CASE #1 - SUPERMARKET DELI TURNAROUND
Problem Set-Up

The client is a national supermarket chain that is facing a very difficult situation. Low-price competitors like Wal*Mart, Costco, and Dollar General are stealing share and eroding margins in the traditional grocery business. Therefore, other departments within its stores, such as produce and deli, are becoming increasingly important to our client's financial health

In particular, the client is concerned about their deli department, a $700M business that has been reporting no profit growth over the last few years. The deli department consists of two main business lines: 1) deli meats and 2) prepared foods (sandwiches, fried chicken, etc.)

We have been asked to help the client understand why their deli profits are not growing and what they need to do to turn things around

Case 1

SUPERMARKET DELI TURNAROUND
Questions and Facts

Topic	Information to share with interviewee
Client's deli financials	• ***Share Exhibit 1***
Overall industry/ customers	• **Deli meat category has been flat to slightly declining recently** • **Prepared foods category has been growing at roughly 10% per year as people have less time to cook at home**
Competitors	• **Increasing competition from deli departments of other supermarkets, discounters, etc. – e.g., expanding product lines, increasing advertising** • **Also compete with fast food restaurants in prepared foods category**
Client's product mix/ recent events	• **Mix has remained constant, with exception of two products introduced a couple of years ago – BBQ chicken wings and "made to order" sandwiches** - **both products have been a major boost to prepared foods revenue**
Info on new products	• **BBQ wings are similar to the chicken wings the company already sells, although they take a little longer to fry and are tossed in BBQ sauce after frying** • **"Made to order" sandwiches is client's response to Subway, etc. – for two hours during lunchtime and two hours during dinnertime, one employee's sole task is to make sandwiches to order for customers**
Financials of new products	• **Revenues for each product are $40M annually** • **Costs not broken down at product level** • ***Give info on Exhibit 2 as requested (but do not hand sheet to interviewee)***

SUPERMARKET DELI TURNAROUND
Exhibit 1

		$M		
		2002	2003	2004
Deli meats	Revenues	260	255	260
	COGS	160	155	160
Prepared foods	Revenues	360	400	440
	COGS	190	230	270
Overall	Revenues	620	655	700
	COGS	350	385	430
	Gross margin	270	270	270

SUPERMARKET DELI TURNAROUND
Exhibit 2

BBQ wings

Price	$5	for 20 pieces
Total material cost	$0.10	per piece
Prep time	15	minutes per batch of 200
Employee cost	$20	per hour (fully loaded)
Total COGS	$2.50	per 20 pieces
Margin	$2.50	per 20 pieces

"Made-to-order" sandwiches

Price	$4	per sandwich
Avg. sales/store	20	sandwiches per day
Total material cost	$2	per sandwich
Employee cost	$20	per hour (fully loaded)
Dedicated hours	4	hours per day
Revenue	$80	per store per day
Total COGS	$120	per store per day
Margin	$(40)	per store per day

Note: Boxes indicate figures that should be calculated by the interviewee

SUPERMARKET DELI TURNAROUND

Sample Approach

Main question

What should supermarket do to turn around deli?

Key areas to explore

Revenue and profit breakdown within deli

External factors influencing the overall deli market

Analysis

Revenue and profit breakdown within deli:

- Deli meat revenue and profits flat - consistent with overall category
- Prepared foods showing revenue growth (10% consistent with category) but no profit growth – therefore declining margins – why?
  - made-to-order (MTO) sandwiches losses offsetting profit growth from BBQ wings

External factors influencing the overall deli market:

- People have less time to cook at home – prepared foods category growing, deli meats category flat
- Increasing competition from other deli departments – starting to expand product lines, increase advertising, etc.

Recommendation

- Eliminate made-to-order sandwiches (at least in low-traffic stores or during non-peak hours)
- Raise or lower prices on MTO sandwiches (depending on demand elasticity)
- Boost demand for MTO sandwiches (e.g., advertising, promotions, merchandising)

Other factors

- Eliminating MTO sandwiches or boosting demand can impact overall traffic in store and deli

SUPERMARKET DELI TURNAROUND
Framework and Analysis (I)

There are three main questions that the interviewee needs to answer

- **Which part of the business is responsible for the lack of profit growth – deli meats, prepared foods, or both?**
- **Is the lack of profit growth caused by flat revenues, increasing costs, or both?**
- **What is causing the flat revenues or increasing costs (and what should the client do)?**

Based on Exhibit 1, the interviewee will see that gross margins for both business lines are flat. Furthermore, deli meat sales have been basically flat while prepared foods sales have been growing at 10%.

The interviewee should recognize that the client’s deli meat and prepared food sales have been growing at about the category averages; therefore, revenues are not the main issue here. Deli meat COGS have been more or less flat, mirroring sales. However, despite robust growth in prepared food sales, prepared food profits have been flat, implying deteriorating margins.

At this point, ask the interviewee for some potential reasons for deteriorating margins (e.g., change in product/sales mix, rising material costs, rising labor costs).

It is critical that the interviewee asks about changes in product mix, in which case the interviewer should inform him about the BBQ chicken wings and the “made to order” sandwiches. The interviewee should be suspicious at this point and ask to learn more about these products.

SUPERMARKET DELI TURNAROUND
Framework and Analysis (II)

By doing a back of the envelope analysis of product profitability (based on data in Exhibit 2), the interviewee will find that BBQ wings have a 50% margin, indicating that they are not a problem. On the other hand, the interviewee will find that the client is losing a lot of money on the “made to order” sandwich concept.

The interviewee should then be asked for recommendations, which could include: 1) eliminating the “made to order” sandwich, 2) restricting the sandwich to busier stores or during busier times of the day (e.g., lunch hours only), 3) raising or lowering prices (to either increase profit per sale or units sold – will depend on demand elasticity), and/or 4) boost demand (through increased advertising, promotions, better merchandising, etc.). A good answer will also consider the second-order effects of eliminating the product or boosting sales (the effect on traffic in the deli and the overall store).

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Case 2

CHINA OUTSOURCING OPPORTUNITY
Problem Set-Up

The client is a national manufacturer of plastic consumer products that are sold in a variety of retail formats, including supermarkets, discounters, club stores, and dollar stores. The company has three main product lines – 1) freezer bags, 2) plastic plates and utensils, and 3) specialty plates and utensils.

The CEO has been reading for some time about American companies outsourcing their production overseas to low-cost countries such as China. She wonders whether this makes sense for her company as well. It worries her that none of her main competitors have established foreign production capabilities; on the other hand, this could be a tremendous opportunity to gain a competitive advantage.

We have been asked to help the client understand the benefits and risks of moving its production capabilities to China and to provide a recommendation.

CHINA OUTSOURCING OPPORTUNITY
Questions and Facts (I)

Product description	Costs (China vs. U.S.)	Consumers	Competitive landscape
Freezer bags • Plastic bags used mainly to store food items in freezers	• All three product lines have similar cost structures and savings • *Give interviewee Exhibit 1*	• Top purchase criteria is quality, since low quality bags will result in food spoilage	• Client is #3 in category, 200 million lbs. sold • Category leader has strong brand and strong innovation
Plastic plates and utensils • Disposable plates and utensils; intended for single/limited use	• All three product lines have similar cost structures and savings • *Give interviewee Exhibit 1*	• Top purchase criteria is price	• Client is #2 in category, 300 million lbs. sold • Client at cost parity with category leader but has weaker brand
Specialty plates and utensils • Plastic plates and utensils produced for specific retailers, customized to their design specs	• All three product lines have similar cost structures and savings • *Give interviewee Exhibit 1*	• Top purchase criteria is style/design • Because many products are new and untested, demand is highly variable	• Client is #1 in category, 100 million lbs. sold • No strong competitors

CHINA OUTSOURCING OPPORTUNITY
Questions and Facts (II)

Topic	Information to share with interviewee
Current client production capabilities	• **All products are made in a single factory in Ohio** • **The factory is at capacity and the company is considering building or acquiring a nearby facility**
Chinese production options	• **Client has no previous experience in building and managing a factory overseas** • **Client has met with several Chinese manufacturing partners and has done initial product testing** - **Cost** • **all three product lines have similar cost structures and savings** • ***give interviewee Exhibit 1*** - **Quality** • **lower quality on freezer bags** • **equal quality on plastic plates and utensils (both regular and specialty)** - **Lead time** • **need 3-4 weeks of additional lead time for each product line for transportation from China to U.S. distribution center**
Chinese market, current client presence	• **All three categories are relatively underdeveloped but growing, dominated by local manufacturers** • **Client does not currently have any sales in China, although a few of their U.S. customers (e.g., Wal*Mart) do have presence there**

Case 2

CHINA OUTSOURCING OPPORTUNITY
Exhibit 1

Costs	Costs in U.S. ($/lb.)	Costs in China relative to U.S.	Costs in China ($/lb.)
Labor	0.30	8% of wage rate 80% of productivity	
Material			
• Plastic resin	0.30	80%	
• Other material (incl. packaging)	0.20	75%	
Variable overhead	0.05	140%	
Fixed overhead	0.10	60%	
Transportation			
• China to U.S. distribution center	N/A	$6K to ship 40K lbs.	
• U.S. distribution center to customer	0.05	Same	
Total	1.00		

Case 2

CHINA OUTSOURCING OPPORTUNITY
Sample Approach

Main question

Should plastics manufacturer move production to China?

Key areas to explore

Cost savings	Consumer behavior and purchase criteria	Effect on current production capabilities

Analysis

Cost savings
- Would save $0.25/lb. (25% of current costs)
- At current production levels, would save:
  - $50M in freezer bags
  - $75M in plastic plates and utensils
  - $25M in specialty plates and utensils

Consumer behavior and purchase criteria
- Quality is top purchase criteria for freezer bags
  - lower quality from China
- Price is top criteria for plastic plates and utensils
- Style is top criteria for specialty plates and utensils
  - highly variable demand requires short lead times

Effect on current production capabilities
- Current plant is at capacity
  - outsourcing would eliminate need to build additional capacity
- Plastic plates and utensils are 50% of total production
  - outsourcing may create too much extra capacity

Recommend-ation

- Outsource plastic plates and utensils to China
- Do not outsource specialty plates and utensils
- Do not outsource freezer bags (although further analysis may be warranted)

Other factors

- To compensate for extra capacity that would be created in current plant, could produce new product line, rent out spare capacity, or move to smaller facility

CHINA OUTSOURCING OPPORTUNITY
Framework and Analysis (I)

The interviewee should start with a brief overview of the potential benefits and risks of outsourcing to China. The main benefit is lower costs, mostly driven by inexpensive labor. A secondary benefit is a possible springboard into the emerging Chinese (and other Asian) market. Risks include lower labor productivity, possible quality issues, longer lead times, additional transportation costs, and potential communication/coordination issues. Ask the interviewee about the ramifications of longer lead times – they include greater carrying costs, higher cycle and safety stock, greater forecast error, and less responsiveness to demand.

There are three main questions that the interviewee needs to answer:

- **How much cheaper is producing in China?**
- **What do consumers value and how would outsourcing affect those criteria?**
- **What are the client's current production capabilities and how would outsourcing part/all of their production affect the remainder?**

First, the interviewee should size the opportunity – is this a $5 million or $500 million opportunity? By solving for the last column in Exhibit 1, the interviewee will find that the client would save $0.25/lb. (25% of current costs) by outsourcing to China. Given current production levels, the client would save $50 million by outsourcing freezer bags, $75 million by outsourcing plastic plates and utensils, and $25 million by outsourcing specialty plates and utensils. Two notes: 1) costs may increase if the Chinese Yuan rises versus the dollar and 2) these estimates do not include a profit margin for the Chinese outsourcing partner.

CHINA OUTSOURCING OPPORTUNITY
Framework and Analysis (II)

The interviewee must recognize, however, that cost savings alone are not sufficient to make a decision. It is important to understand how an outsourced product will affect sales. The interviewee should suggest market research to understand consumer behavior.

Freezer bags: since customers' top purchase criteria is quality and outsourcing would produce lower quality bags, the interviewee should raise a red flag here. A more sophisticated recommendation would be to conduct market research to see the impact on sales of the lower quality bag at lower prices – even though quality is more important than price, the magnitude of a price change may override the drop in product quality.

Plastic plates and utensils: the top purchase criteria here is price, which makes this product line an attractive outsourcing opportunity. Ask the interviewee what the client should do with the cost savings – potential recommendations include dropping price to steal share, investing to defend its position in case competitors begin outsourcing (e.g., brand, innovation, customer service), and milking the product line as a cash cow.

Specialty plates and utensils: the highly variable and unpredictable demand for these products means that shorter lead times are critical in order to adjust production quickly. Longer lead times will result in greater forecast errors, higher safety/cycle stock, and more unsold inventory and/or out-of-stocks. Therefore, specialty plates and utensils should not be outsourced.

CHINA OUTSOURCING OPPORTUNITY
Framework and Analysis (III)

An analysis of customer purchase behavior indicates that plastic plates and utensils should be outsourced, specialty plates and utensils should not be, and freezer bags probably should not be. The final step is to understand the impact of outsourcing on the client's current production capabilities. For example, will it lead to plant closings (resulting in closing costs and possible negative publicity)? Will it lead to underutilization of current facilities?

Since the current plant is already near capacity, moving plastic plates and utensils offshore would actually save the client from investing in new facilities. However, since that product line makes up 50% of total production (in terms of lbs.), removing it may create too much extra capacity in the current plant for the two remaining lines. To compensate, the client could produce a new product line, rent out the extra capacity, or move to a smaller plant.

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GROWING SPECIALTY PAPER SALES
Problem Set-Up

Your client is a leading manufacturer of specialty papers sold to commercial printers. The client produces self-adhesive sheeted papers that are ultimately used in a variety of labeling applications – including the labeling of consumer goods and the printing of self-adhesive signs.

Your client's operations are profitable, but the business has failed to grow over the past few years. The client would like to invest in the business and you have been asked to identify opportunities for growth.

Case 3

GROWING SPECIALTY PAPER SALES
Questions and Facts (I)

Topic	Information to share with interviewee
Supply chain	Raw mats → Layering → Sheeting → Packaging → Distrib. Raw mats: • Rolls of paper • Adhesive • Non-stick liner Layering: • Adhesive and liner applied to rolls Sheeting: • Rolls of layered paper cut into sheets • The client is not capacity constrained in its manufacturing processes • The client's manufacturing and packaging operations are currently configured to package specialty papers in boxes
Customers	• There are approximately 24,000 commercial printers in the United States • Printers are roughly categorized into three groups: small, medium, and large • Differences among the groups are driven by the type of printing technology employed and the size of print jobs that the printers are able to serve • Printers prefer to receive product from the specialty paper manufacturers in different forms, primarily driven by the type of printing technology employed - Small printers prefer to receive their specialty paper in boxes - Medium printers prefer cartons of specialty paper - Large printers prefer to receive palletized shipments of specialty paper
Market share	• The client has approximately 30% market share with small printers and only 10% share with medium and large printers
Client financials	• Margins are currently acceptable but management is against cutting price to gain market share, knowing that competitors can match price cuts • Price and cost to serve per equivalent box are different for each customer type

Case 3

GROWING SPECIALTY PAPER SALES

Questions and Facts (II)

	All figures are per equivalent box		
	Small (boxes)	Medium (carton)	Large (pallets)
Price to printer	20.00	18.00	15.00
Materials	5.50	5.50	5.50
Coating	1.00	1.00	1.00
Sheeting	0.50	0.50	0.50
Packaging (direct costs)	3.00	2.00	1.00
Gross profit/($ per equivalent box)	10.00	9.00	7.00
Number of printers	20,000	3,000	1,000
Annual usage (number of equivalent boxes)	100	500	3,000
Total potential profit pool ($)	20,000,000	13,500,000	21,000,000

Information revealed only when asked – interviewee completes all calculations

GROWING SPECIALTY PAPER SALES
Framework and Analysis (I)

The problem set-up indicates that the client wants to invest in this business. Investment can take many forms including expansion of manufacturing operations and capacity, expansion of customer-facing activities, and acquisition of competitors. Its interesting to note that this is currently a profitable, no-growth business for the client. Investment decisions cannot be made unless the management team (and the interviewee) understand the market conditions as well as the client's internal capabilities

This case does not lend itself well to traditional "case solution structures". A strong initial response is to list a set of internal and external factors that must be understood and evaluated. Ultimately, the interviewee should decide whether investment is warranted, and if so, where

Strong hypotheses might include

- **Assuming the client is not capacity constrained, there are likely groups of customers that represent opportunities for profitable growth**
- **Depending upon the current go-to-market strategy, the client may need to re-evaluate the way that it is configured to serve existing and potential customers**

GROWING SPECIALTY PAPER SALES
Framework and Analysis (II)

Assume the client can expand their packaging operations to better serve medium or large customers, but not both

Interviewee should recognize that a comprehensive solution evaluates the required investment to serve a particular market segment (packaging line, manufacturing operations, additional SG&A) against the expected return

- **For simplicity, interviewee should ignore taxes and depreciation, assume SG&A is fixed**

Client economics and cost to serve each customer group are shown on Exhibit 1

Interviewee should evaluate the profit pool from serving medium and large customers. This should be based upon an assumption about the size of the market that the client can capture. Assuming the client can match its small printer market share, the client could capture an additional 20% of the medium or the large printer customer segment

Assume the following (and reveal to interviewee when asked)

- **Investment and operation of carton packaging line would cost $675,000 per year**
- **Investment and operation of the palletizing line would cost $2,300,000 per year**

Case 3

GROWING SPECIALTY PAPER SALES
Framework and Analysis (III)

A logical conclusion would be that an investment in a carton packaging line would be a superior investment compared to the palletizing line

A strong answer may also include following

- The carton packaging line is a less-risky investment (requires less up-front capital)
- The solution assumes a static environment. If large printers are growing in number and or usage of specialty paper, this may change the answer
- The investment in a new carton packaging line would need to be evaluated against other potential investments to understand if it is the optimal use of the client's capital