



Case Study: More Effective Inventory Management through Total Cost Modeling

While the client was doing an excellent job of tracking acquisition and warehouse-related costs, they had no effective way of tracking other product costs before and after that limited segment of the inventory management cycle. From merchandising and administration to managing the product on the store shelves, a more holistic—and realistic—approach to understanding costs was necessary. Without understanding these costs, they were relying on ineffective procurement practices, such as buying larger volumes to achieve per-unit savings.

Guidon's modeling experts used careful profit and loss (P&L) analysis and process mapping to create a total cost model which explores every touch point in the product's life cycle. Through collaboration and communication, the Guidon team was able to overcome the silo-related challenges the client faced and gather end-to-end process information about each SKU, including costs related to merchandising, marketing, replenishment, delivery and distribution centers, and retail stores.

They identified three key areas of the life cycle to model:

- Corporate: Planning, procurement, merchandising, marketing, administration, etc.
- Distribution Center (DC): Warehousing, transportation, distribution, etc.
- Store functions: Monitoring and maintaining stock, in-store merchandising, managing returns, etc.

By abandoning the company's previously compartmentalized approach—where only a few individual silos had a clear understanding of their own SKU-related costs—the model gave company managers a clear look at costs and opportunities. Redundant tasks and other inefficiencies became evident in the end-to-end process review, since the model facilitated transparency between business units. For example, when 100 SKUs were created for a product line that only needed 25, the superfluous 75 wasted downstream resources. Reducing those 100 SKUs to 25 reduced the downstream management work created by each SKU. In addition, costs for such “invisible” expenses as staff time related to a product's visual merchandising had to be considered as part of the true cost of the product.

Once the model was completed, the client could immediately see that the actual costs related to managing inventory include much more than per-unit and warehouse management costs. Users could easily see whether the total life-cycle costs of buying in greater quantities would offset or outweigh any savings.

In addition to this enhanced decision-making ability, the client is now able to test a variety of “what-if” scenarios related to those products being considered as inventory additions. This helps them determine the true cost of procurement, management, and distribution before making a commitment to purchase the product. It also shows where costs expand and shrink throughout the product's life cycle within the retailer's inventory management process. The overall effect is better communication between business units involved in the product life cycle, further breaking down silos.

Client: A large consumer products retailer

Industry: Retail

Service: Total Cost Modeling

Challenge:

- No effective or reliable method for capturing costs associated with any given SKU
- Had little understanding of the true cost of SKU-related functions over the entire life cycle of each product within the retailer's chain
- The invisible costs were significant and lack of true cost understanding was leading to poor decision-making

Solutions: Guidon Performance Solutions helped the client:

- Built a model to map each product line and the related SKUs
- Able to track costs from the moment the product is considered for inclusion until the moment it exits from the company offering
- Greater understanding of the true costs of inventory procurement and management

Results:

- With a comprehensive understanding of each SKU's cost from cradle to grave, the client can make more effective inventory management decisions
- Allows the client to test ideas and potential products without having to physically put those products in the inventory pipeline
- Allows the client to make accurate decisions about the true costs of adding new products



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