SURVEY Industry Watch

Mergers and disruptors impact on supply industry stability

ANDREAS SCHWILLING
Partner, Transportation
Roland Berger

The last year has seen further consolidation among system integrators and their principal sub-suppliers, potentially altering the degree of vertical integration and the balance of negotiating power between the two groups. We asked our panel whether they expected this to change in the coming years.

The past few years have seen significant mergers and acquisitions activity in the railway supply industry. Following the combination of China's CNR and CSR in 2015 to form the world's largest rolling stock builder (p36), the resulting CRRC group is reportedly in discussions to acquire Czech rolling stock manufacturer Škoda Transportation. Hitachi Rail Europe has taken over AnsaldoBreda and a majority stake in Ansaldo STS. And Swiss rolling stock builder Stadler purchased Vossloh's Spanish locomotive and tram business in late 2015.

M&A activity is not only taking place at the OEM level, but also among the leading suppliers of components and subsystems. US-based Wabtec Corp has been steadily acquiring smaller businesses in many rail-related fields, most recently taking control of French brake and air-conditioning manufacturer Faiveley Transport. This year, Vossloh has agreed to the sale of the former Kiepe electrical components business to the Knorr-Bremse group, and has completed the acquisition of Denver-based sleeper manufacturer Rocla Concrete Tie to strengthen its core infrastructure business.

So there has been a lot of consolidation in the industry, and we can expect this to continue. The key question is whether such takeovers will change the balance of negotiating power between manufacturers and their principal sub-suppliers. We asked our panel of senior executives what changes to the industry structure they expected to see in the coming years.

Almost half of all respondents felt there was no clear trend, particularly in terms of more insourcing by the larger groups. Some manufacturers would strengthen their position while others would lose negotiating power, and the same would apply to the Tier 1 suppliers.

However, 23% of respondents believed that the bigger manufacturers and system integrators would 'flex their muscles' and increase the degree of vertical integration, strengthening their hand when negotiating with sub-suppliers. This poses the interesting question as to which subsystems or components are most likely to be brought in house. We could perhaps anticipate a focus on train management systems as the first candidate; technologies which integrate the control of other onboard sub-systems are increasing their 'share of wallet' in terms of the overall price of vehicles.

Only about 8% of respondents felt that negotiating power would shift the other way, to the Tier 1 suppliers. There was no widespread belief that such companies would increase their share of 'value added' for key vehicle components such as brakes, doors or air-conditioning, given that the OEMs retain a high level of vertical integration, continuing to manufacture bodyshells, running gear and traction equipment themselves.

By contrast, almost a fifth of all respondents believe that the railway supply industry is facing significant disruption. These 19% anticipate that market trends such as digitisation and disruptive innovation will see the rise of new players, taking share from both manufacturers and their sub-suppliers.

Traditional players will have to react through their own digital transformation, adapting their business models and increasing the level of innovation. As a recent Roland Berger study on the digitisation of the rail supply industry pointed out, companies need to harness the trends to transform their value chains, including productivity enhancements and cost reductions.

Overall, our panel's responses suggest that the industry expects only limited changes to the balance of negotiating power between manufacturers and sub-suppliers. Players that 'do their homework' in terms of innovation, digitisation and continuous transformation to meet customer and market requirements have the best chance of remaining competitive, increasing or at least maintaining their market share.

The global rail market environment continues to be attractive, with Unife predicting a stable rate of growth at 2·6% per year until 2021 in its latest World Rail Market Study (RG 9.16 p121). Start-ups focusing on digital products and services can be expected to take a proportion of spending from the established OEMs and Tier 1 suppliers. But several of these start-ups are likely to end up being taken over by bigger players, as with Alstom's recent purchase of Nomad Digital. And of course many manufacturers are already developing their own digitisation strategies. ■

To find out more about the survey and apply to join our panel, visit the RSIW website at: **www.railsupplyindustrywatch.com**

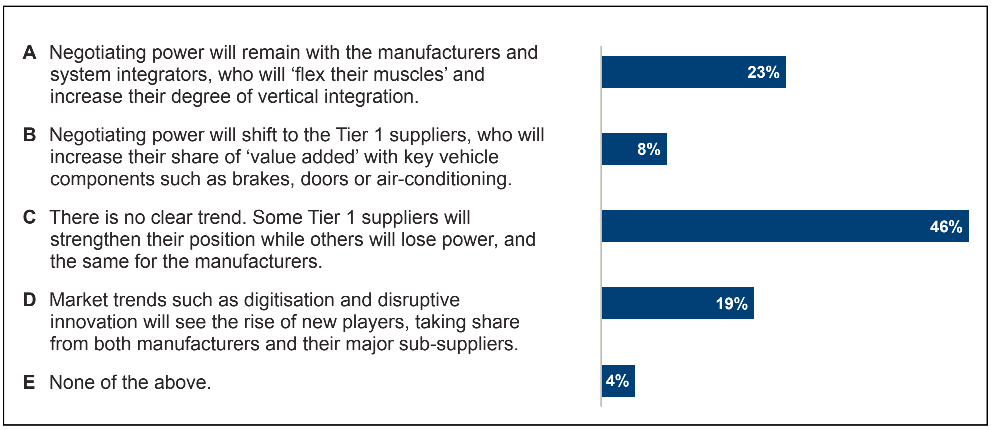

Fig 1. Respondents do not see clear trends in the evolving rail sector, but digitalisation is expected to have a significant impact.