

Logistics in the automotive sector. On the margins of a crisis.

06/Oct/2008



The global car industry is in crisis. Possibly the most severe crisis it has been in for 50 years. Not only is it going through a period of pressure on profitability that in any other sector would lead to drastic consolidation but its technological fundamentals are undergoing a transformation.

The evidence of that change is strongest in the US, where what used to be called the 'Big Three' – Chrysler, Ford and General Motors – are in the financial equivalent of intensive care. The US market has also seen the most dynamic market for new types of vehicles. Once the homeland of the V12 SUV, hybrid engine cars from Toyota and Honda are now the most dynamic part of the US car market. The President of Honda, Takeo Fukui, has said he expects more than 10% of Honda sales worldwide to be hybrid vehicles, a total of 500,000 vehicles. That is only part of a wider transformation in automotive technologies that embraces new fuel sources, new materials and digital technology.

So what are the implications of all this change for logistics in the automotive sector? So far very little, as the vehicle manufacturers are still wedded to their traditional dominance of the supply chain.

Crisis in the supply chain

One of the key problems in the sector remains the crisis in the automotive supply chain. A high proportion of automotive suppliers are either bankrupt – such as Delphi – or have begun to grow away from the sector – for example, Bosch. That has been driven by the endemic unprofitability of the sector, the aggressive purchasing methods of many of the vehicle manufacturers and the industry's low growth prospects in key western markets.

Those problems are usually thought of as applying to component suppliers. However, they equally apply to logistics service providers. A good example of that in the logistics sector is Ryder. Once dominated by big automotive customers such as General Motors and Toyota, plant closures across the US have caused major challenges to Ryder's Supply Chain Solutions business. The dramatic downsizing of the automotive sector means that the electronics OEMs (original equipment manufacturers) are becoming the driver of its business.

The issues for automotive logistics are not just restricted to problems over price and growth. Rather, the way the vehicle manufacturers approach logistics outsourcing and the opportunities they offer logistics service providers is making the sector less attractive.

Toyota is a good example. Increasingly unchallenged as the leader of the automotive industry, the company has a tight grip on outsourcing. In both North America and Europe, for example, the car manufacturer has just completed the construction of its own finished vehicle distribution system that includes a network of seven European port-based 'vehicle distribution centres' which manage the inventory and transport of its cars to dealerships. In the US, Toyota has even created its own fleet of car-carrying trucks. For such a client, the opportunities for 'added value' hankered after by the big LSP's (logistics service providers) are limited.

Exceptions to the rule

However, there are still opportunities in the sector. An example is DHL Exel Supply Chain's new contract with the Tata-owned Jaguar-Land Rover business based in the English Midlands region.

Purchased from Ford by Tata at the beginning of 2008 for £1.15bn, Jaguar-Land Rover is still dependent on major components from Ford but has ripped out Ford's production and logistics systems. Faced with the need to construct a materials management system from scratch, Jaguar-Land Rover embraced the concept of outsourcing to a lead logistics supplier. The result is an LSP's dream – a contract for the management of the entire inbound logistics of three assembly plants at Castle Bromwich, Halewood and Solihull in the English Midlands.

After competing with NYK Logistics, the LSP which ran inbound transport at the plants for Ford, DHL Exel Supply Chain won a contract worth £150m. DHL now manages the 'milk round' that collects components, consolidates them and then distributes them around the plants. DHL Exel now even manages the movement of materials within the Jaguar-Land Rover factories, effectively taking control of 'line-side' component-feed. That is really most unusual, with only Schenker's role at the VW plant in Hannover, Germany or Ceva's role within FIAT being comparable contracts in Europe. Indeed it is DHL Exel Supply Chain's largest single automotive contract, bigger even than its 'milk round' contract for BMW in Germany. Paul Dyer, managing director Automotive UK, observed that: "This contract is unique in the fact that it encompasses all of our inbound products, i.e. LLP services, UK and EU collections, in-plant and sequencing, all wrapped up into an integrated offering".

What this example illustrates is that the prospects for extensive outsourcing contracts for logistics service providers largely lie at the periphery of the automotive sector. Either smaller specialist providers who lack scale or plants in geographically hard to supply locations are likely to offer prospects for logistics service providers. Fortunately for logistics service providers, that periphery is quite dynamic, with many niche players and new entrants such as Tata.

Car Carriers

Not that all areas of automotive logistics are gloomy. If you want to make money in automotive logistics there can be few better places than deepsea car carriers. The demand for inter-continental movement of vehicles is growing yet there is a limited supply of the sophisticated ro-ro vessels they operate. Consequently, leading providers such as NYK and WalleniusWilhelmsen Logistics (WWL) are experiencing a high level of profitability and a doubling of revenue.

According to WWL, its volume is growing by 7-10% a year, with WWL moving 2.3m CEUs (car equivalent units) per annum. Indeed, WWL's CEO Arild Iversen observes that demand is so great that WWL is "stressing the system" with a potential utilisation rate of 104-5%.

However, those figures hide a murkier reality. The vehicle manufacturers are supremely aggressive in their pricing and even for a dedicated automotive logistics service provider such as WWL other markets are more attractive. For example, 60% of WWL's loads by volume (CEU) are cars. However, that accounts for 50% of revenue. The really lucrative and dynamic part of the car carrier market is 'high-heavy' cargo such as capital equipment vehicles or project cargo such as boats or equipment for the energy sector.

Of course a company such as WWL is not going to turn away from its core business of moving cars worldwide but clearly the company's business has changed from 10 years ago when 70%-80% of it was cars. So even in a sector as apparently automotive-dedicated and as profitable as car carriers, players are gradually diversifying away from reliance on the big vehicle manufacturers. Indeed, WWL's experience with its disastrous investment in the French logistics company Groupe CAT – where Renault played one WWL shareholder off against another – only illustrates the difficulty of doing business with the big vehicle manufacturers.

Yet the very international nature of WWL assures it and the other big car carriers a rewarding position in the automotive sector. Within the past few years, the profile of the global automotive market has been transformed. Russia has the potential to be a larger market than Germany, whilst China could be as large a market as the US within a decade. The location of assembly plants has also changed, with plants designed to serve markets in Europe opening in Turkey and North Africa, whilst some China-located production is being exported worldwide. So the continuing complexity of finished vehicle movements means that demand for car carriers will continue to be reasonable, if hard to predict. If, as WWL's Iverson insists, "the Indians and Africans have the right to have cars as well", growth is set to be long-term.

However, the final element in the uncertain future of automotive logistics remains the production technology of vehicles. Until recently, the 'metal bashing' methods of producing cars had not changed much in several decades. However, the pace of innovation in automotive engineering is increasing amazingly quickly, forced by the demand for more fuel-efficient vehicles.

That is likely to have big impact on supply chains. The increasing dominance of electronics, in particular, is likely to drag automotive production away from its 'local-for-local' model towards more global sourcing. Greater use of polymers and technologies such as batteries will do likewise. That must be viewed as a major opportunity for large LSPs to replicate the market penetration that they have achieved in sectors such as consumer electronics, for example, with the growth of their freight forwarding businesses.

Source: Transport Intelligence, Oct 06, 2008

© 2008 TI Briefing. All rights reserved. Republication or redistribution, including by framing or similar means, is expressly prohibited without prior written consent. TI Briefing is a service from Transport Intelligence Ltd. Transport Intelligence shall not be liable for errors or delays in the content, or for any actions taken in reliance thereon.