Integrating Supply and Demand

At many companies, sales generation activities have become disconnected from the operational activities required to fulfill that demand — resulting in conflicting objectives and foregone business opportunities. Bringing the supply and demand sides of an enterprise together can represent a significant opportunity for efficiency and value creation.
Many companies compete in multiple product or customer categories, each of which requires a distinct supply chain capability. Such companies are challenged to develop capabilities in both cost leadership and product or service differentiation — a tall order, given that the ability to compete in different strategic segments at the same time requires precise coordination of the sales side of the company with supply chain operations. This is especially tricky given the fact that in many organizations, the two sides are completely disconnected, a perennial problem that management thinker Peter Drucker considered one of the “great divides” in management. The divide between demand and supply is a key reason that companies are so often trapped into selling excess products well below market rates or losing sales because an inventory shortage makes it impossible to fulfill demand.

As remarkable as it might seem in this age of big data and just-in-time delivery, our research suggests that the divide between demand and supply is as serious a problem today as it was in Drucker’s time. Despite all of our technological and managerial advances, most companies are still trying to play off of three different sheets of music — the financial plan, the marketing plan and the operations plan — with results that seldom end in three-part harmony. Our research suggests that most companies still do not know how to serve their most important customers in a way that maximizes the value to their customers and to themselves.

To understand more about how a few companies have managed to bridge this divide, we conducted interviews with managers and senior executives at eight different organizations who worked at different roles on either side of the gap between sales and production. We found that value requirements often vary significantly across customers or segments of choice, demanding cost efficiency in some cases and product and service differentiation in others. Unlike sales, which has learned to tailor its offerings to the customer, the operational side of the enterprise is often incapable of altering its service proposition. The upshot is that a company may have an excellent sales and marketing team and a top-flight operations team and still deliver the wrong benefits to a customer — cost efficiency to customers who want high levels of service, or service to customers who want a very basic product. Or a company may simply overlook opportunities with those customers who could make the most difference to the business.

**Toward Demand and Supply Integration**

Traditional attempts at coordinating demand and supply have generally focused on functional levels of the organization. The lower levels of the organization have been left to go through the motions of integration without the appropriate mindset, knowledge, motivation, incentives or structure to actually execute the plan. Our research suggests that companies that develop demand and supply integration have done far more than merely implement a single initiative. The successful ones tend to pass through five stages, each of which demands patience and perseverance:

**Stage 1. Develop a relevant value focus.** Senior leaders must cultivate a focus on creating value for the organization and for customers.
customers. Achieving this typically requires developing cross-functional structures and installing dashboard metrics that keep the business focused on implementing demand and supply integration.

Stage 2. Share knowledge across the organization. Managers must work on building inter-functional collaboration within the company, building external collaboration with supply chain partners and adopting technology that facilitates collaboration.

Stage 3. Allocate resources strategically. Once the entire organization shares the same set of facts, the company can then begin to make more thoughtful analysis of where and where not to allocate resources based on which customers deserve priority. Executives in sales and marketing can meet with the operations executives to make decisions about how to create and fulfill demand for customers of choice.

Stage 4. Learn to walk the talk. Executives at this stage make individuals accountable not just for their own unit’s performance but for the overall performance of the organization. They empower them to make decisions that maximize overall value and develop new education and training systems that encourage collaboration. Finally, they develop new incentive systems that encourage employees to stay focused on how to provide sustainable value to high-priority customers.

Stage 5. Balance capacity and demand. All of the work in stages 1 through 4 is just a prerequisite to the final goal: To make sure that the company’s most important customers’ needs can be satisfied profitably. This typically requires streamlining processes and then developing flexibility and fluid scheduling to meet variable demand.

Two Fortune 500 companies, now well on their way toward developing demand and supply integration, offer good examples of how this process works in practice.

Company A: Food Manufacturer Company A recently began to conduct joint business planning with its top customers. Managers now focus on balancing supply chain capacity with the demand being created. This change, generated by the highest leadership, is a significant cultural shift for the entire organization. The new joint business-planning processes are changing the way managers think about prioritizing and allocating resources. Both marketing/sales and operations.supply chain teams are involved in planning and subsequent resource allocation. They prioritize resources around key customers and jointly determine opportunities, balancing them with capacity constraints. This holistic approach to resource allocation allows the company to make better trade-off decisions. For example, an initiative that might not make sense from a purely functional perspective, such as the introduction of a new product to a particular grocery chain, may be approved by the team anyway, once it is understood to be part of the company’s strategic growth initiative with that customer.

Better planning is also allowing the company to improve its execution. More comprehensive information about key customer profitability enables managers to make short-term decisions to flex their operational capacity in a way that maximizes their margins. The joint business-planning process focuses on a 12- to 24-month time horizon, enhancing day-to-day execution capabilities and reducing the need for the reactive decision making that dominated previous operations.

A key factor facilitating this dialogue is a balanced scorecard methodology. A scorecard is a helpful method for translating an organization’s strategy into specific, quantifiable operational goals and metrics that span demand and supply activities in a way that ultimately improves financial performance. Managers say it has become such a regular part of their conversation that it now drives behavior at all levels of the organization and sparks far more cross-functional dialogue. As one manager told us, “We are living the balanced scorecard every day now.” Executives at Company A say the evolution is not yet complete, but given that the company’s financial results are now improving, it seems likely that the momentum toward even deeper integration will continue.

Company B: High-Tech Consumer Goods Historically, Company B chased market share to the exclusion of other goals and paid for that quest with high levels of obsolete inventory. A cultural change brought about by senior leaders has helped the company develop a more balanced approach.

Past forecast errors led to distrust between the demand and supply sides of the organization. Now, managers are working hard to develop a shared interpretation of knowledge across the organization, based on one master sales plan and one production plan. The supply side also had bad relationships with its suppliers, reflecting an earlier focus on price concessions that were needed to offset the cost of unsold inventory. To be fair, the company’s cost focus, exacerbated by the fast-paced nature of change in the industry, makes it challenging to build truly open, collaborative supplier relationships. However, the company is striving to make progress in this area and has a good

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put in place to facilitate information flow and create visibility across the organization and its partners.

Pursuit of relevant value requires making choices. Without an understanding of which customers matter most, every decision within a company becomes a territorial battle across the demand and supply divide. Strategic direction is required to better manage supply and meet demand. A deep understanding of which customers are the most important to the company helps managers make the best decisions about how to invest their time and money.

Excellence is not enough. Daily execution requires coordination between operations and demand-generating functions to deliver the required level of value to each customer on each transaction so that it generates economic profit. Flexibility and fluidity of process are required, fostered by internal alignment across operational activities. Rules, work arrangements and incentives may all need to be revised to keep everyone focused on the success of the partnership.

If an organization only makes incremental improvements, it should expect only incremental increases to its profits. More dramatic gains in profitability require a radical overhaul to high-level organizational thinking. Our research suggests that demand and supply integration offers one such pathway to creating a culture that recognizes that an organization cannot simultaneously be all things to all customers. Instead, demand and supply integration helps companies get ahead by enabling organizations to make tough decisions about how to allocate scarce resources to optimize creation of value — and for which customers.

Key Insights for Managers

Demand and supply integration is not a functional-level process or even a process that exclusively focuses on integration between functional processes. It’s an organization-wide orientation that spans functional domains and company politics to provide a basis on which to effectively and efficiently run an entire business enterprise. Building that capability takes time and effort. Leaders need to create the right organizational climate for demand and supply integration and establish goals and metrics that align functions to organizational goals that enable the entire organization to create relevant value for customers of choice.

Integrated knowledge is needed to guide demand and supply integration decisions. Organizations do not create value for themselves or their customers without closely collaborating across both internal functions and with their supply chain partners to share knowledge about customer value, supply chain capabilities and constraints. Arrangements made with partners become much more than simple buy-sell transactions and include joint coordination and planning, and, most importantly, a willingness to share both information and risk. Structures and processes need to be

HOW WELL DOES YOUR COMPANY INTEGRATE DEMAND AND SUPPLY?

To take a short questionnaire to help you assess the current stage of your company’s demand and supply integration, visit the online version of this article at http://sloanreview.mit.edu/x/56403 and see the “How Well Does Your Company Integrate Demand and Supply?” section of the article.

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