

Organizing a Company to Achieve Effective Inventory Management

By Jon Schreibfeder

What is Effective Inventory Management?

“Effective inventory management enables an organization to meet or exceed customers’ expectations of product availability with the amount of each item that will maximize net profits or minimize its total inventory investment.”

What is necessary to achieve the goal of effective inventory management?

Effective inventory management requires that your company masters two different subjects:

- **Inventory Control** – Protecting the inventory stored in your facility and minimizing the cost of filling orders. *That is controlling what you already own.*
- **Inventory Management** – Replenishing stock inventory with the right quantity, of the right item, in the right location, at the right time. *Managing your inventory investment to maximize your net profits while maintaining your customer service goals.*

What does it mean to “stock” a product?

When you stock a product in a particular warehouse or branch you are making a commitment to have reasonable quantities of that product available for immediate delivery to customers.

How do different people contribute to achieving the goal of effective inventory management?

One person, on their own, cannot achieve effective inventory management. It takes cooperation and a commitment from most, if not all, the people employed in your organization.

Salespeople:

- Salespeople should be in almost constant communications with customers. They are probably in the best position to determine what you must have in inventory to meet your customer’s expectations. That doesn’t mean that you must carry anything and everything that a customer might ask for someday. It does mean that your customers’ impression should be that your inventory better meets their needs than the stock of your competitors.

- Help develop the forecast of future sales of each product. Your salespeople are also in the best position to observe your customers' changing needs over time. They should help determine why there was a large discrepancy between a forecast and what was actually sold in a specific week or month. For example, why did a customer buy an unusually large quantity of an item? Will this be a new ongoing requirement or was it a one-time only sale? Studying unusual sales activity can provide salespeople with valuable information for increasing future sales!
- Help keep inventory records accurate. Salespeople are usually very empathetic with their customers. They often will go to great lengths to meet a customer's needs. However, salespeople must follow your established rules for properly recording all material disbursements. For example, salespeople should not take material out of a warehouse without properly recording it in your computer system.

Purchasing or Replenishment Personnel:

Purchasing agents, buyers and inventory planners must make sure that inventory is available to meet the sales or usage forecast. While accomplishing this primary and most important goal, they must replenish stock in such a way to either maximize your profitability or minimize your total inventory investment. Decisions they must make include:

- Deciding the best source of supply for each product in each stocking location. Do you buy it? Or are replenishment quantities transferred from a central warehouse or distribution center?
- Determining the quantity to buy of each item. This can be either the economic order quantity or just enough to last between deliveries from the supplier. The economic order quantity (i.e., EOQ) balances the cost of the material, the carrying cost of inventory and the cost of issuing and receiving replenishment orders. It is designed to maximize your profitability. Buying just enough to last between deliveries will minimize your total inventory investment.

Warehouse Personnel:

Warehouse personnel are just as important as salespeople and buyers in achieving effective inventory management. They must:

- Organize stock in the warehouse to minimize the cost of filling orders. After all you ship material far more frequently than you receive it. It makes sense to store material to maximize the efficiency of the order fulfillment process.
- Keep inventory records accurate. If the quantity in the computer system does not agree with what is in the warehouse, salespeople won't know what is available for sale, and buyers will not replenish inventory at the right time. This task involves conducting full physical inventories or cycle counting certain products each day.

IT Personnel

A distributor cannot be successful without good computer hardware and software. IT personnel are responsible for implementing and managing this key to achieving your goals:

- Ensure that all necessary data has been entered. Check lists should be established for the information required for each new stocked item, vendor, warehouse and product line. IT personnel should verify that the supplied information is correct and that codes and descriptions are consistent. For example, “lubricant” must be consistent in all product descriptions. You might use “lubricant” or “lube” but the same word should be used in the description of all applicable items.
- Provide training and support users can understand. This facilitates efficient operations at the lowest possible cost. Remember that sales, purchasing and warehouse people all have distinct areas of expertise that are necessary for the success of your organization. However, they are not computer experts and can easily become confused and frustrated in their interaction with IT equipment and software. Support personnel should avoid answering questions with phrases like:
 - “What you are asking for is impossible”
 - “The results may not make sense but the system is performing as it was designed”
 - “How many times do we have to tell you the same thing?”

Attributes of Key Personnel

In order to achieve the goal of effective inventory management you must be sure that you have the right person in the right position. For example:

Warehouse Manager

Your policies and procedures must be enforced in order to you to achieve effective inventory management. Often companies will promote the warehouse employee who knows most about your inventory to the position of warehouse manager. Unfortunately unless this person is a leader, the results may be disastrous. While he or she probably will work hard, they may not have the ability to lead others. As a result they may adopt the attitude of “if you want it done right....do it yourself.” Often these folks burn themselves out while other warehouse employees stand around and watch them do it.

A good warehouse manager must be a leader. He or she must:

- Be able to set and achieve goals (e.g., “all orders received by 3pm will be shipped the next day” or “all stock receipts will be processed within 24 hours of arrival”)
- Insist that all policies and procedures are followed
- Not be afraid to provide constructive criticism when necessary

- Be neat in appearance and insist on a neat workplace

Receiving Personnel:

Assign people who have the best knowledge of your products the job of receiving material and putting away stock. Many companies start new warehouse employees in the receiving department. These people may be eager, and have good intentions, but they don't know your inventory. They may mix items that are similar in appearance, but are actually quite different. Or, they might be afraid of asking too many questions and "stash" products they can't identify. After all, out of sight, out of mind. How often have you heard someone say something like?

"Yeah, I saw those D345J's come in. They were right over there. But I don't know what happened to them. We've searched everywhere but can't find them....."

Always remember that lost material is extremely expensive. Experienced people know your products. They know the difference between similar looking items. And, they know how to put away stock so that customer orders and outgoing transfers can be filled quickly, with a minimum of effort.

Order Pickers:

Have new people fill orders. It's a great way for them to learn your products, your customers, and your paper flow. And, just as important, it's easy to check their work as the orders they pull are packed for shipment.

Purchasing Agents and Buyers:

Many organizations allow individual branches or warehouses to decide when to reorder products as well as the quantity to buy of each item. However, better inventory management occurs when one person or group is responsible for replenishing specific product lines throughout a region or your entire organization. These individuals can focus on your total corporate inventory performance and profitability.

Understand the different roles of purchasing agents and buyers:

- Purchasing agents negotiate with suppliers. They work out discounts, payment terms and other considerations. These individuals have to have good management and negotiating skills.
- Buyers supervise and coordinate forecasting and replenishment tasks. They have to be detail oriented and be experts on your software system.

Remember that employees are the key to success in any organization. Every individual should be placed in a position that will utilize his or her unique skill set. And, appropriate compensation should be provided for well done work!

Test Your Knowledge

1. What is the goal of effective inventory management? (Choose one)
 - a. To always have whatever customers want, regardless of the cost
 - b. To meet or exceed customers' expectations of product availability with the amount of each item that will maximize net profits or minimize your total inventory investment
 - c. To maximize inventory turnover

2. What is not a responsibility of salespeople? (Choose one)
 - a. Deciding what products should be stocked in each location
 - b. Deciding how much of each product should be stocked in each location
 - c. Helping to develop the forecast of future demand of stocked items

3. What is the responsibility of warehouse personnel? (Choose all that apply)
 - a. Issue replenishment orders for stock items
 - b. Organize products in the warehouse to minimize the cost of filling orders
 - c. Maintain accurate on-hand quantities of products
 - d. Decide when quantities of products should be transferred to other warehouses

4. Where should your most experienced, technically knowledgeable, warehouse employees work? (Choose one)
 - a. Order fulfillment
 - b. Receiving and stocking products
 - c. Warehouse management

Test Answers:

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