Logistics Association of Australia Ltd

LAVAZZA- LESSONS FROM A COFFEE MAKER

The following is the third in a series of articles from Amelia Chan, winner of the Logisitcs Development Award 2000 sponsored by CHEP Australia and supported by Morgan & Banks.

In Italy, Lavazza is Italy's undisputed number one coffee. In Australia, Lavazza is now market leader in Victoria - an amazing achievement particularly since Lavazza sells at a premium to the well-known brands Nescafe and Harris/Moccona. Its leading market position in Victoria is largely due to the strength of its Australian distributor, Valcorp.

The Lavazza factory in Turin produces all the sales requirements for the Italian and overseas markets, representing 350 tonnes per day of roasted coffee. 300 SKUs covering 50 products are produced. Storage capacity is 11,000 pallets of finished product. Lavazza utilizes an extremely high degree of process automation in both production and distribution, enabling staff to number only 360.

Lavazza's supply chain – upstream

Lavazza is justifiably proud of its supply chain which it has simplified through good procurement practice and completely automating the production process.

- Procurement of raw material
As Lavazza sources its coffee beans from geographically dispersed farmers in South America, Africa and Asia, there is a constant supply of raw material throughout the year to match customer demand which is not subject to seasonality.

- Receiving of raw material
This appears to be the only part of the upstream supply chain requiring improvement. Currently, 60kg bags of beans arrive by ship, are transferred onto small trucks and transported directly to the Turin factory where they are unloaded by hand - the sole manual process in production and distribution.

Although the unsophisticated nature of operations of the bean-producing countries may present difficulties, I believe that Lavazza should implement bulk delivery. This would result in savings in transport costs and would

facilitate automatic receiving. Firstly, however, the tight unloading dock at Lavazza would need to be extended.

- Production
To ensure the removal of foreign substances from the raw coffee, the beans enter stone shifting machines. They then pass through optical sorting machines which eliminate beans of the wrong colour. Subsequently, the beans are roasted and ground into coffee. Packaging lines produce 120 packets per minute. Palletising machines handle 600 pallets per day. Through all of the above stages in production, conveyors transport both beans and the packaged coffee. I found the production process quite slick and seamless.

Lavazza's supply chain – downstream

Lavazza has two streams of business: the retail supermarkets and food service.

Retail
Retail represents 80% of Lavazza's business. A company could not wish for a better distribution operation. A roll-on/roll-off fills full-pallet trucks for retail DCs. The retailers give Lavazza green light preferences at their DCs accepting pallets 24 hrs/day.

Food Service
Food Service comprises the remaining 20% of Lavazza's sales. It is the complexity of these customers that provides the complication in Lavazza's supply chain. Lavazza is making good progress in dealing with this just as it has done in streamlining its upstream supply chain and retail business.

- The challenge of route customers
Until recently, milk bar customers could place an order at any time and the Lavazza-employed drivers would fulfill the order. The drivers tended to do the same route each time and developed a customer service relationship with the customers.

A year ago, the route distribution was contracted to TNT. The logistics disciplines which TNT brought into the relationship has caused interesting changes in Lavazza's own relationship with its customers. Firstly, TNT sent different drivers to do the customers rate each time, making it difficult for customers to develop any form of sales relationship with the driver. Secondly TNT paid its drivers by consignment, reducing the incentive for the driver to spend time with the customer. Thirdly TNT works to strict order time cut-offs and this drove Lavazza to train its route customers in ordering disciplines. Another logistics efficiency of TNT's is eliminating intermediate warehouses.

- The challenge of bringing on a third party
Lavazza and TNT are addressing issues which result when separate companies come together. I believe a service level agreement quite separate from the formal contract which already exists between TNT and Lavazza. would clarify the responsibilities of each party - e.g. who has accountability for logging customer service issues in the food service business?

Another challenge is in the information systems area where one party may be more technologically advanced. TNT's vision is to electronically transact with its customers. Currently it is working with Lavazza to develop a systems interface.

Interesting learning's for Australia

Service level agreements are essential for major relationships

In Australia, it is quite common for a manufacturer to contract out a major portion of its logistics business e.g. Meadow Lea contracts Frigmobile for its NSW and national-based distribution. Goodman Fielder Milling contracts Linfox for its NSW warehousing. Kellogg contracts Maynes for its cereal distribution.

I believe it is essential to work through a service level agreement between the two parties who will most likely have cultural differences and different business objectives. Service level agreements specify the commitments and benefits of each party and minimise misunderstandings which may arise from undefined responsibilities. Additionally, they provide an effective tool for the regular monitoring of the relationship.

Forming Associations is not so text book

The drivers for Lavazza's retail business were formerly employed by Lavazza, but since being employed by an "association", are now off Lavazza's books. A separate entity was created by Lavazza to achieve lower costs, minimise trade union disputes, and to increase flexibility and productivity.

In the European labour environment many companies are transferring their employees to an association. Wage levels in Europe are high and artificially boosted by government policy. For example, to increase the number of people employed, the French government stipulates that an employee must work no more than 35 hrs/week, otherwise heavy penalties are incurred.

I visited two other firms in Northern Italy where associations were a success. TNT Spare Parts formed an association which enabled FIAT to sell off its employees; indeed the association was a condition for winning the FIAT spare parts tender .Benckiser the detergents company which merged with Reckitt & Colman, operates its warehouse with an association.

At the warehouse, productivity was high and the relationship between association-employed operators and the Benckiser employed logistics management and load planners schedulers, was strong. Examples of associations are more difficult to find in Australia. However, this arrangement is working successfully in a production environment at Kellogg following the recent acquisition of The Healthy Snack People. In the bakery department which is under the association, trade union disputes are fewer, productivity is high and worker morale is good.

The ACTU is pushing for limited working hours with two major test cases to push for a new overtime and hours clause into Federal awards. Whilst it maintains that wages will not increase greatly, it would seem that limiting hours per employee will result in employers incurring increases in training, work cover, and other such overheads as additional staff are employed.

Logistics practices are largely influenced by the regulatory environment. As Australian regulatory trends follow those of Europe, we can learn a lot from the European experience.

If *you would like* to discuss *any of the issues in this* paper, please feel free *to* contact her on ameliachan @Kellog.com