



S&OP: How to Move Past Tradition

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Introduction

With the rise of the global multi-national organization, Sales and Operations Planning (S&OP) increases in importance. It is a way to align and drive balance within the organization to align strategy to execution.

Traditional approaches are not sufficient. For the past three decades, S&OP focused on volume-based decisions. Today, there is the opportunity to shift the discussion from volume (quantity available) to value (price and revenue management). With 90% of industry sectors losing ground on operating margin over the last decade, the shift in the S&OP process from volume to value is critical. As companies move from a regional to global focus, this capability increases in importance. However, it requires new capabilities in technology investments. Companies need to reskill.

The Shift from Volume to Value

The supply chain organization directly controls 70-85% of the cost of goods within a manufacturing organization. Yet, today's planning processes manage volume. Traditional technologies—Enterprise Resource Planning (ERP) and Advanced Planning Solutions (APS)—predict and plan quantities and availability. The systems are blind to margin or cost trade-offs. As a result, managing the trade-off of opportunity and risk is difficult. This capability is only found in mature processes within 1% of companies. The evolution of new planning technologies now enables the journey from volume to value possible and changes the game.

As an example, let's closely evaluate the management of commodities. With rising commodity and transportation costs, an effective S&OP process focused on value, not volume, grows in importance. While historically, labor productivity was a central focus of S&OP. Today, there is a renewed interest to connect S&OP to direct material buying to orchestrate the bill of materials.

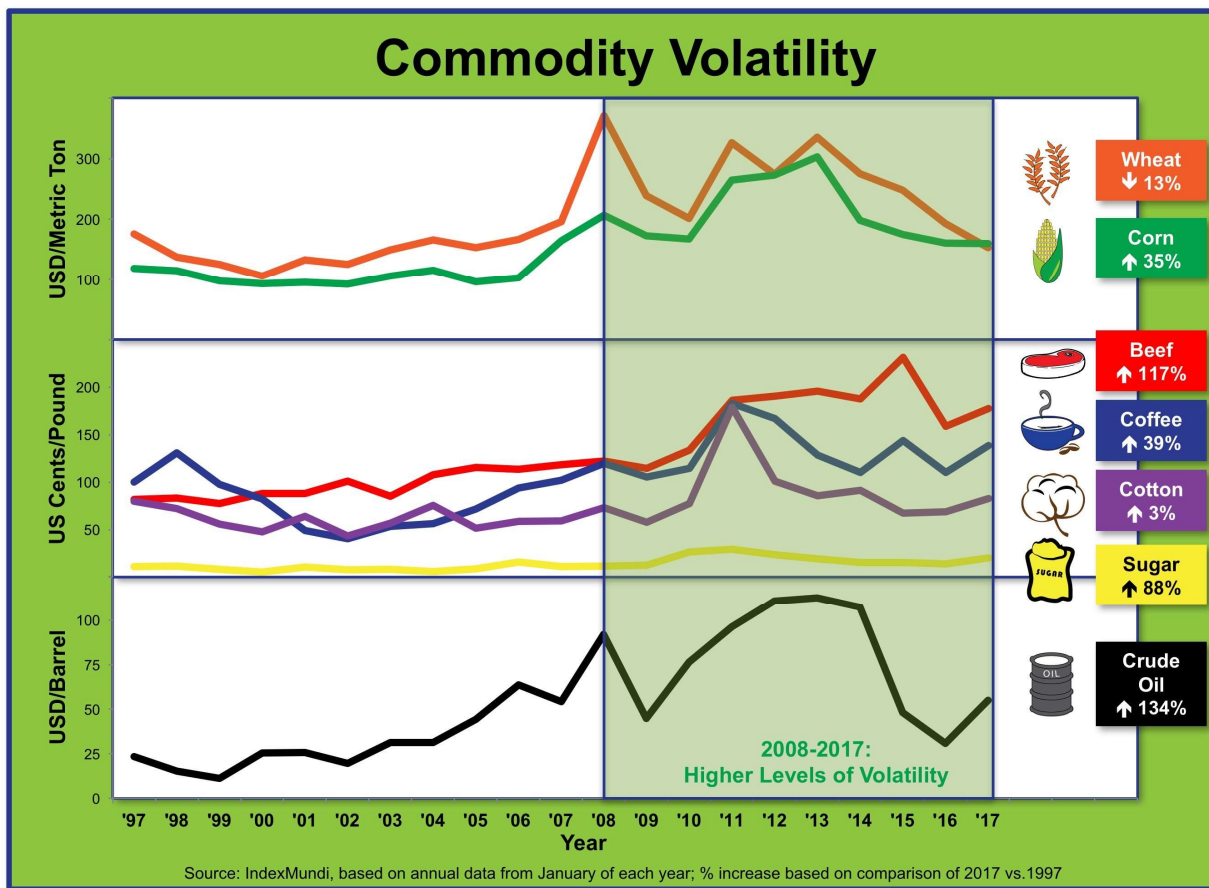
This is essential due to the increased volatility in the commodities market following the 2007 recession. In an effective S&OP process, planned orders are passed from supply planning into procurement to build commodity

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buying strategies. This is critical since commodity volatility is the highest since World War II. This trend is shown in Figure 1. Managing this volatility requires alignment between finance, procurement and manufacturing. The discussion of buying strategies as an input into cross-functional S&OP processes opens up new levels of value.

Figure 1. Commodity Volatility



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S&OP A Driver of Growth?

As growth slows to the rate of GDP, companies are asking for more. They want the supply chain leader to not only drive cost improvement, but to also improve the value of the firm. An effective S&OP process improves revenue. For many supply chain leaders, the use of the supply chain to drive growth is new. It is awkward: like walking in new shoes. The supply chain leader is more comfortable controlling costs. However, an effective S&OP process drives growth while driving value. Supply chain leaders constantly ask “What defines value in the supply chain strategy? Is it improvement in market capitalization? Price to book? Market Price to Tangible Book?” In our research, we use Price-to-Tangible Book Value (PTBV). We believe that the supply chain leader directly controls tangible book value.

To help the supply chain leader think more strategically about the role of supply chain processes in market valuation, in 2017, we analyzed the data collected in 42 quantitative studies over the past five years (2012-2016). This included 2147 respondents from manufacturing, retailing, distribution and third-party logistics companies. We tested 61 factors and found four correlations. (These are shown in Figure 2.) Companies with an effective center of supply chain excellence and strong Sales and Operations Planning processes outperform their industry peer group on Market Price to Tangible Book. In addition, companies with lower levels of business pain on supplier reliability and higher performance on supply chain visibility with second and third tier suppliers also perform better. In contrast, we did not find a correlation to specific technology choices—number of ERP instances or technology selection.

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Figure 2. S&OP Maturity and the Correlation to Price to Tangible Book Value (PTBV)



Building an Effective S&OP Process

So, how do companies get started? The first step is defining supply chain excellence. The second is driving organizational alignment. This is easier said than done. A balanced portfolio of key KPIs that are common across the organization across source, make and deliver out-performs a functional approach. To maximize value, the efforts should align to enterprise metrics that transcend functional boundaries. This includes growth, operating margin, inventory turns, customer service (on time and in-full service) and Return on Invested Capital (ROIC).

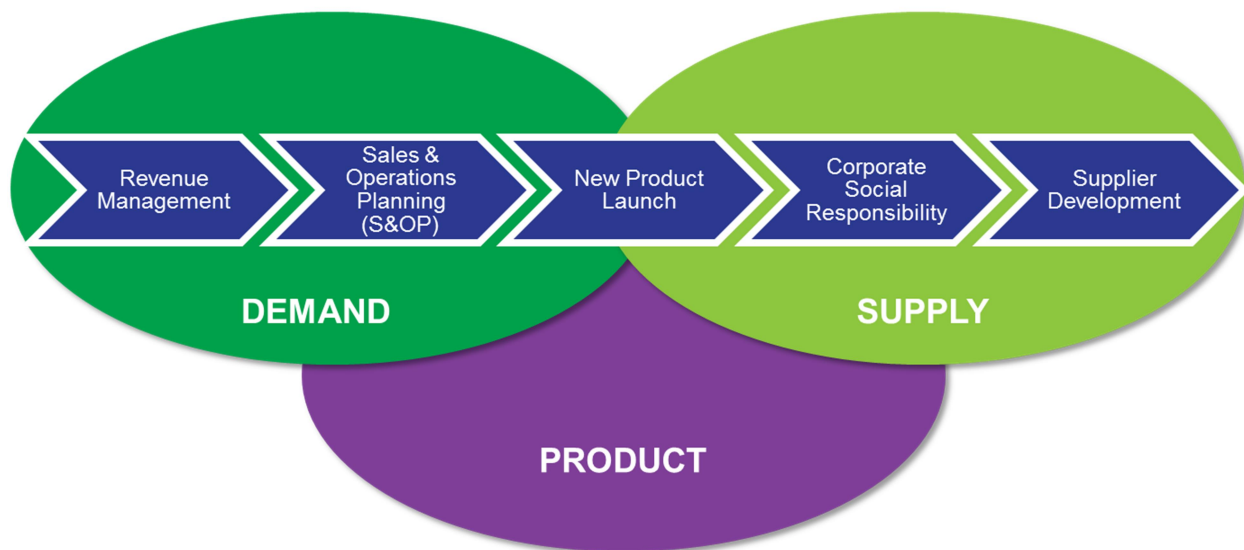
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When companies allow the functions of transportation, manufacturing and procurement to set their own targets, they will sub-optimize the supply chain. The reason? Today, only 12% of companies can quickly analyze alternatives cross-functionally to understand the lowest total cost alternatives. Most companies measure too many metrics and the focus is on costs within the functional excellence of source, make and deliver.

The second step is to apply this definition to the implementation of (S&OP). The processes of S&OP are more successful when the team reports to a profit center manager, and when the company builds planning capabilities to examine alternatives and align on market options with a focus on this balanced scorecard. The best teams include finance leaders and collaboratively work what-if scenarios to align to the supply chain strategy.

Figure 3. Horizontal Processes



The third step is connecting S&OP across the organization into other horizontal processes as shown in Figure 3. This is very critical at the intersection of S&OP a new product launch and the connection to procurement. Supplier strategies and supplier development reduce supplier issues and improve supplier reliability.

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When we look at the building of horizontal processes, companies are stronger in the areas of new product launch, but weaker in supplier development and revenue management. The center of the supply chain is stronger than the ends. The key is alignment of all of the horizontal processes within the organization to deliver on end-to-end supply chain strategies.

Alignment: Managing the Process Dynamic

Visibility of cost and the connection to profit is critical to align financial, commercial and operational teams. The use of what-if analysis and scenario planning in new technologies allows teams to connect strategy to execution while delivering a feasible plan.

A Tough Nut to Crack

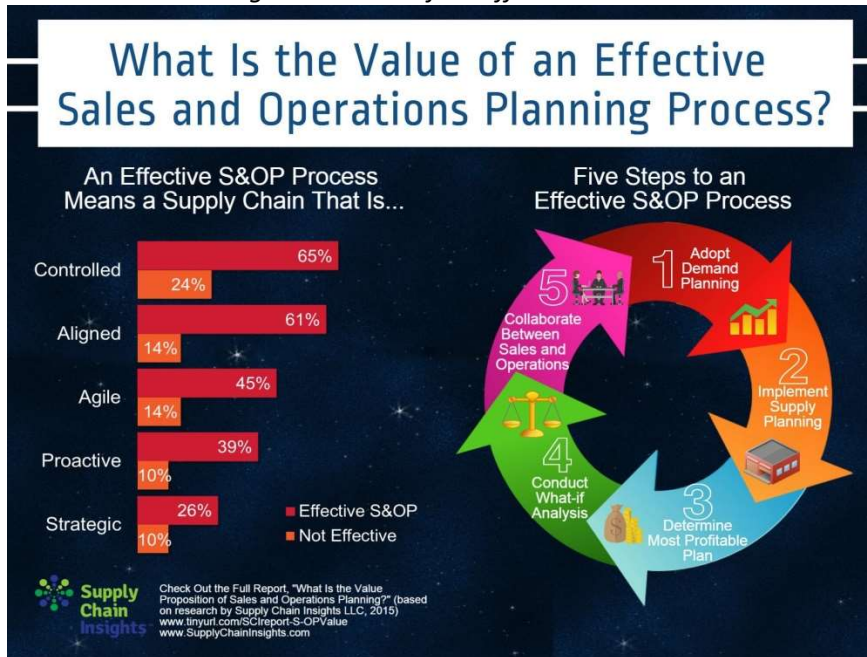
Most companies are not up to this challenge. They lack skilled resources, and too few companies have the right technologies to enable executive alignment and collaboration on the plan. Decisions are easier when the alternatives are visible. While many companies have implemented solutions for demand and supply planning, the ability to evaluate alternatives, through value based what-if scenarios, is an issue for 76% of companies.

S&OP improves organizational alignment and drives agility. With S&OP maturity, business results are more controlled, agile and aligned.

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Figure 4. Value of An Effective S&OP



What is an effective S&OP process? An effective S&OP process has three characteristics:

1. **Balance Between Sales and Operations.** In an effective S&OP process there is a balance between the "S" and the "OP" with a clear objective for the business. When the groups are not aligned and there is not balance, the results suffer.
2. **Effective Modeling.** The use of technologies to model a feasible plan is not as common as most people would like to believe. Many organizations still rely on spreadsheets with no understanding that a complex supply chain cannot be adequately modeled using a spreadsheet. The effective S&OP process is built using technologies that can yield an effective feasible plan with what-if analysis. Less than 20% of companies have this capability today. Unfortunately, the supply chain planning processes are too rigid without planning workbench capabilities to evaluate alternatives through what-if optimization.
3. **Goal Clarity.** To drive alignment, the S&OP plan needs to be guided through a balanced scorecard approach. Commercial, operational and finance teams need to own the same set of metrics and drive improvement cross-functionally

So, in a nutshell, S&OP maturity takes time and a focused effort to perfect. It happens over many years. The opportunity is to shift to drive value and power growth. Start by actively tackling the issues. While it cannot be a technology project, companies cannot achieve S&OP maturity without the use of technology. Audit your technologies to ensure that you can model price/revenue/profit and drive collaborative workflow for what-if analysis.

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About Supply Chain Insights LLC

Founded in February 2012 by Lora Cecere, [Supply Chain Insights LLC](#) is in its sixth year of operation. The Company's mission is to deliver independent, actionable, and objective advice for supply chain leaders. If you need to know which practices and technologies make the biggest difference to corporate performance, we want you to turn to us. We are a company dedicated to this research. Our goal is to help leaders understand supply chain trends, evolving technologies and which metrics matter.

About Lora Cecere



*Lora Cecere (twitter ID [@lcecere](#)) is the Founder of [Supply Chain Insights LLC](#) and the author of popular enterprise software blog [Supply Chain Shaman](#) currently read by 15,000 supply chain professionals. She also writes as a LinkedIn Influencer and is a contributor to Forbes. She has written six books. The first book, *Bricks Matter*, (co-authored with Charlie Chase) published in 2012. The second book, *The Shaman's Journal 2014*, published in September 2014; the third book, *Supply Chain Metrics That Matter*, published in December 2014; the fourth book, *The Shaman's Journal 2015*, published in August 2015, the fifth book, *The Shaman's Journal 2016*, published in June 2016 and the sixth book, *The Shaman's Journal 2017*, published in July 2017.*

*With over 16 years as a research analyst with **AMR Research, Altimeter Group, and Gartner Group** and now as the Founder of Supply Chain Insights, Lora understands supply chain. She has worked with over 600 companies on their supply chain strategy and is a frequent speaker on the evolution of supply chain processes and technologies. Her research is designed for the early adopter seeking first-mover advantage.*