

## **Strategic Alliances in Liner Shipping: Underlying Drivers, Expected Benefits and Future Challenges**

### *Evolutionary Path from Shipping Conferences to Shipping Alliances:*

Liner shipping is described by Sjostrom (2009, p.1) as “the business of offering common carrier ocean shipping services in international trade”. The liner shipping industry gained considerable importance in the 1870s with the steady increase in shipment of raw materials and finished goods from Europe to global destinations and vice versa. An exploratory study of the historical roots of the inter-firm collaboration in shipping reveals that “collusive agreements” have dominated the firm behaviour, starting from the formation of the Calcutta Conference in 1875 and recently supplanted by other forms of cooperation like consortia and strategic alliances (ibid). In reality, shipping conferences (alternatively known as liner conferences) were cartels characterized by a set of formal agreements among shipping lines for particular routes, and they were primarily geared towards setting fixed prices to ensure and sustain industry profitability, regulating competition among themselves and pre-empting entry of new players (Wang, 2015). In order to eliminate competition from the market, conference members resorted to intense rivalry in the form of aggressive freight price cuts (often below total costs), thus leading to shippers expressing concerns with regards to the instability in operations and deterioration of service levels. Concerning political and regulatory developments, a debate has been raging on with the anti-conference lobby highlighting the potentially deleterious effects of the existence of the shipping cartels, and the pro cartel group defending the rights of such conferences to exist in the face of high fixed costs and a demand for regularity in service (ibid). In 1988, the Senate and House of Representatives members of the United States of America congregated to review and modify the Shipping Act of 1984, and the main objectives of this

exercise was to devise legislative measures that would encourage competition in the global shipping industry and secure the growth of US exports. As a consequence, a new Ocean Shipping Reform Act (OSRA) was adopted and enacted in 1998, the main aim of which was to “deregulate and modernize the international shipping business” (Wang, 2015, p. 27). In combination with the phenomena of globalization and improved quality of the services rendered by non-conference members, the OSRA catalysed the shipping industry and led to the rise of alliances that emphasized on formulating “efficiency-enhancing operational agreements” that would allow for sharing of vessels, cross route rationalizations, joint use of charters and ports, collaborative scheduling, and leveraging of “economies of density” (Sjostrom, 2009, p. 2). In parallel, the shipping industry witnessed a steep decline in the potency of conferences due to their diluted ability to offer antitrust protection.

#### *Drivers and Benefits Associated with Shipping Alliances*

Lun, Lai and Cheng (2010, p. 72-73) reiterate that as part of a strategic alliance, two or more shipping lines agree to share common goals for mutual advantages, and they are driven to become partners in order to achieve the organizational objective of securing operational efficiencies. Further, the authors assert that shipping liners continue to forge alliances in the face of external threats like increasing competition and pressures on profit margins. The underlying business drivers propelling the growth of alliance formations are:

- **Financial Objectives:** Maximization of profit through rationalization, optimization of capital investments, monetizing excess capacity (Huang and Yoshida, 2013), and mitigation of financial risks.
- **Economic Objectives:** Reduction in operating costs and economies of scale.

- Strategic Objectives: Growth achieved through gaining access to new markets (especially for smaller liners), increase in geographical influence, and economy of scope.
- Marketing Objectives: Enhancement of customer service levels through extended fulfilment and increased shipping frequency, attractive options of a variety of shipping routes and shipment destinations.
- Operational Objectives: Effective vessel planning and increased ease of handling/coordinating global operations.

Further, elucidating upon and expanding the scope of above mentioned propositions, Panayides and Wiedmer (2011) assert that no single organization is self-sustaining and the success of its economic actions rests upon its ability to leverage the network resources that are located outside the boundaries of the firm and are deeply embedded in the mesh of interfirm relationships. Network resources tend to leave a lasting impact on the strategic behaviour of individual firms, and their propensity towards executing “adaptations” by entering into strategic alliances is governed by their perceived ability to acquire and exploit key resources. The authors extend the argument further to augment the case for alliance formation highlighting the relevance of transaction cost theory. Accordingly, it is argued that empirical evidence exists that is indicative of the fact that minimization of transactions costs (utilization of alliance partners’ comparative advantages for information acquisition and shared capital investment) has been a prominent “antecedent” of strategic alliance formation (ibid, p. 27). Specific to the issue of achieving operational synergies, Panayides et al. (2012) report that in previous years, shipping liners made big investments in increasing vessel capacities in order to sustain profitable operations. Thus, accounting for the size of capital investments involved, profitability can be ensured only when the utilization levels of the firm’s assets are near optimal. Consequentially, in a period of subdued maritime trade (in the aftermath of 2008

global financial crisis), liners are incentivized to integrate their supply chains in order to obtain cost efficiencies (Wright, 2016). As an empirical manifestation of such strategic manoeuvres, CMA CGM recently announced the formation of a new partnership agreement called Ocean Alliance that included players like China's Cosco, Taiwanese Evergreen, and Hong Kong's Orient Overseas Container Line (ibid).

### Future Challenges

While experts and consultants agree that the shipping industry is an ominous cauldron of fragmentation and overcapacity that have suppressed industry earnings for long, they also view internal transformations and alliance formation as the key remedial measures that could ensure long-term survival and sustainability (Marle, 2015). However, not everyone is convinced that the current alliance configurations are adequate to meet all the challenges. For example, Porter (2016) cites the views of Morgan Stanley analyst Doug Hayes and asserts that alliances can in fact worsen the financial performance of shipping firms. Primarily, experts argue that any new alliance formation will not mitigate the problem of too many price-setters, and as legal/regulatory provisions disallow joint decision-making on freight rates, any form of cost savings accrued due to rationalization and optimal capacity/demand management will be quickly neutralized by constant rate-cutting (ibid). The other challenge lies in extending the benefits of alliances to landside operations. According to Joerss et al. (2015), operational alliances aimed towards resource rationalization are currently restricted to the utilization of assets that are seaborne, and once the containers are unloaded on land, shippers adopt separate pathways for terminal agreements, logistics and operations management, thus bringing the advantage of economy of scale to an end.

### Research Aim and Research Questions

This research study aims to evaluate the benefits that the shipping liners expect to reap through the mechanism of global strategic alliances. Specifically, the primary research objective is to explore the operational and strategic opportunities that the alliance members hope to capitalize upon, and the various financial, operational, economic, marketing, strategic and regulatory drivers that support this practice of industry restructuring. Finally, the research project aims to study and analyse the different challenges that the alliance members are confronted with. In accordance with the above, the following research questions have been formulated:

- What financial, operational, economic, marketing and strategic objectives are achieved by forming strategic shipping alliances?
- What are the different regulatory factors that drive the formation of strategic shipping alliances?
- How do the alliance members plan to deal with the challenge of global antitrust enforcement (as highlighted by the failure of P3 alliance)?
- How do liners address the challenge of partner selection for alliance formation?
- What are the different coordination related challenges that shipping firms face and how do they overcome those challenges?
- What strategies do the shipping firms plan to implement to overcome the challenge of price-based competition?
- How do the shipping firms plan to address the challenge of port responsiveness and discontinuity of economies of scale at the port level?
- How do the shipping firms plan to extend the benefits of strategic alliances to landside operations?

- Are there any viable growth alternatives to alliance formation like mergers and acquisitions?

### Research Methodology

For the purpose of this research study, it is proposed that the research paradigm of interpretivism will be adopted. The ontological underpinnings of this approach dictate that the reality of organizational life be treated as a “flux of processes, experiences, practices” (Saunders, Lewis and Thornhill, 2016, p.136). From an epistemological perspective, interpretivism focuses on narratives, perceptions and interpretations and in accordance with the same, the data gathering process will aim to generate new understanding and worldviews about shipping alliances. By utilizing the qualitative methods of data collection and analysis, this project will focus on a small sample and will utilize in-depth interviewing and investigations techniques. The choice of a qualitative approach is justified as it helps in answering the “how” and “why” questions, and it also helps in comprehending a sustained, ongoing process (Tracy, 2013). A multi-method approach will be adopted to gather evidence from different sources like interpretations and public documents. In specific terms, a semi-structured interviewing technique will be employed wherein a set of key themes and questions will be formulated, but the exact ordering of questions will be left open to changes. Finally, in terms of sampling strategy, a purposeful sampling plan will be prepared that will cover organizations and respondents that fit the parameters of research aims and objectives.

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