Thoughts on quantifying the <u>benefits</u> of trimming your product line

Stirring the Pot

What's a "SKUWORTH?"

Lately I've been hearing and reading that a lot of manufacturers have "SKU Rationalization" as one of their initiatives for 2017. And it always makes me chuckle to remember a friend who said "every time we try to do a SKU Rationalization project, it ends up being a *SKU Justification* project!"

As we've written before, the major hurdle to implementing a successful SKURAT project is the fact that it's hard to see the benefit of eliminating products, but it's really easy to see the cost of lost revenue, margin, and disappointed customers. It seems that if we could just *quantify the benefits* of managing fewer SKUs as well as we can quantify the downsides, these projects would be easier to swallow!

So what's the math? How do you put a number on the <u>cost savings</u> associated with SKU Rationalization so you can balance it against the costs?

We've never done a formal study, but we'd start by identifying the cost drivers or activities associated with managing your portfolio of products (a better term than "SKUs" but we'll use SKUs from here on out because everyone else does….)

A partial list would include:

- Sales forecasting
- Inventory management
- Maintenance of specifications (packaging, palletizing, ingredient labels, nutritionals, etc.)
- Pricing
- Management of packaging (ordering, warehousing, managing inventory)
- Management of ingredients (as above)
- Assigning warehouse slots
- Labeling (ensuring accuracy as well as maintaining label inventory)
- Marketing images and materials
- All other GS1 requirements
- ….this is probably half of the list; Manufacturing and Supply Chain folks could round it out

From here, we'd calculate or estimate the number of hours spent on these activities, with the associated cost. And the first eye-opener would be to compare it to Gross Margin for the entire portfolio just to establish a baseline and get everyone on the same page.

Our instinct would then be to divide that cost number by the total number of Finished Goods SKUs in order to come up with that elusive "Cost per SKU." But be careful- the Sales Guy in me knows that someone will say "Great! Let's add more products and get the Cost per SKU down!"

And this brings up Hurdle #2. The costs of managing a product portfolio aren't fixed, but they aren't exactly variable, either, are they?

This leads to what some might call "creeping incrementalism." Sales and Marketing routinely add 5, 10, or 20 new products at a time, and no one asks for a headcount increase to handle the workload. But over time the burden gets too heavy, Operations calls a timeout and asks for a reduction of 100 or more SKUs, and the fan gets dirty all over again.

The cost of complexity is even more difficult to quantify, but it's very real. More SKUs mean more production line changeovers with resulting downtime and reduced output. More SKU's mean more time and cost to manage warehouse storage and handling operations.

And what about the diluted focus for Marketing, Sales Managers, Brokers, and Distributors? An overgrown garden hides all of the prize plants, while a well-tended garden shows them off. Similarly, an overly complex product portfolio (price list, food show booth, sales presentation, etc.) can overwhelm the senses and distract the customer from seeing what you want him to see.

SKU Rationalization projects (or as I like to call them, Product Line Optimization Projects) will never be a simple math exercise. There are strategic reasons to keep products that look like losers, and there is always hope that with a few tweaks or 30 days of Sales focus, a struggling product line can turn into a winner. And the emotional attachment of some customers and sales people (and sometimes CEOs) to certain products often comes into play as well!

But I believe that your next Product Line Optimization initiative will go a lot smoother, with better results, if the Operations side can make a solid financial case for streamlining. Without it, you'll probably end up with "SKU Justification" all over again.

That's what I think; what do <u>you</u> think? Is your company able to "see" the financial benefits of trimming the product line? Do Marketing and Sales buy into the math? Or do you go through the same wheel-spinning every time?

Tell Dave