



Logistics Takeaways from Introduction to Retail Financials

Retail Profit and Loss Statement

This class introduces you to Retail Financials. It is designed to teach you the key points without needing to be an accountant. It starts with a breakdown of the main headings in a retail profit and loss statement.

There are four major ways a retailer can increase profits:

- Increase sales - either by increasing actual sales or reducing markdowns
- Reduce cost of goods - by improving sourcing, better negotiation and/or supply chain efficiencies
- Reduce expenses - through more automation and other types of efficiency improvement
- Reduce interest charges through efficient use of inventory.

How does logistics or improved supply chain processes help? It can contribute to increasing sales by increasing availability on the shelf, and it can do this by getting out of stock products back in stock faster. It can also increase sales by avoiding clearance markdowns, through faster e-commerce returns. It can make a small contribution to reducing the cost of goods by reducing shrink (retail stock losses due to theft, administrative errors, and damage to products) and avoiding demurrage charges in some cases. It can reduce expenses by automation and reducing labour. It can reduce interest charges by eliminating an element of cycle time stock by speeding stock through the supply chain faster.

Balance Sheet

A balance sheet gets its name because it has two sides which must balance each other. One side is the money invested in the business from various sources, such as share capital and long-term loans. The other side is how the money has been spent.

On the spent side there are current assets, fixed assets, and liabilities. The biggest current asset for most retailers is stock. Stock consists of cycle time stock and safety stock. Cycle time stock is often 40% of the total stock and safety stock makes up the rest. Logistics can impact this by reducing the cycle time element. Reducing stock releases cash to be invested in other things, like opening new stores. It also reduces the inventory carrying cost in the profit and loss account.

The inventory carrying cost has two components – the financial cost and the physical cost. The financial cost is cost of money tied up in the inventory. The physical cost is the cost of space to store it, security, shrink, periodic inventory counts and associated administration. It does not include the cost to receive it, pick it, ship it and associated handling costs. In current inflationary



times, the total carrying cost can be 12% to 15% of the cost value of the average inventory. So reducing inventory reduces carrying cost. In the US, a typical Target store could hold US \$4m to \$5m average inventory and that's just one store. So the carrying cost for that store alone could be \$125,000 a year. Reducing average inventory by 1% (roughly equal to 3.65 days' worth of unit sales) could save \$1,500 a year. Multiply that by the number of stores and then count in the warehouse stocks as well and you reach very large sums of money.

Fixed assets is also a big number for most retailers. This includes, buildings, fixtures and fittings, forklift trucks, other automation, transport fleets and similar. These assets incur annual depreciation charges, which reduces profitability. Logistics service providers can sometimes help retailers avoid some fixed asset costs, reducing business finance costs and the trade-off of supplier expenses versus asset depreciation may be beneficial. In this case, you have to do the sums to be sure, but it is worth looking at in major accounts.

Cash Flow

Retailers are unlike many other businesses in the sense that their customers often pay them before they have to pay their suppliers. This is less true of imports and less true of small retailers, who do not have negotiating leverage. By speeding up the sale of goods before the retailer's payment terms to suppliers are exceeded, the retailer's cash flow improves. Many large retailers invest their surplus cash on the overnight money markets to make an interest income. Getting out of stocks in stores replenished faster is a potential contribution to improving their cash flow.

