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Fitch Ratings: Some Chinese Exporters Face Increased Costs due to Red Sea Crisis

Fitch Ratings-Hong Kong/Shanghai-06 March 2024: Chinese companies exporting goods to European markets face higher shipping costs resulting from the ongoing Red Sea crisis, says Fitch Ratings. We believe this supply-chain disruption has less overall impact on Chinese exporters than in the pandemic years of 2021-2022, because of reduced external demand for Chinese goods and growing container shipping capacity, which is likely to expand further this year.

Around 60% of Chinese trade with Europe typically transits through the Suez Canal. Some vessels now face detours and heightened costs as they have to re-route via the Cape of Good Hope, lengthening the transit by 10 to 15 days. Shipping freight rates have increased, particularly for container shipping. Some smaller-volume goods have been shifted to rail, notably on the China-Europe railway line, where utilised capacity for goods transport from China to Europe has increased significantly from the pre-crisis level.

China-flagged ships, however, may have been less affected by the crisis, with press reports suggesting some vessels from Chinese shipping lines still travel via the Suez Canal. Major Chinese seaport operators have not experienced significant congestions or loss of volume at their ports. In addition, bulk cargo ports are less affected than container ports.

Auto and solar modules, among China’s exports to Europe, are more affected by the disruption as shipping constitutes a large portion of these products’ cost structures. Europe is a key destination market for China-made electric vehicles (EVs) – led by Tesla – and inflated shipping costs may dampen their competitiveness, potentially eroding market share, especially amid Europe’s tightening regulatory stance towards Chinese EV exports. This could accelerate the Chinese EV exports' pivot away from Europe and also encourage Chinese automakers to build overseas capacity near key markets.

We expect some small and mid-sized solar module exporters to bear losses and face an increased risk of exiting the market if shipping costs stay at high levels. The extended shipping time results in uncertain delivery times and lengthens working capital turnover. Larger solar module markers, which typically have more diversified production footprints and long-term contracts with shipping companies, have been less affected by soaring logistics costs. However, they face higher prices for contract renewals in 2024.

The impact on Fitch-rated Tongwei Co., Ltd (BBB-/Stable) should be minor, as its earnings – as measured in EBITDA – are predominantly from upstream polysilicon manufacturing, which has low reliance on overseas markets due to China’s dominance in wafer production.

Shipping costs are also significant for other major products Chinese companies sell to the European market, such as furniture, but we expect exporters to pass through some additional expenses to customers, therefore mitigating the negative impact on profit margins. The impact of higher shipping costs on China’s exports of most other electric and machinery products should be modest, as we believe they represent less than 3 percentage points of the products' landed prices before the crisis.

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