How to Create a Transportation Spend Management Plan

TranzAct Technologies Inc.
Logistics Management Solutions

An "Inside Out" Orientation to Transportation

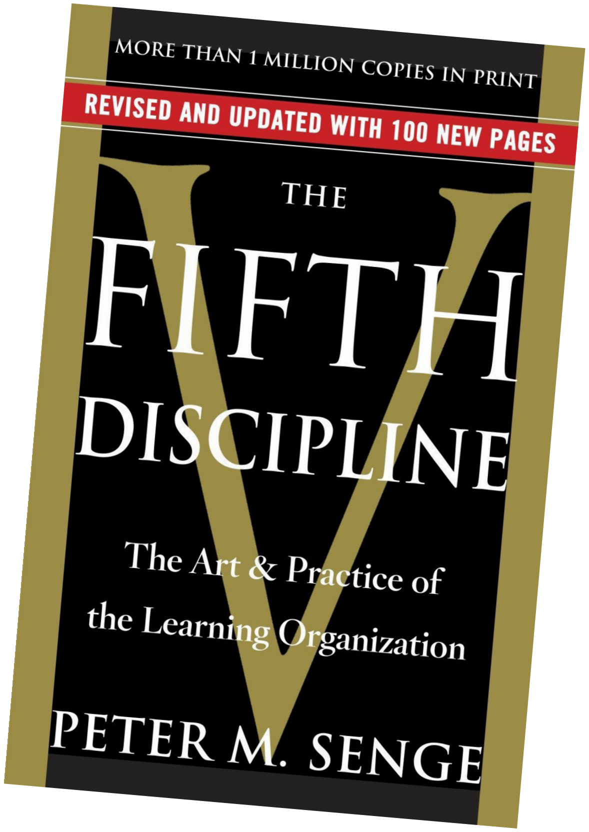
What comprises an "Inside Out" Orientation to Transportation?

One of the major challenges most companies face in controlling their transportation costs the "Outside In" orientation they take. This orientation has a major impact on their ability to truly control how much they spend on freight.

This eBook will help you understand the value of an "Inside Out" orientation, and how it can result in significantly lower transportation costs for your company. Second, it will show why the creation of a written, comprehensive Transportation Spend Management Plan (TSMP) is essential for effectively controlling your transportation spend.

Many companies have written documents that address strategic plans, sales strategies, IT requirements, operational issues and other important areas. However, most companies do not have a written TSMP. Consequently, they lack a holistic view of their corporate transportation costs.

Creating a TSMP will help you take a "Systems Thinking" approach to your transportation spend, understanding how to control costs from both inside and outside your organization. Systems Thinking is a concept outlined in Peter Senge's business classic, "The Fifth Discipline."



Why Freight Has Moved to the Forefront

The Perfect Storm that was 2018

As shippers reflect back on last year, many are asking:

"What happened?"

It was obvious from the start that most companies would blow their annual freight budget. Just five months in, 148 CEOs from the S&P 500 had already highlighted transportation as adversely affecting their profitability.

2018 was a year that exposed the "fault lines" in the way many companies manage their transportation costs. Those with a "status quo" approach to managing their freight dollars were caught off guard by the magnitude of carrier rate increases.

They also lacked the ability to effectively implement strategies to contain or manage the impact of these increases.

Electronic Logging Devices

The enforcement of ELDs drastically reduced the distance drivers were allowed to travel, causing many lanes to be extended. Former one day lanes became two, and so on....

Driver Shortage

As drivers age out of the workforce, qualified replacements have been hard to find. Even with increased wages, many young people don't see truck driving as an attractive career.

Natural Disasters

Hurricanes and storms piled right on top of each other compounded infrastructure damage, disrupting networks, and hogging existing capacity for recovery efforts.

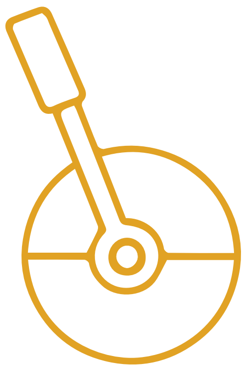
Economic Growth

Continued economic growth at a rate above 2.5% meant demand for freight continued for raw materials, consumer goods, and most business sectors.

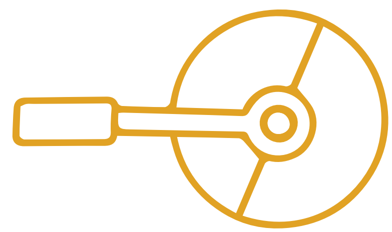
These companies possessed an “Outside In” orientation to manage their freight costs. They relied on a few traditional levers.

The principal lever they used was negotiating rates with their carriers or third party providers. Second, many shippers employed consolidation strategies and mode shifts to decrease overall shipment costs. Finally, some more strategic shippers looked for ways to become more carrier friendly.

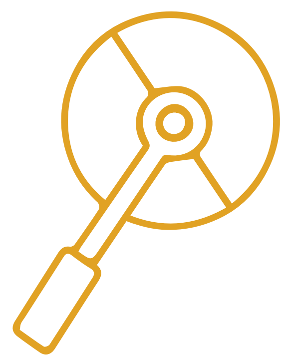
> *“There is a set amount of freight to be moved, and our job is to move it at the lowest possible immediate cost.”*
>
> *–“Outside In” Oriented Shipper*



Rate Negotiation



Consolidation/ Mode Shifts



Carrier Friendly Process Changes

These are all part of a sound plan for managing freight costs, but they exclude much of what is impacting those costs. A key assumption is present in these strategies: “There is a set amount of freight to be moved, and our job is to move it at the lowest possible immediate cost.”

To make this assumption is a critical mistake that prioritizes current savings over long term spend.

"Why?"

Companies who manage from the outside in see their need for capacity as a static variable, but that is not the case. The number of carriers they need to get their freight moved changes. The cost of moving freight is not constant in terms of KPIs such as percentage of freight costs-to-sales or freight costs per pound.

These companies rarely look inside their own organization to analyze how the decisions they are making in departments across the company impact their end to end supply chain (Procurement, Sales, Operational, and I.T. areas) and the business practices and processes in these areas affect their consumption of freight.*

Carriers view these companies as "transactional shippers" who emphasize their carrier rate negotiation process with a focus on obtaining the lowest possible rates, while eschewing building partnerships. Traditionally, transactional shippers place little value on input from their carriers regarding potential internal changes that could ultimately reduce their freight costs.

Maintaining their orientation on things outside their walls, these shippers are essentially telling carriers: "This is the way we do business, so price your services accordingly!"

**Consumption being defined as the number of shipments or freight movements necessary to support their supply chain. There are several examples of changes companies can make that can significantly impact things like the cost per pound, or the number of carriers that are required to move freight into or out of a company's facilities .*

What does an “Inside Out” orientation look like?

A better way to manage freight costs is to adopt and Inside Out orientation.

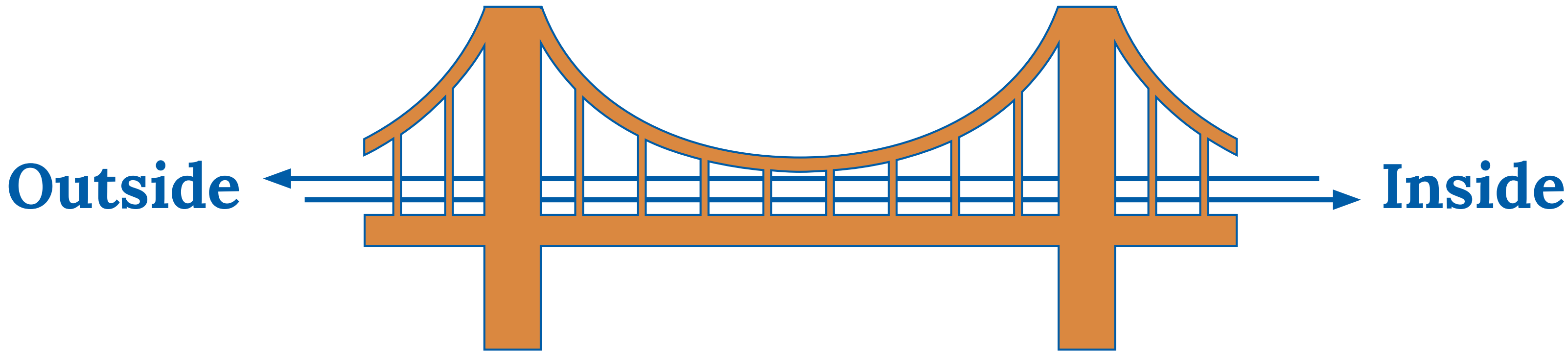
Companies who are truly committed to effectively managing their transportation spend recognize that the objective isn’t just getting freight moved as cheaply as possible. Additionally, they know that there are some critically important variables that can significantly lower their corporate transportation costs and increase their profitability.

So, what are some of the distinguishing factors for companies that have an “Inside Out” orientation?

First, they understand that the internal decisions they make throughout the total supply chain areas will have a significant impact on the consumption of freight they need to meet their supply chain requirements.

Second, they ask the strategic question: What changes can we make inside our organization that could significantly impact how much freight we have to move, the number of shipments it will take, and how many carriers we will need?

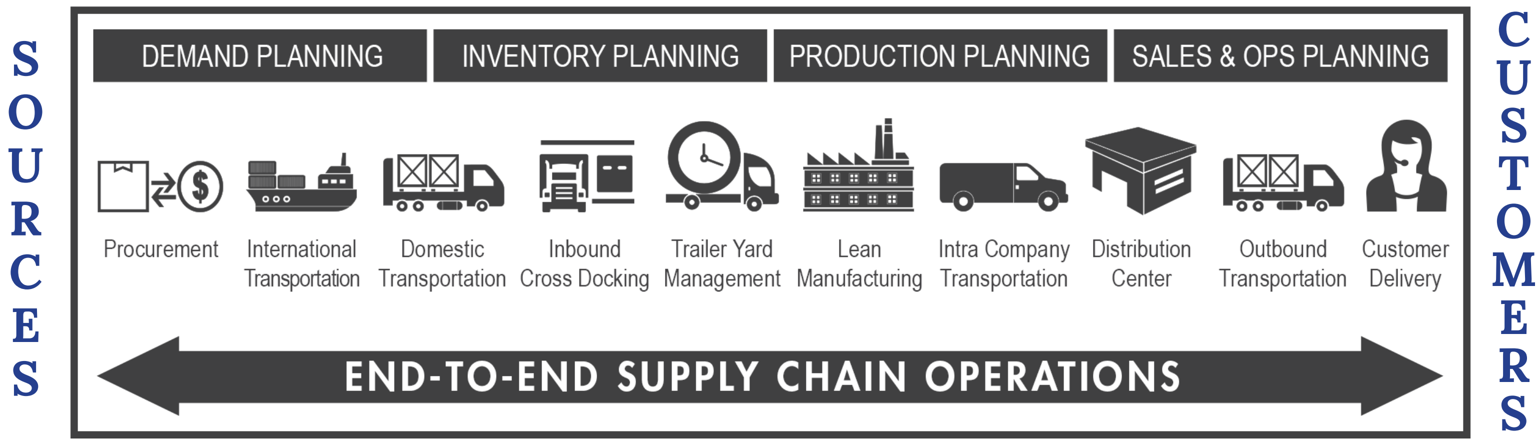
What changes can we make inside our organization?



Changes inside your organization will impact what happens outside your walls.

Applying Systems Thinking to Freight

Understanding that freight is a derived demand, these shippers know that the decisions they make in areas outside of transportation still impact the cost of freight. Furthermore, they understand the significant impact those freight costs can have on their overall corporate profitability. Finally, these shippers realize that managing from the "Inside Out" versus managing from the "Outside In" can help them achieve a sustainable competitive advantage.



As a result, these companies study their organization and create a written TSMP that details:

- How their business processes affect the consumption of freight
- Strategies and tactical steps to manage these business processes and practices
- An analysis of how changes in these processes and practices will affect their Procurement, Sales, Operational, IT and Logistics areas
- The resources that will be required in to effectively manage and maintain these changes, including KPIs for documenting progress
- A prioritized plan for implementing changes and documenting rationale for that prioritization
- An overview of the transportation marketplace and its likely impact on freight costs over the next 24 months

Freight Costs are Affected Internally

Following are a few examples of how freight costs are impacted by decisions made at different parts of the organization to give you some ideas as to what types of analysis go into creating a TSMP.

How Freight is Impacted Inside Your Organization

Manufacturing Delays Impact Your Freight Costs

Changes to your manufacturing schedule can drastically impact freight costs. Consider this real life example where a prepaid order that was originally set up as a single outbound shipment instead took three shipments to complete due to delays creating the product.

Going from a suburb of Chicago, IL, to Arlington, VA, the cost for **multiple shipments meant a much greater total freight cost** than if manufacturing had been able to stick to their schedule.

Original Order	Weight (lbs.)	Cost
Wood Dale, IL to Arlington, VA	5,575	$648.63
Actual Shipments		
Shipment #1	3,750	$549.90
Shipment #2	1,400	$243.60
Shipment #3	425	$106.04
TOTAL	**5,575**	**$899.54**

A cost difference of $250.91, or 27.9%!

This is just one of thousands of orders companies make every year. Consider how many increases of this type your company experiences.

What changes can you make to your manufacturing processes that would increase your fill rate and decrease your total freight spend?

How Freight is Impacted Inside Your Organization

Procurement without Transportation in Mind

It is common for procurement to look for products at the lowest available price. However, they often fail to look at the **total landed cost**.

We found a recent example where a company's sourcing organization was measured on **lowest acquisition cost for each item—excluding freight**.

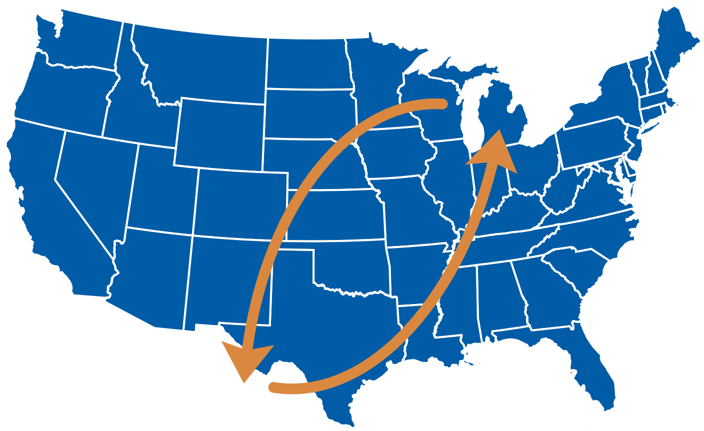
One part of the organization was tasked with sourcing 30 gallon fiberglass fuel tanks. A second group was charged with getting fuel gages for the tanks and having them installed prior to being sent to the manufacturing site for installation in the final product.

The first group found the best price for fuel tanks was in central Wisconsin. The other found the best pricing for fuel gages, along with their installation, was just across the Mexican border. Each of the these separate groups thought they were successful because they have acquired their respective products and the lowest cost.

So what happened next? The company had to ship empty fuel tanks (mostly air with very little weight) from central Wisconsin to just across the Mexican border near Texas. The fuel gages were installed in Mexico and then shipped to the final assembly plant in back north in Michigan.

The Transportation Department did as they were requested and found the best rates they could, but there was no one looking at the overall flow or total landed cost of not only the tanks, gages, and installation, but the wasted dollars spent shipping products long distances.

In this example, the cost of shipping far outweighs the savings on acquisition.



What procurement changes can your company make to avoid unnecessary freight costs?

How Freight is Impacted Inside Your Organization

Understanding Freight Purchasing Power in Procurement

Inbound purchases where the cost of the product and shipping are bundled as one price can often mean a firm is paying more than they should.

More advanced purchasing organizations like to know a total landed cost, as discussed in our previous example. However, while they use this to compare one supplier to another, they rarely take the time to **separate the product cost from the freight cost**.

Therefore, while they can compare one supplier's product cost to another on an FOB origin basis, they cannot account for who is in the best position to purchase the freight from the carriers.

A recent example of this was a company whose supplier was sending product with freight that was being purchased unbundled. But when this firm explored the market themselves, they discovered that their large size would allow them to ship the same freight at a rate that was 15% cheaper!

Unless your company does a formal analysis of all the product they plan to purchase, they will not **understand who is in the best position to buy freight**. Without this knowledge, they could be leaving significant dollars on the table.

Do you know who is in the best position to buy freight—you or your suppliers?

How Freight is Impacted Inside Your Organization

The Potential Hidden Costs of Free Freight

Generally, the concept of free freight is designed to encourage a customer to order more at one time. However, if it is not set up or monitored properly, your costs cost can get out of line with the original intention.

For example, a firm sets up a free freight policy on all shipments over $550. In this case, that amounts to a shipment size of 550 pounds with an average freight cost of $20.50 per CWT.

However, prices increase over time. Two years later, the unmonitored free freight is still set at $550, but now the $550 only buys 475 pounds of product, and the actual cost for shipping this amount is now $46.25 per CWT.

The dramatic increase occurs because the pricing for shipments under 500 pounds falls into a higher cost shipping bracket. **What had initially been designed to encourage customers to by more, and save the firm shipping costs, has now become higher cost**—most likely without anyone knowing.

Free freight can easily get out of control.

Are you aware of how your sales policies are currently affecting your freight costs?

Undefined Service Strategies by Customer Type

Many firms set their service offerings to be the same for all customers. They want to be all things to all customers at all times.

This commonly results in situations like the following. Smaller customers place small orders daily or every other day as compared to larger ones that order weekly or bi-weekly with larger orders.

The internal cost of servicing the small frequent orders is the same as the large orders with the possible exception of warehouse labor for orders of grealty different sizes. However, **the freight costs on a cost per pound basis is often more than double for those smaller orders**.

Firms that have encountered this situation have taken a couple of different but coordinated approaches such as first segmenting their customers by a defined category and varying the service offering to each category to support customer's business needs and the firm profitability.

One example might be to define shipping dates by geography for a defined set of customers that generate a certain level of sales. Another approach is to defer smaller customers to distributors that are better suited to handle small frequent orders.

Are you trying to be all things to all customers?

Level 1

Deliveries will be made on a scheduled basis to save on costs.

Level 2

Deliveries will be made on demand to meet service levels.

So Let's Get Started

By now, you can see how the decisions made inside your organization can have a major impact on your freight costs. There are many ways to save on freight costs beyond negotiations with your carriers. However, supply chains can be complex, and therefore you must have a plan in place that can look at all the factors and determine the best policy going forward. Following are some sample documents to help you consider areas where you can begin to form a Transportation Spend Management Plan of your own.

Example #1: Sales Policies

What's our Sales policy regarding free freight?

POLICY / THREAT
"Free freight", rush orders, using customer carriers

SCENARIO
Concessions and gimmicks that look like a solution to earn sales actually increase the order fulfillment cost and potentially reduce the product and customer profitability.

KEY METRICS
Variance between actual delivered cost vs. least cost delivered expense, Customer and Product profitability reporting

How are we currently managing our freight in this area?

How is this policy impacting our business?

What strategic options do we have in this area and who is involved?

What mitigating issues are there?

When did we last review this policy?

Estimated Current Associated Spend:

Potential Costs/Savings?

Estimated Future Spend:

Example #2: Finance Policy: Keep "Lean" Inventory

What's our Finance policy regarding inventory?

POLICY / THREAT
Keep inventory low, focus on inventory turns.

SCENARIO
Purchasing orders the smallest quantities it can on a weekly basis, paying Parcel or minimum LTL rates which is typically 2-4 times the cost of a non-minimum order. Larger shipments should be considered and encouraged where possible.

KEY METRICS
What is the "total landed cost"? Total landed cost = The inventory carrying cost of the product plus the freight costs per unit and the receiving and accounting costs for handling the purchase order.

How are we currently managing our freight in this area?

____

____

____

How is this policy impacting our business?

____

____

____

What strategic options do we have in this area and who is involved?

____

____

____

What mitigating issues are there?

____

____

____

When did we last review this policy?

____

Estimated Current Associated Spend:

____

Potential Costs/Savings?

____

____

____

Estimated Future Spend:

____

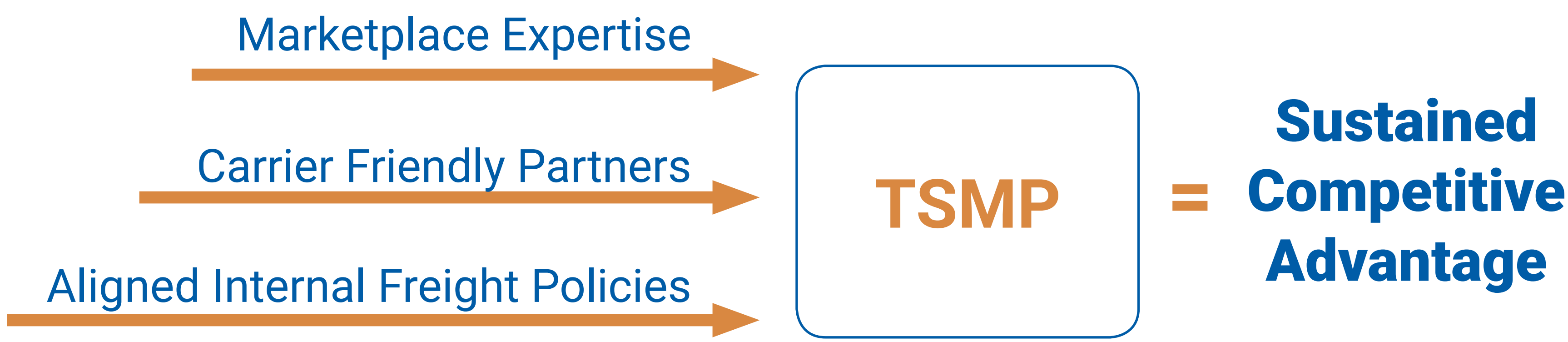
Maximizing Your Dollars

These are just a few examples that show how the decisions made inside your walls dramatically impact your freight spend—and your bottom line. In most of these cases, intentions are good, but the larger transportation picture is not being seen by the organization. There are plenty of other areas your organization can look at to free up freight dollars.

This is where the TSMP comes into play—**to maximize every dollar spent**.

An effective TSMP will help you address a comprehensive array of issues that ultimately determine the amount of freight your company consumes to support your supply chain and sales requirements.

Once your internal policies have been examined and strategic options outlined, the potential savings can be quantified and prioritized. Add to that carrier-friendly practices and an understanding of the marketplace as a whole, and you have a comprehensive Transportation Spend Management Plan that positions your company to outperform the competition.



Quantifying the Impact

The issue is not whether opportunities exist; it is determining which opportunities have the highest ROI and financial benefits to the organization.

Every organization is different. There may be areas where certain processes cannot be changed. In some cases, the gains from servicing customers may outweigh the benefits of freight savings.

But in almost every case, there are significant savings opportunities that can be realized, and often it is simply a matter of determining how long the process changes will take and then deciding upon the order in which to move forward with them.

Operational Area for Change	Current Spend	Future Spend	Savings Opportunity
Procurement Example #1	400,000	200,000	200,000
Procurement Example #2	340,000	300,000	40,000
Sales Example #1	250,000	200,000	50,000
Distribution Example #1	400,000	320,000	80,000
Distribution Example #2	400,000	200,000	200,000
Customer Service Example #1	340,000	300,000	40,000
Shipper of Choice Example #1	400,000	320,000	80,000
Shipper of Choice Example #2	400,000	320,000	80,000
Total	**3,580,000**	**2,560,000**	**1,020,000**

How TranzAct Can Help

Take the next step.

Most organizations we talk to believe a TSMP would indeed give them an edge over their competition. Some even try to put one together on there own—a great start.

But many companies also know they need some help in putting together a written, comprehensive plan. We can help.

We can work with you to study your organization, build a plan, and help you execute that plan to perfection.

We will get your company on the same page when it comes to freight, ultimately reducing your costs while maintaining or improving your services. We will strengthen your carrier relationships and bring unparalleled marketplace expertise to your organization.

Give us a call, and we can get started on your Transportation Spend Management Plan and put you on the path to becoming an “Inside Out” oriented shipper.

About TranzAct Technologies

We save our customers money by reducing their freight costs.

A Nationally and Internationally Certified Women's Business Enterprise, our superior technology, quality processes, and comprehensive network help our customers reduce costs while improving services.

Our solutions provide shippers of all modes with freight audit and payment, reporting and TMS applications, rate negotiation and procurement savings, contract development, consulting and analysis. With offices around the globe, we serve our clients on a 24/7 basis.

Access more great information online at:
https://info.tranzact.com/transportation-market-storm-center

TranzAct Technologies, Inc.
360 W. Butterfield Rd., Ste. 400
Elmhurst, IL 60126

630.833.0890
solutions@tranzact.com

www.tranzact.com