CASE STUDY – CHANGES IN THE NEW MILLENIUM

Over the last fifteen years manufacturers have suffered recession and market saturation, causing them to accurately assess their product ranges, markets and structures and review all operations within the supply chain. As they recognise that higher contributions can be realised from a smaller portfolio of products, the key to survival is being seen as achieving high market share in a limited number of products.

The need for restructuring is being driven by a changing relationship between the manufacturer and the retailer, where the increase in competition between retailers has led to price sensitivity being a key factor in the relationship. Further, the larger retail groups are able to exert enormous pressure in terms of responsiveness and cost reductions. Invariably for the manufacturer the fear of losing production volume to key retailers leads them to absorb increased raw material prices as the retailers either cannot, or will not, pass these costs on to the end customer.

In an increasingly competitive environment, life has become ever more demanding for the food manufacturer. The leveraging of retail buying power forces economies of scale on hitherto unprecedented levels and the rise of the retail own label brands is prompting many manufacturers to review their strategy. They are embarking on major restructuring programmes in an attempt to pare their operations to consolidate and focus on core activities and look towards critical mass as a means of achieving margins.

This in turn is developing a divergence of the industry into two camps - ‘branded’ and ‘own label’ players, thus helping firms avoid the conflict of operating in both markets and supporting the market perception that firms concentrating solely on ‘own label’ offer retailers a superior service.

Whilst cost reduction is pertinent for both groups, the drivers for achieving lowest cost production are different in each case. For own label producers, a clinical understanding of their cost build up throughout the process is essential in being able to control the cost in a structured manner. The branded producers have the issues of innovation and Economic Consumer Response (ECR) in the face of the increased dominance of the retail own labels to keep process costs to a minimum. One fact remains however. Whatever the drivers, only those manufacturers able to operate their factories at peak efficiency will be able to compete profitably in the run up to the new millennium.

This has led to many manufacturers now requiring consolidation, rationalisation and the re-shuffling of portfolios to support the economies of scale necessary in focusing on a smaller section of core brands. Dalgety and Nestlé have provided good examples of this with the former's disposal of Golden Wonder and Homepride in favour of consolidation of its Spillers brand and the latter's withdrawal of Findus from the vegetable sector to focus on value-add sectors.

The result for the manufacturer is that, in order to maintain margins, the reduction of the cost base is essential. The first problem for the manufacturer is that to understand the costs is crucial to being able to reduce them. Traditional costing is insensitive to the variety of activities involved in today's complex business processes, products and services and consequently fails to cost them accurately. An Activity Based Costing programme provides a tool that gives insight and understanding of cost build up through the process.

The problems of understanding the process costs are compounded when we consider the fact that technology in all our plants has reduced the level of direct activities and proportionately increased the level of indirect activities. However, traditional costing fails to recognise this fundamental shift in cost structure. The root cause of many of the problems we find today is the way we allocate an increasing proportion of overheads to a narrowing band of direct activities.

With the cost clarity provided by Activity Based Costing (ABC) we are permitted a more focused and meaningful allocation of resources and budgets. We can concentrate on the activities that need to be performed to both meet the company's objectives, retailer price pressure and eliminate waste within the process.

Problems related to costing and cost clarity are usually further complicated by the highly functionalised organisational structures which typify our manufacturing operations, all with strong departmental measures (such as utilisation, budget variance and output values), coupled with little or no management of the Business Processes. In line with this, company performance measures are not normally customer oriented.

Business Process Management takes the output from the ABC and establishes the true relationship between the way our business operates and the activities and costs that are incurred in delivering products and services. The change from managing functions to processes means that customer oriented performance measures can drive all areas of the business to show dramatic improvements not only in competitiveness but also traditional financial measures.

Such a programme facilitates the elimination of waste through the quantification of Non Value-Adding (NVA) activities. The savings gained by the eradication of NVA can be dramatically leveraged through the other benefits of process improvement by increased customer satisfaction, improved responsiveness, higher quality, lower costs and more flexibility, and the understanding of the added value we can give to the customer.

Finally, underpinning the above should be a comprehensive Lean Manufacturing programme that maximises the companies ability to be flexible, provide the shortest possible lead-time, best innovation, quality, lowest cost and highest customer service, through the eradication of all physical and process waste.

It is only by such a comprehensive overhaul that the manufacturers will cope with the demands of the retailers and provide the margins necessary to delight the shareholder as much as the customer and provide economic justification for both the Brand and the Own Label on our supermarket shelves.

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