

Myth Of Corporate Cost-Cutting Revealed -- Financial Executives Admit That Cost Savings Back Within Three Years

Source: PriceWaterhouseCoopers www.pwcglobal.com

New Global survey reveals shareholder appeasement NOT long-term business success is dominant in time of economic uncertainty

LONDON--9 APR 2002 --THE COMMITMENT of businesses to corporate cost cutting is today (April 2002) facing a new challenge – from the financial executives responsible for keeping firms competitive.

Nearly 60% of global CFO's or equivalent concede that the costs they are currently cutting will creep back into their businesses within two to three years.

Global financial executives also reveal that they are victims of a 'copy-cat' culture of short-term cost cutting that is overriding the drive for long-term prosperity. Globally, 55% of CFOs say that cuts are driven more by a keenness to impress analysts and shareholders than to improve their own businesses.

These findings are among the highlights of a new survey by PricewaterhouseCoopers – the first of its kind to be undertaken – exploring the attitudes of over 590 businesses in Europe, the Americas, Africa and Australia towards cost cutting and the current economic uncertainty.

The survey reveals that while the vast majority of CFOs understand the importance of long-term strategic cost reduction, they are failing to practice what they preach. This gulf between theory and business reality is demonstrated by a number of contradictory survey findings including:

- While 86% of respondents agree that significant short-term cost reduction programmes can be strongly detrimental to staff morale and loyalty;
- 61% of firms have imposed a freeze on recruitment and nearly 60% have reduced staff
- 88% agree that, during a downturn, companies should be willing to invest to add long-term value to the business BUT
- Nearly 60% have already deferred or cancelled investment.
- While 74% agree that companies often get their cost-cutting priorities wrong by cutting what is easy to measure rather than what is most needed;
- Less than half (48%) of all firms have a cost reduction strategy in place.

- While nearly 50% of all respondents think it is inevitable that all businesses will have an online procurement process in place within 2-3 years, and 51% of respondents without online procurements systems say they plan to introduce them in the future;
- 53% of global businesses claim e-technology is founded on hype and peer pressure rather than any genuine long-term benefit.

Jonathan Tate, partner at PricewaterhouseCoopers and sponsor of the report, "Strange Days – Are businesses equipped to catch opportunity in an unpredictable world?" said:

"Cost is not the root of all evil. Too much cost cutting can be fatal, leaving companies under-resourced for the future. But our survey shows that firms have yet to understand this – quick fix cost reduction dominates the global corporate agenda, with 60% of companies putting recruitment and investment on hold.

"Companies are failing to differentiate between good costs and bad costs and shareholder appeasement is winning out over long-term strategic management.

"Companies are failing to take advantage of opportunities for re-shaping their cost base. Only 38% of respondents are investing more in web and e-business development, while 30% are actively cutting back on IT investment."

Strategic Cost Reduction – A Great Idea

PricewaterhouseCoopers firmly believes that it is essential for every organisation to understand which costs add value to a business, and which do not. Effective cost containment programmes will address good, bad and neutral costs:

- **Good Costs** are those that drive current and future growth. Good costs include spending on targeted sales and marketing, research and development and business-critical training. Stripping out good costs will normally have a detrimental effect on any business in the medium term.
- **Neutral Costs** do not drive growth directly, nor are they prime candidates for significant cost reduction. Neutral costs include spending on IT infrastructure plus frontline and customer-facing support staff.
- **Bad Costs** are those that neither support growth nor support the organisation's infrastructure. Bad costs include duplicated processes, uncontrolled procurement, unnecessary IT spend, non-strategic projects and capital investments, as well as bloated back-office support functions.

It is the role of strategic cost containment programmes to assess all categories of corporate spending – including IT; head-count; procurements; assets and tax - in order to identify good, neutral and bad costs. This assessment can then be used to target costs more effectively and to

reinvest savings into growth areas of the business.

Businesses adopting a strategic approach to cost containment will also avoid the knee-jerk, me-too response of the 'copy-cat' cost cutters' who are prepared to risk long-term prosperity in order to secure the short-term appeasement of shareholders.

Look forward, however, and by establishing a culture of strategic cost reduction businesses will prevent bad costs creeping back on to the balance sheet once the markets improve.

Looking at strategic cost reduction – the case of procurement

In the survey, 70% of respondents agreed that procurement efficiency is key to any cost reduction strategy. In addition, 73% also believe that making procurement a priority is essential in preparing for the economic upturn.

But if the theory once again appears sound, the messages communicated by the respondents are mixed and confused. While 64%, for example, say they are investing more in IT-driven process improvements, just 38% are investing more in web and e-business development. In addition, 34% are actively cutting back on web investment.

Karel de Baere, PricewaterhouseCoopers Global e-Business Head said: "Our survey demonstrates that businesses globally do believe investment in web technologies and strategic IT, such as procurement, can play a key role in securing organisation-wide cost savings and enhanced stakeholder relationships.

"The reality, however, is that all too often many IT investments fail to deliver the cost savings expected of them. The conclusion is that enterprise-wide cost control depends on fully integrated processes: technology must become part of the underlying process – not bolted on to an existing superstructure."

ENDS

Notes to editor:

- 1) The report is based on the experience of PricewaterhouseCoopers and on quantitative independent research, profiled below:

Between the beginning of January and the end of February 2002, PricewaterhouseCoopers commissioned arnold+bolingbroke to conduct an independent global study, gauging attitudes to the prevailing climate of economic uncertainty. The research was designed to establish what strategies businesses are adopting to address market shocks and volatility and the key drivers behind the decisions they are taking. Over 590 managers (mostly at CFO, or equivalent, level) were surveyed in companies worldwide.

592 quantitative interviews were conducted, predominantly with CFOs, in Europe (UK, Germany, France, Netherlands, Belgium); North America (USA, Canada); South America (Brazil); Africa (South Africa); and Asia Pacific (Australia). Around 50 interviews were conducted in each country, with the exception of the USA, where 138 interviews were carried out.