Waiting for the deluge in the shipping world

There is an old French proverb, "Après nous, le déluge," that often has been attributed to an 18th-century king. Translated as "After us, the flood," it is frequently cited in reference to premonitions of the French Revolution.

Perhaps it should now be translated into Danish, to take into account the recent announcement that Maersk Inc. will acquire the liner shipping division of Sea-Land Service. For this transaction is likely to initiate a deluge in the ocean shipping world.

This trend toward increased consolidation is not new. According to Containerisation International, the top 20 liner steamship lines had 35% of the global vessel capacity in 1986. By 1995 that figure had increased to 46%, and this year it is estimated at 53%.

This trend is even more pronounced when looking at the capacity share of only the top 10 carriers — 22% in 1986 and 58% today.

Merger and acquisition activity has been constantly in the news. The creation of P&O Nedlloyd and NOL/APL have certainly drawn the biggest headlines, although CP Ships also put together a large, patchwork network with its multiple acquisitions. And Maersk is still busy with its acquisition of Safmarine and East Asiatic several years ago.

An acquisition such as Maersk's buy of much of Sea-Land would have been unthinkable even a year ago. The reason was the cargo-allocation system used by shippers signing conference contracts.

Sea-Land and Maersk shared many customers. A merger would have resulted in two plus two equaling three. To preserve routing options and flexibility, customers would have most likely reallocated at least part of their combined business to another carrier.

For example, when NYK acquired Nippon Liner Service, customers reallocated business among other lines. In fact, the sales forces of other lines focused on former NLS customers as an easy sell.

The Ocean Shipping Reform Act eliminated this problem. First, the ability to enter confidential service contracts caused conferences to disappear. Second, new service contracts can now address service — as well as pricing. Astute customers can negotiate service protection that will enable them to commit larger volumes to fewer contracts.

The future of steamship lines — and, in fact, of the entire industry — is one of consolidation. Terminal operators are already merging, and we are seeing the emergence of a handful of global terminal operating companies. The leasing industry also continues to consolidate. The two largest container lessors control almost half the world fleet.

In the meantime, steamship-line earnings suffer. Financial protectionism in Asia, where most of the major steamship lines live, has forced companies to realistically assess the profitability of their myriad business holdings. We are starting to see conglomerates broken up as unprofitable business holdings are abandoned.

Ocean shipping is a fiercely intense business with very low profitability. Shipping has become a commodity whose cost savings are usually passed on quickly to the customer by one line, with all other lines immediately following.

Steamship alliances were supposed to provide the economies of scope and scale that would ensure the survival of the lines. While there were major benefits to ocean linehaul, anticipated marine-terminal and inland-logistics savings never materialized. And further savings opportunities were never developed.

John Reeve, a shipping consultant, has examined the liner-shipping value chain and identified several areas of high merger benefit that had little alliance benefit. Sales and marketing, customer service, finance and administration represent such areas of possible improvement.

In addition, Reeve points out that the advent of e-commerce will have a major impact on the traditional ocean-shipping value chain. The liner industry is not providing e-commerce solutions to customers. In fact, many lines aren't able to provide basic EDP functionality.

Nevertheless, e-commerce is becoming a critical component of international supply chains and it is possible for the emergence of an "intermediary" that may sever whatever links are left between carriers and customers.

This would leave the ocean-shipping community two choices. A line could strive to be the largest carrier with the lowest cost structure so as to be the preferred commodity provider. This would result from rapid industry consolidation.

Alternatively, lines could try to become global logistics providers by developing the service networks and technology to support whatever customer requirements are specified. Either scenario implies an upcoming period of industry turbulence and consolidation.

Only a handful of liner-shipping companies are prepared to take on global logistics business. The rest will really struggle during this period. Mergers may be forthcoming as acquisitions, or national governments may decide to "assist" the combination of multiple liner companies into one.

In this case, countries with multiple shipping companies would consolidate into one. The possibility of consolidation within Greater China — in other words, the Peoples Republic of China, Taiwan, Hong Kong and even Singapore — even exists.

Ocean shipping has traditionally been a game of follow the leader. Today's leader is clear, as is its strategy. The betting as to who will be next has already begun.

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