



THE TIMES 100

McCain Foods brief

Introduction

McCain Foods is the world's largest maker of frozen chips. McCain makes around 45% of all frozen potato products sold in the UK. It is the clear market leader. This scale makes McCain a major user of energy. It has set up two projects to reduce the amount of energy it has to buy from energy companies. The two projects are a wind turbine system and a wastewater treatment plant. The projects aim to reduce costs. McCain has fixed costs like buildings and equipment that it must pay whatever amount it produces. It also has variable costs, like labour, that relate to the amount of goods produced. These projects will provide sources of renewable energy, so are more environmentally sound. The projects will also help to show McCain is committed to being socially responsible.

Investment

The projects cost £15 million. McCain needed to see if they made financial sense. To arrive at a figure for profit, McCain takes costs from sales revenue. This gives gross profit. Taking fixed costs from gross profit gives net profit. The cost of building and running the projects is cash flow out. The savings the projects may give is cash flow in. This can be set against cash flow out to see if the projects are worthwhile.

Investment appraisal

A business can choose whether to invest in one project or another or not at all. There are different ways to find out if a project is worthwhile. One of these is investment appraisal. There are a number of ways to do this, such as:

- Payback. This is a simple way to measure investment efficiency. It works out the time it takes for the set-up costs to be paid back through savings. The two projects both paid back in around 4 years.
- Average Rate of Return (ARR). This is more complicated. It shows the average return over the life of the project as a percentage of the set-up cost. This helps McCain to compare projects against each other.

Discounted cash flow (DCF)

Discounted cash flow takes into account the effect of time on an investment. This is how it works:

- £100 invested at 10% interest gives £110 in a year.
- Therefore £110 in a year's time is worth £100 today.
- Put another way, if you invest £90.90 today, you will receive £100 in a year's time.

This shows net present value (NPV). This helps to show what each project is worth in the future. It also shows that a rate of return depends on interest rates.

The Internal Rate of Return (IRR) is like DCF but more specific. This shows whether the value of a project is better than the return the company might get if, for example, the money was in the bank.

Investment for sustainability

McCain worked out that both projects were worthwhile. They also help the environment. The wind power project will reduce CO₂ and produce 60% of McCain's power needs. The wastewater lagoon will also provide power through the capture of methane gas.

Conclusion

McCain needs to know that it will get a good return on its investments. It can do this by working out rates of return. The two projects it has set up are not just to reduce costs. They also show McCain Foods' commitment to the environment.