

Extracting Profitability Between the Squeeze

Author: Rocco Petrilli, President/CEO, PRIMA Business Specialists LLC

ABSTRACT

Raw material pricing increases at a record rate while revenues decrease by double digits. Other health care and supply costs follow. Fuel surcharges arrive quickly and are slow to depart. Reduction in product demand and historic lows and credit restrictions make investment for vital cost reduction actions nearly impossible.

Certain opportunities for salvaging profitability remain within a management team's control. New and novel techniques for improved product launch effectiveness, capacity utilization and optimization, sales and operations planning, and other areas of process problem solving are combined with solid execution based philosophies, variable compensation methodologies and conjoined measurements to deliver cash from internal sources. In a time of critical economic challenge, past improvement techniques require refreshment with the proven methods contained in this offering.

INTRODUCTION

The PM business and its longstanding inherent tie to the North American automobile industry has placed its members under the heaviest and longest period of cost pressure than almost any other industry. This existence, coupled with the wide spread fragmentation of the PM company base, has worked to erode the industry's overall profitability and cash availability to a point where it can no longer support the high capital intensity of the business. Generations of intelligent workers have exhausted the traditional means of cost reduction in an effort to maintain and restore an acceptable level of profitability. With that well being mostly dry, companies must now look to the integration of less obvious, softer techniques to continue to drive costs from their businesses.

The Historic Approach to Cost Savings

Over the years, companies have repeatedly implemented traditional cost savings measures when profitability began to wane:

- Staff reductions
- Purchasing pressures
- Travel restrictions
- Engineering efforts
- Increased quality controls

Such actions typically created issue within an organization, including but not limited to effects like:

- Painful
- Drain energy and moral

- Converts (+) energy into (-) energy
- Loss of motivation and momentum
- Costly (paradox)
- No fun

Additionally, the more successful firms expanded these efforts into organized activities that include rampant employee empowerment. While these efforts were effective and helped to neutralize some of the issues listed above, they also sometimes worked against the achievement of the reduction targets at hand by creating unproductive and political situations and by drawing focus from the primary purpose from the effort.

Whatever the case, the effectiveness of the traditional cost reduction methods have reached the point of diminishing returns in their by repetitive implementation. Companies are now faced with finding new, fresh and effective means of finding dollars that are less obvious and totally insensitive to the various traditional techniques.

A Fresh Approach

Although none of techniques discussed are new or revolutionary, many successful authors and business people in our past and recent history have taught us the value of the implementation of disciplined philosophies when properly tailored and integrated into a companies' structure. This manuscript deals with several of these established principles and processes that, when combined with the tailoring and additional new approached of the manuscript's authors, create effective and less obvious paths to driving additional cash to the bottom line.

Typically Untapped Cost Savings Initiatives- The Famous Six

The most effective of these non traditional approaches to cost savings are listed as "The Famous Six" below. They are called "The Famous Six" because they have proven their effectiveness in both PM, non-PM and even non-manufacturing businesses.

1. Self assessment
2. Time management (as a priority)
3. Execution
4. Formal sales and operations planning (S&OP)
5. 5S
6. Disciplined and timely new product launch

Let's have a basic look at each of these disciplines and their overall effect on the bottom line.

1. Self Assessment

Ollie Wight, in his book, *The Oliver Wight ABCD Checklist for Operational Excellence*, recommends the following self assessment for companies aspiring to be the best.

- Is Your Company Committed To Excellence?
- Is There Dissatisfaction With Your Current Level Of Performance?
- Does The Executive Group Provide The Necessary Leadership For Change?
- Is There A Written Business Strategy That Includes A Vision Mission Statement?
- Do We Continually Measure Our Products And Practices Against Our Toughest Industry Competitors?

- Does Our Business Strategy Recognize The Value Of A "Sustainable Competitive Advantage?"
- Do You Really Strategically Plan?
- Are All Spending Requests Evaluated On A ROI Basis And For Agreement With Our Business Strategy?
- Do We Employ A Financial And Business Planning Process That Includes Input From All Operating Departments In Our Company?
- Does Our Accounting System Provide Accurate Unit Product Costs?

Although Mr. Wight developed this checklist in the late 1970's, the impact of this type of self assessment on a company's bottom line has not dissipated with age. Companies who employ such self study and equally as important, fully implement the results of its findings, find themselves in a position of measuring overall progress and those factors that dictate the progress. Results emanate from the process and its outcomes as well through the discipline that it brings to the companies' top management and those being tracked. Realistically, "what gets measured gets done."

2. Time Management (as a priority)

We hear about it and quote it almost daily. We all recognize that it needs to be addressed. But do we really address the core issues?

Time is our greatest gift. It is also finite. Learning to use it efficiently can make a tremendous difference in the overall quality of our professional and personal lives. Understanding this, why don't we take more definitive action?

One reason is that, like diets and weight loss formulas, there is an over abundance of supposed "magic" but confusing "solutions" in the market place advertised as effective in attacking the problem. But also, like these weight loss programs, there are no potions or concoctions that take the place of common sense and hard work. Time management is a disciplined series of choices and varies for differing people and personalities. An effective approach to its improvement involves tailoring a program that best fits an organization and its associates.

There are many detriments to effective time management including those listed below.

- E-Mail
- Meetings
- Phone calls / Cell calls
- Co-workers
- Customer problems
- Stress
- Family issues
- Urgent projects

Dr. Stephen Covey, in his famous book "*The Seven Habits of Highly Effective People*", Simon and Shuster, 1989, discussed several techniques for combating certain of these distractions. My personal experience has found the proper use and expansion of the simple relationships illustrated in Figure 1 that it provides to be very effective in conquering this time management challenge.

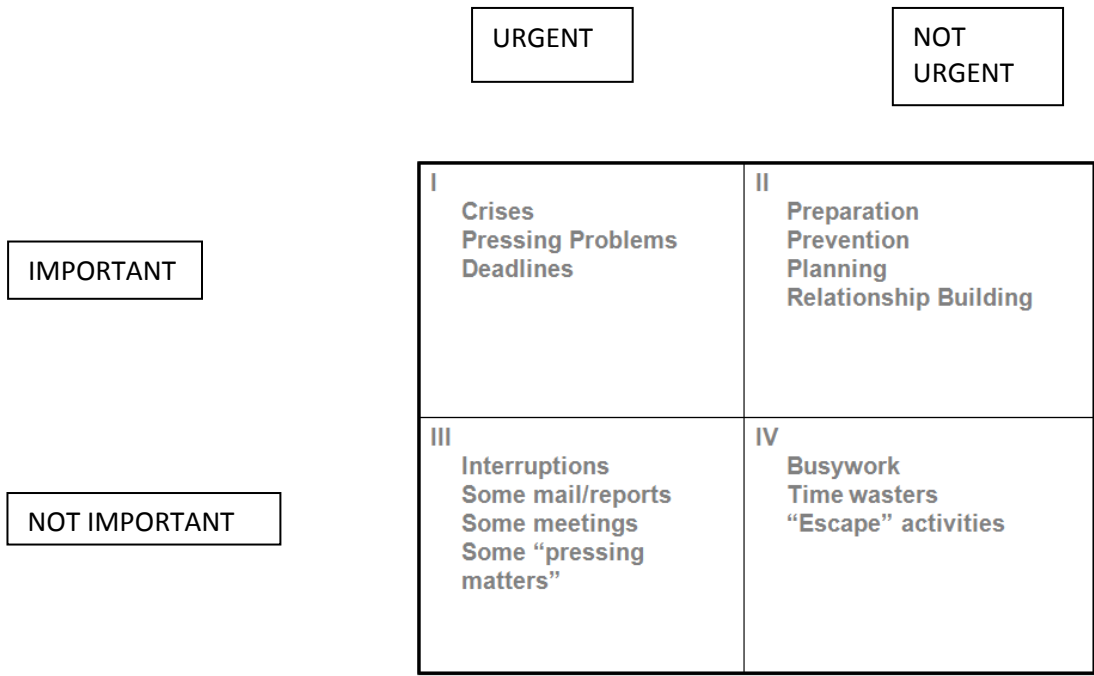
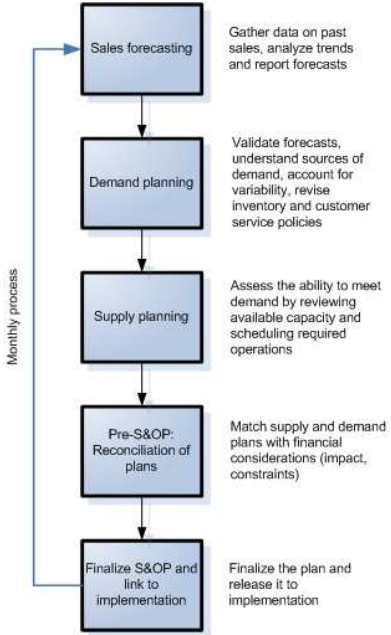


Figure 1: Urgent vs. Important Time Uses

Dr. Covey observes that the typical business person spends upwards of 85% of their time in quadrants I and III. Logically, the majority of this time would be better invested in the pursuits outlined in quadrant II. Further observation concludes that the more time spent in II, the lower the occurrences of those issues listed in I. Experiences business people have ample experiences which tie the time spent in (I) issues and the associated negative cost impact on their companies.

3. Formal Sales and Operations Planning (S&OP)

APICS defines S&OP as the function of setting the overall level of manufacturing output (production plan) and other activities to best satisfy the current planned levels of sales (sales plan and/or forecasts), while meeting general business objectives of profitability, productivity, competitive customer lead times, etc., as expressed in the overall business plan. The theoretical definition goes further to state that one of its primary purposes is to create a plan of operations that will execute top management’s business plan as measured by of inventory levels and sales order backlogs in a way that levels demand and keeps maintains a stable and happy work force. To work effectively, the individual process must extend through a planning horizon sufficient to plan the labor, equipment, facilities, material, and finances required to accomplish the operations plan. The core of this plan is the intrinsic (internal) sales forecast which is delivered as a blend of the customer forecasts (extrinsic) and the history that companies build on specific customers and products. Because the plan affects many company functions, it is normally prepared with information from marketing, manufacturing, engineering, finance, materials, etc.



The monthly Sales and Operations Planning process

The cost savings benefits of S&OP are numerous. Proper planning in the areas of raw materials, labor, inventory, capital, capacity, engineering product development, financing, budgeting etc. can have the single most prominent impact on a company's P&L as it impacts all of its determining categories. Figure 2 details the typical flow of a properly running company S&OP process.

4. Execution

The largest common characteristic of a profitable company is one who demonstrates the ability to execute the plans that are put in place. Too many are impacted by the illusion that things are under control after the plan is made to address the particular problem. I am sure you have heard the old adage "from the best laid plans of mice and men."

Successful and profitable companies are best characterized as those who execute or in plainer terms "get things done." Execution finds its core in proper planning followed by an intertwining of the following tools/principles/disciplines to assure that the plan is properly carried out.

- A detailed project plan
- Regular review meetings to track progress
- Single point accountability for completion of tasks
- Visible measurements designed to evaluate the magnitude and depths of individual tasks
- Repetitive testing of items to assure long term effectiveness
- A reward system to reward the doers and to penalize the non-doers

Mr. Larry Bossidy, former long time GE executive and Allied Signal/ Honeywell CEO, in his book "*Execution; The Discipline of Getting Things Done*" with Ram Charan and Charles Burck, outlines the basic requirements of an execution based culture. Of these characteristics, I consider the insistence on robust dialogue (say what's on your mind..respectfully) and emotional fortitude (having a thick enough skin to ingest robust dialogue) as that being key to execution based success.

5. 5S

One of the best definitions that I have found for 5S comes from Wikipedia 2009. It defines 5S as workplace organization methodology that uses five Japanese words which, when translated into English, start with the letter S. 5S is a philosophy and a way of organizing and managing the workspace and work flow with the intent to improve efficiency by eliminating waste, improving flow and reducing process unevenness.

The 5S's are:

Phase 1 - **Seiri** (整理) Sorting

Phase 2 - **Seiton** (整頓) Straighten or Set in Order

Phase 3 - **Seisō** (清掃) Sweeping or Shining or Cleanliness

Phase 4 - **Seiketsu** (清潔) Standardizing

Phase 5 - **Shitsuke** (躰) Sustaining the discipline

A properly planned and executed 5S system yields greater morale, safety and efficiency. Aside from the direct efficiency benefits that convert to profitability in the areas of less wasted time, lower safety costs, a clean workplace and its effect on product quality, etc., the 5S mentality also delivers a sense of responsibility, accountability and accomplishment to the entire business operation. 5S represents the highest visible means of execution and its discipline carries over to all other profitability enhancements discussed in this manuscript.

6. Disciplined and Timely New Product Launch

The single largest current and historic problem in the PM and other manufacturing and non-manufacturing industries is the inability to launch new products on an accurate and timely basis. Although formal statistics are not available, individual and group experience provides substantiation that lost dollars wasted by these failed launches in the areas of lost sales and added costs have impacted the combined PM industry in the tens of millions of dollars in the past 30 years.

The two largest causes of failed product launches in the PM industry are the lack of upfront engineering, planning and product development and the premature release of the products to the production group prior to full process capability being established. The frequency of both of these problems is substantially reduced with the implementation and execution of a detailed and disciplined new product launch procedure.

The primary requirements of an effective new product launch process are as follows:

- Totally integrated, cross-functional team approach
 - INCLUDES CUSTOMER
- Focused on critical sources of process variability
- Combines customer defined fit, form and function with PM process capabilities – CLASSIFICATION OF CHARACTERISTICS
- Drives the formation of PFMEA and process control documentation
 - Prior approval of gauging plan
- Drives true process capability sign-off well past the PPAP stage
- Requires process capability sign-off by all levels of the organization
 - Totally eliminates the “throw it over the wall to production” mentality

PHASE	QUANTITY	EVALUATION	SIGN OFF
I - TOOL	100	TOOL SET SIZES	ENGR/OPS
II - PPAP	500	CPK ALL 3,4	E/OPS/DIR/ CUST
III - R@RATE	3 SHIFTS	CPK ALL 3,4	E/OPS/DIR/ CUST
IV - PRODUCTION READINESS	3 WEEKS PRODUCTION	CPK ALL 3,4 (VARIABILITY)	E/OPS/SR. STAFF
V - PRODUCTION ASSURANCE	25% ANNUAL PRODUCTION QTY	CPK ALL 3,4	E/OPS/SR. STAFF

In addition, the implementation of a multi staged product/process capability signoff procedure (Figure 2) assures that full process robustness is established before the engineering professionals fully turn their attention to a new launch.

As related to S&OP, all product launch activities should be brought to the S&OP process by engineering to assure proper planning and provision for launch activities and the necessary time associated with them.

FIGURE 2: The Five Stages of a Robust Product Launch

SUMMARY AND CONCLUSIONS

Like the many applications that the PM industry has successfully converted over the past 25 years, the “low hanging fruit in the areas of business cost reduction have also been fully harvested. To meet the challenges of today’s economic recession and future pricing pressures emanating from a truly global economy, business leaders must embrace innovative and complex means of increasing efficiency and maintaining workforce moral in order to survive in this growingly difficult manufacturing environment.

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