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OF INTEREST

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AMAZON'S EVER-INCREASING PRESENCE IN LOGISTICS



Ten years ago Jeff Bezos, founder and CEO of Amazon.com, which had started in the 1990's as an online bookstore and rapidly achieved great success, had a brilliant idea—give customers who were willing to pay a modest annual fee unlimited free two-day shipping. Thus Amazon Prime was launched. This was an unusual and almost counter-intuitive business decision that did not seem to make any sense at a time when Amazon's shipping costs were skyrocketing. But a lot of people signed up and the program took off.

In 2011, Amazon sweetened the pot with an unlimited video streaming service as a benefit of Prime membership. People continued to sign up, and, what's more, those who were already members stayed on as members, in part due to the video service. Like Netflix, Amazon began to make original shows and movies to get more people to sign up for the video service—and also to buy more cameras, toothbrushes, and coconut milk while they were at it. Now membership benefits have expanded to include music streaming, a Kindle e-book library, and cloud-based photo storage. At \$99 per year—a little more than \$8 per month—this is a great deal for consumers; but how can this business model possibly benefit Amazon enough to absorb all of those shipping costs?

Despite the raise in the annual fee from \$79 to \$99 in 2014, Amazon Prime membership has continued to increase year-over-year. At an estimated 54 million subscribers, Amazon Prime now has more members than Canada has citizens (35 million), and is on target to exceed the U.K.'s population of 65 million. So what does this do for Amazon? Simply put, it was a forward-looking long-term strategy that worked beautifully; Amazon Prime members spend about three times more each year ordering goods from Amazon than their non-Prime counterparts. Amazon has created a finely-tuned engine that has driven an optimized consumption cycle custom-built for the 21st century.

But growth doesn't come without a cost. The burgeoning, busting-at-the-seams e-commerce industry—led largely by Amazon—experienced a hiccup in 2014. As a surge in last-minute peak holiday shopping strained the resources of the larger small-package delivery network, a package delivery meltdown ensued. This was an “aha” moment for Amazon, a call to action to evolve its supply chain practices. Amazon could not keep its delivery promises if it could not count on its shipping partners to handle the steady growth in volume, and this was squarely at odds with its contract with consumers. Clearly something had to be done.

“In order to properly serve our customers at peak, we've needed to add more of our own logistics to supplement our existing partners,” said Amazon CFO Brian Olsavsky in January. “Those carriers are just no longer able to handle all of our capacity that we need at peak. They have been and continue to be great partners. It's just we've had to add some resources on our own.”

Some resources on their own. In the past few months, Amazon has been open and aggressive about increasing its reach, capabilities, and capacity in the logistics and distribution arena. They

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have purchased thousands of trailers with the Amazon logo in the U.S., registered as an NVOCC to better manage the flow of imports from China, and leased 20 U.S. domestic cargo planes from Air Transport Services Group. Amazon fulfillment and sortation centers are springing up all over the U.S., as are Amazon Prime Now hubs and Amazon Fresh grocery delivery stations. There has also been rapid expansion in Europe, building networks country by country, as well as expansion of shipments into China.

Some speculate that Amazon is positioning itself to compete with small-package carriers such as FedEx, UPS, and DHL, but FedEx founder and chairman Fred Smith isn't worried. He recently called that idea "fantastical", and said that reports of market disruption are based on lack of knowledge, citing that it would take years and tens of billions of dollars to replicate existing networks.

But these remarks are based on the belief that Amazon's use of internal transportation options to position its inventory resemble those of any traditional retailer, like Wal-Mart or Target.

As we know, Amazon is far from being a traditional retailer, and its rapid growth and increasingly more time-specific delivery demands, which have been shown to challenge current transportation suppliers, could be just the catalyst to propel it more deeply into the logistics industry. Also consider that Amazon spent about \$11.5 billion in outbound shipping in 2015, while collecting about \$6.5 billion in shipping-related revenue, leaving a \$5 billion net gap; that's a lot of incentive for them to take more control of their shipping costs.

FedEx may not see Amazon as a disruptor or a competitive threat, but others do not agree. According to Satish Jindel, president of SJ Consulting, which is preparing a white paper on Amazon's logistics expansion, Amazon is in the process of building an asset-light distribution network for fast delivery of goods, much as Roadway Package Services (now FedEx Ground—*hmm*) did in the 1980's. Only it is doing so on a global scale.

Amazon has taken the first steps in Germany to reduce its reliance on established logistics companies. In 2015 they opened a parcel sorting center in Munich and are using more than 200 delivery vans operated by a subcontractor for last-mile delivery to customers. And there are plans to open more sorting centers near major German cities and offer last-mile delivery to retailers that don't sell their products on Amazon.com.

Amazon has indicated their intention to establish a parcel network across Europe. This looks a lot like direct competition with Germany's Deutsche Post DHL Group, the world's largest courier company.

The next target in Amazon's sights appears to be La Poste, France's largest mail delivery provider. Amazon currently owns 25% of the private delivery firm Colis Privé, and is said to be in the final stages of buying out the company entirely. Colis Privé is the largest private parcel delivery company in France, specializing in guaranteed delivery in 24 to 48 hours.

"Amazon will likely continue this path of controlling its supply chain all the way to the customer's front door in other European countries," John Haber, CEO of Spend Management Consultants, a supply chain management consulting firm, told the Journal of Commerce. According to Haber, Amazon is integrating itself into the supply chains of the countries in which it already has a fulfillment presence. You only have to look at a map and count the fulfillment centers to get an idea of where Amazon will go next. France first with its four fulfillment centers, and perhaps Poland next, which has three.

FedEx may not be worried now, but there is every reason to believe that they may be staring at a diminished revenue stream in the future as Amazon takes more control of its own logistics. And they just may be looking at a future direct competitor, especially as the tech-savvy millennials make up an ever-larger part of the consumer pool.

SOURCE: Journal of Commerce ongoing coverage; Wired article—2/9/15.





SMALL PLATES

Panama Canal Locks to Open June 26

Nine years after the expansion project began—two years after the original completion date and \$150 million over budget—the new Panama Canal locks are scheduled to be inaugurated on June 26, 2016.

Ocean carriers have been eagerly awaiting the completion of the new locks, which will be 1,400 feet long, 140 feet wide, and 60 feet deep, compared with the 1,000-by-110-by-40-foot dimensions of the three sets of existing locks. This means that vessels with capacities of up to approximately 13,000 20-foot-equivalent-units will be accommodated. The current Panamax size is 4,500-5,000 TEU's.

Work on the locks was started in 2007 and was scheduled for completion by April, 2014, the 100th anniversary of the canal's opening. But construction delays and other issues, including a dispute with the international construction consortium handling the project and cracks detected in Fall, 2015, contributed to cost overruns and pushing back the timeline.

A training center has opened with a scale model that will be used to train pilots and tugboat captains to operate in the expanded canal. Commercial operation is set to start during the third quarter of the year.



SOURCE: *Journal of Commerce* article—3/24/16.

New Shipping Hub Potential for Cuba

Officials from 18 logistics companies were part of a trade delegation that visited Cuba on March 25th, coinciding with President Obama's visit. After watching operations at the Port of Mariel and meeting with prospective partners in Cuba, they said that Cuba may be an ideal location for cross-docking, or resorting and distributing, cargo from post-Panamax ships to smaller vessels headed to the U.S. and to Mexico, especially in anticipation of the opening of the new Panama Canal locks.

"Their location is absolutely perfect to be a hub...to push freight into northern Mexico, or all along the southern coast, and even up to our ports that don't have that deep draft on the eastern side," said Sue Spero, president of Carrier Services of Tennessee, Inc.

Poor infrastructure and heavy bureaucracy pose significant hurdles, but the group found the Mariel port to have modern facilities, including the ability to handle refrigerated shipments and weigh trucks entering or leaving the container terminal.

Members of the logistics delegation said agreements already in place, such as a multimillion-dollar deal underway for Starwood Hotels and Resorts Worldwide to manage hotels in Havana, will start a flow of goods for the hospitality business.

While the door has been opened to more travel, tourism, and some business dealings, it is to be remembered that limitations on trade are still in place and can only be lifted by Congress.

SOURCE: *Wall St. Journal* online—3/29/16.

East Coast ILA Squabbles

The latest squabble at the Ports of New York and New Jersey involve allegations of discriminatory hiring leveled at the International Longshoremen's Association (ILA) by Newark Mayor Ras Baraka.

In a letter to Labor Secretary Thomas Perez, Baraka has requested a federal investigation of "severe racial, gender, and ethnic inequality" and "an apparent bias against the hiring of local residents" at the East Coast's largest port, one fourth of which is within the city of Newark.

ILA president Harold Daggett calls these claims "baseless" and "misleading", and says there is no need to "waste time and valuable resources investigating them."

The ILA is also the subject of an inquiry currently underway by the Waterfront Commission of New York Harbor, trying to get to the bottom of who called the illegal one-day wildcat strike in January, which blindsided terminal operators, truckers, shippers, and even many dockworkers.

The Commission has also investigated hiring practices by the ILA in an effort to curtail nepotism and favoritism and orga-

nized crime influence on the docks, which lends support to Baraka's complaints.

The current labor contract is up as of September 30, 2018; it is to be hoped that the bickering and finger-pointing going on now is not a harbinger of things to come. Shippers may be understandably nervous about the disruption that may ensue if negotiations on the East Coast follow the same pattern as last year's West Coast negotiations.

SOURCE: *Journal of Commerce* articles—3/15/16 & 3/23/16.

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TRIVIA

1. Which famous fictional character celebrates a birthday on the 17th of April—Sherlock Holmes, Daffy Duck, Tom Sawyer, or Shrek?
2. “Here cometh April again, and as far as I can see the world hath more fools in it than ever.” This is a quote by which English writer—Percy Bysshe Shelley, William Wordsworth, Charles Lamb, or Samuel Taylor Coleridge?
3. April 13th is National Scrabble Day. Can you name the two letters in English Scrabble that are worth 10 points?
4. April marks the beginning of baseball season. Which major league team has won the most World Series?

[Click here for answers to Trivia questions.](#)