A weighty lesson from history for forwarders

Larry Woelk on how the express integrators are quick to spot a niche they can turn to their advantage

Since the inception of the express industry, or rather since FedEx's invention of it, the integrators have had it their own way. Granted, it wasn't easy and there is the famous story of how Fred Smith went to Las Vegas and parlayed his last penny into enough dosh to meet payroll. If he hadn't been lucky, then FedEx, and maybe even the express industry, wouldn't be with us today.

Since then, the integrators have prospered by picking low-hanging fruit from the traditional providers – particularly the freight forwarders. In the early 1970s, there were ample flights to move air freight overnight around the US market virtually from anywhere to anywhere.

In the days before expensive fuel, the airlines handled the heavy stuff in the US market and the freight forwarders the smaller shipments. In fact, 75% of shipments in freight forwarders' consolidations were less than 25kg. Internationally, flights weren't quite as frequent but by using the airlines, the forwarders would send consignments "direct Iata" and achieve fast transit times.

FedEx came along and proved that its model of controlling everything – road transport, handling and aircraft – worked and was extremely profitable. Freight forwarders were able to achieve gross margins close to 15%, practically triple what they are today. Once it got going, FedEx was hitting margins more than double that.

Airborne Freight Corp, or Airborne Express as it became known, was the first to try to copy FedEx in the early 80s. But Airborne never quite had the resources to compete service-wise, so it tried to get business by being cheaper. Not the best strategy when your customer "absolutely, positively" had to get a package somewhere.

UPS eventually woke up to the potential in express and became an express integrator. It had a couple of advantages: it was already a package integrator, albeit by road, and it had deep pockets. UPS just needed to develop a process that would move packages faster. As the largest ground package company in the US, even larger than the US Postal Service, it had a huge customer base.

UPS also had staying power. It identified express as where it wanted to be and didn't sway from that strategy until it got there.

Meanwhile in the international express market, DHL was growing in leaps and bounds. Internationally, it used couriers on airplanes to service the world. Not being straddled with high fixed costs, and with a "do now" mentality, DHL digested the international market.

The integrators have now set their sights on urgent heavy freight

TNT was DHL's only real competitor. TNT was a little bit like Airborne and never quite had the resources or the customer base to overtake DHL. Both FedEx and UPS faltered when they went "international" while they adjusted their domestic processes to international ones.

Initially, forwarders' consolidations were full of small packages. Strategically, they had two problems with moving small urgent shipments in consolidations long-term: it was slow, and it cost too much.

When the courier association organised a courier handling facility, CFL, at Heathrow with BAA, forwarders complained that the courier companies were getting preferential treatment to achieve an hour cut-off for outbound flights and an hour recovery for inbound ones. When they were advised they could join the CFL, they declined. They opted instead to keep moving small packages in consolidations so they could continue generating revenue from customs clearance, airline handing, documentation, bonded warehouse and the like.

Fifteen years after the CFL opened, no forwarder has joined. Their lack of response fed the growth of the integrators internationally. Today less than 5% of shipments in a freight forwarder's consolidation is under 25kg.

The integrators have now set their sights on urgent heavy freight. If something big has to get from one place in the world to another quickly, they have the dedicated lift and flights to handle it. Of course, they also charge above normal air freight rates for the service, which produces high margins. Their success in moving into the urgent air freight market is helped by a "misconnect" in the air freight chain.

Air freight rates are very competitive. Shippers are always putting pressure on forwarders to reduce their rates. The forwarders, in turn, pressure the airlines to reduce their rates. As a result, airlines' margins go down and service deteriorates.

What does this leave for the freight forwarders? Slow, cheap freight. Together, the airlines and forwarders have the flights and coverage to move heavy freight as fast as the integrators. They just don't have the process, communication or pricing strategy to compete and it looks like history will repeat itself.

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