

LEAN THINKING IN WHOLESALE DISTRIBUTION...



Vendor Managed Inventory – What’s True Collaboration?

Introduction

As we know it today, Vendor Managed Inventory (VMI) is used to monitor and replenish a distributor’s inventory by a supplier. However, VMI implies some degree of collaboration, between the two, that link the different planning processes of each partner. There are several ways to specify these links between each partner’s processes. Are there common objectives? Are there any requirements and/or constraints?

Supply chain collaboration has become a more strategic effort in today’s demanding business environment as a way to create new sales revenue opportunities, greater efficiencies, and customer loyalty. Researchers have written “dissertations” on this subject, yet distributors and even some manufacturers have not often been privy to many of the practical considerations – and in plain terms.

The need for supply chain collaboration between partners, particularly as it regards sales/demand visibility, and the sharing of sales/demand data is often cited as an important challenge - as each partner wrestles with product availability, high stock levels and inefficient capacity utilization - dependent on their own particular circumstances, focus, and place in the partnership.

Efforts to increase demand visibility actually go back to the 1980’s. In the 90’s “Continuous Replenishment Policies” were developed by some pretty large companies, many in retail, that were based on “actual consumer demand”, and so was born the “pull systems” that began to replace historical “push systems”. “Lean Thinking” philosophy was interjected as a way to squeeze-out all the unnecessary “wasteful” activities inherent in each partner’s “value-stream”. Ultimately, the practice grew into VMI, and a transfer of the distributor’s inventory replenishment responsibility to the supplier; a delegation of ordering and inventory replenishment planning.

So when we talk about VMI today, we have to go beyond the notions of logistics and the physical and tangible activities, to relationship building and management, the behaviors of each partner, and maybe even some other intangibles. Beyond the replenishment aspect of the relationship, what does VMI mean in terms of “mutual advantage and productive relationships”, the tactics and the strategy?

What Are The Collaborative Objectives of VMI?

VMI alters the fundamental structure of the supply chain. Processes, cooperation (emphasizing relationships), and technology to support VMI is impacted. Often though, there is only general consensus as it relates to the VMI concept’s objectives and the expectations of all the partners:

1. Distributors typically want to ensure higher customer service levels with lower inventory costs.
2. Suppliers want to reduce production, inventory and transportation costs

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Now, some of these may be common objectives between the partners, but others may not be. At the most simple level, for instance, distributors may only consider VMI as “a different method to procure stock” – but maybe based on some pre-specified criteria.

Certainly from a supplier’s perspective, the use of the same “actual sales/demand” information and product inventory status that the distributor previously used to make buying and inventory management decisions, provides the supplier with “better visibility” into actual customer demand and the priority of need. The supplier’s production, logistics, and transportation costs can potentially be reduced as a result of coordinating replenishment plans for all its partners.

Both partners have the potential to reduce safety stocks and re-order lead times. **Both partners** have the potential to implement a change to a “pull system“, that fosters a “continuous flow” of product through a “higher replenishment frequency” (speeding-up the supply chain) and towards reducing average inventory levels, i.e.; inventory cost savings. These become the new “levers”, and opportunities, for mutual advantage. Each partner, for VMI to reach its potential, has to “inherit” each of these objectives.

What Is The Scope of A VMI Relationship?

For “real” VMI success, several concepts and ideas need to be understood:

- How a pull replenishment system works
- A collaborative and pre-established middle to long term objective for both partners, which identifies and supports what the “new reality” in supply chain management will be
- The technology to share sales/demand information between partners
- Integration of the supplier’s production planning and scheduling into the entire VMI process
- How “target inventory” fits into the equation; a shared and understood plan for the necessary inventory level objectives
- The integration of “Lean Thinking” concepts into the “value stream” of each partner that reduces total supply chain costs

Put it another way, call it the new “agreements” between distributor and supplier;

- The agreement that specifies the planning required of the partners in the VMI relationship
- The agreement that determines what the parameters are which will regulate inventory management (target inventory, order size quantity and delivery frequency, inventory cost targets, service level targets, and transportation rules, etc.)
- The agreement that governs product replenishment priority rules

So you see, distributor and supplier have a lot to understand and agree on, for successful VMI, including their own objectives and what might be their own and/or each other’s constraints.

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Conclusion

Sometimes it's not clear, to all, whether VMI is a model, a process, a strategy, a relationship, or some other "link". Best said; "there has to be a unified view between partners, that incorporates the needs of both, to the largest extent possible". In other words; identify and obtain the most favorable aspects of VMI, within the context of your relationship with your partner.



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