“THE LUNCHEON”

Lunch with the chairman of the board was a monthly ritual to which all of the senior managers were invited. It appraised the chairman of progress within the company and it gave him an opportunity to "address the troops". This lunch was no different to any others, except that the chairman brought with him a guest whom he introduced as an "adviser". The guest was a greying man in his middle fifties who was wearing a suit that seemed to belong to a previous era.

Lunch had gone quite amiably with the chairman hearing about the successful introduction of the new product range and the indications of an increase in market share. During coffee the usual silence fell over the room which was the cue for the chairman to "sum up" and deliver his normal "state-of-the-nation" address.

"The board is very pleased with the progress made with our products and shares your optimism regarding potential growth......." He went on to praise all that he had learned during lunch and his morning visit. Despite this, everybody in the room sensed that there was something wrong.

"However,"…. the chairman continued; "....the board and the company's shareholders are concerned about the amount of shareholder's funds that are tied up in the business. Our return on investment is far below what can be expected from an enterprise such as this"

The term "return on investment" was familiar to every manager in the room but few knew precisely what it meant or how it was determined.

"You will notice from the balance sheet the very large amount of shareholder's funds that are tied up in inventory". With the exception of the finance manager, and possibly the general manager, nobody in the room had any understanding at all of the balance sheet. But all present were aware of the finance manager's pre-occupation with inventory and his pleas for it to be brought under control.

The chairman turned to the man in the out-of-date suit and invited him to comment on the question of this inventory.

"It represents about four months of material in sales" he said without referring to any notes.

As a question which seemed to be addressed to the assembled group the chairman asked; "Why do we need four months of stock hanging around in the store?"

The G.M., who was not prepared for a discussion on inventory in these terms offered: "Our market strategy is based on very short customer lead times.

Most of our purchased material has much longer lead times. We have to buy just about everything against forecasts."

The chairman invited comment from the man in the outdated suit with no more than a beckoning glance,

"Who writes these forecasts?" the guest inquired.

"Each of my sales people maintain a forecast file which is used to set sales budgets" volunteered the marketing manager.

"If I purchased against those forecasts, two-thirds of what we purchased would never be used,"..... declared the supply manager, who could see that he was already implicated in this,…….."those forecasts are only used as revenue guides."

Now clearly leading the discussion, the luncheon guest asked the supply manager how he actually determined, in that case, what was to be purchased.

"My people buy from experience and are guided by direct requests from the sales people." replied the supply man who was mentally preparing a defence by shifting the blame back to marketing.

"In other words then, the supply team writes the forecast by default" offered the lunch guest.

"I guess so" agreed the supply man, satisfied with, at worst, no more than a share of the blame.

The lunch guest then asked if any measurements were taken to determine the accuracy of forecasting to which nobody seemed to have any reply, except to agree that the accuracy was generally "pretty awful". When the man in the outdated suit asked if anybody set the safety stock levels according to the "awfulness" of the forecast accuracy for each part, nobody ventured an opinion. The purchasing manager did acknowledge that one of his junior P.O.'s was doing an APICS course which covered this kind of thing.

In an attempt to relieve the pressure from those in the room by implicating previous management groups, the marketing manager declared "In actual fact, the 'operational' stock turns over fairly quickly, redundant stock is the biggest component of our inventory."

"From what we've learned today, I'm not at all surprised!" replied the guest with a wry smile directed towards the chairman.

"It seems, gentlemen,"…… rejoined the chairman, who had been listening intently to the exchanges,…… "that the biggest problem facing this business at the moment is being addressed entirely by your subordinates, who's methods seem to be unknown to you and who are apparently proceeding with very little guidance"

In 1987 this Australian manufacturing company was closed. Its 90% share of a growing market in the leisure industry is now in the hands of importers.