PHANTOM INVENTORY

The Amount of Lost Sales is Greater than Most Retailers Think

Is Phantom Inventory a True Problem?

Phantom Inventory is a common retail industry expression for goods that inventory accounting systems consider to be on hand but are not actually available for purchase. Some retailers refer to this as inventory leveling. These are items that should be selling but they're not available. Available, meaning the customer can easily find product in its home location. Unavailable simply means the customer cannot find product in its home location.

Many retailers are, rightfully, focused on obvious inventory issues like overstocks, excessive markdowns, and out-of-stocks. Further, nailing the correct assortment for each store in a chain is paramount. A retailer's profit hinges on getting these areas right.

Given these challenges, it's easy for the most adept merchandisers to miss the magnitude of their phantom inventory.

Any professional working in retail supply chain understands common inventory issues. A customer may pick up an item and return it to a shelf in another department. Or, a store employee may have left a few items from a shipment on a back-room shelf to stock later but forgets to do it. Most retailers view these instances as few and far between and are focused on multi-million-dollar orders in the supply chain.

Unfortunately, phantom inventory is a much larger issue. If addressed properly, retailers can greatly reduce lost sales from this problem.

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Here are four common reasons phantom inventory exists:

1. Operations Execution: Product is in the back room not on shelf; product is obscured from view by a box or display in the aisle in front of the item. Product is on the wrong shelf or peg within the store; product is behind other similar product on shelf or peg.

2. Inventory Selling Errors: Product not scanned correctly when sold,

3. Inventory Receiving Errors: Recorded and confirmed receiving more product than received into the physical inventory.

4. Employee Theft: Employee remove product from shelf and/or backroom. This happens because retailers do not have the same vigilance with security for the back door as they do for the front doors.

The Culprits

The causes of phantom inventory are multifaceted. For example, understaffing at the store level is one problem a retailer may encounter that can then lead to many other problems. Employees simply do not have enough time to move product from the back room to the sales floor with perfect execution. They intend to go back and retrieve the last few boxes that may not have fit on a pallet, but then run out of time.

Careless or busy customers may pick up a product, continue shopping, and then decide they don't want to buy that item. That item often ends up, not only on the wrong shelf, but the wrong department. When the store is understaffed, there is no clerk available to search shelves for misplaced inventory. Consider that this scenario doesn't happen only once per day. Hundreds of customers shop for dozens of items every day, depending on the type of retailers. A good percentage of items get returned to the wrong shelf in a store.

Employee theft is considered to be a greater issue today than product theft by customers. There are enough security measures in place to prevent or reduce theft by customers: bar codes, security cameras, and human security staff. Less measures are in place to prevent employee theft. A retailer is generally unaffected when an item or two is stolen from one store. Those small losses are built into the pricing of each SKU. However, the employee theft that hurts a retailer is when a well-planned scheme is devised to steal boxes of physically small, high-ticket items. The loss is not just the physical merchandise, but the lost sales associated with it.

Compound these issues across a national retail chain, and it's easy to see how valuable inventory can be left unsold. When a merchandiser in a retail corporate office sees enough unsold product, he or she may initiate a markdown. That markdown directive may be for product that hasn't even left the back room.

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Busting Phantom Inventory

First, retailers need to recognize the magnitude of the problem. It is larger than most believe. To what extent and at what cost is phantom inventory hurting the bottom line? Knowing these answers determine the next course of action. How quickly can a retailer catch and correct the causes or determine the cost they incurred in lost sales? These issues are an HR problem, an operations problem, an accounting problem, and most definitely an inventory problem.

Phantom inventory is best solved by 4R's Phantom Inventory Solution. It includes the following:

- Set up and configuration to accurately analyze the occurrence and probability of phantom inventory
- In-store review to measure the accuracy of the estimation and quantify the potential lost sales
- Implementing a process, in collaboration with the retailer, to systematically evaluate and recommend where the high probability for phantom inventory exists within stores and districts
- Equip the retailer to focus effort on the problematic and highest potential opportunities to increase sales

Old Methods Bring Weak Results

In the past, retailers attempted to solve, or at least reduce, phantom inventory through the operations department. A simple directive to thoroughly check the back room for stock could seem to solve the issue. Again, between employee theft and an understaffed store, that directive won't solve the issue completely.

Having a partner with expertise in phantom inventory helps a retailer understand the extent of the issue, how to prioritize efforts and get the maximum ROI of their time and inventory. 4R gives this insight and practical empowerment to help retailers focus on higher payback efforts.

Less Markdowns

Who hasn't visited a department store in the summer and seen a small display of Christmas items marked down 80%? Many products have a defined shelf life in that they are seasonal product and only relevant during a specific time of year. 4R can assist in helping a retailer prevent markdowns by identifying product categories and stores that are experiencing a high likelihood of phantom inventory. These can be addressed for the retailer relatively quickly, within season, to maximize full margin potential rather than having to mark product down out of season when the product is found.

3 Reasons 4R's Phantom Inventory Solution is Most Profitable

1. The solution helps retailers target stores, items or specific root causes of phantom inventory. 4R delivers quantifiable cost data and the potential value of addressing phantom inventory.
2. The solution leverages machine learning and is guided by the experienced Delivery Team at 4R. This gives the retailer the benefits of the machine learning with configuration and tailoring to give the retailer truly actionable data.
3. Taking action on 4R's data and addressing the causes of phantom inventory have proven to result in increased sales.

Quick Returns

Employing 4R's Phantom Inventory Solution is a relatively quick process. There is no software to deploy and no training of staff. The algorithms used to determine phantom inventory probability are executed as part of a standard weekly processing. The additional implantation steps involve working with the retailer to understand how they intend to use the analysis and the appropriate delivery of the information. This helps the retailer better execute and configure parameters to measure and evaluate results. The process of tuning the solution takes just a few weeks. The results are then available to the retailer to begin to execute and start to position the inventory, making it available for the customer purchase.

Retailers using 4R's Phantom Inventory Solution have seen measurable, tangible results in just a few weeks.

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