



COST MANAGEMENT = COMPANY VALUE

Why this should be the most natural equation in every organization

Before solving the equation, we first want to elaborate on its terms, starting with the company value. There are multiple ways to define company value, yet alone the term value. One thing all the definitions have in common though, is that in all of them earnings play a major part. So, one of the ultimate company value driving figures are the company's earnings. Let's park "earnings" for a minute and come back to them.

To define the other term of the equation "cost management", we consulted several different sources. Summarized from these sources, cost management would be defined as the process of planning and controlling a company's budget. Really? Yes, we're surprised too, this can't be the entire deal. How could our equation on this definition possibly make sense, controlling your budget = earnings. Well, it doesn't, and the reason lies in the definition and perception of cost management.

We, the savings iD, define the term cost management as the continuous reduction of your cost base at same or better quality. And suddenly the equation makes sense. Just think of it as a scale. If you reduce your cost base (make it lighter), the earnings side will increase (get heavier). And furthermore, there is a 1:1 correlation.

It sounds so simple, yet this equation doesn't seem to be on every one's mind. There is one term that people think of first instead.

We've asked, in a non-representative survey, what lever would you pull, if you wanted to increase your earnings by 5%? Here as a side note to iterate, earnings define a company's value. Amongst the possible answers to select were "reduce your cost base" or "increase your sales revenue". Guess what! More people think that boosting your sales revenue would lead to 5% earnings increase easier than cutting your cost by 5%. That's a dangerous perception that might lead to a competitive disadvantage for a firm.

Let us outline why.

A 5% earnings increase can be achieved by taking out 5% of your cost base. The beauty is the direct 1:1 correlation, as long as you don't spend the money somewhere else. Whereas sales revenue won't come with a direct 1:1 earning correlation. Reason being that every sales revenue transaction comes at a cost. Hence you would need to over-proportionally increase your sales revenue to achieve the exact same results.

Yet we find ourselves in a situation where many firms don't have a well-established and regarded cost management function or a procurement organization that is correctly financially incentivized and enabled to achieve exactly above. When it comes to cost, a firm's procurement organization is the MVP of the game. The most valuable player. Depending on the industry your firm is in, cost influenced by procurement alternates between the largest to second largest cost block in a firm's P&L. That is why, we at the savings iD, wanted to change the game how a procurement organization continuously reduces a firm's cost base.

The plan of cost attack can no longer be unsustainable top down budget cuts, short term cost saving fire drills or expensive cost saving projects ran by a 3rd party. And on top with natural attrition of procurement employees, fundamental knowledge related to cost savings and maturity gets lost and one often starts from scratch, pulling the exact same levers, just in a different way.

The ones that take the daily decisions on how money is spend in a firm must be enabled to become more than just a buyer, sourcer, contract manager or category manager. Procurement folks must become end to end cost owner, be aware of the financial impact of every decision they take and be able to pull all existing cost saving opportunity levers. Moreover, pulling all the levers in an efficient, easy and comprehensive way.

You might now think that we're talking about a superstar of a procurement person. Or you wonder how on earth can any procurement person know all this. It's actually quite simple. It has nothing to do with the person itself, the key is enablement.

One of the many things 2020 taught us is that things can actually be done differently, easier, remotely and more digitally. We set ourselves the goal to find a way to enable every person in a procurement organization to identify all possible cost reduction opportunities, easily, efficiently, digitally, within the matter of hours and without the risk of data exchange, installment of software or engagement of a costly 3rd party. And we found a way.

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