How Best-in-Class Shippers Are Reducing the Impact of Logistics Costs and Capacity Constraints

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Initiatives: Logistics and Customer Fulfillment

Disruptions in the ocean freight and airfreight sectors are constraining capacity and sending prices sky high. Logistics leaders must adapt to this ongoing volatility by implementing new strategies for managing 3PL providers and carriers.

Overview

Key Findings

- Shippers feel powerless on correct strategies to address air and ocean freight rate increases and capacity constraints.
- Years of inertia on the part of shippers, such as poor capacity planning, inaccurate forecasts and a lack of transparency, have led to punitive penalties from logistics service providers.
- Shortfalls in creating integrated partnerships with logistics providers across all functions and seniority levels prevent the ability to leverage key relationships during critical periods.

Recommendations

Logistics leaders responsible for customer fulfillment, carriers and third-party service providers should;

- Secure space and optimize costs by providing and delivering on accurate shipping forecasts.
- Improve the ease of doing business by enhancing end-to-end processes to more effectively communicate capacity requirements and optimize costs.
- Ensure costs are controlled and capacity is managed by focusing on more collaborative partnerships with third-party logistics (3PL) providers.
Introduction

Decades of oversupply in ocean freight and airfreight capacity created an almost uninterrupted period of shippers driving down prices. Ocean and air carriers, complicit in the commoditization of their industry, engaged in a price race to the bottom in an effort to grab market share and fill their ever-growing ocean and air freight capacity. Shippers became addicted to lower and lower rates, and carriers found themselves powerless to stem their downward spiral.

These consistent demand patterns and oversupply of capacity provided contract and negotiation landscapes optimized for shippers to achieve consistently lower costs and favorable terms. These desirable outcomes for shippers were achieved with relative ease as carriers fought between themselves to achieve greater market share and optimize their assets.

The onset of COVID-19 during 2020 heralded a seismic shift in the global transport industry, bringing severe capacity constraints and spiraling cost increases. The volatile market is unlikely to recover before 2023, and the recovery will not see us return to pre-COVID-19 rate and capacity levels. Figure 1 details the movement in ocean container rates over a 12-month period.
Similarly, the airline industry has very publicly suffered immensely as a result of COVID-19, as their operational and commercial models relied heavily on a well-blended mix of passenger and freight volumes to deliver optimum yields. In 2020, airline industry revenue totaled $328 billion, around a 40 percent decline of the previous year's total.

Figure 2 shows the steep decline in air industry figures in 2021, according to the Air Transport Bureau.
The impact on ocean and air transport has sent shockwaves into all sectors of the logistics industry, exposing previously hidden weaknesses at its very core. This research details actionable approaches that logistics leaders should adopt in an effort to mitigate the disruption and secure their global transport needs and more effectively manage their costs.

**Analysis**

**Forecast and Planning Accuracy Drives Carrier Performance and Reliability**

Booking cancellations, rebooking of shipments and erratic volume patterns all combine to increase workloads and costs across the logistics sector. Inconsistencies due to lack of planning and inaccurate shipping forecasts drive even greater potential for volatility in a 3PL network. This risk is calculated and planned into a 3PL provider’s costs and drives conservative capacity planning to ensure space is optimized. Building 3PL relationships through sharing transparent data from effective planning and forecast tools will demonstrate reliability and consistency. This position of trust in your data, and delivering on commitment, will assist in reducing these risk factors and help build a collaborative relationship with your 3PL provider.

**Forecast and Planning Reliability**
In the foreseeable future, it is clear that carriers in both the ocean and air markets will not be able to offer shippers the flexibility and tolerances around fluctuating demand for space they previously accommodated. In the future, carriers are favoring customers who can offer transparency on forecast planning and deliver on their commitments.

Carriers and 3PL providers alike will favor shippers with accurate demand data by offering them greater levels of cost and service reliability in exchange for better order visibility.

Improving forecasting and demand planning accuracy across your product base, and translating this into more accurate shipping forecasts for ocean and air, will allow your carriers to plan, prebook and secure capacity for your shipments.

In this product planning stage, it is vital that shippers segment products based on two factors (volatility and volume). The ability to distinguish products in this way will enable you and the provider to prioritize shipments based on their level of importance in times of capacity constraints.

Carriers in the future will be less flexible, providing contract space over and above the contracted volume if the spot market is healthy. Consider this possibility in your planning stage. Managing product portfolios and allocating based on customer demand will help manage the supply-and-demand cycle in a constrained environment.

Figure 3 demonstrates, based on Gartner research, eight key recommendations on how effective management of the supply planning and demand management within your organization can assist organizations in navigating these highly volatile periods.
Agreeing on a tolerance level in advance that a carrier can easily accommodate variances forecasted volumes versus delivered volumes (actual volumes +/- 10% on any service), will give logistics teams better predictability of when future disruptions can occur. This advance predictability of potential disruptions will allow business continuity planning (BCP) to start at an earlier stage (see Supply Chain Executive Report: Drive Customer Value Through Culture and Insights).

Process Improvements Will Reduce Logistics Disruptions

Simplifying logistics processes will help your 3PL and logistics partner more effectively manage and handle your orders and shipments in a more consistent manner. If the end-to-end shipment management process for 3PLs was thought of as a production line, it makes sense that the more consistent and easy an order, the quicker and more efficiently it can be handled. Those orders that require more manual intervention, and are harder to predict and manage, will take longer to process. The easier and more consistent orders will be managed first in line as they can be processed quickly; whereas, harder orders will be handled last as they require more insight, planning and internal collaboration to deliver successfully.

It makes sense that shippers who work on creating a framework of logistics processes and procedures to deliver simplified and consistent orders will position themselves at the front of the line for available space and cost considerations. These best-in-class shippers win considerable favor from 3PL providers, as these are the clients that can be leveraged across their operations and can plan to improve their own internal processes to get efficiency gains. Some areas that logistics organizations are looking at to improve to simplify their end-to-end processes are identified in Figure 4.
Adopting lean processes and networks will streamline your logistics surface area, creating a smaller target area which will be less prone to associated risks (see Figure 5). Gartner's Supply Chain Executive Report: Shaping Supply Chain Disruption in a Volatile Risk Environment indicates that if the supply chain surface area is thought of as a target, it makes sense that smaller surface area organizations perform better than their peers in this risk environment. With a higher cadence of risk events, a smaller surface area is an asset, but a larger surface area will become a major liability.
Focus on More Collaborative Partnerships With 3PL Providers to Control Costs and Manage Capacity

Highly Fragmented Sector — Knowledge Is Power

The logistics industry is highly fragmented and relies heavily on outsourcing and partner programs to drive scale and coverage.

This fragmented network is evident across the 3PL industry, offering anonymous services across a large partner network in the airfreight, ocean freight, transport and warehouse markets, often with wide variances in service levels.
In the past, shippers enjoying a proliferation of space with all-time-low costs would spend little time to understand and specify the service level, or understand the variety of services on offer. If there were few or no exceptions, or large and regular service failures, logistics providers were allowed by shippers to specify services, and products goods would be shipped.

However, this lack of transparency in the industry is now being questioned and queried by shippers, who are in search of ways to influence better outcomes in their networks and from providers. In the current logistics climate, it is prudent to better understand the partners, products and services that are being utilized by 3PL providers within their global networks. This will enable organizations to direct negotiations with 3PL providers and carriers to optimize networks and costs.

Understand the following target areas to better make decisions on carriers that can support your product flows and alleviate potential risk (see Figure 6):

- **Capacity** — Which carrier holds the most space on a particular trade route and who are their partners?
- **Transit time** — What is the port-to-port transit time on a route and is this being met?
- **Frequency** — How often are these services operating?
- **Route** — Is the route consistent and are there any transit points with equipment changes?

**Figure 6: Understanding Logistics Networks**

A Commoditized Market — Shipping Lines
Ocean carriers have exercised greater control over supply and demand through consolidation, and there now exists three primary carrier alliances that control around 80% of global capacity. Understanding the ocean carriers’ offerings within different trade lanes and markets will allow logistics leaders to focus their discussions with 3PL providers to obtain the right service, at the right price, with the right provider (see Figure 7).

Logistics leaders can ensure they are selecting the right carrier and service for their business in the following ways:

- Request the carrier and/or transit time for the service you are being quoted.
- Request data on historical transit time adherence.
- Request data on schedule reliability.
- Look at risks around transshipment air/ports and any change of equipment.
- Request notifications of changes to rotations or schedules.

**Figure 7: Ocean Carrier Alliances 2021**

![Ocean Carrier Alliances 2021](Source: Navegate)

In the future state of global supply chains, it is imperative to consider these critical factors to ensure you are protected from the ongoing threat of cost spikes and capacity compression (see Figure 8).
Figure 8: Checklist of Actions to Manage Future Disruptions

**Checklist of Actions to Manage Future Disruptions**

<table>
<thead>
<tr>
<th>Planning and Forecasting</th>
<th>Process Improvement</th>
<th>Industry Expertise</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Align S&amp;OP and S&amp;OE functions to ensure ongoing planning accuracy.</td>
<td>✓ Ensure product master data is correct with correct lead times.</td>
<td>✓ Understand the logistics infrastructure surrounding critical suppliers/customers.</td>
</tr>
<tr>
<td>✓ Agree space and cargo commitment with 3PL or carrier on weekly or monthly basis.</td>
<td>✓ Ensure incoterms are correct and agreed with supplier.</td>
<td>✓ Have greater knowledge of logistics networks – best providers in each location.</td>
</tr>
<tr>
<td>✓ Communicate shipment plans in advance with any deviations to forecast.</td>
<td>✓ Correct paperwork checklist based on product and country requirements is supplied in advance of shipments.</td>
<td>✓ Develop more integrated relationships at multiple functional levels with your provider to give you leverage.</td>
</tr>
<tr>
<td>✓ Ensure accountability in contract for any failure to move agreed forecast.</td>
<td>✓ Ensure inventory holding is optimized and correct protocols agreed and reviewed.</td>
<td>✓ Invest in the right visibility tools to give you a deeper and wider view of your supply chain.</td>
</tr>
<tr>
<td>✓ Correct metrics are in place to measure performance or improve process.</td>
<td>✓Correct paperwork checklist based on product and country requirements is supplied in advance of shipments.</td>
<td>✓ Engage procurement and select the right provider for your business with a mutual beneficial agreement.</td>
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**Source:** Gartner

**Evidence**

This document is supported by industry research and extensive industry engagement. It is further substantiated through Gartner research and insight along with wider research and intelligence (see Supply Chain Executive Report: Shaping Supply Chain Disruption in a Volatile Risk Environment and 3 Must-Do Steps in the Allocation Management Process).

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