

POLLEN

SKU PROFITABILITY

**FROM INCREASED  
TRANSPARENCY COMES  
ACTIONABLE INSIGHT**

MARCH 2020



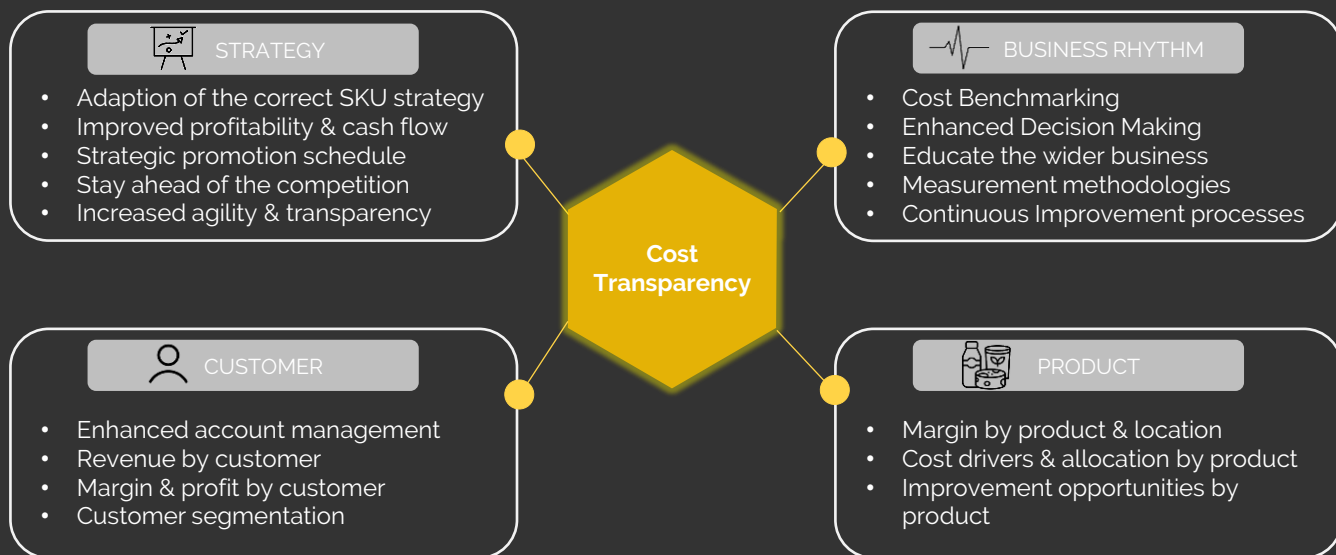
# INTRODUCTION BACKGROUND

## SETTING THE SCENE

In today's highly competitive and volatile marketplaces, the need for companies to identify and understand which of their SKU's and customers are profitable or not has never been more relevant. In finding the optimum balance between the value of variety and the costs of complexity, companies need to understand the economics on both the demand and the supply side; in terms of, what are the drivers of complexity and the relative costs for each SKU? Through growth, expansion and other factors, the task of measuring profitability often becomes blurred and buried through confusion, misallocation of costs and having reporting structures that are setup primarily designed for purposes other than profitability; such as meeting regulatory requirements or cost budgets.

The solution is to adopt a structured, methodical approach to building a dynamic profitability model. In doing so and by applying the correct thinking to the SKU portfolio, customer segmentation & channel management, companies can deliver pricing strategies and optimisation models needed to price for value & profitability.

## BENEFITS TO A COMPANY





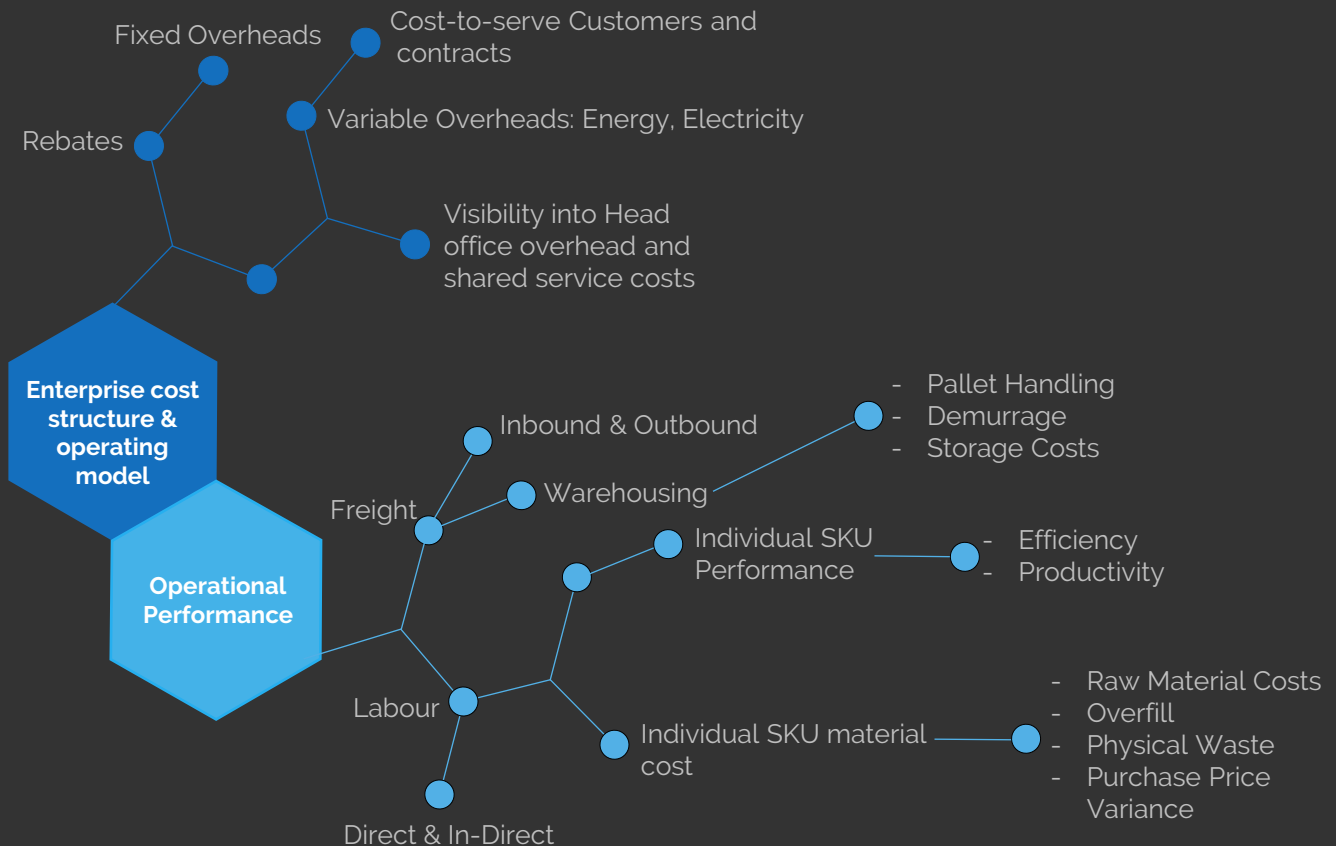
# UNCOVERING THE COMPLEXITY

## DIFFICULTIES COMPANIES FACE

This scenario is not uncommon. The apparently simple, certainly critical and rarely achieved task of accurately calculating true SKU profitability is often lost in a myriad of outdated cost allocations. Companies can measure revenue but not the profit associated with the product or client group. This in turn means that decisions about what to sell, in which markets, to which customers and at what price is based on partially inaccurate information. Without one single version of the truth or structural method to allocate large bucket of costs, they can be arbitrary and again; inaccurate.

A combinations of factors such as, **globalisation**, years of **consolidation**, **complex supply chains** and **multiple business lines** have left companies fragmented with a disparate array of financial systems and costing methods.

If the bottom up allocation of costs to products is not visible, you're potentially, and cynically, almost certainly losing money on sales you do not know about. This seems a simple formula, however business' reporting structures and cost centres are not set-up for nor designed around the value chain.



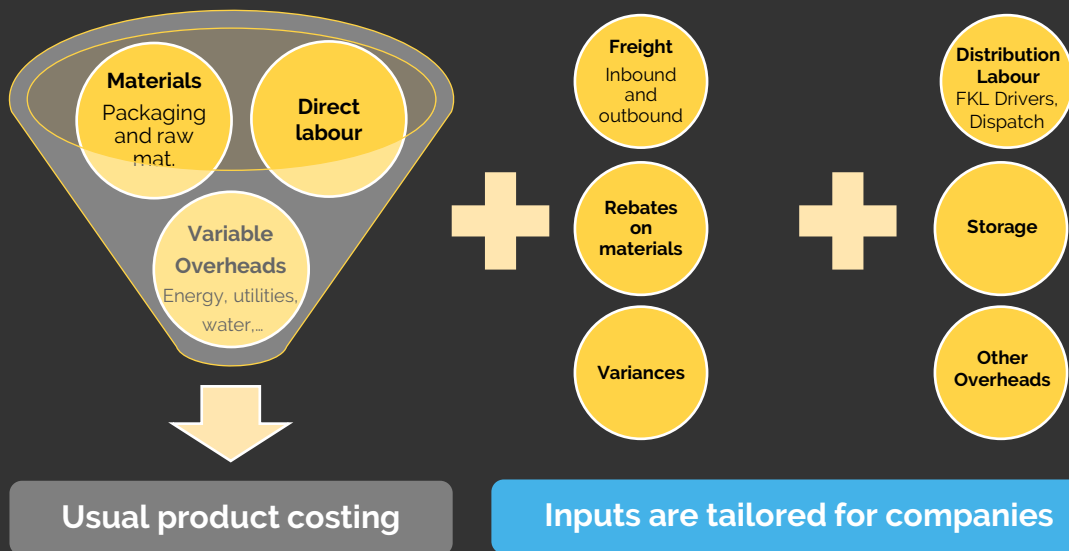


# OUR SOLUTION

## BUILDING A ROBUST AND DYNAMIC COSTING

Utilising a bottom up approach unlocks the ability to root out unnecessary and costly complexity. In identifying true contribution and profitability, companies must apply granular assessments to individual components across the value chain so as to understand the impact of customisation or scale on the cost profiles of each product.

The bottom up approach is a deep dive into the backbone of an operation, building a detailed model of cost allocations on the relevant cost buckets such as:



Generally speaking, the information is available within a business' current data sets, it is a question of understanding these sources, cleaning them (or updating) and allocating to the correct element of the value chain

From a macro level, businesses have a very good handle on profitability. P&L accounting offers little opportunity to hide bottom line profitability, however allocating costs to the wrong buckets can allow certain parts of the P&L to seem more attractive/undesirable. That being said, at an EBIT level these costs will have to be accounted for through variances or overhead allocation.

True visibility of costs will make sense of the variances and cost allocations within the P&L. The top down financial reporting will validate that the bottom up analysis has included everything. Combining the two approached brings to light the true performance of the business.

The power of this approach is to then leverage the information to determine accurate financial forecasts and understand how to influence profit margin growth. Integration of this clarity into a businesses S&OP process is a powerful tool to driving actionable decision making and strategy based on profitability.



# ROADMAP TO SKU ENLIGHTENMENT

## METHODOLOGY

Setting up a structural approach that embeds a cross-functional capability supported by the right tools and methodologies is key to unlocking your value chain and generating dynamic costings. Once the heavy lifting of setting up the structure is installed, strategic decision making can begin. Not once; but continually.

That said, there are **4 main steps** to follow to ensure the optimum outcome:

### Build Site Master Data

1. Source relevant company data (minimum 12-month period)
2. Compile database for:
  - SKU Master Data
  - Asset Master Data
3. Validate datasets accuracy with relevant people
4. Categorise data into groups (e.g. assets) based on similarities if necessary

### Build Dynamic model & validate against P&L

1. Identify the most appropriate methodology to allocate costs to SKU's
2. Calculate the total costs of each bucket (e.g. material & labour) extrapolated over 12 months
3. Sense-check and Identify variances to P&L
4. Understand and adjust model to bridge gaps to P&L if required.

### Perform Shopfloor data and analysis collection

1. Perform shopfloor studies to gather accurate data regarding:
  - Direct Labour
  - Actual Speeds and throughput
  - Changeover times & types
  - Waste & overfill
  - Indirect Labour
2. Perform spot checks to validate other information where necessary

### Identify improvement opportunities

1. Identify margin targets by SKU
2. Compare model costs to financial standards with costing methodology improvements
3. Calculate savings from improvements identified
4. Cross-reference with CAPEX and site plans



# MINING & LENSES

SKU profitability analytics is critical to determining the correct strategic choices for a business such as price, cost, volume of product mix.

Identifying the right strategic choice can be confusing and if not underpinned with the right information can be damaging to the business. Bottom up, accurate SKU profitability can unlock confidence in making the right decisions.

Through application of lenses and categorisation of SKUs the analytics can ensure the correct approach is applied. The lenses to review a businesses service offering are typically:

- SKU
- Product Group
- Customer
- Channel/Location

In order to understand the right approach, all lenses need to be considered. A SKU lens might initially show products that are not profitable, however when applying a customer lens, it is identified that this is driven by one specific customer. The correct action can then turn this SKU profitable.



Typically, SKUs within product groups will have similar operational processes. This means that application of focused process improvement can raise the profitability of the whole product group. Applying the correct product lens will help with the below:

- Optimising promotional activities by allocating to high margin products i.e. Which products should we promote?
- Change your pricing structure suited to product portfolios
- Identify potentially important customer segments for growth that had not been targeted before
- Are there products at the tail that can be rationalised or deleted?

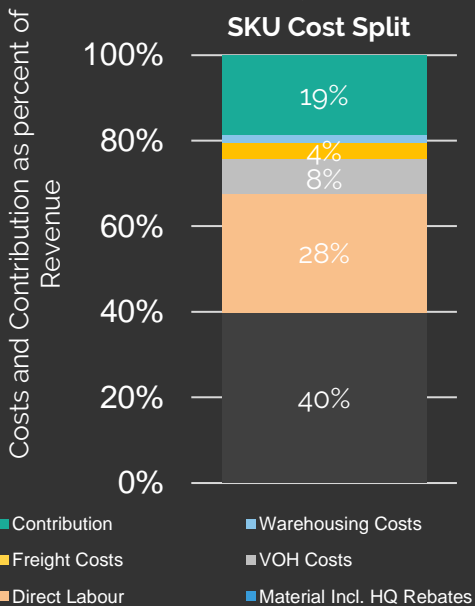
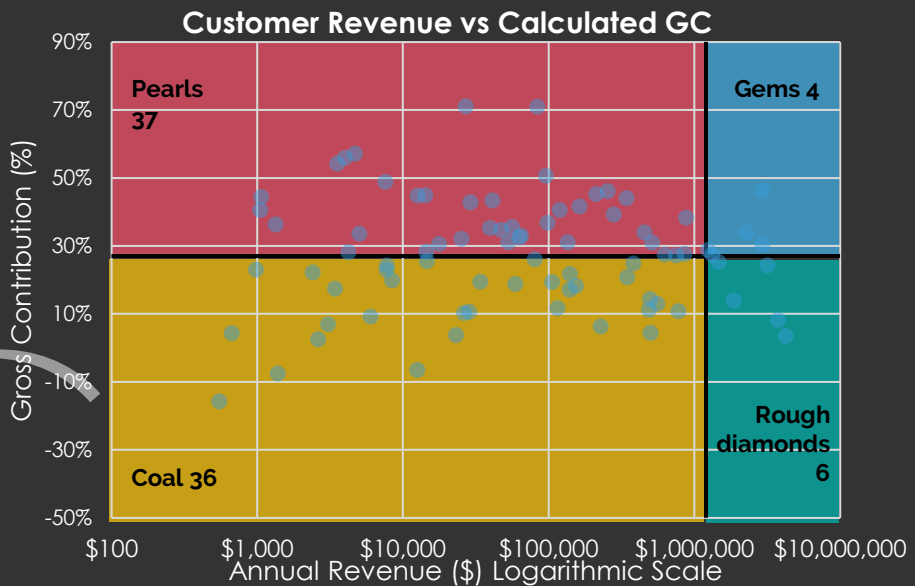


# ACTIONABLE DECISION MAKING

In deriving the ability to empower leadership within an organization to make decisions in the firms best interests, they must first have a detailed understanding of their cost structure and drivers of cost, where their resources can be best utilized to their advantage, how to price and promote products to drive profitable growth. This will then position a company to fulfill their growth agenda and shape their future.

This should be underpinned with the correct business rhythm structure in place and a decision support model to action information on:

- Customer Revenue
- Category Revenue
- Margin by SKU
- Profitability by SKU
- Cost Drivers
- Sales Distribution Map



- Typically, SKUs within product groups will have similar operational processes. This means that application of focused process improvement can raise the profitability of the whole product group.
- Product group cost breakdowns will be similar and when costs considered for SKUs within the group relative to each other. Insights can therefore be gained as to where to focus the improvement.

# OUT-THINK THE COMPETITION

## MAKE YOUR VISION VISUAL

The ability to create a multidimensional model whereby the distribution of costs can be allocated and actioned, empowers executives with the tool for the basis of discussion at both the strategic and tactical level.

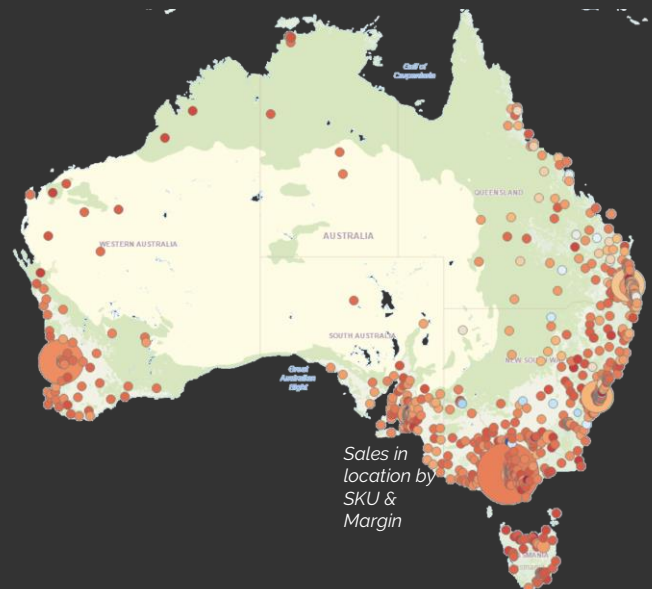
Understanding the market dynamics, based on the analysis of customer profiles, product nature and distribution strategies, is the key to designing a framework for the Pricing function that can be organized into several levels, from a fully centralized model to a fully decentralized model.

A company must be able to answer four key questions for every category to stay ahead of their competition:

- How is the category evolving- by segment, region & channel?
- What are the pockets of growth and decline?
- Which brands & SKU's are winning or losing and why?
- Where are the profit pools, and how are they shared across the value chain in different channels?

By answering these questions a company will be able to respond with greater agility to environmental and business paradigm shifts that may occur within the market, This agility and market focus will setup a company for infinite success.

SKU Categorization Real vs Standards





# CASE STUDY

Pollen Consulting Group was engaged to perform a SKU profitability analysis across 6 sites in Australia for a specialty packaging company. With the objective of **establishing a true picture of product margins**, an activity-based costing methodology was implemented and executed to build a dynamic costing model. High level output are shown below:

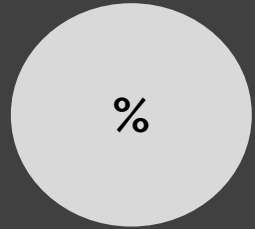
## Current State



Number of Products



Customer Base



Current Group Avg GC

## WHAT WE DELIVERED IN 6 MONTHS



1) Bottom-Up, granular assessment studies



2) Build a dynamic pricing model



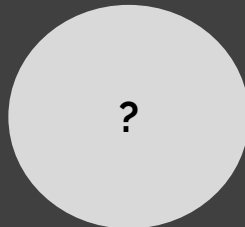
3) Validate with site & align to Operational plans



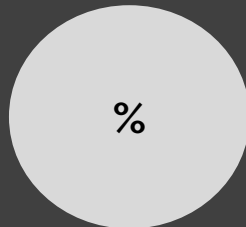
4) Train staff on new processes & methodology

× 6 Sites

## Potential Future State



New recommended number of products



New Group Avg GC



Value of Opportunities Identified

# CONTACT



## Why Pollen Consulting Group?

Being a fresh and new business, allows us to challenge the consultancy model, building a new level of competency. Pollen is driven to make a difference.

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