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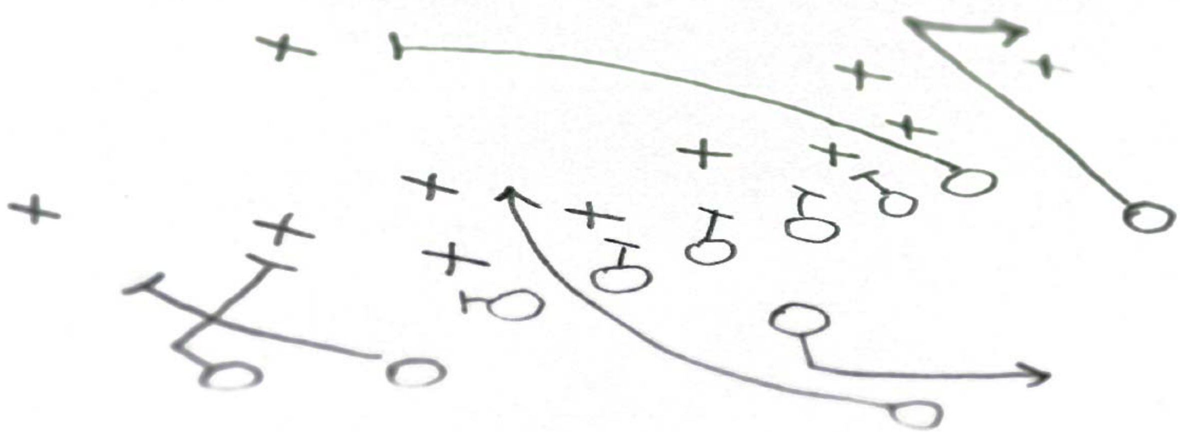
Playing to win

Ten ideas to survive the economic downturn and position for the future



A thoughtful approach to enterprise cost management helps companies cut expenditures without sacrificing the future

Only a few months ago, many assumed the Canadian economy would be insulated from the impact of the global recession. Commodity prices had softened, but remained high by historical standards. Canadian banks, almost uniquely among Western economies, emerged from the U.S. mortgage crisis with balance sheets intact. And the Federal government was forecasting a balanced budget. But as the economic crisis has widened, it has become clear that no country – and no company – has been spared.

Given the guarded yet optimistic outlook that prevailed in the closing months of 2008, perhaps it's unsurprising that many Canadian companies were caught off guard by the downturn's speed and impact. In fact, according to a Q1 2009 survey conducted by Deloitte, nearly 50 percent admit they underestimated the severity of the downturn when developing their 2009 plans and budgets. Now, companies across Canada are scrambling to reduce their costs and protect their margins. A full 80 percent of survey respondents indicated they have initiated formal enterprise cost management programs for 2009. But in the rush to slash spending, many are applying short-sighted approaches that could limit near-term savings and undermine competitiveness in the long term. Here are ten practical tips to help companies reduce costs more effectively and position themselves to capitalize on the recovery:

1. Understand the magnitude of your issue

Most of the surveyed executives know they initially underestimated the scale of the current downturn. It appears almost as many are now underestimating the scale of the fix. Half of all survey respondents are pursuing cost reduction targets of less than 5 percent, a laudable enough goal in a growth year, but not ambitious enough to preserve profits in the face of near-unprecedented revenue erosion. That's why the first task in enterprise cost management is to know the size of the potential budget shortfall. Knowing how tightly costs must be squeezed makes it easier to define the cost reduction program and approach.

> "Despite very conservative budgets, we are not even meeting the most pessimistic forecast"
>
> survey respondent

2. Start with the obvious

Structural cost reduction is never easy, so it makes getting the obvious stuff right even more important. The vast majority of survey respondents reported a focus on improving operations and reducing discretionary expenses such as travel & entertainment and training. They are also reducing headcount and deferring non-essential capital projects. On the external cost front, Sourcing & Procurement groups need to deliver a big year for their companies, aggressively recouping price conceded during the commodity bull run and holding the line on indirect costs.

3. Lead from the top

When executives were asked who in their company is responsible for enterprise cost management, the answers were all over the map. That's a problem. In times like these, senior executives need to take ownership of cost reduction. Only the C-suite has the clout to drive cost reduction across the enterprise, as well as the strategic perspective to make the right cost trade-offs without sacrificing the company's future.

> "Every company understands the imperative to quickly take out costs to survive the downturn. However, most companies are thinking far too tactically."
>
> Jim Kilpatrick, Deloitte

4. Take an enterprise view

Many of the biggest savings opportunities cut across organizational silos, which is why it's important to take an enterprise view to cost reduction. This should not be confused with straight across-the-board budget cuts, however, which harm the leanest parts of the business as much as they streamline the less efficient areas. Rather, an enterprise approach to cost management involves a broad-based assessment and prioritization of savings opportunities. Find the big opportunities, wherever they exist in the organization – then go after them.

5. Focus on the major cost drivers

Identify the levers that have the biggest impact on your cost structure, and then focus your effort there. Also look for opportunities to convert fixed costs to variable costs where possible. Consider centralizing selected activities to a shared services center, or outsourcing non-core functions. Consider pruning your product and service portfolio and reducing complexity in your business. These types of moves can help reduce your short-term costs while giving you the flexibility to respond to unexpected changes in the future.

6. Challenge your business model

The structural elements of enterprise cost are difficult to overhaul quickly. However a formal enterprise cost reduction program should prompt the kind of introspection needed to address elements of cost embedded in your business model – or even change your business model altogether. For example, you may challenge your supply chain network which was designed to meet the needs of the past – not the needs of the present and future. Short of that, you may decide, for example, to consolidate SG&A across business units. Either way, effective enterprise cost reduction demands asking the big questions about your embedded cost structure – indeed your entire business model.

7. Protect strategic investments

In the rush to cut costs companies often sacrifice long-term strategy on the altar of quarterly cost-reduction. Although the immediate pressure to reduce costs can be intense, long term investments in areas such as in R&D and marketing are the seed corn for tomorrow's revenue. And targeted investments in your supply chain can be the key to emerging from the recession with competitive costs and a customer service advantage over those companies that simply hunkered down. Vigorously guard against cuts to strategic investments that could harm your business tomorrow.

8. Focus on the short run AND the long run

When the need arises, enterprise cost reduction must necessarily be implemented with urgency. However, don't push off opportunities to make changes that can have a significant impact in the longer term for the sake of expediency. In times of crisis, the imperative to change is clear and this may be the time to make some of the bolder changes that you may have otherwise put off.

Cost improvement levers

	Cost improvement levers	Description	% saving*
Tactical improvements	**Spend reduction and demand management**	Focuses on strategic sourcing, demand management, and tax management to aggressively reduce external spend	10 – 20%
	Business process redesign	Focus on streamlining business processes via simplification, elimination, or outsourcing	5 – 10%
	Infrastructure rationalization	Focus on IT and real estate portfolios, projects, platforms, and support rationalization	15 – 25%
	Service Delivery model and organization alignment	Focus on re-aligning staff based on method of adding value and relationship to business	10 – 30%
Strategic structural improvements	**Business model redesign**	Shift to a more cost-efficient business model	20 – 30%

*Relative savings estimates based on Deloitte experience

9. Hold managers accountable

When it comes to reducing costs, actions speak much louder than words. To convert strategies and plans into actual savings, the C-suite guiding the program needs to assign clear responsibility -- and then hold people personally accountable for achieving the company's goals. In this downturn, CxOs who are serious about cost reduction meet face-to-face with their lieutenants on a daily or weekly basis and ask detailed questions so they know exactly what's going on.

10. Engage your people

Maintaining employee engagement and creativity is always essential, but pay special attention during a downturn. Hiring freezes and layoffs can sap morale when companies need productivity to be highest. Maintaining employee engagement requires open communication and a deliberate effort to maintain morale. It may also require a focused investment in training to help employees expand their skills. On the plus side, a downturn provides an opportunity to acquire new talent that might not have been available otherwise.

It's been said that a crisis is a terrible thing to waste. Although no one enjoys managing in a deep recession, in some ways the downturn can be viewed as a prime opportunity to boost efficiency and implement structural cost improvements that may be long overdue. Companies that make the right moves to reduce costs now will not only survive the crisis, they will improve their long-term competitiveness and position themselves for success when the economy bounces back.

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