Aligning the Warehouse, Purchasing & Sales for Your $uccess and Sanity!

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What does aligning purchasing, distribution, and sales mean?

- The three disciplines work in unison as a supply chain to provide the best possible product and the greatest profit
  - Marketing is also a forgotten, but key player
- Decisions about everything from vendor selection, product stocking decisions, and "go to" market sales strategies are decided as a team
- Financial and performance results are measured as impact to the corporate bottom line, not silo accomplishments

The Three Silos

- Procurement
- Distribution
- Sales/Marketing

Silo 1 – Procurement

- Their Current Core Priorities
  - To source stocking product at the cheapest price
    - To reduce COGS
  - To have enough product in stock for sale
  - To lower the impact of inbound freight on COGS
  - Many procurement teams are awarded (financially) on lowering the COGS metric

Silo 2 – Distribution

- Their Current Core Priorities
  - To validate and receive inbound stock against expected requirements
  - To house and manage inventory
  - To process outbound orders at the lowest possible cost with highest possible accuracy
  - Many procurement teams are awarded (financially) on order OTD, order accuracy, and cost per order/line shipped

Silo 3 – Sales and Marketing

- Their Current Core Priorities
  - To sell product at the highest possible price while increasing sales
  - To provide clients with goods and services that differentiate their products from competitors
  - To ensure that their customers are satisfied with the level of product and services received
  - To introduce new and improved products
  - Usually directly compensated by margin on sales

Why is this a problem?

These 3 elements; Procurement, Distribution, Sales and Marketing typically work as independent entities within a company

- They are rewarded on goals that may negatively affect the other areas
- The true cost burden of decisions made within an area may be shifted to another area
- There is not a true understanding, operationally and financially, of the true impacts of decisions made outside of their own immediate goals
- The 3 areas work as Silos working to independent goals as opposed to a larger corporate vision

3 components of profit

- Revenue
- Margin
- Operating Expense

Example 1

REAL WORLD EXAMPLES

Example 1 – Procurement Changes Inventory Source

- Procurement switches vendors from US based to china based vendor
  - Saved 4% on unit COG (including freight
    - Viewed as 4% margin bump
    - Core inventory line (several items affected)
    - Larger purchases (to account for over extended lead times) made freight costs neutral

Example 1 – Procurement Changes Source

- Distribution Impact
  - Cartons stacked in container, not on pallets. Had to be hand unloaded, sorted, and stacked
  - Carton Labeling was not adequate and cartons has to be relabeled by the distribution center for facility use
  - Damaged product increased from less .25% for domestic OTR to 9% (either repacked or non-saleable)
  - Pallets had to be purchased, shrink wrap added for internal handling
  - Purchasing quantity raised from 1 month supply to 3.5 months to get container loads maxed and overcome lead times; pallet storage requirements more than tripled
  - Packaging was slightly different and the DC had to keep the different products segregated (even returns)

Example 1 – Procurement Changes Source

- True impact
  - The great deal that procurement got
    - 4% reduction in cost of goods
    - 7% increase in the cost of goods when the distribution impact costs were added to the COGS
      - Originally, the DC impact was only considered a cost against the operations, not as a cost of the product (higher sales margin, unrelated increase costs in operations)
    - The Net result was a 3% margin loss

Example 1 results

- The true LANDED cost of the product (ready for distribution) went UP when all costs were factored in
- The DC had increased labor and supply costs NOT attributed to the product change
- Inventory turns dropped as physical storage requirements increased
- Service level and quality dropped
- The lack of vendor compliance requirements and guidelines means the company ASSUMED the extra responsibilities and costs for the product
- There is no mechanism for the company to see the true cause and effect as a supply chain metric…only in the silos

Example 2

REAL WORLD EXAMPLES

Example 2 – Marketing and sales pushes a product line

- Sales/Marketing wants to give a boost to sales numbers
- Key Product line, core items to have special lower price for 2 weeks starting the following sales Monday
- Sale Product is featured on landing page of website
- Email blast announcing limited time special price
- Sales force is given marching orders to push the product
  - Sales given extra incentive rewards for category sales
- Call Center and CSRs given scripts to push the product
- All hold messages changed to reflect sales offer

Example 2 – Marketing and sales pushes a product line

- Impacts to procurement and distribution
  - Were not informed of sale, the scope, or forecasted increases in volume
  - On hand quantities not sufficient to fulfill increased volume
  - Procurement forecasts were not accurate due to the unprecedented temporary bump in volume
  - Procurement ordered product based on short term need with lead times out of range of sale; product was expedited at a higher cost and the supplier had to beak up shipments
  - Stocking levels of the primary pick mediums in the DC no longer sufficient / running through stock
  - Average line per order / average revenue per order drop
  - Product out of stock must be backordered
    - Process as separate orders by the DC (doubling costs)
    - Company must pay shipping on back orders

Example 2 results

- Increased gross sales
- Lower gross margin (due to special pricing)
- Lower revenue per order / lower profit per order
- Increased landed cost of product (higher COGS)
- Increased warehouse cost per line (receiving, replenishment, picking, packing, consumables)
- Increased outbound shipping cost burden
- Increased sales at a lower net operating profit

LET'S FIX IT

Teamwork

- The disciplines CANNOT work and make decisions in the vacuum of their department
- Weekly planning meeting that have all of the disciplines involved
- The silos should be aligned on concepts and programs
- The true impact of a program or concept on the supply chain should be clear and understood by the entire team
- Never have performance goals or incentives tied to things that will negatively affect another discipline, rather positively affect the corporate bottom line

Fixing it! Think like a 3PL when it comes to operations

- Every function has a cost
  - Product storage and space required / cost per location
  - Product handling (receiving, picking, counting) / cost per touch
  - Product prepping (re-boxing, labeling, documents, etc)
  - Value added costs (inbound and outbound)
  - Product attribute impact – products of unusual size or handling requirements
  - A good 3pl will NEVER take on product or services where they cannot clearly define the cost impact to the COMPANY

Procurement's NEW Priorities

- Vendor Compliance Program
  - Spell out all inbound requirements
    - Cartons, labeling, pallets, UOM's
    - Volumemetric data (key for Ecom)
  - Police Vendors in terms of communicating results
- COGS calculated on TRUE landed cost (ready for put-away in the DC)
- Product Return program, especially on new products/ product lines
- Increase inventory turns by focusing on both volume items and excess / obsolete
- Calculate the FULL financial impact and physical requirements of special buys

Distribution's NEW Priorities

- Define cost of storage and services to communicate to the other disciplines
- Document vendor compliance performance results
- Streamline and automate value added services
- Use volume-metrics to determine space and system requirements (no guess work)
- Use cost per order/line processed to measure financial performance and gauge improvements
- Define and communicate order service levels to sales (what is the time horizon to process orders)

Sales & Marketing's NEW Priorities

- Include the other disciplines on sales and marketing initiatives
- Align sales quantity breaks with stocking UOMs whenever possible (i.e price break on 5 when box is 6)
- Understand the prep time to ramp up procurement and operations for a major sale or product launch – BE PREPARED TO FORECAST
- Understand what the value added service you offer or your customers request REALLY cost
- Provide realistic sales forecasts for proper planning

Joint Operations

- Active excess and obsolete program resolution
  - Inventory carrying costs valued typically at 20-25% of it's value year over year
  - Invoke a REAL program – set up a structure
    1. Put the items on sale
    2. Put the items on sale AND spiff the sales/CSR's
    3. Fire sale the items below cost
    4. Sell the items to a jobber for whatever you can
    5. Throw the items out or donate them

Carrying Cost Financial Impact - Item

Example	
Light bulbs - D item class	
Cost Ea	$ 10.95
Quanitiy on Hand	50
COGs on hand	$ 547.50
Last Year sales	2
Carrying cost factor	20%
Year 1 Carrying cost	$ 109.50
Year 2 Carrying cost	$ 109.50
Gross Margin on Product	25%
Margin on my 2 units	$ 27.38
After 2 years, COG	$ 766.50

Carrying Cost Financial Impact – overall

Actual Client			
Total Inventory Items		52852	
Items without sale in one year - E Items		12581	23.80%
Total Inventory COG		$3,800,000	
E Items COG		$855,000	
Carrying cost factor		20%	
1 year carrying cost		$171,000	
3 year carrying cost		$513,000	

Summary

- Think like a 3pl – every function has a cost
- Sales, Procurement, and Distribution should be a working team for ALL facets of planning
- Understand the real impacts of inventory carrying costs and give yourself options to return inventory before it gets old
- Implement a vendor compliance program, even if you can't get 100% compliance
- Don't be penny wise and pound foolish – understand overall true cost impact to the company, not just on metric

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