Controlling Expenses:

Inside a Common Challenge for Business Owners

Controlling business expenses is a top stressor for leaders of small and midsize companies. By understanding how other owners rein in expenses—and where they find the biggest savings—you can better position your company for growth.

Running a business can be challenging, complicated and stressful. In fact, a recent nationwide survey conducted by SunTrust indicates that about half of leaders at **companies with annual revenue between $2 million and $150 million feel somewhat or extremely stressed about their businesses.** *(Figure 1)*

One source of that stress is disparity when it comes to controlling operating costs and other expenses. Businesses recognize the importance of keeping costs in check, with about 87 percent of them indicating that controlling costs is somewhat or extremely important, and nearly 70 percent stating that controlling expenses has either some or significant impact on their business' success. *(Figure 2)*

Feel somewhat or extremely stressed about their business

Figure 1

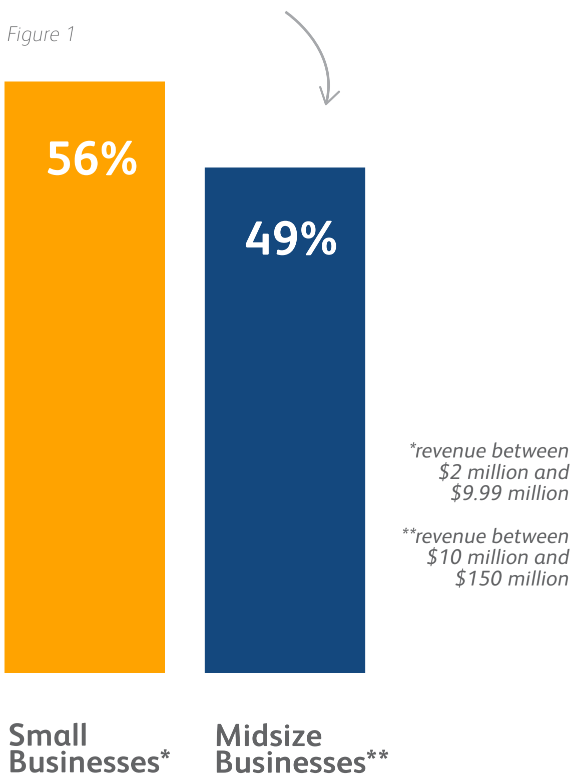
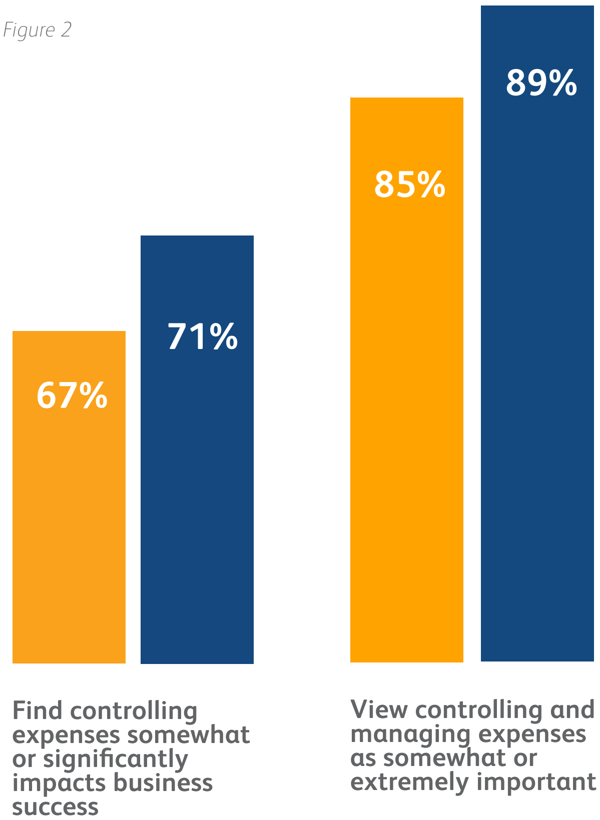


Figure 2



Indeed, controlling costs can substantially improve results. Depending on the company's operational structure, cost savings of $200,000 each year could be equivalent to earning an extra $1.5 million in annual revenue, says Marc Spiegel, partner at ACC Atlanta, an office of Alliance Cost Containment, which helps midsize businesses reduce expenses in categories ranging from office supplies to uniforms to janitorial services.

"The $200,000 doesn't go to the top line and have costs or expenses taken out," he says. "It goes directly to the bottom line."

Despite the benefits of cutting costs, many business leaders do not feel ready to implement the necessary changes. Almost half of businesses feel only somewhat prepared to control expenses in the near future, according to the SunTrust survey, and one-fourth feel unprepared to do so. *(Figure 3)* About half of businesses report that controlling expenses is challenging and stressful. *(Figure 4)*

The process isn't easy. Employees often assume they'll lose something when cost-cutting initiatives are introduced, says Baron Christopher Hanson, principal and lead strategist at consulting firm RedBaron Strategy/PR. They believe their jobs will get harder and their paychecks and perks will shrink.

"Obviously, uncomfortable changes and challenging conversations will take place, yet the best way for employees to be engaged positively is for leadership to present the benefits that will result from smarter and harder work," he says.

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Figure 3

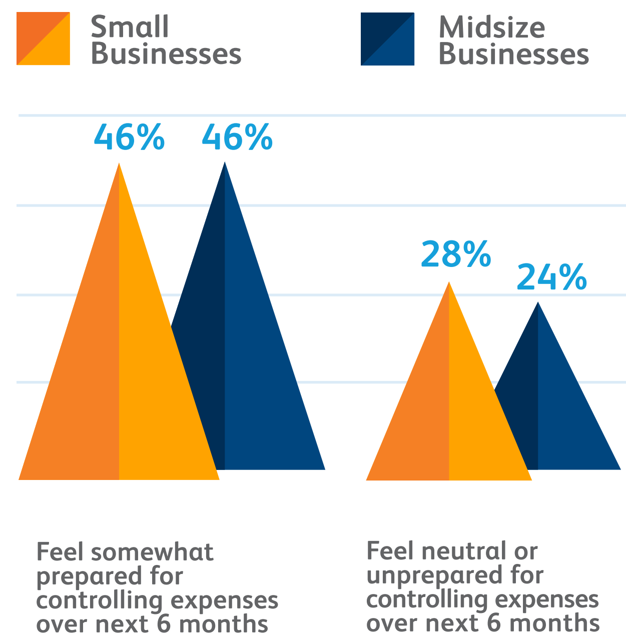
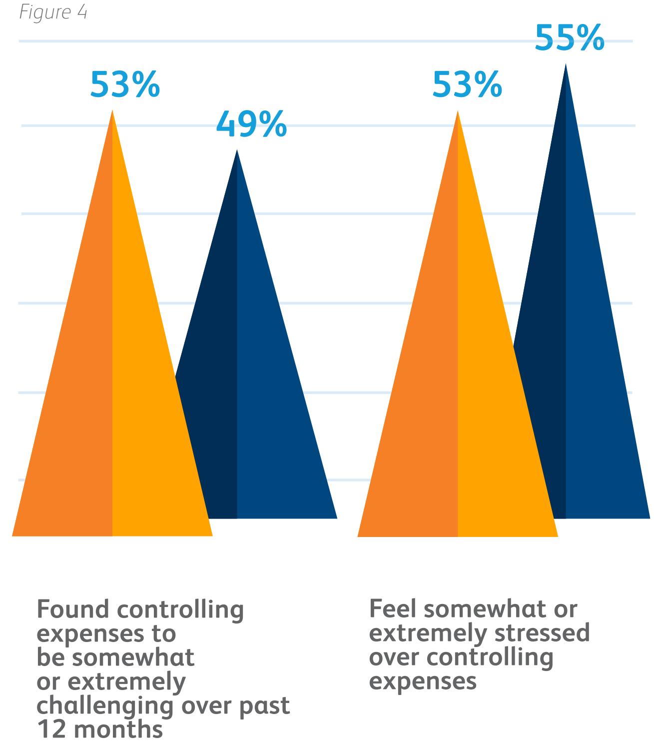


Figure 4



Controlling costs in small and midsize businesses

Controlling costs concerns decision-makers at businesses of all sizes, locations and industries, according to the SunTrust survey. Companies that have been in business for a few years expressed many of the same feelings about cutting costs as did companies that have been operating for decades.

Perhaps most importantly, effectively controlling costs can affect the competitive position and overall outlook for businesses. Those firms that find controlling costs to be challenging also reported feeling less confident about their financial well-being, finances and business outlook. Organizations that don't find controlling expenses challenging tend to be more satisfied with their marketplace positioning relative to competitors and more optimistic about their future prosperity.

So, businesses can benefit considerably from learning to identify and assess expense control methods and taking steps to improve the chances that they'll succeed. **Many small and midsize businesses surveyed by SunTrust, for example, matched payment terms with their cash cycle as a means to control expenses.** Thirty-six percent of small businesses that tried this tactic realized success, as did 56 percent of midsize businesses.[1]

Small and midsize companies, provided they're well-managed, also have an advantage when it comes to cutting costs.

"Middle-market companies are surprisingly nimble," Hanson says. "They are still quite entrepreneurial, or at least they can be if that is leadership's attitude."

That agility can translate into substantial relative cost savings. For example, a company with $750 million in annual revenue that trims costs by $25 million will save 3.33 percent, but a company with $75 million in annual revenue that reduces costs by $5 million will save 6.67 percent, or double what the larger business saved. Those savings can then be reinvested to help fuel growth.

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SunTrust

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Cutting costs with cutting-edge technology

One of the most common actions businesses take to reduce costs is investing in technology or equipment to improve productivity. More than a third of the businesses surveyed by SunTrust report they've done so, or 34 percent of small businesses and 44 percent of midsize businesses, respectively. Companies often find these investments succeed, and they report they're likely to use them in the future. *(Figure 5)*

Hanson recommends managers and executives carefully assess any investments to help ensure their firms achieve their goals.

"Our first criterion is typically to witness an actual existing customer using the technology, equipment or software," he says. This interaction should be face-to-face, not through phone calls or email. The purpose is to help companies thoroughly understand all aspects of owning, operating, staffing and maintaining the investment before committing to it.

The larger and more significant the investment, the more important it is to evaluate firsthand. A company with $30 million in annual revenue may spend up to $3 million, or 10 percent of its revenue, on an enterprise resource planning (ERP) system that will affect nearly every aspect of its business. That large of an investment in something that's likely to change everyday operations warrants an in-person visit.

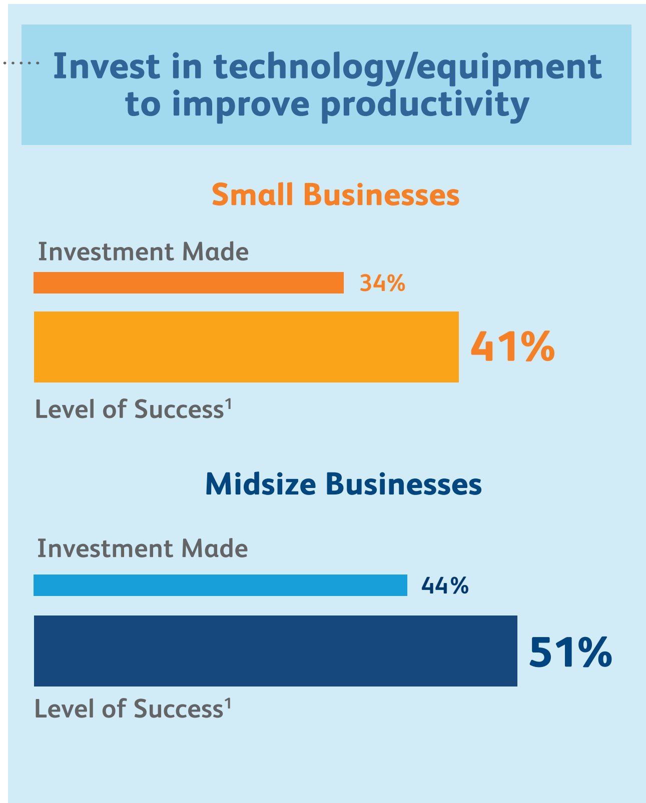
"The second step is to prove that the additional technology or equipment is going to operate within the business cost-effectively, beyond the promised value and function," Hanson continues. "Will employees know how to use it after the sale? Is it safe to operate in your current facility? Most importantly, will two or more people inside your company be able to monitor it or repair it?"

Taking these steps will also help prepare businesses to encourage employee buy-in, says Hanson, which is important in ensuring investments pay off.

Paying for technology and equipment often means seeking financing, a task business leaders can make easier with thorough preparation.

Business leaders who have effectively assessed their potential purchases will be able to explain how the new software, machine or other innovation will operate, earn cash and be maintained for years to come, Hanson says. That information can ease the financing process.

Figure 5



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Renegotiating contracts to realize savings

Renegotiating contracts with suppliers is another method businesses frequently use to control expenses, and which they are likely to use in the future. **Thirty-seven percent of small businesses surveyed by SunTrust reported renegotiating contracts to better control expenses,** with 32 percent of their midsize counterparts using renegotiation as a strategy to cut costs. *(Figure 6)*

But controlling business service costs does not have to mean sacrificing service or quality, Spiegel says.

"The biggest thing about cutting costs is understanding what you're buying and looking for the best value, which I equate to price plus service," he says. "It's not always finding the cheapest deal but the one that's most dependable. That saves you money in the long run."

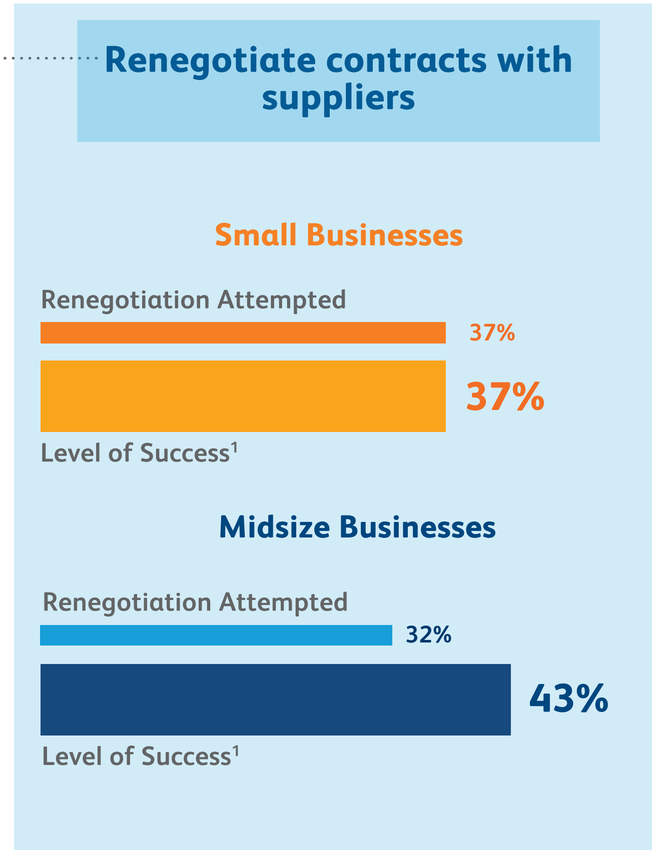
Many businesses rely on requests for proposal to identify and decide on vendors, but that process isn't always effective at controlling costs, Spiegel says. Vendors often include annual rate increases, as well as fuel and environmental surcharges, to boost their margins, and the staff members reviewing the responses may overlook these added costs.

Company employees might have expertise in one or two expense categories and therefore be able to select the best vendor, but it's difficult to know all aspects of every category. This can be especially challenging for small and midsize businesses, where employees may have multiple responsibilities and lack knowledge about how suppliers operate, Spiegel says.

As a result, outside experts can help companies quickly realize savings in specific categories, such as telecommunications and phone and Internet systems, and even waste removal. For industries outside of your own, it's not always easy to determine what constitutes a fair margin. Some businesses take advantage of this and charge unnecessarily high fees.

Small and midsize businesses may also lack volume purchasing power, Spiegel says, which prevents them from gaining access to the best possible deals. Companies can overcome this obstacle by looking for ways to join forces with other firms to purchase supplies.

Figure 6



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Outsourcing as an effective, but overlooked measure

Some businesses are outsourcing, specifically beyond U.S. borders, as a means to rein in expenses. While outsourcing wasn't a popular cost-cutting tactic in 2014—only 16 percent of small businesses and 18 percent of midsize businesses reported trying it—it achieved relatively high levels of success. About 45 percent of firms that have made this move report it successfully reduced costs. *(Figure 7)*

For those companies thinking about outsourcing, Hanson recommends looking beyond the potential immediate cost savings.

"Will outsourcing be a long-term, profit-producing, culture-enhancing behavior, or will it cheapen the brand and tarnish the company's customer service reputation, just to save a few bucks?" Hanson says.

To ensure outsourcing falls into the former category, Hanson suggests businesses assess the sustainability of the estimated savings and the possible effects on brand reputation. In some instances, outsourcing can lead to lower or inconsistent quality, which could create additional costs or irritate customers.

Spiegel agrees that ensuring quality remains high is key when evaluating outsourcing as a savings strategy. Several of Spiegel's clients have outsourced various parts of their operations, and he's found that each case is unique. However, many companies are now also finding overseas labor costs are not as low as expected.

"With the price of labor rising globally, a lot of people are more comfortable on-shoring everything," he says.

Figure 7

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Saving through reduced travel and automated expenses

Substituting teleconferencing and videoconferencing for travel offers yet another possible path to reduced expenses. **More than 40 percent of survey respondents indicated this is a successful way to control expenses, and about 30 percent indicated they'll likely use it in the future.**[1] Travel costs are not getting any cheaper, Hanson notes, especially for international trips. For routine communications, he sees this cost-reduction method as useful, especially if it's typical within the company's industry.

"However, ruling out travel altogether is not exactly wise," he says. "Keep both options ready based on the importance of the business or sale or event at hand. It's all about the importance of the meeting, and if the interaction via computer screens, large or small, will be sufficient based on the outcomes required."

For important sales calls, meetings with new vendors or initial client discussions, face-to-face interactions may be worth the travel costs.

Furthermore, **software programs that track expenses help businesses catch billing errors, which Spiegel says can amount to annual savings of 4 to 5 percent.** The employees processing invoices don't always know when they're over-paying, and the programs can compare contracted rates with invoiced rates and flag discrepancies.

One challenge in implementing these systems is getting employee buy-in and training workers who may have been doing their jobs the same way for 10 or 15 years. Spiegel suggests rewarding employees who use the systems to help overcome these obstacles. He also advocates choosing cloud-based systems when they're available. These allow for more flexibility, and with a larger number of people working from home, are often easier for remote personnel to access.

Taking advantage of bank software that improves fiscal awareness can also streamline the process of cost cutting. Approximately three-quarters of businesses in the SunTrust survey indicated these services would be somewhat or extremely valuable in controlling expenses. The good news is that these services are already available.

For example, companies using purchasing cards simplify their procurement efforts and reduce the time necessary for paying invoices. These cards offer not only spending controls, but also an easy way to track purchasing patterns. Ideally, these cards integrate into an online spending analysis program that connects to ERP systems to centralize expense management.

Cash flow software shows real-time balances and accounts for pending transactions and open invoices so businesses always know where they stand financially. Mobile banking options, especially those with customer alerts, can help businesses forecast expenses.

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Controlling expenses and the path to long-term growth

As businesses grow, they may face new and unanticipated expenses. These costs can come in the form of taxes, new software—such as customer relationship management (CRM) systems—expanded facilities or additional staff. Other growth expenses include real estate and marketing. Hanson says managing growth is largely about constant analysis and preparation and suggests businesses look at how companies already in the next life cycle stage are operating.

In anticipation of rapid growth, businesses can obtain lines of credit to tap if cash flow becomes tight. They can also consider business term loans to fund expansion into new markets or pay for new projects. Sometimes, growth comes unexpectedly or all at once, and these tools provide ways to manage surges in demand so that business leaders prosper rather than stress.

The process of cutting costs is never easy. However, the benefits can be substantial, sustained and give companies a competitive edge. **No one cost-cutting method fits all businesses, but there are many possible paths to the same destination: increased profitability and reduced stress.**

For more information on how your company can trim costs and boost revenue, contact your SunTrust Relationship Manager or visit **SunTrust.com.**

Source: SunTrust Quarterly Nationwide Survey Conducted July, 2014

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