3PL PERSPECTIVES 2014

Inbound Logistics' 10th annual research report looks under the hood of the 3PL sector to see what makes the market tick.

BY JOSEPH O'REILLY

PERSPECTIVES

The rise and fall of the U.S. economy has had a marked impact on third-party logistics outsourcing over the past 15 years. Privation has always fueled the 3PL value proposition as companies look to divest cost centers and concentrate on top-line initiatives. But today's slow economic recovery is only fanning the flames.

Inbound Logistics' annual *3PL Perspectives* market research report documents these changing dynamics. While cost reduction remains the dangling carrot leading shippers to the 3PL well, that impetus has expanded considerably during the past several years. And the economy is a big factor.

"Inflation is expected to rise as the Fed changes its easy-cash policies; economic growth is projected to shrink; higher payroll taxes and rising fuel prices all impact the consumer's appetite to spend," explains one 3PL respondent to *IL's* research survey.

When you consider that freight volume directly correlates with consumer confidence, the impact on the supply chain is great. Beyond that, a threatening capacity shortage, rising freight rates, and stricter government regulations only exacerbate the challenges shippers face.

Companies want cushion—not just in terms of inventory, but in supply chain management execution flexibility as well. Many are hesitant to dump capital into fixed costs, whether it's infrastructure or technology. Leveraging 3PLs to assume that risk, and provide scalable solutions that ebb and flow with changing market conditions, can be a smart option.

But the greater transformation in today's 3PL landscape is the changing perception of logistics service providers. When commoditized warehousing and transportation functions dictated contractual arrangements, the idea of partnership was buried in the fine print. Relationships were transactional, pragmatic, and physical. 3PLs were "third parties," or replaceable outsiders.

That sentiment is changing, big time. As shippers rely on 3PL partners to provide more strategic oversight, and help catalyze business process change within the organization, the relationship is growing more fluid, and less analytical. Service providers are becoming an extension of the enterprise.

That's the direction in which 3PL outsourcing is moving. As shippers lean on logistics service providers to deliver more than just meat-and-potatoes capabilities fixed on tactical cost reduction, outsourcing partnerships are evolving at pace. 3PL partnerships are turning into an enduring strategy, rather than a short-term fix.

3PL Growth Continues Unabated

Similar to last year's data, 92 percent of service providers surveyed in *Inbound Logistics*' 2014 *3PL Perspectives* market research say they grew their client base by at least five percent over the past year. This compares with 90 percent in 2013, 88 percent in 2012, and 73 percent four years ago. The 3PL value proposition continues to take hold.

Following course, 93 percent of 3PLs report they increased sales at least five percent during the past year. By comparison, 82 percent indicate profit growth in excess

3PL PERSPECTIVES METHODOLOGY

Every year, *Inbound Logistics* conducts an extensive survey of the 3PL market to explore how both logistics service providers and shippers are adapting to change and pushing the outsourcing needle in new directions.

Our outreach effort comprises two parts. First, *IL* solicits questionnaires from more than 300 3PLs, asking them to detail the services they provide and their areas of expertise–geographically, functionally, and vertically. We also ask service providers to supplement this empirical data with contextual insight about business during the past year, relationships with customers, and emerging outsourcing trends.

Second, we received input from more than 5,000 3PL users to provide a counter perspective to the different elements shaping outsourcing decisions.

Inbound Logistics' 3PL Perspectives juxtaposes these two points of view to provide a robust overview of the trends that are impacting the 3PL space, and how shippers and service providers are responding.

PERSPECTIVES

of five percent, down from 85 percent in 2013. Asset-based service providers face strong headwinds investing in equipment and technology, as well as recruiting and retaining new talent. These costs are negatively impacting the bottom line.

To compensate, 3PLs are turning over stones looking for new business, whether through acquisition, targeting verticals ripe for growth (notably healthcare, chemicals, and apparel), focusing on emerging markets, or sizing up smaller companies and scaling solutions accordingly. They are also using technology – proprietary or private label – to expand their value and attract new customers, as well as cross-sell different solutions to existing clients.

"Customers want more services and better visibility for the same cost," says one 3PL survey respondent. "Technology is becoming increasing important in delivering key metrics."

This is a critical pivot point. 3PLs are leveraging this IT play to push their solutions capabilities. As big data continues to saturate the space, shippers are looking for partners that can help capture, analyze, and execute against this wealth of information. Cloud-based solutions provide networking possibilities that expand a 3PL's scale. And the integration with customer processes and data only strengthens the relationship.

Because software integration increases visibility, clients no longer fear losing control over their networks. "They realize that a strategic logistics partner can operate as an extension of their existing infrastructure," says one 3PL. "With increased regulation, volatile market conditions, and capacity concerns, shippers are forced to evaluate their relationship models. As a result, we are seeing a demand for strategic outsourced solutions at the forefront of our business relations."

The technology piece is critical, especially as shippers court new service providers. To point, 56 percent of 3PL survey respondents name technology investment as the most important challenge they face in today's market—second only to capacity (*see Figure 1*). By contrast, only 12 percent of surveyed shippers identify technology strategy and implementation as a foremost challenge (*see Figure 2*). Instead, they are turning to IT developers—and, increasingly, 3PLs—to fill this void.

FIGURE 1 **What is the greatest challenge 3PLs face?**

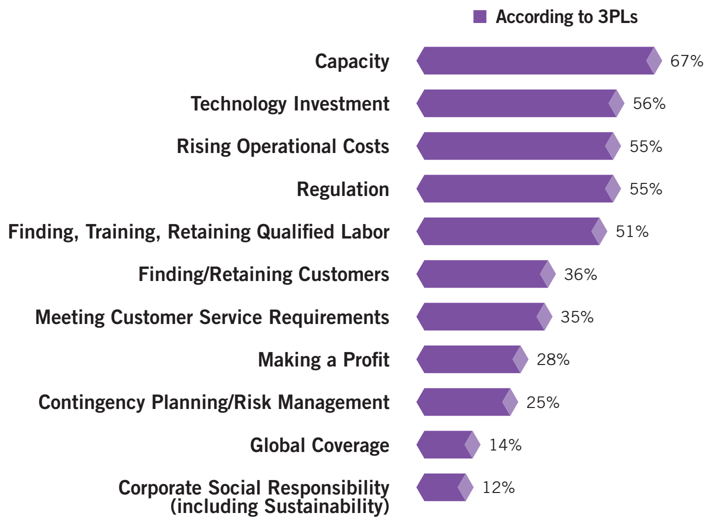
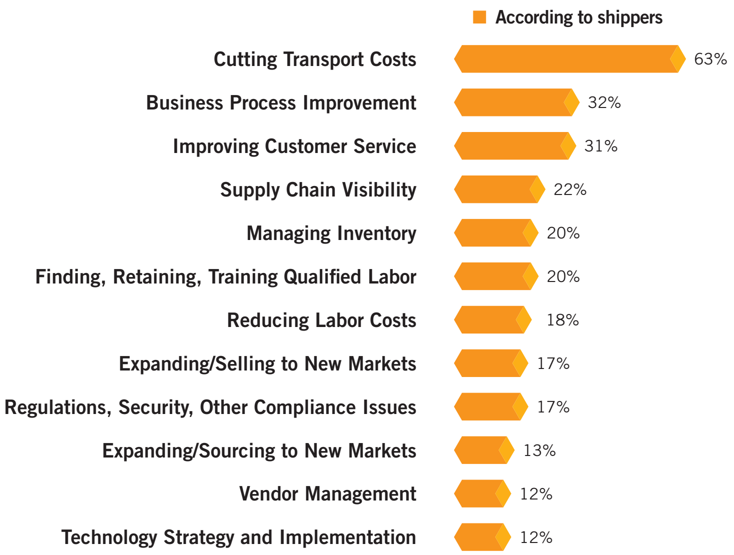


FIGURE 2 **What is the greatest challenge shippers face?**



Some 3PLs have developed their own homegrown solutions; others are secondary channels for IT companies to deliver best-in-class solutions to end users. Apart from manufacturing (93 percent), consider that warehousing, carriers, and other service providers (87 percent) are the top industry target for 3PLs, trumping even retail (86 percent). Especially with regards to brokerage operations, technology has become a commodity.

As far as specific technologies, EDI (95 percent) and transportation management systems (87 percent) have become standard offerings for most service providers: the former a means for sharing data and connecting networks; the latter a tool for assessing, benchmarking, and improving transportation operations. Optimization (68 percent) and freight payment/claims/auditing tools (63 percent) are other popular options—the latter up eight percent compared to 2013.

Notably, the survey shows a sizable spike in 3PLs that provide customer or supplier relationship management solutions (71 percent in 2014, compared to 59 percent one year ago). This is indicative of the premium 3PLs and their clients place on customer service and support, and the efficacy of using cloud networking to deploy these types of solutions.

In much the same way logistics technology has democratized supply chain management—lowering barriers of entry and raising levels of competency—logistics outsourcing is trending in a similar direction. Large global 3PLs and second-tier regional players have focused greater attention on small and medium-sized businesses (SMBs)—recognizing this remains an untapped segment.

The growth of e-commerce and entrepreneurial-minded businesses has similarly stoked new demand for logistics and supply chain execution capabilities. Seventy-six percent of 3PLs say they target companies of all sizes, while nine percent serve large companies exclusively, 13 percent medium-sized businesses, and two percent smaller organizations.

Reassessing Assets

The past several years have seen a clear bifurcation within the 3PL space, triggered by the explosion of non-asset-based freight brokers. The lines have blurred in terms of what defines a 3PL. Where transportation and warehousing assets once dominated the trade, freight brokers now flaunt technology, talent, and the "capacity" to match multiple mode requirements.

The recession hit asset-based carriers and 3PLs hard, leading to much attrition within the industry. Some even scaled back their fleets in favor of following an asset-light approach.

The 2012 federal highway funding authorization, which requires agents to carry a $75,000 surety bond, triggered greater contraction in the brokerage industry. Moreover, private equity investment continues to feed a ravenous mergers and acquisitions market.

Following 2013 data, 46 percent of surveyed 3PLs pass as non-asset-based service providers, compared to 12 percent that are purely asset-based, and 43 percent that identify themselves as both.

As capacity tightens and freight rates continue to rise, the spot market is seeing more activity. Shippers and carriers are leveraging brokerages to shop rates, find space, and maximize assets. The 3PL segment has always been typecast as countercyclical. But brokers are evergreen.

Still, capacity concerns and a looming driver shortage are slowly swinging the pendulum toward asset-based intermediaries. "As capacity tightens, we've seen a considerable shift by customers and prospects requesting asset-based fleets only, rather than non-asset brokers," notes one service provider.

Indeed, 67 percent of 3PLs cite capacity as their biggest challenge moving forward—compared to 55 percent last year—trumping technology investment (56 percent); rising operational costs (55 percent); regulations (55 percent); and finding, training, and retaining qualified labor (51 percent) as top priorities.

Transportation Rates

As capacity tightens and freight rates rise, shippers are looking for opportunities to pull costs out of the supply chain. Transportation is a recurring pain point. Accordingly, 63 percent of surveyed shippers cite cutting transport costs as their primary challenge—easily surpassing business process improvement (32 percent), customer service improvement (31 percent), supply chain visibility (22 percent), inventory management (20 percent), and finding, retaining, and training qualified labor (20 percent).

Transportation is a burning platform for shippers looking for areas to optimize. Tactical problems often prompt more prescriptive supply chain solutions. 3PLs steward this progression. Often, the hardest leap for companies is seeing the bigger picture, and understanding how different functions impact one another. The fact that shippers value business process improvement so highly—in 2012 only 22 percent identified this as a challenge—suggests they are looking more broadly at ways to improve the supply chain.

For both asset-based 3PLs and freight brokers, truckload services remains the sweet spot, with 98 percent of surveyed companies indicating as much. This is followed by LTL (95 percent), intermodal (90 percent), rail (83 percent), and dedicated contract carriage (68 percent).

The number of 3PLs providing rail services has increased 13 percent compared to 2013. Dedicated services jumped seven percent—which is to be expected, especially as capacity grows tight.

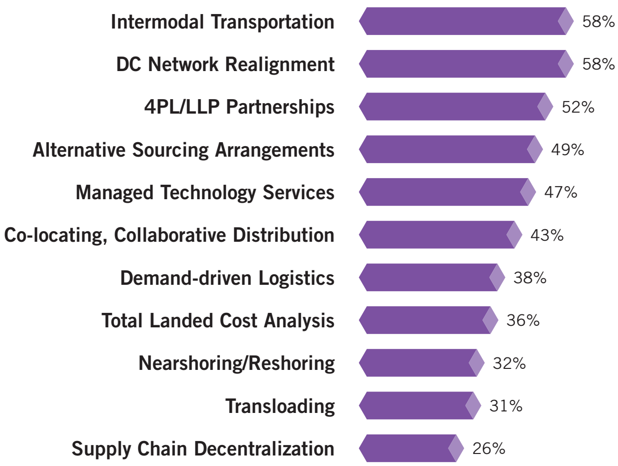
That more 3PLs provide rail/intermodal solutions speaks to the cost and capacity considerations shippers are dealing with. In fact, intermodal transportation tops the list of outsourcing strategies (*see Figure* 3), according to 58 percent of service providers. That's a seven-percent bump over 2013 figures.

"With the volatile market during the first quarter of 2014, shippers of all types are working hard to acquire as much capacity as possible to allow for possible disruptions," explains one survey respondent. "This presents an opportunity for 3PLs to display their broad expertise, and provide real value back to those customer relationships."

Mixing modes offers one ideal opportunity for shippers to engage 3PLs, find efficiencies, and reduce costs. But it's not the only way. How companies align their domestic distribution networks similarly impacts mode selection and transportation costs. As global sourcing and selling dynamics grow more fluid, and demand responsiveness accelerates, shippers have to look at the totality of their distribution footprint.

Fifty-eight percent of service providers point to DC network realignment as an important strategy for doing business—compared to 48 percent in 2013—followed by 4PL/lead logistics provider partnerships (52 percent), alternative sourcing arrangements (49 percent), managed technology services (47 percent), and co-locating/collaborative distribution (43 percent). Companies are incented to look beyond transportation, and increase visibility between different functions to find areas for improvement.

FIGURE 3 **What strategies are shippers and 3PLs using to manage current challenges?**



Changing DC Dynamics

While pricing and capacity concerns direct shipper attention to the transportation side, there is equal need for action elsewhere in the DC network. Companies can drive only so much cost out of the supply chain from better asset utilization. And a litany of market and regulatory issues are forcing shippers to consider 3PL outsourcing.

Fifty-five percent of logistics service providers view regulation as a top challenge. Hours-of-Service and CSA rules are here to stay—so, too, are the costs these regulatory provisions bring to the market. Driver recruitment has become a significant expenditure, which conflates with rising operational costs. Shippers share, and often outsource, these anxieties. That's part of the 3PL's expanding value proposition.

Other market forces come into play as well. E-commerce growth, the omnichannel dilemma, and last-mile urgency add further complexity and cost. The percentage of 3PLs that specifically target e-commerce is only increasing—this year 60 percent, up five percent from 2013. Shipper expectations for time-definite shipping and above-and-beyond customer service hold no bounds. This forces retailers, wholesalers, and even manufacturers to rethink how they manage their distribution networks.

It's little wonder, then, that DC network realignment and collaborative distribution services are popular strategies. 3PLs offering network realignment services jumped 10 percent compared to 2013; those providing co-sharing-type services increased seven percent. Shippers are more willing to share resources and capacity with other shippers on the supply side—even when there are competitive stakes—simply to reduce costs.

Planning DC strategy is contingent on unique industry requirements. But one commonality is that companies need flexibility. Far too many variables are at play in today's market—whether new sourcing locations, import/export points, shifting consumer demographics, supply chain disruptions, fuel prices—to rely on a fixed network of facilities.

Many companies have turned to 3PLs as part of this strategy, using third-party resources that have specific functional or geographic capabilities to create more latitude. The change in the past several years from functional cost outsourcing to variable cost risk aversion is notable.

Companies are also moving toward using more, smaller distribution facilities—even brick-and-mortar retail locations—to get closer to consumers and reduce costly transportation moves. Omni-channel's rapid evolution, and the acceleration of last-mile expectations, only raise the importance of tactical competencies.

Especially with regards to DC strategy—what types of facilities, how many, and where—each company approaches channel management in a different way. The market needs to mature before any tried-and-true standard operating protocol develops.

Emerging Markets

As companies address transportation and distribution planning, they similarly need to consider "big picture" supply chain scope—where they manufacture/source product, and where they sell. For many U.S.-based companies over the past decade, the balance has tipped toward import-centric sourcing. That is now changing.

Apart from functional capabilities, many 3PLs also provide global coverage. As U.S. companies look farther afield to grow brand awareness, and extend top-line projections, an obvious outsourcing synergy develops. Following 2013 data, more shipper respondents are challenged by expanding to new markets to sell into (17 percent) than source from (13 percent).

Consuming populations in other parts

3PLs UP CLOSE

Inbound Logistics' **annual 3PL survey captures insights about how today's logistics service providers are operating, and the capabilities they offer. Here's a look at the services and specialties that fuel 3PL operations.**

ASSET BASED OR NON-ASSET BASED

Non-asset-based	46%
Asset-based	12%
Both	43%

INDUSTRIES SERVED

Manufacturing	93%
Transportation (incl. 3PLs, warehousing, carriers, int'l. trade)	87%
Retail	86%
Wholesale	82%
e-Business	60%
Services/Government	56%

VERTICAL SPECIALIZATION

Consumer Packaged Goods (CPG)	83%
Food & Beverage	80%
Electronics	72%
Construction & Building Materials	68%
Apparel/Textile	64%
Automotive	64%
Healthcare	60%
Furniture	58%
Chemicals	57%
Grocery	53%
Agriculture	45%
Oil & Gas	39%
Aerospace	37%
Trade Show	35%
Renewable Energy (wind & solar)	34%

CERTIFICATIONS

SmartWay	61%
C-TPAT	45%
ISO	42%
Six Sigma	27%
Lean	24%
AIB	21%
ICCA	7%

LOGISTICS SERVICES & CAPABILITIES

Inbound Logistics	92%
Integrated Logistics	81%
Inventory Management	72%
JIT	69%
Vendor Management	68%
LLP/4th-Party Logistics	68%
Logistics Process Reengineering	60%
Payment Auditing/Processing	56%
Shared Services (co-locating, collaborative distribution, etc.)	54%
Global Trade Services	38%

TRANSPORTATION SERVICES & CAPABILITIES

Truckload	98%
LTL	95%
Intermodal	90%
Rail	83%
Ocean	68%
Dedicated Contract Carriage	68%
Air Cargo	67%
Small Package	56%
Bulk	54%
Final Mile	49%
Equipment/Drivers	36%
Fleet Acquisition	19%

WAREHOUSING SERVICES & CAPABILITIES

Crossdocking	82%
Transloading	71%
Pick/Pack, Subassembly	69%
Fulfillment	67%
Vendor Managed Inventory	63%
DC Management	60%
Site Selection	55%

SPECIAL SERVICES

Logistics/Transportation Consulting	89%
Direct to Store	73%
Reverse Logistics/ Product Lifecycle Management	67%
Import/Export/Customs	64%
Sustainability/Green Logistics	57%
Marketing/Customer Service	46%
Foreign Trade Zone	41%
Direct to Home	38%
Contingency/Crisis Planning	36%
Labor Management	31%
Security Analysis	12%
Global Expansion (sourcing and selling)	8%

TECHNOLOGY/WEB SERVICES & CAPABILITIES

EDI	95%
TMS	87%
Visibility	75%
Customer Relationship Management/Supplier Relationship Management	71%
Optimization	68%
Freight Payment/Claims/ Auditing	63%
WMS	62%
Cloud-based Solutions	60%
Wireless/RFID	50%
Sustainability	43%
ERP	40%
Predictive Analytics	28%
Global Trade Management	26%

of the world—notably Asia—are growing fast, and present ripe opportunities for both manufacturers and retailers to expand their presence. The proliferation of e-commerce similarly affords more options. Companies don't necessarily need a physical location if they have the right business model and third-party logistics partner in place.

But a large gap separates multinationals and SMBs. 3PLs that are increasingly targeting small companies can leverage assets on the ground in other parts of the world—as well as customs brokerage capabilities, carrier alliances, and technology—to bring new customers into the fold. For many 3PLs, this is becoming an expectation.

Only 14 percent of service providers identify global coverage as a challenge. Ninety-one percent of 3PLs serve the North American market, while 18 percent operate exclusively in the United States (*see Figure 4*). On the shipper side, 77 percent outsource in North America (compared to 63 percent in 2013) and 39 percent in the United States alone (compared to 30 percent in 2013). Mexico's growing share in the NAFTA trade is likely responsible for this emerging trend, especially as nearshoring competitiveness brings manufacturing back to the Americas.

Asia continues to rank as the top region for 3PL operations (44 percent), outdistancing Europe (43 percent), Southeast Asia and India (41 percent), and South America (40 percent). The Middle East/North Africa (33 percent), and Eastern Europe/Russia-Europe (34 percent) follow accordingly. There is little change in terms of the countries where 3PLs operate. As developing economies mature, Eastern Europe/Russia and South America are prime targets.

Notwithstanding the current geo-political climate in Russia, the country is projected to become Europe's largest consuming population by 2020. Doing business in Russia is difficult, and necessarily requires third-party assistance. Certain areas of South America present similar opportunities and obstacles as both sourcing and selling targets. Any 3PL that operates in Brazil needs to have customs brokerage chops to deal with labyrinthine rules and regulations. Completion of the Panama Canal will bring even greater focus on the region.

From the shipper side, survey respondents report similar global leanings. Asia and Europe are top outsourcing destinations, according to 28 percent and 25 percent of respondents respectively, followed by South America (18 percent), Southeast Asia and India (17 percent), Middle East/North Africa (15 percent), and Eastern Europe/Russia (13 percent).

North America's manufacturing competitiveness, which has received a shot in the arm thanks to more affordable energy resources and Asian inflation, gives shippers plenty of options as they plot their global roadmaps. Thirty-six percent of 3PL respondents identify total landed cost analysis as an emerging strategy for their customers (compared to 31 percent in 2013). Nearshoring/reshoring—which no doubt serves as a business development trigger for domestic outsourcing activity—receives similar consensus (32 percent).

As the North American energy market continues to develop, sourcing strategies will shift significantly. But, manufacturers and retailers will also eye opportunities to sell into some of these emerging global markets. A more export-oriented mindset

FIGURE 4 **Geographic scope**

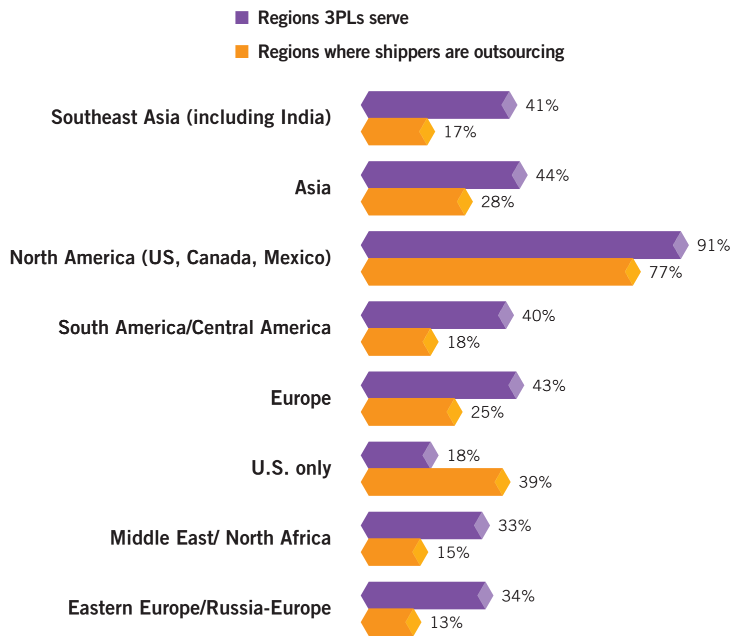


FIGURE 5
What's most important?

■ Shippers say

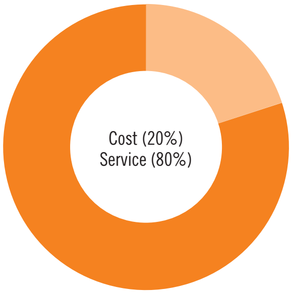


FIGURE 6
Should shippers partner with one 3PL or more than one?

■ 3PLs say

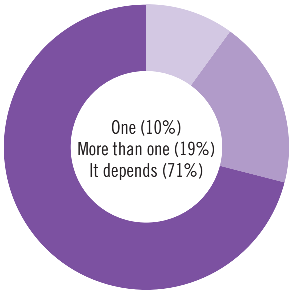
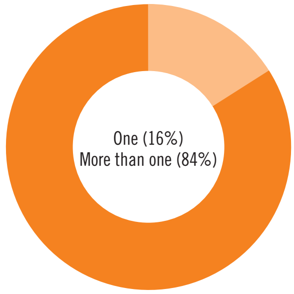


FIGURE 7
How many 3PLs do you use?

■ Shippers say



presents different challenges for shippers, especially small and medium-sized businesses that are new to the game.

Service vs. Cost

When the U.S. economy tanked in 2008, the cost vs. service pendulum swung away from service as shippers became myopically focused on squeezing as much inefficiency and waste as possible out of the supply chain. 3PLs willingly embraced the challenge because it fed their business model. That austerity mindset has stuck. But as capacity tightens, and freight costs rise, pricing becomes less negotiable.

Shippers are losing leverage as carriers and asset-based 3PLs gain the upper hand. So, they are now rallying around customer service. This year's research documents an interesting change in perception: 80 percent of shipper respondents value customer service over cost when measuring a 3PL's value (*see Figure* 5). This represents a 16-percent jump from 2013, and clearly reflects changing sentiment in the market.

Perhaps Pareto's 80/20 business axiom has new meaning as companies recognize the risk of poor customer service. When costs are passed along, and consumers and/or business partners are paying more, that leaves less room for exceptions.

A more service-oriented shipper mindset plays into the 3PL value proposition, especially for asset-based service providers that have long lobbied customers to consider the importance of partnership. Now, more than ever, that advice resonates.

Fifty-one percent of shippers cite poor customer service as the number-one reason for botched outsourcing partnerships, followed by failed expectations (25 percent), and cost (nine percent), among other considerations. These results suggest that companies are willing to pay for quality service. Partnerships built around financial metrics are fraught with risk.

This hyper-focus on service and quality is segmenting the 3PL industry. There's no shortage of service providers with specialized capabilities, whether by vertical, geography, or function. Shippers have myriad options. The day of single-sourcing all transportation and logistics activities to one partner has largely passed. The risk of over-promising capabilities and failing to deliver is too great.

Accordingly, 90 percent of 3PLs (88 percent in 2013) say customers should consider partnering with more than one service provider, while only 10 percent feel customers should work with one partner (*see Figure* 6). Shipper respondents share a common view—84 percent use more than one 3PL, while only 16 percent have found a one-stop-shop solution (*see Figure* 7). ■

2014 TOP 100 3PLs

Inbound Logistics' Top 100 Third-Party Logistics Providers list, as selected by *IL* editors, complements *3PL Perspectives*. This annual list celebrates logistics service providers that are at the top of their game, while detailing the broad array of services and solutions they provide.

Pulling together this list of Top 100 3PLs demands a great deal of due diligence. More than 250 companies submitted questionnaires for consideration this year, and *IL* editors conducted a careful analysis of surveys, phone interviews, and online research to qualify and vet these selections.

After you process *3PL Perspectives* and parse the Top 100 list, we would like to know what you think. Does the information we provide serve as a resource for your business? Does this information support trends you see in your own day-to-day operations? Let us know. Email: editor@inboundlogistics.com