BusinessPlus+ Newsletter

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Approaches to Improving Business Profitability & Cashflow

Virtually every company is familiar with the broad challenge of improving work efficiency and streamlining costs to boost profitability. By simplifying operational procedures and focusing the product ranges, companies can reduce complexity in specific areas and increase revenue while reducing costs. Companies can also achieve long-term structural improvements by, for example, optimising plant operations, inventory management and distribution structures.

Regardless of their individual circumstances, companies usually ask themselves the same question: ***Where does the operational full potential lie along the value chain, and how do we achieve it?***

Examining Operational Performance

Regardless of its financial situation, every company should carry out an operational performance improvement program occasionally. However, the motivations for conducting such a program vary substantially. Typical reasons include urgency to achieve financial targets, exhausted cost-reduction potentials, a challenging strategic and competitive position, and evolving market conditions.

Expanding Leadership Positions

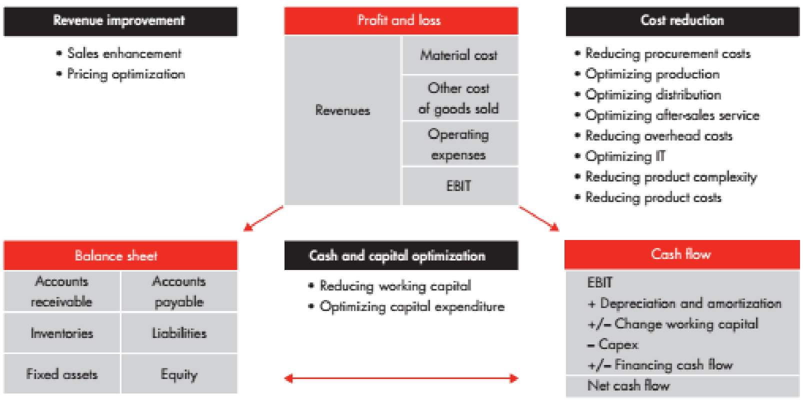
Successful market leaders work constantly to improve a good cost structure. However, some market leaders achieve a satisfactory profit margin but fail to fully exploit their profitability potential.

Closing Cost Gaps

The key is to determine the extent to which the current profitability and cost gap results from operational inefficiencies.

Operational Restructuring

Companies experiencing stormy weather are often confronted with drastic changes in market conditions. Especially in capital-intensive sectors, cyclical or structural market weaknesses quickly lead to revenue losses and dwindling profits. In this situation, companies must optimise their operational business, usually under time constraints.



Source: Bain & Company

Cost management and protecting the bottom line can mean the same thing if handled correctly. This is even more true for companies facing loss of revenue in times of economic uncertainty. However, we know costs don't fall in line with revenue, due to the fixed costs component of overheads – perhaps totalling 70% to 85% of all overheads, depending upon the nature of the industry the business operates within.

In difficult times, leaders and their financial team normally turn to the big items to find savings. This usually includes reducing staffing headcount, closing offices, cutting marketing budgets, inventory and moving to cheaper premises, to name a few.

These types of large cost cuttings can often feel like a 'Let's See if it Works' School of Management strategy of *'slash and burn'*. But it doesn't have to. However, the approach to cost management does need to be prudent to ensure it does not undermine the key differentiated business strategies that management have adopted.

The diagram below illustrates some guidelines to the various cost reduction initiatives and the approach that might be used by business owners and management.

	Initiative		Approach
Cost reduction	• Reducing procurement costs	→	Expertise
	• Optimizing production	→	Expertise
	• Optimizing distribution	→	Expertise
	• Optimizing after-sales service	→	Expertise
	• Reducing overhead costs	→	Benchmarking
	• Optimizing IT	→	Expertise
	• Reducing product complexity	→	Analytics
	• Reducing product costs	→	Benchmarking
Cash and capital optimization	• Reducing working capital	→	Benchmarking
	• Optimizing capital expenditure	→	Benchmarking

Source: Bain & Company