

Consensus Demand Planning

*Driving towards true synchronization
in the retail marketplace*

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1 Introduction

Are high inventory levels keeping you up at night? Are you concerned about product replenishment being constrained by supply? Have you had to deal with low service levels and store stock outs? You need to improve the accuracy of your forecasting. As consumer behavior grows more unpredictable and unforgiving, the need for retailers to have the right product mix on the shelf becomes more vital than ever. Poor forecasts lead to inventory imbalances, which lead to stock-outs and overstocks, and unhappy customers. Consensus demand planning improves forecast accuracy and reduces inventory through communication and collaboration.

2 Defining Consensus Demand Planning

Demand Planning is quickly becoming a functional necessity in retailers' business models, acting as the lever that converts companies from a supply chain to a demand chain business operation. So why are retailers increasingly incorporating demand planning as part of daily activities? Simply put, to gain a competitive edge by understanding, shaping, and predicting customer wants and needs.

Through demand planning, retailers are able to more accurately forecast future demand and send forecasts to merchandise planners as a baseline enabling them to optimize inventories. Statistical capabilities, combined with market intelligence gained from internal collaboration, bring pinpoint accuracy to companies' demand plans. The result: a single, company-wide view of the "truth" that provides the foundation for sales and operations plans and helps drive measurable improvements.

3 Legacy Demand Planning

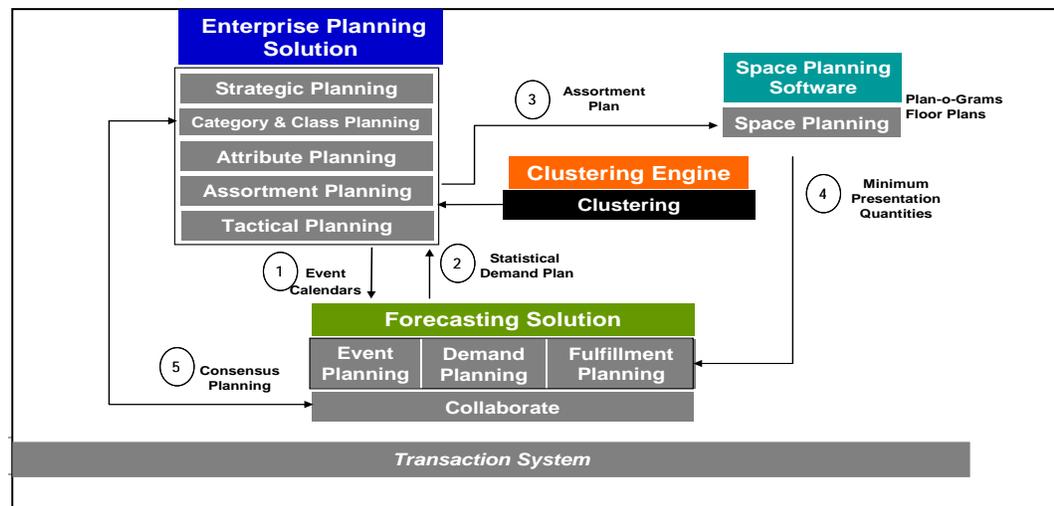
Retailers today have two different options for approaching demand planning: Top Down or Bottom Up. Top Down demand planning starts at an aggregate level; total demand is allocated to products and stores to support replenishing and purchasing activity. The Bottom Up approach begins at the store level and includes various levels of an item hierarchy through the SKU-store level that support execution activity. Forecasts are aggregated to support demand planning requirements at higher levels. A Bottom Up forecast creates an unconstrained replenishment plan by passing need up the supply chain, while a Top Down forecast creates a replenishment plan constrained by supply.

The Top Down approach is currently the most prevalent, particularly among retailers with short life cycle products. However, the Bottom Up methodology has much greater potential for reduced costs, improved service levels, and improved inventories. As technologies improve and processes become more sophisticated, the Bottom Up method is gathering momentum.

4 Consensus Demand Planning

Consensus Demand Planning incorporates both Top Down and Bottom Up Demand Planning philosophies. The statistically-driven Bottom Up forecast is reconciled with the financially-driven Top Down forecast. This new “consensed” forecast guides the assortment planning process and sets the inventory “cycle stock.” This forecast is evaluated, and modified when necessary, through ongoing reporting and consensus meetings. The result is deploying the right product at the right place at the right time and for the right customer. Consensus Demand Planning is one piece of the Consumer Driven Replenishment puzzle that challenges companies today (see Exhibit 1).

Figure 1: Consumer Driven Replenishment Model

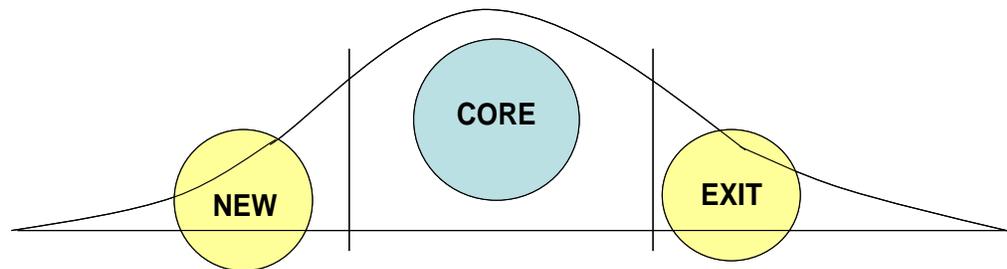


5 Methodology/Process

Although retailers should refine their demand projections on an ongoing basis, many companies limit demand planning to a single monthly demand forecast. Continuous demand forecasting enables companies to quickly detect, interpret, and act on changes in demand.

The statistical evaluation process, or “Pre-Consensus Activities,” involves force ranking items into A, B, or C categories and identifying the “Critical Few Choices” (CFCs) – the few items that have the largest impact on the business. In this way, the planners can focus on the 15 to 20 percent of products that make up 80 to 90 percent of the revenue and profit. The most efficient retailers use forecasting tools that automate these more basic tasks. This allows the planners to form a Collaborative Model that enables them to focus on the areas of their business that require more attention, such as new and exit items (see Exhibit 2).

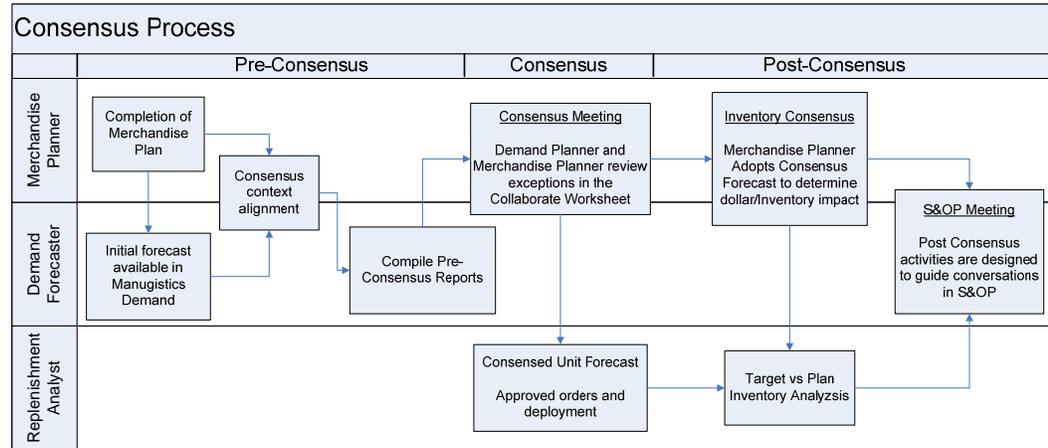
Figure 2: Collaborative Model



A collaborative model that includes input from Merchandise Planners, Forecasters, Replenishment Analysts, and Merchants allows replenishment forecasting accuracy to become automatic for a business’s core items, allowing planners to focus more time on the tails.

A Consensus Demand Plan is an agreed-upon unit forecast created during the consensus meeting where a Demand Forecaster and Merchandise Planner reconcile the top-down merchandise plan with the bottom-up forecast. Discussions during a consensus meeting are centered on exceptions and timeframes that will influence a buy or even long- and short-range themes. Following the consensus meeting, Merchandise Planners, Demand Forecasters, and Replenishment Analysts take part in Post-Consensus Demand Planning activities that include reviewing the financial and inventory implications of the unit demand signal. (See Exhibit 3 for a detailed summary of the Consensus Demand Planning Process.)

Figure 3: Consensus Demand Planning Process



At demand planning-focused companies, demand forecasters use statistical analyses to generate a base sales estimate for all products. These forecasts leverage historical demand, product lifecycles, and scenario analysis. The demand forecasters participate in ongoing tuning activities to improve the accuracy of their forecasts, including considerations of external factors such as newly added events and past/future promotions. By blending art with science, demand forecasters can bring an independent point of view into consensus meetings.

This focus allows merchandise planners to bring more value to the business. Rather than simply looking at past sales or shipments and determining a best guess for the future, planners can provide true value based on information not contained in the usual historical data. This might be the planner's knowledge of a new deal that has closed, a product that is being transitioned, or a customer event that is forthcoming.

Human insight is a key component in demand planning. Understanding and interpreting the demand signal requires skilled people, not just computers. It requires leadership with a commitment to continuous improvement, and staff who can balance consistency, speed, and judgment. Demand planning is a learning opportunity. As companies gain a deeper understanding of the drivers of demand, they can use this knowledge to shape demand and supply rather than react to surprises. Throughout the initial adoption stages, management must effectively deal with the Demand Forecasters' and Merchandise Planners' feelings of uncertainty. Leaders need to give their planners and forecasters direction on how to deal with that uncertainty, and help move the risk off of their shoulders and onto management.

6 The Challenge of Creating Consensus Demand Planning

As assortments grow, the task of forecasting which products consumers will buy becomes more difficult. Retailers need a solution that allows them to control their merchandising and supply chain operations by better predicting, and then shaping, consumer demand. Businesses can maximize sales and marketing effectiveness by accurately predicting future customer demand, and using the information to synchronize demand with their sources of supply.

Even as technology improves, retailers struggle to find an automated, consistent way to communicate with their business units and their suppliers. As a first step in driving synchronization, retailers need a collaborative platform for sharing key data streams with their business counterparts. As the process of working together is automated and streamlined, collaboration can be ramped up exponentially.

Many other potential challenges and roadblocks will present themselves during the implementation of Consensus Demand Planning. The learning curve will vary, but some of the business process issues may include:

- **Change management** – Relinquishing what may be perceived as individual control over the forecast, and aligning around a one number forecast that is owned by everyone in the company.
 - **Merchandise Planners** – Wrestle with balancing art with science. Science is defined as the algorithms that are native to the application. These algorithms utilize historical data to help produce a forecast. Art is defined as the planners' ability to better inform the forecast. Planners must clearly articulate the art.
 - **Demand Forecasters** – Challenged with incorporating emotional decisions into forecast through overrides, events, and tuning activities.
 - **Replenishment Analysts** – Tasked with making weekly decisions that influence how they meet/preserve/support demand plan. Replenishment Analysts need to evaluate which products and how much of them get allocated across stores.
- **Data issues** – Identifying and performing data cleanup activities on POS data to help validate historical data. Activities may include Normalization/Demand Classification.
- **Adherence To Merchandise Calendar** – The entire Merchandise Planning and Allocation team needs to adhere to and execute the overall merchandise calendar, consisting of tasks such as defining the Assortment List, Adjusting POGs, Merchandise Plan

approval and completion. The result is enough lead time (greater than a finished good item's longest component lead time) to appropriately develop a consensus demand plan that will impact future buys.

- **Missing CRM Events/Promotions** – Demand Forecasters need to make sure their forecasts incorporate all CRM events and promotions in order to ensure accuracy.
- **Lack of Collaboration** – Merchandise Planners and Demand Forecasters must share the relevant information with each other and with other areas of the business such as inventory deployment, space planning, and planning managers.
- **Granularity of Forecasts** – Forecast accuracy becomes more difficult as granularity increases. Precision at the store or SKU level is a lot more difficult than achieving an aggregate number.
- **Overall system efficiencies** – Companies must ensure they have the proper technology infrastructure in place to allow for successful consensus demand planning.
- **New Product Introductions** – Planners/Forecasters need to predict how a new product will behave in terms of future sales by building like models with existing items that have similar packaging, price points, fabric, etc. What attributes drive the decision?
- **Exiting Items** – A strategic approach is needed to help determine how much product you need to push out and for what period of time. What will your markdown strategy be? Where can you afford to reduce margin?
- **Preparation** – Retailers must allot the proper time to complete all pre-consensus activities. This will lead to a productive meeting that drives value throughout the organization.

Management must often take a leap of faith as they implement a new solution. They must be willing to experiment with new approaches and disrupt existing solutions. They must be confident and stay the course even in the face of financial pressures in the core business. These kinds of management commitments are rarely easy, but the rewards for success are immeasurable.

7 Realizing Benefits

Consensus Demand Planning improves forecast accuracy. Having the right product on hand means higher fill rates, increased customer satisfaction, and ultimately, higher profitability. In addition, a more definitive forecast makes it easier and less costly to respond to unexpected demand, as well as introduce new products. By improving forecast accuracy, retailers can optimize production and distribution plans to reduce excess inventory and safety stock.

Benefits of Consensus demand planning include:

- Improved forecast accuracy
- Improved product margins
- Reduced inventory throughout the business.
- Increased demand visibility across your entire business.
- Increased collaboration among functional teams
- Increased order fill rates and on-time delivery
- Reduced inventory carrying costs
- Reduced excess and obsolete inventory write-offs
- Improved product configuration management
- Flexible process to manage historical data cleansing and accounting for future promotions
- Increased user confidence
- A sustainable and repeatable knowledge base

8 Capgemini's Business Perspective and How We Can Help

Capgemini's Global Retail Industry practice is aligned with skilled professionals from around the world. We work with leading retailers to create sustainable value measured by improved profitability, revenue growth, customer satisfaction, and ultimately, shareholder value. We have clients in all segments of retail, including department stores, mass merchandise/discounters, specialty, drug/convenience, and supermarkets.

Our core expertise blends art, science, and technology to transform key areas of the business including merchandising, advertising, store operations, store format, supply chain, and customer relationship management. Through the Collaborative Business Experience, we work shoulder to shoulder with our clients to develop and execute high-growth, transformational strategies in areas that touch every facet of the supply chain. Capgemini can help you through its expertise in areas such as:

Integrated Planning & Execution – Capgemini has implemented Integrated Planning & Execution in many client environments in industries that range from grocery to lawn care to specialty retail.

Inventory Modeling – Capgemini has designed and developed a unique modeling methodology to identify key inventory drivers, understand the optimal inventory level for each product, and identify the steps needed to reach that level.

Supply Chain Strategy – Recognized by Gartner as a top four supply chain services provider, Capgemini combines its expertise and experience to turn the modeling recommendations into quantifiable business benefits.

Application Development & Integration - Solves critical business and technology problems by developing custom software. Our collaborative methods, efficient development techniques, and alliances with top technology companies allow us to develop high-quality software solutions quickly and cost effectively.

Systems Integration - Applications and business processes must often span systems and enterprises to create real value. Our systems integration teams help clients move in an incremental, pragmatic way—away from the ad-hoc integration patterns of the past towards a well-planned future.

Organizational Change Management – Like any initiative, it is imperative to have team members onboard. Our OCM practice has the experience to ensure that new processes and systems are adopted, and the benefits are derived.

Retail Transformation – We have extensive experience assisting leading retailers with large-scale transformation. Today’s winners have adjusted to today’s market realities. Capgemini’s structured approach will assess the readiness of your organization, technology infrastructure and process to develop a comprehensive plan to take your organization to the next level.



About Capgemini and the Collaborative Business Experience®

Capgemini, one of the world's foremost providers of consulting, technology and outsourcing services, enables its clients to transform and perform through technologies. Capgemini provides its clients with insights and capabilities that boost their freedom to achieve superior results through a unique way of working - the Collaborative Business Experience™ - and through a global delivery model

called Rightshore®, which aims to offer the right resources in the right location at competitive cost. Present in 36 countries, Capgemini reported 2007 global revenues of EUR 8.7 billion and employs over 88,000 people worldwide.

More information about our services, offices and research is available at www.capgemini.com

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