

# Cost Reduction Report

Cost Reduction & Profit Improvement for Increased Profitability

## ***A White Paper***

By

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# **BUSINESS SOLUTIONS**

**THE POSITIVE WAY**

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### **Cost Reduction Report**

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## 1. Summary:

Updating this in 2015, I see that the acid test of the 2008 recession has proven these tactics and principles to hold true. Companies have used them successfully and are in much better shape as a result.

This paper lists the top 5 cost reduction tactics used during the 2008 global recession and ensuring troubled economy. It expounds on the top 3 current challenges – some of which have been created by those tactics. Suggestions are offered for overcoming and even taking advantage of these challenges. Additional resources include 22 additional cost reduction and profit improvement ideas from real businesses. These demonstrate a cross section of ideas to act as examples.

The paper provides perspective and offers both tactical and strategic suggestions for cost reduction and profit improvement.

## 2. The top five recession Cost Reduction tactics:

Although the 2008 recession is technically over, parts of the economy have not yet recovered. These are still very difficult times for many employers and employees alike and the effects are anticipated to linger into 2015 and beyond for some industries. As revenues fell and cash flow dwindled in 2008/09 companies of all sizes grabbed the control levers on every major expense in an attempt to stay afloat.

Many businesses have applied more than one of these five most commonly used tactics.

1. Reduce discretionary spending (e.g. travel and entertainment, overhead, information technology spending, etc.)
2. Freeze and/or reduce compensation (e.g. wages, salaries, bonuses, retirement contributions, insurances, etc.)
3. Layoff employees
4. Delay and/or cancel capital expenditures and/or investments
5. Cut spending on marketing, sales & product development (research and development, advertising, travel, promotion materials & events, etc.)

This list is an example of the classic top-down approach to cost cutting. Top executives pick a dollar number to cut, look at the major cost categories and direct their managers down the line to make across the board cuts to hit their number. The selection criteria include: will it cut enough cost, can it be done quickly enough and can we survive the cut? The selection criteria rarely include: will we be better off in the long term if we make this short term cut?

Emergency cutbacks are useful for cutting cash outflow but unless you have made structural changes to the way your business actually operates, these are not sustainable. The downsides of this approach can be significant. Results are often less than expected and most of these tactics will not result in sustainable cost reduction.

History shows that a significant proportion of companies that cut their costs in a downturn by cutting headcount find that their costs are actually higher after the downturn than before.

Best in class companies engage in strategic cost reduction and profit improvement before a downturn and change the way they do business to become even more efficient when business is bad. These companies also use the downturn to gain a competitive advantage and are well-positioned to grow profitably when the economy improves.

### **3. The top three current challenges:**

The current challenges are driven both by the economy and the consequential impact of the top five cost reduction tactics. You may see your own business here to some extent and certainly some of your competitors are facing some of these challenges.

Businesses now find themselves in a catch-22 situation with a driving need to increase revenues as the markets recover but lack the human and technical resources necessary to drive and support those revenues. If we had the people to make the sales we would have the cash flow to support those sales...and so it goes. Which comes first?

#### **1. Inadequate resources:**

- a. Across-the-board cuts were made in the interest of survival or hitting a profit and loss target rather than in the interest of efficiency. Productivity may be up for some business units but, in all too many cases, this is neither sustainable nor efficient.
- b. Understaffed and under-funded departments may be getting by for the time being but are inadequate to drive growth.
- c. Budgets, staffing and plans for longer range projects in marketing, technology, infrastructure and the like were slashed to the bone. They are not only inadequate to return to pre-cut levels without significant investments in money but also in time. The momentum has been lost. Knowledge has been lost; some of it forever and much will require additional time to recreate.

#### **2. Need to increase profitable revenues:**

- a. Market share may have taken second place when markets contracted but with the recovery the challenge becomes one of either retaining or growing market share.
- b. Revenues drive cash flow and now that companies have survived, the focus can return to cash flow to support growth and profits to increase shareholder value.
- c. Competition is increasing in more and more business segments as weaker businesses fail, new competitors enter the market and stronger ones become even more aggressive.
- d. Traditional sources of capital (lenders and investors) are still tight which makes it even more important to have profitable revenues.

### **3. Loss of momentum:**

- a. After a long hiatus nothing can pick up immediately where it left off. In the simplest of cases it takes time just to bring people back up to speed. In many cases, however, the team has been disbanded and it may be very difficult to rebuild.
- b. Retraining staff takes time...months to years.
- c. Time is running out. Delayed projects may now be obsolete. At the very least, their return on investment has changed as the competition and substitute products have moved ahead.
- d. Cuts to marketing and sales budgets means a loss of market presence that will have to be rebuilt over time.

### **4. Opportunities with the three challenges:**

The good news is that your competitors are facing these same challenges and this is your opportunity to move ahead.

Here are some opportunities for each of the three challenges:

1. Optimizing resources:
  - a. Start with a blank piece of paper and streamlining your key business processes based on what you have learned by running with such short staffing, new technologies and new best practices. Prioritize carefully to include some early wins that are worthy of celebration by line staff and not just the accountants.
  - b. Re-prioritize the work. Apply resources where and when appropriate. Do not make the mistake of relying on prior assumptions. The world has changed.

- c. Identify and eliminate waste of all Seven Vital Resources: time, people, space, energy, knowledge, financial and material.
  - d. Engage your people throughout the business in a formalized continuous improvement program.
  - e. Train your people in the concepts and tools of efficiency. Now listen to them and act positively. Plan for the next business cycle now.
2. Increasing profitable revenues:
- a. Continue the process of analyzing revenue streams to find those that are the most and least profitable. Capitalize on the most profitable and fix or fire those that are the least profitable.
  - b. Make good acquisitions. Buy businesses and product lines. Every industry segment is seeing consolidation to some degree.
  - c. Market and sell aggressively with rifle shot precision into market segments that have been disrupted by industry consolidation and change. Take advantage of customer confusion and help them choose you when their historical supplier or alternative supplier is gone. "We are still here and we will take care of you by..."
  - d. Reevaluate the market to find new revenue streams. Markets have undergone change; some have undergone drastic shifts.
3. Regaining momentum:
- a. Reconnect with your workforce. This may be difficult but it must be done. Deal with the disruptions your staff has been through. Listen carefully to what your team is saying and observe how they are feeling. It can take a lot to overcome the stress of layoffs as they tend to lead to a loss of trust. Take action with a well considered recovery plan rather than letting things take their own course.
  - b. Choose your priorities well and give them the resources to make progress. Your people will be watching to see if you are going to try to get by with under-resourcing projects. You need enthusiasm and cooperation to regain momentum. Manage well and you can help rebuild trust and enthusiasm.
  - c. Leapfrog projects. Instead of just restarting stalled technology, marketing, product and other business projects convert them into the next generation by leaping over the prior goals to the next goals. Take the time to determine what is now best in class and change project goals. Of course you will need to do new business cases and justifications. Don't get hung up on sunk costs with existing projects. Make new decisions based on new information.

## 5. 22 cost reduction & profit improvement ideas:

We have been exposed to tens of thousands of cost reduction ideas in the course of our business experience. In a few months the process helped just one client develop over 6,000 ideas worth tens of millions of dollars of additional profits. You would think then that it would just be a matter of looking through the list to hand you just the right ones for your situation but that is not practical.

Experience shows that somewhere between 1 and 10% of ideas that are generated will eventually end up as a valid cost reduction or profit improvement project. Every situation is different and even great ideas may not be transferable from one business to another for any number of reasons.

One of the key elements of success for an idea is that it has to be acceptable. This makes it difficult to just impose ideas onto an organization. Buy-in occurs when those who must implement and support an idea are involved in its generation and evaluation. That is how the ideas on this list were created: facilitated teamwork with a carefully led process.

### The lessons of this list include:

- Ideas come from everywhere in the organization; not just top down but also bottom up
- Ideas can be generated, evaluated and readied for action in hours – not months
- Even if these ideas don't precisely fit your situation they may stimulate your thinking to find something that does fit
- Everything is fair game for improvement when people are given the right training
- Profits are influenced by three factors of the Profit Equation: revenue, expense and loss. Manage all three for the best business results.

<b>Annualized \$ Profit Increase</b>	<b>Whose idea</b>	<b>What is the project</b>
\$7,200	Mail department clerk	Reduce the amount of unnecessary use of FEDEX for mailings
\$6,575	Secretary	Renegotiate cell phone contracts to a better plan.
\$795,000	Mid-level manager	Reduce the size of the car fleet
\$10,000	Low-level manager	Prohibit purchase of premium gasoline for company cars and rentals.

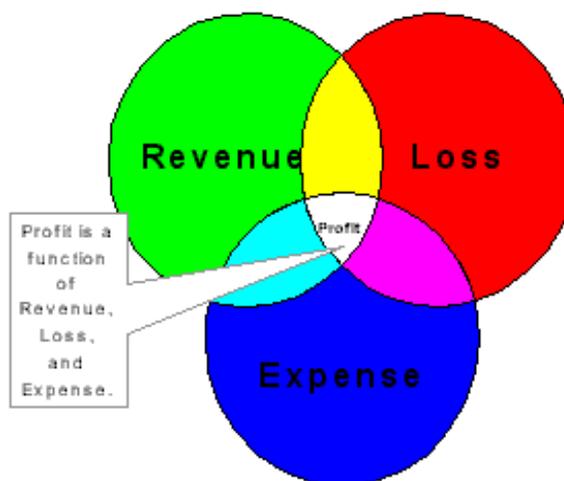
<b>Annualized \$ Profit Increase</b>	<b>Whose idea</b>	<b>What is the project</b>
\$22,800	Mid-level manager	Reduced interest expense by accelerating the billings for a particular service. Accelerated cash flow of a significant amount of money.
\$540,000	Mid-level manager	Organize the work process on certain inspections to eliminate duplicate or early inspections. Reduces contract expenses by this amount.
\$300,000	High-level manager	Renegotiate the lease on specific equipment where the market had changed enough to give the company leverage.
\$10,000	High-level manager	Reduce space rental at a facility by consolidating offices.
\$24,000	Low-level manager	Reduce space rental at a facility by consolidating offices. Same company as above but different location.
\$130,000	Mid-level manager	Reduce space rental at a facility by consolidating offices. Same company as above but different location.
\$485,000	Mid-level manager	Reduce sales commissions on a particular product. Allowed by changing market conditions.
\$4,000	Low-level employee	Outsource the printing and production of a regular mailed report.
\$1,200	Low-level employee	Outsource the maintenance of mailing list returns.
\$7,986	Mid-level employee	Eliminate unused equipment leases and reduce maintenance costs.
\$330,000	Mid-level manager	This is the expected net profit margin from expanding an existing product into a new market territory.
\$85,000	Mid-level manager	This is the expected net profit margin from introducing a new product into an existing market territory.

<b>Annualized \$ Profit Increase</b>	<b>Whose idea</b>	<b>What is the project</b>
\$350,000	Mid-level manager	Reduce the loss and waste of a particular product during process changes.
\$50,000	Warehouse labor	Reduce the damage to product by rearranging the shelving system to allow forklifts to pass safely.
\$18,000	IT/MIS manager	Stop leasing dedicated phone lines and use the Internet for some data communications.
\$175,000	High-level manager	Close a satellite office that is running at a loss instead of a profit.
\$49,000	Mid-level manager	Reduce inventory costs by eliminating or reducing slow moving items that don't make a profit.
\$500,000	High-level manager	Stop servicing a specific market segment that is causing a loss. This is a result of a market segment contribution margin analysis. In addition, some of the segment was kept but at higher prices and increased fees to obtain satisfactory margins.
<b>\$3,900,761.00</b>	<b>GRAND TOTAL</b>	

We are surrounded by opportunities. The skill comes in being able to efficiently see them and effectively evaluate them for implementation.

## 6. The profit equation:

Profit is a function of revenue, loss and expense (figure to right). Revenue is additive while loss and expense are subtractive. The quickest and surest way to improve profitability is to effectively reduce costs. Each dollar removed from expense reports to the bottom line profit. The same is generally true for loss (e.g. quality rejects, waste, shrinkage, unrecoverable



insurance loss; warrantee costs).

The more difficult approach is to increase sales but this must not be forgotten. The equation creates serious dynamic tension in business reality. Studies have shown that companies that focus primarily on cutting costs do not perform well in the long run. Cutting may be expedient for the present but it does not necessarily respect the future. For example, if you want to really cut costs today, stop all future-oriented tasks such as preventive maintenance or product and market development. You will, however, pay a greater price tomorrow.

One approach that we have used with our clients that has generated exceptional results is to increase revenues while controlling expenses. In other words, grow revenues faster than costs. Simple, and one of the most effective ways of achieving profitable growth.

The best corporate plans focus on the total equation. The inclusion of revenue in the drive to improve profits mandates that the future revenue stream be considered in all changes – cutting or revenue growth.

## 7. Conclusions and recommendations:

Companies that are proactive in their approach to managing for the bad times as well as the good times do far better in the long term than companies that take a reactive stance to economic cycles.

**No company has ever cut its way to long term success. It is time to build.**

Now is the time to not only rebuild but also to rebuild with an eye toward being a business that can prosper in both the down and up phases of the inevitable business cycle. This requires innovation and an unwavering commitment to a formal continuous improvement process. Well-designed continuous improvement processes pay for themselves immediately and generate a lifetime of dividends.

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### About the Author

Steven C. Martin is a seasoned international business consultant, problem solver, and continuous improvement expert with over 40 years of real-world experience. His engineering degree is supplemented with extensive graduate studies including an MS in Creativity and Innovation (one of fewer than 400 in the world). Businesses of a wide range of types and sizes have used his proven methods to save money and improve their corporate health. He is available for

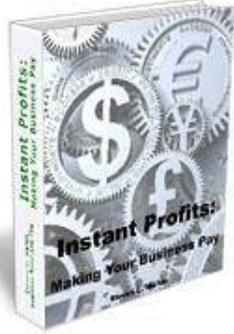
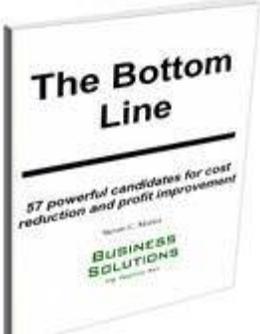
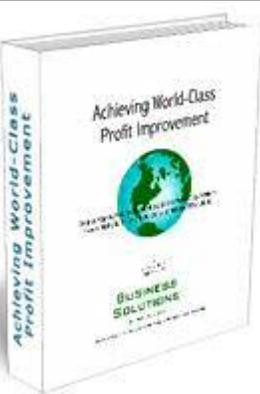
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training, speaking engagements, Profit Improvement Process installation, and business consulting. He is currently helping companies to reenergize their Continuous Improvement programs and to move beyond the historical limits of programs such as Six Sigma, Lean and the various permutations.

## 8. Resources for Cost Reduction and Profit Improvement

These resources are all available now at: [www.ProfitPro.us](http://www.ProfitPro.us)

	<p><i>Instant Profits: Making Your Business Pay</i> - A powerful business book with 250+ business tools, methods, ideas and tactics could lead you to cost reductions and increased profits.</p> <p>Any one of these 250+ business tools, methods, ideas and tactics could lead you to cost reductions and increased profits.</p>
	<p><i>The Bottom Line</i> report includes 57 powerful ideas and tactics that are candidates for Cost Reduction and Profit Improvement.</p> <p>These were all developed in real-life business situations and can get you started with your business improvement projects.</p>
	<p><i>Achieving World-Class Profit Improvement</i> - This book delivers you what you need to establish a continuous or periodic Cost Reduction or Profit Improvement program in you business. It has already saved \$ millions for businesses around the world. Includes:</p> <ul style="list-style-type: none"> <li>• 23 tools and methods to improve profits</li> <li>• 11 real-life tested strategies to guarantee success when you install a cost reduction program or a profit improvement process</li> <li>• How to move Beyond Cost Reduction to the next generation of corporate intellectual growth</li> <li>• Much, much more</li> </ul>

