INVENTORY CONTROL PHASE-IN

A GOOD METHOD IMPROVES YOUR PARTS OPERATION

BY SHAWN LARKIN

There's an undeniable fact in the Parts industry that everyone holds onto Parts they don't need or want.

The reality is that every dealership has Parts that are idle and lack demand and shouldn't be in inventory. These tens of thousands of dollars in Parts — your dealership's capital — just sit and collect dust.

You wouldn't be wrong to point an accusing finger at the manufacturer and it's true you don't have the return allowance to clear out those unwanted items.

The reality is, your return allowance isn't substantial enough to handle even the portion that's just auto phase-out Parts, but you still must work within the rules of the return allowance policy. The execution of a strong special order policy is great, but only one piece of the solution to control idle and obsolescence.

Let's take aim at a different piece of the puzzle, one that can properly control your use capital and ensure that your Parts purchases are only applied to performing inventory that has demand. Let's look at your Inventory Control Phase-In Criteria.

Inventory Control Phase-In: What It's About

Inventory Control Phase-In is a critical tool in how you control and handle Parts that come into your inventory in the first place.

Typically, in the Parts industry, Parts Managers control and purchase items based solely on months-no-sale, meaning the number of months since the last sale date. Although months-no-sale is the standard for most Parts Departments, it sets you up for an underperforming inventory in terms of costs and it inflates your inventory.

To understand your inventory needs and to properly handle your inventory, a methodology is required. For inventory control, the methodology is based on a single factor — demand.

Demand, at its root, is a Part's sales and lost sales within a month and reviewed over a longer period, like 12 months. Demand is tracked on a per-part number basis by your dealer management system (DMS) and counted by individual calendar months. This demand-based methodology is used to set up your DMS to automatically recommend items for a stock order.

Why Methodology Matters

The issue of methodology boils down to dollars and cents. Parts that lack demand have a high likelihood of never selling.

These Parts in stock take up space, time and return allowance — none of which you can spare. And, most importantly, they freeze capital. That's certainly not something a dealer principal likes to see.

Fast-moving Parts use the same methodology, as well. Demand must be used just the same, otherwise you don't "phase-in" Parts and you aren't able to fill orders immediately. This compounds problems and creates spin-offs, including:

- Potential lost sales due to lack of inventory.
- An item special ordered for a customer creates urgency to fill the order on the customer's schedule once the part arrives. It creates a rush for many levels of Parts and Service staff to fix the vehicle and get the customer back on the road. If Parts are filled by stock orders, the scheduling is on your terms.
- Added pressure on Parts drivers and / or shuttle drivers due to an extra customer visit.
- The Service Advisor cuts their efficiency in half. They must call the customer for a repeat visit, write another work order and follow progress for a second time.
- The Technician needs to tie up a Service bay or pull the vehicle outside and then repeat the process once the part arrives.
- Purchase to fulfill order is urgent, typically resulting in lost discounts earned if purchased on a stock order.
- A repeat customer visit for the special order part install, means another customer can't fill that shop time instead.

Calculate the lost time and effort put into filling a single special order. The costs in realized expense and potential sales unrealized are huge.

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The Method: A Picture Painted by Numbers

The information gets thick, but stick with it. The information is invaluable for making your phase-in methodology benefit your Parts Department, saving time, unlocking capital and increasing sales.

There are different criteria that are common in inventory control. One such example is three separate periods (months) of demand in the last 12 months. This is known as “3-in-12.” There are many others criteria, including “3-in-9” and “3-in-8.” They are known as the “phase-in criteria.”

Simply put, this tracks how many separate periods (months) of demand (sales and lost sales) in a given month, within 12 months rolling, there have been on a per-part number bases.

In the example of 3-in-12 phase in criteria, when a part reaches 3 (three separate months of demand), this particular part will now qualify for stock and will be seen on your stock order, provided that you set up your DMS system’s source controls to read this criterion.

A period (month) doesn’t look at the quantity sold during that month. Demand only needs to have a number greater than 0 to be counted as 1 for period of demand. The quantity sold within a period could be 1 or 75. Only when “days supply” is calculated on a part does the quantity for “a” demand period matter, but that’s a whole different topic.

Here’s a look at what 3-in-12, 3-in-9 and 3-in-8 looks like.

Phase In Criteria

	MONTH 1	MONTH 2	MONTH 3	MONTH 4	MONTH 5	MONTH 6	MONTH 7	MONTH 8	MONTH 9	MONTH 10	MONTH 11	MONTH 12
3 in 12	5	1	0	4	0	0	0	0	0	0	0	0
3 in 9	0	0	2	0	5	0	0	0	0	0	0	0
3 in 8	14	9	0	0	0	0	0	13	0	0	0	0

Which Phase-In Model Is Best?

The 3-in-12 phase-in is ideal because it takes into consideration the seasonality that most dealerships experience in their region.

Although many practice other phase-in criteria, it’s possible that you run the risk on many parts of becoming auto-phased-out — out of active stocking inventory — only for the part to requalify itself back into inventory during or just after the busy season.

Consider this with less than a 3-in-12 model: in the northern region, your air-conditioning Parts could phase out during the long cold winters, while in the south, your engine block heaters could phase out before cold weather returns.
To clarify, auto-phase-out simply means lack of demand over a specified period of consecutive months. What number you use is up to you.

Typically, you would set an auto-phase-out to 9, meaning that nine consecutive months without demand means a part will auto-phase out and turn the stocking status of a particular part to be returned to the manufacturer. Auto-phase-out simply means a part is no longer considered an active part in inventory and you should neither have it nor stock it.

These numbers — and the methodology you use — matters.

It’s commonplace in the industry to say that all Parts that have months-no-sale less than X are stock. Many say X for their Parts Department is either nine, 10 or 12. But not all Parts are created the same. Just because it may have sold in the last two, or even six months, doesn’t mean it should be in stock, or brought in again for stock.

Here are some numbers to think about.

Parts with demand of 1-in-12 = this is a random sale. This part has a 37 percent chance of selling.

Parts with demand of 2-in-12 = this is a condescendence. This part has a 55 percent chance of selling.

Parts with demand of 3-in-12 = this is a trend. This part has a better-than 93 percent chance of selling.

Parts with less than three demand periods will be below a 45 to 63 percent range range of ever selling in the near future. These are bad odds and very poor use of capital and inventory control.
As a part ages and sits on the shelf, the probability you will sell it drops drastically each month that goes by.

Here are some figures on the likelihood of selling a part after X amount of months-no-sale:

9 Months-No-Sale: 15 percent chance of ever selling again at your dealership.

12+ Months-No-Sale: 5 percent chance of ever selling again at your dealership.

If a part in your inventory has been idle for nine months or longer, think long and hard about phasing it out.

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The Takeaway

Thinking about Parts inventory control only based on the last sale date is a bad idea. This ties up capital and makes a mess of trying to run a Parts inventory.

The Parts Manager's job appears straightforward: Parts and Operations. But the Parts Manager's job, like any other manager's root function, is to make capital perform. If capital doesn't perform and multiply, there's a major problem.

This inventory control methodology can be implemented easily in your DMS system. You can learn to do it yourself with your DMS consultant, or the consultant can do it for you.

Having a methodology will reduce your stress and simplify your inventory in the end, and your stock order pumps out on the right part numbers every time.

Most importantly, your fill rate increases, your inventory gets in line and the performance of your capital usage dramatically improves.

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