TURN CONTINUOUS IMPROVEMENT INTO CASH FLOW

JASON FURNESS

Have you ever sat through a business unit review and been told how much efficiency will be improved if you approve the investment in new machinery? Have you ever been told how much labour utilisation has gone up due to the latest continuous improvement projects? Have you ever then gone to the end-of-year financials to see the bottom line impact and found no impact at all?

How can it be that we can invest so much time and money into improving and achieve sometimes tiny financial results?

In order to answer that question, first I'd like to introduce you to quite a different concept to describe the operations of a business.

To begin with, let's look at the primary activity of a business. Firstly, let's accept that safe operation in all areas is a given. This is just a fundamental principle of business in the modern era. Also, I would like to take as a given that all legal compliance issues are being followed. These are fundamental parameters all of us should always operate within.

The primary activity of a business is to make money. Make money not just today, or next month, or next quarter, but also into the distant future. A sustainable business must make money now and into the future.

A sustainable business must make money now and into the future.

Making more money now and sacrificing the company's future is not a sustainable methodology. More money now and into the future, this is really what we want to be doing.

Notice we are talking about a business, not a factory, or a sales division, or a logistics function, or any other individual unit, but the business as a whole. This is one of the key distinctions I would like to make.

The concept I would like you share with you is to think of business as a chain. In a chain we've got individual links joined together to form the length of chain. In this analogy, the individual links are individual functions or business units, or even pieces of machinery. Joined together they form the business. So we have a link for marketing, a link for sales, a link for logistics, a link for manufacturing, a link for distribution, and a link for financial collections. This chain also has a link for the end user and links for the suppliers, right back to the raw materials. Remember, all of those chain links are connected.

Now in a chain, the amount of weight or load a chain can carry is defined by what? It's defined by the weakest link. We all know that. There've been TV shows about it. We've all grown up with that metaphor, that's why it's a good one. In a business, the equivalent measurement to the strength of the chain is the cash flow of the business.

In summary:

- Individual links represent departments.
- The chain represents the business.
- The strength of the chain represents the cash flow of the business.

So the performance of the overall system, the strength of the chain, isn't determined by how strong each individual link is, it's determined by how strong the weakest link is. Now this is an important distinction, particularly as in larger businesses we often treat each individual link as an individual department.

We may give them individual measurements and other performance KPIs, and we run on an assumption that if we improve the performance of each individual link at a local level, then the individual performance improvements will all add up and we will have improved the performance of the overall chain.

I would ask you to consider whether this assumption is valid, or is it fundamentally flawed?

The overall chain will only improve its strength if the strength of its weakest link improves.

The overall business will only improve its cash flow if its weakest link improves.

Spending money to improve the local performance of any department when it is not the weakest link is like making an individual link of the chain stronger but leaving the weakest link untouched.

- Will the chain carry any more load? No!
- Will the business generate any more cash? No!

Focusing efforts on improving departments that are not limiting the cash flow of the business is almost a waste of money, time, and effort. You may be able to reduce your operational expenses. You may be able to improve your efficiency; you may be able to improve your scrap. The impact on your bottom line performance for the business is negligible.

Your largest return on investment for your improvement efforts can only occur if the improvement effort is focused on the weakest link of the business as a whole.

If you look at the individual departments inside your business, people will tell you that they have great projects to improve that will save money. These projects may make life easier, may be desirable by the people in that area. The key question is:

Is this the highest ROI use of our precious cash, and even more precious management time?

There are many projects that improved local measurements. Fine! I'm glad it made your life easier, but did it really contribute to improving the bottom-line performance of the enterprise, when we measure it through the overall performance?

If the performance improvement did not show up in the bottom-line financials, then it was a mirage all along!

Go and have a look at your own business, I'd be very, very comfortable in saying that if you added up all the cost savings you supposedly had when you measured it at individual department level, and then you went to look at the bottom line of the global enterprise, you won't find it there.

What do we do differently in the future?

I am going to take you through the 'Five Focusing Steps'. This is work that originates with Eli Goldratt, the author of 'The Goal'. If you have not read this book I recommend you go and grab one. I was given this book at the very start of my career back in 1991, and I have given a copy of this book to every management team I have led in my two decades in manufacturing.

The Five Focusing Steps

Step one: identify

What you and your team can do first is to ask yourself: "Where is the weakest link in my chain?" Identify where in the system the flow of money is being blocked up. Remember the chain analogy that encourages you to think of the business as the entire system. Some common examples include:

- A certain machine within a factory.
- Marketing can be a weakest link on the money flow of the business if there are insufficient sales.
- Customers.
- A specialist skill set.
- Labour.
- Shipping.
- Suppliers.

A clue to help you find this weakest link is to look for the most heavily loaded resource, look for where inventory of work piles up.

Step two: exploit

In step two, we want to maximise the output from our weakest link using the resources we have already invested in it. Change the way you run it so as to maximise its output. We are increasing capacity by wringing all of the output we possibly can from the process as it currently exists. Run this task longer, change the tactics you use. Apply whatever continuous improvement tools (Sales Training, Lean Manufacturing or Six Sigma) you have to improve the output of this process. Often exploiting the weakest link is enough to make a significant improvement in the cash flow of the business, if the weakest link is internal to the business.

Step three: subordinate

Subordinate means changing the priorities of the organisation. This is the trickiest part of the process, as it is very difficult to break the old culture of whose is the most important function. The whole organisation must change its behaviour to support the weakest link. What is easy for the weakest link is the most important thing, and this often means other parts of the organisation may have to wait, share or give up resources, change operating policies, etc. Successfully implementing subordination will lead to another upsurge in cash flow, if the weakest link was internal to the business.

Step four: elevate

If there is more improvement desired or necessary, we then look to elevate the weakest link. Elevation means that we seek to raise the capacity even further by adding capacity by finding another machine, person, whatever it takes, as long as any increase in investment or expense is less than the increase in gross profit generated. This is the only stage at which you should consider investing your precious capital, not before.

Step five: don't let inertia set in

Often steps one to four are sufficient to strengthen the weakest link and achieve a breakthrough in performance. To develop and then maintain a sustainable competitive advantage, an organisation must always be looking to improve. Celebrate your success and then go back to step one – identify, and repeat the cycle.

Jason Furness is the CEO of TheManufacturingMentor.com. For more information call 1300 226 121, email Jason@TheManufacturingMentor.com or visit www.TheManufacturingMentor.com. *mhd*