

the distribution of sales in Grocery

80:20 it is not!

About 12 years ago, in 1987 to be precise, I read an article written by Porter Henry, President of Porter Henry & Co. In an article entitled 'The Important Few - The Unimportant Many' he mentioned in passing that the 80:20 distribution with which we all are so familiar, does not describe the distribution of things in FMCG. In his original article he used data to construct calling plans for a territory, and to illustrate how easy it is to over-service small customers - and thus by definition under-service the few big ones who count. In fact Porter Henry did not make a big song and dance about the fact that 80:20 does not fit grocery, so I will address that issue now.

The 80:20 rule is so well known because it does describe distributions which fit many situations in business. In fact it describes accurately the distribution of sales in industrial selling, where one or two big customers will dominate your orders. But wherever consumers play a large part, there is a different distribution. In this situation the sales are far more evenly spread.

So if you are looking to:

- optimise your sales territories, and ensure your merchandisers or sales reps allocate their time efficiently
- determine if your sales are adequately distributed across a territory
- find out if your product range is too deep
- find out if you should expand your product range

You need to take a close look at 65:15

How do we know it works? Well I have had the occasion over the last ten years to test the distribution myself. In Australia Grocery Chains do not release sales by store, so it is only when I had access to direct store deliveries or alternate FMCG channels like pharmacy that I could test the distribution. I found in the distribution of retail customers for fresh and frozen poultry sold to butchers, supermarkets and delis, and for suncare products sold through pharmacies that the distribution was spot on. I also tested a slight variation in confectionery - the sales per SKU. Here again I found that for a typical confectionery manufacturer 65% of sales came from 15% of the range. In confectionery wholesale distribution I found that 65% of sales came from 15% of customers and again I also found in distribution that 65% of a confectionery wholesaler's sales revenue came from 15% of the product range. Will you always find this distribution? Obviously no. It is possible to mess up your business so that you have the wrong customers or product range. So my advice is that if you find your sales do not fit this distribution, first assume you have a corporate problem before questioning the 65:15 rule in FMCG.

How do I use it?

The rule is 65:20:15 gives 15:20:65. If you are analysing a sales territory, and you rank your customers in size order from biggest to smallest, you will find that the first 15% (biggest) give you 65% of total cumulative sales, the next 20% account for 20% of sales and the last 65% of customers only account for 15% of sales. Similarly if you are analysing sales by product, and put the products in rank order from biggest to smallest, the first 15% of the products will deliver 65% of your total sales, the next 20% only 20%, and the last 65% a measly 15% (See Figure 1 opposite).

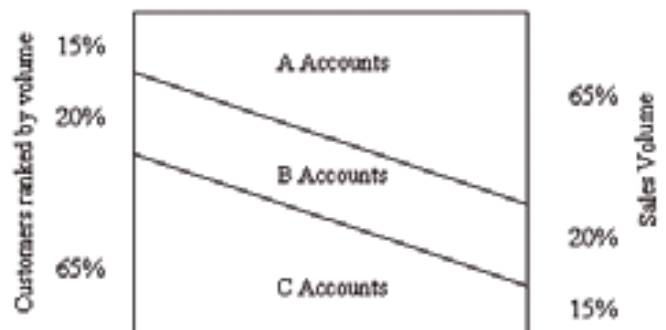


Figure 1



You might be tempted to cut the 65% that only deliver 15% of sales. If indeed you are not profitable, this may be a factor. You should bear in mind that no matter how small your product range (within limits) you are likely to end up with a long tail. However if you find that the last 65% of the product range delivers 20% of the sales, it means your first 35% of products delivers 80% instead of 85% and suggests your range is too large. Similarly if the last 65% of products delivers 10% of sales, you are getting 90% of your sales from only 35% of the range and suggests you really do need to extend the range. Equally if you are not getting 65% of sales from the first 15% of your outlets, maybe your product distribution is patchy and you do not have a fair share of the larger outlets. Or if you are getting much more maybe you have neglected the smaller customers.

Using the model to allocate time to customers

This issue was very well described by Porter Henry. Space does not permit the same coverage here. Pick a sales territory and obtain a customer sales report. Put them into rank order, biggest to smallest. Count down the first 15% of customers. These are the **A** customers. Add up their sales and it should be 65% of the territory.

The real value of this 65:15 rule is that if you do not know the sales per customer, as long as you can rank them, possibly by estimated sales, or facings per store or some other measure, the first 15% by number will be the **A** customers. If however you do know the sales value, or can reasonably estimate it, you can work out the sales per call your people are managing. (This works fine for centralised buying where merchandisers do not take orders, but whose efforts contribute to sales) The next 20% of customers will be the **B** customers, and the rest are **C**'s (at least at this stage)

Now work out how many calls per year you have available, allowing for leave etc. Generally you will not exceed 200 working days for full time people. Set the frequency for each class. Typically that might be **C**'s once per month or six weeks, **B**'s every two or three weeks and the **A**'s weekly - maybe some even bi-weekly. Now multiply out the total number of calls and discover you do not have enough time. Then reassess the call frequency, or split the territory. This exercise is complicated by the need to distinguish between calls to carry out shelf routines and calls to erect promotions or check compliance. Unfortunately you have to dart around a territory to match promotional activity, whereas routine work can be planned and travel distances optimised. The final result might look like this schedule:

Customer types	No of Customers Customers	Sales in this Territory per year	Average Sales per Customer per year	Call Frequency	No of Calls per week	Sales Value per call
A	15	\$1,300,000	\$86,667	Weekly	15	\$1,805
B	20	\$400,000	\$20,000	Every 2 weeks	10	\$833
C	65	\$300,000	\$4,615	Monthly	16	\$390
Totals	100	\$2,000,000	\$10,000		41	\$1,016

The last column is worked out on the basis of 48 productive weeks, thus 48x15 calls to **A** customers in a year, or \$1,805 per call. This calculation is quite fair, even where we are talking about merchandisers who do not sell. We are trying to see whether their costs are covered by the sales that do occur! This table shows how scary the numbers become where the customers are many and small. For example if you plan to keep direct merchandising costs to 2% of sales value, a \$390 average value of a call, generates \$7.80 for a call. Bear in mind that your 2% of sales must relate to the average sales per call, in this case \$1,016. However it is sensible to plan around this figure within each category, although it is almost certain that the bigger **A** customers will not need 2% and the smallest **C** customers will need considerably more than 2%. Note it will take an average of 18.7 **C** customers to equal one average **A** customer (the ratio of \$4,615 to \$86,667 is 18.7). So even if you could find 18.7 **C** customers, you would probably not cover your costs in doing so. The real message is make sure you never lose sight of the A and B customers!

The cost of a call in Grocery is related to the time in store, and thus short calls will cost less than longer calls. Nevertheless you probably cannot really service a supermarket in under 20 minutes, so you have to be sure \$7.80 is enough (2% of \$390). If it is not, you need to call less frequently, and spend more time when you do call. This sort of exercise can lead to a new customer classification - **D** for do not call as they are too small. It is a judgement call as to the extent to which you should under-service the big **A** customers and over-service the **C** customers in terms of sales costs as a percentage of sales revenue.

Inevitably you must offer the **C** customers some level of service, and in the above example if you call on the **A** customers weekly, the model suggests you should call on the **C** customers once every 18.7 weeks. Clearly that is not going to go down at all well with the **C** customer. And it illustrates the folly of over-servicing customers who simply will never generate enough sales to pay for the time invested. And while you are wasting time on the **C** customers, your competition may be gaining distribution in the **A**'s. I know in Australia in the last few years many companies have



said - I can't influence anything in the chains, but I can in the independents. So they have focused their sales force on the **C** customers. However this does not mean that they do not service the **A** and **B** customers, but all the effort goes into **C**'s. I know the logic seems to have merit, but I fear the day of reckoning. In Australia, the chains account for about 85% of sales, and the independents, with the exception of Western Australia, mostly run small stores.

If the logic of another paper on this site is employed here, 41 calls a day is about 13 per day, based on the six hour three day model favoured by merchandisers. On that basis the direct cost of each hour in front of a customer is about \$30.00 per hour. At 13 calls per day, the in-store call duration is about 12 to 15 minutes at maximum. That has a value of \$6.00 to \$7.50 per call. If sales costs are to be kept to 2%, then the average value per call needs to be \$375.00. In this example it is an average of \$1000.00, suggesting that possibly the call rate is far too high, and that this representative/merchandiser should slow down and spend more time in-store and make fewer calls per day. It probably also means the territory is too big. The old style sales managers always wanted high call rates - but here I am recommending call rates matched to the value of the business.

One of the common issues raised by sales people when I point out the folly of calling too frequently on **C** customers is the comment: 'I only call on them when I am in the area.' This sounds reasonable, until you analyse the proportion of costs spent on travel versus time costs. At worst, when you are doing 10 calls per day, travel costs will be about 30% of costs, so the sales person should be worrying about maximising the use of time, not travel costs. And adding an extra **C** customer who is close to an **A** or **B** will not add much travel cost, but it will use up time. There is never a good reason to over-service **C** customers!

The real beauty of the 65:15 rule is that it enables you to classify your customers accurately without necessarily knowing the precise sales per store. All you need to be able to do is rank them in order. It is not difficult to determine the approximate sales per category in each store, if you spend some time asking store staff. You can use other measures like finding out how many per week you are selling of your major lines. Provided you have built up a good relationship with store staff, this data is forthcoming.

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