



▶ CUTTING COSTS TO KEEP VALUE

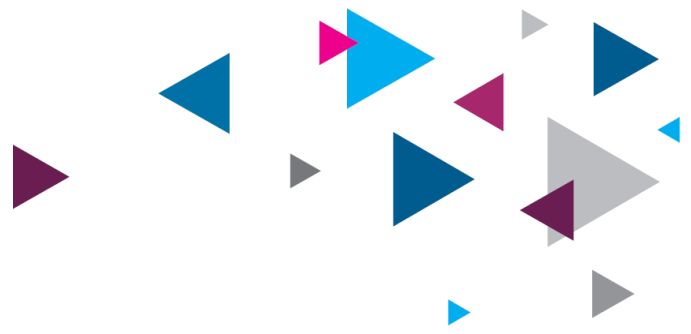
By Andy Way, Baringa Partners

Economic news makes for grim reading these days, and we have entered a new era of corporate austerity. Cost-cutting has become a major focus and belts are being tightened across the board.

For those charged with slashing expenditure it is tempting to simply rush around rationing the stationery, instituting redundancies and slashing the IT order. But perspective is essential and it must be value, not price, that provides the impetus for any successful reduction in costs. You need a long-term strategy that accounts for the implications of cuts on the overall health of the business, and it's the low-value areas that must be

addressed as a priority, not necessarily the high-cost ones.

There's a logical set of steps to follow, from low-ticket budget items all the way through the potential restructuring programmes. So instead of jumping straight in, it pays to take a more measured approach and start at the shallow end.



Step One

It's easy to dismiss the seemingly small change – that tied up in discretionary spend. But a taxi fare here and a client lunch there soon add up. In fact, travel and entertainment (T&E) expenses are estimated to be a company's second largest controllable outgoing after salaries, and there is often some room for tightening up.

Then you can consider your uncommitted spend. Do you really need to replace your current estate of desktop PCs this year? Is there headcount budget that you have not used up?

But if you sacrifice planned hardware upgrades or new hires, will it cost you in the long term by compromising your ability to deliver? Or will it constitute a valuable saving? These questions need to be answered before slicing the allocated budget.

Step Two

'Tidying' up small change items is relatively straightforward, and should yield some useful savings. But it is unlikely to reduce the overall spend by more than five to ten per cent. The next stage may be harder, but offers greater opportunities. For this, you will need to coordinate with various department heads across the organisation.

First of all, talk to HR. Many organisations play host to long-established fiefdoms and management layers that can mask inefficiency. Similarly, old accepted processes are not necessarily the most effective, given the current team and tasks at hand. It may well be possible to consolidate entire areas to reduce management overheads. However, savings in staff costs can be a tricky one. They tend to be handled centrally and often don't pay back within the financial year when redundancy payments are taken into account.

A good place to start is to establish the staff activities that are valued most highly by customers. Prioritise these, and you may find you can redeploy and redesign services accordingly. Depending on business growth objectives and projected deliverables, it might be

appropriate to adopt a policy of staff attrition and a hiring freeze.

But whatever the outcome of your deliberations it is important to remember that all decisions must be taken with an eye to the future. Short-term gains lose their value if made at the expense of the organisation's medium to long-term stability and this applies to HR as much as any other business area. The economic upturn will come, and when it does, your business must be in a position to capitalise on it.

Procurement can also deliver major savings. Under scrutiny, many organisations discover that they have a supplier base that is large and unwieldy – and spreads their purchasing power too thinly to allow for any quantity discounts and significant savings. By consolidating deals and taking the long term view you ensure that economies of scale can be negotiated. You also become a key customer, leading to improved service levels, which increase value while reducing cost.

Again, the lowest cost option is not necessarily future-proof. Vendors who make cheap initial offers know how to boost their profits by adding essential extras, such as service and support, throughout the life of the contract. For any long-term purchase, be it goods or services, you should always look at the total cost of ownership. The costs associated with any amendments to systems or services you may need to match changes in your business are all too often overlooked. So it's vital to assess cost and value over the expected life of the system or service contract to make savings of real value.

You should also talk to the finance teams. There may be scope to look at certain asset classes and revise the policy – although this will require buy-in from all key stakeholders. Alternatively, it's worth looking at whether older or missing assets could be written off to a restructuring fund to allow a lower charge to come through in future years. Consider too the capitalisation policy; could more be done here? Of course with all of these actions the effects will be long term – there may well be a knock on impact in the following years. It might be that you can spread reduction costs across the years to come.



Step Three

Avoiding major projects or cutting back on existing programme commitments may seem like a quick route to significant reward. But it's important to take into account the underlying resources tied up on project work, and what the mid- to long-term effects will be. Take a measured view on which resources are delivering the least value for money and consider reining those in instead.

Even in the current climate, there remain projects that can improve the efficiency, viability and profitability of your business, to give you a smoother passage through the turbulent waters – as long as you are prepared to look beyond the next quarter.

A transformation project, ie a review of what and how your area delivers its service through the development of a target operating model, with supporting people, process and technology, can offer a valuable insight into the structure of the business. This in turn will arm you with the necessary information to achieve sustained cuts while keeping in line with longer-term business objectives.

Offshoring is also traditionally used to reduce costs, but actually often carries with it the benefit of improved service. Similarly, outsourcing may be a key cost-cutting tool but it too often has the knock-on effect of improving both service and support. Thirdly, shared service centres, used to centralise and standardise processes tend to combine lower cost with improved service. All are worth consideration.

These projects can all help to realise significant savings, but may also require wholesale restructuring of the business. 'Going it alone' for big projects like these can prove a false economy; you are likely to need specialist expertise to guide you through the process efficiently. Investing wisely here will almost certainly lead to long-term savings.

If an organisation is to conduct a cost-cutting exercise effectively, while ensuring that it doesn't starve itself of future potential, a long-term view is essential. You need a realistic and flexible plan that looks equally at cost and value. Oscar Wilde once described a cynic as one who knew the price of everything and the value of nothing. This is no time for cynicism.

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