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IMPROVING INDIVIDUAL AND ORGANIZATIONAL PERFORMANCE

## Improve Profitability Through Supply Chain & Product Design Enhancements

Customers rarely buy what we think they will buy. They, instead, buy what they need, when they need it—just like you and I do. Their customers' projects sometimes go off-track necessitating a change in product orders. In reality, they can fall victim to the same inventory and business scenarios that your business does.

Controlling the inventory levels and the financial consequences associated with it is a never-ending balance between too much and too little. The finance department reports too much inventory destroys profits while the sales department also states too little inventory causes lost sales revenue which destroys profitability.

Who is right? Both of them? Neither of them?

The reality is that both of them are correct and this is the dilemma of every business that sells physical products. The dilemma is that excess inventory can always be (negatively) quantified in the month-end financial reports but revenue missed due to insufficient stock is rarely measured. This simple disparity in measurement practices can drive the wrong behaviors and cause missed profit.

### Getting it Right is Never Good Enough

One of my mother's key phrases when I was a child was "I'm damned if I do and damned if I don't." This didn't really sink in until I started working with inventory planning. When you have too much inventory, finance gets very nervous—too little inventory, salesmen and customers get angry. Worse still, even if the numbers are good enough to service all customers on time with very little remaining in stock, finance might say "why do you need to keep 2 in stock?" and sales may say "if only we had had 4 in stock I could have won a big deal." DIYD,DIYD.

Balancing the needs of your business is the key to success. Doing this correctly will keep everyone a little uneasy but tolerable. Some factors to consider when defining balance are:

- growth requires inventory - the faster or the more varied the growth, the more inventory needed
- tolerance for risk, in finance and in the C-suite
- your marketshare position versus desired position



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### **Improving Profitability**

There are numerous challenges in inventory planning—many more than can be presented in a brief article. However, here are three actions that can be initiated today that will demonstrably improve inventory usefulness.

#### **SOLIDIFY THE SUPPLY CHAIN**

The concept of “solidifying” the supply chain is beyond just making sure it is stable and secure. Solidifying it means to make act as one “solid” piece. If your supply chain contains multiple suppliers, which it will, then they will all act together as one company. If you have to deal with other divisions of your large corporation, then the concept is the same as with external partners, except it will probably be more difficult to accomplish.

Solidification Concepts:

1. the entire supply chain must act as if it's from one company
2. companies freely communicate relevant data with partners to maximize production efficiency and shorten lead times
3. successful inventory planning requires input from many departments—not just sales
4. finally, gain trust first and then work to improve communication

#### **MEASURE LOST SALES**

One of the missing sets of critical information is a metric of lost sales due to inventory shortages. Tracking lost sales provides a health check on the entire inventory planning process. These data combined with sales and total inventory data gives a complete view of how sound a process is in place.

Implement a mechanism that documents sales lost because of inventory shortages. This is typically difficult to accomplish because there is “nothing” to record - no sale leaves little to record. An alternative to quantification, is a qualifying report. Sales leaders can document anecdotal information and report on the known issues. Not a perfect system, but I know of few that are. Some information, properly vetted, is better than no information.

#### **IMPROVE PRODUCT DESIGN**

Lastly, how a product is designed has implications on supply chain and inventory flexibility. The product line manager and the R&D team need to clearly understand the inventory system and the customers' needs before they get too far into the design phase. Seemingly simple design choices can increase the lead-time by weeks or months. While this may provide a better or less expensive product, the benefit may be short-lived if the inventory carrying costs swamp the savings.

Have in-depth conversations with leaders at all stages of the product, and its components', supply chain. Understand which are the few components that most affect lead times and flexibility and modify the design accordingly.



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## Conclusion

I agree with the successful businessmen I know who state “you make your money when you buy, not when you sell.” The market sets the selling price, not you. Inventory costs are what you are “buying” but the good news is that you do have significant latitude in your supply chain decisions and resulting savings. Using the tips above to design your supply side will help tip the balance of the profit & loss equation to your favor.

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