

Tight Economy? Audit Your Inventory

Thousands may be sitting on your shelves

By Wendy S. Myers

To please his associates, Dr. Niceguy lets doctors order whatever medications they want. Every NSAID and preventative on the market crowds pharmacy shelves. A recent inventory audit flagged expired products and too many brands of similar drugs. When the hospital administrator hollered for help, I suggested ways to regain control of their inventory and to better manage expenses.

Drugs and medical supply expenses average 15 percent of total revenue, according to *Financial & Productivity Pulsepoints*, Fourth Edition (AAHA Press, 2006). Try these strategies to diagnose and treat inventory ailments in your hospital:



Identify your inventory goals. When I met with the hospital administrator and staff responsible for drug and food inventory, they shared these objectives:

- Decrease the amount of drugs and vendors
- Have physical counts match computer reports
- Get doctors to agree on drug selection
- Prevent expired medications
- Keep product minimums without running out of stock

Identifying objectives will help you create an action plan with specific solutions for your practice's inventory problems.

Schedule a doctors' meeting about consolidating drugs. Veterinarians often have personal preferences, but they will agree to stock less variety when they see the positive impact on profitability of keeping fewer items in inventory.

Start the meeting with a powerful exercise. Pull every preventative off shelves, pile products into a large box and place it in the center of the table. Ask doctors to guess the practice's cost as well as the retail value of this inventory. In most practices, this is easily a five-figure number. The visual exercise will help doctors understand the urgency and need to reduce inventory.

Evaluate differences between similar products. Have doctors list specific drugs you carry in categories such as preventatives, NSAIDs and antibiotics. Create a table that lists each

product name, what makes this product unique, whether it should be our #1 choice and what was last year's revenue from the drug. You'll quickly identify duplicate drugs and sluggish sellers.

Set guidelines for evaluating new drugs. Create a discussion form for doctors to use when choosing medications. Discussion questions might include:

- How is this drug different from similar drugs we stock?
- What is our cost for the drug? What is the expected retail price to clients?
- What profit do I want to make to be sure it's worth stocking and selling an item?
- How often will we use this drug?
- What is our probable inventory turn, or how often will we sell this item?
- If a new drug or product is added, what item will it replace? Practice the one in, one out rule.
- Does the drug have any side effects?
- Does the drug require medication monitoring if used long term?
- What is the shelf life or expiration of the drug?
- What form is the drug available in (liquid, tablet, etc.)?
- What dose sizes are available? (Consider the need to split tablets, carry too many sizes of one drug, etc.)



Get help from vendors. Pharmaceutical representatives can advise you on what quantities you need to stock. For preventatives, ask about point-of-purchase displays, merchandising tips, manufacturer's rebates and samples, reminder postcards and marketing programs that will help you sell more products. Representatives also can host in-clinic training for your team. Vendors can tell you what products are hot and how they're selling in your area and nationally. They'll often give you a heads-up about a new product in development. Find out whether there are quantity price breaks that might be beneficial for you, but be sure you don't buy more than you can sell quickly.

Set inventory reorder points to stock fewer products. Overstocking is common in veterinary practices. The average hospital keeps 100 days of inventory on hand. Because most

vendors can deliver products within a few days, overstocking wastes money. To determine your number of days of inventory on hand, calculate your inventory turnover with this formula: Cost of goods sold (total drug and supply expenses) divided by average inventory (beginning inventory + ending inventory, the sum divided by 2).



Inventory management experts recommend this formula to calculate reorder points: $\text{annual sales/desired turnover} = \text{reorder point}$. Inventory turns over four to five times per year in a typical practice. If your practice sells 100 units per year and takes a conservative approach to turnover, the formula is: $100/4 = 25$. When 25 items remain, you reorder. If you sell 100 units per year divided by 12 months, you

average 8 sales per month. If you reorder when 25 items remain, those products collect dust on shelves for three months before you need them.

A smarter formula for calculating the reorder point is: $\text{annual sales}/12$. If you sell 100 units annually, the reorder point is 8. A more assertive formula would be $\text{annual sales}/18$. Then the reorder point would be 5.

Keep tightening reorder points. If you typically order Product X once inventory reaches 10 units, wait until you reach 8 before reordering. If that works, hold off until you have only 6 units before reordering the next time, and so on. When the reorder point shrinks, you save money over time. If you must add to an order to meet minimums, look first to products that sell quickly.

Check your inventory turnover because you probably have thousands of dollars sitting on the shelf when it could be sitting in the bank.

Create a Savvy Inventory Program

Keeping track of products coming and going is crucial. If you don't have an inventory control program in place, it's time to get serious about managing products and supplies. An inventory control system should:

- Be easy to use and improve efficiency
- Minimize out-of-stocks and emergency shipments
- Increase inventory turnover

- Signal when items need reordering
- Track past and present costs and indicate appropriate pricing as costs change
- Ensure orders are received and back-orders are tracked
- Identify expired or outdated items for removal and/or return to the supplier for credit
- Reduce the risk of employee theft and malpractice liability
- Fulfill certain accounting, tax and insurance requirements for reporting value of inventory on hand
- Generate timely and useful reports to track your investment in inventory and your inventory turns

About the Author:



Wendy S. Myers owns Communication Solutions for Veterinarians in Denver. Her consulting firm helps teams improve compliance, client service and practice management. Communication Solutions for Veterinarians has provided mystery phone shopper training to more than 2,600 receptionists nationwide. Wendy is a partner in Animal Hospital Specialty Center, a 13-doctor AAHA-accredited referral practice offering internal medicine, surgery, neurology, oncology, specialty dentistry, and emergency care in Highlands Ranch, Colorado. She is the author of four books and five videos. Subscribe to Communication Solutions for Veterinarians' e-newsletter on our website at: www.csvets.com. E-mail Wendy at: wmyers@csvets.com.