

THIRD PARTY LOGISTICS IN DISTRIBUTION EFFICIENCY DELIVERY FOR COMPETITIVE ADVANTAGE IN FAST MOVING CONSUMER GOODS COMPANIES IN KENYA

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ABSTRACT

The authors aim was to undertake a comparative study on how using third party logistics can deliver distribution efficiency and its contribution to competitive advantage for organizations. The study adopted a descriptive research design with a sampling frame of 50 companies operating in Kenya. Primary data collection method was used through mail questionnaire. Data was analyzed using Statistical Package for Social Sciences (SPSS) package version 14. The article addresses key issues related to third party logistics, why organizations decide to outsource, advantages and disadvantages of third party logistics, their impact on distribution efficiency in the Fast Moving Consumer Goods Companies in Kenya. Results based on the analysis of data relating to 50 Companies in Kenya showed that the use of third party model is effective in enhancing delivery of products to the customers premise. Moreover, organizations have a high chance of minimizing costs while maximizing their revenue from the use of third party logistics. Further, Third Party Logistics has the potential of improving customer performance in meeting consumer needs. The scope of the study was limited as it only focused on a small data set of 50 Kenyan FMCG companies. The generalization of results to other non-FMCG companies or even to all African countries ignoring potential organizational/regional differences arose as the two limitations of the study. In a time when companies are outsourcing noncore competencies, the study recommends that organizations recognize the potential contribution of 3PL firms and take advantage of opportunities to address organizational needs. It is evident from the findings of this study, Companies should be aware that 3PLs provide an opportunity for an increased competitive advantage. Through their unique position and evolving capabilities, 3PLs can be seen as strategic players in a supply chain management as opposed to mere vendors of a given organization.

Key Words: *third party logistics, outsourcing, supply chain management, FMCG, customer, consumer, Kenya*

Introduction

The use of Third party logistics (3PL) is a growing phenomenon all over the world. In Kenya, the importance continues to grow with Fast Moving Consumer Goods Companies opting for this mode to deliver their products across the country and beyond. This article intends to provide a 3PL perspective within FMCG companies in Kenya. It concentrates on three key issues: (1) evaluate how using third party logistics can deliver distribution efficiency and achieve competitive advantages within FMCG companies in Kenya, (2) the reasons that drive organizations to outsource 3PL and, (3) the advantages and disadvantages of using 3PL and its impact on business performance. The findings of this indicate that most FMCG corporations are content with the services provided by 3PL provider. The performance of the 3PL has brought about competitive advantage for the corporations. From the findings of this paper, 3PL usage may be adopted across many other organizations and in Africa as a whole in the very foreseeable future.

The concept of “*Logistics*” started many years before Christ and was used by Greek generals (Leon the Wise, Alexander the Great) in order to describe all the procedures for the army’s procurement on food, clothing, ammunition, etc. Alexander the Great was a big fan of the mobility of his troops and he didn’t want his troops to stay in one place waiting for supplies from Macedonia. Thus, he tried to resolve the issues of supplies by using supplies from the local resources of his defeated enemies. World War II was the major motivation of logistics to increase recognition and emphasis, following the clear importance of their contribution toward the Allied victory. Starting from the early 1960s, many factors, such as deregulation, competitive pressures, information technology, globalization, profit leverage, etc., contributed to the increase of logistics science in the form we know it today (Couriel, 2013).

Starting in the 1980s, firms viewed time as a source of competitive advantage, based upon the observation that firms competing effectively on time tend to excel at improving quality, understanding evolving customer needs, exploiting emerging markets, entering new businesses, and generating new ideas and incorporating them into innovations. Thus, firms started to focus on eliminating waste in the form of time, effort, defective units, and inventory in manufacturing-distribution systems. In fierce time and quality-based competition, logistics capabilities become critical. In fact, many firms – particularly those operating in commodity or convenience goods markets – succeed as a result of their logistics systems, rather than their marketing strategies (Christopher, 2002; Bowersox et al., 2000; Mentzer and Williams, 2001).

Early logistics literature focused on the economic theories of the firm – that is, cost control and its contribution to the bottom line. Thus, total cost analysis was an important performance measure (Stock and Lambert, 2001). The role of logistics during this period is reflected in Drucker’s (1962) statement that logistics was one of the last real frontiers of opportunity for organizations to improve their corporate efficiency. The goal of logistics was, thus, to optimize the number, size, and geographical arrangement of plant and warehouse facilities, select transportation methods, and control distribution costs. Consequently, logistics has done an

excellent job of managing and moving inventory – the operational aspects of logistics (Mentzer et al., 1999).

Logistics excellence has become a powerful source of competitive differentiation (Mentzer et al., 2001). In the 1980s and 1990s, companies began to view logistics as more than simply a source of cost savings and recognize it as a source of enhancing product or service offerings as part of the broader supply chain process to create competitive advantage (Novack et al., 2001; McDuffie et al., 2001). Despite the growing importance of logistics in corporate strategy and the global economy, the logistics discipline does not have as rich a heritage of theory development and empirical research as older and more established disciplines such as anthropology, philosophy, psychology, and sociology (Stock, 1997). Notably, much logistics literature and research has been considered largely managerial in nature and lacking a rigorous orientation toward theory development, testing, and application. Specifically, logistics researchers have made little effort to build a unified theory of logistics (that is, a theory of the role of logistics in the firm). Although there have been attempts to build logistics theories (for example, Bienstock et al., 1998; Cooper et al., 1997), they are limited to particular components of logistics (for example; customer service and logistics quality). In addition, it is not clear how any particular theory is related to the foundation of the logistics discipline to understand the strategic nature of logistics.

The purpose of this study was to evaluate how using third party logistics can deliver distribution efficiency and achieve competitive advantage while building value for Fast moving Consumer Goods companies in Kenya, its business partners and consumers.

Towards a 3PL Distribution Efficiency Delivery

According to Council of Logistics Management (2003), logistics, is the process of planning, implementing, controlling the efficient and effective flow, storage of goods, services and related information from the point of origin to the point of consumption for the purpose of conforming to customer's requirements. Logistics management tries to have the “*right product*”, in the “*right quantity*”, at the “*right place*”, at the “*right time*”, with the “*right cost*”. Logistics management must balance two basic objectives: Quality of Service and Low Cost. Hanfield and Nichols (1999) defined Supply Chain Management as the integration of the above activities, through improved supply chain relationships, to achieve a sustainable competitive advantage. According to Ballou (2004), the logistics activities can be classified into a) core and b) supporting. The core activities take place in every supply channel and include: (1) Customer service (typically defined by marketing); (2) Transportation; (3) Inventory management and (4) Information flows and order processing. Support activities vary from company to company. A comprehensive list includes: **Warehousing** (Space determination, stock layout, configuration, stock placement); **Materials handling** (equipment selection & replacement policies, order-picking procedures, stock storage & retrieval); **Purchasing** (supply source selection, purchase timing, purchase quantities); **Protective packaging** (designed for handling, storage, protection from loss/damage); **Cooperate with production/operations** (specify aggregate quantities, sequence & time

production output, schedule supplies); and *Information maintenance* (information collection, storage & manipulation, data analysis, control procedures).

Ballou (2004) also notes that logistics in an organization are considered as a continuation of marketing. Logistics play a critical role in each of the three critical elements of the marketing concept (customer satisfaction i.e. suppliers and immediate customers, integrated effort/systems approach i.e. Product, Price, Promotion, Place (distribution) and corporate profit i.e. maximization of the long-term profitability, lowest costs given an acceptable level of customer service).

The Problem Statement

The heightened competitive pressure of today's global business environment has forced companies to focus on their core competencies and increasingly outsource business tasks perceived as noncore. Today, in an era of shrinking product life cycles, proliferation of product lines, shifting distribution chains and rapidly changing technological advancement, mastery of logistics has become an essential ingredient for organizations in gaining competitive advantage. Given the day-to-day pressures on functional managers to meet performance goals, it is impossible to manage logistics effectively unless its integrative nature is seriously considered. Because inefficiencies drive inventories and logistics costs higher than necessary, the most obvious route to better logistics performance is cost reduction. Disposing off dead stocks, policing minimum order-size rules and cutting warehouse costs, for instance, can enhance efficiency. Distributors and retailers are increasingly alert to the effects of reliable deliveries in reducing their costs and in enabling them to give their customers more responsive service.

Most researchers has written about the reason and benefits of third party logistics (Langley & Sink,1997, Bhatnagar, Sohal & Millen, 1999), classification of different third party providers (Hertz and Alfredsson, 2002, Virum, 1993, Bagchi and Virum, 1998), the use and development of third party logistics by firms in European countries (Lieb and Randall, 1996, Sohal, Millen & Moss, 2002 respectively). Little has been written about the third party logistics providers in Africa and more specifically there is very little research done on third party logistics providers in Kenya. Armstrong and Associates (2012) estimate that the global 3PL gross revenue in 2011 at \$133.8 billion in 2011 was up 5.2 percent over 2010, Annual growth for the third-party logistics (3PL) market in 2013 is expected to be north of 6 percent, with much of current market activity centered around mergers and acquisitions, with many of the same underlying market fundamentals of 2012 still intact.

With this prediction in mind, the study focuses on, how can third party logistics provide distribution efficiency and in turn competitive advantage for FMCG Companies in Kenya? What advantages and/or disadvantages does the third party logistics provide? And the reasons that drive organizations to logistics outsourcing? These are the questions that the authors will address.

Third Party Logistics

Murphy and Poist (2000), notes that terms such as “logistics outsourcing” “logistics alliances” “third party logistics” contract logistics” and “contract distribution” have been used interchangeably to describe the organizational practice of contracting-out part of or all logistics activities that were previously performed in-house. Different definitions tend to emphasize different aspects of outsourcing arrangements such as the service offering, nature and duration of relationships, performance outcomes, and extent of third party responsibility over the logistics process and position/role in the supply chain. Third Party Logistics (3PL) is usually associated with the offering of multiple, bundled services, rather than just isolated transport or warehousing functions (Leahy et al., 2001). Contemporary 3PL arrangements are based on formal (both short- and long-term) contractual relations as opposed to spot purchases of logistics services.

Outsourcing logistics functions to other firms has increasingly become a powerful alternative to the traditional, vertically integrated firm. 3PL arrangements are more than simply contracting out cost-inefficient functions (Skjoett-Larsen, 1999). Gentry and Vellenga (1996) argue it is highly unlikely that any one firm to maximize customer value will perform all of the primary activities in a supply chain – inbound and outbound logistics, operations, marketing, sales and service. Changing customer demands and regulatory frameworks encourage firms to outsource logistics functions to gain flexibility to quickly adjust to the market. The scope of 3PL arrangements encompasses a variety of options ranging from narrow (limited to specific activities like transportation) to broad (covering substantive activities in the entire supply chain) (Sink and Langley, 2003). The primary reasons for outsourcing logistics functions are to save costs and enhance revenues (Boyson et al., 1999; Bowersox, 1999).

Literature Review

Reasons to Outsource 3PL

The decision to outsource (or not) logistics activities depends on a multitude of variables, which refer to both internal and external considerations. Rao and Young (2003) have identified factors such as centrality of the logistics function, risk and control, cost/service trade-offs, information technologies and relationships with Logistics Service Providers (LSP's). The concept of logistics complexity is also introduced to incorporate a number of critical drivers that impact on the above-identified factors. Product-related (for instance, special handling needs), process-related (example of cycle times) and network-related (example of countries served) drivers are believed to have an indirect influence in the outsourcing decision (Rao and Young, 2003).

The decision to contract-out logistics can also be driven by resource and capability considerations (Bolumole, 2001). Forming relationships with 3PL providers is an efficient and effective means of achieving the required service without investing heavily in assets and new capabilities (Persson and Virum, 2001; Stank and Maltz, 2000). In this way, shippers can focus on their core business. Furthermore, changes in the business environment, increased competition, pressure for cost reduction and the resulting need to restructure supply chains are often quoted as motives for the formation of alliances with LSP's. Whatever the rationale for contract logistics, it

is noted that the outsourcing decision should be examined in the context of corporate and logistics strategy at specific time periods (Ferne, 2000).

Merits and Demerits of 3PL

A variety of benefits and risks in relation to 3PL has been reported. These can be classified as strategy, finance and operations related. Outsourcing non-strategic activities enables organizations to focus on core competence and exploit external logistical expertise (Sink and Langley, 2000). 3PL providers can also contribute to improved customer satisfaction and provide access to international distribution networks (Bask, 2001).

The most often-cited risks are associated with loss of control over the logistics function and loss of in-house capability and customer contact notes Ellram and Cooper, (2001). However, it is usually the case that shippers employ a mixed strategy regarding logistics and retains important logistics activities (for instance, order management) in-house (Wilding and Juriado, 2004). While it is reported that users of 3PL enhance their flexibility with regard to market (investments) and demand (volume flexibility) changes, lack of responsiveness to customer needs is also cited as a problem of outsourcing (van Damme, 2002).

Logistics outsourcing offers many cost-related advantages such as reduction in asset investment (turning fixed cost into variable), labor and equipment maintenance costs. LSPs serve multiple customers and are able to utilize capacity better and spread logistics costs, thus achieving economies of scale (van Damme, 2002). However, cost reduction is not always realized due to unrealistic fee structures proposed by service providers (Ackerman, 2007); and even if realized, it can be offset by the provider's margin (Wilding and Juriado, 2004). Cost savings evaluation can be difficult due to the shipper's lack of awareness of internal logistics costs. Indeed, the outsourcing option may be chosen in order to give an indication of in-house costs and serve as an external benchmark for logistics efficiency (van Laarhoven et al., 2000).

Regarding operational advantages and problems of 3PL, evidence is contrasting. Reported benefits include reduction in inventory levels, order cycle times, lead times and improvement in customer service (Bhatnagar and Viswanathan, 2000; Daugherty et al., 1996; Wong et al., 2000). However, other authors cite problems with respect to service performance, disruption to inbound flows, inadequate provider expertise, inadequate employee quality, sustained time and effort spent on logistics, loss of customer feedback and inability of 3PL providers to deal with special product needs and emergency circumstances (Ellram and Cooper, 1990; Gibson and Cook, 2001; Sink and Langley, 2000; Svensson, 2001; van Laarhoven et al., 2000). Despite gaining access to logistics information systems (Rao et al., 2002), shippers appear to be dissatisfied with service provider's IT capabilities and prefer to rely on in-house systems instead (van Laarhoven et al., 2000).

There have been many studies so far investigating success factors for 3PL partnerships (Lambert et al., 1999; Murphy and Poist, 2000; van Laarhoven et al., 2000). Some factors, which appear to be common to those presented in the wider inter-firm partnership and strategic alliances literature include: common goals and compatible interests; compatibility of information systems;

compatibility of organizational culture and routines; customer orientation; expert knowledge in specific markets/products/processes; financial stability of service provider; frequent communications and information exchange; joint investment for achieving relationship objectives; joint planning, management and control of 3PL relationship; mechanisms for dispute resolution; power balance between contracting parties; provider ability to stay updated with respect to new technologies; risk and reward sharing; service level improvement/reduction of distribution costs; service provider flexibility and responsiveness; top management support; and understanding client's supply chain needs.

Therefore, creating customer value is possible by focusing on logistics customer service beyond the efficiency function; logistics capabilities are a source of competitive advantage (Zhao et al., 2001; Lynch et al., 2000; Bowersox et al., 1999). Superior skills are the distinctive capabilities of personnel that set them apart from the personnel of competing firms, and superior resources as more tangible requirements for advantage (for instance, physical facilities, wide distribution channels, and brand name) that enable a firm to exercise its capabilities. Superior skills and resources, taken together, represent the ability of a firm to surpass its competitors in the marketplace. Customer value consists of economic values such as profitability, and lowest total cost and market value including assortment and convenience, both of which satisfy customer's current and future requirements. Logistics capabilities, thus, contribute to a firm's competitiveness through creating economic (Cost leadership) and market-based (differentiation) values (Bowersox et. al., 2000).

Traditionally, companies selected from a defined, limited set of options (that is; direct sales, manufacturers' representatives, distributors, dealers) and most firms in an industry made similar choices. Recently, the number of options has expanded greatly and the breadth of choices by competitors has proliferated in parallel, creating potential instability in competitive positions for current leaders and areas of opportunity for others. To make matters more uncertain, some of the traditional options no longer offer the same balance of services and costs and now cease to achieve the desired results. Therefore, many companies are forced to rethink their approaches to distribution. The fundamental purpose of an optimal distribution network as asserted by Ghines (2003) is to aggressively achieve market penetration at the lowest possible cost in the shortest time frame possible in the product's life cycle.

All the authors above have given their views on 3PL; whereas every good thing must have another side; they seem unanimous about 3PL enhancing distribution efficiency while ensuring that an organization achieves cost leadership and differentiation. Thus, selecting a distribution approach is a key element of a successful business model. The overall process of delivering products to customers, at once encompasses both a company's connection to its customers and a significant portion of its total costs.

Research Methodology

The study adopted a descriptive research design. There are over 60 FMCG Companies in Kenya. The authors divided the country into the three regions, that is, Nairobi, Western and Mountain

regions. The FMCG Companies were further grouped into three. The three groups were in terms of Units of production that is; 24,999 and below, 25,000 units to 59,999 and 60,000 units and above. This study had a sampling frame of 50 companies countrywide selected from the list of all registered organizations in Kenya. The sample size was selected using non-random sampling technique and specifically purposive sampling. This sampling technique deliberately targets a certain criterion of the population. The sampling frame enabled the authors to have fruitful relationships with respondents and enhanced theoretical examination to address the research problem in depth. Selection of the 50 Companies out of the over 60 FMCG's in Kenya was arrived at in regards to the units sold by the companies selected. The sample frame also enabled the authors close association with the respondents, and enhanced the validity of in-depth inquest in realistic scenarios.

The target population included all firms with significant logistics use and thus the authors considered the criteria for selection to be sales of over 60,000 units and sales not below 25,000 units on a monthly basis. The 50 selected companies were then contacted on phone to get contact of the Operations Director. Primary data collection method was used in this study and data was collected using a questionnaire that had been developed by the researcher based on the research objectives. Data collection was done through administering a mail questionnaire survey which was sent out with a cover letter explaining the need for the study. The response rate for the study was 80% with 40 out of the 50 mail questionnaires sent out received back. This was a high and acceptable rate to proceed to analysis stage as well as use the results as conclusive and generalizable to the entire population. Data was analyzed using Statistical Package for Social Sciences (SPSS) program version 14.

Research Findings

The study found out that the use of third party model is effective in enhancing delivery of products to the customers premise. In addition, planned orders from third party enable the customer fulfill their forecasted demand and thus effectively serve the markets of their jurisdiction without any out of stock situations. Moreover, organizations have a high chance of minimizing costs done by reduction of fixed costs through assets and the costs of labor and equipment maintenance costs while maximizing their revenue from the use of third party logistics. Further, Third Party Logistics has the potential of improving customer performance in meeting consumer needs, exploiting market opportunities and being innovative, this is achieved from the time saved by use of Third Party Logistics, the customer is fully focused in improving quality of service to the consumers, understanding evolving consumer needs, exploiting emerging markets and generating new ideas and incorporating them into innovations that grow the organization. However, a number of customer respondents disagreed that they were not able to easily get in touch with third party logistics and this has the potential of negatively affecting third party effectiveness. Another issue that arose was on the improvement of timely communication between FMCG company and the third party logistics to enhance efficiency in distribution to the companies they serve.

Conclusions

The highly competitive environment has businesses now concentrating on their core activities and divesting activities to experts in those fields. Traditional logistics management activities, such as transportation, warehousing, order processing, and related information technology support, are deemed as noncore functions for many firms. In addition, logistics activities have significant asset requirements and offer the potential for large cost savings, making it a primary candidate for outsourcing. The key to successful outsourcing of logistics services lies in finding a 3PL provider that has the most strategic fit with the company's goals. The purpose of using third party logistics cannot be considered as cost reduction alone, but a mixture of service improvement and efficient operation. From the findings, it was noted that Companies have successfully used 3PL providers to handle their logistics needs. Although the future of the 3PL industry is somewhat uncertain, it can be assured that the increasing global demand and technological capabilities will lead to further integration between 3PL providers and companies alike.

Recommendations

Competency in logistics has often been seen as a source of sustainable competitive advantage that firms can accumulate over time. The actions of organizations to reorganize their operations to outsource more activities to 3PL and remain competitive cannot be explained by merely minimizing transaction costs. Additionally, the ability of organizations to focus on their core competencies and engage outside firms to carry out other organizational operations is driving organizations closer to gaining competitive advantage. Furthermore, all logistics functions can be outsourced, permitting the firm to have access to a full range of resources it does not own.

In a time when companies are outsourcing noncore competencies, this study recommends that organizations recognize the potential contribution of 3PL firms and take advantage of opportunities to address organizational needs. It is evident from the findings of this study, Companies should be aware that 3PLs provide an opportunity for an increased competitive advantage. Through their unique position and evolving capabilities, 3PLs can be seen as strategic players in a supply chain as opposed to mere vendors of a given organization.

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