



How restaurant supply chain management can boost profits and build market share

Executive Summary

Caught in a vise—squeezed from one side by cutthroat competition and rising consumer demands, and from the other by increased costs and supply chain complexity—restaurant chains are pressured as never before to manage volatility and maximize profits. Yet at many chains, functions including supply chain, procurement, finance, menu management, operations and marketing fall short in responding to this crisis, largely because they are struggling with outdated practices and legacy systems.

Best practices in farm-to-fork supply chain and procurement orchestration are the only way for restaurant companies to build resiliency and enhance their competitive position in today's marketplace. Next-generation solutions and modern business processes allow managers to source fresher products at lower cost; improve promotions and new product fulfillment; and do their part to deliver higher, more predictable and more reliable margins for their company and franchisees. This paper provides three case studies from SCA Technologies that illustrate best practices for boosting profits and market share for your business today.

Background

Restaurant supply chain, procurement, finance and menu management executives are facing an unprecedented conjunction of complex challenges from farm to fork, including:

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- INDUSTRY COMPETITION:** A mature market with little real growth; weakening power, reach and profitability of large chains as smaller chains and non-restaurant players gain share of stomach.
 - CONSUMERS:** Stronger-than-ever consumer resistance to menu price increases . . . but also higher expectations for quality, freshness and novelty; increased demands regarding sourcing.
 - MENU FULFILLMENT CHALLENGES:** A drastically shortened go-to-market process for new menu items; more LTOs and seasonal items; more emphasis on fresh foods and in-house prep.
 - SUPPLY CHAIN PRESSURES:** Increased volatility in commodity price and availability; disruption and cost pressures in the distribution chain; deteriorating transport infrastructure/capacity.
 - INFRASTRUCTURE INVESTMENT:** The imperative of investing significant sums in frequent front-of-house and back-of-house upgrades chain-wide to maintain or enhance competitive positioning.

- ✓ **FRANCHISEES:** Increased insistence from franchisees for transparency regarding food costs and the potential profitability of menu items they are required to offer.
- ✓ **LABOR:** Pressures on minimum wage and prevailing wages, employee benefits; shortage of qualified and reliable labor in some areas.
- ✓ **GOVERNMENT:** Enhanced food safety regulations and increasing demand for traceability.
- ✓ **INVESTORS:** Pressure on managers to demonstrate quantifiable best practices in cost control and menu optimization so the chain can receive equity funding for future growth.
- ✓ **INHIBITORS WITHIN COMPANIES:** Silos in corporate structures that hinder collaboration; data overload as the rising volume of information captured exceeds companies' ability to analyze and profit from it.

[Conventional Wisdom]

"New menu items are where we build traffic and sales—not from pushing commodity costs lower and lower."

"Food costs aren't our real problem. It's labor, store upgrades and other costs that are killing us."

"Everyone in the industry is facing the same cost pressures, so there's no need to take steps that others aren't taking."

"The commodity cost cycle is coming down right now, so we'll be okay."

"We use eSourcing/RFP to bid out fixed-price contracts."

"We have new procurement and supply chain software, so we're in good shape."

[Reality]

Most people still order from the regular menu or value menu. Chains must maintain menu quality, check averages and value across the menu.

Restaurant chain success lies in the simultaneous management of all costs as well as the ability to seize competitive advantage through purchasing.

Restaurants have reached their limit on taking menu price increases. To compete, chains must bring their cost structure to a leadership standard.

Management of commodity costs not only mitigates downside risks but also creates upside opportunities to gain competitive advantage.

Restaurants that use an eSourcing/RFP process can sacrifice flexibility and gain a false sense of security. Vendors pad up their bids so the risk is all on the restaurant company.

Current software only attacks each silo; companies need farm-to-fork cost visibility and cost management. But traditional supply chain software focuses only on fulfillment and inventory. To get products to your restaurants—profitably—requires looking all the way back to the vendor and making the right tradeoffs between additional capacity and overtime using a more dynamic sourcing model.

The Imperative

As we have seen, restaurant supply chain, procurement, finance and menu management departments are under pressure, squeezed from one side by customer demands and from the other side by cost constraints.

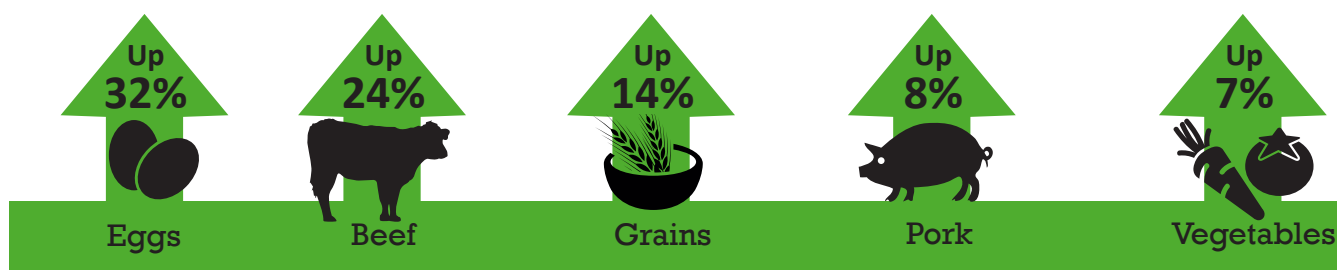
Inputs of food and supplies represent, on average, about 30% of all costs for restaurant chains. The executive suite sees these costs as more amenable to management than other high fixed costs such as labor and infrastructure improvement. Supply chain, procurement and finance professionals are expected to play a heroic role in holding down costs, but must also do their part to uphold menu quality and reliability—or the chain risks decline or death.

In such an environment, the best practices outlined in this paper are the **only** options that will allow restaurant chains to maintain profits and enhance their competitive position in the marketplace.

Chains that employ SCA Technologies reduce store food costs by 3%–5%

Producer price index rises in 2014

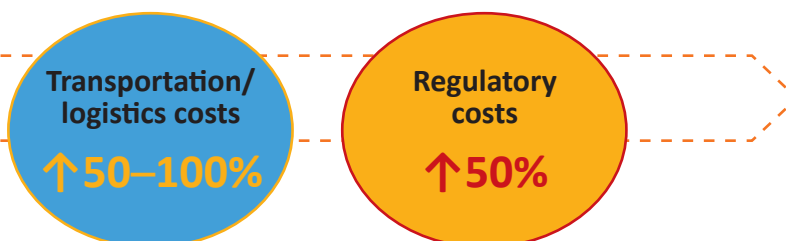
YOY Dec 2013–Dec 2014



Source: Bureau of Labor Statistics

COST PROJECTIONS (next 5–7 years)

Source: Technomic Inc.



Expert Assistance to Solve the Sourcing and Supply Chain Crisis

SCA Technologies has strong evidence that its farm-to-fork solutions and skills can help major restaurant chains address these critical issues, saving millions of dollars and significantly enhancing their bottom line. *SCA Technologies has enabled its clients to annually achieve over \$100 million in savings and migrate to world-class supply chains.* This white paper discusses instances in which SCA Technologies has successfully worked with major restaurant companies to transform the sourcing and supply chain function, and will conclude with Key Takeaways targeted to executives at large chains.

Unsnarling the Knots: Expert Supply Chain Solutions in Action

SCENARIO ①: SOLVING A CRISIS IN FOOD/PAPER COSTS AND STORE MARGINS

A national restaurant chain was facing commodity-market volatility impacting input costs and store margins, particularly in connection with the promotions calendar. Increasingly, the chain relied on risk management to insure against market volatility. But using a cumbersome Excel-based method, managers in supply chain, finance and procurement had ever-greater difficulty

understanding raw material and production needs for the latest demands. Planning didn't move efficiently from the latest demand forecast to projections for supply, risk management and cost.

Solution: SCA helped the chain implement a shared system to analyze commodity forecasts, hedges, supplier costs and store-level food and paper costs. Executives could now see cost of goods sold and margin projections in real time, including the impact of commodities, conversions and freight. "What-if?" scenario analysis now allowed them to switch out volumes, costs and commodities to get a full price and demand picture and deeper understanding of what drives margin. Dynamic risk management was enabled by instant updates to commodity purchase requirements, driving marketing calendar changes and demand forecasts.

Result:

- 95%+ improvement in forecast accuracy
- A reduction of 25-50 worker days per quarter in time required to compile food and paper forecasts
- Enterprise platform for collaboration among finance, sourcing, risk management and suppliers
- Real-time updates to COGS and margin forecasts with commodity or sourcing changes

SOLUTION IN ACTION

Solving a crisis in food/paper costs and store margins: With SCA assistance, the chain could see market-basket risk in real-time with the latest base and LTO volumes, as shown here.

| | UOM | Volume Needed | Volume Hedged | Commodity Spend (MM \$) | % Commodity Spend At Risk |
|--------------------|---------|---------------|---------------|-------------------------|---------------------------|
| Commodities | | | | | |
| Shortening | MM lbs | 4.50 | 1.00 | 2.43 | 79.38% |
| Flour | MM lbs | 135.00 | 70.00 | 31.65 | 51.34% |
| Corn | MM bu | 11.00 | 5.00 | 69.05 | 56.52% |
| Soymeal | MM tons | 0.11 | 0.00 | 46.22 | 100.00% |
| Sugar | MM lbs | 22.50 | 5.00 | 4.85 | 79.38% |
| Block Butter | MM lbs | 7.07 | 0.00 | 7.51 | 100.00% |
| Barrel Cheese | MM lbs | 82.22 | 53.05 | 139.22 | 36.00% |

SCENARIO ②: SOLVING THE CHALLENGE OF BEST-IN-CLASS FOOD SOURCING AT TARGET COST

As changes in the supplier industry and supply base added complexity to the purchasing function, a national restaurant chain was urgently challenged to improve food sourcing with reliable supply at target costs. Changing sourcing requirements and product mix made it hard to get the best products at the lowest cost, and the chain struggled to build strategic supplier relationships and keep down costs in an uncertain supply and demand environment.

Solution: SCA's next-generation software and services helped the chain optimize sourcing by uncovering true supplier cost structures for sourcing decisions and negotiating leverage. Emerging constraints, such as verified sustainable sourcing and animal welfare practices, were incorporated. Supply chain executives could now update sourcing for LTOs and promotions in real time, and could track savings from sourcing changes. Supplier performance management allowed them to measure variances against the contract, the budget and the prior year, and to identify opportunities via supplier benchmarking. Automated exception reporting allowed them to manage outliers.

Result:

- A 3%–5% reduction in food and paper costs
- Notable impact on margins—cost of the new solution was offset within a month
- A reduction of 25–50 worker days per quarter per category in time required to manage sourcing and suppliers
- Assured supply for core products, LTOs and promotions

SOLUTION IN ACTION

Solving the challenge of best-in-class food sourcing at target cost: SCA helped the chain evaluate sourcing alternatives for LTOs, seasonality and supply constraints, as shown here.

| | UOM | LTO Supply Scenario | Optimized Sourcing—NO Constraints | Impact | Impact % |
|---------------------|---------------|---------------------|-----------------------------------|----------------|---------------|
| Total Volume | MM lbs | 573.68 | 573.68 | 0.00 | 0.00 |
| Plant A | MM lbs | 123.97 | 145.67 | 21.70 | 17.50 |
| Plant B | MM lbs | 375.39 | 328.67 | (46.72) | (15.30) |
| Plant C | MM lbs | 74.32 | 99.34 | 25.02 | 36.43 |
| Cost | MM \$ | 769.81 | 754.75 | (15.06) | (1.96) |
| Conversion Cost | MM \$ | 197.15 | 185.67 | (11.47) | (5.82) |
| Commodity Cost | MM \$ | 526.72 | 526.72 | 0.00 | 0.00 |
| Packaging | MM \$ | 23.03 | 19.79 | (3.24) | (14.07) |
| Freight | MM \$ | 22.92 | 22.57 | (0.34) | (1.50) |

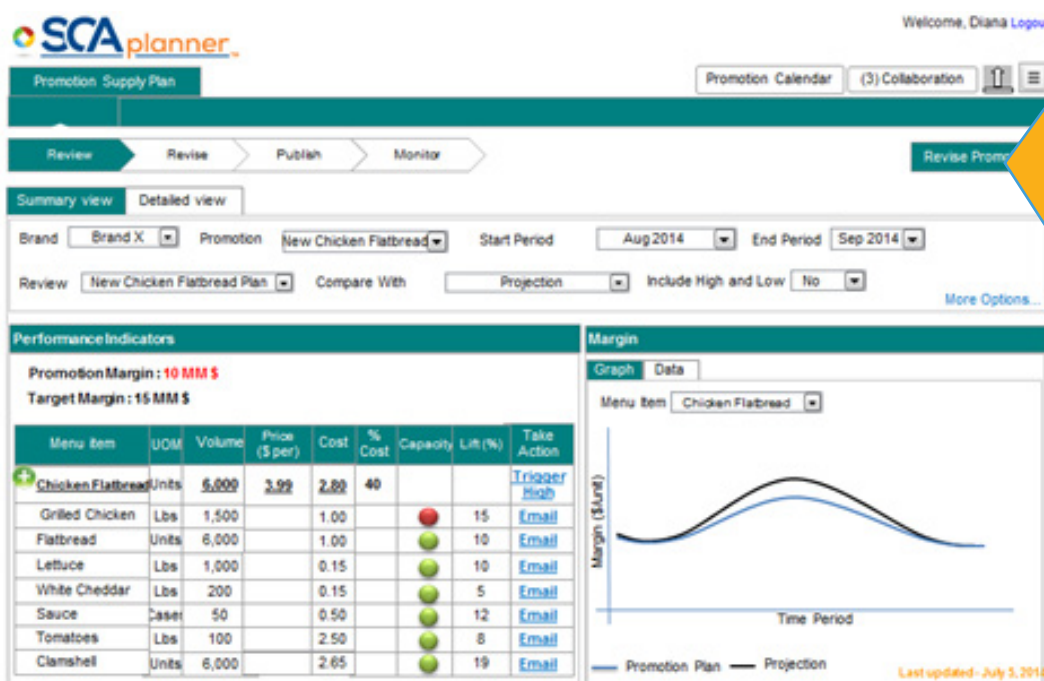
SCENARIO ③: SOLVING A MARGIN AND MARKET SHARE CRISIS WITH GUARANTEED, SUSTAINABLE SUPPLY

A national restaurant chain faced ever-greater pressure to increase market share and gross margins with focus on promotions and new products, balancing assured supply with minimal product obsolescence/spoilage. Changes in sourcing requirements, mix and supply base were making it harder to assure supply at target costs; in particular, greater emphasis on fresh products required increased diligence in supply planning and inventory management.

Solution: SCA worked with the chain on margin-driven supply planning to optimize real-time supply plans and inventory allocations. Chain executives gained greater understanding of available supplier capacity for their company's core items and LTOs, and were able to fine-tune supply plans and inventory allocations in real time. Running "what-if?" scenarios for capacity, inventory and cost enabled rough-cut capacity and contingency planning. Managers could improve planning and execution of LTOs and promotions by analyzing margin scenarios and creating responsive supply plans for high-volume and low-volume contingencies.

Result:

- 1%–2% increase in revenues for LTOs and promotions
- Assured supply with minimal obsolescence for core products and LTOs
- A reduction of 15–25 worker days per LTO/promotion in time required for data collection, analysis and communication
- Development of a farm-to-fork enterprise platform for collaboration across promotions, supply, sourcing, finance and suppliers



SOLUTION IN ACTION
Solving a margin and market share crisis with guaranteed, sustainable supply: SCA solutions provided margin visibility for all promotions, as shown here.

“SCA has saved our system in excess of \$100 million. Their ability to integrate strategic sourcing requirements into the supply processes has been instrumental in enabling partnerships within our organization while driving value in the supply chain.”

VP, Supply Chain, Large QSR

“SCA’s application has been tremendously valuable for continued success and collaboration with our customers.”

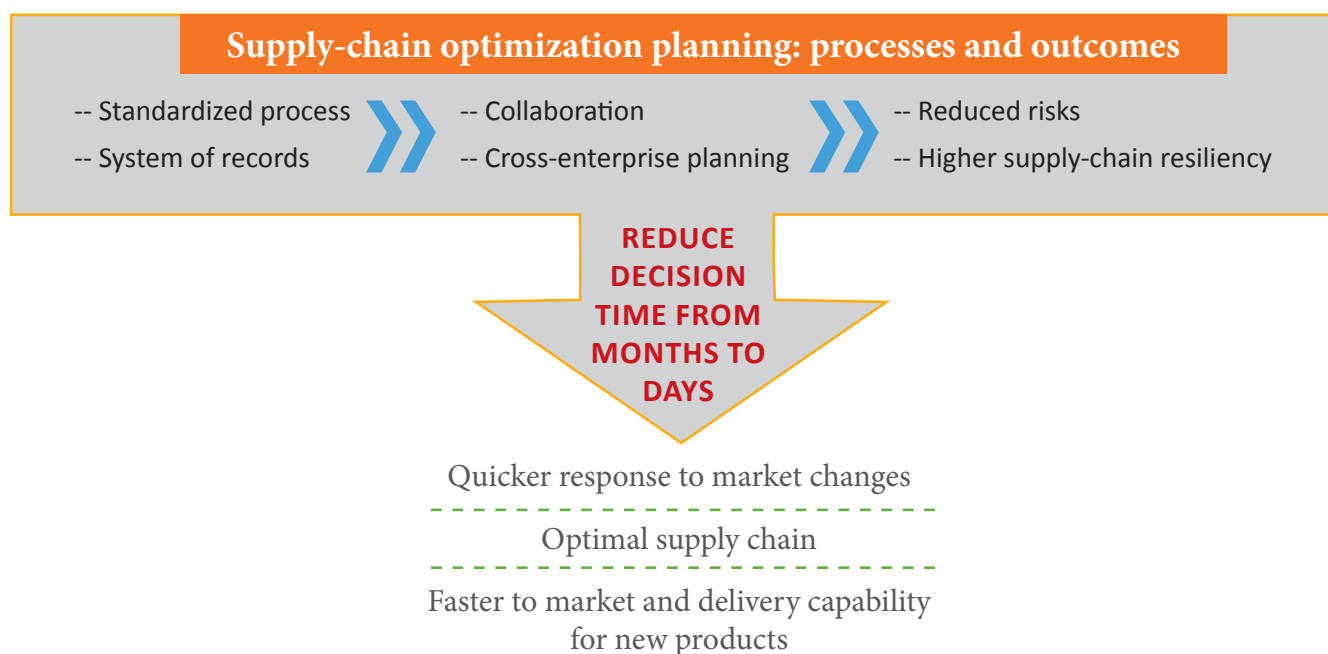
Group Controller,
Large Foodservice Manufacturer

Key Takeaways

Procurement and supply chain organizations within large restaurant chains can be overwhelmed as they face today’s extreme challenges, in part because they’re often using outdated practices and legacy systems. These practices and systems have become dangerously ineffective in addressing the dramatic commodity challenges and competitive pressures that will only increase over the coming decade. In many cases, chains are at risk of declining or even dying if they delay in facing the crisis. Something has to change—right now.

SCA clients are seeing tremendous benefits and will continue to do so in the coming decade. Chains realize these benefits in three key areas:

- **Fresher products at lower costs.** Farm-to-fork supply planning delivers fresher products while achieving reductions in COGS, typically of 3%–5%. Chains are able to reduce the time it takes to collect and analyze data from months to days, and from days to minutes.
- **Improved promotions and new product fulfillment while delivering target margins.** SCA’s software and services help chains align decisions across the enterprise for store level impact. The system can be extended out to supply chain partners, creating a seamless supply chain that is updated for store optimization. This agility generates better responses to changes in demand, promotions and products, helping to fulfill chain needs at better margins.
- **Higher, predictable and reliable store margins.** Deep farm-to-fork cost planning and forecasting with resulting proactive business and marketing planning is necessary to generate reliable margins in today’s environment. This margin reliability is what chains need to gain collaboration and involvement from stores, leading to successful transformation and growth.



Utilizing SCA Technologies' suite of software and services, restaurant chain executives can take effective control of multiple data streams, build cross-functional collaboration within their organization and with supply partners, enhance executive-suite visibility within their organization, and make a measurable and significant year-over-year impact on the bottom line.

As more chains migrate to sophisticated farm-to-fork software suites and consultant services to manage procurement, supply chain, finance, menu management and marketing functions, those that delay are in danger of falling further and further behind.

The good news is that with the right integrated business process and the underlying software system, restaurant chains can acquire the capability to deliver inputs effectively in this difficult environment. A tailored version of a multifaceted procurement, supply chain and finance software suite—designed specifically for large restaurant chains and supported by expert consulting from supply chain specialists with a proven track record—can enable chains to overcome these hurdles and build the platform for growth they so critically need.



About SCA Technologies

SCA Technologies is a provider of patented software, services and business process consulting for the restaurant industry, offering a unique farm-to-fork cross-functional approach for category sourcing and cost management. SCA Technologies uses “Big Data” and predictive analytics to optimize supply chain functions and margin-driven supply planning. And, unlike other providers, SCA helps clients achieve a more comprehensive view by including commodity market modeling and hedging for COGS risk management, among other aspects of procurement and supply chain. SCA solutions include sourcing optimization and supply planning, COGS forecasting, margin-driven sales and operations planning, LTO planning and execution, risk management and supplier performance management.

The company, with offices in Pittsburgh, Chicago and India, has a 16-year track record of delivering supply chain excellence. SCA customers include McDonald's, Yum! Brands, Church's Chicken and many other leading chains. Since 1999, SCA Technologies has enabled its clients to annually achieve over \$100 million in savings and migrate to world-class supply chains, with their investment in SCA software, services and consulting typically paying off at least tenfold in improved margins and profits. For more information, please visit www.scatech.com.