

Action Opportunities

There are eleven key areas that should be reviewed when you are running supplier development projects. They all focus around process and cost control of your supply base, but should also be used internally for driving business process improvements for cost savings. Supplier development teams need to be focused on the big picture of Lean and TCO. The following are basics that we hear about, but many times do not have the cost modeling tools developed, we forget, and at times teams are not provided the appropriate training.

Therefore, in addition to the Seven Wastes, Supplier Development Teams need to understand how to calculate their associated savings, including product quality benefits. Part of this process will require either a team member from Finance to support cost analysis, and areas of focus during the lean exercises should include:

1. SG&A

- In a deflationary market companies have reduced their fixed costs. Have these reductions been reflected in your current business or new quotations?

2. Raw Material Costs

- Raw material prices fluctuate greatly in challenging economic environments. Review supplier quotes from the past three years, against competitors and benchmark indices.
- Can your company take advantage of different trade pacts that allow shipment of materials via other countries versus direct from the country of origin to your operations.

3. Purchase Component Costs

- Are your suppliers marking up component costs that they pass along to their customers?

- If yes, why? If the answer is to cover incremental labor and O/H. This should be a quick check to determine if the incremental amount is covered in your suppliers standard SG&A.
- Spot check prices to validate accuracy.

4. Overstated Labor Rates

- Are rates consistent with DOL published rates for the region? Compare past to current rates in the cost breakdowns.

5. Suppliers Engineering Design & Development

- May be difficult to verify. Should only represent the cost associated with the part.

6. Capital Equipment

- Are the suppliers and Purchasing involved with Engineering and Manufacturing?
- Is Manufacturing requesting specs that are not necessary and how does the proposed design compare to industry leaders?
- Typically the cost of capital equipment can be reduced 5 – 20% when asking the suppliers to design equipment and tooling around part performance specs.
- Are tooling and capital equipment compatible?
- If your company is experiencing financial challenges, evaluate an operational lease with performance metrics versus upfront expense?

7. Indirect/MRO

- Little emphasis in this area. Yet one of the easiest to implement and achieve significant results. While much smaller than Direct Spend, the total savings in this area at a company can actually surpass Direct. Greatest opportunity to leverage across dissimilar businesses and have

autonomous contracts. Bob Rudzki has written a significant amount on this subject in preceding chapters. The tools and concepts apply during lean exercises.

8. F/X

- If you source to LCC regions, document the base exchange rate from which you start your negotiation. Not doing this and not establishing year over year productivity goals to mitigate up or downside risk can promote a cost structure that is difficult to manage.

9. Transportation

- Small package and LTL are some of the biggest drivers of cost, yet little time is spent understanding the mark-ups. Are you up to the challenge?
- Drayage – Costs are small but add up fast.
- Accessorial charges for all modes of shipments. Do you understand the details? Solid opportunity.
- These areas alone have the potential to add 5% to the bottom line.

10. Warehouse

- Are you using both SOMI and VMI for warehousing suppliers inventory at on-site, off-site warehouses, or transportation providers DC's to feed your factory? If yes, what is the true cost?
 - Companies sometimes forget to evaluate the total the incremental costs associated with these program, i.e. logistics costs, resources (total burden value vs annual salary).
 - Suppliers have a cost of capital that they are paying to store these goods at their expense. These are not free programs.
 - Some hard questions for operations, but Procurement and Supply Chain profession is about total cost. Operations are where money is made, and nobody likes to get singled out. However, supplier development teams have the ability to ask tough questions, but

are the operation MRP tools adequate to generate JIT? Are personnel using the MRP tools correctly?

- Improvements in inventory ordering, scheduling, and shipping processes can add 2 – 5% to the bottom line.

11. Lean

- Are the suppliers practicing Lean? Should Purchasing apply concepts with Suppliers to drive efficiencies for cost savings?
 - If yes, does the Purchasing Team understand how to calculate savings from newly implemented programs? If not, a representative from finance needs to be part of the team.
 - Using a Six Sigma Methodology teams:
 - Identify performance opportunities
 - Classify – What is in scope and out
 - Name the Project Sponsor(s) and Team from both supplier and customer
 - Measure processes, performance gaps, and establish baselines
 - Develop and implement improvement plans
 - Identify the ROIC
 - Present and implement the plan.
- Does Purchasing understand how to calculate savings from improved supplier quality?

The prime message on Lean – If you are implementing a Supplier Development program with a focus on Lean and TCO, the savings that can be achieved can be better than sourcing to LCC regions.