Outsourcing Private Fleets

Informed fleet managers and financial executives will consider conversion to dedicated contract carriage.

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Framework for considering private fleet conversion to dedicated contract carriage.

Private fleets have been a mainstay of U.S. business distribution strategies throughout the 20th century and continue to be so into the early 21st. Industry data tells us private fleets are a $124 billion enterprise, making up roughly 24% of the total truckload marketplace.

While private fleets continue to play a large, integral role in U.S. business, emerging industry trends and market research results suggest companies are beginning to consider alternative, outsourced solutions. Certainly, the recent economic downturn has accelerated the process, as it has forced CFOs to challenge all spending within organizations, including those functions that have always been taken for granted as core to the business, such as private fleets.

Recently, a comprehensive market research study was conducted to better understand private fleet operators' consideration of an outsourcing model, or dedicated contract carriage (DCC), as an alternative to their private fleets. Both transportation and finance executives were interviewed.

Research findings provide a framework for private fleet operators in determining whether outsourcing to a DCC is a viable business alternative. This decision model includes the following considerations:

Why do I maintain a private fleet?

Do I understand the DCC concept?

How do I benchmark my private fleet vs. DCC?

Private fleet operators must first understand the DCC concept before analyzing alternatives to their private fleet.

Earlier this year, the 3PL consulting firm SB Hirsch, Inc., conducted in-depth interviews with executives at firms with private fleets. Firms represented included food products, manufacturing and processing, and retail and wholesale. Respondents were either individuals with decision-making authority and overall responsibility for private fleets or those with financial decision-making oversight.

Research findings identified a series of long-standing perceptions suggesting why survey respondents believe their firms still rely on private fleets. Among them is the primary reason why private fleet operators do not consider conversion to DCC – a limited understanding of the DCC model.

The chart below summarizes the gaps between respondents' perception of DCC and the reality of DCC.

Model Characteristics	Private Fleet Model	Dedicated Contract Carriage (DCC) Model	
		PerCePtIon	realIty
Management	Managed internally	Company contacts carrier with daily route requirements	Managed on-site by DCC with ongoing communications with company
Drivers	Company drivers	DCC provides drivers on an as-needed basis	DCC provides dedicated group of drivers
Driver Domicile	Company-designated distribution center	Driver picks up equipment at DCC depot and then goes to company distribution center	Company-designated distribution center
routes	Typically, same driver operates same daily (weekly) trip profiles	Different drivers each day for routes	Designed for same driver to operate same daily (weekly) trip profiles
Flexibility	Company can make operational changes quickly, except in the case of union drivers	Drivers are tied to rigid routes and schedules	With on-site DCC management and broad capabilities, DCC can provide necessary levels of flexibility
Customer Service	Company drivers provide customer service function	None	DCC drivers trained to provide customer service functions
Branding	Uniformed drivers and branded vehicles	Only branding may be for carrier	DCC drivers are uniformed and vehicles are branded for the company
Financial Investment	Company financial investment	Typically, DCC owns or leases all equipment	Typically, DCC owns or leases all equipment
liability	Primary liability on company	Primary liability is placed on the carrier; however, since the shipper is the better known firm, they will be fully exposed in any lawsuit	Primary liability is placed on the DCC
Balance Sheet	Company keeps purchased assets on their balance sheet	Company may still be required to purchase or lease equipment that is operated by carrier	Company is freed of capital commitments made to purchase tractors, trailers and other related traditional private fleet expenses
revenue Gain Sharing	Typically, secondary consideration	Little or no effort on revenue gain sharing	Actively engaged in seeking out backhaul revenue gain sharing
Brokerage	Handled internally, with primary or multiple brokers	Not applicable	Can provide full range of complementary brokerage functions
require excess Capacity	Contact carriers seeking space	Not applicable	Provides access to capacity throughout overall network

Respondent feedback

The following comments reinforce these perceptions about the need for private fleets. However, it is worth reiterating that many of these comments are made without the benefit of a strong understanding of DCC capabilities.

With private fleets having grown up with many companies, many senior decision makers, including the CFo of a wholesaler, have not thought about changing distribution models:

"My guess is that no one has really thought about it in a long time. At some point the company was small and could handle everything with a handful of vehicles and just kind of sat down and said let's look at our alternatives here. It is just one of those things where that's the way we have always done it, so that is the way we are doing it."

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not surprisingly, when private fleet operators better understand the range of capabilities provided by DCC, they are more likely to consider this outsourced model. For example, a wholesale fleet director tells us that employee and regulatory savings can be significant:

"I think one of the big things that would probably influence that would be not so much the fleet itself, but maybe some costs centered around employees. Because with every one of those trucks comes a truck driver and benefits and medical insurance and all the other costs associated with that driver. That is as big a cost as anything."

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a wholesale CFo clearly understands that backhaul can be a tipping point to convert from private fleet to DCC:

"That may be what tilted the table at (previous company), because for the most part, all their trucks were coming back empty. That is a lot of empty trucks and empty miles… So there are a lot of headaches that someone else can do, and they probably know how to do it better than we do."

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a manufacturing business owner can see how as a fleet gets larger, and complexity and liability issues increase, it may make sense to convert to DCC:

"After a certain size, it is going to be hard to manage the fleet. You have more and more drivers, and more and more equipment and everything…I think that the owner is probably going to do an exit strategy somehow."

Making the right decision for your organization requires a different approach to benchmarking private fleets vs. dccs.

Research findings suggest a number of companies operating private fleets may not be accurately weighing the variables that drive the decision to either maintain a fleet or outsource to a DCC. Not surprisingly, when private fleet operators better understand the range of capabilities provided by DCC, they are more likely to consider this outsourced model. When they reach this realization, there are tough questions that need to be asked in order for private fleet operators to assess the DCC alternative. To achieve a true understanding of the DCC model's viability (or lack thereof), private fleet operators need to consider the following:

Company culture

- When looking at your transportation/distribution team, do you have "change activists" who regularly ask the simple question, "Why are we using this distribution model in our company?"
- Is transportation a core function of your organization or not? Should you be in the private fleet business?
- Is there a quantifiable benefit from a marketing and customer service perspective to running a private fleet? Have you actually compared this to external solutions?

Exterior benchmarking

- Do you have a clear view of the resources at your disposal – internal vs. external? It is critically important that you get a perspective beyond that of your transportation team. Too often we get comfortable and complacent. Do you benchmark against your competitors regularly?
- Even if you are satisfied with your private fleet today, do you bring carriers in to benchmark their service capabilities and pricing vs. your own? Does the firm have a formal plan to benchmark its private fleet with DCCs? Who is responsible for these business reviews? Transportation management or finance? What is the role of the CFO and other executive level team members in this process? How are the decision criteria established?
- If you already rely on third-party carriers, how financially stable are your carriers? What contingencies do you have in place should your primary carrier run into problems?

Fleet requirements

- How unique are your firm's distribution requirements?
- Are there DCCs currently serving your industry vertically? What is their track record?
- Based on their performance with your competitors, peers and/or industry partners, is it reasonable to believe a DCC can handle your requirements?

Assessment of DCC capabilities

- Does the DCC provide greater access to MIS and other technology?
- What are the advantages of taking capital dollars required to run private fleets off the balance sheet?
- What liability concerns can be mitigated when not running private fleets?

Fleet performance and financial reporting

- What are the fleet performance metrics and why were they established this way?
- What elements are included in fleet budgets (the fleet manager may have access to top-line data such as wages, fuel and repair costs but not to below-the-line expenses such as liability insurance, equipment depreciation and retirement costs)? We have found that this information may reside in three or more separate departments within a given organization.
- How are fleet budgets established and do these targets change over time? For example, if a company targets fleet costs on a percentage of sales, does maintaining that percentage over time demonstrate fleet management success?

To successfully conduct benchmarking with DCCs requires a team effort. Not only does the transportation department have to take an active role but other departments must also actively participate, including:

- Finance – to confirm that all relevant "above" and "below" the line costs have been adequately integrated into the analysis. Additionally, Finance needs to liaise with the corporate Strategic Planning group to determine optimum use of corporate capital, including prioritizing the value of fleet expenditures.
- Risk management – to conduct necessary "what if" analyses of liability exposure.
- Operations – to determine how well fleet service offerings meet underlying performance metrics and overall customer satisfaction.

Is conversion to DCC appropriate for your organization?

Our research identified a number of well-run private fleets characterized by strong MIS reporting, continuous improvement and regular benchmarking with other private fleets and DCC carriers. On the other end of the spectrum, the research also found a number of private fleet operators that were lacking in each of these areas.

While all businesses have their own unique set of operating characteristics, study findings strongly suggest that private fleet operators who actively stay abreast of industry trends, including regular benchmarking with outsourced DCC providers, are in the best position to make the correct fleet decisions for their organization.