SUPPLY CHAIN EDGE

Case Study

Finding a Path to Value: Supply Chain Alignment and Assessment at a Heating Equipment Manufacturer

The company is a heating equipment manufacturer created by a private equity-funded merger of two separate and very distinct market players—one focused on a small range of make-to-order products and the other offering a broad range of products with a make-to-inventory operating model.

The Business Challenge

Mergers and acquisitions comprise a major portion of many companies' growth strategies and can be a highly effective way for organizations to quickly enter new markets or gain access to strategic assets. However, as is widely acknowledged, executing a business combination effectively can be difficult: Integration challenges have derailed many a merger or acquisition, and are a primary source of failures to realize the value on which deals are based.

This manufacturer knows these challenges all too well. The significant differences between the two original firms created many challenges that blunted the new organization's performance. One firm was a small, family-run, niche player focused on making a limited range of products in response to customer orders and maintaining very low inventory levels. In contrast, the other firm offered a more extensive range of products and stocked higher levels of inventory in two separate distribution centers, which enabled it to respond quickly to a wider variety of customer demands. The integration of these two firms involved transplanting the operations and product portfolio of the make-to-inventory company to the make-to-order company's facility, which unleashed a spiral of negative consequences.

One of the more important ramifications was that the new entity now would need to provide fast service for a broad range of products and customers with virtually no inventory and a much less extensive distribution network. This, in combination with poor integration of processes such as customer service, quality assurance, and distribution following the merger, resulted in unacceptably long lead times, low quality levels, and inconsistent order fulfillment for customers. Making matters worse was the fact that the lack of integration made these processes inefficient and more costly than necessary. As a result, the company was struggling to retain customers and positively differentiate itself in the marketplace—not the scenario the original entities had envisioned when they decided to join forces.

Recognizing the situation was untenable for much longer, the company approached Supply Chain Edge for help. While company leadership initially was focused on reducing costs in its transportation network, it ultimately determined that a complete supply chain assessment would help it address the broader challenges that were undermining its ability to serve its customers and grow more profitably. However, as almost a year had elapsed since the integration of these two companies, deep experience and a significant effort would be required to get the new entity back on track.

How Supply Chain Edge Helped

One of the factors in the manufacturer's decision to hire Supply Chain Edge for this project was SCE's proprietary Supply Chain Alignment and Assessment process, which is designed to help companies identify areas for improvement across the supply chain. At the heart of the process is an easy-to-use, Web-based tool that allows SCE to gather feedback from a company's employees, suppliers, customers, and other key stakeholders on the importance and performance of

42 separate competencies that are vital to a healthy supply chain.

Working closely with the heating equipment company's leadership, SCE used the tool to survey the company's associates, customers and suppliers to gather a wide and rich collection of data on the current state of the company's supply chain and its most substantial improvement opportunities.

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The assessment certainly confirmed that the company had many shortcomings in its supply chain. But more important, the survey revealed that substantial gaps existed between the perceptions of the company's customers and those of its empl yees—meaning the company thought it was performing much better than it really was, at least in the eyes of its customers. For instance, on a one-to-seven scale where one is highly ineffective and seven is highly effective, customers said the company deserved only a 1.6 ("ineffective") for the way in which its supply chain processes and information systems accommodated last-minute customer requests. The average rating given to this capability by employees was a 3.6 ("neither ineffective nor effective"). Similarly, customers stated the company's ongoing compression of order fulfillment cycle time only merited a 1.6. In comparison, employees rated this capability an average of 3.4 on the same scale. And in terms of fulfillment efficiency, customers rated the company's ability to move materials through the supply chain efficiently through tight coordination with customers and suppliers an average 1.8, while employees rated it more than twice as highly (3.9).

The survey revealed the same trend in terms of the company's customer responsiveness. While customers gave an average score of 1.6 to the company's ability to understand customers' views of its performance, the company gave itself a 4.3. Similar gaps existed between customer and company ratings of the company's ability to translate customer needs into supply chain priorities and of the alignment between functions such as operations, sales, marketing, and finance. Customers also had lower opinions than employees did on the way in which the company balanced its product portfolio to meet customer requirements while minimizing complexity; the ability of the company's supply chain to translate corporate strategy into daily activities; the integration between the company's information systems and customers; and the effectiveness of those systems in enabling the company to make business decisions. In sum, the survey revealed a host of areas in which the company was disappointing its customers—and employees were not fully aware of the magnitude of the problem.

However, while the survey was an important first step in identifying potential problem areas, it could not tell the full story. To augment the survey findings, SCE conducted in-depth group and one-on-one interviews with key customers, suppliers, and employees. The customer interviews were of particular interest to the company and to the Supply Chain Edge team, which tailored its approach to focus on the specific problems—and solutions—that customers thought were most critical.

Several major themes emerged from these interviews. For instance, many customers described the company's order cycle, fulfillment and back-order management processes as inconsistent and as significantly worse than those of the competition. Customers also indicated the company's product portfolio was too large and complicated, and its communication was ineffective across the board—from co-op ads and back-orders to new products, events, customer service, and changes to SKUs and prices. Indeed, the interviews made it abundantly clear the company lacked competitive strength in every single performance metric under consideration.

Confronted with this wealth of feedback and information, the company sought clear and rapid ways of addressing these issues and protecting its position in the marketplace. Drawing on decades of experience helping manufacturers overcome similar challenges, the SCE team quickly began developing a comprehensive and prioritized improvement initiative that would help the company get its supply chain operations up to speed.

There were four elements of this plan, each of which was designed to tackle the top issues uncovered during the assessment phase of the project. One of these elements focused on the ways in which the company segmented its products and markets, and sought to alleviate customer complaints of a large and complicated product portfolio. The SCE plan laid out a go-to-market supply chain strategy based on the revenue and margin contribution of each product, seasonally adjusted for market forecasting, production, and order fulfillment ranges. This segmentation resulted in four tiers of products—A, B, C, and D—with tiers A and B generating 80 percent of the total contribution. The SCE team also devised a similar segmentation strategy for the company's customers, focusing attention on those that generated the bulk of the company's revenue and profits. SCE then worked with the company to combine these product and customer segments into one matrix that clearly depicted which were most important, and would enable the company to adjust its supply chain strategy accordingly.

To support this new customer and product segmentation more effectively, the plan called for the company to modify its order placement and management processes. Among the key changes would be providing a customer advocate and more extensive self-service options for all of the company's top 100 customers, while shifting customer service for non-top 100 customers to a third party.

The customer and product segmentation was instrumental to the second aspect of the plan, which would substantially improve the company's order fulfillment processes and enable the company to deliver class-leading cycle time, order fulfillment integrity, and delivery accuracy for its top products and customers by revenue and margin. Of course, with any ambitious plan, trade-offs are necessary, and in this case the plan called for the company to deemphasize production of those products that contributed less profit and revenue, and focus attention on the products and customers most important to the company's overall performance. The SCE team also recommended the company consider implementing dedicated regional distribution networks for these top products and empower local distribution centers to develop inventory replenishment plans, both of which would enhance the service provided to the company's top customers. And to ensure that these higher customer satisfaction and fulfillment performance levels were sustainable, SCE encouraged the company to implement a new supplier development and qualification process that would be executed for all its domestic and offshore suppliers.

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The third element of the initiative centered on improving the company's demand and sales and operation (S&OP) planning processes, which would help it further improve customer service and its overall performance. The SCE team suggested the company implement a formalized and accurate demand forecasting process for its top product segments, optimizing the balance of make-to-inventory and make-to-order items as conditions changed and its capabilities evolved. Another key recommendation was for the company to link its improved demand forecasts to a new S&OP process, which would help it ensure that all functions were working in concert to support the company's more intense focus on its top products and customers.

Process changes such as the preceding would go a long way toward transforming the manufacturer's ability to improve the way it served customers. However, the changes would not be sustainable—or, in some cases, even possible—without the appropriate new supporting organization and technology capabilities. One of the most important of these was a new supply chain management organization, which would provide high-quality, centralized oversight of all critical supply chain activities—including distribution, warehousing, transportation, strategic sourcing, purchasing, supplier development, qualification, performance tracking, planning, forecasting, scheduling, and customer service. With one well-run function in control of its full breadth of customer-facing processes, the company would be in a better position to provide market-leading service as conditions evolved.

Other actions recommended by SCE included creating an internal council responsible for overseeing and improving all communications the company has with customers; implementing an annual company-wide strategic planning process to ensure that major industry, market, and customer trends were reflected by the company's most important initiatives; and deploying third-party order consolidation software to improve and streamline its transportation planning and order pick processes.

Results and Benefits

While there is debate about the precise figure, various studies generally put the failure rate of mergers and acquisitions above 50 percent. In other words, more than half of all deals do not deliver the desired benefits and, in fact, actually may destroy value. Ineffective integration—technological, organizational and functional—generally is recognized as the main culprit.

Determined not to be one of these statistics, the heating manufacturer took a commendable step by not only recognizing it had an integration problem after its merger, but also by committing to doing something to fix it. Working with Supply Chain Edge, the company was able to use SCE's Supply Chain Alignment and Assessment process to discover the sources of the problem and develop detailed, concrete improvement plans that reflected the priorities of the company's most important stakeholders. Armed with this detailed roadmap, the company is now in a position to invest its time, energy, and resources in high-value supply chain improvement programs that can help it deliver greater value to its customers and achieve sharper market differentiation.

About Supply Chain Edge

Supply Chain Edge is a team of seasoned supply chain specialists who are highly skilled in identifying, quantifying, and capitalizing on opportunities that drive performance improvements in key areas such as business growth, earnings per share, return on capital, margins, cash-to-cash cycle times, and customer service.

Supply Chain Edge is unique in two important ways: Our extensive experience in numerous supply chain initiatives with dozens of companies enables us to bring best practices used by other enterprises to every project while working collaboratively with a client's existing internal talent. And, we don't simply advise clients what they should do, but instead, help them execute more effectively and efficiently to realize tangible, quantifiable financial gain.

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Maximize Your Profits and Increase Your Competitive Edge. Supply Chain Edge is a team of experienced supply chain advisors. SCE delivers improvements to key business metrics such as business growth, earnings per share, margins, return on capital, cash-to-cash cycle times, and expanded margins and profits to those clients we serve.