

How to Create a Winning Outsourced Logistics Strategy

Best Practices for 3PL Strategy and Selection



How to Create Winning Outsourced Logistics Strategy

- ⌘ Making the Case for Using a Logistics Service Provider (3PL/LSP)
- ⌘ Considerations when Evaluating and Selecting a Provider
- ⌘ Best Practices for Creating High-value 3PL Relationships
- ⌘ Case Studies in Logistics Outsourcing Success
- ⌘ Q & A

Making the Case for Using a 3PL: Market Drivers

- ⌘ Outsourcing's "Perfect Storm" increases opportunity for 3PLs
 - Changing growth strategies in the aftermath of downsizing
 - Increased supply chain complexity exacerbated by globalization
 - Executives' vogue status of outsourcing non-core functions

- ⌘ Growth through innovation, revenue, and marketshare

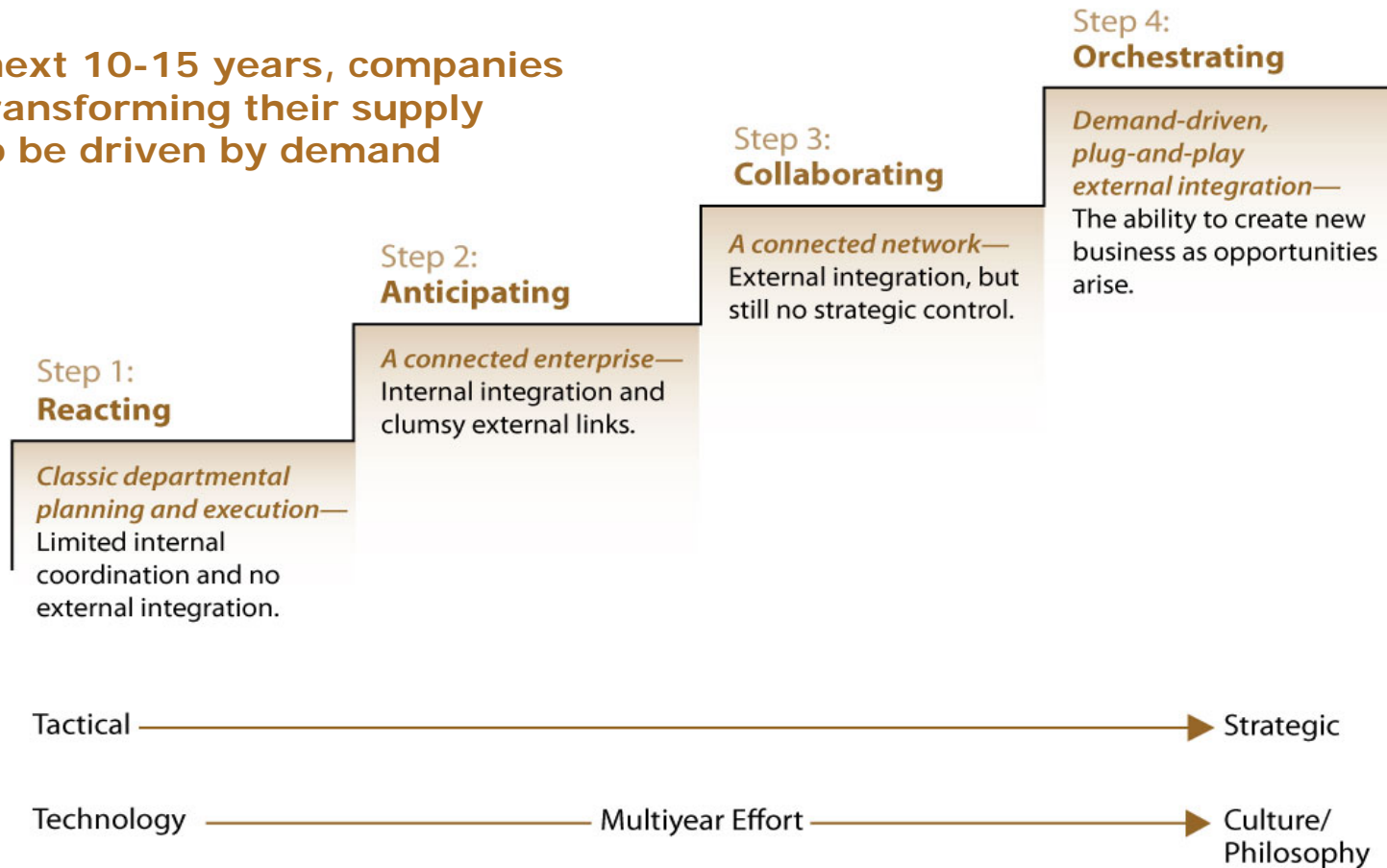
- ⌘ Increased supply chain complexity
 - Becoming demand driven requires adaptive supply networks
 - Globalization of supply chains adds even more complexity

- ⌘ Offshore outsourcing of non-core functions is perceived by management as cost cutting panacea

Making the Case for Using a 3PL: Market Drivers

Figure 1: Four stages of demand-driven maturity

For the next 10-15 years, companies will be transforming their supply chains to be driven by demand



Source: AMR Research, 2007

Making the Case for Using a 3PL

⌘ Corporate drivers (internal)

- Process competencies and specialized supply chain expertise
 - e.g. Support shift to demand-driven supply strategy
 - e.g. Support increasing complex global logistics requirements
 - e.g. Support sophisticated network and inventory optimization strategies
- Redeploy capital assets and shift fixed costs to expense
- Internal supply chain technology deficiencies
- Focus on new product design, development, and launch strategies
- Struggle with product promotion execution and proficiency

Making the Case for Using a 3PL

❖ Corporate drivers (internal)

- Desire to leverage global postponement and late-stage fulfillment
- Difficulty integrating mergers and acquisitions
- Aid growth and new market penetration
 - Help with new product lines or categories
 - Obtain jump-start on geographic opportunity
- Difficulty achieving lower costs, staff productivity, and managing labor
- Leveraging aggregate buying power of provider makes sense
- Flexibility needed to support cyclical variability

Making the Case for Using a 3PL

❖ The essential questions:

- How much does our supply chain / logistics proficiency play a role in my company's competitive position in the industry?
- Have my supply chain / logistics needs surpassed the capabilities of my company (core competency, technologies, infrastructure, etc...)
- Have the dynamics of my supply chain network changed such that our existing assets (facilities, people, physical assets, etc...) are too few? too abundant? obsolete? too costly? to be flexible enough and profitable enough?
- Will our culture allow us to appropriately manage an outside party through the risks and perceptions of turning over control and customer relationships?

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Overview of the Supply Chain Outsourcing Market

⌘ Logistics Outsourcing Companies (3PLs / 4PLs)

- Transportation outsourcing (not for hire transportation carriers per se)
 - e.g. Ryder, Penske, Menlo, Transplace
- Warehousing – public, contract, bonded, cold storage, etc...
 - e.g. Exel, EGL Global, UTi Logistics, Weber Distribution, etc...
- Freight forwarders and global logistics providers
 - e.g. APL Logistics, Kuehne+Nagel, NYK Logistics, Panalpina, etc...
- Logistics services divisions of carriers or companies
 - e.g. FedEx Logistics, Amazon Logistics, Schneider Logistics, etc...

Overview of the Supply Chain Outsourcing Market

- ❖ Contract Manufacturing and SC Outsourcing Companies
 - Contract Manufacturers
 - e.g. Jabil, Flextronics, Elcoteq, Sanmina, Plexus
 - Postponement and Product Completion Companies
 - e.g. RR Donnelly GT, ModusLink, Arvato, XpedX
 - Fulfillment Houses – internet, catalog, and TV fulfillment
 - e.g. Fosdick, Innotrac, IFS, Fulfillment America, etc...
 - Outsourcers of Packaging, VMI, Network Design, Inventory Optimization, etc...
 - e.g. UPS Professional Services, etc...
 - On-demand Software Providers (some offer associated managed services)
 - e.g. Lean Logistics, GT Nexus, JP Morgan Chase Vastera

Overview of the 3PL Market

⌘ According to CSCMP

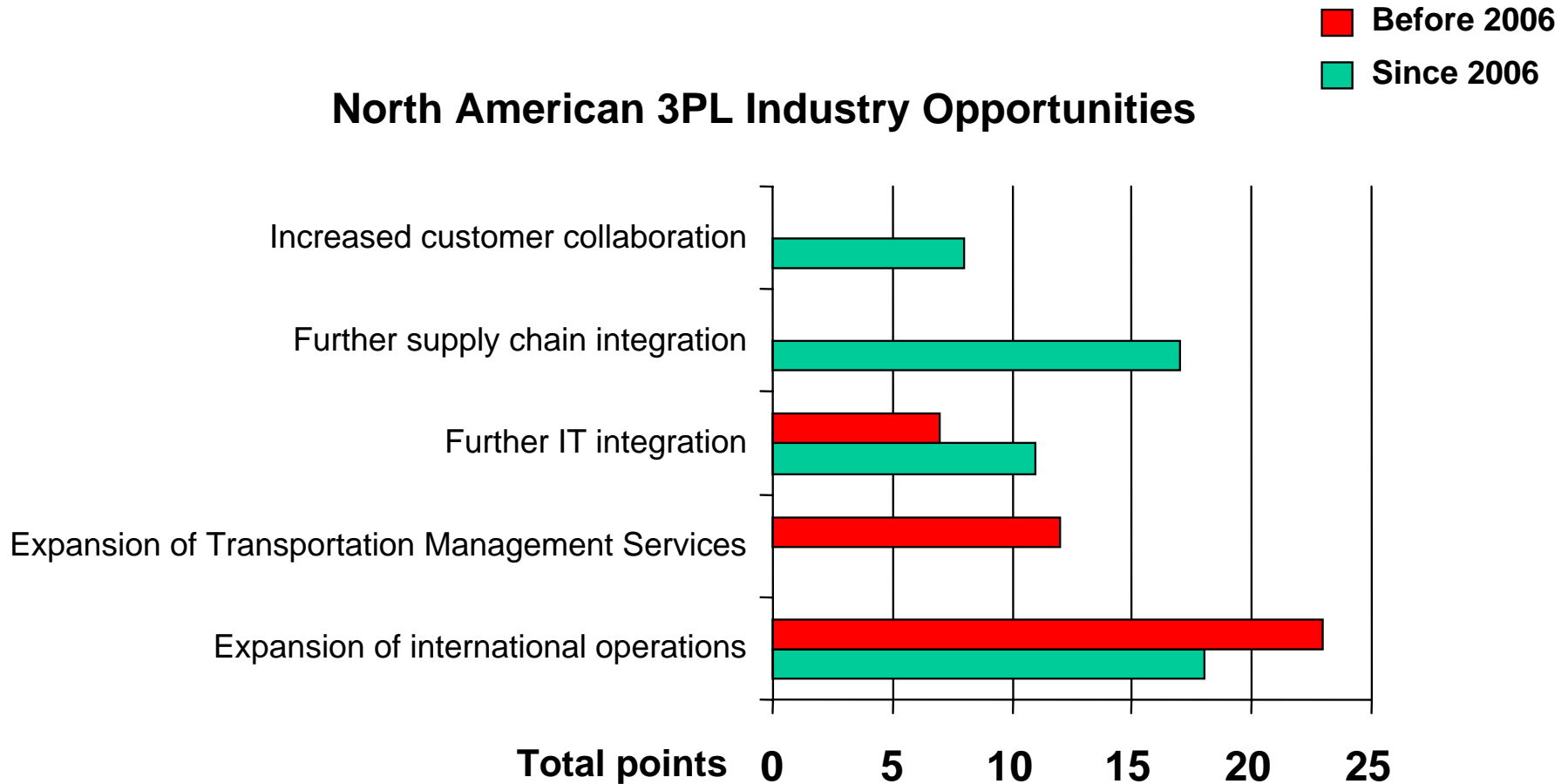
- Global market share for logistics services: \$1,140 B
- The core logistics sectors in North America – warehousing, transportation management, air/ocean freight forwarding – are growing between 15 – 25% annually
- North American usage dissected further:
 - 83% of companies outsource transportation
 - 74% outsource warehousing
 - 71% outsource customs clearance and brokerage
 - 55% outsource freight-forwarding functions
 - 10% outsource order fulfillment and customer service

⌘ Even still, major issues do exist

- 51% of companies report 3PLs are not meeting service commitments
- Only 35% are satisfied with their 3PL's IT capabilities

3PL Industry CEOs: Most Important Opportunities

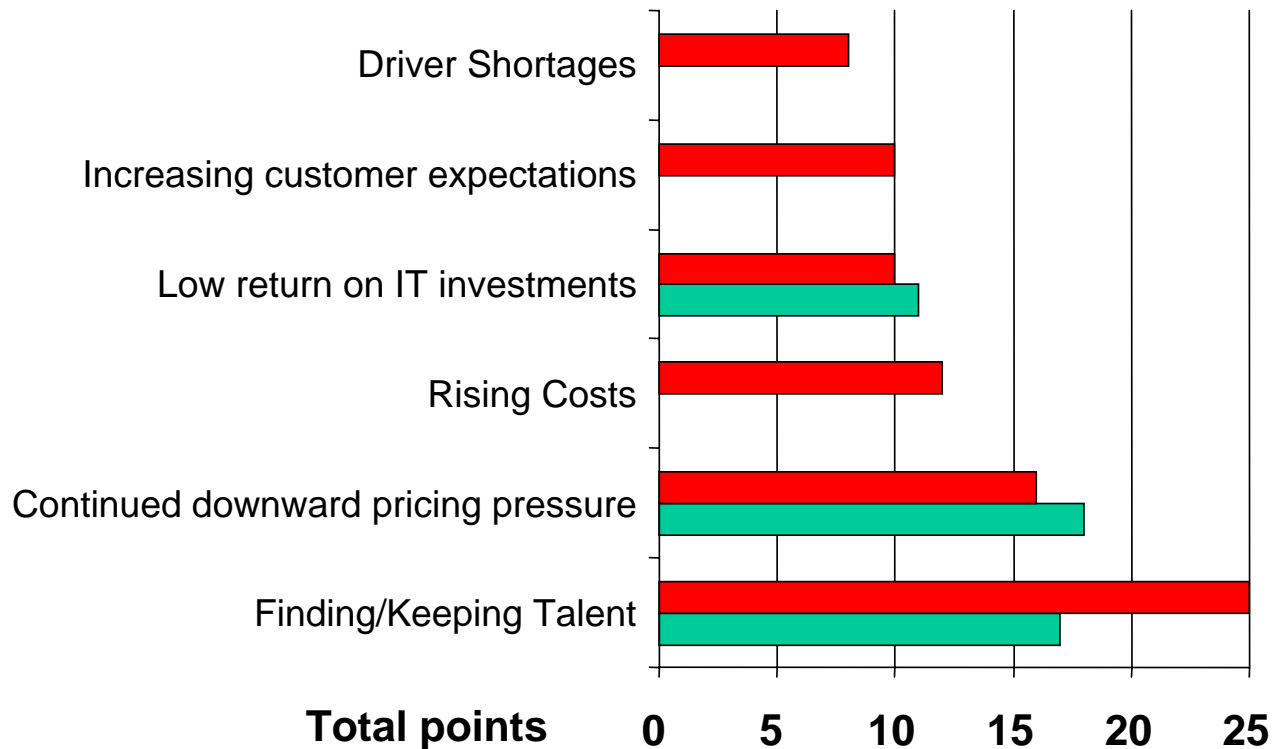
North American 3PL Industry Opportunities



3PL Industry CEOs: Most Difficult Challenges

■ Before 2006
■ Since 2006

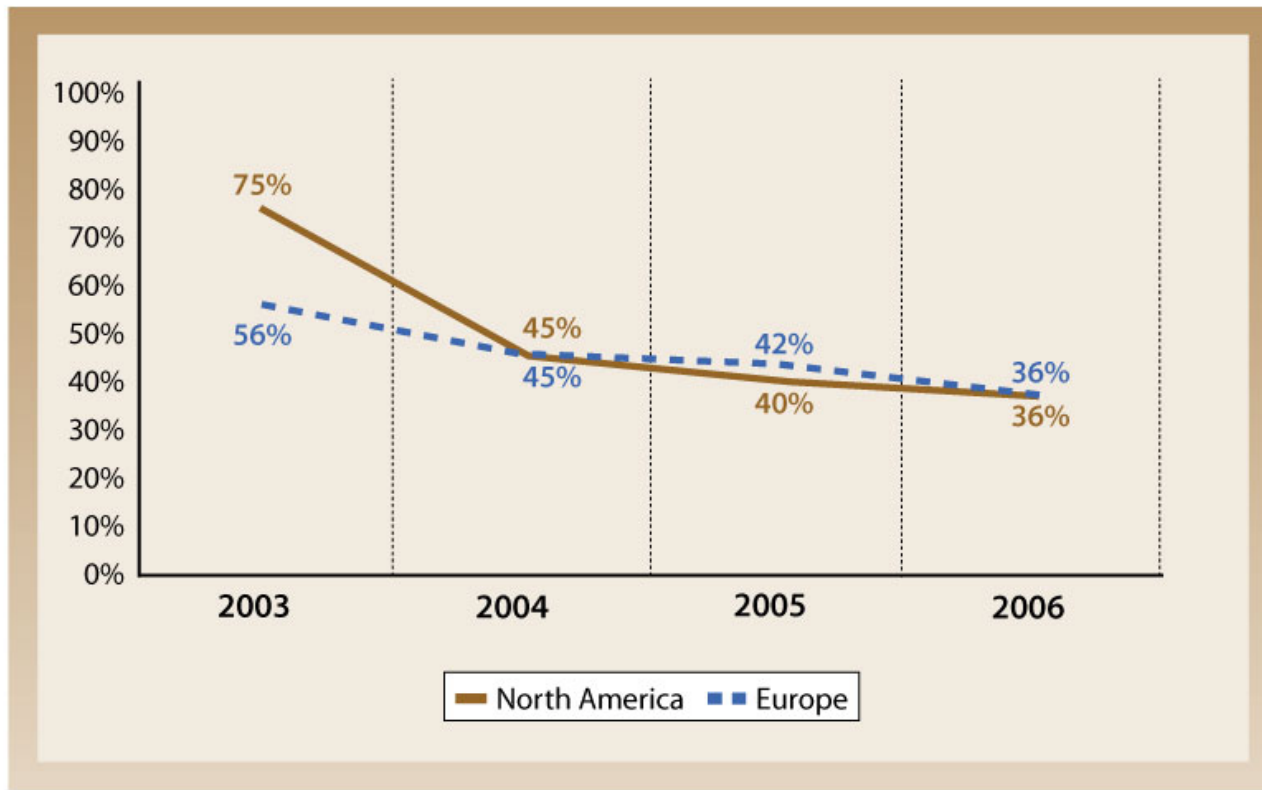
North American 3PL Industry Challenges



3PL Market Considerations: Technology Deficiency in LSPs

As information requirements have increased in importance over the last several years, dissatisfaction rate with 3PL's IT capabilities has risen

Figure 2: Declining satisfaction levels for LSP's technology capabilities



Source: Capgemini/Georgia Tech Study

Overview of the Supply Chain Outsourcing Market

- ❖ The 3PL industry in North America is undergoing a major transition. The combination of high growth and high fragmentation in North America makes the logistics industry ripe for consolidation.
 - A growing economy combined with the “market drivers” supports a broad range of successful outsourcing companies that become expansion-minded buyers
 - High fragmentation translates into an abundance of small acquisition opportunities for larger, cash-rich companies.

- ❖ Private Equity’s toes are definitely in the water for 3PL opportunities
 - Platform companies for aggregation – to sell or go public
 - Equity arbitrage using a roll-up acquisition strategy

- ❖ As the 3PL market matures, businesses and investors that have come to expect growth of more than 20% are likely to need to augment their organic growth with acquisitions in and out of the Americas
 - To grow customers and top-line revenues
 - To expand their service offerings
 - To provide broader geographic coverage for their customers

Key Considerations when Selecting 3PLs

- ⌘ Develop the appropriate outsourcing strategy in advance
 - Clearly define the scope of WHAT is to be outsourced
- ⌘ Clearly define your requirements and service level expectations
- ⌘ Use a professional and standard provider identification and selection process
- ⌘ Keenly evaluate the providers capabilities against you requirements
 - Remember 3PL sales reps believe in “Field of Dreams”
 - Use site-visits and references to verify sales rhetoric
- ⌘ Evaluate information technology infrastructure critically
 - Use references and site visits to ensure that technology capabilities presented are actually in use

Key Considerations when Selecting 3PLs

- ⌘ Compare pricing competitively – be sure to evaluate price in the context of risk of service failure and reliability
 - The lowest up-front price isn't always the best choice
- ⌘ Develop a contract with service levels that represent your expectations but include optional incentives for the provider to exceed expectations
- ⌘ Establish and articulate clear policies and procedures
- ⌘ Identify potential friction points and pre-design solutions for avoidance or effective handling

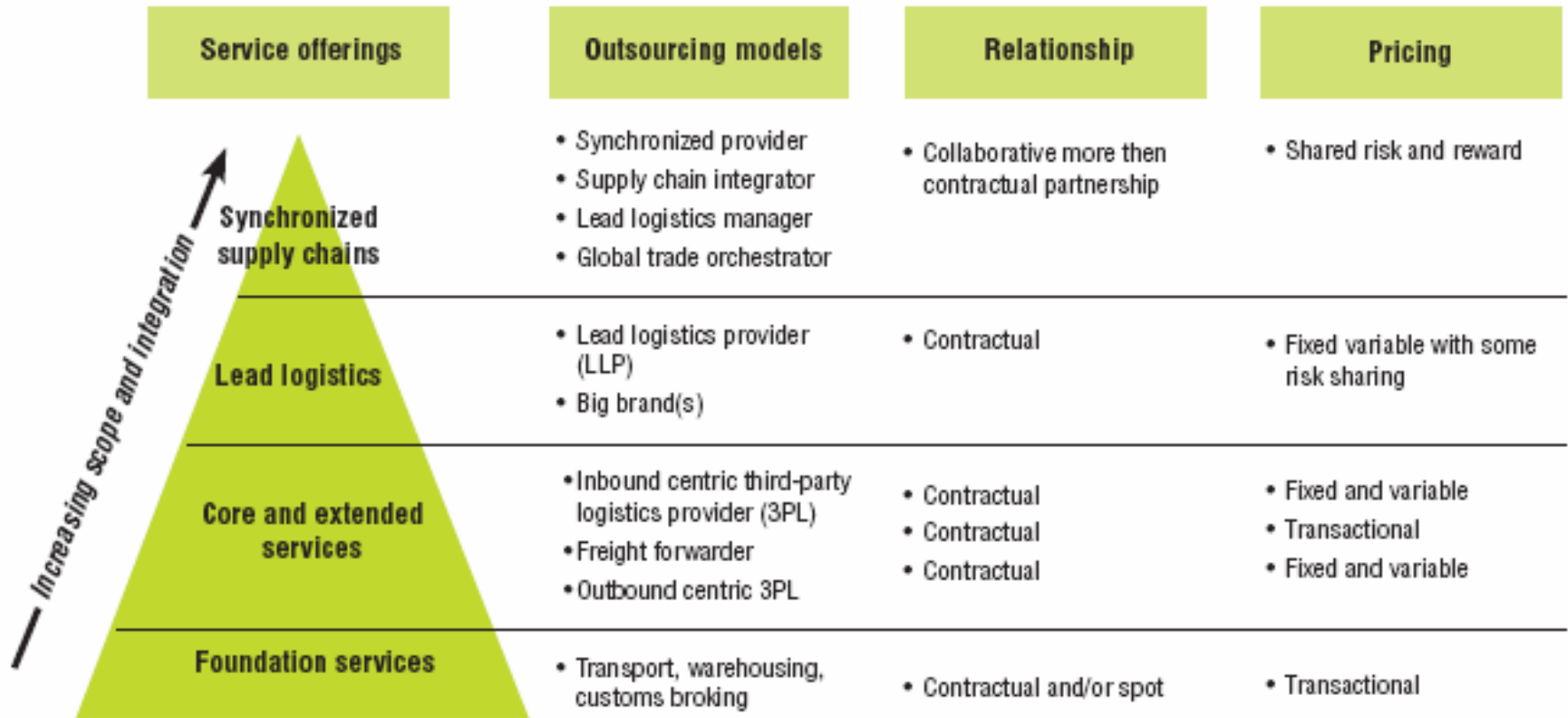
Key Considerations when Selecting 3PLs

- ⌘ Set open and effective communication mechanisms with your logistics partner
- ⌘ Set up KPIs and systems to measure performance and communicate results frequently
- ⌘ Involve providers in continuous improvement processes – they typically know the root cause of faulty processes and have good suggestions for corrective action
- ⌘ Be a good partner – success is mutually advantageous

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Outsourcing Relationship Maturity Model



Outsourcing Agreements and SLAs

- ⌘ Structural as to define the relationship and the overall interaction of the 3PL with the customer
 - Flexibility for change
 - Incentives for continuous improvement
 - Culture and process for problem identification and resolution

- ⌘ Tactical measurements of execution – SLA
 - Key KPIs to be measured and reported on
 - Frequency
 - Culture and process for monitoring and resolution

Potential Obstacles to Managing the Outsourced Relationship

- ⌘ Pricing and service levels rarely contain mechanism for continuous improvement
- ⌘ Differences in buyer and supplier cultures cause misunderstanding and distrust
- ⌘ Outsourcing contracts are based on key assumptions regarding technologies, business conditions, processes, personnel, etc...
These assumptions often change post relationship – most contracts don't include provisions for changes in assumptions
- ⌘ Once the contract is in force, both parties tend to suboptimize in an attempt to better their own position at the expense of the other

Potential Obstacles to Managing the Outsourced Relationship

- ⌘ The time and attention required to manage an outsourcing relationship is often not fully understood
- ⌘ Lack of management oversight is usually the result of two factors:
 - The team that negotiated the contract often does not stay engaged in contract management.
 - A new team that may or may not understand the contract's intentions is given responsibility for managing the relationship.
- ⌘ If suppliers operate in a priority vacuum, service levels tend to deteriorate because the supplier's agenda is not in sync with the buyer's business objectives
- ⌘ If employees with knowledge of the pre-outsourcing process are no longer involved, problems frequently arise post relationship

Sample Communication Mechanisms and Frequencies

- ⌘ Periodic open communication between senior management of both firms
- ⌘ Monthly conference calls between customer service personnel of the two companies
- ⌘ Annual meetings with all logistics providers are invited, client outlines its plans and providers exchange information and solutions
- ⌘ Daily telephone conversations between operations personnel
- ⌘ Performance evaluations using a monthly report cards
- ⌘ Provider participation in continuous improvement planning with client
- ⌘ Client visits provider to discuss operational issues

Communication is Key

⌘ Rules for better communication

- Approach all problems openly with the responsible party. Do not operate with a hidden agenda.
- Treat the other party as you would like to be treated were the roles reversed.
- Do not become emotional. These are business issues, not personal.
- Make sure you have all the facts before confronting.
- Do not exaggerate or embellish this only complicates the resolution and causes harm to a relationship.
- Give the other party reasonable time to respond.
- Develop a plan for preventing a recurrence when solving the problem.
- Share the problem and its method of resolution with others.

Measurements and KPIs

- ❖ *Warehouse operations* usually are evaluated by personal visits and evaluation can be quite detailed. Ordinarily, there will be a monthly inspection with a more thorough audit conducted annually
- ❖ *Productivity* can be measured in different ways, but most firms will want to measure some form of productivity per person-hour. This can be orders, line items, cases, unit loads, or any other unit of measurement that is important to the user firm.
- ❖ *Order cycle time* is simply the time elapsed between the time an order is received and the time it leaves the dock. In a highly sophisticated order fulfillment operation, this time will be measured in hours; in other more relaxed environments, in days.
- ❖ *On-time performance* will be a measurement of either on-time shipping or delivery, or both.
- ❖ *Perfect order rate*, determines the number of orders that were shipped complete as ordered, without any back order.
- ❖ *Inventory variations* can be determined by calculating the differences between physical and book counts. In many situations, physical count is required to match both client and provider book inventories.

Motivation and Reward

- ⌘ Good performance is often taken for granted
- ⌘ Report cards measure against established performance benchmarks
- ⌘ Companies make use of various award programs
 - “Provider of the month”
 - Annual “Excellence in Logistics”
 - Cash awards

Case Studies in Logistics Outsourcing Success

Andrew Breckenridge



\$1.5bn Footwear Manufacturer and Distributor

⌘ Key Business Challenges

- Dissatisfaction with existing 3PL provider around price, service and business risk
- Rapidly expanding multi-channel distribution requirement, growing at 30% per annum

⌘ The Process

- Using FORTE's standard methodology, tailored to fit the client's needs, key business drivers and critical success factors were identified
- Potential 3PL providers were aligned with client in terms of both quantitative and qualitative needs with capabilities linked to critical success factors
- Integration of capabilities and expectations through SLA negotiation
- Development of detailed transition plan

⌘ The Results

- With the new 3PL relationship, dramatically improved service (on time shipment, fill rate and inventory accuracy) and risk profile but financially, cost neutral
- Alignment of business cultures and "way of doing business"
- SLA agreement detailing both soft and hard expectations
- Seamless transition to new relationship



Questions

- ⌘ Greg Aimi
- ⌘ Andrew Breckenridge