

Merrifield Act II

Insights Into Quantum Profit Management

SCRIPT #1:

SELLING MORE, MOST-PROFITABLE CORE ITEMS; FROM MOST-PROFITABLE SUPPLIERS; TO ANY AND ALL CUSTOMERS

Introduction:

Waypoint's Quantum Profit Management System (QPMS) enables many new profit improvement actions including defining and maximizing the profits from the intersection of selling most profitable items to most profitable customers. (For more on this "core intersection" read articles 2.35 and 2.29 at www.merrifield.com and ideas for maximizing more "old-to-old" selling.)

Although I recommend doing all that I cover in past articles on "renewing or maximizing core sales", what is a first-step, simplest "script" (a term from the book "Switch") pitch that we can carve out of this opportunity area? This one involves working with suppliers – one at a time – in a simple, powerful and novel way.

PITCH TO THE SUPPLIER (I have included some actual true numbers from a Waypoint Client):

Hi, Supplier A! Whether you know it or not, you are one of our most profitable suppliers on a net profit basis based on powerful new analytics capability that we have developed. We can even determine the net profits we make on each SKU that we buy from you.

Assuming pictures and facts speak more emphatically (remember scripts should be visual and visceral, if possible), let's look at the whale curve for the items we buy just from you and then the profitability ranking of all of your SKUs. (Using numbers from a Waypoint Client)

You are one of 330 suppliers we have.

You are our most profitable supplier of 4 that have good product offerings in the specific, product-category of "Z" (this distributor could identify 25 discrete product categories that mattered).

Your 110 SKUs are only about 2.5% of the 4000+ SKUs we stock.

Of the 110, about 50 are highly profitable; the rest we lose money on (which is another day's conversation, script and set of experiments).

Of the 50 items, 20 account for the majority of the profits and our most popular by both picks and different customers that buy them. (At the other extreme, there are some items in your line that aren't bought by anyone or by just one customer.)

They comprise graphically the front end or head of the whale in the whale curve.

Here's our first, scientific experiment proposal:

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We would like to increase our average inventory investment in the top 20 most profitable items by some significant percent (50-100%) in order to track how much our – sales, margin dollars and profits – increase on these items. We will track their sales versus the rest of your stocked line that is not changed, as well as other similar, competitive items from other competitive, category suppliers. This could lead to an experiment to then switch redundant-supplier volume to your line.

Our assumptions are that:

Our effective fill-rates on our best items are not as good as we think that they are, because:

Customers call and ask if we have items (especially unusually large amounts of them which they may not have been able to source from their first choice supplier). If we don't have enough of an item, the customer will then call somewhere else. We don't enter the information as a lost order or as lost demand into our automated forecasting system which would then increase inventory levels in the future.

If we don't have the item at all or in full, we will often be able to save the order (especially on most popular items that all category suppliers make) with a substitute item from within your line or more likely from another supplier line. (We could also switch them from a competitive item to your better stocked item.) This informs future buying to buy less of what the customer initially wanted and more of what we substituted.

We are, therefore, both losing sales volume and growth rate in our market share.

After three months, we will see a bigger increase in sales and profits than we might think. There are no more profitable and popular items in our entire inventory. Growing them X% will have a more powerful impact on our bottom line than any other product promotion that we could do. (By contrast, imagine if we promoted some small-dollar-per-pick items that have margin markups, but for which the cost of picking the line item exceeds the dollars in the pick. We don't think we would make any money on greater volume!)

These items are probably your most profitable items too, so our amplified gain in our trading area will also be yours.

In these tough times, there are competitive distributors and suppliers that are on the ropes. When a distributor gets squeezed, they cut back on inventory starting – unintentionally -- with A+ items first, because those items sell down the fastest while the garbage items continue to sit). The customers of the imploding distributors will then come to us for the "shorts". We want this new demand to be filled by and/or substituted on to your deeper stocked items. This will help you to gain both new market share and preserve existing market share which may be at risk through other distributors in our area.

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How can you participate and benefit in this controlled experiment?

Help by financing just the incremental inventory investment for the target 20 items with dating that matches the months of extra stock (details to be negotiated)

What's in this for you?

Besides picking up growth and share in a tough market in a very focused, low-risk way, you will be able to extend this experiment to other parts of the country using hard data about the inherent profitability and incremental growth.

We are approaching you first. If you are not interested, we will then go to our second most, long-term profitable supplier in this category space.

Assuming this experiment works, we would then like to work on two more "scripts" that focus on:

- How to convert current customers buying alternative products to your products in order to close down redundant, less profitable supplier lines.
- Why the bottom half of SKUs on our profitability ranking report are unprofitable? Then, see if we can co-create win-win supply chain solutions to make them profitable.

How will we track the results? Our QPM system has a "delta PBIT" report that we can run on any supplier's line for any period of time. We will be able to see how much the better stocked items perform versus the rest of your line as well as against other similar supplier lines/items.

Shall we precede on deciding the specific amounts of extra inventory investment and the dating terms?

COMMENTS:

To use terms from "Switch", how stressful will this script be to any of "the elephants" that any or all of your managers are "riding"? I can't imagine a CEO, CFO, banker, or buyer would have any problems with this. The sales force would have more confidence in and preoccupation with selling the targeted line and items, because they know that we would always have it in stock.

How un-nerving will this be to any of our target supplier's people (regional rep, national sales manager, etc?). Their credit manager might have a problem if we are a credit risk, but otherwise, we are still ultimately buying more from them which they can book as a sale right now. (They might be particularly interested in this inventory loading plan at the end of one of their monthly or quarterly closings.)

The script does not address all of the most popular/profitable SKUs that we are selling to a target niche of customers. Such a program might involve 200+ items from 20 different

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category-leading suppliers which would be too big of a change for some people, especially if they thought that the company would have to finance the incremental inventory investment with more bank debt. If we keep the change steps small (20 or less SKUs from one co-op investing supplier), then we can reduce risk and test quickly.

What if this “experiment” does not increase true profits big enough and fast enough? (I have personally experienced relative growth rate increases from 15 to 30% with this script experiment in a number of different distribution channels.) Such a “concern” is the type of ambitious energy (to change for the better) we want to hear. It is possible to:

Run 10 or more such experiments with our #1 chosen supplier in each, competitive, product category that we stock and sell.

We can suggest to any one supplier who gets excited about the opportunity to consider extending the experiment to more of the most profitable items.

We can pursue more and other scripts (like #2 and #3 in this package). No turnaround tactic, for example, is more quickly beneficial for the least amount of resource investment (and stress) than working with a super-losing account to turn it into a super winner with additional incremental volume. (Script #2)

Other questions, ideas or concerns? Let me know at bruce@merrifield.com or 919-357-2372.