Squeezing More Juice Out of a Global Winery's Supply Chain

Aggressive sourcing strategy and business discipline drive 42% average cost reduction.

Business Profile

A leading producer of luxury and lifestyle wines that produces, markets, and sells distinct wines from California, Italy, Chile, and Australia.

Business Challenge

Many of the company's brands were experiencing tremendous downward price pressure in the market from an influx of lower-priced import and domestic wines. Additionally, the industry as a whole faced a glut of grapes on the market, which further contributed to price pressure by encouraging the entry of more low-priced wines in the market.

In response to these pressures on profit margins, the winery decided to target its supply chain to deliver significant cost reductions, and publicly committed to its shareholders to markedly reduce its cost of goods sold.

The winery hired Tenzing to help rapidly drive several key supply chain cost reduction efforts.

A Taste of Success

The executive team knew something had to be done, but where to start? They had never approached cost reduction with aggressive strategic sourcing before. They wanted to try a pilot project to see the results they could get before broadly analyzing their spend. The corporate procurement group, which mostly supported packaging and winery operations purchases, was considering putting their label portfolio up for bid, but had only just begun organizing the effort. So, they decided that labels would be a good pilot for strategic sourcing.

Historically, the winery bought high quality labels from a handful of well-known regional suppliers. These suppliers were steeped in the industry and had done business with the winery for years. While corporate procurement coordinated the buy, the individual brands had the last word on sourcing decisions. Furthermore, the suppliers possessed a great deal of undocumented, informal knowledge regarding the winery's specific requirements.

A viable sourcing strategy quickly emerged. Thoroughly document all label specifications. Segment the label portfolio by type, quality, and volume. Combine purchasing of similar label types across brands to increase spend concentration by segment. Introduce new national players into the competitive mix.

After a highly analytical supplier screening process, a very public bidder conference, and intensive bidding and negotiations, the results were clear: the supply base could be consolidated to between one and three strategic suppliers and labels cost would be cut nearly in half without sacrificing quality. Through a rigorous post-bid site

Getting a Handle On Spend

With the label sourcing success in hand, the executive team launched a total spend assessment to find similar opportunities. This was easier said than done. Despite having an ERP system, they did very little coding of purchases anywhere in the operation, so essential commodity spend data was buried under various unrelated accounting and budget designations. In addition, a lot of field sales and distribution spend was not even recorded in the ERP system since it was routinely processed through travel vouchers.

After performing some focused analysis and making a few reasonable assumptions, the team identified several targets including point-of-sale (POS) print and vineyard chemicals. Although these sounded simple, this spend was not managed or controlled by corporate purchasing. The next challenge was to determine how to source spend that lay outside traditional procurement processes.

Who's In the Driver's Seat?

Vineyard chemicals were a key component of the overall vineyard operations budget which was managed by Grower Relations. The traditional process for managing it was to negotiate budgets each year with vineyard management providers. This approach provided some visibility into costs, but little opportunity to influence them. In fact, vineyard chemicals were bought by the four vineyard management providers on behalf of the winery, so chemicals were outside the winery's direct control.

POS print was, fortunately, an internal spend area, but purchases were driven largely by the marketing and creative departments. They eagerly responded to sales and distributor needs on an ad hoc basis, without stepping back to look at the effectiveness of their overall purchasing process.

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Partnering with First-Tier Suppliers

Influencing the vineyard chemical spend would require constructively and creatively engaging the vineyard management companies, the first tier of the supply chain. At first, this seemed impossible since they had no contractual commitment or economic incentive to collaborate with the winery on reducing chemical costs. In fact, the suspicion that this was really a "margin grab" on the part of the winery was an initial barrier to implementing this strategy. However, after assuring the vineyard management companies that any savings would be passed through without reducing their margins, and that any advantages in pricing could be applied to their other customers, they agreed to participate.

Market analysis showed that the winery's combined chemical spend was larger than that of any of its individual vineyard management suppliers. This validated the assumption that a winery-based pooling of demand to establish a preferred supplier base and volume pricing would probably result in a cost reduction that could be offered to the vineyard managers.

Once again, the team detailed the specifications for chemicals and related services and prepared a request for quote. The team created a bid that was not only for chemicals, but also separated out services, such as vineyard assessments. Historically, the chemical distributors had often thrown in those services for "free", effectively distorting the pricing of the chemicals. The detailed quotes revealed great results: by consolidating to a few key chemical suppliers with the most competitive pricing, vineyard chemical costs could be reduced by 15%. Another win for the winery.

It's All About the Process

In the fast-paced competitive world of lifestyle wine sales, speed and visibility are a matter of survival. To be able to produce and deliver the needed POS print materials to distributors and retailers quickly is fundamental to any effective wine marketing program. In an effort to be highly targeted and responsive, the winery's creative services group had developed purchasing practices for POS print that were highly reactive to field requirements and with little supply base or cost management strategy.

Every request for POS print materials became a project in itself with the goal of finding the best quality supplier that could deliver the materials the fastest. That was the extent of the process: no preferred suppliers, no pre-negotiated pricing and terms, no segmentation of similar requirements. After looking carefully at the aggregate requirements,it became clear that there was a great deal of fairly predictable demand that did not require short lead times.

Certainly, some demand required very quick turnaround, but it was much less than perceived. However, given the criticality of marketing and sales to the overall success of the company, changing this process would require disproportionate justification.

Understanding the two tiers of demand, small short turnaround projects and large predictable demand, suggested a sourcing strategy. Since printers tend to have competences in either large-run efficiency or rapid set up for small jobs, the market economics could work in the winery's favor if they could structure their buying differently. Another rigorous requirements definition and bidding process revealed more breakthrough results: by focusing on regional short-run press shops for small quick-turnaround projects and larger national printers for predictable demand, the cost of POS print could be reduced by over 50%.

The Best Way to Save Money

It's been said that the best way to save money on a purchase is by not spending the money in the first place-voila, 100% savings. That was the case for an $8.5 million planned capital expenditure the winery was considering to add a third production line to their bottling facility. Pressure to provide quick market response for new brands, without disrupting the weeks-long production runs for flagship brands, resulted in a proposal to build a new line since it was widely believed that the existing lines were operating at or near capacity.

This proposal was given very serious consideration and garnered significant support from marketing and sales until the CFO recommended a closer look at production planning and operating practices. The investigation revealed that unresolved carton quality issues and other sub-optimal planning practices were resulting in the facility running at rates roughly 30% lower than internal best demonstrated performance showed was possible. The result was the immediate implementation of a Six Sigma quality program and the indefinite deferral of the $8.5 million expansion program.

The team also tackled several additional sourcing projects, resulting in the development of long-term sourcing strategies for other key commodities. The team built on early successes in testing synthetic closures to develop a well-grounded and fact-based synthetic closure sourcing strategy which is critical to their evolving overall packaging strategy. The team also developed a new approach to negotiations with the winery's long-standing integrated bottle and carton supplier to create better visibility and control of second-tier costs like corrugated cartons and inbound transportation to drive further efficiencies in subsequent contracts.

Results

- 42% cost reduction in critical spend areas including labels, chemicals, and print services through strategic sourcing
- Developed long-term sourcing strategies for critical packaging materials including cartons and closures
- Identified bottling plant throughput improvements resulting in an $8.5 million capital avoidance
- Established a repeatable strategic sourcing process that will be utilized for future sourcing initiatives

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