SO THE DIESEL PRICE IS COMING DOWN

With the diesel price coming down many customers will be expecting rate decreases. So how will you deal with this?

For many years there was a stable cost environment in New Zealand. With fuel cost increasing there was a need to increase prices to retain margin and profitability. This has put the onus on transport operators to negotiate an increase in transport pricing. Recently I spoke with one transport operator who is only now coming to terms with the effect of the increased fuel prices on margin. They felt by having a surcharge that they would be able to maintain their margin and profitability. This was not the case. What occurred was the surcharge only covered the fuel component and a number of other costs (that have a fuel component) were also rising. In a previous article I indicated the Commerce Commission had in my view done a favour to the transport operators by insisting that they incorporate the additional fuel cost in the rate rather than by way of surcharge which they deemed illegal. I believe my stand has been vindicated when I now see financial results of transport operators that have used the fuel surcharge and found their returns dramatically declining. My stand provoked some comment from a number of people who took issue with the surcharge and they had many reasons as to why they couldn't do it. My view remains the rate should incorporate fuel price increases.

What transport operators are now finding is customers are requesting a reduction in their rate because the fuel price has come down. However, the analysis done in a transport index indicates many other costs are rising and a transport operator needs to look at items line by line to see what their cost increases are and incorporate these in the rate charged. To just increase their transport charge by the amount of the fuel increase is insufficient to remain profitable with a reasonable margin in the longer term. I accept this is difficult but I repeat what I have said previously, in articles and publicly, that you need to have the skills to negotiate with your customer. I further accept that there are many operators who do not know their costs are severely impacting the long term profitability of businesses. I do not endorse inefficiency but it is necessary to adequately recover the costs to achieve a fair profit and remain within the legal requirements (and there are many for transport operators).

It is interesting to note my discussions with bankers and financiers indicate in their file reviews significantly reduced performance because of increased costs and an inability to increase their revenue. More files are going to the people in the bank who are responsible for under performing businesses. Banker and financiers interests are making sure they get their money back. My view is that it is necessary for the transport operator to get a reasonable return on their money and efforts. This takes a considerable effort and requires a great degree of working on rather than in the business. It also is very demanding where you need to increase the rate and the customer rejects the proposed new rate and threatens to get another carrier.

A further case study that I have recently observed is where rates have been 'cut to the bone' by a new transport operator who is now finding it very difficult to get the returns that are appropriate for the service demanded. The customer has high expectations on service delivery and a low expectation on price. This has damaged the business of the operator who thought greater volume would be attractive but has found the demands of the customer at a level where they are unable to deal with their regular customers on a satisfactory service basis and the higher margin work is deserting them. Whilst the strategy of taking on the additional work was on the basis of marginally priced work on top of their existing work they are finding the existing work disappearing because of the demands of the lower priced work. It isn't working for the transport operator and there is a real need to deal with the pricing issue before profitability (or lack of it) has a significant detrimental effect on the long term business future.

This is a new environment for transport operators (well it's been around a couple of years at least) and the need to have strong negotiating skills and the will to perhaps walk away from unprofitable work needs to be considered. In a further case study that I have seen the sales revenue of the business declined but the profitability improved when a low margin customer was exited. Initially it was a brave call but now the transport operator will not engage in doing work that ends up 'at a back load rate' and therefore puts at risk the ongoing sustainability of the business.

So the challenges with transport operators to be able to explain and negotiate a fair return that has an enduring rather than a short term business. I urge you all to contemplate how you will meet the challenges of customer requests, because the fuel price has gone down, to maintain a rate to maintain your profitability.

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