

Rapid and Sustained Cost Management



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The Winning Edge in Uncertain Times

Improving Performance
through Rapid and Sustained
Cost Management

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Taking advantage of a downturn

How do successful companies achieve high performance during times of economic turmoil?

This question is uppermost in the minds of business leaders today. The realities of volatile capital markets and a struggling global economy confront management decision making at every turn. In recent years the challenges around managing costs have multiplied: relentless competition, increased earnings expectations, complex global operations, regulatory compliance, efficiency imperatives, proliferating risks and the sheer speed of change. Now, in addition to those challenges, companies are experiencing incredible economic turbulence. Commodities costs are soaring, banks are failing, credit is unavailable, stock markets are plummeting, net worth and home prices are tumbling and consumers are cutting their spending. All of these challenges are putting enormous pressure on businesses in all industries. Still, as every company knows, shareholders expect high performance in all weather, no matter how tumultuous or turbulent the economic storm.

In uncertain times, organizations have two fundamental choices: to hunker down or strengthen their strategic position. Which is the winning strategy? Accenture's ongoing research into High Performance Business and our experience in working with clients have yielded important insights into how high performers distinguish themselves. Among our findings in studying more than 6,000 companies: high-performance businesses act decisively at all times. They are realistic about the pressures of today and optimistic about the opportunities of tomorrow, which enables them to outperform their peers in revenue growth,

profitability, cash flow and total return to shareholders. And these businesses sustain and increase that superiority over time.

Does this hold true even in a slowdown? Absolutely, and to get a closer look at how leading companies managed their businesses during the last downturn, Accenture analyzed the financial results of 850 companies in the United States that experienced the recession of 1990-1991¹. Based on Return on Invested Capital (ROIC), we separated them into three categories: winners—those that outperformed their industry for six years following the recession; losers—those that underperformed their industry; and average performers—those that ended up in the middle.

What did we find? Winners took the bolder path. While attentive to current cost structure, they kept their eye on the prize: building sustainable

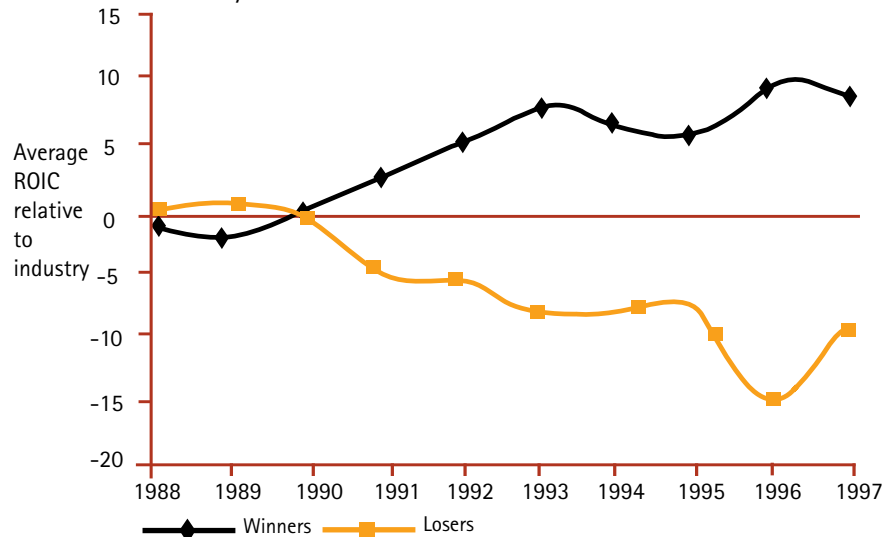
future value for the company and its shareholders. In essence the winners pursued an "and" strategy, not an "either/or" direction. They looked to strengthen their strategic positions and they also practiced rapid and sustained cost management (RSCM) in areas of their business where their costs were not competitive.

These industry leaders invested to strengthen existing positions and take market share, often trading off a low ROIC in the early years for a high ROIC later; see Figure 1. Strategies included acquisitions, forays into new markets, organic growth in adjacent markets, business unit divestments and new product lines.

¹ Jane Linder and Brian McCarthy, "When Good Management Shows: Creating Value in an Uncertain Economy" Accenture Management Consulting Research Report, August 2008.

Figure 1: Performance comparison following the 1990 - 1991 recession

"Winners" Pull Away After Recession



Winners are those that outperformed others in their industry for the six years following the recession of 1990-1991; losers are those that under-performed others in the industry

At the same time they used RSCM to provide cash for value-building opportunities. Winning organizations did not randomly hack away at the typical expenses such as travel, training, marketing and "across the board" arbitrary headcount reductions. They made sure they understood the strategic impact and sustainability of their cost-optimizing actions. The result: a company well positioned to achieve high performance by dramatically outpacing the competition when the economy stabilized.

The winners' strategy

The wisdom of the winners' strategy from 1990-1991 still holds true today. In the uncertain economy businesses currently face, cost reduction and cash flow generation are a front-and-center issue for every global business leader. That inescapable fact makes RSCM more critical than ever for companies determined to succeed during and after this economic slowdown.

True to its name, RSCM carries out cost reductions that aim to be optimal and sustainable for the company. RSCM does that by reducing costs diagnostically through an end-to-end process-driven approach—addressing identified cost drivers, with the goal of optimizing the cost-value relationship and minimizing negative impacts to the growth of the business as a whole.

RSCM creates value by generating incremental cash. Based on organizational priorities, this cash can then be

used to solidify existing positions and fund new directions. Through RSCM, the organization can become leaner and simpler; its vision and roadmap, sharper. The company's investment risk profile can also improve, making it more attractive to lenders and shareholders.

RSCM implementation roadmaps are situational. Initiatives may vary from attacking excessive consumption and rationalizing roles to reducing wage and procurement rates, working capital improvements, eliminating cross-functional redundancies and optimizing the cost-value relationship. Roadmap decisions are based on multiple factors: probability of success, timing of benefits, ease of implementation and the potential for margin and cash flow improvement, to name a few. They must also make sense strategically.

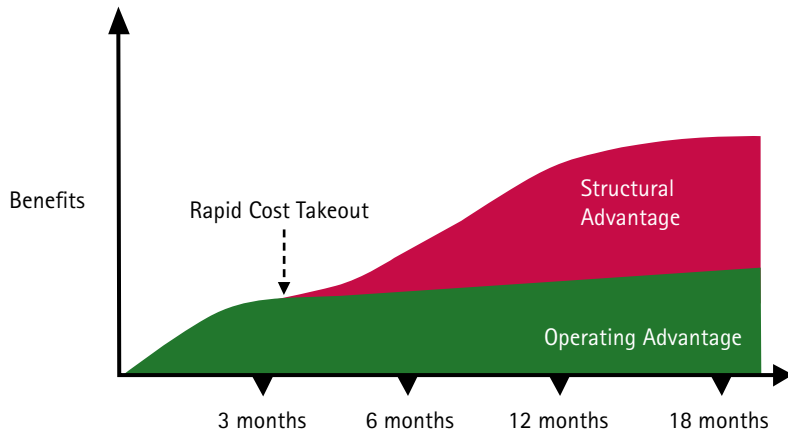
As an example, Accenture worked with a large high-tech equipment

manufacturer to reduce the complexity of its sales operations from lead to order. By conducting a segmentation of past opportunities based on size and complexity Accenture was able to develop a "deal factory" solution that reduced cycle time by more than 50 percent for small simple deals. The deal factory was staffed by lower-cost resources with strong telesales skills. By rationalizing the roles and making sure that the right people were focused on the right tasks the deal factory eliminated a large number of administrative and small deal tracking activities from the field sales force thus giving them back one day per week to sell. Giving back a day a week to the sales force was critical because it enabled the company to start focusing its field sales force on growth in a new market. In this way costs were reduced without sacrificing the ability to grow the business. This is one example of how Accenture helped deliver high performance through RSCM.

Rapid & Sustained Cost Management: a dual focus

Using RSCM, Accenture's approach is to focus on two kinds of initiatives: those that drive operating advantage and those that drive structural advantage; see Figure 2.

Figure 2: Rapid and Sustained Cost Management



Operating advantage: Initiatives drive operating advantage by rationalizing, simplifying and automating current operating capabilities to drive margin and cash flow improvements. Gaining operating advantage is about identifying opportunities for quick wins as well as reviewing processes from the customer to the back office of the organization to optimize costs within the current operating structure. This analysis should be based on whether or not each step within that process adds value to the customer and to the organization as a whole.

Structural advantage: Initiatives drive structural advantage by determining the right portfolio of businesses, capital structure, organizational structure and geographic presence that support the sustained efficiency and long-term growth of the business. Gaining structural advantage is about a systematic and analytic approach to increase the efficiency of managing the most significant assets of the business such as capital, property, plant and equipment and people.

Operating advantage and structural advantage are inextricably related to each other. Together, they generate the cash flow and credibility with the investment community needed to fund growth initiatives. Operating advantage looks at the current state of the business and asks, what can we do better, faster and cheaper while maintaining or improving our customer service? Structural advantage looks beyond the current state of the business and asks, what is happening internally and externally and how does it affect our current business model? Looking forward, it asks, what could this business be tomorrow and are we structured appropriately to achieve these goals?

RSCM analyzes the tradeoff between these two dimensions of competitive advantage. Here is a closer look at how each works.

Building Operating Advantage

How does our company operate today—and how do we leverage our capabilities? How do we rapidly take out costs without inhibiting our ability to pursue growth opportunities? How do we improve efficiency, margins and cash flow while maintaining customer service levels? End-to-end process-driven analysis of activities from the customer back through the operation is the way to create operating advantage. All too often companies cut the wrong costs for short-term gain, when instead reductions should be based on data and analytical evidence that keeps the company's sustained success uppermost on the cost-control agenda.

Where logical, decreasing headcount may also be a part of the solution. However, a focus on reducing high levels of cost primarily through headcount cuts may produce unintended consequences. Figure 3 demonstrates what happened to a small sample of 20 companies we analyzed who announced significant headcount reductions (average reduction for these 20 companies was 8 percent of their total workforce). Over a period of 5 years their total return to shareholders was only 37 percent compared to the S&P 500 return of 90 percent.

Taking a process-driven approach to identify the costs is the key to success. Cost-reduction and working capital initiatives that drive operating advantage are intended to confront current cost and cash flow pressures. This approach enables a company to reduce the costs that often hide in redundant activities, manual hand offs and rework that occurs between functions. Key processes to consider are lead to cash (sales operations), procure to pay (procurement to accounts payable), hire to retire (all the processes that treat the employee as a customer of the business), plan to manage (strategic planning to

budgeting to managing the performance of the business). Other potential initiatives that can drive high performance for the business are product portfolio rationalization, span of control optimization, global resource and site location rationalization, and marketing spend optimization.

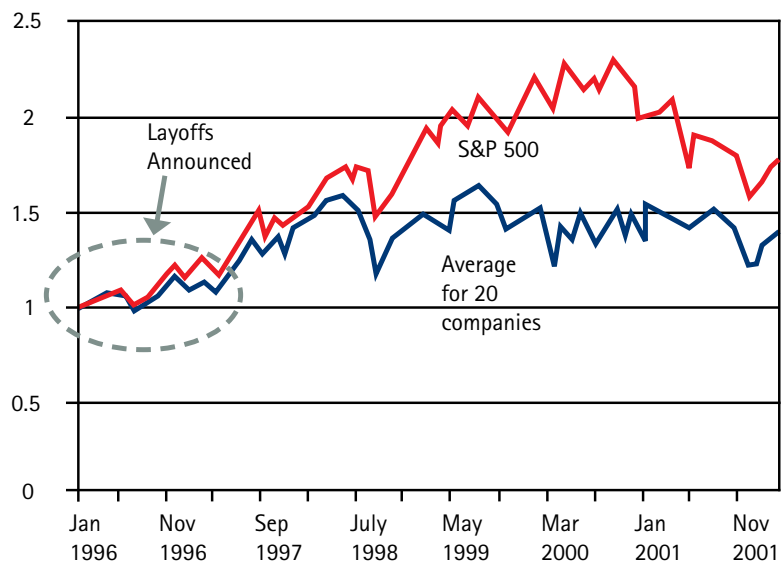
How it is done makes all the difference. RSCM is not unilateral cost reduction. It does indeed reduce costs, but not at the price of enterprise strength. Take marketing for example. Analyzing the pool of marketing spend through the lens of RSCM would include a look at advertising effectiveness. Breaking down that spend into TV advertising vs. radio, newspaper or collateral materials, a return-on-investment analysis becomes the basis of where to cut or reallocate that cut. It may even determine targeted spending increases at the cost of another less beneficial investment.

As an example, Accenture worked with a large global consumer goods manufacturer to reduce its warranty costs that were averaging 12 percent of revenue. By gaining a deep understanding of warranty cost drivers and

end-to-end processes, we were able to work together with the company to make changes in its business rules and operating model. The result: a 50 percent cost reduction with no decline in customer satisfaction. Likewise in supply chain dynamics, we collaborated on a broad cost-reduction initiative with a large U.S. drug retailer. As part of that effort, we identified fragmentation and breakdowns in the indirect procurement sourcing process that resulted in a less-than-optimized supplier network. Through Accenture's sourcing skills and experience, we were able to produce \$60+ million in savings in less than a year for this retailer. As a matter of fact, in our experience Accenture can in many situations help our clients achieve savings of around 10 percent, and in some cases more, off their baseline indirect procurement costs.

Figure 3: A focus on reducing costs primarily through headcount reduction can produce a short-term boost but not necessarily long-term value.

Total Return to Shareholders
1996-2001



Identified 20 companies that announced significant job cuts in 1996-1997 time frame

Source: Bloomberg, Accenture analysis, Mercer Commentary, ProQuest Database of Wall Street Journal
Note: Average # of lay offs was 5,200 at an average of 8% of total workforce

Building structural advantage

Winning companies see beyond today and toward the future state of the business. They look around corners and position the business for the transformational opportunities of the future. These strategic initiatives can be more difficult to execute but they can also be the key to high performance for the business. Structural advantage is driven by efficiently managing the assets of the business.

There are four pillars of structural advantage:

- Capital structure
- Organizational structure
- Geographic presence
- Portfolio of businesses

To gain structural advantage, companies should assess and rationalize their portfolio of assets. Based on that analysis, they should consider changing the structure of the business if appropriate for the organization. Actions might include financial restructuring to improve debt to equity ratios, organizational consolidation and restructuring to improve agility, reconfiguring physical assets based on a global resource and site location strategy and acquiring or divesting businesses to reshape the portfolio of businesses for the future. Structural initiatives are intended to reduce the cost and complexity of the business operating model, drive long-term profitable growth and demonstrate multiyear expectations to the market.

As an example, Accenture worked with a high-tech equipment manufacturer to identify a 30 percent cost reduction in real estate costs. The savings were driven by developing a global resource and site location strategy, which included extensive use of flexible office space for an increasingly mobile workforce and the alignment and consolidation of the efforts of each corporate

function to use shared services out of low-cost locations so as to eliminate duplication of effort and redundant locations.

Accenture collaborates with many clients to pursue structural advantage. For instance, offshoring takes non-strategic processes performed by headquarters or business units and moves them offshore for lower costs and greater economies of scale. In addition, it's no secret that a sound acquisition strategy during a downturn can result in purchasing strategic assets well below market value. Accenture teams with its clients to contribute valuable insights for the client when it is considering target markets and potential acquisitions. Running an onshore/offshore strategy team, Accenture is helping a communications client execute its acquisition strategy as part of their broader overall growth plan. Just like operating advantage initiatives, savings from structural advantage initiatives can also be used to help fund those acquisitions and drive greater synergies for the business.

Back in the late 1990s a large retail client experienced a 50 percent decline in earnings before interest and tax (EBIT) and share price, its competitors were considering a takeover and its focus was on survival. During this crucial time, the retailer teamed with Accenture on a number of initiatives aimed at optimizing key capabilities and continually improving business performance. The results were dramatic as same store sales increased by more than 15 percent and market capitalization more than doubled. Good for the customer—good for the bottom line. By 2004, the retailer had become the leader in its market. For high-performance businesses the drive to stay ahead of the pack is never ending. Not content to rest on its success, the retailer teamed again with Accenture to

continue its transformation to an even more customer-focused enterprise while also achieving additional cost savings. Initiatives included IT and business process outsourcing, supply chain optimization, improved analytics and reporting, enhanced functionality and performance of websites, and the support of international and new business model expansions. Many of these initiatives already have achieved intended cost savings and value. This is one of many examples of our ability to deliver high performance for our clients.

RSCM is a dual effort, with operating advantage and structural advantage mutually important in building the sustained value of the company. That dual approach is a part of what makes the Accenture difference.

The Accenture difference

With deep industry knowledge and functional experience, our people know where to look for improvement and can hit the ground running on day one. Unlike pure strategy firms, we are experienced implementers. We don't just leave our clients with insights and instructions and expect them to implement on their own. This comprehensive approach allows us to help clients identify and execute realistic opportunities that can contribute to driving long-term shareholder value.

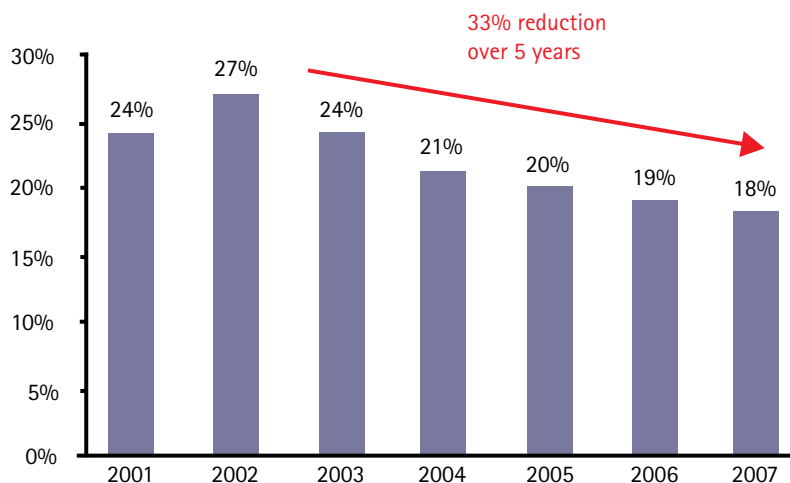
We've collaborated with 94 of the Fortune Global 100, more than two-thirds of the Fortune Global 500 and major government agencies around the world. Our consultants serve our clients' functional and organizational needs across all industries and geographies. Accenture also has more than 40 outsourcing centers and 625 outsourcing clients worldwide. With focus on high

performance, we leverage critical lessons gathered from hundreds of cost transformation, merger and acquisition, outsourcing and other integration engagements. And we can leverage our extensive ready-to-go proprietary tools and assets.

At Accenture, we work with you to achieve measurable results. Cost reductions for our clients can in many situations be around 10 percent (and often times more) across all industries.

We also follow our own advice. In reviewing our own operating and structural costs, Accenture leveraged the RSCM methodology to strategically drive down SG&A costs by 33 percent over a five-year period. See Figure 4 for year-by-year results.

Figure 4: Accenture's SG&A % of Revenue



Why do it now

The economic environment is turbulent and profit margins and cash flow are under intense pressure. RSCM is a roadmap to help companies navigate that turbulence. The destination: helping the organization to gain greater value for shareholders today and tomorrow. Getting there requires a focus on high performance. RSCM is one vital way Accenture can help your company achieve success. In the pursuit of high performance, every angle of gain, every push forward, every advantageous idea helps sharpen the company's competitive edge—and RSCM is one of those ideas.

The wisdom the winners demonstrated in the last slowdown still holds true today. Organizations can leverage that wisdom to drive success in the changing world to come. What will tomorrow look like? Wouldn't it be nice to know that answer? But one thing we do know is that being successful tomorrow means being optimal today.

It is not enough to survive today; we can help your organization on the journey to high performance. If you'd like to talk about how Accenture can help your organization improve performance, please contact us at fpm.service.line@accenture.com or 312-737-8290.



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