



Finance Must Play a Role in Sales and Operations Planning

Research shows top companies regularly merge financial outlook with sales and operational plans

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Summary

In a recent research study entitled "Sales and Operations Planning," Ventana Research found that companies reporting the largest gains in revenue, margins, inventory turns and customer satisfaction have a rigorous monthly review process that combines sales and operational plans with their financial forecasts. It is an approach that views the sales and operations planning (S&OP) process as a strategic function and the resulting S&OP plan as the main driver for all other operational plans in the business. Yet it is clear from our research that most companies underutilize S&OP. In doing so, they are failing to seize an important opportunity to improve their performance and competitive position. To be sure, there are other success factors that improve operational performance, but it isn't hard to recognize that doing considerably more with S&OP is both feasible and worthwhile.

View

Although best practices in this discipline have existed for more than 20 years, most companies are new to S&OP and so lack a rigorous process. In the Ventana Research study, 65 percent of companies with a formal S&OP process in place have had it for less than five years. Most use it in limited fashion, for short-term planning for single entities or a single line of business that focuses only on demand, not supply. Many companies (42 percent) that have multiple factories or regional operating facilities do not include them in S&OP. Nor do most include new product introduction plans (57 percent) or use it to reconcile financial plans (60 percent) or to account for strategic initiatives and projects (59 percent). Even fewer (37 percent) have formal meetings where executives review S&OP.

To put this laxity into perspective, we note that companies have been doing rigorous financial accounting in the U.S. for nearly a century. Every day they record millions of business transactions using generally accepted accounting principles (GAAP). These principles – which more precisely are objectives and conventions – have evolved over time into a framework to govern how financial statements are prepared, reviewed and presented. In general, these financial transactions and statements record past events and actions.

In contrast, formal S&OP – the major set of operational planning processes that link strategy to execution – is about determining future actions, particularly what will happen in sales and in company operations. It impacts not only future demand and supply volumes but also revenue attainment, inventory levels, asset utilization, profits and, ultimately, customer satisfaction. Yet our research reveals that few companies apply the same kind of thoroughness to S&OP that they do to their financial accounting and reporting – yet. While no regulatory framework of the kind governing financial statements exists for S&OP, many buy-side and sell-side stock analysts are beginning to ask companies when they deliver earnings guidance what their S&OP plan reveals about potential performance.

Central to establishing this much-needed process rigor is the finance department. Our research found that involving Finance in the S&OP process is the second-most significant contributor to achieving gains in revenue, profit, customer satisfaction and forecasting accuracy. For example, in general 42 percent of companies include Finance as part of their S&OP plan development. But 90 percent of companies that reported overwhelmingly large gains in revenue, and 70 percent that reported gains in gross margin, include Finance as part of their S&OP process. We also found that companies that do a good job of aligning their financial plans and S&OP plans hit their targets more often. In fact, this was the most significant factor contributing to overwhelmingly large gains.

Assessment

Ventana Research believes that companies committed to maximizing results by establishing true performance management must put in place the same kind of rigorous process for their S&OP that they use for financial accounting and reporting. Toward this end, finance executives must take a leadership role in process improvement, using the S&OP plan as one of the drivers for their own financial and performance outlooks. When S&OP is done right and supported by the appropriate technology, it will synchronize the activities and resources of individual departments and the company as a whole as they respond to changing customer and market demands. Thus, when S&OP is part of an overall performance management process it will connect operations to financial objectives in ways that optimize organizational performance.

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