OIT-17-E
April 2023

Improving Last-Mile Productivity at Paack

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> It seems like that book is closed. Gorillas acquired for USD 40m cash + 1.16bn shares! I wonder if an alternate universe exists, in which interest rates are still close to zero and Gorillas turns into a legitimate business.
>
> I hope you are doing well. From my side, I just went to the UK again, this time for a couple of months to restructure Paack's operations there.
>
> Regards,
>
> Niklas

Niklas Lachenicht, operations research manager at Paack, had just sent an email to his former business school professor. He had been at Paack for more than two years and had seen the company grow from a start-up to a relatively large-scale last-mile logistics firm.

Since mid-2022, interest rates had been rising, and venture capital had dried up. Paack was fortunate to have secured a series-D investment round of more than €200 million in January 2022, led by SoftBank, which gave the company fuel for further growth. However, as was the case with all venture capital investors, the focus of Paack's investors had also shifted from aggressive growth toward an accelerated path to profitability. For Paack, this meant being financially sustainable with the available capital and translated, among other things, into a hiring freeze, in contrast to hiring around 100 employees per month in the preceding period.

In comparison, other operators in the last-mile logistics business were burning cash fast. Gorillas, a Berlin-based q-commerce operator, promised to deliver any item from a standard assortment of about 1,000 products in less than 10 minutes, charging less than €2 per order. Gorillas had

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This case was prepared by Professors Mihalis G. Markakis and Víctor Martínez de Albéniz. April 2023.
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Last edited: 13/5/24

made headlines by becoming the fastest-growing unicorn start-up in 2021,[1] reaching a valuation of €3 billion.[2] In December 2022, the company was acquired by the Turkish last-mile competitor Getir for a valuation of €1.2 billion, although most of it was in the form of shares.

Fortunately for Paack, its judgment had not been clouded by these mind-boggling valuations, focusing instead on fixing last-mile delivery economics. Considerable work had been conducted to improve driver productivity, the focus of Lachenicht's work, which had a major impact on its profit and loss account (P&L). Lachenicht had been debating with top management about the directions that the company should prioritize in this regard.

E-commerce Logistics

The creation of the World Wide Web in the 1990s allowed companies to start selling through electronic channels, a form of distribution that eventually came to be known as e-commerce. Amazon was founded in 1995, Rakuten in 1997, JD in 1998, and Alibaba in 1999. E-commerce steadily grew during the 2000s and 2010s and received a definitive boost from the 2020 COVID-19 lockdowns around the world, during which physical stores remained closed and consumers started shopping online massively. In 2022, e-commerce accounted for 20% of total retail sales (see Exhibit 1), although metrics varied across measurement methodologies and countries, with higher penetration in China and the United States than in the European Union (see Exhibit 2).

One of the most attractive parts of the e-commerce shopping experience was the convenience of having goods delivered directly at home. This saved time and effort for shoppers, who could avoid visiting stores and expending energy on finding the desired products and getting them back home.

As a result, it was necessary for retailers to build logistics solutions to connect their inventories, located at distribution centers or stores, with consumers. They typically outsourced distribution to third-party logistics (3PL) providers, such as DHL, UPS, or Fedex. However, these companies offered limited capabilities and charged high rates for courier last-mile shipments, with rates of €5–7 per delivery being common.

Large e-commerce retailers, such as Amazon and JD, invested heavily in internal logistics to manage these costs and gain a competitive advantage. For example, the Amazon Prime program offered free deliveries for a flat rate of $99 per year and, as of 2022, served more than 120 million households in the United States. The program not only "locked" customers into shopping on Amazon, but also gave the retailer considerable bargaining power in dealing with sellers within the Amazon marketplace, incentivizing them to join the Fulfillment by Amazon program.[3]

Other retailers opted for lower-investment logistics strategies. Nevertheless, they were all mindful of the high standards expected by consumers when shopping online. Deliveries were expected within the next day or two, in contrast to lead times of weeks at the beginning of the 2010s. Customers also valued the ability to choose delivery slots, the ability to track their deliveries in real

[1] Rahul Raj. "Gorillas Becomes the Fastest Unicorn in Europe: The Berlin-based On-demand Delivery Startup Raises €244M." *Silicon Canals*. Last modified March 25, 2021. https://siliconcanals.com/news/startups/gorillas-raises-244m/

[2] Dan Taylor. "Getir Acquires German Competitor Gorillas in $1.2 Billion Deal." *Tech.eu*. Last modified December 9, 2022. https://tech.eu/2022/12/09/getir-acquires-germany-competitor-gorillas-in-1-2-billion-deal/

[3] Matt Stoller. "Amazon Prime Is an Economy-Distorting Lie." BIG by Matt Stoller | *Substack*. Last modified May 30, 2021. https://mattstoller.substack.com/p/amazon-primes-free-shipping-promise

time, and the free shipping option. Consequently, fulfillment costs steadily rose during that decade. Indicatively, Amazon's fulfillment costs rose from 8% to 14% of net sales between 2010 and 2019.

Even more extreme approaches were adopted by q-commerce retailers, such as Getir and Gorillas (see Exhibit 3), which promised deliveries within 10 minutes for fees as low as €2. Q-commerce attracted large investments from venture capital—for instance, Gorillas raised €1.3 billion in four investment rounds—but many were skeptical about its longer-term prospects.

The last mile—that is, the final leg of the shipment journey from the last logistic stop to the customer's premises—was by far the most inefficient and, thus, most expensive part of fulfillment. Not only was it a very costly element of e-commerce, but it also generated negative externalities for city stakeholders in the form of traffic congestion, pollution, and loss of local retail jobs. Some cities, such as Barcelona, imposed new taxes on delivery companies to mitigate these negative impacts.[4]

History of Paack

In 2015, Xavier Rosales and Fernando Benito traveled to Dubai to participate in Turn8, a start-up accelerator in the United Arab Emirates. There, they presented a project that offered deliveries in less than two hours through a local courier network. Paack was born as a delivery solution that was adaptable to customer needs. The company's headquarters were set up in Barcelona, Spain.

One of Paack's earliest partners was El Corte Inglés, a leading Spanish retail chain mainly operating department stores. Paack enabled it to fulfill online purchases from its brick-and-mortar stores. Time slots selected by the customers were essential. By 2019, Paack had earned the trust of e-commerce giants such as Amazon and Inditex and had expanded from Spain to France, the United Kingdom, and Portugal. COVID-19 restrictions during 2020 fueled Paack's further growth. The company broadened its client base and expanded into Italy. Paack had always been positioned as a fourth-party logistics company. In other words, it provided a marketplace that connected retailers seeking logistics services to a range of logistics companies. Hence, it served e-commerce retailers as customers and used logistics companies as subcontractors (suppliers). Its main operational goal was to be an aggregator of last-mile logistics to achieve economies of scale and subsequent cost reductions.

To avoid various legal and organizational problems, Paack targeted professional logistics companies rather than individuals from the outset. Indeed, companies such as Glovo, Cabify, and Uber had been sued for violating labor laws in many European countries. For example, in 2021, the Spanish "rider law" recognized food delivery workers as employees of delivery platforms rather than independent contractors, implying that platforms should provide them with social security benefits.[5]

[4] Clara Blanchar. "Barcelona Comenzará a Cobrar En Marzo La 'tasa Amazon': La Pagarán Los Grandes Operadores De Reparto Por Aparcar Al Entregar a Domicilio." *El País*. Last modified December 2, 2022. https://elpais.com/espana/catalunya/2022-12-02/barcelona-comenzara-a-cobrar-en-marzo-la-tasa-amazon-la-pagaran-los-grandes-operadores-de-reparto-por-aparcar-al-entregar-a-domicilio.html

[5] Gorka R. Pérez. "Spain Approves Landmark Law Recognizing Food-delivery Riders As Employees." *EL PAÍS English*. Last modified May 12, 2021. https://english.elpais.com/economy_and_business/2021-05-12/spain-approves-landmark-law-recognizing-food-delivery-riders-as-employees.html