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What to watch: Economic scenarios for Israel - Hamas conflict, rolling back on climate goals and drought at Panama Canal disrupts trade

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Executive summary

This week, we analyzed three important issues:

- First, one month on, we wanted to share our latest [economic scenarios for Israel – Hamas conflict](#). As of today, tensions look set to develop into a protracted but contained conflict (75% probability). The impact on global commodity prices and inflation remains very contained as initial conditions were already very tight. Overall, we expect a slight stagflationary effect on the global economy, with little impact on capital markets. In a downside scenario of severe escalation into a regional conflict with direct intervention of Iran and the US, OPEC+ countries could decide on a drastic cut in oil production, echoing the 1973-1974 oil embargo, and fears of a disruption in commerce in the Strait of Hormuz would soar. This would lead to record high oil prices and cause a recession for the global economy. Capital markets would be also severely affected, with equity indices likely to fall by -7% in the US and -9% in the Eurozone, alongside widening credit spreads.
- Second, it's [one step forward, two steps back on climate targets](#). European governments are procrastinating on their climate goals. The UK and Sweden have already announced rollbacks on climate goals, while resistance and skepticism towards existing targets are growing in other economies. The ongoing cost-of-living crisis and climate populism may explain this unfortunate movement. The energy, transport and housing sectors face the most pressure as they directly impact voters' lives. Sobering news for climate month.
- Third, [the drought at the Panama Canal could prolong the trade recession](#). The number of vessels that can pass through the Panama Canal will be halved to 18 vessels per day starting in February 2024, particularly affecting US exports. After global trade bottomed out, such disruption fuels fears of higher imported inflation. The drought also hints at what lies ahead as global temperatures increase: by 2030, rising temperatures could lead to a -38% decrease in transportation capacity, reducing potential growth in global trade of goods in volume by -5pp per year. The physical costs of climate change are real.

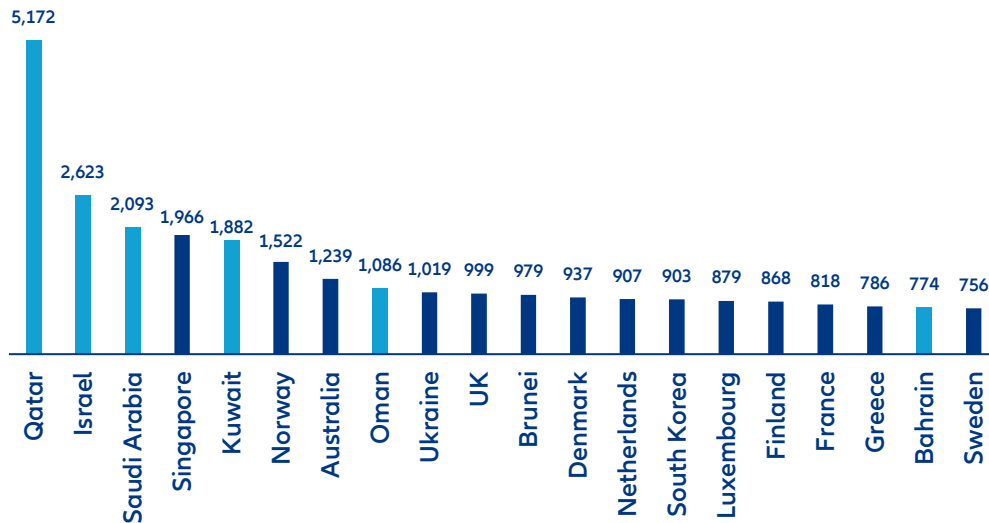
Economic scenarios for Israel – Hamas conflict

One month on, the Hamas incursion into Israeli territory looks set to develop into a protracted but contained conflict (75% probability), with hostilities likely to persist well into next year but limited to within and around Israeli borders. In response to the Hamas attack on 07 October, the Israeli government initiated operation 'Swords of Iron' and triggered Article 40 Aleph – the first such occasion since the 1973 Yom Kippur war. Business interruptions are already visible, with several flights and logistics operations halted or diverted. Major oil companies have also suspended production from the Tamar natural gas field off the Israel's northern coast. Moreover, some cargo was diverted from the Ashdod port to Haifa, the heart of the potential India-Saudi-Arabia-Israel corridor, causing a moderate backlog and calls for force majeure on carriers. Looking ahead, we expect the conflict to remain concentrated in the territories around Israel, notably the northern part of the Gaza Strip. Israeli troops are likely to continue occupying Gaza City and neighboring countries will take steps to support refugees.

Israel is exposed to increased financing risks and we see a risk of GDP growth dropping by around -2.5pps from +3.2% to +0.7% in 2024, with negative rates from Q3 2024 and inflation remaining above 4%. In Israel, the inception of a government of national unity has temporarily eased domestic tensions and watered down the role of extreme-right parties in the coalition, without healing deep-seated divisions. However, the risk of early elections remains high. The independence of the judiciary, the likelihood of civil disorder, potential impacts on business and, in general, additional constraints due to a marked deterioration of bilateral, regional and international relationships remain key issues. However, low unemployment at 3.1% and a thriving defense industry should more than offset the impact of large-scale military conscription and lower revenues from investment and tourism on GDP growth, at least in the short term. Israel's public-debt-to-GDP ratio decreased from 71% during the Covid-19 pandemic to around 61% in 2022, thanks to a prudent fiscal stance, even though military expenditure stood at 12% of GDP before the current crisis. A recession is likely in 2024, caused by reduced economic activity, a lack of workers, potential disruptions in computer and electrical networks, the absence of tourism receipts and lower private consumption. A significant strain on the government's fiscal position would likely materialize.

For the Middle East region overall, we expect the conflict to cost -0.8pp of GDP growth, taking it down to +1.7% in 2024, as already high regional uncertainty increases further. Four of the top five countries in the world by per capita defense spending are in the Middle East. Qatar, which is first on the list (Figure 1), can leverage extensive diplomatic networks both in the West and with Hamas, of which it hosts several members in exile, and has already played a mediating role in the recent past. However, in September, Qatar announced that it had cut its financial backing to Hamas due to disagreements over the latter's foreign policy and its rapprochement with the Syrian government. It is indicative in this regard that the United Arab Emirates warned Syria not to intervene just a few hours after the attack against Israel. Egypt and neighboring Arab countries will continue to support a ceasefire but will refrain from getting involved further as they focus on domestic economic challenges and financial weakness. The most vocal countries (Iran, Syria) are not expected to support a further escalation in the conflict, preferring a pragmatic approach in the face of limited domestic economic and military capacity. Meanwhile, Ankara has made no secret of its preference for a trade corridor from the East through Iraq and Türkiye itself rather than Israel and further support towards this objective, as well as that of maintaining its clout over regional issues, will become more likely under current circumstances. Egypt could also see an increase in foreign investment and bilateral financing, particularly from the US and EU, which would allow for more government spending – crucial to reducing the loss of purchasing power caused by inflation.

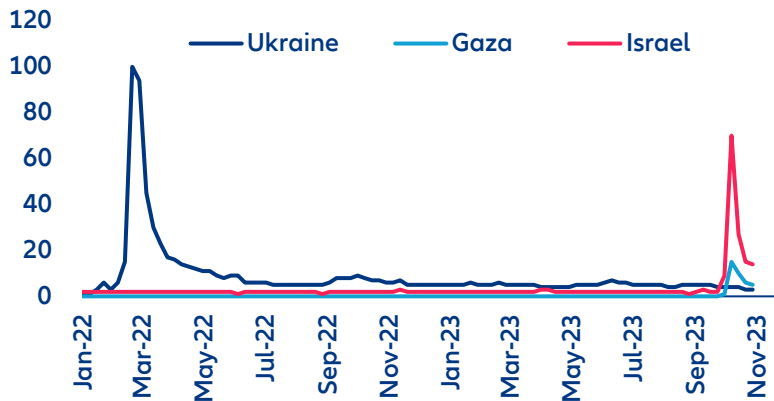
Figure 1: Top 20 countries by military spending per capita in 2022, USD



Sources: SIPRI, Allianz Research

G7 countries will continue to support a ceasefire in the Middle East, but the conflict could draw attention and military support away from Ukraine. The EU and the US will continue working on creating efficient humanitarian corridors in the Middle East. The EU supports a ceasefire and the creation of two states. While G7 countries continue to support Ukraine, it could see a decrease in assistance as long as Russia does not invade or escalate that conflict further. Ukrainian President Volodymyr Zelensky has raised concerns that the Middle East conflict could divert attention away from the war in Ukraine, and Google search data confirm the shift in focus (Figure 2).

Figure 2: Google searches

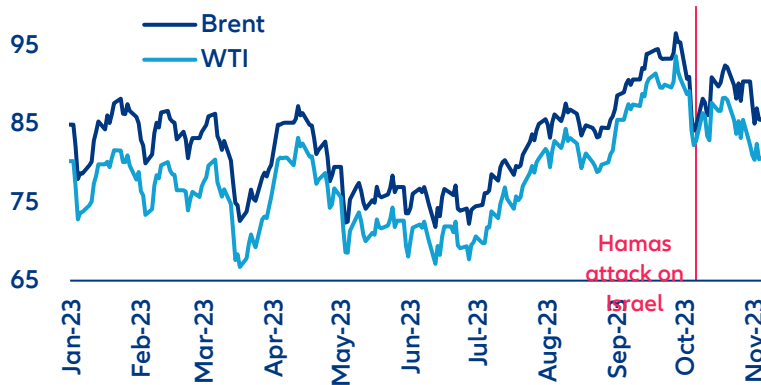


Sources: Google, Allianz Research

So far, the impact on global commodity prices and inflation remains contained as initial conditions were already very tight. The volatility associated with the conflict has had a limited impact on transportation and commodity costs, with an expected rise of +5%. Trade corridors remain open and we do not expect any blockages of the Suez Canal. Although Brent crude oil prices increased moderately immediately after the outbreak of the conflict by about USD5 per barrel, they have returned to USD80/bbl as of 08 November, lower than their level before 07 October (Figure 3). This was mainly driven by lower global demand expectations. Although supportive of Israel, the US administration has taken a cautious approach towards oil markets, even easing sanctions against Venezuelan crude. It is unlikely that sanctions could be reinstated against Iran. In 2023, Iranian crude oil production increased by 600,000 barrels per day to

3.14mn barrels per day (the world's second-largest source of incremental supply after the US). Overall, we continue to expect oil prices at 90USD/bbl on average in 2024, an increase of +4USD/bbl compared to our latest forecast, and the differential between Brent and WTI to increase slightly.

Figure 3: Oil prices (USD)

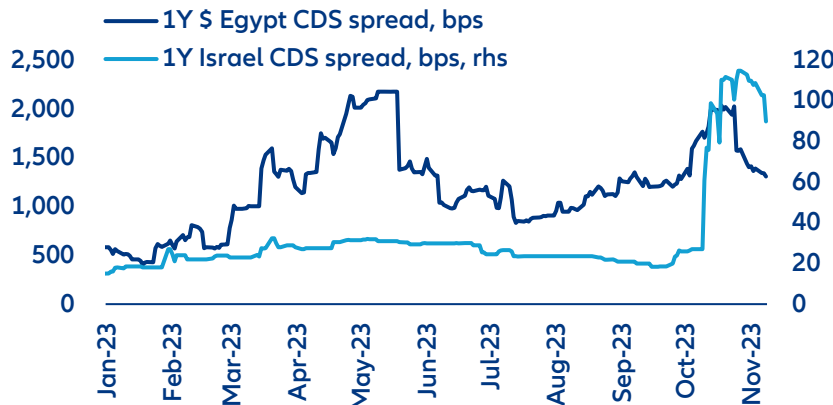


Sources: LSEG Datastream, Allianz Research

Overall, we expect the conflict to have a slight stagflationary effect on the global economy, with little impact on capital markets. We have cut our forecast for global GDP growth in 2024 by -0.1pp to +2.3% and revised up our forecast for inflation by +0.1pp to 4.4%. In this scenario we do not expect any material changes from the pre-conflict scenario in terms of policy mix: moderate fiscal consolidation and no cut in interest rates before H2 2024. In terms of capital markets, we see little change from our forecast from September. Longer term rates may ease from current levels to 3.9% in the US (10y) and 2.6% in Germany at the end of 2024 amid ongoing, albeit slightly slower, disinflation and subdued growth. Equity indices in both the US and Eurozone are projected to yield a total return of 9% in 2024, slightly below their long-term average.

However, the potential for financial turmoil in the Middle East remains elevated. Israel's credit default swaps (CDS) have risen significantly since the Hamas attack (Figure 4) and the shekel lost more than 5% against the dollar before the Bank of Israel intervened by selling foreign currency reserves. Egypt was already grappling with severe economic conditions before the Hamas attacks and is heavily reliant on IMF support, being the second largest debtor after Argentina. Its central bank will likely devalue the currency again in the coming months and its CDS are at extremely high levels – albeit not having increased further. On 03 November, the rating agency Fitch downgraded Egypt's foreign currency rating by one notch to B-, citing downside risks to tourism and social stability because of the Hamas-Israel conflict, on top of the numerous domestic economic problems.

Figure 4: Credit default swaps of Egypt and Israel



Sources: LSEG Datastream, Allianz Research

What could go wrong? A major humanitarian crisis and/or military event could lead to a severe escalation and a regional conflict (downside scenario, 20% probability), sparking the direct intervention of Iran and the US. This would include Hezbollah launching deeper attacks into Israel and a full-scale Israeli occupation of the Gaza Strip. In this scenario, Iranian-backed forces in Syria and Iraqi troops would launch operations from the Golan Heights into Israel, while Palestinian organizations begin battling Israeli soldiers in the West Bank. The US would provide air support on the Syrian and Lebanese fronts, while Iran's Islamic Revolutionary Guard Corps would join the fight against Israel through "measured" responses hitting military targets.

However, apart from the US deploying military equipment and defense systems, no other G7 country would take military action. A navy build-up in the Mediterranean would divert funds away from Ukraine but military assistance to Kyiv is likely to remain in place until the presidential election in the US. Demonstrations and violence across the Arab world would add to the risks faced by foreign companies. Attacks against major infrastructure in the region would likely disrupt trade from/to Israel and the West, increasing global logistics costs by +4%.

In this scenario, the Netanyahu-led national unity government would bear co-responsibility for an escalation, while greater distrust from international allies would make his victory difficult in an early election. Israel has had five general elections from April 2019 to November 2022, and polls have also been held in the past during particularly tense periods. GDP growth in Israel would likely turn negative as increased instability affects international trade and lowers revenues; Saudi Arabia and the UAE could also see negative growth due to reduced appetite for the region, with repercussions on real estate and services.

An escalating conflict could prompt OPEC+ countries to agree on a drastic cut in oil production to make a statement to the West, echoing the 1973-1974 oil embargo when 7.5% of global output went offline. A potential cut of another 10mn barrels (about 10% of global demand, equal to 36% of OPEC crude oil production in October 2023) would have a major impact on prices in a year marked by elections in many countries, even though Western countries have reduced their dependence and diversified sources, and because demand is lower due to the pre-conflict economic slowdown. An escalation of the Middle East conflict could spark the return of inflation due to rising energy and transportation costs, as well as a potential hoarding effect due to the winter season.

Oil prices would rise also due to heightened geopolitical risk premia amid fears of a disruption in commerce in the Strait of Hormuz, a significant chokepoint in the global oil market. Escalating tensions could see Israel attacking Iran's oil infrastructure, halting oil transport across the Strait of Hormuz and worsening already tight oil markets. The worst-case-scenario could result in oil prices reaching USD120/bbl on average in 2024, with a spike up to 170USD/bbl and a distinct divide materializing between Brent and WTI prices in line with energy costs for the US and Europe.

In such a downside scenario, the global economy would enter a technical recession (+1.7% in 2024) and global capital markets would be severely affected. Escalating oil prices would push global inflation up to 5.2% in 2024 (Figure 5), halting the previously anticipated disinflationary trend. Consequently, Western central banks may find themselves unable to cut rates in 2024 as previously anticipated. With monetary policy staying restrictive and a rebound in inflation expectations, long-term government bond yields would remain around 4.5% in the US and 3% in Germany throughout 2024. Simultaneously, the economic deceleration in Western economies, exacerbated by soaring energy costs and continued restrictive monetary policy, would make fiscal support very limited. This would precipitate a downturn in risk markets, with equity indices likely to fall by -7% in the US and -9% in the Eurozone, alongside widening credit spreads.

Figure 5 – Economic, policy and capital market impact of different scenarios for the conflict in the Middle East

Scenario		<i>Prolonged but contained conflict</i>	<i>Severe escalation into a regional conflict</i>
Probability		75%	20%
Crude oil price Q4 2023 & 2024 (Brent, avg. USD/bbl)		87 90	120 120
GDP 2024 (delta to end-September baseline)	Global	2.3% (-0.1pp)	1.7% (-0.7pp)
	Eurozone	0.8% (-0.1pp)	0.2% (-0.7pp)
	US	1.0% (-0.1pp)	0.3% (-0.8pp)
	China	4.6% (-0.1pp)	4.0% (-0.7pp)
	Middle-East	1.7% (-0.8pp)	1.0% (-1.5pp)
Inflation 2024 (delta to end-September baseline)	Global	4.4% (0.1pp)	5.2% (0.9pp)
	Eurozone	3.1% (0.1pp)	3.6% (0.6pp)
	US	2.4% (0.1pp)	3.3% (1.0pp)
	China	1.8% (0.1pp)	2.4% (0.7pp)
	Middle-East	7.0% (0.6pp)	7.4% (1.0pp)
Global trade of goods and services in 2023 and 2024 (in volume, delta to end-September baseline)		-0.3pp/-0.5pp	-6pp/-8pp
Logistics cost index (maritime freight, delta to end-September baseline)		+0.75%/+1%	+4%
Foreign direct investment flows		Slightly lower due to increased policy uncertainty and fragmentation	Significantly reduced and concentrated in nearby/friendly areas.
Policy-mix		Moderate fiscal consolidation & no cut in interest rates before H2 2024.	Little fiscal space to offset high energy prices due to restrictive monetary policy & no cut in interest rates before end of 2024.
CB rates (eof 2024)	US	4.75%	5.75%
	Eurozone	3.50%	4.00%
10y gov. bonds (eof 2024)	US	3.90%	4.50%
	Eurozone: GER 10y % / ITA-GER 10y spread	2.6% / 150bps	3.0% / 230bps
Corporate spreads (eof 2024)	US	120	180
	Eurozone	140	220
Equities (2024)	US	9%	-7%
	Eurozone	9%	-9%
EURUSD 2024, average (delta to end-September baseline)		1.08 (-3.0%)	1.03 (-8.0%)
Financial markets summary		No material change from baseline.	CBs refrain from policy easing amid high inflation leading to higher yields and risk-off.

Source: Allianz Research. Note: 5% tail risk scenario of a global conflict including an open war involving Iran, the US and other countries not shown here.

In this scenario, Egypt would likely default after being isolated by other Arab countries for its perceived alignment with the West. Existing lines of credit from Gulf countries would be maintained but it would be up to multilateral institutions to take charge of keeping the balance of payments on track. Energy projects would be halted or postponed. Amid increasing political and social tensions, the results of the presidential election confirming El-Sisi could be subject to contestations, leading to increased uncertainty in the country that would require the military to resolve. The Suez Canal itself or tariff flows would be given as a pledge for debt repayments. Türkiye would likely welcome Palestinian refugees and threaten to consume the entire flow of natural gas shipped through the Southern Gas Corridor, leaving none for Europe. Qatar and Saudi Arabia would not intervene, but would deploy their navies to keep trade corridors open. Shipping companies would start to avoid the Gulf and Suez Canal to avoid putting their fleets at risk of terrorist

attacks. The Global South would start boycotting Israeli products and companies associated with being allies of Israel.

An accidental event or further escalation (e.g. a terrorist attack on an oil tanker transiting through Hormuz or Suez that would make the route unnavigable or a missile striking Jerusalem) would prompt other countries to enter the conflict directly and that would trigger a tail risk scenario (5% probability). In this situation, the conflict could expand further and trade routes would be compromised, potentially increasing geo-economic fragmentation to a level not seen since the end of the Cold War.

One step forward, two steps back on climate targets

The UK government is reorienting its green policies as the cost-of-living crisis starts to bite. This week, the King's Speech in the UK signaled a potential retreat from stringent climate policies by voicing support for new oil and gas drilling in the North Sea. The administration views ongoing local oil and gas extraction as crucial for its energy assurance and consistent with its aim for carbon neutrality, though its own Climate Change Committee disagrees. The Climate Change Performance Index 2023 suggests that the UK has been making good progress on its climate goals. However, the government is responding to voter criticism by backtracking on key climate policies, including delaying a proposed ban on the sale of new petrol and diesel cars by 2030 and the 2035 phase-out of fossil-fuel boilers, besides dumping energy-efficiency rules for landlords. In an attempt to increase coal supply for the steel industry, it has also approved the country's first deep coal mine in 30 years and promised to investigate nuclear power as part of its energy-security strategy.

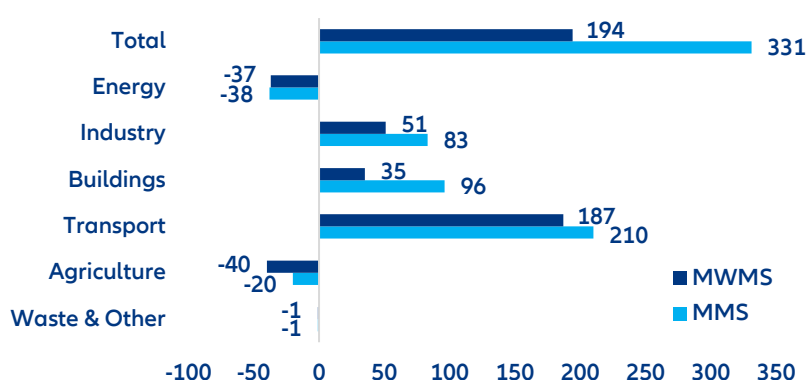
But the UK is not alone. Other European governments are also contributing to the worrying trend that risks undermining the global commitment to maintaining the global temperature increase to 1.5°C. As the window to prevent the most severe consequences of climate change narrows, advanced economies should be phasing out fossil-fuel extraction, not promoting it. But in Sweden, for example, the right-leaning government recently announced not only a EUR22.17mn cut in funding for climate and environmental measures but also tax cuts on petrol and diesel, which contradicts the target of achieving a -17% reduction of emissions in the transport sector between 2023 and 2030. Sweden also abandoned its 100% renewable energy goal and modified its net-zero target to 100% "fossil-free", creating the conditions for the return of nuclear power to the country's energy mix. The energy crisis sparked by Russia's invasion of Ukraine has also contributed to keeping fossil fuels on the table. Germany and Slovakia, for example, temporarily increased coal mining and coal imports to shore up energy reserves ahead of the winter and supported gas and coal consumption instead of renewables. In France, two out of four coal plants that were to be shut down in 2022 will now be used up to the end of 2024. And nuclear energy is back on the table: Instead of bringing its share below 50% by 2025, from 75% in 2017, France is now considering opening new nuclear power plants. And a planned carbon tax on diesel fuel has also been scrapped. Meanwhile, several central and eastern European countries have used the energy crisis to not only temporarily alter their energy mix but also to backtrack on previous commitments. Hungary increased the domestic production of fossil fuels and delayed the phase-out of coal power, and Bulgaria could follow.

Meanwhile, despite making comprehensive climate policy proposals to reach its 2030 targets, Europe's largest economy will still emit 200mn tons more of CO₂ than planned until the end of the decade. Renewable energy is not growing fast enough and the transport sector still needs to cut emissions dramatically. Yet, Germany – backed by Italy, Poland and Bulgaria – reneged on a deal to ban the sale of new cars powered by internal combustion engines in the EU by 2035, bowing to pressure from its car manufacturing industry. Instead, Berlin reached a deal with the European Commission that allows for cars to be registered after 2035 if used the fuel is exclusively carbon neutral. This is echoed by an Italian-led coalition of nations that is pushing for synthetic fuels and biofuels to be counted towards carbon standards

for heavy-duty vehicles. Green building standards are also not making much progress in both Germany and Italy.

German climate targets are at risk because of a lack of comprehensive action across all sectors. The advanced nuclear phase-out has inadvertently increased greenhouse-gas emissions as the government agreed to close some coal capacities later than originally planned – in 2024 instead of 2022 – to conserve gas. However, the larger blow might result from the substantial new investments in gas infrastructure, particular into LNG-terminals, as a reaction to the cut-off from Russian gas. Germany's international actions also contradict its domestic climate policy, given that it continues financing gas projects abroad, such as in Senegal, rolling back COP26 commitments. Current projections suggest that the costly and highly subsidized LNG overcapacities potentially result in lock-in effects and stranded assets, and stress fiscal budgets, further limiting funds that are desperately needed elsewhere in the just energy transition. Meanwhile, renewable electric capacity is on track for solar but lagging for wind energy. According to the German Environmental Agency, the energy and agriculture sectors may be the only ones that could meet 2030 targets, if the renewable-capacity expansion accelerates according to plan. However, internal division within the coalition government could further jeopardize the achievement of the short-run sectoral climate targets as the ministries responsible for buildings and transport failed to submit an emergency program as required by the German climate law. Consequently, the government has proposed weakening the climate change law by allowing sectoral compensation, even though it is unlikely that any sector will exceed its targets significantly (Figure 6). Additionally, the coalition has also failed to advance a socially just climate transition, delaying the implementation of an announced "climate dividend" that is supposed to redistribute revenues from carbon pricing on heating and transport emissions.

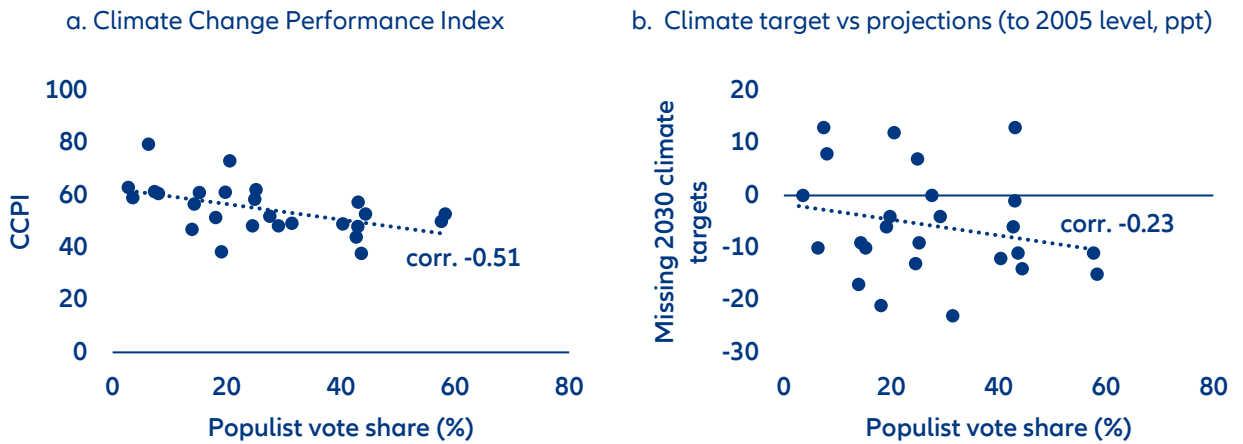
Figure 6: Cumulative gap of German sectors from emission targets, 2023-2030 in mio. t CO₂-equivalents



Sources: German Environmental Agency, Allianz Research. Notes: The 2023 Projection Report focusses on two scenarios: The with existing measures scenario (MMS) projects the effects of policies and measures already in place. The with additional measures scenario (MWMS) also considers additional measures which are currently planned by the German government.

Overall, Europe is still on track but political opposition might derail climate targets. Despite the challenges faced during the transition to climate neutrality, it is crucial for politicians to stay the course in order to provide industry and households with clear signals that the transition will be followed through. Maintaining strategic and systemic legal certainty for green investments, such as with the European Climate Law and its ETS, could give the EU an advantage over the US where subsidies provided under the Inflation Reduction Act have encouraged investments in clean sectors but could easily be abandoned. However, there is a risk that political opposition in the EU could derail plans to reach net zero by 2050 as an ideological divide over green policy emerges ahead of the upcoming European elections. We find for EU countries and the UK that a higher populist vote share in the last elections relates to a lower Climate Change Performance Index (CCPI) (Figure 7a), which ranks countries based on progress and ambition in pps compared to an ideal scenario of reaching set climate targets in 2022. The connection is less pronounced but still negative for a country's potential of missing the climate target by 2030 (Figure 7b).

Figure 7: Correlation between populist party vote share in last election and climate targets, EU 27 and UK

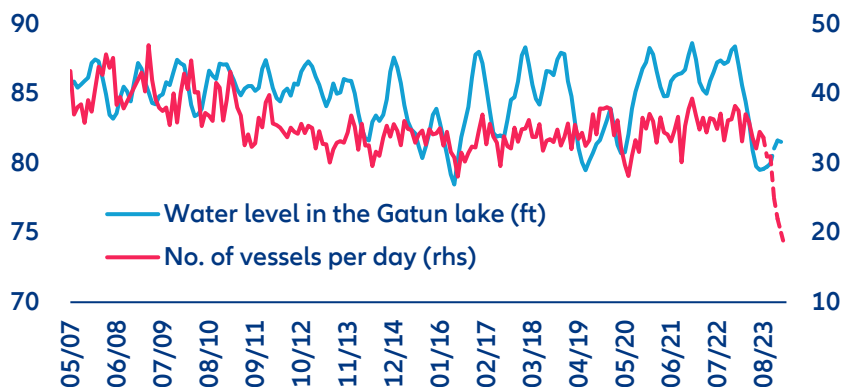


Sources: Germanwatch, European Commission, ParlGov and World Bank, Allianz Research

The drought at the Panama Canal could prolong the trade recession

Historically low water levels in the Gatun Lake that feeds into the Panama Canal are reducing the number of vessels that can pass through, putting a crucial trade route at risk. Stretching approximately 80km and connecting routes between the Atlantic and the Pacific Ocean, the Panama Canal has been an important trade route since 1914, carrying about 3-5% of global trade each year. Although the Republic of Panama generally records high levels of annual precipitation (247cm of precipitation on average in the past 10 years), this year has been the second driest since 1950. As a result, the artificial lake created to supply water to operate the locks and help vessels transit the Canal has seen historically low water levels. Consequently, the Panama Canal Authority (ACP) has limited the number of vessels that can transit through the canal to 24 per day (from 31 previously), starting on 07 November. This number will reduce further to 18 per day from February 2024. This is equivalent to a nearly -50% reduction in daily vessel through the Canal, which in normal times sees about 36-40 vessels passing through every day (Figure 8). The ACP also had to reduce the draft limit from 50ft to 44ft and for each foot of draft that is reduced at the Panama Canal, shippers are having to take about 300 to 350 containers of cargo off of their ships, which has led to them to charge about USD600 more per container to their customers. The largest impact has been on liquefied petroleum gas (LPG) tankers.

Figure 8: A sharp decline in the number of vessels transiting the Panama Canal in recent months

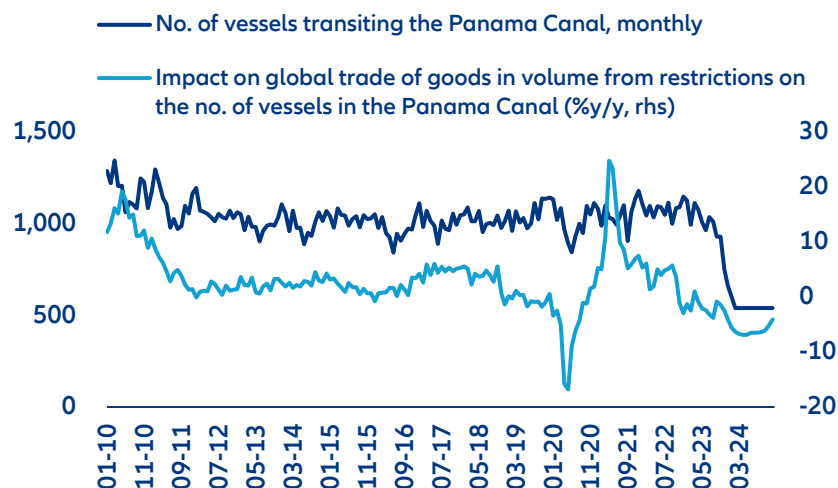


Sources: Bloomberg, Panama Canal Authority (ACP), Allianz Research. Notes: Dotted lines indicate projections for the water level and limits announced by ACP for the number of vessels per day.

The -50% reduction in capacity exacerbates trade recession fears for 2024. Our simulations suggest that a -1pp decrease in the number of vessels transiting through the canal due to episodes of drought reduces

global merchandise trade by 0.14pp on average, compared to the previous year. Prior to the drought, the canal was being used at close to full capacity, with 35 vessels passing through it daily on average until July. We estimate that reducing the number of vessels that transit through the canal could have a cumulative impact of -1.3pp in 2023. In the worst-case scenario, this could cut around -6pps from global merchandise trade volume growth if restrictions are prolonged until end-2024, which would push global trade of goods into recession.

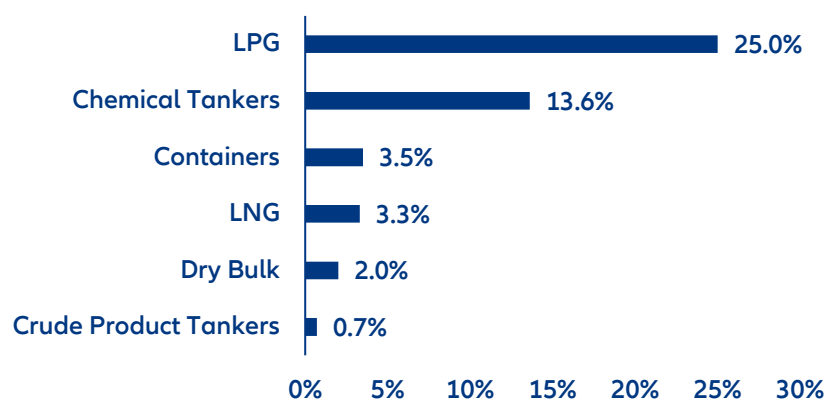
Figure 9: Trade impact of the reduction in the number of vessels transiting the Panama Canal



Sources: Bloomberg, Refinitiv Datastream, Allianz Research

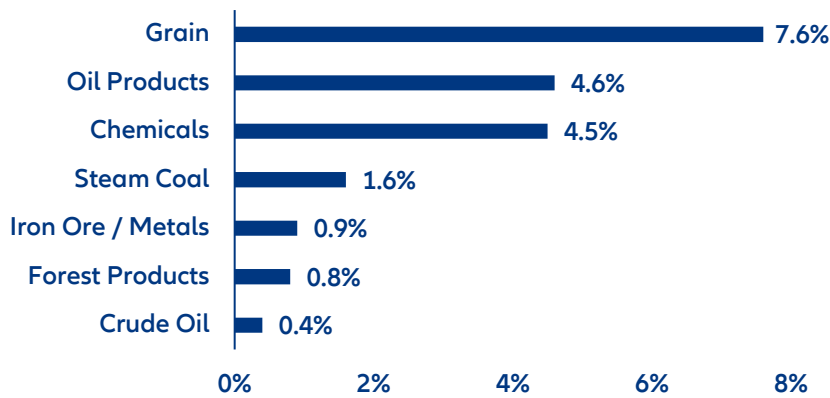
The US would be most affected. The US accounts for 70% of total container traffic passing through the Panama Canal. Moreover, of all US container traffic, 40% travels through the Canal annually – representing about USD270bn in cargo. The Canal primarily connects the US East Coast with Asia and the West Coast of South America, so reduced vessel capacity could increase the prices of products shipped between these regions, the vast majority of which are commodities (Figures 10 and 11). On the consumer goods side, container ships carrying finished goods book their voyages a few weeks in advance and may not encounter waiting times as long as those encountered by dry-bulk cargo ships which usually do not book their passage. Still, container carriers will have to manage delays and improve their logistics in order to ensure deliveries of consumer goods for the key upcoming Thanksgiving and Christmas seasons in the US. Overall, we calculate that reduced capacity in the Panama Canal could cut US exports by close to -0.3pp compared to the previous year. Latin American countries would be second on the list with a -0.2pp cut to exports.

Figure 10: Panama Canal - Traffic by shipping market segment in relation to global trade in 2022



Sources: PCA, Clarksons, Moody's, Allianz Research

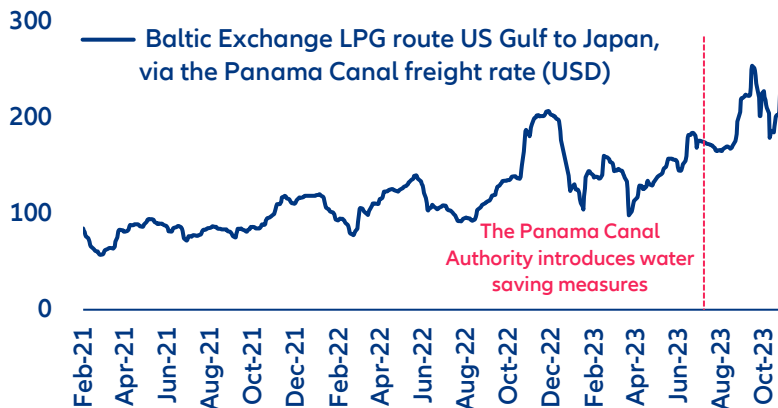
Figure 11: Panama Canal - Transit by commodity in relation to global trade in 2022



Sources: PCA, Clarksons, Moody's, Allianz Research

Concentrated price increases in the energy and consumer sectors cannot be completely ruled out. In 2022, the three main goods shipped through the Canal were petroleum and petroleum products (30%), container cargo (22%) and grains (13%). In terms of traffic by shipping market segment in relation to global trade, liquefied petroleum gas (LPG) claimed the largest share, followed by chemical tankers and containers, while in terms of transit by commodity, grain, oil products and chemicals constituted the largest share. But as the Panama Canal is a facilitator and not the only connecting solution, carriers linking the US East Coast with Asia have been considering using other alternatives such as the Suez Canal or bordering the Cape of Good Hope (South Africa). Though this takes longer¹ and represents greater fuel use, doing so would allow companies to avoid Suez Canal fees, which increased this year. Freight rates of LPG tankers have risen by +44% between August and November 2023 after the ACP introduced measures to combat the crisis (Figure 12) and auctions for slots that are usually won by LPG and LNG sectors have reached record highs of USD2.85mn while slots have sold at USD2.4mn in 2023, already higher than the USD900,000 of normal times. These developments are highly likely to impact shipping companies' margins.

Figure 12: LPG freight rates from the US Gulf to Japan via the Panama Canal



Sources: Refinitiv, Allianz Research

Climate change could have long-lasting impact on the Panama Canal. Considering a rise in the global mean temperature by 1.5°C and a deviation of -7.4% in the median river discharge² relative to current water levels, the daily number of vessels will be lowered by -15 compared to normal times (i.e. 40) which would mean -38% decrease in transportation capacity, reducing potential growth in global trade in volume by -5pps per year. While projects to improve and restore rainforests in Panama may reduce climate-related costs to trade through the Panama Canal in the long term, reduction in draft measures and a restriction on the limit of vessels passing through the canal seem to be the best solution in the short term.

¹ VLGC (very large gas carriers) connecting the US East Coast to China take around 58 days through the Panama Canal, 81 days via the Suez Canal and 88 days going around the Cape of Good Hope.

² Defined as the volume of water flowing through a river or stream channel.

These assessments are, as always, subject to the disclaimer provided below.

FORWARD-LOOKING STATEMENTS

The statements contained herein may include prospects, statements of future expectations and other forward-looking statements that are based on management's current views and assumptions and involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those expressed or implied in such forward-looking statements.

Such deviations may arise due to, without limitation, (i) changes of the general economic conditions and competitive situation, particularly in the Allianz Group's core business and core markets, (ii) performance of financial markets (particularly market volatility, liquidity and credit events), (iii) frequency and severity of insured loss events, including from natural catastrophes, and the development of loss expenses, (iv) mortality and morbidity levels and trends, (v) persistency levels, (vi) particularly in the banking business, the extent of credit defaults, (vii) interest rate levels, (viii) currency exchange rates including the EUR/USD exchange rate, (ix) changes in laws and regulations, including tax regulations, (x) the impact of acquisitions, including related integration issues, and reorganization measures, and (xi) general competitive factors, in each case on a local, regional, national and/or global basis. Many of these factors may be more likely to occur, or more pronounced, as a result of terrorist activities and their consequences.

NO DUTY TO UPDATE

The company assumes no obligation to update any information or forward-looking statement contained herein, save for any information required to be disclosed by law.