

## **Sustainable Cost Savings.....**

Cost savings in logistics and the supply chain are always welcome because they feed directly down to the bottom line and boost profits. They are even more welcome in the current environment in which sales revenues are weakening and there is significant cost pressure from rising oil prices and labour costs which make up a largest proportion of operating costs.

Anyone can cut costs, but how does one do it in such a way that it has a minimal impact on customer service which might pose a threat to the business's market share? This is what we call 'sustainable cost savings'. It is quite a challenge and one which managers are increasingly faced with today. The more so in businesses where tight control over costs has been the principal focus of logistics and supply chain managers for years. The pressures of just coping with the day to day operations often leaves management with little time to step back and analyse in an objective way what opportunities there may be to cut costs in a sensible manner. This is where consultants can help. However, this is no place for simplistic benchmarking exercises where dubious percentage comparisons are made with businesses or industries which have little connection with your own. Benchmarks have meaning when there is a reasonable match between companies in terms of structure and market-place and where product offering and order sizes are similar. In reality, it is often extremely difficult to get hold of such information with any confidence in the operational statistics and one is often left with doubtful cost comparisons with profit and loss accounts which may be structured in an entirely different way from your own. In any event, one cannot take percentages to the bank. The cost savings must be real and sustainable and these are not simply achieved by reference to hopeful commentaries on the profit and loss account. So, where can one go from here?

One solution is to find consultancies like ours with demonstrable line management experience of cutting costs and dealing with all the pressures and trade-offs to which management are routinely exposed. It is not just an issue of establishing credibility with local management. Logistics and supply chain operations may only represent a relatively low percentage of net sales, but they are often very complicated and difficult to change without substantial risks. The devil is in the detail. Effective change management depends on far more than the logic of a good idea. It requires practical experience of the good and bad consequences of implementation to help mitigate the inherent risks involved in change. One must be able to identify waste and opportunities to reduce costs and this essentially comes from changing processes and the ways things are done. If one does not understand how changing processes can go wrong, then it is very difficult to put in place the steps needed to manage the risk. Sustainable cost savings are based on the identification of practical opportunities and careful thought about their implementation. And there is a further important consideration. If the management of the business does not own the savings project because it does not believe in

the logic and the plan, then in our experience the cost savings are rarely ever achieved in practice. The process of engagement between the consultancy and client management because a critical element in the success of the assignment. This is a joint exercise and iterative process where the conclusions are agreed and shared together. At the end of the day, however much help consultants may provide during implementations (and this varies widely), ownership of the project must lie firmly with the business for it to have any chance of success.

Where do the cost savings come from, and what can businesses reasonably expect? We carried out a straw poll within our own consultancy which is staffed by senior line managers from the logistics and supply chain industry and has been in operation for over 15 years. After a great deal of debate, the following consensus emerged from our collective experience. Businesses which have poor customer service levels almost invariably have high costs as well because of a lack of management control. Such businesses offer the largest potential for cost savings alongside those which can be achieved through the process of mergers and acquisitions. Savings on logistics and supply chain costs are in the range 15%-35%. Often the greatest savings lie in the interfaces and channels between the different links in the supply chain. One finds a similar experience in businesses which have not seriously reviewed their logistics and supply chain processes and costs in an integrated and holistic way in over 5 – 10 years. The problem which such businesses can face is that while they may have responded to changing customer needs in terms of product offer, their logistics and supply chain service may not have been adapted at the same pace. In such cases, the business often finds itself poorly equipped to deal with increasingly demanding markets which require a high level of service and flexibility. The need to improve service at an acceptable cost through sensible restructuring becomes an ever more urgent task. Formal supply chain and logistics reviews can kick start the process of constructive change. In well run businesses, identifying cost savings is generally a much tougher proposition and the changes are often harder to implement. In our experience, cost savings here are generally in the range 5%-15% of operating budgets.

We take a naturally conservative approach to cost savings because there are so many variables involved in implementation. Unless cost savings can be identified which easily exceed 5%, then one should be wary about declaring them because they can so easily be lost through the process of change during implementation. Not every contingency can be accounted for even with the best experience and will in the world. Cost savings come from many different aspects of logistics and supply chain operations, and it is rare indeed to find a magic bullet in a single area. While it can happen, our experience is that sustainable cost savings are best achieved through actions on a number of fronts. Those seeking revolutionary change are best advised to undertake it in an evolutionary manner. If it does not pass the commonsense test, it is unlikely to be achieved in practice. Pragmatic analysis and practical implementation plans are the secrets behind sustainable cost savings. **Neil Middleton**