A change in tone

The ECG president tells **Christopher Ludwig** that although European carmakers are healthier the finished vehicle logistics providers are struggling, and capacity will lag behind without new investment

Costantino Baldissara has a vision for change in the European vehicle logistics sector. Re-elected this past May as the president of the European Association of Vehicle Logistics (ECG), a position he commenced in 2009 as the sector entered its most difficult period in recent memory, he has long campaigned that vehicle logistics should be treated with more respect. In particular, he has stressed the high level of investment by logistics providers, a point he believes is not always considered by carmakers or industry observers.

"There are some who say that the vehicle logistics industry does not have a high level of investment. But there is a tremendous amount of investment necessary. To move a car from A to B in Europe there are 100 companies involved who have invested €40 billion ($57.5 billion) in ships, trucks, rail wagons and terminals," he says.

Baldissara believes that the need for investment is reaching a critical urgency as rising costs and stagnant rates have left European logistics providers struggling to invest in new capacity even as the market improves.

Baldissara warns that carmakers should consider the cost structure of vehicle logistics more carefully. Providers must invest about €5 billion in car carrier ships, trucks and rail wagons to get capacity back to pre-crisis levels, he says.

"Rates are not moving in line with the costs of vehicle logistics," says Baldissara. "I'm afraid that in the next 12 months, unless there is another economic shock, there will be a lack of capacity [for vehicle logistics] because companies cannot invest."

Baldissara has been warning the industry in speeches and interviews over the past 18 months that vehicle logistics could become "the bottleneck of the recovery" in Europe without investment in equipment. But to make those investments, providers need support from their customers to help align their operating costs and expenses.

But despite carmakers' improved balance sheets, the vehicle logistics market remains "in poor shape", Baldissara asserts. While carmaker profit margins have recovered strongly to around 7%, according to ECG estimates the profit margins among the top 100 vehicle logistics companies in Europe for 2009 stood at just 3.8%, compared to 6.7% in 2008. Results for 2010 do not appear to have improved much at all.

But the European vehicle logistics sector may not even be as healthy as that. Stripping out the top six companies, the industry's total profits were just €125m in 2009. "This is far too little to contemplate significant investment in new capacity," he says. "And today, as the automotive industry improves, we are becoming the bottleneck in some markets."

Perhaps it is Baldissara's role in the capital-intensive shipping industry–he is the commercial, logistics and operations director for the Naples-based shipping giant, Grimaldi Group–that has sharpened his focus on asset investment. In the shipping industry, for example, investment can approach that of manufacturing plants. Baldissara points out that a factory exporting 300,000 cars per year from India, for example, would need a fleet of 20 ships. "If you consider that each of those ships costs €60m, then you are talking about capital costs of more than €1 billion."

Even beyond shipping, Baldissara's investment warnings reflect the specialised nature of the vehicle logistics industry's equipment. While in other sectors major logistics operators have focused on asset-light and third-party business models–including automotive inbound logistics–it is clear that in most cases vehicle logistics remains asset driven. Baldissara's simple but pressing warning is that if companies cannot earn enough to renew their fleets, carmakers could suffer delays in the outbound supply chain that could even threaten sales.

The disappearing *padroncini*

In the early days of the recovery, when Baldissara first started to warn about a lack of investment, his words were taken more rhetorically than as an impending threat. With sales and production down in most major markets, and overcapacity rife across most modes, few considered that what vehicle logistics needed was shiny new equipment. At last year's ECG Conference in Berlin, STVA's Alain Leray even went so far as to say that the industry probably needed fewer investments to restrict supply versus demand and thereby increase rates.

But Baldissara was never calling for investment for its own sake. Rather, he warned that carmakers and providers should try to look ahead of the business curve: as consumer confidence improved and global markets like China, India and the US recovered, so too would Europe see its production and eventually its sales rise. The idea was to head off potential bottlenecks and be ready to profit in the recovery.

That may now be too late in some markets. In Russia and Germany, where car sales and production are strong, Baldissara points to increasing capacity issues that have delayed lead times across all transport modes. In the UK, during the March registration period (when the market typically reaches a peak), there was a significant lack of truck capacity, compounded further by cabotage restrictions that limit the amount of foreign trucks on British roads. "Capacity has stabilised now in the UK but it will be under stress again during the September registration period," Baldissara says.

But even in markets where sales are down, there is a troubling lack of trucks. This shortage is especially visible in Italy, despite new car sales down more than 20% in the first quarter. "This is because the smaller owner-operator truck companies–known as the *padroncini* in Italy–are simply going out of business. Larger companies should be able to invest but they cannot."

The troubled Italian market defies the typical expectations that a shrinking market would have an excess of supply. But Baldissara believes vehicle logistics has suffered from a serious investment drain, and that private equity and capital investors are receding from the sector. He warns that one consequence could be a major player, or even a carmaker–such as Fiat's iFast trucking company–buying up a lot of capacity, which would effectively shrink the competitive market.

Fiat's head of supply chain management–and managing director of iFast–Paola Petrone confirmed such a scenario in the last issue of *Automotive Logistics*, saying that Fiat would invest in more trucks if it could not secure capacity. Meanwhile Gefco, the logistics arm of the PSA Group, recently acquired 70% of the Italian-based Mercurio Group.

And this past May, at the ECG General Assembly, Daimler's Egon Christ, head of worldwide vehicle transportation, said that Daimler would also consider investing in its own fleet if it continued to face capacity shortages. "This is not a final decision but it is an option we are considering," Christ said.

Improving costs rather than rates

But carmakers seem to turn to in-house resources only with reluctance. Daimler's Christ spoke of it as more of a last resort, as the carmaker is now seeing "real problems" with capacity. Baldissara believes that the solution is not simply in higher rates but in developing a deeper understanding of the real costs and operating realities of the sector.

THIN BY COMPARISON

EBIT margin expectations European OEMS

	2010	2011	2012	2013
BMW	7.2%	9.8%	10.7%	10.9%
Daimler	7.4%	7.8%	8.6%	8.9%
Fiat	2.8%	3.4%	3.9%	4.4%
Peugeot	3.2%	3.3%	3.8%	4.3%
Renault	1.1%	2.8%	4.4%	4.5%
Average	**4.6%**	**5.4%**	**6.2%**	**6.6%**

EBIT logistics sector

	2010	2011
Deutsche Post	4%	4.4%
TNT	7.5%	8.2%
FedEx	7%	8%
UPS	11.7%	13.4%
Kuehne+Nagel	3.8%	4%
Panalpina	2.2%	2.6%
Average	**6%**	**6.6%**

Source: Barclays Capital

European vehicle logistics EBIT

	2008	2009
Average	**6.7%**	**3.8%**

Source: ECG

As an example, Baldissara points to the practice among carmakers of rushing cars for delivery by the end of the month, often to meet sales targets. But this end of month focus leads to huge imbalances in the vehicle logistics network as providers scramble to move vehicles in one half of the month, only for them to sit idle for much of the other half.

"Not only that, but during the rush period the sector often has to subcontract assets to meet demand at a higher cost. So we are losing money during the idle periods, and paying more during the peaks," Baldissara says (see commentary on p6).

A more balanced and stable delivery pattern would remove distribution costs at no damage to customers, although Baldissara recognises that responsibility for the order-to-delivery cycle is often out of the hands of vehicle logistics managers. On the rate side, Baldissara does not believe that all the blame lies with carmakers, either. He says that providers determine rates, and that many could be accused of "rate dumping" by taking on business at a loss.

> The primary enemy of [the European vehicle logistics] sector is often itself – **Costantino Baldissara, ECG**

"The primary enemy of this sector is often itself," he said.

But OEMs also have a responsibility to avoid "dumping offers", he says. "Carmakers know the cost of our business and our investments, and they should take responsibility by avoiding the offers that they see are clearly below operating costs."

There are also significant efficiencies that could be generated by new equipment, as improvements in fuel consumption for newer ships and trucks could ultimately help lower costs in the outbound chain. Baldissara has first-hand experience of these benefits with the Grimaldi Group, which has seen its profits rise in part thanks to more efficient new vessels (see p56).

Carmakers such as Fiat's iFast trucking company may be forced to buy up capacity, with resulting implications for competition

Harmonising European policy

The ECG sees European Union policy as another way to help improve efficiency. On the equipment side, it backs a Europe-wide ban on the elimination of older, higher polluting trucks as well as ships older than 30 years of age. "A new generation of ship consumes about 55% less fuel than a 29-year old ship when both are moving at 15 knots," he says.

But Baldissara maintains that only a few companies–Grimaldi among them–are in a position to invest right now. In particular he would like to see some kind of scrapping bonus similar to that used for passenger cars during the recession to incentivise the renewal of the wider transport fleet.

The ECG also supports a standard maximum length of 20.75 metres for car carriers in the EU, which currently has almost as many variations in truck length standards as it does member countries. The ECG estimates that such a standard–which would be above the 18.75 metres typically allowed in Germany and below the 25.5 metres in Scandinavia–would reduce external costs by €30m, and eliminate about 100,000 loads per year to move the same number of vehicles without changes to infrastructure.

"The current variation in truck sizes is really a terrible distortion of competition," he says. "If member countries are equal and make up one internal market, then why should it be different between Italy and Germany? We don't want a longer truck, but we want to have the same length. This is an important distinction."

Building a control room

Baldissara believes that more coordinated communication with carmakers would go a long way towards ironing out inefficiencies. "We would like to see our clients set up a kind of control room where they can talk to providers about the future," he says. "GM, for example, has a supplier council for logistics, which is a great idea."

Baldissara also believes that a more forward-looking approach to planning and contracting would help everyone. "The clients that award their logistics business two years in advance of even opening a factory are the best and most intelligent ones," he says.

Baldissara has hopes that the ECG might become more of a forum for carmakers and LSPs to share ideas and set standards. Among the groups with which Baldissara believes the ECG should coordinate more is the ACEA Logistics working group, which brings together logistics managers at member carmakers.

There are signs Baldissara and the ECG are making headway. Christ–who plays a leading role in the ACEA group–gave a conciliatory speech at the ECG Assembly this spring, admitting that Daimler took drastic measures during the downturn to reduce costs, including cancelling or modifying all of its logistics contracts. He recognised both the necessity of rebuilding trust between carmakers and providers, as well as ensuring that both maintain a relationship that allows the right level of investment in equipment. "It is time to create new business principles, and to write a new code of conduct that allows for closer partnership," Christ said.

Among his suggestions were several that echo Baldissara, including longer contract lengths that allow providers to better plan investment. He also agreed that carmakers had a responsibility not to accept "dumping rates". Finally, Christ suggested that one method of developing these new business practices would be through a more aligned collaboration between the ACEA logistics working group and the ECG.

Baldissara hopes that the change in tone will be reflected across the sector, otherwise he predicts more trouble ahead for vehicle logistics as providers take a tougher stance. "In the future the only [providers] that will be ready to do business are those that will earn a reasonable profit," he says. "So unless there is more cooperation between clients and companies, there will be a lack of capacity."