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Under pressure

To placate C-Suite, US logistics managers scour ways to mitigate 2019 trucking costs

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By Ari Ashe and William B. Cassidy

FOLLOWING A YEAR when US surface transportation budgets were not just blown, but shredded and burnt, logistics managers are ripping up their playbooks and looking for new ways to control costs, if not cut them. They're working cheek-to-cheek with truckers and logistics companies to eliminate inefficiencies while placating impatient CEOs, CFOs and procurement officers.

If not, they're likely hoping to finish rewriting their resumes before being kicked off the dock and onto the curb. Double-digit increases in transportation costs, especially for-hire trucking rates, shook some of the largest publicly owned US retailers and manufacturers this year, sending shudders through financial markets and raising fears of consumer price inflation.

"Missing on the (transportation) budget has been brought up on almost every earnings call this year," said a manager of domestic logistics at a Midwest retailer. "Everybody is struggling with it. But as we roll into 2019, CFOs will expect us to find a way to manage costs better." In other words, don't expect "it's the market, boss," to fly next year.

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With transportation costs in the crosshairs, logistics managers must really, truly collaborate with carriers and logistics operators and also dig into their own operations to eliminate waste and save dollars and cents. Rates aren't falling any time soon, so that means turning over as many rocks as possible in search of savings, both inside and outside transportation, sources said.

Shippers also need to do a better job communicating with their CFOs and CEOs, and educating sales personnel, procurement executives, and others who make decisions that affect the supply chain and transportation budget — for example, the sales executive who promises next-day delivery without realizing the length of haul makes that promise impossible to keep.

"Your savior is not going to be found outside your own organization," said Andrew Lynch, president of Zipline Logistics. "You know your costs are going to be inflated over last year, and those costs were 20 to 30 percent higher than in 2017," he said. "What are you doing internally to put yourself into a position to buy better? And it's not all 'shipper-of-choice' stuff."

Re-evaluate services

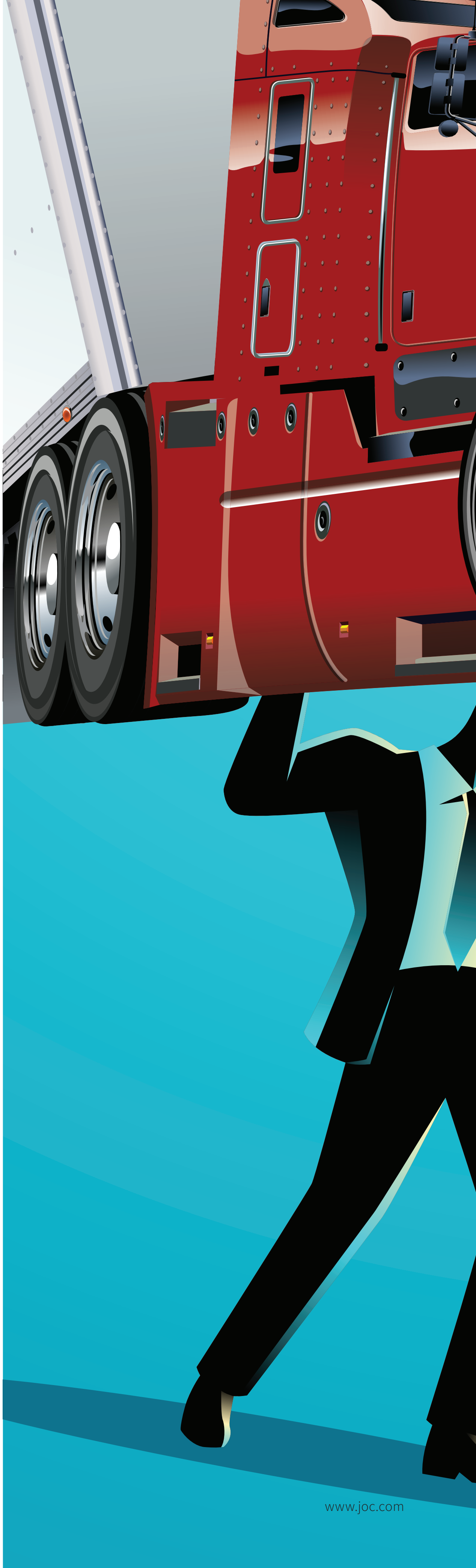
Logistics managers need to take a "more granular" look at operations in order to "buy capacity better," said Lynch, whose Columbus, Ohio, third-party logistics firm works with consumer packaged goods companies. "Think of the nuts and bolts of dealing with customers," he said, consignees who may demand freight be delivered on a Saturday or Sunday.

"There were times when sales folks were told to just say 'yes' to demands like that, but those are things that need to be re-evaluated." What's needed is a more detailed, realistic discussion of costs between not just carriers and shippers but shippers and consignees, who need to know the cost of demands such as Saturday morning delivery, or a last-minute freight tender.

The logistics manager at one Midwestern parts manufacturer said she has spent more time this year explaining the reasons for tight truck capacity and higher rates to her company's salesforce than ever before, and those conversations have paid dividends. "Those salespeople didn't understand the impact of the electronic logging device (ELD) mandate," she said.

A better educated salesforce can provide relief for stressed-out logistics managers who spend half the day fielding phone calls from irate customers wanting to know why a shipment wasn't delivered overnight or is a two-day haul. That education requires placing the supply chain directly at the heart of a company's operations and long-term strategy.

"Are we starting to re-evaluate



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the shapes of our supply chains to have them make more sense for our times?" Lynch asked. "Our times" means this "new normal" world of tight truck capacity, longer transit times, higher transportation rates, and more stringent customer demands. That last factor can be blamed on fulfillment expectations set by two-day Amazon Prime service.

Logistics managers are likely to get some relief in 2019: The meteoric rise of spot market and contract truck rates in 2018 is expected to slow, though rates won't actually drop. US contract truckload rates could rise by single-digit percentages in 2019, according to forecasts from research groups, economic analysts, and conversations with shippers and truckers.

Five percent rate hikes on average appear to be a benchmark right now. That wouldn't be "a shipper's market," but it would be a huge improvement over the rapid contract rate increases reported for 2018. Contract rates have climbed double digits this year, resulting in shippers spending up to an additional 25 cents per mile or about $100 to $300 more per load.

Also, consider diesel prices are higher than at any time since 2014. As of Sept. 10, the US average retail price of diesel, the basis for trucking and rail fuel surcharges, was up 16.4 percent year over year. West Texas Intermediate crude oil was priced at nearly $70 a barrel. This is the second consecutive year of fuel price hikes, and a third would push freight bills higher.

All that means shippers can't afford to stay on the sidelines and hope for rate relief.

The storm is here

Transportation managers need to act, while dealing with intense pressure and often some pushback. CEOs and CFOs have final approval on a budget. For publicly traded companies, CEOs and CFOs also answer to shareholders. The transportation department might request a 5 percent budget increase, but the CFO might only authorize 2 percent, or none.

"The conversations usually end with 'here is the number. Find a way to do it, get it done,'" the Midwestern retail domestic logistics manager said. In an August webinar, Mike Regan, chief relationship officer at TranzAct

Technologies, said CFOs insist on that solid rate number — whether 2 percent or 5 percent — because it affects decisions in sales and operations.

One logistics director working in e-commerce used the analogy of a wolf in a conversation with *The Journal of Commerce*. "For 10 years we've been telling CFOs that the wolf is at the door. Their response was, 'Put yourself in front of the door; don't let the wolf through the door.' Eventually, we told the CFO the door is splintering and we can see the wolf, but the CFO said hold the door," the logistics director said. "Today the door is in shambles and the CFO says, 'Stop crying wolf!'"

Motor carriers have warned shippers for years of an impending capacity crunch that would drive up costs, but many ignored the topic until it was too late. To be sure, not all CFOs put on blinders, but many expected, and still expect, business as usual and for the economic cycle to behave normally.

"You need to tell the CFO, 'I'm not sitting on my hands or putting my arms up in surrender, but you're standing on the tracks and the train is coming through,'" the e-commerce logistics director said. "You can deny it all you want, but either way the train is coming. I cannot land on budget unless you're willing to work with me, so here is my plan."

"You have to think cost optimization and dig deep to see where you can shave a penny. You have to offer a plan."

Strategic plan needed

That requires some soul-searching, said Brian Reed, a consultant and a former transportation executive with Niagara Bottling. "It has to also be a conversation with yourself," Reed added. "If the C-suite is not listening, what am I doing to get to their number? You have to think cost optimization and dig deep to see where you can shave a penny. You have to offer a plan."

And there's the rub: You need a strategic plan. "You need to make a business case for each idea and quantify it," Reed said. "There's always something else you can do that offsets rate increases," he said. "You have to have the right mindset. If you just go in and say. 'I'm going to do what I've always done,' well, you're going to get a 5 percent rate increase."

One idea is working with other departments to drive cost optimization across the enterprise. Good CFOs will allow managers to reach targets in creative ways, he said. "You've

Pay attention to spot markets

After rising by double digits in 2018, US contract truckload rates could rise a more modest 5 percent on average in 2019, and swing even farther toward shippers afterward, if the hot US economy begins to cool.

Some industry analysts believe 2019 will be a transition year in which carriers still hold power over shippers, but the grip is loosening and could be lost completely if economic growth stalls by 2020. Others understand conditions may change eventually but say a repeat of the freight recession in 2016 is unlikely to happen unless the US economy slumps into recession.

Forecasters also warn shippers they are merely making an educated guess, so a sound strategy would include paying close attention to spot markets in the next six months. Much depends on the strength of economy in 2019, and whether the balance between truck supply and freight demand swings closer to an equilibrium next year.

Shippers looking for a return to balanced conditions shouldn't set their hopes too high, based on currently available market data and projections of US economic growth. Some believe today's bullish conditions — for truckers, that is — will last longer.

The US economy seems able to absorb capacity faster than trucking companies can add trucks and drivers. US real GDP expanded 4.2 percent in the second quarter and is growing faster than 4 percent in the third quarter, according to the Federal Reserve Bank of Atlanta's GDP Now estimate.

Carriers are ordering trucks at record high numbers, but those trucks won't be built, let alone hit the road, until next year. Drivers will still be hard to hire.

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For every pro-carrier market, however, there is a pro-shipper market — CFOs just have to be patient. Often, spot rates are a leading indicator on contract pricing and history can teach us valuable lessons on the issue.

In 2014, spot market rates rose more than 25 percent on a year-over-year basis. Growth rates, however, decelerated to 15 percent by the end of 2014, and into single digits by February 2015. Eventually year-over-year spot rates went negative in June 2015, according to DAT Solutions. In the 2015 third quarter, US real GDP expansion dropped to 1 percent, and to 0.4 percent in the fourth quarter, and remained between 1.5 and 2.3 percent until the 2017 second quarter.

In the contract market, motor carriers secured rate increases in 2014 and 2015, but shippers negotiated freezes and rate cuts in 2016 and early 2017.

The spot market began to recover in March 2017, eventually climbing more than 32 percent year over year this January. Contract rates quickly responded too, growing more than 10 percent earlier this year, and by 20 percent in August, versus a year ago.

For shippers, the silver lining is that spot market rates have decelerated since January, ending August up 17 percent higher year over year. DAT predicts rates will grow in the teens through December, then further slow into single digits in 2019.

It will be increasingly hard, even with a healthy economy, to sustain year-over-year increases comparable to those seen in 2018. If history repeats itself, contract rates next year will look like 2015, then flip back toward shippers in 2020.

"There is enough pressure from the economy to continue to push rates higher but at a more moderate pace going forward," DAT industry analyst Mark Montague said. "When you look at the structural drivers — energy, e-commerce, or general economy — everything says rates will still be higher next year, but there will be moderation got to think outside transportation," Reed said. "My costs may be rising 5 percent in transportation, but my team will find 5 percent in savings somewhere else. You've got to convince them.

"You have to be able to say, 'I'm going to get the number you want, but it's not going to come just from my bucket, it's going to come from across several buckets," he said.

The right carrier for the lane

Shippers can get stuck in a money pit by using the wrong carrier in the wrong lane. Every trucking company is stronger in some regions than others. "Finding the carrier that makes the most sense in your network should be a huge effort right now. I don't care who you are, your No. 1 effort should be finding carriers that best match your network needs," Reed said.

It's a tough job, but it can be done. For example, Home Depot has more than a 90 percent tender acceptance rate because of solid communications with its carrier base that helps match the right driver with the right freight.

> "In Europe, we actually see shippers who are competitors work together on multivendor platforms. That's a new mindset."

Such a rate is well above industry average since rejection rates are fluctuating between 20 and 30 percent this year.

"We are constantly asking carriers for feedback about difficult vendors, difficult [distribution centers] to deliver to, difficult stores," Michelle Livingstone, vice president of transportation, said during a recent webinar hosted by TranzAct Technologies, the National Shippers Strategic Transportation Council, and the Council of Supply Chain Management Professionals.

"We're working with our business partners to make changes so that [each location] is a better place to deliver to or pick up from," Livingstone said. "It's a slow process, but we're plugging away at it." She said weekly communication with Home Depot's core motor carriers lets them know where they stand on tender acceptance, on time pickups, and on time deliveries.

"When we get ready to launch the truckload bids for the following year, carriers who have performed well and want to maintain their lanes will retain their lanes," she said. "We will pull them out of the bid." That's a bidding strategy transportation an-

in both the spot and contract markets."

Matthew Harding, vice president of Chainalytics, explains that it's very difficult to anticipate where the spot market will head because there are too many variables. Some of it is behavioral such as actions to counteract tariffs on Chinese-made goods. It can also be psychological, however, such as retailers panicking about empty shelves this holiday.

"What is most important to us is the differential between spot and contract rates. Coming out of August, our data shows there was a 10 percent differential in rates. That 10 percent falls below the pressure that is necessary to continue sustainable growth in contractual pricing," he said.

Based on a seasonally-adjusted reading of Truckstop.com's Market Demand Index, trucking economist Noel Perry thinks capacity has reached an apex, and spot rates will continue to fall, pulling down contract rates in 2019.

"Pricing and profits will stay strong in the contract segment through the end of the year, at least, and perhaps through the end of the 2019 first-half seasonal peak," Perry said in an Aug. 3 column published on his Transport Navigator website. In early September, however, pricing relief still seems far off.

Broughton Capital economist Donald Broughton has a different view. Rather than being in the ninth year of a recovery, he believes the consumer market is still early in the recovery cycle, with the consumer-led portion of the recovery less than 2 years old.

"Although the comparisons are extremely difficult in the first couple months [of next year], overall freight shipments and freight expenditures will be higher in 2019 than 2018," said Broughton, author of the Cass Freight Index and chief market strategist for Freightwaves.

In August, the Cass Freight Index was up 6 percent on shipments, 17 percent on shipper expenditures and 10 percent on truckload linehaul rates, not showing any inflection point.

Shippers should remember the lessons learned from this year as they negotiate rates in 2019. Next year won't be as nasty as 2018, according to Andrew Lynch, president of Zipline Logistics, a Columbus, Ohio-based 3PL, but he also doesn't "see freight markets plummeting back to where they were in 2016 for a very long time."

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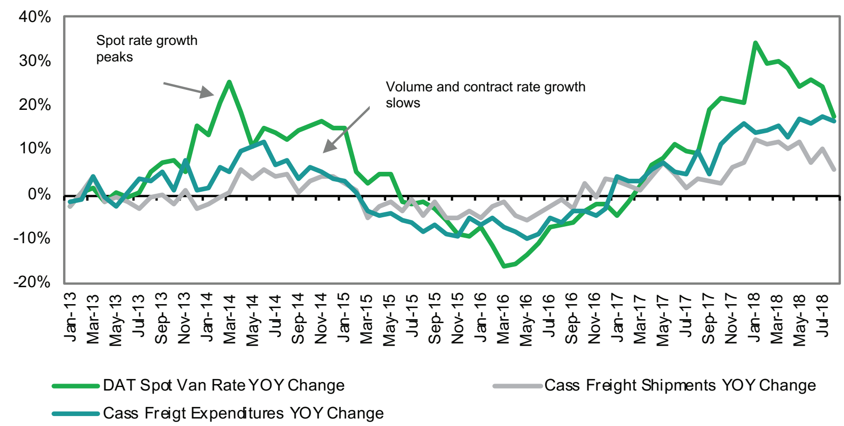
Trucking spot market trends hint at future contract levels

Year-over-year change in DAT spot van rate and Cass Freight Shipments and Expenditures



Notes: DAT rate excludes fuel surcharges
Source: DAT, Cass Information Systems

Navigating the space-time continuum

Imagine how much truck capacity could be unlocked with weekend hours. Distribution centers might be closed, but truckers are always on the road. What if more DCs were open?

"If you did a survey of how many drivers are willing and able to run on a Saturday and Sunday but can't because none of the warehouses are open, you'd be surprised by the results," said Andrew Nutting, a logistics executive formerly with Bob's Discount Furniture and TJX Cos.

Making space available on weekends may mean additional costs, but also creates much needed capacity and flexibility for truck driver hours. "Companies need to make more decisions to open up capacity rather than restrict it, or else costs will keep going up," Nutting said.

"There's tons of money to be made on the weekends," said Brian Reed, CEO of Laguna Consulting and a former transportation and supply chain executive with Niagara Bottling. "I'm surprised more people haven't gone beyond five days. It's a mental thing for people. The world operates 24/7 today. If you've stuck with a five-day week, you've just been lucky."

A Northeastern food manufacturer said it took about six months to roll out a weekend work schedule a few years ago. "It's not too hard to assemble a skeleton crew on Saturdays and Sundays," the logistics manager of the company said. "Trucking companies will offer pretty good rates to keep their drivers moving on the weekends, so it's a win for everyone."

"There's tons of money to be made on the weekends."

Speaking of time, allowing your motor carriers to plan ahead can lead to better rates. The Northeastern food manufacturer offers 12 days lead time to carriers. SanMar, an apparel shipper, sends out a three-week rolling forecast to carriers containing a preview of what freight volumes will look like. That's extremely helpful in the electronic logging device (ELD) era.

"For the next 12 to 18 months, forecasting will be the biggest challenge you have," said Andrew Lynch, president of Zipline Logistics. "Forecasting is the hardest thing to do for every department. But real-time management and building flexibility and setting expectations the right way, those are things you can achieve to get what constitutes success today."

Another way to open capacity is to plan three-dimensionally. Dry-van trailers are 53 feet long, 8½ feet wide, and 9 to 10 feet high. Shippers concentrate on length and width but often ignore height as pallets are only stacked 5 feet high. Shippers waste valuable space if they leave the upper half empty, unless the trailer hits the weight maximum beforehand.

"If we used 10 percent more space on each truck, then we would use 10 percent fewer trucks, an e-commerce shipper said. Better utilization means "fewer yard moves, less yard space, less equipment usage. Full utilization of trailers isn't discussed enough. If you're worried about your budget, fill your trucks better."

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alysts say more shippers are adopting as capacity stays tight and contract trucking rates continue to climb.

"For the last two or three years, carriers have just been barraged by an unprecedented amount of bids, from large shippers especially," said Ben Cubitt, senior vice president of supply chain and transportation at logistics provider Transplace. "When the market was good (for shippers), everybody bid. For carriers it's amazingly disruptive, not knowing what you're going to get."

At Niagara Bottling, "we would withhold business (from bids), where we thought the carrier was doing well," Reed said. "It's very hard for procurement people to do that, but there's a huge cost in disrupting the network, the lane. Sometimes getting rid of a carrier that might be more expensive but works great and bringing in someone cheaper might not work."

Finding a match

The search for carriers that make a good fit in certain lanes is increasingly intense. A food logistics manager in the Northeast explained how his employees drive to other companies' distribution centers and write down the names of carriers in their lots. His company has backhauls out the Northeast, a region where freight often goes in but doesn't usually come out.

"We write down trailer names and make cold calls trying to uncover carriers that need freight going back," he said. "We may only use them in a few lanes, but you can make a killing in those lanes and offset higher rates in other lanes." Some shippers are working with their core carriers to find other shippers to match headhauls and backhauls or manage inventory to offer a truck multiple runs. That coordination requires shipper-to-shipper collaboration.

"In Europe, we actually see shippers who are competitors work together on multivendor platforms," Bart De Muynck, research vice president at Gartner, said at the Transform 2018 Transportation Tech Executive Summit in Chicago Sept. 13. "That's a new mindset." That collaboration also underscores the importance of technology in transportation planning.

Transportation managers face a daunting task in 2019. Thinking outside the box to maximize time, space, and freight flows can be effective ways to shave money and reach hard budget targets. But the wolf is here, and it will take creative solutions to satisfy CEOs and CFOs.

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