Business-friendly Solutions

DISTRIBUTOR PERFORMANCE EXCELLENCE IN CPG INDUSTRY

A PRACTITIONER'S VIEWPOINT

INTRODUCTION

For the success of any CPG company in the emerging markets, multi-tied distribution plays a vital role in ensuring market reach. The key entity in the distribution channel, the distributor, is the bloodline of any CPG company and plays a very influential role in overall CPG performance landscape.

Many major CPG companies have employed multiple initiatives to improve the overall business delivery including supply chain; but they are limited to:

- Supply Chain efficiency until Distributor point
- Retail Execution Plan for company sales executive
- Route map for distributor's sales man
- Primary Order Management system
- Trade Promotion Management
- Shopper Marketing Programs

Most CPG companies showcase the Return on Capital Employed (ROCE) to every new distributor they wish to enrol. However, few companies try to monitor ROCE on a monthly, quarterly or even on annual basis. Given the same, there is a significant value unlocking potential for a CPG company if they were to undertake Distributor Performance Excellence Initiative (DPEI) as one of their key business KPI at a strategic level.

DPEI: DEFINITION & SCOPE

In our view, DPEI is a consolidated framework that talks about a 360 degree view of Distributor Performance on a real time basis. The below figure shows the key attributes to be monitored for gauging Distributor Profitability Management on a holistic basis.

Figure1: Key attributes of Distributor Profitability Management

The following section details how monitoring each of the above-mentioned attributes contributes to incremental ROCE for distributors.

INVENTORY & WAREHOUSE MANAGEMENT

For any CPG company distributor, efficient Inventory and Warehouse Management contribute largely towards the overall profitability. The key lies in how successfully one can measure warehouse operations and costs. What to order, when to order, what quantity to order, what warehouse layout design to adopt to maximize capacity, what processes to adopt to optimize overall warehouse cost, percentage of permanent/temporary labour, are few of the points to consider to have an effective Inventory and Warehouse Management system.

Industry Good Practice: Top CPG companies in the emerging markets are moving from traditional inventory management model to a new scientific lean-based inventory management system that derives the Order Basis agreed Sales Estimates finalized post S&OP process. Under this new system, inventory is aggregated at upper nodes like HUBS & Company's warehouses making Distributor Warehouse act more like a cross-dock or flow-through hub & thus increasing the inventory turns for the distributor for the same amount of capital employed.

Dock to stock time	■ Plan inbound material flow ■ Manage inbound material flow ■ Monitor inbound delivery performance ■ Manage flow of returned products
Operate warehousing	■ Track inventory deployment ■ Receive, inspect and store inbound deliveries ■ Track product availability ■ Pick, pack and ship product for delivery ■ Track inventory accuracy ■ Manage Inventory
Stock to Dock time	■ Plan, transport and deliver outbound product ■ Track carrier delivery performance ■ Manage transportation fleet ■ Process and audit carrier invoices and documents
OTIF %	■ Deliver Quality Goods on time in full. ■ Goods damage control measures
Manage returns- manage reverse logistics	■ Authorize and process returns ■ Perform reverse logistics ■ Perform salvage activities ■ Manage and process claims
Warehouse Management Information system	■ Upstream and Downstream flow of quality information for better forecasting

Figure 2: Key High-level Activities for Effective Inventory and Warehouse Management

FIXED ASSET EFFICIENCY

Fixed asset optimization plays an important role in deciding the ROCE for a CPG distributor. If a distributor has property and equipment assets that are not employed or are not generating enough cash flows, it may impact the financial health of a distributor's business ecosystem. How well the distributor is able to employ his real estate and machinery can make a difference to profitable business delivery.

Industry Good Practice: CPG companies are moving towards FDOS (Fixed Days of Service) for delivering goods at both General Trade & Modern Trade outlets. This practice gives the required lead time for all stake holders to plan activities with error minimization & fill rate maximization (Company Warehouse knows the approximate order volume and is able to plan logistics in time, so is the case with the distributor.) Other than FDOS, different mobility solutions are being implemented which are helping CPG companies reduce overall Order service life cycle by:

- Electronic order capture through handheld devices
- EAN based order capture
- GPS based Order sync with Distributor Management system
- Automatic order flow from DMS to Company's ERP system

Above activities have helped distributors reach more outlets simultaneously thus increasing the fixed asset efficiency.

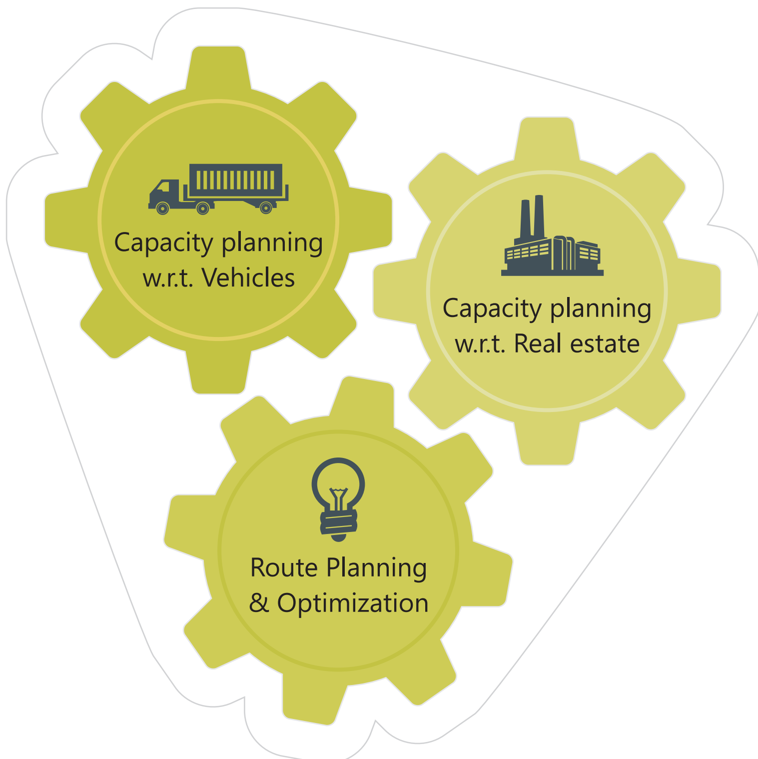


Figure 3: Key Parameters of Fixed Asset Efficiency

EMPLOYEE EFFICIENCY

Any successful business delivery rotates around the capability, integrity, attitude and performance of the people employed. It is of paramount importance for any distributor to hire and retain right employees who are passionate enough to contribute to pull the necessary levers, to maximize top line, optimize middle line and in turn, incremental bottom line.

Industry Good Practice: Top CPG players are using simulation based training playbooks for training distributor salesman. This is a scenario based training program that enables salesmen to adapt to dynamic events, making them more productive by moving towards relationship based sales techniques rather than transactional ones. Other than scientific trainings programs, companies are also developing personalized step-up channel incentivization programs basis the salesman's past performance, which takes into consideration the bottom and the top quartile performers.

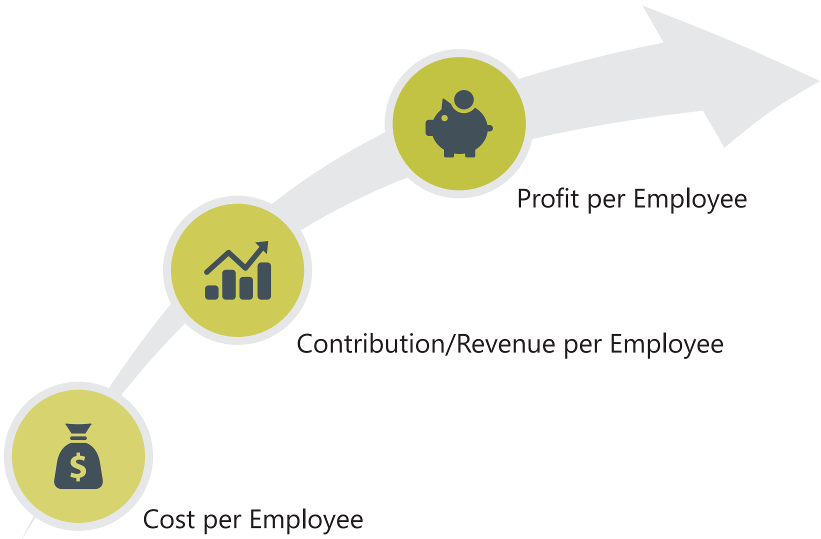


Figure 4: Incremental Employee Efficiency Journey

WORKING CAPITAL MANAGEMENT

An optimal Working Capital Management contributes majorly towards the profitability of a CPG distributor. How well a distributor manages its DSO and DIO can heavily impact the bottom line. Therefore, every distributor must focus on parameters like Inventory Turnover, Stock Ageing Analysis, Account Receivables Ageing Analysis and Cost to Serve at retailer level to maximize return on working capital. To have an effective business delivery, a distributor needs to focus upon both Cash Conversion Cycle (CCC) and Net Trade Cycle (NTC).

Industry Good Practice: Gone are the days when claims processing used to take anywhere between 4-8 months. Top CPG companies have now in place a fully automated paperless Claims Management system which enables the distributor to file claims electronically and get the credit note within 7-30 working days. This process reduces the requirement of working capital, increasing its efficiency. Other than this, many companies have a monthly account reconciliation process that is aligned with the KRAs of both Sales & Finance Executives.

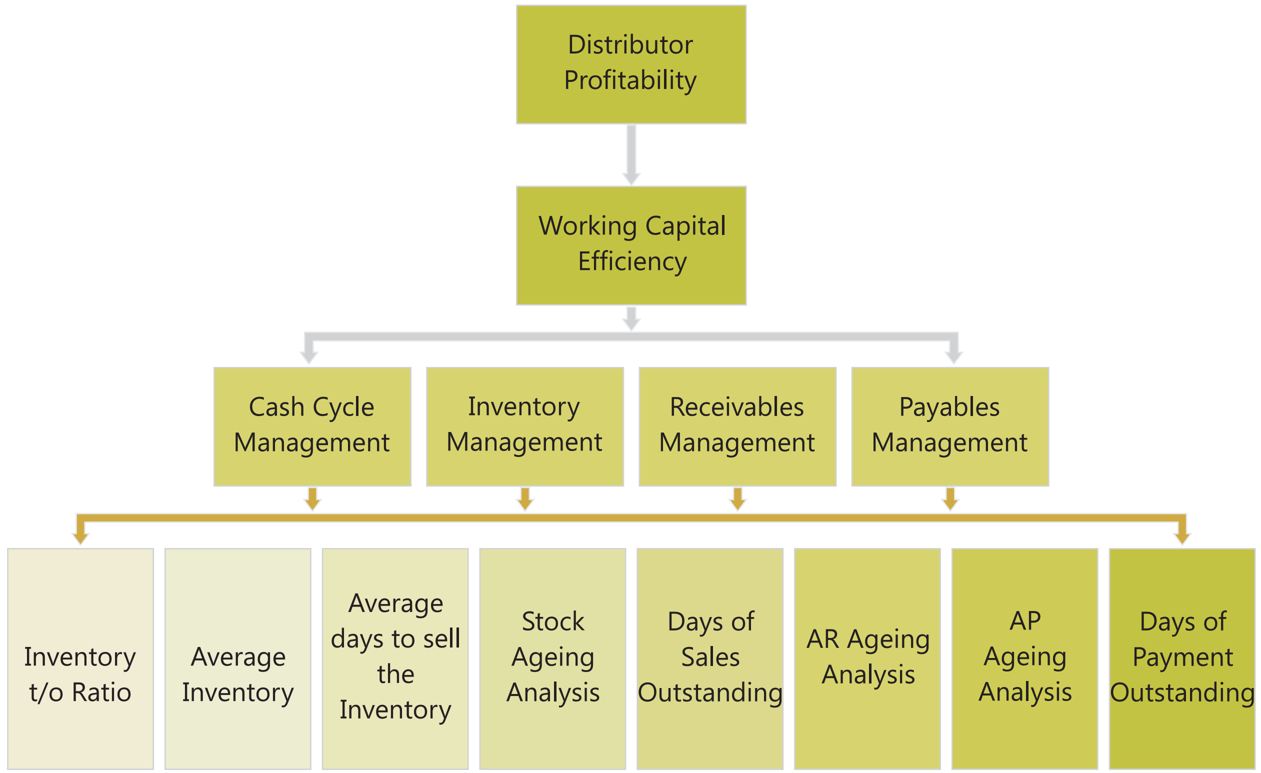


Figure 5: Key KPIs for Working Capital Efficiency

SECONDARY SALES PROCESS

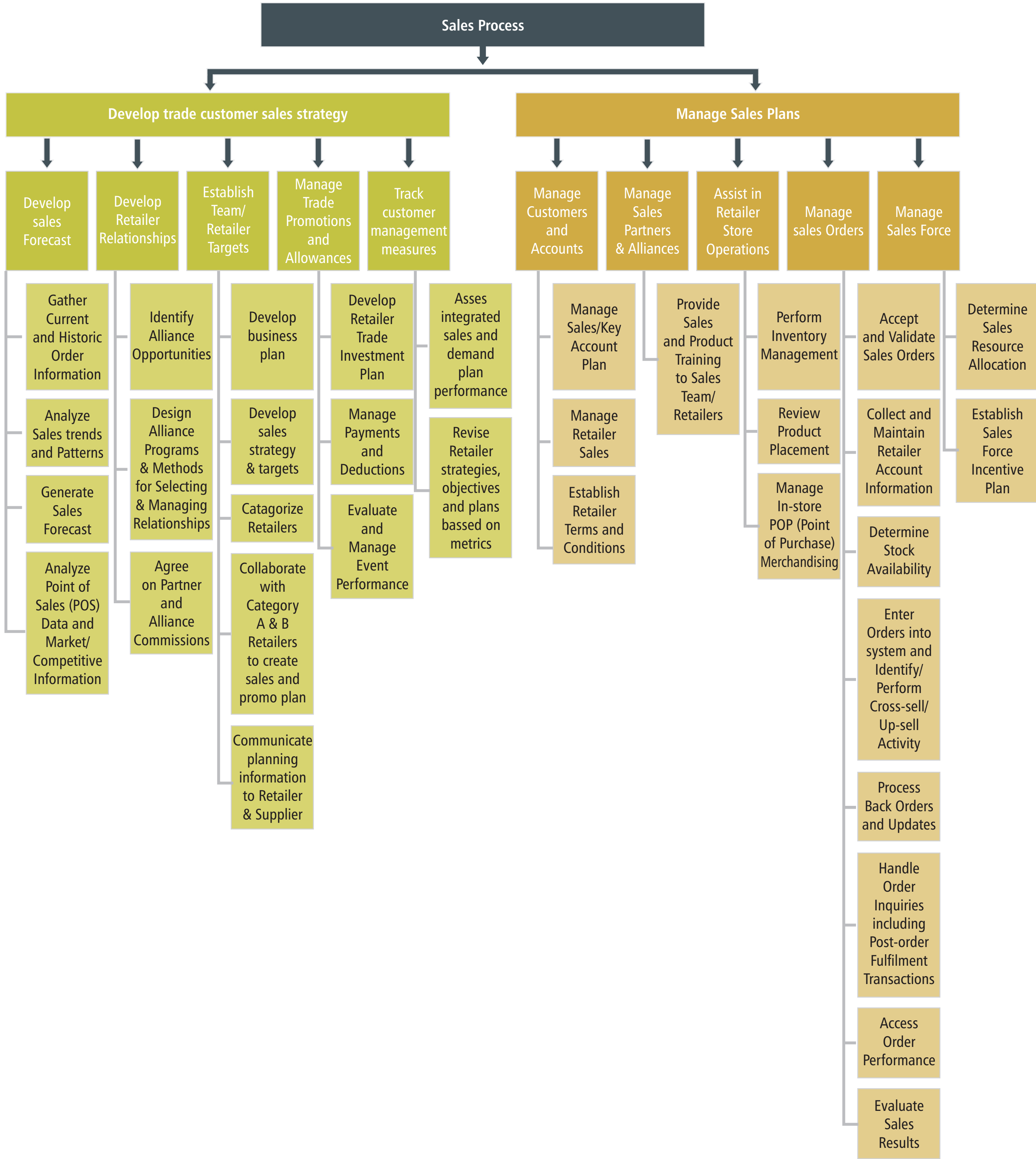
A CPG distributor must have an effective and efficient sales process that can help do the following:

- Plan & Forecast Demand accurately.
- Optimized Order Management
- On time Delivery of goods in full
- Collect Receivables with minimized cost
- Reduce Cost to Serve
- Increase Market share
- Manage Relationships
- Improve Profits

Industry Good Practice: Major CPG Companies have segregated their primary and secondary sales processes; where the whole focus has been shifted from a Push base to a Pull based sales system. In today's business ecosystem, field sales executives along with distributor sales men roles, revolve around:

- Capture shelf space
- Create product visibility
- Pre-empt demand
- Moving retailers from product loyalty towards advocacy

The following figure shows key activities involved in executing a secondary sales process.



LIABILITY MANAGEMENT

When, how much, from where, for how much time, for what purpose? - are a few questions every distributor has to think about before borrowing funds, either for asset creation or for working capital. Liability management is a four-step process:

Industry Good Practice: Various CPG companies have the facility to provide low interest working capital loans to facilitate smooth business delivery. Other than loans, distributors are getting subsidized & incentivized for implementing advanced technology in their working such as:

- Distributor Management Systems
- Order capture handhelds
- GPS for vehicle tracking
- On-the-go invoice printing facility

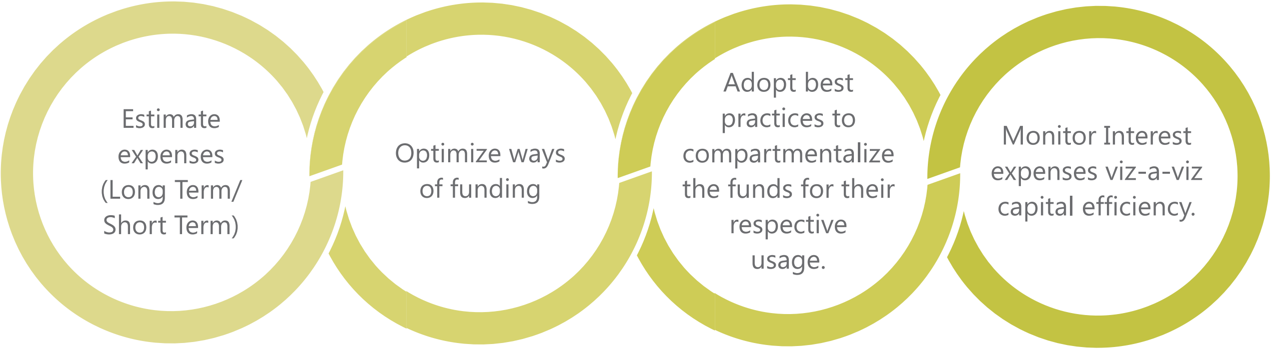


Figure 6: Four Pillars of Liability Management

These collaborative activities help both distributors and CPG companies to gain maximum value in their overall business operations.

VALUE UNLOCKING POTENTIAL FOR CPG COMPANY

A pictorial representation of all the above factors will help in understanding the value unlocking potential for a CPG company, if it implements the Distributor Performance Excellence Initiative (DPIE), making it a part of the strategic KPIs.

	EV Levers	Value Levers	Operational Levers
Enhance Profitability	Increase Operating Income	Increase Revenue	Increase Channel/Sales Force Effectiveness
			Expand the Market
			Improve Service Quality/Effectiveness
			Improve Customer Experience
			Optimize Relationship Management
		Improve SG&A Productivity and Optimize Costs	Improve Process – Reduce Effort per Transaction
			Work on Profit per Employee Model
			Work on Cost to Serve Model
			Improved Warehouse Management Processes
	Increase Fixed Assets Efficiency	Increase Asset Productivity	Increase Asset Utilization by Efficient Capacity Planning
			Route optimization and Planning
	Increase Working Capital Efficiency	Maintain Adequate Cash Levels	Optimize Cash Management by Focusing on CCC and NTC
		Reduce Inventory Levels	Optimize Inventory Management Process
			Improve Demand Planning and Forecasting
	Liability Management	Estimate Expenses	Clearly Define Long-term and Short-term Capital Requirement
		Optimize Ways of Funding	Balance between Secured/Unsecured Funding and Repayment Period
		Adopt Best Practices	Compartmentalized Funds for Long-term/Short-term Usage
		Monitor Interest Expenses	Retire Expensive Loans with Excess Cash

If by employing this initiative a distributor can increase ROCE, it will help in improving the top line, which in turn will help the supplier in improving the top line significantly by:

- Further investments by distributor into inventories
- Better demand forecasting at distributor level which can be aggregated at Branch/Regional/ National level that will help reduce the bullwhip effect, thus leading to lower cost by minimizing uncertainty
- Gain market share by Optimizing Distributors Sales Force and thus reducing company level SG&A costs
- CPG company can improve the overall efficiency of its indirect channel by:
  - Implementing DPEI at one distributor as a Pilot
  - Replicating the initiative at other distributors by showcasing the benefits from the pilot case
  - Incentivizing the performance of top distributors
  - Benchmarking the performance of top distributors with other at Branch/Regional/National level and motivating others to reach the benchmark level
  - Improving the overall channel efficiency

CONCLUSION

With the increasing competition in every business domain, the CPG industry is getting more and more commoditized. In this scenario, the role of a distributor becomes all the more crucial. What they do in the market not only decides the short-term future of the company, but also impacts its long-term position. It is the responsibility of the Supplier to help the Channel partners conduct business profitably and efficiently. DPEI can be one such Initiative that any CPG company can undertake and create a win-win situation for the entire Ecosystem.

AUTHOR

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Abhinav Verma is a Senior Associate Consultant at ITC Infotech, Business Consulting Group, specializing in the CPG domain. He holds a Degree in Management Science with M.B.A in Marketing & Finance, with 10 years of experience in Territorial Business Planning & Logistics, Customer Analytics, ROI Management, Profit Centre Management, Risk Management, Vendor Development & Procurement, Key Account Management & Quality Management in CPG sectors. He has built comprehensive Financial Benchmarking models, Redesigned the Demand Estimation & Promotional Planning process, Set up the SOPs for Centralized Order Processing system & SKU rationalization and created Process Blue print for Distributor Management System (DMS) for CPG Sector companies.

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