



Estimated Order Row Holding Cost

By order row costs we refer to all cost associated with your procurement processes.

All from preparations, negotiation, arrange agreements to receiving of goods and invoicing. This is best done per supplier or at least on a group of suppliers with similar conditions. In SOLO the data is then entered and used per supplier.

There are two ways to establish relevant order row holding costs – average- and variable order row cost. They are both explained later on in this document.

Below you will find a couple of suggestions on activities that can be relevant in your estimation.

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|------------------------|---------------------|
| 1. Quotations | 8. Arrival control |
| 2. Negotiations | 9. Stocking |
| 3. Supplier selection | 10. Goods receipt |
| 4. Order monitoring | 11. Reports |
| 5. Relations | 12. Invoice Control |
| 6. External transports | 13. Payment |
| 7. Goods receiving | |

Costs for above mentioned activities is mainly personnel costs, general administrations and transports. Any blanket releases from an already existing contract will reduce costs for items 4-6 considerably and completely for items 1-3.

Estimation of Average Order Row Holding Cost

In this calculation both fixed and variable costs are included.

How to:

1. X - Calculate/estimate the total yearly ordering costs regarding purchase- and warehousing for the upcoming year.
2. Y - Estimate the total number of orders which will be placed during the upcoming year.
3. Z - Estimate the number of average order rows per order for the upcoming year.
4. Divide the sum of yearly order cost (X) with the estimated number of purchase orders (Y).
5. Divide the result (X/Y) by the average numbers of order rows (Z).

The obtained number represent the estimated order cost for next coming year and is crucial to SOLO and it forecast calculation. If no value is entered manually by you to the supplier, SOLO will lean on an average of a 100 SEK per standard.

Example:

X - Calculated/estimated total yearly ordering cost for purchasing and warehousing upcoming year = 1 283 000 SEK/year.

Y - Estimated total of orders placed during upcoming year = 4260

Z - Estimate number of order rows/order = 20

Result per order = $1\,283\,000 / 4260 = 301 \text{ SEK} / 20 = 15,5 \text{ SEK}$

If necessary, round up the result to make it applicable to SOLO.

Average Order Row Holding Cost = 15

Note that if fixed costs are included in above calculation the cost determined will be somewhat higher than supposedly, and as a result so will your tied up capital.

Estimation of Variable Order Row Holding Cost

A somewhat more refined way of estimating your order row holding cost could be to exclude the fixed costs and only let the variable costs be represented. If you in your finance system is able to separate the two (fixed and variable costs) earlier estimation can be used. If not – the below is recommended.

How to:

1. Calculate/estimate the total ordering costs regarding purchase- and warehousing for the upcoming year by using the activities mentioned earlier. Use the at least three previous years as benchmarking.
2. Estimate the number of purchase order during each of these years.
3. Mark the number of purchase orders (X-axis) as well as the total order row holding cost (Y-axis) on a chart as per below. Note – use one tick per each year which you used in your estimation.
4. Use a ruler to draw a line which as close as possible coincide with your marks on the chart. Where the line hits the Y axis indicates your fixed order row holding cost. See below example.
5. Reduce the earlier estimated total amount with the number generated via the chart. Now divide the remaining sum by the number of purchase order estimated for the upcoming year. The now obtained number should give you a fair appreciation of your fixed order row holding costs for the upcoming year.

Example

The total ordering costs regarding purchase- and warehousing for the last four years has been estimated to 1 283 000 SEK and the number of purchase orders during the same period of time to 2 260. These numbers has then been ticked in the chart per below in addition to the totals for each of the four years.

The chart displays the result of fixed holding cost to 550 000 SEK.

To further calculate the variable cost - $1\,283\,000\text{ SEK} - 550\,000\text{ SEK} = 733\,000\text{ SEK} / 2\,260 = 324\text{ SEK per order}$.

