Foodservice Marketing Insights

presented by Franklin Foodservice Solutions

YOUR FREE MONTHLY NEWSLETTER

Sent Monthly to Over 650 Subscribers Worldwide

Volume 7, Issue 7

July, 2009

IN THIS ISSUE:

"The Quest for Foodservice Customer Profitability" - commentary by Jim Klass of MarketIntelligence, LLC regarding the importance of understanding Total Profit to Serve by customer

"Shining the Light on Foodservice Pricing Practices" - calls attention to a court case involving foodservice pricing, with a link to a brief on the topic

Greetings! I hope you're having a good summer and finding a little time to get away from work...

This month, old friend Jim Klass has written an article about his company's approach to measuring Customer Profitability. It's a great topic, and my sense is that a lot of manufacturers could benefit from having a reliable, easy-to-use tool with which to manage their business.

The second section calls attention to an interesting court case involving our business. There's a LOT more I'd like to say about this, but prudence suggests we all just keep an eye on developments and prepare for potential implications.

Thanks for reading, and as always, let me know what you think. **Tell Dave**

Dave

"Wise men profit more from fools than fools from wise men; for the wise men shun the mistakes of fools, but fools do not imitate the successes of the wise" - Unknown

"The Quest for Foodservice Customer Profitability"

Jim Klass is an industry veteran whose resume includes running a foodservice brokerage agency, and heading up the Food Industry practice for Hitachi Consulting and Booz & Co. As Managing Partner of MarketIntelligence, LLC, Jim is focused on helping manufacturers understand their Total Profit to Serve for every customer. When we spoke, JIm's approach touched on the work that I do regarding Supply Chain costs, and reflected recent conversations I've had with other colleagues regarding customer profitability.

We speculated on the degree to which foodservice manufacturers are able to calculate customer profitability, and how many actually use it to manage their business. Jim agreed to provide the following commentary; we welcome your comments by following the links at the end.

With the foodservice industry transitioning from a growth to a mature market-share driven model, foodservice companies have begun to examine how to increase profitability even as the supply chain is adding additional pressures and regulations.

What are three things would you change in your trade partner relationship?

The common responses are:
-Price
-SKU Rationalization
-Customer Profitability

The challenge is to have the knowledge to know which levers can be adjusted and how far. Profit to Serve (P2S) is an approach that provides realistic fact-based answers to this question.

"...the most profitable 20% of customers generate between 150 and 300% of total profits. The middle 70% of customers about break even, and the least profitable 10% of customers lose 50 - 200% of total profits, leaving the company with its 100% of total profits. And, often, some of the largest customers turn out to be the most unprofitable."
-Dr. Robert Kaplan
"Customer Profitability Measurement and Management"
Harvard Business School

Profit to Serve encompasses three core decisions:

Go to Market Decisions:
- Product portfolio- market basket and SKU rationalization
- Services Decisions- sales force, transportation, R&D
- Customer Portfolio- Customer tiers and value

Operational Decisions
- Customer Service
- Plant scheduling
- Procurement

Investment Decisions
- New Lines
- New Equipment
- New Plants
- Mergers & Acquisitions

An initial approach is to focus on customer profitability. The same tools and methodology can then be applied to price and SKU (Product) rationalization.

Focus first on Customer Profitability
Customer Profitability is a result of net revenues less direct costs, less indirect costs. Simple, yet complex. For foodservice manufacturers, the difficulty lies in deriving the unique rebates, discounts, incentives, and cost to serve (found in "indirect costs") for each customer (distributor AND operator). Manufacturers embarked on the journey of "costing" to get to these results. Traditional systems aggregated costs and spread them equally over all customers—a scenario that made it very difficult for manufacturers to identify exactly which customers were making them money and why.

Manufacturers seeking to improve customer profitability need visibility into the true cost to serve and profitability of each customer (direct and indirect). With traditional costing methods, the costs of services were often averaged across all customers. P2S seeks to de-average the customer, which enables manufacturers to quantify the differences among their distribution partners and operator programs. In other words, they understand how doing business with some distributors and operators is much more efficient (and profitable) than doing business with others.

Customer profitability should not merely indicate the profits derived from a retail trading partner, it should also indicate the costs of the specific activities performed for that retailer, such as “shipping”, and compare that to the category and company average. The benefit of using P2S for customer profitability is that it derives accurate analysis and provides for root cause determination. P2S takes into account the unique characteristics of a customer or the services he requires in order to accurately assign costs. A low cost to serve customer may have a single buying office, request full pallets shipped full trucks with infrequent deliveries to short distances. On the other hand, a high cost to serve customer may require store ready pallets, shipped LTL with frequent deliveries to long distances.

A bottoms -up Profit to Serve approach will provide a repeatable, realistic insight into your costs at a granular level utilizing your current information systems. This methodology will provide insights across the customer/product and order dimensions allowing a firm to understand customer behaviors and internal processes that are impacting the bottom line.

Profit to Serve:
-Incorporates cost, revenue, profitability and resource capacity/utilization in one unified model
-Preserves the link between your financials and operations via transaction level "bottoms-up" modeling
-Is easy to sustain and maintain, enabling more frequent creation of the insight
-Provides a deep level of accuracy by modeling your complexity and operational variances, resulting in both operational and financial validity
-Can be implemented and provide measurable results in a short time frame

Conclusion

A P2S system custom designed for a foodservice manufacturer accurately identifies specific costs associated with business activities. At the very least, P2S enables better communication between manufacturers and their supply chain partners. The most successful manufacturers also leverage P2S for use in pricing and SKU rationalization programs. By helping manufacturers identify and reduce costs in their supply chain, P2S paves the way for a greater efficiencies and profitability.

The benefits of an effective Profit to Serve practice are significant. A McKinsey report on pricing estimates that the average 5% improvement in return on sales from improved pricing creates $1.5 billion in additional value over 5 years for the average S&P 500 company. In today's tough economic climate companies cannot afford to leave any potential revenue on the table. The technology and expert advice exists today to help drive better profit decisions tomorrow.

If you're interested in learning more, please contact Jim Klass of MarketIntelligence,LLC, at 704-562-9794.

"We all know here that the law is the most powerful of schools for the imagination. No poet ever interpreted nature as freely as the lawyer interprets the truth." - Jean Giraudoux

---

"Shining the Light on Foodservice Pricing Practices"

There is a fascinating case winding its way through the courts right now. This case involves a single distributor calling into question the pricing practices of a single manufacturer supplier, as it pertains to discounts offered to a large contract feeder. But the practices in question are not unique to these companies, and I believe the ultimate outcome of this case will have implications for virtually all readers of Foodservice Marketing Insights.

A legal firm has prepared a brief for IFDA; if you haven't seen it yet, I suggest you **click here** to read it.

I'm not a lawyer. But it looks like if the judge's decision stands, a lot of companies will have to rethink their pricing strategies, including how they view the various classes of trade. Stay tuned.

Comments? Questions? Further Thoughts? Criticism? All are welcome at **Tell Dave**

My Website: **Franklin FS Solutions**