Good Time to Rethink European Distribution

By David Bovet

David Bovet is a partner at Norbridge, Inc., where he leads the supply chain consulting practice. He can be reached at dbovet@norbridgeinc.com.

Why should U.S. companies focus on their distribution networks in Europe? Headlines about Greek sovereign debt and German unhappiness at "rescuing" the euro could give pause to expansion strategies aimed at Transatlantic markets.

Yet the European Union (EU) remains a $16 trillion economy, the world's largest. Many U.S. companies are seeking to further diversify their business globally, hedging bets and searching for new geographies. American exports to the EU are up 3.5 percent, in nominal dollar terms, this year (January-April) over 2009. Meanwhile, despite a reversal in the past few months, the U.S. dollar is still down by 27 percent versus the euro since ATMs across Europe first started dispensing the new currency in January 2002. And Europeans remain among the wealthiest consumers in the world—six countries in Europe currently have higher nominal GDP per capita levels than the United States.

Drivers of Location Decisions

Where to begin in thinking about establishing, growing or simplifying a European distribution network? Whether starting from scratch or adjusting current locations, it's critical to consider the customer base, projected growth and service requirements. Product characteristics, such as demand variability and freight intensity, are also essential ingredients in setting network parameters.

Logistical considerations span three key aspects of the supply chain:

1. Market proximity (outbound)

- Reaching European customers quickly and cheaply. (For many, overnight truck delivery; for others, rail and inland waterway access.)
- Avoiding congestion and restrictions.
- Minimizing "last mile" cost to customers.

2. Gateway logistics (inbound)

- Inbound sourcing (e.g., from China, United States, Eastern Europe).
- Proximity and capacity of seaports, airports, autoroutes.

3. Hub efficiency (DC operations)

- Occupancy or outsourced hub costs.
- Management, labor skills, cost and flexibility.
- Tax levels and incentives.
- Regulatory ease of doing business.

The optimal solution, in terms of total delivered cost and service, will vary from one company and industry to another. But as in the U.S., certain patterns are apparent that bracket the likely answer for many businesses.

European Distribution Patterns

Wealth and income remain concentrated in Europe's west and north. The "Blue Banana" of wealth in Europe cuts a swath roughly from Birmingham in the UK, across the Channel to the Benelux countries, through Germany, France, Switzerland and northern Italy to end up in Madrid, Spain. This is still true despite the dramatic expansion of the EU towards the east and south. While manufacturing has moved eastward to lower-cost areas, wealth itself remains—for now—in the traditional heartland of Western Europe. For example, GDP per capita is $48,000 for the Netherlands versus $11,000 for Poland.

Traditionally, the Benelux countries (Belgium, Holland and Luxembourg) have been major locations for European distribution centers. This is driven by a number of natural advantages, including proximity to major gateways:

- *Seaports:* Rotterdam and Antwerp are Europe's two leading container ports, together handling 17 million TEUs in 2009.
- *Airports:* Airfreight is also well-served in these countries, with the four main airports

(Amsterdam, Brussels, Luxembourg and Liège) handling about 3 million metric tons of cargo per year.

In addition to excellent gateway infrastructure, the international distribution role is highly developed in these countries. Clear strengths include:

• *International trade genes.* The Netherlands, in particular, has been trading for centuries.

• *Language capabilities.* The Dutch typically speak two languages other than their own—English, German, often French or Spanish as well. Staffing a customer service center that covers much of Europe is relatively easy to do in the Benelux countries.

• *Road links.* Benelux is closely tied to the major European markets.

• *Management and labor.* These countries excel in producing well-educated and experienced warehousing and transportation professionals.

• *Government policies and incentives.* The Netherlands, Belgium (both Flanders and Wallonia), and Luxembourg all offer favorable tax rates and incentives.

The downsides to these locations, particularly in parts of the Netherlands, reflect the consequences of their own success over the years. Road congestion can be a major problem. The population density and limited land for expansion make road freight movement slow in many parts of the Benelux, particularly along the axis from Antwerp to Amsterdam. Building costs can be problematical, too. Due to the scarcity of land and the existing high density of construction, the Netherlands is not low-cost in terms of DC space. However, parts of Belgium (Liège, Hainaut) are not as developed and offer reasonable real estate costs.

Recent Activity

Where are companies locating their European DCs at present and why? Despite the global recession, new facilities are being built and public agencies are more focused than ever on attracting certain kinds of investment to their region. Here are a few examples that illustrate recent activity and the underlying rationale.

The Netherlands. Several U.S. companies have announced new distribution facilities in the Netherlands this year, for example:

• Warnaco Group, a U.S. apparel maker (with brands such as Calvin Klein and Speedo), is building a 30,000 square meter European distribution center near Roosendaal (midway between Rotterdam and Antwerp). Warnaco is consolidating its operations, closing distribution centers in France and Italy as well as an existing logistics site elsewhere in Holland.

• Stryker, a U.S. medical technology company, is partnering with property developer Goodman to build a new 7,875 square meter warehouse in Venlo, Holland, which will gain sustainability certification.

Wallonia in Belgium. This is the French-speaking area, in the southern half of the country. A recent study named Wallonia the best European DC location, because of its available land, incentives offered and good transport infrastructure toward the south. Examples:

• Hennes & Mauritz (H&M), the global Swedish-based apparel retailer, recently announced its selection of a site in Hainaut, Belgium, for distribution of garments all across southern Europe. Wallonia was the group's first choice because of the attractive price of greenfield land, the quality of the work force and the availability of investment grants.

This is an opportune time to assess your European distribution network.

• Skechers, a U.S. footwear maker, recently expanded its European logistics center in Liège to 41,000 square meters.

Other regions of Europe. Much depends on target markets and on sourcing.

• To serve the Nordics, for instance, the Copenhagen area is ideal. This is due to the overnight truck delivery possible to some 80 percent of the population in Denmark, Norway and Sweden. The Øresund Bridge, an 8-km engineering marvel, now directly links Denmark with Sweden. Distances are too great, from the Benelux, to support next-day truck delivery to this area.

• Distribution centers are also being built in the eastern countries of the EU, where manufacturing has expanded rapidly. Poland, Hungary, Czech Republic and Romania, for example, have all gained new plants and DCs in recent years. Dell and Lenovo build notebook computers, and Delphi makes auto parts, in Poland. About 1 million square meters of warehouse space was leased in Poland during 2009. And U.S. logistics facility developer ProLogis had half its total European rentable DC space in the Czech Republic, Hungary, Poland, Romania and Slovakia, at end-2009.

Bottom Line

The economic recovery is uneven in Europe, as in the United States. Yet for American companies, this can be a good time to acquire space for expansion or to consolidate older country-level DCs to a single site.

The market strategies, understanding of customer needs, and considerations involved in designing an effective European distribution network and locating key DCs are more complex than in the U.S. National and regional differences in transport infrastructure, land availability, tax incentives, and worker skills are all important considerations in making successful decisions.