Managing Inventory with Inventory Turns

A Quick Guide for Christian Booksellers

Importance of Managing Inventory

When you're buying inventory for your store, what types of constraints do you take into consideration?

Past / Future Demand	Available Space	Available Cash
Credit Card Limits	Product Freshness	Presentation
	Etc.	

In a perfect world, we would establish inventory levels that help us:

Maximize Sales	**Minimize Inventory Investment**

But, these TWO Business Goals are at war with each other.

> *"Inventory management means finding a balance between these two conflicting goals while considering all other constraints."*

Every buying decision affects these two goals.

To the Rescue: Inventory Turns

"Inventory Turns" is a simple tool that we can use to manage inventory better. Simply: It is the number of times you sell your average inventory in 1 year.

Simple Example: April's Apple Cart

- April keeps **10 apples** on hand at all times.
- She sells **120 apples** per year.
- **120 apples sold / 10 avg inventory = 12 turns.**

> April has TURNED her inventory **12 times** in one year!

Your Turn Number acts as a **multiplier** to profitability. In general, a higher turn ensures that every dollar you have invested in inventory is working as hard as possible for you to:

generate more **gross profit** dollars over time	reduce **cash outlay**	improve **cash flow**

Practical Uses

Use Turns in these THREE ways:

- **Trailing Indicator** = "How did we do?" - Review last year's performance.
- **Current Indicator** = "How well are we currently positioned?"
- **Inventory Goals** = "How should we buy going forward?"

Turning Inventory Into Profit

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What is a good Target/Goal for Turns?

There are a couple of ways to determine what a good "turn" for your inventory would be:

- **Industry Averages:** Ask your marketing group, data provider or other retailers to find the industry average.
- **Your own History / Experience:** The more you track this number, the better you will get a feel for how well you are servicing your customer and managing your inventory budget.

For reference, our industry probably averages around 2.5 - 3.0 turns, but higher could be better. It is not necessary to adopt that number for your store, but it can be used as a guide.

Set your Goal Turn based on business conditions and goals.

Effects of HIGH-er Turns Goal

- **Pros (Desired outcomes):**
  Decreased Inventory
  Decreased cash tied to inventory
- **Cons (negative but accepted effects):**
  Potentially lost sales
  Increased order frequency and time required to make more orders

Effects of LOW-er Turns Goal

- **Pros (Desired outcomes):**
  Increased Inventory
  Increased Sales opportunity
  Decreased order frequency
- **Cons (negative but accepted effects):**
  Increased cash tied to inventory
  More space required for more inventory
  Freshness: All products (i.e., apples and communion cups) go bad over time!

How Best to Calculate Turns?

Turns can be calculated in different ways depending on what information you have available to you.

Most Accurate = Inventory at Cost

Pro: Values readily available from P&L and Balance Sheet. **Con:** Trailing Indicator (COGS – remember the "S" is for "Sold" meaning past tense).	**Calculate:** COGS / Average Inventory OH **Example:** \$30,000 / \$15,000 = 2.0 Turns **Your Turn:** COGS: ________ / Avg. Inv. OH: ________ = ________

Easy = Inventory at Retail Value

Note: Use any date range. **Pros:** Values may be readily available. **Cons:** Discounts to customers affects calculation. We don't pay for inventory in "retail" dollars.	**Calculate:** Retail Sales / Inv Value at Retail **Example:** \$180,000 / \$30,000 = 6.0 Turns **Your Turn:** Retail Sales: ________ / Inv. Value at Retail: ________ = ________

Easiest = Units

Pros: Quick, easy and close enough when used for categories. **Cons:** Can be misleading with items of varying prices.	**Calculate:** Units Sold / Average Units OH **Example:** 4,000 / 860 = 4.65 Turns **Your Turn:** Units Sold: ________ / Avg. Units OH: ________ = ________

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Calculating Turns with Current Inventory

Q: Can you use current inventory levels to calculate Turn?

A: Yes. Using Current Inventory at Cost provides great benefits:

- It gives you an easy way to see how you stand at that point in time
- Lets you know if you should make adjustments which...
- Informs your buying decisions

What can be done to improve turns?

- Return product that has not sold and is still returnable.
- Discount non-returnable product to convert into cash.
- Purchase less inventory more often.

What is the enemy of higher turns?

A: Buying a higher quantity than necessary IN ORDER TO OBTAIN A HIGHER DISCOUNT!
A note of caution: 1 more turn (i.e., lower order quantity) is often equivalent to a 6-7% extra discount.

Replenishment Buying with Turns in Mind

Before making purchasing decisions, know your turns at the:

Store Level	Department Level	Category Level

Applying a Turn Goal to the Individual Item Order Decision

An easy way to achieve a higher turn overall is to apply a "Goal Turn" to your reorder decisions. Let's say the goal for this category is 4 turns. Items projected to sell less than ~3-4 times in a year: you may not want to reorder.

Formula: Order Qty = (Est. Ann. Sales of Item) / SLIDING Goal Turn) - Current OH

Example: Item A, based on history, should sell 24 times this year. We have 3 on hand today.

(24 / 6) - 3 (OH) = 4 - 3 = 1

Expected Annual Sale Quantity	Item-applied Turn Goal
Up to 8 units	4
9 - 15	5
16 - 24	6
Etc.	

Note: *This assumes a lot! Sales are relatively consistent, you order frequently, etc.*

Note: *Round down when being conservative (higher turn) and up for aggressive (lower turn).*

Additional Notes

When setting a goal, attempt no more than a 0.25 - 0.5 turn change in any season.

For example: Sales: $500,000, Inventory (Ret): $250,000 = 2 Turns.

- To aim for 2.5 turns: Reduce inventory by $50,000 through returns and lower replenishment.
- Make sure sales didn't suffer due to the change before making further changes.

Other constraints should always be taken into consideration.

Achieving higher turns becomes less important if dating covers the selling of product (i.e., consignment, for another extreme example!).

Further Resources

Here are some additional resources for in-depth information:

- www.ingramcontent.com/retailers-document/turning-inventory – Although a little old, this is a great, in-depth review of the importance of Inventory Turns and GMROII.
- www.amazon.com/dp/0878380256 - for The Mathematics of Bookselling: A Monograph by Leonard Shatzkin, 1997.
- Questions or want to talk inventory? Contact Link McGinnis – Cedar Springs Christian Store - Link@csChristian.com

April Knows Inventory