Distribution Center MANAGEMENT
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From the Golden Zone

How to apply lean thinking in supplier relationships

By Howard Coleman

If you want to reduce waste (all non-value-added activities and inventory), the best starting point is to recognize that only a fraction of the total time and effort in an organization adds value for internal and external customers.

Eliminating non-value-added activities and inventory provide the greatest potential sources of improvement in a distribution center.

The following areas of non-value are typical of those hindering improvement:

- Too much inventory — more than necessary to fill a reasonable day's supply of customer demand.
- The use of outdated economic order quantities that pushes inventory into the DC.
- Product waiting around for movement.
- Over-processing — or over-checking.
- Poor inventory control — finding product becomes a treasure hunt.
- Errors in receiving, put-away, picking, and shipping. Mistakes cost money.
- Unused employee creativity — a waste of human resources.

It's time to rethink inventory

Frequent reordering of product from a vendor might seem antithetical to those who have spent their careers trying to reduce transportation costs or take advantage of a vendor's prepaid shipment terms. It's a fact that more frequent ordering of product reduces the average inventory on hand and the associated annual carrying costs (typically estimated at 25 percent to 36 percent).

No, I am not suggesting that you ask your vendors to provide "daily milk runs," and I recognize that most vendors are not located around the corner.

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But is it necessary to have two or three months supply of a product on hand when we can have it delivered in one or two weeks — or less? Lean thinking suggests we put in place a process that works toward a "sell one — buy one" result (assuming some safety stock for variations in demand). That is called "pull."

Now, we may never actually reach the promised land (we won't buy one egg instead of a dozen), but we can have a dramatic impact on what we need to stock to satisfy customer demand by ordering to actual demand and fostering a continuous flow of product.

To meet prepaid minimums, I see buyers ordering multiples of what is really needed.

Even worse, I've seen safety stock and lead-time parameters raised just to generate sufficient purchases to meet prepaid order minimums —

again "pushing" inventory.

Many of the enterprise software solutions also over-emphasize the use of economic order quantities. It results in a large batch of inventory being pushed into the warehouse, which at least 50 percent of the time is more than what is needed to satisfy customer demand before the next inventory replenishment.

I've often questioned vendor special deals which involve accepting (again "pushing") large quantities of product into inventory to obtain a discount or meet some purchasing objective. Often this occurs at year-end, maybe even just before a physical inventory.

This can devastate inventory investment and create the potential for obsolescence. Often, the immediate issue becomes, "Where do I put it all? My primary stocking location won't hold it!"

"It's an 'A-item' and I have to store it in the back of the DC or high up on pallet racking. And I'll have to move it again later, otherwise we'll lose picking productivity!"

Of course, there is also the issue of the cost of storing this material, lost productivity, possibly overtime, and the missed benefits of a smooth and continuous flow operation that lets product move through the DC faster.

Take a total-cost view

A client recently said to me: "I want to leverage my volume with my vendors, but I'm also looking for a continuous flow of product based on what I am actually selling (pull vs. push). If I could just get my suppliers to accommodate, I know my inventory would go down, and I believe service would not be negatively impacted. I'm committed to service and flexibility; my suppliers have to be also."

My client never said the exact words, but what he was effectively saying was, "I want to take a total-cost view." His objective was to reduce total costs, including inventory costs, rather than any one cost element, such as transportation.

Asking the right questions is a simple but effective approach to find the ways lean thinking can address these issues of inventory, cost reduction, profitability, and customer service. To suppliers, the downside seems weighty, and convincing them is no small task, because so much has been invested in the "way we do things."

A good starting point is to gain a common understanding of the mutual supply chain and distribution challenges between buyer and seller and see the perspectives and issues from all sides.

A lean transformation will begin when the assumptions built into the organizations and business processes are challenged. Confidence to take additional steps will come with the growing sense that collaboration is driving some change and mutual advantage.

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