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How to Manage Through Worse-Before-Better

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Many Western managers were introduced to lean production in 1990, with publication of The Machine That Changed the World, based on a five-year study of Toyota by MIT's International Motor Vehicle Program. Since then, thousands of managers have been drawn to the principles of lean management as a way to achieve faster cycle times, reduced defect rates and sharp gains in on-time deliveries. Lean management permits a marked reduction in inventory levels required across the supply chain. These changes should result in better financial performance, especially because companies achieve simultaneous declines in manufacturing and service costs.

But, as the authors point out, the transition takes time, and it is full of obstacles. One of the biggest and most predictable hurdles is the crisis in confidence that occurs when management isn't able to improve financial performance quickly enough. Lean transformations generally have short-term adverse impacts on the company's bottom line (that is, things get worse before better). Management needs to anticipate these challenges and explain them clearly.

To help managers overcome the financial hurdles on the path to lean, the authors offer new tools for anticipating the deterioration in financial performance that invariably occurs as a mass producer goes lean and for understanding the real performance improvements that take place during this period. Their approach, which they call "value-stream accounting," helps managers plan for the short-term financial impact, monitor progress, understand the operational improvements and develop strategies to maximize the longer-term benefit.

Traditional accounting systems are not designed to show the causes of adverse impacts or reveal the future benefits that will accrue from improved operational processes. Managers need to understand that the "bad" news isn't really bad — it's part of the necessary process of establishing a stronger, more productive organization. The authors' approach replaces the traditional cost-accounting system with a transparent accounting system that tracks the company's value streams, which incorporate all of the value-adding and non-value-adding activities required to bring a product or service from start to finish.

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