Smart Inventory Management for Increased Profitability

EVERYTHING YOU NEED TO KNOW TO MAXIMIZE INVENTORY TURNOVER, PREVENT AN AMAZON STOCKOUT, AND GROW YOUR AMAZON BUSINESS
Introduction

The key to any successful retail business is a solid inventory management strategy — one that finds you the best-selling products at the lowest supplier prices, protects you from going out of stock, and increases your profitability.

In the following pages this definitive guide to smart inventory management starting with talking the talk and mastering the calculations you need to know all the way through to preventing stock outs, maximizing profitability and increasing your inventory turnover.

Special thanks to our customers for their feedback and our partners Teikametrics, BoxFox, and Appeagle for their contributions to this eBook.

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How to find and set the best price so you can maximize your ROI. Section includes pricing strategies, repricer tools, and more.

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Everything you need to know to prevent an Amazon stockout.

Industry Trends

- 51% of Units sold by Amazon are from 3rd Party Sellers
- 18% sell Home & Kitchen
- 32% sell Private Label

Out-of-stocks, overstocks, and returns cost $1.75 trillion per year.
Part One: Inventory 101: Understanding All Things Inventory & Figuring out What to Sell
Part One: Inventory 101

Inventory Glossary

Inventory Turnover? Reorder Point? Suppressed Listing? These — and many more inventory-related terms — defined.

INVENTORY-SPECIFIC TERMS

- **Amazon Stockout**: A term that refers to going out of stock on Amazon. If you experience a stockout, you’re putting your Amazon account at risk of losing sales, Amazon SEO rank, even selling privileges.

- **Gated vs. Ungated Categories**: Amazon places restrictions on certain product categories, called Gated Categories. To sell within a Gated Category, sellers must go through Amazon’s application and approval processes. For Ungated Categories, sellers can list items without the need for approval from Amazon, but some Ungated Categories come with their own Brand Restrictions. See Pages 9-10 to learn more about restricted categories and products and how to get approval.

- **Inventory Holding Costs**: The cost of carrying or holding inventory. It is the sum of 1) Money tied up in inventory (cost of capital or the opportunity cost of the money), 2) Physical space occupied by inventory (rent, fees, depreciation, utility costs, insurance, taxes, etc.), 3) Cost of handling the items, and 4) Cost of deterioration and obsolescence.

- **Inventory Management**: The practice of overseeing and controlling the ordering, storage, quantities, and restocking of items a company sells.

- **Safety Stock**: A certain amount of extra inventory that functions as a buffer or insurance against an Amazon stockout.

**PRO-TIP**

When it comes to managing your supply chain, make sure you have understanding of each step in the production process, including where your raw materials are coming from, what locations they will have to pass through, where the distributors are located, and how the finished goods will travel to your warehouse.

Understanding all these points could help you eliminate added, unnecessary inventory costs.
INVENTORY-SPECIFIC TERMS (cont.)

- **Supply Chain Management**: The management of the flow of goods/services and the movement/storage of raw materials as inventory is ordered, being created, and shipped out.

- **Lead Time**: The amount of time between when you initiate an inventory order and when your products arrive to your warehouse/shelves.

- **Minimum Order Quantity (MOQ)**: The amount of goods a retailer is required to purchase, at a minimum, from a supplier.

- **Minimum Based Quantity (MBQ)**: Commonly known as ‘Base Stock’. It refers to the minimum amount of stock a retailer has on hand, including back up or safety stock.
COMMON INVENTORY CALCULATIONS

- **Inventory Turnover**: A measure of the number of times inventory is sold within a certain period of time. Inventory turnover is calculated by dividing the cost of goods sold by your average inventory value (or the monetary value of all the goods you have sitting in warehouses or on your inventory shelves).

- **Reorder Point**: A measurement of when you should reorder inventory, based on how many units of inventory you have in stock. It also factors in how long it takes to get inventory (aka your Lead Time) by how many units you sell in a day (aka your Sales Velocity). To calculate the Reorder Point, multiply your lead time by your sales velocity. If you have any Safety Stock, add that to the Reorder Point you just calculated.

  From there, you can calculate when you need to reorder:
  \[(\text{Current Inventory} - \text{Reorder Point}) / \text{Sales Velocity} = \# \text{ of Days Until You Should Order}\]

  For example, if you have 1,000 units of regular inventory, 100 units in Safety Stock, 60 day Lead Time, and a sales velocity of 10 (selling 10 units per day):

  \[
  \text{Reorder Point} = 60 \times 10 = 600. \text{ Add Safety Stock (100)} = 700. \\
  \text{When to Reorder} = (1000 - 700) / 10 = 300/10 = 30 \text{ days}
  \]

- **Economic Order Quantity (EOQ)**: An equation that determines the ideal order quantity a company should purchase to minimize the total costs of inventory (including holding costs, order costs, and shortage costs). Variables include:

  - Carrying cost per unit per year (C)
  - Fixed cost per order (F)
  - Demand in units per year (D)

  The EOQ Formula is as follows:

  \[
  \text{EOQ} = \left( \frac{2FD}{C} \right)^{0.5}
  \]

  To learn more about EOQ, [click here](#) or [calculate yours online](#).

PRO-TIP

Once you've calculated your Inventory Turnover, you can use it to find out how long it takes you, on average, to sell your entire stock of inventory. This can help you determine how often/when/in what quantities you need to re-order. Use the formula:

\[
\text{Time} = \frac{365 \text{ Days}}{\text{Your Inventory Turnover}}
\]

For example, let's say you have an Inventory Turnover ratio of 10 for a given year. By dividing 365/10, you get 36.5 days. In other words, you sell an entire stock of inventory, on average, every 37 days.
SALES

• **Lightning Deal:** A promotion offered in a limited quantity for a short period of time. Products featured as an Amazon Lightning Deal typically see a bump in sales throughout the duration of the deal.

• **Enhanced Brand Content:** A benefit that allows Registered Brands to showcase the unique value proposition of their products through enhanced images, product videos, and custom text formatting.

• **Sponsored Products:** Pay-per-click ads that appear on page 1 of Amazon search results, on product detail pages, alongside and below search results.

• **Demand Forecasting:** Predicting future demand of a product, so you know how much at a minimum to have available.

• **Cash Flow:** The total amount of money being transferred into and out of a business, especially as affecting liquidity.

• **Sales Velocity:** The amount of sales you make in a given time period. Ultimately, this metric tells you how well your product sells when it’s available.

• **Subscribe & Save:** A program for Amazon customers to receive regular deliveries of everyday items in exchange for a discount and free shipping. Orders are replenished based on the time frame a customer selects. Based on any Subscribe & Save orders you have, you’ll know at a bare minimum how much inventory to have available each month.

• **Suppressed Listing:** Product listings that Amazon deliberately hides from search if they do not meet specific standards (such as complete product information, including images, category and item-type, 80-characters-or-less titles, etc. (Find out more about these standards here.)

• **Margin:** The difference between a product’s selling price and how much it cost to produce - effectively, your net revenue.
SOURCING STRATEGIES

- Retail/Online Arbitrage: Buying discounted products from retail stores or online and reselling them on Amazon for a profit.

- Drop Shipping: Buying products from a retailer or wholesaler after you’ve made a sale on Amazon, and having them ship the order directly to the customer.

- Wholesale: Buying brand name products directly from their manufacturer/brand owner, most often in bulk and therefore at a discount.

- Private Label: Buying generic products directly from their manufacturer, adding your own labels, and selling under your own brand.

- Alibaba: One of the largest online marketplaces in the world that is a common sourcing destination for Amazon sellers. Buy in bulk and for a discount.

- Auctions/Thrift Stores: A type of retail arbitrage that is specific to auctions and thrift stores. 35% of Amazon sellers are selling used goods.

- Brand Owner: You fully control the manufacturing and branding of your products.

- Department/Liquidation Stores: A type of retail arbitrage that focuses on large department and liquidated stores like Walmart or Big Lots. These stores often sell heavily discounted items, sometimes at 75% off retail.

- Overstock & Excess Inventory: If you’re ungated in popular brands on Amazon or have an additional sales channel like eBay, check out an online auction site like BoxFox.co to purchase bulk lots of new-condition overstock inventory.

PRO-TIP

Road trip! If you’ve always wanted to take a cross-country road trip, consider it a business trip. Rent an RV and hit discount stores, flea markets, and tag sales along your route to stock up on inventory.

For more information on how to source your products, check out the Payability blog for our 10 Ways to Source Amazon Inventory.
Category & Product Restrictions

In some cases, sellers are required to get approval from Amazon to list certain products or sell within certain categories.

GATED CATEGORIES
Product categories that require approval from Amazon:

- Automotive & Powersports
- Beauty
- Clothing & Accessories
- Collectible Books
- Collectible Coins
- Entertainment Collectibles
- Fine Art
- Gift Cards
- Grocery & Gourmet Foods
- Health & Personal Care
- Independent Design
- Jewelry
- Luggage & Travel Accessories
- Major Appliances
- Services
- Sexual Wellness
- Shoes, Handbags & Sunglasses
- Sports Collectibles
- Textbook Rentals
- Video, DVD & Blu-ray
- Watches
- Wine

PRODUCTS REQUIRING APPROVAL
Even if you sell in an ungated category, you may need approval to sell specific products.

To sell products within the following categories, you’ll need to submit a request to Amazon: Software, Laser Pointers and Related Products, Amazon Frustration-Free Packaging, and Hoverboards.

For more information about how to obtain approval in any of these categories, click here.

PRO-TIP

When you’re evaluating product to source, input some ASIN’s into Seller Central before you buy to make sure you’re cleared to sell those items before you make the investment in inventory,” recommends Josh Cunningham, Growth Manager at BoxFox.
HOW TO GET APPROVAL FOR A GATED CATEGORY OR PRODUCT

Each gated category has its own set of approval requirements (you can find them here). At a minimum, you must meet the following criteria:

- **Account Type:** You must have a Business Selling Account, which is $39 per month.

- **Good Standing:** Your account must be in good standing. Amazon takes third-party seller metrics VERY seriously. To be in good standing, your metrics should be as follows:
  - <4% late shipment rate
  - <1% order defect rate
  - <2.5% pre-fulfillment cancel rate

Depending on the category or product in question, you may need to submit proof of purchase, product images, and/or other product information, so make sure you’re prepared with:

- **Invoices:** Amazon may want to see your invoices, which show them that you’re purchasing legitimate products (i.e. NOT counterfeits) through legitimate methods. Make sure your invoices include your supplier’s information (including company name, address, phone number, and website) as well as your company name and address (as they appear in your Amazon seller account). Note: Retail receipts DO NOT count as invoices.

- **Product Information:** If you have a specific product that needs approval, make sure you have the ASIN, UPC, and Item Model Number handy.

- **Images:** You may need to submit up to five high-resolution product images. You can get these from your supplier or from an existing Amazon listing.

PRO-TIP

Josh at BoxFox recommends “Work to become an expert in specific product categories. This helps focus your sourcing efforts and makes you more capable of negotiating with suppliers.”
Part Two: Buying and Selling At The Right Price to Maximize ROI

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Part Two: Buying and Selling At The Right Price to Maximize ROI

Negotiating Price with Your Suppliers

While you want to build a good relationship with your suppliers, you can’t get what you don’t ask for. There are several ways to build negotiating leverage with your suppliers:

NEGOTIATING PRICE WITH YOUR SUPPLIERS

There are several ways to build negotiating leverage with your suppliers:

• **Know your numbers:** This includes your sales velocity, revenue, and profit margin. The more history you can show of steady or growing sales, the more likely a supplier will be to negotiate.

• **Establish a track record:** Place regular orders and pay for them on time, plain and simple. If you’re just starting to work with a supplier, show your numbers and on-time payment histories.

• **Be specific:** Tell your suppliers exactly what you want (including product name, item number, size, color, quantity, etc.) and what you’re hoping to spend.

• **Consider all points:** The unit price isn’t the only term to negotiate. Ask about shipping methods and costs, minimum order quantity, lead times, packaging and labeling, printing, etc.

• **Shop around:** Often the best way to negotiate is to show a better offer from a competing supplier. Talk to multiple suppliers to see who offers the best deal - and who is willing to beat it. And aside from price, pay attention to your interactions with the various suppliers you’re talking to — who is quickest to respond? Who is the most thorough in their response? Who is going “above and beyond” to win your business?

• **Confirm:** Before you pay for anything, make sure you get confirmation (in writing or via email) on all points that you discussed during the negotiation period. You don’t want any surprises!

• **The Three Ps of Supplier Negotiations:** Be prepared, be persistent, be patient. Know exactly what you want, provide any documentation and numbers that would be helpful, and be prepared to wait for the best price.

**PRO-TIP**

As you’re negotiating with your suppliers, ask to see photos of the manufacturing process. This is a great way to catch any mistakes before your products leave the warehouse, ultimately saving you a lot of time and money.
Part Two: Buying and Selling At The Right Price to Maximize ROI

Setting a Price That Maximizes ROI

Figuring out how to price your products is a critical step in building a solid inventory management system. After all, if you price too low, your stock could fly off the shelves faster than you’re able to replenish it. On the flip side, pricing too high could mean that your inventory doesn’t sell at all. In either case, your margins aren’t looking good.

Appeagle’s Director of Growth Jordan Schanzer says, “When it comes to pricing strategy, online sellers must act fast and stay flexible. Markets are literally changing every second, and competitive prices and scarcity play a major role in profitability.”

- **Repricing Efficiently and Effectively:** With the frequency that prices are changing on Amazon - not to mention the move away from round pricing (i.e. $10.00 or $10.50) - it is just not feasible for sellers to manually change pricing in Seller Central. To make sure your pricing is competitive at all times, and hopefully winning the Buy Box, Jordan suggests, “Sellers should arm themselves with intelligent price management software that will automatically keep them competitive against the most relevant competition on each marketplace without taking up too much of their time.”

- **Maximizing Inventory Turnover:** Inventory Turnover is the key to maximizing revenue and gross profit in retail and especially for Amazon sellers. Jordan offered a couple of key tips saying, “The most efficient way for a seller to maximize inventory turnover is to combine price management software with paid advertisements on third-party marketplaces to optimize sales at the individual SKU level. On top of that, I’d say that sellers must continually make the most informed decisions by leveraging reporting and analytics for purchasing and forecasting.”

**PRO-TIP**

If you still don’t know where to start on price, consult a repricer tool or, at the very least, look at the price and selling history of your product(s) on Amazon.
Part Three: 6 Ways to Ace Inventory Management and How to Prevent an Amazon Stockout

Smart Inventory Management for Increased Profitability

Payability

Smart Inventory Management for Increased Profitability
Part Three: 6 Ways to Ace Inventory Management and How to Prevent an Amazon Stockout

**Introduction**

After you’ve found the right products and set the optimal price, the last thing you want to do is open your Amazon account dashboard and find this:

"Amazon Selling Coach" report with inventory levels at/close to 0 -- something like this:

To help you avoid the dreaded Amazon stockout and simultaneously maximize sales, here are 6 ways to ace inventory management:

**#1 - KNOW YOUR LEAD TIMES & OTHER MANUFACTURING CONSIDERATIONS**

Each step in the production and shipping process takes time - and you’ll want to know exactly how much time in order to accurately predict when you need to place a Resupply Order. While you should absolutely know the overall lead time (which includes every step of the production and shipment process), you may want to also pay close attention to each individual step in the process:

- Lead time
- Manufacturing time
- Product inspection time
- Payment processing time
- Import time (via ocean vs. air)
- Customs delays
- Ground shipping in the U.S.
- Packaging and shipment prep time
- Amazon FBA receiving/stocking time
#2 - KNOW YOUR SALES VELOCITY & AMAZON’S

If you’re not already tracking your sales velocity, now is the time to start. Take a look at how much you’re selling in a given month — or, if you’re new to selling, look at the Amazon sales history of your product. You’ll want to get a sense for how much inventory (at a minimum!) to order, and your sales velocity is your best predictor of that — but it’s not the only one.

In addition to understanding demand for your product(s), you should know when Amazon sees an overall spike in customer traffic, as this could mean more traffic to your listings. Consider the holiday season (especially Black Friday and Cyber Monday), Prime Day, and other holidays throughout the year.

#2 - INVEST IN SAFETY STOCK

Consider adding a buffer to your inventory to account for unexpected spikes in demand or any product damage that may occur in transit. This inventory buffer — also know as Safety Stock - is essentially your insurance against a stockout.

So how much Safety Stock should you actually have on hand? There are a couple ways to determine this. You may want to have a certain number of days of extra inventory, for example an extra week or month’s worth. Or, you might want a certain percentage extra.

If cash flow is an issue, you could add an extra week or two worth of stock to your next order and see what happens. The key is to not over order, otherwise your money will be tied up in inventory that isn’t turning fast enough.

PRO-TIP

One size does not fit all. If you sell a number of different products and/or categories, your inventory management strategy may differ from one to the next. Make sure to account for each product’s individual popularity, sales velocity/cycle, production lead time, etc.
#4 - TAKE DESPERATE MEASURES

As a last resort, you may need to slow your own sales to prevent a stockout. This should only be necessary if a) you need inventory sooner than your lead time allows, b) you’ve experienced an unexpected spike in demand, and c) you don’t have Safety Stock.

There are two ways to do this: Pause any Sponsored Products, Lightning Deals, or other marketing campaigns, and temporarily raise your price.

Meanwhile, make sure you’re talking to your suppliers about getting a new order underway ASAP.

#5 - INVEST IN INVENTORY MANAGEMENT SOFTWARE

You shouldn’t have to handle all aspects of your inventory management strategy on your own. Thankfully, there are a number of Amazon reports and third-party tools to help you keep tabs on your stock levels and reorder points. Some even account for other platforms, in case you sell on sites like Etsy or eBay as well.

Amazon’s inventory reports tell you how much stock you have available to sell and how many days until you run out (based on your current sales velocity). You can also set low stock alerts so when you hit a pre-set minimum, Amazon will remind you to place a Resupply Order. While these are indeed helpful, the alerts don’t factor in your supplier’s actual lead time, which means the alert might be too late.

#6 - KEY CALCULATIONS TO PREVENT A STOCK OUT

Mike Indigaro, who runs business development at Teikametrics shares valuable insights on stockouts, “Naive sellers only see stock outs as a sign of strong sales, but in reality, stocking out can disrupt sales, drive away customers to your competitors and cause any sales rank to plummet, which can take weeks or months to recover from.

To make sure this doesn’t happen, track your Inventory Turns and Days of Inventory. Calculate your optimal DOI, set goals for your turn metrics and measure across products, suppliers and buyers.

You should constantly look for ways to reduce lead-time at each step of the supply chain, negotiate better terms with suppliers and eliminate poor performers to save time and money. These steps will lead to a higher inventory turn rate and optimized DOI that will increase cash flow, allowing you to reinvest capital in profitable investments and avoid costly stock outs"
Conclusion

We hope by now you’re ready to take your inventory management strategy to the next — more profitable — level. Here’s a summary of what you should be doing, at a minimum, to maximize your inventory management, and your business’ growth:

• Work with suppliers that you trust and that are willing to bend their terms to get you the products you need when you need them and at a price that gives you the biggest margins.

• Pay close attention to your numbers, especially sales velocity, seasonal spikes in demand, and sourcing lead times.

• Consider supplementing your own calculations and Amazon inventory reports with inventory management software.

If you do these three things, your business will be set on a path to profitability. Just don’t forget to re-invest your profits in buying more inventory — the more you do this, the more likely your suppliers will be to negotiate terms like unit cost or shipping time.

PAYABILITY

Need help boosting cash flow so you can re-invest profits in inventory? We have a solution for that, too.

Payability gives Amazon sellers faster access to their income within one business day of making a sale. Instead of waiting two weeks for Amazon to pay you (during which you’re likely to run out of stock), you’ll have real-time access to your funds so you can re-invest in inventory, drive more sales, and grow your business faster.

It’s not a loan or a cash advance — it’s your income, as you earn it and when you need it.

Learn more at www.payability.com.

“Payability keeps money in our bank... now I’m buying phones 2-3 times a week because we don’t have to wait two weeks for our Amazon income.”

- Jon Rush, Payability customer and owner of C7 Device Recycle
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