

CAPACITY CRUNCH: RELIEF IS POSSIBLE

Managing Your Supply Chain When Capacity Is Tight and Costs Are Going Up

The squeeze is on. Higher fuel prices, a driver shortage, a major wave of government regulations and an improving economy are all playing their part in creating a problematic logistical environment – a nationwide truck capacity crunch and rapidly rising costs.

We have been here before. Analysts hyped the capacity crunch of 2004 as the “perfect storm” – when an improving economy and new Hours of Service (HOS) regulations caused a record shortage of drivers.

Transportation industry consultants FTR Associates and Transport Fundamentals provide the following summary of 2004 capacity conditions and how 2011 compares:

In 2004, a surge in freight caught the industry by surprise and outstripped its ability to increase driver hiring proportionately. Just when that effect was at its worst, the federal government rolled out significantly tighter HOS regulations that reduced industry productivity by 5%. This loss in productivity meant that it took nearly an extra 100,000 drivers to do the same amount of work. When that was added to the almost 200,000 driver shortage due to the slow response to growth, there was a record shortage of 295,000 drivers.

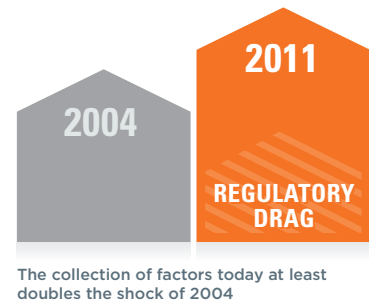
It took about a year for the full effect on prices to come home, but shippers ultimately had to bear a 24% price increase (before fuel) and a 36% price increase after fuel by the end of 2006. Note that, although fuel price hikes peaked in early 2008, fuel prices had already increased 127% during 2004–2006.

CURRENT CONDITIONS AND INDUSTRY FORECASTS FOR CAPACITY.

First, fuel prices are up again. Even with the recent moderation in pump prices, fuel surcharges are up 48% YoY and fuel prices are forecast to increase by 5% more over the next two years, but volatility will be the norm.

Second, despite disappointing economic growth this up-cycle, freight demand is still up 13% over its recession bottom. Fleets, with recession memories fresh in their minds, have been especially reluctant to add capacity. As a result we have a driver shortage of 125,000 drivers, with perhaps more to come if the economy picks up momentum. This would put the industry well below the peak of the last cycle on its own. Add to this more governmental regulatory changes (CSA and others), and another perfect storm is brewing.

While none of the individual changes are expected to match the HOS shock of 2004, the weight of the whole collection will double, or perhaps triple, the 2004 regulatory drag over a period of three or more years. Using 300,000 drivers as a good rule of thumb for the peak effect, we get similar numbers to the 2004 shortage – only reversed in its major causes. This time the regulatory effects dominate.



CAPACITY CRUNCH WILDCARDS

? Economy

* Regulatory changes

\$ Fuel and tax environment

TWO ADDITIONAL INSIGHTS LOOM ON THE HORIZON THAT DESERVE SHIPPER ATTENTION.

First, the effects quantified above assume a continued slow economy. Should we get anything resembling a normal recovery, the pressure will ramp up quickly and could take us above the shortage levels of the last recovery.

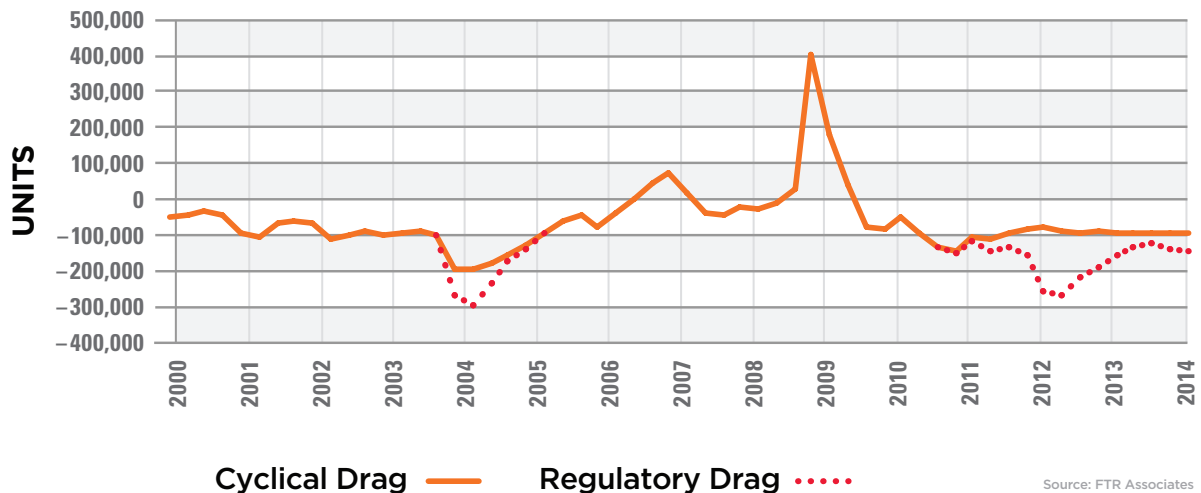
Second, the new and potential regulatory changes are being phased in over a longer time this go-round. Although the timing reduces the impact in any given year, it will keep the pressure on for a much longer time. In the last recovery, the crisis lasted about one year. This time we could get a full three years of tight supply (capacity). Either one of these two exposures could result in spot crises when up to 10% of freight will not move on its intended schedule. This is a condition that causes supply chain failures, with very large cost penalties. According to Transport Fundamentals, under these conditions, the 30% price increases currently forecast over the next three years would get much higher on the most affected lanes.

One more danger lurks, warns FTR Associates: Current forecasts are based on a very orderly fuel and tax environment. Any reasonable observer of oil price markets and U.S. governmental decision making must consider the possibility of major disorders in either of these arenas over the next three years. One imminent possibility is \$5-per-gallon diesel fuel, as the potential to add more tax on fuels exists. Whether the latter is simply to fund infrastructure or a convenient means to solve deficits, the shipper will ultimately bear the cost.

The wise shipper should be looking for ways to reduce supply chain costs now. Keep in mind that a full five years of low margins have exhausted the carriers' ability to absorb increasing costs – this is one of the root reasons capacity is tight. The industry has been very reluctant to risk its scarce capital on growth.

Moreover, the supporting banking community is even more risk averse, especially with the small-fleet segment that historically has supplied the bulk of recovery capacity. All is not lost, however, because the smart fleets working with the smart shippers have a number of ways to create incremental capacity and hold down total logistical costs.

ACTIVE TRUCKLOAD SURPLUS OR SHORTAGE



MARKET CONDITIONS ARE TOUGH, BUT RELIEF IS POSSIBLE.

While managing supply chain variables has become trickier, it's not mission impossible. Proactively managing through this issue in the short term will set shippers up for success in the long term. Making freight more attractive, working with drivers and collaborating with a multimodal provider can provide relief. Each of these will assist with freight movement and can deliver improved management of increasing costs.

Making Freight More Attractive

There are many adjustments shippers can make to their freight – some simple, some more involved. Shifts in each can make a difference in how carriers, intermodal providers and drivers view and ultimately price the freight.

1. Open pick-up times. When shippers can be flexible with pick-up times it provides a greater pool of available drivers, resulting in an earlier dispatch for the driver and an earlier delivery for the shipper.

Appointment times exist in three ways: “at,” “on” and “by.” Many shippers require an “at” appointment with a specific time, on a specific day. Others simply need pick-up “on” a certain day, during the company’s shipping hours. The most flexible option is “by” a certain date. Shippers who expand pick-up time options to those that are “on” or “by” will increase the likelihood their freight will be covered efficiently and cost effectively.

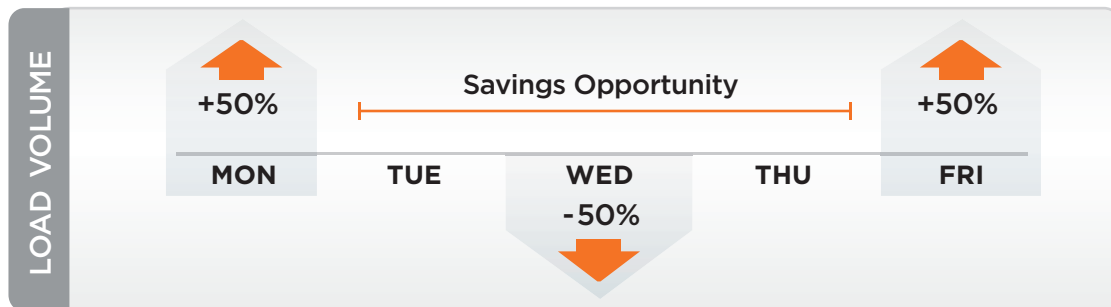
2. Drop and hook freight. As most within the industry know, driver-friendly freight is drop and hook freight. If a shipper has the volume and facilities to support trailer pools, converting to drop and hook freight can result in more efficient pick-up and drop-off scenarios.

3. Preloaded containers. While drop and hook freight is the most appealing for truckload, preloaded containers are the most attractive freight for intermodal. As with drop and hook, preloaded containers keep the drivers moving. Live load and unload require a lengthier stay for the driver and, ultimately, a more difficult time of scheduling for the intermodal provider.

4. Forward visibility. Shippers who communicate earlier secure freight faster. With 24 hours or more advance notice of a pick-up time, most carriers and intermodal providers will be 75% more likely to move a shipper’s freight.

Shippers who are able to accurately forecast their anticipated surges and spikes with their carrier will also win. They may receive priority in capacity allocation over other shippers.

5. Weekend pick-up and delivery. If pick-up and delivery times are available daily – including weekends – shippers will be far more likely to have their load moved more efficiently. Although some drivers are available on weekends, shippers may consider this dead time. Shifting operations to allow for weekend service may prove beneficial.



6. Flattening the week. For intermodal shipping, the majority of activity takes place on Monday (deliveries) and Friday (pick-ups). With a 50% increase in volume movement from Wednesday to Friday, this large swing in activity can be costly for carriers and, ultimately, the shippers. Shippers who can flatten the week – pushing pick-up or delivery to midweek instead of at either end – may realize cost savings.

Working with Drivers

Everyone in the supply chain can play a role in creating job satisfaction for professional drivers. Shippers have several opportunities to positively position themselves in the eyes of drivers, moving them to the top of the list when the call comes for a potential pick-up.

Two primary job satisfaction motivators continue to rise to the top in relation to drivers:

1. Respect for time
2. Sufficient pick-up/delivery facilities

Like every employee, drivers want consignees to respect their time and provide adequate working conditions. There are a few things that shippers can keep in mind:

Driver Detention

Regulations require everyone to be more efficient to save costs. With the HOS definitions of “on duty” and “off duty,” drivers must log their time spent at a shipper’s facility – whether they are actively doing something or not.

Shippers that are able to tighten a driver's wait time for pick-up and/or drop-off will be seen as driver friendly. Keeping a driver moving means returning them to logging miles – where they are able to earn dollars while on the clock.

While drop and hook freight is one way to keep drivers moving, other practices can also move drivers in and out efficiently. The most basic of these is for shippers to give drivers clear instructions on what to do upon arriving at the facility. Another is to be accessible to the driver for follow-up questions. Shippers that are willing to “go along for the ride” by being an ongoing resource for drivers and dispatchers as their freight moves down the highway will be viewed as driver and carrier friendly.

On-Site Facilities

Providing drivers with the basic necessities will also allow shippers to attract and retain the best drivers and carriers. Some suggestions include:

- A place to park their rig while waiting for pick-up or drop-off instructions
- The basic necessities: a restroom, vending machine and a simple lounge with seating, heating and air conditioning (since many drivers are not permitted to sit in an idling truck)

With the right appointments, driver satisfaction will increase – along with shipper's ability to find drivers to cover the load.

DRIVER-FRIENDLY ➤ Drop and Hook Freight
CONSIDERATIONS ➤ Clear Instructions
 ➤ Accessibility at All Points
 ➤ Basic On-Site Facilities

Collaborating with a Multimodal Provider

The definition of insanity is to keep doing things the same way and expect a different result. Shippers should consider alternative solutions to meet their supply chain needs in today's capacity crunch environment. A multimodal provider can transcend the transportation complexities of various businesses, providing today's shippers with the options and creative solutions needed.

Supply chain providers who offer comprehensive services have multiple modes to suit shipper needs and freight demands. The benefits of working with a multimodal carrier are many:

1. Strategic guidance. As opposed to offering shippers a cookie-cutter solution, multimodal providers can create and recommend the modes and services that best fit the shipper's needs. Very few shippers approach a carrier needing a complete overhaul to their supply chain. More often, a business needs assistance with one link in the supply chain that's been a pain point. Some shippers need to move freight in a tough-to-cover location. For others, the spike in freight that periodic surges in their business warrant is challenging. The result: expensive disruptions to a business.

OPTIONS = SOLUTIONS

Truckload | Dedicated | Intermodal | Brokerage

Shipping consultation may be necessary to strategically develop the best solution. Options include comparing and contrasting modal options that can alleviate pain points and ongoing headaches. Working with a broker who manages thousands of carriers can also be a powerful solution and can provide various intermodal, LTL, truckload, specialized and other solutions that can be provided in a contract or as ongoing capacity.

2. Efficiencies. When it comes to time and money, multimodal solutions can be a savings to a shipper. With a full-service provider, typically there are many financial economies that can be found because of the large networks, facilities and negotiating power they have in place.

Various services, and therefore solutions, should be available with a multimodal provider. Those with supply chain experience develop creative, innovative solutions for freight needs, big and small. Services such as dedicated, intermodal and supply chain management were all created by providers looking to find transportation solutions to fit shippers' needs and demands.

Additionally, a multimodal provider is a one-stop shop. This can be the greatest asset in time savings for securing freight shipment. Shippers do not need to make initial contact or manage contact with the multiple players and hand-offs involved with various aspects of the shipment. In one call, a shipper can move and manage their freight from the port to the rail yard ramp to the loading dock.

- 3. Supply chain innovation.** Supply chain engineers are an integral part of a multimodal organization. Charged with developing new, creative supply chain solutions, these experts are constantly on the lookout for opportunities to improve supply chain efficiencies and reduce cost. From innovations that synchronize visibility to international and domestic supply chains to services designed to cost-effectively move LTL freight by having competitors share supply chains, the opportunities to innovate are endless.
- 4. Customer service.** Multimodal providers have experience moving freight across multiple transportation modes, with various levels of freight complexity. With the level of service this logistically demands, communication must be paramount to the carrier's – and shipper's – success. Shippers should find providers with decades of transportation expertise. That tenure should assure solutions-oriented thinking, as well as the latest technology for dispatch and tracking and a level of service that makes the complex, easy.
- 5. Guaranteed capacity.** Shippers who tire of managing through capacity issues and constraints often find relief in a dedicated solution, where capacity is locked in and guaranteed. This can be provided through a multimodal provider on a contract basis or by turning over a private fleet for complete oversight and management by the provider – thereby allowing shippers to focus on their core business while leaving transportation and logistics concerns to someone else.
- 6. Buying power.** Large networks matter when shippers need to optimize every mile on every lane. When a carrier manages a broad portfolio of services, the nuances of a particular shipper can be matched with the best, most appropriate, most cost-effective mode of moving freight. And with greater volume across the board, the time and cost efficiencies are shared with every shipper that does business with the carrier.

The capacity crunch is here – and everyone is feeling it. For many, these are defining moments. Does a shipper continue to do what they've always done to manage capacity, or is it time to shift gears and get more involved and engaged to ensure that what you're bringing to the market is desirable by carriers and drivers alike?

The economy, fuel prices, regulations and driver shortage are each contributing catalysts. However, relief is possible. Shippers who proactively make their freight more attractive, work with drivers and collaborate with a multimodal provider will win.

Shippers who join forces with strong carriers will be in the best position to manage overall costs and find the optimal solutions for their supply chain. It is when everyone is proactively working toward a solution that all can find capacity relief.

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