DISTRIBUTOR POWER TOOLS: THE INVENTORY OBITUARY
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THE DISTRIBUTION TEAM

One of the most common struggles all distributors face is managing their dead and obsolete inventory. It is one of those back burner items that no one wants to bring up for fear that they will be appointed to deal with the task. Most people like to employ the ostrich approach to dead stock – just stick our head in the sand and hope it goes away.

One of the more novel approaches I have ever heard of took a little help from Mother Nature. This clever individual had a facility right next to a river that flooded seasonally. He had built this large deck overlooking the river in order to entertain customers and employees during the summer months. On a particularly wet year, they received word that the river was going to flood much higher than usual. When life gives you lemons, make lemonade. The distributor hauled all the dead inventory out to the deck. He sandbagged the walls of the facility, in order to protect his turn and earn inventory, and let the rising river manage his dead stock for him. Something tells me that Allstate would take issue with this approach.

The power report I will be discussing this month deals with a more proactive approach to managing dead inventory. As in previous articles, I believe that the key to getting a return on your software investment is to learn how to extract and manipulate data. We all paid a significant sum for our software, yet we typically use only a fraction of the capability. Mastering the report generating function will substantially increase your overall system utilization and give you the tools necessary to make significant improvements to your bottom line.

A number of years ago, my business partner Scott Stratman wrote an article where he stated, "Wouldn't it be great if dead stock would just stink?" As inventory managers, we have a very difficult time identifying the moment in time when a product ceases to be part of our turn and earn inventory. Our lives would be infinitely easier if we would enter the warehouse on the first day of the month and a pungent odor, something akin to dead fish, would tickle our nostrils. We would be forced to hunt down the offending item and eliminate it from the premises. Unfortunately, most of our products do not emit an odor when they parish. Our challenge is to use our software to make them stink.

When I speak to distributor groups, I usually pose the question, "If I wanted to find the dead stock in your building, I would ask for one piece of equipment. What would it be?" Several folks mention the white glove and a dust mask. Perhaps, but I have a feeling that a majority of our live products would not stand up to white glove scrutiny. I would ask for a ladder or forklift. I'm not sure where we picked this up, but we tend to move all the dead stock a little closer to heaven. It could just be the old out of site, out of mind. In many facilities, there is no discernable separation between the dead and the living. Both occupy the same shelf space.

In order to help us identify our dead inventory, we must define the moment of death. We have seen some unusual methods for defining the point in which an item is classified as dead. The rainbow method comes to mind. During an annual physical inventory, many distributors use colored dots to mark the items that have been counted. When a product displays stickers from all colors of the rainbow, it is most certainly dead. I would not suggest that this is the most effective definition. In our practice, we suggest that distributors choose a moment in time. When was the product last sold? The most common definition for dead stock is: zero sales in the past 12 months. There are several distributors out there who need a much shorter window. The paper goods industry uses a much shorter 3 month window. For most hard goods distributors, 12 months is a good place to start. Over time, a distributor can begin to decrease the months. I generally suggest that companies exercise caution when going below 9 months due to seasonality issues. Once a definition has been created, everyone in the company must know it. This is not a time to be secretive. When I work with a private company, it is a big red flag when I get several different answers as to the time of death.

Once we have defined the time of product death, we need to let our software make it stand out. As I mentioned before, most dead items do not appear or smell any different than our living products. Enter the Inventory Obituary. Some folks who use the no sales in 12 months definition refer to this as the "13th month, first day report". Not nearly as colorful, but not all of us are motivated by style points. The report can be formatted in a simple spreadsheet using these columns:
Item Code
Description 1: This will help us pull the item out of the live inventory.
Quantity On Hand
Unit Cost

Total Investment: This is the motivational column.

Date of Last Sale: Exclude anything sold within the last 12 months.

Run the report and this will become your inventory obituary. In order to really turn up the stink factor, calculate the sum of column 5. Don't be shocked if you have a significant amount of money accumulated. Let's just call it job security for some lucky individual to be named later. I will touch on the role of the mortician a little later. Identifying dead products is not an annual event. I recently ran into a software package that recommended running their dead stock report on an annual basis. This is not a good suggestion. We need to be far more proactive than this. If we employed this method, we could tack on an additional 11 months of inventory carrying cost to any items that died in February. I need to know what died every month. Make this report a part of your first day of the month routine.

Once you have run your obituary and identified the dead items, we need to perform some tasks to help prevent further bleeding. As I mentioned above, we have been losing money on these products in the form of carrying costs. Carrying costs accumulate at an average of 25% annually. For example, an item that originally cost us $1.00 will actually end up costing us $1.25 by the time we hold it in our inventory for an entire 12 months.

The first task is to shut off the faucet. Turn off the automatic replenishment controls for all the items on the list. We do not want to buy more. Incidentally, the worst thing that can happen on day 1 of the 13th month is that someone will buy a dead item. All of a sudden, we think there is new life in the product. Out come the shock paddles and we are ready to give mouth to mouth to a stiff. Dead is dead. Let the item rest in peace. Change the controls in your system to identify the item as non-stock.

The next step is to remove the living from the dead. It is one thing to make an item stink on paper; it is entirely more effective to make it stink visually. Create a dead stock graveyard. Move all the dead items to your newly created cemetery. Don't hide the cemetery in the back of the warehouse. We want it visible. We really want the owner to be able to see all the old money accumulated in one place. It tends to give additional motivation when we see a visual representation of the total problem. Some distributors have added their creative side to the project. A few well placed tombstones would not be out of order. Who says you can't have fun in the warehouse?

If you are anything like me, this next suggestion will resonate. I hate to lose money. When we are selling a stinky dead item, our first inclination is to give a discount so that it will disappear. Remember, we have already accumulated an additional 25% in carrying cost. I'm no math major, but if we bring the sell price down and our costs have gone up, this ain't good. Perhaps we need to give ourselves a fighting chance at some cash. My suggestion is that you jack up the price on any dead item by 300%. Since we are going to give someone a discount anyway, why not start from the highest point? When someone calls, do you really think that we are the first person they have tried? We have it, the previous 5 distributors didn't. Gotta love supply and demand.

The final step is to turn the list over to the mortician. Hire a dead stock manager to liquidate your dead inventory. Wait a minute, doesn't this sound like throwing good money after bad? If you structure the position right, it will be a positive contributor to your bottom line. Look for a part-time employee for this position. I happen to like retirees for this job. Pay the person a commission on the dollars recovered – not on gross profit dollars. We are probably going to be selling things below what we paid for them. I have seen commission ranges from 25-50%. Do what works for you. The sole mission of this individual is to make our inventory obituary disappear in 30 days because something new will die every month.

A consistent running of the inventory obituary will yield tremendous bottom line results. At the beginning, the list will seem like an insurmountable task. Over time, and the efforts of a diligent dead stock manager, the list will reduce to an acceptable level. If you need some suggestions on methods of dead stock disposal, please feel free to contact me or look for articles on our website. Purchasing your distribution software was a significant investment. The return on that investment is up to you. Good luck.

About the Author:
Jason Bader is the principal of The Distribution Team. He is a holistic distribution advisor who is passionate about helping business owners solve challenges, generate wealth and achieve personal goals. He can be found speaking at several industry events throughout the year, providing executive coaching services to private clients and letting his thoughts be known in an industry publication or two. He recently launched his first podcast, Distribution Talk. Episodes can be found at www.distributiontalk.com. He can be reached at (503) 282-2333 or via email at jason@distributionteam.com. You can find additional resources on his website: www.thedistributionteam.com