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Panama Canal threatens West Coast ports' regained market share

Bill Mongelluzzo, Senior Editor | Apr 19, 2016 7:18PM EDT

West Coast ports have regained the market share of U.S. containerized imports they lost last year during the longshore labor disruptions, but industry analysts say the deployment of bigger ships through the enlarged Panama Canal later this year could swing the balance back to the East Coast.

Market share numbers released Tuesday by PIERS, a sister product of JOC.com within IHS, show the West Coast share of U.S. imports is back in the range of 51 percent to 53 percent, where it has been in recent years. That's noticeably higher than it was in February 2015 when the West Coast's share of U.S. imports plunged to 46 percent.

West Coast ports went into gridlock in early 2015 due to work slowdowns by the International Longshore and Warehouse Union and retaliation by the Pacific Maritime Association during the lengthy and contentious coastwide contract negotiations. East Coast ports' market share, which is normally in the 40 percent to 42 percent range, shot up to 46.6 percent in February 2015, according to PIERS. The Gulf Coast's share, which is usually 5-5.5 percent, increased to about 6.5 percent in early 2015.

The trans-Pacific trades returned to normal by last summer. Imports through the East Coast were strongest in the early summer, peaking in July, while imports through West Coast ports increased in late summer, peaking in August and September. Higher-value merchandise is normally shipped in late summer and fall for the holiday-shopping season. Shippers are willing to accept a higher all-inclusive freight rate and intermodal rail rate through the West Coast in return for faster time to market. Lower-value, redundant shipments that are governed mostly by price normally move in higher volumes during the winter and spring on the less costly all-water services from Asia to the East Coast.

January and early February this year were busy months for West Coast ports, and trans-Pacific freight rates were higher, during the run-up to Chinese New Year in Asia. After the factories closed for the two-week celebration, volumes dropped steeply and West Coast market share also went lower.

The bottom line, as far as West Coast ports are concerned, is that most beneficial cargo owners did not make permanent changes in their cargo routing due to the port congestion that resulted from almost four months of ILWU work slowdowns from Oct. 31, 2014, until a tentative contract was reached on Feb. 20, 2015. Noel Hacegaba, chief operating officer at the Port of Long Beach, said that after extensive meetings with BCOs, "it is safe to say they have regained their confidence in the West Coast."

Paul Bingham, vice president at Economic Development Research Group, said the 2015 loss of market share on the West Coast was a temporary reaction to port congestion and labor issues, and the distribution networks of retailers and component suppliers didn't change overnight. That is evidenced by the resurgence of transloading of international freight into domestic intermodal containers at West Coast ports. On the other hand, "this is no guarantee that long-term evolution of the distribution networks won't continue to favor more use of East Coast all-water routes," Bingham said.

The next big change in cargo routing and market shares could occur this summer. After numerous delays, the Panama Canal Authority is assuring customers that completion of the third set of locks, which will allow larger ships to transit the canal, is set for late June. John Wheeler, vice president of carrier sales at the South Carolina Ports Authority, said carriers say they are committed to deploying larger vessels on those routes this summer. If the canal is not immediately ready for commercial service, carriers will most likely begin the services through the Suez Canal, and then migrate them to the Panama Canal when it is ready.

Wheeler said that initially the current strings of vessels with capacities up to 5,000 twenty-foot-equivalent units will be upgraded to about 8,000-TEUs. In late 2017 or shortly thereafter, when the Bayonne Bridge in New Jersey is raised and bigger ships can be accommodated at the largest East Coast port of New York and New Jersey, vessels of 10,000- to 12,000-TEU capacity will be introduced into all-water services through the Panama Canal, he said.

Of course, even larger vessels, up to 18,000-TEU capacity, are regularly calling at West Coast ports. Hacegaba said carriers have told the port they will continue to upgrade the size of vessels calling in Southern California. The steady flow of mega-ships into the trans-Pacific is forcing freight rates lower, but when compared to other global trade lanes, and especially the Asia-Europe trade where the world's largest ships now call, freight rates in the trans-Pacific are not as low, he said.

The combination of declining all-water freight rates to the East Coast, and more aggressive intermodal pricing by eastern railroads compared to the intermodal pricing policies of western railroads, is driving more cargo to East Coast ports that is destined to the mid-South, Wheeler said. Charleston is seeing increased cargo flows to destinations such as Memphis, Nashville and Birmingham, he said.

East Coast ports are also gaining some market share due to the growth of manufacturing in Southeast Asia, said Dan Smith, principal at the Tioga Group. With production increasing rapidly in Vietnam, all-water services via the Suez Canal make East Coast ports more competitive, he said.

By the same token, when the Panama Canal is ready for full commercial use, the first shift of cargo to that route will come not at the expense of West Coast ports, but rather will be cargo from North Asia that had migrated from the Panama Canal to bigger ships transiting the Suez Canal the past two years, he said. When bigger ships are able to transit the Panama Canal later this year, there will be a shift of cargo from North Asia away from the Suez Canal to the Panama route, he said.

In the longer term, the two most important factors driving cargo routing will be carrier pricing and the reliability of port labor, industry experts say. Right now, with the labor problems of 2014-15 fading, pricing is the major driver. Wheeler noted that BCOs shipping cargo to the mid-South can save save several hundred dollars per 40-foot container via the South Atlantic compared to intermodal services through the West Coast, so that is where the growth is.

At the same time, larger retailers that are planning their distribution needs for the next few years are closely watching what the ILWU on the West Coast and the International Longshoremen's Association on the East Coast are doing in terms of extending their existing contracts, Smith said.

Planning the location for a distribution facility is a multi-year effort to build the facility and achieve a return on the investment, so retailers want assurances of labor peace, Smith said. Last year, the ILA and employers represented by the U.S. Maritime Alliance announced they would initiate discussions on extending the existing contract beyond its 2018 expiration date to possibly 2025. However, those talks seem to have stalled.

At the same time, PMA President Jim McKenna on Friday formally asked ILWU President Bob McEllrath to present to the union membership a proposal to initiate contract extension talks beyond the expiration of the West Coast pact which is set for July 1, 2019. McEllrath is expected to present the request this week at an ILWU caucus in Panama.

Smith said 2014-15 proved that reliability trumps all other factors in cargo routing, so the coast that is first to produce a contract extension will have an edge in the battle for market share.

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