Think growth, not recession

The news reporting about the culling of over two million jobs and more to come or the austerity drive by some auto majors would have sunk the hearts of many and created gloom in the minds of those who work in such industries. Although most of the jobs lost are overseas and in the West, it would have set speculation afloat about the fate of other industries. Read on to know how you can beat this recession...

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Many people succumb to the fear and uncertainty surrounding the present economic situation. No doubt that there has been certain lesser consumption in recent months. But then, what is new about this? The sign was visible long ago (Figure 1). Those who have been around over the past three decades know that depressed market conditions, financial crises or recession are all economic corrections that are going to show up now and then. History tells us that since the oil crisis of 1973, we have had demand recession situations roughly once every six to eight years, then why all the fuss now, and what have we learnt?

Companies that do not change their behaviour to adapt quickly and continuously to the changing demands and consumption patterns of their customers will - in a situation like this - end up with large inventory and other costs. Companies that run production lines from a speculated demand forecast will be more affected in a demand recession and strapped for cash because their cash will be locked up in inventory and the facilities

built to store it, as compared to those whose production lines are run using the dynamic demand rate concept and a lean value stream.

Understanding costs

Companies whose thinking resonates with the American or European industrial system can be found groping for conventional solutions today, expecting a miracle. Many companies grope for costs in wrong areas. What have we learnt about costs over the past three decades? We see the same thinking and hence the same reaction as we have seen over the past three decades – cutting travel and hotel costs, entertainment, stationary; freezing recruitment, training and employee costs; switching off lights, etc. These may show up under the expenditure statement and the accountant might call them austerity measures. But world-class companies are expected to have a goal-oriented thinking when it comes to spending money in these very areas - at all times and not the discrete behaviour that is found to be out of place when the going gets tough. Companies that have inculcated a discipline in the entire value stream have their very business processes built with austerity.

The usual reaction seen from most companies during hard times such as these – financial crisis or recession – is to cut costs in every possible way. Rarely do managements propose new programs that are different to doing 'more of the same'. This kind of a reaction happens when accountants take the centre stage in the cost control efforts, while it should really be the job of the production or the value-creating stream. A crisis is the best time to implement lean manufacturing: after all, the Toyota Production System was born out of a crisis! Toyota used the crisis after the war to fuel the paradigm shift. Other managements who used such crisis situations to implement lean manufacturing and produce great results are Harley Davidson, Ford in 1920's, Bridgeport's joint venture in South East Asia, Wiremold, back home Mysore Kirloskar and many more. Crisis need not be environmental; it can be company specific too. Crisis helps because it makes a paradigm shift easier and faster, lean programs do not require injection of capital as they are self financing, and there is a need to improve the cash flow.

A planned and well-executed lean implementation is usually self-financing. The improvement in positive cash flow pays for the implementation program as it goes along. Unlike other improvement programs such as computer systems, software or new equipment, lean requires relatively little expenditure, if at all, early in the program, and the most dramatic results come early through the elimination of type-two wastes. The results of inventory reduction bring in improved cash flow. The time required for achieving productivity improvements may vary from one company to another. But as productivity improves and costs begin to come down, the cash flow keeps improving. Productivity improvements and just-in-time inventory contribute to a positive cash flow.

Lean value streams think differently about costs (Figure 2). In the past three decades, we have seen a different production management system that is capable of producing far superior results than those being achieved by most industries. Companies that have adopted the lean manufacturing system have learnt

> The mantra to tide over any crisis really is efficiency, efficiency and more efficiency. We have constantly brought down inventory levels and reduced the throughput time. High efficiency ensured that we do not have to succumb to market pressures
>
> Brij Mohan Lall Munjal

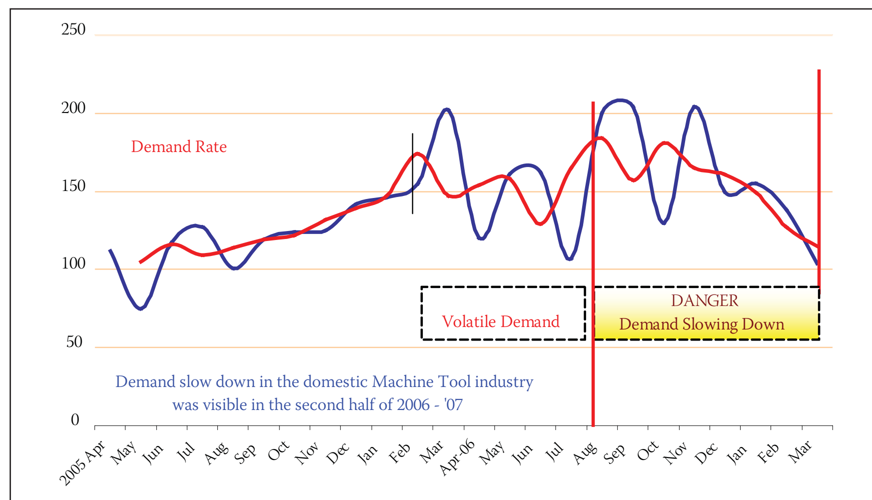

Figure 1: Coming events cast their shadow

Figure 2: Reduce wastes to reduce cost

> There are two major lessons learnt from the past recession; first, the need to go beyond cost control to cost reduction. The other lesson is to look for tools, techniques, concepts (lean manufacturing); grab them and use them, ahead of the curve, before the competition
>
> Dr Mrityunjay Athreya

to cut overall costs by 20 to 40 per cent which are hidden in the form of wastes occurring in the value stream. Companies must develop a better understanding of costs, where 'overproduction' is seen as inventory; where 'overprocessing' as extra time utilized of men and equipment, while the extra cost is not paid by the customer; where when material, men or information 'waits' for want of demand, action or decision it creates inventory; where any form of 'rejection or rework' or even acceptance with a deviation and customer complaints are costs to the company; where every unnecessary 'movement' is a waste; where 'transport' or hauling is non-value added; where any form of 'inventory' - be it as raw material or work in process or finished goods - is a sign of inefficiency that comes with a huge cost and blocks capital.

Lean manufacturing companies have learnt to see cost as conventional minds cannot even comprehend. That is how they look at productivity improvement through reduction of costs. The result - they end up with extremely good cash flow and far more profits. Mentioning the case of Mysore Kirloskar may sound like a cliché, but when the world reeled in recession they remained flooded with customers and orders. How did they cut lead times by over 90 per cent, improve quality by over 99 per cent, cut inventory by over 80 per cent, gave a price reduction to customers by 30 per cent and yet made more profits and had a dream cash flow is decoded and has many lessons to learn, especially one on how to beat the effects of recession very quickly.

Understanding demand rate

The way to avoid inventory pile-up starts with first thinking about the customer and how one addresses the customer demand. Lean organisations constantly monitor the demand rate – on a monthly, weekly or daily basis. Since consumption is never a straight line, so is demand. They link this rate of demand to the value chain through which the value is made to flow in conformity with the demand, considering the intrinsic capacity available. Allowing the value to flow by customer pull, they ensure that there is no build-up of inventory. Lean thinking will help one to proact rather than react.

Understanding demand rate will also develop any company's ability to see more clearly into the future and be proactive in taking corrective actions – address new markets, develop new products, develop new segments, acquire new technologies, just-in-time inventory, training & development, etc. Not allowing build-up of inventory means not overproducing; not requiring excess raw materials, equipment or man-hours, floor space, storage space/racks, material handling equipment, data-entry operators, computer terminals; overcoming threat of obsolescence; eliminating the need to rework due to surface deterioration, removal of surface damages such as dent and pitting marks, minimising blocking of capital, interest on capital, etc. Everyone involved in such activity – including those who make such decisions – are people with negative roles and therefore easily avoidable cost.

Most companies do not carry out a dynamic measurement of the demand rate. They resort to conventional

> At a time when there is spare manufacturing capacity and employees are not as busy, the management needs to pursue all possible steps to improve quality, reduce cost and improve productivity of operations. At Bajaj Auto, we are trying to see what we can do to come out stronger when demand starts picking up
>
> Rahul Bajaj

forecasting. The problem with a forecast-based plan is that it varies in behaviour with the actual customer demand. When the plan is released for action, all the suppliers are activated with the new demand. The suppliers in-turn gear up for execution and take action. A couple of weeks down the line, the marketing department which helped make the forecast begins to see that the actual demand is in variance to its plan. They then rush to do a plan correction. By then, there is inventory flowing in accordance with the forecast-based plan. This material is then shelved both at the mother plant as well as at all the suppliers. Those who use the 'batch and push' concept end up with more unwanted inventory than those who resort to 'pull and flow'. This is how unwanted inventory is successfully created. Those companies that allow for planning of failures such as allowances for rejections etc end up with higher levels of inventory. Measuring inventory levels on a daily basis is a great way to measure the operational efficiency of an organisation. An accountant may consider inventory as an asset, but when it is not flowing to the customer or waiting, that asset becomes a liability.

Think growth

Another problem is with the complacent way in the thinking that exists with many organisations. Companies that produce any kind of an end product must understand that while during a recession the consumption in the market place may come down, it does not become zero. A hundred may reduce to 65 or 70, but never to zero. Companies must think about the size of global consumption in their product portfolio vis-a-vis their share in it. Invariably, the share comes out to be low, which means the actual consumption is many times any one company's production volume. Then, the right question for introspection is "If there is consumption still happening out there, why am I not in that market?" "If my share in the global market is one or two or five percent, how can I make it grow and double?" Such positive possibility thinking sees no recession.

The answer is simple: customers will look for companies and products that deliver them the best value. So companies that have worked on improving the value delivered to their customers compared to their competitors will be less affected. Companies that have learnt to pull and flow value only against definite demand will have a rich cash flow at these times. Organisations that have not started their lean journey can start now, using the lull, and secure the advantage for the future. Recession or depressed market conditions or demand crunch, call it what you will, they are all economic correction cycles that are going to come once in every six or seven or eight years and there is no running away. There is an opportunity here to stand tall and beat the trend. Companies like Toyota in Japan and Mysore Kirloskar back home have shown how it is done. Can you do it? Yes you can. How? By making a beginning! MMT

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