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Helping hands

By William Epmeier

Third-party logistics providers can keep warehouse operations running smoothly, allowing staff to focus on other tasks.

When grocers first contemplate outsourcing their distribution functions, the usual motivation is to lower costs.

In general, that is not a realistic expectation according to several experts, including Steve Tompkins, president of Tompkins Associates, a consulting firm based in Raleigh, N.C. While some retailers may be able to cut expenses, he points out that it is often not the case. “You’ve got to understand where the costs in your operation are,” he says.

For example, many grocers target labor costs reductions by outsourcing to a third-party logistics provider (3PL). The fact is, he says, “3PLs will have good people, and they will deliver efficiency, but they will not be low cost.”

The third-party logistics industry has been growing briskly. The business data firm Armstrong & Associates in Stoughton, Wis. estimates the domestic 3PL transportation and warehousing business is increasing at almost 14% annually and totaled $114 billion in sales last year.

Flexibility is the real key to the growth of the outsourcing trend, according to Robert Shaunnnessey, executive director of the Warehousing Education & Research Council in Oak Brook, Ill. Outsourcing gives companies an alternative to investing in their own distribution, labor and technology.

Omer Rashid, a partner at KOM International in Montreal, agrees. “A lot of retailers are asking if building a new distribution center is the right move, and whether they have the right infrastructure,” he says.

There is an emphasis on limiting capital spending, prompting retailers to seek economies of scale, he notes. “They are drilling down and looking at vendors and commodity classes and analyzing which are best handled by outsiders. With slow-moving items, for example, a 3PL warehouse may be able to gain economies of scale by handling it.”

On the flip side, Rashid adds, companies are also looking at bringing outsourced items in-house. “It may be that because of growth in a particular merchandise category, or because of consolidation, that it now makes sense to run something through your own system,” he says.

MAXIMIZING ASSETS

With so much consolidation within the supermarket industry over the past 10 years, companies have to adjust their distribution infrastructure to reflect their current situation and future plans. The goal is to get maximum use out of existing assets.

When it comes to expansion, speed is usually an argument for outsourcing to a third-party provider, Rashid says. “We had a client recently who needed to get distribution infrastructure up and running quickly, and the best solution was to go with a third-party provider.”

Good technology is also a reason to considering out-sourcing. Most third-party providers have good quality warehouse and transportation management systems, Tompkins says, and retailers reap the benefits by hiring tech-savvy third-party providers.

Another reason to outsource, Shaunnessey says, involves labor negotiations. For example, several years ago Safeway chose to outsource a warehouse operation in California to a third party as a way to avoid bargaining with a labor union. Such moves, however, can be difficult because the ability to outsource may be prevented by the terms of previous collective bargaining agreements.

Jeff Clark, vice president of sales for ODW Logistics, a Columbus, Ohio-based 3PL, says that finding skilled warehousing labor can be a barrier to expansion for some companies, whereas for the 3PL, “hiring is a core competency when it comes to warehouse management and inventory accuracy.”

Quite aside from labor conflict, outsourcing may simply be a means for keeping a retailer’s own labor force consistently employed. In this situation, an outside warehouse operation is used to handle promotional merchandise or various inventory spikes during the year. While chains or wholesalers will pay more operationally for going outside, they save in the long run because they do not have make fixed cost investments in new facilities.

WHAT GETS OUTSOURCED?

Grocers are usually reluctant to outsource functions that they consider to be core competencies, including most warehouse functions and merchandise deliveries to stores.

In-bound freight, on the other hand, is usually one of the first functions to be outsourced, along with vehicle maintenance. Transportation costs on most in-bound freight are typically rolled into the cost of the merchandise. More and more supermarket chains and wholesalers are insisting, as part of their buying negotiations, that the freight cost component be made explicit by vendors. More wholesalers and retailers now receive credit for these freight rebates and instead contract with their own list of carriers to deliver to their warehouses more cheaply.

One other potential benefit to outsourcing inbound shipments to third parties is visibility, says John Harold, president of Business Logistics, a supply chain consulting company based in Scotts Valley, Calif. Many new transportation software programs can give retailers information on the exact status of shipments, so that if there is a delay, dock schedules can be adjusted to take care of the problem.

Another service that often gets outsourced to a 3PL is freight consolidation, which typically involves a cross-docking operation. In these cases, in-bound deliveries of small orders (less-than-truckload quantities) are routed to a specialized facility near the chain's main distribution center. These deliveries are then received, entered into the retailer's inventory system and married up with other smaller orders. These consolidated orders are then shipped out to the distribution center as truckload quantities.

Display building is also a prime target for outsourcing. Ozburn Hessey Logistics assembles and ships a lot of end-cap displays from its national network of warehouses to retailers. The Brentwood, Tenn.-based 3PL provider has many beverage, dry and frozen food manufacturers as vendors to the supermarket company.

BLENDING CULTURES

In selecting a 3PL Shaunnessey of WERC stresses that retailers consider how the companies' cultures will mesh before looking at the economics of a relationship.

In order to assess the cultural fit, retailers need to have a clear understanding of what the task they are planning to outsource involves, and their own strengths and weaknesses. For example, Shaunnessey says, "If you are a high-service retailer that focuses on quality and speed of service, choosing a low-cost provider probably does not make a lot of sense," he notes. Low price will inevitably come with more damage and variability in delivery schedules.

Tompkins recommends involving the retailer's operations and engineering staffers to see how well they interact with the prospective third-party provider. "If you just deal with sales, you'll never know how it will work out," Tompkins says.

When evaluating 3PLs, Harold of Business Logistics notes that grocery companies have considerable expertise internally. Merchandise buyers have wide experience dealing with in-bound freight companies and they know the companies that are reliable and responsive.

The 3PL's commitment to ongoing business investment is another consideration, says Derek Fain, senior vice-president of business development for Ozburn Hessey Logistics. He says: "Ask the question, 'Will they continue to invest in my business after the first year of my contract?' Is there a culture of continuous improvement?"