A multiline distributor strongly increased profitable growth while positioning for industry transformation.

EXECUTIVE SUMMARY

[Disguised Actual Data]

THE CHALLENGE:
Strongly increased profitability along several key dimensions to enable the company to diversify and reposition in its transforming industry, while turbocharging current performance.

THE PROFIT ISLE SOLUTION:
Executed a three-month configuration of the Profit Isle Solution. Identified a three-pronged profit improvement solution that resulted in very strong profit growth in each segment of its diversified business. Drove sustained profitable growth through profit toolkits at the manager level.

Opportunity 1–Customers: Identified Islands of Profit Customers, and focused selling efforts on this segment and on Minnow customers with the potential to grow, while profiling Coral Reef customers to implement targeted profit-improvement measures.

Opportunity 2–Products: Developed strong profit-focused category management processes based on Profit Isle Profit Toolkits (which enable each manager to use our profit stacks – granular all-in P&Ls – and best practice profiles to maximize the net profits of his/her portion of the business), while driving profit-maximizing product mix optimization at the customer level throughout the company.

Opportunity 3–Operations: Determined that the company’s businesses had diversified to the point where they needed parallel supply chains by product-type (not by business) rather than the single traditional operation, and specified these supply chains from the suppliers to DCs to customers – while the customer profit-improvement measures enabled the company to avoid a major capital expansion.

IMPACT ON CLIENT BUSINESS:
Built the foundation for strategic success and long-term profitable growth for a client that was actively diversifying, while rapidly improving the client’s current performance by tens of millions of dollars, meeting the client’s need for repositioning in the transforming industry while generating the cash to reposition and grow.
THE CHALLENGE

Client was a successful distributor with a very strong reputation and solid profitability, but faced a need to diversify and to optimize its performance in both its traditional and new lines of business. Profits were in danger of eroding, as the company’s complexity and internal interdependencies grew, while its functional organization was stretched to the limit and its traditional financial metrics became increasingly unhelpful.

The challenge was to identify and implement a competitive positioning, market focus, and set of implementation policies that would enable the client to continue to diversify, to beat its competitors in each line of business, and to build a new set of organizational processes and metrics that would solidify inter-functional coordination.

Current financial reporting structures and key performance indicators (KPIs) are not suited for rapidly changing environments and industries. Overly broad P&Ls lack visibility into the core value of the business – Net Profitability – on a granular enough basis to focus action.

As markets and supply chains become increasingly complex, and as competitors become more focused, it is more important than ever to measure the all-in profitability of every transaction (invoice line), which yields a complete understanding of a company’s internal and prospective profit landscape.

Traditional approaches to business cost structure leave managers focused on Gross Margin, assuming that some proportion will hit the bottom line. The reality, proven in our analysis of tens of billions of client revenue dollars, is that Gross Margin is statistically unrelated to Net Profits.

For this multi-line distributor, this was the key to long-term profitable growth.

In order to raise net profit, while repositioning in its transforming industry, the client used the Profit Isle Solution to gain deeper visibility into its profitability, which revealed highly focused high-impact insights.

THE PROFIT ISLE SOLUTION

Profit Isle used its proprietary big data analytics engine and easily configured cloud platform to rapidly provide visibility to the transaction level profitability of the company – the client could literally see the full components of profitability of every product sold to every customer every time, summed into any configuration (customers, products, operations). The profit improvement process has five steps:

1. Calculate the all-in profitability of customers, products, and operations across the entire organization by utilizing the client’s invoice records, generating a profit and loss statement for every transaction.

2. Create a set of “Profit Maps”, which reveal the areas of concentrated profit in the company by segmenting total profitability into four quadrants – Islands of Profit for high revenue, high profit business; Coral Reefs for high revenue, but low profit business; Minnows for low revenue, low profit business, and Palm Trees for low revenue, but high profit business – across all variants of customers, products, and operations (e.g. for a money-losing product, why are some transactions highly profitable while most are very unprofitable?)

3. Analyze and compare each segment of the company with the most profitable (best practice) portion for that segment (e.g. like products in like customers).

4. Prioritize an opportunity set which will produce the greatest profit improvements, consistent with the company’s internal initiatives and constraints.

5. Train the client’s managers throughout the organization to manage profitable growth using (a) Profit Isle’s profit solution, which produces an updated profit landscape every month and (b) Profit Isle’s world-class change management techniques, embedded in Profit Isle’s Profit Toolkits which bring the profit opportunities to each manager’s specific business portfolio, and which track profit progress in real-time.
The client’s profit maps showed a big difference in performance between the Island of Profit customers and the Coral Reef customers, although both looked similar in terms of gross margins. A systematic examination of the all-in profit stack (P&Ls) of the Island of Profit customers versus the profit stack of the Coral Reef customers showed that:

1. The Island of Profit customers were very profitable, providing well over 100% of the reported profits, while the Coral Reef customers were actually eroding over one-third of those profits; and
2. A surprisingly small set of sales and operating processes made all the difference – and amazingly, none of these all-important processes were measured or managed.

In addition, the profit maps showed that a surprisingly large portion of the Minnow customers were highly profitable, while others were marginal or actually losing money.

The biggest differences between the profit stacks of Islands of Profit customers and Coral Reef customers were not visible with traditional financial metrics. In terms of revenues and gross margins, these groups appeared similar, but there was a world of difference in the operational costs, which had been buried in a blended cost account.

The Coral Reef customers had a very high proportion of automated ordering, either through EDI or vending machines. In fact this was celebrated as a way to reduce sales cost. The problem was that the sales force had pushed their accounts to order frequently, arguing that it would reduce their inventory cost. What they did not see was that for every dollar of sales/order cost reduction, they were incurring twenty dollars of supply chain cost – plus they lost the ability to cross-sell and up-sell the order items, and to influence the product mix.

The Islands of Profit customers, on the other hand, either had less automated ordering, or much better, they followed order receipt with a call back from the order center to reshape the order frequency and product mix.

The solution was to move all the high-revenue accounts to “managed ordering,” in which the client’s customer contracts had explicit provisions that specified order intervals and product review processes to shape the product mix. Since these were previously unmanaged processes, it was relatively painless to implement as part of contract renewal negotiations, and it led to tens of millions of dollars of cost reduction, both for our client and for our client’s customers.

In another major initiative, the client’s marketing group analyzed the profitability of the Minnow customers, and saw that a portion was very profitable, while others were marginal. They started tracking the profitable group closely to ensure that the volume stayed high, and focused more social media on growing the business. For the low-profit Minnow customers, on the other hand, they developed strong processes to ensure that no discounting took place, even at the loss of sales volume.

Before the company intensified its diversification, the product management and sales managers had a very good sense of the business. However, the client’s profit landscape showed that with diversification, this was rapidly breaking down. A more formal category management process, rooted in granular profit information, was needed. This process had to span product selection, product mix management, channel strategy, and supply chain structure, together maximizing every aspect of a product/category’s profit stack.

In response, we helped the client transition to a new category management organization, supported by our profit toolkits, which enabled each manager to use our profit stacks and best practice profiles to maximize the net profits of his/her business. This gave the category managers enormous leverage to implement improvements, leading to strong, measurable net profit gains.

The client, appropriately, had a single dimension supply chain to support its traditional business, in which most of the products had similar storage, handling, criticality and value characteristics. However, the diversification was placing difficult strains on their operation.

Our profit maps showed that the client needed a few very different supply chains to support the diversified business, and that these needs reflected product-types (e.g. bulk, value, handling, criticality), rather than line of business. While they could be run from the same facilities, the DCs themselves needed to be somewhat reconfigured, and in many cases, direct shipments from supplier to customer were a superior solution.

In a second important initiative, the customer order management improvements led to great reductions in supply chain costs. In many major customers, order count was reduced by 30-40%, enabling the client to pare operating costs significantly, and to reduce the number of needed DCs, avoiding a major capital expansion.
INSIGHTS TO ACTION: THE CLIENT RESULTS

Organizations can only handle limited change—you need to make it count!

1. The genius in your business.
Most of Profit Isle clients have been under-resourced in their most profitable segments, where there is huge, untapped profit. The Profit Isle Solution clearly identifies their Islands of Profit, and encourages clients to rapidly accelerate their profits by:
• Growing their Islands of Profits;
• Shifting resources from underperforming areas to the high-profit areas — when, in most companies, the problem areas actually consume the most resources.

2. Pounds per square inch.
All of Profit Isle’s clients have engaged in major initiatives – raising revenues, reducing costs – with limited visibility to their actual net profit impact. And, as seen in the case study above, the effect very often is counterintuitive and opposite.

Profit Isle initiatives can join and support existing client initiatives with more focus and clear all-in net profit expectations. The Profit Isle Solution clearly identifies the largest profit opportunities, and the set of specific tasks that will:
• Drive successful change, starting with two or three major initiatives to maximize immediate profitable growth;
• Where possible, showcase each initiative to demonstrate success and speed company-wide acceptance and deployment;
• Accelerate and sustain profitable growth, through the installation of all-in net profit metrics at the top management level and throughout the organization;
• Drive permanent, company-wide profit maximization, even as the company grows and evolves, though Profit Isle’s Profit Toolkits that optimize the profitability of each manager throughout the company.

3. The whole is greater than the sum of the parts.
Most Profit Isle clients have functional organizations, with each department having its own KPIs. The Profit Isle Solution identifies the surprisingly large opportunities in the gaps in coordinating between the functional areas, not reflected in the functional KPIs, and this opens a huge new set of profit opportunities that are latent within the company by:
• Modifying selected functional department KPIs;
• Initiating focused cross-functional teams to eliminate these profitability barriers.

This is a critically important area: in our experience improving the profitability of tens of billions of dollars of client revenues, many of the most important profit levers are unseen, unmeasured, unmanaged, and nearly painless to implement for both the client and for its customers.