



THE FAST TRACK APPROACH

TO

COST REDUCTION



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Wringing cost reductions from every area of the business is an important part of surviving in this economy. All companies today need to quickly identify and implement cost reductions – no sacred cows, no stones left unturned. Analysts and lenders, either for new lending or covenant compliance waivers, will place premiums on cost-disciplined companies. Over the years we have developed our approach to cost reduction projects, which are relatively modest sized projects as compared with the cost reductions that can be achieved. Here is our Fast Track Approach to Cost Reduction.

Mine the Business Platform for New Opportunities

In many companies, management does not have much of an attention span for Business Platform issues. Their focus that can be compared to a “three-sided coin”:

1. Entrepreneurial transactions, deal making, and sales and marketing gets the greatest focus by senior management – the heads side of the coin.
2. Product or service delivery and customer service also gets great focus by both senior and middle managers – the tails side of the coin.
3. The Business Platform gets fuzzy focus at best – the thin side of the coin.

Items 1 and 2 above are key components of the “Value Chain”. Item 3 is the Business Platform that is comprised of Executive and Management Processes as well as Support Processes. This can be illustrated as follows:

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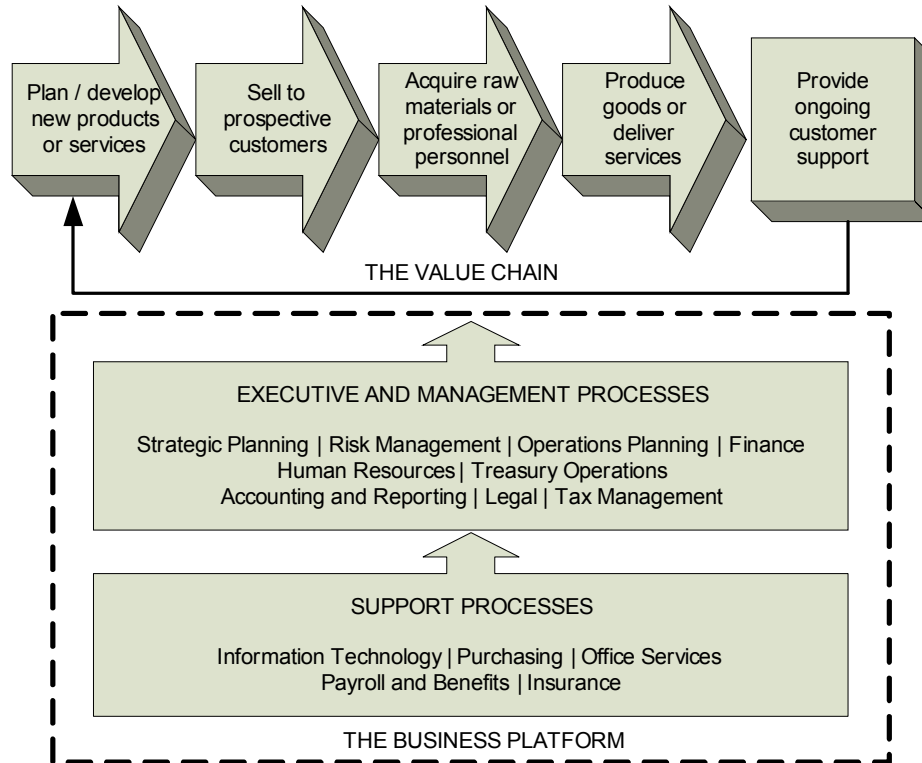


Figure I: The Value Chain versus The Business Platform

The Business Platform is ripe for picking low-hanging cost reduction fruit. That's the first place you should mine for cost reduction opportunities.

Focus on Achievable Change / Results

In cost reduction projects, there are essentially three stages of change which can be correlated to project risk / reward:

1. Incremental Change – describes a strategy that aims for and achieves operating expense reductions and / or improvement in internal effectiveness in the shorter-term. These opportunities will be more numerous, lower in payback but also lower in risk. Cumulatively, they can add up to something substantial.
2. Substantial Change – describes a strategy that results in significant improvements without making fundamental changes to the company's existing business

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- approach. These opportunities will be less numerous, greater in payback but also somewhat higher in project risk.
3. **Transformational Change** – describes a strategy that results in introducing a fundamentally new industry approach. In any given company, there will be few opportunities, if ever, for true transformational change but the payback could be quite dramatic (i.e., “transformational”); however, the project risk will also be greatest.

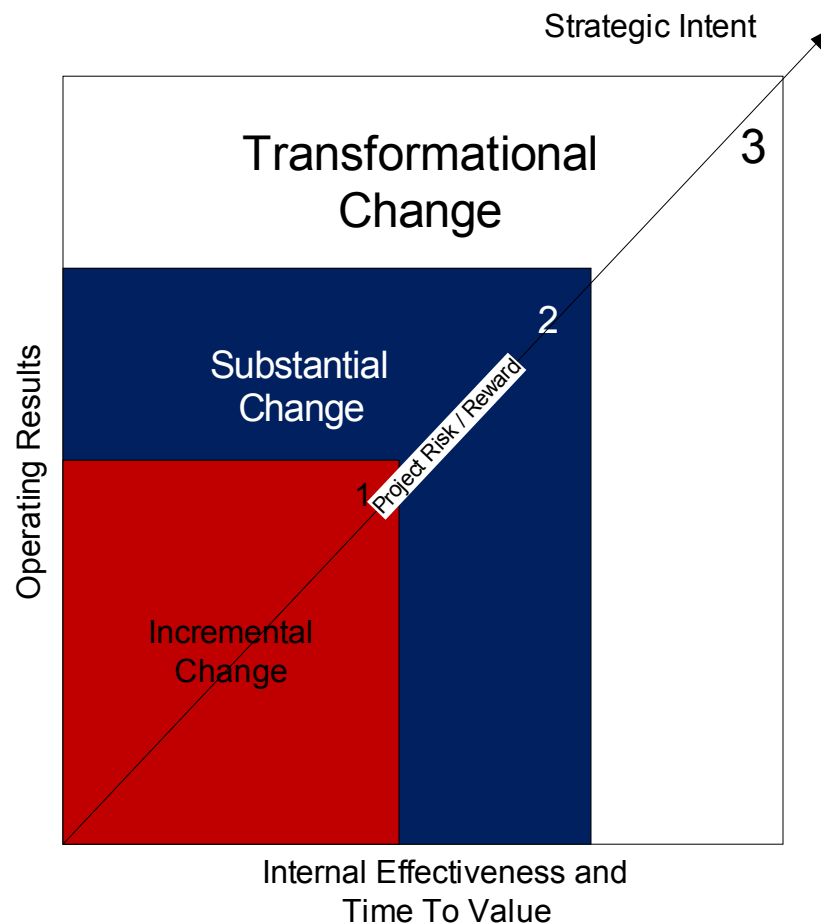


Figure 2: The Three Stages of Change

In our approach to cost reduction, we focus on identifying incremental and substantial change that get our clients significant near-term results without undertaking transformational change and the associated project risks. We prefer to leave transformational change to those newly minted B-School grads that other consulting firms field on their projects!

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Focus on Better Not “Best” Practices

We cringe whenever we hear the term “Best Practice”. What a Best Practice is for one company, might not work within the unique culture and operating environment of another company. Accordingly, we prefer the term “Better Practice”. We have often heard about magical Best Practice metric databases that allowed for benchmarking and comparative analysis against peer groups. First of all, those databases usually existed only in project proposals and other sales documents. Secondly, most “peer groups” are so broadly categorized that any such comparisons are usually worthless – unless benchmarked against an internal peer group.

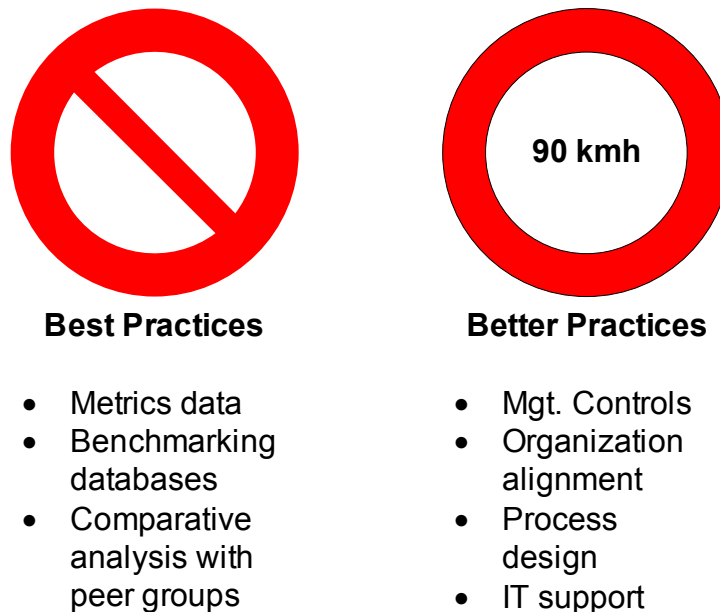


Figure 3: Better, not Best Practices

Identify Lots Of “Quick Hits”!

When we are engaged to facilitate a cost reduction project, we always sort and prioritize our resulting recommendations into two categories:

- Quick Hits; and
- Focused Improvement Opportunities.



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A “Quick Hit” is an actionable task the client’s own personnel can implement on their own, with no outside resources required and in a reasonably short timeframe. It will also result in a reasonable payback for the effort. Some quick hits can be as easy to implement as issuing a memo to correct a processing inefficiency. Or, it might mean writing up a new policy document. It is not an extended project like implementing a new ERP system. We’re talking days, weeks or several months at the most.

A “Focused Improvement” opportunity is more of a sustained ongoing project with its own budget, likely requiring outside resources. A good example would be the implementing a new ERP system requiring software and process consultants beyond the capabilities or time constraints of internal resources. The time frame for these projects is usually at least two quarters and usually longer.

We like to see lots and lots of Quick Hits identified early on whenever we facilitate a cost reduction project. That is because it enables us to expedite the time to value for the client’s investment in such a project. It also generates excitement since middle-level managers can quickly see results. Then you can anchor those results and look for more wins.

Our Project Route Map

Facilitating cost reduction projects is a bit more like of an art form than, say, measuring the extent of a liability under some FAS pronouncement. It requires the “soft skills” of understanding “change management”. Our cost reduction projects are always divided into two phases of work:

- During Phase I we identify a portfolio of improvement opportunities that are sorted and prioritized into the Quick Hits and Focused Improvements.
- During Phase II we monitor the implementation of the Quick Hits and also either develop business cases for Focused Improvements or assist with implementation.

Phase I begins with our confirming our understanding of the business strategy with senior management. We then formulate our “initial hypotheses” of where to look for improvement opportunities within the business platform. That comes from reviewing financial statements, cost trends and other data as well as from interviews. Once we have formulated those initial hypotheses, we gather data and revise our hypotheses as

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necessary. We then facilitate process re-design work shops to present and co-develop solutions which are then sorted and prioritized, as follows.

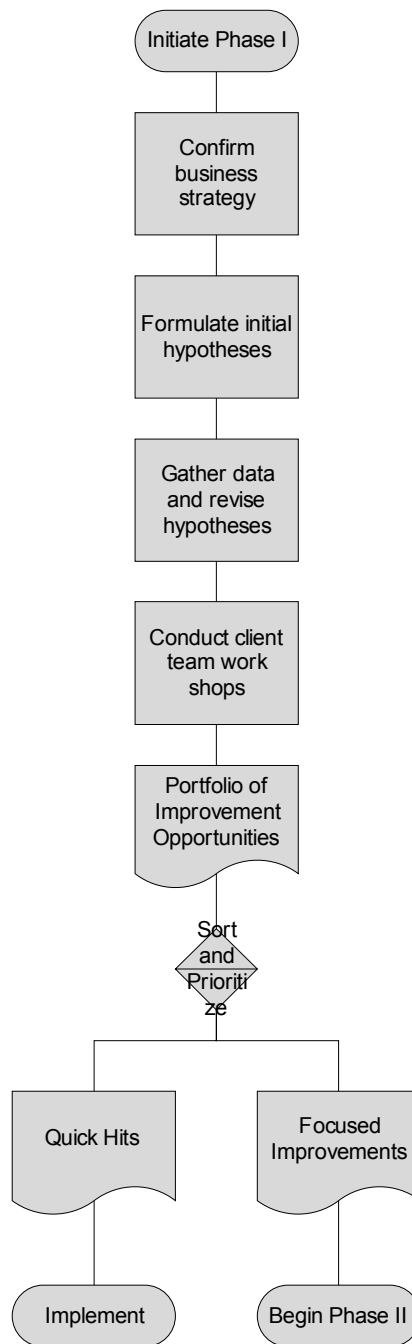


Figure 4: Overall Cost Reduction Project Route Map



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Our Top Ten Steps to Business Platform Cost Reduction

Cost reduction work is more an art form that involves a solid understanding of the process of change management. Along those lines, here is our top-ten list for ensuring a successful cost reduction effort.

1. **Obtain senior-level commitment.** Without the CEO's backing, don't waste your time! That means that CEO needs to actively communicate interest, support and willingness to commit resources to the effort.
2. **Establish a sense of need and urgency.** In today's economic climate this should be easy to do – as in “your job depends on the health and survivability of this company”.
3. **Create a guiding coalition.** This is a cross functional team of managers headed up by a project sponsor who would be their direct manager. One thing to keep in mind when forming up this team, you want people on the team that don't have the time to be on it, not those who do.
4. **Develop a shared vision and strategy.** This is a subtle but an important first step in establishing a “touch stone” against which all resulting improvement opportunities will be measured against. If a recommendation doesn't fit in with the shared vision and strategy, don't waste too much time with it.
5. **Communicate the change vision.** It is important to establish a project communication program early on. If the project leadership doesn't communicate where they are headed, how can anyone down the line be expected to follow?
6. **Empower employees for broad based action.** The team must be empowered to be able to take broad based action. If the project team doesn't believe they have the power to change the status quo, they won't.
7. **Generate short-term wins.** Quick Hits are the key to overcoming initial project inertia. Find lots of Quick Hits and implement the low hanging fruit quickly. Nothing breeds success like early success.
8. **Consolidate gains and procure more change.** Once momentum is achieved through lots of Quick Hits early on, the project team will be psyched up. Now is



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the time to undertake the more challenging projects that will result in greater paybacks. Go for it!

9. **Anchor new approaches in the culture.** Once most of the project results have been achieved, don't stop now. Keep the project teams intact and focused. You have a chance to keep it going and anchor change management into the culture.

10. **Hire the right consultant to guide the process.** Although this may seem self serving, there is much to be said for having an independent professional driving this type of process. For one thing, a consultant will bring fresh ideas and a willingness to challenge "sacred cows". And, there is much cost to be wrung out of those cows! In addition, change management is something that requires a good deal of neutral meeting facilitation skills. And, it's always easier to challenge the status quo when you know you're leaving after a project is over.

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We hope you have found Our Thought Leadership white paper to be helpful and we would appreciate your feedback.

For additional information on our Cost Reduction services, please call us on 917-267-7685.

Richard T. Azar, CPA
Managing Member
The Fast Track Group, LLC

(p) 917-267-7685

razar@TheFastTrackGroup.com
www.TheFastTrackGroup.com

420 Lexington Avenue, Suite 550
New York, New York 10170-0550

P.O. Box 291
Oyster Bay, NY 11771-0291