Our Greatest Ever Inflection Point:

# Now is the Time to Change the Course of Maritime History

**Martin Helweg, CEO, P&O Maritime Logistics**

It was the former Intel CEO, Andy Grove, who said "Bad companies are destroyed by crises; good companies survive them; great companies are improved by them". This is a sentiment I agree with, but I would add that it can apply to whole industries too.

To be clear, I believe that both shipping and offshore energy are great industries – the calibre of the people working in them, and the value they create for the world is too great not to be. From working tirelessly to ensure goods and medical supplies keep moving when it matters most, to enabling the energy production that keeps lights on in homes, businesses, and hospitals around the world – our efforts have never been more important.

And yet, without question, we are now at an inflection point where we must choose between urgent, significant improvement - or destruction.

For far too long we have accepted massive inefficiencies in our business models and supply chain. Left unchecked, these problems will kill our businesses, wreck peoples' livelihoods, and irreparably damage the world's energy security and the energy transition.

This is unacceptable.

## What brought us to the brink?

Collectively, the oil & gas and shipping sectors have been living in a cocoon. The rest of the world has developed by using new technologies to transform business models, remove friction and create more value for customers. This process has been accelerating in different industries all around the world while we have been under the illusion this didn't really apply to us.

Offshore energy companies have focused on improving extraction and production, which is understandable given the economic benefits of enhancing the efficiency of your reservoirs by even two per cent. Yet they have also allowed their vital, commendable commitment to safety and need to have control of operations, create a risk-averse culture that has stifled innovation in other important areas of their business, such as logistics.

One result of this focus on the production cycle and a tendency towards the status quo is that oil majors have been using the wrong metrics to measure the efficiency of their supply chain, such as the amount of time vessels spend at sea.

The marine solutions industry, which conveniently makes its money from leasing out vessels, supported this mistaken way of thinking because it meant more boats would need to be leased out overall. Regardless of how empty they were, or how unnecessarily far they were sailing. Shipping companies became complacent and focused on the vessels themselves as being the core value we deliver - but they are not. Rather than considering the underlying service we provide, we allowed our remuneration to become completely decoupled from the real value we drive for customers.

***When you order something from Amazon - do you really care about the truck they use to deliver it? No! You only care that it arrives on time, in good condition.***

Now, I am not saying customers don't get value from our vessels, of course they do. It's just that the current business model offers no upside for shipping companies to find massive new efficiencies at scale and pass this value on to our offshore energy partners. Instead, marine organisations have been incentivised to operate ships with relatively little cargo just because this metric is not being measured.

As a result, oil majors have been heavily overpaying for services and assets they don't need, creating an estimated 30 per cent oversupply of shipping assets in the market.

This fairy tale cannot continue. Marine solutions business models must change.

Meanwhile, oil & gas have become labelled as bad, or dirty energy. Regardless of how accurate or fair this perception is, it means shareholders of international oil companies (IOCs) want these organisations to do something different, to become greener and more efficient. Even if some of the older IOCs have not quite worked out what this means yet.

On top of this, the COVID-19 pandemic created huge fluctuations in demand and added speculation in the financial markets meant the price of US oil turned negative for the first time in history. This created further conflict between oil companies and shareholders, who are now questioning the entire oil & gas business model too, demanding rapid step changes in efficiency and sustainability - and for good reason, in some cases.

Right now, offshore energy companies are holding 40 per cent more inventory than they need and ordering up to six months of supply in advance, on the false premise that the cost of shutting down a rig is too expensive to risk doing anything else. In reality, this is simply happening because the supply chain is not visible enough and not efficient enough.

This is why the oil & gas and shipping sectors are both facing a once-in-a-lifetime inflection point, one that will require us to help transform each other, to survive.

## The bleak future we face - if we fail

To understand just how high the stakes have become, it is worth considering what our intertwined destinies will look like, should we fail to make the progress customers and shareholders are demanding.

For marine solutions companies, what has been happening for the past decade will accelerate. There are already less than a handful of offshore shipping suppliers that are not in financial distress, having gone bankrupt or currently restructuring because of the oversupply of assets in the market.

Unless shipping pivots to create more value for customers, it will become increasingly commoditised and margins will keep getting slimmer. Technical reliability will no longer be a meaningful differentiator and outdated logistics and supply chain infrastructure will only make things worse.

## A new business model

Our customer needs have rapidly changed - commoditized models are no longer fit for purpose. We must adapt and evolve because status quo is not an option.

**Either we change our business model to adapt to customers' needs, or we become increasingly commoditised and vulnerable to market forces.**

**Old model**
Boat company

- Physical asset
- Technical reliability

- → Commoditized business model
- → Leasing contract provides no control over vessel and services
- → Vulnerable to market changes


Meanwhile, the shareholder pressure on oil and gas companies will keep increasing, as they become more unpopular with investors. To keep the peace, dividends - which are already high - will have to get higher and higher, regardless of price volatility.

**New model**
Integrated Offshore Logistics Provider

- Supply chain management
- Cost, efficiency AND reliability

- → Customer and supplier sharing rewards
- → Adaptable to the market and customer needs
- → Use competitors' assets in our model

Meaning more and more oil & gas fields become economically unproductive.

If this goes on for long enough, more IOCs will become marginalised, which means they are even less likely to be able to make the longer-term environmental and sustainability progress needed to attract investors. When your company performance becomes tied up with a country's economic fortunes, the pressure to deliver short term profits tends to increase.

In short, more pressure, less investment, less innovation - and less time to evolve. No one wins in this scenario.

So, what must we do?

## Simple solutions, but a more complicated long-term transition

One of our first solutions to help achieve change is a new, relatively straightforward model where we increase supply chain efficiency and reduce cargo delivery times - all whilst minimising costs for our customers. For example, if you want something within 24 hours, that requires more investment, but if you can wait a week, you can get it at a lower fee.

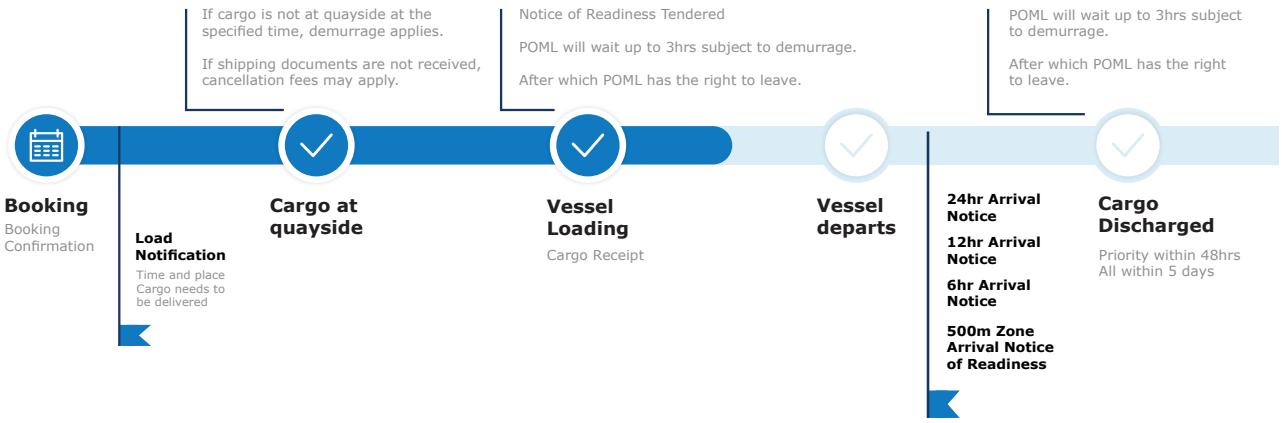
We call it **"Supply on Demand"**, and launched a successful pilot programme in Qatar, in January this year. This new model uses route and load optimisation to offer

marine services on a pay-as-you-go basis, meaning customers don't need to enter into restrictive contracts with offshore cargo providers. It's also a digital solution that provides customers with an online dash-board, allowing them to create bookings, track cargo, as well as monitor, analyse, and optimise routes to further reduce costs.

It's already proving popular because it immediately forges a closer link between our remuneration and what drives value for customers.

## The Process - You are in control

With the Supply on Demand model, the customer is in full control of their cargo movement, from the point of booking through to post-transit analysis.




## Terms and Conditions Compared to a time charter

EHSQ and marine assurance processes

Loading and discharging processes unless using Operator's berth (if offered)

Liability regime knock for knock, pollution, exclusion of consequential losses

Governing law

| | Supply on Demand | Time Charter |
|---|---|---|
| → The agreement only creates obligation when a Booking is made | ✓ | ✗ |
| → The agreement will apply unless terminated but only to the extent Bookings are made | ✓ | ✗ |
| → No responsibility for port fees or fuel | ✓ | ✗ |
| → Increased accuracy as to when goods must be available, time for loading and discharge | ✓ | ✗ |

- → Invoicing per transaction rather than a day rate
- → A bit more documentation around the specific shipment than under a time charter
- → Freight and Surcharges in case of cancellation, waiting time, overweight replaces the day rate
- → No responsibility for any taxes related to the vessel

**With this model, customers only pay for the cargo they transport, offering sustainable cost savings and efficiency gains through better use of vessel space, improved route planning and reduced fuel consumption. As well as enabling the optimisation of these variables in real-time.**

Pilot programmes like this are vitally important, but they are the tip of the iceberg compared to what we can, and indeed what we must achieve. Fortunately, the potential of these new models is incredible.

After reviewing two years of route optimisation data in one region, and verifying it in others, we believe we can deliver offshore 40 per cent faster using 30 per cent fewer assets. What this means for our oil & gas partners is paying less rent, for less inventory. Companies like Shell and BP spend billions every year leading equipment, up to 25 per cent of which is wasted because it's not used as it's stranded somewhere in their logistics supply chain.

If a new model like this can reduce that waste by up to 40 per cent, it will save international oil majors hundreds of millions of dollars in cost, by cutting down on inventory and leasing costs, fuel consumption and by freeing up more space on the rigs.

Now, it's worth noting that, in a world where UPS already uses algorithms to determine how many right turns its vehicles make, taking a more sophisticated approach to logistics in oil & gas and shipping should not be rocket science. Rather, it is a test of our mindset and our willingness to fundamentally question how and why we do things - just like Tesla questioned how you even build a car. In fact, there's a lot our sector can learn by looking at how the car manufacturers like Mercedes approach logistics. They operate using just in time delivery and yet wouldn't dream of letting a C-class leave the factory without a single part just because it didn't arrive in time.

Similarly in renewables, companies have a different mindset because their solutions were born on state and government subsidies, with negative margins. They never had a choice but to optimise for every single dollar spent, and as a result, have paid much more attention to creating world-class supply chains.

***This tells us the biggest barriers preventing us from achieving long term change, are not technological, but cultural.***

As shipping companies, are we able to make the necessary shift to get on the same page as our customers about what value means to them? This means realising our boat's specifications, the propulsion system, or the size of the crane on the back deck… None of this really matters anymore. We must instead offer our customers vehicle-agnostic logistics services that focus on speed and efficiency above all else.

Are oil & gas companies willing to accept they are not logistics companies, that the time has come to let go and delegate management of certain elements of the supply chain? So that the right expertise can help find them the massive new efficiencies they so badly need and free them up to focus on the extraction and production they do so well.

These are the biggest questions we face.

## How do we make this work in the real world?

Achieving this shift is going to require listening, dialogue, and investment – in technology and people. The pull is there from customers, but we will have to engage all stakeholders and understand their individual worldviews. The existing model is comfortable for many reasons and makes complete sense to many people because of their frame of reference. It is based on technical reliability, makes daily revenue easier to predict, and we don't have to worry about how fully loaded the boats are. Why would they want to change this?

To many people, modern logistics and supply chain management will be new, different, and not well understood. We must communicate to our captains, vessel operators and engineers why they are still essential, why we need to measure success differently and share more data with each other. That it is vital for evolving our operations and creating a more sustainable business for everyone.

Ultimately, change is going to come down to two basic parameters: capability and willingness.

There are only two or three marine solutions providers in the world that have the capability to drive this progress because they are not under massive financial pressure, that also have the technical expertise to deliver this kind of innovation.

Similarly, there are less than a handful of shipping companies whose leadership, staff and shareholders get the big picture, understand the vision, and have the willingness to change.

I believe P&O Marine Logistics is the only company in the world that has both the capability and the willingness to make this happen. As such, this is a big opportunity - but it is also a massive responsibility - because it means we have an obligation to step up on behalf of our industry.

It's also going to take agility to adapt to market conditions as we go and a degree of patience. We know service contracts in our sector are firm and usually a minimum of 12 to 18 months long.

## A roadmap for change and the team that can deliver it

Right now, we have expanded our Supply on Demand model, from Qatar to new regions including Nigeria.

The next step after this will focus on integrating the offshore supply base and removing a lot of the inefficiencies from the transitions between energy fields, the shore, and the vessels. Throughout this area of the supply chain, we are seeing too many disconnected organisations not using data or managing end-to-end logistics properly.

***We are working towards an offshore logistics model in which combined shore bases, quaysides and vessel operations for major capital projects are supported by tailormade IT systems for each of our clients.***

***With the different links in the project cargo cycle connected for the first time, customers benefit from speed, transparency, and cost savings, all the while enabling planning security for the critical last-mile delivery. This is part of P&O Maritime Logistics' phased roll-out approach to using big data with the goal of becoming an end-to-end logistics provider.***

**Christian Arndt**, Vice President Logistics at P&O Maritime Logistics

Long term, I can envisage a future where oil & gas companies do not even have to worry about the supply chain, if they don't want to - we can manage as much of it as they are comfortable with. The efficiency gains from

not owning inventory could be even greater. I would estimate oil majors have about 30 per cent more inventory than they need, give or take. What if we could just lease them that equipment directly for as long as they need it?

By using a just in time model, we could supply multiple companies interchangeably and cut down on wasted equipment and unused inventory across the whole industry. A truly optimised supply chain will mean if it is something that can be delivered, like a spare part, it will be delivered – right on the day it's needed, whether it's drilling equipment or pipes.

This is the kind of new business model that could save our partners millions, and drive efficiencies at a scale our sector has so far only dreamed of. Indeed, if there is anything I have learned from the disruption of the past 18 months - and the two years of data we have analysed - the potential value of these changes is much, much bigger than I had previously imagined.

From watching my team at P&O Marine Logistics respond admirably to all the disruption during 2020, I have also learned they have the character and the skills to make this vision a reality. The strength of our will, our capacity for change, and the speed at which we can adapt is far greater than I had realised, and we haven't even hit top speed yet.

Which, as I said, means we have an obligation to seize this incredible opportunity. If we get this right, we could shape our industry for decades, and contribute to the energy transition and global supply security for generations to come.

I for one, refuse to let this chance slip through our fingers.

If you are interested in being part of this remarkable journey, please do get in touch by dropping Martin's team a line at **POML.Communications@pomaritime.com**.

We would love to speak with you.