

## It's Bye-Bye for DHL Parcel Operations in US Market

### Service to End In January, 2009; Pricing Power Boost to UPS and FedEx; Opportunity for Regional Carriers?

#### SCDigest Editorial Staff

The long, strange journey of DHL in the US parcel market has come to an end with the announcement this week that the company would close its US parcel operation effective January 30, 2009. The company will, however, continue its US import/export, forwarding, and logistics services business here.

The announcement ends an odd saga in the company's attempt to penetrate the US parcel shipping market. After building a small direct US presence, DHL (a division of Deutsche Post) doubled down in 2003 with its acquisition of Airborne Express. That company was much smaller than either UPS or FedEx, but had developed a sizable customer base and was touted for its attention to customer service.

The combined company decided to close its internationally-focused Cincinnati parcel hub and move its sorting operation to Airborne's Wilmington, OH facility. But from early on, DHL was criticized for poor strategic decisions and the loss of Airborne's attention to customer service. It often used price to win customer business, but it never gained more than a small share of the US market, and the combination of those two factors led to substantial losses over each of the last several years.

Earlier this year, DHL tried to fix that situation with a strategy to radically transform its US operations. That involved a plan to outsource its airlift operations to UPS, a move that would effectively shutter its Wilmington hub and bring the loss of thousands of Ohio jobs. DHL also announced further increases in its existing outsourcing relationship with the United States Post Office for some local deliveries.

DHL executives said those moves were needed to cut losses, but that it intended to remain in the US

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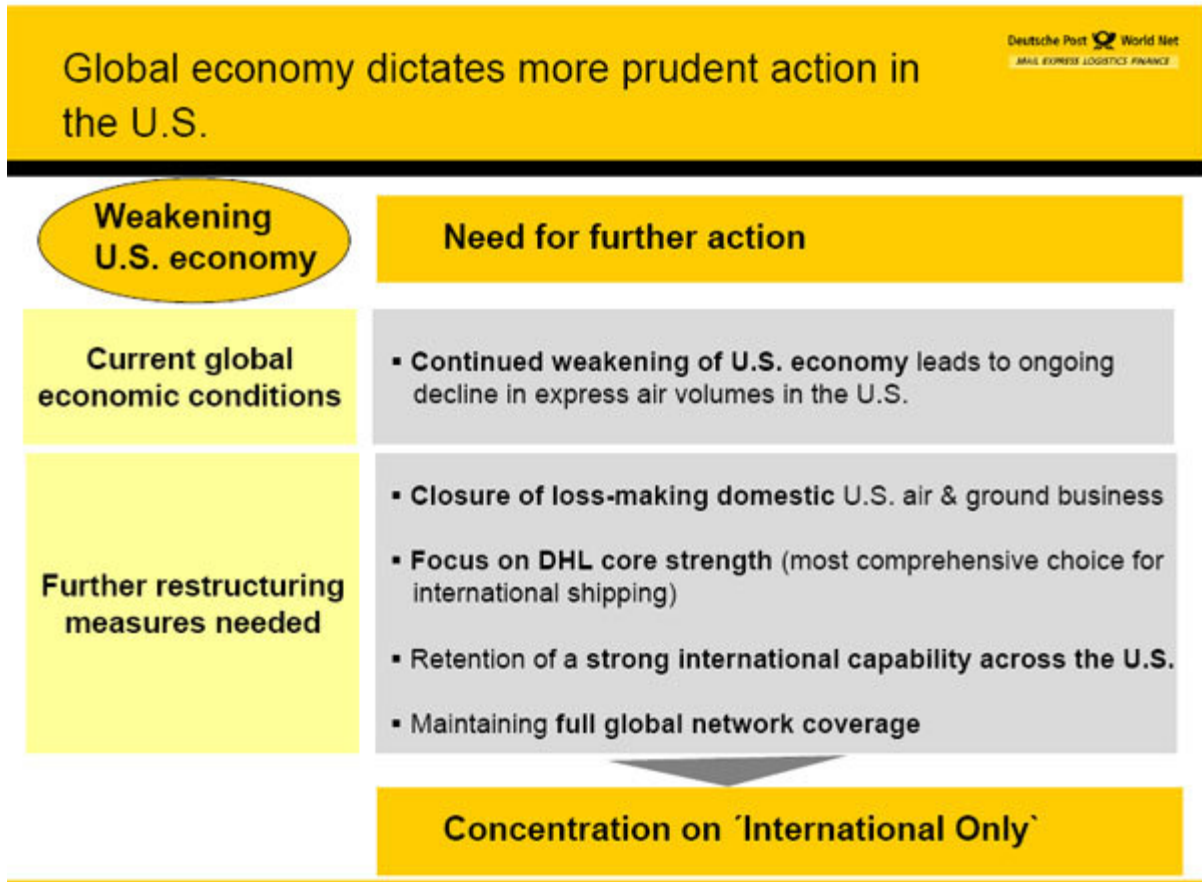
parcel market. Nevertheless, in May the company said it was still expecting to lose \$900 million in its US operations in 2009 even after the new strategy was in place. Some members of Congress wanted more investigations as to whether the UPS relationship would violate anti-trust rules, mostly in an effort to try to save the Wilmington hub operations and jobs there; the hub closure actually became a minor presidential campaign issue.

DHL made that a moot point with this week's announcement. In addition to the closure of the Wilmington hub, the company will also shrink its US network from 412 to just 103 stations, with those left open to support import/export shipments. The company said the pull-out was the result of "Continued weakening in the US economy, which leads to an on-going decline in express air volumes in the US."

There were reports DHL was seeing heavy defections in its customer base as a result of the May announcement, particularly because it had yet to finalize its outsourcing agreement with UPS. Many in May questioned the logic of announcing the net-

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**Deutsche Post Summarized its Plans for the US Parcel Market in an Investor Presentation this Week**



work changes without having a done deal first with UPS, as the announcement weakened DHL's negotiating position.

The company said it will still employ 3000-4000 in the US internationally focused express business, and notes it employs almost 25,000 in the US in its logistics services business, such as Exel Logistics.

The closure of all US parcel operations was predicted by many in the industry at the time of DHL's original restructuring announcement in

late May of this year.

**Impact on Parcel Shippers**

The real question of course is what the impact of the DHL move will be on parcel shippers. Early this year, parcel industry consultant AND ex-DHL sales executive **Gerry Hempstead** told SCDigest that "there would be a profound impact to carrier pricing offers and shipper cost if something were to dampen or eliminate DHL from the USA competitive landscape."

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"Today, DHL sets the benchmark for the bottom thresholds of pricing. There are deals out there that FedEx and UPS just would not handle at the price DHL offers," Hempstead said. "From a competitive marketplace point of view, I know that when DHL is in the game and the other carriers are aware of it, the pricing is significantly better from the competition."

**Ed Wolfe** of Wolfe Research says he expects UPS and FedEx to basically split the now up for grabs DHL US domestic business. Wolfe recently estimated that DHL was down to about \$2.6 billion in US domestic air and ground parcel shipment business.

While Wolfe says that will only raise UPS and FedEx revenues from 3-6%, he also sees the bigger impact being on price levels shippers pay given that the low price competitor is now gone.

We believe that DHL's removal from the US market should lead to material improvement in pricing for FedEx and UPS over time," Wolfe recently wrote in a research two weeks ago that said there were strong rumors that DHL's pull out in the US might be near.

One industry observer believes there might be opportunity for some regional parcel carriers as well.

"With DHL's announcement, there will be a rush to pick up the business between FedEx and UPS, especially in the current economic climate where the overall market growth is stagnant," said **Brian Hodgson**, vice president of marketing and business development for Kewill Americas. "With DHL's historical strategy to win on price, the larger regional carriers also have large opportunity as they have become a stronger force in US domestic market since the Airborne acquisition. In fact, some of the traditional DHL business may not be appealing to FedEx and UPS as it may not be profitable at current rates."

Obviously, greater pricing power for UPS and FedEx means higher costs for shippers. Economists have often noted that it is the presence of a third competitor that tends to create more competitive markets versus those with just two providers, or a duopoly.

"Shippers will rue the day that DHL left the competitive marketplace if that happens," Hempstead predicted in March.

We'll see if that proves true, but clearly not enough shippers believed so to turn DHL's US fortunes around.