Eliminating Unseen Transportation Expenses

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As the economy slowly recovers from the recent recession, food manufacturers are continuing to seek ways to contain costs. Inbound transportation is one area ripe with cost saving potential, but is often overlooked. Inbound transportation costs can comprise as much as 35 percent of some companies' total logistics cost. Controlling those costs can be significant because any savings in inbound transportation costs can go directly to your bottom line.

Typically, the majority of inbound transportation is prepaid or "delivered" — that is, the transportation is arranged and paid for by the vendor. But when shipping choices — including setting rates, choosing carriers and assigning classification codes — are left to the vendor, the purchaser has little control over the inflow and transportation charges related to its goods. This can lead to production delays, stock shortages, late deliveries and, ultimately, higher costs.

How much higher? The markup for vendor prepaid transportation can be as high as 40 percent. The higher costs result from the fact that most vendors use transportation as a profit center. They build excess transportation and handling charges into their delivered, prepay-and-add and bundled product prices. And when they negotiate reduced transportation rates, they often don't pass the savings on to their customers. If you make your purchases on a freight collect basis, you may not be effectively leveraging your company's buying power to get the lowest transportation rates possible.

If food manufacturers can learn to identify these hidden expenses, eliminate them and enact other cost-saving measures, they can save 10 to 25 percent on transportation costs. For the majority of large manufacturers, this represents hundreds of thousands, if not millions, in savings.

Seven Steps to Reduce Inbound Transportation Costs

Step #1: Conduct an audit of your current inbound transportation process. Start by reviewing who your vendors are and from where they ship. Then determine the volume in each lane — the route between the pickup and delivery points — and, if shipping by truck, the merchandise class being shipped.

Next, discuss with your purchasing and receiving departments the visibility your company requires regarding shipments and transit times in each lane. Conducting a lane-by-lane benchmarking analysis will enable you to identify poor carrier service, inefficient routing decisions and too-high rates on inbound shipments. In the lanes with particularly poor service and high rates, start to implement changes by switching to the carriers with which you’ve chosen to negotiate.

Determine total annual costs for inbound transportation, then calculate it as a percentage of gross sales. This gives you a cost baseline so you can accurately track your cost savings. The audit becomes the backbone of any solid vendor inbound transportation program, and is the first step in taking control of your inbound transportation costs.

Then, take the information you’ve gathered from the audit and undertake the following:

Step #2: Evaluate and implement appropriate transportation classifications for the items you ship. Domestically, every item has a National Motor Freight Classification (NMFC) number that equates to a classification and directly correlates to the rate charged. The higher the classification number, the higher the transportation rate — and these rates can vary by hundreds of dollars per shipment. Additionally, items shipped internationally have a Harmonized Tariff Code (HTC) that serves a similar function. By implementing appropriate transportation classifications, some food manufacturers will be able to save up to $100,000 or more per year.

Step #3: Develop and enforce a vendor routing guide. Routing guides help you control costs and improve receiving efficiency. The guide itself should be simple and on one page, and it should be included with the purchase order as a separate item. It should include proper routing instructions telling your vendors exactly which carriers to use by transportation mode and in priority order. When you distribute your guide to vendors’ shipping departments, your single carrier choices should be entered into your vendors’ order-processing systems. Use the guide to enforce vendor compliance. Clearly state the rewards for strict adherence and the consequences, such as charge-backs, for those who neglect your routing instructions.

Step #4: Demand that transportation be clearly identified on each vendor’s invoice. Don’t accept pre-pay and added or “free” transportation. Sometimes transportation is prepaid and added to your invoice. But often transportation is buried in the price you pay for each item shipped. This is called free freight. (Working with suppliers to break out transportation costs from the cost of goods isn’t easy; the process requires frank conversations.)

Step #5: Create visibility. In-transit transportation tracking will reduce the time buyers spend confirming shipments with vendors. It also helps to monitor individual carrier performance. So, look for carriers who can supply such tracking methods. Also, utilize these reports to file for service failures with small parcel carriers for not performing up to their guaranteed services.

Step #6: Adopt a core carrier program that identifies strong carriers in given lanes. Having 20 carriers backing up to your receiving dock can create continual confusion in your distribution center and become overwhelming to manage. In creating a core carrier program, you identify pick-up coverage, service facility locations, financial stability, systems and technology prowess and transit times.

Step #7: Negotiate lower transportation rates. Leverage your volume to get better transportation discounts on both your international and domestic transportation. In most cases, the fewer providers you utilize the more leverage you have. Negotiate with your carriers to eliminate or modify extra charges identified during Step 1.

One way to leverage your transportation volume is to band together with other companies to pool resources and buying power. Many manufacturers are currently benefiting from consortium transportation rates, and some of the most cost-effective consortia are among companies in a single industry — such as food manufacturing — which collaborate on the supply chain. Single-industry-specific consortia can be more effective than other multi-company arrangements because the pricing can be geared specifically toward a single industry’s commodities (Step 2); routing guides are easier to enforce because more companies are shipping from common vendors (Step 3); and the more freight pickups that occur at common vendors (Step 6), the more productive core carriers are, enabling the carriers to provide more competitive pricing. Additionally, carriers’ pricing tends to be more aggressive when they know they’ll lose out on multiple accounts — not just one — if their pricing isn’t right.

One way to engage in consortium rates is through an independent third party that can gather the data, negotiate single-rate base contracts with a limited number of carriers and supply the software to track shipments. A third-party alliance can increase your buying power without your having to share information with competitors.

Proactively managing your inbound transportation can help you reduce costs and improve your supply chain. The keys are to take control of carrier selection and classification decisions; track all inbound transportation dollars expended; and reduce the number of delivering carriers. The resulting savings will make the effort well worthwhile.

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