

It's all about growth

Burgeoning trade forcing each container line to navigate a course towards competitive advantage.

In this month's *Strategic View*, Deep Parekh describes how competition has changed the way liner carriers view success in the marketplace.



The Strategic View

BY DEEP PAREKH

Global trade has never been better. More products are being shipped around the world each year. From 1980 to 2004 global seaborne trade nearly doubled from 3.5 billion metric tons to more than 6.5 billion metric tons (Figure 1). Current trends show world trade is not expected to cool down anytime in the next decade.

According to *Global Logistics and Supply Chain Strategies* (March 2006), "the world's container lines continue to burgeon in size and volume, thanks both to global appetite for goods from the Far East and to the struggle for market share growth among container carriers. According to BRS-Alphaliner, the Paris-based shipping broker that closely tracks capacity and market share among the world's container lines, container capacity in this decade has increased 77.4 percent from 5.15 million twenty-foot-equivalents to 9.14 million TEUs. Just to keep their market shares during that period, carriers had to increase their fleet capacities by this percentage. As a result of this pressure, not only has liner capacity increased, but there have also been major shifts in industry leadership based on carriers' willingness to invest in new capacity."

And so, we see there is a shifting dynamic in the marketplace. Carriers who have historically been risk-averse are venturing forth into somewhat uncharted territories for them historically. With increased competition coming from different places, liner carriers are finding they must pursue success differently. They are beginning to explore different dimensions along which

they may be able to differentiate themselves: through better costs and efficiencies, better capital leverage, innovation in service offerings, market-extension, and other strategies, albeit haphazardly.

In order to examine liner carrier strategy and define how carriers should think about their survival, entry, exit or excellence in the industry, consider the Value Creation Matrix in Figure 2. Using this matrix, industry behavior can be segregated into the five quadrants shown. The quadrants represent different strategies that businesses may pursue. The matrix

represents industry attractiveness and relative competitiveness.

Attractiveness is a measure of the market potential, determined by the growth rate of the spectrum of services that the liner carrier is providing. It is important for the liner carrier to separate its portfolio of services to determine in which services it really wants to compete and to what extent.

Competitiveness is a relative market

share factor. If primary competitors have about the same market share, they would be in the midpoint of the competitiveness axis.

So what do these quadrants signify? This framework allows liner carriers to segment their services in their portfolio, assess their competition and define their strategy "playbook." Generally, companies enter at the top left quadrant (Enter Market) and work their way around to the lower left quadrant (Extract Cash). Let us go through each of these in more detail.

Enter Market. This top-left quadrant is where competitors generally enter. It begins with the provision of low-end, low-capital services, such as order consolidation. This market entry position is often pooh-poohed by the bigger players. But if they can do this segment well, then the liner carrier with all its size and scale, is useless to compete in this service, and eventually must give it up. This is how an industry such as freight forwarding became so popular and populated.

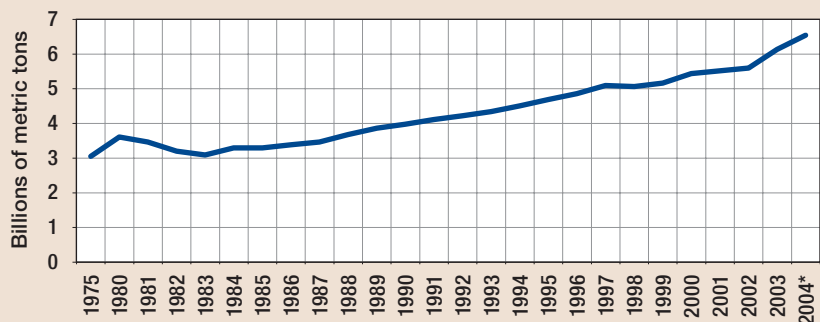
Liner carriers can change the rules of the game, such as by creating industry-wide information and technology formats, which then deters smaller niche players from entering. Typically this is not initially a big competitive space for too many players. But the more restricted the number of players here, the less expensive the battle becomes for market share when the particular service matures.

Build Leadership. The top-right quadrant is all about segmenting customer and offering services that are cost-to-serve friendly to the liner carrier. You cannot possibly afford to provide all services to everybody. It is critical to escape the competitive stranglehold and decisively take the No. 1 position in a few battles

Figure 1

World seaborne trade

(1975, 1980-2004)



* Estimate

Source: Equus analysis, American Association of Port Authorities original data, May 2006.

in competitive services. In this quadrant, you also want to increase the overall size of the total market through the use of innovative new services that the competition does not have yet, such as what tracking and monitoring were a few years ago, or what e-business services are today. In this quadrant you also want to dictate trade terms and set the standards with customers for other competitors to follow.

Generate Cash. This lower-right red quadrant is one where the services that the liner carrier is providing are mature, there are many competitors in the marketplace, but the relative market share of the liner carrier is still quite high. Hence, although the

market as a whole is declining, there is still sufficient cash in it to make it attractive to the carrier.

Breakbulk is a perfect example of such a service. Carriers can use this segment to fund innovative services and as a loss-leader for other more margin-rich services.

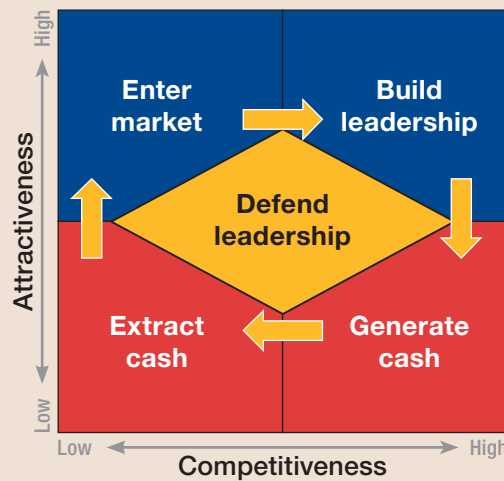
Liner carriers must optimize their pricing here, and avoid price-based competition by any means, as it would only accelerate losses.

Extract Cash. This is when the market is in steep decline, or the carrier wants to use a particular service only because it is important for the customers as part of its overall service offering. This quadrant should show services the carrier would want to exit during the next three to five years. It is a segment in which the carrier does not want to fragment its services further, and needs to simplify greatly, lower costs, maintain the revenues and have little to no investment. This might include services such as customs clearance.

Defend Leadership. This middle quadrant is a very interesting one. It is

Figure 2

Value creation matrix



Source: Equus research.

when companies slip when more competitors enter the market, when they lose market share on their core services, when they get into price wars, and many other instances. Carriers would find themselves here if they have not read the market right and price themselves incorrectly, take wrong calls on future capacity requirements, investment in assets, and market growth.

Does this sound familiar? Unfortunately, many carriers are found in this quagmire of a zone, which is difficult to get out of because it requires either significant investment, very clever innovation, tough calls around divestiture, and tougher calls for cashing in the chips and calling it “game over” — all of which are difficult to do. Hence much-needed decisions are postponed till new leadership takes over, or there is forced consolidation.

Out Of The Yellow. There are four things liner carriers can do to get out of the middle yellow zone:

- **Invest more.** Through better execution of current services, or by building out or extending their service base, they can

beat the competition and retain their leadership.

- **Make services a fuel for growth.** Make the decision to generate cash from it, and not use it as a competitive weapon. Do this only if you have other innovative projects (services) in your arsenal that are launching in due time (which would make your critical mass move to the upper left quadrant of Enter Market).

- **Cut your losses.** Lower your investment to the minimum and extract the most cash out of it, while pushing some other services to the top right quadrant — to balance the growth and revenue generation.

- **Develop new services.**

This is difficult to do, but through alliance partnerships and joint ventures, liner carriers can enter new market services that are relatively greenfield, and offer plenty of opportunity going forward.

If you like the yellow, then make sure you at least map out all your services in the different quadrants, and make sure you’re competitive in all of them.

Other companies that have worked this exercise have often found plenty of internal opportunities just by doing this mapping exercise, which makes them realize their inability to compete on some things, and their minimal investment required to strengthen their leadership, because competitive forces are a long second place, and gaining strength is relatively cheap and easy.

In any case, a little strategic housecleaning never hurts every now and then!

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