

KERNELPoint

Enhancing Competitiveness

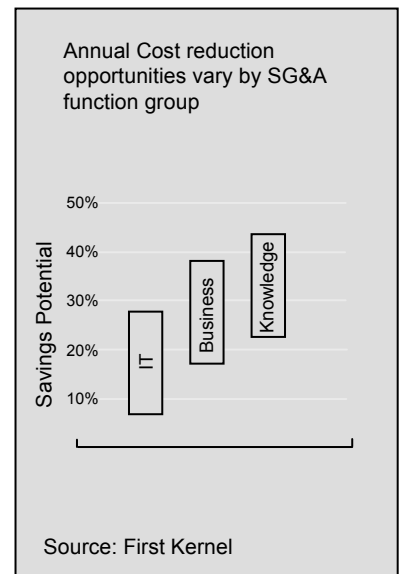
Through *Agile SG&A™*

It is clear to SG&A (Selling, General & Administrative) executives in enterprises that the performance of their domain directly impacts the competitive posture of the entire firm. The ability to implement a differentiated brand management infrastructure at Starbucks, the ability to lower KLO (Keep-Lights-On) expenses year-on-year at AT&T, the ability to shift the mix of Capex and Opex rapidly in response to shifts in business strategy at TXU – the SG&A domains driving them provide these firms the ability to dominate an industry or in some instances, remain viable.

Of late, high-performing enterprises are evolving what can be termed as 'Agile SG&A' domains. Its roots can be traced to proactive initiatives by a visionary CIO, CFO, Head of HR, Head of Procurement, or Head of Supply Chain. The emergent 'Agile SG&A' domain embodies, in aggregate, the minimum threshold of each of the following three abilities:

- ▶ Reduce unit costs by 15% or more year-over-year
- ▶ Attain and sustain service quality in the upper quartile of industry peer group
- ▶ Respond effectively to significant business shifts in 30 days or less

While one or more of these abilities have been attained by several enterprises we've individually assisted over the past several years during our work with them, the combinatorial 'Agile SG&A' domain status is always the result of a planned performance transformation journey, with measurable inputs and outcomes.



How much more will 1% less SG&A spend add to your company's EPS in 2006?

Further, while each ability does confer its own substantive benefit, the whole of all three translates to a distinct, order-of-magnitude competitive advantage for the SG&A domain and therefore to the enterprise.

1. Cost Advantage: Creating a risk-balanced portfolio of insourced and outsourced functions

Companies often tackle SG&A cost challenges via outsourcing. As services globalization accelerates and supply constraints develop, operating expenses even in offshore locations like Bangalore, India are increasing 20%-35% each year. Given cost pressures and eroding margins, many outsourcers are tempted to explore creative ways to compensate, raising the possibility that outsourcing driven savings may not be fully realizable.

Outsourcing alone may not therefore deliver the expected year-over-year SG&A cost improvements.

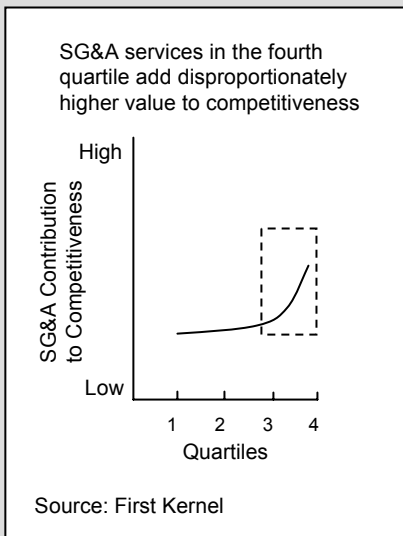
Fortunately, SG&A executives are finding that they've perhaps not fully explored the benefits of in-sourcing (i.e., retaining and optimizing an SG&A function) and that there is demonstrable value in maintaining a robust in-house service capability. The increasing ROI hurdle-rate faced by outsourcers coupled with a mostly deflationary labor and technology cost trend in the United States in the last several quarters has opened up some interesting options on the insourcing front. Assuming that the efficiency of an SG&A function can be improved in-house by about 20% or so, the case for insourcing starts to look compelling, particularly if it additionally requires intimate knowledge of the business and whose future changes are somewhat unpredictable.

SG&A domains that utilize a 'tailored' combination of insourcing and outsourcing are more likely to realize a sustainable risk adjusted 15% + year-over-year spend reduction, versus those that rely on just one or the other mechanism.

2. Quality Advantage: Leveraging standardization and benchmarking

One of the major SG&A trends during the 1980's and through the 1990's has been the rapid 'standardization' and 'componentization' of Information Technology functions within enterprises. Solutions that were routinely homegrown became available as off-the-shelf, standardized applications, providing everything from Enterprise Resource Planning (ERP) to Customer Relationship Management (CRM). Enterprises were able to shift their focus to their core business while utilizing these in a plug-and-play manner. CIO's led the charge, and as a result, the IT domain was able to achieve dramatic cost/performance improvements and related benefits for the enterprise.

Starting in about 2000, the remaining SG&A business functions in enterprises are experiencing a similar pattern of 'standardization' and 'componentization'. This in fact, is driving the scale, size and pace of the Business Process Outsourcing (BPO) phenomenon.



	Infrastructure	Methodology	Metrics	Tools	Training	Visibility
5	TMO, SSO drive major transformation initiatives	Standard transformation framework institutionalized	Comprehensive metrics in place, fully integrated across entire lifecycle and continually fine tuned	Full suite of transformation tools, integrated across both lifecycle and ecosystem partners	Transformation COE in operation, offering formal in house training programs	Substantial and continuous visibility to drive staffing, spending and sourcing arrangements
4	Formal TMO, SSO structure in place and staffed, but with limited span of influence	Standard transformation framework adopted across the entity in scope	Comprehensive suite of metrics in place and covers most lifecycle stages	Full suite of transformation tools, but integration primarily around lifecycle or ecosystem partners	Strong institutional affiliation with external industry recognized COEs	Substantial, but point in time visibility to drive staffing, spending and sourcing arrangements
3	TMO, SSO functions implemented and staffed in some parts of the entity in scope	Transformation frameworks adopted in some parts of the entity in scope	Detailed metrics in place, but focused on selected aspects of process/service (ex. process efficiency)	Full suite of transformation tools and some end to end integration	Formal transformation skills training in place in several parts of the entity in scope	Visibility limited to drive staffing, spending and sourcing arrangements for a process/service
2	TMO, SSO roles filled ad hoc, driven by point in time needs	Ad hoc transformation framework	Ad hoc metrics utilized in select parts of the entity in scope	Partial suite of transformation tools with some integration	Informal transformation skills training, however mostly internal, by subject experts	Some visibility to drive staffing, spending and sourcing arrangements
1	No resources allocated for TMO, SSO roles	No transformation framework in use	Few metrics utilized. Use and reliability limited	Few home grown tools, mostly discrete point solutions	No transformation related training offered	Staffing, spending and sourcing arrangements driven by intuition

eTMM-Execution Reference Model co-developed by First Kernel at the ETM Forum with University of Texas at Dallas



One of the obvious offshoots of standardization is the ability to more easily benchmark and to target improvement initiatives more precisely to close gaps in select categories such as staff productivity, process efficiency, cycle-time, or compliance accuracy. High-performing enterprises are increasingly utilizing benchmarking across all their SG&A domains and are undertaking them more often, to identify weaknesses and target improvements to achieve and sustain top-quartile status.

3. Speed Advantage: Empowering and equipping internal staff to effectively partner with the business

Looking at leadership rotations in the Dow and S&P lists over the past decade or two, it is clear that incumbency in a particular industry is not necessarily a permanency and, further, a particular industry itself is not necessarily a permanency. High-performing enterprises are therefore placing a lot of emphasis on change-management capabilities in their SG&A domains; i.e., the ability to rapidly align the scale, reach, character, cost structure, and KPI (Key Performance Indicator) of an IT



or Business Function to reflect changes in their firm's business strategy.

A framework co-developed by First Kernel with the School of Management at the University of Texas at Dallas, called the enterprise Transformation Maturity Model (eTMM) and proposed as an industry standard, is particularly useful in identifying the structural components that deliver the Speed Advantage. The eTMM framework helps SG&A domains achieve exceptional performance transformation competency by improving in six contributing areas – Infrastructure, Methodology, Metrics, Tools, Training and Process Visibility.

The eTMM framework employs five maturity levels, with each level representing about a 10% improvement in the cost structure of the SG&A domain over the prior level. The model is similar in orientation to the Capability Maturity Model (CMM) developed at the Software Engineering Institute (SEI) at Carnegie Mellon in the late 1980's to improve the discipline of software development in enterprises.

Bottom Line

An 'Agile SG&A' domain offers SG&A executives a simplified framework to plan, organize, manage and measure their domains. In turn it provides the enterprise the ability to compete better, achieve industry leadership sooner or to sustain a leadership position longer.

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About First Kernel Consulting, Inc.

We are experts in Enterprise Performance Transformation. We help enterprises implement a seamless combination of exceptional in-house capabilities and effective sourcing arrangements to harvest substantial value and savings from their IT Services and Business Functions.

Our clients leverage the integration of our expertise, intellectual property, tools and guidance to achieve or surpass their SG&A performance targets. First Kernel has developed the industry's first *Enterprise Performance Transformation System*™, currently pending a United States patent.

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