

Making Volatility Work for You

A Better Approach to Business Planning and Decision Making

Today's companies operate in a rapidly changing business environment. To drive profitable growth, managers must build strategies and business plans that take this dynamic context into account, aligning a broad range of decisions with key marketplace features. Supply-chain-related and other environmental complexities make this task even more daunting, as managers must assess ever-growing market data to gauge the impact of their decisions on the enterprise. Continual market change requires frequent revisiting of decisions, and drives mounting uncertainty. To thrive amidst these challenges, managers need a forward-looking view of information from inside and outside the organization, along with the capability to use those data in developing and implementing optimal enterprise solutions—frequently and often.

The problem is that traditional decision-making practices seek to address these issues using loosely linked cross-functional teams and spreadsheet-driven analyses that typically offer only minimal variations on historical data. Further, these practices—involving high transaction costs and significant time—result in the inability to integrate several fast-changing forward-looking events into greater understanding of the impact of key decisions on the total value chain and, in turn, the realization of greater value. Not surprisingly, then, many organizations expend significant effort to make marginal progress. This paper presents a holistic framework enabling companies to deploy faster, forward-looking decision-making processes that provide a total view of enterprise impact.

Planning and Decision Making in Corporations

Corporations typically set business objectives for the overall business entity. However, the actual planning and decision-making are performed within independent functional sub-entities based on geography, market, product line, or other dimensions. Sometimes, business-entity-level problems are artificially broken down into smaller, supposedly more manageable problems to be solved independently within sub-organizations. This process fails to account for the linking of the entities by common assets and operational elements, thus failing to develop an integrated view that maximizes the ability to react to changing business contexts quickly and effectively. Managers are forced to look outside the silos to leverage the linkages, business knowledge, and economies of scale resident in the corporation as a whole. That entails the daunting task of making decisions that span multiple complex multi-echelon supply chains, product lines, functional entities, business units, geographies, and even companies, and impact the company's capability, cost and customer service. There are three major reasons this decision-making practice is suboptimal.

1. Distributed, local knowledge and biases: The expertise and information required for effective decision-making typically reside within different individuals and incompatible information systems. Establishing a cross-functional team with the appropriate expertise and information (often from un-reconciled sources) to make value-adding decisions can be slow and costly. Moreover, the members of such cross-functional teams will likely represent divergent interests, organizations, functional expertise areas, and points of view, and be handicapped by the lack of a holistic cross-functional framework for decision-making. As such, decision-making is largely governed by oversimplified quantitative models and suspect qualitative factors including experience and 'gut-feel,' rather than fact-based analytical reasoning. Most critically, the process inevitably fails to account for variances in the marketplace, preventing timely responses—whether related to sourcing, product introductions, or pricing.

2. Slow, inadequate methods: A purely cross-functional team-based approach will generally be hampered by suboptimal solution-development methods, limiting efficiency and impact. Teams select an option from those generated by individual members. The initial set reflects team members' limited ability to visualize options available in the integrated supply chain, based on their experience and functional knowledge, precluding higher-order and/or counterintuitive solutions based on hidden opportunities or pitfalls. Many strategies fail because the teams behind them never explored these less obvious solutions.

3. Failure to build a flexible, responsive ongoing business: Most traditional business analyses (e.g., for sourcing and capacity-building initiatives) tend to be one-time initiatives carried out manually. But courses yielded by previous decisions must be continually adjusted to prevailing business conditions. Due to the large cost involved in recreating multiple detailed scenarios based on different projections (e.g., variations in demand, product mix, sourcing costs), companies tend to avoid frequent reviews of operating strategy, risking severe misalignment with their business environments and markets.

Saddled by the lack of a repeatable, cross-functional, holistic analytical framework for decision-making, companies make slow, short-sighted, risk-averse, suboptimal decisions. Implementing such a framework can reduce total value chain costs up to 15%, diminish risks of poor decision-making, and improve response speed.

A New Business Planning and Analysis Framework

An effective business planning framework must deliver three critical functions: providing an internal and external forward-looking view, assimilating and reflecting internal linkages, and identifying and optimizing cost and operational implications. An ideal framework yields an actionable plan for a finite horizon using a collaborative environment and enterprise optimization, with a process that takes days, not months. Such a planning framework, combined with a recurrent re-engineering process, should significantly impact performance. The company can respond to variances in real-time, visualize and anticipate internal/external constraints, and revisit solutions faster and more effectively. For example, a company may discover that a near-term supply shortage will drive a 5% cost increase for a longstanding customer, and allow the customer to choose among a price increase, alternative products, or price averaging, protecting the relationship. The holistic framework delivers value through three related areas:

1. Planning: The ability to incorporate inline forecasts based on external (e.g., market fluctuation in demand and supply costs) and internal (e.g., decisions related to capitalizing opportunity windows) real-time data is critical. While forward-looking forecasting information is available today, the cost of frequently refreshing data and redoing analyses is prohibitive. Consider, for example, the process of planning promotions in light of updated demand forecast or commodity prices. As the event planning horizon nears, the firm can decide whether to continue the promotion, how to price it, and how to source the products—decisions best taken within weeks, not months. Using an optimal framework will help the company maximize the opportunity.

2. Collaboration: The enhanced ability to assimilate information in an inline process can be used by capturing the right information along the process steps and allow fast contextual information exchange. In the previous example, the proposed promotion may require a significant increase of raw material in a certain time window. The improved planning/forecasting process will enable suppliers to see the demand and respond with price impact, supply strategies, and other input the buying manager reviews.

The buyer then uses optimization decision support to determine the best enterprise supply plan, which is instantly available to marketing to update pricing assessments. Again, this exercise can be completed in weeks, rather than months.

3. Cost Optimization and Modeling: The framework enables decision-makers to understand the impact of any decisions on their business's financial and operational metrics. For example, a decision to reduce plant inventory might affect freight costs, service levels, and the P&L and balance sheet at points further downstream in the supply chain. The framework captures such cascade effects by incorporating a thorough understanding of the business's cost structure, end-to-end operations, and their interdependencies. The framework gathers the functional knowledge of individuals organization-wide into a repository, to yield this understanding.

Developing the Optimal Framework

How can such a framework be developed? A quantitative framework that integrates activity-based costing principles with sophisticated value chain (includes manufacturing) modeling can accurately capture interdependencies between operations and costs. Mathematical tools such as optimization further empower the system by identifying optimal, and often counter-intuitive, decisions given real-world constraints. Given the complexity of operational characteristics, such frameworks need to be computer-based, rather than ad hoc. The system integrates data from disparate systems (e.g. ERP, MRP, Accounting) with forward-looking information.

Benefits of Using Such a Framework

An effective system enables managers to plan by rapidly evaluating multiple scenarios representing different operating decisions and/or business parameters, assessing trade-offs among the costs, service levels, lead times, markets served, product offerings, and other areas associated with different operating decisions. The framework can also help senior managers and investors understand the costs, benefits, and risks represented by shifting environmental factors, along with allowing review of past decisions—and outcomes—based on updated information.

A computer-based information system that incorporates supply chain modeling, activity cost drivers, and optimization techniques can address up to 90% of typical business decisions, enhancing the visibility of future outcomes to increase the speed and quality of business decisions, unearthing hidden value in today's fast-changing environment.

About SCA Technologies:

For over a decade, SCA Technologies has provided category sourcing and cost management solutions that help industry leaders maximize profits by better managing market, supply and demand volatility. Supply chain, procurement, finance and corporate social responsibility professionals use the unique cross-functional approach of the SCA Planner™ suite to make better decisions for billions in category spend each year. With our patented technology, customers can finally address the tough challenges of volatile commodity prices, extended supply chain networks and corporate social responsibility tradeoffs in a coordinated manner. Our innovative, cloud-based solutions deliver increased visibility and quicker response, leading to an average 3-5% reduction in the cost of goods sold on an annual basis. Learn more at www.SCAtech.com.