MULTICHANNEL MERCHANT

OPERATIONS SPECIAL REPORT

Why Yesterday's Carrier Strategy Has Expired

by **Tom Gresham,** Multichannel Merchant

The shipping landscape today for retail and ecommerce companies bears little resemblance to the one that existed just two short years ago. The COVID-19 pandemic and the subsequent spike in demand for products, driven by an explosion in ecommerce and a nagging labor shortage, has put capacity at a premium and left shippers struggling to keep up.

The result has been a refashioning of the simple supply chain truths and principles that many shippers have leaned on for years. Shipping practices that worked for decades with minimal disruption and high predictability suddenly don't work anymore.

Carrier strategy is among the areas to experience the most dramatic changes. For years, the optimal carrier strategy was straightforward for many shippers: Link up with a national carrier and give them all your business to secure the best possible rates. The pandemic has altered the landscape, as the major carriers hike prices and cap volumes in response to skyrocketing demand.

That demand appears likely to continue to grow. Brie Carere, chief marketing officer for FedEx, said in a conference call with analysts in September 2021 that the parcel market is expected to expand 10% annually through 2026, according to BloombergQuint. That same month, FedEx announced a general rate increase (GRI) of 5.9% for 2022, a departure from the traditional lockstep 4.9% of itself and UPS, which is really a starting point for shippers.

As a result, today's retail and ecommerce shippers must be more flexible, adaptive and creative, while pursuing strategies that would have seemed unthinkable for many just two years ago.

Richard Palmer, who is in enterprise sales with multi-carrier software provider ProShip, said the industry has been stagnant and predictable for years, sticking to an accustomed way of doing things. The pandemic-related disruption since March 2020 has been significant, he said, with some shippers still unable to fathom what is happening.

"It doesn't seem like it's still quite resonating with some of them, what their challenges really are," Palmer said. "They haven't experienced this before. People tend to be in disbelief that something could change this much this quickly. It's human nature. People are in shock and trying to figure out what the next step is."

CONTINUED ON PAGE 2

FEATURED IN THIS REPORT

Finding a New Carrier Strategy

Palmer said the biggest element necessitating a change in carrier strategies is the volume limits imposed by UPS and FedEx. Shippers who were used to giving all their volume to one carrier to secure the best discount ran into a major obstacle as demand exploded and networks were flooded, a problem that still persists. FedEx said as part of its 2022 Q1 earnings report that the labor shortage was causing "network inefficiencies, higher wage rates and increased purchased transportation expenses."

The capacity limits in particular have hampered shippers in growth mode that needed a carrier to support that spurt. UPS estimated that demand for its services surpassed capacity by 7 million packages per day during the 2020 peak, and projects that figure will be 5 million packages per day during the 2021 holidays.

FedEx and UPS have made it clear they are prioritizing margins and profits over shipment growth, said Tim Sailor, principal of Navigo Consulting Group. In a July 2021 earnings call, UPS CEO Carol Tomé referred to her company's approach as the "better not bigger" strategy. That means less pricing flexibility and more surcharges for less desirable freight, such as oversized items or those requiring additional handling.

Sailor said the surcharges and rate hikes by FedEx and UPS in the pandemic era have played a particularly strong role in convincing shippers to seek a new carrier strategy. Because today's landscape is unlike any that preceded it, Sailor said, shippers are compelled to develop a distribution strategy reflective of these new conditions.

Experts say the key to a successful carrier strategy today is flexibility. A key strategy for building flexibility is through a diversified mix and becoming a multicarrier shop. Large shippers, in particular, need multiple options to provide "safety value" in case their primary carrier caps volume or applies a rate increase, said Kenneth Moyer, partner and vice president of supply chain strategies at LJM Group.

Sailor agreed that the concept of putting all of your eggs in one basket is "a completely outdated paradigm today."

"Right now, shippers are at a disadvantage in their relationship with the carriers," he said. "So, the question is, how do you create leverage? One of the best ways you can create leverage is to engage in a multicarrier strategy."

John Haber, founder and CEO of Spend Management Experts, said shippers today need creative thinking, a good TMS, longer lead times and acceptance of the reality that they have to pay higher rates and surcharges to gain sufficient capacity. Haber said a carrier strategy should include more than one mode of transportation and have built-in risk mitigations if capacity is cut, freight is delayed or other complications arise.

Diversification and redundancy are not just about carriers – they're also about having a range of levers to pull when necessary to keep the orders flowing in the face of capacity challenges. That can include solutions such as offering consumers a discount to buy a product online and pick it up at a store, or for accepting a longer delivery time. Zone skipping, line hauling, drop shipping from vendors and ship from store also may be productive alternatives for some shippers.

Clint Boaz, senior sales engineer with ProShip, said shippers are seeking to go beyond simply mixing up their carriers and instead also considering changing their distribution model itself.

"More businesses are reevaluating the supply chain as a whole with much more scrutiny and urgency than they have in the past, as opposed to just mixing up what carrier they signed a contract with this year," Boaz said.

The Rise of Regional Carriers

Haber said regional carriers have played a critical role for some shippers during the pandemic, particularly in developing a multicarrier strategy.

"Regional carriers have become an alternative solution to UPS and FedEx who have cut capacity for some of their customers in an effort to maintain profits," Haber said. "For those shippers looking to position inventory and deliveries closer to customers, regional carriers have become a go-to since they tend to operate only in a few states."

Moyer said he highly recommends investigating regional carriers as shipping options, saying they "have really come into their own in recent years." He noted that prominent regional carriers saw robust growth in 2020, particularly LaserShip, primarily on the East coast but recently expanded to Tennessee (+58%), LSO, in the Southwest but expanding into the Midwest (+100%) and OnTrac, from the west coast into Colorado (+34%).

"These carriers provide an important safety valve to the national carriers in these times of limited capacity," Moyer said.

In his experience, Sailor said, regional carriers tend to have better rates and surcharges. Depending on location, he said, shippers may have an opportunity to reduce transit times with regionals, as well.

Sailor said he recently finished a project with a parcel shipper that was with a major carrier and its costs were going up and up. In a distribution analysis, he said the company determined that 30% of its shipments were eligible for a regional carrier. It shifted that volume to a regional, reducing its shipping costs and gaining a day in average transit time – particularly impactful since it had a perishable product. The rapidly growing shipper was maximizing its current carrier agreement, so the shift was be made without jeopardizing its primary carrier discounts.

The recent and growing emphasis on regional carriers led to the highly unusual result of several shutting off volume during the 2020 peak season, and now doing the same as they look ahead to forecast demand in Q4 2021. In light of those conditions, planning ahead is more important than ever.

"Shippers really don't have a choice but to get ahead of it and to get those contracts going with the regionals," Palmer said.

Palmer believes regionals will continue to grow during the next 5-10 years. As noted above, some regionals have begun expanding outside their traditional footprints, building on growing volume that justifies entering those areas.

Ensuring Survival in a Carrier's Market

When the major carriers focus on profitable accounts, profiles and categories, shippers must be creative and disciplined to survive as carriers take advantage of their leverage. Moyer said their shift in focus has been a huge struggle since COVID hit, especially for large enterprise accounts. For instance, he has seen UPS approach large shippers with aggressive incentive programs and tell them their contracts were in danger of being canceled. In order to continue to receive service from UPS, the shippers had to sign a new contract, sometimes with cost increases north of 20%, Moyer said.

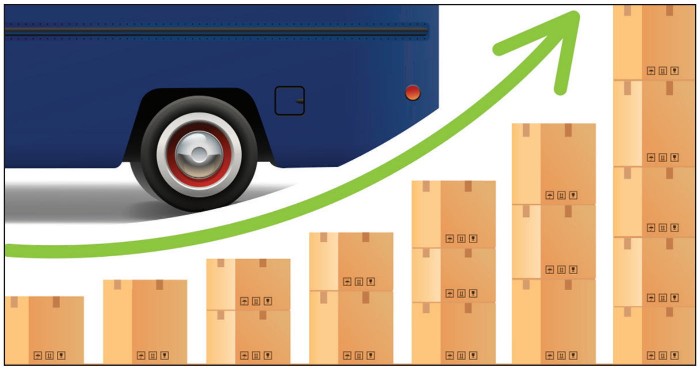
"With more business than they can handle, the national carriers have the luxury of shifting their focus to yield management," Moyer said.

In such a climate, Moyer said the shippers' best defense is not only creating a multicarrier environment that allows for excess volume to be diverted, if necessary, but working with their primary carrier to find other ways besides higher rates to make their account more profitable. For example, he said, pre-sorting packages and practicing good label discipline can reduce carriers' hub sortation costs, perhaps avoiding a mid-term rate increase.

Boaz said surviving in a seller's market starts with a shipper understanding its strengths and attractiveness as a business to carriers. For instance, someone with a high volume of heavy goods going B2B through a premium service is more attractive than someone shipping low-volume, low-value, low-weight goods to residential addresses.

"Recognizing the nature of your business, what you offer to the carrier and how it distinguishes you from others is critical when you sit down to the negotiating table," Boaz said.

Palmer said automation can play a role in helping shippers navigate their best carrier options in a more complex landscape, providing them with critical visibility and insight. For instance, you may lose some of your previous earned discounts when using software for network management based on business and cost rules, "but you can get it back or even exceed it with proper rate shopping among carriers that are still competing for your business," he said.



A critical question shippers face is how to maximize and maintain their discount while staying within capacity constraints. "Those shippers who can accomplish this effectively will have a significant competitive advantage over the market," Moyer said.

Moyer said success in this area starts with technology. He pointed to TMS systems that can optimize carrier choice by time in transit, cost and customer preference while load balancing carrier volumes to meet commitments. "Investing in cutting-edge technology solutions often provides an impressive ROI," Moyer said.

Boaz said hitting your sweet spot requires keen analysis on the front end (understanding your parcel shipping profile and available services) and sharp execution on the back end (putting systems in place that enable a multi-carrier approach, while enforcing your business rules).

"And the rules you put in place need to be easily configurable," he said. "So, if next week one of your major carriers tells you they're going to cap your capacity again, or a regional carrier goes out of business, you can make adjustments on the fly and still be able to capitalize on the most efficient mix without significant pain."

In the past, Moyer said national carriers have made a major push to eliminate any toehold their competitor may have had in an account in order to be a shipper's sole carrier.

"I think in today's world, except for small shippers, this approach comes with more dangers than benefits," Moyer said.

The Bottom Line

Throughout the new "post pandemic" era, major carriers have raised rates, increased surcharges and penalties, capped volumes and declined service to less profitable accounts. Through these practices, they've underscored the idea that a multicarrier approach is not only optimal but necessary for many.

For those that don't adapt, the consequences may not just be higher costs but a perpetual struggle to simply ship their products. Ultimately, the major carriers have forced shippers' hands to look elsewhere, and the impacts will reverberate for years.