STRATEGIA
Partners

Lowering Costs to Accelerate Growth

By
Jean Berg
Founding Partner, Strategia Partners

Periods of economic slowdown often highlight certain realities.

Every company must regularly adapt and reallocate its resources. This applies not only to the choice of activities, businesses, business models, and geographies but also to the efficient management of costs.

Only a significant reduction in costs will allow you to invest in growth.

1. Growth costs and cruising costs

Every business is based on a mix of growth costs (transitional costs incurred to expand and gain market share) and cruising costs (structural costs required to maintain market presence).

Growth costs include expenses related to innovation, necessary marketing and sales investments required for growth, temporary sub-optimizations during scaling phases, the various benefits of a more attractive business model to customers, and price reductions required to capture market share…

These costs must be optimized through prioritization, reallocation of resources across businesses and geographies, strategic differentiation, and business model adaptation.

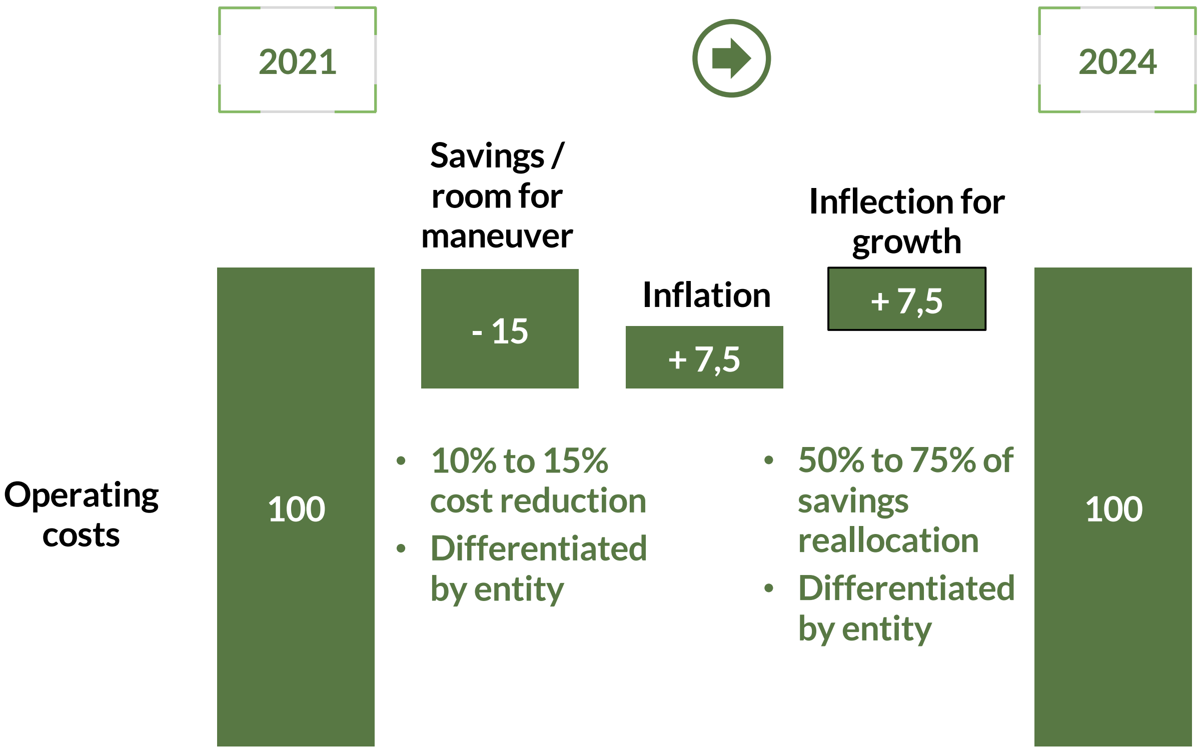
Cruising costs must be competitive and as low as possible to create room to maneuver and finance growth: competitive costs for production, logistics and customer access, as well as for overhead costs, operational processes and support functions.

This means moving production facilities to low-cost regions, moving certain support functions (finance, IT) or development functions (R&D) to these regions, clusters or outsourcing certain support functions or outsourcing them, reducing complexity and costs, optimizing the brand portfolio, optimizing prices, digitizing operations, and concentrating functions...

Sustainable growth cannot be achieved unless the cost of crusing is competitive and provides the necessary margins to finance growth. It is essential to explore all sources of efficiency and cost savings that can generate an additional 1 to 3 points of EBIT to finance the additional costs of growth.

STRATEGIA
Partners

Lowering Costs to Accelerate Growth



- Based on solid management principles
- With disruptive measures and approaches for cost savings
- With project selection approaches for growth to prioritize and track impact

2. The methodology for reducing costs and investing in growth

1. Define/validate management principles

A move of this magnitude must be based on solid management principles by senior management. These principles should define the basics of the management approach: value creation levers, delegation principles, centralization principles, autonomy and localization principles, cross-functional modes, and links between countries and activities...

They will help build organizations, operating modes and, consequently, costs, with an orientation that is coherent with the strategy and consistent across entities. They will provide a framework and boundaries for the detailed implementation of approaches and the balance between centralization and local adaptation logic.

2. Set ambitious reduction targets that require new approaches

Cost reallocation programs for growth should be based on a global vision and management ambition, before being implemented and detailed at the entity level.

For operating expenses (OPEX), a typical approach is to set a goal of reducing costs by 10% to 15% and reinvesting 50% to 75% of these reductions in growth initiatives. The ultimate goal is to achieve stability or low growth in these costs. This approach needs to be fine-tuned based on growth ambitions, the nature of the business, and economies of scale effects.

3. Differentiate cost reduction by business units and strategic priorities

Differentiation by entities and strategic priorities is essential to focus efforts on the key challenges, while involving all functions. It involves analyzing the competitiveness of the various functions in relation to competitors and benchmarks, especially for support functions (finance, human resources, and certain IT roles, etc.).

To achieve the initial target, reductions should vary between 5% and 35%, depending on the specific needs and strategic importance of each area.

4. Differentiate investments by unit and growth priorities

Each entity must invest to respond to market and technological changes and to improve productivity. It is also critical to re-energize teams: for operating units, to accelerate growth; for support functions, to serve operating units more effectively. Often, these investments are not made adequately because of a lack of resources. Managers are reluctant to make the drastic reallocations within their scope that would make this possible. This movement must come from top management. Differentiation of opex investments is also needed at this level. Simple rules for investment priorities and returns need to be defined. For example, as a general rule, 1 euro of marketing and sales investment should generate 5 to 7 euros of gross margin over three to five years.

STRATEGIA
Partners

Without room for maneuver, no investment.

Without investment, no growth.

Without growth, no value creation.

KEY TAKEAWAYS

- Growth is the only way to create value in the long term.
- A company that does not grow by more than 7.5% per year (i.e., a doubling of revenue every 10 years) loses its attractiveness and independence in the long term.
- Organic growth is the result of investing more than competitors do, and applying the impact of that investment is applied to the most favorable mix of businesses, geographies, and customers.
- This growth investment can take several forms: it includes the cost of product & technology innovation, business model innovation, digital innovation, environmental innovation, marketing and sales investments, price reductions...
- This investment must be optimized to maximize efficiency.
- To finance this cost of growth, we need to free up room for maneuver in ongoing costs.
- An approach focused solely on lowering ongoing costs for their own sake is sterile: it's necessary to combine cost reduction with the reallocation of investments for growth.

5. *Launch the program at the operational team level*

With solid management principles, ambitious cost reduction targets, both overall and by unit, and investment targets, both overall and by unit, teams must define a three-level action plan: disruptive actions with new approaches to cost reduction, optimization actions and investment actions. This action plan, quantified and defined over time, will prioritize objectives to ensure financial coherence by emphasizing cost reductions first, followed by investments, not the other way around.

What to conclude?

Companies must adapt to changes in their markets, technologies, and skills in order to survive. But, this perspective alone is not enough. It must be accompanied by investment in activities and approaches for growth. That's why we need to combine two approaches in a combined way: reducing costs to regain flexibility to reinvest in growth and doing so in a differentiated way.

Without flexibility, there can be no investment. Without investment, there is no growth. Without growth, there can be no value creation.

STRATEGIA
Partners

Strategia Partners

Strategia Partners *is an international strategy consulting firm based in Europe (Paris & Zurich), the United States (New York & Seattle), and China (Shanghai). It assists the top management of large European and North American companies in their growth strategy. Its approach integrates 3 perspectives: strategic and financial performance, environmental performance, and human performance.*

Contact : jean.berg@strategiapartners.com

Paris | Zurich | Shanghai | New York | Seattle

STRATEGIA
Partners

Strategy Consulting for Sustainable Growth

Strategy. Impact. Growth.

For Corporates

For Private Equity

Portfolio Strategy | Business Acceleration Strategy | Operational Strategy | Due Diligence