Save to prosper: from cost reduction to cost optimization

Ernst & Young
Quality In Everything We Do

Businesses face unprecedented threats to their financial health if they fail to sustain the cost reductions forced on them by a downturn. Yet achieving such reductions is easier said than done. In this report we highlighted the many challenges that confront enterprises as they grapple with cost reductions and suggest strategies to follow.

In the course of a downturn, businesses put cost reduction at the top of their agendas. In a recent Ernst & Young *Opportunities in adversity* report, cost reduction was identified as one of the principle initiatives undertaken by global enterprises. We now consider the next logical steps: once savings have been implemented, does a business consign cost reduction to history and return to previous patterns?

Emphatically not. This report argues that effective cost reduction has to become engrained in businesses' DNA, in order to tackle the challenges of the coming years. Low cost operations are no longer a matter of choice but of necessity. Competitors – whether online, from emerging economies or simply traditional rivals who have adopted cost reduction programs – will not hesitate to flex their competitive advantage.

The challenge now is to instil a pervasive cost reduction culture, to the point that it becomes a regular, normal and expected part of business life. There needs to be a paradigm shift, such that cost reduction becomes relevant to front and back office operations, to the shape of the business model, to the portfolio of customers (are they sufficiently profitable?) and to organizations at whatever point they are in the economic cycle, in whatever sector or in whatever geographic region.

This report identifies a full program of sustainable cost reduction targets and strategies to properly implement them. It outlines when such action should take place, in what order, with what partners, to what ends and how enterprises can move from efficiency to effectiveness, from simple cost reduction to cost optimization.

In this report

Executive summary

This report takes as its premise the fact that 60% of businesses do not sustain cost reduction programs, despite the clear evidence that sustainable cost reduction pays long-term dividends.

Based on our survey of 561 decision-makers in 11 of the largest world economies, we identified the challenges that face businesses wishing to achieve cost reductions, the kinds of savings that are typically made and how they vary by industry sector and by geography.

We look at the psychology of cost reduction: what prevents individuals and businesses from carrying it out, along with proposals to counteract such barriers and strategies to help motivate employees to instill their part.

This report covers specific courses of action and proposes, distinguishing between sales, general and administrative (SG&A) cost reductions and costs of goods sold (COGS) reductions to provide a distinct and targeted approach to cost reduction.

We detail cost optimization, rather than simple reduction, using a series of examples to aid businesses in their push to improve profits with limited resources. We also debate the merits of improving profits versus maintaining market share, along with the expectation that there will be a higher level of mergers and acquisitions (M&As) in the coming months.

A series of threats from global competition and from new business models means that companies must treat cost reduction as standard practice in order to survive and prosper. We outline the source of these threats and the varying attitudes of certain business sectors and geographies to them, providing insights, actionable suggestions and strategies for business leaders to follow.

The opportunities offered by innovative business ideas and by environmental measures such as renewable energy can assist businesses as they strive to reduce costs. We highlight some leading business innovations and some elements of the green agenda that can be harnessed by companies for cost reduction, detailing how these integrate with conventional cost reduction strategies.

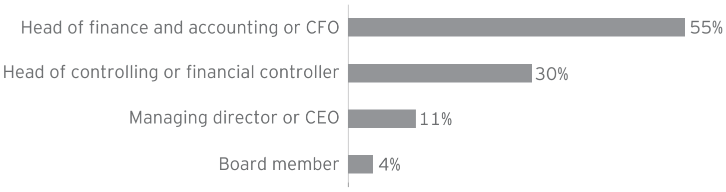
Throughout the document, we stress that cost reduction must be embedded into business strategy, to prevent repeating the mistakes and missing the opportunities of previous economic cycles. We argue that businesses have to shift from efficiency measures to effectiveness, from cost reduction to cost optimization, and to help ensure that cost reduction becomes a permanent factor in commercial behavior.

Scope of the survey

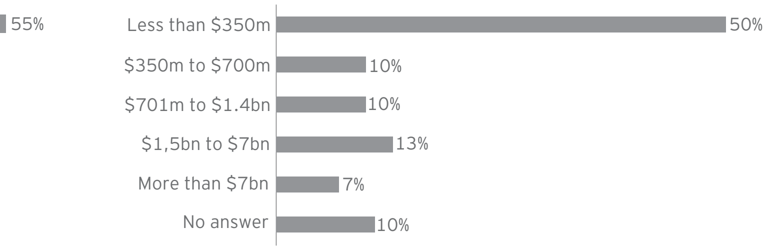
In July 2009, Ernst & Young engaged an independent market research company to conduct a survey of 561 decision-makers on the subject of ECR. The companies surveyed represented 11 of the largest economies in the world and 11 different industries.

Respondents included CFOs, representatives from management, accounting, financial control and boards of directors. Telephone interviews lasting between 15 and 25 minutes were conducted anonymously.

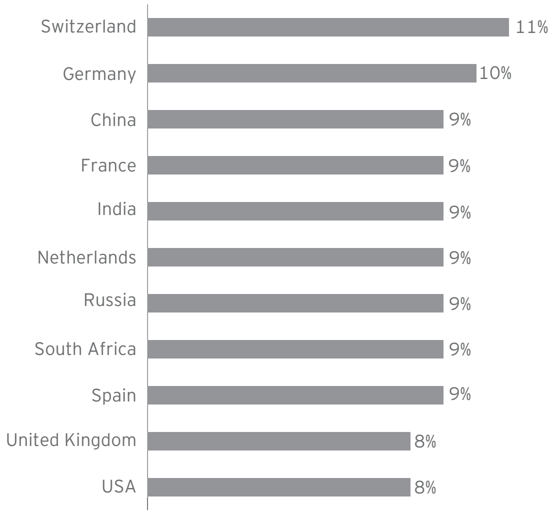
What is your job title?



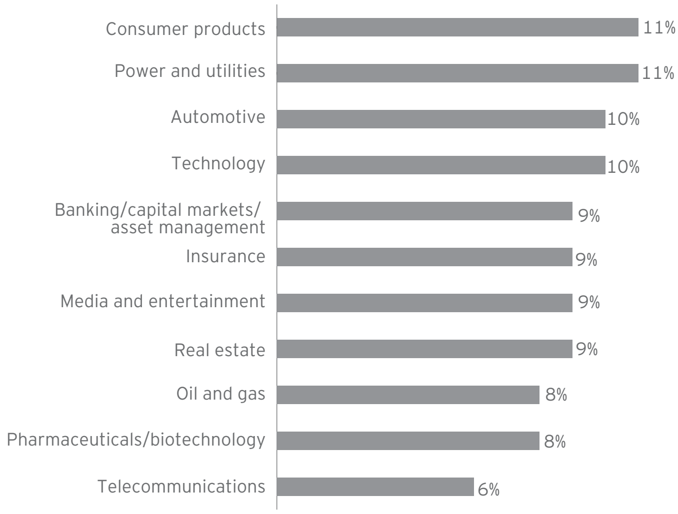
What are your organization's annual global revenues? (in US dollars)



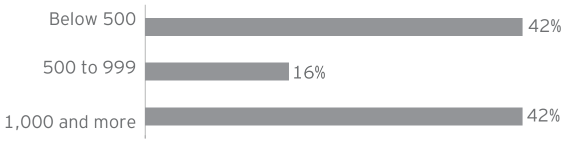
In which country are you personally located?



What is your primary industry?



How many employees does your organization have?



Sustainable enterprise cost reduction (ECR) – a blueprint

"You only find out who's been swimming naked when the tide goes out." – Warren Buffet.

Between 2002 and 2008, the tide of share prices, corporate earnings and profits rose relentlessly in most of the world's major economies. But the global credit crunch and subsequent recession left many businesses exposed to unfamiliar conditions, forced to make rapid and radical cuts to many aspects of their operations, before they were left high and dry.

In this recession, with many thousands of businesses still unsure of their ultimate survival, cost-cutting is at the forefront of executives' minds. More than two-thirds of businesses (68%) say that cost consciousness became "extremely important" in their company during the last year, compared with the previous two years.

A further 86% were extremely confident that they would achieve sustainable cost saving benefits through continuous cost management, structural adjustments and the concerted efforts of management and employees.

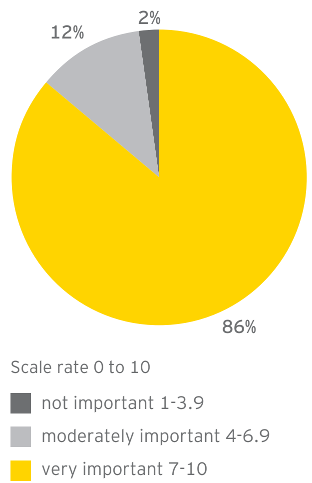
You could say they have little choice; cost savings must be made, whether executives want them or not. And these will clearly be easier to achieve if you tell your colleagues (and persuade yourself) that savings are sustainable and for the long term good of the business, rather than simply a knee jerk reaction to a temporary downturn.

Although cost consciousness has become extremely important in most organizations during the last year, a majority of company achievements so far have been on tactical and temporary measures, delivering no more than 10% cost reduction in most businesses. The most important steps to cost reduction have yet to be fully addressed or implemented and realized. No more than 25% of companies are looking to achieve a 20% or more cost savings over the next 12 to 18 months.

As we detail later in this report, it is no simple task to persuade employees that the business has to make cost reductions. It endangers morale, it may impact on recruitment and retention of staff and it may play badly in the media. Nevertheless, for most businesses, it is an inescapable fact of life in the current economic environment.

According to figures gleaned by Ernst & Young from previous recessions, 60% of companies fail to sustain cost reduction programs over the longer term, especially when the enterprise and the wider economy begins to grow again.

Please indicate the extent to which you are confident in retaining sustainable the cost saving benefits achieved by cost reduction program?



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We have identified a number of reasons for this failure:

- Lack of sufficient monitoring and tracking
- Allowing tactical cost reductions to push out strategic reductions
- Making size a higher priority than profitability
- Losing focus on cost reduction as expansion gets under way or the business model changes

We recommend that businesses take a series of steps to secure their cost savings for the longer term, helping to engrain new and lasting behavior in the enterprise and providing a form of insurance against the inevitable shocks of the future economic environment. The way forward is about achieving more with less.

We believe that business leaders should better understand what drives costs across their business in order to increase flexibility to react to volatile demand levels, paying for this if necessary. We recommend that businesses leverage synergies and scale more actively, plan more frequently and monitor demand more closely. We also recommend that businesses manage suppliers more acutely, to mitigate the risk of them failing.

Where substantial costs need to be taken out of a business (say 30% of revenue or more) then we recommend that the operating model is redesigned and fundamental changes are made.

Businesses should regard cost reduction as an everyday, routine part of their working lives. If it is seen as something extraordinary or special, it is unlikely to be sustained. Many companies adopt cost reduction in a downturn and then abandon it in better times. It is important to recognize the true, long-term value of cost reduction and stay the plan.

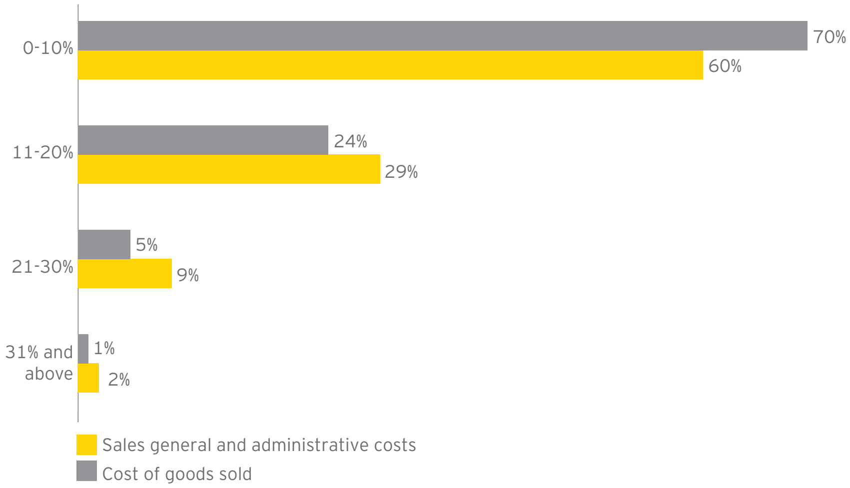
A first guide to sustain cost reduction:

If you are in the midst of a cost reduction program, or are thinking of launching one, here are five key questions to help you assess whether your organization is positioned to deliver sustainable benefits:

1. Are you addressing all possible areas of cost savings to deliver the required profitability targets over the next 12 to 18 months?
2. Does your operating model need to be changed to achieve or sustain the required financial benefits and are you clear about what it needs to look like?
3. Do you have the right data and insights to give you the confidence that you are making well-informed decisions to achieve success in your cost reduction program?
4. Do you have the right leadership to convey the messages, the right capability to deliver the change and the proper mindset in the business to maintain long-term focus and discipline?
5. Do you know what sustaining success looks like once you have delivered on your cost reduction program?

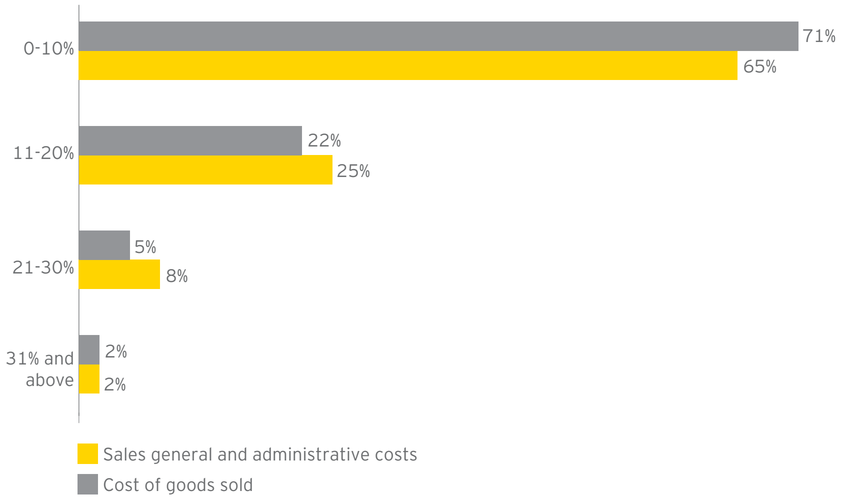
If you are not satisfied with your answers, it probably means that your cost reduction program will not deliver and sustain the value you expect.

As a percentage of revenue, what cost saving have you achieved?



shown: percentage of respondents

As a percentage of revenue, what is the additional cost target in the next 12-18 months?



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The psychology of ECR

"Whenever you see a successful business, someone once made a courageous decision." – Peter Drucker, management consultant.

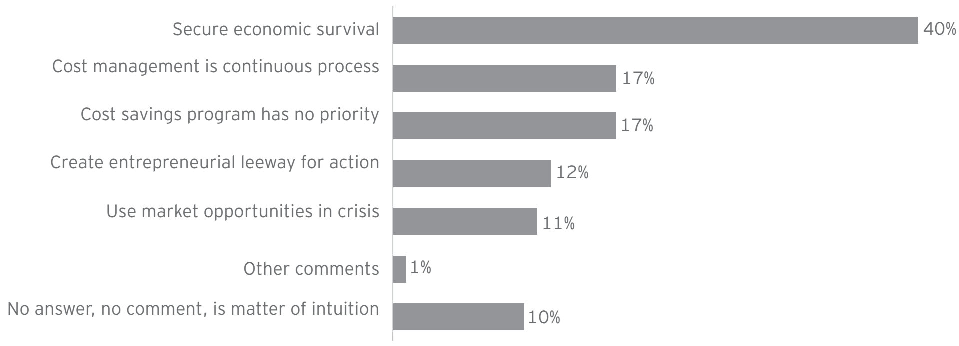
Some executives regard proponents of long-term, sustainable ECR in a similar way – maintaining that cost reduction is a necessary but annoying fact of life in a downturn, but should be relegated to a back seat so long as conditions are good.

Just as the former delivery clerk is now head of logistics, the person responsible for wiring the telephone is now the chief technology officer and the librarian is now the chief information officer, so the discipline of ECR is shifting from irritating occasional necessity to a major element of corporate strategy.

As our survey shows, however, there is some distance still to travel before ECR is fully accepted in this way. By far the most common reason (40%) given for carrying out an ECR program was "to secure economic survival". Just 17% saw cost management as a continuous process, while the same percentage said that a cost saving program was "not a priority."

So what is holding companies back? Why are businesses so reluctant to adopt a strategy that not only saves them money but increases their effectiveness and helps to secure their long-term viability? Despite the dire economic conditions, 25% of our respondents have no plans to carry out any kind of cost reduction program.

Could you please explain in detail why you have adopted cost reduction programs?



shown: percentage of respondents and "open"/without pre-quoted response

Among the barriers to carrying out effective ECR we have identified:

- Companies' unwillingness to follow-through on cost reduction, even where they have made firm commitments. This may stem from anxiety that the business will appear weak, that competitors will take advantage of lower investment or from management inertia.
- Difficulties in "selling" ECR to executives and to employees in general must be overcome. Most companies have an element of competition between departments or offices. Each is reluctant to accept that it should lower its costs - an additional concern is that it is a commonplace in business life that departments overspend in order to maintain their budgets for the following year.
- There is a mis perception among employees that there is often unfair treatment during ECR programs. People react badly to lower rewards if they see executives receiving higher rewards at the same time.
- Issues of recruitment and retention are intensified during ECR. Candidates are likely to prefer to work for a company which is expanding and increasing its investment, whether in people or in new business. It indicates that their options will grow, and that their remuneration and the status of the organization will increase.
- When businesses undergo change programs, ECR is often dropped.

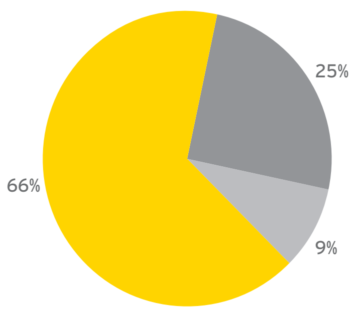
To counter these concerns we recommend that business leaders do a number of things. They should refer to the process as "cost optimization" rather than cost reduction (see "From reduction to optimization"). Executives need to be patient, and to develop a communications strategy that stresses the improvements achieved through ECR and what they mean for the enterprise as a whole.

Time must be set aside for the change process to take effect, creating an environment where employees feel like they are being treated fairly. Costs saved in one part of the business can be invested elsewhere, so that there is still a sense of expansion and optimism.

Executives must have enough humility to accept where cuts need to be made, rather than playing competitive games with their colleagues over budget levels.

And finally, cost reduction and optimization need to become a routine, normal part of business operations, rather than something which is identifiably short-term and done only in response to a crisis.

Are you actively engaged on cost reduction program?



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Where and when to act

"About the time we can make the ends meet, somebody moves the ends." – Herbert Hoover, President of the United States, 1929 to 1933.

The suddenness of the credit crunch, prompted by the collapse of Lehman Brothers on 15 September 2008, took world markets by surprise. Many businesses that had relied upon credit found themselves in severe difficulties, unable to sustain their investments. Naturally, they cut back wherever possible, meaning that items such as travel costs, bonuses and marketing were all quickly reduced.

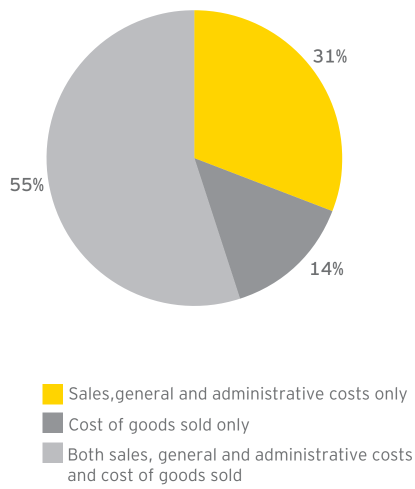
When a business is in acute financial peril, as many businesses have been in the past year, the business is often unable to afford the most sensible option. In the short-term, survival is the key factor, and to achieve this, businesses had to get the best debt terms possible. In some sectors, such as automotive, overcapacity had to be addressed through sharp cost reductions.

Some have argued in favor of restructuring business models through further standardization and consolidation of core processes, conducting M&A deals or moving operations to a lower cost economy. Yet, since this may entail a lengthy payback period, in recent months we have recommended that many companies concentrate on becoming cash positive, identify cost savings that pay back within three to six months and make tactical cost reductions that will place the business on a stable footing.

As a first step, we believe businesses should look to achieve cost reductions in general and administrative costs, followed by sales and marketing (altogether known as SG&A). Once this is underway, businesses should identify savings in COGS. As our survey results show, this pattern is borne out by global companies, with more than twice as many respondents addressing SG&A as are looking at COGS (14% to 31%).

Nevertheless, there are significant variations in sector between businesses that are concentrating solely or largely on SG&A cost reduction, such as banking and insurance, against those which are committed to tackling both SG&A and COGS, including pharmaceuticals and technology. Equally, respondents in China, France and the UK showed a marked preference for SG&A cost reduction programs, whereas those in Germany, the Netherlands, Spain and Switzerland are looking at both kinds of reduction. A more detailed look at sector and geographic variations is provided in "From recession to recovery."

What areas are your cost reduction program addressing?



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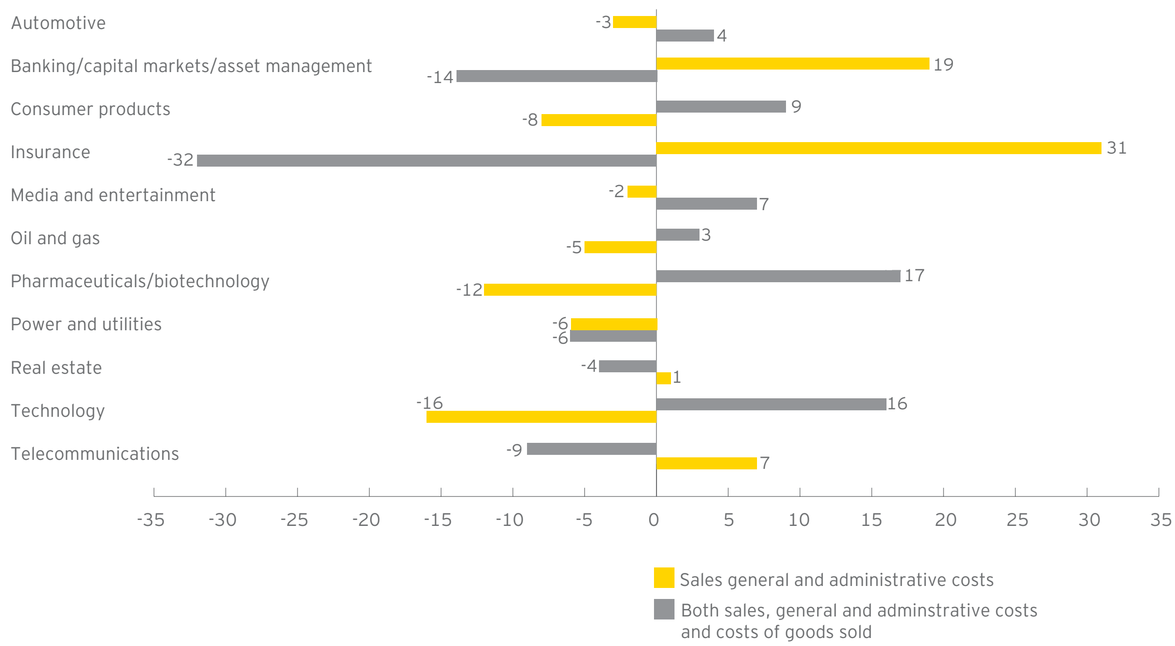
A services company will clearly have more scope to reduce SG&A costs than COGS, whereas a manufacturer will be more able to reduce COGS than SG&A costs. What is important in the current climate is to distinguish between measures taken to alleviate the effects of the credit crunch and those which can be sustained into the longer term, to produce more fundamental benefits.

We think that companies should look at the relative impacts of SG&A savings, as the economy (and individual companies' trading position) begins to improve. SG&A costs generally remain stable as revenues increase, meaning that they form a relatively smaller percentage of total costs over time. This can lead companies to ignore them or to neglect to monitor them, allowing them to increase as revenues increase. When this happens, earlier cost reductions are lost and businesses return to old habits and spending behaviors.

Cost reduction programs need to be treated in the same way as EBITDA reporting (i.e., something that is performed routinely as a means of checking the health of the business and planning for the future). Executives may have become familiar with ECR programs for the first time in this current downturn, as a means of digging their businesses out of trouble, but the challenge now is to integrate the programs into normal operations, to help ensure that unnecessary costs don't reappear and to safeguard the enterprise against future shocks.

What areas are your cost reduction program addressing?



shown: deviation from the global average results (percentage)

From reduction to optimization

"It's not your salary that makes you rich, it's your spending habits." – Charles A. Jaffe, author.

From the "quick-fix" approach to cost reduction that took hold in the summer of 2008, with its emphasis on the easily achievable, mostly policy-driven targets such as travel and recruitment freezes, business leaders are now turning to longer term goals. What should their companies look like in the future? What are the cost reduction priorities and how can they be addressed?

Although the business priorities for most businesses will not change over the next 12-18 months, the emphasis is now moving from tactical to strategic initiatives. Therefore, we contend that the focus of corporate energy in this field needs to shift from efficiency to effectiveness, from cost reduction to cost optimization... The challenge moving forward, perceived by a large number of executives, is sustaining momentum and having the courage to act. As one executive recently said, "Our challenge is to keep the momentum going, our employees are getting tired and are being asked to do more than before." The question that needs to be asked is not "how much have we saved?" but "how much additional revenue has been created?"

It is a pity that so few companies – less than 40% have traditionally sustained cost savings once recessions have passed. It is akin to when someone crashes a car through failing to look where they are going, has the car repaired and then does the same thing again.

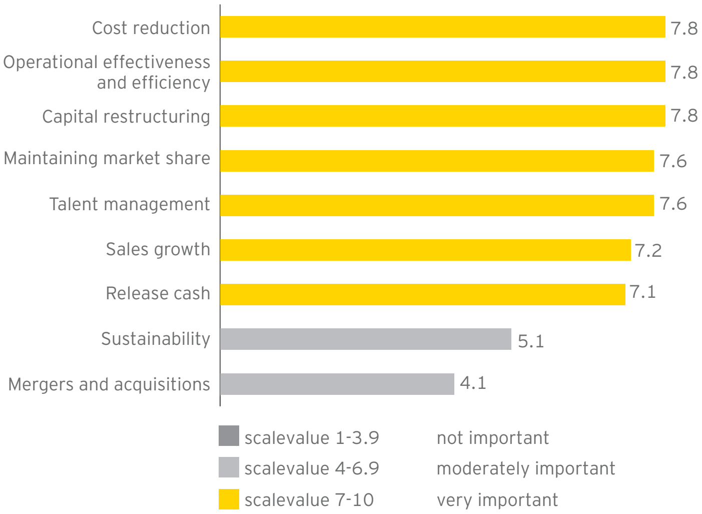
There are some encouraging signs. Our survey found that while most respondents are very concerned with cost reductions, they place equal emphasis on factors which will help them achieve growth and future security. As this chart shows beside, operational efficiency and effectiveness is placed as a top priority, alongside capital restructuring and cost reduction. Maintaining market share and talent management are slightly lower, with sales growth and releasing cash also highly ranked.

We believe that achieving these objectives can be considered as part of a cost reduction program – so long as any increased costs are outweighed by even greater revenue growth. In this way, cost savings become a fundamental part of a business model, with profitability (rather than sheer cost reduction) as the defining metric.

Professionals from Ernst & Young have identified key points on how to achieve cost optimization:

- Cost reduction programs should liberate pools of available cash to invest in people, projects and acquisitions, to aid company growth and create a positive effect for employees.
- Cost management should be a tool to push business development and overall growth.
- Make and maintain as many costs as possible flexible, without losing control of them, to prepare your business for future volatility.
- Look for incentives offered by governments, to hire certain professionals or set up shared services operations for example.
- Advise and equip your sales teams to negotiate hard to reduce discounts and keep margins high.

How relatively important in your opinion are current the following strategic objectives to your organization?



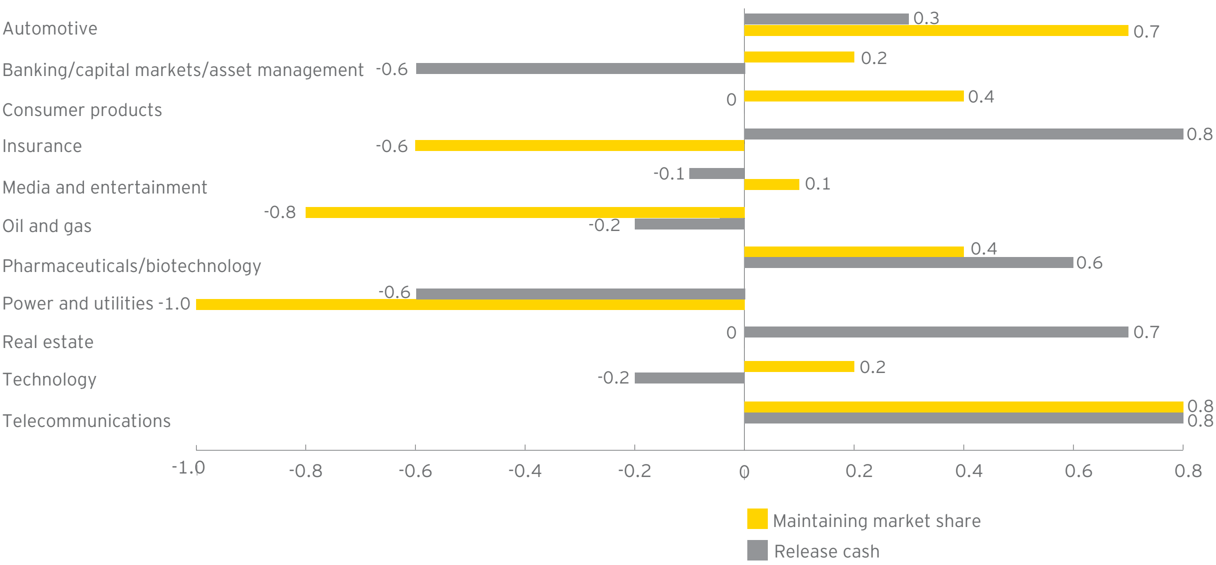
shown: rating from 0 to 10 of respondents

There is an ongoing debate within corporations over the value of profit optimization versus maintaining market share. For sectors such as automotive, pharmaceuticals, consumer products and telecommunications, market share is seen as a high priority in itself. These sectors believe that share price is related to market share and that competitors will take advantage of any reduction in market share and that customers are not easily regained, once lost.

While we understand these sentiments, we argue that for many sectors, profitability should be a higher priority than market share. Where selling to a segment of customers is no longer profitable, businesses should consider exiting the market. This goes against the grain for many sales people, who prefer to achieve volume results rather than high margins, but the new business mantra of "smart is better than big" needs to be adopted by many enterprises.

Finally, although M&As have been greatly reduced over the past 18 months, and enthusiasm for them remains somewhat weak, the justification for sensible mergers has not disappeared. Mergers still offer significant opportunities to achieve synergies and cost savings (not to mention gaining greater market share). We anticipate that M&A will experience a renaissance in the coming year, as the global economy returns to growth and opportunities present themselves. Business leaders should consider this option among their cost reduction strategies.

How relatively important in your opinion are current the following strategic objectives to your organization?



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From recession to recovery

"There are two kinds of companies: those who work to charge more and those who work to charge less." – Jeff Bezos, Amazon CEO.

As the global economy emerges from recession, it will be tempting to return to previous patterns of behavior, to spend in the same way as before, to allow cost reduction to be relegated to a marginal position and to sigh with relief that the period of austerity is over and the party can recommence.

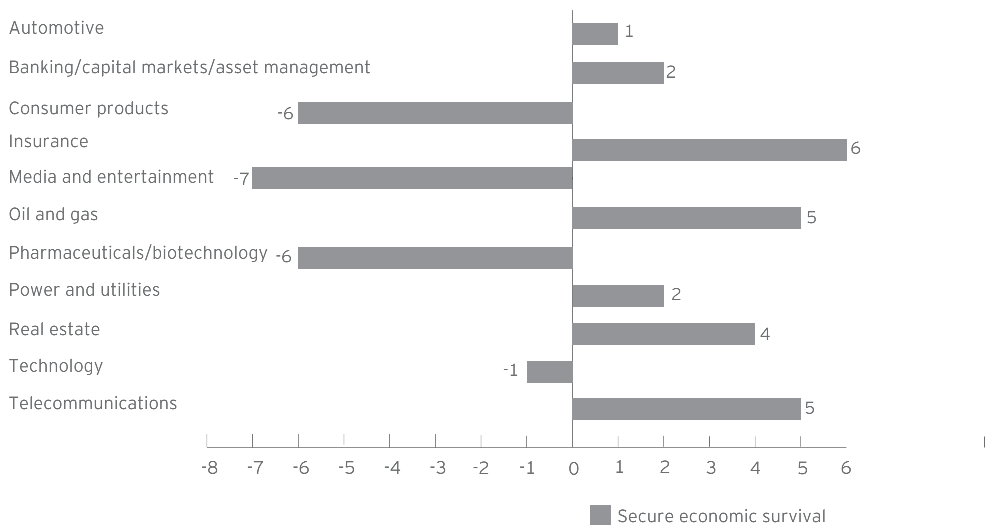
We believe that this would be a mistake. The world of businesses has changed in many ways. The threats and opportunities are far removed from those that pertained as recently as 2007. The internet has overtaken print and television as the most important advertising medium. We are likely to see "peak oil" in the next 20 years and legislation to tackle climate change. The increased volatility that will result from these factors means that businesses can no longer rely on a safety cushion in their P&L forecasts.

Of all these factors, the rise of new competitors from the Far East may cause the most disruption to business models and create the most need for sustained cost reduction. China and India are becoming manufacturers of high-quality goods, developed in the Far East but marketed around the world. They are no longer simply low cost destinations for the manufacture of Western goods or for back office functions. Their low cost bases will soon provide a challenge to competitors everywhere.

For evidence of this newfound confidence, see chart page 13. While respondents from most countries surveyed fell into a mid-range of between -13 and +14 (deviation from global average results) when assessing cost saving as a priority, as a continuous process or to secure economic survival, Chinese-based responses regarding economic survival were off the scale. There is no question that Chinese companies fear for their existence. It is the rest of the world that should be afraid.

Conversely, the Swiss response gives a strong signal that cost saving "has no priority" among companies there. This is a curious finding, given that Switzerland has suffered disproportionately from the crisis in financial services. Either Switzerland is well placed to emerge in good shape from the recession, or Swiss executives are uniquely short sighted. Some of the countries most affected by the credit crunch, including Germany, the UK, the US and Spain have understandably embraced cost reduction strategies, as they worked hard to reduce their cost base.

Could you please explain in detail why you have adopted cost reduction programs?



shown: deviation from the global average results (percentage)

There were further disparities among the business sector responses. While the insurance, telecommunication, oil and gas, real estate, power and utilities and banking sectors regarded cost reduction as a means of securing economic survival, pharmaceuticals, consumer products and media and entertainment sectors did not.

These results reflect the uncertainty that emerged in late 2009 as the recession appeared to abate, yet recovery was not fully underway. Unemployment was rising in many economies, there were persistent fears of a "double dip" recession and many Western countries were mired in debt.

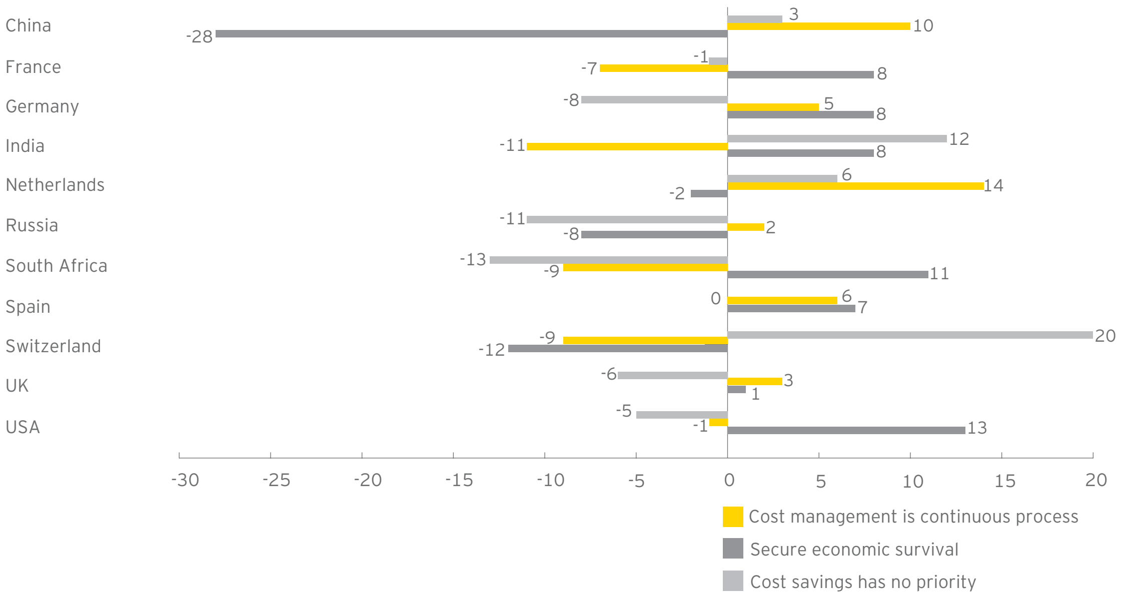
We argue that such uncertainty must be accepted as a new constant in business life. Cost reduction programs are no longer a last resort, to be executed in extreme situations when a recession hits, but a necessary and fundamental everyday business practice.

To achieve cost reduction as the economy improves, we propose that businesses:

- Look carefully at standardization and centralization possibilities, especially when an outsourcing agent can achieve better economies of scale to reduce costs
- Address all operational areas, both back and front office, with the objective to make the organization as flexible and agile as possible to reflect the economic fluctuations other time
- Track costs carefully to help ensure that they rise more slowly than revenues to improve margins

The respondents to our survey said that "clear ownership and accountability" is of most importance in achieving cost reduction targets, along with "accurate benefits tracking."

Could you please explain in detail why you have adopted cost reduction programs?



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Innovation and the green agenda

"Innovation distinguishes between a leader and a follower." – Steve Jobs, Apple CEO.

In 1980 and 1981, in the middle of a savage global downturn, Apple Computer went public and Microsoft sold its first operating system to IBM. In 1990, with the economy stagnant, Cisco launched on the Nasdaq. And in 2001, amid the ruins of the dot.com crash, Google emerged as the world's favorite search engine.

There is every chance that a further pioneer will emerge from the current recession, unleashing disruptive technologies to excite and confuse the corporate world. Yet at every level, the desire and need for innovation is enhanced during a recession.

Among the most recent innovations that facilitate cost reduction are:

- **Collaborative working, with suppliers, customers and partners**

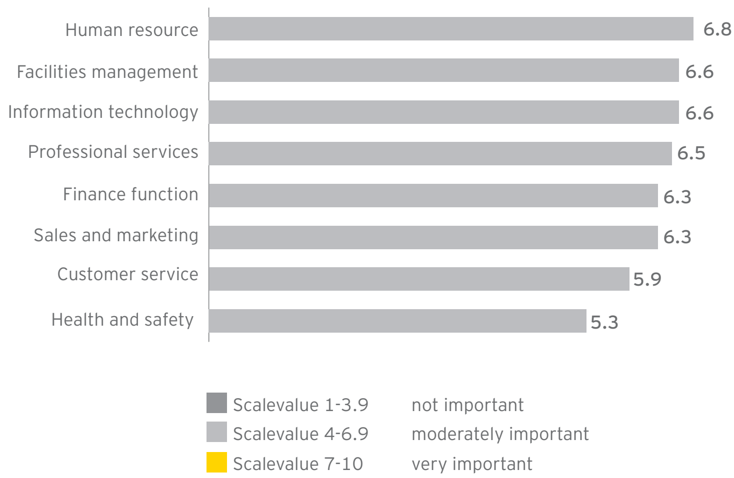
  This has been one of the corporate wonders of the age, as previously aloof and brand-jealous companies such as Coca-Cola and Microsoft have opened up their lines of communication, accepted more customer suggestions and allowed their brands to develop in a more fluid way.

  In the automotive sector, rivals Renault and Peugeot have begun to identify common suppliers potentially at risk, and to work with the FMEA (Fond de Modernisation des Entreprises Automobiles), the FSI (Fond Stratégique d'Investissement) and the CDC (Caisse des Dépots et Consignation) to support the most vulnerable suppliers to mitigate supplier risk. Airbus has launched a workshop, with government funding, to collaborate with suppliers and acquire equity in their businesses. For the government, employment is protected, and for the company, contracts are secured.

- **Virtual working**

  Spurred by the need to cut down travel costs, many companies are now turning to video conferencing, but also to virtual worlds such as Second Life. Businesses have established virtual premises, host virtual conferences, discuss job opportunities with virtual candidates and conduct virtual trade. Second Life is now a US$500m+ economy and is growing rapidly, as its attractions and cost advantages become clear. Online tracking, monitoring and collaboration systems help businesses to save on transport, recruitment and telecommunication costs, among many others.

Please indicate the extent to which you concentrate your attention on the following areas of sales, general and administrative costs in your cost reduction efforts?



shown: rating from 0 to 10 of respondents

- **Nanotechnology and semiconductors**

  Sensors in fields tell farmers how much water their crops need. Intelligent glass changes its properties according to temperature to cut down on heating costs. Mobile phones can transfer funds much more cheaply than Western Union. All these applications are transforming the world around us – businesses need to be aware of them, put them into practice and harvest the savings.

Green means lean

Environmental issues traditionally get less attention in a downturn. When an enterprise is fighting for its life, corporate social responsibility is never its first priority. Yet this time, with the conjunction of the recession and a concerted global effort to tackle climate change, along with high and rising fuel costs, the green and cost reduction agendas are growing ever closer. Here are some examples:

- The clean tech sector, including renewable energy, will become a US$2t market within the next decade, providing opportunities for businesses in every sector.
- China is building the biggest solar and wind production industries in the world, yet only one of the 10 largest wind or solar companies is based in the US.
- Walmart has reportedly increased the fuel efficiency of its fleet by 30% in the past few years, through small changes such as aerodynamic skirts on its trucks or power units on its vehicles so engines don't have to idle while the driver rests.
- Microsoft has redesigned its data centers so they now use half the energy they used before.

Besides cost savings, green initiatives aid relations with customers, suppliers and employees and enhance a company's reputation. This has an enterprise value, even in a downturn. Many energy-efficiency projects (such as low energy lighting) achieve payback within as little as three months.

Business leaders need to adopt these principles, looking for cost reductions that apply innovative or green solutions. The chart page 14 shows a range of sales, general and administrative (SG&A) areas that respondents to our survey have ranked in importance for cost reduction. Each of them could entail innovative or green aspects. For example:

- Human resource work in recruitment can be managed at low cost through virtual websites such as Second Life.
- Facilities management can achieve massive savings through energy-efficient technology.
- IT can help an enterprise save costs throughout the supply chain.
- Professional services can employ web-based collaboration to reduce costs.

If companies discard innovative or environmental issues for short-term expediency today, their customers may not forgive them tomorrow, especially if they believe they are paying over the odds for goods or services from a dirty, old-fashioned business.

Conclusion: using ECR to gain competitive advantage

"Whenever an individual or business decides that success has been attained, progress stops." – Thomas J. Watson, IBM president 1914 to 1956.

Of the many competing demands on executives' time, cost reduction is an easy one to neglect. As this report has demonstrated, it is a complex and difficult area, typically espoused in a downturn and discarded in a boom, tricky to execute well and liable to alienate employees or to compromise market share.

As President John F.Kennedy said, "a great nation does things not because they're easy, but because they're hard." Equally, a great company has to face up to the task of sustainable cost reduction, understanding the challenge ahead but firm in the knowledge that it will yield long-term results.

The majority of companies fail to sustain cost reduction. Employees and fellow executives may resent cuts to their pet projects or their remuneration. The company share price may fall in response to a decision to pursue profit over size and salespeople may resist attempts to limit their volume in favor of better quality targets.

Despite all these hurdles, achieving sustainable cost reduction or optimization will mean that the business is far better equipped than before to deal with competition, whether from domestic rivals or from the new breed of online operators, or from emerging businesses in low cost, Far East economies, for example.

Without effective cost reduction, many businesses will struggle in the years ahead, victims of their own inflexibility, their unwillingness to recognize new commercial realities and burdened with legacy costs that make them uncompetitive and lethargic.

We believe that business leaders should consider the points raised in this report. Some of it will make uncomfortable reading, but we commend it to you as a crucial tool, as you guide your business out of recession and attempt to capitalize on emerging opportunities, while tackling the unpredictable challenges ahead.

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