Sales & Operations Planning

Creating a Formula for Success

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In discussions with business leaders around the globe we hear a common theme:

- We are getting increased demands from shareholders to improve business returns.
- Demand for products is soft.
- In spite of heavy investment in R&D, the product development process is not delivering a sufficient number of new and innovative products.
- Overly optimistic sales forecasts fail to materialize.
- We are all working harder, but with fewer results.

What these executives are missing is a methodology for generating planned, predictable performance!

In this study, we will discuss a process for addressing these issues and building a platform for delivering consistent financial returns on a long-term basis. At the end, we have provided a quick self-assessment that you can use to gauge your performance against other World Class companies that used to struggle with these same issues.

What is Sales & Operations Planning? S&OP is a senior management process that seeks to improve sales forecasts, optimize inventory, bolster the new product pipeline and improve customer relations. Often, companies have well thought out strategies and business plans, but lack the methodology for effectively executing them. S&OP's primary purpose is to convert a company's strategy into tactical plans that can be executed throughout the business.

The S&OP process creates a robust organizational framework around the core processes of the business. This framework allows the CEO to effectively communicate strategy, understand the changing dynamics of the business, and to have the organization quickly adapt to and execute smartly in the new environment. The output of the S&OP process is one set of numbers to drive the business.

On a monthly basis, the CEO sits down with his/her direct reports to update a single operating plan for the business. With this plan, they seek to bring the supply chain into alignment with demand. This reduces the reliance on excess inventory to anticipate customer orders. The balancing of demand and supply includes the new product development process. This ensures that new products and services are readily available in conjunction with marketing and promotional initiatives. Finally, the financial impact of the operational decisions just mentioned are analyzed, and if the projected results are satisfactory, the plan is approved.

Companies both large and small have successfully implemented S&OP. The list includes 92% of Fortune 500 companies and hundreds of smaller firms. They are all realizing tremendous financial benefits. *Aberdeen Group, 2007*

Proven Benefits	
Improved Forecast Accuracy	20-40%
Inventory Reductions	7-15%
Revenue Growth	2-8%
Successful Product Launches	20%

How Does it Work?

S&OP is a five-step process that is executed on a monthly basis. Where traditional management reviews have focused on past performance, usually at quarterly business reviews, the S&OP process focuses on future projections-typically out to 18 or 24 months into the future. Because S&OP focuses on integrating all core areas of the business, new products, sales & marketing, supply chain, financials, strategy deployment and Key Performance Indicators (KPI's), business leaders can quickly see if the business is executing according to plan or needs a course correction. By reviewing core process regularly on a monthly basis, executives have ample time to adjust their strategies to take advantages of changing conditions in the market.

One of the first steps is the establishment of KPI's. These help set the expectations for the business and determine how success will be measured. Organizationally, it sends the message that business will be driven by data and facts – not opinions and guesswork. To make sure an organization is focused on the right performance criteria, it is imperative that the management team cascades the KPI's to the entire organization. Employees, from the top to the bottom must understand how they contribute to the success of the business, their specific role in obtaining these goals and how their performance will be measured.

Executing the S&OP Process

Once the KPI's have been established and rolled out to the organization, the S&OP process can begin. Each of the following steps has its own unique metrics, which taken together, provide a comprehensive overview of the organizations performance.

Step 1: Product Review

The monthly S&OP process starts at the beginning of each month with a review of new products, technologies, and services. This step focuses on a company's product pipeline and the marketing initiatives required to successfully propagate the company's product portfolio and strategic mission. It is also used to measure the performance of recently launched products to ensure they are delivering the required returns. The product review also checks for alignment between the new product strategy set by senior management and actual activities taking place throughout the organization to ensure maximum value is being delivered.

Step 2: Demand Review

Building on the new product review, sales plans and marketing initiatives are combined to provide an overall revenue plan for the next 18-24 months. To maintain a high-level perspective, the various products and services are aggregated in to product families both in units and in dollars. This allows executives to see how each major segment is performing without over whelming them with massive amounts of data. It also allows process owners to quickly roll the product families together and provide a total revenue projection for the business. A key concept of S&OP from a demand perspective is that we are building a plan or commitment of what the sales & marketing organization will deliver – on time and on revenue target, versus the traditional forecast, which is a best guess of where near term sales will come in. The sales and marketing plans must be developed in dollars as well as units. Units are necessary to plan resources throughout the supply chain.

Step 3: Supply Chain Review

Once an accurate demand plan has been created and reviewed, it is compared to the existing supply plan. The supply plan is a representation of how effectively and efficiently an organizations supply chain can deliver to customer demand – both in orders on the books and future projections. The goal of the supply chain review is to balance the requirements of the demand plan and deliver product on time, at the lowest possible cost, and in the most efficient manner possible. One of the key outputs of the supply plan is a projected inventory and stocking plan. This helps determine what resources and capital will be required well in advance to effectively service the business. If projected stocking levels start to increase or decrease beyond a pre-determined level, corrective action can be taken to maintain target inventories.

Another added benefit is the increased visibility 18-24 months ahead on new products coming down the pipeline. This visibility allows planners to minimize surprises to the extended supply chain, allowing ample time for suppliers to provide raw materials and components in the most economical manner. This helps to mitigate expediting and prevent stock out situations during initial product launches.

Step 4: Financial Review

Now that demand and supply are in balance, the next step in the process is to look at the financial impact on the business. A critical question the CEO must ask is, *"are the overall revenue goals being hit and is the revenue in the proper periods?"* The goal is to identify any financial shortfalls before they adversely impact the business-while there is still time for correction. Because S&OP is a forward-looking process, it is easy to quickly generate projected financials – such as gross sales, cash flow, and pro forma financial statements. This stage of the process is called the integrated (see diagram) reconciliation. The sole purpose on this step is to determine if the business will meet its financial projections going forward. If not, then recommendations are developed to re align the organization to achieve its financial objectives.

Step 5: Management Business Review

The final stage of the process is the summary and review of the prior four processes – new product, demand, supply chain, and financial reviews. This information is consolidated into a formal presentation called the Management Business Review (MBR). Typically, this review takes place at month end. During this high-level review, each of the core areas of the business are reviewed and compared to the strategic goals and objectives of the business. A key output of the MBR is acceptance of the individual reviews by each of the process owners. It also serves to provide any required re alignment to the business plan.

Should there be a major shift in strategy; the MBR is the vehicle for disseminating that new plan to the organization. This plan is taken back to each of the core areas of the business, converted into tactical plans, and feed back down the chain of command. This strategic linkage ensures that the organization is acting in unison and can react to every changing market demands.

After all, of the five process steps are completed, the S&OP cycle starts over at the beginning of the next month. While to the un-initiated this appears to be a lot of work, those that have been successful in this process will tell you that you are already (or should be) doing these things as part of your regular business management process. Unfortunately, for organizations that do not have a structured S&OP process, it takes a lot more effort and resources to execute these actions. Most of the time key parts of the process are not operational or simply ignored. This causes a significant imbalance between the demand and supply plans. It also makes the financials less predictable and the sales planning volatile. This lack of visibility and predictability keeps CEOs up at night. Any executive that has implemented a successful S&OP process will tell you that the clarity and visibility it brings allows you to focus more on strategic issues and less on the day-to-day running of the business.

How Do I Know If My S&OP Process Is World Class?

Whether you have an S&OP process in place or not, it is always a good idea to perform periodic audits against Best In Class companies of your industry on an annual basis. It is also helpful to conduct an assessment prior to strategy development and annual budgeting exercises. This allows for key learning's to be incorporated into the strategy deployment and ensure alignment to goals for the next 12 months.

Most comparative benchmarking data is available through your industry trade groups or the US Department of Commerce. By comparing your organization to the competition, you gain valuable insight into how they stack up against competitors, and provide indicators of potential weaknesses and opportunities. Aligning this with your strategy makes for a formidable weapon that can be used to gain market share and expand existing segments.

Below is a list of 14 questions that can be used to gauge how your S&OP process stacks up against World Class companies.

Self-Assessment:

1. The business plan (strategic objectives) drives the S&OP process.
0 - No strategic objectives are present in the S&OP process.
1 – KPI's exist, but are not incorporated into the S&OP process.
2 – Strategic objectives exist, but are only reconciled on an annual basis.
3 – The business plan is incorporated into S&OP process, but only reviewed on a quarterly basis.
4 – Strategic objectives are reviewed as part of the MBR process and re alignment occurs as required.

2. All S&OP process steps are performed on a regular basis.
0 – Not happening on a regular basis and/or some process steps not happening at all.
1 - Quarterly S&OP meetings.
2 –Monthly meetings, but not all processes incorporated.
3 - All processes are being completed on a monthly basis, but not on time or to S&OP calendar.
4 – Monthly all processes complete on time and to S&OP calendar.

3. Supply and demand are being balanced on a regular (monthly) basis, and inventory levels are decreasing in accordance with plan, while fill rate is improving.
0 - Not happening
1 – Supply plan does not incorporate new products and/or demand plan into review.
2 - Supply plan utilizes new product and demand plans as basis to build desired inventory and stocking levels.
3 – Reconciliation of demand and supply happens on a monthly basis and major adjustments to the near term supply plan are decreasing.
4 –The supply chain plan, on a regular basis, meets the demand requirements of the business with minor adjustments within the near term (1-3 month) time horizon.

4. Stock outs and expediting to fill un-planned orders are decreasing.
0 – Stock outs and expediting are the rule, not the exception.
1 – Stock outs and expediting costs consume more than 25% of the inventory/shipping budget.
2 – Stock out and expediting are diminishing, but still occur on a frequent basis.
3 – Stock outs and expediting have diminished for a majority of all product families and sku's.

4 – Stock outs and expediting are an infrequent occurrence and account for less than 1% of inventory/shipping expenditures.

5. Month and quarter-end "pushes" to hit revenue targets have gone away. Sales and product goals are consistently achieved.
0 – Revenue targets are often missed.
1 - A majority of the revenue targets are achieved through month end pushes.
2 – Revenue projections are frequently modified (up or down) due to incorrect forecasting and/or supply chain issues.
3 – Month end pushes have subsided, and quarter and yearend pushes have become minimal.
4 – Quarter and yearend pushes are nonexistent.

6. Forecast variance at the product family level is minimal 5-10% or less.
0 – No sales plan or forecast exists.
1 – A sales forecast is in use, but is either at too highly aggregated (total revenue for business) or too low at the sku level.
2- Demand plans exist and but horizons are near term (1-3 months) and accuracy is still poor.
3 – Demand plans extend 18-24 months, but accuracy is low.
4 – Demand plan accuracy at the product family level is consistently +/-5% or less.

7. The overall financial plan is frequently achieved.
0 – The financial plan is not achieved.
1 – Financial objectives are occasionally met.
2 – Financial goals are regularly achieved, but only at the aggregate (vs. product family) level.
3 – Financial plans are met consistently at the aggregate level, but product family targets are greater than +/-5%
4 – Financial and revenue goals are consistently meet at both the aggregate and product family levels with a less than 3% variance.

8. KPI's exist for all S&OP process steps.
0 – KPI's do not exist
1 – Some metrics exist, but have not been applied to all processes.
2 – KPI's exist for each of the core areas of the business, but are not integrated.
3 – Metrics are linked via a common scorecard and are reviewed as part of the MBR process each month.
4 – All KPI's are strategically linked to the business plan and are being realized on a regular basis. Performance is within the tolerance range and actively being improved.

9. The planning horizon for the business is greater than 18 months
0 – No plan exists and are still using an aggregate (in dollars) forecast to project revenue.
1 – Performance to plan is still a historical looking metric (vs. forward).
2 – S&OP plans are used to project future performance. The horizon is 12 months or less.
3 – The planning horizon is greater than 12 months but accuracy is only obtained in the near term, 1-3 month time frame.
4 – The S&OP planning horizon extends to a minimum of 18 months with active work to extend the horizon out further.

10. Strategy realignment occurs on a regular basis
0 – No strategic plan exists and/or is communicated outside of the executive suite.
1 – There is no linkage between the strategic plan and the S&OP process.
2 – S&OP process is driven by the business plan.
3 – A strategic linkage exists between the business plan and S&OP process. Adjustments to strategy do not always get disaggregated down into the organization via the S&OP process.
4 – The S&OP and Strategic plan are an integral process. And are consistently (as required) being re aligned.

11. New products are launched on time and to budget
0 – No formal product pipeline exists
1 – Products regularly do not launch on time or to budget.
2 – A formal, maintained new product process exists and a majority of launches occur on time.
3 – New products launch 95% on time +/- 15 days (except pharmaceuticals) and +/- 10% of budget. Measurement horizon is 6-12 months prior to launch.
4 – 99% of projects launch on time and on budget.

12. Margins are improving
0 – Margins for all major products and services are decreasing.
1 – A majority of product margins are flat or declining.
2 – Product margins are holding steady – neither increasing nor decreasing.
3 - Margins for a majority of product families are increasing
4 – Aggregate product margins are improving on a consistent basis by a minimum of 2-5% annually.

13. The supply plan is stable and minimal (weekly or monthly) overhauls are required
0 – The master schedule is not linked to the supply plan and changes on a weekly basis. The scheduling horizon is less than 12 weeks out.
1 – Portions of the supply plan is used to build master schedule, but frequently is not obtained.
2 – Changes in the supply plan drive the master schedule, but are continually re planned due to discrepancy in forecast accuracy.
3 – A solid master schedule is generated based off the supply plan. Minor adjustments are still made within the frozen and firm planning zones.
4 – The master schedule is considered a key linkage in the overall supply chain and S&OP processes. Information is communicated up and down the processes, as well as regularly disseminated across the supply chain.

14. Customer service performance is improving
0 – Customer service levels are declining for all product families.
1 – Customer service levels are decreasing for a majority of product families.
2 – Service levels are neither declining nor improving, but still carry unacceptable customer lead times.
3 – Customer service levels are reaching 95%+ across a majority of product and service families.
4- Customer service levels are in the top percentile of industry, a minimum of 98% for all products and services, and are improving. Customer lead times for new, existing products and services are decreasing and meet or better expectations.

Self-Assessment Results

0 – 14 **Poor** – Sales & Operations Planning processes are not utilized or are nonexistent. Business is performing at or below industry standards. The organization is in a constant state of "fire-fighting" and most likely does not have an effective strategic plan. Most processes are informal or where they do exist, lacking uniform application.

15 –29 **Average** – S&OP process has been implemented and is in use, but most likely not evenly deployed across organization. Frequency of meetings are irregular and lack strategic linkages to the business plan. While some of the performance criteria may be obtained, it still requires a tremendous amount of resources and energy to achieve basic goals. High-level strategic goals are often not achieved on time and do not deliver the anticipated returns.

30 – 44 **Good** - Sales &Operations Planning is deployed across the organization and is the common vehicle for executing strategic goals. KPI's are regularly achieved and actively being improved by team members, but are still not delivering World Class performance. Executive leadership is actively involved in the monthly process.

45 – 56 **Best-in-Class** – S&OP is fully integrated across the organization and its subsidiaries. A full feedback mechanism is in place from the dissemination of the strategic objectives, to the process owners and down into tactical areas of the business, as well as across the supply chain to key suppliers and service providers. Feedback from all S&OP participants is highly encouraged and integrated into the overall process. Senior management views S&OP as a strategic weapon in its arsenal and wields effectively it to gain market share and a competitive advantage.

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