

Rx For Cabinetmakers

For the first eleven months of 2006 housing starts were down 12.5 percent vs. the same period last year. Cabinetmakers that supply homebuilders are crying the blues. With existing home sales off 11 percent, those cabinet producers who sell via the remodeling channel are also susceptible to these housing woes. Those in the know claim the cabinet business is off 10+ percent.

So what is a poor cabinetmaker to do? Here is one man's answer. Keep perfecting your business:

■ **Invest in engineering expertise** – Product lines are getting more complicated. The line between furniture and cabinets is blurring as finishes get more complex and more cabinet configurations are developed. At the same time, buyers continue to demand faster delivery. The industry employs only 500 engineers in total or one for every \$34 million of annual shipments. Compare that to the computer equipment business at one engineer per \$2 million in annual sales.

■ **Focus on process improvement** – During the recent ten-year run of solid

growth, most cabinetmakers have worried more about filling orders than optimizing their processes. The top line took priority over cost performance. Little time was left for revolutionary changes in the cabinet value chain. A slower pace of business is a good time to look inward and make your operations more efficient. Band aids over process weaknesses must be converted to longer-term remedies.

■ **Maintain the pace of capital investment** – Over the last 10 years, investment in technology has increased as a percent of annual cabinet sales. Those funds have strengthened the competitiveness of the U.S. industry resulting in higher labor and asset productivity as well as faster time to market. These improvements have enabled a strong defense against foreign-based competitors. Now is not the time to back off. The trajectory of Chinese cabinet exports to the U.S. is worrying. That graph

looks suspiciously like the early days of the home furniture export boom there. Anecdotal evidence is showing that some Chinese furniture makers, in the face of overcapacity there, are looking to convert their plants to similar wood products. Some no doubt will shift to cabinets and components.

Business will certainly turn more competitive. But the best cabinet producers have never run from a challenge. Increasing demands for product customization have been met with remodeled plants, slashed inventories, and faster deliveries. These changes were nothing short of revolutionary.

Bottom Line – Mr. Cabinetmaker, don't stick your head in the sand. Keep your bias for change alive even in tough times.

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Is More Productive Labor Enough?

“The only way to turn a profit has been to drive unit labor cost lower.”

Over the past 25 years U.S. manufacturers have generated annual productivity gains averaging 4.1 percent. That performance put the U.S. in the world's top five as measured by output per labor hour.

This accomplishment has saved the skins of many cost-cutting manufacturers. Over the past ten years prices for manufactured goods have increased by only four percent. Meanwhile prices for construction and health care – two essential production inputs – have jumped nearly 60 percent. By and large, prices for most manufactured goods are set by the lowest cost producers who are located in places like Shanghai or Munich. U.S. producers therefore have little, if any, pricing power. The only way to turn a profit has been to drive unit labor cost lower.

A good example of this predicament is the U.S. wood furniture industry. Competition from overseas has brought declining prices. That is good for consumers but bad for producers who are unable to keep pace. Given the labor-intensive nature of furniture, no amount of capital investment would have improved production economics sufficiently to save the U.S. industry.

But labor is not the only cost that manufacturers confront. A recent study by the National Association of Manufacturers (found at www.nam.org) revealed that U.S. producers face a significant cost disadvantage beyond wages. External factors - taxes, worker benefits, litigation, energy, and pollution abatement - add 31.7 percent to U.S. costs vis-à-vis our nine major global competitors. These costs are beyond the control of company management. No amount of internal cost cutting will correct that disadvantage.

Manufacturers must therefore look beyond headcount reduction as a means to lower costs. The focus now must be on two other factors:

■ **Asset Utilization** – Getting more output from plant and equipment.

■ **Responsiveness** – Recognizing demand shifts and adjusting output quickly to avoid building inventory.

The former can be improved by better maintenance, shop floor control, quick set-up equipment, and multi-shift operation. In the future, a single shift operation will be a rarity.

The latter requires the implementation of accurate forecasting systems, de-

mand-pull logic, and empowerment programs for front line workers. Tuned-in plant floor workers can positively affect labor and asset productivity.

The promise of lean manufacturing, Six Sigma, and other leading edge practices still exists for many U.S. manufacturers. Few U.S. firms can claim to have completed the journey to lean. Most are only 10 percent there.

Even Toyota is worried about its competitive edge. Other motor car companies have copied much of Toyota's vaunted Production System. As a result, their cost and quality advantage has narrowed. The practice of *kaizen*, a focus on incremental improvement, is now seen by senior management as insufficient. Toyota leadership now espouses *kakushin* or revolutionary change. Their goal is audacious – cutting \$1,000 from the cost of every vehicle. The solution involves radical redesign of their manufacturing value chain from the plant floor up and throughout their supplier network.

At the end of the day, it's all about management. Any business advantage can be competed away. To stay ahead of the pack a company must constantly

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Business Quote...

“Great ideas have always encountered violent opposition from mediocre minds.”

Albert Einstein

“Today only one out of eight U.S. workers is represented by organized labor.”

Are Labor Unions On the Rise?



Golf Quote...

“Golf is a lot like life. When you make a decision, stick with it.”

Byron Nelson
(1912-2006)



Philosophy Quote...

“A man is not old until regrets take the place of dreams.”

John Barrymore

Today only one out of eight U.S. workers is represented by organized labor. But every day the business news includes the story of labor unions' relentless attack on Wal-Mart, the world's largest retailer.

As the Wal-Mart situation confirms, manufacturers, whose ranks account for only 16 percent of the U.S. work force, are not their target. Instead, unions are going after the 42 percent of workers in the burgeoning service sector. Last July the Service Employees International Union (SEIU) led a coup by leading 4.6 million workers out of the AFL-CIO, the largest U.S. labor organization. The SEIU is the fastest growing union in the U.S.

Most service employees work in jobs that are relatively protected from the threat of outsourcing. Unlike manufacturers, the service sector cannot easily replace U.S. workers with lower cost Chinese. Union organizers understand the leverage that situation creates.

The globalization of business also enhances this leverage as the labor move-

ment becomes more international in reach. More than ever businesses are dependent on foreign suppliers and complex supply chains to generate their product offerings. This dependence comes with a price – the risk of disruption in supply chain links beyond a company's control. A union like the SEIU with memberships around the world could outsource a strike against a U.S. company by paying Indian workers in its supply chain to walk out. This type of action is part of the SEIU's strategy.

At the top of the unions' wish list for the 110th Congress in 2007 is the Employee Free Choice Act. This law will require employers to recognize a union after a majority of its workers sign cards authorizing union representation, a so-called “card check” election.

Such a ballot is non-secret and historically has been preceded by union threats, coercion, and the like to get workers to sign. This law, if passed, threatens the flexibility that underpins the U.S. economy.

To confront this threat U.S. businesses themselves must unite. Labor-related problems like the high cost of health care benefits require the combined thinking and effort of every business operating in the U.S. as well as lawmakers on the state and national level. Trade associations like the National Association of Manufacturers and the Kitchen Cabinet Manufacturers Association are good vehicles for initiating this dialogue. Individually every business must work to persuade workers and consumers alike that its objective is not short term profit at the expense of its work force.

Bottom Line – The pendulum that has been swinging business' way may soon be reversing course. Understand the risks of a changing labor landscape, get involved in their mitigation, or suffer the consequences. The choice is ultimately yours.

Source: *The McKinsey Quarterly*, 2006 Number 1, *Investors Business Daily*

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perfect its processes. That task requires innovative thinking, capital, a tolerance for risk, and most of all, a bias for change.

Bottom Line – If Toyota, soon to be the world's largest car maker, is worried about total productivity, you should be too.

Sources: *The Wall Street Journal*; *Managing Automation*, December 2006, the National Association of Manufacturers

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This newsletter is made possible by earnings from the world's forest products - the only renewable natural resource.

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“Providing contemporary furniture at affordable prices fuels Ikea’s success.”

Swimming Against The Tide

All previous issues of *The Wood World Monitor* can be found at our web site:

<http://www.raymondnet.com>

Any issue may be downloaded in Adobe PDF format for easy printing.

While the pace of plant closures in the U.S. furniture industry continues, world no. 1 furniture retailer Ikea is building its first U.S. manufacturing plant in Danville, VA. Operated by its Swedwood subsidiary, the 810,000 square foot facility will open in early 2008, employ over 700 workers, and use leading-edge technology to supply the company's 28 U.S. and 11 Canadian stores. The Netherlands-based company has plans to open three to five new stores in North America annually.

Ikea is a cult brand among young furniture buyers around the world. Last year over 410 million shoppers visited an Ikea store to choose from over 7,000 items. As *Business Week* put it, Ikea provides “a one-stop sanctuary for coolness”.

Providing contemporary furniture at affordable prices fuels Ikea’s success. Their relentless focus on cost cutting aims to lower prices across its product line by two to three percentage points every year. Lower

prices mean higher volume, and nothing trumps volume in achieving production efficiency.

Ikea is proving that dedication to great product and process engineering brings results even in the design-crazy world of furniture. And apparently Ikea believes that manufacturing near your market makes economic sense, too.

A.G. Raymond & Company is proud to be a member of the Ikea/Swedwood project team.