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Advisory Panel on the Question of the Red Sea

The Red Sea Economic Crisis

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Hidde van der Ligt

Forum	Advisory Panel on the Question of the Red Sea
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Student Officer:	Hidde van der Ligt
Position:	President

Introduction

The Iran-backed Houthi militia, which rules over a significant part of Yemen, has been attacking multiple Western shipping vessels close to the Bab El-Mandeb Strait in the Red Sea since mid-November 2023. Major maritime firms have redirected their trade and ceased Suez transits in retaliation. Due to falling water levels, this diversion occurs while cargo at another maritime chokepoint, the Panama Canal, is declining.

The shortest alternate shipping route between Asia and Europe is to round South Africa via the Cape of Good Hope, a voyage that takes an extra 10 to 14 days. Due to rising fuel and insurance expenses, shipping rates had already begun to rise. Global supply lines have been disturbed by the diversion, and some businesses have decided to stop their production.

Definition of Key Terms

Houthi militia

An Iran-backed armed group controlling significant parts of Yemen, involved in attacking Western shipping vessels near the Bab El-Mandeb Strait in the Red Sea.

Global supply lines

The international network of trade routes and shipping paths crucial for the movement of goods and raw materials across the world.

Macroeconomic uncertainty

Economic instability and unpredictability affecting global markets, often influenced by geopolitical events and trade disruptions.

Trade facilitation measures

Initiatives aimed at simplifying and speeding up international trade processes, often through digitalization and improved infrastructure.

Port congestion

Overcrowding at ports due to increased ship traffic, leading to delays and inefficiencies in the loading and unloading of cargo.

Global core goods inflation

The rise in prices of essential goods on a global scale, influenced by increased shipping costs and supply chain disruptions.

Maritime chokepoints

Strategic narrow passages in international waters where maritime traffic is concentrated, such as the Suez Canal and Panama Canal.

WTO Trade Facilitation Agreement (TFA)

A 2014 agreement aimed at expediting the movement, release, and clearance of goods across borders, which many African nations have ratified but struggle to fully implement.

Bunkering services

The supply of services such as fuel for ships, crucial for their long voyages, especially important at ports seeing increased traffic due to rerouted shipping lanes.

Port operations and performance

The efficiency and effectiveness with which ports handle incoming and outgoing ship traffic and cargo, crucial for maintaining smooth trade flows.

Extended supply chains

Long and complex networks of production and distribution that are vulnerable to disruptions from geopolitical and logistical issues.

Inflationary Pressure

The economic force that drives up the general price level of goods and services, often caused by increased demand, higher production costs, or a decrease in the supply of goods, leading to reduced purchasing power and potential economic instability.

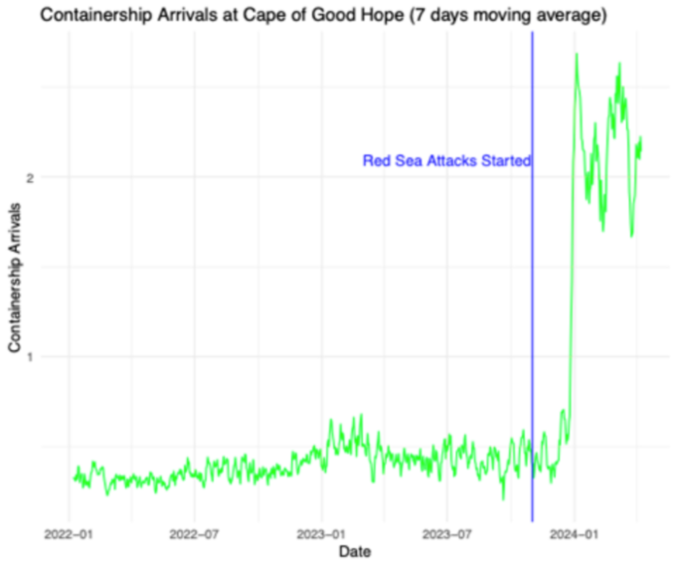
General Overview

Significant interruptions to international maritime commerce flows started at the end of 2023 as ships passing through the Red Sea, the Suez Canal, and the Gulf of Aden were under attack from Houthis headquartered in Yemen. This second wave of disruption came after the COVID-19 pandemic and its aftermath in 2020–2022 and the war in Ukraine since 2022. Furthermore, it exacerbates the problems brought on by the decreased ship traffic in the Panama Canals caused by the effect of drought on water levels.

Ship arrivals and transits have been significantly redirected due to security concerns in the Red Sea, with far-reaching implications for global trade and transportation. The Asia-Europe and Asia-Atlantic commerce lanes have seen ships from all shipping sectors veer off course and begin circumnavigating Africa's Cape of Good Hope. Ships are now required to go farther and incur greater operating expenses as a result. Pressure is being applied to the supply side by the rerouting of vessels.

For a ship heading from Shanghai to Rotterdam, the extra 12 days at sea increases expenses and extends delays.

Figure 1: Cape of Good Hope Containership Arrivals



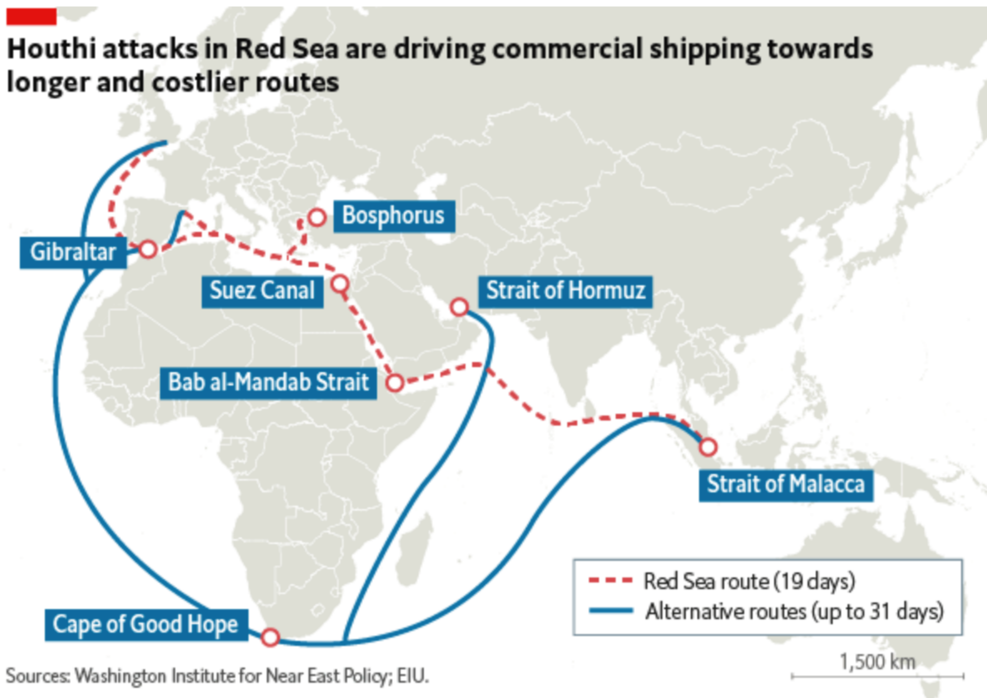
Source: UNCTAD chart based on Clarksons Research, March 2024

As rerouting necessitates the need for additional vessels to call at African ports, the Red Sea issue has also affected and caused congestion. However, these ports aren't always equipped to handle more ship calls and accommodate bigger ships. To reduce port congestion and expedite the clearance of goods, African countries and ports must step up ongoing efforts to implement trade facilitation measures, embrace digitalization, and mainstream green processes. This has become necessary by the disruption in the Red Sea and the increased shipping traffic around Africa.

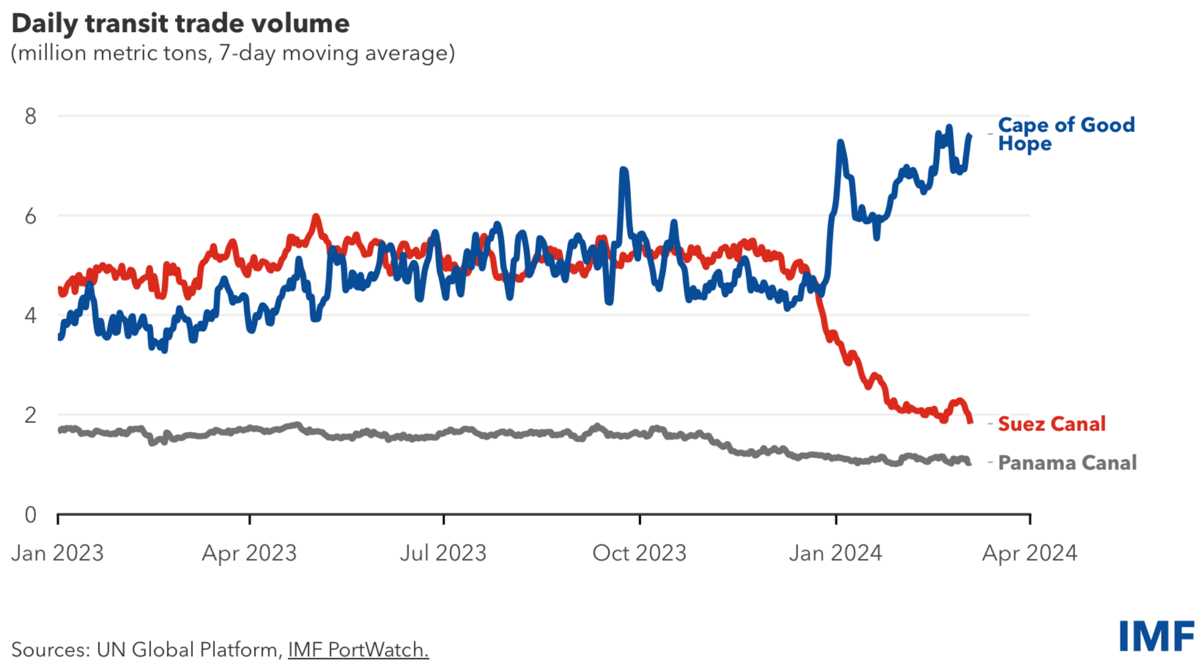
The turmoil in global logistics between 2020 and 2022 caused by the COVID-19 pandemic and its aftermath, along with the conflict in Ukraine, has highlighted the vulnerable nature of extended supply chains to disruptions and instances of inadequate readiness. The importance of supporting trade during disruptions and preparing for new obstacles is demonstrated by the Red Sea crisis and the Panama Canal challenges. Strengthening trade networks by lowering port congestion and enhancing resilience is essential to maintaining trade during crisis. The increased ship traffic around the African continent is certain to have an impact on port operations, even though the entire economic impact on Africa is still unknown. Supporting the use of trade facilitation measures, such as digitization and infrastructure improvements could furthermore boost African economies.

Economic Impact

On March 7th, 2024, the International Monetary Fund (IMF) published a report in which the economic impact of the dropped Suez Canal trade is calculated. According to the IMF, 10% of all seaborne traffic and 22% of all containerized trade worldwide are made possible by the Suez Canal, making it an essential global commercial route. In the face of persistent inflation and economic uncertainty, the present Red Sea shipping crisis is aggravating tensions in international trade, problems with regional stability, and difficulties with economic recovery. Given that Europe is one of Africa's main economic partners, the closure of the Suez Canal has a substantial impact on trade on the continent. The Suez Canal plays a major role in the foreign trade of East African nations, particularly Djibouti, Kenya, Tanzania, and Sudan. Due to longer cargo delivery periods brought on by the crisis, there are shortages of both standard and perishable items.



The route from Asia to Europe is prolonged by approximately 12 days when ships are rerouted around the African continent. This, according to the IMF, results in a 30% increase in transit times and a 9% decrease in the capacity of container shipping worldwide. While tonnage entering the Gulf of Aden has decreased by more than 70%, vessel transits through the Suez Canal have decreased by 42%. On the other hand, the number of ships arriving at the Cape of Good Hope has increased by 85%, with the arrival of container ships rising by 328%.



The cost of shipping has risen dramatically, going up 350% on the Shanghai-Genoa route and doubling on the Shanghai-Rotterdam route. This might result in a 0.7 percentage point increase in the inflation of core goods globally. African ports are under stress due to the rerouting of shipping routes, which is causing congestion and a rise in the demand for port services, especially in Durban and Cape Town. Due to a lack of resources, ports like Mombasa and Dar Es Salaam are finding it difficult to handle the growing traffic.

The WTO Trade Facilitation Agreement, which was adopted in 2014, has been ratified by the majority of African nations; however, implementation is still relatively low, which is reflected in a low ability to adjust to unforeseen changes leading to increased trade disruptions, economic losses, and diminished competitiveness due to inefficiencies. By updating border agency procedures with digital solutions and flexible, coordinated management systems, trade facilitation not only speeds up the processing of imports, exports, and transit items but also increases predictability and resilience to shocks. Many African nations currently have TFA implementation rates ranging from 20% to 79%. Only three nations—Benin, the Democratic Republic of Congo, and Mozambique—have declared that they finished full TFA implementation.

Major Parties Involved

Yemen (Houthi Militia)

A major actor in the Red Sea economic crisis is the Houthi movement in Yemen, which is supported by Iran. Since mid-November 2023, their strikes on Western transport boats near the Bab el-Mandeb Strait have caused severe disruptions to global maritime trade. The Houthis' aggressiveness has prompted major maritime companies to reroute their vessels, avoiding the Red Sea and the Suez Canal. This strategic canal is essential for international transportation because it serves as a critical shortcut between the Mediterranean Sea and the Indian Ocean, facilitating the swift and cost-effective movement of goods between Europe and Asia. These acts further destabilize Yemen and add to the economic unrest affecting global supply lines. They also emphasize the Houthis' military prowess and the wider geopolitical difficulties in the region.

Egypt

Egypt is severely affected by the economic crisis in the Red Sea since it has major control over the Suez Canal. Ship transits through the canal have significantly decreased because of the interruption brought on by the Houthi strikes, which had a direct impact on Egypt's economy. The nation is largely dependent on the money the canal brings in, and the ships' detour around the Cape of Good Hope has resulted in significant losses. Egypt is an essential partner in any endeavour to reestablish peace and guarantee the safety of shipping lanes across the Red Sea due to its strategic located ports at the Suez Canal.

South Africa

As ships are diverted around Africa to avoid the Red Sea, South Africa's strategic location near the Cape of Good Hope has grown in importance. Port infrastructure is being strained and traffic in South African ports, like Durban and Cape Town, is increasing because of this surge in maritime traffic. While South Africa might benefit economically from this growth in shipping traffic, the nation must also overcome logistical obstacles to meet the growing demand for port services.

Djibouti

Another significant actor impacted by the Red Sea economic crisis is Djibouti. Its economy is mostly dependent on maritime traffic that crosses the Strait of Bab el-Mandeb. The Houthi attacks have caused shipping vessels to reroute, which has decreased port activity and Djibouti's revenue.

Djibouti, an important hub for trade in the area, must deal with the economic effects of the delays while looking for measures to improve its port facilities and guarantee the safety of its shipping lanes.

Sudan

Sudan is heavily impacted by the Red Sea economic crisis as the Suez Canal handles about 34% of its foreign trade. Due to the interruption, there are now shortages of necessities and higher prices, which has put a heavy burden on the economy. Due to its reliance on marine trade, Sudan is especially susceptible to changes in international shipping lanes. In addition to its ongoing political and economic problems, Sudan must deal with these obstacles.

Europe

Due to its substantial reliance on the Suez Canal for trade with Asia and Africa, Europe is greatly impacted by the Red Sea economic crisis. Due to the obstruction of this vital marine route, there are now significant logistical difficulties, which raise shipping prices and cause delays. Europe accounts for 26% of Africa's imports and is the destination for 26% of African exports, making the seamless operation of the Suez Canal vital for European supply chains. The availability and price of commodities have been impacted by the rerouting of ships around the Cape of Good Hope, which has increased delivery delays and heightened inflationary pressures in Europe.

United States

Because of its geopolitical interests and extensive international trade networks, the United States is indirectly impacted by the Red Sea economic crisis. The United States, which has strategic interests in the stability of the Middle East and the Red Sea region, is concerned about global economic security in light of the Houthi strikes and the ensuing disruption to international shipping lanes. Regional conflicts have far-reaching effects on global economies; for example, delays and higher shipping costs can affect American consumers and enterprises.

Timeline of Key Events

November 19th, 2023.	The first (of later many) commercial ships were attacked in international waters in the southern Red Sea, with anti-ship ballistic missiles fired from Yemen by Iranian-backed Houthi rebels.
Late November, 2023.	Major maritime companies begin rerouting their ships to avoid the Red Sea and the Suez Canal, opting instead to travel around the Cape of Good Hope. This decision is driven by security concerns and rising insurance costs. The rerouting of vessels around the Cape of Good Hope adds approximately 12 days to the Asia-Europe shipping route, resulting in increased transit times and higher costs. Meanwhile, rising fuel and insurance expenses start pushing up global shipping rates, adding to the economic strain on global supply chains.
December, 2023.	Cargo traffic through the Panama Canal decreases due to falling water levels, further complicating global shipping dynamics.
December 19th, 2023.	US Defence Secretary announced that the US had formed a coalition of ten nations, including Bahrain, Canada, France, Italy, UK and other countries, who would send ships to assist in fighting against Houthi attacks in the Red Sea. The coalition quickly expanded.
Early January, 2024.	African ports, in South Africa (Durban and Cape Town), Kenya (Mombasa), and Tanzania (Dar Es Salaam), are increasingly experiencing significant congestion due to the increased maritime traffic.

January 10th, 2024.	UN Security Council passes Resolution 2722, condemning Houthi attacks and emphasizing freedom of navigation.
January 26th, 2024.	Vessel transits through the Suez Canal have dropped by 42%, highlighting the impact of the crisis on this critical maritime chokepoint.
February 8th, 2024.	J.P. Morgan Research estimates the disruptions could add 0.7 percentage points to global core goods inflation, and 0.3 percentage points to overall core inflation, during the first half of 2024.
February 12th, 2024.	The United Nations Conference on Trade And Development (UNCTAD) reports that the tonnage of ships entering the Gulf of Aden decreases by more than 70%, while the gross tonnage of vessels arriving at the Cape of Good Hope increases by 85%, with container ship arrivals rising by 328%, indicating a major shift in shipping patterns.
Ongoing.	The prolonged transit times and higher operational costs continue to disrupt global supply chains, affecting the availability and cost of goods worldwide. Meanwhile, the continued diversion of shipping routes around Africa results in sustained congestion and increased demand for port services, particularly in Durban, Cape Town, Mombasa, and Dar Es Salaam.

UN involvement, Relevant Resolutions, Treaties and Events

- Renewal of sanctions against Yemen imposed by the Security Council, February 25th 2021 (S/RES/2564)

- Condemning Houthi attacks and emphasizing freedom of navigation, January 10th 2024 (S/RES/2722)

Previous Attempts to solve the Issue

The TFA, adopted in 2014, aims to expedite the movement, release, and clearance of goods, including through improved cooperation between customs and other authorities. African countries, particularly those affected by the Red Sea crisis, have been working towards implementing TFA provisions.

Implementation of TFA measures has varied across African countries, with some making significant progress in modernizing customs procedures and reducing trade barriers. However, overall progress has been slow, and many countries still face challenges in fully implementing the agreement.

While TFA implementation has the potential to mitigate some economic impacts of the crisis by improving trade efficiency, the benefits are limited by the pace of adoption and the scale of disruptions caused by the conflict.

Possible Solutions

Naval Coalition

The UN could spearhead the formation of an enhanced multinational naval coalition dedicated to patrolling and securing the Red Sea and its adjacent waters. This coalition would involve increased contributions from member states in terms of naval resources, intelligence sharing, and the deployment of advanced surveillance technologies such as drones and satellites. The primary objective would be to deter and prevent further Houthi attacks on shipping vessels, thereby ensuring the safe passage of maritime traffic. By establishing protected maritime corridors and conducting coordinated patrols, the UN-led coalition would provide a significant deterrent against threats and reassure shipping companies, potentially reversing the costly trend of rerouting ships around the Cape of Good Hope.

Enhancing Trade Facilitation Processes

The UN could focus on enhancing trade facilitation processes, particularly in the affected African ports experiencing increased congestion due to the crisis. The UN could assist in accelerating the implementation of the WTO Trade Facilitation Agreement (TFA) provisions across these ports. This would involve modernizing customs procedures, investing in port infrastructure, and promoting digitalization to streamline operations. Specific measures could include the adoption of automated cargo handling systems, electronic documentation, and improved logistics coordination to reduce delays and increase efficiency. Additionally, the UN could encourage the integration of green processes in port operations to manage the environmental impact of heightened maritime traffic. These efforts would not only address the immediate challenges posed by the crisis but also enhance the long-term resilience and efficiency of global supply chains.

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