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Turns, Turns, Turns

Custom Retailer
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With all due respect to Pete Seeger and The Byrds, every season is an important time to look at turns. Inventory turnover that is...

Are you looking at turnover all the time? Inventory turns are a subject that everyone talks about, and very few actually manage in a disciplined organized process. At the end of the day, improving inventory turns is the best way to improve cash flow and free up dollars for spending on other revenue producing parts of your business. For example, let's say that you are 9-12 weeks out in scheduling installations. You should be asking yourself, "If you only had the cash to lease or buy another truck, tools and labor to shorten that back load of work". If you improve your turn over, you can free up cash to allow for these additional expenses and create more sales. These new sales, with no other increases in expenses, will therefore increase revenue and profits.

What is inventory turnover? Turns are measured by taking the value of the products sold at cost and dividing that number by your average inventory. For example, let's use the following Custom Retailer's numbers as an example.

The business has a sales revenue of \$1,200,000 per year. The labor portion of these sales is 25%, which agrees with the average from CEDIA surveys of Custom Installers. If we deduct this 25% number (\$300,000) from the revenue side, this business sold \$900,000 of product during the year. If the gross profit margin on products sold was 33.33%, the value, at cost of the product sold was \$600,000. If your average inventory during the previous 12 months was \$150,000, you turned your inventory 4 times. If your average inventory is \$200,000 your turnover was 3 times. Most custom retailers that I speak with have a turnover of 3 to 3.5 times per year. The following Chart shows the months supply of inventory you have, on average, for your business.

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Sales at Cost	Average Inventory	Turnover	Months Supply
\$600,000	\$600,000	1 Time	12.00
\$600,000	\$300,000	2 Times	6.00
\$600,000	\$200,000	3 Times	4.00
\$600,000	\$150,000	4 Times	3.00
\$600,000	\$120,000	5 Times	2.40
\$600,000	\$100,000	6 Times	2.00
\$600,000	\$85,714	7 Times	1.71
\$600,000	\$75,000	8 Times	1.50
\$600,000	\$66,666	9 Times	1.33
\$600,000	\$60,000	10 Times	1.20
\$600,000	\$54,545	11 Times	1.09
\$600,000	\$50,000	12 Times	1.00

As the chart shows, 3 turns a year means that, on average you have a 4-month supply of product in your warehouse. If you have only 3 turns a year (a 4 month supply), if you go to 4 turns a year, (a 3 month supply), you will free up on average \$50,000 of assets that can be used in another part of your business.

I have looked at the inventories of numerous custom retailers over the several years and the following are well proven steps to improve inventory turns, cash flow and allow for better investment opportunities in the future.

- 1) Run a report of all your items that you have on hand. Typically 10-20% of these items are products that are either discontinued, open box, or defective. If they are more than 20%, you need to start working on this immediately. By identifying these items, selling them off, getting products repaired or replaced will improve your turn over and free up cash quickly. If you have \$150,000 in inventory, these efforts will give you \$15,000 to \$30,000 quickly. Please remember that these products are not antiques and that they do not become more valuable over time. Sell off these old, discontinued products NOW.
- 2) Completely review your product mix. If you are like most dealers, duplication in some product areas is probably significant. For example, in-wall speakers or \$2000 receivers. Narrow you mix of products. If you have four in-wall vendors, narrow it to three. You become more important to vendors and your ability to negotiate better terms and discounts increases considerably.

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- 3) Use the cookie cutter principal in installations. Sell the same system over and over again. This repeatability will increase the reliability of your installs and lower inventory by narrowing your mix of products.
- 4) Have a plan for increasing your turnover and freeing up cash. Keep track of your inventory product levels and total inventory. The success of this plan can be measured and the results can be important factors in growing your future business.