



**New Strategies
for Transforming
Transportation Management**

The Challenges

After more than 20 years of declining transportation costs, recent spikes in fuel prices and tightening carrier capacity are combining to drive shipping costs up again. Companies have benefited greatly from this historical decline, but it is no longer a buyer's market.

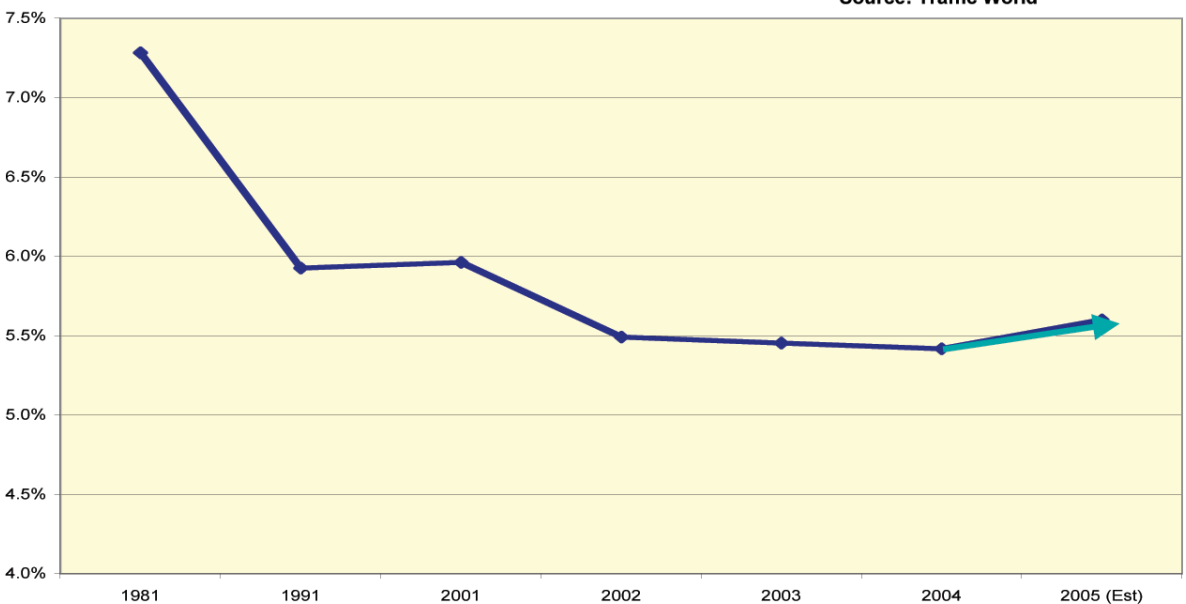
Capacity constraints across most modes of transportation (ocean container shipping being the notable exception) have shifted to favor the carriers, and many shippers are struggling to find any available transportation, regardless of price. For example, railroad customers, especially boxcar users, often find that only half of their daily or weekly car requirements are met. Motor carriers struggle to find enough drivers due to issues with long hours, low pay, and an aging work force.

Government regulations are also impacting transportation costs adversely. New limits on drivers' hours of service are impacting dwell time, facility service hours and utilization of labor and space. EPA diesel fuel and engine standards are driving up operating costs. Additionally, infrastructure projects, such as increasing highway capacity or improving rail lines, remain on planning boards because of local opposition and lack of funding.

Transport Costs are Headed Up, After Years of Decline

Transport Costs as a % of GDP

Source: Traffic World



Source: Traffic World

Outsourcing for transportation services has produced mixed results. In fact, many shippers are reviewing their existing 3PL contracts and wondering why they have not experienced sustainable improvements in service and cost control. The fact is outsourcing can bring additional risks and costs. For example, shippers are legally responsible for freight charges if their outsourced freight bill payer fails to pay and claims for freight loss and damage can be complicated. Unfortunately, these problems can trigger Sarbanes-Oxley issues for publicly traded companies.

As a result of these challenges, companies seek ways to manage their rising transportation costs more diligently, without sacrificing the high levels of service that the marketplace increasingly requires. Hitachi Consulting recommends a three-step approach.

Step 1 - Develop a Transportation Strategy

Since there isn't much that can be done to lower fuel costs or limit regulations, the trick to managing rising transportation costs is to take a higher level view of the entire business function.

For example, while most companies do a good job of minimizing costs for individual locations, they often miss opportunities to optimize service and costs across the entire supply chain network. Today this perspective is not sufficient; it laggardly misses a major opportunity to achieve scale economies and purchasing power with carriers.

Transportation is one of the top ten costs of running the business at many companies. The time has come to give it strategic consideration as a function that can bolster customer satisfaction and create competitive advantage. Leading companies ask questions, such as:

- How can we use our transportation and logistics processes to gain a competitive edge?
- How can we improve our transportation processes to increase customer satisfaction?
- Can we use enabling technology to streamline logistics in order to reduce transportation costs?
- How can we create sustainable barriers to prohibit our competitors from doing the same?

With this more strategic approach, transportation can be transformed from a "sunk cost" to a key differentiator in terms of customer service and in terms of managing relations with suppliers. A well-developed transportation strategy helps to determine the role transportation should play within your company. Just as importantly, it helps support an overall financial strategy to improve shareholder value, because, as we show below, transportation impacts a company's income statement and balance sheet.

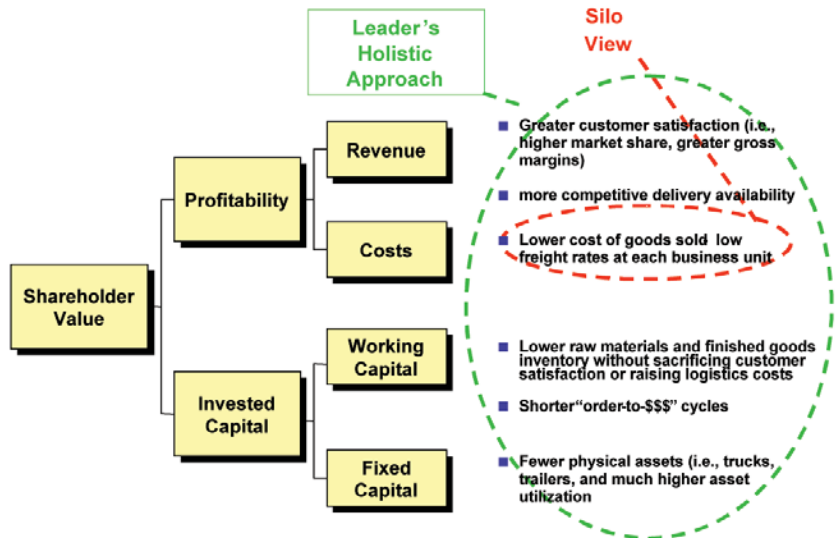
Leaders in Transportation Management Have a More Holistic Perspective on the Potential Impact of Transportation

Silo'd Viewers

- Take the full brunt of rate increases and capacity/performance shortfalls

Leaders

- Take action to avoid these problems and improve overall service and financial performance
- Their approach goes beyond just lower freight rates
- Impact is felt across the enterprise



In other words, leaders act as internal “XPL’s” or even as profit centers...and every transport move has a “buy-side” and a “sell-side.”

Developing a coherent transportation strategy is not the job of shipping clerks or local transportation managers and supervisors. It is a job for senior management, and it needs to be integrated with the overall plan for managing supply and demand.

Step 2 - Create a Roadmap

A roadmap for improvement includes the following tasks:

- Assess the transportation and logistics management processes
- Document systems and processes and compare them to industry best practices
- Develop a roadmap from your current state to your desired state
- Conduct a robust economic analysis to measure the impact of the opportunities that lie ahead
- Develop a business case around transportation management projects

Typically, improvements are a company-specific combination of process improvement, investment in enabling technology, organizational change and the use of Key Performance Indicators (KPIs) to measure progress towards desired improvements. With these in place, companies can expect substantial change in transportation performance, better cost control and higher profits.

Hitachi Consulting uses a proprietary diagnostic tool to measure the current state of a company's transportation management performance. The tool rapidly analyzes

specific functional areas of performance and the types of improvement needed in terms of organization, people, processes and technology. Following the assessment, Hitachi Consulting develops a plan for improvement that includes a roadmap and specific recommendations for improvement in business processes, enabling technology and the use of Key Performance Indicators (KPIs).

Hitachi Consulting’s Transportation Management Diagnostic Tool

Hitachi Consulting’s Distribution Diagnostic Tool evaluates clients’ processes in Logistics, (as well as Warehousing, Global Trade and Event Management) against industry best practices, and identifies the inhibitors to achieving full best practice adoption.

Transportation Diagnostic Tool

| INBOUND LOGISTICS Best Practices | DEGREE OF BEST PRACTICE COMPLIANCE | | | | | BEST PRACTICE ITEM SCORE | INHIBITORS TO ACHIEVING BEST PRACTICE COMPLIANCE | | | |
|---|------------------------------------|----------------|-------------------|-------------------|----------------|--------------------------|--|-------------------------------------|--------------------------|-------------------------------------|
| | Strongly Agree | Somewhat Agree | Somewhat Disagree | Strongly Disagree | Not Sure / N/A | | Technology | Process | Measurement | People |
| For each vendor, terms of sale are reviewed with the purchasing function to determine lowest cost method of delivery. | Somewhat Agree | | | | | 2 | <input type="checkbox"/> | <input checked="" type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| Freight allowances are sought from vendors for inbound transportation | Somewhat Agree | | | | | 2 | <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| Inbound transportation costs are compared to freight terms of sale and are added to cost of goods sold | Strongly Disagree | | | | | 0 | <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> | <input type="checkbox"/> | <input checked="" type="checkbox"/> |
| Inbound freight allowances are constantly monitored to ensure that at a minimum, freight charges are adequately covered | Strongly Disagree | | | | | 0 | <input checked="" type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| Optimizer interacts with Demand Management System, Raw Material Procurement, Inbound Logistics, Manufacturing and Production Planning | Strongly Disagree | | | | | 0 | <input checked="" type="checkbox"/> | <input checked="" type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| Freight exchange is used as carrier and trading partner resource in a highly collaborative environment | Not Sure / N/A | | | | | 0 | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

During the assessment, address the following questions:

- How can we develop an enterprise-wide transportation solution that results in better service to customers and lower supply chain costs?
- How can we take maximum advantage of scale economies across the entire company?
- How can we select and contract with carriers to get the best balance of service reliability and low cost for each traffic lane?
- Are we tracking shipment volumes and seasonality swings to use in rate negotiations and carrier management across the year?
- How can we control inbound shipments and reduce costs, even when the vendor has historically controlled the freight?
- How can the transportation management function consistently choose the best mode and carrier in terms of cost and service reliability, so as to minimize capacity constraints?
- How can we use Internet-based technology to get early notice of events and unexpected costs in the supply chain so we can manage exceptional activity pro-actively?
- How do we handle unplanned shipments or last minute capacity issues?

Step 3 - Management Supporting Systems

Companies that spend more than \$25 million on freight can often benefit from systems designed to specifically support transportation and event management processes. These systems can usually be implemented in four to six months and typically provide payback within 12-18 months.

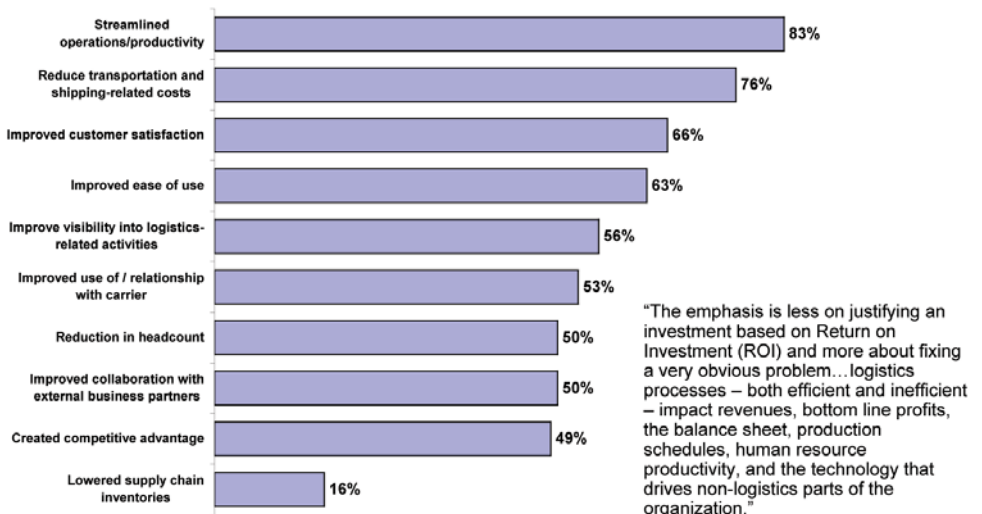
Adopters of transportation management systems report better on-time performance, substantially reduced enterprise-wide transportation costs, and higher gross margins.

Transportation Management Opportunity

Survey: TMS Benefits

What business benefits have you achieved through the use of Transportation Management Software?

% of Responses



Source: AMR, 2006

The selection of an appropriate vendor is key. We recommend identifying your unique requirements for transportation and event management and then developing requirements "scripts" using your own terminology. Require vendors to follow these "scripts" when responding to your request for proposals. This will help you understand the product on your own terms and force vendors away from canned demonstrations, which are often irrelevant.

Conclusion

Although there is a great amount of change taking place across the transportation industry, new thinking and technology solutions can help companies achieve greater savings, improvements in inventory management and customer service, as well as higher overall margins, revenues and profits.

With a complete transportation management solution that covers inbound and outbound shipment planning and optimization, quoting, tendering and booking, carrier management, cost allocation and freight payment, companies can:

- Reduce transportation costs by 15 percent
- Achieve more efficient truck loads
- Gain better equipment utilization through continuous moves and backhaul opportunities
- Improve carrier and rate management
- Improve warehouse labor productivity
- Increase overall visibility into inventory across the extended supply chain

Companies that achieve these gains also find that they measurably improve their "Perfect Order Rate" (defined as on-time per customer requirement, correct quality and quantity and shipped and invoiced to meet each customer's needs). Research shows (see previous AMR 2006 graphic) that a three percent improvement in the "Perfect Order Rate" results in a one percent gain in gross profit margins. Such improvements in profits deliver a better bottom line and an increase in shareholder value.

Companies with large and increasing investments in transportation must assess their Transportation Performance at strategic, tactical and transactional levels, identifying and validating improvement opportunities that best fit their company's needs for both short term capabilities and long term expectations. In addition, they should define the gap between current state and future state, and develop the business case to close the gap.

About Hitachi Consulting

As Hitachi, Ltd.'s (NYSE: HIT/TSE: 6501) global consulting company, Hitachi Consulting is a recognized leader in delivering proven business and IT solutions to Global 2000 companies across many industries. We leverage decades of business process, vertical industry, and leading-edge technology experience to understand each company's unique business needs. From business strategy development through application deployment, our consultants are committed to helping clients quickly realize measurable business value and achieve sustainable ROI.

With offices in the U.S., Japan and Europe, Hitachi Consulting's client base includes nearly 35 percent of the Fortune 100, 25 percent of the Global 100, as well as many leading mid-market companies. We offer a client-focused, collaborative approach, which integrates strategy, people, process and technology, and we transfer knowledge throughout each engagement. For more information, call 877.664.0010 or visit www.hitachiconsulting.com.

Hitachi Consulting – Inspiring your next success!®

About Hitachi

Hitachi, Ltd. (NYSE: HIT), headquartered in Tokyo, Japan, is a leading global electronics company, with approximately 356,000 employees worldwide. Fiscal 2005 (ended March 31, 2006) consolidated sales totaled 9,464 billion yen (\$80.9 billion). The company offers a wide range of systems, products and services in market sectors including information systems, electronic devices, power and industrial systems, consumer products, materials and financial services. For more information on Hitachi, please visit the company's Web site at <http://www.hitachi.com>.

