

IS YOUR HUB AND SPOKE EFFECTIVE? BY JASON BADER, PRINCIPAL - THE DISTRIBUTION TEAM



There are many different schemes for managing inventory in a multi-location company. Most start out with locations that control most of their replenishment needs; but over time, most companies will fall into a few bigger locations supporting several smaller ones. This is commonly referred to as “hub and spoke” with the larger location feeding inventory to the smaller locations. The reason for this type of replenishment is that the smaller locations generally do not have adequate sales volume to meet the supplier requirements for economical requirement. Larger locations will feed inventory to the smaller ones through a series of planned transfers via common carrier or company owned trucks. This can be an effective way to maximize purchasing power, but it can also lead to an escalation of expense and constant shell game of sellable inventory. Is your current method satisfying your customer to a high degree or are you just driving up operating costs and causing discontentment in the branches?

This subject has come up twice in the last month, so that is usually a fairly good indicator that I should write about it. Trust me, coming up with topics to write about every month isn't always easy. So, when one slaps you upside the head, you should probably run with it. The first occurrence was in a pod of purchasing managers that I facilitate. We were talking about the challenge of keeping A and B items available for sale in the branch locations. As many of you know, I hate the alphabet designation of ranking because it can be so subjective. “A” is in the eye of the beholder. In this case, we are talking about high hit items. These are the items in the branch that have

the vast majority of transactions on an annual basis. Generally, these are your top 250 – 300 items. When you run out of these, customers become disenchanted and branch managers question the intelligence of the inventory management scheme.

In the second occurrence, a new client shared their discontent with the current inventory replenishment scheme. Although they have had their fair share of stock out on high moving items, the real indicator has been the number of transfers rolling around their geographic footprint. Too many last-minute transfers and some questions on how to support their internal replenishment system. Furthermore, they are pondering a move to a non-selling distribution center. Although this is a common evolutionary step, it does cause some intestinal discomfort to the sales dominated folks out there. Selling versus non-selling hub locations is in interesting debate. I will take a crack at it later in this article.

Fortunately, both of these occurrences have similar considerations and solutions. First and foremost, you need to understand the capabilities and functions of your ERP. If you don't understand how the system handles branch inventory replenishment and how to set it up properly, you are in for a lot of disappointment and a fair of manual work arounds. Neither of these were in the product literature when you invested in the system. Time to head back to school. For the most part, good distribution-based ERP systems have thought through this challenge and given you a solid solution. It may not be the solution you are used to, but it was probably crafted by the multitude of users of a considerable

period of time. Rather than fighting the way the system wants you to move the stuff around the company, perhaps you should give it a chance to work its magic.

When was the last time you had the ERP supplier in to look at how you are using the software? If you have been on the system for a while, it has probably been a few years. A lot can happen in a few years. Software modules are improved and people on your staff change seats. It's probably time for a refresher. This is often called a system audit. These used to be fairly cost effective, but one of my pod participants indicated that some of these ERP companies have jacked up the pricing on their consulting audits. I am going to be very clear in my response here. This is a really stupid and short-term direction. By pricing this in a manner that keeps your users happy and curious about the product, your customers will give you glowing testimonials and become your non-commission sales force. As an alternative to this foolish trend, you should look to other users for help. Many ERP systems have robust user group platforms for you to join. Members of these user groups tend to be very generous with their time and experience. They have often far more adept in system functionality than software consultants.

One of the biggest killers of multi-branch inventory scheme is control. It is fairly common that companies start out with branch managers having the ability to stock their own inventory levels and make most of the purchasing decisions. Whether they are pulling from the hub or sourcing direct from the supplier, this mentality can lead

to poor inventory performance. I understand the reasoning. Yes, these branch managers are closer to the local customers. Unfortunately, this gut instinct and in the trenches information gathering is limited at best. As an individual, you can only mentally process a handful of customers and a small basket of products. Computers are far superior at managing large customer and product data sets. When this data is analyzed by individuals who have been trained to extract it and manipulate the software, branch inventory management improves. In short, centralizing the process of inventory replenishment removes emotion, optimizes the transfer process, and leads to better utilization of the inventory asset.

Moving inventory control out of the hands of the branches can be a challenging process. Taking something away, especially something that may define their role, will have to be thought out and managed carefully. The best way to help smooth the process is to focus on the things that make managers happy. Right stuff, right time, and right place. In other words, make sure that they will not be riddled with stockouts and backorders right out of the shoot. Any backorder will be perceived as one more reason that they could have done it better. Jack up the inventory on high hit items. By eliminating backorders on the most commonly transacted items, the perception will be that central purchasing kind of knows what they are doing. Don't expect a perfect transformation here.

Centralizing the control will also help curb the number of transfers. The first step to tackling a transfer problem is to recognize that there are good and bad transfers. Good transfers are something your plan, such as a hub to spoke replenishment. A bad transfer is when a branch has to grab inventory from another location to satisfy a sale

for inventory not on the shelf. Can you eliminate all bad transfers? Nope. We can, however, greatly reduce them by analyzing the hits ranking of each location. Just as I mentioned above, pay attention to the stocking levels of the higher hit items. I generally divide the stocking SKUs in half. The top half, ranked by hits, are the items that I intend to reduce the number of stockouts in. The bottom half is where I thin out the inventory to pay for bolstering the top half. If I can work within this basic philosophy, I will improve the overall effectiveness of the inventory in the branch.

The debate between a selling hub, or distribution center, and a not-selling location can cause dissension in the ranks. When I think about a distribution center, I really envision a location that is devoid of customers and salespeople and is focused purely on the logistical distribution of products. The real challenge falls between the ears of those who cannot justify an expense without opposing income. There, I said it. This debate is more about tradition, assumption, and emotion rather than efficiency and logic. If we take a look at the wins associated with a large hub location, we might be able to get past the lack of traditional income.

One of the reasons that we open up a distribution center is so that we can accommodate larger purchases and shipments from suppliers. Traditionally, these come with financial incentives such as rebates, discounts, and freight concessions. All of these have monetary value. This is your "income". Unfortunately, we often allow these discounts to wash down to the selling branches, which in turn, find their way to the sales pricing. All that investment in buying bigger and redistribution gets washed out in the sales process. Stop doing this. If you are going to get goodies for buying in bulk, let the company keep it. Transfer the products

at a reasonable base cost and let them sell at an appropriate margin. Rebates and bulk buy discounts should never be used to reduce the selling cost of branch inventory.

In an effort to bring this opinion piece to a close, I will leave you with this. Branch inventory management is one most difficult aspects of distribution. We often get it wrong and wind up driving up expenses. As the entity gets larger, we have to let go of our small company scheme. Our methods of redistribution must evolve. This means that we need to get educated on how larger entities function and what tools they use to be successful. Learning how to work with your ERP, rather than trying to beat it into submission, is an exceptionally good step toward making your branch management system effective. Good luck and know that I am here to help.

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