

Failure to Launch

How Vietnam's once promising container future was scuttled by poor port planning and an ill-timed economic downturn.

By ERIC JOHNSON



Editor's note: The cover story of the December 2007 issue of American Shipper chronicled the potential of Vietnam as a sourcing location for containerized cargo. The country was a couple of years away from seeing the opening of its first deepwater port complex in Cai Mep, a development that seemed to herald big growth in container volume as it positioned itself as an alternative to China. American Shipper subsequently looked at Vietnam in greater depth in a two-part series in early 2009. The following article represents an attempt to capture what has happened since.

It appears that the last five years have been a missed opportunity of sorts for one of Asia's rising giants.

As the world grappled with a historic recession and reduced cargo demand, Vietnam stood on the cusp of an exciting new era. In 2010, for the first time ever,

shippers in Vietnam would have access to deepwater ports that portended container volume growth through more efficient terminals and expanded liner carrier capacity.

Foreign direct investment flowed into Vietnam, as did logistics companies, terminal operators, and ocean carriers. The thinking was that multinational shippers would come as well, enticed by a veritable beehive of cargo-related activity.

The thinking was sound — Vietnam offered a legitimate alternative sourcing option to China, whether as part of a China-plus-one strategy or as a primary sourcing location in its own right. China's real estate, labor, and energy costs were on the rise,

and the Chinese government was actively trying to shift some of its low-cost export production to neighboring Asian nations as it focused on manufacturing higher value export goods.

In January 2010, the deepwater container terminal complex called Cai Mep (also called Cai Mep-Thi Vai, or sometimes Vung Tau) opened, and the possibilities seemed limitless. Finally, there was a way for shippers manufacturing in Vietnam to ship goods direct to markets in North America and Europe on large vessels using modern container terminal facilities. Previously, shippers in the south of Vietnam had relied on a network of smaller river terminals around Ho Chi Minh City that catered only to feeder vessels, predominantly from Singapore.

As any shipper surely knows, using feeders and transshipping cargo results in higher costs and longer transit times. The lure of bringing direct mainline services to Vietnam was easy to understand.

By mid-2011, no fewer than 14 direct services to North America and Northern Europe were calling at Cai Mep's terminals. Carriers clearly saw the potential and sought to capitalize on it. Vietnam's promise was especially attractive given carriers were still recovering from a bloody 2009 that drew containerized cargo demand levels down to 2003 levels.

But something happened to Vietnam's inexorable rise. Things have stalled a bit. This is not to say that containerized cargo volume in Vietnam has failed to grow — according to statistics from the Vietnam Seaports Association, total throughput at Vietnam's ports rose 18 percent from 2010 to 2012 (the latest year for which the VSA provides full year numbers).

Perhaps more indicative of Vietnam's prowess as a container cargo provider to consuming nations, U.S. containerized imports from Vietnam rose 14 percent in that same timeframe, according to Datamyne. Last year, roughly 590,000 TEUs of cargo was imported from Vietnam to the United States, about 26 percent higher than in 2010 (the year Cai Mep opened).

So there is growth, but it's not explosive growth.

A deeper look tells the tale. For one, carriers quickly reduced the number of direct services to North America and Europe from Cai Mep, realizing that the demand was just not there to justify so much capacity. From 14 direct services offered in June 2011, there were only seven by June 2012. Over the last year, that number has settled at six, including only one to Europe. Cai Mep's utilization was at 18 percent in January of this year.

What gives?

According to a range of experts *American Shipper* spoke to, the problems are many. It's difficult to pin the slow growth, or poor capacity utilization at Cai Mep, on any one factor.

"There are five fundamental reasons for lack of ship calls at Cai Mep-Thi Vai," said John Isbell, vice president at the consulting group Starboard Alliance and former logistics director at Nike. "One, the government continues to operate inner-city terminals near Ho Chi Minh City that were to cease operations when Cai Mep became operational. Two, Vietnam, like most countries, has not regained the export volume levels that existed prior to the global economic recession. Three, the fragmentation and lack of inter-terminal connectivity between the various terminals in Cai Mep-Thi Vai also inhibit the growth of transshipment volumes, as terminals lack sufficient scale and volume, while feeders would need to call at multiple terminals to cater to multiple line-haul services that call at different terminals.

"Four, cabotage rules limit the ability of foreign-flag carriers to carry containers between Vietnamese ports, including inter-

national cargo bound for other countries. And five, ocean carriers need subsidies from the government to cover pilot and terminal charges to call Cai Mep-Thi Vai terminals due to limited loadings."

Problems Run Deep. If that sounds like a lengthy laundry list, it gets longer the more people you speak with.

"Really, it highlights the need for good port master planning and execution," said Jonathan Beard, global lead for ICF's ports and logistics consultancy team. "It also indicates the investment risks faced by major international operators, even in high growth markets."

To Beard, the key problem is the river terminals near Ho Chi Minh City. Cai Mep is a roughly two-hour drive from the country's largest manufacturing cluster in and around Ho Chi Minh City. The plan, as Isbell alluded to, was for the network of inner-city feeder terminals to gradually close as services (both mainline and feeder) shifted to Cai Mep. But that hasn't happened.

The inner-city terminals remain full and very much open, and that's because there remain distinct advantages for traditionally

Top U.S. imports and exports from Vietnam 2010-14

(In TEUs)

Imports	2014*	2013	2012	2011	2010
Furniture	62,340	228,460	209,218	169,744	167,093
Apparel	29,267	106,258	93,135	85,513	89,309
Footwear	17,400	57,499	41,811	41,172	35,390
Seafood	5,514	19,318	16,612	14,287	10,569
Nuclear reactors/machinery	3,970	13,615	13,528	11,671	12,223

Exports

Cotton	1,031	5,643	1,347	7,914	7,539
Wood	1,244	3,292	5,626	4,764	2,560
Oil, seeds and grains	294	2,585	940	751	1,725
Fruits and nuts	214	2,266	1,513	926	1,117
Iron and Steel	58	1,236	738	834	589

U.S. import volumes from Vietnam 2010-14

(In TEUs)

	2014*	2013	2012	2011	2010
Imports	170,246	589,914	535,042	471,317	468,072

Notes: Ranked by full year 2013 volumes.

*2014 (thru April).

Source: Datamyne.

risk-averse shippers in using those terminals despite the need to transship.

"Later cut-off times, since boxes can be trucked directly or barged in shorter time," said Abraham Elias, head of commercial (Southeast Asia cluster) for the liner carrier APL. "Lower trucking costs because factories are located closer. Two-way trucking and frequency to and from river ports mean trucking companies can offer competitive rates."

Elias said carriers would obviously prefer to deploy larger vessels to serve southern Vietnam.

"Generally, the preference is to call larger ships, given the economies of scale and availability of bigger-size ships which cater for lower slot costs," he said. "Further, Cai Mep offers more schedule flexibility as vessels are not subject to navigation restrictions — for example, no waiting required because of tide or night navigation."

"However, as shippers prefer to export out of river ports, it is a challenge for carriers to provide a similar service in Cai Mep. Regional port-to-port operators will continue to serve river ports directly, and they will have an advantage. On the other

hand, for some trades, it may be better to serve over a relay port. For example, a U.S. East Coast connection over Singapore if a direct call at Vietnam is not justifiable because of insufficient cargo or schedule considerations," he explained.

A port advisory expert said the carriers' troubles arose from a market with too many providers and mismatched demand.

"The main line services deployed vessel sizes of 8,000 TEUs and above," said Jason Chiang, director and Southeast Asia specialist at Drewry Maritime Advisors. "These vessels were too large to call at the terminals in Ho Chi Minh and called at Cai Mep exclusively. The container shipping market in South Vietnam is fragmented, with multiple shipping lines without a dominant shipping line. This made economic sense for the shipping lines to use smaller vessels with higher utilization to serve South Vietnam instead of the larger vessels. In addition, the cargo that is handled through Cai Mep would have to be barged back to Ho Chi Minh City as the final destination is nearer to the city. The cost of barging is borne by the shipping line. Thus, the shipping lines have switched back to using smaller feeders (in the 1,000- to 1,500-TEU range)."

Regression To Feeders. But this demand-driven regression back to transshipment at Singapore or Kaohsiung is precisely what the Vietnamese government, and a handful of terminal operators, wanted to avoid when Cai Mep began operations.

Isbell noted though Cai Mep is nowhere near capacity, it still provides shippers in Vietnam with an option that doesn't exist for those in other burgeoning Southeast Asian nations.

"Deep-water terminals at Cai Mep-Thi Vai enable Vietnam to have direct line-haul services to Europe and North America whereas competitors like Indonesia, Bangladesh, and Myanmar have to rely upon more expensive feeder services," he said. "Some ocean carriers have been able to reduce the transit time from Cai Mep-Thi Vai to Los Angeles by three days."

Indeed, Beard noted the terminals in Cai Mep are "operationally fine, just struggling to get the volumes." In many ways, the problems are similar to other port cities in Asia where authorities have wanted services to migrate away from the city center to more modern, operationally efficient terminals outside the hustle and bustle of the metro centers. It has worked in Shanghai due to government dictate, less successfully so in South Korea's Busan and Bangkok, Thailand.

Chiang said only three of the seven ter-



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minals in Cai Mep have regular container services, with the others switching to handle non-containerized cargo, including general freight and even passengers. Four other planned projects are on hold indefinitely, awaiting demand that may not come for quite some time, if at all.

As *American Shipper* wrote in its March 2009 issue, “each terminal is being built seemingly as if many of the others don’t exist, a development that very well could cause overcapacity in the short term.”

Overcapacity Predicted. APL, for its part, predicted this rash of overcapacity in a report it released in 2008. The report noted that container volume in Vietnam grew 20 percent a year between 1995 and 2006. If it had continued at 20 percent annually through 2013, the country would be under-capacity for container throughput by this year. Clearly, that hasn’t happened.

“The volume projections were based on higher growth estimates, the assumption that the river ports will gradually be scaled down and the volumes moved to the deep-sea port, and also the expectation of more direct services to Europe and the U.S.,” Elias said.

Indeed, Elias said while Cai Mep is underutilized, the Ho Chi Minh City river terminals are full. To drive the migration that had originally been planned, he suggested the government ease future expansion of river ports, migrate volumes from

river ports to Cai Mep, and encourage more transshipment of northern Vietnam cargoes over Cai Mep. The latter move would imply allowing foreign carriers to transport boxes up north or down south and vice versa.

Elias also suggested incentivizing carri-

ers to use Cai Mep for intra-Asia, a move that is too costly for carriers at present, with stevedoring rates 20 to 30 percent higher than those at river ports.

“Port call charges are also high in Cai Mep, even by regional standards,” Elias said.

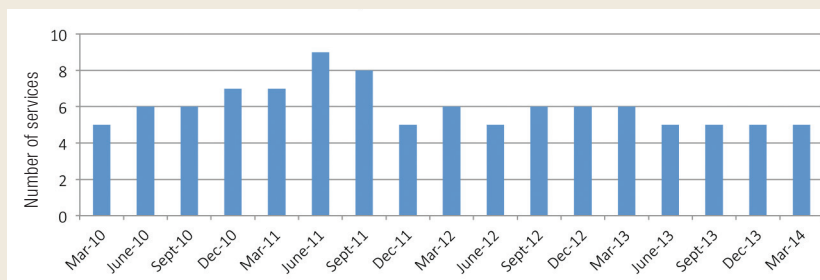
Terminal operators at Cai Mep have dubbed the situation “dire,” according to Chiang. A *Bloomberg* article in March cited figures from Seaports Consultants Asia that pegs the joint losses for terminal operators at Cai Mep at \$1.5 billion. Improbably, the seventh of the terminals at the complex opened in December, despite the other six terminals struggling for business.

Question Of Planning. Beard said the problem could have been sorted during the planning stages if there had been a single authority with the power to oversee phased development of Cai Mep.

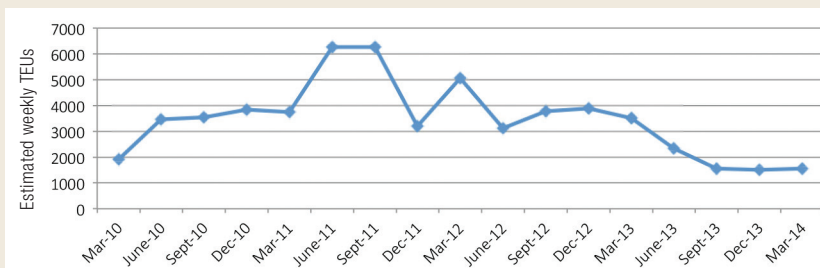
“Whether it’s a port authority that would have a coordinating role over that cluster, the reality is there have been conflicting decisions from local governments,” Beard said. “They needed to have a clear commitment as to what would happen to the city center terminals. Some triggers that once a certain threshold is met, the city center terminals close. But you can’t close them down until you’ve got decent landside infrastructure available.”

Beard said Cai Mep would be flourishing if there were three terminal operators

Services from Cai Mep to United States

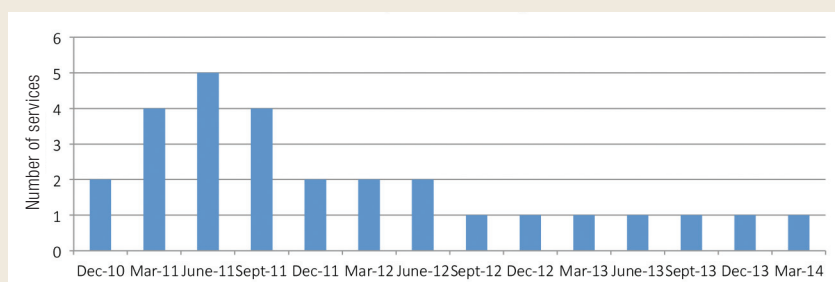


Weekly allocated capacity Cai Mep to United States

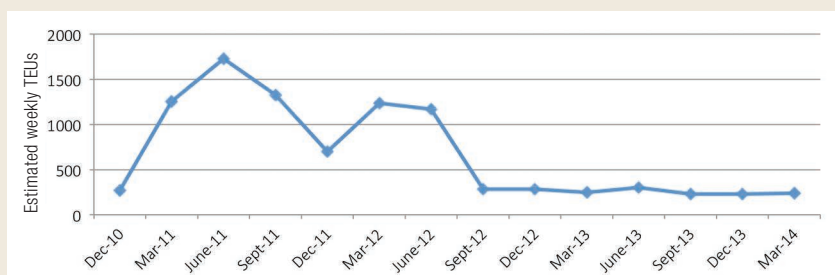


Source: BlueWater Reporting.

Services from Cai Mep to N. Europe



Weekly allocated capacity Cai Mep to N. Europe



Source: BlueWater Reporting.

(instead of the six there at present).

"Then you can regulate tariffs via competition," he said. "With one, you have to regulate, but the market can support more than one. Three is enough for competition and gives scope for operators to phase development and achieve economies of scale."

As things stand now, Beard estimates there is an overhang of 4 million TEUs of capacity.

"If you close down the city terminals, that disappears," he said.

But there has been progress on one front, according to Isbell.

"There has been a huge improvement in the roads in the Ho Chi Minh City area, along with new bridges and a tunnel under the Saigon River," Isbell said. "There is still some congestion at the major roundabouts in the Ho Chi Minh City area."

Indeed, five years ago, it was theorized that the only thing that could slow Vietnam's growth was inland infrastructure chokepoints.

"While there are certain highway sectors that are heavily congested and delaying freight shipments, overall, I think Vietnam's infrastructure is handling the current level of demand," he said.

In the north of Vietnam, Isbell pointed to a new modern express highway soon to open between Hanoi and Haiphong, the nearest port area to Hanoi. He also noted that the government is committed to bringing a new deepwater terminal at Haiphong (called Lach Huyen) online by 2016.

But investors are likely to be gun-shy to invest in Haiphong given the poor returns from their investment in Cai Mep. Isbell added that Vietnam lacks an efficient highway and rail network between Ho Chi Minh City and Hanoi, which limits the opportunity to increase manufacturing in central Vietnam.

Bright Spots. On the positive side, the government is beginning to embrace the idea of multimodal logistics.

Total Vietnam container traffic

(In TEUs)

	2009	2010	2011	2012	2013	% change 2009-2013
Imports	1,637,259	1,868,502	1,998,750	2,031,808	2,268,239	38.5%
Exports	1,519,642	1,738,147	2,000,307	2,371,882	2,593,784	70.7%

Source: Seabury.

"New industrial parks with modern warehouse facilities are being developed, primarily by foreign logistics services providers," Isbell said. "Some government officials in the Ministry of Transportation are beginning to talk about integrated multi-modal logistics concepts in terms of integrating logistics parks with major highways, ports, and waterways. Hopefully, multi-modal concepts like strategic freight corridors, (industrial parks built along major highways that would also be linked to ports by inland waterways and rail), will become part of future planning initiatives over the next five to 10 years. This will expedite freight shipments within Vietnam at a lower cost."

Isbell co-authored a 2013 study for the World Bank, *Efficient Logistics: A Key to Vietnam's Competitiveness*, that, among other things, described the underutilization of the Cai Mep terminals. One section, based on interviews with 25 international beneficial cargo owners, cited a number of reasons why shippers continue to use the river terminals around Ho Chi Minh City.

For one, most transshipment moves via the river terminals are competitive versus direct services from Cai Mep in terms of transit times. Shippers, as Elias noted, indicated the closer cutoff times to vessel departures, reduced drayage costs, and lack of restrictions on the hours containers can be drayed are also factors.

But the shippers interviewed for the study also pointed to operational problems at Cai Mep.

"(The government) issued operating licenses to foreign operators at Cai Mep-Thi Vai in a way that resulted in numerous small terminals and led to overcapacity," the study said. "The small footprint of each of the terminals is considered an impediment to smooth operations and quick container turnaround time."

The cabotage issue is also broached in the study, with suggestions from terminal operators that the government allow foreign carriers to handle transshipment cargo destined for northern feeder ports via Cai Mep. As of the time of writing the study report, no domestic feeder operators called at Cai Mep.

"The relaxation of cabotage rules for international transshipment containers would have little impact on existing Vietnam-flag carriers' share of the domestic market," the study found. "Instead, Vietnam forgoes port revenue at Cai Mep-Thi Vai as these international containers will be transhipped at hubs external to Vietnam."

Isbell chalks up Vietnam's failure to meet sky-high expectations to a simple dynamic that has changed little even as modern ports have sprung up.

"One reason why Vietnam is not meeting its potential as a source country is because it has not been able to develop the raw material supplier base in infrastructure that clearly gives China the advantage over (other Asian nations)," he said. "The vast majority of raw materials to manufacture export products in Vietnam still must be imported."

Still, Isbell said Vietnam's struggles must be seen within the context of the struggles of other nations in Asia after the 2009 economic downturn.

"Vietnam has not achieved its projected economic growth but that can be said of many countries in Asia," he said. "Vietnam has benefitted from the higher manufacturing and transportation costs in China. The question is how much of China's export production has shifted to Vietnam, Indonesia, Bangladesh, and Myanmar? The latter three countries have lower labor costs than Vietnam, but worse infrastructure."

So it's not yet long-term opportunity lost, but perhaps a short-term opportunity squandered. ■

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