

How to cut your costs

Almost every business goes through the annual ritual of budgeting for, or forecasting, its sales and expenses over the next year. Unfortunately this ritual often misses a golden opportunity. Used properly, budgets are not only useful for monitoring performance, they can actually help to *reduce costs*.

It is important to be crystal clear on one thing, though. A budget that merely takes last year's figures, and adds a percentage for inflation will *not* help to reduce costs one bit. The only way that budgeting will reduce costs is if every cost has to be justified from *first principles* before it is allowed to be included in the budget.

What do we mean by "first principles"?

You and your team will have to answer the following questions about every single element of your business's cost base:

- Can it be eliminated without significantly damaging the business's profitability?
- Is it over-specified for the needs of the business and could the specification be trimmed to save costs? i.e. are you using a Rolls Royce when a Mini Metro will do?
- Does it cost more than the benefit it delivers?
- Can the same outcome be achieved more cheaply in some other way, perhaps by changing company procedures or by installing a new computer etc?
- Can it be done more cheaply by an outside sub-contractor?
- Is there a way of paying for it in kind rather than in cash?
- Can it be done less frequently without harming the business?
- How do other businesses achieve the same outcome?
- If you were to start in business again, would you still decide to incur this type of cost?
- Is there any duplication of effort, and can the task be combined into one already carried out elsewhere in the business?
- Is somebody responsible for the cost? How do they go about discharging that responsibility?
- When was the last time competitive price quotes were obtained? Has the choice of supplier become a matter of habit and convenience rather than sound economic sense?

Although these questions should be asked about all of your costs, it probably makes sense to concentrate initially on your largest costs. After all, the larger the costs, the larger are the potential savings.

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