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Cost reduction strategies for SMEs

Cost control should be an integral part of your business strategy, not something you turn to when your business hits hard times.



Business UPDATE

Introduction

During tough economic times such as these businesses can be faced with the need to reduce costs to remain competitive, maintain profitability, or even to survive.

And whereas it is necessary to respond to these needs with appropriate measures the truth is that short-term, unplanned cost cutting is often not sustainable - and can come back to bite you.

Where possible, it is better to mitigate the need for short term cuts by adopting a long-term strategic approach to cost control.

First, a couple of tips

1. *Involve your employees*

Experience shows that cost control is most effective when employees are involved in the process and a culture of cost awareness spreads throughout the business. It is important, when establishing or reviewing cost control procedures, to ensure your employees are fully informed and have an opportunity to add their opinions. Some businesses encourage employee participation by offering incentives and rewards for cost-cutting initiatives.

2. *Start with the biggest costs*

Generally, it is wise to begin by looking at the biggest costs first. Clearly, a saving of 1 per cent of £100,000 is much more significant than 1 per cent of £10,000. But though it is largely true that if you look after the pounds the pennies will take care of themselves, there is something to be said for keeping a close eye on small costs as well, especially if it helps to raise awareness of cost control among employees.

Review your office systems

One area where substantial savings can often be made is the reorganisation of office systems, especially IT. But these savings can take time to filter through and might even involve added expenditure initially.

Increasingly popular with small and medium sized businesses (SMEs) is the adoption of cloud computing - using third parties to provide services such as computation, software applications, data access, data management and data storage via the Internet.

Cloud computing has many benefits for SMEs. It requires much less investment and

expenditure on both hardware and software, reduces the need to have IT professionals on site, and offers access to data at any time and from any location. Most significantly, it can be expanded to cope with increased demand and charges are generally based on the use made of the services, which can result in significant savings compared with providing all the services on site.

There are of course disadvantages with cloud computing, the main one being a degree of loss of control over your data and possible associated confidentiality and security concerns. There might also be data protection issues if the data is stored overseas. And of course if the service provider fails, your business could suffer. So backup and redundancy have to be built into any cloud computing arrangement.

Savings through outsourcing

Cloud computing is just one example of the increasingly popular trend towards outsourcing, which can often result in substantial cost savings. Well planned

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outsourcing can also result in greater efficiency and productivity because the business's key resources are focused on its core activities. New and growing businesses often find that directors spend too much time 'running the business' and not enough time doing what the business was set up to do. Outsourcing non core functions to agencies that have the skills and resources to execute them efficiently and in a cost effective manner can help redress this balance.

Areas that are frequently outsourced include:

- IT
- HR
- finance
- PR
- payroll
- sales and marketing
- health and safety

But outsourcing also has its drawbacks. Besides the potential for losing a degree of control over certain processes, and the possible associated risks to both your internal efficiency and external reputation, there can be problems with managing relationships with the third party agencies. This can be time consuming and take up resources that outsourcing was supposed to free up.

However, outsourcing is now very popular and clearly many businesses are finding ways to make it work to their advantage. Making outsourcing work is largely a matter of being clear from the outset about what you want to achieve and agreeing specific, measurable goals.

Cut back the creepers

Business costs tend to creep up almost unnoticed through the year, so it is worthwhile to arrange regular reviews of your fixed costs. Almost certainly you will find ways to cut them back. Some businesses set a target of a certain percentage reduction each year to offset these natural increases, and although this might not always be achievable it does help to develop cost consciousness in the business and keep cost control higher up the agenda.

Reducing labour costs

For many businesses, labour is the biggest cost centre. Unsurprisingly it is one of the first ports of call when savings have to be made. Also not surprisingly it is one of the areas where short term savings come back to bite, and may even have long term detrimental effects on the business if they are not well considered.

It is especially important to avoid cuts that might leave you without key human resources or at a competitive disadvantage when the economy improves or market conditions change. It is equally important to avoid measures that undermine the morale of the remaining workforce.

Some areas where savings might be made without staff reductions are:

- flexible working
- teleworking, especially when combined with cloud computing
- smart recruiting
- improving employee retention

Suppliers and the ordering process

The ordering process can sometimes be a source of unnecessary costs. This might happen, for example, if:

- you are dealing with too many suppliers
- there is no clear ordering policy or guidelines
- ad-hoc ordering is allowed
- ordering is not centralised
- there are insufficient internal controls against mistakes and/or fraud

Reducing the number of suppliers you deal with can often result in savings, especially if it gives you the opportunity to improve relationships with the remaining suppliers and negotiate lower prices or better payment terms.

Other possible savings

It can also be helpful to look at:

- major sources of repeated error or rework
- excessive stock

Tax and financial

This is an area that requires constant review, especially:

- debt servicing costs
- credit control
- tax efficiency

Strategic savings

On a larger scale, joint ventures, mergers or acquisitions can also result in considerable cost reductions.

Simple cost savings that won't hurt

- regularly review utility contracts
- make sure you are not paying for more insurance than you need
- cut down on paper and print
- consider leasing rather than purchasing
- buy second hand where appropriate
- pool resources such as office space
- join/create purchasing co-operatives
- purchase basic supplies in bulk
- watch the thermostat

How we can help

This is a vast topic and we have only touched on a few key points here. These are all areas where we can provide help and advice.

Examples of the kind of help and advice we can provide are:

- conducting a detailed analysis of cost structure, cost drivers etc, and identifying potential savings
- improving tax and financial efficiency
- budgeting, planning, forecasting
- improving internal controls
- advice on change management

Why not contact us for an initial review to see how we can help you with your cost reduction strategies?

