

# LTL-Parcel Competition Puts Pressure on LTL Pricing

By Satish Jindel

## OPINION

In the early 1980s, the less-than-truckload segment of the trucking industry had little concern about competition from the parcel carriers like United Parcel Service and Federal Express. And of course, RPS was not a factor at all, as it did not even come into existence until March 1985.

Now, the long- and short-haul LTL carriers find themselves losing market share to these competitors. This market shift is quite apparent and well understood. The implications for LTL trucking are profound, particularly with respect to that industry's traditional pricing methods.

According to 1983 and 1993 estimates published by Alex. Brown & Sons, LTL market share of non-local trucking dropped from 10% to 7.3% while the parcel carriers market share increased from 3.9% to 8.2%. In terms of revenue, the total LTL industry went from \$14.3 billion to \$17 billion while the parcel industry increased more dramatically from \$5.6 billion to \$19 billion.

Many LTL carriers are reporting a drop in tonnage per shipment and revenue per shipment. While some economists believe this will reverse with improvement in the economy, other factors will keep the trend going:

- Growing emphasis on just-in-time and quick response inventory and distribution management systems, which results in smaller, more frequent shipments.
- Tracking and tracing capability has become essential for the success of the JIT and QR initiatives.

The minimum charge pricing approach of the LTL industry has opened the door for parcel carriers to capture this niche with attractive pricing, improved delivery options and better information systems.

Technology-driven changes in product design will shift more parcels from being profitable to marginal

LTL shipments — but they still will be profitable for parcel carriers.

The classification system used by the LTL industry was established to incorporate the impact of various characteristics of products on the operation cost for the carriers. Technological changes, new products and rapid change in products have made

- Introduction of Hundredweight and Multiweight products by UPS and RPS, respectively, aimed at minimum charge shipments previously handled by LTL carriers.

- Parcel carriers are increasing weight and size limitations. In the early 1980s, UPS' limits were 70 pounds and 108 inches in combined length and girth. RPS entered the market with limits of 100 pounds and 130 inches. RPS later increased the weight limit to 150 pounds in recognition of the fact that it could handle these heavier parcels more efficiently than its sister LTL companies. During this period, UPS also raised its limits to RPS' to capture a share of the \$6 billion applicable LTL market.

- Freight is getting lighter and more compact thanks to use of lighter materials — aluminum, fiberglass, and graphite instead of iron and steel — and miniaturization. For example, the weight of televisions, video cassette recorders, and desktop computers has been reduced by several pounds in the past few years.

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- New technology has made certain products obsolete: Compact discs have replaced larger and heavier LPs, for example.

- The shift in distribution patterns from long haul to regional has compressed transit time for order fulfillment. The growth in time-definite and next-day delivery service is driven by technological developments in the telecommunication industry, which have increased the speed of business activity.

it impractical to keep the classification system current.

The problem is further compounded by the growing willingness by many LTL carriers to discard the product classification system in negotiating the freight charges. Too many shipments are priced on FAK (freight all kinds) basis, further hurting the classification process, which depends on such data base.

The increased emphasis on JIT and

QR, driven by the faster pace of business communication, has pushed LTL carriers into making significant improvements in transit time.

However, these service improvements have not produced any enhancement of freight charges, due to the current pricing approach that has remained largely unchanged for several years and does not recognize the new market environment.

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## Pricing

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These developments will continue to shift heavier LTL shipments into lighter and minimum charge shipments. Since the parcel carriers have a lower cost structure for handling these shipments, the LTL carriers will either have to accept further market share loss to parcel carriers, or undertake a major restructuring of the business that integrates the technological developments in the shippers' industries into their own operational and pricing approach.

The current LTL industry's operating structure involves significantly higher cost for pickup and delivery of such smaller shipments in comparison to the parcel carriers.

Similarly, the current LTL pricing approach based on distance, weight and product-based classification may not be suited to the changing needs of this technology-driven economy.

It is true that the products influenced by such technological developments represent a portion of all shipments handled by the LTL industry. However, these shipments are generally of higher value and thus more service sensitive and less price sensitive. Hence, they can support higher prices if accompanied with savings in the total supply chain management process.

This influence of technology on high value products contained in LTL shipments will further benefit the parcel carriers that have targeted the more service sensitive segment of the LTL market.

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