

Inventory Control and Performance of Manufacturing Company

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ABSTRACT

This paper examined the cost benefit analysis of inventory control in manufacturing industries and to know the effect or challenges facing manufacturing companies and how it can be handled. The researchers made use of secondary data from SOSACO Nigeria Plc. The method used monthly descriptive EOQ (economic order quantity) model, to determine the optimal order quantity via the used of Economic Order Quantity (EOQ) which is an optional policy that would provide adequate inventory level when needed at the minimum total cost of ordering cost and the Economic Production Quantity (EPQ) which is the quantity demand of goods produced by the company to the economic. The method that was used to analyze this data was the EOQ model and EPQ model It was discovered that though the companies guide against ordering material that will effectively minimize the cost in an optimal way nevertheless the manufacturing companies could still do better if all cost that is associated to the production are minimized. The conclusion on this, show that the survival of any company manufacturing organization depends, to some extent on the inventory level being kept by the company. The recommendations made is that the company should adopt the EOQ and the EPQ model so as to adequately tackle the problem of sub-optimization, which result when the factor is under-utilize.

Keywords: Economic Order Quantity (EOQ), Economic Production Quantity (EPQ), Optimisation, Sub-Optimisation

INTRODUCTION

A critical review of the financial statement of most companies would reveal the substantial amount normally held before inventory.

Inventories refer to stock of items used within the production system or the operation of business among which are: raw materials, semi finished

(work – in - progress) and finished goods of a given company. Inventories are stock of goods that are maintained by a business in anticipation of some future demands, such demands could be for products manufactured by the company or supplies used in the transformation process. In other words, inventories are current assets not related to a specific accounting period, their use should as much as possible be regulated within the period to which it relates. The type of inventory kept by a firm depends on the firm in question, the business operation, financial resources and other factors.

Inventory control system must always maintain a sufficient amount of material and supply to meet the demand of the production unit. Being out of stock and item may cause both time and production rescheduling. Management is the function in business of making decision and hence of determining what follows, how resources are used and what is produced. It is a management responsibility to define the nature or organization of a system and how they will operate it. Manufacturing companies has inventories as the centrifugal force that determines their business operations for the availability and quality of those inventories; it is therefore, a parameter for determining their efficiency.

Their investment in inventories is usually so high that proper and continues on them. The stock is an investment which repress out some equivalent amount in cash from which profit or margin is expected. However, where the stock does not attract a profit due to the stock lying follows in the stock than cost storage is profit regarded as loss made on such stock therefore this recognition do this topic. The objectives of this study is to (i) To examine the cost of material handling in terms of delivery to customer and the cost of receipt to be from the Warehouse house. (ii) To examine the benefit to be derived from effective and efficient control of inventory and effect of poor control system. (iii) To identify effectiveness of the procedures and process of inventory management in the manufacturing company. However, the research questions are (i) To what extent does the cost of handing material to its delivery point? (ii) To what extent does the benefit derived from control of inventory system and its cost? (iii) To what extent does the procedures and process of inventory management in the manufacturing companies and its cost? The following hypotheses were formulated (i) H_01 : There is no significant relationship between the cost of handing material and the cost of delivering it.(ii) H_02 : There is no significant relationship between benefit derived from control of inventory and its cost.(iii) H_03 : There is no significant relationship between the process of inventory control and its cost.

LITERATURE REVIEW

There are lots of what in the handling of inventories; some of more significant costs are interest charge storage cost, handling cost, insurance cost, obsolete cost and space utilization. Cost inventories lead to loss of sales and customers of good will.

Obviously, manufacturing companies as a whole are passing through a temperature period as a result of the prevailing state of the economy. The survival of any company depends on how effective and efficient the company's strategies. Nearly all manufacturing concerns are aiming to provide goods and services to customer at the least possible cost in order to generate maximum profit. However, it was realized that without keeping the necessary level of inventory, the manufacturing concern might spend too much on keeping excess inventory or lose customers as a result of keeping insufficient inventory. These adverse effects of keeping excess low level of inventory necessary the need to venture into studying inventory. Cassivi, (2006) traced the genesis of inventory management from the early 1990s. He claimed that the current emphasis in management science probability system. He recalled that in 2004, Orodho, (2003). Developed the first economic lot size equation, which marked the beginning of the use of mathematic medals to represent management science.

According to Dowling, (2002).the idea further and attempting to account for account for a variety of condition whom he published his quantity and economy in manufacturing. In the post period as Zeithaml, & Bitner. (2003). said that analysis of inventory and production control system partly because of the great interest shown by such progressive companies as the Zeithaml, *et al* (2003). Company, The Proctor and Gamble Company, Sutherland, (2001) simply puts his own definition of inventory as an idle resource that possesses economic value. It is important to note that these two definitions connote the same meaning. Lee, (2002), is of the opinion that inventory are also store of goods and stocks.

According to Johnson, (2011) a firm's inventory control can be described as the totality of stock of various kinds. Garland,(2002) also defined inventory control as the science based art controlling amount of stock held in various forms within a business to meet economically the demand placed opened for business. Cunningham, (2001) further observed that inventory control is usually associated with manufacturing industry. But many do occur in re – organization such as demand services, transport undertaking, hospital and so on. Ketzenberg, Metter, & Vargas, V. (2000) referred to inventory as

any resources physical financial or human that has value because it can further satisfy a future need.

Cunningham, (2001) saw inventory as the physical stock of goods which enough remain idle in a store but is essential for smooth sailing of the company Monks (1900) from 25% of their current asset depending on the firm and the type of industry. Any inventory system requires are the collection and processing of large quantity of data, in these pre-computer days. The cost of data collection and processing was quite high. Consequently, these inventories were relatively simple starting in the 1950's according to Hasapidis, (2001) Computer brought down the handling data. Hasapidis, (2001) briefly stated that task objective in holding raw material inventory is to separate purchase and production activities. Nevertheless, it is believed that as long as we continue to have operation researchers with emphasis on inventory management there will be no shortage of supply of definition of inventory control system.

INVENTORY MANAGEMENT CONTROL

In any business organization, the functions of management are planning, motivating, coordinating, directing, staffing, controlling and so on. Inventory the management rest mainly on planning and controlling for it convey meaning. Planning as a management function is deciding in advance what to do, how to do it, when to do it, who is to do it Barratt (2004). Therefore, inventory planning involves the determination of inventory needs of the company in advance for maintain flock of production schedule, for proper inventory planning, information on past usage is to be available with size of the company warehouse has to be considered with production estimated will have to be evaluate cost associated with inventory acquisition and holding and the likes have to thoroughly considered. Controlling is the measuring and correcting of activities of subordinate to ensure that events conform to plans. Thus, it measures performance against goal and plan show where negative deviation exist and by putting in motion actions to correct deviations, helps to ensures accomplishment of plans.

Herbert (1990) defined inventory control as a systematic method of recording and reporting the movement of material work - in - progress and finished goods through a company. Therefore, control process commence on loss planning is accomplished. Inventory control has the following objectives:

- I. Ensuring that the right amount and quantity of materials are available when needed
- II. To maintain accurate cost as much as possible
- III. To reduce storage cost and provide management data
- IV. To give consumer maximum satisfaction and this increase the returns on investments.

CLASSIFICATION OF INVENTORY

There are four (4) main classes of inventory namely;

- i. Raw – material inventory: - This is the stock of goods from which the product of the company is made.
- ii. Work – in – progress: - This can be called the intermediate stage, between the raw material and final output stage that is materials that have been transformed but not to the final desired stage.
- iii. Finished Goods inventory: - This is final stage of production. This consists of all stocks that is ready for sales (Weiss and Gashon 2009) e.g. SOSACO Nigeria Plc: milk, margarine, cornflakes, seasoning Benton, & Maloni, (2005). etc. as part of finished goods.
- iv. Supplies and miscellaneous inventory: These include any item stock by a company that do not become part to final product but needed in for the company to function e.g. office supplies lubricating oil etc.

REASON FOR INVENTORIES

Inventory play a vital role in the operation of business the reason for the existence of inventory is that , it is completely impractical for many reason to produce on item upon demand Holweg, & Pil, (2004), identified there(3)general motive for holding inventories. The transaction motive. The precautionary motive and the speculative motives

- i. Transaction motive: This assures that a given level of production require a minimum level of inventory that is for a day to day operation
- ii. Precautionary motive: To guide against uncertainty since demand can not predict with certainty
- iii. Speculative motive This is necessary because of time of sufficient rapid price rise as well if there are no changes in cost or in the possibilities of sale within a fordable be used as an ledge against the uncertainty because as an ledge against the uncertainty of price change and the availability of materials Premaratne, (2001) modern concept of inventory management can be trace to 1990-2007. When several management scholars develop on economic size of equation, which immerse the cost of ordering and holding for cases where demand was

known and constant. Cachon, & Olivares, (2010), put in the inventory control and management are essential because of profit maximization.

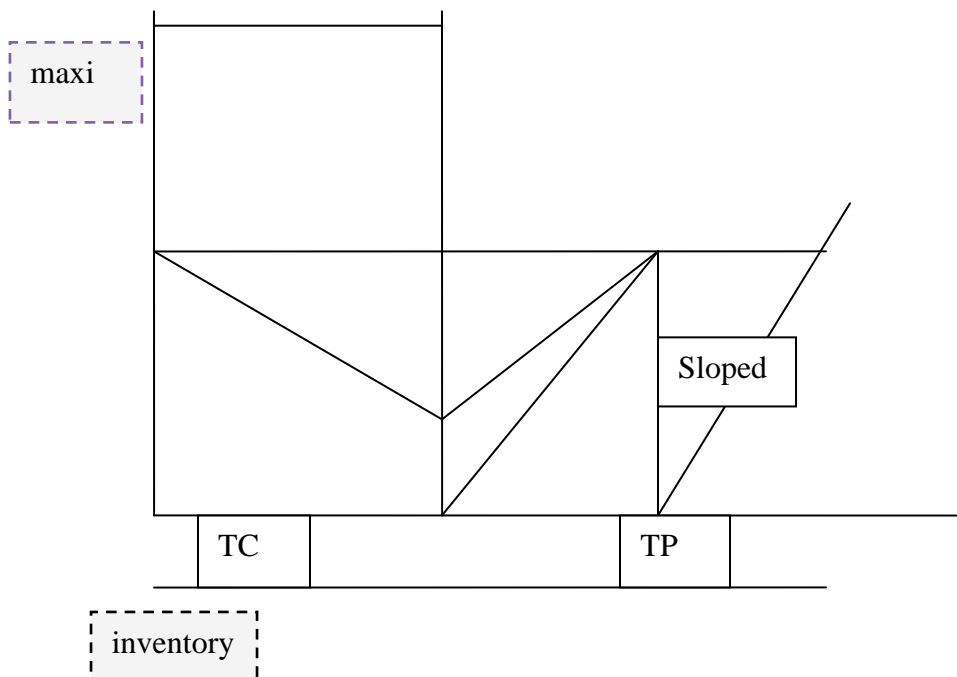
Various methods exist for regulation inventory procedure. They are from one organization to the other, the following parameter of an inventor , ordering or set up cost carrying or holding cost stock out and purchase price either cost include overtime cost labour inventory cost etc (a) .Demand: Inventory decision are made with reference to a future demand three state of knowledge can exist with regard to this level may be possible that we known with certainty what the future level of demand will be we may also be estimate the profitability distribute of the future level of demand, which is in inventory problem under risk, in it last cases, we known nothing about live hood of future of demand this is called an inventory under uncertainty. (b). Lead time: Welss and Gerson (1987) put it as the period between when and order is place and the time the supplies arrive in other word this equal the time clasped from the moment and inventory are kept to: (i.) Meet demand for perishable goods (ii). Buy and irregular supply of raw material or finished goods.

According to Lewis 2004), The arm of inventory control system is to held by a business at the level of stock held by a business at level which optimized some management criteria such as minimizing the cost maximizing the business profit providing at a state minimum customer classified the purpose of inventory as follows (i) They aid continuous production by ensuring that input are always available an economic production can be (ii)They do successive stage in producing a product that downtown is one that does not stop the entire process (iii) They provide service to customer with varying us l demand and various location by maintaining and adequate supply to meet their immediate seasonal need Traditionally, inventory model seek to minimize cost rather tan the increase profit. to keep an optional level of invention, their should Effective balance in the four made inventory related cost(i) **Ordering Set Up Cost** : The first is ordering cost that is the placing of an order .They are according to Joshi (2009) is obtained and include similar cost such a purchasing inspection as well as expense of delivery postage, telephone or sending a telex to the supplier , and trying out an order .(ii) **Carrying or Holding Cost**: To carry inventory cost or group money . This cost was to be broken down into several components.

The first is the inventory which could for another productive purpose to this opportunity cost, we must also add storage space must be bind vented ,

it become a legitimate management expense , in other hand , there are no marginal storage cost .(c.) **Replacement Rate and Replacement Period:** The replenish period is the time during which unit of a particular order are added to the inventory while replenishment rate is the quantity on inventory delivery per time. (d) **The Average Inventory:** According to Joshi (2005) this parameter is useful for decision making on well as for insurance and taxation. He said further that if demand is constant the replenishment is instantaneous and there is neither shortage nor surplus. The average inventory equal exactly half of the initial inventory serves to discourage large quantity in frequent order for goods which suffer this affliction. Johnson, (2001) summarize the cost of carrying in the following way $I=C+G+K+T$ Where I=cost of carrying inventory percent per period, C=opportunity cost of carrying inventory percent per period, K=deterioration and obsolescence and K=taxes percent per period. (iii) Stock out: This can be referred to a shortage. (iv) Age cost: This cost can be attributed to running out of cost and also cost money when an item can not b supplies on demand then a shortage have occurred If the customer is willing to wait according to Arnold, (2002) there are administration cost which are associate with such expediting of the order and customer notification when the item profit on the goodwill may be considered. According to him , stock at hand include stock act order demand order , which have already been committed to production programmed , under , this policy ,a replenishment order place is generally for a fixed quantity.

Inventory Model



The explicitly interpretation of the third diagram is contain in little child explanations. He explained future that the solid line represents the inventory broken a replenishment order of is place. But there is a delay before the order actually arrive which is known as lead time (L). In each cases , The stock on hand immediately vise of (since the moment actual stock continue to be depleted by successive demand withdrawal until lead time expire and the replenishment order is received at time to the process is repeated as stock on hand again to read or level Maximum time

INVENTORY POLICIES

Inventory policies are of two types. One is that in which decision concerning replenishment held is known as reorder level policy and the other is that in which such decision are made on time basic is known as periodic system.

RE ORDER LEVEL

This system operates on the maximum and minimum level stock with the minimum, stock serving as safety stock, it is called the continuous review policy. Order point level also tend to minimize, compare to protect against possible shortage and they are therefore generally used when the unit cost of item high in the diagram below, little child (1990) is place when the

stock on hand capital equal or falls below fixed valued M known as the re-order level.

PERIODIC REVIEW SYSTEMS

According to little child (1990) order are placed at predetermined point in the generation representing fixed interval say weekly, monthly. In this system, the quantity order varies at the time of review

ECONOMIC ORDER QUANTITY EOQ MODEL

An optimal inventory policy is one that would provide adequate inventory level when needed at the minimum total cost of ordering carrying and this purchase table able to calculate a basic economic order quantity, certain assumption are necessary they are:

- i. They are rate is known and constant.
- ii. The per unit purchase on production cost per unit holding cost and order cost are independent that out of the quantity needed.
- iii. They are replenishment rate is ultimate.
- iv. That lead time is sew

That no stock out allowed. It should be noted that most procurement inventory model fall into two categories they are:

- i. Deterministic model
- ii. Probabilistic model

Deterministic model is different from probabilities model in assure condition of certainty, both model attempt to minimize cost maximize contribution through trading of carrying cost, ordering cost and stock out costs. For the purpose of this write up, economic order quantity will be formulated within the frame work of deterministic model. The equation below shows an inventory system that satisfies all the assumption of an EOQ model. Also it is pertinent to know the parameter of an EOQ model

$$\underline{DTC = PCH} = \underline{DCO}$$

$$DQP \quad 2 \quad Q^2 \quad 2DCO = Q^2 \text{ (Squaring both size)}$$

$$\text{And when } \underline{DTC} = 0 \text{ cost are minimum} \quad \underline{PCH}$$

$$\underline{DQ} \quad Q = Q = 2DCO$$

$$\text{That is } 0 = \underline{PHC} - \underline{DCO}$$

$$\text{And to find } Q^2 \quad Q^2$$

$$PCH$$

$$\frac{DCO}{Q^2} = \frac{PCH}{2}$$

$$2DCO = Q^2 PCH$$

The relationship between ordering cost and holding cost

MATERIAL AND METHODOLOGY

Secondary data were obtained from the following:

- (i) The company accounting record.
- (ii) The company production schedule.
- (iii) The company statement of audit account. The method that was used to analyze this data study was the EOQ model and EPQ model to the motive of management to determine the right quantity to order and who to order them as relate to inventory management and control is available of right quantity and quantity of human material input to meet production at anytime.

The essence of this is to avoid committing management blunt or by keeper excess or inadequate stock which could be economic waste. The method used monthly descriptive EOQ (economic order quantity) model, this was used to determine the optimal order quantity, then at a point in time order will be equal to holding cost at this point the economic level is reached where the order quantity and the total inventory cost is maximum. The EPQ (economic production quantity) model was to find the find the rational amount of production capacity to be covered by the company at any $Q = 2DCO$

DATA PRESENTATION

TABULATION OF DATA

Production Material	Annual Demand Kg	Material Cost Per Ton	Ordering Cost Per Order	Average Quantity of Order	Number of Order Per Year	Carrying Cost of Inventory
Takum Powder	83298	13437	25152.19	27766	3	20%
Menthol Natural	7144	125,53	26,140.6	238	3	20%
Camphor Powder	9786	70	14483	3262	3	20%

Material purchase and inventory cost of May 2016, material store purchase and cost accounting record of Sosaco Nigeria plc.

The data obtained regarding the company product are tabulated below:

Production Material	Annual Demand Kg	Material Cost Per Ton	Ordering Cost Per Order	Average Quantity of Order	Number of Order Per Year	Carrying Cost of Inventory
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Material store purchase and cost accounting record of Sosaco Nigeria Plc June 2016.

This implies that Gino tomatoes should be produce in a year

$$= 250$$

$$143 = 1.73$$

$$= 2\text{days}$$

This signifies that each run of 143 should be once in every 2 working days

3. Total inventory cost

$$CTo = \frac{DCO}{Q} + \frac{(Q(r-d) PCH)}{2r}$$

$$D = 40$$

$$Cs = 9.50$$

$$R = 1,698.215 \text{ units}$$

$$P = 0.133$$

$$CH = 20\%$$

$$Q = 2856.199$$

$$\frac{409,000,000 \times 9.5}{2,853,199} + \frac{(2855.199(1.698.215))}{2 \times 1.698,215}$$

$$-(1687,272) 0.183$$

$$= \#1,361.80 + 1361,80$$

$$2,713.60$$

1. Optimal production run for cornflakes

$$D = 86650,000\text{units}$$

$$P = 6,092$$

$$CH = 20\%$$

$$r = 365,44\text{unit}$$

$$\begin{aligned}
 Q &= \frac{2DCS(r)}{PCH(r-d)} \\
 &= \frac{2 \times 88,050,006 \times 835 \times (365,44)}{0.092 \times 0.2(365,444 - 351,759)} \\
 &= \frac{176,100,000 \times 3,051,459.4}{0.0184 \times 13685} \\
 &= \frac{251.804}{23,181,062,27} \\
 &= \frac{15,86833325}{1,460837.858} = 1460,838 \\
 &= 1,466,837 \text{ unit per production run}
 \end{aligned}$$

2. Optimal number of run per year and optimal time between successive run

$$\begin{aligned}
 N &= \frac{D}{Q} \quad \text{and} \quad T = \frac{W}{N} \\
 \frac{250}{N} &= N = 88.000, 000 \\
 &= 60 \text{ run per year}
 \end{aligned}$$

This indicate that cornflake should be produce in 60 run per year

$$\begin{aligned}
 T &= \frac{250}{60} \\
 &= 4.16 \\
 &= 4 \text{ days}
 \end{aligned}$$

This signifies that each run of 60 should be scheduled once in every days working.

$$\begin{aligned}
 &\text{Total inventory cost} \\
 CT0 &= \frac{DCO}{Q} + \frac{(Q(r-d) PCH)}{2r} \\
 D &= 88,050,000 \text{ units} \\
 CS &= 8.35 \\
 R &= 365,444 \text{ units} \\
 P &= 0.92
 \end{aligned}$$

$$\begin{aligned}
 Q &= 1,60,438 \text{ units} \\
 &= \frac{88,050,000 \times 8.35}{1,469,838} + \frac{(1,460,438(365,444 - 351,7590.092 \times 0.2))}{2 \times 365,444} \\
 &= \#503.28 + 503.28 \\
 &= 1006.56
 \end{aligned}$$

DISCUSSION AND INTERPRETATION

It is pertinent to know that inventory is an internal aspect of and manufacturing concern as such should be recorded with necessary attention.

The analysis show that Sosaco Nigeria plc is benefiting optimally from other inventory management system currently being used giving by the expectation process of keeping inventory.

The characteristic of cost saving of EOQ model showed that the company could have saved about #81,257, 87 per annum on the raw material considered on the other hand, it also showed that the cost saving of the EPQ model on the three finished goods amount to #8,136,6.9 these show that the company is looking huge amount of money by not using EOQ and EPQ models.

SUMMARY

The essence of carrying out this research out of the need to minimize cost and maximum profit through effective and efficient inventory management. Obviously, the current economic situation decision hence, management needs to formulate policy and strategies on how to make considerable returns.

The study also show that the quantity of a given item of order by Sosaco Nigeria plc at any period in time is determine by the nature and capacity in production scheduled meaning that quantity order that each period varies and are how on the average. If adjustment could be made in the total cost of order that it thus enhancing Sosaco Nigeria plc profit and ensuring that it says in business and even complete favorable in its environment with competitions.

Finally, the model used in this study was found to be more adequate than parched by Sosaco Nigeria plc using the EPQ and EOQ model, total cost incurred in keeping inventory was found to be significant on how about

twice less than what is incurred order the firm's current method of inventory management

CONCLUSION

This study has showed that the survival of any manufacturing organization depends (to some extent on the inventory level being kept by the company. Obviously, we have attempted in this topic to show that inventory constitute a critical and in most cases, a sizable investment of firm's resources on which considerable cost saving be made with made with sound inventory management policy.

Furthermore, one of the major objectives of any business organization is to maximize profit and minimize cost, therefore the desire level of inventory decision in order to meet their demand and time. Management should plan for inventory control such that an insufficient excessive inventory situation is never allowed. Also, the attempt in the Sosaco Nigeria plc functional specialist irrespective of their areas of calling the inventory are not dust held to meet production demand but also guide against risk of stock out.

RECOMMENDATIONS

All manufacturing company should adopt the EOQ and EPQ model so as to adequately tackle the problem of sub- optimization, which result when the factor of production are under – utilize, it can be usually recalled from our finding that the calculated economic batch quantity was far above what is being produce, these different represent sub- optimization of production scales. Furthermore, the EOQ and EPQ model must be adequately applied to guide against ordering materials below or above the normal quantity that will effectively minimize the cost in an optimal way The company should seek for way of sourcing for raw material in the order to reduce the burden of high ordering cost and high exchange rate The company should make provision for shortage facilitate has hindered the will minimize cost in the most simple way. There is need to have a material control division in between the purchasing and storage division ,Storage personnel should be encourage so that maximum output could be attained by motivation them through worthy recommendation, improving the working condition through enough and accommodate storage space dynamic training and enchase remuneration.

The company should introduce efficient inventory management system Government should come to aid of companies by monitoring and impart duties and tariff. Lastly, optimal level for every important item should be

worked out and maintained in order to achieve the result for the organization.

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