

# Staying Afloat

**Gary Ferrulli | Jan 12, 2012 6:45PM GMT**

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Ocean carriers are at a turning point. The financial results paint a picture of an economically troubled industry that has grown by leaps and bounds because of global trade, yet is unable to take full advantage of that growth because it flooded the market with capacity just as the downturn hit.

The results are compounded by what many familiar with the industry believe is its Achilles' heel: self destruction brought about by allowing overcapacity to drive down rates, even as global volumes were growing, sinking carriers back into the red after a breakthrough 2010.

We're also seeing what some think is a war of wills, or at least of philosophy. For decades, the industry has been filled with a combination of "national interest" and "family owned" businesses. As we roll into 2012, the world's largest carrier appears to be flexing its broad-based corporate muscle to thin the herd. With a laser focus on particular segments of the Asia-Europe market, Maersk Line did what many have been challenged to do for decades: By launching the Daily Maersk service, it's created a real differential between itself and all others.

Some scoffed at the idea, a 70-ship string dedicated to, in essence, a trade. If early results are an indication, Maersk may have found a true differentiator. In the first 10 weeks of operation, the carrier's market share in the trade grew from 22 to 28 percent. Some say it's because Maersk lowered rates, but many have lowered rates without this level of success.

In the process, Maersk delivered another message: It launched Daily Maersk with 70 relatively large vessels, and still has more than 500 to compete in other lanes. It used only 11 percent of its existing fleet, and still has 20 18,000-TEU ships waiting in the wings.

But others aren't sitting still. Mediterranean Shipping and CMA CGM created their own stir by announcing a vessel-sharing agreement in multiple trades. The combining of parts of their large fleets makes them what could be viewed as an entity with more vessels and capacity than Maersk.

But they're not an entity; they're still two companies with other partners in other trades with other vessels.

Looked at carefully, this isn't a direct reaction to Daily Maersk; it's a series of actions meant to strengthen their overall competitiveness in global trades, not a singular focus.

Then there's the new G6 Alliance, or maybe the New Grand World Alliance, another vessel-sharing agreement said to cover services in nine trades. Like the CMA CGM-MSC alliance, it's an attempt to strengthen the market presence in specific trades in a way that none of the six carriers — APL, Hyundai Merchant Marine, MOL, Hapag-Lloyd, NYK Line and OOCL — could have done on their own.

These actions account for nine carriers, leaving the intentions of many large carriers a mystery. It also raises questions regarding those in and out of these activities. Is the rumored combination of Japan's Big 3 container operations dead? Not necessarily. I think combining the three would be a smart business move; it would give the entity size and scale as well as slash redundant costs.

What about others? Evergreen's policy of refraining from building five-digit-TEU ships makes it difficult for the Taiwanese carrier to compete from a cost perspective, while maintaining a virtual interchangeable fleet. But if you can't compete cost-wise, and rates aren't high enough, how do you survive?

There are a couple of realities in all of this. First, we have talked about relatively few of the carriers plying global trades today. That doesn't mean they aren't viable, but it suggests that each must have a plan to cope in this new environment, and that's going to be difficult. The other reality addresses operating costs. Yes, each carrier in an alliance gets to share costs and thus lowers its theoretical cost of having the same capacity by itself, but neither does it have the capacity. It's a tradeoff with less theoretical risk.

The name of the game must be cost control for the next several years as carriers allow global trade to catch up with capacity while hoping rates rise to long-term sustainable levels. Alliances don't address that long-term cost-to-revenue issue because, as in the G6, there are six fully compensated staffs, six sets of systems to operate and maintain, and six sets of offices, communications and advertising.

Although these aren't the largest part of the cost structure, they add up to more than 15 percent of spending — enough of a burden to make a difference. Hypothetically, take the three Japanese carriers, combine them and, over time, reduce their total staffing by half, operate with and maintain one system, one set of offices, one advertising budget and one

communications department. That can be the difference between surviving and not.

We are reaching that point where decisions already made, and those being made, have set into motion the scenario of who will survive over the next five to seven years. Some won't last three years, and some could be gone within 18 months. Some may turn into niche players, where they won't need 14,000-TEU ships to compete. And some may be betting the behemoths will annihilate each other, with the more conservative approach allowing them to survive until then — or until a giant meteor hits the earth.

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