Cost reduction by improving strategic inventory management decisions

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As today’s markets become more dynamic and competitive, companies are pressured to remain responsive and efficient and well-performing supply chains have become a necessity for success (Jaber, 2009). Companies are constantly striving to cut costs but with today’s already efficient production and logistics, new areas to improve need to be identified in order to continue to reduce costs. An unexplored topic with large potential for improvement in companies is inventory management on a strategic level. Inventories need to be put in a new perspective, seeing them not as assigned a passive role but including them as an active part of the company strategy (Jaber, 2009).

Inventory management is still one of the key challenges in supply chain management. It is not uncommon that large amounts of working capital are tied up in goods throughout the supply chain and proper management of inventory is therefore vital for the success of a company. (Thonemann, 2011). To continue growing and to offer lower prices and reach more customers, IKEA – the global home furnishing company – has in line with the Growing IKEA - 2020 Together direction, where the aim is to double the revenue (2011) before 2020, realized that inventory management will play a central part in the future of their work and that there are possibilities to develop smarter ways to approach the topic compared to how the enterprise works today.

As a measure of approaching the problem with evolving this work, a new inventory concept has been constructed by the company. It consists of new ways of classifying stock, guidelines for how these new structures should be approached in the practical work and a clearer division of responsibilities for employees. However, IKEA lacks the strategy of how to approach the task of closing the gap between the current way of working with the future wished position.

In the thesis A Strategic framework for improving inventory management decisions at IKEA (Ellesson and Hultin, 2016), a strategic framework in line with IKEA’s new inventory concept was established aimed to improve their organizational structure and strategic decisions related to inventory management in order to reduce inventory costs. The process was developed based on identified and highlighted problems in steering and planning inventories for one product area within IKEA.

The study found that the work with inventory planning at IKEA was characterized as reactive and ad-hoc instead of being proactive with clear guidelines and decision support. Further, it was found that a fear for shortages was a clear representation of the attitude in the company. In order to change this way of working, with the aim of reducing inventory levels, a planning process including clear follow-up was needed. Cost support for storing at different parts of the supply chain needed to be developed so that IKEA could make more informed decisions and reduce
their inventory costs. Furthermore, directions were needed for how to select articles to prioritize, so that the time spent on inventory management is utilized in the most efficient way.

To better approach inventory planning and avoid keeping large amounts of excess stock, a process for more long-term inventory planning was developed. One of the goals with the planning process was to better coordinate different parts of the organization, using knowledge and goals from both the sourcing and supply chain directions in the company and clearly defining responsibilities and interactions, something that previously had been lacking. The planning process includes clear guidelines and various decision support and was established in line with the new IKEA inventory management concept.

Figure 1: The planning process developed in the thesis *A Strategic framework for improving inventory management decisions at IKEA* (Ellesson and Hultin, 2016).

The planning process is carried out over six weeks with a planning horizon of eight months and is illustrated in Figure x. The result of the planning process is an inventory plan that consists of:

- a set of selected articles - ensures better prioritization of work
- location of inventory - both in terms of where in the supply chain (i.e. at supplier, IKEA warehouses or at stores) as well as geographically (i.e. what countries or regions)
- a start- and end-date of the stock - ensures a proper build up and build down of stock
- target goals and a follow-up plan

One of the major benefits of the planning process developed in the thesis is the prioritization between articles. Commonly, articles in a product range is treated in the same way which consequently leads to companies stocking up on articles not selling as good as others. By instead differentiating between articles, focus is put on the important articles, resulting in both more time efficient work and less overall stock. Another benefit of the planning process is that common target goals related to inventory are set for the organization as a whole. By ensuring that input from various concerned sources is used, more accurate and justifiable decisions can be made.
The planning process can be seen as a useful tool for working in a more active and proactive way and avoiding the passive approach of today. By setting an inventory plan with a long-term planning horizon and ensuring it is followed up, inventory can be kept at more appropriate levels. This more strategic way of planning inventory will result in savings, as has been outlined in the thesis.

**Conclusion**

The planning process discussed has been implemented for the product area investigated in the thesis and IKEA aims to spread it to other product areas. However, proper inventory management is not a unique challenge to IKEA and the planning process and aspects brought up in the thesis may therefore be useful for similar companies to consider. Thinking long-term and having distinct plans for inventory and thus having a more strategic view on the use of stock could ensure that companies avoid the large potential costs that are related to inventory.

**References**

