

Change your tune

Does taking a more harmonious approach to your supply chain issues mean no more flaky supplier headaches and no more lengthy credit wranglings? *Excellence in Leadership* listens in to **Michael Hitchcock** of Moss Bros, Pret a Manger's **Nick Candler** and **David Bateman** of Paperchase.



From maximising profits to efficient measurement of return on investment, FDs and CFOs are constantly told that they need to improve to reach an optimum level of performance. High on this list of priorities is the drive to get the best possible performance from working capital.

For most companies, maximising the flow of cash through the business is key to maintaining its financial performance. After all, cash is king. However, while the physical supply chain has seen huge developments in efficiency and innovation over recent years, the financial supply chain – where cashflow must be optimised while ensuring that suppliers are paid on time – has often been overlooked.

The term financial supply chain (FSC) has only come into use relatively recently. In the past it was largely covered by techniques such as factoring and invoice financing. But for the new generation of lenders offering FSC, the guiding principle is collaboration. Banks are offering services to companies whereby they can extend finance to their suppliers in return for better payment terms. As one of the many firms offering this to corporates claims, FSC aims to optimise accounts payable and receivable, cash management, working capital, transaction costs, risk and administration. Indeed, one recent study carried out by Visa revealed that a £1 billion revenue company could save £10 million in working capital costs if it managed its cashflows with suppliers more carefully.

Excellence in Leadership spoke to three finance directors of businesses in the UK. Michael Hitchcock has a long background in retail, taking in stints at bookshop chain Ottakars and now men's fashion retailer Moss Bros; Nick Candler, FD of fast food chain Pret a Manger; and David Bateman, who took over as FD at boutique stationers Paperchase in 2000 has worked with private equity backing and at a US corporate.

Is the financial supply chain anything new, or is it simply a fancy name for good supplier management?

David Bateman: Well, there can be huge amounts of cost embedded within the supply chain and I think you need to make sure you challenge that while adhering to your corporate strategy. I think we, as a business, and the retail sector generally, possibly don't take this seriously enough. Really, retailers need to take a proper look at the level of costs within the financial supply chain and



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how best to manage them. If, like us, you decide to move the business to a global platform, then you might start trading in Australia, say. Now you can do that, but can you do it efficiently or profitably? Just because you've got a supply chain that services several parts of the world, it doesn't necessarily mean that you can service that new territory efficiently.

How do you manage your financial supply chain to make sure you're on top of risk?

Michael Hitchcock: We're constantly looking at ways of managing risk through the supply chain. Currently we use indirect sourcing and by that I mean we use a middleperson. They basically make sure the stock is available when we want it and if it's not, then they pay a financial penalty. The flow of goods through our supply chain is more fluent so we don't have the risks of production stalling in the Far East, or a strike on the dockside or problems with the containers or heaven forbid the ship going down.

That means all our risk is with the middle person. We obviously don't currently get the downstream margin you can achieve when you source product directly. But it also means that we're not exposed to currency fluctuations as all our prices are set in sterling. That means we don't need a big treasury team here that has to hedge forward or get involved with letters of credit. We also don't need people on the ground, which you do need with direct sourcing. We avoid all that central cost and risk by using that middle person extensively.

How important is forecasting in protecting your financial supply chain?

Nick Candler: In the long term, we do a cashflow forecast over a three-year horizon. Then we do detailed cashflow forecasts on a monthly horizon and daily cashflow forecasts along with that. So we think it's really important to get the business fully forecasted and connected to the granularity and detail based on that period.

DB: Supply chain cashflow forecasting is not the most critical part of my job, although in a tougher trading environment it becomes more important. For four years we were owned by a VC and since then we have been owned by a US corporate. When we were VC-backed, it was daily cashflow forecasts, so we were really tight on the numbers every day. That was because you were managing an asset-backed loan and so on. But, with the US corporate, there was far more emphasis on quarterly earnings. So, as a consequence, you might not look at the cashflow impact down to the last detail of a decision although of course it will always be considered. Whether you're optimising short-term cashflow is not the determining factor because the rush from the gate is always to establish new trading centres and so on.

What about balancing the demands of time and cost? Is there a disparity there?

MH: First and foremost you need the product in the store otherwise you can't sell it, and your suppliers need to understand that. There are times when you may need to fly product to the UK to meet the deadline for a new product launch but because this is a very expensive form of supply it rarely happens; in the main product is sent via boat (Far East) or truck (Europe) which is the most cost efficient.



Is business intelligence software all it's cracked up to be? Do you think installing a new 'bells and whistles' system will help drive efficiencies in the financial supply chain?

MH: I think that's a load of rubbish, personally. By the time the vendors and consultants charged you a massive fee to set it up, it doesn't take away the risk involved as far as the factory burning down or currency fluctuations and so on. At the end of the day that's still your risk. Of course, systems can help with driving efficiencies in a steady state world where variables conform to the norm or fluctuations are mitigated with logarithms and such like, but it cannot mitigate local economic variable shifts in the country of manufacture, nor the grand forces of nature.

DB: I could talk for hours on this. But suffice to say, any package that you buy off the shelf or that has been developed for another business, will never suit the needs of your business exactly. The reality is you should get one that's the best fit and go in with your eyes open. That means assuming you'll have to spend money on development and



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customisation for it to properly help the business. So many people I talk to say, 'Oh that system doesn't do what we believed it would do'. But of course there may not be an inherent problem with it, it's just not designed specifically for you and that's the way software vendors work in providing packages for small and mid sized businesses. At the end of the day every business operates with different strategic priorities

driven by the stakeholders and, in the retail market, the personalities running different businesses will have their own ideas on what they want so you can't solve every problem instantly. So go in prepared to spend a bit of additional money to get what you want. It's very disappointing if you fail to get what you want post initial investment, so appreciate you'll need to spend more to optimise the benefits.



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What approach do you take to managing your suppliers?

NC: Obviously we try to have the best possible relationship with suppliers, and we try to bring them on board as partners to get the best product and the best price. So, to that end we have tried to encourage them to think of themselves as partners in the business and that means it works better for everyone.

We make sure we manage them correctly as far as payment terms go, but given the working capital position overall it's not something that we put first in the business plan. Of course, it's one of a number of things one has to consider when making sure you're running the business in the right way.

MH: We let the middleperson deal with the difficult stuff and insist that the penalties are quite stringent when orders are not met. That means that whatever cost to them, they make sure whatever the order is they fulfil it. Using this means we don't have a 'lumpy supply' since we let the middle person deal with it.

My current opinion is that I think, like lots of retailers of our size, we don't have the scale of volume to justify laying down the fixed cost either in the UK or the country of direct supply. We are currently undertaking a detailed exercise internally to understand if indeed this is the case.

DB: We don't manufacture anything ourselves but we do design everything, so we're managing a supply base as a bespoke design business. So, absolutely, that relationship is crucial to the success of the business.

What about letters of credit, are they a thing of the past?

DB: We have tried to build in extra flexibility to the supply chain by moving away from letters of credit to a large extent since they're fiddly and expensive and can cause problems with product delays, although for certain suppliers they work fine. So certain things we've done are after taking a step back to question whether they made sense. Is benchmarking useful?

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MH: Well to be honest, no one will tell you what their true costs are in the area of supply chain or payment terms so you can only go on industry benchmarks. Thankfully, when we make those comparisons, we're quite proficient, though of course there's always room for improvement.

Do you think collaborative financing has a future?

NC: We look at any new innovations as they emerge. But you need to be very cautious of the danger of window dressing – the business is straightforward, and we try to be innovative in our products as opposed to our financing arrangements. We don't have our heads in the sand and will consider things on their merits of course.

DB: In the end, it's about balance and making sure the supplier is not the most important thing to you and vice versa. It's being a big enough business to make a difference but not the be all and end all for the supplier. There's no doubt that we go out of our way to preserve our relationships with our suppliers, those who deliver consistent quality at a fair

price. The reality is all about the personal relationship you have with your suppliers.

Summary

It is clear from the comments here that the FSC still has a way to go to convince retailers of its value. But with more scrutiny being placed on corporate supply chains generally, the financial flows between buyer and supplier will inevitably come under the spotlight. Transaction costs in particular can be a serious drain on the bottom line in any businesses with high volume supplier contracts, so establishing a more efficient way of handling these can bring immediate benefits.

What is undeniable is that if applied correctly, extending finance to established suppliers could ensure a better deal for those on both sides of the transaction. It's likely that, as belts begin to tighten and cash becomes even more prized, blue chips and those below will be looking at anything to make the bumpy ride a little more comfortable. ■

Michael Hitchcock

Michael Hitchcock has been the finance director and an executive director on the board of Moss Bros Group plc since October 2006. He joined the company from UK-based book chain Ottakars plc (owned by HMV Group), where he was finance director. Hitchcock is a qualified chartered accountant.

Nick Candler

Nick Candler has been finance director of Pret a Manger since January 2006. Previously he was FD of Allied Domecq's business in the UK and Ireland and before that worked for Unilever, most recently in the US, as the FD of its culinary operation.

David Bateman

David Bateman is finance director and company secretary of Paperchase. Following the trade sale to Borders in 2004, he remained as FD and transitioned to CFO as Paperchase expanded internationally within the host store environment, especially in North America, and continued its UK growth.