OLIVER WIGHT PAPER series

Who Owns Inventory?

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People frequently ask: Who owns inventory?

They see inventory created as the result of actions or lack of execution by different functions of the company. They wonder whether accountability for inventory has been established.

In asking who owns inventory, people frequently neglect to consider inventory as a strategic asset. When inventory is considered a strategic asset, inventory tactics are developed that address:

- Seasonality of demand
- The advantages of building product prior to a new product launch
- The need for safety stock as a hedge against demand and supply uncertainties.

Inventory tactics are often not considered when companies lack formal, integrated processes that align demand, supply, and financial plans. Effective processes for setting inventory tactics include Integrated Business Planning (IBP) and Integrated Tactical Planning (ITP).

When inventory tactics are not formally considered, decision-making roles are not clear and inventory is not well governed. Accountabilities are also hidden or not accepted.

What Is... ?

Definition of Integrated Business Planning

Integrated Business Planning is a decision-making process to align strategy, portfolio, demand, supply, and resulting financials through a focused and exception-driven monthly re-planning process. **The result is a single operating plan,** over a 24+-month rolling horizon, **to which the senior executives hold themselves and their teams accountable for achieving.** Done well, it is the formal way that the business is managed and strategy is connected to execution.

Definition of Integrated Tactical Planning

Integrated Tactical Planning is a **cross-functional,** detailed planning process that **routinely re-aligns** and re-optimizes **core process plans** (product, demand, and supply). The ITP process facilitates effective communication should re-alignment not be possible. Review and realignment are performed **weekly, typically over a 13-week horizon.** The primary objective of the process is **to ensure execution of plans approved through the Integrated Business Planning process plans.**

Definition of Demand Planning

Demand Planning **involves planning all demand for products and services** to support the marketplace. It involves all functional areas that plan and execute demand-creating activities, **including the sale of unwanted inventory and stock that is nearing expiration dates.** The volume and financial projections from the demand plan are **communicated to those who need to know in order to perform their responsibilities.**

So who owns the inventory?

Here's a way to think about ownership of inventory when seeking to establish accountabilities:

If the inventory was unplanned, the function that caused the unplanned inventory technically "*owns*" it.

For example, if inventory is the result of a demand plan error (selling less than the demand plan), the demand side of the business "owns" the inventory. If the inventory is the result of producing more than was approved in the supply plan as part of the IBP process, then the supply side of the business "owns" it.

Either way, the demand side of the business is responsible for selling unwanted inventory.

The plan to sell the inventory should be part of the demand plan with assumptions and tactics documented and communicated. The plan should be updated every month as part of the demand planning process. The demand plan for the unwanted inventory should be part of the monthly Demand Review as part of the IBP process until the stock is depleted.

Case example: A supply organization purchased more than was authorized in the supply plan, fearing disruptions caused by the upcoming Chinese New Year. The lead times for products supplied from China are 12-16 weeks.

Wanting to avoid a potential stock outage, the supply planning team ordered $1+ million in safety stock that was not authorized or approved. The transaction was not reviewed in advance in the IBP process.

A further complication: The supply planning team was not aware that some of the safety stock was for products at the end of their lifecycle in the coming months.

In cases like the above example, the demand organization is still tasked with selling the "extra" inventory – even though the inventory is the result of a supply planning decision.

Here is a commonly used process for depleting unwanted inventory:

The supply team informs the sales and marketing team that excess inventory exists. In developing the demand plan for this inventory, the sales and marketing organizations may propose pricing and promotion tactics for stimulating the sale of the inventory.

These tactics are reviewed and approved through the Demand Review as part of the IBP process. The status and any updated demand plans and tactics are addressed every month in the Demand Review.

The demand plan for unwanted inventory may also be addressed as part of the Integration Reconciliation Review of IBP. When the magnitude of the inventory is a financial concern, it is also common for updates to be included in the Management Business Review until the inventory is depleted.

The same process is used for depleting inventory that resulted from selling less product than planned.

Ownership is different when inventory is the result of an agreed-upon tactic

Companies may decide on a make-to-stock strategy. In this case, agreement on the strategy must be reached between the sales, marketing, supply, and financial organizations. The discussions center on how much target inventory to maintain in order to meet customers' service expectations.

Safety stock is also an agreed upon tactic. It is used to "cushion" against demand plan inaccuracies and supply execution problems. The sales, marketing, supply, and financial organizations work together to decide the amount of safety stock to carry for individual products.

The demand, supply, product management, and financial organizations may also propose inventory tactics.[1] The proposed tactic should be reviewed in the Integrated Reconciliation step of the IBP process. The purpose of the review is to formally understand the costs, risks, and benefits of the tactic. It also is the venue to reach agreement on the volume and financial investment to support the tactic. The tactic is approved by the senior leadership team in the IBP Management Business Review.

Who owns the inventory that is the result of an agreed upon tactic?

The senior leadership team of the company does. The inventory is the result of a leadership decision to ensure that:

- Customer expectations are met in the most cost-effective manner, and
- The company’s business and financial objectives are achieved

[1]Dawn Kynaston, Inventory as a Consequence: Improving Supply Planning, www.oliverwight-americas.com/whitepapers-articles/

Why not focus on who “owns” lead time, too?

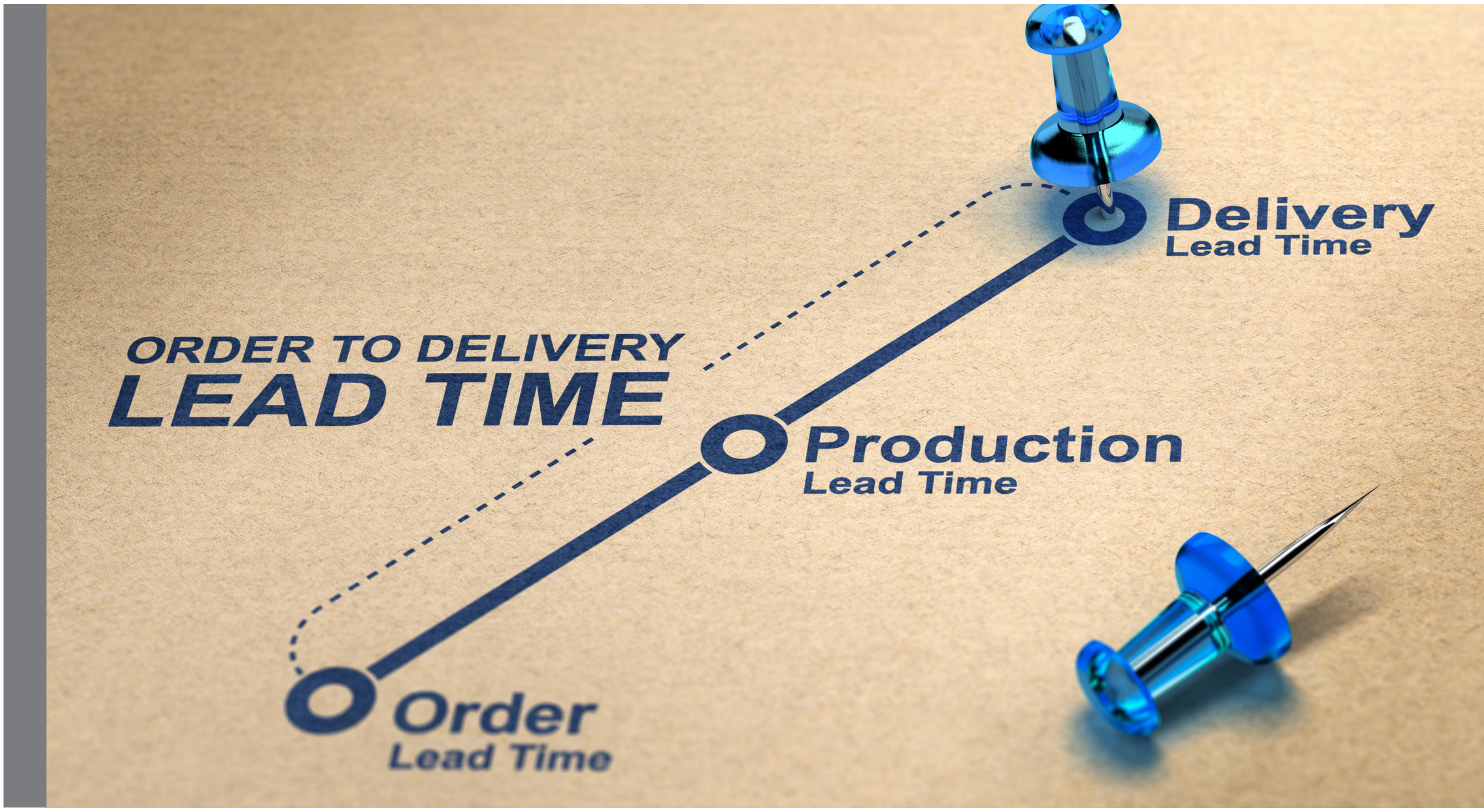
It is ironic that people focus on who “owns” inventory, but do not devote an equal amount of energy on the subject of lead time. The calculation for determining how much safety stock to carry includes:

- Lead time (both supplier lead time as well as order lead time – the time a customer spends waiting for an order to be fulfilled)
- Historical forecast, or demand plan, error

Like inventory, lead times are a tactic that should be agreed upon by the business leaders. Longer than agreed upon lead times are typically the result of poorly executed demand plans and supply plans.

For example, when actual demand exceeds the planned demand, longer order lead times in providing customers with product can result. This is particularly the case when a company has not agreed upon a safety stock tactic to cushion against demand plan inaccuracies. Longer supply lead times and order lead times can also result from execution problems in the supply chain. Execution problems include manufacturing problems, quality issues, and poor supplier on-time delivery.

Actual versus planned lead times should be measured every month. The purpose of the metric is to determine how to improve demand and supply execution.



Reaching consensus on inventory ownership

One purpose of the Integrated Business Planning process is for the senior leadership team to reach consensus on aligned product, demand, supply, and financial plans. The plans must also align with a company's strategies and business goals.

Once consensus is reached and the plans are approved in the IBP Management Business Review, it means there is commitment to execute those plans (see definition of IBP). Commitment to execute the approved plans is one of the most important behaviors a company can exhibit and is considered a best practice. This leadership behavior alone stimulates significant improvement in customer service and financial performance.

Most companies measure and report the financial investment in the inventory. The purpose of the measurement often has a financial orientation. The measurement also should be used to understand and correct execution issues or unapproved tactical decisions.

To make the financial measure more actionable, execution performance should be measured in the form of demand plan accuracy and supply plan accuracy (planned versus actual).

Lead times (as well as expedites) should also be measured and reported as they are influenced by inventory tactics and execution problems. Few companies measure the amount of lead time (and whether lead time is decreasing or increasing).

It is also uncommon to link the lead time measurement to other performance issues. These issues include the impact of lead time on inventory, customer service, lost sales opportunities, and lost sales revenue. Nor do many companies focus on lead times as a symptom of execution issues.

When superficial inventory measurements are reported without identifying the root causes of problems, the "blame game" results. That is why managers and leaders challenge who "owns" the inventory.

Who owns inventory is the wrong question to ask

Dig deep enough, and it will become evident that inventory is a symptom of other business issues. In reality, ownership of inventory should reside with the entity that owns the "root cause" of inventory.

Working on those root causes will simultaneously improve customer satisfaction and financial performance. Root causes are commonly execution issues and poor decision making.

Companies with agreed upon tactics for safety stock and lead times typically exhibit these leadership behaviors:

- They have considered the cost/benefit tradeoffs of the tactics as part of the decision-making process.
- They also see the value of improving execution – both demand execution and supply execution.
- Minimizing the root causes of the inventory symptom is the focus of concern, rather than on inventory ownership.[2]

[2]Leon Dixon, Inventory Is Not a Problem; It is a Symptom, www.oliverwight-americas.com/whitepapers-articles/

So who owns inventory?

Business leaders that have developed a Class A Integrated Business Planning process know the answer: The senior leadership team.[3] There is rarely an argument about accountability in companies with a best practice IBP process. In developing and maturing the process, the roles, responsibilities, and decision-making accountabilities are clearly defined and agreed upon.

For companies that have not yet developed a Class A Integrated Business Planning process, the answer of who owns inventory is the same: The senior leadership team!

In all companies, senior leadership is ultimately accountable for the operational and financial performance of the company.

In companies that lack a best practice IBP process, the roles, responsibilities, and decision-making accountabilities often are not clearly defined. As a result, people at all levels of the company become mired in the non-value add "blame game." Their energy would be much better spent addressing the execution issues and decision making that create inventory.

[3]The Oliver Wight Class A Standard for Business Excellence, Seventh Edition, John Wiley & Sons, Inc., pp. 47-61.

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