

Business Services - Common Problems:

Too much obsolete inventory

The volume and value of obsolete inventory is too high leading to increased costs and decreased cash flow.

Indicators

- Increasing storage costs.
- Increasing inventory returns.
- Cash flow is becoming tighter.
- The business is in an industry where there is a constant change in consumer preference or there is rapid technological change (eg the computer industry).
- The inventory turnover ratio is worsening (i.e. inventory is held in the warehouse for longer before it is sold).

Causes of the problem

- There is no record of what percentage of inventory is obsolete or any guidelines as to at what age inventory becomes obsolete.
- There is no policy to dispose of obsolete inventory.
- The speed at which consumer preferences change has been underestimated.
- The business's return of inventory policy is too liberal. Too much inventory is held in store, rather than ordering on an 'as needs' basis (the principle of Just In Time inventory management).

Short term solutions

- Inspect all inventory on hand and identify the obsolete items.
- Examine whether obsolete inventory can be rejuvenated or recycled.
- Ensure that the business's return policy is not being abused (eg all returns should be authorised by a senior employee).
- Analyse whether the inventory can be sold at a reduced rate or to other types of consumers.
- To save on storage costs, dispose of obsolete inventory (eg donate to charitable institutions).

Long term solutions

- Set limits on the amount of obsolete inventory which will be tolerated and derive a policy for the timely disposal of any excess.



- Examine budgets for future production and ensure that the expected life of the product is in line with the production period.
- Determine whether the return policy should be modified.
- Adhere to the principles of Just In Time inventory management. Do not ever hold, at any one time, inventory above a predetermined level.

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