Collaborative Outsourcing®

Preparing for a Successful Logistics Outsource

WHITE PAPER

C.H. ROBINSON WORLDWIDE, INC.

In brief

Many companies are responding to increased global competition and challenging economic conditions by outsourcing their logistics. The shipper's level of preparation before outsourcing and the role they play after the strategy begins are crucial to the success of the engagement. This white paper outlines the steps and considerations that need to be addressed by the shipper in order to achieve a high level of success through logistics outsourcing.

Contents

The concept of outsourcing various logistics management tasks to a third party is not new. In recent decades, enterprises realized third-party providers could spread operating costs for specialized talent and technology over multiple client organizations.

Equal parts costs savings and value proposition

Cost reduction was the primary (and often solitary) objective of logistics outsourcing relationships from the 1960s through the 1990s. Shippers could take advantage of the way third party suppliers could measurably reduce their operating expenses by spreading the costs for talent and technology across many companies.

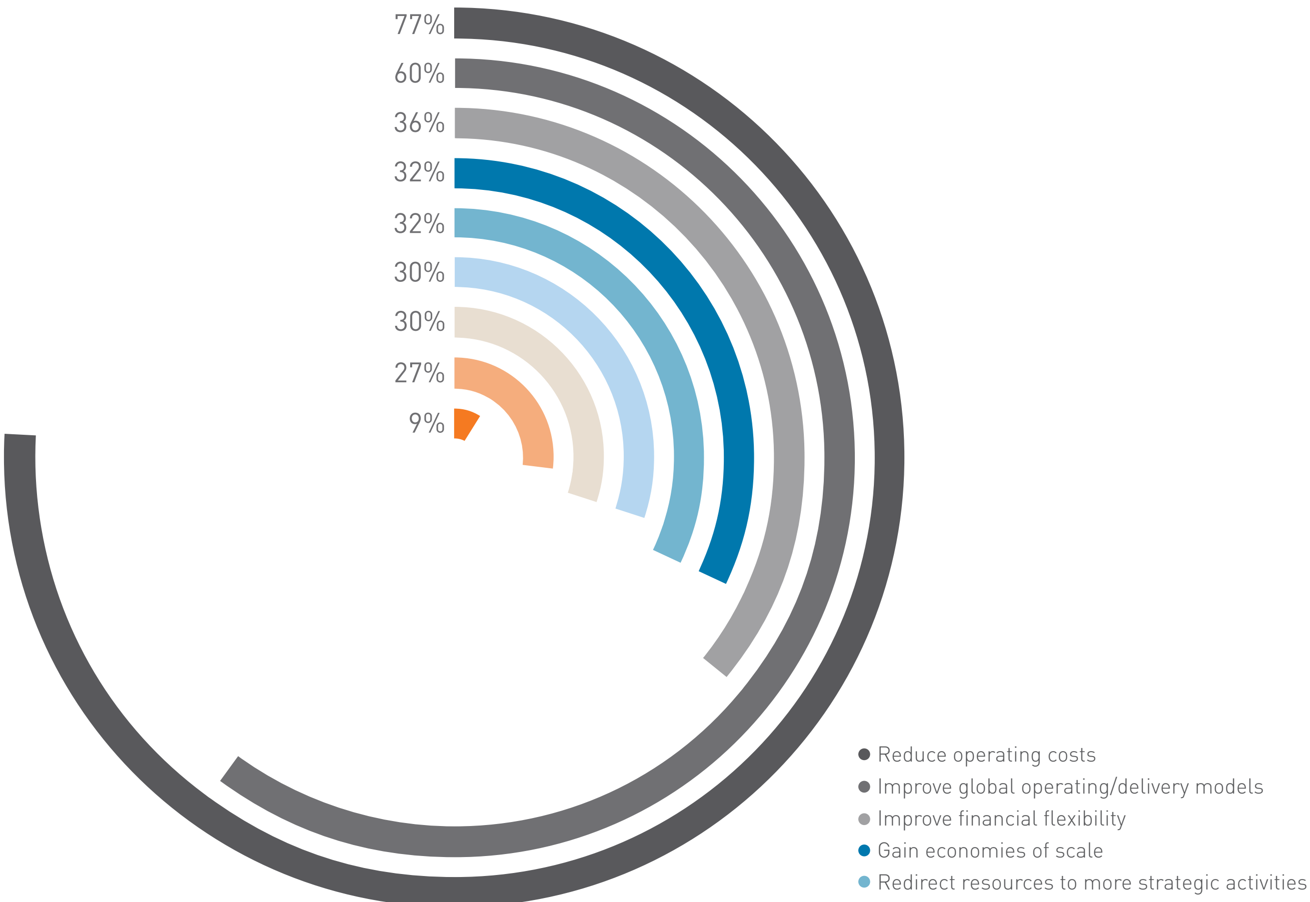
Since then, two macro-trends have converged to change the way companies view logistics outsourcing and their supply chains in general. Fierce global competition and challenging economic times have created a sense of urgency in enterprises of all sizes. Radical cost reduction has become a constant driver, even in the most successful organizations. However, while companies move to cut spending and reduce both headcount and infrastructure, they are looking for new ways to improve service levels to existing customers and efficiently reach new markets.

In fact, a leading industry analyst wrote, "Supply chain outsourcing has undergone a paradigm shift from a cost center to a revenue generating opportunity. It has leveraged logistics to improve service levels to customers, accelerate the speed of launching new products and stimulate market penetration."[1]

1 Cabodi, Cecelia. "Foreseeing Fourth Party Logistics Growth." Material Handling & Logistics. March 1, 2004.

This shift from pure cost cutting to a joint strategy of savings and revenue generation is either the result of, or the impetus for, a successful logistics outsource. Shippers integrate external resources—both human talent and transportation management technology—into their existing transportation or logistics groups. By adding these resources, shippers are maintaining strategic control and visibility, and adding resources, without fixed costs or new capital investment.

TOP DRIVERS FOR OUTSOURCING—GLOBAL BASIS[2]



2 Price Waterhouse Coopers. "Outsourcing comes of age: The rise of collaborative partnering." 2007

The fundamental difference between “subtractive” and “additive” outsourcing

Traditional outsourcing models might be described as subtractive. That is, the client organization packages up work that is to be done and passes it on to an outside resource. For the client to achieve successful outcomes with this model of outsourcing, their organization must clearly define tasks. The better the work is defined, the better able the provider will be to perform it. In this “activity based” model, success is a linear “yes/no” measurement with a relatively finite upside (i.e., cost savings).

In an additive outsourcing model, however, success depends on more than immediate cost savings. The client intends to integrate specialized talent and transportation technology into its existing transportation organization. The success of this model clearly includes both immediate and long-term cost savings, which are typically defined by a savings plan. However, because the talent and technology is integrated into the enterprise, their effects radiate further into the enterprise and farther down the value chain. The level of success in this case is not “activity based” as it is in the subtractive outsourcing model, but rather “outcome based.”

Key performance indicators (KPIs) are established for criteria throughout the supply chain. Typical KPIs range from efficiency gains in the manufacturing process, to time-to-market in new geographies, to ultimate customer satisfaction levels. Multiple departments within the enterprise will realize the effects of outcome-based logistics outsourcing. Therefore, those various disciplines must be included in (1) the definition of KPIs related to the outsource strategy, and (2) the preparations to ensure effective integration of the external talent and technology.

APPROACHES TO OUTSOURCE MODELS

Traditional “Subtractive” Outsourcing	Collaborative Outsourcing®
Define and Package Tasks	Prepare Enterprise for Integration
Pass Tasks on to Provider	Determine KPIs for Supply Chain
Measure Activity Levels	Monitor Performance Against All KPIs
Monitor Cost Reductions	Ongoing Cross-Functional Optimization

5 Steps to prepare for a successful logistics outsource

Whether you ship products locally or worldwide, globalization is dramatically changing your competitive landscape. In 1950, global trade totaled $50 billion USD; by 2015, it will likely exceed $24 trillion (see Figure 1). This means more competitors and increased price pressures, especially on commoditized offerings. Globalization opens access to new markets with millions of businesses and billions of consumers. Clearly, in a more global world, success requires both aspects of logistics outsourcing—cost reduction and value creation.

FIGURE 1 GLOBALIZATION GAINS MOMENTUM

Volume of Global Trade

Source: World Trade Organization, 2011.

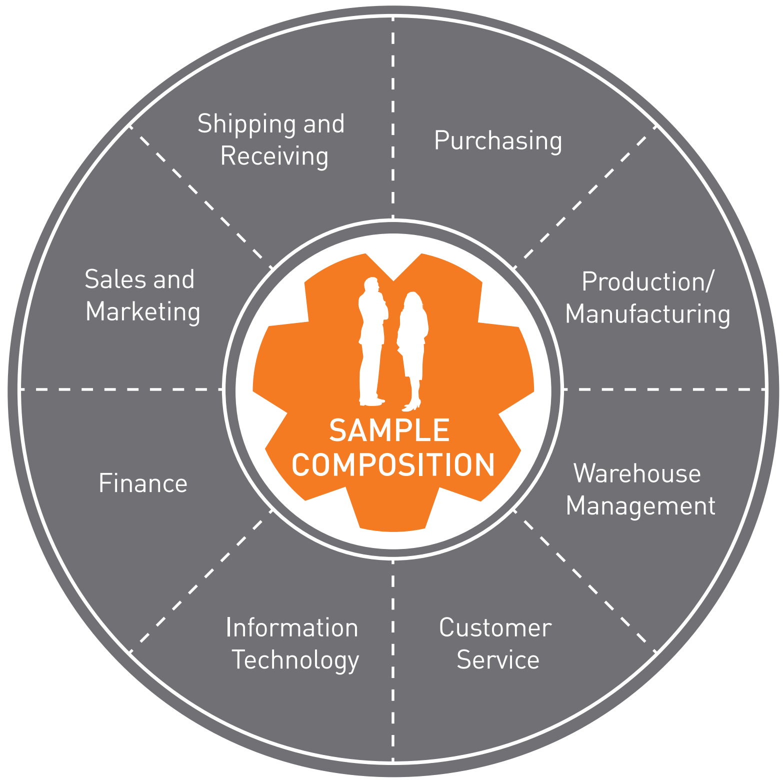
Making a successful transition to a global company—or even to a company that is well suited to compete regionally in an increasingly global economy—requires true transformation. But with increased competition and challenging economic conditions, transformation strategies should not require either significant capital investment or protracted deployments. This makes outsourcing—with its low- or no-cost integration of talent and technology—an appealing transformational strategy for shippers of all sizes.

A logistics outsource engagement depends on any number of factors; some are within the control of the client organization, and some are not. Best practice compilation from outsource engagements worldwide have helped identify five steps to preparing for a successful, long-term outcome.

1. Selectively Form a Cross-Functional Team

While every organization is somewhat unique, an effective cross-functional team will include representatives from multiple disciplines and departments across the enterprise. Companies with the best success tend to choose team members based on strategic inclination, as opposed to title or seniority. Since the potential impact on the entire supply chain is not always clear in the beginning, participants should have a strong strategic vision.

CROSS FUNCTIONAL TEAM



Contributions from each of these functional areas are critical for three reasons. First, understanding your "current state" processes, costs, and customer service implications requires a 360-degree view of your supply chain. Input from each department is vital. Second, your cross-functional team members will need a first-hand understanding of your supply chain strategy so they can implement their portion of the plan and measure outcomes in their specific areas. And third, accurately quantifying the impact of your outsource strategy will require continuous feedback measurement and alignment of KPIs, such as lead times, manufacturing costs, and customer service levels.

Improvements made to the transportation process will have a tremendous impact on both brand perception and customer service levels. In the cross-functional team, include colleagues who are responsible for managing the company's brand and orchestrating the customer experience.

2. Measure Outcomes, Not Activity

Traditional subtractive outsourcing models tend to be solely activity based, with no regard for how the activity is performed or executed. Contracts often are arranged with the intended goal of bringing the greatest savings to the client. Upon closer examination, however, because these agreements measure providers for conducting activities, not how they conduct those activities, they can become the sole focus of the engagement—from the provider's perspective, of course.

Instead, look for outsources that are outcome based. Rather than simply measuring the provider for activities—such as the number of shipments executed, quantities of pallets moved, or total miles travelled—measure the outsource provider on how they perform the activity against KPIs that improve productivity and increase efficiencies. Do your due diligence to realize that, while outsource models and solutions may look similar on the surface, the level and quality of the activities performed will have an impact on other parts of the organization beyond transportation. This includes both upstream and downstream in your supply chain and from manufacturing to sales to service.

3. Grade Your Current Technology Against Emerging Needs

There are three simple measures you can use to evaluate your existing transportation technology. First, does your current technology provide you with the real-time dashboards or reporting capabilities you need to monitor the KPIs you select? Second, are you willing and able to provide accurate data to your provider? Third, does your current technology offer the scalability, accessibility, and low deployment and maintenance costs of cloud computing?

Be prepared to discuss your desired metrics and future expansion plans to know what will be needed for smooth integration with the provider. Also understand how much planning time and internal execution your IT group will need to provide before the outsource engagement, as the level of necessary work varies by outsource model. All of these considerations are essential to evaluating transportation management systems (TMS) and other technologies offered by potential outsource providers.

> "Activities such as forecasting and inventory planning have been less subject to outsourcing trends. However…specialist outsiders are enhancing their abilities in these areas at a faster rate than most in-house teams. Many of those outsiders also are reducing the fees they charge to clients, to the point where the service providers' rates are equal to or even less expensive than what it costs to maintain in-house teams."[3]
>
> —Carlos A. Alvarenga and Pancho Malmierca, Accenture

3 Alvarenga, Carlos A., and Pancho Malmierca. "The Case or Oursourcing Supply Chain Management." Accenture, 2011.

This is a particularly important consideration for companies that rely on IT staff to lead the innovation process. Deploying an established TMS as a utility-based application greatly reduces the potential workload for already stretched IT staff. Instead of deploying, supporting, and updating TMS software, time can be spent on initiatives related to innovation and the enterprise's core business.

"The critical question isn't whether cloud computing will become a fundamental technology in the next decade. It is how extensively companies will profit from the capabilities it offers. If your organization has not yet started the journey to the cloud, now may be the time to start drawing your roadmap."[4]

—Jonathan Wright, Managing Director, Accenture Asian Supply Chain Practice

4. Carefully Choose What to Outsource and What to Retain

Retained strategic control remains a core concept of a logistics outsource. As stated earlier, in a traditional outsource relationship, the enterprise typically turns an entire process or department to a third party, which manages "activity." Successful outsources, however, can also bring talent and technology inside the walls of the enterprise, which allows the organization to maintain strategic control of its transportation network. Presumably, the provider's cloud computing model will allow the internal team to monitor real-time dashboards and receive customized reports based on KPIs.

Given this scenario, determine which processes the enterprise will continue performing and which ones will be outsourced. For example, do you want to manage shipments and route optimization, mode selection, and carrier payment, or will you have your outsource provider manage them? Similar decisions will likely be required for rate negotiations, contract management, yard and dock management, track and trace, claims management, and service level monitoring.

5. Build an Informed Risk Profile

There are a number of risk factors shippers inherently have as transportation and logistics are executed. With these risks come varying levels of associated costs as not all risk is equal—and not all providers have the ability to fulfill all obligations related to risk. How a shipper assesses these risks can help determine the impact of a logistics outsource; this is a key component of comparing multiple outsource providers. By just assuming risk is passed along through an outsource relationship, shippers should understand that not every organization takes on risk the same way—and the cost of assuming, or passing along, these risk factors could make a difference in the outsource relationship you have with your selected provider.

4 Wright, Jonathan. "An introduction to cloud computing in supply chain management." Supply Chain Asia, February 24, 2011.

- **Operational Risk.** This type of risk applies to any aspect of the supply chain or the enterprise as a whole. While it seems outsourcing presents a new set of exposures in the supply chain, the reality is that new risks are quite minimal. These are the categories of general operational risk that can be associated with an outsource engagement.

Operational Concern	Example	Risk Potential
External Disruption	Weather events, political unrest, supplier failure	Equal. Events are the same for internal or external teams.
Lack of Necessary Skills	Awareness of taxes, tariffs, currencies, languages, etc. in global transportation	Equal. Potential for lack of training is the same for internal or external teams.
Brand Reputation	Transportation execution	Equal. Potential to lose clients with poor performance is the same for internal and external teams.
System Failure	Management system crash, incomplete/erroneous data	Typically less with a provider because of cloud computing models.
Process Failure	Poor or outdated business processes	Equal. Although this varies by provider and application of accepted best practices.
Lack of Company Knowledge	Specific information about manufacturing processes, distribution centers, etc.	This can be greater with providers because they depend on knowledge transfer from client.

- **Financial/Legal Risk.** Understanding these risks and evaluating them against the capabilities of internal and external teams represents an important step toward risk mitigation. In the case of global trade or simple expansion into geographic markets, shippers must evaluate competencies in rate/market risk and in global shipping, such as duties, taxes, and customs compliance.

  Shippers must also decide if the providers they work with have the financial wherewithal to stand behind their contractual obligations in carrier payment, cargo claim liability, and carrier compliance (safety and insurance). Signing a contract under the pretense of false protection could have major implications for the shipper down the road. Understanding the risks associated with owning carrier contracts and managing carrier relationships, either by the shipper or outsource provider, includes varying levels of cost and relationship management considerations, as well.

- **Brand Reputation/Service Risk.** Assigning all or part of your transportation operations to an outsource provider poses potential risk for the perception of your brand. Transportation is one of the most frequent and tangible touchpoints for channel partners and end users, and is measured through metrics such as load acceptance, scheduling, and on time performance. The outsource relationship has the potential to greatly enhance the brand experience—or rapidly deteriorate it. To make a risked based decision, identify an outsource provider with technologies, processes, and best practices that measurably enhance the strength of your brand and improve the customer experience.

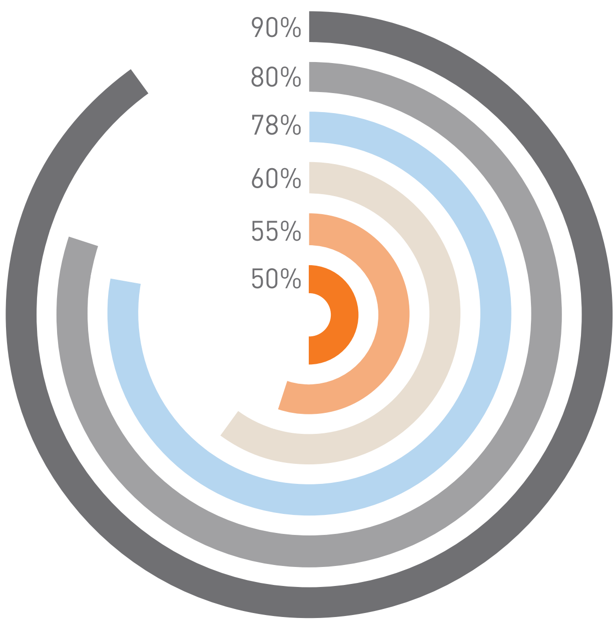
Collaborative thinking

The impact of logistics outsourcing on innovation

Success in increasingly competitive and global markets requires cost control and, perhaps more important, continuous innovation. An outsource engagement typically can accelerate innovation within the supply chain in several ways.

1. Collaboration is paramount. Both companies need to communicate, exchange accurate data, develop a high level of trust, commit to a long-term relationship, and be strategically aligned in order to achieve a high level of trust.
2. The formation of a cross-functional team tends to pull people out of corporate silos and into problem solving or innovation discussions.
3. The integration of outside talent and technology arms the enterprise with new innovation tools.
4. Established outsource providers tend to accumulate a wealth of best practices from other client engagements and introduce them into weekly, monthly, or quarterly innovation discussions.

INNOVATION GOALS



- Improve service quality
- Reduce costs
- Increase speed to market
- Open and develop new markets
- Comply with laws and regulatory standards
- Reduce/minimize environmental impact

Source: KPMG: Driving Innovation Through Outsourcing, 2011.

About us

Founded in 1905, C.H. Robinson Worldwide, Inc. is one of the world's largest third party logistics companies, providing global freight services and the world's first global Managed TMS® solution, as well as logistics outsource solutions, fresh produce sourcing, and payment services. C.H. Robinson's 37,000-plus customers range from Fortune 500 companies to small businesses in a variety of industries.

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