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Rising to the Challenge

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Logistics providers must dig deeper into supply chains for savings for shippers as recession cuts freight demand

Companies specializing in third-party logistics were once thought "recession proof" - no matter how bad the economy, shippers would need their services. This recession is testing that assumption and third-party logistics providers.

Shippers are in full survival mode, slashing costs, consolidating freight and changing modes as freight volumes plummet.

That may mean greater outsourcing and more opportunity for 3PLs, but top logistics providers will have to work harder and smarter in 2009. "It's the most challenging year we have ever seen and will probably ever see," says Tony Zasimovich, vice president of international logistics services at APL Logistics.

He says APL Logistics is receiving more queries from current and prospective customers seeking to downsize and cut costs. In particular, retailers are turning to 3PLs for help in clearing out unsold stock.

"We believe that more prospects will reach out to us this year," says Jim Ritchie, president and CEO of YRC Logistics, an arm of YRC Worldwide, the nation's largest LTL trucking group.

But 3PLs will be hard-pressed to do as well as they did last year, when third-party logistics revenue increased by 5.5 percent to $128.7 billion, according to logistics consulting firm Armstrong & Associates. Armstrong predicts a 4.5 percent expansion in 2009.

It's clear that shippers will demand more from their logistics partners in this recession, and lower transportation rates are only the beginning. As companies vigorously try to drive out all non-essential costs, 3PLs report that shippers are suddenly willing to reexamine every supply chain practice and assumption.

"Providing good services will not be good enough in 2009," says Ritchie. 3PLs "will have to create value in a number of different ways."

For example, Zasimovich says APL Logistics plans to reach out to smaller customers, making its supply chain visibility and reporting tools more readily available.

In 2008, YRC Logistics invested $17 million in technology including upgrades to existing systems and new applications such as a tool for providing multiple options for expedited shipments.

To succeed in 2009, 3PLs must ensure their services are directly aligned with client goals and objectives. Reducing inventory carrying costs will be a priority for shippers this year, whether through vendor managed inventory hubs, pool distribution programs, cross-docking or other means, says Ritchie.

"There's more value there than squeezing more pennies out of transportation carriers," he says. "That can free up a lot of capital, which is gold right now."
Companies are bypassing distribution centers and delivering direct to customers, moving deconsolidation work offshore, using more postponement strategies and packaging goods as close to customers as possible. 3PLs must be flexible to help customers implement such changes.

Companies that can't bend may break. As cost pressures increase, many shippers will reexamine their logistics contracts. If they're not satisfied, they'll bring outsourced functions back in-house or change providers.

Third-party providers will be challenged to maintain service levels in 2009 as freight volumes decline across the board, says Ritchie. "Virtually every industry has been impacted from a volume standpoint," he says. "Providers have to face those volume and cost challenges."

The recession has heightened the focus on continuous improvement activities at San Mateo, Calif.-based Menlo Worldwide Logistics, says Gary Kowalski, the company's chief operating officer. "For us that means pressing harder to add more value and increasing our efforts internally around cost containment," he says.

3PLs and shippers will have to probe deeper into the supply chain to uncover hidden value and opportunities.

Kowalski says that they will have to come up with more comprehensive measures than simply reducing carrier rates. "The gain from that isn't as much as if they ask us to look at their overall network and totals costs."

Formerly reluctant shippers are now willing to change modes, look at value-stream mapping and try other new approaches. They're asking 3PLs to apply supply chain management technology tools with greater vigor.

Customers have asked Menlo to help them relocate Asian-based manufacturing to Mexico. "Some companies flocked to low cost countries without understanding that manufacturing is a part of total cost," says Kowalski.

Scalability is one of the key value propositions that 3PLs can offer these days but it's only as good as the extent to which shippers and providers collaborate. The parties must be in synch to effectively control costs when volumes decline and ramp up operations when they recover.

"The true value of a good 3PL is to understand when changes occur and provide excellent service whether volumes go up or down," Kowalski said.

Shippers searching for a good 3PL in the recession should examine the breadth of a potential partner's services, its financial stability and its ability to provide flexibility as market conditions change, says Denis O'Neill, president of North America transportation for Brentwood, Tennessee-based OHL.

It's also vitally important to have a formalized business review process in place so that shipper and 3PL are in synch as conditions change. OHL generally conducts quarterly reviews with customers, O'Neill says.

Transplace, a technology-based 3PL located in Plano, Texas, is using a number of approaches to help clients cope with the recession, says Matthew Menner, the company's senior vice president for sales and alliances. Transplace is working with retailers to streamline transportation and distribution networks and has undertaken transportation sourcing projects to establish lower baseline rates with contract carriers.

There is a strong trend to cross-docking, network rationalization and collaborative transportation management as customers look to leverage soft freight rates. As volumes shrink it has become a shipper's market but it would be self-defeating to squeeze carriers too hard.

"We are mindful of the shift in dynamics and mindful that things will shift back," says Menner. "We have balanced and delicate discussions of give and take with our carrier partners."

Efficient distribution has always been a balancing act between transportation and inventory costs, Menner says. Abrupt strategy shifts, which some companies are being forced to make because of the recession, generally have negative consequences down the road.

"It's usually best to be pragmatic with small ongoing refinements when altering strategies."

There is more freight rate pushback these days from big multinational customers who have the clout to get terms they want, says Jeff Brashares, logistics services group president for Pacer International, an intermodal transportation and logistics provider based in Concord, Calif. All kinds of companies are asking for lower transportation rates and changes in payment terms.

One customer recently informed Pacer that it would be paying its bills within 120 days instead of the original 30-day terms.

"It blew me away," Brashares says. "They said in a nice way that this is how we are paying and we don't care what the contract said."

Brashares plans to push back. "In my opinion you cannot build your business on the backs of your suppliers."

By some estimates there is as much excess transportation capacity in the market today as there has been since 1994, making it easier for companies to change modes. One Pacer customer is in the process of converting all of its highway business to intermodal, choosing savings over speed. "People are willing to wait a few more days and save money," says Brashares.

When truckload capacity was tight, logistics providers emphasized improving service levels by bringing additional assets into play for customers. That's off the table now as shippers focus solely on bottom line savings, says Will O'Shea, chief sales and marketing officer for 3PD Logistics, a Marietta, Georgia-based 3PL that specializes in last-mile delivery.

"If you don't have a value proposition that helps companies reduce costs there is little interest in talking to you," he says.

Clients are taking a more proactive role in pricing, sometimes asking for visibility into the 3PL''s pricing and cost structure to more closely examine management fees, benefits, health insurance and other cost drivers.

"They want to make sure that you are diligent in getting lower costs," says O'Shea.

3PD has the same number of customers as it did before the recession, but volumes are way down. The company has not trimmed its sales and marketing efforts and is aggressively pursuing new business opportunities while being more diligent about reducing its operational costs.

It has consolidated its multiple North American scheduling and routing offices into a single call center in Marietta and is collaborating more closely with customers and other 3PLs.

A few years ago many users of last-mile services sought branded solutions that included uniformed employees and trucks emblazoned with their corporate logos.

Now those companies are willing to commingle goods with their competitors'' freight to gain more efficient routing, employee scheduling and asset utilization.

"Most companies don't have the volume to have dedicated resources," says O'Shea.
In spite of the grim outlook for 2009, 3PLs and shippers need to plan for an eventual recovery, says OHL''s Reilly.

"It is imperative that companies keep their best talent and continue to wisely invest in processes, infrastructure and technology to meet the needs of the marketplace when the economy improves."