Strategic Assessment

Evolution of the 3PL Business Model: New Competition

Customers are demanding more responsiveness from companies, and accordingly, companies are investing in alternative solutions to meet these needs while expanding and differentiating their services.

These investments are typically significant, and companies are looking for additional ways to leverage the money they are spending to increase revenue streams. In some cases, companies are offering these services to new customers or competitors and may create a solution that can be spun off or provided as a service to others in a similar or even the same industry. This concept has already been tested and proven in some sectors, including the logistics divisions of large manufacturers.

Twenty-seven years ago, Caterpillar, a heavy-duty equipment manufacturer, created a logistics unit to ship products to customers around the world as a division of Caterpillar Logistics Services. Caterpillar was able to capitalize on relationships with existing clients to expand services provided. The manufacturer partnered with Ford Motor Co. and the software manufacturer SAP to create a state-of-the-art service parts logistics execution software package. The cooperative approach allowed both Ford and Caterpillar to share development costs and risks and leverage similar requirements. The end product also increased 3PL market opportunities for Caterpillar beyond its own operations.

As customers continue to demand more from retailers and ultimately from 3PLs, it is likely there will be increased investments on both ends of the supply chain to fulfill omni-channel and future expectations. As a result of the significant capital required, many of these investments will be either shared across companies or developed into alternative service offerings for a wider customer base to improve the return on investment.

While 3PLs offer the experience and resources to help retailers, a growing number of companies are looking to bring some of their outsourced omni-channel supporting technology services back in-house. For example, some are bringing mobile and Web development in-house to test the best features and structure for their customer base. By doing so, they are able to spend more time developing in-house systems and processes that contribute to their omni-channel competitive advantage and ultimate success. Although these companies may be spending more to develop a custom solution of their own, they are ensured that it will be exactly what their customers are requesting. As a result, they may develop a top-tier solution or skill set that can be used within their own business and even beyond.

In a different scenario, some companies are choosing to create partnerships to share in the investment. This can be an interesting decision because often the partners may compete for some of the same customers. Procter & Gamble's partnership with Amazon, in which the consumer goods company lets Amazon set up shop inside its warehouses, means it is competing with its own direct-to-consumer model. However, the company is able to gain insights into trends, receive a boost in online sales through the Amazon platform and enjoy reduced transportation costs. The partnership also provides preferential treatment because product will always be in stock.

What is the pricing model? What is the value proposition to others, particularly for those that compete in the same retail space?

Alternatively, some companies are looking to avoid additional investments altogether. As noted in the omni-channel section of this study, Wal-Mart is investigating the possibility of using their existing in-store customer base to make deliveries to online shoppers, effectively crowd-sourcing package delivery. The in-store shoppers can inform the retailer about their destination location and volunteer to deliver packages for online customers. In return for the delivery, customers would receive a discount on their shopping bill.

If companies continue to creatively invest in omni-channel/fulfillment solutions and embark on new partnerships, these new solutions have the potential to alter the way existing 3PLs do business. However, the timing is unclear.

The competition within the logistics industry is increasing, and there are many startups on the horizon looking to provide last-mile logistics and courier services to replace UPS, FedEx and other similar services. Amazon, for example, is creating in-house delivery services to meet their customers' increasing demands for next-day and same-day deliveries. The company has built out a fleet of delivery trucks in test markets including San Francisco, New York and London. Between the test tucks and drone news that has flooded the market, tomorrow's last mile is quickly evolving.

What will we see happening in the 3PL market in the near future? Where will companies invest? Will they focus on last-mile logistics and will they replace other players that currently offer these services?

Supply Chain Risk Management

There are an increasing number of organizations where supply chains and the risks they face have evolved from a back-office concern to a prominent position on the boardroom agenda and where recognizing the importance of risk management is significantly enhancing the effective management of supply chains worldwide. In fact, the development of processes, metrics and tools for supply chain risk management has become one of the highest priorities for supply chain executives at many organizations today.

Of note is the growing level of commitment 3PLs are placing on risk management services among those they promote and provide clients. When looking at risk management, logical questions shippers should ask are to what extent they rely on their 3PLs to become involved in the risk management process and how they can create strategies to determine how those involvements will be helpful. Within the London workshop, participants discussed an example of risk sharing whereby 3PLs take ownership of inventory once it is in transit within a certain geographic location. During the San Francisco and Singapore workshops, participants discussed how CRM, mobile and cloud-based technologies may significantly facilitate the ability of 3PLs to support their clients with capable risk management services. An example of this is to enhance the effectiveness of real-time shipment visibility that is so critical to 3PLs and their clients.

Within the risk management process, it is helpful to understand the range of risks an organization, and therefore a supply chain, might face. Next companies can assess the potential impact for each type of risk and its likelihood of occurrence. On one extreme are major natural disasters, such as the 8.9 magnitude Tohoku earthquake off the northeastern coast of Japan. It was responsible for a deadly tsunami that struck the Japanese coastline and also caused the largest supply chain disruption in modern history. A less-extreme event, but one that is still of great concern to supply chain managers, is a spike in demand for seasonal holiday gifts, and the extent to which service failures may arise from a logistics provider's inability to deliver all shipments when they were promised to and expected by customers. This is becoming even more important as companies increasingly focus on providing a perfect customer experience.

An example of a company with a well-developed approach to risk management is the global coffee and beverage provider Starbucks Coffee Co., which operates 20,000 outlets in 63 countries and does business with 9,000 suppliers worldwide. Starbucks has created an enterprise risk management (ERM) program to identify any trends or risk factors that could interrupt its supply chain. The program provides early involvement and exposure to emerging threats before they hinder Starbucks' ability to service its customers.

Potential risk factors for Starbucks include supply interruptions, financial volatility and geopolitical events. As part of its risk management program, Starbucks has also created centers of excellence staffed by experts in areas critical to the company's success, such as coffee, other commodities and advanced analytics. The centers provide consulting and analysis that can benefit regional and local operations. To ensure the ERM program remains relevant, Starbucks' board of directors reviews it annually.

Given the current interest in risk management and the emphasis most 3PLs are placing on developing new products and services to create value for their customers, this seems to be a prime area for collaboration between 3PLs and their customers. In the interest of determining the value derived from risk management processes, it would be useful to better understand the roles that 3PLs may play in partnership with their customers to identify and then mitigate, eliminate or deal with the types of risks that may affect the overall supply chain process.

Where are the areas of opportunity for 3PLs and their customers to work together on the formalization and implementation of processes, metrics and tools related to risk management?

The Intensifying Truck Driver Shortage

The impeding truck driver shortage in the United States has been an ongoing topic of conversation and academic concern for many in the supply chain for many years. During the Great Recession in 2007 to 2009, freight demand dwindled and many trucking carriers shuttered and parked their trucks.

As the economic rebound continues, freight demand is increasing, but concerns over who will deliver it are increasing. Coming out of the Great Recession, the pool of aging truck drivers has become older. Retirements and regulations focused on improving health and safety have further whittled down the driver pool. New regulations surrounding drivers' hours of service have made the existing pool of drivers less productive in an effort to improve safety, and fewer young people continue to select trucking as a career option. New supply chain models and mobile devices are making just-in-time ordering and omni-channel fulfillment all the more possible, but professional drivers remain one of the most critical links in supply the chain.

According to the American Trucking Associations' American Trucking Trends study, in 2013 trucks moved 69.1% of all domestic freight tonnage. Trucks also move the majority of all NAFTA trade, hauling 55.4% of all trade with Canada and 65.4% of all trade with Mexico.

"Today, the industry has in the range of 30,000 to 35,000 unfilled truck driver jobs," said Bob Costello, chief economist for the American Trucking Associations. "As the industry starts to haul more because demand goes up, we'll need to add more drivers—nearly 100,000 annually over the next decade—in order to keep pace."

It is clear the truck driver shortage is intensifying and its impact on the supply chain is potentially significant. Media outlets have touted the use of drones or driverless trucks, and companies are testing the technology. While both may be future options, they are still years away from being a reality on the long stretches of highway that lead to the narrow, winding streets that dot American neighborhoods.

Manufacturers, distributors and other intermediaries operating truck fleets are vexed by the driver shortage. Many are outsourcing their trucking operations to 3PLs as a solution, but this may be just kicking the can down the road. During a recent Council of Supply Chain Management Professionals press conference, Penske Logistics President Marc Althen said, "If I could hire 2,000 truck drivers right now I could put them to work, today."

Trucking and logistics companies are doing everything they can to attract and retain truck drivers. This ranges from utilizing social media recruiting techniques and creative advertising methods to offering higher wages, signing bonuses, concierge-type services, benefits, perks and better routing to get truckers more at-home time. Trucking companies are also investing in equipment to improve the drivers' experience. However, these all contribute to a higher cost of doing business.

Many companies are also turning to the abundance of veterans returning from the battlefields of Iraq and Afghanistan. Some federal programs are making it easier for veterans to get commercial drivers' licenses. Still, it isn't enough to meet demand.

Complicating the issue is the amount of competition the trucking industry faces from other industries, including the building, construction and energy sectors. Those industries pull employees from the same pool of candidates of would-be drivers, but don't require long travel or much time away from home.

It is likely that companies will begin making upstream adjustments, such as shifting distribution patterns, relying on intermodal transportation and shipping larger quantities at one time. However, trucking remains the dominant freight mode within the U.S., and the last leg of the journey requires trained, professional drivers. If freight demand grows as it is projected to, the driver shortage could balloon to nearly 240,000 drivers by 2022, according to ATA data.

Are shippers and 3PLs considering the effect a driver shortage will have on their fulfillment capabilities? Will carriers and 3PLs start to have preferred shippers in times of tight capacity? As companies expand the number of fulfillment options for customers and provide a seamless omni-channel shopping experience, who will provide and pay for the increases required for the final-mile of delivery?

Working Corporate Social Responsibility Into the Supply Chain

For international corporations, corporate social responsibility (CSR), which comprises all facets of how companies should do business in a sustainable manner, is growing in importance. Not only are companies demanding more of themselves and their suppliers, consumers increasingly scrutinize companies' approaches and demand improved social and environmental standards. CSR is now broader than ever, and companies are concerned not just with natural resources, but also human rights, labor practices, environmental impact, business ethics and corporate governance.

This has significant implications for businesses' supply chains. Much of today's manufacturing, particularly in labor-intensive sectors, such as textiles, apparel, footwear and consumer electronics, takes place in low-cost countries where working conditions, compliance standards and human rights enforcement are less advanced. Emerging economies often offer even cheaper labor and an even weaker regulatory and compliance environment. These countries attract foreign investment through favorable conditions for production while sometimes trading off occupational health and safety.

A number of leading businesses, including Nike, Levi Strauss and Walt Disney, have incorporated sustainability into their corporate culture. Others are joining suit and providing guiding principles on how to manage the business while contributing to the social and economic development of the communities where they operate and serve.

The new world of CSR utilizes a proactive approach and includes a stronger emphasis on issue resolution, risk reduction and nimble reaction to problems, accompanied by innovation (e.g., green materials, carbon footprint optimization), capacity building, stakeholder engagement (internal and external), crisis management and media relations.

Strategies often address actions throughout the entire supply chain, including logistics and distribution operations, and there is increasing demand for better checks and balances on sourcing and manufacturing. CSR plays a role along the supply chain, all the way from material sourcing to production and global transportation.

As companies increasingly embrace CSR, they are changing how they address talent management and the individuals who oversee sustainability. Achieving success as a leader in the past required a strong focus on operational issues, but today's executives are expected to also be strong business partners and influencers. In addition to having technical skills, the next generation of leaders will need to have certain leadership attributes to improve the sustainability of the global supply chain.

Effective leaders need to know how to mitigate the emerging risks to the key value drivers of the supply chain, propose remedial measures addressing crucial issues, and respond to requests while maintaining independence and objectivity. They need to have passion and courage, as generally sustainability practitioners must be meticulous and strict about various procedures and principles meaning they may not be the most popular group of people within an organization.

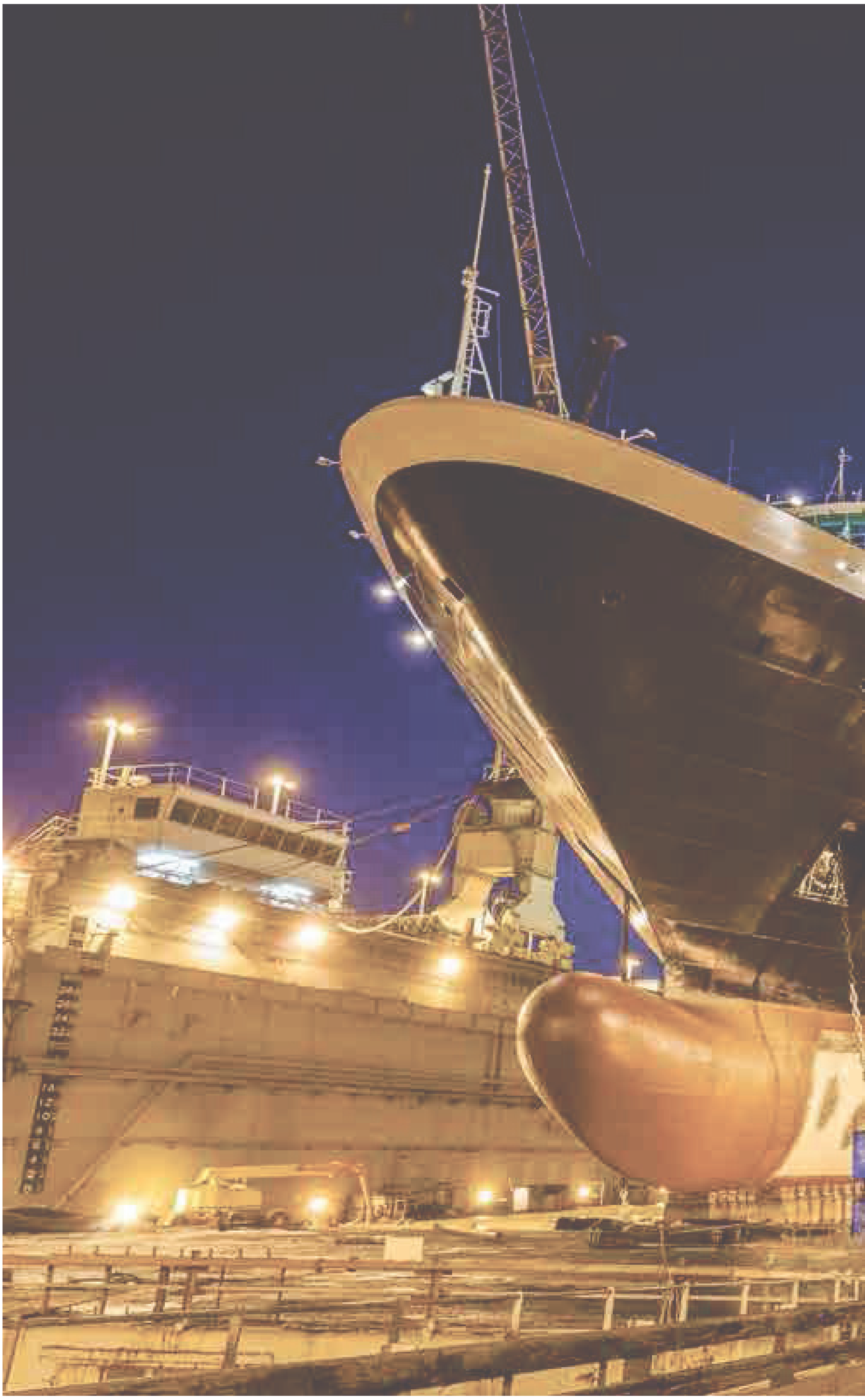
Companies tend to be shifting the reporting chain of command for sustainability executives. Historically, supply chain sustainability has come under the sourcing and/or operations portfolio. However, a recent study by Korn/Ferry International showed that half of organizations now have that function reporting to the C-suite and above level, including CEOs, the board of directors or the steering committee, and 36% of executives had CSR reporting into legal, corporate governance or human resources divisions. This shift shows that while a sustainability approach is a vital factor in the end-to-end supply chain, the two are not necessarily under the same leadership hierarchy.

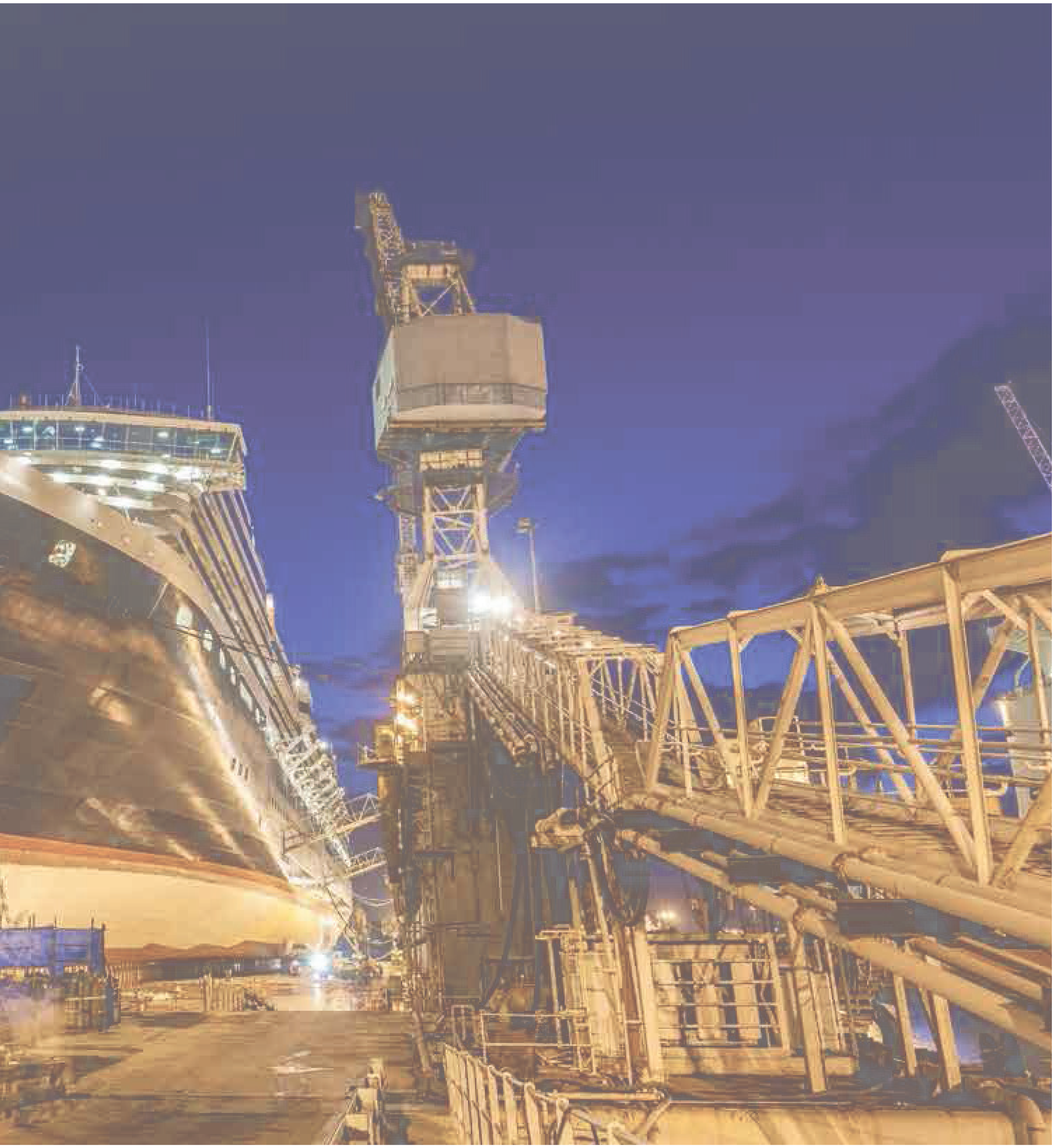
However, sustainability and sourcing functions must remain well connected, as they drive toward a mutually agreed upon destination. As a result, a CSR leader needs strong influencing skills, business savvy and courage to make advancements without jeopardizing the overall company mission.

While embedding social and environmental concepts into the business operation is important, it needs to be done without jeopardizing the commercial intent. That means executives need the ability to understand various business models, including the visible/physical operations along with how companies can make money off sustainable products and services.

Although taking a sustainable supply chain approach can require additional spending to meet social compliance regulations, it can help generate savings through alternative energy, resource recycling, cleanup avoidance and overall business risk reduction, as well as potentially enhance a company's public image.

How will 3PLs respond to the growing importance of CSR? What will shippers demand of their partners within the supply chain? Will CSR improve productivity and efficiency of shippers and 3PLs?





About the Study

Over the span of 19 years, this study has documented significant transformation of the global 3PL industry. In that time, many 3PLs have evolved from tactical service providers to collaborative partners delivering, in many instances, a comprehensive suite of integrated logistics services. Additionally, we have observed an evolution in which providers have become more proficient at the provision of 3PL services, and customers have become better buyers and users of 3PL services. Dr. C. John Langley, Clinical Professor, Supply Chain and Information Systems and Director of Development, Center for Supply Chain Research at Smeal College of Business at The Pennsylvania State University, initiated this study to capture and measure this rapidly evolving industry.

The *Annual 3PL Study* now serves as a vital tool for use by shippers and 3PLs, and as a widely anticipated, heavily referenced index on the state of the 3PL industry. In a year-round process, the study team establishes topics of interest, develops the survey tool, conducts the research, analyzes the results, writes this report, and presents and shares the findings. The study has evolved in both reach and scope.

Just as this study has evolved and changed, so has the participation rate among members and affiliates of the *Annual 3PL Study's* partner organizations. As part of this year's survey process, we attracted 770 respondents, which is lower than in previous years. The study team attributes the change to a variety of factors, from competing priorities to survey fatigue among prospective respondents. As a result, information included in the Current State of the 3PL Market chapter rely primarily on data gathered from respondents in North America (67%) and Europe. Readers are asked to be cautious about comparing the data in this report to data from *Annual 3PL Study* reports produced prior to 2014, since the base of respondents is more geographically limited.

The Annual 3PL Study Process

Steps and elements of the development of the *Annual 3PL Study* include:

Accessibility: Links to the Web-based survey tool are circulated through Annual 3PL Study partner organizations for distribution to their members and affiliates. This year's survey circulated in mid-2014, garnering 433 usable responses, from both shippers (users of 3PL services) and non-users of 3PL services, as well as responses to a separate, related version of the survey by 337 respondents from the 3PL sector. The study report and additional materials are also presented on a dedicated Website, www.3PLstudy.com.

Topics: In addition to measuring core trends in the 3PL industry, the *Annual 3PL Study* conducts in-depth examinations of contemporary supply chain topics that affected both shippers and 3PL service providers. This year's topics include omni-channel, strategic workforce planning, CRM and mobile technologies and business in Mexico.

Contributing Sponsors: The *Annual 3PL Study* is jointly owned by Capgemini and Dr. Langley. Sponsors of the 19th *Annual 3PL Study* are Korn/Ferry International, Penske Logistics, eft (formerly eyefortransport) and IndustryWeek.

Multiple Research Streams: A distinguishing feature of the *Annual 3PL Study* is the multiple streams of research the study team undertakes to validate and illuminate the findings in this report. The team solicits survey topic ideas throughout the year from key industry participants and through desk research conducted by the team and Capgemini's Strategic Research Group, which also helps to vet potential topics of interest. Survey topics and questions attempt to reflect key issues and trends facing both shippers and logistics services providers. Following the survey, the team conducts intensive, one-day facilitated shipper workshops that enable the team to work side by side with shippers to explore survey results in the context of overall industry trends to discover deeper implications.

This year the team conducted three such interactive workshops, held in London, United Kingdom; San Francisco, California; and Singapore. The study team members would like to express their appreciation to the National University of Singapore and the participation of The Logistics Institute – Asia Pacific as a co-sponsor of the workshop held in Singapore. Events in recent years also have been held at selected Capgemini Accelerated Solutions Environment® facilities that are available throughout the world. (See *http://www.capgemini-consulting.com/acceleration-capabilities/accelerated-solution-environments* for more detail about ASEs.)

Wide Coverage: The *Annual 3PL Study* is presented and discussed in prominent supply chain industry venues, including the following:

- Presentations at influential industry conferences, such as the Council of Supply Chain Management Professionals (CSCMP), eft 3PL Summit and Chief Supply Chain Officer Summit, annual THINK! events conducted by The Logistics Institute – Asia Pacific at the National University of Singapore, the Gordon Institute of Business Science (GIBS), the business school of the University of Pretoria in Johannesburg, South Africa, executive education programs available through the Center for Supply Chain Research at The Pennsylvania State University and Penn State Executive Programs and NASSTRAC (National Association of Strategic Shippers Transportation Council).

- Analyst briefings, typically conducted in the weeks following the release of the annual study results in the fall.

- Magazine and journal articles in publications such as *Supply Chain Management Review, Logistics Management, Inbound Logistics, Logistics Quarterly, Supply Chain Quarterly and Supply Chain Digest and IndustryWeek*.

- Webcasts conducted with media, publications and investment analyst firms, including *Supply Chain Management Review, Logistics Management,* Stifel Nicolaus and others.

Supporting Organizations: Each year a number of supply chain organizations facilitate the research process by asking members and other contacts to respond to the survey. In addition to completing the survey, individual companies help out by enabling executives to participate in facilitated workshops and by lending subject matter expertise. Please see the Credits page for a listing of these valued contributors.

Definitions: Survey recipients were asked to think of a "third-party logistics (3PL) provider" as a company that provides one or more logistics services for its clients and customers. A "fourth-party logistics (4PL) provider" is one that may manage multiple logistics providers or orchestrate broader aspects of a customer's supply chain. To ensure confidentiality and objectivity, shippers were not asked to name which specific 3PLs they use.

2015 Third-Party Logistics Study Goals

Research and analysis for the **Current State of the Market** chapter sets out to:

- Understand what shippers outsource and what 3PLs offer.

- Identify trends in shipper expenditures for 3PL services and to recognize key shipper and 3PL perspectives on the use and provision of logistics services.

- Update our knowledge of 3PL-shipper relationships, and to learn how both types of organizations are using these relationships to improve and enhance their businesses and supply chains.

- Quantify the benefits reported by shippers that are attributed to the use of 3PLs.

- Document what types of information technologies and systems are needed for 3PLs to successfully serve customers, and to assess the extent to which this success is being achieved.

- Examine why customers outsource or elect not to outsource to 3PLs.

Goals for the **Special Topic** chapters include:

- **Omni-Channel:** The growing interest in and reliance on an omni-channel network is creating both opportunities and challenges for retailers and shippers. While the importance of the omni-channel network is well understood, omni-channel supply chains are still maturing. The research seeks to understand the opportunities and obstacles associated with the omni-channel network, the growing number of fulfillment options retailers offer and how technology is facilitating growth within the network.

- **Strategic Workforce Planning:** The 3PL industry is on track to face a shortage of talent. The study seeks to understand how strategic workforce management can aid in hiring and retaining top talent among 3PLs. The study also looks at how positions within the industry and the dynamics of supply chain professionals are changing, and the study team sought to understand the return on investment companies obtain from strategic workforce management.

- **CRM and Mobile Technologies:** Given advances in mobile technologies (e.g., smartphones, mobile applications, tablets, iPads, etc.), and in the use of CRM (Customer Relationship Management) by 3PLs, it is an ideal time look at how these can enhance the quality of 3PL-customer relationships. In addition to trying to understand the ways in which customers can benefit from the use of CRM and mobile technologies, the research focuses on how companies can help to make 3PL sales processes more efficient and effective.

- **Business in Mexico:** The strong growth within the manufacturing industry is creating strong growth opportunities for 3PLs on both freight movement and ancillary services. The survey seeks to understand respondents' reasons for shifting operations to Mexico and how logistics services can play a part in rendering Mexico's businesses cost competitive as compared to similar ventures globally.

- Based on what was learned from the study process, the team uses the Strategic Assessment to take an introspective view of the future of the 3PL industry and shipper-3PL relationships.

About the Respondents

Shippers: Figure 37 reveals the percentage of shipper respondents to the survey, including both shippers (users) and non-users of 3PL services and the percentage of 3PLs. The non-user responses are helpful because they provide valuable perspectives on why they do not currently use 3PLs at this time, as well as on a number of other relevant topics. Shipper respondents are typically managers, directors, vice presidents and C-suite executives.

Figure 38 reflects the most prominent industries reported by shippers, accounting for almost 92% of the overall respondents.

Figure 39 includes all shipper respondents' anticipated total sales for 2015.

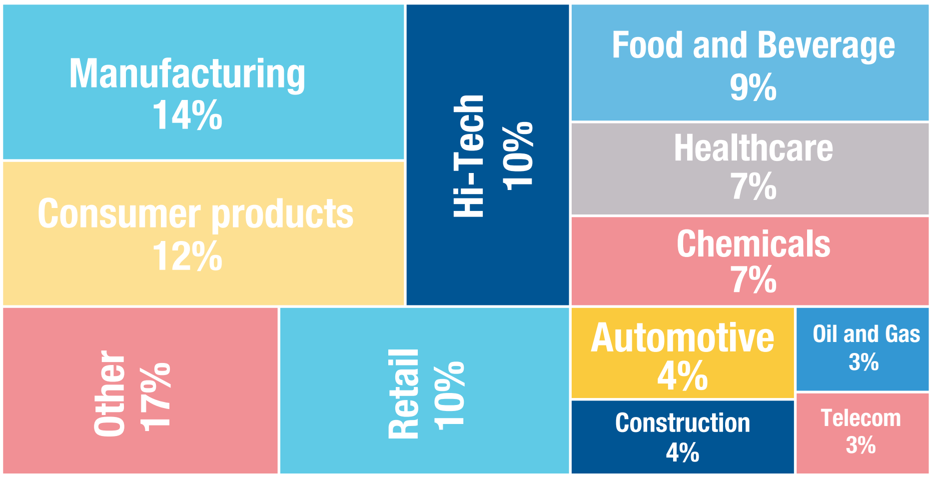
3PLs: 3PL executives and managers responded to a similar, but separate version of the survey. The 3PL respondents represent: 1) several operating geographies; 2) an extensive list of industries served (actually quite similar to the shipper-respondent industries); and 3) a range of titles, from managers to presidents/CEOs. Approximately 34% of the 3PL firms expected 2014 company revenues in excess of U.S. $1 billion (approximately €750 million), while about 66% reported revenues of less than U.S. $500 million (approximately €375 million).

Figure 37: Respondents by category

	Percent
User	40%
Non-User	16%
3PL/4PL	44%
Total Respondents	**100.00%**

Source: 2015 19th Annual Third-Party Logistics Study.

Figure 38: Respondents by industry



Source: 2015 19th Annual Third-Party Logistics Study.

Figure 39: Respondents by sales

Which of the following categories best represents your organization's anticipated total sales for 2014? (select one)	Percent
US$25 billion or more / €20 billion or more	17%
US$1 billion – less than US$25 billion / €750 million – less than €20 billion	37%
US$500 million – less than US$1 billion / €375 million – less than €750 million	14%
Less than US$500 million / €375 million	32%
Total Respondents	**100.00%**

Source: 2015 19th Annual Third-Party Logistics Study.

About the Sponsors

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Penn State University

Penn State is designated as the sole landgrant institution of the Commonwealth of Pennsylvania. The University's main campus is located in University Park, Pennsylvania. Penn State's Smeal College of Business is one of the largest business schools in the United States and is home to the Supply Chain & Information Systems (SC&IS) academic department and the Center for Supply Chain Research (CSCR). With more than 30 faculty members and over 600 students, SC&IS is one of the largest and most respected academic concentrations of supply chain education and research in the world. SC&IS offers supply chain programs for every educational level, including undergraduate, graduate, and doctorate degrees, in addition to a very popular online, 30-credit professional master's degree program in supply chain management. The supply chain educational portfolio also includes open enrollment, custom, and certificate programs developed by Smeal's Penn State Executive Programs and CSCR, which helps to integrate Smeal into the broader business community. Along with executive education, CSCR focuses its efforts in research, benchmarking, and corporate sponsorship. CSCR corporate sponsors direct the Center's research initiatives by identifying relevant supply chain issues that their organizations are experiencing in today's business environment.

This process also helps to encourage Penn State researchers to advance the state of scholarship in the supply chain management field. Penn State's Smeal College of Business has the No. 1 undergraduate and graduate programs in supply chain management, according to the most current report from Gartner.

For more information, please visit
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