

# **The Secret of Soared Profitability: Salesforce is More Than Cost-Cutting-the Case Study of KHC**

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**Keywords:** Profitability; Sales force; Packaged food industry

**Abstract:** This paper sets the focus on finding the fatal point of leading the packaged food manufactured company successful by the case study of KHC. We find that during 2015-2017, packaged food industry indeed endured the declination and then grow up again because of the healthier living style. So the ratification of the customers is the most important factor. To different scale companies, they almost have the same gross profit, but the operating profit always are different. KHC also has its own reason that is the 3G capital entered into its company. Which made it more profitability. But this kind of profitability is unstable.

## **1. Introduction**

By Brian Baskin and Annie Gasparro, Feb. 12, 2018 reported that over the past 2½ years, thousands of workers lost their jobs, and iconic Kraft buildings, including the original Oscar Mayer headquarters in Madison, Wis., have been shuttered and sold. The cost-cutting project is now wrapping up, giving Kraft Heinz Co. the highest operating profit margin among its peers in the U.S. food industry. Whereas Kraft Heinz shares hit a two-year low last week, and are down 21% over the past year, a period when the S&P 500 index rose 13%. Is this KHC lack of competitive advantage? Or is it just the reason of the whole packaged food industry. And how to gain the successive performance? Such questions are the main purposes of this paper. The following parts of this paper is arranged by : Firstly from the outside environment view, using “Pestel” model ,taking the analysis of the packaged food industry ;Secondly into the corporation inside to find out what’s the reason of the profitability. Thirdly make some conclusions.

## **2. Challenges of the Packaged Food Industry**

Food is the basic need of living creature. But now more and more meanings have been given onto the food. One trend is that food, together with cooking food, has turned into being enjoyable and fun in some countries. So probably they consume much more time on preparing food and cooking food. The other trend is that adapting to the fast pace of developing and technology, easy take-out and fast cook food is more popular. Packaged food industry has gained highly grown. As some specialists and institutions predict that the global packaged food market is expected to grow at a moderate pace, its market size maybe up to \$3.03 trillion by 2020, its CAGR will be 4.5% during the period of 2015-2020. Packaged food industry includes a wide range of food products such as ready meals, baked goods, breakfast cereals, soups, baby food, potato chips, nuts, instant noodles, pasta, biscuits, chocolate confectionery, cheese, yogurt, ice cream, sauces, dressings, condiments and non-alcoholic drinks. So the first and second detail market share is baked food, non-alcoholic drinks. They are capturing the ¾ total market by value. And then is the Chocolate confectionery and cheese. Now currently, yogurt and baby food has grown faster. Geographically, world packaged food market is dominated by the North American region, followed by Europe. The market is growing substantially in Northern Europe, whereas the adoption rate lags in Southern Europe[1]. (from the allied market

research).

From the above structure, we can see a lot of factors may have influences on this industry, both positive and negative. In this paper we will more concentrate on the threats to this industry. First and the most important is the fast changing living style and social behavior. They have totally changed our daily life. More and more consumers are eager to have healthier food instead of processed packaged food. Bake or fresh food, drinks and so on, all those reasons make the whole packaged food market share be challenged. Second, but yet very important, the rapid progress of technology will take much effect on the whole industry. The packaging method and its material are the fatal point to its price, quality, and satisfactory of customers. So the new technological processes will add more value to supply chain. Third are the ecology awareness cause customers to choose less harmful material to pack food.

These three main factors from the customers and society will lead the corporations to change their strategy on producing and selling the products. Now we can see form the following Table1, the top 9 market value above 1000million's US dollars listed company, total revenue has declined 2.16% between 2016-2017. Eight listed companies' experiences declination more or less. Except one company gains the growth. Another issue we can see is that higher revenue is not always with the higher market capitalization. Market capitalization is more related to the growth trend and rate.

So we can tell even if the whole packaged food industry confronts declination. To the specific company it can gain its own performance from its customers. Customers is the key factors of performance.

Table 1 A List of Nine Competitor Companies's Revenue and Growth

	<b>Name of Company</b>	<b>Market Capitalization</b>	<b>2017Total Rrevenue</b>	<b>2016Total Revenue</b>	<b>Growth(%)</b>
1	The Kraft Heinz Company KHC: NASDAQ-GS	70,117,679.00	26,232,000.00	26,487,000.00	-0.96%
2	Mondelez International, Inc. MDLZ: NASDAQ-GS	58,719,709.00	25,896,000.00	25,923,000.00	-0.10%
3	Archer-Daniels-Midland Company ADM: NYSE	24,878,096.00	60,828,000.00	62,346,000.00	-2.43%
4	General Mills, Inc. GIS: NYSE	24,249,032.00	15,619,800.00	16,563,100.00	-5.70%
5	Kellogg Company K: NYSE	22,496,561.00	12,923,000.00	13,014,000.00	-0.70%
6	ConAgra Brands, Inc. CAG: NYSE	14,678,296.00	7,826,900.00	8,664,100.00	-9.66%
7	McCormick & Company, Incorporated MKC: NYSE	12,540,869.00	4,834,100.00	4,411,500.00	9.58%
8	J.M. Smucker Company (The)SJM: NYSE	12,451,586.00	7,392,300.00	7,811,200.00	-5.36%
9	Campbell Soup Company CPB: NYSE	10,362,854.00	7,890,000.00	7,961,000.00	-0.89%
	total	250,494,682.00	169,442,100.00	173,180,900.00	-2.16%

All the sources comes from Nasdaq and Yahoo finance. All numbers in 000' us dollars. According to the different accounting period, these total revenues in 2017 and 2016 aren't the same , The Kraft Heinz Company, Archer-Daniels-Midland Company, Kellogg Company are with the calendar year, others are not. Due to purpose of showing the trend ,this paper doesn't distinguish and make adjustment.

### 3. Analysis of KHC's Competitive Edges

Kraft Heinz is one of the largest food and beverage companies in the world, with its sales around approximately 190 countries and territories. It produces a legions of different types of food and beverage products, including condiments and sauces, cheese and dairy, meals, meats, refreshment beverages, coffee, and other grocery products. All over the world we can see the images of KHC with a host of iconic brands including Heinz, Kraft, Oscar Mayer, Philadelphia, Velveeta, Lunchables , Planters, Maxwell House , Capri Sun, Ore-Ida, Kool-Aid, Jell-O ,which are taken as a globally recognized producer of delicious foods available for all occasions whether at home, in restaurants or on the go. As of December 30, 2017, it had assets of \$120.2 billion US dollars.

As the main leader of packaged food industry producers, KHC has the competitive advantages. As the Table2 shows that KHS' revenue, operation income ratio and return of sale information. We can find that gross profit ratio and operating income ratios are stable and high between 2016-2017. What's more these two years' ratios are higher than 2015's.It can testify that KHC does some measures on the cost control and gain good effects both on the products and administrations. But one surprisingly phenomenon is the abnormal of ROS ratio .Which is abruptly higher than former two years .It won't be the operation effects but related to some investment activities. Yet we may say this kind of profit may not be stable. The real sustainable competitive edges to the packaged food industry manufactures should come from the whole supply chain activities values. Which means that sales force are the fatal point. By using new technology and give more customs' satisfaction will lead to the success.

Table 2 A List of KHC'Performance Records

The Kraft Heinz	Year of 2017	Year of 2016	Year of 2015
Total Revenue	26,232,000	26,487,000	18,338,000
Cost of Revenue	16,529,000	16,901,000	12,577,000
Gross Profit	9,703,000	9,586,000	5,761,000
Gross Profit ratio	36.99%	36.19%	31.42%
Selling General and	2,930,000	3,444,000	3,122,000
Operating Income	6,773,000	6,142,000	2,639,000
Operating Income ratio	25.82%	23.19%	14.39%
Net Income	10,999,000	3,632,000	634,000
ROS	41.93%	13.71%	3.46%

All the sources comes from Nasdaq and Yahoo finance.All numbers in 000' us dollars

For we can see from table 3, 4, the two smaller size companies, they can also gain the gross profit as KHC. And even little higher than the big one. But as to the operating ratios small companies are lower. Scale can gain advantages! And the scale is related to the sales force.

Table 3 A List of Campbell Soup Company'Performance Records

Campbell Soup	Year of 2017	Year of 2016	Year of 2015
Total Revenue	7,890,000	7,961,000	8,082,000
Cost of Revenue	4,831,000	5,181,000	5,300,000
Gross Profit	3,059,000	2,780,000	2,782,000
gross Profit ratio	38.77%	34.92%	34.42%
Selling General and Administrative	1,543,000	1,665,000	1,509,000
Operating Income	1,400,000	960,000	1,054,000
Operating Income	17.74%	12.06%	13.04%
Net Income	887,000	563,000	666,000
ROS	11.24%	7.07%	8.24%

Table 4 A List of J.M.Smucker Company'Performance Records

J.M. Smucker	Year of 2017	Year of 2016	Year of 2015
Total Revenue	7,392,300	7,811,200	5,692,700
Cost of Revenue	4,557,000	4,843,400	3,724,000
Gross Profit	2,835,300	2,967,800	1,968,700
gross Profit ratio	38.35%	37.99%	34.58%
Selling General and Administrative	1,463,300	1,614,100	1,085,800
Operating Income	1,031,500	1,145,300	772,000
Operating Income ratio	13.95%	14.66%	13.56%
Net Income	592,300	688,700	344,900
ROS	8.01%	8.82%	6.06%

Furthermore we can see more detail sale information to find the competitive edges about the KHC. Table 5, 6 are the product structure and sales location information. From 2015-2017, KHC indeed endures the little down of its sale as a whole. Condiments and sauces decrease, frozen and chilled meal decreased more than another types. Cheese and dairy, Meat and seafood, on the contrary, are growing fast. It may be reason of the healthier living style. So we can tell customers are the most important things. Producers should make changes according to its customers. Only by doing so, it can lead going on success.

Table 5 Sales Product Structure of KHC

types	Year of 2017	Year of 2016	Year of 2015
Condiments and sauces	25%	24%	32%
Cheese and dairy	21%	21%	15%
Ambient meals	9%	9%	10%
Frozen and chilled meals	10%	10%	12%
Meats and seafood	10%	10%	8%
total	75%	74%	77%

From table 6 are sale location information. We know that North America and Europe are still the main places which picked KHC. But it also means that for KHC there are lots of opportunities to enlarge its sales. Especially by the changes of habit, most of Asian young generations do more like western style.

Table 6 Sales Location of KHC

Place	Year of 2017	Year of 2016	Year of 2015
United States	18,353	18,641	10,943
Canada	2,190	2,309	1,437
Europe	2,393	2,366	2,656
Rest of World	3,296	3,171	3,302
Total net sales	26,232	26,487	18,338

Combined with the detail information we can figure out that its successful strategy and its core competency, which are supply chain and financial management give prosperous to the company.

#### 4. Further Discussion of KHC's 3G Capital Activities

Beside its operation activities we can also find some competitive edges after 3G Capital gains the ownership and controlled KHC. They set up a lot of steps. Cost-Cutting usually aligned with the supply chain, they have set up a new plant with high technology, sanitary standard, more effective and more efficiency, well inventory management, and all the outcome we can see that the high operation income.

Another core competency is maybe the high level of financial management .as table2 shows KHC operation income is 6,773million and net income is 10,999million, even more higher than operation income. The reason is that in this fiscal year KHC has the tax expense of negative5,460million. It maybe the management make the good financial arrangement. To the highly mature industry, the cash flow is most important thing, how to save tax legally, and match with the company's decision, it shows the great financial competency.

According to this competency it probably the power of 3G capital and give the new resource. Now several managers come from the 3G capital. As the investment company, they are familiar with financial regulation and rules, how to use capital efficiency and gain high investment return. They are famous for their acquisition and cost-cutting. And what's more as the new comers, they can take a lot of things to change the big and old company. Set up new disciplines.

## 5. Summary

All in all, to the highly mature and competitive packaged food industry, a lot of challenge and difficulties may confront, the efficient strategy is keeping cautious to important changes, and make suitable strategy in time, combined with its core competency and resources, whatever tangible and intangible, synergy into a whole body to gain sustain competitive advantages.

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