

Bill's Building Blocks

Performance Measurement Starts with a Plan

The raw material warehouse seemed full, and it was taking longer to put away the daily receipts. But raw material inventory normally turned so slowly that it was hard to convince folks that something was wrong. We went to Staples and bought “months of the year” inventory labels. A label was pasted on the outside of every carton before the carton was



put in the racking system. Pretty soon anyone walking through the racks saw “May, May, May, May, May, Apr, May, May, Apr, May,…” and the case was made.

From Bill's Building Blocks four articles ago, lastly as supply chains restart...**Measure startup performance using diagnostics to find and correct issues** – This is the application of key performance indicators to measure network throughput, landed cost, inventory turns, and ROIC against planned expectations. This is validation that the redesigned supply chain can achieve its expected performance and still be tolerant to the risks of demand uncertainty, supply variability, and cash illiquidity.

Demand forecasts convert to order backlog then convert to shipments. Depending on the rules followed by your business, revenue recognition either occurs at the time of shipment or at the time the customer's invoice is paid. Once paid, shipments become throughput. When revenue is not up to plan, determine if the throughput is being demand limited or supply limited. Then take appropriate action.

Profitability starts by having a landed cost budget. When period expenses exceed their targets, find the root cause. Review rework labor hours, material pricing increases, and/or excessive logistics costs. This is difficult because cost reporting occurs well after the fact.

Have an inventory turns budget. Inventory turns can be monitored by marking the time between the receipt and issue of a few key 'A' item raw materials and a few of the most profitable finished goods. Set a nominal limit on the total cubic space allowed in the warehouse for slower turn 'B' and 'C' items. When this cubic space is exceeded, determine the root cause. Too much inventory means too little cash.

Performance measurement starts with a plan for expected throughput, landed cost, and inventory turns. The closer to real-time measurement the better the performance.

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