



Profitability improvement - a structured approach

Methodology

Profitability improvement methodology

Overview of New Light Strategies' approach to profit improvement

The approach as set out below, has been developed and refined over many years in executive management roles in a number of IT services and professional services organisations. These have included organisations in the legal, accounting, IT professional services, IT services, creative design and consulting services industries.

The approach is based on the following core principles:

- Analyse using services and professional services economic drivers as the base and then use these metrics to monitor the achievement of the desired target performance;
- De-aggregate the business to an appropriate sub-level;
- Maintain a client-service focus throughout the diagnostic, strategy identification and implementation phases. Delivering value to your clients must be enhanced and not compromised in any way;
- Involve the people in the organisation to an appropriate and agreed organisation level. This ensures that there is a true sense of involvement, awareness is created and a clear understanding is established of what's required to achieve success and profit growth; and
- The overall objective is to do things better and smarter, driving for a balanced mix of improvement and innovation strategies.

The achievement of increased profitability is an outcome of the process; it's an outcome of doing things better and smarter.

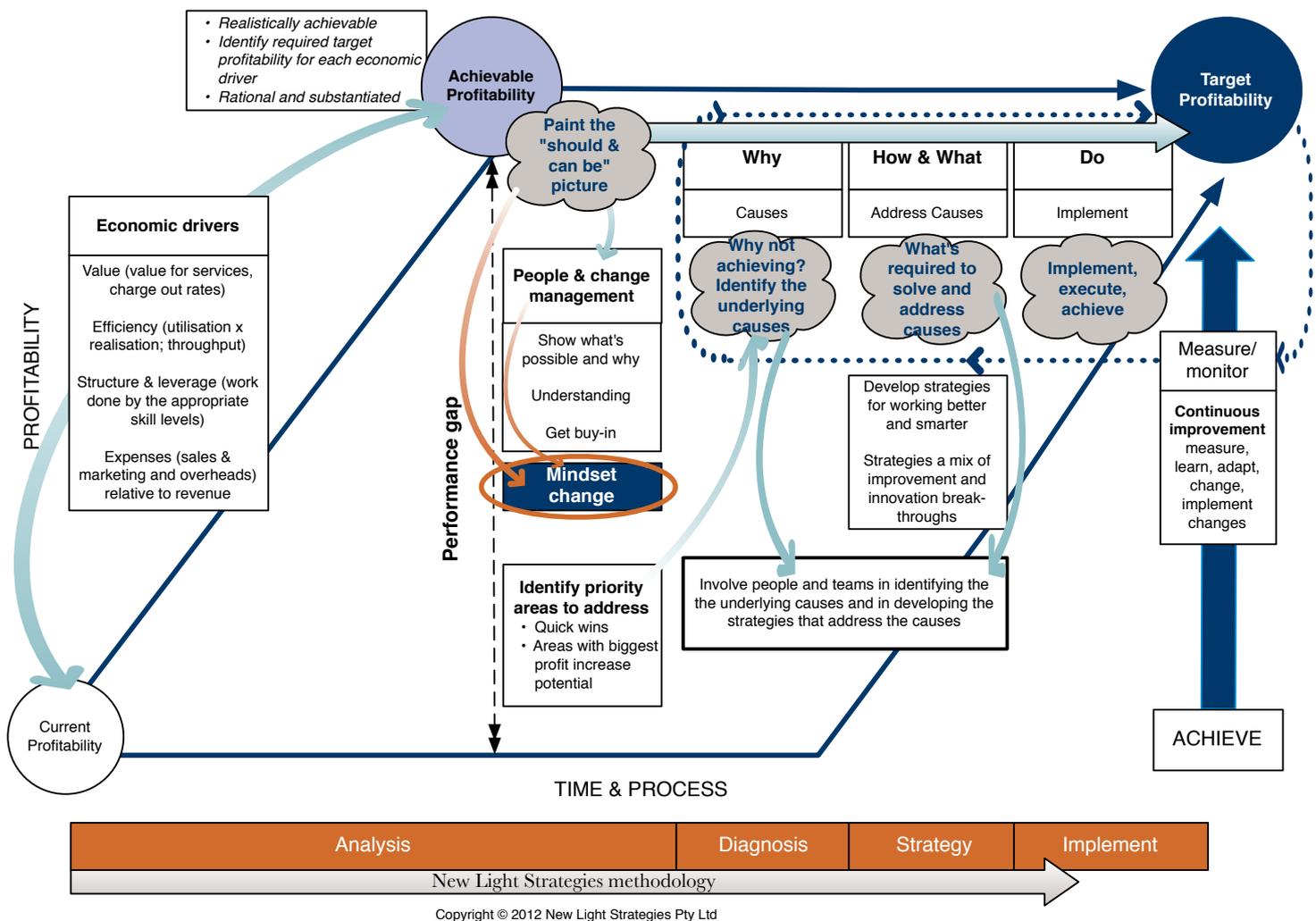
Growing the profit in a services business has very little to do with cutting costs (although appropriate cost control is an essential discipline); growing the

profit is about achieving better quality revenue. This means that your revenue is more profitable, derived from clients who value the service your organisation provides and delivered efficiently and effectively.

The identification, development and implementation of a profit improvement process is made up of multiple phases. The full process is divided into 4 main phases. These phases are analysis, diagnosis, strategy identification and implementation. Each phase can be completed as a discrete or standalone project, with specific deliverables which provide actionable outcomes to management at the end of each phase.

The profitability analysis is essential as a first step in the process. It provides the organisation with a "profitability health check", identifies areas that require improvement and quantifies the profit improvement potential and targets.

Ultimately the real value is derived from the diagnosis, strategy identification and implementation phases as it is only once the profit improvement strategies are identified and implemented that the profit growth potential can be achieved and realised.



Profit improvement process

The consulting methodology used by New Light Strategies addresses each of the phases within the profit improvement model. These methodology phases, which are set out in more detail in the following paragraphs, are:

- Analysis phase;
- Diagnosis phase;
- Strategy identification phase; and
- Implementation phase.

Analysis phase

The analysis phase is the critical first step in the process. During this phase we establish the fact base and identify the areas in the business where profit improvement is required and those areas where the biggest opportunities for overall profit improvement exist.

The analysis, for each of the services economic

drivers, will be completed across a matrix of practice areas, work groups and other relevant areas within the organisation. The extent to which the business is de-aggregated and analysed will depend on the structure of the organisation.

The analysis phase will be comprised of the following broad steps:

- The business's performance is assessed across a number of criteria, with a particular focused assessment of the performance of the services economic drivers.
- The services economic drivers are comprised of the following elements:
 - efficiency (utilisation and realisation);
 - value (actual or implied charge out rates achieved);
 - leverage ratios (staff structure); and
 - expenses and overheads as % of revenue

- Other performance measures that are considered and assessed, if available, are a “people measures” (e.g. level of engagement, turnover, skills and skill shortages), “client measures” (e.g. average client engagement size, client concentration, client satisfaction levels) and engagement or job performance measures.
- Performance measures like revenue growth, gross profit margin, net profit %, performance against budget, etc are also assessed, but these types of measures are “outcomes” and not necessarily drivers of performance. These outcome-measures are therefore not particularly useful in identifying underlying causes during the diagnosis phase.
- The analysis will be done to the lowest level of granularity that’s possible within the constraints of management information and reports available.
- The approach used in performing the analysis and in drawing conclusions, will include a review of the financial and performance information, discussions with key individuals and scenario-testing through the use of spreadsheet modelling of the business.

At the conclusion of this analysis phase, the areas requiring profit improvement are identified and prioritised.

It is possible that potential profit improvement strategies will be identified as part of the profitability analysis. This should however not be relied on and is not a specific deliverable within the profit analysis phase. Identifying such strategies during this initial phase will be more opportunistic and ad hoc. Identifying profit improvement strategies requires proper diagnosis of the underlying issues and a structured approach to identify what’s required to address the underlying causes.

Diagnosis phase

During the diagnosis phase, the underlying reasons for both good and poor performance is identified. This is an essential step before any strategies are developed. By understanding the underlying causes, appropriate strategies can be

developed to address issues and leverage off areas of strength.

This phase will require involvement from executive management and other people within the organisation. Some organisations prefer that only certain key executives are involved in discussions and workshops, whereas other organisations have a culture of broader involvement across more levels and people within the organisation. The extent to which people will be involved in this process will be discussed and agreed with the yourselves. The objective will be to get sufficient people involved without it being intrusive or distracting to the organisation.

The process for this phase is a combination of interviews with people, personal insights gained during the profitability analysis, insights and knowledge of underlying causes experienced at other IT services and professional services organisations and finally, a workshop where the findings are presented, debated and tested. Following the workshop (or workshops), a written report will be prepared and a presentation made to the executive management.

Whilst it is proposed that the profitability analysis (phase 1) is performed on a “whole-of-business” basis, the diagnosis phase can be done on any combination of whole-of-business or limited to specific practice areas or other relevant sub-sets of the organisation. The findings of the analysis phase will provide the basis for the organisation’s executive management to decide which areas to focus on for the detailed diagnosis. This is ultimately a decision for management and not for the consultant.

As a general rule, we select those areas for diagnosis that will generate the biggest profit increases as well as areas where quick wins and immediate profit increase can be achieved.

Strategy identification phase

Strategies for profit improvement are developed based on the findings of the diagnosis of the underlying causes. Here again, people from the organisation will be required in workshops and interviews. In some instances the strategies will be known and familiar to New Light Strategies based on prior experience. It is nonetheless essential that

strategies are developed and agreed with appropriate people within the organisation.

The strategies and initiatives need to have an appropriate balance between improvement strategies and innovation. During the workshops people will be challenged to identify the required strategies.

We will also assess current and existing strategic plans and initiatives to assess the extent to which they are addressing profitability improvement. We would expect that you already have such strategies and initiatives and an assessment of their success or otherwise, needs to be carefully considered.

A detailed list of the required and agreed strategies and initiatives are prepared at the end of this phase.

Implementation phase

Once strategies and initiatives have been identified and agreed, these need to be translated into detailed executable action plans. This phase ensures that “theory becomes reality”.

New Light Strategies has developed templates and approaches for strategy implementation action plans, including tools and templates. It is however proposed that the implementation action plans align with and are adapted to any existing or preferred approach that your organisation currently uses. As a principle we believe in minimising the introduction of new tools, templates and methodologies. The appropriate implementation approach will be discussed and agreed with executive management.

A final critical element in the implementation phase is to structure and introduce appropriate performance metrics. These metrics will monitor and track the success of the strategies implemented and will serve as a basis for identifying which strategies are not delivering on the expected outcomes and consequently need to be refined, adapted or changed.

It is also recommended that these performance metrics are incorporated into your organisation's performance management and remuneration review processes.

William Masson

Founding Principal

+61 419 212 759

william@newlightstrategies.com

www.newlightstrategies.com

New Light Strategies Pty Ltd

ABN 39 152 955 934

Level 4, 95 Pitt Street,

Sydney 2000

T+61 2 8006 2955

F +61 2 9475 0162

