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## IS THE WAREHOUSE OR HUB A REAL CUSTOMER?

In extended supply chains, and even in individual companies, I often hear the remark, "The warehouse is our customer." This usually means that responsibility for demand and production (or procurement) is separated. All customer demand arrives at a central point and is managed by the people there. They order from Production the net requirement to replenish inventory in the warehouse.

In this organizational setup, Production sees as demand only the quantity it is supposed to deliver to the warehouse or hub. Production does not see the true customer demand that the warehouse must deliver to intermediate or final customers, and Production does not see either the inventory of its products in the warehouse. In particular, the Master Production Scheduler at the factory does not see whether true customer demand on the warehouse is covered or not.

Having the warehouse (or stockroom) as a customer adds a level to the supply chain, which violates two of the principles of Supply Chain Management:

1. **Visibility:** the expected flow of future demand should be accessible to the people responsible for covering it; and
2. **Disintermediation:** the suppression of intermediate levels of management which add no value for the final customer. The well known example of « Internet-based disintermediation » is Amazon, whose elimination of intermediaries between the customer and the supplier in the downstream supply chain, has inspired a raft of imitators.

In his book The Agenda, Michael Hammer says, " In the customer economy, we must stop thinking of a distribution channel as a series of individual entities...we need to see all players in the distribution channel as partners and participants in the work of satisfying the final customer's needs."°° The difference is between « *sell-to* » (where the warehouse or stockroom is the customer) and « *sell-through* » (where the real client beyond the warehouse is visible):

### « SELL TO » VS. « SELL THROUGH »

1. **Distribution often acts as a screen, and the company doesn't see or even know its real customers and their real demand**
2. **Production knows everything about the product and next to nothing about the customers.**
3. **Distribution knows everything about the customers and next to nothing about the products**
4. **Recommendation: show true demand to the people responsible for covering it with production**

A better solution to the "sell-to" approach which blinds the factory or the supplier, is to show in the factory's Master Production Schedule or Final Assembly Schedule (1) the customer demand coming from the next downstream node in the supply chain, and (2) the item's current physical inventory at that next downstream node. That way the planner can insure that the MPS or FAS plans enough production to cover the customer demand.

A "hub" or logistical platform may be managed differently from a simple stockroom. Many multinational companies have brought back from their affiliates the inventory that used to be stocked there and put it into "hubs" or major distribution centers, one serving the north of Europe for example and one serving the south. A hub may be considered to be a legitimate node in the supply chain or a legitimate bill-of-material levels in DRP<sup>°°°</sup> if:

1. having the hub helps the company to present one face to the customer
2. many production sources deliver to the hub, and
3. the hub is located far from a factory

If one of these conditions prevails, the hub may be considered to be an customer in the supply chain. But the decision to do so is not automatic. The problem of furnishing visibility of true customer demand to the factory making the products, remains. For capacity planning and for new product development, the factory should be informed of demand. If the traditional channels for seeing demand get closed because of the creation of the hub, another path will have to be created, perhaps through the S&OP process<sup>°°°°</sup>.

This discussion links up with the theme of our Technical Newsletter No. 31, "Advancing to the Past", which showed the defects of the order point technique, which is often used these days for replenishing a warehouse or hub. The Letter gives an example of correct planning in a supply chain with one or more hubs, as well as their integration with Lean for pulling replenishment.

In conclusion, is the warehouse a real customer? Probably not. Is the hub a real customer? Maybe yes. Real clients are sacred, and we don't want to push them farther away in the supply chain. Rather, they should be moved closer to Production and Development, through the elimination of intermediate stages.



*Visibility and disintermediation!*

- ° « hub »: center of a wheel to which the spokes are attached
- °° Hammer, Michael, *The Agenda*, Crown Books, p.161 – 162.
- °°° DRP: Distribution Resource Planning
- °°°° S&OP: Sales and Operating Plan