



# GLOBAL LOGISTICS & SUPPLY CHAIN STRATEGIES

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**COMPLEXITY MASTERS: CARDINAL HEALTH**

## Cardinal Health Finds Cost, Service Advantage in Getting Out of the Transportation Business

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*Supply chain management is a critical core competency of the medical and surgical supply distributor, but the company saw opportunities for improvement in transportation. In Penske Logistics, Cardinal found a partner with a laser focus on this important part of its business.*

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**A**s the nation's second-largest distributor of medical and surgical supplies, Cardinal Health puts a lot of emphasis on its supply chain. "Our business is all geared toward getting the right product in the right place at the right time," says Mike Berg, vice president of transportation for the Dublin, Ohio-based distributor. "Given

the nature of the institutions and the people we serve, our operations have to be very service-intensive."

Cardinal Health's \$91bn business is divided into three distinct units: a clinical products and manufacturing business, medical products distribution, and pharmaceutical distribution. The medical products distribution business, which is the subject of this report, encompasses 40

distribution centers and thousands of healthcare customers, such as hospitals, clinics, surgery centers, clinical diagnostic laboratories, reference labs and physicians' offices.

"Our sales channels are diverse and fairly complex, as are our products," Berg says. "We have access to over 300,000 unique SKUs and stock 70 to 80 unique SKUs in our DCs."

Managing this inventory is clearly considered a core competency at Cardinal Health. The company controls 100 percent of its distribution centers as well as several forward-stocking locations known as replenishment centers. “There is absolutely no interest in outsourcing this activity,” says Berg. “We continue to make significant investments to make sure we have leading-edge capabilities.” Cardinal Health uses a warehouse management solution from Witron Integrated Logistics, a German company with U.S. headquarters in Arlington Heights, Ill. The Witron solution includes software and automated materials handling hardware.

Health decided to outsource its medical products domestic transportation to Penske Logistics of Reading, Pa. Central to this project was the transference of Cardinal Health’s large private fleet to Penske.

“We decided to look at outsourcing because we felt there were opportunities to get better efficiencies from our fleet and to optimize the activities that we perform everyday on behalf of our customers,” Berg says. “We also wanted to find a way to provide better visibility and transparency to our customers concerning their orders and shipments.”

Cardinal Health had previously leased the trucks in its private fleet from the leas-

tions for our customers,” says Berg. “I’m pleased to say that we made that transition without a hiccup. It was totally seamless to our customers.”

In the transition Penske Logistics took over 480 power units, 600 trailers, and about 750 full-time employees, explains Joe Gallick, senior vice president of sales for Penske Logistics. “Most companies that shift a private fleet to dedicated contract carriage do it in phases,” he says. “That is probably safer because you can learn the realities of the business through the early phases and then make improvements as you complete the total network implementation. Cardinal Health considered this option, but decided to invest in the necessary upfront planning to do it all at once.”

The planning was thorough but fast. “Once it was decided that we were going to implement this network in one shot, we had 60 to 90 days to put the organization together,” says Gallick. To facilitate this effort, Penske brought its 6Sigma Change Acceleration Process to the table to help ensure that the project stayed on schedule and that no detail was overlooked.

On the Penske side, much of the planning was around human resources. Penske wanted to retain as many Cardinal drivers as possible because of their accumulated knowledge about Cardinal Health’s customers. “A customer’s most frequent contact is with the driver,” says Gallick. At the same time, the logistics company wanted the transition to be smooth and stress-free for employees. “We worked hand in hand with Cardinal’s HR folks to understand their drivers’ needs,” he says. “The contract was announced on a Friday and we immediately had human resources folks from both Penske and Cardinal at every facility to meet with drivers and their families. It was an emotional time for them and we wanted to assure them that they could have a job with Penske if they met our criteria, and virtually all of them did, and to let them know that we are a good employer.”

The percentage of drivers that made the switch was in excess of 98 percent. “At the end of the day, the changeover basically was a badge-flip process for the employees,” says Berg. “One of the critical elements around making that transition successful was our work at the beginning

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*“We wanted to provide better visibility and transparency to our customers concerning their orders and shipments.”*

— *Mike Berg of Cardinal Health*

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“In our business we need a warehouse system that can support picking pallets, cases, boxes and single units – a system flexible enough to handle small orders all the way to bulk, with storage areas that range from frozen to refrigerated to ambient, plus the added complexity of handling some goods that are classified as hazardous materials,” says Berg. Additionally, he notes that Cardinal Health has regulatory issues to contend with in terms of product storage and chain of custody.

“Obviously, very few off-the-shelf applications are able to meet those requirements,” says Berg. Cardinal Health worked with Witron to customize its solution and has continuously updated the Witron system over its 10-year partnership. “The capabilities we have with Witron include such functionality as automated storage and retrieval, pick-to-voice, lot tracking, expiration tracking and automated rotation,” he says. “These capabilities meet the needs of the healthcare space very well.”

While strong in transportation, Cardinal Health also recognized that there was an opportunity to improve efficiency and cost effectiveness. As a result, Cardinal

ing division of Penske, so it naturally included Penske in its search for an outsourcing partner. “We went through an RFP process and looked at six different 3PL providers before we ultimately decided on Penske Logistics,” says Berg. “I think the biggest value driver behind that decision was Penske’s single-minded focus on understanding where inefficiencies were occurring in our transportation operation and on how to eliminate those inefficiencies. They had really strong resources in logistics engineering that they could call on to help us redesign our routes, evaluate schedule changes and look at other ways to improve operations.” Cardinal also recognized Penske’s IT capabilities and potential to improve product visibility in the supply chain from point of purchase to point of delivery.

Cardinal decided early in the process that it would shift management of its extensive fleet to Penske in one fell swoop rather than making the switch in phases. “As you can imagine, this required a fair amount of preparation and planning to ensure that Penske understood our operational processes and could pick up the ball on day one without any implica-

to ensure there was a good cultural fit between our two companies and an understanding of what these employees value in terms of a working environment. We put a lot of effort into making sure they saw Penske as an extension of our supply chain and that they continued to be a very important part of our service to customers.”

Second to employees, the next priority was to improve fleet efficiency. “One of Cardinal’s goals was to really make their transportation fleet a differentiating asset in their value proposition to customers,” says Gallick. “At the same time, as with all companies now, they were looking at opportunities to better manage costs in this area. So, early in our partnership we aligned our finance organizations and agreed on certain toll gates we wanted to reach in terms of better use of equipment and asset rationalization.” One of these goals was to improve transportation efficiency by 5 percent to 10 percent with no adverse performance effects, he says. “I am happy to report that we accomplished that goal, which is just one example of the benefits we are driving toward.”

To reach these goals, Penske worked closely with Cardinal Health to evaluate all of its customers’ needs, their shipment history and frequency of deliveries to see where there were opportunities to consolidate shipments and increase fleet utilization. Penske also was able to match some of Cardinal Health’s backhaul movements with incoming shipments from suppliers, Gallick says. “Then we started looking to

our broad customer base for additional backhaul opportunities that would enable us to generate income on those assets.”

Penske also looked to the fleet itself for efficiency gains. “We had maintained this fleet for many years so we knew how it performed and what the maintenance costs were,” Gallick says. “Once we were managing the fleet, we also began to look at operational issues and how we might be able to improve fuel efficiency. We had significant success, for example, from reducing road speeds, which also reduces carbon emissions. It’s not that Cardinal couldn’t do these things but they are a distribution company and their focus is on getting product to market and increasing their market share. They came to us because we have a laser focus on transportation and logistics and are able to give attention to all those little details.”

Berg says the improved fuel efficiency that Penske has achieved enables Cardinal Health to get 6.6 miles per gallon instead of 6.4, which he says can deliver significant savings with a fleet that drives more than 30 million miles per year.

The next phase of the project will be implementation of Penske’s transportation management system in its medical products operations. “In the beginning, we used Penske’s engineering team to help us continuously evaluate outgoing freight, optimize our fleet utilization and ensure that we selected the most cost-effective carriers for supplemental moves,” says Berg. Deploying Penske’s TMS application

will automate much of this effort. “We anticipate additional savings as a result of being able to optimize on a dynamic basis,” he says. “This program is in beta now, and we are beginning to evaluate and determine our rollout strategy.”

The partners also are beginning a dialog on how Penske might be able to help with Cardinal Health’s inbound transportation as well as its outbound. Currently, Cardinal Health controls only about 25 percent of its inbound freight, Berg says. “With a portion of our suppliers we manage freight and carrier negotiations and our terms are FOB origin, but a large portion of our supply base maintains control of freight spend and carrier selection. We see that as an opportunity.

“We think there is real value in offering a different model to our suppliers as it relates to inbound product flow,” Berg continues. “We are in the very early stages of this process and I expect we will implement changes over the next 12 to 18 months.”

During the first six months of this partnership, Berg says Cardinal Health has “had virtually no customer complaints, which is quite an accomplishment considering we make a million deliveries a year via our fleet. As we continue to evaluate opportunities to drive efficiencies into the healthcare supply chain, which is something we all want to do, we believe we are partnered with the right people to help us achieve a competitive advantage in both cost and service.” ○