Coffee Production: How Too Many SKUs Can Drag Down Profits

Gerry Gomolka, VP Business Development, Stellar

The coffee industry has exploded in recent years as consumer and retailer tastes and brand preferences have led to a plethora of products. Retailers and food service operators want a competitive edge by offering their customers unique blends, roasts, and grinds in private-labeled packaging. This puts the pressure on coffee producers to meet those demands by turning out a wide range of products.

One customer wants a special blend in a light roast with a medium grind. Another customer wants a different blend in a dark roast with a fine grind. You can do the math and see the exponential impact of the options. Every variation creates a unique SKU for the coffee producer. For example, you produce an identical product (same blend, roast and grind) for two customers, yet one requests reducing the package size from 2.5 ounces to 2 ounces for a more economical price point. You have the same product but two different SKUs due to package size.

As a result, coffee producers often find themselves saddled with too many products, all in an effort to appease customers. Too many SKUs can drag down profits with frequent changeovers that drive up production costs and decrease throughput.

Strategic planning is especially critical for coffee producers to avoid this proliferation of SKUs. While you may not be able to anticipate all of your customers’ unique needs, your strategic plan can establish guidelines and processes to help you manage these requests as it relates to your product mix. Here are the key issues to address to ensure that you can meet your customers' needs while maintaining your plant's profit margin.

The impact on sales

Ensure that your business plan addresses the balance of sales and production. Will your plant produce to inventory or produce to client preference? Detail the process for adding additional SKUs to your product mix. Can a sales representative create a new SKU, or a temporary one, to meet a customer's special request? Does your sales force understand the production process and the impact of adding new SKUs? Walk them through your manufacturing operation and explain how a simple variation, such as a change in roast, affects the entire production process and product cost. How are your sales representatives compensated? Consider factoring each SKU's profit margin, including start-up costs, into your compensation package.

Manufacturing analysis

Conduct an asset optimization study. Assess how your plant's assets are being utilized, or underutilized, based on each SKU. Periodically, review each SKU and analyze them for asset utilization, production cost, market demand, and profit margin. Is there an opportunity to combine two similar SKUs while satisfying customer demands? Can you eliminate a SKU by offering customer incentives to accept a coffee that you're producing in larger quantities? The cost of the incentives may justify substituting a higher quality product versus shutting down production to accommodate a changeover for a smaller run. Determine your most/least profitable SKUs and set a threshold for eliminating those that may be dragging down profits.

Production scheduling

Incorporate production scheduling into your plan and review it frequently. Can you process extra runs of the same blend to save time and money? Consider putting freezes on your production schedule for one or two days out to avoid any last-minute customer requests that throw the entire process into disarray. Customer management by sales and marketing is key.

Reduce changeovers

Fewer SKUs mean fewer changeovers. Can you substitute your most popular blend to eliminate a changeover? Meeting a multitude of packaging needs often leads to frequent changeovers, especially with newer packaging options such as single-serve or tray packs. Consider case size consolidation, on line printing and label application.

Consumer and retailer demand for specialty coffee products will continue to increase. Maintaining your company's strategic integrity and profits, while continuing to meet customers' needs, requires a balance in sales and production.