

NuTerra Strategies Case History

Tier 1 Supplier – Hidden Value Demands Exposed a Value Chain Synchronization Solution

A recent Deloitte & Touche study revealed that fewer than 10 percent of mid-market companies are market aligned and those that are experience robust profits and consistently out perform their competitors both in top line growth and margin.

Recently, in the OEM market, we helped a Tier 1 supplier uncover the hidden value demands of its OEM customers. The Tier 1 supplier was growing but its margins were shrinking. The leadership team believed if they diversified their customer base they could find new customers that were more profitable to balance their portfolio. What we uncovered was the OEM's were suffering a very similar problem. They too were battling shrinking margins despite robust growth. They were trying all kinds of ideas but nothing was working. They had done Lean and Six Sigma and had squeezed out every dollar of waste internally that was possible. They had moved all the parts production offshore they could, but that strategy was actually creating higher costs.¹ All they had left was to force their suppliers to cut costs. Thus, our client was being pressured to cut prices despite its own shrinking margins.

Rather than focus on finding a way to make the same product cheaper (a classic product centric approach), we looked into where the OEMs costs were occurring. Sure, they had Lean and Six Sigma, but they still had a progressive problem. What was interesting was that as their top line revenues grew, their costs grew faster. At some point in the future, they were literally going to outgrow their profitability.

So where was the cost? It turned out to be the cost of the infrastructure required to manage their huge parts inventories. As part of Lean, they committed to managing parts inventories to the lowest level possible. However, they literally managed thousands of parts in bins stacked floor to ceiling all along their production line. The task of managing this inventory at all was Herculean, but to manage it to the lowest level was impossible. As a result, they would regularly run

out of parts. Every time that happened, production would grind to a complete stop. The cost of these shut downs was enormous. The heat was turned up on the OEM inventory managers who were already overworked and understaffed. To solve the problem they shifted the burden downstream and forced suppliers to regularly ship product same-day or overnight when bins would run empty. That solution failed to stop the shut downs plus it added more cost by doubling the cost of parts.

The hidden value demand? The OEMs needed to eliminate their inventory management problem. They simply lacked the staff, the technology, and the power to control supplier production adequately to rein in costs - not the costs of the parts themselves, but the costs of managing them. But no Tier 1 suppliers were offering that type of solution, so the OEMs remained frustrated for two reasons:

1. *Their costs were out of control*
2. *They had no idea what was causing their high costs or how to control them*

This represented a huge market vacancy for our client. We helped our client design a unique program that went far beyond the opportunistic “vendor managed” solution. They brought a complete solution to the OEMs that eliminated their inventory management costs related to our client's products. Plus our client received added benefit by gaining a predictable forecast for production rather than constantly reacting to client demands. The effect was a dramatic reduction in costs and increased margins both for the OEMs and our client.

How did the OEMs respond? One made our client “Supplier of the Year” following the initial presentation, while the others increased their “spend” with our client by a minimum of 30 percent the first year. But most important, our client's margins improved dramatically.

¹ For more on this topic, email NuTerra Strategies LLC at info@nuterrastrategies.com.