Tuning ERP and the Supply Chain for Profitable Growth

Three things every CFO should know about the organization's SCM and ERP systems

White Paper

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VENTANA RESEARCH

Aligning Business and IT to Improve Performance

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Table of Contents

Visibility Needed

In all companies a close link exists between information technology and an organization's ability to execute business efficiently and effectively. This is especially true for midsize organizations, which Ventana Research defines as those with 100 to 2,500 employees. Our research consistently shows that most chief financial officers and other senior finance executives in these companies fail to appreciate this link sufficiently, and therefore are not aware of – or, if they are, may resist – the need to make changes to their core financial systems.

Finance executives are understandably reluctant to make major changes to these critical systems because the process can be time-consuming and expensive. For this reason, they tend to delay any changes for as long as possible. Ostensibly, such a conservative approach reflects a reluctance to put the business at risk if the transition is less than smooth. But a thorough cost/benefit/risk assessment should reveal whether changes in core financial systems are warranted and what those changes may entail.

In both its client engagements and its research, Ventana Research has observed that well before financial systems become "broken" to the point where they threaten the orderly conduct of day-to-day business, they usually become increasingly costly and risky to the company. Usually, these growing problems are concealed by the hard work and clever adaptations of employees. Unfortunately, as a result of these well-meaning efforts, opportunities to maintain and perhaps even improve the company's profitability and competitiveness are lost. In most instances it is only when a crisis develops that company management is able to see the risks and true costs of an aging financial system. Indeed, even with the red light flashing and the alarm sounding, the link between the emergency and the inadequacy of the organization's core financial systems may not be evident to senior executives.

The supply chain is, of course, the primary processing mechanism of every manufacturing company. But in today's competitive, cost-conscious global environment, it's more than that: The multifaceted, multi-company, multinational structure of the supply chain makes it the most complex management challenge found in any enterprise. Supply chain management (SCM), a critical part of any enterprise resource planning (ERP) system, no longer means just making sure that the right materials and resources move to the right place at the right time. Today, it also means ensuring that the sequences of events involved in producing goods and distributing them to customers are tuned optimally to satisfy customers, minimize costs and maximize profit.

For these reasons, we believe CFOs must become actively involved in analyzing their ERP/SCM systems. They should investigate to determine if their core financial systems are adequate in three key areas to support their business. These areas are:

- Supporting a lean supply chain
- Enhancing supply chain visibility
- Enabling globalization of a company's infrastructure.

Failure to address opportunities and gaps in the organization's financial and operational IT systems has the potential to impact negatively a company's costs, risk exposure and competitiveness.

Supporting a Lean Supply Chain

Ventana Research defines a lean supply chain as a set of organizations and processes that are linked in a continuous flow of products and services, finances and information, and that interact collaboratively to reduce cost and waste. Most people in manufacturing are familiar with the idea of "lean" manufacturing. Its foundations are in the Toyota Production System (TPS), which helped turn Toyota into an industrial and automotive giant. Many manufacturing companies worldwide have imitated TPS and now use lean production techniques to pare costs and to speed delivery.

In its simplest form, lean supply chain means producing goods with less; it applies fewer resources to the production process without affecting the quantity or quality of the goods produced.

Demand management is easily the most critical component of the lean supply chain because inappropriate production of goods is the source of much waste and expense. The key to effective demand management is to define customer value. Customer value comes in the form of the physical product itself, as well as its location and the timing of its delivery. Once those three items are clearly determined, a company can begin to set up a signaling system that will inform the supply chain of the state of product demand, thereby pulling, rather than pushing, products through the supply chain.

Creating and managing a lean supply chain requires the appropriate tools and technologies. Depending on the company and its needs, these could range from a basic kanban system – a signaling system used in just-in-time (JIT) manufacturing – to an entire refreshment of company's enterprise resource planning (ERP) and supply chain management (SCM) technology.

Enhancing Supply Chain Visibility

The complexity of today's international, multifaceted, multiple-partner supply chain makes creating a visible information environment to support it both difficult and necessary. Clearly, managing a supply chain requires information, but exactly what that means is not obvious. Merely pushing information about partners or products into a report that lands on a manager's desk every day will not achieve the goals. Nor will a dashboard, even if it delivers that same information in real time.

What today's supply chain managers need instead is an information environment that makes a supply chain visible. Visibility, in this case, means that systems and processes are in place to deliver supply chain data in a way that enables managers to know whatever they need to know whenever they need to it, at whatever level of detail they need, and that allows them to analyze the data and take action based on the results of their analysis. The essence of supply chain visibility is the ability to know the location and status of all physical components, from raw materials to finished goods, as they move from suppliers through the stages of production to delivery to customers.

Defined this way, supply chain visibility is a tall order, but some of today's IT systems can meet it. A visible supply chain can be implemented by using technologies that are readily available and in many cases are already in place in manufacturing enterprises, such as the ERP system and specialized SCM software. To

make these technologies work in a visible supply chain environment, key technologies must be added to the mix: dashboards, portals, electronic data interchange (EDI), business intelligence (BI) and other tools that can track materials and product flow in the supply chain.

Context and collaboration are also important elements in supply chain visibility. Context is especially important in today's information-rich enterprise environments because it is easy to overload users with too much data, from too many sources, with too little context of how it relates to other data and business processes and activities. Most business decisions today require collaboration, so visibility also requires that the information be shared among colleagues. Finally, a visible environment is complete only if it also enables users to act on any decisions that are made.

Enabling Globalization

In the last few years, more and more manufacturing and service companies have entered international markets and globalized their supply chains. As a result, the traditional concept of a domestic company – that is, a single company operating within a single country, even though it may export some products – no longer fits today's midsize or large businesses. The business processes and IT systems companies use to manage their operations need to reflect this fact.

Most companies have an ERP system in place to handle their transactional processes, but such a system often is not enough to address critical global issues involving supply sources, manufacturing plants, service centers and markets. ERP systems typically are designed to support complex business processes occurring in a uniform, integrated environment. This is especially true for companies that installed their ERP systems before going global. Globalization can have serious impacts on key business processes, and SCM and ERP systems must evolve to address the needs of an international company.

Adding even one additional country to the operations of such a business is likely to disrupt, if not destroy, the commonality that enables its ERP system to operate as an integrated environment. In that case, the ERP system loses uniformity of geography, of currency and of measurements, and often loses the singularity of systems. That is because the company will likely also gain at least one network and one distant data location. More to the point, the company now is likely to be operating using an additional ERP system, perhaps from a different vendor.

Without changes to its ERP strategy, an organization expanding globally will not be able to manage its operations efficiently. Recurring obstacles eventually interfere with the company's productivity and profitability, and they may undercut the ability of the company to meet regulatory and other compliance requirements. If this continues, the company may fail to realize the cost reductions and other business advantages that were its reasons for adding overseas partners to the supply chain in the first place.

To manage international operations effectively, a CFO should work with IT to ensure that the company's ERP system can support an international supply chain involving a global network of partners and that links supply resources, components,

manufacturing facilities and markets for finished products around the world into an integrated environment.

Such as system should also have a distributed architecture that can produce sourcing and production schedules to take advantage of the cost and time efficiencies specific to each location, than can synchronize information between manufacturing plants and product management groups and that can aggregate financial results into consolidated financial and management reports in a timely fashion.

Finally, this system should have internationalization capabilities that support user interfaces in English and local languages, automatic translation facilities, local currency and measurement units and local regulatory and financial reporting requirements.

Making It a Reality

Although there are certainly other issues CFOs should consider addressing as well to improve company performance, this white paper focuses on the supply chain and globalization because, in our experience, this is where some of the biggest opportunities – and biggest risks – exist for companies today.

If you agree, we recommend assembling a cross-functional team from finance, operations and IT to assess the need to make systems changes in response to the imperatives identified above. The team should start by identifying the performance drivers for your business that have the biggest impact on cost, competitiveness and business risk. We advise directing the team to pick at least three, but not more than 10 issues.

The next step is to benchmark to find best-in-class capabilities for these drivers, looking not just at direct competitors but also at companies that are in similar businesses. Information on successful benchmarking can be found in books and on the Web; Ventana Research can offer guidance as well.

With benchmarks in hand, the team should proceed to identify where gaps exist between them and your company's capabilities. Assign priorities for addressing these gaps based on their magnitude and their immediate and strategic impact on the company.

Finally, develop an action plan. Be sure to understand the role of IT in supporting changes in business processes and the information necessary to support this plan.

Fully appreciating the link between having the right information technology assets and a company's ability to compete and drive profitable growth has become increasingly important as ever more companies incorporate SCM and ERP into their basic business processes. Ventana Research advises CFOs to ensure their company has the right tools for today's competitive climate.

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