Capital Link Shipping
Weekly Markets Report

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IN THE NEWS

Outside the box thinking- revenue levers and clogged fuel injectors!

Contributed by

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Mainstream media is not the only shipping interface that's on my radar. Mainstream management consultants, ie not the usual suspects from inside the business, are also a great source for real actionable ideas, but also for snarky barbs. A recent report by the Boston Consulting Group (B-C-G), dealing with liner shipping in particular, which can be found online at Battling Overcapacity in Container Shipping definitely fits the bill. Though drybulk and tankers are more my bailiwick than liner (and I suspect that many readers are in the same boat), the report- spread out over a series of online articles, offers considerable food for thought.

My interest in the report stemmed from a new Capital Link discussion on Linked In, on the subject of Consolidation, begun by Mr. Nicolas Bornozis as a follow-up to the Capital Link Conference held in mid March. It was refreshing for me to see some analytical rigor (and perspectives from outside of the maritime bubble), from the likes of B-C-G, supplementing the vast over-supply of opinions and anecdotal evidence on the subject. At the March conference, the point was made that bigger consolidated companies would have an easier time when tapping the capital markets. But, the contretemps was that, in practice, putting companies together was hard to effect, the lunch remarks of investor Wilbur Ross notwithstanding. Big-Data, another area of interest for me (and recently the subject of news releases from Maersk Maritime Technology), is also considered in the B-C-G report. Big-Data is described by the consultants as a "revenue-lever". Buzz, buzz.

In the report, over-capacity is a given- there are more slots (as carriers order 20,000 teu vessels with reckless abandon) than there are boxes (with demand growth slowing down). With the cost curve ($/slot) moving steadily downward over time, so go freight rates- lower, lower and lower. For savvy freight buyers, much of the emphasis is in outright reductions, and various forms of "optimizing" the cost side of the various liner businesses. Certain of the findings, with logical alterations, can inform on the drybulk and tanker businesses.

The B-C-G report points out that alliances, where carriers in distinct corporate entities join forces, have been a form of consolidation preferable than corporate M & A transactions, even though "….the industry is ripe for more consolidation…" The authors provide three groups of reasons for the preference for "vessel sharing" through alliances- 1) value misperception, 2) Ownership structure and 3) integration risks.

Value misperceptions, where the report-writers lament price to book ratios "of about 1x" scaring away potential acquirers, are well known to denizens of the bulk business. When looking at downtrodden the shipping sectors, a market capitalization near book value could be perceived as strong. BCG goes on to note that companies with high priced assets are often reluctant to write them down…well, enough said. Ownership structures, with the vast majority of liner business tied to either families or governments cause "behaviors and priorities <to> be influenced by forces other than financial returns." It adds that: "…most families are unwilling to loosen their grip on their companies." Been there, done that. Integration risks, buzz-worded as post-merger integration (or PMI) risks, may be more germane to the liner side- where back office capabilities, and arranging for equipment link-ups, loom large. In terms of savings, optimization of terminals, intermodal activities and shared service centers (billings, tracking / tracing, etc) with joint IT-developments, could offer cost savings, in the aggregate of 18% to 35%. So, I am imagining Intertanko (or Intercargo) handling the back offices for their members, or subcontracting the agency relations, en bloc, to the likes of DA-Desk. Weather routing- well….that will intersect with the mother of all revenue levers…Big-Data. Consider the TI smart-phone app featured a few weeks ago in the New York Times- how about recouping development costs by licensing it to others? Oh, wait, it's a competitive weapon…no it's not… yes it is….(readers can add their own dialogue here)…

Again, all of this may seem outlandish at first blush, but if Maersk is doing it, then what? Investors typically shy away from such questions on the conference calls, or at one-one meetings, but if B-C-G espouses these measures (albeit for box boats), then maybe the level of conversations with companies needs to be stepped up. After all, parts the solution-set, matters related to fuel savings and technical modifications to vessels (promising 6% - 11% savings, at a given fuel price, which should be factored into increased hires commanded in the marketplace) have already been applied to the bulk and tanker sectors. On the human resources side, joint solutions (think hiring of crews from third party contractors) are already in practice. So, pardon the pun, what about additional out-of-the-box thinking for non-container sectors?

Big-Data, though mentioned by the consultants, does not feature as prominently as I expected it to; it fails to burst through the haze of "business model innovation." But individual market participants may start to carry that ball. For Maersk, data crunching is a work in progress at this point. Interviews with a new guy, who joined from Wartsila, talk about all the terabytes send back but not exploited yet. So, there's plenty of work to do. Hiring a guy from Wartsila says two things to me- routing LNG fueled ships to ECAs (in a new twist on 1970's style operations research type decision support), and Condition Based Maintenance, where data from vessels is analyzed to guide decisions on maintenance and overhauls. There is a real business case to perform such work when it's needed, as opposed to at set intervals which are simply best guesses (with some standard deviations thrown in, possibly) from manufacturers. And, when fuel injectors and the like are acting up, having such data beamed up through Global Xpress or similar, could also guide in vessel routings. All of these measures fit into categories of cost optimization. Where such computer systems (on the carrier side, looking at cylinder heads and, in the future, at things like whether scrubbers are gummed up, or not) begin to interface with those of customers (who, after all, are paying for the fuel in time charters, or in contracts indexed to fuel prices), then it gets interesting! When environmental incentives are thrown in, the $ numbers mount. Suppose that a group like www.shippingefficiency.org or RightShip had access to such data in real time? As a charterer or owner (including listed names) wanting to show its nice green face, that's an app that I would pay for!

And maybe some of the trade associations could follow the dictates of B-C-G and move outside the box in such directions. Attacks on overcapacity may indeed be futile; but new ways of cost optimization might be worth exploring.