

Looking Beyond the “Givens” in Transportation Outsourcing

The most important factor is trust.

Making good business decisions around transportation management outsourcing involves more than just selecting services, defining processes and negotiating pricing. You might be surprised to know that the most important decision-making factor in selecting a provider is not services, systems, staffing or even a savings estimate; it is trust. Here are ways to establish that trust.

First, determine if managed transportation services are right for you.

When shippers consider the merits of outsourcing transportation management, initial conversations usually fall into one of two categories: “top down” or “bottom up.” But regardless of how the conversation begins, it ends with the same points:

1. causes behind currently delivering less than best-practice transportation management and
2. what they should look for in a Managed Service provider.

Top down

A “top down” conversation usually goes something like this: “Since a 3PL is making a margin and we are not, they should always be more expensive. Unless, of course, they are able to spread significant costs (like a systems expenses) over multiple customers. However, we still share similar labor costs, so how can the 3PL really ever be less expensive when they are making a margin and we are not?”



The answer is two-fold. First, whether or not a 3PL will perform a best-practice service less expensively than a shipper really comes down to how complex and investment-intensive the best-practice service is and how well it is sourced. Similarly, if an outsourced service requires significant investment (for example, in planning and execution systems, developing and maintaining carrier connectivity, or strong ongoing capabilities in process design, systems configuration and implementation/upgrade) and you source well enough that the 3PL has to defray some of these investments across other business, then the

difference between the outsourced cost and the optimal internal cost is often not worth the analytical time spent to precisely quantify it. If an outsourced service requires little investment and/or is poorly sourced, then the external cost will likely be more expensive than the optimal internal cost.

Second, the question of whether a best-practice operation can theoretically be delivered less expensively internally or externally is completely moot if the shipper will not, in fact, actually deliver a best-practice operation and maintain it on an ongoing basis. When shippers plan to develop

best-practice transportation management capabilities, they often focus most on systems investment and the cost of additional transportation and IT staff.

These costs are extremely important, but a shipper that only addresses these or other “immediate” causes of their current lack of capabilities, without addressing more fundamental, underlying causes, risks foregoing a decision with a high return because of a mythical option with an even higher return.

Bottom up

A “bottom up” conversation usually goes something like this: “If we had X (often more lead time, volume in an area or on a lane, the “missing” leg in a triangle moves, or a facility in new location, or a certain system), we could be running Y (more IM, TLs, multi-stop TL, pools, dynamic pools, cross-dock, opportunistic cross-dock, zone skipping,

etc.). The savings could be as high as Z, so we really should be outsourcing, right?”

While the ideas behind such business cases are often correct, there are important points most shippers should consider.

1. Good 3PLs are able to provide multi-customer planning with compatible shippers, which can be very important in

generating savings but, most of the time, most of the savings a 3PL generates will be based on stand-alone volumes. **Don’t let a 3PL’s real multi-customer advantages keep you from looking for savings based on your current volumes and footprint, because there are usually some there.**

2. It is easy to over-invest in the precision of a “bottom up” analysis.
 - a. These are complex analyses, and getting a solid answer usually requires modeling and optimization tools and time, which can be costly either in external consulting expense or internal staff time.
 - b. You need to weigh the cost of the analysis against the value of the information it provides.
 - Optimum operational flow answers change (often quickly), so quick actionable analyses may be better than longer, more precise answers.
 - A decision to outsource should really be made on a more enduring basis or standard than the precise, unchanging savings estimate based on current costs and reasonable assumptions.
 - c. Shippers do not avoid analysis costs by forcing 3PLs to do extensive savings estimates in the sales process, as 3PLs must recoup this cost somewhere in their pricing. Again, balancing cost and decision value is key.
3. As with the “top down” conversation, the entire “bottom up” approach can be moot if the detailed savings estimate is based

on shipper behavior that is not going to sustainably occur. If a shipper bases a savings estimate on business process or information changes that need to be undertaken by other parts of the company without really addressing the underlying reasons those changes have not happened to date, they risk developing a precise valuation of a plan that will not happen.

So, why don't more shippers run best-practice operations right now?

Shipping transportation leaders may respond to this question with many answers. They may identify the complexity of leading process change efforts within their companies that would allow opportunities for transportation cost reduction. They may point out the difficulty of getting funding for transportation systems and additional staffing and getting the time and attention of constrained IT resources. These are all real concerns and very valid tactical roadblocks to best-practice transportation management. However, they are rarely the underlying cause.

More serious reasons for not running a best-practice transportation operation tend to revolve around business models and corporate

cultures. Companies do certain “key” things critical to their business model to make money.

Companies should focus significantly more corporate attention on key things driving value in their business model than on

transportation. For most companies, transportation should be a competency, but it does not need to be a core one. Whether these companies are still able to focus enough attention on transportation to drive best-practice operations is often a matter of corporate culture.

Of course, efforts to enable and deliver best-practice transportation management operations have been and can be successful; corporate cultures can be changed. But doing so is not easy and while, for example, a physical network change or a transportation system implementation may be a part of that change, the change will have to be broader than a



network or systems change to be maintained over time. Many companies have made transportation management changes and/or investments and have seen savings, only to fall back to the same levels of performance within a few years.

If transportation or supply chain leadership is not sure that their company is ready or able to adopt a corporate culture in which a best-practice transportation operation can be built and sustained internally, they should procure transportation management. They are likely to find it far easier to source, contract, and measure a managed transportation provider than to deliver this service themselves.



Trusting your managed transportation provider

Two elements of a 3PL's business model in particular should be critical to earning a customer's trust. Real transportation costs should always be visible to the customer so they can be sure that decision making about transportation flows reflect those underlying transportation costs, rather than transportation prices that might be distorted by rate mark-ups. Customers should also maintain direct

Since many of the inputs to the transportation management process, such as volumes-to-be-moved and transportation cost/price levels fluctuate (and sometimes wildly), the most important decision-making criteria is often not a network or routing answer, but trust. Trust that your provider will identify and implement good network or routing answers over time despite the volume and cost/price changes. But this must be earned trust, not blind trust. Fortunately, there are both business model elements and business practices that should help earn your trust.

contractual relationships with carriers for most moves, unless a multi-customer move necessitates that the managed transportation provider should be the contracting party.

Clearly, these are business model elements that are not met by brokers. A managed transportation provider should act as a hired shipper, working on behalf of customers to minimize transportation use and cost, while brokers act as virtual carriers and charge rate mark-up on the loads they buy. Brokers can definitely fill important needs, in particular, identifying and providing capacity during tight markets. However, these are important business model issues that should call into question the use of a broker to provide managed transportation services.

Business practices that are important in

earning shippers' trust include the definition of the services for measurement and contract purposes and some key aspects of pricing. During contracting, a managed service provider, with shipper input, should provide process flow charts that identify all of the steps that the shipper wants performed by an external provider and serve as the basis for Standard Operating Procedures (SOPs). With respect to pricing, important practices include ensuring that pricing at the component level is clear and well understood and aligned with the customer's business.

It is important that pricing is understood on a component basis, because the required services frequently evolve during

solution design and overtime. **A shared understanding about how pricing might change in various situations is critical to building trust and ensuring that trust will survive those changes, should they occur.** One pricing alignment question that frequently arises is whether or not a managed transportation provider should share in the

savings “they” generate. It is recommended that a managed transportation provider be paid a fair market price on the basis of their cost required to provide the agreed services and that savings be one of the metrics that a managed transportation provider is measured by (and hired or fired on the basis of), but that savings “belong” to the shipper.

The value of partnering with a 3PL

The “ownership” statement above is valid and highlights the value of working with a managed transportation provider that provides best-practice services, using a proven business model. This means choosing a company that is part of a broad supply chain consultancy that can evaluate and address issues and opportunities from source to consumption — a professional company that will focus relentlessly on cutting transportation costs and enabling transportation excellence in the context of enterprise excellence. **Ultimately, a shipper has to know that its managed transportation provider is a business partner that they want to be in a long-term relationship with – a partner they can trust.**

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