



For better or for worse – 'till bunker prices do us part

How can container lines remain viable amid spiralling bunker prices? **Arjun Vikram-Singh**, CEO of Quantum BSO, says the industry is not equipped to handle dramatic cost increases and argues real time costing and pricing is the only way forward



Some people in ocean transportation may remember the prediction five years ago by Arjun "Spike" Murthy about what would happen to the price of oil. The prescient 38-year-old managing director of Goldman Sachs predicted in 2003-04 that the then US\$30 barrel of oil would reach \$80. Such a prediction was at the time dismissed as preposterous. In 2005, when oil was trading at \$50, he predicted \$100 per barrel - but again few people took note.

But hear this - he recently upgraded his prediction to \$200 per barrel.

Considering the implications of this for the container industry, the absence of serious discussion on the matter is deafening! For those who are listening, we could well hear the distinct change in pitch as super-sized container ships wind down their revs and trade off fuel cost economy for relatively smaller increases in charter hire costs and longer transit times.

For years now, the container industry's innovation has stood on the platform of economies of scale. The giant boxships have been in turn filled by advances in supply chain management and the globalisation of production and inventory.

Mainstream carriers have mostly marched to battle by selecting bigger tonnage as their weapon of choice. Price barriers and cost challenges impacted or negated their bottom lines.

Bigger seemed the way to go, with the average shipping manager reasoning that a larger denominator obviously meant lower costs. It has also ushered in an era of enormous propulsion units that gobble huge amounts of fuel.

The horizon of opportunity seemed endless, but maritime history marched on to other centres of control. The primacy of the steamship line gave way first to the freight forwarder then to many tiers of logistics

companies. As the distance and layers increased between the line and its client, the profit dynamics certainly did not improve.

The container shipping line appears today to be operating a large number of ships, incurring dramatic capital expenditure, pre-funding a majority of global trade, but making a mere sliver of margin on their top line.

Perhaps a deeper look into this camel of the ocean is called for

In the first instance, there is a dramatic lack of differentiation in the container trade - after all how different can one make carrying a box from point "A" to "B". Operators have tried a number of tactics; larger networks, more types of containers, an illusion of customer service, nascent e-commerce, pricing or saving a day or so in transit time.

All things being equal, perhaps the biggest differentiator is who gets things the least wrong. That may be the cynic's view



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of the business, but as all operators will confidentially acknowledge, containerisation is far from an exact or standardised business.

More containers get shut-out or rolled over in a day than the entire volume of the misplaced luggage at Heathrow T5's recent disaster. Comparatives for the document rework (Bill of Lading and other) or invoicing and calculation errors are hard to find, just as it is near impossible to get clear, concise and trustable track & trace information from most operators.

While technology is dramatically called for in every line's core operating system, there is perhaps no area that calls for it more than in areas of business intelligence, Yield & Contribution and Optimisation of Service. All of these have direct impact to the company's bottom line and the viability and sustainability of business.

Some years ago when I headed a region and had a corporate position in a large container line, the senior management seemed to manage by "gut" instinct. They had an excellent understanding of the business, the scope and pace was manageable, and the cadre of managers and professionals was excellent. IT tools were basic, but Excel seem to fill the gap!

Today however, the predictability on which we made our fundamental decisions has shifted, and many a manager at the helm of a large line is "at sea." All of the assumptions and familiar indices are no longer valid and the consequence and ramification of each aspect of the transport chain is monumental.

The commercial transaction in volume and income terms is significantly larger than previous years as is the operational cost – recent bunker and charter hires need no highlighting. The current liner executive faces challenges that their predecessors could only have vague nightmares about. Unfortunately, IT systems and decision support tools remain woefully inadequate for today's tumultuous tradelanes.

A \$50/teu rate shift between Hong Kong and north Europe can have dramatic impact on the bottom-line; just as currency fluctuations, the loss of a key account, or a trade reversal can have. With most managers (still) not having clarity into their cost base, many of them end up pricing within the market range rather than targeting specific margins and yields.

There are of course solutions to this widespread malady that effects containerisation:

1. There is an urgent need for most container shipping lines to bring in high quality integrated core-operating (ERP) systems that are capable of handling business that run into a multi-billion dollar top-line. These systems need to be based on the latest technology, be completely integrated, eliminate manual key-strokes and duplication, and bring quantum efficiencies to the bottom line.

2. Shipping Lines also need to invest in Decision Support Systems or DSS, that may range from independent components or a suite of the following:

- a. Contribution Management: essentially, each granular element of the business should be mapped for its cost-of-service and thereby when pricing is planned or carried out, the bottom-line is crystal clear. Contribution analysis that is penetrative and accurate should form the foundation of commercial best practice.
- b. Capacity Management: most lines have internal capacity management in one form or another that focus principally on opportunity (bookings) and delivery capacity (space), but few if any work so that the best paying, light weight, optimum container types may be selected. This better cargo selection alone drives a profitable ship – not just a full ship.
- c. Yield Management: this is a step up from Contribution Management, where an optimisation engine is integrated to allow simulation of shipment, voyage, trade or other returns. A yield management system, as used in hotels and other industries allows dynamic pricing with the user being able to mark-up in windows of scarcity or avoid losing trades.
- d. Stock (Equipment) Optimisation: in 2006, one of the top container lines spent over \$1bn in the repositioning of its empty containers, and in 2008, there surely will be many more dollars expended. Questions must be raised on how to manage and flow the surpluses economically, and importantly, how to attain commercial targets while dramatically reducing cost of imbalances. This is of course not a simple matter, for either man or standard software, but is

well within the purview of optimisation systems – used by airlines and airports the world over – even by some major container terminals.

- e. Fleet Optimisation: the airline industry can model the most appropriate equipment (aircraft) to a route keeping in mind booking volumes, ticket sales, operating costs etc. Today this is a fundamental of most airline operations. But as I have mentioned earlier in this article containerisation is seeking to mitigate bunker cost impacts in a far more rudimentary (read excel) form.
- f. Business Intelligence: and finally – Business Intelligence with dashboards, analytics and reports on the fly. Tools exist today to put the business manager "in the know" which means that if he is not distracted by the basics of decision-making, then he can apply his knowledge strengths to winning and serving the best clients.

I am fortunate that I run a business solutions & technology company and not a large container shipping line. Yet for all of us serving the container industry, Arjun "Spike" Murthy (the shared first name is purely coincidental I assure you) has perhaps provided the catalyst to one of the most important debates – will the container business as we now know it make sense at the likely cost of fuel? This is not an easy argument because while BAF/FAF are direct recoveries where carriers feel they may have an offset, actually, they are only skimming the surface of the effect of a high-priced barrel of oil.

Let's face it; there is a dramatic cost push in new tonnage, of container box leasing, haulage, office operation, salaries, and even business travel – everything.

The industry faces too many variables to apply a knee jerk chasing of recoveries. Neither will bigger ships be the competitive solution in this chaotic business environment. Real time costing and pricing models will be the best tool for navigating today's turbulent tradelanes. ■

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