# Restructuring in the Liner Shipping Industry: A Case Study in Evolution

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## Abstract

Like many other industries, the global container shipping industry has been undergoing a period of restructuring and consolidation in the 1990s, reflected in both merger and acquisition activity and in the formation of global alliances. Following a description of this decade of industry change, this paper explores the literature on growth alternatives, the specific case of the Sea-Land and Maersk relationship, and presents a framework to explain the managerial decisions behind the final merger decision.


## Introduction

Shipping is, by its nature, global. Liner shipping companies, those offering regular service predominantly moving containers, serve traders whose markets are increasingly global in scope. The application of location-specific advantages to liner shipping has long been limited to tax and labour elements. The advent of the flag of convenience (e.g., Panama, Liberia) during the Prohibition era in the US meant shipping was one of the first industries to become "globalized." Inputs to the development of the service are purchased from the most cost-effective source; mobility of assets and the ability to source labour (seafarers) and capital equipment (ships, containers and the like) from the most advantageous seller also mark shipping as a long-established global business. The relevance of globalization of production and distribution in today's trading environment is indirect; liner companies' customers want fewer suppliers offering better services and global reach. Hence liner firms may make the decision to offer their services in a market with a global geographic scope in order to serve the needs of these traders.

Does this mean that most liner shipping firms will seek to be global? The short answer is no. Most liner firms are regional or niche players in the supply of liner shipping and do not have the financial wherewithal or managerial inclination to seek a broader scope for their business. There are many examples of shipping companies doing well in servicing geographic and equipment niches. This paper is about the liner firms that choose a global market scope and the restructuring and consolidation occurring among them. The latter part of this paper will focus on one merger: Maersk's acquisition of Sea-Land from US railroad giant CSX in the summer of 1999, a merger that created the largest liner shipping company in the world.

## The Changing Industry[1]

Like many other industries, the global container shipping industry has been undergoing a period of restructuring and consolidation in the 1990s, reflected in both merger and acquisition activity and in the formation of global strategic alliances.

On the merger and acquisition front, consolidations were very high profile. The Top 20 carriers by capacity on offer reported by *Containerisation International* controlled 38.8% of TEU capacity[2] in 1990 (Fossey, 1990) and 52.9% by 1998 (Table 1). In the short period from 1995 to 1999, the Top 19 became the Top 15 with the restructurings of P&O and Nedlloyd (resulting in the P&O Nedlloyd joint venture), the Neptune Orient Lines acquisition of American President Lines, Hanjin's acquisition of DSR-Senator Linie and last, the Maersk acquisition of Sea-Land. Fossey (1998a) counted six mergers from January 1996 to August 1997 and 15 takeovers between March 1995 and November 1997. The most significant of these are found in Table 2, along with the values of Maersk's acquisition of Sea-Land and two other high profile mergers of the time, Worldcom's acquisition of MCI and Exxon's merger with Mobil (for comparison purposes).

As for the role of alliances in industry restructuring, they were not a new phenomenon in this industry. Mahoney (1990) identified 54 consortia operating on 25 trade routes with 143 companies engaging in some sort of vessel sharing arrangements. However, these were operational agreements of very limited scope, and cooperation within the agreements leaned towards relatively riskless pooling of resources coupled with maintenance of firm identity.

The pivotal year in alliance formation was 1995. The Global Alliance between APL, OOCL, MOL and Nedlloyd (with side arrangements with CGM and MISC) was announced; the alliance configuration included services in the transpacific, Europe–Asia and Asia–east coast North America and moved the industry beyond cooperation on a single route basis. However, the key trade route of the transatlantic was missing and so the service was not truly a "global" one. P&O also announced that it would join the Hapag-Lloyd / NYK / NOL grouping, active in the Asian trades. This left Maersk, one of Europe's three operators in the top eight, a free agent on the north Europe / Asia trade. As the second largest carrier in the world at the time, Maersk had the capacity to go it alone but, given the overwhelming economic advantages of consortia participation, opted for a closer relationship with Sea-Land.

**Table 1: Top 20 Container Operators 1998 and 1995**

| *1998 Rank* | *Company* | *1998 Total TEU* | *1995 Rank* | *1995 Total TEU* |
|---|---|---|---|---|
| 1 | Maersk | 346,123 | 2 | 186,040 |
| 2 | Evergreen / Uniglory Marine | 280,237 | 3 | 181,982 |
| 3 | P&O Nedlloyd | 250,858 | | |
| | Nedlloyd | | 6 | 119,599 |
| | P&O | | 8 | 98,893 |
| 4 | Mediterranean Shipping Co. (MSC) | 220,745 | 10 | 88,955 |
| 5 | Hanjin (incl. DSR-Senator) | 213,081 | | |
| | Hanjin | | 9 | 92,332 |
| | DSR-Senator | | 14 | 75,497 |
| 6 | Sea-Land Service | 211,358 | 1 | 196,708 |
| 7 | Cosco | 202,094 | 4 | 169,795 |
| 8 | APL / NOL | 201,075 | | |
| | APL | | 11 | 81,547 |
| | Neptune Orient Lines / PUL | | 16 | 63,469 |
| 9 | NYK / TSK | 163,930 | 5 | 137,018 |
| 10 | Mitsui-OSK Line | 133,681 | 7 | 118,208 |
| 11 | Hyundai | 116,644 | 18 | 59,195 |
| 12 | Zim | 111,293 | 12 | 79,738 |
| 13 | CP Ships | 105,322 | NR | |
| 14 | CMA (incl. CGM) | 91,600 | | |
| | CMA | | 20 | 46,026 |
| | CGM | | NR | |
| 15 | Hapag-Lloyd Containerline | 90,879 | 15 | 71,688 |
| 16 | OOCL | 90,063 | 19 | 55,811 |
| 17 | K Line | 89,717 | 13 | 75,528 |
| 18 | Yangming | 79,840 | 17 | 60,034 |
| 19 | United Arab Shipping | 59,331 | NR | |
| 20 | SCL (1) | 55,584 | NR | |
| | Top 20 Total (share of total fleet) | 3,113,455 | (52.9%) | |
| | Total Fleet | 5,878,214 | | |

Notes: NR = Not Ranked

(1) SCL is a merger of Safmarine and CMB Transport. The CMB share was acquired in July 1998 by Safmarine and the company renamed to Safmarine Container Lines.

Source: 1995 data are from Fossey (1995:56). 1998 data are from *Containerisation International Yearbook 1999* (6-7, Table 3).

**Table 2: Selected Mergers, Acquisitions and Takeovers**

| ***Date of Deal*** | ***Companies involved*** | ***Price($m)*** |
|---|---|---|
| January 97 | P&O Containers and Nedlloyd Lines | US$175 (2) |
| March 95 | CP Ships and Cast | CAN$150 |
| April 95 | Pyramid Ventures and Navieras de Puerto Rico | US$140 |
| February 97 | Hanjin Shipping Co. and DSR-Senator Linie | Approx. US$75 |
| July 97 | CP Ships and Lykes Lines | US$34 |
| August 97 | Petronas and MISC (3) | US$700-750 |
| August 97 | Preussag and Hapag-Lloyd AG (3) | US$1,500 |
| November 97 | NOL and APL | US$825 |
| November 97 | Worldcom and MCI | US$37,000 |
| December 98 | Exxon and Mobil | US$81,000 |
| July 99 | Maersk and Sea-Land | US$800 |

Notes: (1) All prices in US$ million; for takeovers, includes cost of acquisition and subsequent reorganization.
(2) Nedlloyd's payment to P&O in order to balance the shareholding structure in the new venture.
(3) These deals were not pure shipping deals; Petronas is a state-controlled oil and gas company and Preussag is an industrial and services conglomerate.

Source: Shipping data adapted from Companies and *Containerisation International* as cited by Fossey (1998a:37, Table 2 and 38, Table 3.); Maersk/Sea-Land, Worldcom/MCI and Exxon/Mobil dates and prices are the announcement date and estimated value of the deal.

By August, four alliances had been announced: (1) Maersk and Sea-Land, (2) the Grand Alliance of NYK, P&O, Hapag-Lloyd, and NOL, (3) the Global Alliance of APL, Mitsui O.S.K., Nedlloyd and OOCL, and (4) the alliance of Hanjin, DSR-Senator, and Cho Yang (Bonney, 1995). The industry entered a new phase, one where key industry players sought to reach global markets for customers desiring global services. However, market coverage and commitment to these alliances varied. Both the Grand and Global Alliances were initially focussed on Asian trades. The Global Alliance represented a deployment of only 77 of the 187 vessels operated by its partners; likewise the Grand Alliance's vessels were also about one-third (60 the total of 182 operated). This increased with the Hanjin, DSR and Cho Yang alliance (60 of 95 vessels). The greatest commitment to alliance participation was represented by the Sea-Land

Maersk alliance, at 175 vessels deployed of the 206 possible and deployed on all the major trade routes.

The pattern of mergers and alliances changed dramatically between 1995 and 1998, shifting as mergers forced the reconsideration of partners and service patterns. P&O's joint venture with Nedlloyd forced the new company to choose between the Global and Grand Alliances, with the jilted partners reshaping their arrangements. Once P&O Nedlloyd chose the Grand Alliance, the newly merged NOL/APL opted to join the restructured Global Alliance. As OOCL was not included in the new Global Alliance, it became a participant in the Grand Alliance. OOCL's strength in the China and southeast Asia market provided better balance within the Grand Alliance rather than duplicating the strength of its former alliance partner, APL/ NOL. The resulting new global groupings (Table 3) dominated the Top 20 and accounted for 28% of the TEU on offer in 1998. Of the Top 20, 13 were involved in one of the large-scale alliances, all offering services on the three main trade lanes—transpacific, transatlantic and Europe-Far East. In the final analysis, there has been a natural balancing in the process of realignment.

**Table 3: Changing Alliances**

| *Alliance* | *1995 Members* | *1997 Members (December)* | *1998 Vessel Deployment* |
|---|---|---|---|
| Global Alliance | APL<br>Mitsui-OSK<br>OOCL<br>Nedlloyd | APL (NOL)<br>Hyundai<br>Mitsui-OSK | 90 vessels<br>325,487 TEU |
| Grand Alliance (1) | Hapag Lloyd<br>NOL<br>NYK<br>P&O | Hapag Lloyd<br>MISC (2)<br>NYK<br>OOCL<br>P&O Nedlloyd | 93 vessels<br>350,197 TEU |
| Maersk / Sea-Land | Maersk<br>Sea-Land | Maersk<br>Sea-Land | 167 vessels<br>438,089 TEU |
| Tricon / Hanjin<br>(United Alliance) | Cho Yang (3)<br>DSR-Senator<br>Hanjin | Cho-Yang (3)<br>DSR-Senator<br>Hanjin | 85 vessels<br>277,000 TEU |
| Cosco / K-Line / Yangming (4) | | Cosco<br>K-Line<br>Yangming | 65 vessels<br>212,714 TEU |

Notes: (1) The original Grand Alliance agreement was canceled 29 July 1996.
(2) On certain routes only (very limited participation).
(3) Not in Top 20.
(4) This alliance is much looser than the others, with alliance members engaging primarily in slot exchanges, often without vessel sharing or schedule management.

Source: 1998 deployment data as reported by Fossey (1998b).

## Why Has This Restructuring Taken Place?

In liner shipping, there is significant firm diversity—not all companies have business interests solely within the broader industry context of ocean shipping. In part, this diversity has resulted from firms seeking new growth opportunities beyond those merely possible from developing new services or expanding to new markets. Alternative growth opportunities may materialize (1) in related businesses, such as terminals, ports or ferries, or even offshore oil and gas projects; (2) through vertical integration or development of logistics service businesses, which may integrate the firm more fully into the supply chain of the buyers of its services; or (3) from peripheral businesses which may only be marginally related, such as hotels or management information services. Such diversity may be considered a strength, if the overall organization sees liner shipping as a critical core business and is prepared to bring the talents of the whole business to support the core shipping business through the continuing industry restructuring. Diversity may be a weakness if the organization is not structured in such a way as to support the liner business or to benchmark its performance on other than short-term measures.

### *The Theories About What Drives Choice of Restructuring Strategy*

Economic theory views integration as a way of reducing transaction costs. Integration, vertical or horizontal, relocates the risks and the costs of the transacting relationship to within the firm (internalizing it), thereby reducing them. Internalization theory does not consider the possibility that value may be appropriated from intangible assets without ownership of the assets (Mytelka, 1991). Tight alliances may allow firms to extract the advantages of merger without completing a merger.

Williamson (1975, 1985) argued that transaction costs are particularly important when economic agents make relationship-specific investments, noting that firms try to overcome transaction costs by integrating vertically. By 1985, he accepted that intermediate forms (such as joint ventures and strategic alliances) could also create frameworks for transactions. Ring and Van de Ven (1992) concluded that varying combinations of risk and trust will lead transacting parties to choose among four governance structures for their dealings: discrete contracting, recurrent contracting, relational contracting and then hierarchical arrangements.

Relationships in the globalized world have ceased to be simple. The buyer–seller model of business relationships has evolved into a complex web of activity, including horizontal relationships for mutual gain, and business structures that are less able to be neatly categorized. Ghoshal *et al.* (1999) argue that industrial organization economics, with its focus on value appropriation, rather than value creation, does not provide a suitable model for future firm behaviour; it provides a destructive model based on the logic of static efficiency.

### *Strategy and Structure*

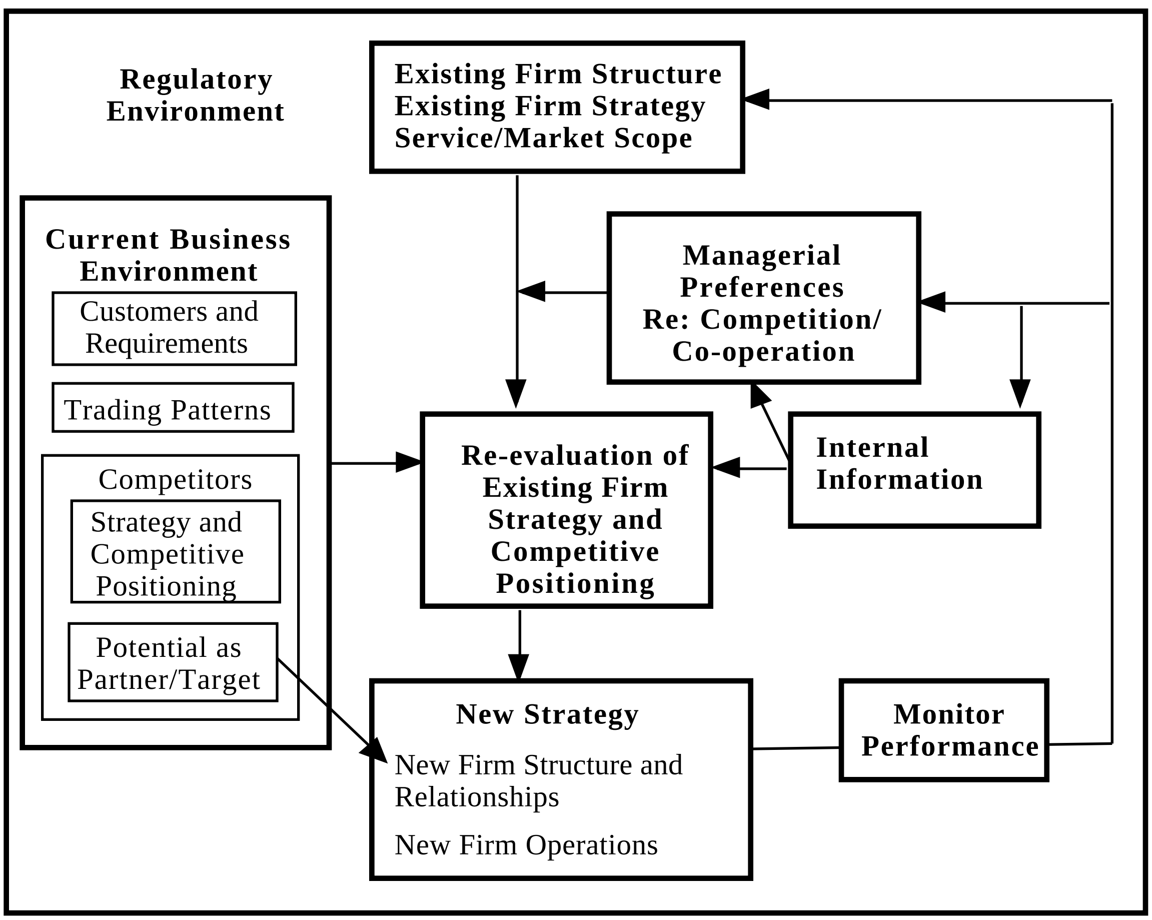
Effectiveness of the organizational structure is a function of “fit,” or how consistent or congruent all of the organization dimensions are with the strategy. Fit results if these core skills are matched correctly to strategy. Competitive advantage accrues to the firm with early strategy-structure fit; that advantage is eroded over time as other firms seek to gain a better fit. If a firm then changes its strategy, it might therefore change its structure. The choice of merger, acquisition or alliance is an execution of strategy that mandates re-examination of structure if not change of structure.

As explained by Galbraith and Kazanjian (1978), in Stage A, the firm develops a strategy which then must have its structure, Structure A, in keeping with Chandler (1962). If the firm adapts to a changing market environment (market structure) and adopts Strategy B, but retains Structure A, the mismatch leads to a decline in performance. This decline provokes the firm to develop a new structure, Structure B, resulting in improved performance due to fit.

To the resource-based strategic management theorists (e.g., Barney, 1986; Hamel and Heene, 1994), matching the nature of a firm's resources (or addressable resources held by alliance partners) to market opportunities in the environment is a critical step in developing sustainable competitive advantage for the firm. The concept of addressable resources provides a partial explanation for the growth in strategic alliances.

In examining growth strategies for transport companies, Brooks (2000) introduced a framework for understanding the choice of structural options, e.g., alliances, mergers, acquisition or joint ventures, within the context of decisions about strategy. That framework is presented in Figure 1.

**Figure 1: A Model of Strategy Formulation in Liner Companies**




Source: A simplification of Figure 3.2 from Brooks (2000): 70. Used with permission.

The firm makes its strategic choices taking into account both the larger context of the regulatory environment and its business situation, as well as its internal evaluation of its resources, capabilities and competencies. A firm's strategy must include its decisions on scope (both breadth—global, regional, multi- or single trade lane—and range of activities). Top managers' perceptions of market structure and of the particular firm's strengths and weaknesses (Caves, 1980) determine that firm's choice of strategy (its plan to achieve its goals and objectives) and, subsequently, its choice of structure (the internal allocation of tasks and procedures to implement the strategy). Hence, managerial perceptions are incorporated into an element called managerial preferences in Figure 1. These managerial preferences may result in a competitor being viewed as a target for acquisition or potentially addressable resources within a well-structured alliance.

Markides (1999) argues that successful strategy is finding a unique market position and successfully differentiating it from those of its competitors. He concludes that strategic failure results from the inability of managers to make clear and explicit choices about that position and its differentiation. As competitors' positions evolve, so too must the company's position. This thinking is entirely consistent with the Galbraith and Kazanjian (1978) view of strategy and structure evolution.

To implement a preferred strategy, structural options enhancing growth will need to be examined, including alliance and merger alternatives. Implementation may result merely in the appropriation of value or may create value, depending on the vision and orientation of management.

## The Sea-Land/Maersk Alliance—A Slow Waltz to Merger

In July 1999, Maersk and CSX jointly announced a merger between Maersk and Sea-Land, the largest American-owned container shipping company. It was a merger many years in the making and created the world's largest container shipping company. Before the merger, Maersk and Sea-Land were held to be the great alliance success story. How did this alliance evolve into a merger?

### *Introducing the Dance Partners*

**Maersk Line** is a subsidiary of the two largest companies on the Copenhagen Stock Exchange, Steamship Company of Svendborg and Steamship Company of 1912; these holding companies form the main parts of the privately controlled A. P. Møller Group.

In the 1980s, Maersk was a well-established operator on Europe–Far East and transpacific trades and, despite a US east and Gulf coast to Middle East service, had not entered the third of the three main trade routes—the north Atlantic. In 1987, the company decided to aggressively expand its operations into the transatlantic and begin to transform itself into a global carrier. It did so by extending its Far East / US east coast service to Europe.

Although the company captured more than 10% of the transatlantic market in its first three years on the route, profitability eluded it. As a result, in 1990 the line announced a rationalization of its transatlantic operations; this rationalization included negotiations with CSX for the possible purchase of Sea-Land. While the negotiations did not result in an acquisition, they produced a vessel sharing agreement (VSA), under which Maersk provided space on its ships, serving the US west coast from Europe, to Sea-Land and P&OCL. In exchange, Maersk received space on Sea-Land and P&OCL vessels calling on east and Gulf coast ports. This agreement signaled Maersk's break with its former go-it-alone strategy.

During the period 1992–1996, Maersk was financially stable. It more than doubled its capacity from 120,000 to 260,000 TEUs and invested significantly in post-Panamax tonnage, all without serious financial damage and at a time when most other carriers were unable to return a profit. In March 1993, Maersk acquired long-time rival EacBen from its Copenhagen-based competitor EAC and secured a leadership presence in the Europe–Far East route. This too was an unusual move for Maersk, long recognized for its belief in organic growth as a strategy (Anonymous, 1993).

A fundamental plank of Maersk's global strategy throughout the mid-1990s was to search out areas of the market where they did not have a connection and make one. The company divided the world into several blocs, establishing regional headquarters. It also advocated a hub and spoke approach to network configuration and, in many of the ports it uses as hubs, it owns its own terminals. Ownership of sales offices is also a central piece of the Maersk strategy. Tight integration and control have been key to Maersk's success.

By 1995, A. P. Møller was a diversified conglomerate with shipping, shipbuilding, oil and gas exploration and development, aviation and distribution interests; it owned container ships, supertankers, dry cargo carriers, gas carriers, supply vessels and tugs, as well as offshore drilling rigs (*Annual Report, 1995*). Maersk Line was reported by *Containerisation International Yearbook 1995* as the second largest container line in the world after Sea-Land (Table 1).

**Sea-Land Services Inc.** was founded by trucker Malcolm McLean, best known as the father of the container shipping industry. It was his concept of transportation that revolutionized the shipping business. When R. J. Reynolds acquired Sea-Land in 1969 from Malcolm McLean for US$160 million, it was the leading container line in the world. By 1983, Reynolds, a key player in the tobacco, food and beverage sectors, had decided to spin off Sea-Land; the container business needed a substantial infusion of cash to maintain its leadership. After a brief sojourn alone, Sea-Land was acquired by CSX, a major US railroad in 1986. The purchase enabled CSX to move into the international intermodal transport business from its strong US domestic base.

Sea-Land had a long history of going-it-alone but began to experiment with cooperative relationships in 1985, beginning with a venture with the French and Italian flag companies in the Trident service between Europe and the Middle East. In February 1988, Sea-Land moved into a very high profile VSA with P&O Containers and Nedlloyd on the transatlantic trade route and followed in 1989 by a VSA with Swiss carrier Norasia Shipping on the Europe / Far East route. These agreements moved beyond vessel-sharing when, on Norasia's Asia–Middle East–Europe service, Sea-Land provided the terminal facilities and EDI systems while Norasia provided a fleet of ten state-of-the-art vessels (Middleton, 1990). In late August 1990, Sea-Land and P&OCL expanded their alliance to include Maersk Line for vessel sharing on the route between Europe and the US west coast.

The company had become a strong advocate of strategic alliances and used the full range of alliance options available—vessel sharing arrangements with other lines, pooling ships and equipment with other lines, slot exchange programs and joint inland management. Sea-Land reported that, prior to VSAs, the cost of operating the Sea-Land fleet accounted for 27% of its total costs; by 1990, that had dropped to 12.9% (Middleton, 1990). Encouraged by these results, in early March of 1991, Sea-Land Services Inc. announced it would join forces in an alliance with Maersk.

### *Learning to Dance..*

The two companies were a good strategic fit: each had substantial assets, a global perspective, managerial talent, commitment to quality, and a high level of customer service (Anonymous, 1991a). One critical attraction of the alliance for Maersk was Sea-Land's ownership by CSX, and the accompanying cooperation this brought on US mini-bridging and land-bridging operations. Sea-Land had strong market share in the northern US while Maersk was stronger in the south; the complementarity of service routes was yet another driver of the relationship (Anonymous, 1991b). The success of this arrangement coupled with P&OCL's withdrawal from its partnership with Maersk in favour of the Grand Alliance paved the way for the eventual "global alliance" between Sea-Land and Maersk announced in 1995.

To form the alliance, Maersk reviewed the whole of its service network and the assets deployed, met with a number of its customers, established future requirements of customers, analyzed the trade flows and then sat down with Sea-Land to design schedules. The alliance between Sea-Land and Maersk was geared toward three specific goals: providing reliable multi-week sailings in the principal Asia / Europe and North American / Asia routes, achieving faster transit times, and extending the global network to include direct calls at specific outlying (regional) ports. As a result, the alliance featured operational cooperation in most of Maersk's trades, with only Africa and Australia outside the agreement as Sea-Land did not serve those areas at the time of the announcement (Fossey, 1996).

Both companies agreed not just to ocean-side cooperation but terminal and equipment sharing as well. Together, the companies expanded their operations and profits, creating one of the more successful alliances in the industry, and one with enviable geographic coverage. The alliance provided an effective tool to reduce costs and rationalize asset use.

From Maersk’s perspective, 1996 profits rose 23% over 1995. The Danish carrier reported 1996 slot utilization in the high 80s (the industry average was 62%). In 1997 the company boasted nearly 10,000 employees in 250 offices in more than 70 countries serving over 80,000 customers worldwide (Damas and Gillis, 1997). Maersk’s strategy was successful in delivering global coverage and leadership through alliances, and 1998 was another profitable year.

This profitability enabled Maersk to grow through acquisition. In February 1999, Maersk announced it would buy the Safmarine Container Lines, a vessel operator ranked 20th in 1998 by *Containerisation International Yearbook*. The acquisition would allow Maersk to consolidate its operations in developing markets. Even before the Safmarine purchase, there were very few routes Maersk did not serve; the company had further consolidated its leadership position.

As for Sea-Land, the situation was not so rosy. In September 1995, John Snow, CSX’s chairman, president and CEO, reported that CSX was happy with Sea-Land and its relationship with A. P. Møller (Glass, 1995), predicting that the alliance would result in annual cost-savings for Sea-Land of US$75-100 million within three years (Machalaba, 1995). In 1996, against a situation of declining market rates, Sea-Land’s operating income increased by US$80 million (Anonymous, 1997). While Sea-Land reported its continuing satisfaction with its relationship with Maersk, its parent CSX was changing its tune. CSX was coming under significant financial pressure. Its 1996-7 bidding war with Norfolk Southern over the assets of Conrail had resulted in the company paying a huge premium for part of Conrail (Brooks, 2000); the impact on cash flow and debt was significant and therefore resulted in CSX looking for assets to sell. In 1998, the trade press reported Snow as saying that sales are always possible if the price is right (Bascombe, 1998).

CSX sold its barge subsidiary, American Commercial Lines, in 1998 and rumours circulated that Sea-Land would be next. After all, although Sea-Land accounted for 40% of CSX’s operating revenue in 1998, it only accounted for 11% of operating income, compared with 50% and 89% respectively for CSXT’s (rail) contribution. Furthermore, Sea-Land’s 1998 operating revenue was down 2% from 1997, itself down 1.5% from 1996 although traffic volumes increased both years (CSX *Annual Report 1998*). The operating ratio for the fourth quarter of 1998 was a mere 1.6% (Cauthen, 1999) and the company was struggling to come to grips with the Asian crisis. In favour of divestiture was the success of Sea-Land and Maersk's relationship; this had many thinking that it was time for the companies to restructure as one.

The first quarter of 1999 proved to be a difficult one for Sea-Land. Average revenue per box was down 3%, so the increase of 4% in volume translated to a 2% increase in total revenue (CSX *Quarterly Flash*, April 1999). In March of 1999, Sea-Land announced a restructuring that would separate its international container shipping company from its terminal and domestic shipping businesses (www.schednet.com, 18 March 1999), a move that would enable Sea-Land to isolate its heavily subsidized domestic shipping business from its international unsubsidized activities. Such restructuring is often seen by the financial world as the first step in either a spin-off or the isolation of a subsidiary as a target for a friendly takeover. CSX's *Quarterly Flash* indicated that the restructuring would enable the company to lower costs and 'take full advantage of deregulated global markets."

### *...As One*

On 22 July 1999, A. P. Møller and CSX announced Maersk was acquiring the assets of Sea-Land's newly created international operating company and 24 container terminals (but not the domestic shipping businesses or some of its terminal operations) for US$800 million. The deal was announced as "a natural development of the close partnership." It merged the largest carrier with the 6th largest (one which had been first less than 5 years earlier). It resulted in a truly global carrier with almost 11% of the TEU capacity worldwide and over 19% of the capacity on order (Boyes, 1999). The two companies faced little opposition in their quest for regulatory approvals (from the US Committee on Foreign Investment, Marad, and all the anti-trust authorities). On 6 October 1999, the European Commission approved the merger and concluded that a position of dominance would not be created or strengthened by it (Commission of the European Communities, 1999). The alliance had evolved into a sale as was long anticipated and predicted by many in the industry.

Since then, Maersk Sealand has worked towards the integration of the two companies, and to secure the new base from which it will compete. This new entity is completely separate from Maersk Logistics, which resulted from the integration of Sea-Land Logistics (formerly Buyers Consolidated) into Mercantile (part of A. P. Møller). A. P. Møller has used the acquisition of Sea-Land as an opportunity to isolate the two types of businesses—logistics activities and ocean carriage—as the former industry has higher operating margins and profitability than the latter. In the process, Maersk Sealand has not forgone the differentiated position of being unusual: a carrier with terminal interests. The acquisition has not blended two carriers so much as created new businesses differentiated distinctly from their competitors but under the single umbrella of the A. P. Møller Group.

## The Quiet Revolution or Merely Evolution

The entry of Sea-Land and Maersk jointly into the transpacific in 1991 marked the beginning of a new wave of cooperative business arrangements throughout the industry. Prior to this, carriers might cooperate in slot charters to provide more destinations to existing customers or they might add a vessel to a consortia because they were unable to provide a desired service alone. With this alliance, Maersk's with P&O in the Europe / Asia trade and the Sea-Land, P&O and Nedlloyd VSA on the transatlantic, the idea of strong companies cooperating with strong companies to multiply sailings was born. These were the earliest alliances of complementary equals, to use Bleek and Ernst's (1995) alliance terminology. In sum, Maersk and Sea-Land established a first-mover advantage with their 1991 alliance, and built on it in 1995 by making it both global and strategic. Competitors agreed with the cooperative strategy but lacked the commitment to fully secure the available benefits and create value through new joint initiatives.

What are the drivers of these changes in strategy for liner shipping companies? Many carriers have concluded that they can no longer grow solely through organic means. The past ten years have witnessed a dramatic shift in their strategies as they have engaged in mergers, acquisitions and strategic alliances, seeking to develop integrated door-to-door capabilities in response to a rapidly changing environment and the requirements of increasingly demanding customers. What will they do in future? It seems less likely that they will go it alone, developing the required capabilities through internal growth, and more likely that they will seek to fill the missing links in their networks through strategic alliances or seek unique positions through mergers with related and possibly boundary-expanding companies.

Even in the rapidly changing market dynamics, organic growth will be a favourite choice for some companies because managers prefer the pace and the extent of control implicit in the choice. Managerial preferences meant that both Sea-Land and Maersk, with their "go-it-alone" attitude, were not willing to move towards alliances throughout the 1980s. The price to be paid for lost independence was judged to be simply too great. Fears about loss of identity and loss of control abound. However, both companies evolved in their thinking in 1988-91 period. The better margins from landside activities coupled with the recognition of benefits from slot charters gradually encouraged management consideration of the alliance alternative. Unlike other carriers that experimented with closer but limited operational relationships, both Maersk and Sea-Land were prepared to make the relationship more.

The next shift in thinking among carriers occurred in 1995. Performance data indicated that alliances could generate significant financial savings and few of the Top 20 carriers possessed the financial capacity for merger. As a result, most carriers moved towards more globally oriented alliances, but only Maersk and Sea-Land made the depth of fleet and managerial commitment necessary to achieve a truly global strategic alliance. The members of the other three alliances committed only about a third of their resources to alliance-based "growth." In fact, alliances were seen by some as a means of retrenchment, given poor operating margins and limited profitability. Back office scale economics appeared to be the primary motivator to be weighed against managerial preference for continued independence. As shipping is dominated by family and private business interests, the importance of managerial preference cannot be underestimated in assessing the strategic choices of players in this industry.

The global strategic alliances of the latter part of the 1990s offered many carriers the ability to develop global networks to service large traders seeking broad market reach from a small pool of transport suppliers. Few carriers, however, maximized the opportunity restructuring afforded. Instead many choose to expand vessel capacity, further driving down rates in an already marginally profitable industry. The alternative was to develop new strategies focusing on more profitable related businesses, such as logistics, terminals and landside distribution. While some did follow this path, the strategies tended to result in mergers based on value extraction rather than value creation. Sea-Land, within the CSX family, was the poor cousin who seemed unable to maintain profitability or stature at the level expected by its parent or its shareholders. The opportunities were certainly there but the managerial preference for divestiture within CSX, really a rail company, was spurred by the excessive premium CSX paid for its share of the Conrail assets. Meanwhile, a more diversified Maersk, whose core business was shipping, was able to acquire Sea-Land and restructure to position itself to exploit the value creation potential of the accompanying logistics and terminal activities.

Will more consolidation occur? Probably. The market continues to grow from a combination of growth in the transport of manufactured goods (as world trade continues to grow in volume) and increasing penetration of containers as the preferred method of transport for semi-processed and finished goods. However, capacity growth will outstrip demand growth and carrier profitability is therefore likely to get worse in the short-term. This will continue to put pressure on profitability, driving those who only know how to extract value into merger (as an alternative to failure) while those with value creation skills will choose between alliances and merger based on opportunities for value creation and managerial preferences for growth and cooperation.

## Endnotes

[1] The background material on the industry is based on and an update of research done for Brooks, M. R. (2000), *Sea Change in Liner Shipping: Regulation and Managerial Decision-Making in a Global Industry*. It is used with the permission of Pergamon Press, Oxford, UK. Likewise some of the literature review and early material on the Sea-Land Maersk alliance are drawn from this source.

[2] TEU = twenty-foot equivalent unit or the capacity of carrying a unit of cargo 20' x 8' x 8' in dimension.

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