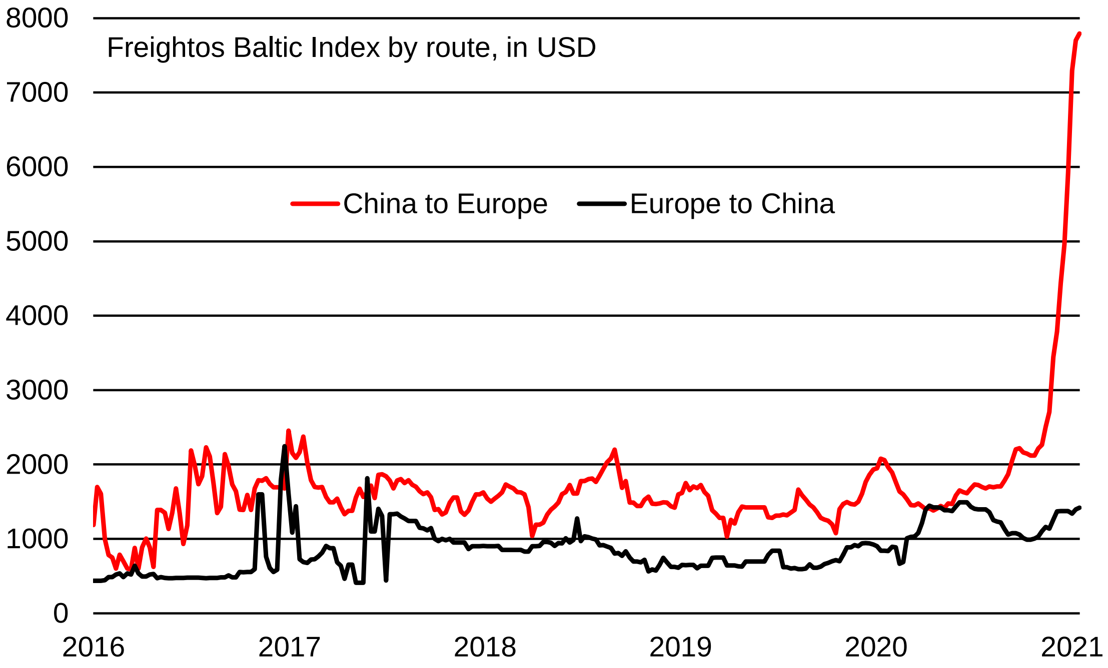
Freight costs of European companies soaring



Source: Bloomberg, UniCredit Research

- The costs of shipping goods from China to Europe by water have hit unprecedented highs recently. Since the start of November 2020, the Freightos Baltic Index for this route more than tripled by surging from about USD 2,100 to USD 7,800 at the end of last week. In comparison, the recent strengthening of the EUR-USD exchange rate by a couple of percent has literally been only a drop in the "ocean" for European companies.
- The Freightos Baltic indices summarize freight costs of so-called 40 containers which equal forty-foot equivalent units and are available for different routes. In contrast to goods coming from China, the costs of shipping goods from Europe to China have been steady.
- We think that there are two major reasons behind the latest surge in freight costs. And both are related to the pandemic and the second lockdown in Europe. First, demand of medical goods produced in China have been strongly rising. Second, and probably more important, consumers have been "reallocating" their demand even further. Instead of going to restaurants and traveling, they have been demanding more durable goods such as electronic equipment, furniture, etc. to have a nice home. And many of these (input) goods are produced in China.
- What are the macro implications for Europe? One could think of the effects for consumers, companies' supply chains and inflation. The good news is that consumers obviously do not bury their heads in the sand despite the difficult situation, as they keep on buying, at least to some part. The bad news have not materialized yet. Despite soaring freight costs and the renewed lockdown, business sentiment among eurozone manufacturers (PMI) has declined only marginally in January.

- Is a boomerang underway in the form of higher inflation for European consumers? China's share was about 20% of extra-EU imports in 2019 (latest available figure). For illustration, if one assumes that transport costs make, say, 5% of total costs, European import prices could rise by 2-3%.[1] However, this calculation only applies if shipping costs remain at the current high level over a longer period of time. And then there is still the question of whether and to which extent companies can pass on higher prices to consumers. As of today, only a moderate cost-push to consumer price inflation seems likely. But the pattern certainly needs to be closely monitored.

Dr. Andreas Rees, Chief German Economist (UniCredit Bank, Frankfurt)
+49 69 2717-2074
andreas.rees@unicredit.de

[1] UNCTAD estimated that freight costs were nearly 7% of the value of imports for developed countries between 2005 and 2014. For developing countries, it was roughly 10%; see UNCTAD (2015), Review of Maritime Transport, p. 55.

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j) UniCredit Bank Czech Republic and Slovakia, Slovakia Branch, Šancova 1/A, SK-813 33 Bratislava, Slovakia. Regulatory authority: CNB Czech National Bank, Na Příkopě 28, 115 03 Praha 1, Czech Republic and subject to limited regulation by the National Bank of Slovakia, Imricha Karvaša 1, 813 25 Bratislava, Slovakia. Regulatory authority: National Bank of Slovakia, Imricha Karvaša 1, 813 25 Bratislava, Slovakia

k) UniCredit Bank Romania, Bucharest 1F Expozitiei Boulevard, 012101 Bucharest 1, Romania. Regulatory authority: National Bank of Romania, 25 Lipscani Street, 030031, 3rd District, Bucharest, Romania

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UniCredit Research* — Macro Research

Erik F. Nielsen
Group Chief Economist
Global Head of CIB Research
+44 207 826-1765
erik.nielsen@unicredit.eu

Dr. Ingo Heimig
Head of Research Operations
& Regulatory Controls
+49 89 378-13952
ingo.heimig@unicredit.de

Head of Macro Research

Marco Valli
Head of Macro Research
Chief European Economist
+39 02 8862-0537
marco.valli@unicredit.eu

European Economics Research

Dr. Andreas Rees
Chief German Economist
+49 69 2717-2074
andreas.rees@unicredit.de

Dr. Loredana Federico
Chief Italian Economist
+39 02 8862-0534
loredanamaria.federico@unicredit.eu

Stefan Bruckbauer
Chief Austrian Economist
+43 50505-41951
stefan.bruckbauer@unicreditgroup.at

Tullia Bucco
Economist
+39 02 8862-0532
tullia.bucco@unicredit.eu

Edoardo Campanella
Economist
+39 02 8862-0522
edoardo.campanella@unicredit.eu

Walter Pudschedl
Economist
+43 50505-41957
walter.pudschedl@unicreditgroup.at

Chiara Silvestre
Economist
chiara.silvestre@unicredit.eu

Dr. Thomas Strobel
Economist
+49 89 378-13013
thomas.strobel@unicredit.de

International Economics Research

Daniel Vernazza, Ph.D.
Chief International Economist
+44 207 826-7805
daniel.vernazza@unicredit.eu

EEMEA Economics Research

Dan Bucşa
Chief CEE Economist
+44 207 826-7954
dan.bucsa@unicredit.eu

Gökçe Çelik
Senior CEE Economist
+44 207 826-6077
gokce.celik@unicredit.eu

Mauro Giorgio Marrano
Senior CEE Economist
+43 50505-82712
mauro.giorgiomarrano@unicredit.de

Artem Arkhipov
Head, Macroeconomic Analysis
and Research, Russia
+7 495 258-7258
artem.arkhipov@unicredit.ru

Hrvoje Dolenec
Chief Economist, Croatia
+385 1 6006-678
hrvoje.dolenec@unicreditgroup.zaba.hr

Dr. Ágnes Halász
Chief Economist, Head, Economics and
Strategic Analysis, Hungary
+36 1 301-1907
agnes.halasz@unicreditgroup.hu

Ľubomír Koršňák
Chief Economist, Slovakia
+421 2 4950 2427
lubomir.korsnak@unicreditgroup.sk

Anca Maria Negrescu
Senior Economist, Romania
+40 21 200-1377
anca.negrescu@unicredit.ro

Kristofor Pavlov
Chief Economist, Bulgaria
+359 2 923-2192
kristofor.pavlov@unicreditgroup.bg

Pavel Sobíšek
Chief Economist, Czech Republic
+420 955 960-716
pavel.sobisek@unicreditgroup.cz

UniCredit Research, Corporate & Investment Banking, UniCredit Bank AG, Am Eisbach 4, D-80538 Munich, globalresearch@unicredit.de
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