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# LEAN THOUGHTS

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## Manage the Contract or Improve the Value Stream

The following is the latest communication from James Womack author of the machine that changed the world .... Enjoy

Dear Richard,

As much as I would like to, I can't walk frequently along every type of value stream. As a result, it has been a while since I've walked along the complex value streams shared by customer firms and their suppliers. So when several firms recently offered a chance to take multi-organization walks -- from the point of customer use back to the beginning of supplier manufacture -- I was delighted to put on my walking shoes and stride along with teams from the customer and supplier organizations.

As I walked I was quickly reminded of how easy it is for all of us to focus on formal measures of value-stream performance as written in contracts: Defects delivered to customers per million opportunities. Price per piece, often without reference to what is happening either to customer volumes or upstream materials costs. Delivery performance, often to a Material Requirements Planning (MRP) schedule that has little relation to actual customer needs at the point of use. These indicators can be useful but they measure results after the fact, when mistakes have already been made. More important, they say nothing about causes of problems or how to eliminate them.

As I walked I was also reminded how hard it is for customer purchasing organizations and the supplier sales organizations they usually interact with to talk in specifics about their shared value-creation process and the root causes of problems, ideally before they occur. In the current time of gyrating customer volumes and raw materials costs for suppliers, the result is often a zero-sum ritual of customers making threats (based on penalty clauses in contracts) and suppliers making promises to do better (based at most on a hope and a prayer.)

It is actually all shadow boxing because without careful attention to the shared design and production processes, little improvement in performance is possible. In the short term, the customers have nowhere else to go and the suppliers can't do any better. So both sides get the satisfaction of some cathartic mud wrestling while nothing actually changes. How can we all do better? Well, first, we can't instantly. The short-term future is determined by decisions made long ago. So contracts with their penalty clauses rule. But we can do better in the intermediate and long term if we shift our focus from wrangling over contracts (reflecting arms-length, abstract legal relationships) to managing shared value streams by jointly observing the actual supply process.

To do this the customer needs to take the first step. Taiichi Ohno at Toyota is said to have said, "The shop floor is a reflection of management". (And if he didn't say this, he should have!) Let me add a corollary: The supply base and the performance of value streams shared with suppliers are a clear reflection of the customer's purchasing management. A brilliant supply base with superior prices, quality, delivery, flexibility, and product performance doesn't happen magically. And it can't be bought off the shelf instantly by visiting some virtual "supplier supermarket." It is created over time by a brilliant purchasing organization. Indeed, creating a brilliant supply base is the real (and only?) value created by purchasing.

So how do we begin the transition from managing contracts to improving value streams? First, the customer needs a "plan for every supplier", just as Toyota has a plan for every part, every machine, every employee, and ... every supplier. This means determining the right suppliers to work with over the long term and then understanding the current state of every supplier's design and production process for the items supplied.

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### Where "Lean Thoughts" Become Reality



Many years ago, when I first visited Toyota in Japan, I had dinner with the purchasing director and asked how he could be sure that Toyota was getting good performance from its suppliers when only two suppliers were employed for a given category of need and when Toyota relied on target pricing rather than supplier bids. "How," I asked, "do you know you aren't getting ripped off?" After an incredulous look, he answered, "Because I know everything -- every aspect of every value-creating process -- running from raw materials at suppliers through Toyota's operations. That's my job."

In practice, this means continually determining the performance gap between what the supplier's value stream is capable of delivering and what the customer needs. Then it requires a future-state plan explaining who will do what when - both at the customer and at the supplier -- to achieve a future-state value stream adequate to the customer's current and future needs.

But creating a lean supply stream also means that purchasing needs to look inward for a bit of organizational hansei (critical self-reflection) inside its own company walls. Why are schedules from production control so erratic and inaccurate? Why aren't orders to suppliers leveled? Why are the logistics to get items from suppliers to the point of use so loosely managed? Why are design requirements for supplied items frozen so late in the development process? Why is the customer's production process so poorly designed and in need of immediate kaizen after launch, upsetting the production process at the supplier (whose process is also poorly designed, in part due to the lack of customer attention)?

The typical reaction of purchasing organizations when I make these points is to say, "Wait a minute. We just obtain needed items from available suppliers and bargain hard to get good terms in contracts that we can enforce. We have no mandate to look downstream into our organization or upstream into what suppliers actually do in their value streams to meet our needs. And we certainly can't afford to build long-term, stable relationships with suppliers as markets continually gyrate." And I respond, "Well fine. But you will always have a lousy supply base with poor performance and you will spend your time chasing parts."

#### Save Headcount!!

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So it's really a matter of what purchasing organizations think they should do and what they think they can do. Perhaps you remember from last month's e-letter Henry Ford's aphorism that you can think you can or you can think you can't and you will be right. (But please forget that Henry actually thought he couldn't create a brilliant purchasing process and therefore vertically integrated instead!)

In today's world we know that vertical integration won't work. De-integration is here to stay and for most organizations purchased items account for half or more of their total costs plus a large fraction of their quality, delivery, and responsiveness problems. So we all need to think that purchasing organizations can create and sustain brilliant supply bases.

Doing this will take time and upfront investment but the cost of not acting is far greater over time. So wherever you are in your organization and whatever your organization's current relation to its suppliers, I hope you will lend a hand to help with the critical transformation to lean supply.

Best regards,  
Jim  
James P. Womack  
Founder and Chairman  
The Lean Enterprise Institute

A Spanish teacher was explaining to her class that in Spanish, unlike English, nouns are designated as either masculine or feminine. 'House' for instance, is feminine: 'la casa.' 'Pencil,' however, is masculine: 'el lapiz.'

A student asked, 'What gender is 'computer'?' Instead of giving the answer, the teacher split the class into two groups, male and female, and asked them to decide for themselves whether 'computer' should be a masculine or a feminine noun. Each group was asked to give four reasons for its recommendation.

The men's group decided that 'computer' should definitely be of the feminine gender ('la computadora'), because:

1. No one but their creator understands their internal logic;
2. The native language they use to communicate with other computers is incomprehensible to everyone else;
3. Even the smallest mistakes are stored in long term memory for possible later retrieval; and
4. As soon as you make a commitment to one, you find yourself spending half your paycheck on accessories for it.

(THIS GETS BETTER!)

The women's group, however, concluded that computers should be Masculine ('el computador'), because:

1. In order to do anything with them, you have to turn them on;
2. They have a lot of data but still can't think for themselves;
3. They are supposed to help you solve problems, but half the time they ARE the problem; and
4. As soon as you commit to one, you realize that if you had waited a little longer, you could have gotten a better model.

The women won.

2008 Consortium Event Schedule



Tour Workshop Conference

January	February	March	April	May	June
<p><b>T</b></p> <p>Wednesday 16  <b>Eaton Electrical</b>,                      contact Joe Fisher,  <a href="mailto:JoeRFisher@eaton.com">JoeRFisher@eaton.com</a></p>	<p><b>T</b></p> <p>Wednesday 13,  <b>ACE Bakery</b>,                      contact Cindy Grolleman,  <a href="mailto:cgrolleman@acebakery.com">cgrolleman@acebakery.com</a></p>	<p><b>T</b></p> <p>Wednesday 19,  <b>Nestle Waters</b>,                      contact Mariela Castano  <a href="mailto:mcastano@perriergroup.com">mcastano@perriergroup.com</a></p>	<p><b>C</b></p> <p><b>Consortium Shareshowcase</b></p> <p>Saturday 05  <b>Eaton Milton</b>,                      Contact Cindy Grolleman  <a href="mailto:cgrolleman@acebakery.com">cgrolleman@acebakery.com</a>                      or Joe Fisher  <a href="mailto:JoeRFisher@eaton.com">JoeRFisher@eaton.com</a></p>	<p><b>T</b></p> <p>Wednesday 14,  <b>Alumicor</b>,                      contact Barry Wood  <a href="mailto:barry@Alumicor.com">barry@Alumicor.com</a></p>	<p><b>T</b></p> <p>Wednesday 18,  <b>Morrison LaMothe</b>,                      contact Tony Vita  <a href="mailto:tvita@morrisonlamthe.com">tvita@morrisonlamthe.com</a></p>
July	August	September	October	November	December
		<p><b>T</b></p> <p>Wednesday 24,  <b>Kraft Foods</b>,                      contact Hanif Jivraj  <a href="mailto:hjivraj@Kraft.com">hjivraj@Kraft.com</a></p> <p><b>C</b></p> <p><b>Executive Forum</b>                      Tuesday &amp; Wednesday                      23<sup>rd</sup> &amp; 24<sup>th</sup>                      Contact Richard to register  <a href="mailto:rkunst@kumstartofsolutions.com">rkunst@kumstartofsolutions.com</a></p> <p><b>C</b></p> <p>22<sup>nd</sup> Transportation                      Thursday 24<sup>th</sup>  <a href="http://www.transportconference.net/emaplan.html">http://www.transportconference.net/emaplan.html</a></p>	<p><b>T</b></p> <p>Wednesday 16,  <b>CTS Corp.</b>,                      contact Navneet Mann,  <a href="mailto:navneet.mann@ctscorp.com">navneet.mann@ctscorp.com</a></p>	<p><b>T</b></p> <p>Wednesday 12,  <b>Messier-Dowty</b>,                      contact Mike Smith  <a href="mailto:Mike.Smith@Messier-dowty.on.ca">Mike.Smith@Messier-dowty.on.ca</a></p>	<p><b>T</b></p> <p>Wednesday 10,  <b>Orenda</b>,                      contact Brenda McIntosh  <a href="mailto:brendamcintosh@orenda.com">brendamcintosh@orenda.com</a></p>