

# Report: RFID Benefits Not Equal

A.T. Kearney says RFID will bring great benefits to Wal-Mart and other retailers, but manufacturers will bear most of the costs and see little return.

Nov. 14, 2003—A new report released by A.T. Kearney, a management consulting firm owned by EDS, says retailers will generate significant savings in inventory and labor costs by adopting RFID technology. But the report stresses that manufacturers will have to spend a lot of money up front on tags and will see few benefits in the short term.

The analysis comes out of work A.T. Kearney is doing with several consumer packaged goods manufacturers, according to Dave Donnan, an A.T. Kearney vice president who conducted the analysis. “The business cases we were working on were all coming out the same way—fairly negative,” he says. “We talked to other CPG manufacturers working with other firms and the same thing was coming out. [The CPG manufacturers] said someone’s got to report this out.”

A.T. Kearney’s analysis suggests that retailers will see benefits in three primary areas:

- Reduced inventory through a one-time cash savings estimated at 5 percent of total inventory
- An annual benefit from a reduction in store and warehouse labor expenses of 7.5 percent
- A reduction in out-of-stock items resulting in a recurring annual benefit of \$700,000 per \$1 billion in annual sales for retailers who reengineer their current shelf fulfillment processes.

The consulting firm estimates that large regional and national retailers will have to spend an estimated \$400,000 per distribution center and \$100,000 per store, and an additional \$35 to \$40 million needed for systems integration across the entire organization.

Manufacturers face similar one-time costs up front for outfitting their distribution centers. But they also get hit with the recurring charge of placing RFID tags on their pallets and cases, as mandated by Wal-Mart and the U.S. Department of Defense. The costs vary by type of manufacturer, according to Donnan.

High-impact manufacturers that sell lower volumes of expensive products and experience significant out-of-stocks and shrinkage—typically drug and general merchandise manufacturers—will not be as hit hard as low-impact manufacturers that sell high volumes of less expensive goods and experience limited shrinkage (food and grocery manufacturers).

The report compares two manufacturers with \$5 billion in sales—a low-impact grocery manufacturer and a high-impact over-the-counter drug manufacturer. It says that if tags cost 15 cents each, the grocery manufacturer will have to shell out \$33 million per year for 221 million tags for its pallets and cases. The drug manufacturer will have to spend only \$2.2 million per year to tag its pallets and cases. The grocery manufacturer will have a hard time making up the added cost through efficiencies created by RFID.

“A reasonably efficient CPG manufacturer already has a warehouse management system, is doing case bar coding and probably has labor [best practices] in all their warehouse operations,” says Donnan. “So the incremental benefit for using RFID internally is rather small. The benefits of reducing out-of-stocks and having better availability is definitely an opportunity. However, that depends on how well they negotiate with

the retailer, because their savings depends on the retailer taking action and changing their business process and there is no guarantee of that.”

There could be some savings from automating shipping and receiving, which could reduce chargebacks from retailers. But Donnan says companies need to synchronize data with retailers, through UCCnet, before they can get these benefits.

“Less than 1 percent of [Global Trade Item Numbers (GTINs)] have now been synchronized,” he says. “We’re talking about a major ramp up just to get all the data issues resolved. With RFID you’ll get fast collection of data, but you’ll have a high level of inaccuracies because the GTIN’s don’t match between the retailer and the manufacturer. You’ll have more errors and cost than you have today. If you don’t have data synchronization, RFID is a wasted effort.”

A.T. Kearney is advising grocery manufacturers and other low-impact manufacturers to closely examine the rationale behind the EPC and RFID tagging and to consider alternative courses to meeting the mandate, such as using bar codes that have EPCs. Those that don’t have to meet a specific mandate could delay implementation until the per-tag cost drops to a reasonable level for the company's business case.

“RFID is a great opportunity,” says Donnan. “But we’re just running so fast that people are expecting it to be implemented in the next two years. But it’s going to be a five- to seven-year journey.”

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