



THE LOADSTAR

LongRead

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Chinese Logistics



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The art of the deal

Chinese Logistics

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Global headlines suggest the trade spat between the world's two largest economies could escalate into a full-blown trade war. April saw tit-for-tat tariffs levied by both sides: the US targeting steel; China retaliating against US pork, meat and fruit

A second round of US tariffs could come into effect in May, with \$50bn in levies slated for Chinese aerospace, robotics and machinery products. China's response was swift, proposing additional tariffs of 25% on 106 US exports, including soybeans, a market worth \$12.4bn to US farmers in 2017.

Rhetoric is a powerful political tool, however, and US president Donald Trump is famously keen to deploy it. Some analysts suggest Trump is well aware he cannot win a trade war with China, and is in fact positioning for concessions in other areas, namely the

barriers to entry China uses to make life difficult for foreign companies operating within its borders.

China is no longer a developing economy, it is claimed, and thus it should not carry out protectionist policies of massive state subsidies for Chinese companies competing internationally, while at the same time implement forced technology transfers as a condition on foreign companies wanting to do business there.

Billy Wong, principal economist Greater China at the Hong Kong Trade Development Council (HKTDC), told



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The Loadstar that Trump's trade bluster may well be tactics straight out of *The Art Of The Deal*, his famous playbook on negotiating.

"It's very difficult to say, but at the moment I think Trump is maybe playing his own negotiation tactics for more bargaining power with China," says Wong.

"China doesn't want a trade war and repeatedly says it's better to go back to the negotiating table, and I think both sides realise that a trade war will harm them both."

Edwardo Erni, Kerry Logistics managing director for China and North Asia, agrees: "President Donald Trump has flip-flopped on similar promises in the past, so there is a good possibility that the present talks are just both sides posturing for better trade negotiations."

According to Erni, the proposed tariffs could potentially impact Apex Logistics, the transpacific forwarding specialist, and Kerry Logistics member-company based in San Francisco.

"However, as we increasingly expand our domestic service capabilities within China, and grasp opportunities along the Belt & Road Initiative trade routes, overall business in China will be minimally impacted," he adds.

Erni and Wong's analysis may be proved correct. China's president, Xi Jinping, eased trade tensions with a speech in Hainan, the southern island province earmarked for a free-trade zone. Xi promised to lower import tariffs on cars and raise foreign ownership limits in the automobile, shipbuilding and aircraft sectors.

For the time being, China's economy appears unaffected by all the tariff talk. According to FocusEconomics, China

started the year on a solid note, with GDP expanding 6.8% for the third consecutive quarter.

"Along with robust GDP growth, the economy continues its re-balancing towards a more sustainable economic model – services and private consumption are clearly becoming the main engines of growth, at the expense of investment and manufacturing," noted FocusEconomics head of economic research and China economist Ricard Torné.

One offshoot of worsening trade relations with the US could be an acceleration of the Made in China 2025 initiative. The policy aims to make the country more self-sufficient and less reliant on foreign technology in key hi-tech industries

However, he says, the main risk to China's stellar economic growth is the worsening trade relationship with the US, which could hit the "all-important external sector". Nevertheless, Torné expects China's economy to expand by 6.5% this year.

Another risk is China's ballooning debt. With a debt-to-GDP ratio now at 300% – up from 160% a decade ago – a debate has raged among economists over the fragility of China's \$14 trillion economy. For Wong, a key consideration is the Chinese

government's apparent recognition of the soaring debt levels and the fact it is taking steps to keep it at bay.

"For example, if you look at the local government debt problem, the central government has already started to regulate it, to manage it and keep it under control and make it more transparent," he explains.

Wong says China's industrial output performed well in the first quarter, growing by 7.2% in real terms – a faster pace than 2017. Exports showed "phenomenal growth" he adds, increasing in US\$-terms by 20% due to strong demand in the US, Europe and Japan.

Wong described the shift of low-end manufacturing away from China's coastal cities as an irreversible trend – albeit one which could be slowing down.

"More and more production facilities are being moved out, not just from the coast to inland provinces, but also out from China into South-east Asia and Bangladesh.

"But having said that, according to an HKTDC survey of Hong Kong manufacturers operating on the mainland, the majority said if they wanted to move they have already done so."

The most sophisticated products in garments and footwear are still processed in the Pearl River Delta region, Wong notes.

One consequence of increased final product assembly in South-east Asia is more upstream textiles and raw materials shipped there from China. According to the latest DHL Global Trade Barometer, China's imports and exports of industrial raw materials both saw major increases in March, upping its ocean and air freight volumes for the quarter.

"We've also begun to see the effects of 'Made in China 2025' on China's trade footprint, driving up production of hi-tech goods locally at the expense of imports," says Steve Huang, chief executive of DHL Global Forwarding Greater China.

"We can expect sectors like information technology, robotics and biopharma – along with more prosaic items like personal and household goods – to experience a relatively rapid shift into net export territory, alongside a continued rise in imports of the raw materials necessary for production."

Indeed, one offshoot of worsening trade relations with the US could be an acceleration of the Made in China 2025 initiative. The policy aims to make the country more self-sufficient and less reliant on foreign technology in key hi-tech industries.

While the initiative was launched in 2015, it has become more significant since Trump's election. For example, in a move that would seem contradictory to Washington's goal of reducing the trade deficit with China, in April the government banned US companies from selling components to ZTE, the smartphone manufacturer and one of China's biggest tech companies. The ban will last seven years and is tied to a breach of US trade sanctions on Iran. And it's not just ZTE that Washington's targeting, it has also blocked a number of acquisitions of US assets by Chinese tech companies.

Whether the primary goal is to protect and buoy the US domestic tech sector is uncertain, but Trump would no doubt enjoy bringing back some smartphone manufacturing to the US, and has offered tax incentives to this end. Apple's iPhone, for example, is mostly assembled in China by Taiwan's Foxconn. The manufacturing giant has potentially mitigated the chance of punitive taxes against US iPhone imports by building a \$10bn LCD display panel factory in Wisconsin, an investment worth up to 13,000 jobs to the local economy.

The US tariffs have so far targeted the same sectors China wants to upgrade via its ambitious 2025 plan, including computer chips, robotics, railways, green vehicles, renewables and medical devices. It may be too late to make an impact, however.

"China is undergoing a major shift in manufacturing," says Kerry Logistics' Erni, noting the potential upside for contract logistics.

"Made in China 2025 is stimulating growth in hi-tech and manufacturing, such as robotics, IoT, 3D printing and 5-axis machining, which in turn is pushing demand for sophisticated and specialised supply chain management.

"The healthcare and pharmaceutical vertical is also undergoing a bloom. China is reforming its healthcare system, which will require a major infrastructure and equipment overhaul, followed by high growth in peripheral industries. Aided by policies requiring a higher level of quality control on the supply chain management of products, the involvement of 3PL players will undoubtedly increase."

One belt, one road for China



Photo: © Hakule | Dreamstime.com

Closely linked to China's 2025 manufacturing blueprint is its marquee economic policy, the Belt and Road Initiative (BRI).

In March, China amended its constitution to abolish presidential term limits, securing the way for Xi Jinping to remain in power for life. Xi is the architect and orchestrator of BRI, and with his continued leadership no longer in doubt, the policy is expected to remain the driving force behind all of China's economic decision-making.

The key to understanding BRI is the Chinese government's disposition towards long-term economic planning. BRI has no end date – no 2025 or 2035 name tag – just a marathon-esque multi-decade vision to transform trade flows across Eurasia, the vast landmass once traversed by a silk-laden merchant named Marco Polo.

Stretching from western Europe to China's east coast, Eurasia is the world's largest market and home to about 70% of the global population, 75% of energy resources and 70% of GDP. By facilitating new economic corridors of interlinked transport and logistics infrastructure, China hopes to increase trade among the 60 BRI-countries from \$1 trillion to \$2.5 trillion within the next decade.

But it's more than just a network of so-called New Silk Roads that China is aiming to create. Yes, new railways, highways and ports are key to the "Belt & Road" concept – coined to describe both the overland and the maritime routes between Europe and Asia – but energy infrastructure and economic integration through new, non-western

controlled financial institutions are also major pillars of the policy.

It's China's all-in-one solution for energy and trade security, combined with a loosening reliance on the US dollar, which, as we've seen so far this year, is a pressing concern for the Chinese. Or, in short, BRI is China's attempt to shape how Globalisation 2.0 will unfold, with all roads leading to the Middle Kingdom.

"BRI is a very important issue for China as well as Hong Kong," says Wong of HKTDC.

"It's another round of globalisation and another round of 'going out' for Chinese companies. By developing more close economic relationships with economies along the 'Belt' and along the 'Road', it creates more opportunities for mainland companies to cooperate with other economies in terms of their production and their market."

Historic bridge

Wong sees Hong Kong as an important enabler for BRI, a kind of historic bridge between the mainland and its foreign trading partners.

"Hong Kong has always been an international business platform for China, so if BRI brings another round of globalisation then it will definitely play a more important role in years to come. Hong Kong is very active and enthusiastic about BRI."

Indeed, BRI could rejuvenate Hong Kong's maritime logistics-based economy, following years of intense competition from opposing ports in the Pearl River Delta. While the ground lost

on container throughput is unlikely to be recovered, Wong says Hong Kong is fast-developing its maritime services economy.

Hong Kong's enthusiasm for BRI is encapsulated by Kerry Logistics, its largest home-grown 3PL.

"In our view, BRI is a complete game-changer in Asia, and we believe China has the means and motivation to achieve its vision, which will transform the logistics industry in Asia," says Erni.

"BRI is opening tremendous new opportunities. With enhanced infrastructure in Central Asia, and new tradelanes connecting China and South Asia to Europe and the Middle East, it is hard to understate the dimension of the new markets and trade routes that will be sparked."

Major projects under the estimated \$100bn-plus BRI-umbrella include the fourth Central Asia-China gas pipeline; Malaysia's East Coast Rail Link; the China-Laos-Thailand railway; oil and gas pipelines connecting Myanmar with Yunnan province; and the expansion of Pakistan's Gwadar Port, part of the controversial China-Pakistan Economic Corridor that includes new highways, railways and power plants

However, perhaps the most symbolic aspect of BRI so far has been the new pan-Eurasian rail routes, such as the train that traversed 12,000km over 18-days from Yiwu to London last year, and the launch of the first rail service connecting China to Tehran.

It's not just headline grabbers like these capturing the imagination – Asia-Europe rail volumes have been

skyrocketing. Kerry Logistics is moving 200-300 teu a week through its twice-weekly block-train service from Lanzhou, to Kazakhstan and Uzbekistan, via Alashankoy or Khorgos, the fast-emerging rail transshipment terminal and industrial zone.

A new city

Located in a once-barren region near Kazakhstan's border with China, Khorgos Gateway and the 5,000 acre Khorgos East Gate Special Economic Zone deserve special mention in the context of BRI and its power to transform the logistics and economic landscape. Indeed, a whole new city, named Nurkent, is popping up next to Khorgos to support it.

Trains from 27 Chinese cities are consolidated at Khorgos, where the rail gauge widens, before leaving again for 11 European destinations via 10 separate railways. Khorgos is already handling some 100,000 teu and is on track to reach its 540,000 teu target capacity by 2020, following investment by COSCO Shipping and the port of Lianyungang which took a 49% stake in the facility.

"One direct result of the BRI is a renaissance of a nascent rail transport market through Central Asia," explains Erni.

"While railways are built to many different standards across Asia, newly built rail freight infrastructure, such as railway and high-volume cross-docking facilities, is pushing for more standardisation and opening of new transport options. Rail freight is much faster than sea freight and cheaper than air freight."

Kerry Logistics also operates a

100-teu-a-week freight service from Yinchuan to Kazakhstan and Uzbekistan.

Erni adds: "In the pipeline is a monumental multimodal land-rail service from Lanzhou, China, through the Himalayas, via Sost, and down to Islamabad and Gwadar, Pakistan. The upgraded overland route will require only 10 days, with volumes expected to reach 1,000-1,500 feu a year, spurred by demand for industrial goods, building materials and commodities."

The fast success of Khorgos is indicative of exceptional Asia-Europe rail freight growth over the past few years. According to data from Sinotrans, there are now about 2,200 block-trains running between China and Europe each year, up from just 307 in 2014. They forecast 5,000 block-trains a year by 2020, equivalent to 500,000 teu.

The Asia-Europe railways pre-date BRI, of course, with the likes of Hewlett-Packard and Dell developing 15-day block-train alternatives to slow sea freight and costly air cargo. Since then, Chinese central and local government subsidies, combined with a plethora of eager service providers, have ensured the rail networks' impressive volume growth.

Crucially, eastbound cargo volumes will need to increase to ensure the railways are viable without subsidies. And there are already European shippers of luxury groceries, meat and dairy products using these new silk roads to reach the massive Chinese market and expanding middle classes there.

According to consultant and BRI-doctoral candidate Andre Wheeler, the



Trains from 27 Chinese cities are consolidated at Khorgos where the rail gauge widens, before leaving again for 11 European destinations via 10 separate railways

subsidies were due to end last year but were extended indefinitely.

“China Rail claims that break-even for the network would be 10,000 freight train Eurasian trips,” says Wheeler.

“There’s currently 7,000, with the objective to get to 10,000 and 2m teu by 2021, with the overall objective to move up to 20% of trade by volume via train, which is currently only at 1.5%. So the volume is there to make it viable and we can expect subsidies to continue to at least 2021.”

There are of course more BRI-implications for logistics service providers than just the rail freight boom. For example, Kerry Logistics is developing cross-border trucking operations between China, Kazakhstan, Azerbaijan, Georgia and Turkey.

“The project is progressing so quickly that we are forced to consider increasing our fleet size much sooner than anticipated,” says Erni. “We are capitalising on the developments stemming from BRI, which we believe will be the fulcrum of a pivotal transformation in freight and trade in Eurasia. Our recent acquisitions of Globalink Logistics in Central Asia and Lanzhou Pacific Logistics in China, enable us to benefit from the trade

development in - and through - the region.”

DB Schenker is another multinational 3PL bullish on BRI and on the expansion of cross-border trucking. Schenker China chief executive Thomas Sørensen says he expects BRI to boost intra-Asia trade.

“BRI is opening tremendous new opportunities. With enhanced infrastructure in Central Asia, and new tradelanes connecting China and South Asia to Europe and the Middle East, it is hard to understate the dimension of the new markets and trade routes that will be sparked”

“It is already one of the world’s most extensive cross-border road systems connecting China with key economic cities in South-east Asia such as Hanoi, Bangkok, Kuala Lumpur and

Singapore,” he claims.

For Sørensen, BRI represents a “very promising development” for logistics services, given that it will spur demand in China’s less-developed western and northern provinces, where it can take three to five days to transport containers to a sea port.

“Many of the cities there are still isolated, with partly poor infrastructure setup. Thanks to the programme they will get enhanced access to the global market and will be able to develop their local economies and boost trading relationships with overseas countries. Hence, the cargo flow out of and into China and the need for logistics solutions will increase significantly,” he says.

One challenge of BRI will be the increased competition, Sørensen notes.

“China’s logistics market is already highly fragmented – there’s an estimated 790,000 road transport companies in China but the top 20 only account for less than 2% of the market share.

“Since BRI was announced some years ago, even more logistics providers – global and local ones – have been entering the market.”



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Economic might reshaping global shipping

Another, broader consequence of BRI for logistics could be a derailing of the shipping industry's drive towards ultra-large containerships. Consultant Andre Wheeler contends this is the likely result from China's 'west coast solution' for trade with Europe, the Middle East and Africa.

"The focus is to find alternative freight routes that bypass the Malacca Straits choke-point, including the likes of Singapore," he says.

"Within this is the development of new port-rail network pairings, together with hub-and-spoke freight corridors that facilitates China repositioning economic development from the coastal cities to inland locations."

As an example, Wheeler highlights the BRI-led development of rail connections in Africa, including the newly opened Ethiopia-Djibouti and Mombasa-Nairobi railways.

"These projects pair ports with rail and road, and build integrated infrastructure to make it happen, including bridges and electrification".

Ethiopia is an interesting example of China's experiment in outsourcing low-end manufacturing, as the policy slowly extends out of South-east Asia to reach Africa. According to a recent report by Bloomberg, Chinese manufacturers are investing heavily into outsourcing fast-fashion manufacturing in Ethiopia, including the building of several industrial parks such as the \$250m facility in Hawassa.

Meanwhile, according to Wheeler, this port-rail strategy also facilitates the move from port-to-port to door-to-door cost considerations – as with online retail – by providing the necessary logistics infrastructure for smaller and more regular deliveries. Furthermore, it allows China to access new manufacturing hubs whilst also addressing the looming emissions control area issue, since rail freight has lower emissions than shipping.

He says: "Finally, it addresses China's transition from pure export dominance to a more balanced export/import economy, and a growing consumer class that will be more widely spread as inland development takes place.

"The effect will be to reduce the need for large ships to transport goods – for example, Chongqing is a major inland 'port' connected to eight maritime ports feeding product into and out of China for



"COSCO, in its role as the champion of China's maritime ambitions, is at the forefront of BRI investment decisions" – Bloomberg analyst Rahul Kapoor

strategic reasons. This will have the effect of reducing the need for large 20,000 teu ships and placing more focus on 10,000 to 14,000 teu vessels as China secures energy and trade security," argues Wheeler.

COSCO the key

Key to China's maritime strategy is COSCO Shipping. The newly merged state-owned container shipping and ports giant has been busy with overseas acquisitions, namely Hong Kong's OOCL and a string of European port terminals: Greece's prized southern Europe gateway, Piraeus; Belgium's second biggest port, Zbrugge; Spanish terminal operator Noatum; and a stake in Italy's Vado Ligure port.

"China has over the past decade come to a stage that its economic might has an outsized influence and is reshaping global trade flows and, consequentially, the global shipping landscape," says Rahul Kapoor, analyst at Bloomberg Intelligence.

"COSCO, in its role as the champion of China's maritime ambitions, is at the forefront of BRI investment decisions. A focused and leaner COSCO positioned for the market upturn can advance from years of capital destruction as it moves toward global domination after its OOCL acquisition."

While Kapoor doesn't think COSCO will overtake Maersk Line in top spot in the container line rankings any time soon, the completion of the OOCL takeover will see the carrier move into third position, ahead of CMA CGM.

The stage is set, then, for renewed competition between COSCO and the major European shipping lines, following the latest rounds of consolidation.

Further mergers and acquisitions among industry players are likely to continue, but there appears to be a new focus for the top carriers on digitalisation and integrated container logistics – a snazzy new term for doing business directly with shippers and providing more freight forwarding services directly.

For Kris Kosmala, vice president Quintiq Asia Pacific, it's COSCO rather than Maersk Line which may have the upper hand in providing door-to-door integration, arguing that the key battleground will be landside logistics acquisitions.

"If COSCO is the avatar of Chinese government investment strategy into dominating global logistics links, then COSCO will be in a much more flexible position to move quickly on promising targets," he wrote on *Splash 24/7*.

For its part, Maersk Line says its strategy to become a one-stop shop for global container logistics is designed to simplify its customers' supply chains in China and beyond, rather than replacing the role of forwarders and NVOCCs.

"Many industry players, carriers and NVOCCs, have identified the need in the market for end-to-end solutions," a Maersk spokeswoman says.

"Maersk is well placed with its ships, terminals and landside offerings to enable this, as well as offer more accessible online solutions and thus respond and contribute to the digitisation of our industry.

"It is not our view nor ambition that the companies under Maersk Transport and Logistics will cover the needs of the full logistics market. Instead we will, where it makes mutual sense, look to partner






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According to Maersk Line, China reported a 7.9% growth in exports last year and a 15.9% uptick in imports. Container cargo volumes reached over 200.3m teu.

“The US imports from Asia jumped from 3.7% to 5.5%, which helped increase volumes through Chinese container ports. Apart from the US increase, the trade with BRI countries is another main driver of export from China,” the spokeswoman says.

“The traditional labour-intensive industries and some high-value-added mechanical and electrical products and equipment manufacturing are the main power in growth. The increase in imports is not only contributed by consumer power but also by the stable domestic environment which kept the market looking positive.”

Chinese ports showed the strongest growth globally in 2017, the Shanghai International Shipping Institute reports, with Shanghai up 8.2% to over 40m teu, and Ningbo-Zhoushan Port and Guangzhou Port up by 14.2% and 8.2% respectively.

This upward trend may well continue throughout 2018, says Schenker’s Sørensen, who notes the global ocean freight market is expected to grow between 4.8%-5.1% this year, while container transport capacity is expected to grow by 5.8%.

“A balanced supply/demand situation is not expected until mid-2019 or even 2020. 2017 was a year of change in shipping. Freight rates went up and their volatility reduced, demolitions went down, and the idle fleet was partially reactivated.

Growth potential

“From Asia’s and China’s perspective, we see growth potential for all intercontinental tradelines, in particular within Asia and with the Americas. Increasing intra-Asia business is driven to a high extent by the BRI,” he says.

One challenge forwarders faced last year was port congestion in Shanghai, Shekou and Dalian. This was caused primarily by seasonal peaks and alliance restructuring, says Han Ning, Drewry director for China.

“However, Shanghai has capacity constraints, so any volume increase may cause congestion. And both Shanghai and Dalian had more bad

weather days in winter. On the other hand, Shekou’s congestion could be more of a trade boom,” she adds.

A recent Drewry report highlights how China’s new environmental laws are affecting container shipping. The analyst says a ban on the import of a variety of waste materials could cost carriers up to 5m teu in lost backhaul volumes. Furthermore, a crackdown in 2017 on heavily polluting factories caused supply chain disruption for some shippers.

“Last year’s factory closures brought fluctuations in the shipment volume,” explains Maersk’s spokeswoman, adding that decreased volumes of waste imports into China resulted in added volumes to South-east Asia, while finished paper from South-east Asia to China also increased, indicating a shift in supply chains.

“China’s increasingly stringent environmental rules may result in short-term uncertainty regarding China’s export in certain sectors.

“However, in the long term, it is expected that the environmental protection rules and implementation improves the quality of products made in China while creating a better environment for the general public.”

Anji-Ceva goes hi-tech to beat automotive slowdown

China’s automotive industry came under the spotlight amid April’s trade tensions with the US.

And in what could be interpreted as a move to address US concerns over the disparity between the two nations’ car import tariffs, China announced it would significantly cut its 25% duty on foreign-made cars and open the sector to full foreign ownership by 2022 from the current 50% limit.

However, for Wang Zemin, chief executive of automotive logistics specialist Anji-Ceva, the policy change will have little short-term impact, considering the 3PL’s extensive relationships with foreign companies already operating in China through joint-ventures (JVs).

Wang explains that Anji-Ceva provides complete automotive logistics solutions, including in-bound, ground transport, after sales, and import-export global forwarding for OEMs, with revenue “much bigger” than its second- or third-placed competitors.

China’s automotive industry is the largest in the world, producing over 20m cars annually. However, according to Wang: “The sector has gone from very fast double-digit growth to stable single-digits, less than 5% overall. What’s very important is that no OEMs have opened any new factories recently, only some small manufacturers focusing on greener vehicles.”

On the other hand, he says, ‘Industry 4.0’ intelligent manufacturing trends are creating new opportunities for 3PLs because “the cost structure is that more and more OEMs are willing to outsource more logistics activity that previously they did by themselves”.

Indeed, Anji-Ceva is investing in its own artificial intelligence



(AI)-based logistics solutions to meet this customer demand. For example, to optimise looping plans and loading capacity.

“We’re also using blockchain technology to organise our supply chain data and adapt further to intelligent manufacturing, transforming from a traditional logistics service provider into a more technical and data-driven company,” says Wang.

Last year Anji and Ceva announced an extension of their JV partnership for an additional 15 years, and agreed to expand their partnership to non-automotive contract logistics verticals.

“I think it’s good to diversify, because the China market is developing very well in terms of industrial markets, consumer goods retail, healthcare and hi-tech,” says Wang.

“It’s beneficial to combine our resources and expertise, as Ceva has a global footprint in these other sectors. Hi-tech and healthcare are moving fast – we’re paying attention and trying to find some linkage in terms of our resources and expertise in automotive and how we can leverage this.”

Eyeing the world's biggest e-commerce market

Maersk Line and other top-tier carriers are positioning for a slice of the ballooning e-commerce pie that's making waves around the globe. Last year the carrier launched a partnership with Alibaba to offer online bookings to small and medium Chinese exporters.

"China is an important market in Maersk's digital journey," its spokeswoman said. "On one hand, China contributes 30% of Maersk Line global business, on the other hand, China is the most developed e-commerce country, with two digital companies ranked global top 10 in terms of market value."

It's true that China's e-commerce industry is simply massive. The statistics are staggering – according to a report by China's Ministry of Commerce, online retail sales rose 32% in 2017 to breach \$1 trillion for the first time. On Singles' Day, November's famous shopping bonanza, Alibaba made a record \$25bn in sales.

Schenker China's Sørensen explains the significance of Chinese e-commerce and the impact of Singles' Day on the 3PL's operations.

"China accounts for 50% of the total worldwide e-commerce spend. Its e-commerce sales are projected to hit \$2 trillion by 2020, equalling those of the US, Japan, UK, Germany and France combined," he says.

Last Singles' Day, Schenker handled two million packages in 24 hours for an American retail customer, up from 300,000 in 2013.

"2,500 employees are needed to operate this huge volume within a given time frame. Every year, we contract and train a growing amount of temporary staff in order to seamlessly manage the increasing orders," adds Sørensen.

Significantly, China's rural areas accounted for a sizable chunk of last year's total e-commerce growth, with online sales outside the major tier-1 cities jumping 39%. The Ministry of Commerce says 28m workers are now employed by the e-commerce sector in rural areas.

Furthermore, the push to extend online shopping to the outer provinces has only just begun, says Zhi Zheng, managing director North Asia cluster, DHL eCommerce.

"We see that cities such as Guangdong, Zhejiang, Hubei and Fujian have increasingly begun to outspend their tier-1 city counterparts, such as Beijing and Shanghai," he says. "The potential in these cities is huge – they are where the



majority of China's population live and they have only just begun to start shopping online."

Zheng notes how growth in these cities is greatly aided by social media apps like WeChat, which have "helped to define the nature of e-commerce in China by greatly reducing the barriers to entry, allowing virtually anyone to start selling immediately". However, he cautions, the rising costs of domestic logistics and labour are putting pressure on retailers.

Alibaba and JD.com, China's first and second-largest online retailers – and their respective logistics units, Cainiao and JD Logistics – are leading this second-stage of the country's e-commerce revolution.

Technology-driven

Alibaba plans to spend \$15bn developing Cainiao's capabilities over the next five years, including building a technology-driven global logistics network that promises to deliver packages within 24 hours in China and 72 hours worldwide. Cainiao, which executes some 57m deliveries a day, plans to expand its warehouses and transport assets in rural areas to meet this target, including 40,000 pick-up facilities close to residential areas.

JD Logistics (JDL), on the other hand, attracted a \$2.5bn investment to expand in logistics automation, drone deliveries and robotics. In September, JDL opened its first fully automated

sorting centre near Shanghai, capable of handling 9,000 orders an hour.

Meanwhile, China's cross-border e-commerce sector is also undergoing a substantial trade boom.

Figures from China

Customs show an 80% year-on-year surge in cross-border

e-commerce in 2017, reaching \$14.3bn.

Kerry Logistics' Edwardo Erni says cross-border e-commerce trade with South-east Asia is driving growth.

"Kerry Logistics is running international line haul services for e-commerce parcels through a subsidiary. We experienced overwhelming demand from China to ASEAN countries, given that the traffic volume of this tradelane approximately trebled in 2017."

DHL eCommerce has also been busy expanding in South-east Asia. Zheng says demand for goods from Chinese sellers has steadily increased in the region, with most packages coming in the form of small parcels and light items.

"These sizes of shipments account for more than 50% of China's total B2C export orders. We also see that both merchants and consumers in both Chinese and South-east Asian markets tend to favour a direct shipping method."

DHL's operations are supported by three distribution centres, in Shanghai, Shenzhen and Hong Kong, which provide capacity for 100m parcel deliveries a year across Greater China.

Zheng says the biggest opportunity for cross-border e-commerce is the rise of regional platforms, such as Lazada in South-east Asia, Souq and

JollyChic in the Middle East and AliExpress in Russia.

"All are expected to have great development opportunities for Chinese merchants, allowing them to reach regional markets with relative ease."

At the same time, he says there are multiple challenges for cross-border trade, such as the period immediately after peak season.

"There exists a post-holiday selling slump, and in addition to slow sales, retailers also have to deal with a large number of returns."

New European VAT policy and regulations poses another challenge. Zheng says it is essential for sellers to understand and master the VAT processes and operations in order to enter European markets.

While traditional logistics players will no doubt be jubilant over China's e-commerce growth, both domestic and cross-border, a creeping wariness of increased competition is rearing its head.

Kerry Logistics' 2017 results showed a dip in its mainland China business due to "rising competition and cost". Erni says it is facing tougher competition from domestic players, including "some non-traditional companies pushing into logistics from peripheral industries like e-commerce and courier delivery".

Into the air

Related to this increased competition is the push by couriers into air cargo and the e-commerce-driven expansion of express fleets. SF Express, for example, is investing \$5.9bn to build a 2.45m tonne capacity cargo airport in Hubei province, central China.

The country's largest private logistics company already owns a fleet of 42 freighter aircraft, carrying over 400,000 tons in 2017. YTO Express also has its own airline, based in Hangzhou. Its subsidiary YTO Cargo Airlines operates seven freighters, with another 10 on order from Boeing.

Total express delivery volume reached 40.1 bn parcels last year, up 28%. While surging domestic e-commerce is responsible for much of this growth, China's express couriers are also launching international services in search of cross-border volumes.

SF Express says it wants to become the 'FedEx of China,' and the courier has already added international destinations across Asia, most recently with flights to Osaka, Dhaka, Hanoi and Ulan Bator. Regarding the latter, SF

says the China-Mongolia service will aid cross-border e-commerce "in the context of the Belt and Road Initiative".

Meanwhile, the global air cargo industry will be hoping China helps fuel another bumper year in 2018 following last year's stellar growth. According to Schenker China's Sørensen, so far the strong momentum for air cargo has carried over into 2018, with first-quarter volumes up 7%.

"In the first two months of 2018, we outperformed the market and were able to consolidate our marketshare gained last year, further strengthening our position as the number 2 air freight logistics provider in China," he adds.

Corrine Png, chief executive of transport research firm Crucial Perspective, says the air cargo market in China is performing well, particularly on international routes, and that this is due to hi-tech and e-commerce growth in central China.

"System-wide cargo traffic growth is trending at about 12% year-on-year and load factors have risen slightly. The airlines and airports based in the secondary cities in China are experiencing the fastest cargo traffic growth. Among the top 30 largest airports in China, Hangzhou, Tianjin and Shanghai airports' cargo throughput growth ranked the highest," she adds.

A spokeswoman for Cargolux, which has a dual-hub approach, with bases in Luxembourg and Zhengzhou, where its Chinese shareholder is based, saw a steady start to the year in China, with market demand showing signs of increasing from April onward.

"Rates continue to remain robust, as well as demand. Consequently our load factors remain at healthy levels."

No single industry vertical is leading growth, according to Cargolux, with demand up for many different products.

"Cargolux's focus is obviously on those products where premium rates are achievable: outsize, live animals, jumbo, pharmaceuticals, charters and shipments requiring special handling. We note that the demand for capacity for perishables is also increasing and we try to balance our loads to provide capacity to our customers."

New year hangover

Despite the apparently promising start to 2018, Qatar Airways Cargo acting chief officer for cargo Guillaume Halleux notes that, after an "exceptional" pre-Chinese new year, the market took longer to recover than expected after the usual slowdown.

"The big surprise for us, and for the market in general, is that the recovery post-CNY took a bit more time than expected," he tells *The Loadstar*.

"Normally volumes get back to normal after a couple of weeks, but it took more than that this year so March was just an OK month. April [data] for us will be the moment of truth, if April is back on track then we're on track for a great year, but if April is also a bit slow to recover – which is not normal – then we may have cause for concern."

Asia provides about 40% of the carrier's revenue, which adds a certain amount of risk if the Chinese market falters.



YTO Cargo Airlines operates seven freighters, with another 10 on order from Boeing

“So the only strategy you can have is to diversify, and try to develop alternative markets. Vietnam being the major one. We have doubled capacity there since the beginning of the year,” says Halleux.

He says another consequence of China’s market might is its power to push up freight rates among its regional neighbours.

“If China needs capacity it’s going to get it because it pays the best, for carriers the yields are one of the highest in the region. Therefore, as a snowball effect, the rates in the Philippines, for example, are also going up, not necessarily because the market is stronger but because access to capacity is becoming a competition between countries,” Halleux explains.

Qatar Airways Cargo is currently the number-2 or -3 air cargo carrier worldwide, according to Halleux, but its operations in China are limited due to traffic rights.

Current services include passenger flights to Beijing, Chengdu, Chongqing, Guangzhou, Hangzhou, Hong Kong and Shanghai; with freighter services to Guangzhou, Hong Kong and Shanghai.

Maxed out

“With that we have maxed-out our traffic rights authorisations negotiated between the State of Qatar and the People’s Republic of China (PRC).

“So for us, the growth for the moment is limited because we can’t add new cities or increase frequencies – it’s not the case for everybody. That’s why we’re relatively small in Shanghai with a daily passenger flight and only three or four freighters a week.

“I’d love to do 20 in Shanghai, but I don’t have the traffic rights.”

Operationally, he says, there is a challenge with congestion in Hong Kong while the industry awaits the third runway there. Elsewhere, flight operations are running smoothly, with no major issues with obtaining slots.

On the other hand, large increases to air cargo imports over recent years has come as a double-edged sword for carriers.

“10 years ago nobody would have expected it, but now you have a capacity crunch into Shanghai, into Beijing, into Guangzhou,” says Halleux.

“This is not a new development, but one that has progressed over the past few years, with imports of perishables, luxury goods and consumer goods

mostly from Europe and the US. And that, from an airline perspective, is absolutely great because it makes our rotations profitable both ways.”

Last year’s growth and subsequent tightening of capacity out of China has led to a shift in booking behaviour, says Halleux.

“What we’ve seen this year is a very strong move from all forwarders asking to move from soft-block mechanisms

to hard commitments. Some of them were even willing to prepay the capacity just to secure it from a cashflow perspective, so that is a very strong signal that the market is anticipating strong demand and no major moves in terms of new capacity.

“Then, consequently, yields are on the rise for sure. We had discussions with many of our global accounts and the price is on the upside, definitely.”

Cargolux is aiming high



The launch of China’s new cargo airline looks set to be delayed yet another year. Henan Cargo Airlines, the JV between Cargolux, HNCA, Henan Airport Group and Xinggang Investment Group, is now more likely to launch in the third quarter of 2019, rather than this year. CEO Richard Forson says the “processes involved have taken longer than anticipated”.

He adds: “We are working on it. We are talking with local branches of the aviation authorities in China about any additional requirements. One of the questions is to what extent the airline would have to have Chinese pilots? There is a significant shortage in China, and there are other technical issues.

“I don’t want to start in a low season, I’d rather launch in a peak. There will be a testing phase next year and then we’ll ramp it up.”

Cargolux had a good year out of its Zhengzhou (CGO) hub. Forson says: “There was scepticism regarding it initially, but the results speak for themselves”. And he argues that there will be sufficient volumes for both carriers.

“The Chinese government has stated that it wants to move more industry into areas without much economic activity, and CGO and Henan is one of those. It enjoys something of a ‘special status’.

He acknowledges, however, that Cargolux still trucks volumes to the airport, but says it is, in part, due to lack of cargo infrastructure at other airports.

“CGO has invested a lot in infrastructure – it’s not as simple, going elsewhere.”

But one risk is increased competition, he adds.

“There are many airlines looking at CGO because Shanghai is completely congested; there are no additional slots and you can’t fly charters there. Beijing too. So airlines are looking for alternatives. As CGO develops and volumes grow, other airlines will be attracted.”

While the year has started well, Forson says there is a possible cloud on the horizon.

“There is a geopolitical risk, specifically, the trade situation,” he said. “If it escalates, it will have an impact. US-China is such a big trade lane that I don’t think it could be mitigated by more flows elsewhere. For us, the risks are with textiles, electronics and consumables.

“It’s one of the uncertainties at this stage. There has been a softening of stances by both sides, but the global economy would suffer and it could reduce demand for US goods.

“A full-blown trade war is not something people would relish. The impact would be felt by all transport providers, as well as transporters of people. Profitability would start falling and then there’ll be cost-cutting.

“It’s not healthy for a truly global economy. No one wants to be isolated, they want to sell to the biggest market possible.”