SupeRx, Inc,\*

Cincinnati, Ohio

SupeRx, Inc is a chain of drugstores with locations in 15 states. The company operates a total of 345 stores that are part of Hook SupeRx, Inc, which operates more than 1100 stores, primarily in the Midwest and Northeast. As in any retail business, the company’s primary functions and concerns revolve around sales growth, profit margins, expense control, and inventory management.

Inventory management is undergoing a rapid transformation from an art to a science. No longer can any retail business expect to operate profitably without a sound inventory management program, and SupeRx has recognized this. A key consideration for the company is product movement information that in turn determines reorder quantities at both the store and warehouse levels. Seasonal fluctuations and advertising can affect product movement, and their effects must be measured using historical data rather than seat-of-the pants guesswork.

General inventory management for SupeRx involves several product categories: basic products carried on an everyday basis, seasonal products carried only during certain times of the year (such as fruitcakes during Christmas), and special items bough on an in-and-out basis throughout the year.

By far the most critical inventory issue is the replenishment of basis products. At SupeRx, as at most retail drug chains, this type of product is ordered under a periodic-review inventory system, with the review period being 1 week. The weekly review uses electronic ordering equipment that scans an order label affixed to the shelf. Such label is located on the shelf directly below each item. Among other information on this label is the “order to quantity”. (Note: This is the replenishment level referred to in the periodic-review inventory model of Section 11.7.) The store employee placing the order determines the quantity to order by subtracting the number of units of product on the shelf from the order-to-quantity (OTQ). For example, if the OTQ is 6 and there are two units of product on the shelf, the quantity ordered would be 4. The OTQ is the key factor in inventory control for basic products.

Several factors are considered in determining individual item OTQs. The most obvious is average weekly demand or movement. SupeRx uses movement figures from the warehouse to the stores. Suppose, for example, an item averages two units per week per store in warehouse deliveries. Setting the OTQ equal to 2 would not allow for sales fluctuations that exceeded the average of 2. To compensate for this and to avoid stockouts, SupeRx sets the OTQ equal to a 3-week demand or movement. Thus, in our example, the OTQ would become 6.

Another factor to consider is whether an item can be ordered in units or cases. In some instances, it is not feasible for the warehouse to deliver in anything less than case quantities. An example would be candy bars. Stores must order a minimum of one case (36 units), no matter what the movement indicates. Thus, the OTQ is 36 or a multiple of 36 to accommodate the case order restriction. Merchandising esthetics must also be considered when determining an OTQ. If an item has four facings or open positions on the shelf, but the optimum OTQ determined by movement is 3, there would be one space without product. This would create an out-of-stock impression to the customer, and, the OTQ would increase to at least 4.

Seasonal fluctuations in movement must be considered when OTQs are determined. For example, the OTQ for a cough and cold item would be significantly higher in January than it would be in July. Adhesive bandages would be just the opposite, with higher usage in the summer than in the winter.

SupeRx is in the process of taking advantage of new technological breakthroughs in inventory management. Today, its OTQs are based on average company warehouse movement into the stored. Soon SupeRx will have a program in place to produce OTQs by item by individual store, based on that store’s movement, rather than on the company movement. Once that in place, SupeRx will be able to accommodate seasonal fluctuations by individual store as well.

The chain drug industry is well behind other retail industries (most notably the grocery industry) in the ability to capture point-of-sale information with the use of scanning registers. SupeRx is in the process of installing them, and once they are in place, the company will be able to use actual point of sale product information instead of warehouse movement. These scanning registers also have the ability to place an order to the warehouse automatically based on what is actually sold that week, so the inventory movement management can only continue to improve.

Good inventory management does not occur in a vacuum, but must be interrelated with sales, gross margin, and expense control objectives. SupeRx is fortunate in that it has had planning software in place for some time. This system allows SupeRx merchandisers to act out “what if” scenarios relating to OTQs product costs, retail sales prices, inventory carrying costs, sales, and other factors. As an example optimum order to quantities normally result in some percentage of missed sales due to individual item movement fluctuations. On the other hand, increasing the OTQs to maximize sales also increases inventory, decreases inventory turnover, and thus ties up capital that could otherwise be used for building new stores, remodeling existing locations, and so on. By using the new inventory management techniques, SupeRx can maximize both sales and inventory turnover. Rapidly becoming a necessity rather than a luxury, the use of this modern technology ensures the maximization of sale, profits, and inventory turnovers that ultimately determine the success or failure of a drug chain.

Questions

1. Does SupeRx use a continuous review or a periodic review inventory system? Why would this system be preferred for a retail business such as SupeRx?
2. What is the decision rule that SupeRx uses to provide a safety stock and minimize stockouts?
3. What is SupeRx doing to obtain information that will help continue to improve inventory management?