PEPERIKSAAN AKHIR SEMESTER KEDUA SESI 2011/2012
FINAL EXAMINATION SECOND SEMESTER 2011/2012 SESSION

KOD / NAMA KURSUS : BPMN 3023 / PENGURUSAN STRATEGIK /
COURSE CODE / NAME : STRATEGIC MANAGEMENT

TARIKH / HARI : 14 JUNE 2012 (KHAMIS / THURSDAY)
DATE / DAY

MASA : 09:00 AM - 11:30 AM. (2.5 JAM / HOURS)
TIME

TEMPAT : KYM/ PMI/ IKIP/ NEGERI/ KTB/ KIA/ DMS/ DSB K.T/WD/ DTSO /
VENUE DSB K.TM/ TE/ MKM.

ARAHAN :
1. Kertas peperiksaan ini mengandungi LAPAN (8) SOALAN dalam EMPAT (4) halaman bercetak tidak
termasuk kulit hadapan.
2. SATU (1) kajian kes The Liner Shipping Industry disertakan.
3. Anda dikehendaki menjawab SEMUA soalan pada buku jawpan yang disediakan.
4. Calon TIDAK DIBENARKAN membawa keluar kertas soalan dan buku jawpan dari Dewan
Peperiksaan
5. Calon adalah tertakluk di bawah TATACARA PERATURAN KECURANGAN AKADEMIK, UUM.

INSTRUCTIONS:
1. This examination paper contains EIGHT (8) QUESTIONS in FOUR (4) printed pages excluding the cover
page.
2. A case study on The Liner Shipping Industry is attached.
3. You have to answer ALL questions in the answer book provided.
4. Candidates are NOT ALLOWED to take both exam question and exam sheet out of the Exam Hall.
5. Candidates are bound by the UUM's RULES AND PROCEDURES ON ACADEMIC FRAUD

No. MATRIK: ____________________________
MATRIC No: ____________________________
(dengan perkataan / in word)
(dengan nombor / in number)

No. KAD PENGENALAN: ____________________________
IDENTIFICATION CARD No: ____________________________

PENSYARAH: ____________________________
LECTURER: ____________________________

KUMPULAN: ____________________________
GROUP: ____________________________

JANGAN BUKA KERTAS PEPERIKSAAN INI SEHINGGA DIBERI ARAHAN
DO NOT OPEN THIS EXAMINATION PAPER UNTIL INSTRUCTED
BAHAGIAN A / SECTION A

SOALAN SATU/ QUESTION ONE (10 MARKAH /MARKS)
Tuliskan nota-nota ringkas mengenai perkara-perkara berikut:

Write brief notes on the followings:

a) Model pembiayaan
   Business model (3 markah/marks)

b) Persumberan luaran
   Outsourcing (3 markah/marks)

c) Krisis hutang Eropah
   European debt crisis (4 markah/marks)

SOALAN DUA/ QUESTION TWO (20 MARKAH / MARKS)
Imbasan persekitaran dalaman dan luaran ialah sebahagian daripada proses Pengurusan Strategik.

Scanning of the internal and external environment is part of the Strategic Management process.

a) Senaraikan tujuan membuat aktiviti imbasan persekitaran
   List down the purpose of undertaking the environmental scanning activity. (5 markah/marks)

b) Apakah input-input yang berlaiman yang boleh diperolehi daripada aktiviti imbasan persekitaran ini?
   What are the different kind of inputs that can be obtained from the scanning activity? (11 markah/marks)

c) Jelaskan mengapa perlunya seseorang memulakan analisis sesuatu kes dengan analisis kewangan?
   Explain why should one begin a case analysis with a financial analysis? (4 markah/marks)
SOALAN TIGA / QUESTION THREE (18 MARKAH/MARKS)

a) Nyatakan EMPAT (4) jenis pakatan strategic dan terangkan setiap pakatan-pakatan tersebut.

Name FOUR (4) types of strategic alliances and explain each of these alliances.

(10 markah/marks)

b) Nyatakan DUA (2) perbezaan antara strategi-strategi di bawah ini, beri contoh bagi setiap satu.

State TWO (2) differences between these strategies below, with an example for each strategy involved.

i) strategi kepimpinan kos dengan strategi kos fokus

cost leadership with cost focus

(4 markah/marks)

ii) strategi pembezaan/ kelainan dengan strategi pembezaan/ kelainan fokus

differentiation with differentiation focus

(4 markah/marks)

SOALAN EMPAT/ QUESTION FOUR (6 MARKAH/MARKS)

Kita sentiasa mendengar berkenaan pihak pergurusan atasan yang membicarakan tentang perluinya untuk mengubah budaya korporat sesuatu syarikat. Akan tetapi mengubah amalan-amalan yang telah menjadi kebiasaan itu bukanlah mudah dan selalunya berakhir dengan kegagalan. Walau bagaimanapun sesetengah inisiatif perubahan perlu juga dilaksanakan untuk mengubah budaya yang negatif. Senaraikan langkah-langkah yang anda fikir boleh membawa kepada perubahan budaya dalam sesuatu syarikat.

We always hear top management of firms discuss on the need to change a firm’s corporate culture. But changing practices that become habit is not easy and generally end up with failure. However, some change initiative need to be carried out to change negative culture. List out the steps that you think can lead to cultural change in a firm.

(6 markah/marks)
SOALAN LIMA/ QUESTION FIVE (6 MARKAH/ MARKS)


Akan tetapi beliau merasakan bahawa satu analisis mengenai strategi yang dilaksanakan dan program sama ada yang berjaya atau gagal pada tahun 2011 sepatutnya dibuat sebelum mensasarkan matlamat yang lebih tinggi untuk tahun 2012. Secara amnya syarikat Hiburan Hallyu perlu tahu strategi dan program yang mana membawa kepada jualan yang tinggi dalam tahun 2011 dan mana yang tidak. Beliau sedang memikirkan sekiranya ada satu proses yang boleh beliau gunakan untuk analisis ini.

_The CEO of Hallyu Entertainment was thinking on the performance of his company for 2011. His company was in the entertainment business, in charge of 4 groups of male and female singing groups in the genre of what is known as 'K-pop' or Korean popular music. The CEO knew that the Board of Directors of Hallyu Entertainment would like to set a high KPI (Key Performance Indicator) for Hallyu Entertainment in 2012 of reaching USD200 million dollars in global sales.

However, he felt that an analysis of the strategies put in and programs that were both successful and unsuccessful in 2011 should be done before setting a high goal in 2012. Basically, Hallyu Entertainment need to know which strategies and programs led to high sales in 2011 and which did not. He wondered if there was a process that he could use to do this type of analysis._

a) Apakah proses yang CEO ini boleh gunakan untuk membuat analisis ini?

_What is the process that the CEO could use to do the analysis?_ (2 markah/marks)

b) Lakarkan proses di atas dan labelkannya.

_Draw the above process and label it._ (4 markah/marks)
BAHAGIAN B / SECTION B

(Soalan-soalan 6-8 dalam bahagian ini merujuk kepada Kajian Kes: The Liner Shipping Industry yang dilampirkan dalam kertas peperiksaan ini).

{Question 6-8 in this section refers to the Case Study: The Liner Shipping Industry, attached in this exam paper}

SOALAN ENAM/ QUESTION SIX (10 MARKAH/MARKS)

Tulis satu abstrak untuk kes yang diberikan.

Write an abstract for the case given.

(10 markah/marks)

SOALAN TUJUH/ QUESTION SEVEN (20 MARKAH/MARKS)

Dengan menggunakan Lima Gerak Kuasa Michael Porter, jalankan analisis tentang kesengitan persaingan dalam industri ini. Anda perlu menyatakan tahap untuk setiap gerak kuasa ini (sama ada tinggi, rendah atau sederhana) selepas membuat analisis tersebut dengan memberi alasan untuk setiap satu.

By using the Michael Porter Five Forces, perform an analysis of the competition in the industry. You need to state level for each forces (high, moderate or low) after conducting the analysis with justifications for each forces.

(20 markah/mark)

SOALAN LAPAN/QUESTION EIGHT (10 MARKAH/MARKS)


Based from the above analysis of Michael Porter Five Forces, make a decision whether the industry is an attractive industry to join. Provide your justification.

(10 markah/marks)

SOALAN TAMAT
‘END OF QUESTIONS’
INTRODUCTION

The shipping industry is among the oldest and largest in the world. As the primary means of transporting the majority of the world’s cross-country cargo, the shipping industry is fundamental to trade, globalization, economic growth, and prosperity. It is inconceivable that global trade could exist or prosper without the shipping industry. Yet the importance of the industry did not translate into an easy or profitable environment for shipping firms in 2008. Instead, the industry exhibited several characteristics that challenged shipping firms, particularly liner shipping firms.

CONTAINER SHIPPING

The shipping industry comprises firms that provide seaborne transportation of heavy, bulky, or non-time-sensitive cargo between harbors. Sea shipping was possibly the first truly global industry, as firms from many different countries moved cargo between ports around the world. The vast majority of the world’s global trade is transported by sea, with shipping moving about 90 percent of global cargo by volume and 70 percent by value in 2008.

There are three main segments in the industry. Bulk carriers transport bulk cargo such as coal, cement, wheat, oil, and gas. The second segment uses specialized ships for the transportation of specialized cargo such as automobiles and other wheeled cargo. The bulk and specialized cargo segments are viewed as separate businesses from the third segment, container shipping, which moves cargo on ships designed for carrying cargo in containers.

The invention of the container in 1956 radically transformed the shipping industry from the 1960s onwards. Containers allowed more efficient packing of cargo, standardized handling and equipment, reduced loading and unloading times at ports, improved transportation and tracking of cargo on land and sea, reduced loss and damage, and better use of shipping space and time. The gains from using containers were so great that by 2007, it was estimated that more 25 percent of the volume and more than 70 percent of the value of global seaborne cargo was shipped in containers. Most containers were 20 or 40 feet long, which led to the industry standard for measuring shipping in terms of twenty-foot container equivalents units (TEUs) or forty-foot container equivalent units (FEUs). Exhibits 1 and 2 show the growth of containerized and general seaborne trade.

INDUSTRY TRENDS

Although the leading shipping lines originated in traditional “seafaring nations,” particularly in Europe, consolidation and new entrants led to a diversity of firms in the industry from the 1990s onwards. With relatively few barriers to overcome, many new shipping firms entered the industry in the 1960s and in the following decades. Many governments felt it necessary to have one or more national shipping lines to support trade and national development, and supported the entry of their flag carriers. Many developing countries, in particular, introduced their own shipping fleets. From the late 1990s, new Chinese shipping lines entered the industry.

The shipping industry tended to experience the same cyclical trends as global trade, which in turn depended on the health of the global economy. In general, the growth rate in container shipment was three to four times the world economic growth rate. Container volumes grew by about 7 percent per year in the 1960s, accelerating to 10 percent annual growth in the 1990s. Global economic growth, and growth
in East Asia in particular, increased foreign direct investment, resulted in greater dispersion of production across countries and regions, and increased demand for commodities, thus significantly increasing trade and the demand for shipping from the 1980s.

To meet increased demand, capacity in the shipping industry grew rapidly from the 1970s. By the early 1980s, capacity exceeded demand, and continued to do so in the following decades. Capacity grew by as much as 15 percent annually in the 1990s, almost doubling during the decade. Exhibits 3 and 4 provide information on container shipping volumes on major routes and liner shipping capacity.

Three main routes accounted for the majority of container shipping: the transpacific, transatlantic, and Asia–Europe routes. As Asia grew in the 1980s and 1990s, traffic on the transpacific routes grew fastest, making it the busiest route. However, rapid growth in Asia–Europe trade had made this the busiest route by 2008. In general, intercontinental shipments were substantially larger than intracontinental shipments.
The exception was within Asia, where transshipments or direct shipments amounted to more than 9 million TEUs in 2007.

The Asian economic crisis of 1997–1998 caused severe recessions in many East Asian economies, affecting trade badly. As a result, shipping volumes
and rates fell. A recovery in world economies in 2000 led to an increase in trade, shipping volumes, and average rates. Although many shipping liners reported record profits in 2000, most experienced sharp falls in profitability in the following year, as geopolitical concerns and a general economic slow down reduced trade and shipping. This pattern was repeated regularly in the industry, with periods of rising trade and rates, followed by excess capacity and falling rates. Exhibits 5 and 6 show TEU rates in general and on selected major routes.

On average, margins for shipping liners were low, with an average return on equity of about 5 percent, and operating margins of 2 percent. Some experts estimated the average return on capital employed for the industry ranged between 6 percent and 9 percent after the late-1990s, though they varied widely across years, and were often lower.

**LINER SHIPPING**

Most major customers shipped cargo on a regular basis to major ports, and hence preferred shipping firms to provide regular and reliable sailing schedules. To meet this need, major shipping firms operated as shipping liners, offering regular shipping schedules on fixed routes with published prices. For example, Maersk's AE1 service featured a ship sailing weekly from Kobe, Japan to Bremerhaven, Germany, taking five weeks to sail through the Suez Canal and calling at ten ports on the way. All major firms in the industry operated as shipping liners, with most concentrating on high volume routes between major ports to achieve high frequency sailings. Smaller shipping firms focused on shorter or less busy routes, or on transshipment cargo. Transshipment cargo was off-loaded at major ports by the liners, and reshipped to smaller regional ports by smaller feeder shipping lines. In this respect, the liner shipping industry mirrored the hub-and-spoke system of the airline industry.

The liner shipping model committed firms to sailing on a fixed schedule irrespective of actual demand. This increased the size of fleets required for regular sailings, and committed firms to larger fleets than might be justified by demand. Larger fleets implied higher fixed capital costs and greater excess capacity. Operating costs for each ship did not vary much in relation to the number of containers carried. This increased the incentive for firms to reduce prices to utilize as much capacity as possible.

To reduce supply, capacity, and route duplication and fleet sizes and costs, and to increase the frequency of sailings, almost all shipping lines joined alliances to coordinate schedules. For example, the Grand Alliance was formed in 1998 by Hapag-Lloyd, MISC, NYK, and OOCL. In 2007, the Grand Alliance pooled about 140 ships on 20 East-West routes, and allowed each firm to market some capacity on each ship on each route. Sharing land-based equipment and other
**Exhibit 6  Average Freight Rates on Major Routes (US$ per TEU)**

| Year | Transpacific | | Transatlantic | | Asia–Europe |
|------|--------------|---|----------------|---|----------------|---|
|      | Asia–N. America | Rates | % Change | N. America–Asia | Rates | % Change | N. America–Europe | Rates | % Change | Europe–N. America | Rates | % Change | Asia–Europe | Rates | % Change | Europe–Asia | Rates | % Change |
| 1995 | 1,746 | 1,339 | -15.6 | 1,369 | 1,219 | | 1,384 | 1,480 | | 1,112 | -18.8 | 995 | -18.4 |
| 1997 | 1,302 | 1,459 | -5.9 | 1,284 | 1,472 | 0.9 | 1,183 | 6.4 | 1,040 | 4.5 |
| 1998 | 1,284 | 1,119 | -8.7 | 1,284 | 1,472 | 0.9 | 1,183 | 6.4 | 1,040 | 4.5 |
| 2000 | 751 | 2,125 | -32.9 | 939 | -25.9 | 1,148 | -22.0 | 1,595 | 34.8 | 664 | -36.2 |
| 2001 | 751 | 1,874 | -32.9 | 938 | -0.1 | 1,290 | 12.4 | 1,566 | -1.8 | 826 | 24.4 |
| 2002 | 751 | 1,540 | -14.4 | 866 | -7.7 | 1,180 | -8.5 | 1,073 | -31.5 | 601 | -27.2 |
| 2003 | 826 | 1,529 | -7.1 | 899 | 3.8 | 1,269 | 7.5 | 1,432 | 32.5 | 704 | 17.1 |
| 2004 | 802 | 1,850 | 21.0 | 778 | -13.5 | 1,437 | 13.2 | 1,586 | 17.7 | 778 | 10.5 |
| 2005 | 800 | 1,867 | 21.0 | 854 | 3.0 | 1,514 | 2.9 | 1,795 | -2.3 | 801 | -4.2 |
| 2006 | 815 | 1,836 | -2.0 | 995 | -1.0 | 1,629 | 1.0 | 1,454 | -15.0 | 793 | -4.0 |
| 2007 | 737 | 1,643 | -5.0 | 1,032 | -3.0 | 1,692 | -4.0 | 1,549 | 0 | 755 | -5.0 |
| 2008 | 861 | 1,725 | 1.0 | 1,193 | 4.0 | 1,706 | -4.0 | 2,021 | -2.0 | 988 | 7.0 |

*Note: All figures as at first quarter of each year.*

*Source: UNCTAD.*
facilities provided alliance members with significant savings.

The liner shipping model and potential economies of scale encouraged larger ships and shipping firms. Industry analysts Roland Berger & Partners estimated that large liners (those that shipped more than 1 million containers per year) enjoyed approximately 15 percent savings over mid-sized carriers (those that shipped less than 500,000 containers per year). Partly as a result, the industry experienced considerable restructuring from the mid-1990s. The merger of P&O and Nedloyd in 1996 led to about 30 mergers and acquisitions in the next five years. In 2005, Maersk acquired Royal P&O Nedloyd and Hapag-Lloyd acquired CP Ships, leading to another wave of consolidation.

Nevertheless, the industry remained highly fragmented. In 1998, the top five shipping lines had a collective market share of 26 percent, and the top 20 lines a share of 55 percent. These concentration levels were lower than in many other global industries. Despite consolidation, concentration levels in 2008 remained relatively low at 43 percent for the top five and 70 percent for the top 20 firms. Exhibit 7 provides general information on the largest firms in the industry in 2008.

It was a common practice for liner shipping firms to join shipping conferences. These conferences focused primarily on coordinating and stabilizing shipping rates and related fees. For example, the 12 members of the Transpacific Stabilisation Agreement (TSA) met annually to set rates for transpacific routes. In January 2005, the TSA raised prices by 30 percent to deal with the approximately 17 percent increase in costs from rising port charges and fuel costs. Despite TSA members accounting for about 70 percent of the containers shipped across the Pacific, this attempt failed when customers refused to pay higher rates. Liners who were not members of the TSA typically set their prices below the conference rates.

Conferences had traditionally been granted protection from anti-competition legislation because of the importance and historical evolution of shipping. However, the situation appeared to change from 2000, as some governments encouraged competitive price setting. The U.S. Ocean Shipping Reform Act of 1998 deregulated shipping and permitted shipping lines and customers greater freedom to negotiate freight contracts. However, the Act preserved antitrust immunity for conferences. There were increasing calls for greater action to reduce the shipping industry's environmental impact after 2000, although specific action was limited. In general, the shipping industry faced relatively few regulatory or government constraints.

**LINER OPERATIONS**

The major investment required to establishing a liner shipping business was the cost of ships. Most operating costs were also directly or indirectly related to ship operations.

In many respects, container ships in 2007 did not differ substantially from those of 20 years earlier. However, improvements in design and engine technologies made new ships up to 20 percent faster and more reliable. Automation and IT allowed smaller crews to operate larger ships, to sail more safely and reliably, and to load and unload ships more quickly. The efficiency of container ships was further enhanced by heavy investments in container handling facilities in ports and in IT to facilitate port clearance. All of these advances had the effect of allowing ships to spend more time sailing, effectively increasing capacity.

However, shipping lines generally lacked the sophisticated IT systems needed to conduct complex yield management, capacity utilization, and route planning, and to offer the high visibility degree of visibility on shipments that customers required. Most firms could not determine or manage the margins or costs per container shipped or the profitability of customers. Most shipping lines appeared to be reluctant or unable to undertake the heavy investments in IT required.

The shipbuilding industry shared many characteristics with the liner industry, being a relatively global, mature, government-supported, high-fixed-cost industry. The shipbuilding industry had seen the entry of many Japanese firms in the 1960s, Korean and Brazilian firms in the 1970s, and Chinese firms in the 1980s and 1990s. Many of these shipbuilders were part of large industrial conglomerates and were well funded. Like the liner shipping industry, the shipbuilding industry was viewed by many governments as important for national development, and attracted government support. The South Korean and Chinese governments, in particular, subsidized their shipyards. Although severe competition in the
<table>
<thead>
<tr>
<th>Carrier</th>
<th>Country of Origin</th>
<th>Capacity in thousands of TEUs</th>
<th>Number of Ships</th>
<th>% of Global Capacity (2008)</th>
<th>No. of Ships on Order</th>
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Source: UNCTAD: Containerisation International
1970s had seen the exit of many European shipbuilders, there was substantial overcapacity in the shipbuilding industry in 2008. The cost of new ships declined steadily through the 1990s. In 2000, the cost of a 2,500 TEUs container ship was US$35 million, 30 percent less than in 1990. Rising steel and other costs resulted in prices rising to about US$66 million in 2007, although there were indications that prices would decline.

Competition, pricing pressures, the declining prices of ships, and potential economies of scale led many shipping firms to order new and larger ships from the late 1990s, further contributing to the capacity problem. As a result, the average age of the world’s container shipping fleet in 2007 was estimated to be nine years, substantially lower than for other types of ships. Approximately 37 percent of the container fleet was estimated to be below five years old in 2007. Major shipping lines often replaced their ships in less than 15 years, to introduce larger and more efficient new ships, and to avoid the higher insurance premiums required for older ships.

The average size of ships more than doubled between 1987 and 2008, to approximately 2,500 TEUs. Though only 86 ships with capacities greater than 7,500 TEUs were operating in 2004, by 2007 there were approximately 130. By 2008, the largest ships had capacities of more than 12,000 TEUs. Large ships were more costly, but operating costs and fuel consumption did not increase proportionately. Large new ships could operate with as few as 13 crew members, fewer than on the old, smaller ships. In general, it was estimated that the largest new ships could reduce the cost of shipping a TEU on transpacific routes by 20 percent to 30 percent if fully laden. The relatively low operating costs and substantial economies of scale allowed large ships to move containers profitably at relatively low rates. However, the need to recover the high costs of such ships required high capacity utilization. Operators of these large ships therefore sailed them on the busiest routes, increasing capacity substantially. However, larger ships could be more costly on a relative basis if their capacity was not heavily utilized.

The global container fleet grew by about seven times between 1987 and 2008, to more than 4,000 ships with a capacity of about 11 million TEUs. In addition, there were about 1,300 ships on order, which meant that the industry capacity would increase by 50 percent when they were delivered. This was more than the normal order book of about 30 percent of capacity. As new ships were delivered, a large number of old ships became available at relatively low prices, as relatively few were scrapped. The prices of these used ships dropped in the 1990s, and again in the mid-2000s.

Containers were a sizeable investment, costing as much as US$2,000 for a twenty-foot container and US$3,300 for a forty-foot container in 2007. The industry owned as many as 15 million TEUs, with utilization rates of about 80 percent. Annual production approached 4 million TEUs, substantially less than the capacity of about 6 million containers. Imbalances in shipping volumes across regions resulted in about 25 percent of containers being shipped empty. The key costs in shipping containers were port, terminal, and handling charges, and transportation fees for the container, which each accounted for about 24 percent of total fees. Exhibit 8 provides the breakdown of costs for an average TEU on the Asia-U.S. route.

The cost structure of shipping operations was affected by external events. Fuel accounted for about 15 percent of total costs for a shipping liner when priced at around $300 per ton. However, when fuel prices rose to about $750 per ton in mid-2008, fuel accounted for as much as 60 percent of the total cost of operating a mid-sized liner. Shipping lines moderated the impact of higher fuel costs by reducing speeds of their ships, which could improve fuel efficiency by as much as 20 percent. This increased the need for ships so that lines could maintain their regular schedules, helping to absorb part of the excess capacity in the industry. In contrast to rising costs, freight rate increases were much more resistant, and price increases were generally smaller.

Increasing security concerns led to the introduction of costly security procedures and increased insurance charges. The failure of many developed economies to expand their ports adequately created congestion, which often led to increased port fees and delays, effectively increasing costs and reducing capacity. Environmental concerns were also expected to raise costs in the medium term. However, most shipping lines could not pass these increased costs to their customers, despite many efforts to raise rates.

For potential entrants, registration, staffing the ships, and obtaining other necessary services and approvals did not pose significant challenges, even for small shipping firms, though a shortage of crew
did emerge in the mid-2000s with the expansion of the fleet. Ancillary services and port services were readily available, although costs were substantial. There were few constraints on shipping firms introducing new routes or sailing to ports of their choice. Many governments provided subsidies and tax incentives to support their national lines, which allowed them to continue operating in the face of poor profitability.

LINERS AND CUSTOMERS

Some liner shipping firms attempted to extend their operations to the provision of value-added logistics services. The logistics industry was viewed as a high value-added, rapid growth industry of the future, in contrast to the shipping business, which was viewed as a low value-added, mature, commodity business. The logistics effort was viewed as a way for shipping lines to offer “one stop services” and to grow into a synergistic and relatively high-margin business. The basic concept proposed by many shipping firms was to take over parts of their customers’ supply chain activities, both before and after shipping their containers. However by 2008, it was clear that most shipping lines that had expanded into logistics had failed, because the businesses required substantially different competencies, dealt with different customers and competitors, and operated in different environments.

The logistics effort was motivated in part by global customers’ preferences for dealing with one firm which could provide a comprehensive set of logistics services. These firms were often multinational corporations, who exercised some pricing power over the shipping lines because of the significant volumes they moved. But the vast majority of shipping lines’ customers were small and accounted for very small shares of shipments, so that each major line dealt with thousands of customers each year. Most of these smaller customers were represented by agents, who coordinated shipments.

Shipping rates were published for each route, and hence were widely accessible to customers, competitors and intermediaries. As all leading lines offered frequent sailings on the main routes, similar rates and
reliable services, customers exhibited little loyalty to shipping lines, shifting their business based on prices and schedules.

Customers were knowledgeable about prices and were generally highly price-sensitive. The importance of shipping costs varied across products. They were substantial for many products, such as rubber and coconut oil, for which shipping costs from Asia to Europe represented between 6 percent and 12 percent of delivered costs. For tea and coffee, shipping costs represented between 10 percent and 12 percent of delivered prices. Though shipping costs were proportionately lower for high value electronics items, these products were time-sensitive and were often shipped by air. A broad estimate was that freight costs represented between 5 percent and 6 percent of the global cost of imports.

THE INDUSTRY IN 2008

The liner shipping industry faced a difficult future in 2008. Many characteristics of the industry appeared to be working against long-term profitability. Average rates were rising, but they were erratic and lagged behind the rises in fuel prices and other costs. Ominously, a large number of ships were scheduled to be delivered in 2009, even as the industry struggled to absorb the largest capacity ever delivered in its history in 2007. There were signs that economic growth was slowing. The structure of the industry would simply not allow consistent profitability. One observer summarized the environment facing the industry succinctly: "... enhanced security demands, skyrocketing insurance premiums, rising oil prices, higher port costs, more competition, stringent environmental and crewing laws, and the ominous threat of waterfront strikes..."

However, many industry participants felt otherwise; the liner shipping industry was simply too important and had too big a role to play in world trade to suffer over the long term. Rising shipping rates and volumes in 2007 had seen the industry enjoy one of its most profitable years in its history. As economies grew, trade would grow. In the absence of alternatives, trade growth would lead to growth in the liner shipping industry and to its sustained profitability. The fundamentals of the industry were simply too favorable for the industry not to flourish in the medium term.

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