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3 KEY COST CONTROL STRATEGIES FOR OPTIMIZED INVENTORY MANAGEMENT

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INTRODUCTION

In today's global marketplace, with increasing competition and customer-driven demand, business success for manufacturers is defined by the ability to deliver the right quantity—of the right item—at the right location and price—at the right time.

Inventory is one of the most significant costs for a manufacturing business, so its optimization should be *(needs to be)* a key corporate objective. Increased globalization, competitiveness, and supply chain complexity have put immense pressure on manufacturing leaders to exert more control over the flow of raw materials, finished goods, and the facilities that store them. Investment in these areas represents working capital that is currently tied up. Today's business leaders need to embrace formal inventory management strategies, in order to improve cash flow, reduce costs and realize optimal revenue potential.

Despite the variety of industries, most manufacturers and distributors typically have very similar inventory-related problems:

- **Too much of some products:** This excess inventory and dead stock leads to decreased turnover and profitability.
- **Stockouts of other products:** This results in back-orders, lost sales, and dissatisfied customers.
- **Questionable stock:** The on-hand quantity does not agree with what is on the shelf, in their warehouse.
- **Unknow location of stock in their warehouse:** They know the material is "out there, somewhere" but they don't know exactly where it is located.

This solution sheet outlines three leading strategies for successful inventory management, as well as highlights:

- Common roadblocks or obstacles to successful inventory management
- What effective inventory management should look like
- How automation and technology, such as ERP, can reduce expensive inventory costs

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COMMON ROADBLOCKS OR OBSTACLES TO SUCCESSFUL INVENTORY MANAGEMENT

For manufacturing leaders, inventory management can feel like a risky balancing act. Not having enough of the "right" inventory can spell disaster for meeting customer orders. However, having too much inventory or the "wrong" inventory on hand can also negatively impact your bottom line. Inventory is money that's been invested at a negative rate of interest. The longer it sits unused, the more it costs. Inventory ties up a business' cash reserves, and it occupies expensive warehouse space.

Moreover, with increasing levels of globalization and economic uncertainty, manufacturers are facing tighter margins than ever before. For this reason, manufacturing executives recognize the need take control of their inventory management strategies.

Common roadblocks or obstacles to successful inventory management, can include:

Complex, global supply chains: To combat volatility, manufacturers feel they need to have more inventory on hand, to respond to fluctuations and unforeseen spikes in demand.

Customer-driven expectations: Customers require higher degrees of product customization, shorter lead-times, and higher quality products—all at lower costs. This results in poor sales forecasting and complex inventory management.

Inaccurate inventory reporting: A lack of visibility into inventory levels can lead to rogue and reactive purchasing, and increased storage costs.

Lack of vendor communications: A good relationship with your vendors is crucial to your company's success. If you are not in constant and consistent communication with them, you run the risk of your fulfillment providers tarnishing your brand.

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WHAT EFFECTIVE INVENTORY MANAGEMENT SHOULD LOOK LIKE

Inventory management is a continuous, concentrated effort—and a process that shouldn't be handled solely at the operations level. A successful inventory management plan should connect all the departmental strategies of your business into one integrated plan—improving alignment, responsiveness and synchronization amongst all business functions of your organization.

DEPARTMENT	SYMPTOMS OF POOR INVENTORY MANAGEMENT	BENEFITS OF EFFECTIVE INVENTORY MANAGEMENT
Purchasing	▪ Too much/too little inventory ▪ Rogue and reactive purchasing ▪ Lack of visibility into actual stock levels	▪ Reduced product shortages ▪ Improved inventory turnover ▪ Accurate and streamlined planning
Operations	▪ Disrupted factory production ▪ Increased lead times and costs ▪ Decreased employee productivity and morale	▪ Reduced production downtime ▪ Constant flow of products ▪ Improved employee efficiency and satisfaction
Sales	▪ Disgruntled customers—reputational risk ▪ Reduced re-occurring orders ▪ Lost revenue	▪ Increased customer satisfaction levels and loyalty (return/lifelong customers) ▪ Increased revenue potential ▪ Improved bottom line
Logistics	▪ Expensive warehouse costs ▪ Shipping and delivery delays ▪ Strained relationships with vendors	▪ Reduced warehouse costs ▪ On-time customer delivery ▪ Improved vendor relationships
Finance	▪ Extended cash-to-conversion cycles ▪ Increased expenditures on unnecessary labor, material and warehouse costs ▪ Working capital tied up in unused inventory	▪ Improved cash-to-conversion cycles ▪ Reduced operating costs ▪ Better cash flow
Executives	▪ Poor/reactive decision-making ability ▪ Lost revenue and profits ▪ Dissatisfied/lost customers—reputational risk	▪ Proactive decision-making ▪ Increased revenue and profits ▪ Loyal customers and employees

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There are several ways to improve inventory management, to reduce overall costs.

Forecast Better

Make a plan, then execute. Most businesses plan because connecting the sales side of the business with the production and procurement side of the business is imperative for success. A lack of planning is often a symptom of a chaotic business.

If you are like most businesses, you create your annual budget and fixed annual operating plan (AOP) for the year. Your forecast is done. Volumes are set. Detailed departmental budgets are also complete. Operating levels are set. Sales targets and/or commissions are also done. But, as everyone knows…plans change. Having a budget is not good enough to avert disaster.

When demand can be predicted accurately, it can be met in a timely and efficient manner—keeping both partners and customers satisfied. Accurate forecasts help to avoid lost sales or stock-out situations, and prevent customers from going to competitors.

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Forecasting can be a delicate balancing act for manufacturers that feel pressure to be nimble, while still satisfying the demands of a volatile marketplace.

The most important aspect to better forecasting is a complete understanding of what it actually is, and of equal importance, what it is not. Regardless of whether a company sells goods or services, it must have a clear picture of how many of those goods or services it can sell—in both the short and long-term. That way, the business can plan to have an adequate supply to meet customer demand. Forecasting is critical to a company's production or operations departments.

Sales and Operations Planning (S&OP) is a business management process, that aims to connect corporate business planning with tactical planning. It drives master scheduling and distribution planning, to support the business plan and meet demand. With successful S&OP, businesses can proactively manage supply and demand—to ensure against any mismatch.

Most importantly, S&OP connects all the functional departmental strategies of a business into one unified plan. It aligns sales to production, and drives effective supply chain and inventory management when correctly implemented. Sales and Operations Planning determines when and how much raw material to bring in to meet forecasted orders, and plan production schedules—to meet customer demand.

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Focus on Demand

Supply chain management is more than just inventory control—it determines your customer experience too—dictating whether you have the product available to meet customer demand, and managing the time it takes for the product to get to the customer.

Unfortunately, according to the Demand Driven Institute, the problem in today's world is that the supply chain is broken. Many organizations rely on old business processes that simply no longer work. Companies are finding it increasingly difficult to use their current, legacy systems to keep up with the complexity of today's supply chain. Furthermore, the demand put on supply chains nowadays is far greater, and the needs are becoming far too complex for many companies to meet this demand. The paradigm shift of today's world is wreaking havoc on manufacturing environments.

Demand Driven Material Requirements Planning (DDMRP), is a multi-echelon demand and supply planning, and execution methodology. It integrates multiple tiers (including the bill of material) into the supply chain, in order to provide end-to-end integrated planning and execution visibility.

DDMRP takes Lean's waste reduction focus and visibility for execution, and combines it with a new set of demand-driven planning tactics, to generate clear planning visibility across an enterprise and supply chain. The results are synchronized demand and supply signals that make capacity scheduling simpler for a company, in order to maximize their supply chain.

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DDMRP encompasses the following manufacturing principles:

- MRP – Material requirements planning
- DRP – Distribution requirements planning
- Lean – Eliminating "Muda" or waste
- TOC – Theory of constraints
- Six Sigma – Eliminating defects
- Innovation

Due to the strategic and thorough planning process that it facilitates, DDMRP is a relatively easy inventory planning strategy to execute. The simple to understand zone coloring (red, yellow, green, blue), synchronization alert warnings, and real-time access to inventory, allows companies to reap several business benefits, including:

- **Improved customer service:** Achieve 97–100% on-time, fill-rate performance
- **Reduced lead times:** Decrease lead times by 80% in certain industry segments
- **Reduced inventory:** Lower inventory levels by 30–45%
- **Reduced costs:** Eliminate most costs related to expediting activities and false signals with fast freight, partial ships, cross-ships, and scheduled break-ins
- **Improved visibility:** View real priorities instead of mixed messages from MRP system

DDMRP allows manufacturers to plan for their production needs—while keeping inventory strategically streamlined and costs at a minimum.

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Integrate Systems, Automation and Business Solutions

Maintaining accurate counts of inventory, while reducing the amount of time spent moving and totalling the number of items around the warehouse is a huge challenge for manufacturers. This is where automation can play a critical role. Leaving paper processes behind and investing in a true inventory management solution helps to ensure that your business has the best visibility into the on hand inventory levels, as well as, opportunities to reduce costs, and improve inventory management processes.

As a manufacturing leader, you are likely familiar with the concept of Material Requirements Planning (MRP).

MRP is a production planning, scheduling, and inventory replenishment system used to manage the requirements for materials. Most MRP systems are software-based, although it is possible to conduct MRP manually, as well. MRP has three main business objectives:

1. Ensures materials are available for production and products are available for delivery to customers
2. Maintains the lowest possible material and product levels on hand
3. Plans manufacturing activities, delivery schedules and purchasing activities

MRP allows companies to plan in advance, schedule production, and allot the necessary time based on capacity needs, while also meeting material needs. It enables businesses to plan manufacturing, purchasing, and delivering activities—while maintaining low inventory levels, and keeping costs to a minimum. Most MRP systems will include inventory control, bill of material processing, and scheduling. Most costing systems use elements of MRP data, such as bills of materials.

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Inventory management solutions will help manufacturing leaders:

- Increase inventory management efficiencies
- Automate inventory processes
- Attain real-time reporting and transparency
- Reduce unwarranted inventory costs

Enterprise Resource Planning (ERP) software provides manufacturers with a strong foundation for integrating and automating key business functions, including core operational and planning processes. ERP solutions that integrate with MRP and business methodologies such as S&OP and DDMRP will return the greatest financial return on inventory management.

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ERP software provides a central planning hub and execution engine that brings together material requirements planning, production scheduling, process forecasting, and capacity requirements planning functions. This integration supports core functions including, sales, order-entry, inventory, shop floor control, purchasing, and finance, that automatically flow relative to associated operational transactions. Manufactures can better focus on meeting current critical needs and order fulfillment metrics through integrated Material Requirements Planning (MRP). They can also increase inventory turns by integrating forecasting, planning, and materials management functions across the board.

ERP solutions will help manufacturers better plan for, and meet, market expectations—while saving money, by achieving the following business benefits:

- Reduces reliance on forecasts
- Eliminates shortages
- Solves for availability problems with Lean implementations
- Works with complex Bills of Materials
- Reduces inventories while improving customer service
- Compresses lead times
- Allows for an integration path with traditional master planning and S&OP processes

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CONCLUSION

Historically, businesses have employed the basic inventory management techniques or inventory control methods to keep their inventory costs in check. Inventory management has become an intrinsic part of today's supply chain management. The ability to reduce costs, improve business operations and improve quality by improving supply chain processes has reached epic proportions in today's manufacturing landscape.

The ultimate goal of effective inventory management is to balance customer needs while minimizing the cost of carrying excess items.

There are numerous ways to take better control of inventory and decrease its associated costs. Many of the strategies outlined in this primer may seem challenging to implement; however, they have all been used effectively in manufacturing organizations for years. The key to managing inventory successfully is to continuously measure your performance and look for new ways to improve.

With smart inventory management, your manufacturing organization will enjoy many business benefits including, improved cash flow, reduced costs and optimized revenue potential.

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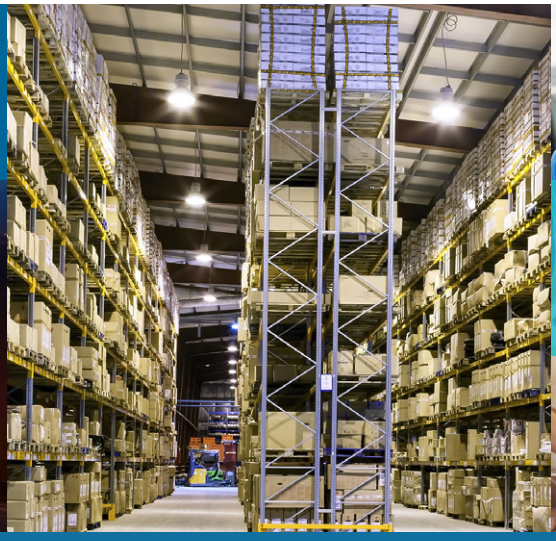
ABOUT SYSPRO



Established in 1978, SYSPRO is an industry-built Enterprise Resource Planning (ERP) solution designed to simplify business complexity for manufacturers and distributors worldwide. SYSPRO provides an end-to-end business solution for optimized cost control, streamlined business processes, improved productivity, and real-time data analysis for comprehensive reporting and decision-making.

What sets SYSPRO apart is an unwavering, sustained focus on the manufacturing and distribution sectors. Combined with a practical approach to technology and a passionate commitment to simplifying business processes, SYSPRO dedicates itself to the success of its partners and customers alike.

SYSPRO is highly scalable and can be deployed either in the cloud, on-premise, or accessed via any mobile device.

NEXT STEPS:

If you want to learn how SYSPRO can help with your inventory management strategy to reduce costs, contact us today at info@ca.syspro.com or +1 (888) 259-6666.