Value-Oriented Supply Chains

Delivering what customers expect while keeping profits up

Supply chains are usually handled with broad strokes—the commercial and marketing sides seek to meet all supposed customer needs, while the supply chain area aims to serve customers while optimizing costs. A more focused, segmented and collaborative view of the role of supply chains can be more valuable for companies and their customers. By determining how to give each customer segment what it values, firms can balance the tradeoffs between offering the service customers want and expect while keeping profits up.

Defining how to meet customer needs while remaining profitable is the vital balancing act companies face in handling their supply chains. The most effective supply chains result not from simple cost-reduction and optimization, but rather when those efforts are conducted in collaboration with a company’s commercial efforts and focused on meeting customer needs.

To achieve this, a new perspective is needed, one in which supply chain leaders understand what each customer segment values while maintaining a lean supply chain and weeding out unnecessary complexity. By increasing transparency for all stakeholders—logistics employees, salespeople, customers, distributors, manufacturers and suppliers—supply chains can become a vital place for improving competitive advantage.

Creating a Company-Wide Vision

Offering value to customers is a mandate for the commercial and marketing areas of a company, but the supply chain has the tools to contribute as well. The two sides must cross departmental lines to meet customers expectations in terms of logistics, and to control costs at the same time. Doing so requires a vision that considers the supply chain comprehensively rather than on a function-by-function basis. By viewing the entire supply chain, you might find that certain customers are getting more than they need while others are actually willing to pay more for an offering.

The best results occur when all relevant parts of your offer to the customer—commercial, distribution, channel and logistics—are designed together. This guarantees that customers are getting what they need while the company maintains a desirable level of profitability. For example, you may offer certain customers a higher discount for reducing the frequency of their deliveries; that helps you and the customer. It cannot be done without a cross-departmental vision.
Segmenting by Value

Many people believe that customers want everything for free. We think this is overly simplistic: Price is a major factor, but it is only one part of the “value” that goes into a purchase decision. If customers perceive an offer is truly worth it, they will pay for it, even if competitors have a lower price. To make such an offer, however, you must know exactly what your customers need and at what price, balanced against what it costs the company to deliver it.

Doing this is, of course, a difficult task—the customer may not even know. Additionally, simply meeting customers’ wish lists or offering the lowest prices is too simple. This is solved by segmenting your customers by what they value, how profitable they are to your company, and what services you can offer them (see figure 1).

Serving the Segments

Armed with an understanding of customer segments, supply professionals can use a cost-to-serve model that maps the costs and cost drivers of each proposed offering, defines the cost per client, and assesses the impact and expected results. In the client example in figure 2, 3 percent of customers provide nearly half of this company’s profits, while the majority offer either marginal contributions or even net losses.

A large construction material company used this approach to improve the sales and profit contribution of several customers after numerous failed attempts to improve supply chain costs and increase customer satisfaction. We had found that the company was trying to deliver too much by offering the same high service level to all customers, whether or not they needed or wanted it. We suggested a more nuanced approach—segmenting customers by their major requirements (derived from research) and then redefining how each should be served. Smaller, less strategic customers were transferred to new, indirect channels. This company stopped trying to deliver peak service for every customer and instead defined strategic customer segments to serve better and more directly. In the end, costs remained the same but the company was better able to serve more rewarding segments.

In another example, we helped another company serve a new segment that had previously been neglected. Our client began accepting different prices for the same product—for example, a lower price, if the customer planned the order in advance, and a higher one for emergency deliveries. In both cases, the firms created more value-oriented supply chains that generated higher profits from more customer segments, and that customers perceived to be more valuable than what competitors were delivering (see figure 3).

Directing Your Indirect Channels

Your indirect, or third-party, distribution channels must be part of the discussion when it comes to creating a customer-focused supply chain. These
channels are as relevant to your customers as any other players in the supply chain, and a smart approach to them can increase your market coverage and share to more satisfied consumers while you also retain a loyal and coordinated network of distributors.

Several of our manufacturing clients developed new programs for developing distributors’ capabilities to ensure they more closely represented the company in the eyes of their customers. They did this by reducing competition among distributors, finding new areas of value for them through joint marketing and technical services, and designing efficient logistics models.

In the end, our clients and their distributors were getting more value from one another, and end-customers were more satisfied.

Implementing a New Perspective

How can you get the whole organization to buy into this new perspective? There are three requirements:

Get a strategic view of customers. The commercial and logistics sides must share an understanding of all channels and customers and their perceived values, and prioritize them to create focused propositions.

Realign the organization. All areas must have a clear understanding of the benefits, and all decisions must be based on a detailed, quantitative analysis. This allows for a flexible supply chain design with simple and specific policies on how to serve each segment. This is critical for creating more accurate demand forecasts for the items and customers that really matter.
Persevere. A trial-and-error period is to be expected—in fact, it is a vital part of implementing the most profitable and most effective supply chain.

Focusing on the Customer
The supply chain is not simply an area where costs can be cut. Using a more measured approach can yield not only revenue opportunities but also areas where you can build a valuable competitive advantage. With a commercially focused supply chain, you can learn who your key customers are and serve them better. In the end, they will get what they want and your company’s performance will be stronger—and value will be generated for both.

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