

**LEAN THINKING IN
WHOLESALE DISTRIBUTION...**



***Your Distribution Center &
Warehouse Operations...
Cost Center or Profit Center?***



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White Paper

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Your Distribution Center & Warehouse Operations... Cost Center or Profit Center?

Executive Summary:

This all may sound a little foreign to you...

One of the first things I learned about is that in most distribution operations the focus is on things like:

- How do we get our accuracy better?
- How do we get our throughput better?
- How do we assimilate more sku's?
- How do we do this...how do we do that?

Sometimes we develop great measurements, for sure. However we tend to forget that each entity in distribution operations, each piece of the "value-stream", is part of your company's financial picture. Of course it is; we're trying to make money. Distribution entities tend to be viewed as cost centers - not profit centers - and that should become a very clear distinction in terms of how you approach your distribution operations.

Think about it this way; what if you had to outsource your distribution operations and the functionalities you now provide internally? How much would you pay for it? Even better question; how much would you **want** to pay someone else to do it? How would it affect your profitability?

The big question: why?

So why is a thing like saying; "I'll double productivity" just not enough? One reason is that you are faced with the following – in fact, I see it almost every time I walk into a distribution center/warehouse:

- "My sku's are growing"
- "We're picking more "eaches", less cases" (or vice versa)

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- “We’re processing smaller and more frequent customer and/or branch transfer orders”
- “E-commerce has thrown us back on our heels”
- “We’re expanding and growing – you want me to reduce my labor costs?”
- “There’s more time compression between order receipt and our commitment to ship/deliver it.”
- “I just got asked to prepare a plan to provide more value-added services to our customers”

These situations all “ask” the same question; “how do I figure how we run an operation and keep our costs down?”

Sure, you can “kaizen” the heck out of it and spend a few days trying to figure out the best place to put a roll of shrink wrap (and frankly, these incremental improvements do help), but the big question is; how will I reduce my costs (and the boss said – by X%)?

You have to show what profit a distribution center/warehouse can generate

Your mindset has to change. In fact, look at it this way. When I’m sitting in a meeting with a VP or Director of Purchasing, that person is probably incented based on the money they can save when they buy product. Yet in a distribution center/warehouse operation, the mindset is – it’s a cost center. Somebody’s thinking; “how much are you costing us today to do your jobs?” The mindset that has to change is - how do I actually show how much profit I’m pulling for the company? What am I adding to the bottom line?

Your competition, as you can tell by all the technology out there - and in use, is getting the proverbial – “mean and lean” - and may be doing things that many of you may or may not be doing. But you know; they too are looking for ways to get better; reducing operational overhead while providing additional services and more cost effective functionality. In other words; they, too, want to answer the questions:

- How do we get our accuracy better?
- How do we get our throughput better?
- How do we assimilate more sku’s?
- Etc., Etc.

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But, it's more than just saying; "I want to go from 99% to 99.5%. Oh, and by the way, it's going to cost \$500,000 in automation"! What's the financial impetus for that investment? There is none, if you are not playing in the arena that companies are driven by - the financial arena.

The race for space

You know the old adage; "if they build it, they'll fill it". We've all been there before. Another xx,xxx square feet; "it'll last us for years". What happens? Well, a year and a half later it's a different story. So space optimization falls into this discussion too, particularly if we really need more of it. That isn't always the case.

"My cost per line or my cost per unit is rising – I'm throwing more people (time) at it, but we're still making mistakes because new elements are being added - I'm not even maintaining".

In a distribution facility – physically automated or not – the fact remains that information has to be automated. People have to be directed. They need to know exactly where to go, why they're going, how long it takes to get it and process it. That becomes the basis for examining whether distribution operations can pull profit.

Now I'm going to pull profit, because I'm actually taking the same structure of the company and I'm squeezing money (cost) out of it. Again, that means you are pulling profit no differently than anybody else in the company (even that Purchasing person, we mentioned earlier). The problem is; nobody realizes it. Very rarely does anyone in distribution operations promote themselves as a "profit maker".

Can a distribution center/warehouse really make a profit?

Is it possible? Well, if your definition of profit is retaining more money than you have previously; then absolutely! You made more money on the same sales and the same margin than you did before - more money to the bottom line. If I save \$1.00 in the distribution center/warehouse, I put \$1.00 in my pocket.

What do I look for in distribution operations?

The **cost per line** is the absolute key measurement, and you should be looking at that on a daily basis. Do you know what it is right now? That's where you start. Use it as

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your benchmark and say; “I’m going to drive that cost per line down!” Yes, it’s the key measurement in any distribution operation.

Now this doesn’t mean that we don’t pay attention to fill-rates or order or inventory accuracy. There are surely costs and “heartache” incurred when you fail in these areas; backorders, post-order correction of errors (some say it costs \$50 to \$300 to fix an error), late delivery, etc., etc. These can easily evaporate your profit. It takes even **more** sales to offset these drains on profit – never mind the customer service impacts.

So let’s talk about labor

I typically discuss labor as being two different entities; productive and nonproductive. Pickers, receivers, etc., are usually doing something (although many could be doing it better – being more efficient maybe). They’re carrying something; they’re processing an order, this and that. Yet, I often see “inspectors” - a sure sign that says; “I give up - I can’t make my operations better, so I’m going to inspect accuracy into product, inspect accuracy into the order, etc. - I’m going to validate what somebody has already done all day long”.

Truthfully, “supervision” is not always non productive, but usually a product of an expanding labor force, a late(r) shift, a night shift, etc. Supervision ends up growing because other things aren’t working properly, rather than limiting the amount of supervision because you have systems in place that will drive and validate operations. Do you really need someone walking around with a baseball bat trying to correct issues?

Things you can do to reduce cost per line

First read our recent whitepaper - *It’s a Game of Minutes...in Your Warehouse – DC, So Don’t Rely On Your Step Child for Efficiency*. It’s a ‘deeper dive’ and describes several things that you can do that directly impact **cost per line** – regardless of the size of your company. It’s available at: www.mcaassociates.com

So play in the financial arena

So again, start measuring “*cost per line*”. Just saying; “I did ‘x’ amount more orders today” actually could get you in hot water. What did it really do for the company? It’s a

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deceiving type of concept because in distribution, we tend to think in terms of statistics and not convert them into financial terms.

I suggest that ultimately you'll find yourself wanting to get even more granular - beginning to look at this in different departments; receiving, picking, put-away and bin replenishment, etc. Maybe, you'll even find yourself, one day, measuring "*time-on-task*" (well, that's another subject... for another day!).

Finally...

Unless you bring your distribution operations into the financial arena, they'll be no financial impetus for change. You just won't be playing in the arena that companies are driven by.

You need to demonstrate that you can...pull a profit.

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