CORE®

Technology-driven Cost Optimisation

Navigating a path through recession & going lean

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March 2023
Blogpost

Public

Key Facts

- According to a recent C-Suite Gartner survey:
  - 90% of CEOs expect persistent high inflation, with supply chain disruption and reducing consumer setiment will put downward pressure on profitability
  - 69% of CFOs believe non-labor input costs will rise significantly
  - 47% of CFOs report that it‘s difficult to find and hire enterprise talent. Retention and cost of ‘in demand’ skills is a major challenge.
  - 48% of CFOs believe supply chain volatility and shortages will last beyond 2022

- Three cost optimisation approaches are available, based on CORE’s experience, each one growing in scale of value:
  1. 5-10% IT cost reduction – Cost Cutting Approach – Return 1-6 months
  2. 10-25% IT cost reduction – Technology Transformation – Return 6-18 months
  3. 25-50% IT cost reduction – Strategic Transformation – Return 12-24 months

- Three case studies are being explored covering each of the optimisation approaches, using CORE’s five step optimisation methodology. The Cost Cutting case study within financial services completed an analysis that:
  - Identified 8 tangible levers for cost optimisation
  - Documented, measurable and traceable action-based plan spanning an 8-year horizon
  - Resulting in a forecasted reduction of 11% in operational costs worth €19m to €52m

The case for cost-optimisation and technological transformation

Businesses are facing major challenges in navigating the current economic environment, characterised by diminishing margins, high inflation, supply-chain disruptions, high political uncertainty and economic volatility. A recent Gartner survey with CEOs and CFOs has reinforced this sentiment (see Exhibit 1), drawing attention to overdue restructuring.

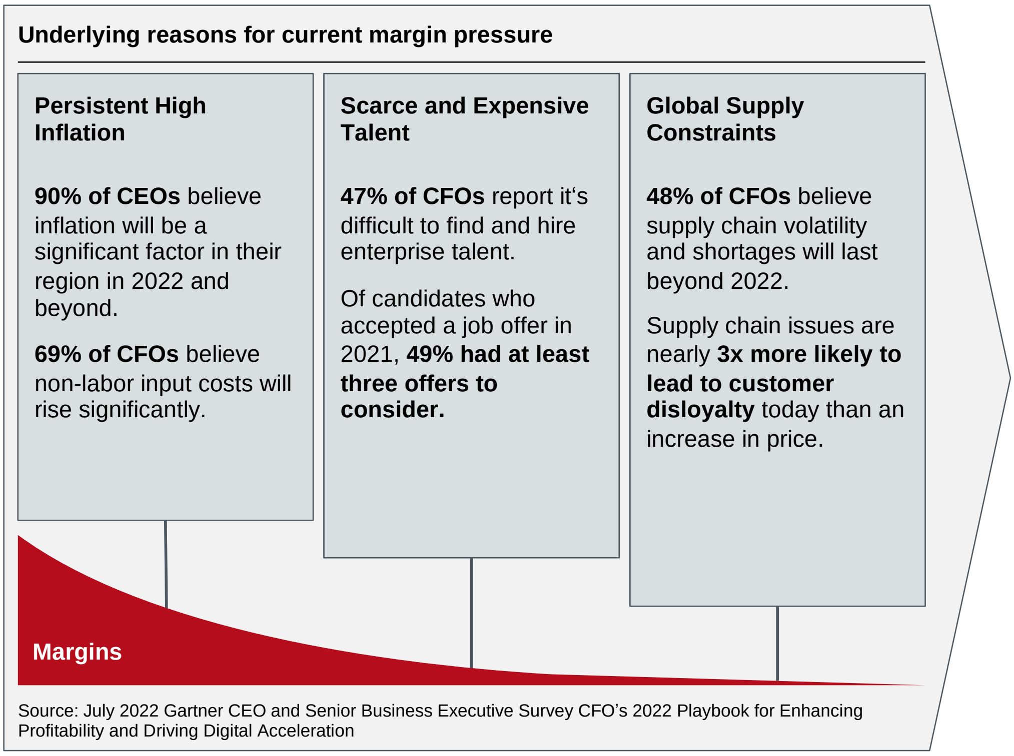

Exhibit 1: Underlying reasons for current margin pressure

According to the Gartner survey, the significant majority of the C-suite surveyed believe persistent high inflation is one of the main factors affecting business profitability in 2022 and beyond**,** whilst 69% of CFOs believe non-labor input costs will rise significantly. Higher inflation often results in reduced customer demand and revenue.

Scarce and expensive talent is another key factor affecting businesses' margins. 47% of CFOs report that it's difficult to find and hire enterprise talent, whilst of the candidates who accepted a job offer in 2021, 49% had at least three offers to consider. Retention and cost of 'in demand' skills is a major challenge.

Thirdly, global supply constraints is another cost-centre. 48% of CFOs believe supply chain volatility and shortages will last beyond 2022, whilst supply chain issues are nearly three times more likely to lead to customer disloyalty today than an increase in price. Unresolved, supply chain disruptions can cause customer delays, increased sourcing costs due to scarcity of raw materials, and certainty risks.

Selecting the right cost-optimisation approach

In order to combat this multi-faceted pressure businesses should prioritise cost-optimisation efforts and technological and business model transformation to offset mounting pressures on profitability and unlock growth opportunities. Three typical approaches are available to management depending on the end business ambition, with varying complexity and expected time to realise the results (see Exhibit 2). CORE has deep experience of each optimisation approach whether it be option 1 that is highly tactical, with quick returns, although the longer term sustainability can be compromised, vs more strategic and logically planned transformations where the entire business model is re-engineered.

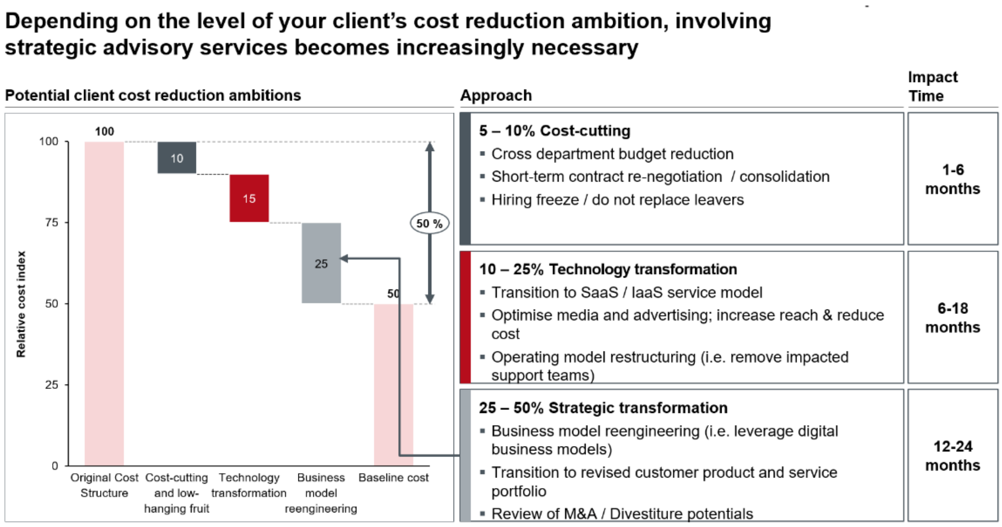

Exhibit 2: Typical options for cost reduction

Approach 1 – Cost Cutting – Typical yield 5-10% reduction. Return 1-6 months

This option is pursued when immediate results are preferred. Measures to achieve this option include reduction of the current cost structure to ensure sustainable market positioning and increased innovation investments. Tends to lead to short term gain, without a great deal of focus on the long term survival of the organisation. Notwithstanding the perspective of short-term benefits, a number of risks are intrinsically linked to this approach:

- Loss of competitive advantage, if direct competitors do not engage in similar cost-cutting efforts
- Significant moral issues
- “Brain drain”
- Does help mitigate symptoms but does not address underlying structural issues

Approach 2 – Tech. Transformation – Typical yield 10-25% reduction. Return 6-18 months

This option would be progressed if the business intends to upgrade or replace legacy systems and improve its competitiveness in the medium-term e.g. shift from on-premises to API, Cloud Native, automation first and outsourced service models. Measures to achieve this option include:

- Shifting from physical to online strategy; digital and technology first
- Focusing on customer, supplier and service automation standardisation of internal processes to drive faster scale at lower cost
- Establishing of a platform and outsourced technical ecosystem to aid faster time to market and revenue or profit
- Installing of digital channel ways of working to drive cheaper costs of customer acquisition, retention and referral

Approach 3: Strategic Transformation Typical yield 25-50% reduction. Return 12-24 months

This option is always required to maximise competitiveness and resilience in the long-term. Measures to achieve this option include business model digitalisation, product portfolio upgrades, and review of M&A and divestiture potentials.

This blogpost will deep-dive into one of the client case studies who pursued the cost-cutting option.

Client Case Study – Cost-cutting in the banking industry

A client in the banking industry outsourced their infrastructure services to an external service provider under a complex contract structure that seemingly locked them into a commcerially disadvantageous position. Given that the outsourcing contract accounted for ca. 75% of the client's yearly cost, any significant run rade reduction would see significant bottom-line impact. CORE was hired to identify potential levers within the existing legal framework (no renegotiation) to effectively reduce the total cost of operations.

The project was carried out in three stages: first, the correct TCO baseline was established, detailing which costs were incurred due to purchased services under the outsourcing agreement and which costs stemmed from in-house operations. Second, potential measures were identified and qualified with the client's operational management. Third, the financial savings potential of each measure was quantified and the respective implementation effort was estimated, yielding a prioritised list of actionable levers as final project result.

Ultimately, three optimisation themes were identified 1) Commercial, 2) Legal and 3) Organisational, with a total of eight specific opportunity levers. They added up to a potential 11% cost reduction over the course of eight years with savings ranging between €18.8 million and €51.7 million (see exhibit 3).

Based on the classification above, this project falls into the "cost cutting" category. Thus, further strategic optimisation potential was highlighted to the client as a result of the engagement, as well as a number of key risks that were identified along the way.

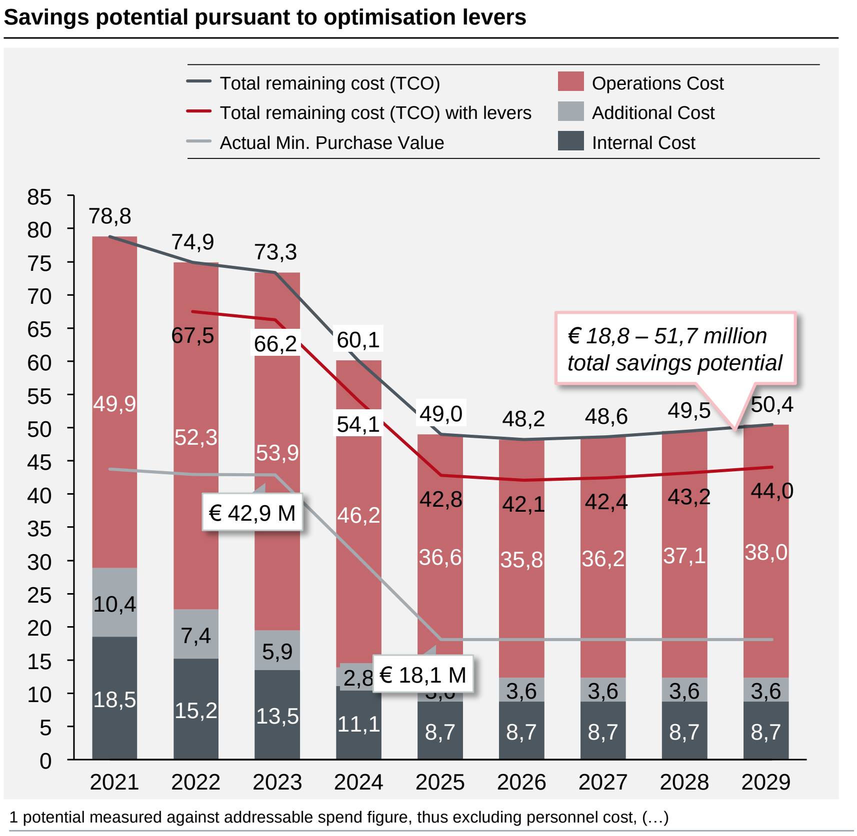

Exhibit 3: The client's forecasted cost savings potential over the following 8 years

CORE approach to tech-driven cost-minimisation

CORE has extensive expertise in technology driven cost-minimisation projects. The typical roadmap for cost-optimisation short-term projects consists of five stages in CORE's approach (see Exhibit 4). The activities and deliverables per stage are outlined below.

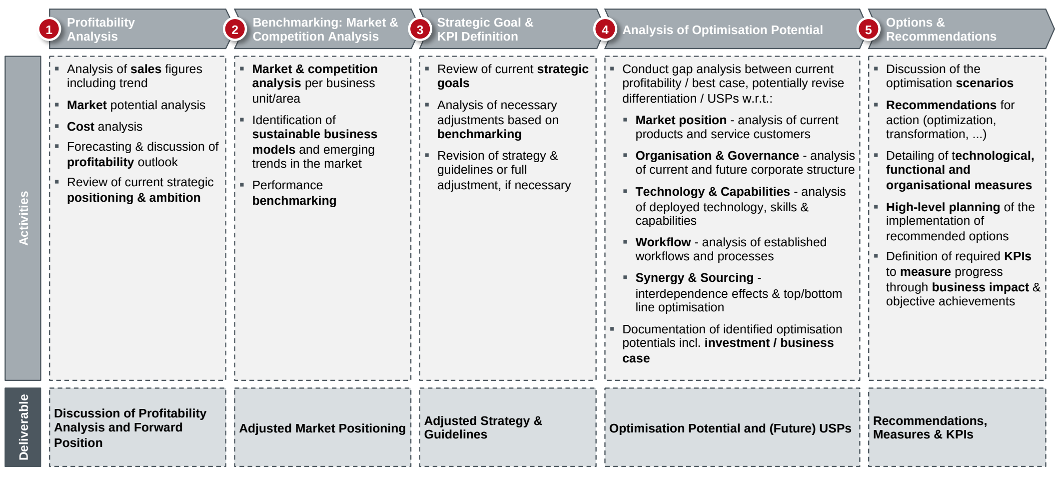

Exhibit 4: Typical short-term tech-optimisation roadmap

1 – Profitability Analysis

First, the analysis of the client's status quo is conducted to assist corporate leaders in determining how to maximize profitability given the proposed initiatives, plans or products. Activities include analysing sales, trends, costs, and market potential. This results in a comprehensive profitability analysis to enable a better understanding of the current and future market position.

2 – Benchmarking: Market and Competition Analysis

Building on the first stage, it is essential to understand the competitive landscape and identify market opportunities to formulate winning strategies. Activities include analysing the market and competition landscape, identifying sustainable business models and emerging trends, and benchmarking performance, to help clients clarify their market positioning for profitable and sustainable growth.

3 – Strategic Goal and KPI Definition

Next, the existing strategic goals and KPIs must be aligned with the proposed optimisation roadmap for accurate measurement of outcomes and a forward-focused vision. Activities include reviewing current strategic goals, analysing the necessary adjustments based on benchmarking, and revising the current goals and KPIs, to deliver an adjusted strategy and guidelines.

4 – Analysis of Optimisation Potential

At this stage, a 'best case scenario' can be formulated to understand the best potential outcome of the client's cost-optimisation transformation and identify the actions needed to achieve it. Activities include conducting a gap analysis between current profitability and 'best case scenario', and documentating identified optimisation potentials, to map the optimisation potential and (future) USPs.

5 - Options, recommendations and execution support

Finally, decisions can be made on the choice, implementation, and measurement of the suggested optimisation options. Actions include discussing the recommended optimisation scenarios, detailing the technological, functional and organisational measures, planning the implementation at a high-level, and defining the required KPIs to measure progress. The deliverables are the recommendations, measures and KPIs.[1]

[1] *CORE SE services offered, key corporate characteristics, locations, integrated model, and for further information of detailed approach, please contact Dr. Philipp Kleine Jäger or Alistair Bennett.*

Conclusion

With interest rate and inflationary pressures expected to last until late 2023, now is the time to define a clear optimisation strategy. From short term cost cutting, to longer term technology and strategic transformation approaches available, leaders need to have clarity of how they will remain viable.

CORE has extensive experience with a suit of cost optimisation strategies, using a proven approach and highly skilled talent to define and deliver the optimisation option that is best suited to each of our clients.

Our approach follows five distinct and parallel activities:

1. Profitability analysis
2. Benchmarking: market and competitor
3. Strategic Goal and KPI definition
4. Optimisation Potential Analysis
5. Options, recommendations and execution support

The work typically takes 2-4 weeks to complete and will provide an actionable plan that can be used to drive the desired outcomes. Whether they are short term for tactical cost cutting, or longer term in the case of technology or strategic transformation.

Sources

Exhibit 1: Underlying reasons for current margin pressure

Source: July 2022 Gartner CEO and Senior Business Executive Survey CFO's 2022 Playbook for Enhancing Profitability and Driving Digital Acceleration

Exhibit 2: Typical options for cost reduction

Source: CORE SE

Exhibit 3: The client's forecasted cost savings potential over the following 8 years

Source: CORE SE

Exhibit 4: Typical short-term tech-optimisation roadmap

Source: CORE SE

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