CFO Outlook Survey

February 2016

Nigeria

KPMG CFO FORUM

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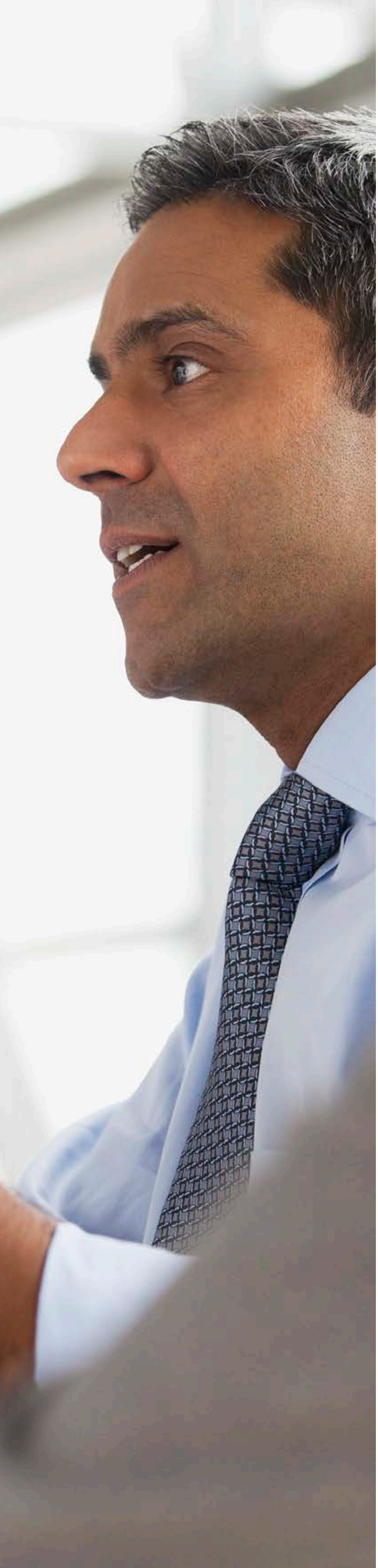

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Foreword

The maiden edition of KPMG's Chief Financial Officers (CFO) Outlook survey took place in 2014 and assisted in fulfilling the CFO Forum's objective of offering a platform to identify and share leading practices amongst CFOs and create an additional channel for CFOs across industries to interact with relevant regulators.

I am pleased to say that this year's edition provides further insights into the critical issues CFOs have to contend with as they seek to protect the bottom line and enhance shareholder value.

Compared to the previous survey, the general outlook from this survey is somewhat less optimistic. This is not altogether surprising, in light of the additional challenges the Nigerian economy is expected to face in 2016. There is a general consensus that the consequences of declining crude oil prices on the macro–economic environment will have a dampening effect across all sectors of the economy.

Against this backdrop, the top three `stay awake issues' for our respondents are; cost management, exchange rates and government regulation. While these are not necessarily new concerns, they have assumed a new urgency, and it is clear that the current economic realities call for more radical and innovative approaches to these issues.

CFOs have to rethink their operations and look for ways to optimise their operating model with a view to reducing their cost of operation. This edition includes some useful thoughts on sustainable cost optimization.

Our conversations with CFOs show that derivative contracts, alternative investments and hedging have all become areas of increased interest as CFOs battle to deal with increased currency risk. Unfortunately, there are no easy answers and for some companies, pursuing these measures now may feel like shutting the proverbial stable door after the horse has bolted.

However, it is important to remember that it is never too late. The institution of robust foreign exchange risk management policies will be key in avoiding future losses. This edition contains some useful tips in this regard.

With respect to regulation, policy consistency remains a recurring issue, but one area of increased concern is `regulatory aggression'. While regulation remains a strategic tool in the hands of government for managing the economy, implementing policy and influencing behaviour, there remains considerable potential to improve the use of regulation to enable the growth of businesses in the country.

Our respondents have highlighted infrastructure, security and exchange rate stability as the top three areas in which they would like to see improved government support for businesses. Coincidentally, these areas align with the priority sectors announced by the new government, and it is fair to say that a lot will hinge on the ability of the government to deliver on these priorities.

At KPMG, we recognize that the complexities of today's business environment are causing an evolution of the role and expectations of the CFO and the Finance Function. We believe that the CFOs that will continue to remain relevant and thrive will be those that are able to develop and implement strategies to deal with the challenges encountered due to the economic downturn. In some cases, this will require a different set of experiences and skills from those currently available within the Finance Function.

My appreciation goes to all the survey respondents for their invaluable time and insights. I hope the findings and additional commentary are beneficial. For us at KPMG, we remain committed to providing a platform for articulating the critical issues of concern to CFOs and contributing to the necessary discussion and actions for their remediation.

Tola Adeyemi
Partner & Head,
Audit Services
KPMG in Nigeria

About the Survey

KPMG International's global survey of CFOs and other senior finance executives of organizations worldwide is one of the most comprehensive and long-running survey series of its kind. Iterations of our global CFO surveys and research papers have been conducted regularly since 2006, charting the evolution of finance departments and identifying leading financial management practices of high-performing companies.

This report presents our findings from the 2015 CFO Outlook Survey conducted by KPMG Nigeria which consisted of seventeen (17) questions. CFOs and Heads of Finance in leading organisations across all major sectors in Nigeria shared their opinions on the outlook for their businesses, their definition of the ideal finance function and relooked at how well cost strategies which have been implemented in their organisations have fared and their root causes. The distribution of our respondents across the sectors is as follows:

Sector of Respondents	
Energy and Natural Resources	25%
Technology, Media and Telecommunication	10%
Financial Services Industry	30%
Consumer and Industrial Markets	32%
Infrastructure, Government and Healthcare	3%

We also interviewed key subject-matter specialists and finance advisory leaders and drew from other KPMG International survey reports and Financial Management thought leadership in order to ensure the report also provides additional insight into some of the key themes identified in the survey.

1 Business Outlook: The Road Ahead

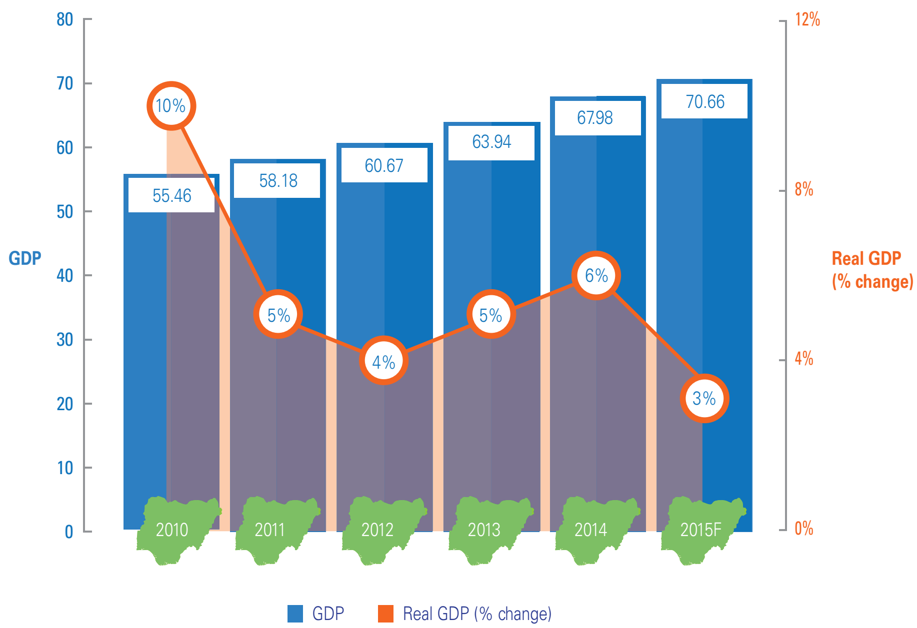
Complexity arising from economic realities

It is estimated that there will be a gradual pickup in global activity during 2016. In advanced economies, a modest and uneven recovery is expected to continue with a gradual further narrowing of output gaps. The picture for emerging markets and developing economies is diverse but in many cases challenging. The slowdown and rebalancing of the Chinese economy, lower commodity prices, and strains in some large emerging market economies will continue to weigh on growth prospects in 2016 and 2017.

The Nigerian economy was forecasted to grow by 5.54% in 2015 and 5.7% on the average between 2015 and 2017[1]. However in 2015, actual GDP growth slowed to 3.96%[2] in Q1 and 2.35%[3] in Q2, down from a peak of 6.54%[4] recorded in Q2 of 2014. With declining oil prices, the depreciating Naira, and increasing financial market volatility, downside risks to the outlook for Nigeria have risen. Nigeria's economic growth is estimated at 3% for 2015 and 4.1% in 2016[5].

2010 - 2014 GDP Growth and 2015 Forecast

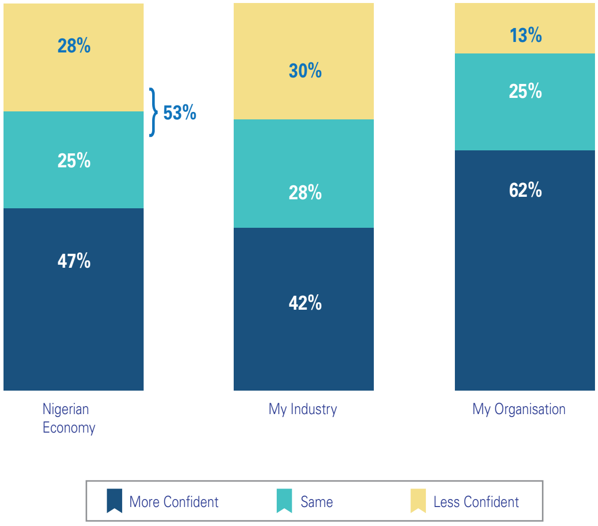
Source: World Economic Outlook, IMF World Economic Outlook Update (January 2016)



[1] Nigeria in 2014: Economic Review and 2015 – 2017 Outlook; National Bureau of Statistics
[2] Nigerian GDP Report,Q1 2015; National Bureau of Statistics
[3] Nigerian GDP Report,Q2 2015; National Bureau of Statistics
[4] Nigerian GDP Report,Q1 2015; National Bureau of Statistics
[5] IMF World Economic Outlook Update (January 2016)

CFOs expressed a less optimistic view on the outlook for 2016. Our survey respondents see a challenging year for their businesses. Most of our respondents believe that reducing costs and improving cash flows will be the highest priorities for their organisations in the year ahead. They believe to succeed, they will need to rethink their operations and explore new strategies so as to remain profitable.

Q1 How confident are you about the prospects for growth for next year (2016) compared to this year (2015)?



Source:
KPMG Analysis

KPMG INSIGHT

Business confidence is an important indicator of the state of the economy. While confidence levels may be falling in the near term, it is important for future growth that both government and business leaders remain focused on long term drivers of sustainable value creation.

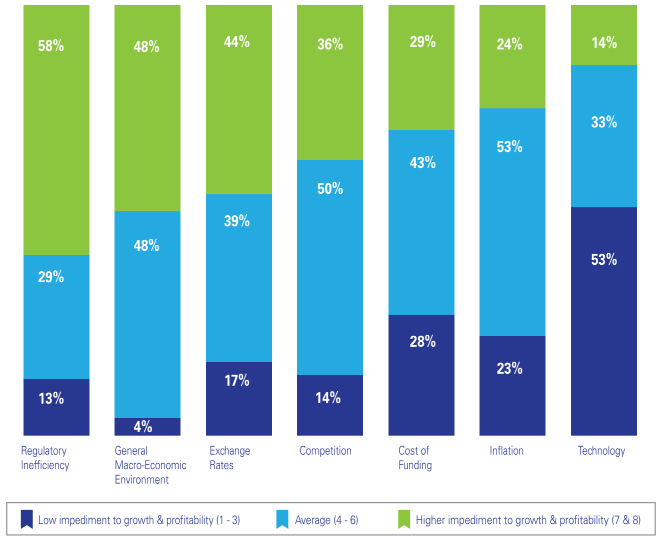
The vast majority of CFOs surveyed do not expect the prospects for growth in their industry or the Nigerian economy as a whole to be better in 2016 compared to 2015. 53% of the respondents are either less confident about the country's economic outlook or are of the opinion that it will remain the same. Surprisingly, about 62% of CFOs surveyed are more confident in the growth prospects of their organisation. This implies they have delinked their organisation's growth from that of their industry and the economy as a whole. Perhaps this is a reflection of a strong sense of 'Self belief'. Further engagements with the CFOs suggest that the strong sense of 'Self belief' being expressed in their individual companies is anchored on the view that their companies are already well positioned to manage the headwinds and have proactively taken steps to mitigate the emerging risks in the business environment.

KPMG INSIGHT

While regulation remains a strategic tool in the hands of government for managing the economy, implementing policy and influencing behavior, there remains considerable potential to improve the use of regulation to enable the growth of businesses in the country. Regulation should be an enabler that provides certainty to investors and the market on the rules of the game and should also be positioned to stimulate growth in the face of dire macro-economic headwinds.

Q2

To what degree is each of the following factors a likely impediment to your organisation's growth and profitability in the next three years? (Rank from 1 – 8, where 1 is Lowest and 8 is Highest)



Source:

KPMG Analysis

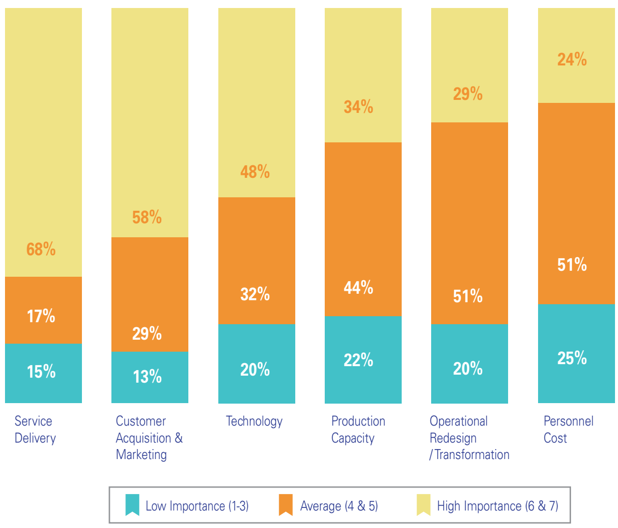
58% of the respondents believe that regulatory inefficiency is likely to impede the growth and profitability of their organisations, while 44% believe the unavailability of foreign exchange and the instability of the exchange rate will likely affect the organisation's growth and profitability in the years ahead.

KPMG INSIGHT

Strong customer experience has great potential for delivering desired financial outcomes especially amidst current macro uncertainties. There is a strong correlation between excellent customer satisfaction and improved bottom lines. From higher prices for service to repeat business, having a good service culture can make a huge difference. Customer experiences have the potential to either push customers away or pull them in.

Q3

How intensely do you think the following spend categories will influence the future growth of your organisation? (Rank from 1 – 7, where 1 is Lowest and 7 is Highest)



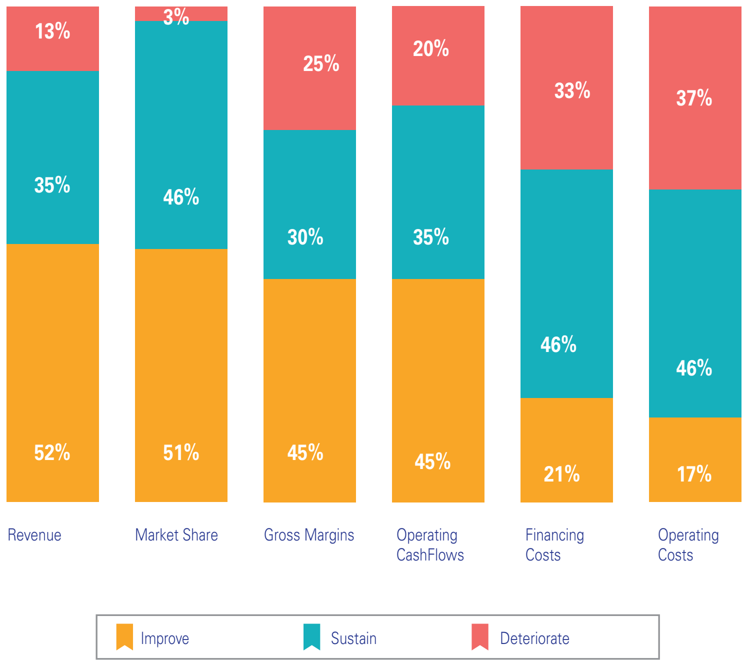
Source:

KPMG Analysis

Respondents identified Service delivery, Customer Acquisition & Marketing as well as Technology as the influential drivers of growth in their organisations for the year ahead, with 68%, 58% and 48% of respondents respectively, ranking these factors as the highest priority spend categories for their organisations. This trend clearly indicates that the 'customer' is at the heart of the growth strategy of most companies with strategic investments likely to continue in the acquisition, servicing and retention of its customers.

Q4

In your opinion, how are the following metrics for your organisation likely to change over the next 12 months?



Source:
KPMG Analysis

83% and 79% of respondents expect their operating and financing costs respectively to either deteriorate or remain same over the next 12 months. This signals the likelihood of decline in profitability despite the optimism expressed in respect of improvements in revenue and market share.

KPMG INSIGHT

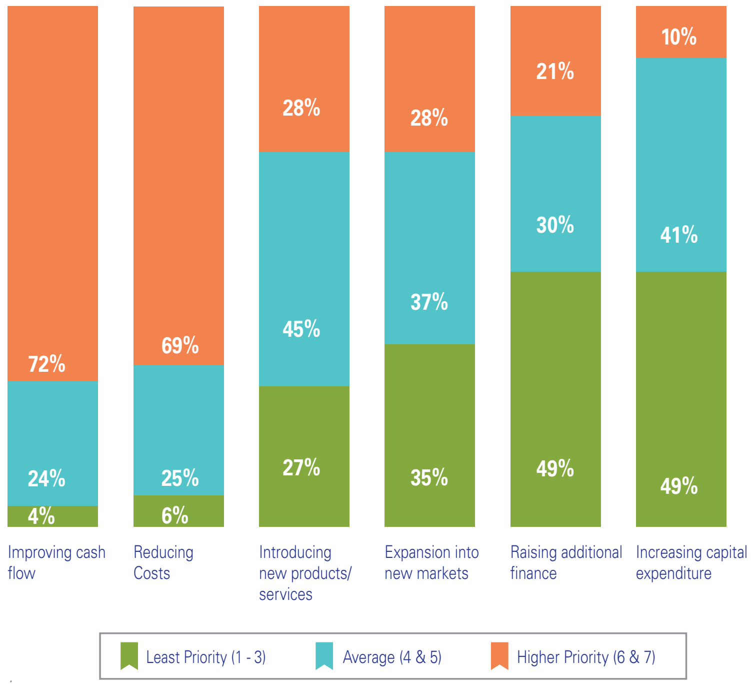
In tough economic times, most companies instinctively seek ways to cut cost. However, not all cost cutting measures are successful, and some even end up hurting the business. Companies need to develop sustainable approaches to cost optimisation. Techniques for achieving this are further discussed on page 21.

KPMG INSIGHT

Cash is king in the financial management of a Company. Cash flow monitoring is critical and complex yet vital for organisations to exist in the market. It revolves around the organisation's ability to monitor its cash flows and subsequently maintain sufficient funds to meet its obligations, financial commitments and new projects financing. Improved cash flow monitoring practices equals reduced risks, superior profit margins, increased visibility, enhanced forecasting capabilities, and greater potential for more efficient assets and liability management practices.

Q5

How would you rank each of the following factors as priorities for your organisation in the year ahead? (Rank from 1– 7, where 1 is Lowest and 7 is Highest)



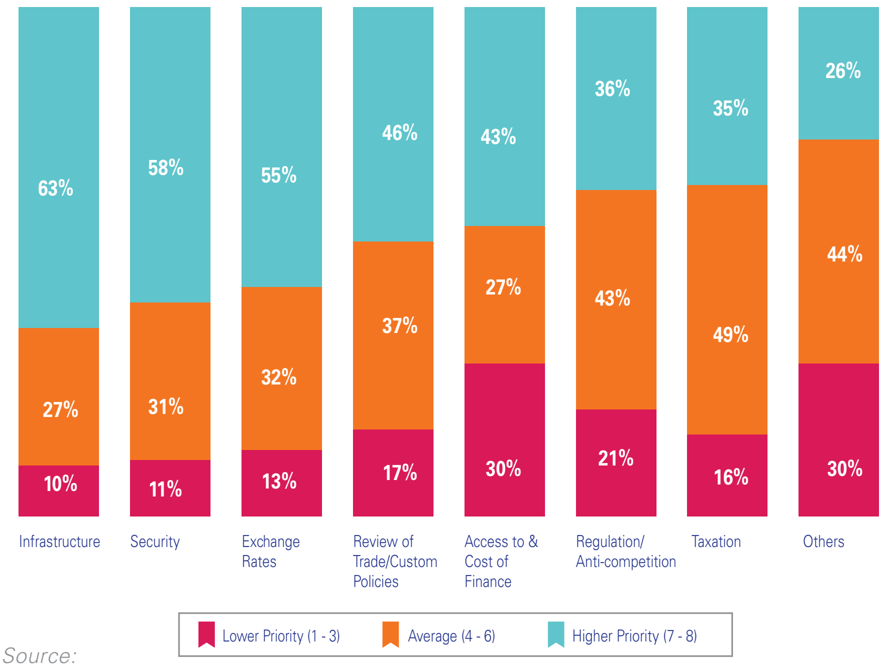
Source: KPMG Analysis

Seven out of ten CFOs surveyed agree that reducing cost and improving cash flows are the highest priorities for their organisations in the year ahead. It is not surprising that improving cash flow is a high priority for CFOs further to their recognition that financing costs will more likely than not deteriorate over the next 12 months. Improving cash flow positions will positively impact an organisation's ability to meet its obligations and directly reduce financing costs.

A CFO's ability to proactively address these areas will impact the quality of results and performance of their companies in the year ahead.

Q6

Which of the following would you rate as the highest priority area in which you would like to see improved government support for your organisation? (Rank all under listed factors from 1 – 8, where 1 is Lowest and 8 is Highest))



Source: KPMG Analysis

CFOs raised concerns on the prevalence of certain external factors capable of impacting the degree of success attained by their organisations. They identified infrastructure, security and exchange rates as the highest priority areas in which they would like to see improved government support for their organisations.

KPMG INSIGHT

The role of government in a mixed economy may be grouped into two categories, namely, regulatory roles and promotional or development roles. The regulatory role of the government involves formulating and implementing various direct and indirect measures to monitor and regulate the economic activities of the private sector.

On the other hand, the promotional /development role involves policies and measures taken for the progress of the economy. Government needs to improve their support for business. Tackling the current problems in infrastructure, security, exchange rates and regulation will go a long way in stimulating the business environment. On their part, businesses cannot afford to wait on government. They must be nimble and constantly evolve strategies to enable them navigate the realities of the business environment.

Foreign Exchange Risk

as a competitive advantage

Foreign exchange (FX) volatility exposes banks and corporations which typically have investments, assets, funding, and revenues denominated in multiple currencies to significant foreign exchange risk. If unmanaged, this risk frequently leads to earnings volatility and cash flow uncertainty. The process of successfully managing foreign exchange risks are typically capital-intensive and technology-driven and require inputs from risk management, capital markets, technology, and trading professionals.

The volatility of the exchange rate causes disruptions in the planned activities of organisations e.g. budget or spend. In managing this risk, organisations are encouraged to do the following:

- Identify and quantify existing price risks using a variety of leading practice metrics
- Model potential impact from exchange rate volatility on earnings and revenue
- Identify potential hedging instruments and methods to effectively mitigate price volatility (e.g., options, swaps, forwards, futures, and non-derivative financials)
- Analyze hedging instrument feasibility considering expected hedging costs, benefits, and aggregate corporate exposures
- Establish potential risk control mechanisms for hedging activities using comprehensive approaches established by industry accepted practices
- Establish enhanced management risk reporting tools using earnings-at-risk, cash-flow-at-risk, value-at-risk (VaR), expected shortfall stressed value-at-risk (sVaR) and other management information metrics
- Coordinate FX risk management design, drawing on extensive experience in developing comprehensive FX risk management frameworks, including infrastructure, hedging strategy, related processes, and risk oversight design

Execution of the aforementioned activities would provide companies potential benefits in the following areas:

- Reduced earnings volatility
- Improved cash flow forecasting
- Maintained or improved corporate credit ratings
- Defined risk management and hedge methodologies (regulatory and internal risk management compliance)
- Improved currency exposure forecasting and measurement capabilities

For more information, please get in touch with any of the contacts listed on the back page of this report.

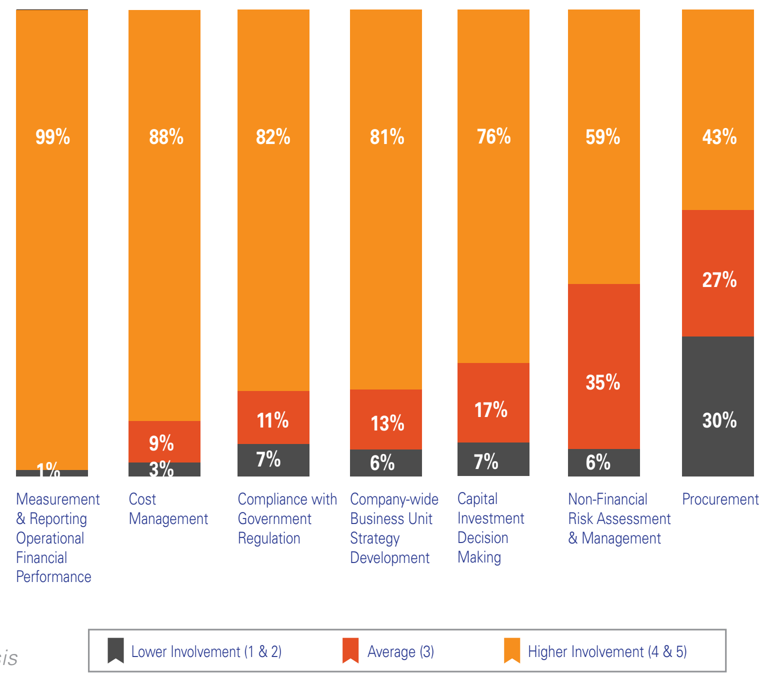
2 Attaining the Ideal Finance Function

KPMG INSIGHT

Increasingly, CFOs will have to deliver on a wide range of fronts: driving a more competitive finance function, establishing ever more robust risk management strategies and supporting their businesses to develop effective strategies for growth while remaining cost competitive. More than ever before, finance leaders and the businesses they represent will operate in a global economy that is significantly more volatile, presenting CFOs with new challenges, but also new opportunities. With opportunity comes challenges, and vice-versa. The CFO team of today is expected to add value well beyond the traditional roles of cost management, controls and acting as the conscience of the organisation. These roles are challenging enough, but today's CFO is expected to work in collaboration, by serving as the integration hub for key business processes, as a catalyst for change including business transformation, and as a consultant or trusted business advisor in helping to create sustainable growth.

Numerous business leaders and finance executives have long recognized the need for CFOs to step out of a 'numbers-focused' role and into a true partnership with the business—by participating in strategic planning, providing essential input on funding, managing growth plans and helping to maximize shareholder returns.

Q7 To what extent are you involved in the following activities? (1 - Low and 5 - High)

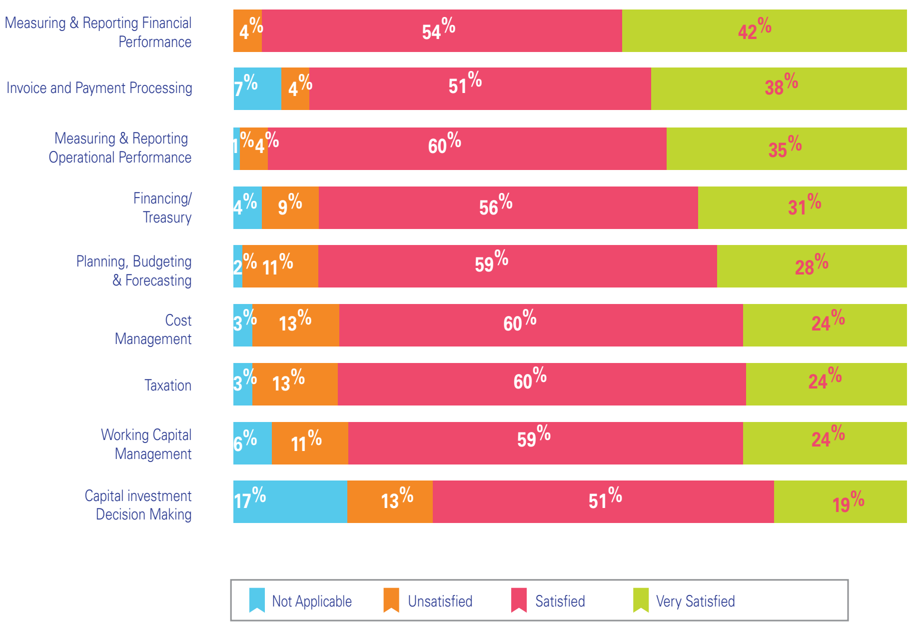


Source: KPMG Analysis

Our survey reveals that CFOs have taken up this challenge. While 99% of respondents indicate that CFOs continue to be involved in the traditional role of measuring and reporting operational financial performance, it also indicates that CFOs are involved in areas that provide an opportunity to contribute to decisions that more directly impact their organisations' performance. Eight out of ten CFOs surveyed say that they are actively involved in non-traditional CFO activities such as driving compliance with government regulation and development of corporate and business unit strategies, while six in ten are involved in non-financial risk assessment and management.

Q8

How satisfied are you with the skills of your Finance Team in the following areas?



Source:
KPMG Analysis

The high expectations of the business from finance increasingly require more diverse skills and capabilities in the Finance Team. CFOs now more than ever, have to ensure their Finance Team can deliver on these expectations by taking ownership of their talent agenda. With these increasing responsibilities, internal and external demands, finance executives will find that recruiting, managing and retaining talent is one of their most important objectives and one of the most difficult to achieve. 13% of our respondents say they are unsatisfied with skills of their Finance Teams in capital investment decision making, cost management and taxation.

CFOs need to continuously consider the implications of business changes on their staff and ensure that qualified resources are in place to meet current and future business needs. Above all, they need to create a talent management strategy that attracts appropriately skilled finance employees and supports their aspirations at all levels throughout their careers.

KPMG INSIGHT

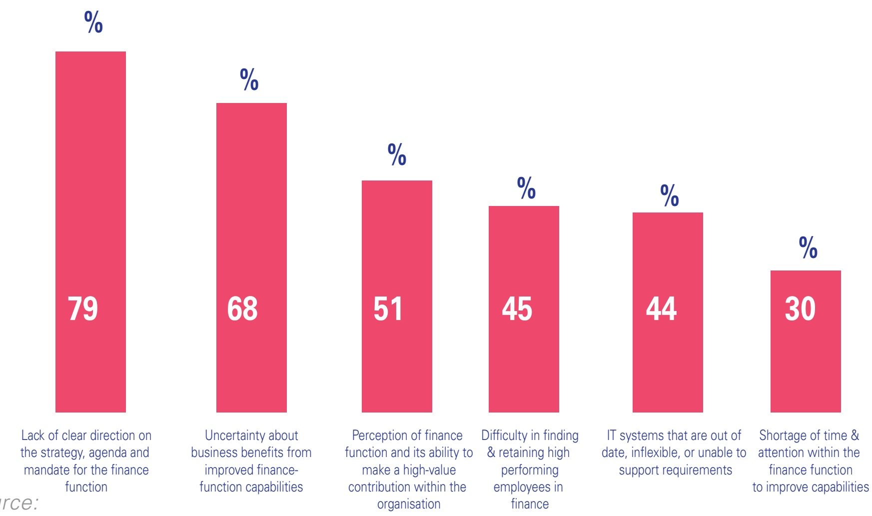
As the leaders of today's finance functions continue to work hard to boost their relevance and value added to the business, they are shifting their focus outward to those financial management activities that contribute the most to better business decisions that improve the bottom line. While talent management is difficult to master, CFOs consider it as the most important factor to the value-adding success and sustainable competitiveness of the finance function. Effective talent management requires that your business goals and strategies drive the quality and quantity of the talent you need. Numerous studies show that companies with better financial performance are more likely to use competencies as the basis for succession management, external hiring, and inside promotions. Organisations need to quickly determine their next steps in ensuring that talent management works for them and not against them.

KPMG INSIGHT

CFOs have made great progress in expanding the role of Finance but there is still a tough job ahead. CFOs need to continue to work hard to persuade leaders in the business that the finance function has even more valuable contributions to make to operational decision making. They need to continue to build credibility and trust by excelling at core competencies as several business partnership efforts have been derailed by errors in management reports or control issues in Finance. With greater credibility comes greater permission from the business.

Q9

What are the greatest barriers to improving the effectiveness of your finance function?



Source: KPMG Analysis

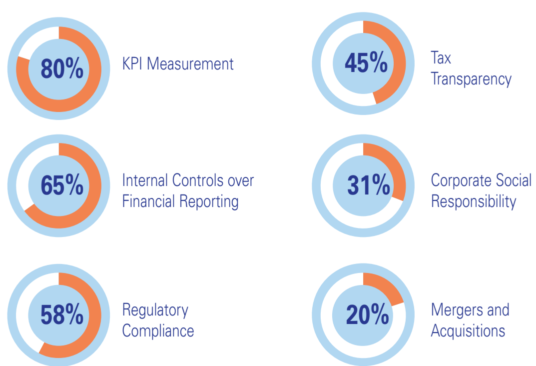
Despite progress attained, CFOs are still faced with various challenges that present barriers to improving their effectiveness and place them at risk of failing to achieve their objectives. Lack of clear direction on the strategy, agenda and mandate of the Finance Function was cited by 79% of CFOs surveyed as one of the greatest barriers to improving the effectiveness of their finance functions. Uncertainty about the business benefits of improved finance function capabilities and the perception of the finance function and its ability to make high-value contributions within the organisation are other key barriers identified.

KPMG INSIGHT

In today's constantly changing world, business decisions have to be based on data, often from multiple sources. This data is both qualitative and quantitative and in many respects the quality of the decision is a function of the quality of the data underlying the decision. There is a general concern by decision makers that the data being used for decisions may either be inaccurate or irrelevant. In reacting to this, CFOs need to consider seeking independent assurance over the accuracy and the relevance of the data underlying key decisions. More information on independent assurance is discussed on the next page.

Q10

In which of the following areas do you believe your organisation will benefit from additional assurance that the agreed objectives are being met? Select all that apply



Source: KPMG Analysis

As the role of the finance function expands, CFOs are seeking additional assurance that objectives are being achieved. The areas of highest concern are KPI Measurement, Internal Controls over Financial Reporting and Regulatory Compliance.

Increased Assurance - the way to go!

In achieving the Company's strategic goals, a multiple and dynamic set of risks need to be managed, some of which include the following:

- How can we ensure that contracts are fulfilled and regulatory requirements are adhered to?
- Does the internal control system function?
- Do we have the required transparency on IT, data security and data protection?
- Are there any insecurities regarding specific accounting and tax matters?
- Are we applying the right methods for our budget and financial planning?
- Are we measuring our KPIs correctly and can we rely on the reported results?

Growing complexity in business and data volumes creates increased uncertainty for businesses. An independent review of risks, systems, and data can increase the reliability of management information allowing for more informed decisions. Decisions with far-reaching consequences require reliable basic data. Published data must be accurate, systems and processes must function at all times, and risks must be assessed adequately. All these things require independent appraisals and confirmations provided by experts.

Stakeholders generally look to the CFOs to provide assurance on the credibility of data used for decision making. Sometimes it is difficult to maintain the necessary distance if one is fully immersed in the daily business. As a result of this, it may not be possible for CFOs to provide the much needed assurance under these circumstances. Obtaining external assurance is the way to go. In cases where some level of assurance is provided by the CFOs, board of directors, management, or an internal committee may require a second opinion. Assurance over these elements helps to identify the right action to be taken and provides independent feedback on their status.

Seeking external assurance will provide you with the following:

- Independent view
- Reliability
- Technical and sector expertise
- Proven methodology
- Ability to engage the right team
- Identification of needs
- Credentials
- Multi-disciplinary resources

KPMG can provide the independent confirmation required by stakeholders in the following areas:

Accounting & Tax – Assurance over specific transactions, accounting solutions and tax implications.

Systems and process assurance over your operating effectiveness – Assurance over the efficiency of the Internal Control System.

KPI Measurement – Assurance over KPI results and accuracy of reported results.

Data – Assurance over Information Technology and related processes.

Regulation and contracts - Assurance over compliance with regulators, terms and conditions.

Future and performance – Assurance over budgeting, forecasting and reporting processes.

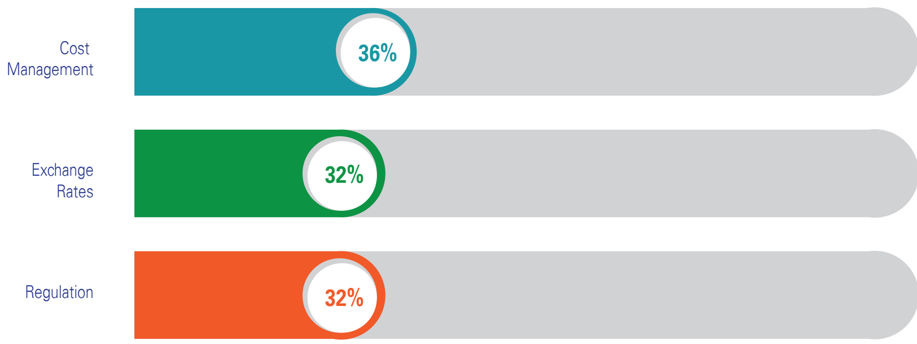
Others - Assurance over specified procedures as requested by stakeholders.

For more information, please get in touch with any of the contacts listed on the back page of the report.

KPMG INSIGHT

Concerns about cost management, exchange rates and regulations cut across all industry sectors. While these are not necessarily new concerns, they have assumed heightened importance and urgency based on current economic realities. Navigating these complexities will require innovative and radical solutions based on the peculiarities of each business. The best solutions will likely arise from a combination of internal and external ideas and resources.

Q11 As the CFO of your organisation, what are your top three 'stay-awake' (most important) issues?



Source: KPMG Analysis

To better define the top of the mind issues of the Nigerian CFO, we asked our respondents to highlight their top three "stay awake" issues. Consistent with the rest of the Survey, cost management, exchange rates, and regulation are the three top of the mind issues for CFOs in 2015.

For the CFO, ensuring the organisation stays abreast and sometimes ahead of regulation present a significant challenge. With increasing pressure from regulators on general industry compliance and financial reporting standards, it is no surprise that regulation is a top of the mind issue for the Nigerian CFO.

The government establishes many rules and regulations that guide businesses. Businesses would normally change the way they operate when government changes these rules and regulations. Government economic policy and market regulation have an influence on the competitiveness and profitability of businesses.

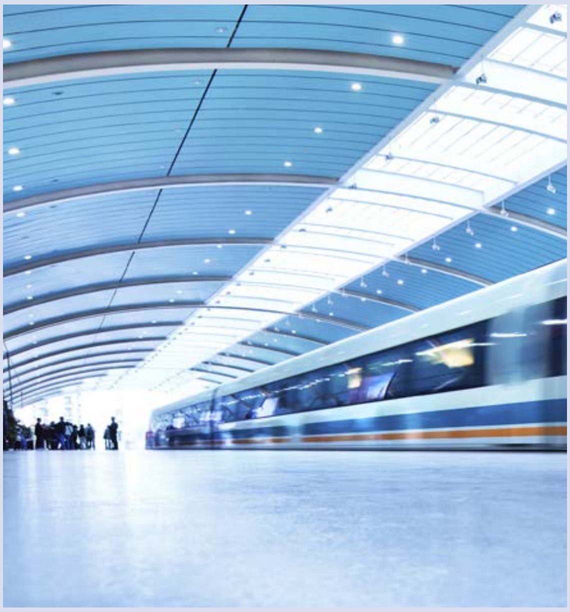
Tax Risk Management

As a result of changing regulatory and fiscal landscape, "getting tax right" is significantly important for all companies operating in Nigeria. Global regulations and wider awareness of corporate governance issues have also made it an imperative for companies to address all aspects of risks in their business. Organizations need to understand and manage tax risks, just as all other aspects of their enterprise and business risks; they also need to manage the rising demand for greater transparency in tax compliance processes and enable disclosures that allow a see-through to their tax operations.

CFOs and Tax directors around the world are shouldering the impact of fundamental changes in attitudes and approaches to tax. For many, the days are gone when tax was solely an expense to be managed. Whether it is corporate social responsibility, tax governance, enhanced transparency with tax authorities, investors, or society holding individuals and businesses accountable for paying a fair amount of tax, these issues are subject to increasingly heated debates.

On the home front, the Nigerian tax environment has undergone significant transformation in recent years. Given the declining crude oil prices and fiscal revenues, the Nigerian government is more focused than ever before, on tax collection and increasing internally generated tax revenues. These difficult economic times are placing compounding pressures on tax departments as they juggle a myriad of responsibilities to meet compliance requirements of more aggressive tax authorities. At the same time, they are still struggling to become more efficient and value-adding to their organizations. Therefore, companies may need to adopt a forward-looking approach to managing their taxes. In our view, adopting a risk-based approach to tax compliance management is necessary to set them on the right path.

To provide clarity, tax risk is generally seen as the risk that something may go wrong, so that the tax consequences of a transaction or business may not be those expected. CFOs and Tax Directors are particularly concerned about unexpected tax costs emerging



from transactions they engage in or general leakages in their tax processes. Unfortunately, many companies are yet to have well-articulated strategies on how taxes should be managed in their organizations. Most companies are still operating at the level of back-ward review of transactions with the aim of determining the associated tax liability. It is, therefore, no surprise that many CFOs are yet to have the necessary assurance of getting their tax numbers right and having a tax department that is fit for purpose!

A forward-looking approach would be to review the efficiency of tax processes and the effectiveness of controls in place to manage tax risks. Doing so will enable companies to proactively manage their tax using good corporate governance principles, to minimize errors, reduce tax risks and plug any tax leakages. This would ultimately enhance tax cost optimization, improve business performance, and create shareholder value. As the public looks to businesses to 'do the right thing', expectations for more transparency are increasing. We expect the trends will continue towards greater demands for transparency in tax compliance and tax risk management.

KPMG Nigeria conducted a survey on the attitude of Nigerian companies towards tax risk management. The survey provides valuable insights on changes that organizations need to make to attain the ideal tax operational environment, which will be more value-adding to businesses and achieve the tax cost optimization agenda.

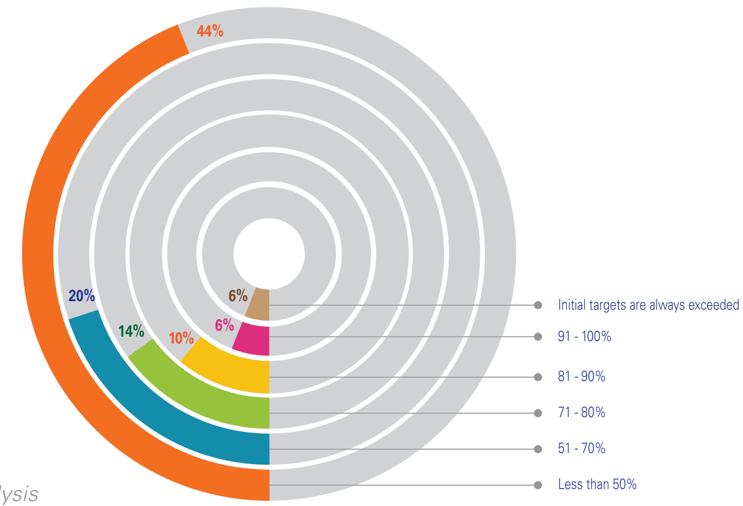
For more information, please get in touch with any of the contacts listed on the back page of this report.

3

Creating a Sustainable Cost Advantage

Cost structures are not immediately associated with revolutionary change, but the reality is that many recent business innovations including outsourcing, category management, process standardization, low-cost market procurement and some internet sales models, to name a few, resulted out of cost concerns. In a highly competitive, globalized business environment under pressure from current economic realities, the competitive advantage which can arise from reducing costs will continue to fuel innovation throughout the enterprise. This segment of the 2015 Survey sets out to understand the challenges business are facing with implementing various cost management strategies.

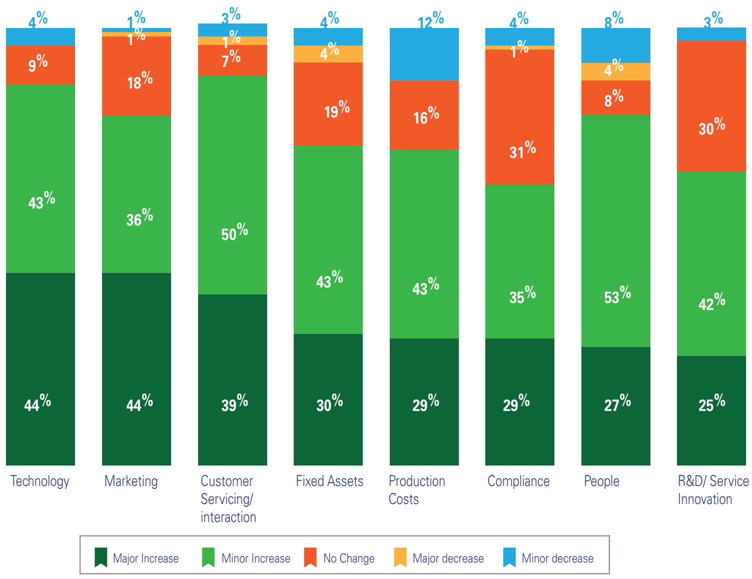
Q12 When your organisation decides to implement cost saving initiatives, on average, what proportion of planned savings is typically achieved?



Source: KPMG Analysis

Five out of ten CFOs surveyed say their organisation achieves less than 50% of planned savings from cost reduction programs and just 6% of businesses exceed their targets. The biggest barriers to achieving these targets are lack of transparency on costs, difficulty in measuring cost savings and negative publicity associated with cost saving programs.

Q13 How will costs change in the following areas of your business over the next three years?



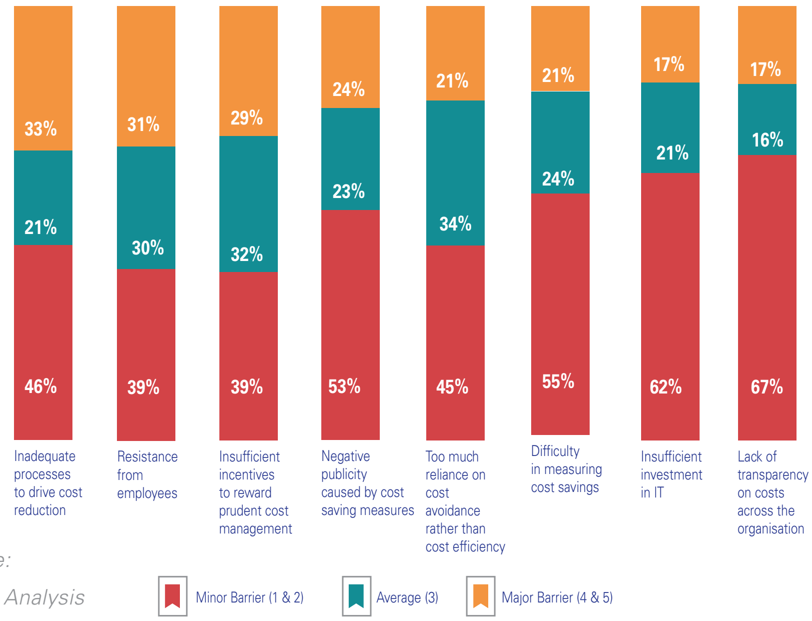
Source: KPMG Analysis

44% of the respondents believe that there will be major increases in technology and marketing. While 39% believe that customer service/ interaction would be key over the next three years. This reflects a focus on spending on areas which will improve revenues and promote greater efficiency.

KPMG INSIGHT

The companies setting the pace in cost leadership have gained an understanding of how their overall business model impacts their expenditure and by making changes at a strategic level, have managed to build a permanent, sustainable lower cost base. Management should however be aware that building a cost-aware environment is certainly not 'business as usual' and requires an extraordinary level of focus across the organization to avoid failure at the implementation stage.

Q14 What are the biggest barriers to implementing cost savings in your organisation? (Rate from 1 – 5, where 1 is Minor Barrier and 5 is Major Barrier)



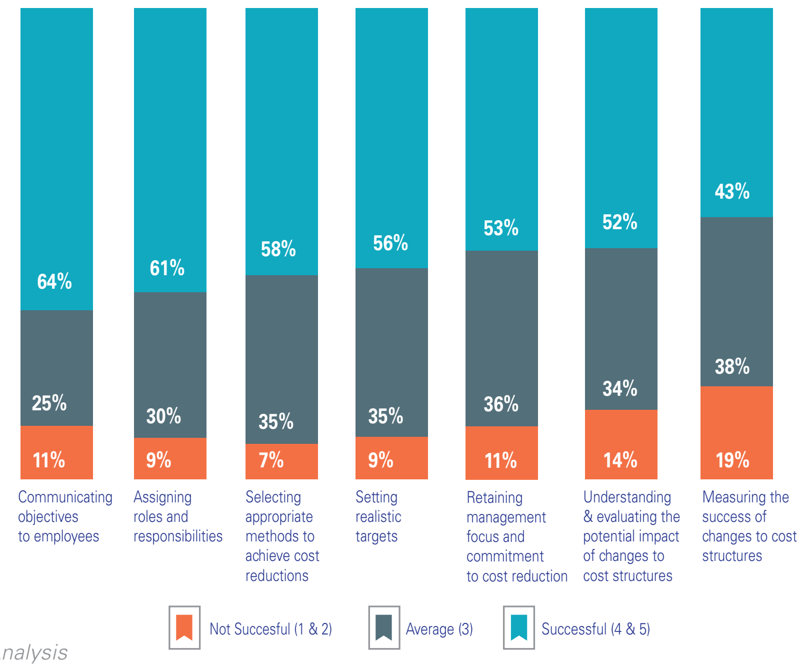
Source: KPMG Analysis

33% of our respondents say inadequate processes to drive cost reduction remain the biggest barrier to implementing cost savings in their organisation. Furthermore, 31% identified resistance from employees a major barrier.

KPMG INSIGHT

Once a company has declared its intention to become a lower cost business, those charged with making it happen need the data and reports to track progress and make individuals more directly accountable. Linking incentive programs to savings is vital to maintaining momentum. An increasingly popular way of encouraging people to meet their targets is to visibly use cost savings to fund actual business initiatives.

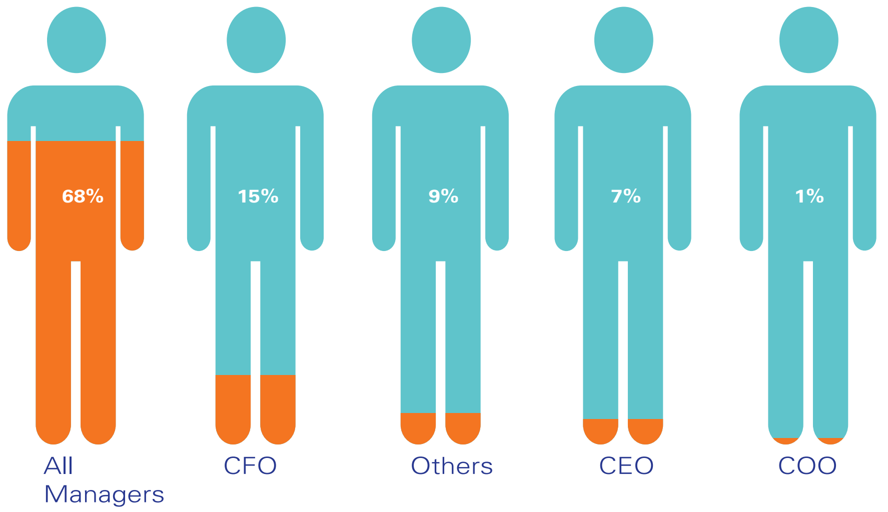
Q15 How successfully do you think your organisation performs the following aspects of cost reduction programs? (Rate from 1 – 5, where 1 is Not At All Successful and 5 is Very Successful)



Source: KPMG Analysis

19% of our respondents say that measuring the success of change to cost structures appears to be the biggest challenge to cost reduction programs.

Q16 Who in your organisation is responsible for cost management?

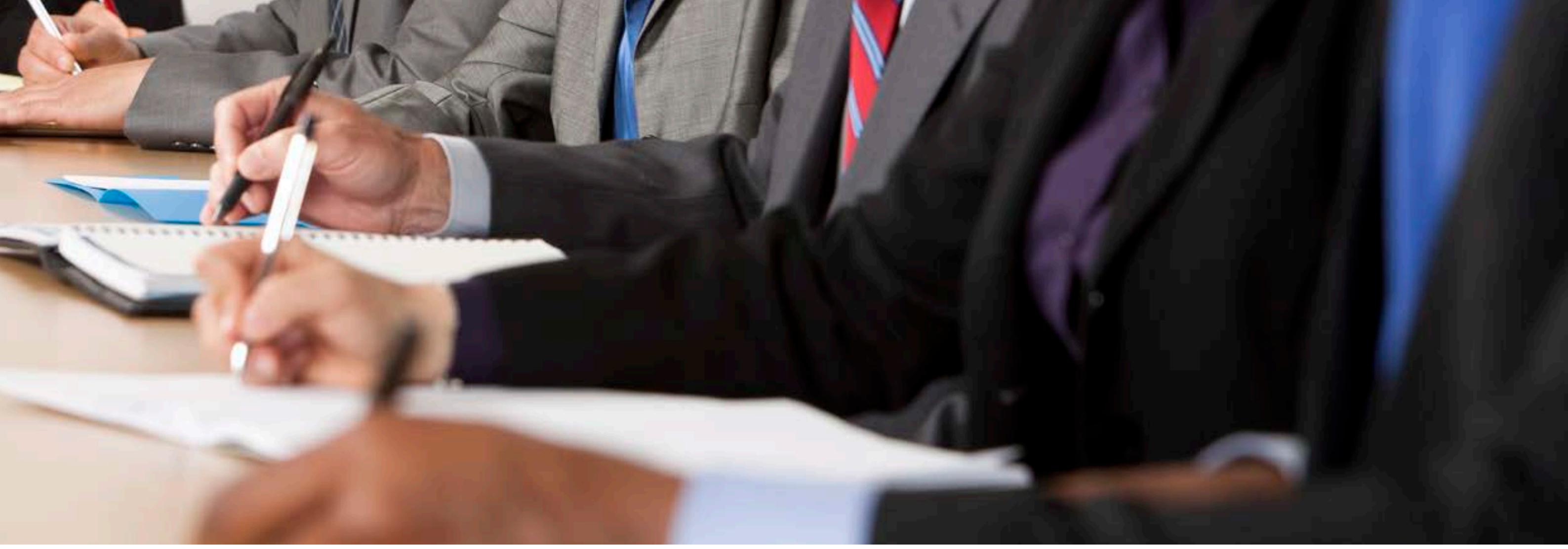


Source: KPMG Analysis

Ownership of Cost Management Initiatives is unclear

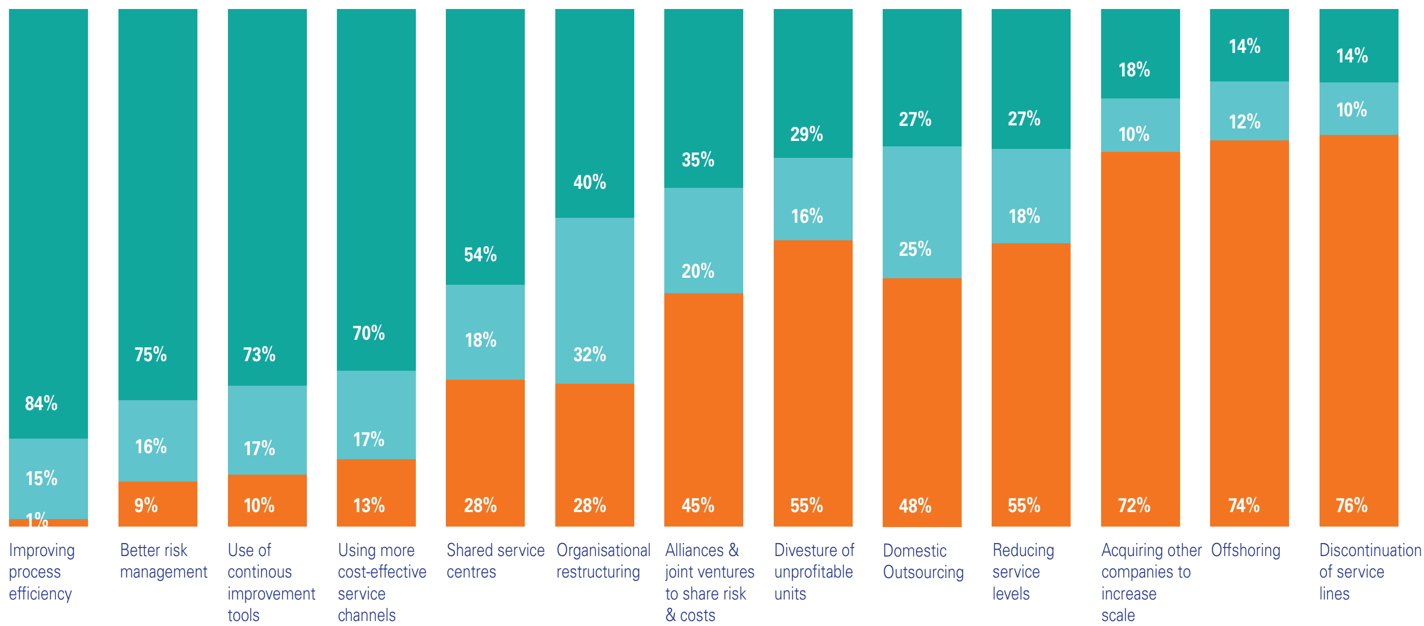
While it is true that everybody is involved in cost management, it is important that there is clarity in terms of who has overall responsibility for cost management programs. Cost initiatives at businesses where there is no clarity on ownership of cost management initiatives will almost certainly fail. While CEOs and CFOs should not micro-manage cost initiatives, their leadership is vital in a number of areas – ensuring the business model supports a competitive cost structure, setting the broad strategy, articulating a clear vision and driving the message down, providing unambiguous commitment and leading by example.

If accountability for cost management is sometimes lacking at C- level, it is even more pervasive elsewhere as 68% of respondents say that all managers are responsible for cost management initiatives. Lack of clear accountability at these lower rungs affects a business' ability to remain competitive. Getting people with the "right mentality who fight for the savings" in the trenches is an essential and an integral part of cost control. Only the people on the ground can say how specifically to make centrally dictated goals happen so as to help rather than hurt operations.



Q17

How important will the following strategies be as part of your cost management program over the next three years? (Rate from 1 – 5, where 1 is Not at all important and 5 is Very Important)



Source:
KPMG Analysis

Low Importance (1 & 2) Average (3) High Importance (4 & 5)

KPMG INSIGHT

Companies can too often pick the easy option for cost initiatives, rather than the one which will yield the most savings. The problem, as the survey indicates, is that many companies are using these tools very timidly, or sometimes not at all. When asked which strategies would be the most important to cost management over the next three years, respondents placed the greatest emphasis on those which potentially require the least disruption. Disruption is more likely going to produce future cost leaders in most industries in the coming years.

Improving process efficiency was recognized as the most important strategy for cost management programs by CFOs, followed closely by better risk management and use of continuous improvement tools. Furthermore, seven out of ten respondents recognised the use of more cost effective service channels as high priority for their business. Notable however is the selection of options of least disruption to existing operating models. However, to realize fundamental and sustainable cost improvements, it is imperative that businesses will have to look hard and embrace some of the more disruptive options around their business and operating model.

Sustainable Cost Optimisation

Cost reduction by definition goes one way – to reduce costs. Cost optimisation is a two-way street – focused on both reducing costs and enhancing the realisation of value within the business. A short-sighted but common approach to cost reduction is to attack in isolation a single part of the business through a single, finite project. Unfortunately, such efforts rarely achieve the desired goals; either they run out of steam or else the costs simply pop up in another part of the organisation. Even for those that succeed, the benefits tend to be short lived, with the same problems cropping up again in the near future.

A study conducted by KPMG and the Economist Intelligence Unit revealed that many businesses find it hard to sustainably reduce their costs, with nine out of ten cost reduction programmes failing to achieve their targets. When faced with margin pressures, businesses often implement rapid and broad cost-cutting measures. These may deliver short-term benefits but not get to the heart of the cost drivers. While companies need to act decisively, the imperative is to balance short-term concerns (e.g. shoring up cash and working capital) against longer term strategic objectives. The focus should be making a leaner, more nimble organisation, with cost reduction as a consequence, not necessarily just the target.

A structured approach to cost optimisation therefore means thinking beyond short-term cost savings to assess and question the underlying business models. By focusing on some of the key dimensions of the business, CFOs and business leaders can identify the core cost drivers and value levers and take steps to sustainably manage costs while driving up value delivery within the organisation. Rather than a quick-fix diet, the clear imperative is a sustainable lifestyle change.

The Imperative

Cost optimisation is not a walk in the park. However, a structured and well-executed approach to cost optimisation can:

- Improve margins, cash flow positions, balance sheet and performance
- Generate efficiencies around production, inventory and supply processes
- Create flexible and agile operating and business processes
- Streamline traditional financial and regulatory processes to reduce costs and free up resources
- Embed a culture of cost consciousness throughout the business
- Turn cost efficiency into a real competitive advantage

Organisations that do not take firm and sustainable cost optimisation measures will likely soon find themselves dealing with ever tightening profit margins and a stagnant bottom line.

Execution is Key

The effective execution of cost optimisation initiatives is as important as the development of the initiatives that will underpin the intended cost reduction and value enhancement. Companies have to put in as much, or even more effort in taking strategic steps to ensure that the cost improvements are not merely one-off benefits, but a culture of thinking cost-conscious is instilled in the workforce.

While changes may be painful to implement, organisations that get this right will enjoy sustainable and efficient cost management that will almost certainly deliver a significant competitive advantage. The following are recommendations for driving sustainable cost-efficiency.

Maintain cost management as a strategic priority

- Do not allow cost efficiency to drop down the priority list of executive management. Cost management will need to be aligned with the organization's other strategic priorities.

Adopt an external investor mindset

- An outside-in view can be value-adding. Challenge the organisation in the same way a potential investor would, unconstrained by current organisational boundaries and perceptions

Create profit and cost transparency

- The business should have a clear view of where costs lie within the business and how this evolves over time as the needs and strategic directions change.

Engage front line workers

- Seek to instil a greater sense of ownership within your front-line staff and line managers. Focus on creating a high level of cost-consciousness that encourages employees to contribute towards active cost management.

Equip staff to 'walk the walk'

- The business should look to develop a deep sense of ownership of cost optimisation initiatives by investing in the tools and training to enable employees to fully participate in creating cost efficiencies.

The CFO as Champion

Significant responsibility for driving cost management initiatives rest with CFOs. Few would dispute that the support of CFOs is necessary for cost-management efforts to succeed. The role of the CFO in cost optimisation include the following:

- Demonstrate to the business that finance has gone through – or is undergoing – the same cost reduction pain
- Help mediate the inherently political nature of such exercises and provide critical energy and motivation
- Ensure value creation and guide the organisation on the appropriate balance between cost and value
- Ensure that the finance team are aware and engaged in cost reduction initiatives and are supporting in driving these changes across the organisation
- Be aware of customer value and not destroying that value by over-cutting costs
- Have a clear view of the baselines and cost drivers

Benefits of sustainable cost optimisation

A structured approach to cost optimisation can;

- Embed a culture of cost management throughout the business
- Improve cash flow positions, balance sheet and performance
- Generate efficiencies around production, inventory and supply processes
- Create flexible and agile operating and business processes
- Streamline traditional financial and regulatory processes to reduce costs and free up resources

The challenging operating environment today provides a massive opportunity for organisations to significantly raise the cost efficiency bar by examining more strategic options for cost management, fundamentally changing their business and organisational models, and instilling a cost-conscious culture throughout their workforce. Successfully delivered cost optimisation efforts will produce a positive ROI that sets the business up for future growth as the engine of the economy roars back to life.

For more information, please get in touch with any of the contacts listed on the back page of this report.

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