



Operational Costing Case Study: Consumer Packaged Goods Manufacturer

Business

\$1.8 billion U.S. manufacturer of office products for the consumer and small business markets. The product offering includes 6,500 product SKU's (a, b, c, d items) that are sold and distributed to food, drug, and mass merchandise stores and warehouses. The supply chain network encompasses two manufacturing and distribution sites.

Client Objective

The company's customer base is highly diversified relative to size and network, order and delivery requirements, order size, seasonal fluctuations, and customer expectations for price "incentives". The company recognized the old adage that treating all customers the same just does not work any longer—the company wanted to begin the journey of understanding their cost structure with particular focus on warehousing, order fulfillment, transportation, and customer service (order management).

Results

1. Defined an approach to create activity-based costing for the warehousing, order fulfillment (distribution), transportation, and customer service (order management) functions. The process included the establishment of a cost matrix by function, order/delivery type and 15 modified channel (retail store, mass merchandise DC), promotion versus regular business order, assembly order versus warehouse order (direct and DC cross-docked) scenarios.
2. Cost variables by function:
 - Allocations, fixed costs, and insignificant variable component
 - Percent of gross sales used as a common measurement
 - "Final" matrix rolls up to a total functional cost that can be applied to any type of customer order (assignment of appropriate matrix values)
 - Option of applying site-specific values or a total U.S. network matrix

3. A. <u>Customer Service (order management)</u>	
Fixed Costs	0.18% of Gross Sales
Regular Business Processing	0.15%
Promotional Order Processing	0.13%
B. <u>Distribution & Warehousing</u>	
Fixed Costs	1.18%
Regular Business Full Case Fulfillment	0.67%
Regular Business Split Case	1.53%
Promotion LTL/TL	0.67%
Promotion Parcel	1.17%
C. <u>Transportation</u>	
Small Package	2.7%
Less-than-truck Load	1.6%
Truck Load	0.5%
4. Variable Cost Matrix (Example: Food Chain Customer)	
Regular Business Full Case Fulfillment	3.68%
Regular Business Split Case Small Package	5.64%
Promotion, LTL, TL	3.76%
Promotion, Small Package	5.36%
Full Matrix Range	2.08% - 5.64%

Summary

The aforementioned process was the foundation for the company's strategy of moving toward developing a more involved process of segmenting customers based on their value over time and positioning the company to increase the value delivered to obtain increased customer loyalty. Evaluating individual customers' profitability is the path to customer strategic value.