

OXFORD CAMBRIDGE AND RSA EXAMINATIONS
Advanced Subsidiary GCE

BUSINESS STUDIES

Businesses, Their Objectives and Environment
CASE STUDY

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This case study consists of 4 printed pages.

McAvoy's Ltd – A Leap Into The Unknown?

The aquaculture industry in Scotland, of which salmon farming is a part, has developed significantly over the last thirty years. Salmon farming is mainly undertaken in the sea-lochs of the West Coast and the Orkney and Shetland Isles.

Multinational companies dominate the salmon farming industry in Scotland, whereas it is more usual to find small companies in the trout and shellfish industries. McAvoy's Ltd is, however, one of the few smaller UK companies. It has carved a niche market for itself by supplying organically farmed salmon and, with careful attention to customer needs, it has grown steadily since it was established in 1992. The co-founders (and majority shareholders) Jamie and Ben McAvoy were left a large area of land by their grandfather in his will. This valuable asset includes a sea-loch on the West Coast that McAvoy's Ltd now uses for farming. The brothers both have a strong interest in green issues and believe in an ethical approach to making money. Jamie, with a degree in marine biology and Ben, a mechanical engineering graduate, had suitable backgrounds for establishing the fish farm. They were able to raise the necessary finance to start the business relatively easily.

Although the demand for salmon has continued to rise over the past fifteen or so years, the competition has intensified considerably. Producers from Chile and Norway dominate world salmon farming. Chile in particular has a cost advantage that Scottish producers find hard to match. In addition, many Scottish farmers complain about the regulatory burden from the European Union which they say drives up costs. In recent years, many smaller Scottish salmon farmers have closed down or sold out to the multinationals.

The industry has had a number of environmental scares since it was established and controversy surrounds the way farms replicate the life cycle of the salmon. Environmentalists have two main concerns: the effect on wild salmon and the effect on the environment. They claim that stocks of wild salmon have been genetically polluted as a consequence of breeding with escaped farmed salmon. With regard to the environment itself, it is claimed that too many chemicals are used routinely as part of the farming process, and that salmon farming produces unnatural areas of concentrated waste – excreta from the fish and from uneaten fish food. These two factors, they say, combine to cause extensive damage to the environment.

Salmon farmers claim that genetic pollution of wild stocks is exaggerated. They also argue that as salmon require the highest water quality if they are to thrive, it is not in the farmers' interest to farm in any way that will be detrimental to this, or in any way that will damage the lochs' ecosystem. As for the use of chemicals, they point out that, as with any animal, there is sometimes a need for veterinary care involving the use of drugs.

As an organic producer, McAvoy's Ltd has, to some extent, been able to rise above this controversy but this does not mean that life is any easier for the firm. The Soil Association (which also has responsibility for this type of organic production) inspects farms regularly to ensure that its standards are upheld. Also, the West Coast is not always well served in terms of infrastructure, and the farm is quite isolated even though as part of its regional policy the government has designated much of this region of Scotland as a Development Area.

In addition to its isolated location, there are many factors that affect the success of the farm, not least the type of employee. "Don't join us if you want an easy life" is a favourite saying of Ben to prospective employees at interview. He is only half joking.

Those working on the farm may enjoy breathtaking scenery but often have to endure atrocious weather conditions. Employees have to be dedicated and physically tough. 50

As a result of organic production requirements, the individual fish are more expensive to produce than on an ordinary farm. The brothers, however, decided from the outset not to compete on price but on quality. There are clear benefits to the organic approach and this is most apparent in the premium price that McAvoy's Ltd can charge. The 'Scottishness' of the McAvoy's brand name that has been established has served them well and the brothers feel that the business has been a success. 55

However the Marketing Director, Angus Finlay, feels that the firm is, as he puts it, "at a crossroads". Quite a lot of equipment, especially the mechanised feeding equipment, is approaching the end of its useful life. Jamie wants to replace it with the latest technology. This would involve the installation of a computer controlled automatic food dispensing system linked to underwater video monitoring of existing food uneaten by the fish. 60

Angus has a more radical idea. As well as installing the new technology, he wants to expand the farm considerably. At the last Board meeting his view gave rise to a discussion of several issues. Angus spoke first. 65

"With regard to the proposal that I circulated to you all two weeks ago, you will see that the additional cost for expansion would not be that big if we are going to be replacing and upgrading anyway. We can buy some of the equipment in bulk and demand discounts from our suppliers. We'd need more cages and nets obviously..." 70

"And more tanks, pumps, filters, anti-predator fencing and a hundred and one other things," pointed out Ben. "It's all very well you having your dreams, but whatever you say it's going to cost a lot of money."

"That may not be too much of a problem actually," said Alison Potter, the Finance Director. "Our financial position is quite healthy. We've steadily been repaying our loan – its down to about £50,000 at present and..." 75

Angus interrupted her. "This is not a dream," he said hotly to Ben. "I've done some research. The market is there. Our distributors are constantly asking for more fish. We can't hope to compete in the low cost market but this is our chance to make it big." 80

"Is that what we want?" asked Jamie. "I'm sure I speak for us all when I say we're all grateful to you. You've created the brand name and built it into a symbol of quality. But what does 'make it big' mean? This expansion is on a scale that's never been our objective."

"To my mind, our present objective of 'sustained growth' is much too vague," said Angus. "We need to be much more specific and clear. As I said in my proposal this is our chance to do that. And in answer to your question, by 'make it big' I mean really grow – not plod along. I know it'll take time to increase capacity, but let's aim for a growth in sales of 5% per year from 2007. Our profits should increase considerably." 90

“Hang on!” replied Jamie. “This is changing the whole nature of what we are trying to achieve. When I started this business with Ben I did it to provide us with steady work and because organic farming is something I believe in. I’ve never made any secret of the fact that I’d like to make some money by selling my shares when I retire, although that’s years off yet. I for one never considered our objective as striving for an ever-greater profit. We may not be millionaires but I’m reasonably happy and I don’t want any more stress!” 95

“I hear what you say,” said Angus. “But just bear with me for a moment. As I said, I’ve done some preliminary research and some calculations. I’m happy to accept they are a bit rough and ready but I can easily submit a formal analysis if we decide to go any further. I reckon that including the upgrading, the increased capacity, the staff training, and the extra sales promotion we would only be talking about a capital cost of £400,000.” 100

“Only £400,000!” spluttered Jamie.

“You want to ask yourself just exactly what this company is trying to achieve, Jamie,” 105 said Angus. “Come on, this growth would benefit everyone, and we’d still be doing what we’ve always been doing. It doesn’t change anything – it isn’t a leap into the unknown.”