

## What does the next phase of the economic cycle hold for the logistics industry?

08/Sep/2009 by John Manners-Bell



In his keynote speech at Global Distribution Strategy conference, October 6-7, 2009, Brussels, Ti's Chief Executive, John Manners-Bell, will talk about prospects for the logistics industry. In his speech he outlines three scenarios for the market: 'golden', 'difficult but manageable' and 'meltdown'.

With many sources claiming that the worst of the economic downturn is now over and that the recovery may only be a few months off, it is an appropriate time to assess the state of the market, and suggest how things will change in the near future.

So far the market has reacted in exactly the way in which classical transport market economics theory would suggest. As volumes fall at the end of the economic cycle, capacity (air, sea and road) has outstripped demand. This leaves freight rates in freefall, hurting carriers, but allowing freight forwarders to increase their margins as they take a larger slice of a diminishing pie.

There is plenty of evidence, anecdotal and otherwise, to suggest that enough capacity has been removed from the market to allow carriers to slowly increase their rates. This is helped of course by volumes in the last quarter improving on a month-by-month basis. This will lead to a more positive market environment for the carriers, and although forwarders will find margins squeezed, they will benefit from higher revenues and profits.

So far so good. However things may not be that straightforward given the unique underlying causes of the recession. Ti has identified three scenarios, all of which will have very different implications for the global logistics industry.

The first 'golden scenario' will be a return to growth following the bust, but in a low interest rates and low fuel cost environment. These two factors are important for carriers as they account for a large proportion of variable costs. Volumes will increase in line with growing consumer confidence, and rates will harden until capacity catches up with demand.

The next scenario is less positive. As the economy recovers, volumes increase but so does the price of fuel as demand for oil grows. This increase translates into higher inflation, which Central Bankers try to control with higher interest rates. Carriers find themselves struggling to pass on their higher input costs to clients, and consequently, despite higher revenues, continue to work on negligible margins. Some inevitably go out of business and forwarders find themselves squeezed too. The market can be characterised as difficult, but manageable.

The final scenario, and the worst from everyone's perspective, is 'stagflation'. Volumes remain flat, but inflation, stoked by the vast amount of money which has been pumped into economies by the Central Banks in so-called stimulus packages, becomes engrained. Interest rates are raised to control inflation, but have the side-effect of suppressing economic growth further.

This last scenario is worse than the reality of the present downturn – at least carriers have not had to contend with high oil and interest rates. It would result in a structural transformation – a 'meltdown' in fact – of the industry as capacity is driven very quickly out of the market. Some (the survivors) may

see this as a good thing in the long term, although it would not suit forwarders which work best with a large pool of high quality, but low cost suppliers.

To a large degree the logistics industry's future is very much at the mercy of the administrators and bankers who brought about the present economic crisis. If they are able to navigate the global economy out of the present recession without making things worse, carriers and forwarders can probably look forward to the second scenario outlined above: difficult, but manageable. However the 'meltdown' can not totally be ruled out as very few economists, if any, have much of an idea what the effect of printing so much money (so-called quantitative easing) will have on the global economy.

**Source: Transport Intelligence, Sep 08, 2009**

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