

The ABCs of Lower Costs

Some shippers think that simply negotiating the lowest prices with their carriers means they are shipping at the lowest possible cost. But more experienced distribution professionals know better. The reality is that shipping costs include additional expenses beyond price, and you may be paying more for transportation services than you realize.

These hidden shipping costs are a growing factor in how much you pay. An infusion of several billion dollars in new systems by leading small-package carriers exploits shippers who operate under traditional assumptions, making it important for shippers to approach shipping costs a little differently. The good news is that advances in technology are quietly altering the economics of transportation, and shippers can adapt and reduce shipping costs with little effort.

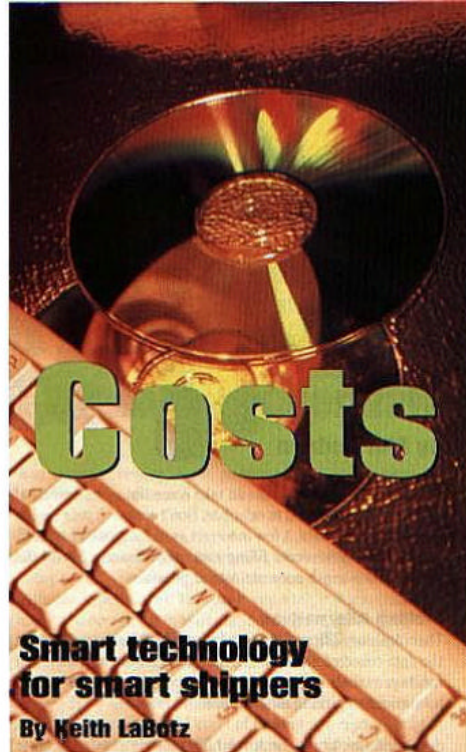
Total Cost

Everyone uses the principles of total cost instinctively. Consider the example of purchasing an automobile. If you've ever purchased an automobile, you know the importance of looking beyond the dealer sticker price when calculating the cost of a car. Additional costs such as gas mileage, depreciation, service costs, insurance and warranty must be included to determine the "total cost of ownership." These extra costs are not visible in the dealer's price, but they are real, and an educated buyer accounts for all of them. A knowledgeable buyer can evaluate competitive alternatives and negotiate the best deal. This same approach works just as well for shippers when purchasing transportation services.

Shippers who look at the costs beyond freight price pay less than other shippers. Just as hidden costs vary between different vehicles and car dealerships, hidden shipping costs also vary between shipments and different carriers. The problem facing most shippers is accounting for these expenses. Fortunately, new software makes this easy for shippers by automatically employing the ABCs of shipping costs.

Carriers' ABCs

There's no better way to learn the ABCs than from the experts: leading small-package carriers. With millions of packages in the balance each day, squeezing the last few cents out of every package can impact profit margins by millions of dollars annually.



Smart technology for smart shippers

By Keith LaBotz

Carriers such as FedEx and UPS spend a fortune each year capturing shipping data. Utilizing Activity Based Costing (ABC), carriers calculate their true costs of delivering each package by totaling all costs associated with a shipment from initial dispatch through Accounts Receivable. This final cost is the Total Delivered Cost (TDC), analogous to the total cost of auto ownership in our previous example. Adding margin to TDC ensures carriers of a profitable price.

Smart ABC systems allow carriers to compensate for unpredictable costs in a number of ways. Surcharges can be automatically assessed for shipper-imposed exceptions such as incorrect addresses or pickup delays. Package handling can be prioritized based upon shipment profit margin or account profitability. Finally, data feedback is incorporated back into pricing systems to ensure profitable pricing on each shipment. As carriers use sophisticated systems that inextricably link pricing and logistics performance, shippers must respond in kind.

Putting the ABCs to Work

Smart systems work as well to minimize shippers' costs per shipment as they do for the carriers. These systems operate alongside a shipper's existing business systems. Most ABC systems do not require process changes or IT resources to be utilized, allowing some vendors to provide no-cost analysis of their ABC solutions. Other ABC systems offer optional tools to reduce costs associated with exception management and freight payment.

Here's an illustration of how ABC saves shippers money. Let's say that you have a package you want to ship "least cost" method.

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Carrier X is a little more sophisticated and provides you with more "value-added" technology than Carrier Y. Carrier X quotes you \$20, and Carrier Y quotes \$10 for the same service commitment. Which carrier is less expensive?

Determine the true cost of the shipment (the TDC) by accounting for all costs associated with the shipment. Calculating the TDC for Carrier Y looks like this:

- \$10 freight price
- \$ 2 extra labor for data entry into Carrier Y's manifest system that is not integrated with order entry
- \$10 labor spent responding to customer complaint, gathering shipment details because Carrier Y does not provide automated Late Delivery Alerts as Carrier X does
- \$10 address correction resulting from outdated address records in Carrier Y stand-alone manifest system
- \$ 2 rural delivery surcharge assessed that Carrier X does not assess
- \$ 1 cost of shifting volume to Carrier Y reduces discount level with Carrier X
- \$35 true cost of shipping with Carrier Y

ABC reveals that shipping with Carrier Y is 75% more expensive than Carrier X. These hidden costs are every bit as real as freight expense, and they impact your company's bottom line the same way. The only difference is that your manifesting and accounting systems do not itemize these expenses. Consequently, these expenses become obscured overhead and continue out of control. You can't fight what you can't see.

Choosing an ABC System

All ABC systems share a three-step cost reduction process: accounting, which calculates accurate shipping cost (TDC); benchmarking, which identifies excess costs and savings; and control, which directs action for repeatable results.

Accounting

TDC clarifies transportation analysis by comparing different carriers' varying pricing, performance standards and billing practices. A universal TDC measure for all carriers will expose higher costs that may be concealed by low-ball prices or complicated proposals. Better systems can compile a variety of cost factors to determine your TDC:

- Labor** — shipment preparation, tracking, accounting, payment, claims
- Freight Expense** — transportation, surcharges, service fees, insurance
- Accuracy** — data errors, billing errors, service failures, routing mistakes
- Property Loss** — damages, theft
- Packaging** — cost of packaging materials

Benchmarking

Benchmarking TDC and external benchmarking discloses savings opportunities that are overlooked by traditional freight cost

analysis. Some ABC systems enable proactive cost prevention by monitoring incoming and outgoing shipments in real-time, comparing actual performance against expected results. The proactive approach also prevents delivery exceptions. Regardless of a particular system's capabilities, all ABC systems use benchmarking results that direct the shipper to take cost-saving action.

Control

The best ABC systems show the way to repeatable gains through process improvements and identification of new savings opportunities. Features might include automatically alerting parties upon delivery exceptions, electronically contesting overcharges on carrier invoices or identifying better pricing arrangements. The shipper can use this data for a recommended process improvement such as filing claims for missed delivery or renegotiating pricing, terms or technology arrangements.

Feedback for Negotiations

Carrier contract terms, pricing and billing practices are growing more complex with every negotiation. Shippers who use TDC have a wider range of options with greater savings potential, just like the educated auto buyer. An ABC system compares carrier proposals so they can be translated into clear financial terms. The shipper can negotiate technology, human resources, terms and equipment based upon their true values. Benchmarking TDC externally with other shippers and carriers allows a shipper to readily validate the competitiveness of any proposal. Additionally, ABC systems identify opportunities for reducing a carrier's TDC, allowing the carrier to offer a lower price without eroding its margins in the process.

A Win-Win Approach

The ABCs of lower shipping introduce a win-win situation into the shipper/carrier relationship. Many of the costs constituting a carrier's TDC are also present in the shipper's TDC. Shared costs can be shipment data entry, data inaccuracy, dock time, exception management, tracking, accounts receivables, etc. Reducing a shared cost reduces the TDC of both parties. Keep this in mind the next time your carrier representative touts the value of spotting a trailer or offers the shipping, tracking and billing systems at no charge. Sure, these "extras" lower your operating costs, but they also increase your carrier's profitability. That's how the ABCs of lower shipping cost work. You're both winning.

ABC systems offer an exciting new approach for reducing shipping cost, improving performance of shipping and receiving operations as well as enhancing shipper/carrier relationships. The ongoing efficiency gains and business intelligence will do far more for your business than a one-time negotiation for lower prices. An ABC system is not just smart; it's a technology that smart shippers cannot afford to operate without.

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