

Barriers to Innovation and pro-activity in Third party logistics (3PL).

By

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Jonathan Weekes, once said at a 3PL (Third party logistics) debate in 1987 that 3PL operators failed when they turned their backs on innovation and concentrated on what they thought they did well. They compounded this failure by having to ask the client “if there was anything they could do to help”.

10 years later similar comments were being made in research and surveys.

“We are urging our providers to improve their change management skills and to be more innovative. We outsourced because distribution is not a core activity for us. We should not have to drive improvements”.

There is too much of ‘what can we do to help you?’ rather than ‘here is a proposal to help improve costs or service’.

Both the above comments came from a survey by PE Consulting in 1996 in which Jan Szymankiewicz also commented that *“There appears to be a belief that LSPs are not being innovative and proactive enough. They are simply doing what they are told to do by the customer and no more. It is one of the main reasons cited for firms changing their logistics providers”.*

John Styles, Head of Logistics Services at Asda, during a debate in 1997, famously said *“At Asda we continue to use LSPs for distribution but we have a major concern that they can’t go in the same direction we are going in. We have been able to hand over complete responsibility to third parties for our IT function and auditing and pay systems. They look like us, talk like us, they are part of us. Logistics is the next opportunity but less than 10% have a clue about what we really are”.* He went on to say *“..... no proactivity, no openness or honesty, no corporate synergies, they are just good at running warehouses and fleets”.*

So, nearly twenty years on, has anything changed?

The CILT recently undertook a study of its members within the supply chain and transport faculties to ascertain whether users of 3PL services still felt that their suppliers were not innovative or proactive enough.

The questions were based on an MBA thesis which was written in 1997 by the author and provide an interesting comparison between the thoughts of today’s logisticians and those from eight years ago.

Q1) “How proactive has your company’s relationship with your 3PL (s) been to improve the operation and avoid problems?”.

These figures were compared with a survey undertaken by PE International in 1996.

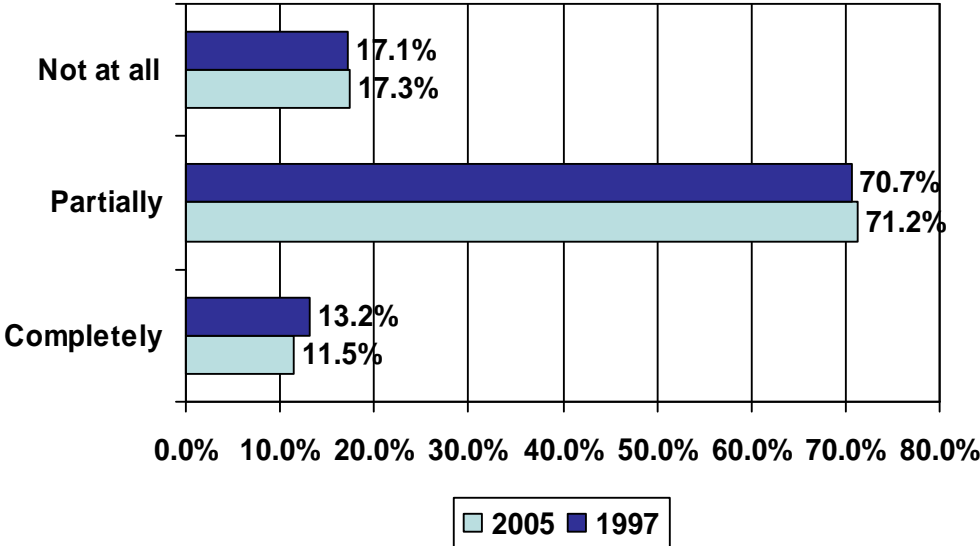
The results are as follows:

	Entirely reactive	Mainly reactive	Mainly proactive	Very proactive
1996	2%	16%	54%	28%
2005	4.3%	38.3%	44.7%	12.8%

These figures tend to suggest that 3PLs are less proactive than they were 10 years ago, although the survey sample was much smaller.

When asked the question whether the users agreed with the statement that “the majority of logistics service providers are neither proactive nor innovative” the replies were as follows:

Q2) There has been some criticism that the majority of logistics service providers are neither proactive nor innovative. To what extent do you agree with this view?



As can be seen above very little has changed since 1997 when the same question was asked to delegates at Logistics 1997 on the Oriana.

So why do people think it is so difficult for 3PLs to be innovative and proactive in their relationships with their clients? The survey went on to ask the respondents to state which factors they believed were the greatest barriers to 3PL innovation. The same question had also been posed back in 1997.

Reasons	Importance Ranking 2005	Importance Ranking 1997
Concentration of time on operational issues	1	2
Client resistance to change	2	8
Low margins/profitability	3	3
Quality of management	4	1
Lack of trust	5	6
Lack of information	6	11
Lack of incentive to innovate	7	5
Poor communication	8	9
Length of contract	9	4
3PLs are risk averse	10	7
Staff turnover	11	10
Not in 3PL interest to declare opportunities	12	12
Client staff innovate therefore no requirement for 3PL to innovate	13	13
Other reasons	14	14

The initial research finding in 1997 was that the quality of people, both at managerial and operational level was the main factor which inhibited innovation in 3PL relationships.

However as the research progressed it was found that, although a major factor, it was not the sole cause of the problem. Innovation cannot take place in isolation. Employing the most creative and expert staff cannot guarantee success. The customer has to want the new service/innovation and needs to be involved in the creative process at an early stage.

The subsequent research identified the adversarial relationship between the LSP and the user as being the most significant factor resulting in a lack of innovation. This was manifested by low margins, a lack of trust and a reluctance to share information and to work closely with their 3PLs.

Each of these reasons are now examined in greater detail.

1. Operational issues.

There are two sides to this story. On the one hand the pressure is on the 3PL to ensure that they get the basics right. How many Contract Managers are drawn into operational issues on a daily basis thus reducing the amount of time available to introduce improvements to the operation itself? – an all too familiar scenario.

“regardless of what people may say there is a shortage of very bright General Managers, people who can clearly manage the day to day, which is where the action is, but also have the intellect to be able to think ahead, to plan and be innovative. Finding somebody to do both is very difficult”.

Kanter in 1984 said, *“...when managers are so occupied with the daily routines, there is little energy left for creative endeavour”.*

Whilst on the other hand certain clients will only request the basic service from their suppliers, allowing them to introduce their own innovations. An interesting point to note is that past research has tended to show that users are more likely to introduce innovations as opposed to manufacturers and suppliers.

A respondent from the CILT survey said that *“The client in many cases just wants the job doing, regardless of innovations from the logistics provider”.*

A respondent to the 1997 research said *“Sadly the retailers have now become so strong and so powerful they are the ones with the new ideas and all of the control. Most of the 3PLs are just people providers, efficient people providers and that is all that is being asked of them. The retailers have sucked us dry of ideas and they now employ some very high powered and capable people and very sophisticated software”.*

A recent Eye for Transport survey – ‘Outsourcing Logistics 2005: Best practice for managing 3PL relationships’ showed that users of 3PL companies continue to predominantly view 3PLs as tools for reducing costs and improving their basic logistics services as opposed to ‘improving supply chain management’.

The Capgemini/GIT (2005) survey seems to bear this out as it shows that the “proficiency of a provider’s core services was considered more important than the provider’s ability to deliver value-added services during the selection of a provider”.

2. Client resistance to change

A respondent to the current CILT survey sums up this particular reason as follows: *“My experience in leading an MOD logistics change programme was that the MOD elements outside of the project team were very resistant to change during their implementation”.*

phase....As the MOD programme leader I was extremely frustrated by my organisation's lack of desire to change, even when offered to us on a plate by the successful 3PL".

Traditional operating methods and company cultures are resisting change in all but a handful of companies. Retailers, manufacturers and suppliers have traditionally set up operations structured along functional lines which can block cooperation and information exchange which are seen as crucial to supply chain integration. Companies have to move away from these vertical silos.

3. Low margins/profitability

A recent survey by Provia Software states that "over 60% of the survey respondents believe that decreased profit margins and the reduced lead time to set up new customers are limiting their continued success".

Research estimates an average EBITA margin at 3.4% for 3PLs with cost pressures from fuel increases, the working time directive and increasing calls from customers to lower charges are increasing that cost pressure even further.

For many 3PL providers return on capital invested is around 7% - 8% leaving very little capital to invest in value added services and innovation.

If, according to Jorde and Teece (1992), "*Innovation.... involves uncertainty, risk taking, probing and re-probing, experimenting and testing*" we have another problem in that 3PLs are seen as risk averse and coupled with the low margins are therefore unlikely to invest a large amount of time and money in innovation.

4. Quality of management

This reason has moved from first position to fourth in the survey results which tend to confirm the belief that overall, managers within logistics are improving their skill sets, although there are still skill shortages in a number of areas which the CILT is aiming to overcome with recent initiatives.

However with regard to 3PLs we also get the following comments that the industry is "*very incestuous, not attractive generally. Broadly speaking the industry does not attract the young graduates....the brightest logisticians*"....there is a "*continuing merry go round of staff... you see very little new blood coming through*".

As the supply chain function becomes even more of a focus within a company, management skills will continue to improve and users of 3PL services will look for a step change improvement within their suppliers' management teams also.

5. Lack of trust

Trust is a key ingredient to partnership. From trust, relationships grow, trust progresses to respect and respect fosters the willingness to listen. As people are willing to listen there is an increase in understanding, concern and participation resulting in open communication.

John Parsons, who took part in the initial research in 1997 when he was with Sony still believes that trust is a major factor in curbing innovation and proactivity in 3PL relationships. John is now a senior consultant with The Consultancy Company.

Inherent lack of trust can also cause the break-up of a partnership if a problem is encountered: rather than continuing to work together, each company closes ranks and apportions blame. To overcome this, the companies must continue to talk to each other and work in joint teams to resolve issues.

Bhote (1989) describes four stages of supply management as follows:

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|---------|---|
| Stage 1 | Confrontation with the supplier |
| Stage 2 | Arms-length relationship where adversarial attitudes gradually give way to a cautious, tentative assessment of a working relationship |

Stage 3	A congruence of mutual goals, a coming together
Stage 4	A full blown partnership between customer and supplier, a “marriage made in heaven”.

It is our contention that LSPs and their customers are currently at Stage 2. Mutual suspicions remain, multiple suppliers are still present, contracts are still being tendered regularly and limited information is shared.

“The LSP can only be proactive if he has a really detailed understanding of all of the customer’s supply chain. In terms of sharing information, this is always a sensitive area and it comes back to trust and confidence”.

The traditional relationship between a company and its logistics suppliers can be summed up as follows:

- A mind set that incorporates an arm’s length approach
- Bidding and negotiating are followed as a primary strategy (N.B. note the rise in on-line auctions)
- The company has a multiple supplier base to limit risk
- The flow of information between company and supplier is very limited
- Communication flows vertically within the two companies
- Contact is usually only between sales staff and buyers
- Focus of communication is on problems, not their cause or correction

If innovation is to take place, this type of adversarial relationship has to change.

Erskine Management Consultancy (1996) in their guide to logistics outsourcing suggest the following key points to users of logistics services and they are still valid today. (See also Appendix I)

- Allow the supplier easy access to your organisation
- Share information with the supplier, particularly volume forecasts and possible service quality developments
- Involve him/her in your business as the logistics expert, for example in strategic planning decisions
- Create a “can do” atmosphere and reward proactive initiatives

We can also add the following:

- Consider longer term/single supplier relationships
- Build teams to create a joint vision

In association with Cranfield University, LCP Consulting recently conducted research to determine the extent and characteristics of value creation in the supply chain through innovation. The headline conclusions were that there was plenty of innovation in the sector yet neither clients nor providers were exploiting the full value of their work and investment.

The research found widespread ‘co-dependency’ but little partnership.

Conclusion

So, why is it so critical that the logistics process continues to be driven by innovation and vision? Could it be that, in Professor Martin Christopher’s words it is no longer products and companies who are competing but whole supply chains and that the new relationship between customers and their suppliers in all links of the supply chain is driving the need for innovation. The goal of integrated supply chains is now the holy grail.

The 3PL market needs to move towards a two tier system. One tier represented by the commodity providers who need to demonstrate slick operational expertise and lowest

possible cost whilst the second tier offers a strategic supply chain orchestration which handles all aspects of the supply chain from procurement through to inventory control, final delivery and invoicing.

The key challenge for the 3PLs is to decide which of those two tiers they are going to concentrate on and then to build an organisation to support their decision. These tiers could mirror those within the automotive sector with the main tier taking full responsibility for the coordination of their customer's supply chain, introducing innovation etc, as well as managing a second tier of companies.

In order to establish an environment where innovation can occur the following aspects have to be present in a third-party logistics relationship.

- Presence of creative staff and a Director overseeing the innovation process
- An organisational structure which is conducive to communication at all levels
- An intimate knowledge of the customer's requirements and the industry in which they operate
- Trust
- The sharing of information

We give the final words to our respondents and the business guru Tom Peters.

I firmly believe that innovation should be included in any contract with a 3PL and that the negotiations that take place in getting the contract right also develop a sense of expectation on both parties to deliver”.

CILT member, Yvon Leger from Lithogistics Inc added these comments to her answers.

“As a 3PI, it is imperative that we work on the same level as our customers. We constantly challenge our customers, by questioning, giving honest input and asking for judgement from them. You need to understand your customer from A to Z and be transparent within your activities. We are always in constant communication about their future developments, markets targeted and forecasts. As a service provider we believe it is our duty to help, in any way possible, our customers to achieve their financial goal. I believe that there are a lot of very good and honest service providers in the world but there are also too many that only look at their bottom line first... to which in the end the customer pays the ultimate price”.

“Creativity is both feasible and worthwhile in business; get innovative or get dead”. Peters 1991.

Appendix I Features to Support a Proactive Service

Source: Erskine Management Consultancy 1996

Performance Measures and contractual agreements	<ul style="list-style-type: none"> • Performance measures that focus on those logistics processes critical to the customers' wider business objectives • Performance measures that report on the improvement in performance • Incentivised management fee structures • Performance related staff pay • Open book accounting
Performance improvement programmes	<ul style="list-style-type: none"> • Skills and resources available to better identify and exploit supply chain opportunities • Initiatives to periodically re-engineer processes and radically re-appraise the current logistics solution • Channels and forums for identifying and developing improvement ideas • Bench-marking of critical activities • Periodic strategic and operational logistics audits • Target driven, continuous improvement programmes
Account management	<ul style="list-style-type: none"> • Processes to better understand customer needs • Periodic formal reviews with customers • Non -operational reviews of the customers' wider strategic objectives and the role of logistics in helping to achieve these • Customer satisfaction surveys and customer • Methods to better develop relationships throughout partner organisations
Operations Management	<ul style="list-style-type: none"> • The sharing and use of forecast volumes and business activity • Innovative use of technology within the logistics supplier and back into the customer • The development of added value services throughout the logistics function • Wider inventory management skills

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