WHITE PAPER

Connecting supply chain planning to profitability

What collaboration between supply chain and finance can achieve.

In today's unpredictable business environment, companies that connect supply chain and finance planning achieve faster growth and competitive advantage.

Market unpredictability, rising globalization, and the relentless pace of innovation driven by the informed consumer have forever changed the business landscape for manufacturers. As those changes have developed (and continue to shapeshift), the dynamic between supply chain and finance has evolved as well: while the two departments have always been fundamentally linked, the way in which they engage has been irrevocably altered.

In the midst of the 2007-08 financial crisis, cost-cutting emerged as an imperative for most companies, and finance executives viewed the supply chain as a top target for reductions for obvious reasons—at any given time, an average manufacturer can see up to 45 percent of its working capital tied up in the supply chain. For many companies, reducing those costs became essential to survival during the economic downturn. And while the global economy has recovered, companies have continued to keep supply chains as lean as possible to maximize profits.

Creating a leaner and more cost-effective supply chain requires achieving true collaboration by connecting supply chain and finance across data, people, and plans in order to achieve improved visibility to solve some tough challenges, including:

- Aligning **financial forecasts** with **sales and operations planning (S&OP)** and **supply chain planning**
- Reducing **inventory costs** while **meeting service levels**
- Achieving **strategic sourcing**, with profitability as the key financial metric known as **cost-effective sourcing**
- Ensuring effective planning, budgeting, execution, and measurement of **trade promotion management** activities

This paper addresses the processes to tackle these challenges and the tremendous untapped opportunity to leverage technology. However, despite the benefits of collaboration, only 26 percent of finance executives and 21 percent of supply chain executives **surveyed by Ernst & Young** (EY) say their CFO's contribution to the supply chain is collaborative. But with technology-enabled collaboration delivering real-time, actionable insights, supply chain and finance teams can work together to increase profitability and effectiveness by creating an environment where they can gain clarity on demand, cost-effectively ensure supply, optimize trade promotion management, and accurately forecast revenues.

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>
> - Ernst & Young

Why does finance need visibility into supply chain?

Business and market volatility are here to stay—and leading companies know that managing the financial risks associated with that volatility requires the supply chain strategy to stay in lockstep with their overall business and financial goals. The need for alignment across the business gives supply chain leaders a front seat at the executive table while their peers in finance saw a new purview emerge: Leading finance executives today have moved beyond traditional transactional roles—they now also assume responsibility for bolstering financial performance by uncovering inefficiencies within the organization and championing effective business processes.

As a result, supply chain and finance executives now have the opportunity to collaborate on a level that surpasses traditional monitoring and reporting in four key areas, according to EY's survey, including:

- Creating consistency across the supply chain, business, and corporate strategy
- Supporting and challenging investment choices
- Monitoring and enhancing performance
- Managing risk and business continuity

Companies that have connected their supply chain and finance planning reap the rewards. The survey also found that 48 percent of companies with established "business partnering" relationships between finance and supply chain reported EBITDA growth of more than 5 percent during the prior year. In contrast, only 22 percent of companies in which finance leaders have a more traditional, detached relationship with supply chain executives achieve similar results.

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Finance's responsibilities stretch across multiple areas of supply chain and include:

- Directly supporting optimal sourcing
- Partnering with retail teams in vendor negotiations to drive incremental profitability through reduced freight costs and increased freight revenues
- Partnering with research scientists and economists to build inventory valuation and optimization models
- Supporting vendor selection programs that influence nearly all buying decisions for the business, resulting in multiple decisions daily and considerable monthly revenue
- Supporting new technology programs that use inventory management to improve customer experience and financial performance
- Reviewing and validating economic models and analytics to ensure that initiatives are traceable to financial metrics and resource allocations are justified
- Developing financial metrics based on statistical modeling and simulation techniques to audit initiatives
- Preparing financial updates, including relevant analyses versus prior periods, providing forecasts/budgets, and examining associated risk/opportunities with respect to technology resources

"We achieved a level of integration among supply chain commercial and finance planning workstreams at a level not achievable before Anaplan. We can now look at what drives the profitability of a channel, a SKU, a customer on a monthly basis. And the data and information is available to decision-makers so they can quickly make decisions beneficial to the company. It guides actions."

- Director, Supply Chain Finance, Del Monte

Align financial forecasts with demand planning and S&OP

Predicting the future has never been easy. But it was a lot simpler when past events were the best indicator of future events. Today, only uncertainty is guaranteed. Using last year's events as a basis to plan for what will happen in the current year can be a recipe for disaster as demand patterns can vary wildly from week to week and month to month, year over year. To match the pace of change, planning and forecasting processes that used to be done annually or quarterly now must to be conducted monthly and weekly in order to stay competitive.

But a faster-paced planning process becomes nearly irrelevant if visibility is lacking and information is latent. In the traditional monthly S&OP process, it can take three weeks to address events that took place the prior month. As a result, demand planning based on that information is already obsolete—demand has likely already shifted by the time planning is completed. In turn, financial forecasting, which relies on the demand plan, becomes unreliable. Without a real-time, connected, and single view of demand, responding nimbly to disruptions when they occur—and accurately predicting revenue—is impossible.

The cash-up process that connects supply chain and finance

The potential perils of disconnected planning are readily apparent when examining the relationship between finance's cash-up process and S&OP. Typically used by consumer packaged goods (CPG) companies, the cash-up process enables finance to develop a financial forecast based on the rates and volume of goods sold in the market and compare that against supply chain's SKU forecast. Planners then identify gaps and assess them as risks or opportunities. Cash-ups are done on a monthly basis to recalibrate as needed in response to fluctuations in rates and volumes that occur because of outside factors.

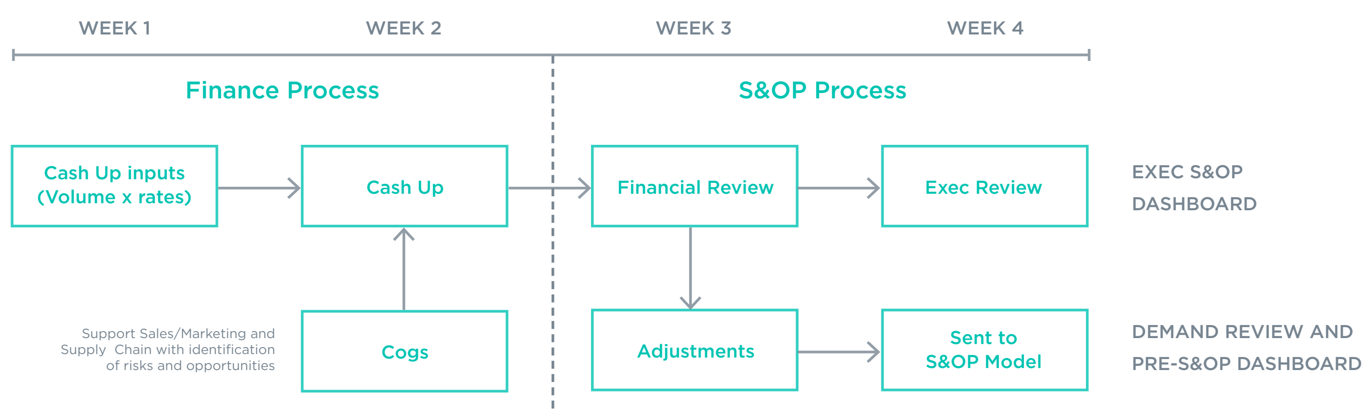
The cash-up process can be summarized in a few steps: SKU volumes are multiplied with their respective rates and then summed up to derive a financial forecast each month. Brand-level summary of this activity is then published to validate and justify marketing investments into the P&L and ensure that the company is profitable each month with moving rates, volumes, and costs.

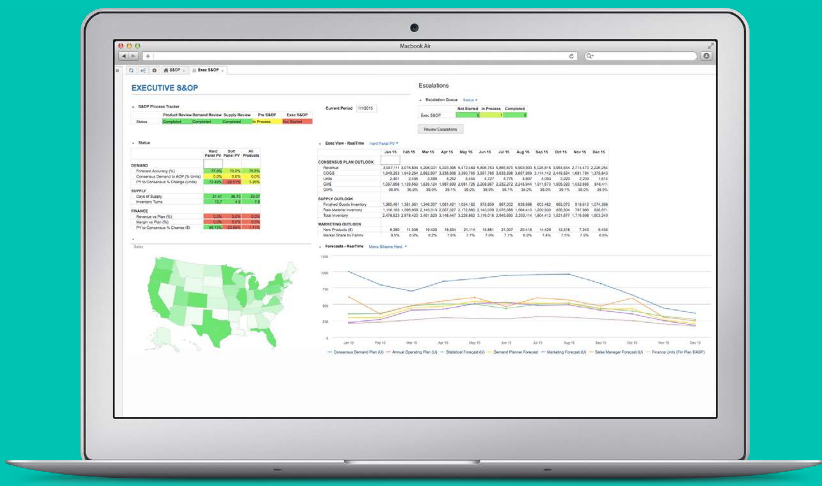
The cash-up process begins in earnest when the results of the loaded data and transformed data from calculation are generated and distributed. That data output is then validated, analyzed, and reported. The finance team uses the report to identify risk and opportunities for sales, marketing, and supply chain. Marketing investments are then consolidated into P&L.

The cash-up process generates data that would support an accurate S&OP process, both of which occur on a monthly basis. But the output of each is typically finalized in week three of the month. When the processes are completed at the same time, the business can't benefit from the data generated from the other.

A connected planning environment assimilates the data and analysis outputs from the cash-up process and seamlessly flows them into S&OP. By timing the cash-up process so that its insights inform S&OP, companies can close the loop between sales, marketing, operations, supply chain, and finance to facilitate operational and financial modeling and analysis.

A typical cash-up flow diagram





Cash-up process in a connected planning environment

Connecting S&OP with financial planning processes like cash-ups create a competitive advantage by enabling users to:

- Respond faster to fluctuating supply, demand, and business volatility
- Recognize the operational consequences of changing financial objectives that enable lower operating costs and inventory
- Increase accuracy of revenue and profitability forecasts

Reduce inventory while meeting service levels

The ways in which supply chain and finance are measured on performance often set them up to have opposing goals that undermine each other's effectiveness. For example, supply chain is tasked with ensuring product is available at the right place and the right time. When supply chain leaders work to safeguard supply at the expense of efficiency, inventory stockpiles can occur that tie up working capital. That loss of working capital prevents finance from meeting its cash flow targets.

From the finance perspective:

- Excess inventory = Low working capital
- Excess inventory (DOI) = High costs
- Excess inventory = Negative impact on operating margins
- Excess inventory = Imbalance in supply chain network
- Excess inventory = Negative impact on market capitalization

From the supply chain perspective:

- Inventory is the buffer for supply chain
- Inventory is the shock absorber between demand and supply volatility

It's clear how inventory levels can create conflict between supply chain and finance. Poorly managed inventory can make or break a company—no matter how large it is.

Strategic sourcing with profitability as the key financial metric

Clashing objectives also present themselves in the sourcing arena. The supply chain network has to ensure a steady flow of product—and in industries like consumer electronics and fast-moving consumer goods (FMCG), suppliers can be numerous and globally dispersed. Gaining visibility into suppliers' capacity, delivery windows, and price fluctuations remains a daunting task for many manufacturers. The still-pervasive practice of managing supplier data and relationships via spreadsheets creates inevitable cost inefficiencies that reverberate across the finance team's profitability goals.

Additionally, wildly fluctuating commodity capacity and prices in recent years have compounded sourcing challenges. Raw materials sourcing is an example where inefficiencies in inventory management and sourcing most readily demonstrate their detrimental effects on financial and operational success.

Given that price serves as the primary decision-making factor in most companies' sourcing strategies, many buyers in the supply chain organization second-guess purchasing decisions in the face of unstable costs. In this environment, determining timing on raw materials purchasing can feel like high-stakes gambling. Timing and price aren't the only factors—the sourcing process also entails determining how long to lock in a price and assuming a secondary position if pricing levels drop below the locked-in price.

Perhaps most importantly, deciding which suppliers to source from and how to gauge their performance on price, capacity, and delivery requires ongoing diligence. Because of their own profit-margin targets, finance also places pressure on supply chain to deliver best-cost options. This creates a breeding ground for adversarial relationships.

When this occurs, how can supply chain and finance move toward a collaborative model with shared goals? Elevating supply chain performance and protecting profit margins requires raw materials sourcing and inventory optimization strategies that connect finance and the end-to-end supply chain on the same platform, working from the same real-time data.

Consider a common example for many manufacturers that can have two starkly different outcomes depending upon how the issue is addressed: **In order to resolve an imminent working capital deficit, the finance department institutes a policy to decrease inventory across the company.**

In the typical response, supply chain works with suppliers to reduce order volumes while increasing trade and promotion efforts. As a result, volume discounts the company previously enjoyed from suppliers vanish. The promotional efforts create markdowns that increase orders, leading to less-than-truckload shipments that elevate transportation costs. The effort to release working capital succeeds, but at the expense of higher costs and lower profit margins.

However, when supply chain and finance have a collaborative relationship supported by technology that delivers a connected, single view of accurate supply and demand forecasts and constraints, then the response looks much different. Supply chain and finance both recognize that inventory needs to be cut. Using data generated from S&OP and demand planning analytics, supply chain identifies products that can sustain service levels while decreasing inventory that ties up working capital. At the same time, purchasing patterns from customers are analyzed to determine optimal delivery cadences that reduce transportation costs.

In the later scenario, it is apparent that technology can support a collaborative relationship between supply chain and finance that drives more profitable decision-making to support departmental objectives, as well as overall business goals.

Ensure effective trade promotion management

Trade promotion management (TPM) epitomizes a clear area in which finance should be integrated into the planning, budgeting, execution, and measurement processes—especially since it is a multi-billion-dollar line item for most large CPG manufacturers (representing as much as 20 percent of revenue).

The chief goal of TPM will always be to increase consumer knowledge of products and drive demand. Today, in an increasingly competitive and unpredictable CPG marketplace, it's become even more critical to establish TPM strategies that cut through the noise and resonate with consumers. Consequently, TPM complexity has increased. Companies are now directing multiple product lines through a range of promotional activities across a variety of channels.

It's this complexity—when paired with an absence of effective supporting technology and processes—that helps drive widespread dissatisfaction for TPM activities within CPG companies despite its essential nature. Strategy&, a PWC company, published a biannual customer planning and trade management **benchmarking study** that uncovered frustrations with TPM in several areas:

- Eighty-five percent of survey respondents felt that current trade management spending is inappropriately high for the long-term health of their business
- More than 50 percent of surveyed companies believed their trade funding program is ineffective
- Respondents were largely dissatisfied with systems and tools, with 70 percent unsatisfied with current planning and execution tools, and 55 percent unsatisfied with current trade tools
- More than two-thirds of respondents indicated lack of usability and integration across tools as key focus areas for the future

Based on their survey responses and financial performance assessment, the Strategy& study identified a set of market leaders. Those leaders are reaping the financial benefits of TPM and share a common set of practices, detailed in the column to the right, that others must embrace.

Best practices by TPM leaders that reap financial benefits

Spending efficiency/effectiveness

- Leaders systematically measure and track ROI on a majority of their promotion spending. As a result, these companies have realized demonstrable improvement in the profitability of their trade spending.

Funding allocation

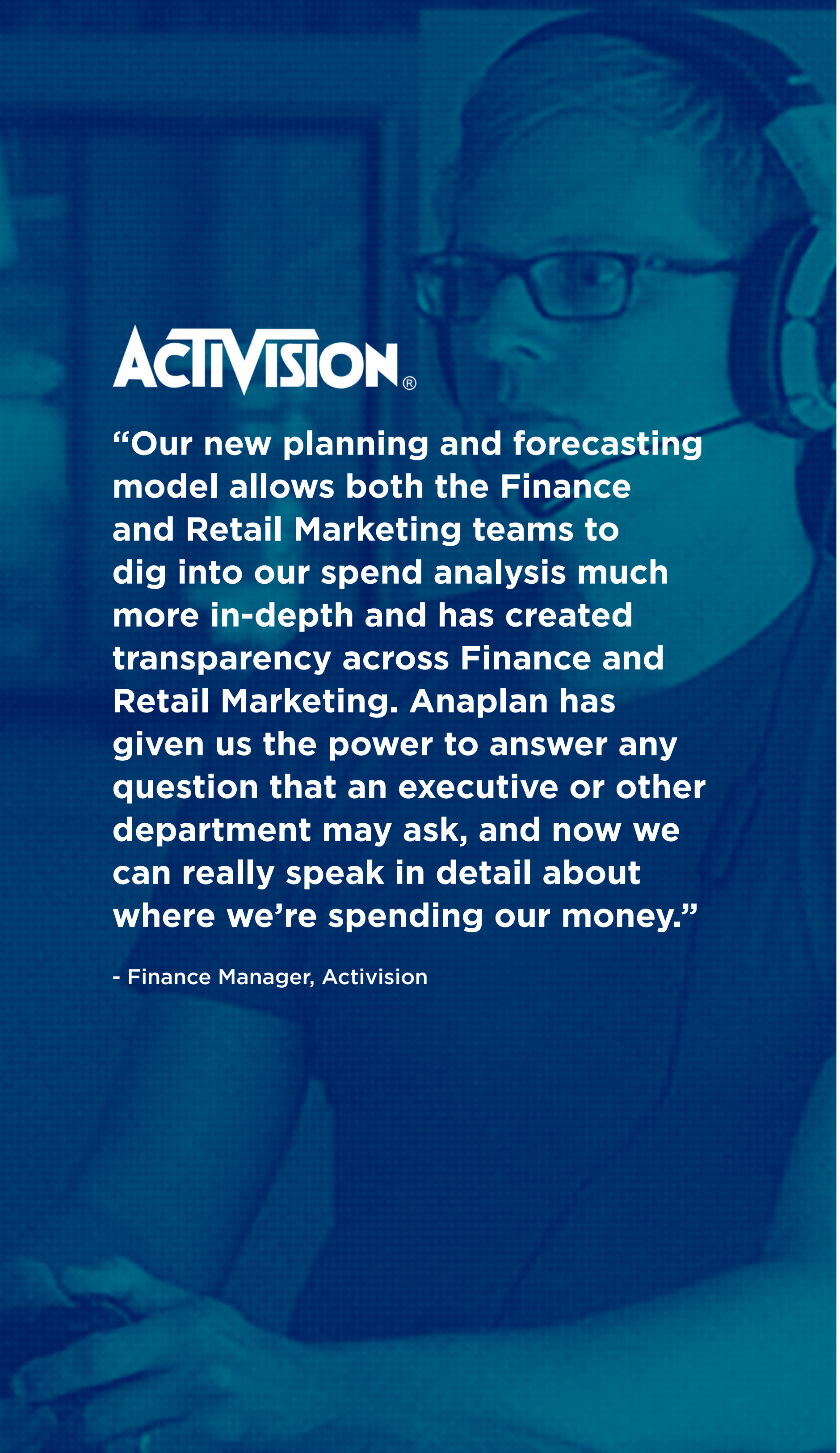
- A majority of leaders' funding programs are based on objective performance criteria as opposed to negotiated spending levels needed to achieve specific revenue targets.
- Leaders are largely transparent about their funding program criteria, citing an ability to better align objectives and build trust with retail partners.

Customer planning

- Leaders overwhelmingly focus on total volume planning, enabled by methodical processes that explicitly consider a wide range of base volume levers.
- Individual or team net revenue and profit performance is the focus of field sales incentive plans often cited as a critical enabler of better, more aggressive planning.

Technology and solutions

- Leaders have invested in a comprehensive suite of systems and tools to enable end-to-end customer planning and trade management. These investments center on simplifying the process for sales through better integration.



"Our new planning and forecasting model allows both the Finance and Retail Marketing teams to dig into our spend analysis much more in-depth and has created transparency across Finance and Retail Marketing. Anaplan has given us the power to answer any question that an executive or other department may ask, and now we can really speak in detail about where we're spending our money."

- Finance Manager, Activision

Similarly, Anaplan has seen that effective TPM decisions—on which supply chain and finance collaborate—are driven by predictive analytics and post-promotion evaluation. If these practices are inadequately constructed, disbursement data will be error-prone or misaligned with promotion events, and accurate analysis of a promotion's effectiveness becomes unattainable.

The ability to make more informed decisions around the volume and allocation of promotions spend are based on establishing clear promotions objectives and measuring past performance against goals. Better TPM decision-making, in turn, leads to higher net sales and improved gross margins.

Keys to ensuring a cross-functional partnership between supply chain and finance

When considering the relationship between supply chain and finance that manufacturers must establish to attain leadership status, the primary takeaway is simple: Companies that connect planning across the organization and cultivate solid business alliances between its supply chain and finance teams achieve stronger financial outcomes than those using traditional business models.

The elite group of companies achieving this status share common best practices, including:

- Establishing a single, connected planning platform for financial planning, supply chain planning, and S&OP to ensure forecasts are aligned
- Leveraging technology and collaborative processes to gain real-time visibility into the end-to-end supply chain—across lead times, supplier capacity, inventory positions, TPM performance, and other KPIs
- Identifying opportunities to respond to market changes and mitigate risks through "what-if" scenario analysis

To gain further insight into how your organization can achieve connected planning and true collaboration between supply chain and finance, request a personalized demo of the Anaplan platform.

About Anaplan

Anaplan is driving a new age of connected planning. Large and fast-growing organizations use Anaplan's cloud platform in every business function to make better-informed plans and decisions and drive faster, more effective planning processes. Anaplan also provides support, training, and planning transformation advisory services. Anaplan is a privately held company based in San Francisco with 16 offices and over 150 expert partners worldwide.

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About Workforce Insight

Workforce Insight is the world's leading workforce management and analytics firm. Workforce Insight operates each day with a purpose: To provide outcome-based, workforce management consulting, analytics and support for our clients, generating significant labor cost savings and sustainable performance gains. Our clients, including 48 of the Fortune 500, span key industries including Healthcare, Manufacturing, Consumer Services (Retail, Hospitality, Gaming), Business Services (Financial Services, Professional Services and Public Sector). With unmatched expertise across all workforce management and analytics platforms, rich industry depth and experience in more than 30 countries, Workforce Insight is the leading and most trusted workforce advisory firm.

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