

## 3PLs Find It Difficult to Close the IT Gap

By Steve Banker

### Keywords

Logistics, 3PL, IT Infrastructure, Warehouse Management, Transportation Management, WMS, TMS

### Overview

Dr. John Langley of Penn State has been doing comprehensive third-party logistics (3PL) surveys for many years. His surveys have documented something he calls the "IT gap" - a gap between the importance shippers attach to a 3PL's IT competence and the shipper's perceived competence of the 3PLs it works with.

This Insight reports on "IT Gap," the difference between a shipper's opinions on whether it feel information technology is a necessary element of a 3PLs expertise versus its view of how competent its 3PL is in the IT area. We explain why it is so difficult for 3PLs to close this gap and the implications for a shipper that is selecting a 3PL for outsourced logistics services.

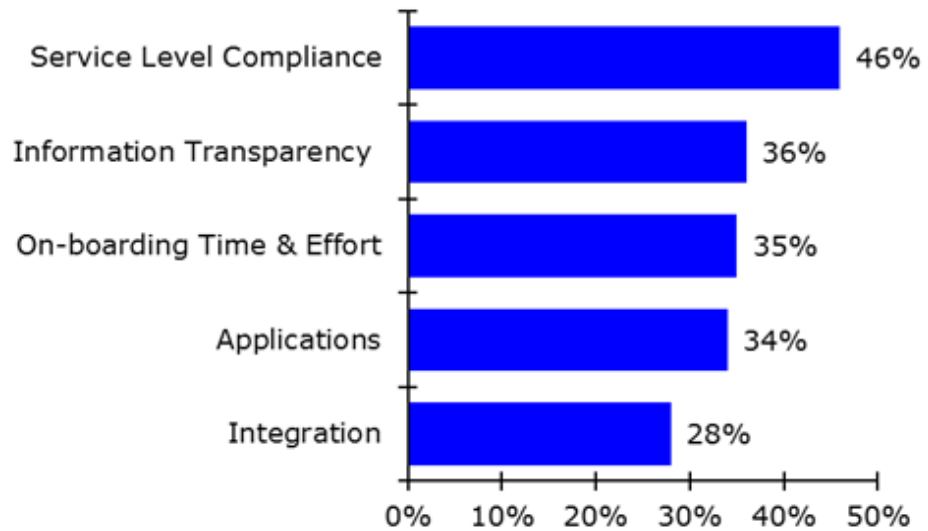
While this gap, first reported in these surveys 11 years ago, has narrowed, it remains substantial. The most recent report analyzes some of the reasons for this gap, but ARC Advisory Group believes the fundamental explanation is that achieving IT excellence is expensive, requires a great deal of time, and has a difficult-to-fully-quantify ROI. These have implications for shippers choosing a new 3PL partner.

### The IT Gap

For 17 years, John Langley of Penn State has been doing comprehensive third-party logistics (3PL) surveys. As always, his most recent report, *2013 Third-Party Logistics Study: The State of Logistics Outsourcing*, had a very large number of respondents; over 1,500.

Ninety-four percent of shipper respondents report they believe IT is a necessary element of 3PL expertise, but only 53 percent are satisfied with their 3PL's IT capabilities. While this IT gap, first reported in these surveys 11 years ago, has narrowed, it remains substantial.





Percentage of Shipper Responses of Above Average or Better for 3PL Capabilities

### Closing the IT Gap Is Costly and Difficult

The 2013 report provides some analysis of the reasons for this gap, but ARC believes that the fundamental explanation is that achieving IT excellence is expensive, requires a great deal of time, and has a difficult-to-fully-quantify ROI.

In the chart above, we see that only 34 percent of shipper respondents felt that their 3PLs had above-average or better capabilities in the applications area. The applications shippers cared most about were warehouse management (WMS) and transportation management systems (TMS), depending upon what is being outsourced. Putting in a centralized WMS that serves large numbers of warehouses would cost millions. A multi-modal, multi-region TMS can cost tens of millions, particularly if the supplier charges based on freight spend moving through the system.

But paradoxically, the ability of 3PLs to delight customers is being stymied by their existing customers. One 3PL put in an advanced TMS and yet only half of the freight it procures for customers is being managed with the modern TMS. While the 3PL has gone from six legacy TMS solutions to four, it has not been able to standardize on the new TMS solution. The problem is that old customers often do not see the value of going through the new set of integrations required to be served by the modern TMS.

But more fundamentally, the problem is that many 3PLs have grown through acquisition. Consequently, they end up with a hodgepodge of logistics and ERP applications and IT infrastructure products (hardware, operating systems, and middleware) across the different business units. Achieving information transparency, the ability to onboard new customers quickly, and to integrate to a wide variety of customer applications all depend upon a 3PL having a coherent end-to-end IT infrastructure. For some 3PLs, this has meant standardizing on a set of enterprise applications and IT infrastructure products from one supplier. For very large 3PLs, these kinds of order-to-cash transformational projects can cost in the low hundreds of millions and implementations can take five plus years.

Further, the payback for these investments can be long, again five plus years. But the explanation for this is partially that strategic IT investments have some quantifiable benefits (total cost of ownership, IT headcount reductions, and other labor-saving process improvements); while other benefits (revenue growth and improved contribution margins) are difficult to tie to any specific IT project. However, C-level executives will admit they could not have achieved some impressive financial improvements without the IT transformation.

In fact, payback period is often a flawed way to look at ROI; low-cost projects that pay back quickly can be far less meaningful than more costly projects that generate much larger savings and revenue enhancement opportunities over a much longer period of time.

### **The Lease vs. Own Debate**

According to the logistics outsourcing report, shipper respondents devote an average of 12 percent of total sales revenues to logistics. And of that spend, 39 percent is devoted to outsourcing. That is actually down a bit from last year when 42 percent of the logistics budget went to 3PLs. The part of the logistics budget devoted to 3PLs is likely to rise again next year. Increased regulatory burdens, particularly for companies that own their own fleets, and an economic environment that has recently become more uncertain, have companies reexamining their outsourcing strategies.

## Recommendations

When companies examine 3PLs for their capabilities, it's important to carefully consider the coherence of the 3PLs overall IT infrastructure. Some helpful questions to ask include:

- Has the 3PL standardized on a functionally rich, flexible warehouse management, transportation management or global trade management system? Do these products have a protected upgrade path? How often are these products upgraded?
- Does the 3PL have a consistent approach to middleware, portals, business process management and SOA development tools, and other key components of an IT infrastructure across all divisions?
- Does the 3PL have a unified enterprise application environment that allows for a customer-friendly quote-to-cash process?
- What is the 3PL's multi-year IT roadmap?

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