Impact on India's Trade Due to Red Sea Disruptions

The Red Sea region has become a focal point of concern due to the skirmishes that have developed around it, involving several West Asian countries and non-state actors. The region is highly critical for global trade as the gateway to the Suez Canal, the fastest route for freight movement from Asia to Europe, through which about 12% of global shipping traffic passes. Experts anticipate that the fallout from the disruptions in the Red Sea could disproportionately impact consumers and economies across the world.

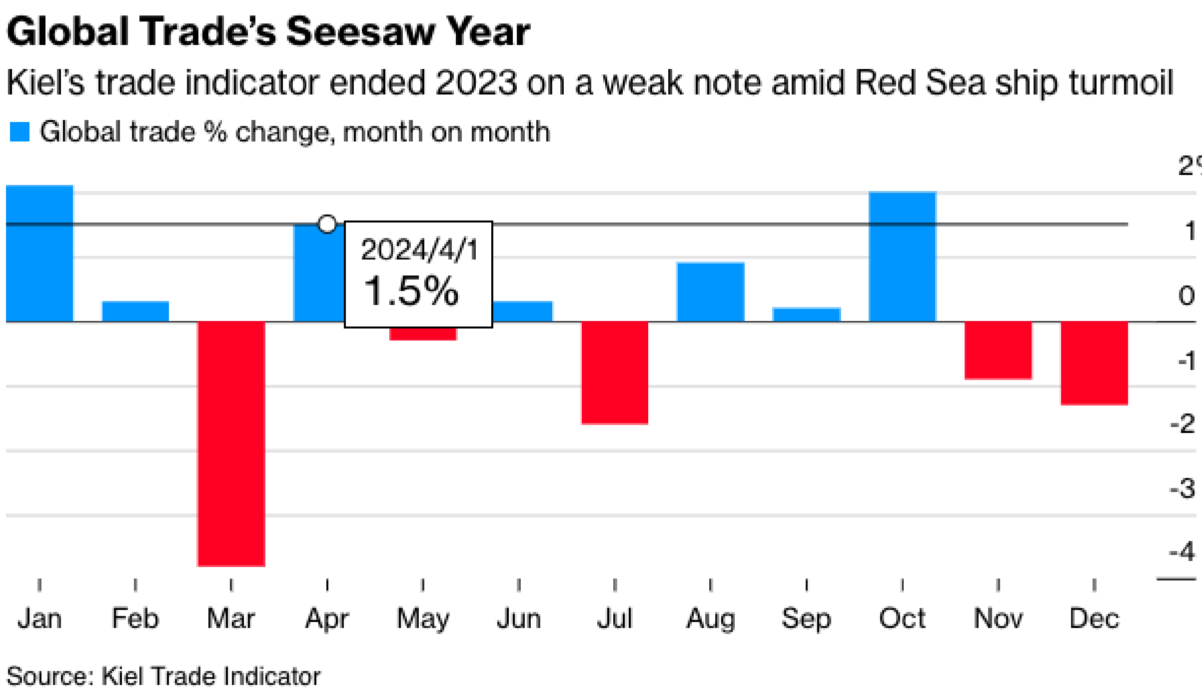

Figure-1

For instance, the recent Kiel Trade Indicator reveals that the European Union's imports dropped by 3.1% in December, and exports were down by 2%. Germany, the world's third-largest exporter, experienced a 1.8% decrease in imports and a 1.9% drop in exports. The global trade gauge indicated a 1.3% decline in international trade last month, reflecting a tumultuous year.

India too, is heavily reliant on the Red Sea for approximately 80% of its exports to Europe. It therefore faces significant challenges. The ongoing Russia-Ukraine conflict has already slowed

India's exports to the European Union, which contributes over 15% to its total goods exports. Additionally, environmental measures such as the carbon border adjustment mechanism and the EU's deforestation law could further impact India's exports. So the Red Sea disturbances have come at a difficult time.

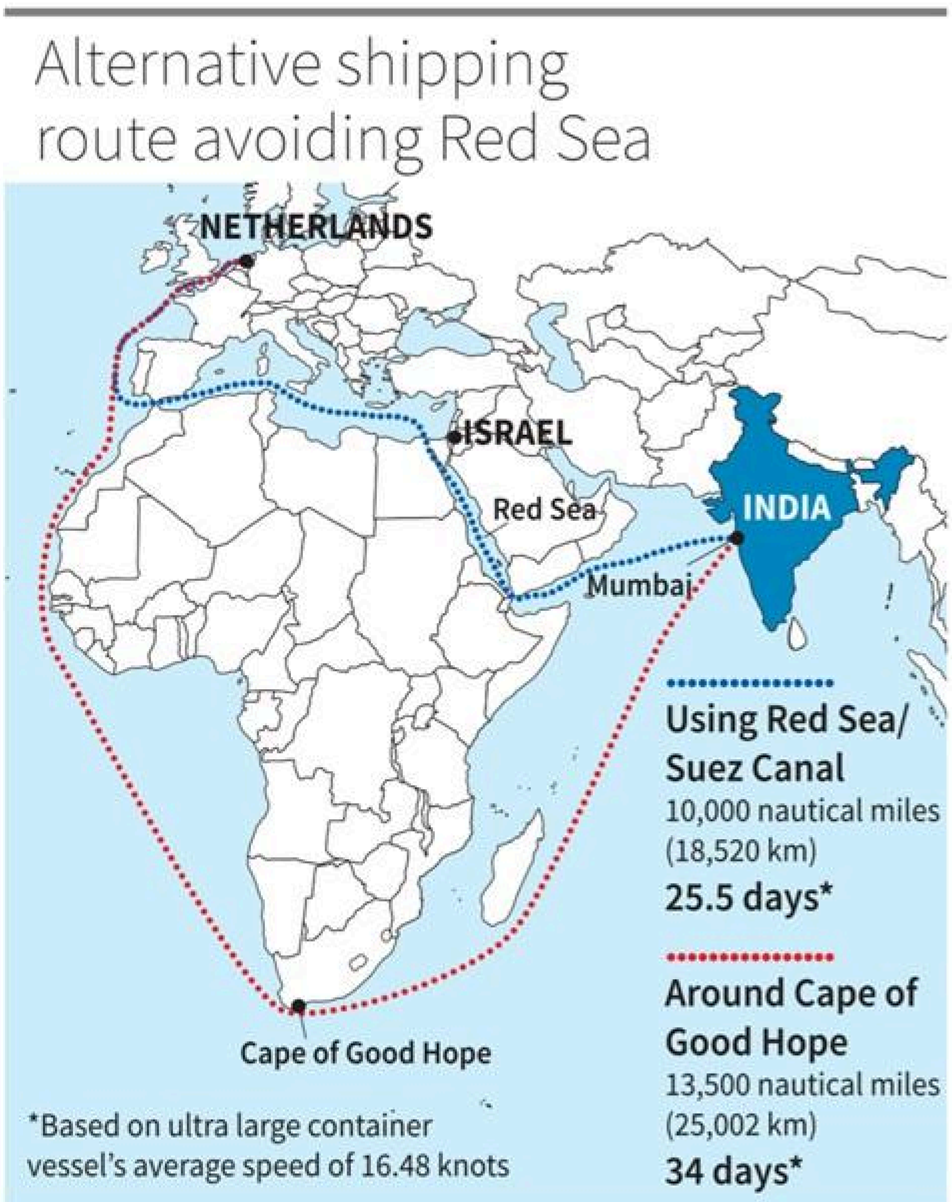

Figure-2

The disruptions have led to delays of 2-3 weeks for most ships with India as a destination or as an origination point, though container availability has not dipped said a senior Ministry of

Commerce and Industry official Satya Srinivas. However, the combined impact of increased freight costs, insurance premiums, and longer transit times could significantly raise the prices of imported goods. The Department of Commerce and Industry and the Ministry of Finance discussed maintaining credit flow to Indian exporters grappling with higher trade costs due to the crisis in the Red Sea. Shippers are rerouting consignments through the much longer Cape of Good Hope, resulting in delays of 14-20 days with concomitant higher freight and insurance costs. Kolkata to Rotterdam freight, for example, has risen from USD 500 to USD 4,000 due to the Red Sea crisis as reported by Business Standard.

Continuous discussions are taking place within the government to take stock of the scale of disruptions and to suggest measures to counter those. An inter-ministerial meeting was chaired by the Ministry of Commerce and Industry Secretary Sunil Barthwal aimed at finding measures to tackle the impact on trade due to the crisis. The Ministry of Defence has focussed on improving surveillance in the Red Sea region, while the Ministry of External Affairs is holding diplomatic negotiations with Iran on the crisis. External Affairs Minister S Jaishankar after his talks with Iranian counterpart Hossein Amirabdollahian said "There has also been recently a perceptible increase in threats to the safety of maritime commercial traffic in this important part of the Indian Ocean,". Terming the attacks on ships in the vicinity of India as a matter of "grave concern" to the international community, he said that such threats have a direct bearing on India's energy and economic interest as he underlined that this "fraught situation" is not to the benefit of any party.

The disruptions in the Red Sea are having a profound impact on global industry players, and key figures from the shipping sector and international banks have shared their perspectives on the severity of these challenges. During the Davos meeting DHL Group CEO Tobias Meyer emphasized the consequences of rerouting ships around southern Africa instead of using the Suez Canal shortcut. Meyer highlighted the emerging imbalances in container capacity, predicting potential shortages within about two weeks. He expressed concerns about the slower-than-expected back-flow, particularly affecting Asia.In response to the challenges, Maersk Line Limited, a major shipping company, mentioned that the few vessels making the Red Sea crossing are closely monitored in the proximity of U.S. Navy assets. This strategic positioning aims to reduce risks to both crews and cargo, ensuring a safer transit amid the disruptions. The renewed threats to global supply chains were highlighted by European Central Bank President Christine Lagarde. Lagarde highlighted key factors such as wage bargaining, profit margins, energy prices, and the potential return of supply bottlenecks as critical areas of concern during an event at Bloomberg House in Davos.

The crisis in the Red Sea has had a favourable impact on Sri Lanka. The strategic location of Colombo is crucial, providing ships with convenient access to the Middle East, South Asia, and East Asia, according to Lal Weerasinghe, a senior official at the Sri Lanka Ports Authority (SLPA). The Port of Colombo, serving as a vital link between Africa, the Middle East, and East Asia, witnessed a 2% increase in handling 6.94 million 20-foot equivalent units (TEUs) in 2023, as per SLPA data. In December alone, TEUs experienced a 15% year-on-year growth. Over the past four to six weeks, shipping lines have sought more berthing windows at the port's three terminals, and transshipment volumes from Colombo have also risen, as reported by two terminal operators. Weerasinghe noted that while the port typically handles 5,000-5,500 TEUs per day, there has been an increase of about 1,000 TEUs per day since late last year.

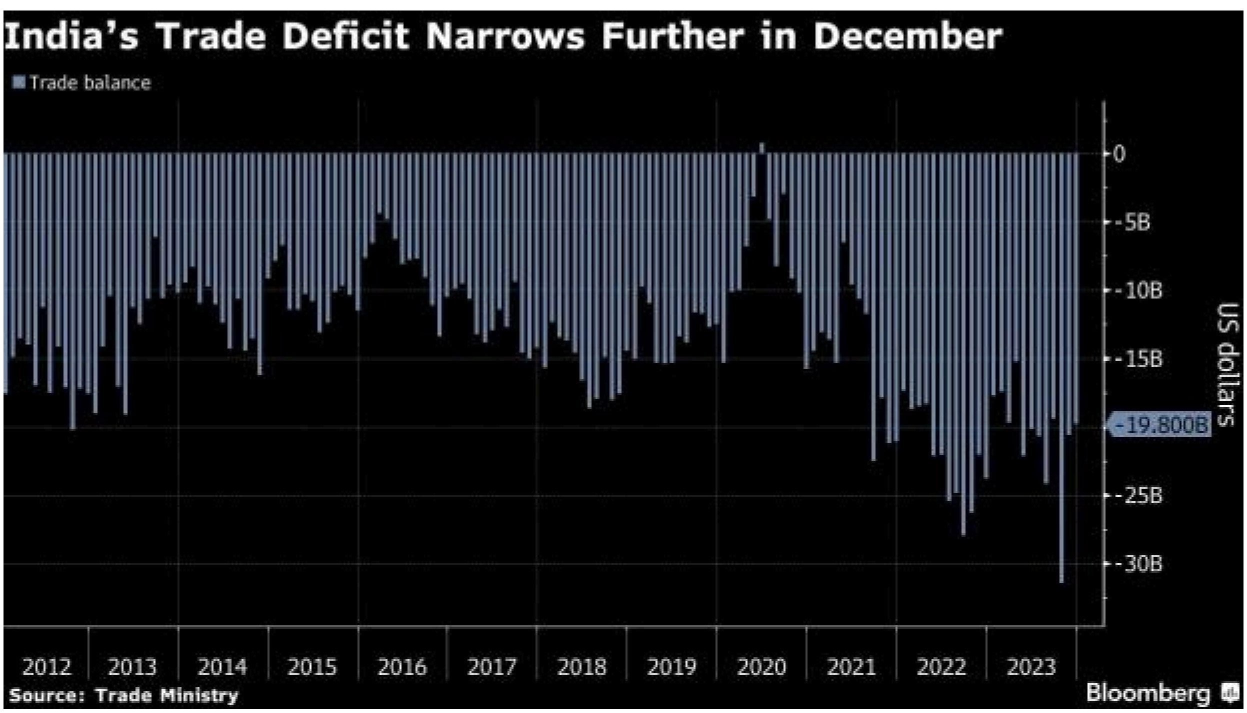

Figure-3

As per data, higher exports helped India's merchandise trade deficit come in lower than expected at $19.8 billion in December, though officials signaled that the turmoil in the Red Sea could have a positive impact on this month's figures. Economists polled by Reuters had expected a merchandise trade deficit of $21 billion in December. Indian officials believe that the situation is tense as the ships taking a longer route than the Red Sea that has escalated freight costs.The Red Sea region's importance is highlighted by its role in 30% of global container traffic and 12% of global trade. With 95% of vessels rerouting around the Cape of Good Hope, journeys are extended by 4,000 to 6,000 nautical miles, adding 14 to 20 days to transit times. Addressing the situation from an oil market perspective, the CEO of Saudi oil giant Aramco acknowledged that global oil markets can manage Red Sea disruptions in the short term. However, he cautioned that prolonged attacks by the Houthis on ships could lead to a shortage of tankers, resulting from extended voyages and supply delays. The CEO of Aramco Amin Nasser a National oil company told Reuters that he anticipates the oil market to tighten, considering that consumers have depleted stocks by 400 million barrels over the last two years. OPEC's spare capacity is identified as the primary source for meeting rising demand in the face of potential supply disruptions.

Low-value Indian exports, particularly in agriculture and textiles, are expected to bear the brunt of the Red Sea region's disruptions. Freight rates have surged by up to 600%, prompting Indian exporters to suggest the establishment of a government-owned shipping line of global repute. The freight hike issue was flagged in the meeting of the Board of Trade (BoT) chaired by Commerce and Industry Minister Piyush Goyal. The Federation of Indian Export Organisations (FIEO) Director General Ajay Sahai in the meeting said “It is a serious issue” and the problem will hurt the global demand for goods besides pushing inflation in different countries. According to the FIEO, India’s outward remittance on transport services is increasing with rising exports.“We remitted over USD 80 billion as transport service charges in 2021. As the country moves towards the goal of USD 1 trillion in exports, this will touch USD 200 billion by 2030. A 25 % share by the Indian Shipping Line can save USD 50 billion year on year basis,” he added.

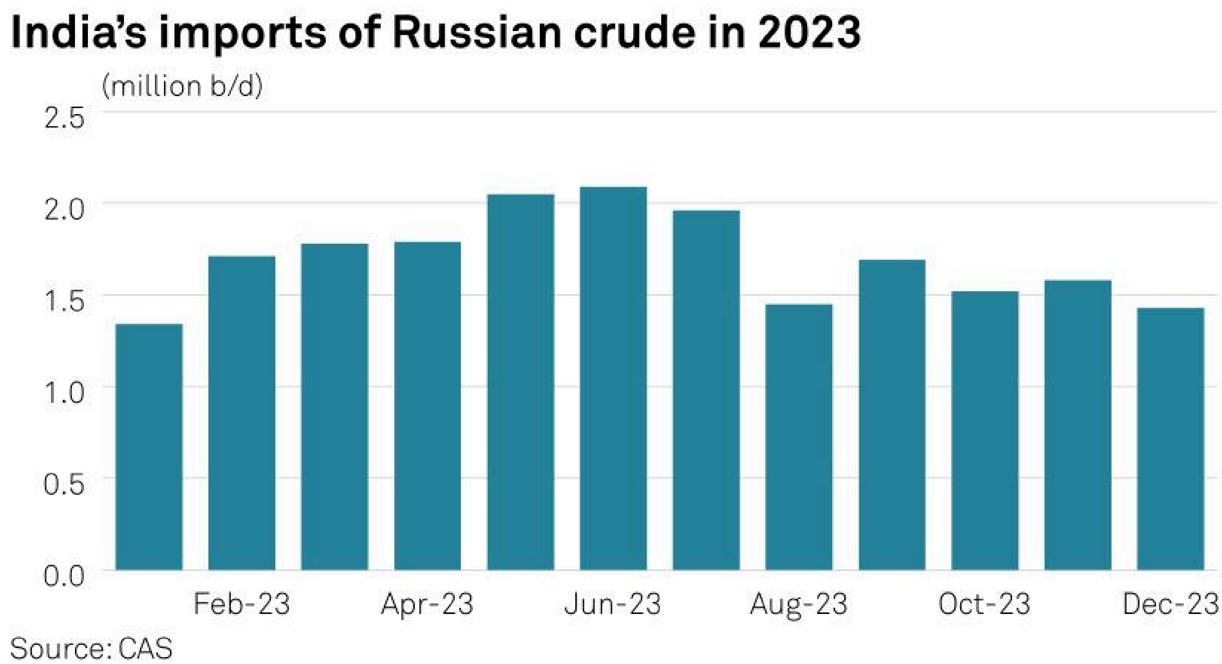

Figure-4

Russia, holding approximately 112 million barrels of oil on water, with a significant portion destined for India, poses another concern. Notably, 19.2 million barrels are positioned in proximity to the Indian subcontinent, covering the Arabian Sea, Indian Ocean East, and Southeast Asia. Refiners and traders may tap into these reserves in case of disruptions, but the situation adds risks to future oil contracts and could prompt India to seek alternative supplies from the Middle East. On the other hand, U.S. retailer Target is experiencing minor disruptions in shipments from India and Pakistan, major regions for apparel manufacturing, due to the Red Sea crisis. The company is working with shippers to redirect merchandise around the Suez Canal, anticipating minimal additional time and costs associated with rerouting. The Red Sea crisis is thus reverberating through global trade, impacting economies, and necessitating strategic responses from various stakeholders.