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The Shipping Industry Finds an Unusual Survival Tactic in Outsourcing

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The outlook for the global shipping industry is less than promising for 2012. A December 2011 report by *Drewry*, a leading container forecaster, says that global port throughput growth in 2012 is expected to decrease by 1.3 percentage points. The shipping industry, which has a close link with the world economy, is currently saddled with multiple pressures resulting from the global financial crisis in 2008-2009, the more recent sovereign debt crisis in Europe, and of course the slowdown of the U.S. economy. Additionally, the cyclical nature of charter rates, intense competition, long build period of vessels and withdrawal of financial support from banks and financial institutions are adding to their woes.

However, two problems that are pushing this industry to the brink are oversupply and rising fuel prices. Although the recovery of economic activity is expected to resuscitate the shipping industry in the next few months, excess capacity and high fuel prices will weaken growth prospects.

Oversupply – Weakening Growth Prospects

In 2007-2008, the availability of cheap credit led many shipping companies to place orders for large vessels, most of which were either delivered at the end of 2011 or are being delivered this year. A recent International Transport Forum report calls the rush for capacity nothing but 'irresponsible investment'. Mr. Dagfinn Lunde, global shipping-expert and responsible for the shipping finance business at *Deutsche Verkehrs Bank* (DVB), said in the company's newsletter that the high growth period led many countries to increase their ship-building capacity.

International Shipping companies have expanded their fleets enormously over the past five years. The global tanker fleet has grown by 40 percent, the dry bulk fleet by 80 percent, and the container fleet by 90 percent, and order-books still remain substantial, points out a recent *Standard & Poor* Ratings report titled, *Top 10 Investor Questions: Oversupply and High Fuel Prices Sink Prospects for Global Shipping.*

Alphaliner, a consultancy firm focused on the liner shipping industry, expects fleet capacity to further rise by 8.8 percent during 2012 and 10.4 percent during 2013.

This oversupply is beginning to severely impact freight rates and bringing down the profitability of shipping companies. A report by Business Monitor International in 2012 titled, *Container Shipping: Replay of 2009 Threatens as Carriers Face Twin Threats of Declining Demand and Overcapacity*, states that the twin forces of overcapacity and declining demands could once again force down rates leading to further losses. The reduction in demand is attributed to declining consumption patterns due to the economic crisis.
The industry had seen a similar drop in demand during the recession of 2008-09.

Adding Fuel to the Fire

Rising fuel prices are further compounding the situation. Bunker fuel, which represents the major part of voyage expenses of shipping operators, has touched a five-year high price of about $720 per ton, compared with an average of about $630 per ton and a five-year low of $200 per ton in 2008.

Standard and Poor's analyst, Izabela Listowska believes that that puts pressure on shippers' operating expenses and hence their bottom-line earnings will continue to mount, if bunker fuel prices do not stop rising.

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The weak conditions prevalent in the shipping industry have had an impact on the credit quality of rated ship operators. *Standard & Poor's* has taken more than 20 negative rating or outlook actions on shipping firms over the past six months. Half of the 14 shipping operators that S&P rates globally have negative outlooks or are on CreditWatch with negative implications. There could be a further downgrade, if conditions do not improve.

Unusual Strategies for Unusual Times

Economic uncertainty, over-supply, a slump in demand and drying up of funding from financial institutions are clearly pushing shipping companies to the corner. To tide over the existing crisis, shipping majors are looking at ways and means to survive the storm even if it means adopting strategies, which are unconventional and were unheard of, until recently. As immediate measures to survive, the industry is forging non-traditional alliances, resorting to 'slow steaming' strategies, re-aligning services, pulling out from unprofitable routes. Some of these measures may seem untenable and are bound to send customer sentiments on a downward spiral.

Rivals Forging Alliances to Stay Afloat:

In 2011, the world's second- and third-biggest carriers, MSC and CMA CGM, forged a strategic alliance to overcome the crisis with a joint strategy and plan. A recent *Financial Times* report pointed out that CMA CGM exemplified the depth of the shipping industry's crisis by admitting during the announcement of the alliance, that it had made a $223 Million net loss on $3.86 Billion revenue for the third quarter of 2011.

To tide over the crisis created by a glut of container ship capacity, both the carriers abandoned traditional rivalries to join hands and formed a partnership spanning several key markets, including Asia-Europe, Asia-Southern Africa and the South American trades. Some industry analysts believe the alliance could re-write the liner industry and may work towards deepening the line between the top three liners and the rest of the competition. The new partnership, with a combined capacity share of 22 percent, is poised to become the leader in the Asia-North Europe trade. The top three Japanese shipping lines – Mitsui O S K Lines (MOL), *Nippon Yusen Kaisha* (NYK Line) and “K'' Line – as well as other smaller lines, including Israeli company ZIM, are also considering alliances to consolidate their position in the market.

‘Slow Steaming' to Cut Costs:

Desperate times indeed call for desperate measures. Driven by losses to the point of near-extinction, global container fleets have started cruising at record-low speeds. Global liners have resorted to this 'slow steaming' approach to cut down on fuel consumption. The *New York Times* recently reported that *Maersk* cut fuel consumption on major routes by as much as 30 percent, by halving its top cruising speed over the last two years.

Carriers across the globe - from Germany to Israel to China are beginning to embrace the 'slow steaming' strategy. According to estimates, today more than 220 vessels are practicing “slow steaming” — cruising at 20 knots on open water instead of the standard 24 or 25 — or, like Maersk's vessels, “super slow steaming” (12 knots).

Pulling Out of Non-profitable Trade Routes:

Many established carriers are pulling out of their non-profitable routes in a bid to prevent losses. According to the second Global Shipping Benchmarking Survey conducted by PricewaterhouseCoopers in 2010, of around 110 global shipping companies covered in the study, 23 percent looked at optimization of network and capacity by adopting measures like re-organizing their fleets and reducing services by pulling out ships.

Maersk Shipping Line, the world's largest container shipping line, has cut its capacity on the Asia-Europe route as a profitability measure to counter the Euro zone debt crisis. Rival shipping company, Orient Overseas (International) Ltd., also announced measures to pull down shipping capacity on this route by 20 percent to maintain profitability amid the market slowdown, as reported in a recent issue of the *Wall Street Journal*.

With formidable challenges facing them, the liner business is continuously seeking opportunities to overcome obstacles and maintain steady growth. Shipping companies will need to re-structure and introduce deep-rooted methods to achieve operational excellence while riding out the economic uncertainties. Now is the time for newer, longer-term business strategies to guard against similar crises in the future and seize new, emerging opportunities. New strategies for growth call for deeper insights into planning, domain expertise to understand the unique characteristics of the industry and strong implementation capabilities.

Outsourcing of processes to bring in higher operational efficiency, lower costs and enhanced customer satisfaction can provide the industry answers to many of its problems.

Outsourcing – A Precise Strategy for Testing Times:

In the current shipping market, outsourcing is emerging as a necessity for shipping companies to maintain a competitive edge in the market. An experienced BPO partner with deep domain expertise and a track record of bringing in operational excellence can be the buoy companies are looking for to cope with the volatility in the industry. Global shipping companies are increasingly focusing on outsourcing as a long-term strategy for operational excellence, sustainability and growth. Ocean carriers like Maersk, Hapag-Lloyd, APL, MOL and CSAV began their outsourcing journey through captives in low cost countries such as Malaysia, India, the Philippines and China.

But several of them are realizing that the costs of managing a captive in these testing times may far exceed the benefits. Shipping companies are exploring the option of engaging with a third-party outsourcing company for their outsourcing needs.

A trusted outsourcing partner with the right mix of expertise in terms of processes, people and platform can deliver outsourcing solutions that go beyond cost arbitrage and are targeted to mitigate industry-specific pain points. An experienced BPO player with in-depth domain knowledge and expertise in complex processes, such as shipping documentation, customer service, terminal operations and analytics-driven vessel plans can help shipping companies reduce the risks related to market volatility and gain an edge in the market. An outsourcing partner with global delivery capabilities also meets the regulatory needs of global companies.

With a recovery in the shipping industry expected only in 2013, shipping companies need to gear up for another challenging year ahead and adopt innovative measures to remain competitive in the market. Companies need to look beyond mere survival and adopt sustainable growth solutions that will impact its business impact in the long run.

WNS provides industry-specific solutions to the shipping companies and enjoys a strong industry track record. WNS can help companies weather the storm and build a strong foundation for steady growth in the years ahead.

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