Introduction to the Theory of Constraints

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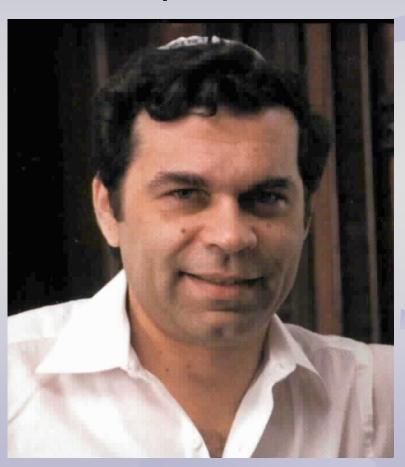
Czech Republic

Introduction

Theory of Constraints - TOC) was formulated approximately in 1980 in the USA. Some important roots of this theory were connected to the ideas incorporated in programs for planning and production control (Optimized Production Technology)

Introduction

Author: Eliyahu Moshe Goldratt



The Goal by Eliyahu Goldratt

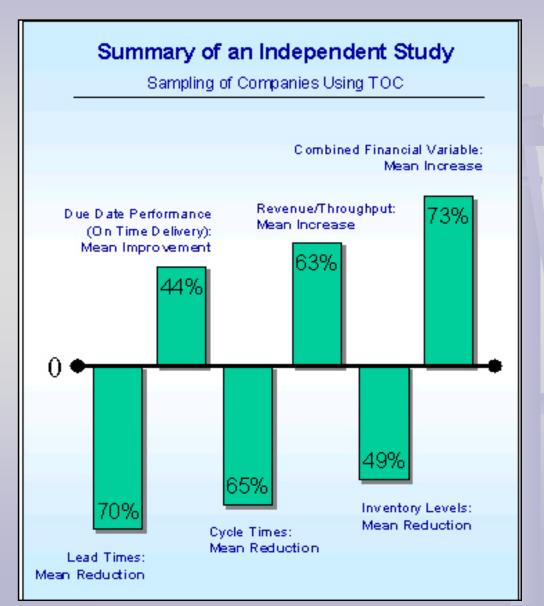
The goal of a manufacturing company?

Make money !!!

Introduction -novels

TOC has became popular particularly thanks to the novels:

- The Goal A Process of Ongoing Improvement
- It's Not Luck
- The Race
- The Critical Chain
- The Haystack Syndrome
- Necessary But Not Sufficient
- Late night discussion
- TOC was together with TQM (Total Quality Management) and JIT (Just-In-Time) classified as one of the most important managerial methods of the last two decades of the twentieth century.



Ford Motor – Electronics Div.

Revenue: \$3,000,000,000

Number of employees: 15,000

Implementation Date: 1991

TOC Applications: DBR

Comment: Drum-Buffer-Rope

IMPLEMENTATION RESULTS

Inventory Decrease: Reduced 100 million dollars (50%)

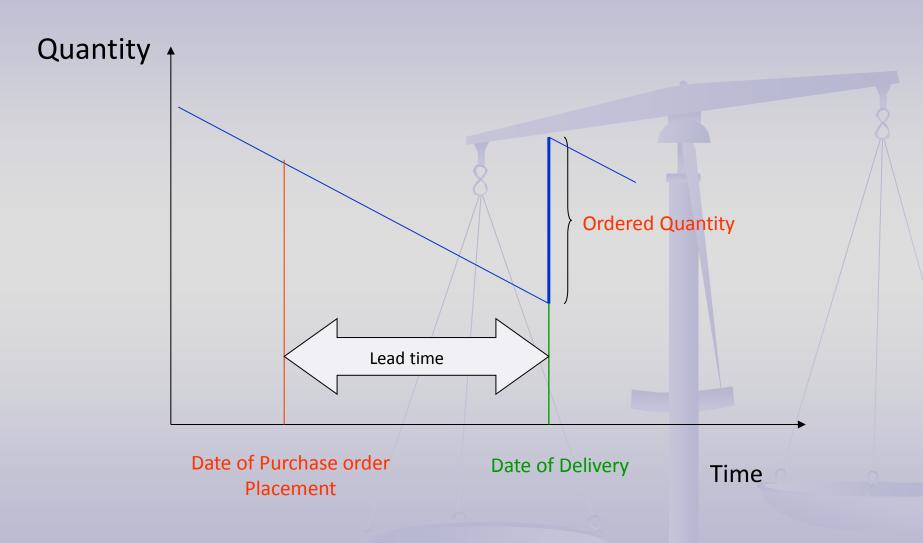
On-time performance: From 89% - to 98%

Lead times: From 6.4 days with JIT to 2.6 days

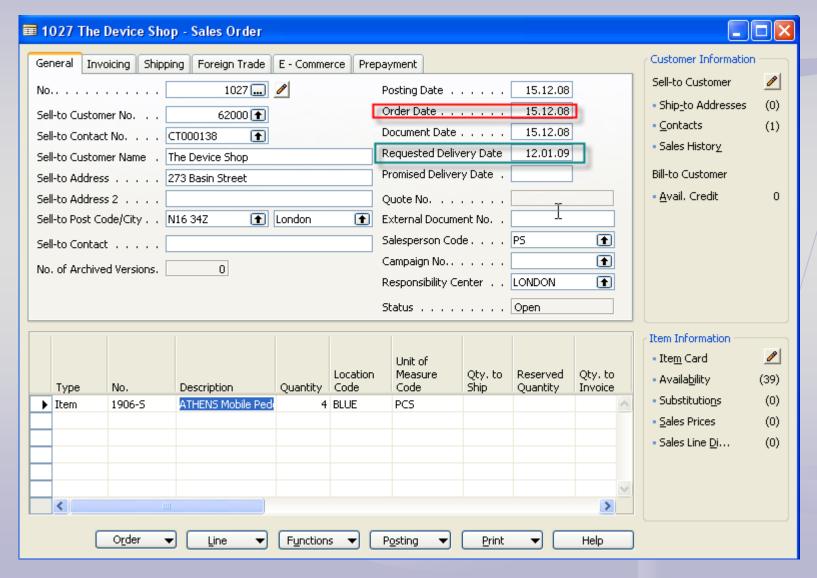
Cost efficiency: Reduced floor space by 57%

Quality: Reduced quality defects by 50%

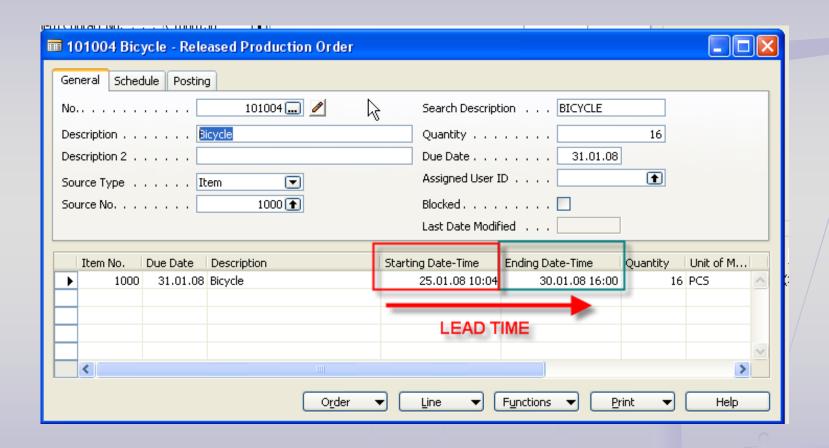
LEAD Time explanation-purchase



LEAD Time explanation-purchase



LEAD Time explanation-production



McDonagh Furniture Ltd

Revenue: \$8,000,000

Number of employees: 100

Implementation Date: 2000

TOC Applications: DBR

IMPLEMENTATION RESULTS

Revenue Increase: 28% Yr 1; 17% Yr 2

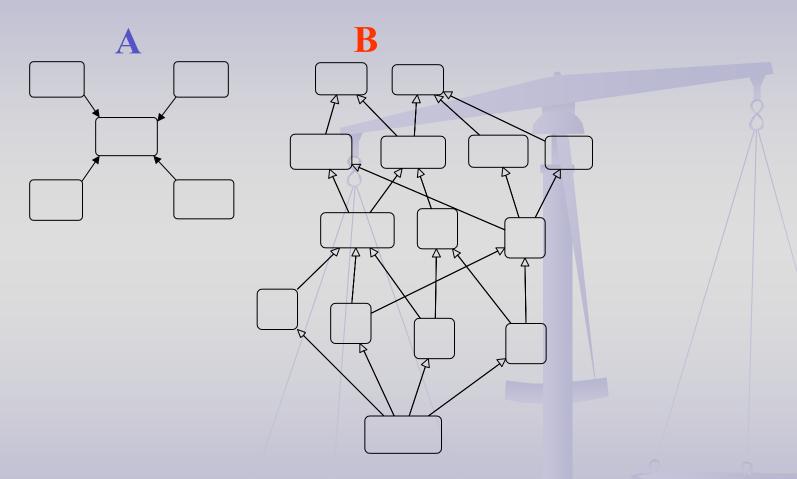
On-time performance: From 70% - To 98%

Lead times decrease: 20 %

Net profit increase: over 300%

Some other companies using TOC applications:

- BOEING –maintenance departments
- MOTOROLA -research
- GENERAL MOTORS
- LOCKHEAD MARTIN (F 22)
- BAE SYSTEMS
-



Which is harder to manage? Left or Right?

It is based on system approach

See next slide

 A company (enterprise) is to be understood as a chain of dependent processes — this picture below is very, very simplified

Marketing

Orders

Purchase

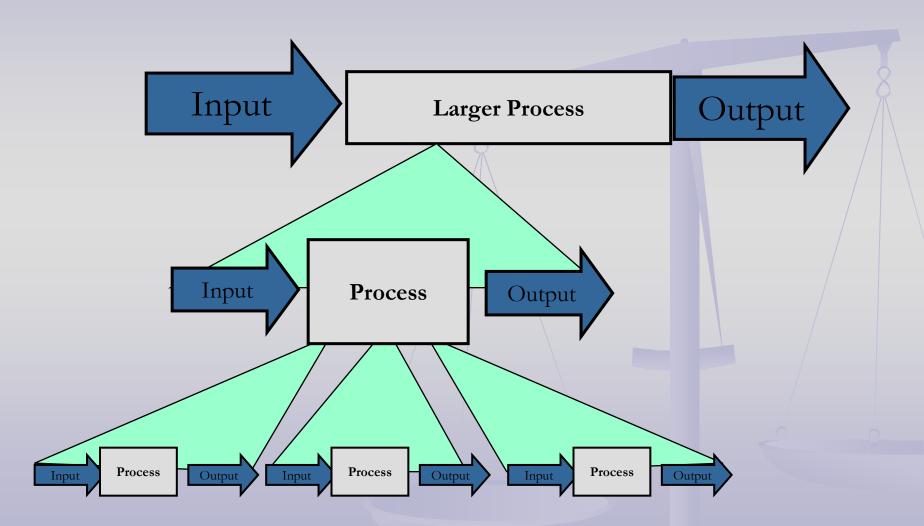
Production

Packaging

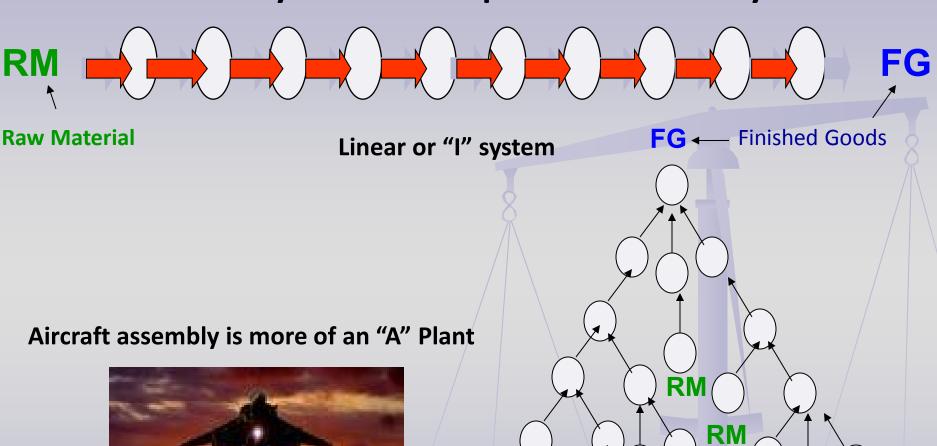
Shipment



Process Theory – more complex than one way chain



Process Theory – more complex than one way chain

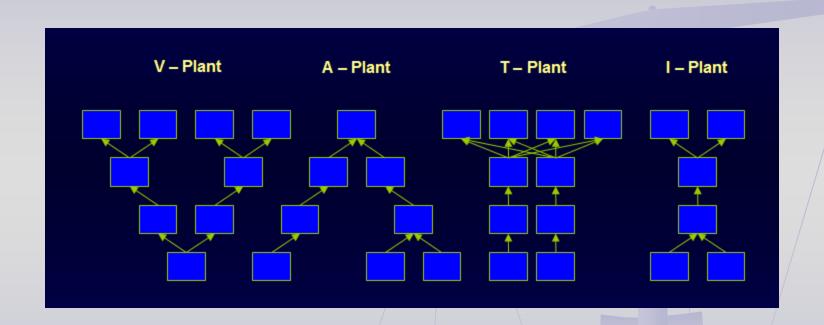




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RM

Types of plants



TOC – system approach

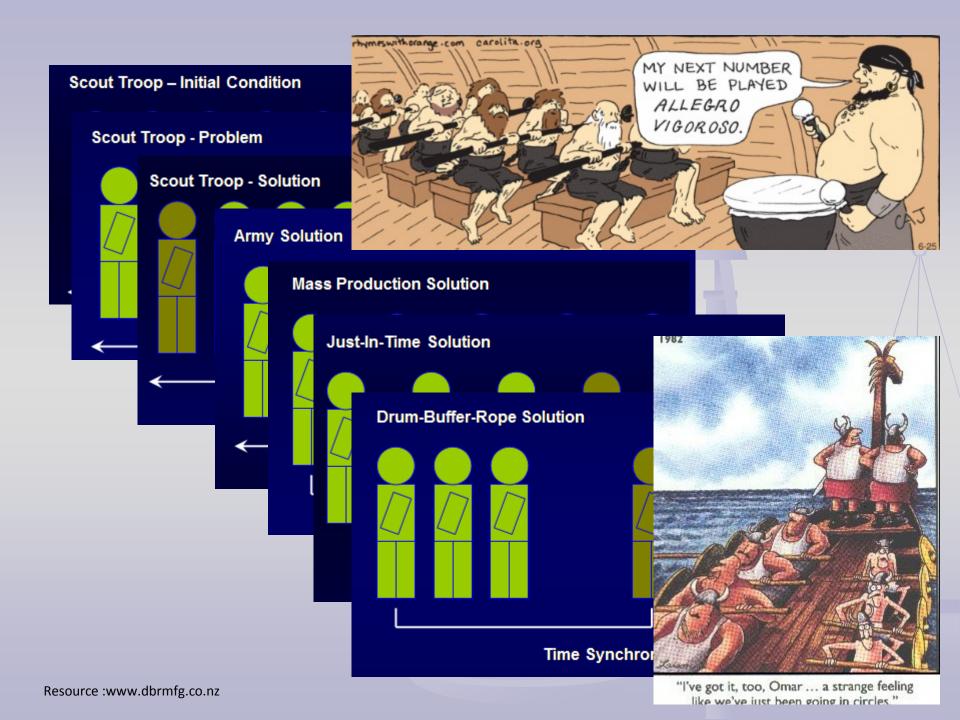
- Organizations / Systems exist for a purpose
- That purpose is better achieved by cooperation of multiple, independent elements linked together
- Each Inter-linked event depends in some detail upon the other links.
- The system owner determines purpose

TOC (home study)

- Most real systems could be seen in such a way, that there are only a few or better only one element (factor), which is the key point, where and only there all possible managerial methods have to be focused in order to control whole system
- "Every system is based on inherent simplicity".
- This element in TOC is called Constraint of the system = bottleneck
- Bottleneck: Any resource whose capacity is equal to or less than the demand placed upon it.

Inherent: základní, podstatná. neodmyslitelná....





TOC- bottleneck I

- Different link capabilities, normal variation and changing workload make it impossible to balance everything.
- One element of the system is more limited than another.



TOC- bottleneck II

When the whole system is dependent upon the cooperation of all elements, the weakest link determines the strength of the chain.

 An exactly balanced chain (system) is stronger than a nonhomogeneous chain, but when close to the breaking point, all

links must be managed



- Why constraint?
- Constraint prevents to reach the goal (make money now and in the future)
- The TOC goal : "Make money now and in the future"

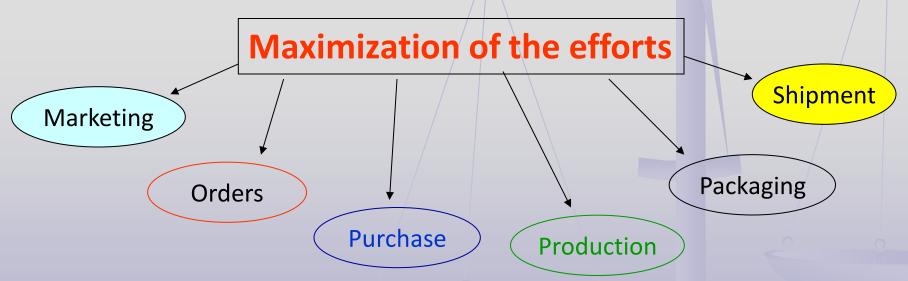
Every system has at least one such a constraint.
 The system without such a bottlenecks would reach the predefined business plans in infinite volumes.

TOC:



of the costs

 Traditional approach – world of where the aim of any endeavour is to optimize locally every segment of the chain, meaning balancing the capacity of every element and not the flow through the chain

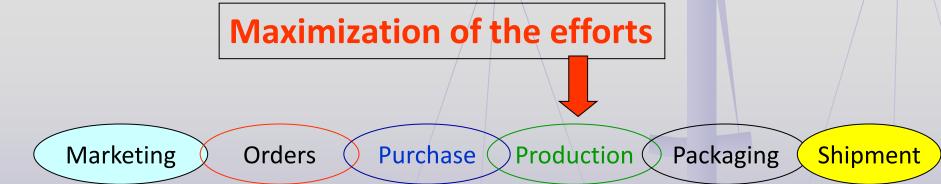


TOC:



of the throughput

- Use of : "common sense"
- The consistent focus of the bottleneck-
 - global optimization





World of costs:

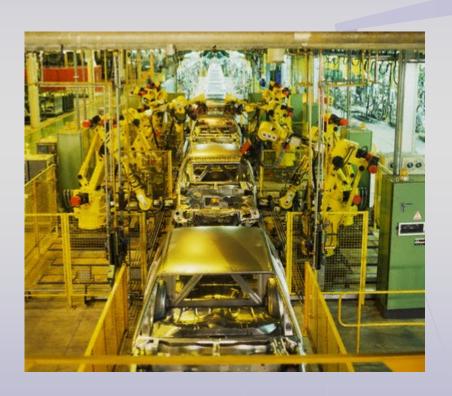
- main metric the weight of the chain (every decrease of the weight of any components will result in better efficiency (performance)
- Total improvement = sum of local improvements

World of throughput:

- main metric —the compactness of the chain
- Only improvement of bottleneck will improve performance of the whole chain
- Total improvement = improvement of the bottleneck

Life show

http://www.tocca.com.au/



Five steps process:

Step 0. Identify the Goal of the System/Organization Step 0.5 Establish a way to measure progress to Goal

- **Step 1.** *Identify* the system's constraint.
- Step 2. Exploit the system's constraint.
- Step 3. Subordinate everything else to the above decision.
- Step 4. Elevate the system's constraint.
- Step 5. If a constraint is broken (that is, relieved or improved), go back to Step 1. But don't allow *inertia* to become a constraint.

http://www.leadingagile.com/2014/01/theory-constraints/brooks-

law/

Brooks'law!!!

Adding manpower to a late software project makes it later!

- "Cost Accounting is enemy number one of productivity". *
- Impact on the behaviour of the people and they habits of finding and improvements of local elements having reason in optimising of these particles.
- New metrics were introduced already presented

* Eric Noreen, Debra Smith and James t. Mackey

Definition (TOC metric) - summary

- Throughput (T): The rate at which the system generates money through sales.
 - Note that the money is generated through sales and not production because if you produce something and don't sell it, you have not really had throughput. (You've just put it into inventory).
- Inventory (I): All the money that the system has invested in purchasing things, which it intends to sell.
- Operational Expense (OE): All the money the system spends in order to turn Inventory into Throughput. See classification of OE later in this show

TOC metrics more in detail (T)

throughput is the rate at which a system achieves its goal. Often this is monetary revenue and is in contrast to **output**, which is inventory that may be sold or stored in a warehouse. In this case throughput is measured by revenue received (or not) at the point of sale exactly the right

TOC metrics more in detail (OE)

Operating expenses includes e.g. :

- accounting expenses
- license fees
- maintenance and repairs, such as snow removal, trash removal, janitorial service, pest control, and lawn care
- advertising
- office expenses
- supplies
- attorney fees and legal fees
- utilities, such as telephone

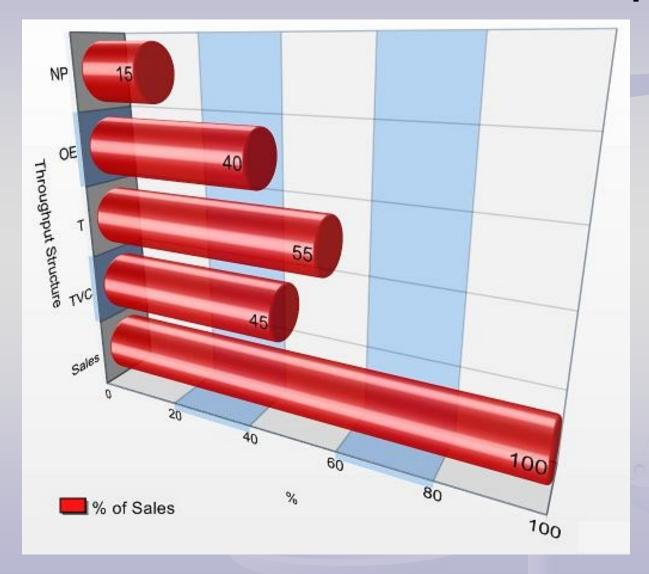
Measuring the goal (TOC metric)

- Net profit (NP=T-OE): (T, I and OE was already explained in this course) -> T=Net Sales TVC =S-TVC, where TVC=Total Variable Costs
- Cash
- Return on Investment (ROI=NP/I)

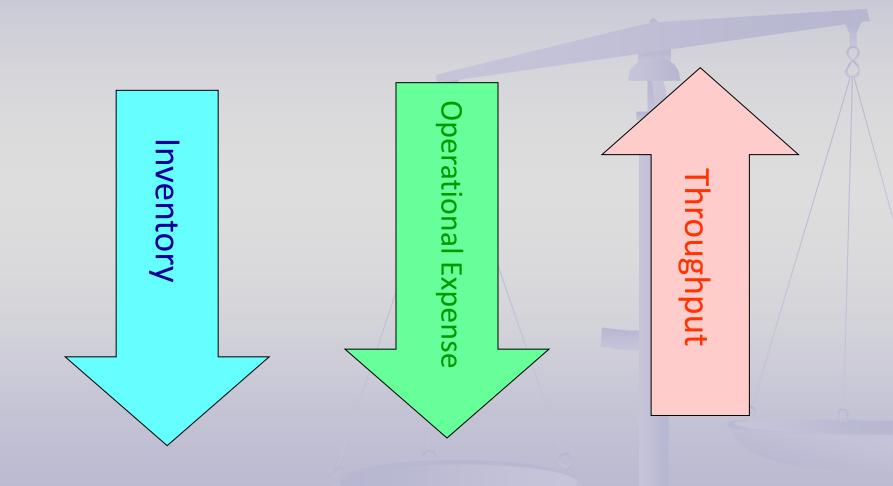
For a manufacturing enterprise, the goal can also be measured by:

- Throughput =T
- Inventory = Investment/=I
- Operating Expenses = OE

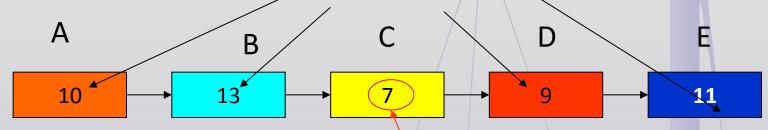
Metrics and their relationships



TOC -required trends



- NP=T-OE = (S-TVC) OE; where **TVC**=Total Variable Costs and S=Unit Price
- \blacksquare ROI=(T-OE)/I=NP/I, where NP=Net Profit
- where T=total throughput (pcs/unit of time)



- 1. Only one product !!! In our example TVS=0
- 2. Unit Price (Selling price) = 100 USD = S
- 3. Raw material /one product =35 USD =OE
- **4.** NP/product=(T-OE)=**100-35**=**65**
- 5. 176 hours/month (constraint of the company)
- 6. T=176 * (7) = 1232 parts/month
- 7. Monthly NP = 1232 * 65 USD = 80 080 USD

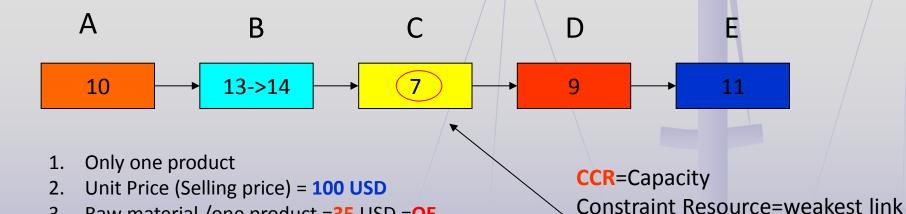
CCR=Capacity

Constraint Resource=

=weakest link of the chain=

bottleneck

- 1st suggestion is to optimize B from 13->14 parts per hour
- T will not increase ->You cannot produce more than 7 !!!!
- Investment to optimize B=5000 USD with depreciation 10 %
- OE(month) = (5000 USD * 0,1)/12 = 41,67 -> 42 USD (when rounded)

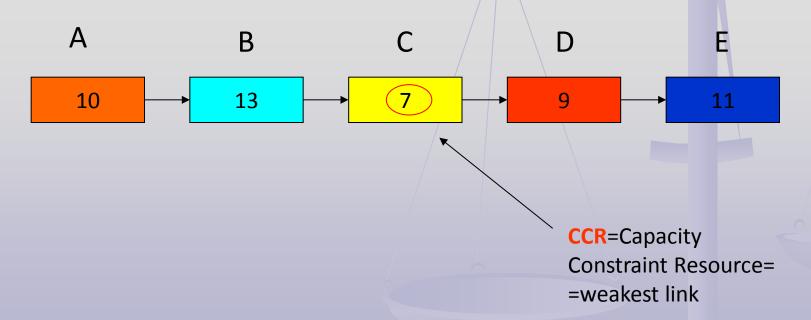


- NP/product=100-(35+42)=23
- 176 hours/month (constraint of the company)

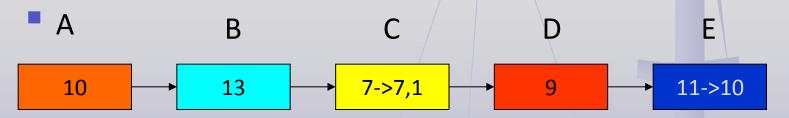
Raw material /one product =35 USD =OE

- T=176 * 7 = **1232** parts/month
- Monthly NP =1232 * 23 USD = 28 336 USD

- T = throughput will not increase
- NP (Net Profit) will decrease based on increased OE (41,67 USD /month)
- Based on NP decrease ROI is negative
- Bad suggestion !!!!!!



- 2nd suggestion is to optimize C from 7->7,1 parts/hour
- part of the 2nd suggestion is an extra load of E so it goes from 11->10
- Necessary investment is 5000 USD (remains the same)
- Increase of the T=production/month = 0,1*176=17,6 parts
- Increase of the company NP= 17,6*23 USD= 404 USD/month



- Necessary investment is 5000 USD = I =Inventory= Investment
- Increase of the T= production/month = 0,1*176=17,6 parts
- Increase of the company/month NP= 17,6*23 USD= 404 USD
- OE/month =(5000 * 0,1)/12= 41,67 -> 42 USD
- OE will be increased by 42 USD/month
- Annual increase of the NP = 404*12=4848 USD
- ROI=NP/I = (28336*12+4848)/5000 = 69 % !!!
- T does not measure local efficiencies, except at the constraint- see next slide



Throughput

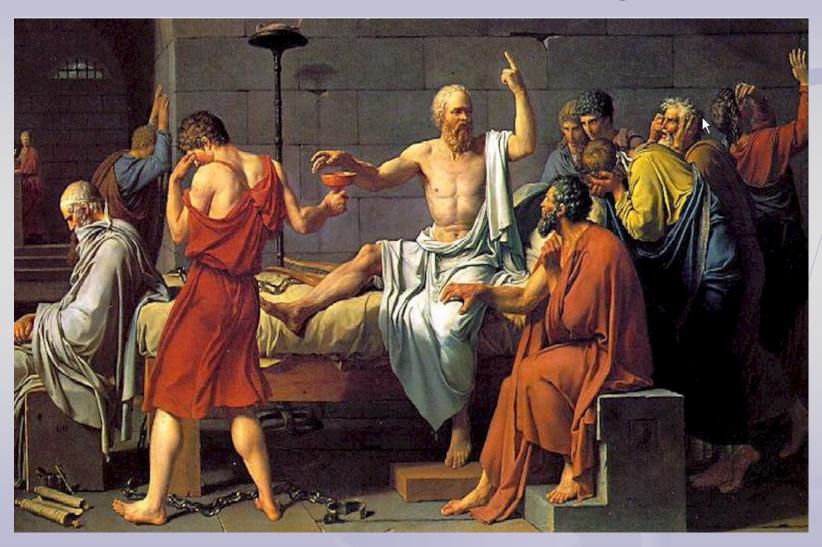
- 1. T=176 * 7,1 = 1250 parts/month (rounded)
- 2. Monthly NP =1250 * 23 USD = 28 750 USD
- 3. Originally:
 - 1. T=176 * 7 = 1232 parts/month (rounded)
 - 2. Monthly **NP =1232 * 23** USD = **28 336** USD

- it represents challenging adventure, where the invested efforts are often not predictable
- it requires cooperation, coordination and use of well informed and trained teams on both sides.
- you will certainly overcame natural resistance against changes and persuade distressed and indolent people
- no one is willing to change anything

- try to find somebody who could accept changes !!!
- you must persuade these guys, that the suggesting changes are in fact their idea and without their creativity TOC would be only toothless beast!
- but how to achieve it ??

- Socratic teaching proving the logic by use of dialog
- Buy-in approach initiator of the changes must have interpersonal and communication talents in order to persuade the targets and squeeze from the people their best ideas.

Socratic teaching



We have to find out the answers to these questions:

- 1. What to change?
- 2. To what to change to?
- 3. How to make the change happen?

What to change?

- Objectives: Situation assessment, description of "current reality," and identification of the core problem or conflict and assumptions that sustain it. Diagnosis and systemic root cause analysis.
- But at any time you will meet enemies the ones who hate any changes You have a lot of people wishing to do the same, a lot o people doing exactly the opposite and immense quantity of people which would like to do nothing!
- Layers of resistance: Lack of agreement on the problem

RESISTANCE



To what to change?

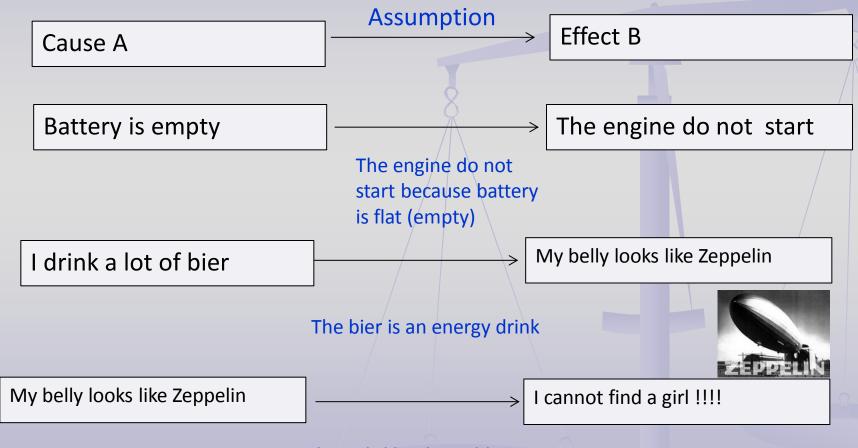
- Objectives: Verbalization of vision/solution, description of strategy to attain the desired state, and avoidance of undesirable side effects. Prescription, decision-making, and solution development.
- Layers of resistance:
 - Lack of agreement on a possible direction for a solution
 - Lack of agreement that the solution will truly address the problem
 - Concern that the solution will lead to new undesirable side effects ("Yes, but...")
 - Or you will get even worse reaction ("NO, because…")



Thinking Process Tools

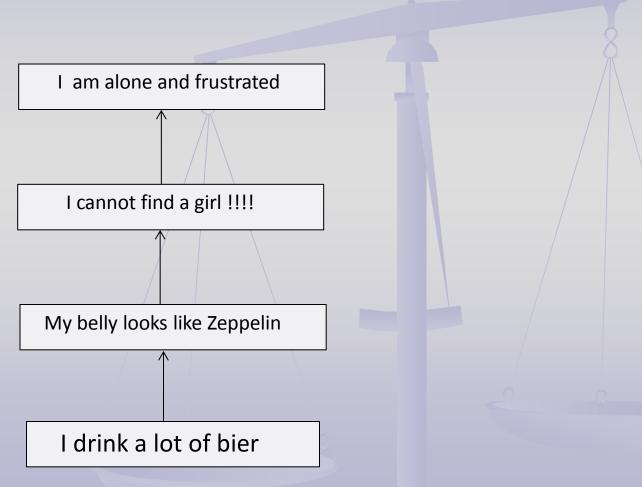
- offer the answers to three TOC questions about changes
- help to clear away every layers of resistance
- visualisation of the thinking process
- verbalization of the thinking process
- use of casual logic (cause ->effect)
- use of sufficiency logic "IF AND THEN"
- use of necessity logic "IN ORDER TO THEN BECAUSE"

Basics



The girls like slim athletes

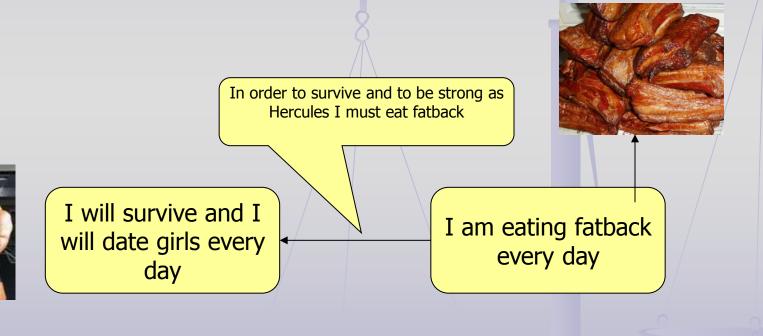
Cause-effect simple sturcture



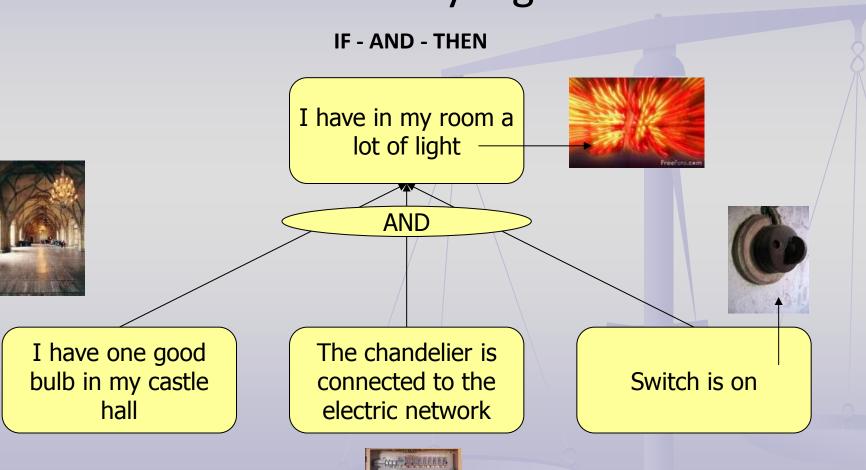
Thinking Process Tools

Necessity logic

IN ORDER TO - THEN - BECAUSE



Thinking Process Tools Sufficiency logic

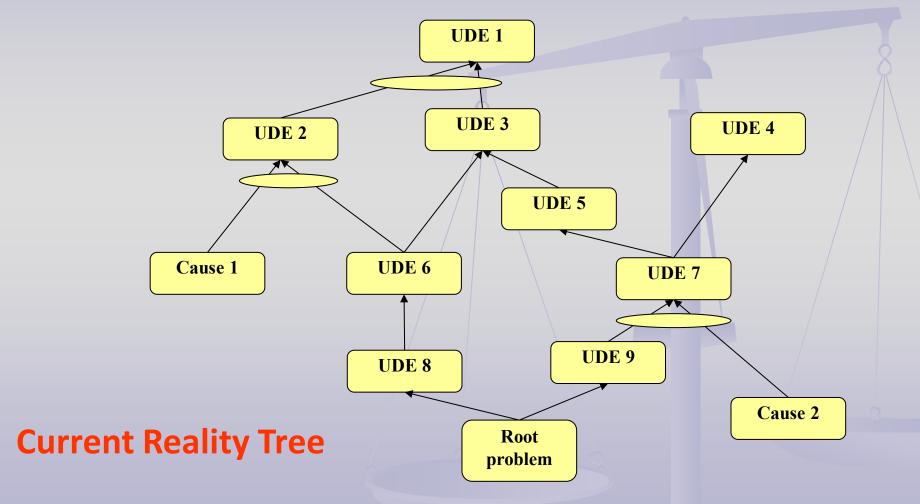


A tool for solving such a task : Current Reality Tree

- Why to change something and what is something (core problem=constraint, bottleneck)
- Summary of all Undesirable Effects (UDE) and their layout based on casual logic - sufficiency logic
- Core Problem common cause of all UDE

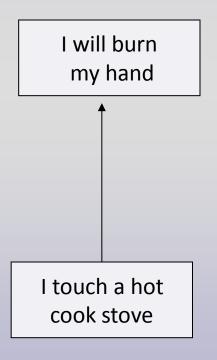
UDE examples

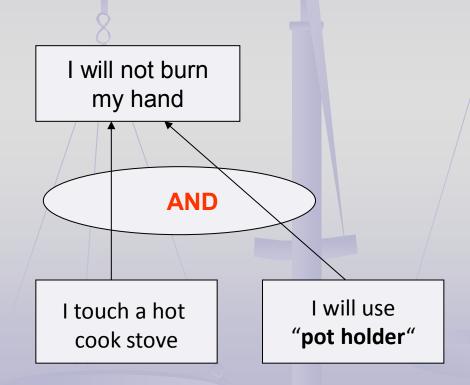
- From the book "<u>It's Not Luck</u>", some examples of the UDEs are:
- Production and distribution do not improve fast/significantly enough
- Engineering is unable to deliver new products fast and reliably enough.
- Companies don't come up with sufficient innovative ideas in marketing.
- In more and more cases the price the market is willing to pay doesn't leave enough margin.
- There is unprecedented pressure to take actions that will increase sales
- Competition is fiercer than ever.
- In advanced material industries there is a need to launch new products at an unprecedented rate.
- In advanced material industries the constant introduction of new products confuses and spoils the market.
- Sales people are overloaded.
- There is increasing pressure to reduce prices.



Causality:

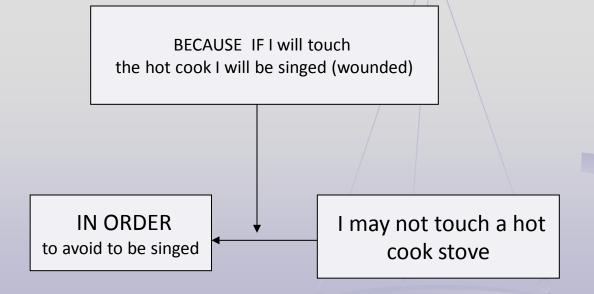
IF a lot of snow AND snowboarding in restricted area THEN avalanche

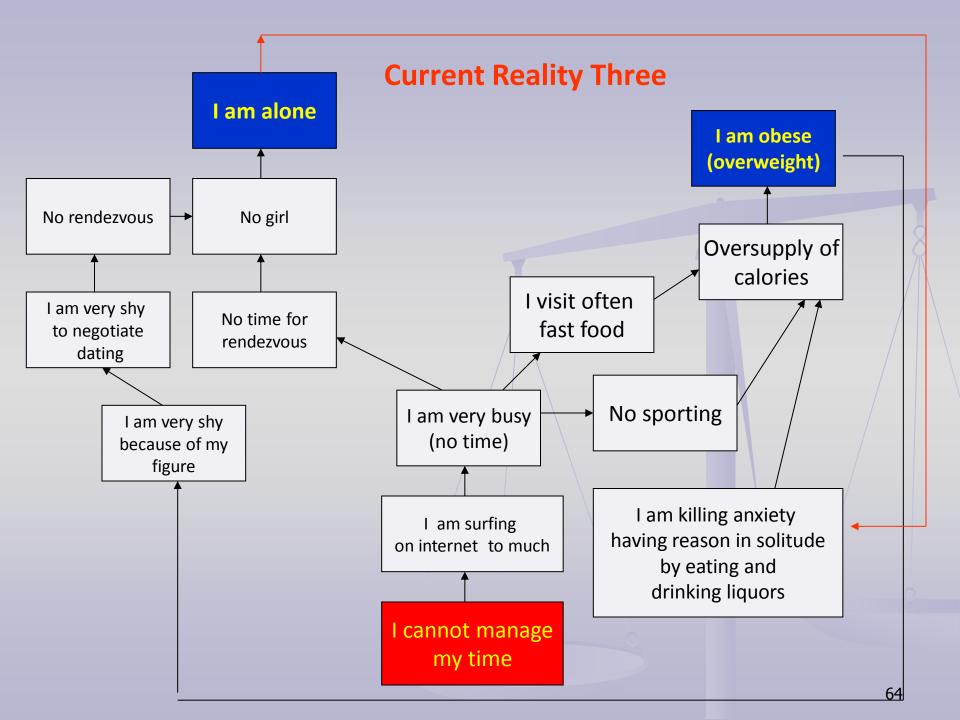




Necessity logic:

IN ORDER to avoid something I HAVE TO do this



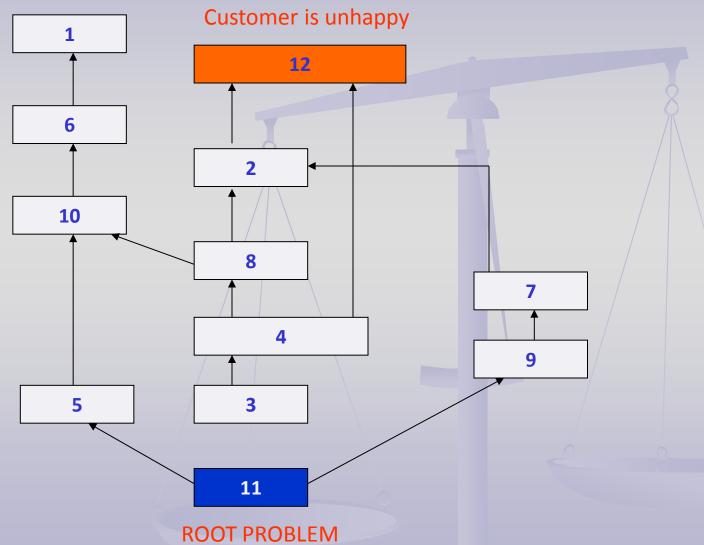


Current reality three (home study)

List of UDE's:

- UDE1 : lack of financial consultants (FC)
- UDE2 : late hand-over of required services during implementation and support
- UDE3: a modern design of ERP is not easily understood by rigid customer's accountants
- UDE4: the customer's accountants tend to use old fashioned methods and processes which are difficult to manage by using a modern ERP
- UDE5 : rigid remuneration does not allow to pay more FC than the others
- UDE6 : high level of fluctuation and job-hopping
- UDE7: overburdened FC as a consequence of bad multitasking (will be explained later in Critical Chain PWP)
- UDE8 : FC are fed up by permanent repetitive explanation to the customer's accountants who do no want to understand
- UDE9 : bad multitasking
- UDE10 : FC are unhappy because of a salary, which is much more lower then their expectations
- UDE11: The management sticks to Cost world and tends to decrease costs by minimising payroll and having all resources as a CCR (Critical Constraint Resources)
- UDE12 : Customer is unhappy

Current reality three (home study)



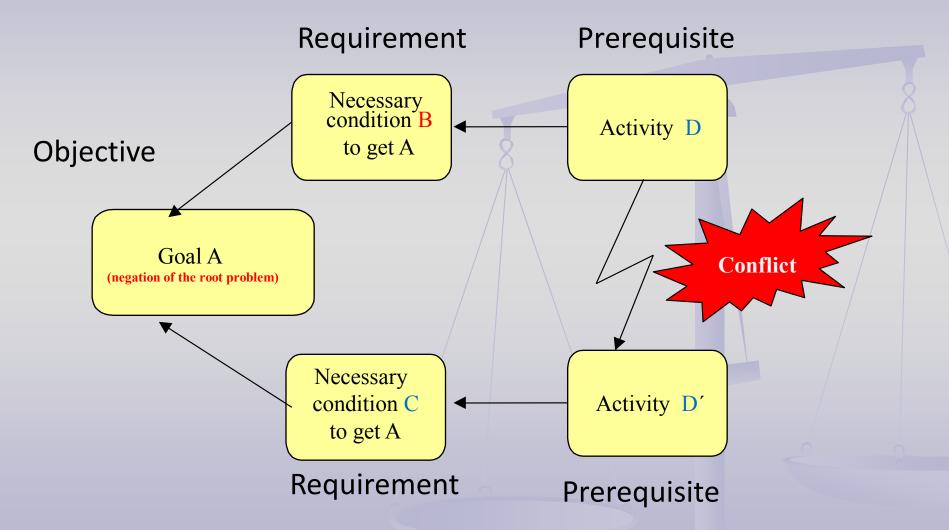
We have to solve another crucial question: the direction of solving a core problem

What is the main reason (injection) supporting the change!

Evaporating Cloud Tree

- the change without any compromise basic and starting impulse for the change
- use of "necessity logic" common goal, necessary condition to reach this goals, what have to be done and where is a conflict
- "well thought out from the scratch" of the problem, disclosure (findings) and verbal definition of hidden assumptions
- Win-Win solution of the whole conflict = injection !!!

We have to solve another crucial question: the direction of solving a core problem



How to read this Evaporation tree

In order to have objective A, we must have requirement B..

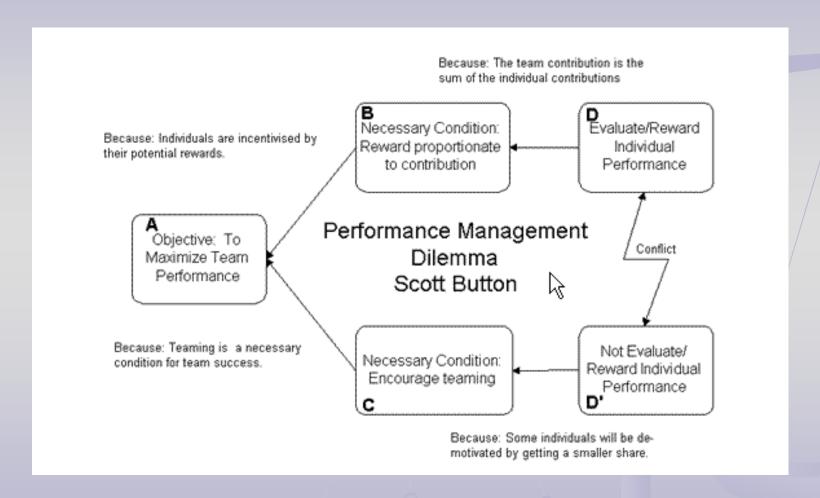
In order to have requirement B, we must have prerequisite D...

In order to have objective A, we must have requirement C...

In order to have requirement C, we must have prerequisite D'...

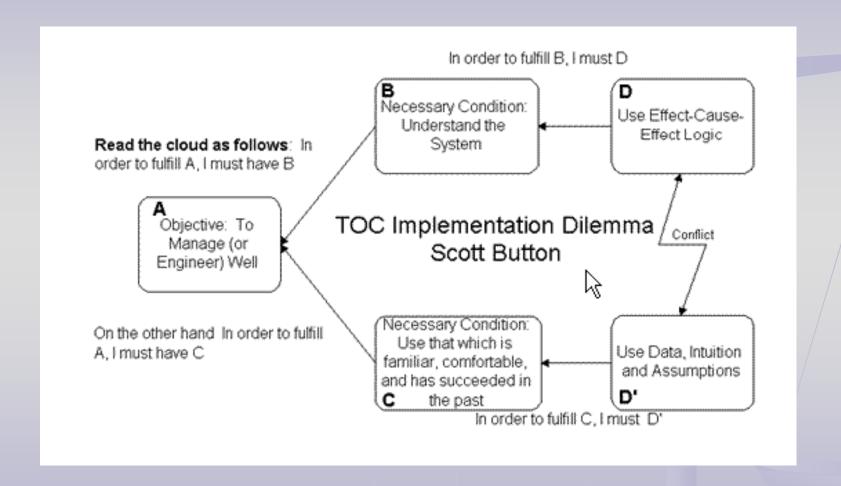
But prerequisites D and D' are in conflict... Like fire and water

Evaporation cloud tree- example 1



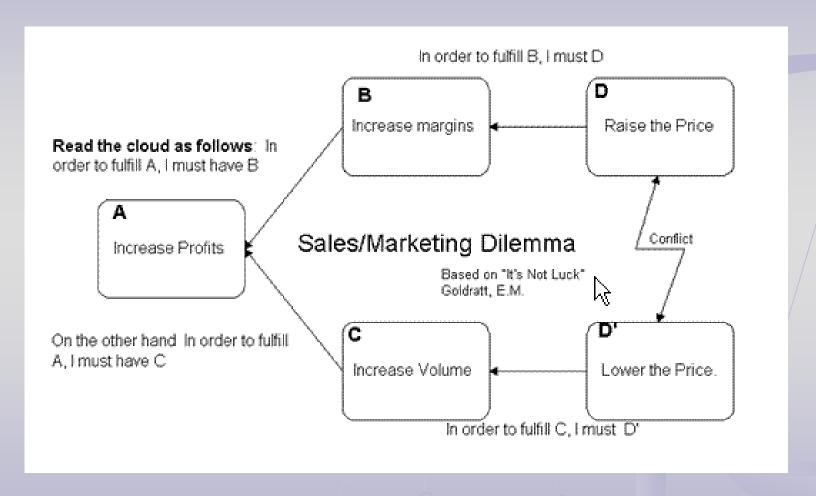
Performance Management

Evaporation cloud tree- example 2



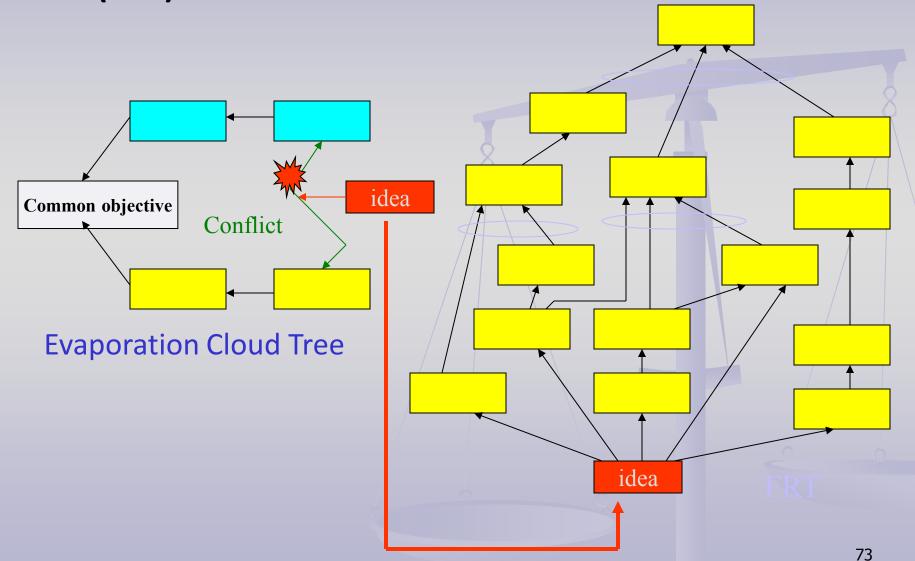
Implementation of TOC

Evaporation cloud tree- example 3



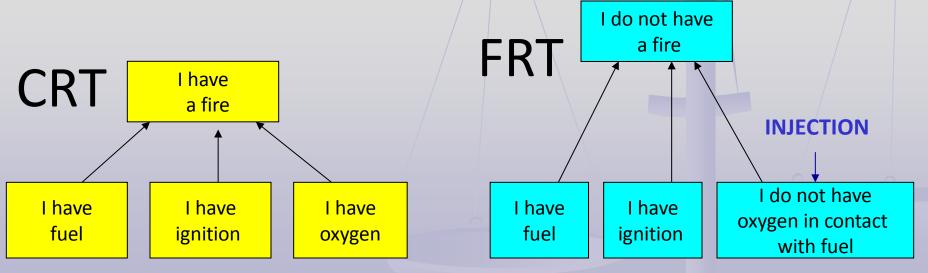
Sales and prices

Transition Evaporation Cloud Tree Future Reality Tree (FRT)



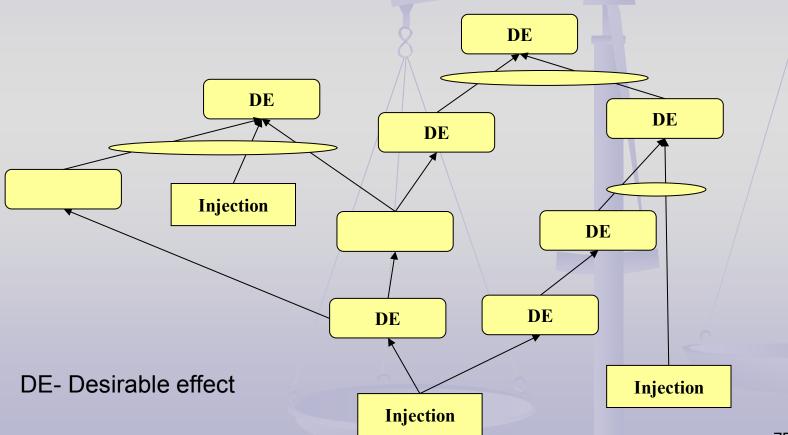
Future Reality Tree (FRT)

- The FRT is similar to the CRT in structure, but with new proposed actions, policies, and behaviour injected into it in order to create a new vision of the future reality of the system.
- The power of the logical "if-then" construction is that if any one of the lower-level causes are removed or mitigated, everything that is above it is subject to change.
- If any one of the three "IFs" are removed or modified, the "THEN" may be removed from consideration as a problem

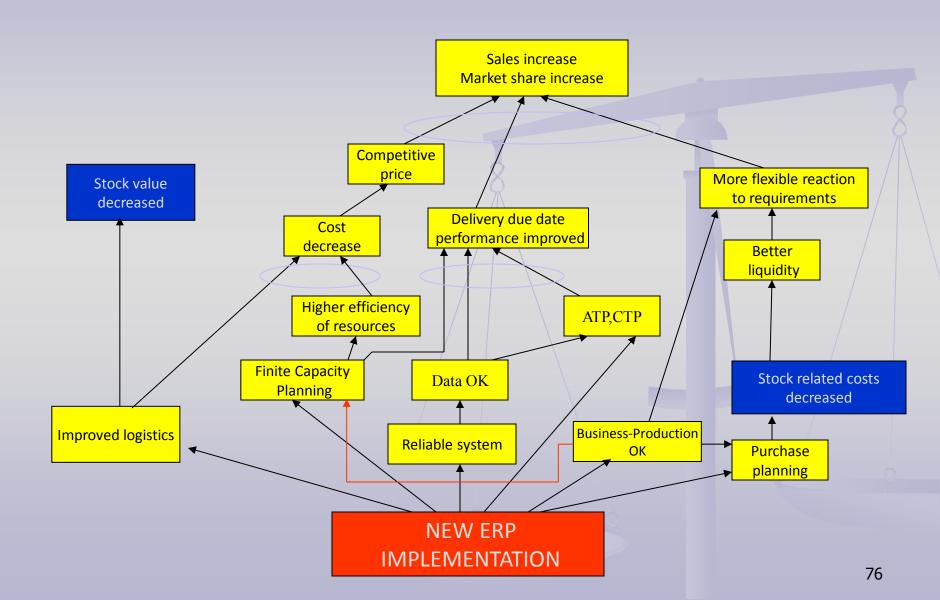


Future Reality Tree (FRT)

 The objective of the FRT is to communicate a vision of how to change the undesirable effects found in the CRT to desirable effects.



Future Reality Tree (FRT)

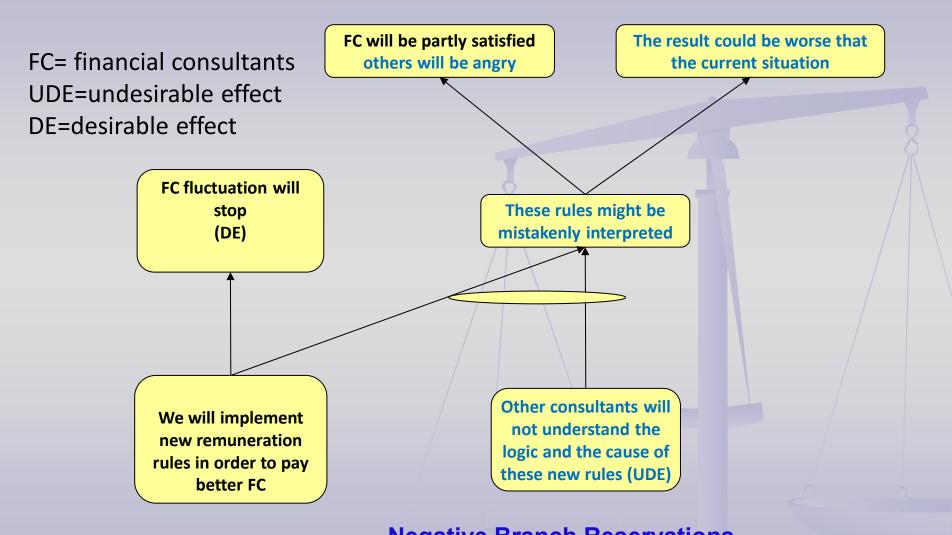


YES, this could be managed BUT.....

Negative Branch Reservations (NBR):

- use of sufficiency logic by taking into consideration objections of other involved persons
- these objections were related to possible undesirable impacts of the injection (solution) implementation
- ➤ NBR is often a part of the FRT (Future Reality Tree)
- Evaporation Cloud Tree, FRT and NBR enable to answer the second question : To What To change ?

YES, this could be managed BUT.....



Negative Branch Reservations

We cannot implement it, because

(Prerequisite Tree):



- use of necessity logic identification of obstacles
- use of the human ability to invent any reason

WHY IT IS NOT FEASIBLE

- > setup of the necessary intermediate objectives
- setup of the schedule for change process

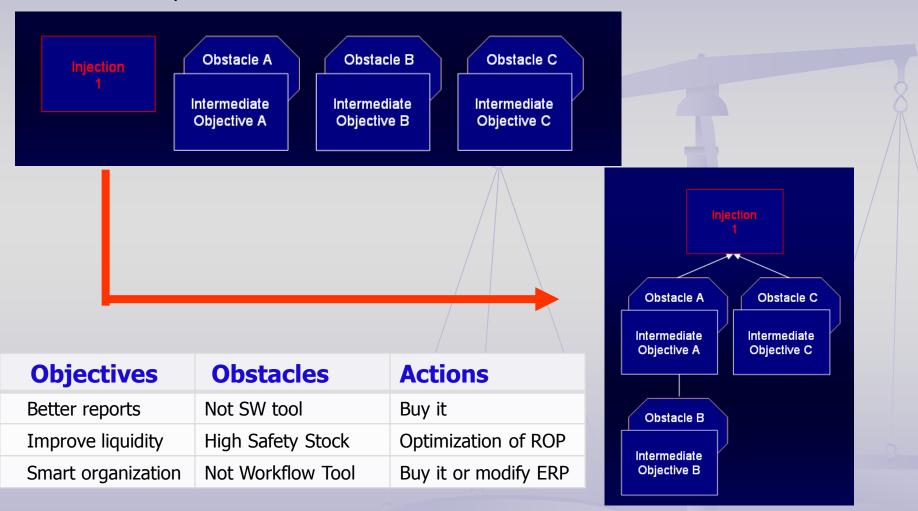
We cannot implement it, because

(Prerequisite Tree):

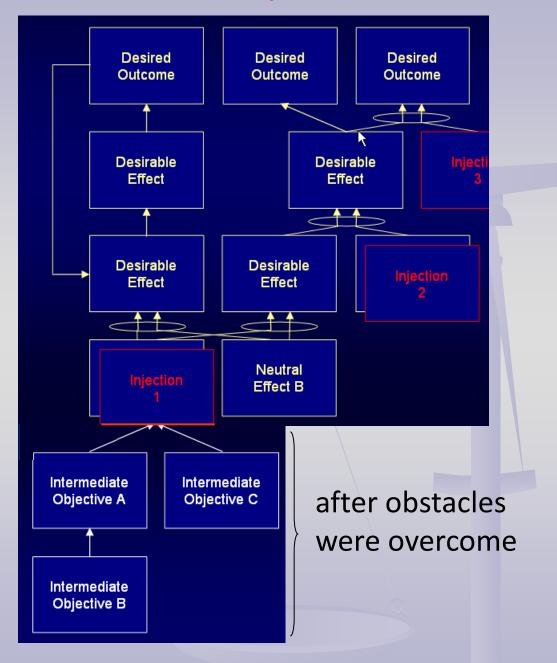
- The pre-requisite tree ought to be considered the most important tree in the Thinking Process suite.
- It is the tree that allows us to overcome the obstacles that stop us from implementing our plan.
- It is also the tree that in fact becomes the implementation plan (it is very, very close to project management practice !!!!)
- And it is the tree to which timelines, responsibilities, and accountabilities can be assigned to.
- The pre-requisite tree occupies the position of "plan" amongst the Thinking Process tools.

Prerequisite tree - construction

So our first step will look like this



HOME study ONLY !!!!



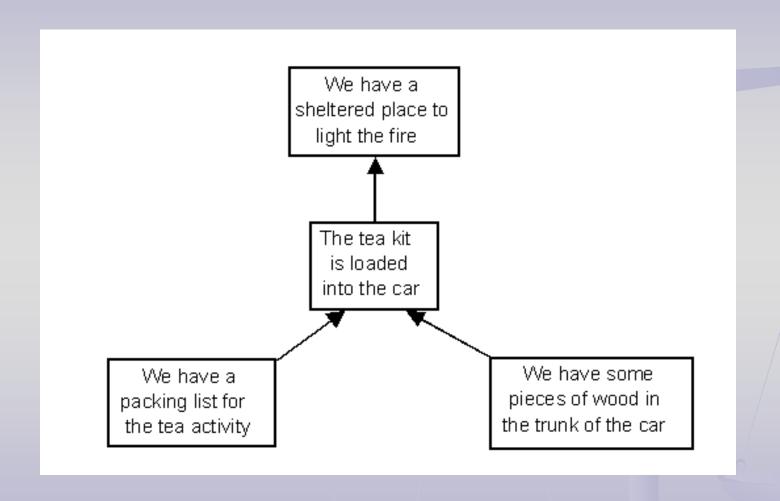
Prerequisite tree - example

- Tea Mission (we want to have a nice cup of tea in the wilderness)
- Obs-1 : We do not have material to burn
 - **Obs-2**: Collection of such material is not allowed in the wilderness.
 - **Obs-3**: There could be a strong wind
 - **Obs-4**: We do not have matches
 - **Obs-5**: We do not have cups
 - **Obs-6**: We don't have a container to boil the water
- IO-1 : We have some pieces of wood in the trunk of the car.
 - **IO-3** : We have a sheltered place to light the fire
 - **IO-4.1**: We have a packing list for the tea activity
 - **IO-4.2**: The tea kit is loaded into the car

IO= intermediate (partial) objective Obs= obstacle

HOME study ONLY !!!!

Prerequisite tree - example



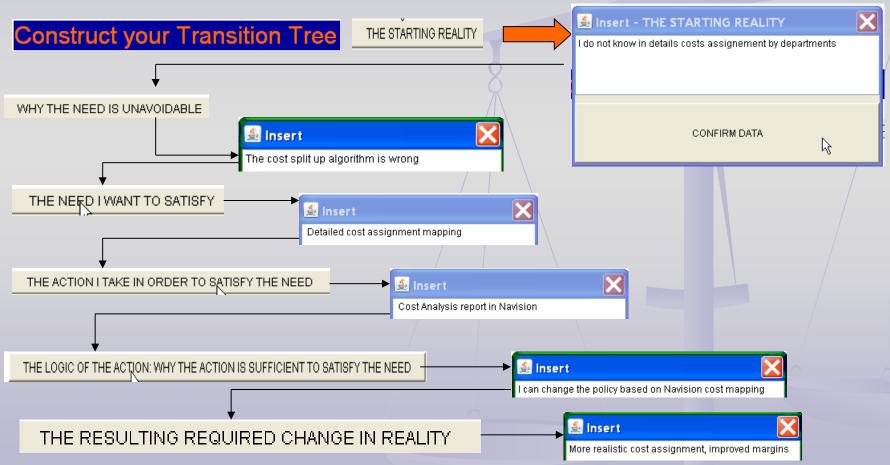
We cannot implement it, because

(Transition Tree):

- detailed schedule of change implementation process
- what actions have to be taken in order to reach intermediate objectives using sufficiency logic (IF-THEN-ELSE)

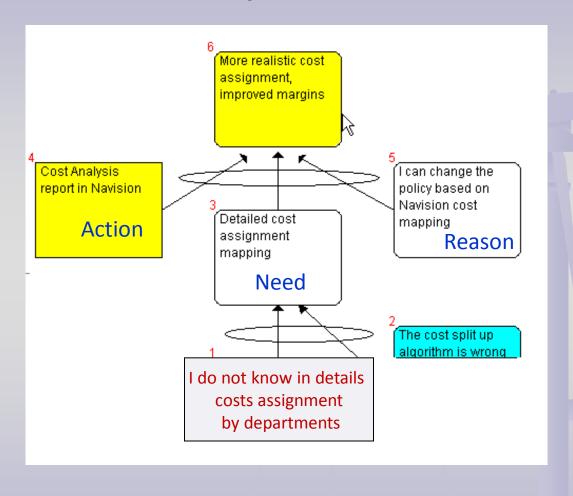
We cannot implement it, because.....HOME study ONLY !!!!

(Transition Tree) http://www.thedecalogue.com/Tools/trt/TREE.html:

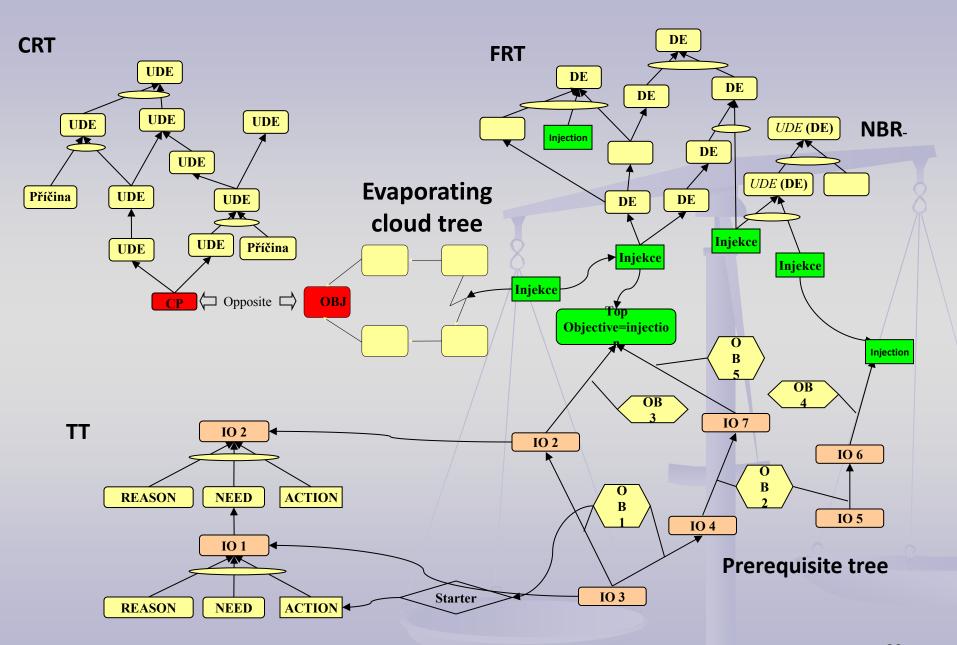


HOME study ONLY !!!!

We cannot implement it, because.....



Thinking Process Tools Relationships



Additional metrics of TOC (appendix 1)

- Inventory dollar days (IDD)
- A measure of the effectiveness of a supply chain i.e., did it do things that it shouldn't have done and as a result is the supply chain holding inventory of products the customer doesn't want? IDD accounts for two things: 1. the time from when a unit is placed in stock until it is actually needed by a customer; and, 2. the monetary value of the inventory being held. IDD is calculated by multiplying the monetary value of each inventory unit on hand by the number of days since that inventory entered the responsibility of that link. The system should strive for the minimum IDDs necessary to reliability maintain zero throughput dollar days.
- NOTE: The resulting unit of measure is "dollar-days". It is neither monetary nor time based. Attempts to compare dollar-days to other monetary measures are invalid. IDDs can be compared only to other IDD levels.

Additional metrics of TOC (appendix 2)

- Throughput dollar days (TDD)
- A measure of the reliability of a supply chain. TDD considers two things: 1. the monetary value of the things a link is committed to deliver but does not; and, 2. the number of days by which the link misses its commitment to deliver. TDD is the summation of the commitments not delivered on time during the chosen time period. The TDD value of individual missed commitments is calculated by multiplying the dollar value of the end product times the number of days the commitment is/was overdue. The system should strive for zero throughput dollar-days.
- NOTE: The unit of measure "dollar-days" is neither monetary nor time based. Attempts to compare dollar-days to other monetary measures are invalid. TDD levels can be compared only to other TDD levels.

Literature

Goldratt, E., M.:

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- The Race
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