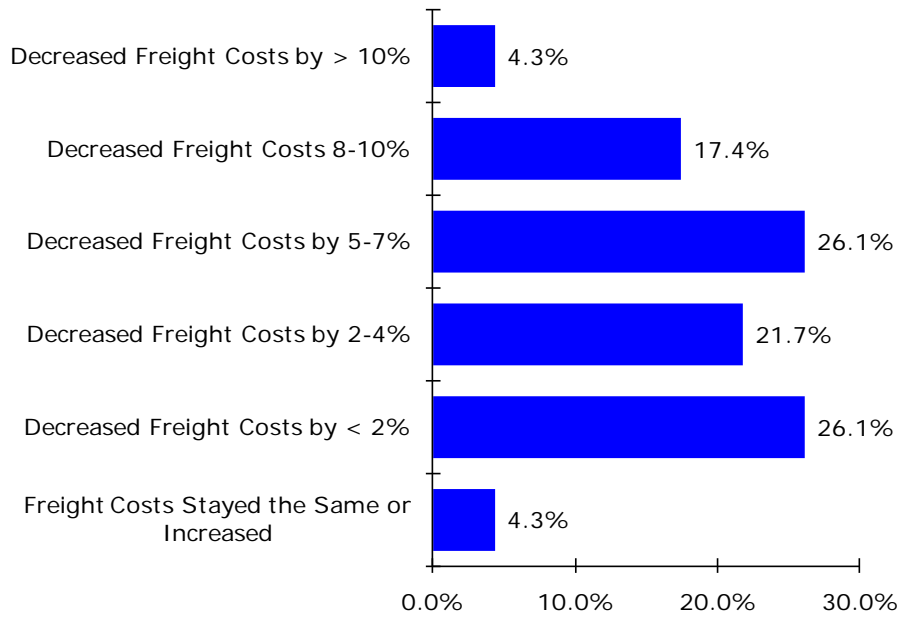


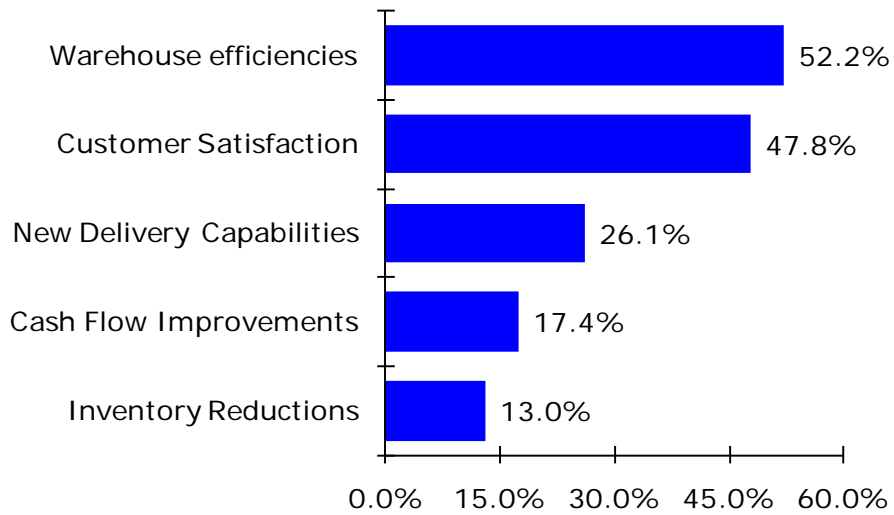
The Return on Investment of Managed Services for Transportation

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Use of Managed Services for Transportation



Multiple Answers Permitted

Other Benefits Associated with Working with a Managed Services Provider

Executive Overview

The decision to outsource any process, including transportation, involves tradeoffs between risks and benefits. Before deciding, it's important for shippers to understand the costs and risks associated with keeping transportation planning and execution in house versus outsourcing these critical activities using a third-party logistics (3PL) provider.

If a shipper currently plans and executes transportation activities using manual processes (spreadsheets, faxes, and phone calls) and has more than about \$10 million in freight spend, it can almost certainly save money while maintaining service levels by moving either to a managed services relationship or by implementing a transportation management systems (TMS). This report focuses on the ROI and risks associated with working with a managed services provider.

Roughly half of survey respondents reported freight savings of more than 5 percent once they began working with a managed services provider to plan and execute their transportation moves.

Managed services for transportation can offer a significant return on investment (ROI). The primary area in which transportation managed service can save a company money is by lowering its freight spend. Although, in a recent ARC Advisory Group survey, users also reported several other types of benefits.

By working with a 3PL to manage their transportation planning and execution, roughly half the survey respondents had freight savings of 4 percent or less and about half had savings of more than 5 percent. Very few respondents achieved no savings from transportation managed services and very few achieved freight savings of more than 10 percent. These savings can occur in a number of different areas, although 3PLs are particularly adept at driving savings in transportation procurement. Companies with a large number of hazardous material shipments are also particularly apt to drive large savings.

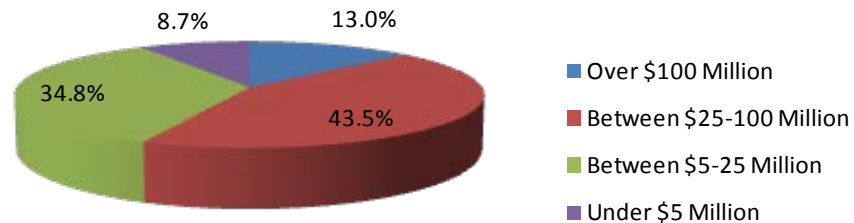
These savings are usually achieved without any service degradation. Half of the respondents reported that their service levels stayed the same after working with a managed services provider. More than four times as many respondents reported service improvements as compared to deteriorating service following the onset of these relationships.

Methodology

The focus of this survey was to evaluate the benefits (if any) that shippers realized from using managed services for transportation planning and execution. In particular, we focused on third-party logistics (3PLs) companies that provided transportation planning and execution based on the use of an advanced transportation management system (TMS). To provide these services, the 3PLs might use their own internally developed TMS or one purchased from a software company. We specifically excluded respondents that use a 3PL to do manual transportation planning and execution.

Eighteen people responded to the survey. ARC then completed five telephone interviews to gather more data points and gain qualitative insights. This brought the total sample size to twenty three. Twelve of the respondents had vice president or director-level titles; eleven respondents were managers, specialists, or analysts.

The majority of respondents came from companies that would be best described as midsized shippers. (See Appendix 1 for additional demographic data.)

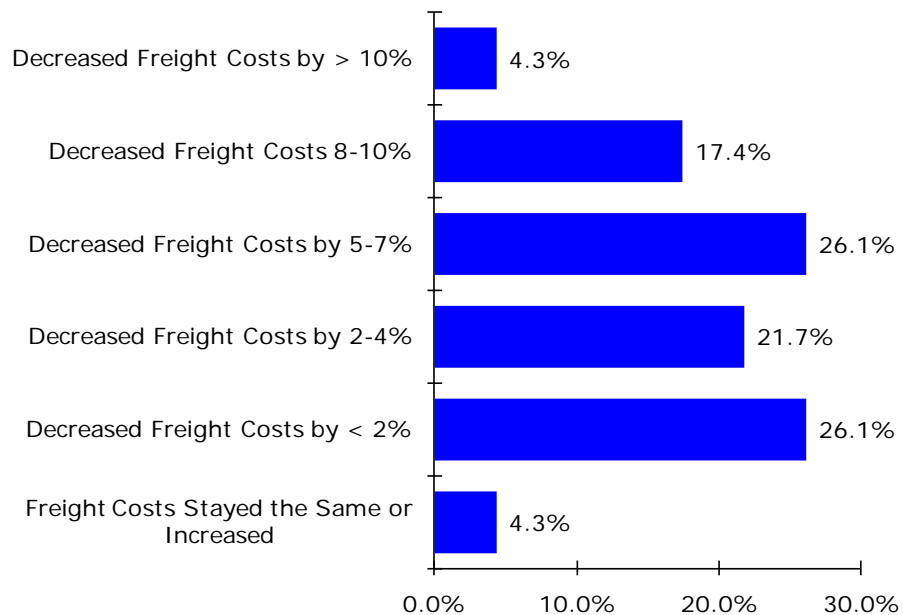


Freight Spend Under the Control of 3PL

The ROI of Managed Services

Managed services for transportation managed services can offer a significant return on investment (ROI). The primary area in which these can save a company money is to lower its freight spend.

By working with a 3PL to manage their transportation planning and execution, roughly half of respondents had freight savings of less than 4 percent, about half of more than 5 percent. Very few respondents achieved no savings from transportation managed services; very few realized freight savings of more than ten percent.



Managed Services for Transportation Reduce Almost All Shippers Freight Spend

Freight spend can be reduced in a number of ways. Some methods focus on collecting data that can lead to better decision making (for example, gathering data for better procurement engagements). Some methods might be classified as process enforcement (for example, by helping to ensure the best carriers on a lane are selected for moves). Some savings are based on the TMS' optimization capabilities. Finally, some are based on the domain expertise and consultative capabilities of the 3PL. The following table shows the savings opportunities of the most common savings buckets.

Savings Buckets	No Savings	Savings <2%	Savings 2-4%	Savings 5-7%	Savings 8-10%	Savings >10%
Increased Usage of Preferred Carriers	34.8%	Most Common		Largest Possible		
Better Procurement Negotiations	17.4%		Most Common			Largest Possible
Lower Cost Mode Selections	21.7%	Most Common			Largest Possible	
More Fully Loaded Equipment	30.4%		Most Common Largest Possible			
Better Routing	34.8%		Most Common Largest Possible			
Reduction in Carrier Overcharges	47.8%	Most Common	Largest Possible			

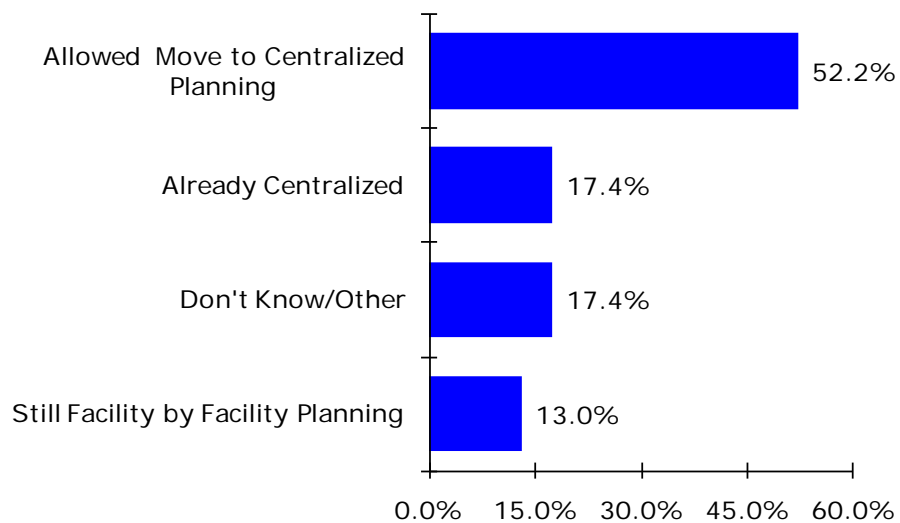
Savings Potential by Category from Managed Services for Transportation

To simplify the data, the table does not include the responses for all the fields. The data bolded in black shows the percentage of respondents that received no savings in a particular category. It is important to realize that not every category of savings will apply to every company. The data bolded in red shows the most common response among those that did report savings. The data bolded in blue shows the largest possible savings. To control for inadvertent responses and outliers, we only list “Largest Possible” savings if a cell on the far right hand side of the table had two or more respondents.

A couple of points to keep in mind when studying the table. First, when we examined the individual responses, the different savings buckets often added up to more than the total freight savings claimed. In phone conversations, ARC learned that these savings often are not linear. We couldn’t simply add the savings of the different savings bucket to get total savings because they apply to different portions of the total spend. For example, a shipper might be doing freight audit with a managed services provider across multiple modes, but its service provider may only be doing routing for outbound truck moves. Further, to a certain extent, the savings buckets are simplifications. In other words, sometimes savings is driven by combining features of what we have labeled as distinct categories.

Procurement can be an area which 3PLs have a relative advantage. Some managed services providers for transportation aggregate spend across several customers to achieve the kind of clout and significance that a midsized shipper could not achieve on their own. In other cases, 3PLs use best-of-breed transportation bid optimization solutions to improve transportation bids.

Finally, several 3PL suppliers do a network analysis to construct better lanes for bids. When the requests for proposals (RFQs) ask carriers for origin-to-destination pricing on long haul shipments, many lanes are classified as "low volume." These shipments are subject to more costly spot market pricing. An analysis that aggregates low volume lanes—defining origin and destination points more broadly— can increase the total shipments moving in a lane and obtain more favorable contract pricing.

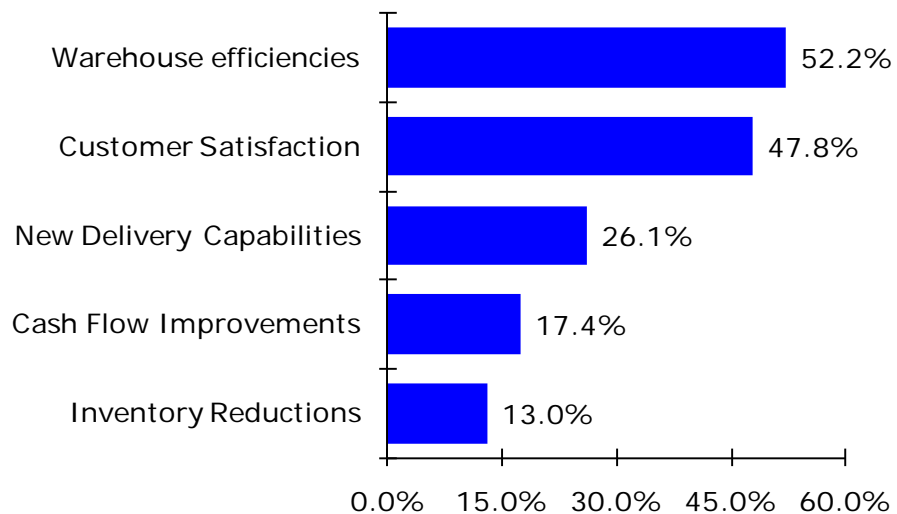


Did Working with Your 3PL Allow You to Move from Facility by Facility Planning to Centralized Planning and Execution?

Shippers with multiple facilities will experience greater freight-savings opportunities if they centralize transportation planning. This will make the shipper's business more interesting to carriers and lead to procurement opportunities. Centralized planning can help improve routing efficiencies and provide other advantages. Respondents reported that the relationship with the managed services provider helped them make the move to centralized planning. In general, the planning was done at control towers run by the 3PL, although in some cases 3PLs send some of their personnel to a customer's facilities.

A control tower is a location where a managed services provider uses its TMS to do regional planning and execute transportation loads for its shipper clients. At one site ARC visited, the managed services provider planned and executed transportation for 40 clients. However, many of these clients retained in-house control of their strategic transportation procurement process, their routing guides, and their approach to transportation pricing for their customers.

While reducing freight spend would be the primary reason for a shipper to work with a managed services provider, these relationships can deliver other advantages as well.



Relationship with a 3PL Can Drive a Variety of Other Benefits in Addition to Reduced Freight Spend (Multiple Answers Permitted)

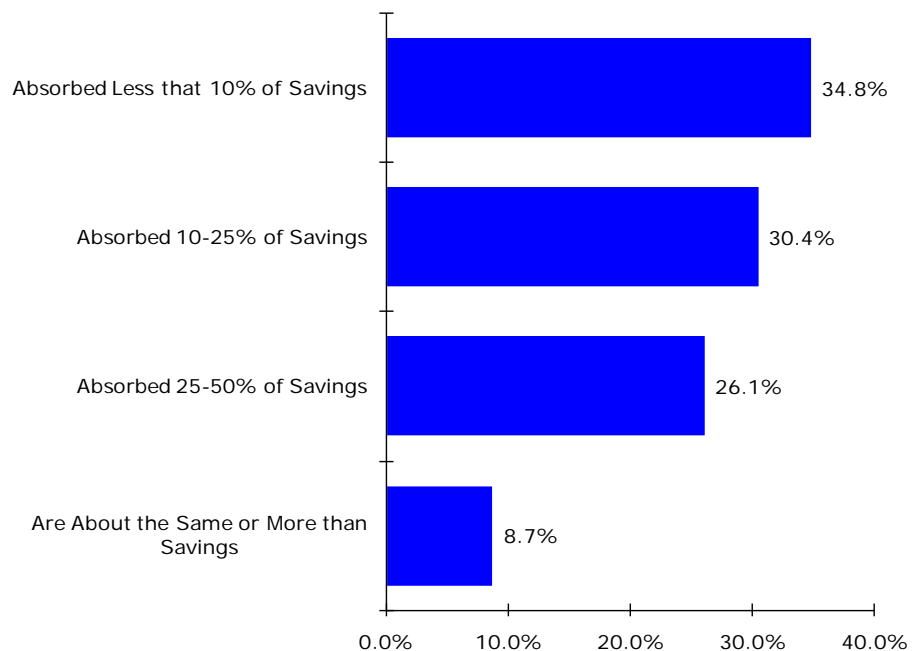
We gave participants a chance to write in other potential improvements that could be realized from a relationship with a 3PL. These included:

- Ability to focus on core business or allow their managers an opportunity to focus on other projects
- Reduced headcount
- Data generated to allow for a better network design or having the service provider actually do a network design project for them
- Having the 3PL do an inventory analysis

- Generating data that would allow for a customer service profitability analysis

Benefits Come with a Price Tag

Obviously, a 3PL does not provide its services for free. We asked respondents, “How reasonable are the fees charged by the 3PL? What percentage of your freight savings are being captured by your 3PL vendor in the form of ongoing payments for their services?”

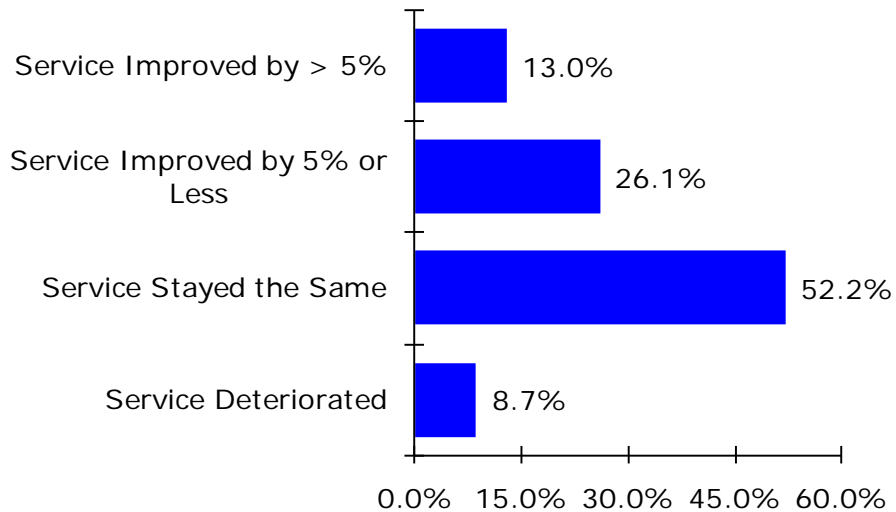


Total Fees for Transportation Management as a Percentage of Freight Savings

Over a third of the sample answered that the 3PL's fees absorbed less than 10 percent of the savings it generated. This indicates a strong value proposition.

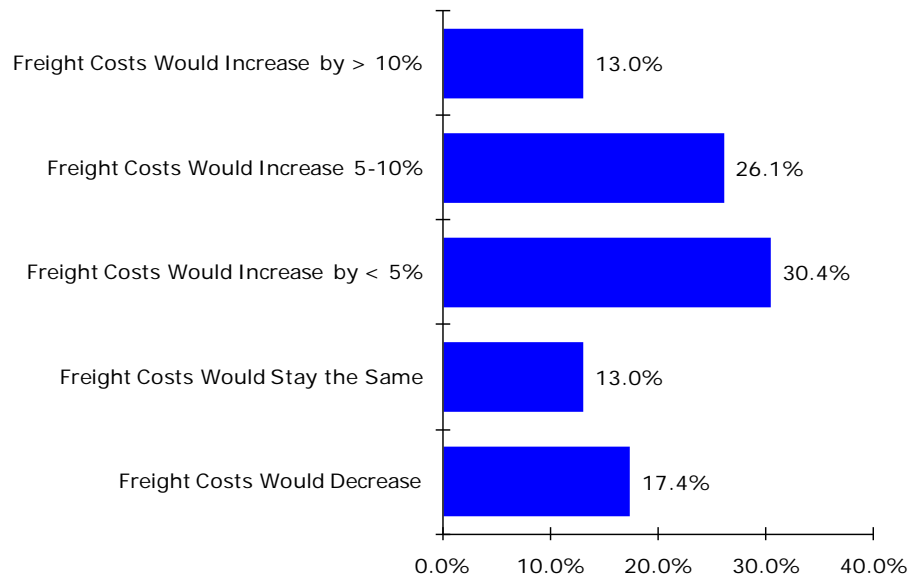
Risk versus Reward

Many shippers worry that a managed services relationship will lead to a deterioration in their customer service levels. However, the survey results suggest that the benefits of managed services do not come at the cost of poor service to a shipper's customers. In fact, most shippers reported improved service levels. Here, we define service level as the number of on-time deliveries within a two-hour window.



Shipper Service Levels Following Engagement of a Managed Services Provider

To help understand how shippers perceive the risk of these relationships, we asked respondents "What changes in freight costs do you believe would occur in the following year if you ceased working with your with your managed services provider?" Four percent reported use of managed services decreased freight costs by more than 10 percent; 17 percent reported decreased costs by 8 to 10 percent. But when respondents were asked how much freight costs would rise if they stopped working with their 3PL, 13 percent said their costs would increase by more than 10 percent and 26 percent by 8-10 percent. In other words, if a company releases its transportation planners and a managed services relationship does not work out, the shipper can't necessarily quickly get back to the base level of freight performance it had achieved prior to the outsourcing relationship, since it must then take the time to re-build the lost internal expertise.



What Changes in Freight Costs Do You Believe Would Occur in the Following Year If You Ceased Working with Your 3PL?

In our conversations with respondents, the risk of these relationships did emerge as a topic. The transportation solutions provided by 3PLs usually include a visibility component. One shipper we talked with used a 3PL for transportation managed services, yet had also implemented a visibility solution from a TMS provider. This shipper, a retailer that sourced extensively from Asia, saw milestone visibility as key to store fulfillment and controlling inventory. While its 3PL said it could provide this capability, this retailer saw outsourcing visibility to the 3PL as being too risky if the relationship was not successful.

A different shipper we talked with was unhappy with its TMS solution and turned to outsourced transportation services. However, the shipper retained some of its planners and continued to pay maintenance on its TMS solution as an insurance policy.

Finally, we came across a shipper that had discontinued working with its managed services provider and implemented a TMS. For this shipper, the key pain point was a kludgy integration between the service provider's TMS and its own internal ERP/order management system. The latencies created by poor integration had led to deteriorating service.

Interestingly, over 17 percent of respondents said their freight costs would decrease if they stopped working with their 3PL. In these instances, these

business arrangements have clearly *not* been successful from the shipper's perspective.

ARC's perspective is that each major approach to reducing freight spend has associated risks or constraints. If a shipper has not automated its transportation planning and execution processes, the two primary paths to freight savings would be by either implementing its own TMS, or working with a 3PL that uses an advanced TMS.

Respondents Reported Working with the Following Service Providers:

- Ryder
- Transplace
- Schneider
- LeanLogistics
- CEVA
- Penske
- DHL
- Ardmore Power Logistics
- Americold
- Geodis
- Kenco

If a shipper was to move from manual transportation processes to a TMS, it's likely that many of its existing planners would lack the right skill set to use a TMS. One key advantage of the managed services approach is the services companies' greater ability to develop power users.

For a decade, this analyst has argued that companies -- shippers in this case -- need to work harder to develop power users. Far too many shippers have skimmed on the necessary training. It would make good sense for companies to allocate ongoing dollars for training, in addition to the ongoing maintenance fees. This would enable them to continue to train their users year after year on how to

make better use of the software. If the TMS users can't stay on top of changes to a company's transportation network, routing guide, service levels, etc., the TMS would not be able to deliver value. In ARC's experience, however, few companies allocate adequate dollars to training.

Let's contrast that with the control tower approach in which the managed services provider has standardized on one TMS. The managed service's TMS planning team is much larger than most shipper's internal teams and are much more likely to have a more formal process for hiring and training transportation analysts.

When comparing the benefits of implementing a TMS versus using a managed services provider, the managed services provider often has an advantage relative to hazardous materials movements. Thirty-nine percent of our respondents reported using their 3PL to plan and execute hazmat shipments. Shippers using a 3PL to plan and execute their hazmat shipments were much more likely to report high freight savings; savings greater than 8 percent, based on the outsourcing relationship. This is one risk cate-

gory where shippers are particularly satisfied with their service providers' capabilities.

Recommendations

The decision to outsource any process, including transportation, involves a tradeoff between risk and benefits. There are costs and risks associated with both keeping transportation planning and execution inhouse as opposed to outsourcing these activities.

If a shipper currently plans and executes transportation using manual processes (spreadsheets, faxes, and phone calls) and has more than about \$10 million in freight spend, it can almost certainly save money while maintaining service levels by moving either to a managed services relationship or by implementing a TMS. Clearly, however, the shipper must weigh the risks and benefits of both paths forward. ARC previously published a Strategy Report on the ROI of Transportation Management Systems. Further, in the near future we will publish an Insight that makes more specific comparisons between these two paths.

Once the decision is made to proceed with a managed services provider, the next decision becomes which one. Different providers have domain expertise in different industries, modes, and types of transportation moves. However, ARC advises shippers to work with a provider that has standardized on one TMS, if at all possible. Service providers have to recoup their investment. If a provider implements a different TMS for different customers, it has higher software and implementation costs and less opportunity to develop power users. Obviously, the robustness of the TMS used by a service provider is another concern.

Finally, an outsourced transportation relationship can take many and varied forms. A shipper can break up the end-to-end transportation process and give responsibility for all or just parts of that process to its suppliers. For example, it is common for shippers to retain the final decision on preferred carriers by lane and freight prices paid by customers.

Appendix 1: Demographic Data

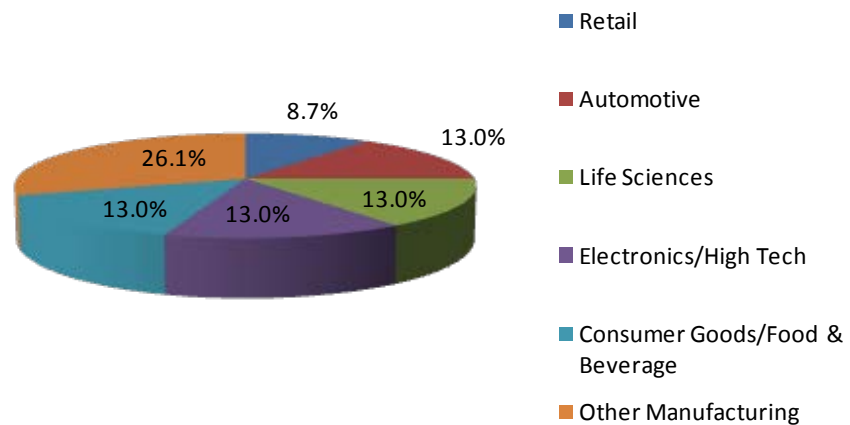
Departmental Job Titles

While a single survey respondent listed his/her job title as “manager,” with no supporting departmental data, all other respondents had supply chain titles. These titles include the terms “supply chain, transportation, logistics, distribution, fulfillment,” and “delivery.”

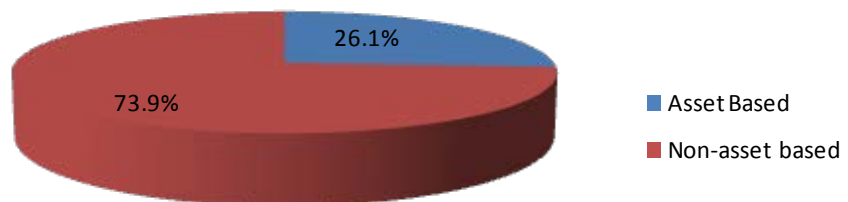
Some respondents’ titles crossed common departmental boundaries. One of these combined “procurement” with “supply chain,” one “IT” and “supply chain,” and one “customer officer” and “supply chain.”

Industry Demographics

Respondents came from the following industries:

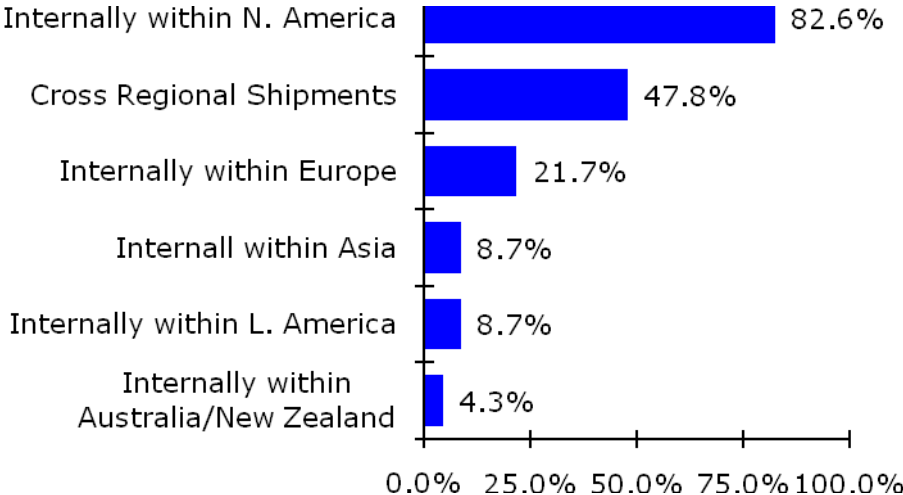


Type of Managed Services Provider



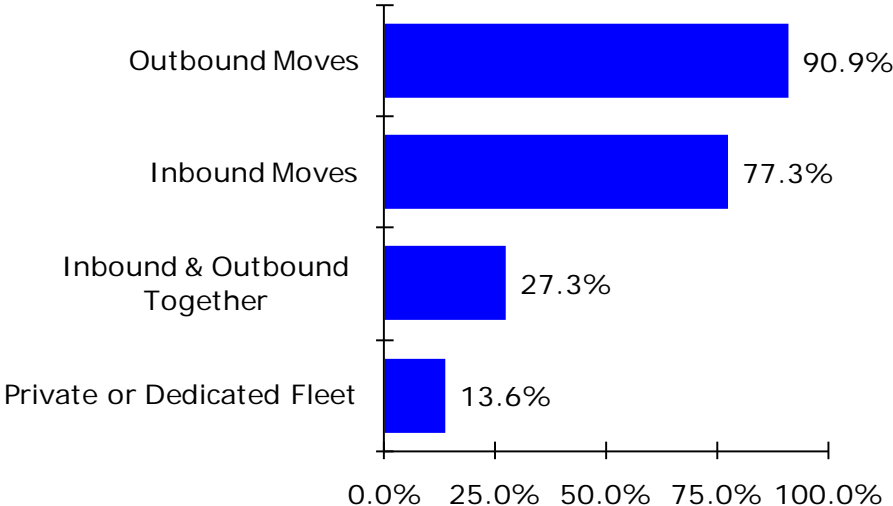
Regional Shipping Supported by the Managed Services Provider

ARC asked, "What regions are you using your managed service provider to plan and execute shipments for? Please select all that apply!"



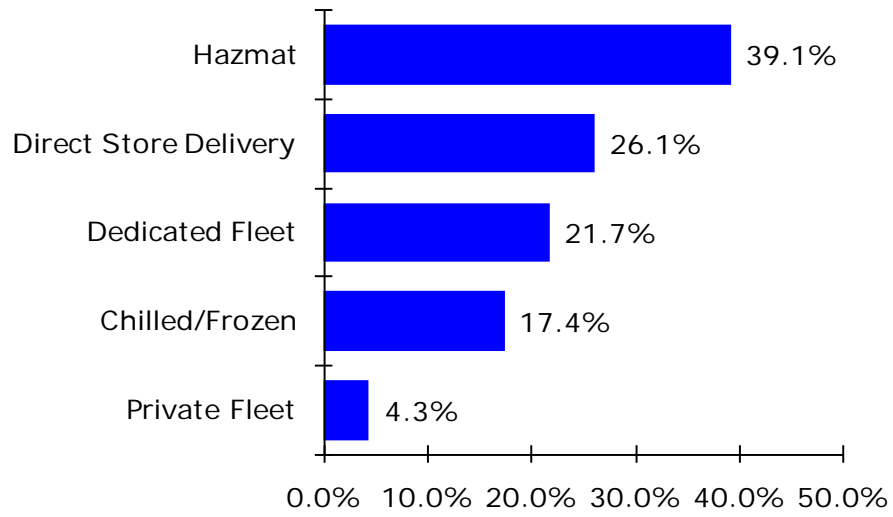
Multiple Answers Permitted

Moves Supported by the Managed Services Provider



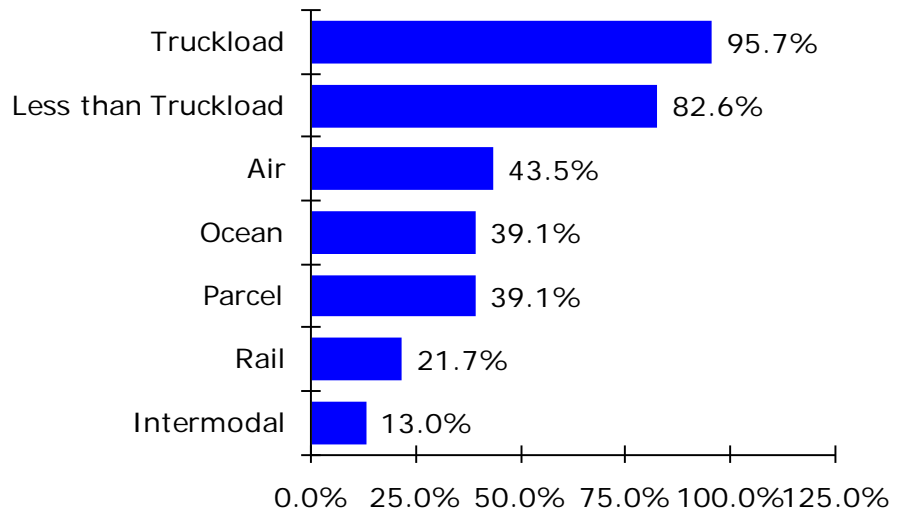
Multiple Answers Permitted

We also asked respondents, “Do you make significant numbers of shipments that have the following characteristics?”



Multiple Answers Permitted

Modes Supported by the Managed Services Provider



Multiple Answers Permitted

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Acronym Reference: For a complete list of industry acronyms, refer to our web page at www.arcweb.com/Research/IndustryTerms/

3PL Third Party Logistics

RFP Request for Proposal

ROI Return on Investment

SCM Supply Chain Management

TMS Transportation Management

System

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