Introduction

McPherson’s Housewares is an Australian listed public company with annual worldwide sales of 120 million dollars. Major brands such as Wiltshire, Richardson Sheffield, Laser, Regent Sheffield and manufacturing plants in Hong Kong, Sheffield in the UK and Melbourne, McPherson’s is one of the world’s largest knife manufacturers for the consumer market. In Australia, McPherson’s business is broken up into seven distinct product groups that includes brand leadership in garden cutting tools, silver and stainless steel cutlery, the Australian icon, Wiltshire ‘Staysharp’ knife and other knife products, the equally well known barbecue product the ‘Bar-B-Mate’ and various scissors, silver plated hollowware and silver photo frames.

In 1994 we realized that while our business was growing we were unable to control inventory and always had too much of the products we couldn’t sell and not enough of the product we wanted. Our customer service was poor and McPherson’s was considered to be one of the worst suppliers in the industry. Our accountants kept telling anybody that wanted to listen that stock turns were terrible (less than two turns per year on our major product group) and we needed to fundamentally change the way we did business. I can remember a discussion with our accountant “You’ve go too many products, too much inventory”. The reply “Consumers need a range, cut my range and the sales will fall. Keep your nose in the figures and let me worry about the important things like getting the sales and growing the business”. Sound familiar doesn’t it.

Product and Rationalisation a Practical Guide

In May 1994 it was decided to change the way that McPherson’s did business. McPherson’s had the MRP software, but we lacked the knowledge to implement. We needed guidance and contacted Phil Heenan from Phil Heenan Consulting and after much discussion we agreed to implement MRP. Our first job was to rationalize the product range and with this decision came our first surprise. Our product range was almost double the size that we had estimated. Counting all the products in McPherson’s catalogues gave a figure of 1500 products that were being sold. As a double check we had our information systems manager write a simple program that listed sales by product for the last 12 months. The result, 2960 active products being sold. We then decided that we needed to put products into three groups.

A: These product groups were the top sellers and would generate approximately 80% of sales.
B: This group while not being the big sellers of the above group were steady sellers.
C: The products that were slow sellers.

This is how the product grouping came out:

<table>
<thead>
<tr>
<th>Product Group</th>
<th>Number of Products</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>244.0</td>
</tr>
<tr>
<td>B</td>
<td>417.0</td>
</tr>
<tr>
<td>C</td>
<td>2229.0</td>
</tr>
<tr>
<td>Total</td>
<td>2960.0</td>
</tr>
</tbody>
</table>

Clearly we had too many products in the ‘C’ grouping, but needed more data before we decided what to keep and what to drop.

We felt that additional information was:
1) % of sales by product group.
2) % of stock by product group.
3) % of gross profit by product group.

The following table shows the results.

<table>
<thead>
<tr>
<th>Product Group No. of S.K.U</th>
<th>Sales Value %</th>
<th>Stock %</th>
<th>Gross Profit %</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>80.0%</td>
<td>25%</td>
<td>82.0%</td>
</tr>
<tr>
<td>B</td>
<td>15.0%</td>
<td>25%</td>
<td>14.1%</td>
</tr>
<tr>
<td>C</td>
<td>5.0%</td>
<td>50%</td>
<td>3.9%</td>
</tr>
<tr>
<td>Total</td>
<td>100.0%</td>
<td>100.0%</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

We now had the framework from which to make an informed decision.
The easy part was deciding what products would stay. All the ‘A’ products stayed. If an entire product category was in the ‘C’ group it was dropped, but the products that caused the most problems were the marginal ones.

We developed a simple model that gave each product a designation. All products in the ‘A’ group were kept and forecasts were initiated under the MRP, these were given a ‘1’ grouping. These products had to achieve sales of $10,000 per annum at a gross margin at least equal to the overall average and have stock turns of better that two per annum.

The second group, the ‘2’ grouping, were products that were going to be deleted, but we had plenty of stock that we believed could be sold at acceptable margin without dramatically affecting profit.

The third group, the ‘3’, were hopeless sellers that were low margin, with stock turns of less than one. In fact we found that in certain product groups such as stainless steel accessories (oyster forks, ice-cream spoons etc.) we were getting stock turns of one every three years. In this group we felt that we would be lucky to get a quarter of our costs and we had well over a million dollars worth of stock.

Once the decisions were made, our first hurdle was to convince the sales force that we could no longer afford to have such a large product offering. Generally speaking, they were supportive of the concept, but if there was a product they felt was absolutely necessary to be included we left it in. We added only 36 products. We did the same with some major customers and added another 15 products. Interestingly most retailers are now measured by stock turn and margin and don’t want to sell products that are slow moving. In this respect our goals were one and the same. Products that offer good margin, good sales and high stock turns.

Twelve Months Later 30/6/95

The greatest benefit of product rationalisation at McPherson’s was that our customer service rates had risen by 10 points. We define customer service as, the filling of any order on time and in full. Therefore an order for 70 items has a customer service level of 100% if all 70 items are filled and delivered on time. While our customer service levels were still not up to our goal of 95% we had at last began to make positive progress.

Our product range of active S.K.U.’s had been reduced to 1900, a fall of almost 1000 from the preceding 12 months. We now had product in stock that we could sell due to forecasting and also had the money to spend on good stock rather than being tied up in slow moving product.

We reduced our stock by almost $800,000 which made our accounts happy and also improved our cash position. And finally we improved our profits substantially. This was not entirely due to product rationalisation and MRP, but the discipline it had introduced to McPherson’s helped to show the managers how to run a more efficient and profitable business.

Another 12 Months 30/6/96

McPherson’s is now well on the way to have the following product line:

<table>
<thead>
<tr>
<th>Product Group</th>
<th>No. of S.K.U. 30/6/96</th>
<th>Compared to No. of S.K.U. 30/6/94</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>202.00 244.00</td>
<td></td>
</tr>
<tr>
<td>B</td>
<td>259.00 417.00</td>
<td></td>
</tr>
<tr>
<td>C</td>
<td>405.00 2229.00</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>866.00 2960.00</td>
<td></td>
</tr>
</tbody>
</table>

For the first time our customer service passed 90% in January 1996. In two years we have gone from being one of the worst suppliers in the industry to one of the better ones. Not the best, but we will be in the near future.

We now run the business with almost 20% less inventory than we did in 1994. We have continued to improve our profit in a difficult segment of the market. Product rationalization has contributed to profit growth. Our warehouse, which was felt to be too small in 1994, now has sufficient room.

The Pitfalls

Product rationalisation has not been an easy path to follow. Our experience at McPherson’s highlighted four areas that caused our company plenty of heartaches.

Stock

Once we identified what was slow moving and how much we actually had, we were faced with how to sell it profitably. The responsibility for selling the stock must be given to the most senior sales person in the company or delegated to a person whose sole function is to sell the stock. We found that the first million dollars worth of stock was sold easily. The second million proved...
to be the challenge. We would recommend that the sales force develop a plan on how they intend to sell the product and report each month on their success, against a pre-determined budget. Financial guidelines on what is an acceptable margin needs to be made clear at the beginning and as long as the sales force works within these guidelines they should be left to sell.

**Commitment**

This is a motherhood statement, but product rationalization will only work if the senior management is totally committed. Their job is to sell the benefits to all staff so that everybody understands how much better the company will be.

**Saying No**

We found that with both customers and our own people, we often were forced to say no when a customer wanted McPherson's to add a new teaspoon for instance, to the range, because they felt it was required. The discipline of MRP had shown McPherson's that we knew we couldn't make money (or sales) from such requests and that often meant having to tell our customers “Sorry, but NO!”

**Stopping it Happening Again**

This was our greatest trap in many ways. The temptation to begin to add other products and lines to compensate for the reduction, or to want to go back to our previous ways. To stop this happening we instituted a new product justification form. The form was filled out by the relevant product/sales manager and covered such issues as projected sales, margin, stock turns, level of competition, strategic importance etc. Each item was then given a score of 1 to 10, 10 being most important and one being of little importance. The product/sales manager was then required to rate on a 1 to 10 scale, each item on the list and to justify the score. The two sets of figures were then multiplied to give a total score. If the figure was less than 450, in McPherson's case, the product proposal was taken no further. If the score was acceptable, then the information was passed to the financial controller who would establish its profitability.

This had two positive effects. It made the product and sales people do their homework before proposing new products and it made the sales managers understand that they were responsible for getting the sales they forecast in the original proposal. This system has been instituted on 8 product launches and with the exception of 1 product group the objectives have been met. Product rationalisation has also taught McPherson's to recognize a product launch that is unsatisfactory and to quit the stock quickly.

**Product Rationalisation – Conclusion**

Product rationalisation has been a long and often difficult road for McPherson’s. Almost two years since we decided to implement a program of product rationalisation, we have improved customer service, we operate with 20% less stock, our profits have continued to improve in a difficult market and we have reduced our product offering by almost 60%.

It has introduced a discipline approach to new product launches and in many ways has improved the working environment for the employees of the company. Product rationalisation is a journey that for McPherson’s has been worth the time and effort. We hope this paper may stimulate you to make a similar journey.

**Customer Rationalisation.**

Once McPherson’s has established the framework for product rationalization it was clear that we needed to also review our customer numbers. As a result of a study done by the Boston Consulting Group on the world wide operations of McPherson’s, one of the recommendations was to rationalise the number of customers in each country.

We began by ranking our customers from biggest down to smallest. The results were in line with expectations, with the top 30 customers generating 83.5% of turnover. What we did not expect was the large amount of small customers that generated little of no turnover at all. In fact 48.1% of our accounts generated only 7% of turnover.

We needed to decide how to handle these accounts. As we had not enforced a policy of minimum order values and we supplied free into store anywhere in Australia, our costs on smaller accounts were rising without a corresponding rise in sales.

We established through our financial controller, that we needed a minimum order of $150 to achieve breakeven. Orders under $50 cost more to process than the actual order value. Our first step was to inform customers that we would no longer accept orders of $50 or less, and
that orders from $50 to $150 would incur a surcharge of $10. Despite some initial reservations our customers accepted this as part of normal business practice.

Again working with our accountants, we also established at what level a customer becomes profitable. This proved to be difficult, as a customer that orders once a year with delivery to one point worth $5000 was profitable, while larger accounts with sales of $8000 who ordered every month to four different delivery points was clearly unprofitable.

We identified approximately 200 accounts that were unprofitable, compiled a list and sent out to each of our State managers for review. We removed 10 customers from the list. In most cases these were new accounts or the managers felt they had potential for the future. In July, our General Manager wrote to each account informing them their account would be closed and if they were unhappy with the decision to contact the general manager personally. We took another 4 accounts off the list based on feedback. In August we closed 186 accounts.

Our experience with the closing of accounts is that while these accounts are unprofitable they do generate sales volume and unless overheads are trimmed the exercise can be wasted. We recognised that once these accounts were closed we would have to reduce staff in customer service, debtors and warehousing. We also implemented different service strategies based on customer profitability. Key account management was introduced with a new staff member hired to look after three of our larger accounts. We believed (although it is yet to translate into additional sales) that improved interface between these customers and McPherson's will ultimately result in improved profitability.

**Conclusion**

Based on McPherson's experience, once the process of rationalisation has been agreed to, a plan of action is needed with dates on which various tasks must be performed. The key to its success is detailed financial analysis. Agreement for the sales force on which customers stay and which ones go and at the same time a reduction in overheads to cover lost sales.

**About the Author**

David Smith is the national Manager, sales and Marketing, at McPherson's Housewares a leading housewares supplier to the retail market. Before joining McPherson's in April 1994 he was the National Marketing Manager for the general products division of BTR Nylex. His responsibilities included a range of consumer garden watering products, industrial fluid transfer, civil engineering and noise control products. He joined BTR Nylex in 1988 after a seven year tenure with Hallmark Cards as advertising and public relations manager. He remains a recent, but committed convert to MRP II and product and customer rationalisation.