

## STACKING UP THE BENEFITS

### Effective inventory management

In some of our earliest articles, we focussed on why you even hold inventory and why you need to manage it – and often – the reasons are strategic.

If you do not improve service levels for example, you might lose a franchise or distributorship.

In this article we want to focus more on the financial results and the impact you can have on the P&L and the balance sheet, through more effective inventory management.

#### Higher Prices – More Sales

You can improve the revenue line by:

- Raising the price and / or
- Selling more

To raise the price you need to provide value. Ideally, that is something like saving the customer time in finding and ordering a product, possibly one that is rare.

Achieving this however, may involve extending your range, which of course has risks. If you can achieve a reputation for service, however, then that can translate into real dollars.

If you run a 10 million dollar turnover business, then even just a one percent uplift in price can be worth it, and five percent almost certainly so.

You can also sell a greater quantity of product. In the aftermarket, that means one of two things – expand the market, so people make more discretionary purchases of accessories and the like, or you sell more of each product by taking share from your competitors.

The latter is of course often very difficult as you will likely have to reduce margins to grow volumes, and that can be difficult to get right. You really need to line up all elements of your strategy if you are to be successful in doing this. For example, if you want to grow share and volumes you will often want to lower your costs significantly too.

Ideally, your inventory management strategies and tools will help you extend your range without incurring too much risk. The holy grail is to raise prices and to raise volumes. Having a part that someone really wants can be a very effective way of delivering higher gross margins i.e. 10-20 percent or more above your normal levels.

Having a lot of parts with higher gross margins is even better. However, you have to be very careful you manage the range very well so you do not lose focus or control.

#### Reduced Costs

There are many ways to reduce costs:

- Buying better, but you need the time to make the strategic buying decisions that deliver better costs
- Taking advantage of buy breaks when they are available, but doing so judiciously so that you

do not incur too high holding costs or obsolescence risks. You could easily achieve savings of five percent or more for the right products

- Packing your incoming containers to the brim so you reduce your transport costs, but top them up with product that will turn quickly. Of course to do this requires cooperation with your suppliers
- Reduce emergency stock transfers. By getting your inventory levels right you can reduce express freight. Also emergency orders often involve less efficient processes associated with the handling of small orders for individual customers
- Avoiding write downs and write offs. As we explored in the March article, 'The Excess of Evil', you can totally wipe out all the life time profit for a product if you get it wrong

Usually, however, these efforts all involve risk. You need to invest more in inventory in order to reduce a cost, or alternatively you run the risk of damaging your service levels.

The trick of course, is to have the right tool that enables you to make the right decisions for the thousands and thousands of products in your range, and keep making them day after day after day.

If you get these sorts of things right then putting an extra one to five percent of revenue onto the bottom line through better cost control is not beyond the realms of probability.

#### Improved Productivity

It is possible to achieve significant improvements in productivity. One of our clients, for instance, achieved a five-fold improvement in purchasing productivity.

This only happens with the right tool and master data that is maintained to enable you to drive a policy driven approach that eliminates a lot of trivial administration.

You have to decide how to harvest the benefits from such a productivity lift. You could just reduce the expense base, or you might however, be better served by having someone with the right skills work on better product sourcing.

How can you eliminate costs by better integration of your processes across your network, and with your suppliers and customers? You need to establish where you can achieve the best multiplier on your efforts.

#### Reduced footprint

A lot of benefits can however be achieved by delivering more with less. When it comes to inventory, that means perhaps stocking two and achieving the right result rather than stocking three. Just saving one unit of stock for one product might



not seem much, but if you add up these sorts of savings across thousands of products the benefits can run into millions.

Techniques like Common Quantities (November 2014) can help you make these subtle but very powerful decisions all the time and to do them on autopilot.

When you do manage to improve your inventory turns, all sorts of other benefits can flow. Overflow storage sites, perhaps with a 3PL are all too common, and often expensive. Eliminating these sorts of efficiencies can reduce working capital but also the double handling inevitably associated with them. Savings could easily be worth hundreds of thousands or more.

#### A Balancing Act

We would encourage you to look at your business strategy and look through all the elements of your P&L and Balance Sheet. There is one theme however that runs through virtually every area of potential prizes – for every reward there is an element of risk.

You need to balance the extra investment you make in range against the extra reputation and margin you can obtain. If you take advantage of a buy break and buy more, how confident are you that you will sell the extra you put into stock, albeit for hopefully a short time.

The challenge therefore is not just to have a once in a while look at the potential benefits but to do so on an ongoing basis, every month and even every day. That way you can move in the right way as the optimal settings shift over time. The trick is to keep the benefits balanced.

For further information consult  
[www.horizoninventory.com.au](http://www.horizoninventory.com.au) or email  
[info@horizoninventory.com.au](mailto:info@horizoninventory.com.au)