WERNER ENTERPRISES AND CHINA

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ABSTRACT

Established in 1956, Werner Enterprises has gone from a small one-truck local operation to a multi-national, multi-billion-dollar global logistics and trucking firm that is an industry leader in innovation and technology while being renowned for its quality service and trustworthy appeal. As the economy continues to become more integrated and globalized, Werner has responded by expanding services into Mexico and Canada. In 2005, Chinese regulatory restrictions became more accommodating to foreign investment, and Werner faced a dilemma, which this case encourages students to address: should this North American giant go truly international by making a jump to mainland China?

INTRODUCTION

As it transitioned to a market economy, China had allowed businesses to partner with domestic manufacturers to bring money to the country without sacrificing the revenues. China's developing economy may present great opportunities for new sources of revenue, though, especially in industries experiencing slowing market growths where competition for market share seems to be the only means of survival. The introduction of wholly foreign owned enterprises to China may settle some fears potential businesses' may have before entering Red China. According to Business Registration Services in China, a WFOE is "a limited liability company wholly owned by the foreign investor(s)" [1]. WFOEs were originally designed to bring export-oriented businesses and newer technology to China. Since this, WFOEs have been expanded to include many different types of businesses, including consulting and management firms, like Werner Enterprises.

Pathtochina.com lists many distinct advantages to obtaining a WFOE in China:

- Independence and freedom to implement the worldwide strategies of its parent company without having to consider the involvement of the Chinese partner;
- Ability to formally carry out business rather than just function as a representative office and being able to issue invoices to their customers in RMB and receive revenues in RMB;
- Capability of converting RMB profits to US dollars for remittance to its parent company outside of China;
- Protection of intellectual know-how and technology;
- No requirement for Import / Export license for its own products;
- Full control of human resources; and
- Greater efficiency in operations, management and future development [1].

In the process of obtaining a WFOE, the most important portion is defining the business scope. Companies are only allowed to operate within the defined business scope approved by the government. If the business later on would like to expand their business opportunities in China, they would need to submit further documentation explaining why and how they would like to change the scope. Another important aspect of the application is the registered and paid up capital. The registered capital is the amount of investment that a company will put towards the new venture in China until it can begin to operate from its own profits. The paid up capital is 20% of the registered capital that will be paid within the first two years. After the business has begun to make a profit, it is able to send the profit back to the home country without needing government approval. The only stipulations are that the company cannot give dividends if the company has not covered previous years' losses, but may hold back dividends to give at a later date.

Werner's History and Overview

Werner Enterprises began as a small one person interstate trucking operation in 1956. Clarence L. Werner was a 19-year-old entrepreneur, who sold his 1953 Mercury for a 1956 Ford Truck. At the time, interstate licensing required that the holder be 21; however, due to illegible type on a doctor's certificate, C.L. received the license and was able to begin operations [2]. The early operation transported commodity goods across state lines on a per-trip basis. At the time, hauling commodities was a less-regulated business than manufacturing goods and had fewer entry barriers, making it a prime choice for him. C.L. officially adopted the name Werner Enterprises in 1959. In 1964, Werner Enterprises purchased its first facility in Council Bluffs, Iowa.

In the early years of the trucking industry, the federal government heavily regulated the transportation of manufactured goods across state lines. This regulation allowed a small number of large carriers to hold a very large share of the market for a great numbers of years. Deregulation of the trucking industry in the 1970s and 1980s allowed Werner Enterprises to capitalize on new markets formerly protected by government regulation. The once protected carriers formerly had very little need to continually update their equipment, and as a consequence many had large quantities of older equipment with less fuel efficiency and capacity. This gave firms like Werner Enterprises, which have continually upgraded their equipment for better efficiency and capacity, a competitive advantage with the ability to haul more for less cost [2].

With newly deregulated markets, sales grew from $7.9 million in 1977 to $73.7 million in 1985. This expansion led to Werner Enterprises' initial public offering on the NASDAQ in 1986 under the symbol WERN. Werner sold 2 million shares of stock at $17 per share, which rose to $22 per share within three months. The new investments allowed Werner Enterprises to expand both its trucks and facilities; Werner opened four new facilities nationwide in 1987 and employed nearly a thousand drivers. By 1989 the company's gross sales revenue had grown to $191.4 million [2].

During the 1990s, Werner strengthened its reputation as a technological leader in the transportation industry as it implemented Qualcomm's OmniTRACS mobile communication system in 1992, became the first carrier to implement totally paperless logs in 1998, and adopted Systems Management and Resource Tracking (SMART) systems. Werner offers satellite communication equipment, which was installed in the company's entire fleet in 1992, allowing Werner to adapt to the Just-In-Time (JIT) manufacturing and stocking techniques now practiced by many retailing businesses. The GIS system allows customers to log onto Werner's website, enter their cargo details, and view exactly where in the world their shipment is 24 hours a day, 7 days a week. Customers can also see where the cargo will be traveling next, and the amount of time until it arrives at their doorstep. The GIS system has served as a safety measure for Werner Enterprises as well. Drivers can be located at any time, which ensures their

safety in the event of severe weather, natural disaster, or otherwise. Due to this technology, Werner promises high on-time delivery service and low accident ratings.
The SMART technology in Werner trucks is also a large part of Werner's Transportation Management System (TMS). TMS systems are used to support special project needs, such as those called in by the Emergency and Surge Event (EASE) management. EASE specializes in product needs, such as when a natural disaster occurs, there is a seasonal surge in demand, or a new product is being rolled out. Werner also offers consolidated, one-time billing for the entire transportation management process [5].
In 2005, Werner was ranked as 816 on a *Fortune 500* Annual Ranking of America's Largest Corporations. This was a higher ranking than received in 2004, which was 858. Werner was ranked the 7th highest in the Trucking, Truck Leasing Industry and had the 7th highest revenues. By achieving rankings such as these, Werner has successfully built a brand identity for responsibility and accountability. A familiar sight in the Midwest is the blue Werner truck, and they are beginning to be just as recognizable worldwide.

Service Offerings

As of 2005, approaching their 50th year of operation, Werner Enterprises was the third largest publicly traded trucking company and now boasts ownership of 8,750 tractors and 25,210 trailers, which are geared primarily to be used in intermodal transportation, such as transferring containers from a ship to a train. Werner has six operating fleets in the Truckload segment: Dedicated, Regional, Van, Expedited, Temperature-Controlled, and Flatbed containers.
While the majority of Werner's operating revenues are generated from trucking, non-trucking revenues generated by four operating units in Werner's Value Added Services (VAS) segment, also make a significant contribution to the bottom line. VAS units include brokerage, international, intermodal, and freight management services. Werner's brokerage services are supported by a Capacity Management Team that forges relationships with carriers and bridges the gap between shipment origin and shipment destination. The brokerage division creates one simplified plan to use air, ship, train, or truck to provide smooth transport and on-time delivery. The international services include offices in Mexico and Canada as well as the United States that employ nationals and bilingual customer service representatives in order to increase ease of transport and provide customer satisfaction. Intermodal services are provided by over 1,500 free-running containers that can easily be trailed behind a truck, stacked onto a steamer, or placed on a train to travel around the globe. Freight Management services refer to Werner Enterprises' ability to act as third-party logistics providers for their customers. Retailers wishing to outsource their supply-chain management function can turn to Werner because they have specialized in integrated, international, and intermodal transportation, as well as warehousing, and can cater to any delivery service for which their customers realize a need.
Werner also owns a small aircraft fleet and has developed several alliances with other intermodal transit carriers. Combining forces with airlines, ocean carriers, and railroads, Werner can haul their customers' product in Werner trailers for the duration of the journey which ensures that, as an international company, Werner's service capabilities allow its employees direct responsibility for every shipment and provide security to their customers. Werner's alliances have catapulted Werner into the freight management industry and allowed the company to create hybrid, custom tailored solutions for customers looking for services ranging anywhere between trucking and freight management.

Financial Status

After the terrorist attacks on the World Trade Center Towers on September 11, 2001, and the subsequent recession, Werner downsized its fleet size, reduced its debt from $100 million to $60 million, and paid

off its Long-Term Debt entirely. In the years since 2001, the economy has begun to pick up again, and Werner has expanded with it while continuing to minimize its debt holdings. In the wake of September 11, Werner stock prices fell from $13.08 per share to $11.70 per share. As of December 31, 2005, Werner stock value had risen to $19.70 per share, and Werner's Net Income as of December 31, 2005, was $98.5 million. When considering a move into Chinese markets, a potential threat to Werner's financial stability is the currency exchange market and complications that could arise from dealing in foreign currency. A potential move to China is a bit more complicated than moves into either Canada or Mexico because the Chinese RMB was 'pegged' to U.S. Dollars at 8.28 until July 21, 2005 [3]. At this time, the currency was reevaluated to reflect a basket of goods and was revalued at 8.11 RMB per U.S. Dollar. This revaluation could continue to cause some variance and uncertainty in evaluating future revenues and expenses in China.

Both the Truckload and the VAS segments generate operating revenues. In 2005, total operating revenue amounted to $1.9 billion, which was a $300 million (15.7%) increase from 2004 operating revenues. Cash from operating activities amounted to $172.5 million. Trucking revenues accounted for approximately 75% of Werner's total operating revenues, and non-trucking revenues created about 12% of Werner's total operating revenues. Fuel surcharges created another 12% of operating revenue, and other operating revenues accounted for the remaining 1% of total operating revenues. Werner also sells used trailers and other transportation equipment in the secondary market, creating some additional revenue. A map of fleet truck sale locations is shown below.

Trucking services, Werner's largest revenue generating segment, typically calculate revenues on a per-mile basis. In 2005, average annual miles per tractor totaled 120,912, with average percentage of empty miles at 12.2%. The average revenues per loaded mile were $1.069, and average revenues per total mile (including empty miles) were $1.413. This brought the average revenue per tractor per week to $3,286, an increase of 4.5% from 2004. The operating ratio (a company's operating expenses as a percentage of revenue) is a commonly used measure to evaluate profitability in the industry. In the transportation industry, a large percentage of revenue is required to maintain operations; thus, a low ratio is desirable. Werner operated at a 91.6% expense to revenue ratio in 2004. This ratio remained relatively constant, rising slightly to 91.7% in 2005.

Competition and Market Analysis

In 2003*,* the trucking industry consisted of 8.9 million jobs, of which 3.5 million of those employed were truck drivers. The industry also had nearly 15.5 million trucks in operation, with 1.9 million of these being tractor trailers. Over 360,000 trucking companies were in operation in 2003. Ninety-six percent of these companies had less than 28 trucks in their arsenal, and 82% of the companies operated with six or less trucks.

The trucking industry has been very profitable over the years as well. In 2003, the total revenues of the industry summed to almost $255.5 billion. Werner Enterprises is listed at number 12. Expenses associated with these revenues, ranging from administrative salaries to truck maintenance, averaged at around $243.2 billion, leaving a profit of only $12.3 billion for the companies in the industry. One of the major expenses is the cost of operating on the roads, which amounted to over $21 billion. Another important expense, especially with a green initiative being a primary focus in today's business, was the 53.9 billion gallons of fuel used on average per year in the industry [4].

In order for any of these trucking companies to survive, though, it must be able to accomplish some key components to the industry. For the logistics division, diversification and access to latest technology are necessities to keep in the game. Diversification is important for offsetting any potential losses on the asset-heavy divisions of the business by partnering with multiple carriers, and the technology helps in offering the customers the best option for what they want to accomplish. For the trucking division, it is

important to have financial stability and late-model equipment. The equipment is needed to transport the products, and even in the presence of possible economic downturns it is necessary to replenish the supply of trucks and keep optimally-working trucks on the roads.

Werner's International Experiences

In response to the recently enacted NAFTA agreement, Werner expanded its operations into Mexico in 1999 and into Canada in 2000. Werner obtained several licenses, awards, and certifications that allow for ease of transport between the United States, Mexico, and Canada. Such recognitions are integral in crossing borders with large amounts of cargo. Werner is a U.S. Licensed Non-Vessel Operating Common Carrier (U.S. NVOCC) freight forwarder, a member of the Customs-Trade Partnership Against Terrorism (C-TPAT), and utilizes the International Air Transport Association (IATA), and the Airforwarders Association. Werner is also Transportation Security Administration (TSA) approved, and participates in Partners in Protection (PIP) with Canada and Mexico. All of these factors allow Werner to transport freight through customs in and out of the United States.

Because it was moving to a new country, Werner hired several nationals for the Mexican operations. Issues, such as taxation, benefits, and wages differences for employees, were successfully navigated. Each unforeseen catch provided a learning experience and knowledge. For native U.S. employees, informal training sessions were held to familiarize everyone with differences in culture and customs. E-mails, meetings, and advice from employees comfortable with Mexican customs were circulated to ensure everyone was comfortable before a business trip or new international venture. Werner Enterprises now boasts two Werner-owned terminals on the U.S./Mexico border, three trans-load facilities at border locations, ten crossing points between countries including El Paso, TX, Otay Mesa, CA, and Douglas, AZ, and four offices in the interior of Mexico. Werner also has bilingual operations personnel onsite at each border crossing location, bilingual sales and customer-service personnel at each office in Mexico, has grown to over 100,000 shipments into and out of Mexico annually. Werner Enterprises is one of the top five truckload carriers providing service to and from Mexico [6].

The decision to move into Canada was due to many of the same factors. Many of Werner's customers were making the move, and requesting that Werner come too. After successfully beginning operations in Mexico, the move to Canada proved easier to navigate. Language and cultural barriers were not as hard to learn, and Canada's political arena and economy have historically been more stable. Once again, Werner has successfully grown and now provides services to all ten Canadian provinces.

In the American competitive context, Werner has been focused on an asset-heavy one-way truckload business plan to focus their energies on succeeding in the transportation industry. In Canada, Werner began operations in 1999 following a similar business model as in the United States. Werner took their current operations in the United States and expanded as though no border separated the two countries.

In Mexico, the company decided that a light asset approach may be more beneficial as they are operating mainly in bringing products across the border to and from Mexico and the United States, not setting up shop for a long-term substantial investment of competing in the Mexican transportation industry as a separate entity. Also, the inability to take their tractors south of the border due to government regulations made it impossible for Werner to treat Mexican operations like the United States' business plan. Most of their business operations in Mexico were to transport products made in Mexico to United States' retailers, transporting over 350 truckloads across the border every day, establishing its place as one of the top five U.S. trucking companies with transportation services in Mexico.

Both previous expansions across American borders had proven successful for Werner, especially in Mexico. The company had expected Werner de México to operate in losses for two years. The new division successfully exceeded expectations, though, turning a profit within only 18 months. Less than two years later, the division was even operating in the green. But would these same results be possible across the Pacific Ocean? Does a WOFE make sense for Werner?*

CASE DISCUSSION QUESTIONS

1. Analyze Werner as a competitor. What are its competitive strengths and weaknesses?
2. Based on your assessment of its resources, capabilities, and knowledge, can you construct a value chain that depicts how Werner creates value?
3. How can this value chain be transformed into a blue ocean strategy canvas?
4. Does Werner have at least one sustainable competitive advantage?
5. What are the advantages and disadvantages of competing in China?
6. What factors are critical for success in the trucking industry?
7. What role does Werner's prior international experience contribute to its decision to enter China?
8. Should Werner enter China with a WFOE?

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*The complete case and teaching note are available from the lead author.