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Retail Vendor
PERFORMANCE MANAGEMENT BULLETIN

An Inflection Point in the Retail Supply Chain? Part 3

By Dan Gilmore, Editor, Supply Chain Digest.

Over the past two months, I have written columns in this space arguing that we may be at an important inflection point in the history of the retail supply chain. Specifically, this has to do with various signs – including new changes at both Walmart and Target with regard to fill rates and on-time deliveries – that some retailers may be getting serious about reducing supply chain variability from the vendor side, in much the same way many manufacturers have been attempting to do for a long time.

For example, this past summer, Target's COO John Mulligan said the chain was going to attack the out-of-stock problem in large part by reducing "variability" in its distribution centers, especially with regard to supplier deliveries. Mulligan said that "An unacceptable number of vendor shipments were received by our DCs either too early or too late," adding that "We have been collaborating with our vendors to increase the percent of shipments that arrive on the correct date and we have already seen meaningful progress." That progress includes an impressive 50% reduction in out-of-stocks for ecommerce-only items in its DCs.

A bit earlier, rival Walmart wrote in a blog post for vendors that it was reducing the window for which a shipment is considered on time from the current four days to just two, starting in February 2017. In addition, the fill rate requirement is being raised from 90% to 95%, measured at the case fill level. Failure to hit either metric results in chargebacks - a practice that Walmart was actually late to embrace versus other retailers.

That's all well and good, and definitely an important step towards supply chain progress. While taking the steps outlined will help, retailers also create much of their own supply chain variability.

It starts with the famous Bullwhip Effect, first identified by MIT's Jay Forrester in the early 1960s, and then rediscovered in the early 1990s by Procter & Gamble and Dr. Hau Lee of Stanford. In great simplicity, the Bullwhip Effect refers to the fact the while actual consumer demand is generally fairly steady and predictable, for a variety of reasons (including simply a lack of supply chain discipline), orders to first tier suppliers and then their suppliers tend to be erratic and hard to predict.

- continued pg. 2 -

Industry News Round Up

Outstanding On-Demand Videocast: Successful Supply Chain Vendor Compliance - for Retailers and Beyond

SCDigest recently broadcast an excellent Videocast on vendor compliance – featuring Norman Katz, author of the new book *Successful Supply Chain Vendor Compliance.* Also participating was Greg Holder, CEO of Compliance Networks.

We reviewed Katz's excellent book on the pages of the *Retail Vendor Performance Management Bulletin* earlier this year, but in this broadcast we delved into more detail, as Katz and *SCDigest* editor Dan Gilmore discuss key issues around compliance program success.

In the Videocast, Katz summarized key elements of his book. Highlights of the broadcast include:

- Why it's time for this book right now
- The current state of vendor compliance – it could be a lot better, Katz says
- Compliance program guiding principles
- What is permissible under the law relative to vendor chargebacks?
- Common mistakes companies make in rolling out and maintaining vendor compliance programs
- Why retailers are often their own worst vendor compliance enemies
- The many "E's" of successful vendor compliance, from "Envision" to "Ethics"

- continued pg. 3 -

Compliance Networks Corner:

Understanding Vendor Compliance Optimization - Part 2

Last month, we provided an overview of retail Vendor Compliance Programs (VCP). As we noted then, the visibility from a robust vendor compliance system that supports a VCP and improvement in overall and individual vendor performance have major impacts on a retailer's supply chain effectiveness, ultimately in terms of service to the store and increasingly to the omnichannel consumer as well. A VCP also provides a platform for:

- Identifying vendor failures and recovering associated costs
- Reducing labor costs by minimizing problem shipments and streamlining inbound auditing
- Reducing the amount of required safety stock
- Improving customer satisfaction and sales

Last time, we introduced our Vendor Compliance Adoption Model, illustrated again here in the graphic on Page 2. This graphic illustrates the three levels of vendor compliance sophistication and value: visibility, variability, and velocity.

Each maturity level provides different degrees of visibility, variability, and velocity benefits. However, it is important to note that as retailers improve the design and execution of their Vendor Compliance Programs they can expect to move into outcome levels that are best described by their focus on visibility, variability, or velocity.

- continued pg. 2 -

An Inflection Point in the Retail Supply Chain? Part 2 (continued)

This presents those suppliers with real supply chain challenges. They could bulk up inventories to buffet the order variability, but that is expensive. Retail vendors do some of that, but more often try to cope by madly shifting production schedules and expediting - which only goes so far. The result (surprise!): problems with on-time deliveries and fill rates, meaning high levels of variability from the retailer's perspective.

Not only are actual orders from retailers to vendors erratic - they in general do a very poor job even of forecasting those orders, though there really is no reason they could not do a much better job of that.

Lack of visibility to future order flow is what spawned the Collaborative Planning, Forecasting and Replenishment (CPFR) "standard" (that's an overstatement) in the last 1990s. I suppose CPFR has produced some benefits, but clearly it never met early expectations - or solved the variability problem in the consumer goods to retail supply chain.

While Target, Walmart and maybe other retailers should be complimented for attacking part of the variability challenge, the other side of the equation also requires attention. That means driving the supply plans truly from the shelf back by both parties, providing time-phased order plans such are commonplace in manufacturing but very rare at retailers (evolving into the concept of "supplier schedules"), and providing retail vendors the type of forecast visibility that Canadian Tire has admirably been doing for years for its retail suppliers. More on all that sometime in early 2017.

Compliance Networks Corner: (continued)

First Outcome Level: Visibility

Vendor Compliance Programs establish vendor accountability for following published guidelines. If and when these guidelines are breached, penalties are assessed and notifications are delivered to the vendor. The penalty corresponds to the cost directly associated for remediation or recouping lost sales.

The intent of penalties is not punitive but to encourage execution of the merchandising plan. Accountability works best when automated processes are involved. Manual efforts to detect violations are not as accurate, and are more costly than automated detection strategies.

A Visibility-level organization's efforts and execution are predominately manual. There is little to no automation for identifying breaches, assessing penalties and notifying vendors.

Beyond manual detection of vendor failures, a basic VCP provides retailers with modest visibility into the performance of their inbound supply chains. Depending on the design and execution of the entry-level VCP, this visibility may or may not provide an accurate and timely view. Regardless of the quality of the data produced, it is highly likely that a manual, entry-level VCP will be limited in scope, depth, and functionality. A basic VCP is of limited value in terms of optimizing supply chain execution of the merchandising plan. If poorly designed or executed, a basic VCP can even sometimes do more harm than good. An example would be inconsistent application of retailer routing guide rules across the vendor community or failure to notify vendors of violations in a timely manner with complete information.

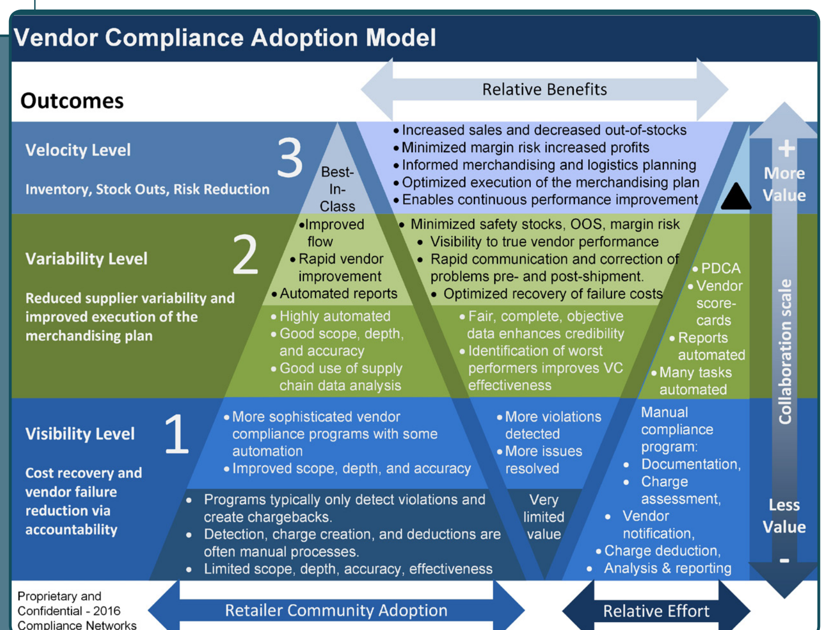
Second Outcome Level: Variability

VCPs leverage data to reduce variation in supply chain activities and by doing so they improve decision-making performance. Objective information is now available to assist stakeholders to manage their organizations so as to develop a continuous improvement cycle.

A second-level organization automates vendor compliance failures, penalties and notifications (with supporting documentation), driving immediate improvements in vendor performance and reducing variability.

Third Outcome Level: Velocity

Objective historical supply chain performance data enables the retailer to base its merchandising plans on facts. Historical vendor performance



is assessed to anticipate future vendor performance. This predictability is leveraged to make short term order adjustments based on a vendor's record of shortages and overages. Velocity-level retailers can also adjust their order timing to accommodate vendor tendencies.

The power of predictability is that the retailer can take advantage of these tendencies in the short term, while encouraging behavior changes in the long term from the vendor. Velocity-level organizations embrace predictability which enables the retailer to optimize its merchandising plan execution and significantly improve prospects of reducing variability in on time and complete performance.

Benefits of Vendor Compliance Optimization

As a retailer matures in their VCP efforts, they create a predictable supply chain performance, which informs the merchandising and logistics planning while encouraging improvement throughout the supply chain.

Improved sales result from having accurate inventory on hand. Reduced inventory costs are enabled by less need for safety stock. A reduction of manual efforts reduces overhead and reduces oversight risk.

As inbound supply chain performance improves, logistics stakeholders are better able to accurately and efficiently execute the merchandising plan.

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Industry News Round Up (continued)

After Katz, Holder offered his current take on the state of retail vendor compliance – a bit more upbeat that Katz's view – and then offered suggestions for both retailers and vendors on how to improve compliance program success.

This excellent broadcast is not to be missed for those interested in starting or improving vendor compliance programs.

You can watch an on-demand version of the broadcast, download the slides, order the book at a discounted price and more at the following URL: ***www.scdigest.com/campaigns/On_Demand_Successful_Vendor_Compliance.htm***

RSR Benchmark Report on Supply Chain Execution

The analysts at RSR released a new benchmark report on supply chain execution, based on a survey of primarily US-based retailers.

Here, we summarize some of the highlights, a lot of which – not surprisingly – focused on omnichannel issues.

- The top three inventory management challenges cited by survey respondents were: (1) inaccurate inventory levels in stores – 57%; (2) consistent stockouts on fast-moving categories/products – 46%; and (3) too many out-of-stocks in stores – 40%.
- Out-of-stocks at the distribution center level was down the list just a bit, cited by 37% of respondents as a major challenge.
- The report observes relative to inventory management that "What was "close enough" in a pure store-based environment and its consequent relatively low percentage of merchandise returns has become completely unacceptable in an omnichannel world." It adds that "Supply chain execution as it relates to managing inventory no longer works the way it used to, and retailers are struggling to adjust."
- Drop shipping by vendors to ecommerce customers is seen as important, but still well down the list from other fulfillment capabilities. 49% of respondents said vendor drop shipping was a "very valuable" capability, versus 71% saying direct customer shipments from DCs was very valuable. Just behind that was consumer shipments from stores (70%), ship to store for customer pick-up from ecommerce focused DCs (61%), and store-to-store transfers for customer pick-up (56%).
- However, just 9% of respondents said they have no plans to initiate vendor drop shipment processes.

"RSR suggests retailers need to get more precise about what they really mean by supply chain visibility, including who really needs to see what, and just how real-time that visibility needs to be."

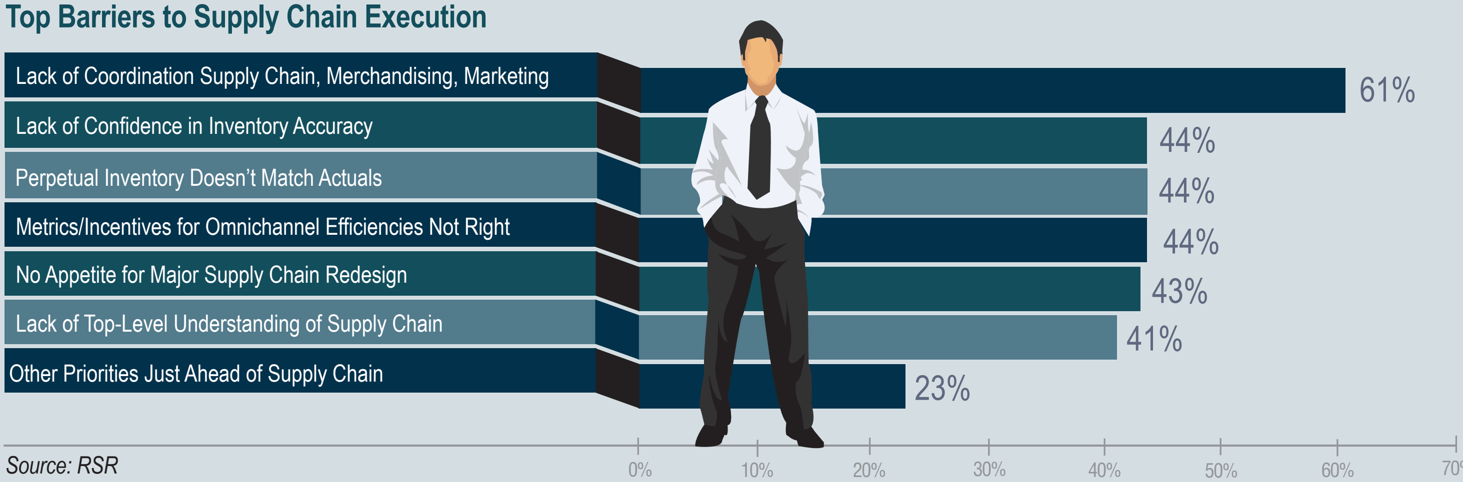
What are the largest barriers to improved supply chain execution?

As shown in the chart below, lack of coordination between supply chain, merchandising, and marketing topped the list (no surprise there) at 61% of respondents, far ahead of number 2 "lack of confidence in inventory accuracy" at 44%, the same percentage as for "perpetual inventory rarely matches actual inventory levels" and "we don't have the right metrics or incentives to measure cross-channel supply chain efficiencies."

Among other recommendations, RSR suggests retailers need to get more precise about what they really mean by supply chain visibility, including who really needs to see what, and just how real-time that visibility needs to be.

There is a lot more detail in the full report, available for free with registration at the RSR web site.

Top Barriers to Supply Chain Execution



Source: RSR

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For current trends & events in Retail Vendor Management...

- An Inflection Point in the Retail Supply Chain? - Part 3
- On-Demand Videocast: Successful Supply Chain Vendor Compliance
- Understanding Vendor Compliance Optimization - Part 2