Logistics

In Chapters 2 through 6, we explored how different CEO strategic mindsets contributed to the success or failure of companies competing in industries that provide products to consumers. For each of these industries, the companies we explored made decisions about which business functions to perform themselves and which functions to outsource to partners. For example, during its early years when it sold books online, Amazon built its own website so customers could place orders online. It relied on partners, such as Ingram, a leading book wholesaler, to fulfill those orders. As the company expanded its product line and dramatically increased its order volume, those fulfillment partners could not meet Amazon's service quality standards – particularly during peak periods of demand. Amazon responded by building its own fulfillment network – consisting of warehouses, trucks, airplanes, and the people and systems needed to operate them. Amazon's decision to backward integrate into logistics has put pressure on its fulfillment partners and changed the structure of the logistics industry. While it began by operating with a few physical assets, the ecommerce industry's ability to fulfill demanding service standards – for example, shipping the right products quickly without breaking them – depends on building an asset-heavy logistics network. Simply put, logistics has become an essential part of ecommerce. That fundamental shift has implications for ecommerce companies, store-based retailers, and the logistics industry. Lessons for leaders include

- **Set customer service quality standards:** It is far more profitable to win new customers and keep them buying than to lure in customers who are disappointed with their initial encounter and decide never to buy again. A customer won't come back if their first order arrives shattered into pieces two weeks later than expected.
On the other hand, if the order arrives intact by the expected time, the customer is likely to buy again — especially if the company already offers the best selection of products at a competitive price. To achieve the benefits of creating and keeping customers over a long period of time, the first step is to set specific, measurable standards for service quality that are higher than competitors’.

- **Assess whether operations can satisfy service standards:** Once a company sets service standards, it must monitor whether its operations are meeting them. For example, a company could set a standard that all orders must be delivered with the products the customer requested, undamaged, within 48 hours. If the company consistently achieves a 100% score for these metrics on its orders, then its operations can satisfy the service standards. If not, the company must investigate the reasons why.

- **Partner or build so your operations can meet your service standards:** If a company is falling short of its service standards, it must conduct a rigorous, methodical analysis of its operations to find the root cause of the service quality problems. Based on that analysis, the company should consider options for fixing those problem causing factors. For example, if the root cause of service delivery problems is found to be with a company’s partners, a company should investigate whether it can solve the problem cost-effectively by building its own logistics network.

- **Develop a CEO successor with the right mindset:** The logistics industry has many traditions — most notably, some logistics providers employ unionized workers. Such logistics providers suffer margin compression should they seek to match the prices of rivals with lower labor costs. Given the rising competitive pressure from ecommerce providers such as Amazon, logistics providers must be prepared to rethink and reengineer their strategies and operations to remain competitive with ecommerce providers that backwards integrate. To that end, the boards of logistics providers ought to be developing CEO candidates with Create the Future or Fast Follower mindsets so that the company is likely to adapt effectively to a rapidly changing future.
These implications emerge from examining logistics – an extremely complex industry based on a simple idea: to deliver goods from their source to their destination quickly and safely. What makes logistics particularly complicated is that this journey can involve many handoffs among different modes of transportation – including ships, airplanes, trains, trucks, and vans – provided by many companies including well-known names such as Maersk, FedEx, and UPS. In this chapter, we will focus on third-party logistics (3PL) – which sorts through all this complexity on behalf of companies. More specifically, 3PLs find the most efficient way to ship goods by providing companies with outsourced warehousing, forwarding, packing, consulting, order fulfillment, brokerage, and transportation documentation. The 3PL industry is a large, steadily expanding, somewhat profitable industry which serves an essential role in most of the industries we have explored in Chapters 2 through 6 of this book. While it is relatively easy to order physical goods electronically, the ability to fulfill orders quickly and reliably is an essential capability for companies seeking to win over new customers and keep them buying. Compared to companies that own and operate asset-intensive services such as trucking, railroad, airfreight, and shipping, 3PL operators are more flexible and less capital intensive – generally with better control over their labor costs.

A more detailed analysis of the 3PL industry reveals that its profit potential is high enough to attract new competitors who can hurdle the industry’s relatively low entry barriers. What is more, one of the most vital choices made by 3PL executives is which customers their companies should serve. If they work mostly with fast-growing ecommerce companies, demand for their services is likely to be solid. However, if they depend too heavily on companies that sell through physical stores, revenue growth could be endangered. The 3PL industry grew a 3% average annual rate between 2014 and 2019 to $194.2 billion earning an average net profit margin of 7.4% in 2019. Barriers to entry into the industry were moderate – with a relatively low level of capital intensity (in 2019, a mere 11 cents in capital was invested for every dollar spent on labor). The 3PL market attracted new entrants – with the number of 3PL providers growing at a 3.2% annual rate in the five years ending in 2019. 3PL providers gained a considerable share of increased freight volumes – for example, by 2019 about 53% of total logistics expenditure was directed toward 3PLs – up from 50% in 2017. The reason for the shift is clear: 3PLs were more adept than retail and other in-house transportation operations at keeping up with the growing complexity of the global supply chain and the latest technologies. Moreover, the growing popularity of ecommerce – up at a 13.7% five-year annual rate through 2019 – boosted 3PL demand. Ecommerce’s growth increased the volume and frequency of small packages. Moreover, online retailers’ desire to expand their logistics and other physical centers made them more likely to outsource...
to 3PLs. By 2024, forecasters expected the 3PL industry to keep growing – at a 3.6% average annual rate to $232.1 billion – and to generate slightly higher average profit margins of 7.6%. Although new companies were expected to enter the market, mergers and acquisitions were forecast to continue to enable companies to expand globally to satisfy demand from multinational corporate clients, while smaller 3PLs focused on niche markets and offered more in-depth services.¹

Winners in the logistics industry excelled at four interrelated skills: to control quality, to deploy the latest and most effective technology, to locate operations near customers, and to maintain a good reputation -- which flowed from doing the other three things well. Since 3PLs delivered packages that are valuable and/or time sensitive, the most successful companies operated control systems that kept deliveries from being lost or delayed. Good-quality control depended in part on the ability to deploy technology that boosted productivity and reliability. Broader technological trends were expected to create opportunities for 3PLs that could adopt them to boost efficiency and reliability. For example, technologies that enabled ride sharing could be deployed to match carriers and shippers more effectively. Online ordering systems were essential to matching 3PLs with customers. RFID and two-dimensional bar code technology could boost efficiency by tracking the movement of packages wirelessly. “Snowflake” magnetic ink imprints could allow 3PLs to track and view assets virtually. Finally, 3PLs could use robots to handle, locate, and store packages more efficiently.²

In response to the Covid-19 pandemic, in 2020 countries around the world shut down their borders, limited transportation and travel, and thereby put the brakes on the global transportation and logistics industry. These responses hampered important supply chains – with varying effects depending on the mode of transportation, air, freight, and sea – and the country. By June 2020, the gross value added of the global logistics industry had declined 6.1%, while the decline in country logistics markets varied widely – with China reporting a 0.9% decline and Italy suffering an 18.1% decline. North America’s sea forwarding market was expected to decline 12.1% in 2020, while the freight forwarding market was forecast to fall 9.5%. Air freight volume was hurt the most – declining 19% in the year ending March 2020. By June 2020, considerable uncertainty prevailed about whether the response to Covid-19 would continue to reduce demand for 3PLs or represent a temporary interruption in this longer-term growth path.³ One 3PL provider, XPO (profiled later in this chapter), suffered a 6% decline in revenue in the first quarter of 2020 and suspended its forecast for the rest of the year in mid-March 2020 as demand rapidly deteriorated around the time that Covid-19 was deemed a pandemic.⁴
Strategic Mindsets of Logistics Industry Winners and Losers

The 3PL industry was large and profitable — yet not all participants were likely to survive. The economic slowdown in the wake of the Covid-19 pandemic put the most pressure on debt-laden companies with high costs and poorly functioning systems and operations. By contrast, the most successful logistics providers excelled at the key success factors described earlier — deploying technology to build logistics networks that enable them to deliver the right goods reliably, quickly, in good condition to the right location. 3PLs positioned between these two extremes had a short window of opportunity to adapt to the logistics challenges faced by rapidly growing ecommerce providers. 3PLs that could upgrade their services to satisfy their more demanding logistics requirements had a greater chance of surviving. 3PLs that failed to keep up would unwittingly motivate their customers to invest more in their own logistics capabilities — which would endanger the survival of the 3PL laggards.

Logistics Industry Startup and Incumbent Success and Failure Case Studies

In the case studies explored below, we will examine how these winning logistics industry practices manifest themselves through three strategic mindsets:

- **Executives with a Create the Future mindset were winners:** Executives who were determined to innovate — specifically, Amazon’s CEO Jeff Bezos and its head of logistics Dave Clark — were able to acquire and build technology that enabled Amazon to set and satisfy the highest delivery standards in consumer retailing. Driven by a determination not to repeat its disastrous 2013 holiday season and Clark’s obsessive focus on meeting ever higher delivery standards, Amazon was able to keep investing in a complex, multimodal network that made it ever more able to rely on its own logistics networks — leaving its logistics partners increasingly in the dust.

- **Companies with a Follow the Leader mindset had the potential to strengthen their market position by tightening operations to become sustainable:** As we will see below, the founder of XPO Logistics — which manages supply chains for more than 50,000 companies in 30 countries — was nimble enough to make large acquisitions that boosted its revenues rapidly. After
making deals, XPO cut costs and improved service quality while allocating capital in ways that generally boosted its shares. XPO also invested in technology to better match shippers and truckers and to optimize pricing. Yet XPO's nimbleness was threatened by the industry slowdown in the wake of the Covid-19 pandemic. Unlike Amazon, which was a clear beneficiary of the social distancing policies enforced worldwide to minimize the spread of Covid-19, XPO's customers were a mix of retailers that were effectively shut down by Covid-19 and ecommerce operators that were beneficiaries of social distancing.

- **Head in the Sand** leaders ultimately presided over the near bankruptcy of their companies: YRC – a unionized Kansas City–based provider of less-than-truckload (LTL) shipping services formerly known as Yellow Corp. – was driven into a precarious financial position by William Zollars who took over from the founding family in 1999. By the time he was pushed off the stage in July 2011, YRC had made two large, debt-financed acquisitions, failed to capture the full cost savings potential of these mergers, and allowed its labor costs to remain higher than those of rivals. When the Great Recession dawned in 2008, YRC's revenues plunged some 50%, and the company barely survived. A debt restructuring caused its stock price to plunge over 99%. Despite many efforts to cut costs and restore growth, YRC was never far from another implosion. The industry slowdown that began in 2019 and deepened further in 2020 due to the Covid-19 pandemic made YRC's future even more precarious. By July 2020, YRC had received a below-market rate loan from the government to keep it afloat.

Success: Amazon Builds Its Own World-Class Logistics Capability in 23 Years

Introduction

Amazon was founded in 1994 to sell books over the Web. By 2020, Amazon was a $296 billion company growing at nearly 27% a year with 798,000 employees sporting a stock market capitalization of $1.2 trillion. One of the most significant reasons for Amazon's growth was its logistics network which enabled the company to fulfill its commitments to
consumers for timely and accurate delivery of their online orders. As it grew, CEO Jeff Bezos realized that it could only fulfill its commitment to high-quality service if Amazon built and continued to improve its own logistics network. To that end, in 1997 Amazon began operating its own logistics network with two fulfillment centers a 93,000-square-foot one in Seattle and a 202,000-square-foot facility in New Castle, Del. By May 2020, that network had grown substantially – consisting of fulfillment and distribution centers in the United States to process and ship goods including small sortable, large sortable, large nonsortable, specialty apparel and footwear and specialty small parts as well as operating facilities the perform returns processing and 3PL.6

Case Scenario

Much of Amazon's logistics expansion was the brainchild of Dave Clark who joined the company in 1999 and became its logistics chief in 2013. Clark was known within Amazon for stealthily identifying and firing workers who were not doing their jobs and for removing obstacles that might keep customers from receiving their orders on time. A case in point was Clark's December 2019 decision to block its third-party suppliers from using FedEx to ship their products due to its slipping performance. Fresh in Clark's mind was Amazon's dismal delivery performance in the 2013 holiday season. Soon after he took over, bad weather and logistical inefficiencies caused Amazon to miss its delivery deadlines, angering customers who demanded and received refunds. To prevent a recurrence, Clark invested billions to build out Amazon's logistics network. By August 2019, Amazon was delivering 46% of US packages purchased on its platform. Although it ended 2019 shipping 2.5 billion packages a year, Amazon lagged FedEx's 3 billion and UPS's 4.7 billion annual packages shipped. Clark's decades of experience give him the ability to sniff out problems in daily reviews of Amazon's operational metrics. He asked the responsible manager to explain the cause of the out of control performance and fix it. Clark also spearheaded the $775 million acquisition of robot-maker Kiva Systems – which saved Amazon’s workers from walking miles each day by delivering the products from the warehouse shelves to the workers. By December 2019, Amazon operated some 200,000 robots.”7

Amazon's logistics network was upgraded to fulfill the promise of its Amazon Prime service which sought to reduce the time to deliver goods from two days to one. Its logistics network included the following components:

- **Prime Now Hubs.** To provide delivery as quickly as 60 minutes from the time of placing an order, in late 2014, Amazon began to open Prime Now Hubs. These smaller distribution buildings located close to metropolitan centers were stocked with 15,000 fast-selling items.
• **Grocery logistics.** Amazon established a different logistics network to fulfill grocery orders – the scale of which was expanded after its 2017 acquisition of Whole Foods. By May 2020, Amazon operated a network of room temperature and cold storage grocery distribution centers across the United States to service Amazon Pantry and Amazon Fresh customer orders.

• **Inbound Cross Dock (IXD) network.** To boost the efficiency of the flow of goods into its network of fulfillment centers, Amazon built an IXD network in the United States. The IXD network was located near ports to receive goods from overseas import containers where they were held until an Amazon fulfillment center needed to replenish its inventory – triggering truckload shipments of merchandise from IXDs to fulfillment centers.

• **Regional sortation centers.** In 2014, Amazon launched so-called regional sortation centers to gain better control of the outbound shipment of packages within its distribution network. These sortation centers organized outbound packages by zip code before shipping them out of the region via Amazon’s Air Hub, to an Amazon Delivery Station, or to the US Postal Service post office responsible for the zip code.

• **Air gateway sortation centers.** Amazon also operated a network of air gateway sortation centers near airports that flew customer packages on Amazon Prime Air flights from, say, Seattle to New York. The air hub facilities placed packages from local fulfillment centers into standard air canisters.

• **Amazon Air Cargo.** In 2016, Amazon launched its air cargo operation – operating out of 25 regional airports, the company expected to expand its fleet to 70 planes by 2021. Cargo planes flew the canisters from regional airports to a central hub in Hebron, Kentucky, where packages were sorted and sent out to regional airports around the country.

• **Last-mile delivery stations.** In 2013, Amazon began building a network of delivery stations aimed at completing the so-called last mile of delivery to consumers. The delivery station sorted packages for outbound routes which were shipped by local couriers who contracted through the Amazon Flex program. Despite problems with Amazon’s contract delivery operation, its more than 90% on time package delivery rate was comparable to the performance of UPS and FedEx.
• **European Air Cargo.** By May 2020, Amazon was expected to build out an air hub similar to the one in Kentucky for Europe – likely close to Frankfurt, Germany – which could fulfill an order picked in the United Kingdom to be delivered within one or two days to Spain.8

As Clark focused attention on improving Amazon’s on-time delivery performance, the company continued to envision new ways to cut the time and cost of logistics. In addition to dreaming of using drones to deliver packages, Amazon was considering the acquisition of Zoox, a provider of self-driving technology. This possible deal could supplement other Amazon investments in automated driving (Aurora Innovation) and electric trucks (Rivian). A Morgan Stanley analyst forecast that self-driving technology could save Amazon $20 billion a year – about 22% of its estimated 2023 shipping costs. Industry experts envisioned that Amazon could convert Zoox’s planned robotaxi into an automated delivery van that could become a mobile version of Amazon lockers. Moreover, Rivian – which by May 2020 had contracted to build 100,000 electric delivery vans for Amazon – could also build the robotaxis. In addition to these acquisitions, Amazon owned 210 transportation-related patents on devices including drones and automated ground vehicles.9

**Case Analysis**

The driving force behind Amazon’s logistics network is its CEO’s strategic mindset. And the two elements of that mindset were most relevant to how its logistics network was created and how it evolved. Bezos’s Day 1 philosophy – that a company must look at its strategy with fresh eyes every day – drove Amazon to build a logistics network that could support ever-shorter times to deliver orders to consumers. Bezos’s concept that its customers are delightfully dissatisfied pushed Amazon to make a major investment in its own air and last-mile delivery networks to avoid a repeat of its 2013 holiday delivery disaster. Moreover, because Amazon excels at using technology to serve customers more effectively than competitors, it is likely to continue to expand and improve its logistics network in the future.

**Success: XPO Acquires Its Way to 3PL Success**

**Introduction**

Greenwich, Conn.-based XPO Logistics participated in several parts of the $1 trillion US goods transportation industry. For example, it helped provide much of the $700 billion worth of trucking services in 2019 – of that, roughly $600 billion was full truckload and $40 billion was LTL – in which a truck picked up different cargoes and brought them to distribution centers, which might ultimately be delivered by another truck to their ultimate destination. Because of the many stops along the way, LTL was more complex than full truckload. XPO used acquisitions to expand
its LTL operations in the United States and Europe. XPO also added multimodal transportation—such as picking up goods at a port and delivering them to railroad terminal. Beginning in 2012, Bradley Jacobs—an industry rollup veteran—began expanding XPO. He did this through a process that was developed by the so-called private equity (PE) industry. Here, debt-backed acquirers dominated industries in which market share was fragmented. PE firms acquired companies with a sliver of equity and big dollop of debt. Such debt-fueled industry consolidation—dubbed industry rollups—was a mixed blessing. It was great for PE investors who used the borrowing to extract dividends and other fees. It also favored investment banks and lawyers who advised the deal makers. But the cash to pay the added debt came out of the hides of employees who lost their jobs in the name of efficiency. Industry rollups could also be bad for customers who looked to these growing companies to invest in innovation that created more value for them. Moreover, PE-backed firms often fared poorly during recessions. As demand for their products plunged, so did their ability to repay the debt. What is more, as we saw in the case of Art Van Furniture, capital providers shied away from bailing them out as their stock prices plunged—often resulting in bankruptcy. This last result was particularly bad for common equity investors—who were generally wiped out in bankruptcy. This comes to mind in considering the growth of XPO. Between 2011 and 2020, Jacobs engaged in a series of acquisitions that led XPO’s revenues to soar from $225 million to $16.6 billion, a compound annual growth rate of 61%. By May 2020, XPO was ranked 196th on the Fortune 500—operating in 30 countries, with 1,506 locations and employing roughly 97,000 employees helping over 50,000 customers to increase the efficiency of their supply chains. Sadly for investors, by June 2020, XPO’s shares traded 26% below their September 2018 high, and revenues for its first quarter of 2020 had declined 7% as Jacobs withdrew the company’s forecast for the rest of 2020. To be fair, by June 2020, XPO appeared likely to weather the Covid-19 pandemic more effectively than some of its rivals.

Case Scenario

Jacobs had an unusually large amount of experience with industry rollups by the time he took over as XPO’s CEO in September 2011. At 23, Jacobs cofounded Amerex Oil Associates, a New Jersey–based oil brokerage firm, and served as its CEO until the firm was sold in 1983. He entered this business after dropping out of Brown University in the late 1970s. He was fascinated by the profits earned by oil brokers, educated himself on the industry, and cold-called until he was able to persuade an industry legend, Ludwig Jesselson, head of commodity trader Phillip Brothers, to be his mentor. In 1984, he moved to England where he met his oil-trader wife, Lamia, and founded Hamilton Resources, an oil trading company. Using most of his savings and a $1 billion line of credit, he built Hamilton into a $1 billion-a-year company which profited by obtaining oil from Russia and Nigeria and booking ships to deliver the black gold to Europe. By 1989, however, futures markets were squeezing Hamilton’s profits, and Jacobs returned to the United States to research
his next company. After reading an analyst’s report describing Browning-Ferris’s significant profit margins, he interviewed dozens of industry executives to meet talent and identify untapped opportunities. Two former Browning-Ferris managers told Jacobs that the company had ignored rural areas. In 1989, he founded United Waste Systems; Jacobs hired them and ended up acquiring hundreds of small waste management companies in southern Kentucky and Michigan. In 1997, United Waste Services paid $2.5 billion (including debt) for Jacobs’s company which had grown to the fifth largest in the United States. As the sale United Waste closed, Jacobs was already working with investment bankers to lead a rollup of the heavy equipment rental business – which he dubbed United Rentals, Inc. (URI). This industry appealed to him because it was fragmented and growing as companies switched from owning to renting equipment such as bulldozers, generators, and scissor lifts. He invested $35 million and in December 1997 took URI public. In 2004, the SEC began investigating URI’s accounting practices – two former executives ultimately pleaded guilty to misstating the company’s financial condition between 2000 and 2002 to meet earnings forecasts. In 2007, Jacobs – who was not implicated in wrongdoing – resigned as chairman after a failed leverage buyout of the company. By June 2020, URI was valued at about $12 billion.13

Though he had never previously run a transportation company, his previous companies had helped him develop significant transportation and supply chain experience, the ability to integrate acquired companies and grow organically, and the ability to use information technology to connect global offices into a single, smoothly operating network. By 2011, Jacobs concluded that he could use these skills to build a sizeable player in the $50 billion trucking brokerage market. He led a team that invested $150 million in cash in a 3PL named Express-1 Expedited Solutions which he renamed XPO Logistics. His aim was to build a $5 billion to $6 billion annual revenue 3PL provider through a combination of acquisitions and opening of offices in new locations. By 2015, Jacobs aspired to create about 20 so-called cold-start offices with each location generating between $25 million and $200 million in annual revenue a year. XPO also aspired to acquire between five and seven brokerages annually from the 10,000 licensed brokers working with 250,000 trucking companies. In 2012, Jacobs said that XPO’s success would also depend on its ability to initiate and enhance relationships with shippers and carriers, and to develop an IT platform extending across its brokerage, freight forwarding, and expedited transport businesses.14

Jacobs oversaw XPO’s growth in two phases – a series of large acquisitions between 2011 and 2015 and a consolidation and integration phase between 2015 and 2020. In the first phase, XPO spent over $8 billion to acquire 17 trucking, freight brokerage, warehouse management, and online fulfillment companies. Some investors were concerned when XPO paid $3.5 billion in 2015 to acquire Norbert Dentressangle, a French transportation company, and later that year paid another $3 billion to acquire US trucker Con-way. While XPO’s stock plunged, it eventually rebounded after XPO integrated the acquisitions, sold Con-way’s truckload division, and increased organic growth. In 2018, a short seller
issued a negative report on XPO which again sent its stock down. But by October 2019, XPO was again considering more acquisitions.\textsuperscript{15} XPO’s success was derived from two key strategies. First, the company had achieved a number one or number two market share rank in each of its lines of business. Second, XPO adopted artificial intelligence – which Jacobs saw as a critical new technology – across its businesses. XPO’s facilities used predictive analytics and collaborative robots among other tools to provide better customer service by gaining deeper insights into its customers’ customers.\textsuperscript{16} In 2018, 1,700 of its 95,000 employees were working on automating XPO’s processes. The projects included pricing algorithms and Uber-like apps that allowed truckers to pick up loads and shippers to track the movement of their cargo in real time.\textsuperscript{17}

In 2020, XPO was scrambling for ways to boost its stock market value. That January it announced plans to remedy what it viewed as its conglomerate discount by spinning off several of its businesses. While XPO planned to retain its LTL operation which handled relatively small freight, units reported to be on the block included its European supply chain, European transportation, North American transportation, and supply chain operations in North America and the Asia-Pacific regions.\textsuperscript{18} That March the stock market collapsed which led to a 54% plunge in XPO’s stock price in the month ending March 20 – prompting Jacobs to pull from the market the business units it had planned to spin off.\textsuperscript{19} By May 2020, Jacobs was focusing on ways to boost XPO’s revenues and lower its costs. XPO expected to benefit from strong demand from ecommerce providers. XPO also planned for growth in its truck brokerage business by investing in technology, listening to its customers and employees, and making the technology do what customers wanted it to do. Jacobs also envisioned “ten levers” – such as pricing, applications of technology, and process improvement – with the potential to boost XPO’s cash flow by $1 billion. More specifically, XPO’s variable costs constituted 77% of its total costs – with fixed costs accounting for the remaining 23%. Jacobs said that he was looking for ways to convert more of that 23% into variable costs. XPO’s mission was to create the most shareholder value. Jacobs was willing to do whatever he thought would achieve that aim – including buying back stock; acquiring companies; or using cash to reduce debt.\textsuperscript{20}

Case Analysis

XPO’s CEO executed a successful 3PL industry rollup strategy. More effectively than YRC, Jacobs was able to acquire smaller 3PL companies, cut costs, and use common systems to operate the combined companies more effectively while lowering costs. While it ran into challenges – such as declining demand resulting from the world’s response to Covid-19 – XPO was able to scramble for solutions more effectively. Whether demand would recover enough for XPO to resume organic growth remained to be seen. Nevertheless, XPO’s skills as an effective acquirer of smaller 3PL service providers suggest that XPO was good at conceiving and executing an effective Fast Follower strategy.
Failure: Heavily Indebted YRC Struggles to Transcend Its Financial Woes

Introduction

XPO made it look easy to build a big logistics company through acquisition. Not all logistics industry CEOs shared Jacobs’s combination of acquisition and operational skills. There are many ways that a strategy of growth through acquisitions can go wrong. Companies can overpay for the companies they acquire; take on too much debt to finance the deals; add new costs that are difficult to cut; struggle to link acquired companies with the parent’s systems and processes; and spend so much time on all these internally focused tasks that they fail to recognize and respond to new industry trends and the market share—winning strategies or more nimble rivals. Such problems can turn what sounded like a bold acquisition strategy into an energy-sapping effort to recover from financial blunders that never seem to end—even as new CEOs come in to save the company and quickly depart as their turnaround efforts fail.

This comes to mind in considering the fate of YRC, an Overland Park, Kansas-based trucking company employing 29,000 unionized workers whose stock price peaked in March 2005 at $438,450 a share and by June 10, 2020, had lost more than 99% of its value—trading at some $1.84 a share after reporting sharp declines in daily shipping volume. This massive plunge in value was the result of two reverse stock splits—a 1:25 reverse stock split effective in October 2010 and a 1:300 reverse stock split in December 2011 in the wake of a September 2011 $500 million financial restructuring–designed to keep YRC’s stock above $1 a share to comply with NASDAQ listing requirements. By the end of 2019, YRC was in financial trouble again. And the Covid-19 pandemic only added to the pressure on the company’s shaky financials. The CEO who created this intractable financial puzzle was William Zollars, a 24-year veteran of Eastman Kodak who joined Yellow Corp. in 1996, became its CEO in 1999, nearly presided over its bankruptcy in 2009, and left the company a shadow of its former self in July 2011 before another brush with financial oblivion.

Case Scenario

When he became CEO in 1999, Yellow’s revenues totaled $3.2 billion—but growth through acquisitions eventually followed. In 2003, Yellow acquired LTL rival Roadway, which doubled the company’s size to over $6 billion in revenue—and it was renamed Yellow Roadway Corp. That move gave the combined company a dominant place in the national LTL market. Analysts thought the $966 million Yellow paid was too high, and they criticized Zollars for failing to take advantage of cost-saving opportunities. Zollars insisted that the companies would operate independently and would keep intact each of their 300 terminal networks. To be fair, Zollars conceded...
that some cost would be saved—$45 million in the first year and up to $125 million a year after five years. He also saw the possibility of boosting revenues by persuading Roadway customers to use Yellow’s Meridian management services. Nevertheless, Zollars was happy to allow both companies’ sales forces to compete against each other. Then, in 2005, YRC bought USF Corp., which operated regional LTL fleets. By 2006, YRC—and renamed YRC Worldwide—was a $9.92 billion company with $277 million in net income. When Zollars joined the company, it had been run by the Powell family for over 40 years. In 2006, Zollars took a victory lap. In an interview with Institutional Investor, he said that under the Powell family’s leadership Yellow had participated in only one segment of the industry for so long that it had ignored other aspects of the supply chain that affected customers. If a customer told the company it needed a delivery to arrive a day earlier, Yellow told the customer “Sorry, we don’t do that.” Zollars claimed to have changed the culture by tracking Yellow’s reliability, dependability, and service offerings. He said that he spent 80% of his time out of the headquarters visiting workers on docks and dining with customers. It took several repetitions of the idea that Yellow would be consumer driven for employees to be convinced.

Sadly, for YRC, Zollars’s victory lap was premature. As he was bragging of his great management skills, the company imploded—beginning with losses at the end of 2007. By 2011, its revenues had been chopped in half, and its cumulative net loss exceeded $2.5 billion. At the end of 2009, YRC nearly went bankrupt—being rescued by bondholders who swapped $530 million in debt for about a million newly issued shares. Prior to his July 2011 departure from YRC, Zollars tried to frame his tenure in a positive light—noting that his acquisitions created the largest trucking company in the world which brought him praise from the industry. He blamed YRC’s problems on the Great Recession which caused revenues to collapse and made it more difficult for the company to repay the high debt load it had taken on to make its acquisitions. Zollars sniped at competitors whose lower fixed costs freed them to cut prices to win market share from YRC. He concluded by declaring that his days in the trucking industry were at an end.

Zollars’s departure did not mark an end to YRC’s turmoil. By 2020, after a few more management changes, YRC was still in financial trouble—suffering from a 2019 industrial slowdown and a plunge in industry demand resulting from the world’s response to Covid-19. James Welch took over as CEO from Zollars in July 2011. Welch had planned to retire in July 2018—but was replaced that April 30 by Darren Hawkins. By December 2019, demand was dropping, and Hawkins’s position was looking increasingly vulnerable as YRC appointed a new chair and CFO. YRC reported a 4.5% drop in LTL shipping volume in October 2019 following a swing from a $2.9 million profit to a $16 million loss in the quarter ending September 2019. YRC appointed a banker, Matt Doheny, as chair and replaced its 15-year CFO with Jamie Pierson who Hawkins credited with engineering a turnaround between 2011 and 2016. What’s more, three directors quit in what was deemed an “effort to help right-size the board.” Pierson’s tenure featured aggressive cost cutting. Corporate head count plunged
from 2,200 to under 400 by 2015. In 2013, YRC closed 20 terminals, delayed new equipment purchases, and sold real estate. In 2014, YRC persuaded the union to accept a 15% pay cut and reduced pension contributions for its 26,000 unionized drivers. Soon thereafter, YRC sold $250 million new shares and convertible note holders exchanged them for stock. YRC used the proceeds to pay down debt.\(^{32}\)

By May 2020, the world’s response to Covid-19 had made things even worse for YRC. Hawkins was scrambling to preserve cash as YRC’s credit rating was downgraded. A glimmer of good news was that YRC’s first quarter report had improved over the previous year’s result — a $4.3 million profit compared to $49.1 million net loss in the quarter ending March 2019. With lockdowns beginning in March 2020, YRC laid off and furloughed some workers, eliminated executive bonuses and merit raises, and cut capital spending. Lenders agreed to defer some interest payments and suspended a covenant requiring YRC to maintain at least $200 million in adjusted earnings before interest, taxes, depreciation, and amortization. YRC missed a March payment to a multiemployer health-care fund covering some 500,000 Teamster members. On March 31, Moody’s Investors Service cut its ratings for YRC — citing its weak credit profile and thin margins.\(^{33}\)

YRC’s position continued to deteriorate. In July 2020, the Treasury lent YRC $700 million in exchange for about 30% of YRC’s stock. On July 1, when the loan was announced, YRC’s stock had fallen 27% during the year and was valued at $70 million. The loan was justified by saying that YRC — which ships freight for the US military — was critical to national security. At the same time, the Defense Department was suing YRC for overcharging in the millions of dollars over seven years for its services and failing to follow government procurement rules.\(^{34}\)

Case Analysis

YRC is a story of an acquisition strategy gone so badly that it defied the efforts of many CEOs to fix it. Ultimately YRC’s problem was taking on too much debt to acquire rivals in pursuit of a rapid increase in revenues. While the short-term ego rewards to YRC’s CEO were high, the company failed to properly integrate the companies it acquired. This resulted in costs that were too high — because the CEO failed to cut overlapping operations — and a failure to integrate the acquired companies into the parent company’s systems and processes. Moreover, YRC’s unionized workers earned high compensation relative to those of YRC’s rivals — which made it easier for rivals to win its customers by cutting price. YRC could not set its prices lower without sacrificing its profit margins. After a financial restructuring that wiped out most of its shareholders’ equity, YRC stock has remained exceptionally low for years. Covid-19 has made hopes for its recovery even more difficult to imagine.
Logistics Industry Case Study Takeaways

The takeaways from these case studies have varying implications depending on where you sit.

**Incumbent Executives**

- **Do:** Based on the Amazon and XPO case, logistics executives may create competitive advantage by
  - Setting ever-shorter delivery time targets and investing in the logistics networks needed to meet those standards reliably
  - Analyzing process inefficiencies that cause delivery problems and seeking out and acquiring or building new technologies that can fix these inefficiencies
  - Building and using systems to track in real time critical operating metrics related to satisfying commitments to customers
  - Hiring and developing managers and staff who can take responsibility for identifying the causes of delivery problems and deploying effective solutions

- **Do not:** Based on all the cases, logistics executives should avoid self-destructive tactics such as
  - Surrounding themselves with executives who seek to retain their jobs by praising the CEO’s pronouncements rather than challenging the status quo
  - Ignoring operational excellence and financial sustainability to pursue rapid growth
  - Failing to develop a next generation of leadership that can sustain the company’s competitive edge

**Incumbent Employees**

- **Do:** Incumbent employees should seek out the specific jobs that will enable them to contribute to the growth strategies of their current employers or at innovative logistics providers such as Amazon or XPO.

- **Do not:** Based on the YRC case, incumbent employees should seek employment elsewhere if they work at logistics providers that are not creating the future or following fast.
Startup CEOs

- **Do:** Startup CEOs should consider partnering with Amazon by developing innovative technologies that these large companies can use to make their logistics operations more efficient and effective.

- **Do not:** Seek out partnerships with logistics providers that fail to adapt to changing customer needs and the strategies of the most innovative industry participants.

Business Students

- **Do:**
  - Business students interested in logistics should start companies that can solve the most pressing operational problems facing innovative logistics suppliers such as Amazon or XPO.
  - Based on all the cases, business students should seek managerial opportunities at innovative logistics suppliers such as Amazon or XPO.

- **Do not** work in the logistics industry unless they are passionate about solving its biggest business challenges.

Do You Have the Strategic Mindset of a Logistics Industry Winner?

If you answer in the affirmative to these questions, you have a winning strategic mindset. If not, you must decide whether to change your mindset, strategy, and execution or find a job that better suits your strengths and interests:

- Do you have a deep understanding of the logistics expectations of your business customers?

- Do you operate a logistics network that can satisfy customers’ delivery expectations reliably and at a competitive price?

- Do you invent or acquire new technologies that enable you to outperform your competitors at satisfying your customer’s delivery time, quality, and price expectations?

- Do you have the management skills and technical talent needed to analyze and solve operational problems in real time?

- Do you regularly delight customers, so they recommend your logistics service enthusiastically to others?
Conclusion

The logistics industry is large, growing slowly, and reasonably profitable. Yet 2020’s pandemic economy reduced demand for logistics suppliers other than those who served ecommerce leaders – such as Amazon – which enjoyed a surge in demand as store-based retailers temporarily shut down and reopened with much lower business volumes. Create the Future companies such as Amazon benefited from these changes. Follow the Leader companies like XPO were in an uncertain position – depending on whether more of its demand came from customers were Covid-19 winners, rather than losers. And companies with a Head in the Sand mindset like YRC found themselves in a precarious financial state. The most important implication for leaders – particularly those in the logistics industry – is that if you lack a Create the Future or Follow the Leader mindset, hire a replacement CEO who does. Chapter 8 will examine the implications of CEO strategic mindset for leaders.