

Kurt Salmon 

RETAIL INDUSTRY INSIGHTS

Bridging the Gap

*The Benefits of Collaborative
Profitability Management*

Financial pressure from all angles—increased raw material, labor, transportation and warehousing costs—combined with a reluctant consumer, places extra emphasis on identifying cost-saving opportunities throughout the retail organization. Although many retailers have seemingly weathered the recession and are back on the road to profitable growth, increased financial performance is always important, especially to thrive in the current retail environment.

Increasingly capable systems solutions are leading the way toward cost reduction by measuring and collaboratively managing the profitability of a trading partnership for the first time.

Visionary partnerships, courageous enough to share information more freely, are starting to break out of their silos and reap the significant benefits of collaborative profitability management (CPM), which include increased sales (2% to 4%), decreased COGS (1% to 3%) and inventory reductions (1% to 3%), and which can ultimately yield increased revenue and gross margin.

The Basics behind CPM

CPM is a new concept combining activity-based costing (ABC) with the power of network optimization and simulation across both sides of a trading partnership to create an integrated approach for evaluating the net profitability of a wide variety of product flow and handling options.

Activity-based costing solutions drive general ledger costs down to the level of categories, vendors and SKUs, allowing for the exploration of differences caused by unique business characteristics such as merchandise cube and weight, shipment configuration and trade promotion considerations.

Network optimization and simulation solutions identify the impact of different supply chain network configurations on transportation, fixed and variable operating expense, inventory cost, and service.

EXHIBIT 1: CPM Approach



CASE STUDY

CLIENT

Multibillion-dollar regional consumer packaged goods wholesaler and retailer.

CHALLENGE

Maintain, and potentially strengthen, already razor-thin margins in the face of significantly increased competition from larger national grocers.

SOLUTION

Kurt Salmon worked with a cross-functional client team to reach a consensus design for the new ABC approach and a vision for how the output would be used to increase profitability.

Kurt Salmon worked with the client to translate the consensus design into a robust ABC technology solution that:

- » **Provided the foundation for establishing the correct framework for building a new pricing program for customers**
- » **Established accurate cost metrics for restructuring transportation fees to customers**
- » **Identified significant areas of cost within the client's supply chain**
- » **Enabled effective negotiations with vendors on ways to improve profitability**
- » **Provided insight into individual SKU profitability to restructure categories (SKU optimization)**

RESULTS

Kurt Salmon worked effectively with the client to design and build an ABC solution that provided individual profit and loss statements at the individual vendor, category, SKU and customer levels. This data, coupled with additional model outputs, was used to identify over \$4.9 million in short-term savings opportunities.

Most current solutions do one or the other—not both. But providers on both sides are extending their reach to offer increasingly integrated solutions combining elements of ABC and optimization to offer more comprehensive guidance on initiatives that drive improved profitability. And, for the first time, with this integration comes a foundation for extending profitability management across the end-to-end supply chain—spanning trading partners in the process.

Why Embrace CPM?

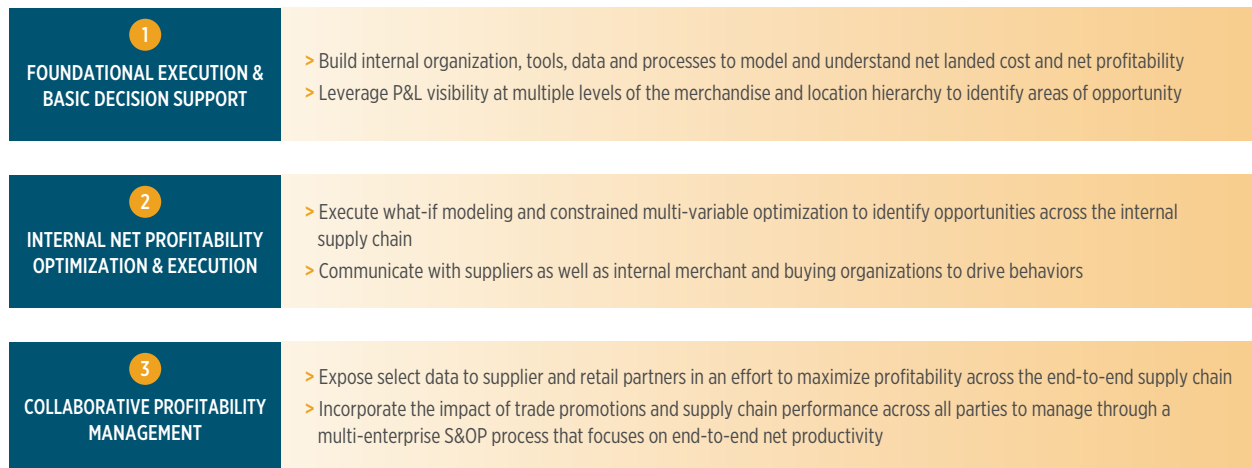
Stepping out of the siloed view of retailer or supplier to understand cost to serve and net profitability of a trading partnership dramatically improves strategic and tactical decision-making. It provides an entirely different view into the cross-organizational “contribution” of entities such as categories, sub-categories, SKUs, customers and suppliers to the bottom line.

The information generated from a collaborative profitability management program can be used to drive opportunities in the areas of pricing, promotion planning and assortment planning, just to name a few. Coupling collaborative ABC profitability modeling with the ability to optimize across the shared infrastructure of a trading partnership drives even more benefit.

Starting the CPM Process

Profitability management is an evolution that begins with enabling resources, data and tools to achieve an internal, actionable, multilevel view of net profitability. Once in place, finding the right partner, moving outside the silo and beginning to share information open up a whole new set of opportunities. A handful of suppliers and retailers have begun to test the waters, most notably in consumer packaged goods, and they are seeing tremendous benefits.

EXHIBIT 2: Profitability Modeling—Process Framework



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