

Rethinking the Corporate Center

How to turn your corporate headquarters from a cost factor into true support for your business



Despite their success in improving operational efficiency, many financial services companies struggle when it comes to optimizing support and back-office functions. Simply cutting cost and setting crude targets for these functions results in little more than frustration for everyone involved. Arthur D. Little proposes a different approach; one that looks not just at the cost of each function but also at the value of the services it delivers. Our approach offers a far more precise assessment of what needs to be kept, what needs to be done differently and what needs to be discontinued.

The result? Corporate headquarters many companies have never dared to imagine: business-focused, flexible, lean where possible, strong where necessary – a true support for the business.

The financial services industry has had its fair share of programs to reduce costs and improve operations. Typically, the areas most closely linked to operations have fallen under the spotlight first and, as a result, branch networks and distribution channels, credit or claims management, and even underwriting are generally in better shape today than they have ever been.

The back office, however, is a different matter. Few support functions have escaped the impact of cost-reduction programs yet there is very little evidence of any imagination having been applied to the challenge of improving the back office's effectiveness. As a result, financial services companies are still far from best in class when it comes to headquarter size and cost.

A snapshot of performance

Analysis by Arthur D. Little of the headquarter functions of several leading banks and insurance companies (Figure 1) reveals that the efficiency of support functions varies widely. The results of the survey suggest that financial services organizations have had very mixed success in optimizing the back office. For example, in extreme cases, such as IT and Accounting, the "worst" data point is one hundred times greater than the "best." At the other end of the spectrum, some banks and insurance companies are close to the benchmark set by very lean manufacturing companies.

Of course, any direct comparison between the support functions of a manufacturer and those of a financial services company

needs to be treated with caution. Financial service companies tend to have more office locations around the world and, although small in headcount, each is likely to require a degree of human resources, IT and accounting support. This complexity is difficult to accommodate, even when the organization makes full use of centralization, outsourcing and self-service applications. In addition, the intangible products sold by financial services companies require more complex IT support than a manufacturer's physical products. As a result, it may not be appropriate for financial services companies to strive to achieve the benchmark set by manufacturers – but it may give a hint.

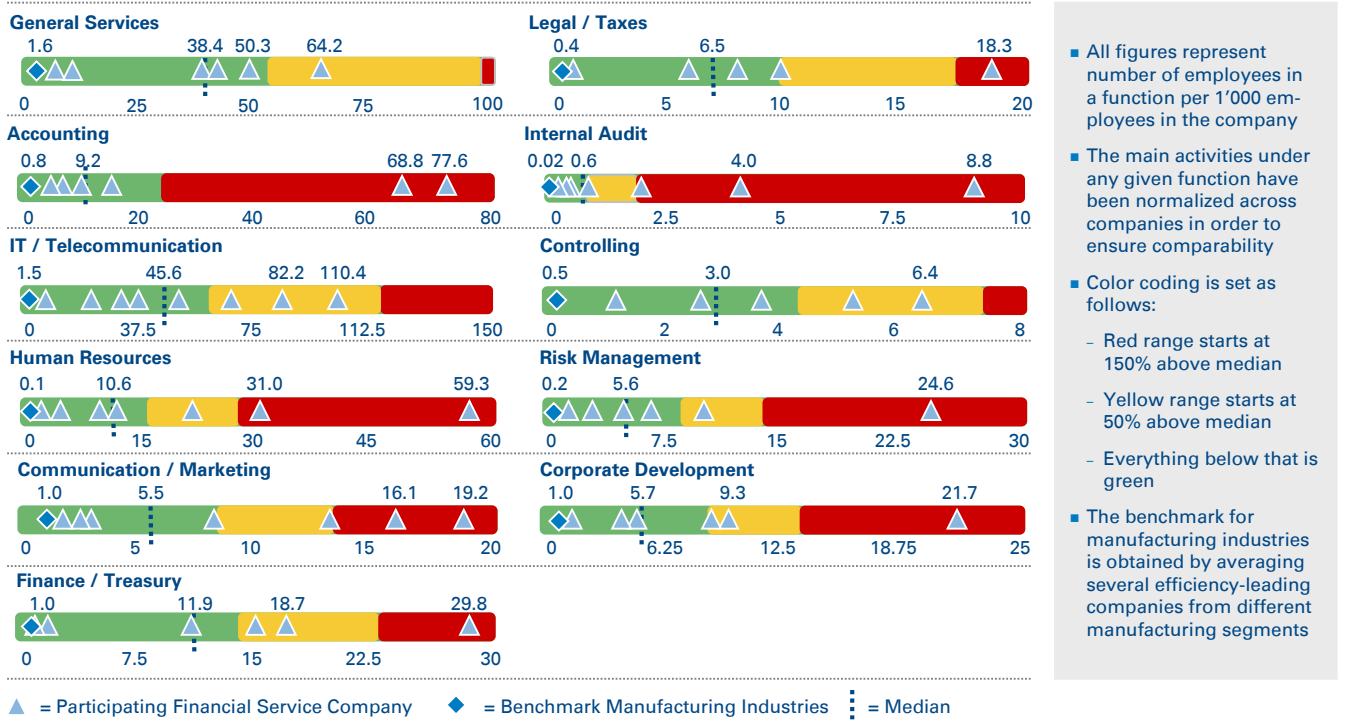
Making a direct comparison between different financial services companies requires similar care. Close analysis will always reveal significant differences even between seemingly similar organizations. These differences will either invalidate the benchmark or at least undermine confidence in the data.

It is for these reasons that benchmarking should be used selectively. It can be useful in highlighting areas of the back office that require closer attention, but should not be used as the sole means of establishing targets for efficiency programs. Arthur D. Little proposes a different approach.

Redesign with value in mind

Treating support functions purely as cost centers and aiming to reduce costs incrementally each year can raise as many problems as it aims to solve. Taken to the extreme, the

Figure 1: Benchmarking of central functions in financial services companies



approach will result in a support function reduced to the bare essentials. But what is essential and who decides? How far would an organization be prepared to deviate from “essential” to “nice to have” if “nice to have” improves morale and increases productivity? How essential is a cafeteria? A company newsletter? A company-owned conference center that employees can use for their vacation?

There is only one way to answer these questions: by assessing the value of each service and support activity in relation to the cost it creates. Such an approach looks at each support function – and the specific services it provides – on its own merit and leads to the only meaningful way of optimizing the headquarters: improving, redesigning, trimming or discontinuing individual services and activities according to the impact they have on the organization overall.

This value-based assessment forms the foundation of Arthur D. Little’s approach to headquarter redesign. Our approach also incorporates several unique features that set it apart from standard cost-saving programs and allow it to generate more useful and sustainable results.

A unique, two-pronged approach

Arthur D. Little’s Value-Driven Headquarter Redesign brings together two familiar methods of addressing corporate redesign – one analysis based, the other more fluid and creative – to create an approach that delivers the best of both worlds. We describe the two key aspects of our approach as EVO (evolutionary) and REVO (revolutionary).

EVO refers to the familiar approach of analyzing the current situation in detail, finding areas for improvement and developing recommendations for change. EVO is useful because the detailed analysis uncovers the hidden causes of the issues observed and improvement recommendations are based on those findings. But EVO also has shortcomings: analysis can become over-detailed without delivering any additional insight (“analysis paralysis”) and recommendations tend to be incremental. Because the ideas for improvement are based on such detailed analysis, they often lack creativity. Real leaps in improvement are hard to come by under a pure EVO approach.

REVO is the opposite of EVO: new ideas for the structure and service portfolio of an “ideal” headquarter are developed on a blank sheet of paper. Key questions and potential answers are brainstormed and organized in an “Option Space”, which allows different combinations of answers to be tested. The completely open format of this exercise allows for the development of solutions that nobody has considered before.

In addition to producing new structural ideas, REVO is useful for defining “ideal” principles for the headquarter, e.g. when it should have sole decision authority, when it should have a voice in a decision, when it consults, and when it simply receives orders.

The clear advantage of REVO is its ability to create a space for creativity and blue-sky thinking. The disadvantage is that the solutions it proposes may be too far-fetched, impractical or impossible to implement. However, merging EVO and REVO produces an approach that cancels out the weaknesses of each component and draws on the strengths of both.

Establishing a framework for analysis

Arthur D. Little's Value-Driven Headquarter Redesign uses "service trees" as a framework for analysis (Figure 2). These are hierarchical structures for each central division or unit that begin with the main elements of their respective service portfolios and then divide into the sub-activities that flow into them. This structure has several advantages:

- Clear service portfolios are established for all headquarter functions.
- Supply relationships/interfaces between headquarter departments become transparent.
- A service tree can be expanded into a resource matrix by allocating staff time, and even cost, to each service, resulting in a high degree of cost transparency even if the accounting system cannot deliver cost data at a service or activity level.
- The foundation is laid for a later discussion about which services are required by whom, what value they deliver, and who should be responsible for them.

Evaluating services from two perspectives

A key feature of Arthur D. Little's approach is the way in which the value of each service is determined. Both the internal customer and the service provider have the opportunity to rate each service activity according to agreed criteria. Combining these two different perspectives provides a clear indication of the points at which the recipient and the provider of a service have different ideas about what is important.

The process of evaluation follows these steps:

- Definition of the underlying benefit of each main service in the service tree. This definition needs to be agreed between the service provider and the recipient. It defines the value proposition of each service and provides critical input for the next step.

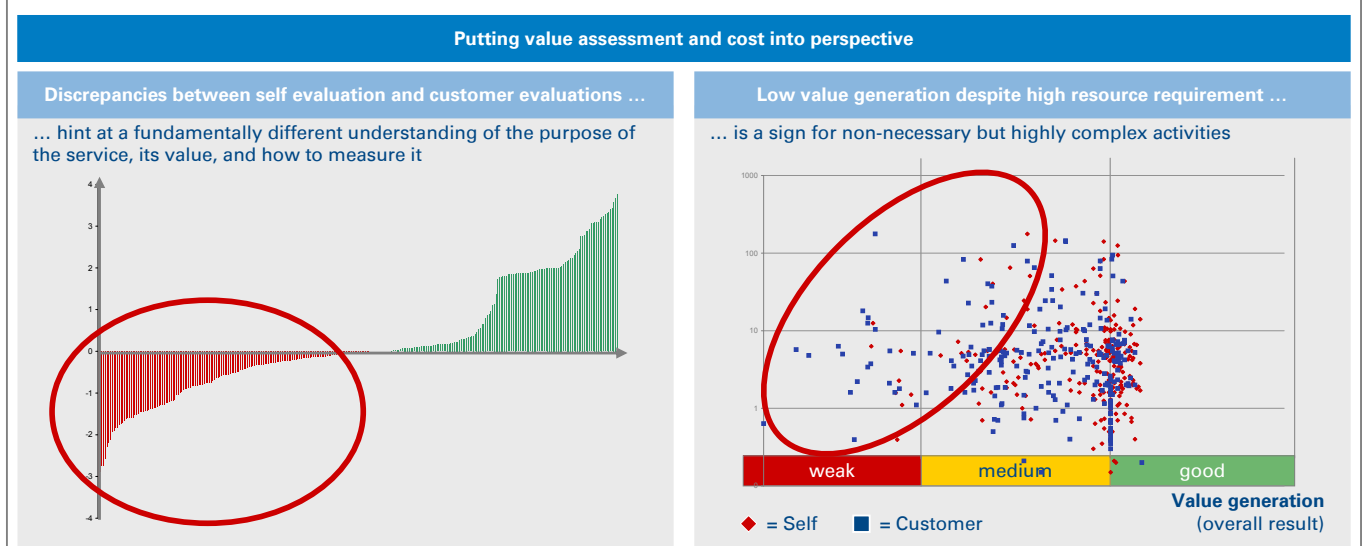
Figure 2: Illustrative partial service tree for Human Resources

Service structure	Resource requirement			Cost
	HR1.1	HR1.2	...	
Standard Services	Σ	Σ	Σ	Σ
Compensation and benefits	Σ	Σ	Σ	Σ
Job description	x.x	x.x	x.x	x.x
Job classification / valuation	x.x	x.x	x.x	x.x
Remuneration strategy and management	x.x	x.x	x.x	x.x
Benefits administration	x.x	x.x	x.x	x.x
...	x.x	x.x	x.x	x.x
Personnel services	Σ	Σ	Σ	Σ
Services / counseling for employees	x.x	x.x	x.x	x.x
Relocation management	x.x	x.x	x.x	x.x
...	x.x	x.x	x.x	x.x
Personnel administration	Σ	Σ	Σ	Σ
Time management	x.x	x.x	x.x	x.x
Payment processing	x.x	x.x	x.x	x.x
...	x.x	x.x	x.x	x.x

- Definition of objectively measurable indicators that help determine whether or not the service delivered lives up to its value proposition. For example, the number of complaints that the company's auditor has each year could be a useful indicator for measuring how well the accounting department does in delivering the annual report.
- Subjective assessment by the service provider, according to a fixed set of dimensions, of how well a service is delivered.
- Subjective assessment by the service recipient, according to the same dimensions. If the recipient rates speed as important but hardly satisfactory while the service provider rates precision as important and great, there is clearly a need for further discussion.

The resulting overall value rating for each service is then plotted against cost (Figure 3). This provides an indication of where major adjustments to the service portfolio or to the cost of

Figure 3: Identification of critical services



delivery are required. This can mean process redesign, the discontinuation of certain services (along with its resource requirements), but possibly also the strengthening of certain critical activities.

The benefit of involvement

An important benefit of Arthur D. Little's approach is that it requires involvement – in the definition of the service trees, in the REVO workshops, in the value assessments, in the discussion of the findings, in intermediate decisions. Our consultants do not design the headquarter for our clients but design it with our clients and their employees. This not only makes for better results, but is also a tremendous asset at the implementation stage. Managers and employees who have been involved in shaping the new headquarter are far more likely to be supportive of change when it is implemented.

Conclusion

The financial services industry has made significant progress in recent years in improving operational efficiency, but much remains to be done with respect to the support functions and the corporate headquarter. Traditional cost-cutting models have a tendency to destroy activities that add value, they are demotivating and they hardly ever live up to their expectations. Arthur D. Little has developed a methodology for redesigning the support functions in a way that simultaneously reduces cost and increases value to the business.

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Arthur D. Little

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