BACK ON TRACK

SupplyChain Review's 2013 Top 50 Supply Chains is notable for the companies back on the list after falling out last year. Anna Game-Lopata reports

The first thing to notice when you look at this year's Top 50 Supply Chains list is a sharp decline in the cashflow return on investment (CFROI) figures. In 2012, number 1 on the list, biotech Acrux, had a CFROI of 124.7 percent. This year, Wotif.com snatched back the top spot with 62 percent. This in itself was a 26.5 percent slide for the online business, which had a CFROI of 88.6 percent in second place last year.

CFROI AT A GLANCE

CFROI concept author, Dr John Gattorna says the idea is that those companies with large, growing cashflows are likely to invest these funds in competitive producing assets such as new IT and new DCs. "This in turn has a positive impact on the share price and market cap of the company," Gattorna explains.
"A high proportion of a firm's working capital is taken up in fixed assets such as factories and DCs and a similarly high proportion is in inventories. On that basis, if a firm is able to make wise investments to improve the productivity of its assets, much of which is in the supply chain, it can be inferred that it has a well-performing supply chain."

Certainly, Acrux may have been an aberration. Having made two landmark deals in the hundreds of millions in 2010 and 2011, the company this half reported its first negative profit after-tax since listing, a significant drop of 58 percent despite a 9 percent increase in revenue. Acrux argues extra 'one-off' tax payments were the cause, however, there's no doubt, cashflow is down as is equity. Clearly something is having its impact on supply chain.

International supply chain thought leader Dr John Gattorna, who developed the CFROI concept, observes an "inevitable, inexorable slowing down of the Australian economy" making things tougher for businesses, which he says will continue in 2013.

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"If you look at the range of the cashflow figures they're getting smaller, even for the top companies," Gattorna says.

Making allowances for Acrux, a downward fluctuating spiral can certainly be demonstrated, with CFROI at the top falling from 88 percent last year to 62 percent in 2013. In 2011, Wotif.com again the top company, achieved a CFROI of 64.8 percent down from 107 percent the previous year.

This should in no way diminish Wotif.com's remarkable achievement of securing one of the top two spots on the list for the last three years in a row. Carsales.com, the only other 'pure play' online business on the Top 50 list, should also be commended. It hasn't fallen below fifth position over the same period.

Top-performing retailers include JB Hi-Fi, Speciality Fashion Group and The Reject Shop. At number 11 two years ago, JB Hi-Fi fell to 46th in 2012. But this year the company has excelled, racing up to fourth on the list.

As predicted, Speciality Fashion has come back fighting from number 15 last year to fifth, while not quite returning to the prime position of second spot it held in 2011. Meanwhile The Reject Shop, number 16 in 2011, and off the list last year, has also soared ahead to number 8 with a respectable CFROI of 38.5 percent.

Given the difficulties of achieving free cashflow and then getting investments, operations, relationships and company culture right for a successful holistic supply chain, it's particularly fascinating to see who's reappeared after falling off the list last year.

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The likes of Woolworths, Wesfarmers, Coca-Cola Amatil and Caltex Australia are all working hard on supply chain management, the duopoly retailers in particular, locked in a competitive fight to the death. These companies have officially left Metcash, Goodman Fielder, Myer, Fosters, Harvey Norman and Ansell behind.

At 36th, David Jones isn't far off its 2011 position of 33, and ResMed, a business Gattorna points to as one to watch, is back in 38th position where it left off two years ago.

On the list since 2011, GUD Holdings regained some ground, jumping to 39 from 48th spot last year, but could not match its CFROI of 25.8 percent which had it in 23rd position two years ago. ARB, which made its debut last year, disappointed, falling from 18th position to 34th after an 8.6 percent drop in CFROI.

Resources companies followed a similar pattern to previous years with several new companies making their debut high on the list and companies with one or more previous appearances slipping down.

Giants fared poorly, with Rio Tinto's $3 billion loss one probable cause for its disappearance after clinging to 45th position last year. BHP Billiton suffered a 14 percent hit to CFROI which pushed it back to 35th, one spot above its 2011 position before the premature rise to 14th last year.

With all the right signs on paper, Troy Resources is a newcomer at number 3. It stole the rank from last year's debut in the position, Kingsrose Mining, which fell to 13. Gold explorer St Barbara and Oz Minerals were the only resources companies to improve, with St Barbara delivered to 12th position from 27th after achieving a strong 12.38 percent increase to CFROI and Oz Minerals climbing to 31 from 39th position last year, after a 4 percent CFROI gain. Saracean Mineral Holdings, Western Areas, Medusa Mining, Pan Aust, Silver Lake Resources and Roc Oil, all fell but remained on the list.

THE MATHS OF CFROI

CFROI=[(Cashflow from operations/capital employed) – capital charge], expressed as a percentage.
Capital employed = total assets – current liabilities [where capital charge represents the cost of capital when the weighted average cost of capital (WACC) concept is applied].
WACC is pertinent as decisions about how companies choose to fund their business reflects effective leadership; the key indicator for effective supply chain management.
Given differing management styles, a company's cost of debt and equity is not easy to specify. We therefore assign the proportion of the costs using an average figure, then calculate the difference by applying 'beta' which refers to the risk ratio of each company.
The full explanation of CFROI methodology is set out on pages 238-241 of *Dynamic Supply Chains*, by John Gattorna (FT Prentice Hall, Harlow, 2012).

Mincor Resources and Medusa Mining bucked the trend, returning to the list after falling out last year, the former now at 24th from number 9 in 2011, and the latter returning at 37th position from 35th two years ago.

Companies servicing the mining industry showed their mettle, though Leighton Holdings remained notable for its continuing absence since 2011. Monadelphous, though, pushed back one spot, held on to its ranking with the cream at number 6, a spot it hasn't slipped below in three years. On its heels in seventh position is competitor Forge Group after a healthy 17.36 percent increase in CFROI. NRW Holdings also did well, jumping from 37th position last year to 17th. Newcomer Sedgman, which at 58th wasn't far from a ranking last year, achieved a 11.25 percent improvement to CFROI placing it at 26.

Austin Engineering and Industrea, both of which debuted in 2012, dropped off this year, while Emeco dropped down from 38 to 44.

Stayers Cochlear, REA Group and Iress Marketing held their ground within the top 10, while New Zealand Telecom and Telstra both moved up the list within the top 25. Joining them was Fleetwood Corp at number 15, which came back after dropping to 35 last year, improving two spots on its 2011 rank of 17. CSL, consistent within the top 30 until now, slipped slightly to number 33.

Of the telecoms, I was surprised to see iiNet fall off the list, however, TPG Telecom made good ground, rising from 34th last year to 21 on the back of a 6.45 percent increase to CFROI.

Interesting newcomers include SMS Management and Oakton, not yet sweating Iress in software and services, Boart Longyear, Macquarie Atlas Roads and Tassal Group. It will be interesting to see how they go next year.