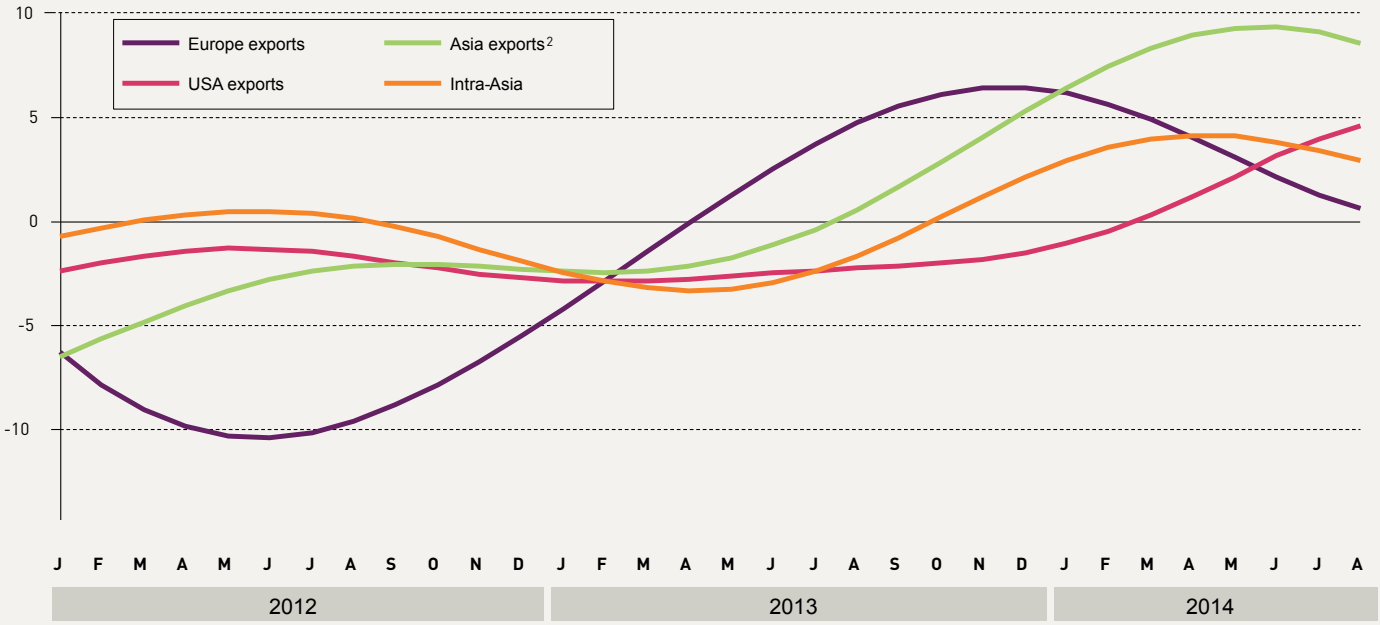
North America, on the other hand, has enjoyed a nice second-half boost, and could start to see some higher growth in its exports, which were weak this year – but that is unlikely to have any significant effect on global air trade. And the brightest star of the year, high tech, is not expected to produce another wave to ride that will better this year's good figures.

## What to watch

It's not a gloomy picture as such. But neither is it one of significant growth: repeating this year's results in 2015 will be challenging. But, like 2014, and even in the more miserable years before it, there have always been opportunities – some expected, others more surprising. But to capitalise on these possibly infrequent chances, companies will need to watch market dynamics, analyse data, and be in the right place at the right time. Whether it's to net some salmon, or capitalise on growth pockets such as Vietnam, there are likely to be some consolation prizes out there. ■

**Chart 7:** Recent growth in 2014 is starting to see slowdown

**Growth trends of the world's largest trade lanes**
YoY growth (%)[1]




**Key export regions showed a healthy growth at the start of 2014, but are starting to show signs of slowdown**

*[1]Smoothed for enhanced clarity; [2]Excluding Intra-Asia flows. Source: Seabury Global Trade Database (12 September 2014)*