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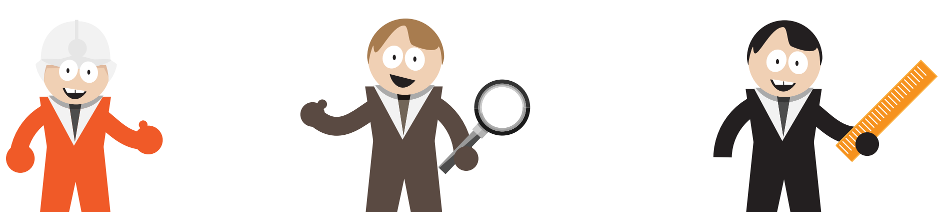
# 3 New Year's Resolutions for Better Inventory Control

By Jon Schreibfeder



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Every business is planning (or hoping) for better performance in 2013. Unfortunately many companies will fail in this quest. Why? Because they are looking for a quick fix rather than a change in corporate culture. Like any permanent improvement in your life, meaningful change only occurs when you implement a fundamental change in the way you do things on an ongoing basis. Why not begin 2013 by implementing these best practices that have helped numerous companies achieve the goal of effective inventory management. That is, to meet or exceed customers' expectations of product availability while maximizing your organization's net profits.

## Resolution #1 - Justify It

**Justify why every slow moving product item remains in inventory. Most warehouses are filled with two things:**

- **Stock** – Products your customers expect to be available for immediate delivery
- **Stuff** – Everything else

There are many reasons for stuff to be in your warehouse: discontinued products, returns of non-stock items, what seemed to be good ideas for new product introductions that didn't pan out, etc. Begin the new year by identifying your stuff and beginning a liquidation process. This will free up valuable space and generate some cash (even if it is only scrap value) that can be better spent on productive stock inventory. We suggest you look at every product that has sold in less than three of the past 12 months.

**Ask:**

- Is this a new stock item that needs additional time to develop a market?
- Is this a critical item that must be on hand just in case a customer needs it? If so, is the profit margin great enough to offset the cost of carrying inventory for a prolonged period of time or does carrying this item directly lead to other profitable sales?

If the answer to both of these questions is no, liquidate your remaining stock. Remember that liquidation does not necessarily mean throwing this material in the dumpster. It means getting as much as possible above the cost of liquidation.

**Consider:**

- Transferring the material to another company location where the inventory is needed
- Discounting the remaining stock to encourage impulse buys by customers
- Returning it to the vendor even if you have to use the credit received to buy other stock items for which there is customer demand
- Advertising the availability of this material to other suppliers

**Don't get emotionally attached to your stuff.**
**Consider any compensation you receive for this unneeded material to be found money.**

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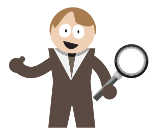
## Resolution #2 - Question It



**Develop a questionnaire for introducing new products. The best way to control the amount of stuff in your warehouse is not to buy it in the first place. Successful companies insist that anyone wanting to add a product or product line to inventory complete a new product questionnaire. The questionnaire includes seven questions:**

I. Who is asking that the product be added to inventory? If it is a specific customer, have they committed to purchasing a certain quantity and have they honored their past commitments to buy products? If it is a sales or marketing person, what is their previous track record for new product introductions?

II. What are the sales or usage estimates for each of the first six months? Be sure to compare actual sales/usage to these forecasts at the end of each month.

III. What is the projected gross margin? Again monitor actual performance at the end of each month to this estimate.

IV. What effect will sales or usage of this new item have on the sale or usage of existing stock items? Do we need to discontinue or cut our inventory of any current products?

V. How much do we need to invest in the new item(s)? Is it possible to perform a market test before committing to a major purchase?

VI. If the item doesn't sell as expected can we return the remaining portion of the initial purchase quantity at little or no cost?

VII. Do we have adequate room to properly store the new product? Remember that the walls of of your facility are not elastic. You can only maintain a certain amount of inventory.

**We have found we have had the most success when at least three members of management, after reviewing a new item questionnaire agree it is a wise investment.**

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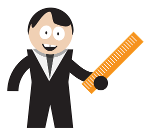
## Resolution #3 - Measure It



**Set appropriate goals for your buyers. Follow the old adage, people will do what you inspect, not what you expect. Every buyer or inventory planner should have goals for the products for which he or she is responsible. We have found two metrics best analyze a buyer's or inventory planner's performance:**

**Inventory Turnover.**
Inventory turnover measures the number of times you sell or turnover your average inventory investment each year. In reality it measures the number of opportunities you have to earn a profit from every dollar of your investment in stock inventory. It is calculated by divided annual cost of goods sold from stock sales by your average inventory investment. Remember that high profits can compensate for low turnover.A good rule of thumb in setting turnover goals is to make sure your turn-earn index (inventory turnover multiplied by your average gross margin percentage) is at least 120. For example, this can be accomplished with six turns at a 20% gross margin or four turns at a 30% gross margin.

**Customer Service Level.**
The customer service level is the percentage of line items for stock products completely filled or shipped in one transaction by the date promised to the customer. If the customer orders 10 pieces of a product you must deliver all 10 to get credit towards the customer service level. Most companies aim for an overall customer service level of 95% (95 out of every 100 product requests are completely filled) and a 99% customer service level for critical items.

**Let's get the new year started right. Change your corporate culture to embrace these three simple best practices. You will experience great results both in customer satisfaction and increased profitability!**

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## ABOUT THE AUTHOR - JON SCHREIBFEDER

Jon Schreibfeder is president of Effective Inventory Management, Inc., a firm dedicated to helping manufacturers, distributors, large retailers and service organizations get the most out of their investment in stock inventory. Jon has designed several inventory management computer systems and has also served as a distribution industry "troubleshooter" for two major computer companies.

Over the past 30 years, Jon has helped more than 2,000 firms improve their productivity and profitability through better inventory management. He is the author of numerous articles and a series of books on effective inventory management, including the recently-published Achieving Effective Inventory Management – Fifth Edition and the National Association of Wholesale Distributors' Guess Right – Best Practices in Demand Forecasting for Distributors. Additionally, Jon is a featured author and presenter for eSoftware Professionals (www.eFoodERP.com).

A featured speaker at seminars and conventions throughout North America, Latin America, Europe, Asia and the Pacific Rim, Jon has been awarded the title Subject Matter Expert in inventory management by the American Productivity and Quality Center. He is an advisor and guest lecturer in the Industrial Distribution Program at Purdue University.

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