RESPONDING TO THE CHALLENGE OF RISING INPUT PRICES
By Kerry Glynn

People driving SUVs are not the only ones worried about rising oil prices. Its impact is being felt throughout industry, and baking is no different. Add in spiralling costs for wheat and other raw materials, and protecting margins in our business is getting harder and harder. How can we respond to this challenge?

With oil close to the $US 100 per barrel mark, and likely to increase beyond that, many industries are starting to consider the impacts. Direct effects are being felt in key areas like transportation, while pressure is going on the packaging sector where petroleum is a key component in production.

The rapid and sustained oil price rise is also translating into higher costs for raw material production. These costs are already starting to be passed on to manufacturing bakers.

For baking in particular there is also the Australian wheat crisis brought on by prolonged drought conditions. Australia recently cut its official 2007/08 wheat crop forecast. Normally the world's second-largest wheat exporter, Australia’s Bureau of Agricultural and Resource Economics, slashed its October forecast for the wheat crop to 12.1 million tonnes. This latest estimate is down 46 per cent on an earlier June forecast for a 22.5 million tonne crop, and compares with normal wheat crops around 25 million tonnes.

Consequently wheat prices are reaching record levels. Prices surpassed a record $9 a bushel for the first time in September 2007 as a drought in Australia cut production, pushing global stockpiles toward a 26-year low.

Increased price competitiveness of ethanol produced from sugar-based feedstock is also reducing land area being sown into wheat. More feedstock diverted into ethanol also raises prices of other raw materials such as eggs and dairy produce.

For bakers these cost pressures continue to grow as competition gets more intense. Companies selling directly to consumers face intense competition from supermarkets and other high volume, low margin sellers. Those providing wholesale goods face immense pressure to absorb cost increases or lose market share.

How can bakers cope in this complex, competitive world where forces outside our control mean volatile input prices and severe margin pressure?

There are multiple ways to do this – reviewing and improving processes, investing in your brand, upskilling staff. But in a margin business like baking there is nothing better than achieving real efficiencies - looking at all those interrelated parts of your business and identifying where you can do more with less.

Simplicity is the key factor. Comprehensive, daily data as well as analysis of trends over time, make it simpler to achieve real efficiencies in inventory, production and sales.

Inventory is a high capital expense for any bakery and there is a significant risk in managing your stock of both ingredients and finished products.

If you can gather the right information there are several ways to improve inventory management. Being able to quickly and accurately compare actual versus theoretical usage of raw materials means you can determine the accuracy of recipes and wastage. Visibility to full purchase and usage history equips you with good data to negotiate hard with suppliers. Setting automated reorder levels based on defined on-hand levels, delivery lead times and future forecast or actual requirements ensures your inventory is as lean as possible.

Volatility in input costs can rapidly erode margins. Selling products near to or below cost is not sustainable. Being able to rapidly analyse ingredient cost changes relative to sales helps determine which products need attention. Discontinuing low margin products and introducing new higher margin products enables your business to respond to input price volatility.

Capturing information that enables you to identify inefficiencies in production processes is powerful. For example comparing yield at end of a production line (actual as measured) versus expected output (theoretical from recipes/inputs); recording and reporting of wastage in the production process; and having a clear view of stock on hand, orders to be filled and capacities of production lines to improve scheduling efficiency.

Better quality sales data enables you to match supply to demand more closely, achieving not just fewer returns (stales/buy-back) but also reducing the likelihood of shortages.

Key information includes forecasting based on previous order/usage history that flows into production planning, impact analysis based on sales history and 'what-if' planning, and being able to easily compare production costs to sales results.

Gaining a single, simple, integrated view of all the information involved in a typical baking operation is not easy. Many small to medium sized bakeries will be focused on computerizing their accounting and payroll, and then use tools like spreadsheets and manual systems to manage inventory, production and logistics.

While only larger manufacturers could previously afford integrated computer systems (enterprise resource planning or ERP systems), these kind of applications are now increasingly cost-effective for smaller organizations.

Integrated computer systems not only provide the information you need to improve efficiency, but deliver immediate cost gains in areas like administration, where data entry and invoicing requirements can be substantially reduced.

The challenge laid down by the growing oil crisis, and other factors like wheat price rises, is to work smarter not just harder. Some of those smarts come from the information at your fingertips that improves your control over your day to day operation. Selling that SUV may also be a clever move.

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