WHITE PAPER

How Do Carriers Establish Shipper Pricing?

By Thomas Andersen

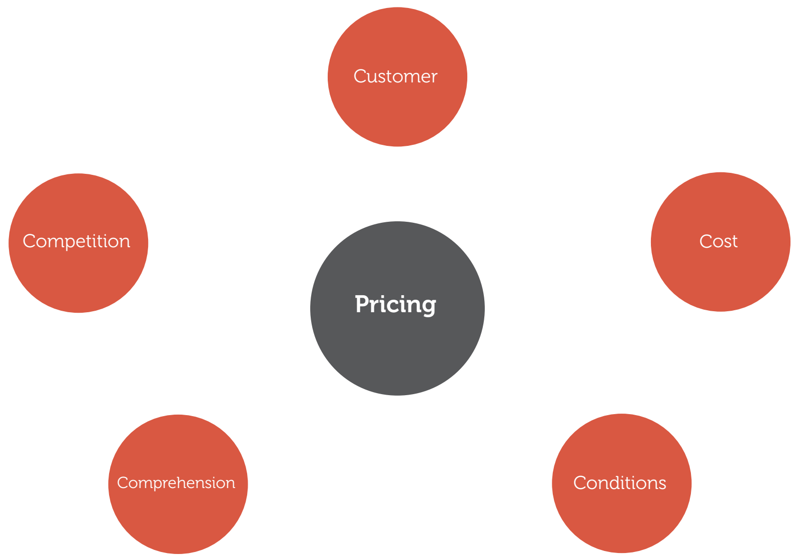
Negotiating pricing with a Carrier is similar to buying a car. There is the notorious sticker price. You expect to get a discount, which you assume that you have negotiated well after several rounds of having the salesperson go back and forth between you and the Finance Manager (the mystical force behind the black curtain). Once the deal appears to be finalized, they add a "destination charge" and you find that you will pay considerably more than you had budgeted. You don't have good ways to benchmark the results however, so you settle.

The car buying process has changed quite considerably, due in large part that the internet makes information readily available. Don't expect the same from the Carriers, however, as contracts are protected by legal language, which limits information from being shared with the public.

So you receive an invoice one week and then ask yourself... are others paying what I'm paying for the same shipments? Are other companies receiving greater discounts or reductions on any of the fees that consistently increase year over year? Bottom line, you ask, **how does my pricing measure up and how did the Carrier establish the pricing**?

Although there are guidelines that Carriers follow when negotiating pricing with Shippers; rates, fee concessions, and rebates certainly are not set in stone. Profit margins are protected, as a result of approaching opportunities, based on charging the maximum amount they expect a Shipper will pay. This applies not only to small to medium sized businesses, but also to National and Global sized companies.

The following are the 5 C's that the Carriers consider when establishing the price for a Shipper:



How Do Carriers Establish Shipping Pricing - By Thomas Andersen

CUSTOMER

A Carrier will evaluate what the needs of the Customer are? An experienced Account Executive anticipates the questions that are likely to be asked by his or her Pricing Analyst (the minimum level of involvement that's required for competitive discounts, fees, and incentives). Questions will include the following:

- As volume is a key driver, what's the size of the Shipper?
- Is Service, Price, Technology, or another requirement the primary component that will drive the Shipper's decision?
- Will the customer's shipment methods require special attention? Although it may increase the cost, applying a fee will generate revenue that could potentially lead to overall greater profitability for the Carrier? The "additional costs" versus added revenue will need to be considered.
- If a change in Carriers is desired, it is important to consider why? If the current provider is unable to properly service the account, less aggressive pricing is likely going to be needed for the Shipper to consider the switch. If price is the driving factor, but the Shipper is highly integrated with the current Carrier, additional concessions may be required, in order for the Shipper to consider a change.
- Most importantly, what's the customer's shipment profile? It will need to be understood, as it's the core basis to help determine what the costs are, and the revenue that will be needed to meet margin expectations.

COSTS

The Carrier evaluates the fixed and variable costs that are associated with managing the Customer and moving its packages. These costs are viewed, based on the activities that occur at the point(s) of origin, at the hub(s), during linehaul, as well as at the destination(s). The following are some factors that can impact the cost, which Carriers will consider, when establishing the price:

- Commodity
- Dangerous Goods - Hazmat
- International Requirements
- Locations (volume per location)
- Package Dimensions
- Product Mix (Air, Gound, & Intl.)
- Residential Deliveries
- Special Handling Requirements
- Temperature Control
- Weights (Actual/BIlled/Dimmed)
- Conveyable/Non-Conveyable
- Implementation Feasiblity
- Length of Haul
- Oversized Packages
- Pickup & Delivery Density
- Remote Deliveries
- Signature Requirements
- Spills
- Value / Scurity
- Zone Distribution

Fees, which often account for 30% or more of a Shipper's cost, are applied to not only offset costs that may be associated with these factors, but in many cases, turn "less desirable" shipments into highly profitable shipments.

Fees should be viewed as a control factor. Fees have historically been used to ensure that the costs that are associated with the worst case scenario are covered, and that the fee is aligned with its competitors. With improvements being made operationally, fees have increased while costs decrease, often making many fees lucrative profit centers.

How Do Carriers Establish Shipping Pricing - By Thomas Andersen

CONDITIONS

What are the Carriers' conditions internally? The Carrier has specific factors to consider on Global, National, Regional, as well as Local levels. The following are some examples:

- Whether it involves bringing on a new prospect or protecting a customer, the impact on the regional hub, local station, or fleet, is analyzed. One thing is certain, planes must fly and trucks must drive, in order to meet delivery times. In markets where fleet is operating at 90% - 95% capacity, the cost of adding or switching fleet will be considered. On the other hand, pricing can be more aggressive, should fleet require additional volume, in order to cost-effectively transport shipments.
- Also, what is the current market-share and how does the business that's in play relate to the company's overall strategy. Are goals in the Shipper's Local, Regional, and National markets being met?
- There can also be initiatives to pursue business in particular industries, based on common time sensitivity requirements (Air versus Ground) or certain density (weights and dimensions). Incentives may be offered to promote growth in these areas.

COMPETITION

The points that were stated in "CONDITIONS" above are valid for the competition, just as it is for the incumbent Carrier. Just as importantly as understanding its market conditions, the Carrier that's involved needs to understand the goals and strategy of its competitors. Service levels are typically quite consistent, so if FedEx or UPS charge more than the other, most Shippers will consider making a switch.

COMPREHENSION

Last, but certainly not least, the Carrier will consider how well the Shipper understands what discounts, rebates, and fee concessions are available to them? Asking for a 10% reduction will seldom provide desirable results. Requesting changes to be made, focusing on discounts at specific weights or zones, as well as reductions on minimums, fees, dim divisors, and in other areas, goes a long way. Having access to and understanding ones data is therefore critical during any discussions about price.

Although some factors are uncontrollable, identifying the factors that are flexible will position one to impact their organization in a positive way. The following are some of the basic things that should be considered, in order to benefit from superior pricing:

- One must be well equipped to understand their agreement with the Carrier. Some questions are: Which service levels are not included? Is a Service Guarantee waiver in place? Will Shipment or Piece rating apply? Do all accounts numbers qualify for the same discounts and fee concessions? Are fee adjustments impacting the business that one expects? Are qualifiers being met?
- Invest time and resources to analyze, negotiate, and monitor your Parcel contracts and spend. Most companies believe that they have good negotiated rates. The large majority have the opportunity to reduce costs significantly, however. Cost reduction means immediate positive impact on the bottom line, as it is much easier to cut costs than to increase profitable revenue. Cross-referencing ones data with the Carrier agreement often leads to many surprises.
- Most agreements suggest terms that last 2 to 3 years. Review shipment patterns quarterly and be prepared to negotiate contracts annually, at minimum. The 30-day out clause positions you to receive appropriate discounts and fees, based on your shipment profile.
- Make the Carrier aware of Service Failures and incorrect charges on their part. 96% to 98% on-time delivery still means that 2% to 4% of your customers are dissatisfied with delivery times, which may impact their decision to use your company in the future.
- Although you may be pleased with your Carrier, be open change. Allow other Carriers to bid on your business and test a selec-

How Do Carriers Establish Shipping Pricing - By Thomas Andersen

tion of shipments. Significant savings may be experienced, as a result, with little or no impact on service levels.

Shippers are positioned for greater savings, should they understand the Carrier, and how the 5 C's influence their decisions when establishing the price. Having proper visibility and knowledge positions one to reduce shipping expenses and maximize the value of each shipment.

***Thomas Andersen, MBA**, is the Director of Pricing for Logica (www.logicacorp.com) Logica, is ranked number 1,866 on the Inc. 5000 list in 2010, and is one of the world's leading logistics consulting firms, specializing in reporting and analytics, audit and recovery, and transportation consulting services for all modes, including Small Parcel, LTL, TL, Air & Ocean Freight. Thomas Andersen can be reached at 800.930.8543 x 726 or at tandersen@logicacorp.com.*

Logica

Solutions. Savings. Service.