Research Reports
Articles

Power of availability

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Surprisingly companies, whose market shares are less than 15 percent, project a sales growth very close to the market growth. Why not more than double the rate of market growth? The reasons provided usually include 'There is no more demand for our product' and that trying to create this demand requires a huge investment (as stated in the above para) which will make the initiative unprofitable.

'There is no more demand for our product' – then how come the market share is 15 percent? It should have been over 80 percent. Somebody else is selling the rest 85 percent hence demand is not the issue.

Can a company increase sales substantially without additional investment? One of the most attractive options is to address lost sales due to unavailability at the retail shops. Obviously one needs to check if the lost sales are substantial and if they can be addressed without additional investment.

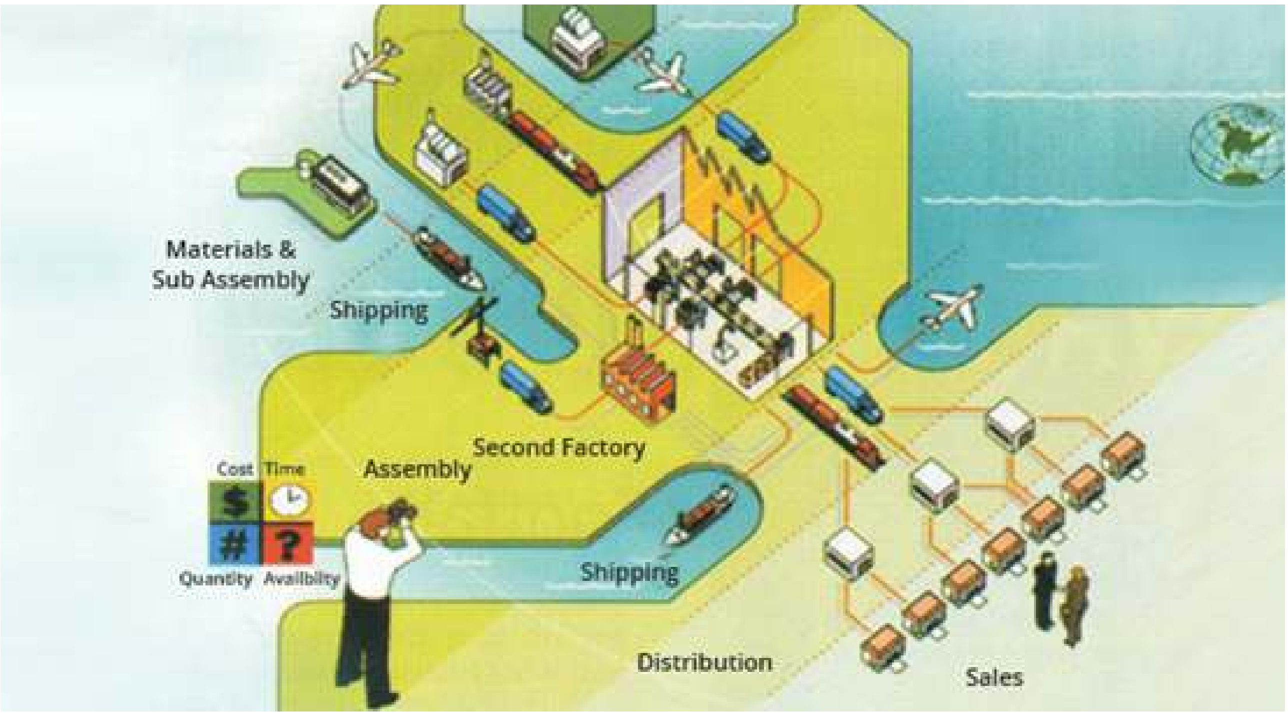
Consider case of a company with more than 50 SKUs, and market shares less than 20 percent and good acceptable competitive quality product. Most well known FMCG and fashion product companies would fall in this category.

The extent of lost sales in any area can be estimated to very close to the stockouts in the supplying warehouse such as a distributor. The check is very simple – take the snapshot of stocks at times spread cross 2-3 months and compare the same with the products that the company has in its range and those sold by all other competitors in the area (and not with what Sales indicates as the saleable range). The snapshot will indicate random stockouts and range thinner that held by the company. You can draw your conclusions of the potential lost sales.

But the lost sales is much higher that this first indication! The chances of retailer not pushing other brand in case the company's product is not available are very low. The potential loss for him is not only the sales loss for this product but the whole shopping list of the customer if the customer decides to switch shop. Obviously he cannot afford such a loss and hence will push hard other brands. Such lost sales are not reported by the retailer as he did not lose sales. The damage is catastrophic if the unavailable SKU is priced higher than its competitors. If the customer believes the influencer (retailer) and has a good experience. he has discovered a lower priced product with the same quality / taste/ experience. Word of mouth will further increase this damage.

What about the shops which do not carry the company's products at all? Not all companies have distributors to cover the whole universe of potential shops.

If the forecasted quantity is sold earlier, in say 15 days, instead of the month. Sales declares either 'sold out or forecast met. The flip side is that sales lost are nearly 100 per cent for the period, as the rate of sales has increased.



The common approach adopted by companies to avoid this lost sales is In 'dump' distributors and retailers with very high stocks. It also serves the purpose of 'locking the capital' of these entities to prevent him from buying other brands.

This approach further increases unavailability and lost sales!!!

Forecasts can never be accurate.

With the dumping and forecasts rarely being accurate the distributors/ retailers' capital gets locked in the higher than required stocks of few SKUs. Resultantly, he does not have cash to buy the stocked out SKUs (indicated by the usual pleas for allowing credit limits overruns or stoppages of supply due to high over due). The stocked out SKUs are items which sell, and SKUs that sell are fast movers!!! We have already discussed the huge damage of random stockouts at the retail stores.

These forecasts are converted to monthly production plans. Plants produce in large batches to achieve the highest productivity. With the pressure to dispose the finished goods produced as fast as possible, the material is allocated to sales people who predicted their requirement. The way out for sales people- Dump irrespective of the sales trend.

It is well known that 'What is displayed is sold'. With capital locked in SKUs not rotating faster, the retailer has no choice but to display these prominently in precious shelf space that should have been giving prominence to fast movers. Further lost sales!

The locking of capital of distributors in the large 'dumps' forces them to limit their retailer reach as increasing retailer reach requires capital.

In conclusion, for such companies, the sales loss is very high due to unavailability. Importantly most such companies have spare production capacity or can be released using right improvement initiatives (such as Theory of Constraints) to an extent of 30 per cent to 50 per cent. If the companies under discussion can prevent the lost sales by better availability with production from existing infrastructure (minimal additional fixed expenses) they can surely double profits in one year!

Ensuring 100 per cent availability: From the analysis above the direction solution is –
Do not push / dump SKUs to the distributor/ retailer. Ie hold back stocks and replenish frequently only what is sold.

Plant's producing not for internal efficiency achievement but only for what is dispatched forward on a daily basis by the immediate warehouses.

With a judicious location of warehouses to ensure that about 90 per cent distributors are more not than 3 days away from any such warehouse, and if the company is replenishing frequently only what is sold, distributors can have 100 per cent availability at about 10 days of 'correct' inventory.

For a distributor whose current stock levels are at 30-45 days stock this means tripling his inventory turns. As availability increases sales, the return on capital employed on this lower capital employed will increase to near 100 per cent!!! How many distributors in India will not ensure adherence to company requirements for secondary sales if they experience such ROI's for the long term?

The 'Theory of Constraints' replenishment and operations solution have been proven to provide near 100 per cent availability without excess inventory at all the stocking points of the supply chain- from raw material to retail shops.

Having a central warehouse or plant warehouse is a critical as it allows for 100 per cent availability for any fluctuating requirement from regional warehouses or distributors. This is possible as not all distributor sales will peak at the same time. Especially for fashion product companies, holding back inventory is very critical as sales are very unpredictable. With the current way of working, fashion product companies usually have early stockouts in some areas while huge surpluses in another.

Additionally, by the principle of aggregation, the inventory required at the central warehouse (or supplying warehouse) is nearly half of the total required at the consuming warehouses. The plants have to produce to ensure availability in the central / plant warehouses (and not to ensure utilization of machines/ resources). With this the warehouse will have 100 per cent availability the most critical element for high availability further down the chain.

To start replenishing to what is sold, the inventory levels for the SKUs of the saleable range have to be decided. If a mechanism is available to change these levels dynamically purely based on the early warning of a stockout or surplus, then an elaborate exercise to determine the starting levels is not required. Fair approximates are good enough to start with as these will get corrected soon.

Further if the selling entities provide daily sales to the previous entity, then the total replenishment times are reduced to just the transportation hatching and actual transport time. Hence the distributors who are 3 days from a depot or regional warehouse can have 100 per cent availability at about 10 days inventory.

With such a system a short term forecast (which is anyways inaccurate) is not needed. The long term forecast is required for only for planning very long lead raw materials.

A similar more simplified mechanism is applied to the distributor. Retailer link. Higher frequency of visit (from current visiting frequency) and the discipline. of replenishment (not dumping) ensures near 100 per cent availability of wider range at retailer. The current incentives to the retailer for prime shelf space can be restructured to ensure shelf space and range.

Most distributors/ retailers interested in a long term relationship are more comfortable with a steady higher rate of return on investment rather than speculating on prices or on anticipated returns on high volume schemes. Most have, in the past, experienced the brunt of the losses when these don't go as predicted.

Transportation costs, against common prediction, will not increase as the trucks are now going always full. With reporting of daily sales, the supplying warehouse/ distributor send vehicles with an assortment of SKUs to fill the capacity of the vehicle. More full trucks means more sales and not higher transportation costs!

'Buffer Management' provides the priority for supply based on the threat to stockouts. This system is based on simple colouring of the stock levels as Red as bottom 33 per cent of the decided stock level. 33-66 per cent as yellow for the next level and 66 per cent to 100 per cent for the topmost band. Such colouring systems are easily understood by warehouse dispatch schedulers.

In summary- it is not difficult to achieve near 100 per cent availability at distributors and retailers without investment and address the lost sales and double! triple profits! Offcourse there is a sequence and methodology of implementing this change. Is it difficult? More about that soon.