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Freight forwarding and logistics: What the high performers know

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Freight forwarding and contract logistics continues to be a growth industry. Though such growth is expected to slow somewhat (from a high of 3 percent over the past five years to about 1.5 percent in the near term), that rate will still likely outpace that of global GDP—a good situation to be in, considering current economic circumstances.

Even so, freight and logistics companies will need to deal with numerous issues in the years ahead. For example, as trade routes become more competitive and as freight rates fall, the industry's traditional bargaining power with its shippers—volume—will be challenged. One important strategy to counter this challenge is to use balance sheet strength to acquire niche players in important trade routes and geographies, especially in emerging markets.

Another key to growth and profitability will be the ability to analyze customers' needs and then respond quickly with differentiated and advanced logistics solutions. That will require better IT tools to improve internal process efficiency and to generate analyses that result in deeper understanding of customers' industries and business processes.

According to recent Accenture High Performance Business research, which analyzed corporate performance in the freight forwarding and contract logistics industry from 2008 to 2011, high performers owe their success to a combination of factors: dominance over profitable trade lanes; strategic growth in key emerging markets; and business models supported by operational excellence and designed to develop expertise in customers' industries while empowering those customers with greater information and better service at the same time.

Industry background

As customers enter new markets, especially in emerging economies, they are demanding much more than traditional transportation and warehousing services from their freight forwarding and contract logistics providers. The ability to offer new, value-added services such as warranty processing, returns management and light manufacturing is now a differentiator, as is providing services such as customs and insurance brokerage, and trade and transportation management. In other words, the ability to become a "one-stop-shop provider" is emerging as a way to achieve differentiation and capitalize on cross-segment opportunities.

However, companies in the industry face multiple risks, particularly in light of continued global economic instability. Rising oil prices are a persistent threat. Industrial production slowed during 2011. Economic challenges in the European Union, political instability and unrest across multiple areas of the globe, and a series of natural disasters have highlighted the often fragile nature of the freight forwarding and logistics business and the industry's customer environment.

According to our research, the following represent some of the most serious risks:

- **Flat growth for forwarders.** After heavy losses in 2009, the sector recovered moderately in 2010. The past year has been a difficult one, with profit growth being limited to volume growth, and with yields unlikely to improve as freight rates remain under severe pressure.
- **Pessimism about growth opportunities in air freight.** In the Asia-Pacific region in particular, the air freight business has suffered more than container shipping recently.

- **Ongoing overcapacity in ocean freight.** Shipping rates for all routes continue to decline.
- **Risk of cheap capacity.** Counter-cyclical businesses such as freight forwarding or contract logistics, with relatively flexible business models, are better able to keep margins stable in the downturn—but they risk sitting on cheap capacity in an upturn.

On the positive side, demand is rising for advanced logistics capabilities and industry-focused solutions, especially in emerging markets. The increasing number of assembly plants in these markets—including Turkey, Mexico and Thailand—has positively affected the dynamics of the logistics industry.

Companies are also responding to market and economic pressure by restructuring their logistics organizations—consolidating service providers and functions, sharing logistics facilities and centralizing management.

Industry imperatives: What the high performers know

Against this background, according to Accenture's exclusive analysis of recent industry performance, high-performance businesses in freight forwarding and logistics have maintained industry-leading operating profit margins and above-average capital efficiency ratios—a result, we believe, of their tightly controlled operating expenses and strong working capital management.

In contrast to most of the companies in the industry, whose top-line growth suffered significantly in the global downturn, the high performers managed a compound annual growth rate of 13.4 percent over the past three years. They also returned a total of 7.5 percent to shareholders over five years—in contrast to negative returns for the rest of the industry peer group studied.

Using the structure of the three building blocks of high performance, as defined by the Accenture High Performance Business research program, the following are some of the important lessons about high performance from which all players in the freight forwarding and contract logistics industry can benefit.

1. Market focus and position

Due to a mixture of organic growth and strategic acquisitions, high performers not only have a strong presence in emerging markets such as Brazil, Russia, India, China and Mexico, they also exert control over the most profitable trade lanes: Europe to Asia, for example, or North America to both South America and Asia. Moreover, by leveraging dominant positions in domestic freight (both air and road), they have managed to maintain volume growth without compromising their revenues.

2. Distinctive capabilities

According to our analysis and scorecard of industry players, three business capabilities stand out in particular.

- **Flexible business model.** The high performers know that time to market is critical in their industry—and they have the flexibility to respond with speed and agility to their customers' need for convenience. High performers have established new ocean freight links to growth geographies such as Africa. And they have opened multiple new service links that span the global trade routes over which they dominate.
- **Deep expertise in key customer industries.** Industry knowledge is growing in importance as customers extend their supply chains in response to globalization. High performers have been leaders in developing extensive expertise in the industries they serve, going well beyond traditional transportation and warehousing solutions. Increasingly, logistics companies are strengthening their ability to collaborate and are better aligning themselves with customers' operations, processes, industry know-how and technology.
- **Using IT to maintain 360-degree control.** The high performers have moved well beyond using IT merely as an enabler of internal process management. Instead, they leverage their proprietary customer-facing technologies to empower their customers, offering them end-to-end visibility across the entire supply chain. Important to ongoing success will be the ability to develop more "intelligent" services, more dynamic planning and increased alignment with customers' operations and processes.

  Supply chain visibility remains a top operational priority for large customers. Customers generally struggle to achieve a unified picture of their supply chains because of the legacy information systems designed to operate within a single company, not across a network of companies. Thus, the ability to share real-time information with key customers, suppliers and partners has become critical in the freight forwarding industry.

3. Performance anatomy

With freight forwarding and contract logistics, performance anatomy relates not only to overall operational excellence but also to such procurement practices as the purchase of transportation capacity and the innovative use of shared services. Because of their relentless focus on productivity improvement, the high performers are masters of operational excellence, achieving significantly higher gross profit conversion.

These companies place much greater emphasis on process automation and on finding the right balance between volume commitments and spot buying—a strategy that enables them to achieve competitive rates in the most important trade lanes. And they have been enthusiastic adopters of shared services, not just for internal processes but also to improve customer services and supply chain management.

Conclusion

A controlling presence in key growth markets and the flexibility to respond swiftly and innovatively to customers' evolving needs distinguish the high performers in freight forwarding and contract logistics. In the future, deep expertise in customers' industries and in the discipline of cost control will be more critical than ever.

High performers will differentiate themselves further by offering supply chain management as a shared service to customers. To drive the continuous innovation of customer-facing applications, industry leaders will leverage IT-driven process management collaboratively with those customers.

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