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White Paper



Logistics Outsourcing:

Change from a *service-provider* to a *business partner* – Leveraging partnership models to create sustainable bottomline.

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Logistics Outsourcing:

Change from a service-provider to a business partner – Leveraging partnership models to create sustainable bottomline.

Introduction

Logistics outsourcing is an increasingly complex discipline, which must be optimized and synchronized as an extended supply chain system within the main business-line. Contrary to the popular belief, the key here is not optimization but ‘*synchronization*’, which requires a strategically-fit design, along with deep logistic capabilities and a streamlined infrastructure to offer low cost and excellent service. If it is not, then companies will face excess inventories, cost increases, variability in supply and poor customer service.



According, to Cap Gemini Ernst & Young US LLC 8th annual report, more than 78% North-American, 79% Western European and 58% of Asia-Pacific respondents indicate that they outsource 3PL (third party logistics) services. However, more than 70% of all respondents view their 3PL as a "**resource provider**," whereas only 24% of Western Europeans (and 43% North Americans) view them as a "**resource manager**" [1].

The debate then comes down to figuring out whether today’s *logistic outsourcing* industry is just a third-party service provider or is it actually moving up the value-chain and transforming itself into a successful ‘business-partner’.

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Industry Structure - Logistics Outsourcing

Depending upon the segmentation of customer needs, the logistic outsourcing industry can be divided into 4 parts:

1. **Insourcers:** The companies (customers) which have an in-house transportation and warehousing service and hence do not outsource their logistics, come under 'Insourcers' segment.
2. **Foundational Outsourcers:** They focus on outsourcing the 'bare-minimum' logistic activities – transportation, warehousing and freight forwarding only. They are primarily based on *cost-of-service* and are fast switchers from one service provider to another.
3. **Lead Logistic Outsourcers:** They demand higher integration and seek wider range of services including – packaging, retail preparation, shelf-stacking and removal of data complexities. They are more of process oriented than objective driven.
4. **Full Spectrum Outsourcers:** They are widest range of service providers taking care of complete planning, control, execution and technology. They obey high process conformance and exuberate economies of scale.

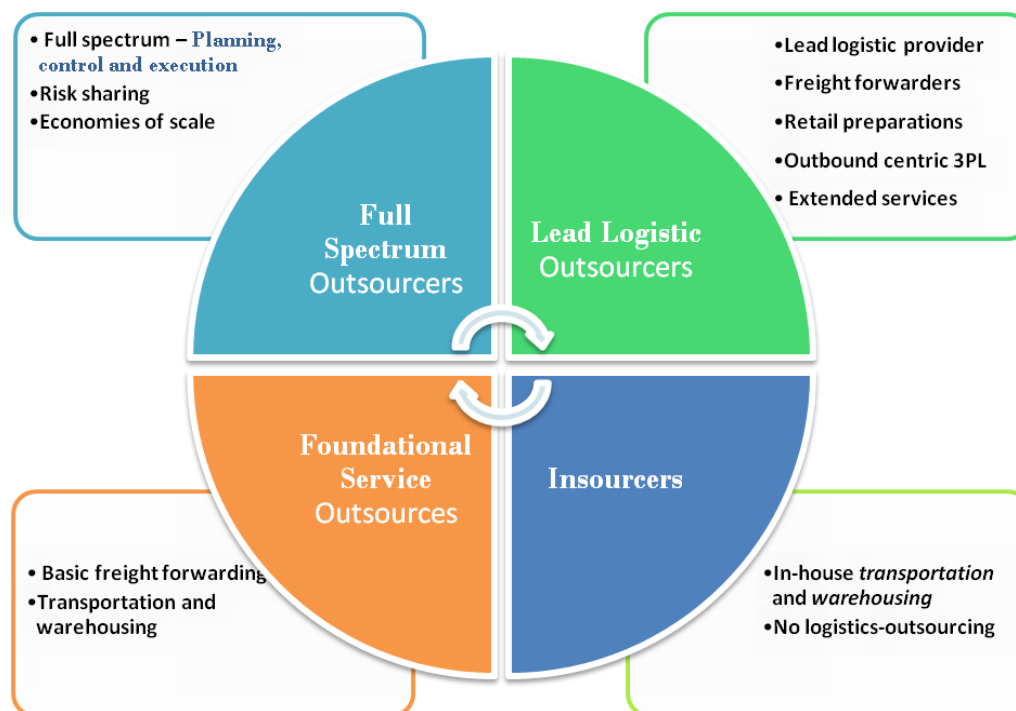


Figure 1: Segmentation of Logistics outsourcing industry

Two way Network-Effects

The most important characteristic of the Logistics-outsourcing industry that it carries is the *two-sided-network effects*. Any ‘logistics-outsourcing’ decision always consist of two parties – *Supply Side* (outsourcing solution provider) and *Demand Side* (Client). The success of the project is dependent upon the ‘**balance**’ between the Supply-side and the Demand-side.

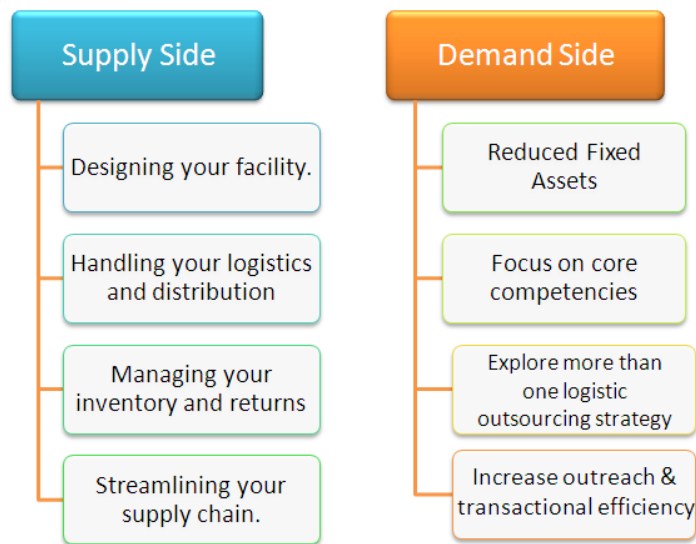


Figure 2: Supply Side and Demand Side for logistics outsourcing industry.

Only if the supply-side is able to meet and exceed the demand-side’s expectations, can the deal be struck.

Drivers for Logistics outsourcing

With the growth of Logistics outsourcing industry, the criteria of choosing the correct partner for outsourcing has also become more complex. There is no Single factor for selection, rather a huge set of *factors* to choose from.

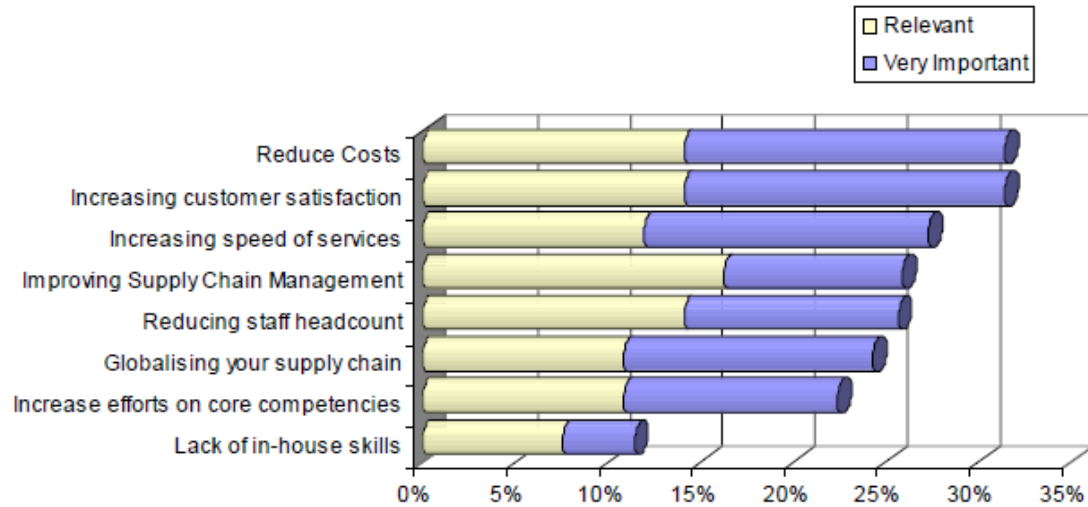


Figure 3: Key decision factors for outsourcing the logistics [1]

Deductions [1]:

From the above data, it becomes clear that the two biggest ‘drivers’ in choosing logistics outsourcing are - **reducing costs** and **increasing customer satisfaction**. This confirms that shippers continue to predominantly view 3PLs as tools for reducing costs and improving their basic logistics services.

On the other hand, new factors like “**improving supply chain management**” and “**need to concentrate on core competencies**” have also started to make their way in the list of *popular* criteria for taking up logistic outsourcing.

This seems to suggest that the opportunity to improve overall supply chain management systems and allow clients to concentrate on the non-logistics related aspects of their business, is slowly catching up with the shippers.

Hence, *logistic-outsourcing industry is increasingly transforming from just being ‘service providers’ to becoming ‘supply chain partners’.*

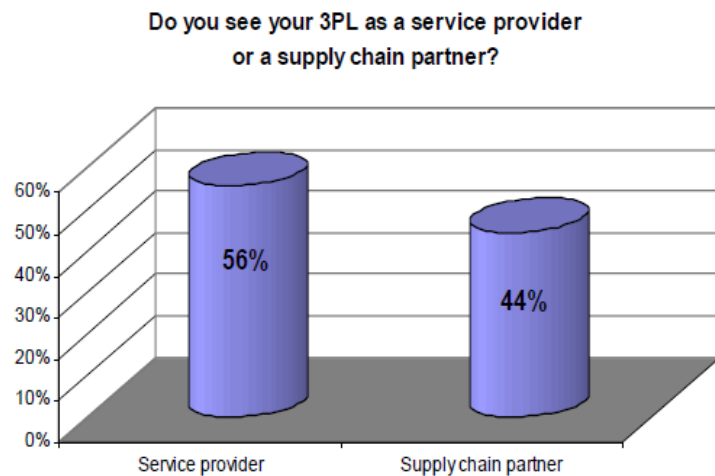


Figure 4: Service Provider vs. Supply chain partner [1]

From Service providers to Business Partners

Over the past 10 years, we have seen huge changes in the Logistics outsourcing business model.

Third-Party-Logistics (3PLs) have long led the way in logistics outsourcing using their core business - forwarding, trucking and warehousing. However, today this offering has become a commodity-service and does not provide any competitive advantage.

Customers, anxious to increase their competitiveness, want improved and more integrated value propositions.

This has led to an altogether new ‘**partnership**’ based business model wherein the outsourcing company brings to table - its own perspective, knowledge, experience and technology to undertake a full-spectrum of activities from *planning, controlling, executing and organizing* the whole logistic process.

Outsourcing Model	Relationship & Pricing	Key Attributes
4PL (Fourth Party Logistics)	<ul style="list-style-type: none"> ➤ Partnership Based ➤ Strategic Relationship ➤ Risk Sharing (and Revenue Sharing) 	<ul style="list-style-type: none"> • Complete Planning and Control. • Knowledge- and information-based • Process Conformance • Adaptive, flexible, and collaborative
LLP (Lead Logistics Providers)	<ul style="list-style-type: none"> ➤ Contractual ➤ Some risk sharing 	<ul style="list-style-type: none"> • Project management/contract management • Single point of contact • 3PL technology integration
3PL (Third Party Logistics)	<ul style="list-style-type: none"> ➤ Contractual ➤ Fixed and Variable 	<ul style="list-style-type: none"> • Enhanced capabilities • Broader service offerings
Basic Service Providers	<ul style="list-style-type: none"> ➤ Contractual ➤ Transactional only 	<ul style="list-style-type: none"> • Focused cost reduction • Niche services

Increasing Trend

Figure 5: Emerging business propositions for Logistics outsourcing industry.

Table 1: Analytical data trends for Logistic outsourcing industry

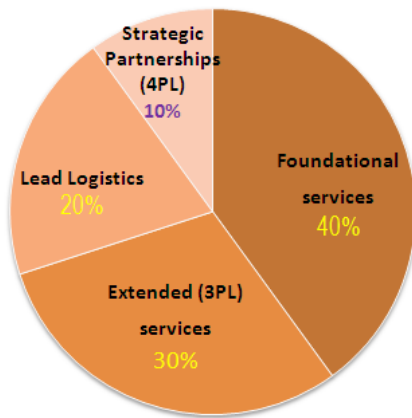


Figure 6: Estimated *Logistic Outsourcing* customer segments (by 2015) [2].

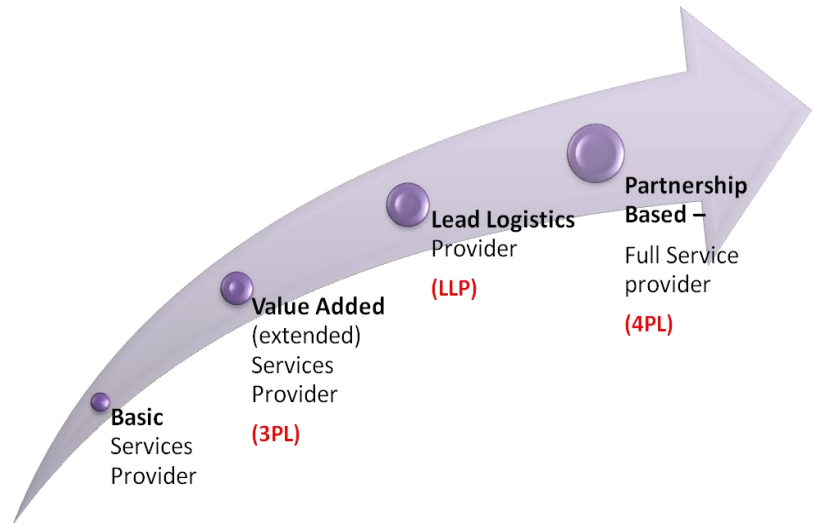


Figure 7: Trends in *Logistics outsourcing* business model

A New model for ‘Partnership’ based Outsourcing

The growing emphasis on efficiency and integration between customers (shippers) and third-party outsourcing firms, has given rise to a unique collaborative model of *Logistics outsourcing*.

Principle

“The focus on end-to-end supply chain effectiveness and optimization will lead to lower unit costs, which in turn will lead to lowest total costs”.

Instead of an inward-looking focus on ownership of hard assets and ‘do-myself’ approach; we need to focus on total supply chain effectiveness and process optimization by utilizing the extended value-proposition of the ‘logistics partner’.

Table 2: Internal boundaries within Logistics outsourcing

Strategic (Planning and control)	Strategy Sourcing	Network and Asset configuration	Carrier Selection	Inventory Ownership	
	Supplier Management relationship		Logistics Oversight	Manufacturing Oversight	
Tactical (Execution focus)	Demand Forecasting	Manufacturer Planning	Logistics Planning	Supplier Planning	
Transactional (basic movement)	Inventory Management	Procurement Logistics	Warehousing	Shipments Planning	Risk sharing
	Product Movement	Product Directory	Customs Clearance	Fleet Management	MES data

Previously, manufacturers and retailers used limited outsourcing of “non-core” processes including only **Transactional** and **Tactical** activities.

But to achieve greater efficiencies, we propose the need for additional supply chain integration and creation of “collaborative” models upto as much as **Strategic** level. Specifically, providers that can add multiple service capabilities up the value chain into planning and control activities by leveraging the use of operational knowledge, logistics information, supply chain integration and user-provider relationships are of critical importance.

Challenges

However, there are many challenges in the use of such Strategic-partnership outsourcing models. Adding capabilities at strategic levels requires an altogether different management priorities and styles. To collaborate and maintain supply chains that are complex, large, and rapidly changing needs a high level of process standardization and conformance.

But, looking at the profitability and competitiveness such a system would bring, it is worth to investigate and research on creating a robust formulation of ‘**shared**’ supply-chain strategy.

References

[1] Laura Goddard (2005), "Outsourcing Logistics – The latest trends in using 3PL providersThe Future Of Outsourcing", Outsourcing Logistics report, January, 2005.

[2] IBM Institute for business Value (2005), "Building value in logistics Outsourcing", IBM Business Consulting Services, 2005.