The Inventory Management KPIs You Should Be Tracking

Like air flowing into the lungs to oxygenate blood, inventory moves through the arteries of your supply chain to keep your business alive and thriving. And just like your lungs, your business won't be at its best if you don't have confidence in what you're "inhaling" and "exhaling." Tracking, measuring, and evaluating your workflows using *inventory management key performance indicators*, usually abbreviated to *inventory management KPIs*, can give you the information and insights you need to streamline your processes, tighten up your supply chain, improve customer satisfaction, and connect inventory management to the rest of your business process management in support of company-wide goals and improvements.

Every business has its own circumstances and faces unique challenges. So whether you're an old hand at inventory management, revamping an existing system, or starting from scratch, ensuring you're monitoring and optimizing the most common, and crucial, inventory KPIs is a step in the right direction.

Why Inventory Management KPIs Matter

As in other areas of business process management, effective inventory management can have a deep and enduring positive effect on several important aspects of your business, including its financial health, reputation, and overall operating efficiency.
KPIs minimize confusion and uncertainty from your processes by establishing clear benchmarks for performance within a specific timeframe. They might be static—e.g., "Fewer than five delayed deliveries to distributors each quarter"—or milestones that support larger initiatives, e.g. "Reduce inventory write-offs by 5% each month over the next year."

The metrics within inventory KPIs are designed to use data collection and analysis to provide insights that drive continuous improvement across the board.

> *Your company's strategic, customer satisfaction, and production goals should be a powerful presence in your KPI management. Every metric measured should have a clear and demonstrable value in supporting these goals.*

10 Essential Inventory Management KPIs

While no two companies will have identical business processes, all businesses will have a need at some point to monitor and improve some or all of the KPIs that affect inventory management.

When choosing KPIs, ten of the most important are:

1. **Accuracy of Available Inventory.** Knowing what's on hand in your

warehouse without having to bring production to a halt for a physical inventory count is essential to keeping products moving and cash flowing into the company coffers. High inventory accuracy makes it easier to manage inventory turnover and yields more useful insights for forecasting demand, more accurate financial reporting, and more strategically useful financial planning.

2. **Accuracy of Forecasted Demand.** Knowing what you'll need can be as important, if not more important than, knowing what's in stock. Tightening up this metric will allow you to run a leaner warehouse. Since you'll have a clear idea of what you'll need, you won't over- or under-order. This reduces inventory carrying costs and back orders while still allowing you to take advantage of growth opportunities when demand is high.
3. **Inventory Turnover.** It might sound like a suspiciously industrial baked good, but inventory turnover rate is in fact a measure of how many times a company's inventory has been sold and replaced ("turned over") within a certain time frame. It's calculated by dividing the cost of goods sold (COGS) by the average inventory in a given time period.
   This metric is an important yardstick for overall company efficiency; generally speaking, the higher inventory turnover is, the more efficient and profitable a company will be. That said, it's important to remember that some companies specialize in items that sell more slowly but have good longevity and profitability that exceeds the expense of keeping higher inventory levels until they sell, so inventory turnover isn't as critical for their overall productivity and efficiency.
4. **Customer Satisfaction.** This can be measured in a number of ways, and can be broken out across different metrics such as average order-to-delivery times, number of late orders, or customer ratings. Many companies measure customer satisfaction via net promoter scores (NPS) to get answers directly from the source.
5. **Order Accuracy.** Are the right items going out to the right people, within

the right time frame? Making sure the customer gets what they asked for, when they want it, is an essential KPI for any business that plans to stay *in* business. The global market is a big place, and if you can't meet customer demand, they'll find someone who can.

This metric, also known as *Perfect Order Performance*, is at the core of doing business effectively; that's why best-in-class businesses set goals of 99.5% to 99.9% order accuracy and completeness. That might seem excessive, but when you consider that (for example) a company processing 4 million orders every year with an order accuracy rate of 99% still has 40,000 order errors annually, that extra nine-tenths of a percent starts to loom large. If each error costs the company $25 to fix, an error rate of 1% is going to cost the company $1 million each year. Ouch.

6. **Order Timeliness.** This KPI encompasses three different metrics:

- **On-Time, Ready to Ship**, which measures orders which are completely packaged, with appropriate shipping documents, and ready for pickup.
- **On-Time Shipment,** which measures orders that are shipped on time once prepared.
- **On-Time Delivery**, which measures orders that arrive within the established time frame selected by the customer. This particular metric has overlap with Order Accuracy, since that KPI includes all aspects of a complete and accurate order.

Consistently meeting these three metrics will help ensure maximum customer satisfaction and avoid generating needless expense from corrections, premium or rush shipping fees, and canceled orders.

7. **Order Cycle Time.** Also known as Inventory Cycle Time, this metric measures the amount of time between an order being placed and the moment it ships or arrives at the customer's door, depending on the scope you're using. The shorter the cycle, the more orders you can process, the higher your order fill rate and productivity, and the faster your customers

can get what they need.
You can refine this metric further by tracking both internal processing times and the process as a whole to identify areas most in need of improvement. Another cycle to track under this KPI is known as Put-Away or Dock-to-Stock; it measures the amount of time between an item being received and the time it is properly stocked on your shelves. This metric may prove to be the most important of the three, as optimal order cycle time can't be achieved with sub-optimal dock-to-stock rates.
8. **Dead Stock.** Also known as write-offs, dead stock is product that isn't selling and is draining resources instead of earning profits. It might be damaged, expired, obsolete, or completely destroyed. Whatever the case, dead stock needs to be removed as quickly as possible to keep labor and storage costs low.
9. **Inventory Carrying Costs.** With this metric, you can determine how much of your working capital is currently sitting on the shelves as inventory instead of funding innovation, product development, or expansion. The carrying cost of inventory isn't a single value, but rather a combination of several inventory metrics, including:

- Put-Away
- Dead stock
- Internal warehouse management system (WMS) efficiency

Along with inventory turnover, carrying costs can help you fine-tune your stock levels and determine which items should be prioritized for maximum rate of return. You can also improve cash flow by minimizing needless inventory, freeing up capital for other purposes while you free up storage space.

10. **Supplier KPIs.** A healthy, efficient, and reliable supply chain is essential to your company's success in meeting your own customer's needs. Using vendor management KPIs to evaluate supplier reliability, performance, and compliance can help you quickly refine your supply chain to minimize

disruption, waste, and costly errors while maximizing product quality and order cycle times.

To manage these KPIs effectively, many companies use frameworks (supported by the use of warehouse management software and inventory management software solutions) to extract actionable insights that can be used to effect strategic change.

Both the Supply Chain Operations Reference (SCOR) model established by the American Production Control and Inventory Management Society (APICS) and the Garner Hierarchy of Supply Chain Metrics from Gartner Research are used by companies across all industries worldwide to implement continuous improvement as part of inventory management.

Choosing the Right Inventory Management KPIs

Deciding which KPIs will bring your business the greatest benefit can seem daunting. However, by carefully reviewing your needs, you can quickly identify the KPIs that measure what matters most.

Consider these concepts when choosing inventory KPIs:

- Broad-scope metrics provide reliable overviews, but offer little insight into the specific areas that might be responsible for boosts—or drops!—in performance. Don’t be afraid to optimize the value of harvested insights by narrowing the scope of your KPIs to target processes within workflows.
- In today’s connected workplace, KPIs that bring teams, departments, and business units together to collaborate on shared improvement and success have greater value than old-school metrics that focused on competition instead.

- Your company's strategic, customer satisfaction, and production goals should be a powerful presence in your KPI management. Every metric measured should have a clear and demonstrable value in supporting these goals.
- Recognize and account for the difference between measuring efficiency and measuring relative improvements in efficiency and efficacy. Choose KPIs that help you track continuous improvement as well as actual performance.
- Choose KPIs that provide value while integrating readily with your existing workflows. In cases where significant change is inevitable (e.g., introducing new barcode tags for stock or adding an app for mobile approvals), be sure to provide training and education to ensure your team is ready to support the processes essential to the new KPI.
- Regardless of the KPIs you choose, ensure you're managing them with maximum clarity, convenience, and capability by using an inventory management system (either as a standalone solution or as part of a comprehensive procurement software package) that gives you total control and configurability. Metrics, after all, are only useful if they can be readily tracked, evaluated, and analyzed.Process automation, artificial intelligence, and real-time analytics give you an edge in calculating everything from average order fulfillment time to labor costs for each individual step in your workflows to the average time necessary for customer orders to transfer from the eCommerce site to your production floor.
- Remember the importance of **MIME**:
    - **Mark** areas most in need of improvement and set targets for improvement to be measured by your chosen KPIs.
    - **Implement** corrections, and adjust workflows to support further improvements. For example, you might set an automatic alert to notify key team members when a specific KPI falls below a pre-defined level.

- **Monitor** the results.
- **Edit** your KPIs as appropriate. With aid from effective inventory management software, you can change or remove the KPIs you're monitoring within your dashboard to provide you with the most contextually useful information.

Breathe New Life into Your Business Using Inventory Management KPIs

As the old saying goes, you can't improve something you aren't measuring. Choosing the right KPIs for your business needs, implementing them effectively within your organization, and managing them through a smart, user-friendly software solution will ensure you have everything you need to measure and optimize the workflows essential to happy customers, a strong bottom line, and a strategic, streamlined supply chain.

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