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# Do or Die: The Dilemma of Aalaya Logistics

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**Abstract**

Mother India throughout the years has been a homeland of successful family owned businesses. Companies from Tata, Birla to Reliance all have the label of a family owned business. We are always audacious about the successes but we seldom care about the vast majority which fail doing business. The use of rule – of – thumb management has affected their business in the long – run. Some remain in limelight for some time and suddenly vanish from the scene. They fail miserably in forecasting the business environment as well as decision making. This case discuss on one such company which is reeling under pressure of soaring cost and plummeting profits due to some poor decisions taken by the promoters.

Sachin Iyer gazed at his watch. It showed 10.30 pm. He knew that he would be late today also. He was alone in the five-storied new corporate office of Aalaya Logistics at Thrissur a small city in Kerala. He was rather perplexed to see the heap of files on his table. For the past few days, he and his team had a tiresome work. He was annoyed by the way his uncles were managing business in a thoroughly unprofessional way. He is supposed to present a revival plan next week for the company whose profit is bleeding since 2010. He was aware that the ecosystem is more complex due the surge in competition from Multi National Corporation (MNC). The whole task is a challenge as well as opportunity to prove himself.

Sachin joined Aalaya Logistics as Chief Executive Officer (CEO) two months before. After graduating from a Tier - I Business School in India, he was heading the retail channel operations of a leading MNC logistics provider at Chennai. He was summoned by the Iyer brothers to help them resurrect their business. He belonged to the second generation of the Iyer family, which was running the business for the past 15 years.

*Key words:* Aalaya Logistics, Revival Plan

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**A Modest Start**

The cultural capital of Kerala, Thrissur was always a fertile land for entrepreneurs. It had never disheartened businessmen with intent. Iyer brothers had a modest beginning. Gopal Iyer after returning from Middle - East in 1999 started business as a contract carrier with the lone truck he purchased pooling his savings. The truck was attached to a parcel company for rental and the annual turnover was a meagre Indian Rupees (INR) 5 million. The volume of business multiplied in a span of three years with a surge in turnover to INR 30 million and the number of trucks also increased to five. Gopal Iyer had an uncanny knack of influencing people, which enabled him to get loans at ease from banks. In 2002 Krishna Iyer his hard working younger brother also joined the business. The duo did wonders as the company grew exponentially over a period of eight years. They personally involved in all the operations and decisions of the business which according to them was the core of their success. There was a touch of rule – of – thumb decision making everywhere.

Freight movement in India heavily depends on roads, which account for about 60% of total freight volumes. As per a 2007 McKinsey report on Transforming Nation's Logistics Infrastructure, roads in India account for a higher share of freight traffic compared to other continental sized countries like United States and China. India's reliance to roads is three times more than that of China. The irony is that bulk materials that forms majority of the items transported, can be more economically served by rail and waterways. Road freight traffic which grew at a slower rate than Gross Domestic Product (GDP) prior to 1991, increased at a higher rate subsequently. As per a study by Transport Corporation of India (TCI) the biggest logistics provider in India, the Indian trucking sector contributes about 5% of India's GDP and accounts for almost 60% of the country's freight movements. Various estimates put the market size to be around 4 billion – 6 billion rupees by 2011. Taking cue from the industry, in 2002 Aalaya Logistics scaled up to cargo operations. The offer mix consisted of full truckload, less than truckload and sundry cargoes. They faced competition from the likes of TCI and also from unorganized players. With the existing fleet size, Gopal realized that it is tough to survive. But they opted for a waiting game even though they knew that inaction is not a safe option.

After a gap of two years, Aalaya forayed into express industry in 2004. The express industry caters to multiple industry segments as well as to individual customers by providing time bound logistics services. The customers use express delivery services for shipment of various products, including documents like letters, trade documents, applications, cheque books and bank statements, promotional materials and non-documents like equipment parts, electronic products, spare parts, trade samples and others. While multiple industry segments use express delivery services, certain industry segments like auto components, banking and financial services, Information Technology (IT) components, readymade garments, pharmaceuticals and telecom products are the largest customer segments for the express industry in India. It was a rather ambitious entry into an already crowded market space. The Indian express industry, which had its origin in 1980s, is estimated to have a market size of INR 10,870 crores (about US Dollar 2.2 billion) in 2011-12. As a premium segment, the express industry is small but a significant segment of the logistics.

The express business of the state was controlled by the veteran companies like TCI, GATI, TVS, ABT etc along with courrier giants like Professional, DHL etc. But Iyer brothers never panicked. The launch was extravagant by opening 14 branches in 14 districts of Kerala in a single day. The branches were started in a franchise route. They penetrated the market with innovations such as door delivery, 24-hour service, cash back on delayed delivery etc. They exhibited the freight matrix in all their branches (See Exhibit I). This strategic positioning worked and quickly Aalaya gained an image as "the most reliable provider "among the customers. Within a span of one year, they were able to gain a substantial market share in Kerala. The turnover of the company touched INR 200 million (mn) in 2003. The fleet strength of the company got increased to 70. The employee strength of the company was 240 at that time. The major chunk of the employees was relatives and friends of the founders. Gopal always had the feeling that if we appoint our blood they will be more loyal to the company. In the meantime, Gopal was named as the founder chairman of the group and Krishna became the founder CEO.

The express industry offers an integrated shipment delivery services to its customers. In order to provide visibility of the shipments to the customers they developed a computerized tracking system and a dedicated customer care centre. Since the competition is high, staying relevant in the business costs more. The company took an additional loan of INR 70 mn from three different banks. They recouped around Rs. 10 mn through franchises. The soaring operating expenses (Exhibit II) were irritating them but since it was manageable they neglected it.

Another major expansion was the start of "Radio – taxi" business. Krishna Iyer argued hard with his elder brother before the start. Gopal was on the view that there is no market for a radio – taxi business. Anyway, the younger brother won and Aalaya Logistics started its first radio – taxi office at Thrissur on April 2007. The company purchased 20 Tata Indica cars by its own and out sourced around 30 more on a five-year contract. The company spent around INR 8 mn for purchasing cars and another INR 5 mn for fitting additional gadgets. The company also gave financial assistance to the rental partners in fixing the gadgets. It hired 10 females graduates for attending calls and 30 drivers with a fixed salary of Rs.15, 000/m. But radio – taxi call was risky that too in a Tier II city like Thrissur. The company was aiming at a target that seldom existed. Krishna was optimistic and he did a door – to door canvassing and started taking daily school trips. This helped to take brand Aalaya to every home. Still fleet of 50 taxis was an exorbitant number. So he thought of designing travel packages. "We know that tour operator business is an overcrowded market. India's travel and tourism industry is expected to generate revenue of INR 1,970 billion (US$ 42 billion) in 2010. So we are confident that we have our share in the market and hope we can leverage the brand Aalaya to tackle competition." said a confident Krishna. His gamble was a success partially. Aalaya Logistics was able to register their presence in that business in the subsequent years.

At the end of Financial Year (FY) 2009, Aalaya Logistics touched the INR 500 mn turnover mark as per their auditors. The foundation stone for the five storey corporate house was laid to mark the tenth anniversary. They also announced their entry into the online business mode. The Iyer family celebrated this landmark achievement with their employees in a 5 star hotel with the presence of some celebrities.

**The Downturn**

All the good fortunes for Aalaya started reversing by the fag end of 2010. On a weekend of Nov 2010, Gopal woke up late night to receive a call informing an accident to one of their trucks. On personally visiting the accident spot he came to know that it was an attempted hijack. The assistant of the truck with the help of some employees in the company tried to hijack a truckload of IMF (read Indian Made Foreign Liquor) along with the truck. This eventually led to the accident killing two people and destroying a bus-waiting shed. This was the first incident in one-decade history of business. Even though this is a trivial issue for Aalaya to solve, the incident haunted the brothers a lot.

The following week charted accountants for the company pointed a mismatch in certain accounts and they suspected forged bills. However, Gopal Iyer was not ready to accept as he was confident in his accountant, who was also his brother – in –law. But things became more serious when the manager from South Indian Bank, the prime lender called Krishna and requested to clear the dues pending for the past 8 months. He smelled a rat, put a secret enquiry on the accountant to find him guilty, and eventually was terminated.

The threatening mega fauna was actually waiting. The “radio – taxi” business was cancerous. It was eating away the profits of the company. The company needed a minimum of INR 10 – 15 lacs every month towards salary and fixed expenses. The soaring fuel as well as maintenance expenses added to the worries. Many a time the drivers were paid even without taking a single trip. The 30 contract vehicles are a burden as premature termination is costly. The call centre service was also contributing to raising operating expenses. They started searching for other revenue streams including advertising. They roped in some contracts for ads within the vehicle – on the back of seats, headrests, and even through small TV sets – there were opportunities on the sides and on the roof of the vehicle. Since all were long-term contracts, termination again seemed a liability. The brothers were really in a “Catch 22” situation. However, various market researches predicted a bright future to this industry.

The cargo business also took a downturn. The cost of operations both trip – specific and non – trip specific had sky rocketed (Exhibit III). The mileage of vehicles, the average speed of vehicles, stoppage delay per km and stoppage expenses per tonne-km were areas of concern.

Average trip expenses and freight rates per tonne-km have increased due to inflation (Exhibits IV & V). The much proclaimed cash back scheme was actually increasing the cost of delays of the company. The majority of the trucks has crossed the 5-year cap kept by the company for replacement that also contributed to mileage drop of the vehicle. Adding to woes they have to invest INR 150 mn this fiscal as the vehicle replacement targets missed. The intensified competition coupled with the economic slowdown has made the business less attractive.

The express service had its own limitations. Domestic and international reach is vital for the success. However, with only domestic operations the initial fad disappeared as the revenue generated is not intact with expectations. The absence of air cargo made life tougher in the industry. In fact, more capital is been infused expecting a faster return. The emergence of online portals like Flipkart provides a ray of hope to the company. But time being they are not lucrative. The INR 100 mn extravagant corporate office was also a major contributor to the operating expenses.

The company’s entry into online space is in its infancy. The mounting employee costs were really an area of concern. To strengthen its operations the company recently infused for the first time fresh blood through campus recruitment. Aalaya now have 500 employees in the roll that formed a strong team. The online business had reasonable clicks but reach was limited.

The saddest part is that at the end of FY’11 and FY’12 the turnover of the company showed a steep decline to 42 crores and 34 crores respectively. This forced the founders to think of restructuring the company. As a beginning of the restructuring process the brothers constituted a Board of Directors including some from their family and announced Sachin Iyer as the new CEO.

**Way Ahead**

Sachin found it difficult to crack the nut. He was into a task of shaping the destiny of many families. He knows how difficult it is to sell his ideas to the board of directors. He has to deal with a series of problems from the group concerns. His revival/restructuring plan decides whether Aalaya Logistics live or die.

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*Exhibit I: Freight Matrix of Aalaya Logistics*

| Routes | Time Taken for Delivery |
|---|---|
| **Inside Kerala** | **Same day** |
| **Outside Kerala < 700 km** | **Less than 24 hours** |
| **Outside Kerala < 1500 km** | **Less than 36 hours** |
| **Outside Kerala < 3000 km** | **Less than 48 hours** |

Source: TCI – IIM Study Report, 2011

*Exhibit II: Expenses Including Overheads, Freight Rates and Profit Margins*

| Parameter | Unit | Minimum | Maximum | Average |
|---|---|---|---|---|
| **Trip expenses including overheads** | **Rs./tone-km** | **1.41** | **1.48** | **1.45** |
| **Freight rate** | **Rs./tone-km** | **1.42** | **1.84** | **1.56** |
| **Profit margin** | **%** | **-3.40** | **26.29** | **7.49** |

Source: TCI – IIM Study Report, 2011

*Exhibit III: Components of Truck Operating Costs Trip*

<table>
<tr><td rowspan="2">Truck Operating Costs</td><td>Non- Trip- Specific</td><td>Distance- Specific<br>•Lubricants •Tyres •Spares •General Maintainance/ Overhaul<br><br>Time- Specific<br>•Staff/ Administration •Tax •Insurance •Interest •Depreciation</td></tr>
<tr><td>Trip- Specific</td><td>Distance Specific<br>•Fuel •Roadside Expenses •Driver’s Wage •Maintenance •Brokerage<br><br>Time-Specific<br>•Driver’s Daily Allowance</td></tr>
</table>

Source: TCI – IIM Study Report, 2011

*Exhibit IV: Growth in GDP, Road Freight Volumes and Road Lengths*

| GDP/Freight/Vehicle/Road | Unit | 1950-51 | 2008-09 2010-11 2012-13 | CAGR(%) |
|---|---|---|---|---|
| **GDP** | **USD billion** | **20** | **1727.11 (2010-11)** | **7.71** |
| **Road freight volumes** | **BTKM** | **6** | **1315 (2012-13)** | **9.08** |
| **Vehicles(All types)** | **Million** | **0.306** | **115 (2008-09)** | **10.76** |
| **Vehicles(Goods)** | **Million** | **0.082** | **6.04 (2008-09)** | **7.7** |
| **Road lengths** | **Million km** | **0.4** | **4.24 (2010-11)** | **4.01** |

Source: Ministry of Road Transport and Highways, GOI (http://www.morth.nic.in) World Bank (http://www.worldbank.org)

*Exhibit V: Comparison between the 2008 – 09 and 2011 – 12 Surveys*

| Parameter | Unit | 2008-09 Average | 2011-12 Average |
|---|---|---|---|
| **Journey Time** | **Hours** | **102.18** | **94.47** |
| **Average Speed** | **Km/hour** | **21.73** | **22.71** |
| **Mileage** | **Km/Lt** | **3.6** | **4.06** |
| **No. of stops** | **-** | **25.30** | **30.33** |
| **No. of toll stops** | **-** | **15.47** | **21.13** |
| **Stoppage delay per km** | **Hours/km** | **0.0024** | **0.0028** |
| **Toll delay per km** | **Hours/km** | **0.0012** | **0.0019** |
| **Stoppage expenses** | **Rs./tone-km** | **0.15** | **0.15** |
| **Toll expenses** | **Rs./tone-km** | **0.07** | **0.11** |
| **Trip Expenses** | **Rs./tone-km** | **0.99** | **1.02** |
| **Freight Rate** | **Rs./tone-km** | **1.39** | **1.59** |
| **Contribution margin** | **%** | **40.40** | **53.68** |

Source: TCI – IIM Study Report, 2011

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