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NOVEMBER 2012

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Management UPDATE

AN EXECUTIVE SUMMARY OF INDUSTRY NEWS

Heavy holiday on the way. Both transportation and logistics bellwethers UPS and FedEx are predicting a hectic holiday season paced by heavy volumes. UPS said earlier this week that it expects to deliver 527 million packages between Thanksgiving and Christmas this year, which would top last year's record 480 million. UPS added that its busiest day of the year is expected to be Thursday, December 20, when its forecast to deliver an estimated 28 million packages globally. To put that number into better perspective, UPS said it is the equivalent of more than 300 packages being delivered every second of that day—whereas on an average day it delivers 15.8 million packages. In terms of air packages on December 20, UPS said that it is expecting to deliver more than 6.5 million air packages.

CEVA CEO Pattullo retires. Global third-party logistics services provider CEVA Logistics announced that CEO John Pattullo retired on October 12. Marvin O. Schlanger, the company's chairman of the board, has been named as new CEO. Pattullo joined CEVA in 2007 following 30 years at Procter & Gamble in global marketing, logistics, and sales roles. "When John came to CEVA, he expressed his expectation of staying with the company for five years," Schlanger said. "Under his leadership, the integration of TNT Logistics and EGL was successfully executed and the company's unique customer-focused, end-to-end operating model was successfully developed."

Diesel prices hit four year high. The price per gallon of diesel gasoline reached $4.15 per gallon in mid-October, according to the Department of Energy's Energy Information Administration. This is the highest price since the week of August 18, 2008, when prices were $4.207 per gallon. Prices overall have been trending up for several weeks, as evidenced by 11 consecutive weeks of gains through the week of September 17, during which time prices rose a cumulative 48.7 cents.

ATA chief upbeat on trucking's future. Despite myriad challenges and obstacles facing the trucking industry, American Trucking Associations (ATA) President and CEO Bill Graves, this month's *Logistics Management (LM)* cover subject, said at last month's ATA annual Management Conference & Exhibition that trucking is on a strong road for future growth, commenting that "the essentiality of the industry and the demand for freight movement by truck is unquestioned. The long-term macro outlook for trucking has never been better, but the near-term micro view continues to be very challenging." Among the challenges cited by Graves were a sluggish economy and a "very dysfunctional" federal government. Also high on the list of trucking industry concerns were regulations, namely CSA, HOS, and EOBR.

Early peak. New research indicates that the peak month for U.S. imports in 2012 will most likely be July. According to Zepol Corp., a leading trade intelligence company, U.S. import shipment volume for September, measured in twenty-foot equivalent units (TEUs), is down 3.6 percent from August. At the same time, however, it is up from September of 2011 by 2.6 percent. Imports of TEUs shifted from over 1.6 million last month to 1.55 million in September. The downward trend of the last two months of Q3 may signal a strengthening of retailer forecasting, said Zepol's CEO Paul Rassmussen, who noted that the surge in goods for the holiday season seems to have come even earlier in Q3. "The third quarter of 2012 is up 3.8 percent from the third quarter of last year," said Rassmussen. "U.S. importers may be feeling optimistic about the economy and preparing early for a busier shopping season than 2011."

Export forward. Department of Commerce Secretary Rebecca Blank recently selected Brandon Fried of the Washington D.C.-based Airforwarders Association to the newly formed U.S. Advisory Committee on Supply Chain Competitiveness. The Committee will act as a liaison between industry and government, and is an important step toward ensuring regular contact with the supply chain industries, including manufacturers, freight forwarders, shippers,

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Management UPDATE

Continued

distributors and exporters. The committee's advice will also be useful in the development of a national freight policy and in executing the National Export Initiative, which aims to double U.S. exports by the end of 2014.

Up in the air. In a related development last month, U.S Secretary of Transportation told delegates at the 26th International Air Cargo Forum & Exposition in Atlanta that a healthy air cargo industry is essential in helping the U.S. government achieve its goal of doubling U.S exports by 2015. According to Secretary Ray LaHood, DOT is doing its part to build a transportation system that supports President Obama's export goal. This includes the recent creation of the new Freight Policy Council, a high level and multi-modal internal body that will help to develop a national plan to improve freight movement.

High-tech speeding up. UPS' annual *Change in the (Supply) Chain* survey, conducted by IDC Manufacturing Insights and targeting U.S.-based senior-level supply chain decision makers in the high-tech/electronics industry, suggests renewed confidence in the nation's exporting potential. Despite economic uncertainty at home and abroad, survey respondents were bullish. "The anticipated shift in consumer market demand for high-tech goods brings opportunities and challenges for high-tech companies," said Ken Rankin, high-tech marketing director at UPS. "Global demand will continue to grow in new and existing markets, causing supply chain executives to shift not only their fulfillment operations but also their sourcing strategies to serve those markets. We have already started to see a shift, as companies look to India and Brazil as key markets not only for fulfillment but for production as well," he said.

Ocean cargo profitability rebound. In its recent report, *Restoring Profitability to Container Shipping*, analysts at Boston Consulting Group recognize that even though some ocean carriers were close to bankruptcy over the past few years, such struggles are not new. "For years carriers have wrestled with earning back the cost of capital, and in 2009 they were confronted with a crisis caused by a significant drop in demand," noted the report. The report said that last year their distress resulted primarily from intense competition and price wars triggered by carriers' reactions to a self-inflicted supply-and-demand imbalance. In 2011, the arrival of new vessels ordered years earlier boosted capacity by one million twenty-foot-equivalent units (TEUs) for 16 of the largest publicly-listed carriers—an increase of 8.7 percent over 2010 levels. Carriers had placed these orders planning to increase market share, noted the report.

Slowdown or just a shift? Global trade patterns from August to September showed sequential declines and annual gains according to data released by Panjiva, an online search engine with data on global suppliers and manufacturers. U.S.-bound waterborne shipments, which were up 9 percent from June to July and down 3 percent from July to August, dropped 4 percent from August to September, according to data. September shipments were up 7 percent on an annual basis. "The data earlier in the year leading up to the holiday season suggested that businesses weren't feeling particularly confident about what the holiday season had in store for us," said Panjiva CEO Josh Green. "What the numbers seem to suggest is that it is not so much of a slowdown as a shift to later orders. What seems to be the case is that [shippers] held off as long as they could in making their buying decisions, hoping there would be more clarity about where the economy is headed."

Prologis' global commitment. Since global industrial real estate bellwethers Prologis and AMB Property Corporation finalized their merger into a singular entity under the name Prologis in June 2011, company officials stress that it's very much committed to international growth—with 80 percent of its total space allocated to global markets. At last month's CSCMP Annual Conference, Steve Callaway the company's senior vice president and head of global customer solutions, told *LM* that global trade and population/consumer base are the two things the company's investments are focused on, with a goal to develop $2.5 billion in property annually.

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Cover photography: Eli Meir Kaplan/Getty Images

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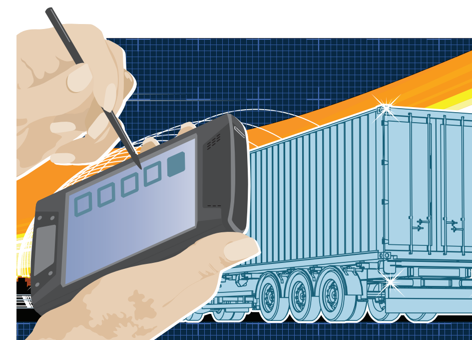

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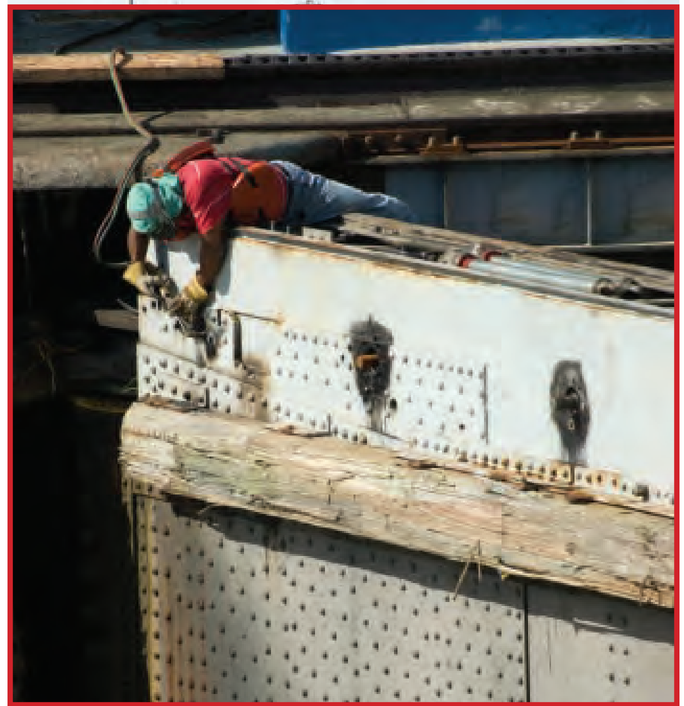

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VIEWPOINT

Nice guys finish first

I'M PLEASED TO ANNOUNCE that the National Industrial Transportation League (NITL) and *Logistics Management* (*LM*) magazine are presenting Bill Graves, former Governor of Kansas and current president and CEO of the American Trucking Associations (ATA), with the 2012 McCullough/NITL Executive of the Year Award.

This honor, which recognizes an individual for achievement and leadership in the logistics and transportation industry, is co-sponsored by NITL and *LM* and is named after John T. McCullough, a former chief editor of *Distribution* magazine, a predecessor of *LM*. I will be presenting the award to Gov. Graves on Monday, November 12, at the opening ceremonies of the 105th Annual Meeting & TransComp Exhibition in Anaheim, Calif.

During a time when the nation is suffering through one of its worst periods of hyper-partisanship, it seems quite fitting that a leader like Gov. Graves is being honored with this year's award. While there's a long list of achievements during his service in trucking that could have earned him this award, there's an even longer list of intangibles that characterize this true leader, mediator, and listener who takes the time to "hear" what you're saying regardless of what side of the aisle you find yourself.

After reading Schulz' portrait of Gov. Graves (page 26), one quickly learns how the roots of his character took hold early. As a youngster,

he began working on the docks at Graves Truck Line, a company that his family operated for 70 years out of Salinas, Kan. "The first year I paid into Social Security was 1966. I was 13," Graves tells Schulz. "So, that would have been the first year that dad had me doing something, probably sweeping the freight docks."

But that was just the beginning of his many life lessons. At the age of 41, Graves was inaugurated as one of the youngest governors in Kansas history. He would end up serving two terms, winning re-election (1998) by the largest margin in the history of the state.

After he completed his second term, capping off 22 years of service to the citizens of Kansas, Gov. Graves' life came "full circle" when he took the reins at the ATA—the federation of 50 trade associations that lobbies Congress, federal agencies, and presidents on behalf of the $700 billion U.S. trucking industry.

While he's had the wheel, Graves has pushed for stronger safety regulation, a national speed limit of 65 mph, and greater drug and alcohol testing of the 3 million long-haul truck drivers operating in the U.S.

Graves is even pushing for an increase in the federal tax on motor fuels to help pay for much-needed infrastructure reinvestment—an initiative that may fall on deaf ears until early next year.

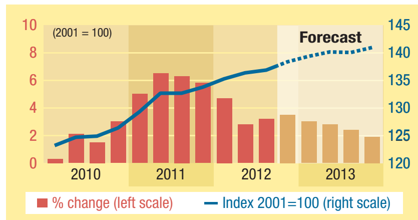
And while his list of achievements would go on for pages, Schulz says what really defines Gov. Graves is the affable, endearing way in which he goes about meeting the needs brought on by a diverse community.

"ATA has about 3,000 members—from UPS to small mom-and-pop truckers," says Schulz. "Some are union, some are non-union. There are LTL carriers, TL carriers, and everybody in between; and on some issues, ATA's stance has to conflict with at least a few of its members. Yet he manages to keep all the balls in the air through his quiet nature and desire for compromise."

Michael A. Levans, Group Editorial Director

Comments? E-mail me at mlevans@peerlessmedia.com

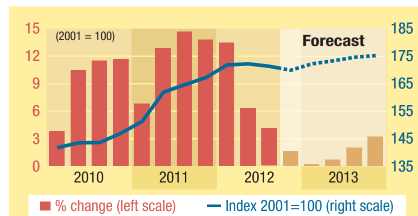
Pricing Across the Transportation Modes



% CHANGE VS.:	1 month ago	6 mos. ago	1 yr. ago
General freight - local	0.0	-0.3	1.0
TL	1.3	1.1	4.9
LTL	0.7	2.5	6.1
Tanker & other specialized freight	0.9	0.8	1.6

TRUCKING

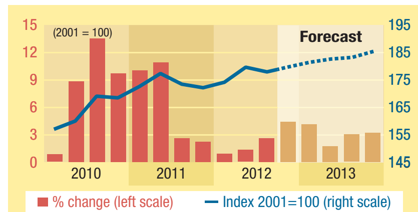
Average transaction prices charged by all U.S. trucking companies increased 1% in September. That was the biggest one-month price hike since March. Are we entering a new phase of pumped-up inflation? Probably not, according to the cost models we've been solving. The industry's single biggest inflationary driver, fuel costs, declined 8.1% from previous quarter and fell 7% from year-ago levels. Total costs likewise dropped by 2.1% and 0.6%, respectively, over the same time periods. Average transaction prices, meanwhile, declined only 0.5% from previous quarter and actually increased 2.7% from year-ago. Upshot: Negotiation leverage favors logistics managers, at least for a moment.



% CHANGE VS.:	1 month ago	6 mos. ago	1 yr. ago
Air freight on scheduled flights	0.2	-0.4	3.8
Air freight on chartered flights	6.6	4.2	8.0
Domestic air courier	1.4	-0.9	3.5
International air courier	1.4	-2.6	2.0

AIR

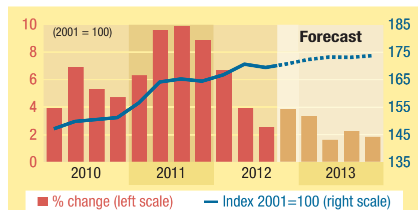
Following four consecutive months of price cuts, average transaction prices for flying freight on scheduled flights of U.S.-owned airliners reversed course, up 0.2% in September. In an even bigger course correction, U.S.-owned planes chartering freight on domestic routes raised their prices 5.6% and those flying international routes hiked tags up 8.9%. Whether or not these one-month price increases survive Bureau of Labor Department's survey revisions, one thing in the air transport business remains clear: turbulence in airfreight pricing remains the rule. Pity the poor economist who dares to forecast. Our annual inflation forecast for scheduled airfreight prices remains 6.2% in 2012 and 1.5% in 2013.



% CHANGE VS.:	1 month ago	6 mos. ago	1 yr. ago
Deep sea freight	-2.0	-1.8	0.1
Coastal & intercoastal freight	0.0	2.4	7.0
Great Lakes - St. Lawrence Seaway	2.7	-4.9	6.4
Inland water freight	0.8	0.8	1.4

WATER

Price trends lately have been favoring buyers who contract with U.S.-owned vessels to move cargo over water. Water transportation service providers report transaction prices fell for the fourth month in row, down 0.6% in September. In the third quarter, Great Lakes/St. Lawrence Seaway prices dropped 2.4% and inland waterways tags fell 2.2%. Summing up the entire industry, prices declined 0.9% from previous quarter, but remained 2.6% above year-ago levels. One reason this industry could cut prices has been due to a pleasing turn in the tide of underlying fuel costs. Our cost model estimates fuel costs are down 5.2% from previous quarter and down 3% from year-ago levels.



% CHANGE VS.:	1 month ago	6 mos. ago	1 yr. ago
Rail	0.2	1.3	2.7
Intermodal	1.9	0.9	3.5
Carload	0.0	1.4	2.6

RAIL

Following tracks set by long-distance truckers, intermodal rail service providers report their transaction prices increased 1.9% in September. Although that was the largest one-month price increase since May 2011, it wasn't enough to derail the quarterly price trend. Intermodal rail prices in Q3 still fell 1% from the previous quarter. At the same time, carload rail tags held steady in September and ended Q3 down 0.7%. Cost pressures to raise rail freight prices remain weak. Day-to-day costs to run railroads (fuel, labor and materials) have fallen 2.9% from previous quarter and dropped 1.9% below year-ago spending. Our rail industry inflation forecast, however, stands pat at 4.2% in 2012 and 2.2% in 2013.

Source: Elizabeth Baatz, Thinking Cap Solutions. E-mail: ebaatz@alertdata.com

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3 WAYS LOGISTICS CAN SHRINK THE WORLD.

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- Looming demographic crisis, increased government regulations threaten recovery

NEWS & ANALYSIS

CEO panel addresses how current capacity is matching up with demand

Myriad factors in play when gauging capacity's impact on modal market conditions

By Jeff Berman, Group News Editor

ATLANTA—Last month's Council of Supply Chain Management Professionals (CSCMP) Annual Conference provided insight into myriad aspects of various transportation markets at its annual CEO panel session. But perhaps the most telling takeaways of the session had to do with how capacity among various modes is matching up with demand.

Atlas Air Worldwide President and CEO Bill Flynn led off, discussing the balance of capacity and demand in what is currently a very challenging air cargo market.

"The last five years for international air freight has been choppy," said Flynn. "We had a good rate of growth from 2000 to 2007 at a 6 percent to 7 percent annual rate, but the market began to contract in 2008 and really fell off the cliff in the second half as international demand contracted by 25 percent and export demand from Asia fell by 35 percent—and that contraction continued into the first quarter of 2009."

In terms of market contractions' impact on capacity for air cargo, Flynn said that when markets contract or grow, capacity responds more slowly. He said that this was evident when capacity left the market in 2008 and 2009 and continued into the first half of 2010.

He added that the market did not believe that type of demand existed, and rates and yield expanded significantly. "At this point, we're looking at a 3 percent to 3.5 percent growth rate in the next 10 years, and it seems that the capacity in the market right now matches that growth rate," said Flynn.

Shifting modes from air to ocean, former CEVA Logistics CEO John Pattullo said that he's seeing significant new capacity entering the ocean market, with larger vessels ordered two or three years ago now moving cargo—all while current demand is lacking to keep capacity fully utilized. This, he said, leaves the ocean market more curtailed toward a global supply of capacity.

On the trucking and intermodal side, Transplace CEO Tom Sanderson said the capacity shortage is primarily in the long-haul truckload segment, where drivers are away from home for weeks at a time and is a very high-turnover business.

"There really is nothing that is going to serve to increase capacity, because you can build all the trucks you want, but you are not going to find drivers that want to live that lifestyle," said Sanderson.

Due to this situation, Sanderson said it makes sense for shippers to reduce demand of freight by shifting to intermodal, as there is plenty of available intermodal capacity.

Another strategy shippers should consider, said Sanderson, is to design networks that have more regional transportation and less-than-truckload

> **"Looking back over the last 20 years as a truckload carrier, we have only seen a few years that have met even a minimum return on invested capital."**
>
> *—John Roberts, J.B. Hunt President and CEO*

alternatives.

J.B. Hunt President and CEO John Roberts agreed with Sanderson in that there is clearly a shortage of long-haul truck drivers, and added that the truckload business model is very unstable.

"Looking back over the last 20 years as a truckload carrier, we have only seen a few years that have met even a minimum return on invested capital," said Roberts. "As a big truckload carrier, we are deferring to intermodal capacity for longer lengths of haul and look at two sets of criteria for that capacity management—revenue quality and utilization."

Roberts said that there are some nuances with regard to intermodal that are not present in truckload when it comes to things like asset longevity. "J.B. Hunt is getting better at seasonally holding equipment, pre-ordering, and allowing that equipment to come in as activity picks up," he said, adding that dedicated fleets then play a role in figuring out the balance between the mid-range length of haul.

But Roberts cautioned that much of the capacity situation comes back to the truck driver shortage situation, coupled with the fact that "nobody is raising their kids to be truck drivers." What's more, he added that there's a wide gap between what private fleets pay their drivers and what common truckload carriers can pay.

Addressing railroad capacity, Roberts said that rail carriers are doing a nice job of investing into their infrastructure with ramps that provide companies like J.B. Hunt with more lift capacity and shorter lengths of haul.

"It is up to us to make sure we have the right number of boxes…overcapacity can lead to rate pressure, which we don't like, and we need to meter that out and stay in balance," said Roberts. □

GLOBAL TRANSPORTATION

FedEx offers up details on cost reduction efforts

MEMPHIS—Global logistics and transportation bellwether FedEx last month rolled out its long-awaited plans to reduce costs in the company's Express segment.

The company said that it has a goal of an annual profitability improvement of $1.7 billion during the next three years, with a majority of the benefits to be achieved by fiscal 2015.

FedEx Chairman, President, and CEO Fred Smith said that much of the improvements will stem from FedEx Express and FedEx Services cost reductions, coupled with the "combined strength" of FedEx Ground and FedEx Express.

A *Wall Street Journal* report broke down some of the major components of FedEx' plan:

- $700 million of the target amount will come from reconfiguring the company's domestic and international networks, including the replacement of 5,000 delivery trucks.
- $300 million would come from modernizing its aircraft fleet, with $400 million gained from consolidating back-office functions.
- Consolidation of some domestic Express pickup locations and driving routes as well as combining selected international flights.
- $150 million in cost reductions from better pricing and yield management initiatives, including European expansion.

The report added that FedEx is expecting nearly $1.6 billion of the profitability improvement to come from its Express division.

Other previously disclosed parts of the company's cost reduction efforts include a voluntary buyout plan, which was announced in August, and decisions to retire certain aircraft and modernize its Express fleet.

"We are revamping the Express cost structure through a combination of cost reductions, efficiency improvements, and service repositioning," Smith said. "Our overall strategy is closely tied to effective yield management. The key is striking the right balance between volume growth and yield improvements."

Smith added that there are various cost reduction efforts going on, with an improved information technology function to serve as a driver to reduce costs. Among the cost reduction efforts he cited were in general and administrative expenses spread throughout company, with an emphasis on FedEx Services and FedEx.

In the fiscal first quarter, the company's net income at $459 million fell 1 percent annually from $464 million. Quarterly revenue of $10.79 billion was up 3 percent from last year's $10.52 billion, and operating income at $742

million was up 1 percent from $737 million. Its operating margin—at 6.9 percent—was down 7.0 percent.

FedEx' total U.S. domestic express packages, at 2.429 million per day, saw a 5 percent annual decline, while international priority, at 408,000 packages per day, dipped 2 percent.

international domestic was up 53 percent at 681,000 packages per day. Total revenue per U.S. domestic package at $17.33 was up 2 percent, due to higher rates, while total revenue per package for international priority and international domestic at $62.68 and $7.00 were down 3 percent and down 2 percent, respectively.

Jerry Hempstead, president of Orlando, Fla.-based parcel consultancy Hempstead Consulting, said that in regards to making changes on the Express side, FedEx is in a strong position in that it can alter its flight routes to obtain cost savings and not be at a competitive disadvantage.

Hempstead also explained that the trucks that FedEx replaces would be more fuel efficient, although buying planes and trucks comes at a cost—although there are some tax benefits associated retiring trucks and planes.

However, the company's emphasis on yield improvement is certain to spell higher rates for shippers, Hempstead said. The reason for this, he said, is that FedEx needs to extract more money from the packages that they transport because packages are not growing.

"This will be done by a combination of means such as raising base prices and reducing discounts offered to existing shippers or to attract new customers," said Hempstead. "The best protection a shipper has is to know its spend by service type, weight, and zone. Both transports provide a consistent predictable high quality service experience, so don't be afraid to switch if there is a significant cost reduction opportunity for your firm to do so."

—Jeff Berman, Group News Editor

TRUCKING

Trucking Forecast: Bullish short term, bearish mid-decade

WASHTINGTON, D.C.—Trucking will see very solid growth next year as U.S. manufacturing improves, but faces a tightening capacity situation because of tougher regulations that could hinder the industry's ability to hire enough qualified drivers.

That's the word from Noel Perry, economist from FTR Associates, a respected and long-time trucking forecaster who is forecasting a decent 2013, but warned of a good chance of recession in mid-decade.

"Most economists don't forecast recessions," Perry said last month at the annual meeting of the North American Transportation Employee Relations Association (NATERA). "But I do."

While Perry is predicting just a 2.5 percent growth in Gross Domestic Product (GDP) for 2013, trucking volumes could rise as much as 5 percent next year. That's because of an improving climate for U.S. manufacturing, among other factors, according to Perry. "We are at the tail end of a period of relative stability in the economy," Perry said. "Not much has happened in trucking in the last 18 months."

He said supply is roughly in line with trucking demand, but warned there are changes ahead in the next three to four years. "There is a new wave of regulation that will change a minor driver shortage into a major driver shortage," Perry said, alluding to the government's Compliance, Safety and Accountability (CSA) program that is estimated to eliminate as many as 150,000 driver jobs in the next five years.

The current overall anemic economic recovery has actually been quite solid for trucking due to improving conditions in manufacturing, including the booming U.S. auto sector. However, Perry is somewhat bearish on the overall economy because of declining orders for non-defense capital goods orders. He said that there's a good chance of recession in late 2013 or early 2014—and that the U.S. might take a decade to completely recover from the downturn of 2008-2009.

"The last time this happened to the U.S. economy was 1930," Perry said. "The economy recovered quite quickly from the depression, but the jobs situation did not improve until 1940."

"There is a new wave of regulation that will change a minor driver shortage into a major driver shortage"

—Noel Perry, economist, FTR Associates

On the positive side, Perry declared the "energy crisis is over" because of the newfound glut in domestic sources including natural gas. He also believes that fuel prices will likely drop about 50 cents in the next year, perhaps more during his forecast recession.

However, because of changing demographics, the continued driver shortage will only worsen. He called driving recruiting the No.1 issue for trucking—"and it's only going to get worse," Perry said.

"How do we go from hiring 200 people one year and 2,000 the next?" Perry said. "That is the No. 1 problem for trucking right now."

Exacerbating the problem is an aggressive regulatory truck safety agenda in Washington. He said driver supply will worsen in the wake of CSA, tighter hours of service, electronic onboard recorders, tougher drug and alcohol testing and aging demographics.

"Not only is the economy putting stress on your hiring ability," Perry told the trucking gathering. "But the government is too." And for the short term that means capacity will remain tight—at least in the next year or two. Because of tighter regulations, Perry is forecasting that the driver shortage could hit as many as 300,000 in the next few years.

—John D. Schulz, Contributing Editor

POLICY

Looming demographic crisis, increased government regulations threaten recovery, says Josten

WASHTINGON, DC—According to a top business lobbyist, the nation faces a demographic crisis that is creating a drastic need to reform retiree and healthcare entitlements.

"You cannot get from here to there without tackling entitlement reform," R. Bruce Josten, executive vice president for government affairs for the U.S. Chamber of Commerce, told the 26th annual meeting of the North American Transportation Employee Relations Association (NATERA) last month.

Meanwhile said Josten, "Congress continues to kick the can down the road…but we're about to run out of road."

Josten said that efficiency in the supply chain is "critical" to the nation's overall economic health. "When government is holding you back as an industry, it's basically holding everybody back in the economy," he said.

Josten added that the government's proposed hours-of-service cutback and other initiatives contained in its Compliance, Safety, and Accountability (CSA) policy are simply lacking in common sense. "When a parked truck is hit by another vehicle and the trucking company is penalized, it's clear to us that common sense is absent," he said.

He added that the 112th Congress is an "embarrassment" due to the lack of action. This Congress passed just 73 laws, well below the famous "do-nothing" Congress of 1947-48 that passed more than 900 laws. "Among other inaction, this Congress has failed to even pass an overall budget," said Josten.

Josten called the election "a jump ball" that will largely depend on how each party's success at getting its base out to vote in two weeks. "The president faces two opponents—Mitt Romney and a stagnant U.S. economy," Josten said, adding that reform of entitlement programs—Social Security, Medicare, and Medicare—are badly needed to create a better fiscal environment to spur an economic rebound.

"Demography is destiny," Josten said, noting that current 3-to-1 workers-to-recipients ratio will fall to 2-to-1 within the next five years. "That worker-to-retiree ratio is accelerating downward."

The Obama administration is currently "in a holding pattern" on issuing new regulations. But Josten, who tracks more than 350 issues as the No.2 lobbyist at the Chamber behind Chamber President and CEO Thomas Donohue, said the administration will continue its aggressive rulemaking once the election is over.

The Chamber is actively fighting what it perceives as regulatory overkill. "We have been forced to play both defense and offense," Josten said.

He added that some of the most economically significant pending regulations affect ozone non-attainment levels, reducing the sulfur content of gasoline, greenhouse gases from oil refineries, hydraulic fracking, and particulate matter in diesel soot.

According to Josten, there are more than 350 large infrastructure projects that are threatened because of the lengthy reviewing process brought by lawsuits from environmental groups.

—John D. Schulz, Contributing Editor

SUPPLY CHAIN MANAGEMENT

Supply chain efficiency can lead to bottom line success, says retail shipper

ATLANTA—The concept of "following the money" may apply to the supply chain and freight transportation sectors more than most. In fact, savvy logistics and supply chain managers understand the following axiom: "Where the freight is the money is."

That mindset was front and center at "How Supply Chain Drives Shareholder Value," a session held in part of the Council of Supply Chain Management Professionals' (CSCMP) Annual Conference last month.

During this session, Greg Rake, senior vice president of supply chain at Pier 1 Imports, explained that supply chain's influence on company value can be measured through speed to market.

"The faster you get products to market, the more full-price sales you get," said Rake. "If we can figure out a way to get a new product into the market prior to Target or Wal-mart, Kohl's, or J.C. Penney…we get to enjoy full-price sales for some period of time. This shows why speed to market is important, and Tthe engine that drives speed to market is effective supply chain management."

Rake quipped that as a college student at Ohio State University 30 years ago, supply chain was someplace where old manufacturing and sales majors were put out to pasture. But now, especially in manufacturing and retail environments, supply chain ranks as one of the top three issues that have an effect on a company's cost of product.

"People are now looking at the supply chain and saying 'that is really a place where we can drive gross margins,'" said Rake. "It has become increasingly important that we, as supply chain executives, recognize the impact we have on the bottom line."

Another area where the supply chain can boost the bottom line is brand protection, said Rake, while stressing that nothing good happens when you touch products. "At Pier 1, each product is touched 11 times before it gets to the consumer," he said. "Every single day, our team works as hard as it can to figure out how to reduce the number of touches we have before the product reaches the consumer."

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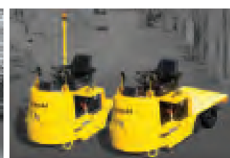
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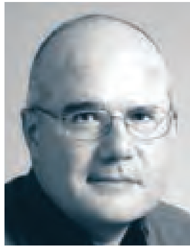

What's the CCSB doing now?

IF YOU HATE PAYING EXTRA FOR BAGGAGE on flights, you will be unhappy with this news. The Commodity Classification Standards Board (CCSB), a voluntary rules committee representing 845 motor carriers, has passed a ruling that classifies pallets as a commodity subject to density rules, and therefore potentially higher rates.

Classification of products based upon weight, density, value, and other factors helps determine rates in the National Motor Freight Classification (NMFC). Pallets that were previously Class 70, or the class of the freight on board, are now a separate variable classification with a maximum class of 400.

If this is upsetting, note that this classification published as Subject 10 2012-3 is subject to NMFC Rule 170 that states that if the shipper fails to specify the density or class on the Bill of Lading it will automatically be subject to the maximum classification—in this case 400.

This means that many shippers will be subject to a price increase that they didn't see coming. But to avoid this economic pain, shippers need to act quickly. This rule was already approved by the CCSB and will go into effect December 1, 2012.

The CCSB is a holdover from the days of legalized rate collusion by carriers and is an affiliate of the NMFC. This is just the latest in a series of CCSB collective moves to raise rates indirectly through classification changes; and the impact will be felt most by the shippers that don't understand the classification system.

Many shippers use a standard Bills of Lading that includes language that reads:

Received, subject to individually determined rates or contracts that have been agreed upon in writing between the carrier and shipper, if applicable, otherwise to the rates, classifications, and rules that have been established by the carrier and are to the shipper, on request; and all the terms and conditions of the NMFC Uniform Straight Bill of Lading, NMFC Item 360.

In other words, what's not specified in a contract between the shipper and carrier becomes subject to the rules as published in the NMFC.

At this stage, many shippers don't have the capability of treating a pallet as a commodity with full separate description on the Bill of Lading. In fact, many will need to make a quick scramble to re-program their transportation management systems.

To avoid being caught in this trap, shippers can check the density of their pallets. The new provisions make the pallets subject to the NMFC density table shown. Note that for many popular pallets of approximately 7.5 lbs./cubic foot, this means Class 125. Rates for Class 125 are approximately 50 percent higher than class 70 rates.

The new provisions do have an "out." The current version known as NMFC 100-H states that: "Participants are neither constrained nor compelled to use or abide by these provisions, as they always have the free and unrestrained right of independent action."

Shippers should immediately open negotiations with their carriers to exempt themselves from this new provision. But if your carrier has already dropped participation in the NMFC, then you won't be affected by this new provision.

This last point is critically important: The NMFC and the CCSB are anachronisms that need to be put to sleep. Carriers and shippers can and should be contracting for services based upon actual product properties and today's dynamics such as capacity, backhauls, insurance, fuel costs, and over 20 other factors. □

New scale of rates for pallets

Pallets; Platforms; Racks, shipping, NOI; or Skids; for lift trucks, steel or wood, or without bodies, enclosures, ends, sides, stakes, standards or stacking posts, to Items 170 and 171 and having a density in pounds per cubic foot of:

Density	Class
1 or less than 1	400
1 but less than 2	300
2 but less than 4	250
4 but less than 6	150
6 but less than 8	125
8 but less than 10	100
10 but less than 12	92.5
12 but less than 15	85
15 but less than 22.5	70
22.5 but less than 30	65
30 or greater	60

Source: CCSB September 14, 2012, *Disposition Bulletin* 1319

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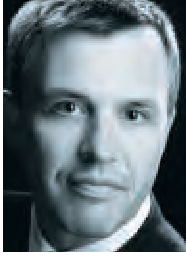

Reducing commodity price risk

ONE HALLMARK IN THE ERA of permanent volatility is fluctuating commodity prices: everything from aluminum (variations up to 30 percent in 2012) to zinc (variations up to 25 percent in 2012). The result is endless headaches for people and departments in virtually every industry: the procurement folks buying materials; the logistics and transportation staff moving it; the finance guys forecasting expenses; and even the sales and marketing staff struggling to pass unanticipated cost increases on to customers.

Despite the broad use of commodities—and the significant risks that volatility poses—few companies excel at "commodity price risk management." Of course there are exceptions, notably specialized commodity processors. But in most fields, price risk management is relegated to a few procurement professionals who use supplier relationship management or strategic sourcing tools that aren't really designed for the task. Following are some technology and process innovations that might do a better job of helping organizations deal with commodity price risk.

Risk analytics. Risk analytics can help companies gauge the effects of commodity price forecasts, control exposure to fluctuating prices, and develop risk-management strategies that align with the organization's risk appetite. One area with particular relevance is sourcing, where companies can use analytics to:

Develop intelligent segmentation—setting strategic direction for categories and subcategories by identifying, and potentially substituting, materials with lower price volatility.

Discover correlations—understanding the impact of market developments and tying that knowledge to production processes and related byproducts. For example, caustic soda is a byproduct of chloride production.

Understand real costs versus low costs—learning more about what a company specifically needs. For example, an animal feed business may need certain vitamins. However, it isn't uncommon for a majority of vitamin content to disappear during high-temperature production. Perhaps it would be more cost effective to use a pricier vitamin composition with better resistance to degradation.

Enable deep sourcing—performing in-depth analyses of specific categories to identify new supplier-development, low-cost-country sourcing, and backward integration opportunities.

Hedging optimization. Most firms understand the importance of direct hedging, or using indexed contracts, commodity derivatives, and strategic pre-buys and contract structuring. However, companies might also benefit by optimizing the total hedge position over time—combining similar exposures across different business units or geographical regions (for example, energy exposure in Europe or North America). The key is viewing prices not only at an absolute level, but relative to each other.

Governance model. An innovative risk-management-focused governance model can help cascade an organization's high-level risk appetite—the amount of budget variation it is willing

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to tolerate—into specific day-to-day tactics for individual commodities and regions. The model could also help specify accountability for daily risk-management activities and establish a hierarchy for oversight and reporting of positions and risk exposures. Once a governance model is established, a risk policy can be penned that details guidelines for risk analytics, risk reporting, exception management, key performance indicators, and specific roles, job functions, and tasks.

Companies with sub-par risk-management capabilities are taking a big chance: Pressure on working capital and wide swings in performance will likely increase, and passing price increases through to end consumers could well become more difficult than ever.

Recipe optimization. Recipe optimization can help companies anticipate market changes and risks by focusing more tightly on product characteristics. Such efforts might include rationalizing the bill of materials and/or recipes by choosing low-risk or hedgeable raw materials that reduce the product's complexity and the variety of required materials. These efforts can help reduce exposure and broaden supplier scope.

Should-cost modeling. Should-cost modeling segments a product into basic cost factors, such as raw materials and transportation costs. Each component can then be broken down into a more-detailed "cost split up." For example, to calculate the should-cost of a certain process step, that step can be segmented by cost drivers. Companies can monitor the should-costs of a raw material over time and compare those figures with the price fluctuations of the entire product.

Turning risk into opportunity

When it comes to commodity prices, permanent volatility may well be the "new normal." As a result, companies with sub-par risk-management capabilities are taking a big chance: Pressure on working capital and wide swings in performance will likely increase, and passing price increases through to end consumers could well become more difficult than ever.

The potential upside, however, is significant: According to Accenture research, an organization with a $1 billion materials budget (half of which is tied to volatile commodities) could leverage commodity price risk management to reduce its annual materials costs by up to 10 percent. ☐

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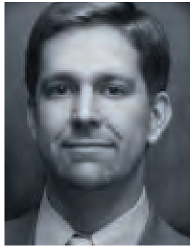

Energy is a bipartisan issue

WITH THE PRESIDENTIAL ELECTION just around the corner, divisive and intentionally misleading partisan talking points on energy have come to dominate the media.

These talking points apply a layer of partisan paint to what are truly bipartisan policies, thus creating an "us versus them" mentality on both sides of the aisle. More importantly, they simplify public perception of our current energy situation, what's possible with regard to energy independence, and what steps will take us in the right direction.

While one candidate or the other may benefit in the short term by oversimplifying energy issues and sowing the seeds of division, such gains are made at the expense of long-term prosperity by erasing the significant amount of agreement that exists between Republicans and Democrats on energy and related environmental issues. As a case in point, few would view any of the following issues as bipartisan.

- Environmental regulation
- Alternative energy subsidies
- "Drill baby, drill"
- Oil pipeline promotion

Environmental regulation and alternative energy subsidies have come to be associated with Democrats, and oil pipelines and "Drill baby, drill" with Republicans. Such generalizations obscure more than they reveal and needlessly consume a truly scarce resource: bipartisan cooperation.

Few realize that the Environmental Protection Agency (EPA) was created with the stroke of a pen held by none other than President Richard Nixon, and the Environmental Protection Act, which shares its acronym and general goals, was signed into law by President George H.W. Bush. Nixon also signed into law the Endangered Species Act, the Marine Mammal Protection Act, the Safe Drinking Water Act, and the Clean Air Act—all of which have complicated domestic oil and gas production and refining as well.

Ironically, laws outlined by these acts are being used by "fracktivists"—those opposed to hydraulic fracturing—to slow or halt unconventional gas production.

Of course Nixon and Bush weren't secret Greenpeace operatives who infiltrated the highest level of government. Rather, each happened to be president when the will of the people insisted that deteriorating environmental health be addressed. These pieces of legislation, which first passed through the Democrat-controlled House and Senate, were common sense initiatives that addressed among other things, the impact that energy production and consumption (especially of fossil fuels) have on the environment and society.

Neither party can take full credit for the positive impact that these initiatives have had, nor can one party take the full blame for the economic inefficiencies that accompany these regulations.

Environmental regulation and alternative energy subsidies have come to be associated with Democrats, and oil pipelines and "Drill baby, drill" with Republicans. Such generalizations obscure more than they reveal and needlessly consume a truly scarce resource: bipartisan cooperation.

Energy production and consumption will always have negative externalities that need to be mediated, and politics is the art of such mediation. Partisan talking points and the "us versus them" mentality that they enshrine inhibit the greater good.

Alternative energy

When we think of alternative energy sources, we see a similar pattern of bipartisanism hidden behind partisan talking points. Traditional energy sources include coal and conventional oil and natural gas. Alternative energy sources include not only the obvious "green" contenders—wind, solar, and hydro—but also the wildly successful production of unconventional oil and gas resources including coal bed methane and hydro-fracked shale oil and shale gas.

While many would not include unconventional fossil fuels in the "alternative energy" category, they share a number of important characteristics with wind and solar. The development of each requires expensive basic research, complex technology development, and lead times that are best measured in decades.

As a consequence, none of the three (solar, wind, and unconventional oil and gas) would make viable investments at the early stage of development. If left only to the private sector, there will be underinvestment in these risky technologies that are not likely to earn a positive return for

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decades—and this is why all three require government subsidies and assistance while in the development phase.

Popular discourse would suggest that all Republicans are in favor of fracking, and all Democrats oppose the practice, but it will no doubt come as a shock that the development of hydrofracking extends back to the Carter administration. That's right, the technology that has pushed natural gas prices down by 75% or more in just the last few years and raised the ire of environmentalists across the globe has been under development for more than 30 years—and can trace its seed funding back to a Democrat.

Of course this funding was continued by Carter's successor, Ronald Reagan, and was further supported by Bush Sr., Clinton, Bush Jr., and Obama.

As Dan Steward, the former geologist for Mitchell Energy who pioneered commercial shale gas production in Texas, explains: "The government was behind the critical moments and tools in the shale gas revolution [including] massive hydraulic fracking, 3-D mapping, and horizontal drilling." By the way, Steward describes himself as "conservative as hell," but as an industry pioneer he recognizes that the Department of Energy programs that sustained the effort received support from both Democrat and Republican administrations.

Wind and solar have been similarly subsidized by Democrats and the GOP alike. Recent grumblings about the $12 billion wind power tax credit, which President Obama supports, paint the subsidy as another example of government overreach and overspending. Yet the fact remains that the wind tax credit was signed into law by President George W. Bush, and even with historically low natural gas prices, wind remains cost competitive in many parts of the country. When natural gas prices rise, and they will, wind will become a more attractive alternative.

The GOP has similarly painted solar subsidies as being supported only by Democrats, and Republicans have had a field day kicking the Solyndra bankruptcy around. While it is true that Solyndra received hundreds of millions of tax dollars, and the company contributed campaign donations to Obama, the company also received more than $1 billion in private capital from Republican and Democrat investors alike.

This fact has not kept the Solyndra case from becoming a Republican punching bag, and Solyndra is not the only solar firm that has failed recently. Take as another case in point the failure of Amonix, whose recent bankruptcy failed to attract the same level of attention from Republican pugilists. While Amonix's late CEO, Brian Robertson, donated to Senator Harry Reid, a Democrat, and the company's modest PAC funneled donations to his party, the company's single biggest government subsidy came in the form of a research and development grant awarded by the Bush administration.

Clearly Republicans and Democrats from both the public and private sectors saw the value in solar, and many, if not most, still do. The problem from the near-term investment perspective is two-fold. On the one hand, even cheaper and

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more heavily subsidized solar panels from China were dumped on the market at prices domestic firms couldn't match. On the other, natural gas prices fell through the floor as a consequence of the (temporary) glut created by the rush to hydraulic fracking—which, again, was only possible after 30 plus years of subsidies and support from both Republicans and Democrats.

In the long run, we need investment in wind and solar to be sustained just as it was for unconventional oil and gas production. In the long run, we will be rewarded.

"Drill Baby, Drill"

Rather than supporting investment in renewable energy research and development, the GOP has repeated the "Drill baby, drill" refrain, and thus talking points have inaccurately painted Republicans as "pro" oil and gas and Democrats as "anti" oil and gas. This is not only false, but it's counterproductive in that it needlessly creates division and animosity.

It will probably come as a surprise to many that the number of drilling rigs in operation has increased from 328 in January 2009 when Obama was inaugurated to 1,423 at last count. By comparison, the number of drilling rigs in operation under the George W. Bush Administration peaked at a relatively paltry 426.

It's important to understand, however, that the vast majority of rigs in operation are drilling on private land, and the offshore drilling moratorium that emerged in the wake of BP's oil spill in the Gulf of Mexico had an obvious impact on drilling activity on federally-owned offshore land. But a few points should be made here as well.

First, and most importantly, the Gulf spill shed light on a poorly regulated system, and while poor regulation was not to blame for the spill (blame falls squarely on BP's shoulders), effective regulation could have prevented the spill and the negative environmental, social, and economic impacts that the spill brought to the fishing, tourism, and related industries.

Moreover, the low number of active drilling rigs is not only due to the offshore drilling moratorium. The number of active drilling rigs has been declining for years primarily because oil and gas producers chose to drill elsewhere in the world.

Roughly 175 offshore drilling rigs were in operation when George W. Bush was inaugurated in January 2001, but during his last full month as President, only 66 offshore drilling rigs were in operation.

By March 2010, the month before the spill, the offshore rig count had fallen further to 51, and of course the moratorium caused the number of rigs in operation to drop further—to just 15 by July 2010. Since then, however, the number of rigs in operation has climbed back to 51, and is likely to continue to climb as the federal leasing system has been restructured.

This past summer, the federal government put up for lease 39 million acres in the Gulf of Mexico, and the highest bids totaled $1.7 billion. The total acreage leased (2.4 million acres) is now in line with the decadal average over the last decade, and the income earned by these bids was higher in only two other years—2007 and 2008. Looking forward, the decision has been made under the Obama administration to put up for bid another 38 million acres of federal offshore land in the Gulf next March. At this point, it's anyone's guess as to whether the bids will be tendered under a Democrat or Republican administration.

These statistics fly in the face of partisan talking points. With the exception of the temporary drop that resulted from the spill-induced moratorium, politics and regulation had little to do with the decline of drilling activity, though one might argue that the restructuring of leases has paved the way for increased activity.

A similar story is told by statistics on pipeline construction. During Bush's last year in office (2008) slightly fewer than 51,000 miles of domestic crude oil pipelines were constructed, despite the fact that oil prices had reached record highs, and the financial system had not yet collapsed. Under Obama, slightly less (55,000 miles) were laid in 2010, which is the last year that data are available.

Of course neither Bush nor Obama had much to do with these pipelines, and when pipelines are brought up as talking points, what is really being referred to is the particularly contentious northern section of the Keystone Pipeline extension. This section of the pipeline will transport Canadian Syncrude produced from oil/tar sands to Cushing, Okla., and on to refineries in Port Arthur, La., and Houston.

In the long run, we need investment in wind and solar to be sustained just as it was for unconventional oil and gas production. In the long run, we will be rewarded.

It has widely been reported that Obama rejected the pipeline, but this statement is misleading. Obama rejected an expedited plan for the northern section only, citing the need for further research into the risks associated with the particular route that had been proposed. Obama has, in fact, pushed to have the southern section approved.

But Obama is not alone in his concern over the routing of the northern section. In August 2011, Nebraska's Republican Governor, Dave Heineman, sent a letter to both President Obama and Secretary of State Hillary Clinton asking that the federal permit be denied because the proposed route traverses a critical aquifer. Here we have a Republican pleading on environmental grounds to a Democrat who has supported drilling and pipeline projects elsewhere.

The truth is that large pipeline projects are always contentious. As a case in point, in 1973, Senator Bob Dole broke with the Republican Party to stand beside then-Senator Joe Biden in opposition to the Trans-Alaska Pipeline System.

With the benefit of hindsight, it's fair to say that the Alaska pipeline has been a great success, but had there been a significant accident, our perception would certainly be less positive. But just because an accident didn't happen doesn't mean that the risk of an incident affecting the Alaska pipeline or the Keystone pipeline has been reduced to zero.

In short, we need to recognize that there is a long history of bipartisan support for important environmental regulations, funding for solar and wind energy research and development, funding for conventional and unconventional oil and gas production, and support for pipeline development to distribute natural gas and oil to end users. □

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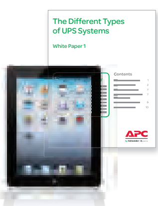

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2012 McCullough/NITL Executive of the Year

Nice guys finish first

American Trucking Associations (ATA) President and CEO Bill Graves is named NITL Executive of the Year for his leadership in shaping the nation's ground freight transportation system—not to mention his affable, endearing management style.

BY **JOHN D. SCHULZ**, CONTRIBUTING EDITOR

He's no longer Governor of Kansas, but the American Trucking Associations' (ATA) President and CEO, William Preston "Bill" Graves, still carries the dignity and political acumen of the office. Around Washington, whenever anyone talks about Graves, they rarely mention his last name, but simply the title "Governor."

Speaking quietly but carrying a truckload worth of industry knowledge and sources, former Kansas Gov. Bill Graves now leads one of the biggest and most revered trade associations—the venerable federation of 50 trade associations that for eight decades has influenced, lobbied, and educated Congress, federal agencies, and even presidents about the essentiality and operations of the $700 billion U.S. trucking industry.

The then 41-year-old Graves was inaugurated as one of the youngest governors in Kansas history in 1995. He would serve two terms, winning re-election in 1998 by the largest margin in the history of the state as a moderate Republican. In January 2003, Graves completed his second term as governor of Kansas, capping 22 years of service to the state.

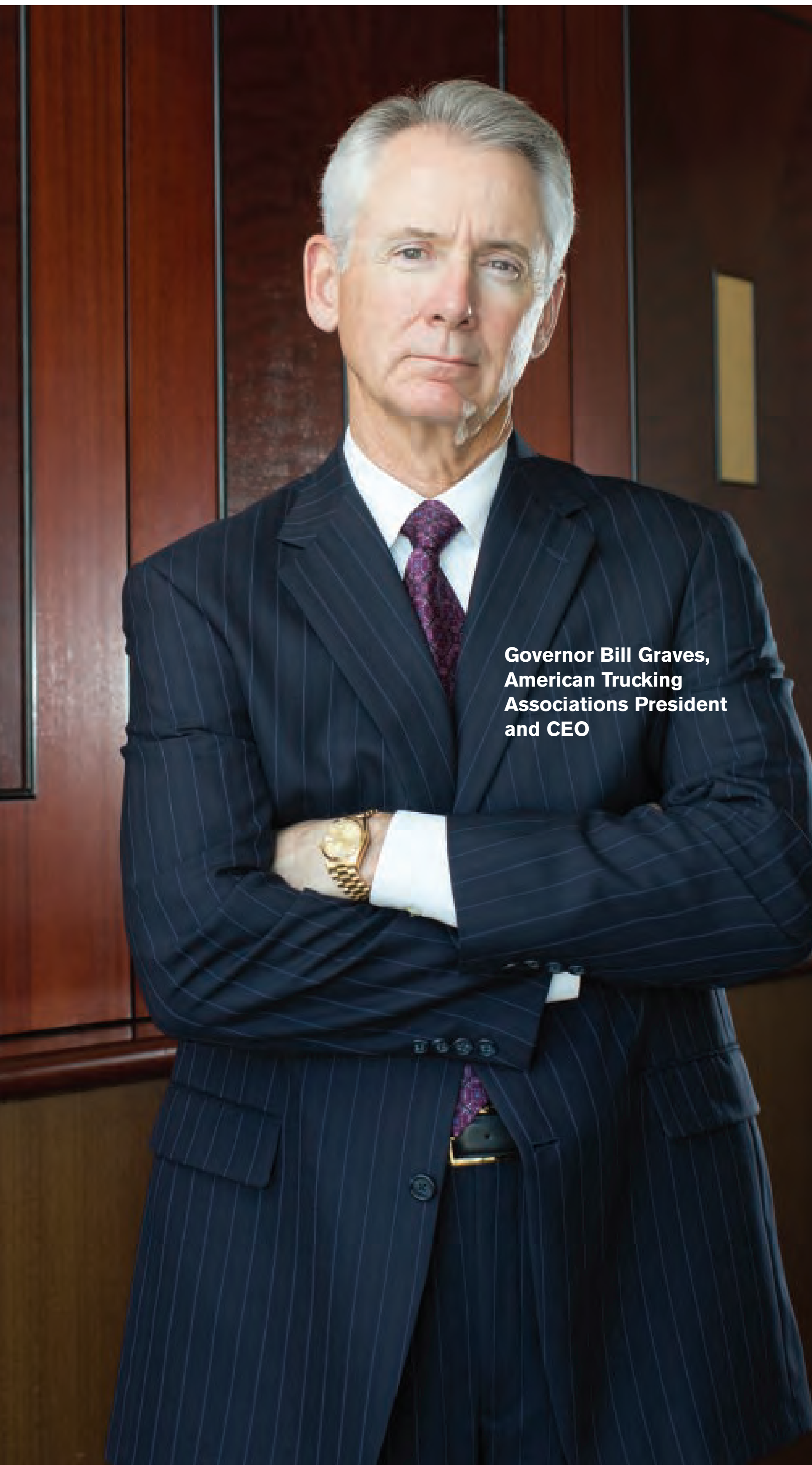
Following that experience, it seemed almost serendipitous that the ATA would turn to the affable Graves to help achieve the herculean task of representing the disparate interests of ATA's 37,000 members—ranging from $54 billion-a-year giants like UPS to thousands of small mom-and-pop truckers.

When Graves was named as the nation's top trucking lobbyist nearly 10 years ago, the appointment to ATA completed a full circle in the governor's life. His first job back in Kansas as a young teenager was working the docks at Graves Truck Line, a company his family operated for 70 years out of Salinas before succumbing—like thousands of other carriers—in the post-regulatory era following the Motor Carrier Act of 1980.

"I learned at a young age in life about work," Graves said in a recent interview in his office in Arlington, Va. "In fact, I was actually surprised the other day when I got that annual recap that the Social Security Administration sends out that gives you how many years you have been paying Social Security taxes. The first year I paid into Social Security was 1966. I was 13. So, that would have been the first year that dad had me doing something, probably sweeping the freight dock."

Besides sweeping the dock in Salinas, Graves learned a few more things along the way. Those attributes include how to treat people, how to learn from past experiences, and, perhaps most importantly, how to get along with even those with whom one may disagree.

For his achievements in guiding ATA, his impact on shaping the nation's ground freight transportation system, and, not coincidentally, his ever-polite and endearing personality, Bill Graves is this year's recipient of the National Industrial Transportation League's (NITL) prestigious Executive of the Year Award, also known as the McCullough Award. The award is named after John T. McCullough, a former chief editor of *Distribution* magazine, a predecessor of *Logistics Management*. Graves will receive the award on Monday, November 12, at the opening session of the 105th Annual Meeting & TransComp Exhibition in Anaheim, Calif.



Governor Bill Graves, American Trucking Associations President and CEO

Eli Meir Kaplan/Getty Images

"This award is about leadership," explains NITL President and CEO Bruce Carlton, noting there are certainly many outstanding and powerful people in transportation. "But leadership is a rare quality that combines a number of sometimes more subtle traits. Gov. Graves is certainly one of Washington's outstanding and powerful people, but it's his leadership skills that set him apart."

With Graves at the wheel, ATA has pushed for several safety initiatives, including a requirement that all new heavy trucks be equipped with speed limiters; a proposed national speed limit of 65 miles per hour for all vehicles; increased seat belt use; and greater drug and alcohol testing and recordkeeping of the nation's 3 million long-haul truck drivers.

ATA under Graves also supports efforts aimed at improving the safety of the trucking industry by requiring the use of electronic logs to monitor drivers' hours-of-service. And in one of the best "man-bites-dog" stories in Washington transport history, Graves and the ATA are actively pushing for an increase in the federal tax on motor fuels—unchanged since 1993—to help pay for better upkeep of our nation's infrastructure.

So far, that latter call has fallen on deaf ears in tax-averse Washington, but Graves isn't giving up so fast. Recognizing his members' wishes, ATA has also organized an effort to combat the use of tolling and public-private partnerships to pay for improvements in roads and bridges.

Graves has also pushed the trucking industry to become greener. He's overseen ATA's efforts to promote the industry's record on sustainability, ranging from support for better fuel economy standards for large trucks (coming in 2014) to promotion of the EPA's SmartWay program that recognizes truckers for their environmental improvements.

But mostly, Graves' achievements take a backseat to his warm and likeable personality. At a time when Washington politics are more cutthroat and partisan, Graves sets himself apart through his quiet nature and desire for compromise.

"My standard phrase is: 'It's OK to disagree, but don't be disagreeable,'"

he says. "Because at the end of the day we've got to work through whatever immediate problem we have. Next week and next month and next year, we have to go through a lot of other problems that are likely to confront us."

That ability to communicate through partisan waters was not lost on NITL voters in naming Graves this year's top service award. As NITL's Carlton says, "We all know people whose ego eclipses their intelligence and skills, but Bill Graves is just the opposite. Quite honestly, he is one of the finest gentlemen I've ever worked with. You sit and talk with him and he's completely self-effacing and genuinely interested in you and what you have to say."

LM Contributing Editor John Schulz had just that experience recently. Here are the highlights from that conversation:

Governor Graves discusses his life in trucking with *Logistics Management*'s John Schulz late last month.

***Logistics Management (LM)*: What influence did your father and Graves Truck Line have on you in later life?**

Bill Graves: My dad was a very hard worker in a farm family and transitioned into trucking after a stint in the military during World War II. He also developed a pretty well run trucking company in the midst of The Depression days. I learned a lot about customer service and taking care of people, and that benefitted me certainly at the ATA and the years that I was involved in the political arena.

My dad was always a giver and was always very involved in his community. He understood the importance of helping people who were less fortunate, reaching out, finding solutions, not being part of the problem. That's also been very beneficial to me, both in politics and here at ATA because we clearly have a very diverse industry. My job is to sort of keep a steady wheel and try to do what we can each and every day to help our members be more successful.

***LM:* How do you represent the interests of the entire industry given all of its diversity?**

Graves: The ability of ATA to represent our members is both our greatest strength and our greatest weakness at some moments. Our guys are very opinionated. I mean, these guys work hard every day, and they don't suffer fools lightly. And so they have definite opinions about what would be good policy for the trucking industry, and from time to time we discover that we don't agree on those things.

My job is to use some of those diplomatic skills that I developed over the years to hold everything together and try to find a path forward. And I'm very proud of the way our members have responded to some pretty tough issues. When I came here 10 years ago, the idea that we would all coalesce in supporting a fuel tax increase to fund infrastructure was probably not something you would expect. In a variety of ways, we have figured out a path forward.

***LM:* How has your experience as governor of Kansas helped you with your work at ATA?**

Graves: You have a bit more of a buffer as governor, but your job is to represent the interest of all the people you work for. Being head of ATA feels more like being a mayor or a city councilman—there's a lot more direct access with your constituents. But that's the kind of feedback I like. When the phone rings and the person on the other end has an issue, you get right to the heart of things in a hurry.

***LM:* Is your Rolodex of movers and shakers in Washington the fattest of anyone in town?**

Graves: Right now over on Capitol Hill there are a dozen individuals that I served with. Take Roy Blunt, U.S. Senator from Missouri. Roy and I were secretaries of state together back in the '80s; so I have known him now for close to 30 years. So relationships matter a lot in this town, and having been a former governor gives me some leg-up relationships.

***LM:* How has your background with Graves Truck Line helped you run ATA?**

Graves: Coming to ATA as the grandson of individuals who operated trucks, drove trucks, and ran a trucking company I wasn't considered just an outsider that was dropped into the middle of ATA. In fact, my father took me along to ATA annual meetings and events probably back when I was a teenager; so, this organization and the state associations have been part of my life for probably close to 50 years.

***LM:* Everybody I talk to compliments your style and demeanor. How would you describe your management style?**

Graves: I've never quite understood anyone who finds value in an angry or contentious or confrontational

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management style. That may serve you well for a very brief period of time, but eventually that wears people out—and it wears out your welcome. And so I have always tried to get along with people. It starts with my wife and daughter, it extends to the staff at ATA, and it certainly extends to all the members of ATA. I don't have time for the 'smallness' that I think accompanies contentious, difficult people.

***LM:* Let's get into a couple of immediate issues facing the trucking industry: It's very unusual to find an industry that is basically saying to Congress "raise the taxes," but isn't that what the trucking industry is asking Washington to do?**

Graves: I believe it's not a question of if, but when they are going to have to increase the federal fuel tax. Every day that we discuss this, a key public policymaker will say something along the lines of "well, that's just not going to happen, that's just not politically possible." We need to think outside the box and be creative. I haven't heard one person actually present a case that there is a good alternative.

There are some alternatives, but none of them are remotely close to the efficiency and effectiveness of the fuel tax to fund infrastructure. I'm confident that we'll increase the fuel tax at some point; but it will probably come at a crisis point in this country before we will wake up and do that. But we are going to keep leading the chants, and we're not going to back away until somebody shows me an alternative path forward that's better.

***LM:* Are there too many regulations in trucking right now?**

Graves: That is a great question, and it's one that, to some extent, is a difficult one to answer because we often ask the government to regulate things that affect our industry. The nature of doing business in this country today, whether you're in trucking, banking, construction, or running a restaurant, is going to involve a lot of government regulations. The goal is to try to shape those regulations in a way that they're manageable and beneficial to the industry and people we serve.

***LM:* What's the status of the hours of service?**

Graves: I don't expect anything to change dramatically. I'm optimistic that we'll be successful in our challenge to the hours-of-service rule, which principally involved the 34-hour restart provision. We're struggling somewhat already with driver shortages in this industry. Not nearly where we were in 2006 and 2007, but we think once the economy recovers, it will be a significant problem again. We just can't afford to minimize the effectiveness of those safe drivers that we have available, so I remain optimistic that we'll prevail.

***LM:* How would you describe the current financial state of the trucking industry?**

Graves: I think the state of the industry is pretty good. In a way we're not unlike the rest of U.S. business in that everyone is very cautious right now about significant investments in expansion of their operations, and a little uncertain about what is going to happen to the U.S. economy.

I think that until we see the outcomes of this election, until we have some sense of what the economy is going to do, everybody will continue to sort of sit very conservatively and be cautious about making any massive new investments or commitments.

***LM:* What was your reaction to being given the McCullough Award by the National Industrial Transportation League?**

Graves: Let me first say that I was surprised. I am obviously very honored, probably a little unworthy because there isn't anything that ATA has been able to accomplish that is not happening without all of the people that I am fortunate to be surrounded with here at ATA.

Our job is to go out each and every day and to figure out a way to take care of our customers and provide the service levels that they need. We keep the U.S. economy moving in the back of trucks each and every day, and that is something that I am extremely proud of. It's an award that I am flattered to receive. ☐

ATA decides to give it the (natural) gas

In late November, the ATA is holding its first "summit" meeting on the pros and cons of the possiblity of converting at least some of the nation's seven million trucks to run on natural gas, either in its liquid or compressed state.

One of the huge proponents of natural gas for trucking is 83-year-old billionaire T. Boone Pickens, who has been vigorously lobbying Congress and even President Barack Obama on a tax subsidy that would encourage truckers to buy new trucks that could run on natural gas.

At press time, natural gas was priced about $1.50 less than a gallon of diesel. Pickens has said that the nation will see "$6 dollar-a-gallon diesel before we see $3-a-gallon natural gas."

How optimistic is ATA President and CEO Bill Graves on natural gas as trucking's fuel of the future? "The summit has been designed to present everything from soup to nuts as to what is going on right now with natural gas and its potential for our industry," Graves told *LM*. "It's got some great upsides and potential, and it's got some unanswered questions and some potential downsides."

ATA's goal with the summit, to be held in Arlington, Va., on Nov. 28-30, is to explore that whole range of issues with ATA members and leaders in the natural gas community.

Graves says that he doesn't believe natural gas is going to be a replacement for diesel; but for an industry that is expected to consume some 55 billion gallons of traditional fuel this year, any break in the price of fuel would substantially help the industry's financial plight.

"It's not going to elbow out diesel and gasoline any time soon," Graves predicts. "But I think it's certainly exciting and encouraging for our industry that there seems to be a legitimate alternative that's available."

For more information on the ATA gas summit, visit trucking.org/naturalgassummit

—John D. Schulz, Contributing Editor

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Truckload Roundtable: Fork in the road

The foremost truckload analysts re-convene to update shippers on current supply & demand, the looming driver crisis, increasing diesel prices, the seemingly endless shifting of government regulations, and what all this means for rates heading into 2013.

BY **JEFF BERMAN**, GROUP NEWS EDITOR

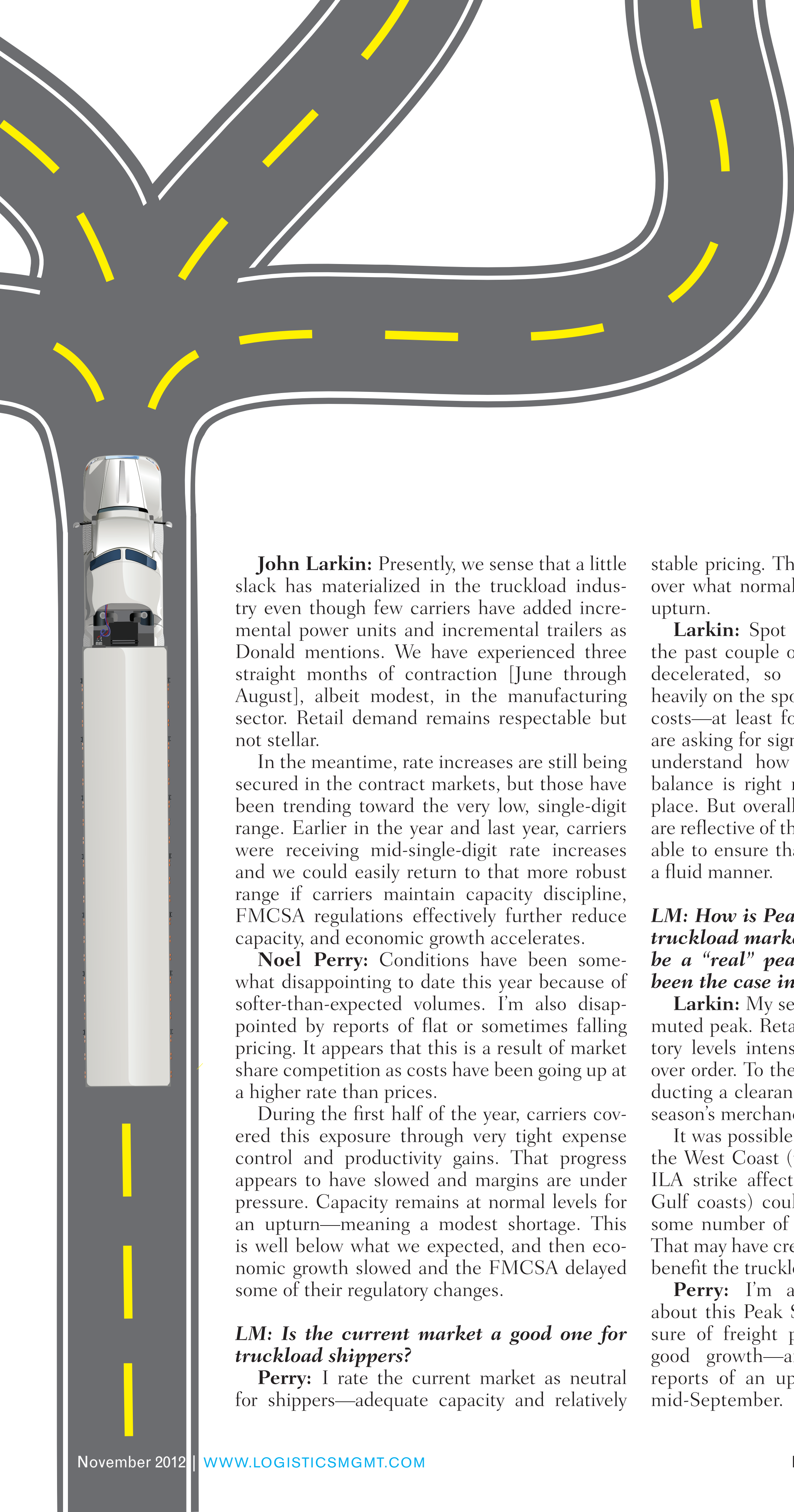
An apt way to describe the current state of the truckload market may be something along the lines of "more of the same." The issues we've been following since early in the year are still affecting truckload market conditions for shippers in late 2012: mounting regulation; rising diesel prices; the looming driver crisis; and the lingering specter of a still uncertain economic outlook.

Cautious consumers have kept demand levels relatively low, which has actually helped truckload shippers better manage capacity. While that may be a good thing in the short term, it still leaves plenty of excess truckload capacity on the sidelines. However, the cost of doing business for truckload shippers doesn't appear to be going down anytime soon.

With so many challenges on both the near- and short-term horizon, *Logistics Management* (*LM*) has invited back three of the nation's foremost truckload analysts to shed some light on the current state of the market and share what shippers should expect as we prepare for 2013. Joining *LM* are John Larkin, managing director of the Stifel Nicolaus Transportation & Logistics Research Group; Noel Perry, managing director and senior consultant at FTR Associates, a freight transportation forecasting and analysis firm; and Donald Broughton, managing director at Avondale Partners LLC, an investment banking and analyst firm.

Logistics Management (LM): How would you describe the overall condition of the truckload marketplace on a year-to-date basis in 2012 in terms of rates and available capacity?

Donald Broughton: No net capacity is being added. The rate of demand growth started strong but unfortunately has steadily weakened throughout the year—and as a result, we've had to repeatedly cut our pricing outlook. We started the year believing greater than 6 percent pricing was possible, then cut that outlook to a range of 4 percent to 6 percent, and have now dropped our pricing outlook to less than 3 percent. Anyone reporting better pricing than 3 percent is living off the increases they booked earlier in the year.



John Larkin: Presently, we sense that a little slack has materialized in the truckload industry even though few carriers have added incremental power units and incremental trailers as Donald mentions. We have experienced three straight months of contraction [June through August], albeit modest, in the manufacturing sector. Retail demand remains respectable but not stellar.

In the meantime, rate increases are still being secured in the contract markets, but those have been trending toward the very low, single-digit range. Earlier in the year and last year, carriers were receiving mid-single-digit rate increases and we could easily return to that more robust range if carriers maintain capacity discipline, FMCSA regulations effectively further reduce capacity, and economic growth accelerates.

Noel Perry: Conditions have been somewhat disappointing to date this year because of softer-than-expected volumes. I'm also disappointed by reports of flat or sometimes falling pricing. It appears that this is a result of market share competition as costs have been going up at a higher rate than prices.

During the first half of the year, carriers covered this exposure through very tight expense control and productivity gains. That progress appears to have slowed and margins are under pressure. Capacity remains at normal levels for an upturn—meaning a modest shortage. This is well below what we expected, and then economic growth slowed and the FMCSA delayed some of their regulatory changes.

LM: Is the current market a good one for truckload shippers?

Perry: I rate the current market as neutral for shippers—adequate capacity and relatively stable pricing. This is a surprising improvement over what normally occurs in the middle of an upturn.

Larkin: Spot market pricing has dipped in the past couple of months as the economy has decelerated, so those shippers relying more heavily on the spot market are enjoying reduced costs—at least for now. Few contract shippers are asking for significant rate reductions as they understand how tenuous the supply/demand balance is right now in the truckload marketplace. But overall, service remains good, prices are reflective of the market, and capacity is available to ensure that freight continues moving in a fluid manner.

LM: How is Peak Season shaping up in the truckload market? Does it look like it could be a "real" peak or more "muted" as has been the case in past years?

Larkin: My sense is that we're in for another muted peak. Retailers are watching their inventory levels intensely to ensure that they don't over order. To them, nothing is worse than conducting a clearance sale to prepare for the next season's merchandise.

It was possible that the diversion of freight to the West Coast (to protect against the possible ILA strike affecting ports along the East and Gulf coasts) could tax intermodal capacity for some number of weeks off of the West Coast. That may have created overflow traffic and could benefit the truckload industry.

Perry: I'm actually guardedly optimistic about this Peak Season. FTR Associates' measure of freight producing sectors is showing good growth—and we're getting anecdotal reports of an uptick in freight, beginning in mid-September.

Broughton: Let me put it this way: When you're supposed to meet a girl at 7 p.m. and she doesn't show up until 7:30 p.m., she's late. When it gets to be 10 p.m. and she still hasn't shown up, you've been stood up. This is October and we still haven't seen a fall surge. In my estimation, the U.S. economy is being stood up.

LM: How big of a factor is the current regulatory landscape 10 months into 2012 with CSA in effect and HOS changes looming?

Broughton: It has undoubtedly raised the cost of drivers because it has reduced the pool of qualified drivers. At the same time utilization has been hurt, which magnifies the negative financial pressure of driver pay increasing.

Larkin: Don is right. The regulatory landscape is a moving target. Trying to gauge the impact of the all the forthcoming FMCSA rulemakings, the various filed lawsuits, the ultimate implementation of CSA, and the ultimate HOS rules is one of the major challenges we face.

In an environment with little economic growth, the implementation of all these rules—including new potential rules regarding EOBRs, speed limiters, new drug testing procedures, and new procedures for certifying the health of drivers—will have only a modest impact on the tightening of supply and demand over the next few years. However, if the economy takes off and freight volume growth accelerates, we could see the "mother of all capacity shortages" by late 2013 and into 2014. Under the latter scenario, pricing could be the best we have witnessed since deregulation.

LM: What do you think the truckload market will look like 12 months to 18 months from now?

Perry: If the economy keeps growing and the FMCSA regulations negatively affect the market, things will be significantly tighter 12 months out. I am much less optimistic about 2014, a possible year for recession.

Broughton: While the current rate of trucking company failure is very low, a quarter or two of contraction in truck tonnage, of which there is a growing likelihood, could produce the largest number of trucks being pulled from the road in history.

Larkin: I'm a little more optimistic. The truckload industry, with any kind of luck, will be in great shape 12 months to 18 months from now. Supply will be tight and carriers will be able to deal only with those shippers willing to productively collaborate. Freight will be ample, enabling carriers to enhance their yields by shedding imbalanced lanes, uncooperative customers, and freight carrying noncompensatory rates.

Dedicated contracts will proliferate as shippers look to lock in capacity on driver friendly, highly repetitive lanes. Hopefully, much of the volatility will be taken out of the truckload market by then; and, of course, we will have a much better handle on natural gas powered engines by then as well. The big, well-capitalized companies will be in the best position to implement what could be a game-changing engine design, further expanding their competitive advantage vis-à-vis the smaller, often financially weaker carriers.

LM: What type of impact might the outcome of the presidential election have on the truckload market?

Larkin: Most companies in the private sector have adopted a very conservative stance as they await the outcome of the election. They aren't hiring unless they absolutely have to and aren't investing new money in capital projects unless they absolutely must. They've been hoarding cash, paying down debt, and buying their own stock.

As a result, the economy seems to oscillate between 1 percent growth and 2 percent growth, which is mediocre growth at best. Right now, by the way, we appear to be at the low end of that range. If Romney wins, then I think the private sector will be reasonably certain that tax rates aren't going up; additional regulations won't soon be put into place, an energy self sufficiency policy will soon be implemented, and Obamacare will be partially or totally repealed.

With the elimination of so much domestic uncertainty, private sector companies will start to hire and invest in long-term projects. Unemployment will decline, disposable income will rise, and more freight will have to be hauled. Given that supply and demand are roughly in balance, an acceleration in demand could create a very favorable carrier-friendly environment where shippers will be more willing than ever to exchange rate increases for capacity commitments.

Broughton: John is correct. The trucking industry can't afford another four years of Obama. Regulations have been dramatically expanded on the industry, adding to costs and hurting productivity. But perhaps as important, regulations have been dramatically expanded on the industry's customers, and that has resulted in slower rates of tonnage demand growth. It's not an accident that this administration has presided over the worst economic recovery in the post-World War II era. If Romney rolls back much of the regulation on the industry, its suppliers, and its customers, he could unleash the U.S. economy.

Perry: I have a bit of a different take. Since neither candidate has either the ideas or the courage to fundamentally address our economic issues, I see little fundamental effect from the election. It is likely that a Romney win would result in a modest reduction in the upcoming waves of regulatory changes.

Jeff Berman is Group News Editor for the Supply Chain Group

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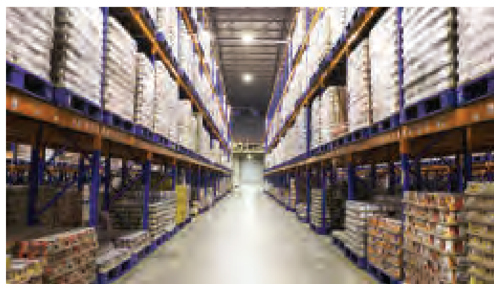

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Analysts report that cloud-based adoption increased 40 percent this year in the supply chain software sector. Our technology correspondent shares the upsides/ downsides of this deployment model—and how vendors are gearing up to meet growing shipper demand.

BY **BRIDGET MCCREA,**
CONTRIBUTING EDITOR

Ever since the term "on-demand" was used in conjunction with the supply chain software sector, an increasing number of logistics professionals have wanted to get their hands on solutions that are served up via the web on a subscription basis.

Now referred to as "cloud computing"—which is defined as the shared software and information that users access via the web—the trend permeated most software sectors as users demand faster implementation times, lower upfront investments, and less resource-intensive ways to get the programs that they need to run their businesses.

On a global scale, the worldwide public cloud services market—where services are provided "as a service" via the web with users having little or no control over the technology infrastructure—is on track to grow by 19.6 percent in 2012 to $109 billion, up from $91.4 billion in 2011, according to recent Gartner research.

And that growth spurt won't wane anytime soon. In fact, Gartner predicts that the total public cloud services market size will expand to $206.6 billion by 2016.

According to Dwight Klappich, research vice president for Gartner, supply chain management (SCM) applications have played a sizable role in the overall growth of cloud computing. Having recently wrapped up the firm's *6th Annual Supply Chain Management User Survey*, Klappich says interest in cloud-based supply chain solutions is actually growing dramatically.

Within the supply chain management sector Klappich estimates that cloud-based adoption increased 40 percent this year, compared to 2011. "And of those respondents that

we label as 'aggressive innovators,' about 30 percent say that the cloud will be their primary way of sourcing applications," says Klappich.

Breaking the growth down among the various supply chain software offerings, Klappich says that the adoption rates are highest in the areas of collaborative sourcing and procurement, demand planning, global trade management (GTM), and transportation management systems (TMS). "Two to three years ago when we talked to shippers about software, the cloud was just one option," says Klappich, who estimates that 50 percent of new implementations in the transportation space alone are now cloud-based. "In many cases, cloud has now become a preference for companies."

Steve Banker, director of supply chain solutions for ARC Advisory Group, says a recent ARC study found that just under 25 percent of TMS vendor revenues came from either public or private cloud offerings in 2011, while just over 3 percent of WMS revenues came from the cloud during the same period.

"I don't see any reason why WMS, which includes yard management services, can't be hosted by a supplier," says Banker, who adds that the presence of several niche solutions—all designed as single-instance, multi-user applications—is likely holding that part of the SCM market back from moving into the cloud at a more rapid pace.

Over the next few pages we'll examine cloud's penetration of the supply chain management space, show what vendors are doing to meet demand in this area, and discuss the advantages and disadvantages of this software deployment model.

Basics of the "cloud"

The term "cloud computing" refers to the shared software and information that users access via the web. Rather than storing information on their own physical servers or computer hard drives, users rely on servers that are maintained by the cloud computing software provider (like Apple's iCloud offering). From the user perspective, all information is stored and readily accessible online in a 24/7 format, and from various types of devices—desktop, laptop, tablet, and smartphone.

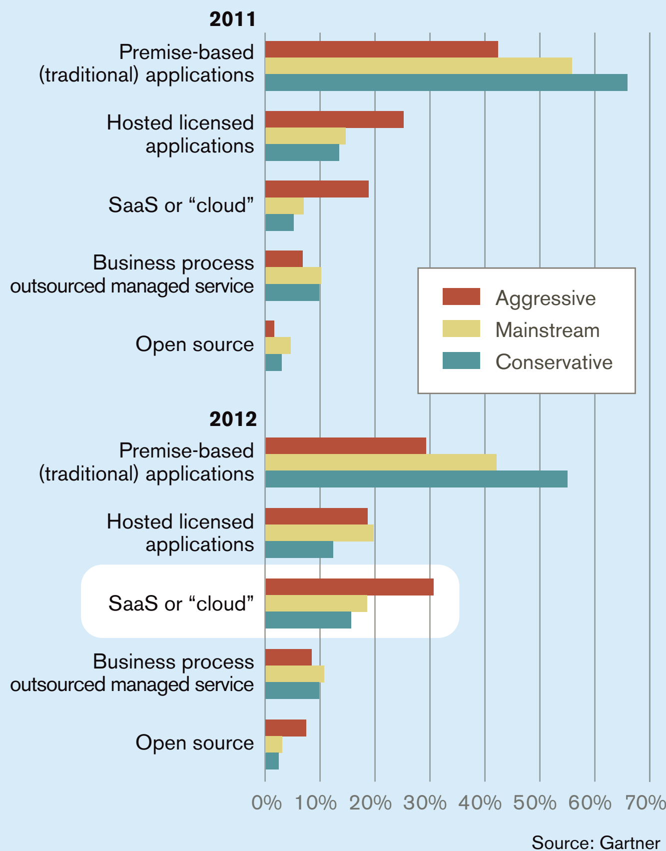
Cloud computing is an umbrella that covers both the applications that are delivered as services in a "Software as a Service" (SaaS) model via the web and the hardware and systems software (together known as the actual "cloud") used to run those applications that companies access and use online. Sometimes used interchangeably with the term "cloud," SaaS is actually the engine that provides users with remote access to web-based solutions.

There's little question that companies like the idea of having their software served up via the web. There are no servers to maintain, no IT infrastructure to set up, no upfront licensing fees, and no software programs to install and maintain on premise. And while you'll read about the cloud's drawbacks later in this article, for the most part this deployment method has garnered positive reviews among companies looking for alternatives to on-premise software models.

In fact, according to a recent CDW Cloud Computing Tracking poll, 84 percent of organizations are currently using at least one cloud application during the course of the business day. Many of those applications are accessed via

the "public cloud," where the software is offered up on a subscription basis to a wide swath of users. Private clouds, on the other hand, comprise internal datacenters for specific organizations and are not available to the general public.

Making cloud computing especially attractive is the fact that the applications are sold on a "pay as you go" model, with shippers paying only for the services that they use instead of investing in a fixed-capacity IT infrastructure that can either fall short or exceed actual needs. And because they are paid for on an ongoing basis, over time, the cloud-based solutions can be budgeted as operating expenditures rather than capital investments.



Pay-as-you-go supply chain

Some supply chain applications lend themselves to the cloud while others don't—or, at least not yet. At the highest level of the food chain, Klappich says that vendors like Oracle and SAP offer web-based ERP solutions, albeit most of those offerings are housed in the private cloud and are "typically still sold as on-premise software."

Vendors like IBM, MercuryGate, LeanLogistics, JDA, Amber Road, Logfire, Deposco, eBIZnet, Questia Web, Integration Point, and Ariba, among others, all offer some level of public cloud deployment models within their respective supply chain software sectors.

Klappich says that such offerings are particularly appealing to mid-market companies that don't necessarily want to invest in a full-blown, on-premise software installation. "The economics of paying on a subscription basis just makes it easier for these shippers to acquire software," says Klappich. Other key benefits include faster implementation times, offsite software maintenance and updates, fewer internal IT resources, and 24/7 web access from anywhere using myriad device types.

Banker adds that in most cases, shippers are drawn to lower initial investments—and the fact that they don't have to request budget or capital expenditures to make the investment. Also drawing shippers in, at least in terms of TMS, are the architectural advantages and visibility provided through the public cloud.

"We're seeing shippers with single-instance, multi-tenant solutions gain understanding of what they're paying for a particular freight lane," explains Banker, "and then using the network data—such as the fact that they're paying 20 percent more than other firms to ship freight from Chicago to New York—to establish benchmarks and make better decisions."

Not without challenges

Cloud computing also comes with its own set of challenges. Three of the most pressing questions that come up when a shipper is assessing the cloud are: Will I lose control over the data that was previously housed on my internal servers and/or computer hard drives? Will my data be safe on the web? And, what happens if there are service outages?

For shippers accustomed to being able to answer all three questions internally, the move to the cloud can be downright daunting.

"Putting information out into the nebulous world where everyone can get a hold of it is a common concern for those firms moving into the cloud for the first time," says William Kammerer, a partner with the consulting firm Accenture. In many cases, such fears are unwarranted. "A lot of companies that are running data centers are working on the same concept as the cloud, but it just so happens that they have control over the security of their data," says Kammerer, who advises logistics professionals to determine what type of access they need to their data, how they will gain that access, who else will have access to the data (business and trading partners), and what those partners can and can't do with the data before jumping into the cloud.

In some cases, the cloud itself is the answer to shippers' online data concerns. For example, the shipper looking to have its TMS datacenter online and available 24/7 must have a number of redundant systems in place. "You can either pay for and maintain that redundancy yourself, or you can take advantage of the cloud-based environment where the host will provide the redundancy and spread the cost of it across various users," adds Accenture partner Brooks Bentz.

When assessing cloud-based versus on-premise solutions, the sheer size and scope of the application itself is another issue to consider. "If you're running

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enterprise systems, it's difficult to envision how you would take an Oracle or SAP solution and turn it into a cloud-based offering," says Bentz. "Those are big, complex, customized systems that just don't lend themselves to the cloud—at least not at the present time."

"We're seeing shippers with single-instance, multi-tenant solutions gain understanding of what they're paying for a particular freight lane…and then using the network data—such as the fact that they're paying 20 percent more than other firms to ship freight from Chicago to New York—to establish benchmarks and make better decisions."

—*Steve Banker, ARC Advisory Group*

Leading the charge

Despite the unanswered questions surrounding cloud-based supply chain software offerings, adoption rates for this web-based, vendor-hosted deployment model are clearly on the upswing. "As more vendors are pressured to move into the cloud," says Klappich, "it will become the underlying operating environment for applications."

Banker says that ARC is also forecasting more growth in cloud-based supply chain solutions, particularly in the TMS sector, where online collaboration is allowing shippers to make more educated, efficient decisions. "Once you have a network in place online, in the cloud," says Banker, "you can tap into new forms of collaboration that you just couldn't access with a traditional solution based on traditional architecture."

With TMS, GTM, WMS, and demand planning currently leading the cloud-based software charge in the supply chain software space, Klappich says other applications that lend themselves to the deployment model could enter the market in the future. Still, he adds, "applications that help shippers plan, source, make, and deliver their goods, are leading the pack right now in the cloud."

Bridget McCrea is a Contributing Editor to Logistics Management

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Optimizing 3PL PARTNERSHIPS

In today's dynamic, global marketplace, shippers need to execute a checklist of essential action items in order to get the most out of their third-party logistics provider.

BY **PATRICK BURNSON**, EXECUTIVE EDITOR

When examining best practices in managing third party logistics provider (3PL) relationships, leading consultants, analysts, and educators recognize that most logistics managers begin their search with one goal in mind: to reduce cost by leveraging outsourced expertise and technology.

Naturally, one assumes that top 3PL players will provide the basic services that are now in widespread demand to achieve these goals. For example, the best 3PLs use the latest tools such as Lean and Six Sigma concept and offer the latest in warehouse management systems (WMS) and transportation management systems (TMS). And, the big players have real-time tracking and event management systems with "shipper alerts" for delays.

Shippers also expect their 3PLs to have network optimization capability to enable them to select the optimal warehouse locations. And, of course, 3PLs are relied upon for global expertise, including regulatory compliance and documentation.

However, according to our expert sources, there's more than meets the eye when it comes to managing and optimizing a 3PL relationship. According to J. Paul Dittmann, Ph.D., executive director of the Global Supply Chain Institute at the University of Tennessee, shippers also need their 3PL to take direction, respond rapidly, and generate ideas for improvement.

"Shippers further expect their 3PLs to become a strategic partner in efficiently growing their business," says Dittmann. "Today, aggressive, continuous improvement is a given."

According to Dittman, industry surveys indicate that the most important factor in establishing a successful 3PL relationship is trust—fostered by good communications between the two parties. Third party logistics providers report that their greatest challenge is finding qualified people who are dedicated to learning the client's business, and taking it to the next level.

However, in order to complete that journey, several steps must be initiated and executed. If a checklist has not yet been established, the time for creating one is now. Our experts have helped us create a list of three steps that they feel will go a long way in helping shippers fully optimize their 3PL partnerships.

1. Establish "gain sharing"

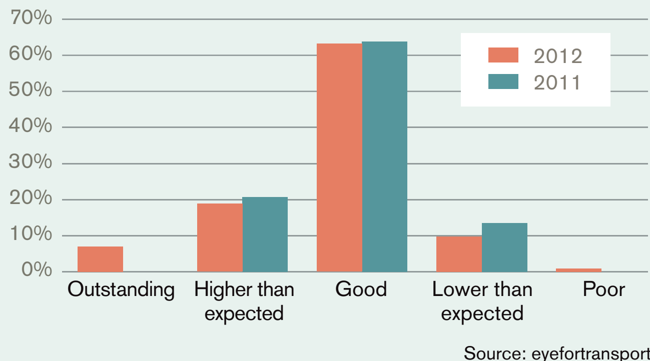
For Dittman, it's all about "gain sharing," or a mutually beneficial arrangement that is nurtured over time.

"Gain sharing is often a second phase, implemented after the relationship matures to some extent," says Dittman. "About one-third of all 3PL contacts have gain sharing arrangements. Most are based on a 50/50 sharing of cost savings, while some have an incentive payout if key performance indicators are met."

But agreeing on a method to measure cost savings against a base line is challenging, admits Dittman, and is the main reason gain sharing arrangements are not used. "Those managers that are experienced with it believe strongly that an arrangement should be initiated only after the 3PL has demonstrated that it can meet all of the performance requirements expected."

Dittman adds that once performance expectations have been met, and a good cost baseline (cost/unit shipped) has been documented, it should be possible to move forward with a plan to share 50/50 in the cost savings proposed and implemented by the 3PL. Service level credits can also be considered.

"A major variable in establishing a gain sharing formula is how to factor in normal inflation," says Dittman. "For example, if a logistics cost index goes up 3 percent and actual cost/unit stays flat, does that mean a 3 percent savings was achieved?" Dittman adds that the downside of waiting a year or more to initiate a gain sharing arrangement is that the 3PL may withhold its cost savings proposals until a gain sharing deal is begun.



2. Find a cultural fit

The vetting process is a two-way street according to John Langley, Ph.D., professor of supply chain and information systems at Penn State University. He says 3PLs carry a checklist of their own when interviewing prospective customers.

"A good 3PL will let a shipper know if they can build a long-term relationship," says Langley. "Basically, the same evaluation principles apply. Third party providers want shippers to share their operational strategies and financials with them, and they want the big picture before committing to a deal."

This includes learning about the shipper's core competencies and its labor relations, says Langley. Once that's achieved, the 3PL can align its offerings with shipper demands. "The shipper can then ask the 3PL to outline its range of operational capabilities and services," he adds. "They should define their geographic areas of strength, information technology, and their capacity for growing the shipper's business."

Langley defines this as "onboarding," or the gradual integration of cultures based on management of performance and feedback processes. He adds that a "pre-planned exit strategy" should also be put in place.

"There is delicate balance to be maintained during the initial collaboration, and if either party fails to understand the shared objective, they should part ways before the situation worsens," says Langley.

Robert Lieb, professor of supply chain management at Northeastern University, agrees, noting that most 3PL contract failures can be traced to the implementation stage.

"Remember, the deal isn't done when the contract is signed," Lieb says. "At that time it's essential that both parties are clear about expectations, responsibilities, and the metrics to be used in judging performance."

Lieb advises shippers and 3PLs to "cross-train" as part of the implementation process, thereby learning the same tactics and strategies necessary for collaboration. "Don't look at the relationship between the two companies as a zero-sum game," he adds. "And don't panic during tough times. My research has indicated that at least one-third of 3PL relationships actually improve during periods of time when the parties look at their problems and work toward resolving those problems together."

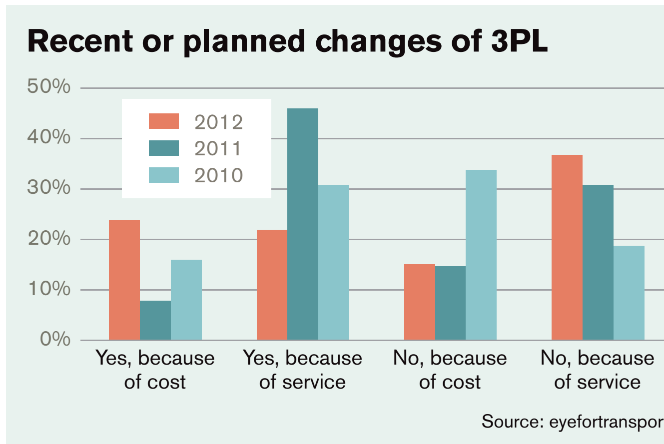
Lieb says he can't stress enough the power and benefit of strong communication between the parties: "Develop an early warning system that identifies potential problems when they first emerge and don't personalize the problems. Collectively work toward problem resolution."

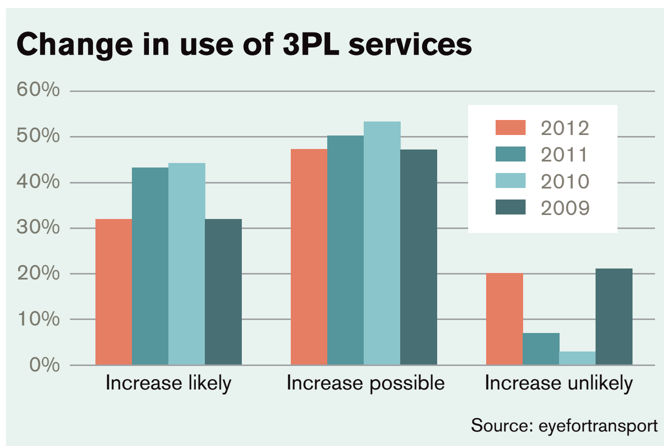
3. Implement risk mitigation

Researchers at Eyefortransport (EFT), a London-based logistics and transportation think tank, report that 3PLs are seeing their best opportunities for growth in China and North America. According to their recent report *Global 3PL & Logistics*

Outsourcing Strategy, the two regions also saw the biggest change in opinion since last year, with North America having seen the largest increase and China having seen the largest decrease.

According to Linda Conrad, director of strategic business risk management for Zurich Services, shippers doing business in China should be especially vigilant. "Productivity there can be disrupted despite an absence of physical damage," says Conrad. "Companies need to think beyond their traditional contingent insurance coverage toward supply-chain disruption, which can come from any cause."





Physical damage has not been the only cause of business disruption in recent years, according to Zurich's database of unanticipated events. Business disruptions can come from many sources, such as information technology outages, port closures, labor actions, or regulatory changes.

"Knock-on effects mean it's more important than ever to map out the value chain from end-to-end, including inter-dependencies. Companies need to ask and be aware of the triggers or drivers that would cause a risk to come to fruition," Conrad says. "Then, they need to determine what they would do to mitigate the risk or severity."

Most companies look at what they can do to respond to a crisis, which is reactive, she says. It's more important to be proactive, by coming up with preventive measures and continuity plans."

"When shippers and 3PLs are planning proactively for business resilience, it becomes a competitive advantage," she says. "Because you're back in the market more quickly than your competitors, they can benefit from a lower cost of recovery and even gain market share."

Shippers can't assume that a 3PL's *force majeure* or typical insurance policies will cover supply disruption from things such as strikes, says Conrad. If the fault is with the supplier, it's the supplier's insurance that should compensate.

"However, the supplier might be under-insured or not insured at all, and you might end up paying for claims that should have been covered by your vendor unless your own insurance covers all risks of non-delivery," adds Conrad.

The ultimate 3PL checklist contains a failsafe clause, analysts agree. When it comes to finding a 3PL, shippers need to do due diligence on the insurance they require of their suppliers so there are no gaps that leave them exposed.

—Patrick Burnson is Executive Editor of Logistics Management

Understanding the shipper dynamic

Researchers for Eyefortransport (EFT), a London-based logistics and transportation think tank, say that shippers continue to report that the service level is, by far, the most important factor in their choice of new 3PL partners. In its recent *Global 3PL & Logistics Outsourcing Strategy report*, EFT analysts note that 2012 has been a year of "shifting dynamics" for 3PLs and their customers.

"In our recent survey, we discovered that only 36 percent of shipper respondents anticipate growth living up to their predictions," says Katherine O'Reilly, EFT's executive director. Furthermore, she says, fewer shippers (32 percent compared with 43 percent in 2011) expect to increase their use of 3PLs.

According to EFT, the new report went beyond the scope of previous years' to focus on the needs and challenges of 3PLs and their customers—and the changing relationship dynamics between them. The results paint the picture of an industry in transition, one that's still rocked by the events of the past few years, but ready to re-emerge with new shipper "checklists."

"We are looking at an industry that is coming together to face challenges head on," says O'Reilly. "And those who best understand the market will be set to prosper in the upturn."

She also observes that 34 percent of 3PLs now report that they have a customer advisory board, and continue to raise the level of priority of customer engagement. Still, 3PLs are tasked with keeping their future promises within "realistic expectations."

Other key findings from the report include:

• Shippers rated the performance of 3PLs in a similar manner to last year, with a slightly larger number rating their 3PLs as "outstanding."

• Last year saw most shippers who changed 3PL providers doing so as a result of service issues, while this year saw results split between cost and service.

• Thirty-two percent of shippers anticipate an increase in their use of 3PL services, though this represents a reduction from the 43 percent who responded as such last year.

—Patrick Burnson, Executive Editor

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How the leaders global trade

are tackling management

As supply chains become more complex and the number of overseas suppliers expand, global trade management has assumed critical importance. How are the leaders managing supplier relationships, data integration, and compliance challenges in this increasingly tough global arena? A new chief supply chain officer study from the Aberdeen Group provides some answers.

BY BOB HEANEY, ABERDEEN GROUP

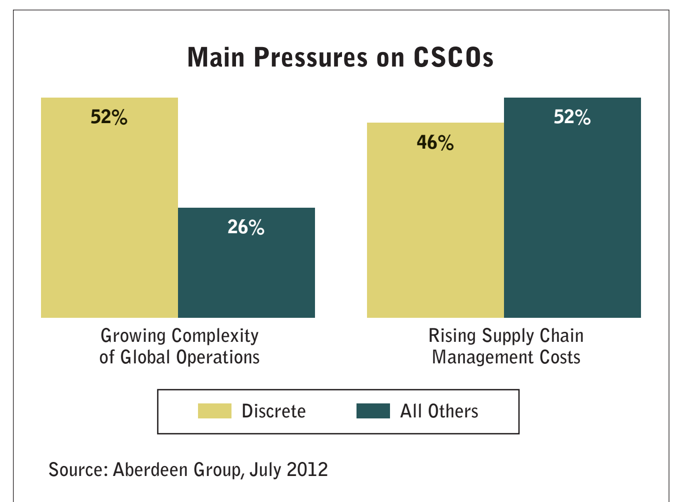
Aberdeen Group's *Chief Supply Chain Officer (CSCO) Survey*, conducted in July 2012, collected data from 191 companies. That survey revealed that the increase in the number of suppliers, customers, carriers, and countries of trade is changing the importance of collaborative synchronization between all parties in the multi-tiered global supply chain. As a result, we're seeing a growing shift in focus towards collaboration and global trade management (GTM) with suppliers and trading partners.

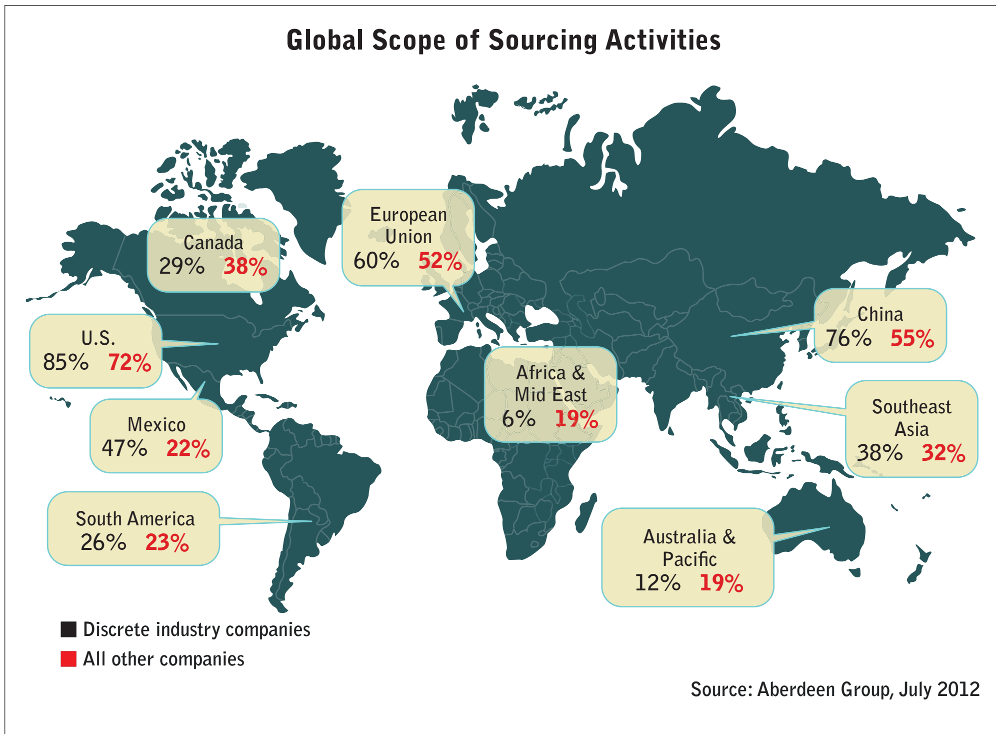
The insights in this article will focus on an important segment of that research sample—the 69 companies in discrete manufacturing industries. In particular, we examine the key process and technology differentiators displayed by the chief supply chain officers in these companies to improve visibility to supplier/partner/customer product flow across an increasingly global, multi-tier, and cross-channel distribution network.

Complexity overtaking the supply chain

Our CSCO study found that the top business pressures facing the discrete segment are the impact of increasing supply chain complexity (that is, longer lead times and lead-time variability, or increasing numbers of suppliers, partners, carriers, customers, trade countries, logistics channels) and rising supply chain management costs (for example, total landed costs, fuel costs, labor costs).

Globalization, global trade, and offshore sourcing are on the upswing as the overseas supplier base grows relative





to a given company's home country. Three quarters of the companies in the discrete segment report having suppliers in China and 60 percent indicating suppliers in Europe. Fully 90 percent of discrete companies in this study have imports or exports, compared to only 38 percent for the others. Other key findings regarding the discrete companies compared to the other respondents include:

• 84 percent of discrete companies are importing vs. 74 percent for others.

• 88 percent are shipping domestically vs. 74 percent for others.

• 83 percent are receiving domestic shipments vs. 64 percent for others..

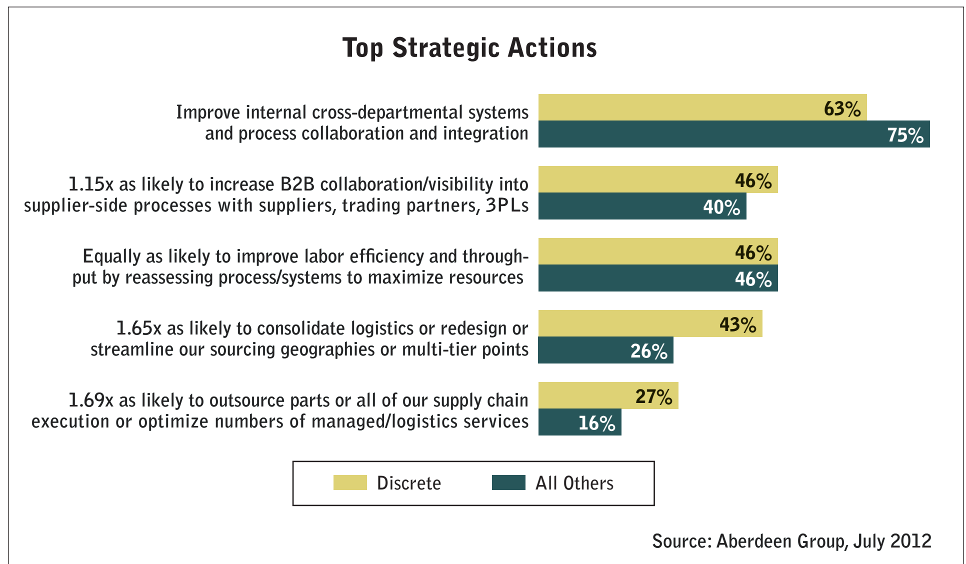
Top supply chain strategic actions

The graph to the right compares the top strategic actions that discrete and other industry segments are pursuing to alleviate the pressures associated with globalization and supply chain cost or complexity. Top among these strategies is internal collaboration, as companies struggle to synchronize and integrate data across various management systems and internal groups. This strategy of multi-party, multi-enterprise collaboration in GTM has held fairly constant during the last year.

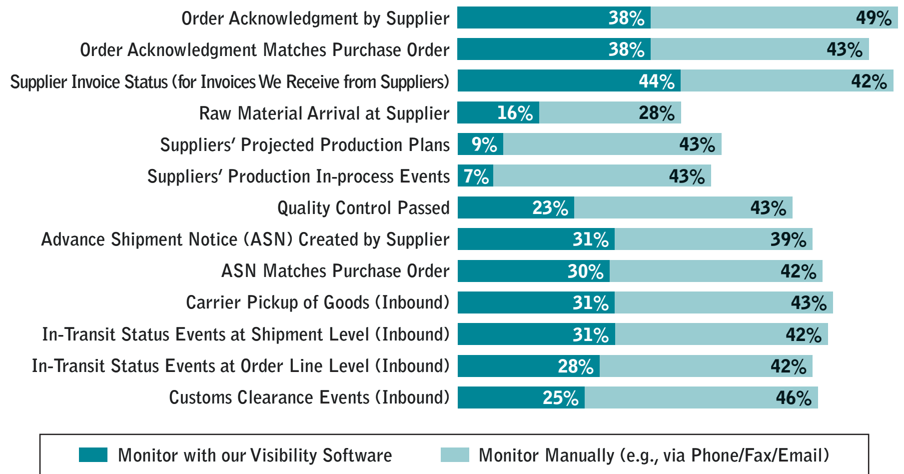
All companies need internal collaboration to operate; however, the level of external collaboration and its relevance grows with the degree of overseas sourcing and global trade. Consistent with the level of overseas sourcing, the discrete segment is more than twice as likely as the others to be pressured by the growing numbers of supplier, carrier, and trading partners.

Not surprisingly, when it comes to strategic actions the companies in the discrete group desire higher levels of control and coordination with the external parties they depend on. For example, they are 1.65-times more likely than the others to "consolidate or redesign sourcing geographies across multi-tier points" and they are 1.69-times more likely to outsource, optimize, and manage logistics services providers.

Discrete and process industries alike are hoping to address the rising costs with more seamless systems and process flows—both within their own company and with their extended multi-country, multi-party supplier base.



To gain visibility and address this complex, multi-party global supply-and demand GTM challenge, we see that the discrete companies are more focused on "B2B collaboration/visibility" with suppliers, trading partners and 3PLs. Consistent with this priority, the vast majority of discrete companies (88 percent of those in our survey) indicate they have plans to invest in new supply chain visibility platforms. The intend to connect them to GTM processes and technology within the next 12 months to drive Return on Investment (ROI) success.



Synchronization of process steps: inbound to outbound

The global landscape is changing and the new priority for the office of the CSCO has shifted to supply-and-demand synchronization across each linked process step in the extended global supply chain. In a March 2012 study, we explored the level of capability the average company has when it comes to coordinating information and synchronizing operations across these process steps from source to end consumer.

As part of the CSCO survey we plotted the degree of automation from the 183 companies mentioned across the Best-in-Class (top 20 percent of aggregate performance scorers), Industry Average (the middle 50 percent of aggregate performance scorers), and Laggards (the bottom 30 percent of aggregate performance scorers). Looking at the best-in-class, for example, we identified the following performance levels:

- 96 percent of orders delivered complete and on time.
- 96 percent of orders received from suppliers complete and on time.
- Decreased by 3 percent the total landed costs per unit.
- Decreased by 3 percent supply chain costs relative to revenue.

Examining these companies across 21 key inbound-to-outbound process steps we can better understand process weaknesses and isolate potential areas of improvement for the office of the CSCO. As we discovered in prior studies, companies of all sizes and classes are hampered in their ability to track, monitor, and synchronize supply chain process steps with trading partners. Generally, only about 30 percent of companies have automated data and event monitoring and/or have optimized process capabilities in place. From source to destination, the 13 inbound process steps or milestones needed to synchronize product and information flows are still being monitored manually (phone, fax, and email) in up to 49 percent of all companies.

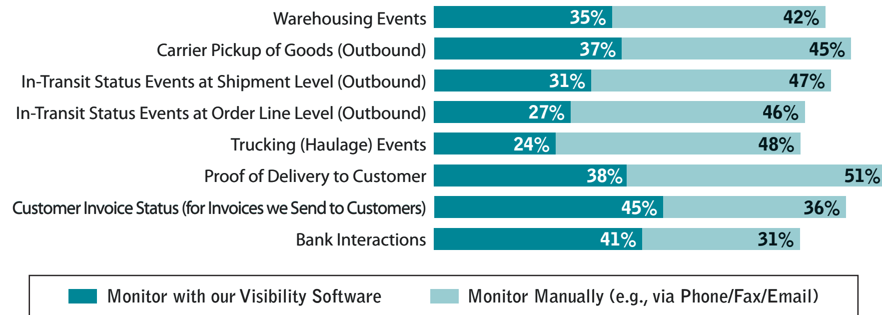
The good news is that leading companies have superior financial and service metrics and are several times as likely as their peers to automate many of these events. For instance, compared to the Industry Average and Laggard companies combined (all others), the Best-in-Class are more frequently measuring and automating events for inbound:

- **Suppliers' projected production plans**—Best-in-Class are 1.42-times more likely to track than all others (68 percent of the Best-in-Class monitoring this milestone).
- **Customs clearance events (inbound)**—They are 1.34-times more likely to track than all others (90 percent of the Best-in-Class monitoring this milestone.
- **In-transit status events at order line level (inbound)**—Best-in-Class are 1.34-times more likely to track than all others, with 87 percent monitoring this milestone.

On the outbound side (Page 50) eight additional linked process steps are plotted and the picture is almost identical. In the typical sequence of event flow (i.e., outbound from shipment/pickup to proof of delivery and settlement), the degree of visibility/collaboration and automated monitoring and control ranges from 24 percent to 45 percent (blue bars). So across warehousing, pickup, outbound transportation/delivery, and payment, anywhere from 28 percent to 49 percent of respondents claim they are still manual (phone, fax, and email).

Once again the good news is that leading companies are performing better and are several times as likely as their peers to automate many of these events. For outbound compared to

Outbound Process Steps from Receiving to Customer Delivery and Payment



Source: Aberdeen Group, July 2012

all others, the Best-in-Class from the study are more frequently measuring and optimizing:

- **Trucking (haulage) events**—1.24-times more likely to track than all others (84 percent of the Best-in-Class monitoring this milestone).
- **In-transit status events at order line level (outbound)**—1.20-times more likely to track than all others (84 percent of the Best-in-Class monitoring this milestone).

Capabilities for global visibility and GTM

So far, we have we discussed the growing interest in GTM, supply chain visibility, and collaboration platforms in the extended supply chain in response to globalization and rising supply chain costs. Let's now dig deeper into the visibility aspect.

Aberdeen's *2012 Chief Supply Chain Officer Study* reveals that 78 percent of executives surveyed said that improving extended supply chain visibility was a top priority. But this requires integration—bringing together best practices and integrating global trade process improvements with the technology available in the market today. It also requires a focus on performance management and automation. In the following sections we explore the capabilities that the leaders have in these key areas.

Performance Management/ Knowledge Management: When KPIs related to global trade compliance (GTC) are embedded in management objectives from the chief supply chain officer down, it drives performance. In the chart on page 48, we saw the relative importance of enabling internal staff and management teams to "collaborate" behind the GTM program and initiatives. But performance management extends beyond the internal organization and becomes extremely crucial in the extended collaborative supply chain. Again, it is not surprising that the Best-in-Class are both measuring more comprehensively and extending performance management to their vendors or suppliers.

- At 80 percent, the Best-in-Class are 1.6-times as likely as all others to support vendor enablement with process and technology (a performance management focus). They are more capable of accessing and integrating with freight forwarders, carriers, and brokers as well as measuring and monitoring their real-time performance.
- At 65 percent, the Best-in-Class are 1.4-times as likely as all others to support cross-functional cost, metrics, and reporting provided to management on a regular basis. This capability from a knowledge management standpoint allows management to assess the performance of their internal and external teams.

Compliance Management and Automating Trade-Related Knowledge: Having near real-time access to the latest trade related content is very important. Even a 10 percent improvement can lead to superior performance. Frequent and accurate updates on security regulations, tariffs, restricted party lists, and other trade-related information are needed for fast and effective trade compliance management. About half of all respondents have adopted or developed automated software tools to obtain such content.

Likewise, the degree of automation is another differentiator across all classes. "Automated" companies are 3.44 times as likely as the "mostly manual" companies to have automated customs entry validation or audit. Similarly, they are 3.5-times as likely to automate supplier enablement, whether manufacturer or distributor (e.g. electronic interface or integration via EDI, XML, portal, and SaaS). Having timely access to accurate trade data and then being able to proactively execute for exception management is one of the fundamentals to successful GTC/GTM management.

GTC and GTM generally lag behind other more generic supply chain software (such as supply chain visibility, transportation management systems, or labor management systems) as to the level of "manual" functions vs. automated. Sixty-seven percent of all companies in this study report that some components of their overall GTM/GTC technology solution involve manual trade compliance practices, with many hybrid and fragmented automation efforts for certain processes reported.

While a given component of technology like ERP may be adopted at fairly equal levels across all companies, there is generally a wide variety of disparate systems, including in-house custom solutions, that in aggregate make up the overall GTM/GTC system. Indications are that this will continue to be the case. Today's multi-enterprise supply chain is evolving

and well over 60 percent of companies indicate that they intend to continue to incorporate collaborative tools to help seam together legacy, ERP, BI, SC visibility, and GTM needs and become more automated.

We've identified the following main levels of global trade management technology maturity as reported by respondents (in ascending order of automation):

- "Mostly manual" and spreadsheet driven (25 percent).
- Fragmented IT approach (28 percent).
- Departmental level automation (15 percent).
- Some end-to-end and cross-functional process automation (23 percent).
- Highly automated (9 percent).

The Advantages of Automation

Our research reveals significant gaps between automated companies (those with some or high levels of automation) and their "mostly manual" counterparts on key GTM activities.

Specifically, the automated companies are:

- **3.5 times as likely to automate supplier enablement—manufacturer or distributor (e.g., electronic interface or integration via EDI, XML, portal, and SaaS).**
- **3.44 times as likely to automate automated customs entry validation or audit.**
- **3.42 times as likely to automate cargo and asset tracking (e.g., GSM and satellite network) globally.**
- **3.35 times as likely to automate proactive and automated monitoring and resolution of GTM exceptions and service disruptions.**
- **3.15 times as likely to automate vendor enablement—forwarder, carrier, broker (e.g., electronic interface or integration via EDI, XML, portal, and SaaS.**

Benefits explored: The Impact of process automation on metrics

Aberdeen Group in this report defines "automated" companies as those with some cross-functional automation or a high level of automation (compared to those with "mostly manual" process automation). As the sidebar shows, these are some fairly dramatic automation advantages across these two groups. But do these automation gaps result in superior metrics? The automated companies have delivered superior gains as follows:

- Automated companies had an annual average improvement in effectiveness of 9.07 percent vs. 3.67 percent for the "mostly manual" companies. The trade compliance functions included in this metric are balanced across reduced supply chain risk and/or costs, increased staff productivity/effectiveness, or improved trade relations with government or trading partners.
- The productivity of the trade compliance staff vs. the prior year improved for automated companies by 25.88 percent compared to just 9.81 percent for those that are mostly manual.
- The number of supply chain disruptions (on import/export shipments) due to trade compliance errors vs. the prior year decreased for automated companies by 4.29 percent compared to a 1.03 percent increase for the mostly manual.
- Companies with automated processes for restricted party screening are 35 percent more likely to have maintained or decreased government fines for noncompliance vs. the prior year.

Of the 69 discrete companies, 51 are planning to either invest in or enhance their capabilities in the areas GTM and GTC to be "more connected and automated".

The real challenge in selection is aligning the right technology/solution to each operation's specific need or operating profile—and then ranking the cost/benefit analysis for all the competing options and to evaluate the relative payback each choice may yield.

While global trade management and global trade compliance vary radically from one supply chain to the next, there is broad consensus (up to 78 percent of CSCOs) that these areas are ripe for renewed investment in the next 12 months. However, each company has different operating profiles and requirements. And these always should be matched

to the solutions that best fit their current operating needs.

Three recommendations for success

As companies go global and increase the numbers of trading partners, the need for collaborative integration with external parties is certainly going to intensify and raise new challenges for supply chain leaders. As the degree of global collaboration grows—and global supply chains become more complex—it is likely that visibility systems and global trade platforms will increase and, as Aberdeen predicts, gain added popularity. All of these trends give evidence to the growing complexity and multi-tiered nature of today's supply chain.

As illustrated by our research specific to supply chain visibility, the top performing companies are most successful in integrating their people, process, and technology. Those successful in this threefold integration are gaining a more end-to-end and close-to-real-time visibility of their supply chain operations and across the multi-tier supplier base. In that visibility research report, Aberdeen makes the following point: "Companies of all maturity groups have varying levels of supply chain visibility. Numerous event and product flows—on inbound and outbound, SKU, container, order, lot, and package level—across dimensions of both cost and service, are being monitored in the course of supply chain execution. It is important that a standardized and structured system roadmap is developed to integrate these system events and data flows as companies bring online new capabilities and new event tracking."

Although most companies and supply chain leaders recognize the importance of effective trade compliance in reducing fines and penalties as well as overall risk, few have understood the true value of GTM and GTC in reducing end-to-end costs. We offer three key recommendations for all companies on their journey to reduce costs and risks in a complex global supply chain to achieve Best-in-Class performance:

1. Improve core processes and leverage automation in global trade management and global trade compliance.

2. Establish or renew the corporate focus on a formal GTM program and ensure alignment with all applicable trade regulations to gain full management buy-in

3. Use GTC knowledge and analytics in company-wide sourcing, purchasing, and supply chain network design decisions to significantly restructure and enhance those activities. (For example, consider special provisions like preferential trade agreements, free trade agreements, and so on, in periodic strategic plans).

There is no one answer for a successful GTM/GTC program. It is a combination of excellence in the areas of access, enablement internally and externally, process/technology, and proactive planning and execution. Most companies are leveraging managed services and collaborative technology beyond the enterprise and are seeking to be more "connected and automated." When these elements are aligned, in proper combination, they yield superior results.

As companies adapt to the globalization of their supply chains, these recommendations and guidelines can equip supply chain executives with actionable steps they can take to bolster performance and address each challenge. Further, this information can enable synchronization of both planning and execution across the multi-party extended demand-supply network. For more information on this or other research topics, please visit www.aberdeen.com.

There is no one answer for a successful GTM/GTC program. It is a combination of excellence in the areas of access, enablement internally and externally, process/technology, and proactive planning and execution.

More Details on the CSCO Survey

Between June and July 2012, Aberdeen examined the use, the experience, and the intentions of more than 191 enterprises regarding their supply chain executives' priorities. From this overall group, 69 companies from the discrete industry segments were analyzed specifically for the purposes of this document.

Aberdeen supplemented these online survey efforts with interviews with select survey respondents, gathering additional information on supply chain executives' strategies, experiences, and results.

The executives sampled represented the following departments or functions: supply chain or logistics manager (43 percent), procurement (11 percent), operations manager (7 percent), senior manager (11 percent), sales and marketing (9 percent), and IT management or staff (14 percent). A range of industries were represented in the sample.

In the discrete organization segment, 47 percent of the companies were large (greater than $1 billion), 30 percent mid-size ($50 million to $1 billion), and 23 percent small (less that $50 million). The majority of respondents (62 percent) were from North America. The remaining respondents were from Europe (20 percent) and Asia/Pacific region (18 percent).

Bob Heaney is Senior Research Analyst, Supply Chain Management at the Aberdeen Group. He can be reached at bob.heaney@aberdeen.com.

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SUPPLY CHAIN MANAGEMENT REVIEW

FEATURES

8 The Supply Chain Top 25: Leadership in Action
The 2011 rankings of the Top 25 supply chains from Gartner Inc. are in. They include repeat winners and some new entrants. Perhaps even more important than the actual rankings, says Gartner Research Director Debra Hofman, are the lessons that can be learned from analyzing the leaders. This year, six specific qualities stand out.

16 The Greening of Walmart's Supply Chain...Revisited
In 2007, *SCMR* ran an article on Walmart's sustainability program, focusing on eight specific initiatives being pursued. Four years later, the author of that original article, Erica Plambeck of Stanford, and colleague Lyn Denend revisit those initiatives to assess just how Walmart is doing on the sustainability front.

24 Achieving Flexibility in a Volatile World
A new global survey from PRTM confirms the importance of operational flexibility in supply chain success and identifies five levers that leaders employ to make it happen. The consultants report that the financial and performance advantages of improved flexibility can be profound. They outline five basic steps that companies can take to start realizing those benefits.

32 What's Your Mobility Index?
Mobile devices are everywhere these days. But what's the real potential of mobility in the key supply chain processes. And what's the best way to identify and tap into that potential? Sumantra Sengupta of EVM Partners says the first step in answering these questions is to carefully determine your "Mobility Index." This article tells how it's done.

40 The Case for Infrastructure Investment: Lessons from Medco and Staples
Smart investment in supply chain infrastructure—and in particular automated materials handling and distribution systems—can pay big dividends. Medco and Staples have proven that convincingly, as these case studies demonstrate. Their stories point to seven key takeaways that supply chains professionals in any business sector can learn from.

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S50 EU Logistics: Meeting the New Challenges

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2012 Warehouse/DC Operations Survey:

Mixed signals

A record response reveals that *Logistics Management* readership is divided in terms of investment: one side remains cautious, while the other is on the verge of making significant changes to their warehouse/DC operations.

BY **MAIDA NAPOLITANO**, CONTRIBUTING EDITOR

After years of slow economic progress, the results of *Logistics Management*'s (*LM*) 2012 *Warehouse and Distribution Center (DC) Operations Survey* show that there appears to be two schools of thought emerging from the ashes: There are those companies that remain cautious, staying conventional with minimal plans for expansion, and there are those on the verge of making significant investments and changes to their distribution operations.

Designed to gauge activities and trends in warehousing and DCs, *LM*'s annual survey offers a first-hand look into the state of today's DC and warehouse operations. In September, a survey questionnaire was sent via email invitation to *LM* readers. The survey gleaned 805 qualified responses (a new record for this survey) from upper-level managers to CEOs—all personally involved in decisions regarding their company's warehouse and DC operations.

Most participating companies came from manufacturing (44 percent), followed by distributors (28 percent), third-party providers (9 percent) and retailers (8 percent). An assortment of products handled in the DC was once again well-represented with food and grocery leading the pack at 11 percent, followed by industrial/chemical at 10 percent, and electronics and building materials, tied for third, at 8 percent each.

This year's findings revealed mixed signals coming from opposite ends of the spectrum. About 52 percent of respondents are adopting a more cautious approach, spending less than $250,000 for warehousing equipment and technology in 2012.

"That's a predominant statistic," says Norm Saenz, senior vice president and principal of TranSystems, a supply chain consulting firm and our partner for this survey. "It supports how tough economic times have controlled spending to less than $250,000 for a majority of respondents. That's only good for minor improvements to operations, such as racking or the purchase of a lift

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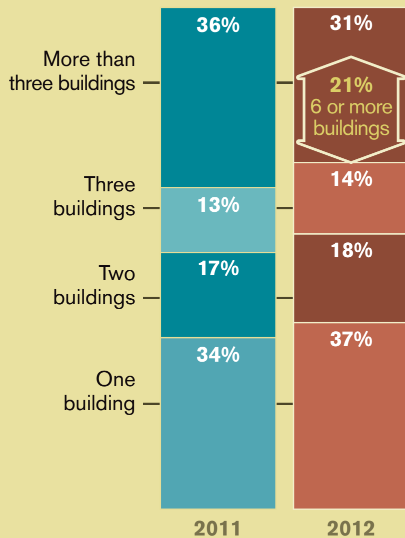
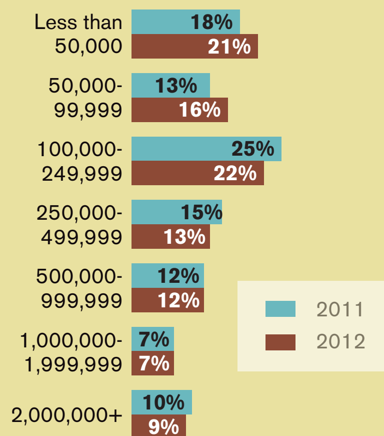
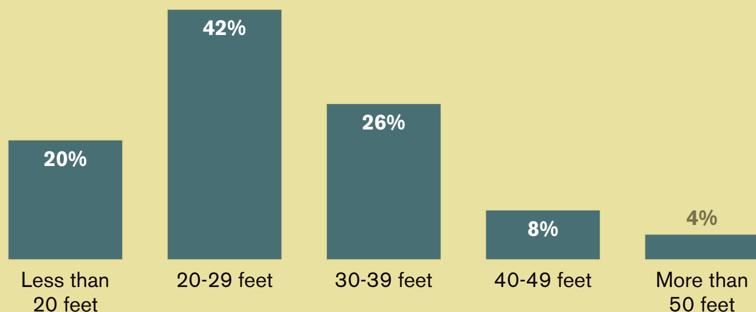
Thursday, November 29 @ 2:00 pm ET

Size of distribution center network







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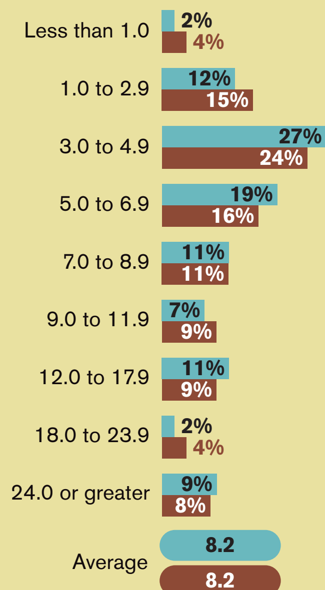
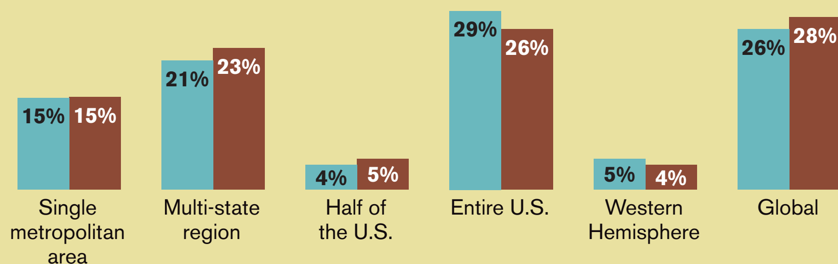
Scope of distribution center operations



2011
2012



Source: Peerless Research Group (PRG)

truck, versus opening a new facility or implementing new technologies."

However, Don Derewecki, senior management consultant also from TranSystems, prefers to focus on the other end of the spectrum: those 17 percent of respondents who are spending $1 million or more this year, and another 16 percent who are planning to spend that same amount next year.

"That's for significant projects—an indicator that companies are doing more than just replacing worn out equipment," says Derewecki. "These stronger companies have diligent managers who have probably been continuously shaving points off their operating costs over the past few years. By now all the low hanging fruit is gone, so they're starting to get more aggressive and finally looking to squeeze the trigger on investments in mechanization and automation."

Over the next few pages, we'll dig into the high-level findings of the *2012 Warehouse and Distribution Center (DC) Operations Survey* to share more detail on how the warehousing and distribution landscape has changed over the past year. We've updated portions of the survey to capture emerging trends while continuing to track the critical measures of warehousing activities that we've charted over the past six years. Let's see how your operations compare to what your peers are doing inside the four walls.

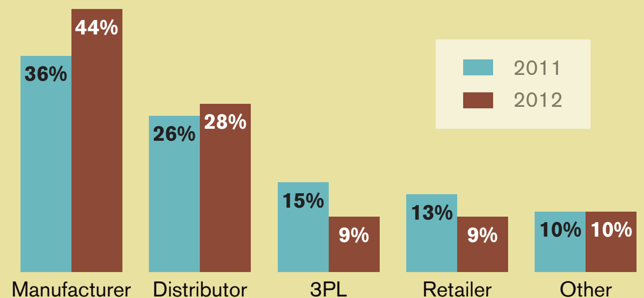
What's trending?

Despite the mixed signals, there's one clear conclusion that both Derewecki and Saenz derived from this year's survey: Corporate is making its presence felt inside the warehouse and DC.

"There's an increasing recognition of the importance of the supply chain and how much money is being spent on it," says Derewecki. "Corporate managers have become increasingly focused on the details that make the difference, even at the DC level."

According to Saenz, this fact is never more evident than in the number of respondents who say they're using their enterprise resource planning (ERP) system's warehouse management system (WMS) functionally in the DC (27 percent)—twice the number of respondents using best-of-breed WMS (13 percent). "Corporate does not want to play around with expensive

Type of business



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WMS packages," speculates Saenz. "They made a commitment to use an ERP system, so they want to use everything these systems can offer—even though it may not be the best thing for the warehouse."

Derewecki agrees, adding that the WMS being offered today by the big ERP players "isn't as bad for the warehouse as it used to be." He says that 10 years ago some of his clients were forced to use ERP at the DC level because corporate wanted everyone to integrate with the company's ERP system. "All of the functionalities that managers used to have with their standalone WMS just weren't there," says Derewecki. "In some cases, they had to switch back to more manual operations." But these days, he adds, developers have significantly improved the functionality of ERP's WMS packages.

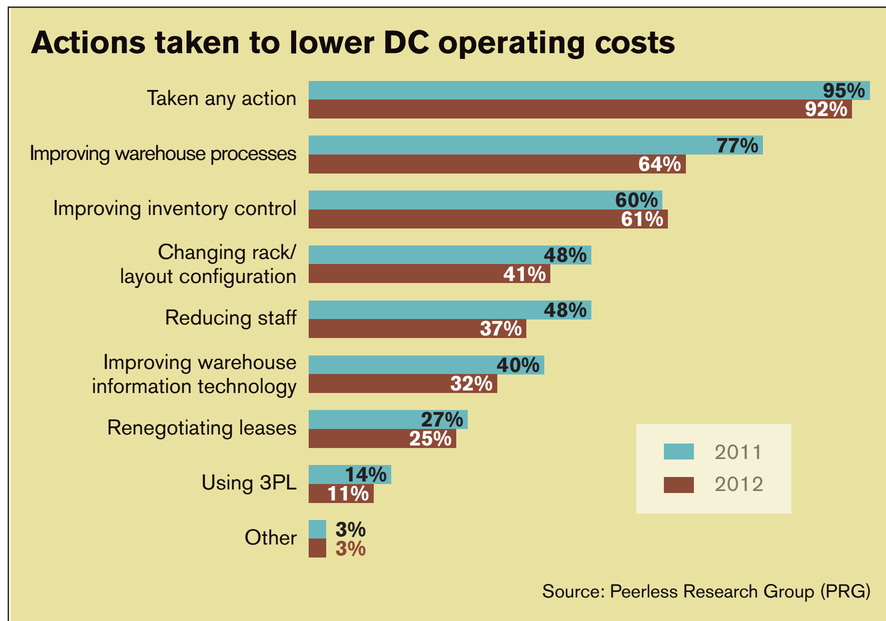
"As more companies run their businesses with an ERP system, it's easier and less costly to simply use that ERP's WMS," adds Saenz. "I think this is a trend that's going to continue."

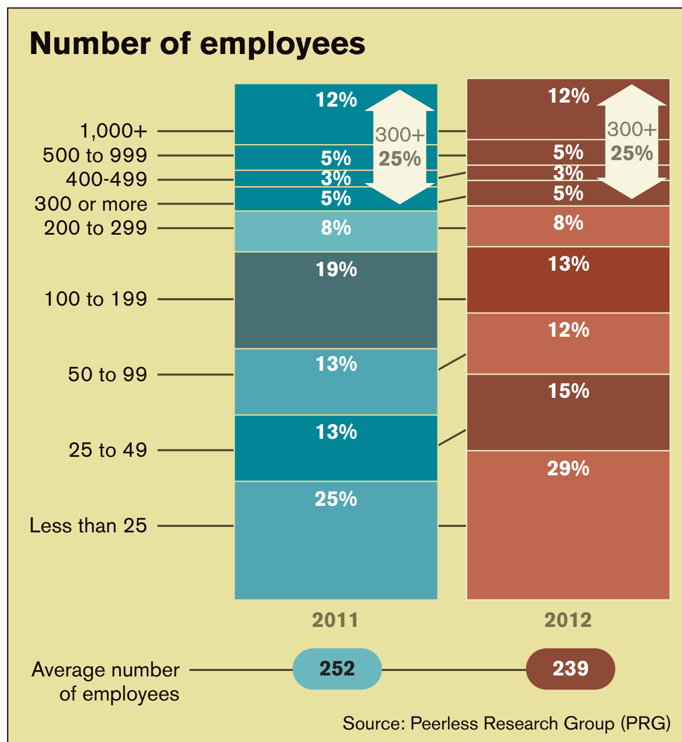
There's also a trend towards a more consolidated network. Since 2010, the percentage of respondents with three or fewer buildings has been steadily increasing, while the percentage with four or more buildings has been steadily decreasing. Saenz believes that it's all part of a continuing push by companies to do more with less.

"However, with fewer facilities, you may achieve savings in operating costs, but you may be potentially increasing your freight," Saenz cautions. "This is not a particularly good move with today's inflating gasoline prices."

Even more mixed signals surface from this year's findings. While some networks may be contracting to fewer facilities, about 60 percent of respondents are planning to do some sort of expansion this year. Twenty-six percent are increasing their number of SKUs, and 25 percent are increasing the number of employees.

Despite these plans for expansion, average inventory turns have not improved and remain steady at 8.2. Derewecki offers a possible explanation: "At many companies, in spite of the emphasis on inventory control and the improvement in information systems tools, the proliferation of SKUs has prevented the overall turn ratios from improving."





The multi-channel effect

For the first time, we decided to track how companies use market channels—or how they make product available to their customers.

Most of the respondents (84 percent) report servicing more than one channel: 67 percent report shipping to wholesalers; 57 percent to retailers; and 29 percent are e-commerce based, shipping products directly to customers.

"I would be most interested in tracking e-commerce penetration over the coming years," says Derewecki. "It seems that

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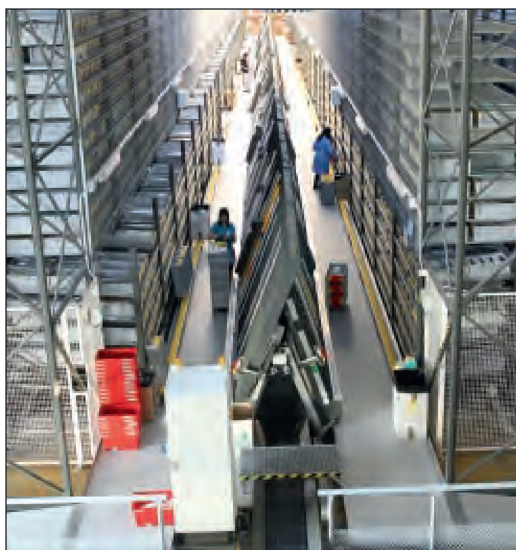

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despite what industry our clients are in, if they are not using the Internet now, they have a plan to get into it." He notes that more consumers are now using brick-and-mortar stores merely as "showrooms" to see a particular model, confirm its looks and functions, but then head back home to compare costs among web retailers before ordering that model online.

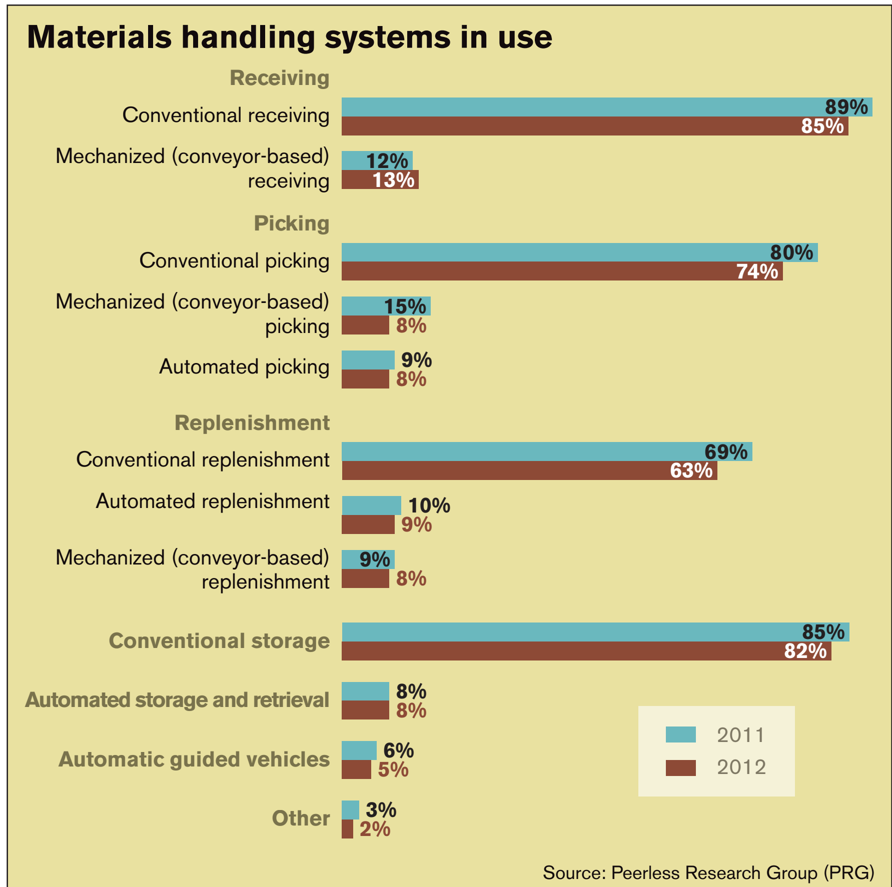
How are multi-channel respondents fulfilling their orders? Forty percent are filling their orders themselves from one main DC, designating separate areas for retail or e-commerce or scheduling specific pick waves for certain channels. "Almost 25 percent of respondents have already decided to put it in a separate DC," notes Saenz. "It would be interesting to see how these results change as each channel grows. I predict more separate DCs and the use of more third-party logistics providers."

2012 DC network profile

The profile of this year's distribution network remains mostly the same as the past few years.

Sixty percent of respondents operate less than 250,000 square feet of space in their distribution network, with most common clear heights of 20 to 29 feet. Derewecki predicts that, over time, the mix is going to shift towards taller, higher buildings. "Lift truck technology is making higher buildings very practical," he says. "Newer, double-deep reach trucks, for example, can lift to a height of over 36 feet."

Seventy percent of respondents report undertaking some kind of distribution network optimization and location studies, mostly on an "as-needed" basis. As a result of these studies, half of respondents (50 percent) report "moving inventory among warehouses" as it is the easiest and quickest option among all the other network improvement actions. For those adding DCs as a result of these studies, most cite "improved customer service" (70 percent) and "the penetration of new markets" (36 percent) as their top two drivers.



Tracking previous trends

Recycling continues to dominate sustainability efforts at 76 percent. This year however, slightly more respondents are "reusing shipping containers" and "using metal and/or plastic pallets."

Derewecki notes that he's seeing more plastic pallets in use at pharmaceutical manufacturing because of FDA requirements. "Wherever you have a requirement of a sterile or cleanroom environment, then that's one good way you can use reusable plastic pallets."

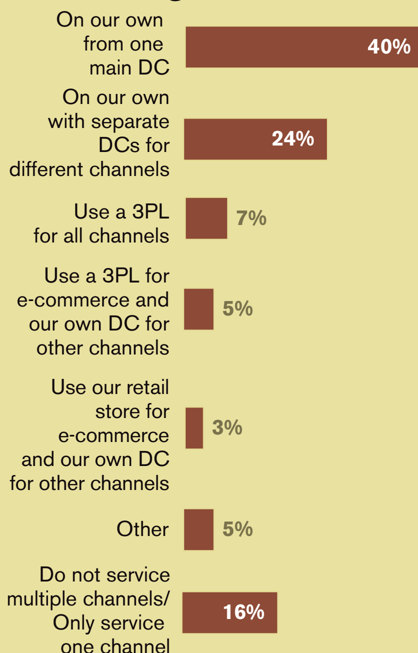
Fortunately, fewer respondents (only 15 percent versus last year's 28 percent) experienced catastrophic events this year compared to last year. Open-ended responses show many operations being hit by hurricanes and tornadoes; but to protect against these particular threats, survey takers have installed back-up generator and data retrieval systems, set plans in place to re-route demand to another DC, and have established multiple sources for parts and raw materials.

To reduce operating costs, "improving warehouse processes" (64 percent) and "improving inventory control" (61 percent) remain the top two actions preferred most by respondents. "It makes sense because both do not necessarily involve a high level of investment," says Derewecki. "However, the better operators have already done all the process improvements that they can do without making capital investments. They are at the next stage. To improve, they may need to invest in mechanization and automation."

Maida Napolitano is a Contributing Editor to Logistics Management

Market channels serviced by company

How multiple channels are being fulfilled



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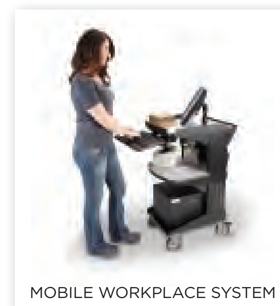

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A SPECIAL SUPPLEMENT TO:
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Special Report:
U.S. Ports Update

Preparation heats up

In anticipation of the Panama Canal expansion in 2014, the fight for market share of inbound cargo remains fierce among top U.S. ports.

By Patrick Burnson, Executive Editor

Influenced by an evolving maritime logistics industry, global trade transformations, the extension of the Panama Canal, and the growth of U.S. exports, U.S. port analysts see a bright, long-term future for our nation's gateways. Today, capital is being poured into seaport infrastructure from both the private and public sectors, responding to increased demand for port-centric warehouse and distribution space.

According to Jones Lang LaSalle's fourth annual seaport report, the U.S. East Coast ports will be especially competitive in 2013. "Developers, investment interests, and supply chain executives remain optimistic about our nation's seaports," says John Carver, head of Jones Lang LaSalle's Ports, airports and global infrastructure (PAGI) group.

As reported in the firm's earlier studies, commercial real estate surrounding major U.S. seaports continues to outperform the broader industrial market. But the report may do little to ease the minds of U.S. port authorities that argue that more must be done to make their operations efficient.

"Despite substantial investments by port authorities and private-sector business partners, inadequate infrastructure connecting ports to landside transportation networks and water-side shipping lanes often creates bottlenecks that result in congestion, productivity losses, and a global economic disadvantage for America," says Kurt Nagle, American Association of Port Authorities (AAPA), president and CEO. "These congestion issues and productivity losses have the potential to stymie our ability to compete internationally."

Nonetheless, both the AAPA and PAGI analysts agree that the nation's leading ocean cargo gateways are spending the most on structural improvements. The

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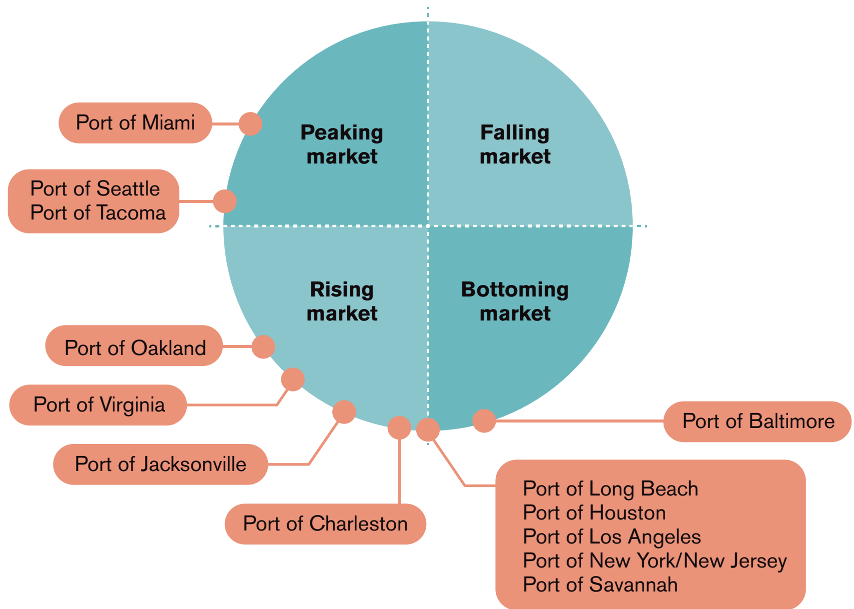
Jones Lang LaSalle's report, which analyzes the health of major domestic container seaports and their surrounding real estate, also reveals that:

Exports are creating inland development opportunities: U.S. exports are now creating back-haul opportunities and are driving new connections between domestic maritime ports, inland destinations, and their surrounding distribution real estate markets.

Investment is pouring into ports: At least $13 billion of public investment is earmarked for port development in the next decade.

Limited options are available for large space uses: Only 20 blocks of space are available for users requiring 250,000 square feet within five miles of a major U.S. port.



Here's how the nation's leading seaports are putting investment to work to ensure their position in a competitive race that's only going to heat up in 2014.

The Port Index: Changes at the top

Success for some ports is detailed in the Jones Lang LaSalle Port Index, which ranks U.S. ports on terminal operating and real estate market factors—including the port's proximity to concentrated population and manufacturing hubs.

For the first time in its four-year history, the index has rated the Port of New York and New Jersey at the top of the list, followed closely by the ports of Los Angeles and Long Beach.

According to Aaron Ahlburn, head of industrial research for Jones Lang LaSalle Americas, these three major seaports profit from several factors: "First, they support vast local population centers; second, infill vacancy around the ports themselves remains tight and new development is prized; and third, they are connected to less land-constrained, adjacent markets that facilitate 'big-box' logistics space."

Ports like Seattle, with strong demographics and a sizeable consumer base within a 24-hour trucking window, have remained high on the index. Similarly, others that are competitive shipping destinations, such as Houston, Miami, and Baltimore, are moving to re-establish more solid industrial leasing and investment conditions.

Ports that may not benefit from immediate large populations such as Hampton Roads, Jacksonville, Savannah, and Charleston remain important throughput hubs to move goods and materials into other parts of the country. However, Savannah, Charleston, Jacksonville, and Baltimore have higher vacancy rates in their surrounding port markets, but have experienced the fastest growth in occupancy over the last 18 months. "We expect development to remain cautious as these markets continue to strengthen over the coming quarters," says Ahlburn.

Many port markets that experienced significant "big box" development prior to the downturn have not been able to burn off their excess construction. Houston, Charleston, Savannah, and Jacksonville have double-digit vacancy rates.

But there are fewer than 10 existing warehouse or distribution facilities of more than 500,000 square feet within a 15-mile radius surrounding the major seaports, according to the report. For large users in markets such as Southern California or the Northeast, that means transporting cargo to inland destinations—inland ports—or bidding against other tenants for space.

This not only provides opportunities to develop smaller distribution centers or redevelop old ones, says Carver, "but it also serves to evaluate supply chain requirements, adapt potential transportation routes, and assess competitive drayage options."

Florida ports poised for growth

Miami-Dade County announced last month that the contracting phase of its project to deepen the Port of Miami's channel to minus 50 feet has begun with the solicitation of bids by the U.S. Army Corps of Engineers. Construction is scheduled to begin in early 2013 and be

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Select top U.S. seaports and property market indicators

Port	2011 Volumes (TEUs)	2011 annual change	2011 YTD (TEUs)	TEU change 2012	Immediate market size (m.s.f.)	Current vacancy	2011 net absorption (m.s.f.)	YTD 2012 net absorption (m.s.f.)	Average asking rents (NNN)	Terminal operator and comments
Los Angeles*	7,940,511	1.4%	4,010,204	6.4%	100.1	7.1%	-0.1	-0.7	$6.60	APM Terminals; California United Terminals; Eagle Marine Services; Port of Los Angeles; Seaside Transportation Services LLC, TraPac, Inc.; West Basin Container Terminal LLC (2); Yusen Terminals Inc.
Long Beach*	6,061,091	-3.2%	2,889,600	-2.6%	152.4	6.7%	0	-0.5	$6.12	International Transportation Service, Inc.; Long Beach Container Terminal Inc., Pacific Maritime Services; SSA Terminals; SSAT Long Beach, LLC; Total Terminals International
New York/ New Jersey**	5,503,485	4.0%	2,720,790	1.5%	211.0	7.6%	0.6	1.0	$5.58	American Stevedoring Inc.; Maher Terminals LLC; New York Container Terminal; Global Terminal & Container Services LLC; Port of New York/New Jersey
Savannah	2,944,678	4.2%	1,508,367	2.4%	39.2	17.9%	4.0	0.1	$3.70	Georgia Ports Authority
Oakland	2,342,504	0.5%	1,148,853	0.6%	104.1	6.2%	-0.6	0.9	$6.96	APM Terminals, TransBay Container Terminal Co.; TransPacific Container Service Corp.; Seaside Transportation Services, Total Terminals, Inc. LLC; SSA Terminals, Inc.; Eagle Marine Services
Houston	1,866,450	9.3%	1,087,315*	0.3%	52.5	7.7%	0.2	1.3	$4.20	Port of Houston Authority
Virginia	1,918,029	1.2%	994,727	5.4%	50.8	7.3%	-0.1	-0.1	$4.56	Virginia International Terminals; APM Terminals
Seattle*	2,033,535	4.9%	1,006,390	-0.1%	35.7	3.0%	0.8	0	$7.05	Eagle Marine Services; SSA Terminals; Total Terminal International; Port of Seattle; Northland Services
Tacoma*	1,488,790	3.9%	729,767	1.3%	23.6	6.6%	0.3	0.1	$5.10	APM Terminals, Husky Terminal & Stevedoring; Olympic Container Terminal; Pierce County Terminal; Totem Ocean Trailer Express; Washington United Terminals
Charleston**	1,381,349	1.3%	743,384	7.4%	26.9	12.9%	1.6	-0.2	$3.80	South Carolina State Ports Authority
Miami	906,607	6.8%	455,001	-0.5%	97.6	8.2%	0.9	0.6	$4.60	Seaboard Marine; South Florida Container Terminal; Port of Miami Terminal Operating Company
Jacksonville	899,258	8.9%	437,660	2.4%	68.1	12.6%	1.0	0.1	$3.49	Jaxport; Ceres Terminals Inc.; Costal Maritime; Marine Terminal Corp., SSA Marine (SSA Cooper LLC); APM; Global Stevedoring/ ICS Logistics; TraPac Marine Terminal
Baltimore	631,802	16.0%	325,852	5.0%	97.7	10.8%	-0.4	-0.1	$4.48	Balterm; Mid-Atlantic Terminal; Ports America; Maryland International Terminal, Inc.

*January-July ** Estimated

Source: American Association of Port Authorities, individual ports and Jones Lang LaSalle Research

completed in time for the opening of the expanded Panama Canal in early 2015.

Bill Johnson, the port's director, says that a deeper channel will provide ships with a more efficient, reliable, and safe navigational route into Miami. "As the closest port to the Panama Canal, we're well positioned to capture new trade opportunities," he says. "The port will double its cargo traffic over the next several years."

Meanwhile, a smaller, but important regional port to the north is undertaking three key expansion projects over the next six years. According to authorities at Port Everglades, the Broward County gateway will add five berths, widen and deepen the channel to 50 feet, and bring freight rail into the port.

According to spokesmen, Port Everglades must take these vital expansion steps to remain competitive with seaports in the Southeastern U.S. "The port already handles Post-Panamax ships," says Steve Cernak, the port's chief executive and director. "But they must be lightly loaded, which is inefficient and drive carriers away to other ports."

Gulf ports plan for inbound

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continue to vie for inbound first call. In fact, German ocean carrier Hamburg Sud recently added the Port of New Orleans to a new weekly service to Latin America through a space charter agreement with Hapag-Lloyd. The service will connect New Orleans with Caucedo, Dominican Republic; Buenos Aires, Argentina; Montevideo, Uruguay; Rio Grande, Mexico; and Suape, Santos, Navegantes and Rio de Janeiro, Brazil.

"Hamburg Sud is among the world's top 20 container lines, and we're thrilled that they are now calling on the Port of New Orleans," says Port President and CEO Gary LaGrange. "This new service will allow our customers better access and more frequent service to Latin American markets."

The Port of Houston, meanwhile, is ranked first in U.S. foreign tonnage, second in total U.S. tonnage, and third in U.S. export tonnage. Federal customs revenue collected from the port's cargo exceeds $768 million per year. The $171 million in harbor maintenance tax collected annually from channel-related activities are far more than the $40 million to $50 million needed annually for adequate channel maintenance.

Compared with other Gulf and East Coast ports, Houston's ship channel receives a fraction of funds on a per-ton-of-cargo basis—9 cents where the average is 44 cents—resulting in inadequate channel maintenance. The U.S. Army Corps of Engineers is responsible for maintaining the channel, which is subject to constant siltation and erosion, based on money appropriated by Congress. Despite strong and bipartisan advocacy from the Harris County Congressional delegation, enormous pressures on the federal budget make it challenging to fund Corps projects nationwide.

West Coast promise

The Los Angeles Harbor Commission recently approved $7.5 million for the final phase of the Port of Los Angeles' main channel deepening project (MCDP). The project has taken the port's main navigational channels and basins to a 53-foot depth, ensuring that the nation's number one gateway for containerized trade can accommodate container ships of all sizes for decades to come.

"Channel deepening has been our single-most important infrastructure priority," says Port of Los Angeles Executive Director Geraldine Knatz, Ph.D.

Dredging of the port's main channel and turning basins has already been completed. The final phase of the project involves removal of dredge surcharge material and completion of a shallow water habitat in the outer harbor.

The port's nine container terminal tenants rely on the port's deep channels to move cargo. Container terminals generate about 74 percent of port revenues and help facilitate hundreds of thousands of direct and indirect jobs throughout Southern California. The 15-year, $370 million project will be completed in early 2013.

The Port of Oakland, meanwhile, continues its measured growth. When the port's executive director, Omar Benjamin, hired James J. Kwon to run the Maritime Division five years ago, ocean cargo industry insiders regarded the move as inspired.

Rather than choosing a port functionary for the post, Benjamin sought out a savvy and worldly deal-maker. Kwon, who speaks both Korean and Chinese, was charged with making Oakland the first port of call for inbound transpacific cargoes and with keeping the gateway positioned as the leading outbound quay on the West Coast.

Kwon had the connections and experience to get the job done, too. Under his watch, Oakland welcomed the largest containership ever to call any seaport in North America. The MSC Fabiola—a 12,562 TEU (twenty-foot equivalent-unit) vessel—is part of the fleet of the world's second-largest shipping company.

Benjamin has also been recently praised for playing a key role in the port's redevelopment of the former Oakland Army Base (OAB). The OAB project involves a transformation of the former base into a world-class trade and logistics center that will strengthen Oakland's position as an export hub. The port handles 99 percent of all containerized goods in Northern California, and agricultural products represent approximately 40 percent of the total value of exports.

—Patrick Burnson is Executive Editor of Logistics Management

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QUARTERLY TRANSPORTATION MARKET UPDATE:
LESS-THAN-TRUCKLOAD

LTL: Primed for profit

After being battered by three years of recession that decimated profits, LTL carriers are now focused on improving yields and profitability in order to recapitalize their rolling stock. Now, what does this mean for rates?

By John D. Schulz, Contributing Editor

Daniel Guidera

After several recession-battered years, the $33.5 billion less-than-truckload (LTL) market is set to get back to making money. Carrier executives and analysts are predicting rate increases in the 2 percent to 4 percent range. That does not include any increase in fuel surcharges, which right now are adding about 30 percent to every LTL bill.

Of course, any 2013 estimate is cautious. After all, we're in the midst of global macroeconomic uncertainty, a presidential election, and just so-so economic growth.

But after three years of recession that decimated profits in the sector, LTL carriers are focusing more on improving yields and profitability in order to make decent enough returns to recapitalize their businesses and rolling stock. Improved conditions in the auto and housing sectors are buoying some carriers' hopes that 2013 could be their best year for profits since 2006.

"Thin margins are not allowing LTL companies to earn their cost of capital, and without an increase in tonnage to drive density and operating leverage, price and productivity improvements are the only real ways to expand margins

to justify reinvesting in the industry's old and aging fleet," says David Ross, the LTL analyst for Stifel Nicolaus.

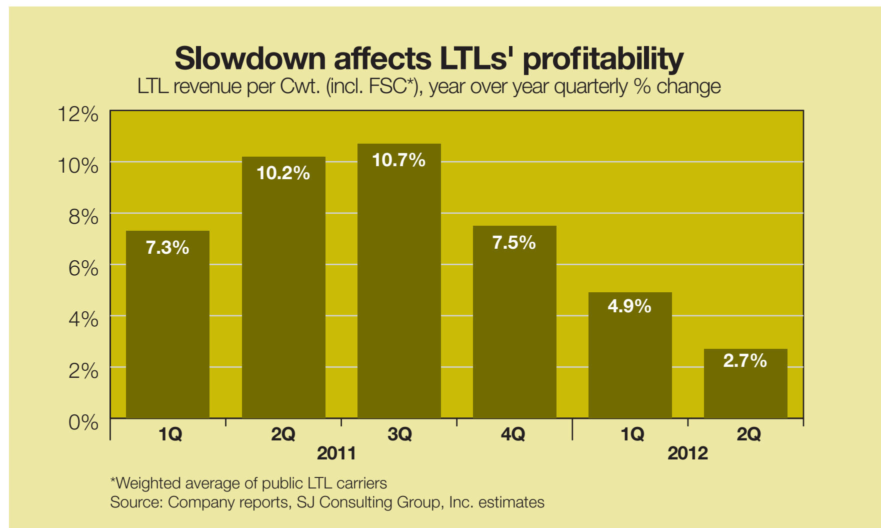
In other words, LTL shippers who took advantage of low prices and excess capacity during the recession should be budgeting for fairly significant price increases in their 2013 budgets. The price war that tried—and failed—to extinguish YRC Worldwide, the second-largest LTL carrier that has lost in excess of $2.6 billion over the past six years, is over. YRC is still in business, and is revitalized under a new management team led by CEO James Welch and his top lieutenant Jeff Rogers, two respected LTL operators.

Whatever YRC's future is, analyst Ross believes LTL capacity will be restrained over the next 12 months. There are no new entrants in the LTL market because of high barriers to entry for terminals, which are costly and time-consuming to build.

That's good news for carriers, who are already showing some margin expansion as a result of re-pricing in their poorest-yielding accounts. This is necessary, adds Ross, to recapitalize aging fleets. He says that it may take two or three years to add enough new trucks to bring the average LTL fleet age into historical norms due to the cutback and elimination of new truck purchases during the recession.

"We're focusing on improving yields, and that was not always the case in the past," says Con-way Inc. President and CEO Doug Stotlar. "There is a new emphasis on profit, and that hasn't always been the case in our industry. But it is now."

So, how are shippers to cope with this new era of tighter capacity, higher rates, and tougher carrier negotiation mindset? Let's look at what's behind the numbers.



Pricing "firms"

Unlike the highly fragmented truckload sector, where even the largest carrier barely maintains a 1 percent market share, the top handful of LTL carriers control the majority of the market. In fact, the top five LTL carriers enjoy a collective 56 percent market share—FedEx Freight (16 percent), YRC (15 percent), Con-way Freight (11 percent), UPS Freight (8 percent) and Old Dominion Freight Line (6 percent).

With these top carriers now concentrating on shedding their worst performing accounts in order to better concentrate on higher-yielding business, it isn't surprising that analysts and carriers agree that LTL pricing is firming.

"I would say that pricing is 'largely rational,'" says Ross. "Certain regions are seeing tighter competition, and soft volumes in late summer put pressure on spot pricing. However, the majority of carriers in what is a highly consolidated industry continue to be focused less on market share gains than on recovering from the record low margins that characterized the freight downturn."

Ross is expecting to see yield increases continue at least through the third quarter of next year—and carrier executives agree. "The pain inflicted by the economic downturn is still fresh in everyone's mind," says Steve O'Kane, president of A. Duie Pyle, a major Northeast regional LTL carrier. "When excess capacity drove prices down during that period, everyone in the industry was injured. But those that lead the way in trying to gain market share—or put a competitor out of business—saw their results suffer the most. I believe this lesson was learned, and it's helping carriers maintain pricing discipline."

Wayne Spain, executive vice president and COO of Averitt Express, agrees with O'Kane's assessment. "Carriers had to discipline themselves to this 'new normal' and find ways to improve yield and drive costs out of their network in order to compete, including removing capacity," says Spain. "As shipping volumes have slowly risen, supply and demand have moved closer to equilibrium. Now we're beginning to see a closer alignment of rates with available capacity."

Satish Jindel, who closely tracks the LTL sector as principal of SJ Consulting, says that there is greater awareness among certain carriers that they need to sustain a minimum 96 operating ratio (OR) in order to recapitalize their fleet and stay in business. "The past three or four years have seen pretty bad results in the LTL sector," says Jindel. "It makes them realize that they can't have that type of 99 or 100 OR. That has helped pricing get firm."

Chuck Hammel, president of regional LTL Pitt Ohio, says that he's noticed a slight weakening of rates this summer as a result of some softening in the economy and less freight all around. "What we've done is slowed down on our rate increases," says Hammel. "We increased everybody on the first of year. But things are slowly down and shippers are pushing back, so carriers are looking for business and are pricing aggressively in order to get new business. That began in the second quarter."

Could yield improvement fail?

This newfound emphasis on yield improvement could be pushed off the road by a couple of factors. First and foremost is the macroeconomic situation. For example, if China's economy slows, that will have a ripple effect on overall U.S. economic conditions—and, by extension, the LTL market place.

"I have never believed that we've ever fully come out of the 2009 recession," says Jindel. "We're still largely in the same situation of high unemployment and slow overall economic growth."

Secondly, Jindel adds that there are certain carriers that, despite difficult times, have an inability to understand what the cost is to service certain customers. "That leaves them offering pricing that is not profitable, and that creates a competitive response," he says. "Some shippers are still using that to their advantage in avoiding price increases."

Pitt Ohio's Hammel agrees: "There are some shippers that, when you mention rate increases, will simply say, 'There are a lot of other carriers that will take my business.' And there may be."

For that reason, Jindel's 2013 LTL rate forecast is more in the 2 percent to 3 percent range, excluding fuel surcharges—which averaged 29.3 percent in the second quarter, compared with 29.8 percent in the second quarter of 2011. Some carriers will get higher than those average rate increases because of special geographic lanes and density issues. "The one other thing that's helping yields stick is that there's more discipline among carriers who had precipitated the decline in rates," Jindel says.

The changing conditions and leadership at YRC are a major factor in the rate environment as well, Jindel says. "YRC management is more focused on the business enterprise as opposed to shareholder value; and that's promoting greater emphasis on service improvement. Through that, you can get pricing improvement."

2013 forecast: Cloudy and more expensive

For at least the next 12 months to 18 months, the analyst community is hinting that LTL rates should run slightly ahead of the rate of inflation. Active LTL capacity remains relatively in balance, supporting continued pricing momentum for LTL carriers. While some carriers have been adding drivers and trucks, analyst Ross says that may be offset by some financial failures of less well-capitalized carriers as lenders may be more inclined to let them fail.

> **"The industry needs it to keep up with costs, and with an infrastructure that is outdated and works against greater productivity, the cost increases must be reflected in prices."**
>
> *—David Ross, Stifel Nicolaus*

Ross is forecasting LTL tonnage growth through 2014 amid a "slow, likely choppy, recovery," with less than 3 percent annual freight growth and pricing rising faster than volume—1 percent to 5 percent annual yield increases, depending on supply/demand situations in specific geographic lanes.

Most carrier executives agree capacity will be "restrained" over the next 12 months. Except for Old Dominion, LTL returns simply are not adequate for the public carriers to be motivated to add capacity, they say.

With new Class 8 tractors costing in excess of $100,000, and terminals in major metropolitan areas costing upwards of $10 million, no one is likely to invest in adding capacity for an operating ratio in the mid 90s, O'Kane says.

"It doesn't make sense…just look where today's LTL yields are as compared to the pre-recession era of 2006-2007. In a time when costs have gone up dramatically, industry yields are not much different than those of five years ago."

O'Kane and other carrier executives contend that rate increases of 3 percent to 4 percent are both realistic and necessary. "But whether or not they play out that way is anybody's guess," adds O'Kane. "If the economy keeps expanding slowly, my guess is David Ross is close to being correct. The industry needs it to keep up with costs, and with an infrastructure that is outdated and works against greater productivity, the cost increases must be reflected in prices."

LTL carriers also believe that the more volume a shipper has with a core carrier, the more opportunity to remove costs. Some examples of cost reduction can come from changing a live pick-up to a spotted trailer; shipping palletized freight rather than loose cartons; directionally loading trailers for a carrier; moving pick-up times earlier in the day to allow the carrier to work freight earlier; providing better information to assist the carrier in load planning; provide electronic bills of lading; or adjusting the lanes being used to better fit the carrier's system.

"Not all shippers will be able to do what's necessary to employ these cost savings measures," O'Kane says. "But the more they consult with their service providers and exchange thoughts, the more ways both sides will be able to take cost out of doing business."

Averitt's Spain adds that shippers can improve their supply chains by sharing as much data as possible with their carriers to improve our ability to accurate forecast needs and provide flexible transportation options. "Collaboration, as always, is the key to a successful partnership," Spain says.

John D. Schulz is a Contributing Editor to Logistics Management

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Quality in Review

The carriers, third-party logistics providers, and U.S. ports that earned 2012 Quest for Quality gold where recently celebrated at our 2012 Awards Dinner at the Omni Atlanta.

The editorial staff of *Logistics Management* was thrilled to offer the logistics and transportation community the results of the 29th Annual Quest for Quality Awards in our August issue (logisticsmgmt.com). This year, 127 providers of transportation and logistics services received the ultimate vote of confidence, posting the highest scores across our lists of critical service criteria. The winners officially accepted their awards on Wednesday, October 3, in the International Ballroom at the Omni Atlanta.

For nearly three decades, *Logistics Management*'s Quest for Quality has been regarded in the transportation and logistics industry as the most important measure of customer satisfaction and performance excellence. To determine the best of the best, *Logistics Management* readers rate carriers, third-party logistics (3PL) service providers, and U.S. ports strictly on the basis of service quality.

Quest for Quality winners are voted on by the readers of *Logistics Management*—the customers that put these carriers and providers to the test around the clock in countries throughout the world. If fact, this year we had 4,709 logistics and supply chain decision makers place their vote during this six-month research project.

29th Annual Quest for Quality in Review

The team from Alliance Shippers was on hand to collect Quest for Quality gold in Atlanta. Alliance put up top marks in the 2012 Intermodal Marketing category, posting an impressive 52.19 weighted average score.

FedEx took home an impressive seven awards in seven different categories this year. Once again, the industry bellwether was well represented at this year's Quest for Quality awards dinner.

The crews from New Penn, Holland, and Reddaway were also busy at this year's awards dinner. Combined, this group stepped up to the podium five times to collect awards in the Regional LTL and Truckload categories.

Perennial Air Carrier winner Southwest Airlines Cargo was also on hand to collect its Quest for Quality gold. For years, Southwest has topped this category for its service, and did so again in 2012 posting an impressive 52.22—one of the best overall weighted averages in this year's survey.

Miller Transporters, Inc. is another carrier that puts up impressive Quest for Quality scores year after year. This year, Miller posted a 54.41 weighted average in the Bulk Motor Carriers, another one of the highest scores we recorded in 2012.

The team from Purolator was well represented at this year's dinner to accept their Quest for Quality gold. Another perennial reader favorite for service, Purolator scored a 46.22 weighed average in this year's 3PL category.

Following dinner and the awards presentation, comedian Orny Adams had the crowd of more than 150 attendees rolling in the aisles. Renown for his searing observational comedy, Adams has been featured on *The Tonight Show with Jay Leno* and *Late Night with David Letterman*; and along with Jerry Seinfeld, he is the subject of the 2002 documentary film, *Comedian*.

SAGE ADVICE

Location, location… does it really make a difference?

By John A. Gentle, DLP

An article in our local newspaper lamented the plight of individuals who live in the suburbs and rely upon bus service to get them to work, often at odd hours. Poor ridership has caused some towns to question the need for increased taxes to subsidize the service, while the metro transit authority cites insufficient revenue.

Without the needed increase in ridership, fares, or additional taxes, all or which is unlikely, the transit authority will soon suspends service and dependent riders will be left without a means to move about.

Carriers are often faced with a decision to limit or abandon a shipper or receiver when an area, that had once been rich with daily inbound and outbound shipments, has shriveled while the center of opportunity has moved to a different geographic area.

So, how attractive is the area where your plants and distribution centers (DCs) are located?

While fair and compensable rates are of paramount concern to both parties, carriers continue to look for opportunities to minimize deadhead miles and time between movements. If your company is able to provide closely timed inbound and outbound moves for your carriers and their drivers, then you're temporarily exempt from this problem.

If you don't provide your own inbound capacity, then you need to be assessing the strength of your proximate area to attract inbound freight—or at least have a plethora of outbound freight using the same transportation modes. Being surrounded by less-than-truckload, reefer, or dry van shippers and receivers provides no value to a flatbed shipper, for example.

In addition, the availability of your freight is also a big factor. If you're in an area where the predominance of companies receive and ship at times that differ dramatically from yours and the predictability of your movements are sporadic, then you're becoming "unattractive."

So, what can you do? First, recognize and accept that the world does not revolve around you. I thought it did until I woke up to the fact that the distribution point for a major metropolitan area had shifted. While I had good outbound volumes, there was no inbound to my area; meanwhile, carriers were taking the opportunity to generate more revenue in a new distribution pocket 60 miles away.

Second, ask your carriers about the companies that ship and receive with the same modes that are within a 10-mile to 15-mile radius of your operation.

Third, talk to metropolitan developers and see where they're planning future distribution complexes—and which of the big box operations are opening or planning to open any new distribution centers and where they'll be.

If your DC or plant can't unload or ship when driver capacity is available, that capacity will move immediately to a more flexible customer.

Fourth, pay close attention to the hours that are kept by the logistics operations with which you'll be competing for capacity. If your DC or plant can't unload or ship when driver capacity is available, that capacity will move immediately to a more flexible customer. Plants and DCs need to recognize that they share responsibility for being a viable and service-effective shipping and receiving operation. They must change their operating practices, and where practical, move their locations to areas that can successfully compete for transportation capacity.

Fifth, do not allow "greenfield" evaluations to be hijacked by controllers who see tax abatements, low interest construction loans, and low cost of labor as the sole driving factors in where to place new operations. Placing a facility in the middle of nowhere will not attract cost and service-effective transportation.

Last, if you can't generate enough of your company's inbound, consider collaborating with another company who may need compatible distribution support—their inbound may be just enough to help you appear more attractive to carriers.

Everyone must realize that, for the foreseeable future, carriers will not be expanding their fleets and they'll be looking to find a way to serve more than one of their good customers on the same day. So, take steps now to make sure that you're not standing alone in the cold at a "truckstop" that's being considered for elimination by your carriers for lack of consistent, timely, and profitable ridership. ☐

John A. Gentle is president of John A. Gentle & Associates, LLC, a Supply Chain consulting firm assisting shippers, carriers, 3PLs, and distribution centers in the management of their Logistical disciplines. A recipient of several industry awards, he has more than 40 years of experience in transportation, warehousing, and materials management. He can be reached at jag@RelaTranShips.

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