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Container shipping: The untapped value of customer engagement

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Despite challenging market dynamics and rising operational complexity, container lines can both increase profitability and improve their customers' experience.

Faced with excess vessel capacity and continued downward pressure on freight rates, container-shipping companies are looking for ways to regain profitability. Large and small carriers alike have expanded their alliances. They've cut costs through mechanisms such as slow steaming and have temporarily laid up assets or suspended some services. Many have outsourced the provision of chassis, reduced the size of their customer-facing teams, and trimmed their organizations. These moves have in some cases temporarily buoyed profitability, but they've also made life worse for their customers, especially those based in the United States.

Over the course of several months, we spoke at length with carriers' customers: the CEOs, supply-chain leaders, and heads of procurement at some of the largest shippers, including several of the world's largest retailers. We also spoke with heads of freight forwarders and senior executives from shippers' associations. Our goal was to get a clearer understanding of how recent changes in the shipping industry have affected shippers' operations and to find opportunities for carriers to serve them better.

Shippers have benefited from lower freight rates produced by oversupply and competitiveness; we estimate the fall in freight rates saved US shippers $23 billion between 2010 and 2015.[1] Still, we found dissatisfaction. In fact, many of those we interviewed lamented the problems that seem to accompany lower rates; we found that shippers see a widening gap between the service they'd like to receive from container companies and what they're actually getting. Based on these discussions, we believe that if left unaddressed, customer satisfaction will continue to decline—and any short-term savings carriers might have achieved from cost cuts could ultimately be erased as shippers turn to competitors who can better meet their needs.

For example, our analysis suggests that if a cost-cutting measure such as slow steaming adds three days to the supply chain between the United States and Asia, the additional annual inventory and obsolescence costs for US importers can reach $415 million. Worldwide, that same three-day delay could cost about $5.7 billion. This could create an incentive for shippers to switch to faster carriers. Further, carriers that don't address the customer-service gap are missing an opportunity for share growth, increased yield, and longer-term cost reductions. They also risk becoming commoditized. With so much at stake, we believe it's time for carriers and shippers to work together to create new rules of operation that could ultimately benefit both groups, as well as their partners across the supply chain.

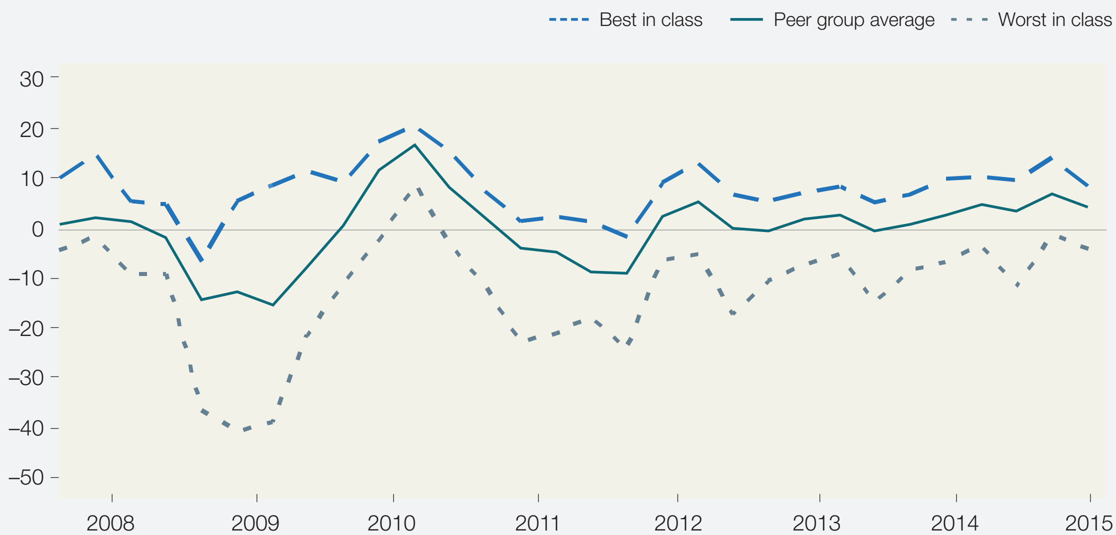
Recent changes have created challenges on both sides

It's important to understand how carriers' attempts to reduce costs have affected their operations—and their customers. Carriers are operating in extraordinary times. Oversupply and persistently low rates have led to widespread unprofitability (Exhibit 1). In response, most carriers have made substantial cuts to their operations. Some of the consequences were expected by the container lines, but others were not.

Exhibit 1

Profitability varies among liners and remains low overall.

Container-shipping EBIT[1] index, margin, %



[1] Earnings before interest and taxes.

Source: Alphaliner; McKinsey analysis

Saving on fuel through slow steaming was the first step for many carriers. As a result, the average transit time from Shanghai to Los Angeles rose from 13.8 days in 2008 to 17.4 days in 2016. This lengthened the supply chain for shippers and—as noted above—it came at considerable cost. Second, lines began deploying larger ships on US routes, which are cheaper to run per box. But larger ships can clog space-constrained container yards when they arrive, increasing dwell times. Third, driven by the need for scale, 15 of the 20 largest carriers have joined or expanded an alliance in the past several years. Some of these partnerships—for the moment at least—have up to six members. Unfortunately, many carriers failed to account for the greater level of operational complexity these new partnerships would create, and so, by and large, have not put sufficient resources toward managing it. (In both Los Angeles and Long Beach, cargo can now flow through any one of up to seven terminals, depending on which partner's ship is carrying it, which makes tracking and planning difficult.) The decision to outsource chassis management to third-party providers made operations at many ports even more complicated. And, of course, some carriers have reduced their sales and customer-service teams as part of their cost-cutting efforts as well.

Clearly, these changes have affected customers, too. Shippers tell us the new operating environment is affecting their supply chain; as one noted, "There is simply no sense of predictability anymore, which affects our planning and inventories."

Others express frustration with what one shipper described as "communication gaps and inefficient coordination among shippers, terminals, ocean carriers, and land-transport companies in the scheduling and movement of containers in and out of the ports." The outsourcing of chassis provision has put additional burdens on shippers; one said his company was being "forced to recover this extra cost from the carriers" by demanding rate reductions. And labor negotiations, which are ongoing in many US ports, can make operations there even more logistically complicated and ultimately affect the entire retail supply chain. In the end, shippers say they want "more accurate and timely information on arrival times, and on berthing and container availability," "more predictable choice of terminals and more reliable transit times," and "more visibility into container status." Some say they're willing to pay more for quality and service, but they all bemoan the "wild swings in rate" they currently see, as carriers experiment with price adjustments in an attempt to stay profitable.

In short, both groups are struggling. For carriers, low levels of customer satisfaction mean freight rates—which are already under pressure from broader market dynamics—could sink even lower. And increased complexity means the cost of landside operations is also increasing, making profitability even more challenging. Carriers are incurring more and more one-time, nonstandard expenses because they're addressing operational problems on an ad hoc basis, such as transporting boxes between terminals in Los Angeles and Long Beach, or paying detention charges for boxes that remain in port for too long because of congestion. For their part, shippers must continue to build additional time into their supply chains and maintain high levels of inventories and buffer stocks, adding to their overall costs. (One shipper summed it up this way: "Our solution to the delays in our supply chain: ship early and seek more nearshoring.")

How can it be fixed?

Clearly, there is cause for action, and significant benefits can be gained by both parties. While solving some problems might require collaboration within and across alliances,[2] individual carriers can do their part by better engaging their customers. And although some of our recommendations are specific to carriers, shippers also must be part of the solution.

Think about different ways to cut costs, and work with shippers to implement them

Actions that look like quick wins can be antithetical to long-term goals. Many lines have reduced the size of their sales and customer-service teams, or closed some customer-facing offices altogether. Although it's helped cut costs, it's brought into sharper relief the transparency and communications problems bedeviling shippers. (One lamented, "There's no one to talk to.") When a carrier is losing money, it's hard to focus on customer service. But shuttering operations and removing the human connection can be detrimental to the customer relationship in the long run.

Carriers want to call at their own terminals. Here, container companies have a true, as-yet-untapped opportunity to improve customer satisfaction—and drive down costs, too—by making more efficient the physical flow of goods off the ship, through the terminal, and all the way through onward conveyance. For example, they might off-load higher-priority boxes first and ensure they are loaded directly onto the first rail cars. To make these kinds of changes, they'll need to work with other carriers and alliances. They will also need to try to persuade port authorities to allow the consolidation of terminal concessions, which according to some executives is overdue in many US ports.[3]

Shippers also tell us they'd like better visibility from carriers and terminals. Using new tools and technologies that make real-time information available to carriers, shippers, and their partners on land (truckers and railroads, for instance) could help all stakeholders along the value chain improve how they plan and execute operations, including carriers themselves. By providing more upstream visibility—a centralized database offered through a web-based, open platform is one way to do this—carriers can, again, tap new pools of cost-cutting opportunity *and* help shippers reduce the costs and complexity of their own supply chains. Some port authorities have already started to play a role in offering this kind of transparency.

Carriers will need to work closely with each other and with their customers to implement these types of mutually beneficial process improvements. One shipper we spoke with encouraged carriers to "openly work with customers on new cost-containment ideas and process improvements." For their part, shippers will need to offer accurate forecasts of their volumes, support truck-appointment systems at terminals, be proactive about moving those appointments to non-peak hours and days of the week, and make sure they quickly move cargo out of the terminal once it's arrived.

Don't give up on engaging the customer

It's tempting to think that container shipments are fully commoditized. Most carriers offer similar routes, ships, boxes, and vessels. But just as our interviews revealed that shippers have a growing dissatisfaction with the service they're receiving, they also revealed a willingness, in some cases, to pay more for a better customer experience. This is not a new concept: carriers have long known that the garment trade in New York offers higher yields than discount-store soft toys. But differentiated service—and a direct customer connection—is one way for a carrier to stand out from the crowd. The challenge for lines is providing this higher level of service at a cost they can afford, given the low-margin reality in which they're operating.

But a higher level of service does not necessarily mean higher costs. In fact, organizations with best-in-class customer service often have a lower-than-average cost base. Knowing exactly where each container is and communicating it to the customer via the web and mobile apps could reduce the number of unnecessary box moves, lower the number of calls from unsatisfied customers, and make turnarounds happen more quickly—and ultimately lower costs.

To improve the customer experience, container lines can focus on the six hallmarks of customer-experience leaders (Exhibit 2). This approach includes, among other steps, identifying the customer journeys that matter the most, continually innovating those journeys, and piloting customer-service-improvement programs that include rigorous metrics and can be compared with a control group.[4] We've seen this approach increase customer satisfaction by 50 percent for some companies as measured by net promoter scale, and we believe it can work for the shipping industry as well.

But do engage at a more senior level

Procurement, transportation, and logistics professionals have an important role to play in creating solutions to the increasingly complex environment in which they're operating. But we believe that the operational and structural challenges facing shippers and carriers are substantial enough to also warrant deeper and more regular engagement of both groups at the senior-most levels. By coming together, CEOs and senior managers from both sides have the

Exhibit 2 **There are six hallmarks of customer-experience leaders.**

1 Deliver **value proposition and common purpose** consistently through journeys

2 Identify journeys that **matter most** and **continually innovate** them

3 Leverage journeys to **manage expectations** (using behavioral psychology)

4 Use journeys to **reinforce frontline culture**

5 Lead with **digital-design** thinking

6 Use journeys to define **metrics** and **governance** system to continuously improve

Source: McKinsey analysis

potential to make sustainable, mutually beneficial changes. Container liners—many of which are based in Europe and Asia—should ensure their top management spends time in the United States engaging their primary stakeholders, which may include key shippers, port authorities, terminals, and regulators. Shippers should ensure that container-freight discussions are not left to their procurement teams but rather are a CEO- and COO-level discussion. One shipper encourages “more intense engagement at a senior level” and notes that “changes in operating methodology, landside collaboration, and other steps to address negative impact on supply chains will need a push from shippers, shipper associations, railroads, and port authorities.”

The structural realities of the shipping industry have forced carriers to perpetually seek more and more cost-cutting measures, many of which have had unintended consequences for their customers. As ships get larger, carrier alliances evolve, and consolidation within the sector continues, operational complexity will continue to be challenging, and margins will remain tight. Carriers must engage their customers, fellow alliance members, and supply-chain partners to cut through the complexity and create joint solutions. And carriers must redouble efforts to engage their customers—including at a senior level—through an improved and differentiated customer experience. ■

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[1] For US imports from Asia, comparing freight costs in 2010 with freight costs over the 2010–15 period.

[2] For more, see Martin Joerss, John Murnane, Steve Saxon, and Ronald Widdows, "Landside operations: The next frontier for container-shipping alliances," April 2015, McKinsey.com. Of course, any collaboration between and within alliances must be done in compliance with relevant laws and regulations.

[3] For example, see Peter Hurme, "LA/Long Beach port execs look to jointly speed the flow of cargo," April 21, 2015, cargologisticsamerica.com.

[4] For more on customer journeys, see Alex Rawson, Ewan Duncan, and Conor Jones, "The truth about customer experience," *Harvard Business Review*, September 2013, hbr.org.

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