

Deloitte.

Consulting

Sustainable cost reduction

A measured approach to long term value

Changing your tune



Audit • Tax • Consulting • Corporate Finance •

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Radically restructuring your costs

‘Death by 1000 cuts...’

Cost reduction is still high on the Boardroom agenda, but are companies still battle weary from repeated rounds of annual cost cutting? Have their programmes resulted in better service to customers and competitive advantage from a more strategic view of cost restructuring? Or have they fallen into the trap of ‘death by 1000 cuts’?

Looking at costs across the organisation

We believe that for cost reduction to be successful an approach is needed that radically restructures costs, and requires an organisation to think about doing business in a fundamentally different way.

Our cost reduction approach looks at Sales, General and Administration (SG&A), Cost of Goods Sold (COGS) or the whole enterprise and identifies short and long term efficiencies that improve an organisation’s competitiveness and leave it more fit for purpose whilst improving the customer’s experience.

Key facts from our recent survey

- Over three quarters of firms had undertaken a major cost reduction programme in the last 18 months.
- Of these 65% had conducted more than one cost reduction programme and 51% had conducted three or more.
- One in three companies employed both tactical and strategic changes in their cost reduction programmes.
- 17% of firms embedded a culture of continuous cost improvement.

The full report can be downloaded from www.deloitte.co.uk/soundadvice

Realising benefits

People within organisations are not short of ideas to reduce cost but often struggle to implement them successfully. A robust project management approach is important to drive the results.

Balancing the need to realise quick wins can often be at the expense of implementing longer-term solutions. We found that only 5% of organisations in our survey implement both strategic **and** tactical solutions. Our experience would suggest that approximately 30% – 40% of total cost savings will come from strategic initiatives and those companies that only focus on the short term are not likely to reach their desired target.

Creating an efficient low-cost organisation with a competitive advantage in the market place is about implementing a balance of tactical and strategic change with short-term actions that deliver long-term results.

Making cost saving sustainable

A key theme in our survey was that nearly two-thirds of organisations contacted had conducted one or more major cost reduction programme over the last 18 months, yet only 17% took measures to embed a culture of continuous cost improvement. The involvement of the business is a key success factor in not only shaping and implementing cost savings but also instilling an ethos of cost control and management that is ongoing. The drive for efficiency needs to be part of everyday managerial life – not just in the second half of the year when revenue forecasts have been missed!

Driven from the top

The CEO plays a key role in setting out the agenda for cost reduction in their organisation, both in terms of setting the initial objective and being the driving force behind getting the job done. This is one of the main success or failure points in any cost reduction programme.

Bringing these elements together into a cost reduction programme enables sustainable cost savings to be delivered.

Figure 1. Delivering sustainable cost savings



Creating business value

What are the fundamentals around creating business value?

Shareholder value creation is the ultimate goal of the enterprise.

Companies create value in the competitor marketplace by formulating and executing a number of 'operational strategies' including, productivity improvement and process re-engineering.

A balanced approach to cost reduction to deliver long-term sustainable results will involve reviewing a broad range of areas and solutions. Often, however, this is not the case leading to repeated efforts at reducing costs.

“One in five attribute positive share price impact to their cost reduction programme.”

Our Enterprise Value Map™

The Value Map is a structured framework applied to examine the organisation from a shareholder value perspective. It helps an organisation answer critical questions.

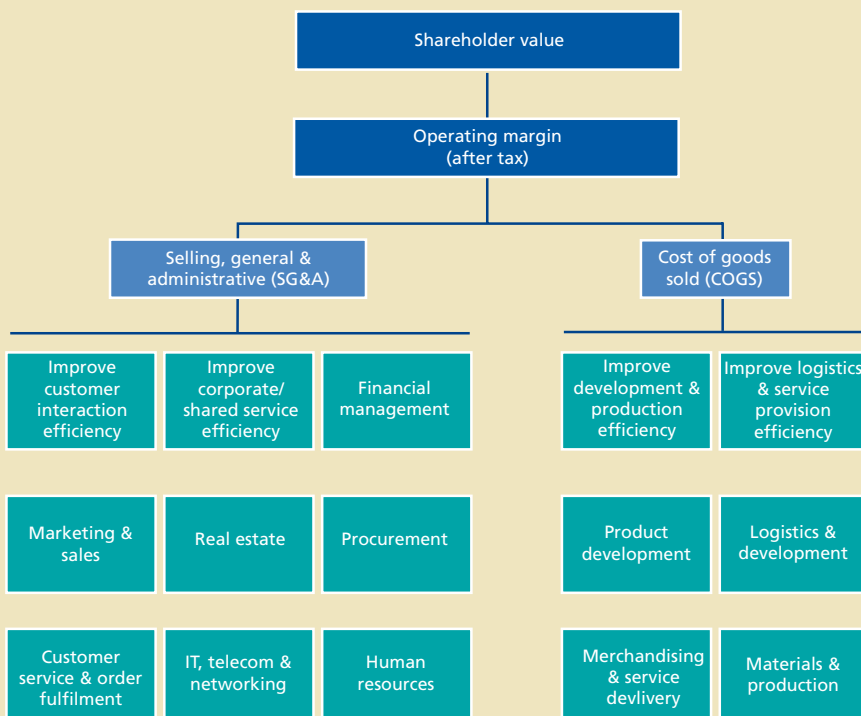
As highlighted in figure 2, the focus on SG&A looks at all the overhead and central costs and identifies a number of key levers and comparative data in order to identify tangible cost saving initiatives. These can range from budgetary control, procurement efficiencies, process re-design, organisational change, strategic partnerships, offshoring and outsourcing.

The review of COGS often looks at the key areas of supply chain efficiency, R&D spend and return, product rationalisation, cost of raw materials and cost of distribution main success or failure points in any cost reduction programme.

Results from our survey suggest a high focus on delivering cost savings rather than fundamental change.

- 93% achieved financial savings.
- 57% achieved major process improvements.
- 49% achieved major organisational change.
- 37% improved customer satisfaction.

Figure 2. A sub-section from our Enterprise Value Map



Case study

After a large financial services organisation announced to the City that it would significantly reduce operating costs, it asked Deloitte to help ensure the programme delivered results.

We helped the organisation to establish baseline operating financials and cost reduction targets to measure results against, and address savings opportunities across IT, Customer Services, Procurement, HR, Property, Finance, Marketing, Sales (Business to Business and Intermediary), and Risk & Compliance. Deloitte also led the Programme Management Office, which coordinated work across the organisation and reported weekly to the CEO and the Board.

Results were achieved in every business unit, including:

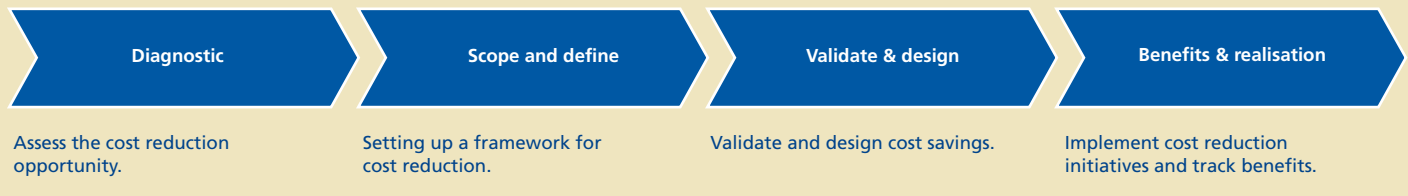
IT – over £100m savings in year 1, plus £105m in recurring savings were achieved, e.g. by adopting robust supplier management, leaner organisation structures, and more efficient use of external consultancies, contractors, and application infrastructure.

Procurement – £25m in tactical and strategic opportunities were realised, including e-Auctions and e-Sourcing to deliver a World Class Procurement Strategy.

Customer services transformation – £32m was saved by defining a new operating model for Customer Services and improving service with all calls answered by a human voice.

It's all about successful implementation

Deloitte's approach to delivering sustainable cost savings



Cost reduction involves large-scale, complex programmes, and requires skill in understanding how to execute. In our experience, there are a number of key reasons why cost cutting programmes fail to deliver:

- Too many 'holy grails', which block you from addressing the real inefficiencies.
- Taking the easy option with budget cuts (even though they have had mixed results in the past).
- Lack of senior executive engagement and internal politics.
- Not looking at fundamental changes to the business model.
- Not putting customer and customer processes at the forefront of thinking.

Many organisations have wide ranging ideas of how to reduce costs and have made continued attempts at executing cost reduction programmes. However, this repetition is hugely disruptive, inefficient and causes frustration among CEOs as they do not see these programmes manifest in reductions in expenses in the P&L.

“Despite all our cost reduction efforts the expense line in the monthly accounts is still not reducing.”

Deloitte has a robust approach to delivering sustainable cost savings. We work with clients to structure and deliver a cost reduction programme and we have the tools and methods needed to implement this successfully.

In our recent survey, key success factors for a successful ECR project are:

- Strategic commitment to reducing costs.
- Board and senior management buy-in.
- Communication, energy and drive to implement the plan.
- Committing to the programme.
- Change in culture regarding organisation's approach to cost.
- Accountability for delivering the result.

Key success factors

1. Set a clear target and align accountability to it.
2. Senior executive sponsorship and buy-in from the outset.
3. Robust project management approach to drive the programme.
4. Include tactical and strategic cost saving initiatives.
5. Engage and involve the business functions and finance in designing and delivering cost savings.
6. Embed a culture of continuous cost management improvement.



Why Deloitte?

Deloitte has wide ranging experience of developing and implementing complex cost reduction programmes on behalf of companies in a number of markets:

- Profitable corporates.
- Distressed businesses.
- Merger and acquisition transactions.

We have a very strong track record in a number of industries – Financial Services, Telecoms, Health care, Media, Consumer Business and Manufacturing.

Our cost reduction practice in the US, EMEA and APA gives us the capability to deliver cross-border solutions to multi-national clients.

We work with clients to help them design and deploy their programmes quickly and efficiently whilst mitigating project risks.

We provide an external perspective and challenge which helps executives and managers steer their cost reduction programmes through the problems and barriers encountered in delivering initiatives of this nature.

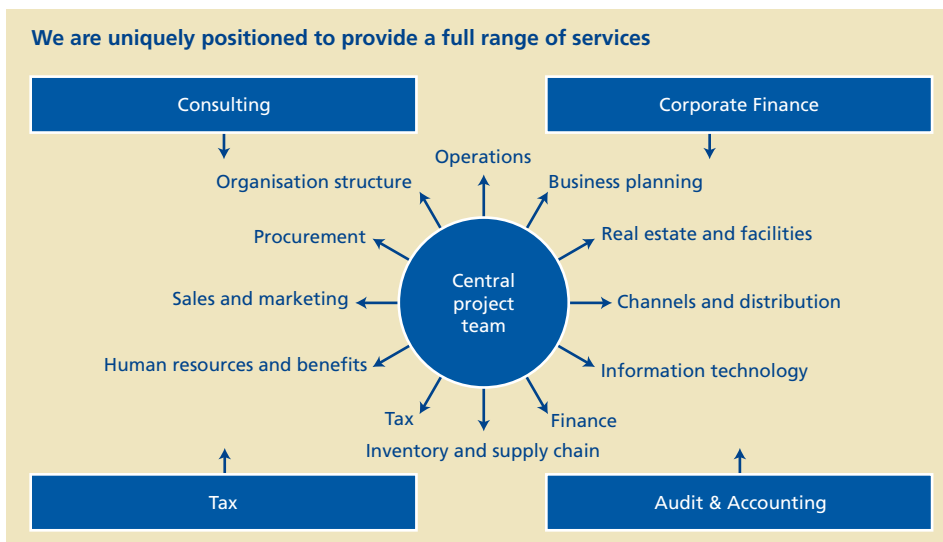
Our functional expertise – from real estate, supply chain, procurement, sales and marketing, human resources to tax – means we deploy an full range of services in a robust methodologies to ensure delivery of a holistic and sustainable programme.

Case study

One such example is work carried out for the Department for Transport (DfT) and its associated agencies. Deloitte was originally invited to carry out a review of all the back office functions of the department, including its IT function, HR, finance, real estate and procurement processes. The aim was to determine how the DfT could best meet its cost reduction targets. Following this review, Deloitte recommended the implementation of a shared services programme for the HR and finance functions of the department. This would involve a consolidation and sharing of services between the department and its family of agencies to help achieve cost savings worth millions of pounds.

“Implementing shared services is a significant challenge for the department. However, if we are to be fit for the future and deliver the services our customers expect at an acceptable cost to the taxpayer then it is a step change we simply have to make.”

Stephen Hickey,
Department for Transport.



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Key factors for successful cost reduction

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