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The Collaboration Game
*Building Value in
the Retail Supply Chain*



Contact Information

Amsterdam

Marco Kesteloo

Partner

+31-20-504-1942

marco.kesteloo@booz.com

Helsinki

Pertti Heinonen

Principal

+358-9-61-54-6638

pertti.heinonen@booz.com

London

Simon Harper

Partner

+44-20-7393-3434

simon.harper@booz.com

Amit Kapoor

Senior Associate

+44-20-7393-3275

amit.kapoor@booz.com

EXECUTIVE SUMMARY

Retailers have historically maintained an adversarial relationship with consumer packaged goods (CPG) companies, their primary suppliers. Negotiations over price, promotional support, and marketing budgets, among other persistent areas of disagreement, often result in damaged relationships and minor gains—only to have the fights resume the following year. For some buyers, this annual wrangling is seen as an important part of the job—and even fun. To them, facing down suppliers is a kind of sport.

But if their goal is to maximize profitability, buyers would be wise to take up tennis instead. As good as old-fashioned haggling may feel, it generally results in very little actual good, as retailers and suppliers overlook the many ways that they could gain from their partnership.

Changing these old habits is not a particularly new aspiration. For more than a decade, retailers and suppliers have tried to learn to collaborate more and move beyond the old zero-sum games. Their initiatives have included assigning “captains” to work with each other on ways to drive category growth and forming industry groups (such as Efficient Consumer Response and Collaborative Planning, Forecasting, and Replenishment) that pursue supply chain optimization. Yet

despite all the hard work, only partial success has been achieved. A recent Booz & Company survey of European retailers and manufacturers found that less than 20 percent of respondents were “very satisfied” with the results of their current collaborative initiatives.

Even now, the most successful collaborative relationships are mostly pilot projects involving a retailer and a single supplier focused on fixing a particular problem in a particular category. Only about 30 percent of the projects involve multiple partners and multiple categories, according to Booz & Company research. Broad-based strategic collaboration remains a rarity, and most retailers still do not consider building collaborative value a core activity.

WATCH VALUE, NOT PRICE

Retailer–supplier partnerships have failed primarily because buyers tend to view their value in a limited way: purely as a means of extracting lower prices or extra promotional dollars from CPG suppliers in their yearly negotiations. Buyers often walk away from a negotiation feeling successful, unaware that their victory may well have been compromised by the failure to address issues that could have much more impact on retailer and supplier profits, such as in-store availability. The shelves are still not fully stocked, and what seemed like a highly profitable day’s work is actually only a slightly larger share of a smaller pie.

These negotiations overlook proven opportunities for enhancing revenues and profits simply because the annual dialogue about products and prices traditionally includes only retail buyers and the suppliers’ field sales teams. This restricted dialogue eliminates the possibility of external and internal partnerships that can raise the level of the negotiation and add value to the annual supply plan. Having the buyer be the sole point of communication with the supplier also encourages a silo mentality within retail companies, in which buyers are separated from their peers in marketing, supply chain, planning, and store opera-

tions—and that results in much less creativity in dealing with suppliers.

Companies that want to build holistic relationships with selected suppliers across the value chain that can result in higher revenue and lower costs than the old haggling habits must pursue collaboration and cross-functional participation. More cooperation at annual purchasing meetings and during the year could improve returns for those on both sides of the negotiating table. For example, a retailer can provide more advantageous shelf availability to a CPG company if the two parties agree on joint programs for replenishment merchandising and promotion. Programs like these require the up-front participation of store operations and supply chain planning managers. And this is not a unique example. A wide spectrum of possible collaborative measures can raise revenue, improve efficiency, and cut costs for both retailers and their suppliers (*see Exhibit 1*).

Revenue/margin enhancement. Working jointly to harness complementary skills and apply the knowledge needed to grow a category can be a win-win proposition. This effort can be as simple as linking the supplier’s consumer insight to the retailer’s pro-

Exhibit 1
Collaborative Levers for Enhanced Profitability

REVENUE/MARGIN ENHANCEMENT	PROCESS IMPROVEMENT	COST REDUCTION
<ul style="list-style-type: none"> Increasing penetration of core products Building multiyear strategies to grow/build the category Managing/reallocating shelf space and products Driving consumer convenience and impulse shopping Collaborating more closely with private labels 	<ul style="list-style-type: none"> Launching new products collaboratively Improving effectiveness of marketing efforts Jointly improving promotion planning and management Practicing life-cycle management Utilizing POS data and improving on-shelf availability Improving demand forecasting 	<ul style="list-style-type: none"> Decreasing shortage Enhancing distribution efficiency Redesigning display operating model Optimizing the role of merchandisers Reducing returns Improving efficiency through supply chain improvements

Source: Booz & Company

motional capabilities. For example, Migros Türk Ticaret Anonim Sirketi, one of Turkey's largest supermarket chains, worked with Unilever to use consumer response and store layout data to increase sales of hair conditioner. Beginning with a survey conducted at an interactive in-store coupon kiosk, Unilever and Migros discovered that shoppers were not buying hair conditioner for a variety of reasons, including simply feeling that they didn't need to (18 percent) and believing that it was too expensive (12 percent). With that new knowledge, Migros and Unilever tweaked their sales program, increasing price promotions and reallocating shelf space so that conditioner and shampoo were sold together in hopes of establishing conditioner as a necessity in the shoppers' minds. As a result of this campaign, Migros's overall conditioner revenue increased by 25 percent, and the chain's sales of Unilever conditioner grew by 36 percent.

Process improvement. A wide range of supplier-related processes can be improved by more collaborative retailer-supplier relationships, including promotion planning and execution, demand forecasting, and stock replenishment. One of the best sources of information for improving these processes is the retailer's point-of-sale (POS) data. For instance, by examining POS data to identify purchasing patterns at certain Tesco supermarkets, Kellogg Company found that most of its out-of-stocks at the United Kingdom retailer's stores occurred midweek, in the afternoon. Consequently, Kellogg's adjusted its shipping schedules—and in the process helped Tesco recapture more than £2 million (US\$4 million) in lost sales and improve customer satisfaction. In a similar initiative, Kraft Foods Inc. used U.K. food retailer J Sainsbury PLC's POS data to improve in-store availability of cheeses during promotional periods. The accuracy of forecasted

returns from promotions increased by 20 percent, reducing the risk of both understocking and overstocking.

Cost reduction. Supply chain improvements such as more efficient distribution, streamlined inventory, increased product availability, and improved merchandising operations are all within reach of collaborative retailer-supplier relationships as well. For example, large U.K. health and beauty retailer Boots, working with a leading supplier of hair accessories, came up with a system to cut labor costs and improve the supplier's displays at the same time. By designing an intuitive, color-coded product display system, the retailer cut setup times from 60 minutes to about 15 and reduced overall store rebuilds from eight weeks to two; this faster path to installing and changing promotional campaigns helped Boots increase sales of hair accessories by double digits in the first year alone.

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FROM SUPPLIER TO PARTNER

Despite the promise of collaboration, few retailers have succeeded in creating such partnerships with their suppliers. It is not difficult to find pockets of excellence within a given retailer-supplier relationship, such as buyers who work diligently on promotional planning, but these tend to be isolated successes—more like pilot programs than established partnerships. Most retailers have found it difficult to expand successful pilot programs into a broad, strategic agenda for deeper supplier collaboration, largely because of the challenge involved in learning to work cross-functionally.

Nevertheless, this challenge can be met. Broad-based collaboration between retailers and suppliers is possible if careful attention is paid to how the relationship is structured. A few key guidelines can make all the difference in undertaking this task:

Generate a full basket of possibilities, but home in on a few prioritized opportunities that are most important to both businesses. Think holistically about revenue and cost, and challenge current ways of work and operating procedures in order to identify as many potential avenues to improvement as possible. Although some of these opportunities can be pursued unilaterally, the best opportunities for

collaborative sourcing improvement are typically those where the data, skills, and insights of the supplier and retailer intersect.

Establish an open dialogue, but make sure that the terms of all agreements are explicitly defined up front. Specific agreements on targets, responsibilities, and accountabilities should be locked in as early as possible, along with explicit expectations.

Create transparency by sharing benefits, costs, and information openly, but build in appropriate confidentiality measures. Collaborative partnerships require parties to move “beyond the gut” to a more fact-based relationship. This cannot succeed without trust and transparency. An up-front agreement on how to share data across the value chain is essential—as is a clear understanding of how the companies will share the benefits and costs of their joint initiatives. Perhaps even more important for building trust is a clear understanding of the areas that each party wants to keep off-limits.

Set both short- and long-term agendas with supply partners to capture value quickly but still pursue the big ideas. Find a mutually beneficial improvement idea that will provide each partner with a quick gain. This will help

build momentum for tackling more complex, and often more lucrative, opportunities down the road.

Gain top-level support, but stay focused on the execution.

Collaboration is less a matter of what is agreed on in the boardroom than what is actually done in the warehouse and on the shelf. Only by managing and monitoring progress with adequate tracking procedures and metrics is it possible to drive success.

Be more open with all suppliers, but choose collaboration partners wisely.

Given that a collaborative approach is more resource intensive and requires more cross-functional engagement than other approaches, supplier partners should be selected on a broad set of criteria that go far beyond their share of the supply spend. The chosen candidates should reflect the retailer's strategic aspirations and demonstrate a serious interest in building a deeper relationship. The selection should also reflect where a collaborative effort can yield the most value creation, such as taking aim at low-margin categories or poor supply chain performance.

One northern European retailer followed these guidelines to very good effect. This retailer had been playing the same old price-based game as competitors whittled away at its once dominant share of a stagnant national market. Then, a major global retailer, which enjoyed a significant cost

advantage, announced its intention to enter the retailer's home market—a move that was expected to create a much more severe and sudden decline in the retailer's results. Faced with this grim news, the company's executive team decided to revamp its strategy.

One of the most daring changes the executives undertook came in the form of an offer to the company's biggest suppliers: "Work with us to review the entire value chain, from production all the way to the shelf, to look for opportunities to improve performance and revenue," they said. "Afterward, we'll make those improvements and share the gains equally."

More than 10 top suppliers agreed, and all the players set to work. The partners agreed to a three-year commitment, which gave the retailer and its suppliers ample time to understand and improve complex processes for mutual gain. The commitment also encouraged the retailer to invest in the process of building a strong individual relationship with each strategic supplier, as well as developing the internal capabilities needed to ensure sustainability, including coaching and skills transfer. At the same time, the partners stayed focused by agreeing to identify improvements and establish plans not in months or quarters, but in just eight weeks, making it easier for both sides to dedicate the staff needed to improve their systems.

Further, the retailer made a genuine commitment to openness. All partners shared data to gain a more complete sense of the value chain. When the data was sensitive, to help reassure suppliers that it would not be used against them, it was routed through a third party (in this case, Booz & Company), which acted as a neutral broker to protect the data from misuse.

After the opportunities were identified, plans were drawn up detailing a new operating model capable of capturing the potential gains. At the same time, the retailer's executive team worked to institutionalize the tools and techniques needed to make the changes happen. And even as immediate gains were achieved, many long-term changes were undertaken to ensure that the forward momentum was maintained.

This collaborative effort has already added 5 to 10 percent in value to overall profitability across all 10 suppliers. Two-thirds of the gains were generated by incremental sales, and one-third came from cost reduction. Value was added in many ways, including increased use of private labels, improved shipping and logistics, and better cooperation between suppliers. The biggest single source of value: better category management, which was responsible for roughly one-third of the overall gains.

After so many false starts, it is tempting to dismiss retailer-supplier collaboration as an idea that looks good on paper but is nearly impossible in practice. In fact, as the retailer described above discovered, collaboration can work. Trust is a key ingredient: Once suppliers feel certain that strategic partnership proposals aren't just another negotiating trick, many of them are keen to drive such partnerships forward. As with any successful commercial partnership, it all comes down to ensuring that both sides gain from the venture.

Collaboration is less a matter of what is agreed on in the boardroom than what is actually done on the shelf.

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