NEW ZEALAND
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Manatū Aorere

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European supply chain update – refocusing on reliability

MARKET INTELLIGENCE REPORT

Summary

Prepared by the New Zealand Embassy in The Hague with input from New Zealand embassies in Berlin, Brussels, London, Paris and Warsaw.

- Three years after the COVID-19 outbreak, supply chain issues are, at least in part, resolved in Europe. Shipping containers are available, arriving on schedule, and shipping prices have normalised. However, Russia's illegal invasion of Ukraine, cost increases, labour shortages and certain product shortages will continue to pose challenges. New sustainability-oriented regulations and a shifting focus from efficiency to resilience are reshaping European supply chains.

- Companies in the region have made changes within their supply chains to diversify production and focus on reliability in addition to cost efficiency.

Report

This report is an update to our Market Insights report: [Exporting to Europe: logistical challenges and how exporters can respond, November 2021].

Supply chain disruptions

During COVID-19 and post-Brexit, continental Europe and the United Kingdom (UK) experienced unprecedented disruption of international supply chains. Containers were scarce, costly and often arrived late. These issues are now mostly resolved and shipping markets have normalised.

Just as the COVID-19 related disruptions started resolving a year ago, Russia's illegal invasion of Ukraine led to an unparalleled set of economic sanctions targeting key sectors of the Russian economy. These sanctions placed new pressures on the region's supply chains, including price hikes, shortages, delays and congestion at key ports as they worked through the implications of the sanctions. The three largest ports in Europe (Rotterdam, Antwerp-Bruges and Hamburg) have reported a drop in throughput since the invasion.

Poland has had well-documented issues dealing with the surge of grain being imported from Ukraine. With Ukraine struggling to use its usual trade routes through the Black Sea, it is having to transport much of its grain through Europe. However, infrastructure challenges remain, such as capacity constraints in Polish ports and different rail gauges between Poland and Ukraine.

The ongoing aftermath of Brexit is still affecting European companies. Sources in the sector note that while the situation has mostly stabilised, there is more paperwork to complete, and that shipping still takes longer than it did previously.

There is broad consensus among industry representatives that companies need to make a strategic decision about warehousing. Some businesses are finding the need to have physical warehousing and distribution presences in both the EU and the UK in order to mitigate some of the procedural challenges and take advantage of the opportunities. This duplication adds costs.

Current supply chain challenges & shortages

Despite shipping prices being back to pre-COVID levels, further supply chain challenges can be expected. Rising costs, cyberattacks, labour shortages, and certain product delays and shortages are adding pressure.

The scarcity of qualified transport workers remains a challenge, with a shortage of 70,000 truck drivers anticipated this year in Germany alone. Vehicle procurement delays are also affecting EU companies, with trucks ordered 12 months ago only being delivered now, placing pressure on the existing fleet. The region's aging heavy transport fleet means higher maintenance costs and disruptions from periods of having vehicles off the road.

Some Dutch cities are planning to phase in emission-free delivery zones from 1 January 2025. This means company vans and trucks will have to be emission-free (likely electric) within these areas.

There are also supply chain challenges specific to fresh fruit and vegetables in some areas of Europe. There have been product shortages due to bad weather affecting crops in Europe and Africa, compounded by high energy prices limiting production, especially in the Netherlands. Dutch production has largely rebounded, however.

Moreover, from 1 June 2023 the largest supermarket in the Netherlands, Albert Heijn, has committed to not selling airfreighted fruit and vegetables, and now relies solely on product arriving via road and sea transport.

Cyber threats also remain prevalent. In June, pro-Russian hackers took down the websites for the port companies in Rotterdam, Amsterdam and Den Helder. The group "NoName057(16)" claimed responsibility. Media outlets reported that the attacks were a reaction to the Dutch intention to buy Swiss tanks for Ukraine. Such cyber-attacks can be costly as they can create disruptions, steal information and damage the reputation of the port companies.

Recalibration of European supply chains

Similar to the rest of world, Europe's supply chains pre-COVID largely focused on cost minimisation and just-in-time inventory management with limited focus on resilience. The COVID-19 pandemic and the ongoing war in Ukraine, along with the practical implications of Brexit, forced many European companies to adjust their supply chain strategies to 'just-in-case', meaning companies were trying to get their hands on as much inventory as they could.

Sources in the sector said by the end of 2022 warehouses were full and the just-in-time concept was effectively frozen. This was normal for times of uncertainty and risk, when inventory levels typically go up. Some industry representatives do not think the region's supply chains will go back to a pure just-in-time. These representatives suggest there could be a hybrid approach, balancing cost-efficiency with greater reliability and security. The extent of this rebalancing would depend on the sector: for some sectors there would be no choice but to focus on cost.

Nevertheless, recent reporting suggests that two thirds of Dutch companies intend to recalibrate their supply chains. 71% of Dutch companies plan to operate more locally, and similar numbers are observed across Europe. Consultancy firm EY reported in its 2023 attractiveness survey that 52% of European companies are redesigning their supply chain to create more regional-based supply models.

Industry representatives have noted an emerging trend of companies bringing production to Europe. Recent announcements of new manufacturing plants in Poland from Japan and US firms such as Intel (semiconductor chips), Pepsico (potato chips and snacks) and Daikin (heat pumps) suggest it is increasingly becoming the factory of Europe.

Sources in the sector also said Portugal was recapturing some of its earlier market share in clothing and footwear manufacturing. In 2022, the Portuguese textile industry registered a 17% export revenue increase from pre-pandemic levels to €6.1 billion. Fashion brands are increasingly attracted by the local industry's skilled but competitive workforce and proximity to market.

Sustainability – EU regulations

Earlier this year the European Parliament and Council approved a law to ban the sale of new fossil fuel-powered cars and vans from 2035 and from January 2035 emissions from trucks must be reduced by 65%. This vehicle fleet transition will impact European countries and supply chains differently. For example, Poland has the largest road transport sector with 19% of European trucks.

The EU is also expanding its emissions trading scheme (EU ETS) to cover additional sectors of relevance to supply chains. Shipping emissions will need to be reduced by 6% by 2030, and by 80% by 2050. Aviation has also been included in the EU ETS, requiring 2% of jet fuel to be sustainable by 2025 and 70% by 2050.

Potential implications for New Zealand exporters going forward

New Zealand importers and exporters will be aware that despite shipping prices returning to more normal levels, supply chain challenges remain. Unfortunately, these current challenges will continue for some time, and a return to a pure cost minimisation and a global just-in-time inventory management with limited focus on resilience should not be expected.

Exporters are therefore looking to strike the optimal balance between 'just-in-time' and 'just-in-case'. While inventory is 'money on the shelf', exporters are also seeking to meet consumers' expectations of reliability and sustainability.

With regards to Brexit, exporters will need to make the strategic decision if they want to have physical presence in both the UK and the EU, balancing the increased cost with opportunities to minimise UK-EU border disruptions and delays.

We are seeing many companies looking at the Netherlands as a European logistics hub and the new gateway to Europe, given its transport connections, English-speaking work environment and favourable tax policies. Exporters are often also using third party companies for their supply chain management. In the Netherlands, the Holland International Distribution Council, a private, non-profit organisation assists companies to set up European supply chains.

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