The Cost of Delay

The Impact of Delays in Decision-Making About Technology for Wholesale Distributors

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Introduction: Competing Priorities

Mid-sized businesses have to balance many priorities competing for their attention … and their working capital. This is especially challenging when their business is growing. When push comes to shove, it is not uncommon for them to postpone investment of many kinds, especially IT. In particular, moving onto a new ERP platform can look daunting. The investment and risks involved often dominate the thinking and decision process—rather than the benefits and returns.

Why is this? Small or mid-sized businesses often have minimal or no IT staff, limited working capital, and are naturally conservative about adopting new technology. It can be hard for them to imagine stepping up to adopt comprehensive, sophisticated systems. They are concerned about what it will really take in terms of time and staff, and especially in terms of disruption and change. They are also challenged by conflicting messages from solution providers on approaches—on premise vs. cloud vs. on demand and so on.

It does take time to evaluate functionality for enterprise systems that touch so many aspects of the business. Businesses need to validate for themselves that the return on investment is real. So, even when it makes a lot of sense and the expected ROI is compelling, the decision to make the leap into the digital age is delayed.

Ironically, for businesses such as wholesale distributors, they are already spending quite a bit more on inventory and operational inefficiencies than they would need to pay for the very systems that can dramatically reduce those same expenses. Lacking a modern ERP system, they are missing many opportunities—to reduce missed sales, minimize late shipments (and the associated expedited transportation expenses), to improve productivity and trim overtime costs due to poor organizational issues and insufficient or bad data. In short, they are missing the opportunity for transformation, using modern technology to dramatically increase speed while reducing errors, creating much better visibility into their business, and leapfrogging the competition in performance and new service offerings to customers.

As time goes on, these missed opportunities, inventory write-offs, and lower margins add up. This is the *high cost of delay*. Being conservative and thoughtful can be good qualities for a business leader. But when faced with compelling evidence and a well-worn path that others have successfully taken, continuing to postpone the leap to better enterprise systems creates enormous costs in lost opportunities and stifled growth.

Business can take from six months to several years to decide and actually implement a solution. During that delay, they can miss substantial benefits in savings, cash on hand, and new sales. To understand this more clearly, below we first look at the difference in cash flow and time-to-implement between a subscription-based SaaS system vs. a traditional perpetual license. Then we examine the typical range of benefits companies are achieving when they implement a modern SaaS system. Using that data, we look at two hypothetical companies and their 'cost of delay,' followed by a number of real-world examples. We conclude with some pointers on sources of delay and how to overcome them.

Return and Benefits from ERP SaaS Investments

Pay-as-You-Go (SaaS) vs. Upfront Lump Sum (Traditional On Premise)

First, let's examine the differences in cash investment timing for SaaS vs. on premise. Modern SaaS ERP systems are cloud, subscription-based (pay-as-you-go) systems that require only a fraction of the upfront capital costs to get started compared with traditional on premise systems. SaaS provides a capital-conserving economic model, reducing upfront cash outlay, shortening time-to-benefit and pay-back period, while providing the same or better economic rewards that traditional ERPs do.

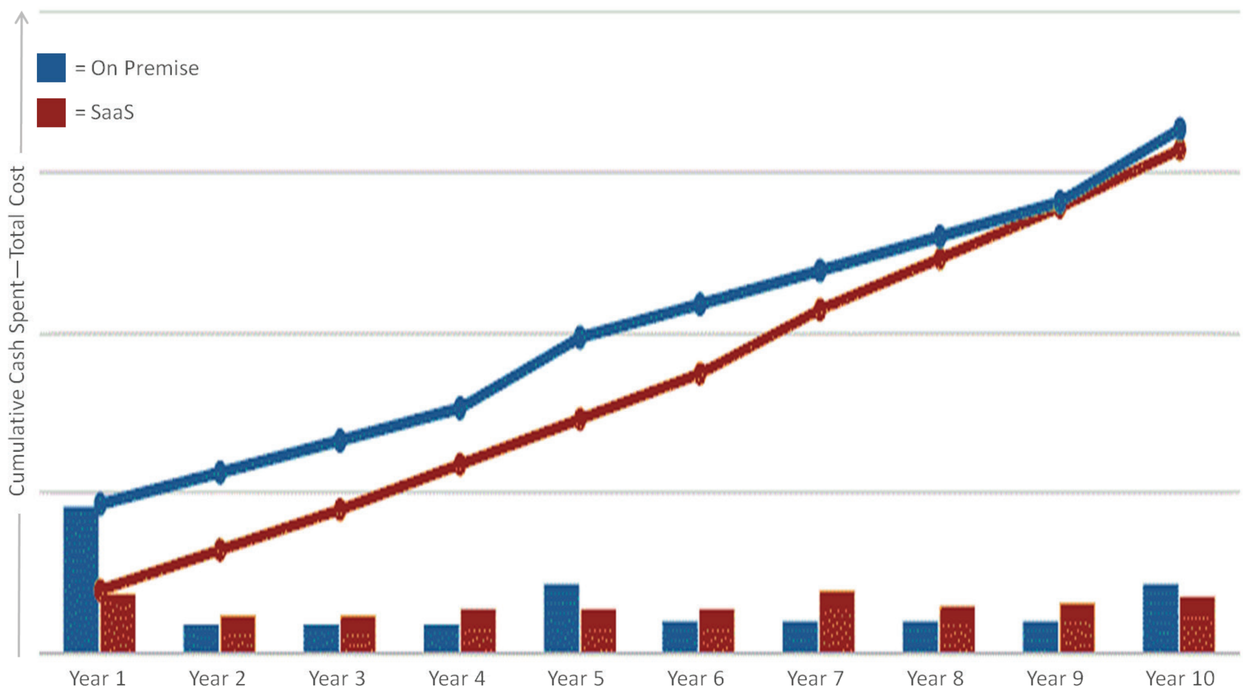

Figure 1 – Comparison of Typical Total Cost 10-year Cash Flow—On-Premise (Perpetual License) vs. SaaS[1]

Figure 1 shows a comparison of typical cumulative cash outlays for an on premise system (traditional perpetual license, the blue bars and lines) vs. a SaaS system (maroon). The upfront year one expenses required for an on premise system can be three to four times (or more) than for a SaaS system. This is not only a big drain on working capital, but it pushes out the ROI breakeven point, by months or years.

Working at the Speed of SaaS

Another advantage SaaS has is implementation time. For typical ERP implementations, studies have shown SaaS takes about 60% of the time to implement compared to an on premise system implementation. For small and medium business, the difference can be even greater, further accelerating ROI realization, achieving time-to-benefit many months sooner.

[1] The graph was created using Software Advice's online TCO calculator using the default assumptions.

Reaping the Rewards

Now let's look at typical benefits from these investments. Research shows that the financial benefits of implementing a SaaS ERP system can be substantial, as shown in Table 1 below.

KPI	Typical Improvements
Revenue	2% - 10%
Gross Margin	1% - 5%
Days Sales Outstanding	5% - 20%
Accounting Staff Productivity	30% - 50%
Inventory	20% - 30%
Obsolete Inventory	20% - 40%
IT Support Resource Costs	50% - 75%

Table 1 – Typical Improvements for Wholesale Distributors Who Implemented NetSuite[2]

Applying these benchmark percents to your own business, the benefits can be substantial.

The Cost of Delay

Delays in implementing a modern SaaS ERP system postpone the realization of these benefits. To visualize the magnitude of benefit being missed, let's imagine two notional wholesale distributors: *General National Wholesale Inc. (GNW)* with revenue of $200M and *Special Products Distributor (SPD)* with $30M in revenue.

GNW is a fairly typical mid-sized wholesale distributor with gross margins and inventory levels near industry averages and with typical sized accounting and IT staffs.[3] Here are some key metrics for *GNW* and the range of improvements they could expect by investing in a modern SaaS ERP system:

Metric	Typical Improvements	Current Performance	Annual Improvement Opportunity
Revenue	2% - 10%	$200M	$4M - $20M Sales
Gross Margin	1% - 5%	22%	$2M - $10M Profit
Days Sales Outstanding	5% - 20%	39 days	$1M - $4M Cash
Financial Staff Costs (per year)	30% - 50%	$1.5M	$0.4M- $0.7M Cost Reduction
Inventory	20% - 30%	38 days	$3M - $5M Cash
Obsolete Inventory	20% - 40%	3%	$0.4M - $0.8M Cash
IT Support Resource Costs (per year)	50% - 75%	$500K	$0.25 - $0.4M Cost Reduction

Table 2 – Annual Cost for GNW of Delay in Implementing NetSuite[4]

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[2] Source: *Research Study: Cloud-Based Business Solutions Suite Delivers Key Performance Improvements to Wholesale Distribution Companies*, SL Associates, 2014

[3] We selected Gross Margin, DSO, Inventory, and Obsolete Inventory levels for *GNW* based on averages for wholesale distributors from NAW's Wholesale and Distribution Industry Key Performance Indicators (KPIs). The finance staffing is based on averages according to Robert Half's 2014 Finance and Accounting Benchmarks, assuming $100K/FTE. IT support resources assume 1% of spend on IT / 25% of that IT spend is on IT support resources.

[4] Based on SL Associate's 2014 research study.

To put it another way, each month that *GNW* delays in making a decision and moving forward with implementing their new ERP system costs them $300K–$1.7M in sales and $200K–$900K in profit. As well, it delays freeing up of $5M–$10M in working capital and accelerating the cash-to-cash cycle time. Together these can make a huge difference in performance, competitiveness, and (in tougher times) even survival.

What about a smaller business like our hypothetical *SPD (Special Products Distributor)*? Being a specialty distributor, they have somewhat higher gross margins. However, as a small company that does not have many of the required disciplines and systems in place, their days sales outstanding and inventory numbers are well above industry average. Their financial and IT departments are modest sized—three people in finance and accounting, and one IT person. Here are *SPD's* numbers and improvement opportunities:

Metric	Typical Improvements	*SPD's* Current Performance	Annual Improvement Opportunity
Revenue	2% - 10%	$30M	$600K - $3M Sales
Gross Margin	1% - 5%	28%	$300K - $1.5M Profit
Days Sales Outstanding	5% - 20%	55 days	$230K - $900K Cash
Financial Staff Costs (per year)	30% - 50%	$300K	$90K- $150K Cost Reduction
Inventory	20% - 30%	66 days	$750K - $1.2M Cash
Obsolete Inventory	20% - 40%	9%	$100K - $200K Cash
IT Support Resource Costs (per year)	50% - 75%	$100K	$50K – $75K Cost Reduction

Table 3 – Annual Cost for SPD of Delay in Implementing NetSuite

Each month that *SPD* delays implementing a modern SaaS ERP costs them $50K–$250K in lost revenue and $40K–$150K in profits, while missing out on inventory reductions worth nearly $1M–$1.5M. As we can see, each month of delay is very costly. These missed opportunities add up fast. Figure 2 below shows the missed opportunities over time for *GNW (the $200M firm described in Table 2)*. This is based on them realizing average benefits, in the middle of the range show by the research, and it illustrates how these missed opportunities just keep increasing over time.

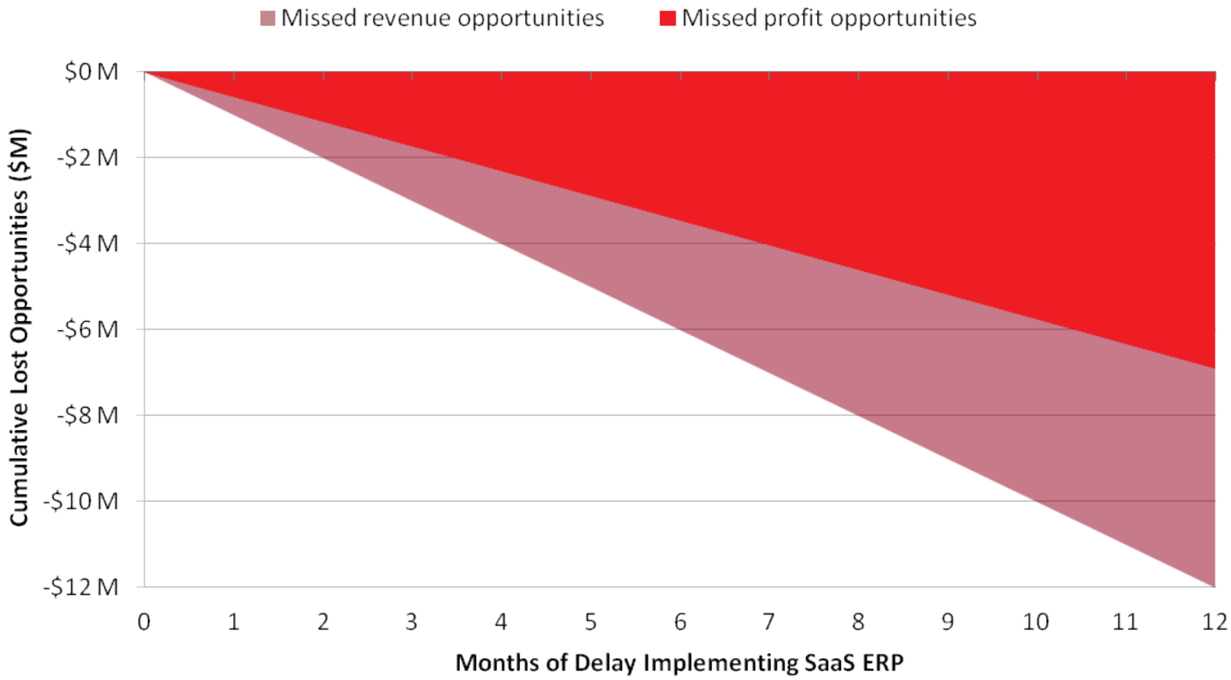

Figure 2 – Increasing Cost of Delay Over Time for $200M Wholesaled Distributor *GNW*

Real-World Cost Savings & Productivity Improvements from Implementing SaaS ERP

The longer the delay, the more cumulative benefits lost. Conversely, the earlier the decision is made, the greater the benefits. These benefits are not theoretical. Here are real-world examples of cost savings and improvements realized from implementing NetSuite:

- Advantage Sign Supply—Decreased inventory by 15% ($500K), cut order processing time by 2/3, saved $1,000/month in postal/mailing costs alone by electronic invoicing.
- Alpha Energy—Improved staff productivity by 20%, eliminated the cost of their onsite server.
- Carryboy—Productivity improved 50% with double-digit revenue growth.
- Corkcicle—Extreme efficiency and outsourcing enabled by NetSuite lets Corkcicle sell via 4,000+ partner locations, 40 countries, and achieve double-digit revenue growth with the barest minimum number of employees.
- EcoBox—POS transaction times reduced by 30%, orders shipped 50% faster.
- EndoChoice—Reduced paperwork 75%, saved one FTE,[5] increased sales efficiency 45%, while growing 65% over four years.
- Finis—Saved $140K annually in labor costs, reduced DSO from 50 to 32 days, increased warehouse efficiency 20%.

[5] FTE = Full Time Equivalent. One FTE is the workload of one full time employee.

- Honey Stinger—Grew at double-digit rates while avoiding the hiring of two additional FTEs in the warehouse, and nearly one FTE in order entry and transaction processing.
- Jetline—Doubled order entry capacity with the same staff while reducing order processing time by 63%.
- Lionel—Avoided the cost of five FTEs needed with its legacy AS/400 system. Reduced inventory while increasing model railroad sales by 118%.

This list is only the tip of the iceberg. There are countless other examples showing how implementing a modern system like NetSuite can improve performance and cut costs. Companies that continue to use outdated or manual systems are saddled with higher costs, excess inventory, and higher error rates.

Missing out on Growth Potential

It is not just about missed savings and cost reduction. Many companies' growth is constrained because they lack systems and processes that can scale with their business, and their inability to serve customers excellently. What is the consequence of shipping items late, shipping the wrong items, and not being able to respond to customer needs? If the item a customer wants is not available from you—or worse yet you tell them you will deliver, but can't—they will go to your competitors. More and more companies have upped their game, competition is fierce, and those who don't perform lose business. Furthermore, technology can help grow your business without increasing headcount. It is a growth accelerator.

Choosing a System That Can Go the Distance as You Grow

It is important to choose a platform that can scale with your business that you can grow with for a long time to come. In most cases, the system you were using when you were doing $1M in revenue will not take you to $100M … definitely not to $500M. For many companies, their system becomes a key constraint to their growth. A system like NetSuite has proven scalability. They have customers ranging from the smallest companies with under 10 employees all the way up to multi-billion dollar enterprises. This is especially critical for fast growing companies who want a system that can serve them now and for many years into the future.

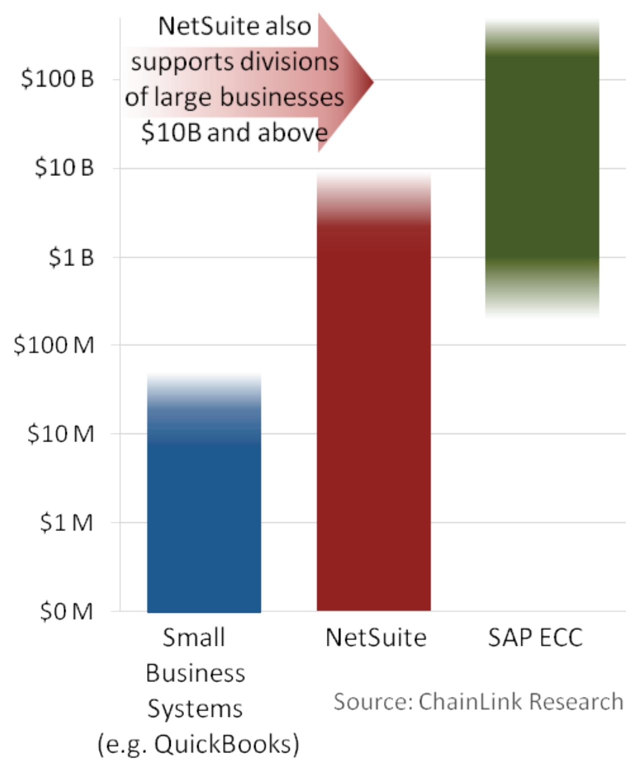

Figure 3 – Scalability of Different Systems

Here are some examples of distributors whose growth was enabled by implementing NetSuite:

- 2Pure—Increased revenue 95% without adding staff, while cutting warehouse space by 40%.
- BioPak—Grew 172% and doubled the number of daily orders, with no increase in staff.
- Capitol Coffee—10% CAGR over past four years with ecommerce growing from 5% to 30% of revenue.
- Free Flow Wines—Grew 300%/year for two years in a row after replacing QuickBooks, while avoiding the cost of adding 3+ FTEs that would have been needed during that growth period using its old systems.
- Hestra—50%/year growth over past five years since installing NetSuite, while saving $50K/year on IT costs and improving shipment accuracies to over 99%.

When a company's systems are a constraint on their growth, then the cost of delay in switching becomes intense. It is much better to move to a highly scalable platform *before* you run into the limitations of your existing approaches.

Rooting out Delay

For a business to go forward more quickly, it helps to understand the sources of delay. Adjustments can be made to a company's approach to evaluation, decision-making, and implementation in order to move things along in a timelier manner, so that the business can start reaping the rewards sooner. It often comes down to awareness, motivation, culture, and the impetus to change. Some organizations take a great deal of time before they realize they have a problem with their current system. Some are caught up in rapid growth and just don't have a *moment to breath*. Older businesses may be stuck in thinking '*this is the way we have always done it*.' Even after an organization realizes they need to find a better system, there can be further delays in starting a search, making a decision, and implementing it. In each case, the result is a delay in achieving better performance.

Figure 4 shows a typical timeline from realization of the need for a new system all the way through implementation and realization of the value from that system. It highlights potential sources of delay at each step, with some guidelines on how to address them:

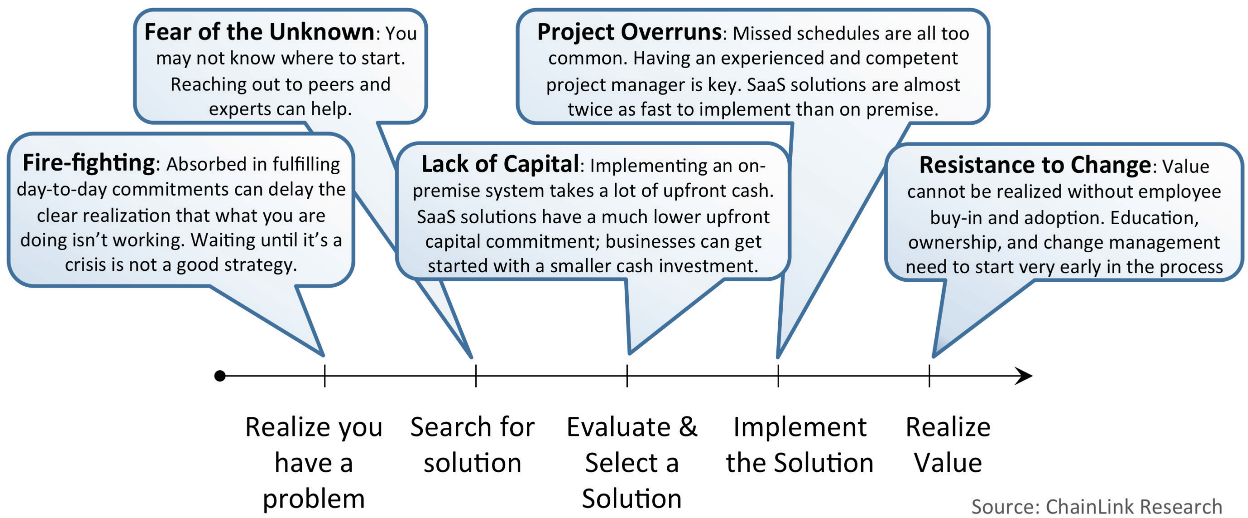

Figure 4 – Typical Sources of Delay

A little thoughtful introspection often helps organizations to honestly reflect on what their real issues are and creates the catalyst for change. Here are some tips on keeping the momentum:

- *Benchmark Yourself*—Having a hunch that your company could be doing better is not nearly as compelling as seeing hard numbers that show whether or not you are performing below average for your industry. This does not have to be a big drawn out exercise. With a modest amount of research, you can find out averages for your sector.[6] This can be useful also for setting concrete goals on exactly what benefits you would like to achieve and justifying the project to move it forward.
- *See What Your Peers Have Done*—At industry meetings or trade shows, you can find out what systems others in your industry have implemented, how long it took them, and what the results were. This can help you learn how value is being realized and steer you to look at those system investments that will give you the most bang for the buck.
- *Dedicate Resource(s) with Accountability*—Giving someone in your organization the time and responsibility to manage the decision process and move the ball forward can make a difference.
- *Bring in Outside Expertise*—Those who have done this many times before can greatly accelerate the whole process.
- *Ensure that Key Executives and Employees Buy In*—Changing management and alignment across your company will be critical. You know your own organizational dynamics, who are the key people who could derail the effort and need to be brought in early. Making sure everyone in the organization understands why change is happening and gets behind it is not a one-time effort, but a continual ongoing process.

[6] For example, NAW's report on Wholesale Distribution Industry KPIs includes metrics by sector.

Conclusion

When faced with investing in technology, a smart CEO wants a frank discussion about what the risks are. A smarter CEO also wants to understand the risks of *not* proceeding as well; the downside of continuing with business as usual. Fear of making these kinds of major decisions and financial commitments can cause business leaders to drag their feet. Sometimes business leaders think "*our current systems are working good enough*" and/or "*we can't afford a new system right now*." But when the current system is a barrier to growth, then really the business can't afford not to move to a better way. 'Good enough' is almost always *not good enough* in the face of increasing completion and low margins.

In today's fast moving world, the competitive bar is constantly being raised. What is good enough today won't be good enough next year … or even in a few months. Threats increasingly come from new competitors and sources outside traditional distribution (such as Amazon). The world is rapidly moving to newer technology-enabled business models, eliminating paper and manual processes. These new streamlined businesses are hyper-competitive, virtually eliminating errors while dramatically reducing cycle times across all their processes … and eliminating some no longer needed processes altogether. Those who are stuck in the old ways, who drag their feet and delay in stepping into this new world, will not be around for long. Now is the time to make your move!

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