The High Cost of International Shipping

by Antonia Colibasanu - November 27, 2023

Though the cease-fire in Gaza has eased tensions in the Middle East, the prospects of a wider conflict still remain, and energy markets expect a new hike in oil prices accordingly. A new hike would make Russian oil all the more attractive to traders, especially since price caps prevent it from being sold for more than $60 per barrel.

This explains why, as European and American officials admitted, “almost none” of the shipments of seaborne crude in October were traded below the $60-per-barrel limit. Apparently, no actions were taken against shippers who moved oil above the price cap until last month. To address the matter, the U.S. Office of Foreign Assets Control started to implement sanctions on offending operators, blocking tankers from Turkey and the United Arab Emirates that allegedly disregarded the price limits. Three Greek shippers that had been delivering Russian oil for decades (and continued to do so after Western businesses abandoned routes to avoid running afoul of sanctions) have since **announced they would finally cease operations**.

Meanwhile, EU officials are **discussing new measures** that could better enforce the cap, by adding to existing mechanisms, requiring more documentation, or introducing a requirement for attestations to include itemized ancillary costs such as freight and insurance. The European Commission is also considering restricting Russia’s access to the used oil tanker industry.

These developments have added more risk and uncertainty for operators in the shipping industry who now have to adapt to evolving physical and legal security in international waters. The war in Ukraine had already made the Black Sea a high war-risk area, and after Moscow withdrew from a U.N.-brokered grain deal, Ukraine had to negotiate a public-private partnership with global insurers, an agreement reached on Nov. 15 to affordably cover ships carrying grain and critical food supplies. Even so, merchant vessels still need to exercise caution; a ship transporting grain was damaged by a mine in the Black Sea just a week ago.

Meanwhile, in the Eastern Mediterranean, ships bound for Israel face a 10-fold increase in war-risk premiums as the conflict in Gaza continues, prompting private operators to ask for government assistance. On Nov. 17, fearing strikes from both state and non-state actors active in the area, the International Maritime Security Construct and the Coalition Task Force Sentinel recommended that vessels make their voyages at night. They also recommended that vessels communicate to either the United Kingdom Marine Trade Operations or U.S. Naval Forces Central Command their movements ahead of time – or whenever there is reason for elevated concern. Owners and management have been additionally advised to make sure that sailors headed to Israel are informed of any potential security issues, and that shore leave is taken with local security in mind.

One of the most immediate challenges after the Ukraine war was a shortage of workers; Ukraine was a major source of seafaring laborers, many of whom were displaced by the conflict. Though the International Maritime Organization highlighted labor risks in 2022, it has yet to update them for 2023, so it’s unclear just how bad the shortages are. (Some estimates believe the number could reach 40,000 by 2025.) The situation in the Middle East is likely to make things worse. The Israel-Hamas war has generated a great deal of uncertainty for mariners, who are concerned with their own safety, and for shipping companies, which have to pay a premium for experienced workers. With a higher risk of damage in two important bodies of water, the price of insurance has soared, making overall operating costs all the more expensive. Coupled with the disruption in maritime trade routes, this means that cargo has had to travel longer distances to reach markets, which has already contributed to a volatile operating environment.

More, Western sanctions have given rise to Russia’s “shadow fleet,” boosting sales and transactions and raising the value of older vessels, particularly tankers. This has slowed the process by which ships are recycled and has spurred growth in new ship-owning corporations in China, the United Arab Emirates and India, with the goal of capitalizing on the large premiums connected with the new trade routes. In 2022, 864 new enterprises in the maritime industry were created with a link to or relationship with Russia. Of these, 87 maritime firms sport vessels that were previously Russian-owned or Russian-flagged. And 23 of them are UAE-based, while Turkey, Singapore and the Seychelles account for much of the remainder.

Before 2022, the International Maritime Organization had **described the shadow fleet** as a collection of gaining, high-polluting vessels with opaque ownership and sometimes unknown identification. While that definition still stands, and while vessels avoiding sanctions are mostly old and may frequently turn off their signals – ships may now be less confidential about their owners and IDs.

Also before 2022, tax policies, especially those associated with climate change, made shipowners flag their vessels under foreign countries, often under open registries. (This mostly affected developed countries.) The growth of open registries is associated with beneficial tax regimes and the ability to hire international crewmembers, allowing owners to reduce costs. In 2022, more than 70 percent of global ship capacity in dead weight tons was registered under foreign flags. Added to the growth of the global shadow fleet associated with Russia, this phenomenon has become only more pronounced.

Gabon is an interesting case study. According to maritime news outlets, Gabon's ship register has **doubled since the start of the war in Ukraine**. In May 2023, data from S&P Global showed that 98 percent of Gabon-flagged tankers above 10,000 dwt fell under Russian trade and shipping sanctions as high-risk vessels, or had no identifiable ultimate group owner. Little is known about Gabon's ship registry since the coup in August this year, but there is no indication that Russia or other sanctioned countries like Iran and Venezuela have stopped using it – on the contrary. At the same time, Russia has reportedly **used Mongolia's ship registry** to cover its oil trade from sanctions.

All of this points to an increasingly complex environment in which the demand for the shadow fleet creates little incentive for recycling but encourages the creative circumvention of legal restrictions. Second-hand vessels may be in demand, but flagging them under open registries means there is little accountability for their operations or safety. The more they are used, the more dangerous they are to the rest of the world fleet and, generally, to the environment.

In addition to flag registry, insurance is a key element in what makes the current shadow fleet tick. Two-thirds of Russian crude tankers are now insured by unknown or no-name companies, most of the time virtually lacking any insurance. Because they lack insurance and conceal their ownership, these tankers do not abide by international maritime norms. As they go offline and carry out shady ship-to-ship transfers – sometimes even in crowded areas like the Bosporus – they not only pose a danger to other vessels in the area but also accentuate just how little political will there is to act on this issue both in the industry and in the Western coalition.

All the while, pressure is growing on worldwide shipping. People still expect to receive their goods quickly despite the fact that the sheer distance of trade routes has fundamentally changed, and despite the fact that consumption patterns and energy markets frequently stymie efficient transportation.

It's a particularly difficult set of interconnected problems to solve, especially since trade policies (including sanctions) require more cumbersome checks, create new risks and complicate shipping routes. Taken together, these dynamics increase the complexity, volatility and uncertainty in the industry's operational and market landscape. The question of how shipping can adapt to these changes while maintaining the necessary capacity to efficiently ensure global trade and stable and predictable rates is a key concern for international businesses. The answer will determine how the global economy will evolve in the years to come, with major implications for global stability and the global geopolitical balance.

Author: Antonia Colibasanu

Read more from this author on geopoliticalfutures.com

