Distribution Center
MANAGEMENT
July 2012
Managing people, materials and costs in the warehouse or DC

From the Golden Zone

To convince bosses to shed inventory, produce analytical evidence

By Fred Kimball, Distribution Design

The number-one reason DC management contacts a consultant for assistance is space — usually the lack thereof.

It often takes pallets stacked on top of each other in the rack aisles before executive management authorizes a consultant. Productivity has declined, getting the orders shipped on time is more challenging, and people wonder why.

The number-one reason for the shortage of space? Excess inventory. It is not the fault of the DC management that the facility is overfull. Operational leadership is usually vocal about the reason for the operational decline, but the cries of "too much inventory" are dwarfed by the need to avoid backorders or to get a lower cost by buying a boatload.

When it comes to making your case to shed excess inventory, the devil is in the details. Complaining about excess inventory does not change bad habits. It is time for DC management to stop pointing out the obvious and offer real analytical evidence to explain the problem in ways that encourage executive management to take action. It is hard to defend bad behaviors when the numbers provide compelling reasons for change. The devilish details are usually undeniable.

Here are some techniques for grabbing the attention of executive management:

Executive sponsor. No one appreciates being blindsided. Your analysis may shed some unfavorable light on long-standing practices in the company, and maybe on some individuals. It is not that people have done things to deliberately cause operational hardships in the DC; it is that they do not know the reasons for doing things differently. They need to learn, and that is the purpose of your analysis. Your sponsor will help pave the way for your efforts and help you address company politics.

Velocity profile. You will need a spreadsheet that lists all the SKUs with each SKU's current inventory on hand in units or cases and each SKU's units (or cases) shipped for the past 12 months. You do not need to be concerned that the inventory is just a snapshot of one point in time.

Sort the spreadsheet in declining order of units/cases shipped so the highest velocity SKU is at the top of the list. Next, divide the SKUs into velocity groups such as high, medium, and low. How you divide the SKUs is not as important as choosing an approach that makes sense for your company. One company learned that 60 percent of it's SKUs represented the bottom 3 percent of the units shipped.

Inventory by velocity group. Determine the inventory on hand for each velocity group. The company mentioned earlier found that the inventory of low-velocity items was 24 percent of the inventory on hand. Twenty-four percent of inventory for items with 3 percent of units shipped is an inventory out of balance.

Zero-ship items. These are SKUs with inventory on hand that shipped zero units in a year. Maybe these are new SKUs that have not started to ship yet, but it is more likely that most of them are dead items. An apparel company learned that 18 percent of its inventory was zero-ship items. Therefore, 18 percent of the warehouse's storage space was occupied by dead items. This is "found space."

Inventory profile. Put the month-ending inventory in units for the past year into a chart. Then add a line for the units shipped in each month. Does the relationship between the two lines seem to be in sync? If so, Procurement may be doing a good job of securing the inventory just before the shipping peaks. If the pattern between inventory and shipping appears helter-skelter, perhaps Procurement could use some help.

Months of supply on hand. Using the velocity spreadsheet, determine the average monthly units shipped for each SKU. Then divide the current inventory on hand by the average monthly units shipped to determine how many months of shipments the inventory would support at the average selling rate. (Note: the zero-ship SKUs will have a "divide by zero error"; you can plug in an arbitrary 6 or 12 months supply for each of these items since the inventory can support an infinite time period.)

Next, sort the spreadsheet based on declining months' supply. You may find the results shocking. The apparel company found items with over 12,000 months of supply on hand based on the current selling rate. That is over 1,000 years. Over 25 percent of the SKUs had more than a year's supply on hand. The SKUs with more than a year's supply accounted for over 40 percent of the total inventory.

In total, the company's inventory had 2.7 months of supply on hand. That is not bad, but the total hides a very severe inventory management problem. You have to get into the details if you expect executive management to listen and take actions to provide relief.

As principal of Distribution Design Inc., Fred Kimball has evaluated 400-plus logistics operations ranging from 5,000 square feet to 2.4 million square feet. He can be reached at 800-679-3233 or fkimball@distdesign.com. DCM

Distribution Center Management

712 Main Street — Suite 187B, Boonton, NJ 07005-1450

Telephone: (973) 265-2300 • Fax: (973) 402-6056 • Email: info@DistributionGroup.com • Website: www.DistributionGroup.com

Distribution Center Management™ is published monthly by Alexander Communications Group, Inc., which provides news, data and information on key distribution and warehousing topics though newsletters, books and website.