NEW SOFTWARE TO HELP FIRMS ASSESS MARGIN WEAKNESSES

This month, Anglia Business Solutions looks at how a cost per transaction tool can help businesses measure their margins in today's pressurised financial environment

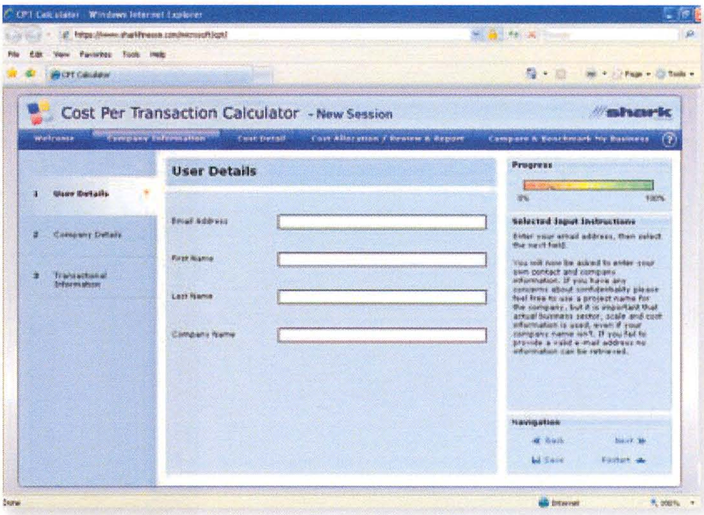
IT WILL not come as a bolt from the blue to those in the fresh produce market that margins are coming under increasing pressure.

The industry is rife with stories of suppliers being hauled in by the major retailers and requested to cut their margins. This is despite increasing fuel prices and general overheads. When virtually your whole business depends on a single supermarket contract, it is difficult to refuse.

Some are already reaching the point where enough is enough, and pulling away from unprofitable contracts. Taypack Potatoes was a case in point, as reported in the May 9 issue of FPJ. In the article, it explained that the company had carried out a review of the contract and concluded that it is not commercially viable. It therefore suggested that Asda takes its £30 million business elsewhere. It does beg the question of whether the fresh produce industry can generate sufficient profits to warrant the continued investments required to meet customer demands.

At top level, the UK fresh produce sector is an £8 billion industry. It is also expanding as people's eating habits change, driven by the trend towards a healthier lifestyle. Based on a small sample, the 2006-07 report and accounts of a dozen of the top industry players, some of the gross margins vary between eight per cent and 17 per cent, dependent on the business models employed by the company. A recent Plimsoll report flagged the fact that the average net margin of the top 100 players is just 1.7 per cent of turnover. This does not leave a lot of room for error in a low margin business.

However, the straw poll of some of the top companies does reveal some significant differences in their operating costs. It shows that some businesses incur higher costs than others, even when operating similar business models. The margins vary dependent on the sector, with those in the same sectors broadly generating similar gross margins. The differences appear in the administrative costs section, where they are identified separately. These can represent as little as 3.6 per cent of turnover, or as much as eight per cent. In a £100m business, this can make more than a £4m annual difference to the bottom line.



The reality is that few organisations, apart from the government, can afford to continue to operate with high administrative overheads.

In today's highly regulated food industry, companies are incurring higher administrative costs to ensure compliance and to deal with product traceability requirements. Usually, these are handled in an expanding business by the recruitment of further administrative staff. Apart from the unavoidable increase in overheads, copying information from one source to another invariably introduces delays and errors in the internal processes. This can be anathema to a fast-moving operation, as produce movements can be slowed to enable the paperwork to catch up.

One of the problems is that there are few reliable benchmarks within the industry against which to measure operational efficiency. How do you know whether you need to invest either four or eight per cent in your administrative procedures to ensure that your operations are efficiently managed?

Furthermore, it is possible that in various organisations, processes are described and costed differently. Comparisons may not therefore be relevant on a like-for-like basis. However, as with all businesses, the health of the enterprise will be defined by its ability to generate bottom line profits.

One area that Microsoft, in partnership with a company called Shark Finesse, is currently investigating is in the measurement of the costs of business transactions. The idea is to provide a widely available tool, pictured, designed to enable businesses to capture and calculate their costs per transaction (CPT). It also enables organisations to compare their CPT rating against the norms across a variety of sectors. The identity of each user is kept confidential, while the data is added to the pool for analysis. The deliverable from the exercise is a personalised report for that company which can be used to put a stake in the ground. This can then be accessed and updated as the organisation refines its processes in the interests of efficiency and cost savings.

The squeeze on margins is causing many organisations to look at their cost base in parallel with the growth of turnover. Some will conclude that certain contracts are simply not worth having, as in the case of Taypack and Asda. Others will explore how tools like fully integrated enterprise resource planning (ERP) systems can assist, by automating many of the administrative tasks carried out within the business.

In the final analysis, if we assume that the average margin across the fresh produce industry is 12.5 per cent, there is more than £1bn of gross profit up for grabs in the UK. It would be foolish to assume that the strongest players only will prosper in this environment. Those who are fleetest of foot and embrace change can prosper even in this most demanding and competitive of sectors.

The tool can be accessed at *www.sharkfinesse.com/microsoft/cpt/*