Excess Inventory in Manufacturing

In today's manufacturing world businesses spend a great deal of time and effort in managing inventory. Inventory is controlled through how it is received, stored and used and this is important because this has a direct impact on profits. One aspect of inventory management that is sometimes overlooked or does not get the attention it needs is excess inventory. If excess inventory is not monitored and managed properly this can lead to losses in revenue not only from the cost of the inventory but the storage and labor in maintaining these items.

What is Excess Inventory?

- Excess Inventory is inventory that exceeds the customers' orders or forecasted demand. Excess inventory ties up cash flow for the business by holding this cash in inventory form and preventing it from being converted into a sellable product. Excess Inventory represents a loss in revenue.

How is Excess inventory created?

- Inaccurate forecasting – forecasting uses data to drive decision making to ensure you have enough product on hand to meet the customer's needs without ordering too much. Forecasting uses data from trends, demand history, qualitative and quantitative forecasting methods to determine what and when to order. If forecasting is off or done incorrectly excess inventory will be created.
- Minimum buys – When purchasing places orders for components based on customer order demands these orders are subject to minimum purchase quantities from distributers and vendors. For example the order is for 100 pieces and the buyer goes to purchase a component that is one per assembly but the minimum order for this part is 200. In this scenario we are required to purchase 100 pieces to fulfill the order but we have also created 100 pieces of excess inventory based on the minimum order requirements.

- Obsolescence – When a customer makes changes to a product (design or functionality) and a component that has already been purchased or received is removed from the product these components become excess inventory. Obsolete components can also be time sensitive and may become un-usable with time so a quick disposition is important with this type of excess inventory.

Disadvantages of Excess Inventory

- Storage costs – holding excess inventory cost the company money. Cost associated with the space, utilities and labor that go into maintaining these parts.
- Storage capacity – Excess inventory takes up space that could be used for items that are able to be sold for profit.

- Loss of revenue – This inventory will decrease in value or cannot be converted into cash.
- Obsolete/Deteriorating Inventory – Inventory that sits too long or becomes un-usable in product will not be able to be sold or used to create revenue. Some inventory has a shelf life and this could expire making these components have no value which means they will be scrapped for a loss.

Managing Excess Inventory

- Accountability – putting someone in charge and accountable for the management and disposition of this type of inventory. In contract manufacturing we use account management to deal with this inventory and to work with their customers to minimize and manage this aspect of manufacturing.
- Rules – it is important to set rules on what excess inventory is and how it is dealt with. Making these rules clear on how excess inventory is handled and that the inventory is not left unattended or forgotten about.
- Upfront communication – In Electronics Contract Manufacturing one of the key components in managing excess inventory is communication with the customer. Letting the customer know what excess inventory is and their responsibility in paying for this inventory. During the quoting stage is the best time to be upfront with the customer and relay detailed information on excess inventory. Some customers like to see it as a separate line item on the quote or some would rather have it rolled into the per piece pricing. How the information is presented to the customer is not as important as making sure they know about it before the material is purchased.

- Visibility – knowing what inventory is excess is important in managing and dealing with this issue. Using the Enterprise Resource Planning (ERP) system to help keep on top of this inventory is an important part of making sure it is taken care in a timely manner.
- Timing – making sure this inventory is payed for is important as well as how quickly this is taken care of. When inventory sits and has no movement it runs the risk of losing value or becoming obsolete.

Conclusions

In Electronic Contract Manufacturing excess inventory is not only a waste of money but also has a major impact on labor, floor space and profits for the company. Businesses that control their excess inventory will have a step up on the other companies that do not put the time and effort into this aspect of inventory management.