

WEBINAR PRESENTATION

Overhead Optimization

From Cost Center to Competitive Advantage

July 31, 2007

Today's speakers are leaders in the Booz Allen Overhead Optimization Team



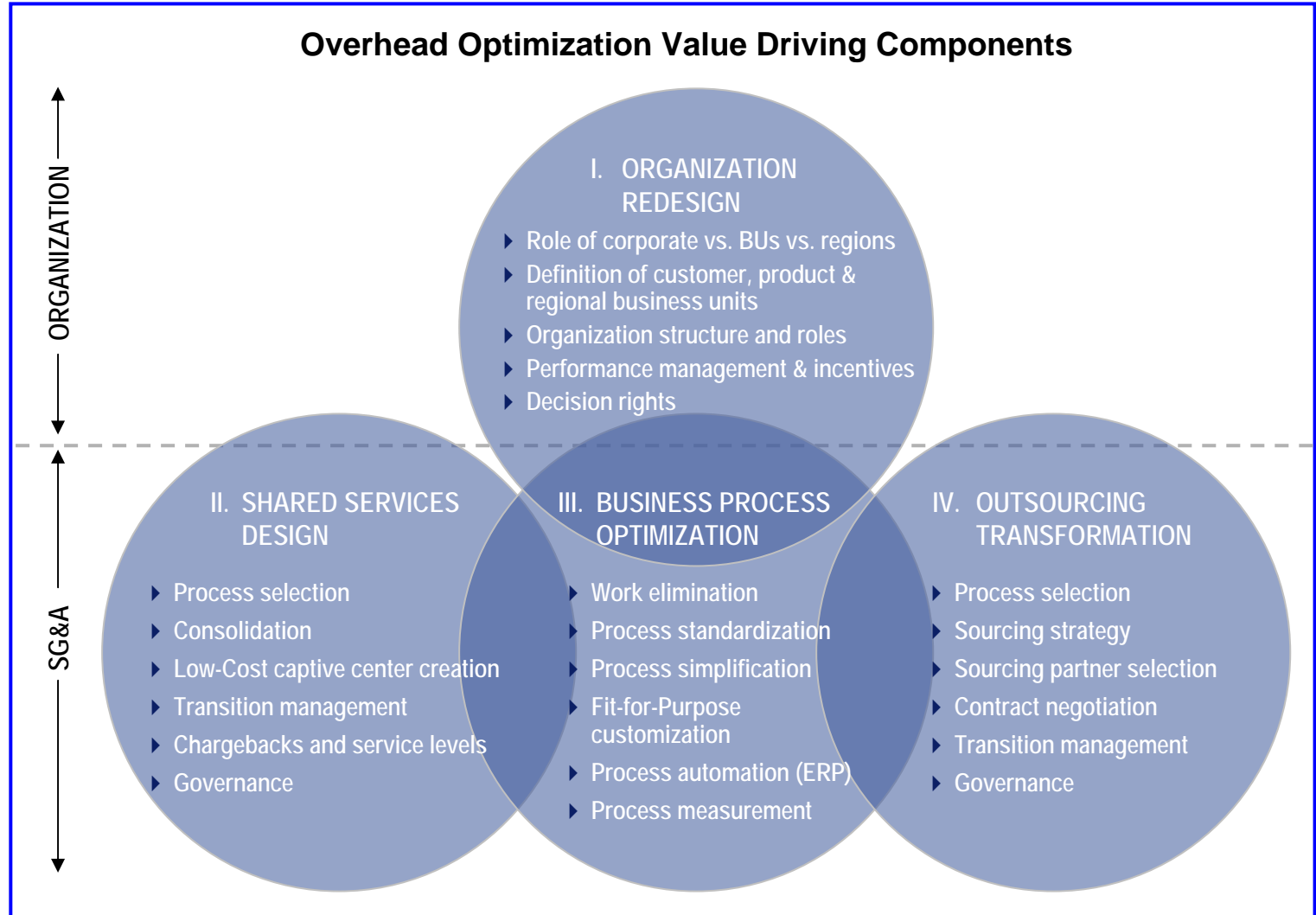
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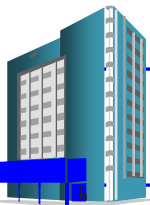
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Overhead Optimization tackles a breadth of functions and has four major value-driving components

Scope
Finance
HR
Purchasing
Facilities
Legal
Technical Functions (Quality, Mfg Planning)
Customer Management
Communications
Sales and Marketing

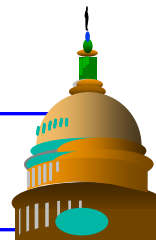


Our clients often wrestle with issues centered around organization efficiency



Commercial Clients

- ▶ Disproportionate growth in **organization costs** relative to revenues
- ▶ Right-sizing overheads in response to **divestitures or major revenue drops**
- ▶ Achieving **post merger integration synergies**
- ▶ **Globalization** into emerging markets and desire to leverage offshore
- ▶ **Renegotiation** of outsourcing contracts
- ▶ **Talent shortage** in developed countries
- ▶ Achieve **scalability** in business models



Government Clients

- ▶ **Expense reduction challenges** while increasing management efficiency & mission fulfillment
- ▶ Business process and technology **modernization programs**
- ▶ **Outsourcing contract re-competes**
- ▶ Compliance with Administration priority regarding **government wide lines of business**

In Booz Allen's view, organizations capture greater efficiencies from their Overhead when they address structural issues

Re-assess How Well It Is Done

Redefine How It Is Done

Challenge What Is Done

Increasingly Senior Decisions

Organization Leanness

Delay and flatten the organization to cut cost and spend decision making

Process Optimization

Redesign core cross-functional processes from the customer back and optimize end-to-end performance"

Best Practice Transfer

Identify internal practices and disseminate through the enterprise

3 Shared Services

Consolidate and automate like work into transaction service centers or expertise centers to achieve scale and scope synergies

4 BPO and Offshoring

Leverage scale, technology and competitive factor costs of third parties to achieve cost variability and efficiency

1 Operating Model

Clarify the role and decision rights of Corporate vs. Business Units

2 Demand Management

Motivate users of services to reduce consumption or make informed cost-value tradeoffs on what to customize and what to standardize

G&A COST SAVINGS OPPORTUNITY

5-15% *Most organizations only focus here, and miss significant value*

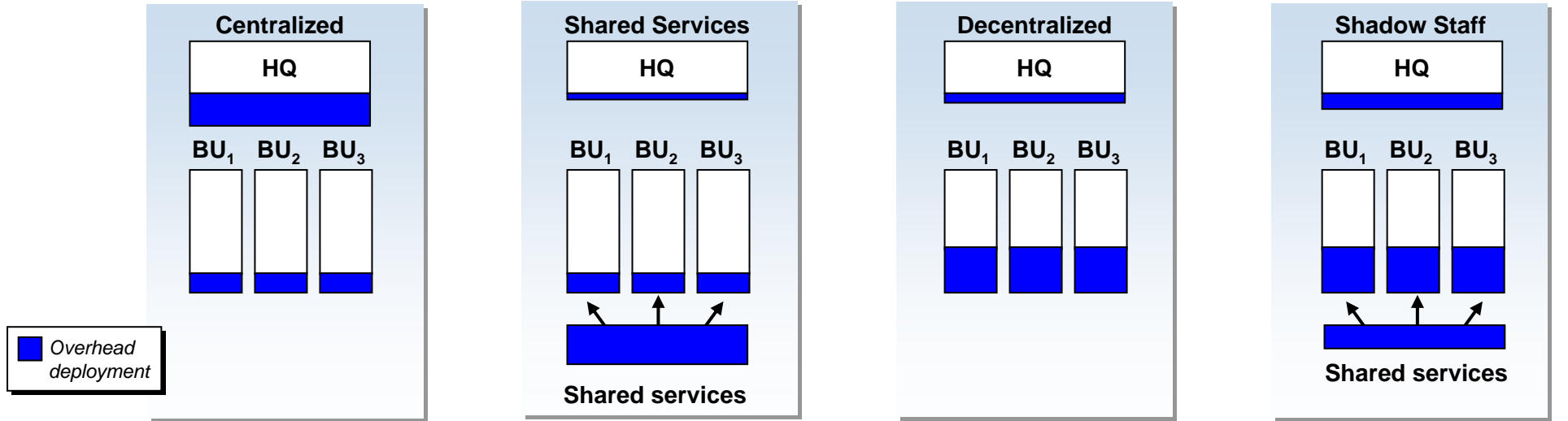
15-30% *Greater potential for value, but requires senior management to address overhead structurally*

20-40%

1) Operating Model

Companies frequently wrestle with organization models that balance centralized scale with decentralized control

Commonly Used Operating Models for Overhead Functions



- | | | | | |
|-------------|--|--|---|--|
| Pros | <ul style="list-style-type: none"> ▶ Scale and critical mass of expertise ▶ Common standards & controls ▶ Ability to capture best practices | <ul style="list-style-type: none"> ▶ Scale and expertise from pooling ▶ Building of capabilities ▶ Accountability for performance | <ul style="list-style-type: none"> ▶ BU autonomy & control ▶ Recognition of unique needs ▶ Responsiveness ▶ Cost transparency | <ul style="list-style-type: none"> ▶ BU autonomy & control ▶ Pockets of best practice ▶ Pockets of common standards |
| Cons | <ul style="list-style-type: none"> ▶ Remote from BUs ▶ Intolerable to BU needs ▶ Inadequate control over service usage and costs | <ul style="list-style-type: none"> ▶ Loss of BU autonomy ▶ Standardization ▶ Inability to respond quickly to changing business conditions | <ul style="list-style-type: none"> ▶ Duplication ▶ Variable standards & controls ▶ Sub-scale processes & systems | <ul style="list-style-type: none"> ▶ Shadow staff ▶ High costs |

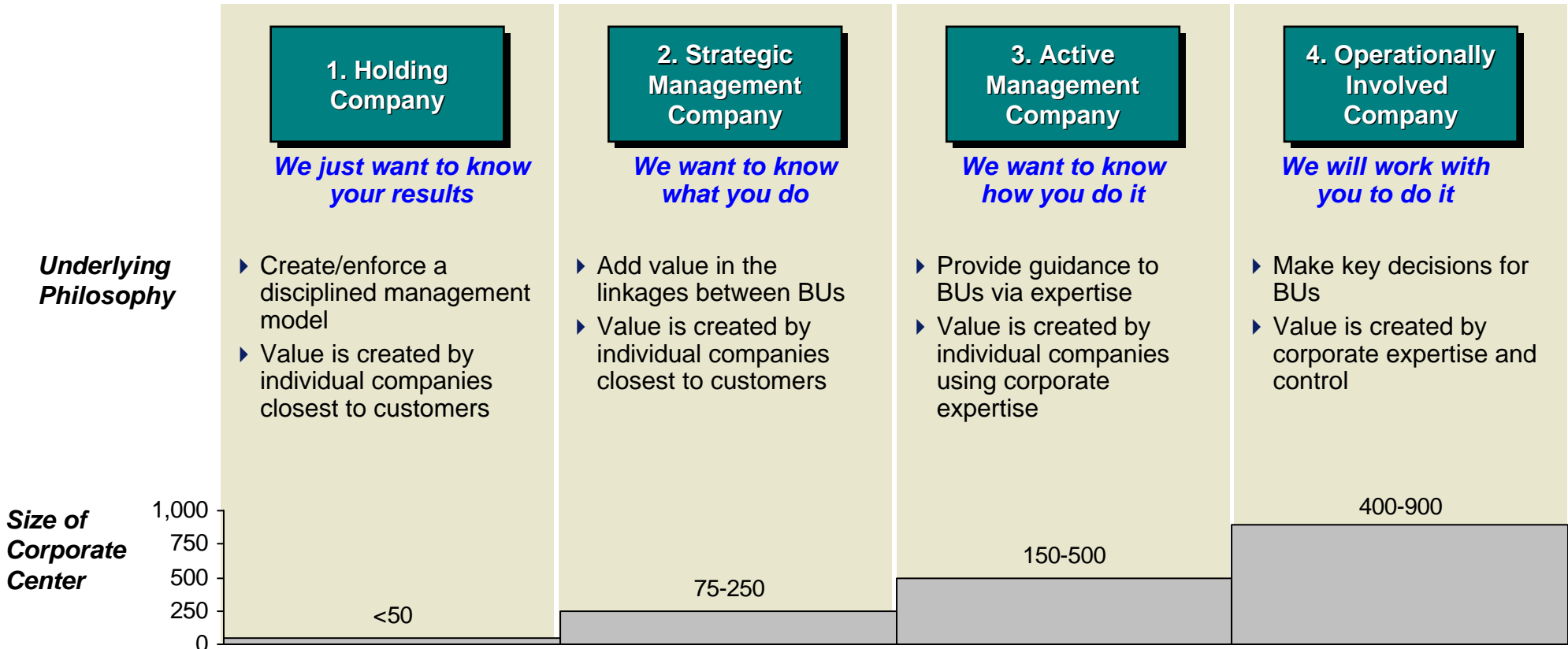
Overhead Costs



1) Operating Model

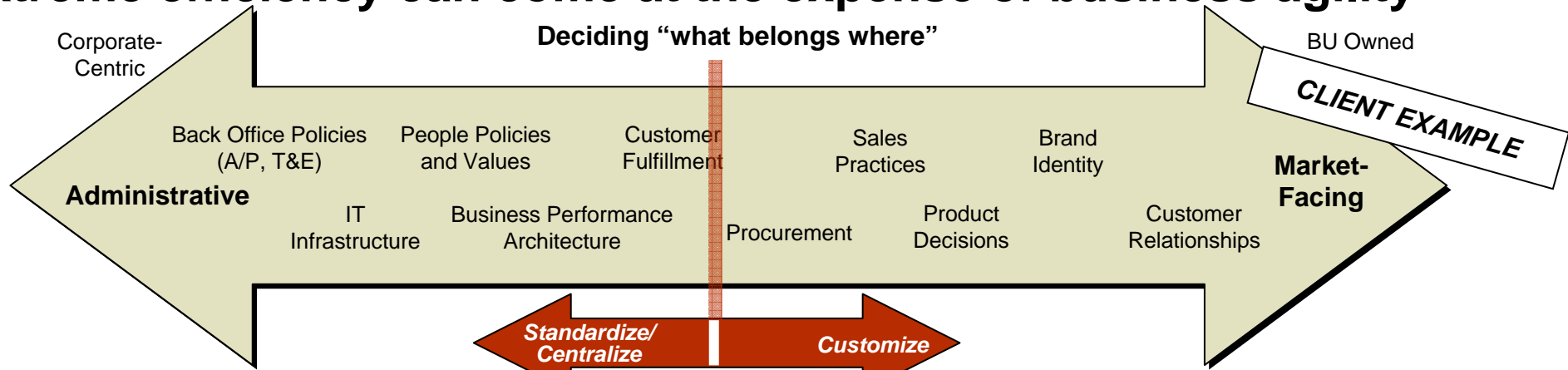
As such, organizations must consciously choose their “operating model” to define how overhead supports the organization

Range of Operating Models



1) Operating Model

Choice of operating model will dictate cost structure, although extreme efficiency can come at the expense of business agility



- ▶ Increased BU autonomy and agility
- ▶ Lean corporate center
- ▶ Greater cross-BU complexity
- ▶ Higher support costs
- ▶ More "Model 2"

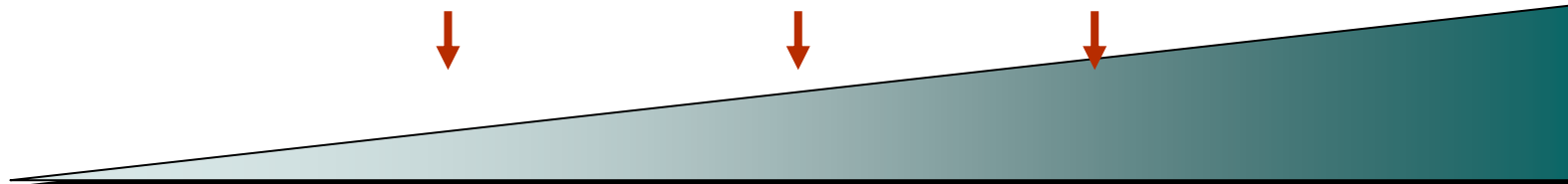
- ▶ Increased scale economies and lower costs
- ▶ Larger corporate center
- ▶ Reduced local agility and flexibility
- ▶ Fewer customized support resources
- ▶ More "Model 3"

G&A Savings Capture (est.)

\$20MM
Model 2

\$40MM
Model 3A

\$100MM
Model 3B



"As-Is Organization" with improved processes

"Standardize G&A only"

"Standardize Sales, Ops, and Marketing support tools"

Organizational Structure

Applying demand management can lead to reducing or eliminating lower value services

What is Demand Management

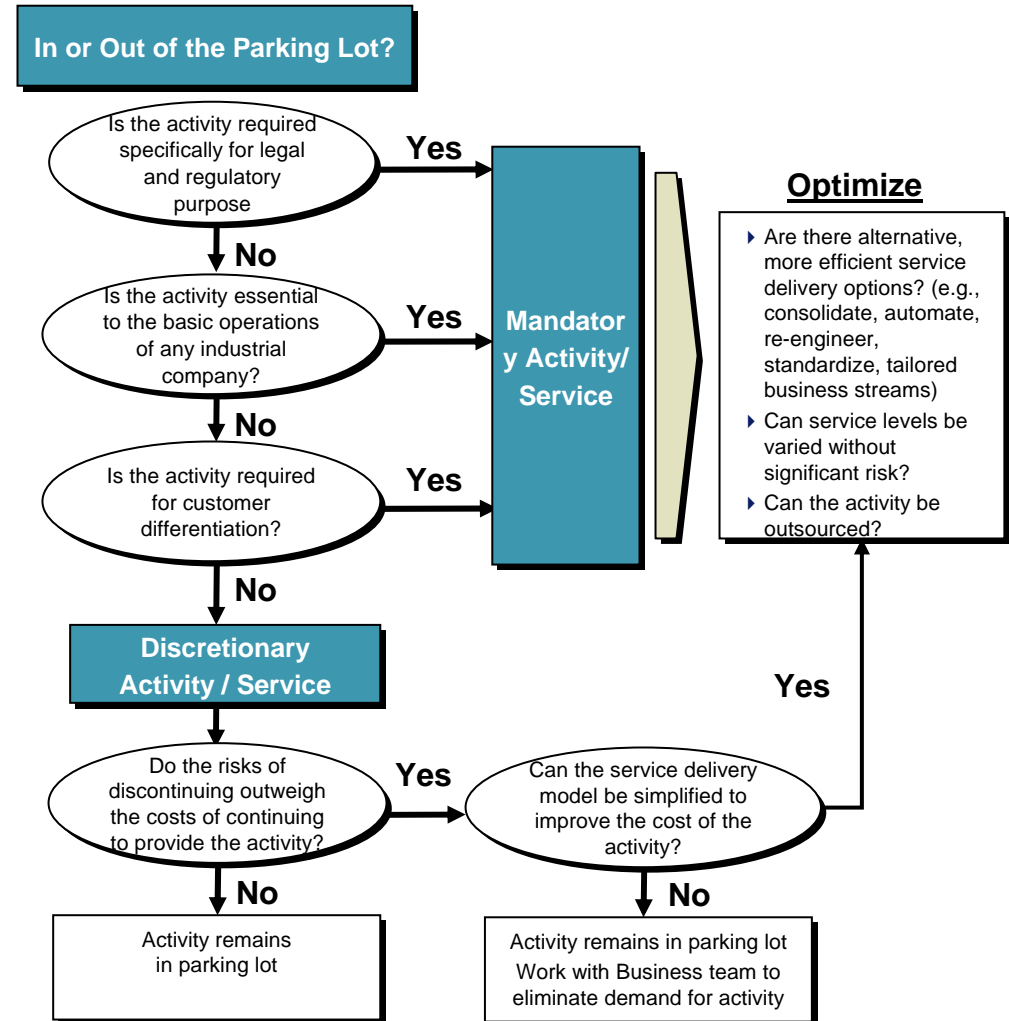
► Constrain demand

- Prioritize “musts” over “wants”
- Eliminate low value added activities
- Adjust service levels

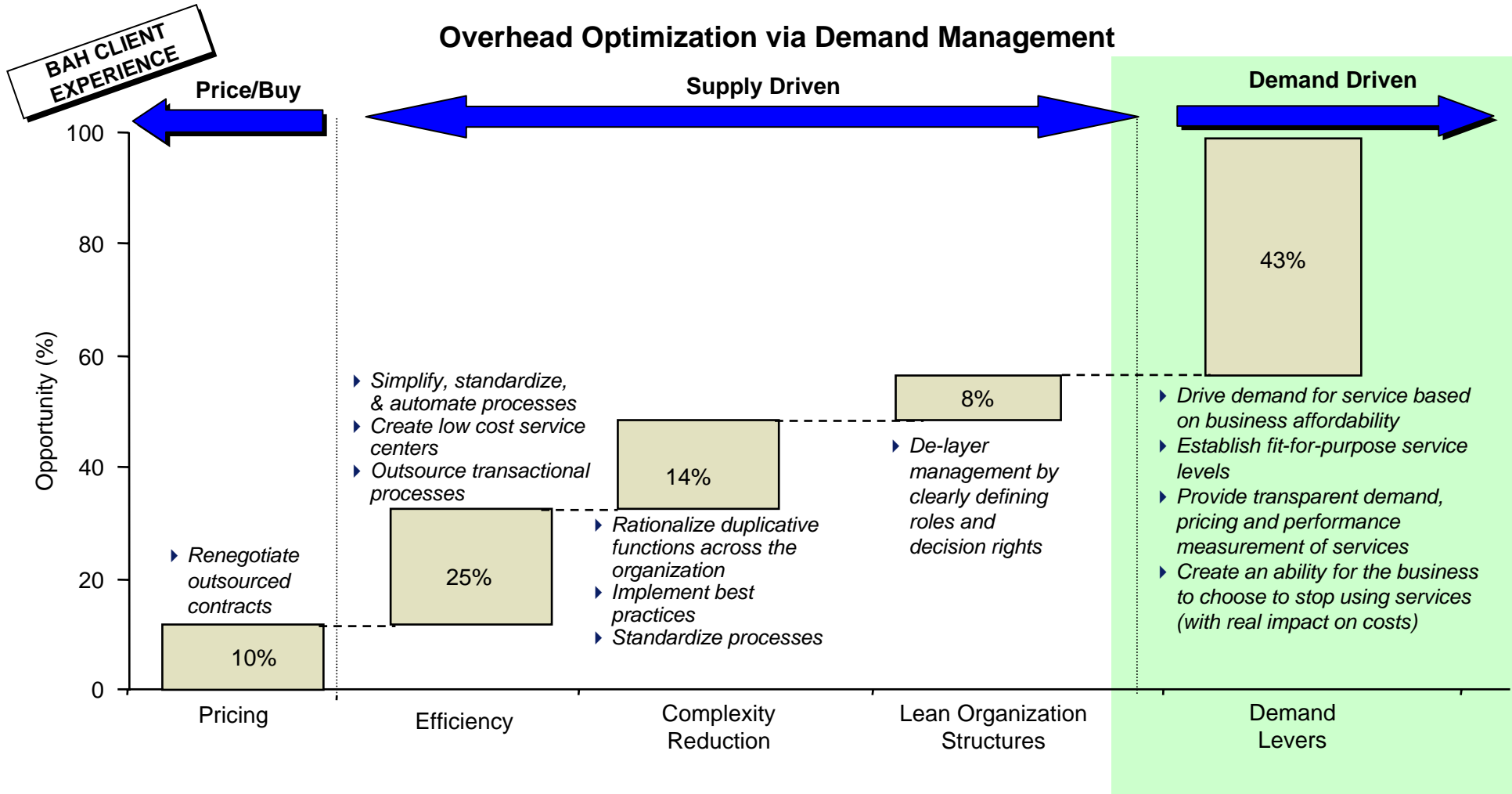
► Reconfigure services offerings, service levels, and delivery models on a tiered or “fit-for-purpose” basis

► Control the change stream—prioritize and limit discretionary enhancements

► Use market mechanisms to get the business to **optimize/reduce usage of services** or select more efficient service options



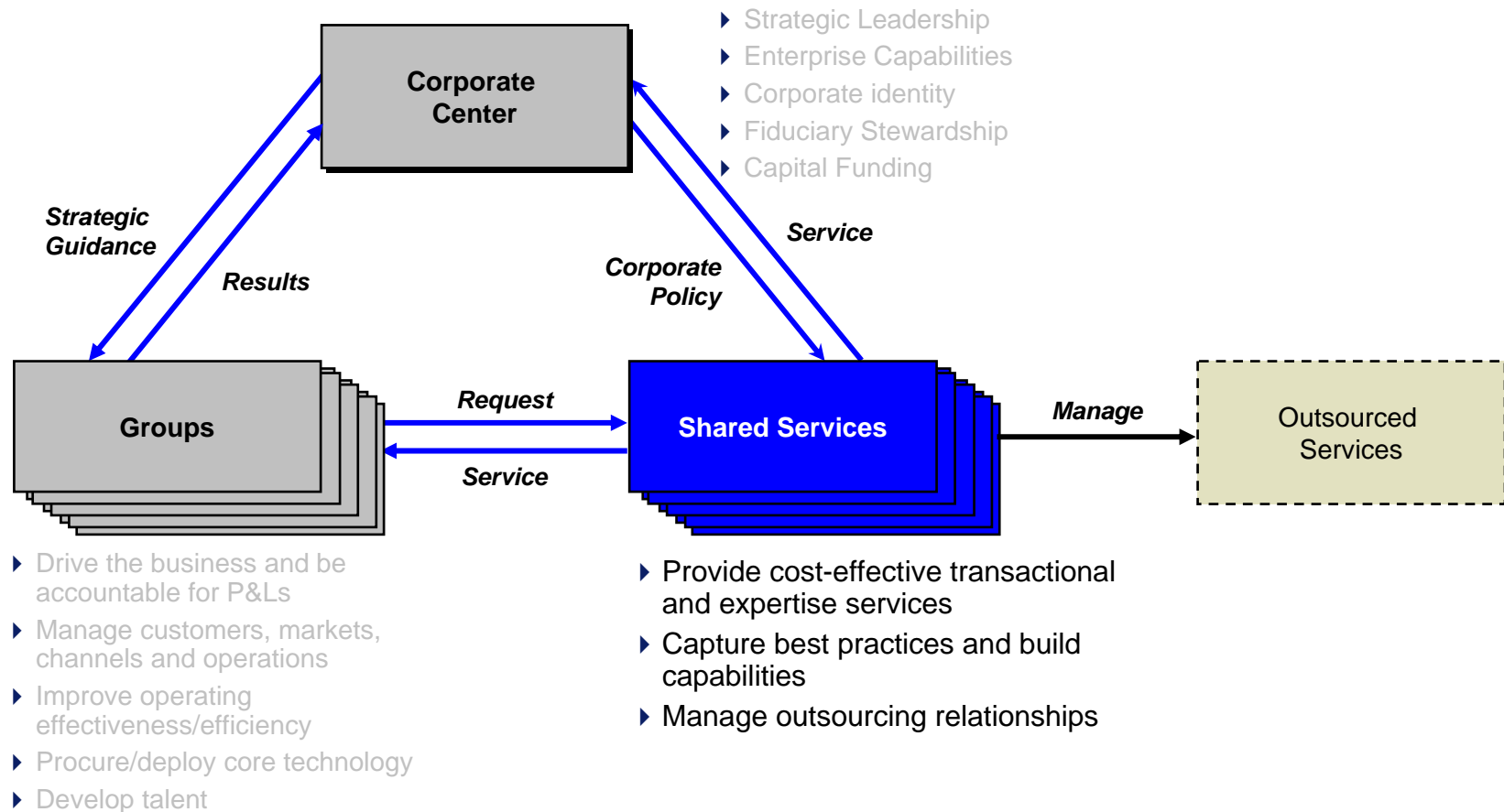
Properly applied, demand management can substantially expand the total benefits pie



3) Shared Services

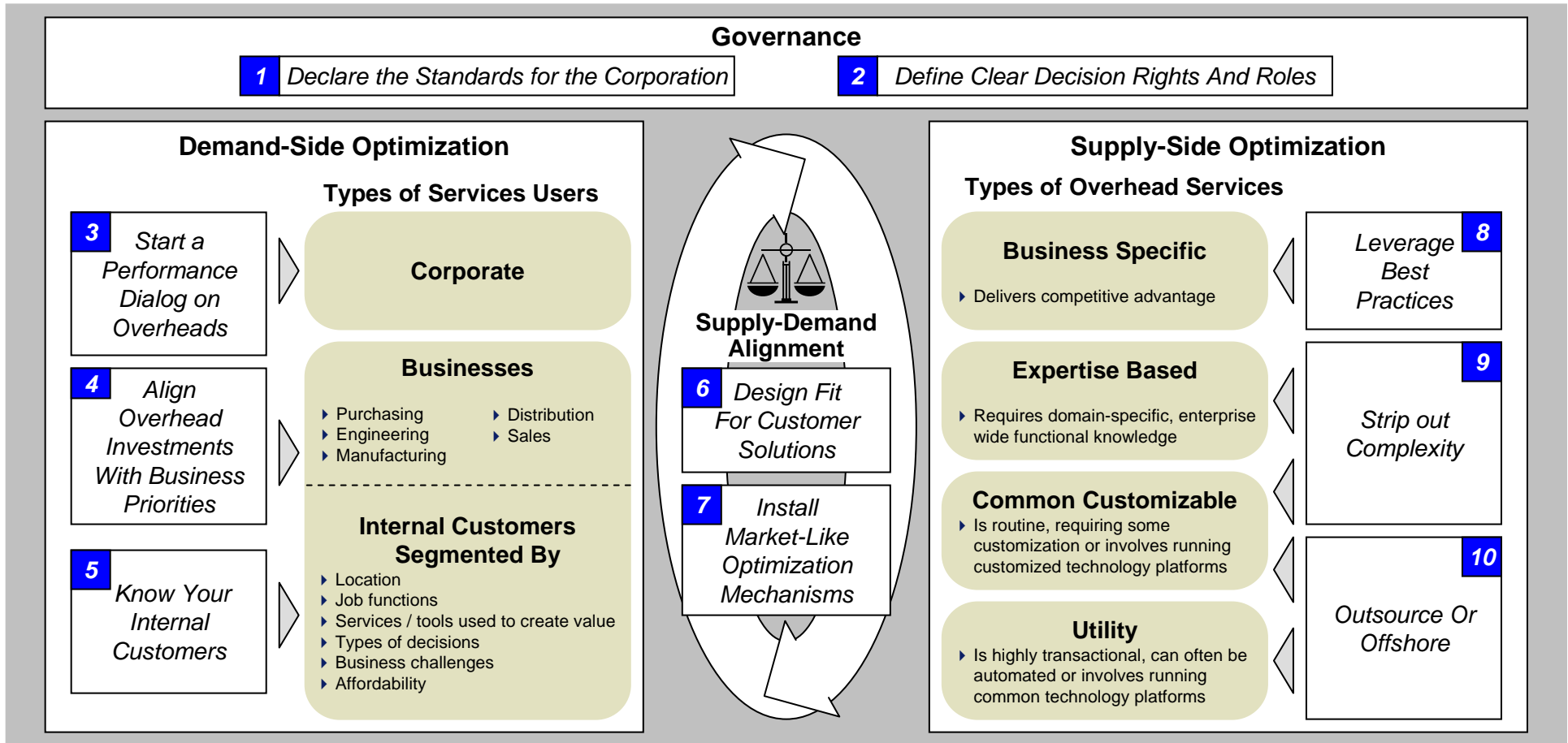
Many high performance organizations have adopted Shared Services that sharpen accountability while leveraging scale and scope

Shared Services in High Performance Organizations



Shared Services has evolved rapidly beyond simple consolidation and standardization...

Shared Services: Next Generation Improvement Levers



3) Shared Services

...and is now a mature model to manage overhead that is commonly used by corporate and divisions

Sector	Companies
Manufacturing	        
Pharma & Chemicals	        
Consumer Packaged Goods	      
Hi-Tech & Telecommunications	     
Energy & Utilities	   
Financial Services	   

4) Outsourcing

Outsourcing has become thoroughly interwoven into the business fabric of market leaders across a number of industries

Operations

- Order tracking services
- Claims processing
- Credit card processing
- Airline reservations processing
- Loan processing
- Account mgmt
- Securities processing

Marketing/Sales

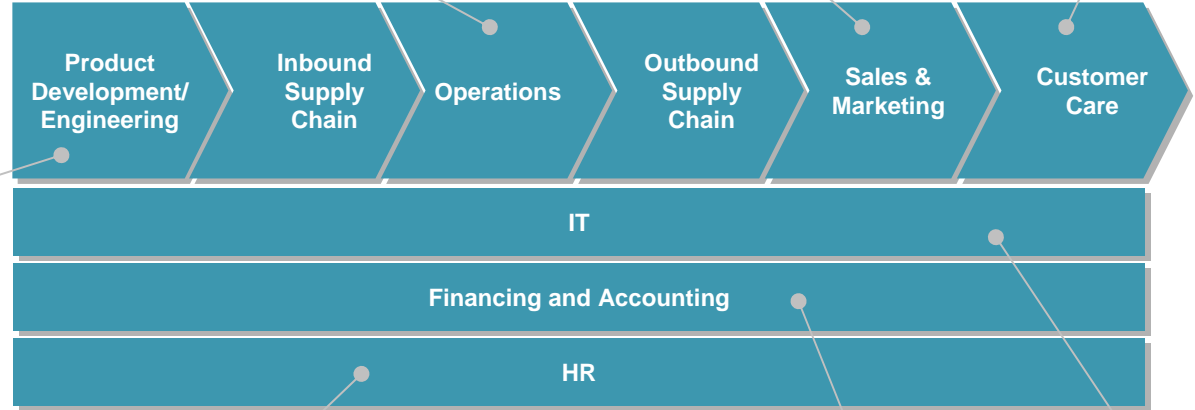
- Customer analytics
- Market research
- Outbound telemarketing
- Sales graphic design
- Loyalty program assessment

Customer service

- Customer Tier 1 support
- Advanced technical support
- Complain resolution
- Customer fulfillment
- Dispatch support
- Collections consumer & B2B

R&D/Product Development/Engineering

- Clinical Research
- VLSI design
- DSP chip design
- Avionics
- CAE
- FMEA
- Simulations
- EBom/PDM
- Graphics
- Vehicle build plans support
- Prototype development



HR services

- Payroll processing
- Employee contact center
- Benefits administrator
- Recruiting administration
- Employee data maintenance

Finance & Accounting

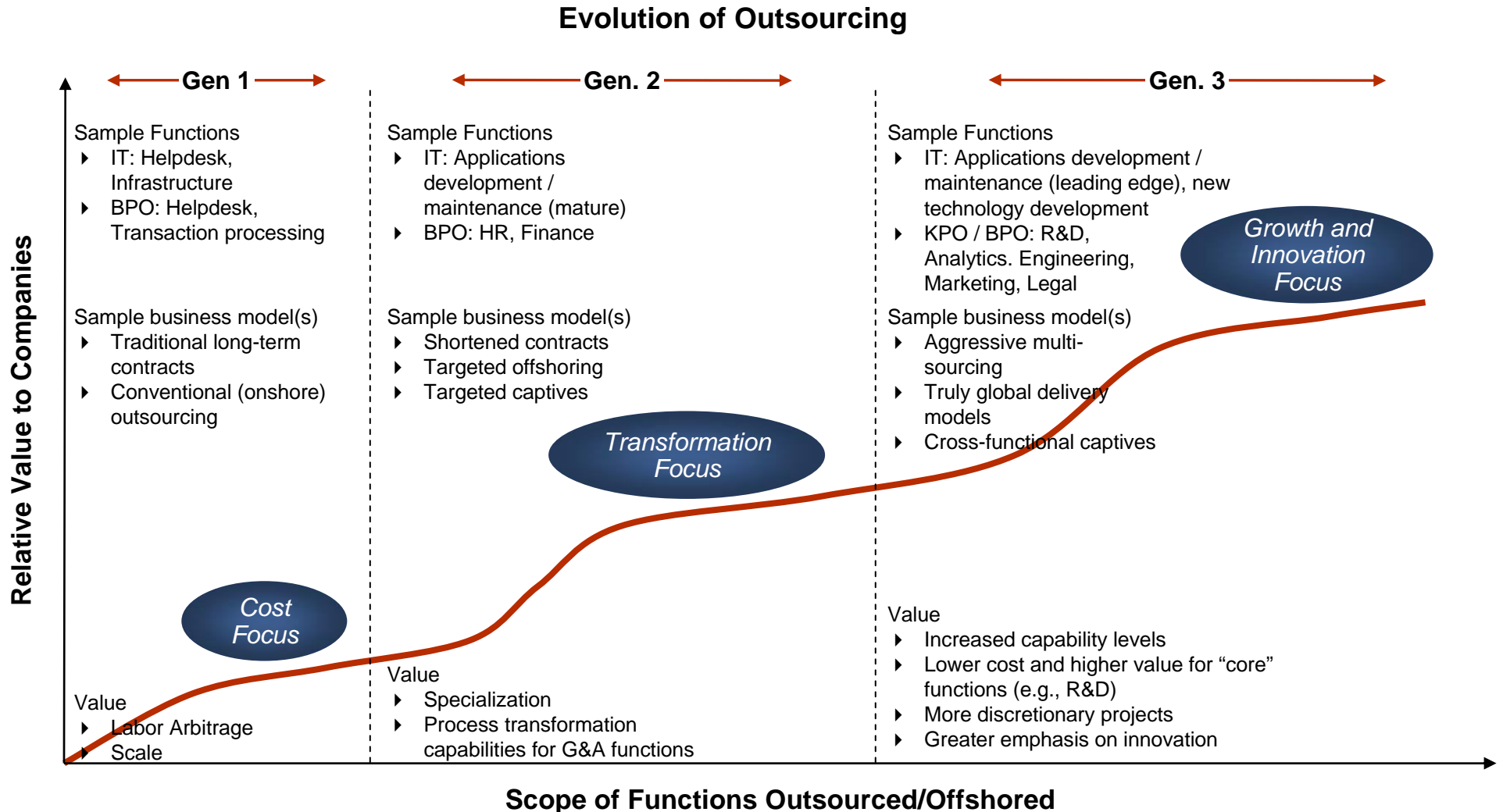
- Accounts payable
- General ledger accounting
- Fixed asset accounting
- Accounts receivable
- Cash management

Technology Services

- Software development
- Custom applications maintenance & management
- Hosting & maintenance
- Customer technology support
- Package/enterprise applications support & installation
- Network infrastructure management

4) Outsourcing

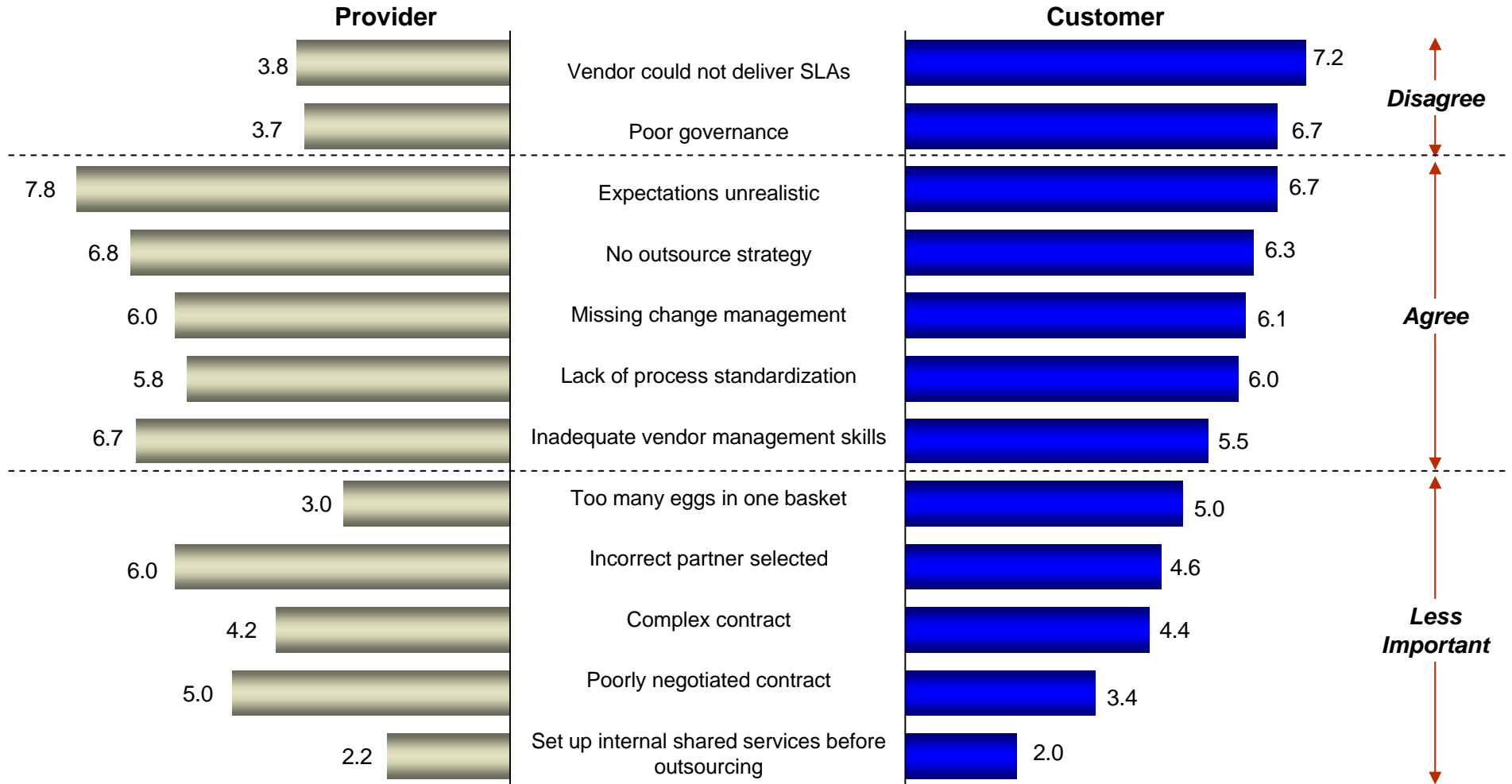
The outsourcing industry is beginning to move beyond its initial cost focus to becoming an enabler of innovation and growth as well



4) Outsourcing

Outsourcing benefits are not a slam-dunk though – many companies are unable to capture the full value of outsourcing

BAH Survey on the Relative Importance to Outsourcing Failure



4) Outsourcing

Companies approach outsourcing differently depending on their unique circumstances – we have seen two approaches

Traditional Approach) : Fix It and then Ship It



- ▶ “Lean out”, simplify, consolidate, automate
- ▶ Establish and monitor service levels and performance metrics
- ▶ Then pursue outsourcing

Emerging Approach): Outsource once you know how processes can be fixed



- ▶ Understand what it will take to fix sub-optimal process, the cost to fix and the potential benefits
- ▶ Work with outsourcer on a clear plan to reengineer and share the benefits while making the outsourcer finance the up-front costs
- ▶ Embed reengineering economics into the deal structure

4) Outsourcing

A Booz Allen/Duke University 2006 study revealed that offshoring is a rapidly evolving business value driver

Summary of Survey Findings

Offshoring has become a Mainstream Practice

BPO is Rapidly Growing While ITO is Beginning to Mature

Offshoring is Increasingly about Seeking Skilled Talent

“Innovation Offshoring” is Taking Off to India, China and Eastern Europe

Barriers to Offshoring are Organizational and Managerial

- ▶ Offshoring is growing across Europe and the US at double digit rates across industries and all major business functions
- ▶ US companies are leading the way in offshoring higher skilled business processes – offshoring is no longer just about low-end back office work
- ▶ Business process offshoring (BPO) is growing at almost double the rate of IT offshoring (ITO), which is entering a maturity stage
- ▶ Future growth trends indicate well over 75% annual growth in BPO projects, with the majority of growth from F&A, procurement and engineering offshoring
- ▶ **Offshoring is no longer just about cost reduction - accessing skilled talent and improving process efficiency have become a major drivers**
 - There is a growing shortage of skilled technical talent in the major Western economies
 - Large pools of high skilled talent are available offshore
- ▶ 50% annual growth in the offshoring of core innovation activities (**engineering design and services, product development and R&D**)
- ▶ **India, China and Eastern Europe are emerging as major locations for global innovation offshoring**
- ▶ **Major risk perceived by companies related to offshoring is the fear of loss of managerial control and the fear of the impact on operational efficiency**
 - Companies that are most experienced with offshoring have evolved their processes and organizational structures to manage these risks
 - It is essential to develop an organizational and management strategy for offshoring, along with developing an economic business case

In summary, Optimizing Overhead requires senior level, enterprise-wide, strategic attention

- ▶ Since we published the first edition of the Overhead Optimization Reader, we have observed some changes and trends in the market place
 - Prevalence of shared services and outsourcing; shared services in Europe and US Government
- ▶ What hasn't changed, however, are fundamental value drivers from Overhead
- ▶ While many organizations view Overhead Optimization tactically at the functional process optimization and automation level ...
- ▶ ... the most impactful Overhead Optimization levers are cross-functional and enterprise-wide in nature
 - Operating Model choice; Shared Services; Demand Management; Outsourcing/Offshoring
- ▶ As such, these levers require C-level attention and decisions
- ▶ The key to Optimizing Overhead is through strategic decisions senior executives must make, considering their overall organization

The new Reader, “Optimizing Overhead: From Cost Center to Competitive Advantage” discusses in greater detail the recent trends and major overhead optimization levers

Overview of the 2nd Edition of the Overhead Optimization Reader

Recent Trends

- ▶ **Outsourcing and offshoring** are here to stay, and US companies are increasingly leveraging them for multiple purposes
- ▶ **Shared Services** have evolved to provide real value to many private and public sector organizations
- ▶ Increasing **availability of technology** is enabling organizations to capture greater value from their overhead
- ▶ Companies are looking to capture **cross-border shared services in Europe**
- ▶ US Government is establishing **Centers of Excellence for G&A services**

Major Optimization Levers

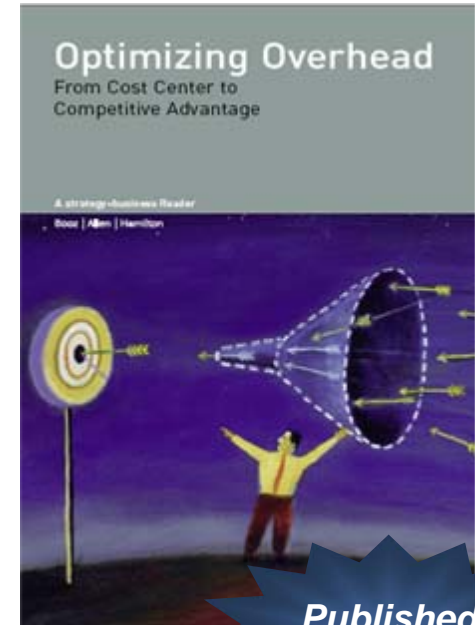
1. **Define the operating model** for the Corporate Core and Operating Units
2. Motivate users of the overhead to **better manage their demand**
3. **Implement Shared Services** to better capture scale efficiencies and define services customer-back
4. **Outsource and offshore** to leverage scale, technology, and factor costs of vendors

Additional Resources

Slides and recording: A recording of the event will be posted at:
<http://www.strategy-business.com/webinars/archive>

To obtain copies of the book, *Optimizing Overhead: From Cost Center to Competitive Advantage*, please use the following link:
<http://www.strategy-business.com/ohreader>

2nd Edition of the Overhead Optimization Reader



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Interested in receiving more information from Booz Allen's Overhead Optimization Team?
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