

Arla Foods

Sales & Operations Planning

Logistics Conference October 5th 2011



CONFIDENTIAL



Arla Foods has quickly harvested low hanging fruits from S&OP, but continuous development is key to ensuring long term success

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- The S&OP process in Arla was defined with a work process, material for decision making and focus on strong meeting execution
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- Going forward also the coordination to financial forecasting is essential to ensure forecast reliability and complete transparency/ alignment of plans

Arla Foods has a quite complex value chain



Arla Foods is a cooperative owned by approximately 7,200 Swedish and Danish milk producers



Turnover 2010: DKK 49 bn. (\approx € 6.54 bn)
No. of employees 2010: 16,215



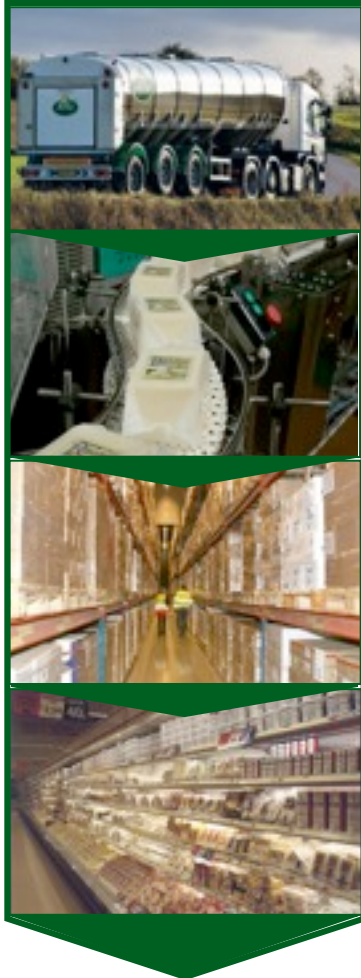
Milk intake 2010:
...from ownership: 6.174 billion kg
...totally: 8.713 billion kg



GCO has 28 production facilities producing yellow, white, mould and cream cheese, mozzarella, butter and spreads, WMP, SMP and caseinate



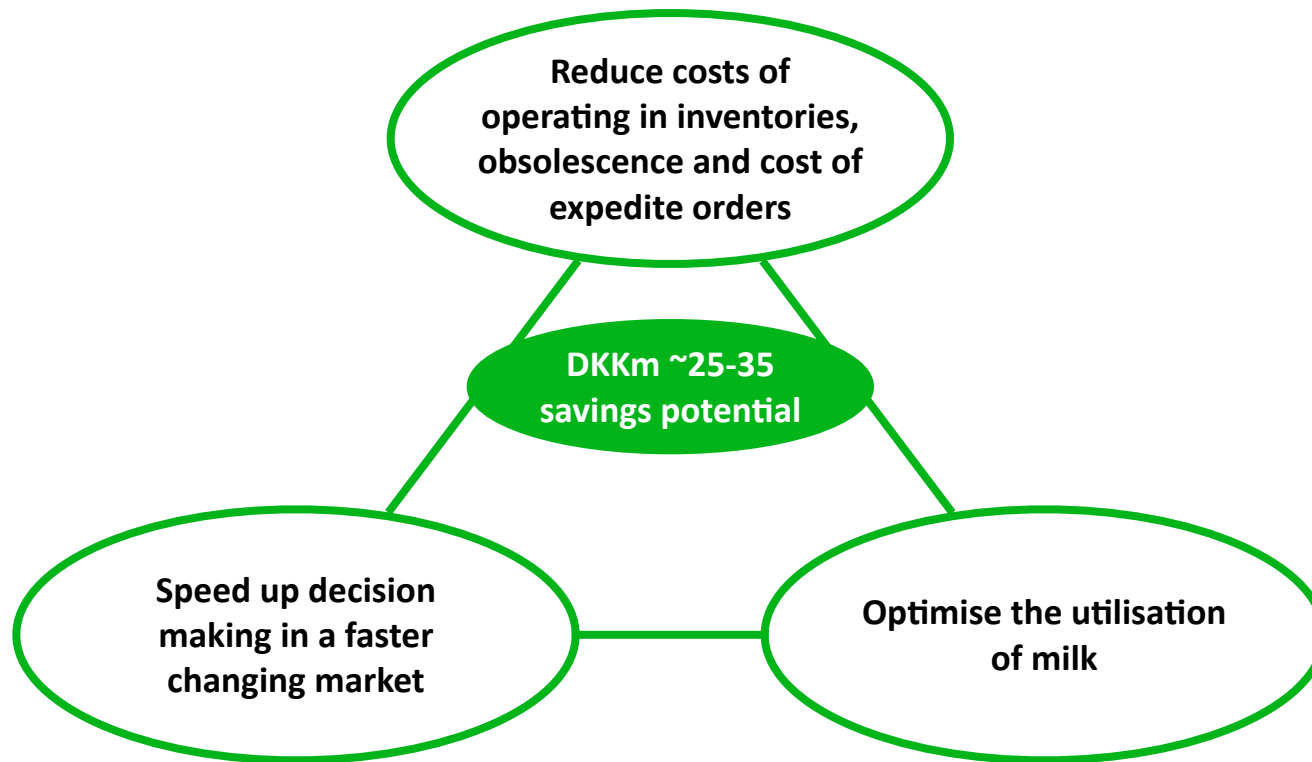
The GCO S&OP covers the value chain from milk intake to distribution to customers



- Milk collection and planning
- Processing and production
- Outbound logistics and Trading sales
- Branding and Innovation

GCO S&OP

The business case was not very formal – but rather a belief in the benefit of three strategic visions



The S&OP process links our strategies with tactical and operational processes

- The planning pyramid

Operational plans are often decoupled from the strategies!



Everyone asks “What is in it for me?”- All parts of the organisation should experience improvements for their areas by implementing S&OP

Markets

- Better product pricing (product calculations)
- Product availability and flexibility, customer service and supplier awards
- Better planning and execution of promotions
- No surprises or misses, no penalties at customer

Categories

- Better product pricing (product calculations)
- Efficient innovations launch
- Better execution of brand activation and campaign plans
- Coordination markets on activity plans

Finance

- Reduce working capital
- Optimise utilisation of raw milk
- Minimise surprises and manage the gap to target
- Visibility and control

Operations (supply chain)

- Minimise inventory and warehouse costs
- Robust planning of capacities
- Longer horizon foresight incl. lower procurement and transport costs
- Visibility on direction through consensus between sales and marketing

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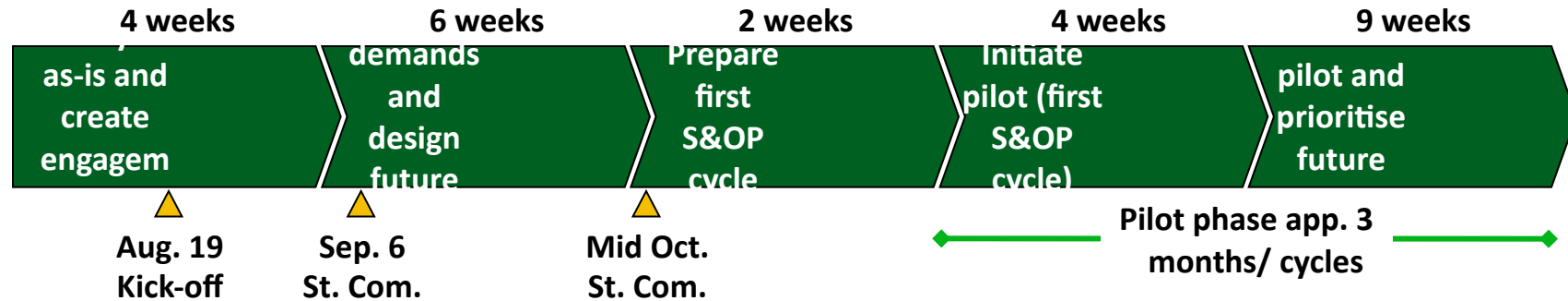
S&OP must be sponsored by top management, defined by the organisation and only include a short definition phase before initiation

- The S&OP must be clearly sponsored from the top management
- S&OP must have cross functional involvement
- Secure capabilities and define clear roles
- Drive a lean and simple, however, effective process
- Let the organisation itself design the process
- Have a condensed project phase followed by trials
- ***Prepare all participants for initial frustrations – but promise continuous improvements***
- (For Arla a new organisation was a clear enabler)

The project plan outlined a very condensed “process definition” process – this was detailed by the groups...

HIGH LEVEL

Timing



Activities and deliverables

- Stage 1 (4 weeks):**
 - As-is analysis and benchmarking of key problem areas
 - Draw high-level future process incl. meeting content, participants and structure
 - Identify stakeholders
 - Communicate vision to key stakeholders
- Stage 2 (6 weeks):**
 - Cross-functional discussions with markets, finance, categories, production etc.
 - Define product and category groups
 - Define KPIs
 - Define templates, responsibilities, definitions
 - Outline IT change implications short and long-term
- Stage 3 (2 weeks):**
 - Initiate and facilitate S&OP process – meeting structure/ calendar, agendas, roles and responsibilities
- Stage 4 (4 weeks):**
 - Have first S&OP cycle
 - Use existing systems
- Stage 5 (9 weeks):**
 - Evaluate the S&OP meetings
 - Adjust solution (content, reports)
 - Document results
 - Evaluate need for IT system changes

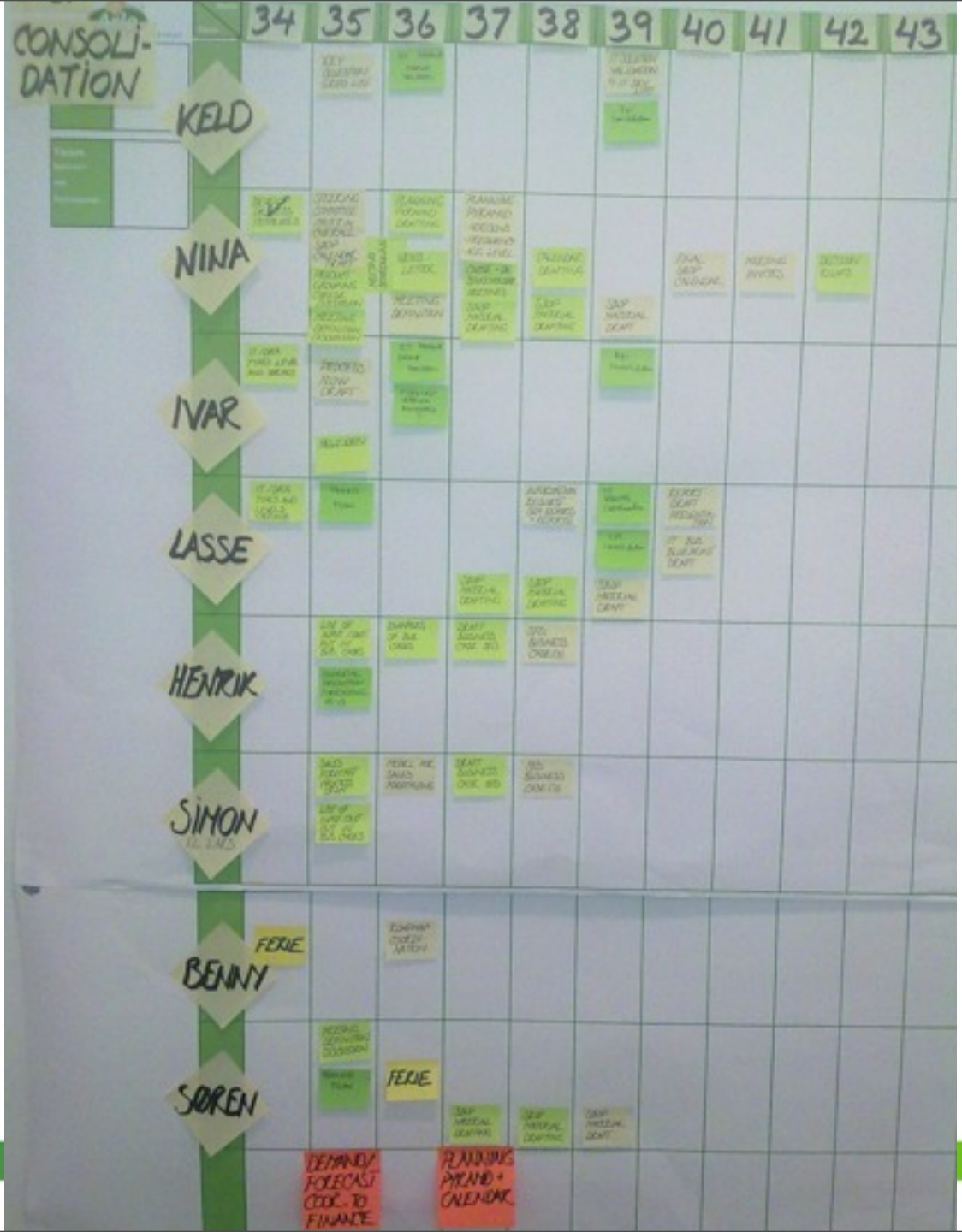
...with visual planning for the overall project...

- S&OP project visual planning

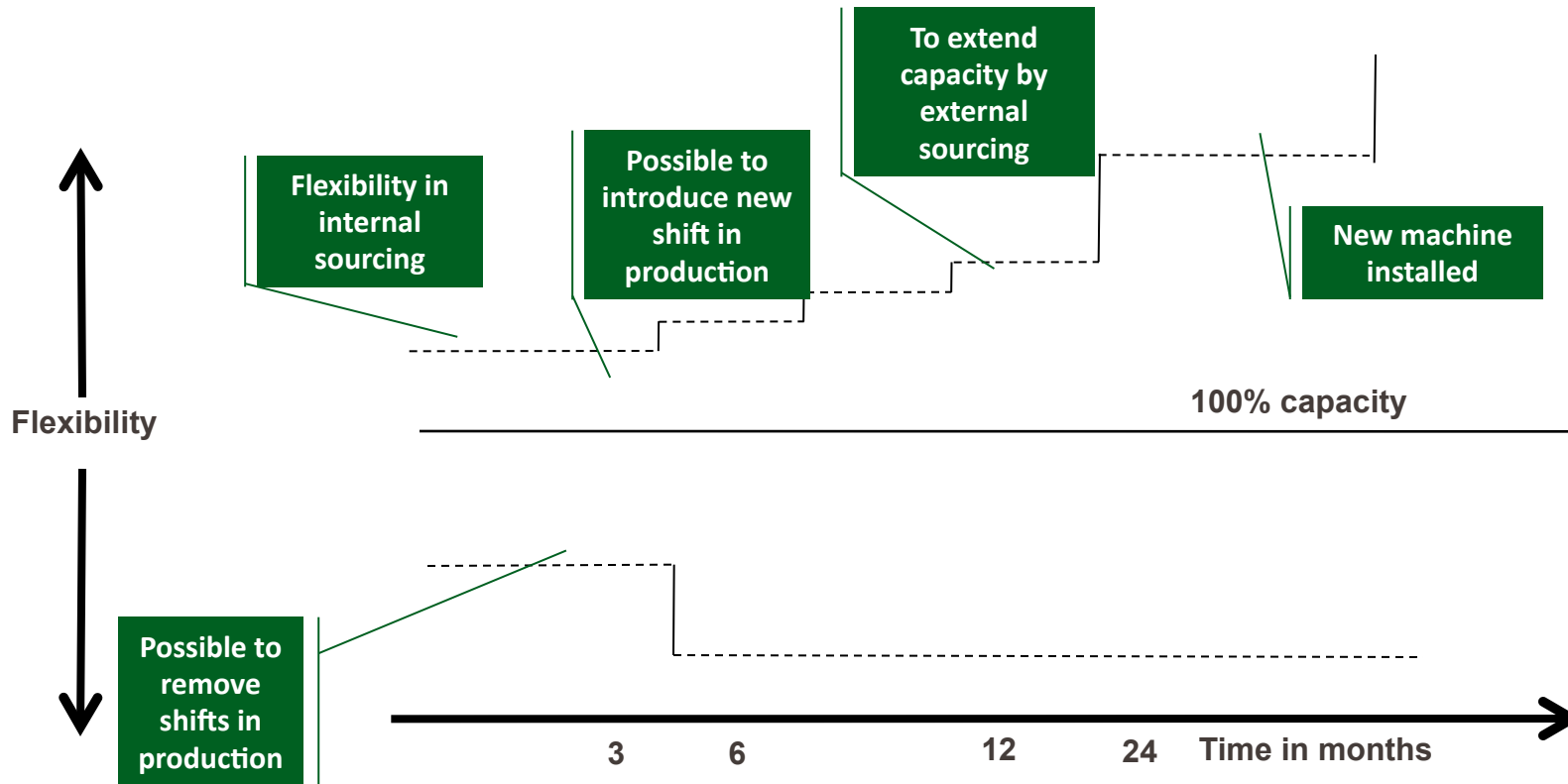


...and by sub-stream

- S&OP project visual planning

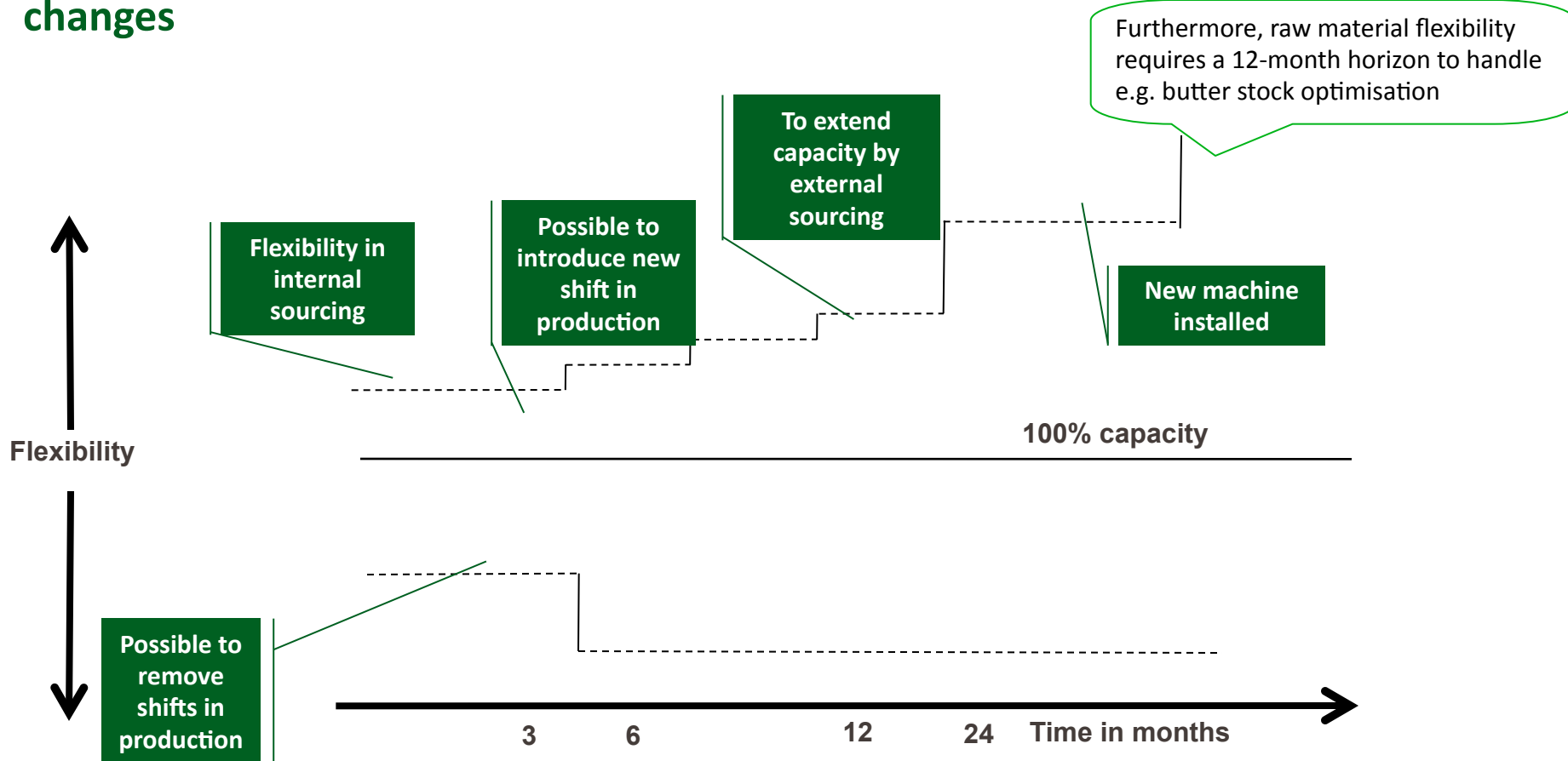


Example of principles needed to be defined - For Arla Foods the relevant S&OP horizon is 4-12 months in order to handle larger capacity and raw material changes



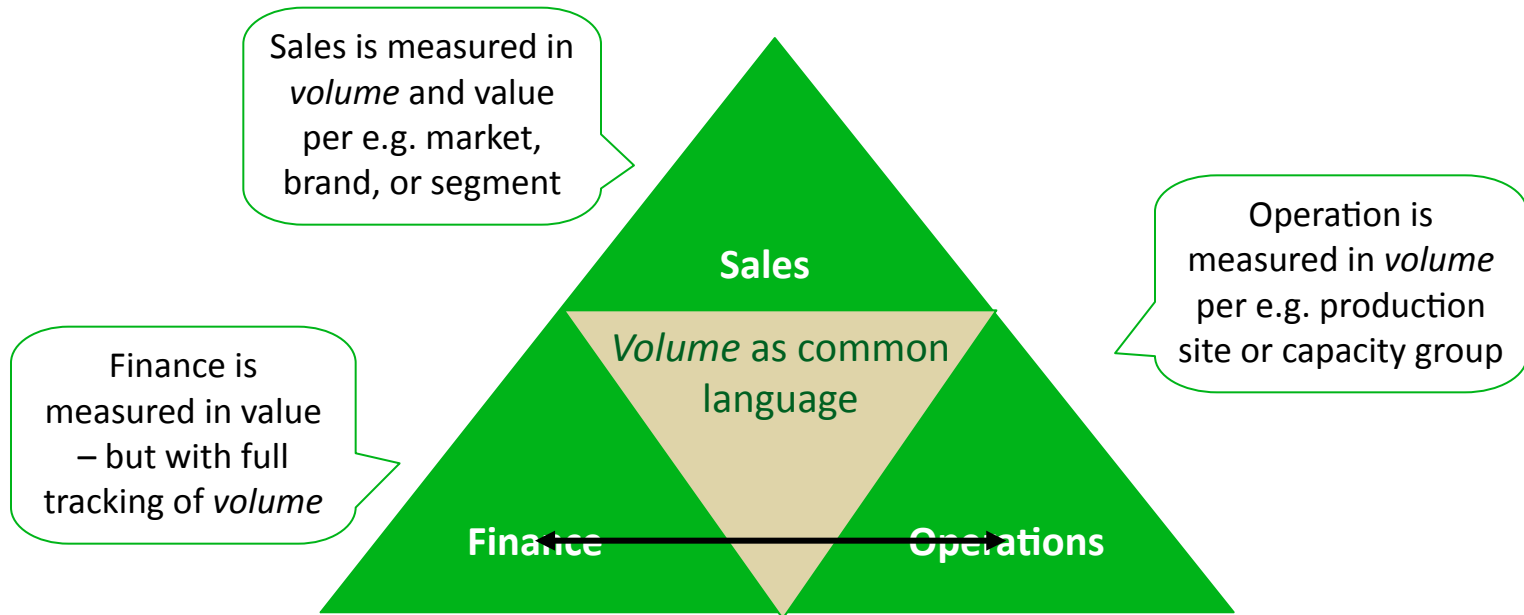
Internal sourcing	Remove shift	Extra shift	External sourcing	New packing line	New dairy/tower
1-4 weeks	3 months	1-3 months	3-12 months	3-12 months	24+ months

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Example of principles needed to be defined - In Arla Foods VOLUME is the logic choice as common language to link the financial and operational forecasts – and WEEKS the common time buckets



Weeks are the standard time buckets in Arla due to the FMCG nature of our products

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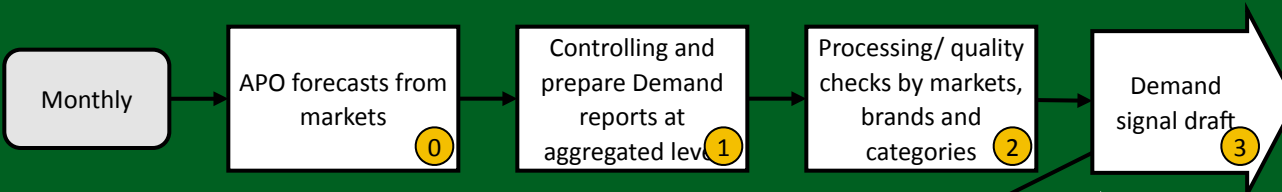
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The detailed process outlines the interactions of the individual processes over the 10 workdays (15 days to start with)

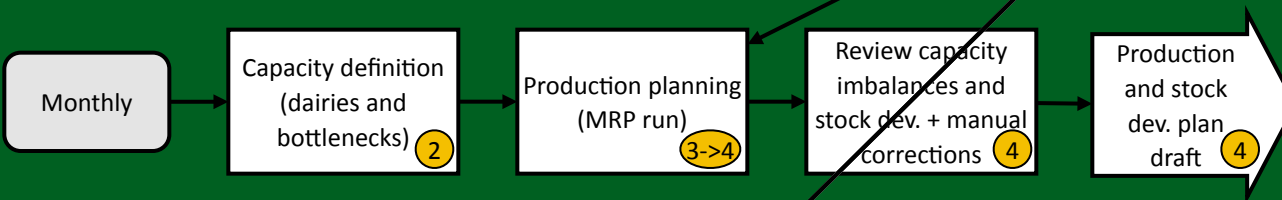
Day

HIGH LEVEL

Demand Management/ Markets/ Categories



Capacity/ production planning



Milk planning



Planning/ Finance/ Categories/ Markets

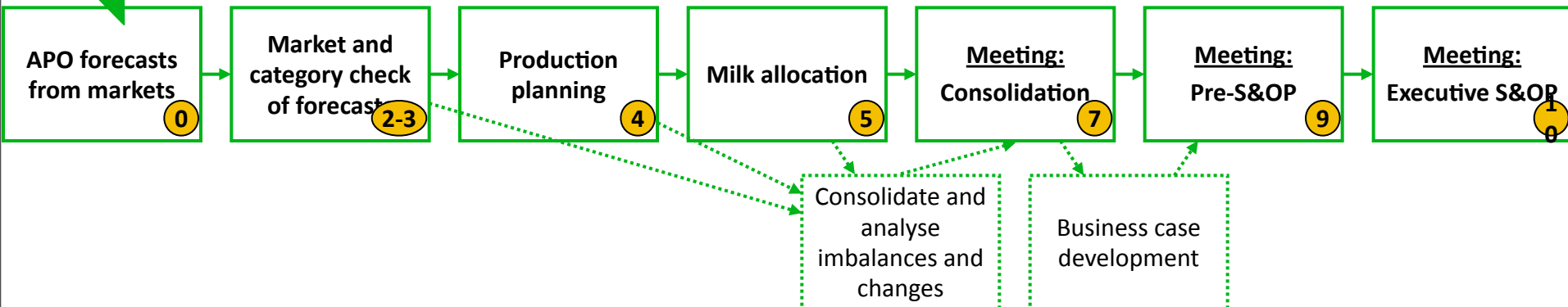


In the three central meetings, the participants have been chosen for ability to solve the task/ purpose of each meeting

HIGH LEVEL

Day

Demand signal
(APO forecasts) for
15-18 months



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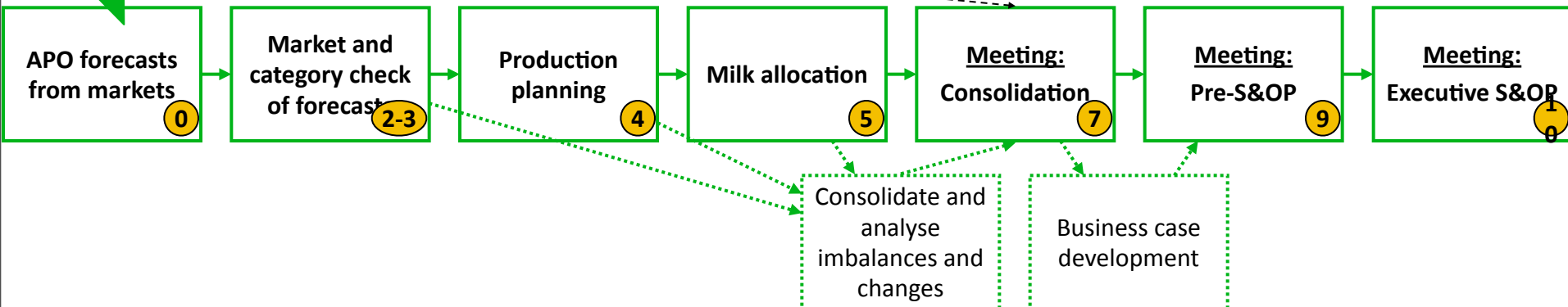
HIGH LEVEL

Day

Consolidation meeting

- To review imbalances 4-12 months ahead for
 - Capacity vs. demand
 - Milk/ fat vs. demand
- For key imbalances, the preferred scenarios are defined and business case tasks assigned
- 2 hour meeting with **participation of category product managers and demand/ production/ milk planners**

Demand signal (APO forecasts) for 15-18 months



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HIGH LEVEL

Day

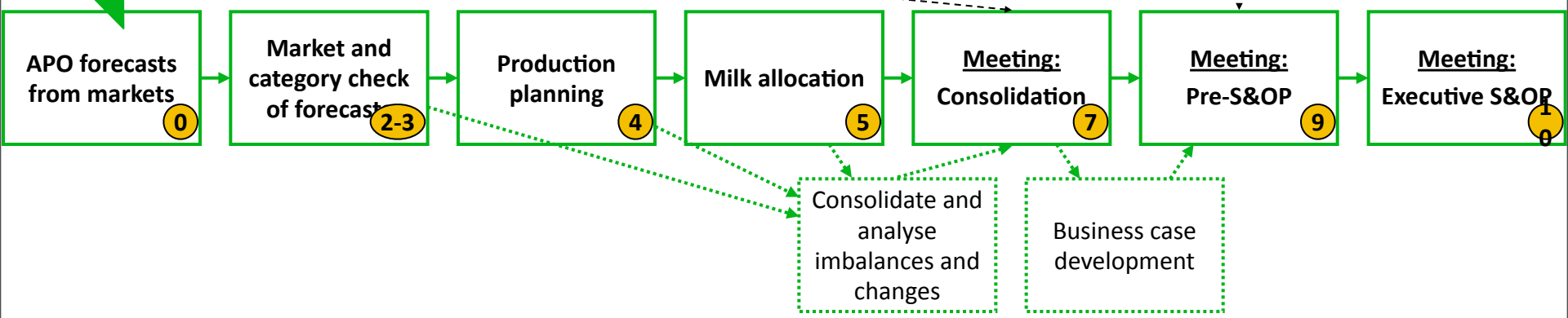
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Pre-S&OP meeting

- To review business cases and recommendations for key imbalances and make decisions or escalate to Executive S&OP
- 1 hour meeting with **participation of category heads, GCO demand planning, production planners and milk planners**

Demand signal (APO forecasts) for 15-18 months



Source: GCO S&OP project team

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HIGH LEVEL

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Executive S&OP meeting

- To approve overall plan, business case recommendations and make decisions for escalated issues
- 1½ hour meeting with **participation of market, category, supply, planning and finance executives**

Demand signal (APO forecasts) for 15-18 months



Consolidate and analyse imbalances and changes

Business case development

Source: GCO S&OP project team

The meetings are executed with strong discipline and always start with the expected key discussion points/ expected conclusions

FROM JANUARY 2011 CYCLE

The agenda for January 2011 Consolidation meeting - Agenda for Consolidation Meeting

Time	Content	Responsible
09.00 – 09.10	Welcome and introduction Action follow-up from previous cycle	NIBUE
09.10 – 09.20	Performance KPIs (Part 1)	JEI/ REVAH/ NIKLT/ NIBUE
09.20 – 09.45	Demand signal review (3 minutes each) (Part 2)	Product managers
09.45 – 09.55	Cheese (Part C)	RENI
09.55 – 10.05	Butter (Part B)	ANC
10.05 – 10.15	Powder (Part P)	REVAH
10.15 – 10.45	Milk (Part M)	PHL
10.45 – 11.00	Evaluation of the meeting and input to improvements	NIBUE

The Consolidation meetings (and Pre-S&OP) have 20-25 participants and are therefore executed with strong discipline and as short an agenda as possible

The agenda for the January 2011 Executive S&OP meeting - Agenda Executive S&OP

Time	Content	Responsible
10.00 – 10.10	Welcome and key conclusions	NIBUE
10.10 – 10.20	Action update previous cycle	NIBUE/ ABLA/ MK
10.20 – 10.35	Performance and process KPIs	NIBUE/ APO
10.35 – 10.45	Demand signal high level and by area (3 minutes each)	APO/ FI/ HASO/ JECOL
10.45 – 11.55	Capacity overview	DAKD
11.55 – 11.15	Milk and fat balance	ABLA/ NIBUE
11:15 – 11:30	Evaluation of the meeting and input to improvements	NIBUE

Key conclusions are presented first to provide a frame for understanding the material before it is actually presented

The fundamental principles and behaviours in S&OP must work like Ying and Yang to generate the best result

Fundamental principles

- Focus 4-12 months out in an ongoing routine S&OP meeting cycle
- Structured meeting agenda
- Anchored high in the organisation - run by an unbiased, responsible organisation
- Cross-functional fora
- Clear ownership and accountability for content and timing of inputs/ outputs
- Able to conclude financial estimate at the end of the S&OP cycle (long term)
- Analysed and documented business cases to fill gaps to target
- All cross functional decisions are channelled into the S&OP process
- Plan gives full visibility and transparency with opportunities and risks

Behaviours

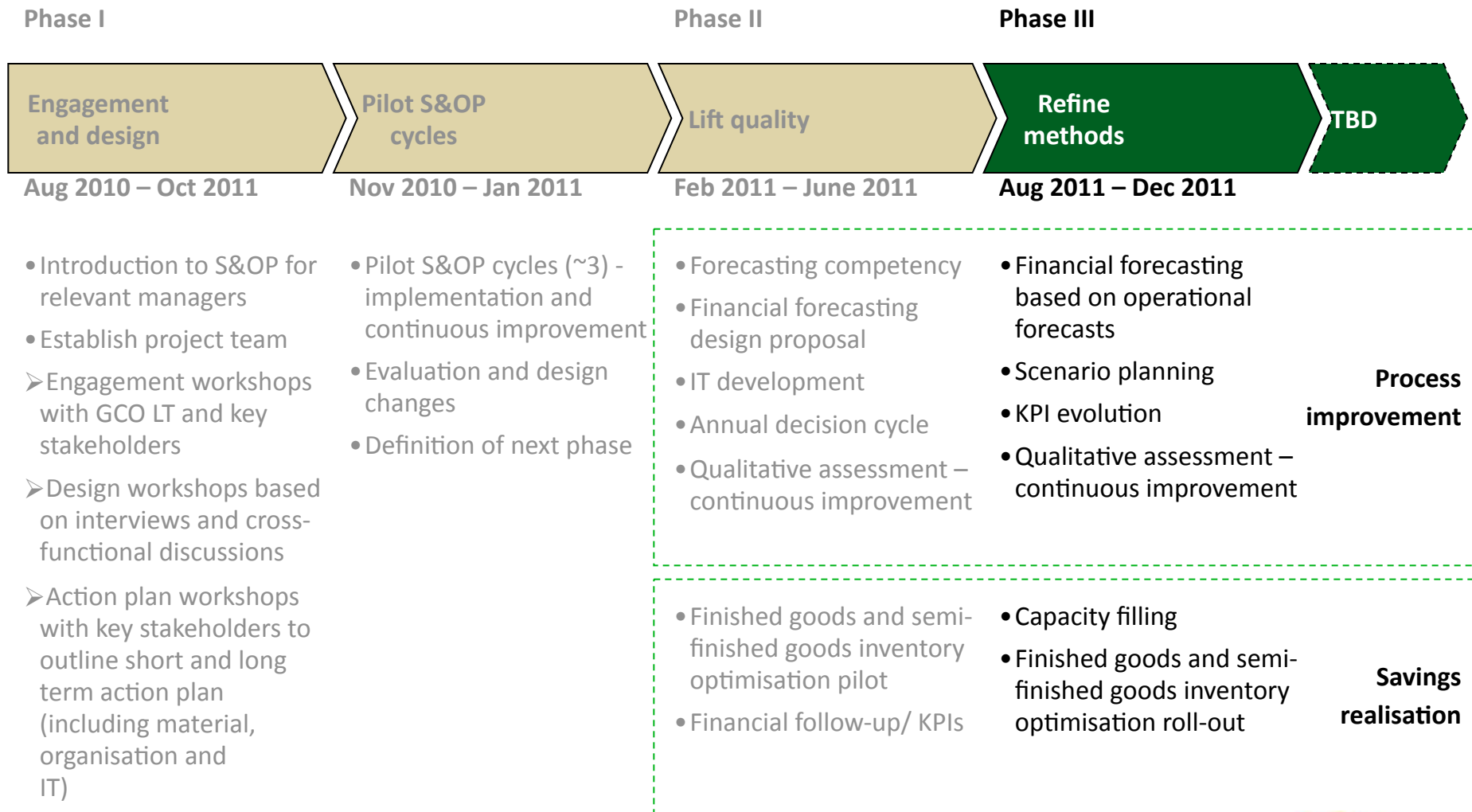
- Openness, honesty and action ability
- Unbiased forecasts to start the process (no second guessing)
- Decision-focused meetings (NOT data sharing) - participants (or substitutes) empowered to make decisions IN meetings
- Recommendations and proposals are part of the preparation work
- Fact-based, no conclusions without firm data behind it
- Everyone works for the agreed plan!

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An S&OP process must have a continuous development agenda - aligned to business priorities - to ensure attention and to reach full potential

HIGH LEVEL



Here, qualitative assessment of the process can help focus attention on weak points and guide development efforts

EVALUATION FEBRUARY 2011 – HIGH LEVEL

5 Best in Class	External collaboration, linked & long term plans	External value chain context, 2-3yr strategic	3yr strategic direction, delegated decision making	0-3 year	Strong leading by example, hold (external) people accountable	Externally aligned tools & processes, calendars	External parties (customers/suppliers) are also involved in bus.planning	A-Score also at all external parties
5 Advanced	High level of collaboration, use of scenarios, profit focus	High level of collaboration, use of scenarios, profit focus	P&L oriented decisions, high level of decision delegation	6-24mth rolling	Passionate about common results, service & improvement mindset	Sophisticated tools support S&OP need for information	X-functional teams physically put in same place, aligned on 1 goal	A-Score + financial performance
4 Better	Regular, proactive reviews, cross-functional & financial view	Use of scenario planning, external parties are prepared	Scenario based decisions, proactive risk mgmt, x-functional alignment	4-12/18mth	Acting fully transparent, proactive and honest towards team	Shared targets, unbiased honest view is rewarded	Strong team behaviour, eyes on the goals of total company	A-Score
3 Intermediate	Transparent assumptions, 12m plans, regular reviews	One set of numbers, regular reviews, agreed view on assumptions	Regular x-functional reviews, what if cases, taking aligned actions	0-6mth	Clearly acting on R&R well prepared, support other functions	Well defined and agreed R&R + RAID, discipline	Finds synergies with others to over deliver goals	B-Score
2 Basic	Some plans exist, occasional input, misaligned goals, fixed agreement	Regular x-functional review of short term issue resolution action	Functionally driven reviews, short term reactive decision	0-6mth	Sharing some data, disciplined attendance	Meeting agenda and timing defined and kept	Some x-functional sharing, optimise department goal with others	C/D-Score
1 Survival	Reactive actions, ad hoc & last min information, minimal sharing	Ad hoc high level consolidation, reactive actions, parallel plans	Occasional backward view, reactive decision functional silos	0-3mth	Low level of trust for other functions, blaming others	No R&R, no discipline and delegation	Work is oriented on functional silos	D/E-Score
Performance Area	Review	Consolidation	Decision making (Executive S&OP)	Horizon	Behaviour / Soft Skill	S&OP Process necessities	Cross functionality	KPI / Value delivery

Use scenario planning for milk/fat allocation

Professional skills

S&OP process & soft skills



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Over the year, certain topics must be discussed and decided at certain times

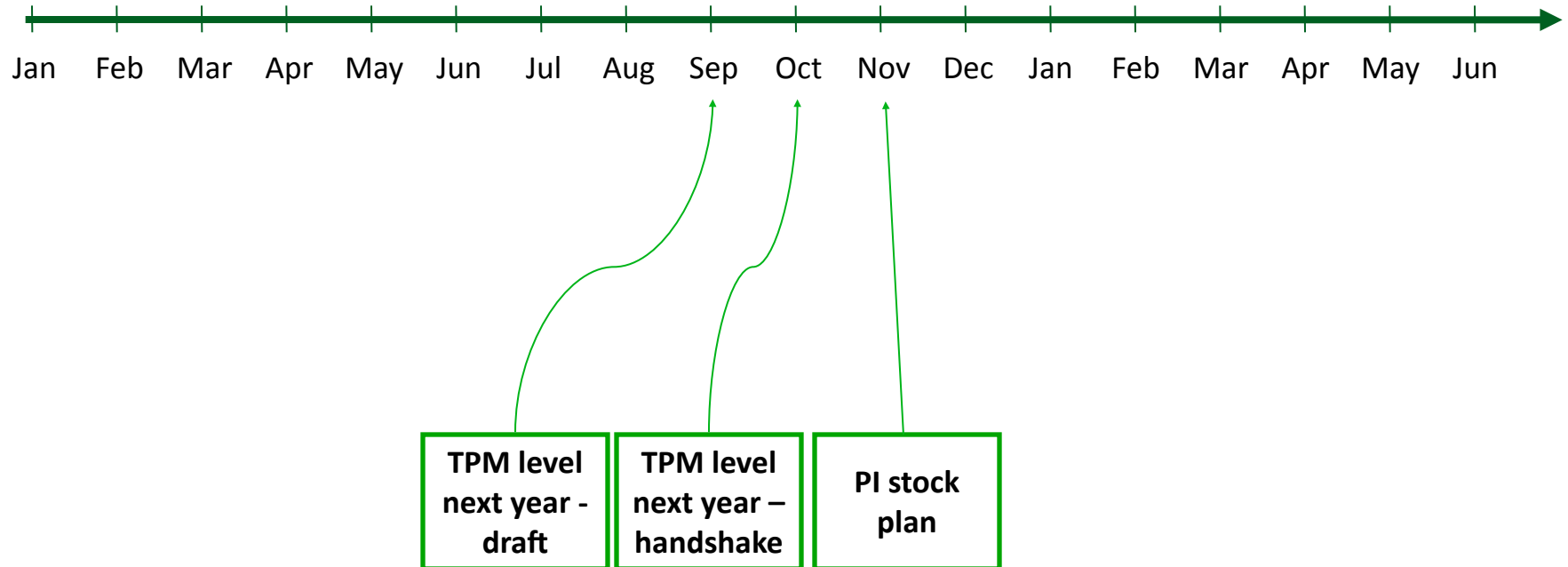
- Illustrative yearly cycle

ILLUSTRATIVE

S&OP cycle

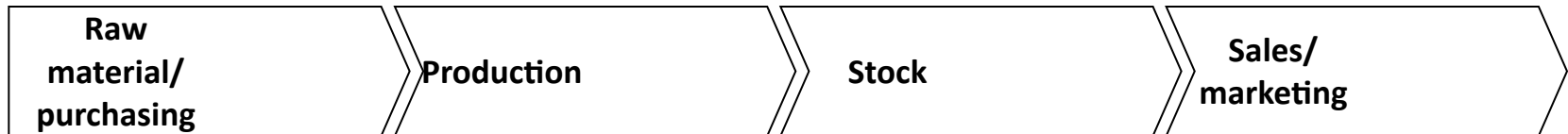


Calendar



We also worked with specific topics to include over time, and we run a continuous effort to define KPIs and targets

HIGH LEVEL



Topics

- | | | | |
|--|--|--|---|
| <ul style="list-style-type: none"> ● Raw material allocation ● Trading volumes and flexibility ● External sales and purchase ● ... | <ul style="list-style-type: none"> ● Allocation of scarce capacity resources ● Capacity moves/ closings, I.e. stock build-up agreements and follow-up ● ... | <ul style="list-style-type: none"> ● PI stock build up for butter - insurance policy ● Working capital tracking/ target setting/ action follow-up ● Seasonal stock building (e.g. feta) - pipeline filling/ replenishment/ phasing out ● ... | <ul style="list-style-type: none"> ● (Forecast transparency – demand changes/ discrepancies) ● Capacity filling ● Tenders – capacity and raw material effects – MUP evaluation ● Product introductions – phasing in/ pipeline filling/ replenishment ● ... |
|--|--|--|---|

- Current topics
- Suggested topics

● Not suggested
October 04, 2011



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Two paradigms exist in the finance world as for interdependence vs. independence of financial and operational forecasts

“One-number forecasting”

As valid as possible

Full volume
integration
between financial
and operational
forecasts

“Independency”

Freedom to diverge

Freedom to set
targets over and
above current
belief – stretch
people

Two paradigms exist in the finance world as for interdependence vs. independence of financial and operational forecasts

“One-number forecasting”

As valid as possible

Full volume integration between financial and operational forecasts

Ensures quality of operational forecasts and limits sub-optimisation based on different “realities”

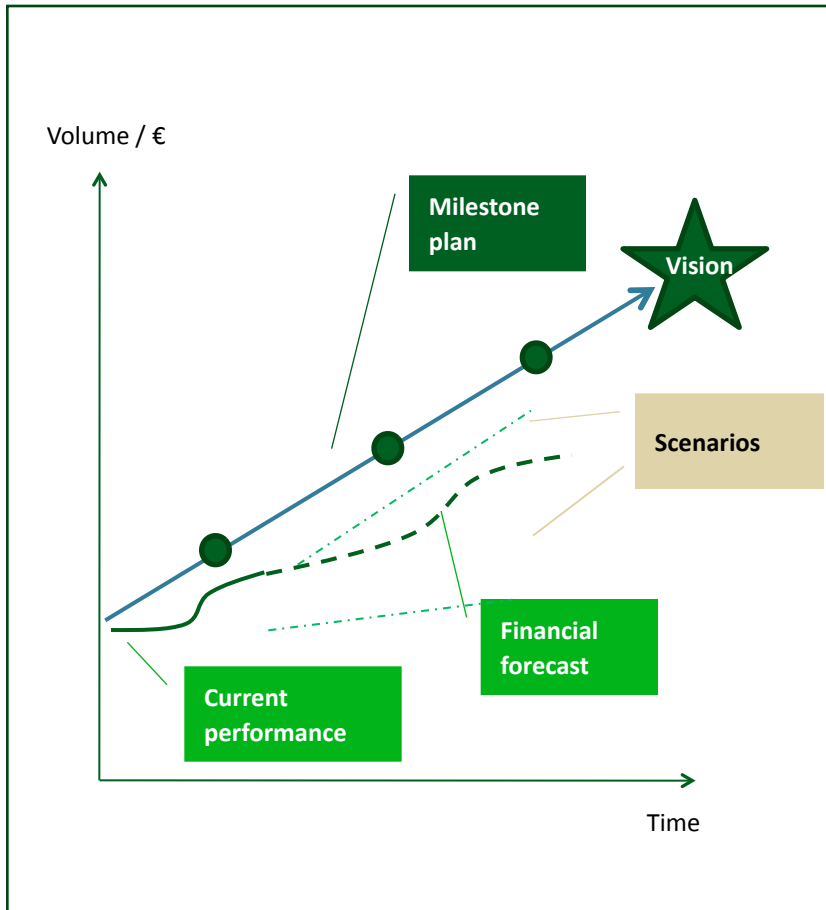
“Independency”

Freedom to diverge

Freedom to set targets over and above current belief – stretch people

Currently the future financial planning principles are being defined – Arla Foods will in future use operational forecasts as basis for financial forecasts

ILLUSTRATIVE



Characteristics (based on interviews)

Stretched Targets

- Targets could be based on milestone plan/ strategy
- Should be *different* from the financial forecast

Financial forecast

- Realistic!
- Best estimate for “current plans” financial performance 0 to 6/12/18 months ahead
- Rolling forecasting (quarterly/ monthly)
- Purpose is to forecast performance – not to be used for target setting

Scenarios

- Simulation of e.g. price changes, market changes
- Risk and opportunity analyses
- Should not be incorporated in financial forecast until a specific plan has been created