

Inventory Turns: The Key Metric to Making Your Money Work for You Management Article March 2010

I get a lot of questions about inventory turns because they can be hard to understand. Even harder to understand or model is how turns affect cash flow. However, the entrepreneur who measures turn and appreciates the connection is much more likely to prosper in the long run.

First, defining inventory turns.

It seems simple: How many times did you turn your inventory? However, there are many ways to view inventory turns -- including financially (at cost or retail) and physically.

I will try to make it as simple as possible.

If we buy a widget for \$1,000 and we sell that widget for \$3,000 and we sell one every three months, we have 4 turns annually at retail. (12 months in a year, divided by three months, equals four turns)

Now in the auto salvage business, if we pay \$1,000 for a car, and we sell \$1,000 in parts off of it in 30 days, we have 12 turns at cost and 30 days to break even.

Let's think about cash flows. If we pay \$1,000 for a car, and we sell \$3,000 worth of parts off of it in a year, our \$1,000 produces one turn at retail, and \$3,000 in cash flows. It also produces \$2,000 in gross margin, with a 33% cost of goods sold and a 66% gross margin.

Now if we buy a car, and sell \$3,000 off of it in 90 days, we have 4 turns, the same gross margin of 66% is applicable, but we produce \$12,000 in annual cash flows. This assumes we take our \$1,000 and reinvest it every 90 days in another car.

In both cases we have a 33% cost of goods and a 66% gross margin.

So, if you have 4 turns per year, you will produce \$12,000 in cash flow, \$8,000 in gross margin (That's what you pay bills with or buy momma a new car with!)

But, if you have one turn, you only get \$3,000 in cash flow, \$2,000 to pay bills with, and in all likelihood, momma won't get a new car.

The owner of any kind of small business can benefit from understanding how quickly inventory is turning, the different kinds of turns, and how much harder money works when inventory can be made to turn a little bit faster.

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Ron Sturgeon, founder of [Mr. Mission Possible](#) small business consulting, combines over 35 years of entrepreneurship with an extensive resume in consulting, speaking, and [publishing](#), and 3 business books with 2 more expected in 2010. Ron's consulting expertise and clients extends to all types of business from restaurants to attorney firms. He helps with sales, productions, financial, strategy and startups to name a few of the areas he is proficient in.

A business owner since age 17, Ron sold his chain of salvage yards to Ford Motor Company in 1999, and his innovations in database-driven direct marketing have been profiled in [Inc. Magazine](#). After the repurchase of Greenleaf Auto Recyclers from Ford and sale to Schnitzer Industries, Ron is now owner of the [DFW Elite Auto](#) suite of businesses and a successful real estate investor.

As a [consultant](#) and [peer benchmarking](#) leader, Ron shares his expertise in strategic planning, capitalization, compensation, growing market share, and more in his signature plain-spoken style, providing field-proven, high-profit best practices well ahead of the business news curve.

To inquire about peer benchmarking, consultations, or keynote speaking, contact Ron by calling 817-834-3625, by emailing rons@MrMissionPossible.com, by mailing 5940 Eden, Haltom City, TX 76117, or online at [Mr. Mission Possible](#).