

Expense Problems?

Our President, Ron McDonald, had a grandfather who came from Scotland. As you might expect, he was very frugal. His advice to Ron on effective expense management was summed up in the following old Scottish saying, "If you hand someone a penny and he can't see your fingerprint on it, you haven't considered the transaction."

While this may seem a little extreme to some, the basic point of this saying is valid. Managing expenses is something that every person and every company must pay attention to, all the time. It's easy to let this focus slip and, when this happens, you can pay a terrible price.

But even under the best of management and circumstances, every once in a while you can find yourself with a serious expense situation that must be fixed. Over the years we've helped a number of clients with this problem. Here are some thoughts you might find worthwhile.

The first step, of course, is get a clear understanding of the scope or size of your expense problem and if it's located in specific areas of the company or is a more general problem. Sometimes this is easy to do. Using industry comparisons and your own past experience for your company can be very useful. If this isn't adequate, there are a couple of things you can do that will help. Two of the most useful are:

You can do an expense allowable analysis. This is a study that identifies the expense level that your current product pricing allows you to have and still meet all of your financial goals. Doing this for the overall company is useful but the real value comes when you expand this analysis to determine the expense allowables for each of your major departments. You can then compare these numbers to your actual results for each department. This Gap Analysis will identify and quantify your problem(s).

For a more complete explanation of how to conduct this type of study, please go to the [Ideas and Concepts](#) section of our website at "McDonaldConsultingGroup.Com". Read our letter dated August, 2002, entitled [Is It time To Move To Expense Allowables?](#)

Once you've done this study, you'll want to keep it up to date. It's easy to do and is a great tool for budgeting, planning and overall expense management.

If a significant part of your expense problem is in your operational areas, you probably either don't have or haven't been using staffing models. We've talked about staffing models in the past. They are interactive computer models, based on your own work processes, that tell your operational areas how many and what type of people they need to do your current work.

Since your employees are by far the most significant expense in these departments, this is almost always something that needs to be addressed. Staffing models are also another very important on-going management tool. They will not only be effective in identifying your expense problem and the solutions you need to implement, they will help you stay out of trouble.

After you have a good understanding of your expense problem, the next big decision is to determine if your best solution is to attack your expense problem directly or if your expense problem is a part of an even larger problem that needs to be addressed.

Let's look at the easier of the two alternatives. Let's assume you just have an expense problem. Most likely, there are some departments that have a bigger problem than others but you probably still have an overall, company wide problem with expense bloat. The best approach to fixing this is to do an analysis of each area, focusing on how to change the way they do their work, to create the improvements and efficiencies needed to lower expenses.

Do not just focus on reducing expenses. This almost always results in temporary cost reductions that quickly return when the heat is off. Instead, focus on identifying the improvements that will create the best overall results; improvements in customer satisfaction, quality, timeliness, persistency and retention and sales growth as well as identifying new efficiencies and reducing expenses. Having expense allowables and staffing models are a big help in this effort.

Be careful that you don't have other, larger problems that also need to be fixed. For example, it would be a big mistake and very demoralizing to have everyone go through a process to downsize to fit your current revenue stream, only to have sales dramatically increase shortly thereafter.

Examples of these larger problems are:

- A significant part of your expense problem is caused because of problems with sales and revenue growth. The best solution would fix all three of these at the same time.
- Expenses are only a part of your overall business problems. You are also having problems with loss ratio, retention and persistency, customer satisfaction, growth, etc. Again, this is a situation for an effort that addresses all of these problems simultaneously, and your solutions will generally cross departmental lines of authority.
- You have a systemic problem. Tweaking the way you do things will not produce the results you need. You need to change the way you do business or make other basic changes to your infrastructure.

Tackling these larger problems always produces bigger results. This makes sense. The broader the scope of the effort, the larger the benefits you will receive. But they also require more effort, take longer to accomplish and affect more people. We call these projects fundamental change efforts because of their focus and the results they achieved. The best results are always attained with the help of a management consulting firm that specializes in these types of efforts. Mc Donald Consulting Group is one of these firms. We would be happy to guide you through this type of effort.

Regardless of the approach you take to solving your problem, do something. Expense problems don't fix themselves. On the contrary, if they are ignored they always get worse. Solving your problem now always takes less effort and produces better results than waiting. Also, avoid incremental changes. Nibbling at a problem is just another way of avoiding or ignoring it. Instead, look at it as an opportunity – an opportunity to create the improvements that may mean the long term difference between your company's success or mediocrity or worse.

In our management consulting practice we help companies with all of the solutions mentioned in this letter. It is why we were created and what we do. Please visit our website (McDonaldConsulting-Group.com) if you want to learn more about our firm.