The Purchasing/Logistics Disconnect

How Silo Structures Are Costing Retailers Millions in Supply Chain Costs

A KANE Viewpoint

Retailers today face an opportunity to save millions of dollars a year, simply by fixing a structural flaw built into most retail supply chains. That same fix can make a huge dent in carbon emissions.

The problem? Large retailers have thousands of suppliers, each managing its own transportation to the same distribution centers (DCs). That's an inefficient practice, marked by redundancy, excess expense and inefficient freight transportation. The opportunity is for retailers to change ordering processes so they receive consolidated inbound shipments on a set schedule in fewer, fuller loads.

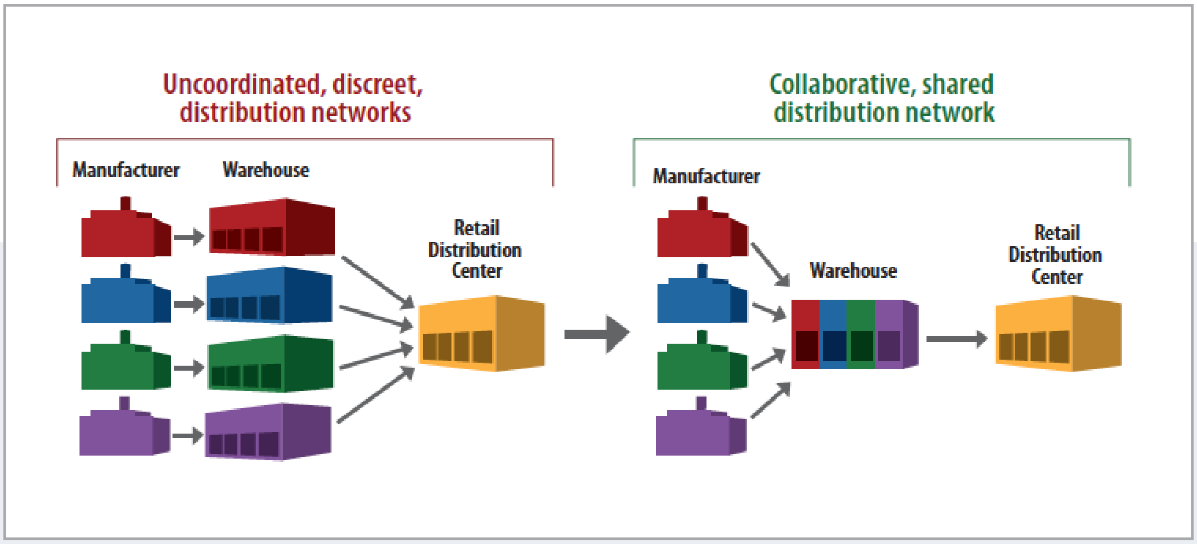
When you leave suppliers in charge of their own transportation, many must use costlier less-than-truckload (LTL) shipments. Trucks coming from suppliers in the same region cruise the highways side by side, often one-third empty, and reach your DCs in ill-timed clusters. You get traffic jams at your loading docks; you pay extra for labor to handle unpredictable inbound volumes; and your suppliers build the cost of those inefficient shipments into the prices they charge your company.

You might not pay directly for your inbound freight, but you still need to take control of that flow. To save money on the inbound side, you must get your suppliers to collaborate – replacing an unruly influx of LTL shipments with regularly-scheduled, multi-vendor truckload shipments. The chart below illustrates the simple shift to a more collaborative distribution environment.

An Aberdeen report, *B2B Collaboration: No Longer Optional*, compared the performance advantage of leaders versus followers in B2B collaboration. Data from the supply chain officers of "leader" companies indicated significant advantages, including:

- Cash conversion cycle of 19.4 days, versus 40.7 days for followers
- Increase in total landed costs of 1.9%, versus 8.8% for followers

For large retailers, the real dollars associated with these gains are staggering. But before you can achieve logistics-related savings, though, you'll first need to do some work inside your own organization. You have to break down the walls currently separating two crucial functions in your organization: purchasing and logistics.



Incentives Gap

A retail buyer's job is to purchase goods at the best possible price and get them delivered on time. Buyers win bonuses for hitting those metrics. But they don't care how many trucks show up at the DC, or what's loaded on each truck, or when those trucks hit the dock.

As for the logistics department, its main job is to move product through the DCs and out to stores. Logistics managers who exceed their targets for pallets picked per hour, on-time deliveries or similar measures get rewarded. No one worries about inefficiencies on the inbound side since this is perceived as something they can't control.

It's as if the retailer's purchasing and logistics departments were seated back to back, each managing its separate silo. No one glances over a shoulder or asks how one team's work affects the other team's performance. There's no incentive for making a cross-functional effort to optimize the supply chain.

Why is that a problem? Look at how money disappears in the space between those turned backs:

- **Excess traffic and costs at the receiving dock:** LTL carriers arrive at all hours to deliver big and small loads from hundreds of vendors. The more trucks that bump the dock, the more workers you need to unload and put away. Since you never know exactly when those LTL trucks will turn up, scheduling the right number of associates for the right hours is just about impossible.
- **Excess carrying costs:** Because an LTL shipment moving from your supplier to your DC passes through multiple sorting points, you can't be sure it will arrive on time. To avoid stockouts, you have to tie up cash in extra inventory.
- **Hidden costs:** Your price for every product your company buys includes the cost of transportation and fuel surcharges. No matter how great a deal your buyers negotiate, if you don't control your inbound, you're probably paying a premium.

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- **Better access to capacity:** Consolidating inbound freight into truckloads reduces the number of trucks required to carry the same volume of freight. There's less need to scramble for capacity, and less need to pay a premium for scarce space.
- **Large carbon footprint:** When each vendor manages transportation on its own, it takes many more trucks to deliver the goods than if you consolidated those shipments. That makes you responsible for releasing extra CO_2 – something that customers and investors deplore.

Retail companies work hard to improve existing processes. Outbound network redesigns, transportation management systems, lean initiatives – they all yield incremental savings. They make companies more efficient.

But "more efficient" just means doing the same things as always, only a little faster and cheaper. It doesn't add up to "more effective." To enhance your bottom line in significant ways, you need to tear down the old model and build a better one. That takes courage, imagination, and pressure from the top to make it happen.

Let's All Get Together

The most effective transportation network would send freight from multiple vendors to a retail DC in full truckloads, already sorted for delivery to stores. To make that happen, the purchasing and logistics departments must turn around in their chairs and work together on a mutual goal – streamlining the inbound supply chain.

Today, retail buyers work independently. Ketchup arrives on Tuesday, paper towels on Wednesday and mustard on Thursday, even though the shipments may originate from the same geographic area. The solution is to adapt the current model so that the same volume of goods is delivered on a set schedule in fewer, fuller shipments.

That solution can take a few forms:

- **Shared vendor DC:** Two or more suppliers occupy the same building and combine shipments to

Drivers of Collaboration

Retailer Benefits

- Lower inventory
- Reduce dock congestion
- Reduce labor to receive and process inbounds
- Improve in-stocks
- Lower carbon footprint

Supplier Benefits

- Reduce transportation costs
- Reduce fuel costs and CO_2 emissions by shipping the same volume of freight in fewer trucks
- Stop ordering extra inventory for transportation efficiency

Market Trends

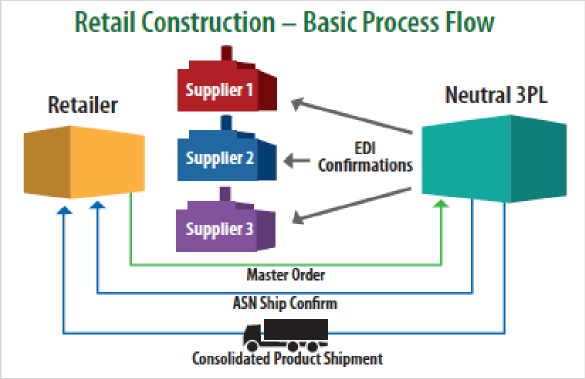
- Rising fuel prices
- Pressure to reduce carbon emissions
- Tightening capacity
- Volatility in LTL carrier space

mutual customers. In 2011, Hershey Co. and Ferraro Group announced a project to conduct this kind of collaboration. This strategy offers clear benefits, but it's not retailer-driven, and few suppliers, let alone competitors, get to this level of partnership.

- **Multi-stop truckloads**: A single truck picks up product from multiple suppliers and then delivers a full truckload to a retailer's DC. CVS has tested this strategy in several pilots, choosing it as a way to improve truck utilization by combining freight from suppliers in the same geographic areas. One of the pilots paired Colgate-Palmolive and Kimberly-Clark, focusing on facilities in Texas and Florida. According to a presentation by the three companies at the annual meeting of the National Association of Chain Drug Stores (NACDS), this collaborative effort reduced inventory for CVS by 7%, improved in-stocks by 2% and saved 28.3 carbon tons.
- **Consolidation centers:** Suppliers deliver product to a DC or crossdock run by a third-party logistics provider (3PL), which builds full, multi-vendor truckloads for delivery to the retailer's DCs. Walmart, Target and the French retailer Carrefour all have implemented this strategy. A 3PL-run collaborative distribution center does not necessarily require retailers to be the catalysts. To capitalize on freight consolidation opportunities, CPG companies are proactively electing to store goods with 3PLs that also house products from like firms moving to the same retailers.

The sidebar to the right explains the process flow if retail buyers proactively consolidated orders for products stored at the same 3PL distribution center.

Although some of the largest players have embraced supplier collaboration with great success, those initiatives are still the exception. Most retailers have not yet started pushing their suppliers to collaborate. They certainly have the power to do so, if they want. Suppliers



In a consolidated order environment, the process for retail buyers would be largely the same. The retailer's ordering system would need to be adapted so that individual orders for certain products are combined and sent, as a Master Order, to the 3PL consolidator. The 3PL would split the orders, pick and ship products to the retailer, and send electronic confirmations to the retailer and suppliers to trigger invoicing. By consolidating orders, retailers would:

- Reduce time spent managing multiple suppliers
- Save money by paying a truckload, versus LTL, rate for the inbound shipment
- Create a far more efficient receiving process at the dock
- Reduce their carbon footprint

The process presumes inventory from multiple suppliers is co-located at a neutral 3PL. More consumer product companies are seeking these shared warehouse arrangements to reduce freight costs. But retailers can hasten this trend by encouraging suppliers, particularly their smaller suppliers that ship LTL, to move to a consolidation model.

go to great lengths to pack and label their products to meet detailed retailer requirements. Retailers who make similar demands for vendor collaboration stand to gain tremendous new efficiencies.

Why Collaboration is Better

When the purchasing and logistics departments work together to facilitate a streamlined inbound supply chain, retailers lose the disadvantages of piecemeal LTL delivery and gain the benefits of direct TL shipments:

- **Effective inbound operations:** Each DC receives full trailers on a regular schedule. It takes less labor to receive those consolidated shipments, and it's easy to predict how many workers you'll need for each shift. The DC gets more work done for less money.
- **Tighter inventory:** Full truckloads travel directly from Point A to Point B, increasing the chance that product will arrive on schedule and in good condition. That reduces the need for safety stock.
- **Lower prices:** Instead of paying high LTL rates, vendors share the lower cost of moving goods via full truckload, including any fuel surcharges. When transportation costs less, your buyers can negotiate better deals for the products they buy.
- **Smaller carbon footprint:** When you put fewer trucks on the road, you use less diesel. That reduces your freight costs and your impact on the environment.
- **New merchandise**: Large retailers often won't give shelf space to a small supplier whose weekly shipment amounts to just one small UPS or FedEx delivery per store; it's too much bother. But when a small vendor can hitch a ride with others on an OTR trailer, the retailer gains a chance to try a niche product that could have great customer appeal.

A Strong Track Record

If supplier collaboration is such a successful strategy, why don't more retailers use it? Some of the problem boils down to inertia. "We've always done it this way" can be a powerful argument, even if it doesn't make good financial sense.

Before you can change the way the purchasing and logistics departments do business, you need to create an incentive structure that rewards an effective inbound process.

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distribution when it only involves your products, your people, your systems, and your carrier partners.

But consider the money that will continue to leak out if you don't innovate. Walmart, Target and other industry leaders have recognized the profit potential of a leaner inbound supply chain. Any retailer can take similar steps to influence how products get to their distribution centers.

How to Get Started

Retailers that want to implement retail consolidation programs should first understand the value potential. Bring together finance, supply chain, product purchasing and logistics leaders and ask a few crucial questions:

- How much money could be saved by reducing the volume of inbound trucks by 20%–40% and having these shipments arrive on a predictable schedule?
- How much on-hand inventory could be reduced due to more reliable deliveries of just the right replenishment quantities?
- If we did not have to worry about our invested assets, what value could a neutral logistics provider offer to improve the efficiency of inbound deliveries from all suppliers?

It may take higher-level leadership – someone in the finance department or the C-suite—to push for this kind of collaboration within a retail organization. But when it happens, the answers to these questions typically suggest a compelling savings opportunity.

To truly make collaboration a company priority, you'll need to establish shared, company-wide objectives and back that up with incentives. To measure the cost of a product, consider the whole cost: the price you pay your supplier and all the money it takes to move that product from factory to store. When your purchasing and logistics teams join forces to push that number down, make sure to reward them.

Reinventing a crucial piece of the supply chain isn't easy, and it isn't risk free. It takes vision and determination. But if you approach collaboration correctly, your company stands to gain tremendous rewards.

About KANE

KANE helps consumer product companies get retail goods to market efficiently and effectively. We operate in every region of the U.S. and our logistics services include transportation, distribution, packaging, cross-docking, retail consolidation, and people logistics.

Looking for ideas to make your retail supply chain work better?

LET'S TALK

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