

## 11.1: Merchandise Flow

### Learning OUTCOME

- Outline a system for controlling merchandise flow

The most important goal of any buyer is to achieve their sales plan. The second most important priority is to keep inventory levels on plan. If you exceed or fall short of your sales plan, the only adjustment you can make to keep your inventory in line is to adjust the flow of incoming merchandise. If you exceed your sales plan, you must accelerate your flow of goods. If you miss your sales plan, you must reduce your merchandise flow. That said, it is not as simple as it looks.

To begin our discussion of controlling merchandise flow, we have to understand how merchandise is procured by retailers vis-à-vis the annual and seasonal planning and in-season merchandise management process. Let us return to our previous scenario where we are in the role of buyer for a national sporting goods and apparel chain.

We have completed our annual and seasonal sales and merchandise plans and are now ready to begin the procurement process to source the goods needed to execute those plans. In general, purchase commitments are made by buyers based on lead times- a concept we introduced in an earlier section. We might begin by working with our internal product production organization on our in-house label line of goods. Typically, these will be designed and sourced by this internal organization and will have the longest lead time.

Next, we would work with our branded suppliers (Nike, Adidas, etc.) to commit for those purchases for the upcoming season. Finally, we would complete our purchases for the upcoming season by filling in our assortment with other domestic vendors' products.

Now that purchase commitments have been made by our national sporting goods and apparel buyer, we enter the planned selling season. This is where the concept of controlling inventory flow is crucial to a retailer's success. How does the buyer now control that merchandise flow to keep the inventories on plan as sales occur? There are two primary systems for doing so: Supply Chain Management (SCM) and Open-To-Buy (OTB).

We discussed the concept of SCM in an earlier section- a system where the retailer partners with vendors to control all aspects of product production to deliver goods to the retailer as planned. Since SCM systems are controlling production and transportation of product, it is possible to utilize the system to increase or decrease the flow of goods to the retailer. However, keep in mind that due to the longer lead times and overall complexity of a SCM system, there is less flexibility to make large adjustments on the fly short-term.

Using OTB is the primary means retailers use to control the flow of goods in the selling season. Here is a simple Open-To-Buy Formula:

$$\text{B.O.P Inventory} - \text{Sales} - \text{Markdowns} - \text{E.O.P Inventory Plan} = \text{Open-To-Buy}$$

So let's plug in some values to see how the formula works: Assume we start with a Beginning of Period (B.O.P) inventory of \$500,000.00. We experience sales of \$100,000.00, markdowns of \$25,000.00, and our inventory target for the End of Period (E.O.P) is \$600,000.00. What would be our OTB?

$$\$500\text{k (BOP)} - \$100\text{k (Sales)} - \$25\text{k (Markdowns)} - \$600\text{k (EOP)} = \$225\text{k (OTB)}$$

In this example we see an OTB of \$225k (using this formula will yield a negative number but we retailers use absolute value to keep the OTB a positive integer). To double-check your math, you can plug the OTB into the calculation as "Purchases" to ensure you are hitting your EOP target:

$$\$500\text{k (BOP)} - \$100\text{k (Sales)} - \$25\text{k (Markdowns)} + \$225\text{k (Purchases)} = \$600\text{k (EOP Inventory)}$$

Keep in mind that these methods will vary depending on retail organization size, sophistication, business goals, strategies and category of goods.

### Practice Questions

<https://assessments.lumenlearning.co...essments/9261>

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