Sales and Operations Planning: Making BPM Work

In many companies, financial planning remains separate from sales and operations planning processes. This disconnect can hamstring corporate performance and undermine BPM efforts.

by Mark Smith

Mark Smith is the CEO and executive vice president of research for Ventana Research, a research and advisory services firm focused on the performance management market.

©2008 GARY KEMPSTON C/O THE ISPOT.COM

SALES AND OPERATIONS planning (S&OP) has gotten the attention of business leaders, for obvious reasons. S&OP is a set of companywide planning and decision-making processes designed to balance the supply of products (or services) with the demand for them and to link day-to-day operations with business goals, operational planning, and financial planning. The purpose of S&OP is to enable senior management to reach consensus on a single operating plan that allocates critical resources optimally so that the company can hit its performance targets.

Considering the importance of S&OP, it's surprising that some companies which use sophisticated financial planning technologies still relegate sales and operations planning to spreadsheets. Even among companies that embrace S&OP technologies, many do so without first considering how they will connect the systems to their financial planning and budgeting process. This hastiness often leads to disconnected operational plans; missed goals and targets; and, overall, unsuccessful business performance management.

Effective corporate planning requires that companies use effective, integrated processes — and technologies — both for traditional business performance management (BPM) and for planning the operational activities and resource allocations that underlie the financial plans.

The Need Driving S&OP Software

The concept of S&OP was born as a manufacturing and supply chain process that focused only on balancing supply with demand. It has evolved since then, as companies have begun to see how it can

help them address the complexities of globalization and the uncertainties created by changing customer orders, supply disruptions, product revisions, and new sales opportunities. Customer demand for quicker response, the ever-increasing variety of products on the market, and a need to deliver the hottest new items faster and faster all add to the allure of improving sales and operations planning processes.

Having a flexible method for allocating resources in today's constantly changing external environment is crucial, yet many executives find that their BPM processes and systems do not adequately support comprehensive operational planning. One common stopgap is to augment BPM systems with spreadsheets. But spreadsheets are notoriously problematic; because they are disconnected from the underlying data, users make assumptions based on data that may be out of date.

Moreover, a spreadsheet cannot provide a comprehensive view of the business-impact trade-offs of a supply decision on the company's procurement, manufacturing, operations, sales and marketing, and finance functions. When a company uses spreadsheets for sales and operations planning, individual departments base plans on their own set of business assumptions and their own market perspective. Sales may develop its revenue forecast based on the current pipeline, while finance creates an operating plan based on current-year budgets, marketing creates product forecasts based on its demand-shaping activities, and manufacturing plans based on its supply outlook. Additionally, each group will frame its forecast differently: Sales revenue forecasts will break down by region and customer, the marketing team will forecast in unit sales by product line, financial forecasts will be measured in currency by internal organizational unit, and manufacturing forecasts will be delineated in units by SKU and part number. It will hardly be surprising, then, when corporate executives have trouble reconciling these different plans, assumptions, and perspectives to produce a single plan for the organization.

In such a situation, the planning processes, metrics, and reporting for individual departments will likely not link clearly and consistently to an overall organizational strategy and set of objectives. In fact, different functional groups may turn out to have incompatible goals, which creates conflict that strains relationships and hampers the company's ability to meet customer expectations. The results are operational ineffectiveness and a high incidence of problems such as mistrust of other departments' plans; unmanaged plan changes (i.e., a lack of transparency about who made what changes, when); flawed communication; and a lack of consensus across functions about how to respond to problems.

This scenario is all too common among businesses that give spreadsheets an integral role in their planning processes. In contrast, recent benchmark research by Ventana Research indicates that high-performing companies are re-examining the important role of integrated business planning in achieving better performance. In particular, they are focusing on sales and operations planning to ensure that their financial plans are built on a solid foundation.

What We've Found

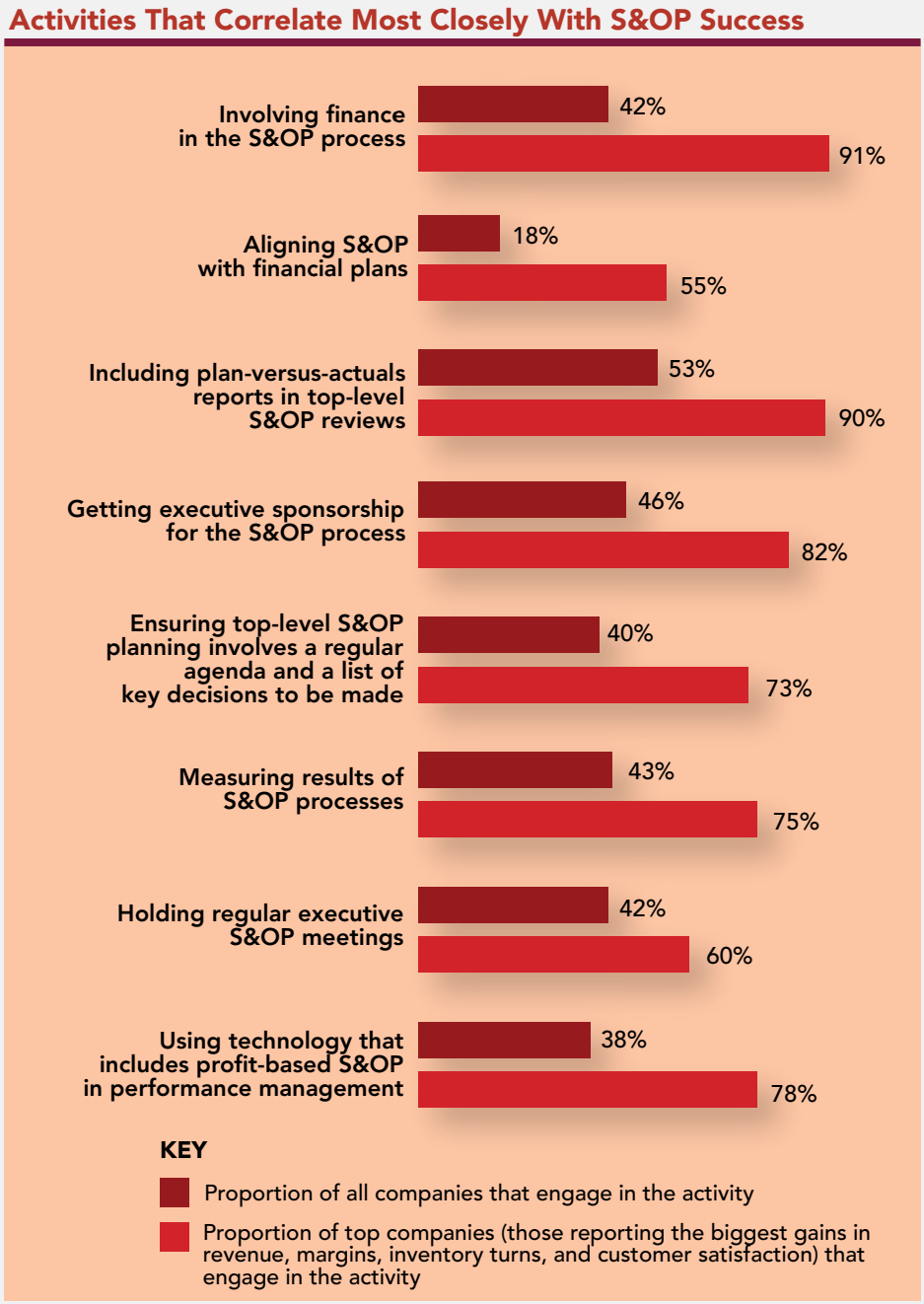
At its core, S&OP is an aggregate planning process, and doing it well brings rewards. Our benchmark research program, entitled "Sales and Operations Planning," involved 470 professionals from a range of industries. The largest segment of participants (34 percent) work in manufacturing, followed by service industries (18 percent) and banking and finance (11 percent). Twenty-four percent work in companies with fewer than 1,000 employees; 28 percent in companies with 1,000 to 4,999 employees; 20 percent in companies with 5,000 to 9,999 employees; and 28 percent in companies with 10,000 or more employees.

According to our research, the top-performing companies — those that experience the largest year-over-year percentage improvements in revenue, margins, inventory turns, and customer satisfaction — all practice sales and operations planning at the strategic level. In other words, for them, S&OP is a consolidated planning activity led by senior management that includes all lines of business or brands and all factories or regional operational facilities, across all product lines. For these top-performing companies (about 7 percent of participants in our research), sales and operations planning involves at least six steps every month: new product introduction planning; consensus demand planning; supply and resource capacity planning; formal demand, supply, and capacity reviews; financial plan reconciliation; and formal executive S&OP meetings.

We also found that these organizations are the exception, not the rule. Most companies are new to S&OP. Despite the fact that best

Exhibit 1

Exhibit 2



practices have been known for nearly 20 years, only 35 percent of companies have had a formal S&OP process in place for more than five years. Thus, most companies' S&OP processes lack the type of rigor most organizations apply to their financial accounting and reporting processes. This is a shame, because organizations that apply rules rigorously and utilize dedicated software in S&OP outperform those that do not.

Our benchmark research found five significant insights into what it takes to effectively combine S&OP with financial performance management:

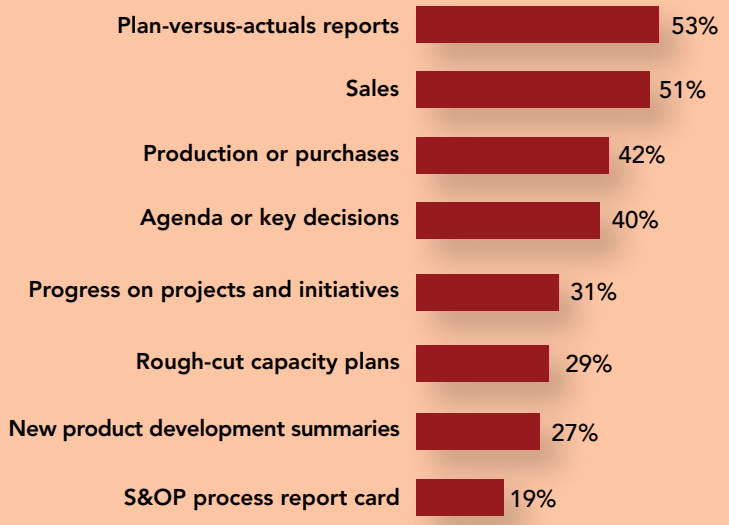
Benefits should be measured. We sought to identify the benefits that users associate with sales and operations planning, and whether companies measure those benefits. We found that the top four benefits companies expect to achieve by improving S&OP are better customer service, better inventory utilization, better asset utilization, and better budgeting. Yet only 18 percent of companies actually measure customer service as part of their S&OP initiative. Worse, only 11 percent of companies measure inventory turns, and only 8 percent measure asset utilization as part of the S&OP processes that they set up. While most companies probably measure these factors elsewhere, the data is usually absent from S&OP activities; thus, most companies' S&OP processes lack a performance management focus.

We found this problem to be pervasive. As exhibit 1 on page 5 indicates, the main problem obstructing companies' improvement of S&OP processes is not the availability of IT resources, but rather a siloed approach to performance planning in which multiple instances of business function planning occur in isolation from one another. Ventana Research concludes that to best help the company meet its financial performance goals, finance and operations must collaborate on forecasts; otherwise, finance will project one goal and operations another.

When plans are aligned, performance improves. According to our research, only about half (52 percent) of companies do a good job of aligning departmental plans with overarching corporate goals. We also found that when companies use S&OP to adjust their financial, sales, marketing, and executive management plans — that is, they use the S&OP plan as the "plan of record" and set other plans and budgets accordingly — they see significantly greater performance gains than companies that don't organize their planning efforts around S&OP. Along the same lines, companies that do a good job of aligning their financial plans with their sales and operations plans hit their targets more often. In fact, our analysis revealed that this alignment is the single most significant factor contributing to performance

Exhibit 3

What information is included or packaged for your highest-level or executive S&OP meeting?



improvement (see exhibit 2 on page 6). Most companies reporting strong improvement in revenue, gross margins, customer satisfaction, and forecast accuracy said they align financial and S&OP plans closely.

Ventana concludes that reconciliation of sales and operations plans with financial plans is critical for successful S&OP and for attaining overall performance goals. If finance and operations functions plan in silos — and thus their revenue, cost, inventory, and capital plans are not aligned — the company will have difficulty achieving financial or corporate performance management objectives. Its ability to hit earnings, growth, and margin targets will always be in doubt, both inside the organization and among investors and other outside stakeholders.

Executive sponsorship and finance involvement are imperative. Our study found that involving finance and executive management in the S&OP process is the second most significant determinant of whether a company will improve its revenue, profits, customer satisfaction, and forecast accuracy. Finance is involved in S&OP plan development in roughly two-fifths of companies. But 90 percent of companies that reported significant gains in revenue, 70 percent of those that reported gains in gross margin, 56 percent of those that reported gains in forecast accuracy, and 76 percent of those that reported gains in customer satisfaction include finance as part of their S&OP process.

Ventana also found that the companies in which the CEO, general manager, or CFO sponsors the sales and operations planning process achieve the biggest performance gains. Among every one of the companies in our research that reported strong gains in customer satisfaction, one of these executives was the S&OP sponsor; among all of the companies we studied, the CEO, general manager, or CFO was the S&OP sponsor only about one-third of the time.

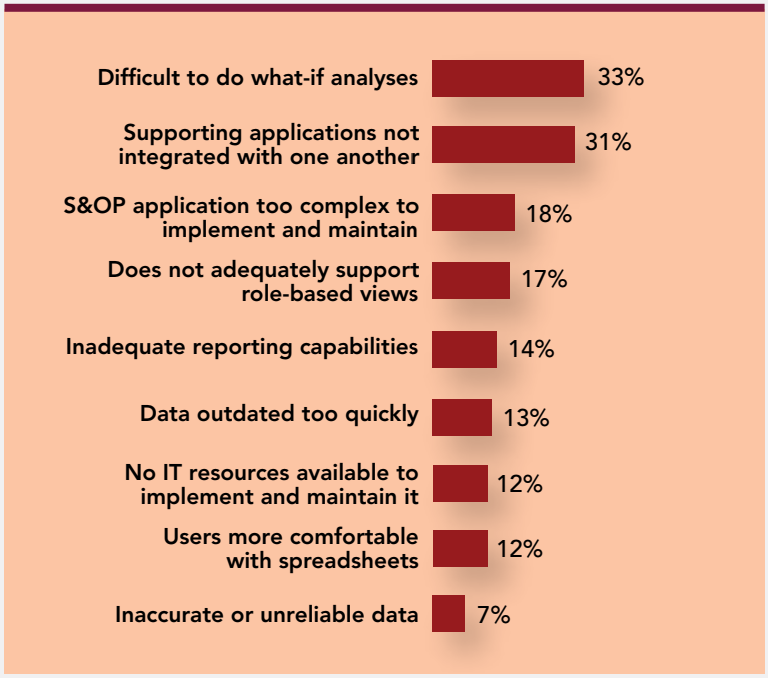
Improving the process a little brings big gains. Our research found that another determinant of how well the sales and operations planning process works is whether the company holds formal executive meetings dedicated to S&OP. In the top-performing companies, regularly scheduled executive meetings review reports of demand and supply trade-off scenarios, track the progress of strategic initiatives, include balanced scorecards or performance reviews, assign action items, and set follow-up assessments.

However, our benchmark research also found that simple improvements, such as including plan-versus-actuals reports as part of the top-level S&OP reporting package, can bring about considerable performance increases. Only about half of companies currently have S&OP plan-versus-actuals reports (see exhibit 3, above), but 90 percent of respondents who reported overwhelming gains in gross margins use them. Similarly, our research indicates that companies which create plans on a monthly basis achieve better performance than those that create plans once a quarter or once a year. Organizations that create plans with time horizons of 18 months or longer achieve larger gains than those with shorter planning horizons. And companies that include multiple lines of business or brands in their top-level S&OP do better than those that don't.

The factor we found to have the third-largest impact on S&OP success is having an agenda and a list of key decisions that need to be made during each top-level S&OP meeting. Again, the 40 percent of study participants that prepare for executive S&OP meetings in this way outperform those that don't.

Dedicated software is the best tool for the job. More than three out of four respondents (76 percent) told us that software is an important element of sales and operations planning. More than half of the companies surveyed use software dedicated to S&OP (59 percent). About one-quarter use nondedicated software, such as an ERP or best-of-breed supply chain management (SCM) system (24 percent). Only 14 percent said they do their S&OP work primarily in spreadsheets. Vendor-provided S&OP software is the type most participants use; almost one-third of the companies in our research

Exhibit 4



rely on either a dedicated, stand-alone application (16 percent) or a vendor-supplied software-as-a-service setup (14 percent). Yet 20 percent use dedicated software that they developed in-house.

Overall, only 20 percent of organizations participating in the research expressed dissatisfaction with their current software; not surprisingly, the least satisfied are those that don't have a dedicated system or that use spreadsheets primarily. The most satisfied are those that have a dedicated, stand-alone software package provided by a vendor (71 percent are pleased with the application's performance).

Respondents identified difficulty in creating alternative scenario plans for what-if analysis as their number-one problem with their S&OP software (see exhibit 4, at left). Lack of integration with supporting applications, such as their financial planning or ERP system, ranks number two. But the companies with the biggest year-over-year performance improvements tend to be well-satisfied with their current technology. Their S&OP software includes features such as workflow, action item assignment, automated financial plan reconciliation, business initiative tracking, and executive reporting and visibility. These companies also are more likely to use profit-based S&OP technology (78 percent) compared with the general population of the study (38 percent).

Making S&OP Work for You

To be effective, the planning process must span the enterprise and cross functional and departmental lines. Yet it is not easy to integrate plans across sales pipelines, demand forecasts, revenue expectations, and products. To assimilate all available external and internal information, and then to plan with it, is one of the most difficult challenges facing operational management.

That said, organizations do have the ability to transform a supply-chain–centric S&OP process into a framework of integrated and improved business planning. To do so, senior executives must identify and address the management and process challenges behind their myopic planning. This initiative will be challenging but worthwhile. Because planning is the link between strategy and execution, improving S&OP processes leads to enhanced organizational performance. And improving S&OP processes is a more feasible goal today than it might have been in the past because the technology that supports enterprisewide sales and operations planning has improved in recent years.

The array of S&OP software choices is expanding, and vendors now offer mature products that are rich in features. The best products enable companies to build a repeatable process for creating plans, while allowing for ad hoc scenario planning. They empower front-line decision-makers to respond immediately to events, while regularly measuring the impact of those responses on the company's progress toward mid- and long-term performance objectives.

When sales and operations planning is part of an overall BPM framework, it can align people and processes and tie operations to objectives. Ventana Research believes that when S&OP is deployed using the right technology, it synchronizes the activities and resources of individual departments and enables employees to respond faster and more fully to changing demands of customers and markets. But before adopting any new technology, companies should evaluate their supply chain, finance, and business intelligence systems to see how these areas might benefit from an S&OP tool.

If you choose to invest in a new S&OP system, be sure to deploy both the system and business processes in ways that work for different levels of management and are accessible to all supporting analysts. Make sure you invest in applications that support both a single enterprise view and departmental views as needed. If possible, tie your sales and operations planning system into the same data warehouse as your financial system. Above all, be sure not to propagate the problems with operations planning that run rampant in spreadsheet-based processes. Data integrity and a single version of the truth are absolutely crucial for companies looking to boost performance by improving planning companywide. bpm